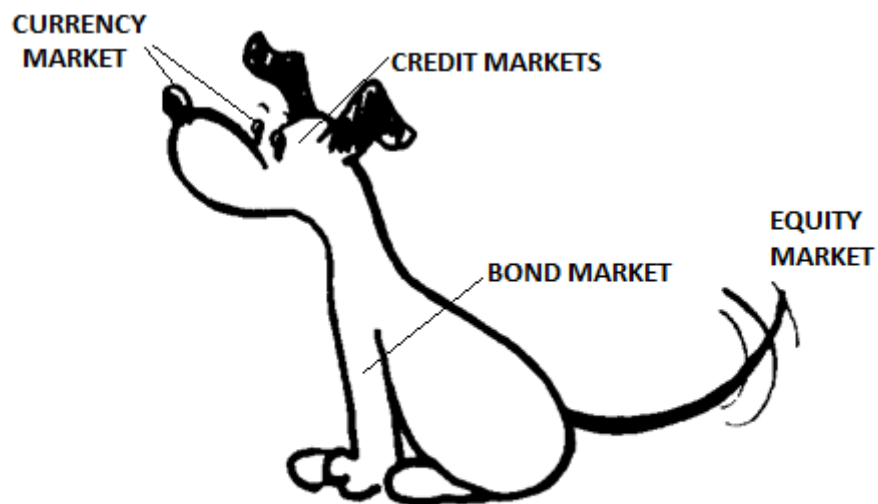


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CREDIT LEADS: Equities Will Be Wagged!

ANALYTIC INSIGHTS



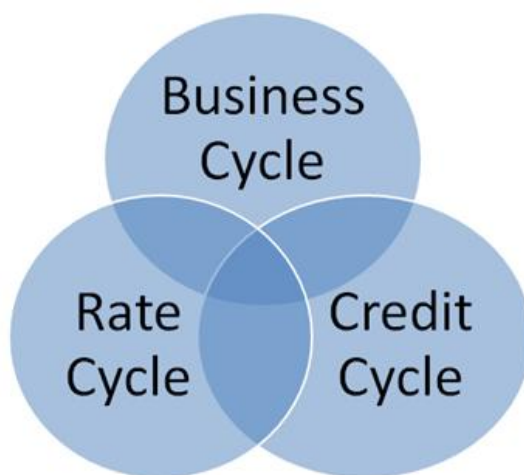
CURRENCY & CREDIT LEAD - BONDS & EQUITY FOLLOW

CREDIT LEADS: Equities Will Be Wagged!

CREDIT INVESTORS BOLT – *HY in Disarray*

3 CYCLES - Three Cycles

What we must fully appreciate is that there are three cycles that work in concert: The Business Cycle, the Rate Cycle and the Credit Cycle. It is our assessment that the Credit Cycles has turned.

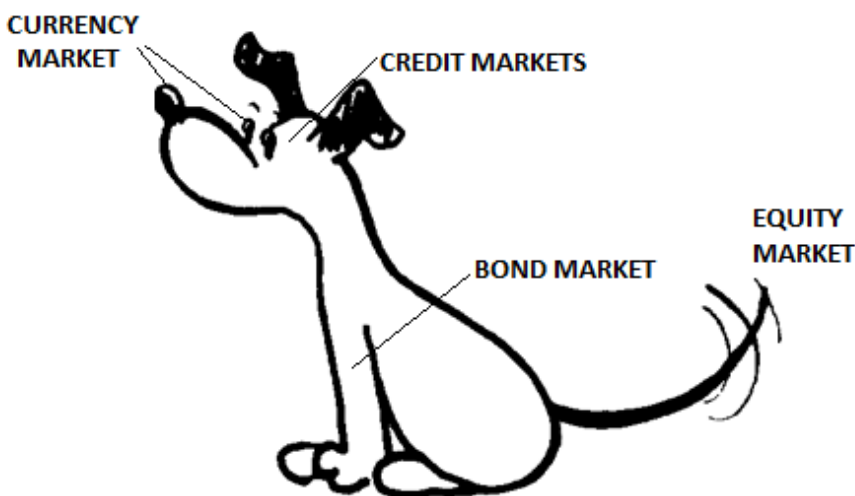


MERRICK CAPITAL

2

CREDIT LEADS

Currency and Credit Markets Lead, Bonds follow and Equities usually are suddenly impacted. Equity direction changes in an unexpected manner. For those watching the cycles and the other markets it isn't that the equity market direction changed, but rather more a matter of how long it was delayed and the timing of it.



