

# Bedrock Friday June 17<sup>th</sup> Newsletter

It is Friday again and we are mid-June. Here at least, it feels like autumn. Global warming they say? Why is it so cold then? But we did have an interesting week- We had the Federal Reserve telling us that they decided to hold interest rates steady, we saw German bund-yields turn negative (a first!), we saw a spike of the VIX as the world suddenly awoke to the meaning of BREXIT risks (UK polls went in favour of Exit), then a Member of Parliament in the UK was murdered and the mood on BREXIT changed.

Well, yesterday Goldman Sachs showed an analysis whereby they predict that the Pound Sterling would fall by 11% (amazing precision, no?) if BREXIT were to happen. The Swiss National Bank followed Janet Yellen in announcing that they elected to hold Swiss interest rates unchanged, adding that "Negative Rates are essential at this time". The market is talking more and more of the possibility that the Fed might be forced to switch tact and go negative as well. It's an inevitable question: Could U.S. 10-year yields turn negative now that German 10-year yields have fallen below zero for the first time ever and Japanese 10-year yields have dipped to record lows of negative 0.17%? According to Dennis Davitt, partner at Harvest Volatility Management and a noted options market veteran, it may well happen. "I think you could see negative rates in the U.S. If Germany and other countries in the world go even further negative, it turns into a number line game. So where zero lies on the number line, who knows?" Davitt said Tuesday. Other strategists, like Larry McDonald of ACG Analytics, say negative U.S. yields are unlikely, since central banks around the world will soon change course due to the failure of the policies to spur growth. One thing is clear though- The Fed's credibility is eroding... how many times can they "cry wolf" and remain believable? We remember with growing fondness the thundering Fed Silence from The Greenspan and Volker eras. Do what is needed, don't talk of it...

Fed officials lowered their expectations for future years, now looking for the funds rate to rise to 1.6% in 2017, as opposed to the 1.9% estimate in March, and to 2.4% in 2018, from a 3.0% estimate previously. The committee did raise its inflation estimates, upping the headline number for 2016 from 1.2% to 1.4%. Well, if indeed they believe that inflation will continue to run below their target level of 2%, WHY ON EARTH would they raise rates? We hold our long-standing view that the world in general and the US in particular is to remain in this extremely low interest rate environment for a very long time. Some are saying that the Fed should stop looking at their computer screens and models and actually go out and see reality. Perhaps they will stop talking so much? Traders tracked by the CME now see about a 26% chance of a September rate hike. They sat at a 35% chance before the statement.

The yield on the 10-year benchmark German bund fell into negative territory for the first time ever on Tuesday morning, amid global growth concerns and jitters over the U.K.'s upcoming referendum on its European Union membership. The move comes as the European Central Bank has ramped up its bond buying program in recent months. Moves in some bond markets have been even more extreme. The 10-year Japanese government bond yield is at a record low of minus 0.20%. The 10 year US Treasury Notes now yield 1.60%, having touched 1.51% yesterday. Interesting week indeed!

Bond guru Bill Gross believes the growing global move toward negative yields will have dire consequences. In a tweet from his firm, Janus Capital, Gross goes back half a millennium to assert that the current situation with the world's debt market is unprecedented and dangerous: "Global yields lowest in 500 years of recorded history. \$10 trillion of neg. rate bonds. This is a supernova that will explode one day"...

Polls say Brexit is likely, but the betting markets say it isn't. A week ago Friday, a poll for the Independent newspaper gave a massive 10-point lead to the British voting public that want to leave the European Union. Over the weekend, another poll for The Times newspaper gave leave vote a small lead. A Financial Times Poll of Polls gives leave a lead as well — 46%, versus stay at 44%.

Furthermore, while Great Britain's vibrant wagering markets have shown the momentum build on the leave side, they still show a significant preference for remain. The latest odds on Monday — 4-7 for stay vs. 7-4 for leave — imply a Brexit probability of 36%!

