July 29, 2016

Dear Investor,

The second quarter ended exactly like the first quarter, which ended just like 2015: **FLAT**. If that sounds repetitive, it is. If you find our emphasis on the pattern a bit dark (but honest), it is! If you are paying close attention, you can see *clearly* what we have been saying for years: 'markets' simply *will not rise at all* without being so-induced by central bank money printing. And so, with the Fed 'stopped' for now, another bout of foreign money printing was summoned to nudge stocks upward again in Q2. Just like at the end of Q1, another ferocious but fully artificial rally rescued Q2 from its two-day sell-off (sparked by the United Kingdom voting to leave the European Union), launching the S&P 500 so it could finish just above flat, up 2.7% YTD. Today stocks again hover near all-time highs, ignoring weakening corporate earnings and economic data. And the Fed *proved* again yesterday it cannot raise rates. As we will detail, the European and Japanese central banks are pumping *$180 Billion per month* into markets. They've the broken system and only rising stocks and real estate prices can keep it afloat.

As we go to print, the political conventions just finished up, but this time there was a very stark realization by the American viewing public that they were watching total theater. Both major political parties have revealed quite clearly that their candidates *must* be chosen and controlled by the established class at all costs. In growing numbers Americans from both side of the aisle, for good or bad, are seeing the political system as 'rigged' and their 'choice' as just a manufactured illusion.

We can see on full display that the asset markets too are fully rigged (by largely the same people), albeit it is being disguised as 'monetary policy'. The situation continues to be tolerated through the implicit buy-in of 3 groups: 1) Small investors, who prefer rising account values over disruption, 2) Congress, the members of which profit personally and massively from the game, and 3) Big investors and Wall Street, who profit the most (*they* profit in both rising and declining markets). Now every major 'Too Big to Fail' bank is far larger than it was in 2008, and every one of them has been levied fine after fine for market manipulation and theft. As more-than-willing participants in the Fed's rigged game, they gladly collect profits, purchase politicians and do the Fed's bidding to lift prices. And prices must rise or the system will surely fail to sustain itself.

Central banks, led by the Fed, have now fully repressed people worldwide. Outside the realm of rising 401k accounts, there is now $13 TRILLION in debt outstanding that has negative yields (IE you get less money back than you invest). There is nowhere for investors to turn except to the risky assets into which they have been herded. Former Fed officials like Kevin Warsh and Richard Fisher are regularly taking to the airwaves to warn that the Fed has only one objective: to make asset prices rise. And so, having fully destroyed any notion of '*free'* in the bond, real estate, commodities and foreign currency markets, the Fed has added the equity markets to the list. They are ***almost*** 'all in'.

This may not be a fun realization, but it is fully visible for those who choose to look. As we see it, investors who wish to participate in today's 'markets' should thoughtfully categorize themselves and revisit their strategy. We see three types of investors: **1)** investors who accept central banks as omnipotent, willing to do anything to lift prices and likely to succeed; **2)** investors who view the 'market' environment as increasingly fake and unstable and likely to fail at some point, and **3)** investors who see the markets as the only way to substantially increase their wealth and willing to try to time it before any major unraveling. We do have strategies for all three types; some type of asset is always rising somewhere. If you are reading this letter, please decide which investor type you are, and call us if we can be of assistance at (614) 734-WLTH (9584). More fireworks may be about to begin!

Best Regards,

Mike Sullivan, President, Certified Financial Planning Professional ®

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Market Update & Backdrop

Another quarter passed with lots of movement, but only a little end-progress in major stock indices:

INDEX	TYPE	2016 YTD
Standard & Poor's 500	US Based Large Stocks (500)	**2.7%**
Dow Jones Industrials	US Based Large Stocks (30)	**2.9%**
Nasdaq Composite	US Based Large Stocks	**-4.0%**
Standard & Poor's 400	US Based Mid-Cap Stocks (400)	**5.6%**
Russell 2000	US Based Small-Cap Stocks (2000)	**1.4%**
Dow Jones Transports	US Based Transportation Stocks	**-7.5%**
Dow Jones Utilities	US Based Utility Stocks	**30.2%**
MSCI EAFE	International Large Cap	**-3.0%**
Nikkei 225	Japanese Stocks	**-18.2%**
Hang Seng	Chinese Stocks	**-19.9%**
Barclay Int Bond	Intermediate Bond	**4.7%**
3 Month Treasuries	Cash Equivalent	**1.2%**
HUI Gold Bugs Index	Gold	**64.5%**

