What to focus on in Global Macro for the week of January 6th, 2020

Macro Themes on the Radar:

On Friday, the FOMC minutes for December's meeting were released. While you will have seen lots of headlines and market commentary on the subject, it can be helpful to go to the source. I have tried to pick out the highlights.

Rates

"The expected path of the federal funds rate implied by the medians of survey respondents' modal forecasts remained essentially flat through 2020. Survey- and market-implied uncertainty about the near-term outlook for monetary policy declined, with market commentary attributing the decrease in part to the Committee's October communications. Survey respondents placed a higher probability on a reduction in the target range over 2020 than an increase."

Repo and Reserves

"Reserve management purchases of Treasury bills continued at a pace of $60 billion per month, with propositions remaining strong and little discernible effect on market functioning. While these purchases accumulated, the Desk continued to conduct regular repurchase agreement (repo) operations in order to maintain reserves at or above the level that prevailed in early September. Repos outstanding from these Desk operations totaled roughly $215 billion per day, consisting of both overnight and term operations. The Desk had already conducted three longer-term repo operations spanning year-end—for a total of $75 billion—and planned to announce an additional longer-term operation, as well as increase the amount of overnight repo offered around the year-end date."

"The manager also discussed expectations to gradually transition away from active repo operations next year as Treasury bill purchases supply a larger base of reserves. The calendar of repo operations starting in mid-January could reflect a gradual reduction in active repo operations. The manager indicated that some repos might be needed at least through April, when tax payments will sharply reduce reserve levels."

(Note that the recent increase in the balance sheet has been achieved using three tools: short-term repo, longer-term repo and Treasury bill purchases. The level of short-term repo will be reduced in the coming weeks as the potential year-end liquidity concerns are behind us. How much the balance sheet actually contracts, if at all, will be watched very carefully by the markets. Remember that going forward T-bill purchases will be doing more of the heavy lifting.)

Economy

"Overall manufacturing production appeared likely to remain soft in coming months, reflecting generally weak readings on new orders from national and regional manufacturing surveys, declining domestic business investment, slow economic growth abroad, and a persistent drag from trade developments."

"In addition, softness in business investment and manufacturing production so far this year were seen as pointing to the possibility of a more substantial slowing in economic growth than the staff projected .... participants saw trade developments and concerns about the global economic growth outlook as the main factors contributing to weak business investment and exports."

"A number of participants observed that the domestic economy was showing resilience in the face of headwinds from global developments. Moreover, statistical models designed to gauge the probability of recession using financial market data, including those based on information from the Treasury yield curve, suggested that the likelihood of a recession occurring over the medium term had fallen noticeably in recent months."

(As to the above models - In a world where one could argue that price signals have been warped or even broken by CB policy, they are relying on those price signals to inform their views. This increases the likelihood of policy errors going forward.)

Financial Stability

"A few participants raised the concern that keeping interest rates low over a long period might encourage excessive risk-taking, which could exacerbate imbalances in the financial sector. These participants offered various perspectives on the relationship between financial stability and policies that keep interest rates persistently low. They remarked that such policies could be inconsistent with sustaining maximum employment, could make the next recession more severe than otherwise, or could strengthen the case for the active use of macroprudential tools to guard against emerging imbalances."

