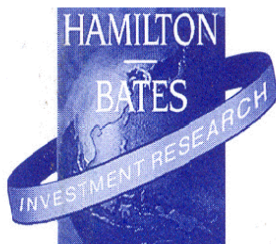
July 8, 1951 - Paris celebrates its 2000th birthday. The history of Paris can actually be traced back to a Gallic tribe known as the Parisii, who in 250 B.C. settled an island in the Seine River, which runs through present-day Paris. By 52 B.C., Julius Caesar and the Romans had taken over the area, marking its official founding as a settlement.



Hamilton-Bates Market Update

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Add China and a Technical Glitch to the Mix
Greece is still unsettled but they seem to desire a deal, but a steep slide in Chinese stocks has entered the news cycle, as one of the top-three world markets loses 30% in less than three weeks. Adding to the uncertainty there was a technical glitch that halted NYSE trading for 4 hours during the middle of the day. It was due to a software upgrade rather than a security breach or cyber attack, but the halt dented any thoughts of buying on the dip that investors had for the day. The major averages are now at key levels that could determine whether the bull market remains intact (or not).

Earnings, Economics, and Interest Rates
The next few weeks are earnings season, and a good dose of earnings could be the trigger for a market rebound. The market needs a good earnings season. The only 'good' news from the Greece and China troubles for the market is that the Fed is likely on hold for any rate hikes. We do not expect a hike in 2015.

Greek Tragedy
For years Greece has been kicking the can down the road, attempting to fix a debt problem with more debt (sound familiar?). But unlike the US, Greece can't print its own currency the Euro, and has reached its debt limit. The Europeans led by Germany are reluctant to restructure (write off) Greek debt, as this would require the funds to be raised through taxes in Germany and elsewhere, and taxing citizens at home to bail out 'the lazy Greeks' is a political bomb. But neither does Europe want Greece to leave, and apparently Greece doesn't want to go either.

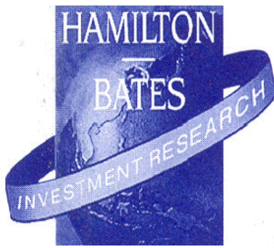
According to an article in the Telegraph, the Greek referendum was held in anticipation that Greece's controlling Syriza government would lose. Greek Prime Minister Alexis Tsipras called a referendum on the latest bailout terms offered to Greece, campaigned that the Greek voters should vote "no" and reject these measures, and expected the vote would still be a "yes." Instead the vote was an overwhelming "no," with 61% of the votes going that way, and Syriza seeming to have won a huge victory. The problem was Tsipras wanted and expected to lose the referendum. In a crazy case of game-theory gone mad, he thought he would lose the referendum and be able to be held blameless for caving into accepting the European Aid Demands without sacrificing 'face' since it was "the will of the people". Instead he got what he said he wanted by really didn't, and no preparations were made, such as going back to the Drachma even if temporarily. A result banks are closed all week and are running out of currency. The economy is falling apart.

Not knowing what to do, the Prime Minister had his abrasive Finance Minister Varoufakis resign in the middle of the night Sunday, an attempt at an olive branch to Europe. Tsipras went to Brussels for an emergency meeting on Tuesday, and due to lack of planning, didn't have an updated bailout proposal. The Greek banks will run out of cash before the weekend. The ECB has maintained its liquidity freeze, and through its inaction is strangling the economy.

What Greece Means for the Economy and Market
Greece doesn't really mean a lot to the US or even European economy, being less than 0.3% of World GDP and 3% of European GDP. The risks of contagion to the US economy and financial system are small, as the direct links between the US and Greece are obviously tiny. European banks have largely off-loaded their exposure to Greece, so the real risk is and has been psychological. As soon as the situation is decided one way or the other, in or out of the Euro zone, the markets should be able to quickly adjust and move on.

In our opinion the real and greater risk to the world economy and financial markets comes from what is going on a little further east.

Chinese Market Meltdown
The last week has really seen attention ramp up on what had been a very un-noticed decline. The heart of the matter in China is/was too much leverage by individual investors who were able to lever 4-10 times or more. All fine as the market shoots higher, but brutally painful on the way down. This week has been



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the true pain phase of the decline, which means we should be nearing a bounce. It is estimated that some 35% of margin loans have been called in over the past three weeks. To put this in perspective, the largest monthly change in NYSE margin since 1960 was -22.2% in October 2008, with October 1987 second at -13.4%. So much of the mandated selling has been done, but the psychological damage might linger. Chinese investors before now thought the government was omnipotent, now they are not so sure. The 2014 lows and next support are just 4-5% away, so we could see a near-term bounce soon.

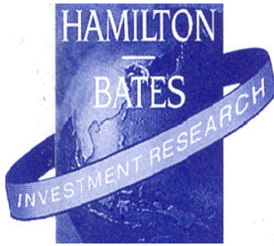
The Chinese government is certainly trying to engineer one. Policy responses to the sell-off continue to be rolled out, with this morning seeing a 6-month ban on insider share sales on top of a ban on new issues and pledges of sale bans from funds and banks. There have also been share halts in some 50% of the stocks on the Chinese Shanghai index. This is a negative as it prevents or rather protracts the needed purge. Sales will occur, its just a matter of when. Because share sales have been banned China has been prices of commodities crash as cash is raised from whatever can be sold. There are also signs of spillover to the economy, as car sales have been slowing as investors hold-off on purchases due to the slide in stocks. The sell-off has pushed Chinese blue-chips into deep value territory. The HSCEI index now sports a P/E just above 8 and a Price/Book at 1.13. That is the area of secular bear market lows.

