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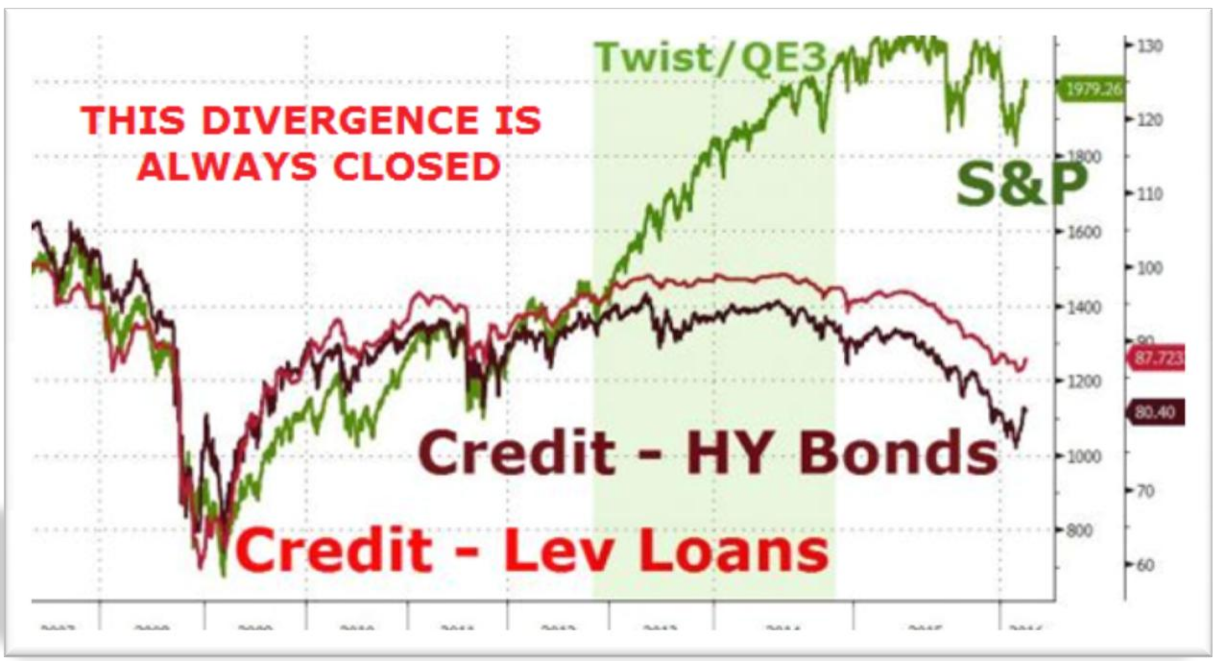
MORE DOWNSIDE THAN UPSIDE

Divergence Between Credit and Equities Will Be Closed!

