rareview macro

sight beyond sight ®

by Neil Azous

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## Risk-Adjusted Return Monitor

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| USD/PHP | USD/PHP | Australia Bank Bills | Taiwan TWSE | Corn |
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*Highlights the largest positive and negative risk-adjusted returns overnight.

## Summary & Views

### One Last Question on Stocks Before the FOMC Meeting…Yuan, Crude Oil, Sweden in Focus

- Chinese Yuan – A New Hedge to a US Dollar Correction?
- Long Crude Oil – Adding to Watch List
- Sweden – Negative Deposit Rates & Larger QE

Despite many players in the professional investment community waiting on today's FOMC meeting, including us, there were still plenty of other moving parts overnight worth highlighting.

We walk into the meeting short both US fixed income and equities. We leave you with this narrative and key question:

If the consensus has grown to believe that the year-on-year S&P 500 earnings are now negative and the Federal Reserve is about to make a policy error why is the Russell 2000 (symbol: IWM) at new highs? Our point is that everyone can explain why the Fed will start some proper correction or say negative earnings are consensus and even display a basket of multi-national stocks down a lot on the year. But high grade credit is not worried, neither really are investors or sentiment would be a lot different. Which gets to our main question. If we accept earnings will be disappointing, even if the Fed just removes patient but has a cautious tone, why do stocks really rally? It would seem to us there would be plenty of supply at higher prices.

**Chinese Yuan – A New Hedge to a US Dollar Correction?**

The focus in China today, following the release of housing data, is not on the continued cleansing process in that market, even though despite February being the first time the price picture has worsened on a sequential basis since August. Much like the impact of the winter weather on the US economy, any distortion will simply be viewed as short-term seasonal fluctuation (i.e. Lunar New Year). The strength in China's stock market is also being overlooked despite the Shanghai Stock Exchange Composite Index (symbol: SHCOMP) closing at another new high. The benchmark is now up for six days in a row for a combined +8.5% performance.

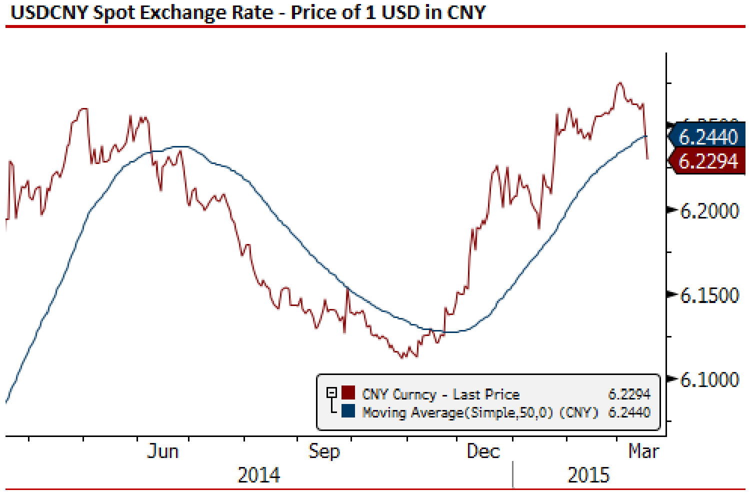
Instead, the focus is on the currency. The Dollar-Yuan (USD/CNY) is showing the largest negative risk-adjusted return across regions and assets.

The People's Bank of China (PBoC) said Chinese banks, including the central bank itself, bought a net CNY42.2 billion in foreign exchange in February, ending two months of net sales. That compares with a net sale of CNY108.3 billion in January and CNY118.4 billion in sales in December. (Source: MNI)

Put another way, China saw its first capital “inflows” in three months. This is very important to recognize because the “outflows” seen in the December-January period were the highest since 2007, and that was the most frequently cited reason for the step-change in sentiment towards a weaker currency profile.

See the below chart. From a technical perspective the currency broke the 50-DMAVG for the first time since last year. While the 50-DMAVG is not really significant in-or-of-itself, it is worth noting that when it crosses either over or under that point, the currency tends to remain over/under for six-month periods.

USDCNY Spot Exchange Rate - Price of 1 USD in CNY




Source: Bloomberg, Rareview Macro

We would advise watching this currency cross more closely going forward. As a reminder, during the February-March 2014 period the PBoC made a calculated attempt to “shake-out” CNY longs and professionals who were attempting to arbitrage the onshore (CNY)/Offshore (CNH) markets suffered severe PnL duress. Wouldn’t it be ironic if this year the PBoC began to really curb the CNY depreciation via its fixing mechanism and stealth currency intervention for no other reason to just remind speculators who are really in charge?

