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am FX

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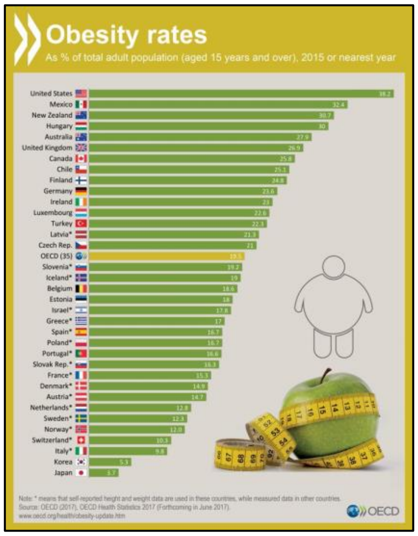


Click on the image to see a bigger version.

NZ is surprising.

Current Views

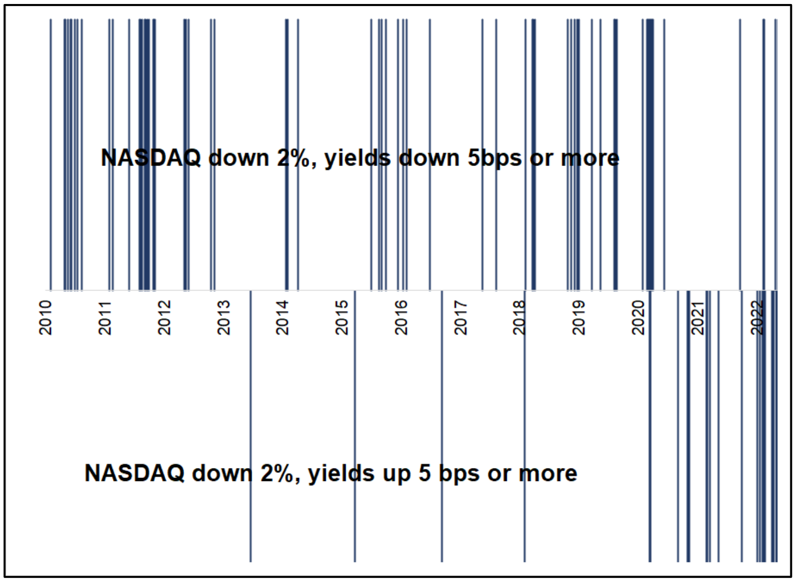
Short CADJPY 101.21
Stop 102.61
Take profit 97.11

Sniffing out a corr flip

One of the biggest issues for investors in this bear market has been the shortage of places to hide. Normally, since 2010, large drops in stocks are accompanied by rallies in bonds. That has not been the case in this cycle because inflation is the fear driving both stocks and bonds lower.

Here is a scan of the market showing all NASDAQ down 2% days since 2010. The up bars show NASDAQ down 2% days when yields fell 5bps or more (that is, bonds were somewhat of a hedge), and the down bars show NASDAQ down 2% days when yields rose more than 5bps (you lost on both sides).

Up bars = bonds worked as a hedge, down bars = bonds didn't work as a hedge



You can see that since September 2020, bonds have not been a good hedge as all those down 2% NASDAQ / higher yield days in the bottom right corner indicate. This came to mind because yesterday bonds <u>were</u> a good hedge. That might be important. It certainly does not indicate a trend yet, but it might be the start of one.