Wonderful statistics, but in truth, since the beginning of this process which started in February this year when Cameron set the date for a referendum, the real odds have been and remain at 50/50, as the outcome is binary. Based on observing the FX market, renowned trader Jon Najarian says "if you examine the pound's movement over recent months, all signs point to a vote by Britain to stay". As we all prefer stability to volatility, let's hope he reads the FX tea-leaves well...

Away from BREXIT, the Fed and other distractions, we have observed strange trading in oil- When oil initially rallied to \$50 there was a surge of optimism in the oil patch, confirmed by the commentary from Continental Resources CEO Harold Hamm, who suggested that oil could travel back to the \$60 to \$70 range. Since that time, selling pressure has pushed the price of oil back down. As we write, WTI is at \$46 and Brent at \$47.

Let's not forget Robert Burns words "There is no such uncertainty as a sure thing"...

## Market Weekly Highlights:

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- The Dollar is down on the week; with the USD Index (DXY) trading at 94.38 down 4.30% YTD. The US\$ is now trading at about \$1.1255 against the EUR and at 0.9621 against the Swiss Franc. The Pound has slipped further as the risk of Brexit appears to grow and now trades at 1.4296. We maintain our belief in the fundamental relative strength of the US\$ with a risk of some further short term declines - this view is driven by the outlook for short-dated interest rates to hold or rise further in the US and hold or decline elsewhere. The Japanese Yen is stronger at 104.27 on the general decline of the US\$. Gold is up some \$50 up for the week, now trading at \$1'285 on the back of the \$ fall. We note that WTI Oil has slipped somewhat to trade now at \$46.73/Bbl of WTI whilst Brent is trading at about \$47.92/Bbl. The Russian Ruble is somewhat weaker at 65.44 per USD as the oil prices dropped. The Brazilian Real weakened this week against a soft US\$ and is trading at or around 3.46. The geopolitical risk and economic outlook in Brazil does not give us comfort in the rapid strengthening of Real; however we are closely monitoring the events which might trigger a more confident view towards this currency.
- This week we listened to Janet Yellen tell us that the FOMC decided to hold steady on rates for now. She further used dovish language to attenuate market expectations of rises into the future. She invoked global economic weakness and risks from Brexit and others. The long-end of the US Treasury curve rallied and yields fell further, the Dollar responded with a drop. We note that the yield on the benchmark US 10 year note is at 1.59% (down some 7% on the week), with the Japanese 10 year JGB at NEGATIVE 19Bps, the German Bund at NEGATIVE 0.16% and the Swiss at NEGATIVE 0.50%. The Italian 10Yr yield has started the week at 1.40 to reach almost 1.58 and is now trading down at around 1.51%. The Spanish 10Yr yield moved on a similar path trading from 1.45% to 1.63% to only trade at around 1.56% as we write. In the UK, the Gilts' yields continued to move lower on the week from 1.21% to 1.07% yesterday and now are at 1.146% as we write.
- This week was negative for equities globally. The S&P500 is down 1.77% for the week so far. The Dow Jones down by 1.40% while NASDAQ at -2.29% with all markets looking to open slightly up. The DAX is trading -1.53% for the week, the CAC40 is now -2.13%, with the SMI at -2.00%, the UK FTSE trading at -1.30% and EuroStoxx50 at -1.60% as we write. In Asia, the Nikkei has closed the week at -6.03%, whilst the Shanghai Composite and the Hang Seng Index closed down 1.44% and down 4.15% respectively.

