INSTITUTIONAL ADVISORS
original independent financial market forecasting since 1980

BOB HOYE

PUBLISHED BY INSTITUTIONAL ADVISORS

SEPTEMBER 7, 2017

Don't Let the Smoke Out

This article is not about wildfires in California and the Pacific Northwest.

It is about cars and speculative financial markets.

When tinkering with old cars it is best not to go near the wires as there is weirdness there. The red ones are definitely taboo. But if you must fiddle with them, be careful not to let the smoke out. The engine will not run. Sometimes the smoke will come out all on its own – same thing – the car won't run.

A good thing about new cars is that you can't see the wires. What you can't see, shouldn't worry you. So, new cars run forever. [1]

Because they are not widely watched, the wires in the financial markets are not worrisome either. With no visible threats, bull markets run forever.

With always outstanding corporate management and the genius of the Fed, adversity is limited to setbacks.

Although not familiar with the smoke theory, quite likely the Fed is doing everything it can to keep the smoke in.

Fortunately, there are technical measures that are warning that the financial wires are getting very hot. The hottest since 2007 and 2000. Bubbles, in any century, are dangerous and failure has been signaled by changes in the credit markets.

What about the climax of this bubble?

Most of the great stock bubbles have clocked a regular timing pattern. 2017 is the year that a great bull market could become hot enough to conclude. Since the advent of modern financial markets by 1700, most of the great stock bubbles have concluded in the ninth year after the climax of a great speculation in commodities.

This history would not be put forward if there weren't signs of excessive speculation (✓) in the ninth year of the equivalent in commodities (✓). The big high in commodities was in 2008.

---

[1] A story from the late 1920s is worth passing on. Back then cars were unreliable and a common question was, ***"How is your car running?"***.
A jokester responded with, ***"It is running so well it takes two mechanics 15 minutes just to turn it off"***.

Beyond the warnings providing by financial wires getting hot, there will be some flashing hazard lights.

One has been that the First Breakout on the change to widening credit spreads which occurred in early July. This hazard light is flashing. The Second Breakout occurred in August and has been modest. Despite this, big smoke is possible.

Also, key would be the yield for the T-bill rates turning down. The increase was from 0.16% in January 2016 to 1.18% in late July. The latter part of the rally was strong enough to register technical excess, the highest in a decade. Another hazard light.

Declining to 1.00%, took out the 50-Day at 1.04% which has likely ended the uptrend. It is testing the high now and the formal breakdown would indicate the start of the contraction. All post-bubble contractions have been brutal.

As these change, market confidence could change to apprehension when comfort could be found in talking about a “Fed cut”. Treasury bill rates in the senior currency go up with the boom and down with the bust.

Every time.

Monitoring these basic changes in the credit markets worked well for us in 2007 and in 2000.

The problem with financial wires has been that when the smokes gets out it not just from one wire. It suddenly gets out everywhere and the contractions have been proportionate to the degree of preceding speculation.

All the great bubbles suffered forced liquidation in the fall of the climax year.