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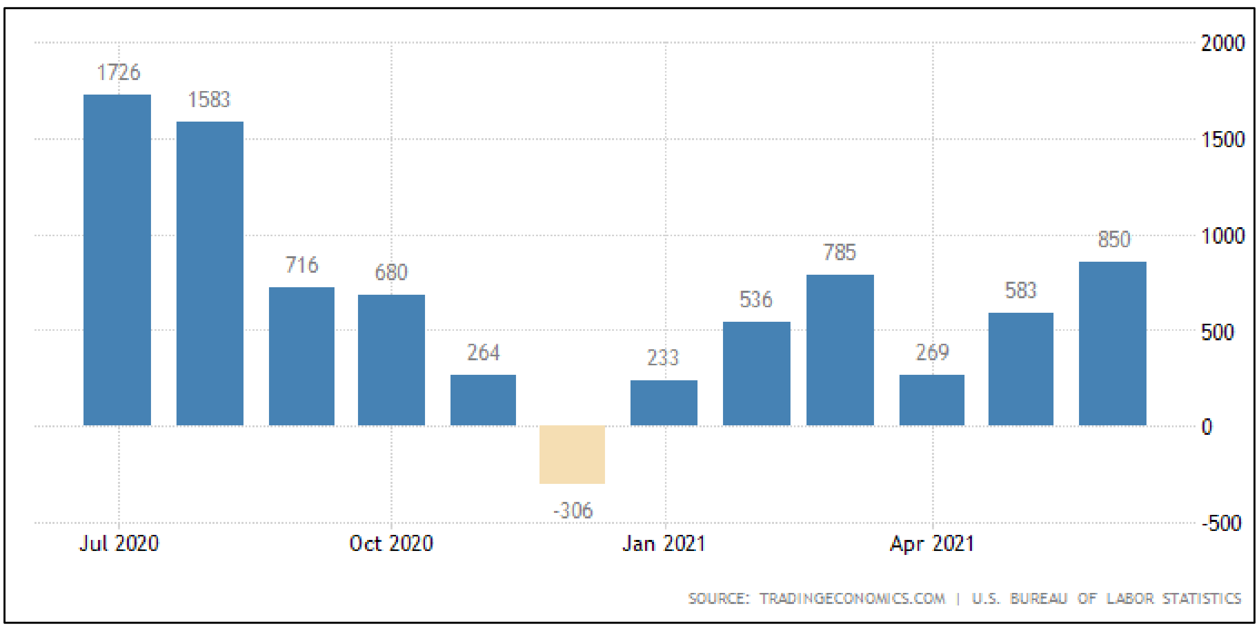
What to focus on in Global Macro for the week of July 5th, 2021

Macro Themes on the Radar:

Better than expected payroll data was partially counteracted by a slightly disappointing unemployment rate in the household survey. The record discrepancy between the surveys leaves plenty of room for doubt. Seasonal adjustments potentially continue to distort the labor market data, and the various labor supply constraints, including, increased/extended unemployment benefits, childcare problems, closed schools, Covid-19 fears, have continued to hold back the pace of the jobs recovery. At 850k this was the best jobs gain in 10 months.

Recent NFP prints:



The market saw the uptick in unemployment to 5.9% as an indicator that the Fed will continue to be patient and that September still looks like the earliest date for a taper announcement.

However, the unemployment rate edged up as more people voluntarily left their jobs and the number of job seekers increased. Not exactly signs of a weak underlying labor market.

In fact, this situation should still lead to major job creation in the coming months.

I would be more focused on the broader U-6 unemployment measure than the official U-3. While U-3 accounts for unemployed who are actively seeking a job, U-6 also includes underemployed and discouraged workers.

Unlike U-3, the U-6 measure fell meaningfully in June.

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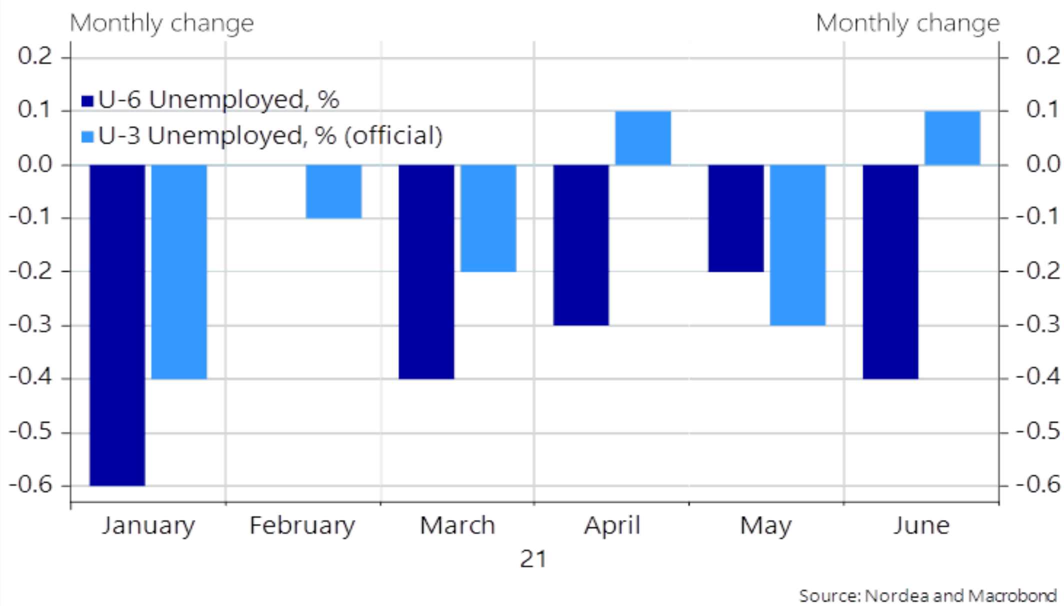
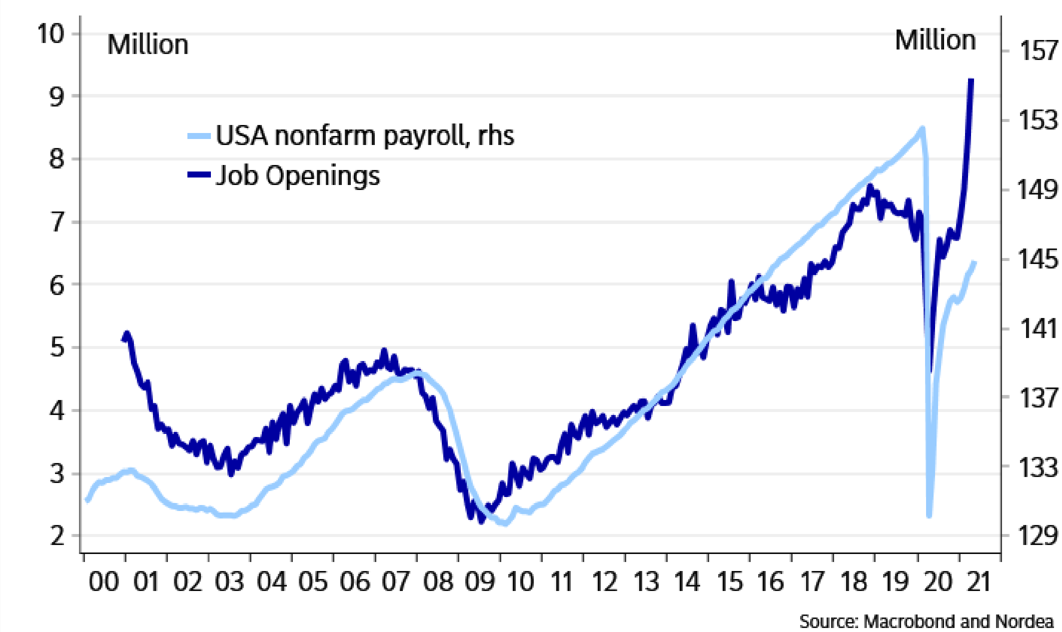
Chart 1. True unemployment dropped MARKEDLY in June despite the rise in the U3 measure

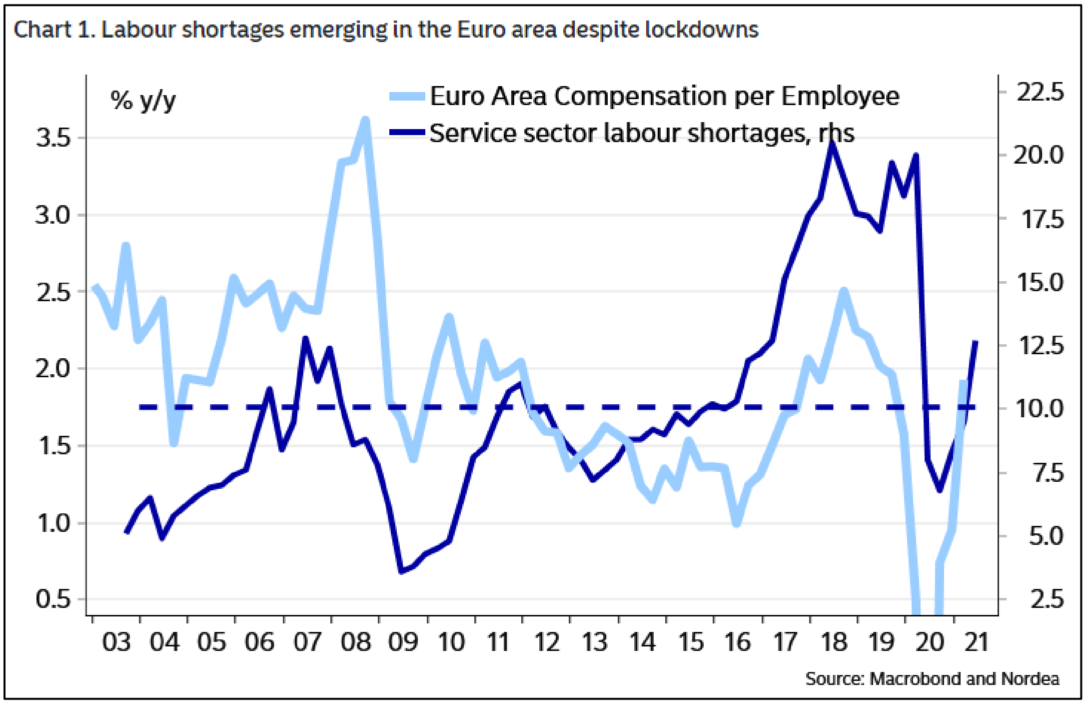


As the supply constraints fade and the labor markets clear, we should still see very good job gains in the coming months.

