Creative Global Investments

Morning market commentary & charts

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Objectivity

Integrity

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Message to the FED!

"Show us the inflation"
and
"then" you can raise rates

US inflation continues to run below the Fed's 2% target, which policymakers view as a "temporary result of the strong US$ pressuring commodity prices". Let's look at the short-term 2 Year chart for the commodities index, the $CRB, and we can see that although the index is tremendously oversold, nevertheless, all short term indicators are negative, from RSI, to MACD to 14-day, 50-day and 200-day, and that the risks for the $CRB to break support are great.

Again, take a look at a chart which we published yesterday, and look at inflation expectations, as gauged by the 5-year breakeven inflation rate, which are showing signs of rolling over following the substantial rebound from the January low.

Then, let's look at the 20-Year chart for the $CRB, which does not look any more encouraging, and one can see risks for the $CRB to drop to below 100

However, when looking at the US$ chart below, maybe the FED should rethink their definition of "temporary" for the US$ strength, and the inherent tremendously negative impacts on the US economy, the negative impacts on competitiveness of US companies, and negative impact on imports, exports, negative impacts on US inflation, or better, the lack thereof.

We just cannot see the rational for the FED to raise interest rates, when macro economic momentum, and the negative impacts of a strong US$ are already at unsustainable levels, nevertheless with risks of a rate hike going to exacerbate and make things much worse.

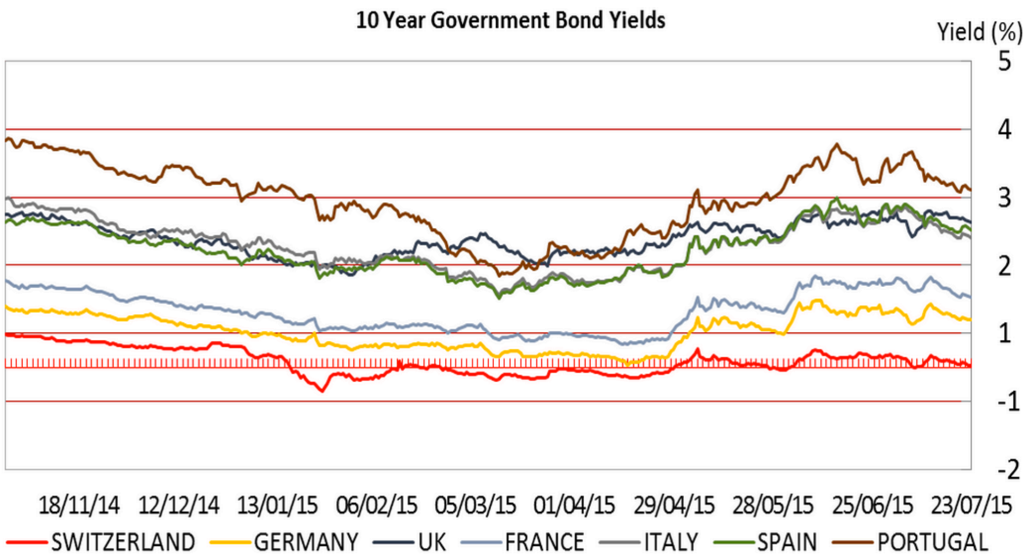
Is the past weeks reversal action in the US$ telling us that there are more investors joining our FED policy camp and believe that a rate rise might be way premature?

