Creative Global Investments

Weekly investment strategy & charts

Thursday, April 20th, 2017

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"Just Surface cracks"?

As we have been warning investors for the past 8 weeks, we have highlighted noticeable surface cracks in the US economy, which slowly are impacting how the US$, US bonds and US equities are performing.

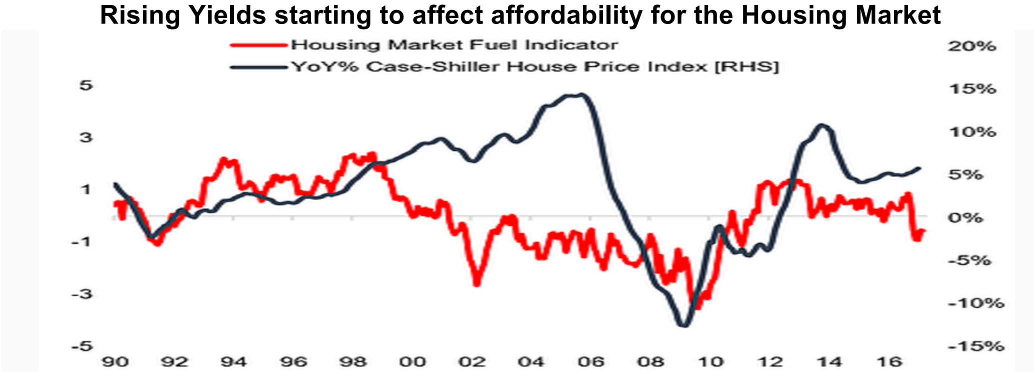
The most relevant ones, which we highlighted and show increasing deterioration are:

- Commercial Credit slowing
- Corporate Spending slowing
- Corporate Productivity slowing
- Inflation slowing
- Consumer credit extremely high
- Consumer confidence not translating into incremental sales
- Auto Sector slowing
- Housing Sector slowing

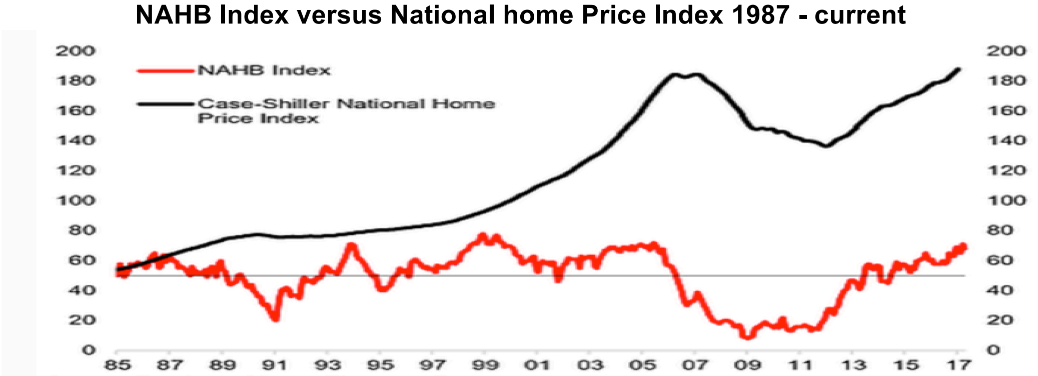
The latest report on housing starts was down -6.8% m/m during March, and the NAHB Housing Market Index for the month of April fell to 68 (vs. 71), having gone through a lengthy recovery following the housing market collapse in 2007. We can clearly see the jump in rates since November affecting affordability at the same time as wage growth and jobs growth have collectively topped out.

Unless something changes on either front (lower mortgage rates/bond yields or an acceleration in wage growth) the weaker "housing market fuel indicator" will continue to wave a downside risk flag for what is a major sector of the US economy. This indicator for the health of the housing market is combining affordability factors (prices vs. mortgage rates) and income factors (wage and jobs growth), and is currently showing increasing downside risks.

