

# Seven Signs

Seven Signs: 3 Red (not safe/caution), 2 Yellow (neutral), 2 Green (safe). Key risks to stocks are a further slide in oil prices or Euro (EPS risk).

Figure 32: The Seven Signs: cross asset class market signals

| "The Seven Signs" Cross Asset Class Market Signals | Current Level | Change vs 1 Wk Ago | Change vs 4 Week Avg. | Change vs 4 Wks Ago | Level 1yr Ago | Syr Avg. | 20yr Avg. | PCTL Rel to Hist. | Risk Aver. Rel to Hist. | Risk Aversion Level | Incremental Risk Aversion | Strategic Safety | Safe Criteria   |
|--|---------------|--------------------|-----------------------|---------------------|---------------|----------|-----------|-------------------|-------------------------|---------------------|---------------------------|------------------|-----------------|
| <b>Interest Rates and Inflation</b>                |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| 10yr Treasury yield                                | 2.19%         | -0.04%             | 2.15%                 | 0.24%               | 2.53%         | 2.42%    | 4.29%     | 4%                | 96%                     | High                | Down                      | Caution          | 2 - 4%          |
| 10yr TIPS yield                                    | 0.32%         | -0.04%             | 0.26%                 | 0.18%               | 0.33%         | 0.27%    | 1.82%     | 7%                | 93%                     | High                | Down                      | Caution          | 0.5% - 2%       |
| 10yr Treasury - TIPS spread                        | 1.87%         | 0.00%              | 1.90%                 | 0.06%               | 2.20%         | 2.15%    | 2.46%     | 7%                | 7%                      | Low                 | Down                      | Yes              | bet. 1 - 3%     |
| 5yr Treasury yield                                 | 1.51%         | 0.01%              | 1.50%                 | 0.15%               | 1.52%         | 1.34%    | 3.68%     | 5%                | 95%                     | High                | Down                      | Caution          | 1.5% - 3%       |
| 30yr Treasury yield                                | 2.99%         | -0.06%             | 2.90%                 | 0.35%               | 3.41%         | 3.44%    | 4.88%     | 3%                | 97%                     | High                | Down                      | Caution          | 2.5% - 4.5%     |
| Fed Fund Rate 2015 End (Futures)                   | 0.33%         | 0.02%              | 0.33%                 | -0.03%              | 0.58%         | 0.25%    | 2.80%     |                   |                         | High                | Up                        | Yes              | below 2.5%      |
| Fed Fund Rate 2016 End (Futures)                   | 1.05%         | 0.02%              | 1.07%                 | 0.04%               | 1.58%         | 0.25%    | 2.80%     |                   |                         | High                | Down                      | Yes              | below 2.5%      |
| <b>Duration</b>                                    |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| US Treasury yield curve slope (10-2yr)             | 1.62%         | -0.07%             | 1.57%                 | 0.19%               | 2.19%         | 2.00%    | 1.22%     | 73%               | 27%                     | Normal              | Down                      | Yes              | above 100bps    |
| US Treasury yield curve slope (10-5yr)             | 0.68%         | -0.05%             | 0.65%                 | 0.09%               | 1.01%         | 1.08%    | 0.60%     | 79%               | 21%                     | Normal              | Down                      | Caution          | above 60bps     |
| <b>Credit</b>                                      |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| Corporate IG credit spreads (bps)                  |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| Financial  | 126.1         | 0.9                | 125.5                 | -2.6                | 115.2         | 191.8    | 175.7     | 45%               | 45%                     | Normal              | Down                      | Yes              | below 200       |
| Industrial   | 134.1         | 1.7                | 132.3                 | -2.9                | 107.5         | 140.6    | 156.0     | 46%               | 46%                     | Normal              | Down                      | Yes              | below 200       |
| Financial spreads over Industrial                  | -8.0          | -0.8               | -6.8                  | 0.3                 | 7.7           | 51.2     | 19.8      | 44%               | 44%                     | Normal              | Up                        | Yes              | below 50        |
| Corporate HY credit spreads (bps)                  |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| TED spreads (bps)                                  | 479.1         | -3.4               | 486.4                 | -29.0               | 395.7         | 533.5    | 610.8     | 36%               | 36%                     | Normal              | Down                      | Yes              | below 600       |
| Muni spreads (bps)                                 | 27.2          | 0.6                | 27.0                  | 1.3                 | 19.7          | 25.5     | 43.8      | 41%               | 41%                     | Normal              | Up                        | Yes              | below 50        |
| Sovereign spreads (bps)                            |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| Germany  | -155.2        | -2.3               | -165.2                | 10.6                | -110.9        | -64.5    | -42.4     | 2%                | 2%                      | Low                 | Up                        | Yes              | below 0 bps     |
| France   | -127.0        | -0.9               | -137.2                | 10.9                | -69.0         | -4.4     | -19.5     | 2%                | 2%                      | Low                 | Up                        | Yes              | below 100 bps   |
| Italy  | -35.1         | 2.6                | -46.1                 | 12.3                | 66.8          | 184.5    | 80.4      | 24%               | 24%                     | Low                 | Up                        | Yes              | below 100 bps   |
| Spain  | -42.7         | -3.2               | -49.9                 | 12.8                | 47.9          | 197.6    | 65.9      | 25%               | 25%                     | Low                 | Up                        | Yes              | below 100 bps   |
| <b>Currency</b>                                    |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| US Dollar index                                    |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| USD/EUR  | 87.58         | -1.1%              | 89.12                 | -2.5%               | 76.50         | 75.79    | 86.35     | 62%               | 62%                     | Normal              | Down                      | Neutral          |                 |
