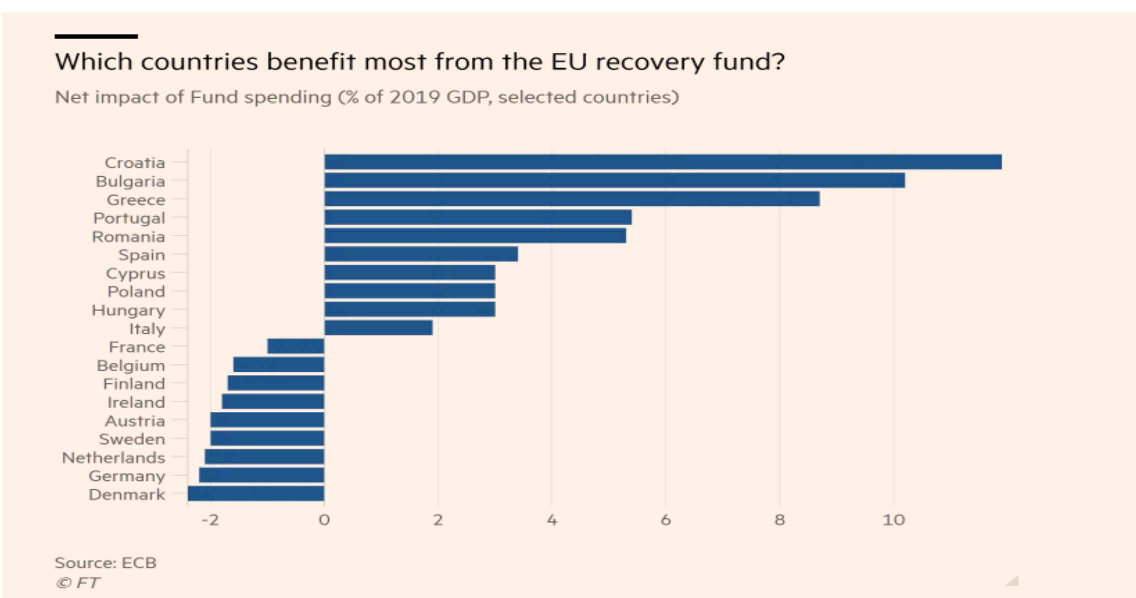
What to focus on in Global Macro for the week of September 28th, 2020

Macro Themes on the Radar:

Last week European equities continued to underperform and potentially broke lower. With poor price action, a slowing recovery and new COVID outbreaks, the focus is back on the ECB and EU fiscal spending. Last week, ECB staff called on Brussels to make the EU recovery fund permanent. This isn't immediately actionable given there is still a long way to go in just getting the current agreement up and running. However, might as well start signaling early. As the FT reports:

"The ink on a landmark EU agreement to establish a €750bn recovery fund is barely dry. Many of the details are still to be worked out. Member states are at loggerheads over safeguards to ensure governments spend the money well and protect the rule of law. The European parliament wants more money for education and research. New EU taxes to help pay back hundreds of billions of euros in commonly-issued debt remain a distant prospect. It will be months before any money is paid out. But its strongest supporters have already banked the recovery fund as a historic breakthrough and are now looking at the next building blocks of fiscal union to underpin the euro.

In a research note last week, European Central Bank staff said the recovery fund would bring sizeable financial support for the countries worst hit by the pandemic and economic shock. They also suggested the fund, supposedly an emergency one-off, should become a permanent deficit facility for macroeconomic stabilization in deep crises. Yannis Stournaras, a member of the ECB's governing council, was more explicit. It should not be a one-off, he argued, but "the beginning of a more coordinated and systemic policy response to a serious external symmetric shock with asymmetric disinflationary consequences". With the zeal of the convert, Germany's finance minister Olaf Scholz says the recovery fund is only the beginning of fiscal union. If the EU is going to complete its banking union, strengthening financial stability and improving the flow of credit to businesses and households, it will need to broach the question of risk-sharing and fiscal backstops."



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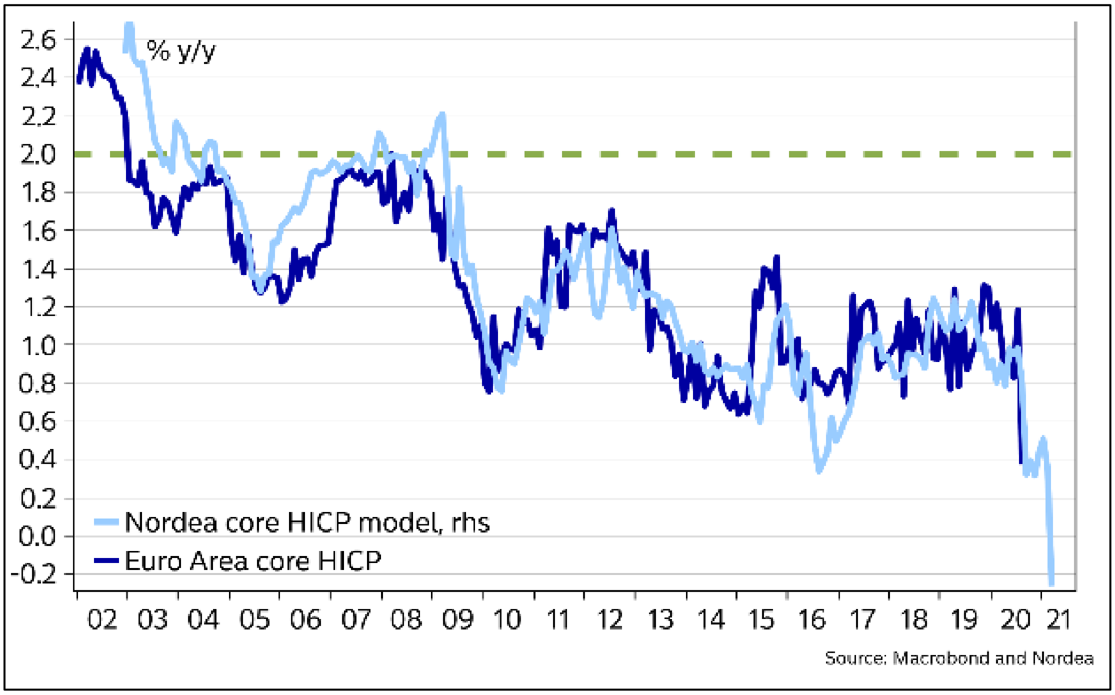
Lots more European "muddle-through" will be required…

In the meanwhile, Nordea points out that we could see renewed downward pressure on European inflation led by wages. The ECB will continue to have its hand full.

