Macro Chart Pack

Tactical Risk Assessment Framework

9th December 2018, **MCP-020**

In markets, participants are discounting a world full of extremely complex and constantly changing information... to try and 'out-compute' the complexities of the world is difficult, it is much easier just to "play the players" - looking to identify behaviour shifts when it matters.

These charts merely highlight a potential 'tactical context' for each of the markets covered, acting as a catalyst for further research.

The framework is designed to complement your risk assessment processes, not to replace them. Past performance is not necessarily indicative of future results.

"...the intelligent trader who has patiently waited to determine this line [of least resistance] will enlist the aid of fundamental trade conditions and also of the force of the trading of that part of the community that happened to guess wrong and must now rectify mistakes."

...Jesse Livermore (1877-1940)

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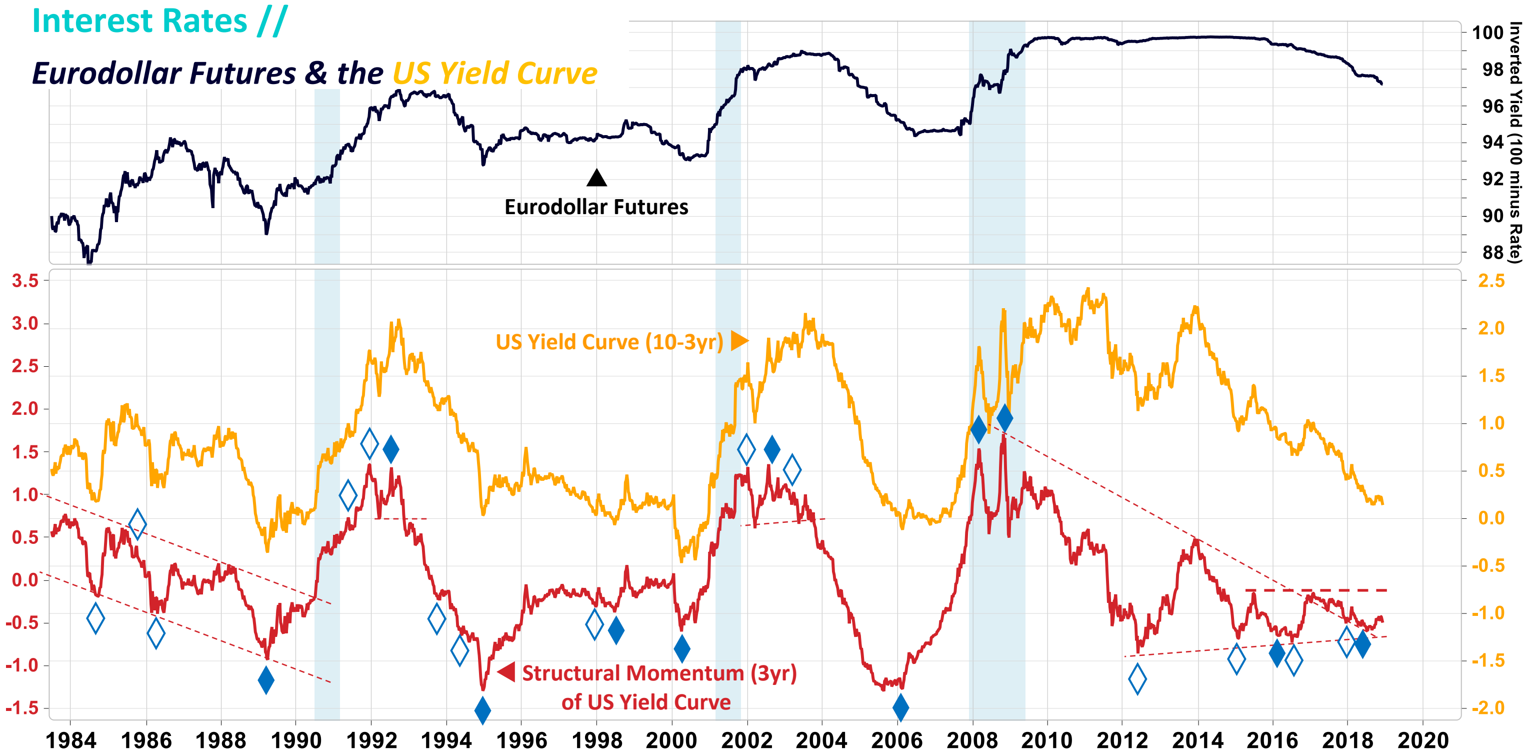
"...focus on the movement of liquidity... most people in the market are looking for earnings and conventional measures. It's liquidity that moves markets."

...Stanley Druckenmiller

Interest Rates //

Eurodollar Futures & the US Yield Curve

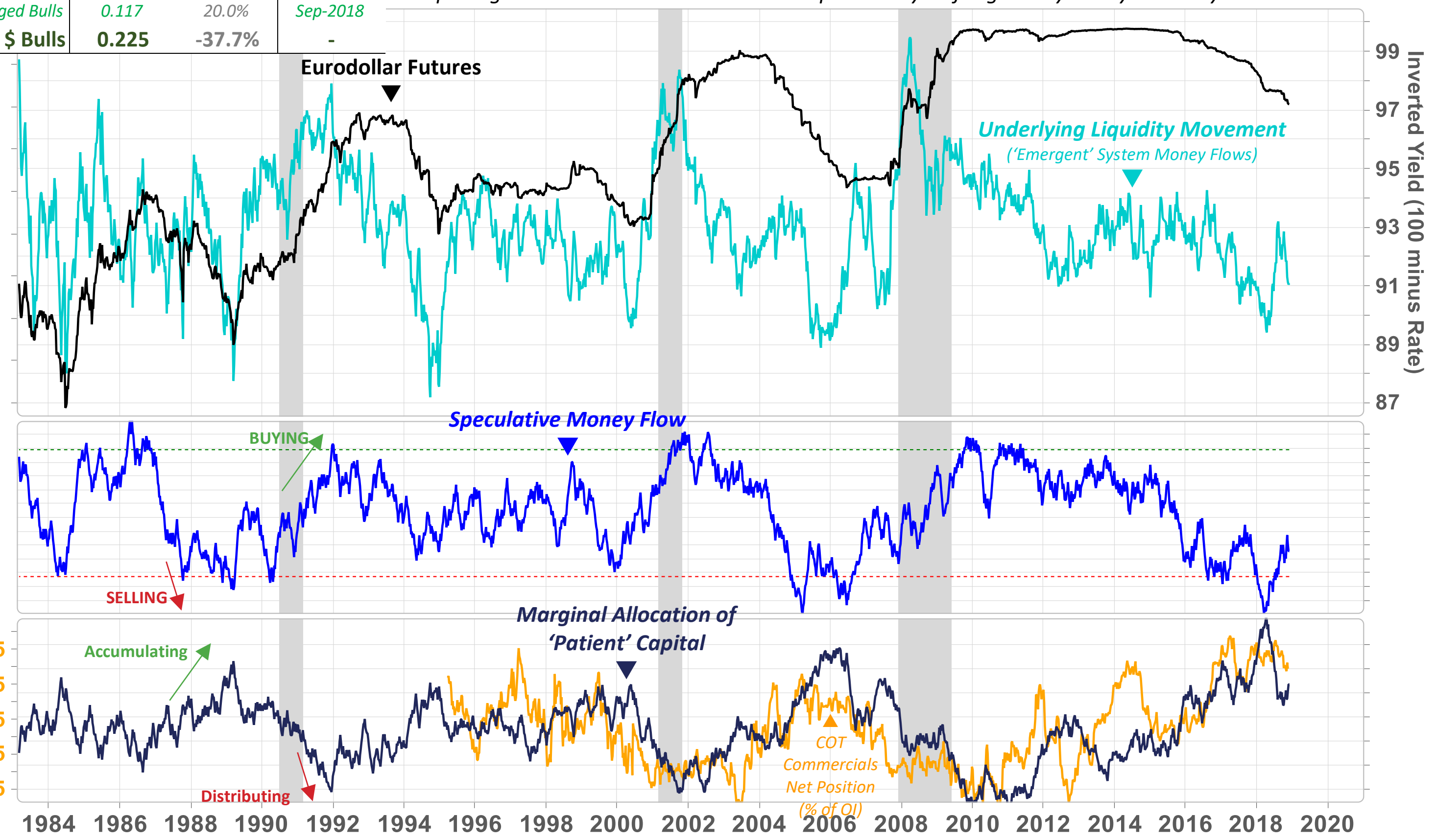


10-3yr YIELD CURVE

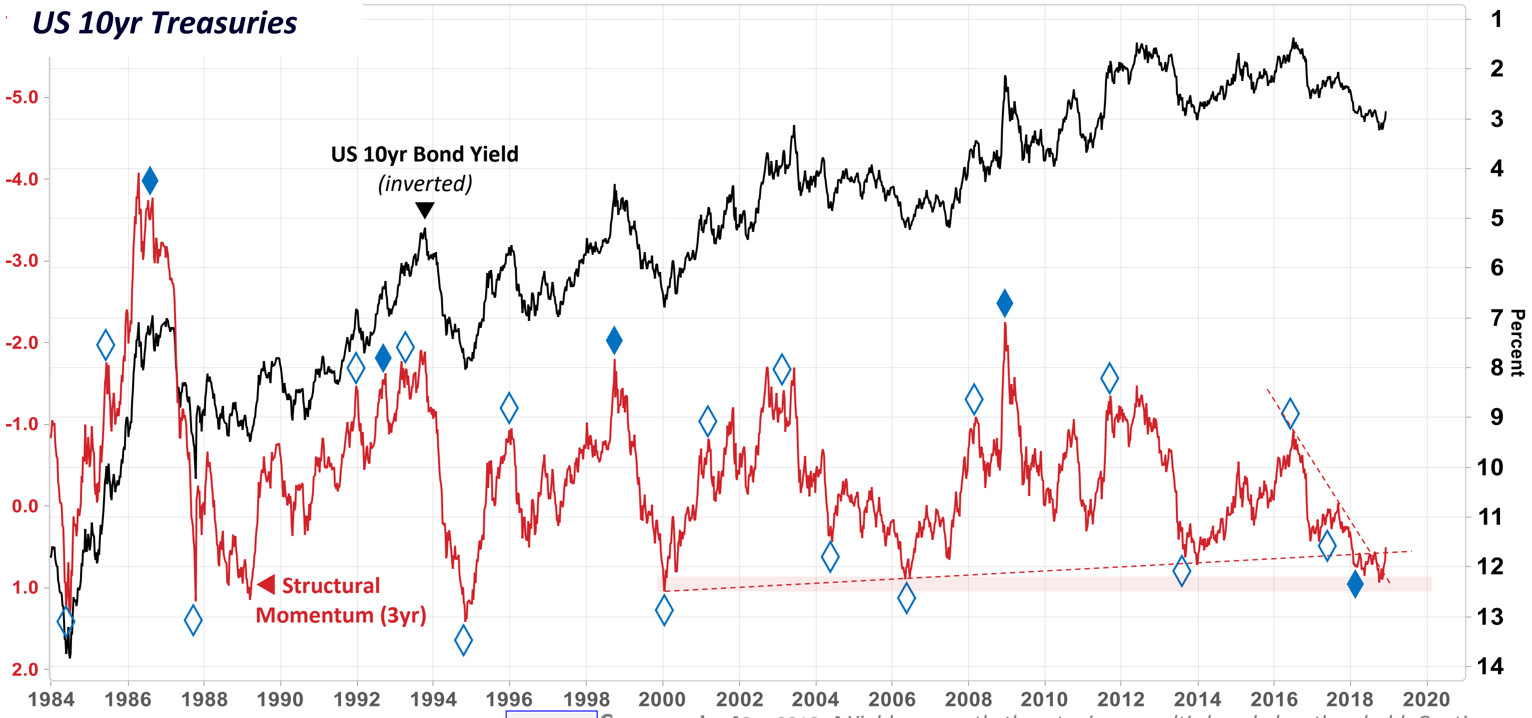
Last Weekly Close: **0.140**

	Point of Control *(Threshold)*	*Perception of Control (Distance)*	***Date Control Began***
Real $ Bears	**0.805**	**82.6%**	**Jul-2011**
Leveraged Bears	*0.418*	*66.5%*	*Jan-2014*
Leveraged Bulls	*0.117*	*20.0%*	*Sep-2018*
Real $ Bulls	**0.225**	**-37.7%**	**-**

Comments: **[Jan-2018…]** *Clearly the Speculative & Patient Money flows are indicative of 'top of cycle' conditions – wherein we would usually expect a reversal in monetary policy in addition to possible recessionary conditions as soon as late 2018. Whether this occurs or not, or whether we have a more sustained and extended cycle remains to be seen, but it is interesting to note the level of conviction demonstrated by the different participant groups. Structural Momentum of the Yield Curve is such that any upside break could be significant.* **[Dec-2018…]** *By the end of 2019 we suspect we'll have both the yield curve steepening in addition to Eurodollar Futures potentially shifting into cyclically side-ways to bullish conditions.*



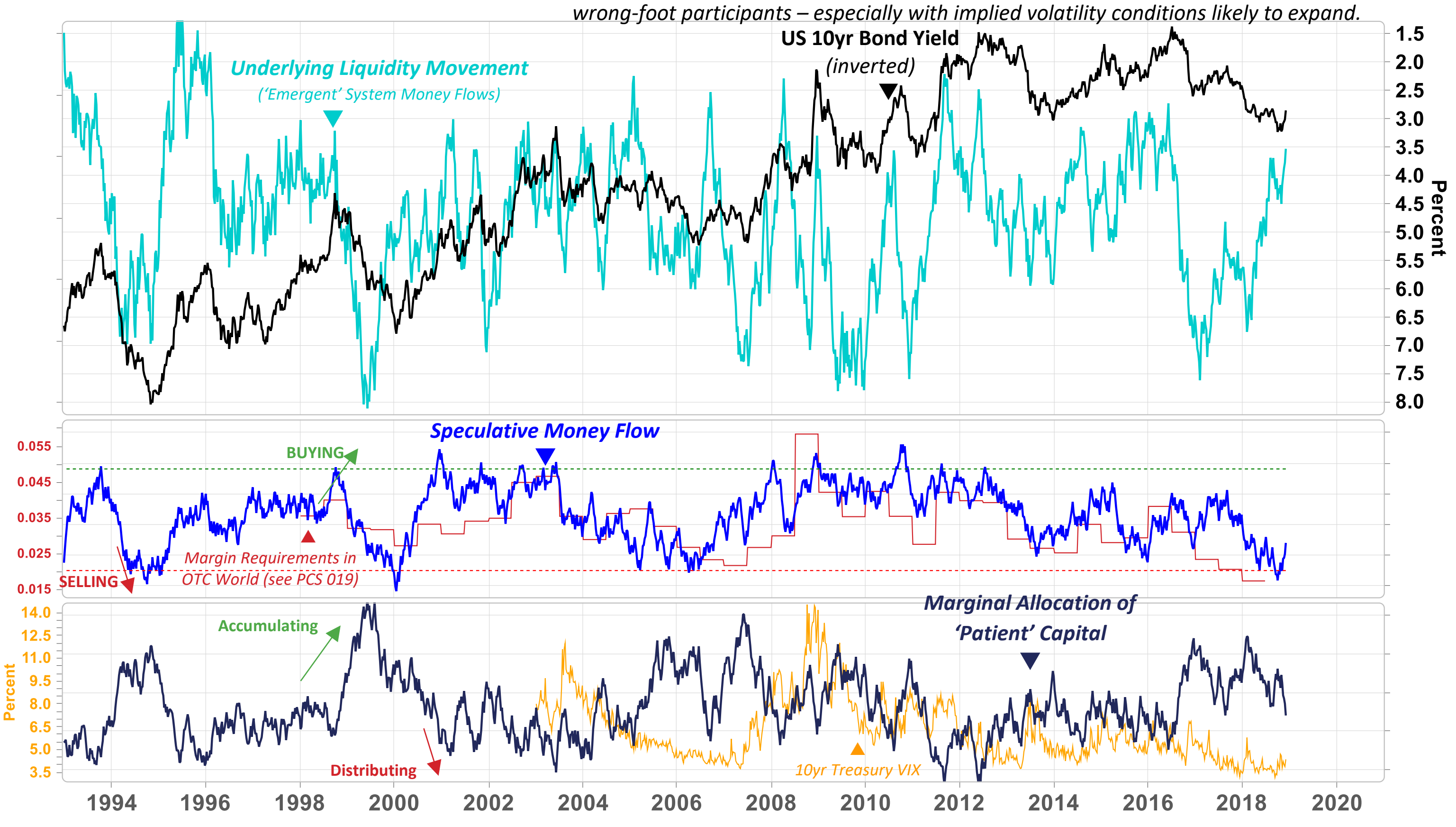
US 10yr Treasuries

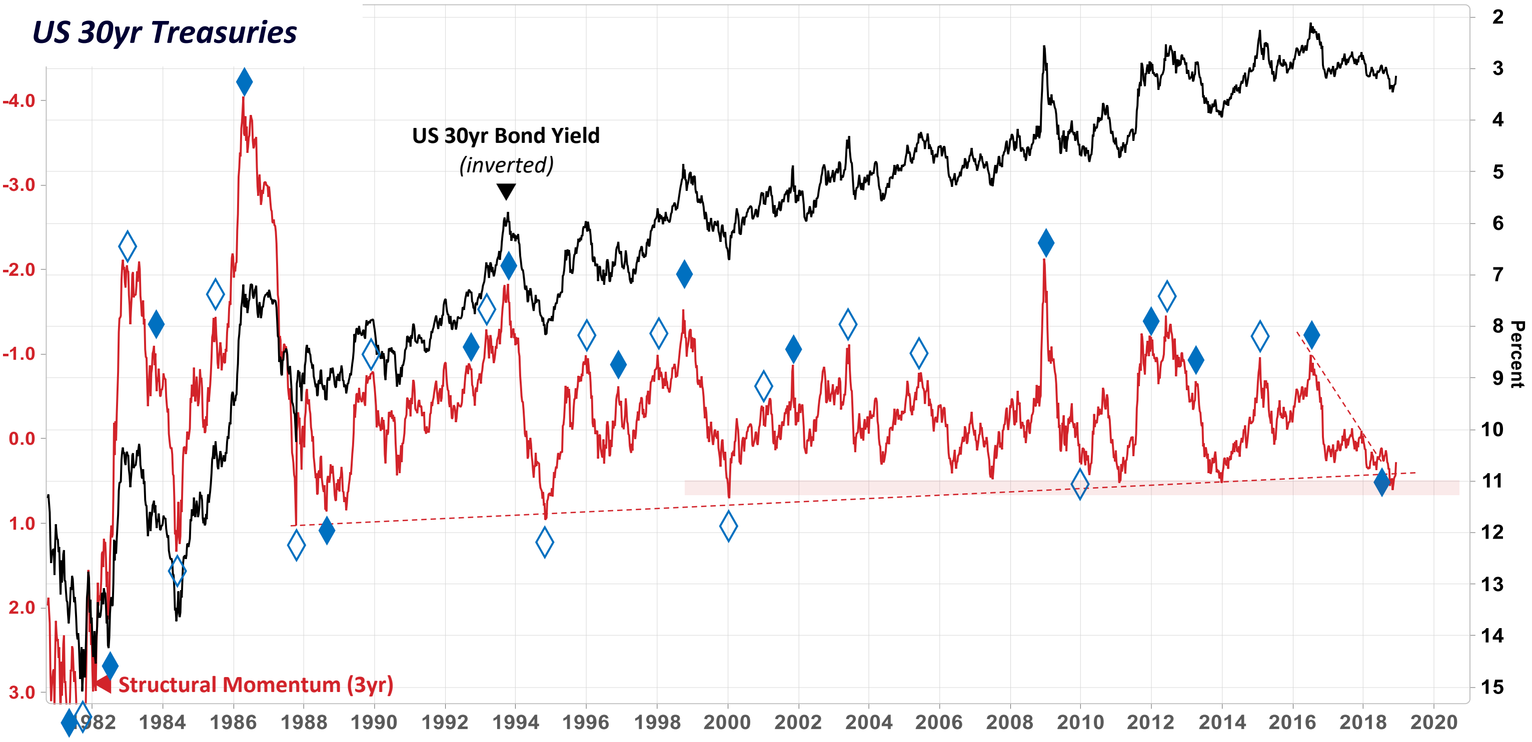


Last Weekly Close: 75.50 → **2.85%**

	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began	Equiv. Yield
Real $ Bears	80.27	5.9%	Sep-2016	2.22%
Leveraged Bears	76.45	1.2%	Sep-2016	2.72%
Leveraged Bulls	73.45	2.8%	Nov-2018	3.13%
Real $ Bulls	75.82	-0.4%	-	2.81%

Comments: [Oct-2018…] *Yields presently threatening a multi-decade key threshold. Caution advised. Broader Money Flows and Implied Volatility patterning still suggestive that Yields more likely to fall from here (rather than break the multi-decade threshold). Major Liquidity signal at the beginning of the year tips probabilities towards 3yr SM being in a bottoming process ahead of a turn higher. Other sovereign bond markets (elsewhere in this report) also supportive of this likelihood, as is the weakness in equity markets.* **[Dec-2018…]** *This will likely prove to be another significant bond buying opportunity on a multi-year basis. The underlying liquidity coming into the market at these levels amidst a Speculative washout will wrong-foot participants – especially with implied volatility conditions likely to expand.*




US 30yr Treasuries
US 30yr Bond Yield
(inverted)
Structural Momentum (3yr)
Percent
-4.0
-3.0
-2.0
-1.0
0.0
1.0
2.0
3.0
2
3
4
5
6
7
8
9
10
11
12
13
14
15
1982
1984
1986
1988
1990
1992
1994
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1998
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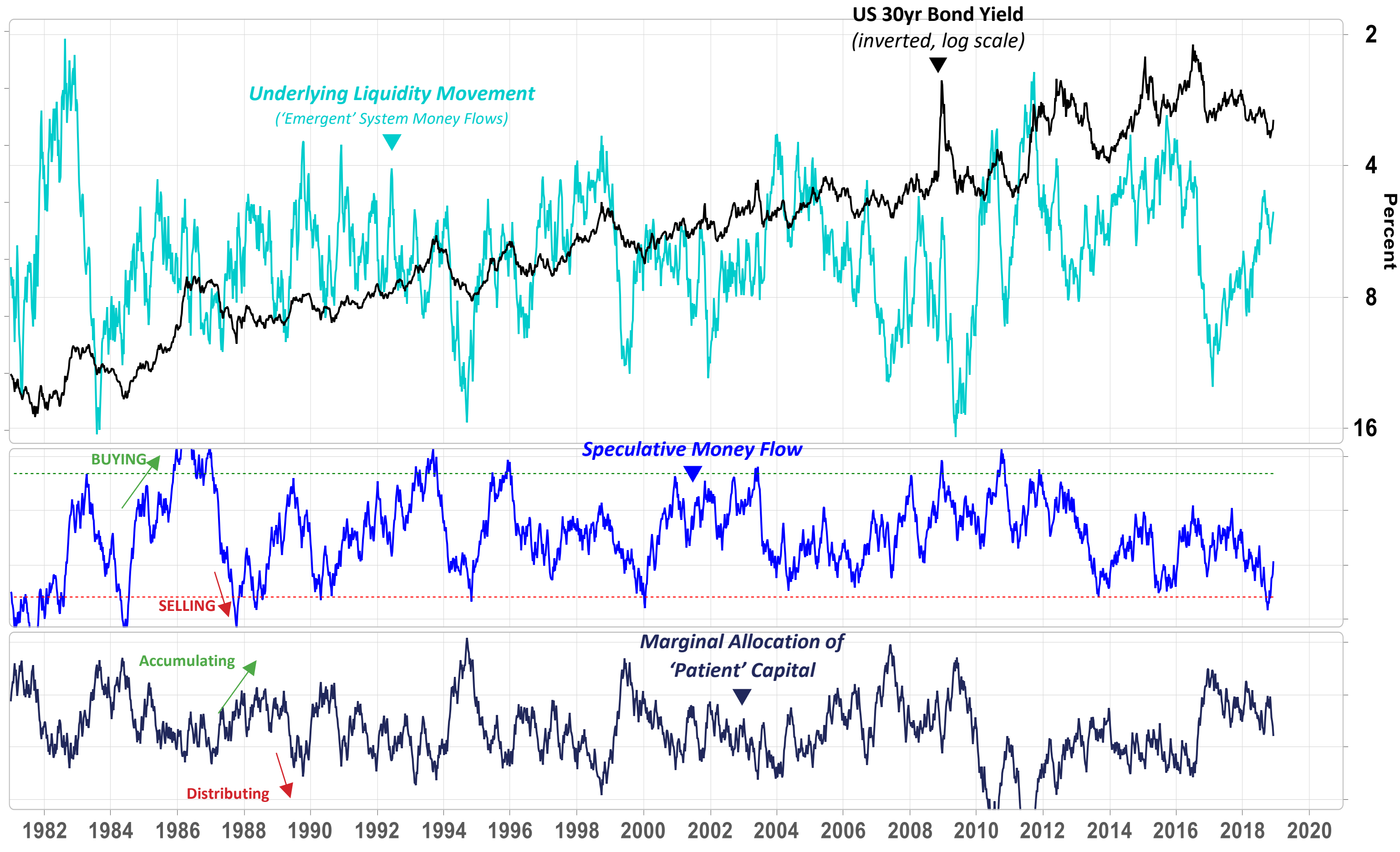
2004
2006
2008
2010
2012
2014
2016
2018
2020


