The Macro Environment For Financial Markets

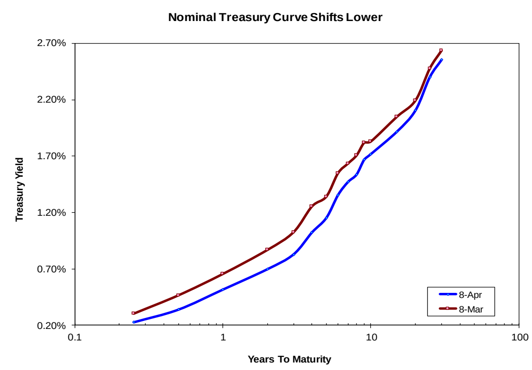
Should you be concerned with the rising yen? No, not really. Should you be concerned about a falling yuan? Yes, really. Should you be concerned if the European Central Bank's latest move precluded any and all possibility of a yen carry trade while China may be buying JPY and not USD in an effort to improve its external balance? No, because that keeps the CNY from collapsing while it keeps U.S. interest rates from rising. If Japan does not like the stronger JPY, then let them start buying U.S. financial assets the way the ECB is going to start buying European investment-grade corporate bonds. None of this razzle-dazzle will help the economy, mind you, but it most certainly will keep a bid under financial assets.

The causal chain now is:

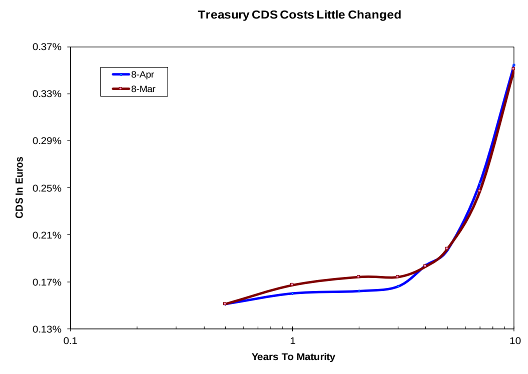
1. The market once again has pushed back the prospects for higher short-term rates in the U.S. ;
2. Disinflationary pressures will persist globally while inflationary pressures are rising in the U.S.;
3. Inflation expectations as measured by TIPS and inflation swaps have established a strong tradable bottom;
4. The U.S. yield curve retains its long-term bias toward flattening;
5. Short-term borrowers are accepting rollover risk again;
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

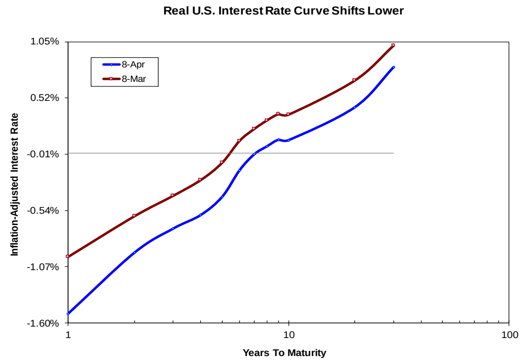
There are many reasons for a market to sell off; that it has been in a long-running bull market should never be one of them. However, any responsible analyst must ask what it would take to produce a jump in yields at this point. The most convincing answer, a collective decision on the part of the world's major central banks to reduce their balance sheets is also the least likely answer. The bull market remains intact.



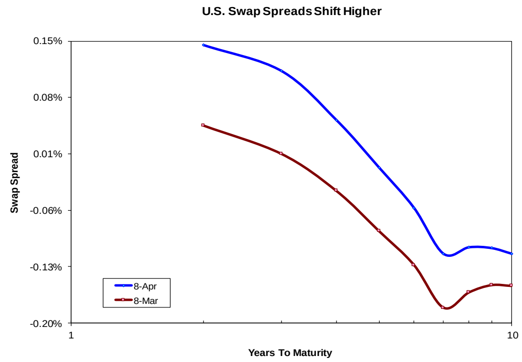
The CDS market for Treasuries has been completely dormant, as it should be. The small shift lower at shorter tenors is insignificant.



