

**Thesis: US Treasuries will rise ↑**

Last Update: December 18, 2018

<b>Short term: ↑</b>	<b>Rising US Fed Funds Rates, coincident with weakening global economies and lower confidence in the US Economy, causes short term rates to rise faster than longer-term rates.</b>
<b>Long term ↓</b>	<b>Twin US deficits, and the end of global quantitative easing, may boost interest rates. This may not occur until 2020 given weakening global economies in 2018-19.</b>

**May'18:** US 10YR Treasuries (and longer terms) will likely fall as the Federal Reserve's constantly increasing Fed Funds Rates weaken global economies (due to the stronger dollar) and shift investment flows out of global equities and into US.

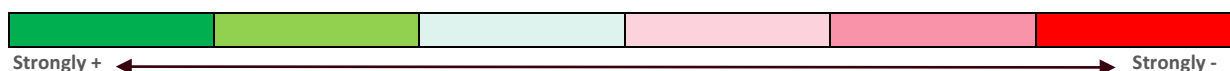
**Sept'18:** Spreading EMK crises (from Turkey to Argentina, then to Brazil and Indonesia and South Africa) increases our conviction of a strong USD, and confirms the negative effects on EMK from higher FFR.

**Nov'18:** Weakening of the Eurozone and Chinese economies (due to trade war). Germany heavily exports to China.

**Dec'18:** Continuing weakness in global equities and oil prices shift investor opinion that global GDP is expected to slow. Portfolio managers are moving from FANGs into safe-haven assets (Consumer staples, Utilities, US Treasuries).

US Treasuries Rise (rates fall):	US Treasuries Fall (rates rise)
<ul style="list-style-type: none"> <li>Rapid FFR rise increases recession risk (Fed stated there will be 3 rate hikes in 2018.)</li> </ul>	<ul style="list-style-type: none"> <li>Large <u>Budget Deficit</u> can cause a Crowding Out effect on treasuries</li> </ul>
<ul style="list-style-type: none"> <li>ECB wants to tighten but is "trapped" by Italian budget (and political movement) and a weakening Eurozone.</li> </ul>	<ul style="list-style-type: none"> <li>Large <u>Current Account</u> (i.e, Trade) Deficit could reduce attractiveness of US dollar denominated assets.</li> </ul>
<ul style="list-style-type: none"> <li>Economists expect U.S. GDP growth to slow in 2019.</li> </ul>	<ul style="list-style-type: none"> <li>Fed's balance sheet is shrinking (not purchasing bonds)</li> </ul>
<ul style="list-style-type: none"> <li>Bearish Futures bets are extremely crowded (though less so as of 12/18).</li> </ul>	<ul style="list-style-type: none"> <li>European Central Bank expected to repurchase fewer bonds (as per 12/18 comments).</li> </ul>
<ul style="list-style-type: none"> <li>If US Dollar rises in a reflexive feedback loop (See USD framework file) foreign investors will likely buy treasuries</li> </ul>	<ul style="list-style-type: none"> <li>Rising inflation in 2018 and 2019. FOMC Minutes say looking for a "symmetric 2% inflation", meaning it could be &gt;2% for a time (5/23/18).</li> </ul>
<ul style="list-style-type: none"> <li>Positive Interest-rate differential b/w U.S. and Eurozone/Japan.</li> </ul>	<ul style="list-style-type: none"> <li>Downgrade of U.S. sovereign rating by the credit agencies.</li> </ul>
<ul style="list-style-type: none"> <li>Global equity market volatility favors safe-haven assets (e.g., US Treasuries)</li> </ul>	<ul style="list-style-type: none"> <li>Trade War? China has been reducing US Treasury investments.</li> </ul>
<ul style="list-style-type: none"> <li>Copper/Gold ratio is indicative of lower rates.</li> </ul>	

