Weekly Report and Outlook on Global Markets

22nd May 2020

Volatility traders abandon VIX bets as stock conviction vanishes

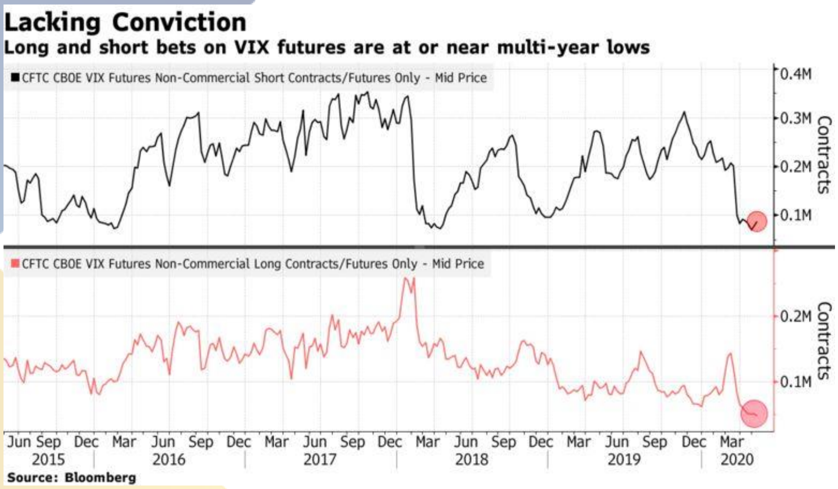

Figure 1: The chart represents long and short bets on CBOE VIX futures by Institutional Investors

As Wall Street frets a rally defying economic gravity, long and short exposures among non-commercial investors on the Cboe Volatility Index have sunk to near multi-year lows, according to the latest CFTC futures data.

Meanwhile, a vanishing number of retail traders are speculating on Wall Street's fear gauge, with volumes across VIX-focused exchange-traded products slumping. It's a world away from the frenzied action in the pandemic roller coaster just weeks ago. If this reflects a lack of conviction about the direction of volatility in the coming weeks, it is understandable .

Amid a busy March betting on the direction of volatility, trading in exchange-traded products has turned downright sleepy. Last week, around $3.4 billion worth of shares changed hands, down from a peak of $54.7 billion in a single week in March, according to data compiled by Bloomberg Intelligence

Extreme Options sentiment is awful omen for stocks

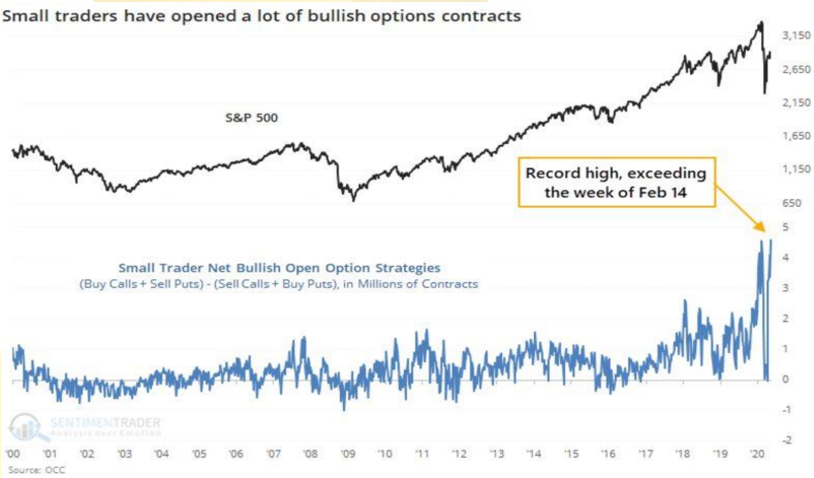

Figure 2: The chart depicts Net long positions in S&P 500 options by small/retail traders

Small options traders are bullish to a point that signals trouble for U.S. equities. Last week, the smallest of options traders, those with trades for 10 contracts or fewer at a time, opened a new record of net bullish positions surpassing the levels formed by them in February 2020.

In comparison, very large traders, those with trades of 50 or more contracts at a time, haven't been betting so much on a rally.

That has widened the spread between small- and large-trader net bullish positions to a record, with the gap jumping "like it did in 2008. It clearly shows that the smallest of traders, who tend to be the most consistently ill-positioned at extremes, have gone aggressively long, in a leveraged fashion. This has a strong tendency to lead to lower prices over the short to medium term.

Municipal Bonds in the US show the greatest monthly increase since 2009.

