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Technical Scoop E-Commentary August 26 2019
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Tweet tumble, retaliation tumble, fourth fall, best gold, spread narrows, financials deteriorate

Shortened commentary this week.

When Trump tweets markets tumble. When China retaliates with more tariffs markets tumble. When Trump stomps his feet and retaliates as well the markets just keep on tumbling. Friday was a rather dramatic day starting with Fed Chair Jerome Powell speaking at Jackson Hole, Wyoming. By the time the dust cleared the stock markets had fallen for the fourth consecutive week and gold put in its best day of the year. It made for a very dramatic day. And it may be only the beginning as the stock markets appear poised to fall further and gold to soar higher. Bond yields also fell further and the 2-10 spread closed the week up only 1 bp as it threatens to join all the other spreads in negative territory.

We highlight this week in our Chart of the Week (page 8) the deteriorating S&P 500 Financials/S&P 500 ratio. Without the participation of the financial sector the markets should be hard pressed to rally. The Canadian Dividend Strategy is designed to allocate to cash in the event of a sustained decline.

Things may be coming apart but in a world of negative interest rates, deteriorating global politics, shaky finances and slowing economies, gold remains a safe haven.

Have a great week!

DC

"Some calamities—the 1929 stock market crash, Pearl Harbor, 9/11—have come like summer lightning, as bolts from the blue. The looming crisis of America's Ponzi entitlement structure is different. Driven by the demographics of an aging population, its causes, timing and scope are known."
—George Will, American conservative political commentator, columnist, *The Washington Post*; b. 1941

"The Mexican debt crisis, Latin American debt crisis, the crises of the 1990s, the Wall Street stock market crash, and other events should have reminded us, and did remind us, that financial instability remains a concern, remains a problem."
—Ben Bernanke, American economist Brookings Institute, Chair Federal Reserve 2006–2014; b. 1953

"I've learned that things change. The whole boy band thing almost turned into a stock market crash."
—Max Martin, Swedish record producer, songwriter, singer, b. 1971

"Doing great with China and other Trade Deals. The only problem we have is Jay Powell and the Fed. He's like a golfer who can't putt, has no touch. Big U.S. growth if he does the right thing, BIG CUT—but don't count on him! So far, he has called it wrong, and only let us down…"
—Donald Trump, tweet on August 21, 2019, 8:52 am

"…We are competing with many countries that have a far lower interest rate, and we should be lower than them. Yesterday, 'highest Dollar in U.S. History.' No inflation. Wake up Federal Reserve. Such growth potential, almost like never before!"
—Donald Trump, tweet on August 21, 2019, 8:52 am

We wish we could tweet like Donald Trump, 45th president of the United States. He's incessant. He tweets so much that we wonder what else he actually does. Oh yes, he plays golf. But he goes on.

"So, Germany is paying Zero interest and is actually being paid to borrow money, while the U.S., a far stronger and more important credit, is paying interest and just stopped (I hope!) Quantitative Tightening. Strongest Dollar in History, very tough on exports. No Inflation!"
—Donald Trump, tweet on August 21, 2019, 9:56 am

"…WHERE IS THE FEDERAL RESERVE?"
- Donald Trump, tweet on August 21, 2019, 9:56 am

Jerome Powell, Chairman of the Federal Reserve, appointed by Trump, is Trump's favourite whipping boy. He is also amongst the few that Trump cannot fire. Okay, maybe he can, but it would be extremely difficult. Trump wouldn't stop him, however, if he resigned. With that kind of abuse, who would blame him?

Jerome Powell spoke on Friday at Jackson Hole, Wyoming. It's an annual economic policy gig. Trump needs to attack Powell to fend off accusations that the U.S. is headed for a recession. Recession calls are coming because of a slowdown in Europe and China, some of it (much of it?) triggered by Trump's trade wars. So, there were no big expectations that Powell would say anything that might be outside the box of normal Fed

speak. Nor were there any expectations that Powell would highlight something that others have not already cited.

