

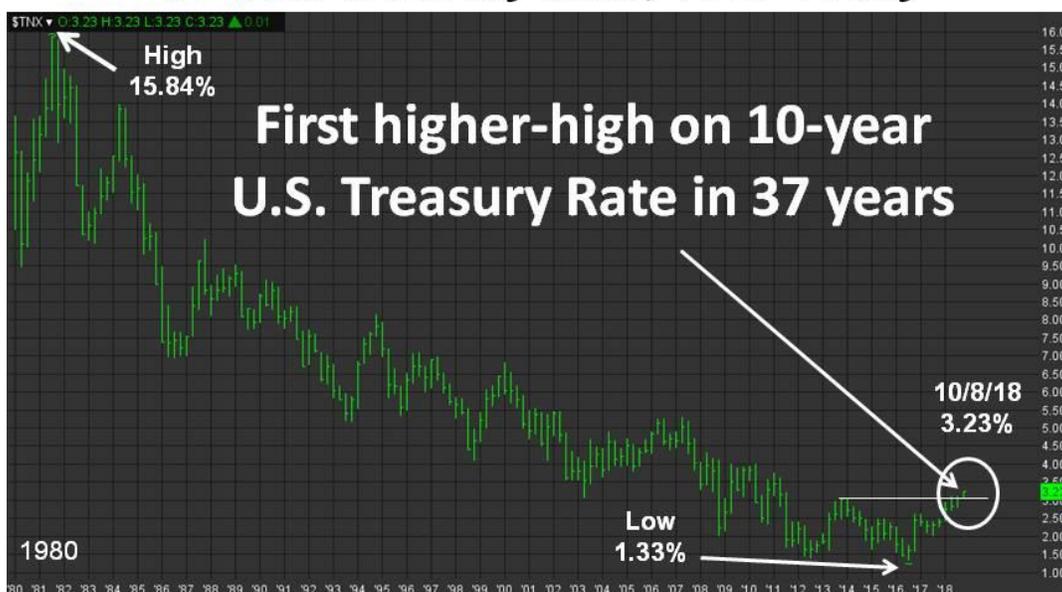
Delta Investment Management is a registered investment advisory firm headquartered in San Francisco. Delta welcomes discussions with individuals seeking investment advice and advisors seeking a new partner. Delta manages portfolios at TD Ameritrade and Schwab. Please contact Delta at info@deltaim.com or 415-249-6337 to learn more.

October 12, 2018

The Rising Rate Bull Case

The 10-year treasury rate is rising. For the first time in 37 years, it set a higher high.

10-Year Treasury Rate, 1980-Today



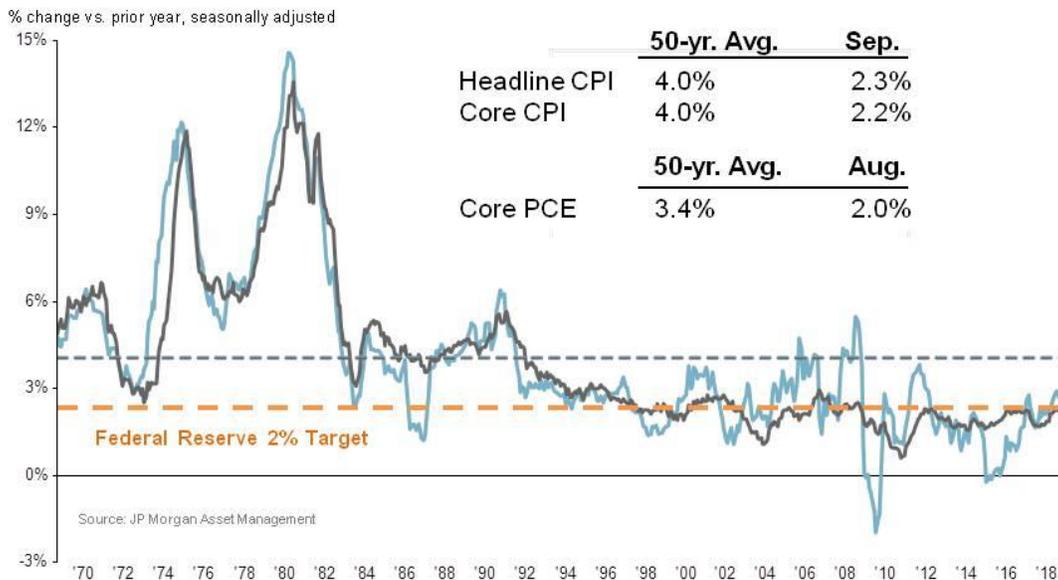
Why is the 10-year U.S. treasury rate rising? In the short-term, there could be a variety of non-fundamental reasons why the rate is rising that are difficult to identify with certainty. Short-term, non-fundamental fluctuations provide little market insight.