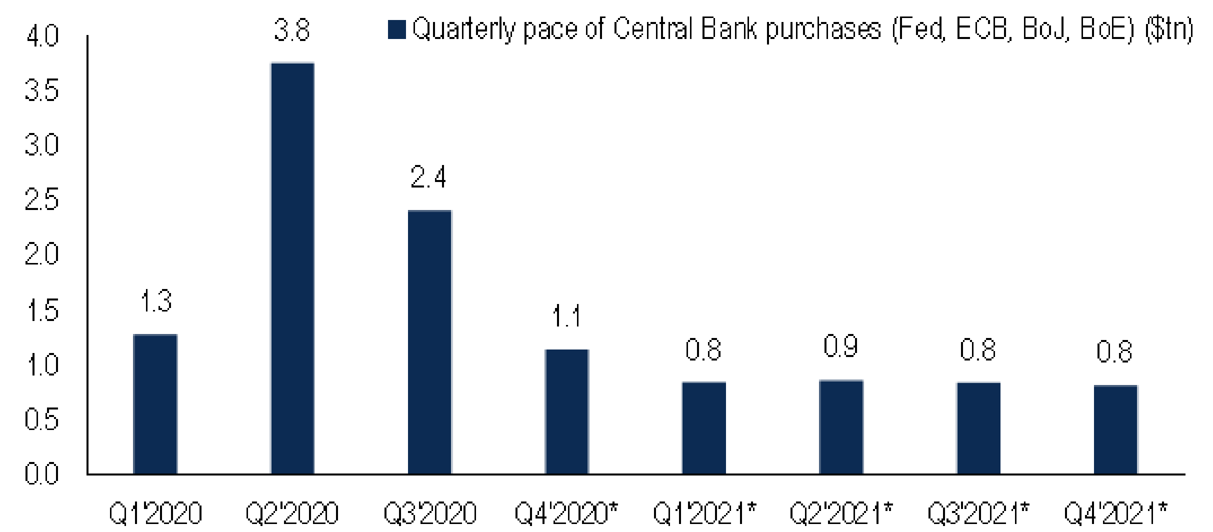


Fed and Mnuchin last week…

Lots of Fed speakers last week topped off by Powell and Mnuchin in front of Congress. In the end, we had multiple officials calling for more fiscal stimulus given the limited monetary policy options. QE has been great for financial markets, but it has also magnified the wealth disparity.

Globally, the pace of QE additions is set to slow…

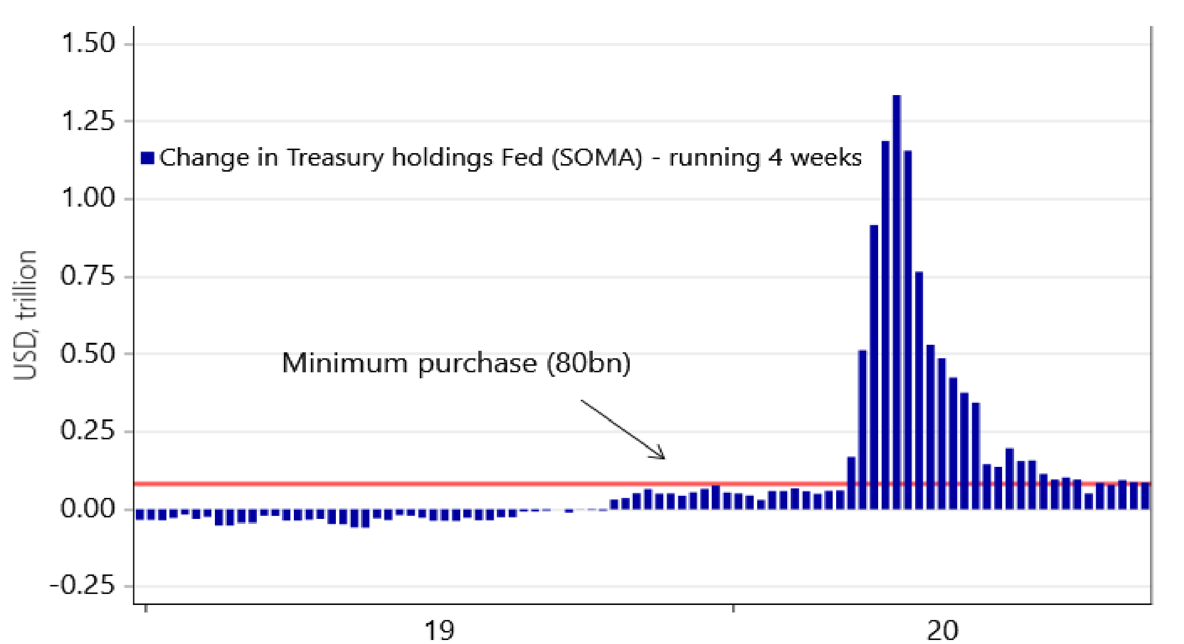
Chart 2: Pace of central bank injections via QE fading



Source: BofA Global Research, Bloomberg

The Fed is back to its announced minimum pace of QE and is expected to stay there unless markets become unruly again.

Chart 5. The Fed is buying right around its minimum promised pace.. No increase in sight short term.



