Equity Index Futures Trading Recommendations
16th October 2024

"Cracks Starting to Emerge in the Uptrend/SELL-off Indicator on +23"

Email: info@longvieweconomics.com

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

- Close 1/3rd LONG December SPX futures at current prices (entry was earlier this week at 5,861.50).

- WATCH & WAIT (for now).

Rationale

Cracks are starting to appear in the upward momentum of the market. Profit warnings over the past 24 hours have triggered those cracks. ASML's weak Q3 order book yesterday led to a SELL-off in the Philly SOX, with the index down 5.3% on the day (& ASML -15.6%, its worst day since 2002; while Nvidia was down 4.7%). LVMH also issued a profit warning overnight (with its ADRs trading, at one stage, over 10% lower). With that, the main US equity indices were also down (caught up in that weakness in tech; the energy sector was also soft on the back of the 4% fall in the oil price). The S&P500 was down 0.8% on the day, the NDX100 was -1.4%. In contrast, some of the mid and small cap indices bucked the negative mood and ended the day (marginally) positive. The main European index (STOXX 600), meanwhile, generated a bearish key day reversal. It also looks like it's failing again at a key technical resistance level (FIG 1). Elsewhere, the dollar was largely unchanged although it has, in the past few trading sessions, strengthened notably (with its usual correlation with the S&P500 breaking down – FIG 1a).

At the same time as those cracks are appearing, though, **signs of risk seeking have persisted**. Italian government bond spreads, for example, have continued to tighten. Other EZ sovereign spreads (e.g. French & Belgium) have also narrowed. Tightening of those spreads is normally a sign of 'risk on'. US high yield and CCC rated corporate bond spreads were largely unchanged yesterday (a key reason US small and mid-cap equities weren't caught up in the weakness in the large caps); whilst the level of outstanding single stock call options continued to rise (a sign of risk seeking behaviour – FIG 1c).

That contrast in markets (& breakdown of correlations across risk assets) is often witnessed at/around major local highs. That is, some risk assets start to break down and roll over (like European equities, Philly SOX etc – as outlined above); while others remain in an uptrend. If this is a market that's rolling over into a wave of risk aversion (as suggested by the SELL-off indicator amongst other factors) then all key risk assets will eventually get caught up in the downside.

As mentioned above (& yesterday), the **SELL-off indicator and other key medium-term indicators continue to signal a high probability of an imminent pullback.** The SELL-off indicator is now on +23 (FIG 1f); the medium term risk appetite scoring system remains on SELL (FIG 1g); while various put to call ratios and volatility indicators continue to flash red. Both the short and medium term put to call ratios, for example, are on/close to SELL (FIG 1d); the NDX100 put to call indicator is on SELL (FIG 1e); SKEW (a measure of professional BUYing of 'deep out of the money' put options) is elevated (FIG 1h); the level of outstanding single stock call options has returned to high levels (FIG 1c); while VIX futures are also signalling concern (i.e. behaving unusually – e.g. see breakdown of correlation of the steepness of the curve with the S&P500, FIG 1i).

Short term models, though, are now mixed. Risk appetite models have rolled over, with some reaching BUY levels (e.g. SHORTEST term RAG, FIG 2b). Technical models, in contrast, have moved higher in recent trading sessions with most now close to SELL (FIGs 2c – 2e).

Given emerging cracks in this uptrend, clear SELL signals from medium-term models, and a mixed message from the short-term models, we recommend closing out the LONG position (i.e. which is currently broadly flat on our entry price). With emerging cracks and growing signs of frothiness adding to the message of the SELL-off indicator (and other medium-term models), **risk reward favours starting to BUILD SHORT positions over the next few trading sessions**. We expect to start doing that over the course of this week (as discussed in Daily publications earlier this week).
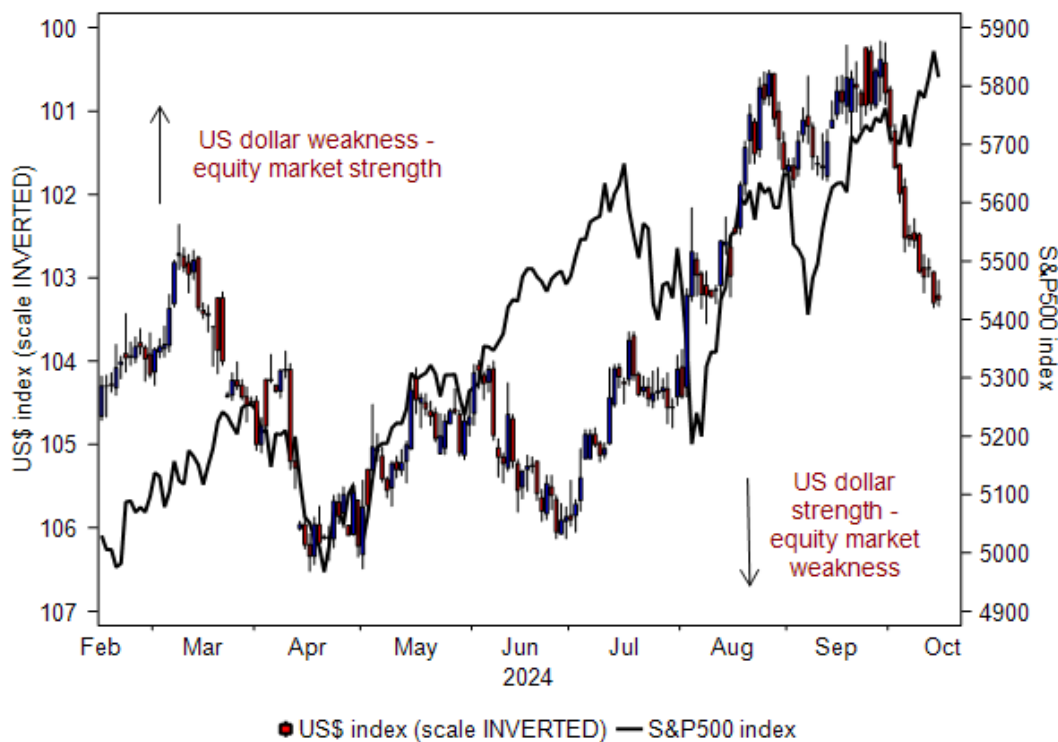
Kind regards,

