MORNING BRIEFING
November 13, 2017

Meltup Medley

See the collection of the individual charts linked below.

(1) It's beginning to look a lot like Xmas. (2) Santa Claus meltup? (3) Will Republicans deliver honey cake or humbug for the holidays? (4) Solid earnings and global fundamentals driving stock prices up more than expectations of tax cuts. (5) The bulls are all coming home for the holidays. (6) Nothing to fear but unrealistically high LTEG. (7) As P/E goes up, PEG comes down. (8) Gift wrap up some equity ETFs with foreign exposure to give to your loved ones. (9) Movie review: "LBJ" (+ + +).

Strategy: Early Christmas. Have you noticed? It isn't even Thanksgiving yet, and yet stores are already decorated for the Christmas holiday and radio stations are starting to play Christmas songs. Hearing too much Christmas music can be bad for your mental health, research shows; psychologist Linda Blair told Sky News: "It might make us feel that we're trapped—it's a reminder that we have to buy presents, cater for people, and organize celebrations."

On the other hand, the stock market often tends to do well after Thanksgiving through Christmas and into the first day of the New Year. This recurring phenomenon has been dubbed the "Santa Claus rally." The weakness in the stock market late last week was caused by concerns about whether the Republicans can get a tax reform deal done before Christmas, as promised by President Donald Trump. Nevertheless, there's already some chatter that the Santa Claus rally could start earlier than usual this year. That's certainly likely to be the case if Republicans make some progress toward completing a deal.

Last year's Santa Claus rally has morphed into this year's meltup. The S&P 500 is up 17.1% since Thanksgiving of last year through Friday. It's been rising into record territory all this year (*Fig. 1*). It's up 20.7% since Trump won the election on November 8 of last year. The latest record high was hit on November 8 when the S&P 500 closed at 2594.38. It is down only 0.5% since then.

Joe and I have been observing since the summer of 2016 that earnings are improving because the energy-led earnings recession is over. Starting late last year, Debbie and I have been noting that the global economy is showing mounting signs of strength. In other words, the market has been boosted by solid fundamentals. Trump's victory and potential corporate tax cuts were icing on the Yule log cake. In other words, if the Republicans fail to do a deal, that won't turn us bearish. If they do a deal, we will be concerned about a Santa Claus meltup. Now let's sit by the fire and play a medley of meltup songs:

(1) *Jingle bull rock.* The bulls are all coming home for the holidays. Investors Intelligence's Bull/Bear Ratio (BBR) soared to 4.47 last week (*Fig. 2*). That's the highest reading since March 1987. The 52-week average was 3.17 last week. Readings above 3.0 for this moving average are rare.

Are there too many bulls? Contrarians might think so, but the BBR works better as a contrary buy signal when the ratio is at 1.0 or less than as a sell signal when it is at 3.0 or more (*Fig. 3*).

The percentage of bears in the Investors Intelligence survey remained at 14.4% last week, the lowest since May 2015 (*Fig. 4*).

(2) *LTEG: Do you fear what I fear?* Joe and I are getting a sense of déjà vu all over again as we watch S&P 500 long-term consensus earnings growth expectations (LTEG) going vertical since early last year (*Fig. 5*). Thomson Reuters compiles this series based on analysts' consensus expectations for the earnings growth of the S&P 500 companies over the next five years. LTEG has jumped from last year's low of 9.6% during March to 13.8% last month, the highest reading since April 2002. Leading the way recently is the LTEG for the S&P 500 Information Technology sector at 16.2% during October (*Fig. 6*).

(3) *Valuation: You'd better watch out.* The good news is that rising LTEG expectations are making stocks look more attractive based on the ratio of the S&P 500 stock price index to its LTEG (*Fig. 7*). This PEG ratio for the S&P 500 has declined from a record high (starting in 1995 for this series) of 1.7 during the week of January 28, 2016 to 1.3 at the start of November.

That's great as long as those LTEG estimates make sense, which they don't. They are too high, though not as high as their 2000 peaks of 18.7% for the S&P 500 and 28.7% for the index's IT sector. They seem to be heading in that direction again, which could fuel a meltup by investors driven by FOMO (i.e., fear of missing out).

The more traditional measure of valuation is elevated, but not excessively so. We are referring to the S&P 500 forward P/E, which rose to a cyclical high of 18.0 in early November, the highest since March 2004 but well below the July 1999 peak of 25.3 (*Fig. 8*). That's not cheap, but valuation metrics that account for inflation, like the real earnings yield and the Rule of 20, show that the market is fairly valued (*Fig. 9*) and (*Fig. 10*).