Source: Macrobond and Nordea

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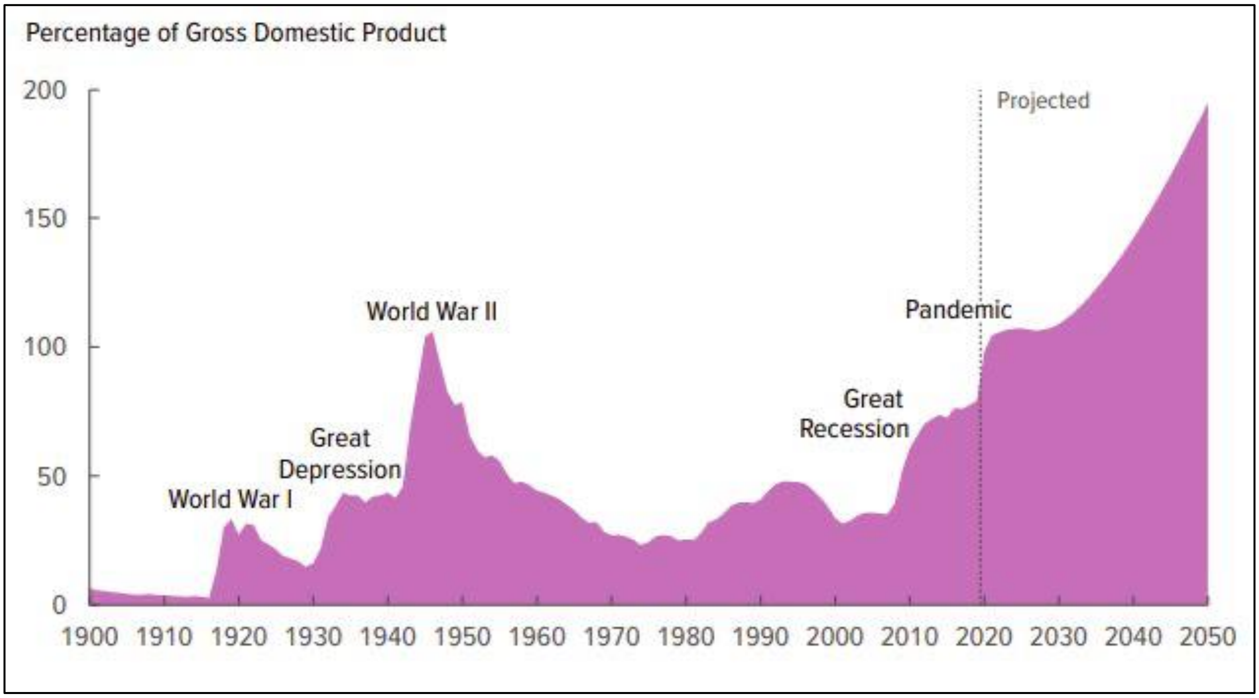
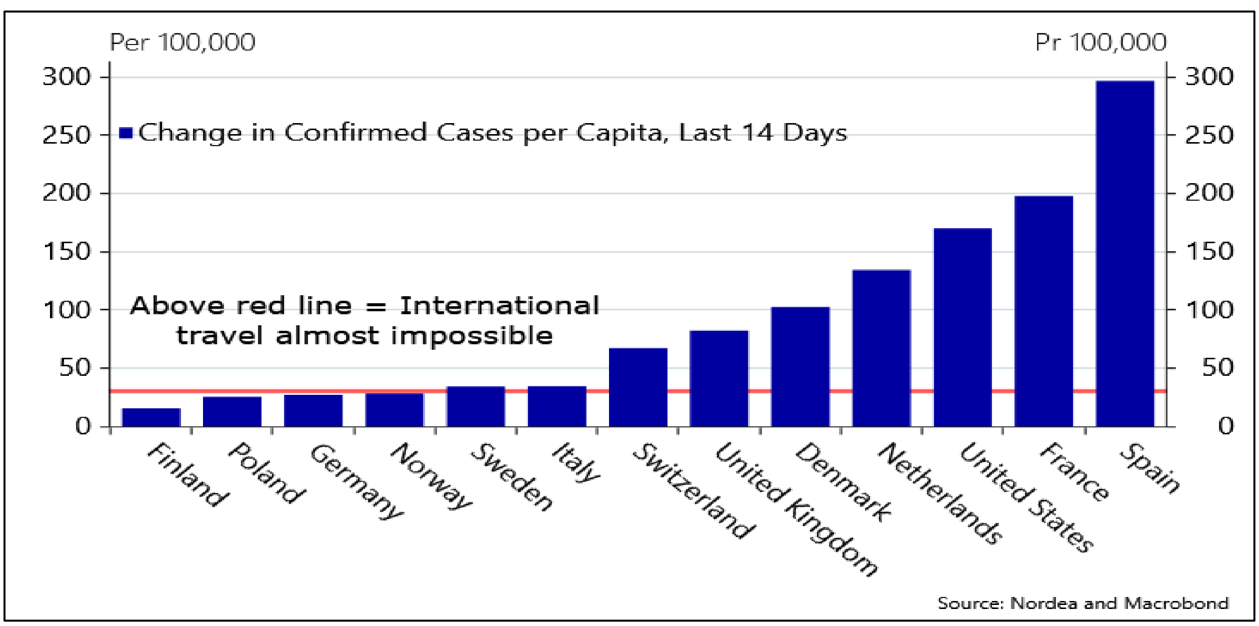
With the Fed putting maximum pressure on Congress to get more fiscal support into the system, it is no wonder that Pelosi and Mnuchin are set to resume negotiations. The Democrats are preparing a new $2.4Trl stimulus plan with unemployment aid and further direct payments.

While the Fed is quick to point out that now is not the time to focus on restraining spending, it must also be eyeing the latest CBO projections for US debt over the coming years. Don't expect QE to go away again, ever.

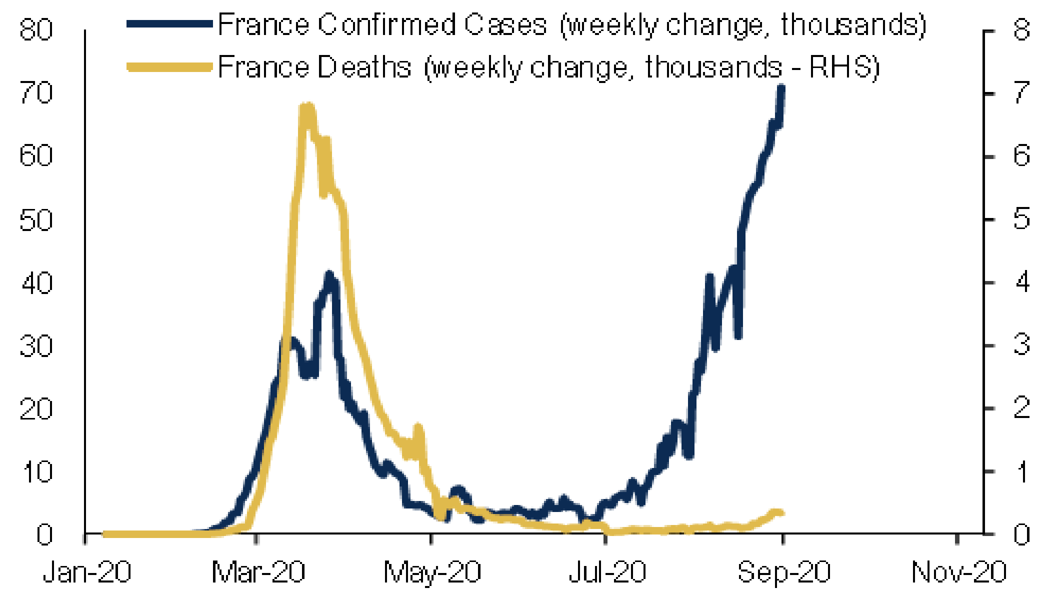


While the US continues to struggle with new cases, Europe has been catching up.



The good news is that, so far at least, the death toll has remained much lower than during the first round. The most recent data on new cases looks like France may be turning the corner, while Spain remains uncontained.

Chart 4: COVID-19 mortalities well below cases



Source: BofA Global Investment Strategy, Bloomberg

<u>**What to Focus on Now:**</u>

Equities

As we head into month end, there is still a very good chance that the big reversals in the monthly charts hold (absent a big early week rally). If so, it is unlikely to be quickly undone.

