

# ECONOMIC / MARKET OUTLOOK

Messages from monetary trends and cycle analysis

14 January 2021

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# OUTLINE

- Cycle analysis – positive 12-18 month outlook
- Monetary analysis – short-term cautionary
- Inflation – “cyclical” upswing or trend change?
- Three suspect consensus views



# ECONOMIC CYCLES

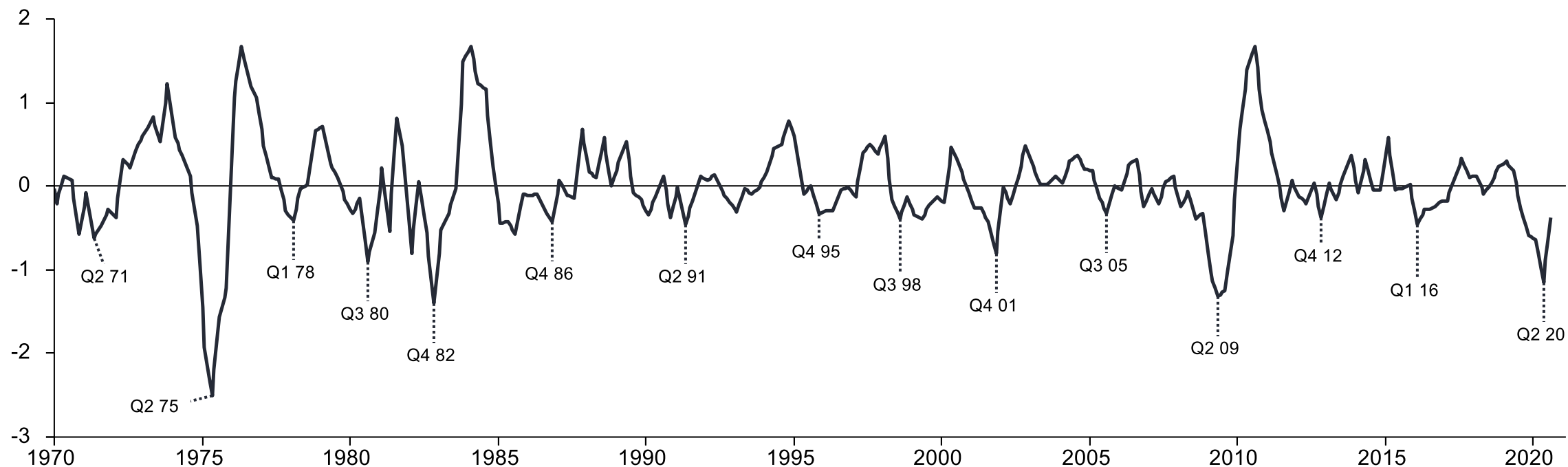
- Stockbuilding cycle (Kitchin cycle, 3-5 years)
- Business investment cycle (Juglar cycle, 7-11 years)
- Housing cycle (Kuznets cycle, 15-25 years)

# STOCKBUILDING CYCLE

Average cycle length = 3.5 years, Q2 2020 low?

## G7 Stockbuilding Cycle

G7 Stockbuilding as % of GDP (yoy change)

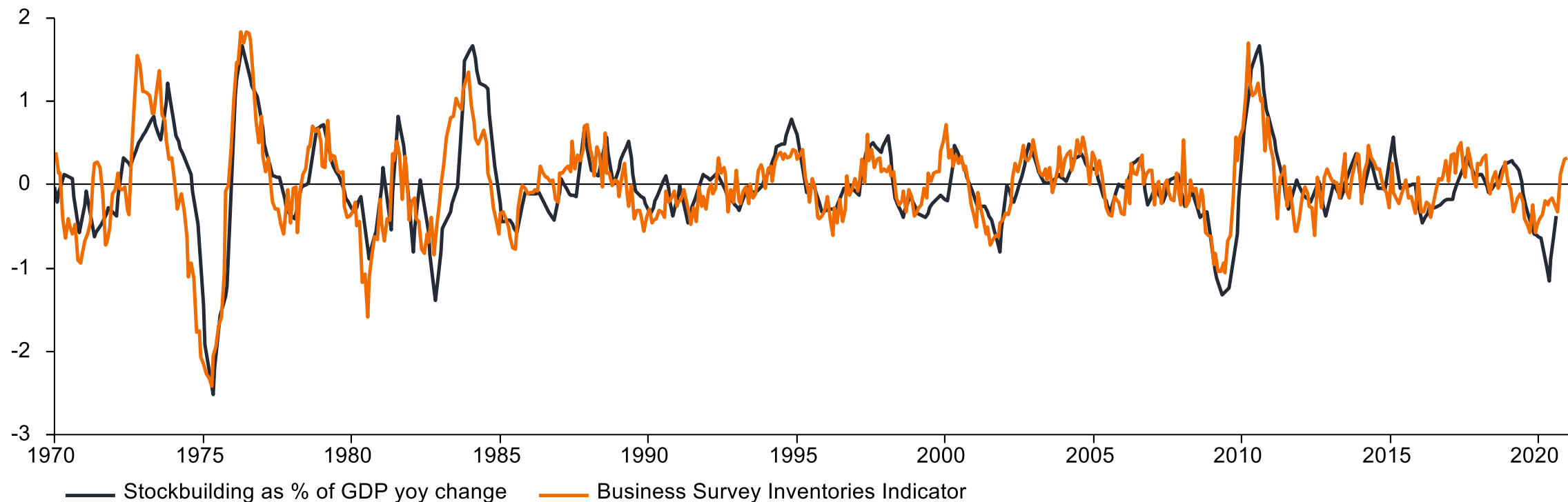


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# STOCKBUILDING CYCLE

Business survey inventories indicator consistent with Q2 2020 low

G7 Stockbuilding as % of GDP (yoy change) & Business Survey Inventories Indicator