ANALYTIC INSIGHTS



Gordon T Long
2/18/2016

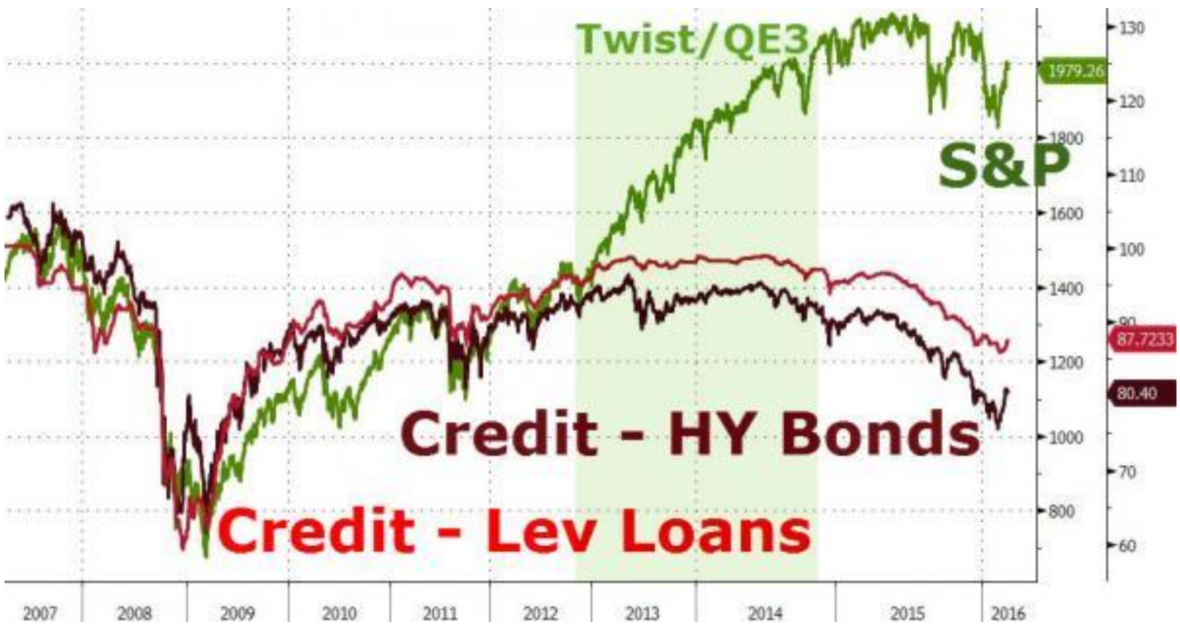
MORE DOWNSIDE THAN UPSIDE

Divergence Between Credit and Equities Will Be Closed!

The following is Jeff Gundlach's (DoubleLine) favorite chart which backs his perspective that equity markets have a:

"2% upside and 20% downside from here".

In his words: *"These lines will converge..."*



TREND CHANNEL IS NOW CLEARLY DOWN

The trend channel is now clearly down and ECB's Draghi may have ensured that with his March 10th policy announcement statement.

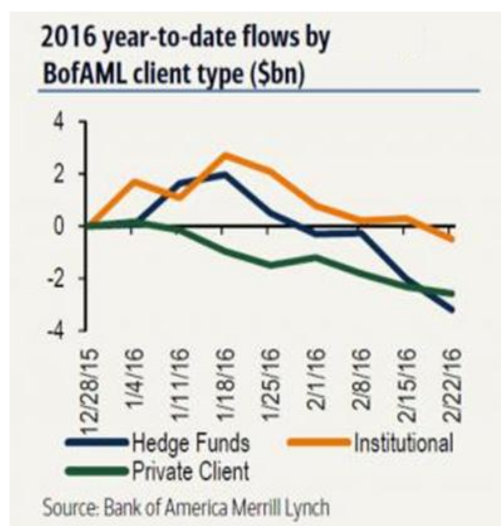
SMART MONEY

Despite the S&P's surge higher due to either

- A record short squeeze or
- Because it is merely another bear market rally,

… the smart money was selling! As reported:

> In fact, as BofA's Jill Hall calculated, the three groups that make up the so-called "smart money" basket, hedge funds, BofA's institutional clients as well its private clients, had been selling aggressively every week for the prior five. As she explained on March 1, "last week, during which the S&P 500 climbed 1.6%, BofAML clients were net sellers of US stocks for the fifth consecutive week, in the amount of $1.5bn. **This was the biggest weekly outflow since mid-December**." Someone clearly was very grateful for the selling opportunity that this squeeze was providing.
>
> Well, we can now add one more week to the total: in BofA's latest note, "**last week, during which the S&P 500 rallied 2.7%, BofAML clients were net sellers of US stocks for the sixth week.**"



> She explains that "similar to the prior week, hedge funds, institutional clients, and private clients were all net sellers, though sales last week were led by private clients (vs. hedge funds the week prior). **Our hedge fund clients remain the biggest net sellers of US stocks year-to-date."**

The full breakdown below:

> Clients were net sellers of stocks in five of the ten sectors last week and net buyers of the remaining five, as well as ETFs. Tech and the commodity-oriented sectors of Industrials and Materials saw the largest net sales, while Financials and Utilities saw the largest net buying... **All three client groups sold stocks last week, led by private clients."**

