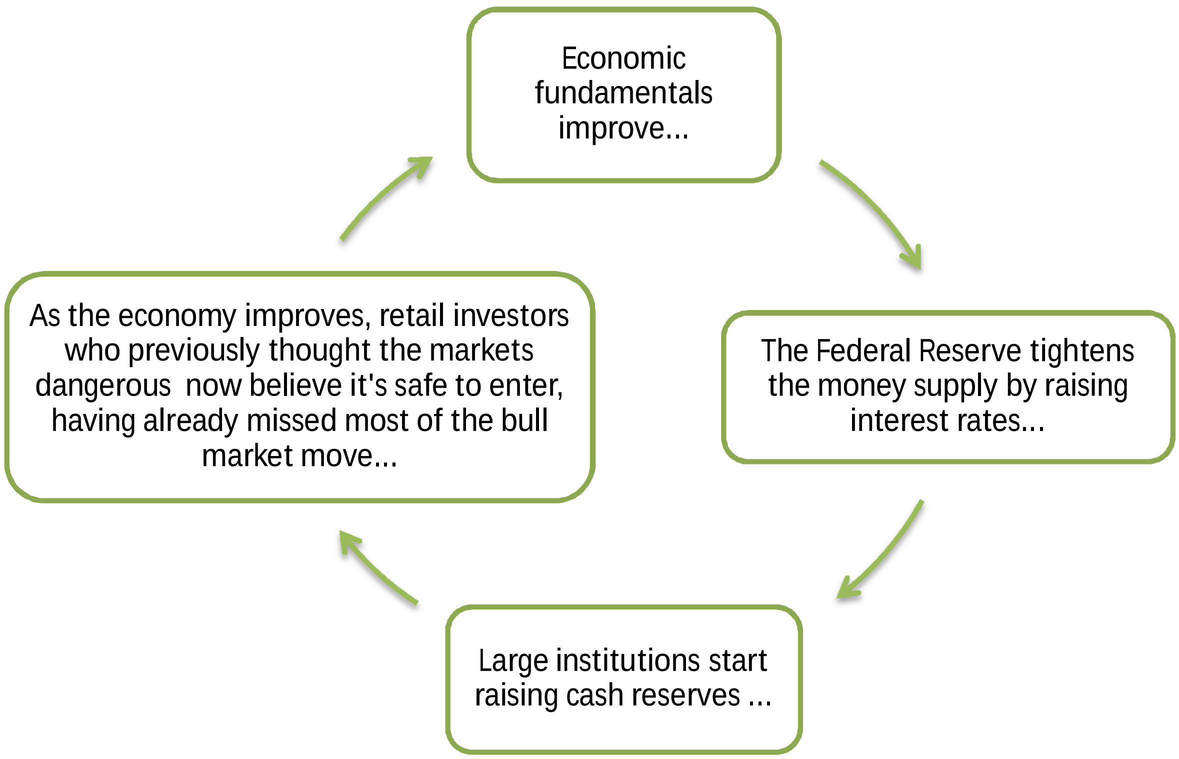
Executive Summary

I. Bull-to-Bear Transitions and Severe Market Corrections: How They Happen



II. Current Economic Backdrop

a. The current unemployment rate is 4.3%.
b. The Federal Reserve has tightened the money supply by raising interest rates three times in the last year and is expected to continue doing so over the next year.
c. Major institutions have been increasing their cash reserves.
d. Retail and day traders are all in and are highly leveraged on margin.
e. Inflation has not yet shown its tentacles, but commodities and emerging markets appear to have entered new bull markets after having under-performed US and European equities over the last 5 years. At the same time, it appears that the 30-year bond bull market is over and this should become more evident as inflation starts to rise.

f. Even though Donald Trump has not yet been able to make good on his major economic plan, the economy has been improving on its own accord. Most likely, inflation expectations will rise if his infrastructure and tax plans make it through. Corporate profit margins are at all-time highs, but this will not be sustainable if wages rise. Employee wages on the whole have not followed profit margins so far. It's an area to keep an eye on. If wages go up, corporate profit margins may decline.

III. Market Backdrop

a. Stock market overvaluation is at its highest level in history other than during a short period in March of 2000. We all remember how that turned out.
b. Market trading is vastly different from what it was only five years ago.
    - Today, the bulk of daily market trading volume is robotic, high frequency, dark pool, and algorithmic trading.
    - Actual humans are rarely involved in these operations.
    - If and when there is any crisis of confidence with investors and traders due to an exogenous event, the likely scenario would be a reversal of the algorithms' bullish bias and increased volatility. Previous examples of their volatility include "Black Monday" of 1987, when the S&P500 fell 22% in one day and 35% in three weeks, as well as the flash crashes of May 2010 and August 2015. These were all within the context of bull markets, but were painful nevertheless.
    - The Federal Reserve has announced plans to sell back the five trillion dollars of bonds it acquired via quantitative easing. Nobody knows how this can be accomplished without resulting in much higher interest rates. Add monetary tightening via other methods and a possible loss of confidence due to an exogenous event and the result may be a market decline of unknown length and proportion.
    - Didier Sornette, an acknowledged mathematical expert on market bubbles and crashes, states that another crash is inevitable:
        - There are fundamental structural flaws in our financial and economic systems which were aggravated by the Federal Reserve's unprecedented need to rescue the financial markets two times in the last seventeen years.
        - These flaws have remain unfixed.

IV. Current Strategy

- Hold some cash reserves.
- New investments are going into commodities and emerging markets which are currently undervalued relative to US and European markets.
- The media has been splashing the airwaves daily with news of all time highs in the Dow Jones Industrials.
    - There are only thirty stocks in this index and it is easily moved by increases in just a few high priced stocks like Boeing and McDonald’s. Also, many major indexes (i.e., S&P 500 and Nasdaq 100) are constructed in a way that allows movement in just a few overvalued mega-cap stocks (e.g., Amazon, Facebook, Google) to make it appear that everything is wonderful. This is the same situation seen just prior to the market top of 2000.
    - No one knows how long the current situation can last. The major indexes continue to hold up on the surface, but there’s been internal deterioration over the last year.