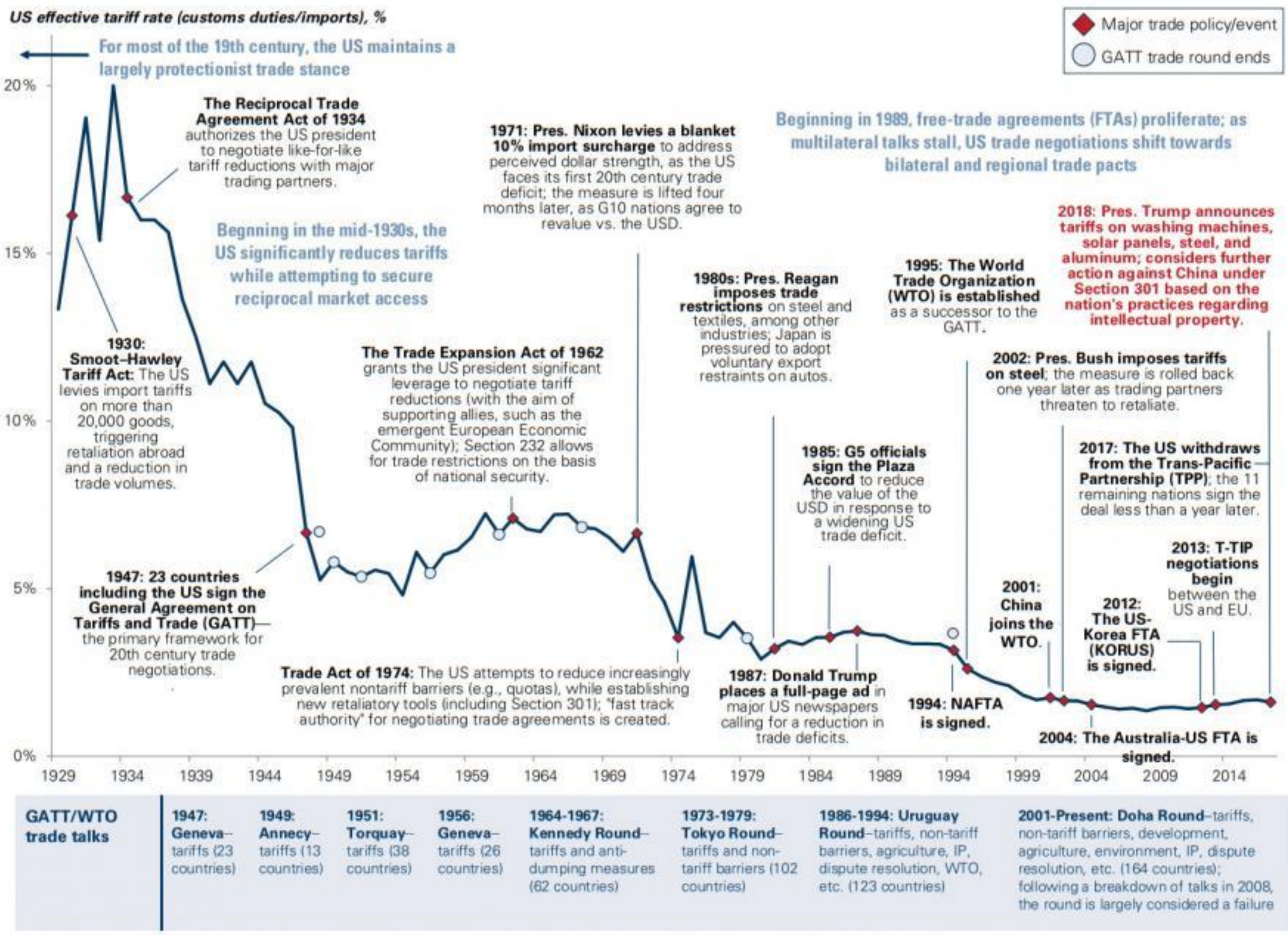
China Answers
Don's Blog 2018.04.02

This morning (04/02/2018), China answer President Trump's tariff policy by placing import taxes on some 128 U.S. export items to their country. And so, it begins. This is serious business and I only hope this is for public consumption. Surely there must be some behind-the-scenes talks going on which will call the dogs off.

