PRIVATE WEALTH ADVISORY

INVESTMENT RESEARCH THAT CONVERTS

Weekly Market Update 4-11-19

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The Fed now has a colossal problem on its hands.

That problem is that in its efforts to avoid debt deflation, the Fed is going to unleash an inflationary spike.

As I've noted over the last few months, the Fed's embarrassing U-turn from extreme hawkishness to extreme dovishness represents a tectonic shift in the financial landscape.

One consequence of this shift is that the Fed will foster a bubble in the stock market: a situation in which stocks will rise to dangerous highs before crashing down. That process is already underway, with stocks rising despite a clear worsening in economic data, as well as a significant drop in corporate profits (more on this later in this update).

The other consequence is that the Fed is going to let inflation get out of control. Indeed, by the look of things, this is already happening.

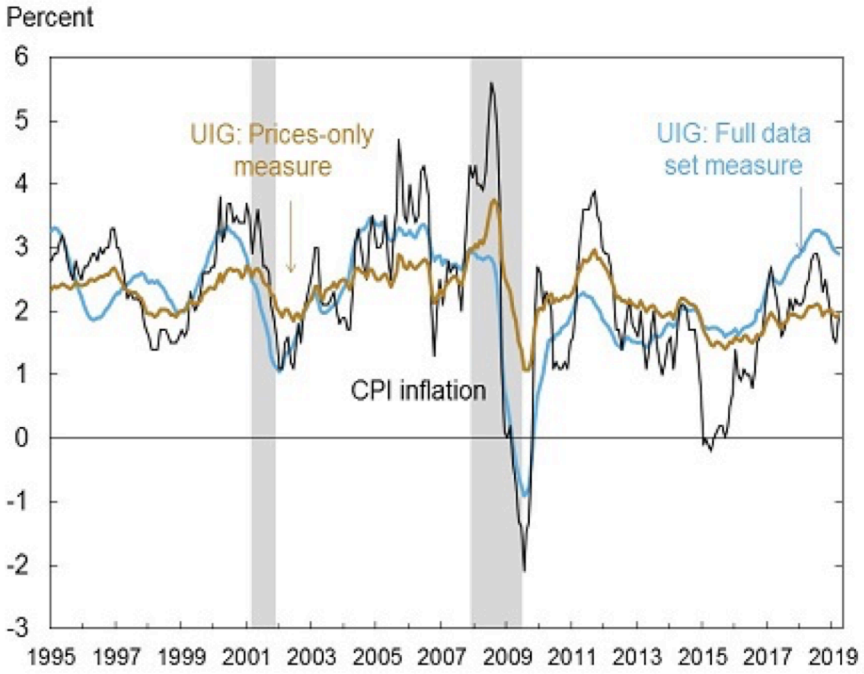
If you'll recall, throughout 2018, Fed Chair Jerome Powell was adamant that the Fed would raise rates to the neutral rate: the rate of inflation/ economic growth.

We've already outlined in previous issues how the Fed completely abandoned this policy once the stock market collapsed in October-December 2018… but what's striking is that Fed officials are now claiming it accomplished its goals, despite the clear evidence this to untrue!

Indeed, we know this from the Fed's OWN DATA POINTS!