Highlighted items are interesting data points for the week

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## MARKET INDICES PERFORMANCE

16/06/2016

INDEX NAME	CCY	Last Price	PRICE CHANGE IN % (unless indicated)									P/E
			1D	5D	MTD	1M	3M	6M	YTD	1Y	3Y	
<b>EQUITY MARKET INDICES - BY REGION</b>												
S&P 500 INDEX	USD	2077.99	0.33	-1.77	-0.90	1.50	1.83	1.77	1.67	-1.07	26.78	17.00
DOW JONES INDUS. AVG	USD	17733.1	0.54	-1.40	-0.30	1.16	1.44	1.36	1.77	-1.13	16.82	16.49
NASDAQ COMPOSITE INDEX	USD	4944.915	0.21	-2.29	-2.08	2.74	1.46	-3.15	-3.25	-4.34	40.35	18.24
RUSSELL 2000 INDEX	USD	1148.191	-0.09	-2.79	-0.57	4.80	5.22	1.13	1.08	-9.47	16.23	17.71
EURO STOXX 50	EUR	2819.3	-0.39	-1.99	-0.86	-2.89	-8.24	-13.71	-12.68	-16.79	5.57	13.21
EURO STOXX 600	EUR	321.29	-0.71	-2.25	-8.33	-2.77	-4.47	-10.81	-11.04	-15.19	10.98	14.88
CAC 40 INDEX	EUR	4153.01	-0.45	-2.59	-0.89	-2.38	-5.57	-10.31	-9.53	-12.43	8.58	14.03
DAX INDEX	EUR	9550.47	-0.59	-1.85	-5.94	-2.40	-2.42	-10.11	-10.15	-12.07	17.49	12.12
FTSE 100 INDEX	GBP	5950.48	-0.26	-1.85	-3.68	-2.67	-3.20	-1.83	-3.84	-10.14	-5.18	16.02
SWISS MARKET INDEX	CHF	7634.66	-0.58	-2.28	-5.76	-2.07	-1.51	-10.55	-12.19	-13.06	0.18	16.53
NIKKEI 225	JPY	15434.14	-3.05	-6.03	-9.49	-6.32	-7.89	-19.40	-18.04	-22.85	19.69	15.41
HANG SENG INDEX	HKD	20038.42	-1.85	-4.37	-3.32	0.03	-1.85	-7.99	-8.17	-24.78	-5.19	10.96
SHANGHAI SE COMPOSITE	CNY	2872.817	-0.46	-1.44	-1.08	1.46	-0.88	-19.41	-18.48	-41.93	33.80	12.84
S&P BSE SENSEX INDEX	INR	26525.46	-0.62	0.01	-0.11	3.36	7.95	3.24	2.00	-0.72	37.84	17.10
RUSSIAN RTS INDEX \$	USD	895	-1.63	-4.79	0.11	-2.83	3.61	14.30	19.59	-6.33	-31.10	7.06
BRAZIL IBOVESPA INDEX	BRL	49411.62	1.02	-3.34	1.94	-2.81	-2.95	9.17	13.98	-7.21	0.66	12.38
MSCI WORLD	USD	1628.13	-0.33	-2.23	-2.78	-0.82	-1.64	-2.08	-2.08	-7.60	10.23	15.97