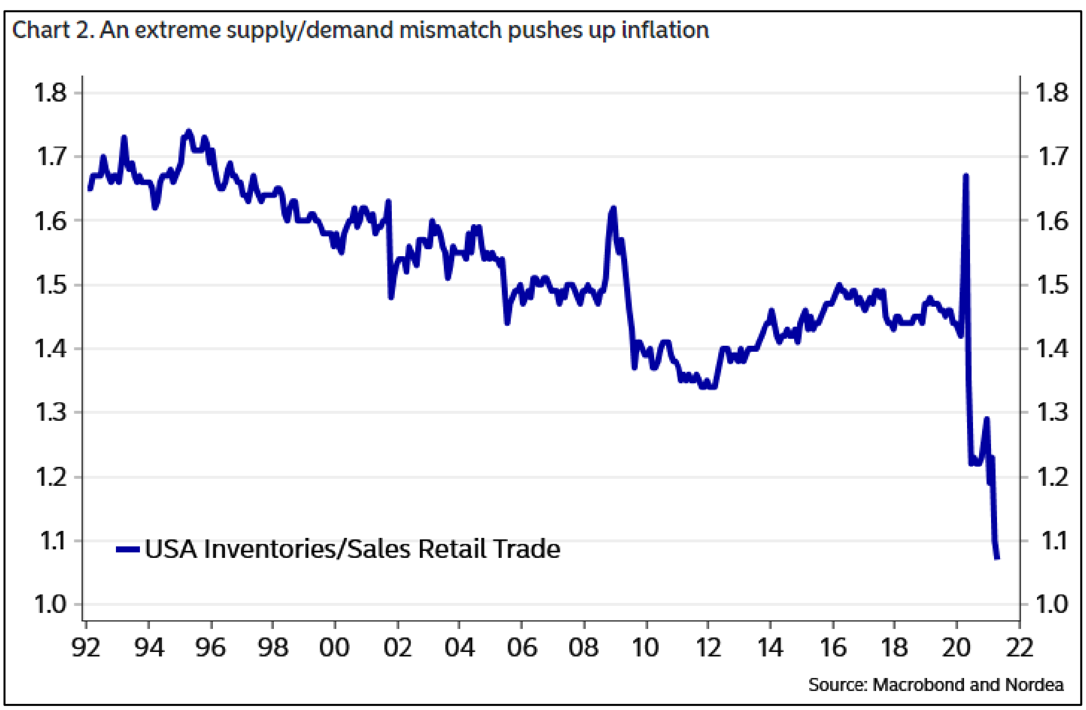
Chart 18. US job openings have surged massively to all-time highs



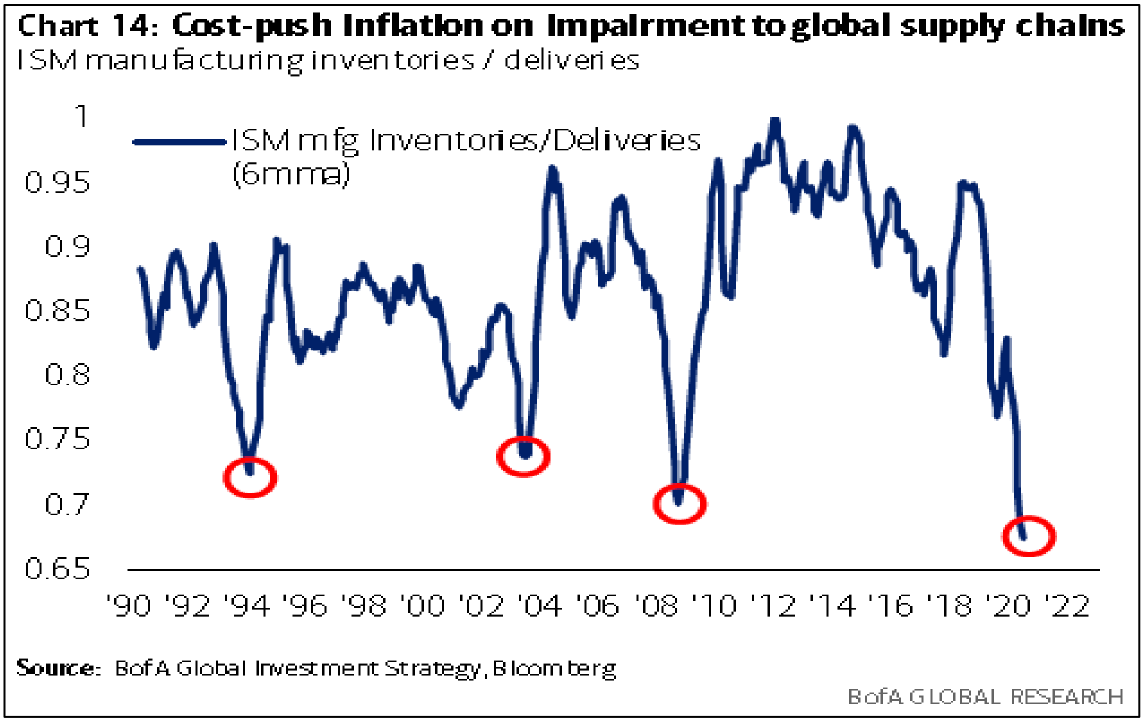
In the meantime, the supply/demand mismatch in labor markets continues to put upward pressure on wages in the near-term. One interesting phenomenon that is emerging is that COVID seems to have accelerated the move to retirement for baby boomers. It remains to be seen if they return or not when COVID subsides. In the meantime, it is worth noting that the labor shortages, with their multiple causes, are being seen internationally as well.



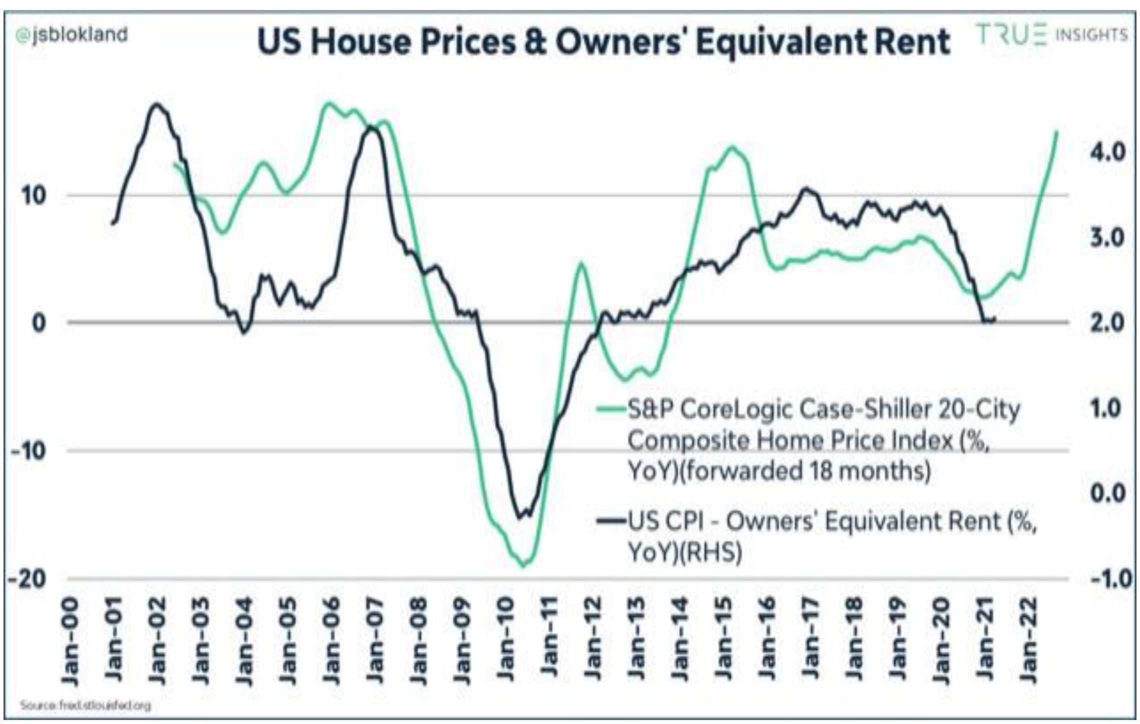
Add wage pressures to the widespread supply chain issues and bottlenecks and it should be no surprise that the inflation prints have even been impressing the Fed.



Seen another way…



They should settle back soon, but how much core comes back down before a new driver like rents kicks in, will be the big question for the Fed and for markets.