History has not been kind to economies that engage in trade wars. Even worse, sometimes trade wars turn into shooting wars. Did you happen to see where Trump's approval ratings have advanced to 50%, a new high? Even this is worrisome if in fact all of this bluster is pleasing to the average guy on the street. The following chart (chart #1) enumerates that story of U.S. trade policy since 1929. Tariffs seem rather common. I guess it all depends on size and severity as well as time as to the consequences.

As you know, I have made what little mark I've accomplished by using the business cycle to trade the U.S. long-term government bond. This market since 1974 has been very good to me. With that in mind, please note the following article that comes from Citibank discussing my favorite asset, which also happens to be the most hated asset. And what's that make it? The cheapest asset class on the planet a la Citi. I like the company, but don't want many to believe and act upon it. Being a contrarian is like having an ace in the hole. Remember, 3% today is like 6% yesterday.

Chart 1



Source: US International Trade Commission, US Department of Commerce, WTO, "Irwin Douglas A., Clashing Over Commerce," Goldman Sachs Global Investment Research.

Citi: "The 30Y Treasury Is The Cheapest Asset Class On The Planet"

by Tyler Durden

Sun, 04/01/2018 - 15:24

Ahead of the Easter Weekend, in lieu of its traditional rates weekly report, Citi's European Rates team headed by Harvinder Sian released a list of 15 non-consensus thoughts among which such ideas as: the 10yr BTP/Bund spread drops sub-100bp, Bunds may ***rally*** on ECB tightening, and that Neutral rates really are that low (*"Why are such low rates restrictive? Because we have borrowed demand from the future and to prevent a reckoning when tomorrow arrives requires ever lower real rates"*).

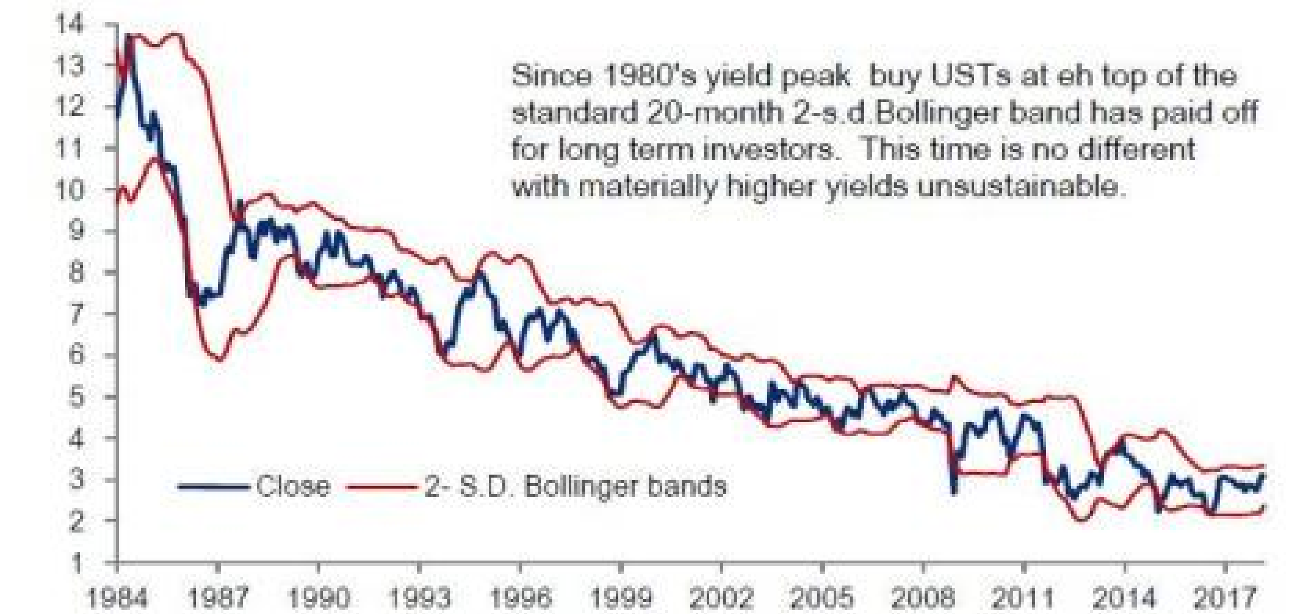
But the one that caught our attention the most was Sian's take on the long-end of the curve, ***the 30Y Treasury***, which in stark contrast to the vast majority of the street, he sees as not only outperforming, but is now the "**cheapest asset class on the plant**" for one simple reason, in fact the same reason why have said for years is why the Fed simply can not normalize: "The consensus that we are set to break multi-decade bull channels does not work **because higher rates crash risk assets and then the economy.**"

That's really all there is to it.

