PROVIDING THE BIG PICTURE ON MACRO AND CREDIT SINCE 2009

Martin Tixier – Strategist

PLAN

WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

1 EXECUTIVE SUMMARY – 8TH OF DECEMBER

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MACRO THOUGHTS

"The ignorant mind, with its infinite afflictions, passions, and evils, is rooted in the three poisons. Greed, anger, and delusion." - Bodhidharma

- The S&P 500 rallied 10.5% in November, its biggest monthly gain since April and its strongest November since 1928. We think the market could be a little bit complacent / too greedy. It is as well the strongest monthly gain since January 1987 for the S&P 500.

- Though we continue to like US over European countries and we continue to be overweight US versus Europe given the significant rise in commodities, we are bullish Emerging Markets commodities players and think, for instance Brazil equities and its currency are oversold, same goes with Russian equities. This could play very well in 2021.

- Our trading indicator sent us a buy signal on the 30th of November on Precious metals and miners given gold was way oversold with RSI lower than 30 at the time. With continued dollar weakness and a rising stock of negative yielding above the $17.5 trillion level with more stimulus coming, it seems to be bullish for the precious metals. January as well is historically a good month for the "barbaric relic". More on this in this presentation.

- Credit wise high beta rally in US High Yield and in particular in the CCC segment which is reaching tighter levels (below 10% yield) has been very strong in November for high beta with CCCs racing ahead. Now CCCs are slightly positive YTD but they ain't cheap at all relative to their current ratings. CCCs depend on a sustained rally in oil prices to maintain the momentum.

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WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

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WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- 2020 is shaping to be another record year for risky assets, showing the disconnect between markets and the economy.

Ranked Asset Class Return by Year. Green Means You're Beating Inflation

Ranking	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 YTD
1	US 10yr	MSCI EM	REITS	US 10yr	MSCI China	Russell 2000	REITS	MSCI Japan	Commodities	MSCI China	US 2yr	S&P 500	MSCI China
2	US 2yr	MSCI China	Russell 2000	Inflation Bonds	MSCI Europe	S&P 500	S&P 500	REITS	Russell 2000	MSCI EM	US 10yr	REITS	S&P 500
3	US Agg. Bond	Global HY	Commodities	EM$Sov Credit	Global HY	MSCI Japan	US 10yr	US 10yr	US HY	MSCI Europe	US Agg. Bond	Russell 2000	MSCI EM
4	US IG	US HY	MSCI EM	US IG	REITS	MSCI Europe	MSCI China	EM$Sov Credit	Global HY	MSCI Japan	US HY	MSCI Europe	Russell 2000
5	Inflation Bonds	Commodities	MSCI Japan	US Agg. Bond	MSCI EM	US HY	US IG	S&P 500	S&P 500	S&P 500	US IG	MSCI China	MSCI Japan
6	EM$Sov Credit	MSCI Europe	US HY	REITS	EM$Sov Credit	Global HY	EM$Sov Credit	US 2yr	MSCI EM	Russell 2000	EM Local Debt	MSCI Japan	US 10yr
7	US HY	EM$Sov Credit	S&P 500	US HY	Russell 2000	MSCI China	US Agg. Bond	US Agg. Bond	EM$Sov Credit	EM Local Debt	Global HY	MSCI EM	Inflation Bonds
8	Global HY	REITS	Global HY	Global HY	S&P 500	REITS	Russell 2000	US IG	REITS	Global HY	REITS	US IG	US IG
9	Commodities	Russell 2000	EM Local Debt	S&P 500	US HY	US 2yr	Inflation Bonds	MSCI Europe	US IG	EM$Sov Credit	Inflation Bonds	US HY	US Agg. Bond
10	MSCI Japan	S&P 500	EM$Sov Credit	US 2yr	EM Local Debt	US IG	US HY	Global HY	EM Local Debt	REITS	EM$Sov Credit	EM$Sov Credit	Commodities
11	Russell 2000	US IG	US 10yr	EM Local Debt	US IG	US Agg. Bond	US 2yr	Russell 2000	Inflation Bonds	Inflation Bonds	S&P 500	Global HY	US HY
12	S&P 500	EM Local Debt	US IG	Russell 2000	Inflation Bonds	MSCI EM	Global HY	US HY	MSCI Japan	Commodities	Commodities	Commodities	Global HY
13	REITS	Inflation Bonds	US Agg. Bond	Commodities	MSCI Japan	Inflation Bonds	MSCI EM	Inflation Bonds	US Agg. Bond	US HY	Russell 2000	EM Local Debt	EM$Sov Credit
14	MSCI Europe	MSCI Japan	MSCI China	MSCI Europe	US Agg. Bond	EM Local Debt	EM Local Debt	MSCI China	MSCI China	US IG	MSCI Japan	US Agg. Bond	US 2yr
15	MSCI China	US Agg. Bond	MSCI Europe	MSCI Japan	US 10yr	US 10yr	MSCI Japan	EM Local Debt	US 2yr	US Agg. Bond	MSCI EM	US 10yr	EM Local Debt
16	MSCI EM	US 2yr	Inflation Bonds	MSCI EM	Commodities	EM$Sov Credit	MSCI Europe	MSCI EM	US 10yr	US 10yr	MSCI Europe	Inflation Bonds	MSCI Europe
17		US 10yr	US 2yr	MSCI China	US 2yr	Commodities	Commodities	Commodities	MSCI Europe	US 2yr	MSCI China	US 2yr	REITS

Source: Bloomberg, Morgan Stanley Research; Note We compute annual returns minus US headline inflation. Green means returns (in USD) beat inflation, and red means returns trailed inflation. Data as of November 30, 2020 close.

Graph source - Daniel Lacalle - Twitter

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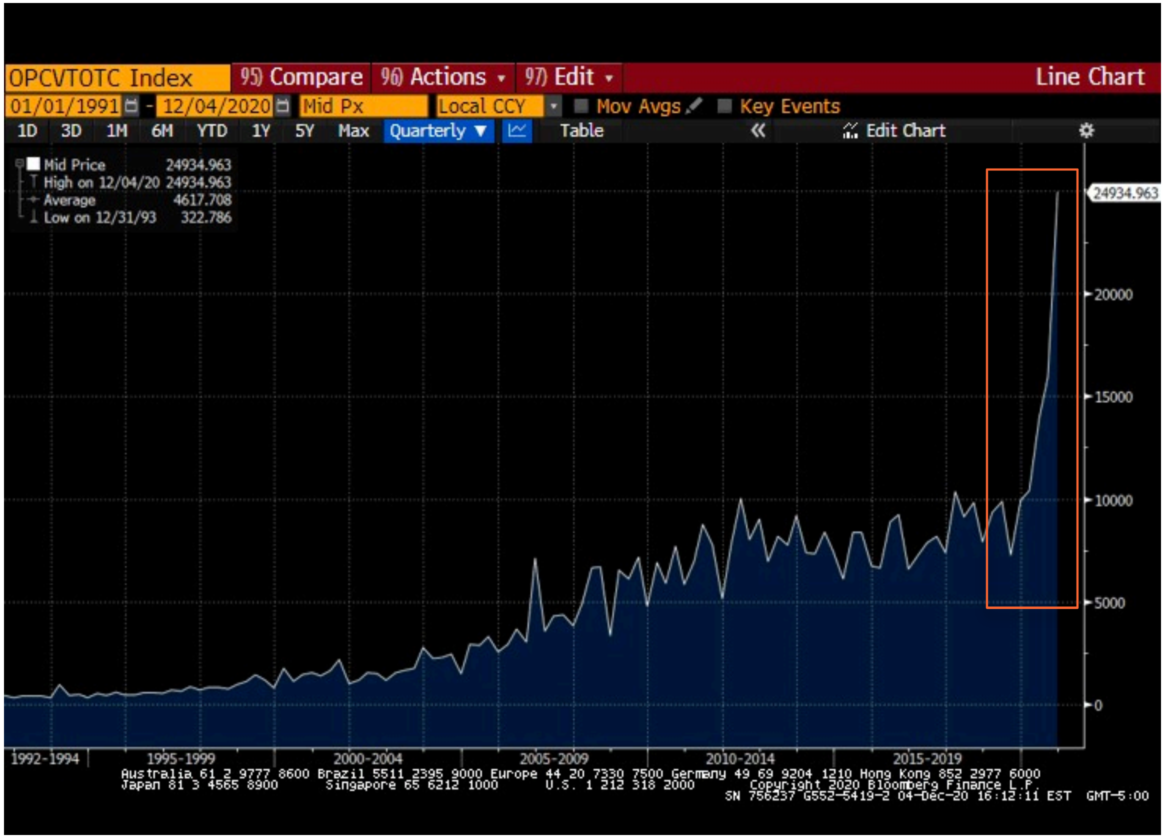
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- Total US call option volume. Biggest bubble of all time.
- Wall Street is getting "greedy".
- Smallest of traders have become the dominant force in the options market. Last week, opening call buys for 10 contracts or fewer accounted for 44% of all opening calls.