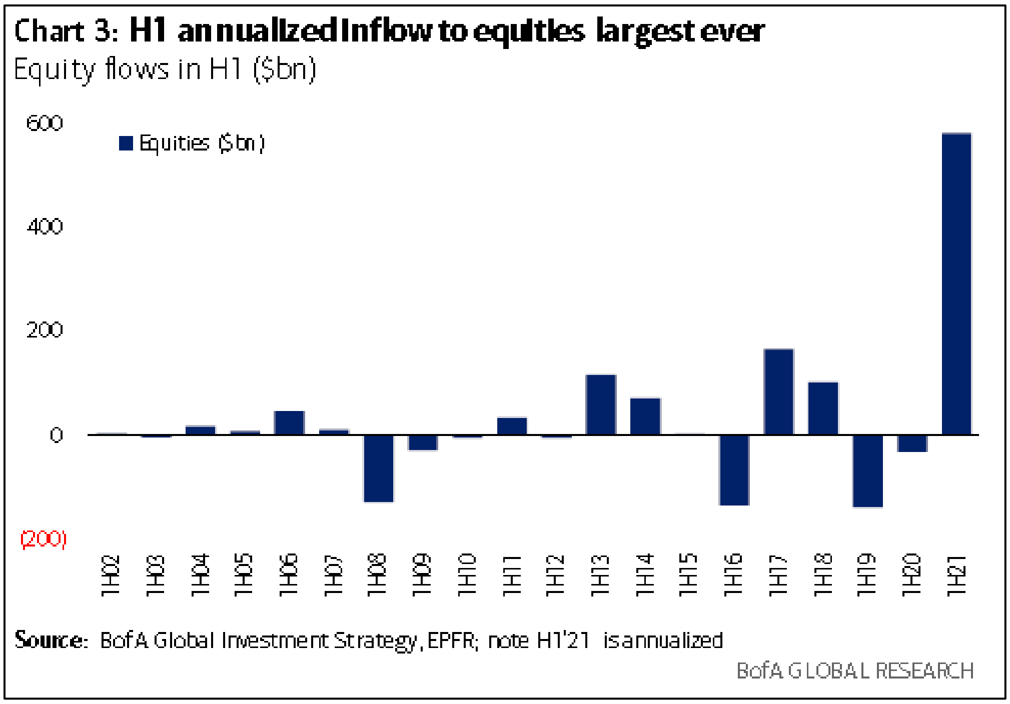


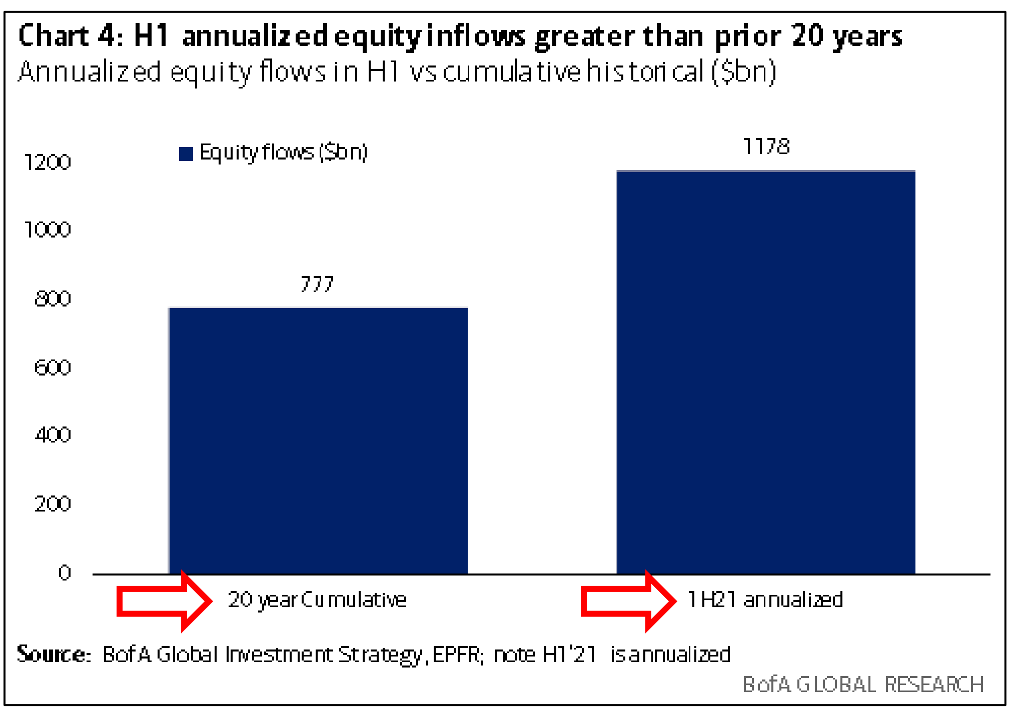
What to Focus on Now:

Equities

Some of the equity flow data is really amazing…

H1 2021 saw very large annualized flows indeed.

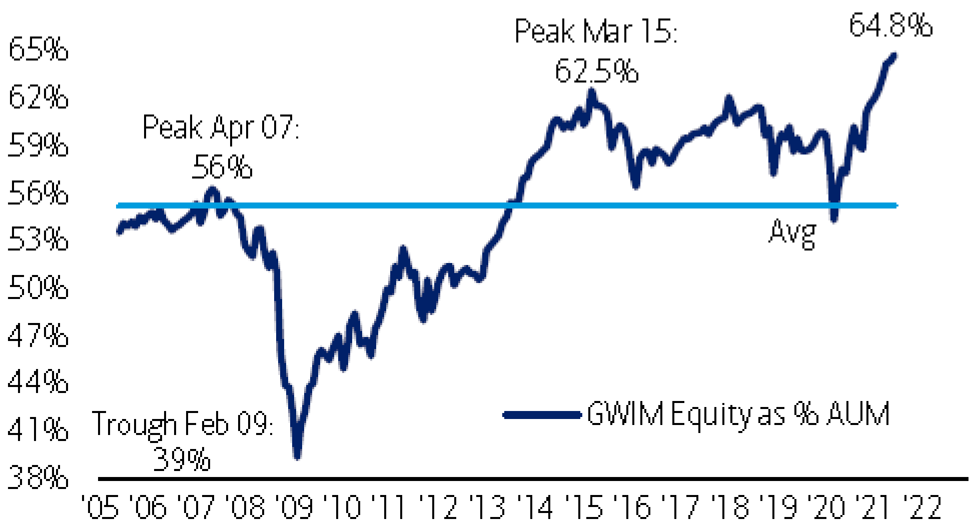




As a result, both institutional and private client positioning has continued to rise.

Chart 19: GWIM equity allocation at record 64.8%

BofA private client equity holdings as % of AUM



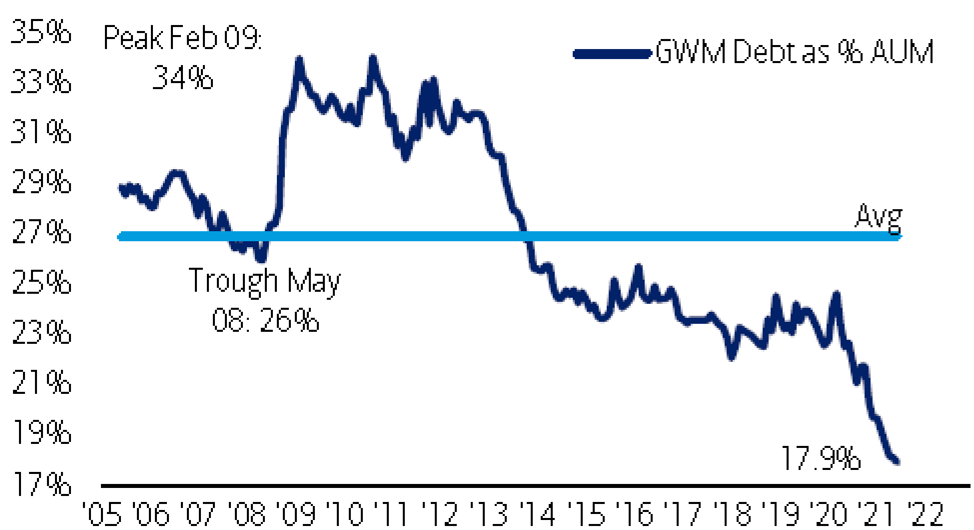
Source: BofA Global investment Strategy

BofA GLOBAL RESEARCH

TINA: Between inflation fears and stocks performing, investors don't like bonds.

Chart 20: GWIM debt allocation down to low at 17.9%

BofA private client debt holdings as % of AUM



Source: BofA Global investment Strategy

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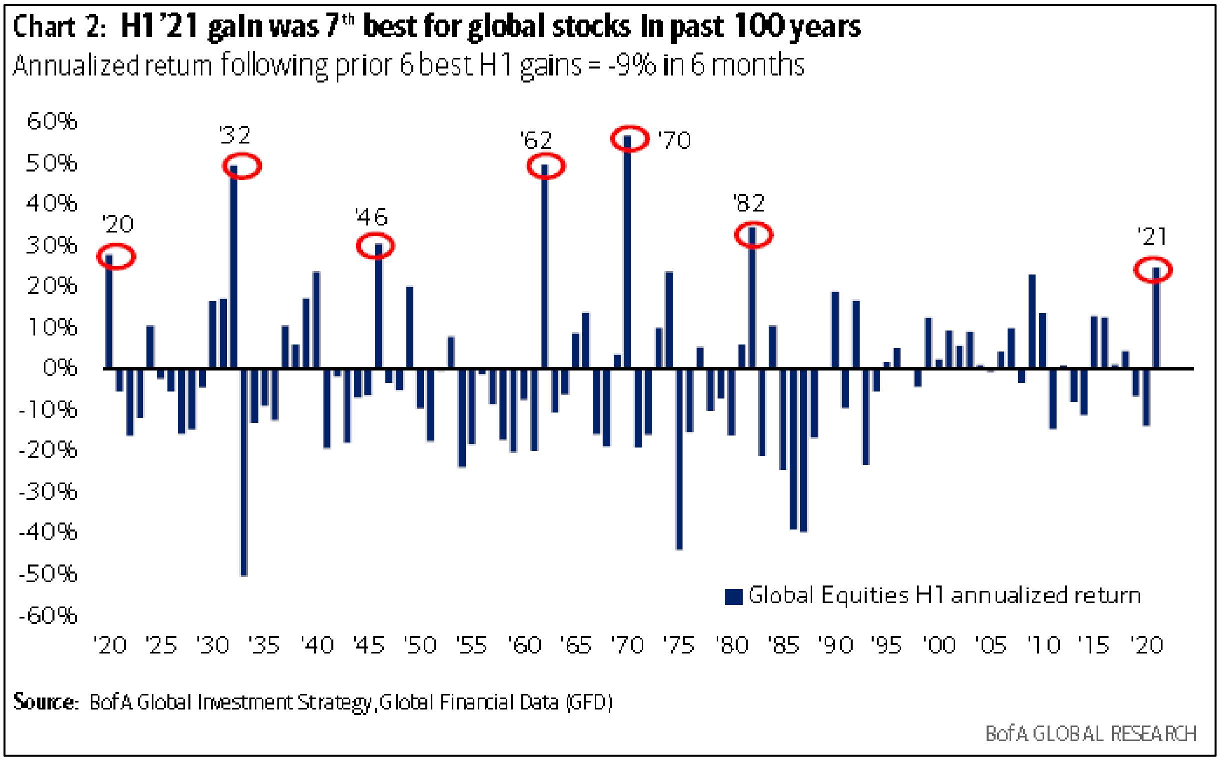
The equity allocation has paid off.



After a strong challenge from small caps and value stocks, the NDX and growth are back...

