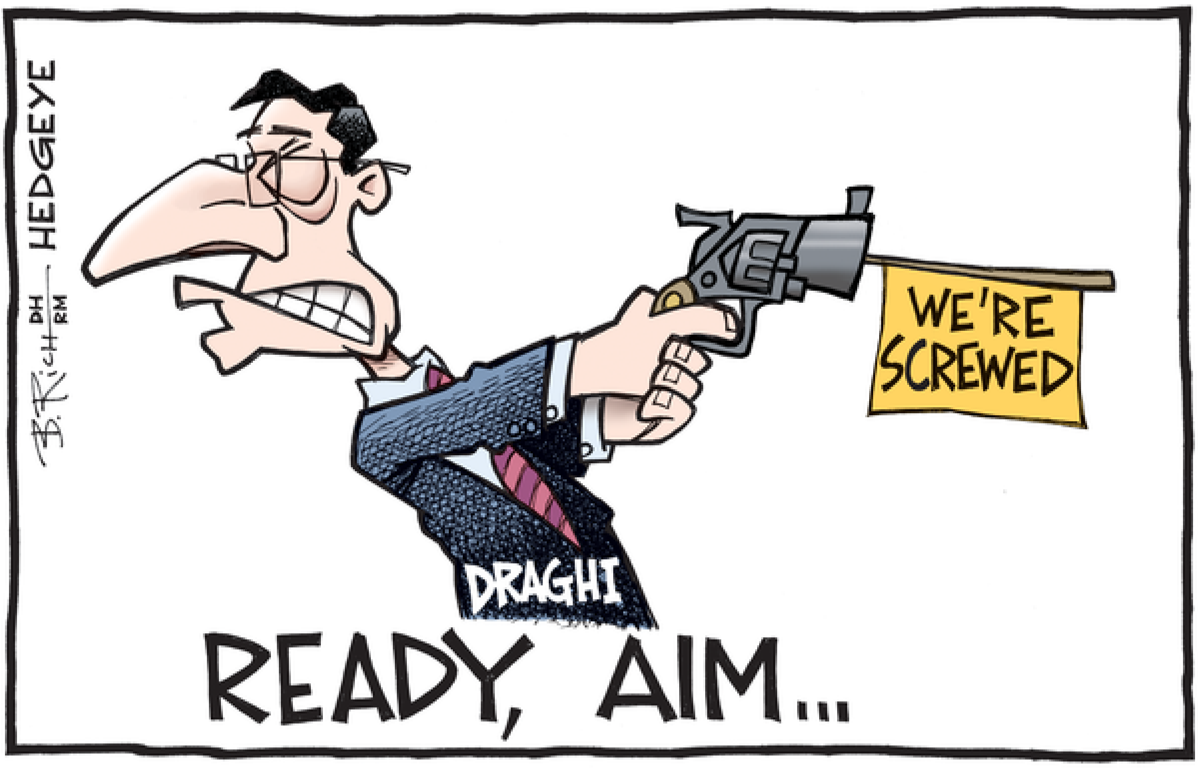
Make sure you are following me on social media for daily updates, announcements, and commentaries. (Twitter, Facebook, Linked-In)

REGISTER NOW FOR RIA'S FINANCIAL PLANNING WEBINAR SERIES

Retiring? Laid-off due to oil crash? Job change?



planning.

At the

beginning of this year, I began discussing the technical weakness that was emerging in the markets. **Since that time, the markets have remained under pressure leading to a continued cautious portfolio stance.** However, I have reiterated many times since then, **interventions by Central Banks could change the shorter-term dynamic of the markets from bearish back to bullish.** This past week saw exactly that as the European Central Bank not only intervened in the financial system but threw everything at its disposal at it. •As noted by[Ambrose Evans-Pritchard:]()

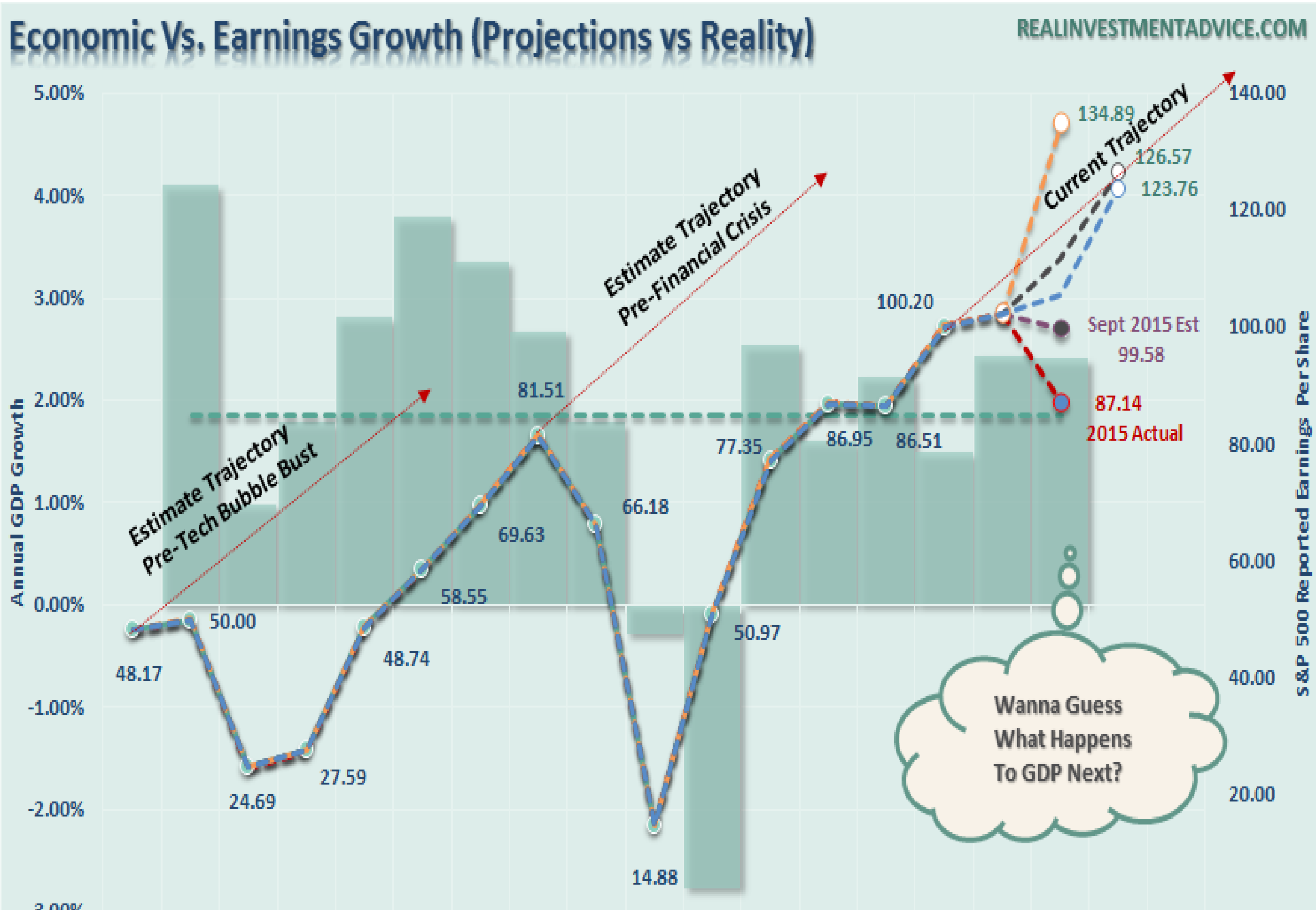
> "Mr. Draghi pledged **to flood the financial system with fresh liquidity for as long as it takes to keep the fragile economic recovery alive** and prevent a deflationary psychology taking hold, yet there was a sting in the tail. Marc Ostwald, from Monument Securities, said the ECB has bet everything on one last throw of the dice. **'It?s a kitchen sink job, but at the same time Draghi is saying there is a limit to what they can do, that this is it,** and there will nothing more,' he said."

The question, of course, is whether the ECB's interventions will be able to change the longer-term dynamics in the Eurozone by creating inflationary pressures and sparking economic growth? **That answer is likely *"no"* as it has failed to do so in the past, not only in the Eurozone but also in Japan and the U.S.** While I am going to spend most of this week's missive re-evaluating the technical underpinnings of the market, I want to start with a quick review of the fundamentals.

EARNINGS STILL RECESSIONARY

[As I noted earlier this week,]() corporate earnings continue to deteriorate.