Graph source - Bloomberg- Twitter

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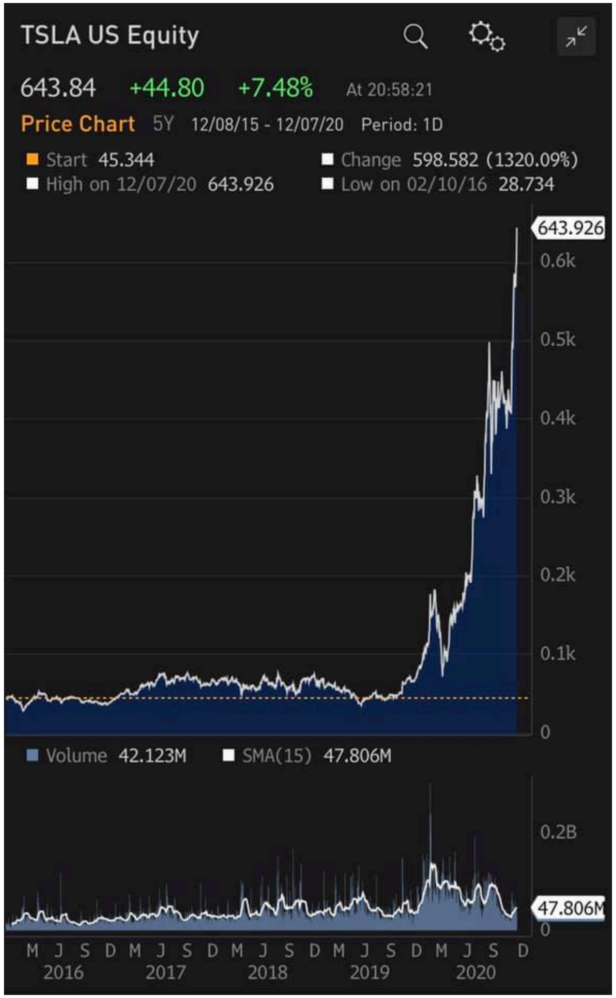
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- TESLA as a poster child of "excessive greed":
- Tesla up 700% YTD

Tesla Market Cap: $609 Billion

Other Autos...
Volkswagen: $96 bil.
Audi: $83 bil.
Daimler: $74 bil.
GM: $63 bil.
BMW: $58 bil.
Ferrari: $52 bil.
Honda: $51 bil.
Ford: $37 bil.
Fiat Chrysler: $33 bil.
Peugeot: $22 bil.
Porsche: $20 bil.
Combined Total: $589 bil.
Data:
@ycharts



Graph source - Bloomberg-

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WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- The “greed” in FANG relative to the S&P 500:

Graph source - Bloomberg- Twitter

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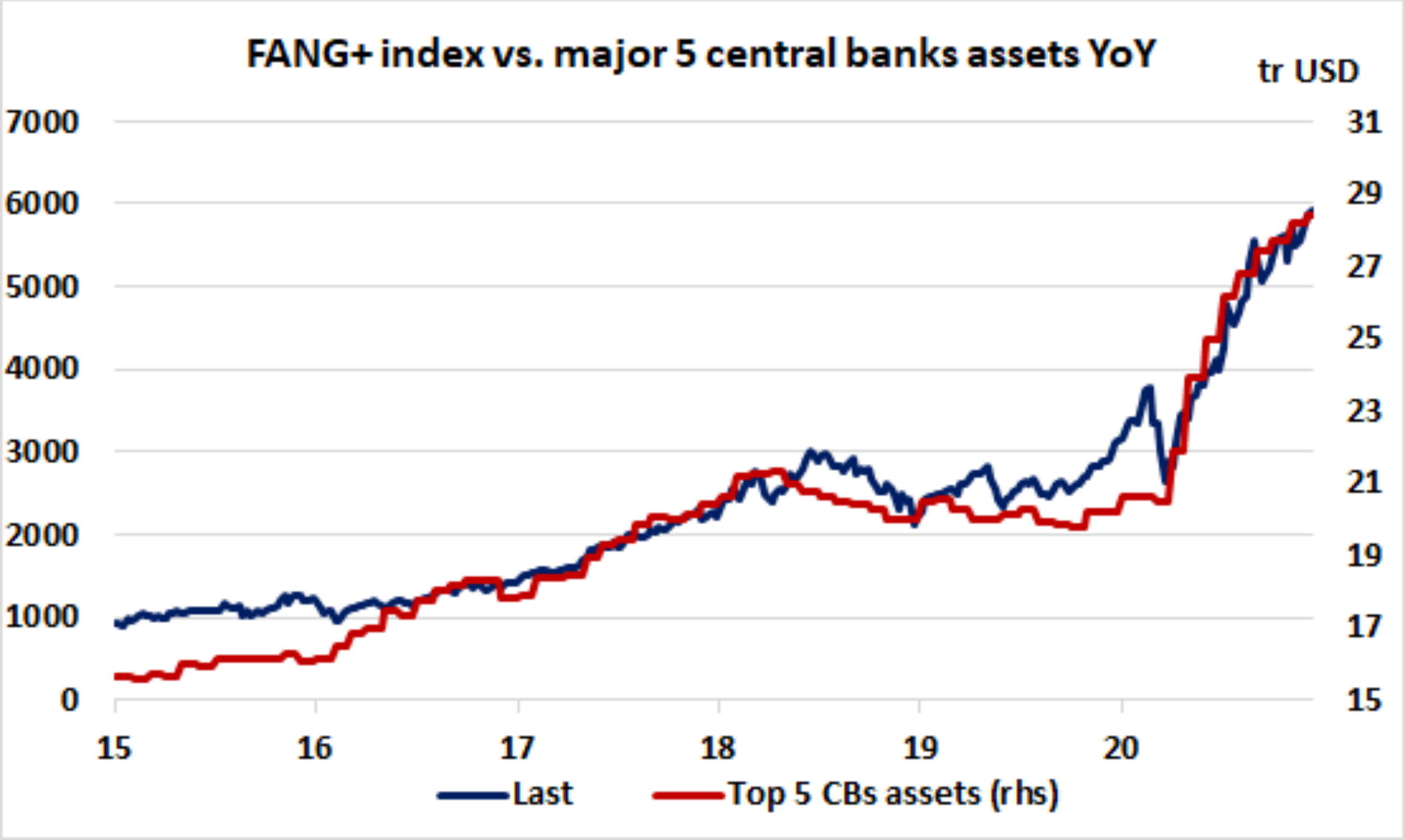
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- The "wizardry" of our central bankers.



Graph source - Rothko Research - Twitter

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WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- US High Yield. Big rally in high beta thanks to the bounce in oil prices favoring the CCCs rating bucket. But it ain't cheap no more for sure.

Graph source - Macronomics - KOYFIN

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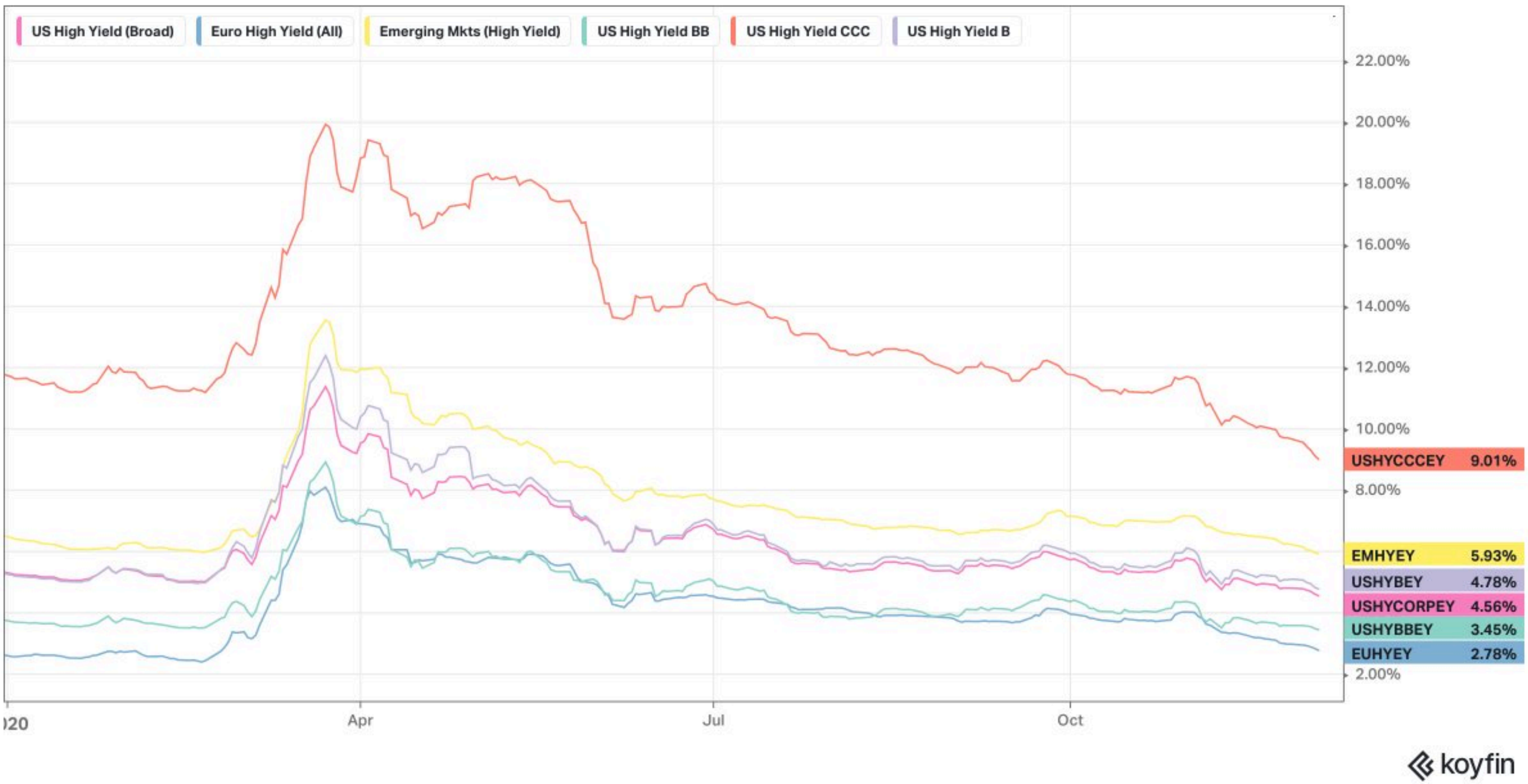
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- Dude where is my yield?
- As long as oil prices continue to rise then US CCCs will find some support as they are now marginally in positive territory YTD in terms of Total Return



