Hamilton-Bates

Market Update *September 24, 2015*

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Be Careful What You Wish For

The bulls bid up the market ahead of the September FMOC meeting hoping the Fed wouldn't hike rates and the market would rally. Well they didn't and it didn't. The consensus was split on if the Fed was going to hike or keep rates the same, but everyone was caught off-guard by how scared the Fed came off in their extremely dovish FOMC announcement. After all, it is **7 years later**, investors were looking for some confirmation that the economy is finally starting to pick up. Instead the Fed completely 'chickened out', deferring a hike due to what it called global events, meaning China. In short order the rebound rally that had been building over the prior two weeks faded.

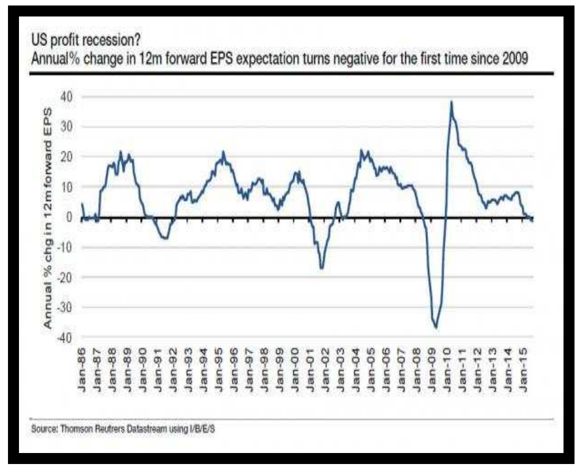
The Fed

After talking tough on rates for months the Fed blinked when it came down to actually moving off their long-running zero interest rate policy. Proving itself deathly afraid, and devoid of leadership, the Fed didn't want to ruffle the markets by doing anything because it might somehow derail the economy. The fact that they couldn't move a quarter point due to foreign concerns is what truly worried the markets. Now investors want to know what does the Fed know that makes it so afraid to hike?

Seven years later no one can figure out under what conditions the emergency that led to this extreme monetary policy in 2008 might be deemed over, or why an economy this long into 'recovery' can't stand even a quarter point hike. And since when does the Fed determine interest rate policy based on what is happening in China?

Economy and Earnings

The economic data released since the FMOC meeting does support the Fed's decision to hold, as now we



have six regional Fed reports that have come in worse than expected, and show a clear slowing in the economy. Earnings have been poor, with revenues and per share earnings growth slowing markedly. The above chart shows just how far forward earnings expectations have fallen- turning negative for the first time since 2009. **The last three times forward earnings turned negative the economy was soon to be in recession**.

Market and Investment Outlook

Its not the news itself per se, but how the market reacts to it that matters. Sometimes the market rallies on 'bad' news and sells-off on 'good' news. The market's response to the Fed decision was fairly stunning. We have seen a nearly 800 point drop since a very dovish FMOC announcement. This confirms something is very wrong with the global economy, or at least the market fears there is.

For now, with the trend action poor and with breadth and volume measures not supportive of a sustained rally, managed accounts continue to hold a larger than usual amount of cash along with bonds—which have

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held up very well. We suspect the current correction will run into October, with the market still needing a true re-test or even undercut of the August low to set up a more lasting rally into year end. We will look to position long assets into a decline which takes the S&P below the August low, and a buy signal would be triggered in a drop below the August low with a subsequent move back above it.

The 1820-1870 area looks like the ideal spot for the low to develop. From there we could see a 10-15% move higher into year-end.

Market Charts

S&P Short-Term Chart (Top)
The bounce from the August low has been choppy with overlapping moves, suggesting it is a bounce rather than a new uptrend. A lasting low could be seen if the market re-tests or even slightly breaks the August low, thereby washing out all the remaining selling pressure. **A decline below 1867 followed by a move back above it would be a near-term BUY signal.**

S&P 500 Long-Term (Bottom)
The monthly S&P chart is definitely at risk of rolling over into a pronounced correction, a move back above the 10-month average is needed to suggest a renewed uptrend. In the prior two breaks which were just pauses (circled in chart), the LOW was in the 3rd month below the 10 month average—which would be October. This suggests we could see a low of some significance next month. Caution until then.