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Weekly Market Update: 9/8/15

Dear Subscribers

All eyes, particularly Central banker eyes, are currently on China.

China is the poster child for every economic ill in the world today. Whether it's misguided Central Planning, aggressive money printing/ stimulus, political corruption, phony economic statistics, opaque financial instruments, garbage debts, etc.… China is the global leader.

With that in mind, China's credit bubble has burst, which in turn has popped its real estate and stock market bubbles. The People's Bank of China (PBoC) is desperately trying to reflate the latter, having realized that the first two (credit and real estate) are far too big to be reflated.

Much is at stake here as China 's economy has largely been seen as the "engine" that drove the global economy out of recession in 2009. This narrative continues today with most official forecasts showing that China will account for over 30% of Global GDP growth going forward. If the "China growth miracle" narrative dies the "growth" narrative as a whole dies.

As I noted in the December 31, 2014, issue of ***Private Wealth Advisory***, titled, A *Gradual Unfolding*:

> Last year (2014) will likely go down in history as the "beginning of the end" for the current global Central Banking system.
>
> **What will follow will be a gradual unfolding of the next crisis and very likely the collapse of the Central Banking system as we know it.**
>
> I want to warn you that this process will not be fast by any means.

Central Banks and the political elite will fight tooth and nail to maintain the status quo, even if this means breaking the law (freezing bank accounts or funds to stop withdrawals) or closing down the markets (the Dow was closed for four and a half months during World War 1).

This process is well underway in China today. And as I predicted in December 2014, the Central Banks and political elite are fighting this process "tooth and nail."

To that end, China has spent an incredible $236 BILLION propping up its stock market over the last few months. This represents an amount equal to nearly 4% of China GDP… **<u>in three months</u>**.

The pace of the spending hasn't slowed either, with $96 billion being spent in August alone. This represents an amount equal to nearly 10% of China's stock market FLOAT (freely traded shares).

<u>Yes, China spent nearly 10% of its free market float propping up stocks in August.</u> This would be the monetary equivalent to the Federal Reserve spending $1.8 TRILLION in a single month propping up stocks.

And despite spending this incredible amount of money, China's stock market managed to lose another 25%.

I have long claimed that there are in fact problems so large that Central Banks cannot fix them. China has proven this in stark detail. It has spent an incredible amount of money to prop up its market. It has also jailed numerous "manipulators"

(patsies) who it claims caused the collapse. And yet the Chinese stock market continues to fall.

This is a massive warning to the rest of the world. When the next Crisis begins to accelerate, nothing will be able to stop it. Central Banks will, at best, be able to slow it somewhat.

Having thrown the monetary "kitchen sink" at the problem and failed to fix it, Chinese Central Bankers are now actively engaging in verbal intervention (much as ECB President Mario Draghi asserted he would do "whatever it takes" at the depth of the EU Crisis in 2012).

> *Saturday, the People's Bank of China released a statement on its website seeking to calm the country's stock and currency markets and reassure the international financial community.* ***The central bank's posting, on the eve of the resumption of trading after a two-day holiday, contains Governor Zhou Xiaochuan's first public words directed to the Chinese public on the stock plunge, which began mid-June, and on Beijing's all-out response.***
>
> *Zhou's statement is in many ways remarkable. The central bank, by issuing its unprecedented opinion on the condition of the markets, has created a test of its credibility—and, by extension, a test of the credibility of the Chinese central government and the Communist Party. Price movements this week will undoubtedly tell us much about the direction of China's markets over the next several months.*
>
> ***Zhou, in comments summarized by the central bank, said the "correction in the stock market is almost done." He also predicted an end to volatility, saying the market will become "more stable."***
>
> *http://www.forbes.com/sites/gordonchang/2015/09/06/china-central-bank-stakes-credibility-on-unprecedented-statement/*

This smacks of desperation, recalling the famous line from EU President Jean-Claude Juncker, *"when it becomes serious, you have to lie."*

For now, however, the markets appear to be "buying" the lie, as we are seeing a bounce, or at least something of a consolidation period in risk assets.

As I noted in last week's market update, when collapses begin, there is usually a bounce to "kiss" former support as the bulls attempt to reignite \ lost momentum. It is only *after* the "kiss" (the bulls fail) that the real collapse begins.

With that in mind, we appear to be heading towards the "kiss" stage in the markets, particularly in Asia.

China has lead Asia lower. Having hit its long-term bull market trendline (dark red line) the China ETF (FXI) is now bouncing. It would not be unreasonable for it rally to "kiss" former support (the green line).

The same is true for Malaysia's stock market…

…as well as Singapore's…

…and South Korea's:

In the US, the Russell 2000, like China, has collapsed all the way to test its long-term bull market trendline (blue line). It is now bouncing to test former support (lower greenline). If it can break above this level, we could see a move to 1,200:

I realize that chart is not the easiest to read so the below chart shows a close up of the recent price action and the levels to which we could see a bounce.

A corresponding bounce would take us to 2,000 on the S&P 500. If we take out that line we could get to 2,075 or so.

The catalyst for this bounce will likely be hype and hope of the Fed postponing its decision to hike interest rates at its FOMC meeting next week (the 16th and 17th). Stocks have a history of rallying into Fed FOMC meetings, and with the market oversold, this is an easy excuse for the usual players to gun the markets higher.

We're positioned to prpofit from this with our UltraLong S&P 500 (SSO) and UltraLong Russell 2000 ETFs (UWM). But after that bounce ends, we're likely heading to new lows.

As I continue to note, stocks never go straight down, even when they enter a bear market. I've shown the below chart before, but it serves as a great reminder that when bubbles burst, you get numerous large double-digit bounces.

If we have indeed entered into a bear market, then we will be gradually working our way down over the coming months/ years.

My own view is that, as stated before, Central Banks will fight “tooth and nail” to hold the system up. With that in mind, we should acknowledge that at some point, if things become dire enough, the Fed will step in with another QE program.

I fully expect this would be somewhere around 1,400 on the S&P 500: the markets’ long-term bull market trendline (green line on the chart on the next page).

Finally, a number of you have written in to ask me about whether the Fed will be hiking rates this month or not. Honestly, I have no idea. And no one else does either (this includes the Fed Presidents, themselves).

Certain Fed officials have been stating that the Fed should commence tightening. However, with China's bubble collapsing dragging down the Emerging Markets, there are plenty of excuses for the Fed to postpone yet again.

Ultimately, I remain convinced that whenever the Fed *does* hike rates, it will largely be a symbolic rate hike, say to 0.35% or 0.5%. At that point the US will roll over into recession (helped by the deflation China is now actively exporting into our economy) and bonds will explode higher pushing yields to new lows. Timing when the rate hike will hit is impossible. But the fundamentals suggest we're rapidly moving into deflation.

This concludes this Weekly Market Update. I'm watching the markets closely and will issue updates as needed. Barring any new developments, you'll next hear from me next week in our usual Weekly Market Update.

Until then…

Best Regards

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