The team @ Longview Economics

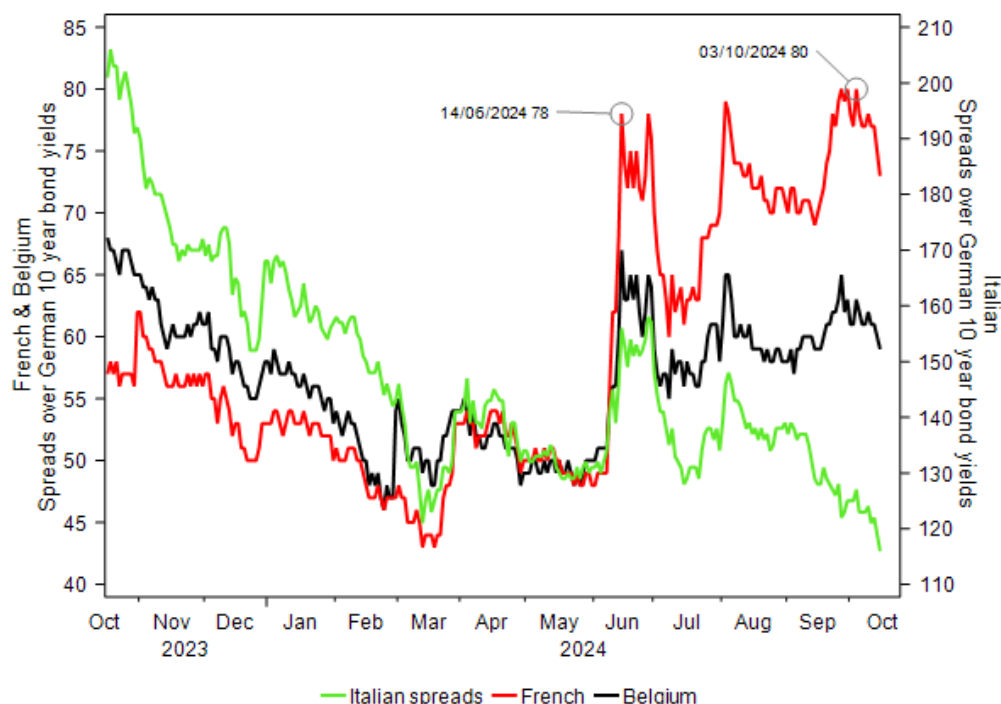**FIG 1:** European STOXX broad equity index with its key 50 day moving average

Source: Longview Economics, Macrobond
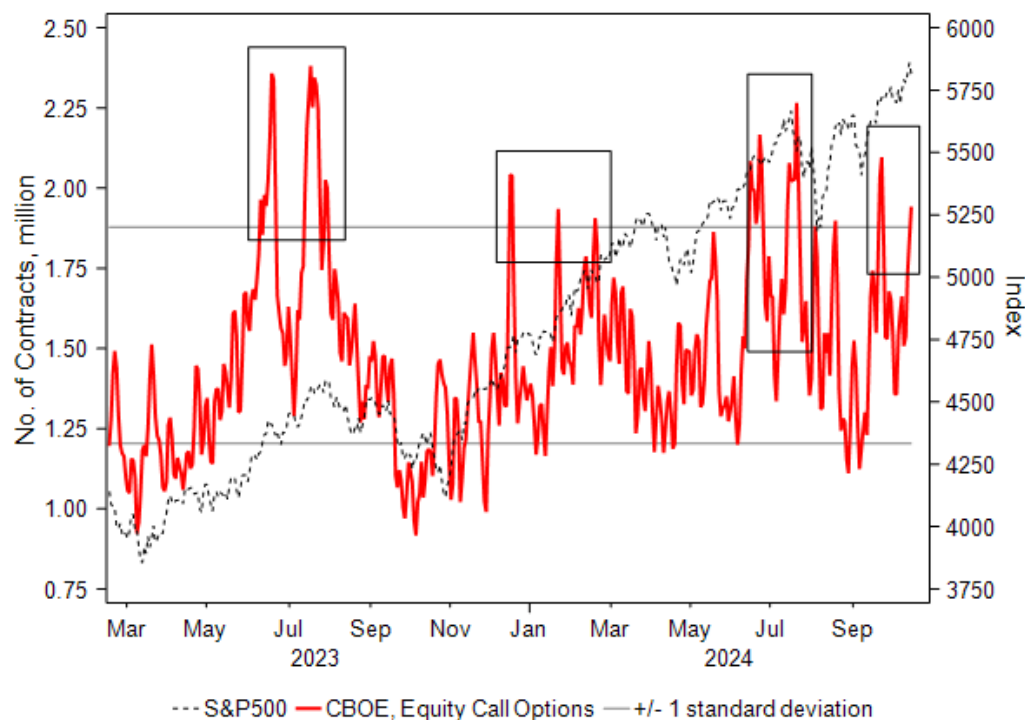
FIG 1a: US dollar index (scale INVERTED) vs. S&P500

Source: Longview Economics, Macrobond

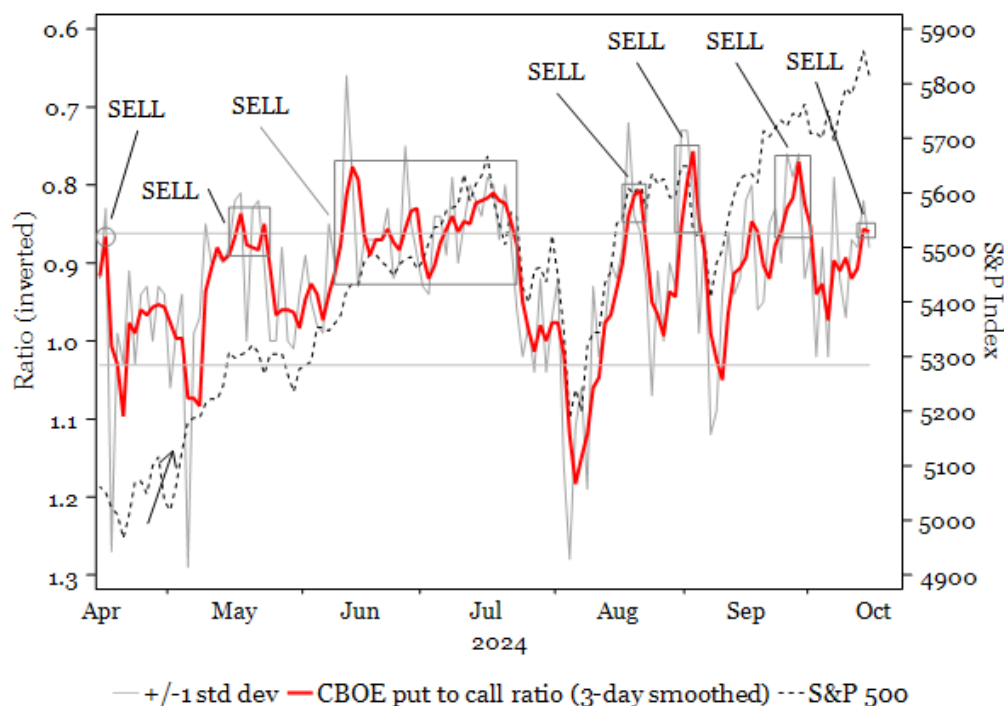**FIG 1b:** French, Italian & Belgium spreads over 10 year bunds (bps)

