JUNE 2022

The Institutional Strategist

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GLOBAL MARKETS

Equity & Fixed Income Markets
Market Themes and Stocks

Featured This Month:

Americas' Equity Market

Crude Oil and the Transition - The Coming Price Spike

European Equity Market

European Outlook – June 2022

Asian Equity Market

China: In a Transitional Period

by TIS Group, Inc.
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GLOBAL MARKETS TABLE OF CONTENTS
JUNE 2022

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PURPOSE:
The Institutional Strategist is a third party, independent, monthly publication, covering geonomics, global stock markets, interest rates, market themes, and currency trends. Our purpose is to present non-consensus, timely analysis designed to call major "turns" and to assess various forms of global risks.

COVERAGE:

Each month we assess investment/ economic risk across major asset classes, and analyze geo-political developments in the world's top economies and financial markets.

A. Major Market Themes

US

- A major secular effort aimed at warding off deflation / depression is underway, including re-thinking monetary / fiscal policy to address social / environmental issues and income inequality. Great Society 2 fiscal spending is dominant US policy now. Inflation has been one of the by-products and will be accepted as a necessary cost up to a point. That "point", 7% CPI has been reached, turning the Fed hawkish. We would not be surprised by a 10% CPI print in the near term and 10%-15% longer term. The actual inflation rate "feels" higher.
- Wage pressure is building as over ten million jobs remain open.
- The US has cost push inflation now, not demand pull inflation. Service inflation is about to get a boost along with further wage pressure and commodity shortages. The Fed will have difficulty dealing with inflation as Sanctions, supply chain disruptions and a lack of cap-ex are the problems. Then there is a sudden drop in productivity, the largest in years.
- Regulatory/tax burdens on tech/financial companies are likely to grow.
- A 15% minimum global income tax has been agreed by the G-7 and over 100 countries. But will it become US law?
- Major shifts in US government spending, taxes, regulation and political re-alignments are unfolding. Austerity is out, spending, income support and reflation-oriented policies are in. Another "health-related crisis" or expansion of the Ukraine war, would be very damaging to the economy, especially if new lockdowns were implemented. Increasingly, it appears the pandemic is moving toward being an endemic.
- Stocks are well off a record high. There are signs of excess in parts of the economy, i.e. a housing boom, used car prices booming, inflation, negative real yields, etc., some of which are just beginning to moderate.
- US equities remain in a bearish trend, interrupted by sharp, short rallies.

Europe

- EU Commissioner, Ursula von der Leyen had a plan to grow Europe's economy in 2020, but due to the pandemic, kick-off was moved to 2021. It includes large scale fiscal spending, deregulation and significant "green" spending. "Green" spending remains a feature of EU / ECB policy. Germany was to shut down its nuclear plants in 2022 and rely on wind power, renewables and Russian gas. That plan has changed. We expect Germany will import more LNG, restart nukes and possibly utilize coal. Anything less probably results in a power crisis this winter.
- Will fiscal spending / monetary policy be able to reflate Europe's economy and European stocks? The war in Ukraine has changed the outlook in Europe on many fronts.
- Little was done to reform the EU banking sector after the 2008-2009 crash. The last European recession took out Greece and nearly took down Italy / Spain. This time, the EU is pushing a growth agenda, which should help the banks, but a flat yield curve constrains NIMs and bank lending. EU bank stocks remain well below their all-time highs.
- European bank exposure to derivatives and leverage generally, may be Europe's Achilles heel. Some German banks and French / Italian banks are still problematic, years after GFC ended.
- Foreigners and even domestic investors are likely underexposed to EU stocks, just as foreigners are probably underexposed to US stocks. The ECB has been unable to reflate European equities over the last ten years despite massive monetary reflation. An attempt at cyclical reflation, based on fiscal spending and easy money, is underway and European equities benefitted in 2021. However, 2022 has been a difficult year for stocks with a new set of problems to price.
- Europe and EM stocks are cheap vs US stocks. Valuation differentials between Europe, the UK and the US are at attractive levels. Relative performance of Europe vs the US should improve gradually, especially if value investing returns to favor – which on the charts, it is trying to do. Europe "Green spending" is the EU's plan for growth. It will also incur another surge in debt.

China

- Expectation for China's actual GDP to be around 2-3% this year and 3-4% in 2022.
- China's economy has grown from nowhere 40 years ago to accounting for 17.4% of global GDP in 2020.
- Domestically, there is a leadership squabble even though Xi will probably be re-elected for a third term, his authority may be cut.

- Due to disenchantment with policies that have been pursed over the last year or so, business and household confidence has been shattered and will take months to recover despite the stimuli packages that are being unveiled almost on a daily basis.
- China may have to continue experiencing rolling lockdowns into 2023 so causing impediments to economic recovery.
- Weakening global business activity will impact exports; and relations with America, Europe and others are getting worse.
- A critical problem for Xi is the now obvious American containment policy and defense of Taiwan. Economic confrontation is clear-cut with a military one remaining a huge risk, one that could become an actual event in 2024.
- China will have to navigate the difficult international environment and the likely global asset crash over the next two to three years before embarking on real growth strategies. Until then the objective is just to stabilize the economy.
- China has the resources to recover: high savings, some 860 million having incomes below the national average, an enviable supply-chain infrastructure, the BRICS as an export base and gold reserves of over 40kt.

III. GLOBAL MARKET MODELS

Global Asset Allocation
USD Reference Currency

Unconventional Allocation (Tactical)

		% of Total
CASH	USD	31%
STOCKS	ProShares Short QQQ ETF (PSQ)	14%
	KraneShares CSI China Internet ETF (KWEB)	10%
	SPDR S&P Oil & Gas Exploration & Production (XOP)	10%
	TIS Energy Security/Infrastructure Basket: (Tamarack Valley Energy, Baytex)	6%
	Energy Select Sector SPDR Fund (XLE)	5%
	VanEck Vectors Gold Miners ETF (GDX)	5%
	Hang Seng Index (HSI)	3%
	ETFMG Prime Junior Silver Miners ETF (SILJ)	3%
* ALTERNATIVES	Gold (GOLDS)*	5%
	Global X Uranium ETF (URA)	5%
	Silver (SLV) *	3%
	TOTAL	100%

OVERVIEW:

US Dollar — A growing problem with unfunded liabilities / medical care / Social Security funding / pension funding, and a surging budget deficit should eventually force the Dollar lower, unless significant revenue raising measures are made or budget cuts are enacted. Tax hikes to pay for additional spending remain unpopular among business, the middle class which is being squeezed by higher inflation. A commodity bull market which is increasingly driven by China, while global supplies are sanctioned / restricted, are a real risk.

Intermediate term, the Dollar looks stable to lower as the Fed will eventually be forced into further balance sheet expansion and QE / yield curve control will eventually be employed. If recession conditions occur, look for the Fed to pivot. An outside the box risk (a higher Dollar) is a liquidity / economic / financial problem coming from Europe, a breakdown in China credit market or a crypto issue which pushes USD even higher. Inflation is becoming a major issue with inflation expectations hitting multi-year highs and commodities in a bull market. This is a cost-push inflation environment due to a shortage of goods, a lack of cap-ex and supply chain issues. This is not something the Fed can do much about.

On a 1–2-year basis, the monetization of US debt seems more and more likely, which should encourage the Dollar to move lower. Inflating away $30 trillion of government debt and more than $50 trillion in liabilities / entitlements seems like a plan. Intermediate term, the USD should move lower.

Euro/Dollar — The US will eventually need a higher Euro / lower Dollar while Europe is almost always happy with a weak Euro. Near term, Euro / Dollar should continue to rally from an oversold position. If it does not bounce off the 1.08 level, the USD could go lower very quickly.

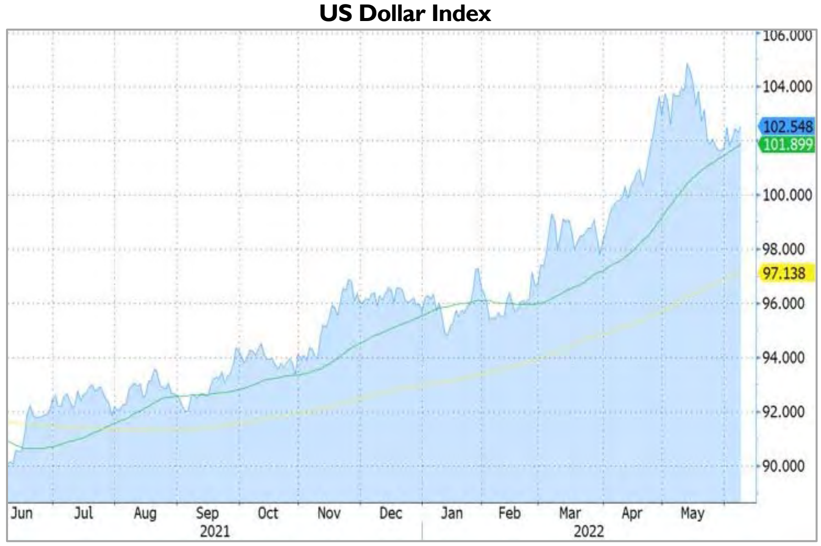
Yen/Dollar — Japanese yield targeting, sets the stage for the same policy in the US. That USD/Yuan/Yen triangle is crucial for Asian trade and global growth. The BOJ was first in zero rate policy, many years ago. There is no sign yet, that they will be the first to exit.

Japan was also the first major country to go into deflation, years ago. Though it seems unlikely, if Japan sees a new burst of inflation, where will Japanese interest rates go? In to what assets will Japanese investors move? And what asset classes will they depart? This will be important for global capital flows and negative for the Yen. Investors in JGBs continue to sell, which bumps 10-year yields up against the 0.25% barrier.

Taiwan is becoming a larger and larger issue for Japan. Japan appears to have aligned itself increasingly with US defense policy and the Indonesia-Pakistan Trade Agreement and the Quad. Japan's government is in the early stages of designing a more offensive military policy which will be expensive.

We are cautious about credit conditions in China which are still troubled, especially in the property market. This effects China's economy, therefore Japan's as well. As China's economy weakens and US growth slows, the Yen should weaken and it has, perhaps by too much/too fast. How events play out in Europe, may yet turn the Yen into a safe haven currency. All things considered, Yen/Dollar seems too low, but it may go lower.

US Dollar Index



Courtesy of Bloomberg LP

Data Sources:
Barron's, 6/6/2022
Investor's Business Daily, 6/6/2022
The Economist, 6/11/2022

S&P 500 Index

Courtesy: Bloomberg LP

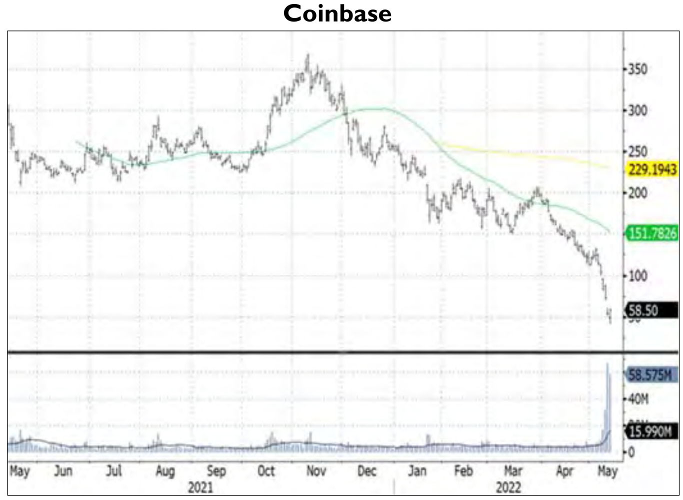
Where is the Low in US Stocks?

In a recent piece, I suggested the PE on the S&P 500 had another 1-2 points to lose, so two things now matter most. The E in PE is one factor and, on that score, the outlook is not great. I will explain in the section below. The second factor is liquidity. If I had any doubts about crypto's ability to overcome liquidity issues, act as a hedge against inflation, ride their own liquidity tide, they are gone. This is just weeks after a massive Bitcoin / crypto convention in Miami, where all the signs of excess were present, cryptos have shown us what happens when liquidity disappears. These were the types of statements going around. Several trillion Dollars in value have disintegrated as stable coins have proved unworthy of their name and Bitcoin has fallen more than 50% since the November 2021 high. I don't think there will be enough collateral damage from the crypto bust to send stocks much lower, but there has been some effect. Look at the charts of Robin Hood and Coinbase, two venues where retail traders have gathered.

Robinhood Markets

Source: Bloomberg LP

Coinbase



Source: Bloomberg LP

The bigger issue for stocks now is the uncertainty of how the US economy (and the Chinese economy), move in the next few months. The UK is headed for a brief recession at minimum, as is the EU. Emerging markets are fighting the DXY tape, which I remind everyone, Mr. Addison has noted a move to 120 is possible on the chart. Think about what cross rates would have to do to get DXY to trade to 120. Euro/Dollar would likely blow through parity. Dollar / Yen would go to 150. Sterling would likely trend back toward the mid 1980's lows vs the Dollar. Calls for a Louvre type accord to weaken the Dollar would build. Emerging markets would be decimated. Currency pegs such as the HKD/USD would come under huge pressure. Commodities would likely fall for the most part, though I caution that the CRB's run over the past 18 months occurred while the Dollar rose. A rise in currency volatility is right around the corner.

I listened recently to an explanation on financial television about why the US consumer would not be bothered to curtail spending. It was rather hard to believe that record gasoline prices, record diesel prices, 8% Inflation, 11% PPI, rents going through the roof, food inflation running very high and potentially going much higher in the months ahead, was to be offset by cash holdings and strong wage growth. Wages have not kept up with CPI. As far as cash holdings are concerned, the crypto world just lost the equivalent of 10% of GDP. The Faangs alone have done even more damage, more than 10% of GDP over the past 6 months and it is consumers who own the cryptos, the Faangs and tech stocks – not all of them but the consumers asset accounts have been hit. Some of their financial cushion is gone. The panic has not even started yet in stocks.

In China, the economic omens are not great. The government says GDP will grow by 5% or so but I don't believe that. Shanghai is in its 7th or 8th week of lockdowns and the traffic data, transport movement and some of the early economic releases which covers April, shows very sharp declines. There is no sign of a let-up in Covid zero policy, the Dollar is cutting off EM growth and the way China is importing food, oil and natural gas, it does appear Beijing is preparing for something of a change. Is the surprise later this year, as to how aggressive Beijing becomes toward the US?

For the sake of argument, let's assume Chinese GDP actually falls in Q2 and Q3 and the full year number is negative. US exports are likely to be down anyway given Dollar strength and if China's economy falters, EM economies follow China lower and are hurt by a rising Dollar, where does that leave the US "E" in PE? I think it goes lower and the equity market has not priced a further deceleration in corporate earnings. How much liquidity is in the financial system will be crucial, and for now, the Fed wants financial conditions to tighten - ergo stocks should fall.

35% declines on a y-o-y basis normally represent reasonable buy points. The S&P 500 would have to trade down to about 2,750-3,115 to move into the buy range. It's not too late to sell.

