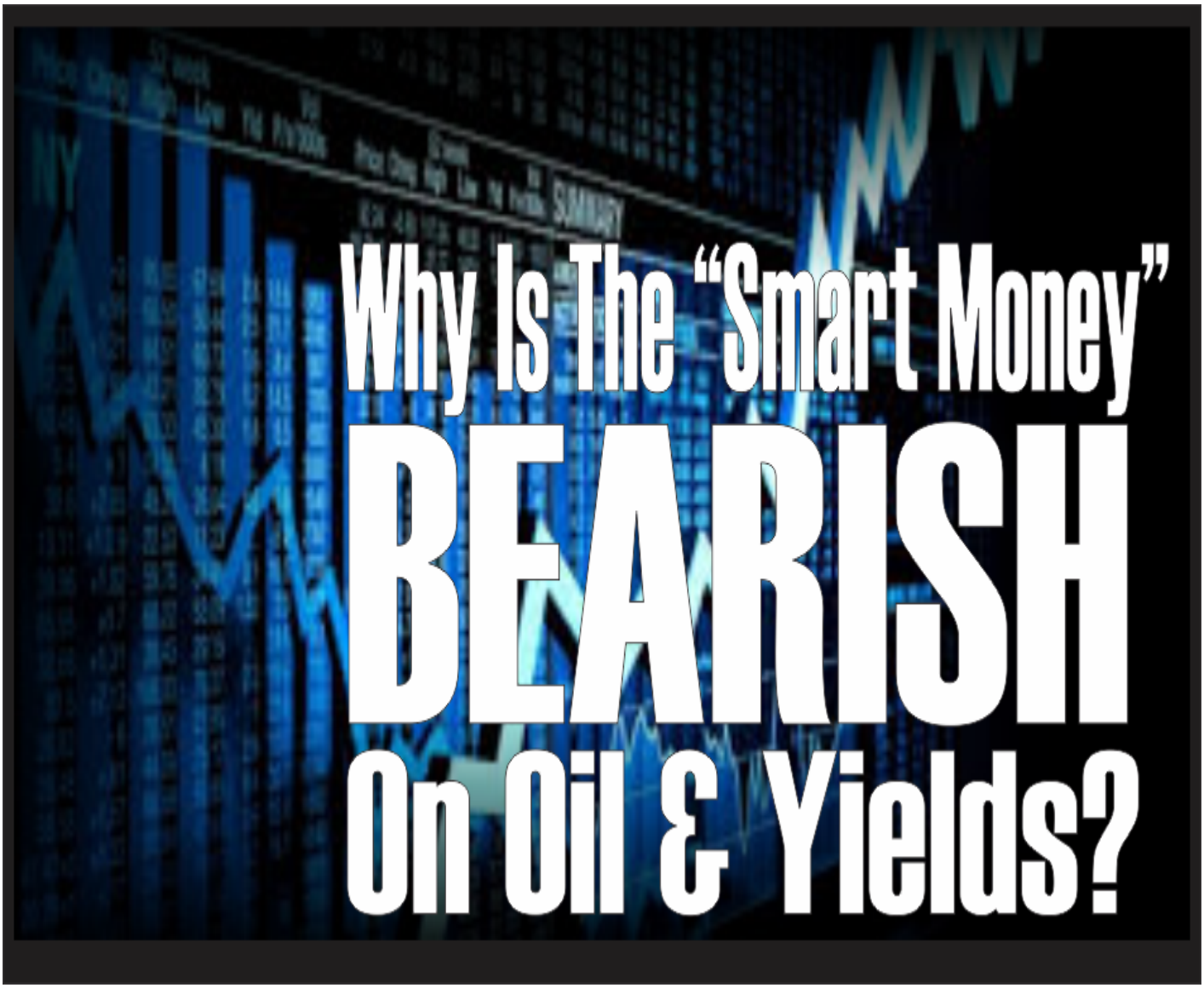
RIA Advice



In recent weeks, I've been discussing an interesting phenomenon I've been observing: "the crowd" or "dumb money" are almost unanimously bullish on crude oil and U.S. Treasury bond yields, while "the smart money" are betting in the exact opposite manner. The "dumb money" consists of large, trend-following funds that tend to be wrong at major market turning points, while "smart money" are commercial hedgers who tend to be right at major market turning points. In this piece, I will tie the two pieces of this puzzle together and discuss likely reasons for this unusual and notable positioning. The weekly chart of West Texas Intermediate crude oil shows that the "smart money" (commercial hedgers) are bearish and the "dumb money" (large funds) are bullish. The positioning of these two groups is ***even more extreme*** than it was before the oil crash in the spring of 2014.

The monthly chart of WTI crude oil shows just how unprecedented the current positioning is:

The "smart money" are bullish on U.S. Treasury bonds (which means that they are bearish on bond yields), while the "dumb money" are bearish on bonds (which means that they are bullish on bond yields). This•"smart money"-"dumb money" positioning is the same in 30 Year U.S. Treasury Bonds, 10 Year Notes, and 5 Year Notes, as the three charts below show:

Let me proffer a theory to explain why the "smart money" and "dumb money" may be positioned the way they currently are in crude oil and bonds: crude oil and U.S. Treasury bond yields are

positively correlated; when crude oil rises, it leads to higher inflation expectations, which leads to higher interest rates (and vice versa).•Here's the mainstream market narrative right now?•*the economy is doing quite well, unemployment is low and job growth is steady, the housing market is improving, inflation is finally picking up, and interest rates will continue to rise to reflect this new reality.?* The "smart money," on the other hand, appear to be skeptical of this mainstream narrative - and for good reason! This group may be expecting another wave of economic disappointment and a sharp downward move in crude oil, which would cause U.S. Treasury bond prices to rebound (and yields to fall). Though I am aware that•the "smart money" and "dumb money" can hold extreme positions for a long time before the market (price) catches up with their view, I am looking out for tactical signals that indicate that another major move is imminent. **Please follow or add me on•Twitter,•Facebook, and•LinkedIn•to stay informed about the most important trading and bubble news as well as my related commentary.**