US 30yr Bond Yield
(inverted, log scale)
Underlying Liquidity Movement
('Emergent' System Money Flows)
Percent
2
4
8
16
Speculative Money Flow
BUYING
SELLING
Marginal Allocation of
'Patient' Capital
Accumulating
Distributing
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
2002
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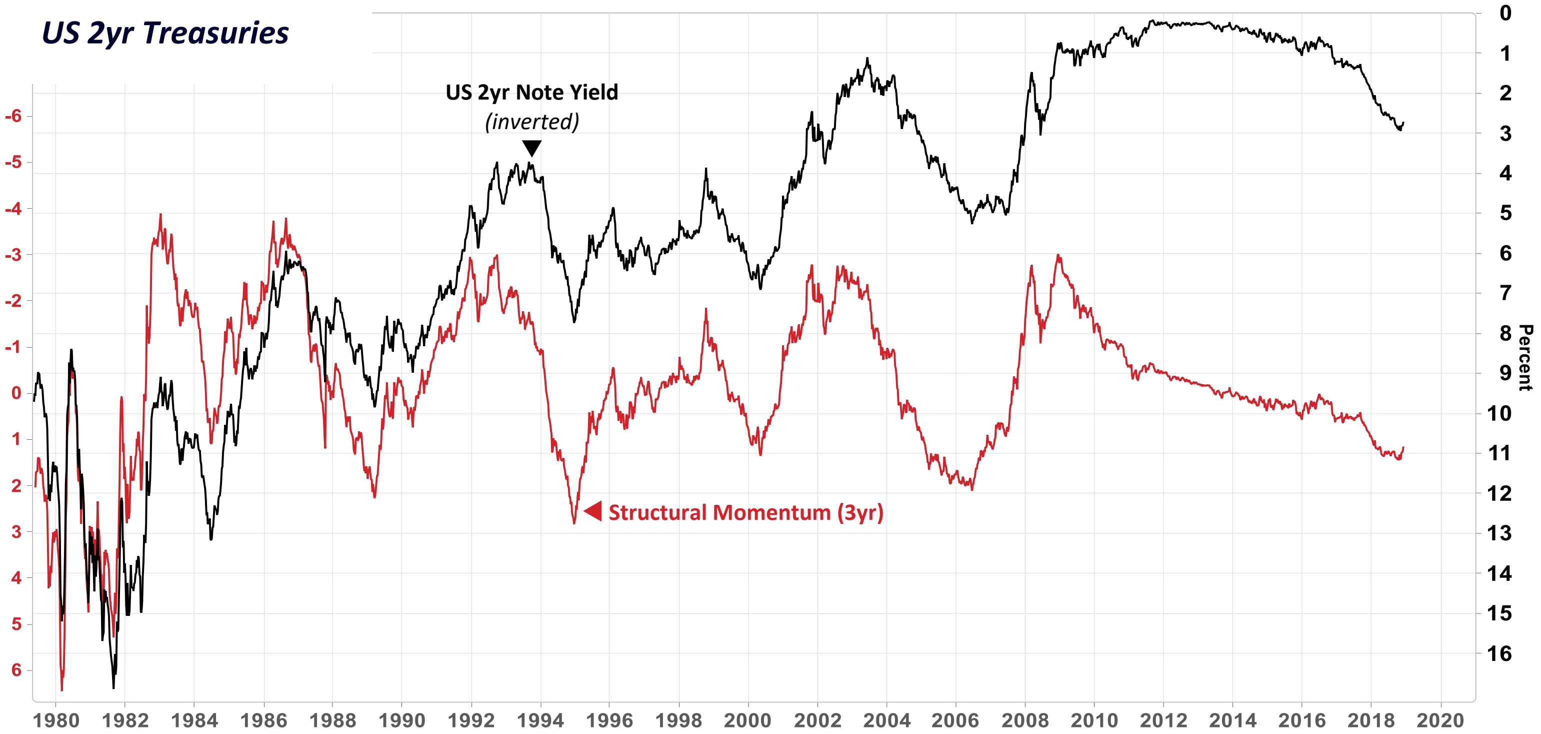
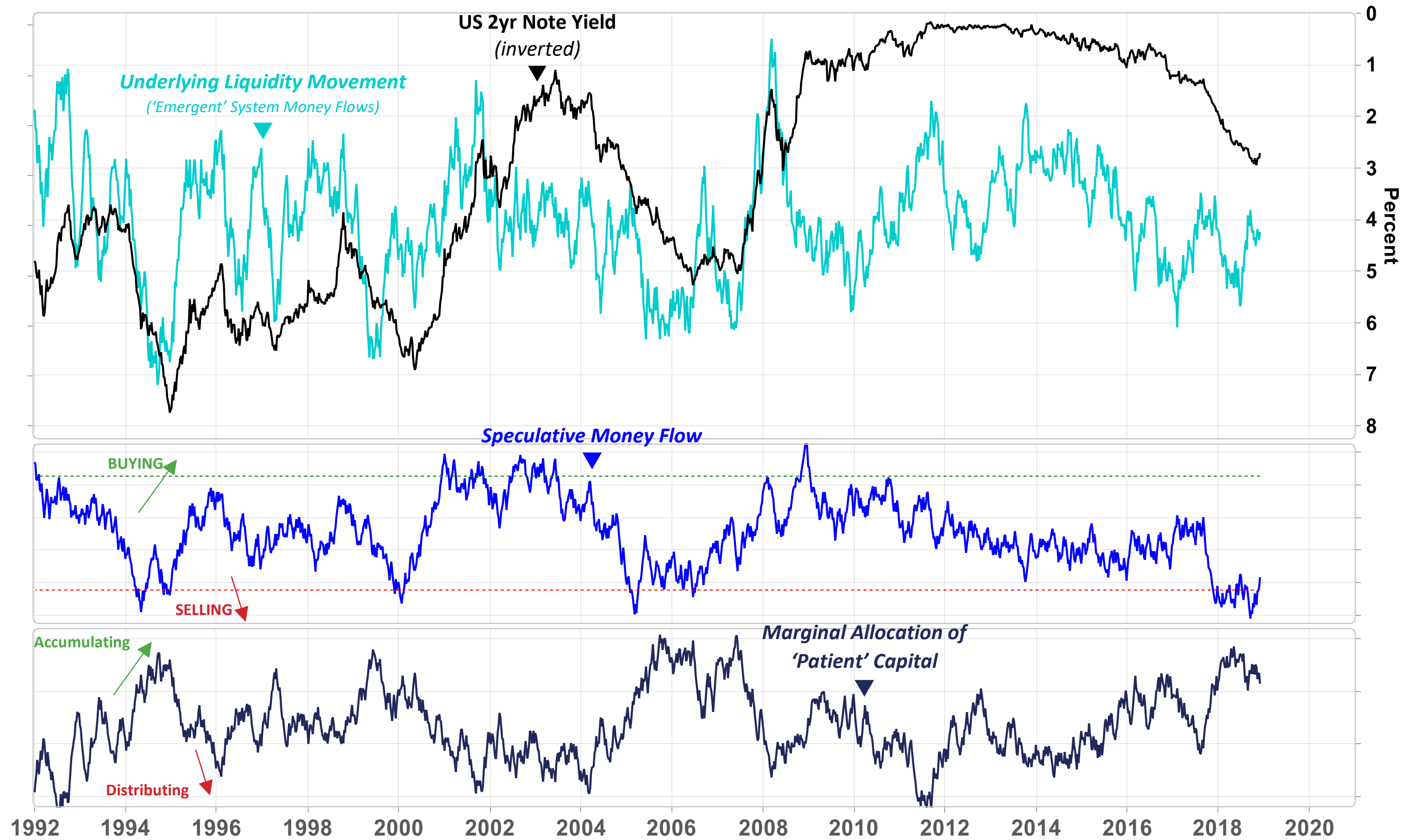
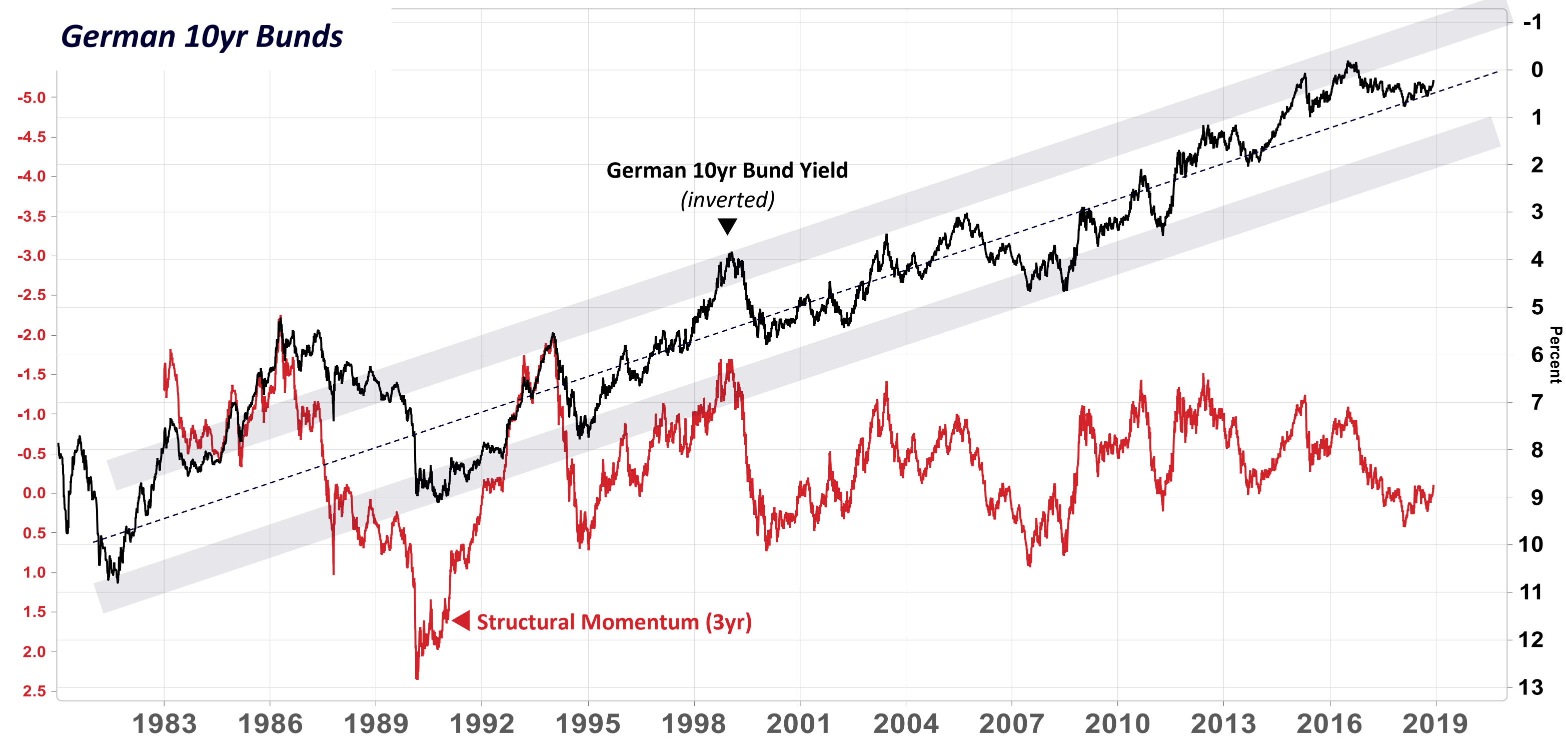
2006
2008
2010
2012
2014
2016
2018
2020