Spyglass Macro

Global Macro Advisory for Active Investors

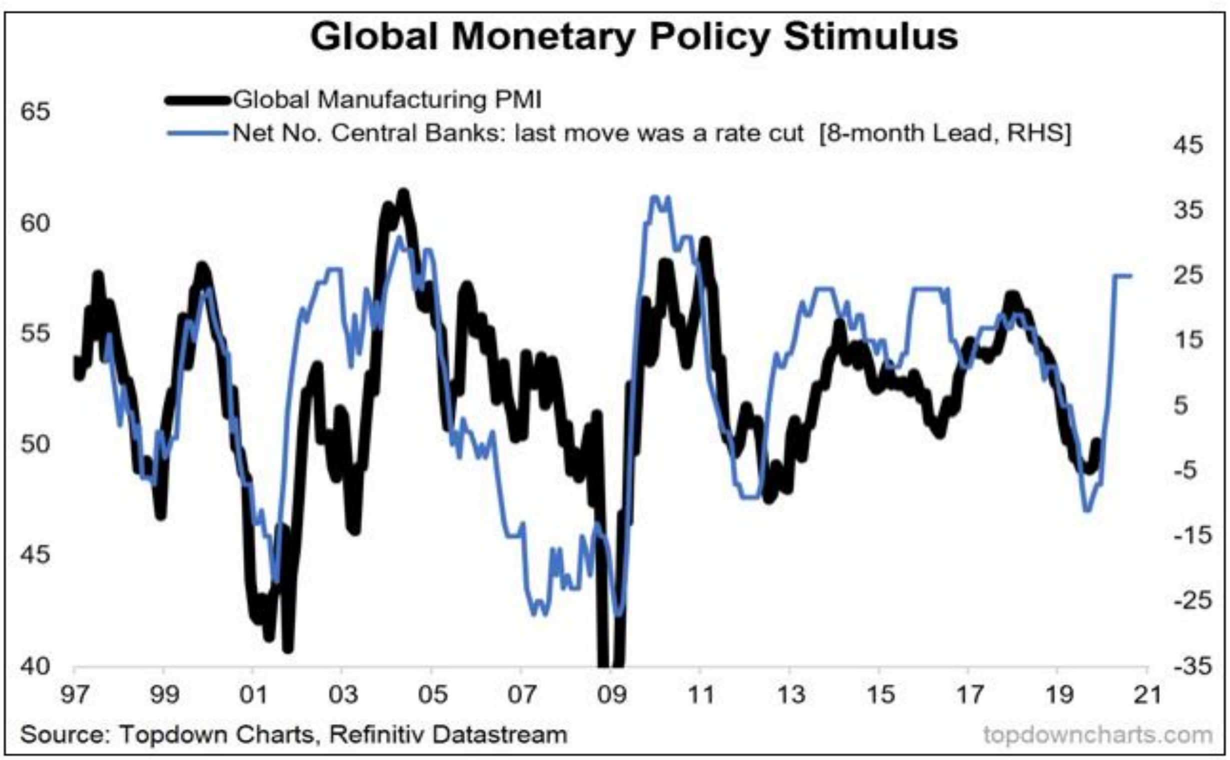
The Markets Growth Narrative

Last year's (oversimplified) sequence of events:

- The late 2018 equity market swoon got the Fed to stop hiking and end QT.
- Stocks rallied hard off the 2018 lows.
- Trade tensions, slowing manufacturing, a strong USD and flattening yield curve scared people out of stocks.
- Stocks couldn't stay down however as Fed started cutting and buybacks continued to take shares out of the market.
- Global Central Bank easing proliferated, sparked by falling global growth and plunging PMI's
- Improvement in China trade story, with a partial solution expected, took stocks up and forced people back in as CB's continued to add accommodation.

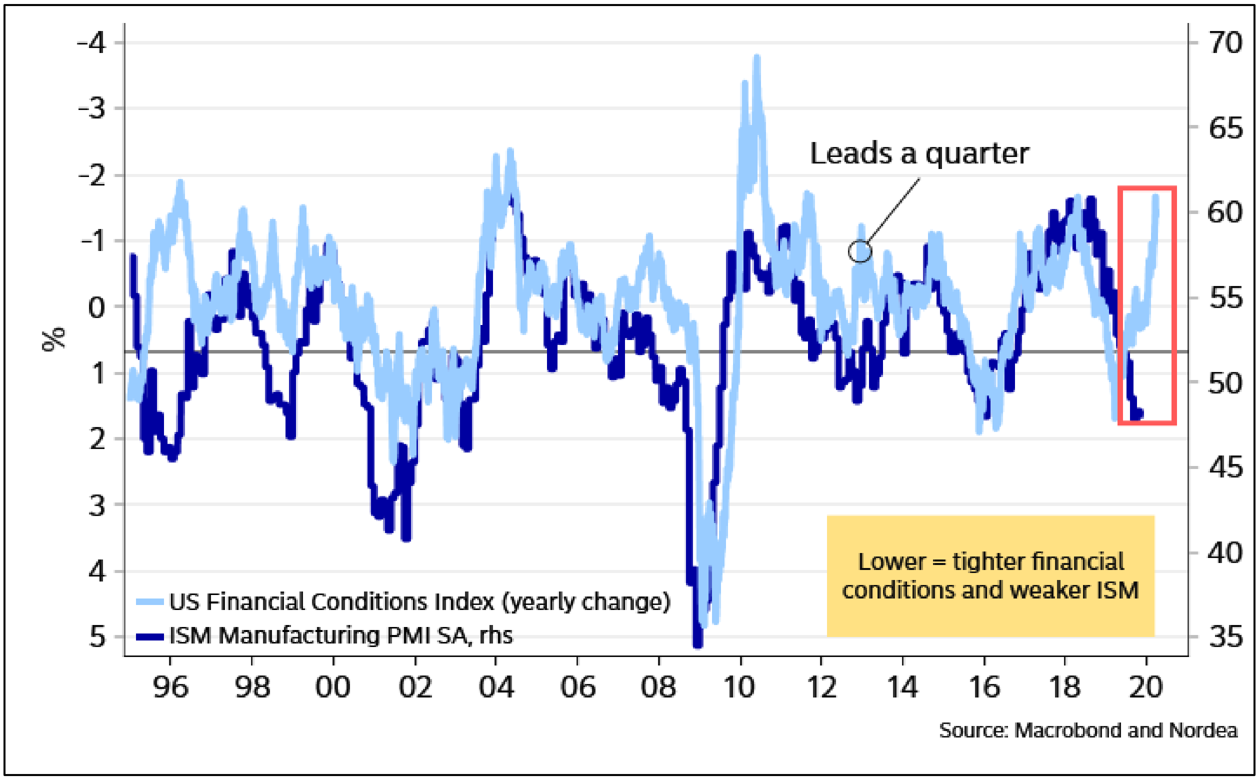
Today's situation:

- Central Bank stimulus and trade war de-escalation to provide support for PMI's and global growth. Global reflation and a growth pick-up are the expected results, if history repeats.