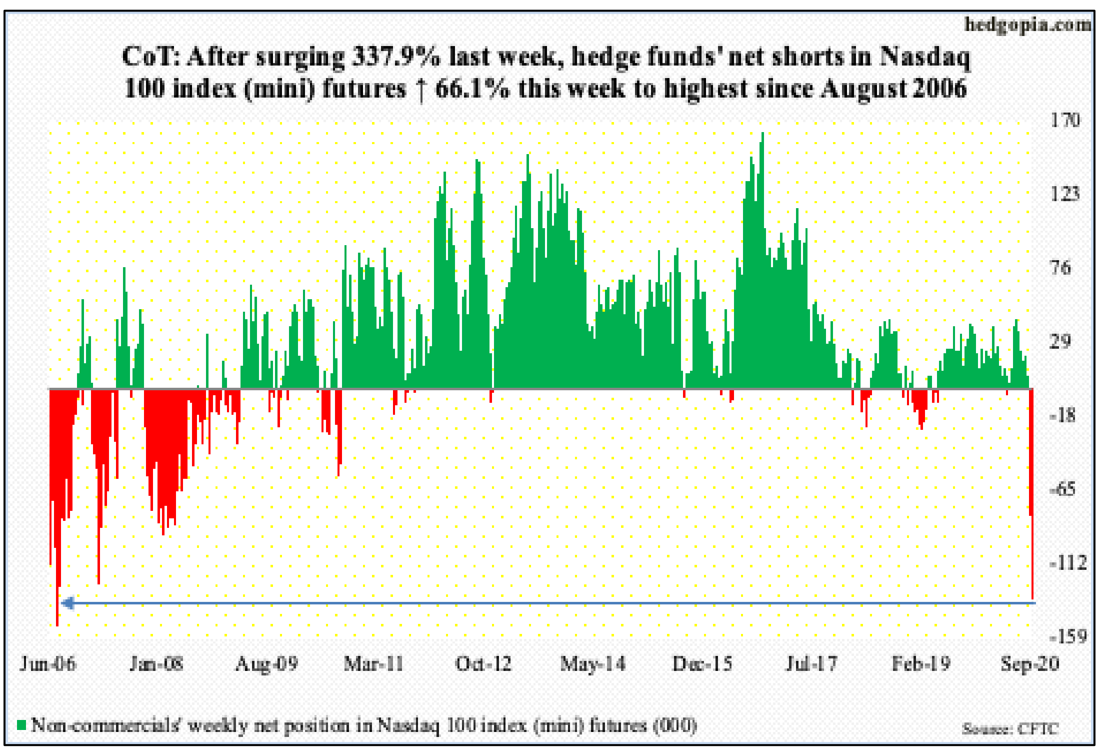
The global importance of politics and fiscal spending as market drivers, is only growing. At the same time central banks, having fully utilized traditional monetary policy, are increasingly active in markets in ways that disrupt price discovery.

With so little transparency due to multiple unknown outcomes and non-economic buyers of assets, volatility should remain high. It brings lots of risk, but also a lot of potential opportunity.

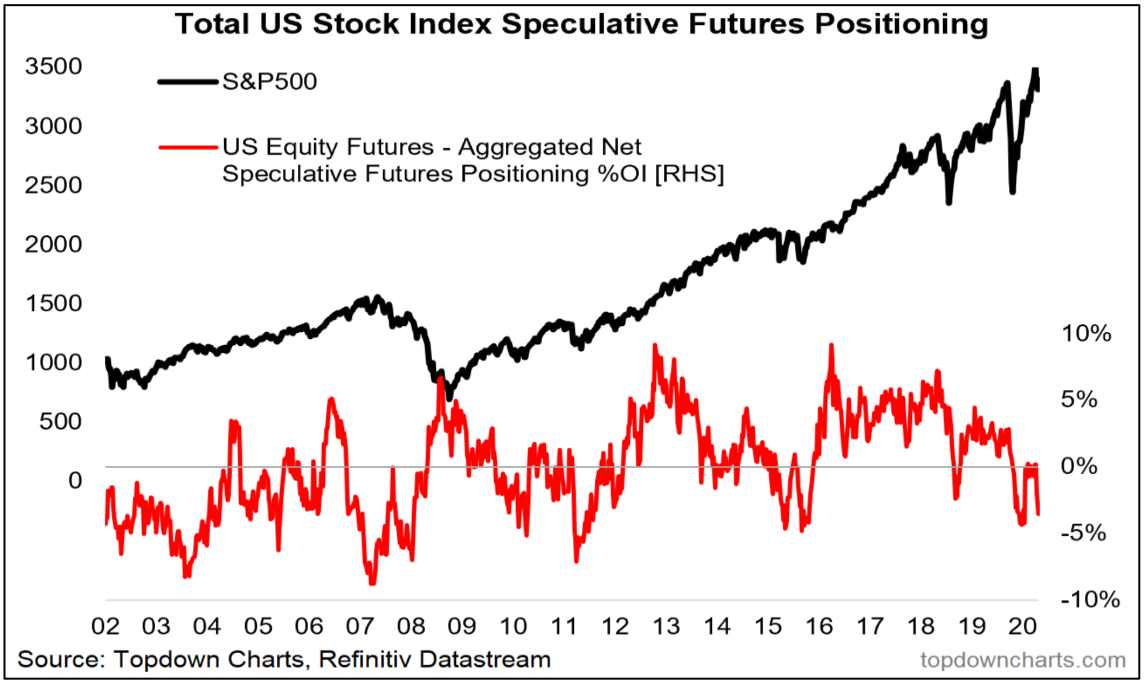
The ever-expanding trading range in equities, that began when global growth started to slow in 2018 and the dollar started to rally, has left us with a very unusual price pattern. Now, potentially with a reversal at the highs.

Here the monthly S&P chart with the outside range month.

There are signs that some investors have already taken the Q4 uncertainties into account and have positioned themselves short via index futures. It is unclear if these are shorts vs. underlying long single stock positions or outright shorts. Nasdaq mini's...



Also, vs. the S&P… On the face of it you might wonder if people are already short, but it is hard to know what the net positions look like.



Potentially, the selling of futures has taken away some of the options buying you might otherwise expect. The VIX has remained relatively calm. Of course, there is a big bulge in volatility already priced for the election and absolute vol. levels never got back down to particularly cheap levels, so maybe those factors are deterring put buyers here.

European equities broke last week and hit an important inflection point. When this signal is triggered, they tend to either quickly bounce or accelerate to the downside. Buying delta hedged 2-3m puts allows you to trade the signal with good risk-reward.

US Financials have had an ugly couple of weeks, even considering their now chronic multi-year underperformance.

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Here they are vs. the entire US market…

And vs. the world ex-US… no recovery here post the Q1 break lower.

With the price action in corporate IG and HY bonds now providing so much less information about the state of credit, banks are worth watching.

USD

It is probably not surprising given the relationship that the dollar has had with stocks (and everything else) since the March lows…

But this month is shaping up to be an outside month reversal in the USD as well. In the case of the dollar the reversal comes after holding big price levels. It could be short lived, but it is meaningful for now.