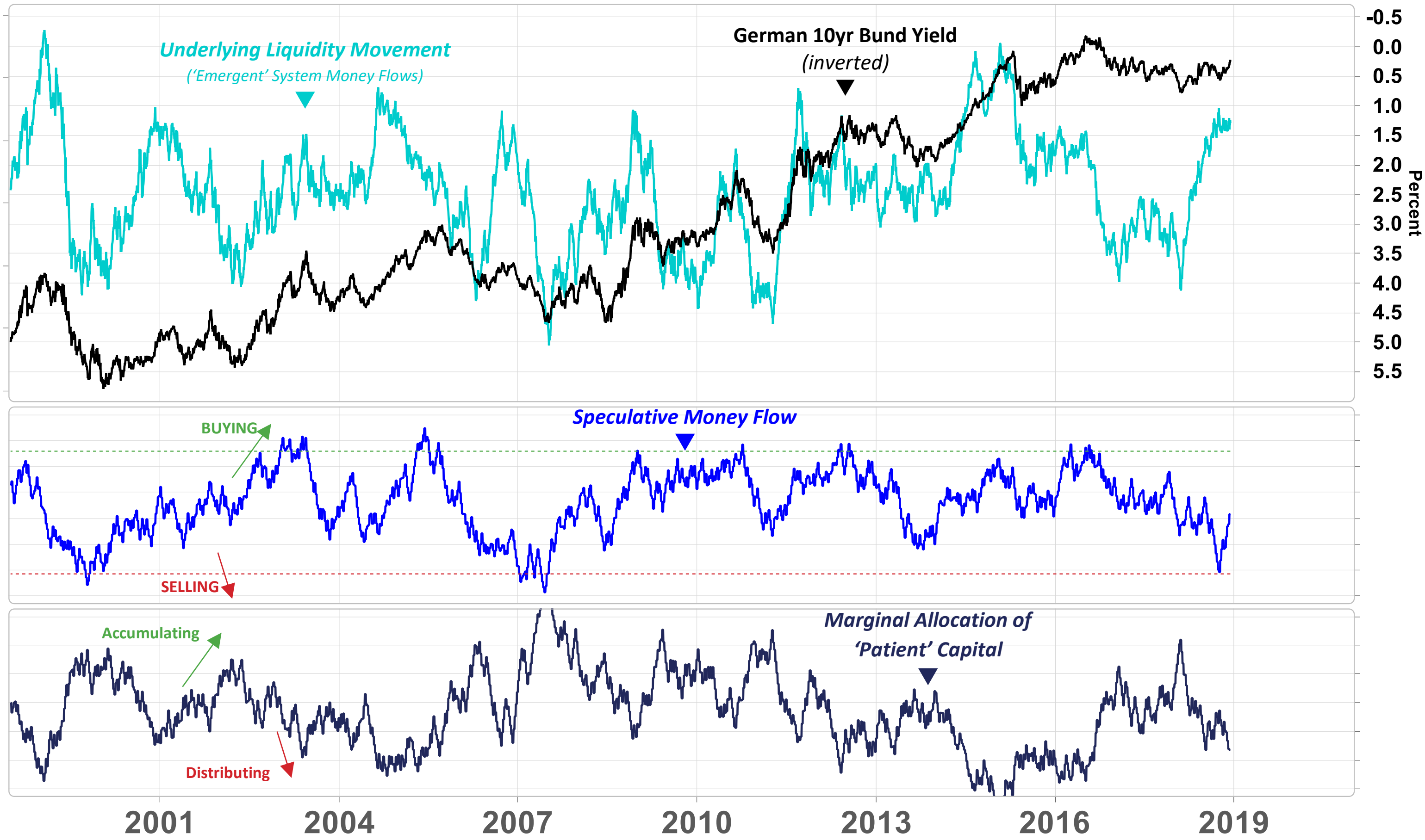
US 2yr Treasuries



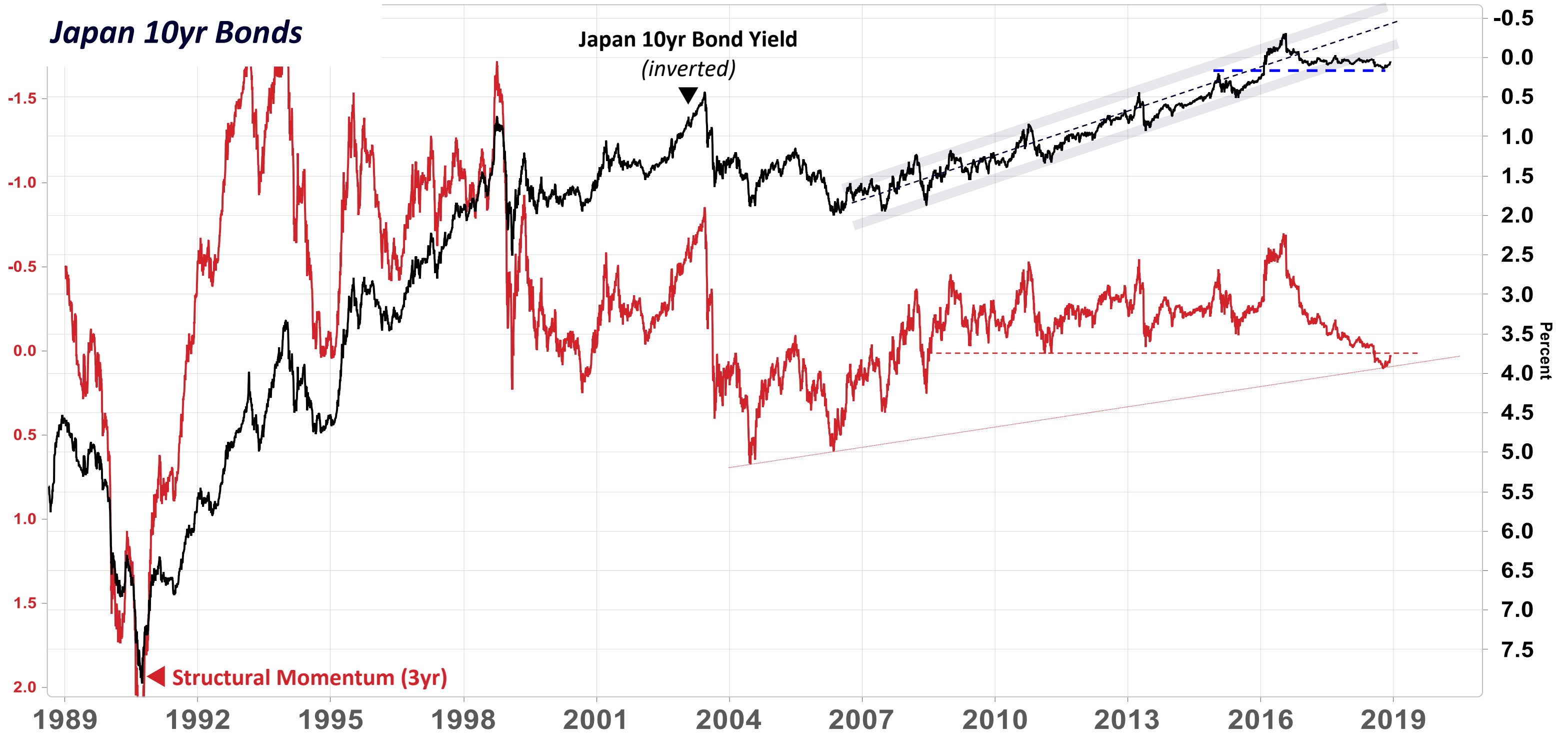


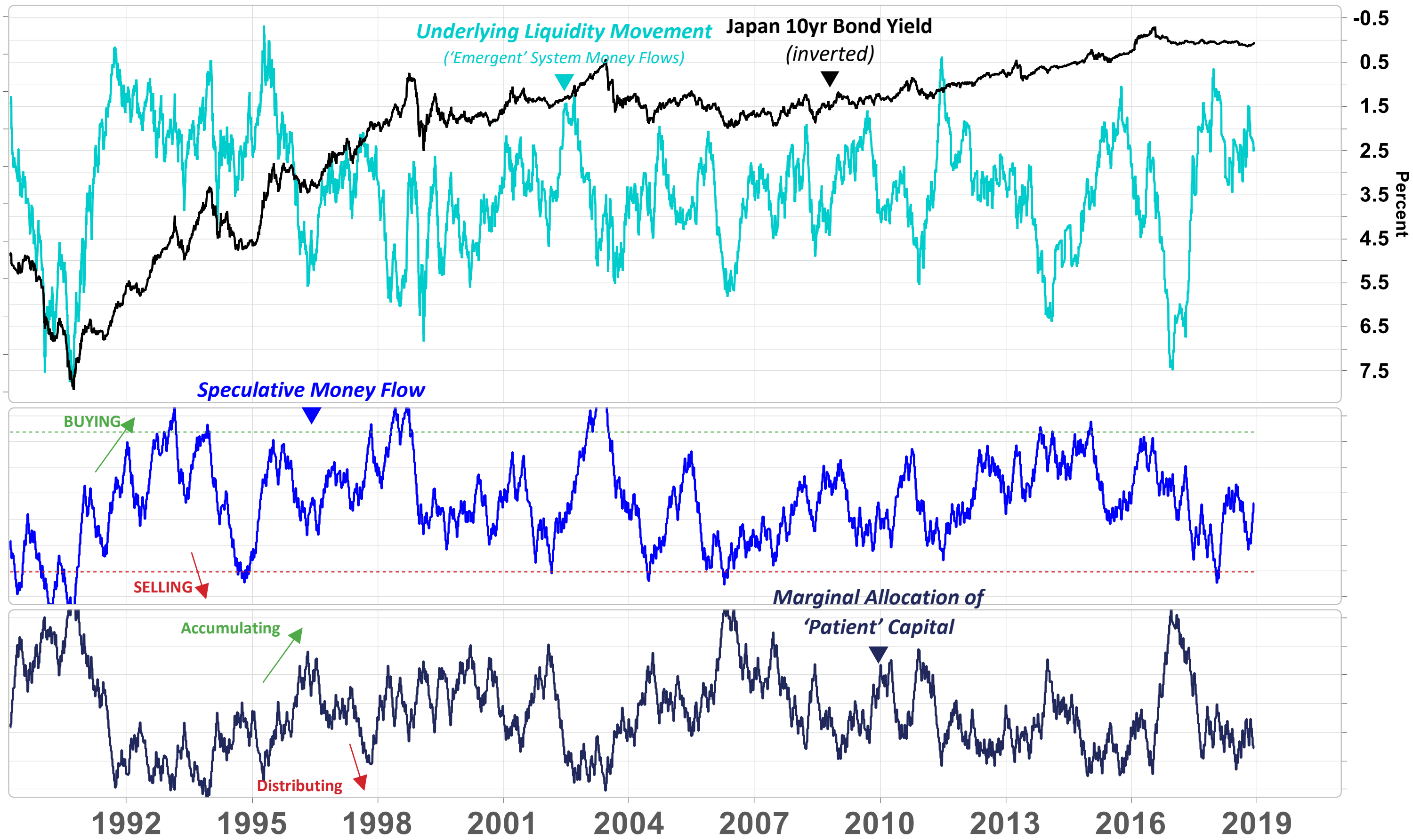
German 10yr Bunds



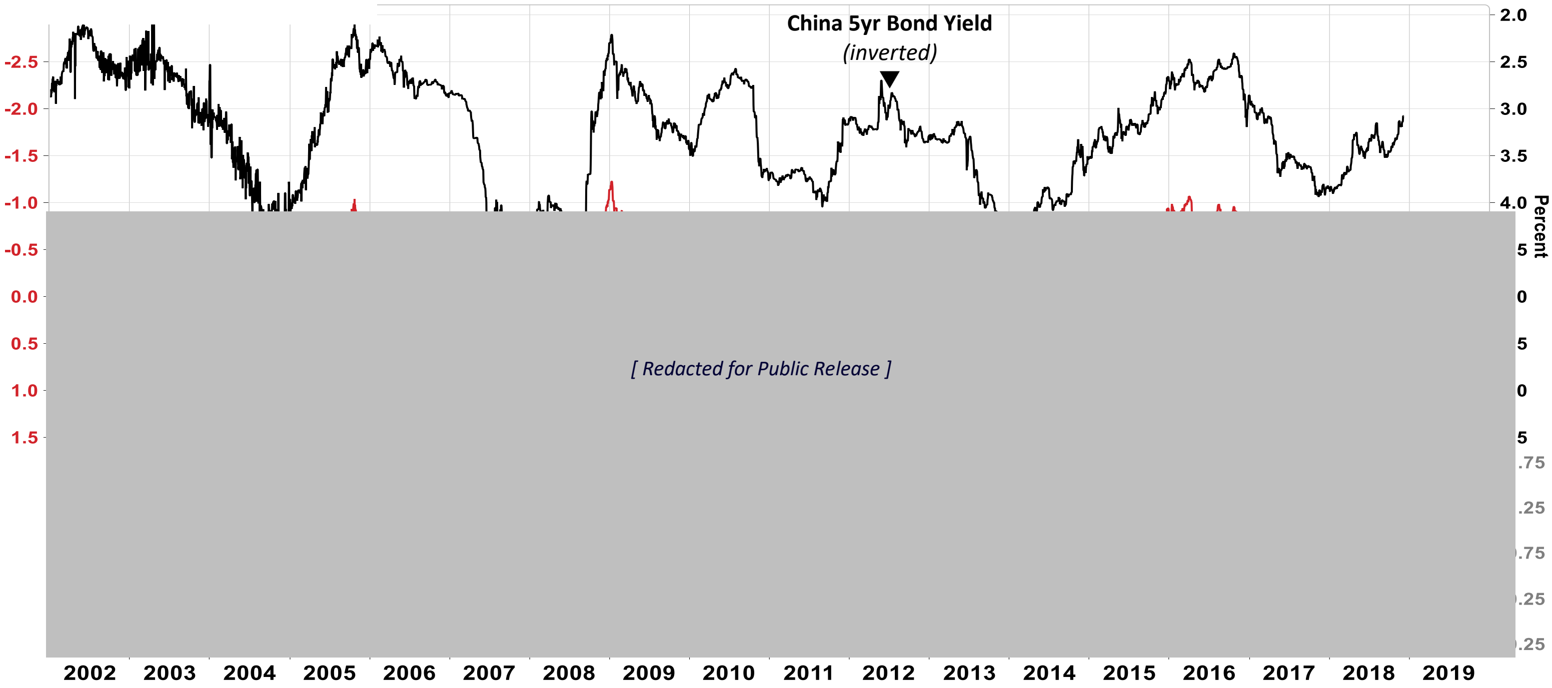


Japan 10yr Bonds



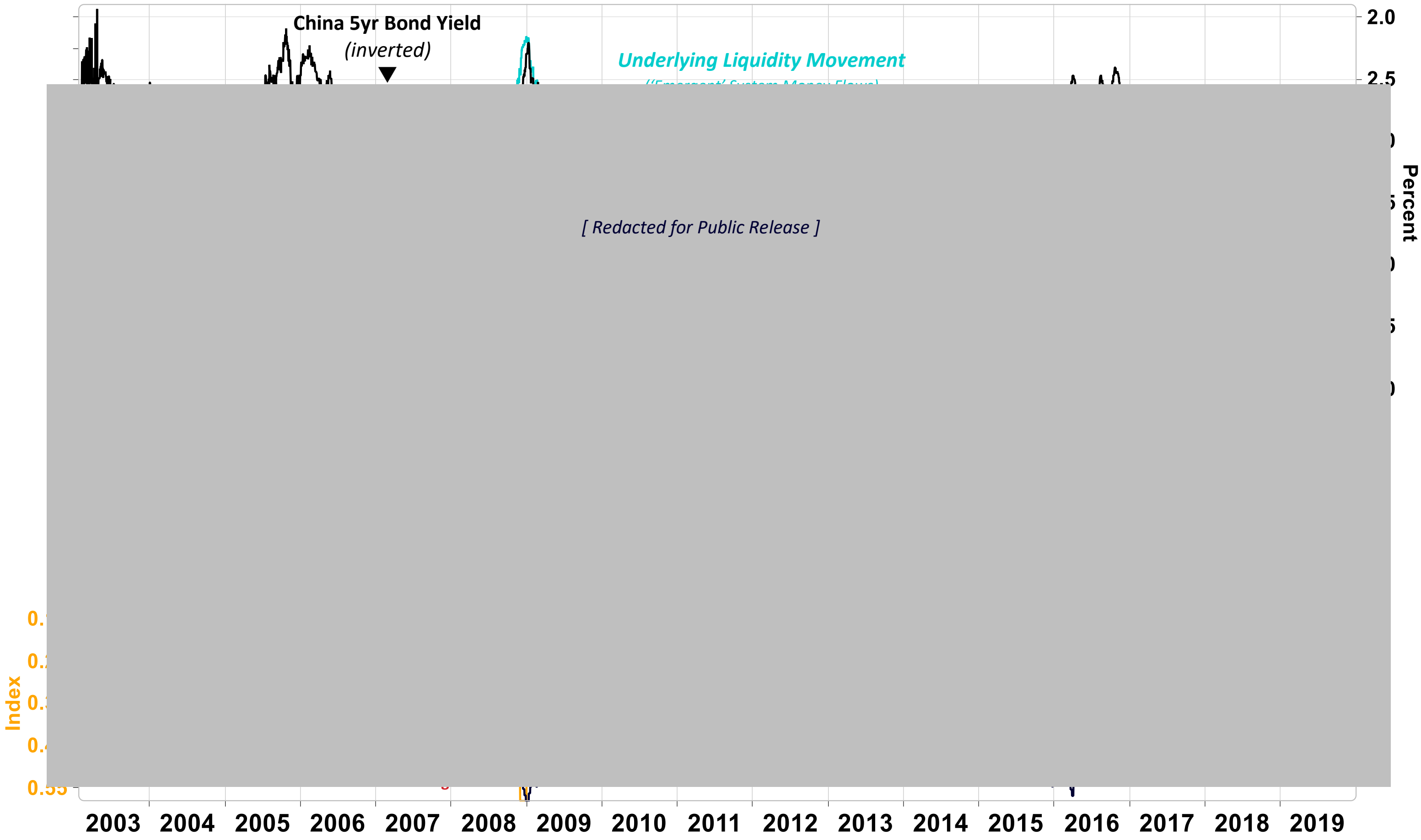


China 5yr Bonds

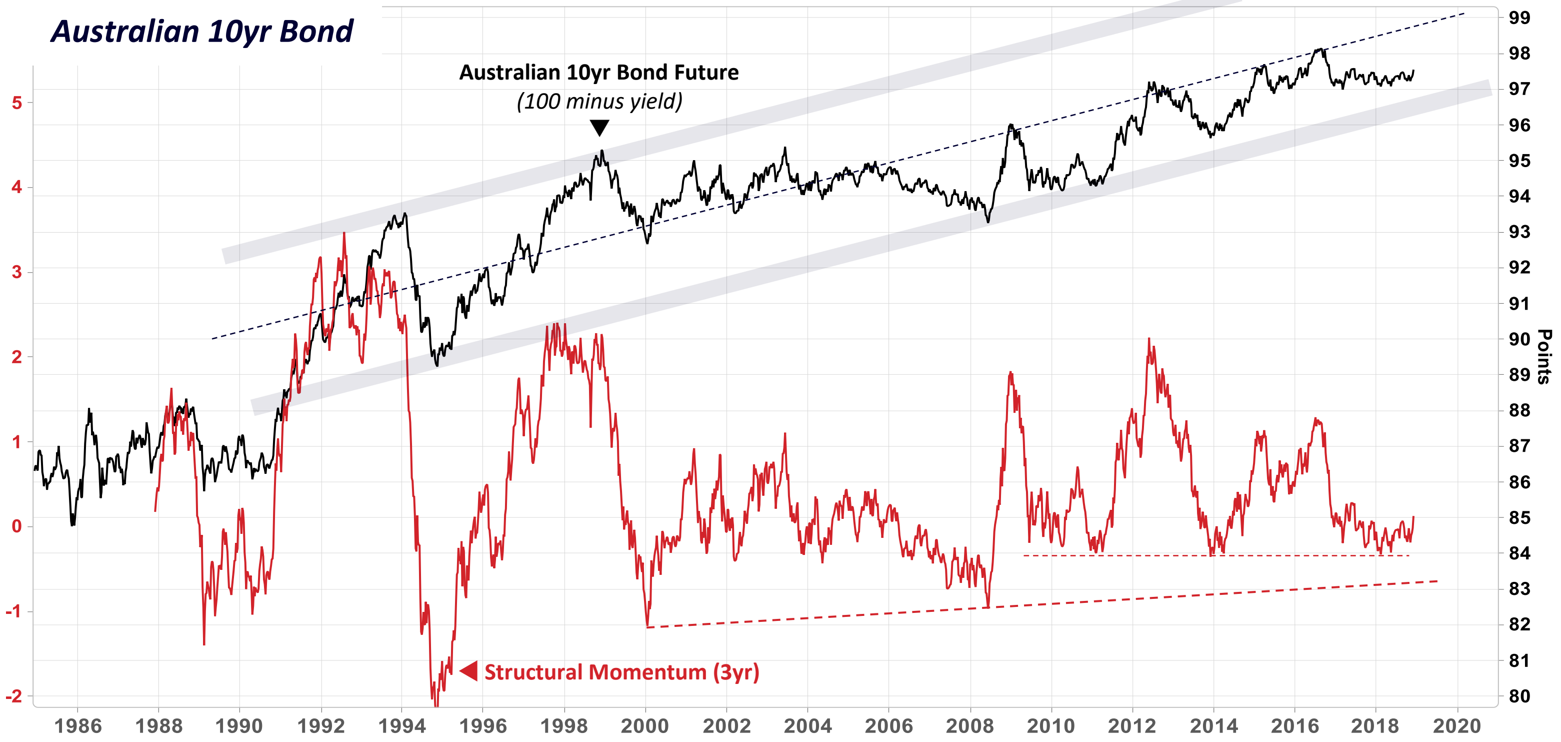


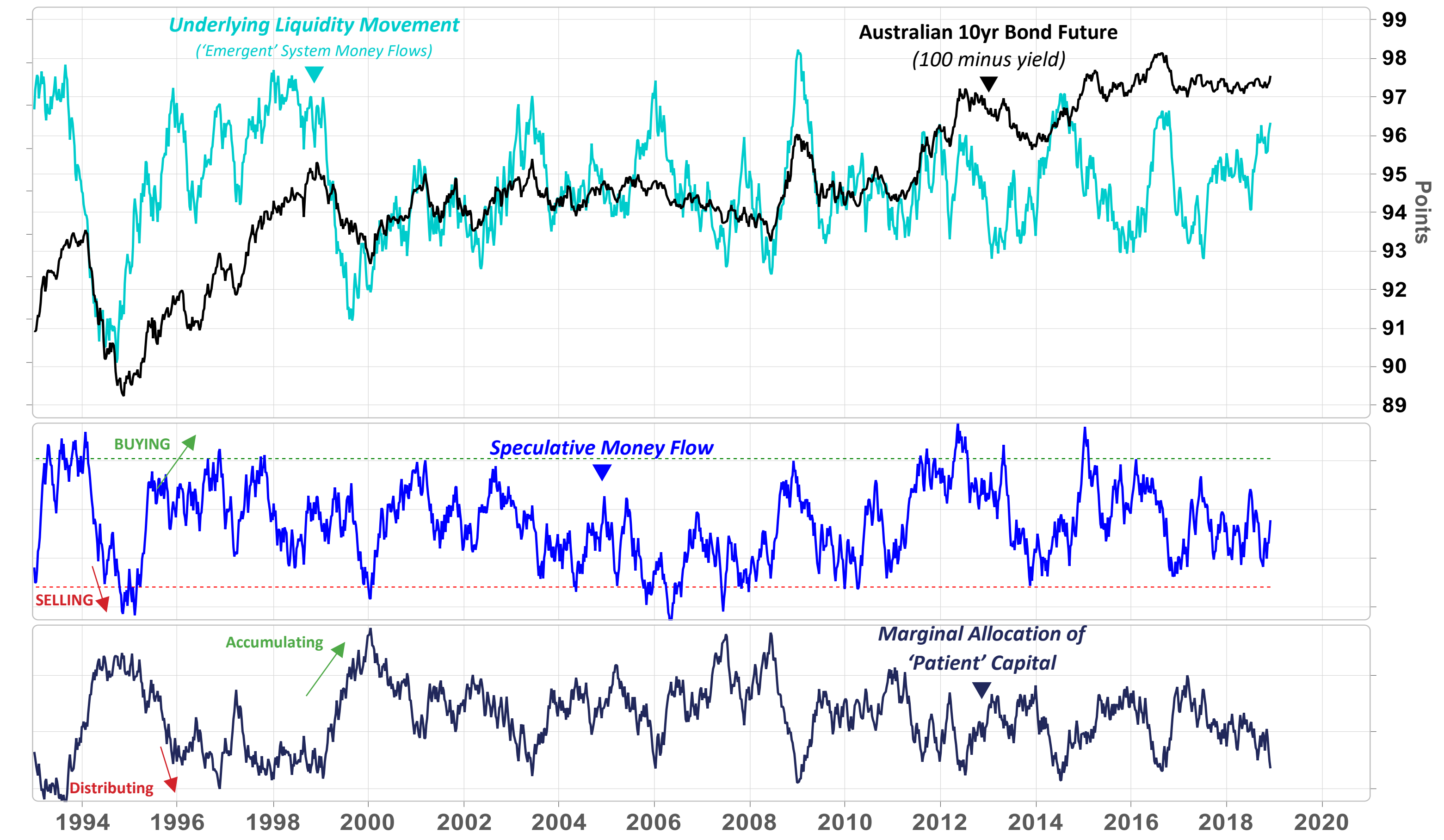
Comments:

[No change to comments from January] *The setup here is suggestive of another one of the 2-4 year 'sub-cycles' rolling over - with negative surprises to both growth and inflation conditions within China implied for the next year or so.*

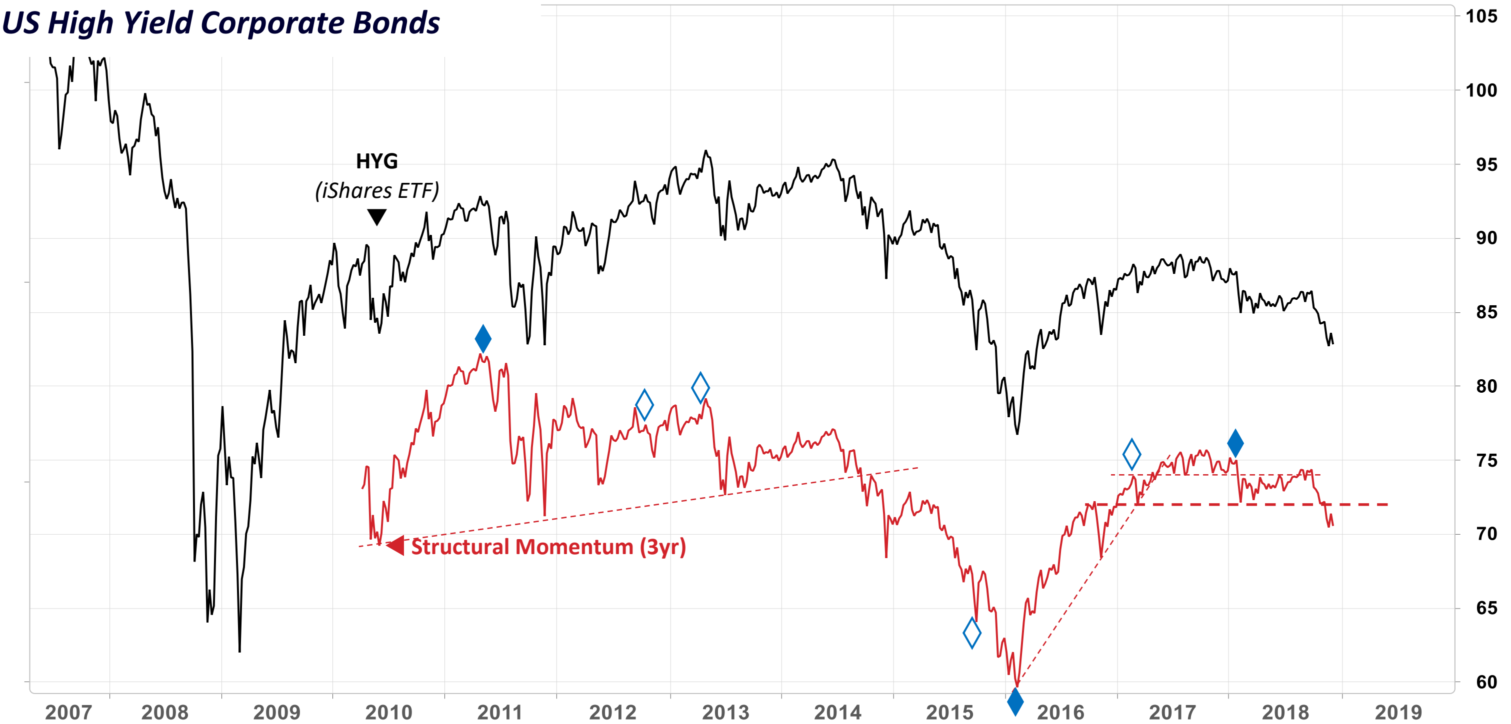


Australian 10yr Bond





US High Yield Corporate Bonds

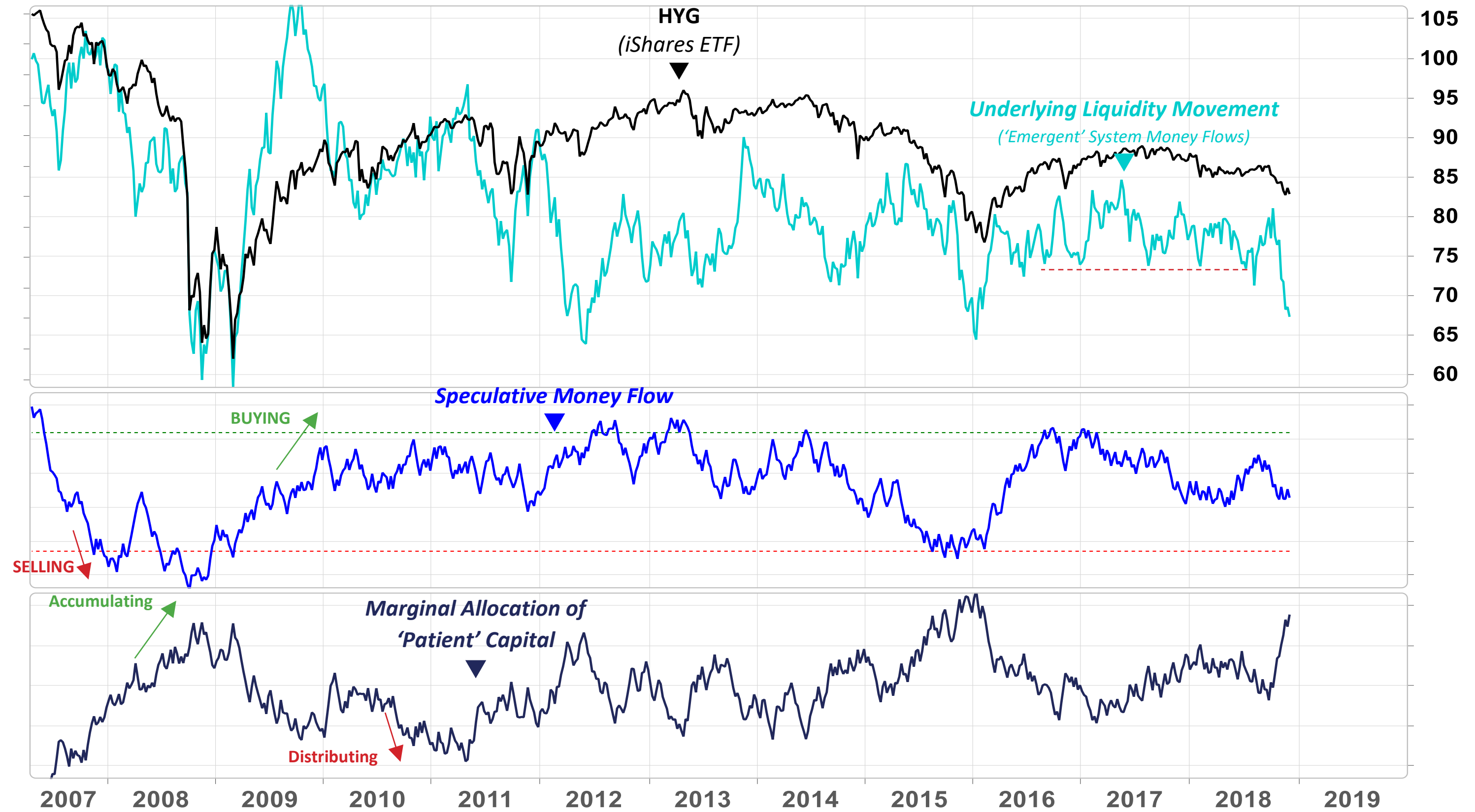


***Last Weekly Close:* 82.83**

	Point of Control (Threshold)	*Perception of Control (Distance)*	*Date Control Began*
Real $ Bears	**85.78**	**3.4%**	**Feb-2018**
Leveraged Bears	*86.01*	*3.7%*	*Apr-2017*
Leveraged Bulls	*84.16*	*-1.6%*	*Apr-2016*
Real $ Bulls	**82.34**	**0.6%**	**Jun-2016**

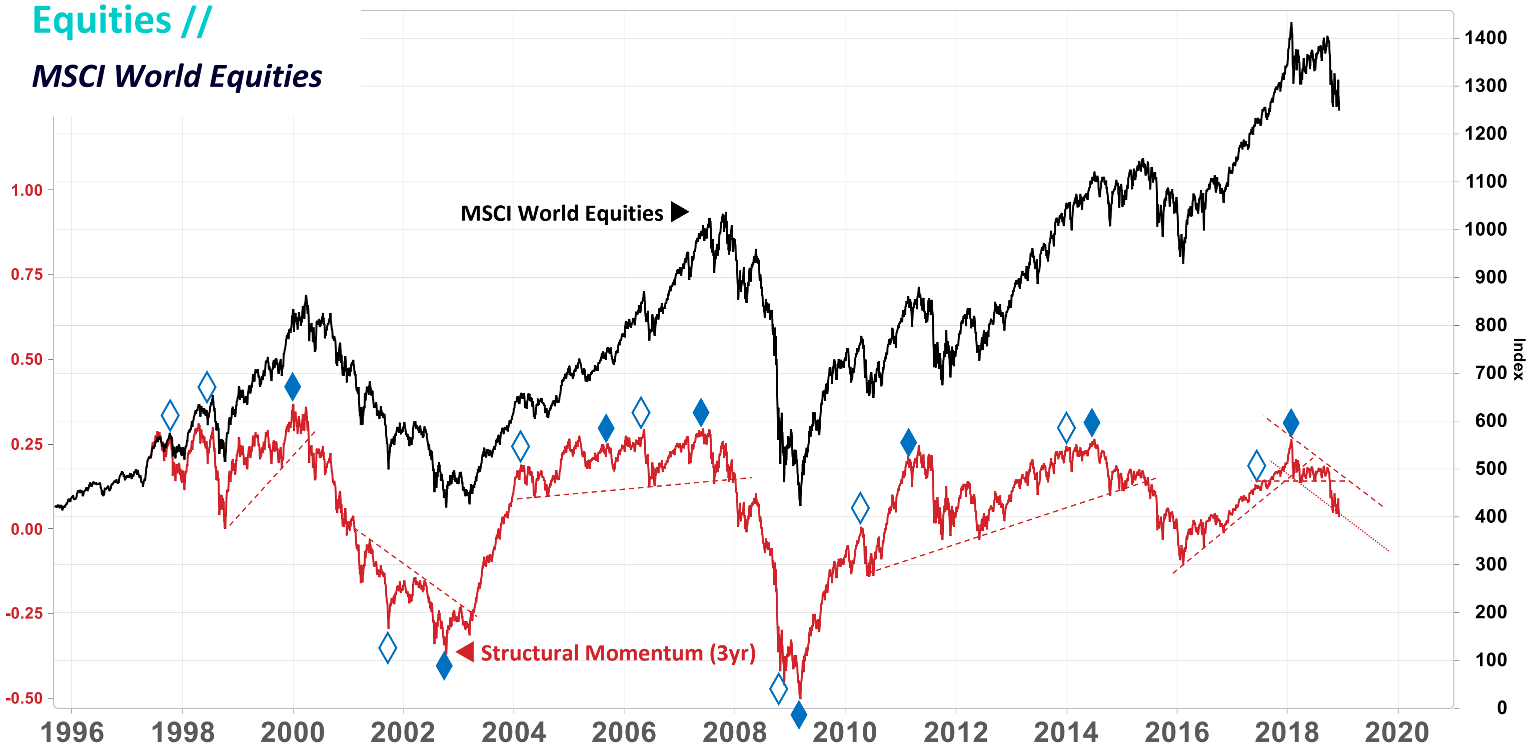
Comments:

[No change to comments from March] *Since the spike in equity volatilities the corporate high-yield complex has been noticeably weak and non-responsive to the moderation in volatilities since the spike. The major liquidity turning point signal triggered prior to the volatility spike suggests that downside risks remain and that the present horizontal support on the 3yr structural momentum is likely to be tested again and potentially broken to the downside.*



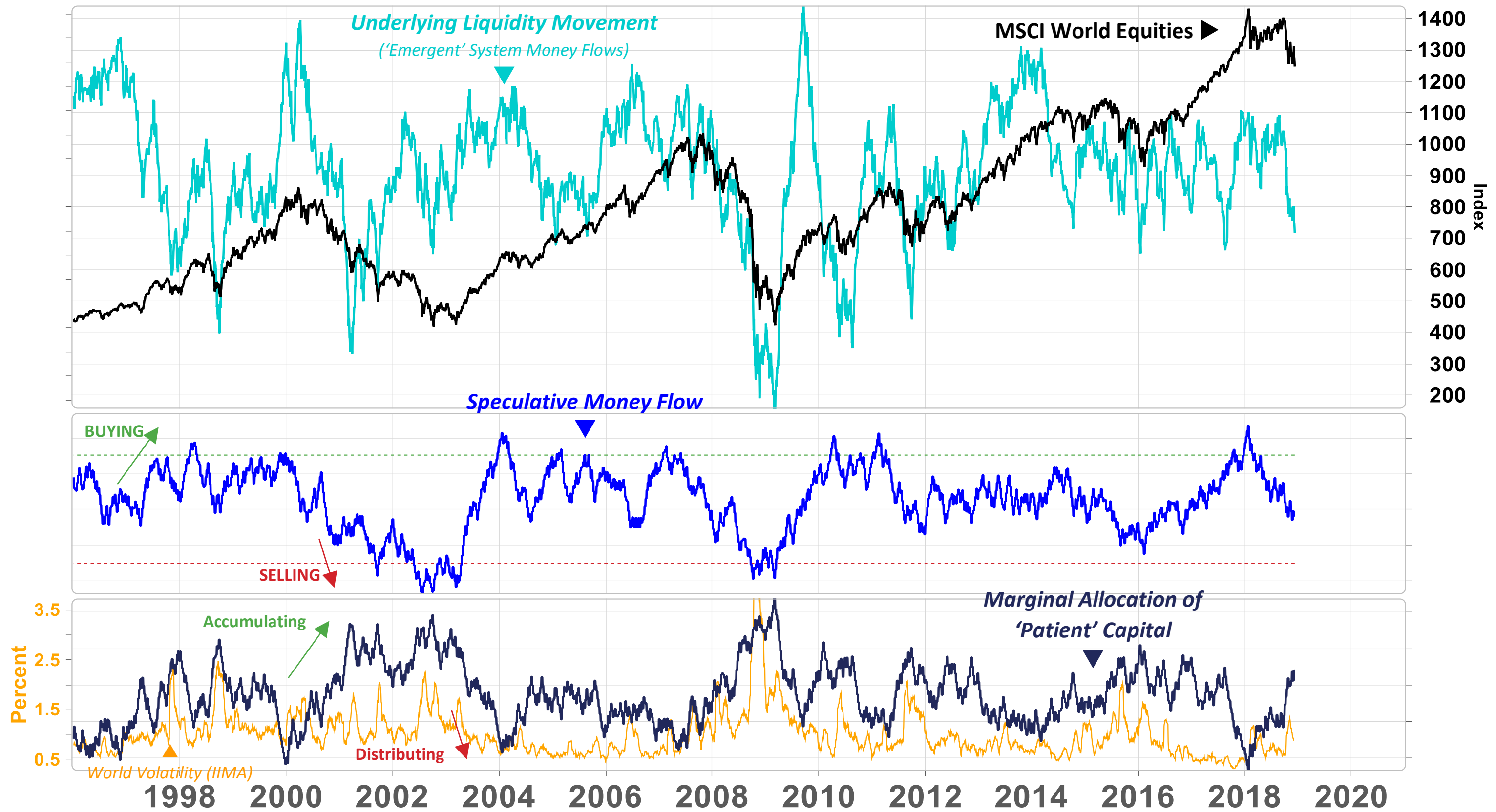
Equities //

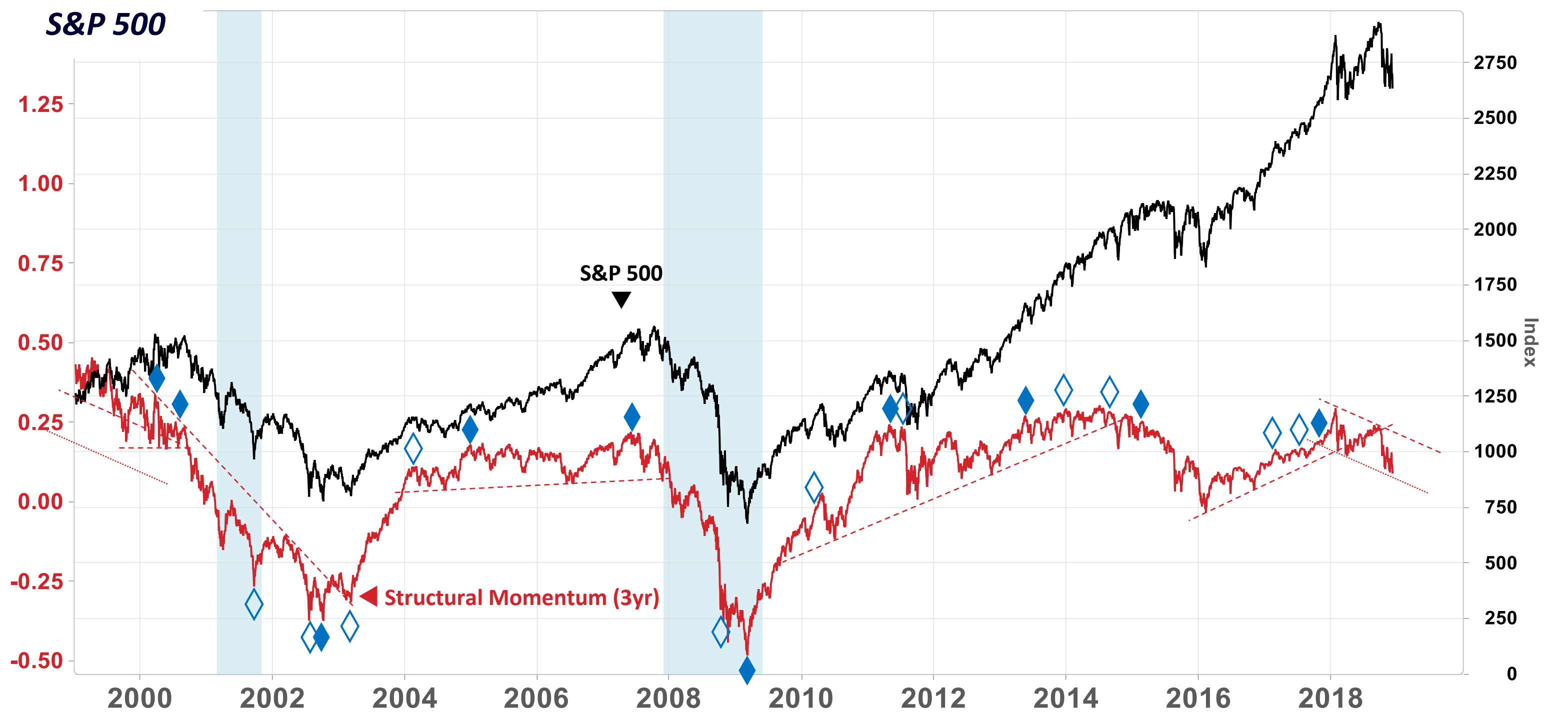
MSCI World Equities



Comments:

[No change to comments from April] *'Emergent' System Money Flows are weak, and with Speculative + Patient Money Flows at historic extremes, world equities are in a vulnerable state. 3yr Structural Momentum is breaking, ushering in the possibility of deeper falls in equities (or at minimum a more extended sideways correction).*



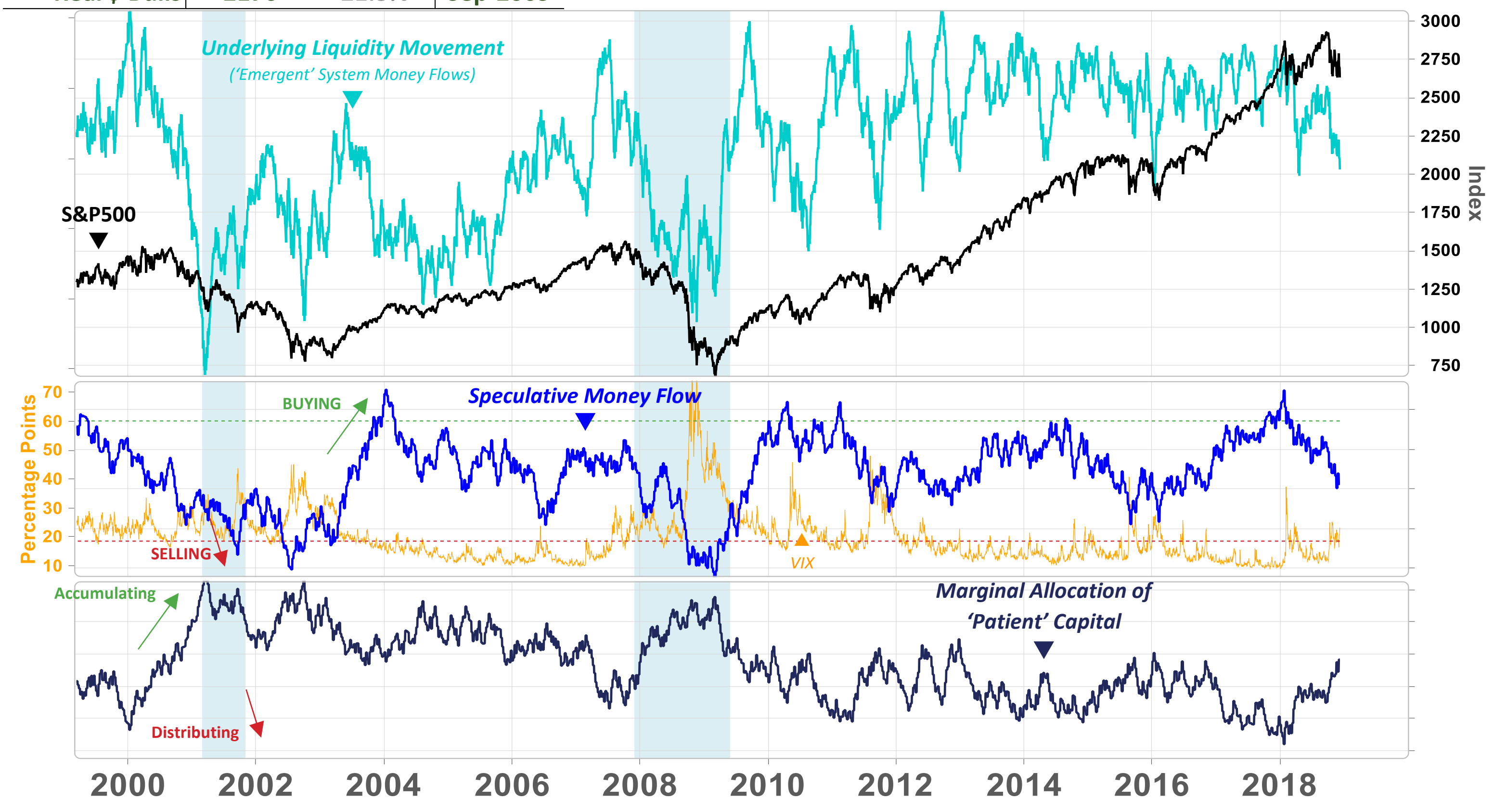


Last Weekly Close: 2633

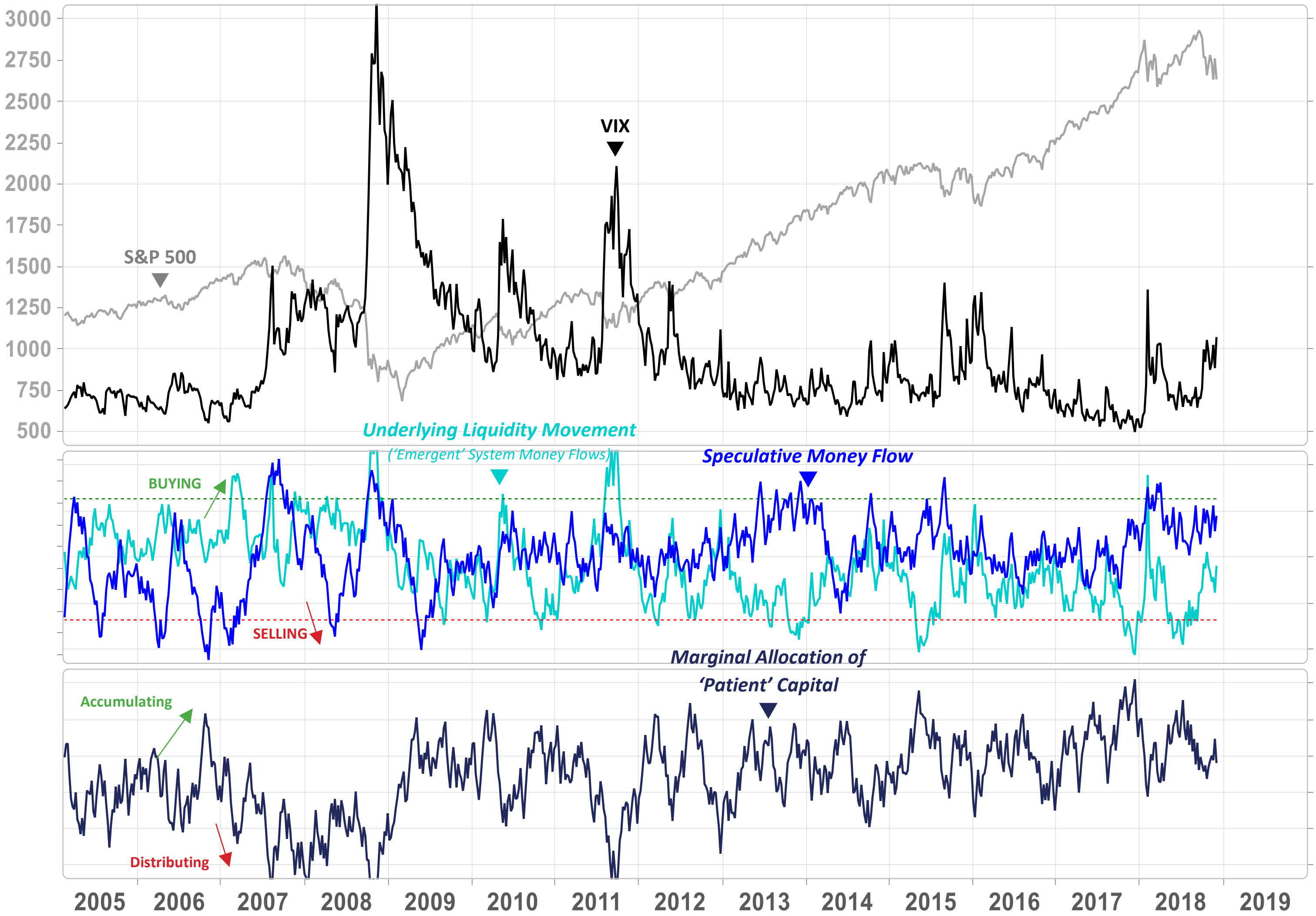
	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**2593**	**-1.5%**	**-**
Leveraged Bears	*2861*	*8.0%*	*Oct-2018*
Leveraged Bulls	*2602*	*1.2%*	*Feb-2016*
Real $ Bulls	**2170**	**21.3%**	**Sep-2009**