The extremely controversial, if brief and to the point, take from Citi:

> *We took down our 30yr Treasury yield forecast for end-2018 to 2.85% because the Fed is into restrictive territory. Long end yields typically peak before the Fed.* ***The consensus that we are set to break multi-decade bull channels does not work because higher rates crash risk assets and then the economy.*** *With $ slope pointing to recession risks* ***we like getting paid a coupon for an asset that should return 30%+, when the Fed initiates yield curve control on 10yr at say 1.25%.***

Figure 3. If higher rates are unsustainable then 30yr Tsys offer good risk-reward and benefit hugely from future Fed yield curve control.

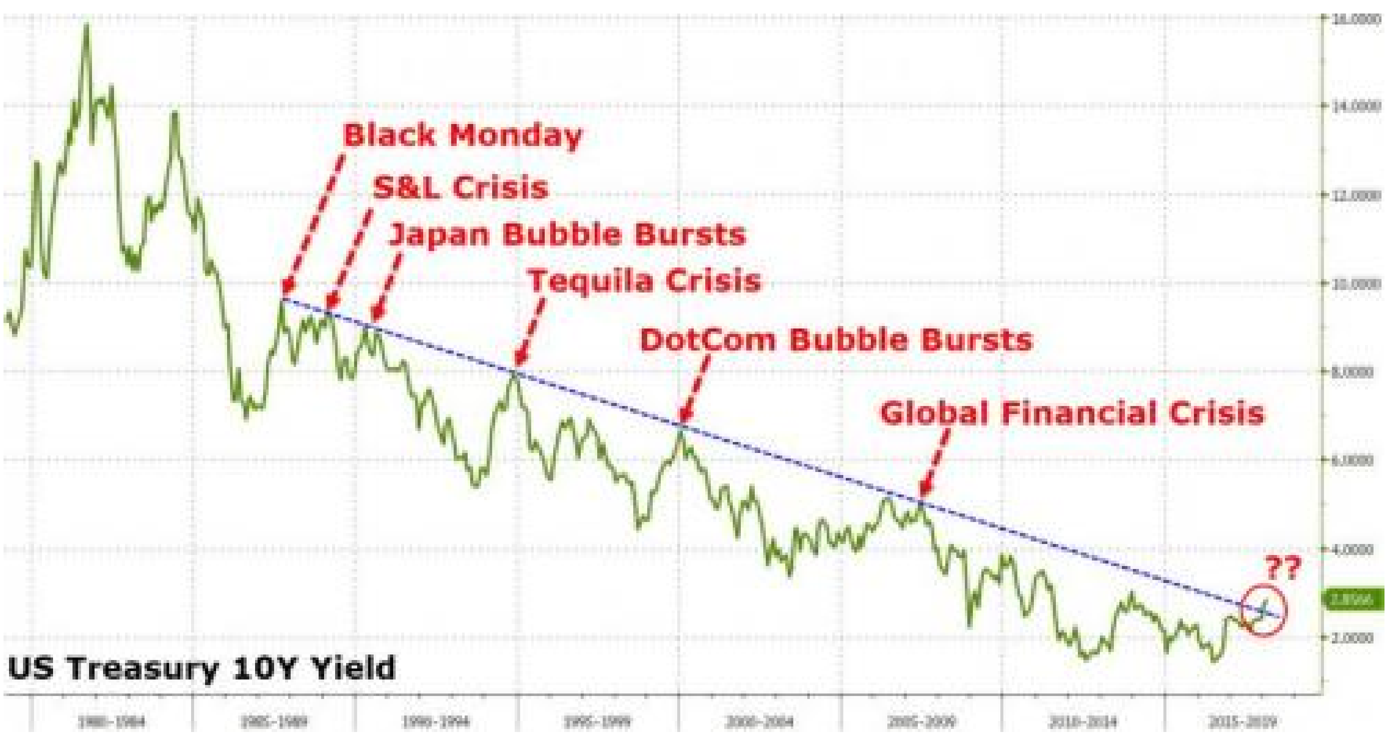


Source: Citi Research, Bloomberg. See our rationale for the 30yr yield view: [US Rates Weekly: The dot plot thickens]

See our framework for rates markets: [Global Rates Strategy View: Can the world live with higher bond yields?]

As of close 27th March.

And here's another, more dramatic, way of visualizing why the Fed is stuck, this time at the 10Y level.



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