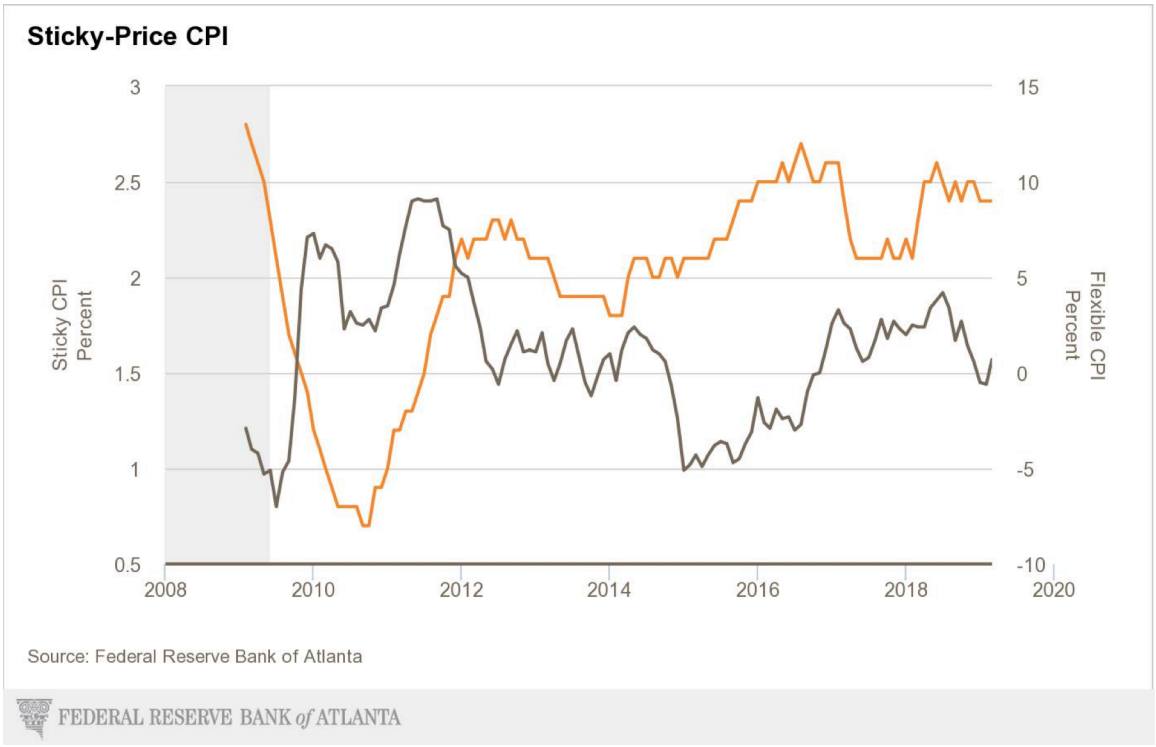
The Underlying Inflation Gauge (UIG) is a broad inflation developed by the **NY Fed** to measure that *"captures sustained movements in inflation from information contained in a broad set of price, real activity, and financial data."*

The UIG shows inflation is currently clocking in at 2.91%



Another Fed inflation metric, is the Atlanta Fed's "sticky CPI" represents a *"weighted basket of items that change price relatively slowly"* (i.e. inflation that takes a while to seep into the financial system).

THAT inflation gauge is clocking in at an annualized pace of 2.7%.

