Creative Global Investments

Market commentary & charts

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Objectivity

Integrity

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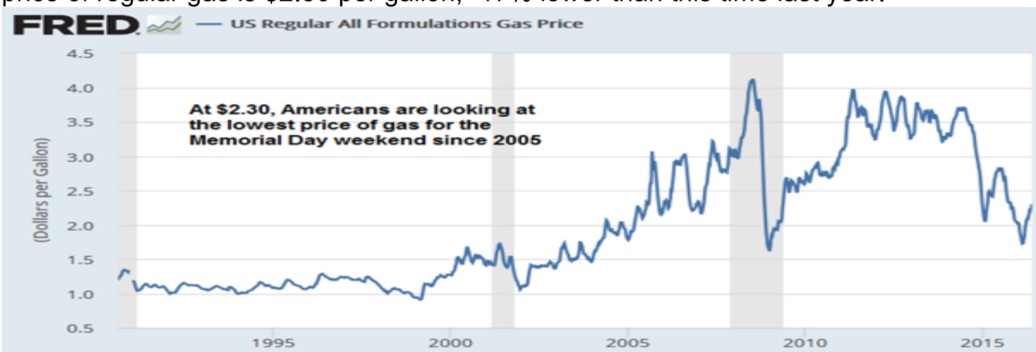
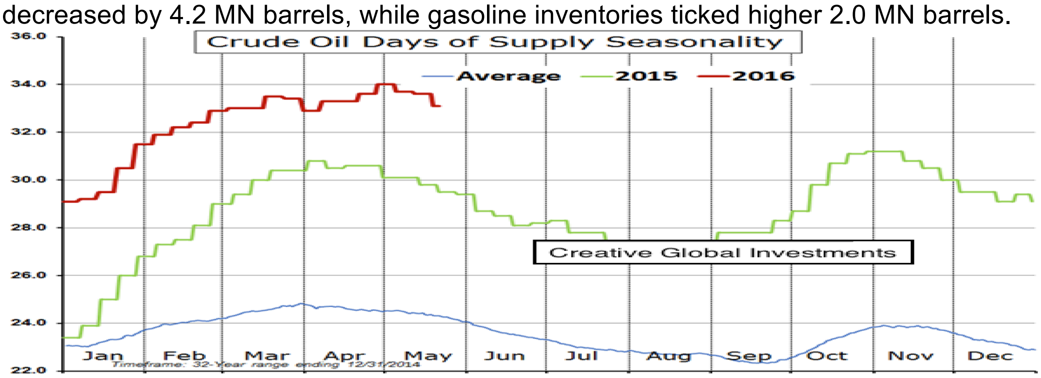
Macro Commentary

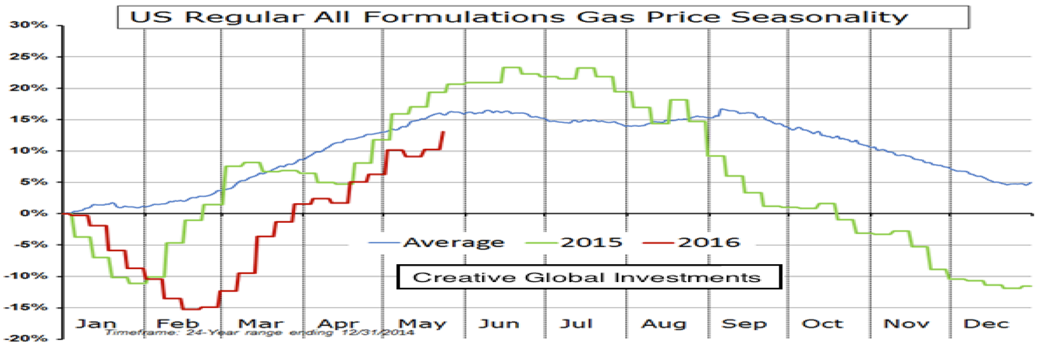
This year's Memorial Day, Americans are enjoying "most memorable low gas prices" for the start of the summer driving season in over a decade, with the weighted average price of regular gas is $2.30 per gallon, -17% lower than this time last year.

