

# Bedrock Friday May 27<sup>th</sup> Newsletter

On Tuesday buyers swarmed the two-year Treasury auction at the same time that market expectations for a Fed rate hike were building. The \$26 billion in two-year notes was auctioned at the highest yield since December — 0.92%. The ratio of bids to the amount offered was 3.00, well above the 2.64 at the last auction. Primary brokers took down only 18% of the auction, while indirect bidding was strong at 49.8% and direct bidding was at a multiyear high of 32.5%. The non-dealers have not taken that high a percent at auction for 13 years. Post auction, the two-year was yielding 0.90%. The strength of the auction of two-year notes was a surprise to traders, who had anticipated some weakness after the Fed started talking up a rate hike for this summer.

Peter Boockvar, chief strategist at The Lindsey Group, said the flattening curve and the auction combined could be a sign. The auction was underway as fed funds futures were pricing in a 40% chance for a June hike and a 68% chance of a July hike. Those levels were close to 30% and 60%, respectively, on Monday. The “spread” between the 10 year note and the two year is at 0.92% and the question is whether it is sending a signal, as a flattening curve often precedes a weaker economy or recession.

Current expectations are that the U.S. central bank will not enact its second post-Great Recession rate hike at the June Federal Open Market Committee meeting, after which there is a news conference, but rather July, where there is no scheduled session between Chair Janet Yellen and the press. If nothing else, such a move would strike a blow against conventional wisdom. From this side of the keyboard we would venture that the Fed is likely to make noises but not take any steps in June, leaving the decision and notification if any to July, once the result of the Brexit vote is known as will be its consequences.

Oil prices have been creeping upwards and are now hovering at the \$50/Bbl. level. Jefferies' Jason Gammel said on Monday that the oil market had swung from oversupply to undersupply in April thanks to disruptions in production in Nigeria and Alberta, Canada, taking around 2 million barrels per day out of the market. As global crude output fell, demand from China — a massive consumer of energy — rose in April. Its crude imports reached 8 million barrels a day, up 7.6% from a year earlier, according to official Chinese data cited by Reuters on Monday. The stage has been set for a fundamental price recovery as per Jefferies... On Tuesday, Citigroup said the worst was over for the beleaguered oil market, which has seen prices tumble from \$114 a barrel in mid-2014 to around \$26 a barrel in early 2016 due to a glut in supply and the failure of demand to keep pace. Citi upped its forecasts for Brent to reach \$65 a barrel in 2017. The thinking we read seems to point to a slow grinding upwards of oil prices into the rest of this year. What does this mean for markets? For inflation? The energy producing sector is the only clear winner if indeed this view does materialize.

Perhaps we should look at the equities for a second opinion? Closely followed market-watcher Dennis Gartman, the founder and publisher of the Gartman Letter, mentioned the early week's market gains could continue for the next couple of weeks. "Anybody who's short — and there are a lot of smart people who are in fact heavily short — they have to run for cover, and I think it could get ugly," he added. Perhaps the ignition of this leg in the equity rally can be found in the Tuesday “New Greek Aid Package”. Or might it be assigned to the good new home sales data out of the US?

The S&P 500 should soon hit a record high due to a number of positive forces coming together, closely followed market watcher Jim Paulsen said Thursday, following the best two-day rally on Wall Street since March. Economic growth, not only in the U.S. but around the world, is picking up in a "synchronized" fashion, and deflationary concerns are fading, so maybe, just maybe we will cross the 'resistance' of the all-time-highs? The S&P 500 index is 1.8% below its historic highs...

A couple of scary thoughts come to cloud this newfound optimism - Donald Trump is now the official GOP candidate and the latest polls show him ahead of the presumed Democrat candidate Hillary Clinton. We find it difficult to be enthusiastic on either candidate winning...

Then, a whiff of 2008 drifted through our thoughts when we saw the headline “Wells Fargo launches 3% down payment mortgage”... And Barclays bank in the UK announced 100% mortgage financing... We learn, we forget, we learn again... then read the Wells Fargo release, "We are fully underwriting the borrowers, we are partnering with Fannie Mae to originate and sell these loans..." is truly scary; back to the future? What happened to Dodd-Frank?

To top off our worries we read that the US military uses 8-inch floppy disks to coordinate nuclear force operations. The Defence Department's 1970s-era IBM Series/1 Computer and long-outdated floppy disks handle functions related to intercontinental ballistic missiles, nuclear bombers and tanker support aircraft, according to the new Government Accountability Office report.

Buddha was right in saying that we're not actually in control... and that was from before the floppy...

