Stargazer
Asset Management

What to focus on in Global Macro for the week of February 15th, 2021

Macro Themes on the Radar:

Last week was an interesting one regarding the inflation debate and monetary/fiscal policy.

Powell's speech at the Economic Club of New York last Wednesday, can only be seen as dovish. He hammered home the Fed's concerns regarding continued high unemployment and called for a national effort to improve the employment picture. He also reiterated that under the Fed's new framework they won't be looking at tightening labor markets as a harbinger of future inflation. Instead, they will wait to see actual and, in this case, persistent inflation before changing policy. Opportunistic reflation, rather than the opportunistic disinflation as practiced in the 80's and early 90's. He pushed back on the idea that more fiscal spending now could overheat the economy.

With monetary policy seemingly stuck at zero for the moment, the debate around fiscal policy and how much might be too much, has been heating up. Larry Summers, the former Treasury secretary, National Economic Council director, and Harvard president, recently wrote an op-ed in the Washington Post arguing that the size of the $1.9 trl Biden rescue plan is too big and risks igniting inflationary pressures and eventually a Fed response that could take us back into recession. On Friday, Princeton University sponsored a debate between Summers and the Economics Nobel laureate Paul Krugman. Krugman had recently written his own op-ed in the NYT arguing that the package was appropriately sized and justifiable, given the damage done to the economy.

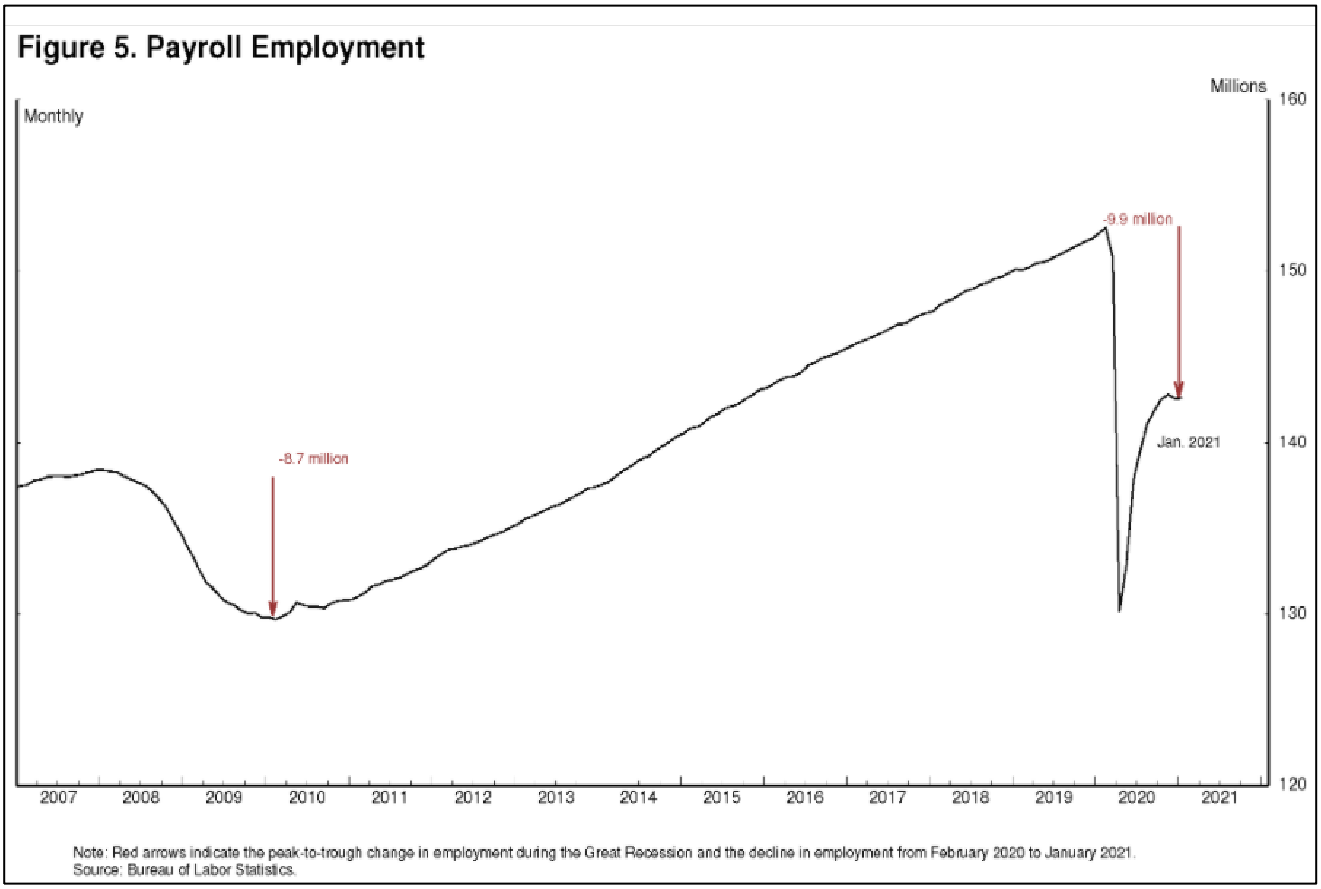
This debate is going on all over the country, and arguably across the globe. With no inflation or bond vigilantes around constraining the ability to continue borrowing and spending, and the US political set-up enabling further action, fiscal spending is set to continue. Will inflation spoil the party? The two camps…

Reasons to expect higher inflation include:

- Massive money supply growth.
- Expected further weakening of the USD.
- Rising commodity prices.
- Supply-bottlenecks.
- Peak supply of cheap global labor.
- Globalization is being challenged.
- Only palatable way out of huge global debt is to inflate.
- Policy makers will continue fiscal spending until they are constrained from doing so.