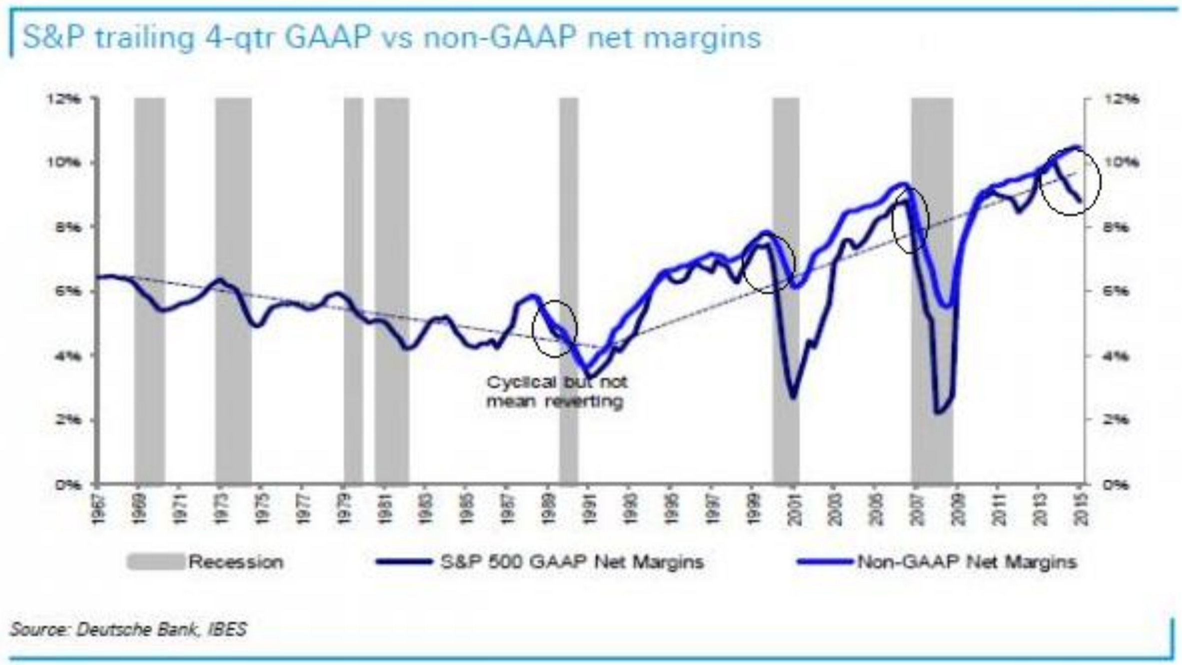
Chart 4: BofAML client total net buys: 4-wk moving avg ($mn) and S&P 500, 2008-present

Source: Bank of America Merrill Lynch

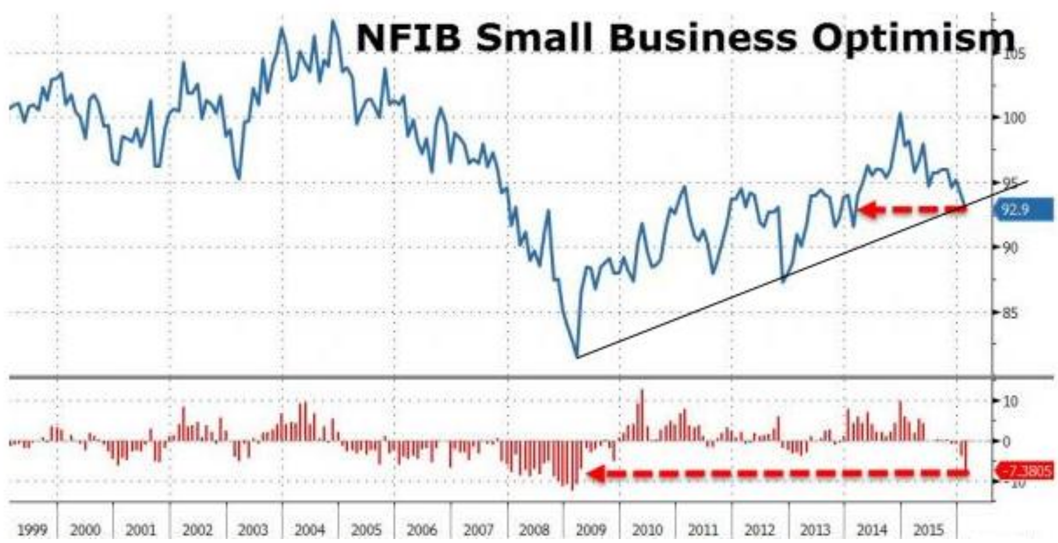
Table 1: Cumulative net buys by BofAML clients, 2008-present ($mn)

