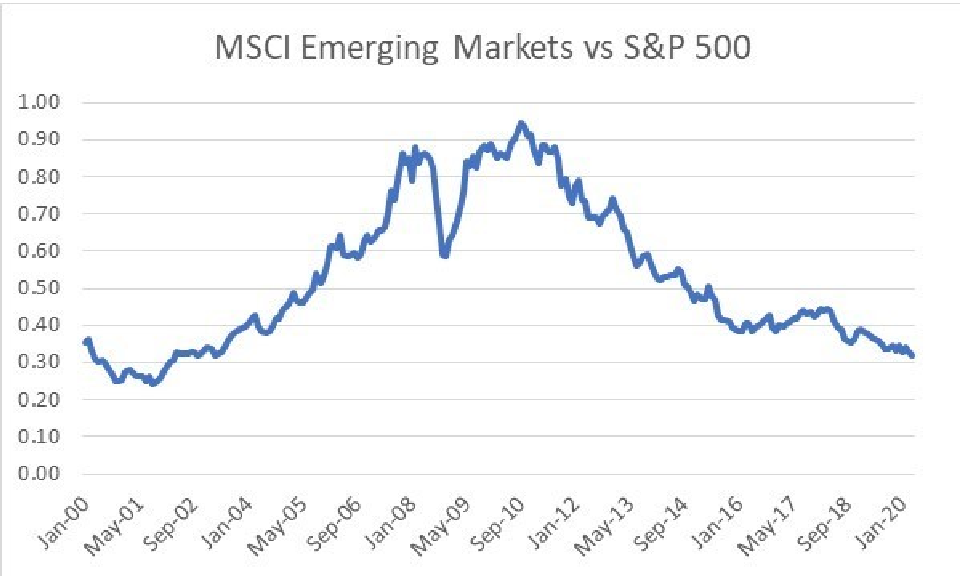
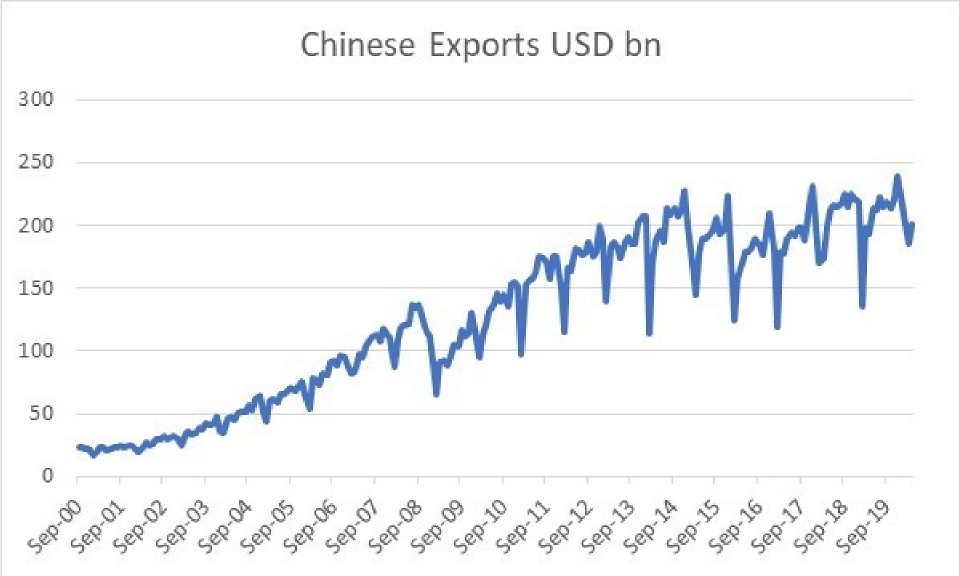
MACRO TRENDS AND MACRO TRADING