Graph source - Macronomics - KOYFIN

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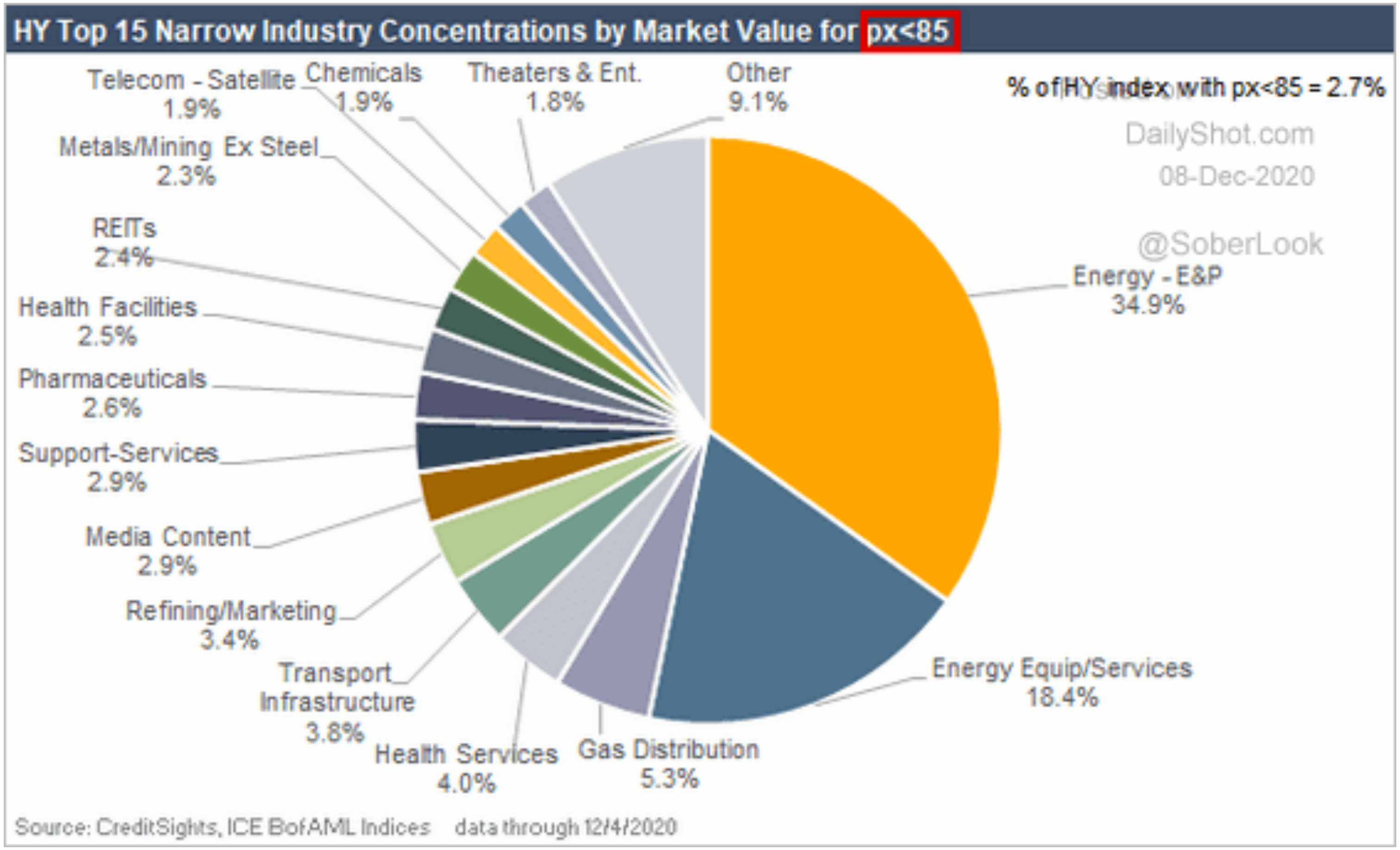
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- "A large proportion of the "stressed names" in high yield (trading below $85) are energy firms."



Graph source -Sober Look- Twitter

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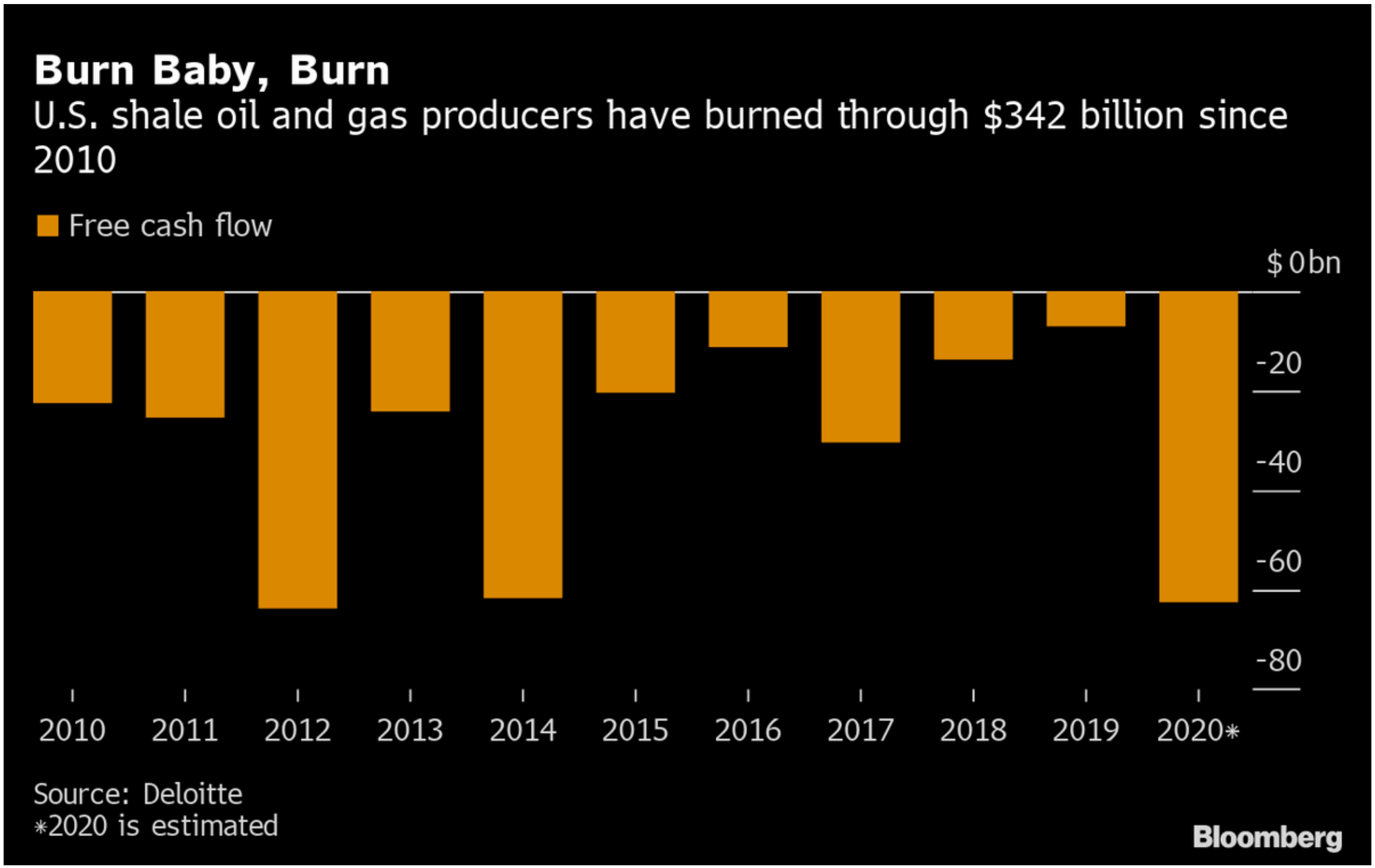
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- US shale has burned through $342 billion since 2010. You find a lot of shale players in US High Yield CCCs…



Graph source - Bloomberg- Twitter

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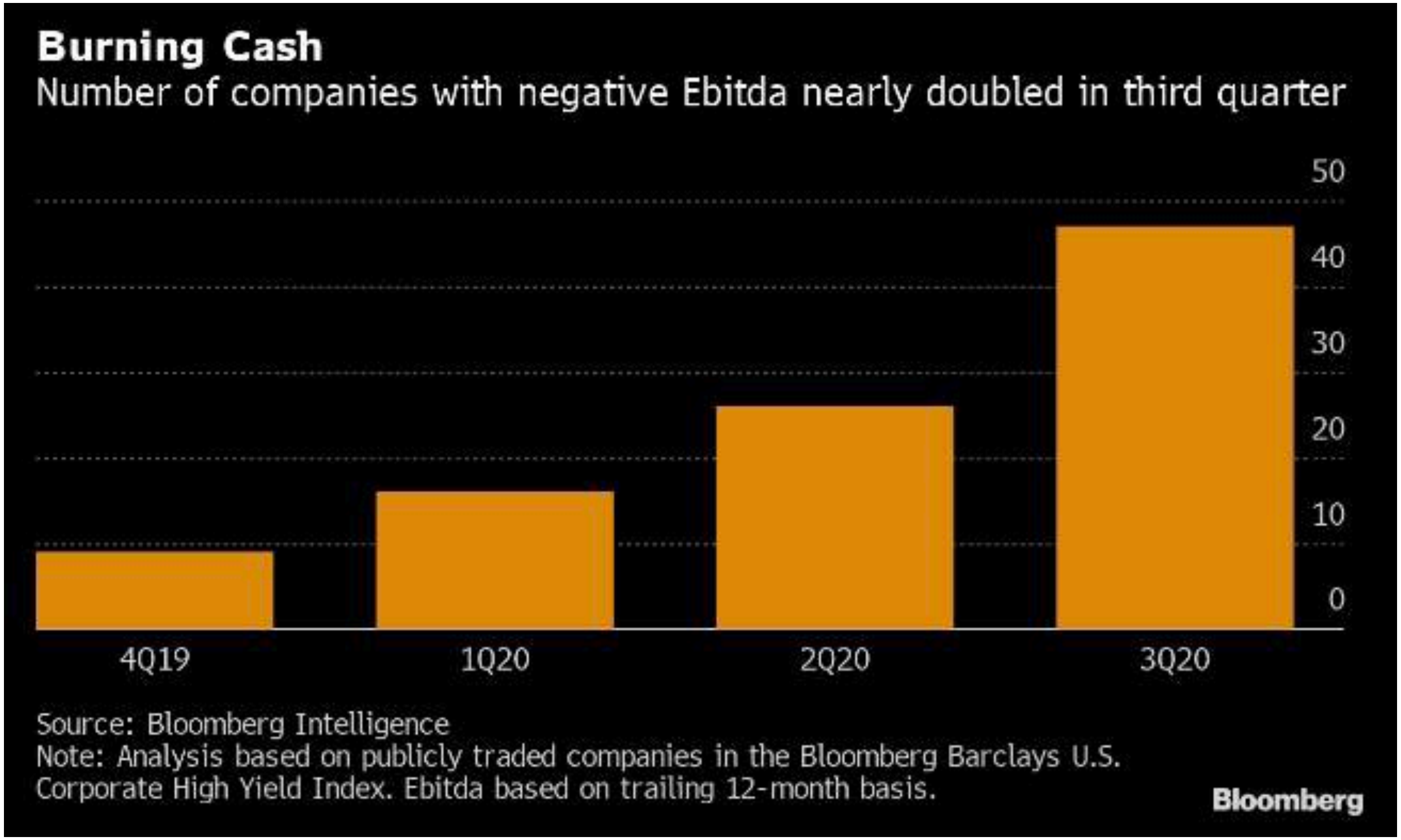
WALL STREET EUPHORIA VS MAIN STREET DYSPHORIA

- Companies feeling cash burn: A growing number of junk-rated firms are losing money before they pay interest and other necessary expenses (like taxes) in latest quarter, number reached 47, double level in 2Q .
- Do you think current spreads are compensating you enough for this?



