

# A 10,000ft View

Date: 2021-12-31

*“It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of light, it was the season of darkness, it was the spring of hope, it was the winter of despair.” – Charles Dickens, A Tale of Two Cities*

## What to expect in 2022: some big-picture charts

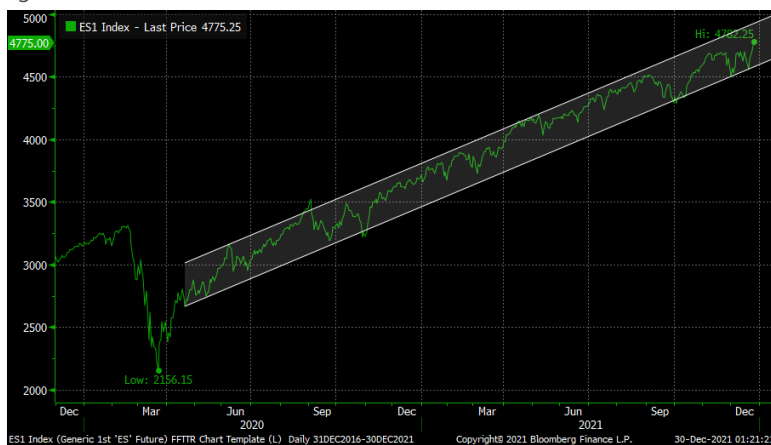
Like many people, we are utterly amazed by how fast 2021 has passed. It felt like not long ago that the whole world was taken aghast by the rapid outbreak of COVID-19. That was only 2020. In 2021 we saw staggering economic recoveries from one of the deepest yet shortest recessions in human history, largely thanks to the global central banks going all out to provide liquidity and stimulus to the economy.

2021 was the story of dichotomy. We witnessed abundant liquidity in the financial system but decreasing affordability in daily necessities from food and energy to shelter. We saw real rates at the most negative level since the 1970s due to extremely accommodative policy rates combined with high inflation. Yet, the two biggest central banks, the Fed and the ECB, seem to be reluctant to normalize interest rates too soon to contain inflation, fearing it may jeopardize economic recovery. We saw broad market speculation by retail investors in meme stocks and cryptocurrencies. Yet, the market breadth continues to deteriorate, indicated by the underperformance of small caps against the handful of big tech names. We saw countries and regulators getting more vocal about “Going Green” to save our planet. Yet, we face one of the most severe energy shortages, especially in Europe. We saw the emergence of revolutionary technologies, like Web 3.0 and the metaverse, which will shape how we interact with each other and bring us closer to one another, or so we were told.

The list goes on. We live in a world with growing divergence and polarization. Could the dichotomy be the “new norm” that we need to adapt to in 2022 and beyond?

Why don’t we dedicate the 1<sup>st</sup> issue of 2022 to a non-biased, 10,000ft view of the financial market, and let the longer-term price actions speak for themselves? As we usher in 2022, here’s wishing all our readers an amazing and rewarding new year, rain or shine.

Figure 1 Generic 1<sup>st</sup> E-mini S&P 500 Future



Since the V-shape rebound in March and April 2020, the S&P 500 index has been going higher in a perfect channel. Every dip along the way was relentlessly bought, and shortly after, another all-time high was made. Rinse and repeat. It would take a sizable event for this very resilient equity market to trip over.

Figure 2 S&P 500 Index vs. Federal Reserve Balance Sheet



In the midst of the 2008 Great Financial Crisis, the Fed started Quantitative Easing. Since then, we can see that when the Fed's balance sheet was expanding, the equity market generally enjoyed smooth rallies. However, when the Fed's balance sheet stopped expanding, the equity market experienced notable increases in volatility. Watch out because tapering will be at full speed in the coming months.

Figure 3 Generic 1<sup>st</sup> Nikkei Future



The Japanese stock market spent the entire 2021 consolidating in a tight range between 27000 and 30000. We are willing to go either way when the index breaks out from the range.

Figure 4 US 10-year Yield



Driven by higher inflation expectations, the US 10-year yield has climbed to one standard deviation (s.d.) above the regression line. North of 2% would be something to watch, as it starts to challenge the multi-decade deflationary trend.

Figure 5 US 2-year Yield



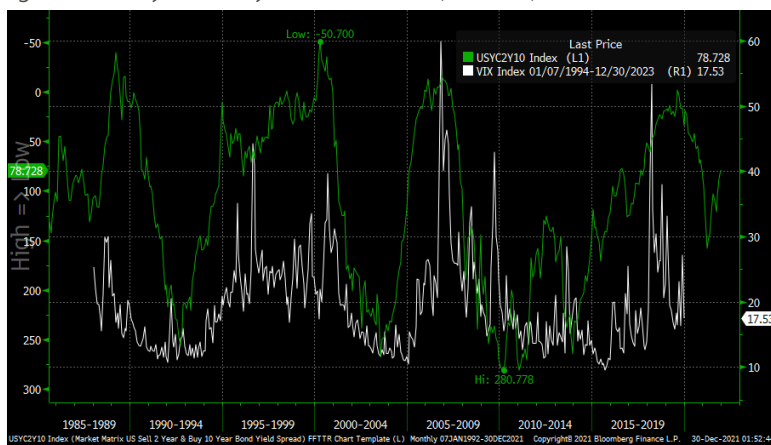
In the past few rate hike cycles, the US 2-year yield always went beyond one s.d. above the regression line, sometimes reaching two s.d. We could see the 2-year yield well above 1.5% if that holds this time.