## Market Weekly Highlights:

- The Dollar remained unchanged on the week, with the USD Index (DXY) trading at 95.25. The US\$ is now trading at about \$1.1120 against the EUR and at 0.99 against the Swiss Franc. The Pound is higher on the week at 1.4665. The Japanese Yen has regained a little ground and is now 109.70. We maintain our belief in the fundamental relative strength of the US\$ - this view is driven by the outlook for interest rates to hold or rise further in the US and hold or decline elsewhere. We note that WTI Oil has rallied again to above \$50, having dropped a little on USD strength to trade now at \$49.10; whilst Brent now trades at a DISCOUNT to WTI at \$49.00/Bbl. The Russian Ruble strengthened in line with oil price moves and is now at 65.90 per USD. The Brazilian Real had remained steady at 3.60. We do not see a further significant rally in the Real.
- The yield for the US 10Yr Treasury is marginally lower for the week at 1.82% as the street may be coming closer to a possible June rate rise from the Fed which was reflected in the flattening of the curve. The German 10Yr Bund yield is down for the week to 0.12%. Whilst the Spanish 10Yr yield is at 1.48%. The Italian 10Yr yield has dropped for the week to around 1.35%. In the UK, the Gilts' yields moved higher on the week from 1.42% to 1.49% only to reverse course as we write to 1.41%. The Swiss 10Yr yield has also dropped marginally to -0.31%.
- This week was generally positive for equities, both European and US. The S&P500 was up 1.84% for the week. The Dow Jones bounced by 1.87% and NASDAQ at +2.77% with all markets looking to open up about 0.2%. The DAX is trading +3.68% for the week, the CAC40 is now +3.67%, with the SMI at +3.62%, the UK FTSE trading at +1.83% and EuroStoxx50 at +3.87% as we write. In Asia, the Nikkei has closed the week at +0.59%, whilst the Shanghai Composite and the Hang Seng Index closed down 0.16% and up 3.65% respectively.

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Highlighted items are interesting data points for the week