Powell did not disappoint. The economy is in a favourable place but faces "significant risks" as the global economy slows and there is continued trade uncertainty. Almost as if on cue, China slapped more tariffs on $75 billion of U.S. goods, including soybeans, autos, and oil. The timetable on this new round of tariffs fits with the U.S.'s September 1 and December 15 dates. The tariffs hit areas of Trump support in farms and factories. Placing tariffs on oil was probably a surprise for many as few knew the U.S. exports oil and petroleum products to China. But it does—apparently around 145,000 barrels per day.

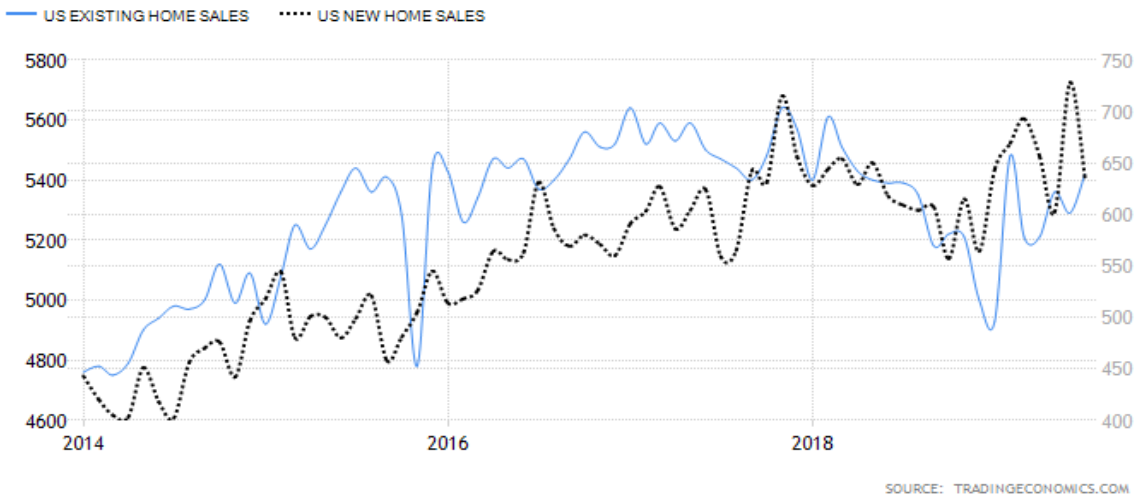
Trump couldn't wait. Like a three-year-old child, Trump immediately retaliated with an additional 5% tariff on $550 billion of Chinese goods. You kicked sand in my face, so I'll kick sand in yours. The stock markets gagged.

The only hints Powell gave of the potential future rate cuts were that the Fed would act appropriately to sustain the expansion. As we said—normal Fed speak. As usual, he cited the low unemployment (U3) and inflation near targets of 2%.

Naturally, he wouldn't want to highlight slowing consumer sentiment and industrial production slipping into contraction territory. The purchasing managers index has fallen to its lowest level since September 2009. Bankruptcies have been rising, department store sales have been lagging, and home sales are generally lagging. Large department stores are even closing stores. Already 4,810 store closures have been announced in 2019. Some of the larger closings have been Gap Inc., Victoria's Secrets, Abercrombie & Fitch, Tesla, Payless Shoe Source, Gymboree, Family Dollar, Chico's, Walgreens, and, J.C. Penney. If things are so good, then why are companies closing stores? Okay, they do that every year. But during this year, store closings have been on the rise.

We should also note that Trump's tariffs have slowed export growth in China, but it hasn't brought it to a halt. About 19% of Chinese exports go to the U.S. China's growth is being slowed not so much by the trade wars but internal problems in real estate and their banking system. All those empty "ghost cities" are coming back to haunt them. They along with many other infrastructure white-elephants are causing problems with loans and that in turn feeds into the Chinese banking system. Like Ponzi-schemes before "wealth management products" are in danger of blowing up. That in turn puts pressure on the Chinese monetary authorities. But China has massive reserves and should be able to withstand it all but not without overall slower growth. In the interim, however, China should soon see capital controls, asset freezes and political repression (already being seen in the detention of the Uighurs and in Hong Kong).

