The Macro Environment For Financial Markets

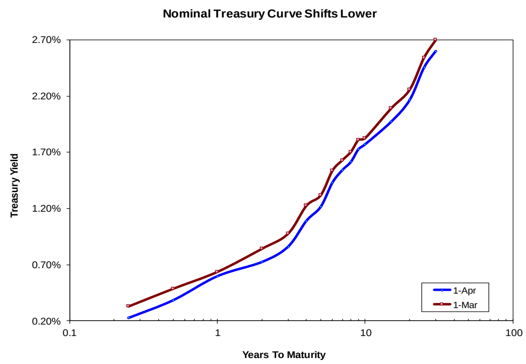
Robert Rubin used to bore everyone and convince no one with his mantra about a strong dollar being in the best interests of the U.S. He should have modified that to say, "A dollar not getting killed by irresponsible policies…" The simple fact of the matter is U.S. equities have outperformed the MSCI World Ex-U.S. in both USD and local currency terms since the greenback fallback began back in January. In addition, while no one is going to classify U.S. economic growth as robust, it is doing well by comparison. The big danger in all of this is policymakers will keep trying to push the USD lower at the risk of rising inflation. The investable result will continue to be financial assets will be pushed higher by miniscule short-term rates and will continue to concentrate both wealth and income at a time when sociopolitical tolerance for all of this is waning.

The causal chain now is:

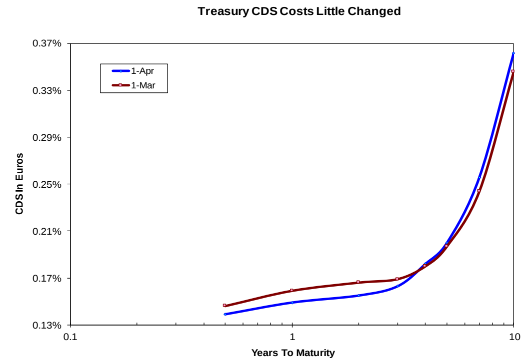
1. The market once again has pushed back the prospects for higher short-term rates in the U.S. ;
2. Disinflationary pressures will persist globally while inflationary pressures are rising in the U.S.;
3. Inflation expectations as measured by TIPS and inflation swaps have established a strong tradable bottom;
4. The U.S. yield curve retains its long-term bias toward flattening;
5. Short-term borrowers have stopped reducing rollover risk;
6. Swap spreads are moving higher at last; and
7. Investment-grade credit spreads have moved back toward 2015 lows while high-yield credit spreads are stalled at resistance.

Key Market Indications

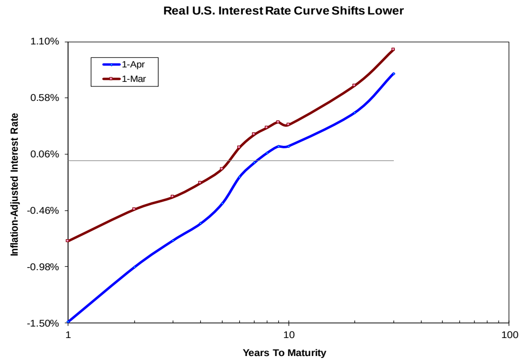
One of the worst feelings for any trader is having to execute a "must-do" trade. As so many banks have been forced by regulatory constraints into the UST market, buying them really is the quintessential must-do. Now that the Federal Reserve is backing off its rate-hike schedule, for a few days at least, investors will find themselves forced out both the risk and duration curves once again. Rinse and repeat.



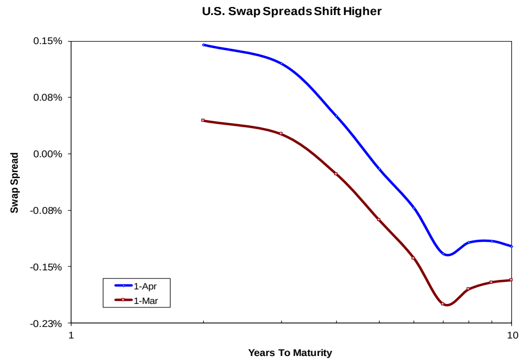
The CDS market for Treasuries has been completely dormant, as it should be. The small shifts lower at shorter tenors and higher at longer tenors are insignificant.



