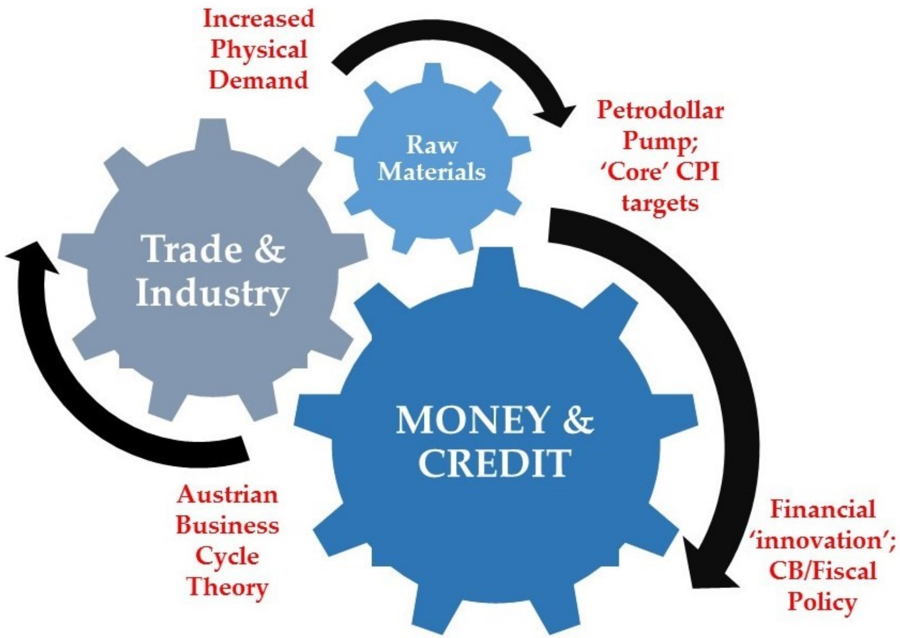
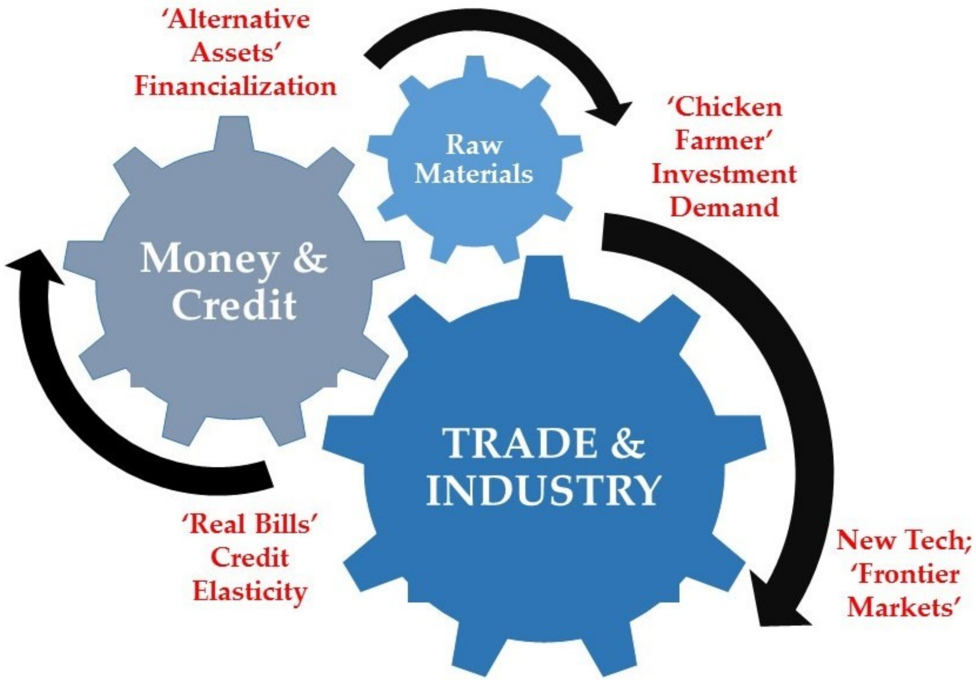
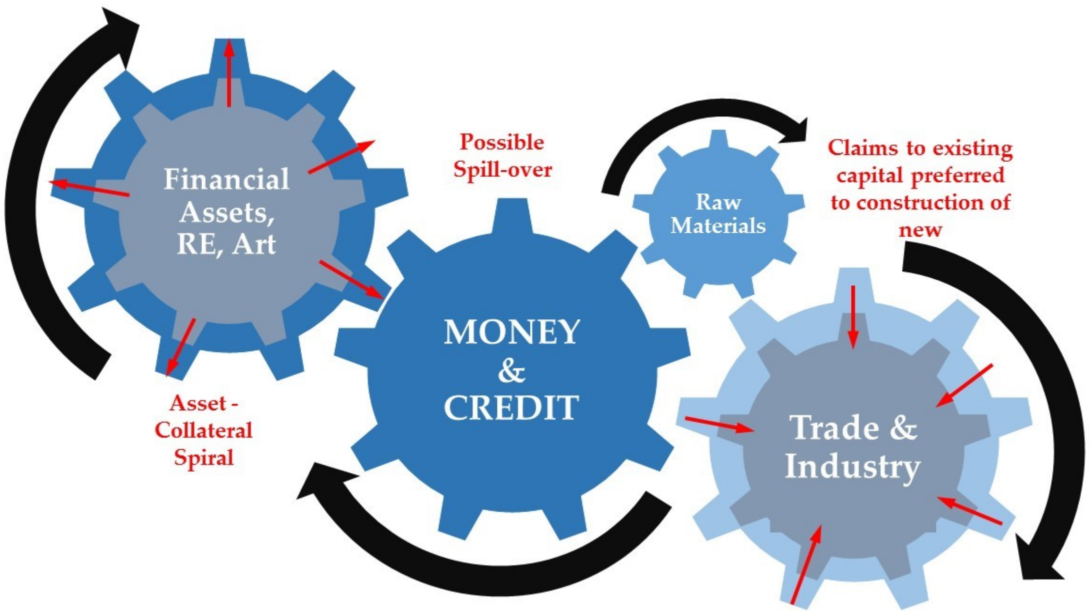
MIDWEEK MACRO MUSINGS

HINDESIGHT LETTERS

12th Oct 2016







Non-Farm Payrolls drew something of a yawn but, coupled with a look at how business revenues are faring, they do tell us that a little stress is building.

Meanwhile, sterling seems to be without a friend in the world, not least back in Threadneedle Street.

