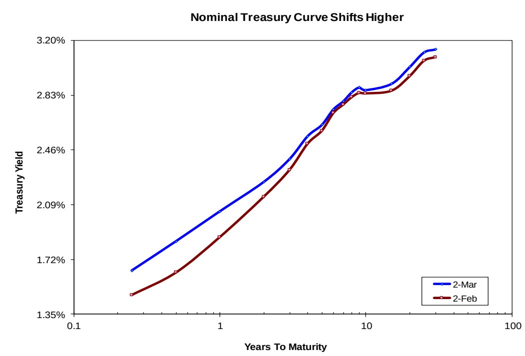
The Macro Environment For Financial Markets

As a rule, it is best to exclude politics from market discussions, but sometimes we have no choice. The idea of tariffs on steel and aluminum is both dangerous and ineffective; it risks both higher consumer costs and a shield for American industries to forestall modernization. It is worse for exporters to the U.S. If we combine this with the removal of monetary stimulus globally and high levels of deficit spending, we have the recipe to ruin a very strong economy and to take markets down as well. The causal chain now is:

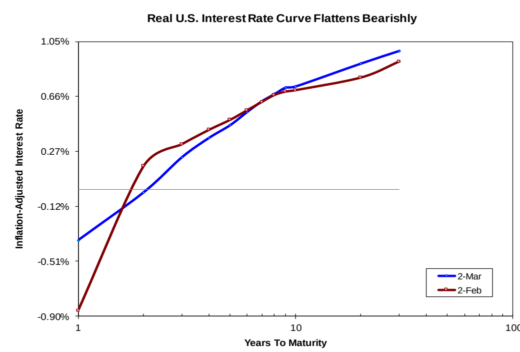
1. The market is pricing in March and June 2018 rate hikes;
2. Inflationary expectations are on pace to reach their next target of 2.26% for the ten-year;
3. The yield curve is drifting back toward a bullish flattening;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing in the bond market;
5. Swap spreads continue to invert bullishly; and
6. CDS costs continue to reflect equity market fluctuations more than credit market conditions.

Key Market Indications

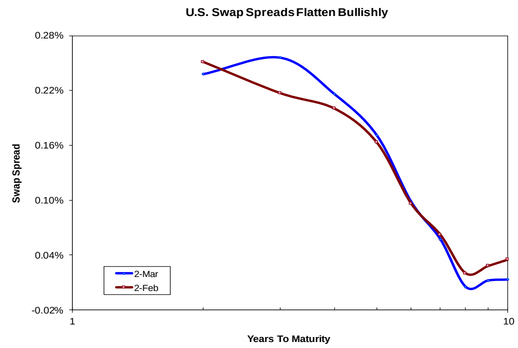
Not only have ten-year UST failed to test their resistance at 3.05%, the recent bearish steepening of the yield curve is returning to what had been a four-year+ bullish flattening trend. However, as much of this is a reaction to the unsettled nature of global equity markets, it is premature to declare we are reentering the secular bull market in bonds.



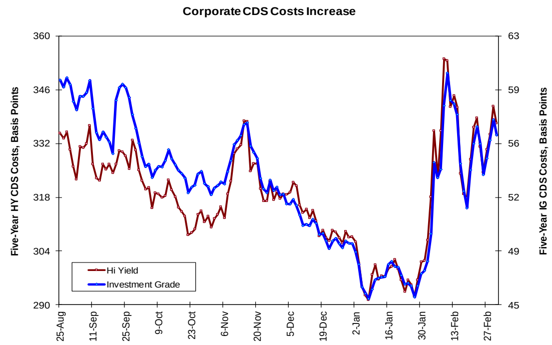
The pseudo-real yield curve shifted higher at the short and long ends of the yield curve. This combination is negative for both long-duration capital assets and for short-dated inflation hedges.



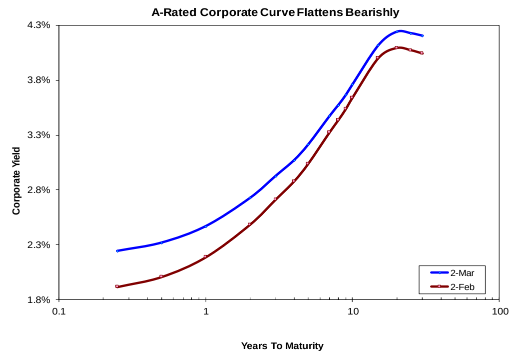
Swap spreads, which rise when floating-rate borrowers want to fix their payments, rose through five years and declined thereafter. This inversion was common during bonds' recently concluded bull market.



CDS costs continue to reflect movements in equities as correlation trades between stock options and CDS dominate individual issues' credit concerns.



The A-rated corporate yield curve continues to flatten bearishly. However, the overall risk/reward profile of the market has benefited from the combination of higher UST rates and tame movements in both swap spreads and credit spreads.



