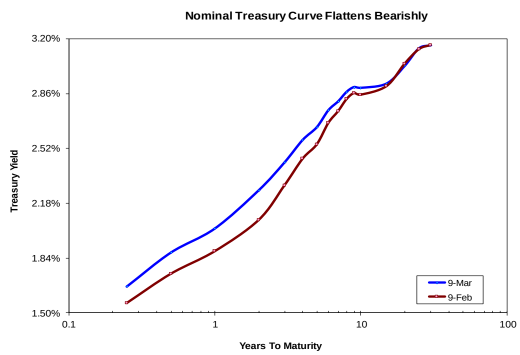
The Macro Environment For Financial Markets

Anyone who claims to have foreseen the combination of misguided tariffs, Gary Cohn's resignation and higher short-term interest as bullish for equities most certainly is lying. So saying, any market capable of digesting this and moving strongly higher is strong indeed. Per usual, I shall wait for the usual suspects who told us in early February why the market needed to go lower to apologize. The wait will be a lengthy one. The causal chain now is:

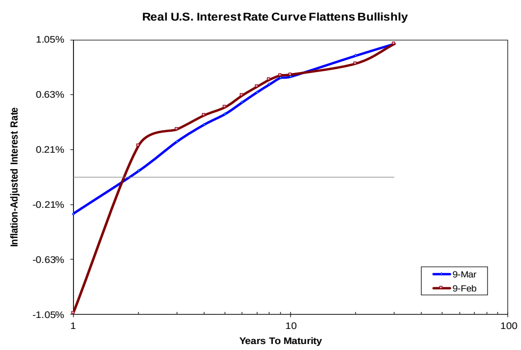
1. The market is pricing in March and June 2018 rate hikes;
2. Inflationary expectations are on pace to reach their next target of 2.26% for the ten-year;
3. The yield curve is drifting back toward a bullish flattening;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing 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

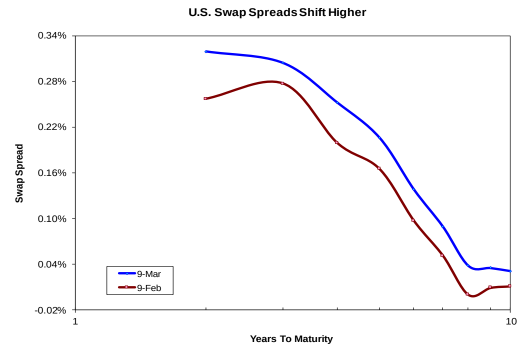
Not only have ten-year UST failed to test their resistance at 3.05%, the recent bearish steepening of the yield curve is returning to what had been a four-year+ flattening trend. We need to remember rising employment is positive for federal finances as it increases tax revenue and reduces various welfare commitments.



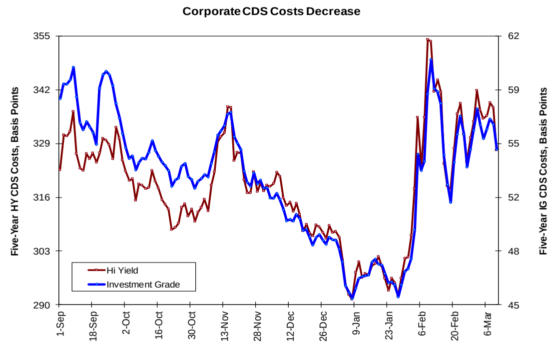
The pseudo-real yield curve shifted higher at the short end of the yield curve but declined slightly at the long end. This is a propitious time for fixed-income investors to shorten duration.



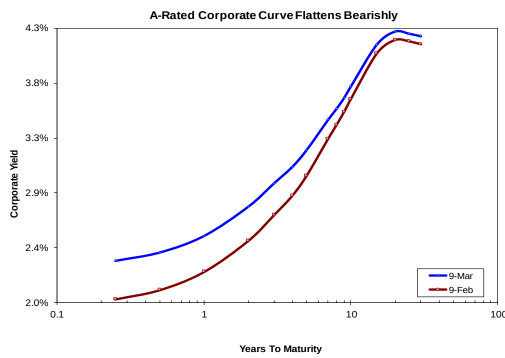
Swap spreads, which rise when floating-rate borrowers want to fix their payments, rose across all tenors. The market at last is realizing long-term rates can move higher.



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 and the main Bloomberg index remain in structural uptrends while Softs joined Livestock in a structural downtrend. All of the financials are in unstable transitional structures.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Mar. 12 - 16
BBerg	24	Trending	0.020	9.6%	0.13%
BBerg Grain	29	Trending	0.224	12.0%	0.22%
BBerg Ind. Metl	17	Transitional	-0.101	16.5%	
BBerg Pre. Metl	13	Transitional	0.012	10.2%	
BBerg Softs	23	Trending	-0.094	13.5%	-0.06%
BBerg Nat. Gas	26	Trending	0.112	20.8%	
BBerg Petroleum	14	Transitional	-0.005	19.8%	
BBerg Livestock	29	Trending	-0.239	10.5%	-0.07%
Dollar Index	14	Transitional	0.017	6.1%	
S&P 500 Index	16	Transitional	0.145	14.6%	
EAFE Index	15	Transitional	-0.027	10.6%	
EM Index	15	Transitional	0.059	11.5%	
Ten-year UST (price)	11	Transitional	-0.039	5.1%	

