No Relief At The Pump Despite Crude Falling

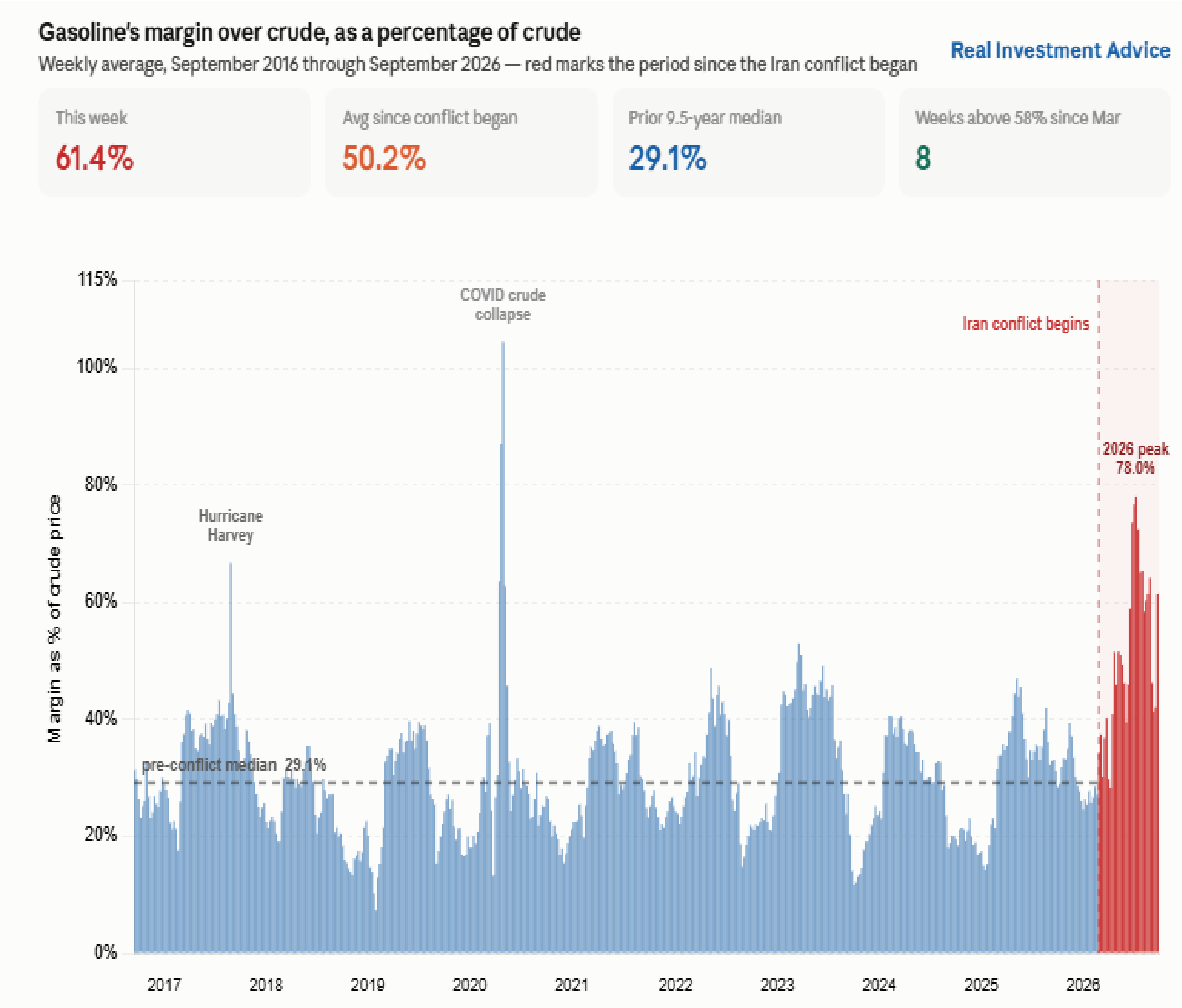
Crude peaked at $106 on September 15 and has since fallen nearly 15% to $90. Despite the recent downturn, gasoline futures are up 1.9% over the same period. The margin between the two widened from roughly $40 to $58 per barrel. That is over three times the twenty-year median, $17, and sits in the 99.8th percentile of every trading day since 2006.