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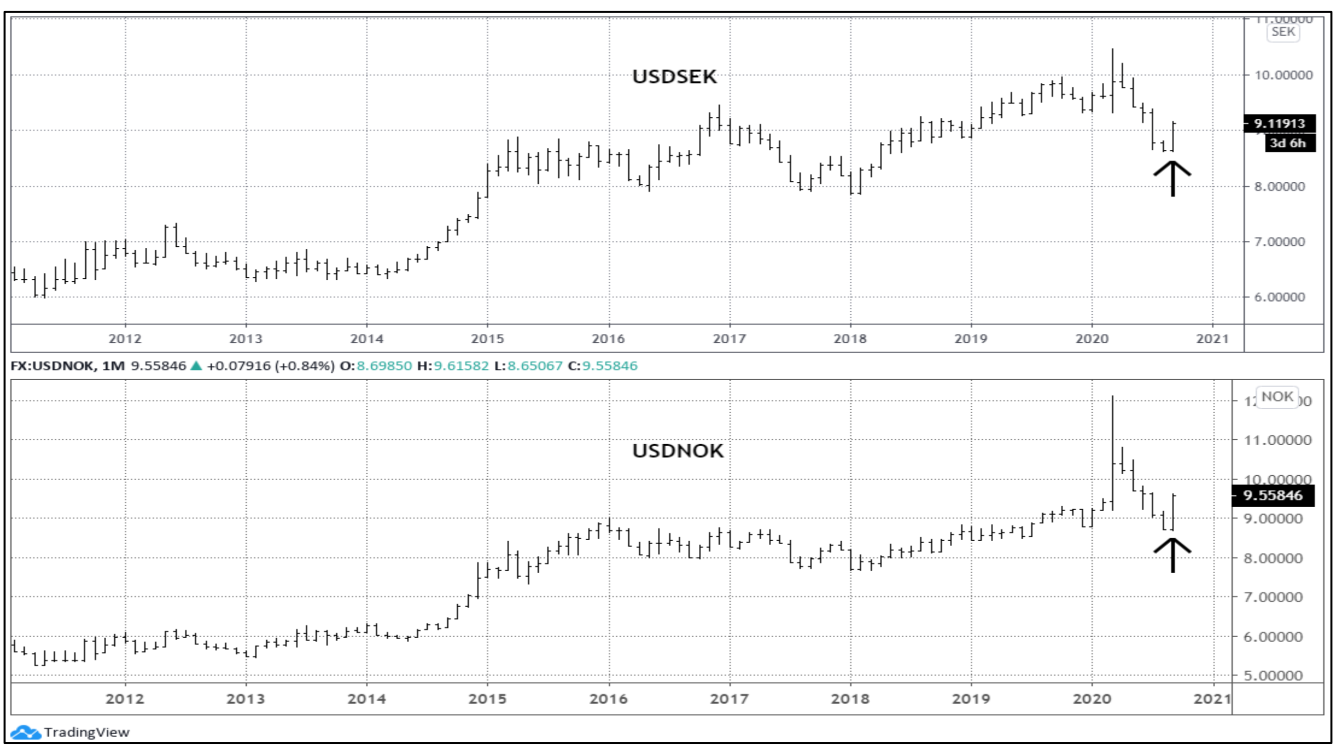
Given its high weighting in the DXY, it isn't surprising we have it in the EUR as well.

But also vs. the AUD and even currencies like NOK and SEK.



Interestingly, USD positioning hasn't backed off given the reversal in prices.

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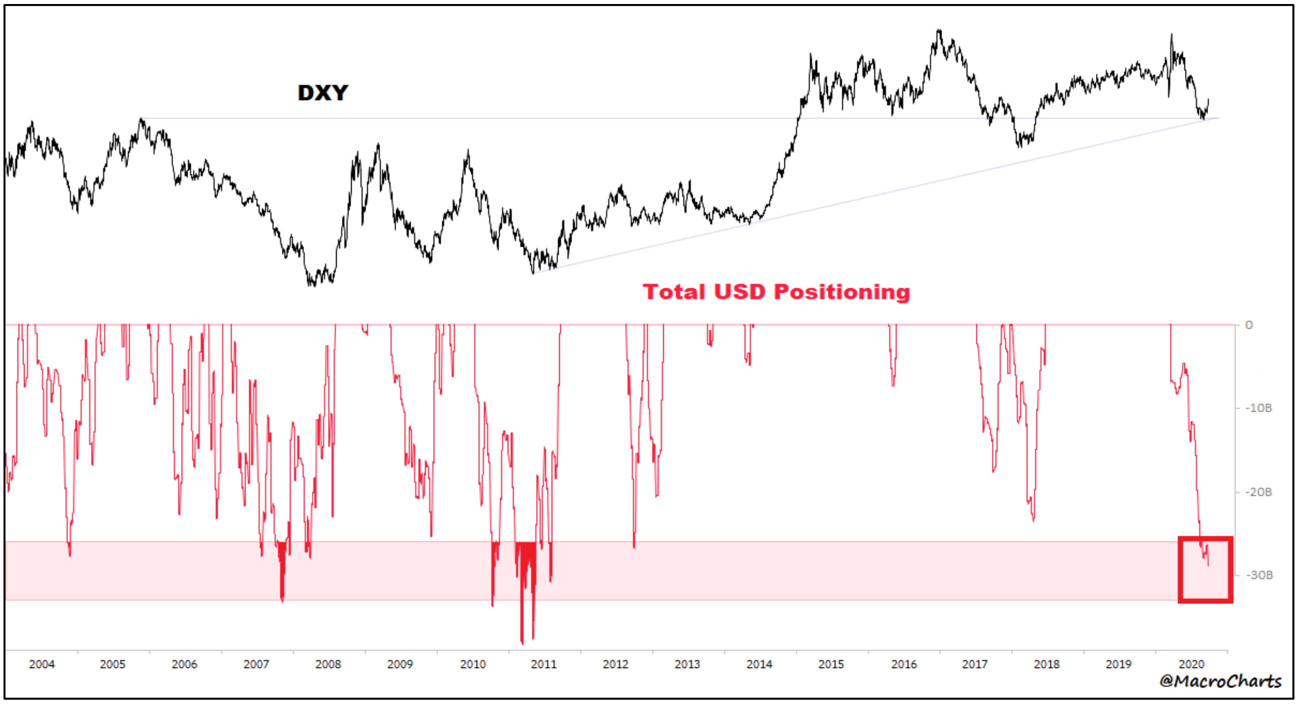
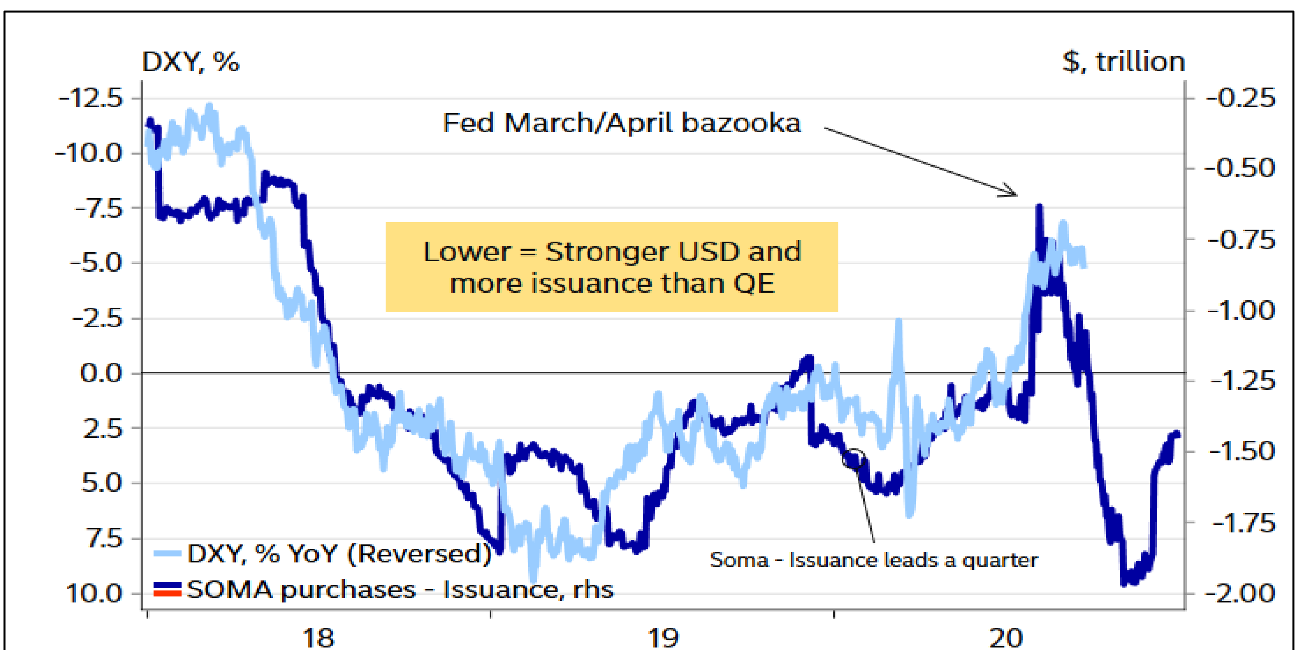