Comments:

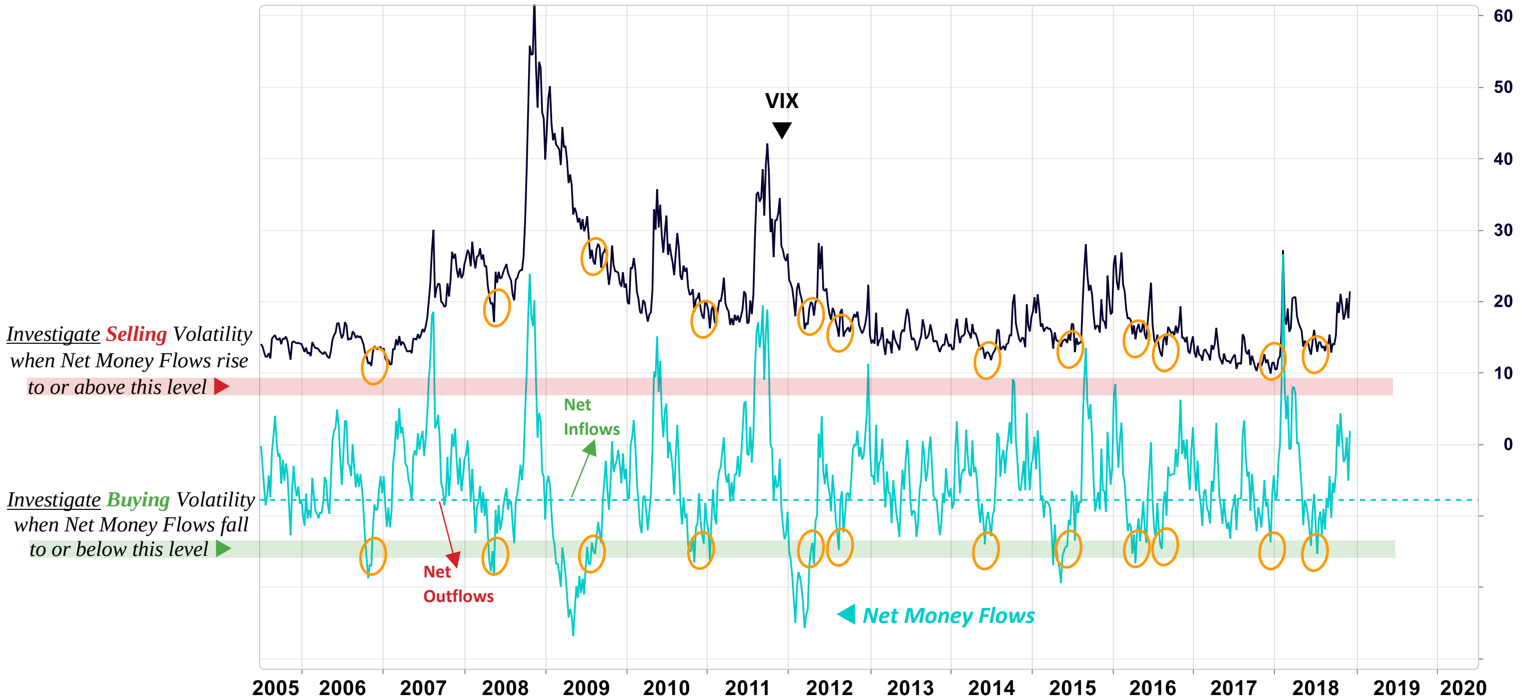
[No change to comments from April] *The market is vulnerable to a deeper fall (or at minimum a more extended sideways correction).*



VIX (S&P 500)

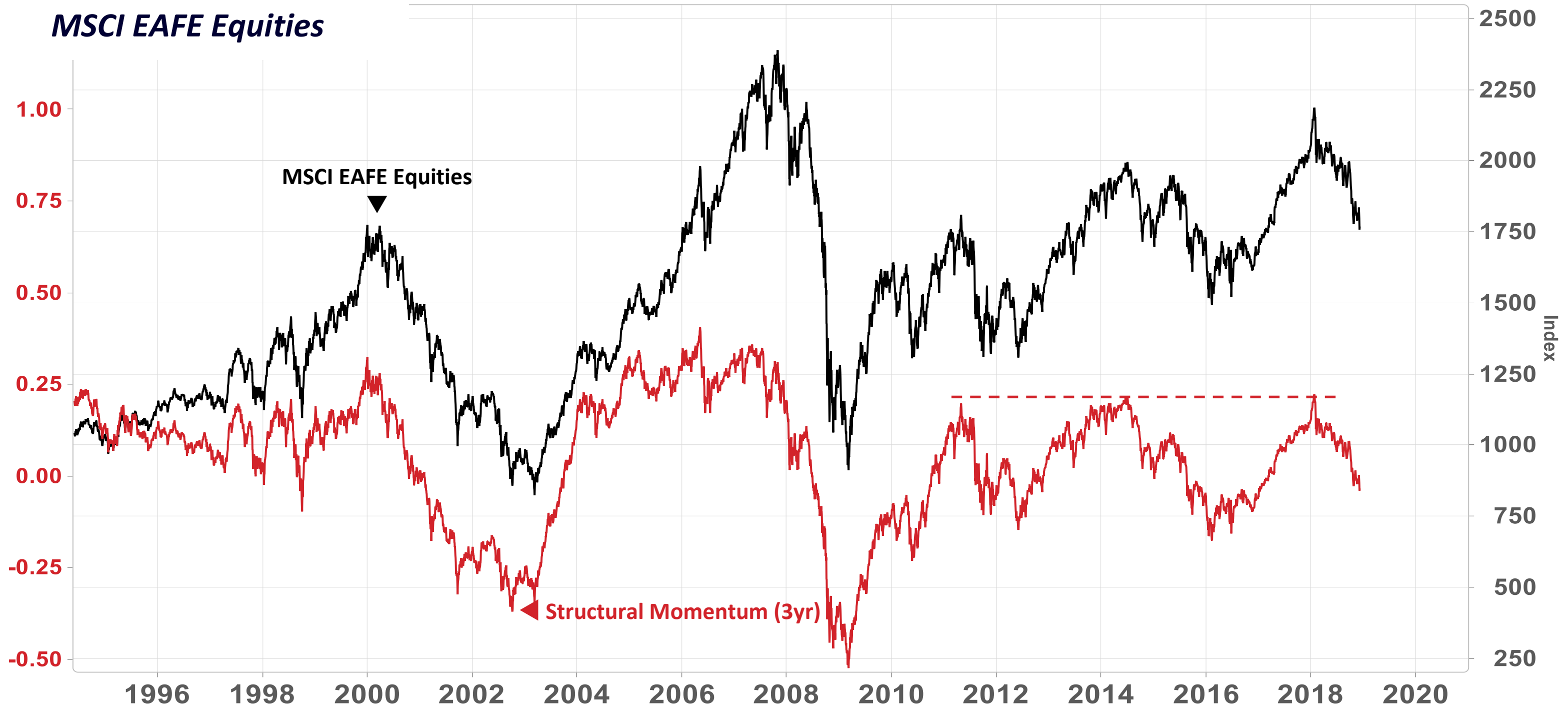


S&P 500
VIX
Underlying Liquidity Movement
('Emergent' System Money Flows)
Speculative Money Flow
BUYING
SELLING
Marginal Allocation of
'Patient' Capital
Accumulating
Distributing



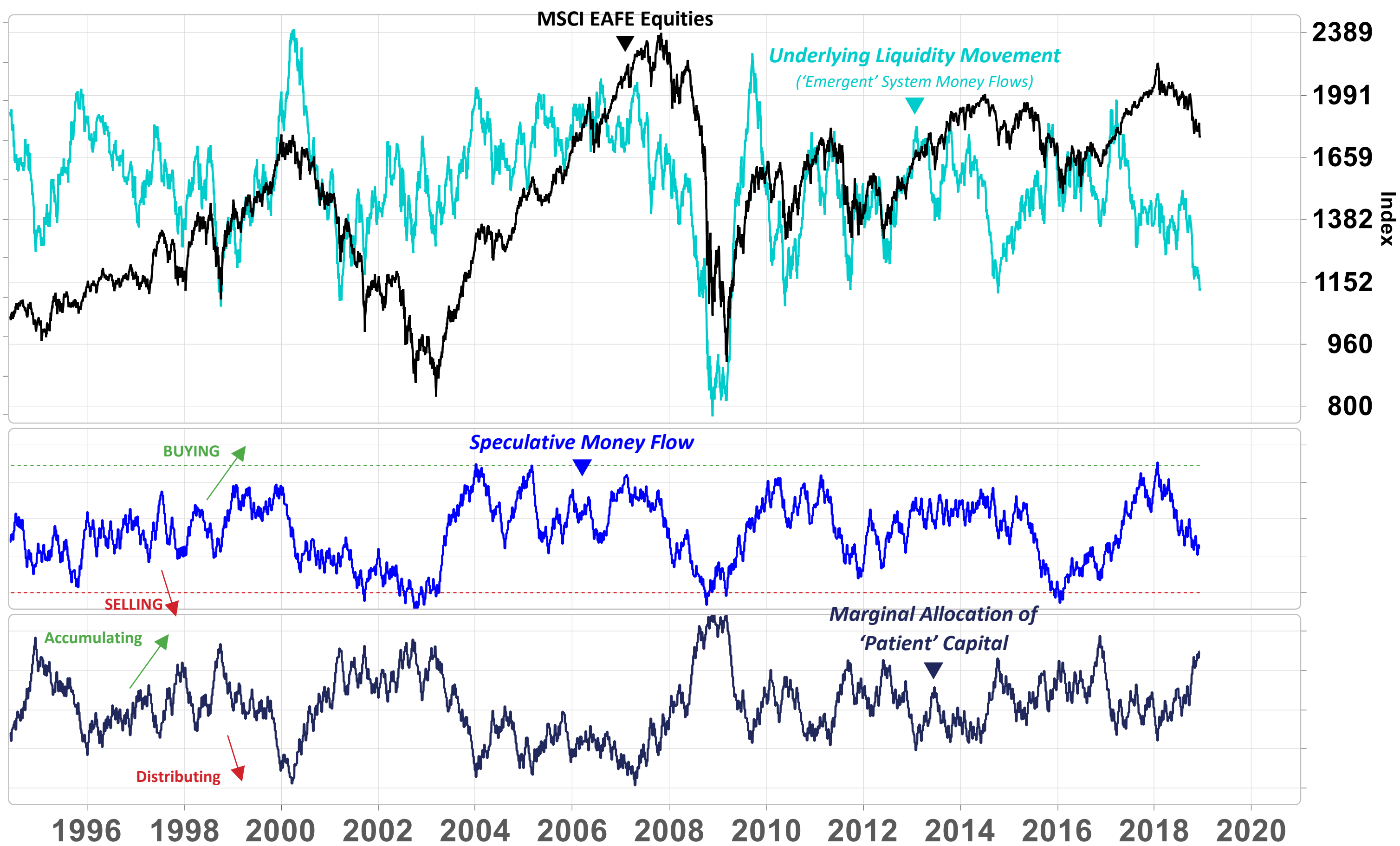
VIX
Investigate Selling Volatility
when Net Money Flows rise
to or above this level
Investigate Buying Volatility
when Net Money Flows fall
to or below this level
Net
Inflows
Net
Outflows
Net Money Flows

MSCI EAFE Equities

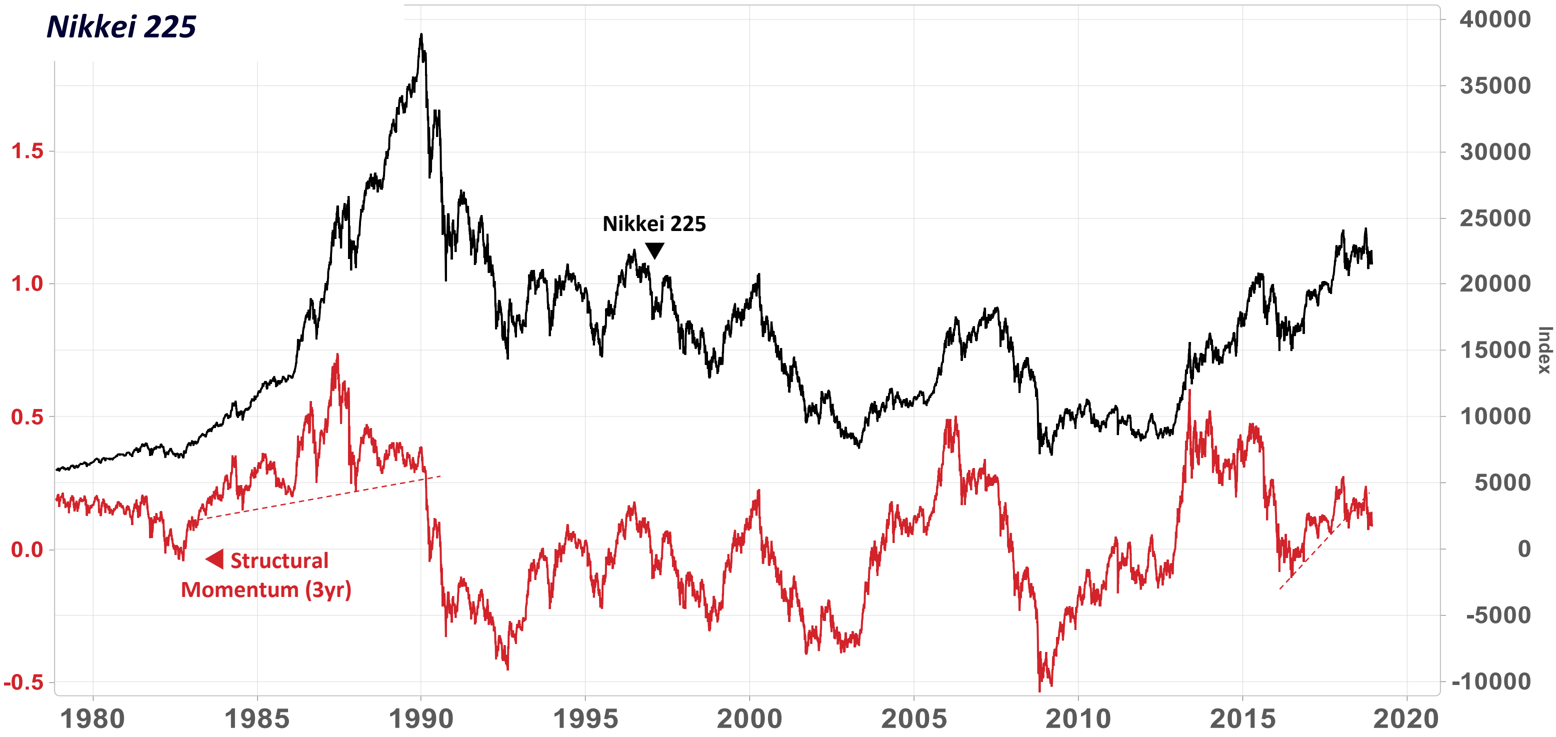


Comments:

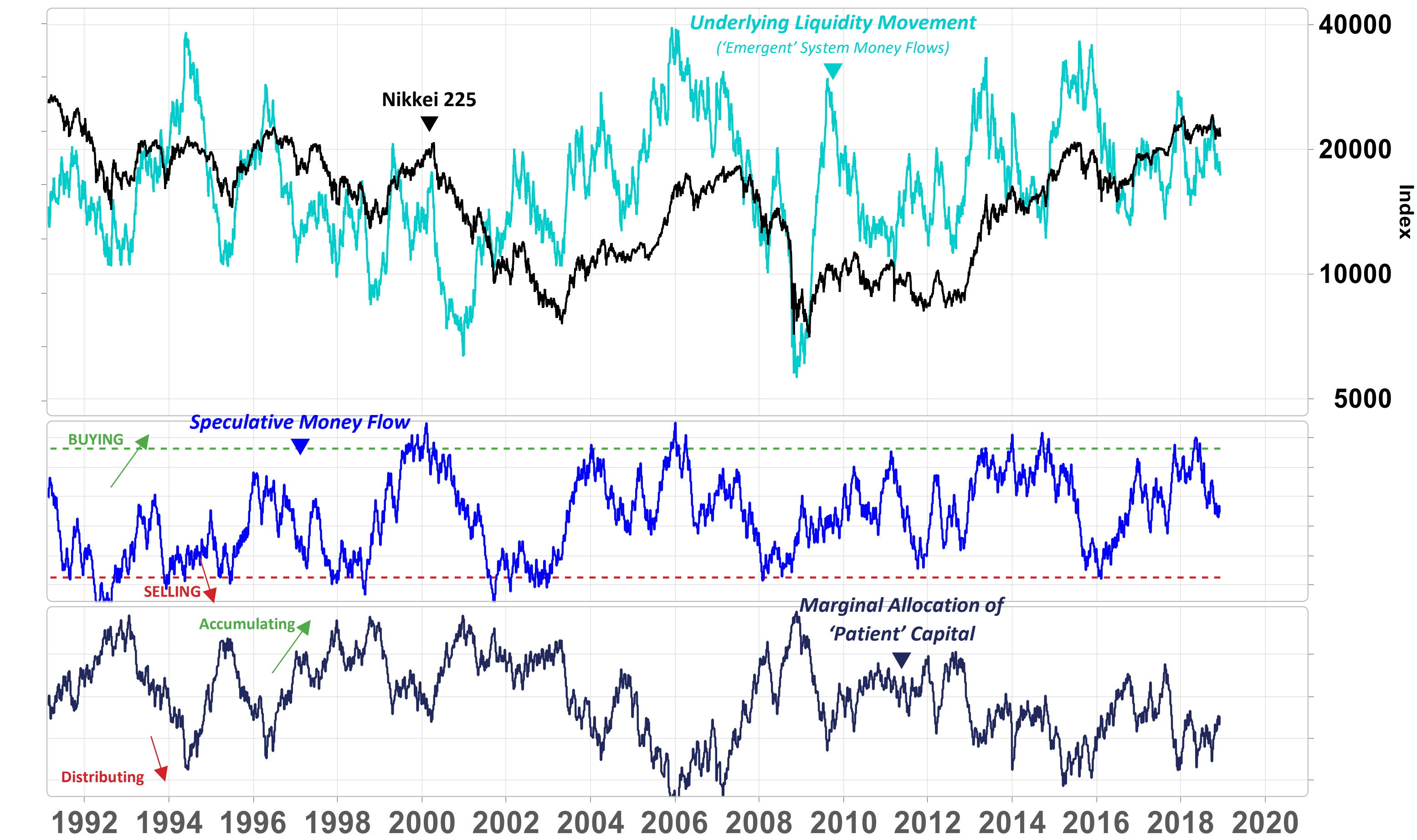
[No change to comments from January] *Flows to non-US Equities in the world are noticeably weak and Speculatively driven. Non-US global equities are in a somewhat vulnerable condition.*



Nikkei 225



Nikkei 225
Structural Momentum (3yr)
1.5
1.0
0.5
0.0
-0.5
40000
35000
30000
25000
20000
15000
10000
5000
0
-5000
-10000
Index
1980
1985
1990
1995
2000
2005
2010
2015
2020



Underlying Liquidity Movement
('Emergent' System Money Flows)
Nikkei 225
40000
20000
10000
5000
Index
Speculative Money Flow
BUYING
SELLING
Marginal Allocation of
'Patient' Capital
Accumulating
Distributing
1992
1994
1996
1998
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2002
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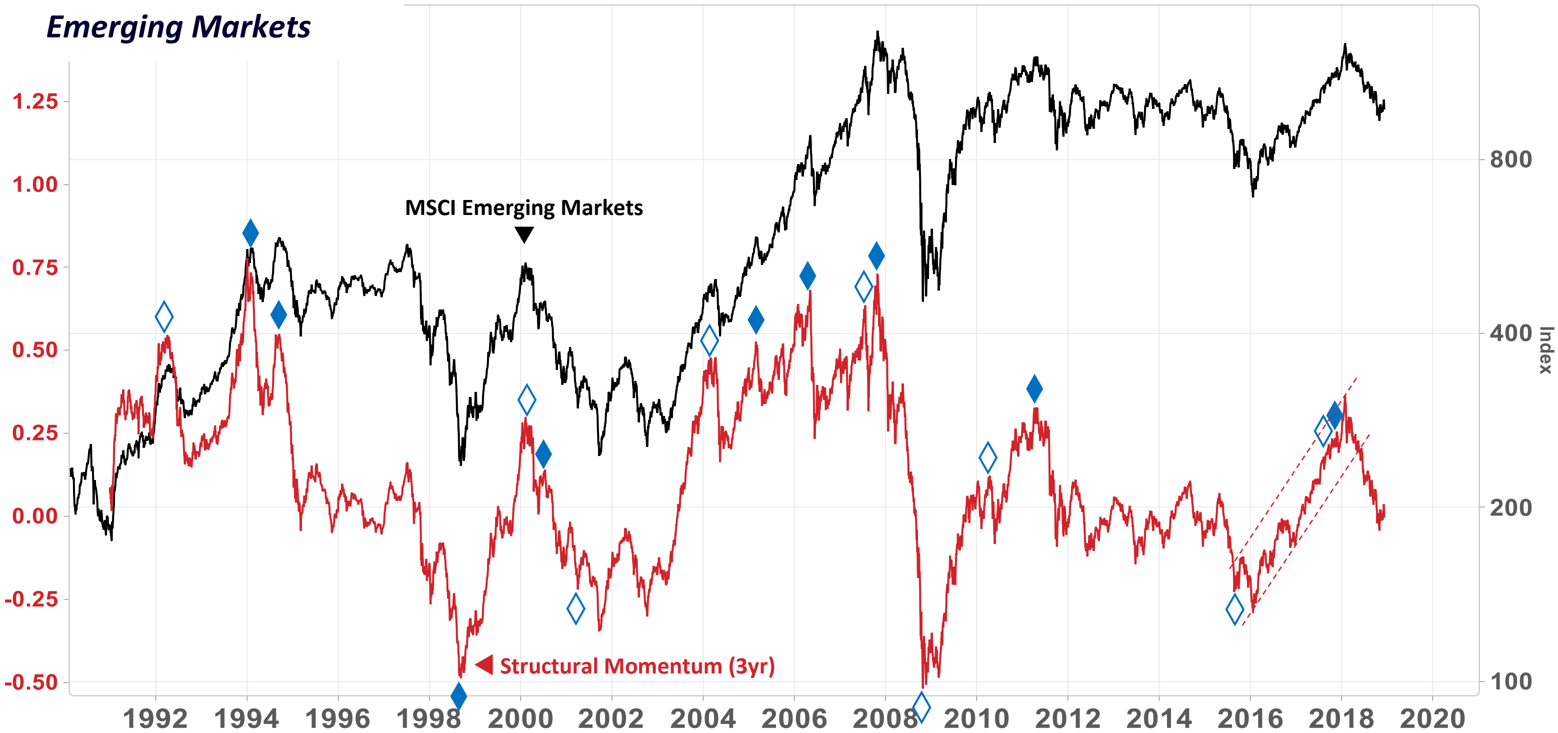
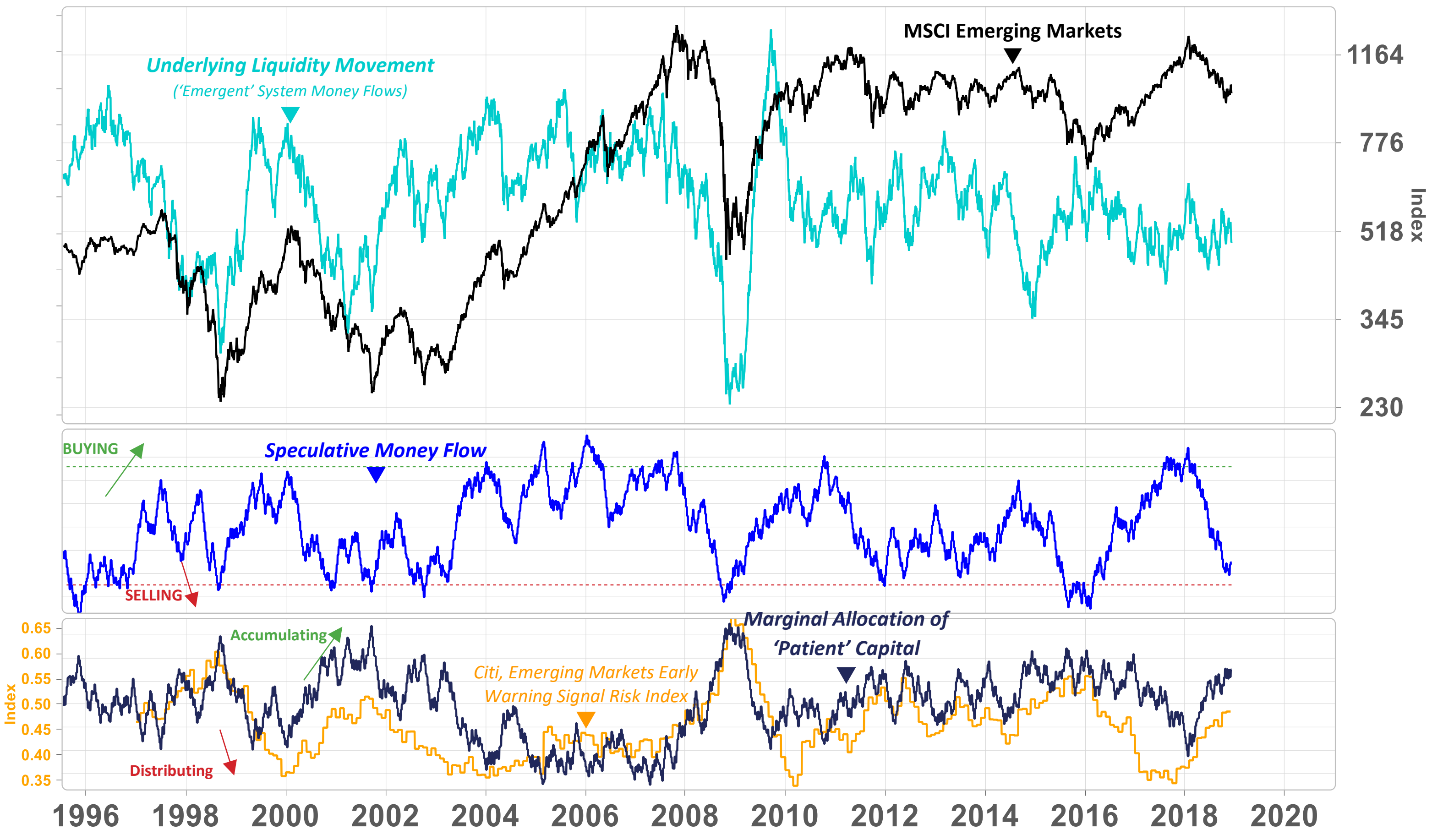
2018
2020