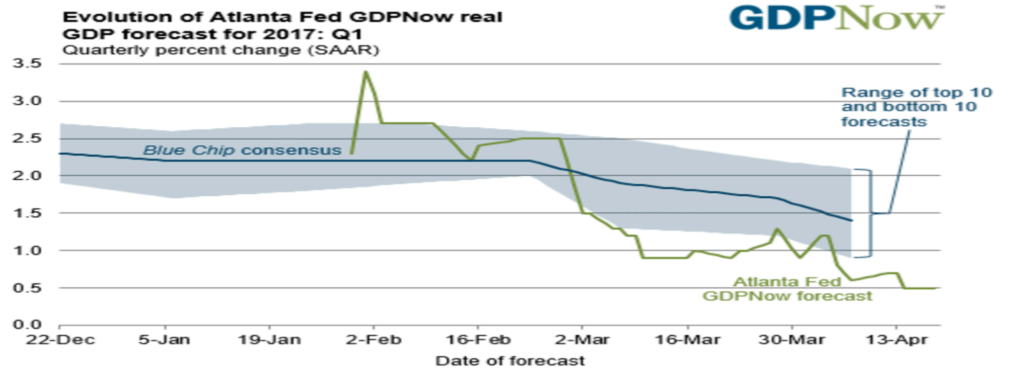
Rising Yields starting to affect affordability for the Housing Market



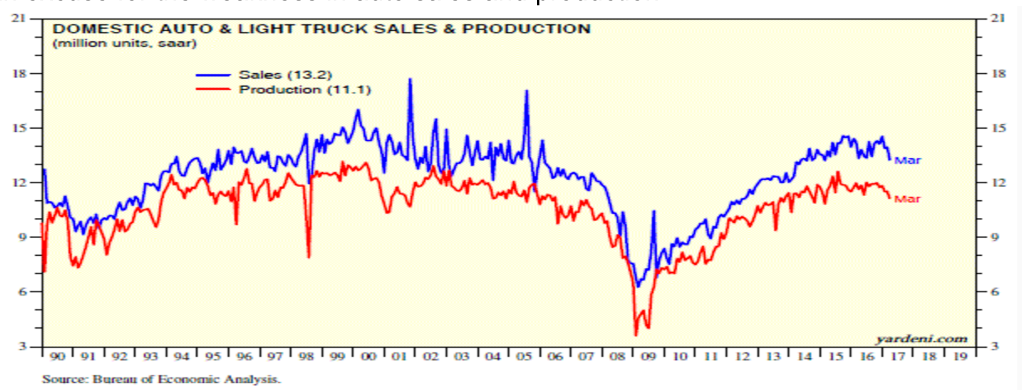
The housing market fuel indicator combines affordability factors (prices vs. mortgage rates) and income factors (wage and jobs growth). Currently, homebuilders remain optimistic on the housing market, but we see this likely change quickly, and we believe they are again, like in 2006 "very late to the plate".



Additionally, manufacturing output is down -0.4% last month, the Atlanta Fed's GDPNow model showed an increase of just 0.5% (SAAR) in Q1's real GDP.

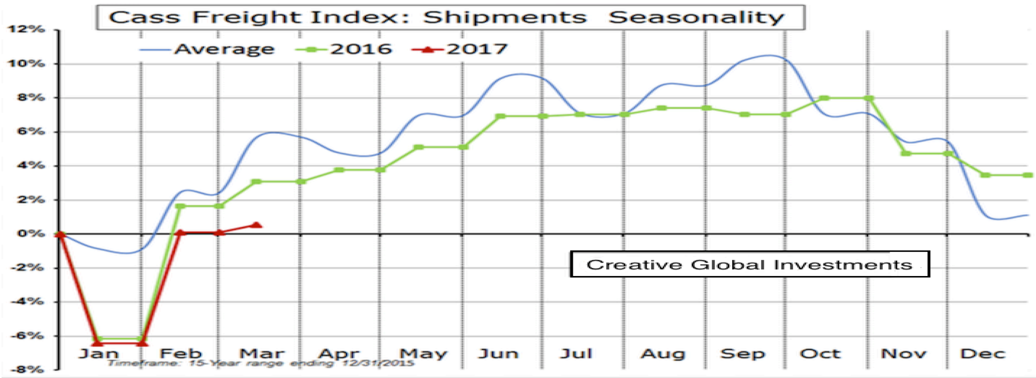


As already mentioned over the past 5 months, the auto industry in the US is in a major soft patch in the economy. Auto output fell -3.6% during March. Auto assemblies are down -7.3% over the past five months to 11.1MN units (SAAR) from last year's peak of 12.0MN. The weather was blamed for the drop in housing starts, but doesn't apply as an excuse for the weakness in auto sales and production.

