
# Macro, Tapering, The Demand Side, & Asset Price Projections

By Thomas H. Kee Jr.
President and CEO
Stock Traders Daily

# How will the changes to monetary policy affect asset prices?

- Global Liquidity will be severely impacted
- $2.41 Trillion is coming out of demand starting now.
- $2.17 Trillion is coming out within 3 months.
- The rest will come out in Q3 and Q4 2022
- These are annualized figures.
- They are huge!

# Price = Supply X Demand

This is a demand-side analysis


Price is a factor of Supply and Demand, but asset prices are more precisely influenced by New Money Demand. That includes New Money from Natural Sources, and Stimulus, with stimulus having been a huge factor recently. Powell finally acknowledged the adverse effect of this, inflation, and seemed to suggest that he now thinks monetary + fiscal policies have gone too far. He also said they did not know what to expect from the pandemic, so they did their best, but they were still very late to the game. It seemed like the new variant was the last straw, and now the FOMC is at full-pivot. Thomas H. Kee Jr., Stock Traders Daily

# This is a Central Bank – Macro – Monetary Policy Observation.

## The FOMC and ECB are the main Central Banks

- Our ongoing Observations of stimulus since inception proves this.
- Evidence also exists from when our Global Liquidity Reports Began in 2015
- Other Central Banks do not have the same influence.

# The FOMC

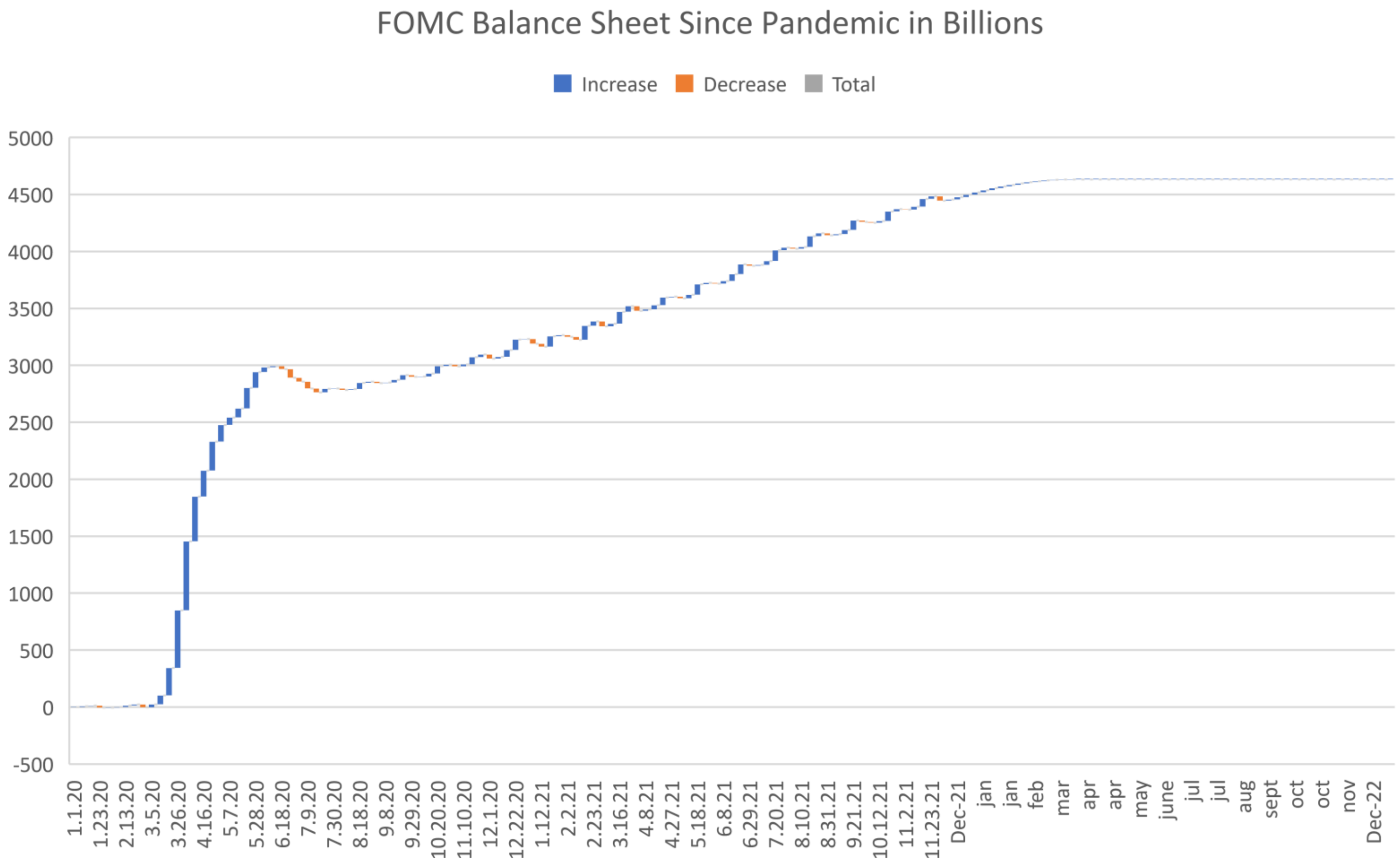
The FOMC Balance Sheet will stop growing in March 2022.

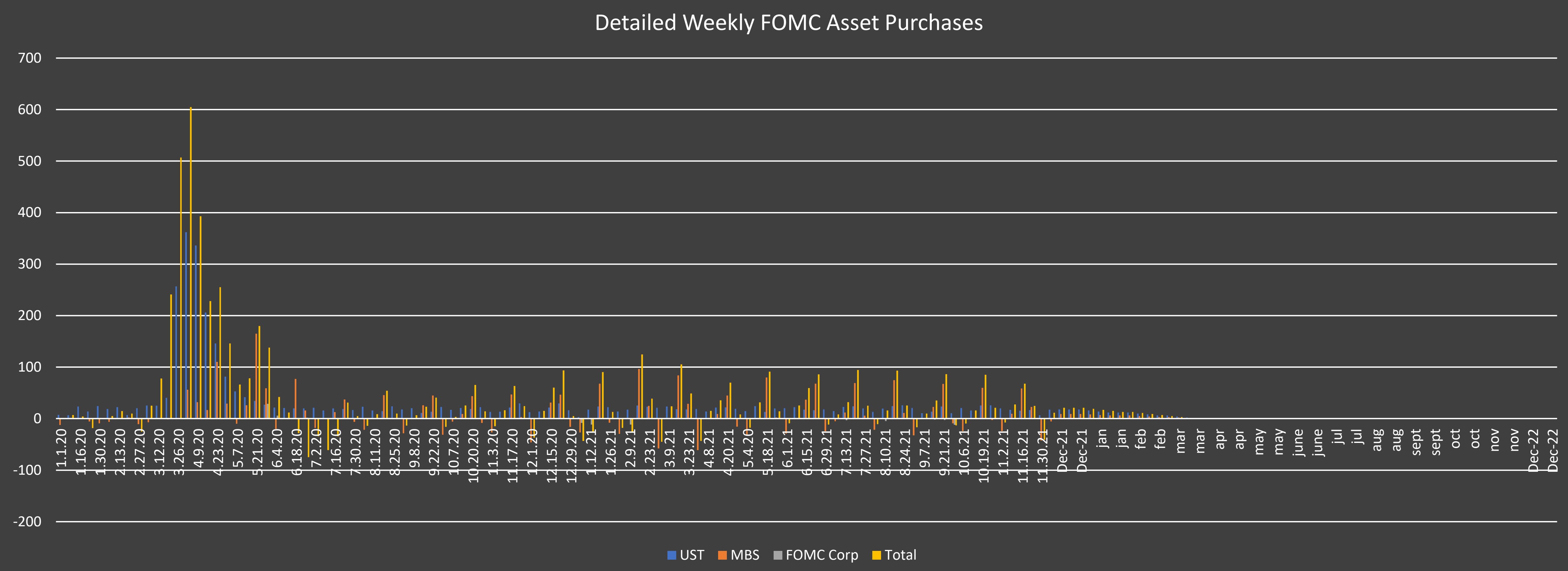
# Start with the Good (It will get uglier fast):

- $4.5 Trillion was added to the balance sheet since Jan 2020.
- This will cease and debt hawks will be appeased.