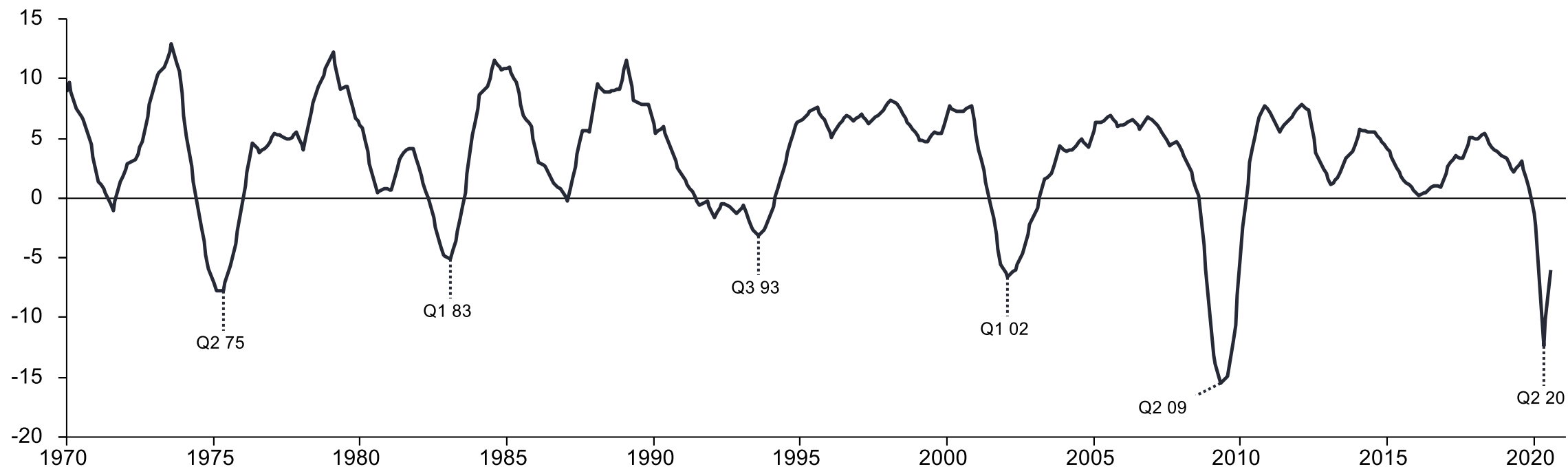
Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# BUSINESS INVESTMENT CYCLE

Average cycle length = 9 years, Q2 2020 low?

## G7 Business Investment Cycle

G7 Non-Residential Fixed Investment (% yoy)

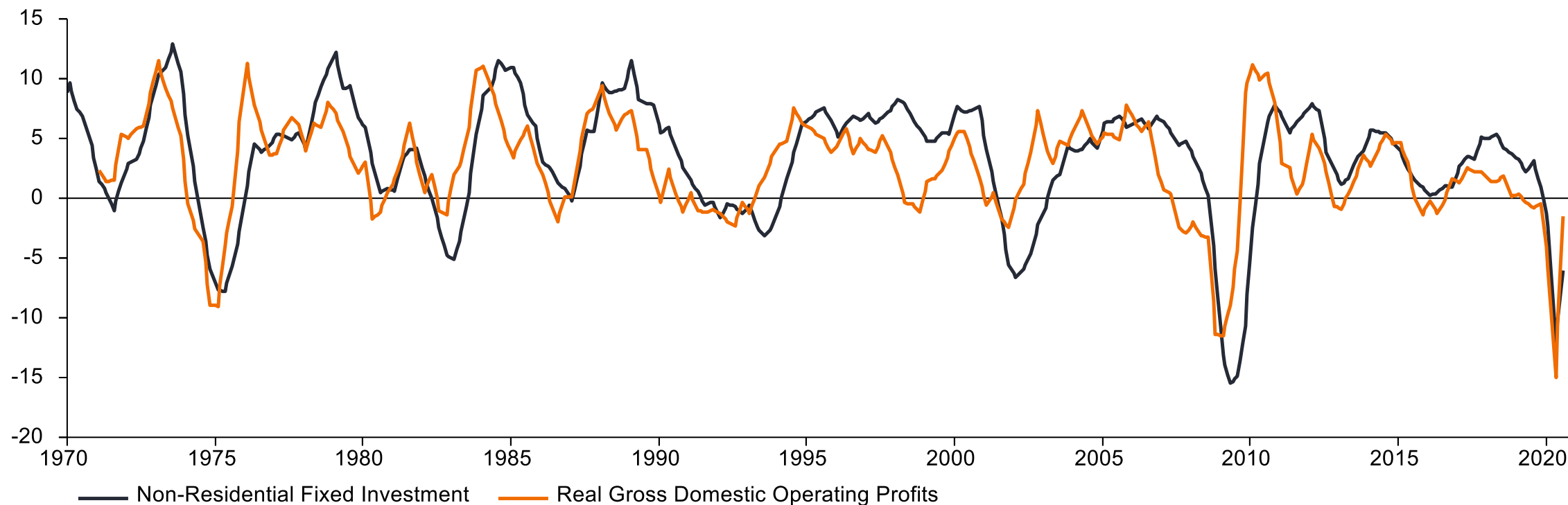


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# BUSINESS INVESTMENT CYCLE

Profits and investment cycles closely correlated, profits rebound consistent with Q2 2020 low

G7 Business Investment & Real Operating Profits (% yoy)

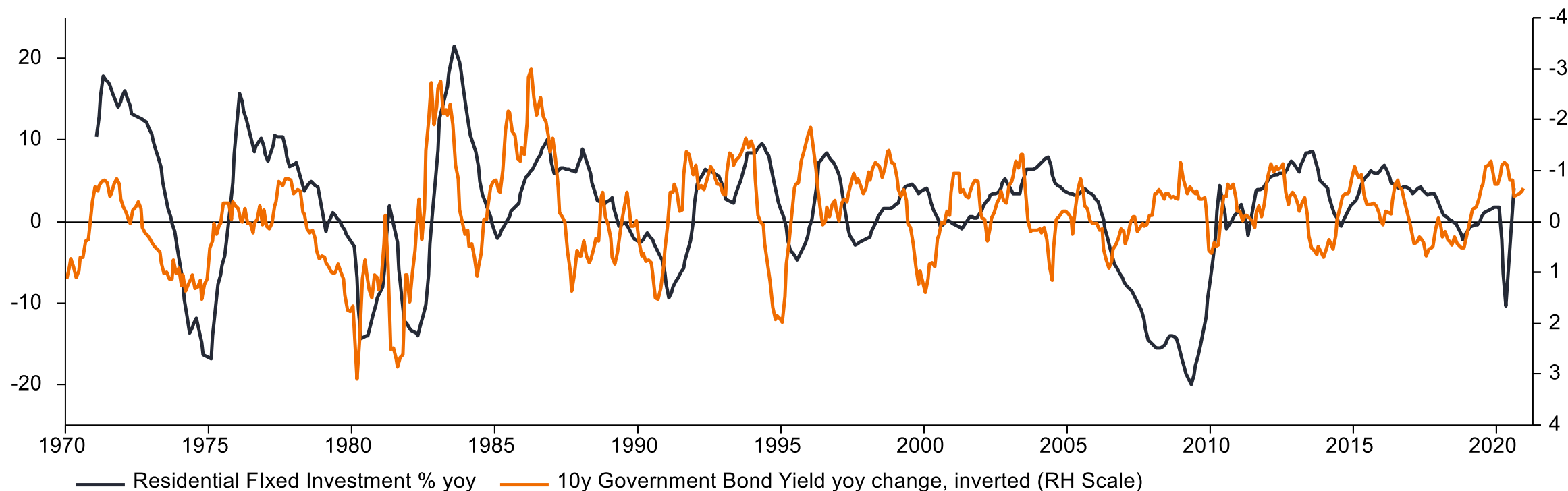


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# HOUSING CYCLE

Average cycle length = 18 years, upswing from 2009 low reenergised by yield fall

G7 Housing Investment (% yoy) & 10y Government Bond Yield (yoy change, inverted)