Contact: efill@spyglassmacro.com / SMS, WhatsApp and Voice at +1.203.219.3649

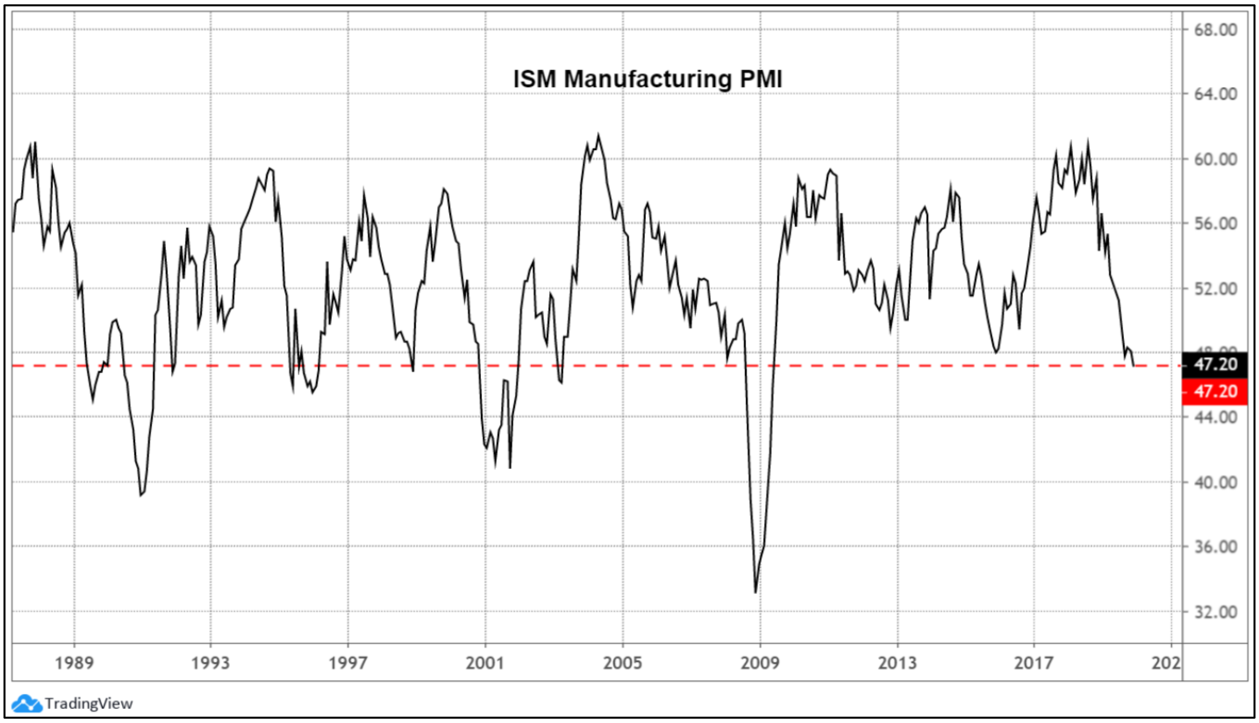
- US Financial Conditions have eased considerably as Fed cut rates, credit remained strong, stocks rallied, and the dollar eased off the highs. A lot has been priced now.
- PMI's should bounce… but might need more time. They need to bounce.