| JPY/USD  | 1.1112        | -2.6%              | 1.1185                | 3.9%                | 1.3687        | 1.3133   | 1.2229    | 27%               | 73%                     | High                | Down                      | Caution          | \$1.20 - \$1.40 |
| CHF/USD  | 121.04        | 1.6%               | 119.75                | 0.1%                | 101.37        | 92.46    | 107.50    | 85%               | 15%                     | Low                 | Down                      |                  |                 |
| USD/Gold (real \$)                                 | 0.9368        | 2.7%               | 0.9321                | -3.3%               | 0.8932        | 0.9325   | 1.2406    | 15%               | 85%                     | High                | Up                        |                  |                 |
| <b>Commodities</b>                                 |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| CRB  |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| Brent Oil  | 509.7         | -1.7%              | 507.8                 | 0.0%                | 545.3         | 625.3    | 344.5     | 75%               | 75%                     | High                | Up                        |                  |                 |
| WTI Oil  | 426.02        | -1.0%              | 424.71                | 2.4%                | 499.05        | 484.65   | 344.20    | 73%               | 27%                     | Low                 | Down                      | Not Safe         |                 |
| Natural gas  | 66.54         | -0.1%              | 66.02                 | 11.6%               | 110.55        | 100.72   | 55.81     | 62%               | 38%                     | Normal              | Down                      | Caution          | \$70 - \$100    |
| Copper   | 60.72         | 1.4%               | 59.18                 | 12.3%               | 104.07        | 90.02    | 54.05     | 57%               | 43%                     | Normal              | Down                      | No               | \$70 - \$100    |
| <b>Uncertainty</b>                                 |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| VIX  |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| 1M Implied Vol                                     | 2.95          | -2.0%              | 2.81                  | 7.8%                | 4.47          | 3.71     | 4.47      | 28%               | 72%                     | High                | Down                      | Neutral          |                 |
| 1M Realized Vol                                    | 6249.0        | -2.5%              | 6293.4                | 4.1%                | 6885.0        | 7598.3   | 4471.1    | 62%               | 38%                     | Normal              | Down                      | No               |                 |
| 1M Vol Premium (Implied - Realized)                | 10.3          | -0.5               | 11.4                  | -0.8                | 10.2          | 15.6     | 18.7      | 6%                | 6%                      | Low                 | Down                      | Yes              | below 18        |
| Correlation (S&P 500)                              | 10.0          | -1.3               | 10.0                  | -2.6                | 8.6           | 14.2     | 16.8      | 23%               | 23%                     | Low                 | Down                      | Yes              | below 18        |
| 1M Implied Correlation                             | 0.3           | 0.9                | 1.5                   | 1.8                 | 1.6           | 1.4      | 1.7       | 29%               | 29%                     | Low                 | Up                        | Yes              | below 3         |
| 1M Realized Correlation                            | 34.0          | -3.7               | 33.7                  | 5.0                 | 35.5          | 41.9     | 36.9      | 46%               | 46%                     | Normal              | Up                        | Yes              | below 40        |
| 1M Correl Premium (Implied - Realized)             | 25.8          | -3.5               | 24.7                  | -12.9               | 19.6          | 38.0     | 31.6      | 41%               | 41%                     | Normal              | Down                      | Yes              | below 40        |
| LTM PE / 3m Avg. VIX (mkt emotion)                 | 8.2           | -0.2               | 9.1                   | 17.9                | 15.9          | 3.9      | 2.8       | 73%               | 73%                     | High                | Up                        | Yes              | below 10        |
| <b>Offered Equity Risk Premium</b>                 |               |                    |                       |                     |               |          |           |                   |                         |                     |                           |                  |                 |
| LTM PE   | 1.30          | 0.02               | 1.24                  | 0.13                | 1.21          | 0.90     | 0.98      | 88%               | 12%                     | Low                 | Down                      | No               | 0.8 - 1.2       |
| PE on 2015E EPS                                    | 18.1          | 0.5%               | 17.9                  | 1.1%                | 17.0          | 15.2     | 18.5      | 71%               | 29%                     | Low                 | Down                      | Caution          | below 18        |
| PE on normalized 2015E EPS                         | 18.1          |                    |                       |                     |               |          |           |                   |                         | Low                 | Down                      | Caution          | below 17        |
| Implied real return offered by S&P 500             | 17.6          |                    |                       |                     |               |          |           |                   |                         | Low                 | Down                      | Caution          | below 17        |
| Implied ERP offered by S&P 500                     | 5.5%          | -0.5%              | 5.6%                  | -1.1%               | 5.9%          | 6.7%     | 6.5%      | 26%               | 26%                     | Low                 | Down                      | Caution          | above 5.5%      |
|  | 5.2%          | 0.3%               | 5.3%                  | -4.3%               | 5.6%          | 6.2%     | 3.6%      | 77%               | 77%                     | Low                 | Down                      | Yes              | above 4%        |

Source: FRB, Bloomberg Finance LP, I/B/E/S, Deutsche Bank  
A signal's risk aversion is based on its current level expressed as a percentile of all the observations in its long-term history. Monthly observations from 1960 for Interest Rates & Inflation, Duration, LTM PE and Implied ERP, 20 yr history for the rest.