HY ETF – *Bond Liquidity*

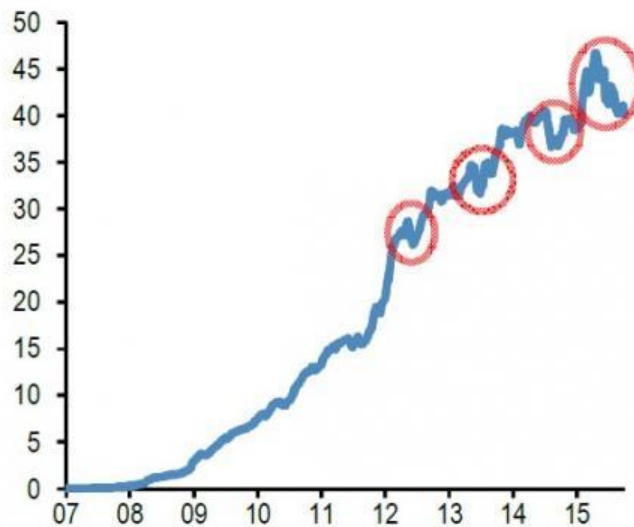
The growth in High Yield (HY) bonds held by ETF's has been nothing short of spectacular. The HY market was previously not readily available to the general public. It was the purview of the professionals.

CURRENCY & CREDIT LEAD - BONDS & EQUITY FOLLOW

Now it is for traders, speculators, mutual funds and anyone else searching for yield and capital appreciation based on QE and ZIRP.

Figure 1: HY ETF AUM

In \$bn. Drawdown marked in red. Red marks are May-12, May-13, Jul-14 And Apr-15.



Source: Bloomberg, J.P. Morgan.

But what happens if this reverses. Is there sufficient liquidity for these ETFs to actually unload their bonds? Who would be the buyers and at what price. This is the proverbial someone shouting fire in a theater with only one exit!

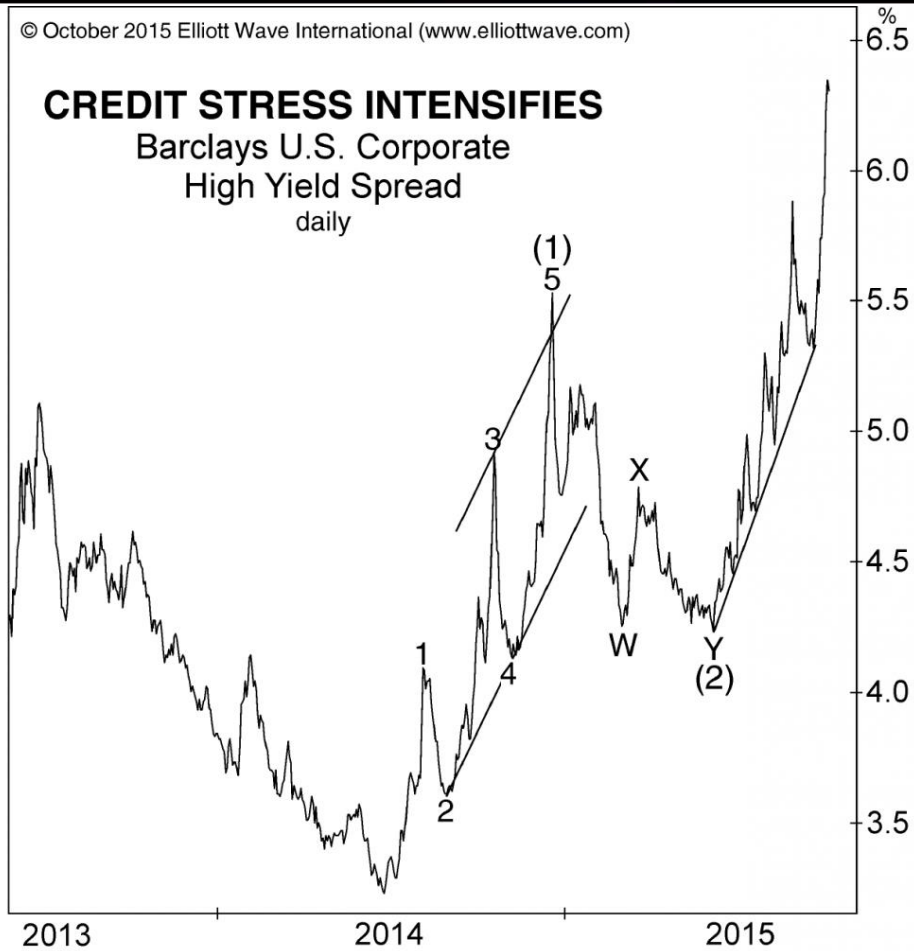
GLOBAL RISK APPETITE – Spreads Are Widening

Global Credit Stress is intensifying. Yields are climbing dramatically as are spreads.