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For once the US employment report produced few fireworks, even though the tally of 167,000 private jobs added registered the second mild disappointment in a row in again falling beneath the past six-years' average of 200k a month.

One reason for the relative anaemia in hiring might be the fact that while business sales for manufacturers, wholesalers, and retailers have been essentially flat over the past year—and, indeed, barely changed, on aggregate, over the whole of the past three—average hourly wages are clearly beginning to accelerate. In the past twelve months, these have recorded a gain of 2.6% - the fastest increase in the seven years since the world economy pulled out of its post-Lehman nosedive.

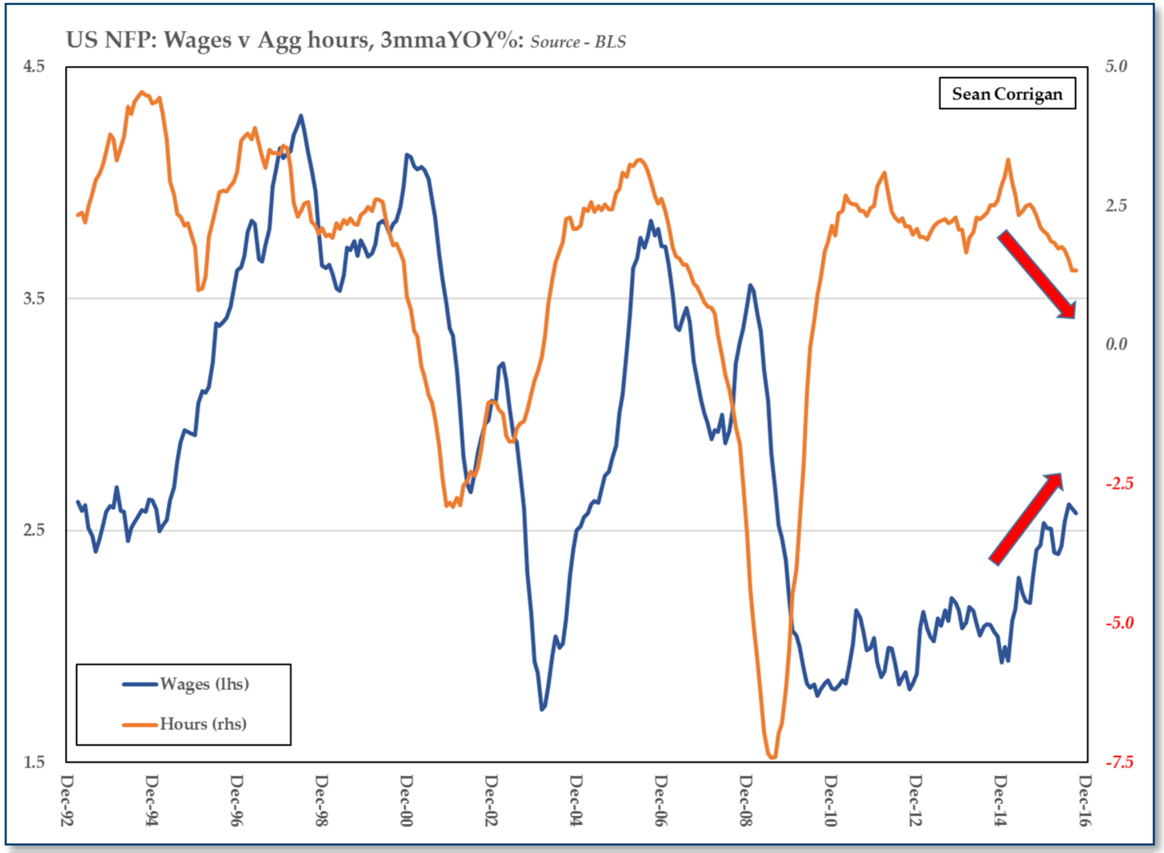
Add in the fact that non-wage costs are also rising sharply—not least for Obama's problematical healthcare programme – and you can see why something of a battle might be developing between what the one datum suggests is a tightening supply of skilled employees and what is clearly demonstrated by the other—a general inability on the part of their would-be employers to increase turnover, no matter how many new (and more expensive) hands they set to the wheel.

In comments *he* made at a major banking seminar in Washington Friday, Fed Vice-Chairman—the *eminence grise* of modern central banking himself – Stanley Fischer, tried to set the detail of the report into the context of the FOMC's thinking on policy (if we can grace its fractious procrastination with the dignity of such a title).

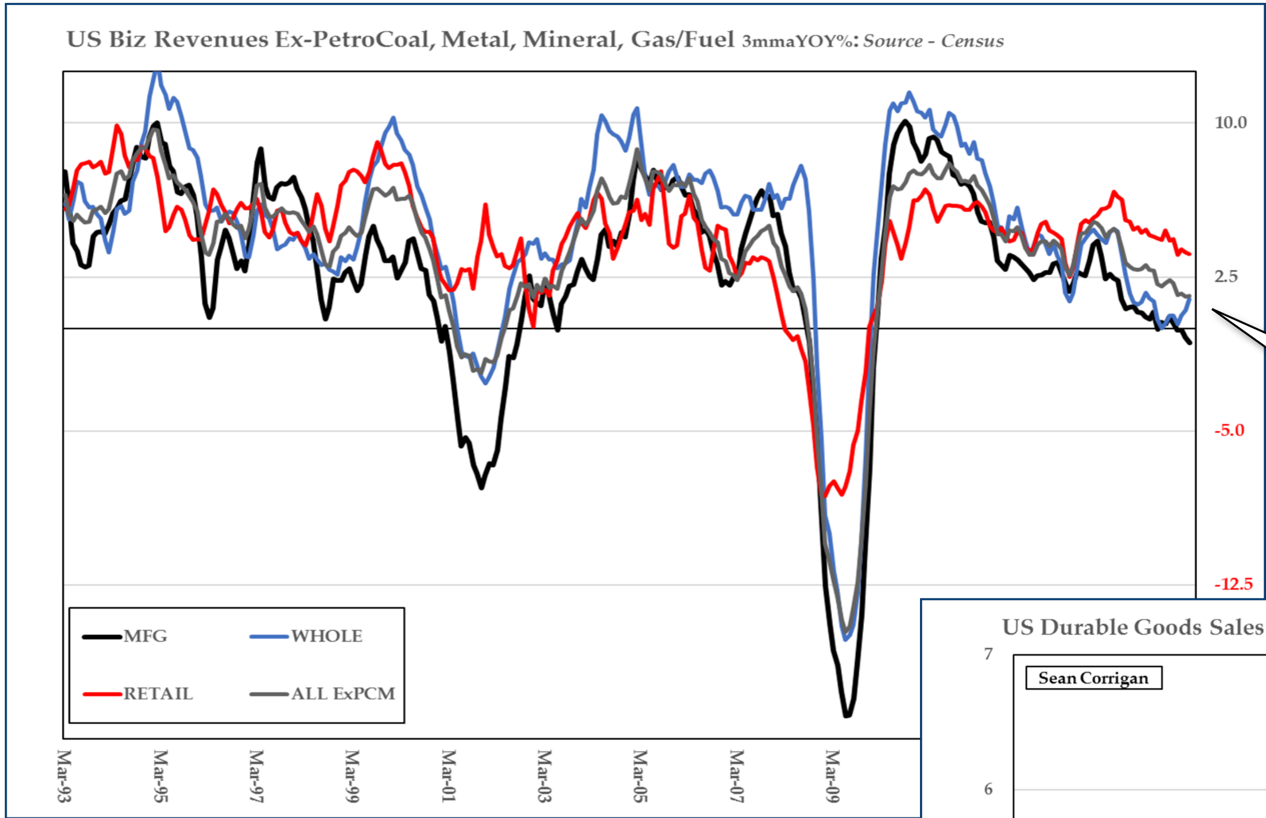
'*Nearing full employment but with some scope for further improvement*' was the gist of his somewhat equivocal spin on the situation—a verdict arrived at after the now-typical, non-committal rehearsal of just about every opinion on the matter being expressed by anyone with a PhD, a newspaper column, or a marketing job at an investment bank. Having thus clothed the intellectual nakedness of his posterior in obfuscation, our sage, while emphasising that the latest call on interest rates was a 'close' one (yawn), vouchsafed—to the surprise of no-one—that wait-and-see, alas, was still very much the watchword.

