

Market Outlook:

Slow leak

It takes time for a bicycle tire to lose its air. And oftentimes financial markets exhibit the same type of slow leak before investors realize that the steam has come out of the rally. (For edification purposes, we note that *panic sells* also can occur, swiftly and without warning). My review of the current stochastic condition for the global equity bourses (relative strength integers) has been unyielding in stating that *while the underlying economic fundamental data has been improving since the end of the Great Recession of 2009, the financial markets have been far outpacing the rate of underlying economic growth, and extending into untenable linearity for the past 4 months.*

Usually, it's only *after* a capitulation happens that investors concede the real danger they put themselves into, but by then it can be too late. We are not suggesting that clients sell everything and abandon the investment markets altogether. That implies *market-timing*, and I would suggest that no one is prescient enough to know how to do that effectively. Besides, buying and selling into and out-of rallies is time consuming and likely not to yield the desired result every time.

However, we are suggesting that as equity and bond performance point toward a "reversion to the mean"; and as the Fed continues to provide us acknowledgement of economic sustainability accompanied by the prospect of higher interest rates; as well as the recent buying indicating a more defensive allocation in Utilities and Basic Materials, this would be a good time to park ones' gains and observe a less passionate posture about capital gains in the near-term.

There are a number of catalysts which might precipitate a *distribution at the top* (unseen selling that occurs prior to a markdown event). Most notably, the political rhetoric, social unrest, and heightened jingoism coming from world capitals like Washington DC, Paris, and London. Persistent bull markets typically thrive in periods of modulation, security, and lack of rancor.....all qualities that are missing from the current political climate. While our nation waits to see the details of the economic blueprint laid out by the President before Congress last week, the world also sits on pins and needles trying to assimilate the divergence between *nationalism* and *globalism* in world discourse.

It is far more likely that we have seen the best quarterly performance for 2017 already, meaning that the balance of the year will be spent reallocating towards defensive sectors and raising cash in order to hold on to gains already won.

Critical inflection?

Long periods of linearity (up or down) are antithetical to quantitative laws and are usually harbingers of a trend *reversal* more so than a trend *perpetuation*. It has been over a year since the last significant stock market "correction", and although the calendar alone does not dictate the length or magnitude of a trend's duration, the RSI (relative strength indicator) data does. Right now, these data are disadvantaging the likelihood of a cyclical advance. Note that these indicators are helpful as an adjunct to traditional fundamental analysis, as well. The fundamentals, as mentioned above, are improving, but not on a parallel scale that would support a straight-line run-up in stock prices indefinitely.

This year is likely to be a year in which politics and economics digress until the policies, attitudes and outcomes start to match up. While it is always difficult to buck the trend and sheepishly call for a retreat, we think it prudent to take advantage of our investment success thus far, bank some gains, and start to concede to the slow leak in the tire.

Having once coined the phrase "*parallel disconnect*" to refer to the divergence between two fundamental data seemingly moving in concert...but not correlated in reality...I cannot think of a time when the definition of the term was more succinct. While economic progress is indeed solid, we would not be surprised if the exuberant popularity of stocks were to take a small hiatus and render a "cooling off period" where the opportunities and risks might be reassessed in an atmosphere more receptive to reasonable evaluation of the data.

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