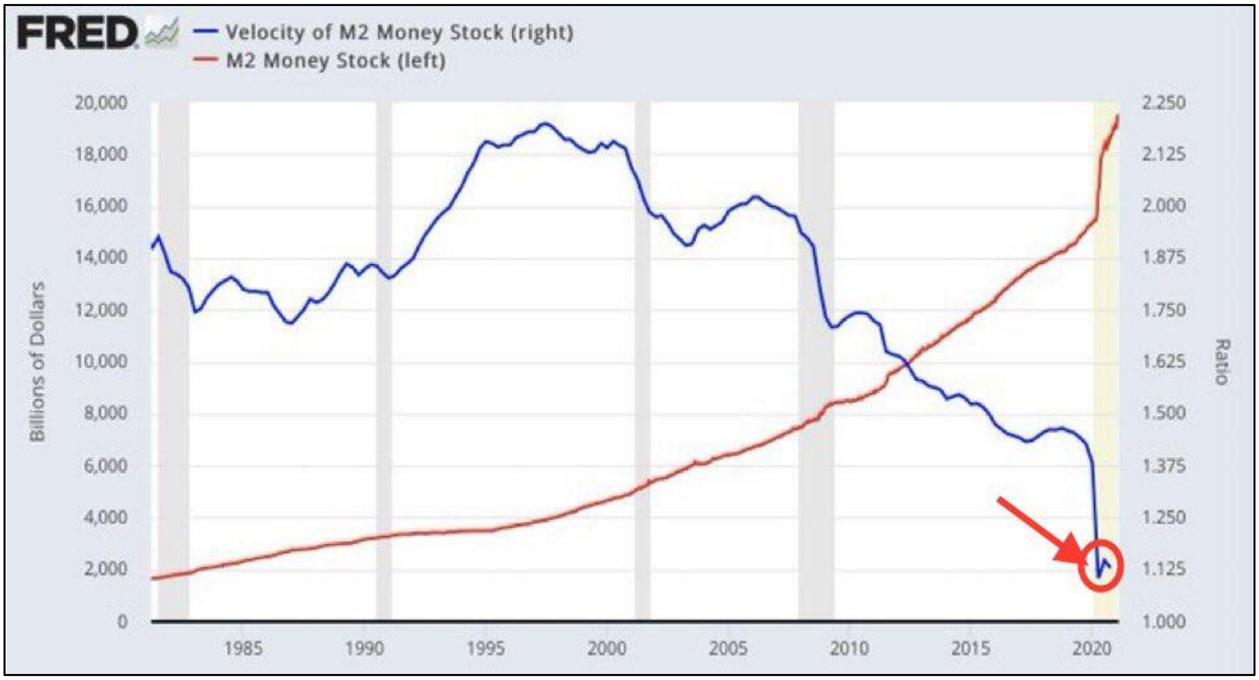
Reasons for thinking inflation will be slow to develop include:

- Positive output gaps and 3.5% unemployment have not been enough to produce inflation in pre-COVID world.
- Fiscal spending is just filling a huge economic hole from COVID.
- While M2 has exploded, the velocity of money has plunged and so far, not recovered.
- Supply-side bottlenecks are temporary.
- An expected jump in reflation from impending post-vaccine reopenings will be temporary. (All the CB's are going to use this to look through any initial jump in inflation)
- A rise in prices without a rise in wages will act as a tax on consumers. Only tight labor markets will generate lasting higher inflation.
- Broadest measures still show very high level of US unemployment.

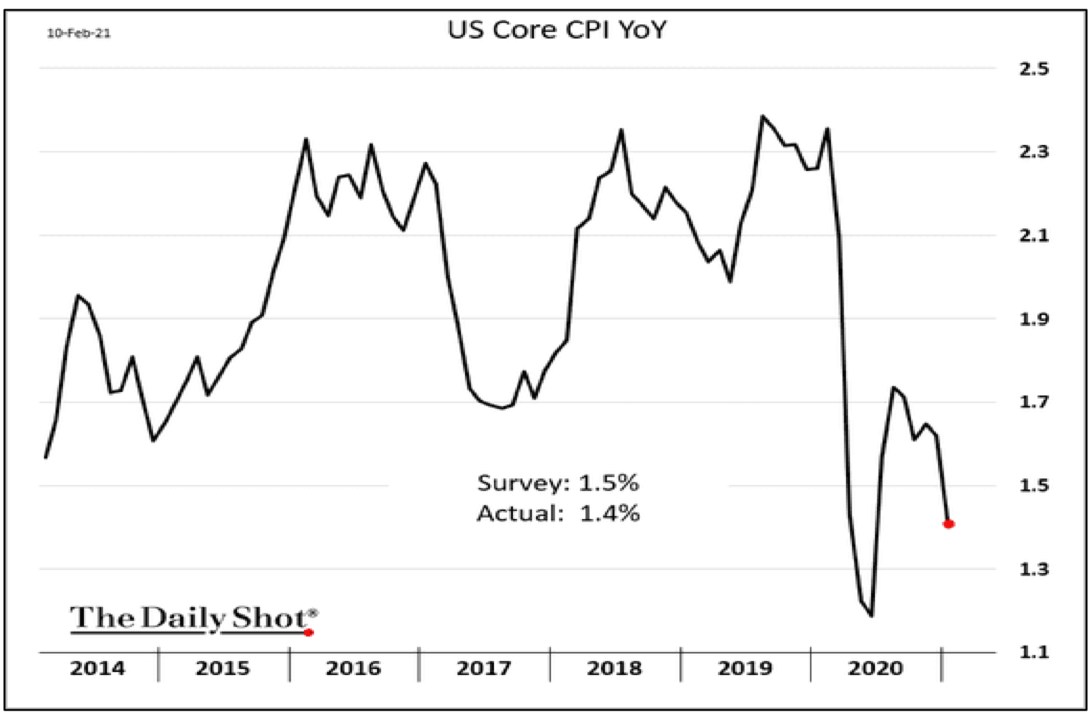


Source: Charts from Powell speech at EC of NY

I would expect the velocity of money to pick up as the economy fully reopens. While it is a lagging indicator, it will be worth watching for confirmation.



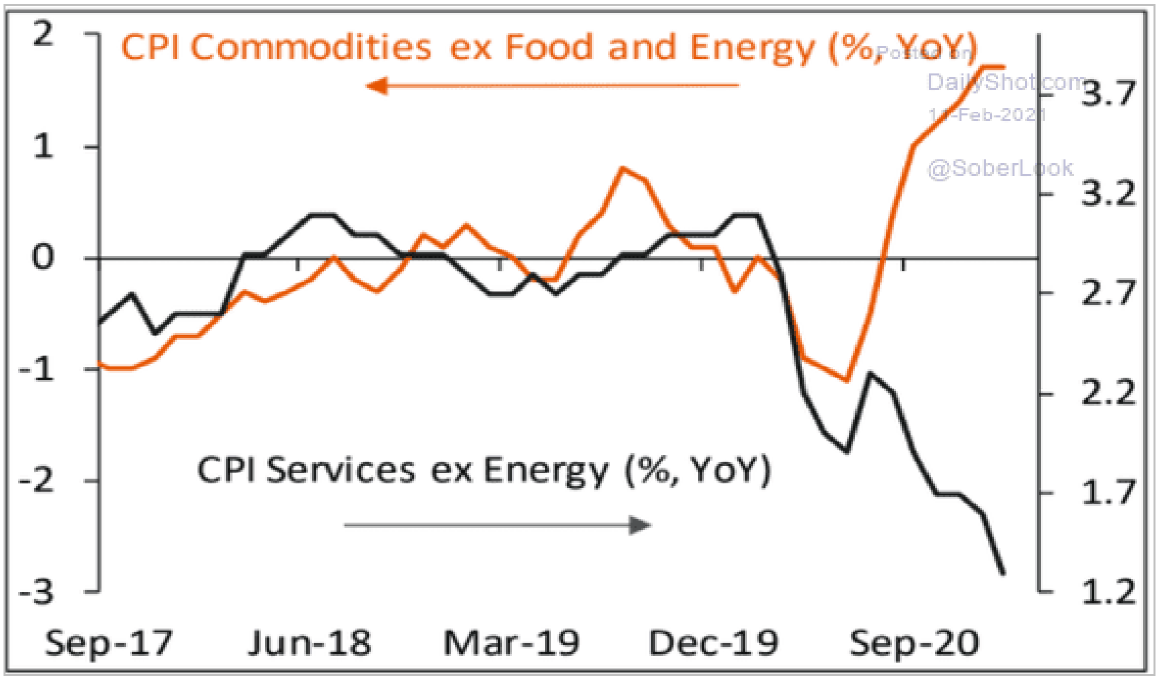
The most recent inflation print came in below expectations...



