TOP DOWN CHARTS

Weekly Macro Themes

End of Year Special Edition - 2020

"The End of Year Special Edition takes a different format to the usual weekly slide deck, and presents you with highlights, reflections, and some of the best charts of 2020. I sincerely hope you enjoy it!"
-- Callum Thomas, Head of Research and founder of Topdown Charts

Topdown foreword: What an interesting year... We got to learn a lot: what a tail risk is like, how fragile the global socio-economic-market system is, what a one-off acceleration of existing structural themes looks like, and in many ways: how we and those around us respond to a crisis.

It also provided an abundance of opportunities for active asset allocators, and frankly provided an opportunity for my process to shine. While I have to say that the crash caught me a little off guard given my bullish views at the start of the year, I believe I pulled through in highlighting the opportunities and providing a chart-driven independent voice of reason.

2021 looks set to deliver a new set of challenges and opportunities, some of which I highlight in this report. I hope you will enjoy this selection of charts which I have meticulously collated from reviewing all of the Weekly Macro Themes reports of the past year. As an exercise in reflection, this has been personally very useful, and given me a number of ideas to elevate my craft.

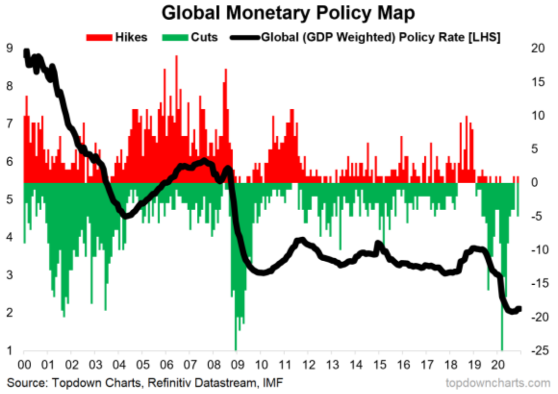
Best wishes for 2021, I look forward to catching up with you soon.

Section A. Charts That Worked

First up is a look at some of the charts and calls that worked particularly well during the year.

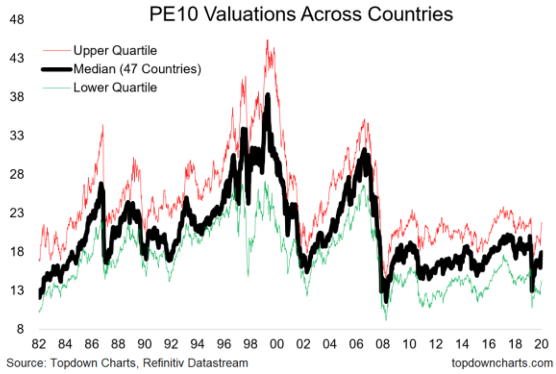
1. It quickly became obvious that a second global wave of monetary policy easing was on the way:

"The global policy pivot was one of my key themes in 2019, and it proved instrumental in a number of key calls, and was starting to take hold with a number of confidence/activity indicators starting to recover. As we know this has been complicated, and with that complication has come a new wave of easing call it the policy pivot part II [PP 2]. Obviously, the Fed emergency cut is the big one, but it adds to a total 21 rate cuts this year 71 last year), and with likely more to come." (6 mar 2020)



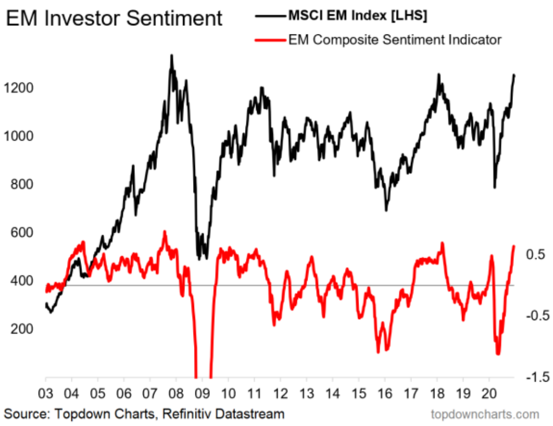
2. Along with that wave of truly historic global monetary (and fiscal) policy easing, sentiment had collapsed, and valuations returned to 2009 levels, prompting me to point out the generational buying opportunity that it plainly represented.

*"the median PE 10 ratio has dropped to the lowest level since the financial crisis. Although we could argue about what counts as "cheap" we can at least say there has been a spike in the number of countries whose PE 10 is below the 15 x mark. So, at this point it is true that we can debate the impact (duration/magnitude) of the pandemic, but one piece of factual information is that global equities have moved to extremely cheap levels, and represent compelling value (*the usual caveat that cheap can get cheaper applies)."* (13 Mar 2020)



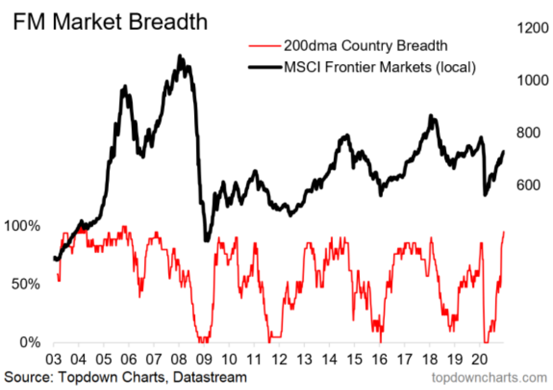
3. As noted, sentiment had collapsed, and a key example was emerging markets. This was one of those times where an extreme reading in investor sentiment provided important and actionable contrarian information. Interestingly, we now find ourselves back at the top end of the range.

"investor sentiment on Emerging Markets has completely flipped from heightened optimism to extreme pessimism (which is a contrarian bullish signal). On the technicals, EM equities have begun to rebound after market breadth collapsed to washed out levels, which in the context of the sentiment + policy + valuations picture is a positive sign." (10 Apr 2020)



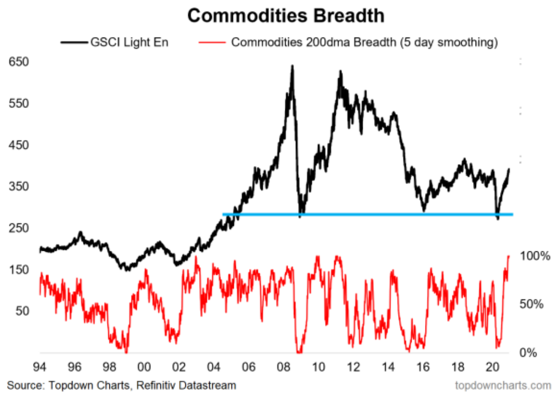
4. Aside from emerging markets, Frontier Markets also began to look particularly interesting. Along with solid technicals, they had also begun to look attractive from a valuation standpoint, and with a number of very interesting strategic features – which I had been adding further colour on through the year, and continue to work on the research.

