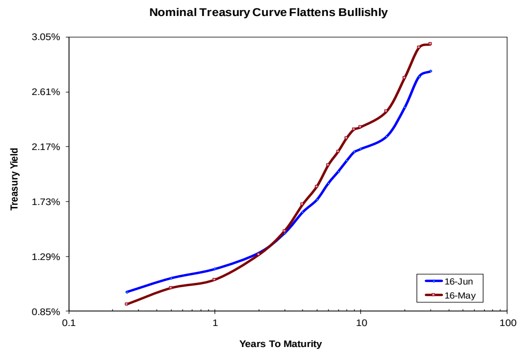
The Macro Environment For Financial Markets

The secular tide of excessive monetary ease is receding, albeit slowly, in the U.S. and possibly in both Canada and the U.K. Neither Japan nor the Eurozone have joined the party yet, but this seems inevitable. Do not worry about the justification for any of this in a time of stable inflationary pressures and modest growth; policymakers have made up their minds and will rationalize any and all actions. Your job will be to accept their omniscience in the face of massive evidence to the contrary. Fortunately, the human capacity for self-deception is enormous. The causal chain remains:

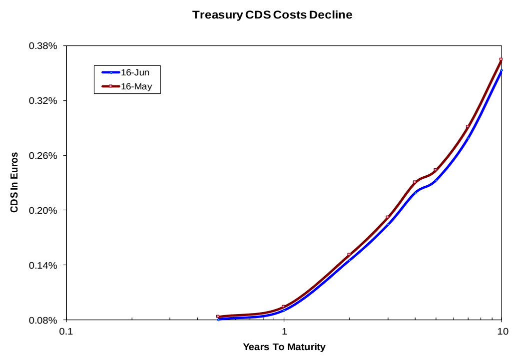
1. The market still is pricing in higher short-term rates in 2017, but the conviction level is declining;
2. Inflationary expectations remain under pressure;
3. The U.S. yield curve continues in its secular flattening trend;
4. Short-term borrowers are close to terming out short-term debt into the bond market;
5. Swap spreads are declining; and
6. CDS costs remain consistent with a bull market in risky assets.

Key Market Indications

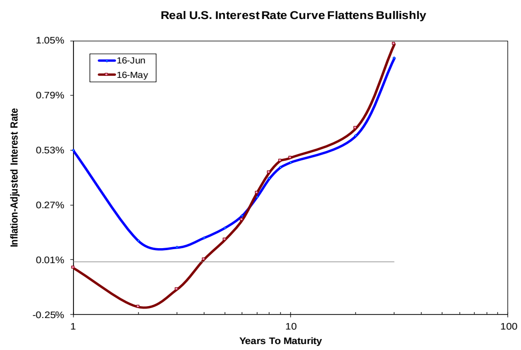
The UST market continues to flatten bullishly, a condition exacerbated by the Federal Reserve's more modestly aggressive stance. If the balance sheet shrinks, credit expansion in the commercial banking system slows and places downward pressure on inflation. More critically, regulatory constraints and keeping demand high for long-term sovereign debt at a time when central banks are the primary holders and are unwilling to sell.



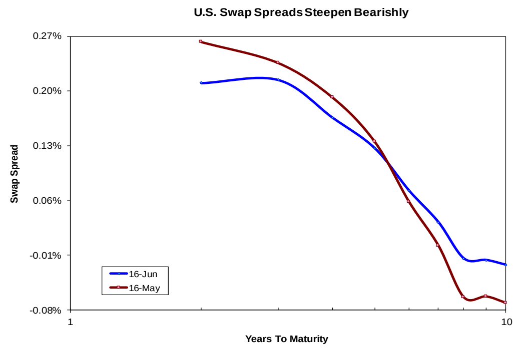
CDS costs on UST declined. This market remains unconcerned about the U.S. debt ceiling.