Source: Refinitiv Datastream, own calculations, as at 11 January 2021





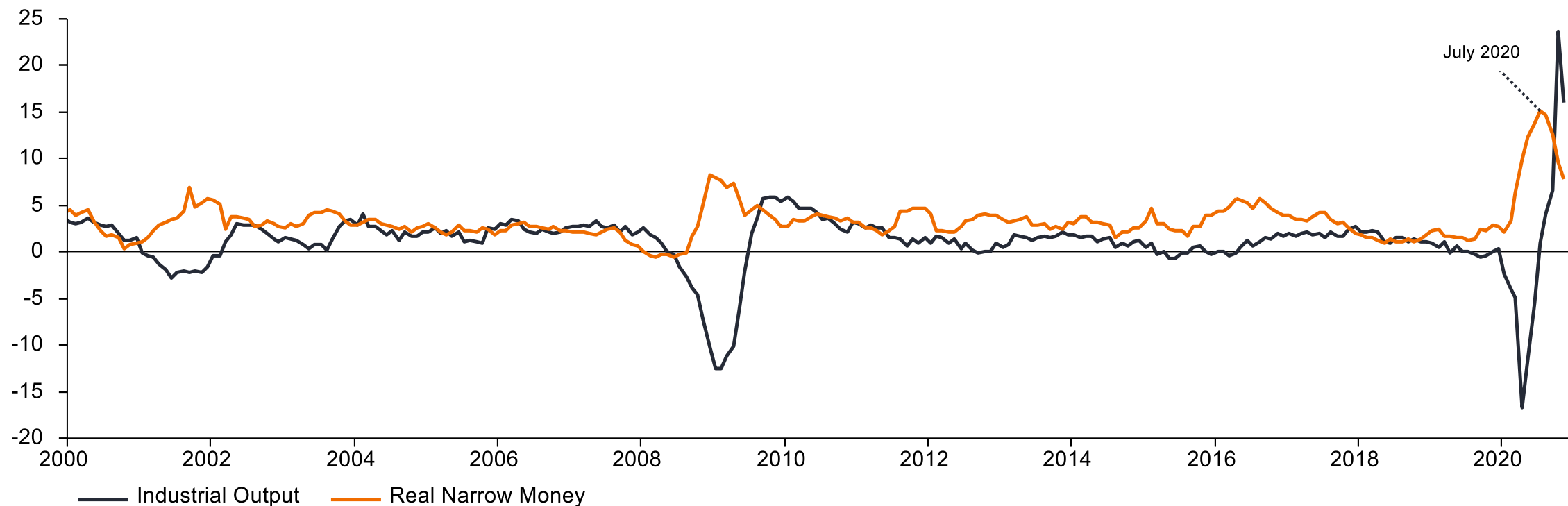
# MONEY & ECONOMIC ACTIVITY

- Turning points in real money growth lead turning points in output growth by 6-12 months (average = 9 months)
- Narrow money gives more reliable signals than broad money
  - Narrow money (M1) = currency in circulation + demand / overnight deposits
  - Broader aggregates (M2, M3, M4) also include time deposits, notice accounts, money funds etc

# GLOBAL ECONOMY & MONEY TRENDS

Six-month real money growth normalising, currently below output growth

G7 + E7 Industrial Output & Real Narrow Money (% 6m)

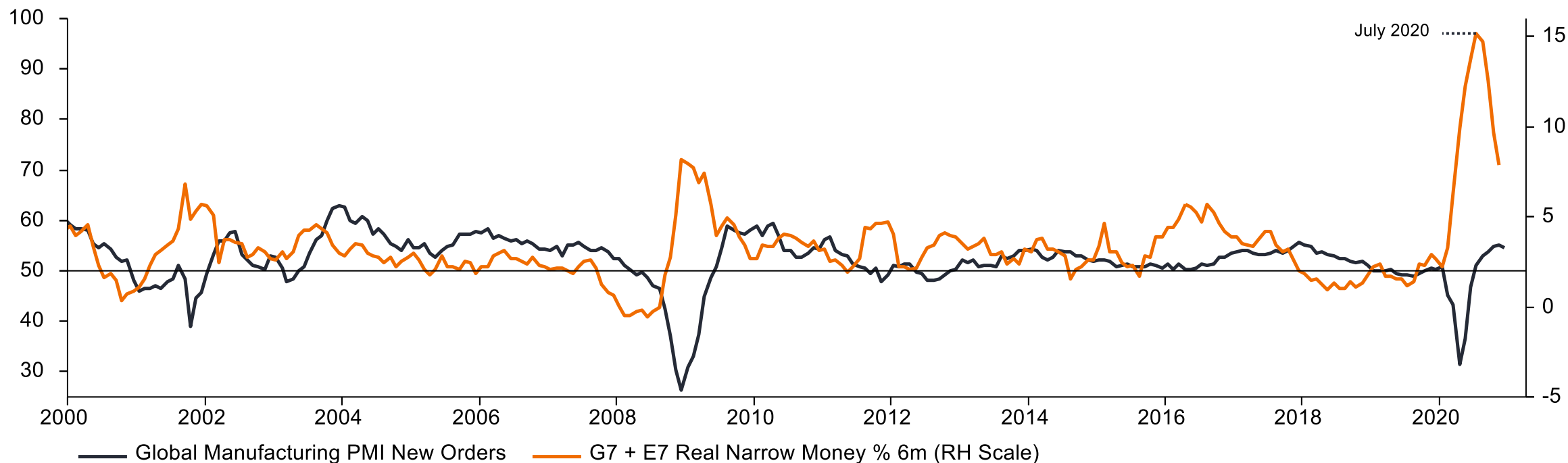


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# GLOBAL ECONOMY & MONEY TRENDS

Average lead time at turning points = 6-7 months, PMI new orders peaking?

