TALKING THE TALK: MARKETPLACE PARALLELS

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"I couldn't quote you no Dickens, Shelley, or Keats
'cause it's all been said before
Make the best out of the bad just laugh it off
You didn't have to come here anyway
So remember, every picture tells a story, don't it?" "Every Picture Tells a Story", Rod Stewart

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CONCLUSION

Marketplace history of course does not necessarily repeat itself, either in whole or in part. However, sometimes it does. In any case, it should not be forgotten. Storytellers reveal (construct, create) parallels (and differences) between the marketplace past and present, not only to explain ancient times and the current situation, but also to predict future phenomena.

Coincidentally, the S+P 500's recent high at 2019 on 9/19/14 occurred almost exactly on the sixth anniversary of Lehman Brothers' 9/15/08 bankruptcy filing. Around the time of that autumn 2008 event, the fearsome worldwide economic crisis that emerged in mid-2007 accelerated.

Yet not so coincidentally, many recent intertwined dramatic marketplace moves in interest rate, stock, currency, and commodity arenas bear significant resemblance to those of the 2007-09 theater. Why? Problems now echo those of the prior period. Some troubles represented by that supposedly distant past have not been sufficiently fixed. In addition, some excesses of that long ago time, even if in somewhat different ways, have reappeared.

In regard to the current vista, underline several trend interrelations between key playgrounds. Focus on the time dimension in this context. Note not only the US Treasury 10 year note's yield decline since its 1/2/14 top at 3.05pc (and the narrowing of the 10 year less two year UST spread), but also the UST's yield slump from 9/19/14's 2.65pc and its break under key support around 2.40 percent. The S+P 500 fell nearly ten percent following 9/19/14's 2019 plateau. In addition, the recent peak in emerging marketplace stocks ("MXEF"; MSCI Emerging Stock Markets Index, from Morgan Stanley) on 9/4/14 at 1104 occurred close in time to both the S+P 500's recent high as well as the rally in the broad real trade-weighted US dollar. Moreover, recall the sharp retreat in the broad Goldman Sachs Commodity Index since 6/23/14's 673 interim top, particularly its recent decisive break under important support at 595/612.

The current and future marketplace theater probably will not duplicate the scope of the 2007-09 global economic disaster. Nevertheless, despite the passage of several years, significant deficit spending by America and other key nations, and widespread extraordinary central bank easy money policies (conjure up the Federal Reserve's yield repression and money printing schemes), we have not entirely escaped the horrific days of the 2007-09 era.

RAISING THE CURTAIN

A recent significant speech by the International Monetary Fund's Managing Director, Christine Lagarde, emphasizes: "The bottom line? Six years after the financial crisis began, we see continued weakness in the global economy." ("The Challenge Facing the Global Economy: New Momentum to Overcome a New Mediocre"; 10/2/14). The IMF's October 2014 "World

Economic Outlook" states: "In advanced economies, the legacies of the precrisis boom and the subsequent crisis (including high private and public debt) still cast a shadow on the recovery." ("Executive Summary", p xv). The International Center for Monetary and Banking Studies warns in its "Geneva Report": "Contrary to widely held beliefs, the world has not yet begun to delever and the global debt-to-GDP ratio is still growing, breaking new highs". The total burden of world debt (private and public, excluding financials) has climbed from about 160 percent of GDP in 2001 to almost 200pc in 2009 to 212 pc in 2013. (See chapter 1, pp1-2 and Figure 1.1; chapter 2, including Table 2.1 and Figure 2.1 at pp12-13).

The glorious and exuberant days of the blessed Goldilocks Era unfortunately possessed noteworthy "excesses" in various marketplace territories such as real estate, interest rate (such as mortgage-backed securities), stocks, and commodities. Recall credit quality and leverage issues. Though the IMF's Managing Director does not conjure up the Goldilocks days and their gloomy aftermath, her speech should evoke memories among audiences. "There is concern that financial sector excesses may be building up, especially in advanced economies. Asset valuations are at an all time high; spreads and volatility are at an all time low." The IMF Director's oration does not refer specifically to US equities or low-grade corporate bonds, but arguably her comments deal with both. She stresses, after mentioning US monetary policy, that "the longer easy money policies continue, the greater the risk of fuelling financial excess." The IMF's "Global Financial Stability Report" (October 2014, "Executive Summary", p ix) notes "Easy money continues to increase global financial stability risks".

