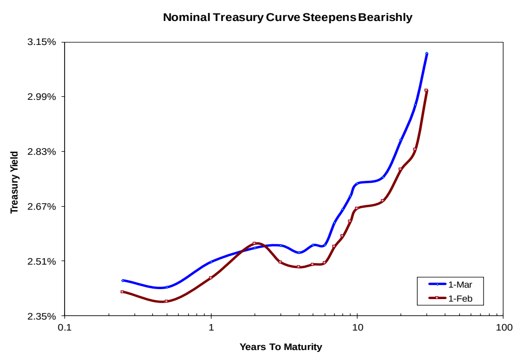
The Macro Environment For Financial Markets

One day future economists will marvel over the debate about "modern monetary theory," the notion deficits do not matter for countries that borrow in their own currency. A better would restatement would be to add, "They do not matter until the moment they do." When the point of rising debt service arrives, growth will slow as current consumption will have to be diverted into future consumption via higher savings. To debate this is to debate the wind or the law gravity. The causal chain now is:

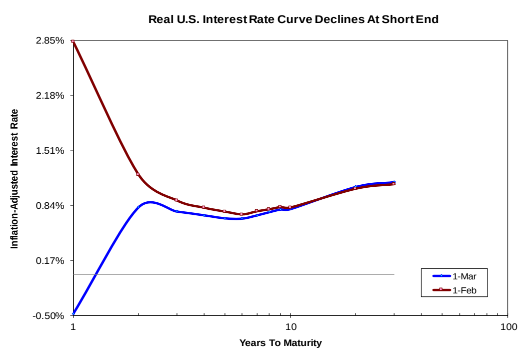
1. The market has priced out a 2019 rate hike;
2. The yield curve is holding its positive slope;
3. Inflationary expectations are rising;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing in the bond market;
5. Swap spreads are declining; and
6. CDS costs are declining once again.

Key Market Indications

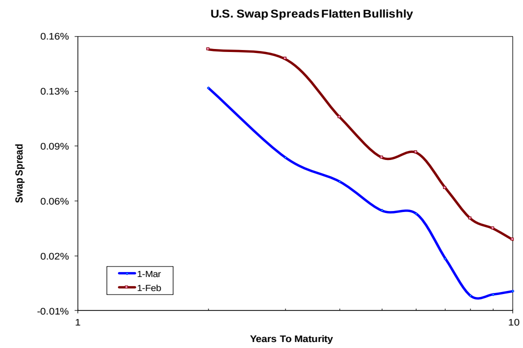
The rally in UST has failed for the time being as the market is interpreting the Federal Reserve's dovish shift as being excessive. In addition, the increasing likelihood of a trade truce with China removes a recessionary risk.



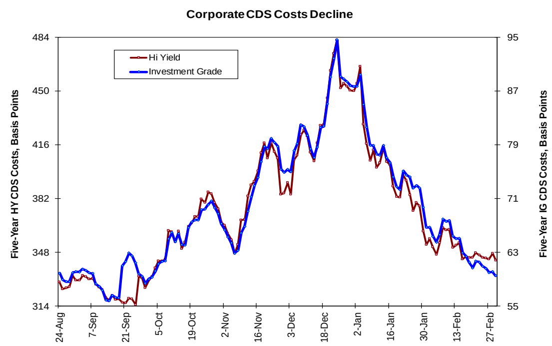
The pseudo-real yield curve declined rapidly at the short end of the yield curve, as expectations for tighter monetary policy dissipate. However, longer-maturity implied real rates have stopped declining. This removes one of the recent boosts for risky assets.



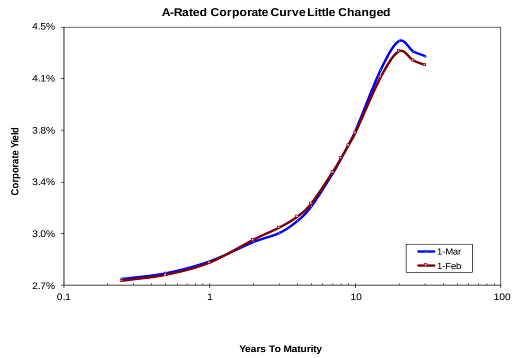
Swap spreads, which rise when floating-rate borrowers want to fix their payments, have declined across all tenors. The market is complacent about higher credit spreads and interest rate shifts.



CDS costs have resumed their decline as prospects for tame monetary policy, no trade hostilities and more stable commodity prices have combined with a form of the TINA argument: In fixed-income, everything is better than sovereign debt.



Corporate bonds continue to rally as recession risk is being priced out of the market and the Federal Reserve appears content to remain on the sidelines.