## MARKET INDICES PERFORMANCE

26/05/2016

INDEX NAME	CCY	Last Price	PRICE CHANGE IN % (unless indicated)									P/E
			1D	5D	MTD	1M	3M	6M	YTD	1Y	3Y	
EQUITY MARKET INDICES - BY REGION												
S&P 500 INDEX	USD	2090.1	-0.01	2.45	1.20	-0.24	7.29	0.00	2.26	-1.57	26.70	17.12
DOW JONES INDUS. AVG	USD	17828.29	-0.13	2.25	0.31	-1.18	7.14	0.17	2.31	-1.84	16.50	16.63
NASDAQ COMPOSITE INDEX	USD	4901.766	0.15	4.02	2.65	0.79	6.78	-4.40	-2.11	-4.01	41.70	16.02
RUSSELL 2000 INDEX	USD	1139.754	-0.10	4.11	0.79	-1.25	9.89	-5.21	0.34	-9.14	15.80	17.52
EURO STOXX 50	EUR	3071.21	0.40	3.36	1.10	-2.20	4.52	-12.25	-6.30	-16.87	9.54	14.13
EURO STOXX 600	EUR	348.91	0.13	2.97	1.93	-0.07	4.98	-9.28	-4.85	-14.87	14.37	15.90
CAC 40 INDEX	EUR	4512.64	0.69	3.22	1.47	-1.44	4.16	-8.85	-3.09	-13.29	12.48	15.00
DAX INDEX	EUR	10272.71	0.66	3.34	2.08	-0.51	7.72	-9.27	-4.61	-12.95	22.24	12.87
FTSE 100 INDEX	GBP	6265.65	0.06	1.67	0.27	-0.97	2.67	-1.82	0.27	-11.01	-5.94	16.86
SWISS MARKET INDEX	CHF	8229.55	0.76	3.31	3.78	2.04	4.89	-8.23	-6.31	-12.07	1.21	17.32
NIKKEI 225	JPY	16772.46	0.09	0.59	1.01	-2.64	3.99	-15.33	-11.55	-17.77	19.04	16.39
HANG SENG INDEX	HKD	20397.11	0.14	3.58	-2.39	-3.74	6.19	-6.82	-6.16	-26.77	-9.36	10.89
SHANGHAI SE COMPOSITE	CNY	2822.443	0.26	-0.16	-3.99	-4.49	1.95	-17.90	-20.29	-42.91	23.02	12.56
S&P BSE SENSEX INDEX	INR	26366.68	1.88	4.91	3.66	1.84	14.64	1.59	1.64	-3.70	32.52	16.93
RUSSIAN RTS INDEX \$	USD	918.79	1.21	3.12	-3.17	-0.66	21.58	7.55	21.65	-9.02	-33.51	6.82
BRAZIL IBOVESPA INDEX	BRL	49482.86	0.28	-2.13	-8.21	-6.78	18.97	4.96	14.15	-7.73	-12.27	12.41
MSCI WORLD	USD	1672.12	0.21	1.97	0.08	-0.82	7.57	-1.66	0.56	-6.77	12.25	16.40
MSCI WORLD HEDGED	USD	722.219	0.09	2.65	1.35	-0.07	7.14	-2.14	0.37	-4.49	24.69	-
MSCI WORLD LOCAL	-	1266.807	0.08	1.79	1.01	-0.56	6.22	-3.40	-0.85	-7.35	17.78	-
MSCI AC WORLD	USD	401.81	0.23	2.00	-0.38	-1.22	7.66	-1.77	0.61	-8.33	8.04	15.81
MSCI EM	USD	802.93	0.41	2.25	-4.43	-4.77	8.50	-2.84	1.11	-21.21	-21.93	11.81
MSCI AC ASIA x JAPAN	USD	487.39	0.35	2.40	-3.00	-4.16	6.04	-4.10	-2.51	-21.65	-11.47	11.99
MSCI EM LATIN AMERICA	USD	2076.09	0.41	0.77	-9.42	-8.30	16.79	4.19	13.46	-18.18	-42.84	14.54
MSCI EM Eur, ME & Africa	USD	226.26	0.61	2.77	-7.10	-5.35	12.14	-1.45	7.64	-19.99	-31.67	10.96
EQUITY MARKET INDICES - BY SECTOR												
MSCI ENERGY	USD	197.57	-0.16	1.66	-1.99	-2.89	15.01	0.37	10.78	-15.35	-22.57	27.06
MSCI MATERIALS	USD	199.56	0.20	1.68	-3.67	-2.71	13.57	3.81	8.06	-14.77	-10.84	18.93
MSCI INDUSTRIALS	USD	198.99	0.32	1.49	-1.03	-1.89	7.59	0.65	3.74	-4.25	14.76	16.55
MSCI CONS DISCRETIONARY	USD	189.04	0.45	1.65	-0.93	-1.50	5.14	-5.05	-2.37	-6.22	21.83	15.75
MSCI CONS STAPLES	USD	217.15	0.48	1.64	0.84	0.76	5.05	4.10	4.20	4.89	17.85	21.42
MSCI HEALTH CARE	USD	202.28	0.06	1.84	0.63	-0.93	4.76	-3.39	-3.77	-8.86	31.23	16.39
MSCI FINANCIALS	USD	93.26	-0.09	2.54	0.10	-1.19	10.11	-5.95	-3.88	-12.16	1.73	12.98
MSCI INFO TECH	USD	146.09	0.25	2.80	3.59	1.64	7.11	-2.47	-0.20	-2.51	38.78	17.44
MSCI TELECOMS	USD	71.58	0.37	1.35	-0.29	-0.58	4.44	4.62	5.37	-0.29	13.37	15.50
MSCI UTILITY	USD	118.79	0.91	1.21	-1.05	-0.45	5.48	7.46	6.38	0.09	8.69	16.35
MSCI WORLD REAL ESTATE	USD	196.39	0.27	1.24	-0.37	-0.89	8.54	3.12	3.46	-1.65	4.18	23.18
HEDGE FUND INDICES												
HFRX GLOBAL HEDGE FUND	USD	1159.54	0.34	0.63	0.24	0.24	2.08	-2.58	-1.24	-7.37	-3.62	-
HFRX EQUAL WEIGHTED	USD	1169.59	0.28	0.44	0.46	0.57	2.31	-1.26	-0.27	-4.22	-0.63	-
HFRX GLOBAL EUR	EUR	1055.46	0.34	0.62	0.14	0.11	1.65	-3.29	-1.84	-8.39	-5.54	-