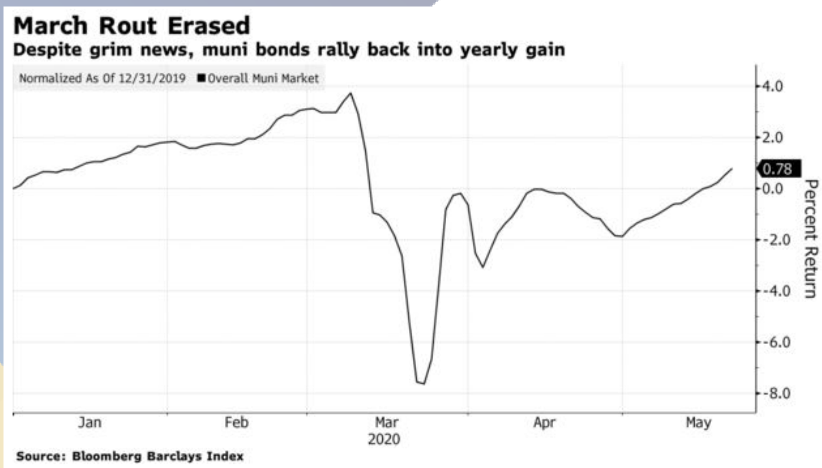

Figure 3: The figure depicts municipal bond returns normalized as of 31 Jan 2019

The municipal bonds have given a return of 2.7% so far in the month of May according to the Bloomberg Barclay's index. The rally wiped out the record-setting loss that hammered investors in March and is driving yields back toward the lowest in more than 60 years, with those on benchmark 10-year tax-exempt debt sliding 5 basis points Friday to 0.83%.

As the country reopens from the shut downs, the public transit agencies, airports, hospitals and colleges, among others that have been deeply affected by the closing of economy will start generating revenue for the municipals which will rescue the Municipals from defaulting on their bonds. Even so, the bonds backed by states and cities are among the least likely to default, since governments could raise taxes and bond payments make up a relatively small share of their budgets.

Merkel plan for EU debt meets opposition from budget hardliners

The opposition to plans for the European Union to collectively finance its response to the coronavirus recession is taking shape after four members proposed a temporary fund for emergency loans as an alternative.

In a joint paper, the leaders of Austria, Denmark, Sweden and The Netherlands, sometimes dubbed the "Frugal Four," reiterated their opposition to joint debt and any direct grants and to an increased EU budget, throwing cold water on the initiative set out by German Chancellor Angela Merkel and her French counterpart Emmanuel Macron on Monday.

"Our objective is to provide temporary, dedicated funding through the MFF and to offer favorable loans to those who have been most severely affected by the crisis," the four countries wrote. "What we cannot agree to, however, are any instruments or measures leading to debt mutualization nor significant increases in the EU budget."

The MFF, or Multiannual Financial Framework, refers to the EU's seven-year budget

Countries like Italy and Spain have been banking on the EU's long-anticipated recovery fund to help them rebound from the economic devastation caused by the pandemic. The European Commission, the EU's executive arm tasked with formulating a blueprint, will present its plans on May 27.

Even though EU leaders have agreed on the need for such a fund to assist with the recovery, they have different views whether it should disburse loans or grants, what its total size should be and what the money should be spent on. And while they've broadly accepted that some of the money will come from jointly-issued EU debt, how much the bloc will raise on the markets remains a point of dispute.

MAJOR MOVES THIS WEEK

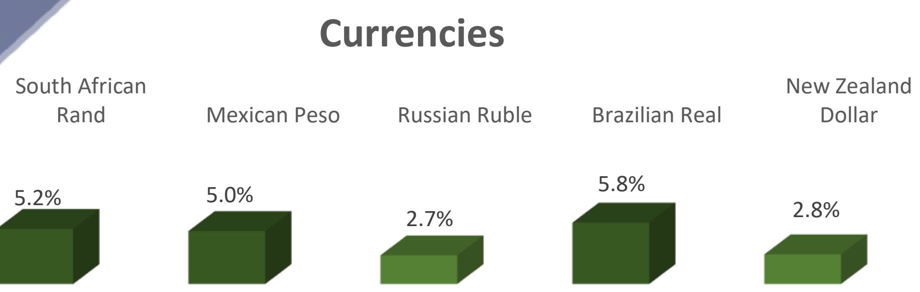

Figure 4: The chart represents Currency returns with respect to US Dollar as the base currency for this week

This was one of the best week for Emerging market as well as many developed market currencies against US dollar recently. Currencies like South African Rand, Mexican Peso and Brazilian Real , among Emerging markets have given spectacular moves against USD. Seems like carry trade is coming back as risk appetite for investors is increasing. Developed currencies like New Zealand Dollar and Australian Dollar also gained against dollar as commodity market stabilizes. Currencies like Euro, Yen and Pound remained flat.

