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Everything Hinges On the Fed

RECENTLY CLOSED POSITIONS

Position	Symbol	Buy Date	Buy Price	Sell Date	Sell Price	Gain
UltraShort China	FXP	10/31/18	$75.07	1/3/19	$80.86	**8%**
7-10 Year Treasury ETF	IEF	10/25/18	$100.69	1/15/19	$104.07	**4%**
Freeport McMoRan	FCX	1/24/19	$10.97	1/29/19	$10.44	**5%**

Everything Hinges on the Fed

As I noted in last week's update, the Fed is currently transitioning from hawkish to outright dovish at a staggering pace.

In the simplest of terms, the Fed went from guaranteeing four rates hikes in 2019 as well as a Quantitative Tightening (QT) campaign of $50 billion per month until the Fed balance sheet hits $1 trillion, to suggesting there would be NO rate hikes in 2019 and that the balance sheet reduction should end this year.

This transition took a total of six weeks.

The speed at which this happened alone is cause for concern as it suggests three things:

1) The Fed is just making up policy as it goes.

2) The Fed is clueless as to the impact its policies will have on the system.

3) The Fed is unable to accurately monitor the financial system in real-time.

Regarding #1, it's well known in private that most Central Bankers really don't have a master plan for what they are doing.

For instance, it's now known that when European Central Bank (ECB) President Mario promised to "do whatever it takes" to save the Euro back in 2012, that he didn't have any actual plan for what he would do (Former Treasury Secretary Timothy Geithner has admitted this in interviews).

Closer to home, we know from Fed transcripts that as early as 2009, when the Fed's balance sheet was just $1 trillion, then San Francisco

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SHORT-TERM ISSUES

- The Fed continues to shred credibility with talk of ending its Balance Sheet reduction this year.
- Every major asset class is watching for the Fed's next move.

INTERMEDIATE-TERM ISSUES

- Either an inflationary blow off in commodities and risk assets… or a deflationary crisis.
- China to enter a deflationary collapse.

LONG-TERM ISSUES

- A Crisis worse than 2008.
- Eventual market collapse of 50%+ in real terms.
- A scramble for high-end collateral to bring about derivatives collapse/ implosion of big banks.
-

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CAPITAL RESEARCH

President, soon to be Fed Chair, Janet Yellen worried that the Fed would not be able to exit its balance sheet expansion.

Again, that was back in 2009.

Now, it's one thing for Central Bankers to admit they are clueless in private (they are, after all, human beings, subject to self-doubt and fears just like the rest of us). It's completely something else for Central Bankers to reveal, **through policy**, that they have no clue.

The Fed has just done this. Which brings us to #2…

For 12 months straight, the Fed was adamant in ALL public statements, that it could safely normalize policy. This would mean raising rates to the historic norms (3%+) and reducing its balance sheet to $1 trillion (down from its peak of $4.5 trillion in 2015).

As I noted in last week's market update, EVERY single Fed President was onboard with policy normalization and stated so in both speeches and during Q&A sessions. It was one of the rare times in Fed history, that the opinion of FOMC members appeared unified.

Which is why it's truly staggering that every single former Fed Hawk (a Fed official who believes its time to tighten) has gone completely Dovish in six weeks' time. And not just dovish, but INSANELY dovish.

In the last two weeks we've seen:

1) The Fed Vice Chair say, "rates are in a good place" (meaning the Fed is DONE with rate hikes).

2) The President of the St Louis Federal Reserve Bank say that Fed policy is already "a little bit restrictive" (meaning the Fed should ease).

3) A Fed Governor suggest that the Fed's balance sheet run-off should end in 2019.

4) The Cleveland Fed President suggest that the Fed should just end its balance sheet run-off full stop without tapering.

You get the idea.

My point with the above is that when every major Fed official goes from pushing one major Fed policy to pushing the exact opposite Fed policy in the span of six weeks, it's clear the Fed is comprised of individuals who are both clueless and simply making things up as they go.

In basic terms, a plan is something that you tweak, not something that you completely abandon only to then suggest you should do the exact opposite.

Which brings us to #3 (the Fed is unable to accurately monitor the financial system in real-time).