Sources:
Bloomberg Data
Bloomberg News

Global Slowdown into August 2022

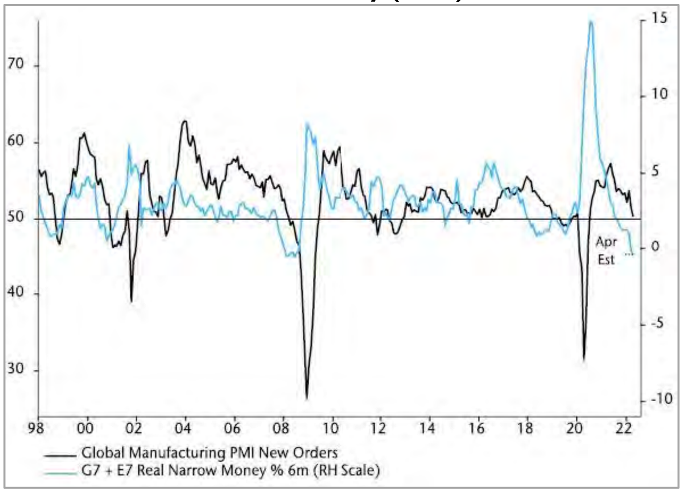
The following article is written by Simon Hunt, who writes for TIS Group's Frontline China Report. If you are interested in articles similar to today's piece, please contact Larry Jeddeloh at tis@tisgroup.net

"Everybody worships at the New Keynesian altar, in thrall to the canonical 'dynamic stochastic general equilibrium' (DSGE) model of Ivy League academia and modern central banking." **Ambrose Evans-Pritchard**, Daily Telegraph

"Every 40 years or so, something Bad happens. Every 80 years or so, something Really Bad happens." **Garrett Jones**, Observations, May 17th 2022

Whatever the pitfalls, such as the leads and lags, measures of money supply provide leading turning points in business activity in contrast to the modern Keynesian DSGE models. The former are real-time business indicators; the latter are politicized fiat money models.

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



Source: Simon Ward, Money & Cycles Weekly Bulletin

The chart shows that a key measure of the money supply, namely six-month real money annualized is now sharply negative across the fourteen largest developed and emerging market economies. Not only should these monetary trends signal a sharp fall in global PMI new orders, but the chart should act as a wake-up call for those in the metal markets who cling to the belief that prices can only go higher.

Declining real money supply across 14 countries has already shown up in the global PMI data as set out in the JP Morgan Manufacturing PMI for April. The percent changes for April this year compared with April 2021 tell their own story.

Global Manufacturing PMI April 2022 vs April 2021 % Changes

PMI	-6.5%
Output	-13.0
New Orders	-11.3
New Export Orders	-11.9
Future Output	-3.0
Employment	-2.0
Input Prices	+3.2
Output Prices	+6.7

April should be followed by sharper declines in the PMI data declining below the 50 level by the Autumn.

In the USA, the University of Michigan's gauge of consumer sentiment fell to 59.1 in May from the April reading of 65.2, its lowest level in more than 10 years; and consumers' assessment of their current financial situation relative to a year ago is the lowest reading in 13 years. For consumer durables, buying conditions reached their lowest reading since the survey began questioning these goods in 1978. High prices were the main reason for the weakness.

In short, America's GDP should rise by just 1% this year.

In Europe, the sentiment indicators slipped in April, consumer confidence slipped and industry confidence fell by 0.8% reflecting an improvement in managers' assessment of stocks of finished products. After over a year of record low assessment of stocks, there are early signs that inventories are being replenished. But the improvement in inventory assessments may be the result of new orders falling by 6.9%.

However, the auto business is the backbone of Germany's manufacturing. In the first four months of the year, car registrations fell by 9%. Liquidity conditions are likely to tighten with the ECB's policy normalization process likely to include a reduction (or end) to long-term lending to banks according to Goldman Sachs. With Euro 2.2 trillion of TLTRO financing outstanding, this should see excess liquidity in the Euro area drop, even without bond quantitative tightening.

Rising oil and gas prices together with food prices soaring will mean that the European economy will be in recession by year-end.

The Chinese economy is effectively now in recession, whatever are the official numbers. Today's (May 20th) reduction to the 5-Year Loan Prime Rate from 4.60% to 4.45% whilst keeping the one-year rate unchanged suggests that the focus is on a revival of the housing market.

However, consumer sentiment has been so badly hit over the past year that a drop in mortgage rates and lifting of local government restrictions is unlikely to lead to any meaningful recovery of the housing market for some months. The same can be said for business sentiment; it will take time for business sentiment to be repaired especially in the all-important private sector.

Announcements of many large infrastructure projects are more likely designed to improve sentiment rather than what will be seen on the ground. Local government revenues have fallen sharply and their ability to borrow is constrained at a time when they have fixed costs to cover (employment, salaries etc.)

Hope is being generated by the gradual lifting of lockdown restrictions in Shanghai but other cities across the country remain locked down thus making the logistics of moving goods across the country difficult. It may yet take several months before the country is free of these restrictions.

Meantime, there are several rumors of a pushback against Xi being given a third term, many of which originate from overseas and recirculated domestically. All that we can say at this stage is that they are rumors for he has the full support of the security services and the PLA as well as nearly all of the country's rural population – 540 million.

Overriding these regional developments, is continued war being fought between Russia and NATO over the lands of Ukraine. The big risk is that this war will spread to other European countries by the autumn together with China being increasingly worried by America's growing overt support for Taiwan.

This is a short note to emphasize our concerns that the world economy to slipping towards recession by the Autumn with consequential further large falls in equity and commodity markets before central banks move from QT to QE causing modest global recovery but roaring inflation into 2024.

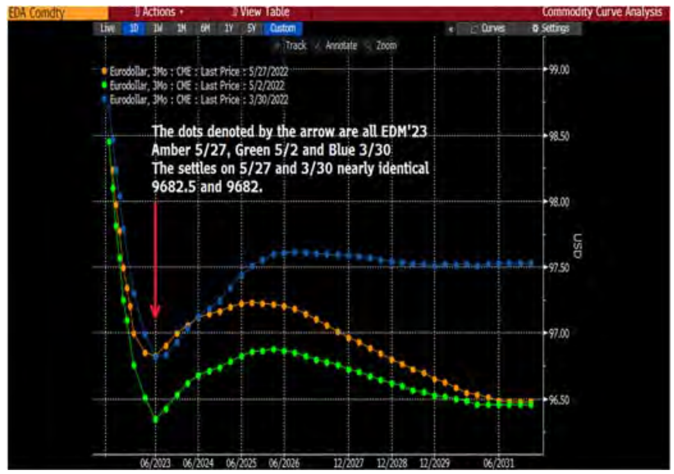
Source: Simon Hunt Strategic Services. May 22, 2022

The End Game

The following article was written by guest author Alex Manzara at R.J. O'Brien in Chicago for TIS Group.

Below is a chart of the Eurodollar futures curve on three dates: May 27th (amber), four weeks earlier on May 2nd (green) and two months earlier on March 30th (blue). As shown, the lowest near-term dot (within five years) has been the June'23 contract. On March 30th, the settle was 9682 or 3.18%. The steep decline prior to June reflects 'front-loaded' hiking, expected to occur in 2022 through the start of 2023.

The low settle in the June'23 contract was on May 3rd at 9631.5. Since that time, it has been grinding higher, (to a lower yield). What does this chart tell us? First, it indicates the market's assessment of what the peak Fed Funds (FF) target is going to be in this hiking cycle, and when. If we use a spread of 25 for the Fed Effective rate to the Eurodollar, then 9682 or 3.17% is more or less consistent with a FF target of 2.75-3.00% (effective federal funds rate, EFFR, would be 2.83%). At the absolute low in early May, the market perceived a target FF of 3.25 to 3.5% (or perhaps a shade higher).



As the month has progressed and stocks wobbled, the market pared back its assessment of the peak FF target, even though official inflation figures remained high. There are a couple of other takeaways from this chart. The first is nearly imperceptible on this graph, but the market is also slowly moving the timetable forward with respect to the end of Fed tightening. Dots to the immediate left of the June'23 contracts are March'23. On the blue and green plots, the March contract is significantly higher than the June contract.

Below is a graph isolating the EDH3/EDM3 (March 2023/June 2023) calendar spread. The decline in this spread over the past few weeks is signaling that the market is moving its perception of the end of hikes nearer in time. The low settle in EDH3/EDM3 was 0.5. That means that both contracts were essentially the same price, and that March is close to becoming the weakest contract. That is, March is where the market is forecasting a peak inflection point between hiking and easing.

There is one other very interesting aspect to the top chart, and that is the forward rates a few years from now. First consider the blue line from the end of Q1 (March 30th). The Eurodollar curve was forecasting a high FF target of about 2.75-3.0% but within a couple of years, a shift down to about 2.25%. An interpretation would be that inflation will be "beaten" causing collateral damage to the economy which would slow appreciably due to front loaded hikes. The green line (May 27th) tells a similar story but with a different ending. Front-loaded hikes (with an even more aggressive trajectory) followed by a subsequent shift lower, consistent with 2.75 to 3.0%, and then a more positive curve again. But look at the amber line: Again, we see front loaded hikes with the subsequent reversion to somewhat lower funding rates, but the reversion features a more modest trajectory, and the highest contract/lowest yield has also been moved forward in time to September 2025 (EDU'25). From there the curve steepens more aggressively than seen in either of the other two timelines. It's as if the market is paring back the peak rate but perceiving a lingering increase in inflation expectations resulting in a steeper forward curve.

Clearly, the message from futures markets can change over time. However, for the duration of this cycle, the perceived peak FF target has never been higher than 3.5%. Front-loaded hikes have not been perceived to continue past the middle of next year. And as of the second half of next year, the market is looking for the possibility of a reversion to lower funding rates. Longer term inflation concerns appear to be growing. Similar to the 1970's inflationary episodes, the market is fearful of another significant wave of inflation emerging several years from now.

The risk of loss in trading futures and/or options is substantial and each investor and/or trader must consider whether this is a suitable investment. Past performance, whether actual or indicated by simulated historical tests of strategies, is not indicative of future results. Trading advice is based on information taken from trades and statistical services and other sources that R.J. O'Brien believes are reliable. We do not guarantee that such information is accurate or complete and it should not be relied upon as such. Trading advice reflects our good faith judgment at a specific time and is subject to change without notice. There is no guarantee that the advice we give will result in profitable trades. Copyright 2022. Alex Manzara.

Asset Allocation

Unconventional Model

		% of Total
CASH	USD	31%
STOCKS	iShares MSCI Emerging Markets (EEM)	10%
	KWEB	10%
	SPDR S&P Oil & Gas Exploration & Production (XOP)	10%
	TIS Energy Security/Infrastructure Basket: (Tamarack Valley	6%
	Energy Select Sector SPDR Fund (XLE)	5%
	VanEck Vectors Gold Miners ETF (GDX)	5%
	Invesco QQQ Trust	4%
	Hang Seng Index (HSI)	3%
	Junior Silver Miners (SILJ)	3%
* ALTERNATIVES	Gold*	5%
	Uranium	5%
	Silver (SLV) *	3%
	TOTAL	100%

CRB Continuous Commodity Index

Courtesy: Bloomberg LP

Crude Oil

The US Department of Energy, after disclosing just weeks ago it would release 1 million BPD from the Strategic Oil Reserve, announced on May 5th it would begin to re-fill the SPR, calling for bids later in the year to buy up to 60 million bpd. This purchase would replenish about one-third of the oil reserves they would be selling. The rationale seems to be to encourage domestic producers to increase production via a guaranteed buyer. I think what they will find is the market has already priced the SPR release, in fact all three of them and in every case, prices moved higher. Recently, WTI ended at $120, a level which is now within striking distance of where it traded at the beginning of the Ukraine war.

Crude Oil WTI

Source: Bloomberg LP

A recession is the best hope for the oil bears, whether it is a US recession or a European recession, or both. Europe's economy is now faced with a third country having its gas supply shut off by Russia - Finland being added to the list along with Poland and Bulgaria. The key market would be Germany and if I heard the numbers correctly, a friend in the UK said his utility bill was rising from 1,200 pounds annually to 3,600 pounds by fall and then the caps come off. I don't know how the UK consumer can tolerate this without it affecting other forms of consumer spending. An energy led recession seems increasingly likely to me, especially if the war in Ukraine shifts in favor of Ukraine and the political turmoil which seems to be emerging in Russia grows in intensity and importance. This is a very dangerous phase of the conflict which is confined to Ukraine now, but I expect it to spread, especially if gas and oil are continued to be used as weapons.

An energy led, European recession will put further upside pressure on the Dollar, as Euro weakness would accelerate. The Euro/ Dollar moving from 1.14 to 1.04 since the war started did little to slow oil's advance. That's an 11% appreciation of the Dollar during which time WTI advanced from $92 to $110, a 20% gain. Wars are inflationary and wars tend to benefit the reserve currency, which remains the USD. No one is fleeing to buy RMB that I know of. Maybe there are is buying of RMB assets, though the Chinese markets do not reflect that. I think the Taiwan Dollar would be more interesting as a safe haven. Every dip in oil prices is an opportunity.

Sources:
Bloomberg Data
Bloomberg News

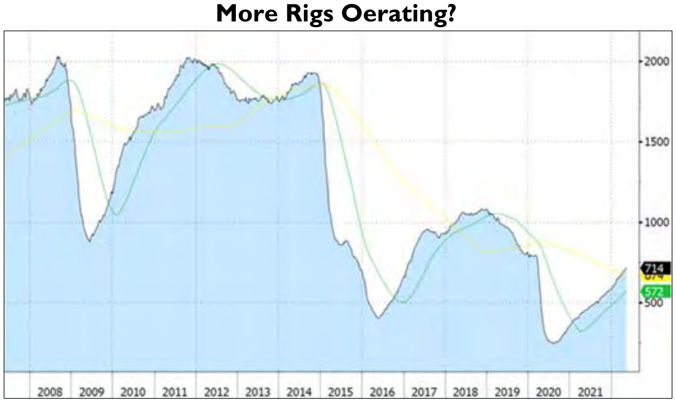
Crude Oil - Going Higher, But How High? US PEs, New Theme

"I am a dinosaur, but I have never seen such things" (1). This quote is from Prince Abdulaziz bin Salman Al Saud and was made while attending a recent conference in Abu Dhabi. The Prince is not a newcomer to the energy world. He has been involved for 40 plus years and what he was referring to is the price of refined energy products. He continued, "The world needs to wake up to an existing reality. The world is running out of energy capacity at all levels" (2).

The world is already short of needed oil production, but also production and refining infrastructure partly due to Russia's problems, compliance from OPEC+ members and regulatory changes plus ESG pressure, especially in the US and Europe. Years of underinvestment led to an almost 3 million bpd shortfall in OPEC+ production in April 2022 alone. An SPR dump from the US did not help. When the West, specifically the US, calls on OPEC to pitch in and increase production, then dumps its own oil on the market and crude prices rise, the warning bells should be going off. Refined product prices will go higher if demand does not shrink or global supplies increase.

It is pretty clear that in America, crack spreads are so high that refiners are producing all they can. OPEC will not help by producing more oil. Russia, while Europeans are lining up to pay for energy in Rubles, is still producing at a lower level. Canada has capacity but the US has shut down the Keystone pipeline, raised royalty rates and talked down energy companies. Proposing windfall profit taxes is not the best way to encourage energy companies to increase their own cap-ex. An Alaskan oil and gas lease sale was just cancelled by the Interior Department, citing a lack of interest. In fact, there are interested parties, including 400,000 Alaskans whose only source of gas is the Cook Inlet where the lease /sale was canceled. There also happens to be military bases in the region, thus the DOD should be interested. One wonders what the thinking is behind a decision like this? Cutting back on gas, which heats homes in central Alaska? Depriving military bases of energy?

Baker Hughes US Oil & Gas Rig Count - Why Aren't More Rigs Oerating?