That gap is what a refiner earns for turning a barrel of crude into fuel, which helps explain why there is no relief at the pump. Refining capacity and freight costs are offsetting declines in crude oil.

U.S. refinery utilization hit 97.4% in late August, the highest since 2018. Shipbroker Gibson noted almost no fall maintenance has been scheduled because margins are too high to idle units. They conclude there ?*is no margin for error*.? Furthermore, Ukrainian drone strikes have hit 21 of Russia?s 38 large refineries.

Freight costs are the other half of the problem. Refined products move on smaller, specialized vessels, while crude travels on a large, largely interchangeable tanker fleet. When Hormuz traffic was disrupted, crude found other routes. Gasoline and other products had less spare capacity to absorb it.

Equity markets recognize the bottlenecks and superior refining margins. The S&P 500 Oil Refiner Index is up 132% year to date against 35% for drillers and explorers.



What To Watch Today

Earnings

COMPANY (TICKER)	TIMING	EPS EST.	REV. EST.
Darden Restaurants (DRI)	Before open	$2.06	$3.21B
Costco Wholesale (COST)	After close	$6.55	$94.85B

Economy

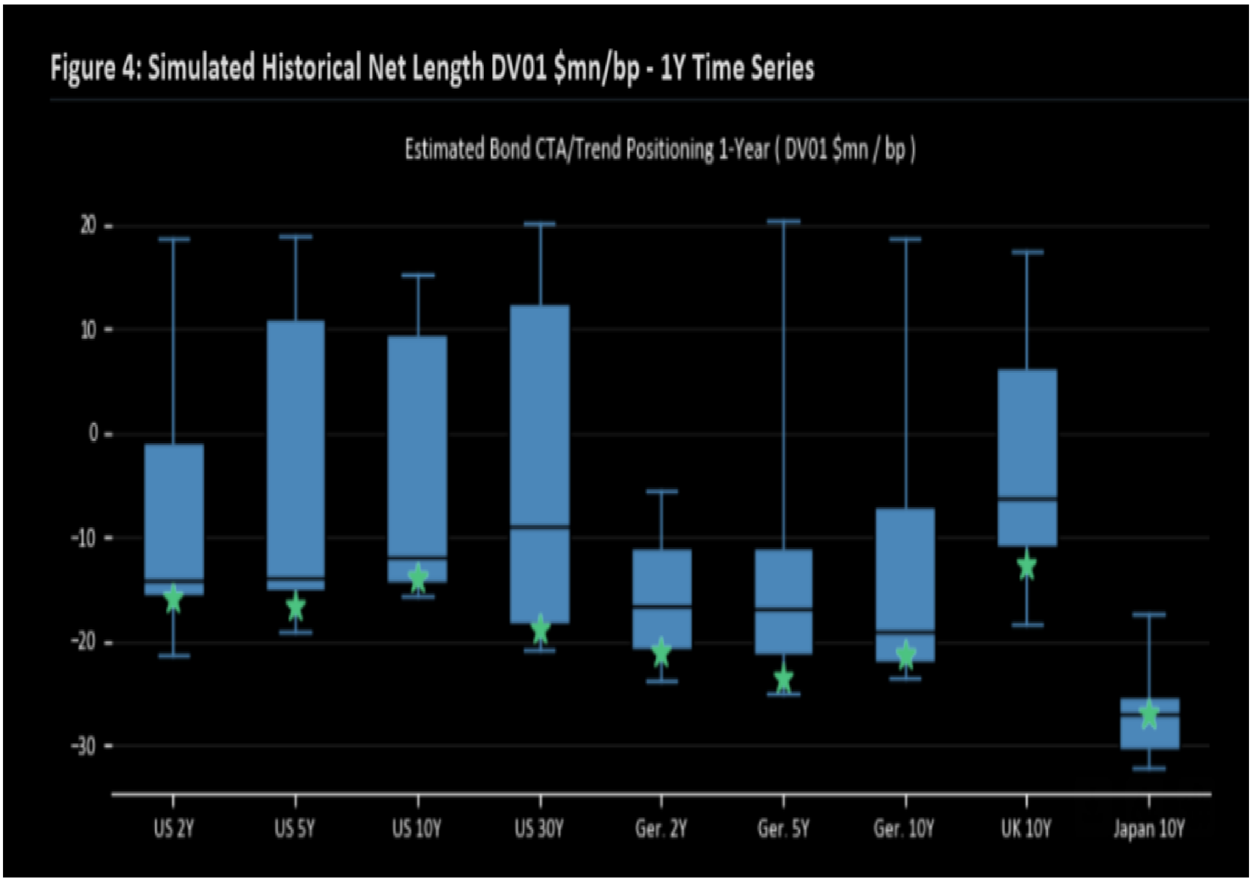
TIME (ET)	RELEASE (PERIOD)	PRIOR	CONSENSUS	FORECAST
8:30 a.m.	Initial Jobless Claims (wk of Sep 19)	196K	201K	201K
8:30 a.m.	Continuing Jobless Claims (wk of Sep 12)	1,730K	1,750K	1,735K
8:30 a.m.	Current Account (Q2)	−$226.8B	−$255.0B	−$249.0B
10:00 a.m.	New Home Sales (Aug)	0.607M	0.620M	0.626M
1:00 p.m.	7-Year Note Auction	4.512%	n/a	n/a