Sector	YTD 2016	2015	2014	2013	2012	2011	2010	2009	2008
Consumer Discretionary	1,107	(3,137)	(4,427)	(5,363)	(3,520)	2,180	(1,470)	(660)	(5,297)
Consumer Staples	(854)	1,072	(5,228)	(3,188)	(6,731)	(4,426)	(3,412)	(3,260)	(7,334)
ETFs	(1,296)	28,158	34,363	10,352	18,684	6,597	8,432	5,702	7,935
Energy	1,014	(1,230)	(4,074)	(3,193)	(5,323)	(933)	(4,290)	(1,970)	(8,694)
Financials	2,172	(858)	(5,408)	(4,591)	(2,248)	(1,730)	(4,734)	4,784	(2,257)
Health Care	405	(5,490)	(5,517)	(4,182)	(829)	2,243	(3,991)	(1,888)	(6,115)
Industrials	(474)	(3,036)	786	(1,616)	(1,699)	(653)	(1,576)	(91)	(6,736)
Information Technology	(2,495)	1,193	(3,128)	(2,468)	(1,217)	2,730	1,475	(4,355)	(6,177)
Materials	787	(3,479)	(1,229)	(3,527)	(3,045)	(1,783)	(1,270)	(413)	(1,068)
Telecommunication Services	717	596	3,223	1,743	(204)	690	(517)	365	(273)
Utilities	270	156	(636)	425	(808)	732	(893)	(461)	(1,622)
Client									
Hedge Funds	(3,478)	(2,434)	(4,683)	(3,417)	(2,085)	(5,695)	(4,456)	6,418	(1,223)
Institutional	(951)	(26,153)	(18,235)	(32,792)	2,668	1,493	(13,755)	6,088	(15,150)
Pension Funds	191	58	347	(1,271)	(115)	(354)	566	1,261	388
Retail	(3,212)	1,764	(13,205)	(18,800)	(39,973)	(23,049)	(25,999)	(23,361)	(21,266)
Retail ex. ETFs	(1,540)	(29,728)	(35,914)	(34,997)	(50,657)	(31,983)	(34,033)	(31,949)	(27,305)
Corporates	8,994	40,767	44,850	39,401	32,449	32,897	31,964	8,609	N/A
Size									
Large cap	(900)	665	4,815	(16,887)	(10,081)	4,480	(9,505)	(3,755)	(33,155)
Mid cap	1,887	9,329	3,991	2,151	3,050	237	(2,845)	301	(3,074)
Small cap	365	3,950	(80)	(872)	90	928	103	1,207	(1,410)
Total	**2,010**	**11,613**	**5,380**	**(21,136)**	**(7,919)**	**4,492**	**(11,659)**	**(2,758)**	**(50,817)**