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CREDIT STRESS INTENSIFIES

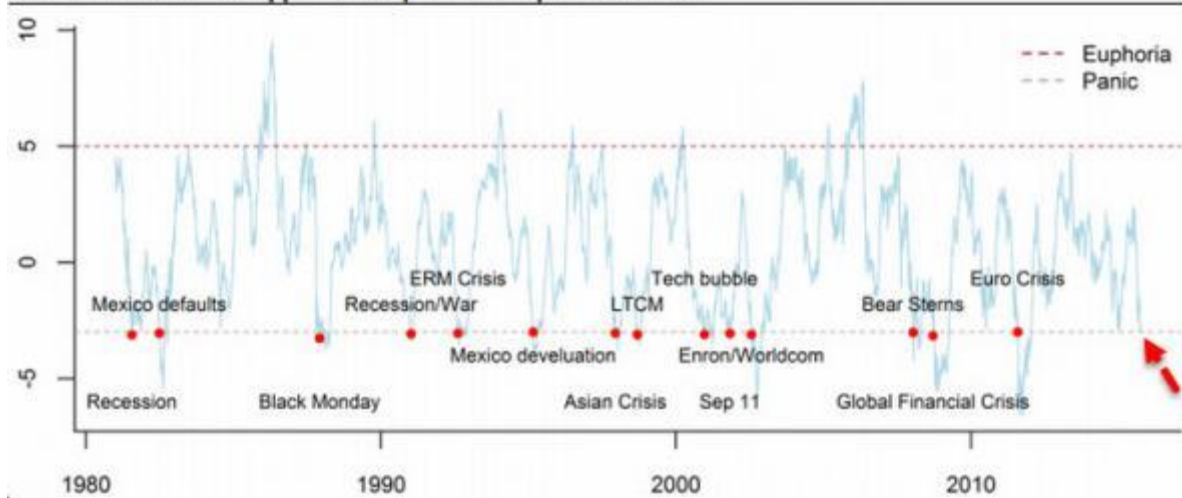
Barclays U.S. Corporate
High Yield Spread
daily



GLOBAL RISK APPETITE - Past Panic Episodes

Global Risk Appetite is falling and is at levels last seen approaching major market moving shocks.

Exhibit 1: Global Risk Appetite with past Panic episode marked



CDX HY INDEX - Signaling A Problem For Some Time

The Credit Default Swaps for HY has been signaling a problem for some time now.

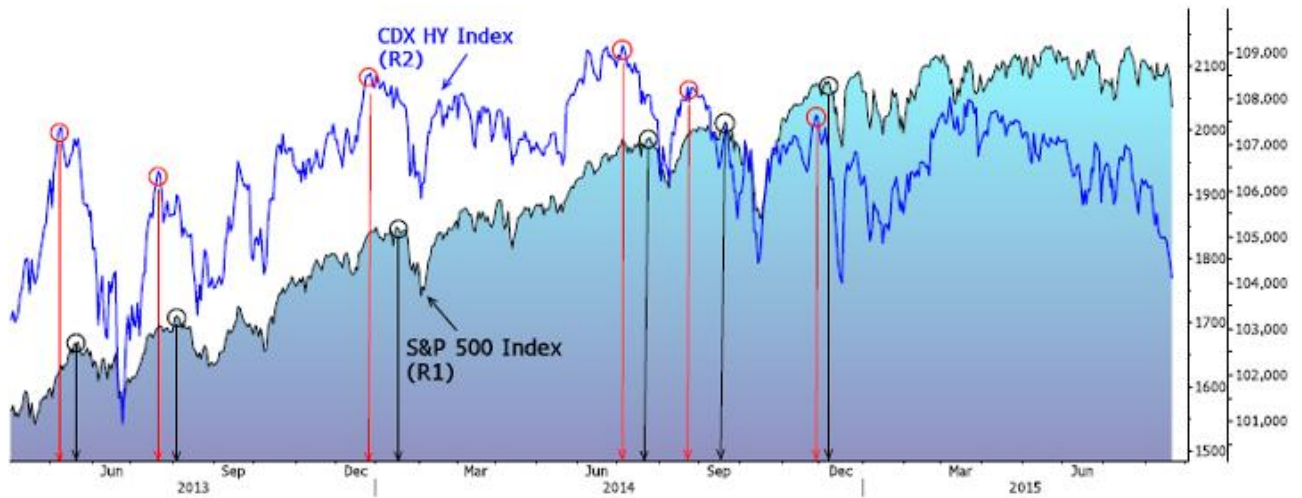
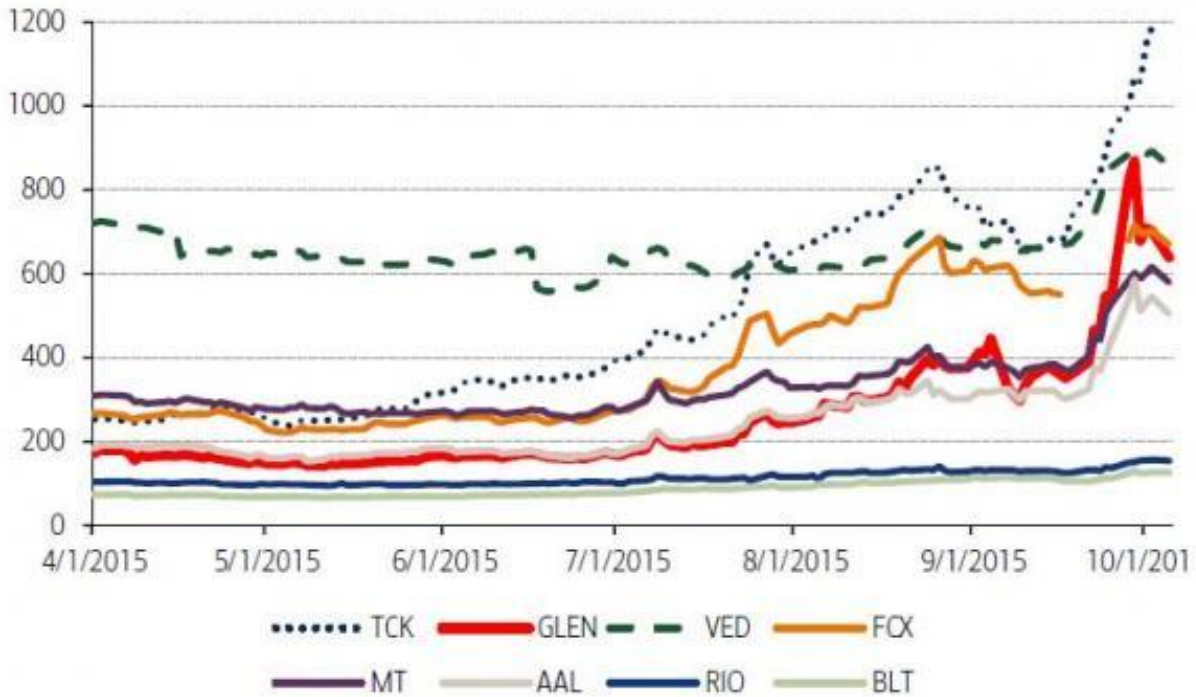