US Government Bonds

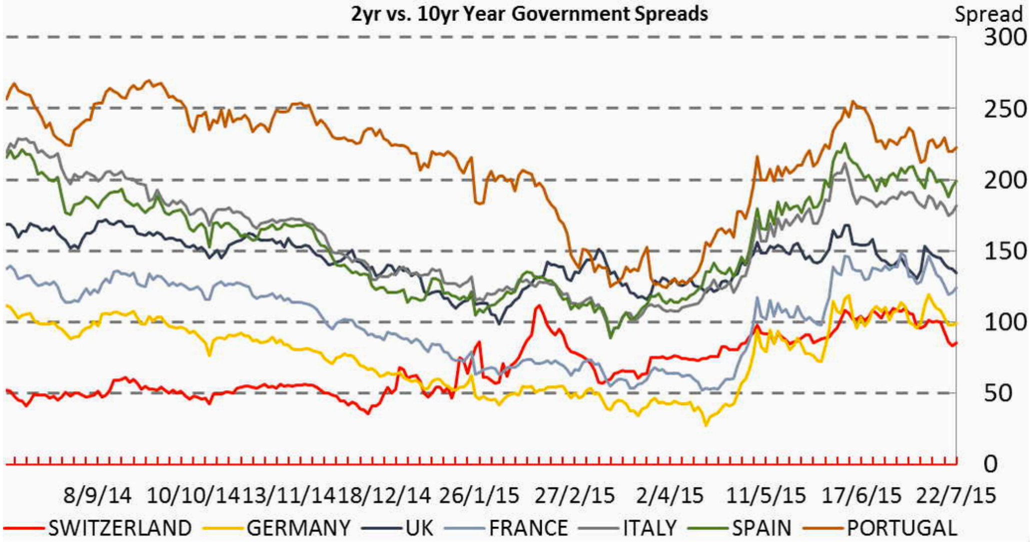
Treasury prices, as gauged by a couple of actively traded treasury bond funds, have moved firmly higher over the past many days, rebounding from a bottoming pattern charted over the past month. Bonds seasonally outperform stocks through to October, benefitting from the risk aversion that is present over the summer months. August has seen gains in the 30-year US treasury bond price 75% of the time over the past 20 years, averaging a gain of 2.0%. The tailwind is present; whether or not the seasonal trend is impacted by the FOMC's desire to raise rates will remain up for debate.

European Government Bonds

Again, for the past month we have been advising for investors to take bigger positions in European 10-Year government bonds, and so far, yields as anticipated have come down substantially, but are not yet at our expected lower levels. We still see the likelihood of -30bps to -60bps yield compression between the Italian, Spanish, Portuguese and Irish 1- Year government bond yields relative to the German Bunds between now and the end of the summer.

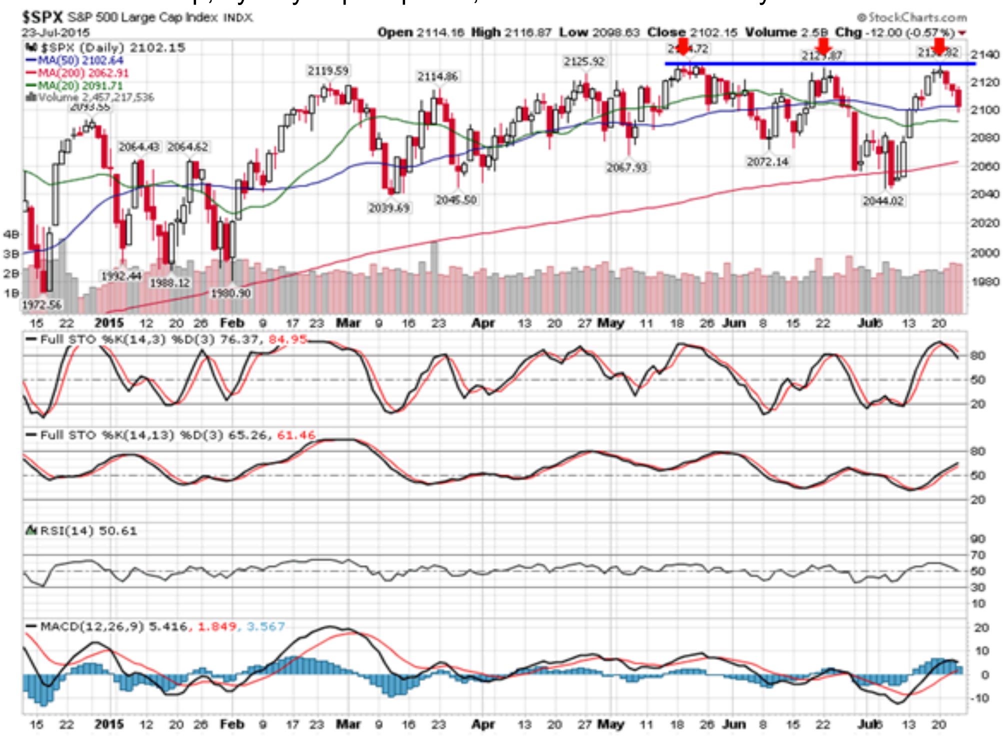


We are expecting for a similar compression for the 2-Year vs. 10-Year Government Spreads until the end of the summer, particularly as the ECB will have to step up in the buy-back programs this summer, and, because there are increasing signs of macro momentum globally, but also for Europe to slow temporarily over the summer, and that bonds are attractively priced relative to equities and commodities at current prices.

