## Market Elements

<table>
<thead>
<tr>
<th>Date</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 27, 2013</td>
<td>NEW Market Elements</td>
<td>2</td>
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## Relative Strength Filter

<table>
<thead>
<tr>
<th>Date</th>
<th>Title</th>
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<tbody>
<tr>
<td>August 28, 2013</td>
<td>NEW BMO Macro</td>
<td>9</td>
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<tr>
<td>August 27, 2013</td>
<td>BMO CDS</td>
<td>10</td>
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<tr>
<td>August 26, 2013</td>
<td>In USD</td>
<td>11</td>
</tr>
<tr>
<td>August 23, 2013</td>
<td>Gold Shares, Up a Notch</td>
<td>12</td>
</tr>
<tr>
<td>August 22, 2013</td>
<td>Focus on the Short End of the Curve</td>
<td>13</td>
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<tr>
<td>August 21, 2013</td>
<td>EM Credit – Hotel California</td>
<td>14</td>
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<tr>
<td>August 20, 2013</td>
<td>High Credit Risk Shorts</td>
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</tr>
<tr>
<td>August 19, 2013</td>
<td>Utility Pressure</td>
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<td>August 16, 2013</td>
<td>Best of Gold</td>
<td>17</td>
</tr>
<tr>
<td>August 15, 2013</td>
<td>It's All About Rates</td>
<td>18</td>
</tr>
<tr>
<td>August 14, 2013</td>
<td>Silver Mining</td>
<td>19</td>
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<tr>
<td>August 13, 2013</td>
<td>Weakest of the 500 &amp; Strongest of Europe</td>
<td>20</td>
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<tr>
<td>August 12, 2013</td>
<td>CDN Right Stocks, Right Groups</td>
<td>21</td>
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<tr>
<td>August 9, 2013</td>
<td>World ex USA</td>
<td>22</td>
</tr>
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<td>August 8, 2013</td>
<td>European Bank Thaw</td>
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<td>August 7, 2013</td>
<td>Price Breakdowns = Interest Rate Sensitivity</td>
<td>24</td>
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<td>August 6, 2013</td>
<td>European Vacation</td>
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<td>August 2, 2013</td>
<td>The Worst of Emerging Markets</td>
<td>26</td>
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<td>August 1, 2013</td>
<td>Europe via Telecom</td>
<td>27</td>
</tr>
<tr>
<td>July 31, 2013</td>
<td>Best of the NASDAQ</td>
<td>28</td>
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<td>July 30, 2013</td>
<td>OEX- Mobility of Mobility</td>
<td>29</td>
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<tr>
<td>July 29, 2013</td>
<td>Out of Japan Into Europe</td>
<td>30</td>
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<td>July 26, 2013</td>
<td>Airlines as an Economic Statement</td>
<td>31</td>
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<td>July 25, 2013</td>
<td>Coming Off the Rails</td>
<td>32</td>
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## Focal Points

<table>
<thead>
<tr>
<th>Date</th>
<th>Title</th>
<th>Page</th>
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<tbody>
<tr>
<td>June 24, 2013</td>
<td>Tighten Up</td>
<td>33</td>
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<tr>
<td>June 20, 2013</td>
<td>Misplaced FED Optimism &amp; Market Risk</td>
<td>39</td>
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<td>September 12, 2012</td>
<td>Inflation Expectations Are Trending Higher</td>
<td>40</td>
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<td>June 22, 2012</td>
<td>Focus Shifts (Back) to Asia</td>
<td>41</td>
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<td>May 16, 2012</td>
<td>Major Double Top for Global Real Estate</td>
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This report was prepared by an analyst(s) employed by BMO Nesbitt Burns Inc., and who is (are) not registered as a research analyst(s) under FINRA rules. For disclosure statements, including the Analyst's Certification, please refer to pages 43 to 44.
**Market Elements**

- Financials led stocks to large losses amid rising Syria tensions. U.S. and European banks dropped 3%. The MSCI World index broke below its 50dma. S&P 500 ended at a 7w low. The VIX spiked 12% to a 7w high.
- Safe-haven 10yr yields fell 2–12bps. Odds of a Dec. 14 Fed hike fell below 50%.
- Major crosses ended mixed vs. the U.S. dollar. The yen advanced to Y97. Asian currencies dragged the MSCI EM currency index to a new 13m closing low. EM volatility jumped to a 2m high.

**Levels**

<table>
<thead>
<tr>
<th>Currencies (USD per)</th>
<th>Commodities</th>
<th>Government 10- Yr Benchmark</th>
<th>Equity Indices &amp; Sentiment</th>
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</thead>
<tbody>
<tr>
<td><strong>Symbol</strong></td>
<td><strong>H/L</strong></td>
<td><strong>Level %Chg</strong></td>
<td><strong>Symbol</strong></td>
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<tr>
<td>JPY</td>
<td>81.15</td>
<td>-0.3%</td>
<td>DJ UBS</td>
</tr>
<tr>
<td>EUR</td>
<td>1.3388</td>
<td>0.1%</td>
<td>WTI Oil</td>
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<tr>
<td>CHF</td>
<td>1.0893</td>
<td>0.6%</td>
<td>NMX Gas</td>
</tr>
<tr>
<td>GBP</td>
<td>1.5541</td>
<td>-0.2%</td>
<td>Gold</td>
</tr>
<tr>
<td>CAD</td>
<td>0.9542</td>
<td>0.2%</td>
<td>Silver</td>
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<tr>
<td>AUD</td>
<td>0.8988</td>
<td>-0.5%</td>
<td>Palladium</td>
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<tr>
<td>NZD</td>
<td>0.7798</td>
<td>-0.7%</td>
<td>LME Cu</td>
</tr>
<tr>
<td>BRL</td>
<td>0.4216</td>
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<td>LME Al 3m</td>
</tr>
<tr>
<td>MXNx10</td>
<td>0.7568</td>
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<td>LME Ni 3m</td>
</tr>
<tr>
<td>ZAR</td>
<td>0.0963</td>
<td>-0.6%</td>
<td>LME Zn 3m</td>
</tr>
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<td>KRWx10</td>
<td>0.8949</td>
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<tr>
<td>SGD</td>
<td>0.7798</td>
<td>-0.1%</td>
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**Moves**

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<th>Equity Indices</th>
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<tbody>
<tr>
<td><strong>Symbol</strong></td>
<td><strong>%Chg</strong></td>
<td><strong>Symbol</strong></td>
<td><strong>%Chg</strong></td>
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<td>2.8%</td>
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<tr>
<td>GBP</td>
<td>0.07</td>
<td>NMX Gas</td>
<td>0.9%</td>
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<tr>
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<td>0.20</td>
<td>Gold</td>
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<tr>
<td>AUD</td>
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<td>0.8%</td>
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<tr>
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<td>Palladium</td>
<td>-0.6%</td>
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<tr>
<td>BRL</td>
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<td>LME Cu</td>
<td>0.1%</td>
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<tr>
<td>MXNx10</td>
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<td>LME Al 3m</td>
<td>-0.3%</td>
</tr>
<tr>
<td>ZAR</td>
<td>0.07</td>
<td>LME Ni 3m</td>
<td>-0.7%</td>
</tr>
<tr>
<td>KRWx10</td>
<td>0.20</td>
<td>LME Zn 3m</td>
<td>-0.2%</td>
</tr>
<tr>
<td>SGD</td>
<td>0.07</td>
<td>Lumber</td>
<td>-1.3%</td>
</tr>
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**Sectors**

- Financials led stocks to large losses amid rising Syria tensions. U.S. and European banks dropped 3%. The MSCI World index broke below its 50dma. S&P 500 ended at a 7w low. The VIX spiked 12% to a 7w high.
- Major crosses ended mixed vs. the U.S. dollar. The yen advanced to Y97. Asian currencies dragged the MSCI EM currency index to a new 13m closing low. EM volatility jumped to a 2m high.
- Brent and WTI oil soared 2.8% to end at a 6m and 18m high, respectively. Gold and silver rose for a fourth straight session.

**Source for all data and graphics in this publication: BMO Capital Markets, Bloomberg, Thomson**

*H/L = at a new closing 52- wk High/Low; */# = within 10% of the 52- week High/Low. Colour codes are inverted for bond and sentiment indications.*
Daily Charts
3-Month View with 26-Day Bollinger Bands and 150-, 200- and 50-Day Moving Averages
Intra Day Charts
2-Day 1-Minute View

Currencies
- U.S. Dollar Index
- Yen
- Euro
- Asia Dollar Index
- Canadian Dollar
- Australian Dollar

Commodities
- DJ-JBS Commodity Price Index
- Gold (Spot)
- Crude Oil (WTI)
- Natural Gas (NMX)
- Copper (CMX)
- Nickel (LME 3Mo)

Bonds
- U.S. 10-Yr Bond
- U.S. 5Yr 5Yr Forward Breakeven
- Japanese 10-Yr Bond
- Canadian 10-Yr Bond
- German 10-Yr Bund
- Italian 10-Yr Bond

Equities
- MSCI World Index
- S&P 500
- S&P/TSX Composite
- CDX North American Inv. Grade Index
- VIX
- DOOM: 1M Yen IV (AUD, EUR, USD)
Daily Sector Charts

3-Month View with 26-Day Bollinger Bands and 150-, 200- and 50-Day Moving Averages

- **Canada** – at a 52-week low: **Utilities**.