Anyone could have seen that the Fed's policies were problematic as far back as August 2018 (well before the market meltdown). At that time it was already clear that China's stock market (blue line) US housing (red line), and Copper (green line) were in meltdown mode.

That chart seems pretty simple to me.

If you're running a Central Bank, and China's stock market, US home builders, and Copper (one of the most economically-sensitive commodities in the world) ALL start collapsing during the month you suggest it's time for four more rate hikes while ramping up your QT program (January 2018), it might be safe to assume that it is your policies are impacting the system adversely.

Again, the above is just a single chart, taken from an ordinary charting service (stockcharts). One would assume, given the importance of the Fed, that its officials would have access to the best data and the timeliest, most accurate information possible so as to monitor the impact of

its policies.

It is now clear that the people running the Fed are incapable of doing this.

A reasonably competent analyst, with access to even a basic means for monitoring the financial system, would have been tweaking Fed policy at least by August 2018, if not earlier. The fact that NO ONE at the Fed was doing this tells us that the Fed is run by people who are incapable of monitoring the financial system in real-time. That alone means they are in the wrong profession.

Which brings us to today… As I outlined earlier, we now know the following:

1) The Fed is just making up policy as it goes.

2) The Fed is clueless as to the impact its policies will have on the system.

3) The Fed is unable to accurately monitor the financial system in real-time.

With that in mind, we need to consider that the Fed is clearly now engaged in a PR campaign to prepare the system for the next crisis and the policies the Fed will implement when it hits.

Consider the following proposal put forth by the current President of the Federal Reserve Bank of San Francisco:

> *Federal Reserve Bank of San Francisco President Mary Daly* ***suggested that the central bank could decide to use its balance sheet as a routine part of how it guides the economy, not just as a last-ditch measure to deploy in emergencies.***
>
> *"An important question is, should those always be in the toolkit?"* ***Daly said of post-crisis bond-buying programs, popularly called quantitative easing, or QE.*** *"Should you always have those at your ready, or should you think about, those are only tools you use when you really hit the zero lower bound and you have no other things you can do?"*
>
> *Daly, who was speaking with reporters in San Francisco on Friday,* ***said the question is part of the discussion as the Fed rethinks its monetary policy framework and procedures this year,*** *a process that will involve public outreach and a conference in Chicago in June. While officials often say that the balance sheet could be used again in a serious downturn when rates head to zero, they rarely if ever paint it as something other than a last-ditch option.*

> ***"You could imagine executing policy with your interest rate as your primary tool, and the balance sheet as a secondary tool, but one that you would use more readily,"*** *Daly said. "That's not decided yet."*
>
> https://www.bloomberg.com/news/articles/2019-02-08/balance-sheet-could-be-in-fed-s-regular-toolkit-daly-suggests

Here is a Fed President, *PUBLICLY* stating that the Fed is discussing whether QE should be a *REGULAR* policy as opposed to something to be used during emergencies.

I want to point out that prior to the 2008 Crisis, the idea of the Fed implementing QE **at all,** let alone to the tune of $3.5 trillion, was considered ***insane***. And yet, here were are, in 2019, a mere 15 months after the Fed first launched QT, and the Fed is not only talking about ending QT but it is talking about making QE a REGULAR policy tool.

As if that were not insane enough, last Friday, Richard Clarida, the Fed's current Vice-Chair, its highest-ranking economist, and the primary advisor to Fed Chair Jerome Powell, asked the following rhetorical question during a speech:

> *Are the existing monetary policy tools adequate to achieve and maintain maximum employment and price stability,* ***or should the toolkit be expanded****?*
>
> *https://www.federalreserve.gov/newsevents/speech/clarida20190222a.htm*

He then continued…

> *In addition to assessing the efficacy of these existing tools* [QE and forward guidance], *we will consider additional tools to ease policy when the ELB* [Zero Interest Rate] *is binding.* ***For example, as is presently Bank of Japan policy, the FOMC could, when the ELB is binding, establish a temporary ceiling for Treasury yields at longer maturities by standing ready to purchase them at a preannounced floor price.*** *During the crisis and its aftermath, the Federal Reserve reviewed but ultimately found this tool and some others deployed by foreign central banks wanting relative to the alternatives it did pursue.* ***But the review will reassess the case for these and other tools in light of more recent experience in other countries.***
>
> https://www.federalreserve.gov/newsevents/speech/clarida20190222a.htm