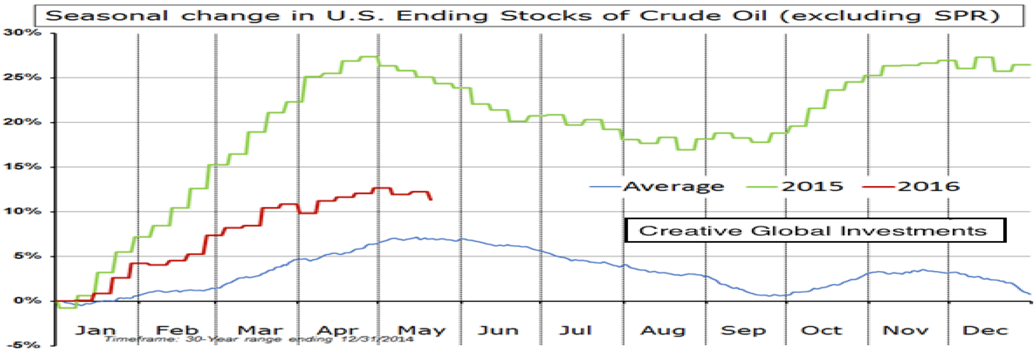


The EIA's latest inventory report for the week until May 20th showed oil inventories decreased by 4.2 MN barrels, while gasoline inventories ticked higher 2.0 MN barrels.

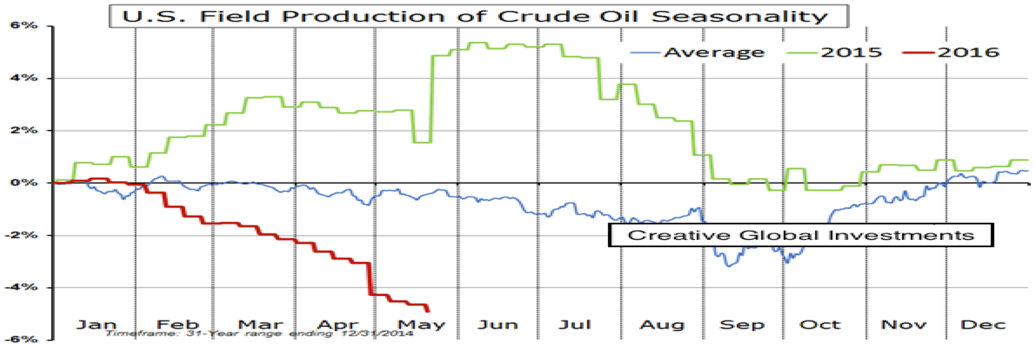


Seasonally, Memorial Day weekend marks the peak for gas prices following the strong spring run-up; prices peak through the summer and eventually turn lower following the Labor Day long weekend. From a seasonal perspective, even though the rebound from the February lows has been robust, the y-t-d change continues to lag the average; the 13.1% gain since the start of the year is below the 15.8% 25-year average increase.