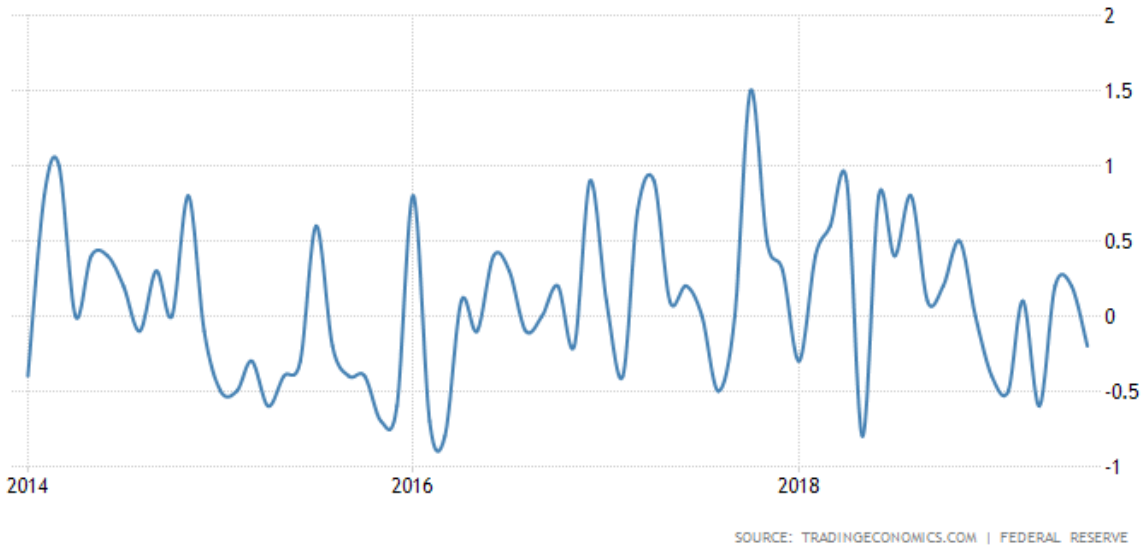
U.S. Existing and New Home Sales



Source: www.tradingeconomics.com

Powell wouldn't want to talk too much about how 74% of business executives surveyed by the National Association for Business Economics believe a recession is coming, although their time frame is by the end of 2021. That's two years from now. One supposes that, yes, they could be right given a wide time frame. The New York Fed has even gotten into the recession prediction game by suggesting one should occur over the next twelve months and the risk is the highest since the "Great Recession" of 2007–2009.

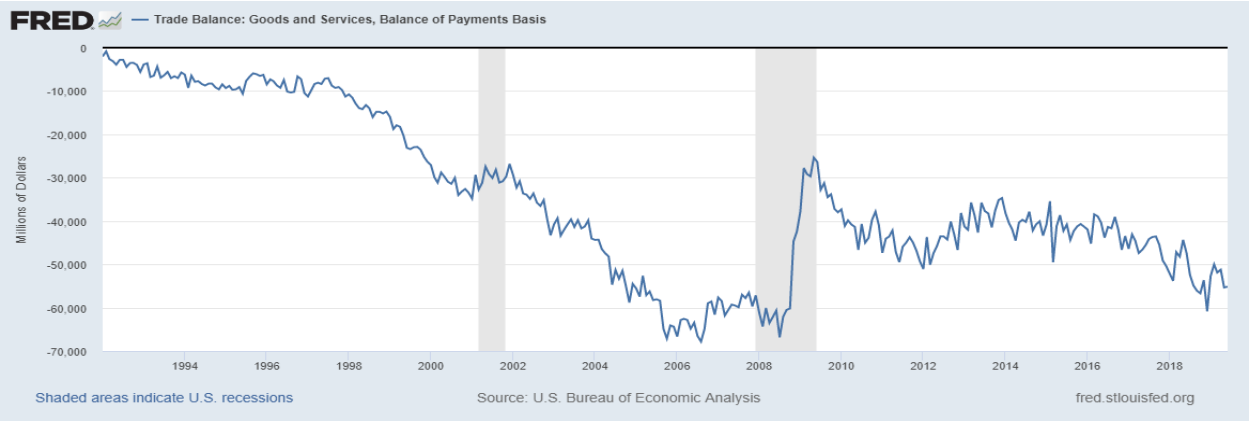
U.S. Industrial Production Month Over Month



