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ROHR ALERT!! BoE and US Employment Win-Win?

1 message

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Dear Subscribers,

In its early morning (literally overnight US time) Monetary Policy and Financial Stability Report announcements (<https://bit.ly/3a3IPYZ> for the summary page with links to the full reports), the Bank of England was clear on its commitment to further liquidity and economic support. It kept its Asset Purchase Facility at the full £745B, yet held off on moving its base rate from 0.10% into negative territory. We consider that enlightened, as similar moves elsewhere have not really done much to stimulate real economic growth, and have created problems for banks.

For a very good summary of their actions and views, please see this morning's Reuters news flash (<https://reut.rs/3gzbF52>.) Regarding negative rates, the article notes the BoE message that, *"...(central) banks in countries which have cut rates below zero were often limited in their ability to pass on lower borrowing costs to lenders and feared negative rates would erode their capital."* This has been borne out by the dismal longer-term experience in both the Euro-zone and Japan.

The good news is that it was less downbeat on near-term prospects for the UK economy on the upward revision to *only* a 9.5% drop in the economy this year, versus the May estimate of a 14.0% annualized drop in 2020. Yet, much like the Fed, it is still quite negative on overall employment and economic prospects over the intermediate-term... also again on the low prospects for jobs (especially at the lower end of the employment curve) to return to industries where businesses have diminished or permanently closed (like dining, hospitality and others.)

The bottom line is continued extensive accommodation support from central banks will continue, underpinning equities, even if not really doing much in its own right to restore economic activity. And the central banks are falling into the 'normalcy bias' charade once again on their projections of higher inflation.

The Bank has promoted the idea that UK inflation will be back up to its 2.0%, just as Fed Chair Powell recommitted the Fed to seeing inflation up to a similar level prior to raising rates. With inflation and economic activity well below targets at present, this is a bit of wishful thinking, and a way to bamboozle the public into thinking central banks can drive economic growth to a level which would foment that sort of inflation. Even if it sounds good, it is simply just not the case.

It reminds us of the early-2015 through early-2016 Yellen Fed warnings that it would need to raise rates soon because the previous stimulus was just about to trigger stronger growth. It didn't happen until the later tax and regulatory changes actually stimulated economic activity the central banks do not control.

Unless the Fed or BoE can actually conjure up a confidence restoring COVID-19 vaccine, the chances they alone can drive better growth is somewhere between slim and none (and

as the classical joke says, “...and Slim just left.”) Just think about how long the ECB and BoJ have been touting the effectiveness of their negative base rate policies with little or no impact on overall economic growth.

What we know is that the excess liquidity does perform the function of assisting the US equities (and others to some degree.) Last Friday morning we noted the ‘Liquidity Bifurcation’ of the different asset classes psychology, On the further push up in US equities on Monday we titled our ALERT!! ‘Liquidity Rally’. And it has continued to extend to new near-term highs despite the continued bad news on the US COVID-19 pandemic becoming “*extraordinarily widespread*” (thanks to Trump COVID-19 Task Force Coordinator Dr. Deborah Birx for that one.)

As noted in Monday’s ‘Liquidity Rally’ ALERT!!, there is something to be said for the degree to which the extreme Fed (and other central bank) accommodative liquidity actions inject enough money into the system to foment redirection of many investments from no-yield bonds into the US equities (and others.) There is also a longer term modest inflation advantage for equities in the form of a new business entrant competition barrier. (See Monday’s ALERT!! for more on that.)

The further actual ‘good’ news this morning (even if in reality it is only less ‘bad’) was the quite a bit lower-than-expected US Weekly Initial Jobless Claims: a mere 1.186 million versus a 1.415M estimate. That was reinforced by the also slightly lower-than-expected US Weekly Continuing Claims at 16.107 million. Those remain at very high levels, even if the trend looks somewhat constructive.

The question now is whether Friday’s US Employment report sees the Nonfarm Payrolls number hit the estimated 1.60 million gain, or was Wednesday’s ADP Employment Change plus 167,000 major undershoot a warning sign on the Friday number’s prospects? Yet does it really matter to the US equities? This gets back to the still stalled highly partisan US Congress relief package negotiations.

If the Nonfarm Payrolls are as good as expected, it will give the Republicans grounds to point to still recovering economic performance. That may assist them in resisting the Democrats’ demands for much higher relief spending, yet also encourage the US equities. Yet if the number is well below expectations, it will provide the Democrats more momentum on their higher relief spending demand.

As such, whether stronger or weaker than expected, and partially based on the continued major central bank accommodation in any event, the US Employment report is likely just an ‘event horizon’ on the way to at least a further near-term rally in the US equities. The impact on the other asset classes might be more classical, with either pressure or elevation of the global govies and emerging currencies more directly tied to the strength or weakness of the US economy.

This is the critical consideration

COVID-19 virus spread caused US equities intermediate-term bull psychology to ‘crack’. Early March already saw front month S&P 500 future back below key congestion around the mid-2019 3,030-00 previous all-time high congestion. That was below support from the push above the multi-year topping line at 3,070 as well, and left a late-February intermediate-term up channel 2,970 DOWN Break.

The subsequent DOWN Break below the front month S&P 500 future 2,600 area major up channel seemed to indicate more of a near-term failure. That was from the early 2016 low

(<https://bit.ly/3i0r5j1> updated through Friday.) That was then the key higher resistance subsequently violated on its mid-April push above its 2,675 trading high Tolerance from prior to the DOWN Break (also monthly MA-48.)

The front month S&P 500 future pushing out of the broad higher range top in the 3,030-2,970 area in early June was the key to it surging to the 3,200 area. That was the next meaningful higher resistance with a 3,230 Tolerance at which it failed previously on the current rally. That is also where it stalled all three days after the early June US Employment surge with no sign it was going to push further after the June 10th negative OECD indications and disappointment with the FOMC.

And it remains a very prominent technical area, which it has just pushed above. After churning recently around the 3,100-30 interim congestion in the middle of the 3,030-2,970 and 3,200-30 ranges rallying above 3,230 despite the expanding US COVID-19 concerns was a strong indication. Even though sinking back below 3,230 two weeks ago was a cautionary sign, the weekly Close above that level seems to reinforce an overall UP Break. Back below 3,200 (and especially its Tolerance at the 3,187 previous DOWN CPR signal) would still indicate a 'false' UP Break, which could signal an important near-term top.

However, as it is now managing to press higher, next resistance is the February 24th major gap down from the February 21st 3,339.25 weekly Close. That is also key congestion as higher resistance, even if the gap begins at the 3,312 high of the following week (established Monday of that collapse week.) The only nominal resistance above that is February's 3,397.50 front month future all-time high.

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