LVRAG
Daily Risk Appetite Gauge

Equity Index Futures Trading Recommendations

20th December 2024

"Start BUILDing LONG - Bounce (or resumption of rally) likely to start in next 1 - 2 trading sessions"

Email: info@longvieweconomics.com

Trading Recommendation ('1 – 2' week equity index trading recommendation)

- Move 1/3rd LONG S&P500 March futures at current prices (approx. 5,890/95).
- Increase to 2/3rds LONG 2% below initial entry price.
- Implement stop loss at 3% below combined entry.

Rationale

This market is oversold (in the short term) at an index, sector, and single stock level. It's also fearfully priced and positioned risk aversely. Reflecting that, a lot of short-term indicators are signalling that either a bounce is about to occur in these markets; or that the uptrend is about to resume.

Index technical scoring systems, for example, are mostly now on BUY/strong BUY. That is, the S&P500, the NDX100, the global equity index, the DAX and the Russell 2000 amongst others are all oversold (with the Philly SOX the one key exception) – see FIGs 1, 3 & 3a. As the S&P500's short term technical scoring system shows, once the model is at this low (strong BUY) level, the equity market should bounce for a handful of trading sessions (at a minimum, FIG 1). On 25th July, for example, the model reached strong BUY. The index then bounced through to 31st July before the final wave of selling in that pullback (which had been ongoing since July 16th). Equally, the BUY signals on 6th September and then late October were both followed by an immediate resumption of the uptrend (see FIG 1).

The **message is similar for 'single stock' and 'sector' technical models.** At 2.3%, the 'percentage of stocks which are overbought', for example (FIG 1a), is at its lowest level since early October 2023. That was then immediately followed by a four-day bounce, before the market sold off again to make its major local low (on 27th October). Other low readings on this model, like the index technical scoring system above, have been followed by strong rallies/resumption of the uptrend (see FIG 1a). The NYSE volumes model (measuring the gap between declining and advancing volumes) is similarly positioned (FIG 1b).

Added to the above, risk appetite models, as highlighted yesterday, are now on/close to BUY (i.e. the market is increasingly fearful – as also shown by high volatility/VIX readings). There was also some BUYing of downside put protection yesterday, such that the 1 day put to call ratio started moving lower (NB inverted on the chart – FIG 4) – although the model isn't yet on BUY.

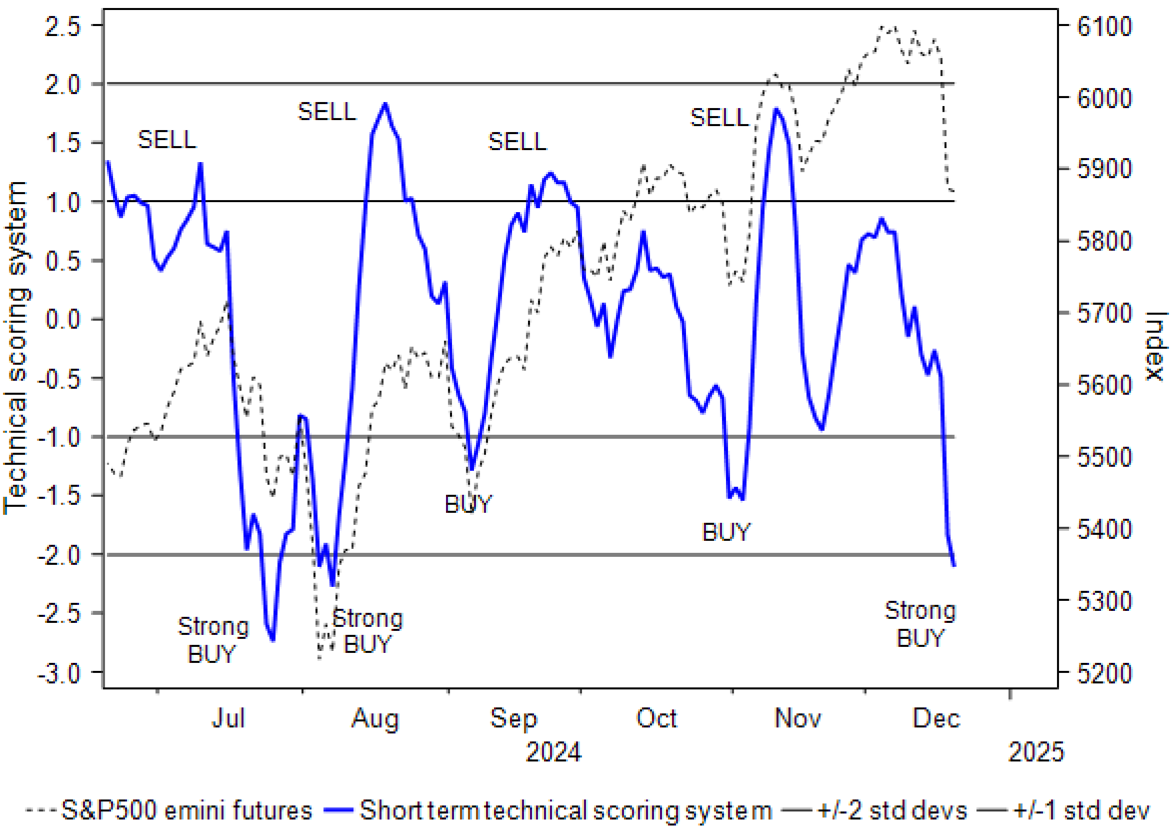
All of the above, therefore, supports an expectation of at least a bounce – which is likely to start today or in the next 1 – 2 trading sessions. That bounce might either last a handful of trading sessions (i.e. 4 or 5); OR continue for several weeks (i.e. if the uptrend resumes/Santa rally etc.). Those are the two most likely outcomes, at this juncture. Naturally if it's the former, risk management of the trade (and specifically the stop loss) will be critical. As such, the most efficacious way to play it is with an initial LONG position at current levels (i.e. with the S&P500 currently at its intraday lows from Wednesday's trading session/which is also a key support level – see FIG 1c); and then increase the position size if the market sells off today/Monday (i.e. at 2% below the initial entry level); with a stop loss that is then 3% below combined entry. Risks, as always, are multiple and include the challenges within Congress with respect to passing a 'funding' bill to avert a government shutdown.

A full list of today's key macro data & events is outlined below.

Kind regards,

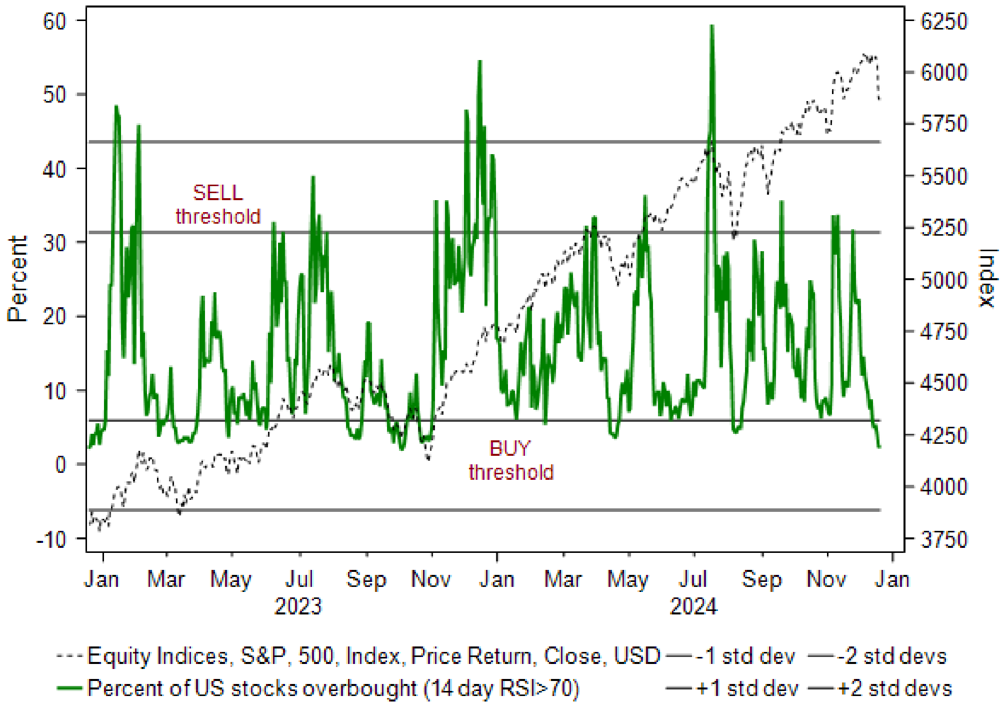
The team @ Longview Economics

FIG 1: Longview **S&P500** short term **'technical'** scoring system vs. S&P500 futures



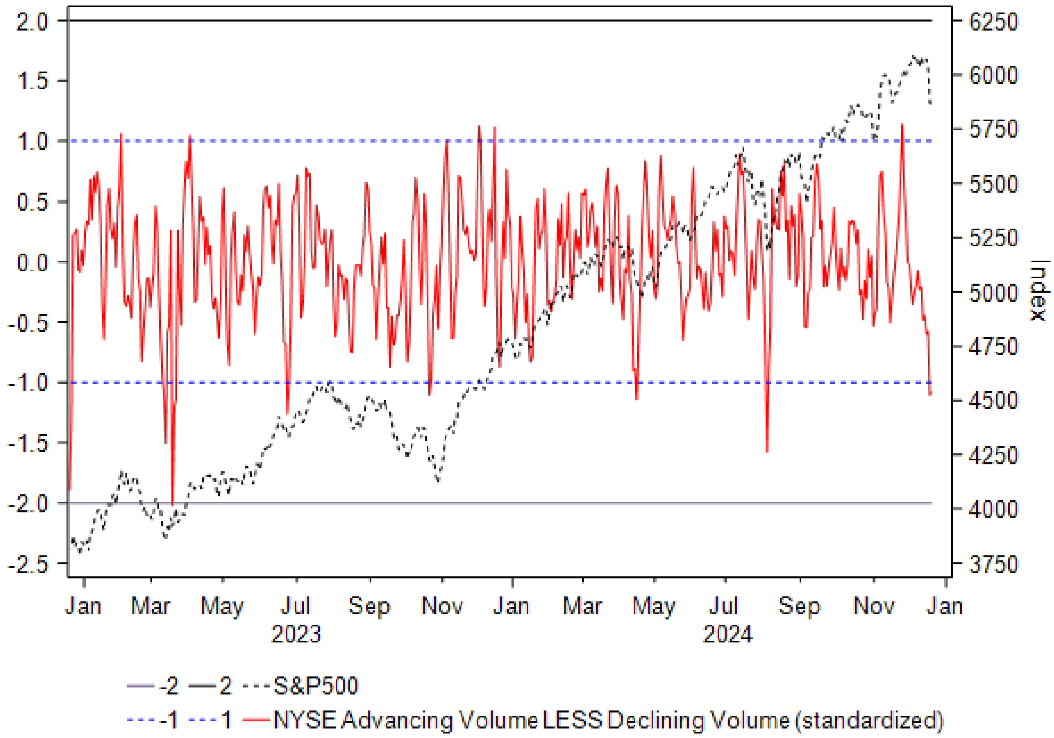
Source: Longview Economics, Macrobond

FIG 1a: Percentage of US single stocks which are overbought (i.e. with RSIs>70)