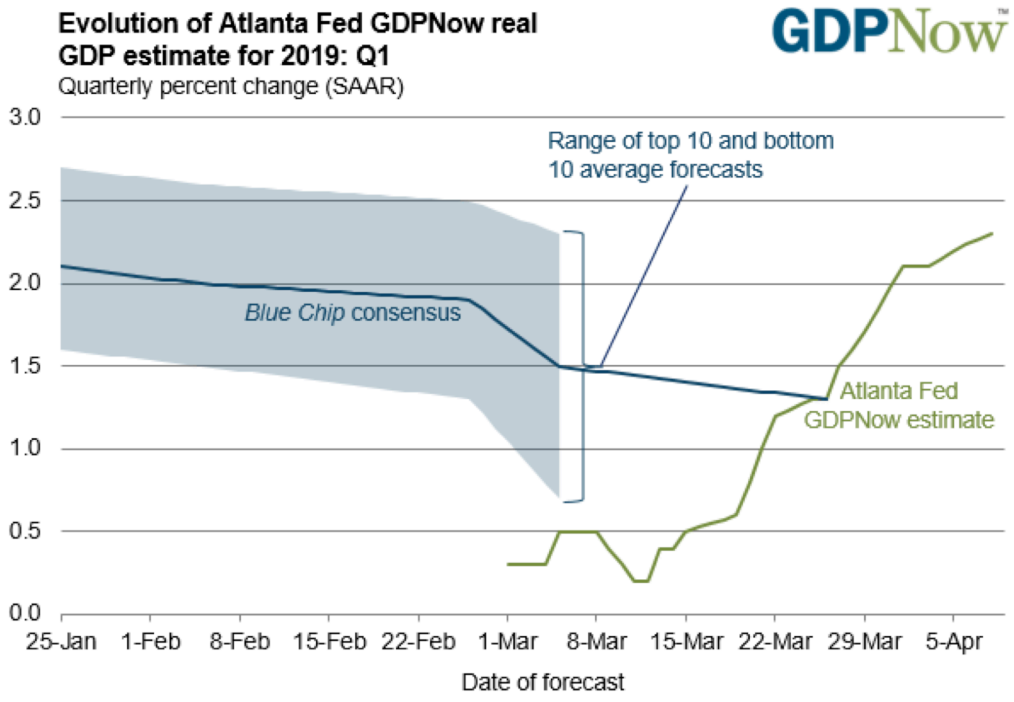


So, based on the Fed's OWN data, overall inflation is near 3% and sticky inflation (inflation that is difficult to halt) at 2.7%.

The Fed's Fund Rate is at 2.5%... well below both.

From this perspective alone, it's very difficult to see how the Fed can claim rates are now at the "neutral rate." However, it's once we start looking at the GDP data that things start to get VERY ugly.

The Fed's own GDP Now measure, which tracks real-time GDP growth is clocking in at 2.3%.



Sources: *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*

Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the *Blue Chip* survey.

So inflation is above both interest rates… AND GDP growth.

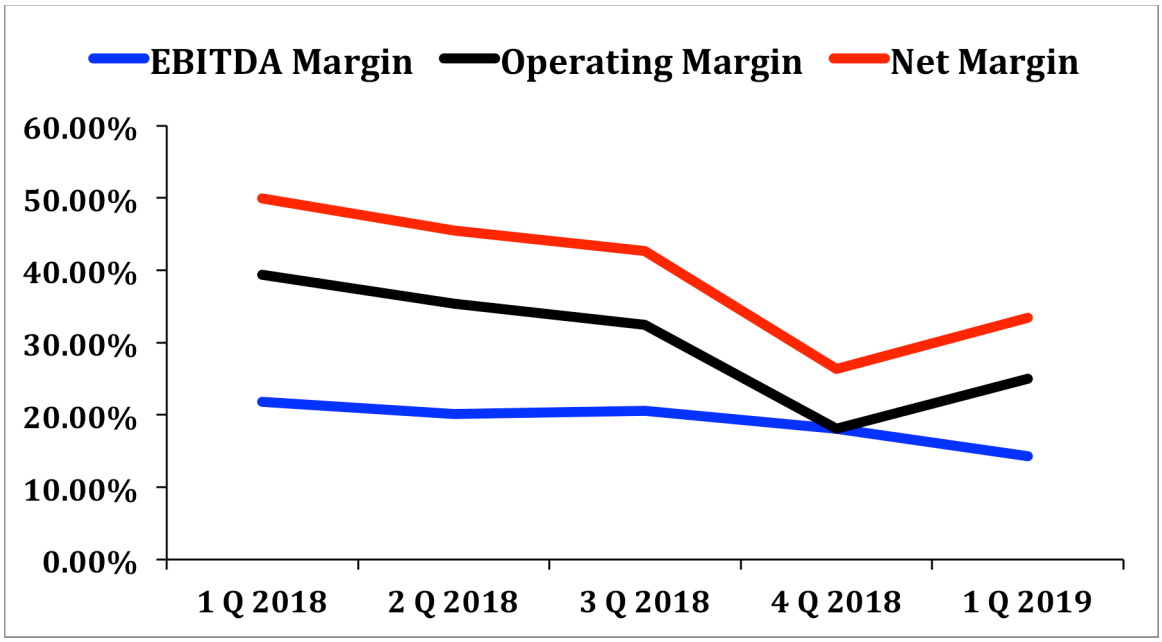
And the Fed knows this.