Interestingly, being short of the Yuan is a very consensus and populated trade right now across all investor types, especially owning upside call options on the Dollar-Yuan (USD/CNY) as a tail-risk hedge should China really falter.

While we have no strong view on the immediate direction of the currency, from where we sit, taking the other side of this view and owning a USD/CNY put option or put options spread for a move back down below 6.20 (spot reference) on an implied volatility level of ~3 seems like the cheapest hedge to a US Dollar correction in the market place and no one has that trade on.

**Long Crude Oil – Adding to Watch List**

Over the last six-months, and unlike everyone else, we have spent very little time commenting on Crude Oil and have not added a position in the “barrel” one way or the other in the model portfolio. Like Fixed Income, the opportunity set may be changing. We are currently evaluating an outright long position or spread.

Each Tuesday evening in the US investors receive the American Petroleum Institute (API) inventory data. Yesterday’s looks something like this:

- Crude: +10.5m (largest build in 4 weeks) vs. +4m expected
- Gasoline: -0.58m vs. -1m expected
- Distillate: -0.25m vs. -0.5m expected

For those who are not dedicated to investing/trading in Energy this data set is very similar to the ADP Employment data that comes two days before the monthly non-farm payroll. Therefore, last night’s API data, despite the make-up being different, is treated as a precursor to Wednesday’s U.S. Energy Information Administration (EIA) inventory release.

As a reminder, those transient to the energy space remain fixated on the EIA’s weekly report, especially the data on the inventory builds at Cushing, and the weekly Baker Hughes rig count, especially the metrics associated with horizontal drilling. Inventories are rising at an extraordinary rate at Cushing and the horizontal drilling rig count is falling at the same speed and degree.

We are not going to pretend we have some special insight into either metric. But we would like to briefly comment on the weekly inventory data and the horizontal rig count.

Firstly, due to the longshoremen strikes, West Coast port shutdowns, and the harsh winter in the US in the first two months of this year, refineries have had a much larger than normal number of shutdowns, which allowed them to complete much of their maintenance and the switchovers needed for the next 4-6 months. Refiners should increase production in the next few weeks and slow the growth in inventories – which has been the major headwind for crude oil recently.

Secondly, there is a prevalent concern that the market is running out of storage. Recently, producers were incentivized to utilize offshore storage due to the narrow spread between Brent and WTI prices. Earlier this year the spread reached its widest level in percentage terms ever. Now they have shifted into onshore storage, which has caused the increase in visible inventories at Cushing. As a result, the WTI crude oil futures curve trades in a steep contango in the first few months.

Thirdly, the dramatic decline in horizontal rig counts in the Baker Hughes survey will take oil out of the market at quicker rate. Due to new fracking technology, large amounts of oil production from new rigs can be brought onto the market within the first few months of drilling. Because of the dramatic decline in new rigs, the rate of production growth in the US, which is already at very high levels, will slow at a rate faster than is historically normal.

The final supply arguments center on OPEC, Saudi Arabia and other GCC countries. We will leave out Libya or the prospects of an Iranian nuclear deal. They go something like this – OPEC does not have the capacity to increase production in a meaningful way, Saudi Arabia is producing its maximum amount and the GCC countries have sold all their oil for the next 2-3 months. The key point here is that these three suppliers, the ones who historically control the sparest capacity in times of fundamental market imbalances, can't be a factor right at the point when the global imbalance is the most skewed to high inventories and high production.

The conclusion? As a result of this profile, we are becoming more open to the idea of getting long on crude oil. At what price and where in the curve is yet to be determined but we are looking out far enough in the time horizon so that we can capture a better supply/demand profile than in the next two months, where the inventory build is finally expected to subside. Specifically, we are looking beyond September, where the steep contango largely ends, and towards the December-January time bucket where the roll-costs begin to normalize.

## **Sweden – Negative Deposit Rates & Larger QE**

The views were mixed but there was certainly a risk that the Swedish Riksbank was going to send a dovish message today at their meeting. They did just that. Coincidently, this fits in nicely with March 2015 BIS Quarterly Review released earlier today – A wave of further easing. See Top Observations section below for the full report.