*From FOMC Monetary Policy directives.*

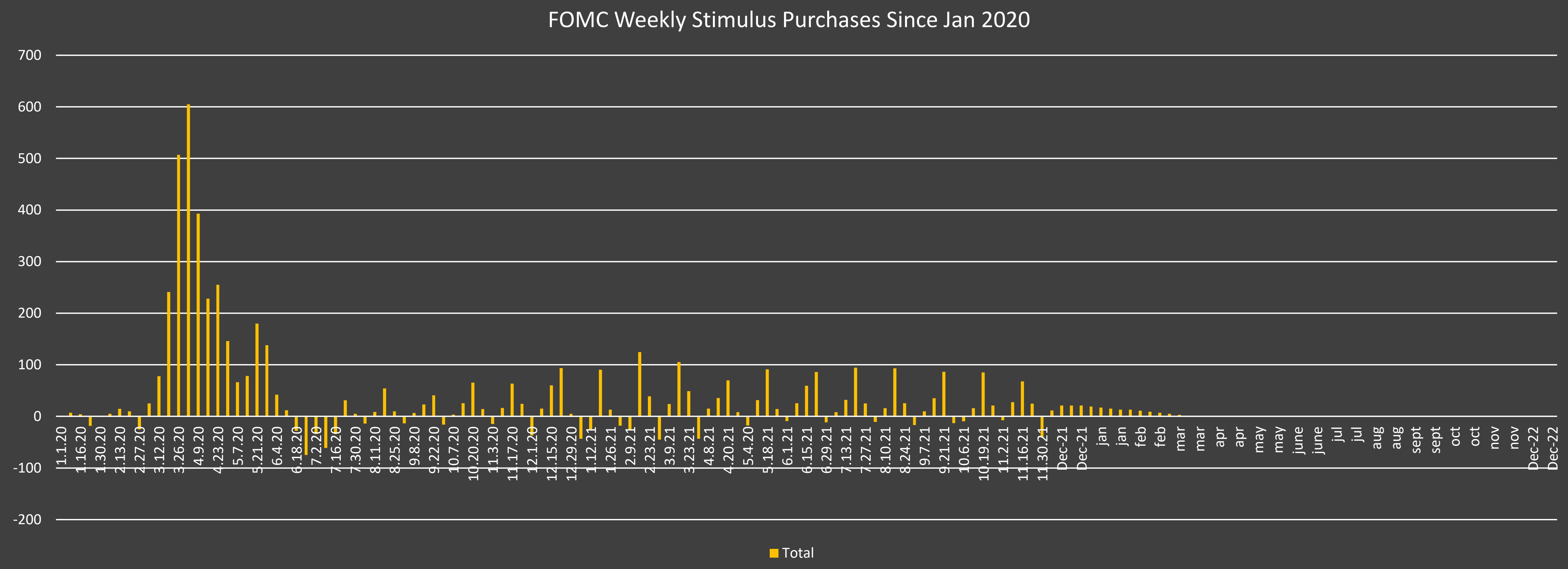
No More New Money from Stimulus






## Detailed weekly asset purchases of the FOMC

- It is a broad look at what has happened.
- We will examine this in closer detail hereafter
- Notice the spike at the beginning of the pandemic
- Notice the trickle to unidentifiable by the end of 2022

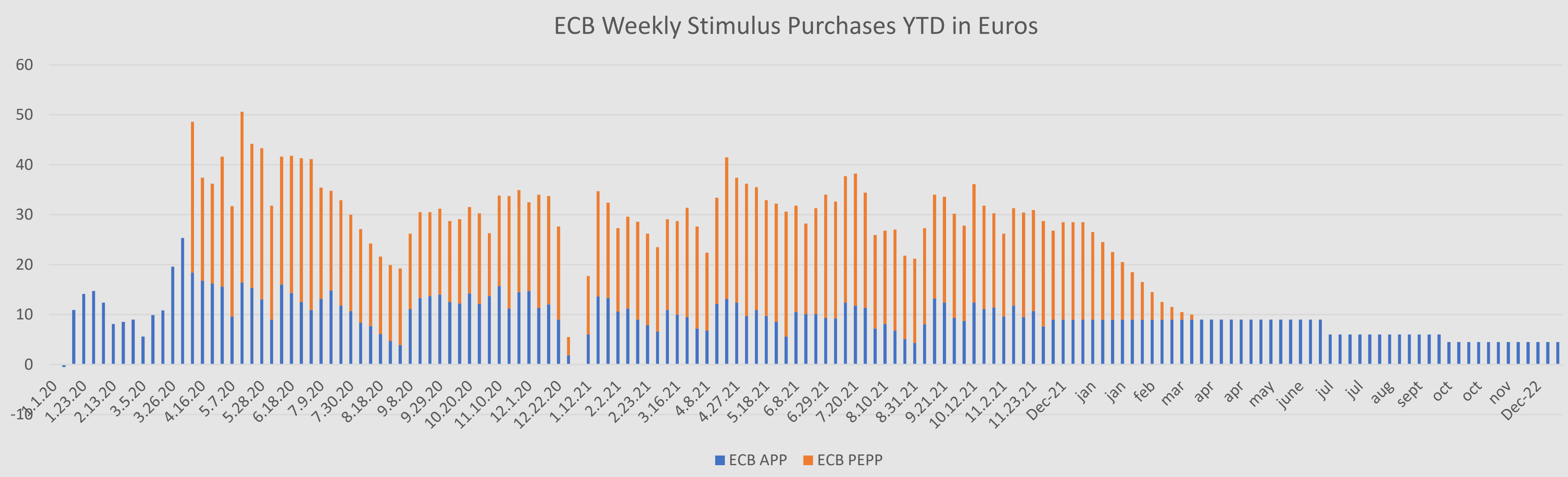



## $88 B Removed from Demand by the FOMC

- Typically, a big purchase was made every 4 weeks.
- In between the pace was much slower than that.
- Since 1.1.20 the pace was $120 B per month
- Since 8.1.21 the pace was $88 B per month.
- That will be reduced to $0 in March 2022.

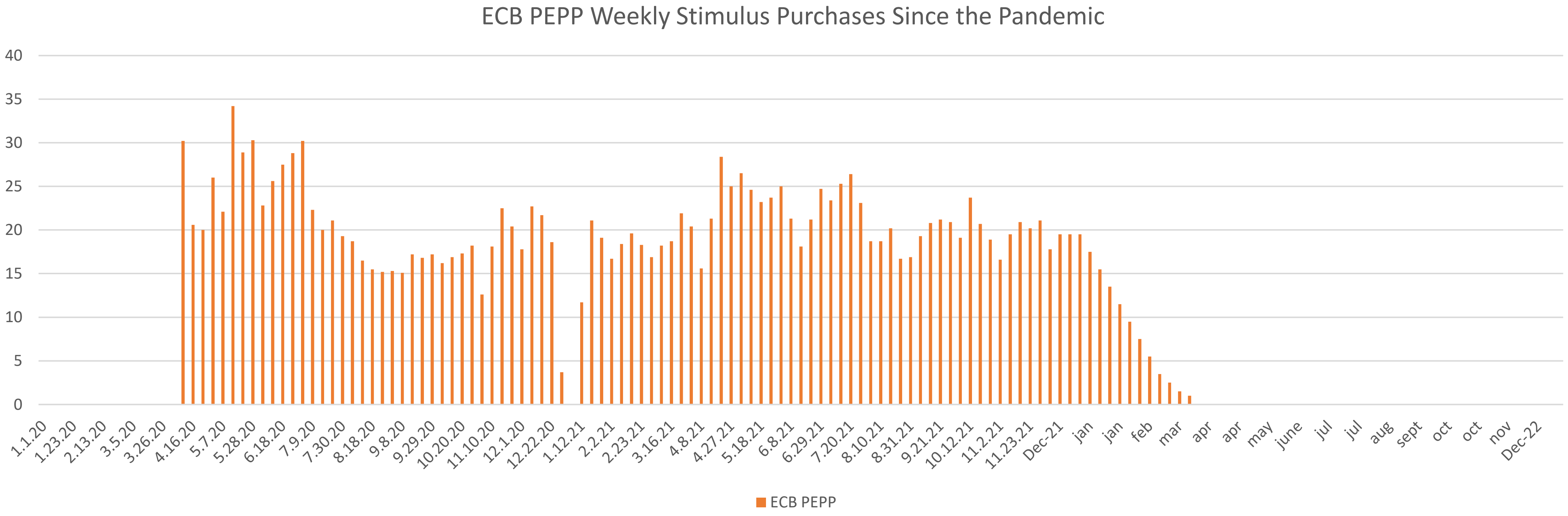
# The ECB

The ECB has two programs: PEPP + APP
Together these have averaged €115 B/month
These need to be distinguished from each other.
PEPP and APP have different tapering schedules and magnitudes.