Source: Longview Economics, Macrobond

FIG 1c: Volume of outstanding CBOE 'single stock' call options (3 day smoothed) vs. S&P500
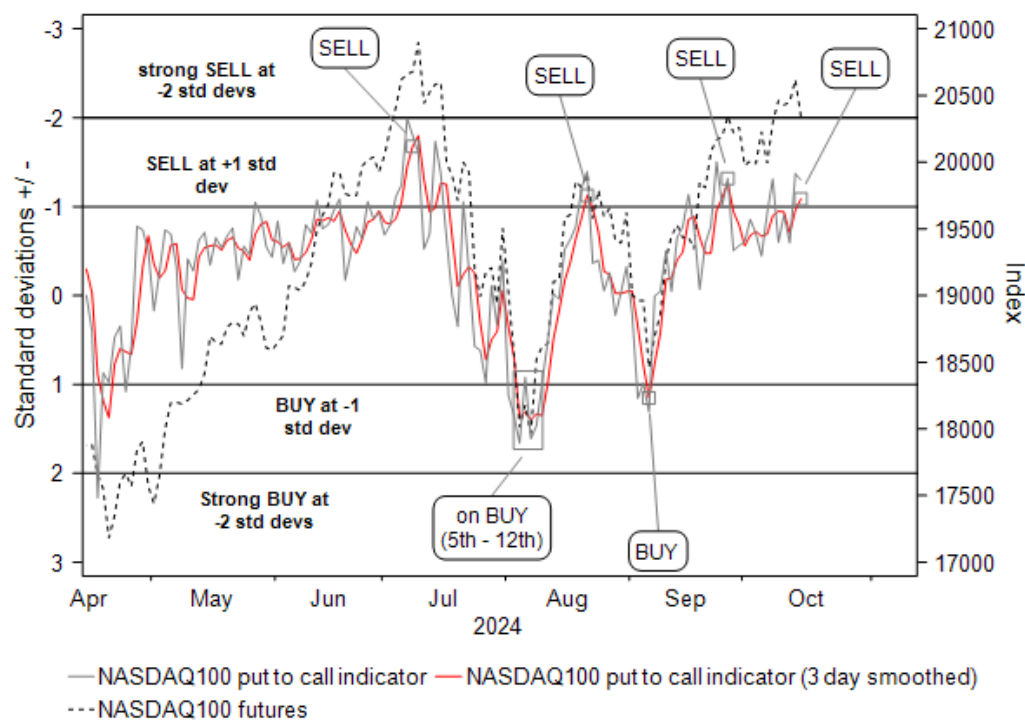

Source: Longview Economics, Macrobond

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

Source: Longview Economics, Macrobond

FIG 1e: NDX100 put to call indicator (1 & 3 day smoothed) vs. NDX100

Source: Longview Economics, Macrobond

FIG 1f: Longview SELL-off indicator vs. S&P500
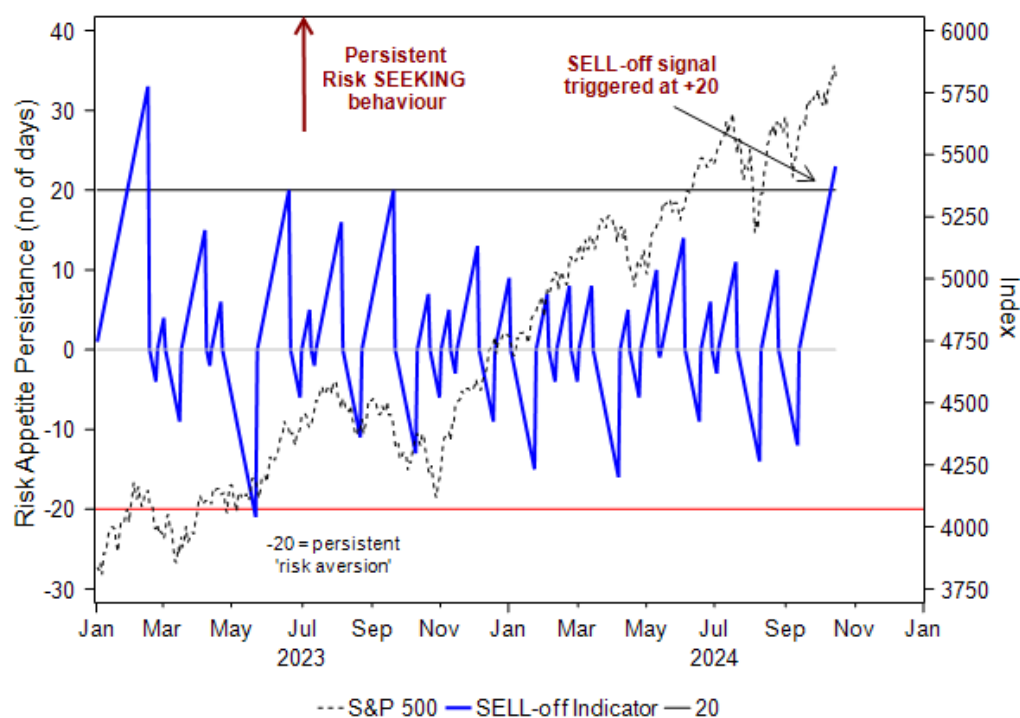
Source: Longview Economics, Macrobond