Global Manufacturing PMI New Orders  
& G7 + E7 Real Narrow Money (% 6m)



Source: Refinitiv Datastream, own calculations, as at 11 January 2021



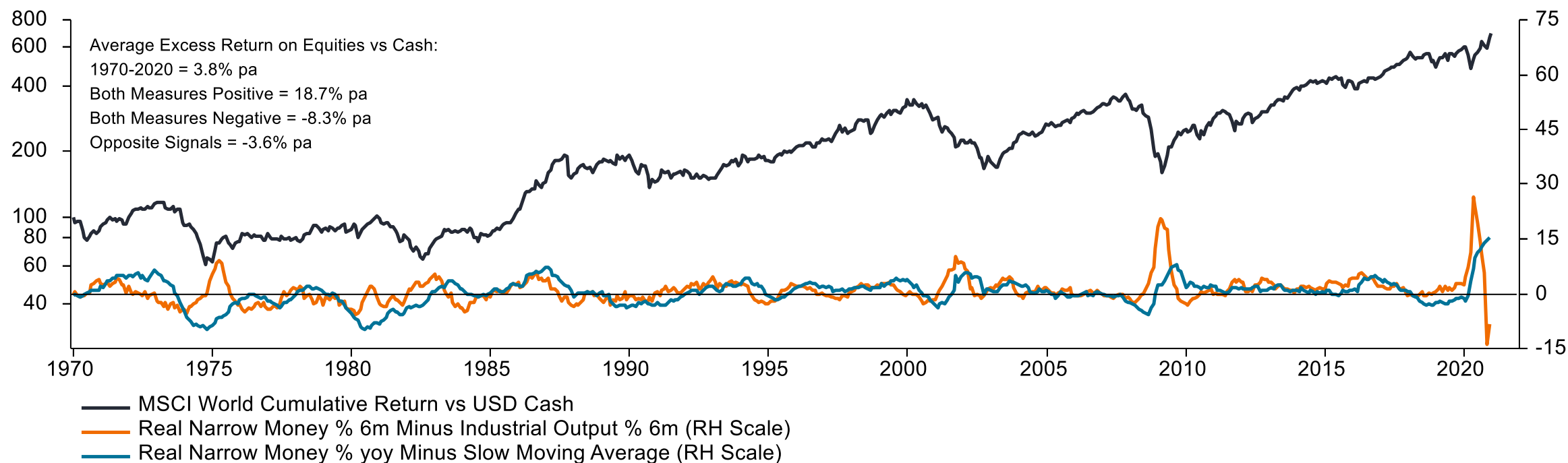
# MONEY & MARKETS

- Real money growth in excess of the rate needed to support economic expansion is associated with an increase in demand for financial assets and upward pressure on prices (“money moves markets”)
- Proxy measures of “excess” money:
  - 1) Difference between real narrow money growth and industrial output growth
  - 2) Difference between real narrow money growth and long-run average

# GLOBAL EQUITIES & “EXCESS” MONEY

Both measures positive from Q2 2020, measure 1) currently negative

## MSCI World Cumulative Return vs USD Cash & Global "Excess" Money Measures



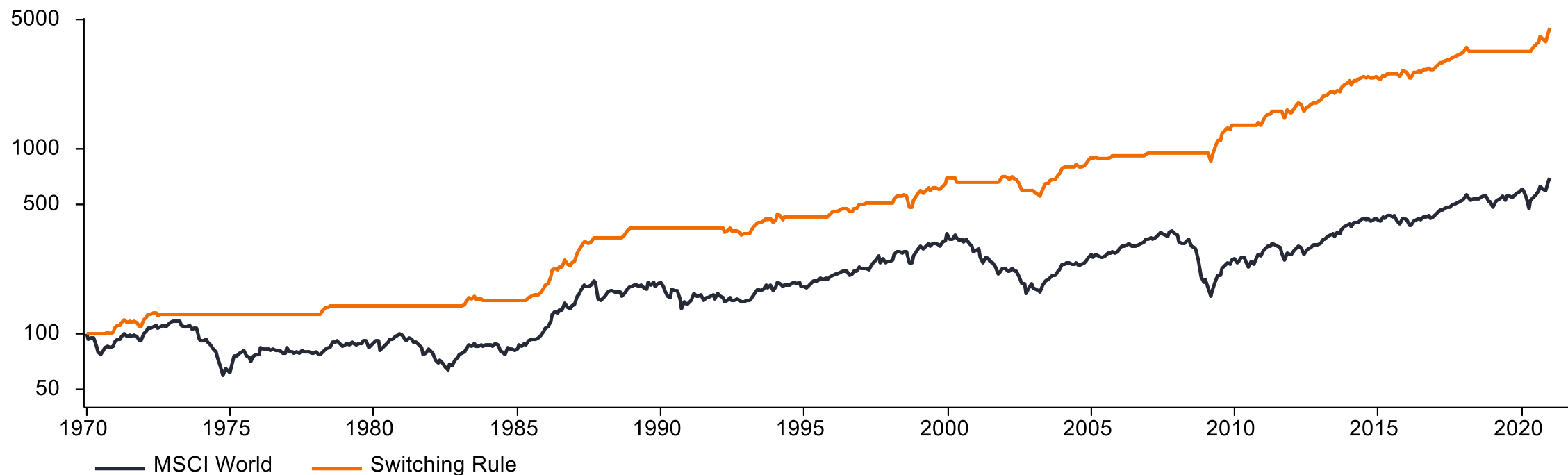
Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# GLOBAL EQUITIES & “EXCESS” MONEY