Here is the LINK to their communique but the Riksbank cut their repo rate to −0.25% from -0.10% announced that they will buy SEK 30 billion worth of government bonds out to maturities of 25 years. As a reminder, at their last meeting, the Riksbank surprised by announcing a mini-QE with SEK 10 billion worth of planned purchases of only 1-5 year Gov't bonds. Other highlights include:

- The repo rate is expected to remain at 0.25% at least until the second half of 2016.
- The Riksbank is still ready to make monetary policy even more expansionary, even between the ordinary monetary policy meetings, if this is necessary to ensure that inflation rises towards the target.
- Looking at loan's to companies and FX interventions.
- Buying "other types of assets".

For us, we will pay close attention to the door they opened to launching a scheme to channel monetary support directly to corporations via lending. While no details were provided for the second meeting, we have for some time believed that a funding-for-lending program (FLS), a measure already used by the Bank of England, or a public-private investment program (PPIP), a liquidity tool used by the US Federal Reserve, are transmission mechanisms that have much greater and immediate impacts on the real economy than quantitative easing.

It will be interesting to see if this type of move from the Riksbank and the BIS report help sway the Swiss National Bank (SNB) to loosen policy even further at their "unusual" meeting tomorrow. Now that would be a welcome surprise.

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## Top Observations

**March 2015 BIS Quarterly Review**: A wave of further easing. Full Report

- A growing share of sovereign debt and even some private bonds are now trading at negative yields as a wave of easier monetary policy feeds through into unprecedented bond market conditions.
- Oil producers' rising debts add downward price pressure
- "High debt burdens may force these firms to maintain production despite the fall in prices in order to generate the cash flow necessary to service the debt, thereby putting additional downward pressure on the price of oil"
- Foreign lending to Chinese borrowers is showing signs of peaking, suggesting policymakers' efforts to tighten credit conditions have started to take hold
- In keeping with past warnings that the easy money now being targeted at sluggish prices risks generating financial market bubbles, the BIS found a stronger link between output growth and sliding asset prices; in the wake of equity and property price peaks, economic expansion is about 10 pps lower over five years
- Credit trading failing to keep up with bond sale surge; Liquidity falling as dealers cut inventories, risking gridlock in a selloff.

**Iron Ore & Australia Dollar**: Iron Ore to avg $60/mt 2015 vs. $63 forecast in December and $88 in 2014 (per Department of Industry and Science).

- Macquarie Bank lowered its 2015 iron ore price forecast by 20% to $54 average and its Australian dollar year end forecast to $67 from $77:
    - Lowered 2016 iron ore forecast by 12% to $58 average
    - Q3 2015 iron ore forecast lowered to $48/t
    - "With major projects still coming online this year in an environment where Chinese demand is relatively stagnant, existing supply will have to make way yet again," it said. "This will require an even lower iron ore spot price"
    - Cut 2015 hard coking coal forecast by 4% to $114/ton

- Fortescue, the world's fourth-largest iron ore exporter, pulled its USD2.5bn secured high yield bond issue due to unfavorable and volatile credit markets. Fortescue shares down 8% at one point (closed -5.3%. Their April 2017 bonds – that were scheduled to be refinanced with the new issue - traded down to 99.71 from 102.75 (-3%) at one point as well. The company needs an iron ore price in the mid-$70s to repay all its debt per Morgan Stanley.

**European Central Bank (ECB) Protests:** ECB opened its new headquarters in Frankfurt today. A group called "Blockupy" gathered 10,000 protestors to demonstrate outside of the building, which resulted in several police cars being set on fire and multiple building's windows smashed. About 350 people were detained at the protests. The demonstrations targeted the ECB because of its symbol of capitalism and the restrictive austerity measures it has enforced countries like Greece. Frankfurt 18 March 2015 below.

**US Leading Indicators:** US AIA Feb Architecture Billings Index m/m: 50.4 vs. 49.9 prior; Inquiry Index: 56.6 vs. 58.7 prior; Index serves as a leading economic indicator that leads nonresidential construction activity; reading above 50% indicates an increase in billings.

**German Bunds**: New record low yield at today's 10-year auction of 0.25%. Bid-to-cover was 2.4x vs. 1.4x at last month's auction. Only sold EU3.298bn versus the EU4bn target.