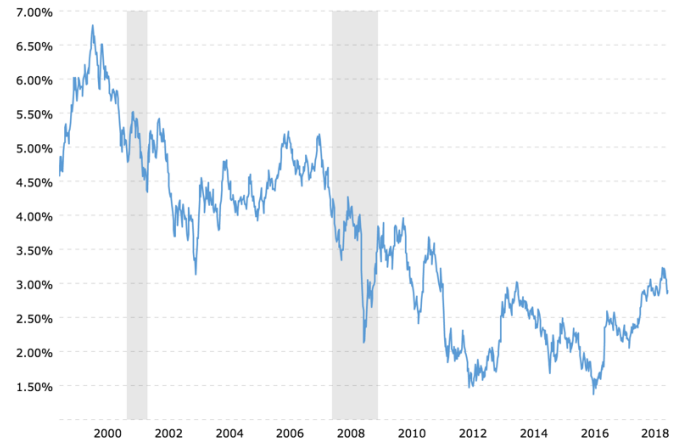
Heat Map legend



US 10Y Treasury Rate



US 10Y Treasury Rate- Twenty Year Evolution



### Notes:

- Thesis considers all viewpoints including Classical and Monetary Theories.
- Portfolio Managers can consider direct investments or derivatives or Utilities equities and ETFs.

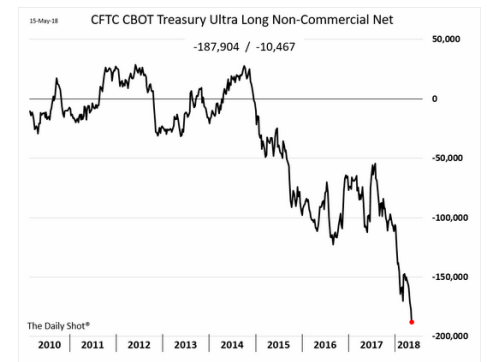
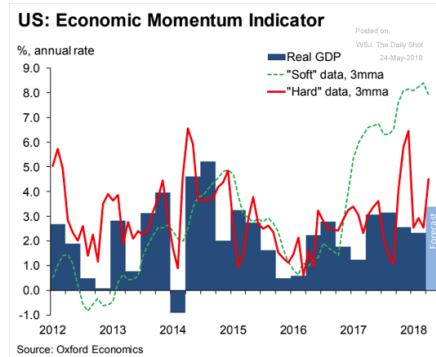
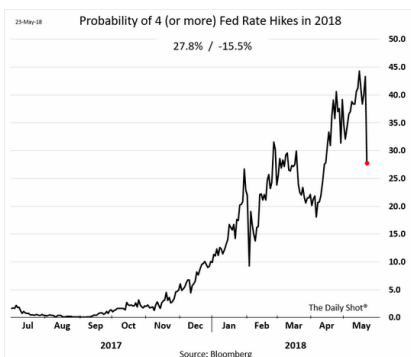
### ETFs:

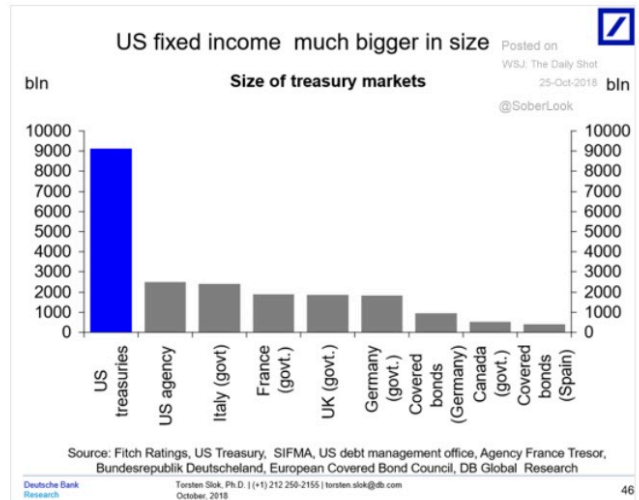
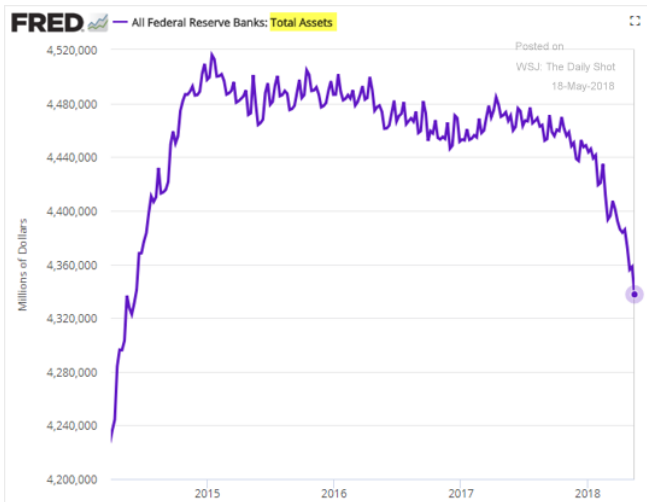
Ticker	Name	Comments
TLT	Ishares 15YR Treasury	Longest term ETF, 0.15% expense ratio
SPTL	SPDR LT Treasury	State Street, 0.06% expense ratio
VGLT	Vanguard LT Treasury	Expense ratio of 0.07%
TMF	Direxion 20+ Daily	Leveraged ETF, high expense ratio of 1.1%