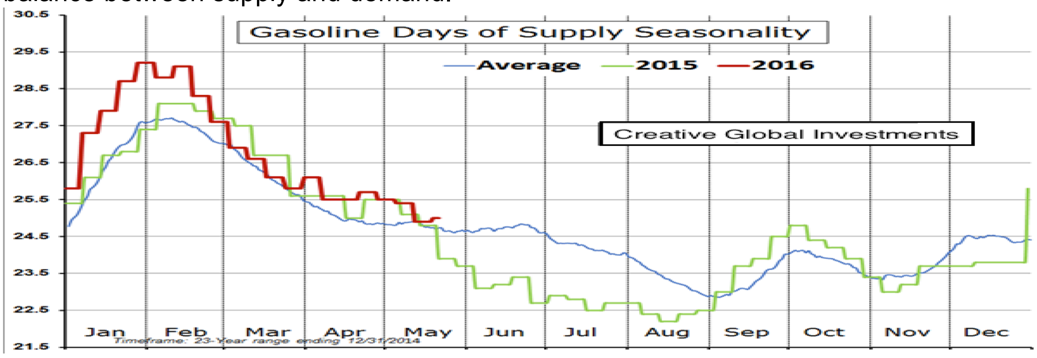


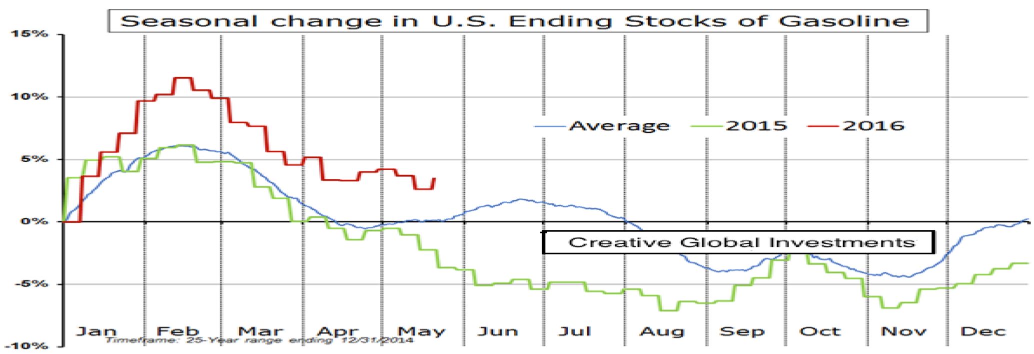


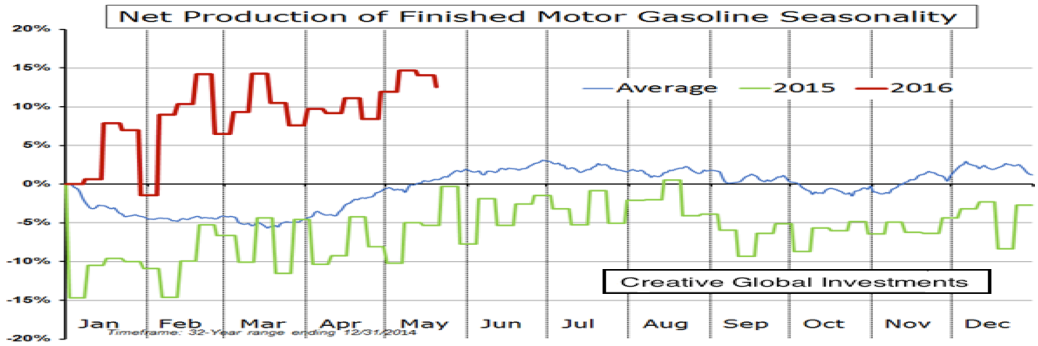
Days of supply of oil is now lower by half of a day to 33.1, while gasoline saw a minor uptick by a tenth of a day to 25. As we've been documenting for weeks now, it is becoming increasingly apparent that the seasonal peak in oil inventories is becoming confirmed as an ongoing decline in production and increased demand of refined product draws on the raw input. The rate of increase in oil inventories remains above average y-t-d, however, it is nowhere near the pace set in 2015 when the commodity saw a 25% increase in supply through the middle of May. Ending stocks of crude oil seasonally decline between now and mid-September.



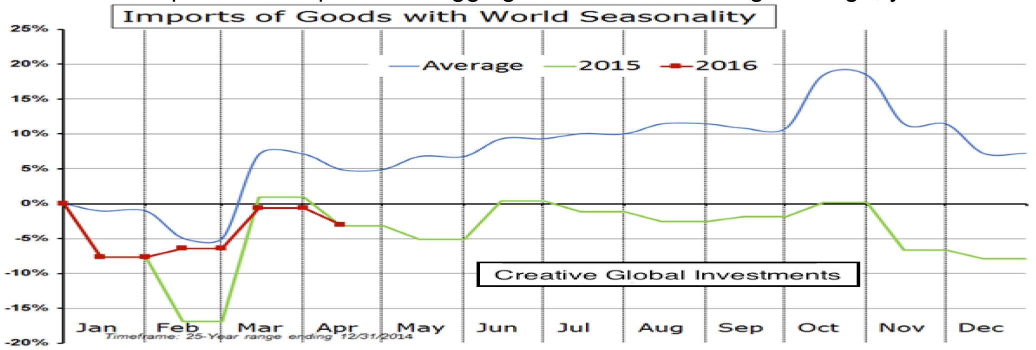
Meanwhile, even though the seasonal change in US Gasoline stocks continues to run above average, the days of supply is inline with the average, suggesting a healthy balance between supply and demand.