Graph source - Bloomberg- Twitter

3

MORE SIGNS OF REFLATION / INFLATION

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MORE SIGNS OF REFLATION / INFLATION

- The narrative of inflation's death is premature. Market-implied US inflation expectations have risen near 19 months high. 30 year Treasury breakeven rate hit 2% on Monday.

Graph source - Bloomberg - Twitter

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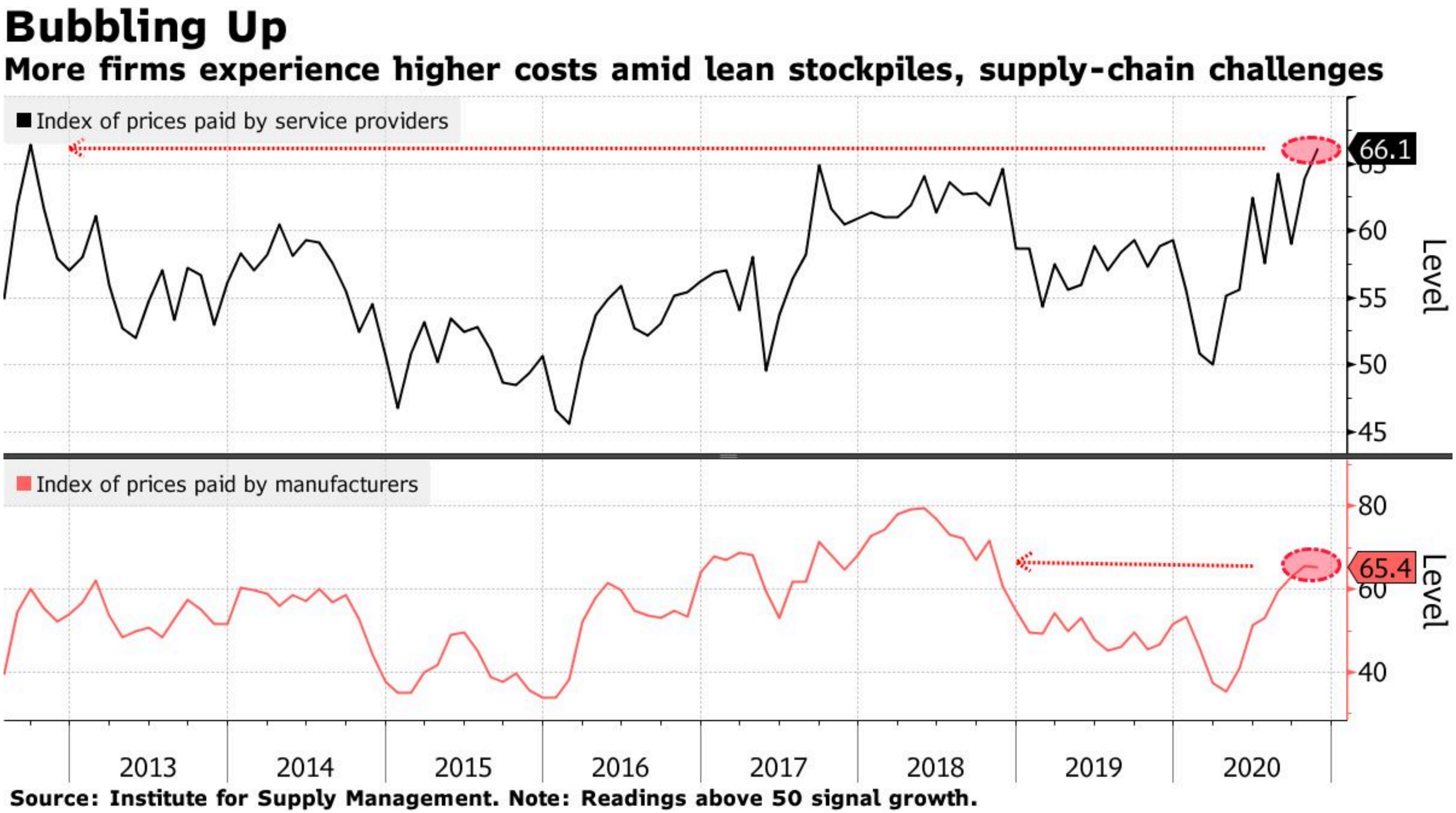
MORE SIGNS OF REFLATION / INFLATION

- This will mean more pressure on prices for the consumer.



Graph source - Bloomberg - Twitter

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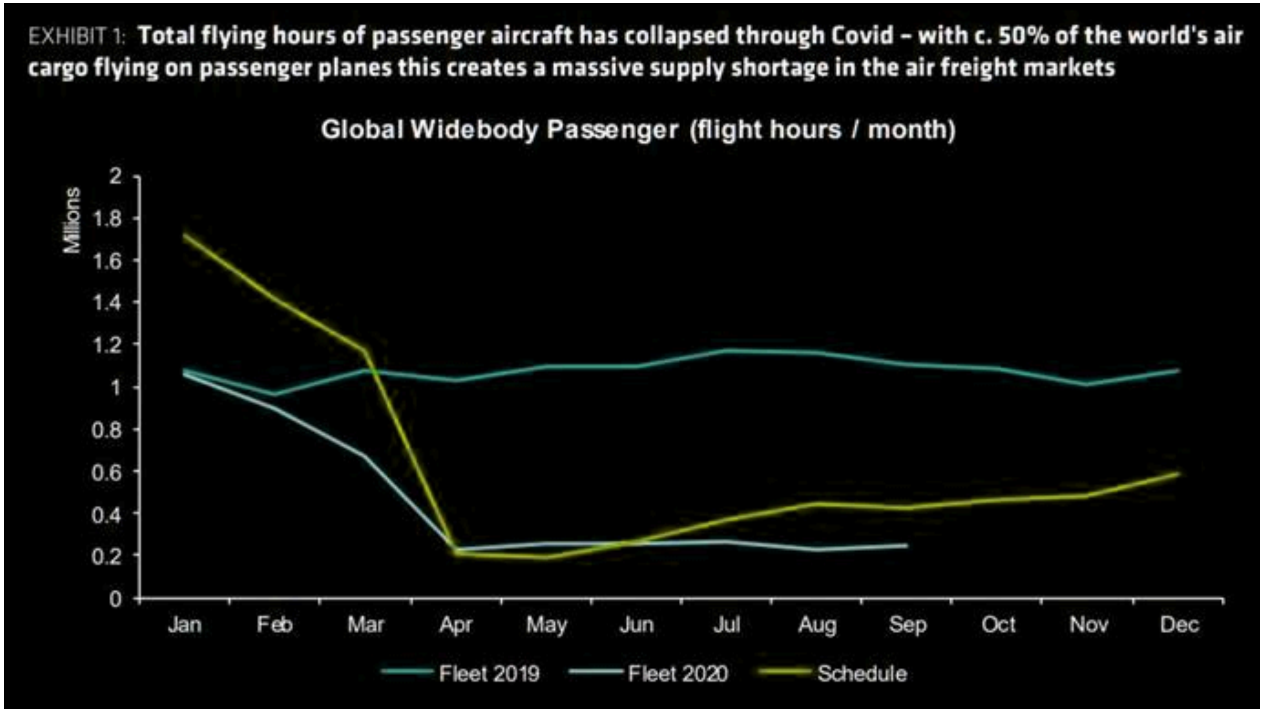
MORE SIGNS OF REFLATION / INFLATION

- "On the theme of "there is always a winner"....Sanford Bernstein shows that tightness in the air freight market will persist for two years. 50% of the world's air freight travels on passenger jets. Global widebody long haul traffic is still -70% in Q4 and we do not expect a full return until 2024, creating volume, mix, and pricing opportunities for air freight carriers, forwarders and express companies. There is no more air freight capacity coming on as the number of widebody freighters remains almost unchanged in Q3. Air freight pricing remains strong at +65%, leading to higher gross profits at all major forwarders."