FIG 1g: Longview **medium term 'risk appetite'** scoring system vs. S&P500
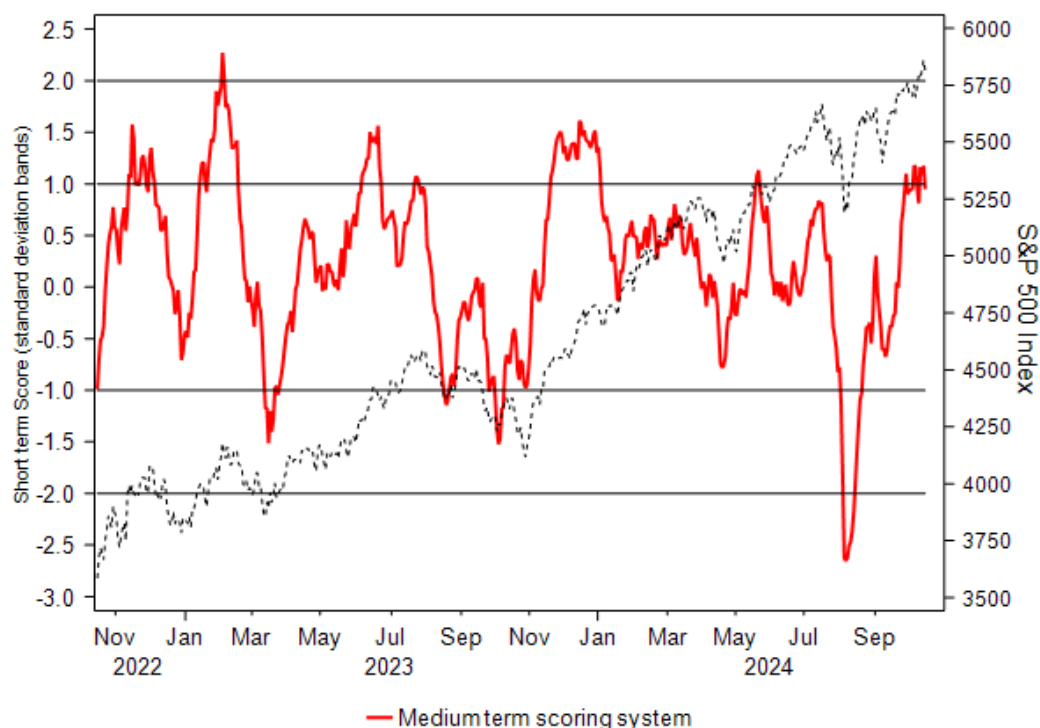
Source: Longview Economics, Macrobond

FIG 1h: US CBOE SKEW index vs. S&P500
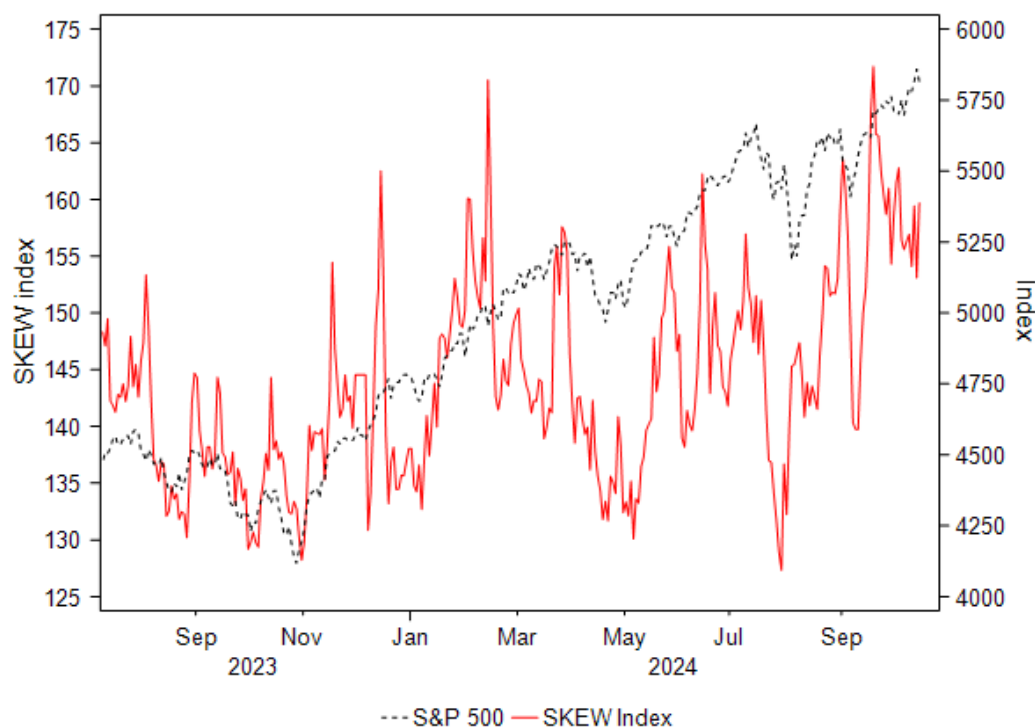
Source: Longview Economics, Macrobond