Source: www.tradingeconomics.com, www.stlouisfed.org

Much has been made about how the yield curve is inverting. Most recently the 2-year–10-year spread went negative for the first time in 12 years. But a reminder that the average lag between an inverted yield curve and a recession is 14 months with a range of 7–20 months. The most recent 2–10 spread is still positive, but barely—by 1 bp. The other much noted spread of the 10-year U.S. treasury note vs. 3-month treasury bills has widened to negative 45 bp.

U.S. Trade Balance



Source: www.stlouisfed.org

Despite Trump's tariffs, the U.S. trade balance is not falling. It has actually been rising—$55.1 billion in the last report of June 2019. Note that the U.S. trade balance kept widening during the tenures of Bill Clinton and George W. Bush but improved under Barack Obama. Since the election of Trump, the trade balance has once again been deteriorating. And the U.S. budget deficit has also been widening with expectations of $1 trillion deficits once again. History shows that budget deficits rise under Republican presidents and fall under Democrat presidents. Trump has kept the record intact.

Trump, of course, believes the Fed should cut interest rates by 100 bp right away and restart quantitative easing (QE). One could suppose that actually might spark a huge stock market rally. But lowering interest rates and QE might not have the impact everyone expects. See Japan and the EU both of whom seem to be in an endless cycle of low to negative interest rates and QE, yet their economies remain lethargic at best. But QE and ultra-low interest rates result in bubbles—in stock markets, bond markets (especially the corporate bond market), housing, and more. And a reminder that bubbles eventually burst.

Speaking of negative interest rates, with some $15 trillion of negative interest bonds outstanding mostly in the EU and Japan it should be noted that this is not normal. There are even corporate bonds trading at negative rates. Corporations are, on the whole, over-leveraged and are now trying to de-leverage. That alone could spark a recession. But slashing interest rates and bringing back QE would have to be considered drastic and it would imply a whiff of panic. The White House is trying to get into the game suggesting cuts to payroll taxes and other measures.

Volatility has returned to the markets. The markets didn't care for Powell's comments at Jackson Hole but he really said nothing earth-shattering. China's retaliatory tariffs hit a nerve with Trump and he "ordered (sic)" U.S. companies to find an "alternative" to China. Trump also suggested that Powell is the enemy (what, an