Graph source - The Market Ear - Twitter

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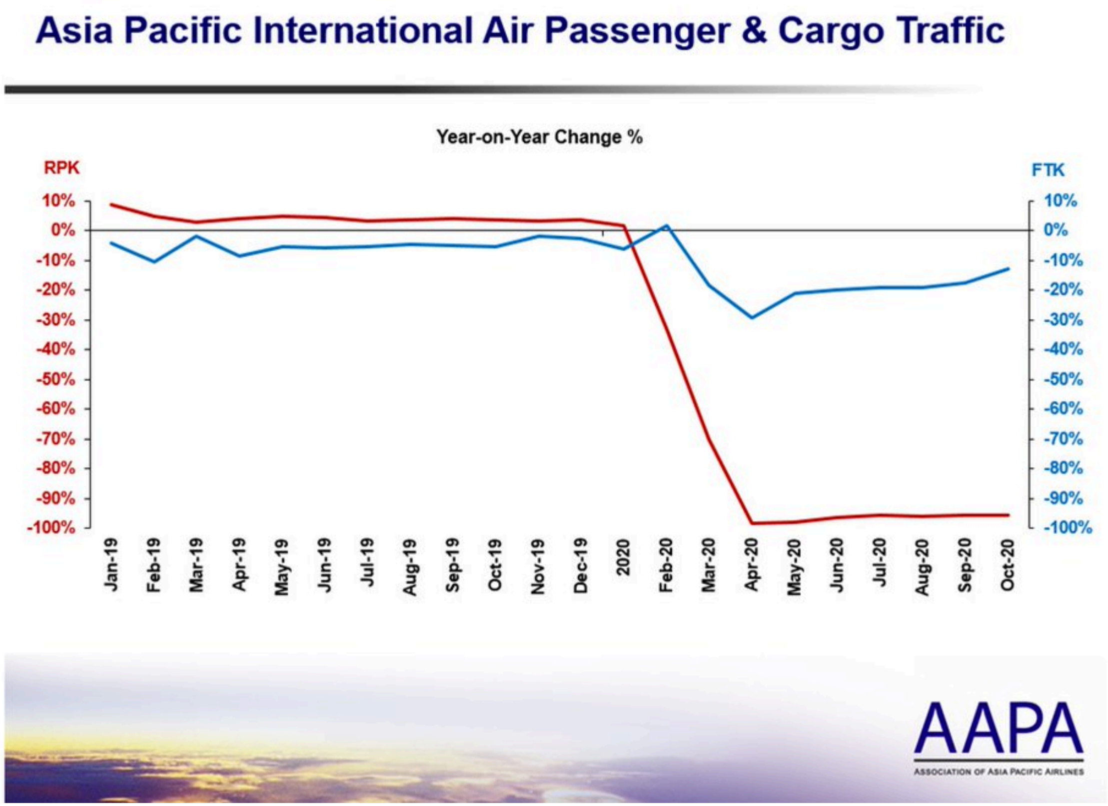
MORE SIGNS OF REFLATION / INFLATION

- "October 2020 traffic figures underscored the devastating impact of prolonged border closures and travel restrictions on international passenger demand, whilst relatively firm demand for air cargo reinforces the need to restore network connectivity given potential capacity shortages." − source AAPA



Graph source - AAPA- Twitter

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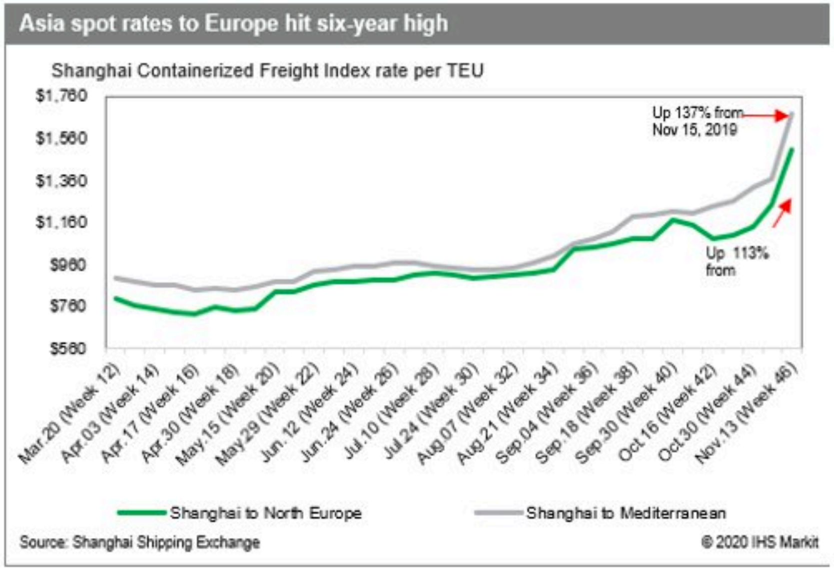
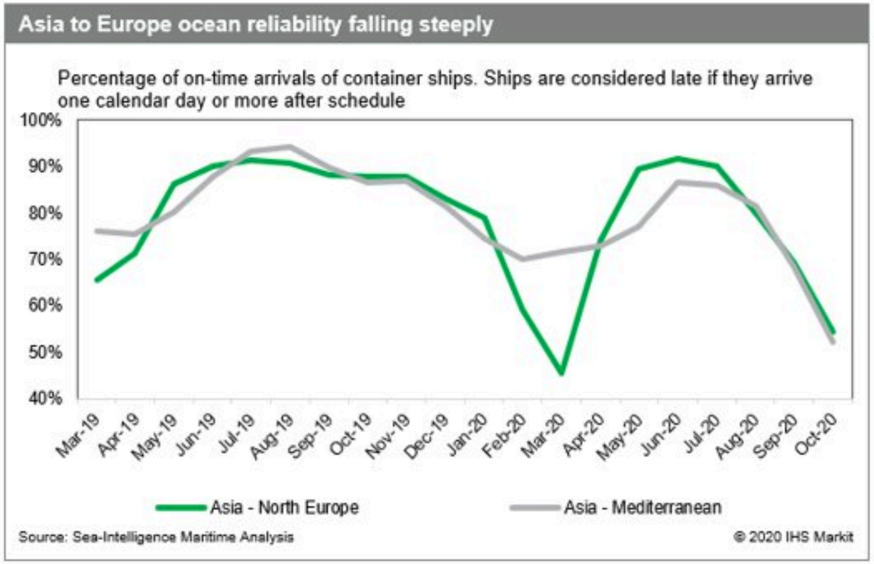
MORE SIGNS OF REFLATION / INFLATION

- "Why is container shipping demand going through the roof this year? The money people would have spent on airlines ($84bn), travel/tourism ($300m), public transport ($100m), etc, is instead going into goods that are made mostly in Asia and moved on ships. But how long can it last?" − Greg Knowler − IHS Markit

- Shipper frustration is growing in the ongoing high rate-low service environment captured by these two charts





Graph source - Greg Knowler − IHS Markit- Twitter

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MORE SIGNS OF REFLATION / INFLATION

- **Import companies say a backlog of empty containers at our ports and not enough ships sailing will mean empty shelves and price hikes by the new year.**
- Shippers have been paying premium rates for container shipping services to secure equipment, but box shortages in Asia are so acute that is proving not to be enough.
- “Container carriers have announced a stream of rate increases and surcharges across multiple trade lanes that will go into effect through December. Unprecedented demand continues to overwhelm the global supply chain and drag container service levels to fresh lows. Box rates are at all-time highs on trades from Shanghai to the US West Coast, Australia, West Africa, the East Coast of South America, and Singapore, and to six-year highs on Asia-Europe.
- In an unusual move, container capacity shortages and high rates have pushed a few service providers to temporarily charter in MPP ships to carry boxes. As MPPs are not designed to optimize container transport, a more typical move to combat high box rates and capacity shortages would be shippers shifting cargo from container to breakbulk modes, as Susan Oatway, Drewry's senior analyst for breakbulk and project shipping, noted in a report Thursday. “Container-friendly MPVs are few and far between,” the report said.
- The Baltic Exchange Handysize Index (BHSI), a measure of spot freight earnings for 38,000-dwt dry bulk vessels, was at 654 on Nov. 29, according to Pacific Basin, up 187 percent from a COVID-19-driven low of 228 in May. “ − source IHS Markit

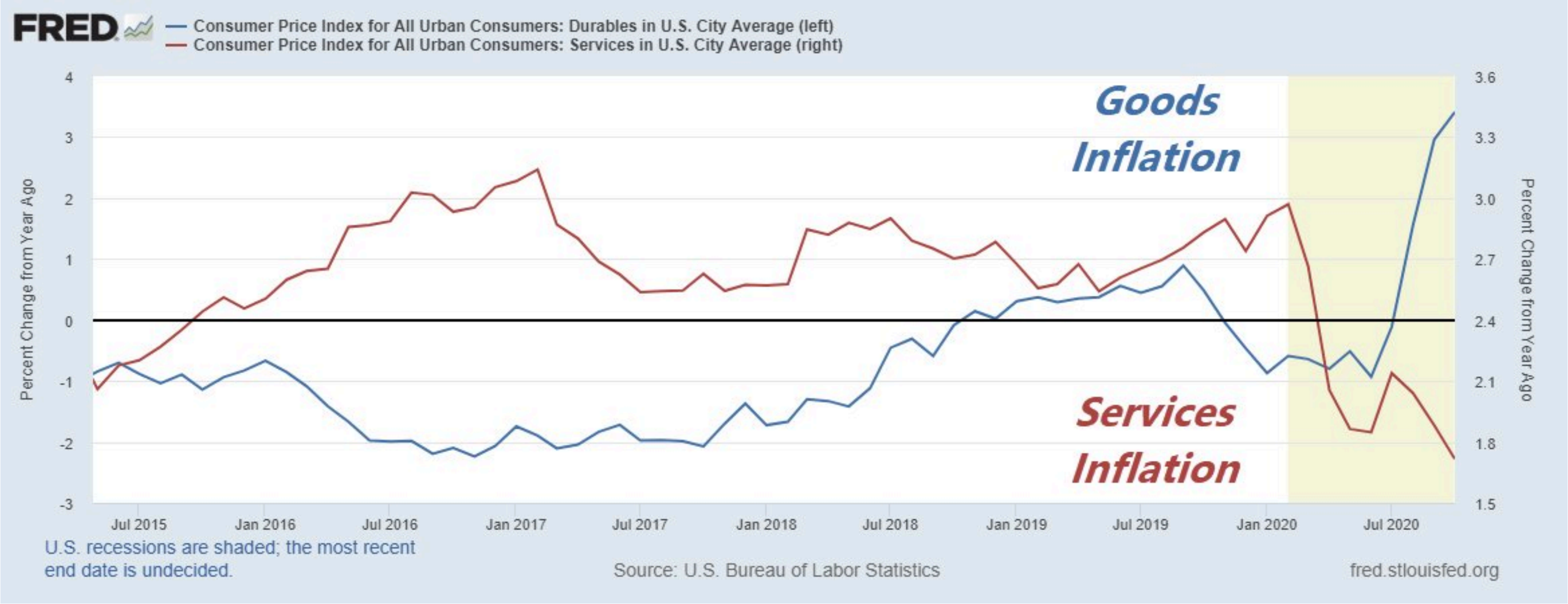
Graph source - The Market Ear - Twitter

MORE SIGNS OF REFLATION / INFLATION

- Goods inflation (manufacturing upturn)

versus

- Services disinflation (social distance rules / changing consumer behavior).