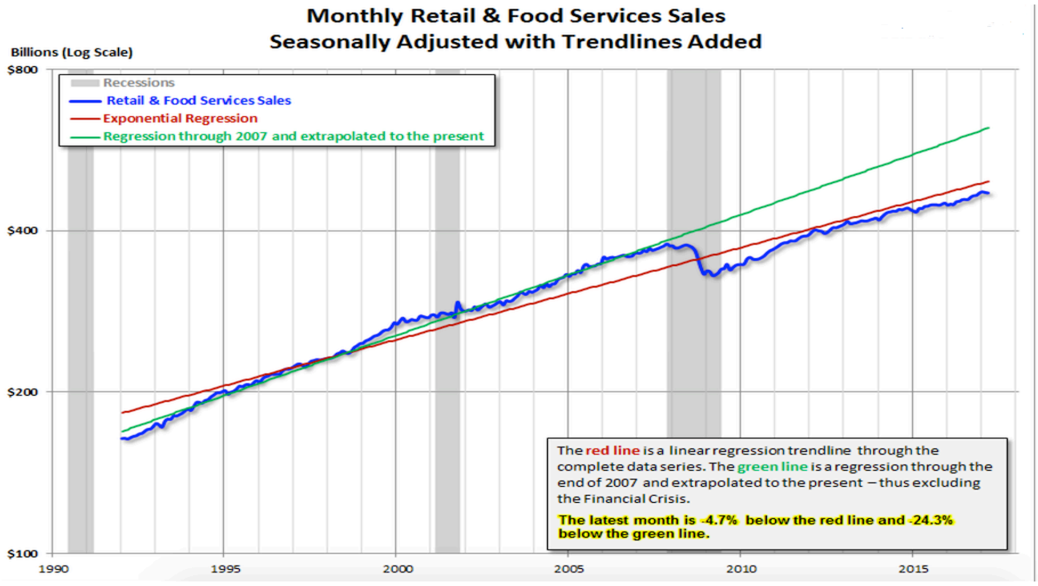


There are other soft patches in the economy. For example, the ATA Truck Tonnage Index dipped -1.0% m/m in March, and is up by only 0.7% y/y. In other words, it has stalled at a record high over the past year. Sales of medium-weight and heavy trucks dropped -8.0% m/m in March and -19.0% y/y.

Another gauge we use frequently is the Cass Information Systems, which released their latest freight index for the month of March, providing a gauge of economic activity in the US. The report indicated that the shipments index rose by only 0.5% last month, while the expenditures benchmark fell by -1.2%; the average change for each in the third month of the year is an increase of 2.9%. The result has brought the expenditures gauge back inline with the seasonal average trend, while the level of shipments continues to lag this historical norm. While the lagging trend in the year-to-date change in shipments, which would be expected to have a direct correlation with broader economic activity, does present concern, it may be premature to count out a rebound as we enter the spring months. Yesterday's report highlighted the lag in industrial production through Q1, failing to represent the enthusiasm portrayed in many of the sentiment surveys released during the period.



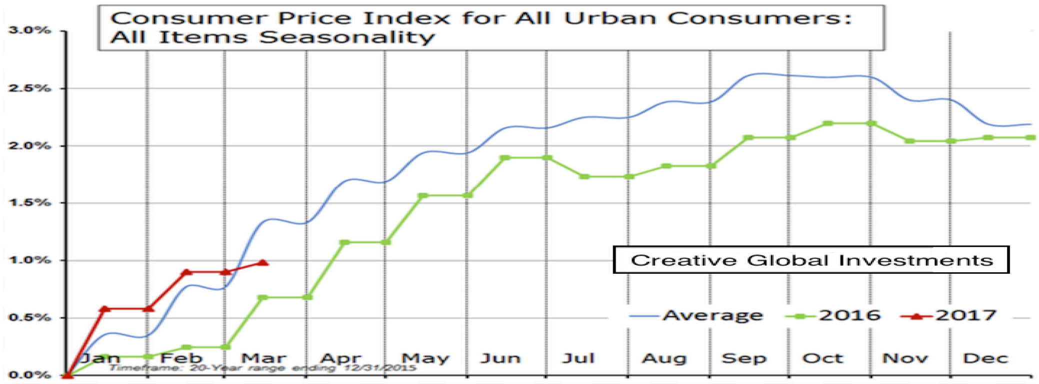
The Census Bureau's Advance Retail Sales Report for March released last week showed a decrease over the February figures. Headline sales came in at -0.2% m-o-m and the February number was revised downward from 0.1% to -0.3%. Thursday's headline number was below consensus of -0.1%. Core sales (ex Autos) came in at 0.1% m-o-m, which was below the consensus of 0.3% and the February Core was revised downward.