Simple rule switch into equities reversed at end-2020

Cumulative Return vs USD Cash: MSCI World vs Switching Rule

Switching Rule: Equities If "Excess" Money Measures > 0, Otherwise Cash



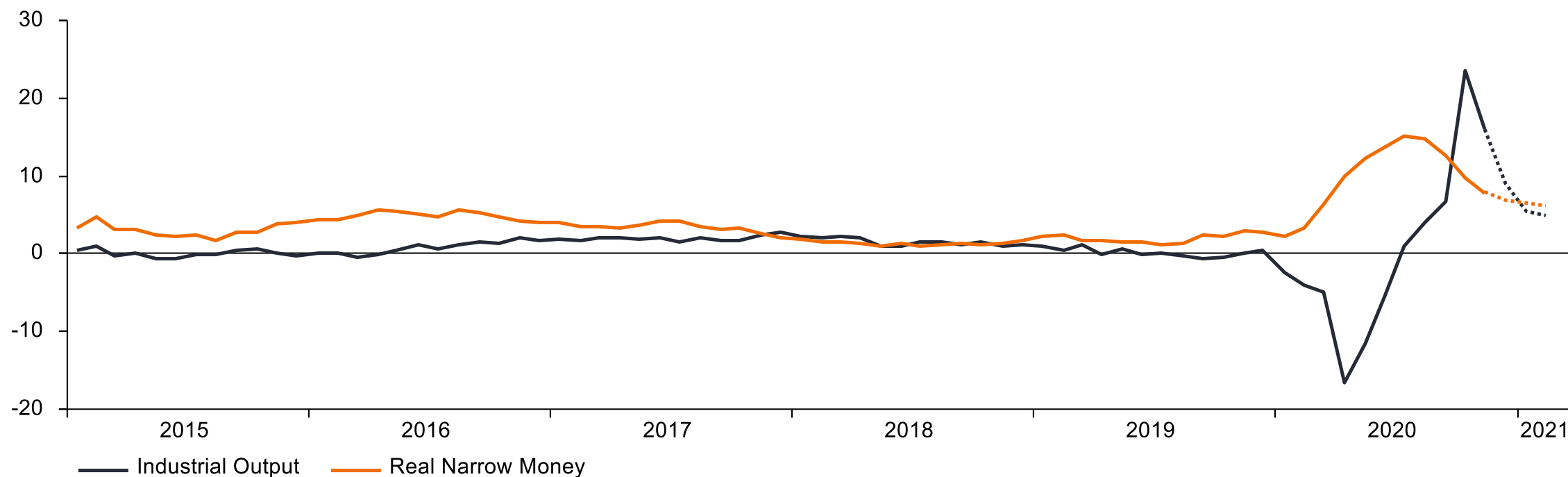
Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# GLOBAL ECONOMY & MONEY TRENDS

“Excess” money measure 1) to return to positive in Q1?

G7 + E7 Industrial Output & Real Narrow Money (% 6m)

Dotted = Projections

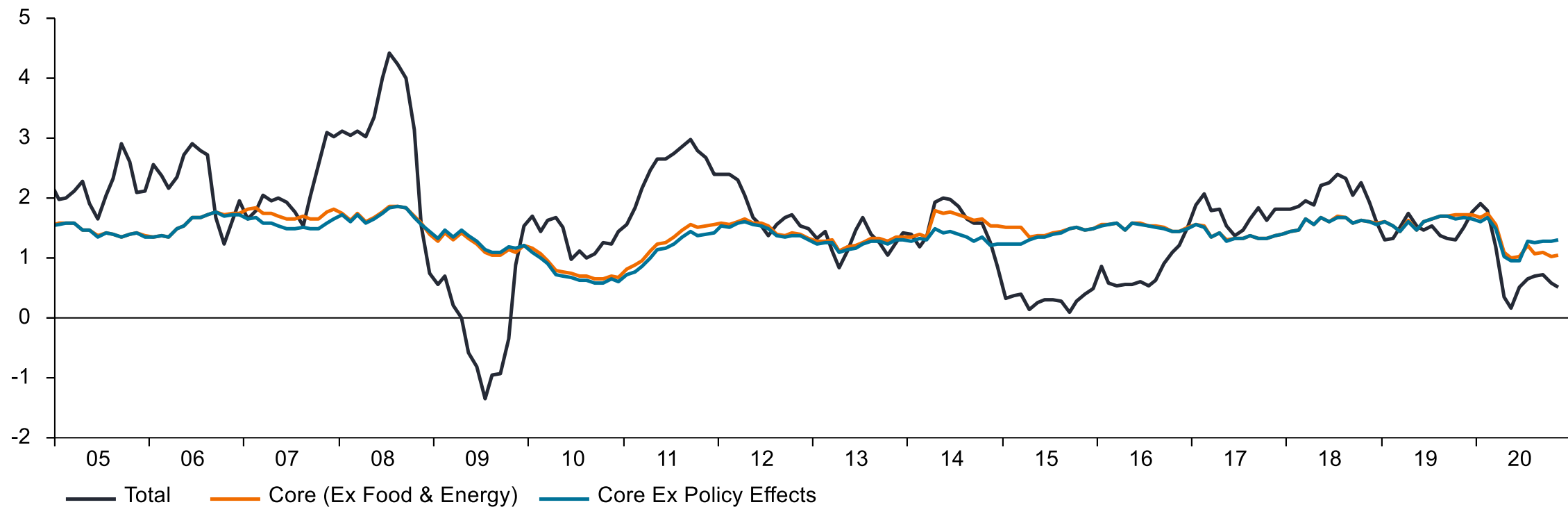


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# GLOBAL INFLATION

“True” core inflation close to post-GFC average

G7 Consumer Prices (% yoy)



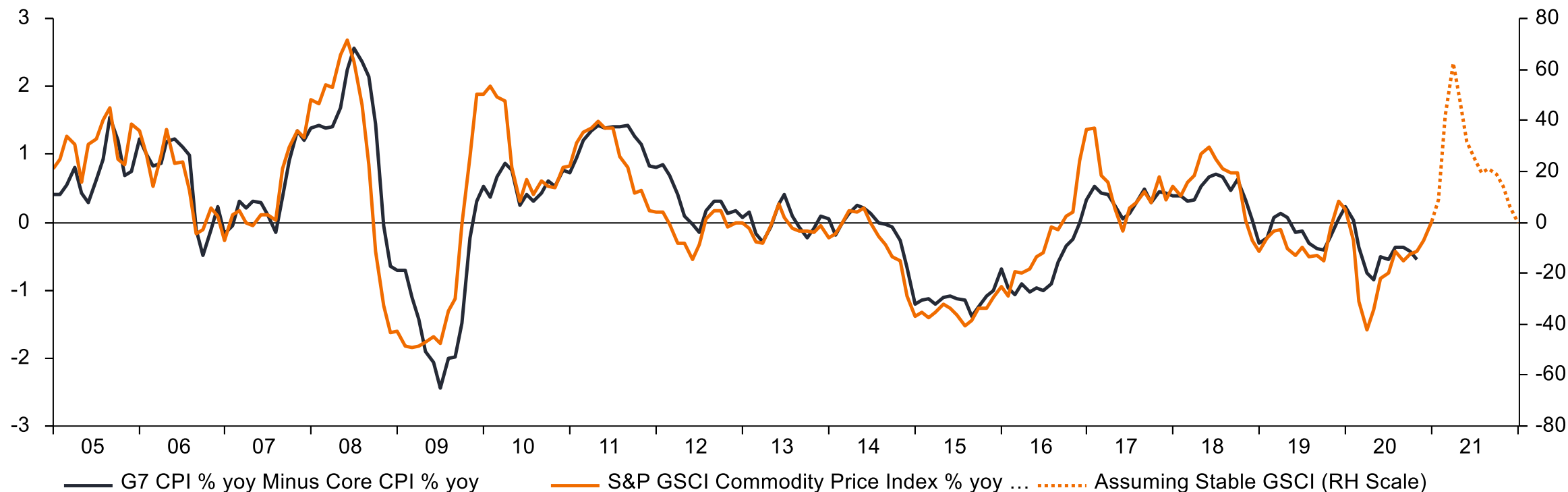
Source: Refinitiv Datastream, own calculations, as at 11 January 2021