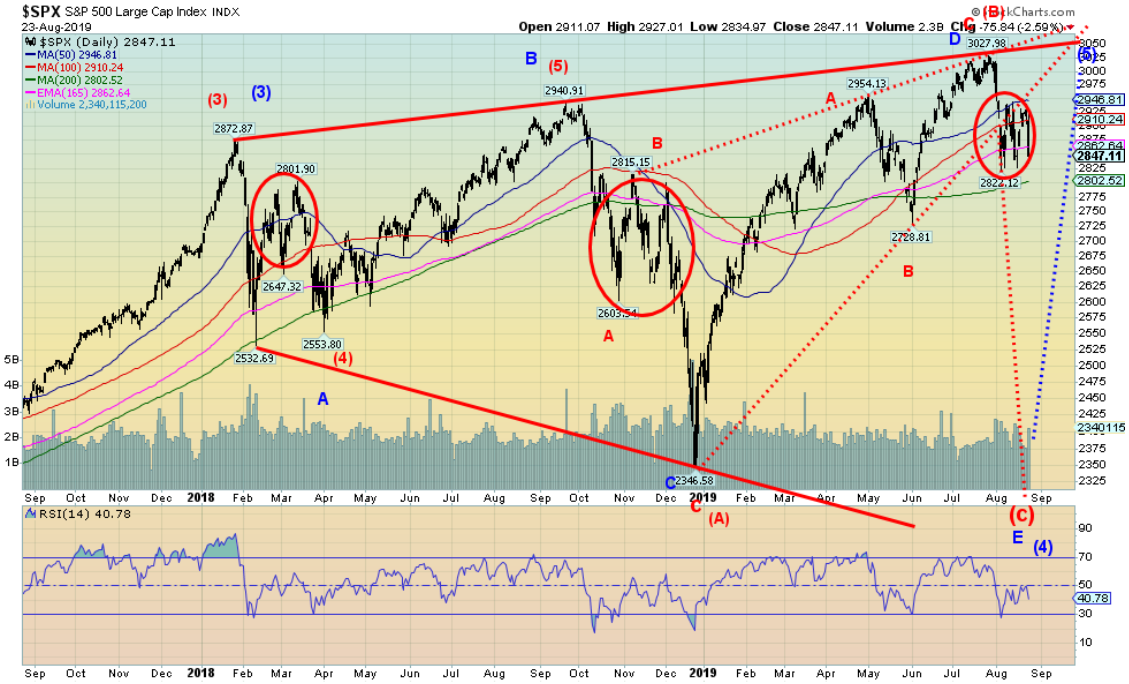
enemy of the state?). As if companies will jump to Trump's command and Powell constantly ignores his temper tantrums (he has to). Corporations thought they could control Hitler's excesses. That didn't work out too well. U.S. corporations may try to do the same with Trump. But will it work?

Markets reacted to all of that as the Dow Jones Industrials (DJI) plunged over 600 points and gold soared over $25. It takes Trump to really send the stock markets into a hole (no, not Jackson Hole) and gold into a frenzy.

Stock markets now appear poised to start the next leg down. This is the fourth consecutive weekly decline. Oh, another save could come in but, as we have noted over the past several weeks, the S&P 500 appears to have formed a large broadening pattern. It stopped right at the top of the channel in late July. Following the first plunge to the downside a consolidation pattern appears to be forming. The 50-day MA appears to be acting as resistance with the 200-day MA acting as support. A breakdown now under 2,800 for the S&P 500 could send the index down to at least 2,700. Ultimate targets could be the bottom of the broadening pattern near 2,200. That's another 23% plunge from current levels. The Dow Jones Transportations (DJT) and the Russell 2000 intermediate trends have turned down. Bulls should beware.

"…better off without them. The vast amounts of money made and stolen by China from the United States, year after year, for decades, will and must STOP. Our great American companies are hereby ordered to immediately start looking for an alternative to China, including bringing…"