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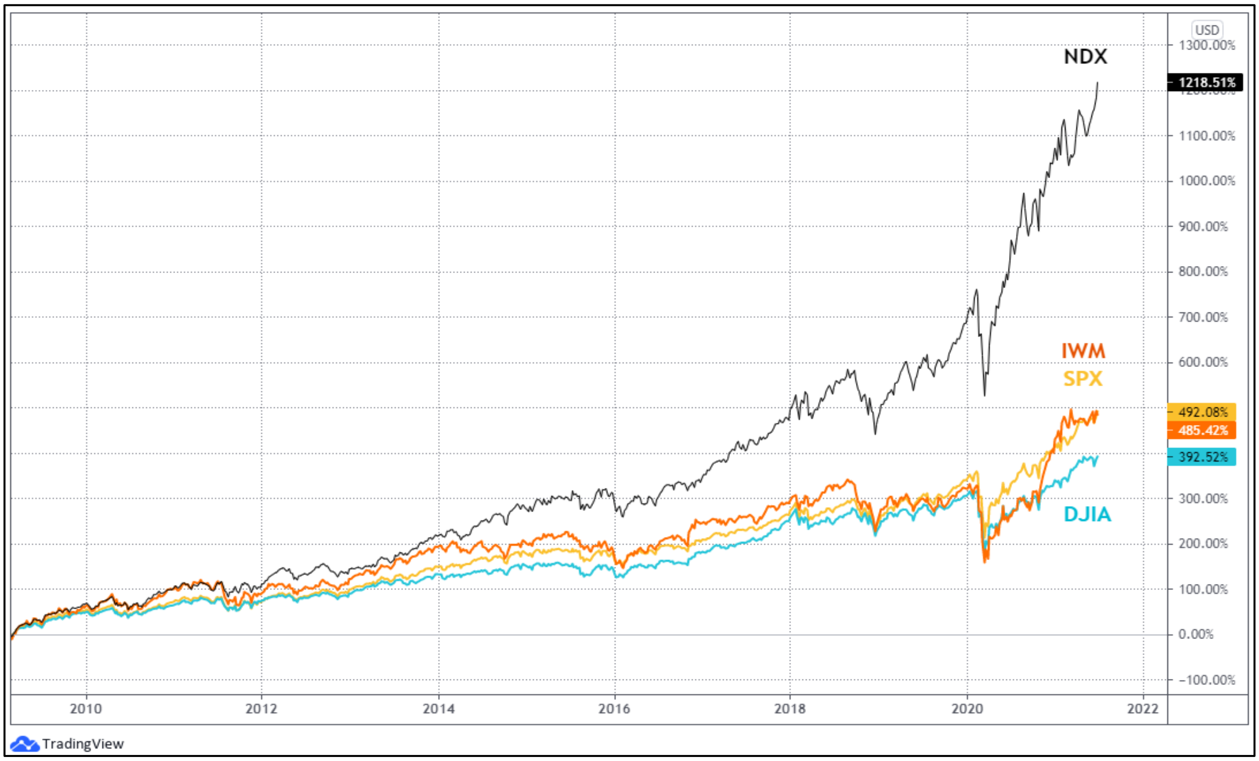
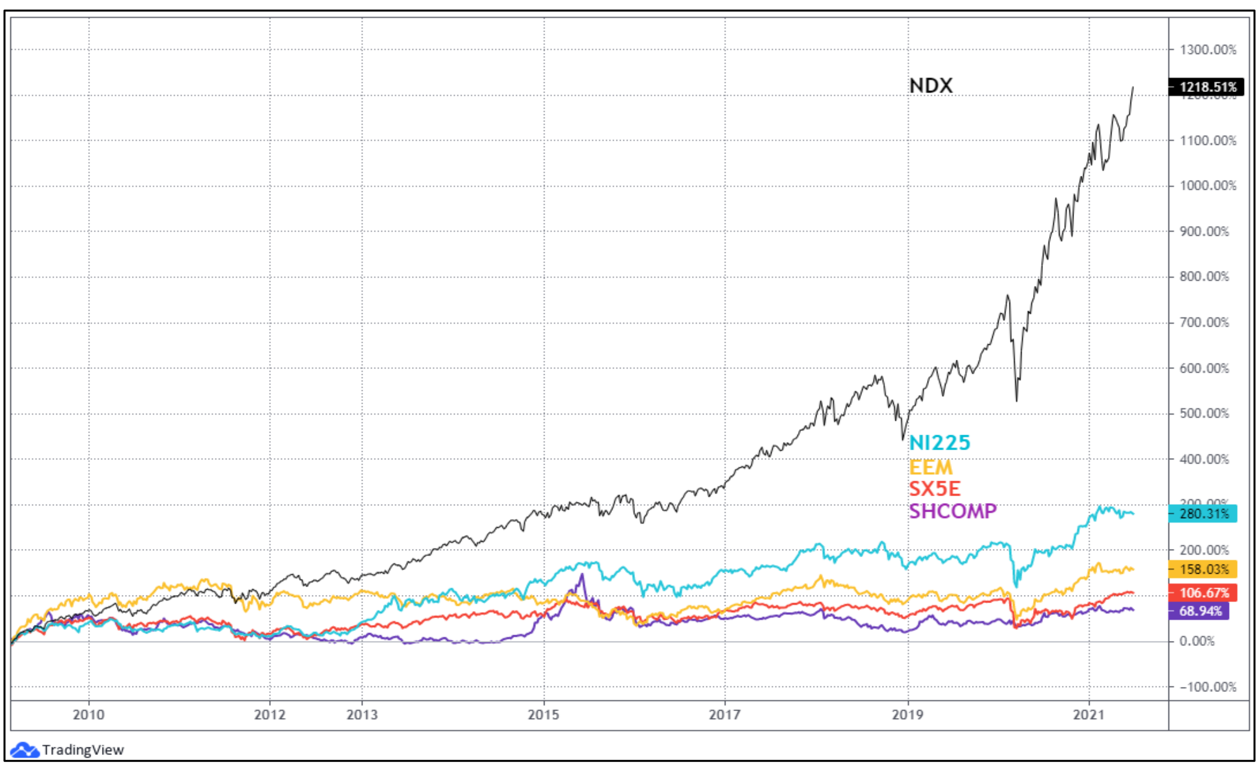
All the flow into value is now facing disappointment as growth threatens to break higher.

As discussed, the NDX pattern that we broke out of 10 days ago doesn't tend to result in a market that sits.

With this move, again outperforming most other indices, the NASDAQ is trying to regain its title as world leader and the primary driver of global equity market returns since the 2009 lows.





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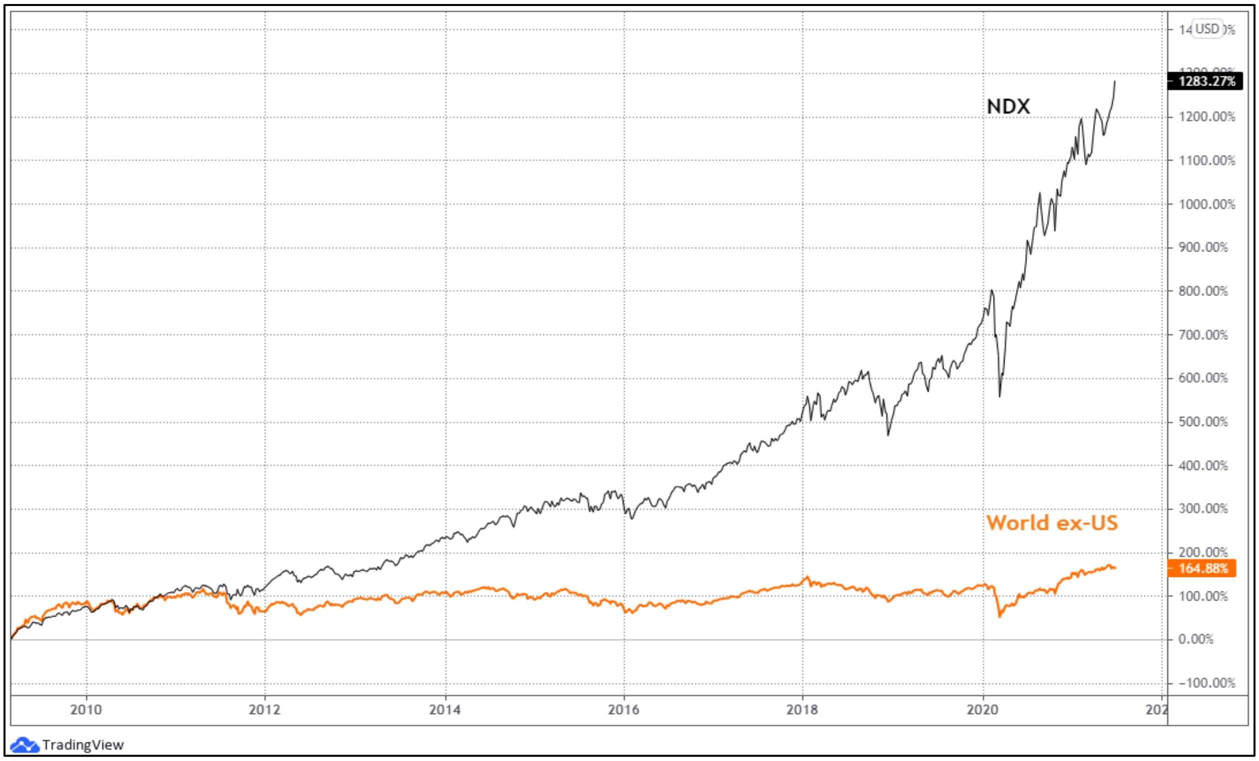
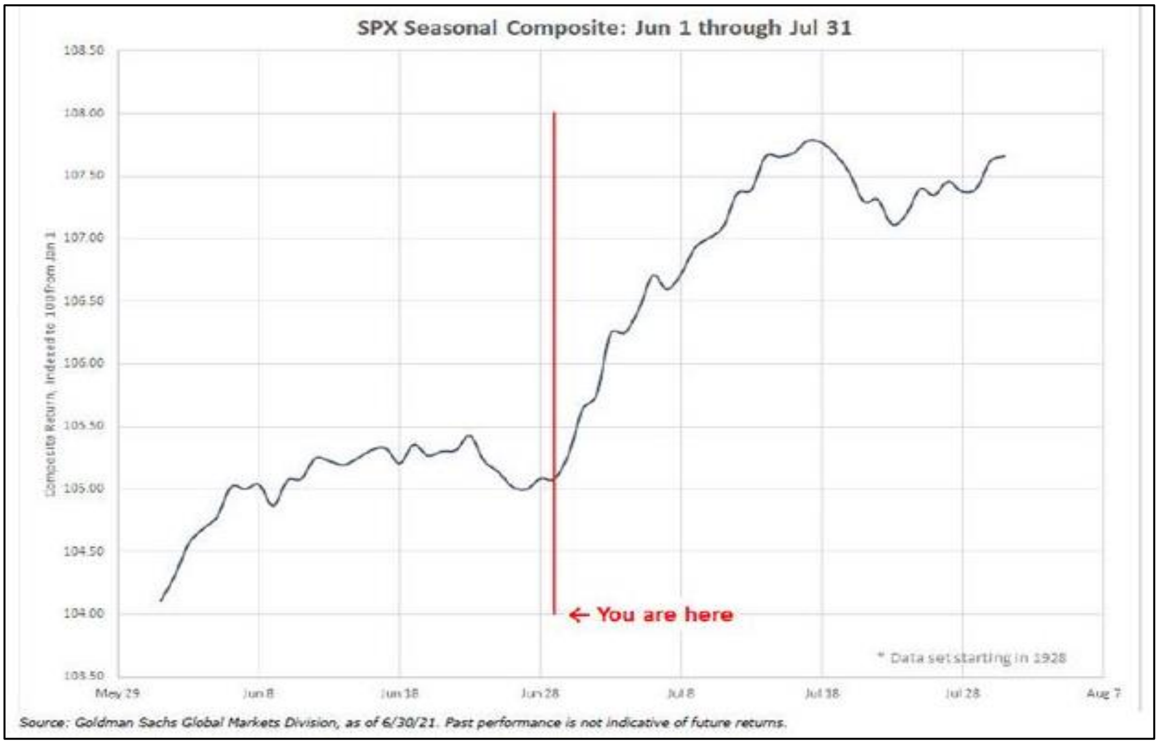
Or to make it simple...