Were we to ignore all else and look at jobs alone—and were we to suppose the Fed to be the best agency to deal with any perceived lack of them, or that its actions to make good that lack did not entrain much deeper failings—some modest grounds for caution could however be found, as we show here.

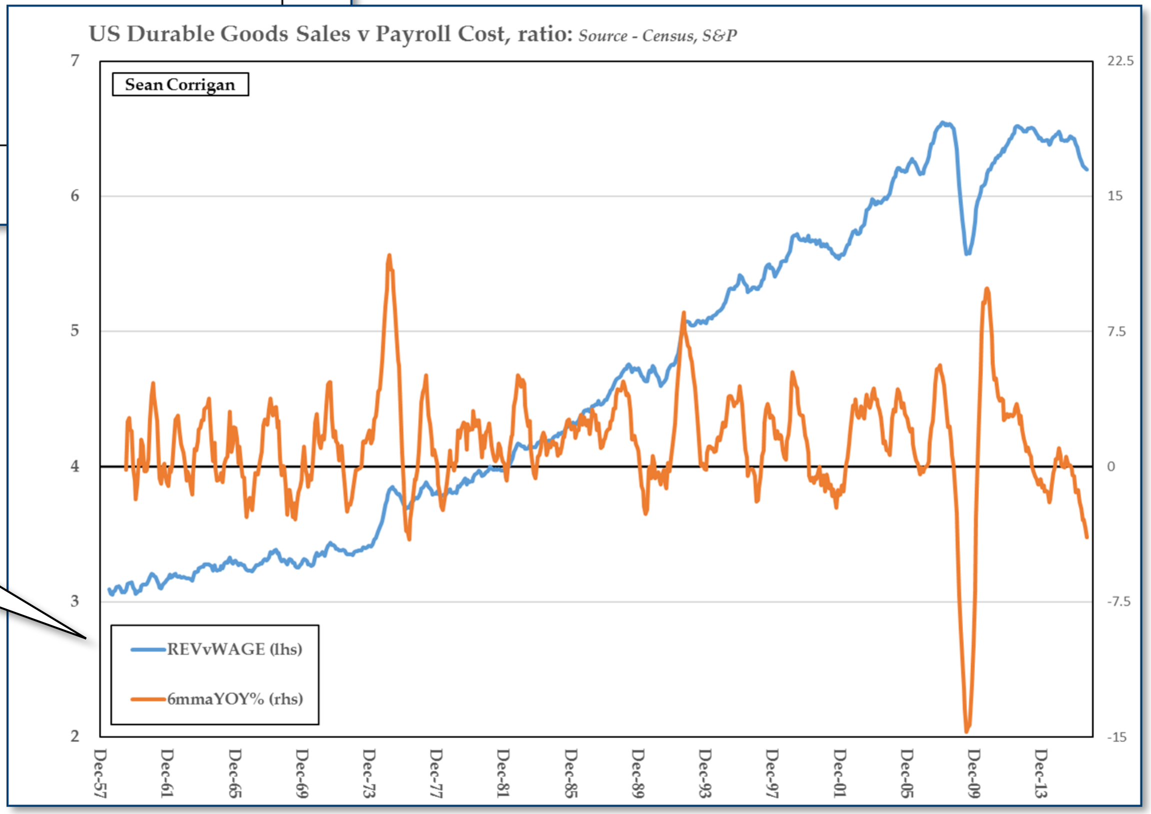
And, as we all know, this is a Fed for which caution is its very meat and drink.