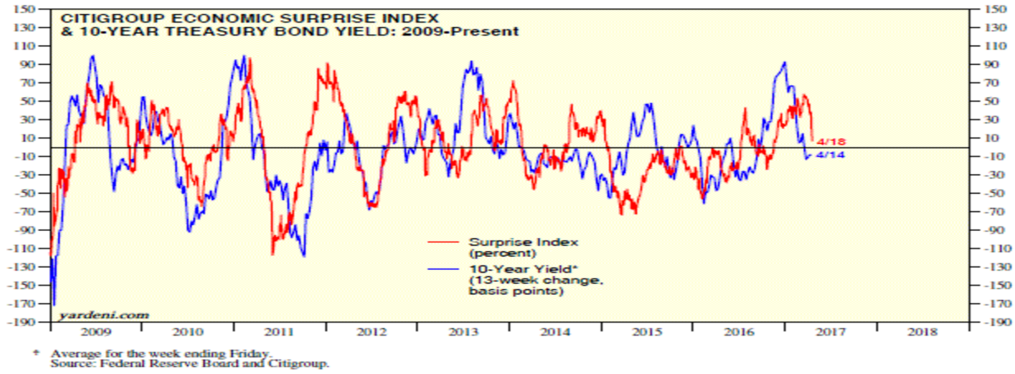
Additionally, the headline print indicated that CPI declined by -0.3% last month, missing estimates for no change (0.0%). Less food and energy, the decline was more muted at 0.1%, but still less than forecasts calling for a 0.2% rise. Stripping out the seasonal adjustments, the All Items Consumer Price Index for All Consumers increased by 0.1%, less than the average increase for March of 0.5%.

Excluding the more volatile components of food and energy, the increase was the same as the aggregate result at 0.1%, still firmly below the average increase of 0.4% for the third month of the year. This is the lowest March increase in the 20-year history that was studied. The result has weakened the year-to-date change to below the seasonal average trend, placing at risk the 2% annual threshold that has become average for the calendar year.

The average is also inline with the Fed's target inflation rate, a target they've struggled to sustain throughout the recovery. Inflationary pressures are typically the greatest in 1H, but March's report is certainly not reflective of this average tendency.



So, in aggregate, we are not surprised a bit by the fact that the Citigroup (NYSE:C) Economic Surprise Index (CESI) has plunged from a recent high of 57.9 on March 15 to 6.6 on Tuesday, which is likely to put pressure on the Fed to hold off on another rate hike for now, and on the Trump administration to move forward with its fiscal stimulus agenda. Treasury Security Steve Mnuchin said on Monday that tax reform might not happen until after the summer, however the weakness in the economy will prompt a faster response by Washington, or there will be consequences how global investors will gauge holding current asset positions in US$ denominated securities.



Just take a look at the correlation between the CESI and the 13-week change in the 10-Year US Treasury bond yield. The actual yield has dropped from a recent peak of - 2.62% on March 13 to 2.17% yesterday, which is close to our 2,10 initial Q2 target, before we are expecting a short correction back towards 2.35% to 2.40$. At that point we see the yield to gather momentum for another run down towards our Q2 low target for the 10-Year treasury yield of 1,70% by the end of Q2.

As per our Q2 Global Outlook and Investment Strategy, we have been advising our clients to reduce exposure to the US$ ($USD) and US equities ($SPX), and instead increase allocations into US long bonds, namely 10-Year Treasuries ($TNX), and into EU and EM currencies and equities, which form a tactical Asset allocation call has been spot on so far in the current quarter.

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2017 Q2 Tactical Asset Allocation

Assets classes		Recommendation as of March 28th, 2017							Change since December 16th, 2016
		+++	++	+	0	-	--	---	
Equity Markets	USA							X	Reduce weighting
	Europe						XX		Reduce weighting
	Japan					X			Reduce weighting
	Asia/Pacific					X			Reduce weighting
	Emerging Markets			X					Reduce weighting
Bond Markets	Developed Markets		XX	X					Increase weighting
	Emerging Markets		XX						Increase weighting
	Inflation Linked			X					Increase weighting
	Investment Grade			X					Unchanged
	High Yield				X				Unchanged
	Convertibles				X				Unchanged
Private Equity & Real Assets	Listed Private Equity				X				Unchanged
	Commodities	XXX							Unchanged
Cash				X					Increase weighting
Forex	USD							XXX	Reduce weighting
	EUR		X						Unchanged
	Yen						X		Unchanged
	EM & Others	XXX							Unchanged