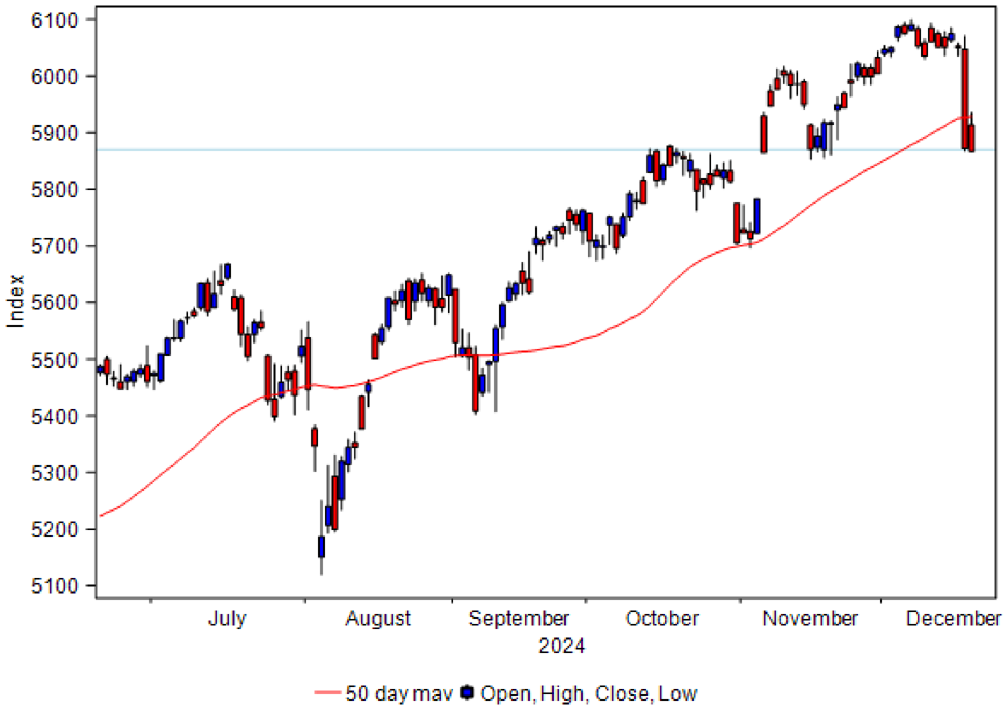
Source: Longview Economics, Macrobond

FIG 1b: NYSE volumes (advancing less declining volumes) vs S&P500



Source: Longview Economics, Macrobond

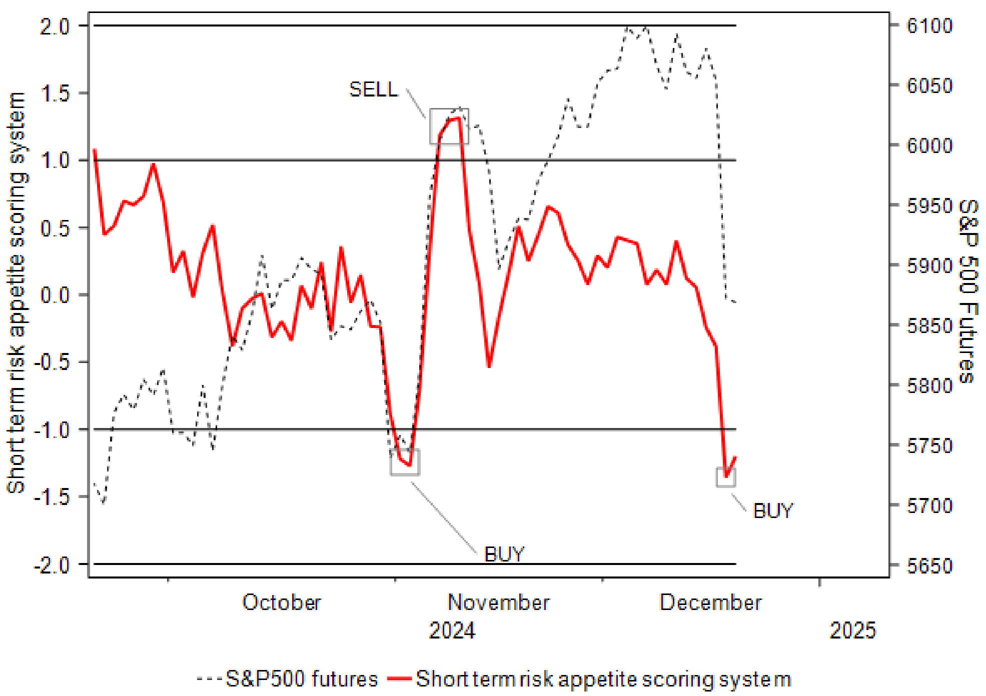
FIG 1c: S&P500 **candlestick** shown with its 50 day moving average



Source: Longview Economics, Macrobond

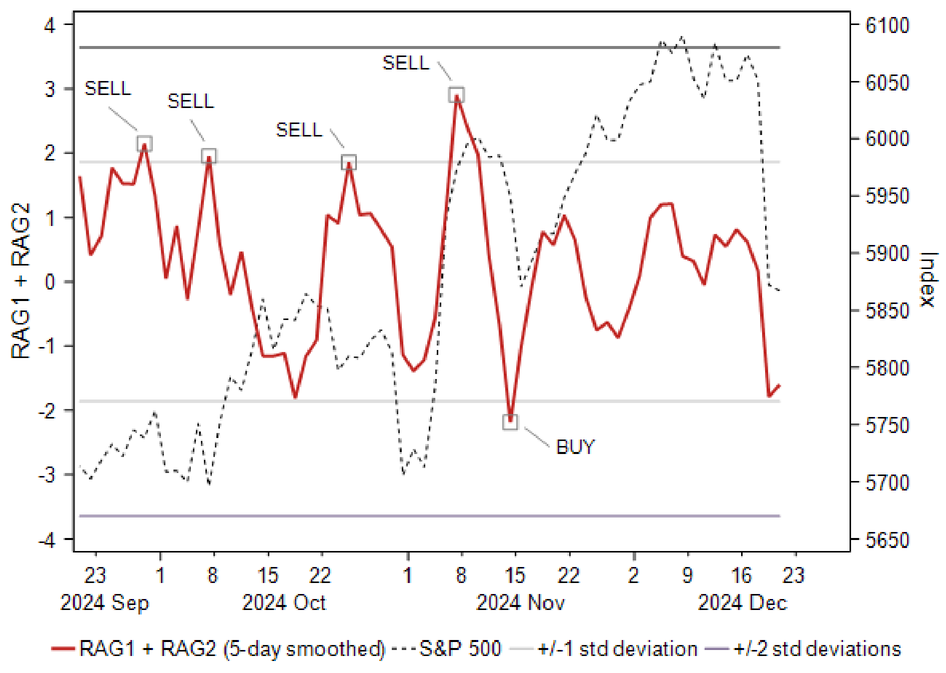
Risk appetite models are now on/close to BUY…

FIG 2: Longview short term **'risk appetite'** scoring system vs. S&P500



Source: Longview Economics, Macrobond

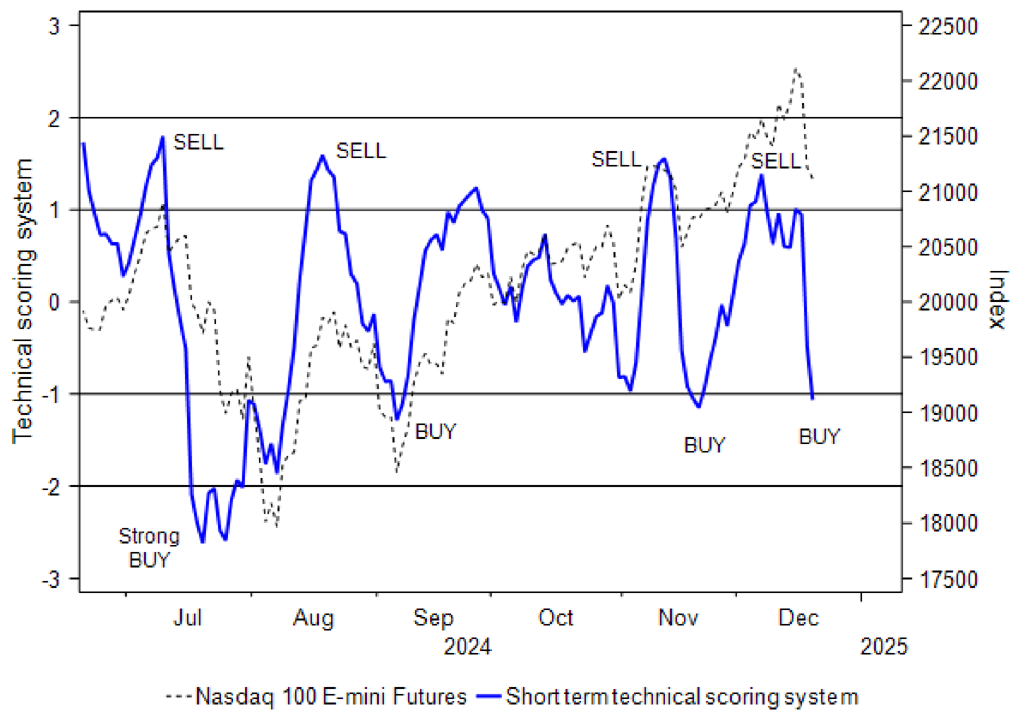
FIG 2a: Longview combined key **'risk appetite'** models (RAG1 + RAG2) vs. S&P500