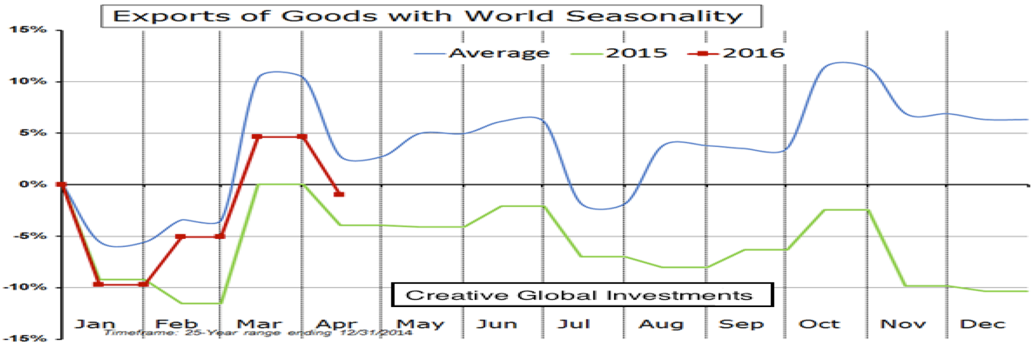




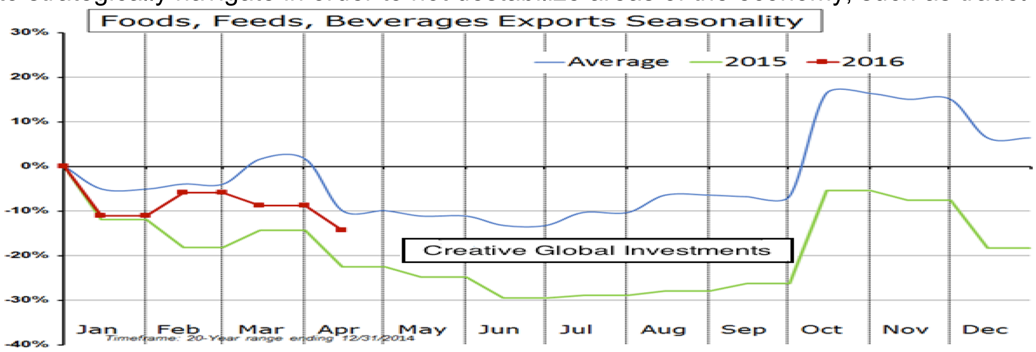


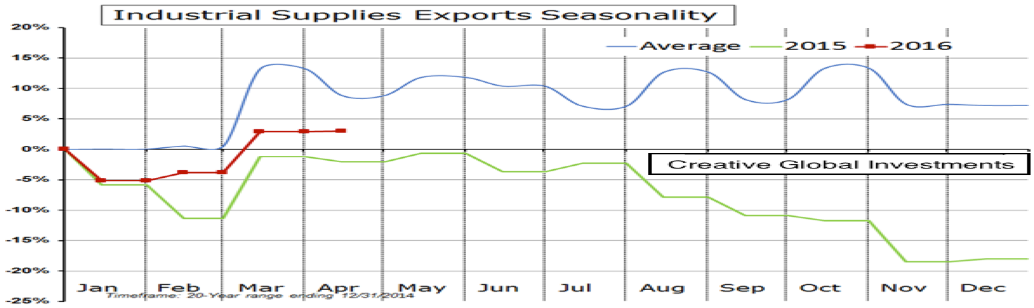
Other US macro data yesterday showed more deterioration of the US April International Trade. Although Exports increased by 1.8%, but imports advanced by 2.3%, resulting in a wider trade deficit than the month prior. Stripping out seasonal adjustments, exports declined by -5.4%, better than the –6.9% average for the month of April, and imports were lower by -2.4%, below the average change for the fourth month of the year of –2.0%. Both exports and imports are lagging the seasonal average change, y-t-d.