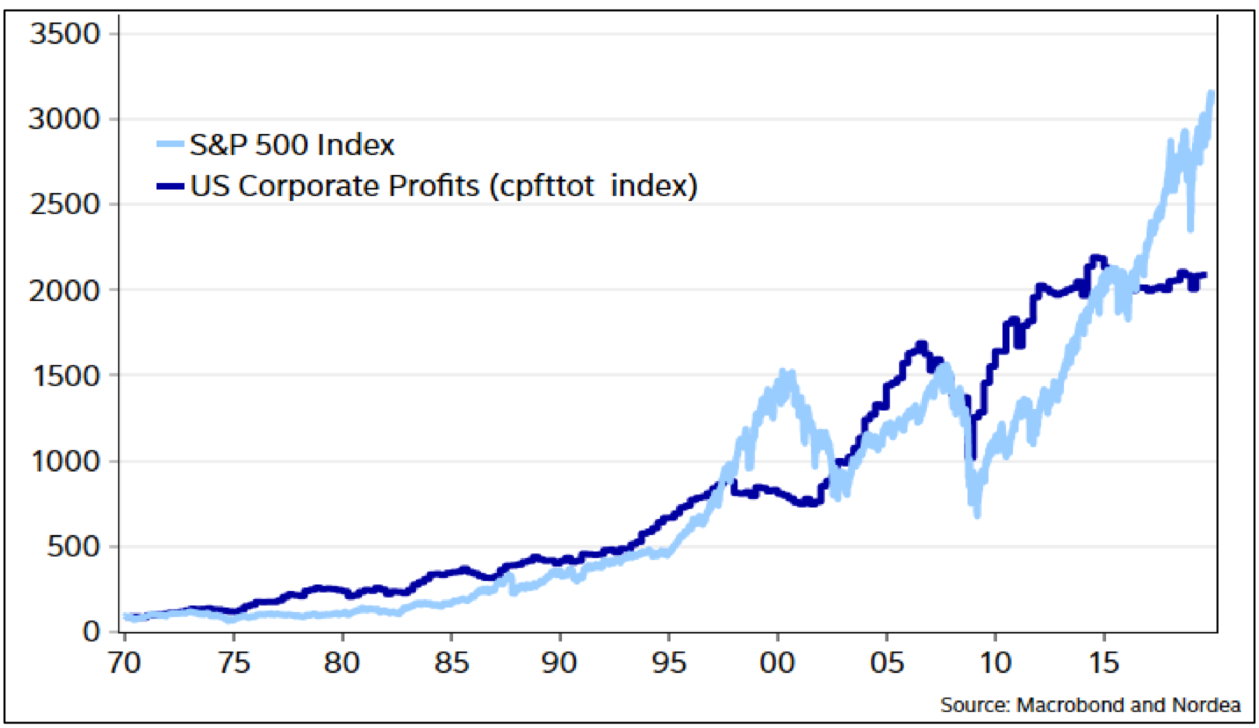
So far, Global PMI's have been lackluster, with some continuing to weaken. Last week's data was more of the same in that respect.

The shocker was the US ISM Manufacturing PMI on Friday. The market was expecting an uptick from the prior 48.1 to 49. However, it came in at a surprising 47.2. While manufacturing only accounts for 11.6% of US GDP it has knock on effects and a global growth component. We have seen dips to these levels before without a recession, but we are now skating on thin ice and further acceleration to the downside would be worrying.

Equities have enthusiastically embraced the large Global Central Bank stimulus, and the expected reflation and earnings improvements it has historically brought. With markets now long again and a bounce in PMI's largely priced, data needs to now improve or at least remain stable (buying time) or the markets will again get jittery.



US Corporate earnings have stalled over the last few years. US stocks are now expensive given that last years equity rally was based almost entirely on multiple expansion.

