THE FED FAILS AGAIN

Another week goes by and another chance for the FED to "normalize" rates goes to the wayside. Why should we expect anything less? Equity markets at all-time highs, yields have risen in expectation of a more hawkish FED and Non-Farm Payrolls post a bigger than expected increase. Why would the FED hike? What has been a recurring theme the last few years, continues unabated into 2017. All the necessary ingredients for a rate hike, but no cook to execute the recipe. It seems like the only cooking the FED has been doing has been their own balance sheet. All this talk of reducing its size, that's all just nonsense. We know and all of you our dear readers know that the FED can never embark on such a path. That ended long ago once the QE and TARP cliffs were crossed, dragging all the global economic herds with it. Anyway let's look at the FED's statement headlines shall we:

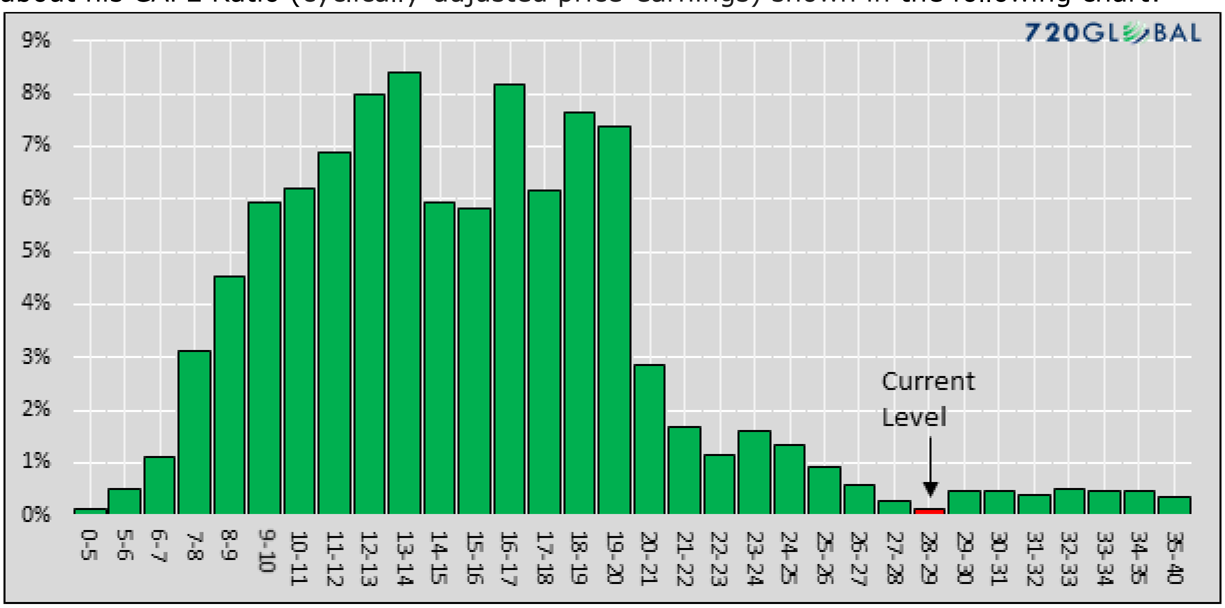
- **FED SAYS JOB GAINS REMAIN SOLID AND UNEMPLOYMENT RATE HAS STAYED NEAR ITS RECENT LOW**
- **FED SAYS MEASURES OF CONSUMER, BUSINESS SENTIMENT HAVE IMPROVED OF LATE**
- **FED SAYS INFLATION INCREASED IN RECENT QUARTERS BUT IS STILL BELOW ITS LONGER-RUN OBJECTIVE**
- **FED REPEATS EXPECTS INFLATION TO RISE TO 2 PCT OVER MEDIUM TERM; STATEMENT REMOVES REFERENCE TO TRANSITORY EFFECTS OF OIL, IMPORT PRICES**
- **FED REPEATS IT WILL REINVEST PRINCIPAL PAYMENTS FROM ITS HOLDINGS UNTIL RATE NORMALIZATION IS WELL UNDER WAY**
- **FED REPEATS NEAR-TERM RISKS TO THE ECONOMY APPEAR "ROUGHLY BALANCED"**
- **FED REPEATS EXPECTS ECONOMIC CONDITIONS WILL EVOLVE IN WAY THAT WARRANTS "ONLY GRADUAL INCREASES" IN FED FUNDS RATE**