And simpler still...

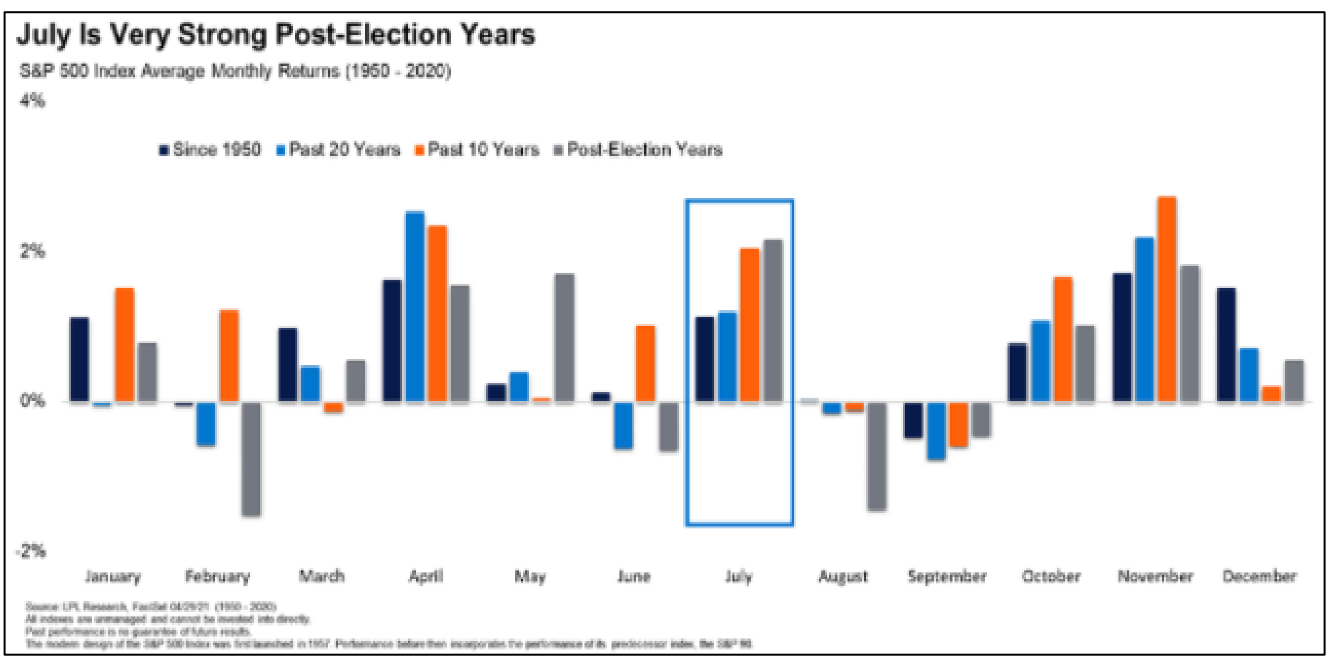
Now what? Historically July is a good month for stocks… although who knows if that type of comparison holds up in a COVID recovery world. This should certainly be taken with a grain of salt, but maybe there is a seasonal tailwind to be aware of.

Here is one from GS bases on data back to 1928…



Source: Goldman Sachs Global Markets Division, as of 6/30/21. Past performance is not indicative of future returns.

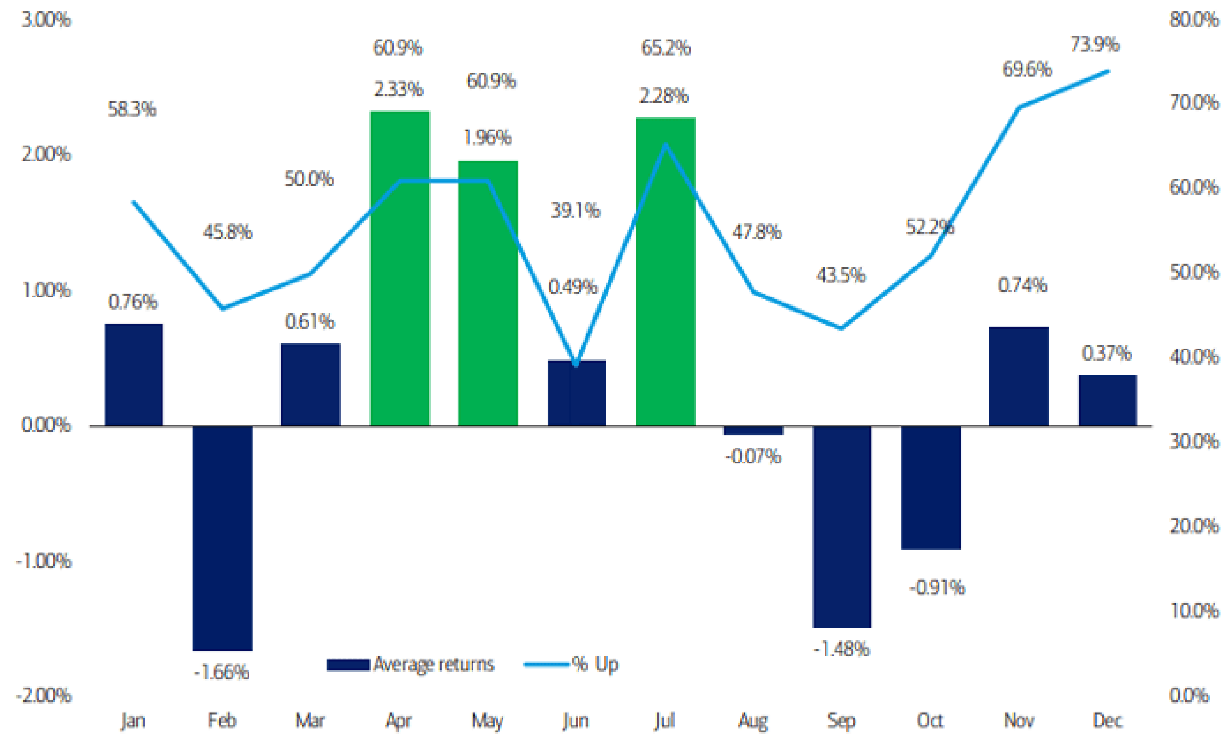
July at this point in the Presidential cycle is also being highlighted as bullish.



Source: LPL Research, FactSet 04/29/21 (1950 - 2020)
All indexes are unmanaged and cannot be invested into directly.
Past performance is no guarantee of future results.
The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

Chart 1: Monthly S&P 500 seasonality for Presidential Cycle Year 1

The S&P 500 has the highest average monthly returns for April, May and July during Presidential Cycle Year 1. This supports the case for a 2021 spring into summer rally.



Source: BofA Global Research, Bloomberg

Although, in the first two days of the month we have already booked over half of those average July gains.

EM and USD

EM needs to be watched here. Whether it is delta variant fear, concern about slower Chinese growth and credit supply, or general EM growth doubts, EM is underperforming. The recent USD strength is certainly not helping and if maintained will start to weigh on EM.

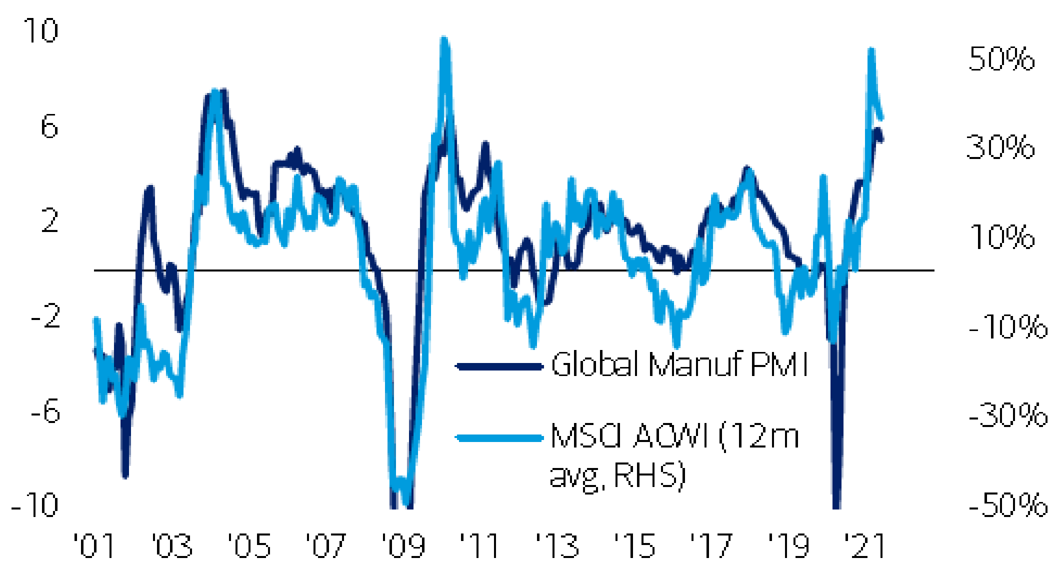
EM positioning is meaningful and has been seen as a reflation trade that would benefit not only from higher global growth, but also from a weaker USD and strong commodity prices.

However, while EM has rallied, it hasn't been able to keep pace with the US, or even Europe.

Now there are some signs that the underperformance is accelerating.