# ECB PEPP will dissolve to €0 by March 2022

- PEPP has averaged €78 B per month
- That will decline to €0 in March 2022
- This is based on ECB Monetary Policy directives.



# FOMC Stimulus + PEPP will dissolve within 3 months!

- The entire FOMC ‘New Money’ Stimulus program will dissolve in 3 months.
- They will churn already invested (old) money (but that won’t influence price).
- New asset demand is required to influence asset prices higher
- Reinvesting principle & interest is neutral, reductions are different.
- Balance sheet reductions are far worse than stimulus reductions too.
- Last time the FOMC did not start reducing its balance sheet for years

# About Balance Sheet Reductions

- This is not our first rodeo
- They have done this before.
- FOMC Stimulus stopped last time in 2015.
- The balance sheet remained the same until 2018
- That is when volatility kicked in, valuations mattered again.
- That is when our CORE Portfolio Strategy was developed too.

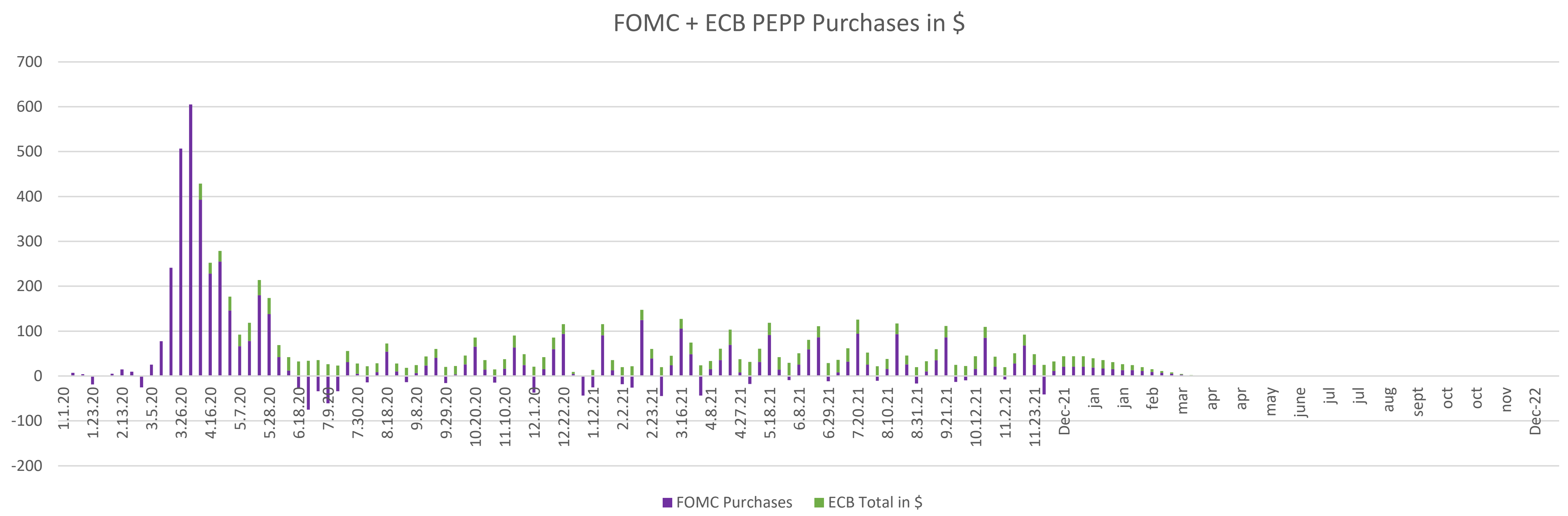
# Our CORE Portfolio Strategy

- After Global Stimulus stopped (2018) CORE was developed.
- CORE was designed to minimize volatility and protect assets.
- This was done in front of what was a coming drawdown in demand.
- The coming drawdown in new money demand was from tapering.
- It had a 34 Sortino in 2019, protected from Corona in 2020…
- CORE worked then and can work now too.
- It was built for this same environment.
- Liquidity levels are drying up fast
- Risk control is the #1 directive

More about CORE later…

# FOMC + ECB PEPP Stimulus in USD $

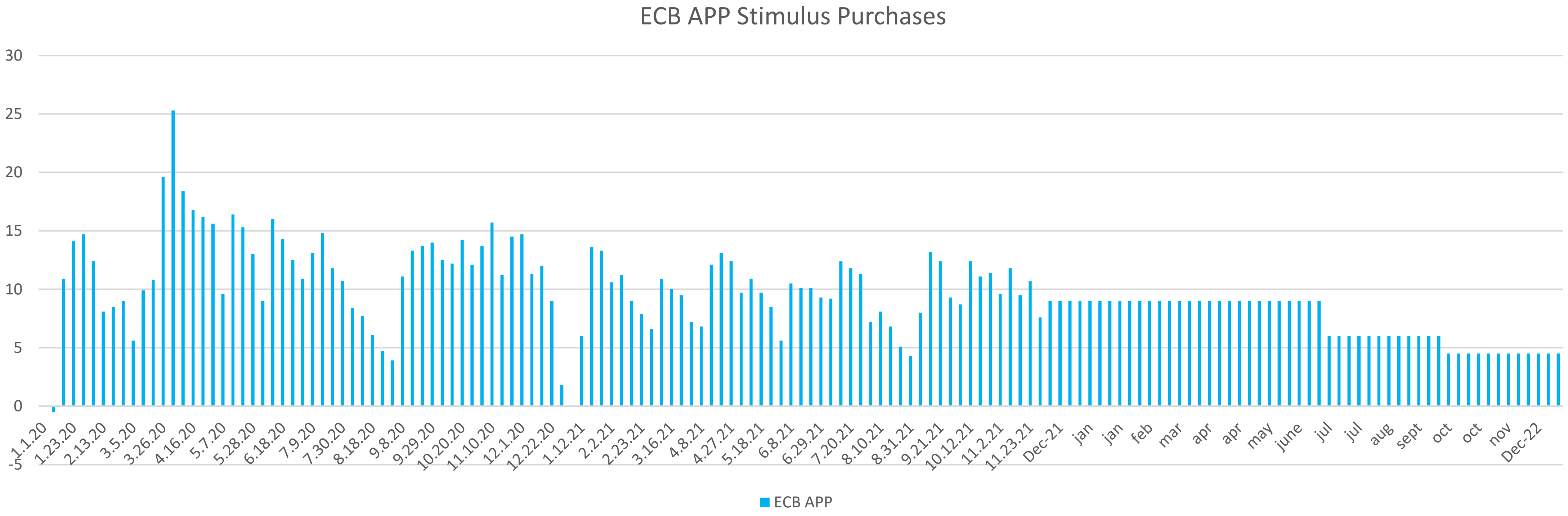
- Since 8.1.21 the combined average is $181 B per month
- That equates to $2.17 Trillion on an annualized basis.
- This will all be gone by March 2022.
- That's 3 months, and it is fast!