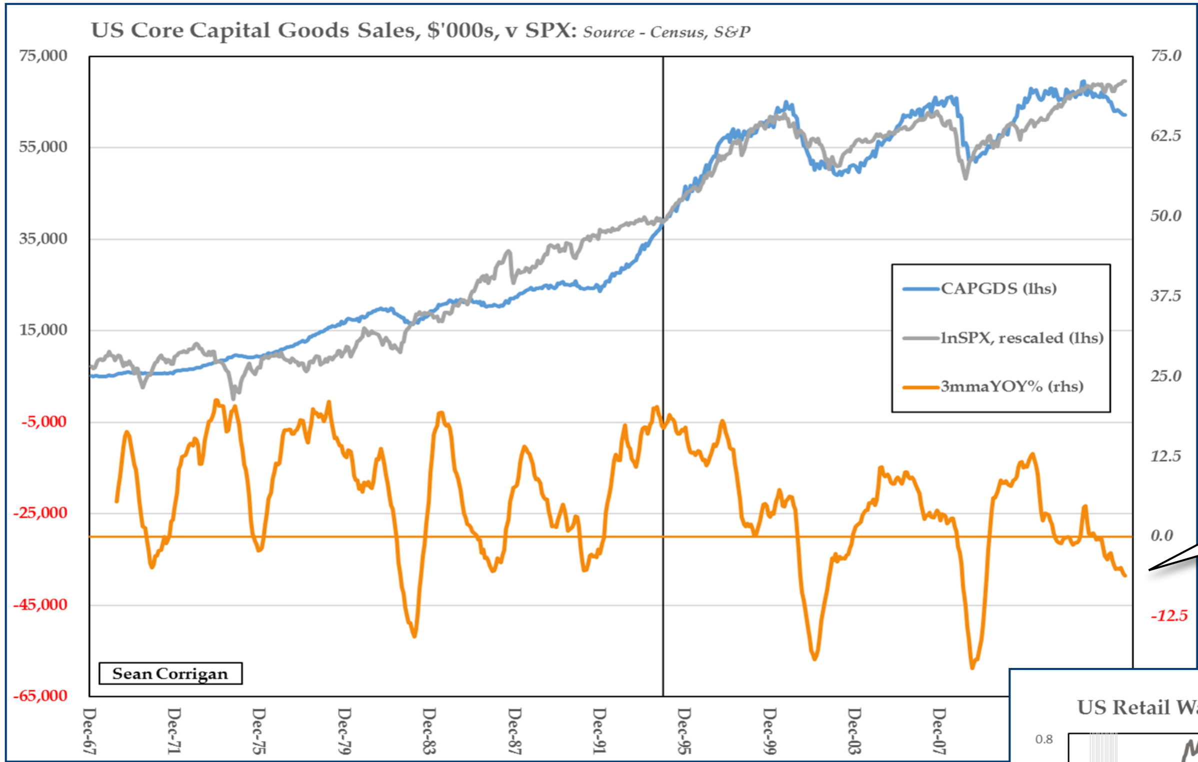
Over the past 18 months, an increasingly rapid rise in hourly pay rates has coincided with a slowing in hours worked to its tardiest rise in 6 years



Even after stripping out the sectors the worst affected by the resource bust, shipments are clearly slowing

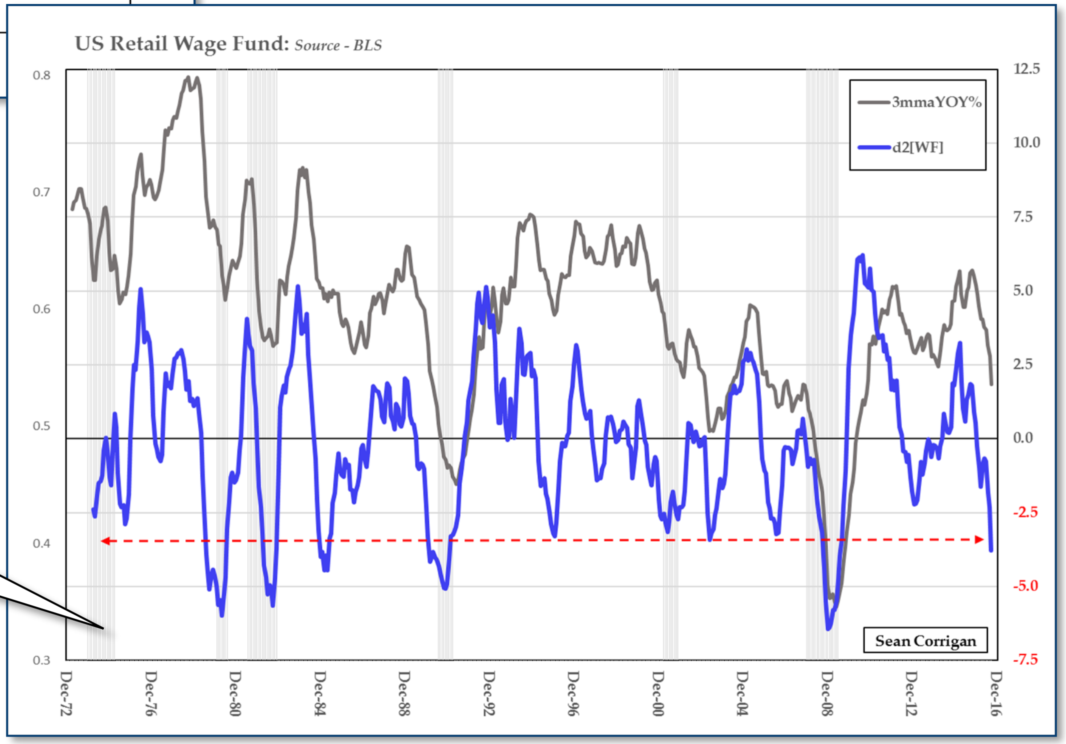


Revenues are therefore outpacing payroll costs, meaning intense pressure on profits and hence on the very rationale for hiring



We Austrians hold that the economic fish tends to rot from the head down. Capital goods are certainly starting to smell, even if the S&P itself is still *just* managing to come up roses

But even down at the Five'n'Dime, the pay-out on staff has slumped from the fastest pace in 8 1/2 years to the slowest since the Crash—a deceleration of a kind normally only seen in well-developed recessions. Can it *all* be Amazon's fault?



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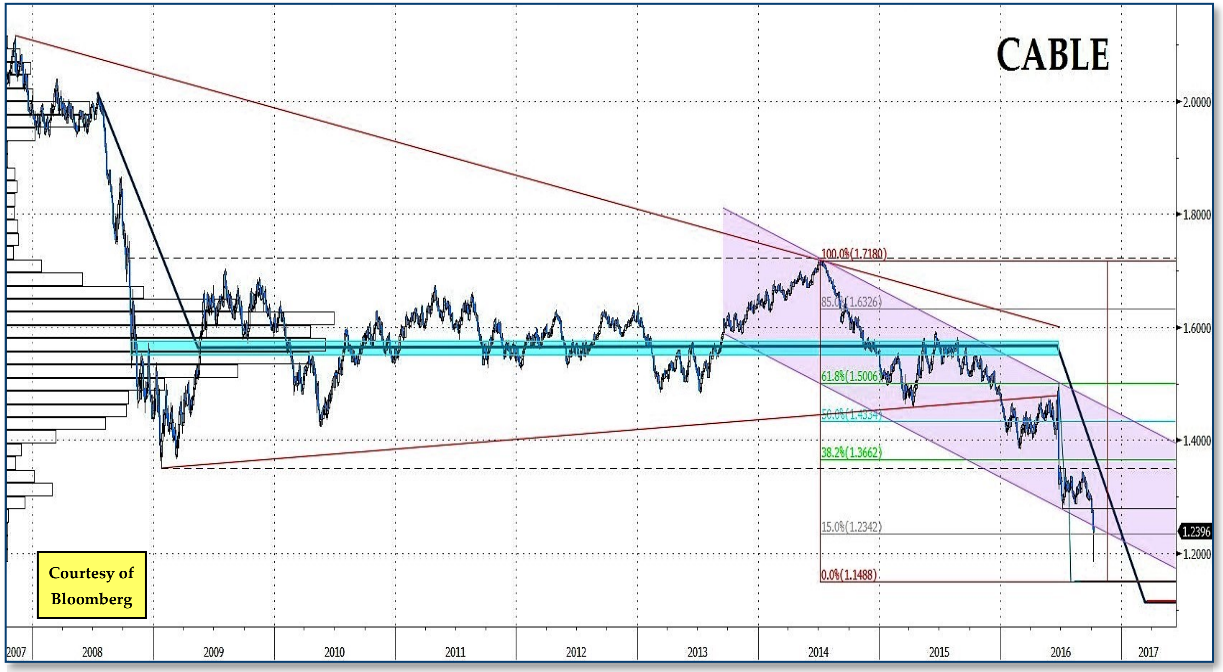
As the witching hour struck last Thursday night in London, someone - or something – lurking out in the twilight zone of cyber space pushed a button – whether by accident or design - which sent Her Majesty's once proud pound plummeting on the foreign exchanges.