Source: Longview Economics, Macrobond

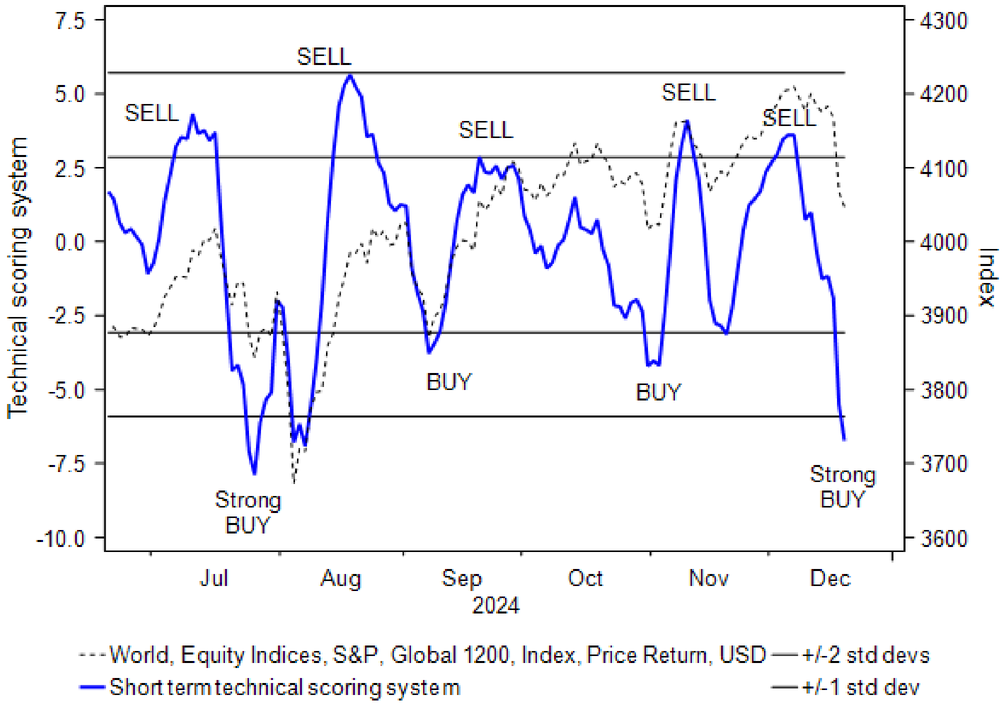
Technical models are mostly on BUY....

FIG 3: Longview **NDX100** short term **'technical'** scoring system vs. NDX100



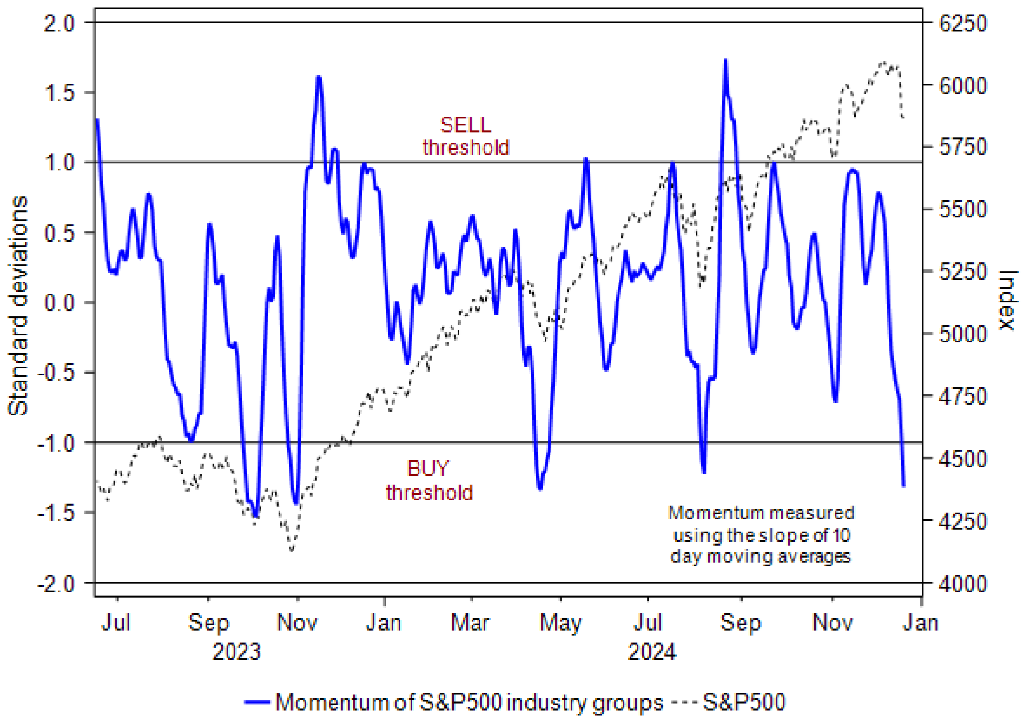
Source: Longview Economics, Macrobond

FIG 3a: Longview global short term **'technical'** scoring system vs. global equity index



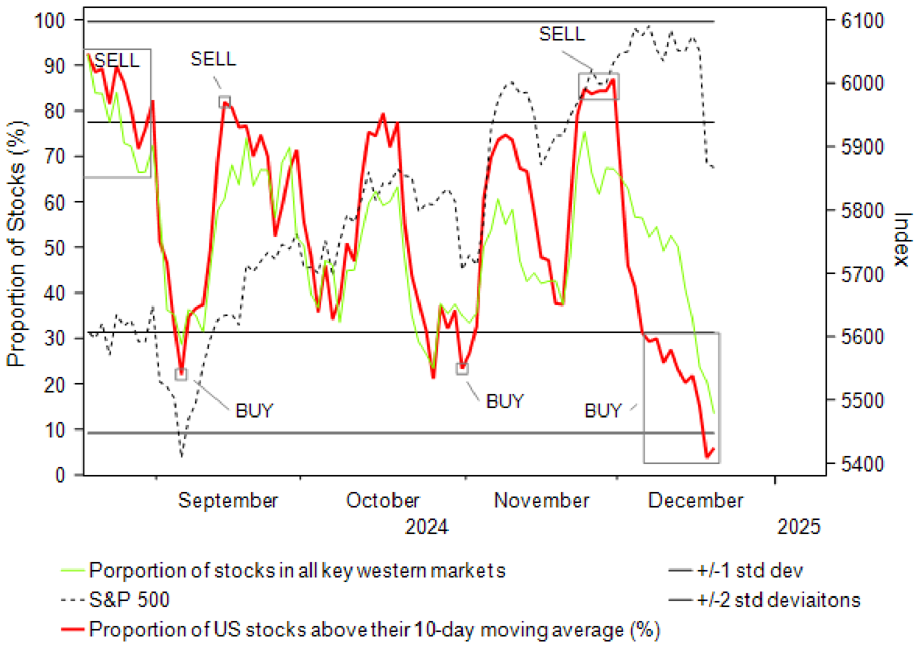
Source: Longview Economics, Macrobond

FIG 3b: Momentum of S&P500 industry groups vs. S&P500 cash index



Source: Longview Economics, Macrobond

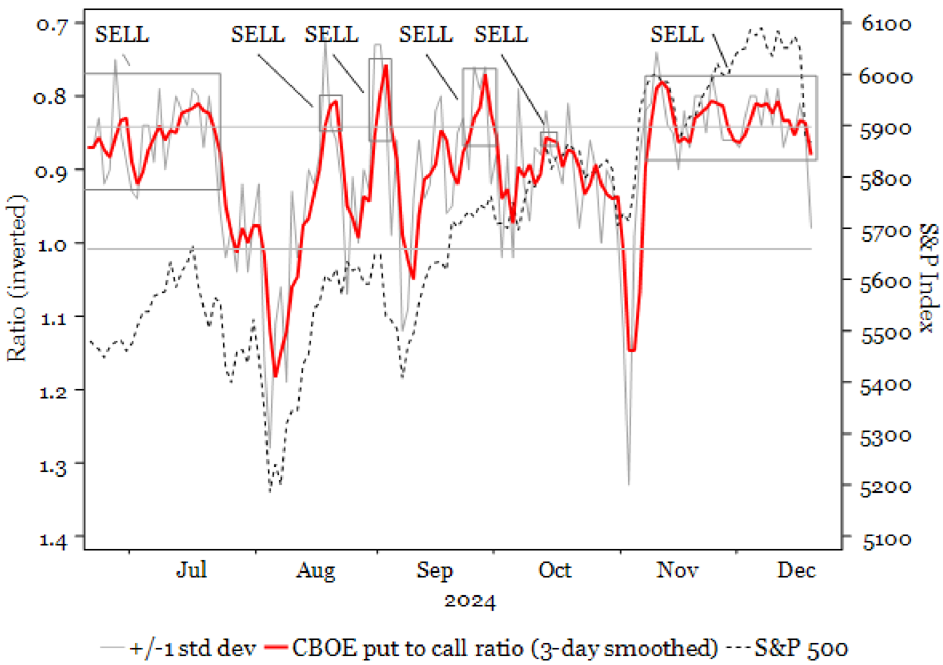
FIG 3c: Proportion of US/Western stocks above their 10-day moving average vs. S&P500



Source: Longview Economics, Macrobond

Downside put protection in portfolios remains low…

FIG 4: CBOE put to call ratio (1 & 3 day smoothed with standard deviation bands) vs. S&P500