Now, even under the best of circumstances, this would be an issue. A higher rate of inflation means higher costs of living, which cuts into consumer spending (70% of GDP).

For investors, a higher rate of inflation ALSO means higher corporate operating costs. Higher corporate operating costs means lower corporate profits (profits=revenues minus costs).

So… based on where things are right now, one could predict that unless the Fed hikes rates soon, inflation will begin to eat into economic growth AND corporate profits.

Indeed, the latter process is already underway. Corporate profit margins (EBITDA margin, Operating Margins, and Net Margins) are all trailing down.



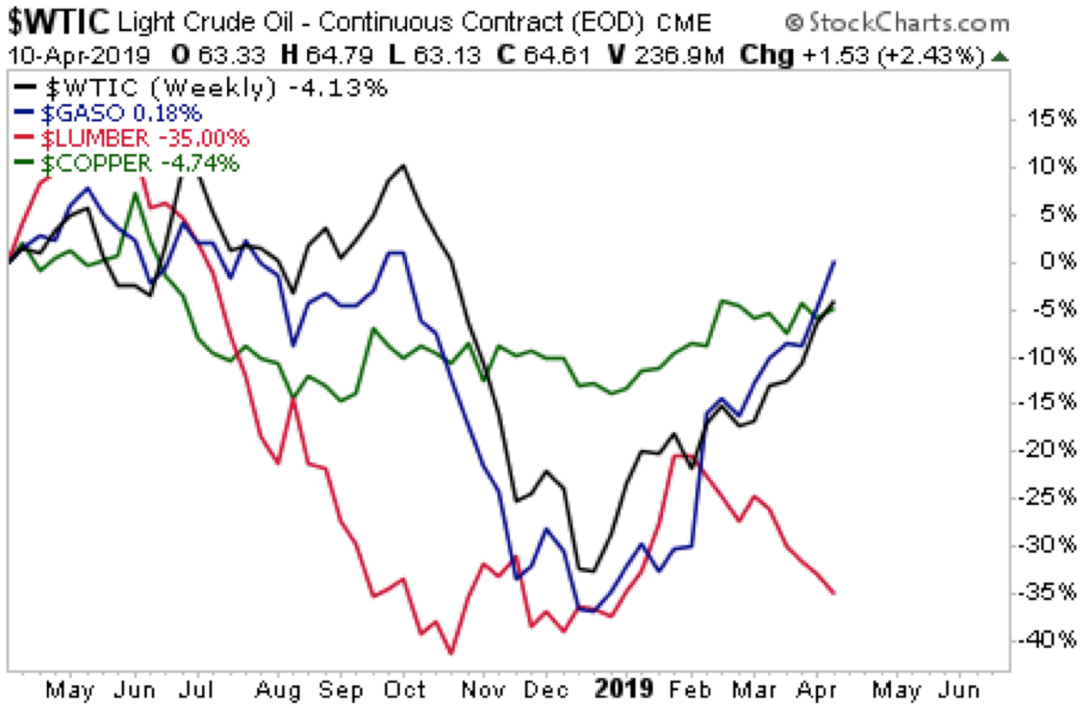
The financial media is bending over backwards to explain that this "earnings recession" doesn't involve inflation causing higher costs. However, the below article from *Bloomberg* hits the nail on the head. It's extraordinary this was allowed to get to print as it suggests A) profits have peaked and B) an inflationary spike is coming.