However, COVID continues to very much muddy the water ...

Services remain a drag on core CPI.

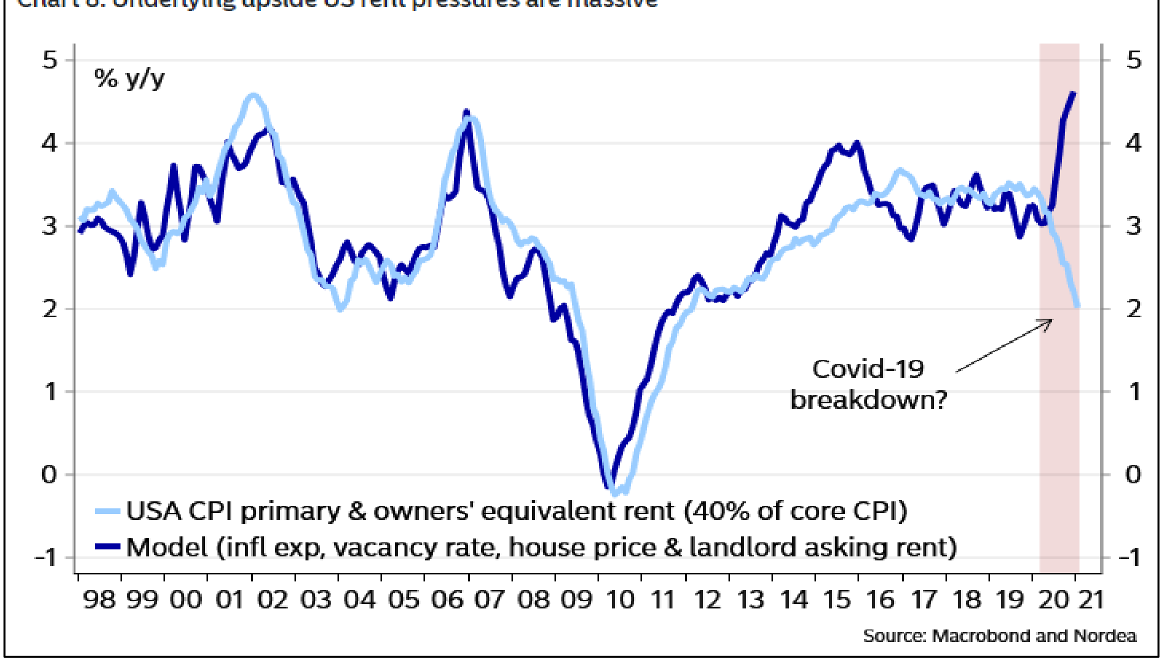
As illustrated with the pandemic-related divergence below.



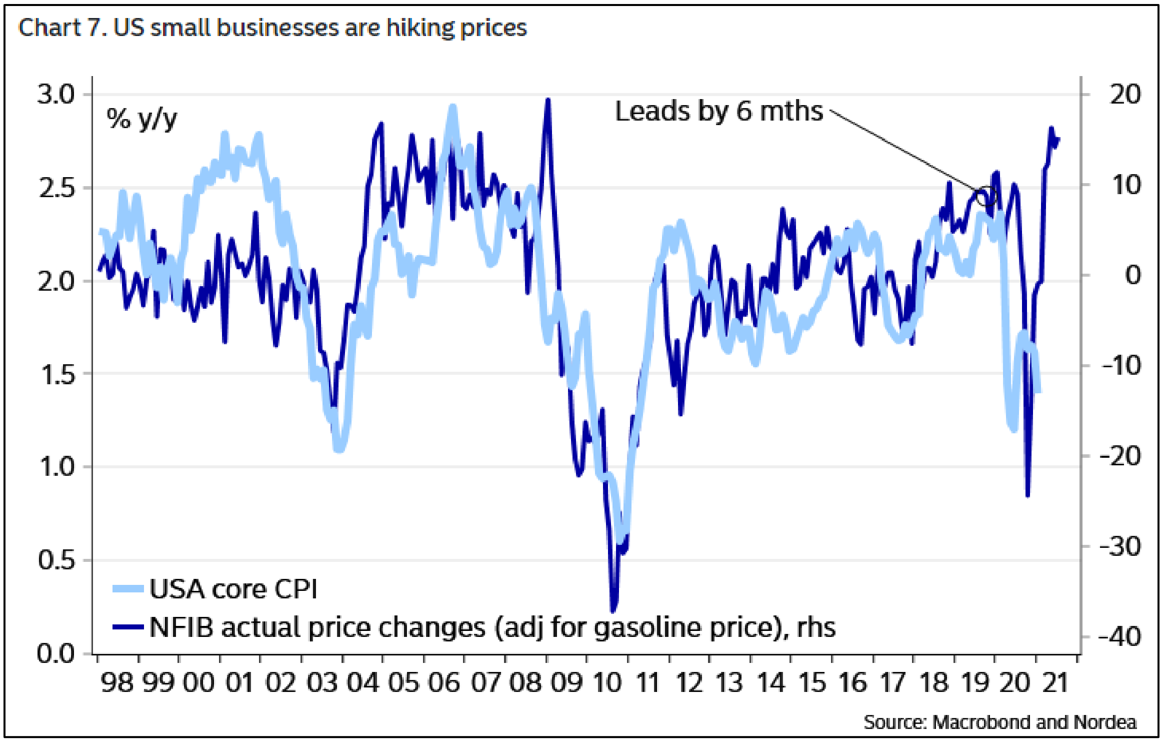
Source: Piper Sandler

The "shelter" component which has a 42% weight in core CPI has been weak. However, there are plenty of signs of building pressure that could soon reverse this component's downward pressure on CPI. Apartment vacancy rates have been falling and are now near record lows. At the same time house prices have been jumping and landlords are signaling large increases in asking prices for rents.