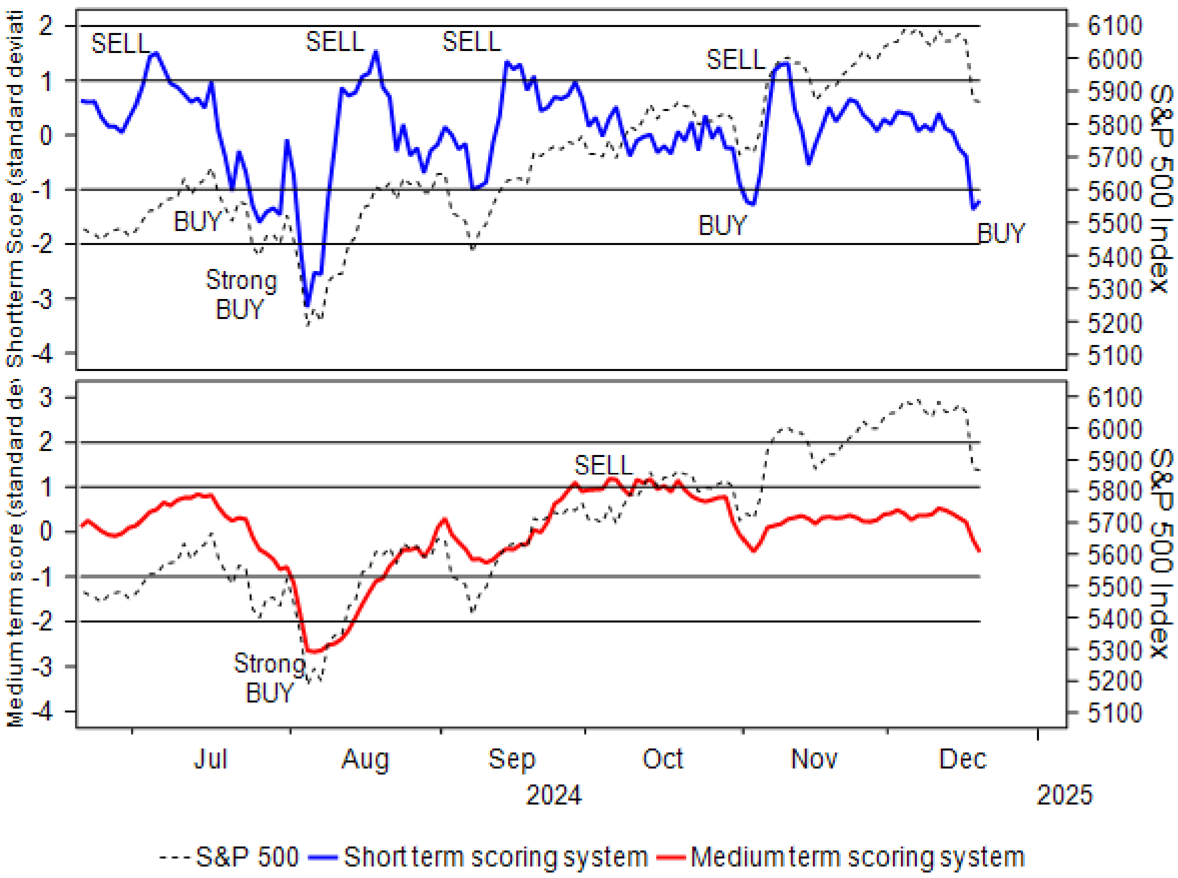


Source: Longview Economics, Macrobond

Key Longview Scoring Systems (chart below)**:**

Short term (1 – 2 week) scoring system: **BUY**
Medium term (1 – 4 month) scoring system: **NEUTRAL**

FIG A: Longview short and medium term scoring systems vs. S&P500



Source: Longview Economics, Macrobond

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Key macro data/events

Key data today include: Australian private sector credit (Nov, 12:30am); UK Public sector finances (Nov, 7am); **UK retail sales** (Nov, 7am); **German PPI** (Nov, 7am); French PPI (Nov, 7:45am); Spanish total mortgage lending (Oct, 8am); Italian ISTAT consumer & manufacturing confidence (Dec, 9am); Italian industrial sales (Oct, 10am); Italian PPI (Nov, 11am); UK CBI distributive survey (Dec, 11am); **US personal income & spending including headline & core PCE** (Nov, 1:30pm); Canadian retail sales (Oct, 1:30pm); **Eurozone consumer confidence** (December first estimate, 3pm); US Michigan sentiment (December final estimate, 3pm); US Kansas City Fed service sector activity (Dec, 4pm).

Key events today include: **PBOC policy decision** (1am).

Key earnings today include: N/A

Definitions & other matters:

RAG = Risk Appetite Gauge

The 'Daily Risk Appetite Gauge' publication is designed to generate '1 to 2' week trading recommendations on equity indices. For trading recommendations on currencies, rates, bonds and other assets, pls see Macro-TAA trade publications.

For a medium-term recommendation please see our '1 – 4' month tactical market views which are updated at the start of each month in our Tactical Equity Asset Allocation publication (as well as occasional ad-hoc intra month Tactical Alerts). The latest update was published earlier this month on 5th December 2024. If you are not on the distribution list and would like to receive these reports pls email info@longvieweconomics.com.

LVRAG

Daily Risk Appetite Gauge

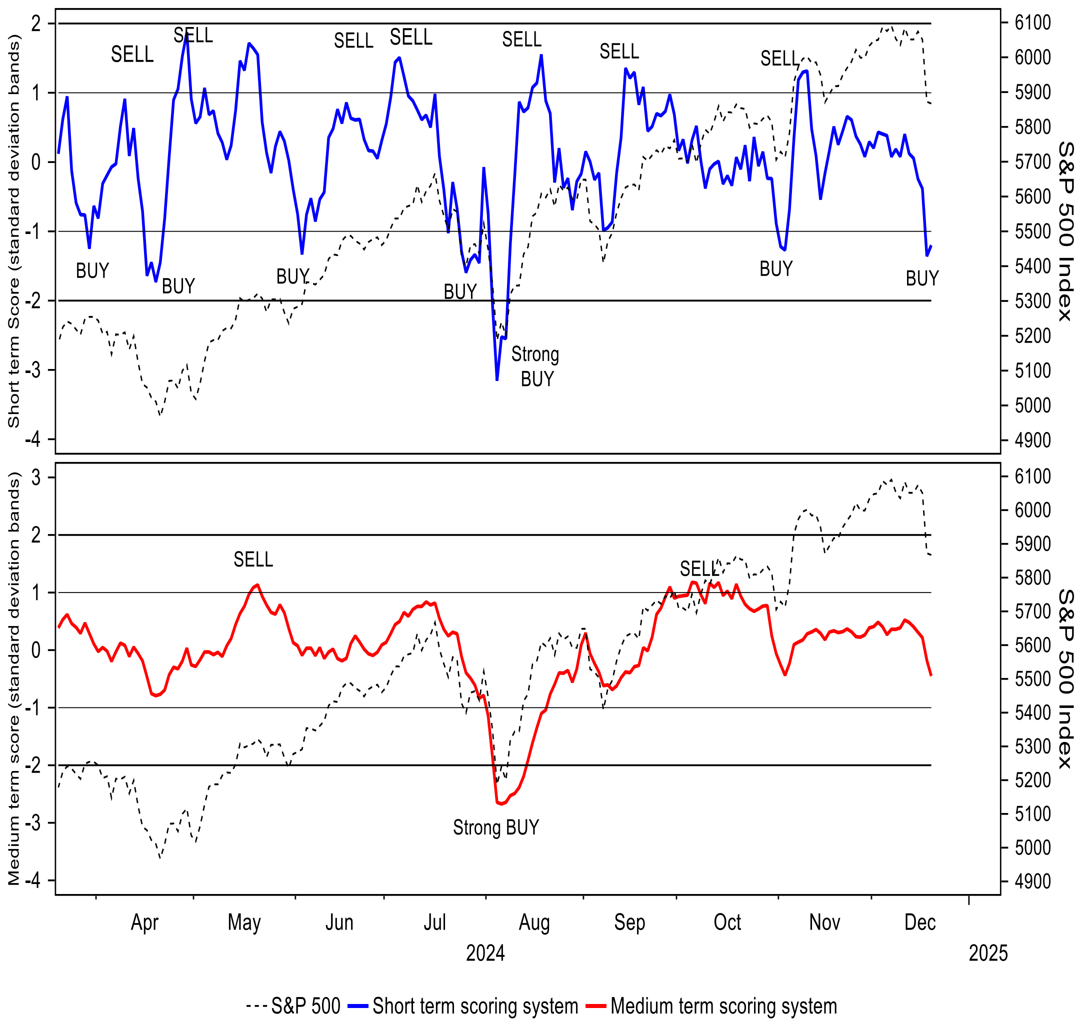
1 – 2 Week View on Risk

20th December 2024

Longview Economics
Email: ragtrader@dailyragtrader.com

Section 1: Longview Scoring Systems (short & medium term*)

Fig 1: Longview 'short term' and 'medium term' scoring systems



Source: Longview Economics, Macrobond

Short term scoring system is on BUY

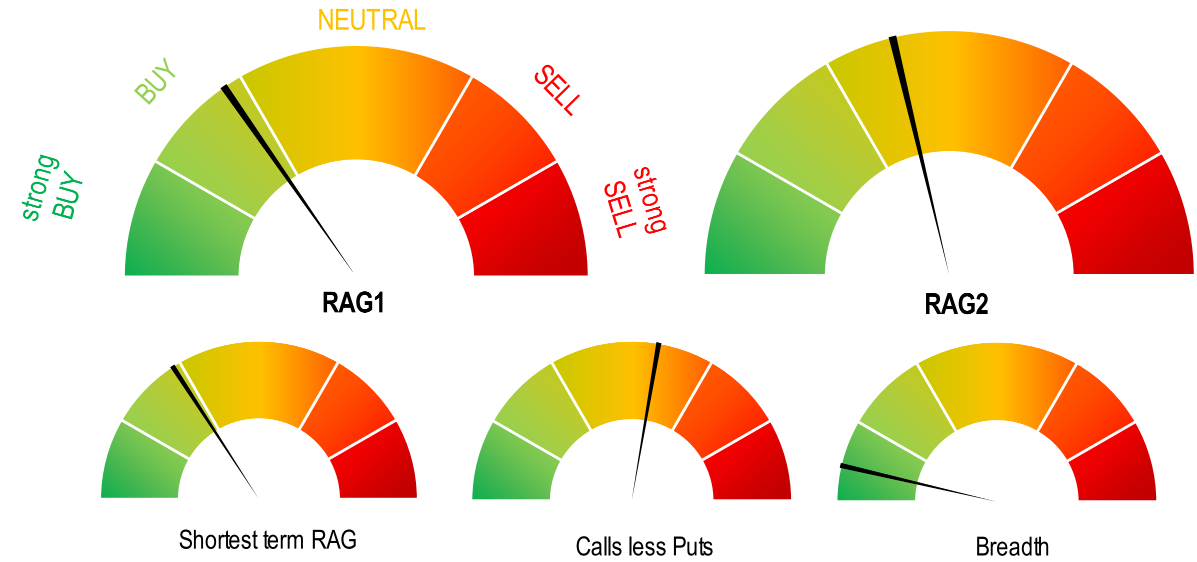
Medium term scoring system is NEUTRAL

*NB short term is 1 – 2 weeks; medium term is 1 – 4 months

Important disclosures are included at the end of this report
For explanations of indicators please see page 10