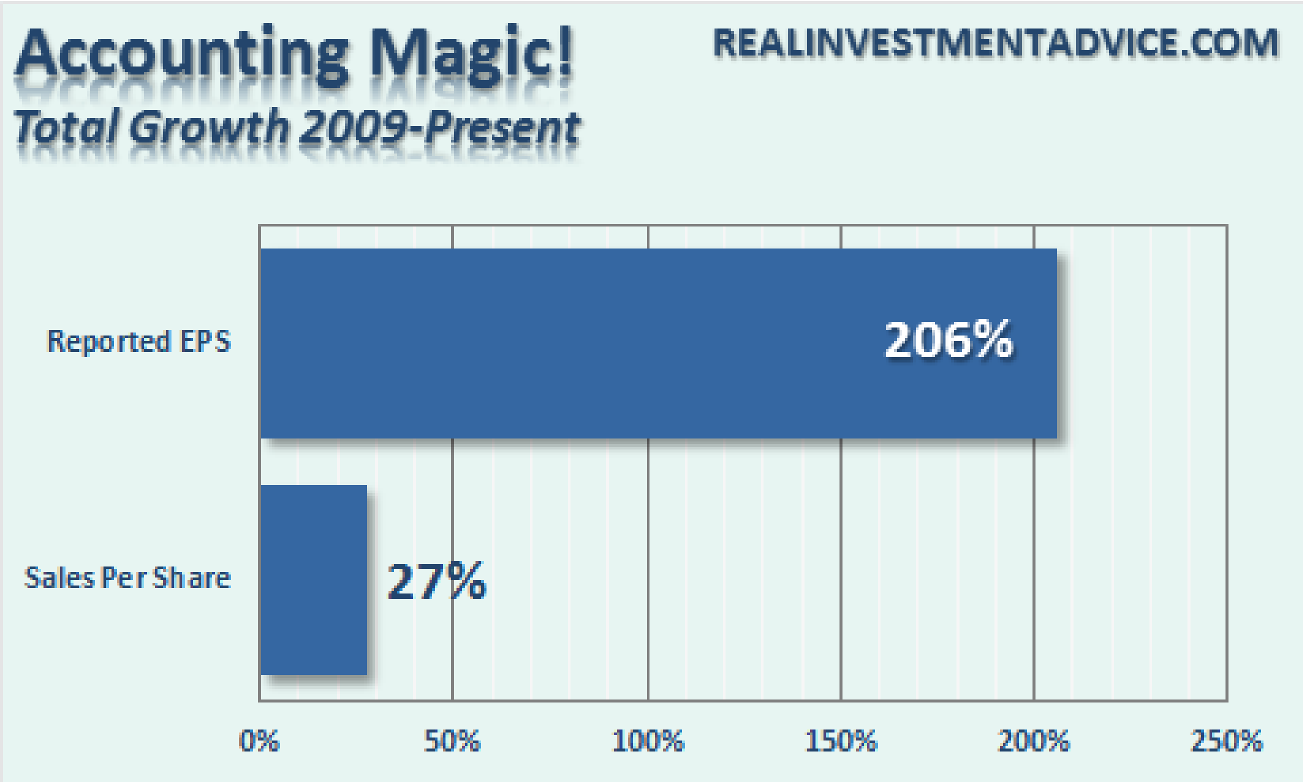
> "The chart below compares economic growth to earnings growth. As shown above, Wall Street **has always extrapolated earnings growth indefinitely into the future without taking into account the effects of the normal economic and business cycles.**•This was the same in 2000 and 2007. Unfortunately, the economy neither forgets nor forgives."



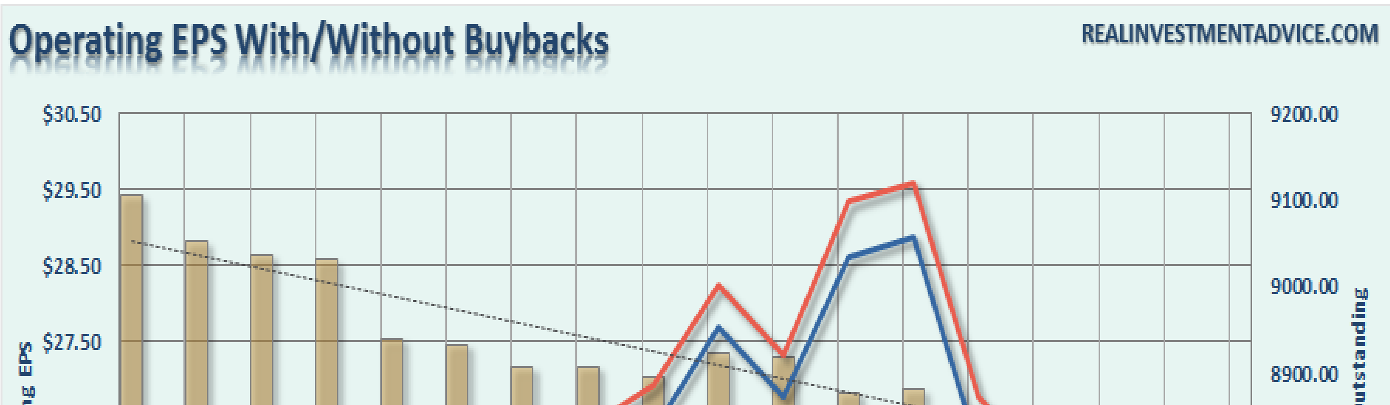
"Unfortunately, it is only a function of time until the next economic downturn takes hold, particularly given the currently weak global outlook. As shown, earnings tend to cycle regularly between 6% peak to peak and 5% trough to trough growth in earnings. **In 2014, expectations exceeded the current 6% peak to peak growth rate. I said then that it was only a question of what will trip up such overly optimistic picture.** We now have that answer and real earnings have fallen far short of those original estimates."

More importantly, despite ongoing Central Bank interventions which•boost asset prices and•acts as a huge wealth transfer tax from the middle class to the rich, corporate earnings are a direct reflection of what is happening in the actual economy.

"Since 2009, the reported earnings per share of corporations has increased by a total of 206%. This is the sharpest post-recession rise in reported EPS in history. **The problem•is that the sharp increase in earnings did not come from a similar surge in revenue that is reported at the top line of the income statement.** Revenue from sales of goods and services has only increased by a marginal 27% during the same period."



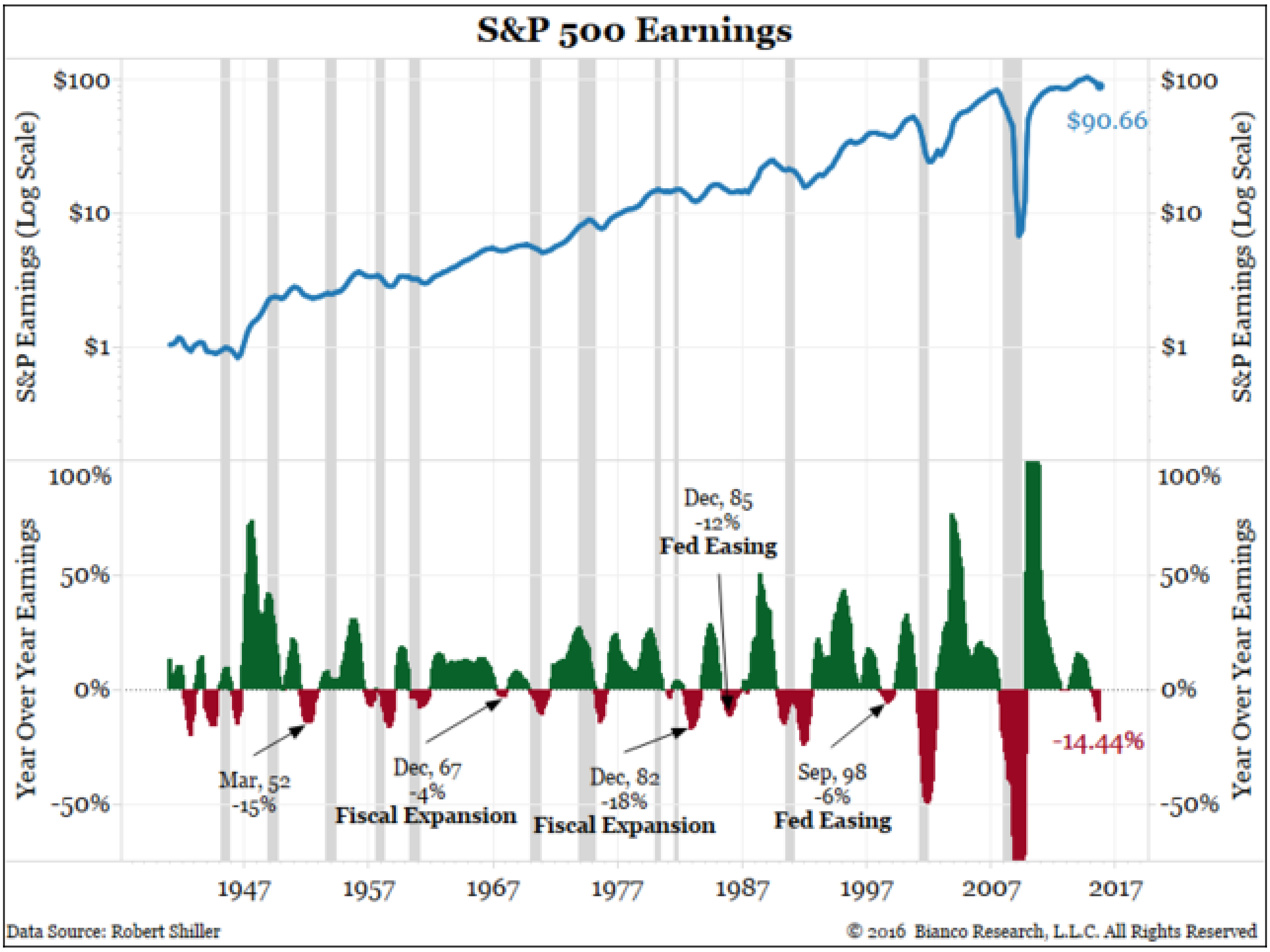
"For profitability to surge, despite rather weak revenue growth, corporations have resorted to using debt to accelerate share buybacks. The chart below shows the total number of outstanding shares as compared to the difference between operating earnings on a per/share basis before and after buybacks."



"The problem now is that despite share buybacks, earnings are no longer growing."

James Bianco from Bianco Research also notes:

"Our chart below starts in 1940 and shows Standard & Poor's 500 Index earnings in the top panel and their year-over-year change in the bottom panel. The shaded areas highlight the 12 recessions over this period."