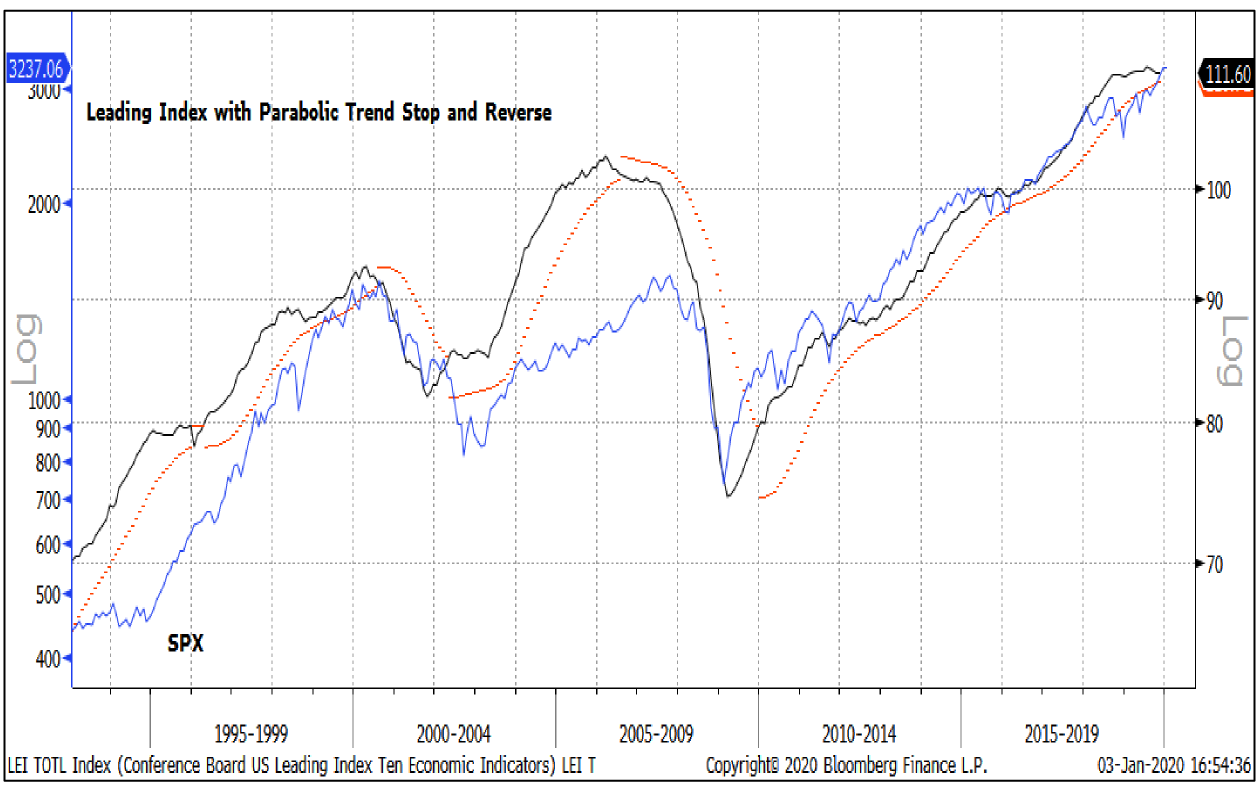


One indicator I have been watching is the Conference Board Leading Economic Index (LEI).

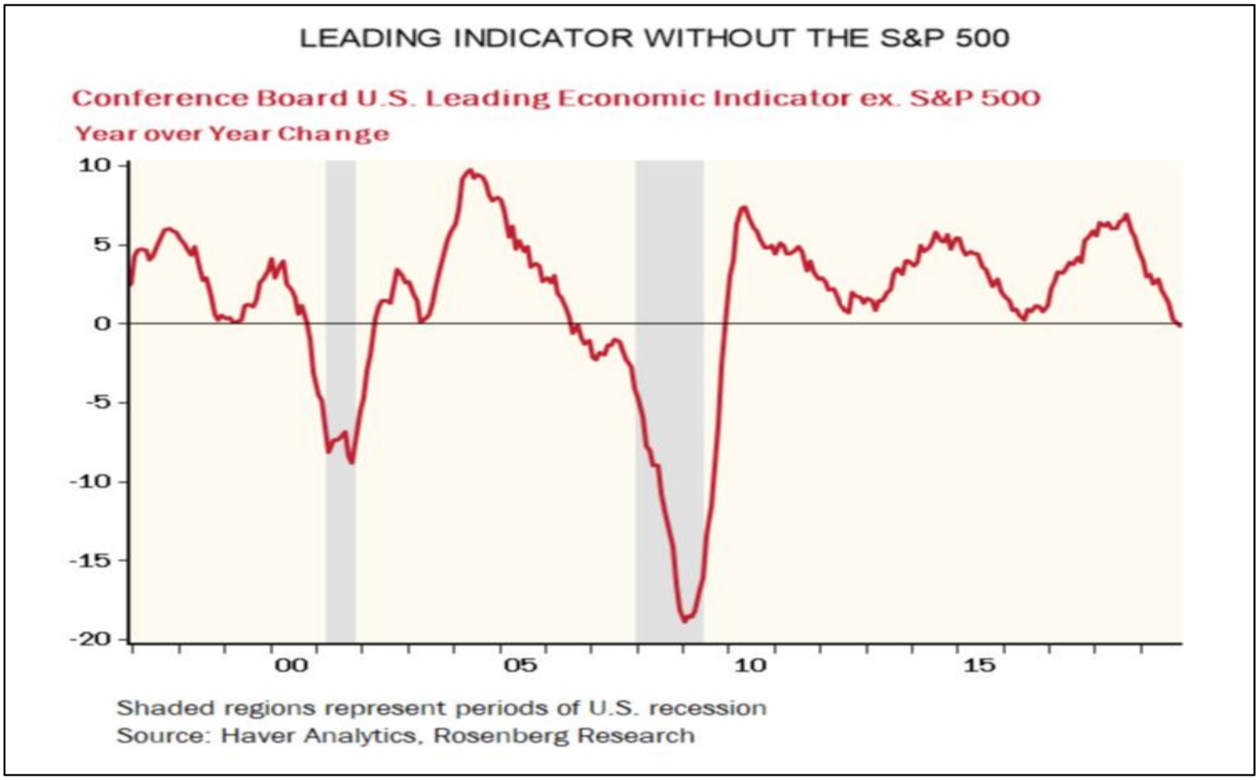
The ten components for the U.S. include:

- Average weekly hours, manufacturing
- Average weekly initial claims for unemployment insurance
- Manufacturers' new orders, consumer goods and materials
- ISM® Index of New Orders
- Manufacturers' new orders, nondefense capital goods excluding aircraft orders
- Building permits, new private housing units
- Stock prices, 500 common stocks
- Leading Credit Index™
- Interest rate spread, 10-year Treasury bonds less federal funds
- Average consumer expectations for business conditions

The LEI has a good record of highlighting when risks to the economy and the markets are rising. I like putting a "trailing take profit" on it via a parabolic indicator. While the index has been flat to declining slightly, it hasn't yet rolled.