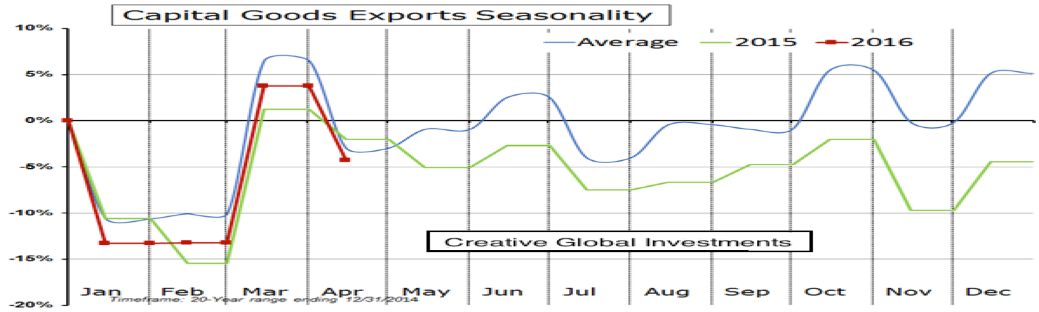


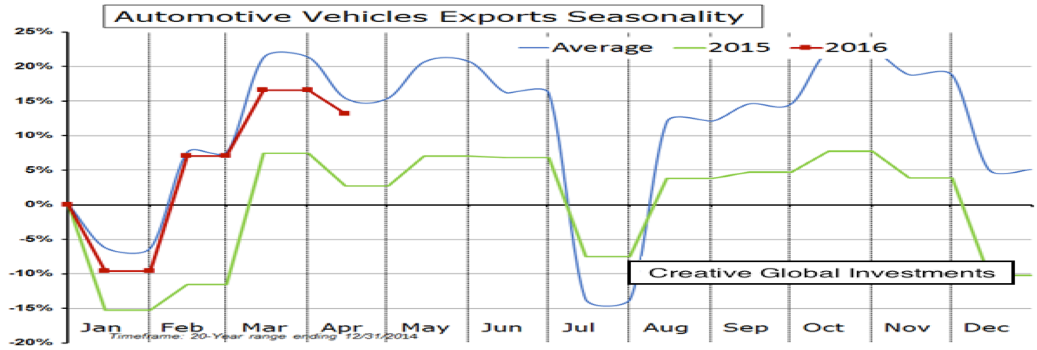


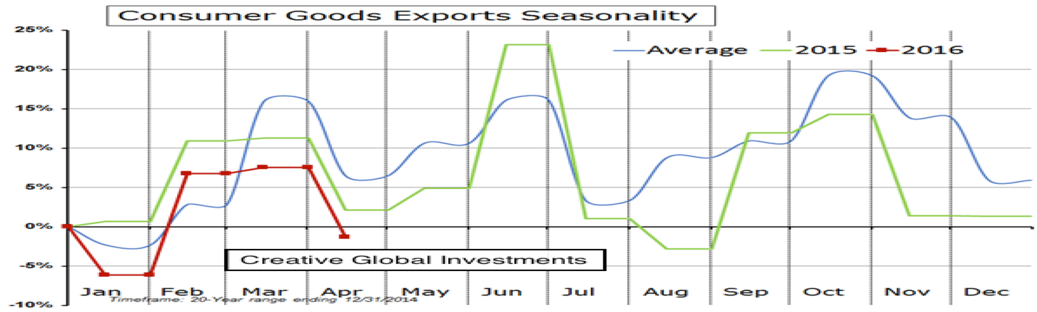
The lag in exports is being picked up across each of the sub-components as the impact of a stronger US$ remains apparent in the results; the last time exports showed an above average seasonal pace was in 2011 when the US$, as gauged by the USD, was hovering around multi-decade lows, around 20% lower than what it is today. The influence of potential rate hikes on the US currency is something that the Fed will have to strategically navigate in order to not destabilize areas of the economy, such as trade.