**US Equity Sentiment**: Newsletter writers classified as bulls by Investors Intelligence slip for 3rd week, fall to 52.0% from 53.6%; was at 59.5% at end of Feb. (Source: Investors Intelligence)

- Bears at 14.3% after holding at 14.1% for the last 4 weeks
- Correction rises to 6-week high at 33.7% vs. 32.3%
- Bull-bear spread 37.7 vs. 39.5

**Israel Election**: Prime Minister Netanyahu Likud party won a surprise victory after a sharp shift to the right, which helped shore up his base.

- Final tally puts Likud on 29-30 seats in 120-member Knesset.
- Opposition Zionist Union won 24 seats, concedes defeat.
- Coalition building to form a government will take three weeks.

**Global Growth:** OECD updates growth forecasts. Full Report

- Outlook in top economies slightly better vs. November
- Raises 2015 euro zone growth forecast from 1.1% to 1.4%, raises 2016 from 1.7% to 2.0%
- Japan's growth forecast rose to 1.0% this year and 1.4% next year

- Lowered Canada 2015 growth forecast to 2.2%, down 0.4% from its forecast in November last year. 2016 forecast lowered to 2.1%, a cut of 0.3%, widening the gap to the United States.
- Governments cannot rely solely on low inflation and easy monetary policy to consolidate recovery and boost employment
- Growth remained too low to "repair and activate labor markets"

**China Internet – Tencent Holdings Ltd (Symbol: 700.HK):** Largest name in KraneShares CSI China Internet Fund (symbol: KWEB) at 10.38%.

Also, take a look at Naspers Limited (symbol: NPN SJ). It is key shareholder of Tencent. Naspers is one of the largest companies in South Africa and viewed as top way to play India e-commerce. Some also view this as a Yahoo/Alibaba type setup in the future.

- Reports Q4 Net CNY6.72B (adj) v CNY6.55Be, Op profit CNY7.39B v CNY4.75B y/y, Rev CNY21B v CNY17.0B y/y - MAU of QQ: 815M, +0.9% y/y (smart device MAU of QQ 576.1M, +32.5% y/y)
- Combined MAU of Weixin and WeChat: 500M, +6.8% q/q, +40.8% y/y
- MAU of Qzone: 654.1M, +4.6% y/y
- Sales of online advertising: CNY2.63B, +8% y/y
- VAS Rev CNY17.1B, +7% y/y (online games CNY12.0B, +6% y/y, Social networks CNY5.17B, +10% y/y)
- Mobile games Rev (mobile QQ and Weixin, WeChat): CNY3.8B v CNY2.6B q/q
- Adj EBITDA margin 40% v 44% y/y- Op margin 35% v 38% y/y
- Fair value of stakes in listed investee companies: CNY60B v CNY61B q/q
- Outlook: During 2015, in addition to developing our ongoing businesses, we intend to cultivate an increasingly vibrant mobile ecosystem, bringing our own and our partners products and services to China consumers (Tencent Earnings Source: TradeTheNews.com)

**HSBC (Largest weight 6.26% in FTSE 100 Index):** Cut to equal weight vs overweight by Barclays analyst Sharnie Wong, citing combination of higher capital requirements, macro headwinds and need for further significant restructuring.

- Cuts earnings expectations by 12%-16%
- PT lowered to HK$69 vs HK$81
- Sees limited growth in earnings, divs in near- to medium-term amid increased structural challenges and as co. seeks to build capital

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## Model Portfolio

**UPDATES**

| Asset Class | Date | Strategy | T/S | | Start/Close PX | | Capital at Risk (USD) |
|---|---|---|---|---|---|---|---|
| Interest Rates | 09-Mar-15 | Short German Bund (RXM5) - new | S | $ | 157.30 | $ | 150,000 per 1 bps |
| Interest Rates | 09-Mar-15 | Long US 10-YR Treasuries (TYM5) - new | S | $ | 126-09+ | $ | 150,000 per 1 bps |
| Interest Rates | 09-Mar-15 | Long German Bund (RXM5) 05/22/15 P154.5 - open | T | $ | 0.39 | $ | 423,150 |
| Commodities | 09-Mar-15 | Long Silver - roll 1 | S | $ | (0.021) | $ | (52,080) |
| Equities | 10-Mar-15 | Short German DAX (GXH5) - new | T | $ | 11,485.000 | $ | (61,697,420) |
| Interest Rates | 12-Mar-15 | Short Sep15 Eurodollar (EDU5) - new | T | $ | 99.425 | $ | 112,500 per 1 bps |

*Source: Bloomberg, Rareview Macro. Capital at Risk (USD) Start Price.

