

Your weekly market update

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## Market Update

14 April 2016

**History and the study of past events can help see what may be unfolding in front of us. In the last few year, I have discussed that China is headed for a collapse and massive restructuring must take hold.** Back in 1997 and 1998 we saw the same events unfold labelled as the Asian flu and Russian ruble collapse.

The Federal Reserve was tightening monetary as the American economy was strengthening.

Europe was on a slow but improving economic path. China and emerging markets sharply declined after the deep devaluation of the Yen by the Bank of Japan. Countries heavily dependant on foreign capital and exporting struggled. Russia's currency collapsed as the currency devaluation got out of control.

Commodity prices fell to all time lows and oil touched \$12.00 a barrel. The Federal Reserve decided to stop raising interest rates which saw markets boom and brought in the tech boom.

The similarities are nearly identical. China aggressively devalued their currency twice in a short period of time last year. Economies heavily dependant of foreign capital and exports are all struggling. Commodity prices have fallen to record lows along with oil and energy.

Investors are also concentrated in the tech side again with a preferred stock grouping known as the FANG (Facebook, Amazon, Netflix's and Google). All to familiar except back in the day it was



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Apple, Microsoft, Yahoo, Amazon, AOL. It is important to note, that as in the past, investors are looking to tech and innovation investments as they believe that these companies can exceed the normal range of price earning and go well beyond. However, as in the past most will jump in blindly. Most of the darlings of the first tech boom are non existent today. Just like the automotive boom of the early 1900. There even was a taxi service corporation that traded publicly that promised to revolutionize the way people travel making trains obsolete and the needed to buy a car unnecessary. It was forward thinking for its time but eventually went bankrupt.

When looking at tech companies do not just seek innovation or disruption look for entries that can apply lateral knowledge.

How does this play out? The American Federal Reserve will act favourably supporting the American economy while emerging economies recover from their malaise. As price earning ratios reach their peak investors will turn to stocks that trade at higher multiples such as disruptive innovation and corporations that deploy such strategies. The American economy will strengthen and Europe will lag behind. The main driver of economic growth will be forged in both fiscal and monetary policy not sheer corporate horse power. Government policy will open the door to allow corporations to see North America and secondly Europe as the favoured destination for investment capital to flow into.

Client portfolio models are squarely positioned to take advantage on many fronts such as geographical allocation, sector location and investable cash. Our client models are meant to be fully tactical focused on absolute returns.

On the economic front, producer price inflation report released this week shows a lack of inflationary pressure a condition that would favour continued monetary policy accommodation. Notwithstanding a weak headline number, retail sales growth has been fairly positive, with much of the weakness centred on autos. The American Labor Department reported that import prices rose 0.2 percent month over month in March following a 0.4 percent drop in February. Economists had expected a steeper 1 percent increase. The increase was driven by a 4.9 percent jump in fuel prices. Excluding fuel, import prices edged down 0.1 percent. Meanwhile,

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the report also stated export prices were unchanged, the first time prices did not decline since May 2015. The export price performance was in line with expectations and followed a 0.5 percent decrease in February.

The Commerce Department reported that retail sales edged down 0.3 percent month over month in March, belying the 0.1 percent increase expected by economists. The previous month's sales were upwardly revised to show an unchanged reading compared to the initially estimated 0.1 percent drop. Excluding autos, sales rose 0.2 percent compared to the 0.4 percent increase forecast by economists. Auto sales plunged 2.1 percent compared to an unchanged reading in February. Electronic store sales and building material & garden equipment store sales rose at a similar pace of 0.1 percent and 1.4 percent, respectively.

Gasoline station and home furnishing store sales rebounded. On the other hand, non-store retailers and food services & drinking places saw weakness.

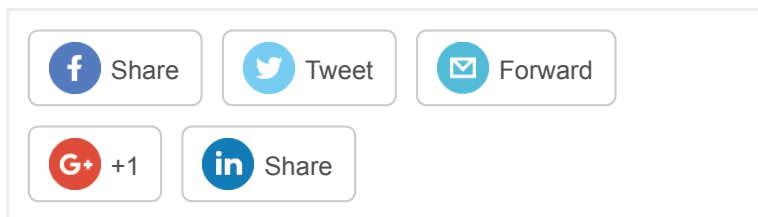
Crude oil stockpiles fell by 4.9 million barrels to 529.90 million barrels in the week ended April 2nd. Nonetheless, stockpiles were at historically high levels for this time of the year. Meanwhile, distillate inventories rose by 1.8 million barrels and were above the upper limit of the average range for this time of the year. Gasoline inventories also increased, rising by 1.4 million barrels, and were well above the upper limit of the average range.

Data released by French statistical office INSEE showed that its consumer price index edged down 0.1 percent year-over-year in March, declining for the second straight month. EuroStat reported that industrial production in the Euro zone fell by 0.8 percent month over month in February, with non-durable goods and energy production showing marked weakness. However, annually, industrial output rose 0.8 percent. Economists expected a 0.7 percent monthly drop but a 1.3 percent year-over-year increase. The old continent is not picking up steam like expected but still moving forward. Another round of monetary stimulus may be necessary.

A report released by the Chinese Customs Office showed that

exports rose 11.5 percent year over year in March, ahead of the 10 percent increase forecast by economists, compared to a 25.4 percent drop in February. Imports fell 7.6 percent, slower than the 10.1 percent decline forecast and the 13.8 percent decline in February. Consequently, the trade surplus came in smaller than expected at \$29.9 billion. In yuan-terms, export jumped 18.7 percent compared to a 1.7 percent drop in imports. After February's fall, exporters are pulling all stops to get back on track. Both manufactures and exporters are dropping prices to stimulate exports beyond the already devalued Yuan. I would expect to see more fire selling of Chinese goods till manufactures have reduced excess capacity. China's excess capacity will drag the dragon economy into a deep recession, if excess capacity is not removed rapidly. This would mean massive downsizing, lay offs and debt restructuring. Watch for many corporations to fold in the short term as China's corporate landscape reshapes itself.

The Bank of Canada's near term issue will be managing our Loonie as our nation becomes a choice destination of foreign capital. It appears that all the fear around Canada's future debt levels does not faze investors. Stability and opportunity right now define Canada economically. The hold steady approach to interest rates will keep our Loonie higher. However, Stephen Polz, governor of the Bank of Canada was careful not to add to much excitement about economic prosperity as this would push our dollar above the 80 cent mark. Investors will take the lack of change in interest rates as good news about the Canadian economic landscape as few places in the world can claim currently.



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