"market breadth has collapsed for frontier markets, with the 52-week new highs minus new lows indicator dropping to 2009 levels, and 200dma breadth likewise falling to oversold levels. Notably the MSCI Frontier Markets index (in local currency terms) is starting to stabilize at a key technical level." (10 Apr 2020)



5. Closely related, commodities had collapsed, and were teetering on a key decade+ support line. Breadth was washed out, valuations cheap, and sentiment shaken significantly. Thus, from my point of view it ticked all the boxes for a high conviction bullish medium-term position.

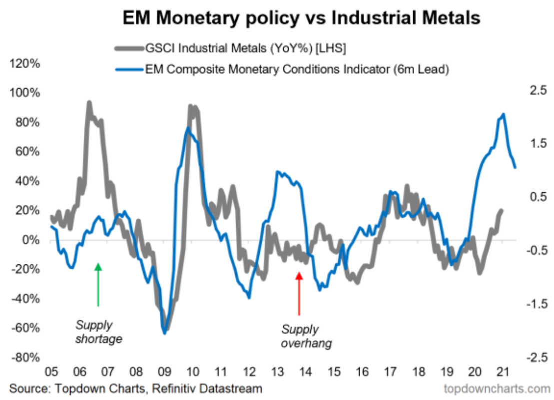
"some of the tactical indicators are looking interesting: breadth is washed out, commodity volatility has moved far beyond 08, positioning has come down a lot (both in the surveys and futures positioning data), and the GSCI light energy is holding support (for now)." (13 Mar 2020)



6. Well, this one could easily have made it into the ones that didn't work, because I featured it back in January – thus it was initially wrong, but ultimately became more compelling as EM central banks ventured into QE, and indeed was ultimately right.

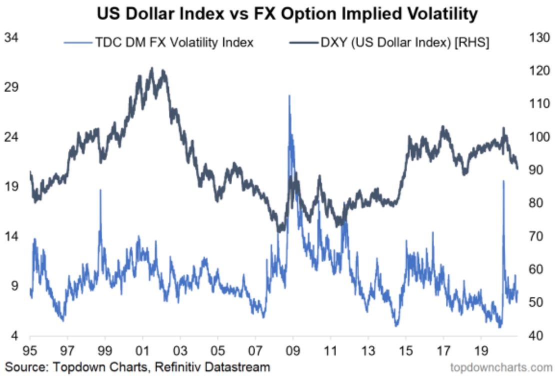
"historically there is a tendency for EM monetary easing to lead industrial metal price returns" (first featured on 17 Jan 2020)

"The substantial policy easing both late last year and again this year with the pandemic policy response has injected a lot of potential energy for metals. I would note in passing, that while China has been doing some easing, it's the rest of emerging markets which have been doing the heavy lifting on the stimulus front" (19 Jun 2020)



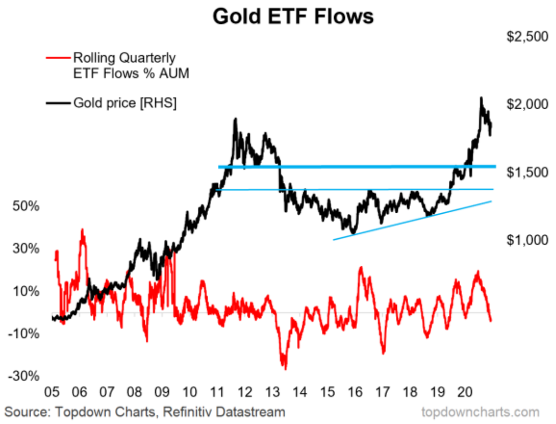
7. What a wild ride for the US dollar. I began the year with a bearish view on the US dollar given the technicals, progression of longer-term cycles, valuation, positioning, and policy picture. I had my conviction tested during the peak of the panic when the DXY made a false upside breakout, but stuck to it. The interesting thing on this chart is it basically nailed the turning point… certainly one to keep an eye on in the future!

"…also note the implied volatility chart: volatility compressions have been seen prior to both bullish and bearish moves)," (17 Jan 2020)



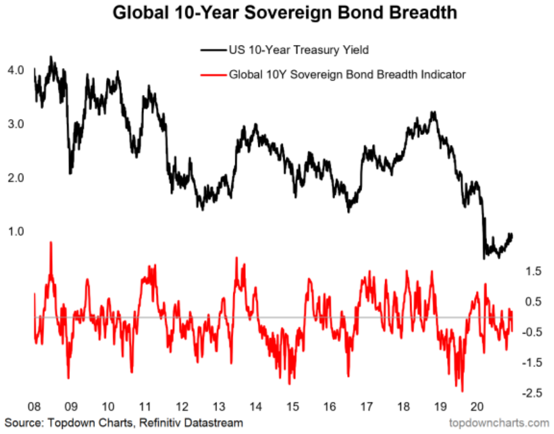
8. Gold was also very interesting. I'm a perma-pragmatist when it comes to gold. I believe the best thing to do is focus on the cyclical/tactical view. I basically went with the breakout, and extended the view to bullish gold miners. Interestingly though I decided to flip to bearish in early October as the tactical indicators flipped to excess optimism, and the technicals turned.

"gold has a couple of short-term signals looking interesting. At the time of writing gold has managed to hold onto the break above 1550 (with a couple of false starts at heading higher in attempt at clearing the key 1600 mark). Gold ETF flows have fully reset from excess optimism to slightly negative," (24 jan 2020)



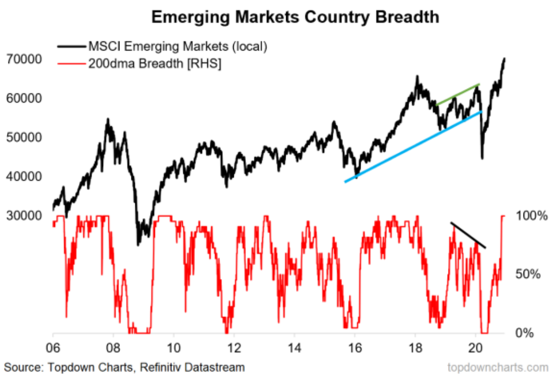
9. These last two are about a couple of tactical views headed into the crash. I would say I was perhaps too optimistic on the core views, but at least managed to catch the short-term bullish indicators for treasuries when yields were back above the 1% mark. I didn't pound the table on it, but I did at least flag it as a possibility.

"short term there are a couple of tactical indicators giving bullish signals for bonds. For example, global sovereign bond breadth has rolled over from oversold levels," (24 jan 2020)



10. Again, while I held onto my core bullish medium-term view for emerging market equities, I managed to flag a couple of emerging tactical risk signals, such as the one in this chart (as well as bearish divergence on the S&P500 and EMFX). But I do admit I never imagined how fast and furious it would ultimately unfold!