Source: Bloomberg LP

Then there is China. Something is changing politically in China, but even without any major change in the politically driven economic direction, the lockdowns should conclude before year end, thus improving oil demand further. The Gulf oil producers are warning that the world has not invested enough to meet current demand. If China starts to reflate, there will be an oil price spike, which takes WTI to a new high, above the old peak at $147. If that price spike occurs in the near term, the odds of a global recession increase quite quickly. American equities have not priced a recession. The "E" in PE has adjusted to higher interest rates but not lower corporate earnings. The last 2 US recessions ended with the S&P 500 PE at 11x and 13x. The current PE is around 17x.

The two or three major factors which hold the keys to the markets next moves, I believe are the price of oil, China and food prices. Even the BOE is warning of a problem coming in terms of food prices in the UK. They will be joined by the US and probably Continental Europe as exports from Ukraine dwindle this year, drought grips the US and a move to organics reduces crop yields, not just in Sri Lanka, but anywhere organics are grown. Crude oil is the issue which Middle Easterners are warning us about and they should be heeded. When even producers are warning of prices which may be too high for the global economies to absorb them, it should pay to factor them into our thinking - especially about what consumers can afford. Spending more than $100 to fill up your car and $10 or more for a box of Frosted Flakes is going to cause an adjustment in consumer spending. My spaghetti indicator has re-emerged after two years under wraps. It's a simple measure of inflation, what is the cost of a plate of spaghetti in a local bistro. It was around $20-$22 at the Covid lows. The cost is now $30-$32 but don't worry there is no inflation, nothing to see here. And that -1.4% GDP reading in Q1 for the US economy, ignore that. Perhaps it is time to re-read Extraordinary Delusions and the Madness of Crowds.

I placed a rebound basket in a recent MIR which included Sea Limited, Square, ASML and Cameco. These are trades. There is a new basket forming I will call the cap-ex/infrastructure/secular theme basket. In it, we start with a 3% position in Canadian energy with the Peyto Exploration & Development Corp. and original holdings. Cash is reduced by 3% The model now looks like this.

Baytex

Source: Bloomberg LP

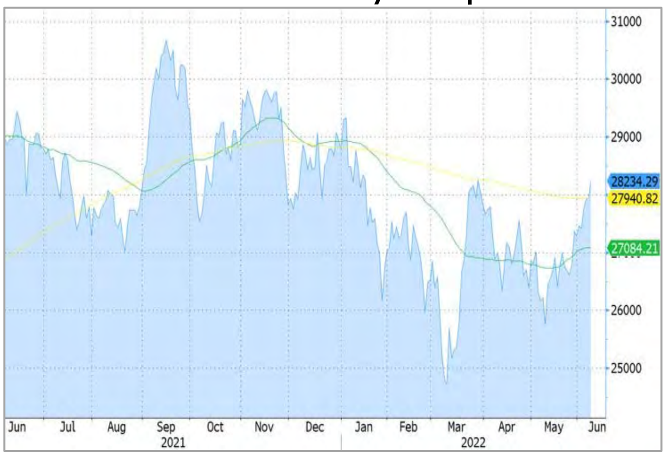
Sources:

Bloomberg Data

Bloomberg News

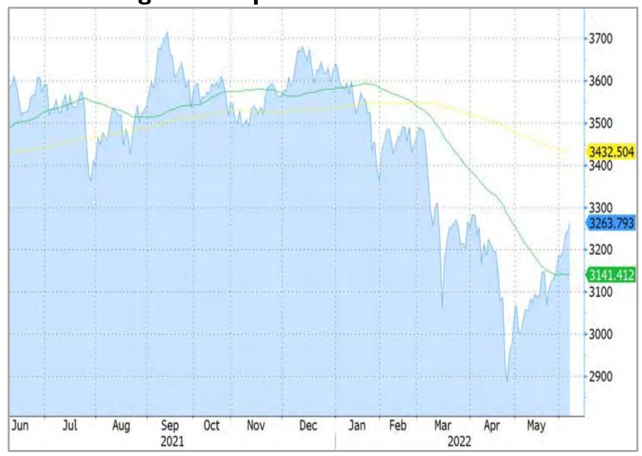
(1, 2) https://www.bloomberg.com/news/articles/2022-05-10/saudi-oil-chief-says-all-energy-sectors-running-out-of-capacity

Nikkei Index—Buy the Dips



Courtesy of Bloomberg LP

Shanghai Composite Index—Sell Rallies?



Courtesy of Bloomberg LP

China to Help the Markets Find a Floor?

In "A Rock & a Hard Place (MIR – 5/3/22), the following was written:

"Beijing may begin stepping back slightly from their relationship with Russia. Yellen recently confirmed that the US was reviewing their trade strategy with China as regards the potential removal of tariffs as one method to try and lower inflation. That has now been echoed by US Trade Representative Katherine Tai who clarified that any actions must be viewed in the grander context of a changing relationship with China. It certainly sounds like the Biden administration is starting to consider measures to limit the expected outcome for the midterms (e.g., student loan forgiveness). So, if Beijing is able to assist with the inflation conundrum to some extent, while putting Russia at arm's length, perhaps the Dollar will start to find some resistance before unintended consequences take over."

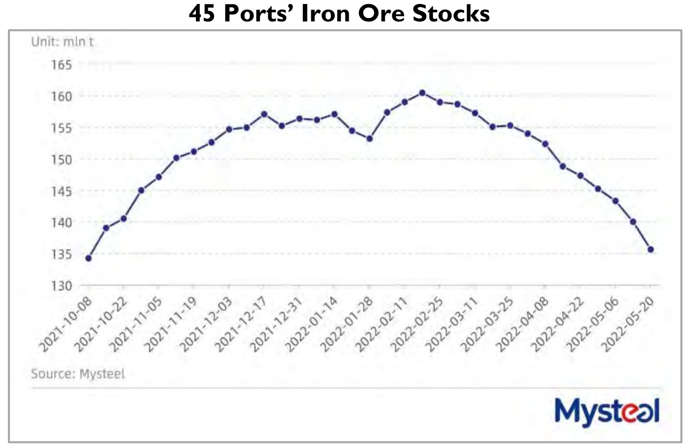
That MIR also discussed a meeting between Chinese regulators and their banks, to query how assets could be protected in the event of US sanctions, the short answer being, they couldn't. Markets got off to a good start this week, with Biden and Sullivan both saying that trade tariffs are actively under consideration as Yellen had discussed at the start of the month. Biden also answered a reporter's question saying that the US would defend Taiwan. This was rapidly followed up on by The White House, who clarified that the US would support Taiwan in defending itself via the supply of military equipment rather than military assistance. When combined with the announcement of the Indo-Pacific Economic Framework for Prosperity (IPEF), it is important to note that the thirteen member countries do not include Taiwan.

Chinese Foreign Minister, Wang Yi, is off to visit Fiji, the Solomon Islands, Papua New Guinea and Vanuatu to drum up support for a variety of projects, while Beijing has quickly responded to the IPEF, concerned about the US pushing for greater influence in the region and greater isolation of China, even though some members straddle the Regional Comprehensive Economic Partnership (RCEP) and/or the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Over the weekend, the Quad (US, Japan, India and Australia, with new PM Anthony Albanese), indicated a new announcement will be forthcoming for a joint maritime surveillance operation to counteract Chinese illegal fishing in the Indo-Pacific region. China's agreements with the Solomon Islands set alarm bells ringing and any additional island deals would be increasingly concerning so the timing of the IPEF is interesting.

While China has been suffering economically, their response to regional crises has been more muted than normal, providing a window for the US and particularly India to step in to provide assistance. Sri Lanka received a rapidly extended helping hand from Modi, which has not been lost on other Chinese debtors and members of the Belt Road Initiative (BRI). China has been more concerned with events at home of late and who can blame them.

Bloomberg recently asked the question as to whether China has enough food, regardless of their stockpiling, they still purchase about 60% of all soybeans and so the food crisis the MIR has been writing about, combined with inflation is a very real concern for the risk of social unrest. China just announced $1.5bn of subsidies for grain farmers according to the Ministry of Finance. The *WSJ* pointed out that "the entire high-yield Chinese property sector was trading as if it were in financial distress; 60% of the bonds of developers that haven't defaulted are trading at under 40 cents on the dollar (1)." The PBOC began the week with the largest Yuan adjustment since 2005, in a push for stabilization of the currency. And amid market chatter about the Politburo's pushback against Xi, his zero-Covid policy and its effect on global growth, Apple announced their intent to increase production outside of China. The European Chamber of Commerce in China remarked that members were again seriously considering their presence in the country on the back of the lockdowns, which saw Shanghai's April GDP at -61.5% Y/Y (2). Iron ore inventories at Chinese ports are at a seven-month low. How much more bad news can be priced in?

45 Ports' Iron Ore Stocks

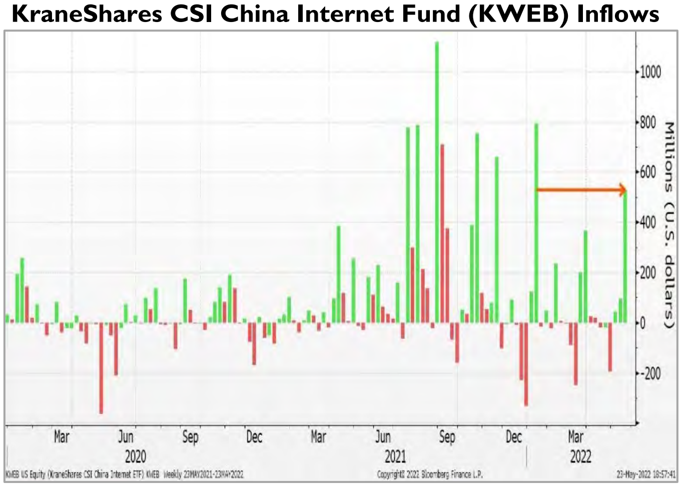


Source: https://www.mysteel.net/article/full-5030036/WEEKLY--China-iron-ore-port-stocks-dip-further-to-7-m-low.html

Tesla expects to see production return to normal in Shanghai this week. A State Council meeting chaired by Premier Li Keqiang has announced a variety of measures including tax rebates, increased loans to SMEs, increased numbers of domestic and international flights, tax cuts for new vehicle purchases, as well as unemployment benefits adjusted for inflation, all to try and stabilize both sentiment and the economy. An update from Maersk stated that Chinese disruptions will take months to clear even though certain ports, such as Ningbo, are now working normally.

Markets are forward looking, and even knowing it could be months before supply chains restore themselves to even their pre-Chinese lockdown levels, this could be a boost of good news the markets are craving with negative sentiment so prevalent. The Biden administration, with diesel and baby formula shortages, proving the most recent dent to their chances in the midterms, would have a shot at affecting some supply driven inflation with China coming back online. For China, Bloomberg now thinks this would be the first time since 1976 that Chinese growth underperforms that of the US. Notably, they also point out that should this hold, it will certainly have political ramifications.

KraneShares CSI China Internet Fund (KWEB) Inflows



Source: Bloomberg LP

The KraneShares CSI China Internet ETF (KWEB) took in its largest inflow since January last week, and that accounted for about half of all inflows to US listed emerging market ETFs. Foreign investors also closed out last week with the biggest inflow to Chinese equities this year. If the uncertainty surrounding China is too much risk to consider at the moment, perhaps the Singapore market is a better option. The Straits Times Index was one of the best performers this year before China pulled Asia lower and this year, Singapore will be chairing the CPTPP commission. Prime Minister Lee Hsien Loong is supportive of both US and Chinese supported trade pacts, preferring an approach of joint prosperity, allowing a more neutral approach which seems sensible given political uncertainties in both Beijing and Washington. "Lee said Singapore wants to "nurture" links with a range of countries including Japan "and maintain a balance so that we have resilience and we are not overly dependent on any single party (3)." Volatility is still a major factor for global markets, but end of month rebalancing as we head towards June could help steady the ship if the market believes that changes might be afoot in China.

The Straits Times Index (STI)

Source: Bloomberg LP

Sources:

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DJ Euro Stoxx 50—No Weighting

Courtesy: Bloomberg LP

Russia/Ukraine and China's Covid Policy

Two of the conundrums in the world today must include why China is locking itself down into a recession/political unrest and prolonging the worldwide supply chain problem. The second problem is the war of words over which side is winning in Ukraine, what Putin wants and how long the war lasts. Here are some new thoughts on these matters after considering the issues among our colleagues.

In China, the Covid policy has more to do with politics than public health. There is no question that with 180 million people over the age of 80, an ineffective vaccine and a population which relies in many cases on Eastern medicine, that the risk of a mass Covid death event, should the virus escape the cities, is possible. That would be a huge problem for the leadership and the CCP. Remember the CCP is organizing itself for the next five years and so far, the betting has been that Xi is a shoe-in.

We think it is possible Xi is not a shoe-in and that the lockdowns, while they may be a rehearsal for dealing with future economic sanctions (i.e., US sanctions on China), are meant to squelch political dissent and to exert greater control. The lockdowns started in Shanghai, which is where opposition exists. Locking down 26 million people for 8 weeks is not normal, nor given the track records lockdowns have, they are not great public policy. So, there must be another motivation. If it is political, the lockdowns could continue into November. Which markets are pricing that?

Regarding Russia, what Putin seems to want is to return to a powerful Imperial Russia. He is not interested in returning to a Soviet Union style country. He is at risk domestically as any leader running this war would be. Over the past twenty years, Russia was westernized to some extent, fortunes have been lost and now lives have been lost. The casualty figures which circulate in the West are much larger than those Russia offers. We believe the Western numbers are closer to the truth, as are the number of damaged/destroyed vehicles.

We have also noticed the obvious changes in Putin's physical appearance over the past year. My question is which Putin have we been seeing? Has he even been in public this year or last year or for that matter during Covid? Keeping visitors yards apart, which we have seen in the media photos, is not normal, even in the Covid era. Why?

What does he want? My guess is he wants Ukraine's agriculture industry and control of the ports. He can then sell Ukraine's grain to his customer, China. If this is the right line of thinking, half of Ukraine's grain production will be offline this year. If the remainder or a large portion of the grain harvest were to head to China, what will Western grain prices look like this autumn?

How long will the war last? 5-10 years if there is nothing dramatic which happens, that is the estimate of how long a stalemate could last. If something dramatic does happen, i.e., a major cyber attack is launched against the West or a small tactical nuke were used in Ukraine, a conclusion may be reached much sooner, but the damage will be much greater to the world economy.

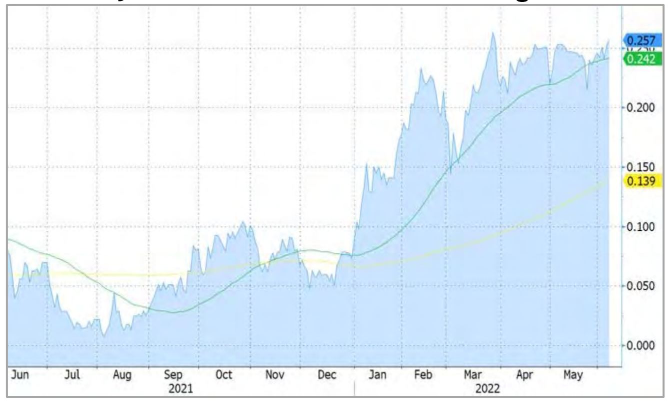
For the moment, Russian forces are re-grouping. They will be back, but in the meantime a respite for stocks and risk assets should unfold without a change in the major trend - which is for lower stocks.