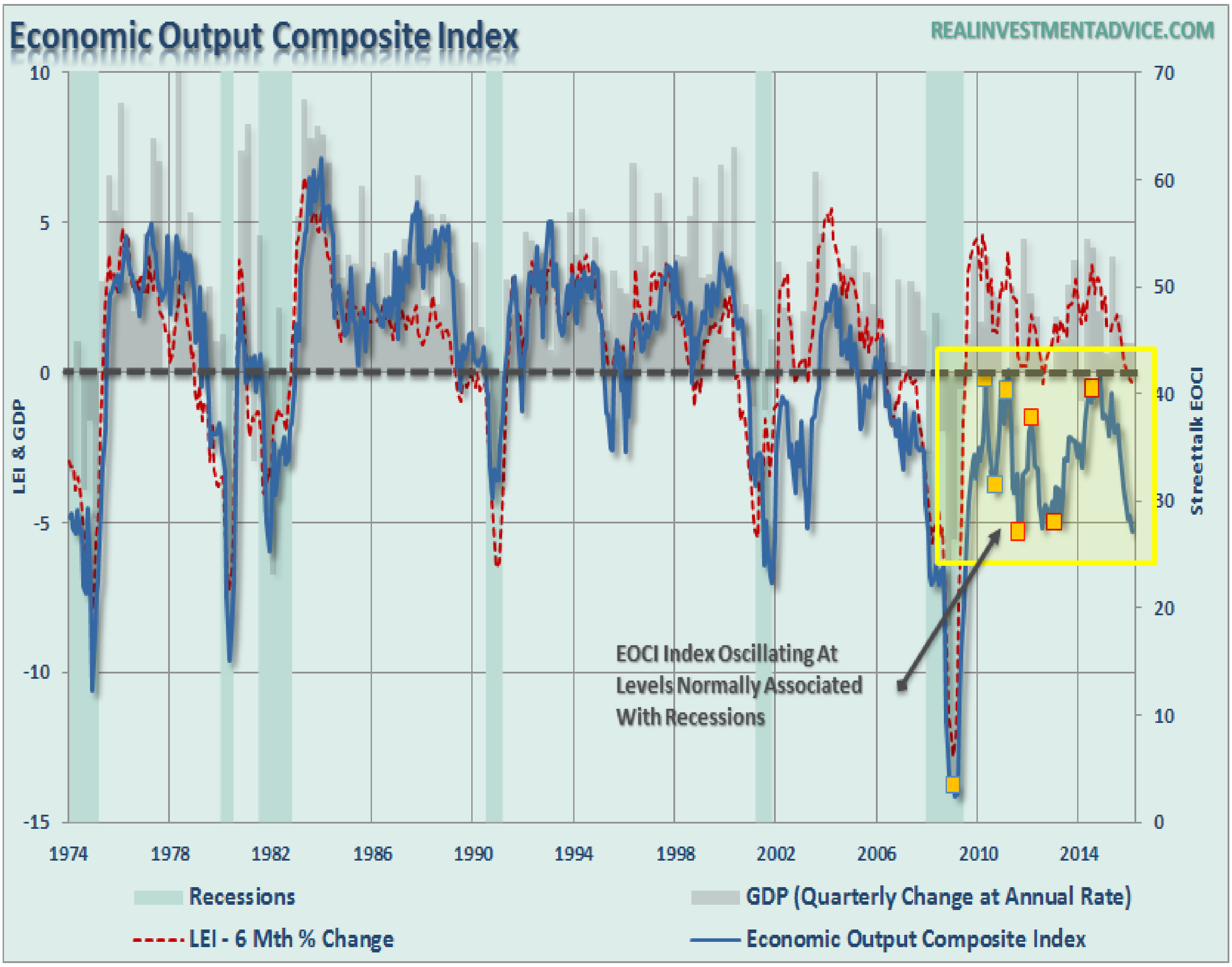
"**Earnings turned negative either during or just after all 12 of these recessions.** This should come as no surprise. Also noted on the chart are the five instances when earnings turned lower *(at least two consecutive quarters)* without a recession. **Hence, the last time earnings turned lower without a recession, Fed easing or fiscal expansion was in 1952. So if we are going to be in a period of negative earnings in the absence of any of these, it would be the first time in more than 63 years.**"

The point here is that Central Bank interventions likely can not fix that problem in the longer term. **While liquidity injections have the ability to *"Rob Peter To Pay Paul"* by dragging forward future consumption,** it continues to enlarge the future consumption void when it inevitably arrives.

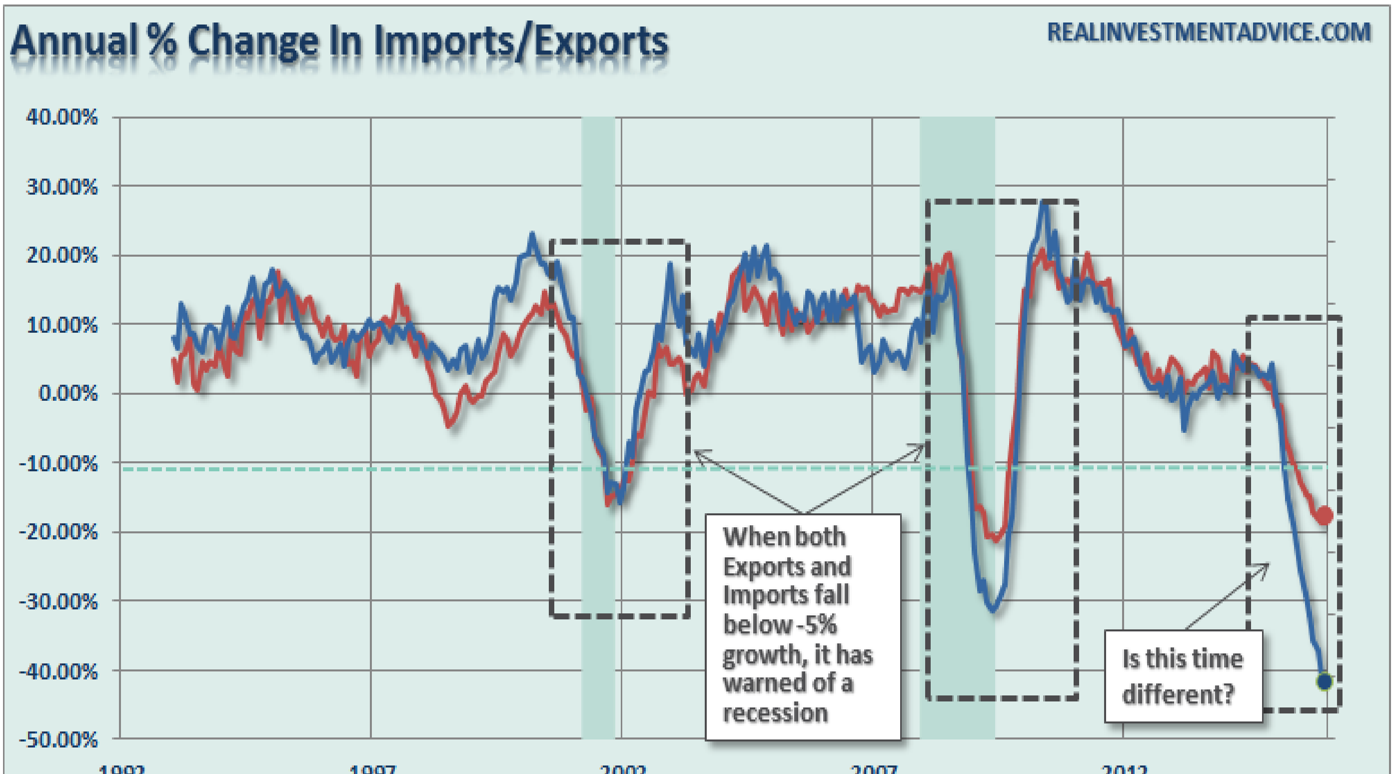
ECONOMIC DATA NOT MUCH BETTER

The economic picture, not surprisingly, is not doing well either and, as stated above, is being reflected in current earnings growth. While many pundits have tried to suggest *?this time is different?* because the *?service?*•sector has not fallen into contraction, this may be presumptive as the?*trend?* of the data•suggests this is not the case.

The same can be seen in the **Economic Output Composite Index (EOCI)** which is comprised of a variety of broad indices including the Chicago Fed National Activity Index, Chicago PMI, several Fed regional manufacturing surveys, ISM composite, NFIB survey and the LEI. **The last three times this index has fallen towards these current levels the Federal Reserve intervened.•**



Lastly, imports and exports are the *"blood"* in the veins of both corporations and consumers. Exports make up roughly 4o% of corporate profits and imports show the strength of consumer demand. See any problems here?