# INFLATION & COMMODITY PRICES

Sharp rise in headline inflation ahead

G7 Headline / Core CPI Inflation Gap & Commodity Prices (% yoy)

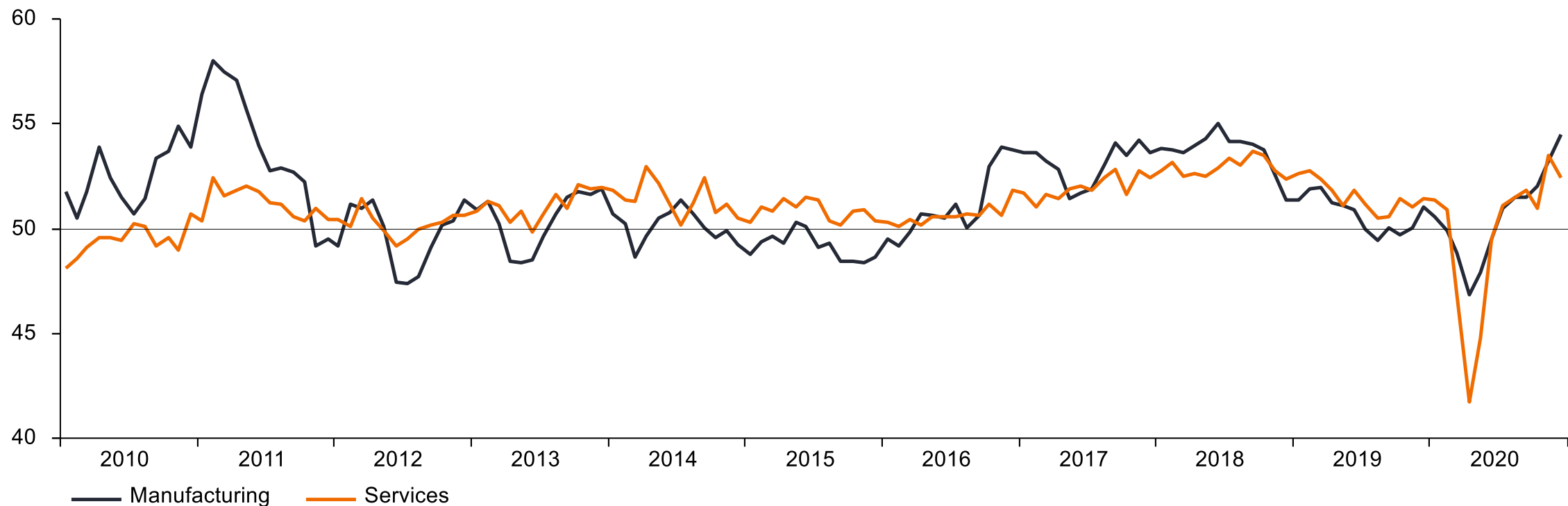


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# GLOBAL PMI PRICE INDICES

Earlier / stronger rebound than after GFC

Global PMI Output Price Indices

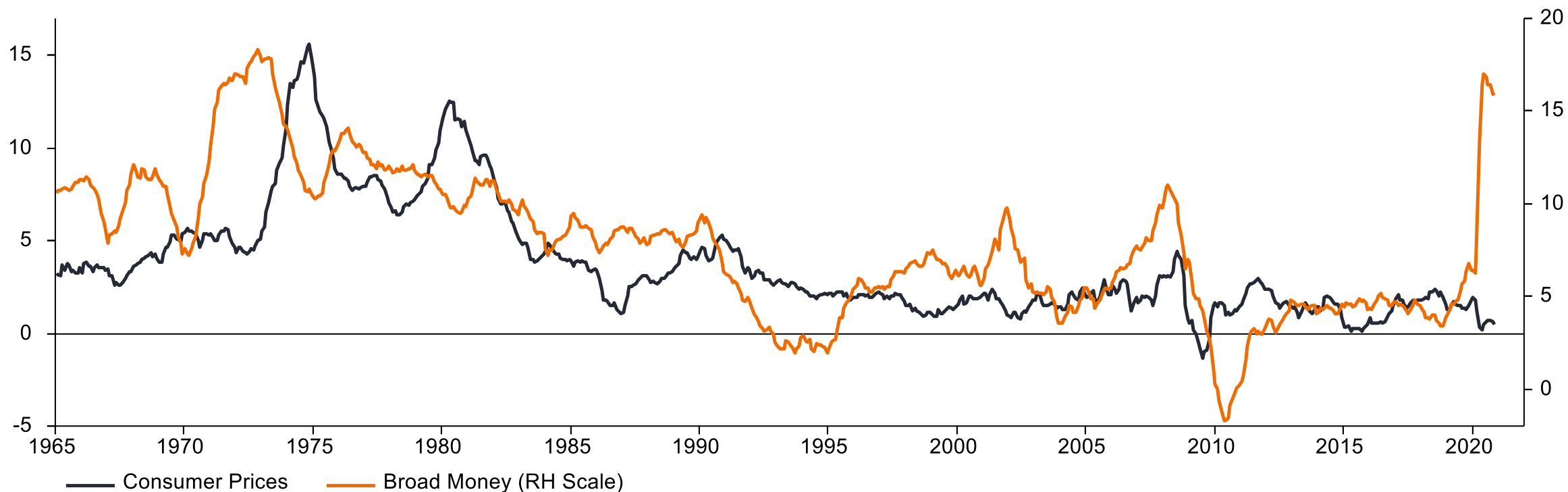


Source: Refinitiv Datastream, as at 11 January 2021

# GLOBAL INFLATION & MONEY TRENDS

Monetary backdrop more expansionary than before prior “cyclical” inflation upswings

G7 Consumer Prices & Broad Money (% yoy)