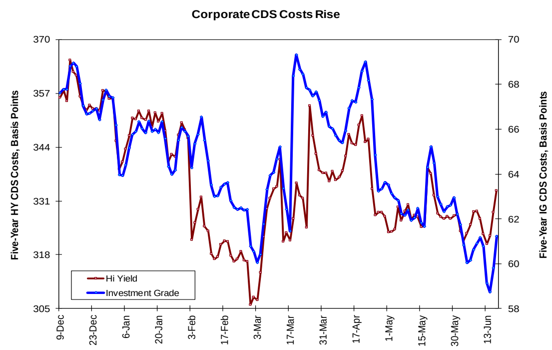
The pseudo-real yield curve shifted higher at the short end of the yield curve but declined from seven years onward. The rise at the short end of the yield curve was bearish for precious metals.



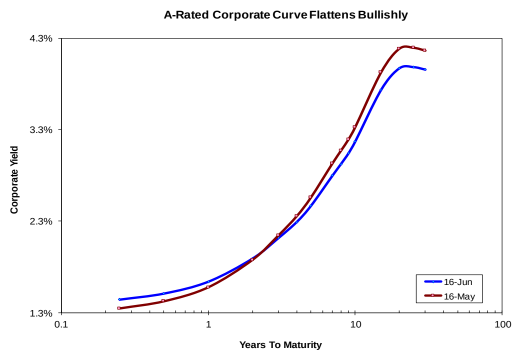
Swap spreads, which rise when floating-rate borrowers want to fix their payments, shifted lower at tenors shorter than six years. The market clearly is backing away from a belief in rate hikes after June.



CDS costs rose from recent lows, but these were minor moves within the context of a secular bull market. We would need evidence of much higher short-term rates and of rising recessionary pressures to reverse these trends.



The A-rated corporate yield curve flattened bullishly. This remains a bull market with limited upside potential.



Market Structure

Only Grains are in a structural uptrend amongst the physical commodities; Petroleum, Livestock, Softs and Industrial Metals are in downtrends along with the main index. Ten-year UST remain in structural uptrends amongst the financials.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate June 19 - 23
BBerg	24	Trending	-0.220	8.2%	-0.10%
BBerg Grain	26	Trending	0.218	13.9%	0.07%
BBerg Ind. Metl	22	Trending	-0.097	12.6%	-0.18%
BBerg Pre. Metl	25	Trending	-0.112	10.3%	
BBerg Softs	29	Trending	-0.489	14.7%	-0.63%
BBerg Nat. Gas	7	Sideways	0.024	22.8%	
BBerg Petroleum	24	Trending	-0.265	23.6%	-0.83%
BBerg Livestock	22	Trending	-0.140	12.6%	-0.77%
Dollar Index	10	Sideways	0.030	5.6%	
S&P 500 Index	6	Sideways	-0.005	8.1%	
EAFE Index	12	Transitional	-0.035	7.7%	
EM Index	14	Transitional	-0.128	6.8%	
Ten-year UST (price)	29	Trending	0.184	4.0%	0.15%

Performance Measures

Only Grains prevented a complete rout amongst the physical commodities. Higher short-term interest rates pushed Precious Metals lower, while supply issues continue to weigh on Energy, Softs and Industrial Metals. The break of a retracement rally in March has put the Bloomberg total return index on path to test its January 2016 low.