- Rates of return for the quarter ended 6/30/2016. Data from Morningstar, yahoo.com

The major strength in Q2 emanated from those most-beaten-down sectors of 2015: oil and energy, precious metals and other commodities and commodity producers. Small company stocks helped too, courtesy of a 'short-squeeze', the age-old Wall Street trick to ramp stocks. The party has continued since 6/30 with the same leaders, particularly gold and silver. But, corporate and economic data remain mixed, the same condition that has existed for three years running now. Here is a sample:

- In the corporate world, Apple's sales, revenue and earnings all dropped. I-phone sales dropped 22%, yet Apple's stock surged 7% after reporting.
- Caterpillar's retail sales have dropped for 43 consecutive months.
- Reports from the twelve regions presided over by the Federal Reserve report more and more weakness and less and less confidence. Philadelphia and Chicago regions just went negative and flat respectively[ii], and the comments from the negative Dallas Region color this fact.[iii]
- Other indicators like the PMI Manufactures index hover just above the 'growth level'.[iv]
- Subprime car loans are imploding, just as sub-prime housing loans did in 2008. It is the same story with the same winners and losers, just a different asset. Ford is worried.
- The summary? Earnings for the S&P 500 have *dropped six quarters straight* and 74% of the companies reporting early on have reported *negative guidance* (including Apple).

In the more important 'macro' areas, housing is cooling as individuals are increasingly priced out of the housing market[v], transportation companies are slowing as goods move around less frequently, and health services companies (the engine of market strength the past few years) are falling off as companies realize they cannot continue perpetually to raise health care and insurance costs at a pace of 10 to 20 percent per year[vi]. In other words, the middle class seems tapped, crushed, spent.

Yet the effort to inflate asset prices to save the system continues. It is the *only* goal of today's central planners. Just as former Fed Officials Fisher and Warsh are telling us, artificial asset inflation is the only card they have. Play it they must, so play it they do. But, like it or not, the strategy is one that has failed throughout history, so we feel you must know that. *Decide which of the 3 investors you are!*

Our last letter and one of our recent updates covered the fact that the large institutions dubbed 'Smart Money' had been selling stocks hand over fist (it reached 18 weeks straight in May). A very ominous sign, it seemed to signify that the big boys viewed that 1) stocks were overvalued, and 2) the central banks would likely be painted into a corner and have to back off their relentless stimulus.

The first point remains firmly true today and may well become even more exaggerated: the Price-to-Earnings ratio for the S&P 500 is 19.4 based on the trailing twelve months of actual earnings, a *very* high level. Based on *projected* earnings going forward, the P/E today is 17, also very high. So far, reported earnings and forecasts are actually *missing* the mark, so earnings going forward should be *lower* than anticipated. How we get a forecast for higher earnings (thus the lower P/E of 17) is anyone's guess. Obviously you get the point. Corporate and economic health are not nearly as rosy as is being portrayed. You might even say there is a lot of 'peddling fiction' going on.

But the second point, the one suggesting central banks might actually cease their lunacy and stop printing money before they collapse the entire system, was once more confirmed to be very far off the mark in Q2. Instead, in Q2 they cranked into even higher gear on the back of the UK's vote to exit from the EU. Clearly, central banks will not stop until they fail. It has gotten so absurd now that many of them just step in *themselves* to buy stocks when real investors don't want to do so.

Given this bizarre new reality, we can see that two very opposing points of view have developed:

1) Stocks will *not be allowed* by central banks to decline to any large degree, so 'real' investors should flock to own them, and perhaps just buy them up without worry. And/or,
2) All semblances of real free markets are essentially gone and faith in unlimited paper money and unlimited manipulation must never falter in order to keep us from outright failure.

The result from view 2 has the potential be catastrophic since if or when confidence (necessary for central banks to successfully manipulate markets) is lost, things will likely go south in a big hurry.