### Futures:

CME Ticker	Name	Comments
TN	Ultra 10YR Notes	Maturity < 10YR
ZB	Classic T-Bond	Maturity < 25YR
UB	Ultra T-Bond	Maturity >= 25YR

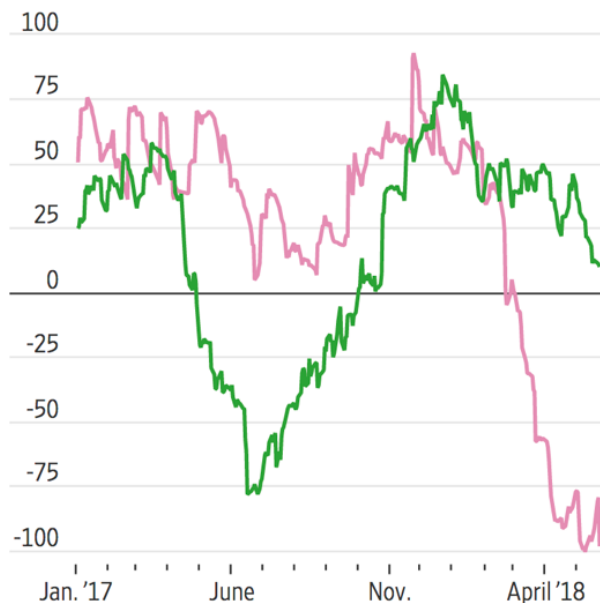
## Charts supporting or contradicting the above thesis (charts are retained given the evolution of the data over time):