Chart 2: Evolution of Credit Default Swaps (CDS)

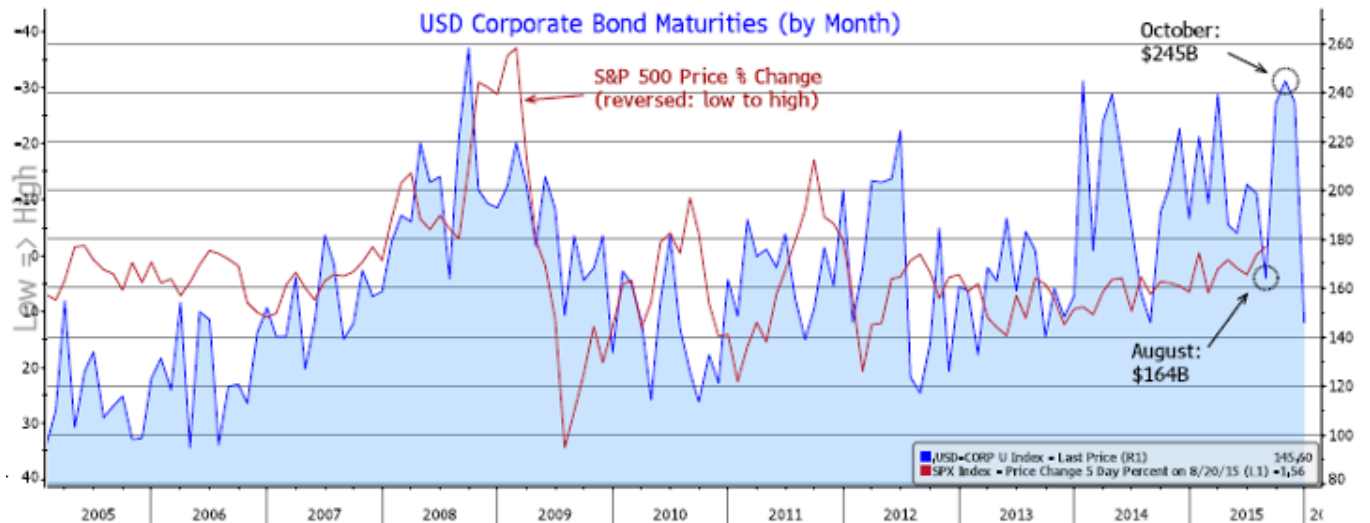


Source: Bloomberg

GLOBAL RISK APPETITE

It isn't just in HY.

It is also in IG Corporate Bonds.



Something is looming!

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