—Donald Trump, tweet on August 23, 2019, 10:59 am



Source: www.stockcharts.com

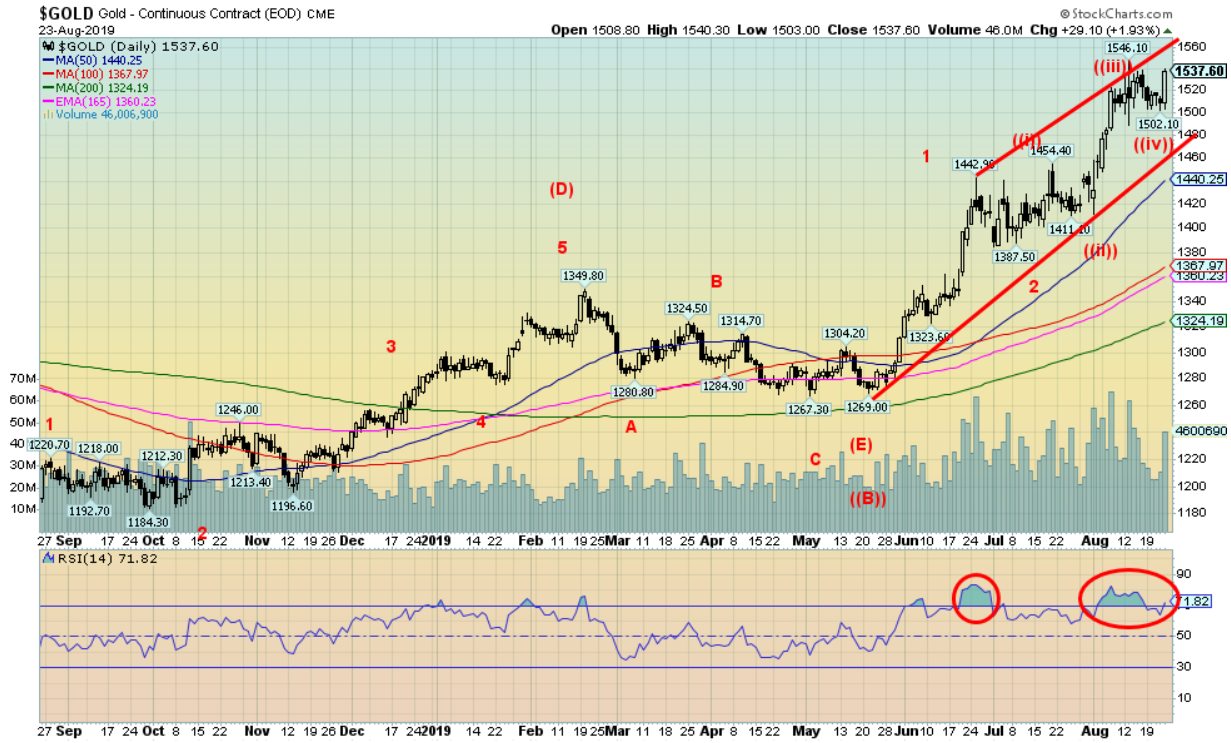
Gold soared. Targets of up to $1,590 appear to be in the crosshairs. But sentiment is the most bullish we've ever seen (95%) and the commercials are holding a record short position. (Commercials are net short 336,250

contracts as per the latest COT.) So, it is a cautioning note that taking profits into a further rally may be wise. However, gold now appears to be headed to its next target up around $1,590. Gold stocks are rallying as well, as both the TSX Gold Index (TGD) and the Gold Bugs Index (HUI) gained roughly 5% this past week and put in new 52-week high closings. Both indices are now up roughly 40% in 2019.

Given the trade wars and Trump's ramblings and threats, the U.S. dollar finally caved on Friday and the US$ Index dropped 0.5%. While all major currencies rebounded against the U.S. dollar on Friday the main beneficiaries on the week were the Japanese yen, the Swiss franc, and, surprisingly, the pound sterling. The US$ Index may now be poised to break down although 96 remains key support. Under that level the $ bear may get underway. If the US$ Index does break down, the odds of gold falling—despite the overbought, high bullish sentiment and record commercial shorts—are low.

One of the highlights we are seeing in the markets is the weakness of the financial sector. No strong bull market can develop without the participation of the financial sector. The S&P 500 Financials/S&P 500 ratio peaked in February 2018 with the market. It has been downhill ever since. The peak in February 2018 never remotely approached the peak seen in 2007 before the 2008 financial crisis. This bodes poorly for the stock markets given the importance of the financial sector. Cutting interest rates won`t help either as that would most likely slash their interest rate margins and negatively impact their trading operations. We feature the Financials S&P 500 ratio chart below as our chart of the week.

Gold



Source: www.stockcharts.com

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US$ Index

Source: www.stockcharts.com

Chart of the Week

S&P 500 Financials/S&P 500 Ratio

Source: www.stockcharts.com

A reminder that in a world splitting at the seams both politically and financially, gold remains a safe haven.

Note: Markets and Trends Chart is below.