What China Means to our Economy and Market
A 30% drop in a significant global market has negative effects felt around the world. In the short-term those effects are psychological and have a chance to carry over to other markets. Financially, there is some spillover as Chinese holdings in other markets are sold and brought home. This is limited to Hong Kong residents as most Chinese investors cannot invest abroad. The larger risk of the stock market decline in China would be economic, if the decline dampened the Chinese economy. The Chinese economy has become very important for the auto and technology sectors to name just a few. Many chip stocks get more than 50% of their revenue from China, and China is responsible for most of Apple's recent revenue growth. The Chinese market is due for a bounce at least, but we will be watching the spillover effects to the Chinese economy, which we deem to be the most important potential fallout from the Chinese market drop.

CHINESE MARKET SWOON—Chinese stocks had been trading like the NASDAQ in 1999. But too much leverage finally took its toll, and the drop has been brutal—30% in three weeks. Over $3 Trillion in investor assets have been lost, sending reverberations throughout the globe.

Market and Investment Outlook
Our market has fallen in response to events in Greece and China, taking the major averages down to key levels that must hold for the bull market to continue. For more on key technical levels see the chart section on the next page.

We remain invested with a focus on stocks over bonds, but cash has built up largely from the sale of some corporate bonds this week. Cash and bond holdings now range from 30-55% in our managed portfolios, and have helped to somewhat offset recent weakness. Despite the sell-off and the negative headlines, there is still the good possibility for a strong rally in July and August. The next week or so is where the 'rubber meets the road' for the bulls, and the market needs to see stocks begin to build positive momentum. Structurally the bull trend remains intact, but only just barely. Ideally the market will bottom this week and push higher.



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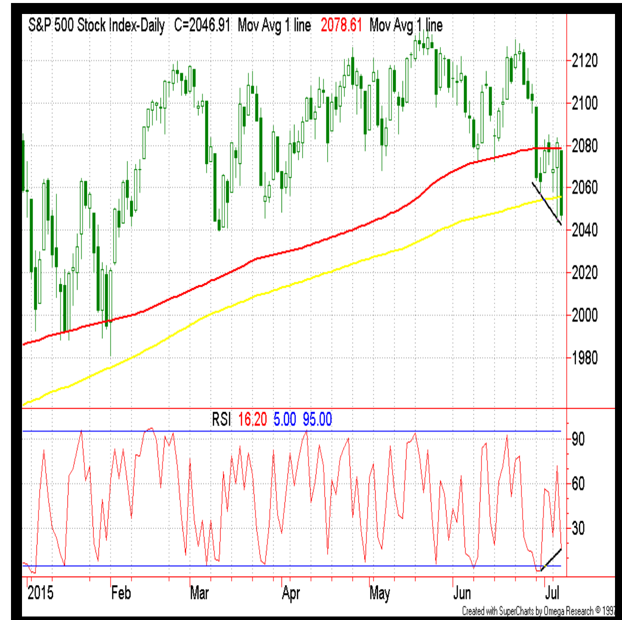
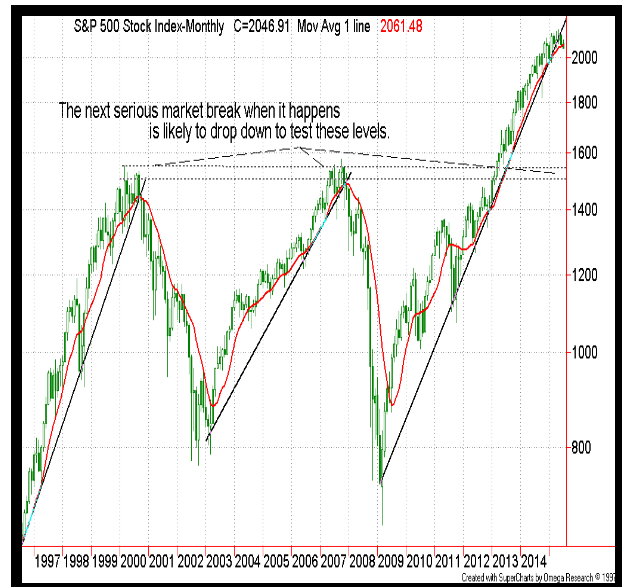
S&P 500 Charts—Key Point in Time for the Bulls

Near-Term S&P 500 Outlook (Top Chart @ Right)
The weight of the Greek fiasco and Chinese market meltdown have taken our market down a key level, its 200-day average (yellow line). We have seen two successful bounces from that key level in the last 8 trading sessions, but the latest decline means we now need a third. Will the third time be the charm? Today's break back below the 200-day average (yellow line) is a clear negative, and reverses yesterdays reversal higher. A reversal of a reversal is normally a strong signal and in this case it's a negative one. The market needs to reverse the downside quickly or the larger trend is at risk. One positive is that downside momentum has diminished (bottom panel of top chart), suggesting there is the chance for a market rebound. **A move above 2060 on the S&P would give near-term momentum to the bulls, and a move above 2080 would suggest the low has been seen for the pull-back and allow for a July-Aug rally.**



S&P 500 Long-Term (Lower Chart @ Right)
The bull market is teetering on the precipice, and the bulls need to recapture the 2060 level on the S&P immediately to halt the damage of the recent pullback. After six years the long-term trend is very over-extended, and the S&P 500 is threatening to drop below both the long-term trend line (bold black line) and its 10-month average (red line), something it hasn't done since the prior tops in 2007 and 2000.

A move below the 2050-2060 range is threatening to turn the trend from bullish to bearish. Investors should pay close attention now that we are below that level. Should July finish the month below 2060 on the S&P 500, it would be a technical 'sell' signal. Our models could already be defensive by that time.



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