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So let's identify parallels between marketplace trends in the 2007-09 vista and nowadays. These similarities signal there is more current and future weakness in the interconnected global economy than many clairvoyants assert.

For additional related analysis, see "Walking the Walk: US Stocks and the Dollar" (10/5/14), "Stepping Higher: UST Two Year Note Yields" (9/21/14), "Bond Yield Perspectives: Easing Comes, Easing Goes" (9/1/14), "Commodity Marketplace Travels" (8/1/14), "Exit Strategies: the Fed, US Treasuries, and US Stocks (7/14/14), "China: Its Great Growth Story Grows Old" (6/23/14), "America the Debtor" (3/17/14), and other essays.

A PORTRAIT: THE TEN YEAR US TREASURY NOTE ALONGSIDE THE S+P 500

"Men make their own history, but they do not make it just as they please; they do not make it under circumstances chosen by themselves, but under circumstances directly found, given and transmitted from the past. The tradition of all the dead generations weighs like a nightmare on the brain of the living." Karl Marx, "The Eighteenth Brumaire of Louis Bonaparte"

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After the Fed ceased its prior rounds of quantitative easing (money printing), the 10 year UST note yield and the S+P 500 tumbled. Although that benevolent central bank embarked on a slow tapering process in mid-December 2013, America's 10 year government note yields headed downhill from 1/2/04's 3.05 percent top. US longer term government interest rates should tend to rise if significant real GDP growth or widespread hopes for it exist, right?

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Anyway, as the Goldilocks Era faded into the sunset, the 10 year's yield established a major peak on 6/13/07 at 5.32 percent, preceding by several months the S+P 500's 10/11/07 major summit at

1576. As UST yields eroded, note the timing of subsequent interim yield tops. The 10 year UST's 4.72pc height on 10/13/07 coincided with the S+P 500's pinnacle. See also the closeness in time of the S+P 500's 5/19/08 final high at 1440 and the UST's 6/13/07 top at 4.27pc.

In the current situation, the UST's 3.05pc top likewise preceded the noteworthy S+P 500 high on 9/19/14 at 2019. Moreover, the UST made an interim top at 2.65pc on 9/19/14 which coincided with the S+P 500's summit that day.

As UST yields plummeted in 2008, and especially from 6/13/08's 4.27pc and 10/5/08's 4.10pc, they broke through key support around 3.25pc (1/23/08 and 3/27/08 bottoms at 3.28pc, 9/16/08 low at 3.24pc). This accelerated the decline in the S+P 500, which collapsed from around 8/11/08's 1313 and 9/19/08's 1265 height. Compare 2014's 10 year UST yield decline, including the fierce move under important support around 2.40pc, from 2.65pc on 9/19/14 to 1.86pc on 10/15/14 alongside the significant price slump in the S+P 500 (the UST had edged down to 2.30pc in mid-August 2014, but this move under 2.40 was not decisive).

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The major bull move from the S+P 500's 10/10/02 bottom at around 769 to 2007's lofty 10/11/07 major high at 1576 lasted five years. The October 2002 bottom times two is 1538, or within about three percent the October 2007 peak. Since the S+P 500 achieved its major bottom on 3/6/09 at 667, its bull move has run about five and a half years, even longer than 2002-07's advance. Whereas S+P 500 prices doubled over the 2002-07 span, 9/19/14's height at 2019 triples March 2009's major bottom (doubles 7/1/10's 1011 trough; and jumps about 50 percent over 11/16/12's 1343 low).