"note the bearish breadth divergence signal in emerging market equities, where in local currency terms the MSCI EM index made a higher high (note the green line) but the 200dma country breadth indicator made a lower high. This kind of pattern can help in flagging turning points so while I remain bullish medium term on EM equities, it's not one to take lightly from a risk management standpoint" (14 Feb 2020)

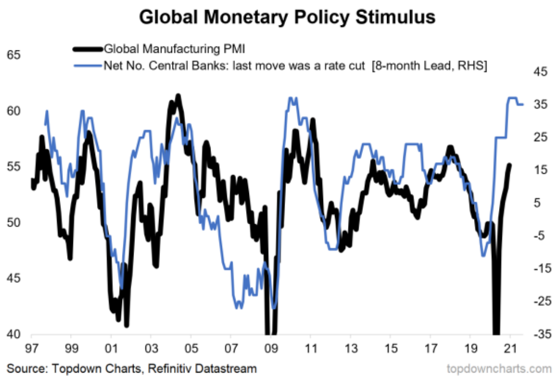


Section B. Charts That Didn't Work

Of course, it wouldn't be complete without a look at some of the charts that didn't work (or shall we say the ones that worked "less well!").

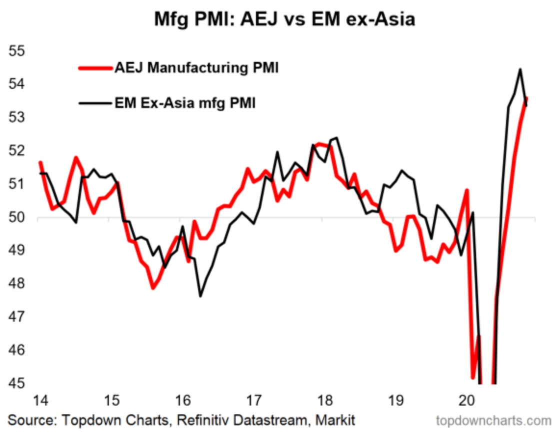
1. This was one of my most famous charts of the previous year, it was one of a number of reasons I left 2019 with a bullish view on global growth... And then Covid happened. The global manufacturing PMI resolutely fell off the page. Ultimately it did snap back as monetary stimulus was added and sentiment recovered.

"and here's everyone's favourite global monetary policy stimulus indicator. The policy pivot was a key theme of last year where central banks made a resolute pivot from tightening to easing, and we've seen the global manufacturing PMI begin to turn as a result" (17 Jan 2020)



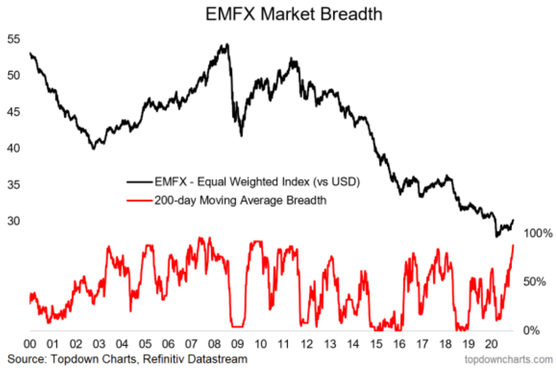
2. Again with the PMIs, we initially saw the start of what looked like a promising turn upwards.

"It's interesting to note how the Asia weighted average manufacturing PMI has turned up quite decisively (while the EM ex Asia version has dropped) there is a tendency for Asia to lead EM ex Asia, which makes sense given much of the Asian economies are at the leading edge of the global economic cycle" (17 Jan 2020)



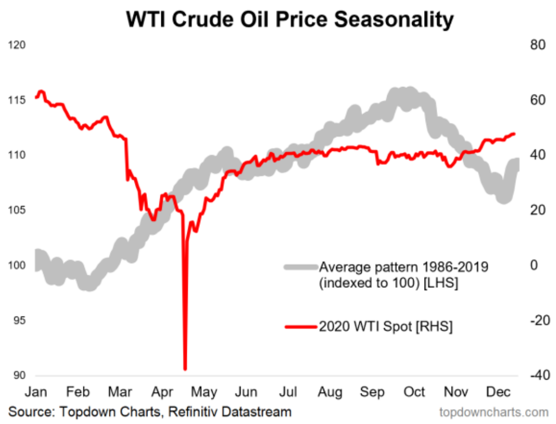
3. Another one from simpler times: pre-Covid it looked like EMFX was gearing up for a rally. It had put in a bullish breadth divergence signal (usually a good turning point indicator), and valuations were on the cheap side. As I noted, I was also sitting bullish on emerging market equities and bearish US dollar, so it all looked coherent and consistent, but then sometimes you can end up being right on the analysis but ultimately proven wrong by an unforecastable external shock.

"EMFX market breadth has rebounded and a bullish divergence pattern is in play" (17 Jan 2020)



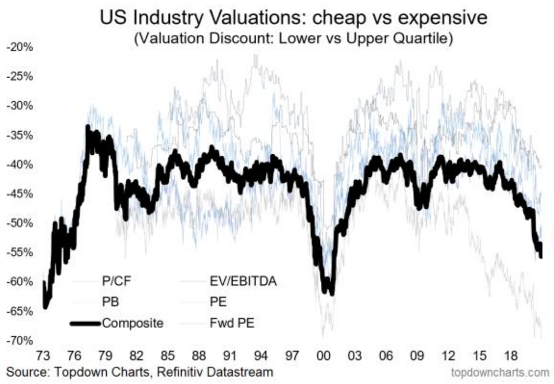
4. Remember the assassination of the Iranian general at the start of the year? Oil spiked on that news and then began to drift downwards. As it was sitting around support, I argued it looked oversold and seasonality was about to shift in its favour. As a slight redeeming note, I did highlight that $51 was the key level from a risk management standpoint and a break down would be a key trigger to the bearish side… but I would never have imagined that it would have gone that far that fast, or even that it was actually possible for prices to go negative. Lots of learning this year!

"the RSI is now looking oversold, and seasonal tailwinds about to hit I would say that odds are support will hold" (31 Jan 2020)



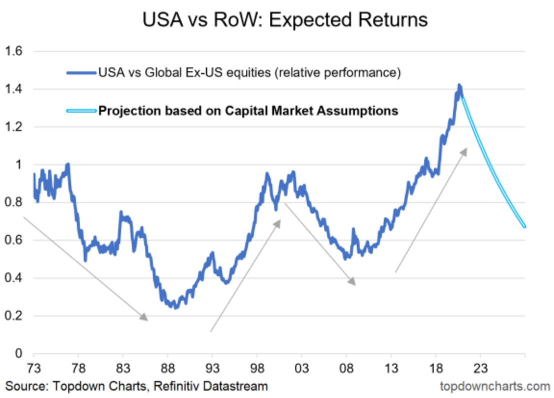
5. I entered this year thinking that value vs growth might finally be ready to turn upwards given my thesis on the macro outlook (recall I was bullish global growth late last year). Valuations were also in favour. Later in the year I doubled down on the call, but again was early. After the price action in November, it does seem like things are on track now and the various puzzle pieces are falling into place. So let's see, maybe it's a 2021 story.

"One thing I keep coming back to is the relative valuation picture: the cheaper part of the market is more cheaper than usual vs the expensive end of the market." (17 Jul 2020)



6. With regards to global ex-US vs US equities, again it seems to be a case of simply being too early. All the elements look to be in place, at least from a medium-longer term perspective, but it comes back to timing. I will say that later in the year I did more work in developing tactical indicators to finesse the timing side of things, so hopefully that helps things going forward.

