2016 Market Outlook

Many analysts and investors have low expectations for 2016

Bullish Case

- U.S. economy continues in expansion mode.
- Job creation continues, and the unemployment rate has dropped to 5%
- Earnings are expected to grow about 5% to 8% for 2016
- Mergers and acquisitions were at record levels in 2015. M & A is expected to be continue in 2016.
- Inflation and interest rates should remain low that helps the economy and markets
- Consumers are 70% of the economy, and they have been spending.
- Shareholder perks like share buyback programs, spinoffs and dividend increases are expected to continue in 2016.
- Central banks around the world have been pursuing stimulative efforts to help their economies.

Bearish Case

- Many of our trading partners are in or near recession.
- The Federal Reserve is expected to raise rates from 2 to 4 times. This could be disruptive to the bond and stock markets.
- Higher interest rates and U.S. growth could cause a stronger dollar.
- The strong dollar will make U.S. goods and services more expensive, less competitive to most of our international customers. Foreign currency conversions could create losses for U.S. companies.
- Low oil prices will continue to hurt oil companies' earnings and the major markets.
- Earnings estimates continue to move lower due to falling oil prices, a strong dollar, the prospect of more interest rate hikes and a slower global economy.
- Many analysts have low expectations for the markets in 2016.

- The conflicts between Russia and the Ukraine, Syria's civil war, ISIS in the Middle East, conflicts between Sunnis and Shiites remain and are unresolved.

- Our Federal Reserve has very few effective bullets to use if we have a major financial crisis, or if we go into a recession.

- Technicals are looking bad, see forecast charts below. I wrote about the economic, fundamental and technical metrics that are providing red flags.

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  The markets are the best leading economic indicators, and the stock and bond markets are providing warning signals.

- Black and grey swan events. Events that have a low probability, but if they happen they would have a big impact.

Review 2015 Forecasts

Below was my 2015 forecast for the Dow 30 and S & P 500:

2015 FORECAST					
	EARNINGS ESTIMATES	RISK,GRWTH ADJ P/E	FORECAST	CURRENT PX	PTNTL %
DJIA	1148.73	16.5	18,954.05	17,511.57	7.61%
SPX	127.28	17	2,163.76	2,019.00	6.69%

Below is a chart of the Dow 30 for 2015:

The Dow 30 high for the year was 18,350, my forecast was off by about 3.5%. By the end of 2015, my forecast was way off. As earnings fell, and the troubles in China started to get more attention, I did bring my forecasts down. Below was my 2015 September forecast:

2015 FORECAST					
	EARNINGS ESTIMATES	**RISK,GRWTH ADJ P/E**	**FORECAST**	**CURRENT PX**	**PTNTL %**
DJIA	1078	15.5	**16,709.00**	17,217.00	-3.04%
SPX	125	16.5	**2,062.50**	2,030.00	1.58%
2016 FORECAST					
	EARNINGS ESTIMATES	**RISK,GRWTH ADJ P/E**	**FORECAST**	**CURRENT PX**	**PTNTL %**
DJIA	1168.22	15.5	**18,107.41**	17,217.00	4.92%
SPX	132.53	16.5	**2,186.75**	2,030.00	7.17%

These forecasts were much closer to how the market ended.

Below is a chart for the S & P 500 for 2015:

My original forecast for the S & P was 2,163, and the index did reach 2,134; the forecast was off by 1.3%, not bad.

I did lower my forecasts as risks started to rise, and earnings estimates started to decline.

2016 Forecast

Before I provide my forecast for the Dow and S & P based on earnings, it's important that I go over the technicals, again as they are raising RED FLAGS. Below is a chart for the Dow 30:

Most major reversal tops that lead to bear markets have several characteristics in common:

1. They take time to build, on average about 14 months. This top has been building for over a year.

2. Most tops have an identifiable topping pattern. This pattern is called a rounding top, also known as an umbrella.

3. The right and left side of the formation are mirror images:

The left side has a rising top and bottom trendlines (black solid lines) and was making new highs. The right side has a declining top and bottom trendlines.

There are a few more concerns I have about the market: 1. December is normally the strongest month of the year, last December the market was down. 2. Normally January is harbinger of a new year, so far this January is pointing to a weak market for 2016.

From a technical analysis stand point, if prices don't hold long-term support, the 15,750 area, the market could lose about the same amount that it lost from the its peak to long-term support. This means the market could fall to 13,200 (15,750 long-term support – 2,550). Technicians call this calculation measuring.