Given that the S+P 500's major bull move since March 2009 was even longer-lasting and stratospheric than the preceding one, observers should be watchful for a very noteworthy S+P 500 decline, extending (or greater than) the one that so far since 9/19/14 has reached around ten percent. With parallels between the 2007-09 world and the current environment in mind (given the recent moves in the UST 10 year, emerging marketplace stocks, the broad real trade-weighted dollar, and the broad GSCI), the S+P 500's 9/19/14 height probably represents an important top. If that top is broken, it probably will not be exceeded by much.

Incidentally, for those seeking further timing parallels in the S+P 500, the 9/19/14 date is not far from the October 2002 and 2007 calendar tops and bottoms (10/10/02; 10/11/07), but also 10/4/11's important low at 1075.

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Watch trends in corporate junk bond yields alongside moves in the S+P 500 and the UST 10 year government note. Monitor credit spreads, such as those between the UST 10 year note and lower grade corporate debt, or those between sovereigns (for example, compare Germany's 10 year government note with that of Spain, Italy, or Greece).

EMERGING STOCK MARKETPLACES

What about merging marketplaces in general (MSCI Emerging Stock Markets Index, "MXEF")? The MXEF attained its major and final highs (at 1345 on 11/1/07 and 1253 on 5/19/08) alongside those in the S+P 500. It crashed from 1057 on 7/24/08 to 446 on 10/28/08.

Emerging stock marketplaces have had many cheerleaders in recent years. However, unlike the S+P 500, the MXEF did not climb to new peaks since spring 2011 (4/27/11 at 1212). Indeed, the MXEF's 2011 elevation never reached its autumn 2007 peak. Yet over the past several years, several important MXEF marketplace turns have occurred around the same time as those in the S+P 500.

Note the timing parallels between the 2007/08 and 2014 relationships between the MXEF and the S+P 500. The recent high in the MXEF on 9/4/14 at 1104 occurred close in time to the S+P 500's 9/19/14 ceiling. It slumped about 11.4 percent to 978 on 10/15/14, a bit more than the S+P 500's almost ten percent slide to 10/15/14's 1821.

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In an interdependent international economy, the ongoing sideways to down trend in emerging marketplace stocks in general warns of slowing growth in advanced as well as developing nations. The retreat in the overall commodities complex roughly resembles that of emerging marketplace equities.

COMMODITIES, ENCORE

Since around mid-2008, movements in commodities in general (broad Goldman Sachs Commodity Index) have tracked those in emerging marketplace stocks to a significant extent. As has been the case for the MXEF, the GSCI has not exceeded its spring 2011 peak (4/11/11 and 5/2/11) at 762.

After peaking on 11/1/07 at 1345, the MXEF made interim highs on 5/19/08 at 1253 and 7/24/08 at 1057. The GSCI's major high on 7/3/08 at 894 occurred midway in time between the MXEF's May and July 2008 interim tops.

What about the GSCI's travels in calendar 2014? After reaching 673 on 6/23/14, the GSCI eroded. Important GSCI support stood at around 595/612. Note the lows at 596 on 4/8/13, 605 on 6/24/13 and 11/7/13, and 604 on 1/9/14. Twice 2/19/09's major trough, attained shortly before the S+P 500's major bottom on 3/6/09 at 667, is 612. On 9/9/14, and thus shortly after the time of the key MXEF high at 1104 on 9/4/14, the GSCI's first close under 595 occurred. The GSCI subsequently tumbled lower as UST yields fell and the MXEF and S+P 500 dropped

TRADE-WEIGHTED DOLLAR

In spring 2008, the broad real trade-weighted dollar ("TWD"; monthly average; Federal Reserve H.10 statistics) began a substantial bull move which interconnected with trends in the UST 10 year, the S+P 500 and emerging marketplace stocks, and commodities in general. The TWD's recent modest strength in relation to these other marketplaces apparently parallels the early stages of the massive 2008 marketplace trends.