Graph source - FRED – Eric Basmajian - Twitter

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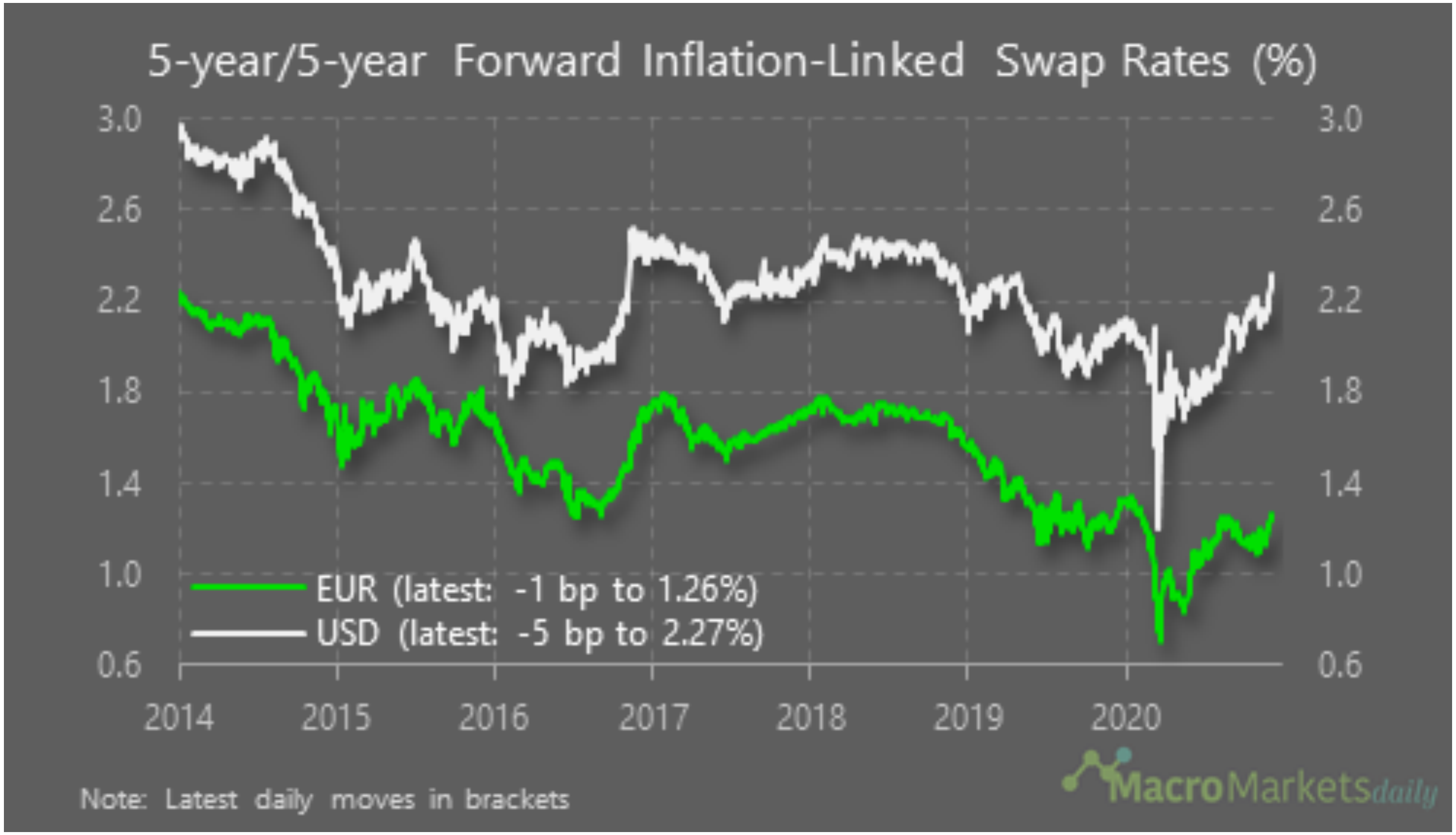
MORE SIGNS OF REFLATION / INFLATION

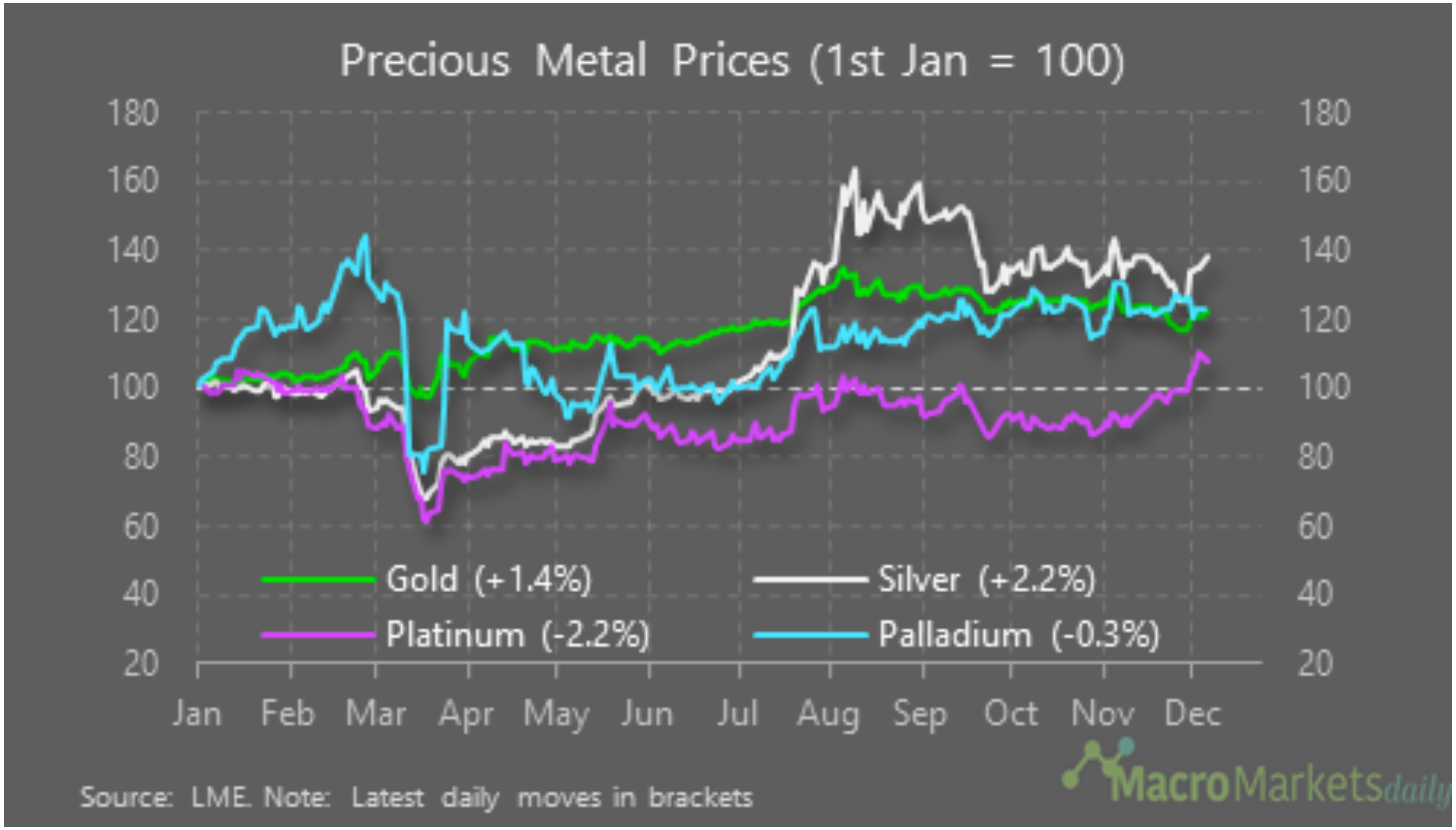
- Why we favor US over Europe?
- Simple, the FED and the ECB followed different paths leading to different outcomes and different credit impulses over the years, leading to different inflation trajectory.



Graph source - MacroMarkets Daily - Twitter

MORE SIGNS OF REFLATION / INFLATION

- Our “BUY” signal was triggered on the 30th of November.
- Gold was oversold in November from a RSI perspective. Now it is bouncing back nicely.
- Gold, Silver and Miners have underperformed in November.



Graph source - MacroMarkets Daily - Twitter

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MORE SIGNS OF REFLATION / INFLATION

- Market Value of Global Negative Yielding Debt jumps more than $500 Billion on the 7th of December to a record $17.57 Trillion.

Graph source - Bloomberg - Twitter

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THE RETURN OF COMMODITIES?