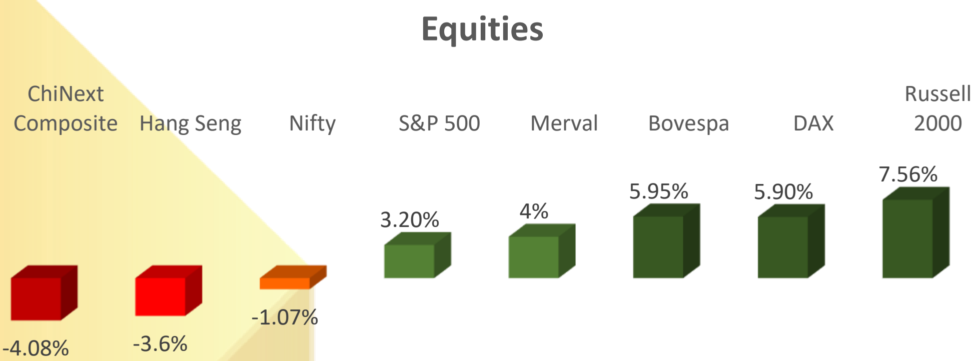

Figure 5: The chart represents the equity index returns over this week.

The Equity markets all over the world have shown a bullish picture except countries like India and Philippines. This is because of higher than expected jump in the total Covid-19 cases which was driven by opening up of the economies in these countries. Chinese and Hong Kong equities were under pressure after China moves to impose controversial Hong Kong security law. Rest all other equities all over the world have almost mimicked the US equites. The Russell 2000 index which is the small cap index has outperformed the S&P index by about 4% point which shows a major risk on environment in the world.

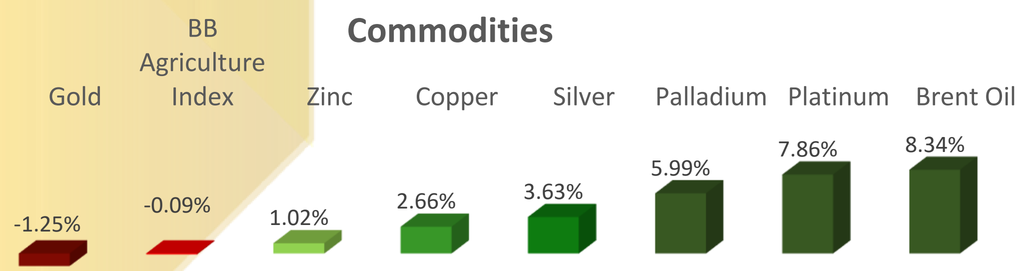

Figure 6: The chart represents the weekly returns of the following commodities.

This commodity futures this week were in line with the risk on sentiment in the equity markets. Out of all the precious metals, gold is the only commodity to close in red this week. Silver, Palladium and Platinum have outperformed the bullion. The industrial commodities too have closed in green this week as the economies slowly open resulting in increased demand for these metals. Brent oil has continued its upward journey this week as the OPEC+ countries have increased their production cuts in line with the demand for the commodity.

GLOBAL FUND MANAGER'S STATEMENTS

1) Scott Minerd (CIO & Chairman of Guggenheim Partners) : "While the U.S. speculative-grade default rate could reach 15 percent and more risks lie ahead, the market is offering better entry points than seen in years." - Tweeted on 21st May 2020.

2) Jeffrey Gundlach (Founder of DoubleLine Capital LP) : "30-year Treasury yields seem as anxious to break out to the upside as a rodeo bronc waiting to buck out of the chute. Fed's getting clearer they want to keep the bronc in the chute forever. Can they? We'll see. Surely they won't last the rodeo 8 seconds if the gate is opened." – Tweeted on 21st May 2020.

PACE 360'S FUTURE OUTLOOK

"Global risk assets have had a good last week. This is particularly true of Emerging Market currencies which had an absolutely banner week. We expect the bullish bias to continue over the next few weeks even though most of the equity indices may remain broadly rangebound. We particularly expect Emerging Market currencies to further extend their uptrend in the coming week"

CONTACT US

+91-11-4742 1001

info@pace360.in

A-1/291, Safdarjung Enclave, New Delhi – 110029

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