**S&P 500**

**S&P/TSX Composite**

**S&P Europe 350**
### Market Movers – Largest Daily Percentage Moves

#### Energy
- **Petroleo Ltd**: PFE LN, +8.5%
- **BG Group PLC**: BG/LN, +2.4%
- **Cairn Energy PLC**: CNL LN, +1.9%
- **Tenaris SA**: TEN M, -2.3%
- **Empresas CPCEA SA**: COPEC CC, -2.8%
- **Petróleo Brasileiro SA**: PBR/A LN, -3.3%

#### Materials
- **Randgold Resources Ltd**: RRS LN, +4.1%
- **Arahi Kasei Corp**: 3407 JT, +2.1%
- **Mitsubishi Materials Corp**: 5711 JT, +1.8%
- **Empresas CPCEA SA**: CMPC CC, -3.6%
- **CRH PLC**: CRH D, -4.4%
- **Cia de Minas Buenaventura SAA**: BVN LN, -6.6%

#### Industrials
- **Bunzl PLC**: BNZL LN, +1.6%
- **Nidec Corp**: 6594 JT, +1.3%
- **Samsung C&T Corp**: 005830 KP, +1.1%
- **International Consolidated Air**: IG LN, -4.6%
- **Jardine Matheson Holdings Ltd**: JMP SP, -5.2%
- **Vestas Wind Systems A/S**: VWS DC, -7.9%

#### Cons Disc
- **Sands China Ltd**: 1928 HK, +3.3%
- **Sony Corp**: 6758 JT, +2.8%
- **Panasonic Corp**: 6752 JT, +2.1%
- **GNK LN**: GKN LN, -4.2%
- **Renault SA**: RNO FP, -4.7%
- **Daimler AG**: DAI GY, -4.8%

#### Cons Stap
- **Want Want China Holdings Ltd**: 151 HK, +9.6%
- **MWM Morrison Supermarkets PLC**: MW LN, +1.4%
- **Shiredo Co Ltd**: 4911 JT, -1.3%
- **Distribuidora Internacional de**: DI SQ, -3.5%
- **Casino Guichard Perrachon SA**: CO FP, -3.7%
- **Carrefour SA**: CA FP, -4.9%

#### Health Care
- **Takeda Pharmaceutical Co Ltd**: 4502 JT, +1.0%
- **Taisho Pharmaceutical Holdings**: 4581 JT, +0.6%
- **CSL Ltd**: CSL AT, +0.6%
- **UCB SA**: UCB BB, -2.9%
- **Esisal Internacional SA**: EI FP, -3.0%
- **Lonza Group AG**: LONN VX, -3.0%

#### Financials
- **Land Lease Group**: LLC AT, +2.5%
- **Commonwealth Bank of Australia**: CBA AT, +1.2%
- **Dexus Property Group**: DXS AT, +1.0%
- **Banco Espirito Santo**: BSE PS, +4.1%
- **Banco de Sabadell SA**: SAB SQ, -6.4%
- **Banca Popolare Equatoriale**: POP SQ, -7.7%

#### Technology
- **Rich Co Ltd**: 7752 JT, +2.0%
- **Konica Minolta Inc**: 9002 JT, +1.8%
- **Nintendo Co Ltd**: 7974 JT, +1.1%
- **Cap Gemini SA**: CAP FP, -3.2%
- **Nokia OYJ**: NOKY FH, -3.3%
- **AcaliLucent/France**: ALU FP, -5.7%

#### Telecom
- **NTT DOCOMO Inc**: 9437 JT, +1.6%
- **Chunghwa Telecom Co Ltd**: 2412 TT, +0.3%
- **China Mobile Ltd**: 941 HK, 0.0%
- **Orange SA**: ORA FP, -2.7%
- **Portuguese Telekom SGPS SA**: PTC PL, -3.0%
- **Vivendi SA**: VIV FP, -3.3%

#### Utilities
- **Tokyo Electric Power Co Inc**: 5901 JT, +12.3%
- **Kyushu Electric Power Co Inc**: 9508 JT, +2.0%
- **Chubu Electric Power Co Inc**: 9502 JT, +1.2%
- **Enel SpA**: ENEL M, -3.4%
- **Acciona SA**: ANA SQ, -3.9%

#### S&P/TSX Composite

#### S&P 500

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**Bold** = move of more than 5%
## U.S. Market Movers

**Energy**
- Symbol: ESV
  - Last: 56.77
  - %Chg: -0.7%
- Symbol: NTV
  - Last: 99.21
  - %Chg: -1.1%
- Symbol: DO
  - Last: 65.00
  - %Chg: -0.8%
- Symbol: NBR
  - Last: 15.38
  - %Chg: -2.8%
- Symbol: HP
  - Last: 63.22
  - %Chg: -1.2%
- Symbol: RDC
  - Last: 30.00
  - %Chg: -0.7%

**Industrials**
- Symbol: PTEN
  - Last: 19.62
  - %Chg: -2.0%
- Symbol: UNT
  - Last: 46.03
  - %Chg: -0.8%
- Symbol: ATW
  - Last: 56.52
  - %Chg: -1.7%
- Symbol: PES
  - Last: 6.95
  - %Chg: -3.7%
- Symbol: SLB
  - Last: 81.17
  - %Chg: -1.8%
- Symbol: HAL
  - Last: 41.83
  - %Chg: -0.6%

**Consumer Discretionary**
- Symbol: JCI
  - Last: 40.11
  - %Chg: -3.7%
- Symbol: GM
  - Last: 33.69
  - %Chg: -3.5%
- Symbol: HOG
  - Last: 18.58
  - %Chg: -3.2%
- Symbol: MHD
  - Last: 120.15
  - %Chg: -3.3%
- Symbol: PHM
  - Last: 15.59
  - %Chg: -3.5%

**Consumer Staples**
- Symbol: CVS
  - Last: 57.69
  - %Chg: -0.9%
- Symbol: HIG
  - Last: 47.21
  - %Chg: -3.1%
- Symbol: SYK
  - Last: 31.74
  - %Chg: -0.4%

**Technology**
- Symbol: GOOG
  - Last: 850.15
  - %Chg: -1.8%
- Symbol: EBAY
  - Last: 50.07
  - %Chg: -2.1%
- Symbol: YHO
  - Last: 27.00
  - %Chg: -2.5%

**Financials**
- Symbol: WFC
  - Last: 41.36
  - %Chg: -3.0%
- Symbol: MSFT
  - Last: 175.24
  - %Chg: -2.0%
- Symbol: CHASE
  - Last: 47.51
  - %Chg: -4.1%

**Utilities**
- Symbol: MCHP
  - Last: 38.54
  - %Chg: -0.6%

## Market Elements

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Last</th>
<th>%Chg</th>
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<tr>
<td>BAX</td>
<td>13.18</td>
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<tr>
<td>CL</td>
<td>51.30</td>
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<tr>
<td>DOW</td>
<td>25.98</td>
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<td>EMN</td>
<td>55.63</td>
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<tr>
<td>TDW</td>
<td>54.84</td>
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<tr>
<td>X</td>
<td>18.05</td>
<td>-3.4%</td>
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**Health Care**
- Symbol: DAL
  - Last: 19.11
  - %Chg: -4.7%
- Symbol: CSX
  - Last: 24.81
  - %Chg: -2.5%

**Technology**
- Symbol: GOOG
  - Last: 850.15
  - %Chg: -1.8%
- Symbol: EBAY
  - Last: 50.07
  - %Chg: -2.1%
- Symbol: YHO
  - Last: 27.00
  - %Chg: -2.5%

**Financials**
- Symbol: WFC
  - Last: 41.36
  - %Chg: -3.0%
- Symbol: MSFT
  - Last: 175.24
  - %Chg: -2.0%
- Symbol: CHASE
  - Last: 47.51
  - %Chg: -4.1%

**Utilities**
- Symbol: MCHP
  - Last: 38.54
  - %Chg: -0.6%
<table>
<thead>
<tr>
<th>Symbol</th>
<th>H/L</th>
<th>Last</th>
<th>%Chg</th>
<th>Symbol</th>
<th>H/L</th>
<th>Last</th>
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<tr>
<td>ABB</td>
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<td>ADU</td>
<td>19.90</td>
<td>1.99</td>
<td>-1.0%</td>
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<tr>
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<td>ADX</td>
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<td>-1.0%</td>
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<tr>
<td>AEO</td>
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<td>AEO</td>
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<td>AF</td>
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<td>-2.3%</td>
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<tr>
<td>AGC</td>
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We’ve gone fishing this week, and are using this time to detail some of our favourite tools and screens that we can’t jam into the link to the toolkit on the left. Today, we highlight a link to BMO Macro.

We put this together a few years ago as one-stop shopping for the trends we observe on the macro front. The risk aversion triggered by Syria tensions mostly exacerbated existing trends.

- While financials led equity markets sharply lower yesterday, counterparty risk barely budged – Figure 1.
- Amongst our currency screens: the risk-off mood sent major commodity and most Asia currencies lower – Figure 2; the Indian rupee is plunging to a fresh record low this morning. There are signs of life when gold is shown in major currencies. The buy high yield/sell low yield carry trades have just been throttled.
- Amongst our commodity screens: the DJUSS basket keeps us abreast of key trends and reversals; Brent crude oil, which bottomed in mid-April, soared yesterday. The energy sector has come off the bottom, but remains in negative territory – Figure 3.
- The trends and divergences viewed when looking at major long yields give an immediate nod to many of the trends we see in equities.
- Trends in volatility show where old (trending) and new (reversals) pressure is being applied – Figure 4. Emerging market volatility spiked to a one-year high this morning.
Relative Strength Filter

BMO CDS

TOOLKIT

- We’ve gone fishing this week, and are using this time to detail some of our favorite tools and screens that we can’t jam into the link to the toolkit on the left. Today, we highlight a link to BMO CDS.