Perhaps we have more of an unwind in the USD shorts yet to come…

With QE purchases having fallen behind issuance, some are arguing that we are due for a bout of USD strength in the near-term as the net effect has been a tightening of USD supply.

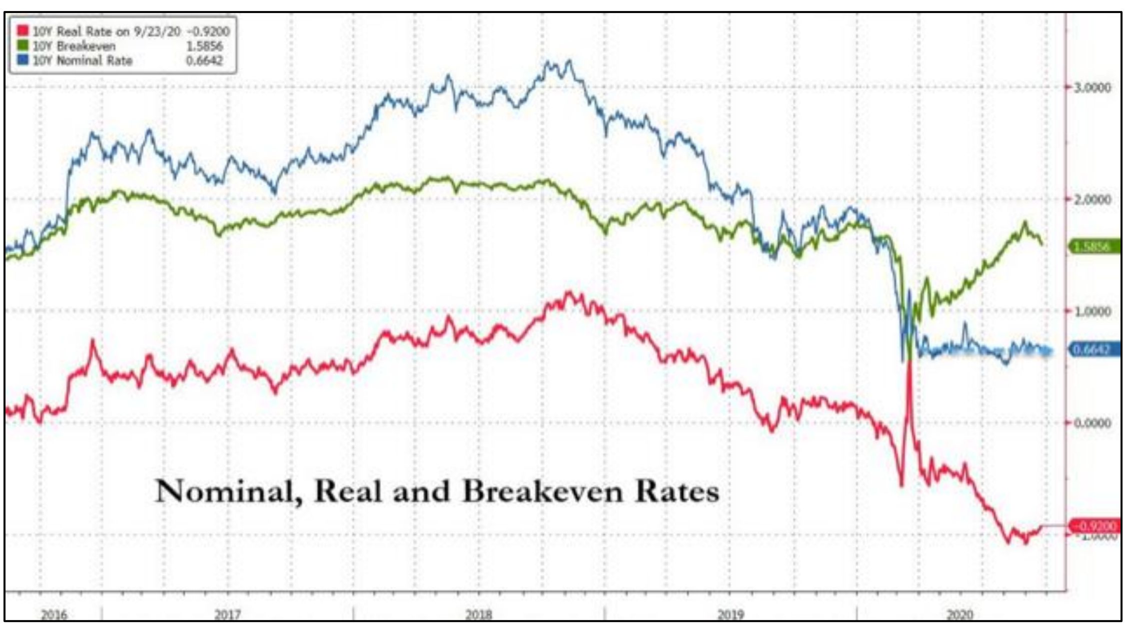


Source: Nordea and Macrobond

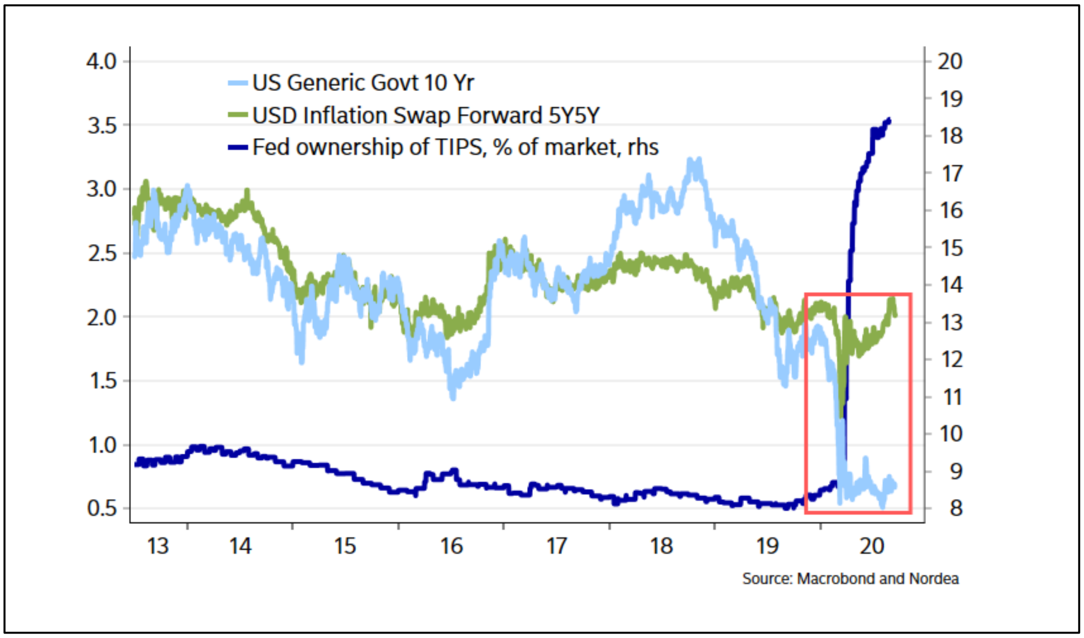
Fixed Income

Despite the price action in equities over the last week, US 30-year bonds are stuck.