In under ten minutes, the world's fourth most heavily traded currency dropped at least 6% against the dollar – and possibly more if rumours about what went through on less visible forex platforms are true – taking it from an already lowly $1.2640 to an abyssal $1.18 and change almost before you could say, '*Yours! Mine! Dets outside. See you for lunch, sha-a-ag!*'

Though the next hour did restore some sanity to the market, it has to be said that the enthusiasm of any bargain hunters was strictly limited thereafter, dooming it to drift slowly south of the $1.22 level – a hefty 28% below the point where it entered the second half of the year and at a mark where it is threatening to break the all-time trade-weighted lows which now are its last line of defence.

As (bad) luck would have it, the nosedive coincided with the release of weakish industrial production numbers—after a run of better, if far more airy-fairy, survey data.



The scariest thing about sterling is the sheer, fractal nature of its chart patterns. Hourly, daily, weekly, monthly—all share similar bearish formations. UGH!

Worse yet, was the announcement of yet another numbingly wide visible trade gap whose £132 billion, 12-month running total serves as a stark reminder of just how much Britain relies upon the credit extended to it by its corpus of overseas suppliers of everything from coats to cars, and chemicals to cookers. Not that they'll be overly cheered at having put their savings to such a use—not when the dollar returns to holding long gilts have cratered 12% in under a month, wiping out 14 months' worth of hard-won gains in the process.

But it's not all gloom and doom. For one thing, that fall in the price of gilts corresponds to a nice little 35 basis points rise in their yields, taking them back to the levels of late July.

Given that August's Bank of England-driven decline had wiped £112 billion off the funding levels of the country's defined benefit plans - and given, too, that equities are now handily 4-5% higher in terms of the British peso – some much needed respite should be reported there, this month.

Then there's the FTSE's batch of mining stocks - big names in global dirt moving such as Anglo-American, BHP, and Antofagasta. Any UK fund manager who was smart enough to accumulate these in the dark days of winter must be feeling pretty chuffed with himself as they've risen 125% in the nine months since – something only matched in the past two decades by the rebound from the depths of the Lehman crisis itself. Who says there's no such thing as a copper lining?

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Next, as if anxious to drive his own personal nail in the coffin of a currency which last fell as steeply on his watch, former Bank of England chief Mervyn - sorry, *Lord* – King of Lothbury - was the next to add to the angst surrounding sterling by telling Sky News that the drop was a '*welcome change*'.

Well, yes, My Noble Lord – a country which runs the globe's second biggest external deficit (and the largest per capita one among the bigger nations) is clearly in need of *some* re-adjustment if the super-proportion of imports to exports is ever to be addressed. But it would be nice if that 'change' did not become a disorderly rout along the way by scaring the pants off the country's many foreign creditors.

It would also be helpful, M'Lord, if your successors at the Old Lady were not anxiously trying to ensure that everyone either fleeing the pound, seeking protection against its further decline, or speculating outright against it gets as much ammunition as they need, at as cheap a rate as possible, while they are doing so. '*Driving capital to the airport in a limo to catch its flight*,' as your author put it on CNBC a few days after the Brexit vote.

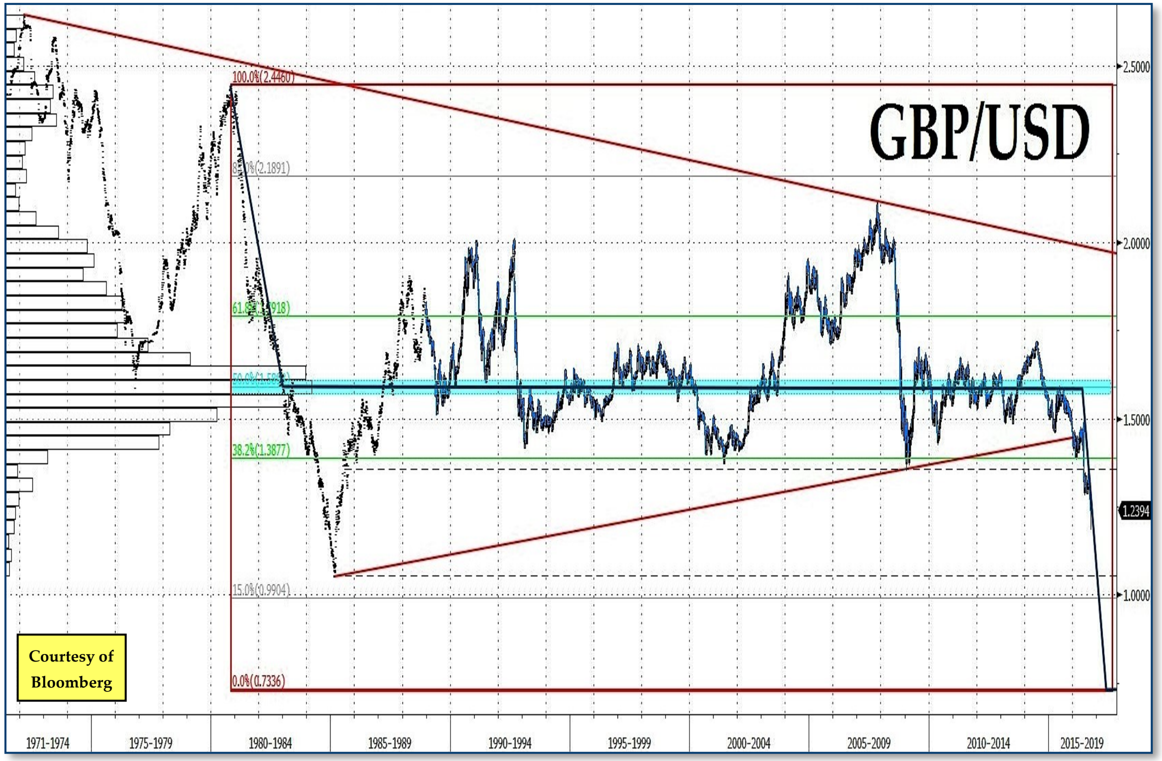
Increasingly there is a sense that no-one has very much of a stake in trying to arrest the slide. Certainly not the many political opponents of Brexit who are all too eager to point at the pound's plight as the verdict of the 'impassive' arbiters of global markets upon what they are anxious to paint as the Leave camp's abiding folly (dark whispers about our favourite Hungarian *Schieber* have even begun to be muttered in this regard).