FIG 1i: Steepness of VIX curve (6 less 1 month futures) vs. S&P500
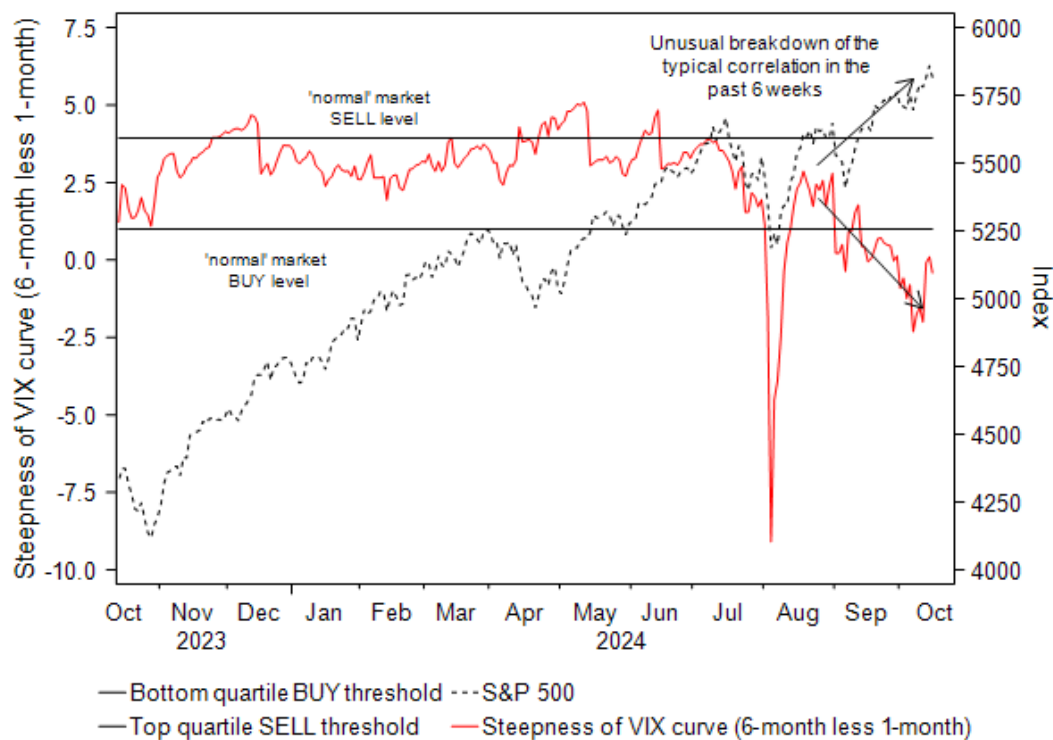
Source: Longview Economics, Macrobond

Short term market timing models are mixed......

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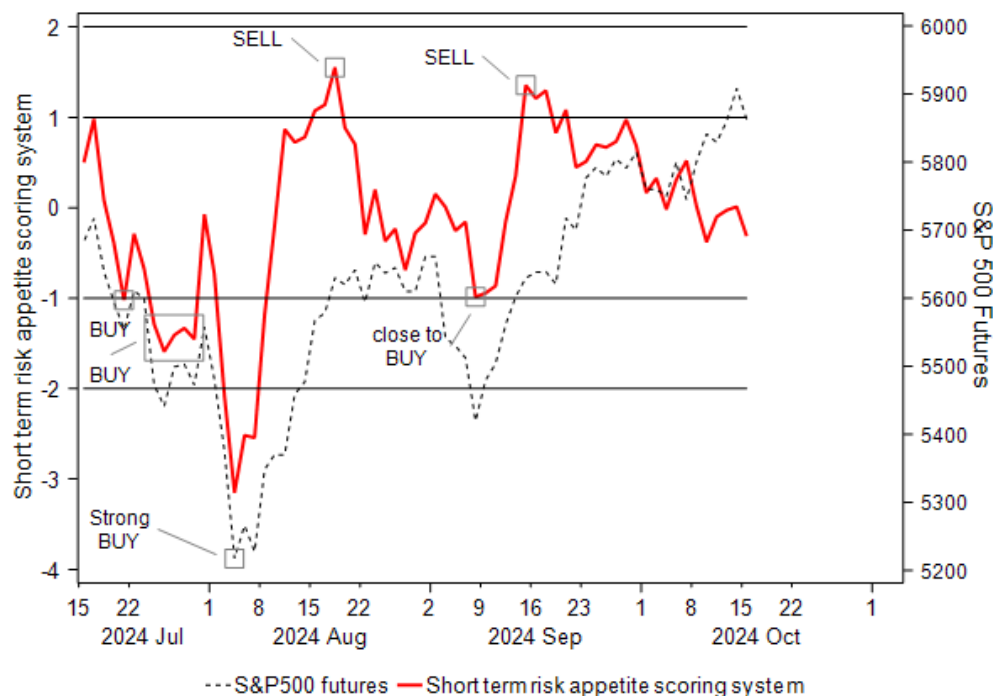
Source: Longview Economics, Macrobond

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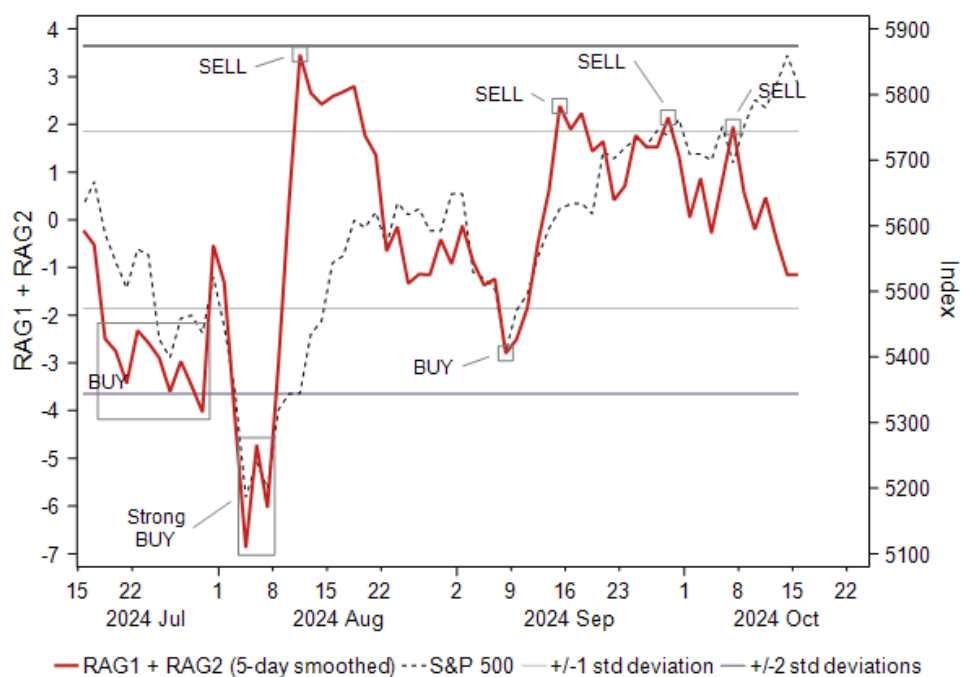
Source: Longview Economics, Macrobond