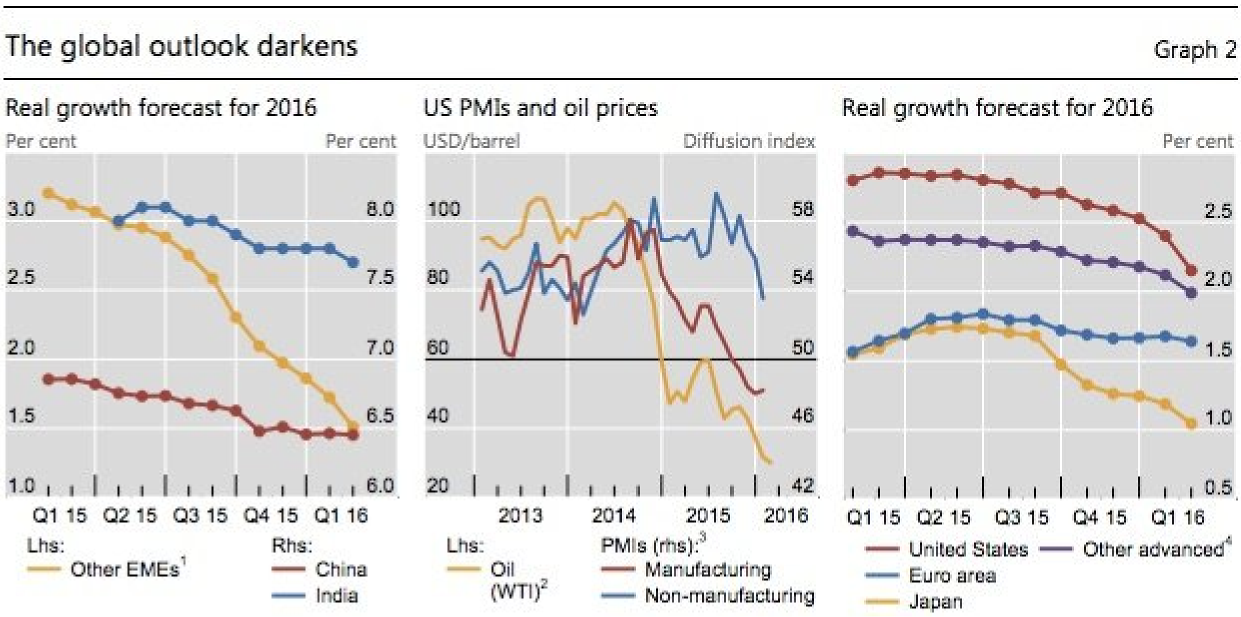


Interestingly, even the ECB understands that liquidity interventions will not be effective in the long-term. As noted by [William Watts at MarketWatch]() this week:

> "**With the effectiveness of monetary policy 'clearly diminishing,'**•Draghi**'threw down the gauntlet to fiscal policy makers today, arguing for infrastructure spending while lowering the ECB?s own growth forecasts,'** said Alasdair Cavalla, economist at the Center for Economics and Business Research, a London-based forecasting and analysis firm."

That help has not been, and will likely not be, forthcoming. As noted this past•Sunday,[BIS economists highlighted]() the fragile global economic backdrop and **said negative interest rates could become a reality for many more countries as central banks search for ways to stoke real growth**.

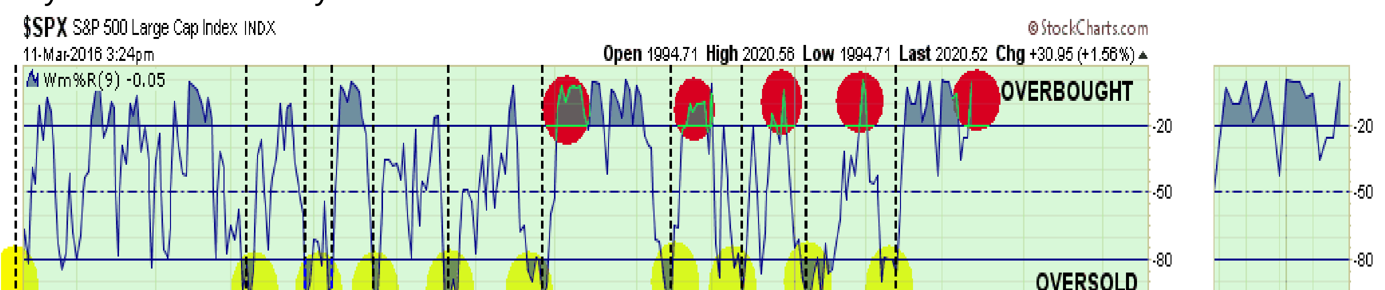
> "**The tension between the markets' tranquility and the underlying economic vulnerabilities had to be resolved at some point.**•In the recent quarter, we may have been witnessing the beginning of its resolution. **We may not be seeing isolated bolts from the blue, but the signs of a gathering storm that has been building for a long time.**"



Unfortunately, all one has to do is look at Japan to see the shortcomings and deteriorative impacts of negative interest rates.

TECHNICALS•IMPROVE SHORT-TERM

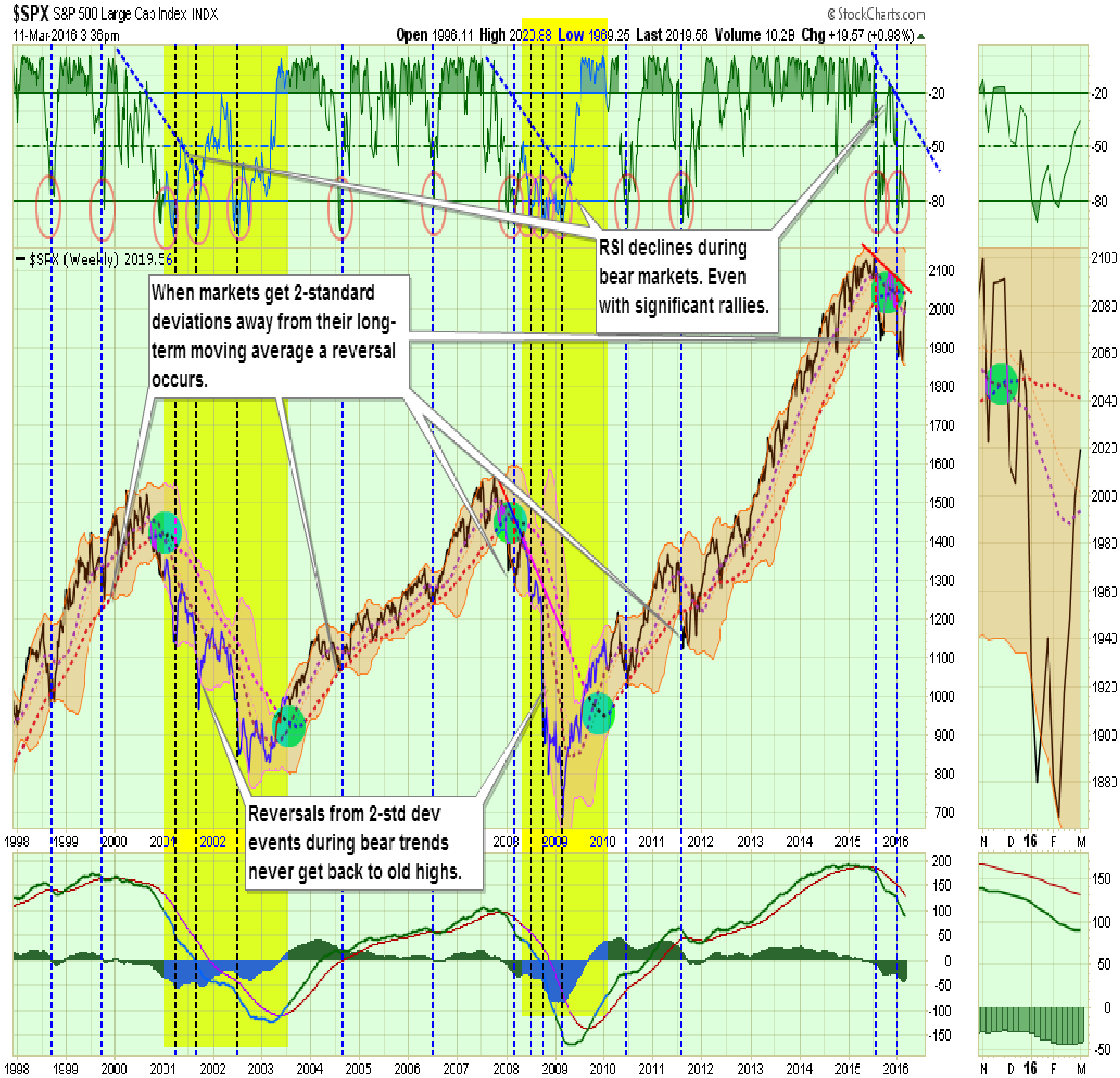
While the economic and fundamental backdrop are still waving very important cautionary flags, **the recent rally in the markets in anticipation of both ECB and Fed support have turned the technical backdrop more constructive.** However, has enough repair been done to change our currently cautionary stance more bullish? Let's take a look. From a short-term, daily, perspective, **the current rally is very similar to the one we saw last October following the summer swoon.** The steepness•of the ascent, amid continued overbought conditions, smacks of a short-covering rally and a scramble by markets for•momentum.



Given the *"accommodative"* stances of Central Banks globally, the current rally runs well in the confines of a reflexive rally. **However, as shown in the chart above the current bearish trend remains intact for now.•**