Fed speakers:&#2013266080;NY Fed President Williams (4:10 a.m.), Richmond Fed President Barkin (8:00 a.m.), Cleveland Fed President Hammack (8:50 a.m.), Philadelphia Fed President Paulson (10:10 a.m.). The Fed Board releases the Senior Credit Officer Opinion Survey (SCOOS) at 2:00 p.m.

Market Trading Update

Yesterday, we discussed why 2027 earnings estimates need record profit margins &#2013266080;to keep expanding. Today, I want to turn to the bond market, where a potential bond short squeeze is building. Goldman Sachs estimates that systematic trend followers are short roughly $171 million of global bond DV01. That?s the largest aggregate short since April. Before that, you have to go back to February 2022 to find a comparable reading.

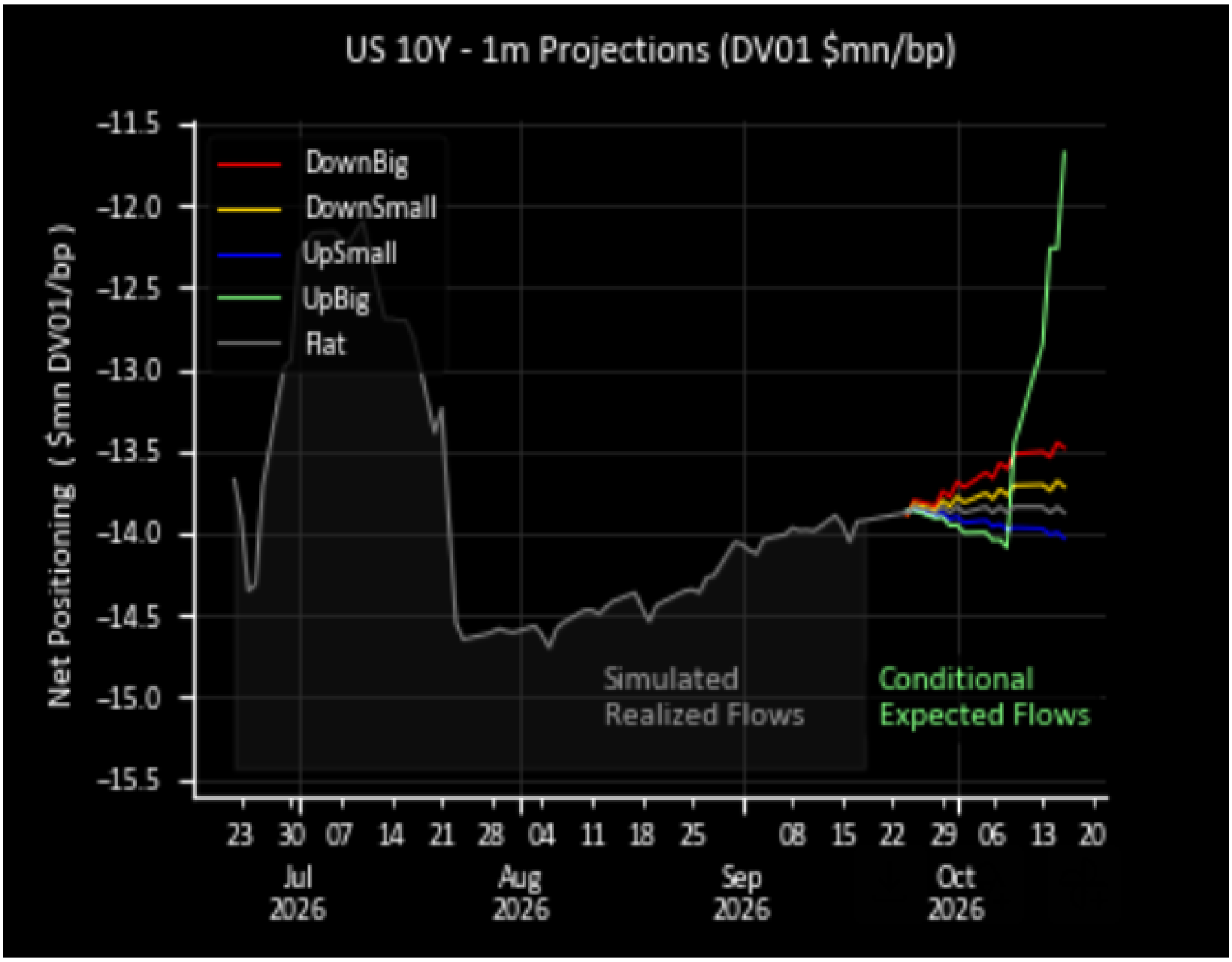
DV01 is simply the dollar change in a position for a one basis point move in yield. In plain English, it measures how much a move hurts. The shorts aren?t concentrated in one spot either. The largest relative bets sit in Japanese and European rates, but the positioning runs across the U.S. curve, including the 5-year. Notice in the chart below that the current readings (the green stars) sit near the bottom of their one-year ranges in nearly every market.