This is the Fed's #2 official, stating that the Fed is considering CAPPING TREASURY YIELDS as well as other more extreme monetary policies. And before we simply dismiss this as an economist gone rogue, consider that the above statement was made at the at the **2019 U.S.**

Monetary Policy Forum and was made in reference to a review in which the Fed is already engaged!

Put another way, this was NOT one Fed official talking about some fringe theory, this was the Fed's #2 PUBLICLY discussing what the Fed is ALREADY doing!

So we now know that the Fed:

1) Had previously reviewed extreme monetary policies including capping Treasury Yields during the 2008 crisis, but decided NOT to employ them.
2) The Fed is currently reviewing these same policies again, NOW.

The implications of this are of extreme importance, the first of which is… if everything is under control, **why is the Fed reviewing the use of policies so extreme that it previously didn't employ them during the Greatest Financial Crisis of the last 100 years?**

The second implication is to ask ourselves, "just what policies is the Fed talking about here?"

The Fed has already given us a clue.

In Clarida's speech he references the Bank of Japan and its policy of capping bod yields. As I've stated previously, the Bank of Japan (BoJ) is roughly 15 years ahead of other Central Banks in terms of monetary policy insanity. The Fed first went to Zero Interest Rate Policy (ZIRP) and launched Quantitative Easing (QE) in 2008. The BoJ introduced these policies in 1999 and 2000, respectively.

With that in mind, and given Fed Vice Chair Clarida's reference to the BoJ, we can consider what other policies that Central Bank has been employing.

They are:

1) Negative Interest Rate Policy (NIRP).
2) Massive Shock and Awe levels of QE.
3) Buying stocks and ETFs outright.

Now, there are certain critical differences between the US and Japan. First and foremost is a matter of culture. The US populace is far more politically charged and engaged in politics than Japan. As a result, Americans are far less tolerant of extreme Government policy, particularly monetary policy than the Japanese.

Case in point, as far back as 2017, half of Americans viewed the Government as a threat to their

freedom.

With that in mind, the bar at which the Fed could implement extreme monetary policy is set far higher than it is for the BoJ.

The Japanese electorate has been willing to stomach 20 years of deflation while the BoJ effectively nationalizes the entire Japanese financial system (it is now the largest owner of most Japanese stocks and owns so many Japanese Government Bonds that some segments of the latter asset class sometimes don't even trade some days)

In the US, it took the Great Financial Crisis for the American electorate to "sign off" on bailouts, ZIRP, and QE. So it is safe to assume that the Fed would need a crisis as extreme if not worse to warrant implementing policies so extreme that it previously didn't push for them during the 2008 meltdown.

All of this provides more evidence to what I have been saying since December: that the Fed is aware that something truly horrific is coming and is already preparing for it.

This is why I continue to believe that another Crisis is approaching. The key to understanding the Fed is to focus on what it does, NOT what it says.

In early 2000s, the Fed hired, then promoted Ben Bernanke, a so-called deflation expert and scholar of the Great Depression, to Fed Chair. THIS told us much more about what was coming than anything Bernanke publicly stated.

Today, the Fed has abandoned ALL of its hawkishness, has ended rate cuts, is talking about ending its balance sheet reduction early, and is engaged in a formal review of monetary policies so extreme that it previously didn't try them during the 2008 crisis.

THIS, more than anything any Fed official states in public, tells us what is going on. The Fed is absolutely TERRIFIED of a crisis hitting and so is waxing dovish while also engaging in a PR campaign to prepare for the next round of extreme monetary pressures.

The Fed is not alone.

Globally Central Banks have completely abandoned any pretense of normalizing policy. The ECB ended its QE program in December. It's already talking about MORE monetary easing… less than eight weeks after it ended its last one!

Moreover, the BoJ has just announced that it will NOT be tapering its QE programs and that it will engage in even MORE QE if the Yen rises too much.