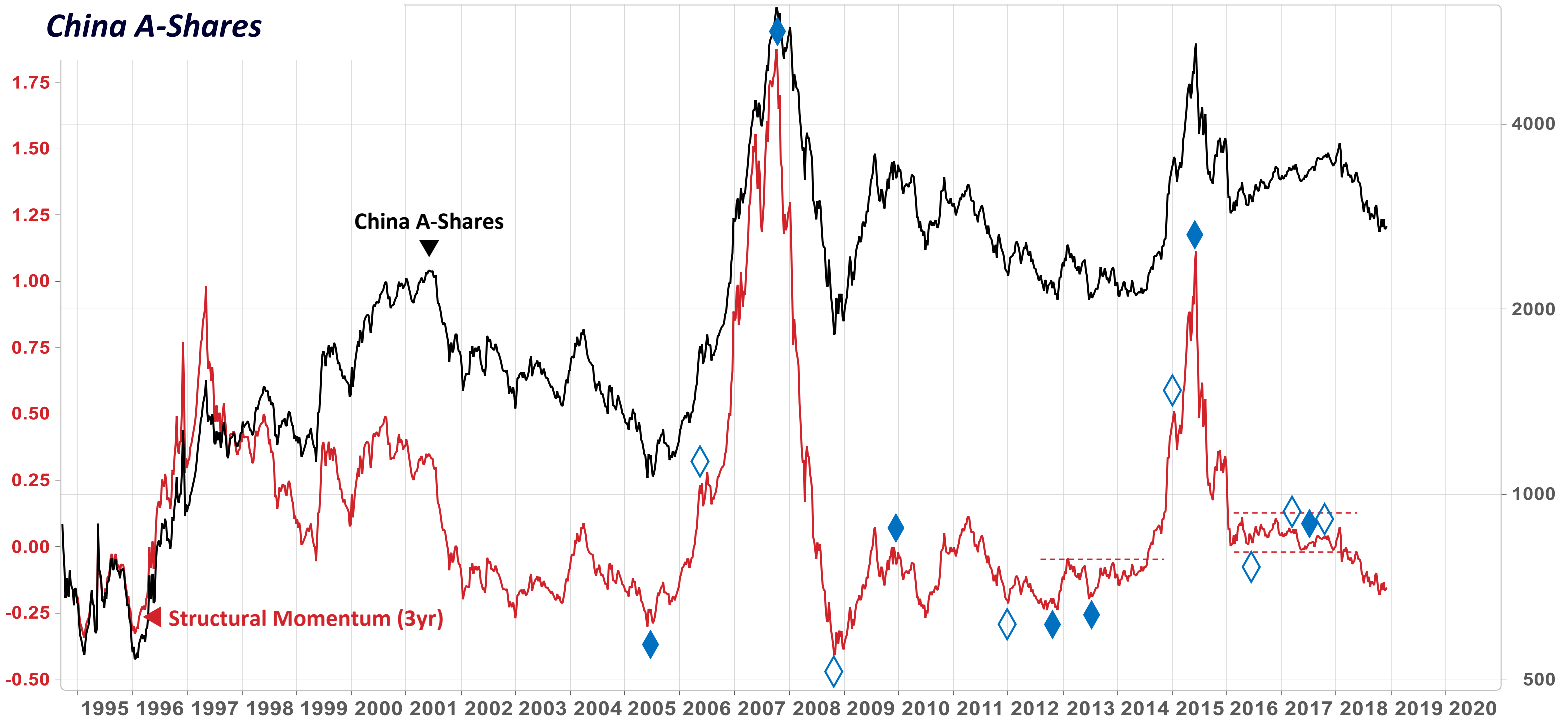
Emerging Markets



Comments:

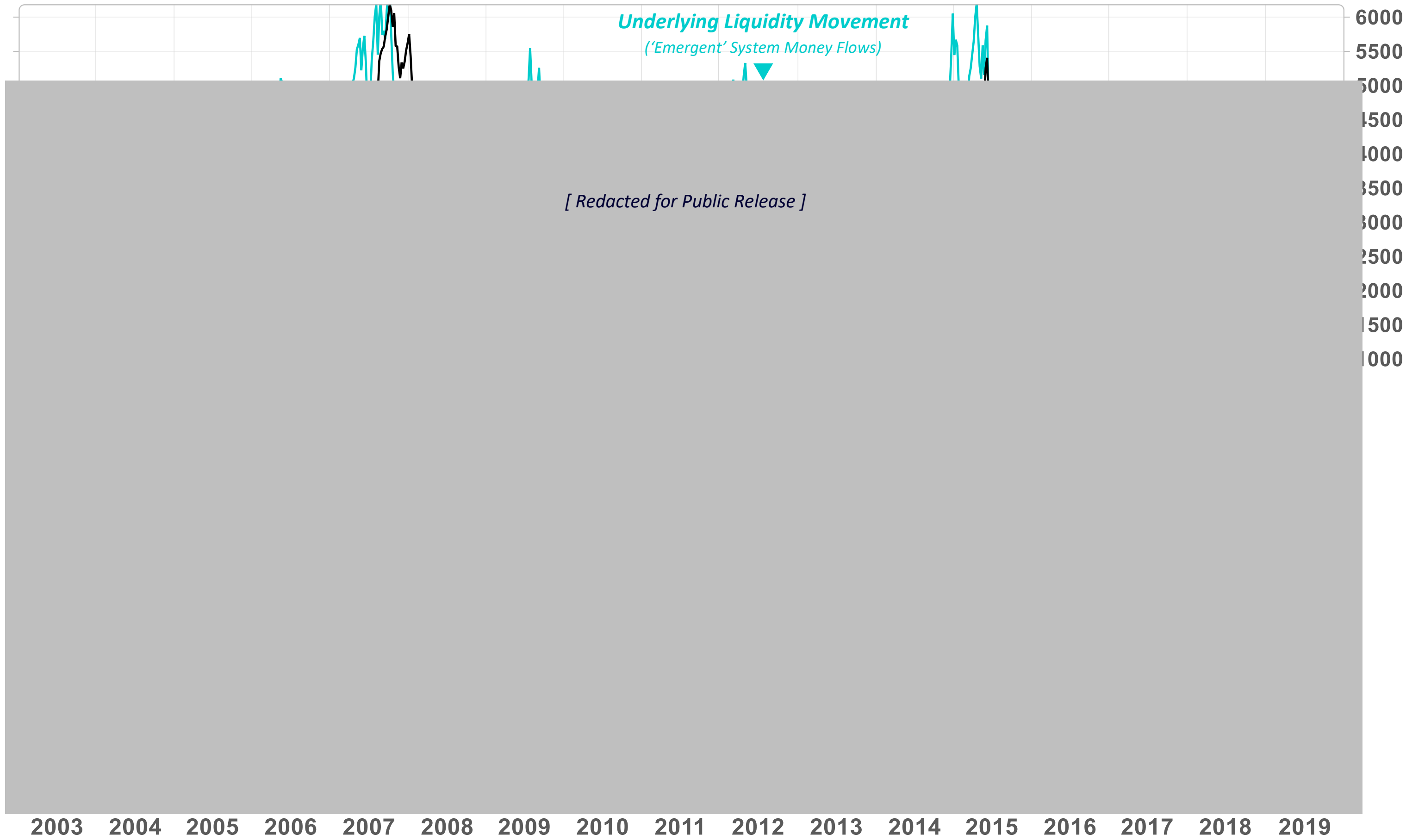
[No change to comments from February] *Likely to be some sort of a significant top.*



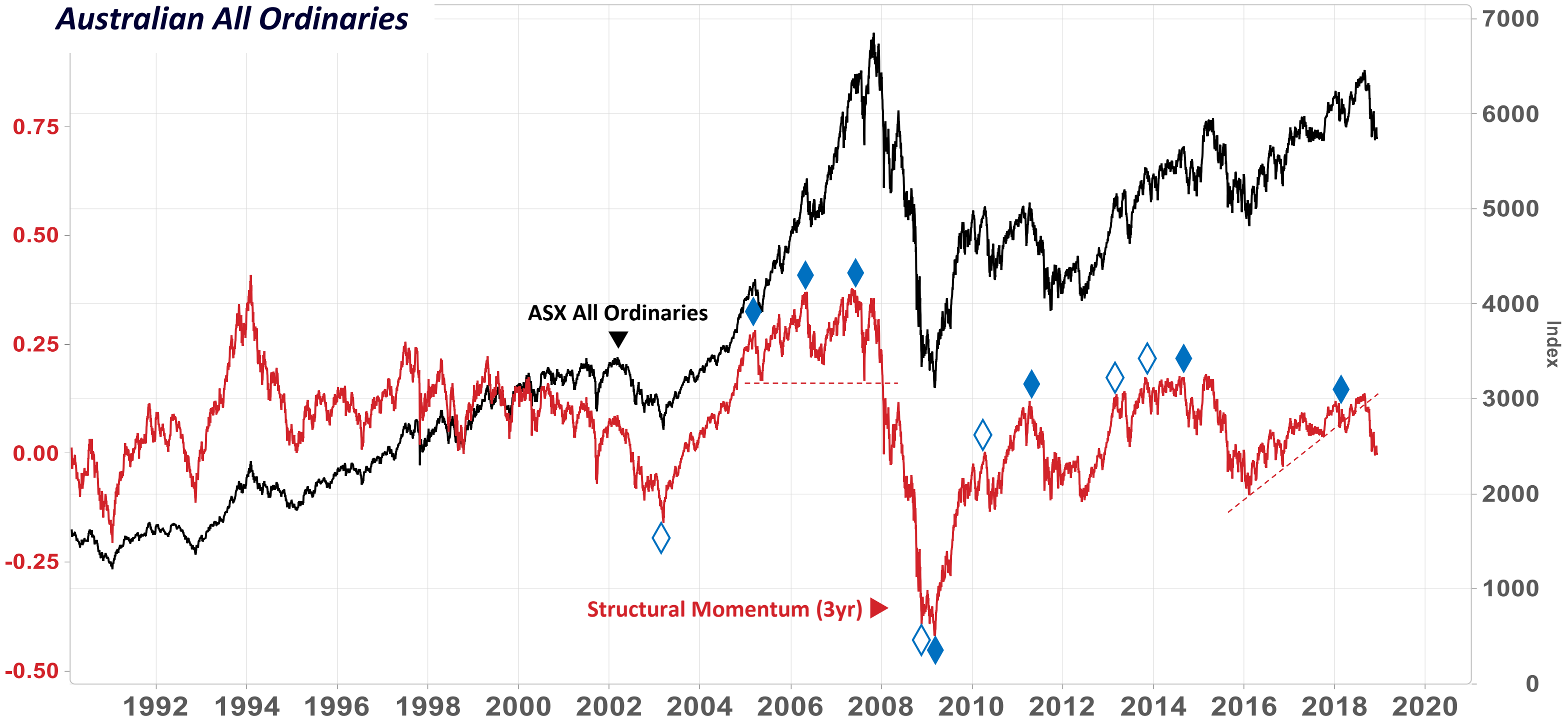


Comments:

[No change to comments from April] *Likely to be some sort of a significant intermediate top – quite vulnerable to further downside risks.*

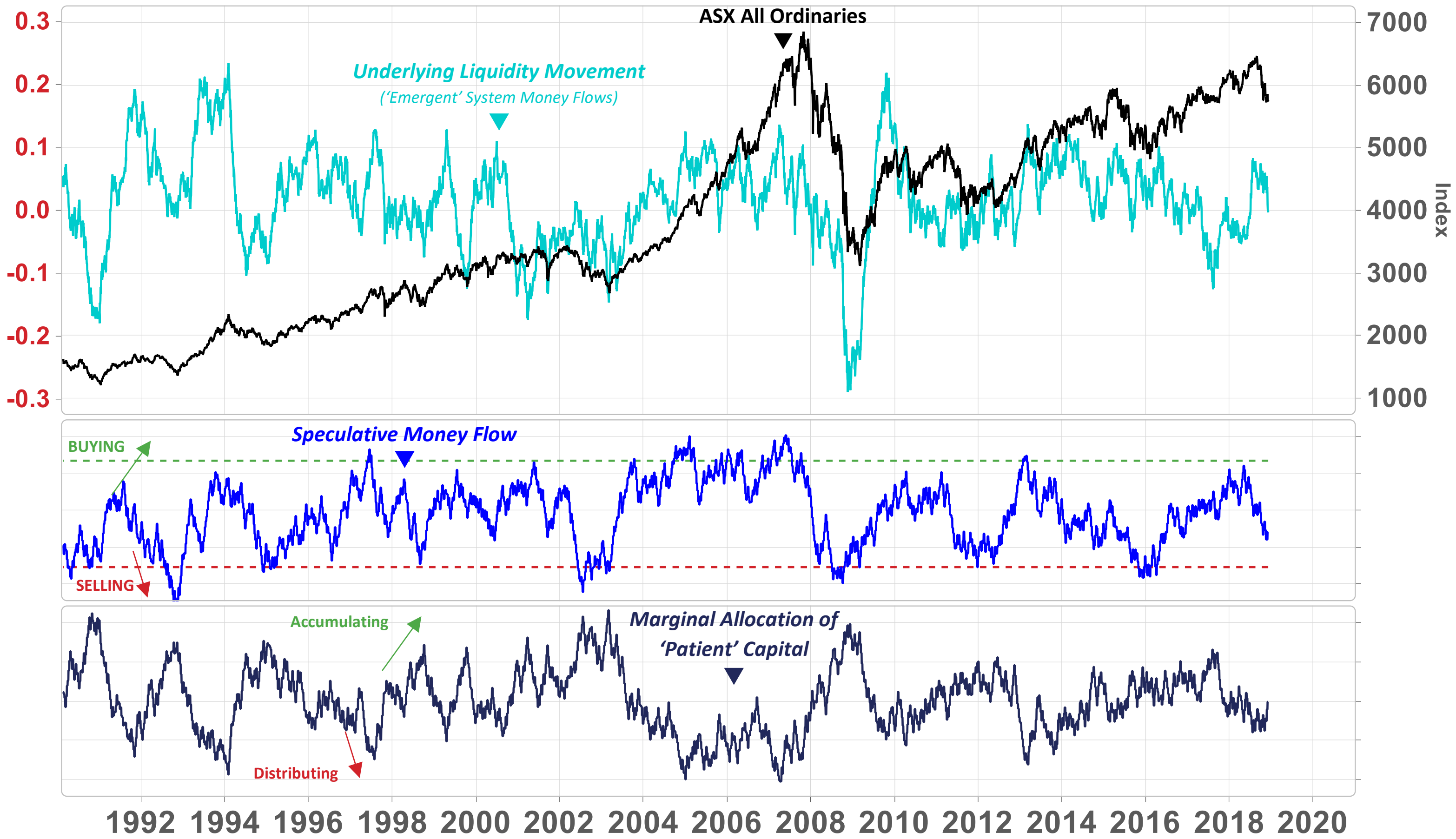


Australian All Ordinaries



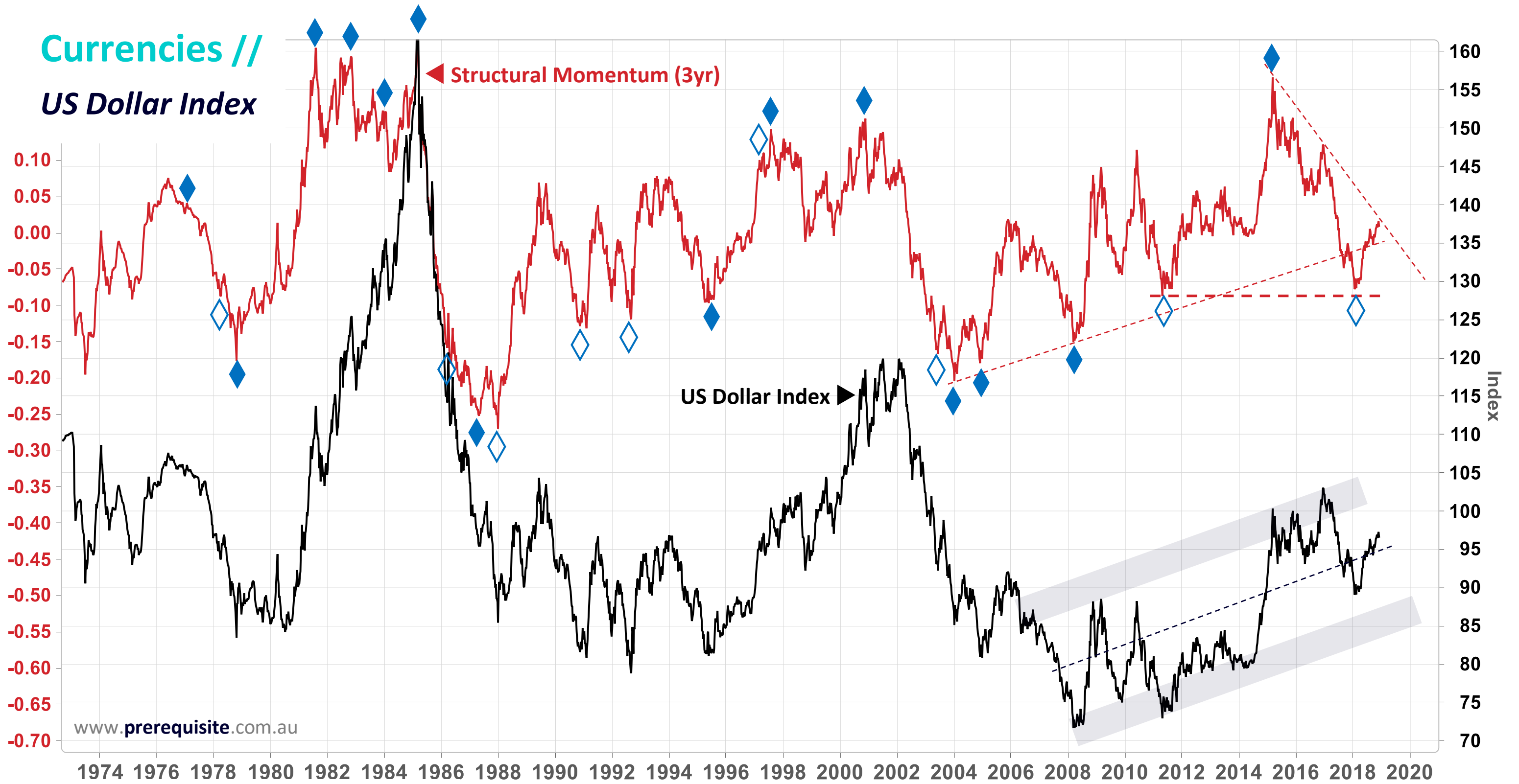
Comments:

[No change to comments from August] *It's very easy to read this last run up in price from a broader perspective as a possible 'last hurrah' before rolling over. Flows, Structural Momentum & Liquidity Signals all coalescing to warn that beneath the surface this market is weaker than price would suggest. Caution is advised.*



Currencies //

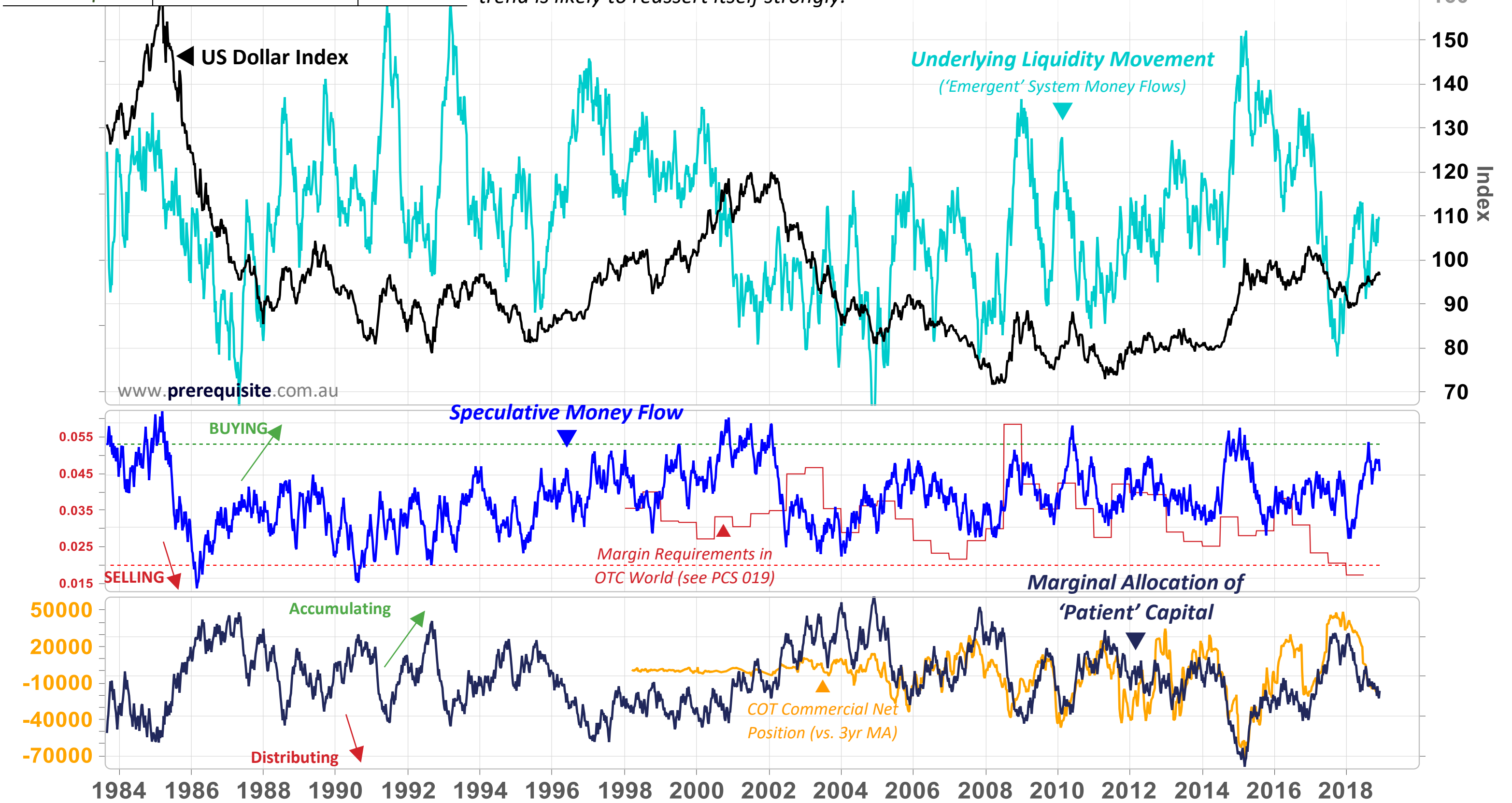
US Dollar Index



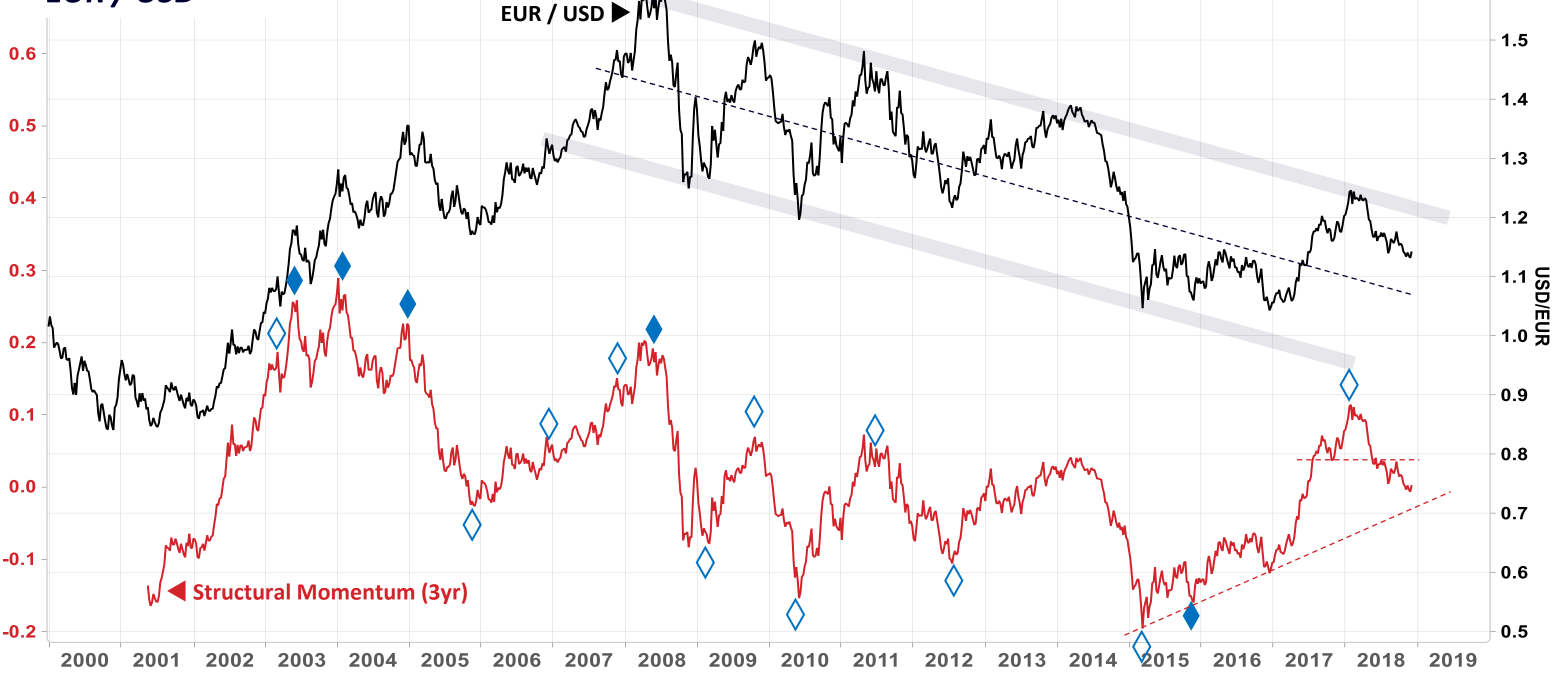
Last Weekly Close: 96.5

	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**102.0**	5.4%	**May-2017**
Leveraged Bears	*96.1*	*-0.5%*	*-*
Leveraged Bulls	*92.7*	*4.1%*	*Apr-2018*
Real $ Bulls	**89.7**	7.6%	**Feb-2018**

Comments: [Feb-2018…] *Money flows suggest a bear trap (especially having Emergent flows not confirming the most recent fall below 90). Real Money Bulls trying to wrest back control. The freshly triggered liquidity turning point signal suggests the bearish crowd are at the point of forming a critical mass of consensus (i.e. too bearish from a tactical perspective).* **[Dec-2018…]** *Bear trap from the beginning of 2018 is set. We can't rule out one last swing into the low to mid 90s to mop up any additional bears (and to work off the marginally overbought speculative sentiment), but once the 97-98 range is decisively breached the bullish overall trend is likely to reassert itself strongly.*