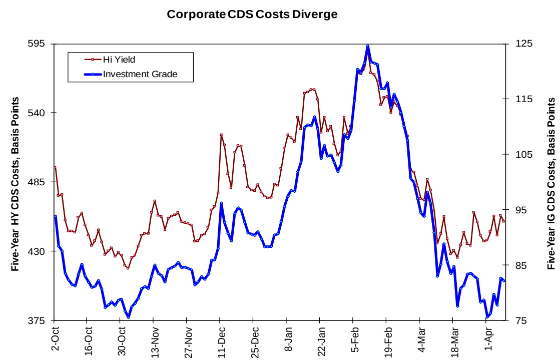
The pseudo-real rate curve shifted lower over the past month and is negative through seven years. The strong move lower at the short end of the yield curve is attributable to a large increase in breakevens intersecting with smaller changes in nominal rates. The decline in pseudo-real rates remains positive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



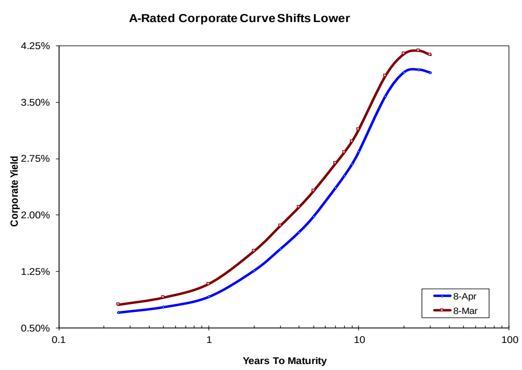
Swap spreads, which rise when floating-rate borrowers want to fix their payments, have shifted higher over the past month and remain inverted. The inversion of this curve is confirmed in the swaption market as well. The belief seems to be that long-term rates will remain constrained even if short-term 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 tested 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 shifting lower as the search for yield is pushing investors out of UST and into corporate bonds.



Market Structure

Only Livestock is in a structural downtrend amongst the physical markets; critically, however, Petroleum shifted into a structural uptrend and took the main Bloomberg index with it. Ten-year UST remain in an uptrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate April 11 - 15
BBerg	29	Trending	0.030	10.4%	0.11%
BBerg Grain	26	Trending	-0.030	11.1%	
BBerg Ind. Metl	19	Transitional	-0.192	14.9%	
BBerg Pre. Metl	23	Trending	0.015	14.9%	
BBerg Softs	29	Trending	-0.081	17.6%	
BBerg Nat. Gas	8	Sideways	0.016	31.6%	
BBerg Petroleum	29	Trending	0.085	26.8%	0.30%
BBerg Livestock	29	Trending	-0.088	9.8%	-0.28%
Dollar Index	4	Sideways	-0.029	7.7%	
S&P 500 Index	8	Sideways	-0.050	10.1%	
EAFE Index	29	Trending	-0.001	13.0%	
EM Index	7	Sideways	-0.029	12.3%	
Ten-year UST (price)	29	Trending	0.196	5.3%	0.22%