And then there's the People's Bank of China… which has just engaged in the single largest liquidity pump in its history, flooding some $600 BILLION in liquidity into its system.

Simply put, globally Central Banks have given up all pretense of ever being able to normalize. The next round of stimulus will soon arrive. The question now is figuring out which one will have the greatest impact on the financial system.

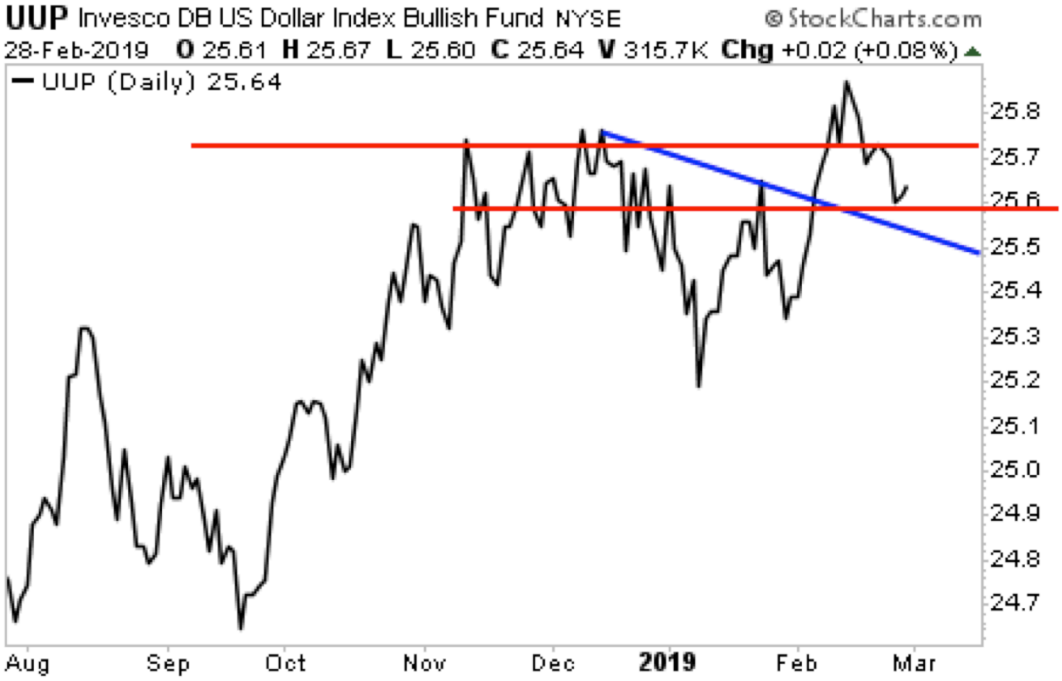
The answer is THE FED.

If the Fed really does end its balance sheet reduction in the near future, then the entire landscape of the financial system will shift into reflation/ inflation mode.

This is the single biggest issue for the financial system today. Literally every asset class is waiting to see what the Fed will do. Oil, Stocks, Gold, etc…. are all at lines of MAJOR importance.

Let's start with the $USD.

The $USD has failed to breakout to new highs. Instead it has rolled over and taken out one line of support before bouncing off a second lower level of support.