Source: Bank of America Merrill Lynch

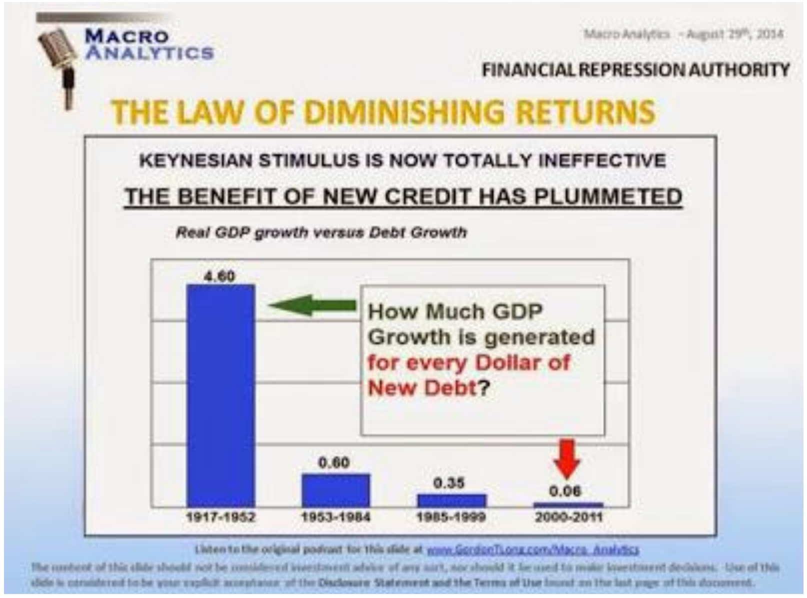


BUSINESS SENTIMENT BECOMING WORRYING



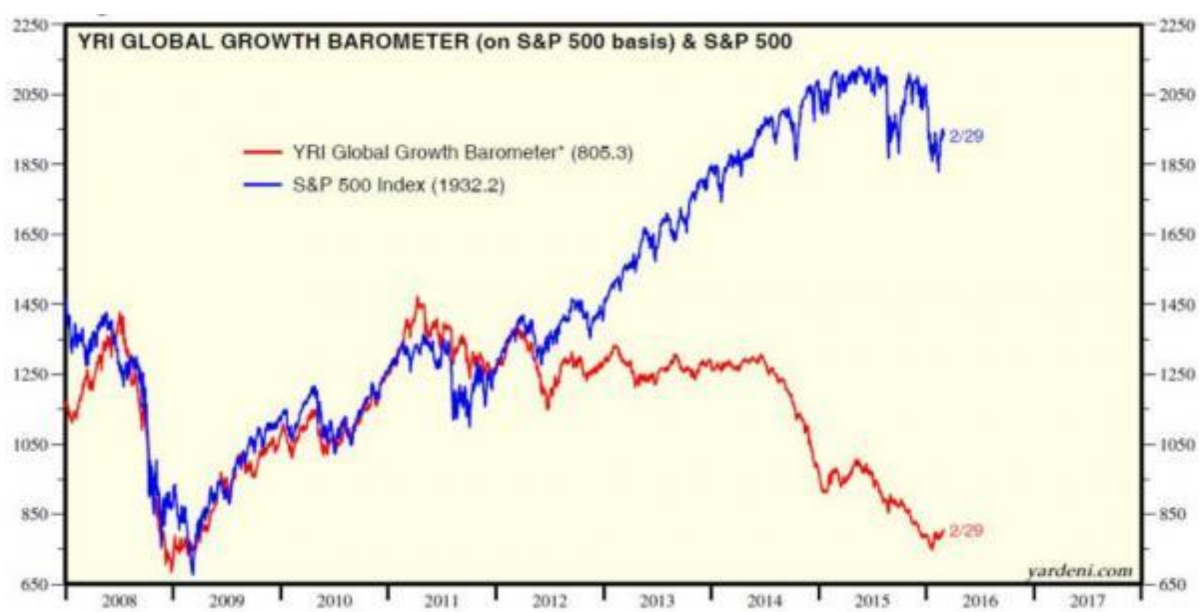
CENTRAL BANKS WILL REACT

We were very clear in 2011 that new credit was on the verge of becoming ineffective. We felt it would be convincingly negative by 2012.