- First and foremost, CDS trends on too-interconnected to fail banks at both the macro and granular level keep us alert to signs that something may go bump in the night.

- By looking at custom baskets, we are able to see the shift from a great credit environment, to one which is more spotty, with some CDS trends widening and other positive trends breaking – Figure 1.

- We also look at trends on the standard corporate benchmarks used to hedge and place directional bets – Figure 2.

- Our link also lets us hone in on emerging market versus developed market credit, or high risk liquid CDS as examples.

- Not getting much airtime, but we find most interesting the trends we see in sovereign CDS, like the difference between Western and Eastern Europe.

Figure 1: Custom CDS Indices

Figure 2: Corporate CDS Trends

This report was prepared in part by an analyst(s) employed by BMO Nesbitt Burns Inc., and who is (are) not registered as a research analyst(s) under FINRA rules. For disclosure statements, including the Analyst's Certification, please refer to pages 2 to 3.
We’ve gone fishing this week, and are using this time to detail some of our favourite tools and screens that we can’t jam into the link to the toolkit on the left. Today, we highlight a link to “In USD.”

It was the soaring Japanese equity market, coupled with the sinking yen, that nudged us to detail price trends of all of our stocks and ETFs in USD terms for clients who do not hedge currency. The combination of the two moves makes the currency-adjusted outperformance of Japan less of a “WOW” and more of a “well, OK” – Figure 1.

Priced in USD, the Nikkei 225 ETF has trended higher at just below half the rate of the Japanese equity market when viewed in local currency terms – Figure 2.

We can now put the MSCI US and Japanese stocks together, to properly compare a Tesla Motors to a GungHo Online Entertainment.

A momentum buy list of European stocks (largely European listed) when converted back into USD terms looks like Figure 3.
Gold Shares, Up a Notch

- Gold has been as quiet as a mouse, but gold shares went up a notch in our Group Selection report yesterday. The reading is still meager at 7th decile, but that’s at least at the low end of neutral – Figure 1.
- All but one gold share in the MSCI World index have broken above underperforming trends – Figure 2.
  - If you broaden the list out to the 99 gold stocks we cover, 70% of them have broken above underperforming trends against the ACWI.
- With interest rate concerns pulling global equities lower, we are interested in seeing which stocks are going against the grain. The group of gold stocks reaching at least a 1-month high in yesterday’s session, are mostly small cap, low priced, and also on the move – Figure 3.
- Our Aurum link shows about every gold trend we could put in one piece – see here.

### Figure 1: Gold Equity Relative Strength Decile

![Gold Equity Relative Strength Decile](image1)

### Figure 2: MSCI World Gold Stocks vs. MSCI World

![MSCI World Gold Stocks vs. MSCI World](image2)

### Figure 3: Gold Shares Reaching at Least a 1-Month High Yesterday

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Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Focus on the Short End of the Curve

- This morning, Fed fund futures point to a 51% probability of a hike in U.S. rates by the December 2014 meeting.
  - This is the first time over the 50% mark in six weeks.
  - This is more important than the quote on U.S. 10-year yields.
- With equities (our key focus) typically considered long-duration assets, why is the short end of the curve most important?
  - Because as the world becomes stressed on tightening of global markets via interest rates, the S&P 500 has moved more like the short end of the curve than the long end of the curve – Figure 1.
  - Uncertainty in the corporate bond market has been behaving more like the short end of the curve than the long end of the curve – Figure 2.
- Yesterday we noted that emerging market corporate default risk is predominantly trending higher (negative) while developed market corporate default risk is predominantly trending lower (positive). Currently, DM risk is tainted red, with a quarter of positive trends breaking down (like SPLS yesterday).
  - If short rates continue to push higher, expect to see more red, both in corporate default risk (Figures 2, 3) and equities (Figure 1).

Figure 1: S&P 500 With Long and Short Treasury ETFs

Figure 2: Corporate Bond Implied Volatility and US 2y Yield

Figure 3: 5y CDS Trends on Liquid Developed Market Securities ($9B Cut-off) – Click Here for Full List
EM Credit – Hotel California

- The emerging market equity index has not taken out the low, emerging market bonds have not taken out the low, but this morning the MSCI emerging market currency index took out the June spike low – Figure 1.
- One way to quantify the Hotel California pattern for emerging markets is to look at the rolling correlation of returns between EM bonds and treasury bonds. The two are weakly correlated in good times when rates are stable, but strongly correlated in bad times, when treasury yields are rising – Figure 2.
- When we looked at the major moves on the CDS front yesterday, they were dominated by two themes – widening and emerging markets.
- Split the liquid CDS trends that our system finds into developed markets and emerging markets, and you see a ratio of narrowing (good) : widening (bad) of 3:1 for developed markets, but almost all trends are widening in EM – Figure 3.
- Our momentum sell list of EM stocks sporting widening CDS trends includes Indosat Tbk, IDBI Bank, VTB Bank, Samsung Electronics, KT &G, and Petrobras.

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
High Credit Risk Shorts

- The credit market is feeling the same nervousness as the equity market is as interest rates back up.
  - The Markit CDX North American high yield CDS basket broke above a narrowing trend (Figure 1) yesterday, on the same day that the S&P 500 broke its uptrend (the DJIA broke its uptrend last Friday).
  - Unlike the S&P 500, which hit a higher high in August, major CDS indices failed to reach a lower (risk) low.
- We will use a number of factors to pick out a few high risk credit shorts.

- Every custom CDS index we put together widened yesterday, but Chinese banks, where the 5yr CDS is rising at over 200%/year, widened the most at 4.4%. Bank of China and other Chinese banks are fading at the top of their downtrends – Figure 2.
- The 5-year CDS trend on Louisiana-Pacific started basing at the start of the year, and really moved wider as U.S. treasuries sold off in Q2. We expect support just below $15 to break, and downside risk is closer to $10 – Figure 3. As a sub-industry, we rank Forest Products as 9th decile, down from 1st decile at the start of the year.
- As many of the most consistent credit deterioration trends are EM related, and there is no currency falling faster than the Brazilian Real, we will target AmBev, which is trending lower, as the CDS level is trending higher; albeit the CDS level implies a lower stock price – Figure 4.

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Relative Strength Filter

Utility Pressure

- With last week’s breakout for the many global bond yields (Figure 1) and the resurgence of treasury implied volatility, the relative performance of the utility sector to the global equity market was pushed to a new low – Figure 2.
  - Last week we highlighted many key themes, related to the interest rate picture; this is just one of many.
  - Near-term risk and our target for the U.S. 10-year yield is 3.25%.
- It’s interesting that our momentum sell list of utilities picks up another theme, which is a victim of higher rates: emerging markets – Figure 3.
- A more U.S.-centric list of utilities under pressure is found when one looks amongst the 46 utilities that have broken below positive price trends.

Figure 1: U.S. 10-Year Bond Yield

Figure 2: Global Utilities vs. MSCI World

Figure 3: Momentum Sell List of Utilities (USD Price Trends)

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Best of Gold

- It's a very interesting day, when the DJIA breaks an uptrend, while the resource-dominated S&P/TSX Venture Composite index breaks a downtrend – see link.
  - A key driver was gold, which broke above downtrends in CAD, AUD and USD yesterday – Figure 1.
- We also have to stand down from the statement that gold acts like a hedge against 1st decile equity performance – Figure 2. That was a very unusual nine-month phase, which appears to be over.
- We have written very sparsely on gold recently (on Wednesday, we wrote on silver), as from the perspective of a global portfolio, the breadth of gold equity relative strength has improved from horrible to merely less bad – Figure 3.
- Many portfolios can just invest in bullion, and avoid the mining risk. There are, however, a handful of gold stocks that are outperforming bullion, these are the best of gold – Figure 4.
- For those wanting to delve further into bullion, key ratios, relative performance of gold against different benchmarks, see Aurum.