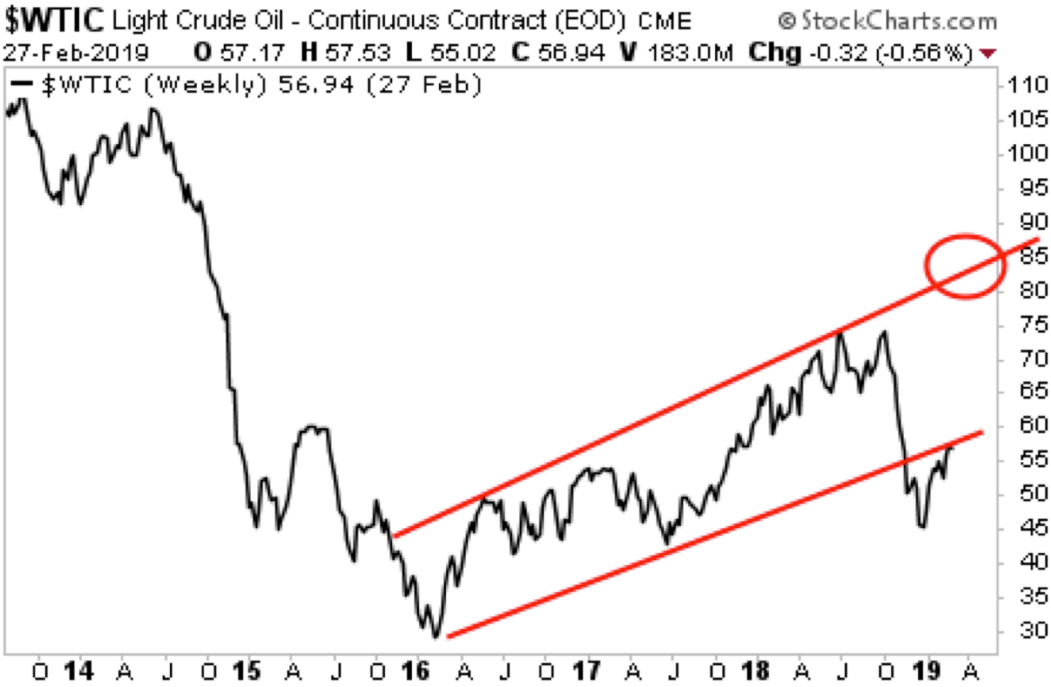
If this doesn't hold here, then the currency markets will "smell" that the Fed is indeed done with any kind of tightening and the $USD will break down in a significant way.

If that happens, the $USD will have broken CRITICAL support on the monthly chart which suggests its heading to the mid-80s.

This would represent a TECTONIC shift for the financial system from towards inflation/ reflation.

Literally every asset class is watching this.

Oil is at THE line for its rally. If it breaks out to the upside here, then a run to $80-$85 is possible.



Similarly, Copper is at THE line in terms of resistance (purple line). If it takes this line out, Copper will make a run to $3.75.

Similarly, Gold is at THE Line in terms of overhead resistance today (purple line). If it takes out this line, it will begin a long-term bull market run to $1,550.

In terms of stocks, the S&P 500 is at THE line for overhead resistance. I also note that it has *just* broken out of its bearish rising wedge formation to the downside.

The Russell 2000, which leads the S&P 500, suggests stocks will NOT break out to new highs.

Based on my Fed analysis, this would indicate that stocks realize that higher inflation is coming, which would squeeze margins and destroy profits. Between that and the approaching recession, this would be a perfect storm of stagflation (slow growth and higher inflation).

Bonds are watching this closely. The long Treasury is at THE line in terms of support (purple line). A breakdown here would mean bonds are shifting towards inflation too. This would mean TLT heading towards 110.

The same is true for 10-Year Treasury Yields, which are at THE line in terms of support (purple line). If we hold here, yields will rise (inflationary) and the yield on the 10-Year will rise to over 3.3%

Bottom-line: EVERYTHING hinges on what the Fed does next.

There is a LOT of talk by Fed officials about whether or not the Fed will completely "throw in the towel" on its hawkishness. The markets are watching this. And as I said before, EVERY major asset class is at THE line in terms of deciding which way things go from here.

The picture will be clear within a month. But given the magnitude of what's happening, it will be well worth the wait to see what happens. If the Fed DOES abandons any pretense of hawkishness, we're moving into an inflationary blow off in commodities and risk assets.

If the Fed doesn't do this, but proves that all of its talk of abandoning hawkishness was just talk to juice stocks, we'll have a deflationary collapse right here and now.

EVERYTHING will be decided in the next four weeks.

Right now, the jury's still out, which is why we are remaining in all of our bearish hedges, including ones related to inflation (Oil, Emerging Markets, etc.) But as soon as it's clear what's coming, we'll be positioning our portfolio to profit from it.

And given the magnitude of what the Fed is doing, the gains are going to be ENORMOUS. Think "going short right before the 2008 crash" big.