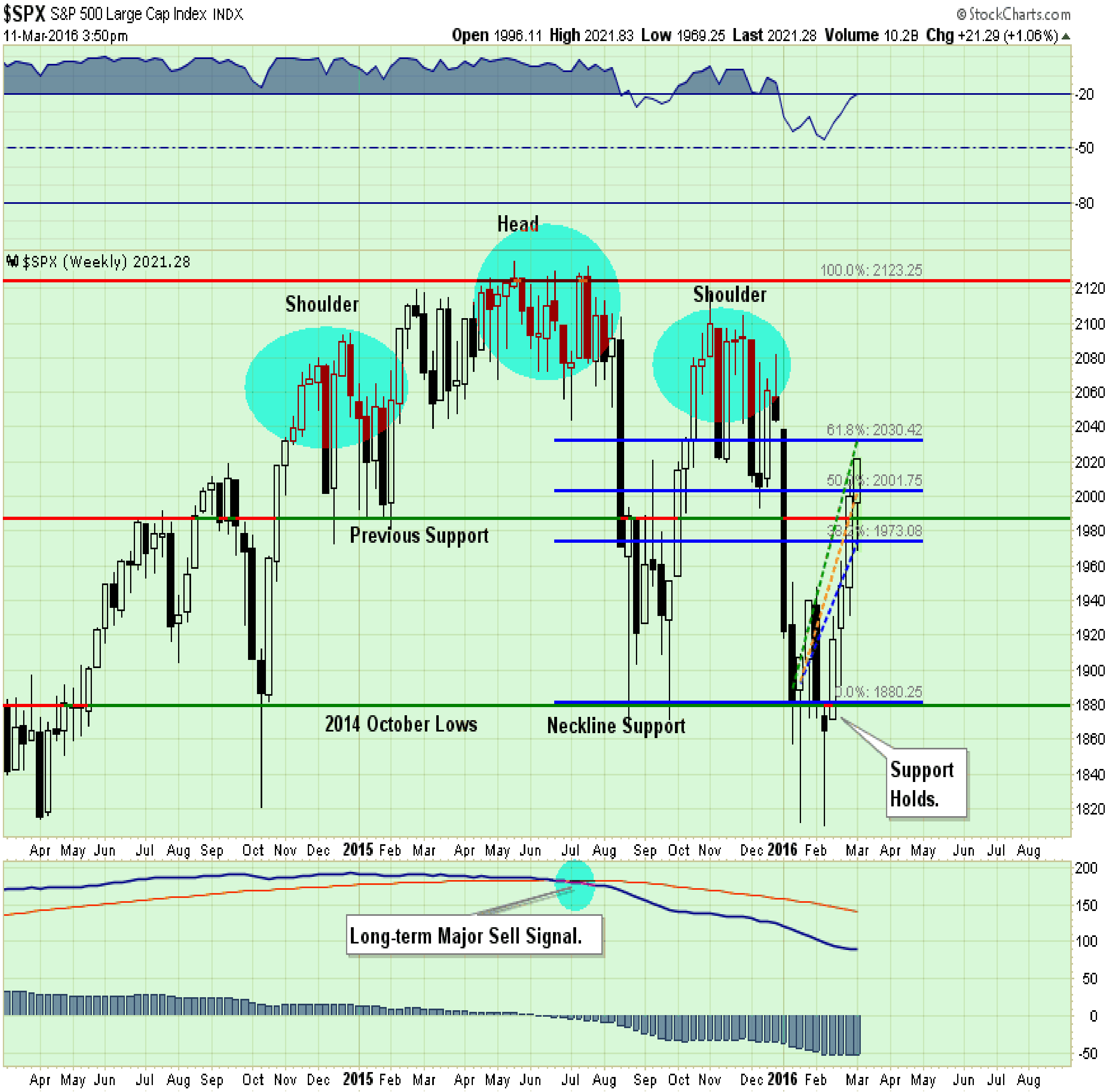
LONGER-TERM NOT SO MUCH

If we step back to an intermediate, weekly, perspective, a little clear perspective emerges. As shown below, **while the recent rally has been extremely sharp, it is still confined to an overall negative price trend.•**



Starting at the top of the chart above, it is important to note the declining trend of the overbought/sold indicator. **The yellow highlights denote previous bear market cycles where the markets remained primarily oversold during the entirety of the reversion process.** Moving to the bottom of the chart, there has been **NO IMPROVEMENT** in the intermediate *"sell"* indicator which also suggests that the current rally remains confined within an ongoing bear market trend. **Note that this indicator has only been this negative during the previous two bear market cycles.** Also, as I discussed last week, the current rally is still within the context of a standard Fibonacci retracement. **The target of 2030, [which I laid out in January of this year,](#) is**

now being approached.



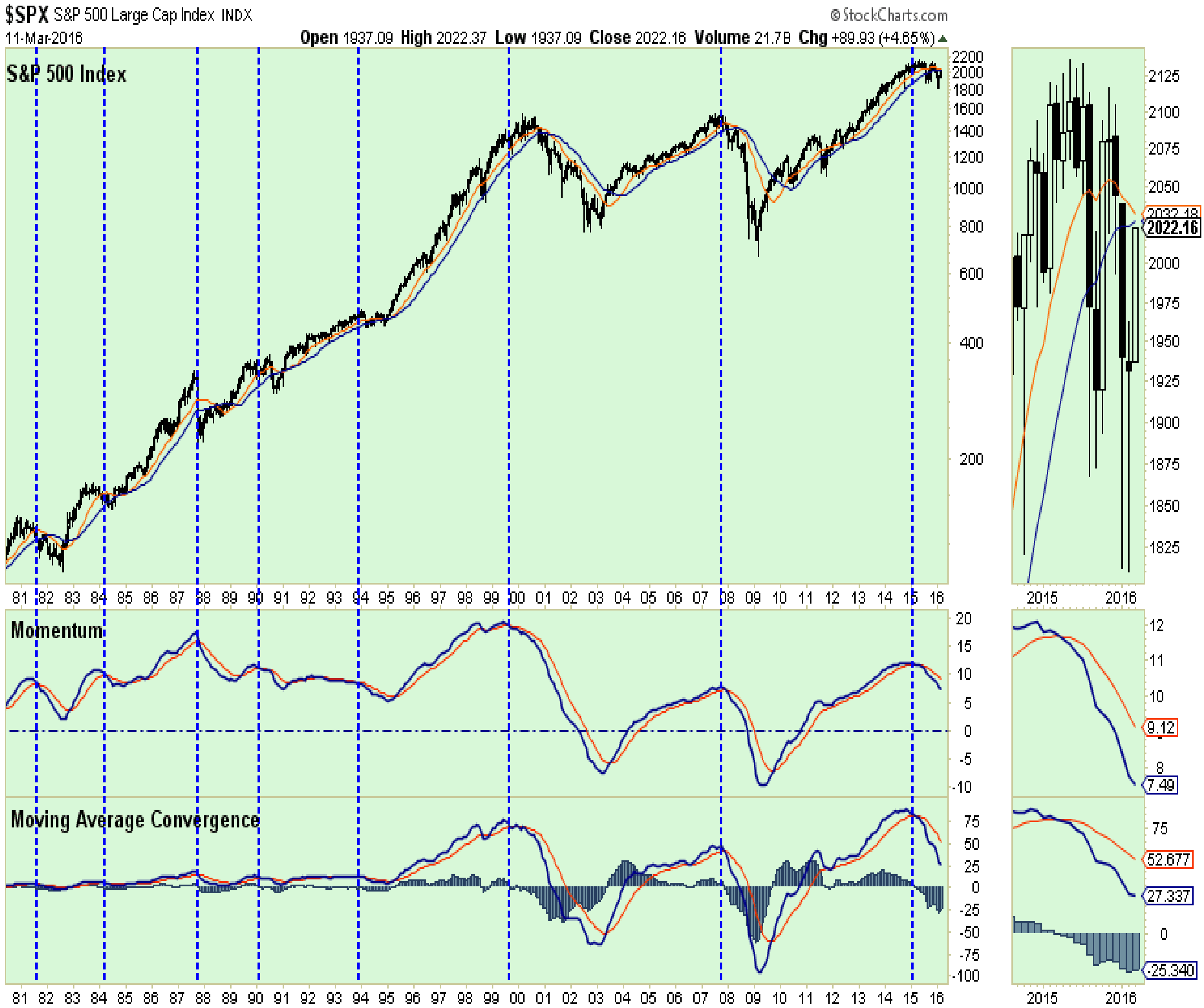
It is worth noting what I said way back then:

> "It is that very oversold condition that has continually suggested that something would happen to elicit a short-term retracement in the market. **Not to be disappointed it was the promise of more liquidity by the ECB and Mario Draghi that elicited a massive short-covering rally on Friday."**

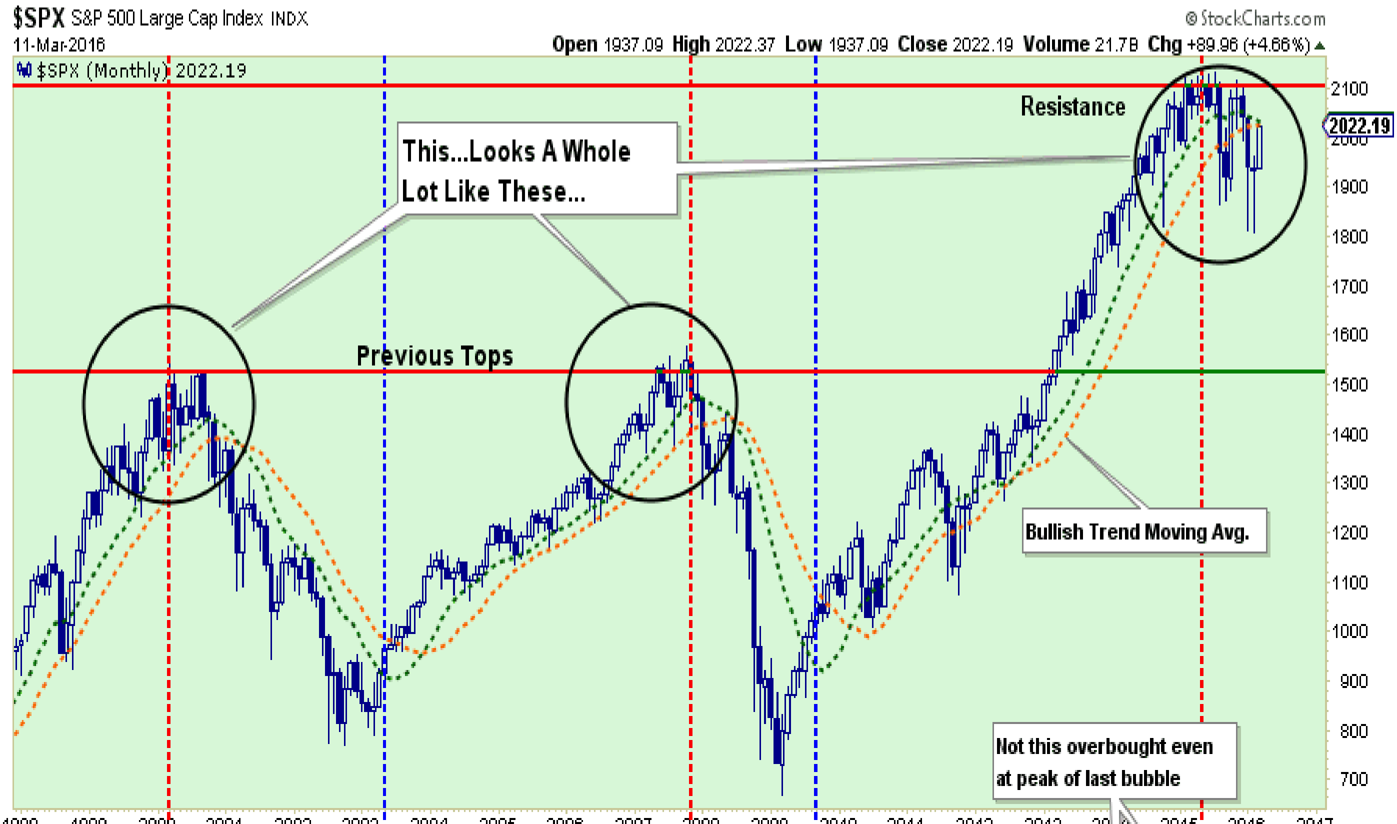
As you will notice, that rally failed and actually broke previous lows. It was then the BOJ's turn to provide support for the market, more promises from the G-20 and finally action from the ECB. **Again, this rally looks an awfully lot like last October, but with with much weaker economic and fundamental underpinnings.•**