Global manufacturing PMI's have had a great run but are potentially starting to peak. That doesn't necessarily have to be a bad sign for the global economy as it could be due to the service sector taking over or short-term supply chain issues that are holding back production.

Chart 15: Peaking PMI's…
Global manufacturing PMI vs MSCI ACWI (12m avg)



Source: BofA Global Investment Strategy, Bloomberg

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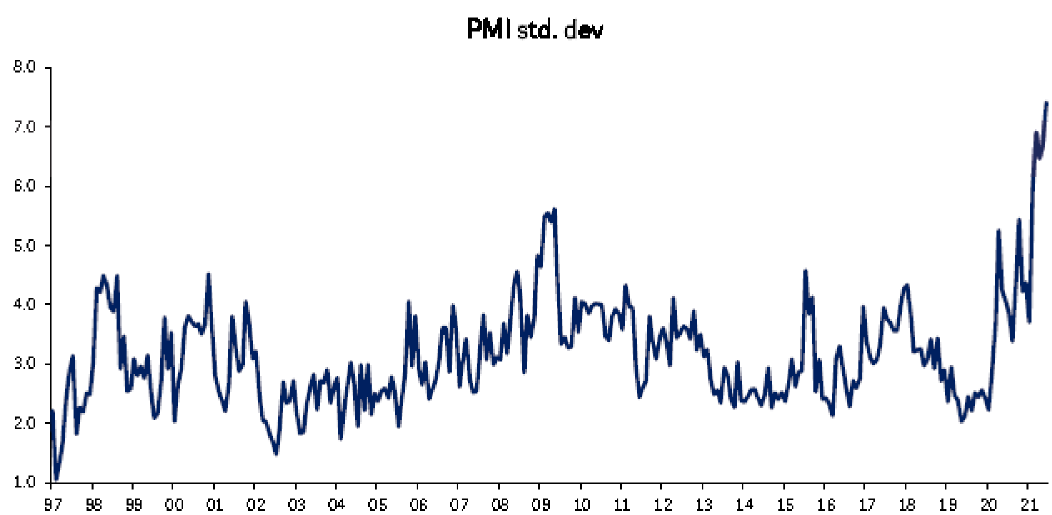
However, there is a growing divergence between DM and EM PMI's.

Figure 1: PMIs deviation - Growth is mostly positive but the PMI variation across countries is unusually high, with a schism between DM and EM. The global cycle is becoming less and less synchronized.



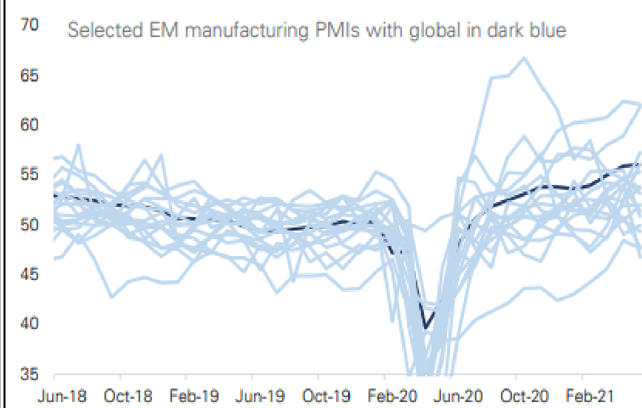
Source: Deutsche Bank, IHS Markit, Datastream.

EM is lagging. Again, is it just the lag in the distribution of vaccinations?

Figure 5: The global composite PMI improvement is entirely being driven by developed markets

Source : Deutsche Bank, Haver Analytics

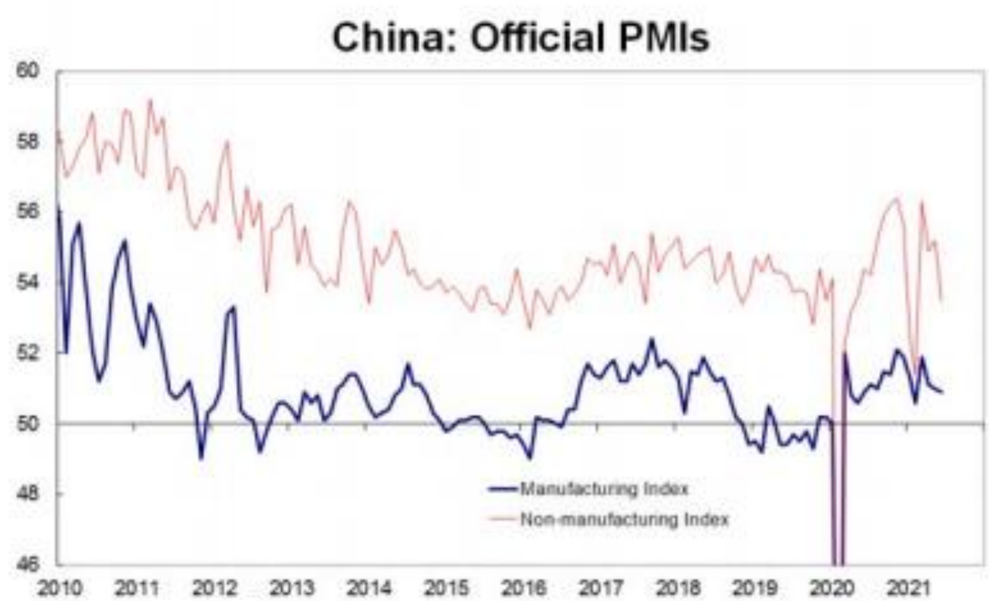
Figure 6: And most EM manufacturing PMIs now running well behind the global one



Source : Deutsche Bank, Haver Analytics

Or, the softer than anticipated data from China? It is hard to know at this point.

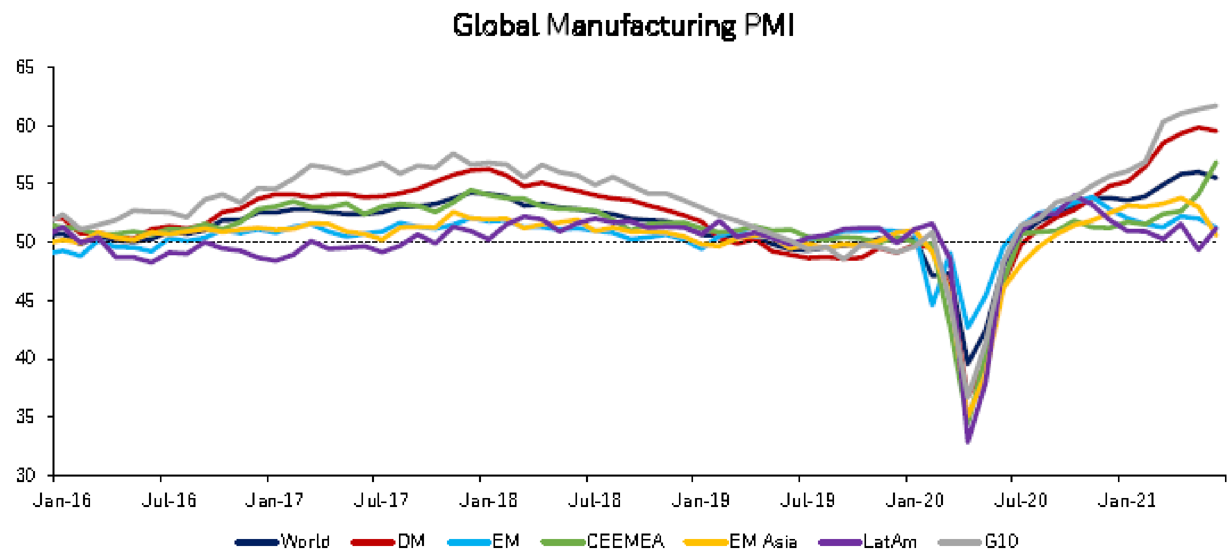
Figure 4: China non-mfg PMI missed in June



Source : Deutsche Bank, Bloomberg Finance, L.P.

Those could well be the drivers, and if they are, they should be temporary, and EM should regain its footing.

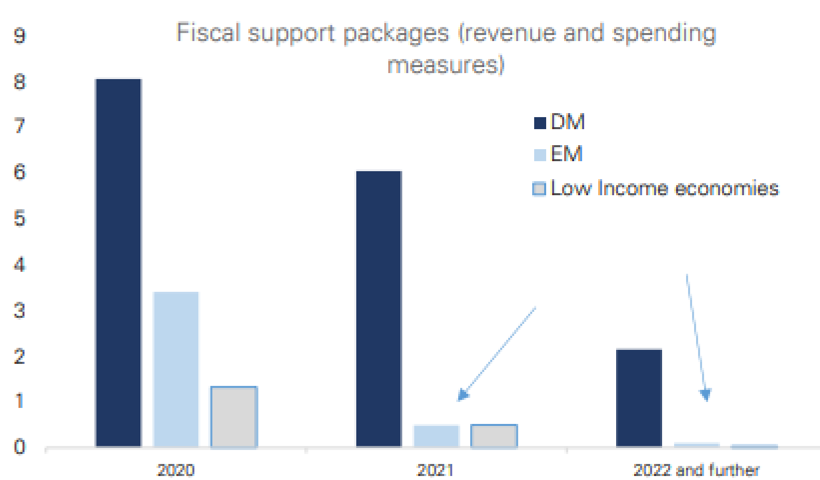
Figure 13:Global Manufacturing PMI - G10 far in the lead, helped by vaccine optimism; EM Asia and Latam lag.



Source :Deutsche Bank, IHS Markit, Datastream.