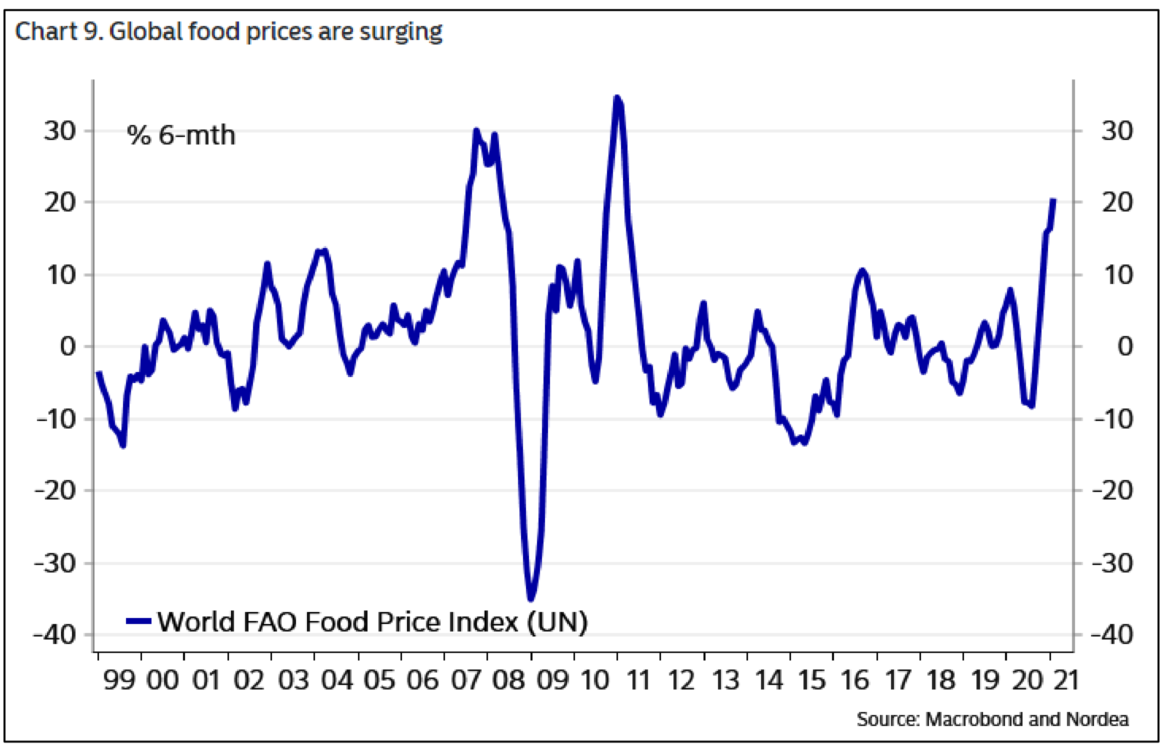
Chart 8. Underlying upside US rent pressures are massive



At the same time, US small businesses are planning on and raising prices…



And food prices are surging. As discussed, the big open question remains how much of all this is temporary?



What to Focus on Now:

Another week, another record for equity inflows.

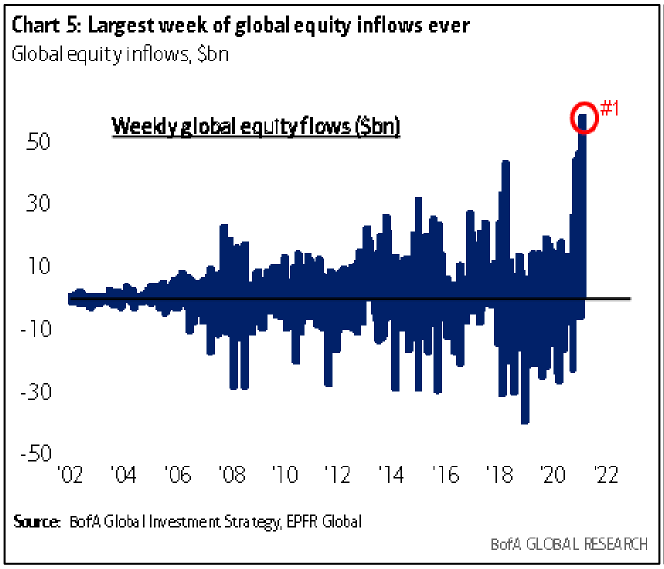


Chart 5: Largest week of global equity inflows ever
Global equity inflows, $bn
Source: BofA Global Investment Strategy, EPFR Global
BofA GLOBAL RESEARCH

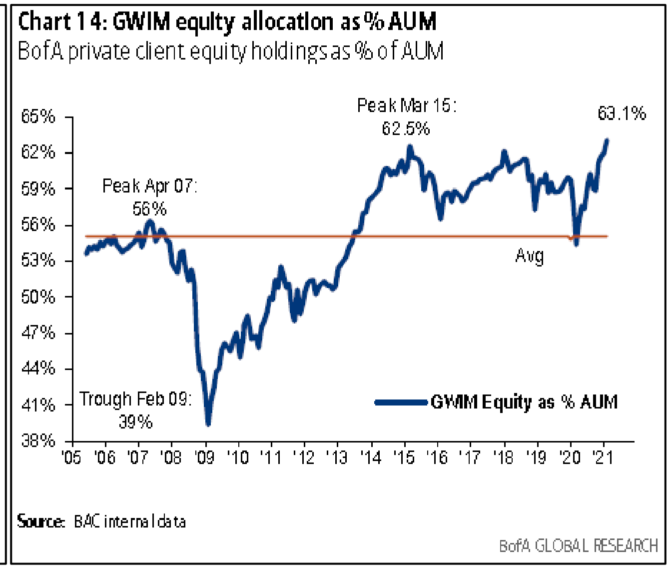


Chart 14: GWIM equity allocation as % AUM
BofA private client equity holdings as % of AUM
Source: BAC internal data
BofA GLOBAL RESEARCH

Positioning is high for individual and institutional investors, but not yet at extremes it seems. Sentiment indicators are also stretched, but not yet at "flashing red" extremes.