"the medium-longer term view remains fairly one-sided. Projecting future relative performance based on my capital market assumptions outputs presents a pretty clear scenario … there seems to be a relatively reliable circa-10-year cycle in play (and the current cycle of relative performance is past due for a turn)." (7 Feb 2020)

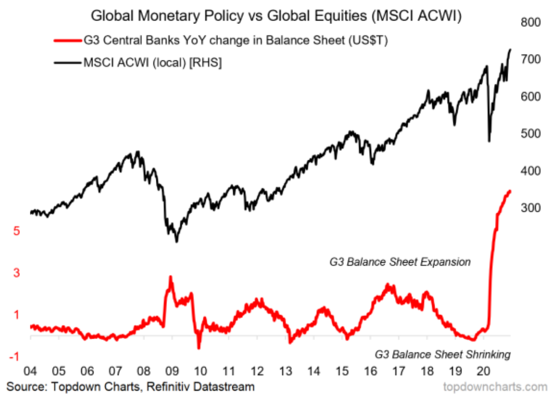


Section C. My Favourite Charts

These are some of my favourites – either new or interesting, or ones that helped illuminate some of the key developments across macro and markets.

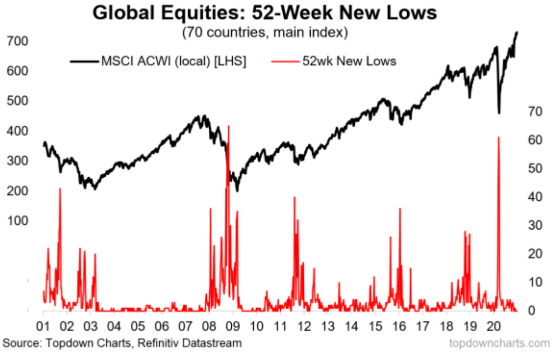
1. This one was helpful in laying bare the clear pivot in global QE (albeit this only shows the big 3 i.e. Fed, BOJ, ECB, while this year saw dozens of other central banks starting their own programs). It also laid down a clear linkage to equities, and thus a key fundamental reason to be bullish.

"Aside from interest rates, balance sheets are likely to come into focus as those at and near the ZLB figure out the rock and the hard place of NIRP vs more APPs. The Fed already has QE lite, and could do a twist and/or cease MBS runoff to help push mortgage rates down (a more direct transmission to the consumer). Already the policy pivot last year saw a reversal of the brief contraction in balance sheets," (6 Mar 2020)



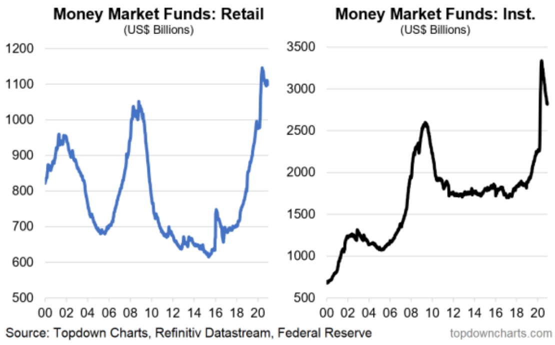
2. This was one of those "wow charts", it was just plain interesting due to the extreme movement in the indicator. But also extremely useful in helping fill out the bullish case for global equities.

"The number of countries making new 52 week lows at 58 (70 countries covered) is only matched by the depths of the GFC" (13 march 2020)



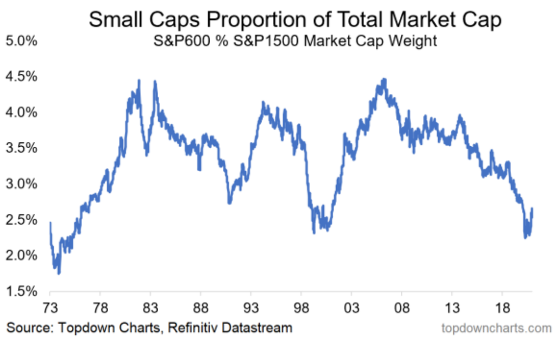
3. This pair of charts showing basically cash holdings (AUM in money market funds) was really interesting, especially when considered alongside the massive spike in personal savings rates across the globe as people in lockdown stopped spending and either at least kept receiving their pay check or got topped up by the various fiscal policy "economic life support" measures. At the time it led me to quip the term "quarantined cash", and I think this will be an important background feature as we head into the recovery as a source of fuel for a resurgence in consumer spending… "roaring 20's" anyone?

"Cash allocations have shot up to near decade highs, and money market funds have made new record highs in AUM… Looks to me like there is a fair amount of dry powder both in portfolios and consumer bank accounts." (8 May 2020)



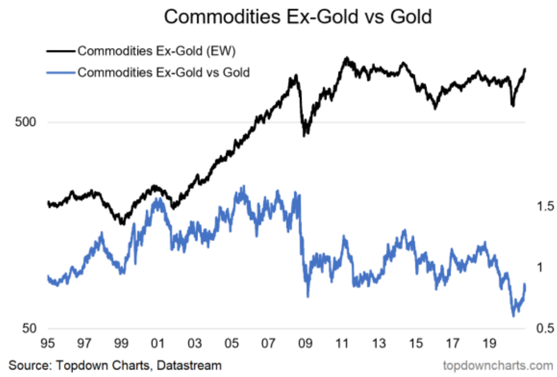
4. An intriguing chart, this one shows the market cap weighting of the S&P600 small cap index as a proportion of the S&P1500 (total market). At the low point it got to a 42-year low. This turned out to be a good contrarian buying signal (which lined up with a few other things like (relative) valuations, flows, and implied allocations).

"also worth highlighting is the drop in allocations, and the market cap weighting of small caps falling to a 20 year low I would consider these basically as contrarian indicators, and possible signs of a cyclical bottom" (10 Apr 2020)



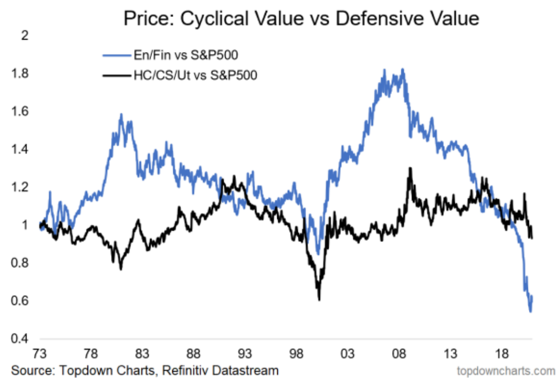
5. I like this one because it's a bit non-obvious. Many people lump gold in with commodities, and indeed, the term commodities itself can end up oversimplifying an incredibly broad and diverse set of markets. The point of this chart is to differentiate between gold and commodities ex-gold. As it turned out with the rally in gold and collapse in commodities, there ended up being an attractive relative value opportunity as gold left the rest of commodities behind.