Sources:
Bloomberg Data
Bloomberg News

DXY—Dollar Being Squeezed Higher

Courtesy of Bloomberg

JGB 10 Year Yields—12 Month Highs



Courtesy of Bloomberg

Fed Speak and Other Anomalies

The Fed has gone from talking about multiple rate hikes to when they might be able to look at easing - all before the rate hike season hits lift-off! I don't recall ever seeing this before. It tells me they are getting economic data which is alarmed them. That is a distinct possibility, as measures of the economy such as the Philly Fed Manufacturing and the Empire State manufacturing indicator have virtually collapsed. US corporate earnings revisions have turned negative, small business in the US expect economic conditions to worsen matching levels last seen in April, 2020 according the wsj.com. Gasoline in LA is over $7 a gallon and food prices are soaring. Chicken shortages are appearing in some Asian markets (i.e., Malaysia), while the fear of a ban on rice exports by some Asian countries is growing. Meanwhile in the UK, a 25% windfall tax on oil company profits will result in less investment, leading to higher prices down the road. This is being done to help the public pay heating bills which are too high and about to go higher. Other than helping in the very short term, does this not set up another inflationary burst in energy prices down the road?

Russia's central bank cut rates by 300 bps after the Dollar/Ruble touched 57, a gain of over 60% since the Ukraine war began. So now Russia is cutting rates, buying back their own debt at a discount and has blockaded 20 million of tonnes of wheat trying to leave Ukraine via the Black Sea.

An expert told the UN Security Council that the world has a 10-week supply of wheat. Nuclear power is being included in Europe's power plans. Romania will use an old coal power plant as the site of Europe's small nuclear reactor. Even California, where the anti-nuclear movement began in the US, is re-thinking the closure of its last remaining nuclear plants. Natural gas prices are above $9 in the US, the highest level since 2008.

Natural Gas (NG1)

Source: Bloomberg LP

The US economy is so financialized, so sensitive to rates and the government's debt levels, is it possible the Fed is finding even a minimal amount of intervention already done has incinerated trillions of Dollars in speculative investments in cryptos, non-earning tech companies, spacs, etc. and they are now concerned they have already gone too far? Or will they channel their inner Volcker and raise rates and do a QT, while the US enters a recession? And does the current administration have the conviction that the Carter/Reagan administrations did, that this was the right thing to do for the economy, even though it probably cost Carter a second Presidential term and Reagan's approval numbers plummeted as the 1982 mid-terms approached?

Is the US already in recession? Yes, I think it is, we have already had one quarter of negative GDP and I cannot see how given China's lockdown and the cost-of-living crises developing in the US and Europe, that Q2 and Q3 GDP readings in America are not negative. If the Fed blinks, then where do stocks bottom? More important the Dollar heads south and I would be a buyer of energy, EURUSD, agriculture and metals involved with EV production and/or Russian production which goes one way - to China.

Sources:
Bloomberg Data
Bloomberg News
Bloomberg NI TOP

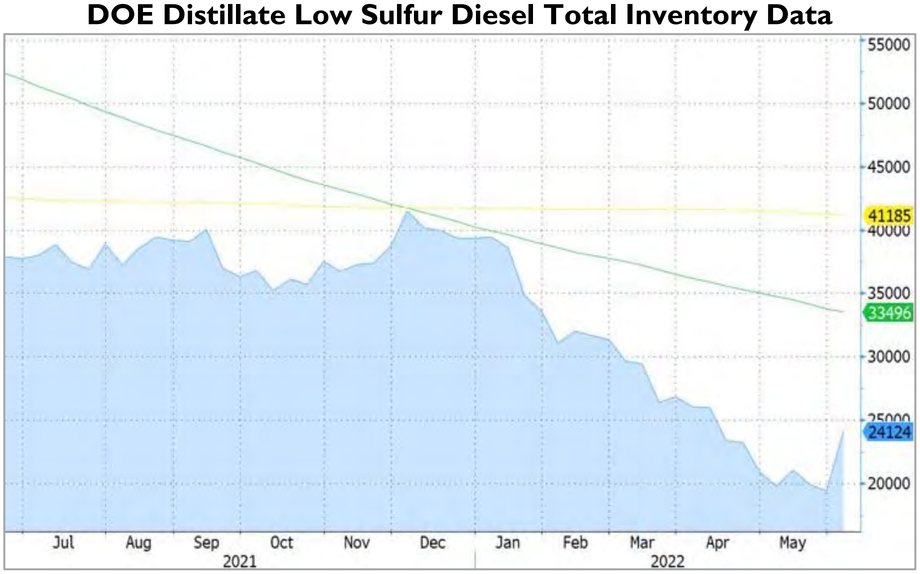
Crude Oil and the Transition - The Coming Price Spike

I was accused by one of my Canadian friends last year, of writing about crude oil every other day. For a time, I may have come close to achieving his observation, but it was worth it. Crude oil and energy stocks performed as expected and food prices are following crude oil/natural gas. What now?

The speeches being made on Tuesday at the World Economic Forum, regarding energy were highly informative. Fatih Birol from the IEA, who suggested in 2020 that oil production capacity should be increased, said yesterday he claimed just the opposite - as gasoline, ammonia, fertilizers etc., all hit new highs. Birol went on to explain that one of the reasons we have such high prices is the European heat wave - and I thought Europe had limited air conditioning.

Also at Davos, Norwegian Finance CFO Kjerstin Braathen said the energy transition will create energy shortages but the pain will be worth it. Whose pain? The pain coming from anti-fossil fuel policies and a lack of global energy cap-ex for 8 years has given us an oil market which is going up in spite of SPR dumps? The Biden administration has drained 40 million barrels from the SPR and WTI prices rose. Why are they draining the SPR while starting to talk to the Venezuelans? I believe there are two reasons. One reason is they may be preparing for a disengagement from importing Saudi oil. This would shorten US supply lines and avoid the problem of a sudden shortage if the Saudis decide to re-direct production elsewhere i.e., China. Longer term, I do think some oil producers in the Persian Gulf will accept payment in other instruments than Dollars for their oil. By shifting imports to Venezuela, the supply chain is shortened, Dollars are used as the medium of exchange and only one thing remains to be done. Refineries across the Gulf of Mexico will have to be converted to cracking heavy oil. They currently crack light sweet, in part due to the shale revolution. Putting some heavy oil in to the SPR makes sense, but watch for a refinery overhaul or two- at a time when crack spreads are off the charts and diesel inventories are very low.

DOE Distillate Low Sulfur Diesel Total Inventory Data



Source: Bloomberg LP

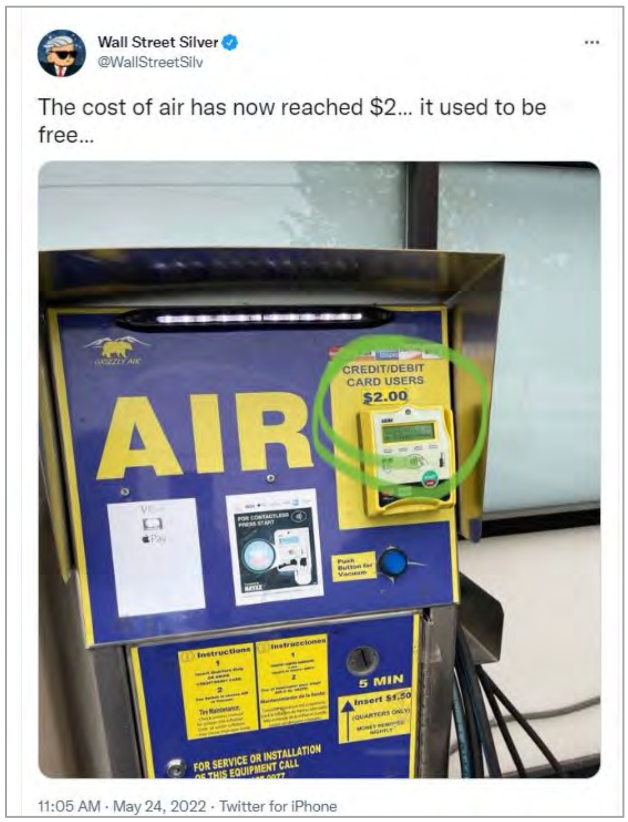
So, what's next for diesel? The US authorities are thinking of tapping diesel reserves to depress the price, just as they tapped the SPR to depress WTI. If they do, diesel prices will fly, just as WTI did. The cost of trucking goes up, freight goes up and the end cost to consumers goes up.

Food prices follow energy prices. I was looking at completion of wheat spring planting and this is not a good look in the US. According to the USDA/NASS, Minnesota plantings are only 11% complete vs. 90% average over the past twenty years. North Dakota is 27% complete vs. 80%. Nationwide completion rates are 49% vs. an 80% average. Some of these shortfalls, I believe are due to farmers being more careful about their use of expensive fertilizers- which will reduce crop yields.

There are signs overseas that energy prices are about to create the cracks in the system I have been writing about. Sri Lanka hiked petrol prices by about 22% and diesel prices by roughly 35%. The Sri Lankan government has told people to work from home - a sign of things to come in other lands. In Germany and in the UK, I do not see how natural gas prices do not crack the consumer as contracts roll off in the autumn. The coming shock to European markets and the European economy could be the trigger for a consumer-led recession.

Finally, what happens when China ends its lockdown policy and opens up? What then happens to the price of oil? Some of the Davos folks are suggesting buyers simply set a maximum price they will pay for oil. Price controls do not work, they have been tried before and if this is an idea adopted by some countries in the West, it will be the prelude to a wild west oil market. Oil is a buy on every dip.

If you think there is no inflation, take a look at this picture.



Source: https://twitter.com/WallStreetSilv/status/1529131478478635008

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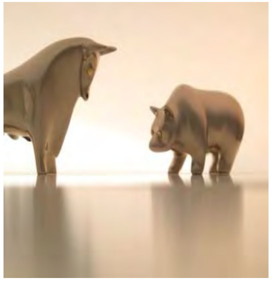
USDA/NSS



China: In a Transitional Period

The following article is written by Simon Hunt, who writes for TIS Group's Frontline China Report. If you are interested in articles similar to today's piece, please contact Larry Jeddeloh at tis@tisgroup.net

"They've said (US Administration) that China is America's number one enemy. If you're going to call a country your number one existential enemy, you're not going to be increasing your trade and mutual dependency with it." **Michael Hudson**, Economics Professor at University of Missouri-Kansas, 19th May 2022

China is tightening international production chains dependence on China to form a powerful countermeasure and deterrent capability against foreigners who would artificially cut off supply to China." President Xi Jinping

"In strategy, diagnosis precedes prescription of a solution. So, the proper diagnosis, I believe, is to recognize this as a classic Thucydidean rivalry, in which a genuine, rapidly rising power is in fact threatening a colossal ruling power." **Graham Allison**, American Political Scientist talking about US-China Relations, 10th March 2022

"…We can say there has been an overall decline in confidence in Chinese business in April. Since the BCI and its related indices look to the upcoming 6-month period, this means difficult times ahead. Comparing today with the situation over the past two years, we see the current situation is just as severe as that of March 2020, and GDP growth in the second quarter will reflect this." **Professor Li Wei**, Director of China Economy, Cheung Kong Graduate School (CKGSB), Beijing, May 2022

Summary

• China's economy has grown from nowhere 40 years ago to accounting for 17.4% of global GDP in 2020. The real question is whether she can regain the dominance that she had in AD 1000 when she accounted for 26% of global GDP.

• The difficulties are immense. Domestically, there is a leadership squabble even though Xi will probably be re-elected for a third term, his authority may be cut.

• The economy is in deep trouble not just from the lockdowns, but from disenchantment with policies that have been pursed over the last year or so. Business and household confidence has been shattered and will take months to recover despite the stimuli packages that are being unveiled almost on a daily basis.

• In contrast, China may have to continue experiencing rolling lockdowns into 2023 so causing impediments to economic recovery.

• Actual GDP probably won't exceed 2-3% this year and 3-4% in 2022.

• The external problems are magnifying. Weakening global business activity will impact exports; and relations with America, Europe and others are getting worse.

• A critical problem for Xi is the now obvious American containment policy and defense of Taiwan. Economic confrontation is clear-cut with a military one remaining a huge risk, one that could become an actual event in 2024.

• China will have to navigate the difficult international environment and the likely global asset crash over the next two to three years before embarking on real growth strategies. Until then the objective is just to stabilize the economy.

• China has the resources to recover: high savings, some 860 million having incomes below the national average, an enviable supply-chain infrastructure, the BRICS as an export base and gold reserves of over 40kt.

Introduction

China's difficult issues are both domestic and international. Monetary and fiscal policy must balance both; the former requires stimuli but the option for a fully-blown stimulus as carried out in 2020 would only create longer term problems; and the latter has to allow for relations with America to deteriorate with the risk that Washington takes measures to close down key seaway choke points.

China's support for Russia with its war against NATO being pursued over the lands of Ukraine has awakened long-held fears that America's real policy is to contain China's rise and influence internationally and to derail China's growth.

In seeing where China stands globally it is important to look back to where she has come from and the progress that the country has made over the last 40-years. Nothing like China's achievement has been recorded in history and probably never will be. Here are some of these signposts.

China Progress 1980-2020

Year	World Population	of which Poverty %	GDP $	% World	Exports $	%
1980	981 bn	88%	191 bn	0.17%	11.3 bn	0.5%
1990	1.14 tr	70	361 bn	1.6	49.1 bn	1.4
2000	1.26 tr	50	1.21 tr	3.6	253.1 bn	3.2
2010	1.34 tr	17	6.09 tr	9.2	1.65 tr	8.6
2020	1.41 tr	0	14.72 tr	17.4	2.72 tr	12.1

Source: World Bank

The question is what comes next? Will China be able to recapture what history tells us is that the country was the center of the universe as records back to AD 1000 show. The data shown below is taken from Angus Maddison's history AD1000 to 2000; and 2020 to World Bank's data series.

USA & China % of Global GDP AD 1000 to 2020

	USA	China
AD 1000	0.06%	26.0%
1500	0.03	25.0
1700	0.01	22.0
1900	1.09	11.0
1913	18.9	9.0
1938	17.8	6.4
1960	24.3	5.2
1980	21.1	5.2
1990	21.4	7.8
1995	21.4	11.2
2000	21.9	11.7
2010	22.5	16.6
2020	24.7	17.4

Some institutions such as the IMF and the CIA Factbook consider that PPP is a more accurate assessment of a country's GDP. On this basis China's economy surpassed America's in 2017 and by 2020 China's GDP had reached $24.273 trillion and USA's $20.937 trillion according to the IMF.

Using nominal GDP data and assuming that China's economy's trend growth will be 4% a year to 2040 (versus average growth of 8.7% a year since 2000) and America's 1.6% up to 2030 and thereafter 2% a

year (average growth last 20 years was 1.6%), the crossover year should be 2037 when China's GDP would be $28.7 trillion and America's $28.5 trillion.

The above are trend growth rate profiles, but how does China move from today's difficult period to achieving the country's growth potential.

The Main Issues

The domestic and international issues are inter-linked because China's leadership is preparing for difficult relations with America and for a forecast global crash of asset values somewhere in the mid-2020s. This means that reflating the economy from its current problems will have to be cautious as government does not want to spend all its reflation tools now as it will need to keep the big guns until the world economy crashes.

International Issues

Biden's signing into law the new Act on 27th December 2021 signaled a new tougher policy to contain China than was spoken about before. The Act effectively seeks to militarize countries surrounding China including Taiwan so as to contain China's growth and influence. The current meetings in Tokyo are part and parcel of this new policy.

Today (Monday 23rd May) Biden went one step further by saying that should China invade Taiwan America would use its military to support Taiwan (it's a commitment we made, he said). Biden has also launched the Indo-Pacific Economic Forum which is designed to deepen America's cooperation with countries in the region covering subjects such as supply chains, digital trade and clean energy.

These are steps which Beijing has long known would be surfacing. They understood that the war over Ukraine is NATO's attempt not just to contain Russia's influence across Europe but to so weaken its economy that the country can be readily absorbed into the Western Alliance.