An institution full of over 700 Phd wielding economists certainly likes to use generalizations in their statements, words like "roughly balanced and gradual increases." Come on, honestly we know you can do better, hell we expect a bit more clarity from the single largest most influential monetary entity on the planet. Why the general public, doesn't hold this institution more accountable is certainly troublesome. Perhaps we can chalk it up to lack of initiative, lack of incentives, lack of any true understanding of how our financial system and economic viability are truly managed.

It irritates us to know that our current system, by its inherent design has been sold down a river flowing ever so slowly toward an endless cavern to be devoured deep into the abyss. The current is strong and there seems to be no fighting it. It's the system we have and those that haven't figured out by now that it has nothing to do with fundamentals, are going to be left covered in the dust bins of history.

The markets have no mercy, they can operate against the laws of fundamentals for longer than most can stay solvent to fight them. This isn't a call to dismiss those out there that are staunch supporters of value, the Robert Shiller, James Grant types. Rather we heed their call to urgency, yet we also understand that the financial system is not predicated on past fundamental valuations, but rather predicated on ongoing and continued central bank support. **We don't like it, we don't agree with it**, but we aren't dumb enough to believe that the central banks are simply going to let go of something that they have worked so hard on achieving. If it's one thing we understand about the psyche of academics is, that they would rather go down in flames and bring everyone with as opposed to admitting that their theories are flawed. Call it ego, call it lack of humility, call it whatever you like, but its far easier to defend ones position under the guise of intellect and theory than it is to admit to blatant inaccuracies.

Speaking of Robert Shiller, this week 720 Global's Michael Lebowitz had this to say about his CAPE Ratio (cyclically-adjusted price-earnings) shown in the following chart:



Data Courtesy Robert Shiller

*"While not a perfect bell curve, the chart above does have a similar shape, albeit with a long right tail. Over 80% of the data lies between a ratio of 8 and 20. The current ratio of **28.14 has only been eclipsed by 3% of the observations**. Put more bluntly; the S&P 500 is in no man's land by this measure."*

We have heard these fundamental value investors clamor for some time now. Their rationale is certainly easy to accept, but like we said, when you have a money printing entity or entities it's easy to see why distortions can last a lot longer than people think. Then again, perhaps it's just more of the same, more of the same rinse, recycle and repeat mechanisms. Sure the distribution that this chart represents puts us into the tail, the only question is when will it revert? Obviously we can make astute judgment calls via data, but that's where it stops. The question is what do we do with this data? How can we make an investment choice via this data? Yes by this metric the markets are overvalued, no question, but as we have pointed out many times in the past, these aren't the markets that they once were. Once the central banks decided to concentrate and centralize all the power, markets ceased, well, being markets…

The bigger question is why do people continue to think that equity markets are overvalued and to what are they comparing it too? Overvalued versus what? Historical metrics? Overvalued versus some other investment? We think far greater importance and emphasis should be made toward a more relative current value of investment X versus investment Y. In the past money and capital required more time and displayed more friction. Today, money, capital and or credit are virtually electronic and can be transferred at lightning speed to invest or divest as it sees fit. This borderless, frictionless aspect of current capital, credit and money is a large factor as to why correlations seemingly arise to then breakdown. Capital is on a constant search for the highest reward at the lowest risk and all the quantitative power is merely focused upon achieving and obtaining that very goal. One would think that this would create extreme bouts of volatility, yet volatility metrics seem to be constantly clinging to new lows. One of the answers seems to lie in the fact that the actual concentration of wealth has been targeted to a lot less players. We touched on this a few weeks back and Oxfam reported that "since 2015 the richest 1% owns more than the rest of the 99% combined."

