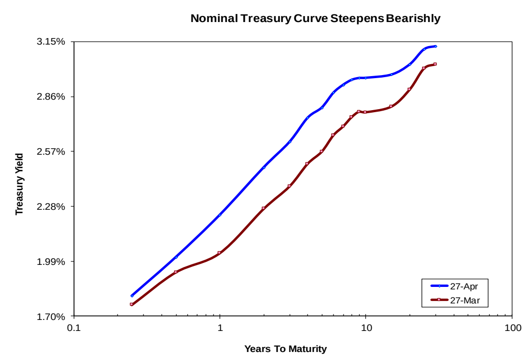
The Macro Environment For Financial Markets

When a capital goods supplier says earnings growth is as good as it is going to get, listen. When a franchise like Alphabet increases its capital spending, ignore it. The former sells a good with limited demand while the latter has a franchise with relatively unlimited demand. This is the classic old vs. new economy debate. The causal chain remains:

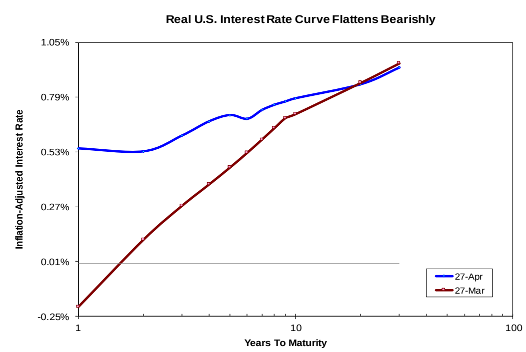
1. The market is pricing in June, September and increasingly December 2018 rate hikes;
2. Inflationary expectations are rising;
3. The yield curve has resumed its flattening trend;
4. Short-term borrowers are accepting rollover risk rather than term-out borrowing in the bond market;
5. Swap spreads continue to invert bullishly; and
6. CDS costs continue to reflect equity market fluctuations more than credit market conditions.

Key Market Indications

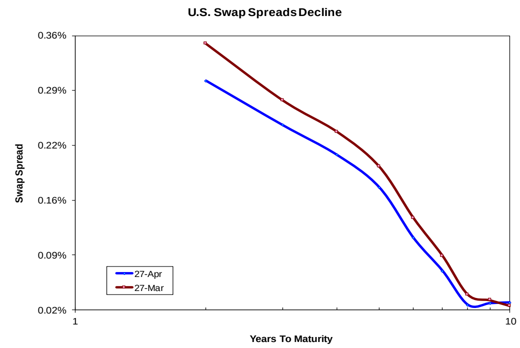
Inflation expectations remain in their uptrend despite expectations for higher short-term interest rates. The selloff at the long end of the UST market constitutes a successful test, so far, of 3.05% support in the ten-year note. The yield curve resumed its flattening trend.



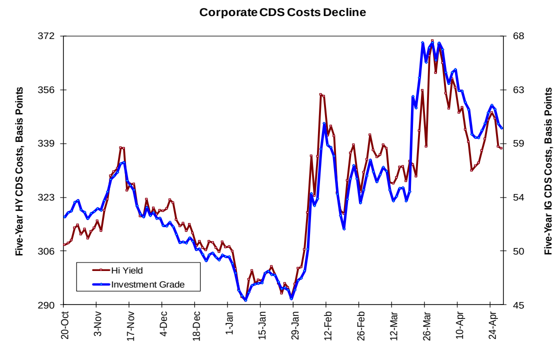
The pseudo-real yield curve continued to shift higher at the short end of the yield curve. This is a major negative fundamental for gold.



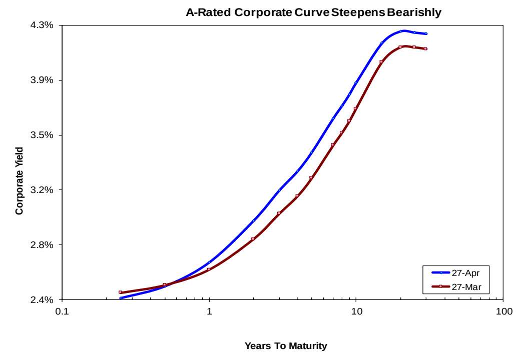
Swap spreads, which rise when floating-rate borrowers want to fix their payments, shifted lower, especially at the short end. The market continues to resist the idea long-term interest rates can rise significantly from here.



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 steepened bearishly in line with UST. Rising LIBOR has not posed a threat to this market yet but must be considered a negative given how it affects carrying costs.



Market Structure

Grains reversed into an uptrend, while Precious Metals and Softs are in downtrends within the physical markets. Within financial markets, the dollar index and the EAFE remain in uptrends while ten-year UST remain in a downtrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Apr. 30 - May 4
BBerg	6	Sideways	-0.009	8.5%	
BBerg Grain	25	Trending	0.117	15.8%	0.20%
BBerg Ind. Metl	29	Trending	-0.003	24.5%	
BBerg Pre. Metl	27	Trending	-0.108	10.0%	-0.43%
BBerg Softs	29	Trending	-0.106	12.8%	-0.06%
BBerg Nat. Gas	29	Trending	0.006	18.2%	
BBerg Petroleum	4	Sideways	0.023	14.0%	
BBerg Livestock	17	Transitional	-0.030	12.9%	
Dollar Index	29	Trending	0.299	5.4%	0.03%
S&P 500 Index	29	Trending	0.034	17.2%	
EAFE Index	29	Trending	0.085	9.3%	0.12%
EM Index	14	Transitional	-0.079	9.3%	
Ten-year UST (price)	29	Trending	-0.209	4.0%	-0.16%