EUR / USD



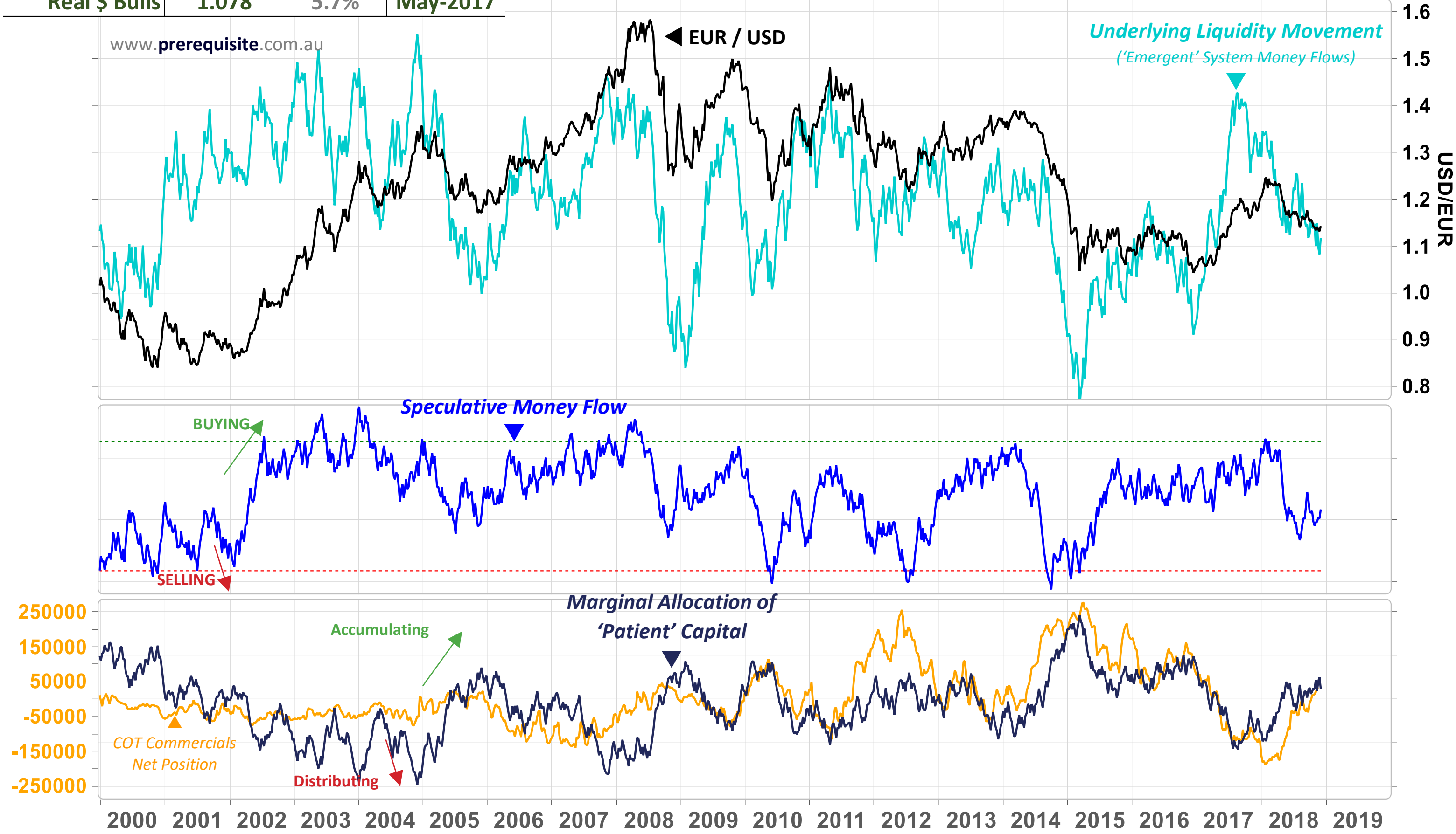
***Last Weekly Close:* 1.139**

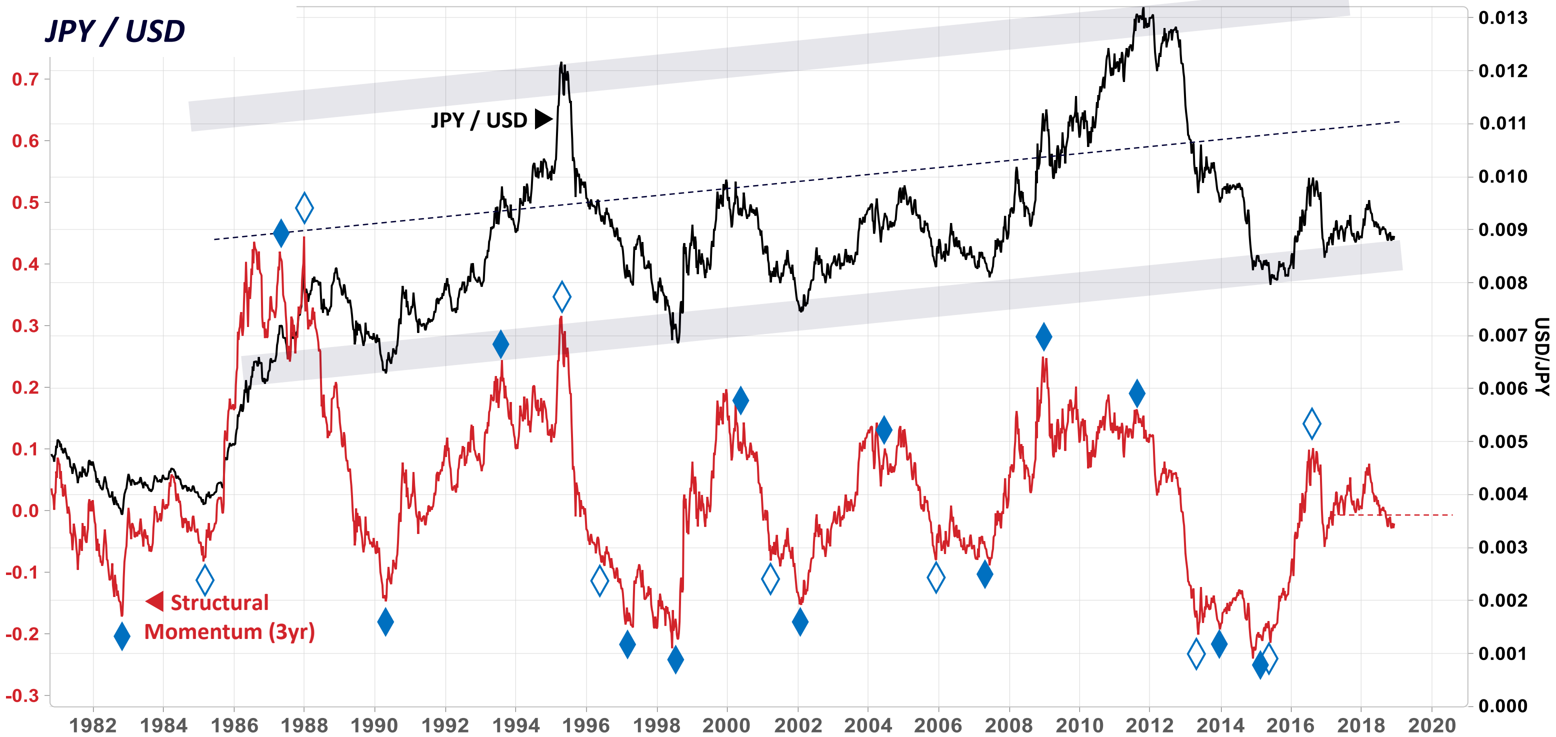
	Point of Control (Threshold)	*Perception of Control (Distance)*	*Date Control Began*
Real $ Bears	**1.215**	**6.2%**	**Apr-2018**
Leveraged Bears	*1.198*	*4.9%*	*Apr-2018*
Leveraged Bulls	*1.138*	*0.0%*	*Mar-2017*
Real $ Bulls	**1.078**	**5.7%**	**May-2017**

Comments:

[Jan-2018…] *Essentially the inverse of the USD Index comments. Clearly we are at a critical juncture for the EUR/USD, with the market in a vulnerable condition (especially considering a minor liquidity signal has just been triggered in the context of over-extended participants and an apparent bearish divergence forming within the Emergent Flows).*

[Dec-2018…] *Towards parity or below still seems the primary underlying trend on a multi-year basis.*



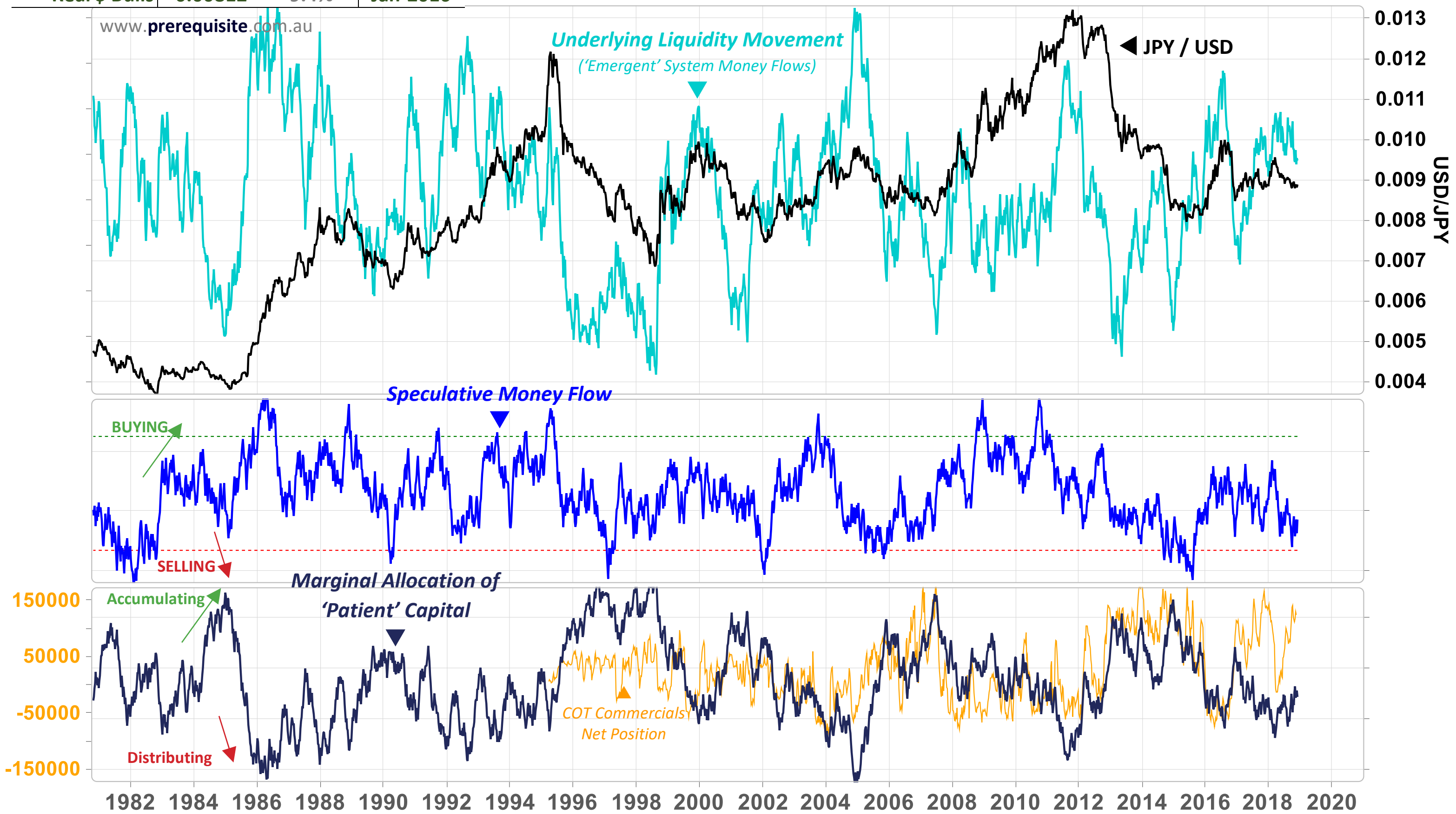


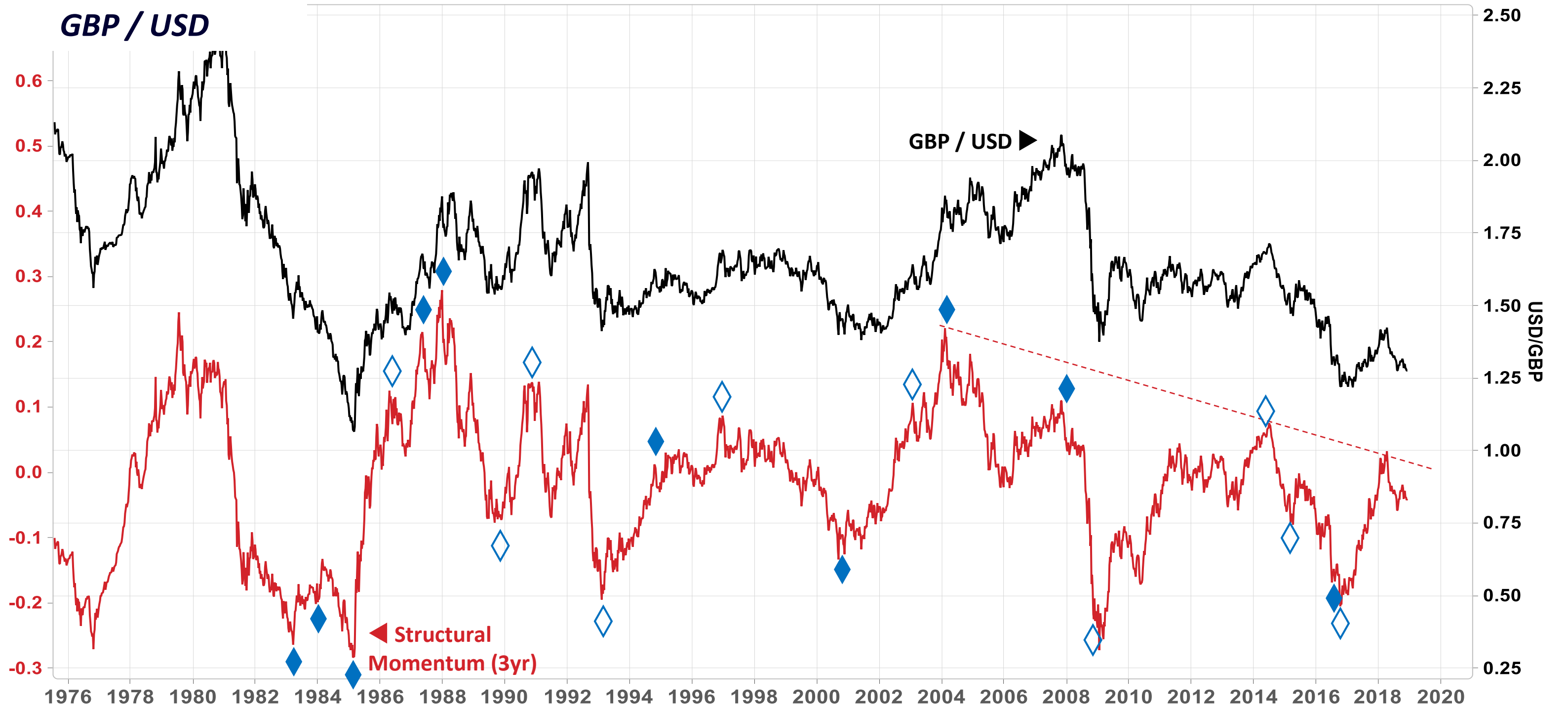
Last Weekly Close: **0.00888**

	Point of Control (Threshold)	*Perception of Control (Distance)*	*Date Control Began*
Real $ Bears	**0.00984**	9.7%	**Nov-2016**
Leveraged Bears	*0.00920*	*3.4%*	*Mar-2018*
Leveraged Bulls	*0.00885*	*0.3%*	*Mar-2017*
Real $ Bulls	**0.00812**	9.4%	**Jan-2016**

Comments:

[No change to comments from April] *Given the early signs of how this pair is behaving, our suspicion is that the divergence between our Patient Money Flow tool and the COT Commercial Net Positions will in hindsight be reconciled in favour of our tool being the more accurate reading overall (i.e. there's a scenario building that the JPY/USD could actually be approaching an intermediate top?).*





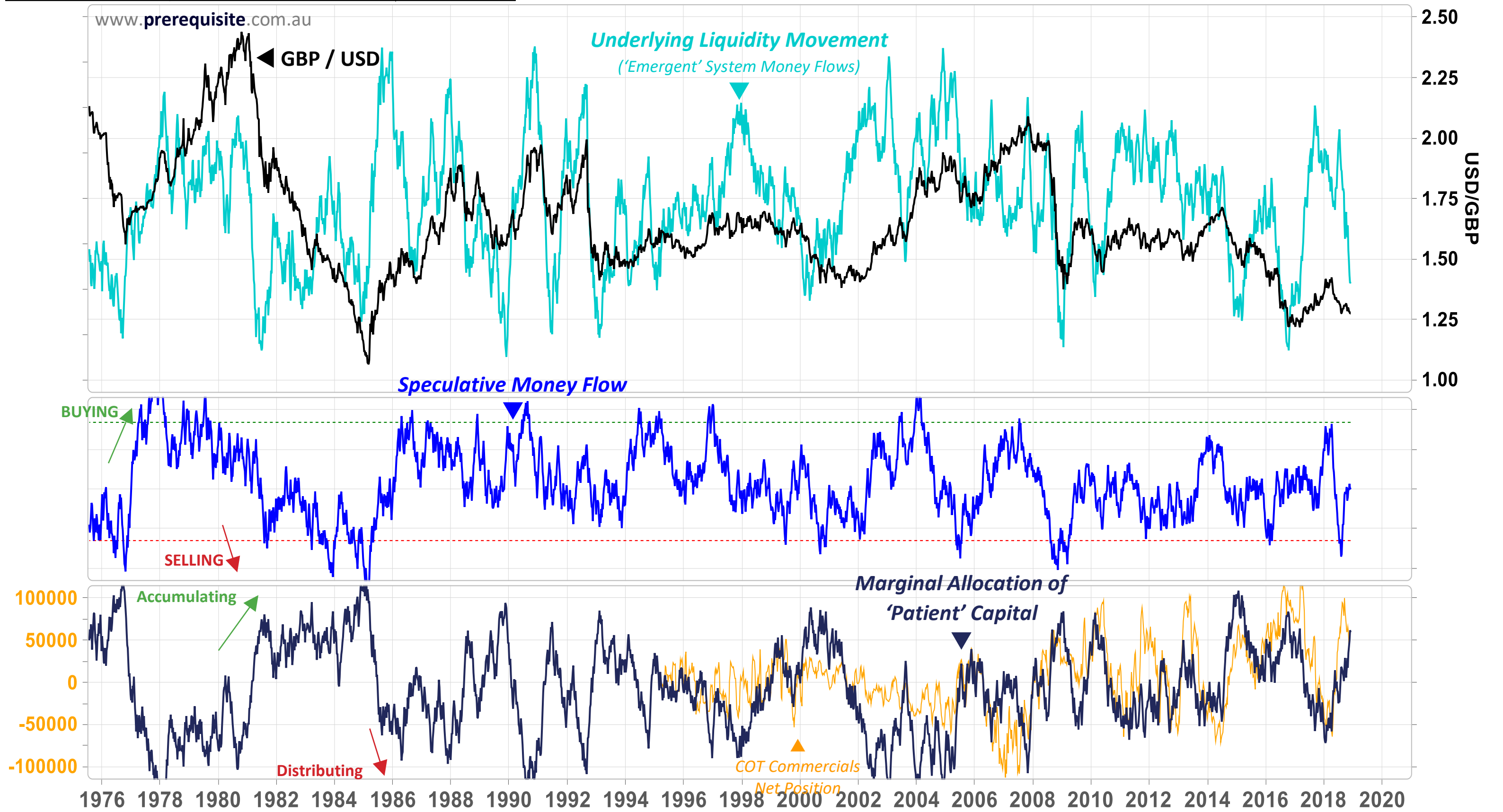
Last Weekly Close: **1.276**

	Point of Control (Threshold)	*Perception of Control (Distance)*	Date Control Began
Real $ Bears	**1.406**	9.3%	**Feb-2018**
Leveraged Bears	*1.345*	*5.1%*	*Apr-2018*
Leveraged Bulls	*1.302*	*-2.0%*	*Apr-2017*
Real $ Bulls	**1.276**	0.0%	**Jan-2018**

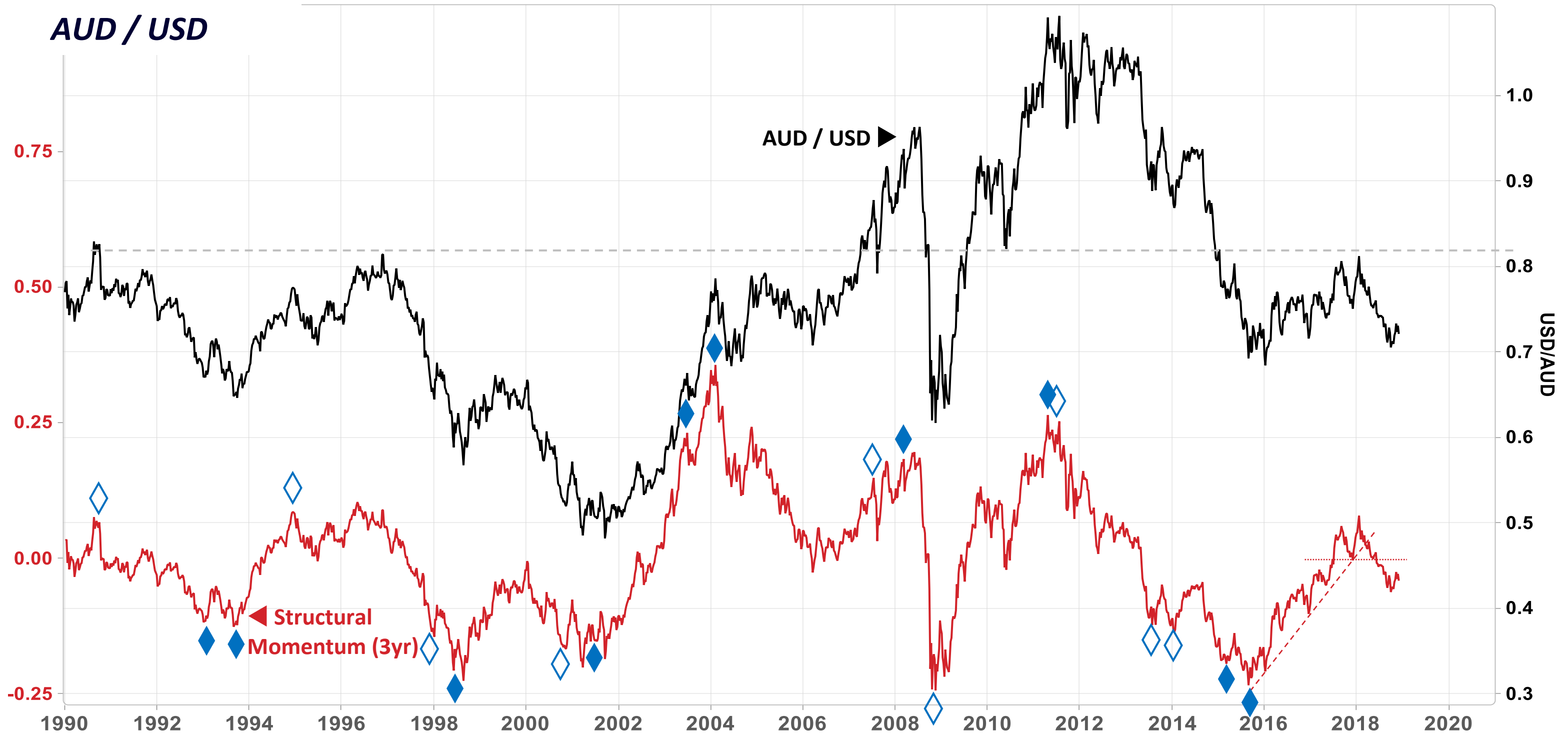
Comments:

[No change to comments from August] *If the GBP can find support fairly soon, it 'could' be setting up to surprise to the upside in a fairly big way over the next 12-24 months? However, to the degree that the UK is unable to disconnect from the European Union, any potential for a cyclical base in the GBP is jeopardised with substantial downside risks remaining.*

Structural Momentum and trapped Bulls still suggest downside run can go further.