China's leadership sees America's actions to reduce Russia's global influence as a prelude to what Washington means to do to China. America is trying to weaken both Russia and China so that they can become subservient to Washington's dictates.

However, these policies stem from a fear that Russia and China will create a new trade and currency platform - which is advanced – that would exclude the US dollar and therefore if successful would create a group of countries stretching across central Asia, the Middle East, Africa and even into S America which would prefer to deal with this New Platform rather than within the dollar's western alliance structure. If this platform succeeded, roughly half of the world would be trading without the US dollar implying the end of America's 77 years of hegemony.

The train, as it were, has left the station bound for the New Trading & Currency Platform. There will be many red signals before the train reaches its station but despite the obstacles it will get there, by 2025 in our view.

One reason is that Russian and China have been planning this New World since the SCO was founded in June 2001, followed by BRICS in June 2006 and the Eurasian Economic Union in May 2014. The new trading and currency platform is the product of years of planning.

Domestic Issues

The leadership has many challenges to overcome to ensure that growth will continue to outpace the world, some of these are discussed below.

• The lockdowns have brought growth to an abrupt halt. There are two reasons why the leadership has chosen a covid-zero path. First, the elderly or those over 65 years number some 160 million. Should the virus hit many of them they would overwhelm the health facilities given that the Chinese vaccinations have only 25% of the strength of those in the west.

• Second, Chinese goods are embodied in nearly all global supply chains. Without these goods and components global industries slowly grind to a halt as they are unable to find alternative supplies at short notice. As Xi Jinping has said, 'China is tightening international production chains.' Lockdowns are a way of showing to Washington, Brussels etc. how much their countries depend on China.

• In effect, the lockdowns have a greater political context than an economic one. The economic pain can be righted by skillful management but the political outcome has wide implications both internationally and domestically.

• Domestically, lockdowns are one of the centers of the rumored leadership struggle between President Xi and younger members of the China Youth League, which the president has always abhorred.

• Xi's policies are to switch the focus on growth from the coastal cities to the central and western provinces where most of the households have incomes below the national average.

• The China Youth league incumbents want growth to remain based on coastal cities (the Shanghai clique). These 6 coastal cities account for 49% of the country's GDP whereas the 15 poorer ones' account for just 21% of the country's GDP.

• The dispute between the two cliques is also over property. The president wants to pursue policies that make housing affordable to all under his 'Common Prosperity' plan and to reduce the debt held by private sector developers. By doing so his policy will break the incestuous ties between the developers and local governments, as both sides have been in each other's pockets, as it were.

• The longer-term strategy is for central government to provide the purse strings for local governments by seeing that most revenues accrue to central government who then parcel out funds to local governments. The process probably includes a thinning out of local government bureaucracy over time.

• Thus, the lockdowns are more to do with the politics of the country and partly internationally rather than the economy. Lockdowns give the president the means to tighten control over large sections of the population; they weaken those sections which have gained huge wealth over the last 40 years which has weakened the structure of the CCP; and they have helped to create the tools for a leveler of the playing field or Common Prosperity.

• The substance of the policy dispute between the two factions is that the President is focusing on creating the platform for Common Prosperity and the establishment of the new International Trading and Currency platform whilst the State Council led by the China Youth League members want to focus on the domestic economy.

• Despite President Xi's rather clumsy 'old-style Maoist behavior', he will probably be re-elected since he has the support of the PLA, the security forces, nearly all of the country's 540 million rural population as well as the 190 million who have left the rural areas for the urban community since 2005. What may emerge is that Xi's victory could be less comprehensive than seemed likely a year ago thus increasing his need to seek compromises.

• Finally, there is talk that Xi may have just had a minor stroke and that the level of dissension is starting to fracture the Party. Dissension at the top of the leadership does not provide a solid foundation for sound economic policy making.

• In summary, for all of these reasons a series of rolling lockdowns may well be experienced into 2023 for political reasons and because of variants of covid which could well surface during the usual flu season.

• The Economy is in deep trouble which just a few numbers illustrate. Excavator domestic sales, a solid indicator of construction activity fell by 61% in April YOY with Caterpillar saying that they expect sales in China to be below 2019 levels this year. Auto sales despite strong growth in EVs fell by 48% in April YOY but by 12% in Jan-April months YOY.

• Household and business confidence has been shot to ribbons; households are saving rather than spending and businesses are 'running away' as one friend said to us. It will take months for confidence to return despite the new measures introduced to stimulate the economy.

• China's economy is like a tanker; it takes time to change direction. We don't think that real GDP (as opposed to reported GDP) will exceed 2-3% this year and 3-4% next year.

• Lockdowns together with a renewed thrust towards state ownership are resulting in a heavy exodus of expat business people and bankers from the mainland and Hong Kong to Singapore, Dubai and other parts of the world. The exodus includes also foreign trained Chinese. In effect, this is a brain drain of large proportions.

• China has been preparing for a growing Washington centralized world for many years. The central policy is one based on greater self-reliance which means to distance the country's imports and investments out of the western alliance countries and to reinvest in those countries which share China's international objectives based on a multilateral world without any one country dominating the universe. The policy includes liquidating asset and portfolio investments in western alliance countries.

• The self-reliance policy also means stockpiling those imports on which the economy depends whether agriculture or commodities or technological products. The policy includes investing and building industries domestically and locating imports more in countries within Asia and in S America such as Argentina, Brazil, Chile and Peru.

• Food is an intrinsic part of self-reliance as the leadership must be able to feed its population.

• China's difficulty is the lack of arable land compared with the size of its population. For instance, China fed 19% of the world's population with only 8.5% of the world's arable land last year. To tackle this issue, the leadership controls the net amount of arable land that can be converted for other use maintaining at least 307 million arable acres in 2020.

• Arable land is being increased by demolishing family houses and relocating households into modern apartment blocks so releasing new land for farming. There are some 900,000 villages in rural China which gives some idea some idea of how much new arable land has been created: half an acre per village?

• Agriculture production has risen by an average of 7.2% a year since 2010 to RMB 7.175 trillion in 2020. However, with the decades' of focusing on manufacturing, agriculture as a percent of GDP has fallen from 34.8% in 1970 to a derisory 7.7% in 2020, though better than the low point of 7% in 2018.

• There is a new focus on expanding grain harvests through technology and scientific innovation such as by providing assistance to key seed breeding programs and expediting major biotech breeding projects.

• Imports have been a major contributor to China's food supplies growing from $610 million in 2010 to $4 trillion ten years later.

• Should China's agriculture share of GDP reach what it was in 2000 by 2030 and given that China's 4% trend growth should give us a GDP of $21.8 trillion in 2030 then agriculture production would rise to $3.27 trillion compared with 2020's $1.1 trillion.

Recovery

• The next few years will be difficult for China's leadership to navigate the economy through the treacherous international waters: not just the American containment policies but the expected global asset market collapse and resultant depression in the mid-2020s.

• Moreover, it takes a year or so for a new government to bed-down especially if Xi's powers will be contained.

• There are five powerful forces that will ensure that China overcomes its transitory difficulties. First it has a vision to be the center of the universe as it once was. 40 years ago, the then leadership had their vision of where China's economy would be and set out plans to achieve that objective which was to bring poverty down to zero.

• Second, households have huge savings last year totaling $3.7 trillion rising to $6.2 trillion by 2030 (Global Demographics). The country's gross domestic savings was 45.2% of GDP in 2020 (same as in 2019) according to the World Bank giving a likely savings of $6.9 trillion last year.

• Third, there are about 860 million with average disposable incomes below the national average which was RMB 35,128 or $5400 last year. Per capita income doubled in the last decade; it will do so again.

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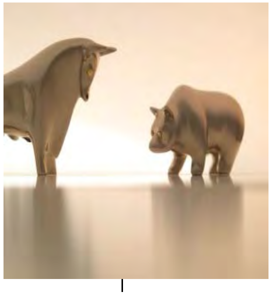


European Outlook – June 2022

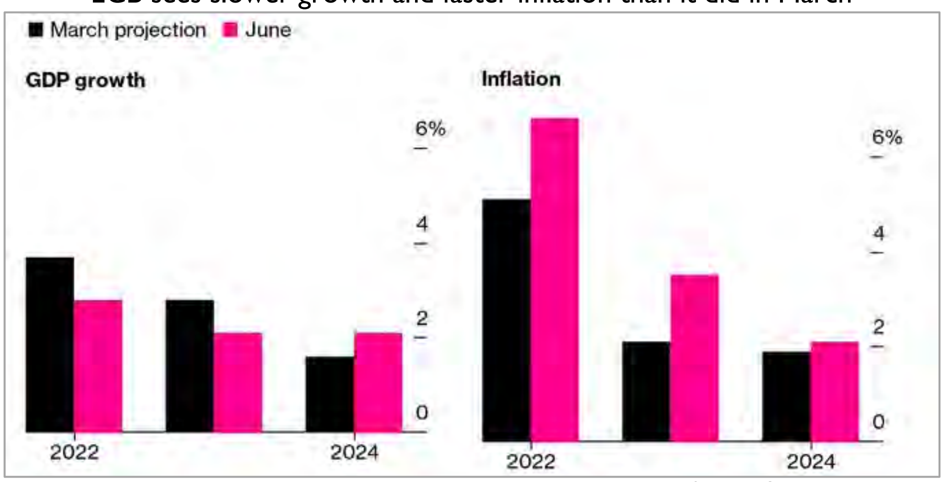
The ECB

The ECB announced that a 25bp hike is incoming for July, with the potential for a larger rate hike in September. Market focus and the ensuing reaction was more based on the concern for peripheral spreads and what that might mean for fragmentation not only for the Eurozone but for the Euro itself. For now, the focus is on defeating inflation which has gotten out of hand, having been dismissed as transitory for too long before the impact of Russia / Ukraine and the longer-term supply constraints associated with the war, further impacted the inflation scenario.

The rising possibility of renewed asset purchases to quell any peripheral stress will not sit well with the hawkish members of the ECB. And following the other central banks (e.g., BoC & RBA) who voted for a 50bps hike, the ECB is still seen as treading too carefully to calm inflation as staff projections finally forecast medium-term inflation above the 2% target.

Bad Mix

ECB sees slower growth and faster inflation than it did in March



Source: ECB & Bloomberg

Bloomberg expects the hiking cycle to top out close to 1.5%, yet the slow stepping forward with a 25bps hike (which would be the first since 2011) has raised additional questions about whether the Euro-area economies can handle a much higher rate path without further stalling an already slowing economy. It would require a consensus effort across Europe, likely with fiscal aid in tow, and collectively that only happens when pressured by immediate danger. Market expectations for ECB rates have at least 130bps of tightening expected before 2023 kicks in, but the concern for the effect felt by the peripheral nations has led to Lagarde remaining non-committal beyond a couple of months from here. That lack of foresight has the market concerned for this reactionary nature from a major central bank. According to the ECB's main hawk, Holzmann, "if the situation doesn't change or deteriorates, then in September a bigger step will be implemented." This wait and see attitude is keeping the € under pressure, already down more than 8% against the Dollar this year. This ambiguity was addressed by former ECB chief economist Peter Praet, who criticized Lagarde for blogging about a less aggressive path of rate hikes just a couple of weeks ago before her U-turn at the ECB meeting.

The periphery is also under threat from rate hikes that must be implemented in the face of inflation, knowing that supply driven inflation is hard to counteract solely with monetary policy. Italian Finance Minister Daniele Franco agrees with Draghi regarding the predicament facing Italian bond yields. "(Rate)

Increases per se do not affect very much the macroeconomic scenario." This has pushed rates back towards the 250bps line in the sand against the German benchmark, but as this outlook has previously shown via the chart below, the cat might already be out of the bag.

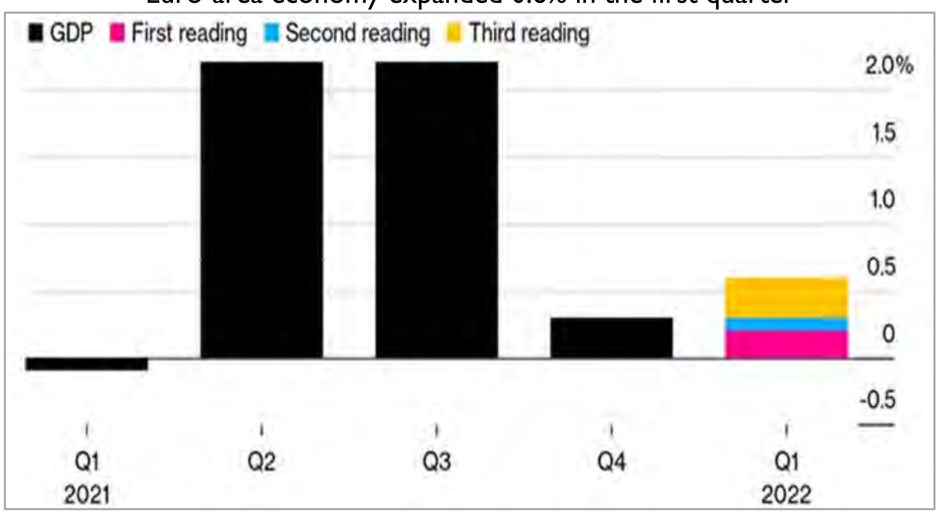
Italian BTP – German Bund 10-Year Yield Spread

Source: Bloomberg Finance LP

The Eurozone

Better Than Expected

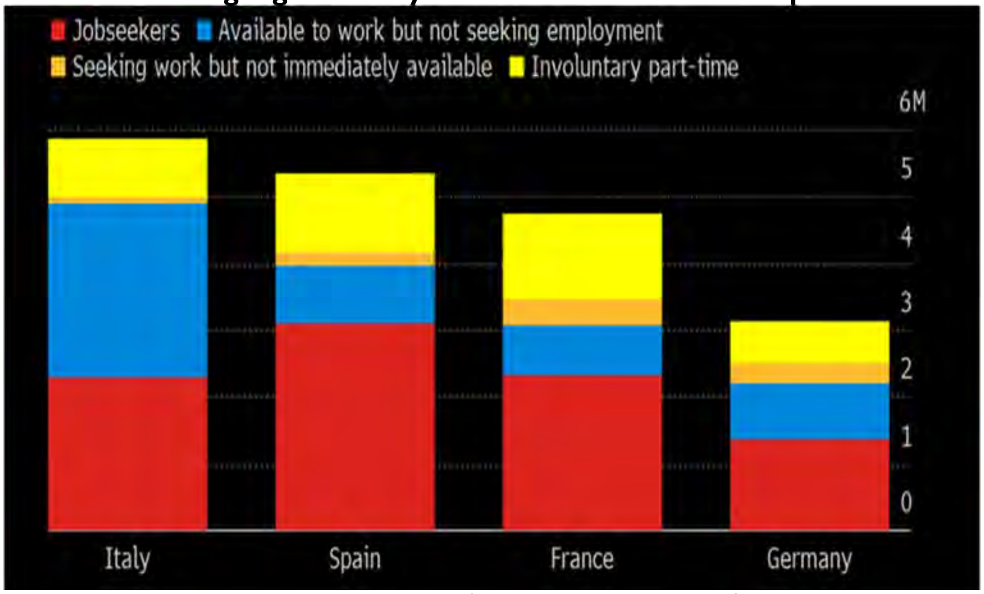
Euro-area economy expanded 0.6% in the first quarter



Sources: Eurostat & Bloomberg

Italian industrial production increased by 1.6% in April, the third consecutive positive month and well above the expectation of -1.1%. However, the Bank of Italy now forecasts 2022 growth at 2.6%, revised down from 3.8%. The warning was also provided that should energy supplies be cut off by Russia, GDP would slow further and contract by at least 1% next year. The Italian central bank is also concerned by the labor situation, regardless of the trend lower in the unemployment rate from 13.2% in 2014, the rate is still stubbornly high at 8.4%, with youth unemployment at 23.8%. Bank of Italy Governor Ignazio Visco is most concerned by the data that shows 2.62 million people are available for employment but are not actively seeking work. Italian 10-years are at 4.16% as I write and the FTSEMIB is down 20% YTD. Russian oil imports are now running at a 30-month high and so Draghi continues to scour the region for relationships to help alleviate dependence on Russia. This time around, it's Israel that could provide natural gas and hydrogen, but again these projects take time, putting Italy and the EU under continual headline risk.