Fig 1: Gold Breaking Above Downtrends in 4 of 7 Currencies

<table>
<thead>
<tr>
<th>Name</th>
<th>1-Day Chg (%)</th>
<th>5-Day Chg (%)</th>
<th>Chg Last Day</th>
<th>Reward /Risk</th>
<th>Trend Slope</th>
<th>Hi (Mo)</th>
<th>Low (Mo)</th>
<th>%Chg wrt Gold MA</th>
<th>Chg wrt 50 Day MA Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAD</td>
<td>2.0%</td>
<td>-3.6%</td>
<td></td>
<td></td>
<td></td>
<td>4.0</td>
<td></td>
<td>5%</td>
<td>Above Rising</td>
</tr>
<tr>
<td>JPY</td>
<td>1.5%</td>
<td>4.8%</td>
<td></td>
<td></td>
<td></td>
<td>-33%</td>
<td>1.0</td>
<td>4%</td>
<td>Above Falling</td>
</tr>
<tr>
<td>CHF</td>
<td>1.2%</td>
<td>4.7%</td>
<td></td>
<td></td>
<td></td>
<td>-32%</td>
<td>2.0</td>
<td>3%</td>
<td>Above Falling</td>
</tr>
<tr>
<td>EUR</td>
<td>1.6%</td>
<td>4.3%</td>
<td></td>
<td></td>
<td></td>
<td>-34%</td>
<td>2.0</td>
<td>3%</td>
<td>Above Falling</td>
</tr>
<tr>
<td>CAD</td>
<td>1.9%</td>
<td>3.8%</td>
<td></td>
<td></td>
<td></td>
<td>-33%</td>
<td>2.0</td>
<td>4%</td>
<td>Above Falling</td>
</tr>
<tr>
<td>USD</td>
<td>-2.4%</td>
<td>4.0%</td>
<td></td>
<td></td>
<td></td>
<td>-37%</td>
<td>2.0</td>
<td>5%</td>
<td>Above Falling</td>
</tr>
<tr>
<td>GBP</td>
<td>1.3%</td>
<td>3.3%</td>
<td></td>
<td></td>
<td></td>
<td>-41%</td>
<td>1.0</td>
<td>3%</td>
<td>Above Falling</td>
</tr>
</tbody>
</table>

Figure 2: Gold vs. S&P 500

Gold Finally Acting Like a Hedge, and Not a Hedge Against 1st Decile Performance

Figure 3: Gold Relative Strength Decile

Figure 4: Gold Shares in Outperforming Trends vs Bullion

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
It’s All About Rates

- When we scan the trends and the shifts we see at the micro and macro level, the root of all stems from one table, the trends we see on global long rates – Figure 1.
  - Italian and Spanish yields continue to trend lower, and spreads off of German bonds continue to narrow – Figure 2.
    - It’s no wonder the French CAC, with banks levered toward the Mediterranean, is leading Europe higher against global equity markets. This European strength is breaking the outperforming trend of U.S. equities.
  - Global safe haven yields are trending higher and are in many cases above the top ends of their channels.
    - Life and Health Insurance, formerly starved of yield, is now massively tilted toward outperformance, while Real Estate is tilted toward underperformance, and continues to break to the downside. The above links show the granularity. At the macro level, the pairing of the relative strength ratio of insurance/real estate against bond yields is shown in Figure 3.
    - First decile long positions, geared toward a healthy consumer, include Auto Parts and Internet Retail, while Regional banks enjoy the newfound steep curve, which, at 240bps, is double that of a year ago.
    - Pressed for shorts, though the vast majority of equity indices are trending higher, or are reversing downtrends? We would offer up Forest Products, Homebuilders (Figure 4), and North, and especially South, American Real Estate.

Figure 1: Trends on Major 10-Year Bond Yields

<table>
<thead>
<tr>
<th>Name</th>
<th>1-Day Chg (%)</th>
<th>5-Day Chg (%)</th>
<th>Reward /Risk</th>
<th>Trend Slope</th>
<th>Hi (Moa)</th>
<th>Low (Moa)</th>
<th>Chg wrt 50 Day MA</th>
<th>Chg wrt 50 Day MA Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>Swiss</td>
<td>-1.5%</td>
<td>-3.6%</td>
<td>-101%</td>
<td>92%</td>
<td>5 bps</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>U.K.</td>
<td>-0.2%</td>
<td>-4.8%</td>
<td></td>
<td>-37%</td>
<td>22.0</td>
<td>22.5%</td>
<td>Above Rising</td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>-2.7%</td>
<td>-4.4%</td>
<td>-17%</td>
<td>1.0</td>
<td>4.8%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Canada</td>
<td>-0.1%</td>
<td>5.1%</td>
<td></td>
<td>31%</td>
<td>24.5%</td>
<td>9.4%</td>
<td>Above Rising</td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>0.0%</td>
<td>-4.0%</td>
<td></td>
<td>7%</td>
<td>22.5%</td>
<td>8.4%</td>
<td>Above Rising</td>
<td></td>
</tr>
<tr>
<td>Portugal</td>
<td>-0.5%</td>
<td>-0.5%</td>
<td>-8%</td>
<td>-1.8%</td>
<td>Below Falling</td>
<td>Below Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Germany</td>
<td>0.0%</td>
<td>8.0%</td>
<td></td>
<td>9%</td>
<td>16.5%</td>
<td>10.7%</td>
<td>Above Rising</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>-0.3%</td>
<td>-4.2%</td>
<td></td>
<td>-3%</td>
<td>-4.5%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japan</td>
<td>1.3%</td>
<td>-0.7%</td>
<td></td>
<td>-15%</td>
<td>-7 bps</td>
<td>Below Falling</td>
<td>-4.8%</td>
<td>Below Falling</td>
</tr>
<tr>
<td>Italy</td>
<td>1.1%</td>
<td>-1.6%</td>
<td></td>
<td>-27%</td>
<td>-2.5%</td>
<td>Below Falling</td>
<td>-5.3%</td>
<td>Below Falling</td>
</tr>
<tr>
<td>Spain</td>
<td>-1.0%</td>
<td>-3.2%</td>
<td></td>
<td>-26%</td>
<td>-5.3%</td>
<td>Below Falling</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Figure 2: Italian – European AAA Spread

Figure 3: Bond Yield and Rel. Str. of Insurance/Real Estate

Figure 4: USD Price Trends on N & S American Homebuilders

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Silver Mining

- If you thought the gold shaft was deep, with bullion trending lower at rates of 20-40% per year depending on your currency of choice, silver has been shafted to the downside at a rate of over 60% per year – Figure 1.
  - It’s that differential that has helped to form the silver/gold v-bottom.

- There is probably no other segment of stocks where group-think has taken over as much as what we have seen amongst silver names. All 23 names are in downtrends, but 20 of 23 stocks have broken above downtrends – Figure 3.

- Away from group-think, and narrowing down to a favourite few for the rebound:
  - In the majors, Fresnillo and PAN American have stabilized versus the silver price.
  - In the minors, Silvercorp Metals has bottomed against its precious metals & minerals peers.

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Figure 1: Spot Silver

Figure 2: Silver/Gold Ratio

Figure 3: USD Price Trends of Silver Mining Stocks

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Weakest of the 500 & Strongest of Europe

- Yesterday the S&P 500 broke below an outperforming trend against the ACWI – Figure 1.
  - The last time it did so, it was Europe that was forming a v-bottom. This time it is Europe once again, albeit from a more solid base – Figure 2.
  - Globe trotters looking to see who is rising from the weakest of positions (short covering) are looking at China using either the China 25 or H-Share index fund.
- Given the shifting leadership, we point out the weakest of the S&P 500, and the strongest of Europe – Figures 3, 4.

Figure 1: S&P 500 ETF vs MSCI ACWI
Figure 2: S&P Europe 350 vs. MSCI ACWI
Figure 3: S&P 500 Momentum Sells
Figure 4: MSCI Europe Momentum Buys (See Here for Full List)

Source: BMO Capital Markets, Bloomberg, Thomson, Markit

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**Relative Strength Filter**

**CDN Right Stocks, Right Groups**

- The S&P/TSX composite index is **churning**, and **rising rates** have made it difficult to just clip dividend coupons while we wait our turn to be embraced as the US or European markets are.
- Lately, we have **written extensively on positive themes outside Canadian shores**, but for the money at home, we detail the 22 stocks in the Composite which are in outperforming trends against the market, and the sector, and are in top 3 sub industry deciles – the **Right Stocks in the Right Groups** – Figure 1.
- Equivalent lists for other markets are shown here: S&P 500, Russell 2000, MSCI Europe, ACWI ex US, MSCI Emerging Markets.