"the equal weighted commodities ex-gold index has reached a new relative low against gold - which is a similar patten to what we saw during previous major market bottoms for commodities" (10 Apr 2020)



6. Last but not least is a key division within US value stocks that I believe yields interesting clues to the outlook for value vs growth.

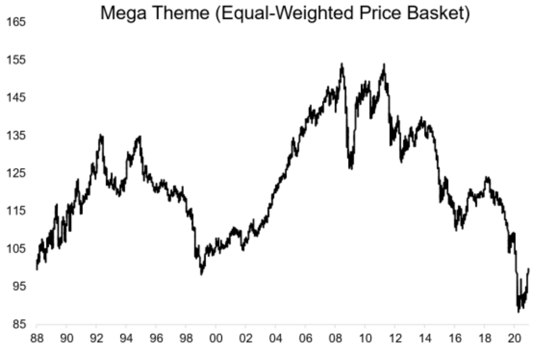
"The other side of value vs growth is what you might call "Defensive Value" i e Healthcare, Consumer Staples, and Utilities. Indeed, if you look at the relative performance of this group vs the S&P500 it certainly has a defensive look to it, and has tended to be a lot more stable against what we might call "Cyclical Value" i e Energy & Financials. Indeed, looking at the relative performance of Cyclical Value vs Defensive Value we can see that it's been Cyclical Value driving much of the underperformance of overall Value vs Growth" (13 nov 2020)



Section D. Charts to Watch in 2021

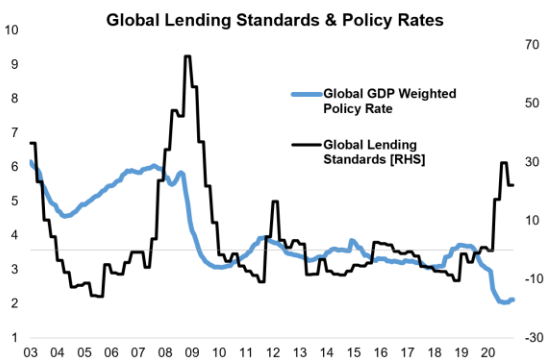
As interesting and sometimes amusing as it is to look back, as investors we get paid for looking forward, and there's a few existing trends and themes that will remain front of mind and be key to keep on the radar in 2021. Following is a selection of the key charts and indicators I will be watching in the new year.

1. Mega Theme: In the last regular edition of the Weekly Macro Themes report, I decided to combine all my big ideas into one "mega theme" given some of the echoes across the ideas in terms of price action and macro drivers. The result is this interesting chart which looks to be either at or near the bottom of a long-term secular trend, and the start of at least a short-term cycle.



Source: Topdown Charts, Refinitiv Datastream topdowncharts.com
"Mega Theme" consists LONG: global ex-US vs US, EM vs DM, EM ex-Asia vs Asia, Value vs Growth Small vs Large, Commodities, EM FX, [and SHORT/inverse: US dollar index, gold, US treasuries]

2. Monetary Policy (limits): The policy response to the pandemic was historic in terms of its speed, magnitude, and coordination across countries and between fiscal and monetary. But this chart perhaps highlights one limitation of monetary policy, the tag line is "interest rates are low, but good luck getting a loan" (given how much banks tightened up on lending standards). One thing on my mind is a possible passing of the torch from monetary policy to fiscal policy – as that's going to be the thing that will achieve a more balanced and more transformative impact in the recovery.

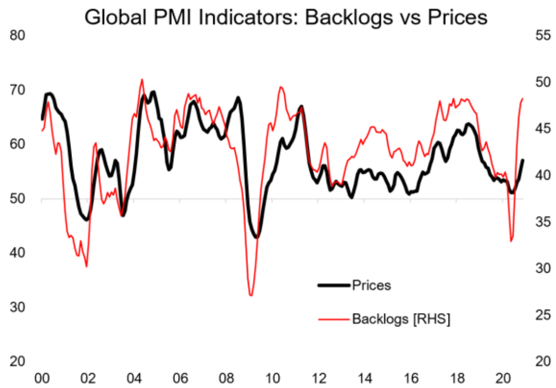


Source: Topdown Charts, Refinitiv Datastream topdowncharts.com

3. Global Trade Rebound: The global economic shutdown saw an abrupt collapse in trade growth, but we have seen clear green shoots and the lead indicators point to an acceleration into 2021.

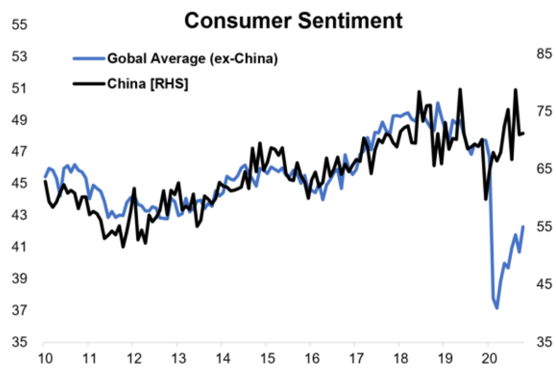
Source: Topdown Charts, Datastream, CPB, RWI/ISL topdowncharts.com

4. Global Backlogs: A nice follow-on, the surge in backlogs has 2 key implications: upside risk to inflation, and a likely spike in activity as firms attempt to clear backlogs and restock inventories.



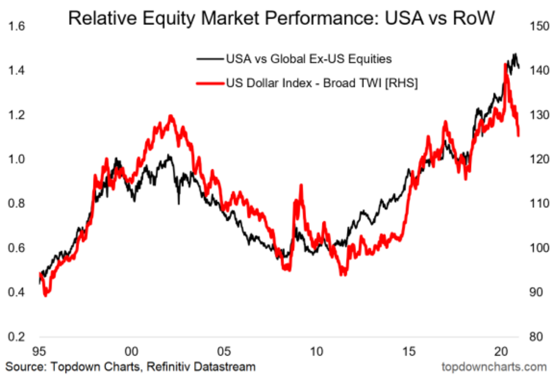
Source: Topdown Charts, Refinitiv Datastream topdowncharts.com

5. Consumer Normalization: Consumer moods remain depressed *outside of China*. This chart provides a playbook for the rest of the world, a key means of keeping track of normalization, and a nod to a potential consumer boom post-vaccine.