(4) *All I want for Christmas is an ETF.* Data available on equity mutual funds and ETFs, compiled by the Investment Company Institute, are available through September (*Fig. 11*). Collectively, over the past 12 months, these funds attracted $275.2 billion, up sharply from $21.6 billion a year ago and the best such inflow since July 2015. On a 12-month basis, equity mutual funds have had net outflows since March 2016, though the pace has been slowing. The big story is the big inflows into equity ETFs totaling $349.6 billion over the past 12 months.

Investors seem to be especially interested in exposure to foreign equities. The outflows from equity mutual funds have been all among domestic equity mutual funds, which lost $154.6 billion over the past 12 months (*Fig. 12*). Meanwhile, over the same period, US mutual funds investing globally attracted $80.3 billion.

A similar analysis of equity ETFs over the past 12 months shows that domestic ETFs attracted $210.3 billion, which was slightly below June's record pace (*Fig. 13*). While net inflows into global/international equity ETFs was less than for the domestic ETFs at $139.3 billion, that was a record amount.

Movie. "LBJ" (+ + +) (*link*) is a very well crafted movie about Lyndon B. Johnson before and after John F. Kennedy was assassinated. Woody Harrelson provides a great performance as LBJ, who had a great need to be loved but was certainly hated by Bobbie Kennedy. Director Rob Reiner is one of Hollywood's more liberal denizens, so the movie focuses on LBJ's achievement in passing the Civil Rights Act of 1964 rather than his role in widening the war in Vietnam.

CALENDARS

US. Mon: Treasury Budget -$58.0b. **Tues:** Small Business Optimism Index 105.0, PPI-FD Headline, Core, and Core Ex Trade Services 0.1%/0.2%/0.2%, Yellen, Evans. (Bloomberg estimates)

Global. Mon: Japan Machine Tool Orders, Kuroda. **Tues:** Eurozone GDP 0.6%q/q/2.5%y/y, Eurozone Industrial Production -0.6%m/m/3.2%y/y, Eurozone Economic Sentiment, Germany GDP 0.6%q/q/2.3%y/y, Germany CPI 0.0%m/m/1.6%y/y, Germany ZEW Expectations 19.5, Italy GDP 0.5%q/q/1.7%y/y, UK Headline & Core CPI 3.1%/2.8% y/y, Japan GDP 0.4%q/q/0.1%y/y, China Retail Sales 10.5% y/y, China Industrial Production 6.2% y/y, Draghi, Carney, Kuroda. (DailyFX estimates)

STRATEGY INDICATORS

Global Stock Markets Performance (*link*): The US MSCI index fell 0.2% last week for its first decline in nine weeks, but ranked 20th out of the 49 markets as 16 countries rose in US dollar terms. That compares to 32nd a week earlier, when it rose 0.3% as 35 countries moved higher. The AC World ex-US index, also with a 0.2% decline, slightly outperformed the US MSCI for just the fifth time in 11 weeks; that result compares to a 1.1% gain a week earlier. Most emerging market regions rose w/w, but EM Eastern Europe performed best as it gained 3.4%, followed by BRIC (1.2), EMEA (1.1), and EM Asia (0.3). EMU was the worst-performing region as it fell 1.8% w/w, followed by EM Latin America (-0.6), and EAFE (-0.4). Russia was the best-performing country, with a gain of 5.4%, followed by Colombia (3.7), China (2.4), Czech Republic (2.0), and Morocco (1.9). Greece was the worst performer as it fell 6.0%, followed by Belgium (-3.0), Argentina (-2.4), and India (-2.4). The US MSCI is up 15.5% ytd, with its ranking improving one place w/w to 30th of the 49 markets, but continues to trail the AC World ex-US (21.0) on a ytd basis. Forty-four of the 49 markets are positive ytd, led by Argentina (62.0), China (51.1), Austria (50.3), Poland (45.8), Korea (44.1), and Chile (33.2). The worst country performers ytd: Pakistan (-25.3), Israel (-12.8), Jordan (-3.9), New Zealand (-1.6), and Russia (-0.2). EM Asia is the best-performing region ytd with a gain of 38.3%, ahead of BRIC (36.9) and EMU (23.4). The worst-performing regions, albeit with gains: EMEA (8.1), EM Eastern Europe (10.8), EM Latin America (17.7), and EAFE (18.7).