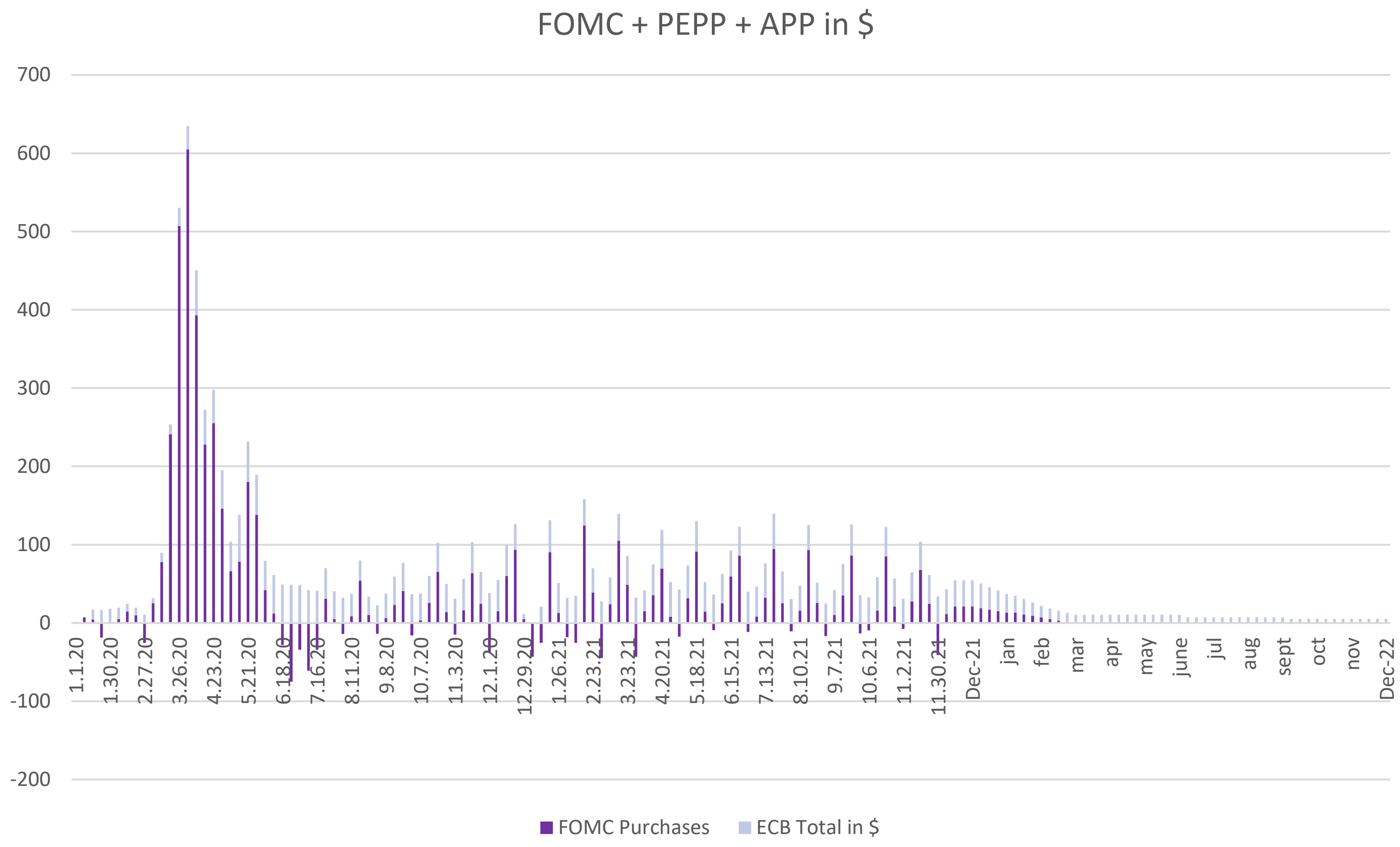
# ECB APP will survive

The Entire ECB PEPP Program will dissolve in 3 months

- APP will survive PEPP conditionally
- ECB APP is at 2017-like stimulus levels (€40B/m)
- ECB APP will not be cut until Q3 2022
- Then it will be cut in half by Q4 2022
- APP is likely to remain at €20B/m)
- APP will dissolve just before rate hikes.

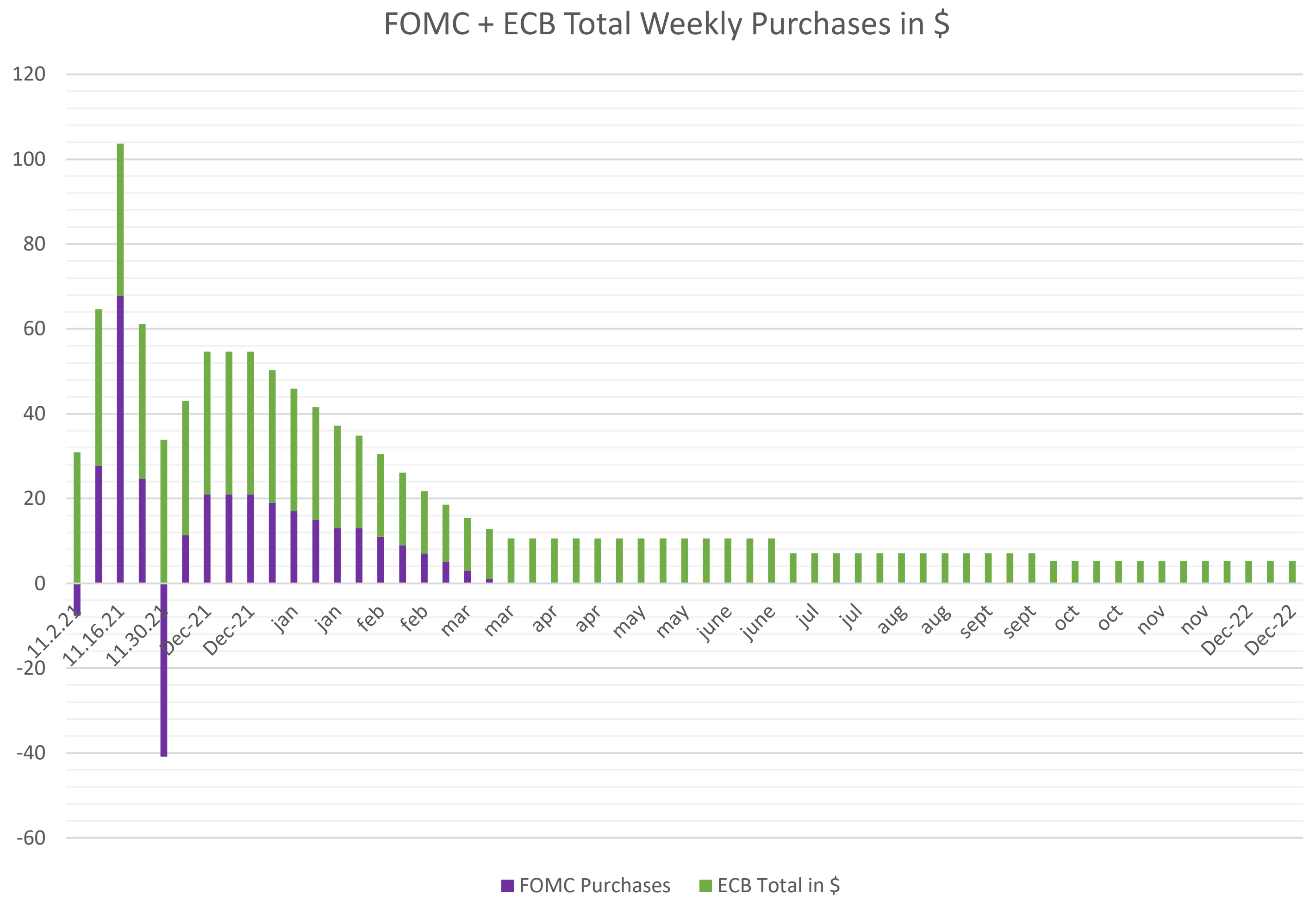


The Chart below shows FOMC + PEPP + APP Notice the material decline, to virtually nil.



# Here's an easier view.

- The combined FOMC + PEPP declines from $181 B/month to $0 by March
- APP will decline from $40 B to $20 B/month between Q3 2022 and Q4 2022.
- $2.41 Trillion of annualized demand will come out of Demand by Q4 2022 (1-year)




The $2.41 Trillion decline in overall annualized demand (reduced stimulus) is material. However, there is a component of that which must be more acutely observed.

# Corp. Debt

# Corporate debt purchases have a more direct influence on Equity Markets.

Reinvestment decisions associated with corporate debt purchases are much more likely to flow into equities and therefore create a bid in the stock market for the life of the stimulus program.

# Comps between corp. debt & equities:

- This was materially tangible in 2015
- In 2017 one-sided up-market, which also included piggybacking
- In 2019, after overnight lending rates spiked to 8%
- And especially when the FOMC got in the game after the corona crash.