As the S&P is in the index and has been on a tear recently it is interesting to see how the index is doing excluding the equities componant. It has the same look as the ISM Manufacturing PMI. This would be a good level to hold…



What to Focus on Now:

The unfolding Iran situation is now the wildcard… If that goes totally sideways over the next few days/weeks, all bets are off.

If things calm down, we may well resume the recent trend towards a weaker dollar.

Over the last two weeks the USD has been weakening vs. other currencies to varying degrees. This has had a positive effect on EM and has enabled Gold to break higher and crack its correlation to bonds. Only over the last two trading days have bonds caught a bid.

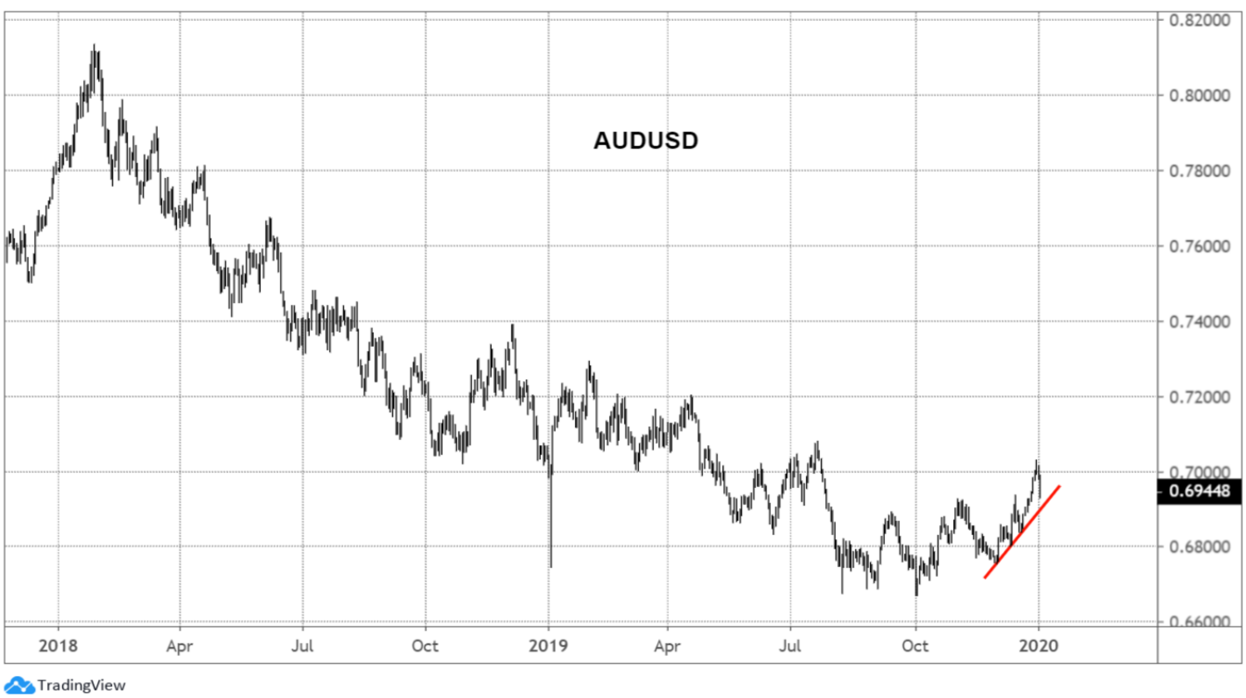
Gold has been leading as the narrative has changed from just following yields around.

As a result, the correlation has cracked.

The DXY and its primary EUR, GBP and Yen components, has so far been pretty dull.

Commodity and EM FX have done better. USDCAD had a nice break… Oil is helping.

AUD, with more of a China/EM tilt, is trying too, but data has been disappointing so far.

