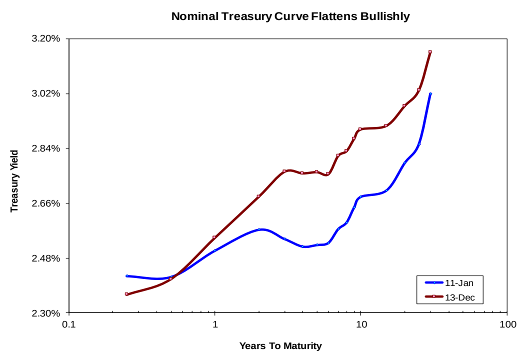
The Macro Environment For Financial Markets

While markets have rebounded following the dreadful December selloff, let's remember positive returns depend on human actions such as the Federal Reserve pausing in its rate cuts, the U.S. and China trying to negotiate a trade deal and petroleum producers adhering to production cuts. Trading by hope is a dangerous activity. The causal chain now is:

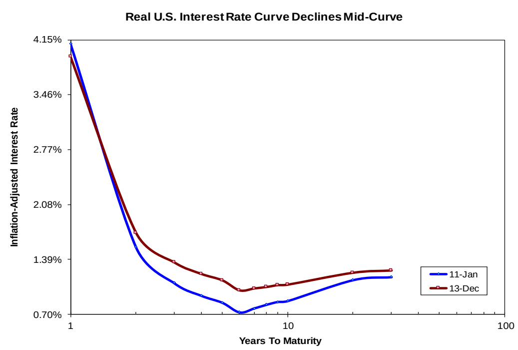
1. The market has priced out a 2019 rate hike;
2. The yield curve is flattening once again;
3. Inflationary expectations have moved back to their December breakdown point;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing in the bond market;
5. Swap spreads remain inverted; and
6. CDS costs are declining from their December highs.

Key Market Indications

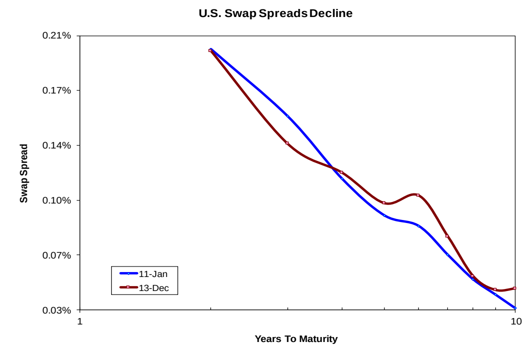
Treasuries remain a reactive market. Yields once again are moving higher on risk-on days even though the risk-on sentiment remains fragile.



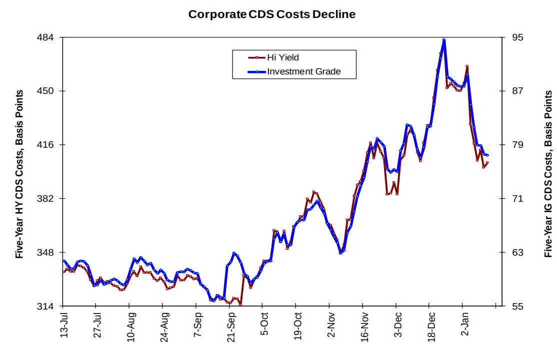
The pseudo-real yield curve continues to shift lower mid-curve but remains elevated at the shortest maturities.



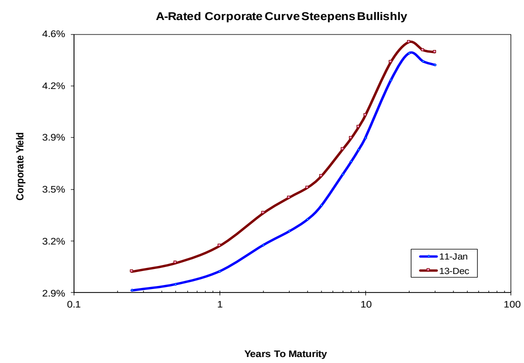
Swap spreads, which rise when floating-rate borrowers want to fix their payments, rose at two- and three-year tenors but remain under downward pressure at longer tenors as the market continues to assess whether the Federal Reserve will resume its rate hike campaign later in 2019.



CDS costs have relinked to the equity market as correlation trades fade. We remain unlikely to revisit the lows from early autumn anytime soon.



The A-rated corporate yield curve is starting to steepen bullishly as some immediate threats to corporate credit quality, such as higher short-term rates and plunging crude oil prices, have ceased for now.