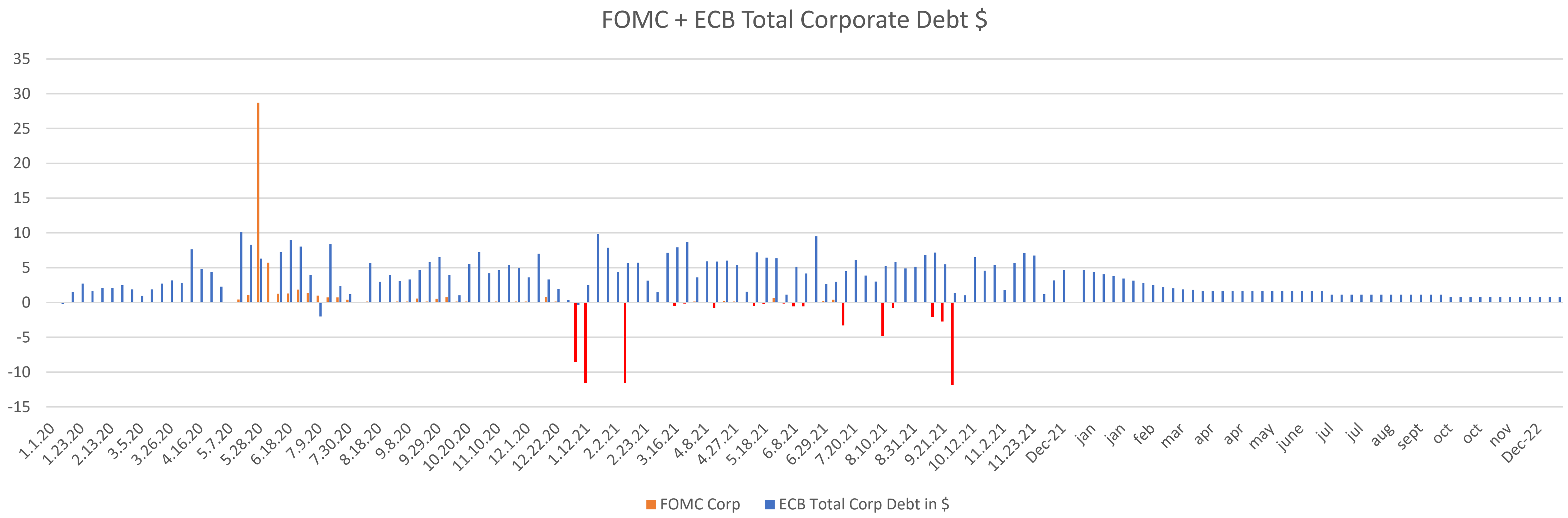
# Corp Debt acutely impacts equity-risk perceptions:

- Stimulus programs do not care about risk or valuation, and it this is especially true in the corp. debt space.
- They encourage reinvestment decision makers to devalue natural and prudent concerns too.
- That makes investors willfully pay higher valuations than they otherwise might.
- Ultimately Stimulus Programs increase risk appetites.
- Higher risk appetites last until stimulus programs end.
- When stimulus programs end, the natural risk perceptions come back

# That is When Valuation Risk Increases

# This Chart shows the combined Corp Debt of the FOMC + ECB.

- The ECB started APP in Nov 2019; it was there before Covid.
- The FOMC hit this hard right at the beginning of the Pandemic.
- The FOMC was extremely aggressive and it spurred a turn.
- The actions of the FOMC were very effective at the time.
- Then, the ECB added PEPP after the pandemic began.
- Since then, the ECB is the only Corp debt purchaser.
- The FOMC has been a net seller of Corp debt.



# The Good, Bad and Ugly

- **GOOD**: Aggressive Monetary Policy moves have staved off disaster in the past.
- But asset purchases have dragged out, and asset price bubbles are everywhere.
- The focus shifted from stabilizing financial markets to spurring asset prices higher.
- **BAD**: The focus shift is BAD; it happened in 2013 too, that was the inauguration.
- Opinion: Buy assets to stabilize financial markets, then let free markets do the rest!
- **UGLY**: These policies have been killing free markets. Normal risk perceptions have dissolved. <u>Risk UNawareness</u> is prevalent.
- But that is about to change…

# Recent Evidence that Corp Debt Matters to Equity Demand

Consider September 2021 (recent memory). The Market reeled in September, but why?

The FOMC sold a bunch of corporate debt, effectively unwinding the pandemic purchases.

Those net sales offset the ECB and stalled Piggybackers, which lowered risk appetites.

The markets no longer had that fabricated bid, and they fell.

# Wen stimulus stops, Piggybackers stop, and they seem to focus on Corp debt.

Piggybackers is a term we use to define the market participants who try to get ahead of the scheduled asset purchases of the Central Banks. These amount to fast – money players, and they have been extremely influential.

We have taken advantage of this.  Not only do we use Central Banks but also the learned decisions of Piggybackers to find opportunity.  We take what the market gives us, as always, and recently it has been stimulus + those trying to get ahead of it, but now that is shifting.

We take what the market gives us

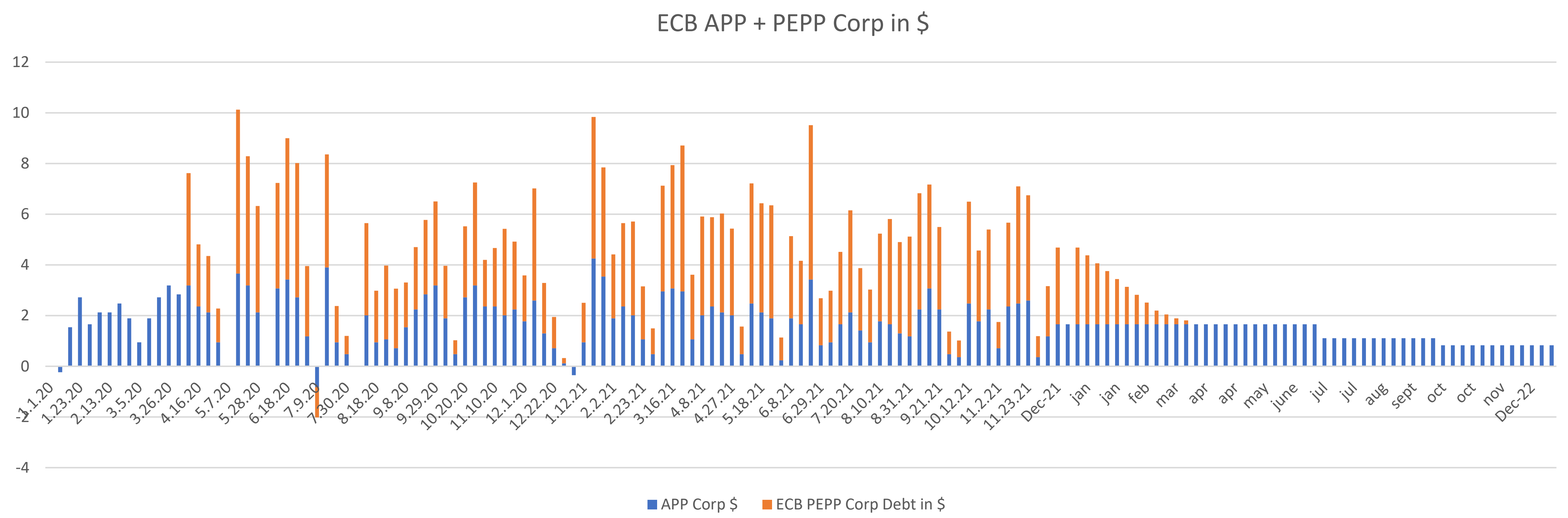

# When Corp. Debt is Removed from Stimulus

- Evidence exists in 2018, when the post credit crisis stimulus era came to an end. That was the first end-point for global stimulus, and it was accompanied by significant volatility.
- This is when natural risk perceptions started to surface as well.
- 2018 is also when we began our CORE Portfolio Strategy

CORE was designed to offer a low-volatility risk-controlled alternative to buy and hold.