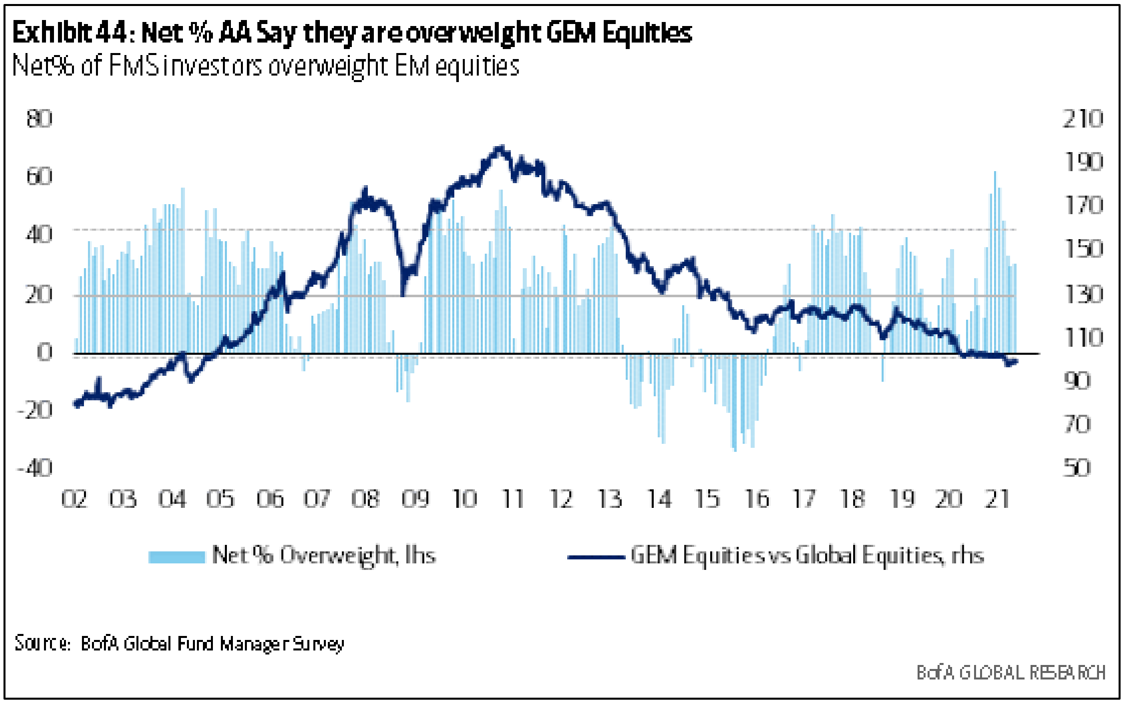
However, there are potentially other drivers as well.

Figure 9: Fiscal support in EM set to evaporate this year

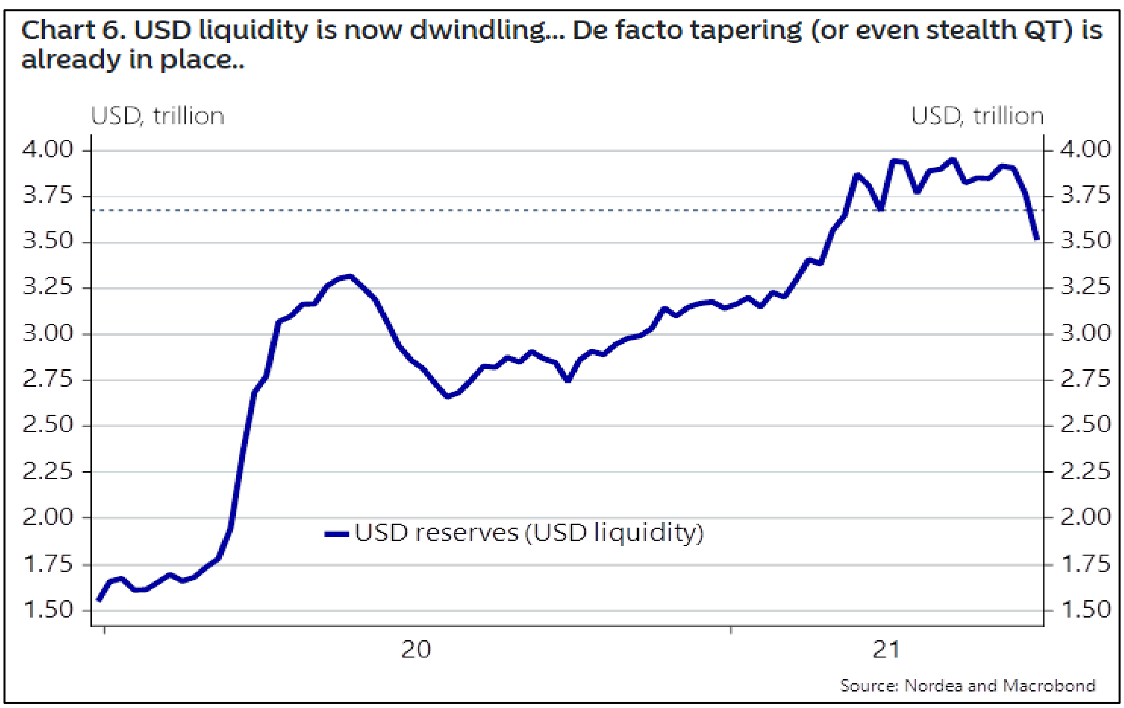


Source : IMF April Fiscal Monitor

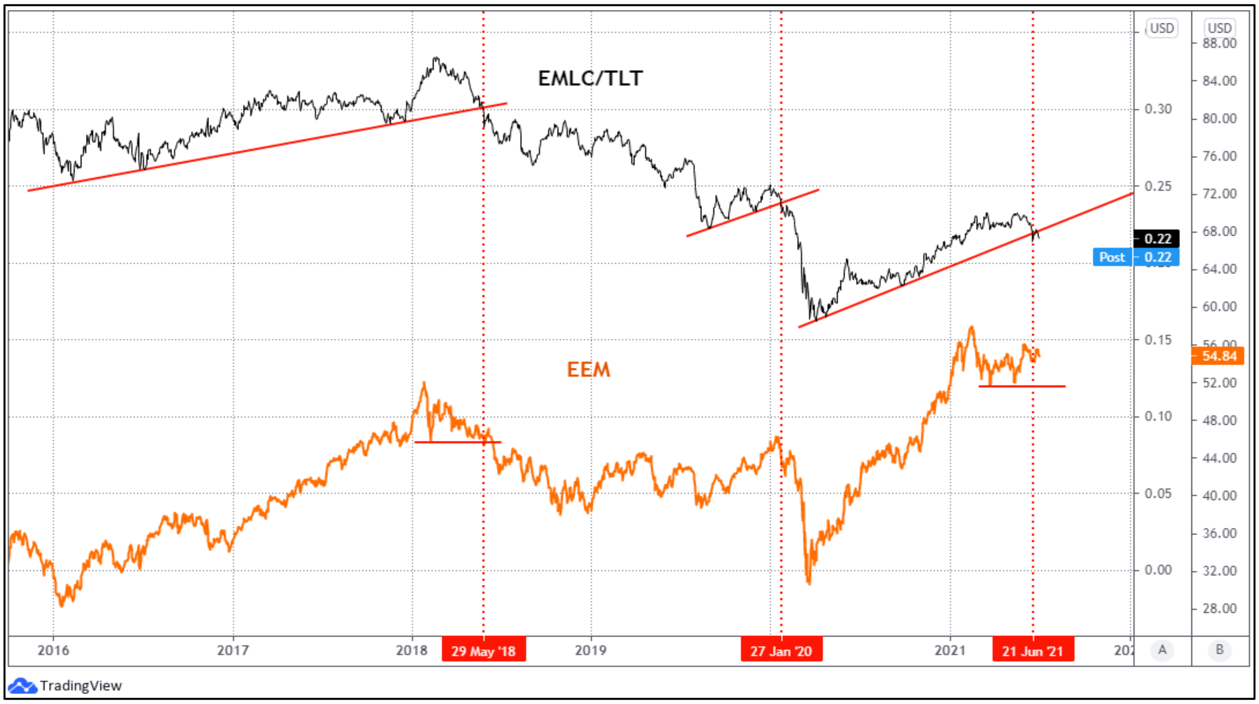
In any case, positioning and the recent strength in the USD means some caution is required.



Some are arguing that even without ongoing QE, US-provided liquidity is already peaking as the liquidity mopping up operations by the Fed in the front end are effectively tapering QE. I'm not sure I fully buy into that, but it is something to consider as the dollar is key for EM here.



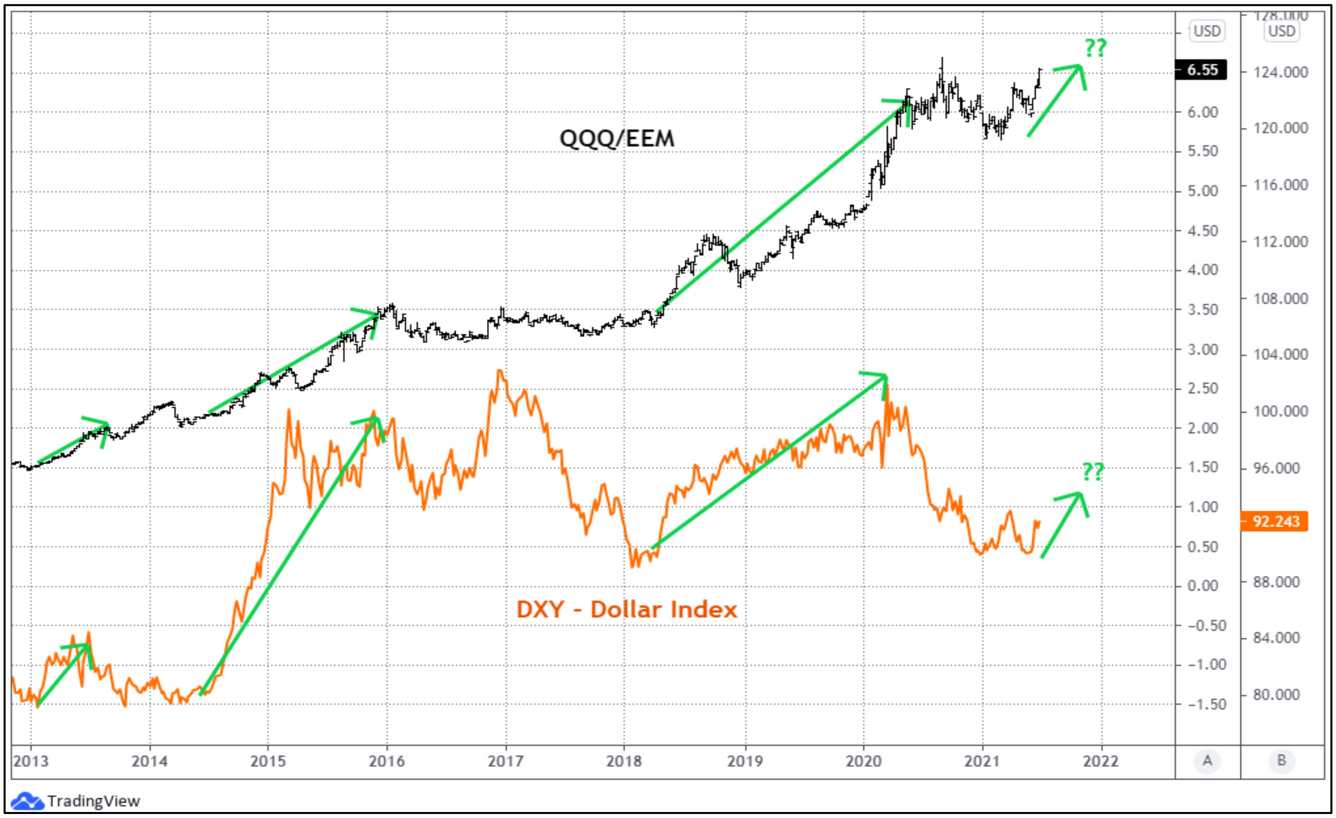
Some price relationships are starting to flash amber. Watch EM local currency bonds on a relative basis. Recent breaks, like we are seeing now, have been a warning sign for EM equities.