> *The Federal Reserve may not see much inflation, but the stock market sure can, and its whereabouts helps explain why enthusiasm for equities continues to build…*
>
> *"S&P 500 gross margins show companies aren't having too much trouble passing prices on to consumers despite the evident slowdown in global growth last fall," wrote Bloomberg Intelligence analysts led by chief equity strategist Gina Martin Adams. "**Pricing power is intact, implying inflation may be 'stickier' than is ideal for a shift to dovish Fed policy."***
>
> *That's the rub, that what's good for earnings and great for investors might contain the seeds of doom for the Fed's suddenly stimulative stance somewhere down the line. "**S&P 500 gross margins don't correlate perfectly with economic measures of inflation, but peaks have historically led peaks in U.S. consumer price inflation by 6-12 months,"** Adams's team wrote.*
>
> https://www.bloomberg.com/news/articles/2019-03-22/inflation-alive-and-well-and-living-in-s-p-500-income-statements

By the way, gross margins peaked on an annualized basis in 2Q18. So we're right in the 12-month window for a spike in consumer inflation.

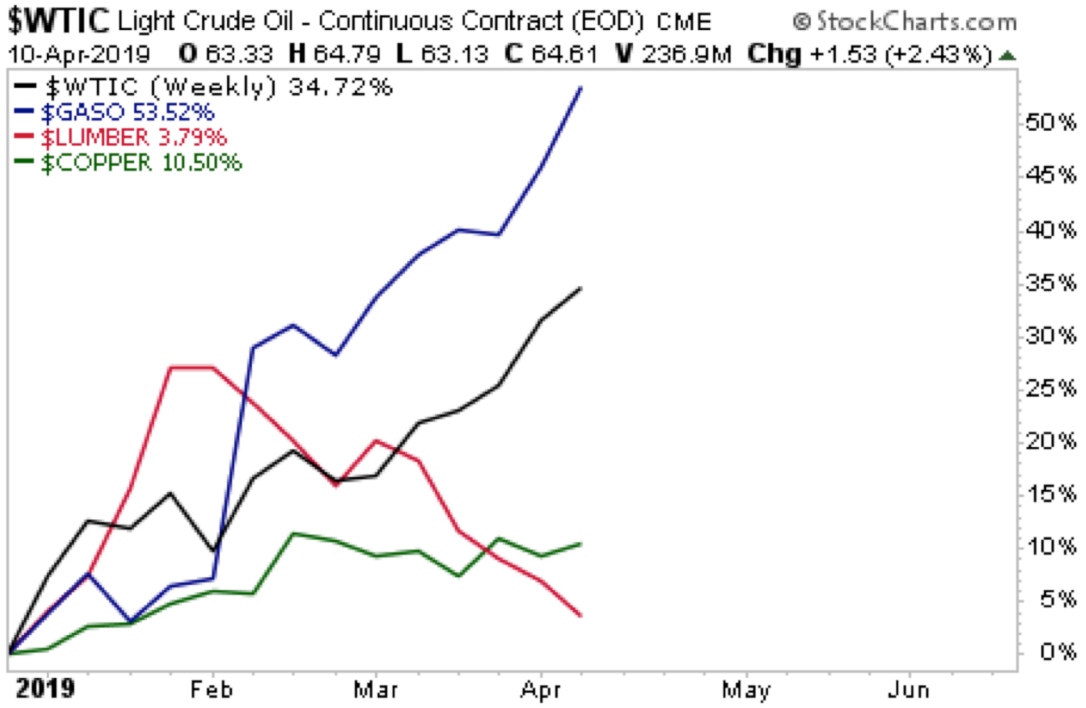
And it looks like it's on its way, courtesy of a spike in economically- linked commodities, specifically oil, gasoline, lumber, and copper.

On a year over year basis, three of these are down. Which is why the "official" inflation measures continue to look reasonable.



However, trends don't move in a year over year fashion, they move sequentially in a week over week or month over month fashion. And that picture is **downright ugly**.

Year to date, all of these commodities are up. Three of them are up double digits. And the single most important one for consumer spending (gasoline) is up 50%.