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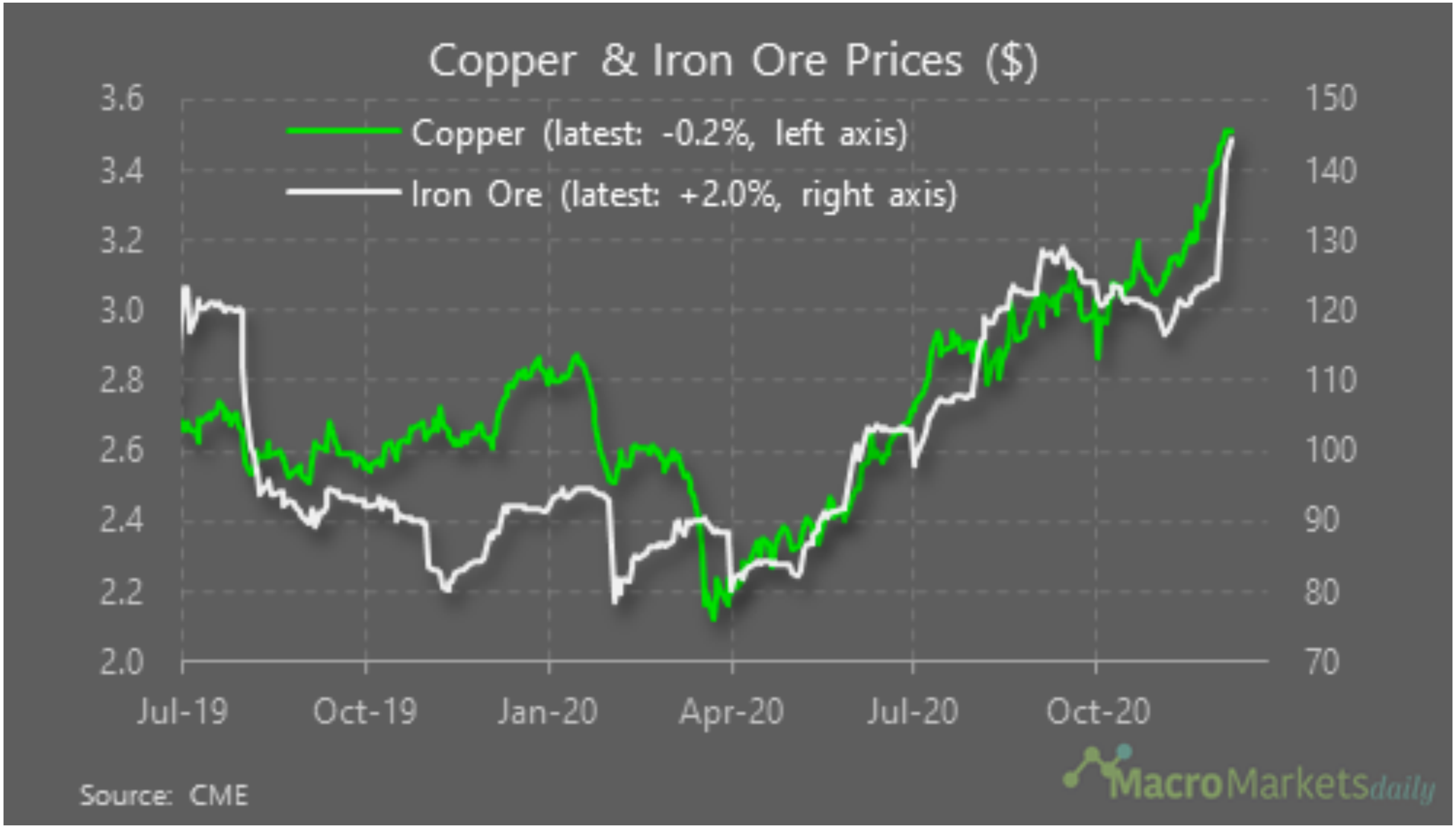
THE RETURN OF COMMODITIES?

- The narrative of inflation's death is premature. Market-implied US inflation expectations have risen near 19 months high. 30 year Treasury breakeven rate hit 2% on Monday.



Graph source - MacroMarkets Daily - Twitter

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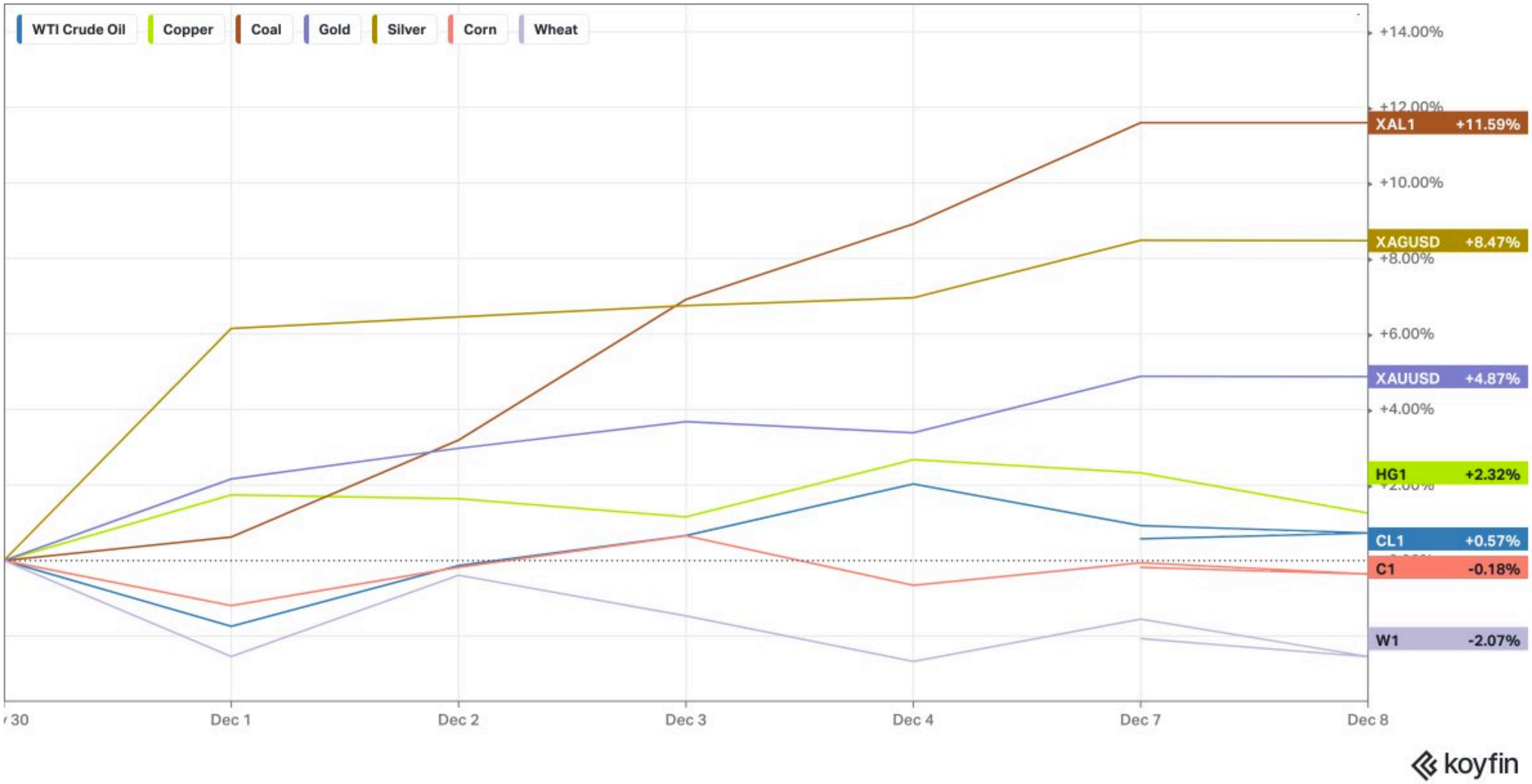
THE RETURN OF COMMODITIES?

- MTD some commodities are rising fast



Graph source - Macronomics - KOYFIN

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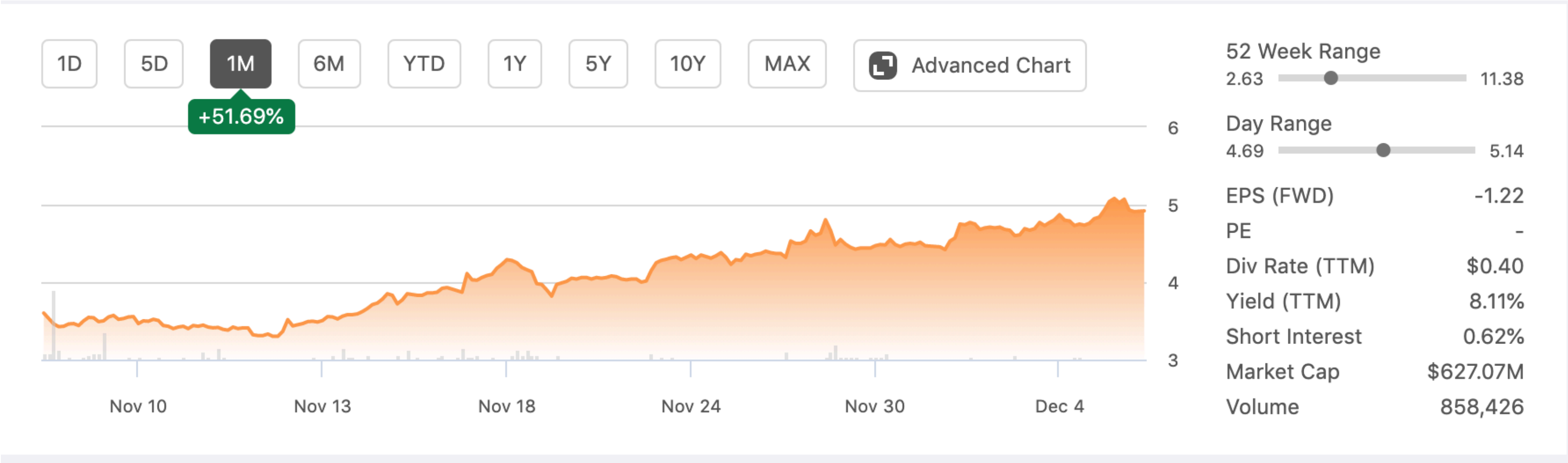
THE RETURN OF COMMODITIES?

- With COAL rapidly surging no wonder ARLP (Alliance Resource Partners, L.P.) is rising fast !
- ARLP with 8% yield is up by 51% in one month. $ARLP was analyzed by 2 analysts. The buy consensus is at 80%. So analysts seem to be mildly confident about $ARLP. Disclosure we do not hold ARLP.