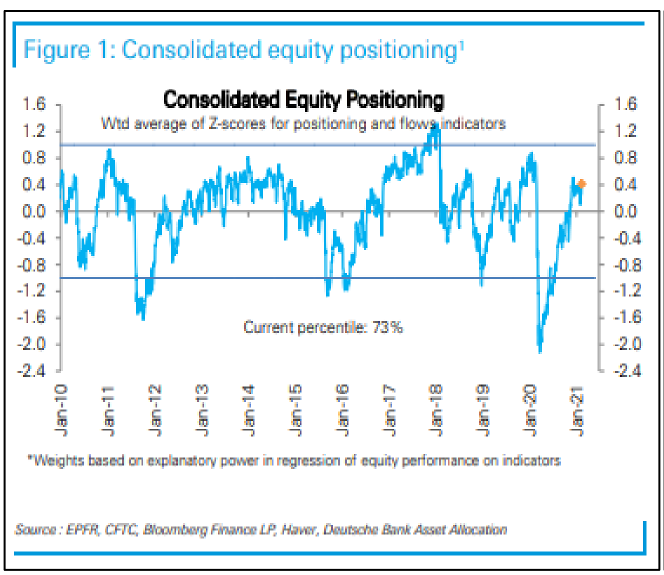


Figure 1: Consolidated equity positioning[1]
*Weights based on explanatory power in regression of equity performance on indicators
Source : EPFR, CFTC, Bloomberg Finance LP, Haver, Deutsche Bank Asset Allocation

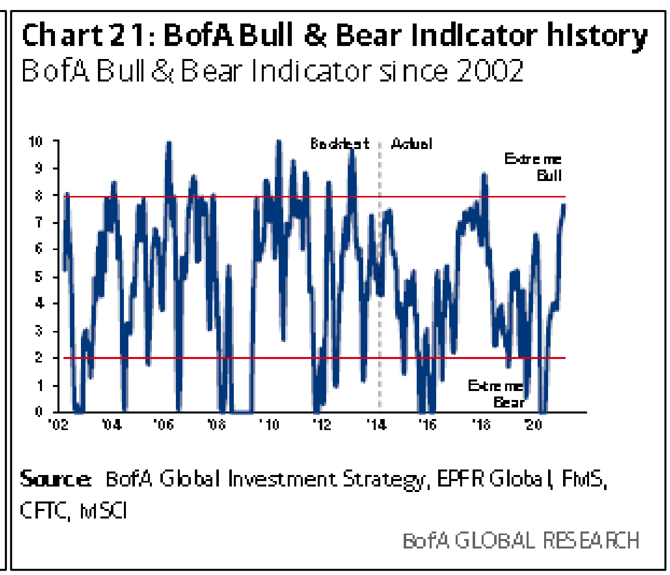
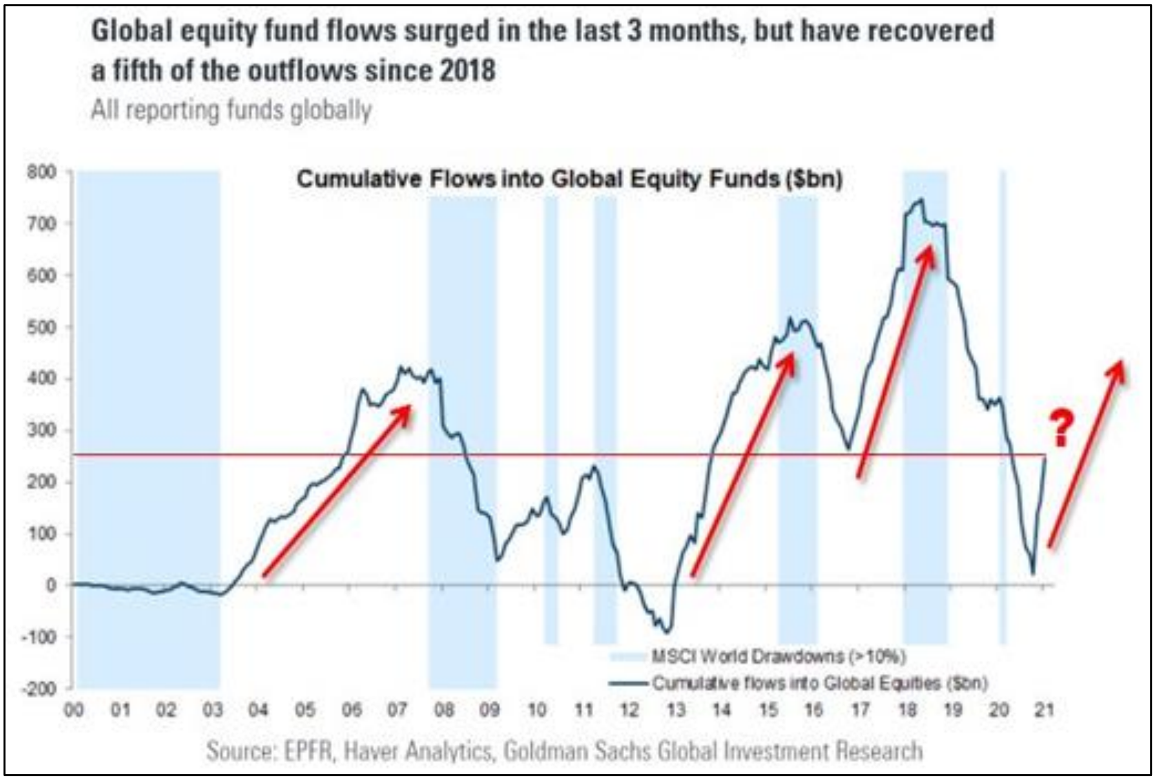


Chart 21: BofA Bull & Bear Indicator history
BofA Bull & Bear Indicator since 2002
Source: BofA Global Investment Strategy, EPFR Global, FMS, CFTC, MSCI
BofA GLOBAL RESEARCH

I thought the following chart from GS was interesting.

It looks at cumulative equity flows. By this metric there would still be plenty of room for more equity inflows.