Visco Highlighted Very Low Labor-market Participation



Source: Eurostat data, Bloomberg Calculations, Bloomberg

France is in discussions with the UAE about energy supplies, as Finance Minister Bruno Le Maire still maintains that the French economy will experience positive growth this year regardless of inflation and the additional issues associated with Ukraine. Macron is pushing for pension reform as his majority in parliament is now at risk, which would affect his ability to lower taxes while facing a push for more referendums and the threat of a financial transaction tax from Jean-Luc Melenchon's left-wing alliance. Contrary to the Italian data, French industrial production has now declined for the third consecutive month.

Asides from industrial production, most French data has arrived in line with expectations. Unfortunately, the same cannot be said for Germany. Factory orders reported a third straight drop, retail sales were -5.4% m/m (versus -0.5% expected), services and composite PMI were both a point below forecasts and industrial production was +0.7% (against a 1.2% expectation). Consumer sentiment is a growing concern with public broadcaster ARD noting that 47% of those polled are strongly or very strongly cutting back on spending. That number rises to over 75% for low-income households adding yet more pressure to Scholz's coalition. Accordingly, the minimum wage has been raised to €12 from October 1st, with the aim of directly benefitting over six million people, mostly women and those from the eastern states. German Finance Minister Christian Lindner has proposed a bill to make it easier for employees to hold stakes in the companies they work for. "Improved employee share ownership will also help us to attract skilled workers more easily, who have previously found even better conditions in other countries. We have to reduce the bureaucracy involved in employee equity participation and make it easier for both companies and employees."

According to the European Commission's monthly survey, consumer inflation expectations are declining. Energy and supply side inflation remain the dilemma that central bankers admit can only be partially influenced by monetary policy. Inflation, when considering the chart below does not support the European Commission's findings and the impact upon German consumers is a worry for the core-EU, especially if that sentiment increasingly spreads to the rest of the Euro-area. Lawmakers have now rejected plans to identify gas and nuclear as green energies, confirming that the risk lies with not fully making the transition to renewables before a further supply side shock takes hold. It seems that the EU's plans will not be swayed even in the face of rising inflation and the risks associated with the Russia / Ukraine war. "The EU has the chance to take the global lead in the fight against climate change and set the gold standard for investment in the climate neutral economy. We need massive investment in the expansion of renewable energies, not the energies of the past."

Europe's Inflation Shock Dwarfs the Rest of the World

Surprise indexes show that the Eurozone was blindsided by rising prices

Source: Bloomberg

High income stocks are back in favor given the stagflationary environment, but the credit markets are at critical levels that should push equity volatility higher should they be maintained.

European High-dividends vs. MSCI Europe

Source: Bloomberg Finance LP

Equity Volatility vs. Corporate Spreads

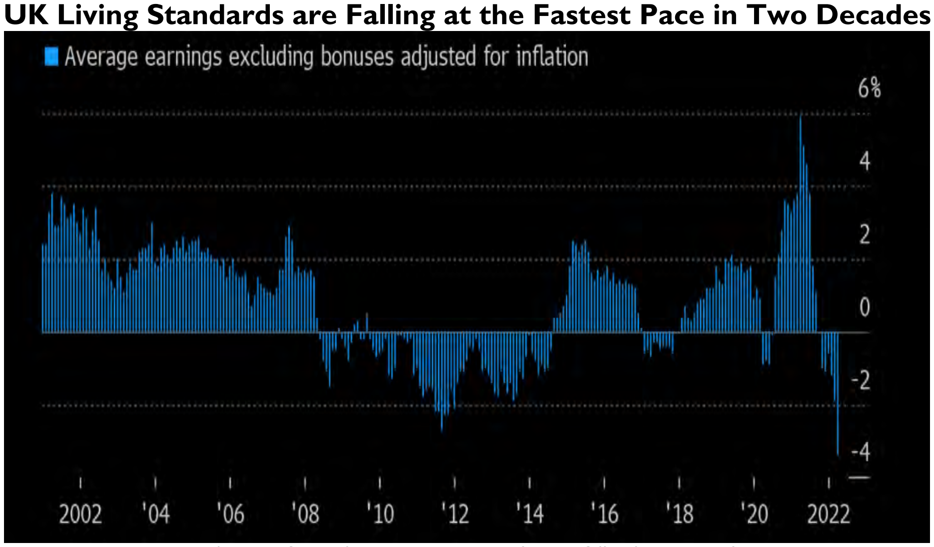
Source: Bloomberg Finance LP

The UK

This outlook is being written just before the BoE meeting and while the markets have priced 125bps of hiking by September, surveyed economists see the scenario slightly differently. Markets have priced two 50bps hikes and one 25bps hike over the next three meetings, with any 50bps move marking the biggest increase since before the BoE achieved independence in 1997. Economists polled by Bloomberg have raised the level where they foresee the bank potentially pausing from 1.5% to 2% as of this time next year. The market implied rate is 3.40% a year from now.

The cost of living crisis continues with Boris Johnson now focused on reforming the UK housing market and tariffs on food imports following his narrow victory with the leadership vote. "Over the next few weeks, the government will be setting out reforms to help people cut costs in every area of household expenditure, from food to energy to childcare to transport and housing." Meanwhile, Chancellor of the Exchequer, Rishi Sunak, has promised to cut taxes in the next budget, in an effort to drive economic growth and corporate productivity. Johnson's political capital has suffered as his leadership was questioned, with the problem being that the alternatives were not being viewed favorably either. A growth slowdown amid rising rates and a lack of political confidence are playing havoc with Sterling which is already on the backfoot due to the strength in the Dollar. Then FTSE had been holding on to positive gains for the year, given the index weightings for components that favored the energy and materials sectors, but those gains have since flipped to red for the year to date. A windfall tax on energy firms which was vehemently opposed by the PM just two weeks before a U-turn was enacted has contributed to both the political disharmony within his own party and the slowing performance of the FTSE as some of the key contributors will now be paying more of their profits to the UK government. Political volatility remains high, and the press are advocating that Johnson's days are numbered. As we have seen many times before, when the UK press gets their claws into someone, they rarely let go.

UK Living Standards are Falling at the Fastest Pace in Two Decades



Note: Nominal earnings deflated by CPIH inflation index Source: Office for National Statistics, Bloomberg

One of the other cornerstones of the UK economy, housing, has been expected to decline in the face of rising rates for quite some time, but now a report from the Royal Institution of Chartered Surveyors (RICS) suggests that time may have finally arrived. Demand declined for the first time since August as respondents forecast sales volumes to drop over the next year with living costs continuing to rise. The RICS survey also reported a third consecutive decline for those expecting higher house prices a year from now. Moody's expects financial distress could affect almost 13% of UK mortgage borrowers should high-single-digit inflation continue next year. The British Chamber of Commerce (BCC) now expects the economy to stagnate in Q2 and Q3 before contracting during Q4. The calls for a recession in the UK continue to swell, with the question being whether Europe is delayed in following in those footsteps.

GBPUSD – Monthly

Source: Bloomberg Finance LP

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USD/Canadian Dollar Spot (GPF)

Courtesy of Bloomberg LP

DXY

Courtesy of Bloomberg LP

THE CAD CORRELATES TO COMMODITIES — AND A BULL MARKET IS UNDERWAY

CANADA DATA

	Rate of Change	as of
REAL GDP YoY	3.50%	3/31/2022
PPI YoY	16.41%	4/30/2022
CPI YoY / Inflation	6.80%	4/30/2022
Unemployment	5.20%	4/30/2022
M1 YoY	11.69%	3/31/2022
M3 YoY	8.50%	3/31/2022
Overnight Lending Rate	1.50%	6/8/2022

Comparative Data to Other Major Currencies

Country	3 Mo Int Rates	10 yr Int Rates	Real Short Rates (Using 3-mo rates less CPI)	Real Long Rates (Using 10-Yr Govt Bonds less CPI)
Australia	1.17%	3.55%	-3.93%	-1.55%
Canada	1.68%	3.27%	-5.12%	-3.53%
Euro	-0.55%	1.35%	-8.65%	-6.75%
Japan	-0.09%	0.25%	-2.59%	-2.25%
Switzerland	-0.75%	1.051%	-3.65%	-1.85%
US	1.24%	3.02%	-7.06%	-5.28%
UK	1.71%	2.25%	-7.30%	-6.75%

Country	GDP	CPI	PPI	Unemployment
Australia	3.30%	5.10%	4.90%	4.03%
Canada	3.50%	6.80%	16.41%	5.20%
Euro	5.40%	8.10%	19.30%	6.80%
France	4.50%	5.20%	27.80%	7.10%
Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

MONETARY/ECONOMIC FACTORS

- Canada's money supply is +8.5% (broad money) and +15.2% on a y-o-y basis.
- Monetary easing is over. The BOC is hiking rates as is the Fed. The interest rate cycle has changed to tightening, which should help strengthen the C-Dollar.
- Canada's energy industry has been under severe pressure. The future of the energy sector should be bullish as it represents a key national asset in Western Canada. A re-balancing of global supply / demand due to cap-ex shortages and sanctions have started a new bull market in oil, which should continue to strengthen the C-Dollar over time. However, the Canadian government is pushing for banks to reduce their funding of the fossil fund industry. This will drive energy companies to seek higher cost capital. In turn, oil/gas prices must rise and remain at a relatively high level to fund cap-ex. Without significant additional cap-ex, oil prices will remain in bull market.
- The "new NAFTA" agreement should boost Canada's economy, unless another key trading partner, i.e., China, continues to have political/legal/economic problems with Canada, offsetting the benefits of the new NAFTA.
- China's PMIs have weakened but Beijing is now saying June may be the economic bottom and the Yuan does not need to devalue further.
- Economic recovery in the US and China are key to Canada's economy. Xi's common prosperity theme, if well executed, will create significant new demand from middle class Chinese consumers and an emerging middle class. But to whom will China be allowed to sell their goods, if sanctions spread? And to whom will the Chinese sell their goods if their ports remained clogged – or closed? And what happens if the current course of China's Covid policy and relationship to Russia changes?
- If Chinese capital, which is big in Vancouver and Toronto, were to leave Canada, the property markets will take a hit, unless there is another round of people leaving Hong Kong – which seems to be underway.
- The currency markets are weighing factors beyond yield differentials. Creditor vs. debtor countries, commodity markets exposure (positive if a commodity producer), fiscal management, QEs or no QEs, trade relationships and asset diversification seem to be additional determining factors. Credit ratings also play a role. The CAD could trade much stronger than expected if the global economy reflates in 2022-2023 and commodity prices continue to rise.
- Canada has concluded a trade pact with the EU, which should boost economic growth over the long term once a lack of cap-ex and supply disruptions end.

POLITICS

C-Dollar should begin to price a long commodity bull market.

WHAT THE CENTRAL BANK/ GOVERNMENT WANT

A rising C-Dollar helps the inflation outlook. The BOC also seems intent on raising interest rates which is supportive.

TARGETS

China/US demand for Canadian exports and the price of gold/commodities, are the principal factors affecting the C-Dollar. Gold, oil and some base metals are in major bull markets – which correlates well to a stronger CAD over the long term. Near term, the CAD is all about the Chinese economy, commodity prices, the US economy and the world economy avoiding another lockdown/recession. If commodities remain in a bull market, that would be very positive for the CAD. The Canadian Dollar should strengthen, over time as commodity prices firm due to years of cap-ex which was too low.

Sources:
Bank of Canada
Bloomberg

Euro vs. Dollar—Long Term Support is 0.82

Courtesy of Bloomberg LP

DXY

Courtesy of Bloomberg LP

EURO: DOLLAR — EURO/DOLLAR WEAKNESS — CLOSE TO THE EDGE

EURO DATA

	Rate of Change	as of
REAL GDP YoY	5.40%	3/31/2022
PPI YoY (changed to OECD)	19.30%	4/30/2022
CPI YoY / Inflation	8.10%	5/31/2022
Unemployment	6.80%	4/30/2022
M1 YoY	8.50%	4/30/2022
M3 YoY	6.00%	4/30/2022
Overnight Lending Rate	0.00%	4/14/2022

Comparative Data to Other Major Currencies

Country	3 Mo Int Rates	10 yr Int Rates	Real Short Rates (Using 3-mo rates less CPI)	Real Long Rates (Using 10-Yr Govt Bonds less CPI)
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Japan	-0.09%	0.25%	-2.59%	-2.25%
Switzerland	-0.75%	1.051%	-3.65%	-1.85%
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UK	1.71%	2.25%	-0.20%	-6.75%

Country	GDP	CPI	PPI	Unemploy-ment
Australia	3.30%	5.10%	4.90%	4.03%
Canada	3.50%	6.80%	16.41%	5.20%
Euro	5.40%	8.10%	19.30%	6.80%
France	4.50%	5.20%	27.80%	7.10%
Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

MONETARY/ECONOMIC FACTORS

A significant current account surplus remains across the EU, giving the currency an upside bias. That CA surplus will continue to be affected by the level of the Euro – which has trended lower in recent months.

Meanwhile, the ECB's monetary intervention of recent years, created a severe mispricing of EU bond market risk. Negative yields for ten years in Japan tended to correlate to a stronger Yen. Will negative rates which are almost gone in the EU eventually have the same outcome for the Euro? Or will Europe be able to maintain a relatively weak currency despite a trade surplus and interest rates which have moved higher with speed and rate hikes on the way?

Germany's 8% trade surplus is not sustainable in an era where the US is, for the first time in years, addressing the global terms of trade. A "low" Euro has been instrumental for German exports, especially autos. It is the Euro / RMB cross rate which is crucial to Germany now along with the price of Russian supplied natural gas. Germany needs a new export market – China fits that bill, but for how long given the emerging global situation?

The global transition from combustion engine vehicles to EVs will be a major long-term issue for Germany's economy as well as from where Germany acquires its energy. Large scale fiscal spending married to monetary easing will be needed to bridge what may be a prolonged period of economic dislocation before German industry can find its long-term footing producing EVs and exporting to Central Asia / China.

2022 could be a very interesting year for Europe's economy and for the Euro, as the EU and the ECB are at a crossroads on multiple issues. Meanwhile, China is looking to increase trade ties with Europe, which may turn out to be Europe's economic salvation from a demand standpoint. Or will the Russia-China partnership force Germany to change course on trade and basically blackball Russia and China? Europe's energy dependence on external sources, particularly Russian natural gas is a major ongoing risk. The EU is likely to begin importing LNG from Qatar, Mozambique and the US – at a higher cost than Russian gas, adding to potential Euro Dollar lows. Economic sanctions, the war in Ukraine, Germany's sudden re-armament have all contributed to recent Euro weakness. None of those trends should change in the near term, the ECB is however changing to positive nominal yields.

WHAT THE GOVERNMENTS / CENTRAL BANKS WANT

Stability and lower inflation – Europe will have neither in the near term suggesting the Euro could go lower against the Dollar, however a lot of work has already been done on the downside. The EU and Germany in particular, is happy with a structurally weak Euro. Below 1.08, what level is too weak?