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Although the S+P 500 peaked on 10/11/07 at 1576, its final high was 5/19/08 at 1440. Shortly before May 2008's final summit, the broad real TWD in April 2008 established a crucial floor at 84.2 (prior major bottoms around 84.0 in October 1978 and July 1995). The UST's yield tops at 4.27pc on 6/13/08 and 4.10pc on 10/5/08 connect with the TWD's rally since April 2008 and the S+P 500's linked downturn (S+P 500 collapsed from around 8/18/08's 1313 and 9/19/08's 1265).

The global financial crisis worsened in late summer/early fall 2008; the TWD's rally continued alongside this. The TWD stood at about 86.7 in August 2008, hopped to 88.8 in September, and leaped to 93.9 in October. After a 15.1 percent bull ascent, the TWD's summit occurred at 96.9 in March 2009, as did the S+P 500's major bottom.

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After the broad real TWD achieved its March 2009 peak near 96.9 alongside S+P 500's major low on 3/6/09 at 667, the TWD commenced a significant bear move, with the S+P 500 travelling on a wonderful bull path. The TWD declined to its record low 80.5 in July 2011. Until rather recently, and thus for about three years, it remained rather feeble; this arguably encouraged rallies in the S+P 500 and helped the US (and worldwide) economy recover. Beginning in September 2011, it edged over 83.0 and stayed in a rather narrow band, promenading around the prior major lows around 84.0, touching a high of 86.3 in June 2012.

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Significantly, the current advance in the broad real TWD has taken it above its 86.3 June 2012 resistance to 86.6 in September 2014, which is right around August 2008's important 86.7 level. In the context of the 2007-2009 history and current trends in the UST 10 year, MXEF, and broad GSCI, this signals the probability of further strength in the broad real TWD. In addition, the current level of and probable near term ascent by the TWD warns that a significant peak in the S+P 500 was or soon will be created. Steps in the TWD near to or above September 2008's 88.8 (and especially) October 2008's 93.9 boost the likelihood of a substantial S+P 500 price fall.

Whereas the Fed's H.10 does not offer daily data for the broad real TWD, it does provide daily statistics for the nominal broad TWD. The nominal broad TWD's initial take-off point on its rally path was 7/1/14's 101.9, rather close in time to the broad GSCI's 6/23/14 top at 673, as well as the UST 10 year's interim top at 2.69 percent on 7/3/14 (which was not long before the UST's 9/9/14 one at 2.65pc). Even more importantly, underscore the timing of the nominal TWD's ascent from 103.9 on 9/5/14 to 106.7 on 10/3/14 (10/10/14 is the most recent data point) alongside the fall in UST 10 year yields (9/19/14's 2.65pc drop-off point) and downturn in the S+P 500 and MXEF.

With 2008 history in mind, given this recent (although modest) US dollar rally alongside falling UST yields and slumping stock benchmarks such as the S+P 500 and MXEF, how strong is the American and worldwide economy?

CALLING IN THE RESERVES: FED MANEUVERING

"We'll be watching out for trouble, yeah. (All down the line.) And we'd better keep the motor running, yeah. (All down the line.)" Rolling Stones, "All Down the Line"

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The Federal Reserve, the European Central Bank, the Bank of Japan, and their central banking allies do not want insufficient inflation and especially do not want deflation. The Fed and other guardians battle to sustain the economic recovery (and boost stock marketplace and housing prices) and reduce unemployment.

In recent years, the eloquent Fed and its friends devotedly have embraced yield repression, money printing (quantitative easing), and other techniques. Recall the Fed's willingness to engage in rounds of money printing as UST yields and the S+P 500 fell together. The very slow pace of the current tapering process probably partly reflects the Fed's effort to not endanger stock marketplace strength.

The Fed slashed the Fed Funds rate during the economic crisis; it has been under .25pc since December 2008 (monthly average). The Fed introduced its QE1 round of November 2008/March 2009 amidst a horrific stock slump (57.7 percent collapse from the S+P 500's 10/11/07's ceiling at 1576 to its 3/6/09 floor at 667).