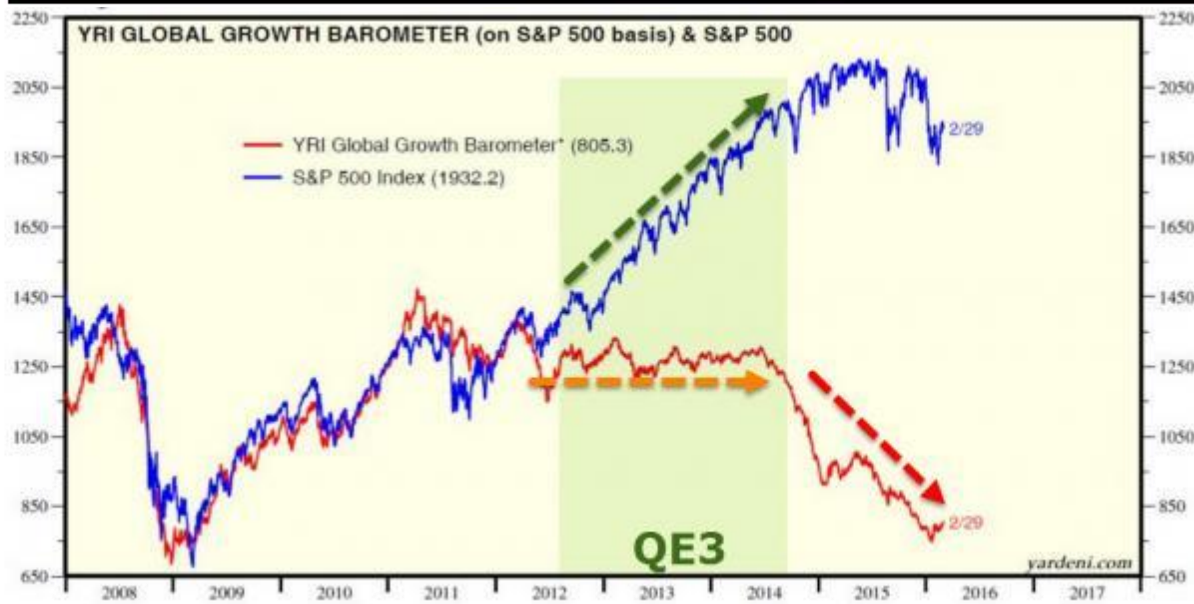
And if you need help spotting the moment when monetary policy became impotent...

Yardeni's YRI Growth Barometer versus S&P 500. *Note 2011 / 2012 turmoil.*



Source:Yardeni.com

Of course the Federal Reserve had no other option than to keep printing until the banks were solvent and loan collateral values were elevated.



This chart by Sprott Global is an approximation. It should be more accurately showing the drop in 2011 and 2012 but it tells the story effectively.

Chart B

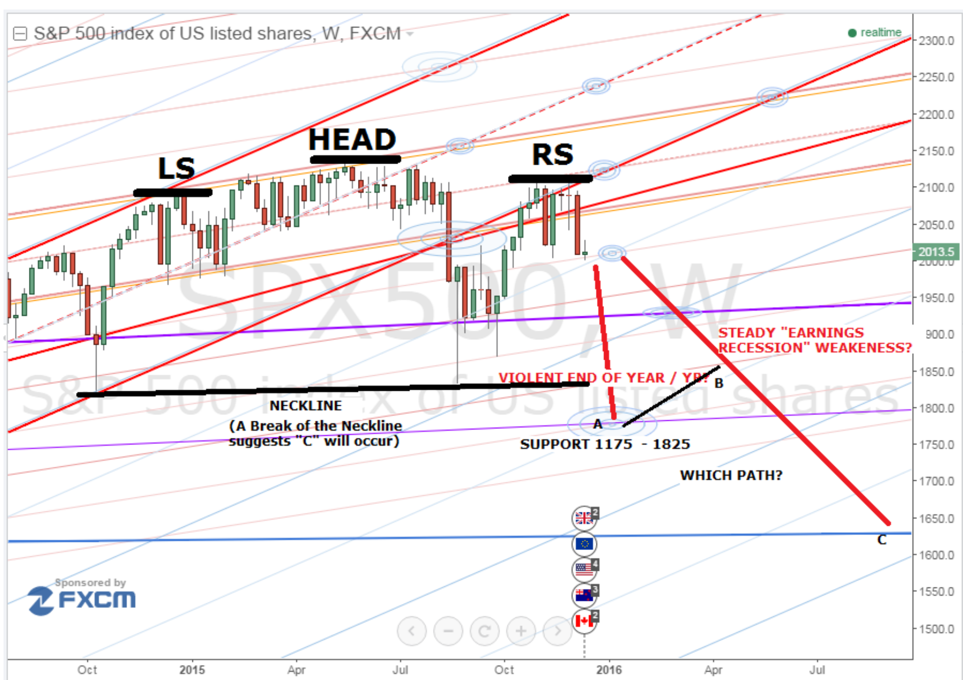
This is all you need to know about Keynesian Economics in an era of Fiat Currencies (Keynes would have been shocked at the removal of the Gold Standard) and the Era of Financial Repression (George Orwell and Aldous Huxley wouldn't be shocked!)