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26/05/2016

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FIXED INCOME INDICES - YIELD ON US GOVERNMENT BONDS (Change in bps)												
US 3 MONTH	USD	0.2899	1.76	-0.02	0.08	0.06	-0.02	0.12	0.13	0.28	-	-
US 2 YEAR	USD	0.875	0.91	0.00	0.09	0.06	0.08	-0.04	-0.17	0.23	-	-
US 10 YEAR	USD	1.8284	0.00	-0.01	0.00	-0.02	0.07	-0.39	-0.44	-0.30	-	-
FIXED INCOME INDICES - BY TYPE OF ISSUER												
GLOBAL AGG TR HEDGED	USD	498.9918	0.18	0.24	0.40	0.59	1.59	3.58	3.87	4.25	11.96	1.37
US GOVERNMENT TR	USD	2158.6	0.28	0.14	0.03	0.30	0.19	2.90	3.05	3.23	6.60	1.37
US CORPORATE TR	USD	2705.83	0.43	0.44	-0.09	0.21	4.35	4.54	5.30	3.78	10.23	3.13
US HIGH YIELD TR	USD	1671.06	0.12	0.77	0.47	0.89	9.67	5.37	7.91	-0.89	8.14	7.31
EU GOVERNMENT TR	EUR	250.4815	0.01	0.43	1.01	1.05	0.74	2.05	3.20	3.75	18.08	0.39
EU CORPORATE TR	USD	253.6485	0.09	0.30	0.35	0.31	2.47	2.68	3.50	2.82	12.33	1.04
EU HIGH YIELD TR	EUR	282.4823	0.15	0.60	0.05	0.02	6.06	2.06	4.07	1.74	16.81	4.37
BARCLAYS GLOBAL CONVERT.	USD	213.18	0.12	1.46	0.61	-0.01	5.24	-1.78	0.16	-6.44	10.53	-
GLOBAL EM TR (HEDGED)	USD	343.9515	0.10	0.22	0.01	0.35	4.96	4.39	6.06	3.06	9.31	4.87
S&P/LSTA U.S. LEV LOAN	USD	90.98335	0.04	0.30	0.19	0.21	5.36	1.99	3.73	-5.65	-7.81	5.68
COMMODITY INDICES - BY TYPE OF ISSUER												
GSCI INDEX TOTAL RETURN	USD	2386.835	0.25	1.27	2.39	4.94	19.77	-1.74	9.96	-24.99	-49.01	-
GSCI ENERGY TR	USD	417.066	-0.32	1.48	4.80	8.61	33.52	-7.29	13.24	-35.55	-60.13	-
GSCI INDUSTRIAL METALS TR	USD	964.827	0.78	0.88	-7.48	-5.63	-0.46	4.45	1.05	-19.88	-30.78	-
GSCI PRECIOUS METALS TR	USD	1499.113	-0.23	-2.57	-5.74	-2.16	1.06	14.21	15.42	1.83	-15.04	-
GSCI AGRICULTURE TR	USD	485.8617	1.24	2.99	2.24	2.70	12.75	5.89	7.95	3.62	-30.87	-
GENERIC 1ST 'CL' FUTURE	USD	49.48	-0.87	1.32	5.30	6.65	34.02	-2.50	10.05	-30.20	-53.42	-
GOLD SPOT \$/OZ	USD	1219.8	0.27	-2.32	-5.41	-1.83	0.03	15.67	15.23	2.95	-12.31	-
CURRENCIES												
DOLLAR INDEX SPOT	USD	95.16801	0.06	-0.11	2.30	0.89	-2.98	-4.79	-3.45	-2.20	13.77	-
Euro Spot	EUR	1.1194	-0.10	-0.37	-2.34	-1.23	2.85	5.57	2.96	2.56	-13.52	-
Japanese Yen Spot	JPY	109.76	-0.03	0.33	-3.00	1.52	2.64	11.85	9.50	12.63	-8.04	-
British Pound Spot	GBP	1.467	0.09	1.25	0.49	0.96	5.50	-2.35	-0.36	-4.37	-2.76	-
Swiss Franc Spot	CHF	0.9893	-0.07	0.03	-3.04	-1.91	0.85	4.06	1.22	-4.10	-2.72	-
Brazilian Real Spot	BRL	3.5835	-0.33	-0.51	-4.12	-0.71	10.41	4.52	10.53	-13.57	-42.75	-
China Renminbi Spot	CNY	6.5585	0.00	-0.15	-1.23	-0.93	-0.10	-2.51	-0.99	-5.45	-6.67	-
Singapore Dollar Spot	SGD	1.3736	-0.10	0.49	-2.24	-1.87	2.30	2.80	3.16	-1.75	-8.30	-
Norwegian Krone Spot	NOK	8.2788	-0.11	0.49	-2.86	-1.52	4.89	5.05	6.70	-6.27	-29.46	-
VOLATILITY / LIQUIDITY INDICES												
CBOE SPX VOLATILITY INDEX	USD	13.43	-3.38	-11.12	-13.95	-1.89	-31.80	-10.65	-25.81	1.81	-3.43	-
USD SWAP SPREAD SEMI 2YR	USD	13.9	-	2.06	2.36	18.13	152.82	122.08	16.84	-40.04	-7.47	-
TED SPREAD	USD	38.92	-	10.01	-9.09	-0.28	19.83	62.98	-13.51	41.12	64.01	-

All data is compiled from Bloomberg

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