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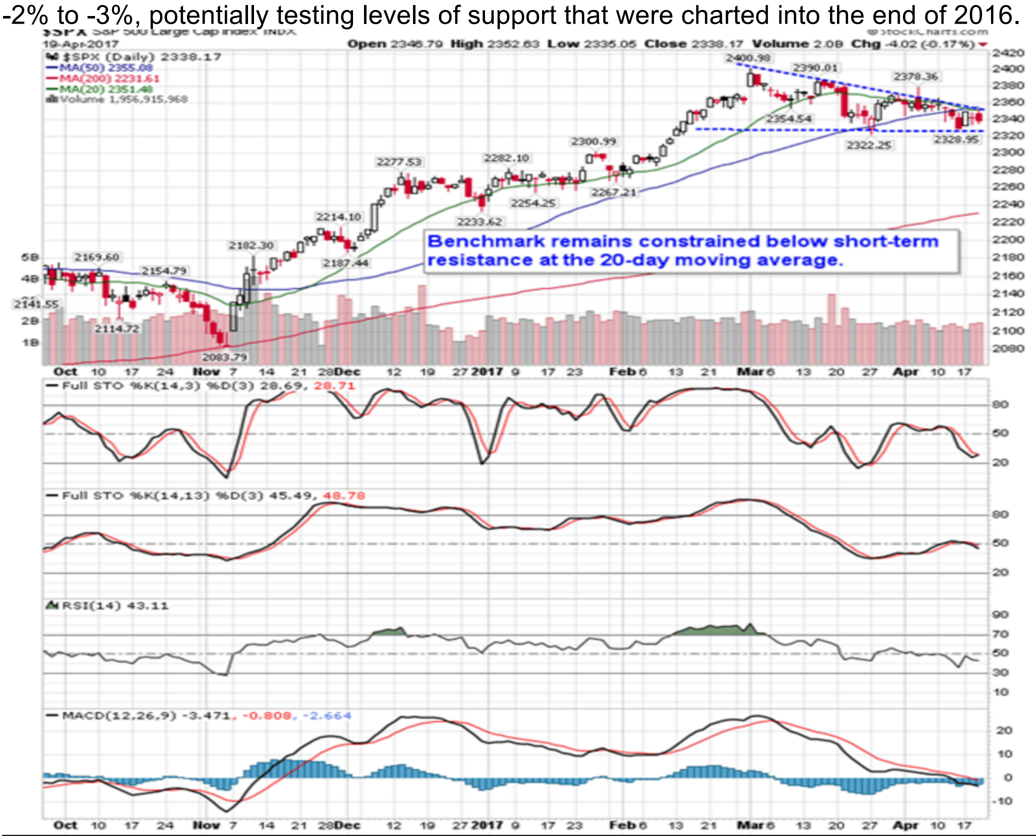
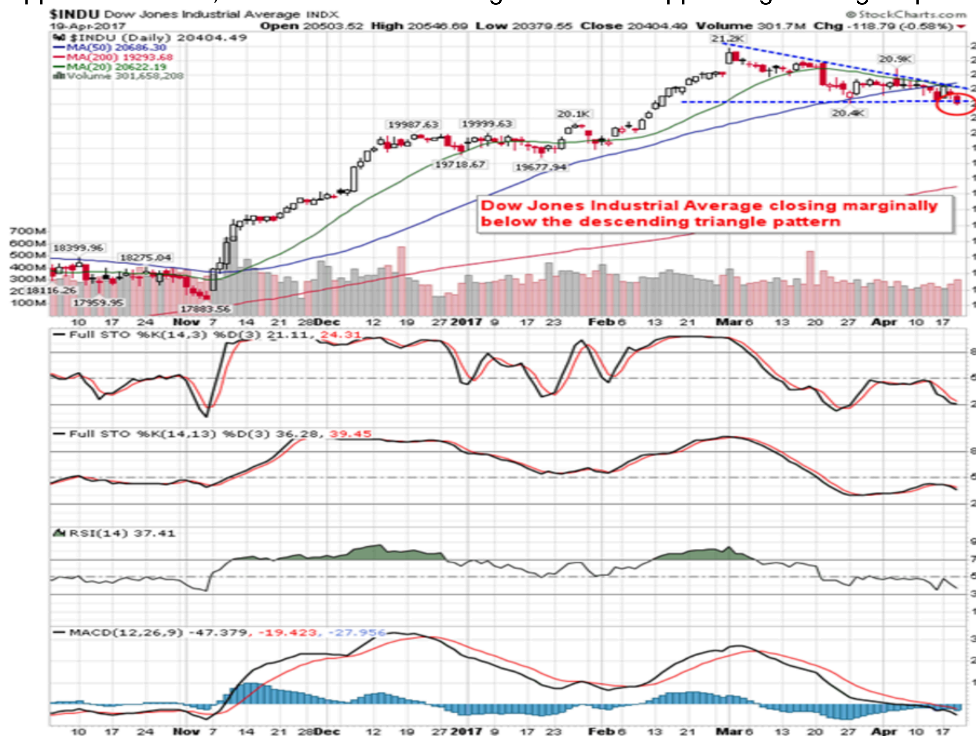
Based on this macro slowing in the US for at least another 6 – 12 months, we believe that currently with the weakening macro evidence investors will have to reconsider their current hope filled allocations towards US$ and US equities, and which will turn the recent "Trump Bump" turning into a coming "Trump Dump".