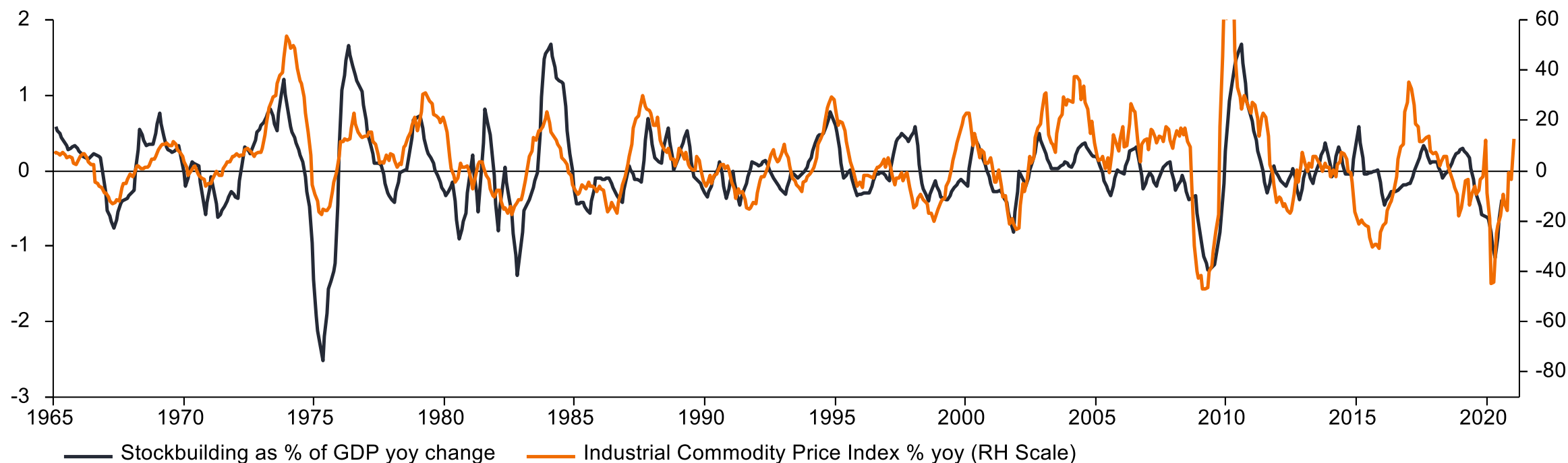


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# STOCKBUILDING CYCLE & COMMODITY PRICES

Commodity prices correlated with cycle, further strength suggested

G7 Stockbuilding as % of GDP (yoy change)  
& Industrial Commodity Prices (% yoy)

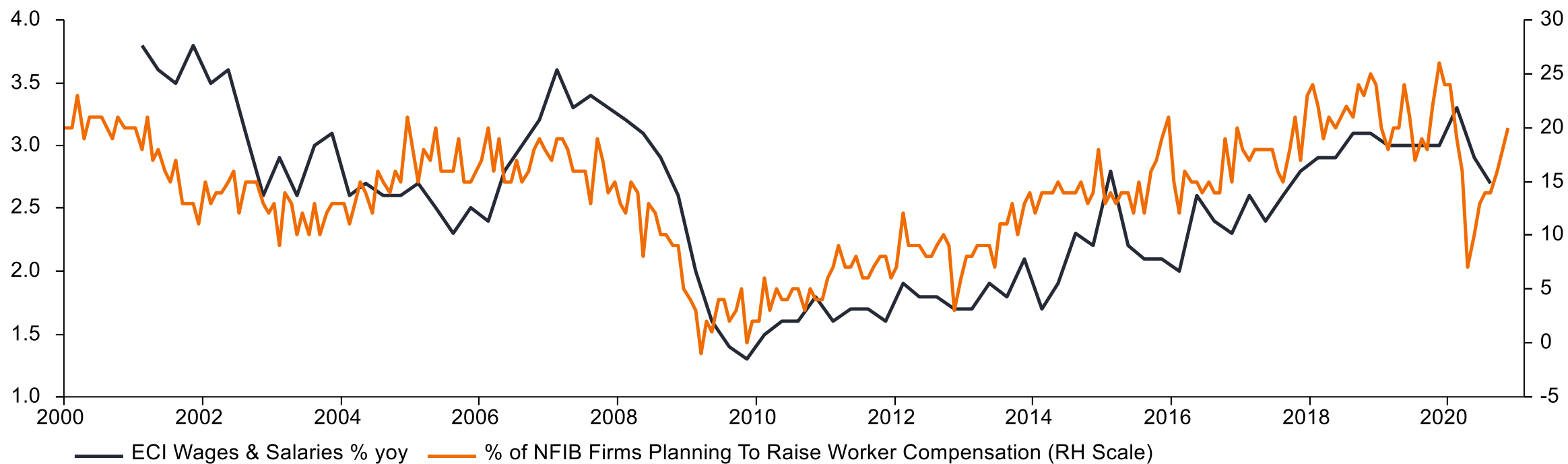


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# US WAGE INFLATION

Disinflationary impact of labour market weakness modest / temporary?