Performance Measures

While it is easy to become distracted by the flow of news, the signal in the Petroleum subindex is unmistakable: We are in the early stages of a secular uptrend. This does not extend to other major subindices, the Industrial Metals in particular, where excess capacity and slow import demand growth from China continue to weight on prices.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	1.40%	0.80%	-12.43%	-20.25%
Grains Sub-Index	0.03%	1.06%	-6.96%	-12.23%
Corn	2.35%	0.53%	-10.61%	-13.90%
Soybeans	-0.16%	3.67%	2.73%	-4.51%
Wheat	-3.30%	-1.09%	-11.35%	-15.42%
Energy Sub-Index	5.68%	4.10%	-31.69%	-38.84%
Petroleum Sub-Index	6.82%	2.45%	-30.66%	-37.04%
WTI	7.92%	3.36%	-35.95%	-43.45%
Brent	7.50%	3.08%	-30.42%	-38.86%
ULSD	5.94%	-1.08%	-32.73%	-38.83%
Gasoline	4.35%	2.86%	-20.96%	-21.48%
Natural Gas	1.85%	10.52%	-37.32%	-45.86%
Precious Metals Sub-Index	1.82%	-1.17%	5.52%	0.13%
Gold	1.66%	-1.58%	8.60%	3.02%
Silver	2.25%	-0.01%	-2.75%	-7.61%
Industrial Metals Sub-Index	-2.58%	-3.80%	-7.63%	-23.14%
Copper	-3.54%	-6.08%	-11.37%	-24.37%
Aluminum	-1.17%	-3.55%	-4.14%	-18.91%
Nickel	2.71%	-0.66%	-16.62%	-33.00%
Zinc	-6.21%	-0.38%	4.09%	-20.77%
Softs Sub-Index	-3.02%	0.17%	-0.16%	-5.96%
Coffee	-5.35%	-1.01%	-10.43%	-20.10%
Sugar	-3.21%	-1.11%	5.57%	3.22%
Cotton	1.46%	5.66%	-3.69%	-12.07%
Livestock Sub-Index	1.06%	-1.06%	-5.03%	-9.24%
Cattle	0.37%	-1.94%	-4.52%	-15.31%
Hogs	1.90%	0.14%	-6.53%	2.33%

While we can only infer real short-term rates, we can detect their presence via currency movements. Japan's must be very high to produce the kind of gains seen for the JPY. With the exception of the GBP, the USD continues to weaken against the majors and gain against the emerging market currencies.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	0.07%	3.52%	1.09%	5.73%
Chinese yuan	0.28%	0.64%	-1.70%	-4.03%
Japanese yen	3.35%	4.21%	10.97%	11.16%
British pound	-0.70%	-0.61%	-7.95%	-4.96%
Swiss franc	0.46%	4.41%	1.31%	1.35%
Canadian dollar	0.18%	3.24%	0.22%	-3.40%
Australian dollar	-1.58%	1.57%	4.08%	-1.67%
Swedish krona	-0.21%	4.06%	1.13%	6.36%
Norwegian krone	1.00%	3.98%	-1.13%	-2.20%
New Zealand dollar	-1.38%	0.93%	2.13%	-9.86%
Indian rupee	-0.33%	0.94%	-2.27%	-6.34%
Brazilian real	-1.02%	4.58%	5.43%	-15.07%
Mexican peso	-2.46%	0.85%	-7.41%	-16.14%
Chilean peso	-2.03%	-0.07%	-0.48%	-10.36%
Colombian peso	-1.71%	3.73%	-7.10%	-19.39%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.14%	1.51%	-0.16%	-3.89%

While the U.S. failed at the SPX 2070 level once again, there really is not much reason to expect a major selloff at this point for the very simple reason sellers have to accept bad alternatives for doing so.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	-0.41%	2.75%	-0.68%	-5.20%
North America	-1.03%	3.75%	2.01%	-1.16%
Latin America	-2.83%	4.58%	2.56%	-17.20%
Emerging Market Free	-1.08%	3.87%	-2.91%	-17.71%
EAFE	0.67%	1.11%	-4.95%	-11.42%
Pacific	1.19%	-0.18%	-2.36%	-11.73%
Eurozone	-0.59%	1.13%	-6.62%	-13.24%

What have CTAs figured out in 2016 that has eluded them for so long? Regardless, they are having a solid 2016 so far. Hedge funds are proving, once again, they have a great deal of difficulty in a stagnant equity environment.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	0.48%	0.87%	5.16%	-3.34%
Newedge Trend	0.73%	0.74%	6.62%	-0.82%
Newedge Short-Term	0.92%	0.46%	6.85%	-1.76%
HFR Global Hedge Fund	-0.37%	0.06%	-3.50%	-8.10%
HFR Macro/CTA	-0.19%	-0.94%	1.14%	-5.27%
HFR Macro: Sytematic Diversified CTA	0.18%	-0.44%	5.50%	-1.77%