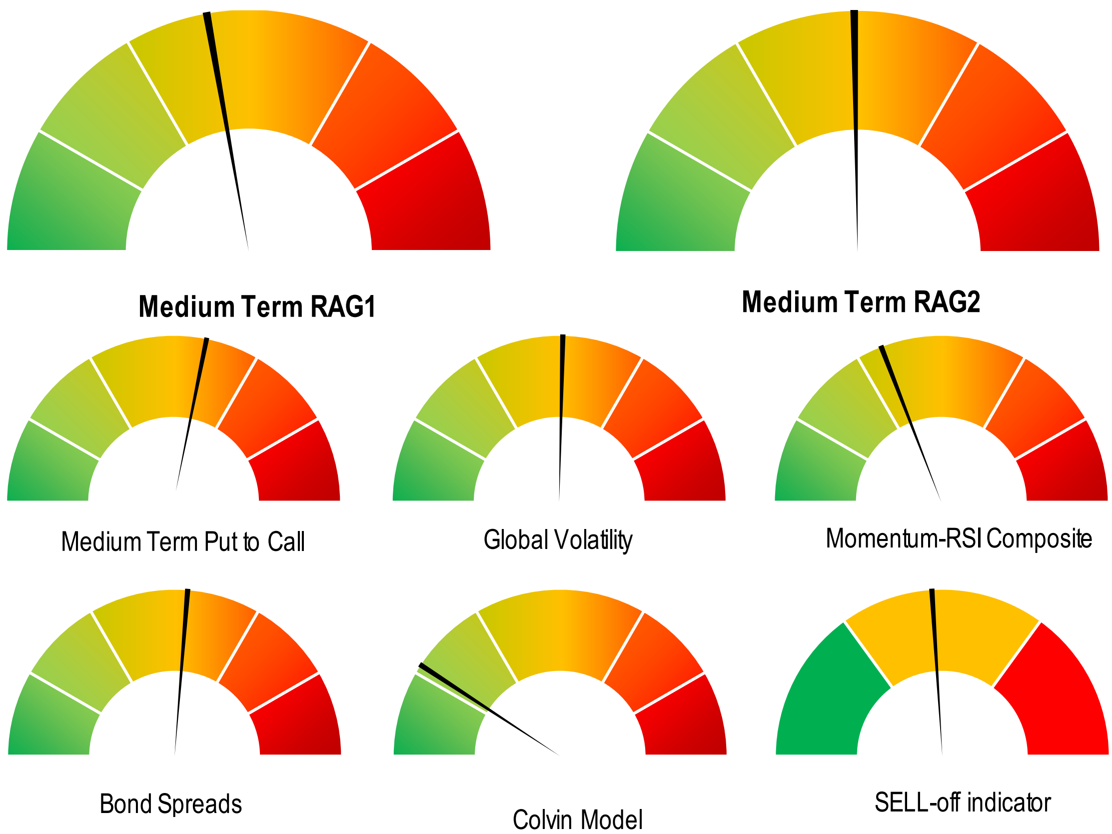
Section 1a: Summary of indicator signals**

Fig 1a: Short term models – shown as gauges using standard deviation bands



Source: *Longview Economics*

Fig 1b: Medium term models – shown as gauges using standard deviation bands

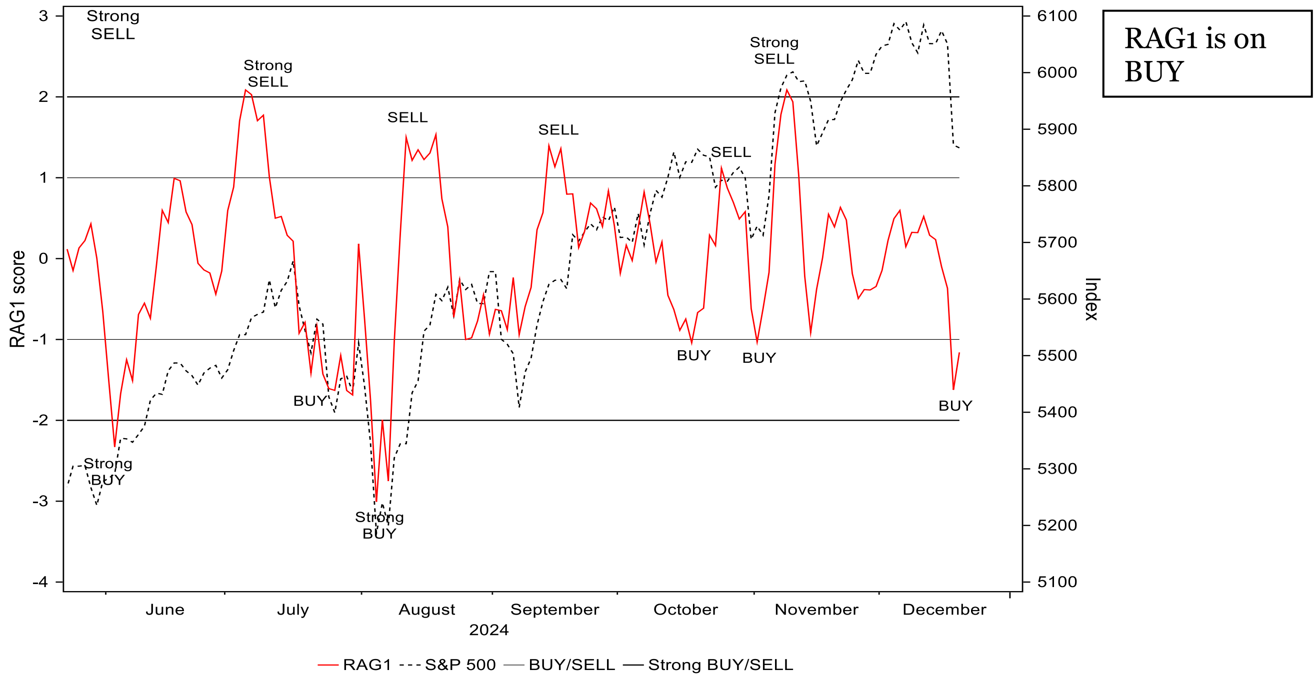


Source: *Longview Economics*

**The gauges are a pictorial representation of the strength of the current BUY, SELL or NEUTRAL signal of each indicator

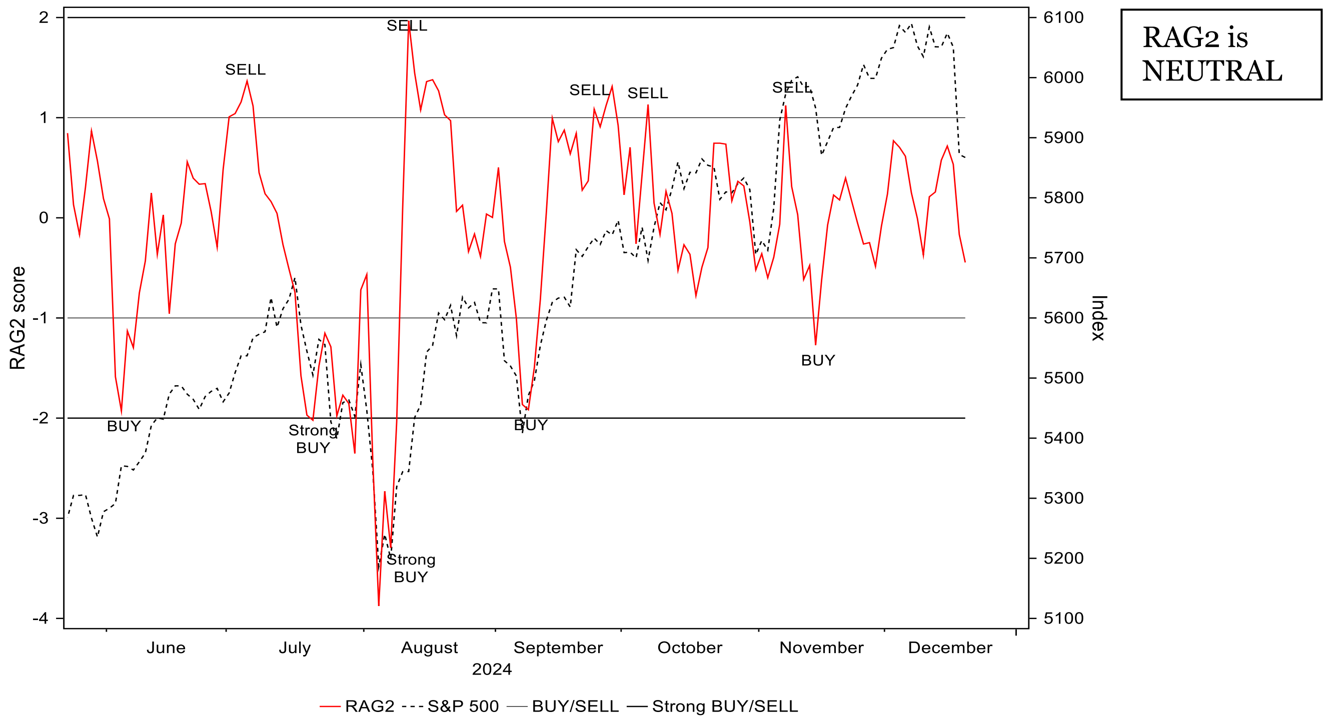
Section 2: Short term (1 – 2 week) trading models