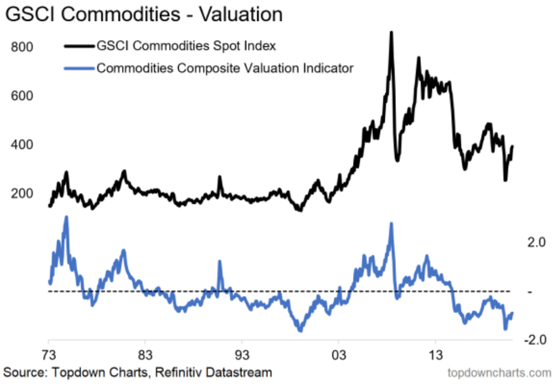


Source: Topdown Charts, Refinitiv Datastream, Ipsos topdowncharts.com

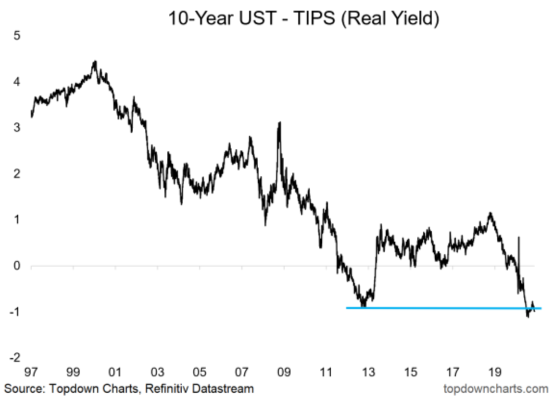
6. Global vs US: All the key pieces of the puzzle seem to be falling into place for the rest of the world to start outperforming vs the US. Along with that, I expect ongoing weakness in the US dollar.



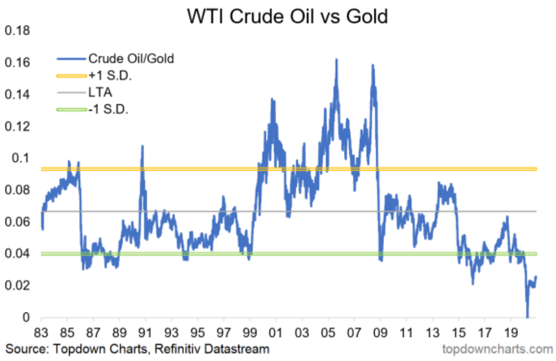
7. Commodities: Given cheap valuations, weak capex, pandemic disruption, an expected weaker USD, and economic recovery (with potential overshoot), remain decidedly bullish here.



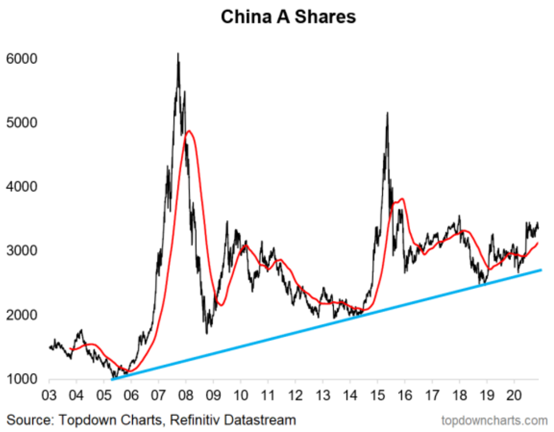
8. Real Yields: In my view the two key drivers of US real yields are risk sentiment and growth expectations. Naturally on both fronts it was entirely rational to see real yields plunge this year. Going forward I expect improved risk sentiment and a rebound in growth expectations; therefore I expect higher real yields (and nominal yields).



9. Crude Oil vs Gold: The logical next question should then be "what about gold?". All else equal, a prospective environment of higher real yields would present a headwind to the consensus and crowded long gold trade. Aside from that, I believe a prospective passing of the torch from monetary to fiscal in the US is strong possibility (Treasury Sec. Yellen has a deep appreciation for the limits of monetary policy and the need for fiscal policy to do more of the heavy lifting). This along with post-vaccine normalization should disproportionately benefit oil at the expense of gold, so I suspect we see some mean reversion in this chart.



10. China: Last but not least is China. While I continue to watch a wide range of indicators, one in particular focus will be China A-shares, particularly as they brush up against a key overhead resistance level, and as policy makers in China possibly move toward actually tightening monetary policy in 2021. Indeed, in many respects, I suspect it will be more of China zigging, while the rest of the world is zagging. In any case, I remain convinced that it is still one of the most important economies and markets to watch in understanding the global macro/market picture.



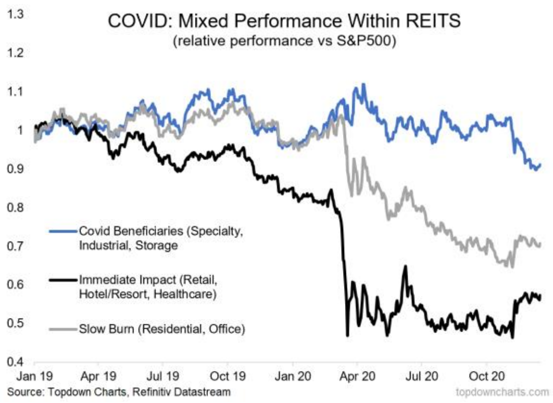
Section E. Honourable Mentions

These charts were worthy of mention but didn't quite fit into any of the previous categories.

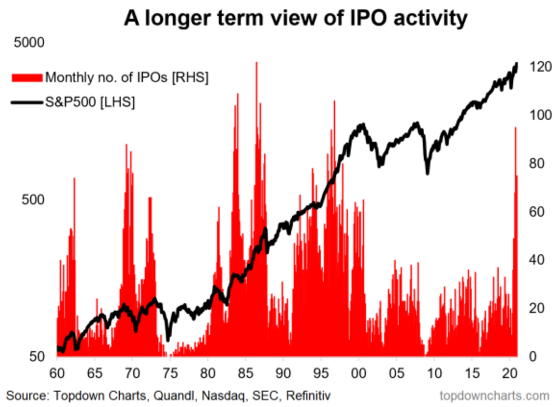
1. As the recovery in markets progressed, the fact that global cyclicals vs defensives managed to hold their uptrend line was a big deal.

2. Due to a surge in backlogs, disruption to global logistics, and a rebound in demand, China shipping rates surged (and that surge was echoed in the copper price); basically, a mix of green shoots and pandemic disruption.

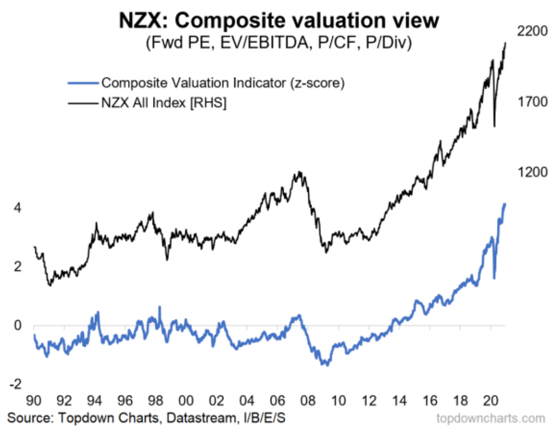
3. REITs were a mixed bag through the pandemic, and this chart helped document the damage.