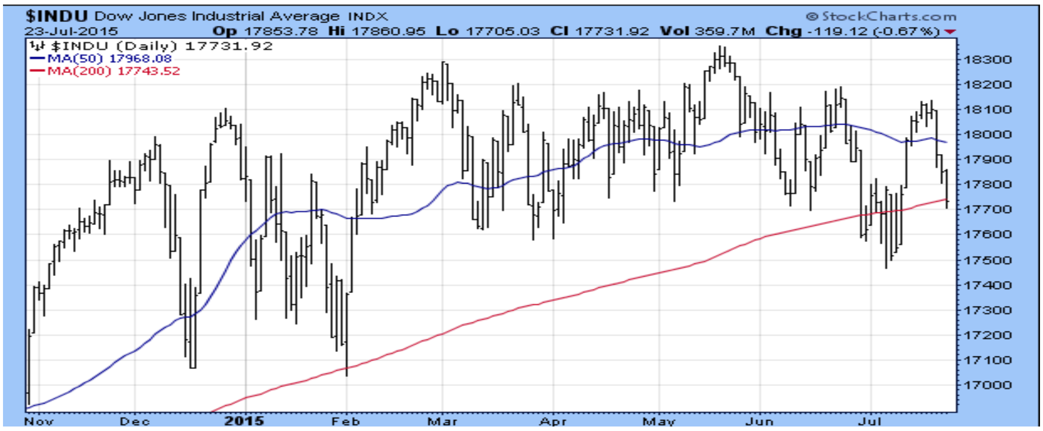


US equities

The S&P 500 Index, it is becoming increasingly apparent that a triple-top is being charted around the all-time peak for the benchmark. First level of downside support is implied around 2075, followed by the July low around 2050. Below this, investors may want to prepare themselves for a move below the 200-day moving average. Recent rebounds from around this long-term moving average since 2012 have resulted in significant gains in the range of 8% to 12%; July's rebound has recorded a gain of only 3.7% from trough to peak, assuming triple-top resistance around 2130 is not surpassed over the near-term. The top would coincide with the VIX hitting support, yet again, at 12, a level that has suggested investor complacency over recent years, eventually resulting in declines in stocks. The lesson provided by this indicator is that when portfolio protection is cheap, by way of put options, don't be reluctant to buy some insurance.