There are lots of bubbly signs out there for sure:

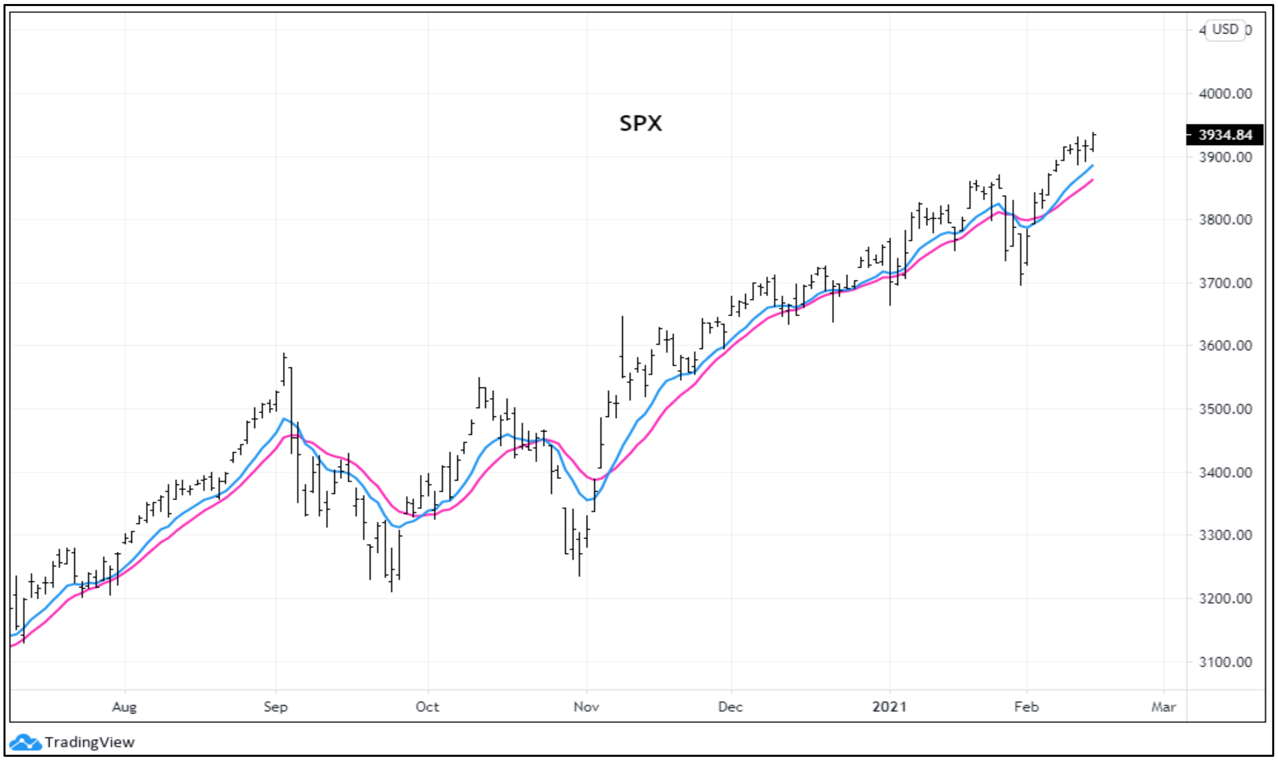
- Most shorted stocks have been some of the best performers
- Micro caps have been on fire
- Non-profitable tech stocks through the roof
- SPACs at every turn

However, after the whipsaw de-grossing selloff of two weeks ago, the equity market is back at the highs and momentum has been reignited.

There is currently no sign that either monetary or fiscal policy is going to be reined in anytime soon.

Industrial commodities are strong. The dollar, after an attempt to rally, has now again come off.

There are not many tells at this point that set off warning bells of an imminent risk-off event.



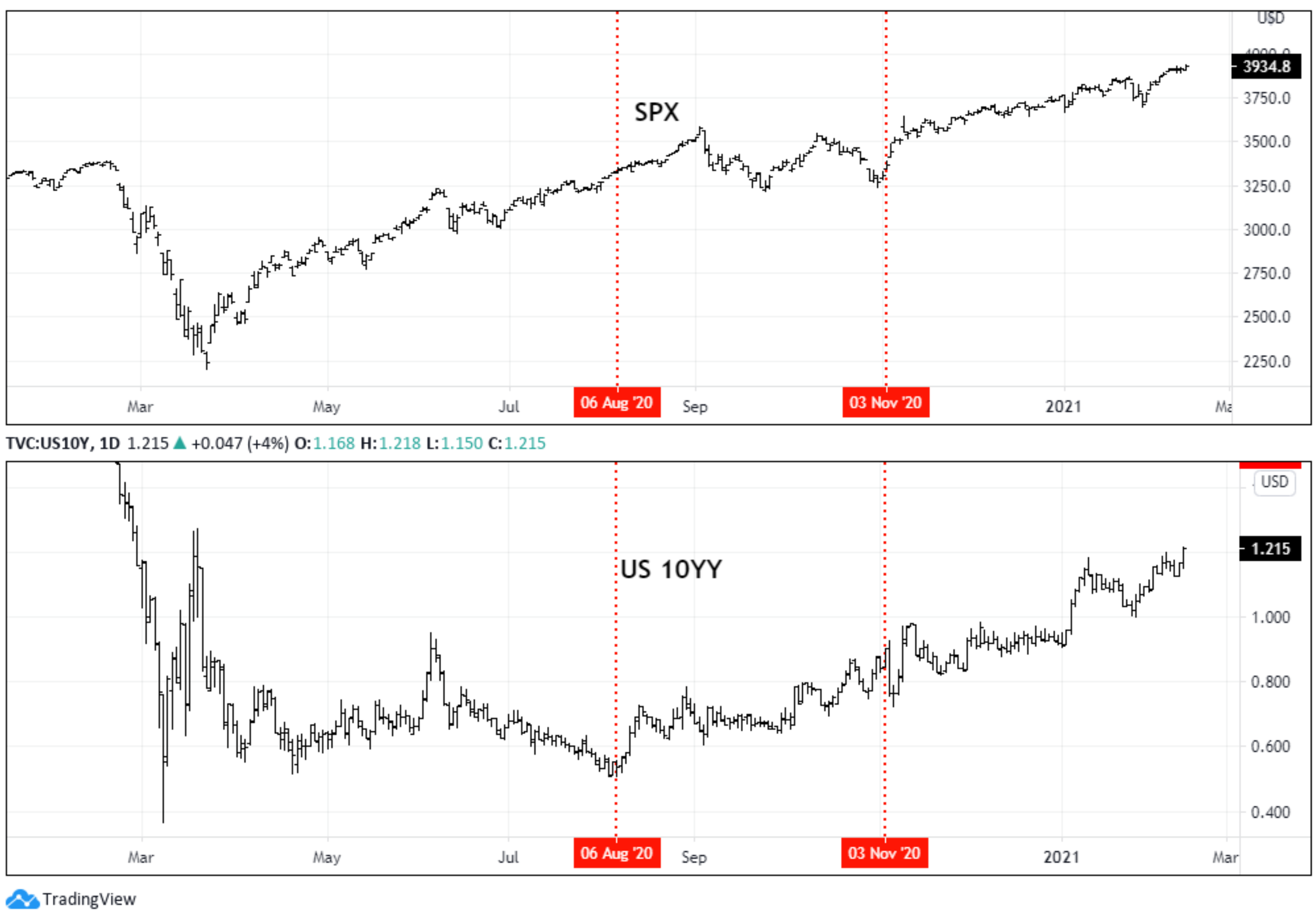
The one thing that has been gaining momentum and could eventually prove problematic, is the rise in Treasury yields. Slow at first, then all of a sudden?