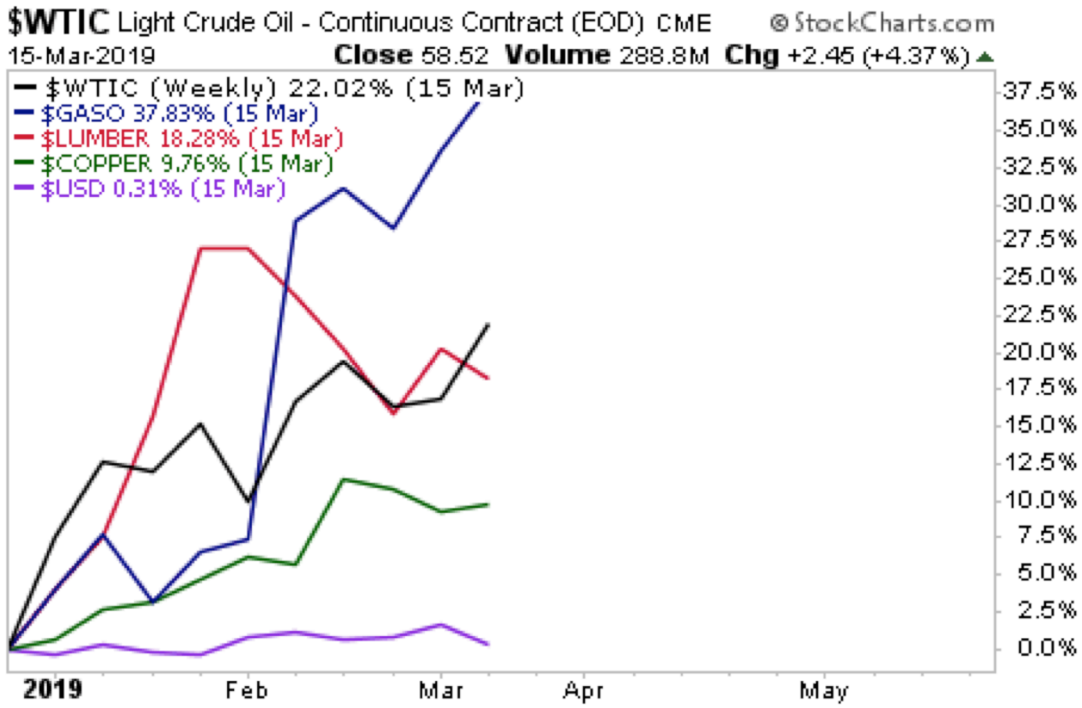


These spikes are going to start seeping into the official inflation data in the coming weeks. Which is why I said the Fed has a colossal problem on its hands.

If inflation was already higher than economic growth and interest rates BEFORE these price spikes show up in the data… what will it look like once these spikes start to be incorporated?

Much higher.

Bear in mind, these price spikes are occurring when the $USD has held up reasonably well. It'd be one thing if we were seeing commodities roar higher on $USD weakness… but they're roaring higher while the $USD has held up (it's flat year to date).



So… if inflation is already higher than GDP growth and interest rates, and commodities are SOARING while the $USD is roughly flat…

The Fed is officially trapped. If it hikes rates more, it risks hurting GDP growth… as well as the stock market (the corporate debt market froze for 40 days during the last month in which the Fed raised rates).

But if the Fed *doesn't* hike rates, inflation will continue to rise, possibly quite aggressively.

Now let's add one more component…

Next year is an election year. And the President of the Unites States has already made it clear that:

1) He associates the stock market with his success as a leader.

2) He thinks the Fed should be CUTTING rates, not hiking them.

3) He is perfectly willing to put political/ media pressure on the Fed if it doesn't support his goals.