This concludes this week's update for ***Private Wealth Advisory***. I'm watching the markets closely and will issue updates as needed. Barring any new developments you'll next hear from me next Thursday in our usual weekly market update for ***Private Wealth Advisory.***

In the mean-time, if you are looking for a way to play short-term market moves or to get into day trading for larger, more rapid gains, I also run a weekly options trading service that typically holds positions for just 2-3 weeks at the most, and usually just a few days.

It's called ***The Crisis Trader*** and it uses options to trade highly predictable moves in stocks and ETFs for double-digit gains. **Since inception, this newsletter has returned average annual gains of 41%.**

Typically a subscription to this service costs $799. But I'd like to invite any of you to join at a discounted rate of $499 (35% off the usual market price).

You can try it for 60 days. If you find it's not what you're looking for, you can email us at support@phoenixcapitalresearch.com and we'll issue a full refund no questions asked.

To take out a 60 day $499 trial subscription to ***The Crisis Trader*** use the link below.

https://www.phoenixcapitalmarketing.com/tctrenewal499.html

Until next Thursday…

Best Regards,

Graham Summers
Chief Market Strategist
Phoenix Capital Research

OPEN POSITIONS

STOCKS PORTFOLIO

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return *
Freeport McMoRan	FCX	2/21/19	$13.02	$12.90	-1%	-1%
US Steel	X	2/21/19	$24.12	$22.41	-7%	-7%

BONDS PORTFOLIO

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return *
Long Treasury ETF	TLT	6/27/18	$120.24	$120.02	0%	2%
1-3 Year Treasury ETF	SHY	2/7/19	$83.68	$83.75	0%	0%

PRECIOUS METALS/ MINERS PORTFOLIO

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return*
Gold		3/17/10	$1,120	$1,314.00	-1%	17%
Silver		3/17/10	$16.15	$15.64	-1%	-2%
First Majestic Silver	AG	5/12/17	$6.78	$6.74	5%	-5%
Iamgold	IAG	9/28/17	$5.08	$3.34	-1%	-31%
Silver Mining ETF	SIL	10/4/17	$29.81	$26.88	1%	-9%
Silver Mining Juniors ETF	SILJ	10/4/17	$10.45	$9.23	2%	-12%
Gold Mining ETF	GDX	6/6/18	$22.64	$22.24	0%	-1%
Gold Mining Juniors ETF	GDXJ	6/6/18	$32.98	$32.41	0%	-1%
Hecla Mining	HCLA	7/23/18	$3.05	$2.40	-3%	-17%

Prices as of 2/28/19 at market's close.
***Gains include dividends**

Bear Market Portfolio

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return*
Emerging Markets ETF	EEM	12/6/18	$40.64	$42.26	1%	-4%
Rio Tinto	RIO	12/6/18	$46.38	$58.20	0%	-25%
Amazon (SHORT)	AMZN	1/3/19	$1,530.00	$1,639.83	-1%	-7%
Alphabet (SHORT)	GOOG	1/3/19	$1,042.56	$1,119.82	-2%	-7%
UltraShort Oil ETF	SCO	1/3/19	$27.40	$18.56	-1%	-32%
Japan ETF (SHORT)	EWJ	1/3/19	$51.08	$54.36	1%	-6%
UltraShort Russell 2000 ETF	TWM	1/3/19	$20.65	$14.96	0%	-28%
Retail ETF	XRT	1/10/19	$43.51	$45.88	-2%	-5%
JP Morgan	JPM	1/10/19	$99.89	$104.36	2%	-4%
UltraShort China ETF	FXP	1/24/19	$65.99	$60.70	-1%	-8%
Arcelor Mittal	MT	1/24/19	$22.59	$22.85	1%	-1%

CASH/ CURRENCIES PORTFOLIO

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return*
US Dollar ETF	UUP	11/8/18	$25.75	$25.64	0%	0%

Macro Trend Portfolio

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return*
Corsa Coal	CRSXF	12/21/17	$1.20	$0.65	7%	-46%
Uranium ETF	URA	1/17/18	$14.93	$12.37	-4%	-17%

Prices as of 2/28/19 at market's close.
***Gains include dividends**