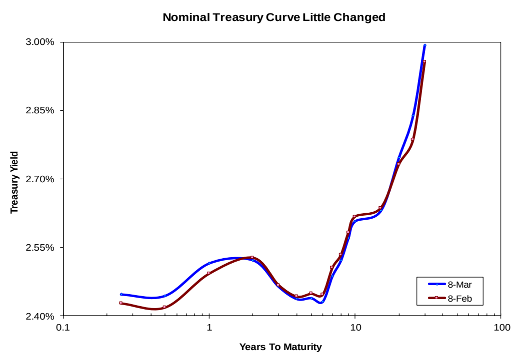
The Macro Environment For Financial Markets

One of life's mysteries is why central bank credit easing is called "stimulus" when little evidence exists it can affect the real economy as much as it does financial asset valuations. The European Central Bank is right back where it was in 2016, and the Federal Reserve is likely to follow later this year if collective egos allow it to admit it erred in 2018. In the meantime, fiscal policy everywhere is going to remain on the sideline. Risks are starting to shift markedly toward a slower growth environment. The causal chain now is:

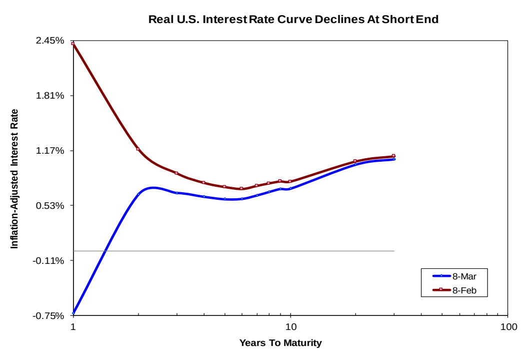
1. The market has priced out a 2019 rate hike but has yet to price in a rate cut;
2. The yield curve is holding its positive slope;
3. Inflationary expectations are retreating once again;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing in the bond market;
5. Swap spreads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

Key Market Indications

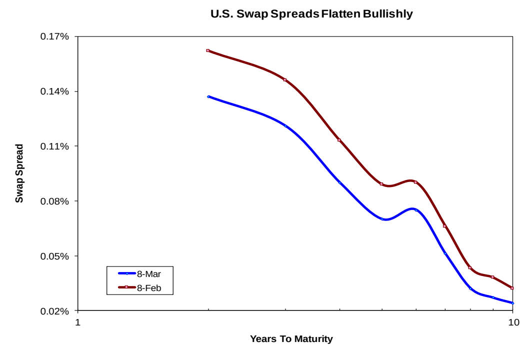
The rally in UST resumed on the realization the Federal Reserve's dovish stance is unlikely to lead to an inflationary irruption. The European Central Bank's capitulation and the downturn in Bund yields have made UST relatively attractive once again.



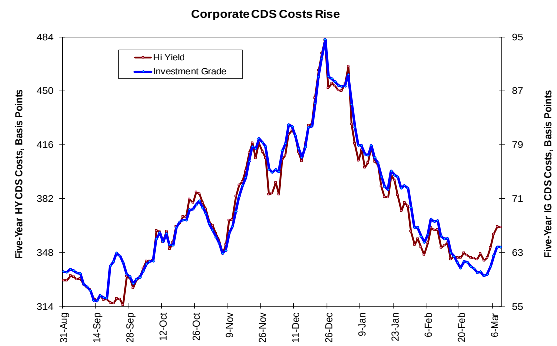
To repeat verbatim from last week, the pseudo-real yield curve declined rapidly at the short end of the yield curve, as expectations for tighter monetary policy dissipate. However, longer-maturity implied real rates have stopped declining. This removes one of the recent boosts for risky assets.



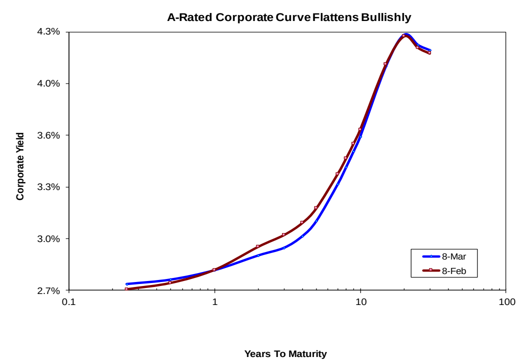
Swap spreads, which rise when floating-rate borrowers want to fix their payments, have declined across all tenors, but especially at the short end of the yield curve. The market is complacent about higher credit spreads and interest rate shifts.



CDS costs rose in response to renewed stresses in GE debt and to the downturn in equities. The recent lows should hold through 2019:Q2.



Corporate bonds are consolidating recent gains, but as was the case for nearly all of 2018, their upside potential remains quite limited. A strong decline in UST yields would be accompanied by an expansion in credit spreads.