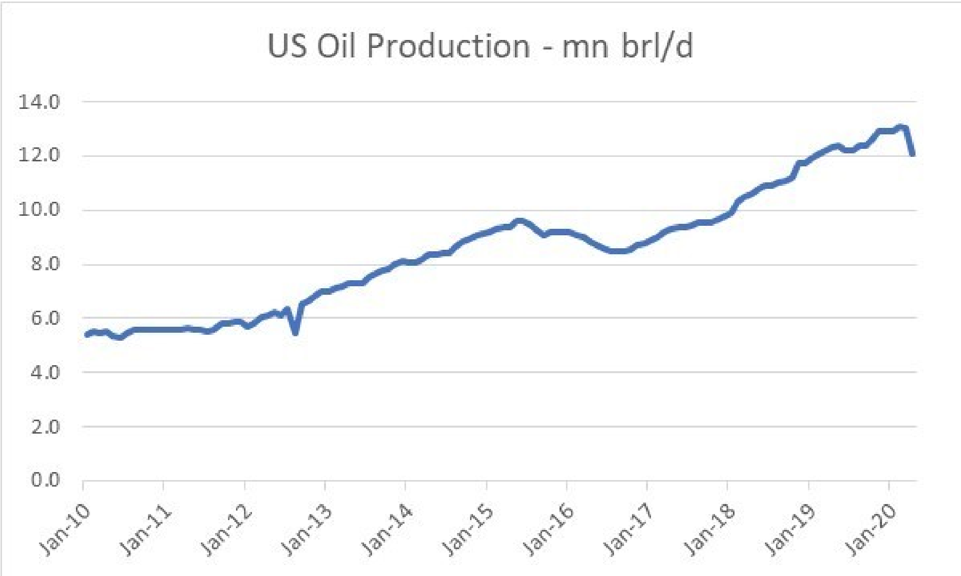
The first 20 years of the 21st century can be divided into two halves. The first half was the reflation trade, which was characterised by rising commodity prices, a weak US dollar, and strong growth. The second half has been the opposite, with falling commodity prices, weak growth and a strong dollar. Perhaps nothing shows this more clearly, that the relative performance of emerging markets, which greatly outperformed the S&P 500 in 2000s, and then gave back all that relative outperformance in 2010s.



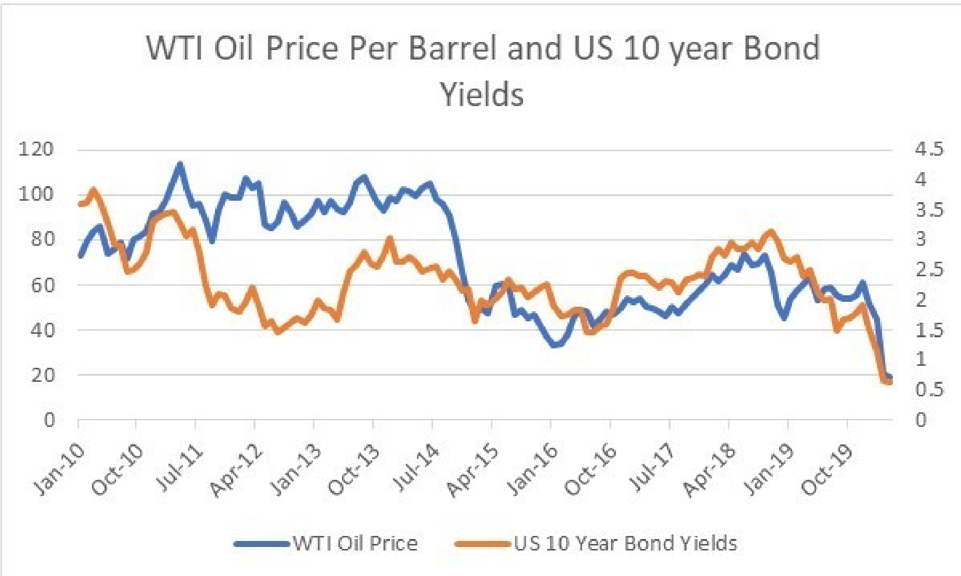
From a purely macro perspective, the emerging market and reflation story of the 2000s was a reflection of the exciting macro story of that period, the rapid growth of Chinese exports, and the 2010s has reflected the slowdown in that growth.



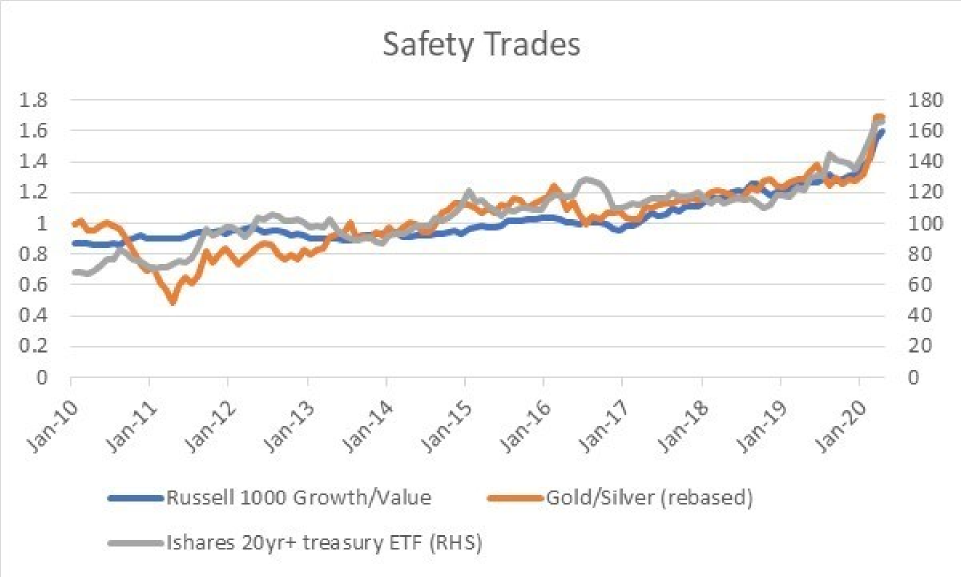
The macro story of 2010s has been the tremendous growth in US oil and gas production, to make the US the world's largest energy producer, and to turn the US from an energy importer to exporter.