Certainly not the Bank itself, which is so wedded to the prevailing fallacy that a little more inflation is a good thing – despite the sorry counter-example of Japan's faltering efforts – that it, too, seems to want to try its hand at sparking it via a rise in the nation's import cost of energy, clothing and foodstuffs in a blast of what one might call *Westminster Abbey*-nomics.

The wider issue here is that the move out of sterling is threatening to catalyse a broader rise in the US dollar of the kind which global markets have found all too uncomfortable in recent times. Crucial to that determination will be the issue of whether or not the euro can hold up in the next few days, buttressed by a rather important trendline. Tthough it's nothing, too, dramatic as yet , it should be noted that forex exchange options vols are moving up from 2-year lows, with dollar calls trading better bid than dollar puts. From little acorns, and all that…

The rise in the Greenback has not been, however, yet proven sufficiently convincingly to stymie what has been a two-week winning streak for oil, denying any respite to those British firms and householders who must be dreading the next time the fuel bill falls onto the doormat—what, with the sterling price of oil up 20% in the past 2 weeks and by 120% since January.

Time, then, to knit granny a nice, thick cardie for the winter, or else, if it all gets too expensive to use hydrocarbons to keep the house warm, fire up a Samsung 7.



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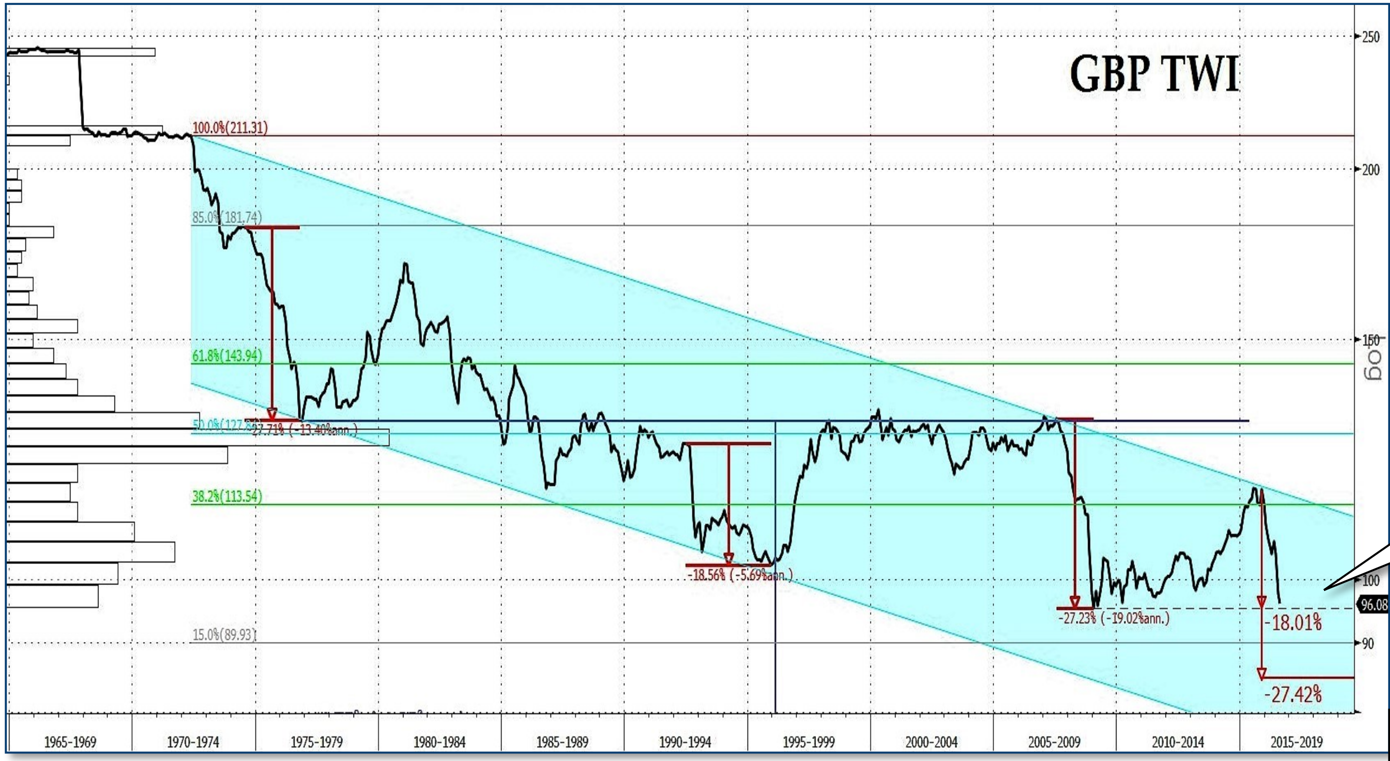

If sterling is EVER going to find a bottom-fishing, responsive bid, it will be here against the old Trade-Weighted Index low

Courtesy of Bloomberg

Don't entirely rule out the possibility that the euro, too, breaks an important, long-term trend line

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Similarly, having mean reverted, the yen has broken out of the down channel. The minimum to be expected next is a range trade between Y100/105

Courtesy of Bloomberg

Now that China's safely in the SDR, no need to spend even more reserves bolstering the yuan. At a six year high already but likely to trade back at least to 2010's pegged level in the CNY6.80s