There are plenty of professional investors in *both* camps today. Certainly, many professional investors worship at the altar of Fed omnipotence. And why not? It is self-serving *and* the Fed has theoretically unlimited power until proven otherwise. Craig Johnson of Piper Jaffrey is one of the many Fed worshippers and he recently made his case for the S&P 500 to rise to 2350 by year end.[vii] That the Smart Money that was dumping stocks for 18 straight weeks obviously thought otherwise means little when central banks can simply replace them as 'buyers'. In fact, few observations about the markets mean much these days other than what central banks think, do they?

With many of the major central banks buying stocks outright, and with unlimited instant money at their disposal, it is hard to see any pullback at all, is it not? The logical extension of that concept unfortunately is that if stocks ever *do* go down, it will have to be because the central banks then *want them to decline*. Thus, all aspects of 'free markets' and 'fair trade' can be deemed effectively dead. The only question investors need to answer these days is whether aggressive exposure to the assets being targeted for artificial price increases will succeed or fail. That's it. That's all there is to it.

As we have suggested for years, pumping asset prices and lying about inflation has some natural limits. Even artificially inflating retirement account values, while pleasing to the eye initially, only goes so far. For example, if the rising value of one's retirement accounts is being more than offset by the inflating cost of living, the result will be a *net loss* to the citizen. And that is where we now stand.

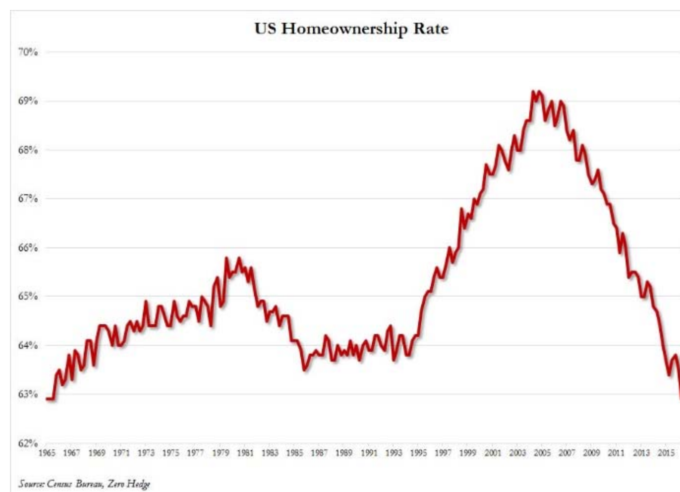
We can see this growing reality simply by observing the increasingly disconnected trends of the S&P 500 versus Consumer Confidence:

Source: Bloomberg

We can also see it in the rising anger in the voting electorates in countries across the globe, including the Trump and Sanders constituencies in the U.S. The Fed and its cohort government agencies can lie about true inflation rates as much as they want, but the balance sheets of the middle and lower classes may now have been punished to the extent they may finally be tapped out.

This condition by itself dispels the establishment narrative that 'everything is great'. It is indeed great for those companies raising their prices, but those are also the costs borne by the majority of the public for whom life gets harder by the month: *real* incomes have not increased for decades.[viii]

But, stocks and real estate valuations continue to rise, totally detached now from historic levels. Yet the problem remains that the benefits of the price pumping go to fewer and fewer people. As Stanley Druckenmiller points out frequently: "Who owns assets? The rich!" Well, these policies have not only mostly enriched the wealthiest (many of whom are Fed cronies who borrow from the Fed at next to nothing), they have priced everyone else out of the markets. For instance, Wall Street borrowed and bought up all of the housing that had been destroyed by their previous bubble, one they created and profited from, while individuals were priced out of those markets from the beginning (destroyed and left with-out a bail-out). Those not priced out, certainly are now: home ownership by individuals is at *the lowest level in 51 years*, dating back to 1965![ix] This can be seen very clearly in the chart below:

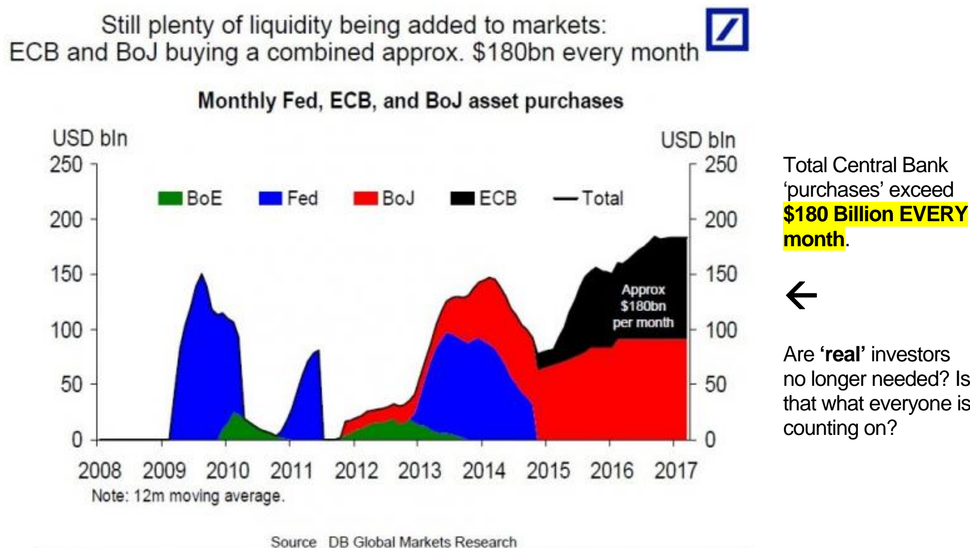


What the chart does not intuitively show is that individuals were lured into houses by the notion of easy riches during the left side climb, then got wiped out. Wall Street, however, profited on the way up (in many ways and because *they blew the bubble*), then got bailed out, and now own the houses.

The fact that the markets are corrupted, manipulated both directly and indirectly, does not mean there are not some prudent investment choices to consider. We will point out some strategies for those who wish to participate later in this letter. It just means prices are truly not dependent on 'real' factors at all anymore. The requirement that we actually have a strong economy (built on a strong public underneath) in order to have a strong stock market is long gone as you can see.

The second quarter served as yet another confirmation ***for you*** that without such meddling, asset prices fall will back very quickly, summoning new rounds of meddling at a faster and faster pace. In Q2 we saw 'markets' rally strongly on the back of the 'Brexit', surprising just about everyone. But *how and why did they rally*? Relief? Economic Strength? Or more all-out meddling at future cost?

As Reuters reported this week, despite the Fed's pretend stand-down, the funny-money injections are ***larger than ever*** now as the ECB and Bank of Japan are pumping $180 Billion into the 'markets'. That is more than was pumped in during the heat of the collapse in 2008. It illustrates precisely how essential money printing is to keep their game going, or rather, to keep their seats at the power table:



With politicians crowing about how great everything is (by pointing at Fed-goosed markets floating near all-time highs but ignoring all of the future costs), the Fed itself again lifted the veil on the farce that it is on July 27th. By passing on another chance to raise rates just 1/4 % (for only the 2nd time in ten years), the Fed once again revealed its claim about being 'data-dependent' is a tall tale. They are *trapped.* While markets celebrate for now, the fiction is soaring to the front of the stage in both monetary and political theaters worldwide. But *yes*, there are more extreme manipulations available.

The 'Brexit', the vote by the United Kingdom to leave the EU, was just the most recent example of complete systemic instability. Immediately after the vote, both the Bank of England and European Central Bank stepped in hard with the ECB buying up everything in sight. As we explained in one of the Updates posted to our website, the ECB expanded its charter to allow it to 'buy' ***corporate*** bonds now. It has already bought up a vast quantity of 'sovereign' bonds (bonds issued by the various states in the EU such as Italy, Spain, Portugal, etc.). You can see *that* activity in the black section of the chart above.) But *now*, it is basically printing money and giving it to *corporations* to make them spend more. Yet elsewhere, such as in the UK, their bubble may be bursting once more as high-end real estate fund? have frozen liquidations to keep wealthy investors from redeeming their investments in the face of diving real estate prices. Trapped?

The *real story* in Europe surrounding Brexit, the *real reason* for the central bank actions, was the fragile state of the major European banks. In fact, the Brexit noise just gave the ECB and Bank of England cover to go hog wild with yet another *bank bail-out*. Under the hood, Germany's Deutsche Bank is an all-out train-wreck, one capable of taking down the global financial system should it fail. Its Q2 its profit tumbled 98%, bearing this fact out loudly, and its stock price is below its 2008 lows.[x] It is crystal clear to the central banks that Deutsche Bank a powder-keg of 'derivatives', owning more of them than any other entity on the planet (JP Morgan is a close second). Nobody else sees it (yet), but the central banks do, and they used the Brexit to orchestrate yet another bank bail-out.