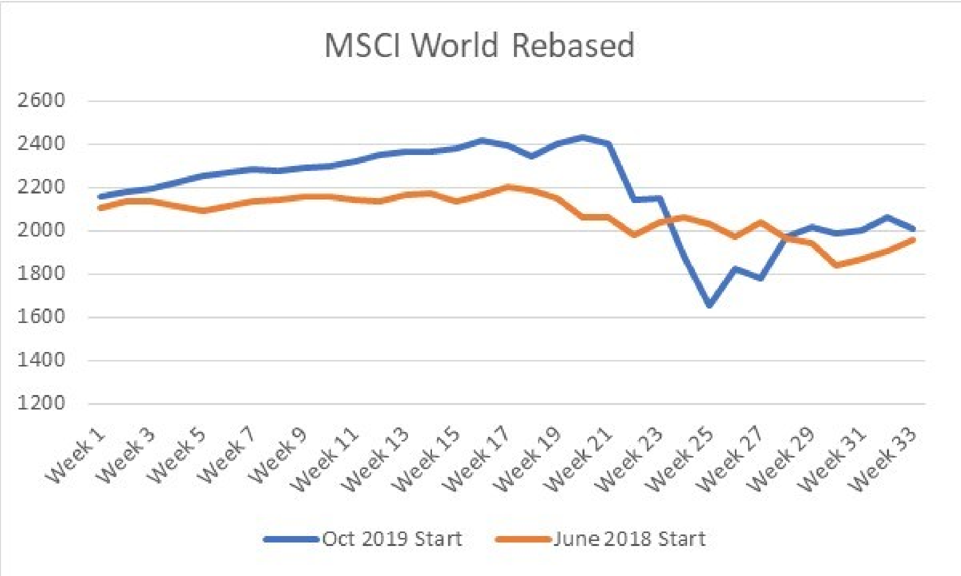
The combination of slower Chinese growth, rapid oil production growth led to a collapse in oil prices, contributing to suppressed inflationary pressures, and this has precipitated a collapse in bond yields as central banks have desperately tried to reignite growth.



Collapsing yields and commodities have forced investors into a variety of "safety trades". Growth stocks over value stocks, gold over silver, and long dated bonds. All have remarkably similar performance, particularly in recent years.

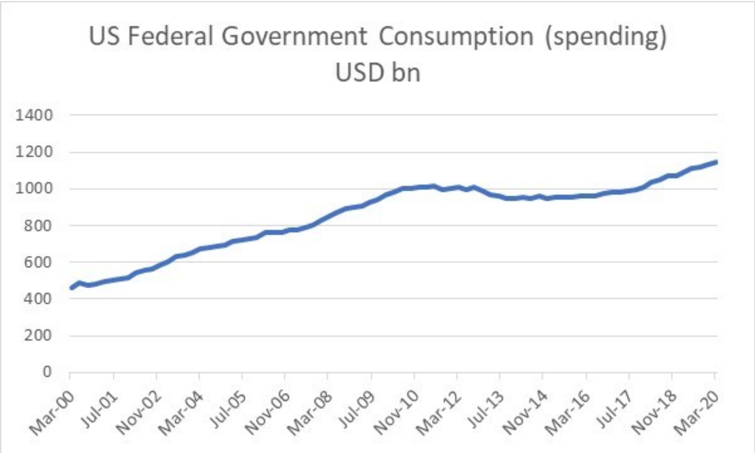


If this analysis is correct, then this would suggest that a return to global growth could indeed be "risky" for asset prices. There is already some evidence for this. In late 2018, when oil prices rose to 80 USD a barrel, world equities declined 15%, or roughly the same decline seen year to date during the COVID-19 pandemic. Both declines were arrested by central bank activism and new lows in bond yields.



As noted above, US oil production has begun to decline, and much more steeply than in 2015/6. Also we are beginning to see a trend change in Chinese exports, where exports to its near neighbours (BRI – Belt Road Initiative countries) are now larger than that to the US, opening up the possibility of export growth again for China.

Safety trades could also be exposed from a more negative angle. US government spending consolidated during the 2010s, but recent spending trends show an acceleration.



Changing underlying trends in oil, government spending and Chinese exports suggest that the macro trend of the 2010s will not be the same as the 2020s. If the experience of changing macro trends from 2000s to 2010s are repeated, then the winners of last decade, are now likely losers.

INFORMATION

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