# ECB PEPP vs. APP

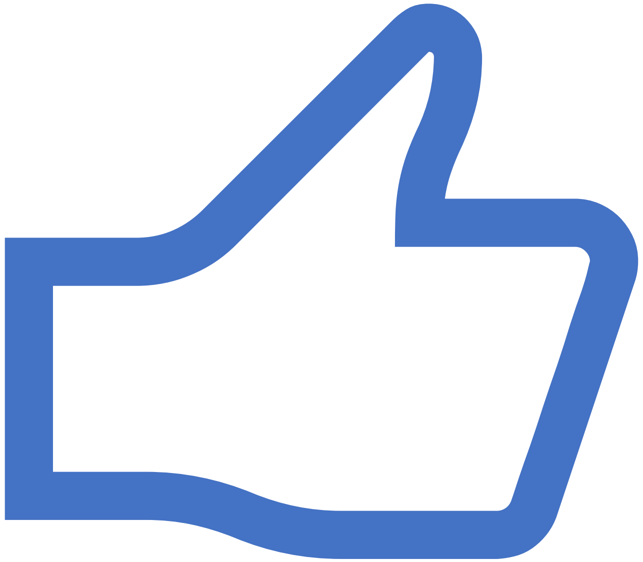
- The PEPP Portion Ends in March, as shown in the Chart.
- But APP will continue until Q3, and then decline
- It will decline below pre-pandemic levels.



# What about Q2 2022?

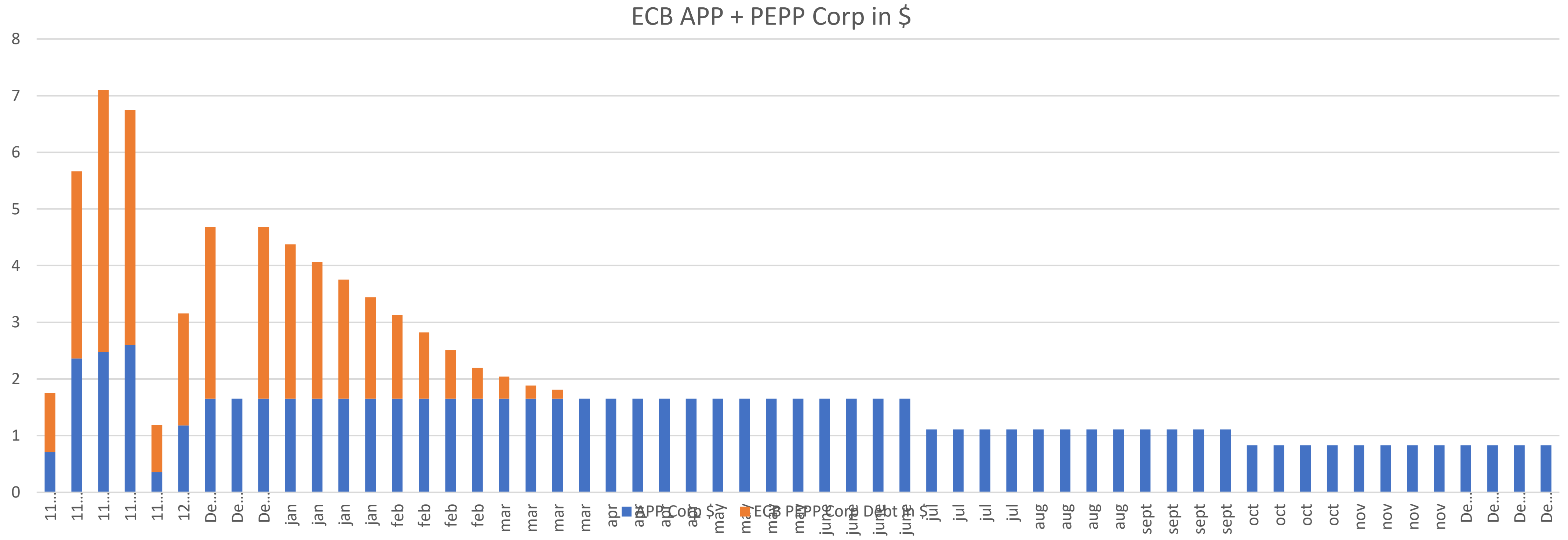
The declines will make the influence of Corp debt negligible.

- However, APP does not decline until Q3 2022
- PEPP ends in Q1 2022
- What about Q2?



# In Q2 2022 there will be a reprieve from asset purchase reductions.

- APP will continue at the 2017-like pace
- That was a very good market.
- In Q3 it will decline again.



# The Writing is on The Wall:

**Price = Supply X Demand**

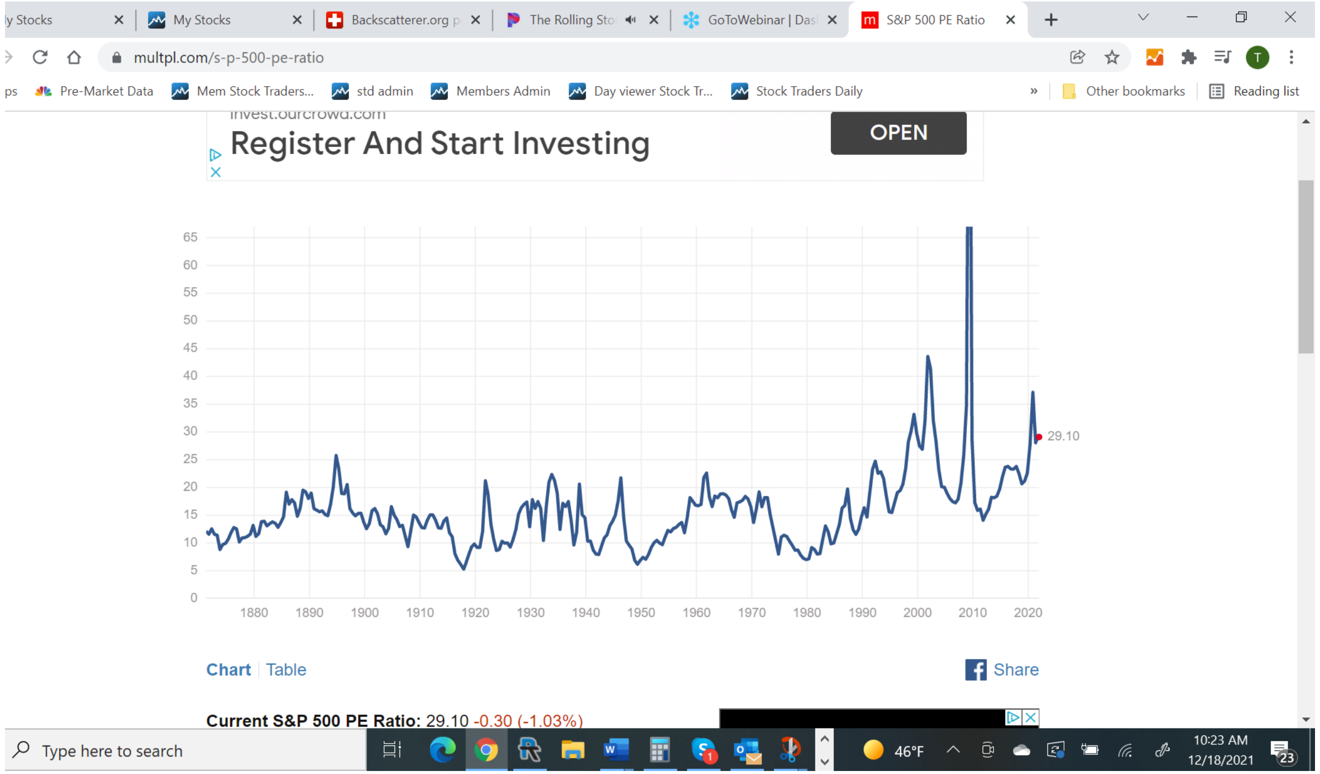
- Demand is declining extremely fast.
- Price will naturally come under pressure.

# Natural Risk Appetites will Return

**The big buyer at the other end of the table will be gone.**

- Risk appetites will revert to natural levels
- Investors will start to ask valuation questions again.
- The Trailing PE of the SPX is near 29x, forward near 26x.
- Historical avg. PE more like 15x

# Interest Rates and Multiples




- Market Interest Rates are likely to increase as risk perceptions increase.
- Market Multiples are likely to retreat from near 29x to even 2010 levels.
- In 2010 the multiple on the SPX was 15-20x.
- Multiple contraction will take time.