Performance Measures

The run in Industrial Metals reversed as the market has become a scorecard on Russian sanctions. This is not to be interpreted as a sign of economic weakness. Precious Metals fell on rising short-term rates. The run higher in the Petroleum complex stalled, but this probably is a short-term affair as global demand growth can and will outpace any increased supply response from the U.S. Grains are benefiting from the combination of poor Southern Hemisphere conditions combined with reduced planting intentions in the U.S.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-0.48%	2.33%	4.48%	7.75%
Grains Sub-Index	3.17%	2.43%	7.12%	-0.50%
Corn	3.41%	0.72%	7.24%	-3.99%
Soybeans	1.57%	0.22%	4.57%	6.39%
Wheat	4.49%	7.06%	8.56%	-3.50%
Energy Sub-Index	0.38%	4.46%	13.01%	18.36%
Petroleum Sub-Index	0.46%	6.11%	21.52%	40.34%
WTI	-0.26%	5.30%	27.09%	36.69%
Brent	0.64%	7.33%	25.13%	44.62%
ULSD	0.77%	6.08%	15.64%	42.05%
Gasoline	1.22%	5.35%	10.47%	36.08%
Natural Gas	0.15%	-0.26%	-10.33%	-29.20%
Precious Metals Sub-Index	-1.80%	0.13%	2.37%	1.24%
Gold	-1.08%	-0.15%	3.74%	3.57%
Silver	-4.17%	1.12%	-1.92%	-5.55%
Industrial Metals Sub-Index	-5.49%	3.32%	1.36%	20.55%
Copper	-2.69%	0.98%	-2.15%	15.65%
Aluminum	-9.97%	12.24%	3.45%	15.59%
Nickel	-6.37%	4.41%	12.67%	45.62%
Zinc	-3.47%	-4.63%	-3.88%	20.87%
Softs Sub-Index	0.17%	-2.31%	-7.69%	-15.02%
Coffee	4.03%	2.01%	-7.19%	-16.14%
Sugar	-2.91%	-7.05%	-21.32%	-31.31%
Cotton	-0.22%	4.39%	23.04%	11.70%
Livestock Sub-Index	-0.38%	0.92%	-15.17%	-10.23%
Cattle	3.19%	4.46%	-13.43%	-13.24%
Hogs	-6.32%	-4.99%	-19.43%	-6.56%

The USD had a clean sweep to the upside as the expected pace of relatively higher USD rates overwhelmed the negative effects of expected increases in the U.S. current account deficit. If the 2014-2016 experience is any guide, the Federal Reserve will start to pay attention to any signs of dollar scarcity in the commercial banking system and react accordingly.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	-1.29%	-2.20%	4.50%	11.56%
Chinese yuan	-0.57%	-0.78%	5.03%	8.93%
Japanese yen	-1.27%	-3.40%	4.24%	2.03%
British pound	-1.56%	-2.66%	4.97%	6.80%
Swiss franc	-1.33%	-4.14%	1.05%	0.65%
Canadian dollar	-0.52%	0.45%	-0.16%	6.28%
Australian dollar	-1.19%	-1.28%	-1.25%	1.55%
Swedish krona	-2.46%	-4.94%	-3.31%	2.03%
Norwegian krone	-1.74%	-3.06%	2.33%	7.58%
New Zealand dollar	-1.69%	-2.60%	3.01%	3.04%
Indian rupee	-0.83%	-2.54%	-2.42%	-3.76%
Brazilian real	-1.28%	-3.81%	-6.43%	-7.90%
Mexican peso	-0.45%	-1.24%	2.79%	2.22%
Chilean peso	-1.96%	-0.59%	4.56%	9.20%
Colombian peso	-1.65%	-0.83%	7.26%	4.68%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.29%	-0.66%	3.36%	5.28%

In case anyone had forgotten, markets are discounting mechanisms. If you announce blowout earnings and then tell everyone they will be as good as it gets, they will take you up on it, especially in a rising short-term rate environment.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	-0.10%	1.66%	4.14%	14.34%
North America	-0.04%	2.35%	4.28%	13.77%
Latin America	-0.59%	0.74%	7.51%	19.31%
Emerging Market Free	-1.01%	-2.26%	5.03%	21.07%
EAFE	-0.21%	2.29%	4.23%	14.88%
Pacific	0.18%	1.37%	5.17%	16.68%
Eurozone	-0.50%	3.22%	2.50%	15.95%

Both CTAs and hedge funds retreated this week, a common occurrence when equities are under pressure. The moves higher in the USD, a stall in the crude oil rally and the emergence of support in the long end of the UST market were headwinds as well.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	-0.98%	-0.60%	0.20%	0.89%
Newedge Trend	-0.88%	-0.39%	-0.44%	-0.03%
Newedge Short-Term	0.67%	-0.35%	0.54%	0.11%
HFR Global Hedge Fund	-0.46%	-0.33%	0.43%	3.00%
HFR Macro/CTA	-0.47%	-1.33%	-0.27%	1.80%
HFR Macro: Sytematic Diversified CTA	-0.55%	-1.73%	1.90%	4.01%