TARGETS

The US will eventually need a higher Euro / lower Dollar while Europe is almost always happy with a weak Euro. Near term, Euro / Dollar should continue to rally from an oversold position. If it does not bounce off the 1.08 level, the USD could go lower very quickly.

Source: Bloomberg

Japanese Yen vs. Dollar

Courtesy of Bloomberg LP

DXY

Courtesy of Bloomberg LP

YEN/DOLLAR HEADED FOR 144?

JAPAN DATA

	Rate of Change	as of
REAL GDP YoY	0.40%	3/31/2022
PPI YoY	9.50%	4/30/2022
CPI YoY / inflation	2.50%	4/30/2022
Unemployment	2.50%	4/30/2022
M1 YoY	6.10%	4/30/2022
M3 YoY	3.20%	4/30/2022
Overnight Lending Rate	-0.05%	6/7/2022
Japan Merchandise Trade Exports	12.50%	4/30/2022
Japan Indices of Industrial	-4.80%	4/30/2022
Jap Tankan Bus ond Large Ent	14.00%	3/31/2022

Comparative Data to Other Major Currencies

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Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

MONETARY FACTORS

- A rapidly declining Yen may well relate to the BOJ printing of funds to buy government bonds. In addition, Japan has been selling US Treasuries. Were these funds used to purchase JGBs and hold the 10-year JGB peg?
- Monetary policy looks steady. Meanwhile, the new PM, Kishida is beginning to acquaint the markets with his plans.
- Japan may be in the early stages of fundamentally shifting its national security strategy. The polls find the public supports putting nuclear weapons in country.
- Japan owns a lot of risk assets in the US, i.e., CLOs, high yield bonds and US stocks. Large-scale repatriation would cause a Yen spike which a bond market sell-off might trigger. Japan's GPIF had a very good year in 2020, rising about 25%. 2022 could be more difficult.
- The BOJ forced a major change in global monetary policies via their rapid depreciation of the Yen from 2013-2015, by employing negative rates. It took several years and a 35% Yen devaluation just to stabilize Japanese exports in the 2012-2020 period. With a trade surplus and Chinese demand rising, the BOJ's challenge is to keep the Yen from strengthening further.
- If a major financial crisis develops, Japanese investors are likely to return capital to Japan by selling foreign assets giving the Yen a big boost. After the Yen's recent decline, a rebound of some magnitude would not surprise.
- Asset allocation shifts by corporate / government pension funds (especially GPIF) will move additional funds toward equities. More Japanese pension funds, public and private, are joining the move toward larger equity allocations, as the government pushes local companies to improve returns, governance and transparency. Japan's foreign holdings performed well last year. If the money is repatriated, the BOJ could have a Yen related capital flow problem.
- The rate of growth in the broad money supply is +3.2% on a Y-o-Y basis, a fraction. Narrow money supply is +6.1% Y-o-Y. The BOJ coupled with lower corporate tax rates and a government-driven shift by pension funds into equities, pension fund allocations will, in the long term, move in favor of equities. Japan's equity market has nearly recovered to the highs of 1990. If a new high in the TOPIX is reached, who will sell it, as who among large scale investors are likely to have a loss? This is a key question for global capital flows. Is the global overweight in US equities about to change?
- Then there is the shifting global capital flows – as currency barriers will go up as sanctions and capital barriers spread.
- The BOJ has committed to printing money to buy all available 10-year JGBs. Yield curve control is in place! Let's see what inflation in Japan does now after running at less than 1%.

WHAT THE CENTRAL BANK / GOVERNMENT WANT

- The MOF and regulators historically have come out in favor of fiscal austerity. Japan's companies seem more interested in growing their businesses and are perhaps not as concerned with the Yen's levels as the monetary/fiscal authorities are. Multiple rounds of QE generally produced marginal economic growth.
- Are Japan's markets essentially being nationalized? JGBs essentially have been and Nikkei ETFs are not far behind. Will new forms of Japanese QE be needed to pay for "buying them all," whether it's stocks or bonds? The JGB market is being essentially transferred onto the JGB balance sheet. Will more foreign equities eventually be bought to weaken the Yen? At the moment, the Yen looks weak enough, but after rallying from 139 to 127, it now sits at a multi-year low around 135-136.

TARGETS

Japanese yield targeting, sets the stage for the same policy in the US. That USD/Yuan/Yen triangle is crucial for Asian trade and global growth. The BOJ was first in zero rate policy, many years ago. There is no sign yet, that they will be the first to exit.

Japan was also the first major country to go into deflation, years ago. Though it seems unlikely, if Japan sees a new burst of inflation, where will Japanese interest rates go? In to what assets will Japanese investors move? And what asset classes will they depart? This will be important for global capital flows and negative for the Yen. Investors in JGBs continue to sell, which bumps 10-year yields up against the 0.25% barrier.

Taiwan is becoming a larger and larger issue for Japan. Japan appears to have aligned itself increasingly with US defense policy and the Indonesia-Pakistan Trade Agreement and the Quad. Japan's government is in the early stages of designing a more offensive military policy which will be expensive.

We are cautious about credit conditions in China which are still troubled, especially in the property market. This effects China's economy, therefore Japan's as well. As China's economy weakens and US growth slows, the Yen should weaken and it has, perhaps by too much/too fast.

How events play out in Europe, may yet turn the Yen into a safe haven currency. All things considered, Yen/Dollar seems too low, but it may go lower.

Japanese Yen

Courtesy of Bloomberg LP

Sources:
Bank of Japan. (http://www.boj.or.jp/en/)
Bloomberg Data
Department of the Treasury/Federal Reserve Board

Swiss Franc (GPF)

DXY

Courtesy of Bloomberg LP

SF/Aussie Dollar

Above two charts courtesy of Bloomberg LP

SWITZERLAND DATA

	Rate of Change	as of
REAL GDP YoY	4.50%	3/31/2022
PPI YoY	4.50%	4/30/2022
CPI YoY / Inflation	2.90%	5/31/2022
UNEMPLOYMENT	2.20%	5/31/2022
M1 YoY	3.29%	4/30/2022
M3 YoY	-0.10%	4/30/2022
Central Bank Rate	-0.75%	6/7/2022

SWISS FRANC—NEARING A BUY POINT

SWITZERLAND DATA

	Rate of Change	as of
REAL GDP YoY	4.50%	3/31/2022
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Comparative Data to Other Major Currencies

Country	3 Mo Int Rates	10 yr Int Rates	Real Short Rates (Using 3-mo rates less CPI)	Real Long Rates (Using 10-Yr Govt Bonds less CPI)
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Canada	1.68%	3.27%	-5.12%	-3.53%
Euro	-0.55%	1.35%	-8.65%	-6.75%
Japan	-0.09%	0.25%	-2.59%	-2.25%
Switzerland	-0.75%	1.051%	-3.65%	-1.85%
US	1.24%	3.02%	-7.06%	-5.28%
UK	1.71%	2.25%	-7.30%	-6.75%

Country	GDP	CPI	PPI	Unemploy-ment
Australia	3.30%	5.10%	4.90%	4.03%
Canada	3.50%	6.80%	16.41%	5.20%
Euro	5.40%	8.10%	19.30%	6.80%
France	4.50%	5.20%	27.80%	7.10%
Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

POLITICAL FACTORS

In recent elections, Swiss voters continue to show a definite trend to vote in favor of the conservative right. Politics are comparatively stable in Switzerland. The major political issue has rapidly shifted to the Ukrainian situation and Switzerland's role in it. Switzerland moved a bit away from its historically neutral stance, by participating in some Western moves against Russian oligarchs. Has Switzerland abandoned its long standing policy of neutrality?

MONETARY/ECONOMY

- The SNB's goal of managing the currency against the Euro to assist the country's export-oriented firms, is having some success and will continue. The economy has picked up to a 3.9% real growth rate.
- If the world is successful in reflating economies, Switzerland will benefit. Economically, interest rates should rise as GDP expands. Inflation remains low. How much longer can the Swiss economy, pension funds and insurance companies live with negative rates and a Swiss Franc this high? It's been many years of negative rates yet surprisingly the financial system has held together. How long can a financial system function effectively under these conditions? Long and short term negative yields could have unforeseen consequences on capital allocations, asset prices and eventually on the economy, over the next few years, especially if rates continue to rise in other major economies. This may be a perfect model for a weaker SF.
- The European bank system remains a risk for Switzerland. By splitting into international/domestic operations, Swiss banks are positioning themselves for the next environment. If the currency market's perception of Swiss banking safety improves further, the SF will strengthen again, prolonging the negative yield environment and perhaps pushing the SNB to continue to intervene by further expanding their balance sheet. European bank stocks have had a rough start in 2022, falling about 20% or more. Credit stress is beginning to show across Europe's banks, which will have some effect on Switzerland.

WHAT THE SNB/GOVERNMENT WANT

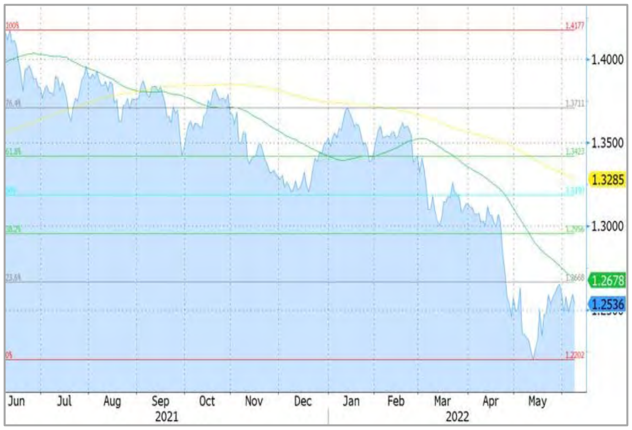
The SNB seems to want a weaker SF, so we look for currency intervention to occur if the SF appreciates further. CPI has remained low, so real yields have not moved much against the SF. A new crisis in the financial markets, would likely push the SF higher. The odds of SF strength emerging, are growing.

TARGETS

The Swiss Franc remains a currency that will be bought in an economic/financial crisis. Increasingly, that sentiment, i.e. further sell-off of risk assets, is gaining ground after January's tech stock sell-off as the Ukraine/Russian war unfolds. There is virtually no inflation in Switzerland, so reflation tools, (lower currency?), can be employed, in large doses. However, in a risk-off world, the Swiss Franc will likely be a go-to asset, again. The Swiss Franc is likely to see further inflows and remain firm.

Sources:
Bloomberg
Swiss National Bank http://www.snb.ch/e/search/index.html

British Pound to US Dollar



Courtesy of Bloomberg LP

DXY

Courtesy of Bloomberg LP

UK POUND/US DOLLAR — THE UK UNLOCKS / SUPPLY CHAINS RE-LOCK FAIL TO IMPROVE MUCH/ BORIS GOES TO WAR? IS STERLING CHEAP ENOUGH?

UNITED KINGDOM DATA

	Rate of Change	as of
REAL GDP YoY	8.70%	3/31/2022
PPI YoY	-1.30%	10/31/2020
CPI YoY / Inflation	9.00%	4/30/2022
Unemployment	3.70%	3/31/2022
M4 YoY	4.90%	4/30/2022
Notes & Coins	0.30%	5/31/2022
Central Bank Rate	1.00%	6/8/2022
RPI	11.10%	4/30/2022

Comparative Data to Other Major Currencies

Country	3 Mo Int Rates	10 yr Int Rates	Short Rates (Using 3-mo rates less	Real Long Rates (Using 10-Yr Govt Bonds less CPI)
Australia	1.17%	3.55%	-3.93%	-1.55%
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France	4.50%	5.20%	27.80%	7.10%
Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

MONETARY/ECONOMIC FACTORS

- The UK economy is at risk of slowing significantly due to soaring energy prices, supply chain disruptions, rising food prices and shortages of workers, who are calling in sick. GDP estimates for the year have already soared, to +6.6%, but will come down now as soaring energy prices spread across Europe. Passage of the windfall profits tax on energy companies will help consumers somewhat. It will also dis-incentivize oil companies to produce more oil.
- Broad money supply (M4) is +4.9% YoY. This is much lower than US broad money growth which may partially explain why Sterling has strengthened vs. the Dollar.
- Sterling is the key UK asset price to watch. Any sign of an economic rebound and/or higher home prices further strengthens Sterling versus the Euro and the Dollar. Interestingly, home prices may be on the verge of dipping, partly due to rising mortgage costs.
- It looks like it will take five or more years before the UK's budget is balanced, if ever. Funding for the NHS is to be increased by 10 billion pounds. Austerity policies are out, whether it is Tories or Labour making the call. Growth initiatives are on the way in, but so are more taxes. Are loose monetary and more balanced fiscal policy the preferred policy mix?
- Flow-of-Funds — The UK is a much more service-oriented economy than it is export-driven. For years, foreign capital poured into the London real estate market and the buy-to-let schemes which pushed even more capital into first-time real estate buyers. That scheme peaked as stamp duties were piled on and buy-to-let schemes ended. Affordable housing remains a problem in London. In the financial services area (London), the EU is looking to help every possible financial service business that it can move out of London.
- The BOE is including asset prices in their policy making mix. This is a good thing, which other central banks should also do.
- The UK's trade deficit:GDP ratio is about 5.9%, a level which suggests an undervalued Sterling is needed to finance it. Sterling has sold off by almost 30% since the pre-Brexit period. It should be cheap enough to start attracting long term-oriented buyers, but so far they have not appeared. Does Sterling need to trade lower still?
- The Boris Johnson era as PM may be coming to a close, but it is too early to make a call on that as well as making a call on the next national election. It's a long way to determining what the next government will look like.

WHAT THE BOE/GOVERNMENT WANT

Lower Sterling / Euro probably suits what the economy needs, but it won't help the inflation picture. Lower Sterling, probably does not bother the government too much, unless it leads to an even larger surge in inflation which seems likely in the near term.

TARGETS

Sterling looks cheap vs. the Dollar. Sterling vs Euro and Sterling vs a basket of world currencies is a good lead on the global economy. Near term, the signals are pointing lower for the world economy.

Sterling is cheap relative to the USD, while the Yen has put downside pressure on currencies across the board. Sterling is probably too cheap due to the UK's unique location, naval experience and commercial experience.

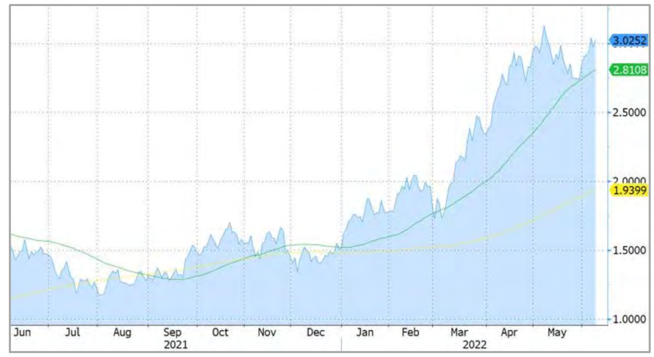
Sources:

Bank of England. (http://www.bankofengland .co.uk/) and Bloomberg LP

US Dollar Index

Courtesy of Bloomberg LP

10-Year Gov't Yields
Are Generational Yield Lows in Place?



Courtesy of Bloomberg LP

Fed Drives Liquidity / Liquidity Drives Markets
Fed Balance Sheet to Grow to 40% of GDP

Courtesy of Bloomberg LP

US DOLLAR—WHAT HAPPENS IF THE FED PIVOTS?