Commodity Total Returns

	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-1.38%	-4.00%	-5.79%	-7.91%
Grains Sub-Index	0.89%	3.05%	0.58%	-19.52%
Corn	-0.91%	3.24%	4.90%	-20.73%
Soybeans	0.20%	-0.90%	-10.23%	-20.65%
Wheat	4.66%	7.25%	9.05%	-18.37%
Energy Sub-Index	-1.43%	-10.84%	-18.49%	-14.73%
Petroleum Sub-Index	-1.90%	-11.32%	-18.52%	-15.66%
WTI	-2.37%	-11.65%	-19.33%	-19.06%
Brent	-1.84%	-11.57%	-17.22%	-14.92%
ULSD	-0.44%	-10.27%	-17.47%	-12.85%
Gasoline	-2.62%	-11.25%	-20.53%	-12.35%
Natural Gas	-0.18%	-9.57%	-18.67%	-11.63%
Precious Metals Sub-Index	-1.72%	-0.17%	7.71%	-4.50%
Gold	-1.15%	0.05%	9.45%	-4.03%
Silver	-3.32%	-0.80%	3.03%	-6.06%
Industrial Metals Sub-Index	-2.05%	-2.56%	-0.34%	17.48%
Copper	-3.02%	-0.45%	1.97%	22.97%
Aluminum	-2.16%	-4.13%	7.92%	13.45%
Nickel	-0.49%	-4.68%	-18.51%	-2.93%
Zinc	-0.24%	-3.74%	-3.69%	25.70%
Softs Sub-Index	-4.22%	-10.98%	-16.65%	-21.04%
Coffee	-2.21%	-6.27%	-16.70%	-19.64%
Sugar	-5.83%	-17.89%	-25.94%	-34.06%
Cotton	-4.56%	-9.00%	0.52%	5.34%
Livestock Sub-Index	-4.04%	-1.49%	10.02%	2.01%
Cattle	-4.56%	-2.30%	16.41%	18.07%
Hogs	-3.19%	-0.19%	0.90%	-16.07%

Low-rate haven currencies such as the JPY and CHF moved lower along with several key EM currencies such as the INR and CNY, but the USD declined against most other currencies, including the commodity-linked CAD and AUD. The key variable now is not the path of short-term USD rates but rather the rising probability there will be no U.S. fiscal stimulus.

Currency Returns

	Five-Days	One Month	Six Months	One Year
Euro	0.03%	1.04%	7.15%	-0.24%
Chinese yuan	-0.18%	1.12%	2.22%	-3.22%
Japanese yen	-0.51%	2.02%	6.36%	-5.97%
British pound	0.29%	-1.04%	2.30%	-10.00%
Swiss franc	-0.40%	1.29%	5.42%	-0.85%
Canadian dollar	1.95%	2.97%	0.93%	-1.86%
Australian dollar	1.25%	2.63%	4.34%	3.50%
Swedish krona	0.06%	0.96%	7.23%	-4.25%
Norwegian krone	0.52%	0.05%	2.56%	-0.77%
New Zealand dollar	0.57%	5.39%	4.18%	2.97%
Indian rupee	-0.27%	-0.55%	5.19%	4.42%
Brazilian real	0.15%	-5.93%	2.92%	5.29%
Mexican peso	1.45%	4.06%	14.10%	5.76%
Chilean peso	-0.13%	0.37%	1.39%	3.73%
Colombian peso	-1.93%	-3.13%	1.11%	1.38%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.14%	0.34%	3.14%	-0.46%

The problem with investing in emerging markets is they simply refuse to emerge; take Brazil, please. Just as soon as the global tide of liquidity threatened to push European equities higher, they pulled back on the increasing likelihood Eurozone QE will start to end in late 2017.

Equity Total Returns

	Five-Days	One Month	Six Months	One Year
MSCI World Free	0.07%	1.71%	10.94%	20.56%
North America	0.10%	1.52%	8.59%	19.17%
Latin America	-0.05%	-8.08%	14.94%	25.75%
Emerging Market Free	-1.41%	-0.93%	18.47%	28.73%
EAFE	0.03%	0.54%	15.86%	24.57%
Pacific	0.54%	2.81%	10.50%	21.98%
Eurozone	-0.70%	-0.04%	20.69%	29.16%

Both CTAs and hedge funds posted weekly losses; the declines for hedge funds were to be expected given the pullback in global equities, but the declines for CTAs are a little more puzzling given the lack of major reversals.

CTA/Hedge Fund Returns

	Five-Days	One Month	Six Months	One Year
Newedge CTA	-0.83%	-0.32%	-3.84%	-7.44%
Newedge Trend	-0.78%	-0.06%	-1.22%	-4.83%
Newedge Short-Term	-0.49%	0.03%	-6.87%	-12.38%
HFR Global Hedge Fund	-0.23%	-0.06%	2.44%	5.97%
HFR Macro/CTA	-0.43%	0.32%	-0.59%	-2.09%
HFR Macro: Sytematic Diversified CTA	-0.53%	0.51%	-2.78%	-3.67%