# Recent FOMC Monetary Policy Commentary

*From the Dec 2021 press conference*

Powell now seems to think monetary + fiscal policies have done too much.

Powell said higher asset prices are keeping people from seeking employment.

Powell may think that a drawdown in asset purchases would help employment.

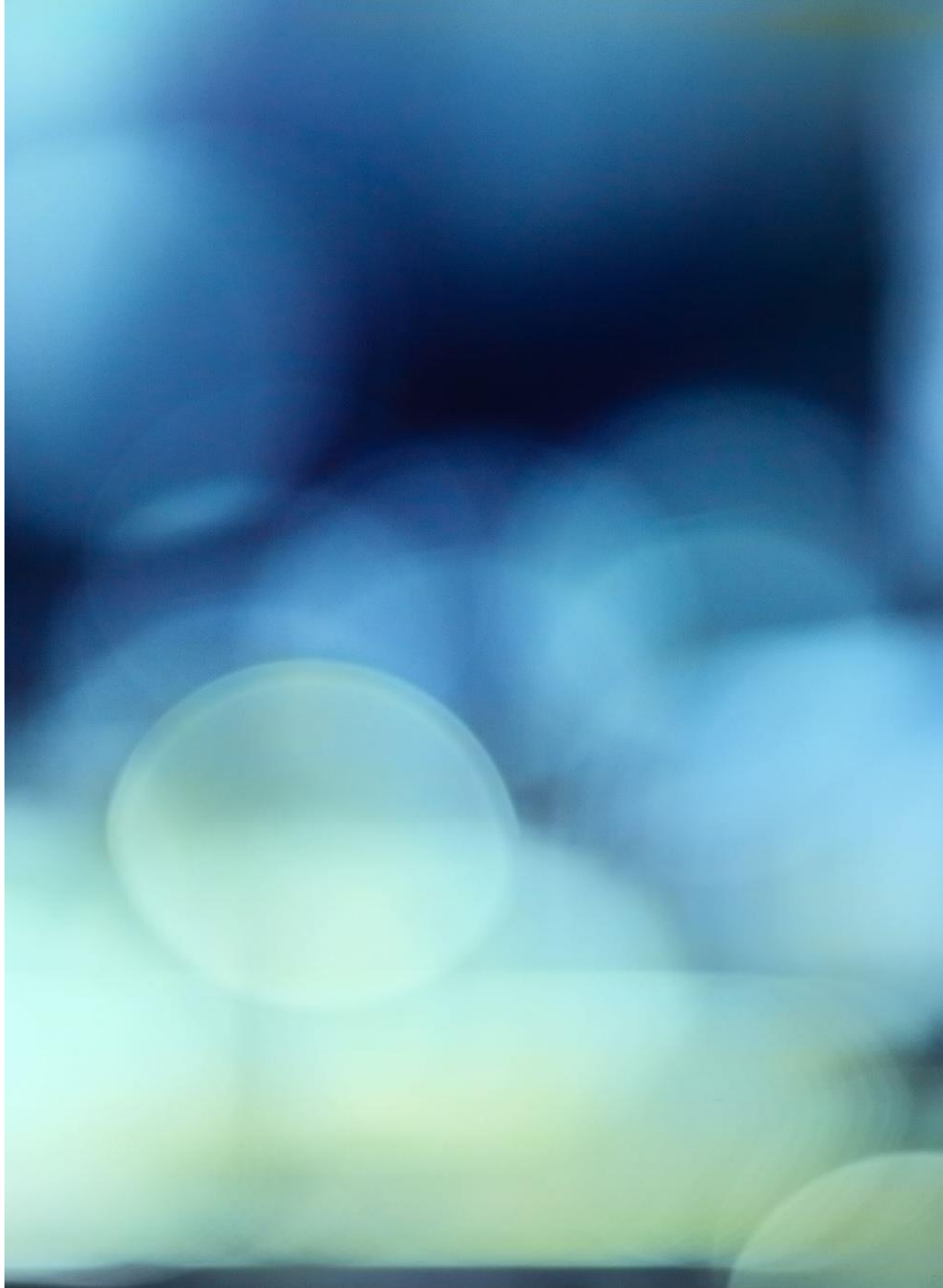
Especially if asset prices come down enough to get people working.

# $2.41 Trillion of annualized demand is being removed over the next 12 months, most of it in 3.

RISK APPETITES ARE LIKELY TO DECLINE.

MULTIPLES WILL LIKELY DECLINE.

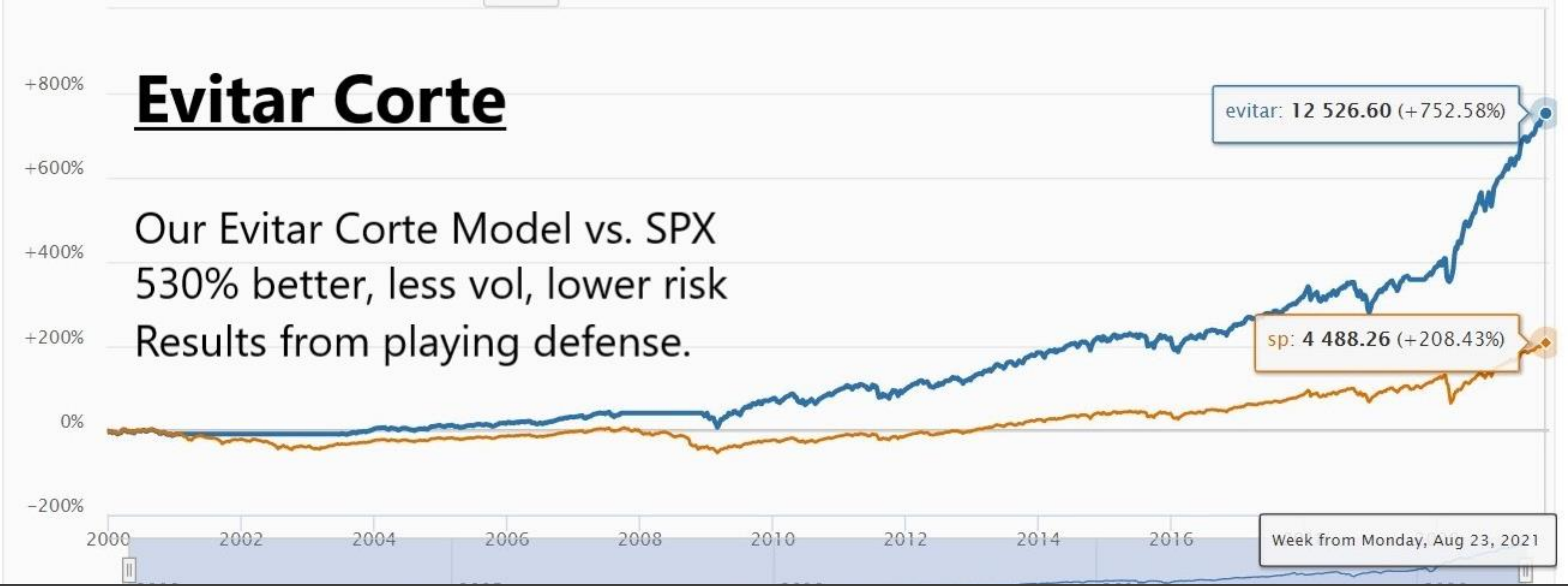
VALUATION WILL MATTER AGAIN



# No asset class will be sheltered

Everything benefitted from stimulus, and all asset prices will be affected as stimulus comes down.

Stocks, Bonds, Real Estate, Private Business




## No Crash

- Our Evitar Corte Model is not signaling a crash
- It has a remarkable history of pinpointing crashes before they happen.
- We use Evitar as a Model
- As a Managed account strategy
- As an overlay for existing taxable portfolios with large cap gains tax issues.

# 6 Months of Solid Stimulus

- 2017-Like stimulus is likely until Q3 2022.
- In Q1 that will be much higher.
- Stimulus is not cut off right now.
- The existence will bring buyers.
- But Stimulus has an end date
- The end date is about 12 months away.

# Not Yet 2018-like conditions

- Investors remember the volatility that existed in 2018
- 2018 is when stimulus stopped last time
- Eventually this will matter again
- But a no-stimulus environment is far away
- We are heading that way, but we are far from there.