Fig 2a: RAG 1 vs. S&P 500



Source: Longview Economics, Macrobond

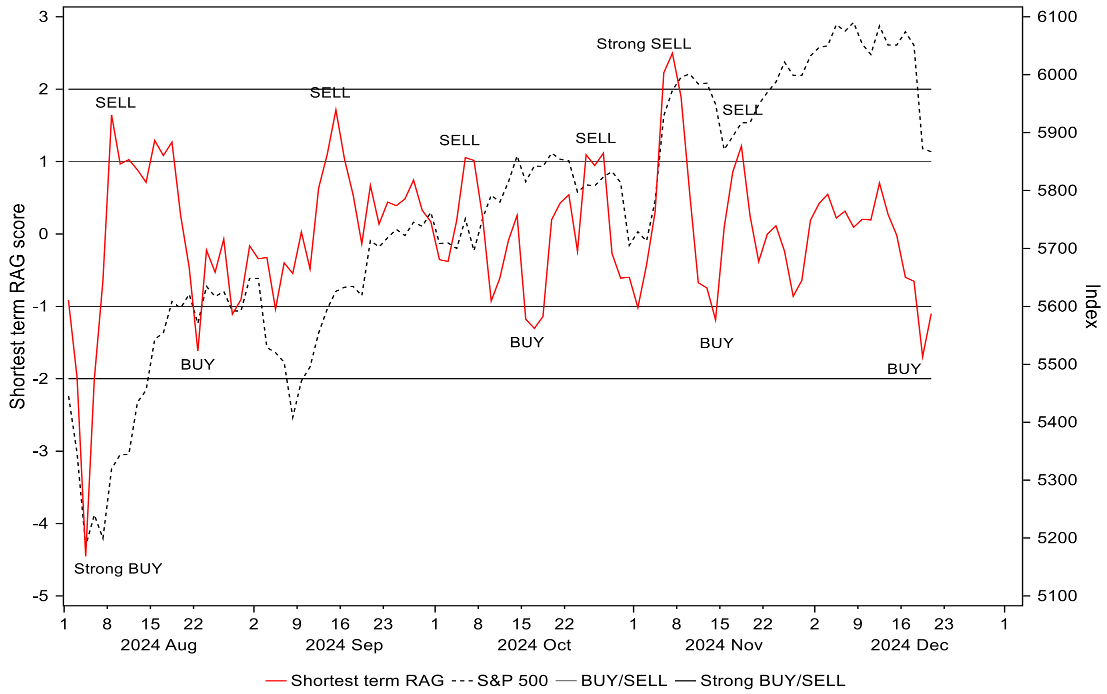
Fig 2b: RAG 2 vs. S&P 500



Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

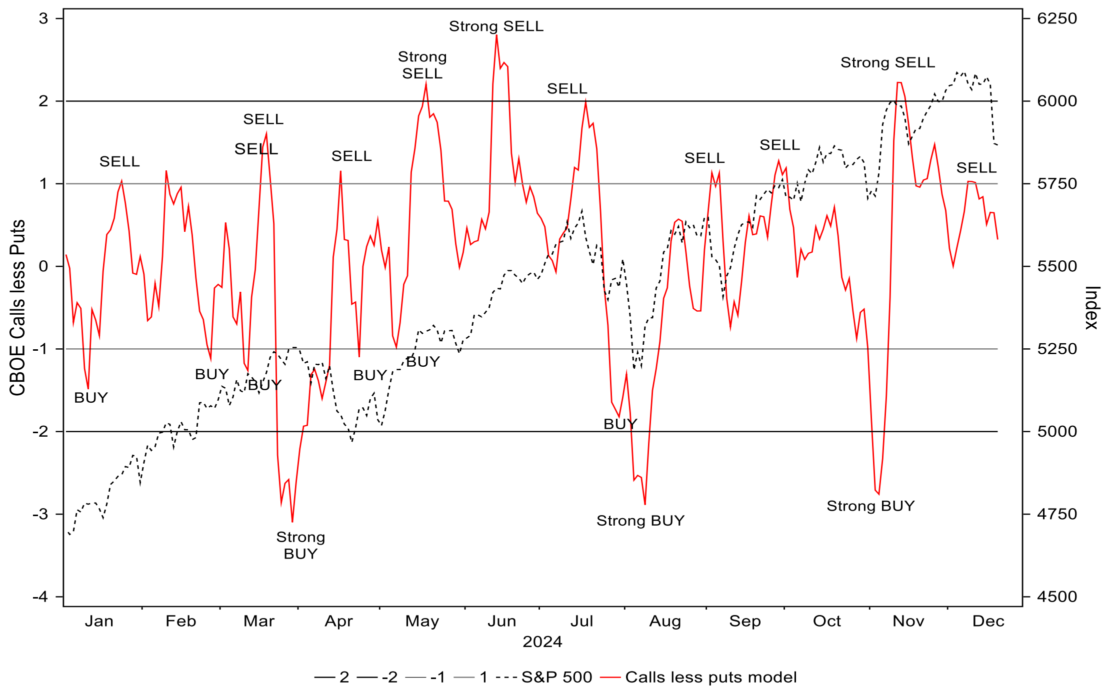
Fig 2c: Shortest term RAG (i.e. using a 3 day moving average) vs. S&P 500



Shortest term RAG is on BUY

Source: Longview Economics, Macrobond

Fig 2d: CBOE calls less puts (5 day moving average) vs. S&P500

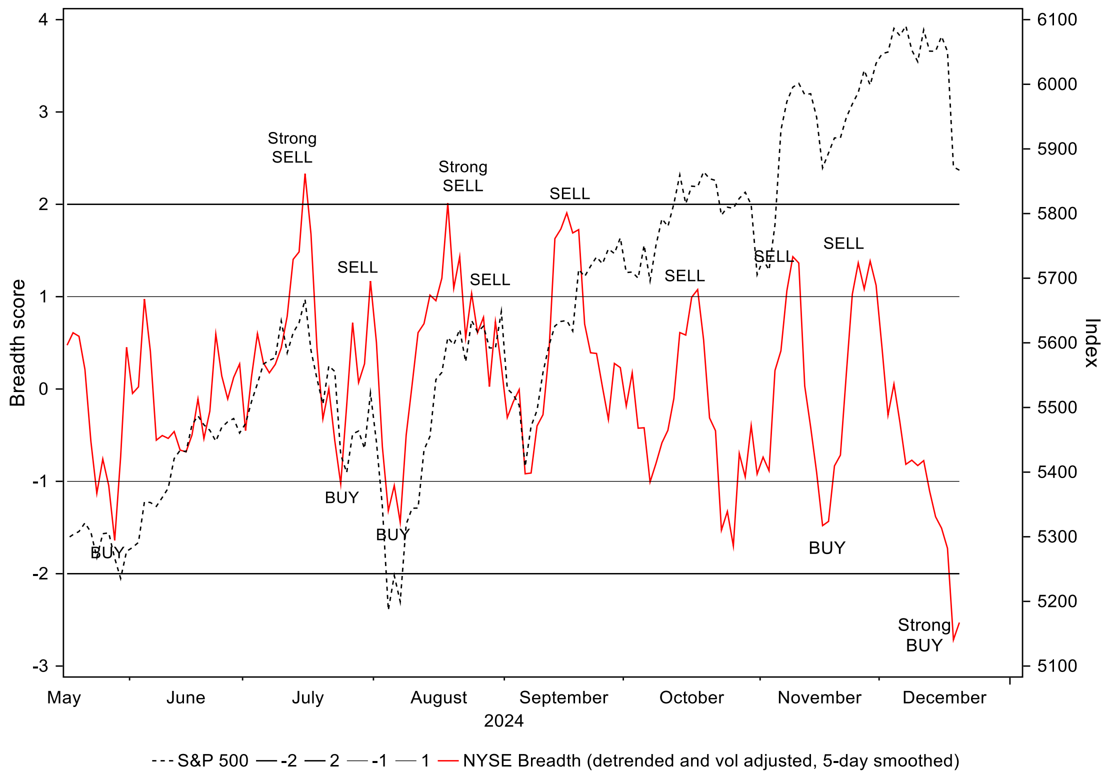


Calls less puts model is NEUTRAL

Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

Fig 2e: Advancers less decliners (NYSE) – 5 day moving average vs. S&P 500



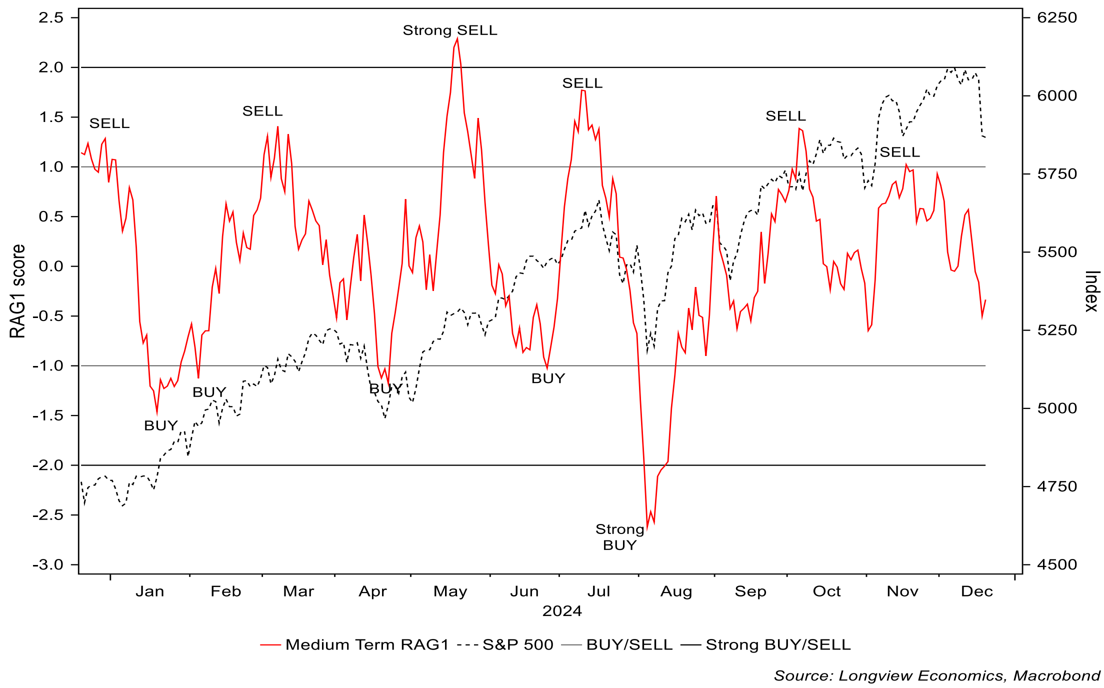
Source: Longview Economics, Macrobond

The breadth model is on Strong BUY

For explanations of indicators please see page 10

Section 3: Medium term (1 – 4 month) outlook

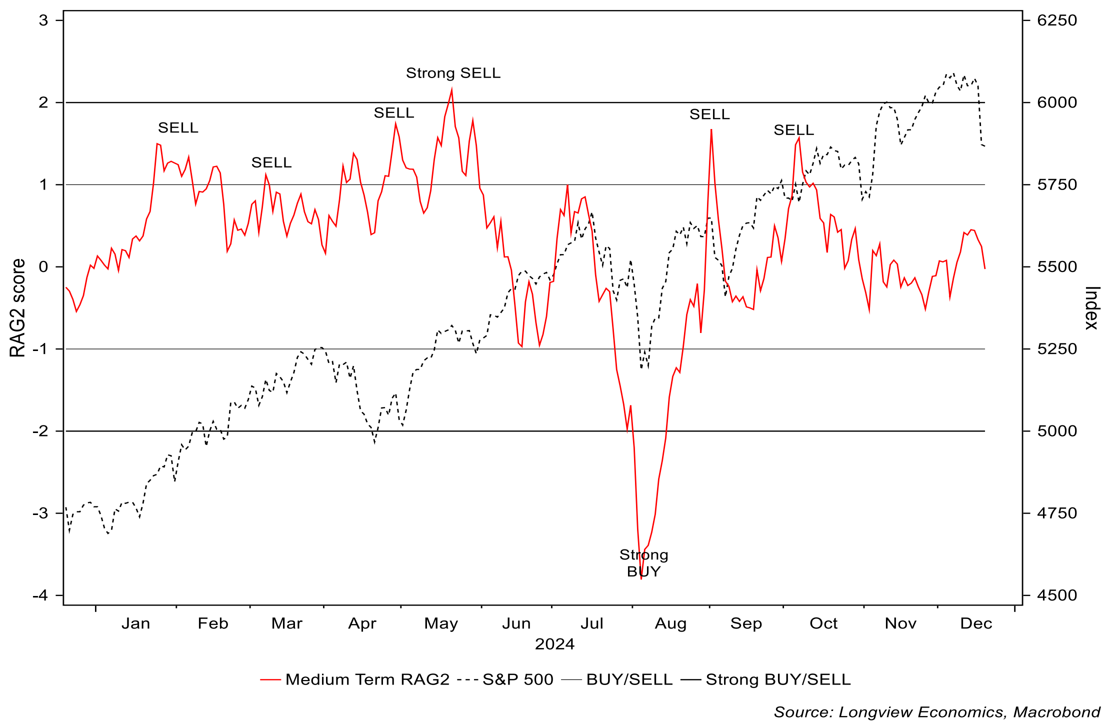
Fig 3a: Medium term RAG1 (1 – 4 month view) vs. S&P 500