Market Structure

Grains and Softs are the only physical markets to remain in structural downtrends, while both Petroleum and Natural Gas are in structural uptrends. All of the equity indices have moved into bullish consolidations, while ten-year UST have reversed into a downtrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Mar. 4 - 8
BBerg	16	Transitional	0.012	8.0%	
BBerg Grain	29	Trending	-0.336	12.1%	-0.12%
BBerg Ind. Metl	15	Transitional	0.222	10.9%	
BBerg Pre. Metl	15	Transitional	-0.292	7.5%	
BBerg Softs	29	Trending	-0.144	13.0%	-0.41%
BBerg Nat. Gas	24	Trending	0.208	19.5%	0.55%
BBerg Petroleum	29	Trending	0.112	23.8%	0.96%
BBerg Livestock	16	Transitional	0.066	8.6%	
Dollar Index	29	Trending	0.053	4.4%	0.12%
S&P 500 Index	4	Sideways	0.057	6.3%	
EAFE Index	4	Sideways	0.006	7.5%	
EM Index	15	Transitional	0.043	8.3%	
Ten-year UST (price)	28	Trending	-0.141	3.7%	-0.04%

Performance Measures

Those who persist in regarding physical commodities as investment assets as opposed to process inputs should observe the strong declines in Grains, Petroleum and Precious Metals in a rising risk-acceptance and lower short-term implied real rate environment. What had seemed like a set of markets linked to equities resumed trading on a set of weaker fundamentals.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-1.36%	0.00%	-1.47%	-6.17%
Grains Sub-Index	-3.19%	-5.74%	-4.74%	-17.50%
Corn	-2.94%	-3.52%	-2.65%	-13.50%
Soybeans	-1.28%	-2.12%	4.37%	-19.52%
Wheat	-6.97%	-13.34%	-15.14%	-17.78%
Energy Sub-Index	-1.06%	4.26%	-10.64%	2.76%
Petroleum Sub-Index	-2.56%	3.80%	-17.28%	-0.70%
WTI	-2.66%	1.48%	-19.99%	-5.57%
Brent	-3.20%	4.15%	-15.95%	5.05%
ULSD	-1.58%	5.27%	-9.51%	9.57%
Gasoline	-2.10%	7.03%	-22.61%	-12.00%
Natural Gas	3.82%	5.66%	4.71%	6.31%
Precious Metals Sub-Index	-3.00%	-2.09%	8.16%	-3.84%
Gold	-2.48%	-1.36%	8.51%	-2.50%
Silver	-4.68%	-4.40%	7.23%	-8.17%
Industrial Metals Sub-Index	0.55%	1.76%	7.15%	-7.30%
Copper	-0.50%	4.85%	13.03%	-6.80%
Aluminum	0.22%	-0.24%	-7.03%	-8.82%
Nickel	1.56%	-0.57%	5.77%	-2.07%
Zinc	2.48%	-0.29%	20.12%	-11.59%
Softs Sub-Index	-2.03%	-1.85%	0.19%	-17.49%
Coffee	0.25%	-7.79%	-6.14%	-26.19%
Sugar	-5.07%	-0.66%	13.30%	-11.78%
Cotton	1.20%	-0.11%	-13.25%	-9.42%
Livestock Sub-Index	0.90%	-1.70%	5.94%	0.55%
Cattle	0.57%	2.18%	10.50%	7.67%
Hogs	1.76%	-10.40%	-3.31%	-14.11%

To repeat verbatim from last week, the USD has been trading without an overarching theme so far in 2019. All we can say with any certainty is dovish U.S. policies have precluded a strong rally. We also can say this period of low volatility cannot last indefinitely.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	0.26%	-0.79%	-2.19%	-7.35%
Chinese yuan	0.11%	0.58%	1.74%	-5.19%
Japanese yen	-1.07%	-2.14%	-0.73%	-5.05%
British pound	1.14%	0.94%	2.58%	-4.17%
Swiss franc	0.11%	-0.37%	-3.00%	-5.75%
Canadian dollar	-1.22%	-1.47%	-1.52%	-3.46%
Australian dollar	-0.70%	-2.36%	-1.87%	-8.73%
Swedish krona	0.83%	-2.36%	-1.86%	-11.01%
Norwegian krone	0.37%	-1.66%	-2.64%	-8.56%
New Zealand dollar	-0.67%	-1.45%	3.01%	-6.19%
Indian rupee	0.32%	0.49%	0.44%	-8.10%
Brazilian real	-0.84%	-3.22%	10.05%	-13.95%
Mexican peso	-0.66%	-0.86%	-0.46%	-2.18%
Chilean peso	-1.13%	-0.97%	3.99%	-9.61%
Colombian peso	0.31%	-0.18%	-1.61%	-7.03%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.31%	-0.02%	1.09%	-4.21%

Equity markets feel more bullish than results indicate; perhaps this is because the equity is climbing a wall of disbelief. However, the declines in the EM index are a signal the rest of the world is not on as solid of a basis as is the U.S.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	0.52%	3.10%	-2.05%	2.85%
North America	0.49%	3.16%	-2.06%	6.27%
Latin America	-4.26%	-5.31%	14.63%	-6.22%
Emerging Market Free	-0.65%	0.47%	2.03%	-8.49%
EAFE	0.58%	2.99%	-2.04%	-3.15%
Pacific	-0.48%	1.68%	-2.37%	-4.93%
Eurozone	1.72%	4.16%	-2.73%	-5.39%

CTAs continued their losing ways as the energy markets turned sideways and currencies remain choppy. Hedge funds are struggling as well during a period of risk-on in financial markets. This is getting very hard to justify.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
SocGen CTA	-0.26%	1.02%	-7.06%	-6.88%
SocGen Trend	-0.21%	0.62%	-3.74%	-4.65%
SocGen Short-Term	-0.40%	-0.92%	-3.00%	-3.81%
HFR Global Hedge Fund	-0.02%	1.05%	-3.57%	-4.10%
HFR Macro/CTA	0.04%	1.56%	-2.90%	-3.17%
HFR Macro: Sytematic Diversified CTA	-0.55%	0.79%	-4.79%	-4.72%