The pace of play matters a lot here, and a 2013 or 2016 type of move higher runs the high risk of destabilizing markets and lifting the level of volatility. We are not there yet, however.

Last year we obviously had the brutal selloff in March to digest, but there were also two other periods that produced some powerful price action.

One was the double-whammy of the election/potential blue wave, and the announcement of multiple vaccines. The other was in August.

November is easy to explain and justify, but what was the driver in August?



One thing that caught my attention was the peaking of the second COVID wave during late July/early August.

The result was near-term positive for equities and Treasury yields. Are we seeing the same effect now as COVID cases and hospitalizations fall?

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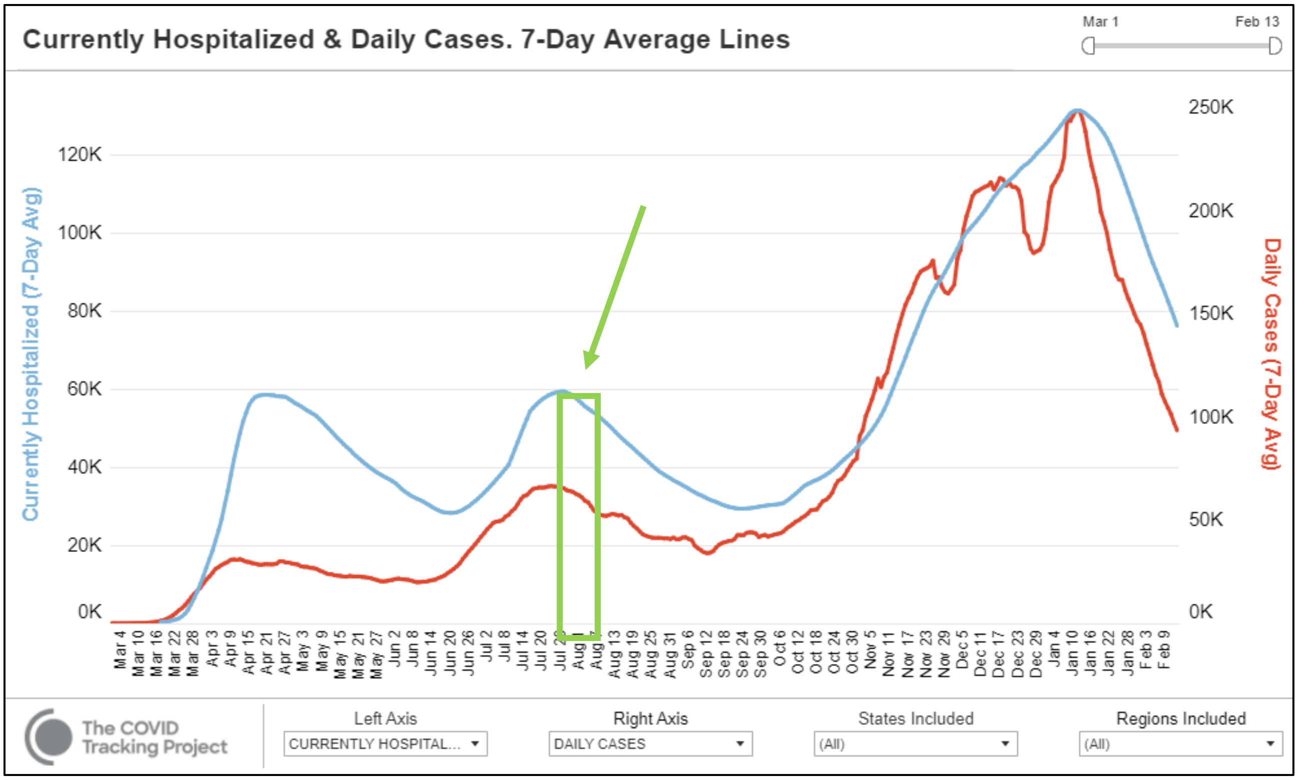
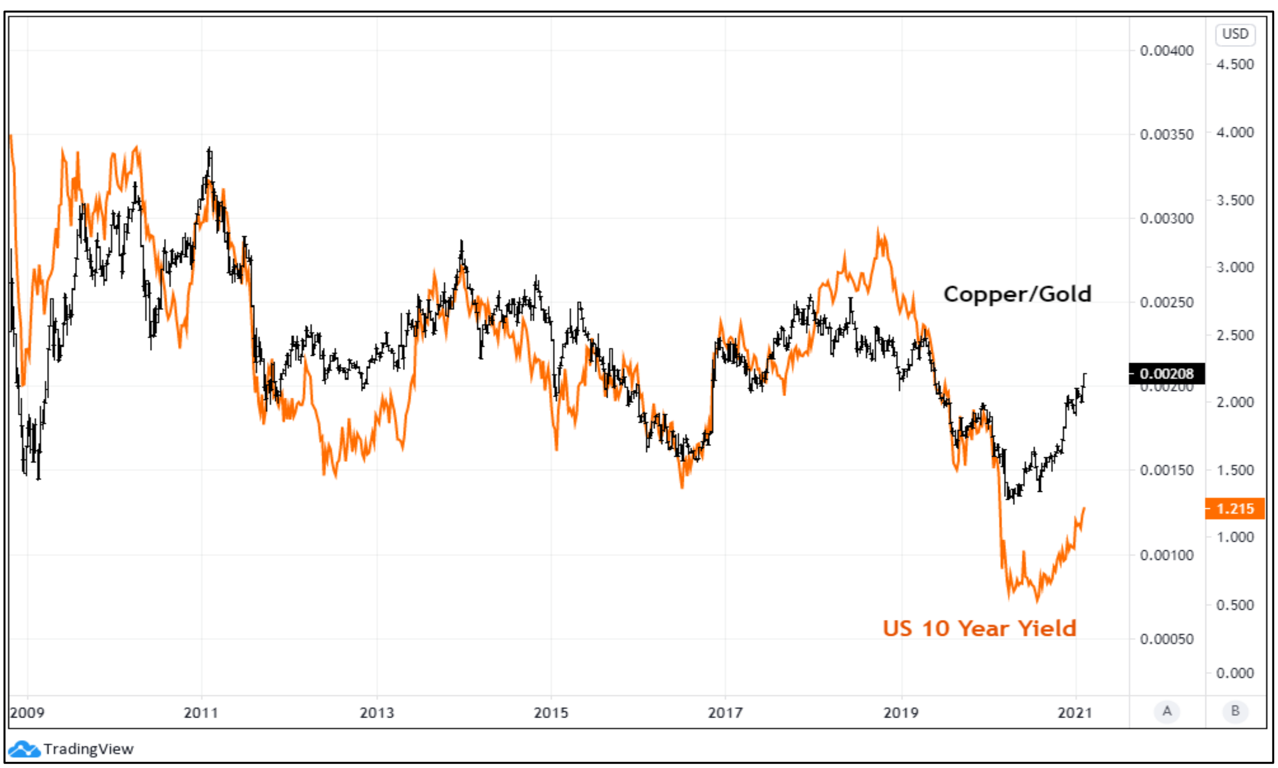