With this newly formed concentration it is far easier to see why the equity markets behave the way that they do. Why they seem to constantly rise in linear like fashion with nary a pullback. Those that control its pricing, for all intents and purposes never have to sell. Well never until the central banks decide to tighten the reigns, which we have yet to see. **The ECB and the BOJ combined and continue QE stands around $180 billion a month, PER MONTH!** We hate to say it but one would have to be somewhat idiotic to think that capital gains can't be achieved with this type of free money being tossed around. This concentration of wealth at the very top is in our opinion one of the leading reasons why valuations can stretch in nominal terms. The QE mechanism that continues overseas via these two central banks continues to allow for both equity rises as well as government and corporate bond markets to be heavily distorted.

The ultra-wealthy continue to benefit from zero cost of funds, all the while everyone else massively over pays for money and credit. This will continue to wreak havoc on general economies but the blow will be softened under the guise of perpetual equity market increases. Hell even CNBC might make a comeback, but we doubt it.

Some of the tech giants reported earnings this week and the markets were a bit mixed to the results. Apple sold a record number of Iphones and beat both on the top and bottom lines, but their China sales continued to slide declining 4 quarters in a row so far. Their stock jumped nearly 8% to a high of $130.49 and settled in the week at $129.08 near the top of their yearlong trend channel. Their net cash sits at a whopping $159 Billion while **total cash is nearing the $250 Billion mark** shown here:

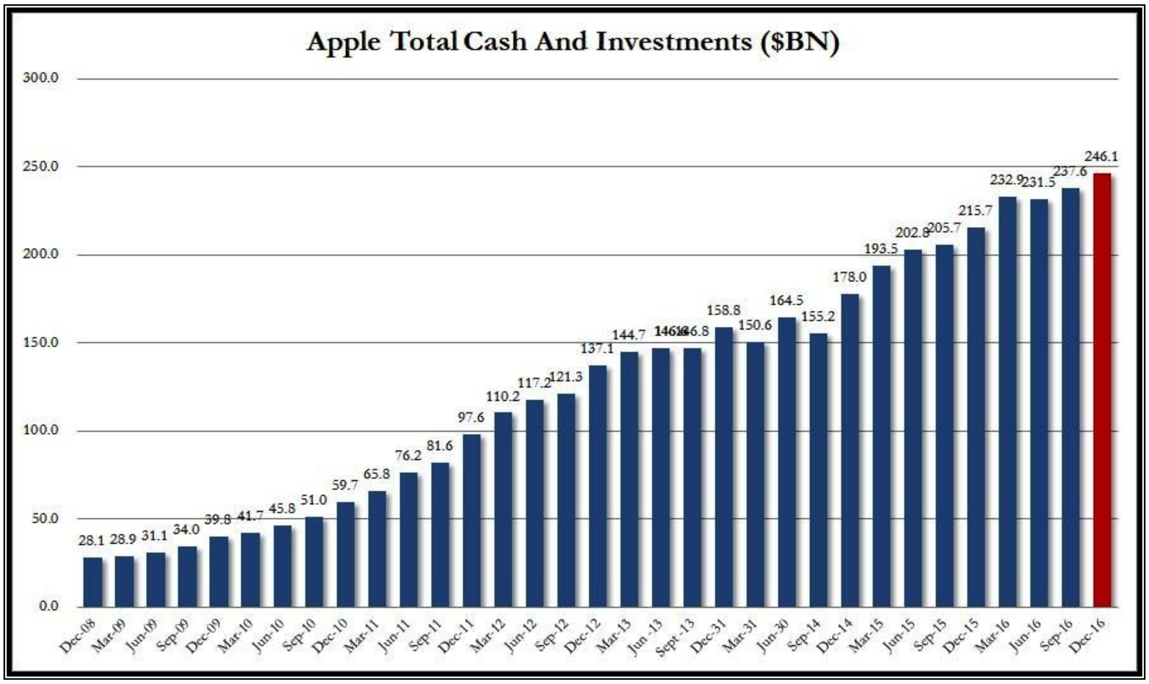


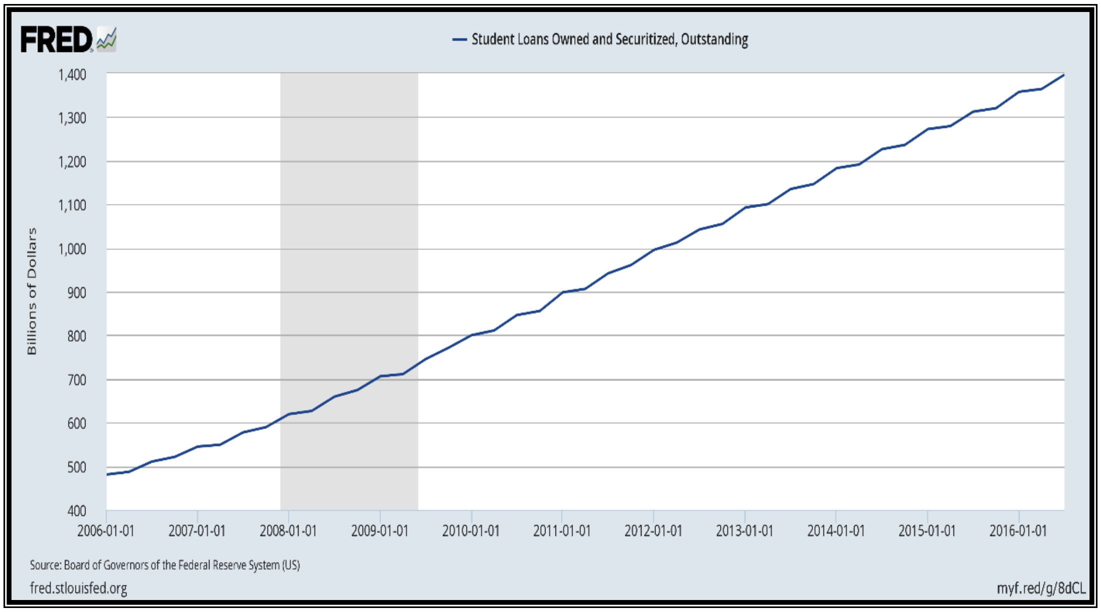
Chart courtesy zerohedge.com

Facebook was also out this week and beat expectations. Active monthly users rose to 1.86 billion. Their stock rose 5% but settled in the week at $130.98 up marginally on the week.

Amazon missed revenue expectations rising to $43.7 billion on expectations of $44.9. They did announce that they were going to create 100k new full time jobs in the US alone over the next year and a half. Their cash flow hit a record high $9.7bln. Their stock didn't fare so well it lost nearly 4% falling to $810.20 down from $842 the prior day.

News this week also included Snapchat (Snap) execs ready to go with an IPO on the NYSE with a t valuation around $20bln. This will be the largest tech IPO in years. How smart were these guys to turn down a $3bln offer from Facebook? With a loss of over $500 mln last year, some may be worried, however their user base rose some 48% over that same period to 158 million daily active users. We can't help but think the Snap IPO is going to see some buying interest at the expense of some of these prior names, especially Facebook. Word on the street is that Facebook is passé and "**Snapchat"** is the Nuevo tech that all the kids are using. Yes Facebook has 10x the amount of users, but we would be remised if we didn't think that gap would close in the future. The NY Times had a good article and more about Snap which can be read Here

Another thing that we are keeping an eye on is this whole student loan bubble. Since the end of 2008 the student loan amounts outstanding have more than doubled from $600bln to nearly $1.4trn. Just wondering what the default amounts truly are and who is going to be left holding the bag. Is there a CDO market yet? Just sayin.

