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Polar Futures Guarded Opportunity

April 2018

Monthly Performance = -3.67%
YTD = 0.63%
**net of fees*

In my mind the biggest development through April was the USD breaking out of a tight 3 month trading range. This is a move that we have been looking to see happen for the past few months, the consolidation at the lows went longer than expected. Even though we were looking for the move higher in the USD, it was the sharp rally in CAD against our position that caused a majority of the 3.67% loss on the month this month. However if the turn in the USD has in fact taken place, like we think it has, it will be hugely important across a variety of markets, not just currency positions. We believe we are positioned well to benefit from a continued move higher in the USD that should help make up some of the ground given back this month.

We had initially established our short Canadian Dollar position at the end of January given our “laundry list” of issues facing the economy and currency. We maintained the short position through March expecting that the bounce at the end of the month would likely be capped around 78 cent level. However given some further USD weakness to start April, further appreciation in oil and a more positive Bank of Canada outlook survey the Canadian dollar rally picked up velocity, surging to almost 80 cents. We had been trying to stick with this position as it was our outlook that CAD would likely test the lows of 2017 in the low 70 cent range. However even after giving it as much room as risk management allowed, we were stopped out of the position. While still marking a gain on the trade from inception, it was a disappointing step backward to start the month.

We also carried a position short the EUR from March that started the month at about the same level we go into it. In our view the economic slowdown we are seeing in the European data would cause central bank policy to diverge and drive interest rate differentials even further in the USD’s favour. However, interest rate differential have not been a key market driver as the EUR rallied for over a year even as interest rate differential widened against the EUR. The key will be for the soft data to be a catalyst bringing the interest rate differentials back into the picture. So as the EUR moved sideways through the middle of the month I restructured the trade to allow us a longer timeframe on the trade. We finally started to see the EUR make a move to downside making 3½ month lows by month end. Given the record size positioning that speculators have built on the long side of the EUR I am expecting that we could see a significant move lower over the coming months. I also see the Fed continuing to move every second meeting (4 rate hikes in 2018) which is tighter than current expectations and that the ECB will be more likely to leave some accommodative policy in place through the end of the year. Diverging central bank policy continues to be key.

After closing out our initial short 10yr note position in early February on the stock induced volatility, we have been looking for another opportunity to get short. In early April we used the month long consolidation move higher to establish another short position. My thought has been that a strong economic backdrop in the US will keep the FED moving forward with rate hikes, keeping interest rates heading higher. My view is that we have seen a long term structural shift in interest rates and that the turn higher from record low rates in the summer of 2016 marked a significant turning point. After getting close to the 3% level in February, we thought the market was likely to consolidate before making another attempt at getting to, or through, the 3% level. My goal will to try and stay with this position for a strong break above 3%.

Near the end of the month we took another shot on the short side of the oil market. Prices had rallied $12 from the lows of February to the highs of mid-April and appeared to be stalling out under the $70. While there are still geopolitical risk events ahead stemming largely from uncertainty in the Middle East, I think this two month rally has priced a lot or these risk events into current prices. If we were to see any moderation in these risk prices could give back some of the recent gains. While the supply/demand fundamentals have come back from extremely oversupplied levels, as the US moves ever closer to becoming the world's largest crude producer that balance may again come into question. The outside influence I think may also start to weigh on oil prices will be a strong rise we are expecting in the USD. All commodities priced in USD will come under pressure with a rising dollar and this could be the added weight needed to help the oil market start a correction. The aspect that makes this trade so appealing is what I believe to a great risk to reward set up. The speculative long positioning is absolutely massive in oil, so if we see oil prices start to roll over we could see a wave of selling emerge. It is also worth remembering that oil has had a $27 move higher, a move of over 64% in the past 10 months! Plenty of room for a correction and given the market dynamics, it could be sharp!

Until next month, Drew Zimmerman

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