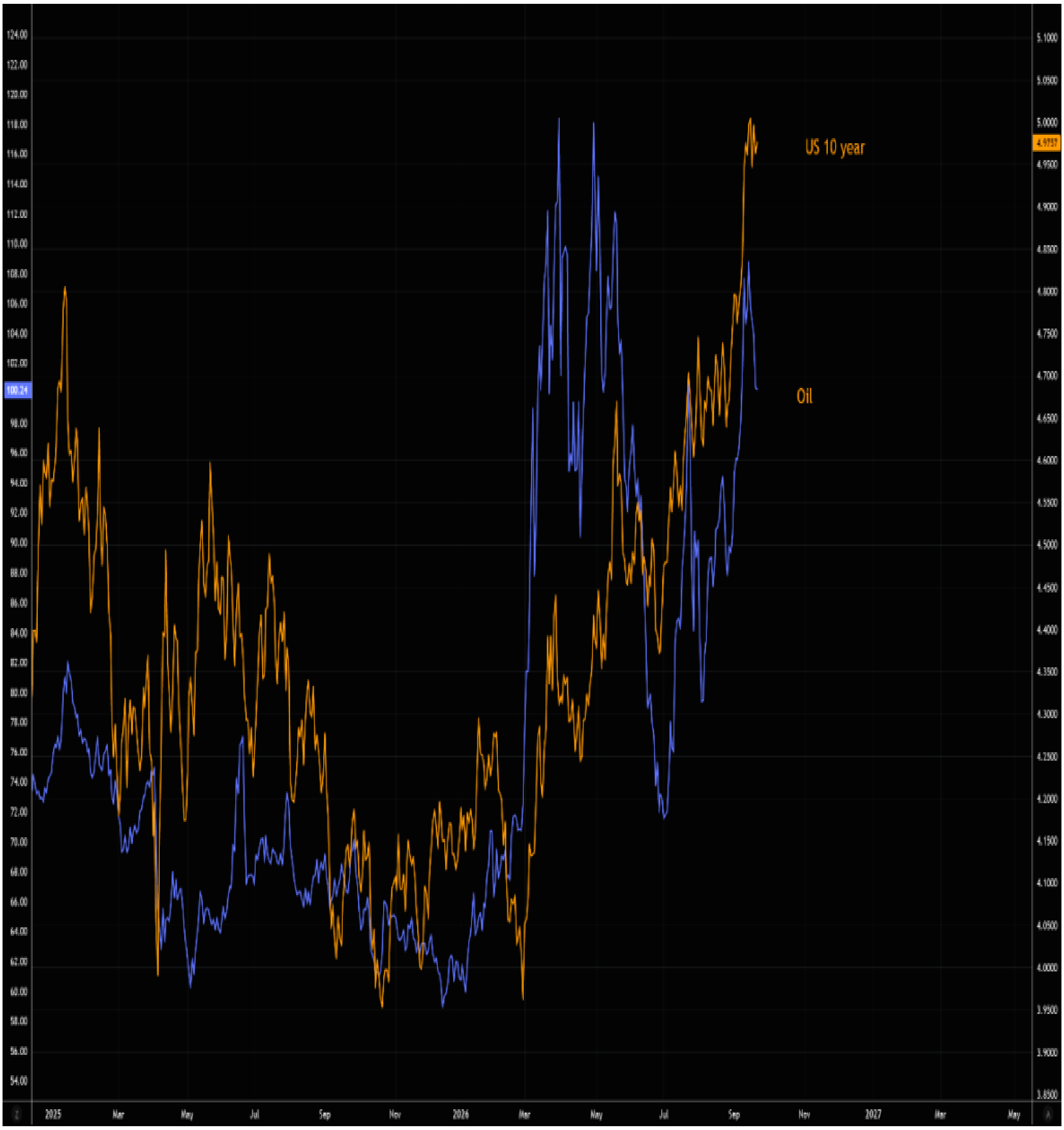
That positioning makes sense given the tape. The 10-year Treasury closed Tuesday at 4.96%, up from 4.64% on August 25. It closed at 5.01% on both September 16 and 18, the highest level since 2007. The 5-year note rate ranged from 4.35% to 4.83% over the same period. Trend followers do exactly what the name implies.