The turn in relative COVID performance stabilized the USD in early August, only to restart its down move on the election and vaccine news.

Gold stalled in early August as well, as the dollar's slide took a break. Unlike the USD however, it has not continued as higher yields and less of a need for safe havens has kept it relatively soft.

Instead, industrial metals have taken up the charge that Gold had been leading. Copper first…



Silver…

And now Platinum…

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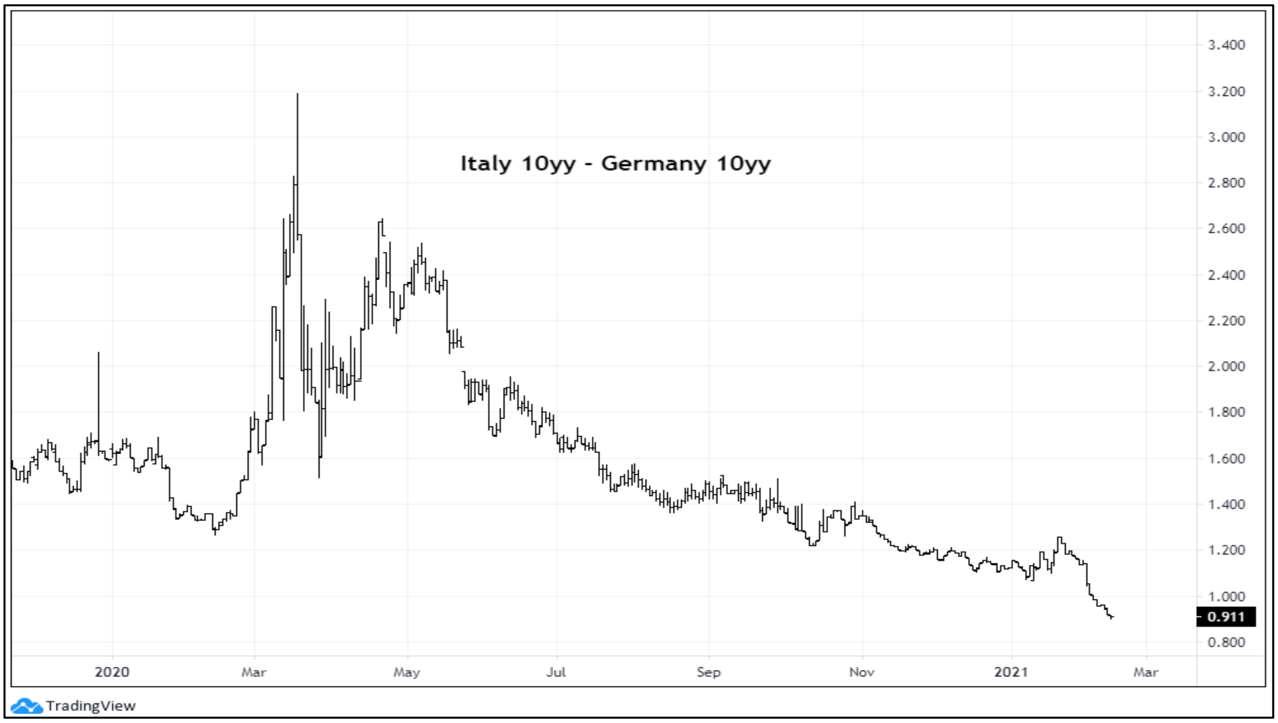
Italy - Mario Draghi has the spot as PM. Now what? It will be a struggle for sure as Italy has a lot of headwinds, including the Euro. However, I would expect that the country unites behind him as they already have. He could be the first shot in a long time at economic redemption.

Italian spreads vs. Germany have reacted favorably out of the gate… can equities follow?



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Important Macro Data Releases and Events for the Week

Monday 02/15/2021	**President's Day**
	Industrial Production s.a. MoM (Dec) Forecast: -0.6%, Prior: 2.5%
	RBA Meeting Minutes
Tuesday 02/16/2021	EcoFin Meeting
	ZEW Survey - Economic Sentiment (Feb) Forecast: 57, Prior: 58.3
	GDP Q4 - QoQ Forecast: -0.7%, YoY Forecast: -5.1%
	ZEW Survey - Economic Sentiment (Feb) Forecast: 60, Prior: 61.8
	ZEW Survey - Current Conditions (Feb) Forecast: -67, Prior: -66.4
	Fed's Bowman SPEECH
Wednesday 02/17/2021	Retail Sales (various versions)
	CPI Core YoY Forecast: 1.5%, Prior: 1.5%
	FOMC Meeting Minutes
Thursday 02/18/2021	ECB Meeting Minutes
	Fed's Brainard SPEECH
	Initial Jobless Claims Forecast: 775k, Prior: 793k
	Continuing Jobless Claims Forecast: 4.575M, Prior: 4.545M
	Initial Jobless Claims 4-week Average Forecast: -, Prior: 823k
	Philly Fed Manufacturing Survey (Feb) Forecast: 20, Prior: 26.5

Housing Starts (Jan) Forecast: 1.654M, Prior: 1.669M

Building Permits MoM (Jan) Forecast: 1.68M, Prior: 1.704M

Consumer Confidence (Feb) Forecast: -15, Prior: -15.5

ECB's Schnabel SPEECH

Friday
02/19/2021

Markit Feb. Flash PMI's across Europe

Markit Manufacturing PMI (Feb) Forecast: 58.5, Prior: 59.2

Markit Services PMI (Feb) Forecast: 57.5, Prior: 58.3

Markit PMI Composite (Feb) Forecast: -, Prior: 58.7

Fed's Rosengren SPEECH