## CURRENT POSITIONS

| Asset Class | Entry Date | Strategy | T/S | Start/Avg PX | Capital at Risk (USD) |
|---|---|---|---|---|---|
| Foreign Exchange | 05-Dec-14 | Long USD/CHF | S | $ 0.9785 | $ 25,734,943 |
| Foreign Exchange | 05-Dec-14 | Long USD/CHF 9/7/15 C1.05 | S | $ 110.314 | $ 911,931 |
| Foreign Exchange | 05-Dec-14 | Long USD/SGD | S | $ 1.3317 | $ 35,103,078 |
| Foreign Exchange | 05-Dec-14 | Long USD/SGD 9/7/15 C1.40 | S | $ 57.2 | $ 1,608,903 |
| Equities | 05-Dec-14 | Long WisdomTree Europe Hedged Equity Fund (HEDJ) | S | $ 60.13 | $ 28,873,400 |
| Equities | 05-Dec-14 | Short SPDR S&P 500 ETF Trust (SPY) | S | $ 207.79 | $ (24,909,538) |
| Equities | 06-Mar-15 | Long SPY 6/19/15 PS 205-180 | T | $ 3.97 | $ 2,704,472 |
| Equities | 13-Feb-15 | Conversion: Long AAPL vs. 1/20/17 C140-P140 Synthetic Short | S | $ 0.50 DVD Forecast | $ 17.79mm Funding |
| Equities | 13-Feb-15 | Conversion: Long GOOG vs. 1/20/17 C600-P600 Synthetic Short | S | $ 0.00 DVD Forecast | $ 11.07mm Funding |
| Equities | 10-Mar-15 | Short German DAX (GXH5) | T | $ 11,485.000 | $ (63,921,778) |
| Interest Rates | 26-Jan-15 | Short Eurodollar Dec15 (EDZ5) | T | $ 99.269 | $ 187,500 per 1 bps |
| Interest Rates | 09-Mar-15 | Short German Bund (RXM5) | S | $ 157.30 | $ 150,000 per 1 bps |
| Interest Rates | 09-Mar-15 | Long US 10-YR Treasuries (TYM5) | S | $ 126-09+ | $ 150,000 per 1 bps |
| Interest Rates | 09-Mar-15 | Long German Bund (RXM5) 05/22/15 P154.5 | T | $ 0.390 | $ 341,275 |
| Interest Rates | 12-Mar-15 | Short Sep15 Eurodollar (EDU5) | T | $ 99.425 | $ 112,500 per 1bps |
| Commodities | 31-Dec-14 | Long GLD 6/30/15 C150 | S | $ 0.30 | $ 41,236 |
| Commodities | 31-Dec-14 | Long Silver (SIK5) - roll 1 | S | $ 15.796 | $ 38,372,172 |
| Commodities | 31-Dec-14 | Short Gold (GCJ5) - roll 1 | S | $ 1,273.60 | $ (38,259,830) |

*Source: Bloomberg, Rareview Macro. Capital at Risk (USD) COB March 13, 2015.

## CURRENT THEMES

| Asset Class | Strategy | Strategic (S) | Tactical (T) |
|---|---|---|---|
| Foreign Exchange | Long US Dollar vs. Short Swiss Franc & Singapore Dollar | X | |
| Equities | Long European vs. Short US Equities Currency Hedged | X | |
| Fixed Income | Short US Fixed Income | | X |
| Fixed Income | Short European vs. Long US Fixed Income | X | |
| Commodities | Long Silver vs. Short Gold | X | |
| Idiosyncratic | US Equity - AAPL & GOOG - Dividend Conversion Arbitrage | X | |
| Portfolio Overlay | Short US Equities or Long Equity Volatility | | X |

*Source: Rareview Macro.