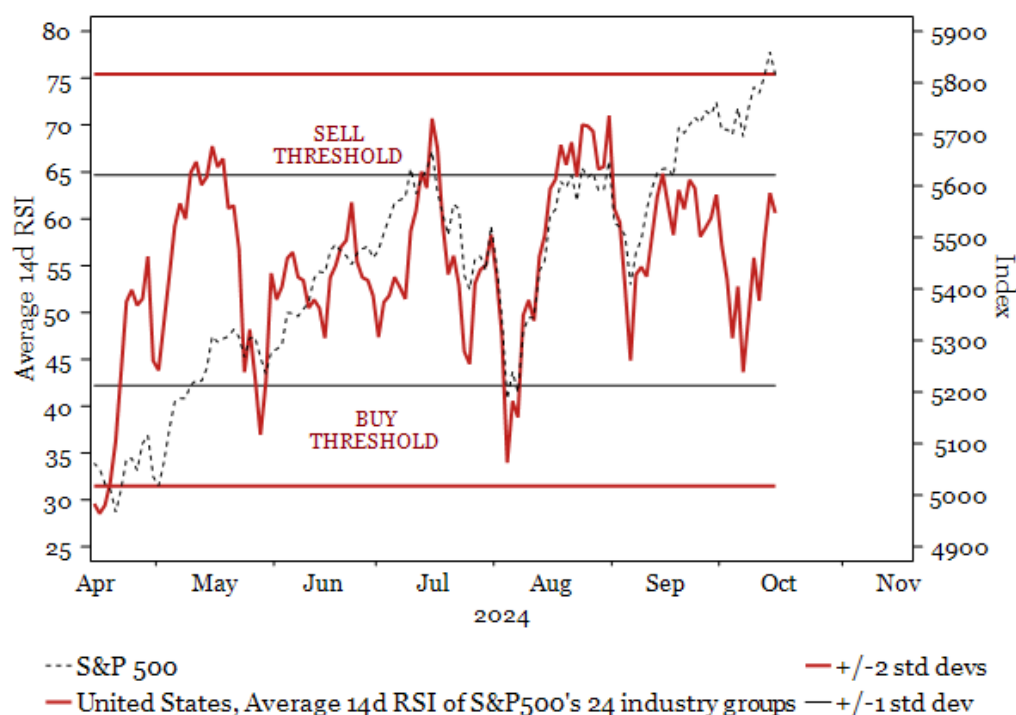**FIG 2b:** Longview **SHORTEST term** RAG1 vs. S&P500
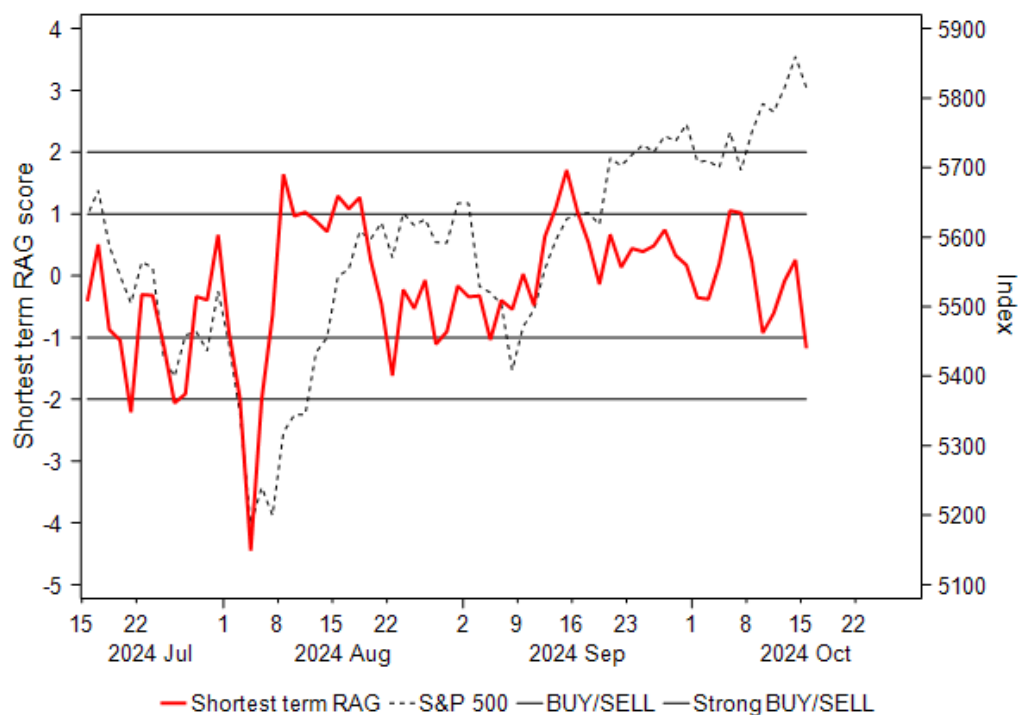
Source: Longview Economics, Macrobond