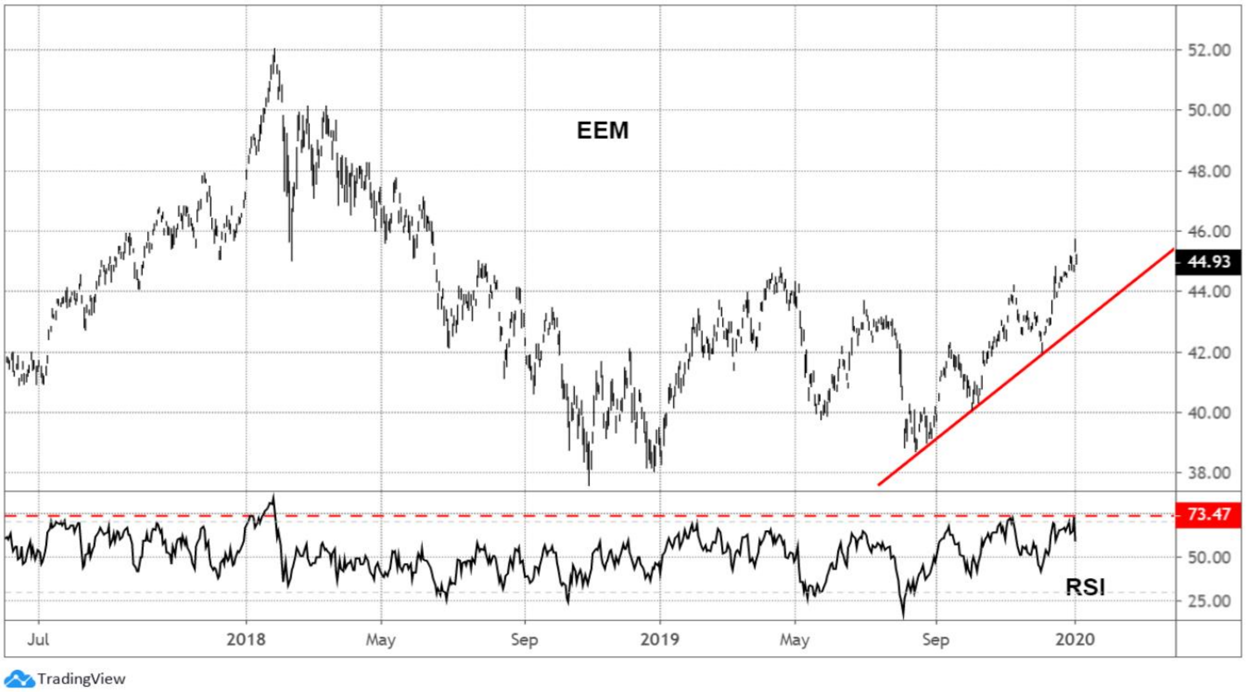


Contact: efill@spyglassmacro.com / SMS, WhatsApp and Voice at +1.203.219.3649

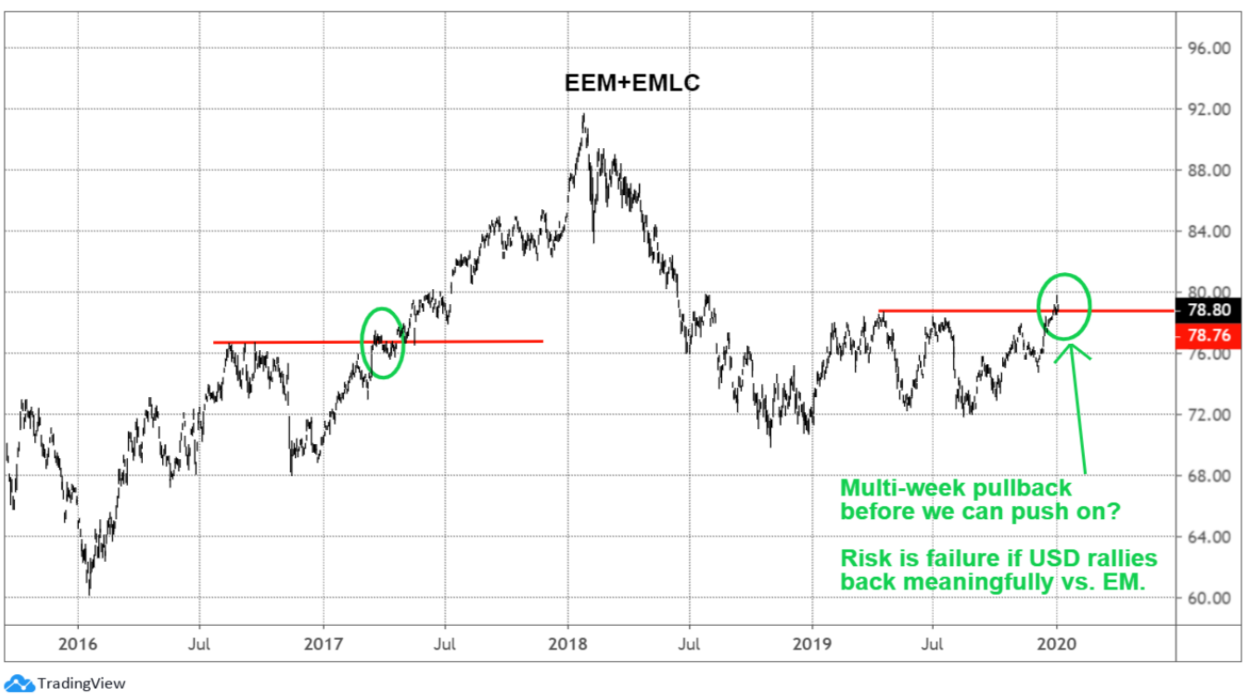
USDSGD had a nice break.