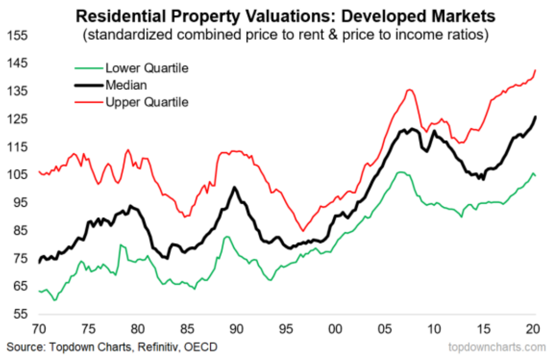
4. Curiously enough, 2020 saw a resurgence of interest in IPOs, with the SPAC phenomenon driving IPO volumes to levels last seen during the dot com bubble: … "have cash, will invest".



5. One from my own country, this chart shows the rise and rise of NZ equity valuations – I've remarked how this is just one of several similarities this market shares with the USA.



6. Very honourable mention to housing market valuations, which have been launched summarily to new all-time highs as record low yields and the global wave of liquidity boosted purchasing power (the axiom: rates go down, house prices go up). This will increasingly become a political issue.

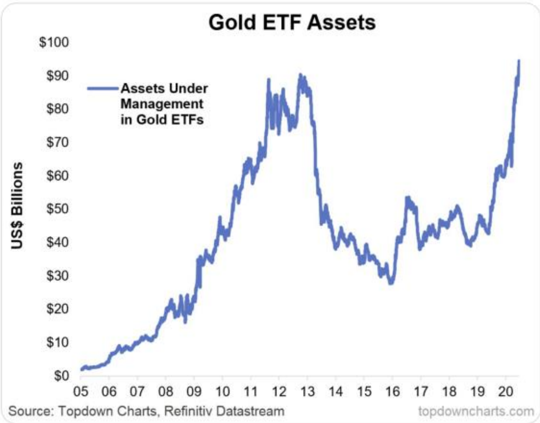


Section F. People's Choice Charts

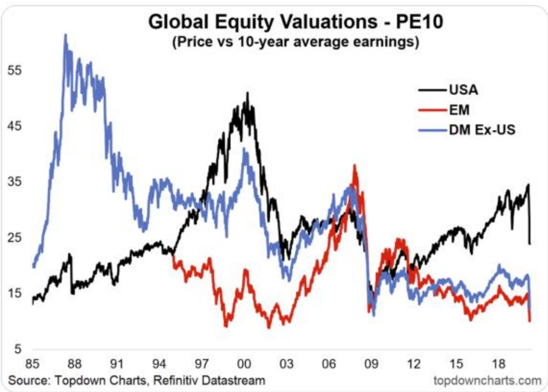
In this section I defer to our followers on Twitter (@topdowncharts) for the most popular charts based on views and engagement.

These charts are *not* updated to the latest -- in contrast to those in the previous sections (because it helps explain why folk were so interested in them at the time …as always, just email me if you want to see any of these or others updated, or if you had any questions in general).

1. It was perhaps no surprise that one of the most popular charts was on the topic of gold. The chart showed aggregated gold ETF assets under management reaching a new all-time high. Gold was truly riding the wave of global liquidity this year and had both true believers and tourists alike scrambling to get a piece of the action.

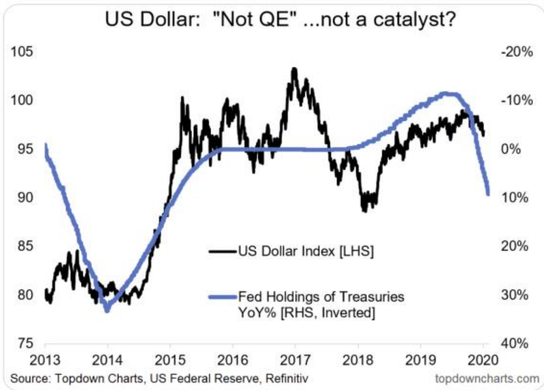


2. For a brief moment there, EM PE10 valuations dropped as low as they got to all the way back in 2003. It's not often that you see such a substantial reset in valuations. There were some questions around "what's the E?" in terms of the PE ratio. But this was exactly the type of situation that the PE10 (price to trailing 10-year average earnings) proves its value.

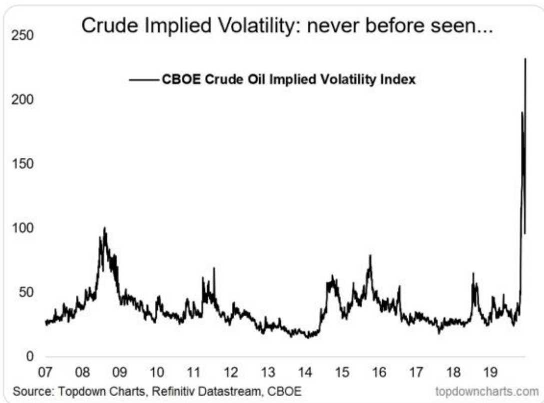


3. Another chart on global equities caught traction: this one documenting the recovery. At the time of that tweet some 74% of countries returned to "bull market" status on the crude 20%-up rule.

4. One from the turn of the year, even before the Fed really stepped things up the renewed QE, or as some called it "Not QE", was basically pointing to a downturn in the US dollar index.



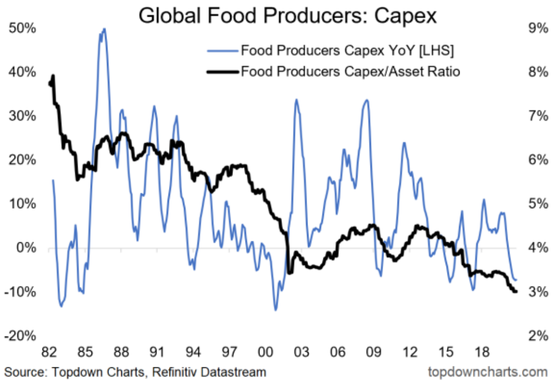
5. Naturally, there was a lot of interest in crude oil charts as WTI crossed the Rubicon into negative territory. We probably didn't need a chart to tell us volatility was at unprecedented levels, but I put it up anyway, and it certainly added another angle on those very interesting days in the market.



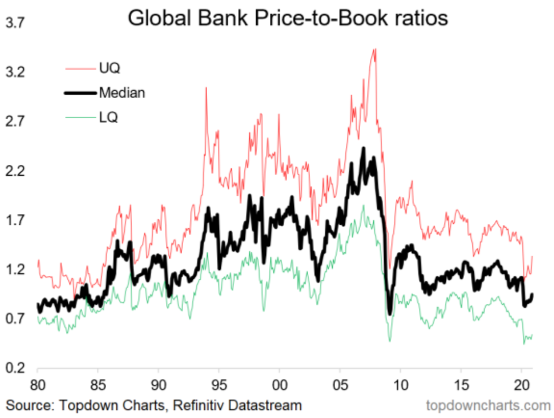
Section G. New Coverage

This section provides a brief selection of the areas of new/expanded coverage initiated over the year.