# A New Breed of Piggybackers?

The definition of piggybackers is one who tries to get ahead of Central Bank action.

If the Central Banks are cutting asset purchases, a new breed may surface.

The New Breed of piggybackers may anticipate 2018-like conditions, and volatility


# Wall Street Knows What is Coming

- Wall Street anticipates volatility
- But they do not expect one-sided action.
- Volatility can exist in both directions (up and down)
- Stimulus is still robust, but the writing is on the wall.

CORE was designed for this, to offer a low-volatility risk-controlled alternative to buy and hold.

# Options

Volatility + No Crash =

Our CORE Portfolio Strategy

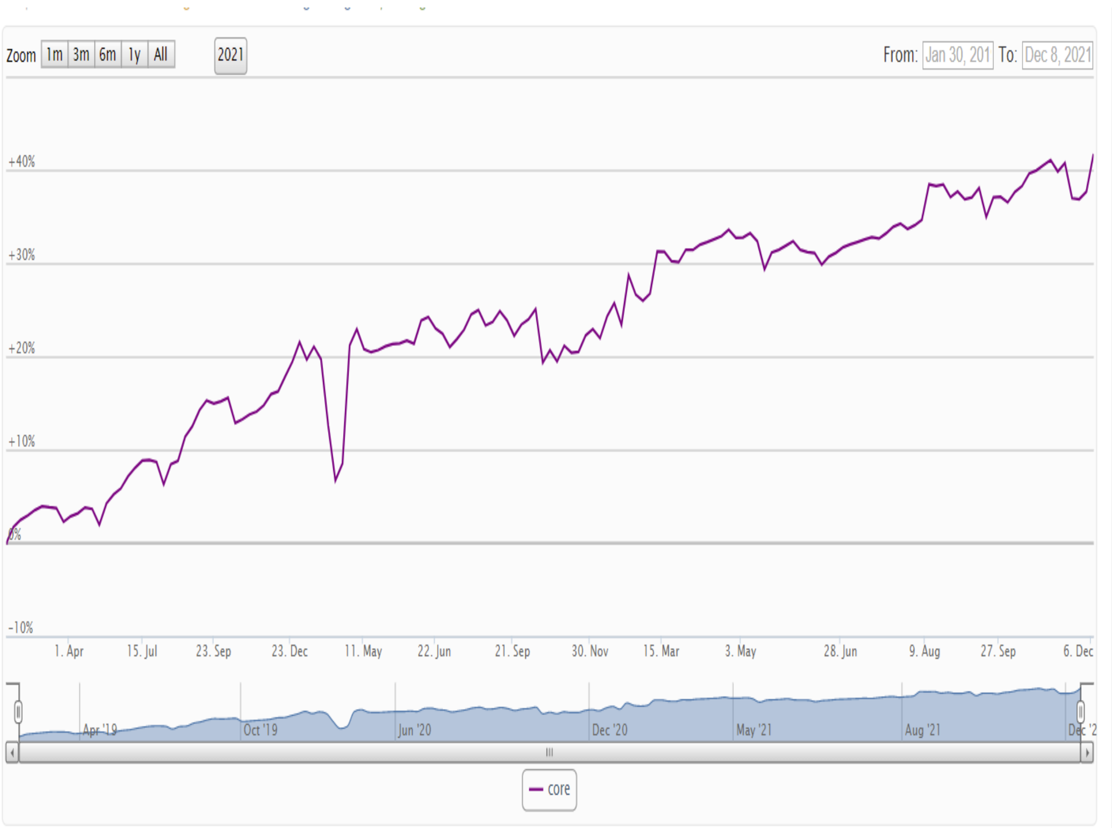
Our Evitar Corte Strategy

A combination of both.

# CORE Portfolio Strategy + Scalable

- CORE was designed specifically for the no-stimulus environment that developed in 2018.
- It is a risk-controlled alternative to buy and hold.
- CORE spends 50% of the time neutralized from market risk.
- Taxable and tax-free versions are available.
- 34 Sortino ratio in 2019; Great Risk Profile
- Protected from the Corona crash in 2020
- Slow but steady, seeks 8% per year, has been averaging 13%.
- CORE was built for the market that lays ahead too.

# CORE was Built For What is Coming

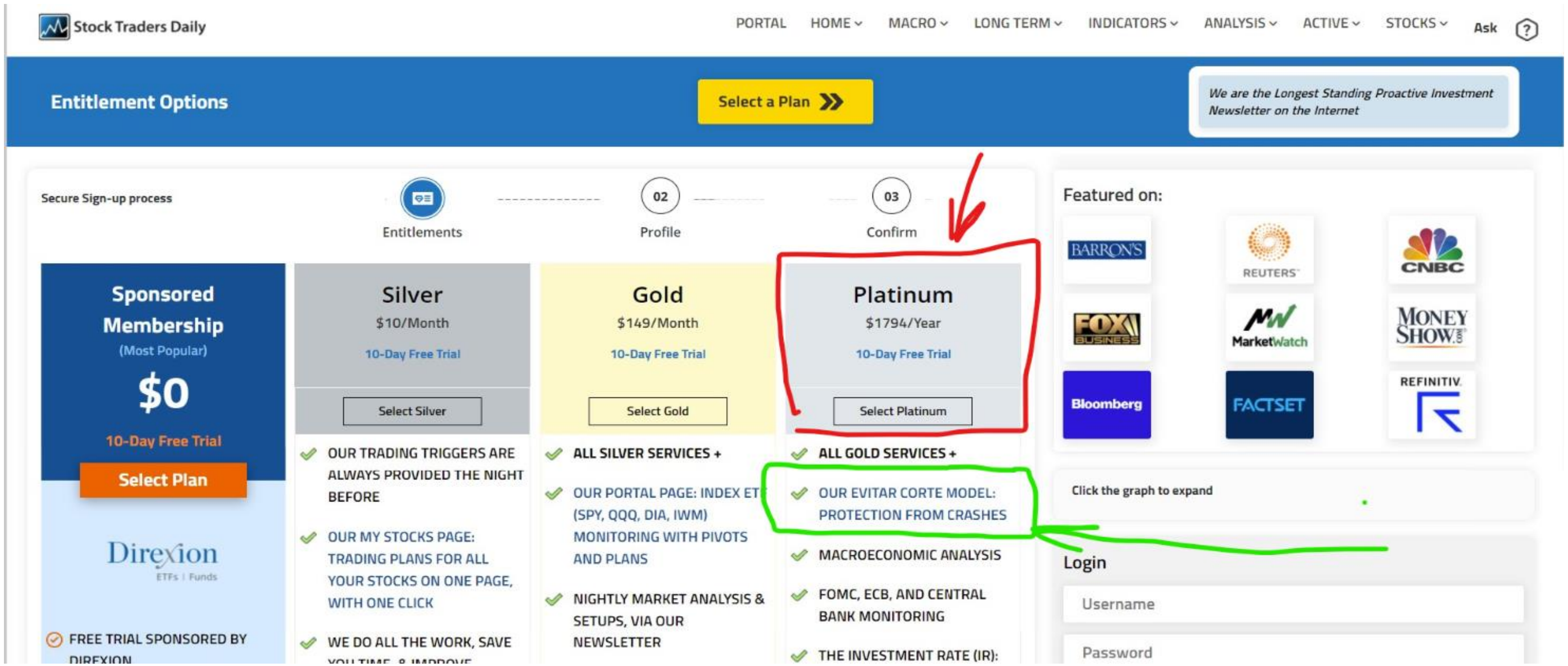
# Evitar Corte – Protect from Crashes

- The Model Warns of Crashes before they happen
- The Strategy reacts to the signals from Evitar Corte in real time
- Evitar Corte uses the FOMC’s Monetary Policy as a crash indicator
- Evitar Corte does NOT try to reduce periodic volatility
- Evitar Corte ONLY helps prevent from crashes.
- Evitar Corte identified the Internet Debacle Before it happened
- It Identified the Credit Crisis and the period of time in 2019 when overnight lending spiked to 8%
- And Evitar Corte identified the Corona Crash too, before the declines got severe.

# Evitar Corte: Defense Wins Championships



# CORE + Evitar Corte




# Platinum Subscribers are Entitled

www.StockTradersDaily.com