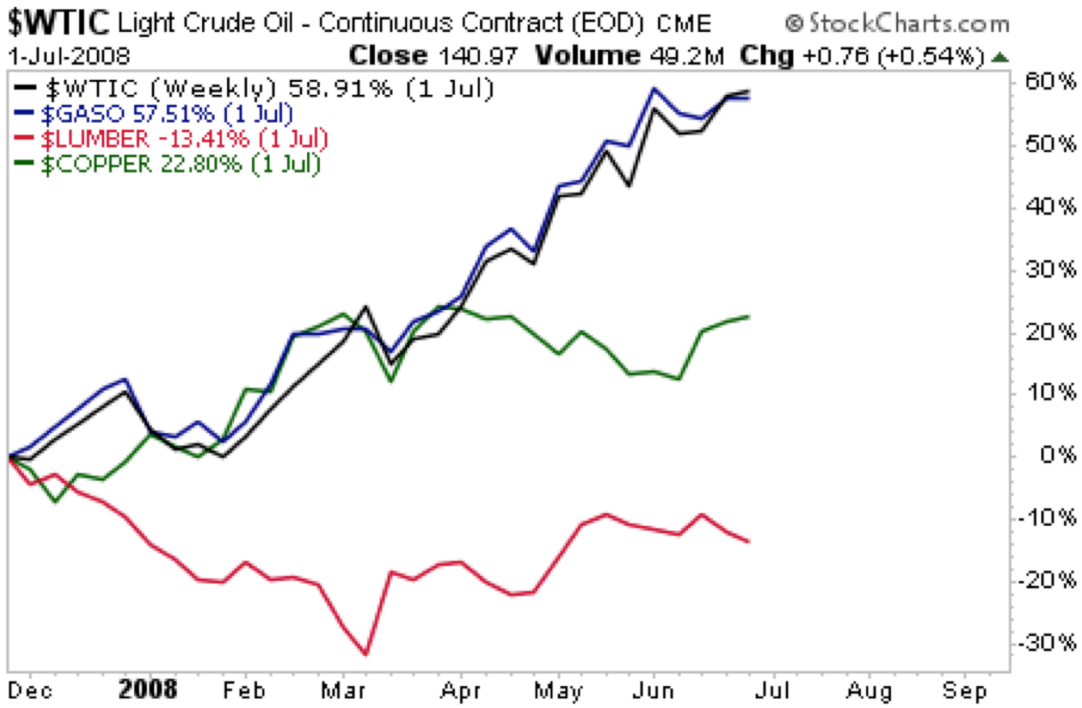
This is not just political theater either. President Trump's two most recent nominations to fill vacant seats on the Fed board of Governors are Stephen Moore and Herman Cain.

BOTH of them support cutting rates NOW.

With that in mind, it's very possibly that in the very near future any attempt at raising rates, or increased hawkishness by the Fed will be met with tremendous push-back, not just from the White House, but from within Fed leadership as well.

Taking all of this into account, the odds now highly favor a situation in which inflation runs "hot" for the next six months.

We saw something similar in 2008. The US economy officially entered a recession at the end of 2007… yet despite growth collapsing, we experienced an inflationary shock as Oil, Gas, and Copper roared higher (Lumber was down due to the housing market collapsing).



We've covered a lot of ground here, but my primary point is this: the Fed's decision to go "into the bubble business" will result in a late cycle inflationary spike over the next six months.

This will crush corporate profits… and unleash large rallies in several commodities. We're already positioned for this with our Bear Market portfolio as well as our position in the Energy

Stock ETF (XLE) and Precious Metals.

Having said that, the stock market currently looks primed for a correction.

The S&P 500 is about to complete a bearish rising wedge formation.

Stocks need to either go parabolic here on buying demand, or we're going to see a corrective decline.

The Russell 2000, which typically leads the S&P 500, suggests the move will be a decline.

Goldman Sachs (GS) which is arguably the most important stock in the market, is also suggesting the move will be DOWN.

As is the yield on the 10-Year US Treasury.

The big "tell" will be seeing where the decline halts on stocks. The S&P 500 has support at 2,790, 2,700 and 2,590 or so. If stocks decline to the first or second line and **hold** there, we could see a run to new All Time Highs (possibly even 3,000+ on the S&P 500).

If those lines DON'T hold, then something MUCH uglier could hit.