S&P 1500/500/400/600 Performance (*link*): Last week, LargeCap edged down 0.2% for its first decline in 10 weeks, but fell less than the MidCap (-0.6%) and SmallCap (-0.8) indexes; they both fell for a second straight week. LargeCap ended the week 0.5% below its record high on Monday, but MidCap was down 1.0% from its October 27 record and SmallCap was 2.7% below its October 3 record. Fifteen of the 33 sectors rose w/w, compared to 10 a week earlier. Energy and Real Estate dominated last week's biggest gainers: SmallCap Energy (5.0%), MidCap Energy (4.1), LargeCap Real Estate (3.2), MidCap Real Estate (2.2), and SmallCap Telecom (2.2). Last week's worst performers: MidCap Telecom (-8.3), SmallCap Consumer Staples (-3.9), MidCap Health Care (-3.5), and LargeCap Financials (-2.7). Twenty-three of the 33 sectors are positive ytd, down from 25 a week earlier, as LargeCap (15.3) continues to outperform both MidCap (9.9) and SmallCap (6.7). Health Care and Tech dominate the biggest sector gainers ytd: LargeCap Tech (37.1), SmallCap Health Care (25.0), MidCap Tech (24.3), MidCap Health Care (18.1), LargeCap Health Care (17.8), and SmallCap Utilities (17.3). Telecom and Energy dominate the worst performers ytd: MidCap Telecom (-50.5), SmallCap Energy (-27.6), MidCap Energy (-20.7), LargeCap Telecom (-18.5), and LargeCap Energy (-7.4).

S&P 500 Sectors and Industries Performance (*link*): Five of the 11 sectors rose last week, and six outperformed the S&P 500's 0.2% decline. This compares to four sectors rising a week earlier, when four outperformed the S&P 500's 0.3% rise. Real Estate was the best-performing sector as its 3.2% gain beat these other outperforming sectors: Consumer Staples (2.1%), Energy (1.1), Consumer Discretionary (0.7), Utilities (0.4), and Tech (0.0). Financials (-2.7) was the worst performer, and was followed by these underperformers: Telecom (-1.3), Materials (-1.2), Industrials (-1.1), and Health Care (-0.5). So far in 2017, nine of the 11 sectors are higher, but only three have outperformed the S&P 500's 15.3% gain. If that holds to the end of the year, it would mark the narrowest number of outperforming sectors since 3/11 sectors beat the market in 2009, and 3/10 way back in 1982. The best performers in 2017 to date: Tech (37.1), Health Care (17.8), and Materials (16.6). The seven sectors underperforming the S&P 500 ytd: Telecom (-18.5), Energy (-7.4), Consumer Staples (5.0), Real Estate (9.6), Industrials (11.7), Financials (11.8), Consumer Discretionary (13.5), and Utilities (13.9).

Commodities Performance (*link*): Eighteen of the 24 commodities we follow rose last week as the S&P GSCI commodities index rose 1.9%. That compares to 18 commodities advancing a week earlier, when the GSCI index rose 2.1% on the heels of a 2.4% gain, which then was its best in 13 weeks. The week's strongest performers: Natural Gas (10.2%), Cocoa (7.4), Lean Hogs (5.5), Coffee (5.1), and Kansas Wheat (4.7). Last week's biggest laggards: Nickel (-4.8), Aluminum (-3.7), Feeder Cattle (-2.7), and Copper (-1.5). Industrial metals-related commodities dominate the best performers in 2017 so far: Zinc (25.7), Feeder Cattle (25.6), Lead (25.4), Aluminum (23.9), Copper (22.5), and Nickel (21.0). This year's laggards: Sugar (-23.3), Natural Gas (-11.7), Coffee (-5.0), Cocoa (-2.2), and Soybeans (-1.7).