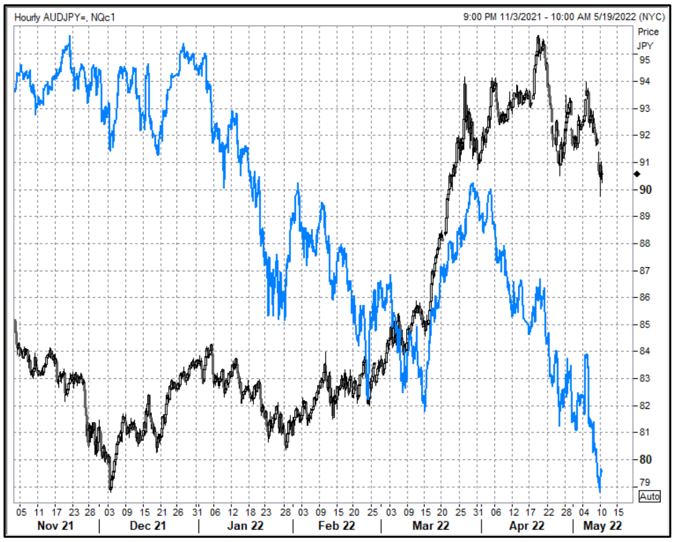
The relationship between yields and stocks should change as the Fed put gets closer. My view has been that the Fed put is much farther than it used to be because the Fed needs to remain on autopilot to get to neutral, no matter what stocks are doing. The Fed speeches I quoted yesterday support this autopilot idea as the Fed claims that 2-year yields show the Fed is not behind the curve. This is nonsense if they have the option of slowing down or stopping hikes (which clearly they do!)

While we are nowhere near the Fed put now, in my opinion, there is enough economic doom and gloom out there to justify a flip in the correlation. My bet is that the stocks vs. bonds correlation is going to revert to the old school way and drops of 2% or more in the NASDAQ will now mean US 10-year yields go **down** at least 5bps, most days. In other words, the period of blue bars on the bottom of the chart is almost over and we will go back to blue bars on the top.

The implication in FX is that cross/JPY correlation to equities should rise significantly now and cross/JPY should start to work as an equity hedge.

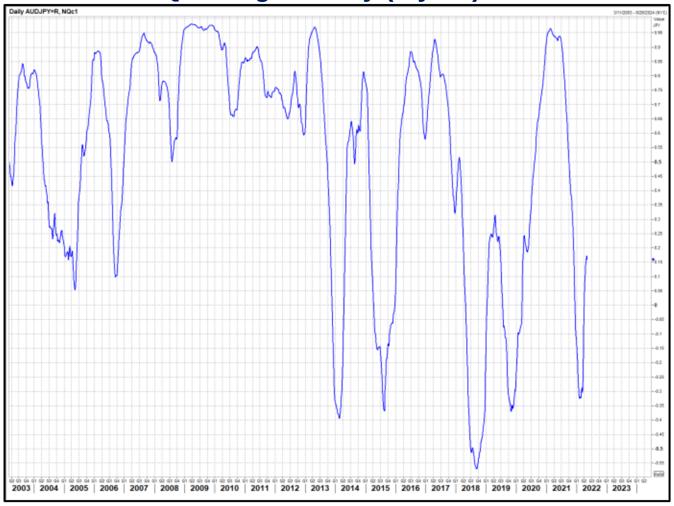
This chart shows you what a bad equity hedge AUDJPY has been.

AUDJPY up vs. NASDAQ down



My view is that we will now return to higher AUDJPY vs. NASDAQ corr. The next chart shows 1-year rolling AUDJPY vs. NASDAQ correlation. You can see it was pinned high and above zero from 2003 to 2012 before it flipped as the taper tantrum and Abenomics created some spicy weirdness in the JPY market. The correlation has mostly still been positive, though much less reliable since then. It flipped negative (stocks down, AUDJPY up) over the past year as rates have been the dominant driver of all markets, not stocks. 2022 has been characterized by: rates up, weak JPY, stocks down. I think that regime is nearing an end. This will make JPY feel like a safe haven again, even though it never really was one as I explain in this piece from March 2022.

AUDJPY vs. NASDAQ rolling 252-day (1-year) correlation since 2003



I will monitor the bond/equity and AUDJPY/equity correlations and keep you up to date!