> *?But Lance, if the trend is higher yields, why fight it??*

Because the setup is asymmetric. CTAs need yields to KEEP rising. They don?t need a rate cut to get squeezed.&#2013266080;**They only need yields to stop going up.** &#2013266080;Goldman?s one-month projections for U.S. 10-year positioning show little change in the flat or small-move scenarios. In the ?up big? scenario for bond prices, the covering accelerates sharply into mid-October.



What lights the fuse? Oil is the obvious candidate. WTI slipped below $90 on Wednesday, its sixth straight decline, as talks with Iran eased supply fears, and Brent is back under $100. Slightly softer inflation data would also work. So would central banks simply deliver the tightening already priced, including roughly a 54% chance of another Fed hike in October, without a fresh ?hawkish? surprise. The data don?t have to turn benign. They only have to be less threatening than the market assumes.



[***Bob Farrell?s Rule #2***]() fits: excesses in one direction lead to an opposite excess in the other.&#2013266080;**The confirmation to watch is intermediate Treasury yields falling while the Fed stays publicly hawkish.**&#2013266080;That divergence would tell you positioning, not policy, is driving the tape. Wednesday?s 5-year auction result and today?s 7-year sale are the near-term tests.

For portfolios, we?re using yields near 5% to add duration in stages, focused on the 5- to 10-year part of the curve, rather than all at once. If the squeeze arrives, it rewards those already positioned, not those chasing it. If it doesn?t, a 5% yield pays us to wait. Keep position sizes honest and don?t bet the farm on timing.

Such is the nature of crowded trades. They rarely end quietly.

Bank Stocks Struggle

Bank stocks sold off on Tuesday, with JPMorgan down 3.4%, Bank of America 3%, and American Express 2.6%, while the Nasdaq 100 closed at a record high. That divergence in performance is recent, but underperformance by the largest banks has been a theme this year. The first graphic below shows the excess returns for the last five days. Financial stocks are down 3.27% versus the S&P 500, while the technology sector is up nearly 7%.

