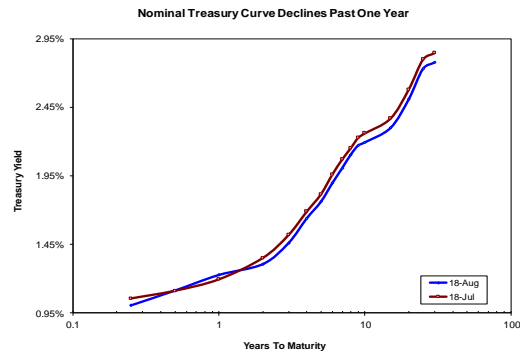


Generally, there is no percentage in discussing politics, but when the long U.S. bull market's gains since the election were based in part on the hopes for tax and regulatory reform, dysfunction is a fundamental. We also have to deal with the volatility tail wagging the equity dog; the sell-the-VIX crowd has to buy their short positions back and force the market-makers to sell stock. Someone needs to inform them this is in the rulebook. The causal chain now is:

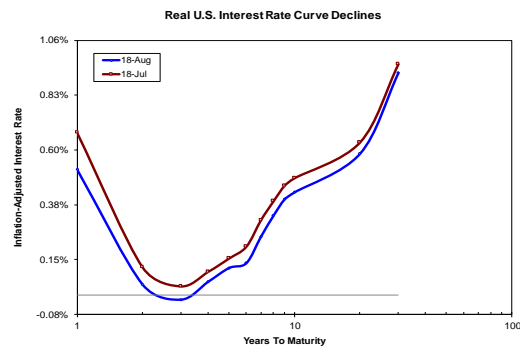
1. The market is pricing out expectations for another short-term rate hike in the U.S. in 2017 but has to deal with the prospects of a shrinking balance sheet;
2. Inflationary expectations are starting to decline once again;
3. The secular flattening trend in the U.S. is encountering resistance as expectations for higher short-term rates fade;
4. Short-term borrowers are close to terming out short-term debt into the bond market;
5. Swap spreads are rising; and
6. CDS costs are rising in response to declining equities.

Key Market Indications

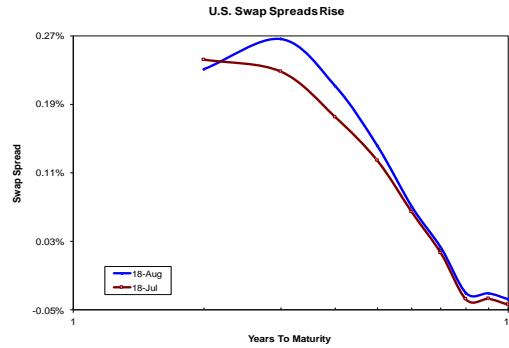
Traders have become so conditioned to seeing UST as a haven asset that the lack of a strong bid is noticeable. However, with inflation expectations declining and with overt tightening still in the uncertain future, the strong hands holding UST are not anxious to sell.



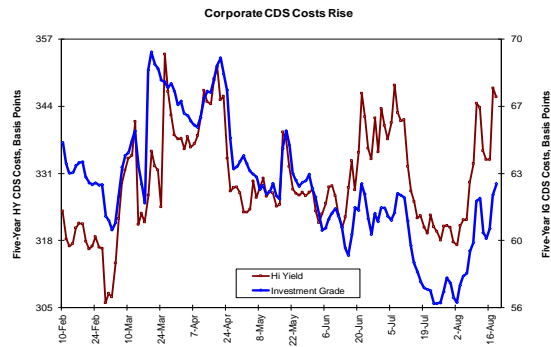
The pseudo-real yield curve declined across the maturity spectrum, with the strongest move at the mid-curve. The three-year remains negative. The shift is not as significant as it may appear as the market simply is pricing out some of its inflation protection taken out early in the year.



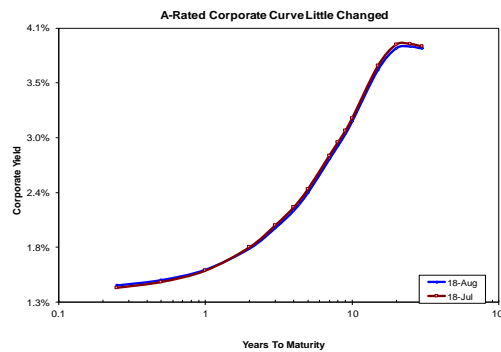
Swap spreads, which rise when floating-rate borrowers want to fix their payments, rose in the belly of the curve while shifting slightly higher at the long end.



CDS costs moved higher for both the investment-grade and high-yield indices. As growth remains firm and nothing yet has turned hostile in monetary policy, it is likely the upturns reflect correlation trades against equities.



The A-rated corporate yield curve barely has changed over the past month. This remains a bull market with limited upside potential.



Market Structure

Softs joined Grains, Natural Gas and Livestock in structural downtrends, while both Precious and Industrial Metals and Petroleum entered structural uptrends. The S&P 500 entered a downtrend.

	N-Day Speed	Market Structure	Trend Oscillator	HLC Volatility	Daily Trend Rate Aug. 21 - 25
BBerg	15	Transitional	-0.036	7.9%	
BBerg Grain	28	Trending	-0.344	18.5%	-0.52%
BBerg Ind. Metl	29	Trending	0.413	12.9%	0.30%
BBerg Pre. Metl	26	Trending	0.170	11.3%	0.20%
BBerg Softs	29	Trending	-0.241	16.5%	-0.91%
BBerg Nat. Gas	29	Trending	-0.049	17.0%	-0.11%
BBerg Petroleum	29	Trending	0.089	20.4%	0.40%
BBerg Livestock	29	Trending	-0.248	13.5%	-0.56%
Dollar Index	7	Sideways	-0.007	6.6%	
S&P 500 Index	29	Trending	-0.271	5.7%	-0.04%
EAFE Index	29	Trending	-0.078	7.7%	
EM Index	12	Transitional	-0.028	7.9%	
Ten-year UST (price)	26	Trending	0.126	4.0%	0.04%

Performance Measures

If you were long zinc and short coffee, you had a great week. Alternatively, you could have been short the grains, natural gas, precious metals and livestock and long the petroleum complex. The dispersion of returns amongst physical commodities is increasing.

