BOND MARKET REVIEW

March 23, 2016

The Comeback

In the NCAA Basketball tournament last week, Texas A&M made up a 12–point deficit with less than 35 seconds to go in regulation, and then won over Northern Iowa in overtime. While NIU did nearly everything wrong in that time, the Aggies got most every break. The stock market pulled off its own comeback, by completing a 5–week winning streak that put the Dow and S&P back in the plus column for 2016. The 5–week gain isn't real news, but stocks had begun the year with their worst–ever start. With a pullback into today, for at least the Dow and S&P, the 'game' is close to being tied – as those indexes closed with the Dow up .45% for the year, while the S&P was off by .35%. It should be a very long time before we see a repeat of the end of such a game, or the beginning of such a market. While global equities lost almost $9 trillion to start the year, over $3.5 trillion has been added back this month. U.S. stocks have rebound by around $2 trillion. However, not only do stocks have some negative cycles to overcome, but also a troubling resurgence in terror attacks – designed to inflict massive injuries and disrupt services.

While not projecting the timing for a U.S. recession just yet, we would note they do tend to accompany the type of economic troughs that the **B**ond **M**arket **R**eview cycle work has been projecting for 2016. Last week, the Fed held rates steady – even though the initial plan in December was, commencing in March, to hike at every other meeting in 2016. Though somewhat optimistic about the U.S. recovery, the Fed cited global growth concerns, and their updated forecasts reflected a less–aggressive hiking campaign. We usually gain insight from members of the committee in the weeks following each statement, and this one was no different. While a Few FOMC members spoke to an April hike as still a possibility, others confirmed what the markets took away from the Fed's March statement, the 'Dot Plot' chart, and post–meeting comments. While the aforementioned U.S. markets have erased their 2016 losses, most global markets are still in the red – some very much so! The Japanese Nikkei is still 10.68% lower for 2016. Germany's DAX is off 6.70%, and China's Shanghai Composite is still a sharp 14.95% lower.

FRB Chicago President Charles Evans explained: *"The rationale for no rate change in March is that economic and financial risks seem somewhat higher for 2016 than we had hoped back last December when we first began raising rates."* He said: *"Most of the Federal Open Market Committee's cautionary pause in the rate normalization path is about assessing risks and just being careful."* Last week, we said the collective member forecast, or the 'Dot Plot' chart, was still projecting 2 more hikes in 2016. At this point, traders place an April hike at only a 6% probability. The first meeting greater than 50% is now September, though July stands at 47.9%. Evans said the projections (the 'Dot Plot' of only 2 more 2016 hikes) are *"really a pretty good setting."* While Kansas City's Esther L. George voted against the stay, preferring a hike in March, there are also a few more in favor of a quicker path to normalization. If you've been in this business for years, you tend to think of a 'normal' 10–year yield being 6 to 8%. We are most likely years from that occurrence – which is probably why someone's always trying to define the 'new normal'.

Many view a non–data dependent Fed as confusing! FRB St. Louis President James Bullard said: *"Prudent policy suggests edging the policy rate and the balance sheet toward more normal levels."* Bullard said *"the FOMC's goals have been met"*, explaining: *"Labor markets are close to normal and inflation net of the oil price shock is reasonably close to target."* The **BMR** continues to take issue with overweighting the low U.S. Unemployment Rate versus the quality of jobs, the lofty number of Americans out of the workforce, and high numbers of those on government assistance. San Francisco's John Williams said *"in isolation, the U.S. economy is looking great"*, and said if not for global factors, the Fed would be raising rates sooner and more quickly – viewing April and June as still in play.

Looking Ahead

- Our bond cycles have yields dropping into April 1st.
- Our equity cycles are calling for a drop into an April 4th–to–7th window.

Treasuries, Agencies, and MBS

We expected yields to begin to fall from March 21st, and the past 2 days have kicked off that type of move. Yields fell by 12, 16, 11, and 8 bps for the 2, 5, 10, and 30–year sectors last week. Longer yields then rose into the 21st, and have since fallen again. Though 2 and 5–year yields were 2 bps higher into today, the 10–year was only .5 bps higher, and 30–year yields fell by 1.5 bps. MBS spreads (for FNMA 30–year 3.0%) widened 4 bps last week. Next week, the Treasury will auction 2–year notes on Monday (03/28), 5–year notes on Tuesday, and 7–year notes on Wednesday.