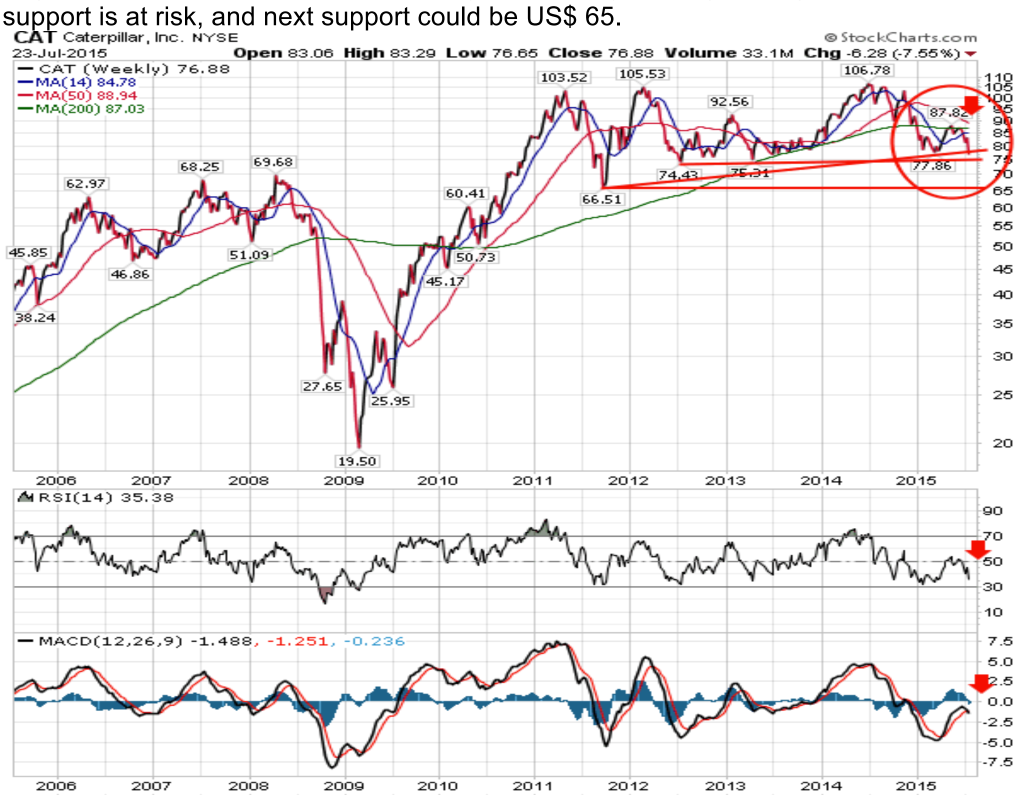


The Dow Industrials is also threatening to slip below their 200-day line. The two biggest percentage losers in the Dow are Caterpillar and 3M. The Dow challenged the long-term support line earlier in the month already, and looks to us like testing it again. A weekly close below that 200-day support line would be a clear negative. Seasonal factors are also starting to work against the market. After a weak Q2, the market often experiences a summer bounce during the first half of July, as we have been showing on our work the past weeks, only then enters the more dangerous months of August and September, which might set the stage for an autumn bottom likely from -10% lower levels.



Q2 earnings disappointments for US companies due to a strong US$ are on the rise, just as we predicted, and what the market does not factor in at all yet, is the weighted currency negative impact for the current quarter and the next will be worse.

Let's look at Caterpillar, which besides Boeing serves as a great proxy to look at the competitiveness of US multi-nationals in the global context. Shares in Caterpillar fell after it reported a drop in profits and revenue during the second quarter. It said earnings per share declined to US$ 1.16 from US$ 1.57 in 2014. Excluding restructuring costs, earnings were US$ 1.27, down from US$ 1.69 last year. Investors were also disappointed that the company lowered its sales outlook for the year. Looking at a 10 year chart shows the CAT is in serious trouble. All short-term technical indicators are negative. CAT has broken below 14 day and 50-day moving averages, and the US$ 75 support is at risk, and next support could be US$ 65.



Now, let's look at Boeing versus Airbus, the two most directly opposed global competitors, one located in the US, the other one in Europe, not that the manufacturing footprint is much different between both companies, however, the earnings translation for Boeing into US$'s versus the earnings translation for Airbus into Euro's has the attention of investors since last June, when the Euro peaked against the US$ as the following chart clearly shows.

So, as the chart shows, Airbus has as of late June last year outperformed Boeing substantially, due to the currency translational positive effects. However, going forward, Airbus can now price future aircraft and service sales much more advantageous than Boeing, as Airbus has been an astute practitioner of currency hedging.

Yesterday transportation stocks also plunged in the US as investors reacted to disappointing profits from rail company Union Pacific. The Dow Jones Transportation Average is now lower by over -11% year-to-date, having struggled around its 50-day moving average since April. The 200-day moving average of the transportation benchmark is showing signs of rolling over, providing negative implications for the longer-term.

Seasonally, between mid-July and early October is the peak period of weakness for the industry, typically coming under pressure as a result of high energy prices in the summer months. Perhaps contrary to the conventional thinking, depressed energy prices are clearly challenging the industry as well. Low energy prices have made natural gas more competitive with the environmentally unfriendly coal, which saw volumes at Union Pacific drop by 26% in Q2. According to the US Department of Energy, natural Gas recently overtook coal as the top source for US electricity production, a trend that is set to become the new norm. Transportation stocks seasonally hit a low in Q4, providing appealing buying opportunities for a trade through to the end of November.

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