The "Trump-Dump" take II

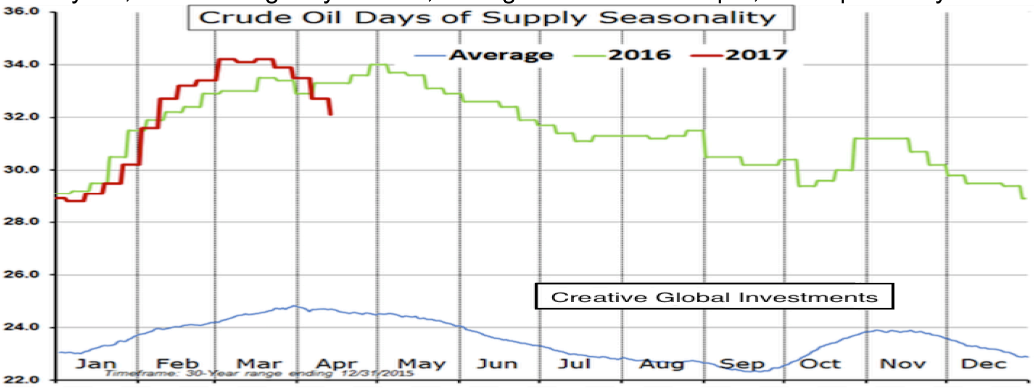
Stocks closed lower on Wednesday as energy stocks weakened amidst a decline in the price of oil. The S&P 500 Index shed around two-tenths of one percent, continuing to struggle beneath a declining 20-day moving average. Short-term support remains at 2322. Calculated downside move upon a break below the descending triangle consolidation patterns on the charts of the two widely followed market gauges is around -2% to -3%, potentially testing levels of support that were charted into the end of 2016.



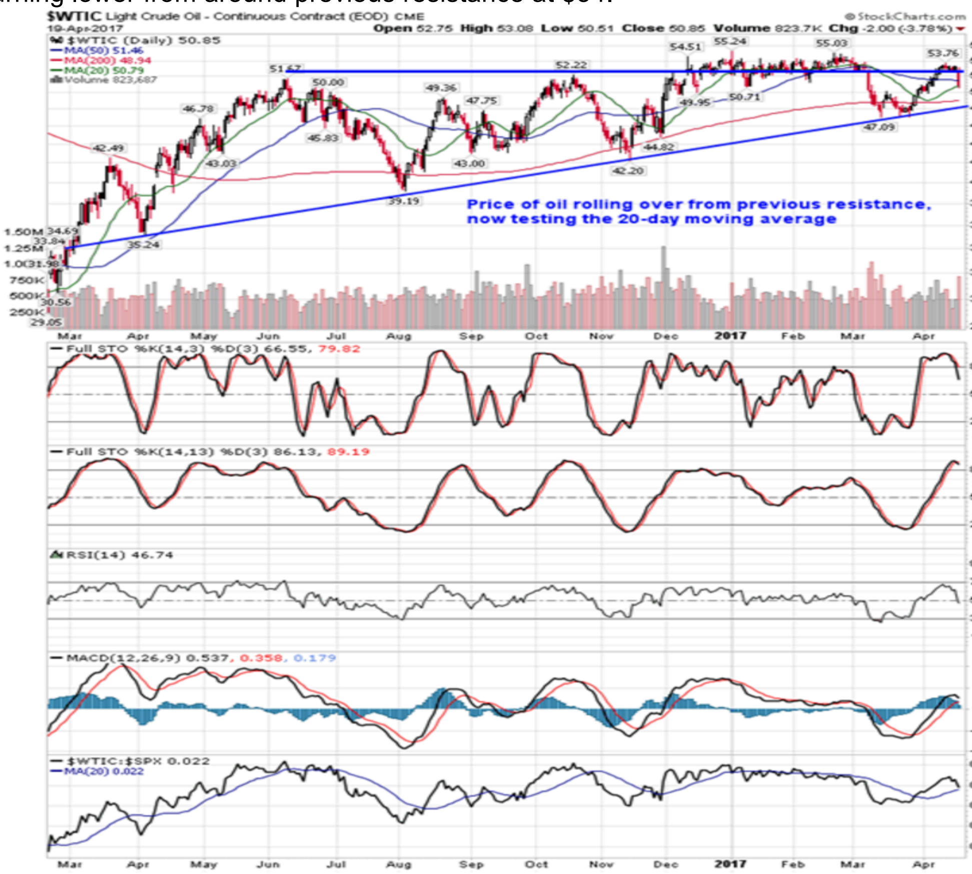
The Dow Jones Industrial Average closed below its short-term horizontal level of support around 20,400 as IBM shares weighed after disappointing earnings report.



