MACRO HEDGE ADVISORS LLP

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ALERT: VIRAL ATTACK TO HIT EURO AND ASIAN EPI-CENTRE OF ASSET MARKET SPECULATION

The Asia bubble and Euro at forefront of viral attack.

The "hard data" has not been signalling strong global economic rebound ahead, never mind euphoria in some asset markets including S&P 500 and most of all FANG +. Some "soft data" – including expectations in surveys and speculative commodity prices – had been encouraging, but how much were these influenced by all the hype about the Xi-Trump tariff war truce. Time would tell. Certainly the markets rose a little further when the "deal of the cronies" was consummated amidst much fanfare.

The smiles and back-slapping of the cronies was all too evident. But that seemed to be soothing to the equity and economic bulls. What is good for Big Finance and Big Tech is surely good for the US and global economy, even if what is at stake seems mainly to be sharing out monopoly rents in China (if these are ever forthcoming). Historical researchers may well find that the leaders preparing the jamboree to announce the truce already knew more about the viral "shock" exploding than they let on, determined not to spoil the party.

Europe was swept up in this optimism, despite the dogged refusal of the hard data to climb. In the currency markets long positions swelled in the euro and the Canadian dollar and short positions in the yen on the basis of traditional relationships between currencies and swings in the barometer of global optimism and pessimism on trade and market prospects. Yet the huge vulnerabilities of the euro remain not far below the surface. Huge and persistent monetary inflation in Europe from the early/mid 1990s to the Great Crash (2008) left a legacy of mal-investment and financial weakness greater there than in the US (where in fact, if this can be believed, monetary inflation had been somewhat less severe than in Europe, taking account especially of the Fed's belated sharp tightening of 2005-7 (and in the earlier cycle of 98-00).

In recent years the driving force between European economic recovery and expansion had been exports to Asia plus the German construction boom/bubble.

Asia has been the epicentre of the latest phases of the Great Monetary Inflation, especially 2010-14, but also from 2016. China has been at the centre of that epicentre, but there have been many hot subcentres outside. In the late months of 2019 global markets were abuzz with reports that this was revving up. Global funds were pouring in (including importantly from Japan into Asian credit markets).

The Cornavirus outbreak has changed all that.   Now optimism based on soft data has swung to pessimism and most of all about the epicentre – Asia. Who knows the ultimate setback to Asian growth and prosperity this year – but whatever it is surely time to be more critical about the opposing optimistic narratives.

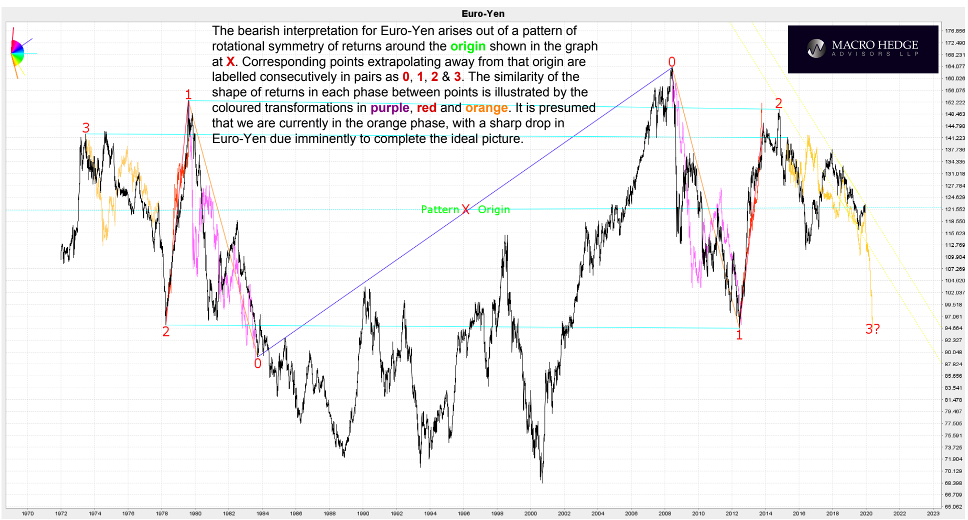
In the big market picture unfolding, the euro appears like a loser – a big loser.   Why should it not sink into the lower end of its life-time range against the dollar, especially as investors gird up for the Greens to assume power (in partnership with the CDU) in Germany and Christine Lagarde to monetize green policy?   Italian regional politics are for now a side-show only.

Here at MHA we have been sceptical of the yen's role as a safe haven asset. At least in the short-run the seizing up of Japanese flows of funds seeking high yields in Asia and the fall in US long-term rates will likely be yen positive. Of course the present wave of concern around the coronavirus can ebb as better news medical emerges (if that is to be the case).

Would that ebbing mean a new outbreak of euphoria?   Much depends on the extent of narrative-damage in the meantime and the hard facts of capital spending in particular across the advanced and emerging market economies. If the hard data reveal a downturn here that would trump the soft data.

Strategy Implications:

The fundamental picture points to a potentially sharp fall in the EUR/JPY FX rate, due as much to EUR weakness as JPY strength. This picture is fortified by a strong long-term pattern in the EUR/JPY FX chart per below with an explanation of why this market could fall by another 15% - 20% this year.



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