INCISIVE INVESTOR

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WEEK IN REVIEW
MARKETS TAKE A ROLLER COASTER RIDE

Review of the week ended February 9, 2018

- **US markets are all down for the week & year**
- **Government shutdown avoided**
- **Foreign markets are participating in downturn**
- **Major company market moves**
- **Special market commentary**

U.S. bounced back from correction territory to close higher on Friday but the market still posted hefty losses for the week. All main indexes rallied in the afternoon with technology, real estate and energy sectors leading the gains.

The Dow rose 335 points, or 1.4%, to close at 24,196 for a weekly drop of 5.2%. The S&P 500 climbed 38 points, or 1.5%, to end at 2,619, down 5.2% for the week, while the Nasdaq Composite Index advanced 97 points, or 1.4%, to 6,874 but posted a weekly loss of 5.1%.

Dow, S&P 500 and Nasdaq have biggest weekly percentage drop since January 2016 during one of the most frenetic stretches of trading on Wall Street. According to financial blog SentimenTrader, Thursday's drop marked the Dow's fourth-fastest decline into correction territory from an all-time high, based on data that goes back to 1897. The Dow has suffered a pair of 1,000-point drops this week, including in Thursday's session, something that has never happened in history.

The CBOE Volatility Index VIX also switched between gains and losses and closed 13.2% lower at 29.06. The so-called "fear index" has more doubled so far this year; the S&P has undergone seven sessions with a 1% move in 2018, nearly equaling the number of such moves seen over the entirety of 2017.

Gold futures settled 0.3% lower to $1,318.10 and marked the steepest weekly

decline in two months while crude-oil futures dropped 3.3% to $59.05 settling below $60 a barrel for the first time this year.

The yield on 10-year Treasury notes rose to a yield of 2.86%. The ICE U.S. Dollar Index moved up 0.3% to 90.477, marking its biggest weekly advance since 2016.

Congress votes to approve 2-year budget deal and end government shutdown

The House of Representatives voted early Friday for a two-year budget deal that raises both defense and domestic spending by hundreds of billions of dollars, approving a package that would also reopen the federal government after it shut down just past midnight. The House

followed the Senate in approving the sweeping bill, which would also suspend the debt limit through March 1, 2019. President Donald Trump tweeted that he signed the bill, which reopened the government.

Foreign Markets

European stocks suffered their worst week in two years, while Wall Street's late plunge hit Asian markets hard, with several indexes posting their worst week in years. FTSE 100 was down 1.09% on Friday. The Shanghai Composite Index closed down 4%, after losing as much as 6% in the session, while the Nikkei 225 index dropped 2.3%.

Major Company Moves

Energy shares were among the worst hit. Shares of Baker Hughes (BHGE) dropped 3.6%, while Schlumberger NV (SLB) slid 3.3%. FireEye Inc. (FEYE) shares surged 9.4% after the software-security company posted its first quarterly profit. Nvdia Corp. (NVDA) shares surged 6.7% after upbeat earnings and shares of Mattel Inc. (MAT) rose 7.9% after the toy maker appointed a new chairman. Nike (NKE) was up 4.8% and Dollar Tree rose 5.95% as well. On the downside, Expedia Inc. (EXPE) plunged 15.5% after a wide earnings miss and its rival TripAdvisor Inc. (TRIP) shares fell 4.3%. Chipotle Mexican Grill (CMG) edged lower by 3.97%.

SPECIAL MARKET COMMENTARY
WHAT HAPPENED, WHAT'S GOING TO HAPPEN?

What is causing the turmoil in the markets?

Two sources are climbing bond yields and higher inflation. These have been partly to blame for igniting once-dormant volatility in the market, with investors already on edge over lofty equity valuations following a mostly straight uptrend for assets perceived as risky.

There is another factor as well- emotions. "Right now markets are moving more on the emotions of trading, rather than economic fundamentals. Once the fears get rolling, it's purely sentiment and what traders can imagine in terms of where things can be going that drive price action," said Bruce McCain, chief investment strategist at Key Private Bank.

In addition, there are program and algorithm trading platforms that automatically start buying and selling when the markets move so much in a certain direction within a certain time frame. These typically push a down trending day further down and up trending days higher adding to market volatility.

A further contributor to the turmoil this week has been hedge funds and institutional traders employing strategies that trade on market volatility using various instruments that are tied to the movement in the VIX. Notice this note from CNBC: "The e-mail arrived in clients' inboxes shortly after the market opened on Tuesday: "LJM strategies have suffered significant losses." LJM Partners, a Chicago-based hedge fund with about half a billion dollars in assets, pinpointed the damage on spiking volatility, a trade that has claimed more than one scalp in the last few trading days. Their mutual fund, known as the LJM Preservation and Growth Fund, collapsed by 82 percent over the last week and was closed to new capital on Wednesday.