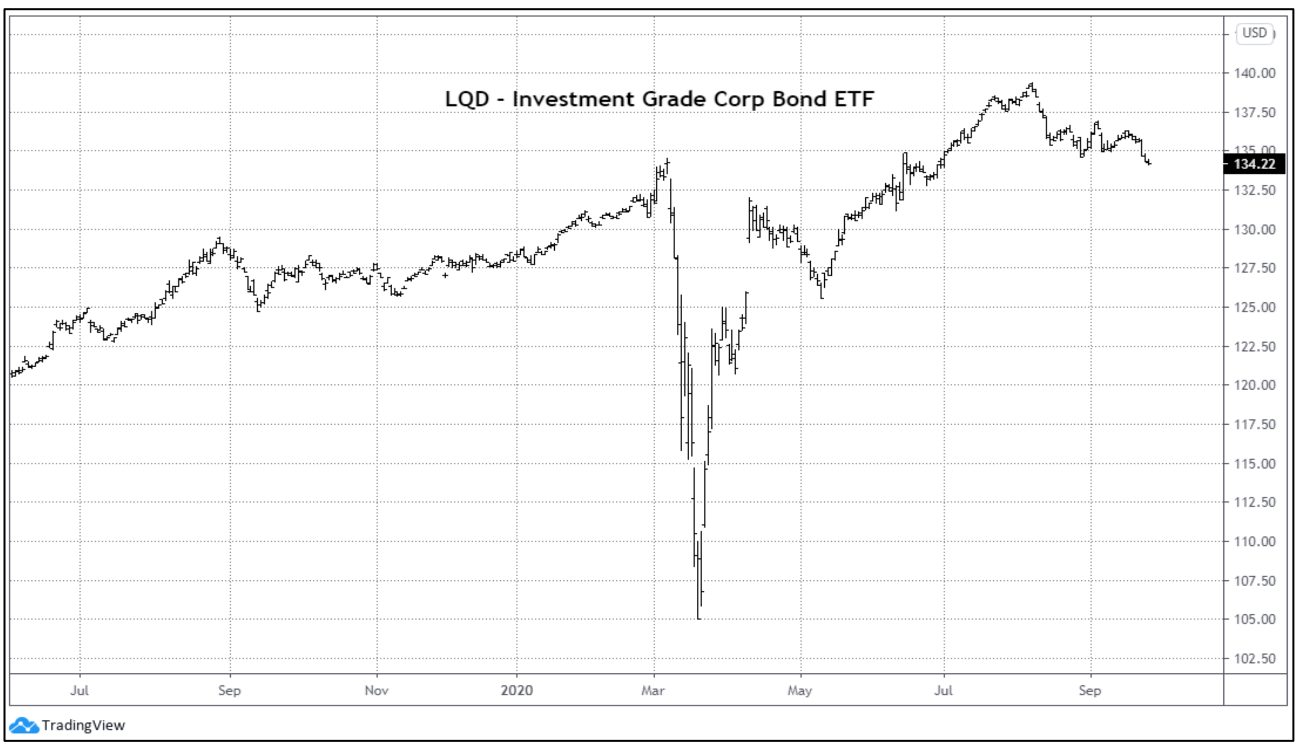
However, despite the sideways in nominal yields (blue is 10-year yield), inflation Breakevens have been moving higher, pushing down Real yields…



However, here again we have the Fed potentially influencing the price and information value. Given that the Fed has been actively buying TIPS, is the implied rise in inflation expectations really reflective of the market's view, or at least partially a result of Fed buying?

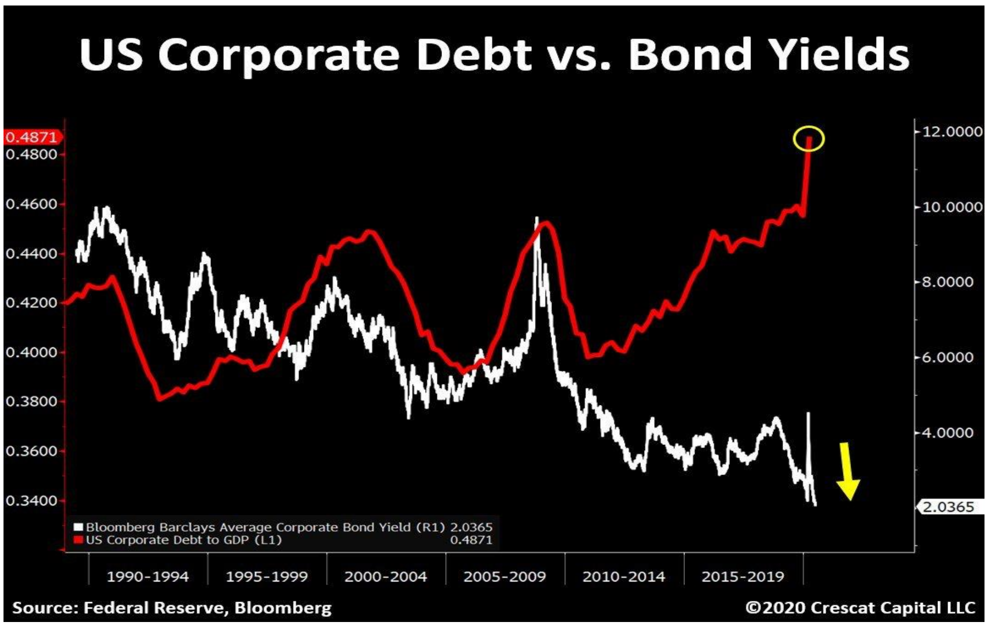


Same story in corporate bonds. Where would IG credit be now without the Fed? Hard to know.