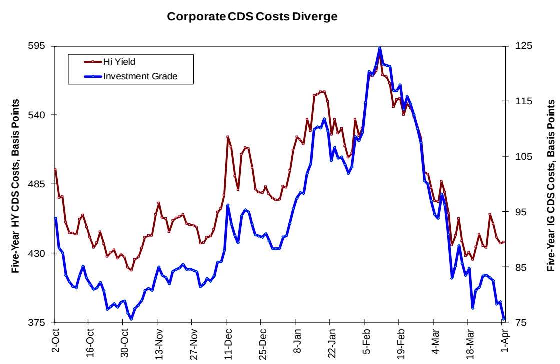
The pseudo-real rate curve shifted lower over the past month and is negative through seven years. The strong move lower at the short end of the yield curve is attributable to a large increase in breakevens intersecting with smaller changes in nominal rates. The decline in pseudo-real rates remains positive for precious metals.



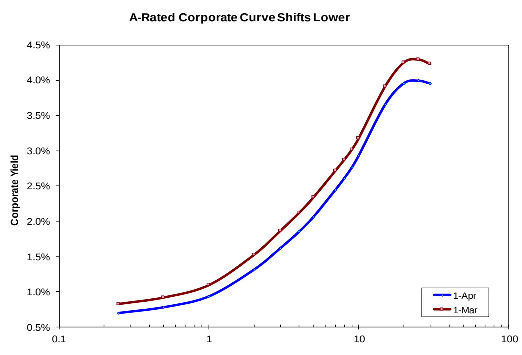
Swap spreads, which rise when floating-rate borrowers want to fix their payments, have shifted higher over the past month and remain inverted. The inversion of this curve is confirmed in the swaption market as well. The belief seems to be that long-term rates will remain constrained even if short-term rates are pushed higher.



While CDS costs for high-yield bonds have stabilized just over their late-2014 resistance levels, investment-grade CDS costs have retreated to their November 2015 low. The combination of expected easier monetary policy in a non-recessionary environment is going to keep these costs suppressed until further notice.



The A-rated corporate yield curve is flattening bullishly once again as the search for yield is pushing investors out of UST and into corporate bonds.



Market Structure

None of the physical commodities are in structural downtrends. This appears likely to change soon as upside momentum has evaporated. Ten-year UST moved into an uptrend while the dollar index remained in a downtrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate April 4 - 8
BBerg	29	Trending	-0.027	11.1%	
BBerg Grain	29	Trending	0.032	11.2%	0.09%
BBerg Ind. Metl	12	Transitional	-0.063	14.7%	
BBerg Pre. Metl	19	Transitional	-0.127	15.4%	
BBerg Softs	29	Trending	0.105	18.3%	0.41%
BBerg Nat. Gas	8	Sideways	0.001	31.4%	
BBerg Petroleum	29	Trending	-0.068	31.1%	
BBerg Livestock	29	Trending	-0.188	9.6%	
Dollar Index	29	Trending	-0.218	9.1%	-0.19%
S&P 500 Index	7	Sideways	0.107	9.6%	
EAFE Index	29	Trending	0.002	13.3%	0.58%
EM Index	7	Sideways	0.033	12.3%	
Ten-year UST (price)	28	Trending	0.111	5.9%	0.22%