Assets Sorted by Spread w/ 200-dmas (*link*): Spreads between prices and 200-day moving averages (200-dmas) rose last week for 17/24 commodities, 2/9 global stock indexes, and 14/33 US stock indexes compared to 18/24, 6/9, and 7/33 rising a week earlier, respectively. Commodities' average spread surged w/w to 6.6% from 4.9%. Sixteen commodities trade above their 200-dmas, up from 15 a week earlier. Heating Oil now leads all commodities and all assets at 19.7% above its 200-dma, but Natural Gas (7.6%) rose 9.9ppts w/w for the best performance of all commodities and all assets. Heating Oil is followed closely by Brent Crude (19.2), and GasOil (18.3). Nickel (17.5.) was the next best, but fell 6.6ppts for the worst performance of all commodities and all assets. Cotton (-4.9) trades the lowest of all commodities relative to their 200-dmas, followed by Corn (-3.4) and Sugar (-3.3). The global indexes trade at an average of 7.6% above their 200-dmas, down from 8.6% in the prior week. All nine of the global indexes trade above their 200-dmas, unchanged from a week earlier. Japan (13.9) leads the global indexes followed by China (13.1), which improved 2.8ppts w/w for the best performance among its peers. Germany (5.5) fell 3.2ppts for the worst performance among the global indexes. The UK (0.6) trades the lowest among its country peers, followed by Canada (3.7). The US indexes trade at an average of 2.5% above their 200-dmas, with 27 of the 33 sectors above, down from an average of 2.9% a week earlier, when 25 sectors were above. LargeCap Tech leads all US stock indexes at 14.8% above its 200-dma, but SmallCap Energy (1.2) gained 5.7ppts w/w for the best performance of the US stock indexes. MidCap Telecom trades at a sharp discount relative to its 200-dma of 32.0%, the lowest among the US stock indexes and all assets, and fell 4.8ppts w/w for the worst performance among the US indexes last week. Also trading well below their 200-dmas are LargeCap Telecom (-9.7) and MidCap Consumer Staples (-4.6).

S&P 500 Technical Indicators (*link*): The S&P 500 index remained in a Golden Cross last week for an 81st week (after 17 weeks in a Death Cross), but both the short-term and long-term technicals weakened for a third straight week. The index's 50-day moving average (50-dma) relative to its 200-dma rose to a 12-week high of 4.1% from 3.9% a week earlier. That compares to a 34-month high of 5.4% in early April, a 39-week low of 3.4% in early October, and a 52-month low of -4.5% in March 2016. The S&P 500's 50-dma and 200-dma both rose together for a 12th straight week, after failing to rise together in mid-August for the first time in 36 weeks. The index closed above its 50-dma for an 11th week after three weeks below, which was its worst streak since it closed below its 50-dma for 10 straight weeks from September 2016 until the November election. The S&P 500 fell to a seven-week low of 1.8% above its rising 50-dma from 2.6% a week earlier, which compares to a 33-week high of 3.1% three weeks ago and a four-month low of 1.0% below its falling 50-dma in mid-August. These 50-dma readings compare to a 38-week high of 4.8% on December 13 and a 52-month high of 6.2% in March 2016. The S&P 500 fell to 6.0% above its rising 200-dma from 6.5% a week earlier, which compares to a 13-week high of 6.7% four weeks ago and a post-election low of 3.0% above its rising 200-dma in mid-August. That's down from a 38-month high of 9.4% on March 1, but up from an eight-month low of -0.1% immediately before the election.

S&P 500 Sectors Technical Indicators (*link*): Among the 11 sectors, four improved w/w relative to their 50-dmas and five relative to their 200-dmas. These four had improvements in both moving averages: Consumer Discretionary, Consumer Staples, Real Estate, and Utilities. Eight of the 11 sectors trade above their 50-dmas, unchanged from a week earlier as Consumer Staples moved above for the first time in eight weeks and Industrials moved below for the first time in nine weeks. Telecom was below for a fifth straight week and Health Care for a second week. Still, that's a turnaround from mid-August, when just three sectors traded above their 50-dmas (matching mid-April's reading, which was the lowest since the election). All 11 sectors had been above their 50-dmas during mid-January, and all 11 were below the week before the election, for the first time since December 11, 2015. The longer-term picture is similarly strong: Nine of the 11 sectors were above their 200-dmas last week, unchanged from a week earlier. Energy traded above its 200-dma for a seventh week after 29 weeks below; Consumer Staples was below its 200-dma for an eighth week after 32 straight weeks above; and Telecom ended the week below its 200-dma for a 33rd straight week. Nine sectors are in a Golden Cross, with 50-dmas higher than their 200-dmas, up from eight a week earlier, as Energy joined the club for the first time in 31 weeks. Consumer Staples was out of the Golden Cross club for a fourth week and for the first time since early March; Telecom was out for a 35th week. All 11 sectors had been in a Golden Cross during a 21-week streak that ended in late October of 2016, the longest such stretch since October 2014. Nine of the 11 sectors have rising 50-dmas, unchanged from a week earlier. Consumer Staples' 50-dma has been falling for eight weeks, and Telecom's for six weeks. Nine sectors have rising 200-dmas, unchanged from a week earlier. Energy's 200-dma fell for a 28th straight week, and Telecom's dropped for an 11th week.