Market Structure

Precious Metals and the main Bloomberg index joined Grains and Softs in structural downtrends, while both Livestock and Natural Gas are in structural uptrends. The EAFE index entered a structural downtrend while ten-year UST moved back into an uptrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Mar. 11 - 15
BBerg	21	Trending	-0.064	7.7%	-0.23%
BBerg Grain	29	Trending	-0.434	12.1%	-0.12%
BBerg Ind. Metl	6	Sideways	-0.083	11.8%	
BBerg Pre. Metl	29	Trending	-0.191	7.3%	-0.19%
BBerg Softs	29	Trending	-0.249	13.2%	-0.41%
BBerg Nat. Gas	26	Trending	0.215	19.0%	0.55%
BBerg Petroleum	5	Sideways	-0.026	22.9%	
BBerg Livestock	23	Trending	0.233	8.3%	0.06%
Dollar Index	29	Trending	0.201	4.4%	0.12%
S&P 500 Index	4	Sideways	-0.086	8.6%	
EAFE Index	21	Trending	-0.107	7.6%	-0.17%
EM Index	14	Transitional	-0.251	8.5%	
Ten-year UST (price)	28	Trending	0.103	3.7%	0.20%

Performance Measures

A strong selloff in Grains, Industrial Metals and Softs pulled the main Bloomberg index lower. Only a modest gain in the Energy complex prevented the damage from being worse.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-0.57%	1.19%	-1.90%	-6.53%
Grains Sub-Index	-2.40%	-6.44%	-5.74%	-18.52%
Corn	-2.30%	-4.16%	-4.54%	-16.65%
Soybeans	-1.68%	-2.39%	4.12%	-18.48%
Wheat	-3.84%	-15.45%	-16.43%	-19.22%
Energy Sub-Index	0.63%	6.82%	-10.17%	2.22%
Petroleum Sub-Index	0.75%	6.83%	-16.91%	-1.09%
WTI	0.47%	6.05%	-19.04%	-6.43%
Brent	1.06%	7.02%	-16.04%	4.37%
ULSD	-0.03%	6.00%	-9.49%	9.04%
Gasoline	3.29%	11.29%	-20.72%	-9.30%
Natural Gas	0.30%	6.78%	5.54%	5.37%
Precious Metals Sub-Index	0.19%	-1.23%	8.15%	-3.91%
Gold	0.05%	-0.80%	8.24%	-2.53%
Silver	0.66%	-2.62%	8.10%	-8.39%
Industrial Metals Sub-Index	-1.76%	2.70%	6.32%	-8.82%
Copper	-1.27%	3.66%	10.72%	-8.34%
Aluminum	-2.50%	-0.64%	-8.42%	-9.75%
Nickel	-0.80%	4.81%	7.00%	-5.73%
Zinc	-2.80%	2.95%	22.12%	-11.98%
Softs Sub-Index	-2.20%	-3.77%	-3.72%	-17.00%
Coffee	-1.65%	-4.55%	-6.80%	-26.19%
Sugar	-3.44%	-2.32%	4.09%	-11.00%
Cotton	-0.44%	2.45%	-13.78%	-12.44%
Livestock Sub-Index	2.14%	1.61%	6.59%	2.23%
Cattle	0.13%	1.23%	11.11%	7.10%
Hogs	7.06%	2.34%	-2.94%	-8.11%

The ECB's capitulation led to strong week for the USD, which once again is looking like the best alternative amongst poor choices. Only the JPY, NZD and INR managed to advance on the week. However, the likelihood of a strong USD remains low given the Federal Reserve's new desire to err on the side of caution.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	-1.14%	-0.78%	-3.10%	-8.75%
Chinese yuan	-0.23%	0.36%	2.00%	-5.64%
Japanese yen	0.65%	-1.30%	-0.04%	-4.44%
British pound	-1.42%	0.55%	-0.08%	-5.76%
Swiss franc	-0.88%	-0.76%	-3.28%	-5.66%
Canadian dollar	-0.89%	-1.03%	-1.88%	-3.88%
Australian dollar	-0.48%	-0.61%	-0.98%	-9.55%
Swedish krona	-1.75%	-1.70%	-3.88%	-12.35%
Norwegian krone	-2.14%	-1.49%	-4.31%	-10.58%
New Zealand dollar	0.06%	0.95%	4.26%	-6.33%
Indian rupee	1.09%	1.65%	3.29%	-7.13%
Brazilian real	-2.26%	-3.46%	5.72%	-15.54%
Mexican peso	-1.13%	-2.13%	-1.13%	-4.27%
Chilean peso	-1.94%	-1.88%	3.76%	-9.72%
Colombian peso	-2.47%	-1.84%	-3.42%	-9.43%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.11%	0.01%	1.54%	-4.47%

I commented last week 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. This came to the fore this week as the signs of a global economic slowdown accumulate.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	-2.07%	1.74%	-3.44%	-2.12%
North America	-2.15%	1.47%	-3.87%	0.46%
Latin America	-1.66%	-3.66%	13.17%	-8.08%
Emerging Market Free	-1.99%	-0.35%	3.59%	-12.22%
EAFE	-1.91%	2.25%	-2.63%	-6.75%
Pacific	-1.60%	1.74%	-2.00%	-6.24%
Eurozone	-2.35%	3.21%	-3.94%	-10.40%

CTAs scored strong gains on the week, suggesting they were long both the USD and fixed-income. While macro- and commodity-oriented hedge funds gained, global hedge funds declined, as is typical during an equity selloff.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
SocGen CTA	2.99%	2.74%	-4.40%	-3.94%
SocGen Trend	2.07%	1.90%	-1.56%	-2.26%
SocGen Short-Term	1.45%	0.74%	-1.08%	-2.10%
HFR Global Hedge Fund	-0.17%	0.46%	-2.72%	-4.25%
HFR Macro/CTA	1.08%	1.54%	-1.92%	-1.99%
HFR Macro: Sytematic Diversified CTA	2.89%	2.24%	-2.37%	-2.12%