MSCI WORLD HEDGED	USD	702.526	-0.23	-3.21	-3.14	-1.03	0.30	-2.50	-2.38	-5.88	25.54	-
MSCI WORLD LOCAL	-	1230.984	-0.24	-2.02	-3.22	-0.78	-0.92	-3.41	-3.66	-7.70	17.22	-
MSCI AC WORLD	USD	392.14	-0.40	-2.30	-2.59	-0.78	-1.02	-1.46	-1.81	-8.83	7.12	15.45
MSCI EM	USD	799.78	-0.98	-2.92	-0.95	-0.23	-2.10	0.15	0.71	-17.50	-16.44	12.06
MSCI AC ASIA x JAPAN	USD	487.85	-1.03	-2.90	-1.31	0.70	-1.54	-2.31	-2.42	-17.16	-5.50	12.37
MSCI EM LATIN AMERICA	USD	2072.41	0.15	-5.15	1.88	-3.22	-3.10	9.45	13.26	-18.20	-36.88	14.47
MSCI EM Eur, ME & Africa	USD	219.11	-1.89	-4.73	-2.14	-2.52	-4.81	3.44	4.23	-18.77	-29.63	10.52
<b>EQUITY MARKET INDICES - BY SECTOR</b>												
MSCI ENERGY	USD	194.05	-0.48	-2.33	-0.91	-1.27	1.93	10.19	8.81	-14.95	-23.12	28.98
MSCI MATERIALS	USD	195.2	-0.84	-2.67	-1.52	-2.24	0.87	7.94	5.70	-14.46	-11.64	18.39
MSCI INDUSTRIALS	USD	194.64	-0.55	-2.32	-2.37	-1.58	-0.98	2.24	1.48	-4.24	12.77	16.14
MSCI CONS DISCRETIONARY	USD	183.83	-0.35	-1.82	-3.16	-1.25	-3.17	-5.13	-5.06	-7.54	18.68	15.40
MSCI CONS STAPLES	USD	215.05	0.00	-1.71	-0.83	-0.14	-0.21	3.69	3.19	5.85	18.58	21.09
MSCI HEALTH CARE	USD	198.9	-0.30	-2.25	-2.16	0.20	4.13	-4.54	-5.38	-9.13	30.36	16.15
MSCI FINANCIALS	USD	87.5	-0.60	-3.54	-6.18	-2.94	-4.40	-9.54	-9.81	-16.77	-3.54	12.13
MSCI INFO TECH	USD	143.96	0.01	-1.17	-2.26	2.35	-0.42	-1.96	-1.65	-1.78	36.51	17.18
MSCI TELECOMS	USD	69.99	-0.09	-1.93	-2.36	-2.28	-3.21	3.66	3.03	-0.57	12.56	15.04
MSCI UTILITY	USD	119.42	0.00	-1.48	0.13	0.76	0.30	7.75	6.94	4.50	11.06	16.51
MSCI WORLD REAL ESTATE	USD	196.61	-0.20	-1.21	-0.16	-0.07	0.02	4.13	3.57	2.37	10.65	22.62
<b>HEDGE FUND INDICES</b>												
HFRX GLOBAL HEDGE FUND	USD	1162.24	0.08	-0.86	0.01	0.87	1.68	-0.86	-1.01	-6.54	-2.26	-
HFRX EQUAL WEIGHTED	USD	1174.76	0.08	-0.41	0.24	0.88	2.23	0.44	0.17	-3.46	0.54	-
HFRX GLOBAL EUR	EUR	1056.95	0.08	-0.86	-0.07	0.75	1.27	-1.44	-1.70	-7.62	-4.29	-