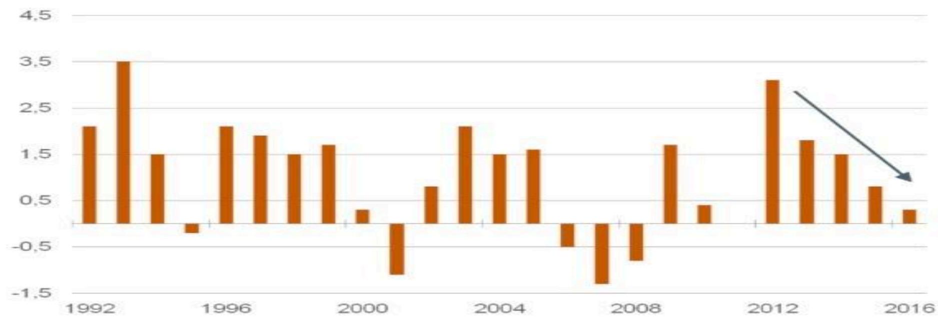






With deteriorating trade data, not solely due to the strength of the US$, the spread of real US GDP versus Europe has shrunk in 2 years to just about nothing, just as we were predicting since September of 2015. Now, investors have to seriously question the "embedded strength of the US$" or the "weakness of the Euro", and should reassess the valuation multiple premia of US asset prices and equities over Europeans.