FIG 2c: Longview S&P500 short term **'technical'** scoring system vs. S&P500 futures
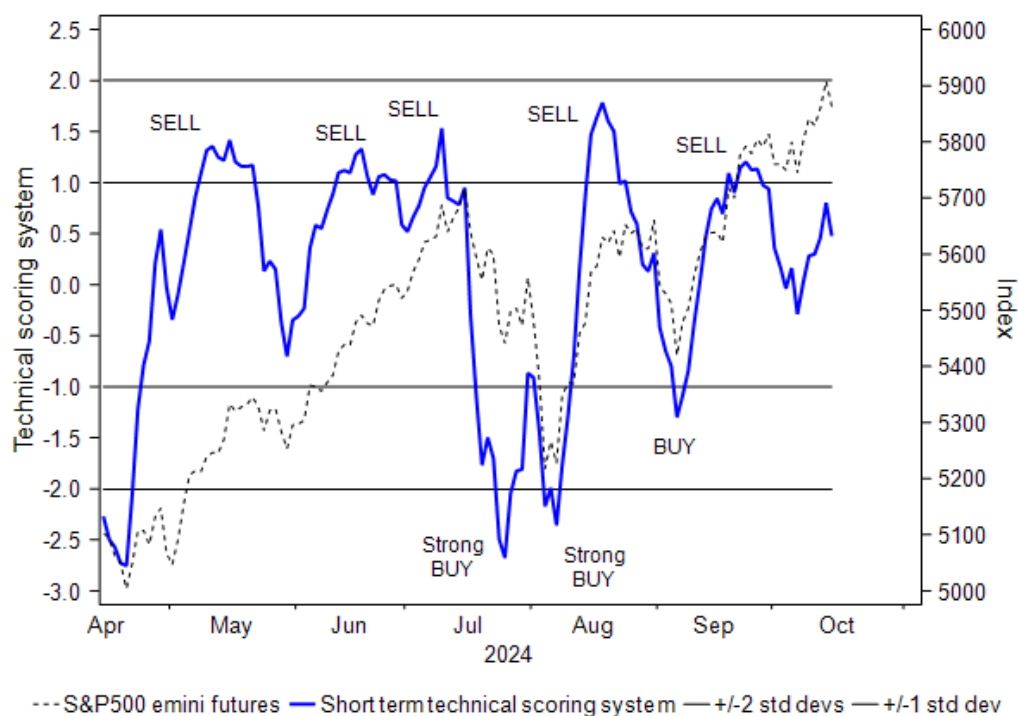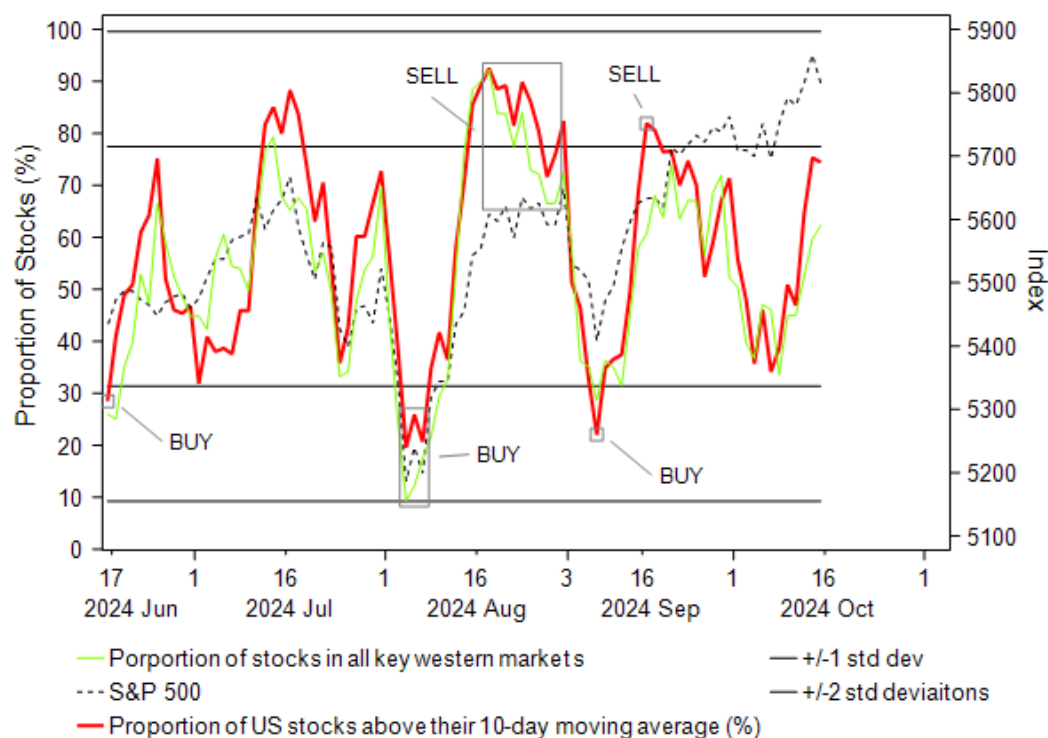

Source: Longview Economics, Macrobond

FIG 2d: Average short term 14d RSIs of US industry groups (i.e. all 24) vs. S&P500

--- S&P 500
— United States, Average 14d RSI of S&P500's 24 industry groups

— +/-2 std devs
— +/-1 std dev

Source: Longview Economics, Macrobond

FIG 2e: Proportion of US stocks above their 10 day moving average vs. S&P500

— Porportion of stocks in all key western markets
--- S&P 500
— Proportion of US stocks above their 10-day moving average (%)

— +/-1 std dev
— +/-2 deviaitons

Source: Longview Economics, Macrobond

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

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

FIG A: Longview short and medium term scoring systems vs. S&P500
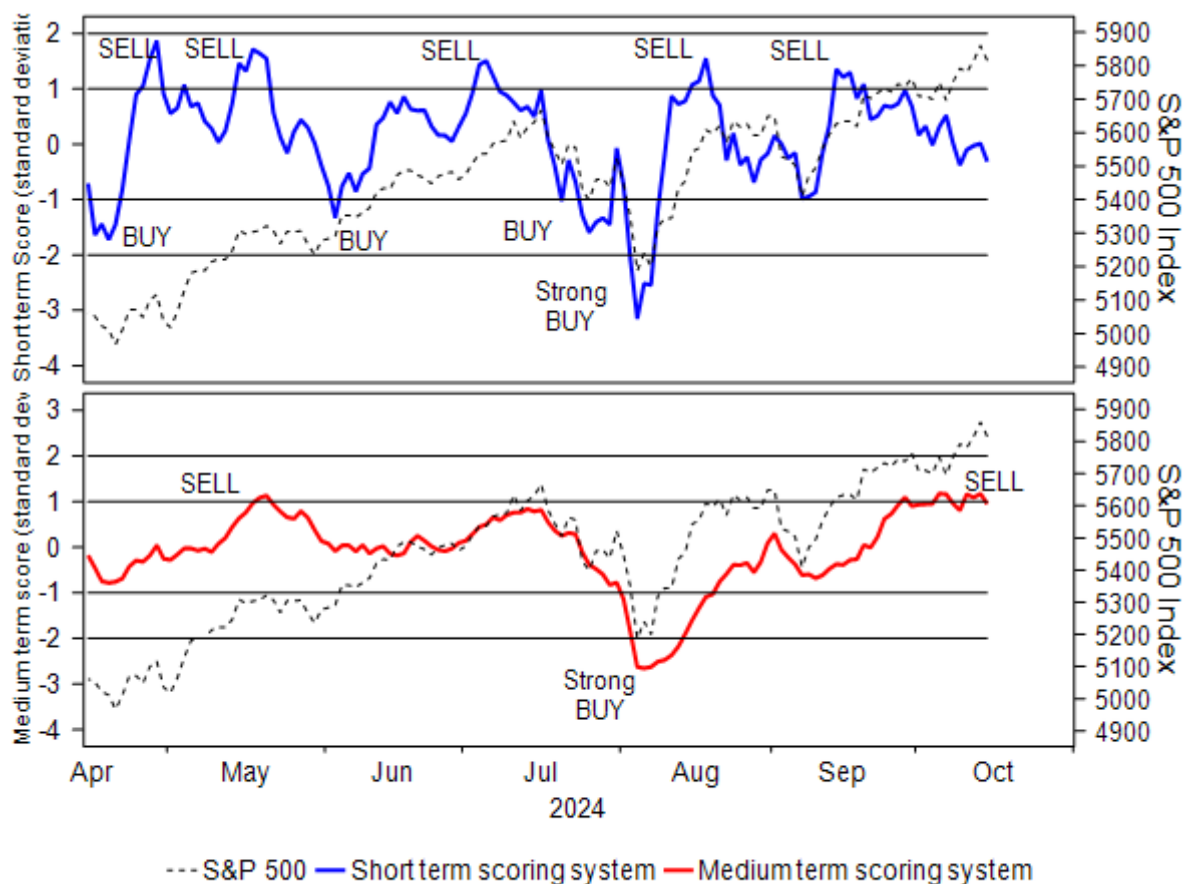
Source: Longview Economics, Macrobond