In the longer run, 10-year treasury rates rise because of inflation and economic growth. Spiraling inflation drove the 10-year treasury rate to almost 16% in 1981. From 1958 to 1981, interest rates trended higher. In the 1970s, the term “stagflation” was created to describe the condition of stagnate economic growth and high inflation. During the 1970s, U.S. equities showed little to no appreciation and incurred a major bear market in 1973-74.

Today, the roles of inflation and growth are reversed. Inflation has been low for the past twenty years in a range of 1.6% to 2% (measured by the PCE deflator). The core Consumer Price Index (CPI – another measure of inflation) was reported this week below expectations. Globalization, technology and demographics are major secular trends that have placed downward pressure on inflation.

The chart below shows persistently low inflation since the late 1990s - and very high levels of inflation during the 1970s.

Inflation: CPI and PCE Deflator



The rise in the 10-year interest rate, if not driven by inflation, could be the result of a positive change in economic growth expectations. US GDP growth has notched higher (from 2% to 3%) and global PMIs are expanding. If this is indeed the case, rising interest rates are not necessarily bearish for stocks.

This week, the Delta Market Sentiment Indicator (MSI) turned from Bullish to Bearish. The Delta MSI is an intermediate price signal indicator. The fundamental justification for the recent slump remains a handful of negative earnings preannouncements. In addition to rising treasury yields, the trade war with China remains a macro concern.

Earnings season began today with reports from JPMorgan Chase, Citigroup and Wells Fargo. We will look for confirmation from company managements and earnings projections over the next couple of weeks during earnings season that the recent rise in the 10-year interest rate is bullish signaling strong growth rather than rising inflation.

We currently do not see fundamental indicators suggesting that there is a rising likelihood of recession in the next six months.

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“Write about dogs!”

Delta Stock Market Dashboard

INDICATOR STATISTICS

MARKET SENTIMENT IS
BEARISH

THIS WEEK'S NUMBER IS
37.4

Our technical indicator decreased
this week from 50.8 to 37.4

Consecutive Bearish Weeks:	1
Cycle Inception Date:	5/10/2018
Range:	37.4
Mean:	37.4
Bullish Weeks YTD:	34
Bearish Weeks YTD:	7
*S&P 500	NA%
*DJIA	NA%
*NASDAQ	NA%

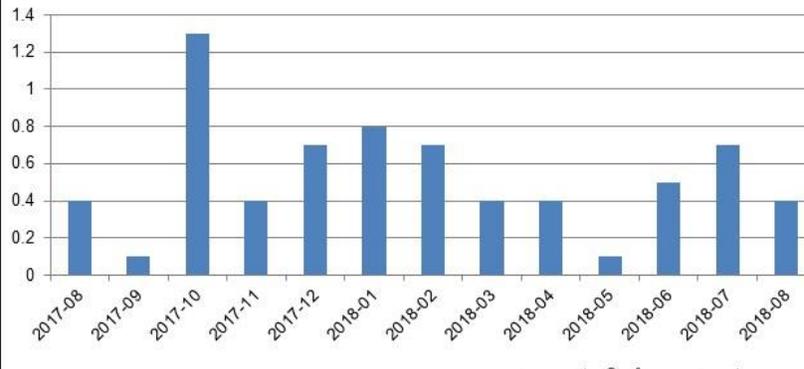
** Percentage change during current cycle*



Bear Market LEI
2006 - 2009



Leading Economic Index % Change Monthly
August 2017 – August 2018
(Updated Monthly – last update 09/20/18)



Source: The Conference Board

(Delta MSI is published in *Barron's*)

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