Elsewhere, Italy, like many of the countries in Europe, is bankrupt too. So Italy is now trying to extort a bail-out from the EU by using the threat that if the EU does not bail them out, a ripple effect will very probably tear down Deutsche Bank and subsequently the global financial system right on its heels. Unfortunately, Italy is likely right. We wonder what the smoke screen for that will be.

And so the game continues. And so the game remains exactly the same: to bail out the banks while keeping the existing establishment in power and sticking the expense to the public.

If you are a Monty Python fan, you can relate the current environment to that classic scene in 'The Meaning of Life' wherein Sir Robin clip-clopped his way into the countryside until he encountered a good peasant, played by Eric Idle. After a thoroughly enjoyable exchange about the political construct of the times, the good peasant and his wife began hollering 'Ee's repressin' me, I'm bein' repressed, I'm bein' repressed.!' If you haven't seen it: https://www.youtube.com/watch?v=fxGqcCeV3qk

What is not quite so funny is the fact that repression is so rampant today. The public is willingly playing the role of the peasant, allowing *financial* repression by the reigning powers. As indicated earlier, there is now over **$13 TRILLION** dollars in *negative debt* in the world. The Royal Bank of Scotland (RBS) even notified its depositors recently that they will likely begin to lose money in their *negative rate* savings accounts![xi] In short: no peasant, nowhere, no-how, can earn a decent return without being forced into risky assets by the powers that be, who in turn risk absolutely nothing.

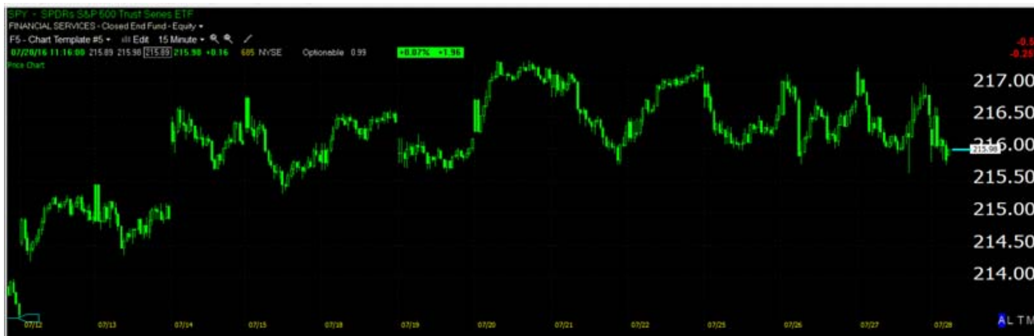
Virtually every quarter now we observe that there seems to be a real possibility we may have reached the turning point we have expected for a long time. The script is the same: the real economy falters without stimulus, manipulation and more repression of the masses. It threatens to tip over, but gets bailed out again. Each time successively more ludicrous tactics follow. The establishment keeps its seats, and throws out various distractions to keep the masses at bay. Unfortunately, on every continent now, the masses *can see* it happening. In increasing numbers, they see the falsity rampant where free markets and real economic data used to be. They see two sets of laws, one for the rich members of the establishment and a second set for those underneath. And they're beginning to see the writing on the wall. This quarter a turn feels closer than ever. But hey, what's new?

Back to the markets, we just emerged from the two-year range in which stocks were trapped. Right after the Fourth of July we broke out, simultaneously breaking a two-year holiday pattern wherein we rally into the upcoming holiday (or, in the few instances in which the markets were declining going into the holiday, we get a rescue rally) … then we roll over right afterwards. In our recent Updates (which you can always read in the Market Updates section of our website) we forecast that we would very likely experience two big upcoming moves: *up, then down*. The 'up' we do not worry about missing. The 'down', however, is a different matter. Remember 2008? For anyone that did not see the Updates previously, the actual chart is below. We may actually be right there … right now:

Source: TC2000

So, here we are, firmly in *the world of the red arrow*. Predictably it is being celebrated as a 'break out' by financial media. As you will see below, it may be being used. As forecast in our [Update](), we saw virtually *no way* Wall Street would not take out the top of this range. There are just too many 'buy orders' there waiting to buy the break out in anticipation of another huge leg up.