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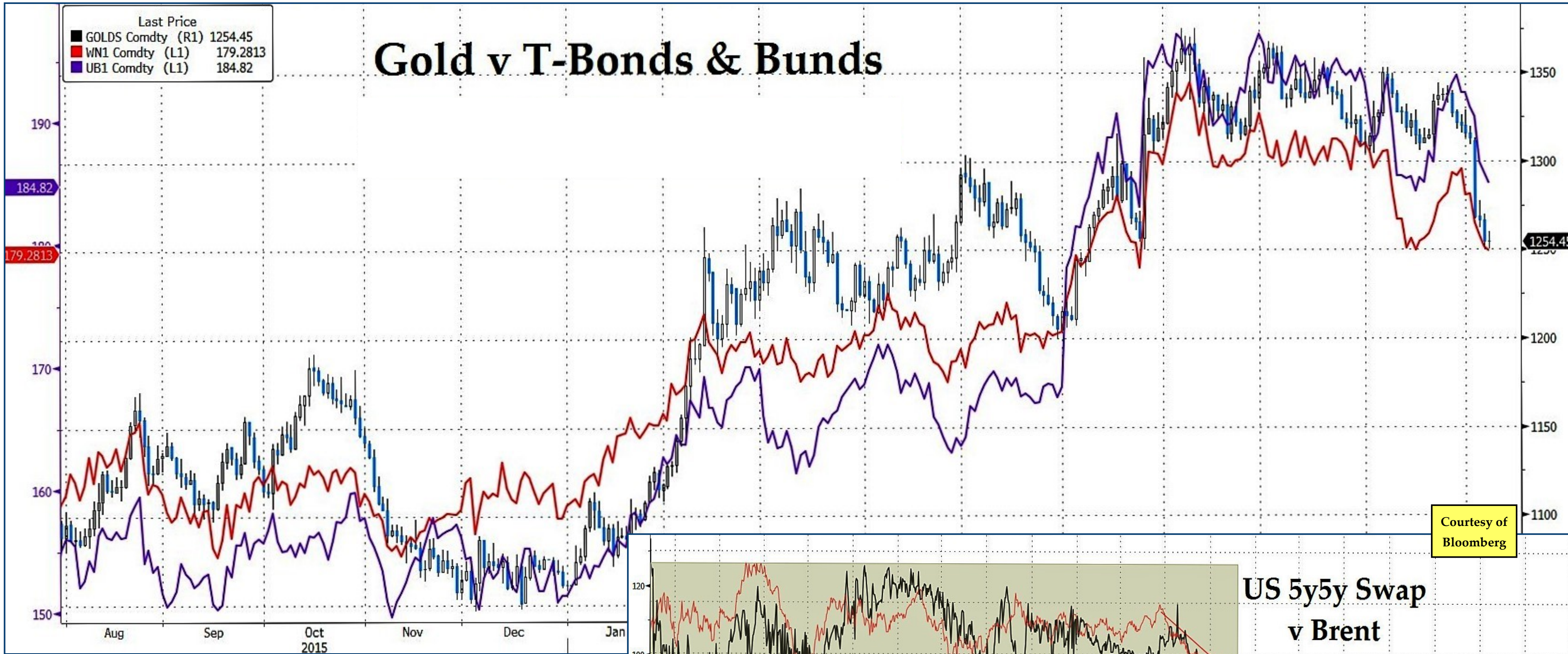
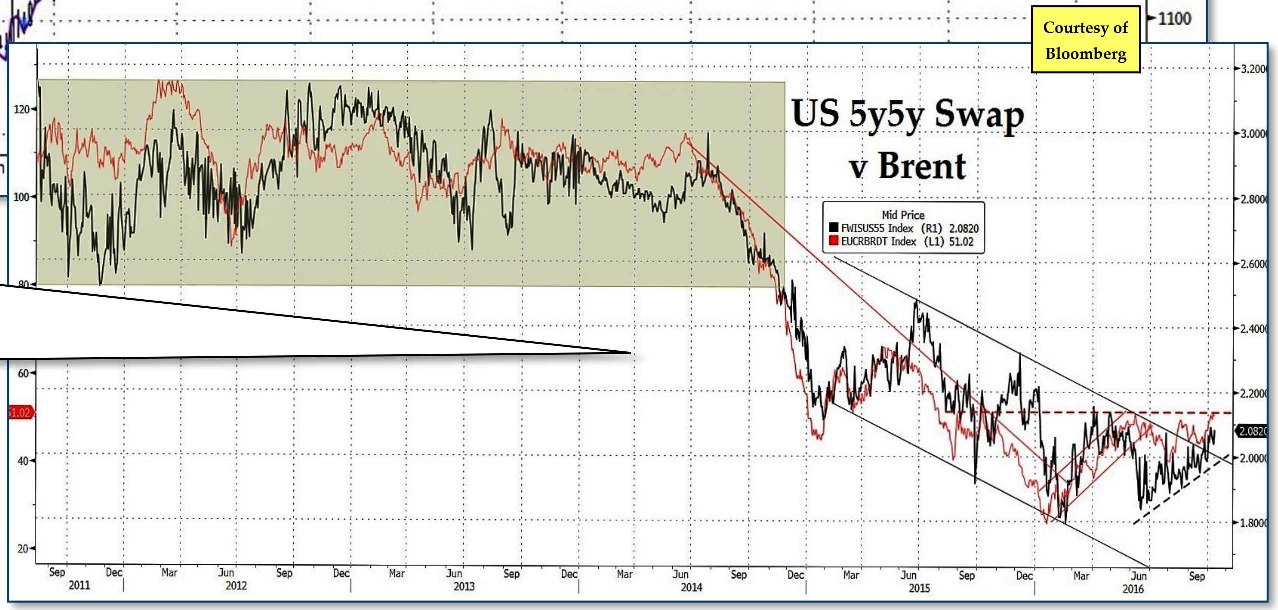
This chart is still the daddy of them all. Can the USD test the upper High Volume area and resume its globally disruptive bull run?

Courtesy of Bloomberg

Though gold broke higher on Brexit night, it has been knocked back down as sterling has succumbed. Options show bulls are giving up for now. This should keep the metal in Feb-June's $1200/1300 band as the market reconsiders its approach.





Gold has maintained its recent relation with bond prices which—ironically—are being pressured by the idea that QE may be nearing an end, not least because of a turn higher in both actual and 'expected' inflation in the US. Gold's recent buyers evidently had other reasons to jump in than a rise in the cost of living.