AUD / USD



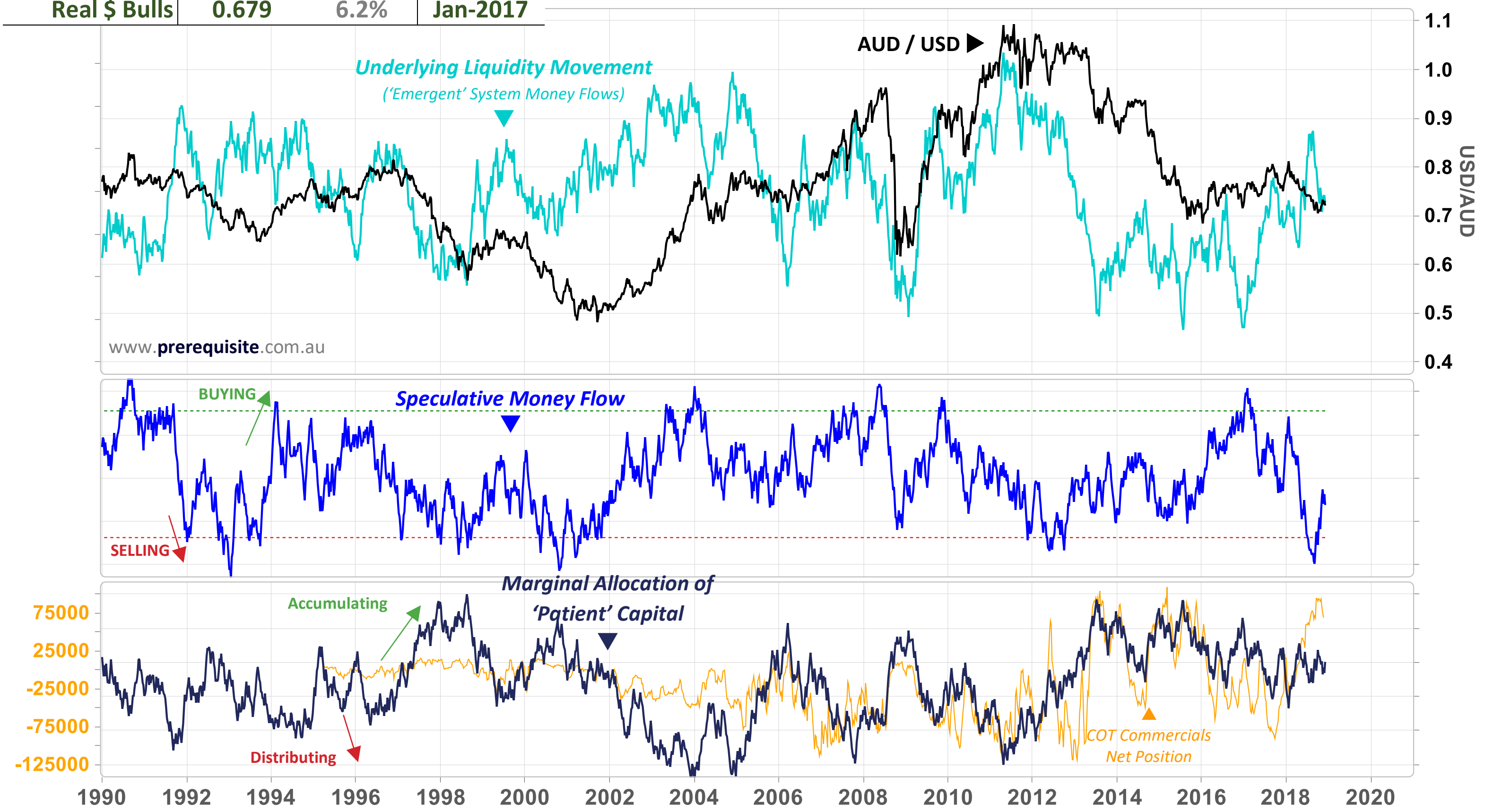
Last Weekly Close: 0.721

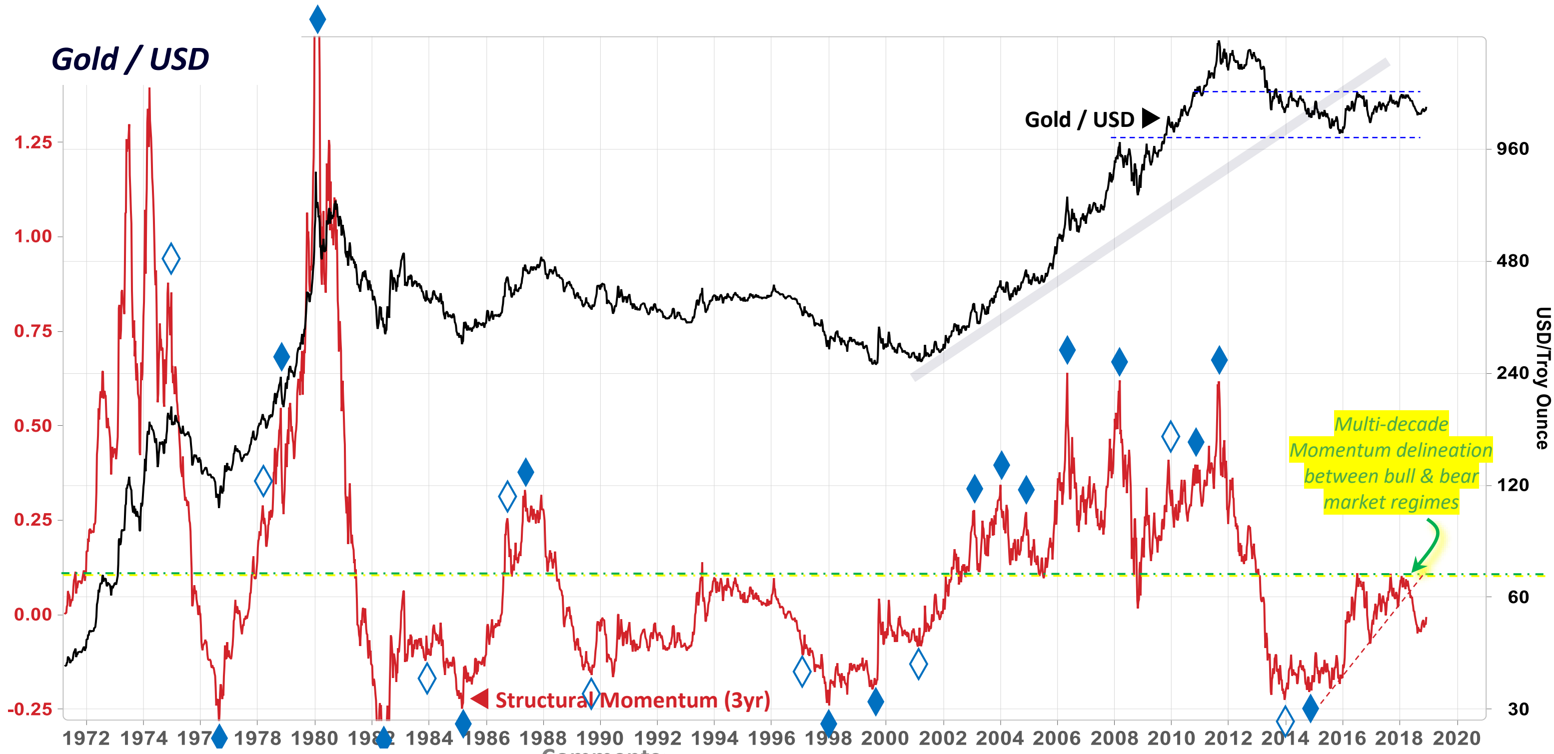
	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**0.822**	12.2%	**May-2013**
Leveraged Bears	*0.747*	*3.5%*	*Feb-2018*
Leveraged Bulls	*0.731*	*-1.4%*	*-*
Real $ Bulls	**0.679**	6.2%	**Jan-2017**

Comments:

[No change to comments from March] *Despite two years of trying to rally, 0.81 has yet proved too formidable. Flows paint a weak picture at risk of significantly rolling over, right at a juncture that could see a downside break of both structural momentum and the leveraged bulls point of control. If this can occur, a move down to 0.70 would be likely in the first instance.*

[August 2018…] *Flows suggest near term bounce is due, but structure overall remains bearish.*





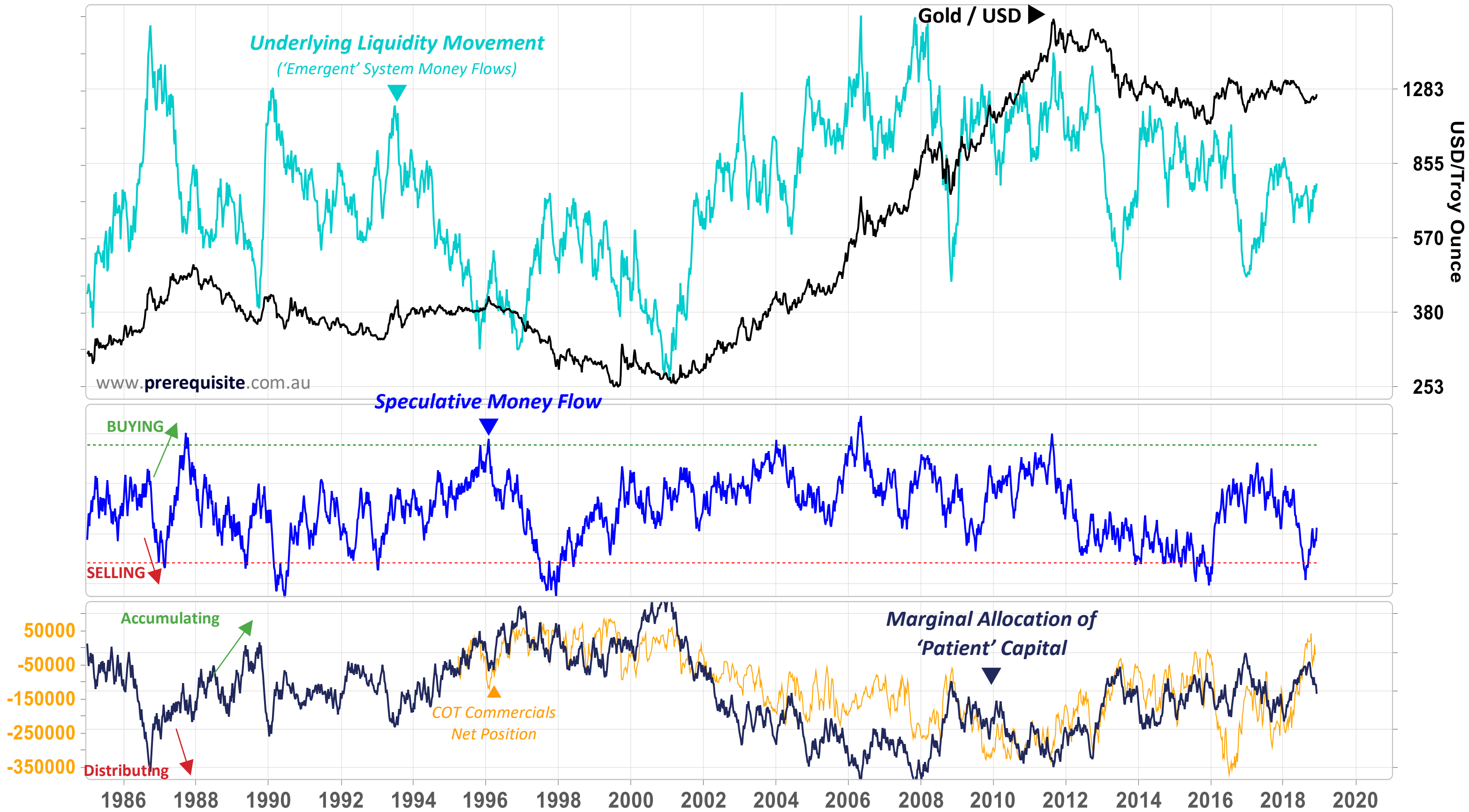
Last Weekly Close: 1248

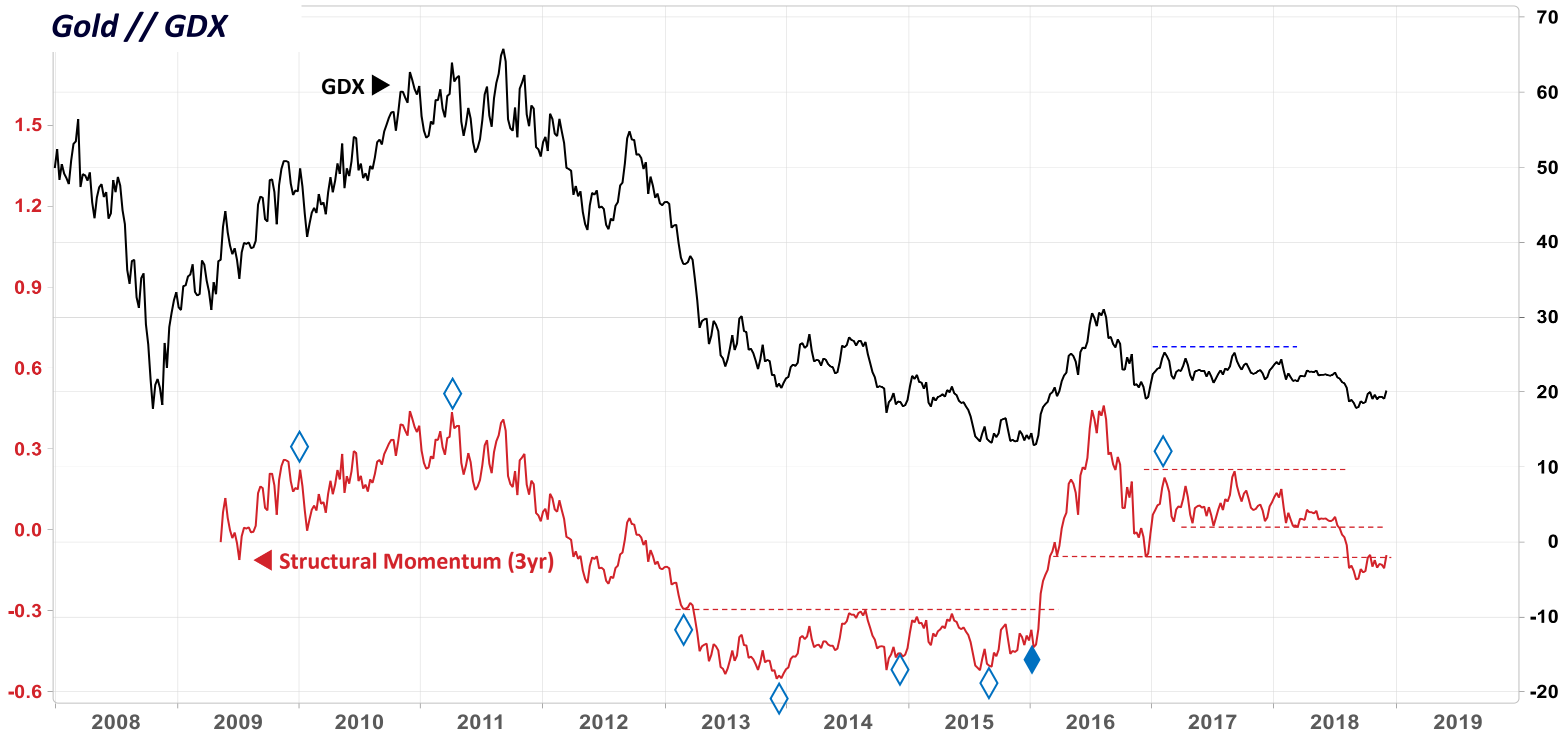
	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**1352**	7.6%	**Feb-2013**
Leveraged Bears	*1271*	*1.8%*	*Feb-2018*
Leveraged Bulls	*1201*	*3.9%*	*Oct-2018*
Real $ Bulls	**1057**	18.1%	**Dec-2015**

Comments:

[No change to comments from February] *It's worth noting that for the last 2 years, the Real Money Bear's point of control has hovered in a narrow band between 1370 and its current low of 1340, so our preference would be a decisive weekly close on strength through this area for it to be decisive. Money Flows & Structural Momentum are not yet confirming any sort of break higher. If anything, this market might be vulnerable to rolling over?*

[April 2018…] *Early signs are that we're witnessing a resumption of the bear market, any bounce is likely to be weak, Real Money Bulls at circa 1050 likely to be tested over the next 12-24 months.*

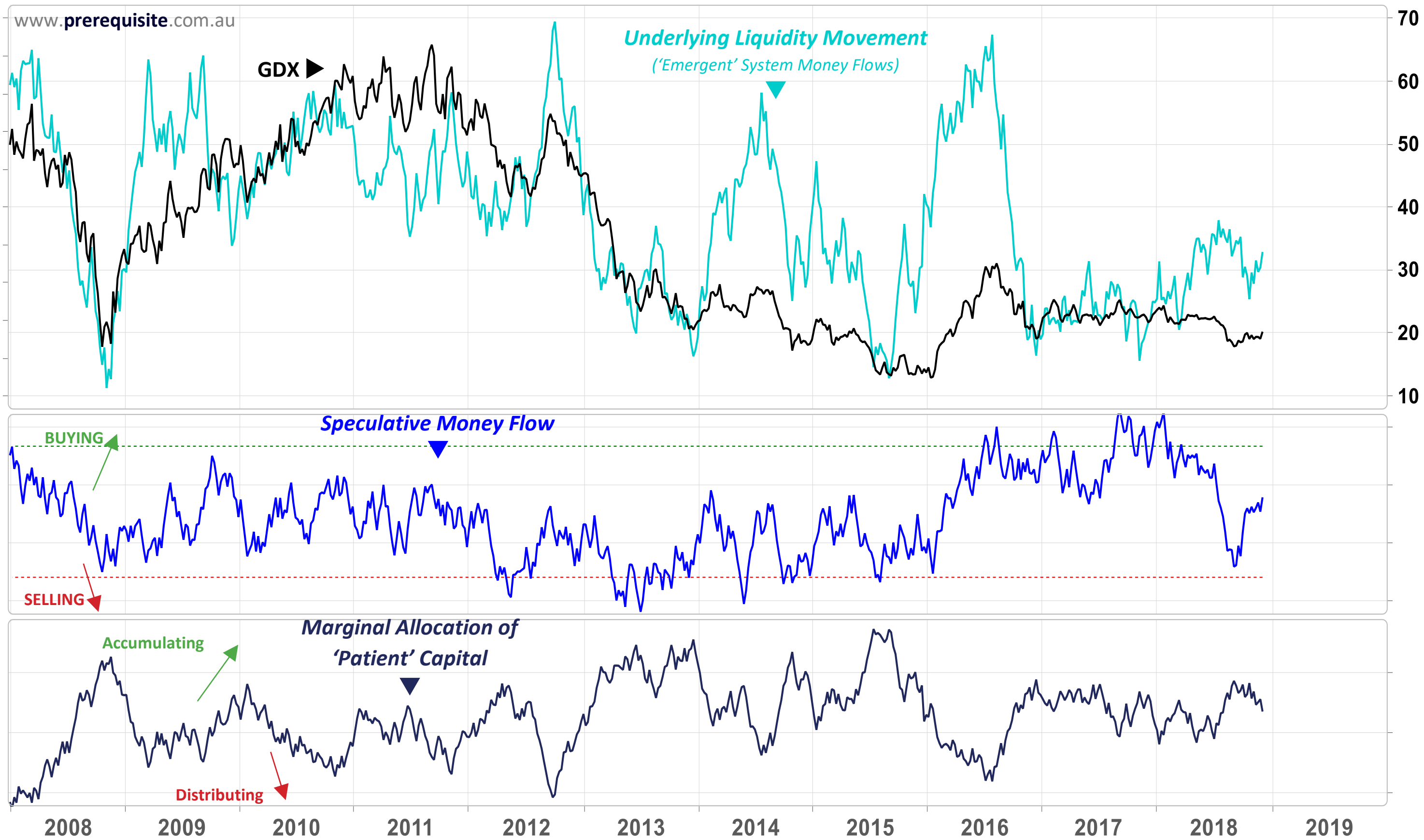




Comments:

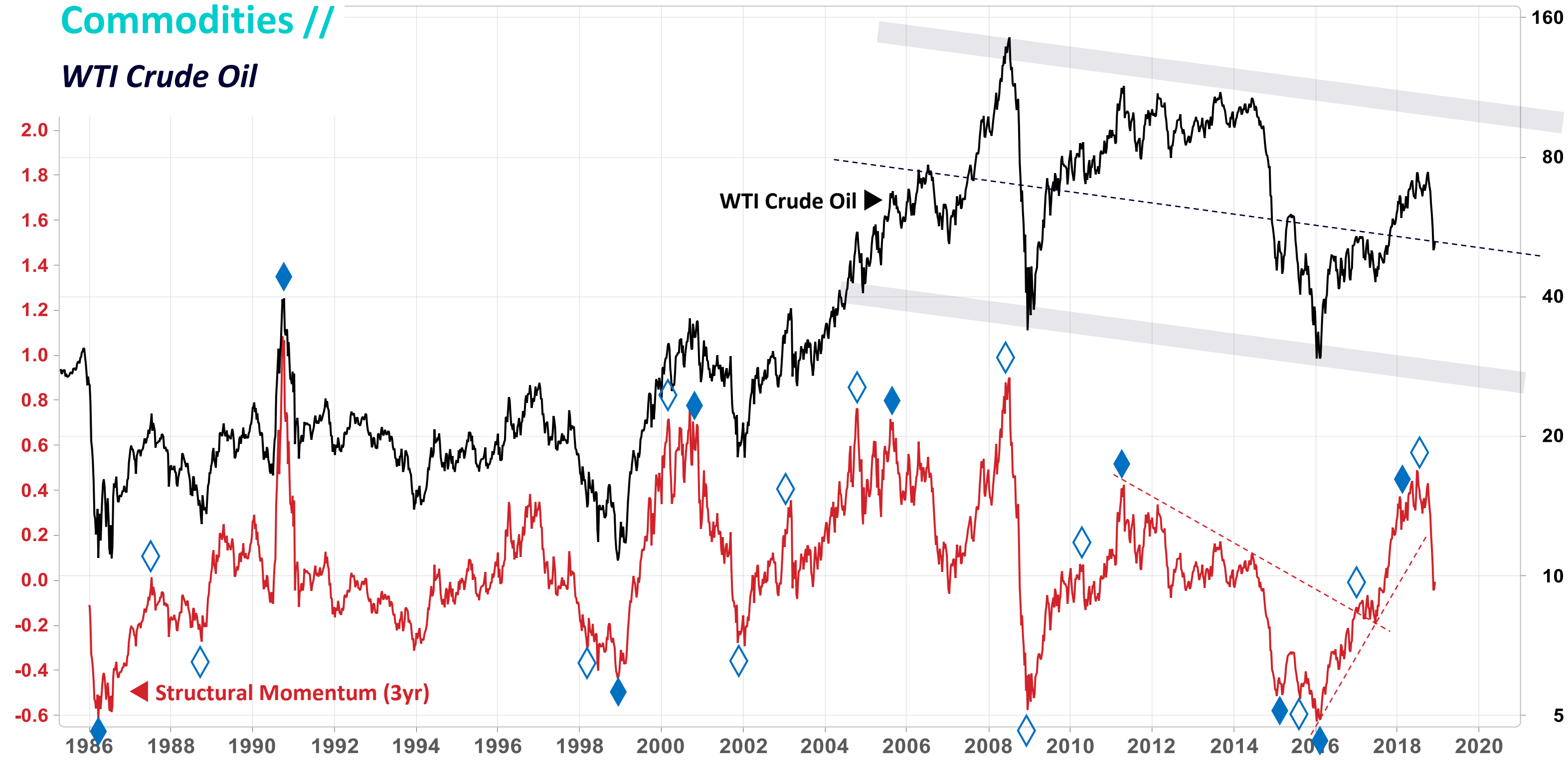
[Feb-2018…] *Gold miners are surprisingly weak given that Gold was trying to challenge a crucial resistance level. Viewing this sector in isolation of spot Gold, this framework suggests lower prices are likely.*

[Dec-2018…] *Some sort of tradable bounce appears to be setup, especially due to the positive Underlying Liquidity trends (amidst a recent Speculative crash in sentiment & marginal Patient Money buying) – however, we doubt the overall bear market is complete.*



Commodities //

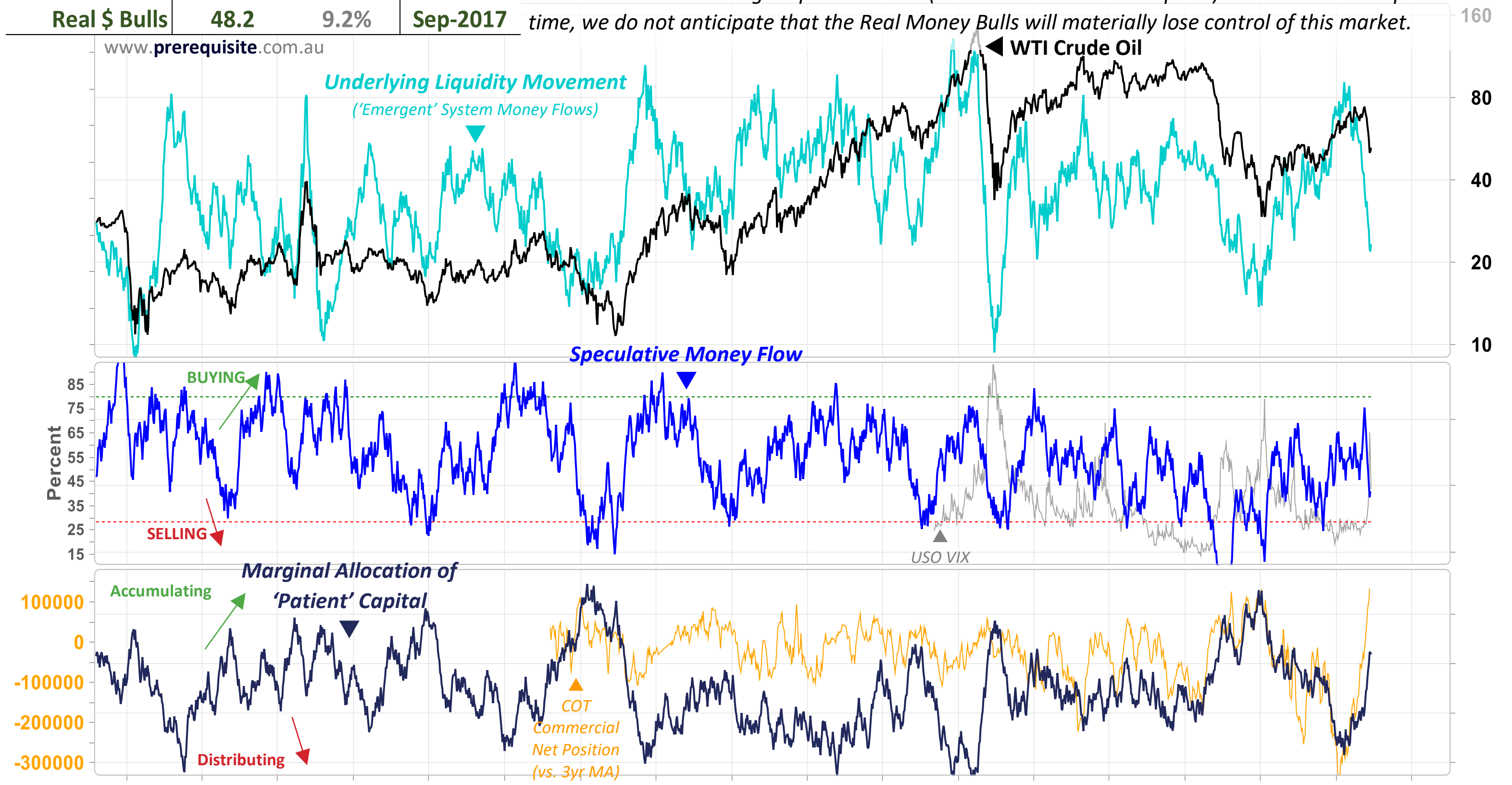
WTI Crude Oil



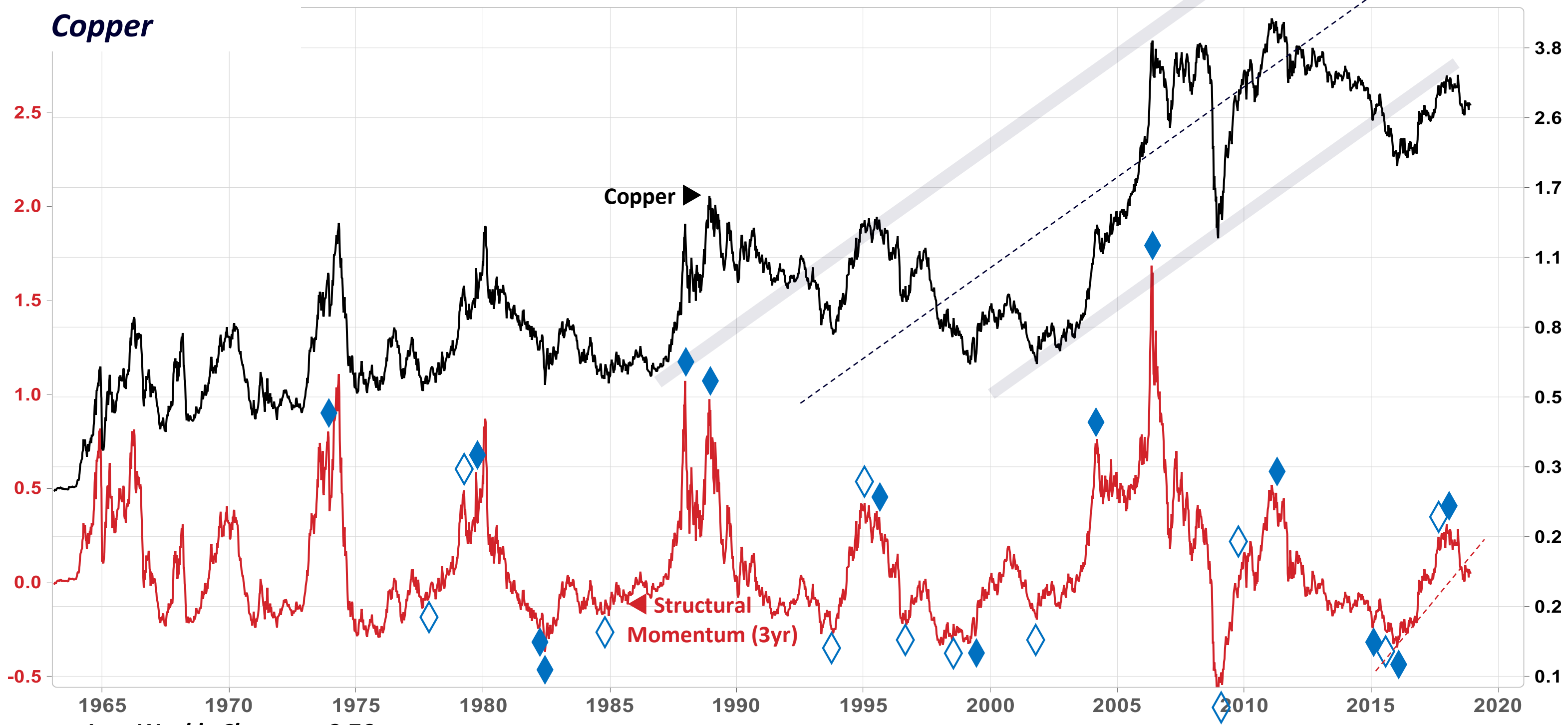
Last Weekly Close: **52.6**

	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**57.5**	8.6%	**Nov-2018**
Leveraged Bears	64.8	18.8%	Oct-2018
Leveraged Bulls	58.5	-10.1%	-
Real $ Bulls	**48.2**	9.2%	**Sep-2017**

Comments: **[Mar-2018…]** *Appears to be a healthy run unfolding from a broader perspective. Near term it could be ripe for a further pause/setback, even a move back to circa-$55 (or even a bit below) keeps the broader uptrend healthy. Momentum structure likely to morph into a sideways structure now that Major Liquidity signal has triggered.* **[Dec-2018…]** *The anticipated pull-back into the mid-50s was quite decisive, foreshadowed by a collapse in underlying liquidity. The Oil and broader energy complex on a multi-year basis still has all the classic hallmarks of being in the 'Wall of Worry' phase, with underlying trends toward overall higher prices in time (as detailed in the PCS Reports) still intact. At this point in time, we do not anticipate that the Real Money Bulls will materially lose control of this market.*