US GDP spread over Europe has vanished



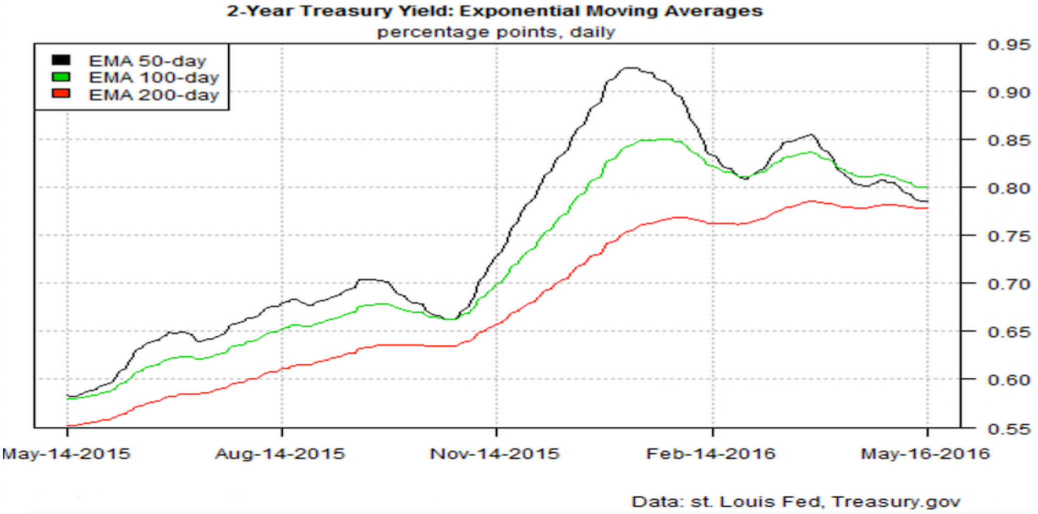
source: IMF

Fixed Income Commentary

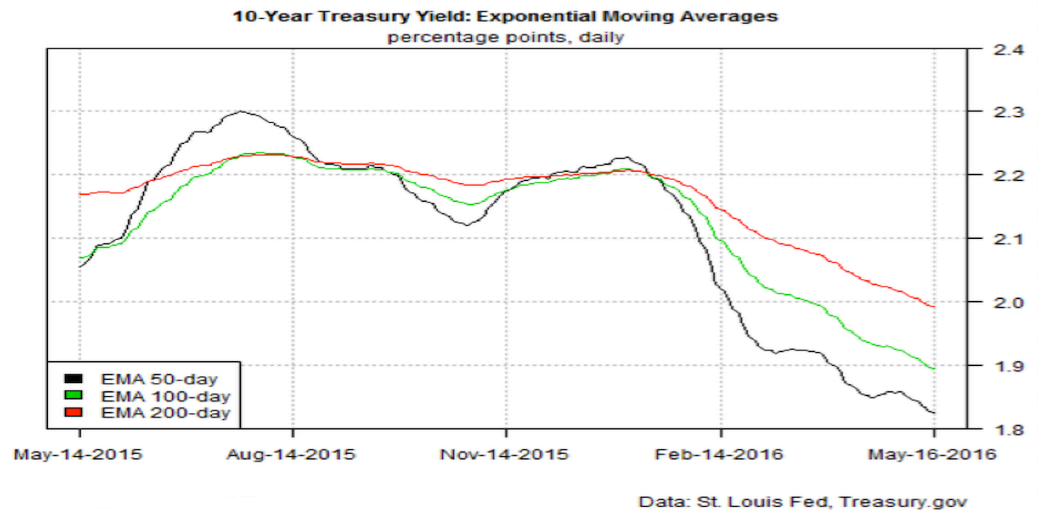
Most recent Fed minutes and data showed the overall PCE inflation was 1%; the core rate was approaching their 2% target.

We think that too many investors still feel that if incoming data were consistent with economic growth picking up in Q2, labor market conditions continuing to strengthen, and inflation making progress toward the committee's 2% objective, then it likely would be appropriate for the committee to increase the federal funds rate in June. However, as we have highlighted for 14 months now, there are slowing macro elements, which the Fed are also taking into account. The strong US$ continuing to cause weak Oil prices and soft international environment led to a 2nd consecutive quarter of contracting business investment.

Moreover, some participants viewed risks to growth and inflation as tilted toward the downside. Others expressed concern about potential international fallout associated with the UK's upcoming "Brexit" vote or China's handling of monetary policy. Still, the narrow parameters of the Fed's dual mandate (maximum employment and price stability) granted the Fed sufficient latitude to argue for a June rate hike.



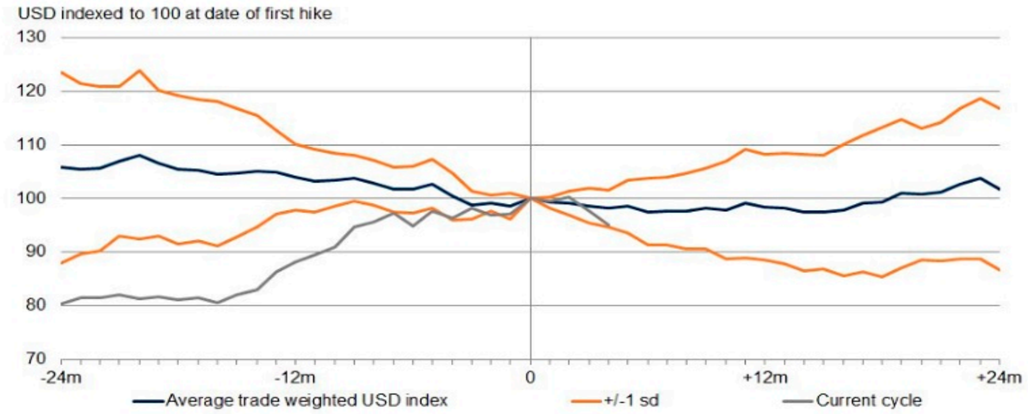
Both show various longer EMAs; the top chart is for the 2-year treasury while the bottom chart is for the 30. The 30-year chart shows a clear long-term downward trend that, should it continue, will eventually move below the 2-year's EMAs. (Longer EMAs are less susceptible to short-term market dynamics and volatility, giving them slightly more predictive power. While the trend is certainly not set in stone, it bears watching).