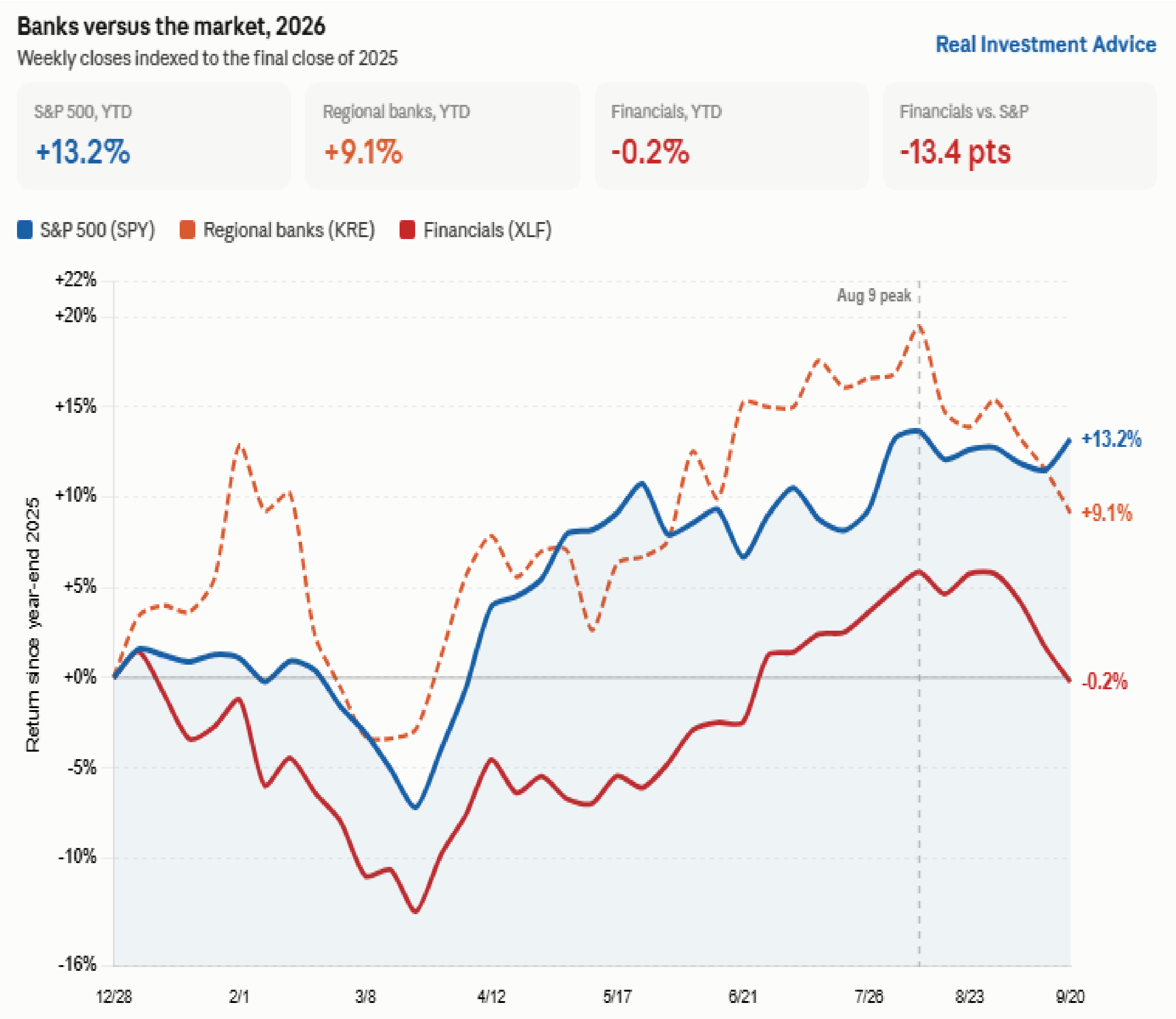
The financial sector ETF, XLF, covering the largest banks and brokers, is down 0.20% year to date despite the S&P 500 rising 13.2%. The 13.4% gap over the last nine months is worth noting, as it may tell investors something about what the market is trying to say. Interestingly, smaller regional banks kept pace with the market until peaking on August 9th. Since then, they have given up half of their annual gains as yields have steadily risen.