Medium term RAG1 is NEUTRAL

Source: Longview Economics, Macrobond

Fig 3b: Medium term RAG2 (1 – 4 month view) vs. S&P 500

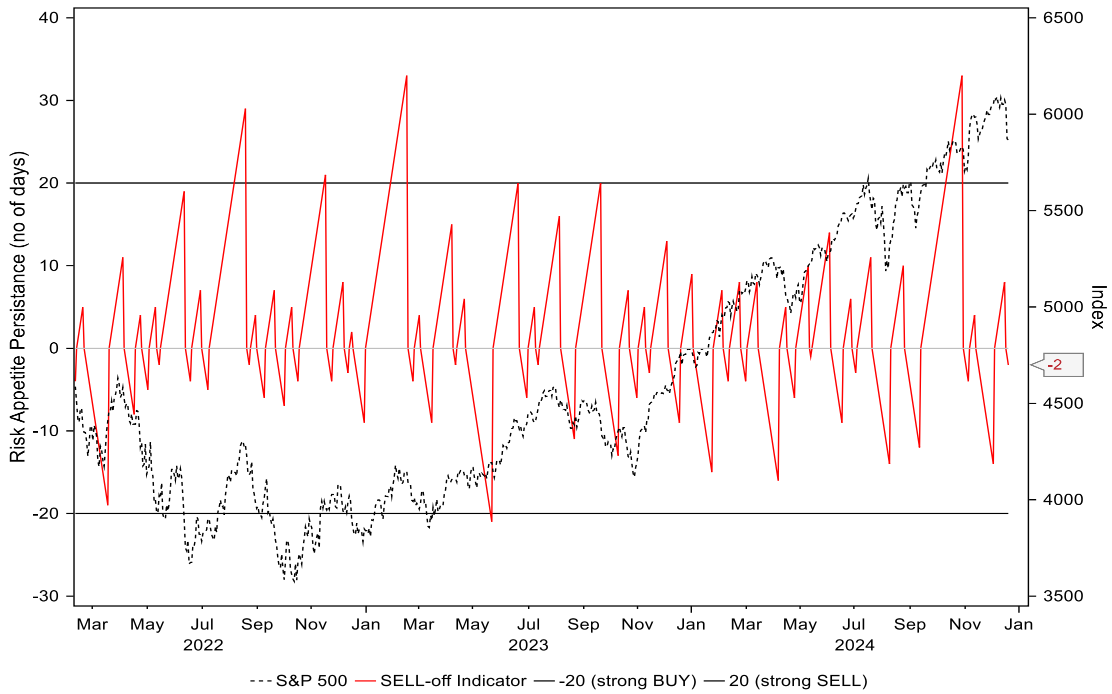


Medium term RAG2 is NEUTRAL

Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

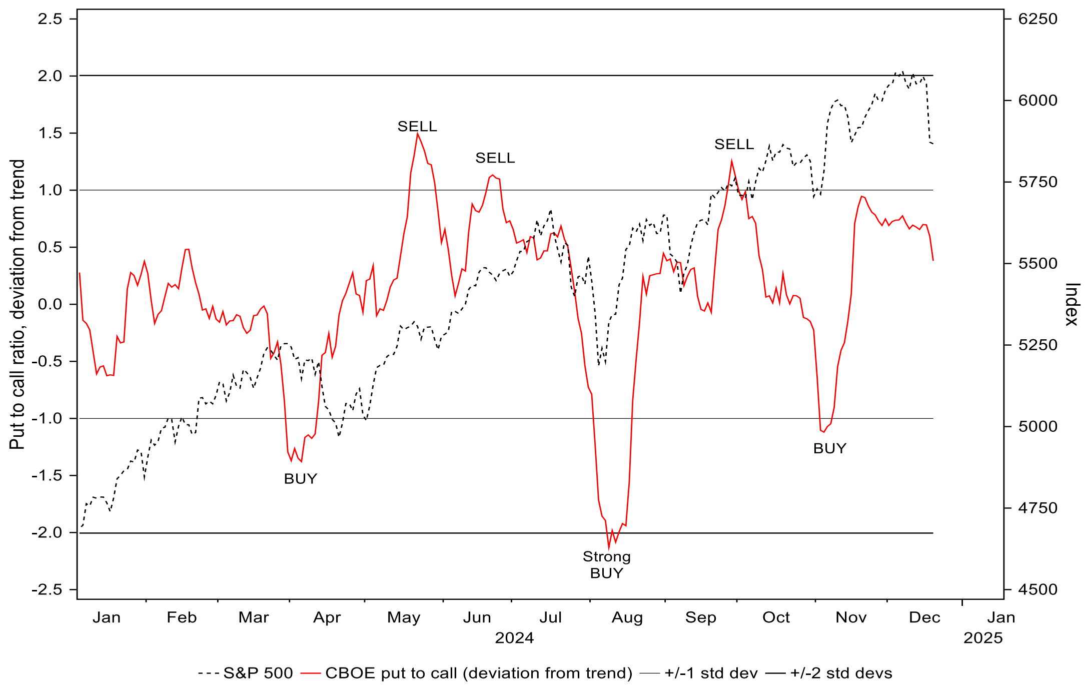
Fig 3c: SELL-off indicator (shown vs. S&P500)