In the Energy Sector, The EIA indicated that stockpiles of oil declined by 1.0 MN barrels last week, while gasoline inventories increased by 1.5 MN barrels. The result saw the days of supply of oil fall to 32.1, continuing to roll over from the all-time high at 34.2 charted last month. Looking at the seasonal change of US ending stocks of oil, the recent declines has the appearance of an earlier than average peak to the inventory levels of the commodity, which typically hits a high for the year at the beginning of May. The concern in the report remains with the climb in domestic production, up by 5.5% y-t-d, the 2nd largest y-t-d rise, through the middle of April, in the past 30 years.



The market sent the price of oil lower by almost -4% following the report's release, turning lower from around previous resistance at $54.



Strategy Review

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CGI 2017/2018 Currency Forecasts

Currency	Spot Price March 28th, 2017	Q2 2017 CGI Forecast	2017 CGI Forecast	2017 Consensus Forecast	2018 CGI Forecast	2018 Consensus Forecast	2019 CGI Forecast	Chart Technical Momentum	Long-term trend
USD Index	100.55	.93	.92	102	.88	.98	.90	neutral	sideways
EUR/US$	1.0658	1.16	1.18	1.04	1.20	1.10	1.30	positive	upward
US$/YEN	111.385	115	115	110	118	110	125	positive	upward
EUR/YEN	118.722	124	125	116	120	120	130	positive	upward
EUR/GBP	.8487	.95	1.00	.90	1.00	.85	1.10	positive	upward
GBP/US$	1.255	1.15	1.05	1.22	1.00	1.20	1.05	negative	downward
EUR/NOK	9.16	9.00	8.85	9.5	8.5	9.00	8.5	positive	upward
US$/BRL	3.122	2.8	2.65	3.10	2.65	3.15	2.70	negative	downward
US$/CHF	1.0029	.95	.90	.90	.90	0.85	0.85	neutral	downward

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2017/2018 Commodity Prices Forecasts

Commodity	Price March 28th, 2017	2017 Q2 CGI Forecast	2017 CGI Forecast	2017 Consensus Forecast	2018 CGI Forecast	2018 Consensus Forecast	Chart Technical Momentum	Long-term trend
WTI Oil	50.85	58	62	60	65	48	Positive	upward
Brent Oil	53.53	60	64	58	64	52	Positive	upward
Nat Gas	3.19	3.30	3.85	4.0	4.0	3.00	Positive	upward
Gold (US$/oz.)	1,251,20	1,350	1,450	1,350	1.500	1.300	Positive	upward
Copper (US$/oz.)	265.25	280.0	300.00	290	315	250.0	Positive	upward
Silver	18.25	21.00	22.00	22.00	24.00	20.00	Positive	upward
Platinum	930.35	1,050	1,100	1,100	1,250	1,150	Positive	upward
Wheat	426.50	430	430	430	470	430	Neutral	downward
Coffee	139.30	143	145	160	175	165	Positive	upward
Sugar #11	16.76	20.00	20	22	24	20	Positive	upward
CRB Reuters/ Jefferies	187.34	215.00	195	210	235	210	Positive	upward