Market Structure

Industrial Metals and Natural Gas remain in downtrends while Petroleum moved into a structural uptrend amongst physical markets. All of the equity indices and ten-year UST exited structural trends in response to their sharp reversals and high volatility levels.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Jan. 14 - 18
BBerg	24	Trending	0.122	10.4%	
BBerg Grain	29	Trending	-0.016	10.0%	
BBerg Ind. Metl	29	Trending	-0.051	12.3%	-0.29%
BBerg Pre. Metl	4	Sideways	0.003	8.5%	
BBerg Softs	26	Trending	0.059	16.5%	
BBerg Nat. Gas	23	Trending	-0.009	23.0%	-0.17%
BBerg Petroleum	21	Trending	0.148	39.0%	0.66%
BBerg Livestock	18	Transitional	-0.047	7.5%	
Dollar Index	28	Trending	-0.160	6.1%	-0.13%
S&P 500 Index	29	Trending	0.033	23.0%	
EAFE Index	29	Trending	0.153	13.3%	
EM Index	29	Trending	0.224	11.7%	
Ten-year UST (price)	6	Sideways	0.010	5.3%	

Performance Measures

The Petroleum complex continued to gain strongly on production cuts, although this is a story with a known ending. Action elsewhere was lackluster. This will remain a bearish asset class for as long as Chinese growth remains under pressure.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	1.41%	-1.79%	-3.90%	-8.43%
Grains Sub-Index	-0.73%	-1.27%	3.35%	-2.89%
Corn	-1.02%	-1.50%	4.78%	-2.48%
Soybeans	-1.49%	-0.20%	7.08%	-10.08%
Wheat	0.56%	-1.80%	-0.25%	8.57%
Energy Sub-Index	4.98%	-6.23%	-11.58%	-8.51%
Petroleum Sub-Index	5.81%	0.41%	-20.42%	-13.11%
WTI	6.36%	0.48%	-24.09%	-15.01%
Brent	5.51%	0.31%	-18.34%	-8.41%
ULSD	5.70%	2.51%	-11.17%	-7.05%
Gasoline	4.75%	-2.45%	-26.72%	-24.62%
Natural Gas	3.48%	-18.17%	13.14%	0.19%
Precious Metals Sub-Index	-0.14%	4.74%	2.49%	-5.30%
Gold	0.00%	4.07%	3.65%	-4.04%
Silver	-0.61%	7.16%	-1.38%	-9.48%
Industrial Metals Sub-Index	0.16%	-2.26%	-7.44%	-16.78%
Copper	0.98%	-3.46%	-4.32%	-18.27%
Aluminum	-2.48%	-4.36%	-8.98%	-15.03%
Nickel	2.77%	3.42%	-18.09%	-10.07%
Zinc	-0.29%	-1.55%	1.02%	-21.94%
Softs Sub-Index	3.97%	-1.66%	-4.88%	-17.34%
Coffee	1.10%	1.76%	-10.05%	-22.61%
Sugar	1.05%	1.22%	10.27%	-16.02%
Cotton	-0.33%	-8.76%	-18.35%	-10.39%
Livestock Sub-Index	1.82%	1.23%	9.18%	2.58%
Cattle	1.66%	2.49%	10.24%	7.26%
Hogs	2.24%	-1.72%	6.71%	-6.77%

The USD declined against all but the SEK, INR and CHF as the market is pricing out higher short-term interest rates in the U.S. in 2019. The strong rallies in the Latin American currencies are likely to fade at the first sign of equity market weakness.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	0.03%	1.51%	-2.00%	-6.42%
Chinese yuan	1.63%	2.47%	-0.74%	-4.51%
Japanese yen	0.45%	4.77%	3.75%	2.13%
British pound	0.64%	2.19%	-2.84%	-6.76%
Swiss franc	-0.34%	1.53%	1.40%	-2.02%
Canadian dollar	0.31%	0.95%	-0.92%	-6.25%
Australian dollar	0.88%	0.54%	-2.80%	-9.47%
Swedish krona	-0.36%	1.48%	-1.18%	-10.15%
Norwegian krone	0.00%	0.98%	-5.05%	-7.61%
New Zealand dollar	1.07%	0.44%	0.74%	-6.48%
Indian rupee	-1.08%	1.93%	-2.44%	-9.69%
Brazilian real	0.05%	5.03%	4.38%	-13.44%
Mexican peso	1.10%	5.67%	-1.73%	-1.54%
Chilean peso	1.15%	1.22%	-3.17%	-10.14%
Colombian peso	1.26%	1.07%	-8.24%	-9.39%
Bloomberg-JP Morgan Asian dollar index (spot)	0.51%	1.78%	-0.20%	-3.92%

Global equities continued their strong rebound from the December selloff, led by emerging markets. The easy money has been made in what is likely a bear market rally.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	1.99%	0.90%	-7.36%	-8.20%
North America	2.78%	0.29%	-6.76%	-5.29%
Latin America	2.94%	12.41%	12.46%	-1.68%
Emerging Market Free	3.77%	3.35%	-5.84%	-14.76%
EAFE	2.89%	2.06%	-8.46%	-13.17%
Pacific	1.97%	2.06%	-6.04%	-11.50%
Eurozone	1.48%	0.97%	-12.29%	-16.95%

CTAs had one of their worst weeks in recent memory, which is somewhat surprising given their recent adroit trading during periods of high volatility. Global hedge funds gained on the week.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
SocGen CTA	-4.67%	-2.78%	-7.39%	-13.93%
SocGen Trend	-3.20%	-1.65%	-4.05%	-10.31%
SocGen Short-Term	-1.89%	-1.16%	-1.68%	-2.89%
HFR Global Hedge Fund	0.74%	0.58%	-5.44%	-6.69%
HFR Macro/CTA	-2.05%	-2.06%	-4.92%	-7.90%
HFR Macro: Sytematic Diversified CTA	-2.51%	-2.17%	-5.83%	-10.64%