**Figure 1: Canadian Outperformers in Top 3 Sub Industry Deciles**

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Name</th>
<th>Sub Industry</th>
<th>Grp</th>
<th>1-day Equity Chg (%)</th>
<th>5-day Equity Chg (%)</th>
<th>MktCap (CAD)</th>
<th>Chg Last Day</th>
<th>SPTSX</th>
<th>Trend Slope</th>
<th>RS Hi (Mo)</th>
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</thead>
<tbody>
<tr>
<td>MG CN</td>
<td>Magna International Inc</td>
<td>AutoParts</td>
<td>1</td>
<td>2.7%</td>
<td>2.8%</td>
<td>19,996</td>
<td></td>
<td>92%</td>
<td>48.0</td>
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<tr>
<td>EFN CN</td>
<td>Element Financial Corp</td>
<td>SpecialFin</td>
<td>1</td>
<td>-0.2%</td>
<td>2.4%</td>
<td>1,671</td>
<td></td>
<td>103%</td>
<td></td>
<td></td>
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<td>GW0 CN</td>
<td>Great-West Lifeco Inc</td>
<td>LifeHthIns</td>
<td>1</td>
<td>-0.4%</td>
<td>0.9%</td>
<td>29,042</td>
<td></td>
<td>38%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PWF CN</td>
<td>Power Financial Corp</td>
<td>LifeHthIns</td>
<td>1</td>
<td>-0.3%</td>
<td>0.8%</td>
<td>23,372</td>
<td></td>
<td>30%</td>
<td></td>
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<tr>
<td>POW CN</td>
<td>Power Corp Of Canada</td>
<td>LifeHthIns</td>
<td>1</td>
<td>-0.3%</td>
<td>0.3%</td>
<td>12,356</td>
<td></td>
<td>26%</td>
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<td>CCL/B CN</td>
<td>CCL Industries</td>
<td>MtGlsCnt</td>
<td>2</td>
<td>-0.3%</td>
<td>1.4%</td>
<td>2,375</td>
<td></td>
<td>47%</td>
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<td></td>
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<tr>
<td>IAG CN</td>
<td>Ind. Alliance Ins &amp; Fin. Serv</td>
<td>LifeHthIns</td>
<td>1</td>
<td>-1.2%</td>
<td>-1.2%</td>
<td>4,219</td>
<td></td>
<td>55%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MFCCN</td>
<td>Manulife Financial Corp</td>
<td>LifeHthIns</td>
<td>1</td>
<td>0.1%</td>
<td>-3.7%</td>
<td>32,555</td>
<td></td>
<td>46%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>GLN CN</td>
<td>Gildan Activewear Inc</td>
<td>Aprls&amp;Gds</td>
<td>3</td>
<td>-1.2%</td>
<td>-1.5%</td>
<td>5,757</td>
<td></td>
<td>39%</td>
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<td>DH CN</td>
<td>Davis + Henderson Income Corporation</td>
<td>DataProc</td>
<td>1</td>
<td>2.4%</td>
<td>1.4%</td>
<td>1,513</td>
<td>34%</td>
<td>48.0</td>
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<td>BBD/B CN</td>
<td>Bombardier Inc</td>
<td>Aero&amp;Def</td>
<td>1</td>
<td>-1.6%</td>
<td>-2.2%</td>
<td>6,982</td>
<td></td>
<td>50%</td>
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<td>GIB/A CN</td>
<td>CGI Group Inc</td>
<td>ITConsult</td>
<td>3</td>
<td>0.3%</td>
<td>-1.2%</td>
<td>9,594</td>
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<td>54%</td>
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<td>DOL CN</td>
<td>Doliama Inc</td>
<td>GMrchStrs</td>
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<td>-0.4%</td>
<td>3.4%</td>
<td>5,695</td>
<td></td>
<td>52%</td>
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</tr>
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<td>FFH CN</td>
<td>Fairfax Financial Holdings</td>
<td>Multi-LnIns</td>
<td>1</td>
<td>0.2%</td>
<td>0.2%</td>
<td>8,491</td>
<td></td>
<td>32%</td>
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</tr>
<tr>
<td>CCA CN</td>
<td>Cogeco Cable Inc</td>
<td>Cabl&amp;Sat</td>
<td>3</td>
<td>-0.5%</td>
<td>0.7%</td>
<td>1,652</td>
<td></td>
<td>32%</td>
<td></td>
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<td>MDA CN</td>
<td>MacDonald Dettwiler &amp; Assoc.</td>
<td>Aero&amp;Def</td>
<td>1</td>
<td>-1.6%</td>
<td>0.3%</td>
<td>2,949</td>
<td></td>
<td>45%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>MRE CN</td>
<td>Martinrea International</td>
<td>AutoParts</td>
<td>1</td>
<td>3.9%</td>
<td>2.3%</td>
<td>1,063</td>
<td></td>
<td>56%</td>
<td>48.0</td>
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<td>TCLA CN</td>
<td>Transcontinental Inc</td>
<td>CmclPrt</td>
<td>2</td>
<td>0.9%</td>
<td>1.8%</td>
<td>807</td>
<td></td>
<td>38%</td>
<td></td>
<td></td>
</tr>
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<td>QUX CN</td>
<td>Qux Corp</td>
<td>MtSecHld</td>
<td>3</td>
<td>0.3%</td>
<td>5.7%</td>
<td>5,910</td>
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<td>27%</td>
<td>48.0</td>
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<td>Sun Life Financial Inc</td>
<td>LifeHthIns</td>
<td>1</td>
<td>0.2%</td>
<td>1.2%</td>
<td>20,521</td>
<td></td>
<td>32%</td>
<td>1.0</td>
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<td>CSU CN</td>
<td>Constellation Software Inc</td>
<td>ApplicSwr</td>
<td>2</td>
<td>-0.5%</td>
<td>4.7%</td>
<td>3,553</td>
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<td>37%</td>
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<td></td>
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<tr>
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<td>2,152</td>
<td></td>
<td>42%</td>
<td>48.0</td>
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</table>

Source: BMO Capital Markets, Bloomberg, Thomson, Markit  
BMO Capital Markets is Restricted on Davis & Henderson Corp.
Relative Strength Filter

World ex USA

- **U.S. dollar strength** against the majors looks less supreme with recent wide swings and the breakdown this week – Fig 1.
  - The **euro** has flattened out, **yen strength** has broken out (Anti-Abenomics), and all but the most EM levered major currency crosses have broken above their 50d MAs this week.

- We thought it a powerful message that, despite the sharp selloff in June, **MSCI World (ex U.S.) small caps** have broken out to a new high – Figure 2.
  - Half of our momentum buy list of ACWI ex U.S. members have market caps below $10B. Our **filter**, down to top 4 industry group deciles (strong stocks within strong groups), is highlighted in Fig 3.

Figure 1: US Dollar Index
Wide Swings and a Breakdown; USD Dominance is Waning

Figure 2: MSCI World ex United States Small Cap Index

Figure 3: Momentum Buy List of MSCI ACWI ex U.S. Members in Top 4 Subindustry Deciles

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Name</th>
<th>Sub Industry</th>
<th>Grp RANK</th>
<th>1-day Equity Chg (%)</th>
<th>5-day Equity Chg (%)</th>
<th>MktCap (US$)</th>
<th>Chg Last Day</th>
<th>ACWI ex US</th>
<th>Trend Slope</th>
<th>RS Hi (No)</th>
<th>RS Low (No)</th>
<th>%Chg wrt 50d MA</th>
<th>Chg wrt 50 Day MA Trend</th>
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<td>5%</td>
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</tr>
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</table>

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
European Bank Thaw

- Peripheral European bond spreads are narrowing (Spain, Italy). CDS trends on Peripheral European banks are balanced, the cost for European financials to obtain U.S. dollars in the swap market is falling, and European banks are reversing an underperforming trend against the S&P 500 – Figure 1.

- For the Eurocentric investor looking at the “severed trends” of European banks against the MSCI Europe index, you see China- and EM-leveraged HSBC breaking to the downside (but interestingly Standard Chartered is trying to pull out of its slump), but many more Eurocentric banks breaking to the upside, with many of the positive reversals occurring yesterday – Figure 2.

- As a whole, we continue to rank a global basket of diversified banks in a weak 9th decile position (most are underperforming the market and the financial sector), but when you look at the spectrum of diversified banks against the MSCI World Index, where you see the green, or stocks breaking above underperforming trends, is in the European names – Figure 3.

Globally, Banks are Tilted Towards Underperformance, But Those Breaking Above Underperforming Trends are Largely European Stocks

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Relative Strength Filter

Price Breakdowns = Interest Rate Sensitivity

- If we scan S&P 500 and S&P/TSX Composite index members in 10th decile groups for price trend breakdowns yesterday, the theme revealed is interest rate sensitivity – Figures 1, 2.
  - Most major long yields are trending higher.
    - Italy and Spain are exceptions, and spreads off German bunds are notably narrowing.
  - This is another reason to note the positive reversals in Europe.
- A 10th decile group in our Group Selection Report means that most stocks in the subindustry are either underperforming the market and the sector, or are breaking in that direction.
- Technical downside risks for some “What’s Not to Like” members:
  - PulteGroup gapped lower last month and balked at resistance. Our downside target is $10 – Figure 3.
  - Brookfield Office Properties finds support at C$13-15 – Figure 4.

Figure 1: S&P 500 Members in 10th Decile Subindustries Breaking Price Trends

Figure 2: S&P/TSX Composite Members in 10th Decile Subindustries Breaking Price Trends

Figure 3: PulteGroup Price Trend

Figure 4: Brookfield Office Properties Price Trend in C$
European Vacation

- A U.S.-centric portfolio is a strong one, yet as we pointed out last week, European shares are turning the corner, and there are pockets of strength out there that deserve attention.

- European Real Estate looks nicer – Figure 1.
  - While U.S. REITS are breaking to the downside versus global peers, most European REITS are in outperforming trends (against other REITS) – Figure 3.
  - The majority of Canadian REITS are in underperforming trends, while Aussie REITS are either underperforming, or are breaking down against a global REIT benchmark.

- European Infrastructure is basing and is turning the corner – Figure 2.
  - While North American Infrastructure is meandering relative to global markets, European shares are basing – Figure 2.
  - European momentum buys against global peers are shown in Figure 4.
  - The spectrum of European infrastructure stocks is bell shaped, but one-quarter of the shares is breaking above the top ends of their channels.

Figure 1: European REITs vs. FTSE Global REIT Index

Figure 2: Europe vs. Macquarie Global Infrastructure

Figure 3: European REIT Outperformers vs. FTSE Global REIT Index

Figure 4: European Infrastructure Momentum Buys vs. Macquarie Global Infrastructure Index

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
The Worst of Emerging Markets

- As North American rates rise, yield curves steepen and global equity markets have a tough time keeping up with U.S. benchmarks, the MSCI Emerging Markets Index trends lower - Figure 1.
  - At a more granular level, our best fit trend for 9 of 10 EM sectors sports a negative slope.
- In relative strength terms, the MSCI Emerging Markets ETF is underperforming the S&P 500 at a rate of 50%/year – Figure 2.
- Our momentum sell list (trending lower but not oversold) of EM stocks listed on a U.S. exchange is shown in Figure 3.

Figure 1: MSCI Emerging Markets Index

Figure 2: Emerging Market ETF vs. S&P 500

Figure 3: Momentum Sell List of U.S.-Listed Emerging Market Stocks

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Europe via Telecom

- The broader Europe 350 is right behind the CAC in breaking above an underperforming trend against the S&P 500 – Figure 1.
  - If you want a more targeted turnaround, we suggest the European telecom sector – Figure 2.
    - For granularity down at the stock level, what you are getting in European Telecom, brought back in USD terms is an abundance of uptrends, where most stocks are above rising 50 and 200d MAs, RSIs which are not overbought, and one-third of the stocks, which are still in downtrends are reversing these – Figure 3.
  - Heck, there is even a birth amongst royalty across the pond.