## Citigroup Economic Surprise Index

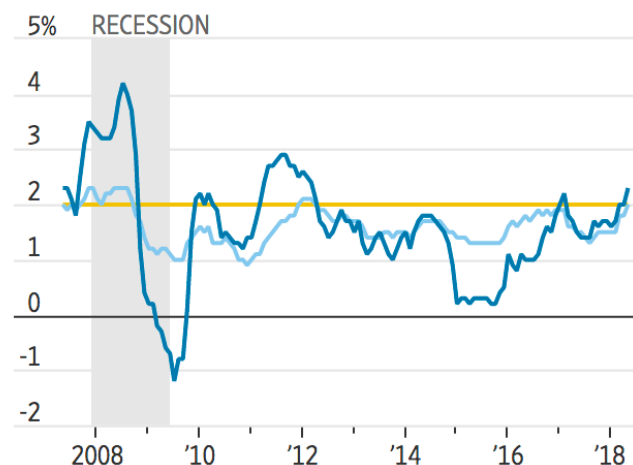
■ U.S. ■ Eurozone

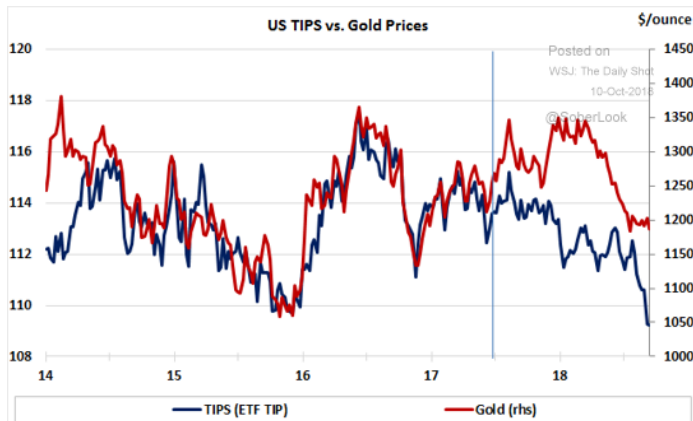


## Inflation Pressures

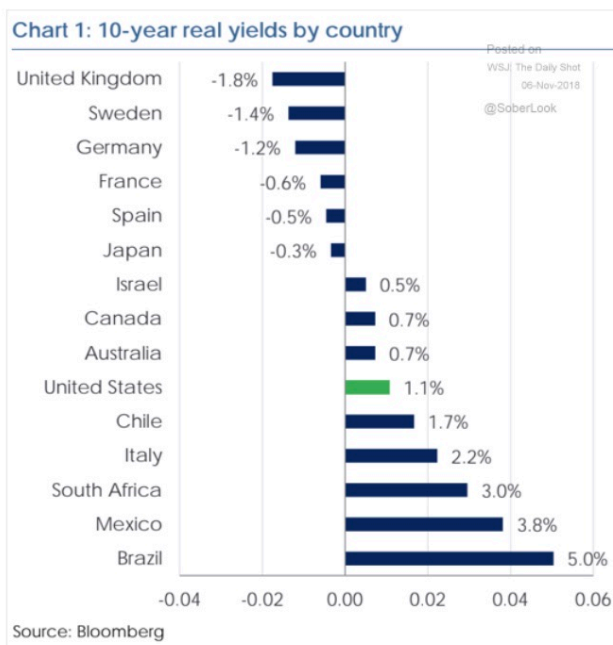
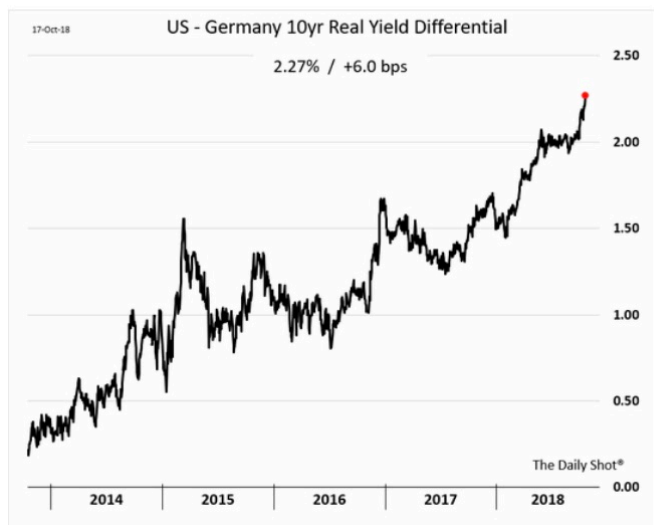
Personal-consumption expenditures price index, change from a year earlier

■ All items ■ Excluding food and energy  
 ■ Federal Reserve inflation target

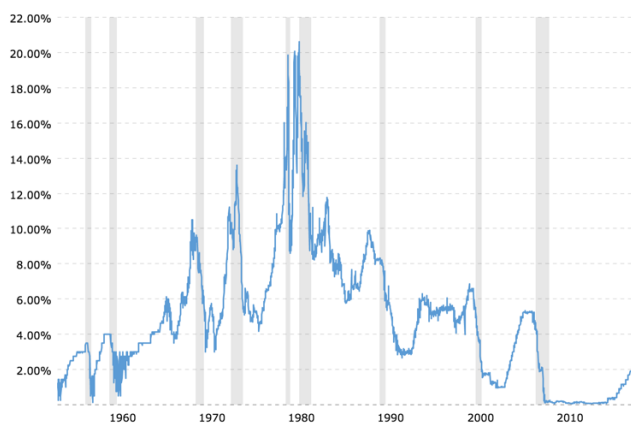


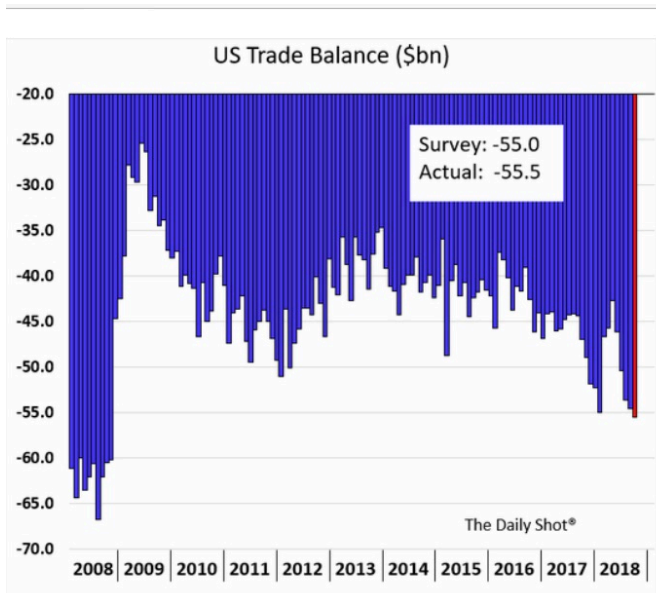


- The 10yr US-Germany **real** rate differential:

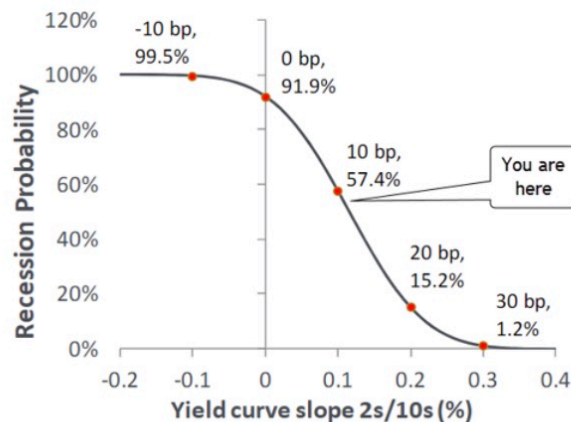


Federal Funds Rate





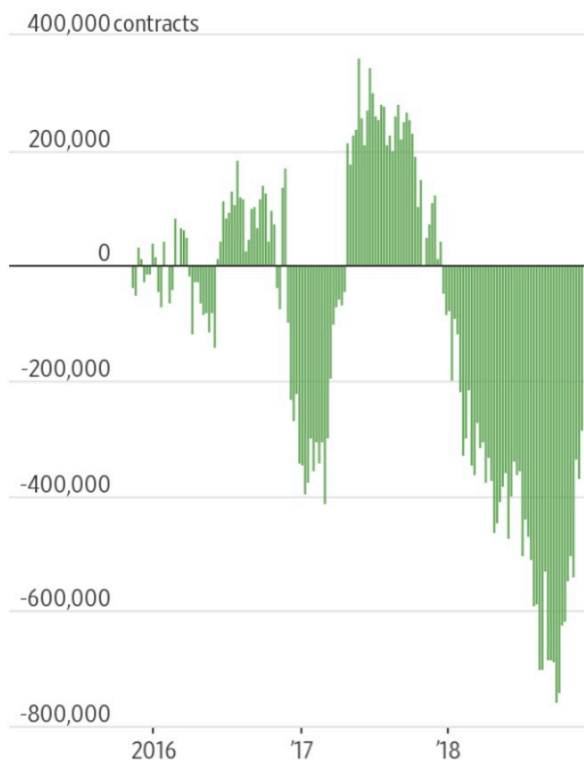
**Figure 41: The odds of a recession increase substantially as the spread drops below 10 bp**



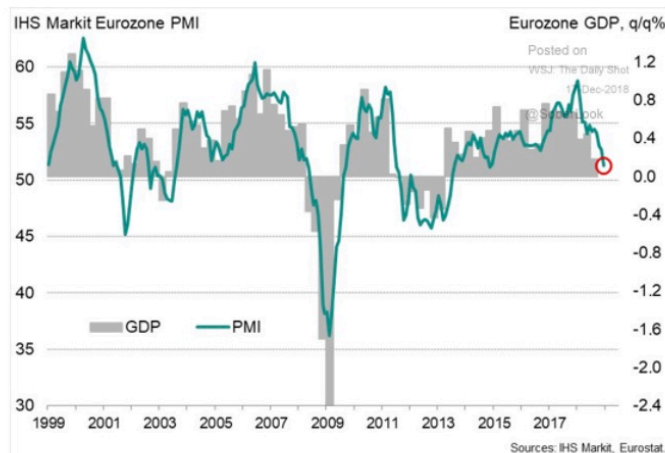
Source: PiperJaffray

## Cutting Back

Speculators have reduced futures bets against 10-year Treasuries.



Source: Refinitiv



### Key findings:

- Flash Eurozone PMI Composite Output Index<sup>(1)</sup> at 51.3 (52.7 in November). 49-month low.
- Flash Eurozone Services PMI Activity Index<sup>(2)</sup> at 51.4 (53.4 in November). 49-month low.
- Flash Eurozone Manufacturing PMI Output Index<sup>(4)</sup> at 51.0 (50.7 in November). 2-month high.
- Flash Eurozone Manufacturing PMI<sup>(3)</sup> at 51.4 (51.8 in November). 34-month low.

Source: @WilliamsonChris; [Read full article](#)