We here must note that we have been in a 15-point range in the S&P 500 for *11 straight days*. Such ranges are typically manufactured by Wall Street as they pin prices in an area where they want to unload a large amount of shares. Note the nice long range of the past two weeks for the S&P 500, perfect for distributing lots of shares; 11 days is plenty of time to do it! Just as we expected to clear the two-year range in the preceding Update, the markets may soon choose to reflect on the fact that the Fed is trapped, helicopters notwithstanding. The Bank of Japan just fired up their helicopters, last night, ready to hand every citizen 15,000 yen. Cause to celebrate or panic? (source: TC2000):



We have stated many times that we recognize it is a fool's game to try to pick market tops and bottoms, and even more so in these days of rampant and relentless manipulation. But, it is also hard to ignore that asset prices are totally disconnected from reality. When will it stop? Only time will tell.

We fully suspect that investors will likely know we are nearing the end of the ability of the system to sustain the manipulation any longer when the Fed goes all-in by printing money and disbursing it outright to U.S. citizens: the American 'helicopter drop'. It is a ludicrous thought, and a desperate too, but it is one that is officially 'on the table' nonetheless according to Yellen. Another burst above this range is expected anyway. Our only question is how big will it be, and how long will it last. If you know Wall Street now, expecting it is far from crazy. Just think about what you will do with it.

Thus, if one were inclined to bet, and 'betting the house' were a prudent strategy, betting it on the unaccountable central planners to do everything possible before they surrender their chairs at the royal table might just be the one and only time to do so. But it is a big bet, and it ought to be a quick bet, because if it fails, it is likely to fail quickly and it is likely to fail in a very ugly fashion.

Now, on to investment strategy for today. ***If*** we are resigned to accept the fact that the uncontrolled powers will manipulate asset prices until they fail, logic would suggest the following paths:

- Stock prices should continue to rise on the back of money printing.
- Precious metals prices should be beaten back down by central planners.
- Other commodity prices should be allowed to rise modestly once more, energy in particular.
- Interest rates should continue to be repressed, pushed further into negative territory.
- Real estate prices should be rescued before they fail, and resume their climb.

So, it is likely more than important than ever for investors who have enjoyed this rally to pick their view. If you favor central bank omnipotence, the above bullets are worthy of consideration and loading up on assets that should benefit it is definitely a viable option, albeit a risky one. If, on the other hand, you cannot believe the fiction unfolding in front of you in the monetary and political arenas, we suggest you continue to be careful with your allocation and consider using any subsequent central bank induced rally to reduce your risk if you wish to preserve current account values. If you see both the control held by the central planners, and the likelihood they will continue on their same path, but are interested in trying to 'time it; we suggest allocating for that likelihood but leaning just a bit on the light side in case they fail. We strongly advise all three types of investors to follow the markets on a daily basis. We are in uncharted waters and there is really not much room for error.

In any case, get your popcorn ready. Things are likely to get very interesting, very soon.

As always, call us at (614) 734-9584 if we can be of assistance helping you allocate accordingly!

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[i] http://www.zerohedge.com/news/2016-07-22/former-fed-governor-admits-fed-not-data-dependent-it-propping-asset-markets

[ii] http://www.bloomberg.com/markets/economic-calendar

[iii] http://zerohedge.com/news/2016-07-25/dallas-fed-respondents-destroy-obamas-no-doom-and-gloom-narrative

[iv] http://www.bloomberg.com/markets/economic-calendar f

[v] http://www.bloomberg.com/news/articles/2016-07-26/home-prices-in-20-u-s-cities-climbed-less-than-forecast-in-may

[vi] http://www.zerohedge.com/news/2016-04-15/what-you-spent-your-entire-pay-raise

[vii] http://www.marketwatch.com/story/bull-market-in-us-stocks-has-a-long-way-to-go-2016-07-27

[viii] http://www.pewresearch.org/fact-tank/2014/10/09/for-most-workers-real-wages-have-barely-budged-for-decades/

[ix] http://www.census.gov/housing/hvs/index.html

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