Figure 1: S&P Europe 350 vs. S&P 500

Figure 2: Stoxx 600 Telecom ETF vs S&P 500

Figure 3: USD Price Trends of European Telecom Stocks

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
The NASDAQ has pivoted back into an outperformance trend against the S&P 500 and is close to taking out the downtrend from the 2012 high – Figure 1.

- Yes, there is certainly an AAPL effect going on. Yesterday, we highlighted the positive reversal of AAPL vs. the OEX, and in yesterday’s session AAPL broke above underperforming trends against the MSCI World and S&P 500 index, but...
- … there is also a small cap effect going on. The NASDAQ small cap index has a slight but prominent outperformance against the Russell 2000 index – Figure 2.

The ratio of momentum buys/sells amongst the NASDAQ composite index members we follow is 4/1. That compares with a 2/1 ratio for the S&P 500 and 3/1 ratio for the Russell 2000. (There is a paltry 1:1 ratio for Canucks and that beats the 1:2 ratio for EM, but we digress).

The NASDAQ composite momentum buys are highlighted in Figure 3. The full list is found here.

Best of the NASDAQ

- The NASDAQ has pivoted back into an outperformance trend against the S&P 500 and is close to taking out the downtrend from the 2012 high – Figure 1.
- Yes, there is certainly an AAPL effect going on. Yesterday, we highlighted the positive reversal of AAPL vs. the OEX, and in yesterday’s session AAPL broke above underperforming trends against the MSCI World and S&P 500 index, but...
- … there is also a small cap effect going on. The NASDAQ small cap index has a slight but prominent outperformance against the Russell 2000 index – Figure 2.

The ratio of momentum buys/sells amongst the NASDAQ composite index members we follow is 4/1. That compares with a 2/1 ratio for the S&P 500 and 3/1 ratio for the Russell 2000. (There is a paltry 1:1 ratio for Canucks and that beats the 1:2 ratio for EM, but we digress).

The NASDAQ composite momentum buys are highlighted in Figure 3. The full list is found here.

**Figure 1: NASDAQ Composite vs. S&P 500**

**Figure 2: NASDAQ Small Cap Index vs. Russell 2000**

**Figure 3: NASDAQ Composite Momentum Buys (vs. S&P 500) – See LINK for Full List**

Source: BMO Capital Markets, Bloomberg, Thomson, Markit

This report was prepared in part by an analyst(s) employed by BMO Nesbitt Burns Inc., and who is (are) not registered as a research analyst(s) under FINRA rules. For disclosure statements, including the Analyst’s Certification, please refer to pages 2 to 3.
OEX- Mobility of Mobility

TOOLKIT

- Within the S&P 100 the **severed trends view** or outperformers breaking down and underperformers breaking to the upside shows one of changing mobility – Fig 1.
- Breaking to the upside is digital mobility:
  - **Apple**, which is above its 150-d MA for the first time since last October, is breaking above an underperforming trend, which itself is tamer than the steep downtrend that was originally formed from the September peak. Less bad deserves attention – Figure 2.
  - **Qualcomm** is the other key click breaking to the upside – Figure 3.
- Breaking to the downside is more old fashioned mobility:
  - We **highlighted the weakness in the Rails last week**, but, yesterday, the best outperformer, **Union Pacific**, joined in by breaking its outperforming trend – Figure 4.
  - The **Aerospace & Defense group** is much stronger in our system, but is worth pointing out that the spectacular outperforming trend in **Boeing** is just breaking to the downside – Fig 5.

Figure 1: **Severed (broken) Relative Strength Trends of S&P 100 Members vs. S&P 100**

**Outperformers** Breaking Down **Underperformers** Breaking to the Upside

**Figure 2: AAPL vs. S&P 100** (see link for Dvd Adj Price Trend) **Figure 3: Qualcomm vs. S&P 100** (see link for Dvd Adj Price Trend)

**Figure 4: Union Pacific vs. 100** (see link for Dvd Adj Price Trend) **Figure 5: Boeing vs. S&P 100** (see link for Dvd Adj Price Trend)

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Out of Japan Into Europe

- The Japanese equity market, which is the sole market in an outperforming trend against the S&P 500, is breaking to the downside for the 2nd time – Figure 1.
- Leading Europe out of an underperforming trend against the 500 is the CAC 40 (Figure 2), but not too far behind lies Germany and the wider Europe 350.

On Friday, we showed Europe economic numbers surprising to the upside more than the U.S.
- One-fifth of European shares breaking above downtrends are banks. A bit of stability enters in.
- Our “best of Europe” in terms of our momentum buy list is shown in Figure 3.

**Figure 1: MSCI Japan vs. S&P 500**

**Figure 2: CAC 40 vs. S&P 500**

**Figure 3: MSCI Europe Momentum Buys (Dividend Adjusted Price Trends) – Click Here for Full List**

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<th>Symbol</th>
<th>Name</th>
<th>Sub Industry</th>
<th>RS</th>
<th>1-day Equity Chg (%)</th>
<th>5-day Equity Chg (%)</th>
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<th>Price Trend</th>
<th>Trend Slope</th>
<th>%Chg w.r.t Std MA</th>
<th>%Chg w.r.t 50 Day MA</th>
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<td>Reinsurance</td>
<td>1</td>
<td>1.4%</td>
<td>-1.5%</td>
<td>8,057</td>
<td>=</td>
<td>42%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>54</td>
<td></td>
<td></td>
</tr>
<tr>
<td>GKN LN</td>
<td>GKN PLC</td>
<td>Autosets</td>
<td>1</td>
<td>0.8%</td>
<td>-5.2%</td>
<td>9,161</td>
<td>=</td>
<td>91%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>51</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SAA FP</td>
<td>Sailfin SA</td>
<td>Aerospace</td>
<td>1</td>
<td>0.5%</td>
<td>-0.1%</td>
<td>23,934</td>
<td>=</td>
<td>67%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>62</td>
<td></td>
<td></td>
</tr>
<tr>
<td>BY US</td>
<td>BT Group PLC</td>
<td>DataTech</td>
<td>9</td>
<td>1.2%</td>
<td>1.0%</td>
<td>41,079</td>
<td>=</td>
<td>63%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>62</td>
<td></td>
<td></td>
</tr>
<tr>
<td>TJK LN</td>
<td>Travis Perkins PLC</td>
<td>Retail</td>
<td>9</td>
<td>-0.1%</td>
<td>0.4%</td>
<td>6,410</td>
<td>=</td>
<td>91%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>67</td>
<td></td>
<td></td>
</tr>
<tr>
<td>PUB FP</td>
<td>Publicis Group</td>
<td>Advertising</td>
<td>5</td>
<td>1.5%</td>
<td>0.9%</td>
<td>10,659</td>
<td>=</td>
<td>53%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>64</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Airline as an Economic Statement

- Airlines as a group have slumped from a top decile position in Q1 to a current much weaker reading of 7th decile.
  - The credit tensions transmitted via taper talk have taken a toll, causing some weakness in the high risk stocks.
  - When you look at airline momentum buys and sells, however, you see that the group is divided along geographic lines.
    - The strength, defined by our momentum buy list, is dominated by European and U.S. carriers – Figure 1. Both are positive, and note that it is the European economic results that have surprised to the upside more than U.S. – Figure 2.
    - The weakness, defined by our momentum sell list, is predominantly China related – Figure 3.

Figure 1: Airline Momentum Buys

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Name</th>
<th>Domicile</th>
<th>USD Close 25-Jul</th>
<th>1-day Equity Chg (%)</th>
<th>5-day Equity Chg (%)</th>
<th>MktCap (US$)</th>
<th>Chg Last Day</th>
<th>USD Price Trend</th>
<th>Trend Slope</th>
<th>Hi (Mo)</th>
<th>Low (Mo)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EZJ LN</td>
<td>easyJet PLC</td>
<td>U.K.</td>
<td>21.52</td>
<td>-1.5%</td>
<td>0.6%</td>
<td>8,534</td>
<td></td>
<td></td>
<td>125%</td>
<td>48</td>
<td></td>
</tr>
<tr>
<td>RYAY US</td>
<td>Ryanair Holdings plc</td>
<td>Ireland</td>
<td>53.61</td>
<td>-0.7%</td>
<td>0.1%</td>
<td>15,261</td>
<td></td>
<td></td>
<td>96</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CPA US</td>
<td>Copa Holdings SA</td>
<td>Panama</td>
<td>138.99</td>
<td>-1.8%</td>
<td>-1.1%</td>
<td>4,645</td>
<td></td>
<td></td>
<td>96</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UAL US</td>
<td>United Continental Holdings Inc</td>
<td>U.S.</td>
<td>34.3</td>
<td>-1.9%</td>
<td>-0.6%</td>
<td>11,573</td>
<td></td>
<td></td>
<td>107%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>LCC US</td>
<td>US Airways Group</td>
<td>U.S.</td>
<td>18.83</td>
<td>1.8%</td>
<td>2.2%</td>
<td>3,616</td>
<td></td>
<td></td>
<td>95%</td>
<td>2.5</td>
<td></td>
</tr>
<tr>
<td>RJE US</td>
<td>Republic Airways Holdings Inc</td>
<td>U.S.</td>
<td>13.03</td>
<td>1.6%</td>
<td>1.5%</td>
<td>641</td>
<td></td>
<td></td>
<td>66%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>JBL US</td>
<td>JetBlue Airways Corp</td>
<td>U.S.</td>
<td>6.76</td>
<td>2.0%</td>
<td>-1.0%</td>
<td>1,907</td>
<td></td>
<td></td>
<td>44%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SKY US</td>
<td>Skywest Inc</td>
<td>U.S.</td>
<td>15.35</td>
<td>0.9%</td>
<td>-0.3%</td>
<td>797</td>
<td></td>
<td></td>
<td>53%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Coming Off the Rails

- North American Railway outperformance trends have been broken – Figure 1, 2.
- Only CP has broken its price trend so far, but most have broken below their 50d MAs and four of the six rails have 50d MAs, which are falling – Figure 3.
- CP (reported results after the close) has formed a head and shoulders top. The key support is at C$120; a break of this brings the downside target of $100 – Figure 4.
- The best rail is Union Pacific. Shares remain in an uptrend, but RSI and MACD give non-confirm readings to the recent high. The key uptrend, which we expect will be tested, comes at $150 – Figure 5.
- While investors are coming off of the rails, they continue to take to the skies with first decile Aerospace stocks.