Currencies Commentary

When looking at the trade-weighted US$ back to 1975, before and after the Fed starts the process of raising rates, one can see the performance of the US$ in the current interest rate cycle has been very different to past cycles. This time, the US$ rose close to 20% in the 24 months leading up to the first rate hike. Historically, however, the US$ has depreciated steadily in the run up. **We believe the embedded US$ strength is way overdone, and that the US$ index ($USD) peaked in March 2015 at 100.71.**

The trade weighted US$ has historically underperformed following Fed rate hikes

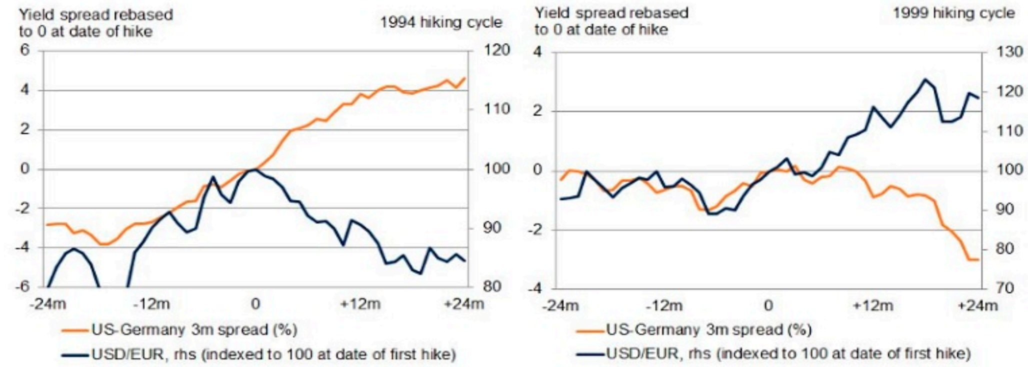


source: Thomson Reuters

The trade-weighted US$, post rate hikes, tends to weaken by around -1.6% within 12 months. Given the parabolic 1-year exaggerated rise of the US$, we are of the opinion that the tremendous damage that this US$ rise has caused globally, the reaction by currency investors with regards to the direction of the US$ (we still are not expecting, contrary to consensus, for rates in the US to rise versus other major central banks) in the unlikely event of a rate rise by the Fed in June will be opposite to historic incidents. **Hence why the US$ carry trade should diminish and inherently weaken the US$. We therefore continue to see fundamental and technical evidence that the US$ will likely weaken all through the summer, even if interest rates between the US and Japan and Europe were to diverge further.**

Unlike in past cycles, when looking at the relationship between the US/Germany interest rate differential and the performance of the US$/EUR exchange rate, we believe that the US$'s recent 2-year parabolic strength has been totally overdone, and will not continue, even in the case where our "no rate hike in 2016" scenario were not to pan out. The impact of interest rate differentials on US$ movements in past cycles looks to be stronger before the first rate hike than after it. This in 2016, as in the 1994 and 1999 hiking cycles, where initially rates and currencies moved together before a pronounced divergence occurred when the Fed finally hiked.

Interest rates and US$/EUR divergence post Fed rate hikes



source: Thomson Reuters

Commodities Commentary

As stated above, with our views remaining negative on the US$, which inversely impacts the price of commodities and particularly the price of WTI Crude, which closed yesterday at a new 10-month high very close to US$ 50/brl. **We have stated since our 2016 CGI Global Investment Strategy & Outlook since mid December 2015 that prices of Oil and other commodities had totally overshot to the downside, and were below extractable global balanced prices. This scenario could not last for very long, and hence we had (and still do) high conviction of our seemingly very high WTI price targets for end of Q2 of $52/brl, and $68 for year-end 2016.**

The S&P 500 Energy Sector index jumped over 1.5%, moving above its 20-day moving average that had been curling lower and acted as resistance over the past couple of weeks. The $SPEN recently found support around its 50-day moving average as investors continue to bet on a rebound in oil prices.

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