> ***"You just have to ask yourself one question. Do I feel lucky? Well, do ya punk?" -*** Clint Eastwood, Dirty Harry

Stepping out even further, **on a very long-term, monthly, picture we see even less evidence the current advance is changing from a negative trend.** The first chart shows the primary *"sell"* indicators going back to 1980. When the two lower indicators have aligned previously on a negative crossover, **it has corresponded with either an intermediate-term correction in the market, a 1987-crash, or worse.•**



The final long-term chart confirms the same **showing a uniform alignment of all technical underpinnings showing NO IMPROVEMENT following the recent rally.•**



In order for the market to change the current negative dynamics, which in turn would warrant a significant increase in long-term equity exposure, it will require a uniform improvement in the technical underpinnings and likely a breakout to all-time highs.•Is such a turn possible? Absolutely. **Is it probable?** Given the deterioration in economic, fundamental and technical backdrops, my best guess is *"no."* But again, anything is possible and the question you have to ask yourself is:

> ***"Do you feel lucky?"***

THE MONDAY MORNING CALL

As I stated last week:

> **"I will readily admit that the recent rally over the last couple of weeks has certainly had me second guessing myself.** I am human after all and am subject to the evils of emotional bias just as anyone is."

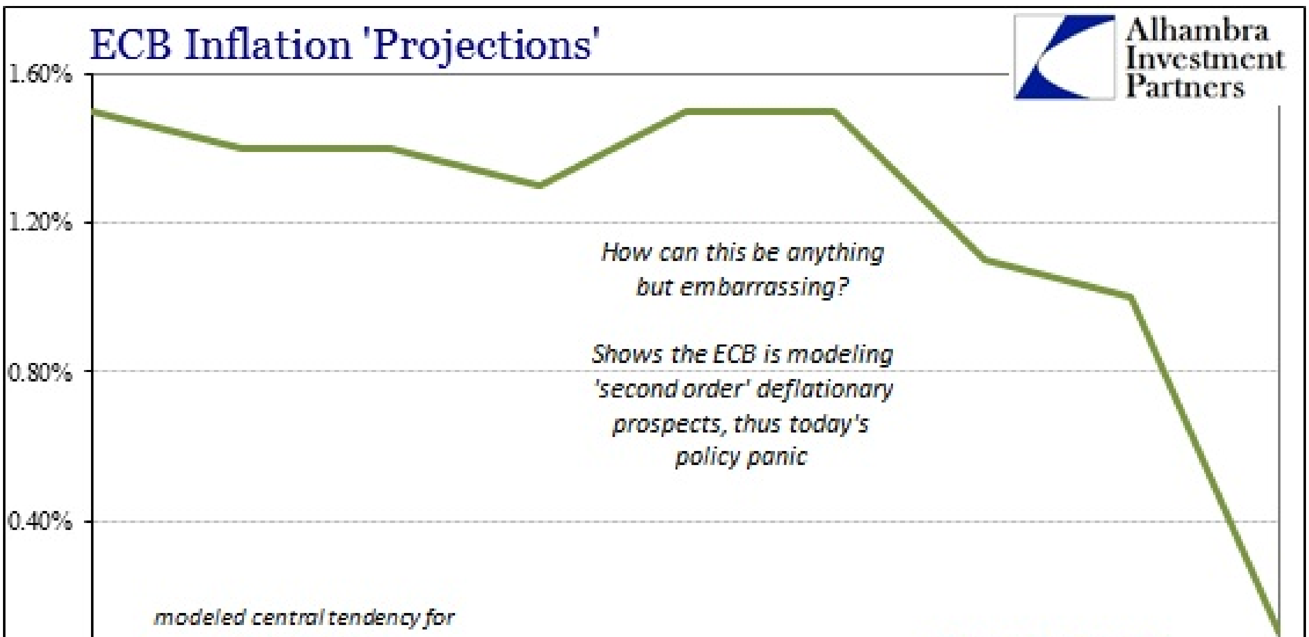
This is where having a strict investment discipline is tested. When markets rally strongly, the inclination by most is to ignore their discipline and chase markets. **During bullish trending markets, such lapses in discipline are forgiven by steadily rising markets. However, during bear markets, such deviations are often brutally punished.•**

Question:

> *If bull markets are a function of earnings growth, increased optimism and strengthening economic trends, then why did the ECB feel the need to drop a nuclear liquidity bomb?*

Jeffrey Snider via Alhambra Partners may have the answer:

> "**The ECB panicked.** Not only did QE fail to ignite inflation, the second order indications, modeled or real, suggest **the real economy is in much, much worse shape than thought just a few months ago.** The timing is not coincidental, as again there was a palpable *global* change starting around mid-year last year, cemented by the events of August and now January. It?s bad enough in policy terms *(in reality, the ECB?s ineptness is the bright side in the real economy as should be apparent by what the Bank of Japan did to the Japanese people)* to see any calendar year at about zero ?inflation? as 2015, but to suggest and model that to repeat for a second? Disaster."



WAITING FOR CHANGE

As discussed throughout this weekend's missive, **there is ample evidence suggesting a more cautionary approach remains the•correct course of action for now•**Therefore, we continue to wait, watch and prepare. As stated last week:

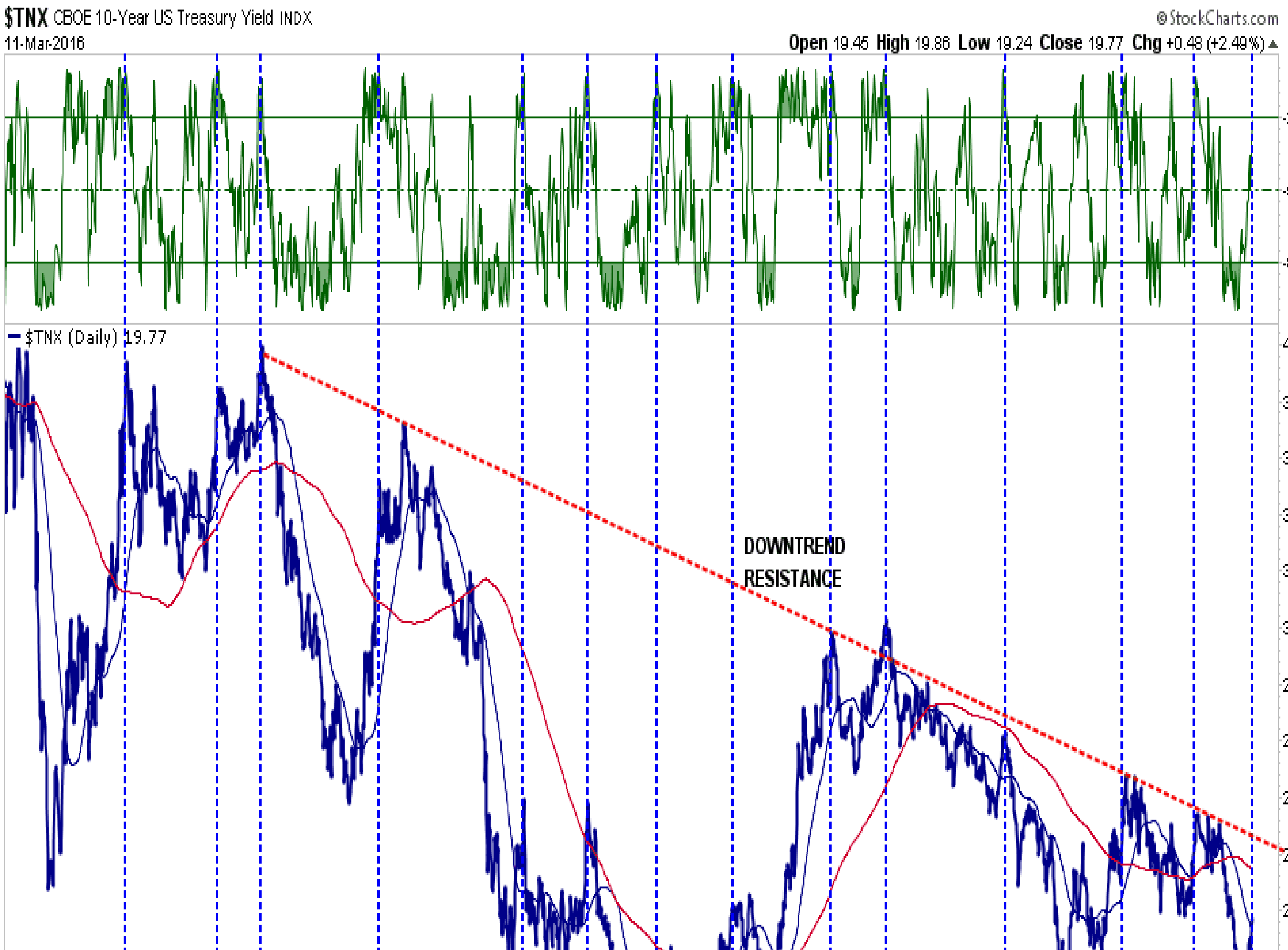
> **"There is now little for us to do except to wait, and watch patiently, for the market to either confirm a '*bear market,'*•OR stabilize and begin to rebuild the bullish supports necessary to allow equity risk to once again be increased."**