LOOSING FAITH IN CNETRAL BANKS

Gold Breaks Out

WE WARNED – *Expect a 'Violent Reaction'*

IN A PREVIOUS REPORT WE SHOWED THIS CHART – We Predicted "Violent YE"



LATEST CHART – It Was a "Violent YB"

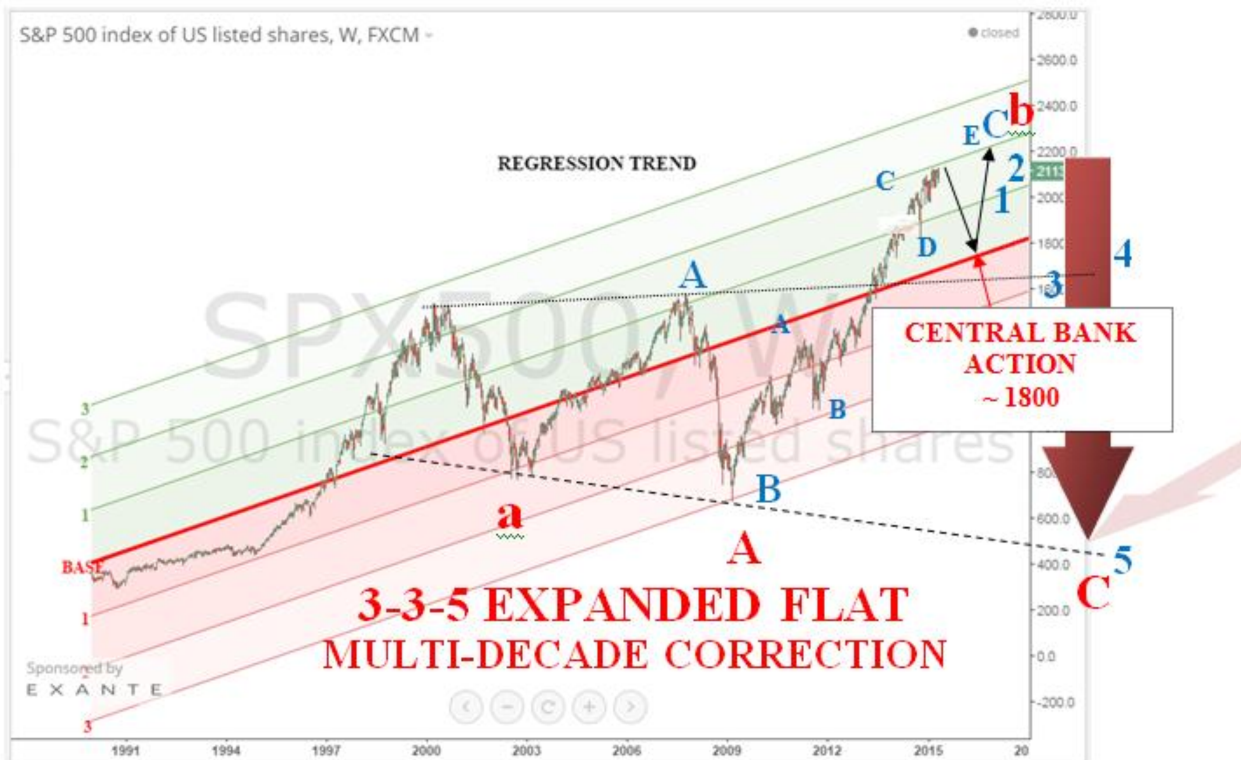
We were off slightly! It didn't happen on December 31st but instead on January 1st… and it was violent!