Source: Longview Economics, Macrobond

The SELL-off indicator is NEUTRAL

Fig 3d: CBOE put to call trend deviation model vs. S&P500

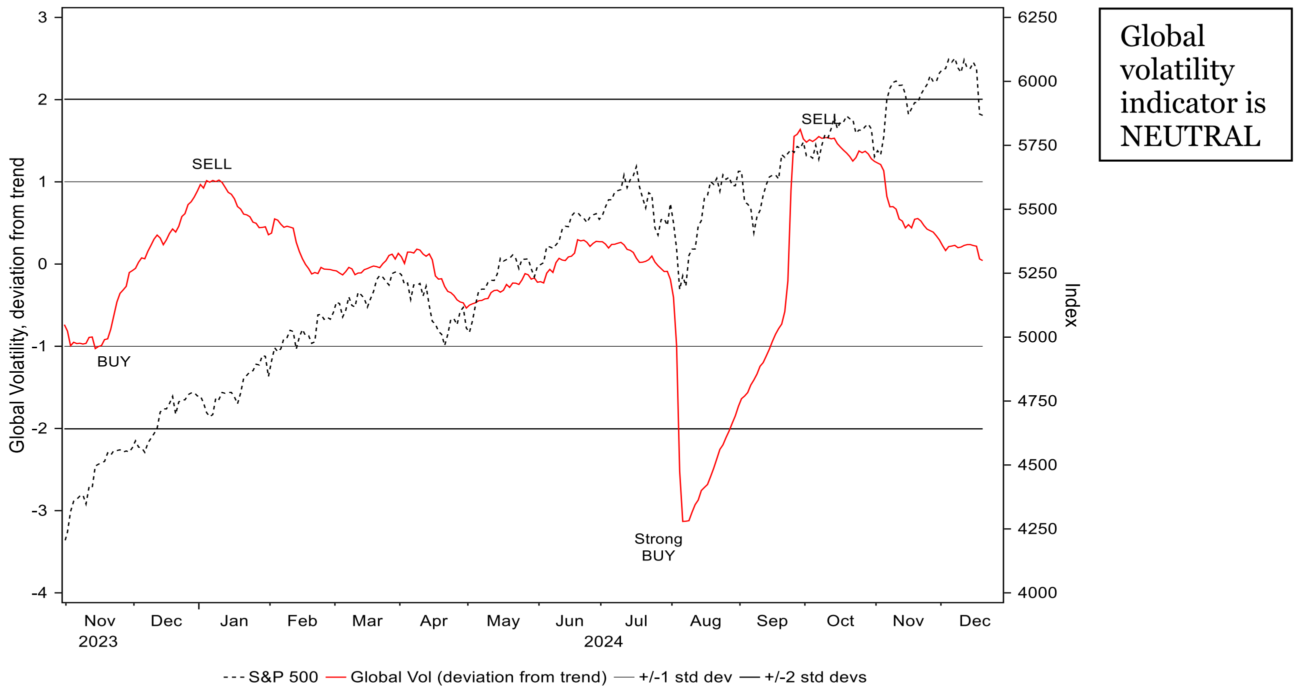


Source: Longview Economics, Macrobond

Medium term put to call model is NEUTRAL

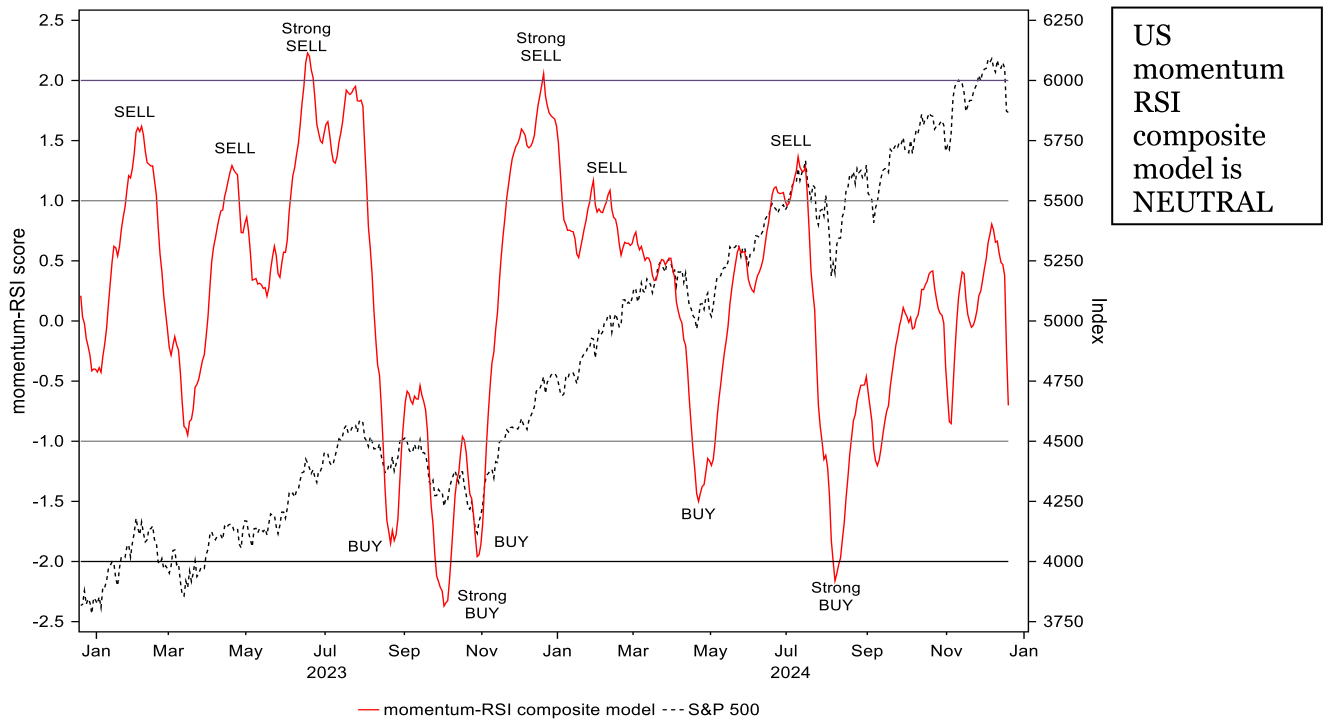
For explanations of indicators please see page 10

Fig 3e: Global volatility (deviation from trend) model vs. S&P500



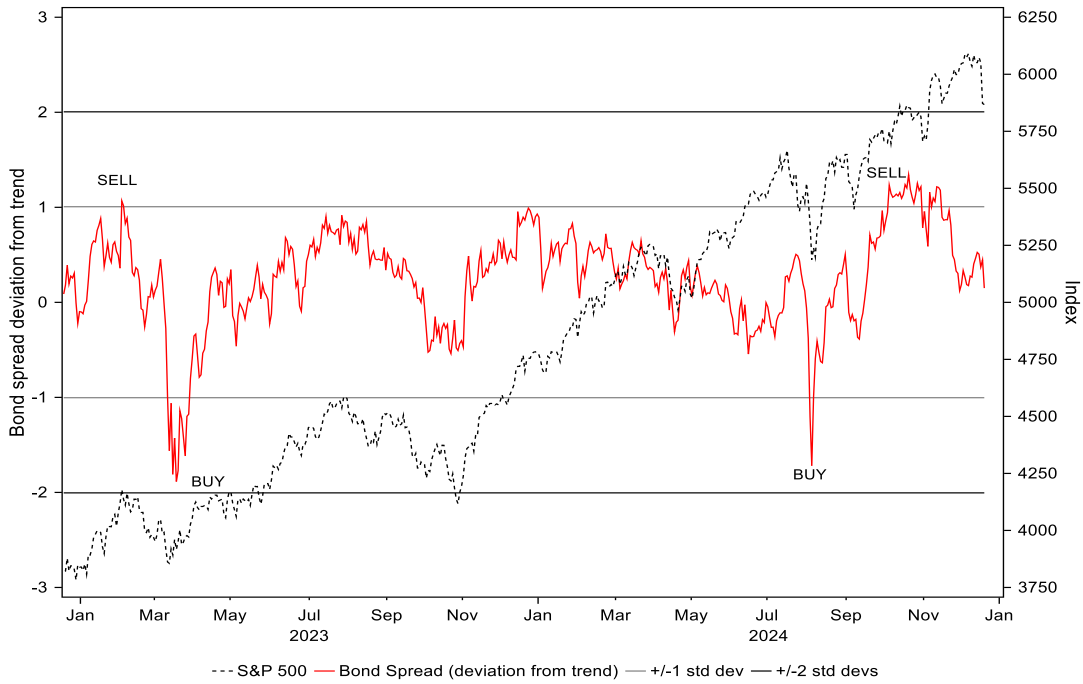
Source: Longview Economics, Macrobond

Fig 3f: Longview Momentum-RSI composite model vs. S&P 500



Source: Longview Economics, Macrobond

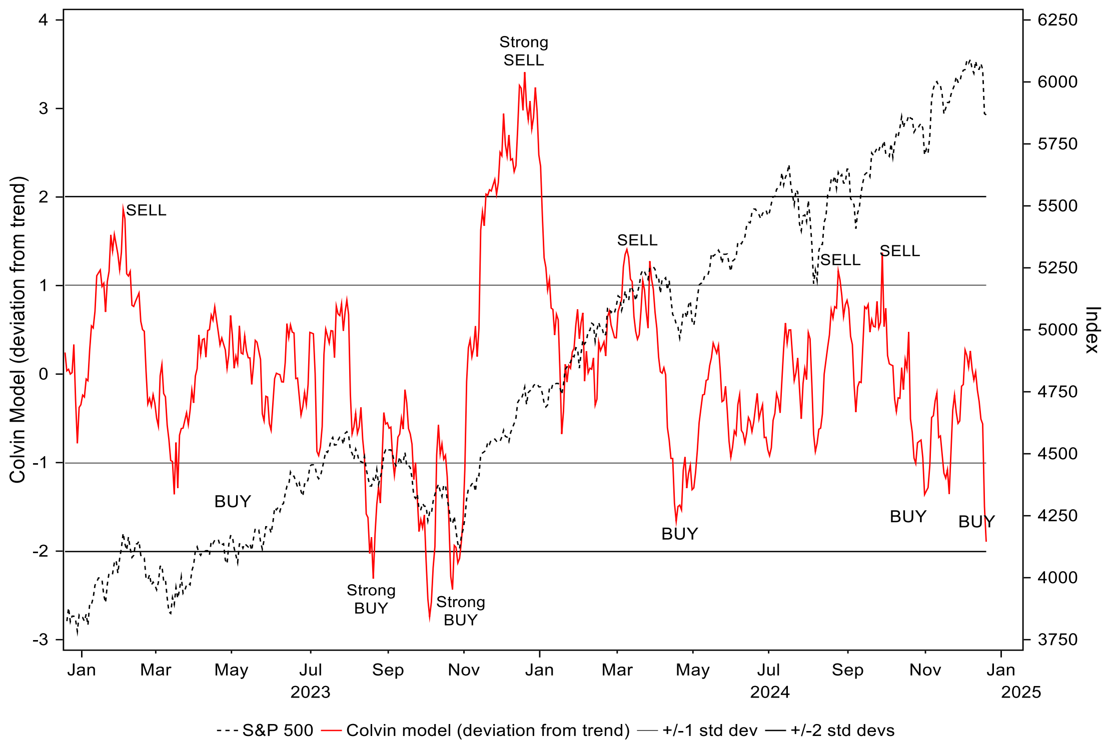
Fig 3g: High yield corporate bond spreads deviation from trend model vs. S&P500



Source: Longview Economics, Macrobond

High yield corporate bond spreads model is NEUTRAL

Fig 3h: Colvin model (deviation from trend) vs. S&P500



Source: Longview Economics, Macrobond

Colvin model – is on BUY

For explanations of indicators please see page 10

Appendix: Model Explanations

Model 2a-b: Short term RAG1 & RAG2 (risk appetite gauge)
RAG1&2 each draw upon the volatility and price movement of approximately 70 financial instruments each day. By plotting risk curves we derive the risk appetite of the investment community as a whole on any and every day's trading in financial markets.

Model 2c: Shortest term RAG
This RAG model is a shorter term moving average risk appetite model than model 2a. By being shorter term in nature it helps to more accurately time the entry day for a specific trade.

Model 3a – 3b: Medium term RAGs
This is a medium term version of the risk appetite models. This is designed to forecast the direction of equity markets on a 1 – 2 month timeframe.

Model 3c: SELL-off indicator
The SELL-off indicator measures the number of days our RAG system has been on a SELL signal (i.e. as a positive number) and the number of days which it has been on a BUY signal (negative reading). When the indicator moves above +20 (i.e. risk appetite has been persistently high for a long period of time) this indicator warns of a potential sell-off in equity markets (and other risky assets). Most major SELL-offs in equity markets in recent years have been accompanied/foreshadowed by a reading of over +20.

Model 3d: CBOE put to call (deviation from trend model)
This model measures movements in the put to call ratio from its medium term moving average trend line. A sharp move higher (lower) in the put to call ratio indicates heightened levels of fear (complacency) and is used as a contrarian indicator. NB Given that the absolute put to call ratio has historically undergone long term structural trends, a deviation from trend model correlates more closely with medium term trends in equities.

Model 3e: Global volatility (deviation from trend model)
The (underlying) global volatility indicator measures the degree of complacency in financial prices. It achieves this by measuring short term realised volatility in over 150 financial assets from around the globe and across the asset class spectrum. A low reading indicates that only a low level of risk is priced into financial markets (and vice versa). Given, though, that volatility is an asymmetric measure of risk we use a deviation from trend version – which correlates more closely with trends in equities.

Model 3f: Momentum Model
Based on the rate of acceleration (or deceleration) of the momentum of the convergence (or divergence) of a short and a long term moving average of the equity or other price index. The concept is equally applicable to any financial market and the signals are particularly pertinent at extremes.

Model 3g: High yield corporate bond spreads (deviation from trend model)
This model measures movements in the spread of high yield corporate bonds over US Treasury yields from its moving average trend line. Given that the spread is an asymmetric measure of risk we use a deviation from trend version – which correlates more closely with trends in equities.

Model 3h: Colvin model
The Colvin model measures global market breadth i.e. the strength of the advance (or decline) in global risk asset prices. Extreme deviations from trend reflect rapid advances/declines in asset prices thereby leading to and generating overbought/oversold signals.

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