BUSINESS CYCLE DEVELOPMENTS

There are now two of six **Market <u>Trough</u> Indicators (MTI's)** signaling, which is sufficient to buy stocks on weakness, if the economy is experiencing something less than recession. If it's recession then five **MTI's** are required, but this has every sign of being only a slowing. To date, there hasn't been the usual -15% average *daily-close* drop in the S&P, only -6% in February. <u>But the evidence is building that the S&P should be bought on weakness</u>. This relatively small -6% decline may be similar to the three shallow experiences below, where *daily-close* declines were -8%, -9% and -10%. Each of these three S&P declines discounted something less than a recession and it's clear that the U.S. is already in an economic slowdown, which began in December 2013. That's when non-durable output and yields both peaked, so we're one quarter into a slowing. It's always difficult to prove a slowing when it's occurring, but there's six of eight **Business Cycle Peak Indicators (BCPI's)** and the output numbers are flat and yields peaked in December – all point to a slowdown.

The 1st **MTI** to signal was the appearance of four out of six **Interest Rate <u>Peak</u> Indicators (IRPI's).** That 4th **IRPI** signaled in September 2013. Since 2000, when there are four of six **IRPI's**, the market bottoms an average of 8 months (+/- 3mo.) later - we're in that time frame now!

S&P 500 DECLINES DISCOUNTING SLOWDOWNS & RECESSIONS

S&P 500 TROUGH	S&P 500 PEAK (MONTHLY AVERAGE DECLINE & DAILY CLOSE DECLINE)	
6/49	-25% & -30%	
9/53 (R)	-11% & -15%	
12/57 (R)	-17% & -22%	
10/60 (R)	-10% & -14%	
6/62	-22% & -28%	
10/66	-17% & -22%	
6/70 (R)	-29% & -36%	
12/74 (R)	-42% & -48%	
3/78	-16% & -19%	
7/82 (R)	-19% & -27%	
7/84	-10% & -14%	
12/87	-27% & -34%	
10/90 (R)	-15% & -20%	
12/94	-5% & -9%	Nasdaq -14% & R2M - 13%
9/98	-12% & -19%	
9/01 (R)	-30% & -37%	
2/03	-27% & -32%	
8/04	-5% & -8%	Nasdaq -19% & R2M -15%
3/09 (R)	-51% & -57%	
7/10	-10% & -16%	
6/12	-5% & -10%	Nasdaq -12% & R2M -13%
AVG.:	-19% & - 24%	
2/14 ?	-.3% & -6% (1)	Nasdaq -6% & R2M -7%

(R) RECESSION. (1) S&P 500 DECLINE TO DATE.

The second **MTI** occurred when two of eight **Business Cycle <u>Trough</u> Indicator's (BCTI's)** signal. That second **(BCTI)** Indicator appeared in January 2014 and the lead-time, from the date of the 2nd **MTI** to the S&P 500 bottom, has averaged two months (+/- 2 mo.). This centers a S&P low in <u>March 2014 (Jan. 2014 to May 2014)</u>. The four to six week reporting lag for most of the data explains the 2nd **MTI** being received late last week. The S&P 500 -6% decline and low, to date, ties into this window of time.

What could explain such a shallow market decline? There have been a few such declines before (see table above) and then again not many could predict the secular flatness in output and equity markets post 2000. Perhaps this is a melt-up connected to the excessive stimulation of the past five years. Venezuela and Argentina have had market extensions after excessive monetary and fiscal stimulation and stocks are a claim on a real asset, which should do well in such blow-off conditions. Time will tell. What is known is that stocks always recover when yields cyclically fall, responding to slow economic activity <u>and</u> then bottom prior to economic recovery and these are the circumstances that the equity markets are expected to respond to today. This rules-based disciplined research process is driven by the Indicators and coupled with a recent history of shallow declines, <u>it's recommended that stocks be purchased on market weakness</u>.