US Private Hourly Wages & Salaries (% yoy)  
& NFIB Worker Compensation Plans

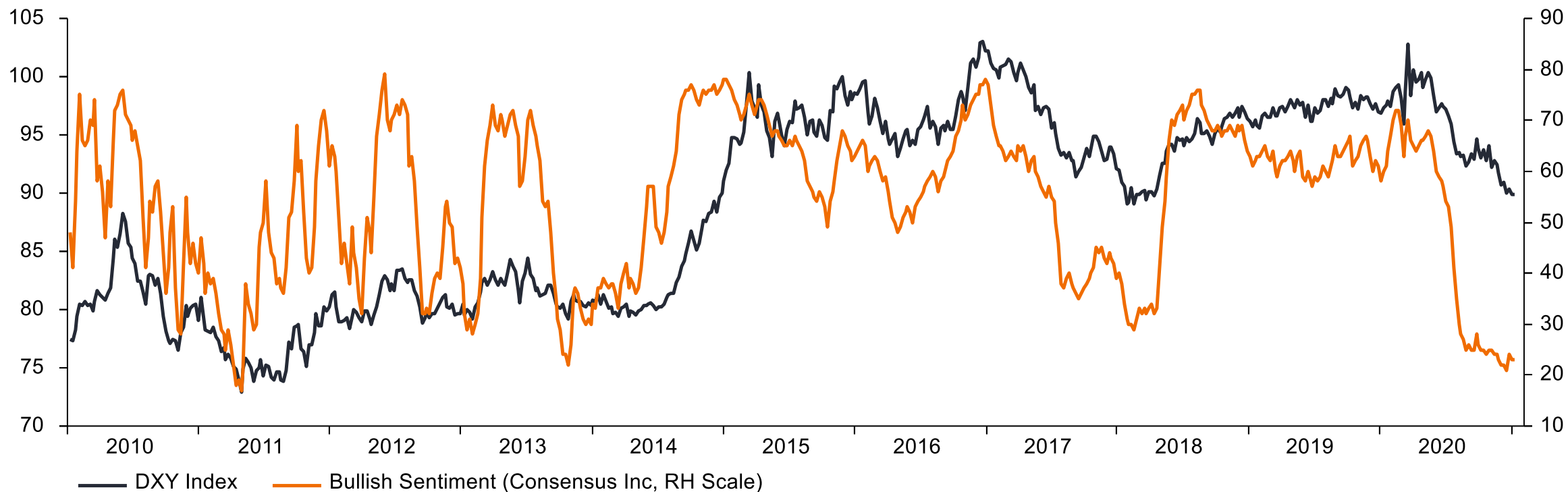


Source: Refinitiv Datastream, as at 11 January 2021

# CONSENSUS VIEWS

## 1) US dollar to weaken further

DXY Index & Bullish Sentiment

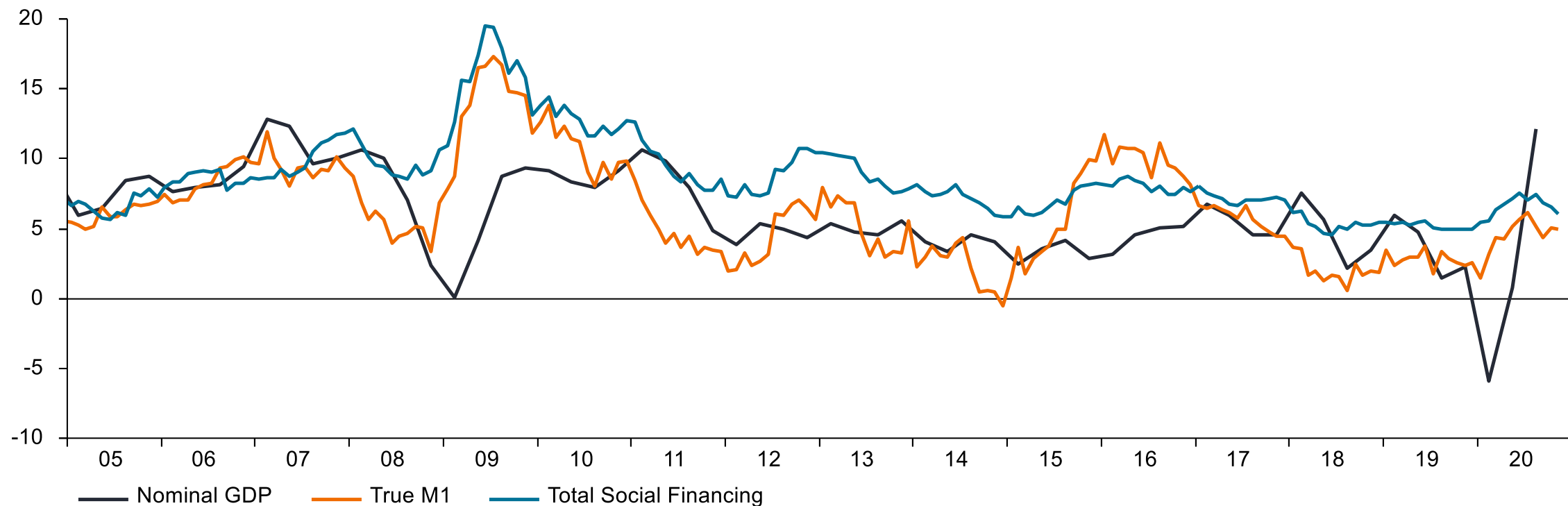


Source: Refinitiv Datastream, as at 11 January 2021

# CONSENSUS VIEWS

## 2) EM equities to perform strongly

China Nominal GDP & Money / Social Financing (% 6m)

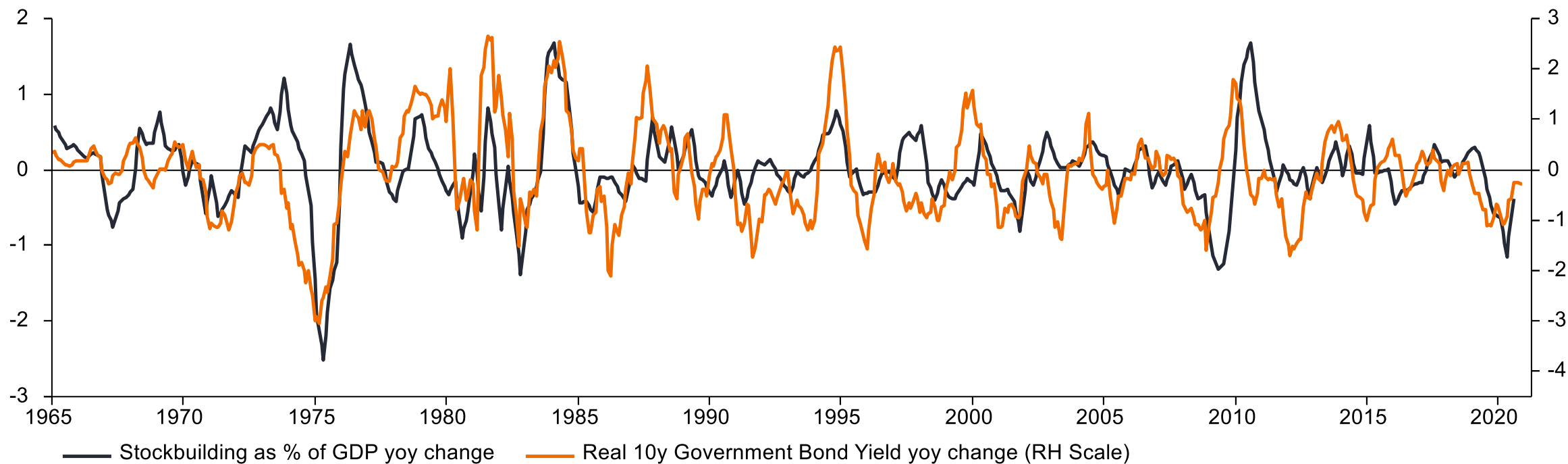


Source: Refinitiv Datastream, own calculations, as at 11 January 2021

# CONSENSUS VIEWS

## 3) Real yields to stay low

G7 Stockbuilding as % of GDP (yoy change)  
& Real 10y Government Bond Yield (yoy change)



Source: Refinitiv Datastream, own calculations, as at 11 January 2021



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