Graph source - Macronomics – Seeking Alpha

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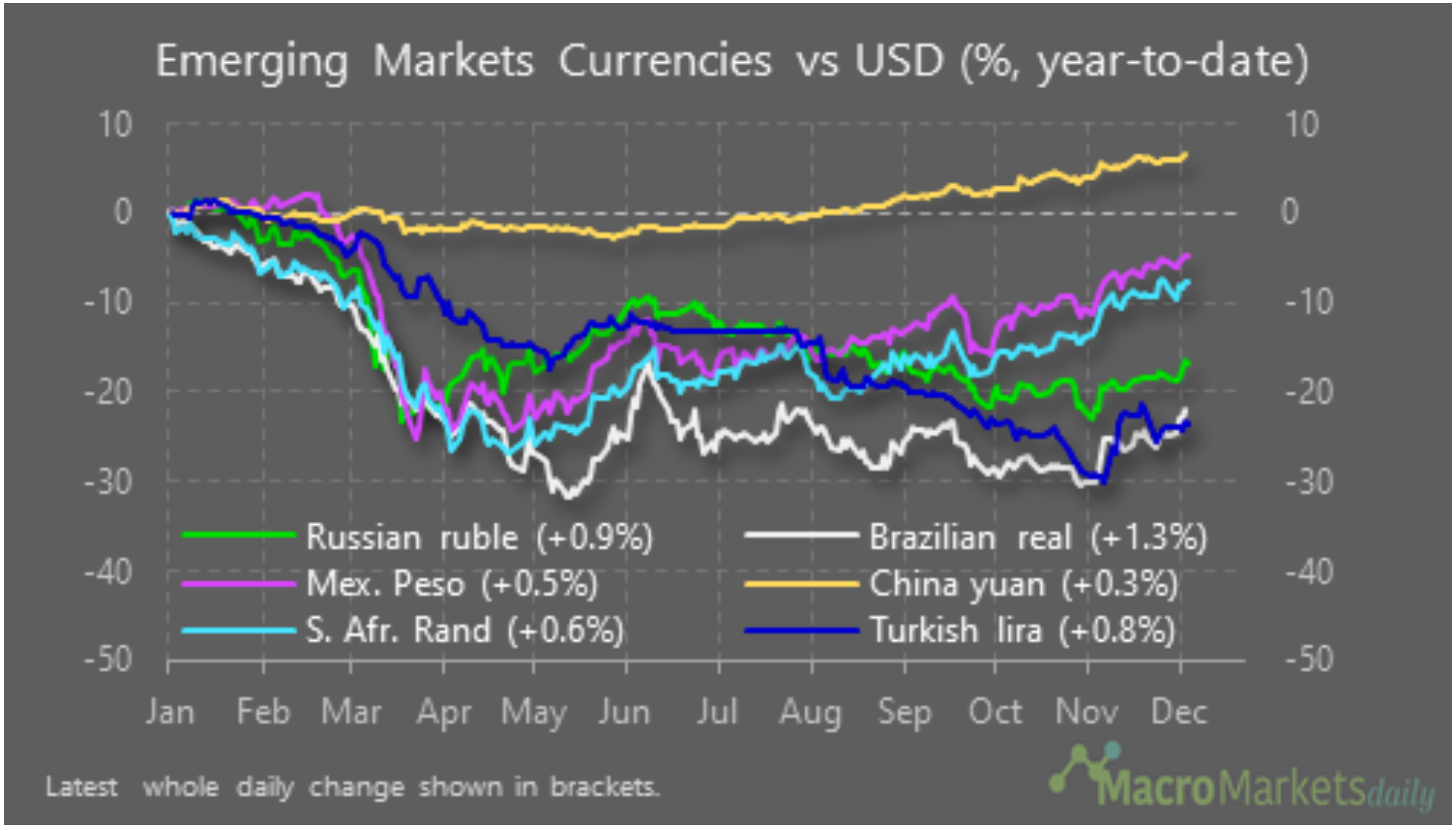
THE RETURN OF COMMODITIES?

- Most Emerging Markets currencies continue to gain ground against the USD.
- Will the rally continue with the weakness in the US dollar?
- We think it will



Graph source - MacroMarkets Daily - Twitter

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THE RETURN OF COMMODITIES?

- “The Brazilian Real started 2020 at $/BRL 4.00, which is easy to forget. So our undervaluation signal for the Real, which says the Real is 20% undervalued and puts fair value around $/BRL 4.50, really isn't all that ambitious, especially when factoring in how healthy the Balance of Payment is...” – Robin Brooks - Twitter

Graph source - Robin Brooks - Bloomberg - Twitter

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THE RETURN OF COMMODITIES?

- 2020 YTD Asset Classes Performance

Graph source - Bloomberg - Twitter

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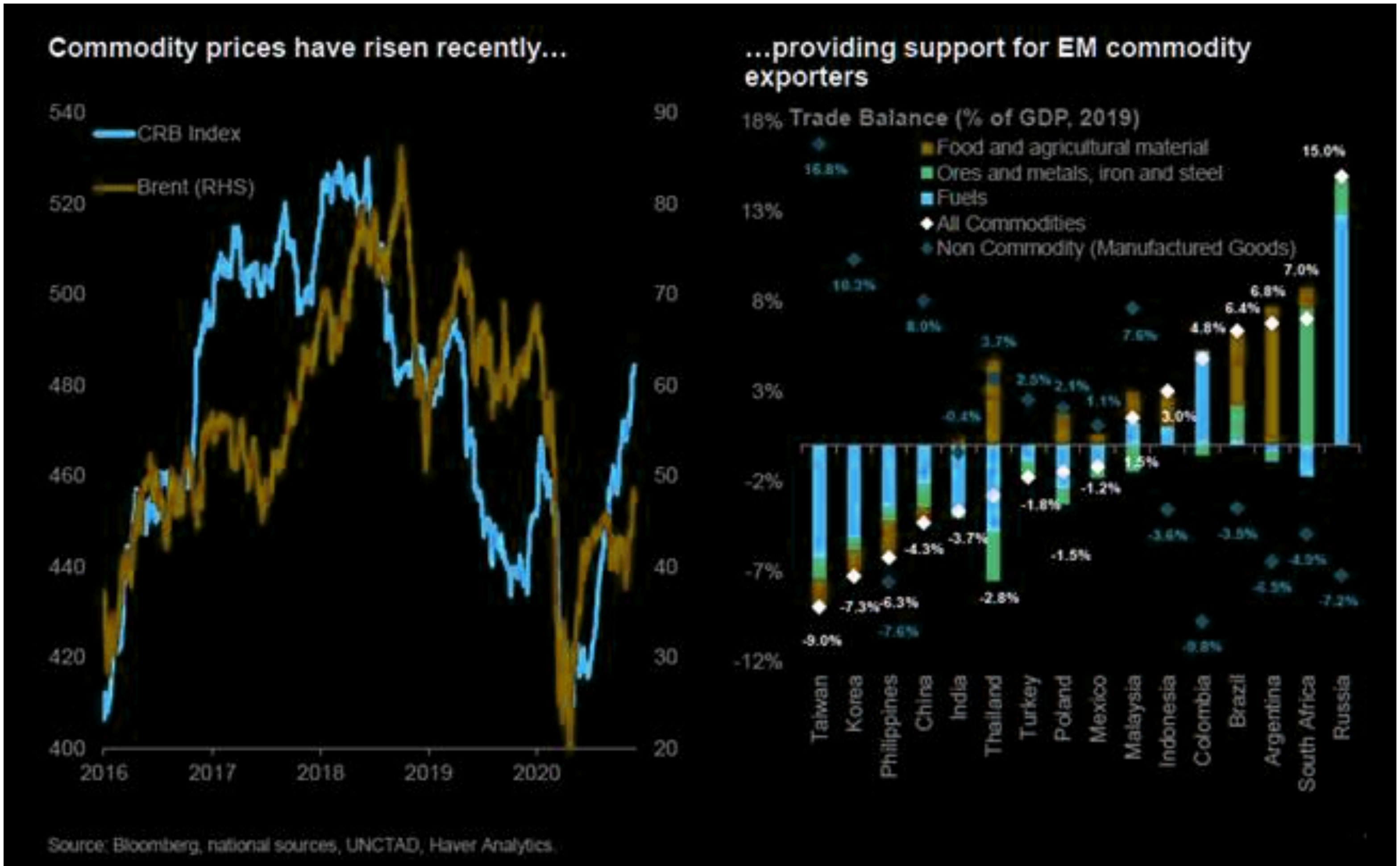
THE RETURN OF COMMODITIES?

- EM Reflation: the next phase.



Graph source - The Market Ear - Bloomberg - Twitter

5 CONCLUSION

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CONCLUSION

- US Main Street is still on “recovery mode” while Wall Street is “full-on greed mode”. Europe is still mired in deflation and underperforming while Asia is doing better. We are seeing more “inflationary” signs with fast rising commodities, hence our favor towards Emerging Markets commodities player such as Brazil and Russia.

- Credit wise it is still “risk-on”. November’s rally has been very strong particularly for the weaker CCC rating segment in US High Yield thanks to a bounce in oil prices. Given liquidity doesn’t equates solvency, ask yourself if you are compensated enough for the risk. For CCCs we do not think you are at the current spread levels but with growing negative yielding bonds, maybe after all it is TINA (There Is No Alternative) and people are extending credit risk.

- Given shipping markets are very tight, we expect “pricing pressure” to build on, hence our rotation from the “deflationista” camp throughout QE towards the “inflationista” camp with more fiscal spending in the pipeline.

- Following oversold conditions for gold, our buy trading signal was finally triggered on the 30th of November. As well from an historical point of view, January is traditionally strong for gold prices from a seasonality perspective.

- Sure, High beta benefited from the strong support from COVID-19 vaccine narrative but given this narrative is slightly fading and given the strong rally seen, taking some profits on some beta plays could be wise we think even if many points out to yet another Santa Claus rally in the making.

BIOGRAPHY

- **MARTIN TIXIER** is the author and founder of the blog "Macronomics" (http://macronomy.blogspot.com) launched in December 2009 and focusing on Macro trends in general and credit in particular. His blog is in the top 20 economic blogs in the United Kingdom (http://uk.labs.teads.tv/top-blogs/economy) and receives around 20,000 views per month.

- Mr. Tixier has served as Senior Fixed Income Investment Specialist in the asset management industry for CANDRIAM, a leading pan-European multi-specialist asset manager managing €80B AUM at end of December 2014

- Mr. Tixier was awarded the highest accolade for a Six Sigma project in 2006 for Bank of America where he worked 7 years in various positions. He won the coveted Best of Six Sigma Award (top 15 projects out of 1500 submitted globally).

- Mr. Tixier graduated from the top ranked ESSEC BBA as well as ISC in Paris where he obtained a Master degree in Business Engineering and International Trade. Martin is a certified CISI Level 3 FCA (Financial Conduct Authority) in Regulation, Securities and Derivatives and also has the ACI Dealing Certificate with distinction and is as well as a certified Six Sigma Green Belt.

- Mr. Tixier has also been lecturing at IAE Lille and Toulouse Business School for post graduate students dealing on the subject of banking regulations and accounting practices and the role of credit in the economy as well as interest rates and credit trading strategies.