Figure 6 US 2-year / 10-year Yield Curve



The US 2-year / 10-year yield curve flattened substantially as the 2-year yield rose much more than the 10-year yield. The past few economic cycles always saw the curve steepening to more than 200bps after inversion. Could this time be a much-truncated move, or is it just a pause before the curve steepens further?

Figure 7 US 2-year / 10-year Yield Curve (inverted) vs. VIX



The US 2-year / 10-year yield curve (inverted) leads the volatility index by about two years with remarkable consistency. If history is any guide, we could be seeing heightened equity volatility in the coming year. It also agrees with our observation in Figure 2.

Figure 8 Bloomberg US Dollar Spot Index



The US Dollar is one of the most important things we are watching. However, it has been trading sideways for more than half a decade, bounded by well-established tops and bottoms of the range. A stable US Dollar is generally favorable to risk assets.

Figure 9 USD/JPY Spot



The USD/JPY almost became a forgotten pair as it traded in a tight range near the apex of the giant triangle for years. However, in 2021 it finally broke out from the triangle and challenged the significant resistance level at 115. The interest rate differentials between the US and Japan could explain Yen's weakening against the US Dollar.

Figure 10 USD/CNH Spot



While most countries are on the path of tapering or tightening their monetary policies, China, on the other hand, is entering another easing cycle. The policy divergence makes USD/CNH a great risk/reward hedge in the portfolio against potential risk-off events.

Figure 11 EUR/USD Spot



The Euro has broken out from a decade-long downtrend. Recent Fed's hawkish pivot and a stronger US Dollar were headwinds for the Euro and brought it back down to retest the trendline.

Figure 12 Generic 1<sup>st</sup> Gold Future



We continue to observe the resemblance of Gold's price action to that in 2011 and 2012. Although the real rates are deeply negative now, Gold failed to fulfill the role of the "inflation hedge," which is believed by many people to be one of the most important characteristics of Gold. This could be due to the hawkish Fed, the strong US Dollar, and the risk-on sentiment of the broad market participants.

Figure 13 Generic 1<sup>st</sup> Copper Future



Copper's price action also displays quite a striking resemblance to the post-GFC period. We saw sharp selloffs in recessions and equally sharp reversals when the economy started to recover. This time, due to the potential manifold increase in demand from electric vehicles, we could see Copper continue its rally after the consolidation is over.

Figure 14 Generic 2<sup>nd</sup> WTI Crude Oil Future



We've been bullish on Crude Oil for more than half a year, and it hasn't changed the slightest. After some shallow pullbacks due to Omicron fears, the WTI Crude Oil is again challenging the 75 resistance level, breaking of which would potentially lead Oil to 100 next year.

Figure 15 CRB Raw Industrials Spot Price Index



The CRB Raw Industrials Spot Price Index measures a group of basic industrial commodities which are among the first to be influenced by economic condition changes. This index has already surpassed the previous high in 2011.

Figure 16 CRB Foodstuffs Spot Price Index



The CRB Foodstuffs Spot Price Index includes commodities such as agriculture and livestock. This index slightly lags the Raw Industrials index and is still trying to break out from the previous high established in 2011. 2022 should see Foodstuffs relatively outperforming the Raw Industrials as the jump in fertilizer prices gets transmitted into foodstuffs.

Figure 17 Generic 1<sup>st</sup> EU Carbon Allowance Future



The EU Carbon Emission Allowance price went from 10 EUR a few years ago to more than 80 EUR now, forcing European companies to reduce carbon dioxide emissions. Unfortunately, it also substantially increased the total costs of companies such as electricity producers, which in turn had to raise prices for the consumers, further worsening the energy shortage in Europe.

Figure 18 Global X Uranium ETF



Facing the energy shortages and aggressive campaigns to abandon fossil fuels and embrace renewable energy, Uranium finally woke up from a six-year bottoming process. Many scientists advocate that nuclear power is one of the greenest and safest energy sources to meet our insatiable energy need. The long-term chart suggests that the Uranium price will go nuclear (pun intended) in 2022.

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## Background

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**Inspirante Trading Solutions Pte Ltd** (“ITS”) was incorporated in Singapore in July 2020. Founded by the partners of Synergy Link Capital Pte Ltd (“SLC”) to consolidate their initiatives in FinTech solutions, research, and training programs for different market participants, while SLC continues its focus in proprietary trading. ITS focuses on providing clients bespoke trading solutions such as algo trading systems, risk management systems, research reports, education, and training courses. With a strong technical background, unparalleled understanding, and insights from the actual market practitioners, ITS managed to obtain FinTech certification recognized by the Monetary Authority of Singapore within two months of incorporation. ITS is now actively collaborating with various trading groups, exchanges, and brokers in multiple countries.

The trainers and researchers in ITS have been regularly speaking on various exchange/broker hosted trading seminars and writing for various research publications over the years. Catering to both aspiring and experienced traders, we want to help in bridging the void between the theoretical and practical aspects of derivative trading, with guidance from our team of seasoned and active traders.

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