Neither situation will make itself apparent in short order, so relax as we let the market dictate what actions we take next. *"Guessing"* at the markets has not typically been a successful and repeatable strategy. •As stated above,**while very short-term indicators have•improved, the longer-term signals have not.•**

BONDS LOOK ATTRACTIVE

While stocks have had a significant surge recently, that short-covering and momentum push has shifted money out of bonds *(safety)* and back into equities *(risk).*•This is something I specifically noted in last week's missive *"Is It Time To Buy Bonds?"*

> **"This analysis also suggests that the current correction in stocks is likely not over as of yet in the longer term.•**However, in the very short-term, the current oversold condition in rates suggests that **the current ?*bear market rally?*could last through the month of March. Such would not be surprising following a rather brutal first two months of the year.** However, as we approach summer, the seasonal weakness of the markets will likely resurface and **bonds will once again become a safe haven for investors against further market declines."**



With interest rates back into overbought territory temporarily, the flight from *"safety"* to *"risk"* may be nearing its end. **While rates could very conceivably push from Friday's close of 1.98% to somewhere between 2.1% and 2.2%, such is not much room to play with.**•Therefore, I am beginning to scale into short and intermediate duration bonds over the next couple of weeks as rates continue to push slightly higher. **I expect that I will be well rewarded by the end of this year as rates reflect the current underlying economic fundamentals and retest recent lows or lower.**•Like every•Mom in the world has said at one time or another:

> ***?Before you turn your nose up at those, try them first. •You might just like them.?•***

S.A.R.M. Model Allocation

Working With A Model Allocation

> ***NOTE:*** *The following is for example purposes ONLY. It is in no way a suggestion, recommendation, or implication as to any portfolio allocation model currently in use. It is simply an illustration of how to overweight or underweight a model allocation structure.*

Again, this is just for educational purposes, and I am not making any specific recommendations. This is simply a guide to assist you in thinking about your own personal positioning, how much risk you are willing to take and what your expectations are.•The closer you want to track the S&P 500 Index, the less fixed income, real estate and cash your portfolio should have. For a more conservative allocation reduce allocations to equities and add more to cash and fixed income.

S.A.R.M. Current

The **S**ector **A**llocation **R**otation **M**odel (SARM) is an example of **a basic well-diversified portfolio**. The purpose of the model is to look *?under•the hood?*of a portfolio to see what parts of the engine are driving returns versus detracting from it. **From this analysis, we can then determine where to overweight sectors which are leading performance, reduce in areas lagging, and eliminate those areas that are dragging.** First, let me show you [where we were at the end of January]just prior to the February trouncing. As I stated then:

> "The Sector Allocation Rotation Model continues to deteriorate suggesting that markets are significantly weaker than they appear. **As suggested all through this missive, any bounce, or a break of the lower support, should be SOLD into•immediately."**

With risk assets primarily in the lagging and improving quadrants, the weak underpinnings of the market were clearly evident. **Importantly, I stated then:**

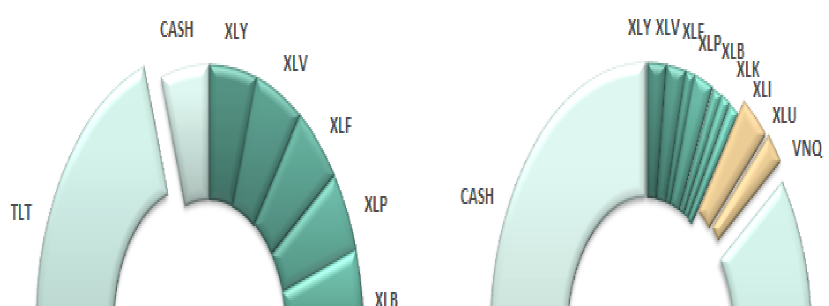
> "Not surprisingly interest rate sensitive sectors, along with the more defensive sector of the market, Staples, surged last week as the 10-year Treasury plunged below 2%?again. **The search for safe haven investments such as Utilities, Bonds, and Staples has become a more crowded trade as capital leaves the previous leaders of Technology, Industrial and Discretionary sectors. As noted by the BLUE circle above, the current level of•outperformance•by Utilities, Bonds &•Staples is unsustainable.** **You should take profits in these sectors immediately and reduce overweighted positions back to normal levels.** *(This is the essence of profit taking.)"*

As noted above, I am now recommending beginning to scale back into "bonds" as the recent uptick in rates has reduced that overbought condition and have taken bonds to an underweight position in portfolios by reducing prices.•Here is the updated SARM model.

You will note that despite the recent rally, not much has changed since the end of January. **Yes, risk assets have improved against safety assets, but not as significantly as one might expect given the sizable rally over the last several weeks.**•With markets once again back to extremely overbought conditions, and fighting a declining 200-dma, **the advantage of adding significantly to risk assets at this juncture is likely not advisable.**•Therefore, there have been no•changes to S.A.R.M. model in the past week.

S.A.R.M. Model Allocation *(Assume 60/40 Allocation To Equal 401k Plan Manager)*

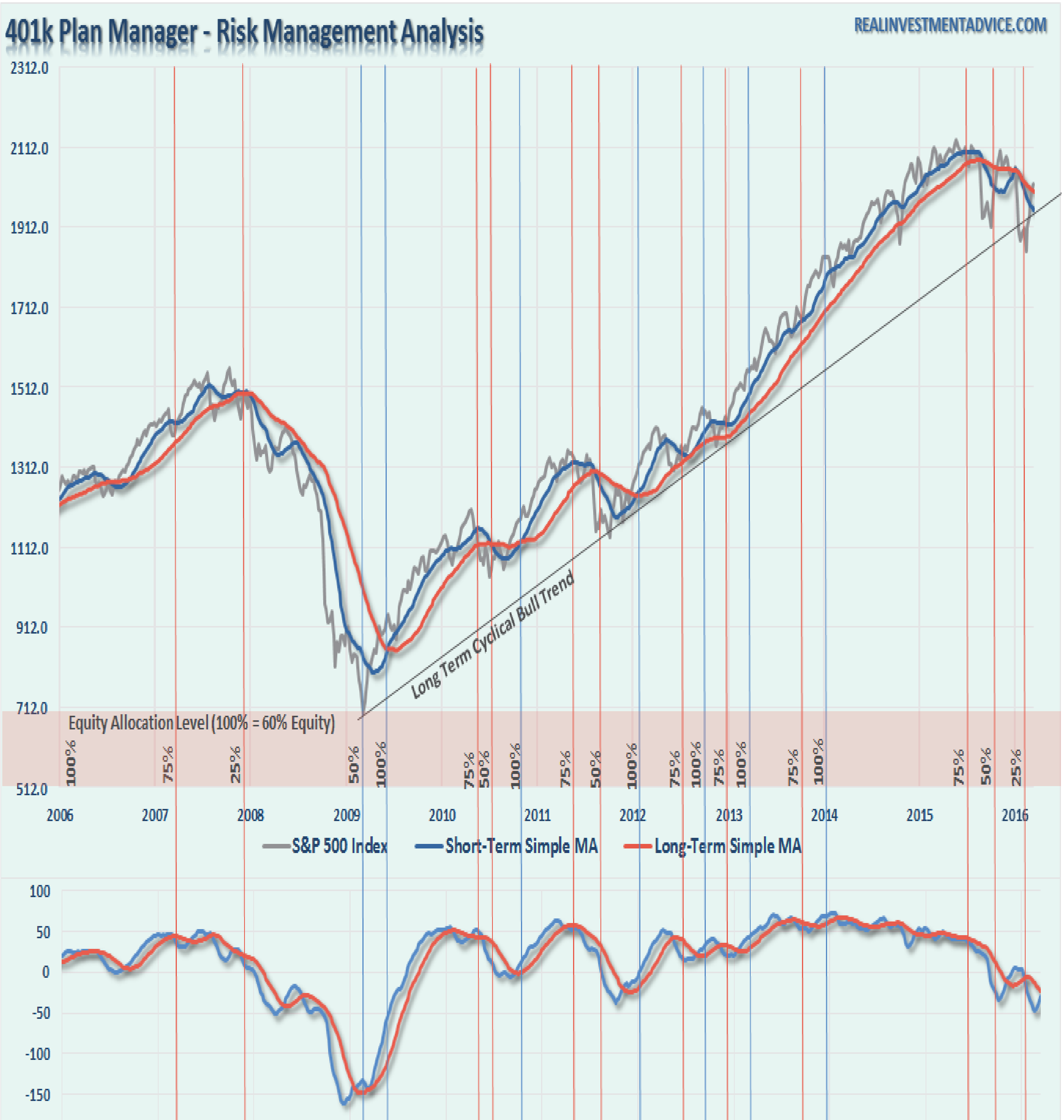
Symbol	Name	Model Weight	SARM Analysis	Adjusted Weight
XLY	Discretionary	5.00%	Weakening	2.00%
XLV	Healthcare	5.00%	Improving	2.00%
XLF	Financials	5.00%	Lagging	1.00%
XLP	Staples	5.00%	Leading	2.00%
XLB	Materials	5.00%	Lagging	1.00%
XLI	Industrials	5.00%	Weakening	1.00%



