Titan Capital Management, LLC
Global Market Letter

July 1, 2016 **Abe Askil, CFP®**

BREXIT ROCKS FINANCIAL MARKETS

Global financial markets were completely caught off guard and did not price in the decision of voters in the U.K to leave the European Union. The European Union as we know it is most likely finished. The question now is who will be next to leave? The U.K.'s FTSE 100 stock index fell 3.2% last Friday, while France and Germany fell 8% and 7% respectively and Spain and Italy each fell over 12%. The markets are already starting to discount who may be next and where the most financial risk lies. The biggest risk lies with the European Banks which fell 16% to 33% during the two days following the vote. Many European banks such as Germany's Deutsche Bank hit all-time lows on Monday and are much lower than there were during the financial crisis in 2008. The Italian government is talking about using some kind of taxpayer guarantee to bailout its banks. The danger for investors is that a banking crisis turns into a full blown global financial crisis, which is pretty much what happened in 2008. Legendary hedge fund manager and Market Wizard Jim Rogers (who retired at age 37) believes that the next market crisis will be worse than 2008. Former Federal Reserve Chairman Alan Greenspan when talking about the Brexit vote said "This is the worst period, I recall since I've been in public service...there's nothing like it, including the crisis – remember October 19th, 1987, when the Dow went down by a record amount 23%? That I thought was the bottom of all potential problems. This has a corrosive effect that will not go away". Greenspan knows a thing or two about creating financial crisis, so his comments should not be taken lightly.

While the S&P 500 is getting close to its all-time highs again, many foreign stock markets are currently in bear markets. The following countries are officially in bear markets, down 20% or more from their peaks: China, Japan, Hong Kong, Singapore, France, Germany, Portugal, Italy, Greece, Spain, and Brazil. This is quite a long list and one has to wonder how much longer the U.S. market will buck the trend that is taking place globally? The chart below shows that the S&P 500 is once again trading above its 200-day moving average, but is still stuck in a trading range. The MSCI EAFE Index which includes stock indices from Europe, Australia and the Far East has been in a downtrend for the past year and a half and is below its 200-day moving average. This divergence between most foreign stock indices and the U.S. indices will not continue indefinitely, either the foreign markets will bring U.S. indices down or the U.S. indices will bring foreign markets up. I think we may have an answer as to which one it will be in the next few months.

2016 HAS A LOT IN COMMON WITH 2000 AND 2008

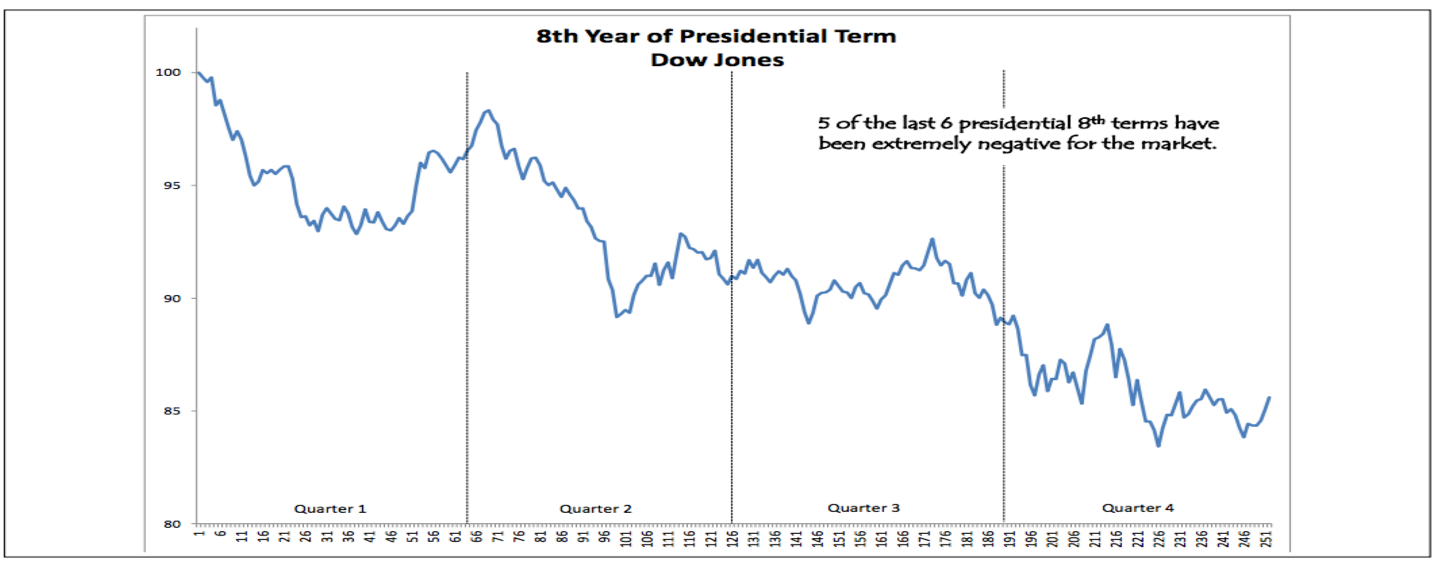
The last two bear markets occurred between 2000 to 2002 when the NASDAQ fell 75% and 2007 to 2009 when the S&P 500 dropped 55% from peak to trough. 2016 may have more in common with 2000 and 2008 than most people realize. Here are a few of the similarities and one big difference:

- Valuations are currently the second highest in history, higher than 2007 and approaching levels seen in 2000.
- The current cyclical bull market is over 7 years old and falls right between the 10 year old bull that ran between 1990 – 2000 and the 5 year bull that ran between 2002 – 2007. Both ended very badly.
- The 2000 and 2008 bear markets were both associated with a recession. Since 1945 the U.S. has experienced a recession every 5 to 6 years on average. The last recession ended 7 years ago, so the economy is long overdue for one. Most economic data has been weak, so it would not take much for the economy to enter into a recession.
- Like 2000 and 2008, it's an election year and specifically the 8th year of the Presidential Cycle. Going back to 1920, the 8th year of the Presidential Cycle has seen the Dow Jones Industrial Average fall 14% on average. Five out of the last six Presidential 8th terms have been extremely negative for stocks as seen in the chart below.
- Investor sentiment is overly optimistic and allocations to stocks are similar to levels seen in 2000 and 2007.
- Unlike 2000 and 2008, global central banks are out of ammunition and have limited ability to deal with a recession or financial crisis. Here is what Fed Chair Yellen said earlier this month, "If there were to be a negative shock to the economy…we don't have a lot of room using our traditional tried and true methods to respond."

Mark Twain said "History does not repeat itself, but it does rhyme". No one knows with any certainty if the next major bear market will start in 2016, but there are a lot of similarities to the last two bear markets. The chart below shows that historically the 8th year of the Presidential Cycle has not been good for stocks. Maybe this year will be different?

8th year of the Presidential Cycle Not Good For Stocks

Going back to 1920, the final year of a two term presidency has not been good for the market.



Source: Bloomberg Financial & FBN Securities

THE BOTTOM LINE

Our Omega equity trend model is positive and Alpha is negative. The market has started the summer off in a volatile manner and this may continue through the remainder of the year. Our exposure to gold and bonds has helped us hedge losses in our stock positions during down market days. Gold and bonds seem to go up substantially when stocks fall and are relatively flat or slightly higher on days that stocks rise. For now the combination of U.S. stocks, bonds and gold is working well in this volatile, range bound market. I hope you all have a Happy 4th!

1500 J Street Modesto, CA 95354 Bus: (209) 529-3089 Toll Free: (888) 378-0777 Fax: (209) 529-3081