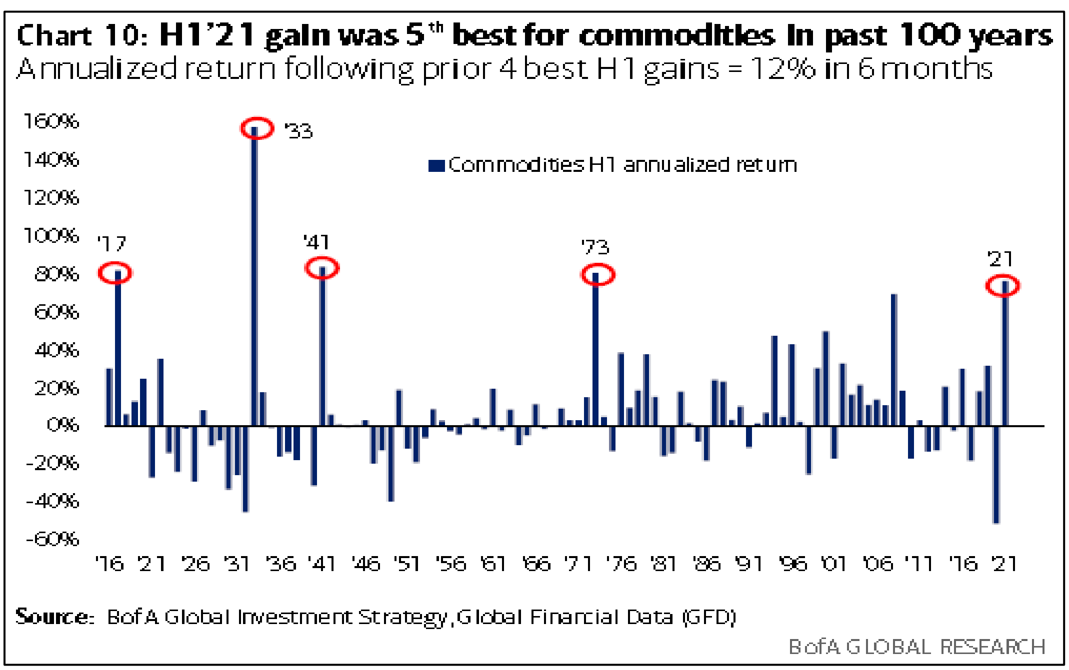
A further USD rally now would not help. In 2018, the move down in EM raised volatility generally.

In some ways, EM underperformance is an expression of a global switch back to growth from value.

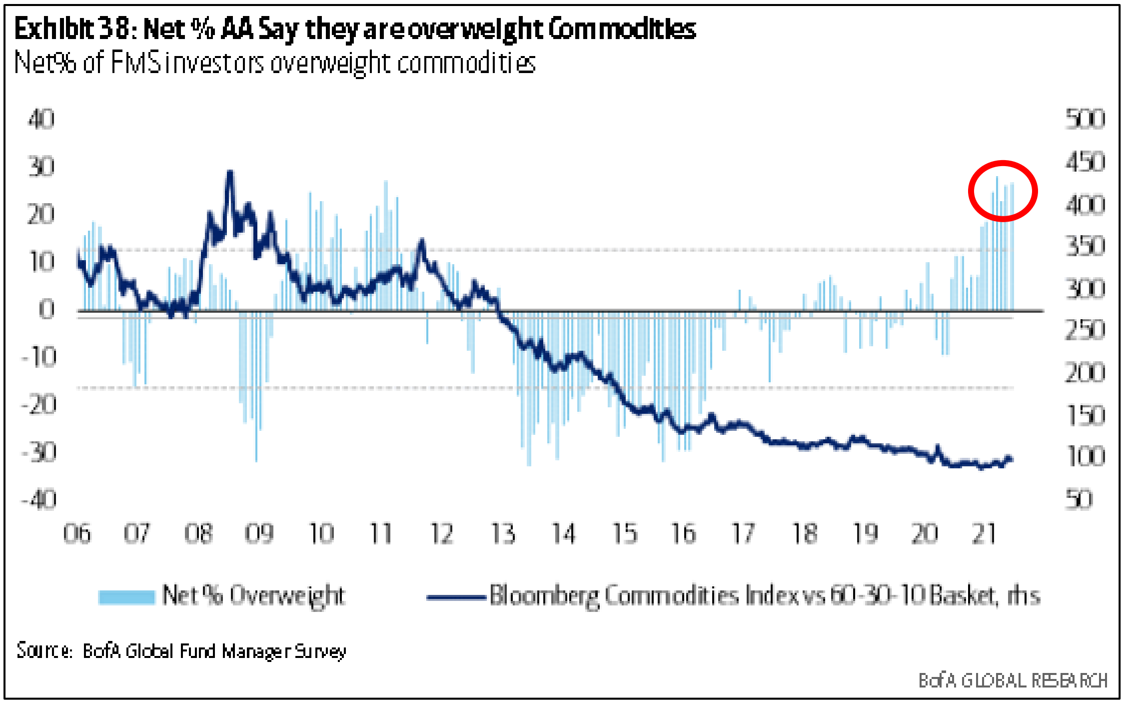
We tend to get strong NDX outperformance vs. EM when the dollar rallies. I suppose we could easily debate whether this is a case of chicken or the egg, but once it gets going, it becomes self-reinforcing.



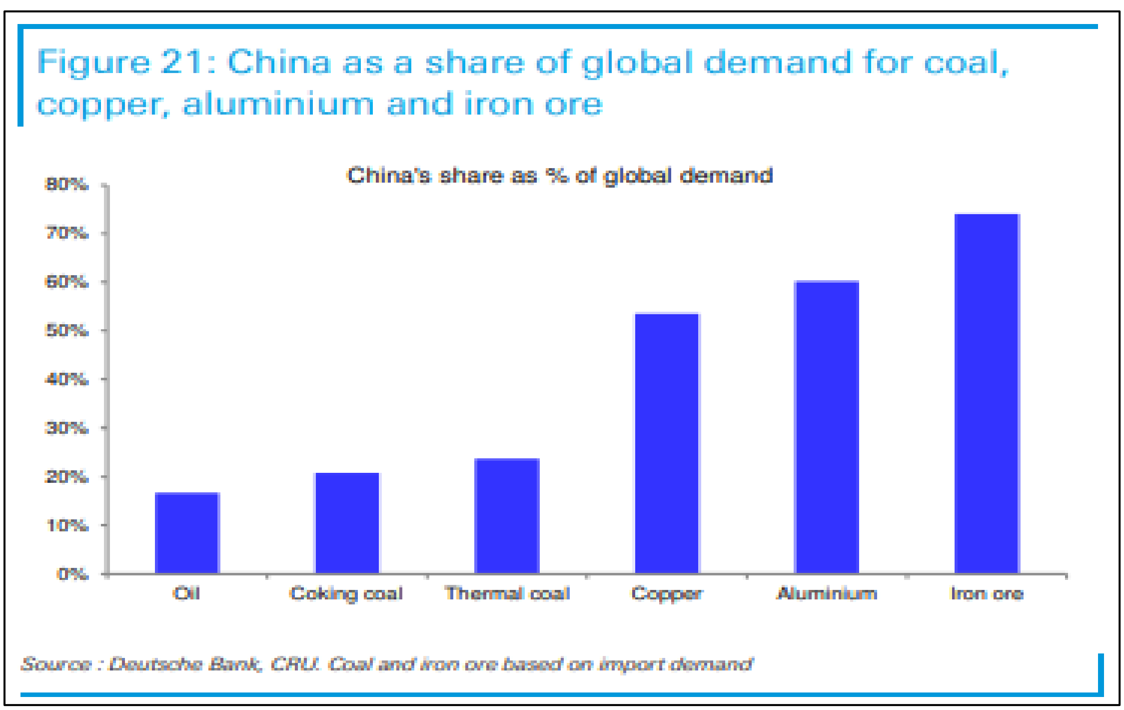
Commodities - They have obviously had a great run in 2021. It has been a tag team event, with industrial metals, softs, and oil, all contributing.



Between the inflation narrative, bottlenecks, and a soft USD, investors have piled in.



So far, so good. China has been trying to dampen down the move recently, and some commodities have run out of steam, at least for now. Again, EM and the USD are key to watch here. A strengthening dollar would make it very hard for a lasting commodity super-cycle to take hold. China is especially important for the industrial metals.



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Important Macro Data Releases and Events for the Week

There is an important meeting next Friday in Venice, Italy. It will consist of G20 finance ministers and central bank governors. One of the topics is sure to be the ongoing OECD negotiations on reforming the global corporate tax system, which, 130 countries and jurisdictions have signed on to. The agreement would see companies pay more taxes in the jurisdictions they operate in, and a global minimum corporate tax rate.

Monday
7/5/2021

- Markit PMI's across Europe

Tuesday
7/6/2021

- RBA Interest Rate Decision and Statement
- ZEW Survey - Economic Sentiment (Jul) Forecast: 84.4, Prior: 81.3
- Retail Sales YoY Forecast: 7.9%, Prior: 23.9%
- **Markit Service and Composite PMI's**
- **ISM Service PMI (Jun) Forecast: 63.5, Prior: 64**

Wednesday
7/7/2021

- European Commission releases Economic Growth Forecast
- **FOMC Minutes**
- Fed Monetary Policy Report

Thursday
7/8/2021

- ECB Special Strategy Meeting
- Initial Jobless Claims Forecast: -, Prior: 364k
- Initial Jobless Claims 4-week average Forecast: -, Prior: 392.75k
- Continuing Jobless Claims -, Prior: 3.469M
- Consumer Price Index YoY (Jun) Forecast: 1.4%, Prior: 1.3%

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Friday
7/8/2021

Employment Data (Jun)

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