Chinese equities have broken above what had been the top of the range for 6-months.

EM has so far benefited from the pick-up in global growth hopes and the weaker USD.



However, the move is a bit stretched and I wouldn't be surprised to see a pullback.



US equities are in a similar position. They have rallied relentlessly, but the Iran story and weaker US data on Friday put in an outside range day for the S&P e-mini's. So far, however, no real roll in momentum (2nd chart).

TradingView

TradingView

Spyglass Macro

Global Macro Advisory for Active Investors

We have an interesting week ahead of us with the Iran situation and US and Canadian Employment data and more PMI's.

Actionable Trades and Developments:

Equity Indexes: Nothing at the moment

Fixed Income: Nothing much right now but there are some cheap Eurodollar trades out there if you want some Eco weakness hedges.

Commodities: Still like Gold and Silver.

Currencies: Short USD vs. MXN, CAD and AUD. Looking for potential USD downside acceleration overall. Iran situation could cause a near-term USD pop however.

Important Macro Data Releases and Events for the Week

Monday 1/6/2019

- Caixin Service PMI (Dec) Forecast: - , Prior: 53.5
- Retail Sales MoM (Nov) Forecast: 1%, Prior: -1.9%
- Markit PMI Composite (Dec) Forecast: 49.5, Prior: 49.4
- Markit PMI Composite (Dec) Forecast: 50.6, Prior: 50.6
- Markit Service PMI (Dec) Forecast: 52.2, Prior: 52.2
- Markit PMI Composite (Dec) Forecast: 52.2, Prior: 52.2

Tuesday 1/7/2019

- Retail Sales YoY (Nov) Forecast: 1.3%, Prior: 1.4%
- Consumer Price Index YoY (Dec) Forecast: 1.3%, Prior: 1%
- Consumer Price Index - Core YoY (Dec) Forecast: 1.3%, Prior: 1.3%

	Trade Balance (Nov) Forecast: $-49 B, Prior: $-47.2 B
	ISM Non-Manufacturing PMI (Dec) Forecast: 54.5, Prior: 53.9
	Factory Orders MoM (Nov) Forecast: 0.2%, Prior: 0.3%
	Ivey PMI (Dec) Forecast: - , Prior: 58.4
	Ivey PMI s.a. (Dec) Forecast: 53.8, Prior: 560
Wednesday 1/8/2020	Factory Orders s.a. MoM (Nov) Forecast: 0.1%, Prior: -0.4%
	Business Climate (Dec) Forecast: -0.16, Prior: -0.23
	ADP Employment Change (Dec) Forecast: 150 k, Prior: 67 k
Thursday 1/9/2020	Trade Balance (Nov) Forecast: 6100 m, Prior: 4502 m
	Consumer Price Index YoY (Dec) Forecast: - , Prior: 4.5%
	Trade Balance s.a. (Nov) Forecast: EUR 20B, Prior: EUR 20.6B
	Industrial Production s.a. MoM (Nov) Forecast: 0.7%, Prior: -1.7%
	Unemployment Rate (Nov) Forecast: 7.5%, Prior: 7.5%
	Initial Jobless Claims Forecast: 222k, Prior: 222k
	Initial Jobless Claims 4-week ave. Forecast: 236.64, Prior: 233.25k
	Continuing Claims Forecast: 1.72m, Prior: 1.728m
	Fed's Clarida **SPEECH**
	BoC's Governor Poloz **SPEECH**
	German Buba President Weidmann **SPEECH**

Spyglass Macro

Global Macro Advisory for Active Investors

Friday
01/10/2020

FDI-Foreign Direct Investment YTD YoY (Dec) Forecast: - , Prior: 6%

Nonfarm Payrolls (Dec) Forecast: 160 k, Prior: 266 k

Average Hourly Earnings YoY (Dec) Forecast: 3.1%, Prior: 3.1%

Average Hourly Earnings MoM (Dec) Forecast: 0.3%, Prior: 0.2%

Unemployment Rate (Dec) Forecast: 3.5%, Prior: 3.5%

Labor Force Participation Rate (Dec) Forecast: - , Prior: 63.2%

Unemployment Rate (Dec) Forecast: 5.8%, Prior: 5.9%

Net Change in Employment (Dec) Forecast: 20 k, Prior: -71.2 k

Contact: efill@spyglassmacro.com / SMS, WhatsApp and Voice at +1.203.219.3649