Market Structure

Grains are now overbought, and this has helped put the main Bloomberg index into a structural uptrend. Livestock reversed into a downtrend, joining Natural Gas. The EM index moved into a structural downtrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Mar. 5 - 9
BBerg	21	Trending	0.027	10.1%	0.13%
BBerg Grain	29	Trending	0.423	11.8%	0.22%
BBerg Ind. Metl	14	Transitional	-0.136	16.1%	
BBerg Pre. Metl	13	Transitional	-0.057	11.1%	
BBerg Softs	18	Transitional	0.035	13.5%	
BBerg Nat. Gas	29	Trending	-0.014	21.2%	-0.05%
BBerg Petroleum	12	Transitional	-0.059	22.4%	
BBerg Livestock	21	Trending	-0.166	10.0%	-0.07%
Dollar Index	12	Transitional	0.024	7.6%	
S&P 500 Index	12	Transitional	-0.067	15.9%	
EAFE Index	12	Transitional	-0.193	12.6%	
EM Index	21	Trending	-0.069	14.7%	-0.22%
Ten-year UST (price)	11	Transitional	0.027	5.0%	

Performance Measures

The Petroleum complex put in another weekly reversal, this time to the downside. There are still those who believe in this complex being a reflection of the USD despite decades of evidence to the contrary. The Grains complex, wheat in particular, moved strongly higher. The real question will be whether this can continue through the Northern Hemisphere growing season. The economically sensitive Industrial Metals turned lower, but aluminum did not as buyers scrambled to beat any tariff.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-0.58%	-0.30%	3.91%	2.23%
Grains Sub-Index	4.21%	8.36%	5.56%	-6.57%
Corn	2.90%	5.31%	2.06%	-10.62%
Soybeans	2.28%	9.37%	7.63%	-0.88%
Wheat	7.73%	10.68%	6.25%	-7.58%
Energy Sub-Index	-2.57%	-4.06%	8.81%	3.92%
Petroleum Sub-Index	-3.99%	-4.81%	19.40%	14.10%
WTI	-3.63%	-3.82%	24.79%	11.14%
Brent	-3.95%	-4.22%	24.37%	15.51%
ULSD	-4.45%	-6.32%	10.42%	16.61%
Gasoline	-4.30%	-6.39%	8.78%	13.14%
Natural Gas	1.56%	-1.94%	-19.04%	-22.68%
Precious Metals Sub-Index	-0.48%	-1.04%	-3.37%	2.92%
Gold	-0.49%	-0.87%	-1.63%	7.11%
Silver	-0.47%	-1.62%	-8.61%	-8.39%
Industrial Metals Sub-Index	-2.41%	-3.39%	3.16%	15.63%
Copper	-3.32%	-3.50%	-0.76%	13.68%
Aluminum	0.41%	-2.71%	1.60%	11.35%
Nickel	-2.29%	-2.15%	10.85%	20.94%
Zinc	-4.29%	-5.22%	8.55%	22.07%
Softs Sub-Index	0.44%	0.52%	-2.60%	-22.00%
Coffee	1.02%	0.39%	-7.90%	-22.14%
Sugar	-0.27%	-2.93%	-6.83%	-33.66%
Cotton	0.95%	5.87%	8.51%	6.88%
Livestock Sub-Index	-3.11%	-4.19%	2.32%	4.15%
Cattle	-2.11%	-2.52%	5.28%	7.45%
Hogs	-5.29%	-7.74%	-3.93%	-2.23%

The JPY once again acted as a haven currency. Only it and the NOK managed to gain against the USD as Jerome Powell once again raised the prospect of the U.S. moving to the fore in raising short-term interest rates to fight an inflation that may not exist.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	0.18%	-1.17%	3.54%	17.23%
Chinese yuan	-0.13%	-0.70%	2.92%	8.58%
Japanese yen	1.08%	4.18%	3.75%	8.19%
British pound	-1.21%	-2.24%	6.74%	12.51%
Swiss franc	-0.14%	-0.64%	2.22%	8.11%
Canadian dollar	-1.93%	-3.52%	-3.62%	3.95%
Australian dollar	-1.06%	-2.16%	-2.32%	2.48%
Swedish krona	-0.87%	-4.15%	-3.40%	10.19%
Norwegian krone	0.79%	-0.73%	0.26%	8.90%
New Zealand dollar	-0.90%	-0.88%	1.03%	2.45%
Indian rupee	-0.19%	-1.75%	-1.75%	2.55%
Brazilian real	-0.44%	-1.05%	-3.50%	-3.07%
Mexican peso	-1.42%	-1.21%	-5.05%	6.25%
Chilean peso	-1.30%	0.64%	4.24%	9.27%
Colombian peso	-0.65%	-0.78%	2.36%	4.08%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.24%	-0.58%	2.52%	6.20%

There are no winners in a trade war. The U.S. managed to lose less than did other equity markets, but this is damning with faint praise.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	-2.33%	-0.44%	7.94%	15.76%
North America	-2.01%	-2.47%	9.10%	14.79%
Latin America	-3.00%	-1.81%	6.87%	22.19%
Emerging Market Free	-2.80%	-3.84%	9.12%	29.50%
EAFE	-2.86%	-5.38%	4.41%	17.53%
Pacific	-1.68%	-2.29%	9.31%	18.56%
Eurozone	-3.16%	-4.72%	2.54%	20.70%

Both CTAs and hedge funds declined again this week. These are the markets where alternative investments are supposed to be diversifying assets, not simply another vehicle for losing money.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	-2.06%	-10.62%	-0.58%	-5.03%
Newedge Trend	-1.40%	-7.59%	-0.55%	-2.91%
Newedge Short-Term	-0.27%	-4.96%	1.78%	-0.45%
HFR Global Hedge Fund	-1.38%	-2.78%	1.63%	3.54%
HFR Macro/CTA	-1.53%	-5.89%	-0.36%	-0.35%
HFR Macro: Sytematic Diversified CTA	-2.55%	-9.23%	0.53%	-1.25%