Investors in the industry are calling LJM among the most prominent funds to fall victim to the popular "short vol trade." The trade had become profitable for many

hedge funds, including LJM, whose "Preservation and Growth" fund posted positive returns every year except one since it launched in 2006, according to fund documents.

But the risk amplified this week after the CBOE Volatility Index, or VIX, more than doubled on Tuesday to the highest levels in six and a half years. The move caused an exchange-traded note called the VelocityShares Daily Inverse VIX which was betting on continued calmness in the markets, to collapse in after-hours trading on Monday. Subsequently, Credit Suisse, which issued and managed the ETN announced that it would ultimately be liquidated." Perhaps the biggest question on Wall Street right now is whether the recent pain in the U.S. stock market is over. If history is any indication, the answer is no.

WHAT ARE THE STRATEGISTS SAYING?

Park 10 Financial

We at Park 10 Financial note that most of the "experts" feel that the market may go down another 5-10% but then should bottom out. Some even think that in the next day or two it could rebound back to close to its high. But no matter what the commentators say, we will be diligent in watching for the interests of our clients.

Using our technical analysis tools we had our clients exit the market on Monday so it doesn't really matter how much further the market drops, our clients are not going to be affected. We will be looking for our indicators to give us a new entry point when market conditions warrant it.

Bespoke Investment Group.

Both the Dow Jones Industrial Average and the S&P 500 entered correction territory on Thursday, defined as a 10% drop from a recent peak—in this case, record highs that were hit in late January. According to

Bespoke Investment Group, which analyzed the 95 corrections the S&P has seen since 1928, investors might want to brace themselves for more pain. Per Bespoke's data, the median decline for the S&P in a correction is 16.4%, and the median length of a pullback is 64 days. Were the S&P to hit that median in the current selloff, it would bottom around 2,400, or roughly 7.8% below current levels.

"Keep in mind, though, that these are median levels. There have been a number of corrections (13) that saw declines of less than 11%, while several saw deeper declines of more than 20%," the research group wrote in a blog post. A decline of 20% would put the index into bear-market territory, where nearly one-fifth of the S&P components currently trade. "In terms of length, prior corrections have also been all over the map. Some have lasted as little as three days, while others have stretched on for well over a year."

"If we look just at the post-WWII period, there have been 55 corrections in the span of 73 years, reducing their frequency to once about every 16-17 months. In any event, the market was still overdue for a correction heading into the current one, but maybe not by as much as it seemed on the surface," Bespoke wrote. The research firm didn't give any indication about when it expected indexes to return to record levels, writing, "Unfortunately, there is no hard and fast rule when it comes to corrections, and that's what can make them so terrifying when you go through one. You never know when it will end."

Renaissance Macro Research

The stock market's turn from borderline euphoria to full-blown correction was swift and unsettling, but it isn't completely unfamiliar territory, according to one of Wall Street's top technicians. Jeff deGraaf, chairman of Renaissance Macro Research, said his firm has a program that looks at price changes for the S&P 500 index over the last-12-month period and then compares them to rolling 12-month historical returns to find the highest correlation with current market action.

In a Friday note, he said the closest match, or analog, is the March 1996 to March 1997 period, which had a .94 correlation (a reading of 1.0 would be perfect correlation). That should provide some comfort to market bulls, but it comes with caveats. "Today's price action is weaker over a shorter period of time than that of '96, and then, as we suspect happens today, the market needed a few weeks to convalesce before resuming its uptrend. When we aggregate the price paths of the top 25 correlations with today, the picture suggests a pause of a few weeks and resumption of trend," deGraaf wrote.

Frank Cappelleri

Capperlleri, an equities trader at Instinet, LLC said "I don't see any signs that it is over.As of Thursday's close, the [S&P 500]

was down 8.5% over the last five days. That's the worst five day move since Aug. 25, 2015. Over the last three decades, down moves this swift have been rare."

Cappelleri points out that recent corrective episodes haven't necessarily meant an end to a bull market. "The 2015 edition was the first 10% drop in over three years when it happened. While a second, harsher, round of plummeting prices popped up a few months later in early 2016 which was followed by a two year rally." That said, the analyst warns that history may mirror the past but is seldom the same. "The 2007-2009 period produced a similar scenario- the worst days eventually led to an epic turnaround, but not before wreaking havoc on the financial world first."

Bankrate.com

Greg McBride, chief financial analyst at Bankrate.com notes "Correction territory doesn't mean we'll see an immediate rebound. A total decline of 15% wouldn't be out of the ordinary and would send a very clear buy signal. I would be surprised to see the S&P 500 fall more than 20%. People have been chasing the market

Park 10 Financial

Now you have read a number of analysis' opinions of the situation. What really matters is whether your portfolio has been made "crash-proof" or not. If yours hasn't been, contact us and let us show you how we can substantially limit your exposure to market downturns and give you peace of mind.

-**Randall Fielder**

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