An easier way to calculate how far the market could fall is by taking the average of the typical bear market. The average bear market is down at least 30% from its peak, so that would mean the market could fall to about 12,810 (18,300 peak times 70% remains from bear market).

If we use the measuring calculation, and if the S & P doesn't hold long-term support, the S & P could drop to 1,585 (1,860 l-t support -275).

If the S & P enters a bear market, the market could fall to 1,493 (2,134 peak times 70%).

2016 Market Forecasts

Below are my market forecasts for 2016:

2016 FORECAST					
	EARNINGS ESTIMATES	RISK,GRWTH ADJ P/E	FORECAST	CURRENT PX	PTNTL %
DJIA	1146.61	15	17,199.15	15,988.00	7.04%
SPX	124	16	1,984.00	1,880.00	5.24%

I reduced the P/E ratios because of slower growth and rising risks. Investors should pay less for earnings in this economic and market environment.

This earnings season that started last week, is expected to be up about 5%. We could get a bounce if the earnings season is good. A few banks posted good earnings last week, but they wound up down, not a good sign, and could be indicative of this earnings season.

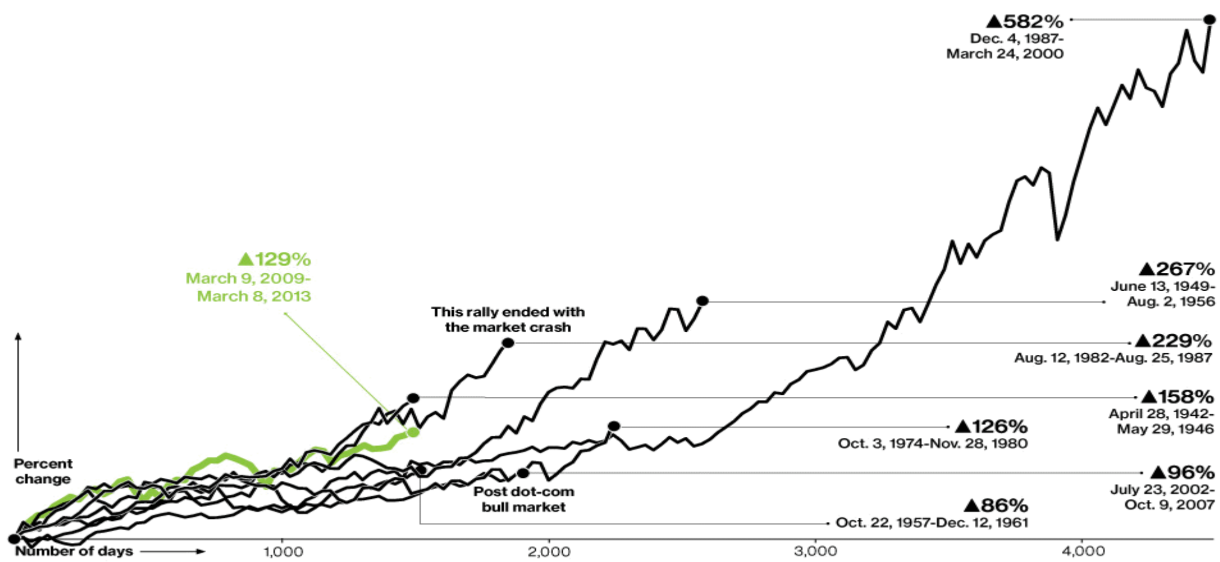
If earnings forecasts are met, and risks are reduced, the markets do have some upside potential.

I would tend to be more cautious. Since the market bottomed in 2009, investors should take profits, raise cash and lower risks in your portfolio.

By taking profits, and raising cash, investors should have cash available to take advantage of lower prices, valuations when we do have our next bear market.

Below is a chart that shows most bull market cycles produce over 100% in returns:

The bull market in the U.S. just sailed past the four-year mark on March 9—and the Dow Jones industrial average hit a record high of 14,397 the day before. The rally in the Standard & Poor's 500-stock index is already the eighth-longest (1,460 days as of March 8) in history, according to financial research shop Bespoke Investment Group, and the sixth-strongest.



If we do have a bear market, there are normally some great bargains for long-term investors.

Make sure you have cash available to take advantage of the next bull market.