Performance Measures

All of the major subindices moved lower once again, and only an odd handful of markets managed an advance. Even if major petroleum exporters fail to agree on production cuts, the damage to longer-term upstream investment and to U.S. shale will combine to prevent a renewal of the petroleum free-fall. Corn's collapse illustrated the producers' dilemma: Farmers have to maintain output to cover their fixed costs.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-1.65%	-0.54%	-11.22%	-21.71%
Grains Sub-Index	-0.96%	1.74%	-6.57%	-13.90%
Corn	-4.32%	-1.16%	-12.21%	-17.46%
Soybeans	0.86%	4.55%	3.74%	-5.76%
Wheat	2.76%	3.28%	-8.64%	-14.16%
Energy Sub-Index	-4.11%	0.66%	-31.41%	-42.18%
Petroleum Sub-Index	-6.24%	-1.66%	-30.16%	-40.44%
WTI	-6.76%	-2.52%	-35.60%	-46.24%
Brent	-5.66%	-1.83%	-29.42%	-42.57%
ULSD	-6.46%	-3.83%	-33.05%	-41.72%
Gasoline	-6.22%	2.34%	-20.44%	-25.70%
Natural Gas	3.94%	9.49%	-37.25%	-48.69%
Precious Metals Sub-Index	-0.26%	-3.87%	5.04%	-1.91%
Gold	0.01%	-3.78%	7.55%	1.52%
Silver	-1.00%	-4.11%	-1.76%	-10.98%
Industrial Metals Sub-Index	-0.11%	-4.51%	-4.96%	-21.48%
Copper	-2.95%	-4.88%	-7.43%	-21.67%
Aluminum	4.04%	-3.63%	-3.22%	-18.70%
Nickel	-3.88%	-11.10%	-17.68%	-37.05%
Zinc	4.34%	0.62%	9.46%	-14.34%
Softs Sub-Index	-1.83%	7.18%	8.05%	1.23%
Coffee	-0.23%	5.15%	-2.21%	-18.70%
Sugar	-4.34%	2.39%	12.94%	8.57%
Cotton	2.57%	3.68%	-2.58%	-9.20%
Livestock Sub-Index	-1.61%	-2.32%	-2.80%	-10.27%
Cattle	-1.43%	-1.81%	-0.31%	-16.68%
Hogs	-1.82%	-2.97%	-7.18%	2.28%

I concluded last week, "The U.S., quite simply, cannot maintain a strong-dollar policy." This was demonstrated by the uniform decline of the USD against all currencies illustrated here. To paraphrase the late Herb Stein, if the U.S. can't maintain a strong-dollar policy, it won't.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	2.01%	4.81%	1.75%	5.83%
Chinese yuan	0.53%	1.08%	-1.92%	-4.38%
Japanese yen	1.24%	2.08%	7.38%	7.23%
British pound	0.67%	1.97%	-5.97%	-4.02%
Swiss franc	2.05%	4.11%	2.00%	0.94%
Canadian dollar	1.99%	3.07%	1.98%	-3.00%
Australian dollar	2.26%	7.00%	9.20%	1.01%
Swedish krona	2.06%	5.95%	2.95%	6.50%
Norwegian krone	1.88%	3.98%	1.29%	-3.45%
New Zealand dollar	3.26%	4.15%	7.89%	-7.37%
Indian rupee	0.59%	3.28%	-0.99%	-5.66%
Brazilian real	3.51%	10.70%	12.82%	-10.94%
Mexican peso	1.15%	3.30%	-2.40%	-12.61%
Chilean peso	1.74%	3.52%	4.08%	-7.69%
Colombian peso	1.19%	6.32%	0.84%	-15.20%
Bloomberg-JP Morgan Asian dollar index (spot)	1.02%	2.51%	1.30%	-3.60%

The U.S. has moved back to what was the key resistance point all through 2015, 2070 on the SPX. While index-level earnings growth continues to struggle, a stealth bull market has emerged and is likely to carry the broader U.S. market higher and take the rest of the world along for the ride.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	1.14%	4.45%	4.52%	-3.21%
North America	1.92%	5.10%	8.05%	1.14%
Latin America	3.90%	17.11%	14.83%	-11.62%
Emerging Market Free	1.74%	9.96%	4.45%	-13.55%
EAFE	-0.18%	3.37%	-1.09%	-9.96%
Pacific	-2.39%	3.92%	-0.14%	-9.95%
Eurozone	0.68%	3.45%	-0.47%	-11.61%

The professional traders managed gains during a week filled with bearish moves in physical markets and a reversal toward dollar weakness. This suggests adherence to the one over-arching trend: Chase yield and you shall be rewarded.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	1.16%	-3.00%	1.56%	-4.20%
Newedge Trend	0.69%	-3.10%	4.00%	-1.71%
Newedge Short-Term	0.61%	-1.11%	4.82%	-2.55%
HFR Global Hedge Fund	0.33%	1.24%	-2.47%	-7.36%
HFR Macro/CTA	-0.03%	-1.12%	-0.33%	-5.11%
HFR Macro: Sytematic Diversified CTA	0.77%	-1.78%	2.55%	-2.12%