POLITICS

It may be in the US' interest (to devalue government debt) by engineering a lower Dollar in order to attract foreign capital and improve the US balance sheet. Inflation has arrived even with a strong Dollar and it is creating a problem for voters, the administration and the markets in view of this year's mid-term elections.

The Progressive wing of the Democrat Party is very much in favor of raising taxes, whether they are personal income taxes, capital gains or corporate taxes. These proposals are anti-growth; however, the economic offset is massive fiscal spending much of it on social programs which was allocated last year. Many of the new administration's policies increase regulation and slow growth, and spend massive amounts on social programs. The issue now for the Dollar is whether this is all bullish or bearish? History would suggest it will turn out to be bearish for the Dollar and inflationary.

MONETARY/ECONOMIC FACTORS

- Governors are admitting they are behind the inflation curve. There may also be a limit as to how high interest rates can go without starting a major rise in risk asset volatility. That risk is unfolding as the 10-year Treasury Yield trade above 3%.
- The Fed has been encouraging an inflation overshoot in the interest of financing massive social/infrastructure spending and maximizing employment. Chairman Powell's rhetoric along with other Fed Governor's has changed to a more hawkish tone. Multiple rate hikes look like the Fed's next move, unless the markets become disorderly. In terms of the political cycle, time is running out for rate hikes to slow inflation, which may not have as much of an effect anyway. The Democrats have apparently decided to run for election during a rate hike cycle.

WHAT THE FED/GOVERNMENT WANTS

A lower Dollar and a long period of low interest rates is needed for the economy to grow at a pace which outruns the nation's debt service. Inflating the debt away which has accumulated in the last two years, could be another priority. The Dollar's strength in 2021 and early 2022 was a non-consensus move which still has not converted the market to being overwhelmingly bullish on USD. The high may be in place.

TARGETS

A growing problem with unfunded liabilities / medical care / Social Security funding / pension funding, and a surging budget deficit should eventually force the Dollar lower, unless significant revenue raising measures are made or budget cuts are enacted. Tax hikes to pay for additional spending remain unpopular among business, the middle class which is being squeezed by higher inflation. A commodity bull market which is increasingly driven by China, while global supplies are sanctioned / restricted, are a real risk.

Intermediate term, the Dollar looks stable to lower as the Fed will eventually be forced into further balance sheet expansion and QE / yield curve control will eventually be employed. If recession conditions occur, look for the Fed to pivot.

An outside the box risk (a higher Dollar) is a liquidity / economic / financial problem coming from Europe, a breakdown in China credit market or a crypto issue which pushes USD even higher. Inflation is becoming a major issue with inflation expectations hitting multi-year highs and commodities in a bull market. This is a cost-push inflation environment due to a shortage of goods, a lack of cap-ex and supply chain issues. This is not something the Fed can do much about.

On a 1–2-year basis, the monetization of US debt seems more and more likely, which should encourage the Dollar to move lower. Inflating away $30 trillion of government debt and more than $50 trillion in liabilities / entitlements seems like a plan. Intermediate term, the USD should move lower.

UNITED STATES DATA

	Rate of Change	as of
US GDP Nominal Dollars YoY SA	3.50%	3/31/2022
PPI YoY	15.70%	4/30/2022
CPI YoY / inflation	8.30%	4/30/2022
U-3 Unemployment	3.60%	5/31/2022
U-6 Unemployment	7.10%	5/31/2022
M1 YoY	8.90%	4/30/2022
M2 YoY	8.00%	4/30/2022
Federal Funds Target Rate	1.00%	6/8/2022
ISM Non-Manufacturing NMI NSA	55.90%	5/31/2022
US Industrial Product MoM 2	1.08%	4/30/2022

Comparative Data to Other Major Currencies

Country	3 Mo Int Rates	10 yr Int Rates	Real Short Rates (Using 3-mo rates less CPI)	Real Long Rates (Using 10-Yr Govt Bonds less CPI)
Australia	1.17%	3.55%	-3.93%	-1.55%
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US	1.24%	3.02%	-7.06%	-5.28%
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France	4.50%	5.20%	27.80%	7.10%
Germany	3.80%	7.90%	33.40%	5.00%
Japan	0.40%	2.50%	9.50%	2.50%
Switzerland	4.50%	2.90%	4.50%	2.20%
US	-1.50%	8.30%	15.70%	3.60%
UK	8.70%	9.00%	-1.30%	3.70%

as of 6/08/2022

Sources:
Bloomberg Data
Bloomberg News

Larry's Travel/Speaking Schedule

June 13-20 ______________________________ *Europe*

Spelling Deficiency Revealed

One of our projects at military leadership school called for us to speak in front of the class on a topic picked by our instructor. A classmate gave an impassioned speech on the benefits of drinking liquor. Alcohol, he insisted, warded off colds, kept you alert, and even made you steadier on your feet.

"Good job," said our instructor when he finished. "Only one thing: Your topic was the benefits of drinking liquids, not liquor."

Supervision Required

When hiring new staff at the public library, I always ask applicants what sort of supervision they'd be most comfortable with. One genius answered, "I've always thought Superman's X-ray vision would be cool."

Easy Answer

There was a typo on a test I was taking. Instead of "(D) none of the above," it said "(D) one of the above." So I circled it.

Parapraxis

"You need to be careful when writing comments," our principal told the faculty. He held a report card for a Susan Crabbe. A colleague had written, "Susan is beginning to come out of her shell."

Cushy Job

My daughter Marina worked in my law office while she attended graduate school. One morning a call came in for her. I said she wasn't in yet and offered to take a message. The caller said she'd phone back later.

At 11:00 a.m., the caller tried again, and I reported that Marina had gone to lunch.

The last call came in at 3:30 p.m. "I'm sorry," I said, "she's left for the day. May I take a message?"

"Yes," the caller replied. "How can I get a job with you?"

Polite But Stupid Thief

A jeweler standing behind the counter of his shop after hours was astounded to see a suspicious looking man in a black ski mask come hurling headfirst through the window.

"What on earth are you up to? What happened?!" the jeweler demanded.

"I'm terribly sorry," said the man, "I forgot to let go of the brick."

Seared Conscience

The district attorney was cross-examining the murderess on the witness stand.

"And so after you had poisoned the coffee and your husband sat at the breakfast table partaking of the fatal dosage, didn't you feel any qualms? Didn't you feel the slightest pity for him knowing that he was about to die and was wholly unconscious of it?"

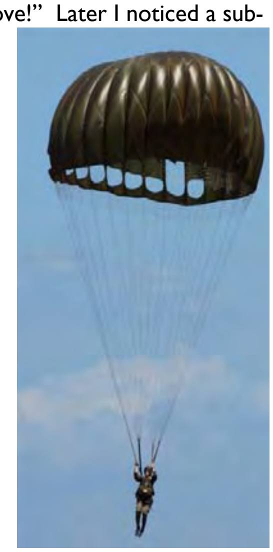
"Yes," she answered. "Come to think of it…there was just a moment when I sort of felt sorry for him."

"And, when was that?"

"When he asked for the second cup."

Surrounded by Death Threats

As a new paratrooper, I was struck by all the T-shirts on base emblazoned with the motto "Death from above!" Later I noticed a submariner with a T-shirt that declared "Death from below!"



Then, standing in line for chow one day, I was served by an Army cook. His T-shirt had a skull with a crossed fork and spoon underneath and yet another warning: "Death from within!"

Lacking In Honor

Since he runs a pawnshop, I decided to ask a friend of mine to appraise my grandfather's violin. "Old fiddles aren't worth much, I'm afraid," he explained.

"What makes it a fiddle and not a violin?" I asked.

"If you're buying it from me, it's a violin. If I'm buying it from you, it's a fiddle."

Insufficient Brains

I requested identification from a department-store customer who had just written a personal check for her purchase. After fumbling through her purse, she presented me with what she said was the only thing that bore both her name and address.

It was a notice of insufficient funds from her bank.

Falsely Accused

Do I look that shady? I just got a GPS for my car, and my first trip with it was to a drugstore. Since the manual said not to leave it in the car unattended, I brought it with me into the store. While there, the GPS came alive, and a voice stated, "Lost satellite contact."

I wasn't embarrassed until a woman turned to me and said, "Your ankle bracelet monitor is talking to you."

Necessary Change

An old man strode in to his doctor's office and said, "Doc, my druggist said to tell you to change my prescription and to check the prescription you've been giving to Mrs. Smith."

"Oh, he did, did he?" the doctor shot back. "And since when does a druggist second guess a doctor's orders?"

The old man says, "Since he found out I've been on birth control pills since February."

Good News, Bad News

Dr. Smith asks his patient, "Which do you want first, the good news or the bad news?"

The patient replies, "Give me the good news."

Dr. Smith says, "You're about to have a disease named after you."

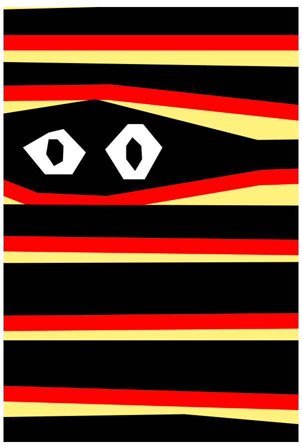
Extreme Measures

One night our dog suddenly began barking almost every night at around 3 a.m.

Irritated and sleepy, my husband, Larry, searched the back yard for what might have disturbed this otherwise peaceful animal.

For three days he found nothing amiss. When the dog woke up the neighborhood a fourth night at 3 a.m. with frantic barking Larry finally snuck around the house through the alley only to discover our quiet neighbor, the last man you'd suspect of wrongdoing, throwing pebbles over the fence at the dog.

My husband demanded to know what he was doing.



"My mother-in-law is visiting," the embarrassed neighbor explained. "If she gets woken up in the middle of the night one more time she says she'll leave."

Self-Absorption

I was sound asleep when the telephone jarred me awake.

"Hi!" It was my peppy mother-in-law. She proceeded to rattle on about the busy day she had ahead and all the things that awaited her the rest of the week.

"Mom," I interrupted. "It's five in the morning."

"Really? What are you doing up so early?"

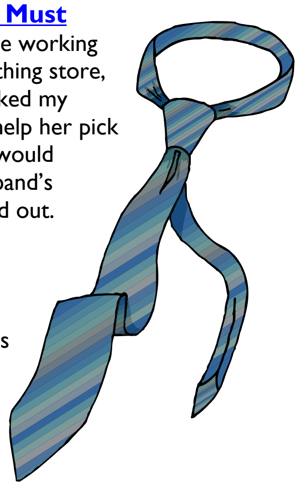
Learned Behavior Without Understanding

We visited our newly married daughter, who was preparing her first Thanksgiving dinner. I noticed the turkey thawing in the kitchen sink with a dish drainer inverted over the bird. I asked why a drainer covered the turkey.

Our daughter turned to my wife and said, "Mom, you always did it that way."

"Yes," my wife replied, "but you don't have a cat!"

Comfort A Must



While we were working at a men's clothing store, a customer asked my coworker to help her pick out a tie that would make her husband's blue eyes stand out.

"Ma'am," he explained, "any tie will make blue eyes stand out if you tie it tight enough."

Groaner

Jimmy: 'Hey, Mike! How's your new pet fish doing? You told me he was really something special.'

Mike: 'To tell the truth, I'm really disappointed in him. The guy who sold him to me said I could teach him to sing like a bird.'

Jimmy: 'What? Let me get this straight… You bought a fish because you thought you could teach him to sing like a bird?'

Mike: 'Well, yeah. After all, you know, he's a parrot fish.'

Jimmy: 'Now listen, Mike, while you might be able to teach a parrot to sing, you're never going to get anywhere with a parrot fish.'

Mike: 'That's what you think! It just so happens this fish CAN sing. The thing is, he's terribly off-key and it's driving me crazy. Do you know how hard it is to tuna fish?'

Possible New Airline Fees

With airlines adding fees to fees, The Week magazine asked its readers to predict the next surcharge they'll levy for something previously free.

1. In the unlikely event of loss of cabin pressure, oxygen masks will drop down. To start the flow of oxygen, simply insert your credit card…

2. $100 On-Time Departure Fee; $25 Delay Complaint Fee.

3. View seating (formerly window seats), $10; Access seating (formerly aisle seats), $10-$20 to use roll-away stairs to enter or exit the aircraft in lieu of no-charge rope-ladder alternative.

4. $9 fee for bumping your head on the overhead bin as you take your seat; $3 additional penalty for looking up at the bin after you bump into it.

Time To Return

When I asked my friend if she was planning to attend church, she just shook her head. "I haven't gone in a long time," she said. "Besides, it's too late for me. I've probably already broken all seven commandments."

Thirsty Car

As the owner of an old clunker, I was used to dealing with a variety of car breakdowns. One day at the supermarket, just after I had filled my trunk with groceries, I noticed a stream of fluid pouring out of the bottom of the car. I knew I had to get home before the car was once again out of action.

When I arrived I asked my husband to take a look at the problem. Expecting the worst, I braced myself for his diagnosis. When he came back in, he was smiling. "It's apple juice," he said.

Convenient But Not Practical

My niece was thrilled to hear that a new car wash was opening up in her neighborhood. "How convenient," she said. "I can walk to it!"

Earthlings

Out in space two alien forms are speaking with each other.

The first spaceman says, "The dominant life forms on the earth planet have developed satellite-based weapons."

The second alien, who looks exactly like the first, asks, "Are they an emerging intelligence?"

The first spaceman says, "I don't think so…They have them aimed at themselves."

Expensive Mistake

"For sale," read the ad in our hospital's weekly newsletter, "sleeveless wedding gown, white, size 8, veil included. Worn once, by mistake."

Things That Never Happened On Star Trek

1. The Enterprise runs into a mysterious energy field of a type it has encountered several times before.

2. The Enterprise visits a remote outpost of scientists, who are all perfectly all right.

3. Some of the crew visit the holodeck, and it works properly.

4. The crew of the Enterprise discover a totally new life-form, which later turns out to be a rather well-known old life form wearing a funny hat.

5. The crew of the Enterprise are struck by a mysterious plague, for which the only cure can be found in the well-stocked Enterprise sick-bay.

6. The Captain has to make a difficult decision about a less advanced people which is made a great deal easier by the Starfleet Prime Directive.

7. The Enterprise successfully ferries an alien VIP from one place to another without serious incident.

8. An enigmatic being composed of pure energy attempts to interface to the Enterprise's computer, only to find out that it has forgotten to bring the right leads.

9. A power surge on the Bridge is rapidly and correctly diagnosed as a faulty capacitor by the highly-trained and competent engineering staff.

10. The Enterprise is captured by a vastly superior alien intelligence which does not put them on trial.

11. The Enterprise is captured by a vastly inferior alien intelligence which they easily pacify by offering it some chocolate.

12. The Enterprise visits an earth-type planet called "Paradise" where everyone is happy all of the time. How-ever, everything is soon revealed to be exactly what it seems.

13. A major Starfleet emergency breaks out near the Enterprise, but fortunately some other ships in the area are able to deal with it to everyone's satisfaction.

14. The Enterprise is involved in a bizarre time-warp experience which is in some way unconnected with the Late 20th Century.

15. Kirk (or Riker) falls in love with a woman on a planet he visits, and isn't tragically separated from her at the end of the episode.

16. Counselor Troi states something other than the blindingly obvious.

17. The warp engines start going haywire, but seem to sort themselves out after a while without any intervention from boy genius Wesley Crusher.

18. Spock (or Data) is fired from his high-ranking position for not being able to understand the most basic nuances of one in three sentences that anyone says to him.

Source:
http://www.cleanlaffs.com

Table of Contents

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US
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- Bloomberg News.
- Paul Nesbitt, 618034, Ltd

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THE INSTITUTIONAL STRATEGIST

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