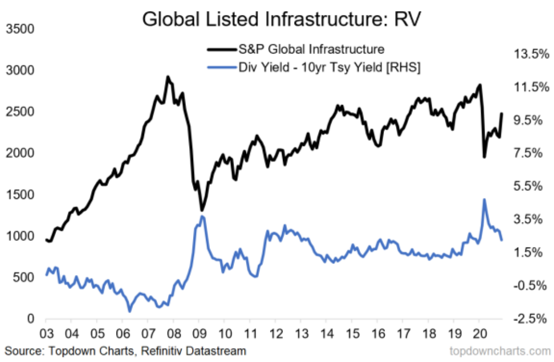
1. Agricultural Commodities: Going beyond just grains, I expanded coverage here, and the timing proved quite good as prices began to breakout.



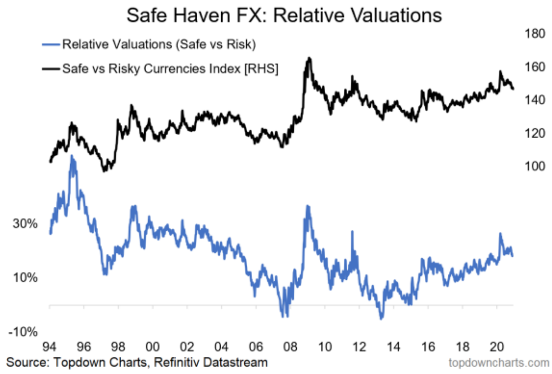
2. Global Banks: I built out a suite of valuation, fundamentals, and technical indicators for the global banking sector (including regions).



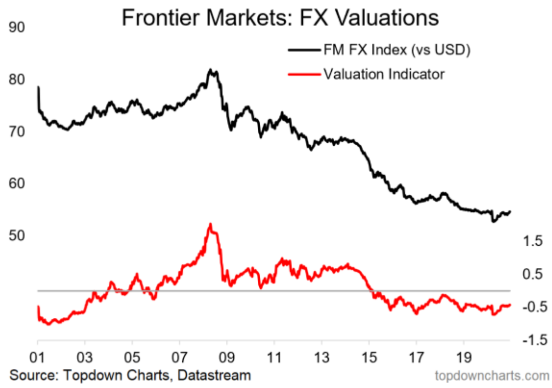
3. Global Listed Infrastructure: Coverage initiated for this niche asset class (including expected return figures), upon the request of a client (right at the bottom of the market!).



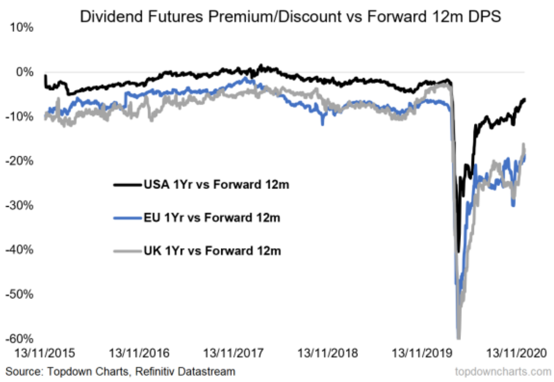
4. Safe Haven FX: Another area initiated at the request of a client involved the construction of a basket of safe haven (vs risky) currencies. An interesting basket to trade, but also interesting applications from an analytical standpoint.



5. Frontier Market FX: Frontier Market Equities were a feature in this section last year, but this time it's about formal coverage of FM FX (using an equal weighted basket). This is particularly for FM equities, given the impracticalities of FX hedging for this asset class -- having a view on the currency side of things is very important.



6. Dividend Futures: Another client request, and another area of the markets that is both interesting in terms of opportunities as well as analytical insights. Built a continuous series to help add insight to what is a relatively obscure instrument.



Report by Callum Thomas, Head of Research at Topdown Charts

About Topdown Charts

Topdown Charts provides chart-driven research across a global multi-asset universe. The service is built around a core set of reports which have been specifically designed and refined through time to support multi-asset portfolio managers, active asset allocators, and macro-driven fund managers. The perspective is that of a buyside strategist and the key deliverables of the reports are: investment idea generation, top-down global macro insights, risk management input, and asset allocation research.

Research Process and Framework

Research Process

Valuation

Valuation as a common anchor in the thesis
- Identify and develop valuation indicators
- Monitor for extremes (where the best opportunities are found)
- Explore the relative value case (no asset exists in a vacuum)

Cycle

Cycles are a constant across time and markets
- Identify the core cyclical/monetary drivers for the asset class
- Develop and monitor indicators and key data points
- Clarify how asset prices evolve across the cycle

Tactics

Round out the idea with tactical guidance
- Tactical indicators aid in idea generation + implementation
- Apply disciplined and sensible technical analysis techniques
- Look for extremes in sentiment, flows, and positioning

Key Beliefs

- Risk = owning an asset which is overvalued, overowned, overbought and out of time.
- Risk also = underexposed to assets which are undervalued, unloved, oversold, and turning around.
- See things as they are: avoid forecasting, be data-driven yet be unapologetically forward looking.
- Must define/frame key risks and drivers for a given asset class.
- Know what indicators/charts to watch and monitor (and strive for constant innovation/improvement).
- Aim = put the odds in your favour.

Key Objectives and Scope of Research

Really there are 3 key objectives that we aim to deliver: **risk management input** (investors tend to disproportionately punish permanent loss of capital vs rewarding exceptional performance), **idea generation** (but exceptional performance is still critical!), and help our clients **gain perspective** (which not only helps them in managing money, but also communicating with their clients and stakeholders).

Risk Management
- Rule 1 of investing: don't lose money.
- What do we need to be paying attention to?

Idea Generation
- Engage multiple factors to find the best ideas.
- Create unfair advantage for our clients through superior research.

Gain Perspective
- Stay focused on the signal, not the noise.
- Inform our clients with cutting-edge studies.

Investment Universe

Equities
- ❑ Regions/Countries
- ❑ Sectors/Industries
- ❑ Styles/Factors

Alternatives
- ❑ Commodities
- ❑ Currencies
- ❑ REITs, MLPs

Fixed Income
- ❑ Government bonds
- ❑ Corporate credit
- ❑ Inflation linked

Topdown Charts -- What we do:

We work with portfolio managers to help make their job easier. The aim is to make it feel like you have an extra investment strategist on the team.

Core Institutional Service

The core institutional service is aimed at multi-asset portfolio managers and investors requiring top-down input in their process: those wanting something a little bit different, and who share a similar philosophy and affinity for our chart-driven research approach.

The core service includes:

-Regular research reports (see below for a full listing)

-Help with questions and requests (either about the reports or in general)

-Use of the charts (e.g. in your own reports and presentations)

The Reports

Weekly Macro Themes: Core report, featuring 5 ideas/topics each week spanning investment ideas, risk management input, and meaningful macro insights.

Global Cross Asset Market Monitor: Weekly intelligence briefing on shorter term sentiment and technicals across global markets and asset classes.

Market Cycle Guidebook: A monthly focus on the more medium-longer term factors such as cycle/valuation/monetary, updated capital market assumptions, and a summary of views across asset classes and TAA positioning guide.

Quarterly Strategy Pack: Slide pack of core views and charts across macro and markets to support discussions and presentations with clients.