The catalyst for the performance differential between the large financial stocks and the broader market is Treasury yields, with the 10-year trading near 5.00%. Higher rates normally help bank margins. However, a flatter yield curve, as is occurring, compresses the spread banks earn. Furthermore, concerns are growing about credit issues involving some companies heavily investing in AI, like Oracle. Credit problems tend to show up in stock prices before they show up in bank financial statements. As such, watch the larger banks? loan-loss reserves in upcoming earnings releases. A sharp uptick may continue the financial sector?s underperformance, but it could also warn the broader market of tightening financial conditions.

SimpleVisor Dashboard Portfolios Market Analytics

BETA BUILD: You're using an early-access beta of SimpleVisor. Features are still evolvi

SYMBOL	1D RETURN	5D RETURN
Energy XLE	-1.09%	-5.74%
Financials XLF	-1.97%	-3.27%
Utilities XLU	-0.32%	-1.19%
Transportation XTN	+0.07%	-0.96%
Consumer Staples XLP	+0.99%	-0.54%
Real Estate XLRE	-0.21%	-0.49%
Communication Services XLC	-1.06%	-0.11%
Materials XLB	+1.65%	+0.06%
Industrials XLI	+0.17%	+1.11%
Consumer Discretionary XLY	+0.09%	+1.53%
Healthcare XLV	+0.52%	+1.72%
Technology XLK	+0.73%	+6.94%



Japan Breaks The ?Debt Causes Inflation Narrative?

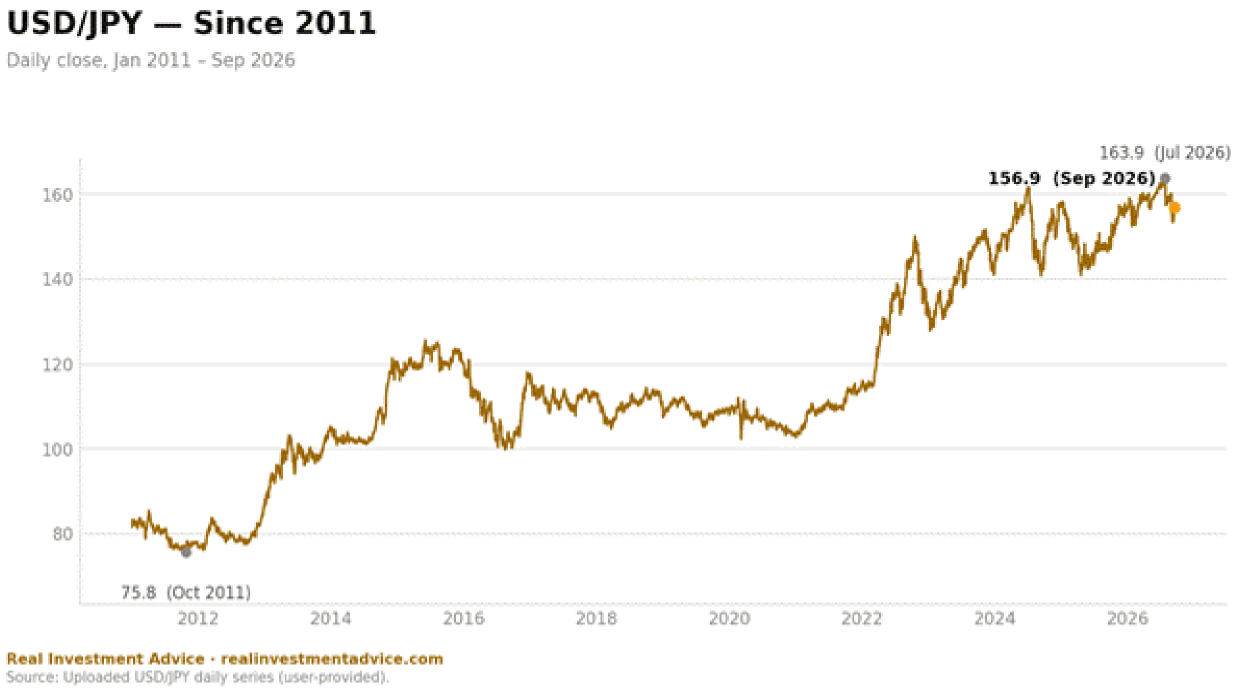
A dollar today buys nearly twice as many Japanese yen as it did fifteen years ago. Crude oil, in yen terms, is up roughly 70% year to date. Food prices are similarly elevated. Japan imports most of the energy and much of the food it consumes, paying for it in dollars that keep getting more expensive. Those facts alone should lead us to conclude Japan has an inflation problem. &#2013266080;