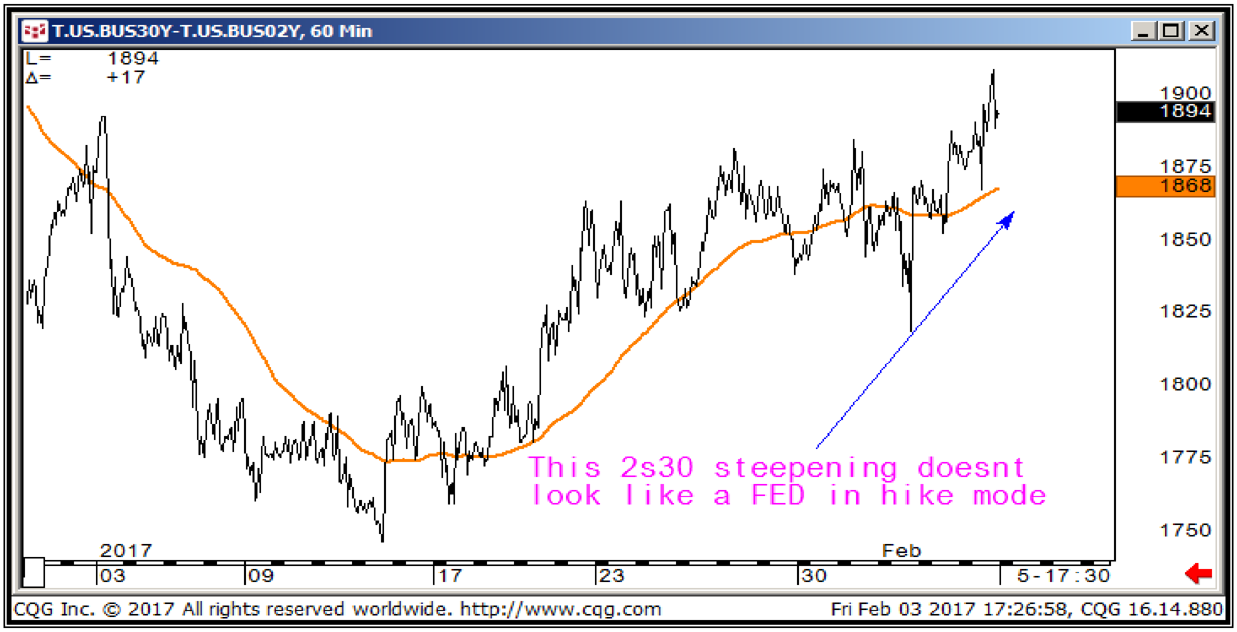


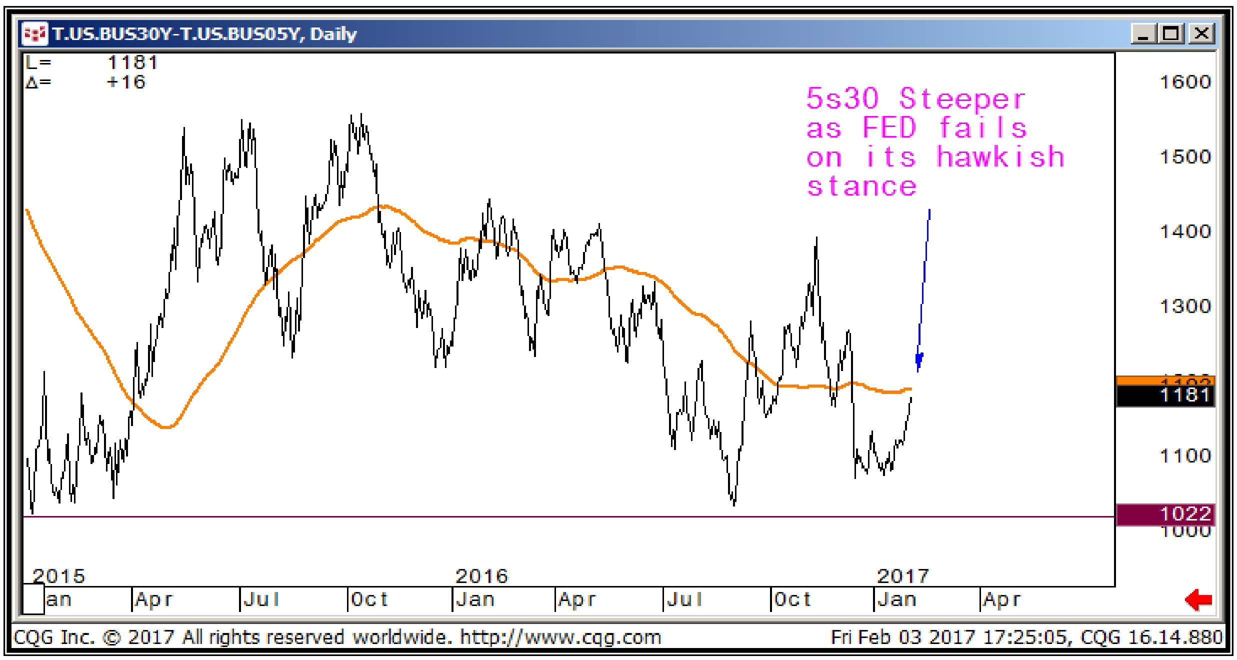
Ok let's get to the technical's and the charts, first up we have the Bond Futures which have seen some consolidation on the lows but having quite a tough time with the Vwap resistance at 151-15:

The bond on a bit of shorter time frame exhibits some nice volatility with the Vwap once again being a magnet:

When looking at the 10yr yield chart a clear range has been formed from 2.30 to 2.55 and an opinion either way cannot truly be made till one of these levels is broken:

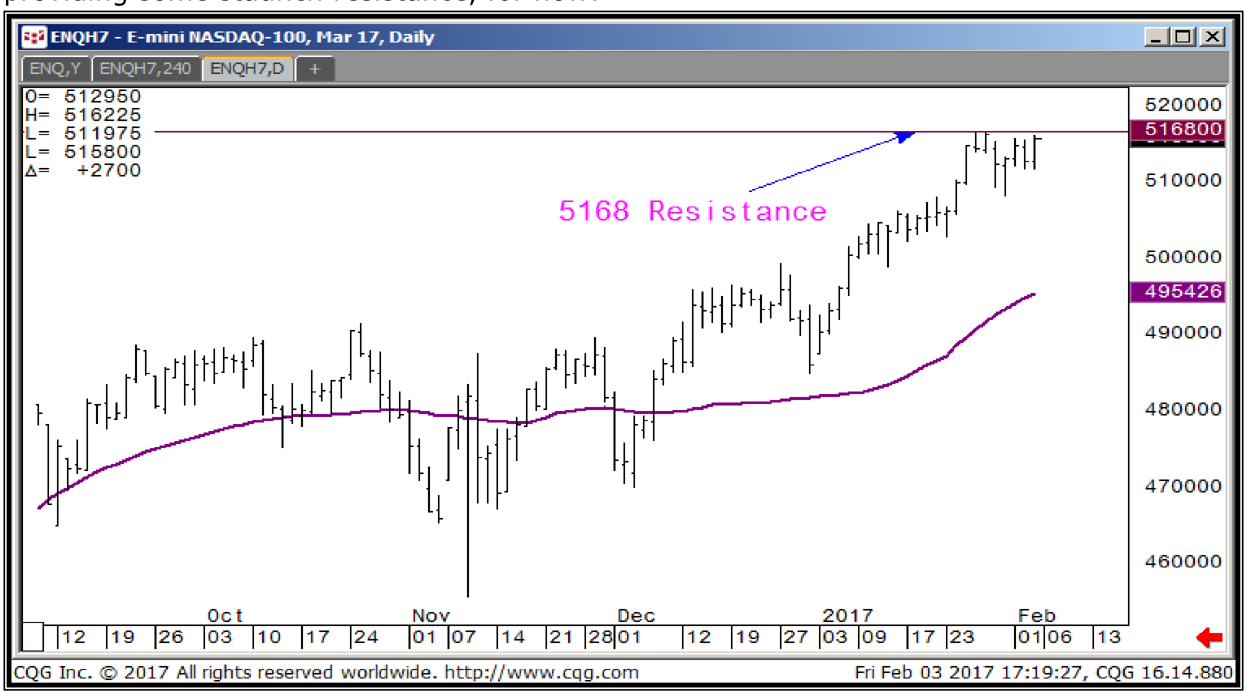
Moving on to the US Treasury yield curves, we can see that the ineptness of the FED has caused the curve to steepen somewhat as displayed by the 2s30 and 5s30 charts:



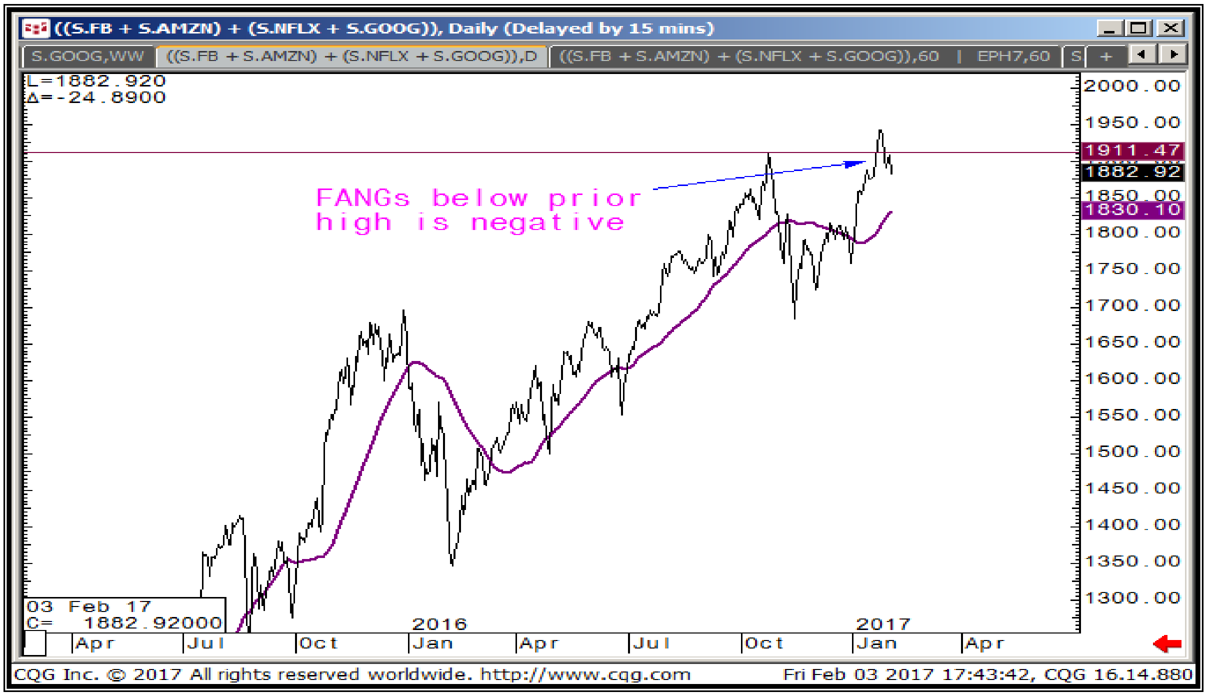


The SP500 chart continues to show strength above the current trend channel:

The Nasdaq however continues to butt head with the 5168 level which seems to be providing some staunch resistance, for now:



The FANGs chart is showing some deterioration led by Amazon's performance this week:

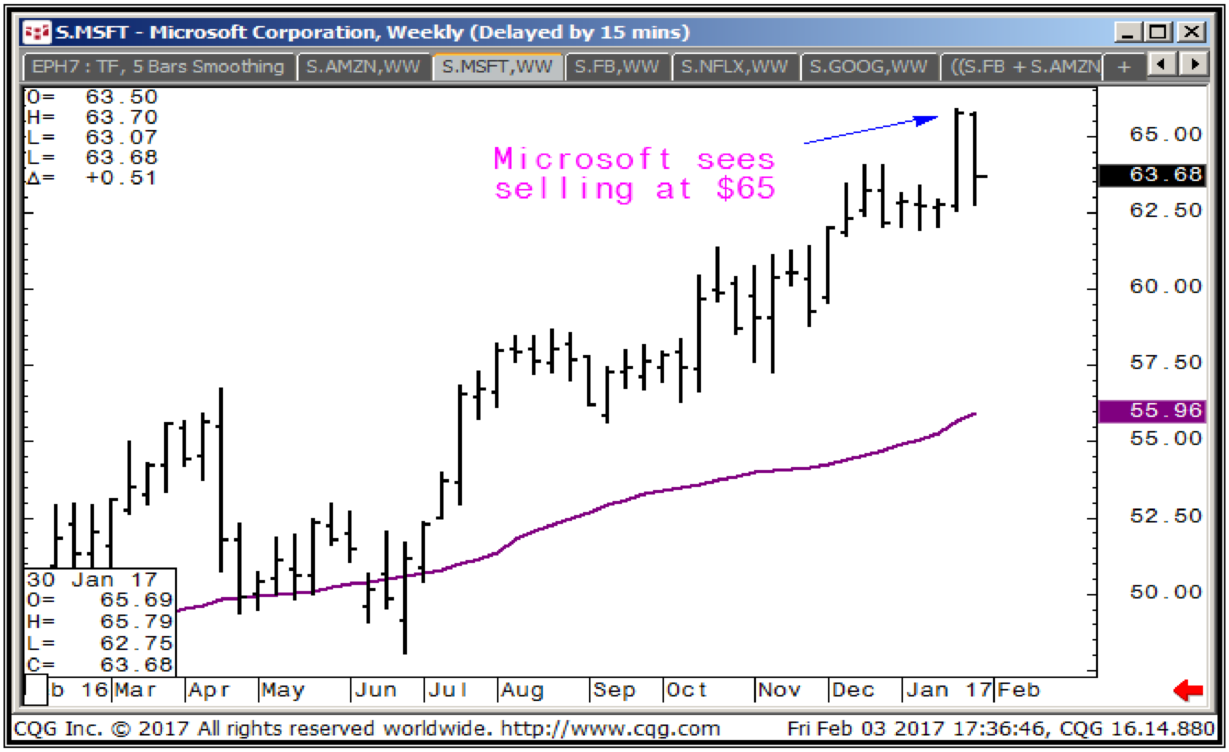


Let's look at a few individual equity charts leading off with Amazon:

Facebook, which looks bearish below $132:

Google sitting on $789 support:

Microsoft saw back to back large moves up then down:



Finally for the equities we have Netflix which has continued its meteoric rise:

Over in currency land we see both the Euro and Yen rising on the heels of a weak at the knees FED. The Euro continues to slowly rise and above 107-55 seems positive:

The Yen found footing at 85-00 and has climbed since mid Dec, 9085 seems logical:

All in all we suppose the week went as expected considering the no show FED and the better than expected rise in NFPayrolls to 227k while expecting only 175k. Equity algo took their cues and hit the buy button and the bond market put in a decent range to end up nearly unchanged on the week with the curve a bit steeper. Gold and Silver performed well up 2.5 and 2% respectively. Bitcoin continues to rise up 11% on the week. We added the Year to Date change to our weekly snapshot. Ok that's it, we will continue to provide ample and relevant coverage for you to digest throughout the year. We hope you stay with us and we hope that our letter stimulates your senses to inquire a bit more about the things we tend to discuss. We feel that this year will be full of surprises, both on an economic front as well as a political front and we will try to our best to keep you ahead of the game. We hope you enjoy the big game this weekend. Will it be Brady's last stand? We tend to think the Pats have an uphill battle in front of them though they are a 3 point favorite, which leads us non linear thinkers to believe they are baiting you to take the Pats. None the less we wish you luck with any pools and squares you may have partaken in, till next time…Cheers

3-Feb		Weekly	Weekly	YTD
Instrument	**Price/Yield**	**Net Change**	**% Change**	**% Change**
US 30yr Govt	3.11%	5 bp	-1.6%	-2.0%
US 10yr Govt	2.49%	1 bp	-0.4%	-2.4%
US 5yr Govt	1.93%	-1 bp	0.5%	-0.4%
MAR Bond	150-01	-0'11	-0.23%	-0.06%
MAR Ten Yr	124-09	0'03+	0.09%	-0.05%
MAR Five Yr	117-24+	0'012	0.03%	0.23%
MAR SP500	2291	2	0.1%	2.4%
MAR DOW	19986	-26	-0.1%	1.3%
MAR Nasdaq	5155	-7.5	-0.1%	6.0%
MAR Nikkei	19050	-420	-2.2%	0.1%
MAR Dax	11661.5	-152	-1.3%	1.7%
Shanghai Comp	3140.17	-19	-0.6%	1.2%
MAR WTI Crude	$53.83	$0.66	1.2%	-1.8%
APR Gold	$1,220.80	$29.70	2.5%	5.8%
MAR Silver	$17.48	$0.34	2.0%	9.3%
MAR Dollar Index	$99.84	-$0.68	-0.7%	-2.4%
MAR EURO	107.82	0.66	0.6%	2.0%
MAR YEN	88.630	1.59	1.8%	3.1%
Bitcoin (BTC)	1,023.54	101.36	11.0%	7.3%

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