Performance Measures

Grains weakened after last week's strong rally, and the Energy markets managed to stabilize from their sharp mid-week breaks. The Softs continue to under pressure as major producers have no alternative but to increase output to maintain revenue. Aluminum, which rallied last week on pre-tariff positioning, retreated this week.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-0.19%	2.00%	4.40%	5.57%
Grains Sub-Index	-1.17%	3.61%	5.89%	-4.26%
Corn	1.40%	4.33%	5.53%	-5.28%
Soybeans	-2.93%	2.76%	6.43%	-0.84%
Wheat	-2.12%	2.85%	4.21%	-6.88%
Energy Sub-Index	1.16%	4.83%	9.46%	9.88%
Petroleum Sub-Index	1.14%	4.50%	20.18%	24.36%
WTI	1.39%	5.51%	27.51%	23.58%
Brent	1.72%	5.14%	24.48%	27.80%
ULSD	0.46%	3.16%	10.77%	24.36%
Gasoline	0.21%	2.65%	8.19%	17.90%
Natural Gas	1.20%	5.76%	-18.70%	-25.20%
Precious Metals Sub-Index	0.26%	-0.08%	-2.43%	6.10%
Gold	0.08%	-0.07%	-0.70%	9.43%
Silver	0.89%	-0.15%	-7.55%	-3.12%
Industrial Metals Sub-Index	-0.12%	0.77%	4.41%	19.92%
Copper	0.40%	1.10%	2.64%	18.59%
Aluminum	-1.49%	-0.41%	-1.70%	10.57%
Nickel	3.05%	5.81%	15.19%	38.53%
Zinc	-2.36%	-3.00%	8.78%	22.36%
Softs Sub-Index	-1.82%	-1.53%	-6.57%	-19.87%
Coffee	-1.65%	-2.63%	-14.26%	-22.38%
Sugar	-4.29%	-5.66%	-10.72%	-31.99%
Cotton	2.99%	9.24%	21.07%	11.07%
Livestock Sub-Index	0.46%	-2.33%	4.06%	3.14%
Cattle	0.66%	-1.54%	4.21%	6.77%
Hogs	0.07%	-4.04%	2.63%	-3.96%

Currencies were erratic as the MXN rose and the BRL, CLP and COP all weakened against the USD; gone are the days of high correlation amongst the Latin American currencies. The haven-like low-rate CHF and JPY both weakened, as did the EUR, but the USD fell against the other majors.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	-0.08%	0.45%	2.96%	16.36%
Chinese yuan	0.17%	-0.49%	3.08%	9.10%
Japanese yen	-1.00%	1.85%	2.41%	7.61%
British pound	0.35%	0.17%	5.22%	13.85%
Swiss franc	-1.46%	-1.34%	0.53%	6.39%
Canadian dollar	0.55%	-1.80%	-5.48%	5.46%
Australian dollar	1.08%	0.40%	-2.30%	4.50%
Swedish krona	0.00%	-1.99%	-2.81%	9.73%
Norwegian krone	0.15%	2.36%	0.81%	10.33%
New Zealand dollar	0.61%	0.34%	0.36%	5.49%
Indian rupee	0.00%	-1.18%	-1.90%	2.37%
Brazilian real	-0.07%	1.40%	-4.69%	-1.92%
Mexican peso	1.08%	0.43%	-5.08%	6.53%
Chilean peso	-0.59%	0.18%	3.33%	10.34%
Colombian peso	-0.21%	2.47%	1.83%	4.45%
Bloomberg-JP Morgan Asian dollar index (spot)	0.34%	0.03%	2.39%	6.96%

The Pacific region weakened this week, but the U.S., the Eurozone and the Latin American markets all shrugged off the negative news and rallied.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	2.91%	3.78%	9.16%	19.28%
North America	3.50%	6.40%	13.54%	19.66%
Latin America	2.10%	6.58%	8.01%	27.76%
Emerging Market Free	2.18%	5.80%	11.46%	34.22%
EAFE	1.88%	2.76%	5.49%	20.42%
Pacific	-0.23%	1.41%	7.77%	17.61%
Eurozone	3.11%	2.24%	2.86%	22.87%

Both CTAs and global hedge funds rose on the week, indicating they remained in long equity positions. Macro-oriented hedge funds lost, however, indicating they were wrong-footed by the equity rally.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	0.84%	0.25%	-1.25%	-2.61%
Newedge Trend	0.60%	0.50%	-1.47%	-1.47%
Newedge Short-Term	0.14%	0.10%	0.95%	0.16%
HFR Global Hedge Fund	0.37%	-0.08%	2.12%	4.51%
HFR Macro/CTA	-0.21%	-1.74%	-0.65%	0.90%
HFR Macro: Sytematic Diversified CTA	-0.27%	-2.07%	-0.36%	1.29%