	Commodity Total Returns			
	Five-Days	One Month	Six Months	One Year
Bloomberg Index	-0.54%	0.38%	-4.85%	-2.84%
Grains Sub-Index	-2.69%	-10.03%	-11.08%	-10.09%
Corn	-2.38%	-7.17%	-9.68%	-5.23%
Soybeans	-0.75%	-8.19%	-10.85%	-10.34%
Wheat	-5.23%	-16.38%	-12.42%	-17.30%
Energy Sub-Index	-0.38%	4.45%	-7.24%	-8.45%
Petroleum Sub-Index	0.18%	6.78%	-9.25%	-7.08%
WTI	-0.57%	6.06%	-12.90%	-11.08%
Brent	0.93%	7.93%	-10.23%	-7.84%
ULSD	-0.63%	6.91%	-4.06%	-2.20%
Gasoline	0.89%	5.78%	-5.49%	-1.63%
Natural Gas	-1.93%	-1.94%	-0.45%	-11.89%
Precious Metals Sub-Index	-0.22%	2.73%	0.80%	-7.45%
Gold	-0.17%	2.51%	3.52%	-5.02%
Silver	-0.38%	3.38%	-6.32%	-13.63%
Industrial Metals Sub-Index	2.28%	9.70%	6.13%	26.15%
Copper	0.99%	8.09%	6.02%	33.29%
Aluminum	0.91%	7.60%	8.28%	21.56%
Nickel	3.00%	15.27%	0.42%	4.46%
Zinc	7.95%	13.50%	8.04%	34.90%
Softs Sub-Index	-3.15%	-3.99%	-23.06%	-22.17%
Coffee	-8.43%	-5.82%	-17.86%	-15.04%
Sugar	1.61%	-6.80%	-35.97%	-34.61%
Cotton	-1.40%	-1.58%	-8.80%	-0.85%
Livestock Sub-Index	-2.22%	-6.85%	2.49%	5.97%
Cattle	-1.38%	-9.72%	4.07%	7.64%
Hogs	-3.62%	-1.55%	0.12%	3.29%

I commented last week those seeking a theme here would be disappointed as none exist. This came true this week as the EUR, GBP, CNY and CHF declined while the commodity-linked and Latin American currencies rose.

	Currency Returns			
	Five-Days	One Month	Six Months	One Year
Euro	-0.51%	1.79%	10.81%	3.58%
Chinese yuan	-0.10%	1.14%	3.12%	-0.59%
Japanese yen	0.01%	2.65%	3.59%	-8.51%
British pound	-1.11%	-1.30%	3.27%	-2.26%
Swiss franc	-0.29%	-1.02%	3.96%	-1.07%
Canadian dollar	0.73%	0.34%	4.14%	1.57%
Australian dollar	0.44%	0.16%	3.13%	3.16%
Swedish krona	0.03%	2.29%	10.10%	2.84%
Norwegian krone	0.32%	2.31%	5.47%	3.10%
New Zealand dollar	0.03%	-0.49%	1.71%	0.32%
Indian rupee	-0.01%	0.29%	4.33%	4.15%
Brazilian real	1.48%	0.30%	-1.89%	2.92%
Mexican peso	0.69%	-1.33%	15.03%	2.70%
Chilean peso	0.06%	1.41%	-0.78%	1.53%
Colombian peso	-0.34%	0.81%	-3.30%	-3.60%
Bloomberg-JP Morgan Asian dollar index (spot)	-0.03%	0.38%	2.39%	-0.70%

The almost inexplicable desire of the Federal Reserve to shrink its balance sheet combined with U.S. political turmoil to push U.S. equities lower. However, both the EAFE and EM indices posted gains.

	Equity Total Returns			
	Five-Days	One Month	Six Months	One Year
MSCI World Free	-0.31%	-1.24%	6.30%	14.26%
North America	-0.55%	-1.24%	3.86%	12.84%
Latin America	1.66%	2.70%	8.32%	15.33%
Emerging Market Free	1.64%	0.83%	14.84%	18.66%
EAFE	0.07%	0.03%	11.69%	15.79%
Pacific	-0.19%	0.21%	7.58%	14.33%
Eurozone	0.77%	0.81%	19.10%	24.64%

Both CTAs and hedge funds posted gains during a week when U.S. equities were down; this is a major exception to the usual pattern.

	CTA/Hedge Fund Returns			
	Five-Days	One Month	Six Months	One Year
Newedge CTA	1.01%	-0.46%	-7.02%	-12.73%
Newedge Trend	0.79%	0.07%	-3.84%	-8.83%
Newedge Short-Term	-0.15%	-0.84%	-2.57%	-11.25%
HFR Global Hedge Fund	0.11%	-0.43%	1.13%	4.45%
HFR Macro/CTA	0.50%	-0.05%	-0.42%	-3.11%
HFR Macro:	0.51%	0.21%	-2.46%	-6.84%
Systematic Diversified CTA				

Futures trading involves the substantial risk of loss and is not suitable for all investors. Each investor must consider whether this is a suitable investment since you may lose all of or more than your initial investment. Past performance is not indicative of future results.