US ECONOMIC INDICATORS

Consumer Sentiment (*link*): Confidence in November fell more than expected, according to the preliminary estimate, though has remained trendless around recent highs since the start of the year. The Consumer Sentiment Index (CSI) slipped to 97.8 this month after rebounding 5.6 points in October to a 13-year high of 100.7. Consumers were slightly less optimistic about both the present and future. The present situation component slumped to 113.6—the second best reading since November 2000—behind last month's 116.5 reading. The expectations component slipped to 87.6, only 2.9 points below October's 33-month high of 90.5.

GLOBAL ECONOMIC INDICATORS

Global Leading Indicators (*link*): In September, the OECD's composite leading indicators (CLIs)—designed to anticipate turning points in economic activity relative to trend six to nine months ahead—once again pointed to stable growth momentum in the OECD (100.2) as a whole. CLIs for the Eurozone (100.6)—including France (100.5)—Canada (100.4), Japan (100.1), and the United States (99.7) continued to show stable growth momentum. Meanwhile, CLIs for Italy (100.6) and Germany (100.1) have been upgraded and are showing signs of gaining momentum. The UK's (99.5) CLI, on the other hand, has weakened as signs of "easing growth have intensified," according to the report. As for the emerging economies, CLIs point to growth gaining momentum in the industrial sector in China (99.7) and firming in Brazil (103.3), while stable growth momentum is anticipated in Russia (100.8) and India (99.9)—an upgrade for the former and a downgrade for the latter.

France Industrial Production (*link*): Industrial production in September rose more than expected, returning to its recent high. Headline production, which excludes construction, advanced for the second time in three months by 0.6% in September (above expectations) and 1.2% over the period, back up at May's six-year high. Factory output also expanded for the second time in three months, by 0.4% m/m and 0.8% over the three-month span. Consumer durable goods production led September's gain, but remains volatile, jumping 5.4% after a 5.3% plunge in August and a 6.2% surge in July; consumer nondurable goods production rebounded 2.9% after three-month slide of 4.1%. Intermediate goods output was in the black for the third month, up 1.2% over the period, to its highest reading since the start of 2012. Meanwhile, capital goods output retreated 1.4% after rebounding 2.8% the prior two months to a six-year high. October's M-PMI held at September's 77-month high as both output and new orders expanded at marked rates.

Italy Industrial Production (*link*): Output in September plunged after reaching more than a five-and-a-half-year high in August. Production slumped 1.3% after a four-month surge of 3.2% to its highest level since December 2011. Manufacturing output fell 1.3% and rose 3.5% over the comparable periods. Sharp declines in intermediate (-3.0%) and capital (-2.0) goods production more than offset a 4.7% jump in consumer durable goods output during September. Meanwhile, Italy's October M-PMI (57.8) climbed to six-and-a-half-year high as both output and new orders accelerated at their best rates since 2011 and jobs creation was the highest since the survey started in June 1997.

UK Industrial Production (*link*): UK industrial output in September blew past forecasts to its highest reading since October 2008. Production expanded 0.7% in September, more than double consensus expectations of a 0.3% gain—and the strongest performance so far this year. It was the sixth consecutive monthly advance, for a total gain of 2.1%, more than reversing the 1.8% contraction the first three months of the year. Manufacturing output accelerated by 0.7% in September and 1.8% the past five months, after beginning the year with a four-month drop of 1.9%. September's advance was fairly widespread, led by a 1.7% jump in capital goods production (which has surged 4.7% the past four months) to a new record high! Also in the plus column in September was consumer durable (1.1) and intermediate (0.9) goods production; consumer nondurable goods (-0.8) output contracted. Markit's manufacturing report for October showed an acceleration in manufacturing activity as its M-PMI rose from 56.0 to 56.3, well above its long-run average of 51.7. The report noted that both production and new order volumes continued to expand at robust rates, benefitting from both strong domestic and foreign demand.

Mexico Industrial Production (*link*): Earthquakes sent industrial production south in September, though output has been drifting lower since April. Headline production fell 0.4% after a 0.2% rise in August and a 0.7% fall in July. Most of September's setback was caused by a 10.0% plunge in oil & gas production—which was the sixth straight decline, for a total drop of 14.4%. Manufacturing production ticked down 0.1% in September after a three-month advance of 1.3% to a new record high. Utilities usage rebounded 1.8% m/m after a two-month decline, while construction output rose 0.8%, though lacks direction this year. On a year-over-year basis, headline production fell 1.2% as mining output plunged 15.1%—the steepest decline since October 1995. Manufacturing's (2.8 y/y) and utilities' (1.4) output results were above year-ago levels, while construction's (0.1) was flat. Markit's October M-PMI (to 49.2 from 52.8) shows manufacturing activity contracted last month for the first time since July 2013 in the aftermath of the earthquakes.

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