Figure 1: U.S. Railroads vs. S&P 500
Figure 2: Canadian Railroads vs. S&P/TSX
Figure 3: North American Rail Price Trends
Figure 4: Canadian Pacific (CP CN)
Figure 5: Union Pacific (UNP US)

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Tighten Up

- In May and June, markets started a new dance called the Tighten Up.
  - 1st tighten up on the long end of the U.S. treasury curve – Figure 1.
  - 2nd tighten up the Chinese interbank lending curve – Figure 2.
  - 3rd tighten up on the short end of the U.S. treasury curve – Figure 3.

Sock it to me now
Tighten it up
Archie Bell & The Drells

- A tipping point has been reached. The central bankers’ bank (BIS) now deems that (1) there has been enough stimulus provided to the global economy, (2) more cannot be done without compounding risks that central banks have already created, and (3) easing has led to the delay of structural reforms (BIS Annual Report June 23, 2013).

- After a period of unprecedented central bank easing, and ultra low interest rate volatility, markets are adjusting to now rather rapid tightening and escalating volatility.
  - The known unknown is that when interest rates move from low and highly certain, to high and highly uncertain, that carry trades blow up. This was Long-Term Capital Management, this was Carlyle Capital Corporation, and this is the known unknown that markets are routing out now.

- Our goal over the next few pages is to detail these stresses, which we believe are still at very early stages. We expect global equity weakness to persist over the near term.

Figure 1: U.S., German, and Japanese 10-Year Bond Yields (Top) and Implied Volatility (Bottom)

Figure 2: Chinese Interbank Lending Rates

Figure 3: Odds of a 14 Fed Rate Hike From Fed Funds Futures

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
FOMC: Early Withdrawal? Really?

- There has been a change in the calculus of the FED this year. In BIS terms, “Delivering further extraordinary monetary stimulus is becoming increasingly perilous”.
  - U.S. inflation expectations just started to ease leading into the FOMC minutes release in February.
  - On February 20 we learned that the FED was concerned about its open ended QE policy.
    - This was also the start of the market's fascination with the term “tapering” which has been written about 150 times per day, on average, in the month of June (“NT Tapering” on Bloomberg).
  - Inflation expectations really started falling after Cypriot debt resolution uncertainty came to bear on March 18.
    - One month later, inflation expectations were breaking down globally.
  - While inflation expectations were falling, asset price inflation was picking up. This is obviously not the inflation that the fed targets, but it was the destination that the market was targeting for QE related flows.
  - Would outgoing Bernanke go down as the FED who stoked asset price inflation? – Figure 4.
    - On May 22 Bernanke and the FOMC told the market that QE could be stepped down as early as June.
    - On June 19 Bernanke delivered the withdrawal schedule verbally.
    - Asset price inflation is no longer a problem.
      - Asset price deflation in our clients’ portfolios is our key interest now.

Figure 4: US Inflation Expectations (10-Year Breakeven Rate) Top; FTSE Global REIT Index (TENHGU) Bottom
PBOC: Money Not in the Right Places

- While it may seem to be a stretch to jump from looking at inflation expectations at the long end of the U.S. curve, to the stresses at the ultra short end of the Chinese credit curve, it is not.
  - The combination of low U.S. interest rates, and interest rate volatility encouraged flows into emerging markets with higher-yielding assets.
  - The FOMC, whose policy underpins the world’s largest and most liquid bond market becomes the central banker to the world via the carry trade.
    - $3.9 trillion had flowed into emerging markets over the past four years.
- It is a mistake to apply market western policy thinking to policy action of the new People's Republic of China government, and the PBOC.
  - Rather than releasing stimulus in response to weak economic figures, which was the point where the Chinese sovereign CDS broke to the upside (Figure 5), China has done the opposite, has withheld stimulus, and has allowed banking stress to build – Figure 2.
  - China is getting its plumbing in order by reigning in the shadow banking system, which it needs to get under control such that it can have a handle on its financial system. During this plumbing exercise,
    - Chinese bank CDS levels are soaring – Figure 6.
    - Chinese Real Estate CDS levels are soaring – Figure 7.
- We are sure that the Minsky Moment for many shadowy players in the Chinese financial system is upon them now, but to call this the Lehman moment for China as a whole is premature. Possible, but premature – Figure 8.
  - China has breathing room to tighten up, and so it is.
  - Global growth oriented resource countries such as Canada should continue to be underweighted.

Figure 5: Chinese Sovereign CDS

Figure 6: Chinese Bank 5Yr CDS

Figure 7: Chinese Real Estate CDS

Figure 8: Chinese Sovereign CDS Levels and Curve
BIS: Borrowed Time

The tone of the BIS annual report released Sunday shows central banking thinking turning from carrot to stick:

What central bank accommodation has done during the recovery is to borrow time...But the time has not been well used

The short end of the U.S. curve is tightening up.
- The FED's assessment, disclosed last Wednesday, was to bring the time of a rate hike forward by two months.
- Fed funds futures on Friday signaled a greater than 50% probability of a FED rate hike next year – Figure 3.

Nowhere does time seem to be more borrowed than in the European periphery where bonds received a massive ECB (Draghi) induced grace period. It seems that European policy makers could use the stick to un-jam the process that calm has created.
- The Spanish sovereign CDS, like many others, has broken to the upside – Figure 9.
- A peripheral European banks CDS basket is basing and should soon mint a higher high– Figure 10.
- Italian-German and Spanish-German stress and spreads are just now starting to turn up again – Figure 11.
- The Italian bank UniCredit remains the SIFI with the most inverted curve – Figures 12, 13.

Figure 9: Spanish Sovereign CDS

Figure 10: Average Peripheral Bank CDS

Figure 11: Italian and Spanish Spreads off of German Bunds

Figure 12: UniCredit SpA 5Yr CDS
SIFI: Stresses Rising

- The cost to protect systemically important financial institutions (SIFI) is rising – Figure 13.
  - Where the trends were showing improvement in creditworthiness (green wedges), the trends have broken (red arrows).
  - Our systems’ best fit for most European SIFI CDS trends is towards widening (red wedges).
- Debt protection costs at the short end of the curve (1yr) debt is rising faster than the long end of the curve (5yr).
  - Our SIFI CDS trend list below is sorted by this ratio (CDS Curve 1/5Yr).
  - No curve is even close to being over 100% (LEH-like), but it is interesting (and unflattering) to see Asia-centric HSBC line up close to UniCredit (top two lines in Figure 13).