Copper



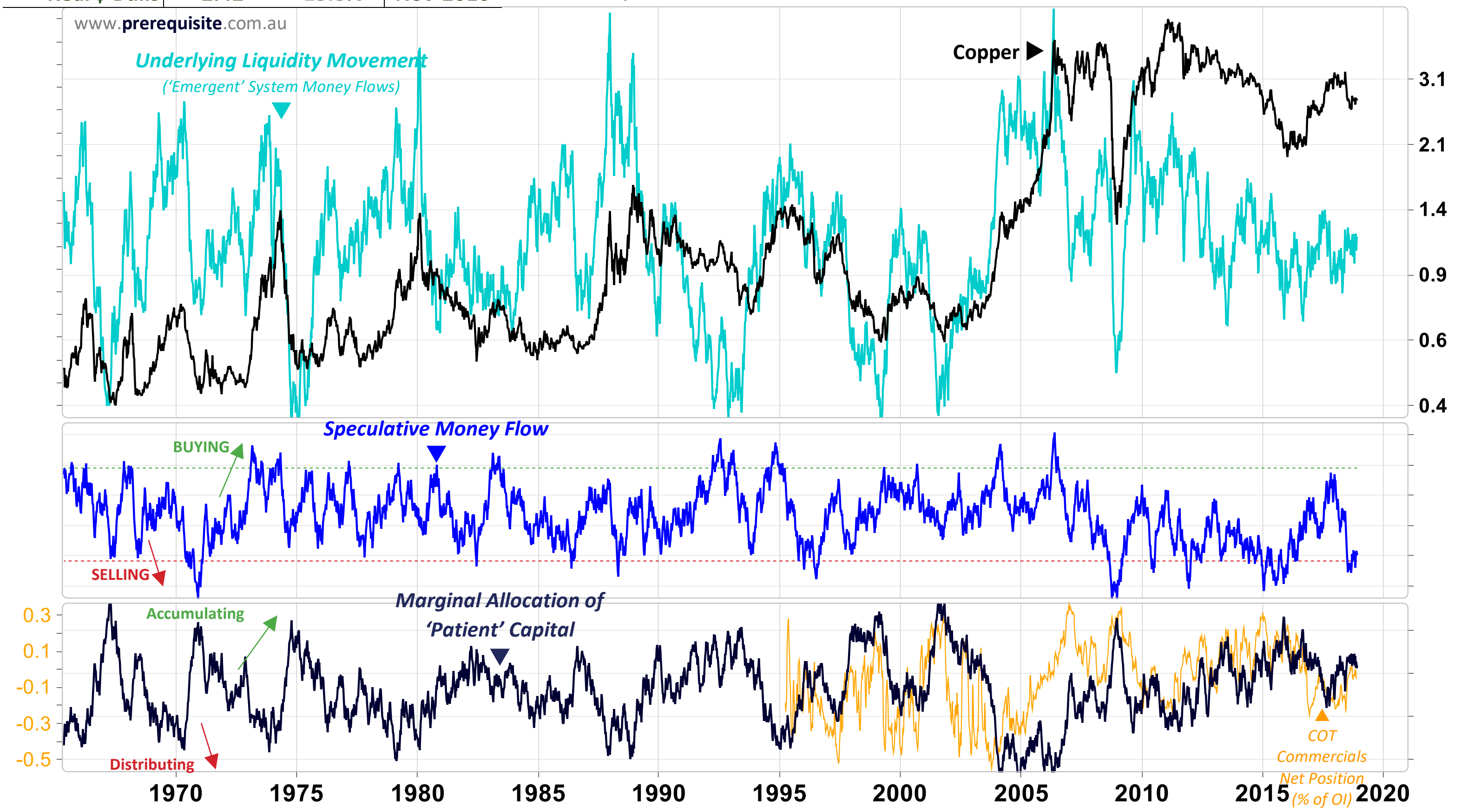
Last Weekly Close: **2.76**

	Point of Control (Threshold)	Perception of Control (Distance)	Date Control Began
Real $ Bears	**2.91**	**5.2%**	**Jul-2018**
Leveraged Bears	*2.96*	*6.9%*	*Jul-2018*
Leveraged Bulls	*2.70*	*2.0%*	*Sep-2018*
Real $ Bulls	**2.42**	**13.8%**	**Nov-2016**

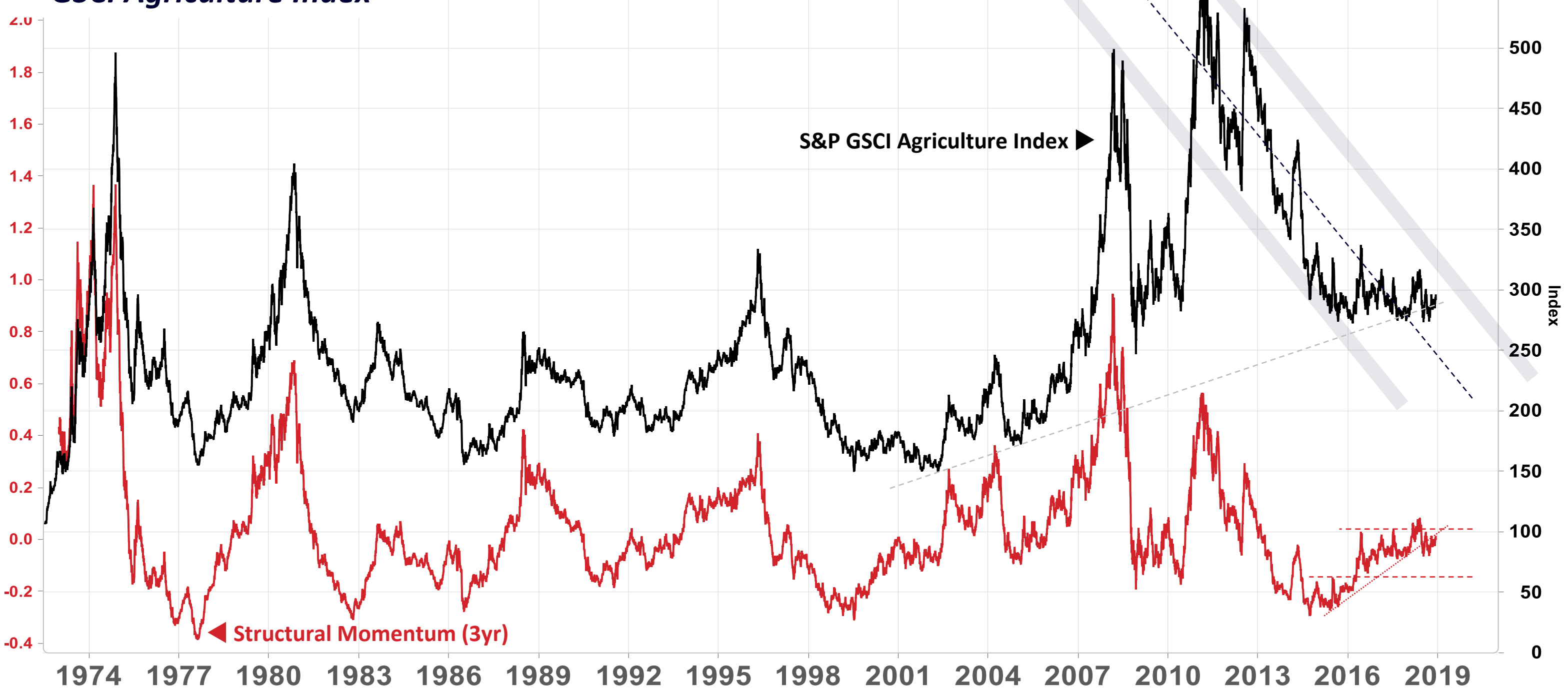
Comments:

[Feb-2018…] *Quite a weak picture here despite the run up it's had of late. It's not hard with these charts to make the case that a significant high is in the process of being established in Copper. (Charts of other industrial metals paint a similar picture.)*

[Dec-2018…] *Underlying Liquidity is still surprisingly weak, we also have 3yr Structural Momentum rolling over. Any bounce here should likely be faded. A cyclical bear market in Copper is likely underway.*



GSCI Agriculture Index



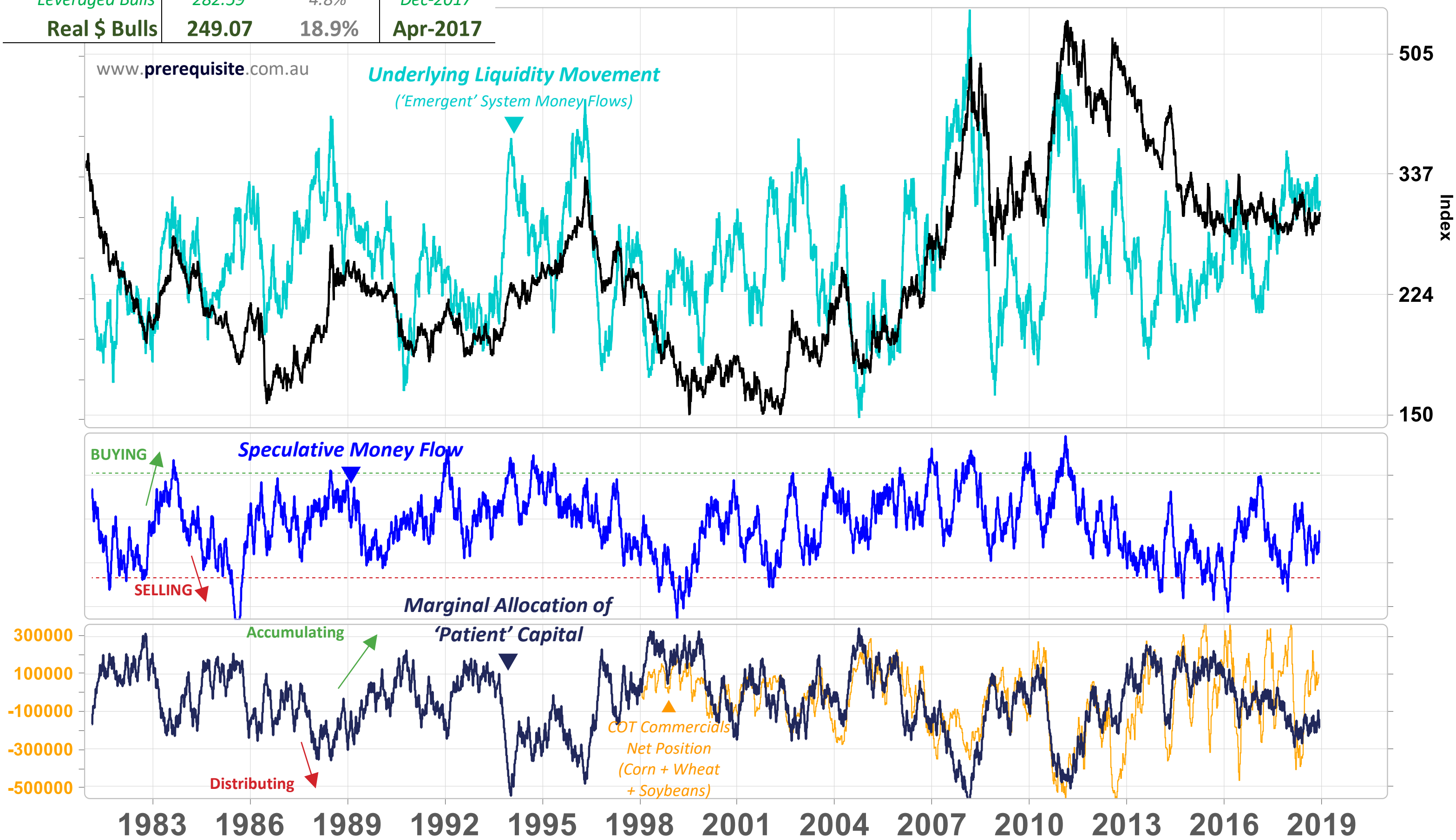
Last Weekly Close: **296.20**

	Point of Control (Threshold)	*Perception of Control* (Distance)	*Date Control Began*
Real $ Bears	**348.40**	**15.0%**	**Feb-2013**
Leveraged Bears	*301.75*	*1.8%*	*Feb-2017*
Leveraged Bulls	*282.59*	*4.8%*	*Dec-2017*
Real $ Bulls	**249.07**	**18.9%**	**Apr-2017**

Comments:

[No change to comments from January] *Worth monitoring. Early signs starting to appear of a more constructive setup, but still not quite there yet – caution is advised.*

[Aug-2018…] *Worth investigating, market is becoming more constructive, but not decisively clear that the bottoming process is complete.*



Appendix //

MARKET CYCLE THEORY...

The different participant categories for any market typically we find can be defined according to where they sit on the following continuums:

1. *TYPE:* **Demand or Supply orientation** (i.e.. are they a user/consumer, investor/speculator/financier, or supplier? If a financier, are they financing supply, use, or investment/speculation?)
2. *INFORMATION:* **Proximity to information** (i.e. in the stock market, CEOs & CFOs have 'inside' information, whereas the average person on the street typically sources info from the Newspapers or stockbrokers etc)
3. *BEHAVIOURAL BIASES:* **Incentives & Conflicts of Interests** (i.e. skin in the game, career-risk or conflict of interest issues, ASX listed management teams more focused on appeasing shareholders than doing what is best for the long term success of the company etc)
4. *CAPACITY:* **Financial capacities, likely pain thresholds and resiliency considerations** (leveraged speculators vs. people/entities with strong unleveraged balance sheets, exposure types, cash-flows, incomes, sensitivities to business/employment/credit cycles etc)
5. *SOPHISTICATION:* **Stewardship experience, sophistication, ability to anticipate market realities, and typical modus operandi** (i.e. the difference between say Brook and the average guy you find in a café talking about property, both have a vastly different range of experiences, sophistication in 'due diligence'/research, operation and approaches to decision making etc)
6. *CYCLE INTERACTION:* **Stereotypical cyclical behaviour** (procyclical, counter-cyclical, leading/coincident/lagging) – (how does this participant category typically interact with the property cycle? For example, the average person on the street is very pro-cyclical in a coincident almost lagging kind of way, usually the most enthusiastic with the most leverage at the top, and conversely doesn't want to even talk about property at the lows etc, such a person is kind of 'lagging' in nature as they'll be inclined to 'buy' the first small dip/wobble after the top just before the clean-out/downswing begins in earnest)

We have found that there are five main participant groups to any market that we find are helpful to monitor (please forgive the poor category names and acronyms for 4 & 5):

(1) The **'Speculative' Crowd**,
(2) the **'Patient Money' Crowd**,
(3) the **'Retail' Crowd,**
(4) the **'Career-Risk Informed Structural-Professionals' Crowd (CRISP)**, and
(5) the **'Experienced Entrepreneurial Structural-Professionals' Crowd (EESP).**

In most markets, 1 & 2 tend to be more orientated towards the 'financial economy' whereas 3-5 tend to be more operative in the 'real economy'. There are ways to measure the activities of these different participants in most markets.

To quickly explain each...

- The ***Speculative Crowd*** have a multi-month timeframe largely (say 6-24mths), and typically operate with leverage in line with momentum. ***This participant group tends to act in a coincident manner***, you typically want to 'flow' with them in the short term, but be wary & cautious of their extremes as price needs to keep moving in their direction or their leveraged structures will crumble and feed strongly in reverse.
- The ***Patient Money Crowd*** have a multi-year timeframe (say 2-5yrs), tend to operate without leverage but on a mean-reversion/fundamental-valuation type basis. ***This participant group tends to anticipate the market***, but in a reactionary manner depending upon their perceptions of price relative

to what they define as a 'fair fundamental value' of the market, you tend to want to pay attention to what they're doing only at extremes and consider doing some research to see if you should be acting in a similar manner, they do frequently however tend to be early.

The *Retail, CRISP* and *EESP* Crowds typically have a 7-14 year time cycle depending on the market in question.

- The ***Retail Crowd*** are the untrained/inexperienced masses who are doing precisely the wrong thing at cyclical peaks and troughs, disbelieving the trends until it's too late and they're sucked in. The 'everybody & their entourage' crowd, who bear the characteristics of being both novice & naïve in their level of sophistication pertaining to a market. ***The retail crowd tend to act in a manner that lags the cycle,*** at extremes they're always doing the wrong thing and investing based on their most recent experiences with their conviction levels dependent upon how long the most recent trend has been in place.
- The ***CRISP Crowd*** are professional Directors and Executive Managements of the typical company or commercial undertaking that controls vast resource and responsibility (relating to supply or demand in a market) but are co-opted by agency/incentive conflicts and are more concerned for what is 'fashionable' among peers and demanded by stakeholders (usually with less-expertise), examples include the boards and managements of the average resource company, or company managements that leverage up the balance sheet in order to fund buybacks or excessive acquisitions, or companies that proactively borrow in foreign currencies creating structural liability issues as the cycles unfold, or institutional investment managers that need to stay in line with benchmarks or fashionable backwards-looking performance stories etc. ***This participant group typically lags the cycle.*** It should be noted that Central Bankers most readily fit into this group.
- The ***EESP Crowd*** are professional larger-scale business owners and wholesale market operators who are running their own capital and are not constrained by career-risk, they tend to be quite shrewd with regards to positioning and timing. They almost perpetually are able to maintain a more sober perspective of cyclical developments as their strength of balance sheet and the disciplines of surviving multiple cycles and having capital at risk (rather than career risk exposure), they view their interactions with the market as either accumulating inventory *('inventory' in this sense being the securities or commodity units of the market in question)* at a discount or distributing inventories at a mark-up, they typically will only act to accumulate inventories provided they see a direct line of sight to demand to distribute into later – or at the tops. ***This participant group tends to act in an anticipatory manner, tend to be reasonably well-informed and frequently tend to lead the cycle.***

Of course, it is important to note that no Participant group necessarily has perfect forward-looking insight, but some are more successful than others, and when you put all the groups together in the context of basic conditions you can triangulate quite effectively where we are likely to be in the cycle.

"When a long-term trend loses momentum, short-term volatility tends to rise… It is easy to see why that should be so: the trend-following crowd is disoriented… It is the growth in speculative capital flows moving in a trend-following fashion that makes the trend so persistent; it is the persistence of the trend that makes trend-following so rewarding; and it is the rewards reaped by speculation that attract increasing amounts of capital.

"Don't try to play the game better, try to figure out when the game has changed."

…George Soros, The Alchemy of Finance

*Often tends to be more **Financial Economy** orientated* ⟵⟶ *Tends to be more **Real Economy** orientated*

www.prerequisite.com.au **STAGE OF MARKET TREND CYCLE:**	**PARTICIPANT CATEGORY:** Speculative *(Leveraged, Momentum)*	Patient *(Unlevered, Value Orientated)*	Retail *(Novice, Naïve)*	CRISP *(Career-risk, 'Professionals')*	EESP *(Capital-at-risk, Experienced)*
1. SHORT SQUEEZES & BEAR TRAPS: As a new uptrend commences from a bottoming process it is dismissed as a 'false hope' or 'false dawn' dynamic – yet higher lows and higher highs start to unfold.	Any bounces seen as new shorting opportunities, as a result the initial phases of the rise tend to have all the hall-marks of speculative money 'short-squeezes'.	The well-informed larger-money crowd tend to have already accumulated their positions.	At bottoms being involved in the market is equivalent to fueling your BBQ with $100 notes, people are concerned primarily for the base of the Maslow pyramid	Career risk informs that you are avoiding exposures. CAPEX of remaining firms is typically at major lows/non-existent.	Peak inventory load *('inventory' in this sense being the securities or commodity units of the market in question)*
2. A 'WALL OF WORRY': As the uptrend progresses it feeds on a 'wall of worry' as skepticism towards the market remains entrenched due to the magnitude of prior seasons of pessimism and loss cycles... yet at each test it proceeds higher in a resilient manner. <u>The trend is well-established and not likely to be broken in a hurry</u>, corrections bringing out swift & pronounced bouts of pessimism & worry.	The speculative crowd steps in but is yet still very flighty.	View the market as somewhat 'fairly valued'	Distrust predominates.	'Shell-shock' of previous rout keeps actions to a minimum and conservative disciplines predominate.	Inventories start to reduce
3a. CONFIDENCE WITHOUT RESPECT: As the uptrend progresses into its more mature phase, confidence builds (especially in the speculative crowd) to the point wherein it detaches from respect (i.e. complacency). The wall of worry has more or less been vanquished, and the market is trading more like a 'currency' than an 'asset' with speculators being rewarded and soberer & sophisticated operators struggling to fight the momentum. (Parabolic rises in price become possible, but keep stops tight – if a parabolic rise ensues, the sober/sophisticated operators begin to be taken out on stretchers).	The speculative crowd has embraced the new reflexive reality as if it could continue linearly forevermore.	The Pricing of the market detaches from a longer-term anchor of underling fair value, old school value guys view the market cynically.	Tops typically are when people are feeling in control, having a high degree of 'perceived' certainty, confidence without respect.	The structural players are by now finally starting to really embrace the bull market, with fashionable decision making by boards and career-risk focused managements embracing the trend en-masse.	Inventories running low
3b. VOLATILITY & DISTRIBUTION: As the uptrend weakens and transitions into a down-trend, volatility escalates, optimism holds despite the increasingly larger swings and shots across the bow. We start to see the beginnings of the 'uh-oh' effect from the more well-informed larger-money crowd which are likely to be distributing en-masse into the demand from the speculative and retail crowd (unless the last phase went parabolic, in which case the sophisticated but 'sober' crowd has been killed already, the risk of a vertical downward crash is high).	The 'buy the dip' mentality has been so well rewarded that you are seen as naïve if you still even talk about fundamentals (due to it being a new era/regime), and any suggestions at shorting are met almost aggressively by an emotionally-overinvested crowd.	Conviction arises to the point of a willingness to sell heavily (but if the market goes parabolic they'll be killed).	At the top, the strong assertion is that you are 'dumb/stupid' if you are not invested to the hilt, people are exhibiting characteristics similar to the peaks of the Maslow hierarchy.	Conservative disciplines have been completely rationalised away.	Inventories near-exhausted
4. BULL TRAPS & A NERVOUS 'BUY THE DIP' MENTALITY: In the early phases of a down trend all swings lower are simply opportunities to 'buy the dip', the commitments to the previous regime of complacency are too large to allow for the prospects of a downtrend commencing (almost a denial dynamic), yet lower highs and lower lows begin to form. The market tends to slide down the slope of 'this is good value' (the inverse of climbing a 'wall of worry' In Stage 2 above).	Emotional (& financial) over-investment causes a cognitive dissonance dynamic to prevail	Emboldened by the initial confirmation of their positioning	Emotional (& financial) over-investment causes a cognitive dissonance dynamic to prevail	Structural 'fashionable' Participants are fully over-committed and over-exposed, typically resisting the idea that they've blundered.	Falling prices causes only very muted or no-reaction in terms of starting to increase inventories again, concerns over line of sight to demand predominate

5. FEAR & PANIC (CONFIDENCE IS REFLEXIVELY CRASHING): As the down trend unfolds the pace of negative surprises escalates and fear becomes visibly observable – you typically see a wave of 'forced' sellers and the previous complacency is replaced by fear and even panic. The down trend is well-established and not likely to be broken in a hurry, at least until you start to see the volatility regime start to exhaust itself, wherein the next phase will be ushered in.	Collapse and capitulation	See market as running through fair value and slowly starting to buy again.	Collapse and capitulation	Write-offs and write-downs begin. The negative capitulation dynamics also set the scene for the next Stage (6) as companies with funding structure vulnerabilities are at increasing risk of creditor nervousness.	Inventory build gathering pace
6. PESSIMISM WITHOUT PERSPECTIVE (IRRATIONAL DETEST), & ACCUMULATION: As the down trend progresses into its more mature phase, the 'relative' pace and magnitude of negative surprises begins to abate (but still remain negative). Volatility escalates, pessimism holds despite the increasingly larger swings with a broader sideways range beginning to form.	The speculative crowd has embraced the new reflexive reality as if it could continue linearly forevermore, money flows/momentum continuing to try push the market lower.	The Pricing of the market detaches from a longer-term anchor of underling fair value, old school value guys start to show interest but still struggle as they're usually too early	Bottoms are when people feel an absence of control and high degrees of uncertainty, operating without confidence and being overcome by fear.	Structural participants (boards and fashionable management terms) capitulating and taking cold showers on everything (i.e. completion of write-down/write-off cycle etc). Bankruptcies occur & significant participants being put into Administration.	Peak inventory building activity

A popular visual representation of a market cycle, (that's not too dissimilar to the above table) can be seen in this graphic of a bubble progression (see below)... however, we must note that the stages of the cycle in the table above are more of a 'generalised cycle' variety and not necessarily of a 'bubble' progression as shown in the below visual diagram – however, in stage '3a' of the above table, if the market starts to go parabolic then the below 'bubble' diagram by Dr. Jean-Paul Rodrigue is a reasonably apt representation of the above table.

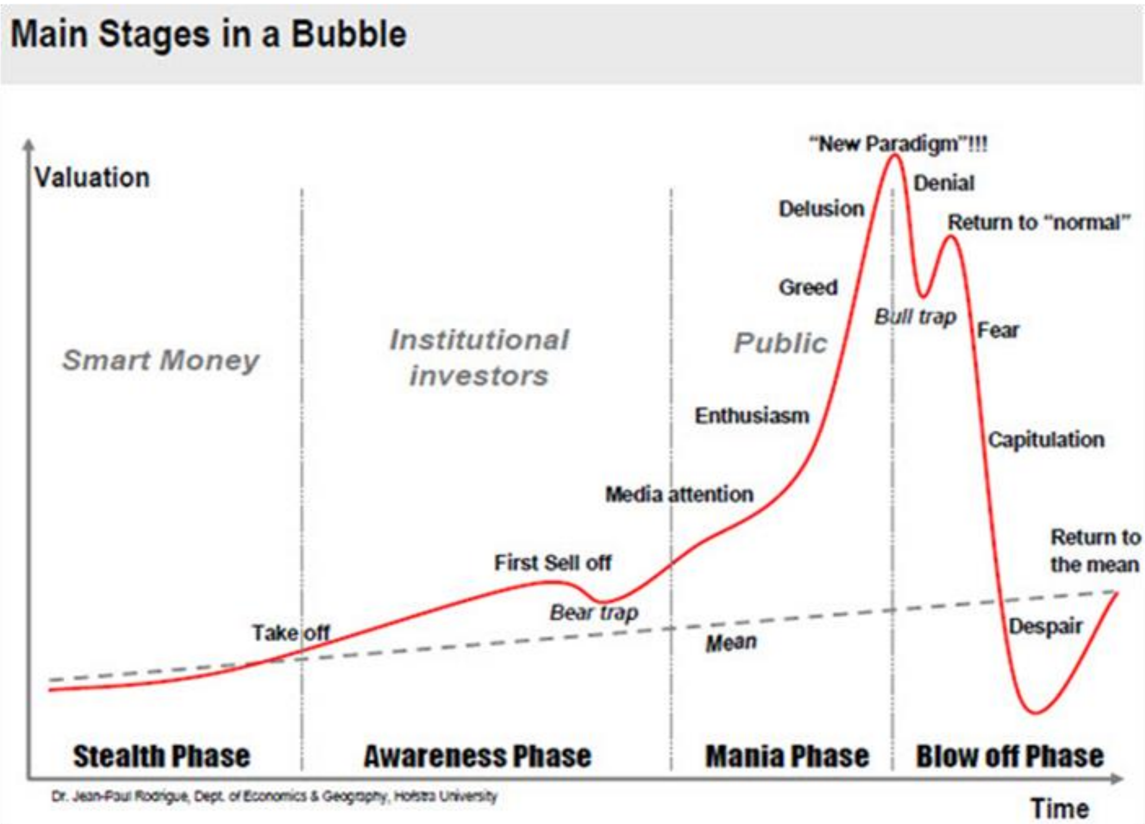
"You pay a very high price in the stock market for a cheery consensus." **…Warren Buffett**

"When reward is at its pinnacle, risk is near at hand." **…Jack Bogle**

"Typically bubbles have an asymmetric shape. The boom is long and slow to start. It accelerates gradually until it flattens out again during the twilight period. The bust is short and steep because it involves the forced liquidation of unsound positions." **...George Soros**

"Psychology in bear markets is always the same. Longs who say, "I don't care how low it goes, I will buy more" usually puke it out at the lows." **…Peter Brandt**

"The best time to buy is when blood is running in the streets." **…Nathan M. Rothschild**



"An investment in knowledge pays the best interest"

...Benjamin Franklin (1706-1790)

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