## WATCH LIST

| Asset Class | Entry Date | Strategy | Wake Up Price |
|---|---|---|---|
| Commodities | 05-Jan-15 | Base Metals - Long Nickel (LMNIDS03) | $ 13,800 |
| Commodities | 05-Jan-15 | Long Uranium - Japan Nuclear/Elections (CCJ CN, DML CN, PDN AU) | TDB |
| Equities | 05-Jan-15 | Extraction of Risk Premia - Long Euro Stoxx 50 Index Dividend Futures (2017, DEDZ7) | € 102.00 |
| Equities | 05-Jan-15 | China: Long SOE & Telecom; H-Share Catch Up (1398 HK, 1288 HK, 3988 HK, 941 HK) | TBD |
| Equities | 05-Jan-15 | Long US Security Theme (PANW US, PFPT US, IMPV US, FEYE US) | TBD |
| Foreign Exchange | 05-Jan-15 | Carry Trade: Short EUR & SGD vs. Long INR and TRY | TBD |
| Fixed Income | 05-Jan-15 | Short US Treasury 2-5-10 Butterfly (BF020510) | 55 bps |
| Tail Risk | 05-Jan-15 | Long 5-Yr Credit Default Swap (CDS) on Brazil | 175 bps |

*Source: Rareview Macro.

## RISK EXPOSURE

| Risk Level | % of Portfolio | Asset Class | Gross Exposure | Net Exposure |
|---|---|---|---|---|
| Medium | 60.33% | Equities | $ 181,679,717 | $ (100,532,916) |
| Low | 44.93% | Foreign Exchange (USD) | $ 135,287,872 | $ 135,287,872 |
| High | 0.20% | Fixed Income (DV01) | $ 600,000 | $ 300,000 |
| High | 25.75% | Commodities | $ 77,532,002 | $ 1,012,342 |
| Low | 0.00% | Credit (DV01) | $ - | $ - |
| Low | 0.00% | Option Premium (<3-mo.) | $ - | |
| Low | 1.86% | Option Premium (>3-mo.) | $ 5,607,817 | |

*Source: Bloomberg, Rareview Macro. Options Delta Adjusted. Risk Exposure (USD) COB March 13, 2015.

PERFORMANCE UPDATE

| Portfolio | Macro Strategy | | Start NAV | | End NAV |
|---|---|---|---|---|---|
| 2015 Year to Date Return | 0.38% | $ | 300,000,000 | $ | 301,138,808 |
| 2015 Month to Date Return | 1.27% | | Net | $ | 1,138,808 |
| 2015 Week to Date Return | 0.38% | | | | |
| | | | | | |
| 2014 Year to Date Return | 17.81% | $ | 113,160,023 | $ | 133,310,565 |
| 2014 Sharpe Ratio | 1.92 | | Net | $ | 20,150,542 |
| | | | | | |
| 2013 Year to Date Return | 13.16% | $ | 100,000,000 | $ | 113,160,023 |
| 2013 Sharpe Ratio | 2.73 | | Net | $ | 13,160,023 |

*Source: Bloomberg, Rareview Macro. Performance COB March 13, 2015.

## Model Portfolio

For important information, including past performance, our process, FAQs regarding how the model portfolio is administered, and disclaimers please click HERE. The portfolio illustrations referenced within this material are hypothetical. No actual investments have been implemented and any references to transactions, positions, gains, or loses with respect to the portfolio are hypothetical.

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# Data & News

## UNITED KINGDOM

Minutes of the Monetary Policy Committee Meeting 4-5 March 2015

- MPC Voted 9-0 for unchanged Bank Rate, QE at Mar meeting
- Ian McCafferty and Martin Weale: decision over a hike was finely balanced.
- Reiterates all members agreed Bank Rate more likely heading up next 3 years.
- Inflation: Stronger pound may prolong inflation weakness, entrench low inflation expectations
- Relatively little news on inflation outlook in month, as the month's most significant news was financial market moves
- Minutes warned that divergent monetary policy, with BOE policy likely on an upward path, could put further upward pressure on sterling and "prolong the period for which CPI inflation would remain below the target". Sterling is being cited as a potential factor weighing on future tightening.
- Faster wage growth needed to meet 2% inflation target; amount of slack in labor market 'matter of some debate' on MPC
- Reiterates more likely than not that CPI dips below zero in coming months
- Growth: Reasons to be confident BoE growth forecast is on track.
- Sees decline in investment from North Sea and pension contributions.
- Little evidence national elections, possible EU referendum, impacting business capital spending

## SOUTH KOREA

- Unemployment Rate Feb:  3.9% vs. 3.4% exp vs. 3.4% prior

## SINGAPORE

- Economists cut Singapore 2015 growth, inflation forecasts – MAS survey
- 2015 growth forecast down to 2.8% from 3.1%
- All-items inflation forecast cut to 0.1% from 1.1%
- Core inflation forecast trimmed to 1.0% from 1.9%
- Dollar-Singapore (USD/SGD) seen at 1.40 end-2015 vs 1.33

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