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CGI 2017 Q2/2018 Global Equities Indices Targets

Index	Price March 28th,2017	Earnings Momentum	Chart Technical Momentum	CGI Q2 2017 Price Target	CGI 2017 High Price Target	CGI 2018 Price Target	CGI 2017 Rating
Global Dow	2,692	+	+	2,650	2,850	2,750	Positive
S&P 500	2.362	0	0	2,150	2,350	2,300	Neutral
Russell 2000	1,385	+	0	1,225	1,425	1,300	Positive
NASDAQ 100	5,911	+	0	5.100	5,600	5,700	Positive
NIKKEI 225	18,909	+	0	17,200	19,800	21,200	Positive
FTSE	7,322	+	0	6,600	7,100	6,800	Neutral
DAX 30	12,312	+	+	10,900	11,800	13,500	Positive
CAC 40	5,122	+	+	4,600	5,400	5,800	Positive
SMI	8,536	0	0	8,000	8,300	8,000	Neutral
IBEX 35	10,462	+	0	9,200	10,000	12,000	Neutral
RTS	1,113	+	+	1,000	1,350	1,550	Positive
BOVESPA	64,984	+	+	60,000	72,000	68,000	Positive
Mexican Bolsa	48,541	0	0	43,500	48,000	53,000	Neutral
Hang Seng	24,111	+	0	23,500	25,500	27,200	Positive
Sensex	29,620	+	+	28,000	31,700	32,700	Positive
Shanghai	3,222	+	+	3,000	4,100	5,200	Positive
TSX	15,547	+	+	14,200	16,850	16,800	Positive

- = Negative
0 = Neutral
+ = Positive

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2017 Q2 Global Equities Outlook per Country

Country	Valuations	Earnings Momentum	Balance Sheets	Chart Technical Momentum	Equities/Bonds DDM	Country risks (political, fiscal, regulatory, other)	CGI 2017 Q2 Outlook
US	-	+	0	0	0	Negative	Neutral
Canada	0	+	+	0	+	Neutral	Positive
Mexico	0	+	0	0	0	Negative	Neutral
Brazil	+	+	0	+	+	Neutral	Positive
India	0	+	+	0	+	Neutral	Positive
China	+	+	0	+	+	Positive	Positive
Japan	0	+	0	+	+	Neutral	Neutral
Russia	+	0	0	+	+	Neutral	Positive
Germany	+	+	+	+	+	Neutral	Positive
France	+	+	+	+	+	Neutral	Positive
UK	0	+	0	0	+	Negative	Neutral
Belgium	0	+	+	0	+	Neutral	Positive
Norway	0	+	+	+	0	Positive	Positive
Turkey	0	0	0	0	0	Negative	Neutral
Spain	+	+	+	0	+	Neutral	Positive
Netherlands	+	0	+	0	+	Neutral	Positive
Switzerland	0	-	+	0	0	Neutral	Neutral
S-Africa	0	0	0	-	-	Neutral	Neutral

- = Negative
0 = Neutral
+ = Positive

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2017 Q2 Global Equities Sector Outlook

Industry Sector	Valuation	Earnings Momentum	Balance Sheet	Chart Technical Momentum	Sector risks (political., fiscal, regulatory, other)	CGI Q2 Outlook
Automotive	+	0	+	-	Neutral	Negative
Aerospace. & Def.	+	+	+	0	Neutral	Neutral
Banks	0	0	-	-	Neutral	Negative
Basic Resources	0	+	0	+	Positive	Positive
Chemicals	0	+	+	0	Positive	Positive
Construction	0	+	0	0	Positive	Positive
Financial Services	0	0	0	-	Neutral	Negative
Food & Beverages	0	0	0	0	Neutral	Neutral
Healthcare	0	0	0	-	Neutral	Neutral
Industrials	0	+	+	0	Positive	Neutral
Insurance	0	0	0	+	Neutral	Positive
Media	-	0	0	-	Neutral	Negative
Oil & Gas	0	+	+	0	Neutral	Positive
Personal Goods	0	0	0	0	Neutral	Neutral
Retail	0	0	0	0	Neutral	Neutral
Technology	0	+	0	-	Neutral	Negative
Telecoms	0	-	0	-	Negative	Neutral
Travel & Leisure	0	-	0	0	Negative	Neutral
Utilities	0	+	0	0	Neutral	Positive

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