However, note the Fed's easing measures after much smaller percentage S+P 500 retreats than that over fifty percent one. Therefore as a guideline, history indicates that a move down of about ten percent (or strong concerns that such a fall will occur) boosts the likelihood of Fed action to generate a stock rally (ensure economic recovery). A decline in the S+P 500 of twenty percent (or fears that this will happen) increases the probability of Fed easing action even more. What is happening in US Treasury rates (and in government securities elsewhere), emerging marketplace equities, the US dollar, and commodities (as well as in the US and international economy in general) surely influences the Fed's decision-making rhetoric and actions.

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In any case, what does marketplace history reveal?

The two and one half month fall from 1220 (4/26/10) to 1011 (7/1/10; 8/27/10 final low at 1040) was only 17.1 percent; the Fed unveiled QE 2 at end August/November 2010. The violent five month stagger lower from 1371 (5/2/11) to 1075 (10/4/11) was 21.6pc; the Fed introduced Operation Twist 9/21/11.

Recall the two month decline in the S+P 500 from 1422 (4/2/12) to 1267 (6/4/12) of about 10.9 percent. Although the Fed did not respond right away, the ECB offered a "whatever it takes" hymn to protect the Eurozone on 7/26/12 and revealed its outright monetary transactions policy (OMT) on 8/2/12. However, the Fed did act merely several months after early June 2012 and probably partly in relation to that bearish April-June S+P 500 shift. The S+P 500 had commenced a new slide. It declined from 1474 (9/14/12) to 1343 (11/16/12), an 8.9pc and two months move. The Fed declared QE3 on 9/14/12 and offered policy guidance and more easing (QE4) on 12/12/12.

In the 'taper tantrum" of spring 2013, which ensued because the Fed raised the possibility of ending its latest QE adventure, the S+P 500 fell relatively modestly. It deteriorated from 1687 (5/22/13) to 1560 (6/24/13) about one month and 7.5 percent. However, the MXEF dove lower more substantially(17.6pc) around the time of this tapering talk, from 1065 (5/9/13) to 878 (6/25/13; 877 was the MXEF bottom of 6/4/12, 6/4/12 also saw a key S+P 500 low, at 1267). Fearful of further S+P 500 declines (economic weakness in the US and elsewhere around the globe), the Fed offered soothing wordplay to calm agitated marketplaces and politicians.

A five percent decline in the S+P 500 from 2019 is 1918, 10pc 1817 (compare 10/15/14's 1821 low), 15pc 1716, 20pc 1615. With the S+P 500 having fallen about ten percent from its 9/19/14 high at 2019 to its 1821 low on 10/15/14 (and note the fall in the UST 10 year under two percent to 1.86pc on 10/15), the President of the St. Louis Fed ran to a pulpit the field and started talking (Bloomberg TV interview, 10/16/14). He preached that the Fed should be wary regarding the decline in inflation expectations; the Fed should try to keep inflation headed toward its inflation target. In addition, he hinted that the Fed should carry on with its current QE money printing scheme (the decision should be data dependent) for a while rather than ceasing it this October.

The Bank of England's chief economist declared on the following day that he favored delayed interest rate increases (Financial Times, 10/18-19/14, p1). The Fed meets 10/28-29/14 and 12/16-17/14.

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Recall the ending days of the Goldilocks Era. The Fed's 2007 easing action after an interim high in the S+P 500, but before its major high in October 2007, reveals the central bank's strong inclination to support the US stock marketplace, even if it is not always able to do so.

In its long bull move, the S+P 500 established an interim high on 7/16/07 at 1556. However, it dropped 11.9 percent to 1371 on 8/16/07. Not long after that apparently scary price drop, the Fed on 9/18/07 cut the Federal Funds rate by 50 basis points to 4.75pc. The S+P 500 achieved its new all-time peak at 1576 on 10/11/07. The Fed nevertheless reduced the Fed Funds rate a further 25bp on 10/31/07 and another 25bp on 12/11/07.

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Looking forward, since history need not repeat itself, the Fed's eloquence and actions may not always achieve the goals the Fed diligently seeks. Continued or even increased easing, whether by the Fed or other important central banks, do not inevitably produce rallies in the S+P 500 (or a continued economic recovery).

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