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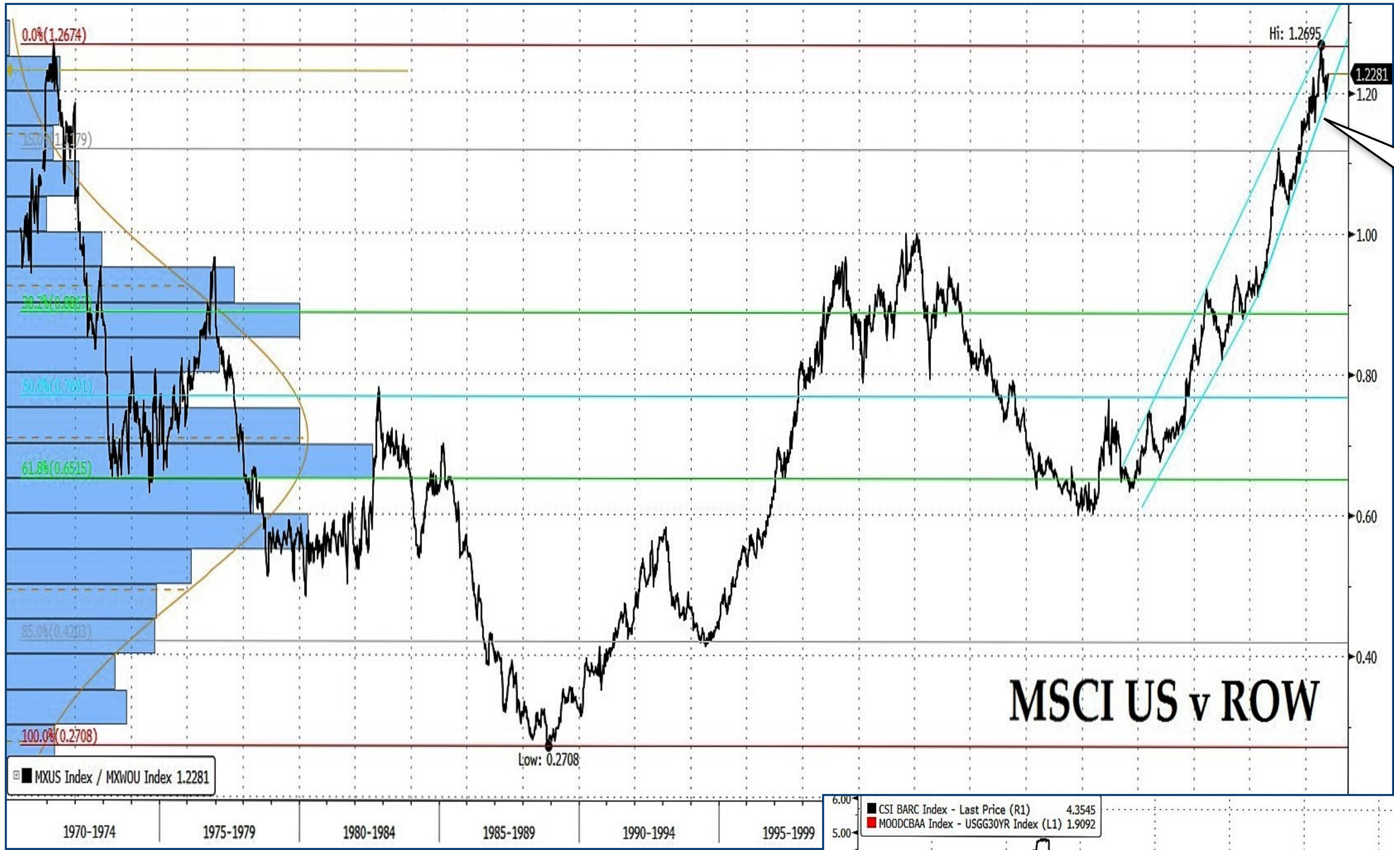
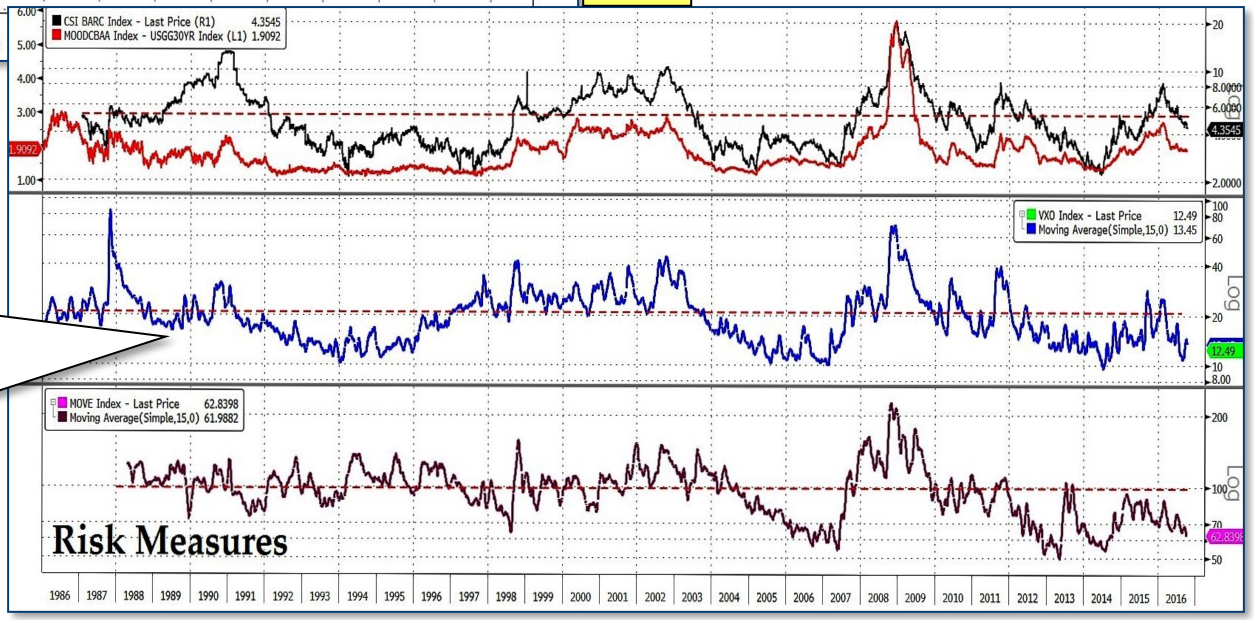


Meanwhile, US stocks trade back to record highs v their ROW peers - as well as being rich on any number of other metrics. 'The only dirty shirt', and all that...

Courtesy of Bloomberg



Despite the Deutsche Bank woes, the Italian referendum, political chaos in the US & UK, mounting tensions with Russia, and rumblings in currency and bond markets, the price of risk remains subdued, whether measured by credit spreads or by bond and stock vols. *Insurance is cheap!*

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