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			1D	5D	MTD	1M	3M	6M	YTD	1Y	3Y	
<b>FIXED INCOME INDICES - YIELD ON US GOVERNMENT BONDS (Change in bps)</b>												
US 3 MONTH	USD	0.2492	-2.01	0.01	-0.04	-0.04	-0.03	0.03	0.09	0.25	-	-
US 2 YEAR	USD	0.6627	1.07	-0.03	-0.18	-0.14	-0.17	-0.29	-0.36	0.04	-	-
US 10 YEAR	USD	1.8027	0.02	-0.04	-0.24	-0.17	-0.29	-0.82	-0.87	-0.71	-	-
<b>FIXED INCOME INDICES - BY TYPE OF ISSUER</b>												
GLOBAL AGG TR HEDGED	USD	504.9979	0.11	0.28	1.18	1.17	2.34	5.07	5.12	6.69	14.18	1.23
US GOVERNMENT TR	USD	2193.16	0.17	0.48	1.63	1.33	2.28	4.49	4.70	5.53	8.97	1.23
US CORPORATE TR	USD	2746.9	0.17	0.12	1.50	1.38	4.16	6.68	6.89	6.81	14.02	2.97
US HIGH YIELD TR	USD	1673.59	-0.37	-0.99	0.01	0.78	4.79	8.43	8.07	0.32	10.26	7.40
EU GOVERNMENT TR	EUR	252.0217	-0.04	-0.24	0.65	0.81	1.15	3.64	3.84	6.90	19.65	0.37
EU CORPORATE TR	USD	255.4911	-0.04	-0.07	0.66	0.83	2.02	4.25	4.25	5.44	14.27	0.96
EU HIGH YIELD TR	EUR	281.3159	-0.32	-1.11	-0.61	0.11	1.98	3.01	3.64	3.28	18.28	4.49
BARCLAYS GLOBAL CONVERT.	USD	211.11	-0.21	-1.93	-1.36	0.24	1.24	-0.38	-0.82	-6.61	10.87	-
GLOBAL EM TR (HEDGED)	USD	347.2847	0.05	-0.27	0.94	0.57	3.61	7.14	7.08	5.98	13.64	4.78
S&P/LSTA U.S. LEV LOAN	USD	90.96148	-0.14	-0.26	-0.03	0.31	2.61	4.43	3.71	-4.71	-7.03	5.79
<b>COMMODITY INDICES - BY TYPE OF ISSUER</b>												
GSCI INDEX TOTAL RETURN	USD	2344.725	-2.22	-5.47	-1.60	-0.71	8.36	9.41	8.02	-26.49	-50.90	-
GSCI ENERGY TR	USD	395.147	-3.39	-8.36	-5.07	-3.37	11.30	8.30	7.29	-39.75	-63.32	-
GSCI INDUSTRIAL METALS TR	USD	973.71	-1.72	0.28	0.48	0.65	-0.53	4.88	1.98	-15.32	-28.96	-
GSCI PRECIOUS METALS TR	USD	1594.735	0.76	2.02	7.03	1.84	6.38	20.69	22.78	9.47	-9.35	-
GSCI AGRICULTURE TR	USD	507.5473	-0.76	-2.32	5.48	6.52	12.57	11.87	12.76	8.40	-27.53	-
GENERIC 1ST 'CL' FUTURE	USD	46.21	1.08	-4.81	-4.87	-4.82	6.11	7.26	4.80	-35.73	-57.12	-
GOLD SPOT \$/OZ	USD	1278.46	0.44	0.80	5.66	0.40	2.08	22.16	20.98	8.31	-7.31	-
<b>CURRENCIES</b>												
DOLLAR INDEX SPOT	USD	94.56901	-0.04	-0.05	-1.42	-0.02	-0.24	-4.78	-4.16	0.25	17.01	-
Euro Spot	EUR	1.1225	0.28	0.04	1.11	-0.50	-0.55	3.97	3.63	-0.71	-15.79	-
Japanese Yen Spot	JPY	104.26	-0.03	2.57	6.18	4.65	6.81	17.52	15.27	18.35	-9.38	-
British Pound Spot	GBP	1.4203	0.49	0.11	-1.46	-1.32	-1.45	-4.22	-3.15	-9.86	-9.22	-
Swiss Franc Spot	CHF	0.985	0.11	0.10	3.11	1.72	0.38	3.35	3.96	-4.35	-4.28	-
Brazilian Real Spot	BRL	3.466	0.23	-1.90	4.20	1.02	7.98	12.07	14.28	-10.88	-37.92	-
China Renminbi Spot	CNY	6.5915	0.06	-0.38	-0.03	-1.02	-1.67	-1.58	-1.42	-5.74	-7.03	-
Singapore Dollar Spot	SGD	1.3488	-0.10	0.76	2.04	1.43	-0.01	5.07	5.07	-1.05	-7.04	-
Norwegian Krone Spot	NOK	8.3603	0.22	-1.17	0.09	-2.27	-0.59	4.72	5.63	-8.53	-31.62	-
<b>VOLATILITY / LIQUIDITY INDICES</b>												
CBOE SFX VOLATILITY INDX	USD	19.37	-3.82	14.03	36.86	24.73	34.49	2.53	6.04	33.93	15.60	-
USD SWAP SPREAD SEMI 2YR	USD	14.76	-	6.28	-2.16	24.52	115.13	47.09	25.67	-42.86	-8.40	-
TED SPREAD	-	39.23	-	-3.73	-2.15	8.49	14.04	38.48	-12.82	39.51	68.95	-

All data is compiled from Bloomberg

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