Currently I put the odds of that last option around 30%. Given the strength in stocks, I think we'll see a corrective decline to somewhere in the 2,700s on the S&P 500. At that point I expect a bottom to form, which will lead to a blow off top to new All Time Highs sometime this summer.

Unfortunately, at that point I expect things will start to get ugly and the bear market will resume in earnest. And I expect it to last through 2020, unless the Fed AGGRESSIVELY eases. But for now, the gameplan is a corrective decline in stocks, followed by a blow off top. And we're positioned to profit from all this beautifully.

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 regular weekly market update of ***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%. We just closed out gains of 17%, 20%, 20%, and 21% in the last two weeks alone.**

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 *
Energy ETF	XLE	3/21/19	$67.08	$67.38	-1%	0%
Wal-Mart	WMT	3/21/19	$98.73	$100.80	2%	2%
Facebook	FB	4/5/19	$175.25	$177.51	1%	1%
Apple	AAPL	4/5/19	$197.79	$198.95	1%	1%
China Tech ETF	CQQQ	4/5/19	$51.90	$50.89	-2%	-2%

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	$124.09	-2%	5%
1-3 Year Treasury ETF	SHY	2/7/19	$83.68	$83.88	0%	1%
7-10 Year Treasury ETF	IEF	3/21/19	$105.66	$105.74	-1%	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	$1,296.00	0%	16%
Silver		3/17/10	$16.23	$15.07	0%	-4%
First Majestic Silver	AG	5/12/17	$7.43	$6.46	-1%	-7%
Iamgold	IAG	9/28/17	$6.40	$3.42	-1%	-30%
Silver Mining ETF	SIL	10/4/17	$32.51	$26.40	0%	-10%
Silver Mining Juniors ETF	SILJ	10/4/17	$11.83	$8.84	0%	-14%
Gold Mining ETF	GDX	6/6/18	$22.58	$22.42	0%	0%
Gold Mining Juniors ETF	GDXJ	6/6/18	$32.99	$31.81	0%	-2%
Hecla Mining	HCLA	7/23/18	$3.39	$2.38	0%	-18%

Prices as of 4/11/19 at the 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 (SHORT)	EEM	12/6/18	$40.64	$44.04	1%	-8%
Amazon (SHORT)	AMZN	1/3/19	$1,500.28	$1,844.07	-1%	-21%
Alphabet (SHORT)	GOOG	1/3/19	$1,016.06	$1,204.62	0%	-16%
Japan ETF (SHORT)	EWJ	1/3/19	$50.73	$54.78	1%	-7%
UltraShort Russell 2000	TWM	1/3/19	$18.24*	$14.72	0%	-19%
Retail ETF (SHORT)	XRT	1/10/19	$43.60	$45.32	1%	-4%
JP Morgan (SHORT)	JPM	1/10/19	$100.39	$106.23	-1%	-6%
European Financials ETF (SHORT)	EUFN	2/7/19	$17.81	$19.13	0%	-7%
Italy ETF (SHORT)	EWI	2/7/19	$25.71	$28.16	0%	-10%
Deutsche Bank (SHORT)	DB	3/7/19	$8.66	$8.39	0%	3%
Etsy (SHORT)	ETSY	3/7/19	$67.24	$67.65	1%	-1%
Netflix (SHORT)	NFLX	3/7/19	$352.60	$367.65	0%	-4%

CASH/ CURRENCIES PORTFOLIO

Position	Symbol	Buy Date	Buy Price	Current Price	Change From Last Week	Total Return*
Australian Dollar	FXA	4/21/18	$71.29	$71.25	0%	0%

Prices as of 4/11/19 at the market's close.
***Gains include dividends**
**** average of $20.65 and $15.83**

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	$0.63	**1%**	**-47%**
Uranium ETF	URA	1/17/18	$14.93	$12.80	**0%**	**-14%**

Prices as of 4/11/19 at the market's close.
***Gains include dividends**