Closing thoughts

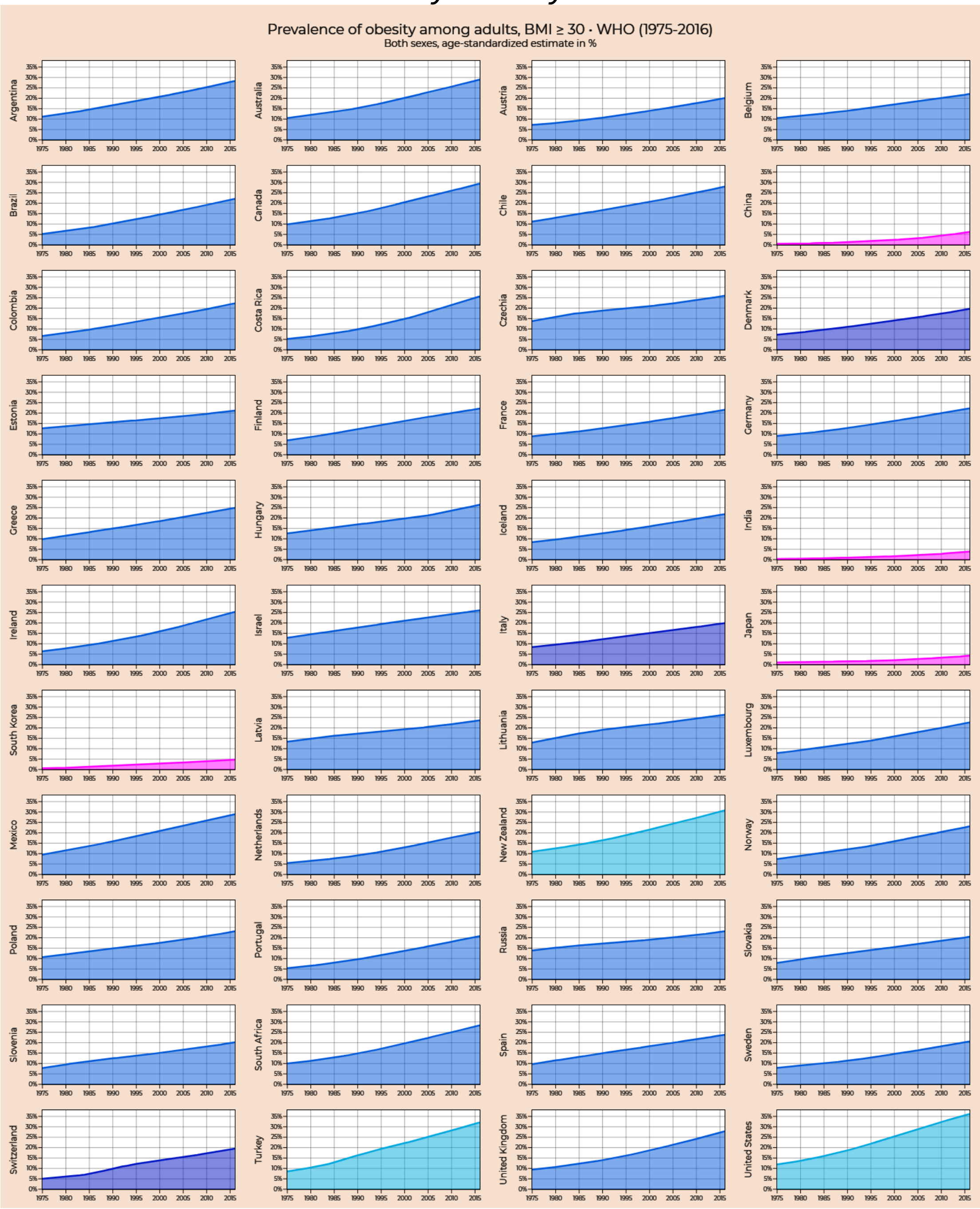
This Washington Post article does a good job explaining how extreme financialization creates a procyclical economy.

Have a filling today.

good luck ⇅ be nimble

Very few surprises, other than New Zealand

Prevalence of obesity among adults, 1975 to 2016
by country



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