It was only a matter of time … and patience.

LONGER TERM VIEW

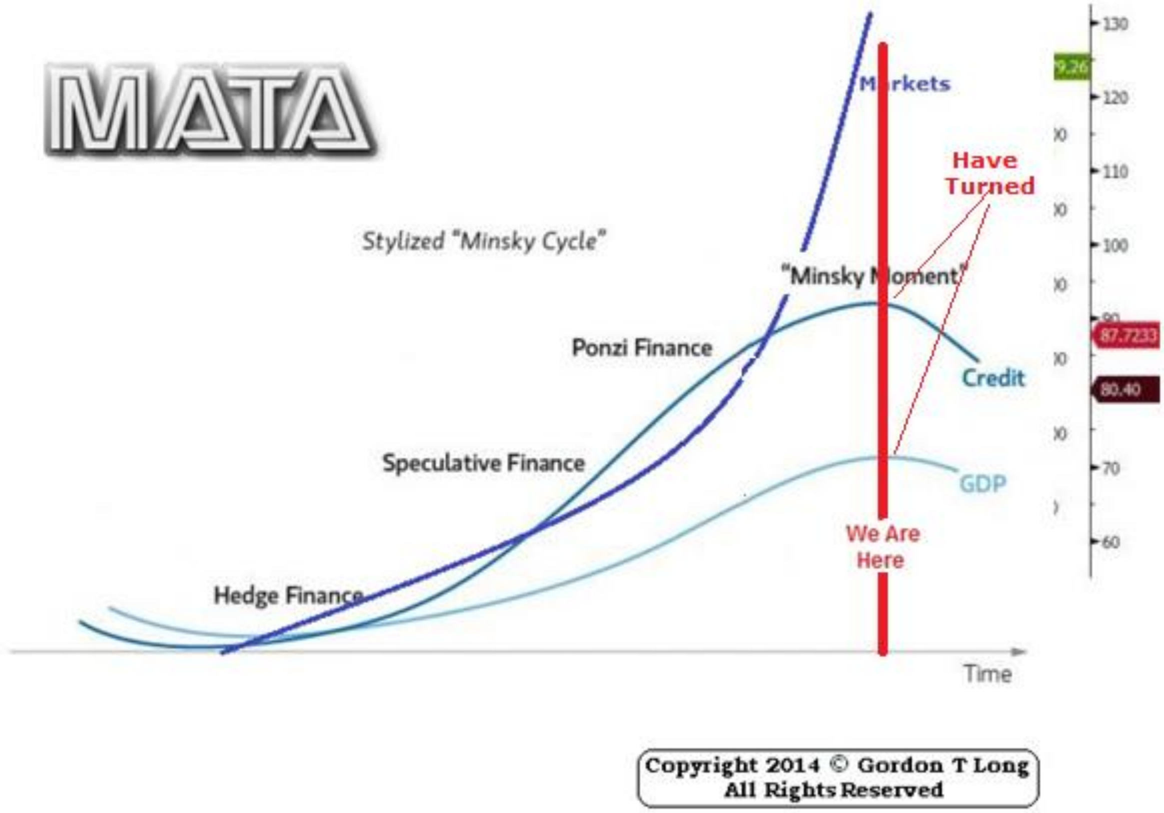
As we have laid out in previous TRIGGER reports, we still see more increases in the equity markets later in 2016 after this consolidation / correction has run its course, but have serious concerns beginning in Q4 2016.

Sometime in Q4 2016, after the central bankers have had one more shot at QE, helicopter money and collateral guarantees - it will end badly!



HAVEN'T CHANGED OUR POSITION

After the near term expected correction we still expect markets to head higher towards a "Minsky Moment" in 2016.



This is based on the assumption that Central Banks will react to any deterioration in the financial markets with yet another round of crisis driven liquidity pumping!

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