As if those factors weren?t enough, add their debt overhang, with the narrative that mounting government debt is inflationary. **If that logic holds in the US, it should apply with even more force in Japan, where government debt is nearly double ours as a share of the economy, and where the yen carries none of the dollar?s reserve-currency privilege to cushion its borrowing needs.**

A collapsing currency, heavy import dependence, and the developed world?s heaviest debt load. Surely that?s a recipe for an inflation crisis. Instead, Japan?s latest data shows headline CPI at 1.9% and core at 1.7%, both below where the US sits today.

Let?s go to Japan and find out why an economy with seemingly every ingredient for runaway inflation has relatively tame inflation. The facts may change how you think about the relationship between government debt and inflation in the US.

READ MORE?



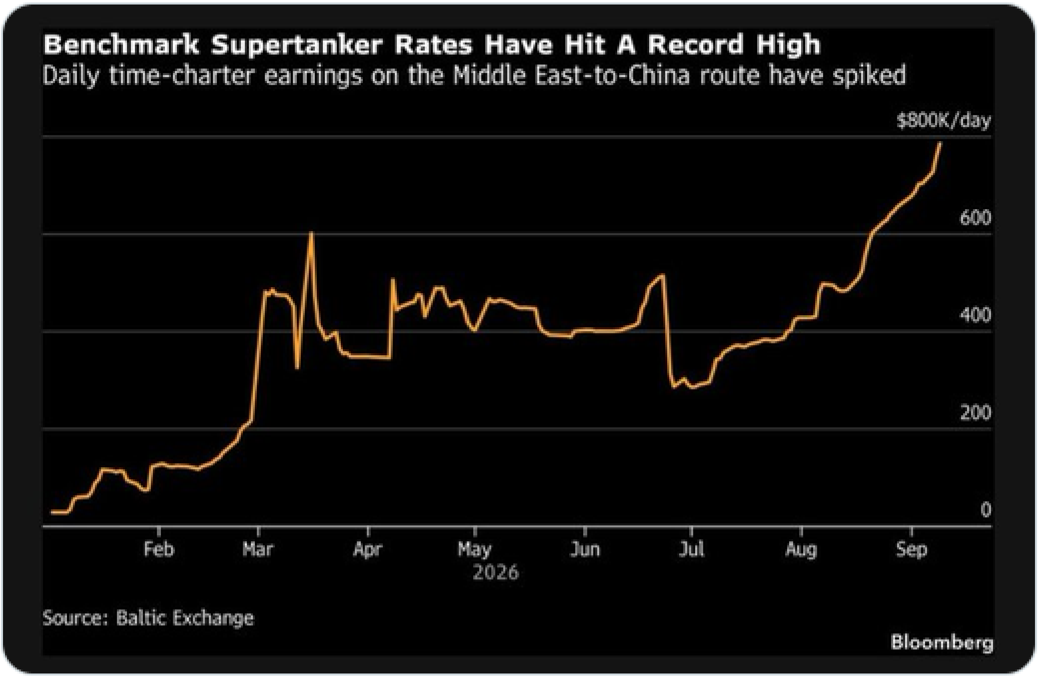
Tweet of the Day

Tracy Shuchart (𝒞𝒽𝒾) @chigrl · Sep 10

Surging **Tanker** Rates Signal a Deepening Global Energy Crisis

Global **tanker** freight rates are surging to record levels with little respite in sight, a sign of the growing strain in oil markets as traders, shipowners, producers and buyers grapple with a drawn-out conflict in the Persian Gulf and increasingly complex workarounds.

Earnings for supertankers sailing on the benchmark Middle East-to-China route are at a record of nearly $800,000 a day. Meanwhile, for the US Gulf to Asia run, charterers have been offering very large crude carriers at a record lump-sum fee of $29.5 million — close to $15 per barrel without considering additional war risks or fees for unexpected delays. (Bloomberg)



New UPDATED Trading Rules With Desktop Printout

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