**Figure 13: CDS Trends on Too-Interconnected to Fail Banks**

<table>
<thead>
<tr>
<th>Name</th>
<th>1-day Equity Chg (%)</th>
<th>5-day Equity Chg (%)</th>
<th>MktCap (US$)</th>
<th>Chg Last Day</th>
<th>Trend</th>
<th>CDS</th>
<th>CDS Hi (Mo)</th>
<th>CDS Low (Mo)</th>
<th>CDS Curve 1/5Yr</th>
<th>CDS %Chg wrt 50 DMA</th>
<th>Chg wrt 50 Day MA Trend</th>
</tr>
</thead>
<tbody>
<tr>
<td>UniCredit SpA</td>
<td>-4.1%</td>
<td>-7.2%</td>
<td>27,666</td>
<td>↑</td>
<td>-13%</td>
<td>2.5</td>
<td>0.58</td>
<td>22%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>HSBC Holdings PLC</td>
<td>-0.1%</td>
<td>-3.6%</td>
<td>191,403</td>
<td>↑</td>
<td>-30%</td>
<td>7.5</td>
<td>0.51</td>
<td>32%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ING Groep NV</td>
<td>-2.1%</td>
<td>-3.1%</td>
<td>33,909</td>
<td>↑</td>
<td>-45%</td>
<td>2.0</td>
<td>0.49</td>
<td>9%</td>
<td>Above Felling</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Banco Santander SA</td>
<td>-1.2%</td>
<td>-6.9%</td>
<td>69,239</td>
<td>↑</td>
<td>-42%</td>
<td>2.5</td>
<td>0.47</td>
<td>24%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Morgan Stanley</td>
<td>-1.0%</td>
<td>-3.6%</td>
<td>48,825</td>
<td>↑</td>
<td>-60%</td>
<td>5.5</td>
<td>0.46</td>
<td>35%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Royal Bank of Scotland Group Plc</td>
<td>-5.1%</td>
<td>-10.3%</td>
<td>27,112</td>
<td>↑</td>
<td>-10%</td>
<td>9.5</td>
<td>0.46</td>
<td>43%</td>
<td>Above Rising</td>
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<td>Barclays PLC</td>
<td>-0.8%</td>
<td>-5.3%</td>
<td>56,350</td>
<td>↑</td>
<td>3%</td>
<td>7.0</td>
<td>0.44</td>
<td>22%</td>
<td>Above Rising</td>
<td></td>
<td></td>
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<tr>
<td>Goldman Sachs Group Inc</td>
<td>-0.7%</td>
<td>-5.3%</td>
<td>70,724</td>
<td>↑</td>
<td>-49%</td>
<td>6.5</td>
<td>0.42</td>
<td>39%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Credit Suisse Group</td>
<td>-1.2%</td>
<td>-5.3%</td>
<td>42,253</td>
<td>↑</td>
<td>50%</td>
<td>7.0</td>
<td>0.38</td>
<td>20%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank of America Corp</td>
<td>-1.6%</td>
<td>-2.9%</td>
<td>136,803</td>
<td>↑</td>
<td>-47%</td>
<td>6.5</td>
<td>0.36</td>
<td>28%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commerzbank AG</td>
<td>-2.3%</td>
<td>-1.8%</td>
<td>10,873</td>
<td>↑</td>
<td>35%</td>
<td>3.0</td>
<td>0.36</td>
<td>14%</td>
<td>Above Rising</td>
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<td>Credit Agricole SA</td>
<td>-2.3%</td>
<td>-6.0%</td>
<td>21,255</td>
<td>↑</td>
<td>6%</td>
<td>2.0</td>
<td>0.35</td>
<td>15%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UBS AG</td>
<td>-1.5%</td>
<td>-4.7%</td>
<td>64,921</td>
<td>↑</td>
<td>11%</td>
<td>6.5</td>
<td>0.35</td>
<td>23%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deutsche Bank AG</td>
<td>0.6%</td>
<td>-4.2%</td>
<td>44,674</td>
<td>↑</td>
<td>27%</td>
<td>2.5</td>
<td>0.35</td>
<td>19%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>BNP Paribas</td>
<td>-2.6%</td>
<td>-5.9%</td>
<td>66,362</td>
<td>↑</td>
<td>-26%</td>
<td>2.5</td>
<td>0.35</td>
<td>15%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>JPMorgan Chase &amp; Co</td>
<td>-1.0%</td>
<td>-2.2%</td>
<td>196,392</td>
<td>↑</td>
<td>-2%</td>
<td>6.5</td>
<td>0.34</td>
<td>18%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Citigroup Inc</td>
<td>-2.2%</td>
<td>-4.8%</td>
<td>142,620</td>
<td>↑</td>
<td>-55%</td>
<td>5.5</td>
<td>0.33</td>
<td>31%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Societe Generale</td>
<td>-2.1%</td>
<td>-5.6%</td>
<td>27,619</td>
<td>↑</td>
<td>-16%</td>
<td>2.0</td>
<td>0.32</td>
<td>13%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wells Fargo &amp; Co</td>
<td>2.2%</td>
<td>2.8%</td>
<td>216,940</td>
<td>↑</td>
<td>-29%</td>
<td></td>
<td>0.29</td>
<td>12%</td>
<td>Above Rising</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
US Equities: Last Dot Finally Connected, Picture Now Emerging

- The stress in the banking system is just starting to be felt in the U.S. equity market – Figure 14.
  - The breakout in the cost to protect the US Banks against default last Thursday coincided with the breakdown in the S&P 500.
- The U.S. 2-year swap spread, a gauge of counterparty risk, has just started to get in the game – Figure 15.
  - It is still incredibly low – Figure 16, but will move higher with continued stress in the banking system.
  - When stresses are high enough, one can watch this counterparty risk move with S&P futures tick for tick.
  - We have not seen this yet, but are expecting it. When we see it, we will be closer to an equity bottom.
- The known unknown is that when interest rates move from low and highly certain to high and highly uncertain that carry trades blow up.
  - This is the precursor to LTCM, to CCC, and to the known unknown of 2013.
  - When this unknown is known, we believe equities will be lining up for a bottom.
**Focal Points**

*Investment & Trading Ideas*

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**Misplaced FED Optimism & Market Risk**

- "Yes, rates have come up some. That’s in part due to more optimism, I think, about the economy. It's in part due to perceptions of the Federal Reserve.”
  Fed Chairman Ben Bernanke during yesterdays Q&A.

- Of the backup in treasury yields, and the associated destruction of “risk on” carry trades, we know that,
  - Very little of the backup in treasury yields increase came from optimism (albeit stronger-than-expected U.S. payroll data on May 3 marked the bottom for treasury yields) – Figure 1
    - Much more comes from perceptions of the FED, which includes the May 22 bomb and yesterday’s "...it would be appropriate to moderate the monthly pace of purchases later this year.....ending purchases around mid-year (next year)"
    - And more still came from yen carry trade (PRDC) related unwind pressure.

- Misplaced optimism, by the world’s central banker, on why treasury yields are rising is causing,
  - another leg up in yields and volatility – Figure 1; and
  - continued collapse of “risk on” carry trades of many descriptions – Figures 2, 3.

- Another notable Bernanke line yesterday was "...as we try to land the ship on a...you know, on a ...in a smooth....in a smooth way into the ...on to the aircraft carrier.” Communication gap? There is a scene from Apocalypse Now, when the ship drops in a harsh way into the ocean. It ends with “I love the smell of napalm in the morning”

---

**Figure 1: US Treasuries Tighten Global Markets via Higher Yields and Higher Volatility**

**Figure 2: ACWI exUS Index and Treasury Volatility**

**Figure 3: North American HY vs IG and Treasury Volatility**

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Focal Points

Investment & Trading Ideas

Inflation Expectations Are Trending Higher

- If you look at a chart of U.S. Inflation expectations, you generally see three years of noise. However, within that noise, the current “best fit” trend is higher, at rates of 12–18%, depending on whether you are looking at a simple 10-year breakeven rate or a more rigorous 5-year to 5-year forward measure – Figures 1, 2.
- This week, the downtrend on the 10-year breakeven rate was reversed – Figure 1.
- Given the fact the European stress is receding (Figure 3), and that the Fed is likely to add more QE fuel, the market is starting to embrace resources. Half of global resource relative strength downturns have been severed – Figure 4.
  - Up trending inflation expectations (Figures 1, 2) give some cover for this maneuver.
- We and markets will be watching to see if they ultimately break out of the “noise zone”; for if they do, broken resource relative strength downturns will eventually turn into uptrends.

Figure 1: U.S. 10-Year Breakeven Rate (Inflation Expectations)  Fig2: US 5Y5Y Forward Breakeven Rate (Inflation Expectations)

Figure 3: Italian – European AAA Spread

Figure 4: Global Resource Sectors vs. Their Markets

Source: BMO Capital Markets, Bloomberg
Focus Shifts (Back) to Asia

- Yesterday, the Asia dollar index suffered the worst day of the past three weeks. Its sharp decline led oil and other industrial commodities lower – Figure 1.
- The day before, it was Asian CDS that widened the most among fellow sovereigns. While we lamented how copper was not following the recent European credit improvement, it was Asia that the market was focusing on.
- China caught the Spanish flu in March, broke away thanks to a surprise rate cut on June 7, and has started to deteriorate again as of this Wednesday – Figure 2.
- Yesterday, equity markets broke to the downside in concert with the Asian currency basket. Downside risk is 5% lower for the resource heavy S&P/TSX – Figure 3.
- The U.S. equity market is also influenced by moves in the Asia Dollar Index. It has been this way for years. The influence is still not as great as that of counterparty risk (which rose for the first day in six yesterday), but it is still substantial, growing and has the potential to hit the 90s as it did last year – Figure 4.

Figure 1: Asia Dollar Index and Brent Oil – Intraday Yesterday

Figure 2: Chinese and Spanish Sovereign CDS

Figure 3: Asia Dollar Index and S&P/TSX Composite

Figure 4: Asia Dollar Index and S&P 500

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
Focal Points

Investment & Trading Ideas

Major Double Top for Global Real Estate

- Those that do not like banks (and we do not like banks) hide out in insurance.
  - Insurance just broke the uptrend from the 2011 low, like most major equity markets, including the S&P 500.
- Those that do not like insurance hide out in real estate, which has given the most consistent positive performance.
- Real estate just broke the uptrend from the 2011 low – Figure 1.
- Now there are breakdowns, and there are breakdowns.
  - The context behind this one is that money (and you know who you are) has flowed into Real Estate as a yield-oriented safe haven.
  - This has pushed global real estate back to the 2011 high, which forms a major double top. Major support is 16% below current levels, which is when the double top would seem more obvious. Double top downside risk is 33% below the current level.
- The wider context is that a bank run on Greece is a “great fear,” and the ECB is apparently cutting and running.
  - In this environment, risk assets will cut and run.
  - The breakdown shows that this attitude has just started for Global Real Estate.

Figure 1: MSCI ACWI Real Estate

Source: BMO Capital Markets, Bloomberg, Thomson, Markit
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<th>Rating Category</th>
<th>BMOCM US Universe*</th>
<th>BMOCM US IB Clients**</th>
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(S) = Speculative investment;

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