03/18/16 Treasury Yield Curve	2-Year: 0.837%	5-Year: 1.334%	10-Year: 1.874%	30-Year: 2.676%
Weekly Yield Change:	–.120	–.159	–.111	–.078%
Support:	0.90/ 0.94/ 0.97/ 1.00%	1.41/ 1.47/ 1.53/ 1.59%	1.93/ 1.97/ 2.00/ 2.07%	2.65/ 2.69/ 2.73/ 2.77%
Targets:	0.84/ 0.80/ 0.76/ 0.72%	1.32/ 1.29/ 1.23/ 1.17%	1.84/ 1.80/ 1.73/ 1.66%	2.61/ 2.57/ 2.53/ 2.49%

Economics

It's a little hard to get a good read on consumer confidence. University of Michigan's survey on Sentiment fell from 91.7 to a 5–month low of 90. Their measure of Current Conditions also fell from 106.8 to 105.6, though Expectations rose from 80.0 to 81.9. Those surveyed also expected inflation to pick up. Bloomberg Consumer Comfort, on the other hand, rose from 43.8 to a 1–month high of 44.3 – though their Economic Expectations result dropped .5 to 42. The Richmond Fed Manufacturing Index rose from –4 to +22, while the Chicago Fed National Activity Index fell from .41 to –.29. The Philadelphia Fed Business Outlook rose from –2.8 to 12.4. After declines of .2% and .3%, the Leading Index rose in February, but only by .10% – pointing to more of that 'modest to moderate' growth. Initial Jobless Claims rose from 258K to 265K, and Continuing Claims were 8K higher to 2,235K. There was a surge in JOLTS Job Openings in January to 5.541M, but that jump was due to a downward revision for December from 5.607M to only 5.281M. Blamed on limited supply and higher prices, February sales of Existing Homes dropped 7.13% to 5.08M units, though 3.89% higher versus last year. The January pace of 5.47M had been the second–highest reading since 2007. New Home Sales rose 1.99% to 512K units. Though sales were off 5.71% to last year, the pickup reflected strength in the western U.S. (as there were actually declines in the other 3 regions). January's FHFA House Price Index had risen .50%. The Current Account deficit narrowed from 3Q $129.9 billion to a 4Q of $125.3 billion.

Thursday is set for jobless claims data, Durable Goods Orders for February, Bloomberg Consumer Comfort, and Kansas City Fed Manufacturing Activity. Though the bond and stock markets will be closed for Good Friday (March 25th), most banks will be open and there is a scheduled data release for updates to 4Q 2015 U.S. GDP, Personal Consumption, and the GDP Price Index. Next Monday (03/28) brings Personal Income & Personal Spending for February, the PCE Deflator (Personal Consumption Expenditures), Pending Home Sales, and Dallas Fed Manufacturing Activity. Tuesday is set for S&P/Case–Shiller home price data, and the Consumer Confidence Index. Wednesday follows with MBA Mortgage Applications (which dropped by 3.30% last week), and a first look into March jobs (due next Friday) from the ADP Employment Change (private payrolls) report.

Equities

We use the Dow for a lot of our cycle work, as it's often a great bellwether for U.S. equities. However, there are only 30 stocks in the Dow, and last week we noted the broader market was extending to a high nearer March 22nd. Stocks reversed on the 22nd, and should trade off for a week. There are cycles projecting another high near April 14th, which could line up with another surge by Crude Oil (into April 12th). Whenever that expected rally concludes, the **BMR** cycles get very negative into June – so selling or hedging may be in order! Hopefully, we can fine–tune that April cycle over the next 2 weeks. Last week, the Dow rallied 388.99 points or 2.26% to 17,602.30. After 5 weeks of gains that sent the Dow back positive for 2016, it's .57% lower this week – with only one trading day left, and ahead for 2016 now by only .45%. The S&P gained 27.39 points or 1.35% to 2,049.58. That put it also ahead for 2016, but by only .28%. The S&P is off by .63% this week – and it's back down for 2016 by .35%. The Nasdaq gained 47.18 points or .99% to 4,795.65, but it's .56% lower this week. The Dow Transports gained 4.97% to mark a 9th week of gains. They're 1.47% lower this week. Bank stocks rose .72%, but are .94% lower so far this week.

Resistance:	Dow:	17,652/ 17,919/ 18,186/ 18,457	Nasdaq:	4,767/ 4,831/ 4,901/ 4,972	S&P:	2,033/ 2,056/ 2,079/ 2,102
Support:		17,386/ 17,134/ 16,867/ 16,604		4,693/ 4,625/ 4,558/ 4,491		2,011/ 1,991/ 1,970/ 1,946

Other Markets

After the FOMC left rates unchanged last Wednesday, and it appeared that the market is now expecting 2 more hikes in 2016 at the most, the U.S. Dollar plunged over 2% to an 8–month low. The day after the FOMC meeting, Crude Oil traded above $40/barrel for the first time since early December. However, the Dollar has rallied 1.68% since Friday's low, and today Crude Oil once again sank below that $40 support–resistance level established back in August. Last week, Commodities gained 1.63%, but improving on their streak of 4 weekly gains is in danger with CRB prices off 1.76% so far this week. Crude Oil added 2.44% to rise for a 5th week, and is holding on to a 6th with prices still .89% higher since Friday. Gold lost .40%, and is 2.42% lower this week. The U.S. Dollar lost 1.09%, falling for a 3rd week, but is .99% higher so far this week. The Japanese Yen surged 2.03%, but is .74% lower this week. The Euro rose 1.02% last week, but is .79% lower this week. Corn rose .27%, and is .41% higher this week. Cotton gained .02%, and has added 2.15% since Friday.

"Make the most of yourself, for that is all there is of you." Ralph Waldo Emerson

Additional Information is Available on Request

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