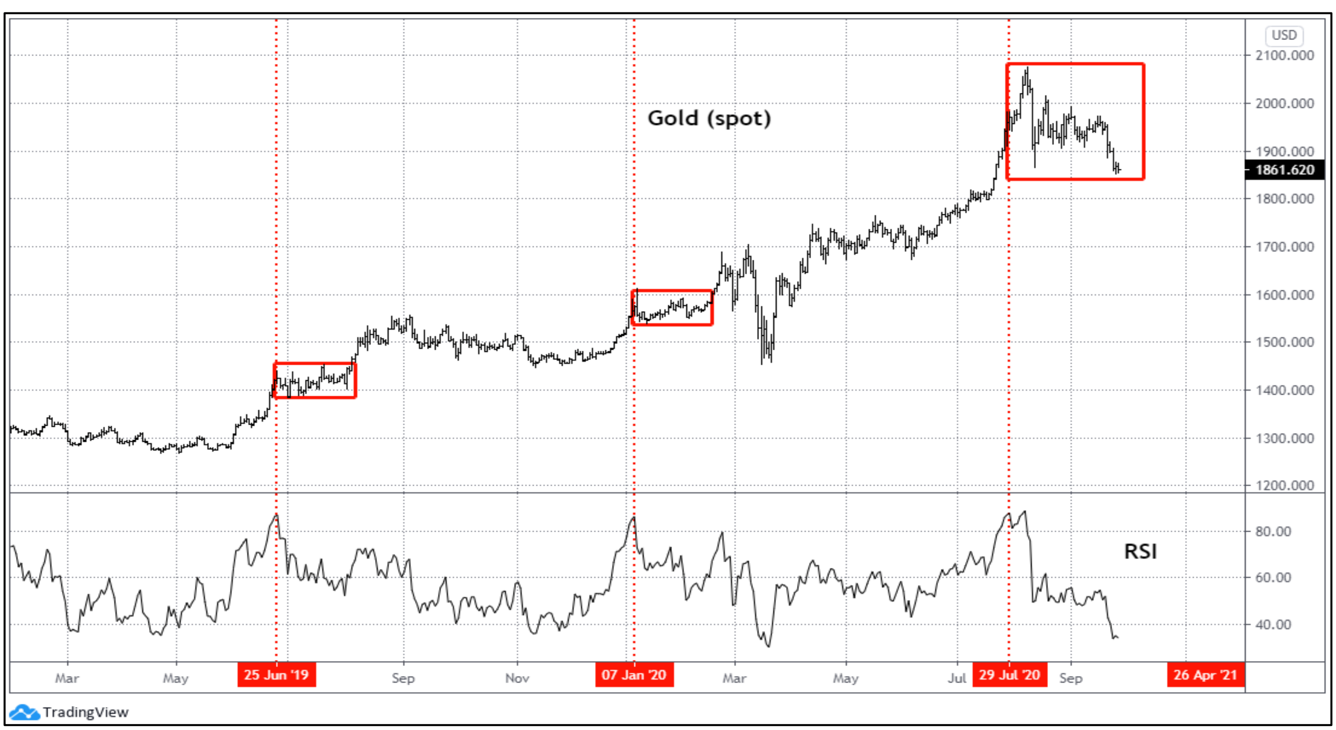
The recent effects of Fed buying are certainly relevant, as are the longer-term effects of financial repression.

Since the GFC we have had a break in the relationship of Corporate Bond Yields (white) and Corporate Debt to GDP (red).



Gold and Silver

Gold has been hit as positions have generally been unwound and the dollar has rallied.



I still think 1800/18500 is the buy zone. A more pronounced dollar rally could be problematic in the near-term, however.

Silver has been hit hard for the same reasons as Gold (but always more volatile). Here too it is worth owning some longer-term upside.

<u>Global PMI's this week and a number of Fed speakers. Of course, closing the week with US employment data.</u>

Important Macro Data Releases and Events for the Week

Monday 9/28/2020
- Leading Economic Index (Jul) Forecast: 86.9, Prior: 86.9
- Consumer Price Index (Sep) various measures

Tuesday 9/29/2020
- Consumer Confidence (Sep) Forecast: -13.9, Prior: -13.9
- Business Climate (Sep) Forecast: -1.38, Prior: -1.33

Stargazer
Asset Management

		Harmonized Index of Consumer Prices YoY (Sep) Forecast: -0.2%, Prior: -0.1%
		S&P Case-Shiller Home Price Indices YoY (Jul) Forecast: 3.8%, Prior: 3.5%
		Consumer Confidence (Sep)
		Fed's Williams SPEECH
		Fed's Clarida SPEECH
		First Presidential Debate
		Retail Trade s.a. MoM (Aug) Forecast: 3.2%, Prior: -3.3%
		Industrial Production YoY (Aug) Forecast: -10%, Prior: -15.5%
Wednesday 9/30/2020		Non-Manufacturing PMI (Sep) Forecast: 52.1, Prior: 55.2
		NBS Manufacturing PMI (Sep) Forecast: 51.2, Prior: 51
		Caixin Manufacturing PMI (Sep) Forecast: 53.1, Prior: 53.1
		Retail Sales YoY (Aug) Forecast: 3.4%, Prior: 4.2%
		BoE's Haldane SPEECH
		Unemployment Rate and Change (Sep)
		Consumer Price Index - Core YoY (Sep) Forecast: 0.7%, Prior: 0.4%
		Consumer Price Index YoY (Sep) Forecast: 0.2%, Prior: -0.2%
		ADP Employment Change (Sep) Forecast: 600k, Prior: 428k
		GDP Annualized Q2 Forecast: -31.7, Prior: -31.7
		Core PCE (Q2) Forecast: -1%, Prior: -1%
		PCE Prices (Q2) Forecast: -1.8%, Prior: -1.8%
		Chicago PMI (Sep) Forecast: 42.1, Prior: 51.2

Pending Home Sales MoM (Aug) Forecast: -, Prior: 5.9%

Tankan Large Manufacturing Index (Q3) Forecast: -23, Prior: -34

Thursday
10/1/2020

Markit Manufacturing PMI's (Sep) across Europe

Unemployment Rate (Aug) Forecast: 8%, Prior: 7.9%

Core PCE - Price Index MoM (Aug) Forecast: -, Prior: 0.3%

Personal Income MoM (Aug) Forecast: 0.1%, Prior: 0.4%

Personal Spending (Aug) Forecast: 0.7%, Prior: 1.9%

Initial Jobless Claims Forecast: -, Prior: 870k

Initial Jobless Claims 4-week ave. Forecast: - , Prior: 878k

Continuing Jobless Claims Forecast: -, Prior: 12.58m

Markit Manufacturing PMI's (Sep) Forecast: -, Prior: 53.5

ISM Manufacturing Employment Index (Sep) Forecast: 45.8, Prior: 46.4

ISM Manufacturing PMI (Sep) Forecast: 56, Prior: 56

ISM Manufacturing Prices Paid (Sep) Forecast: 54, Prior: 59.5

ISM Manufacturing New Orders Index (Sep) Forecast: 54.5, Prior: 67.6

Fed's Williams SPEECH

Friday
10/2/2020

Nonfarm Payrolls (Sep) Forecast: 875k, Prior: 1371k

AHE YoY (Sep) Forecast: 4.6%, Prior: 4.7%

AHE MoM (Sep) Forecast: 0.4%, Prior: 0.4%

Labor Force Participation Rate (Sep) Forecast: 61.5%, Prior: 61.7%

- U6 Unemployment Rate (Sep) Forecast: 15.4%, Prior: 14.2%
- Unemployment Rate (Sep) Forecast: 8.3%, Prior: 8.4%
- Michigan Consumer Sentiment Index (Sep) Forecast: 72.8, Prior: 78.9
- Factory Orders MoM (Aug) Forecast: 1.5%, Prior: 6.4%