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MARKETS AND TRENDS

	Close Dec 31/18	Close Aug 23/19	% Gains (Losses) Week	YTD	Trends Daily (Short Term)	Weekly (Intermediate)	Monthly (Long Term)
Stock Market Indices							
S&P 500	2,506.85	2,847.11	(1.4)%	13.6%	down	up (weak)	up (topping)
Dow Jones Industrials	23,327.46	25,628.90	(1.0)%	9.9%	down	neutral	up (topping)
Dow Jones Transports	9,170.40	9,739.74	(2.3)%	6.2%	down	down	up (weak, topping)
NASDAQ	6,635.28	7,751.77	(1.8)%	16.8%	down	up (weak)	up (topping)
S&P/TSX Composite	14,322.86	16,037.58	(0.7)%	12.0%	down	up (weak)	up (topping)
S&P/TSX Venture (CDNX)	557.20	581.95	2.0%	4.4%	down	down	down
Russell 2000	1,348.56	1,459.49	(2.3)%	8.2%	down	down	up (weak, topping)
MSCI World Index	1,710.88	1,828.93	0.7%	6.9%	down	neutral	neutral
NYSE Bitcoin Index	3,769.99	10,400.70	.01%	175.9%	down (weak)	up	up
Gold Mining Stock Indices							
Gold Bugs Index (HUI)	160.58	**226.21**	5.9%	40.9%	up	up	up
TSX Gold Index (TGD)	186.74	**260.61 (new highs)**	4.8%	39.6%	up	up	up
Fixed Income Yields/Spreads							
U.S. 10-Year Treasury yield	2.69	**1.52 (new lows)**	(1.9)%	(43.5)%			
Cdn. 10-Year Bond yield	1.96	**1.17 (new lows)**	2.6%	(40.3)%			
Recession Watch Spreads							
U.S. 2-year 10-year Treasury spread	0.21	**0.01 (new lows)**	(85.7)%	(95.2)%			
Cdn 2-year 10-year CGB spread	0.10	**-0.22 (new lows)**	(22.2)%	(320.0)%			
Currencies							
US$ Index	95.73	97.53	(0.5)%	1.9%	up	up	up (weak)
Canadian $	0.7350	0.7525	(0.2)%	2.4%	down	neutral	down
Euro	114.58	111.36	0.4%	(2.8)%	down	down	down (weak)
Swiss Franc	101.88	102.53	0.4%	0.6%	up	up	neutral
British Pound	127.50	122.76	1.1%	(3.7)%	neutral	down	down
Japanese Yen	91.24	94.80	0.8%	3.9%	up	up	up
Precious Metals							
Gold	1,281.30	1,537.60	0.4%	20.0%	up	up	up
Silver	15.54	17.41	1.2%	12.0%	up	up	neutral
Platinum	795.90	855.30	0.5%	7.5%	up (weak)	up	down
Base Metals							
Palladium	1,197.20	1,454.30	0.9%	21.5%	up	up	up
Copper	2.63	2.53	(2.5)%	(3.8)%	down	down	down (weak)
Energy							
WTI Oil	45.41	54.17	(0.6)%	19.3%	down	neutral	neutral
Natural Gas	2.94	**2.16**	(1.8)%	(26.5)%	down	down	down

Source: www.stockcharts.com, David Chapman

Note: For an explanation of the trends, see the glossary at the end of this article.
New highs/lows refer to new 52-week highs/lows.

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GLOSSARY

Trends

Daily – Short-term trend (For swing traders)
Weekly – Intermediate-term trend (For long-term trend followers)
Monthly – Long-term secular trend (For long-term trend followers)
Up – The trend is up.
Down – The trend is down
Neutral – Indicators are mostly neutral. A trend change might be in the offing.
Weak – The trend is still up or down but it is weakening. It is also a sign that the trend might change.
Topping – Indicators are suggesting that while the trend remains up there are considerable signs that suggest that the market is topping.
Bottoming – Indicators are suggesting that while the trend is down there are considerable signs that suggest that the market is bottoming.

Disclaimer

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