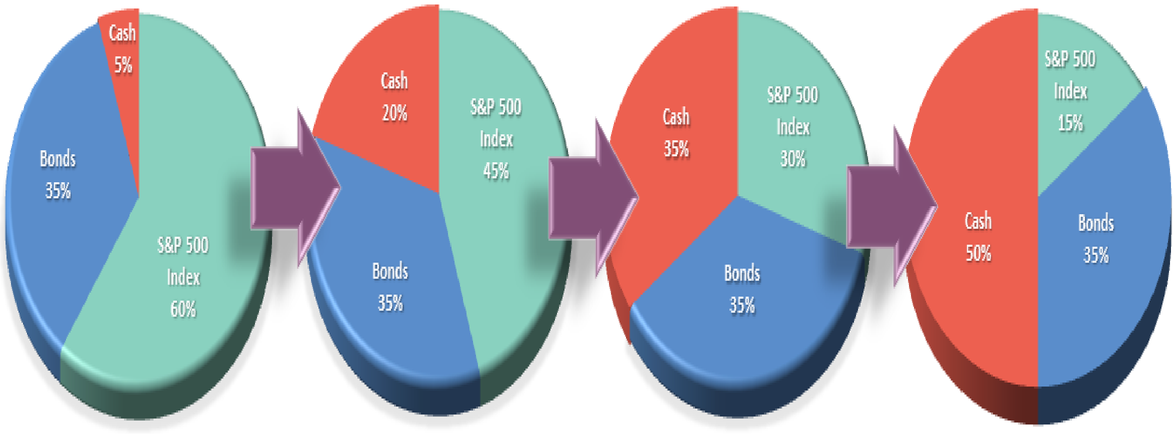
The portfolio model remains unchanged this week with•CASH to•50%, 35% in bonds, and 15% in equities. **It is completely OKAY if your current allocation to cash is different based on your personal risk tolerance. This is just a guide.** If the market can pull back and form a bottom at the 50-dma (establishing a higher low) and move the markets back into an oversold condition in the process, such would likely provide a reasonable opportunity to increase short-term equity exposure. However, for longer-term investors, we need to see an improvement in the fundamental and economic backdrop to support a resumption of the bullish trend. Currently, there is no evidence of that occurring. **Such is critically important as•economic growth is directly related to P/E growth and stock market returns. This is because earnings/profit growth is directly linked to economic growth. Therefore, over the course of a full-market cycle, corporate profits cannot indefinitely grow faster than the economy.**

> ***"Money follows earnings."*** - David Dreman

THE REAL 401k PLAN MANAGER



There are 4-steps to allocation changes based on 25% reduction increments. As noted in the chart above a 100% allocation level is equal to 60% stocks.•I never advocate being 100% out of the market as•it is far too difficult to reverse course when the market changes from a negative to a positive trend. Emotions keep us from taking the correct action.



SITTING AT TARGET FOR NOW

While the market rally was quite exceptional over the last couple of weeks, it has done little to change the currently negative market trends back to positive. **As shown in the 401k portfolio manager chart above, all sell signals remain in place currently, and while they improved slightly over the last two weeks, remain in the negative.** However, as I stated last week:

> "...**some event *(exogenous, monetary or fiscal)* could occur which would render such analysis incorrect.** If such an event occurs, we will re-evaluate holdings and readjust accordingly."

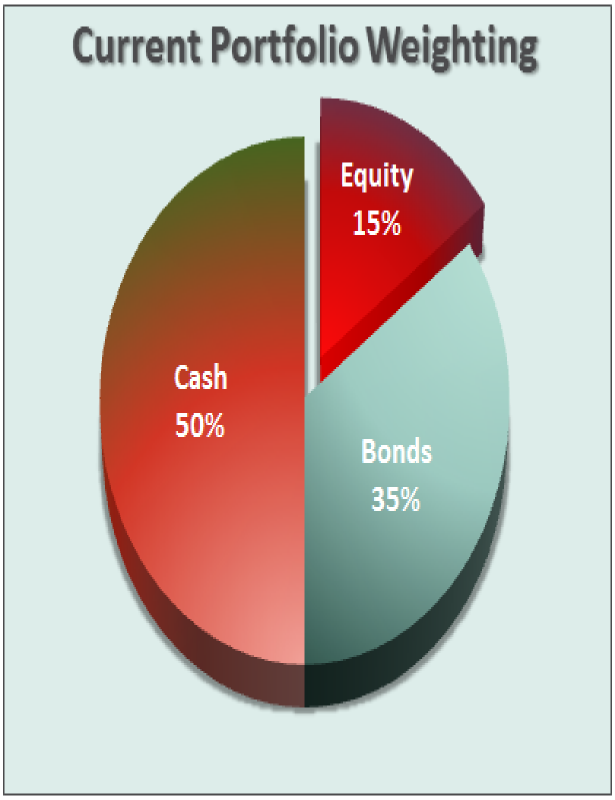
That event was the ECB last week which gave a modest boost to stocks on Friday. The Federal Reserve is now up on deck as we head into the end of the month, which could either provide a further lift or a sharp decline. As discussed throughout the entirety of this week's missive, **the technical damage to the market remains over the intermediate and longer-term time frames. This suggests the reward is still outweighed by risk and continues to suggest a more cautionary allocation.** •Therefore, I reiterate last week's note:

> **"With portfolio allocations now reduced to TARGET levels, the only action to currently take is NOTHING.** We are now in the position to just WAIT and allow the market to TELL us what it wants to do next. **While many will speculate on a resumption of a "bull market" in the short-term, the RISK of being WRONG far outweighs the possibility that such prognostications are correct."**

Portfolio management is not difficult, **it is just a function of letting the markets tell you what it wants to do, rather than *"hoping and guessing"* at what YOU want it to do. You are not in control. When you learn to accept that, managing your money becomes vastly easier.**•If you need help after reading the alert; don?t hesitate to contact me.

Current 401-k Allocation Model

The 401k plan allocation plan below follows the K.I.S.S. principal. By keeping the allocation extremely simplified it allows for better control of the allocation and a closer tracking to the benchmark objective over time. *(If you want to make it more complicated you can, however, statistics show that simply adding more funds does not increase performance to any great degree.)*



Current 401k Allocation Model

50.00% **Cash + All Future Contributions**

Primary concern is the protection of investment capital

Examples: Stable Value, Money Market, Retirement Reserves

35.00% **Fixed Income (Bonds)**

Bond Funds reflect the direction of interest rates

Examples: Short Duration, Total Return and Real Return Funds

15.00% **Equity (Stocks)**

The vast majority of stock funds track an index.
Therefore, select on ONE fund from each category.
Keep it Simple.

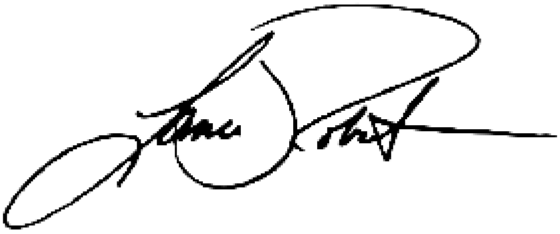
7.5% Equity Income, Balanced or Conservative Allocation
7.5% Large Cap Growth (S&P 500 Index)
0% International Large Cap Value
0% Mid Cap Growth

401k Choice Matching List

The list below shows sample 401k plan funds for each major category. In reality, the majority of funds all track their indices fairly closely. Therefore, if you don't see your exact fund listed, look for a fund that is similar in nature.

Common 401K Plan Holdings By Class

Cash	*Stable Value*	**Equity**	
	Money Market	**Large Cap**	*Vanguard Total Stock Market*
	Retirement Savings Trust		*Vanguard S&P 500 Index*
	Fidelity MIP Fund		*Vanguard Capital Opportunities*
	G-Fund		*Vanguard PrimeCap*
	Short Term Bond		*Vanguard Growth Index*
			Fidelity Magellan
Fixed Income	*Pimco Total Return*		*Fidelity Large Cap Growth*
	Pimco Real Return		*Fidelity Blue Chip*
	Pimco Investment Grade Bond		*Fidelity Capital Appreciation*
	Vanguard Intermediate Bond		*Dodge & Cox Stock*
	Vanguard Total Bond Market		*Hartford Capital Appreciation*
	Babson Bond Fund		*American Funds AMCAP*
	Lord Abbett Income		*American Funds Growth Fund Of America*
	Fidelity Corporate Bond		*Oakmark Growth Fund*
	Western Asset Mortgage Backed Bond		*C-Fund (Common Assets)*
	Blackrock Total Return		*ALL TARGET DATE FUNDS 2020 or Later*
	Blackrock Intermediate Bond		
	American Funds Bond Fund Of America	**Balanced Funds**	*Vanguard Balanced Index*
	Dodge & Cox Income Fund		*Vanguard Wellington Fund*
	Doubleline Total Return		*Vanguard Windsor Fund*
	F-Fund		*Vanguard Asset Allocation*
			Fidelity Balanced Fund
International	*American Funds Capital World G&I*		*Fidelity Equity Income*
	Vanguard Total International Index		*Fidelity Growth & Income*

Lance Roberts  Lance Roberts is a Chief Portfolio Strategist/Economist for Clarity Financial. He is also the host of ?The Lance Roberts Show? and Chief Editor of the ?Real Investment Advice? website and author of ?Real Investment Daily? blog and ?Real Investment Report?. Follow Lance on Facebook, Twitter and Linked-In