Key macro data/events

Key data today include: Australian Westpac leading index (Sept, 12:30am); Japanese machinery orders (Aug, 12:50am); **UK headline & core CPI**, RPI & PPI (Sept, 7am); UK Land Registry house prices (Aug, 9:30am); Italian headline & core CPI (Sept, 9am); Canadian housing starts (Sept, 1:15pm); US New York Fed services business activity (Oct, 1:30pm); US import & export prices (Sept, 1:30pm).

Key events today include: Speech by the BOJ's Adachi in Kagawa (2:30am).

Key earnings today include: **Abbott Labs**, **Morgan Stanley**, Prologis, Lam Research, U.S. Bancorp, CSX, Kinder Morgan, Crown Castle, Las Vegas Sands, Discover, Equifax, PPG Industries.

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 last week on 10th October 2024. If you are not on the distribution list and would like to receive these reports pls email info@longvieweconomics.com.

Longview Economics
@chriswatling
@LviewEconomics
Longview Economics
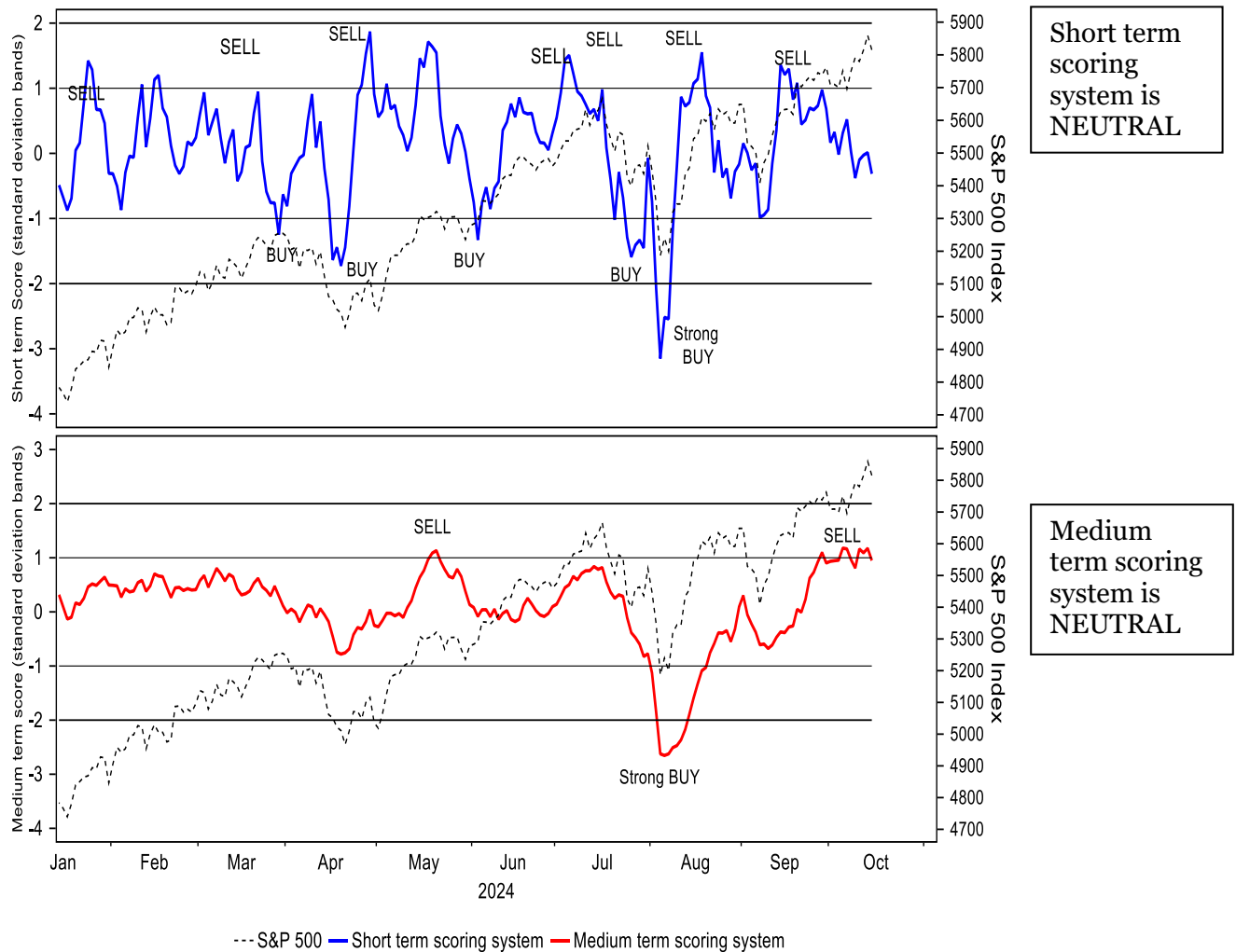Longview Economics
Longview Economics

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

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

| Short term scoring system is NEUTRAL |

| Medium term scoring system is NEUTRAL |

Source: Longview Economics, Macrobond

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

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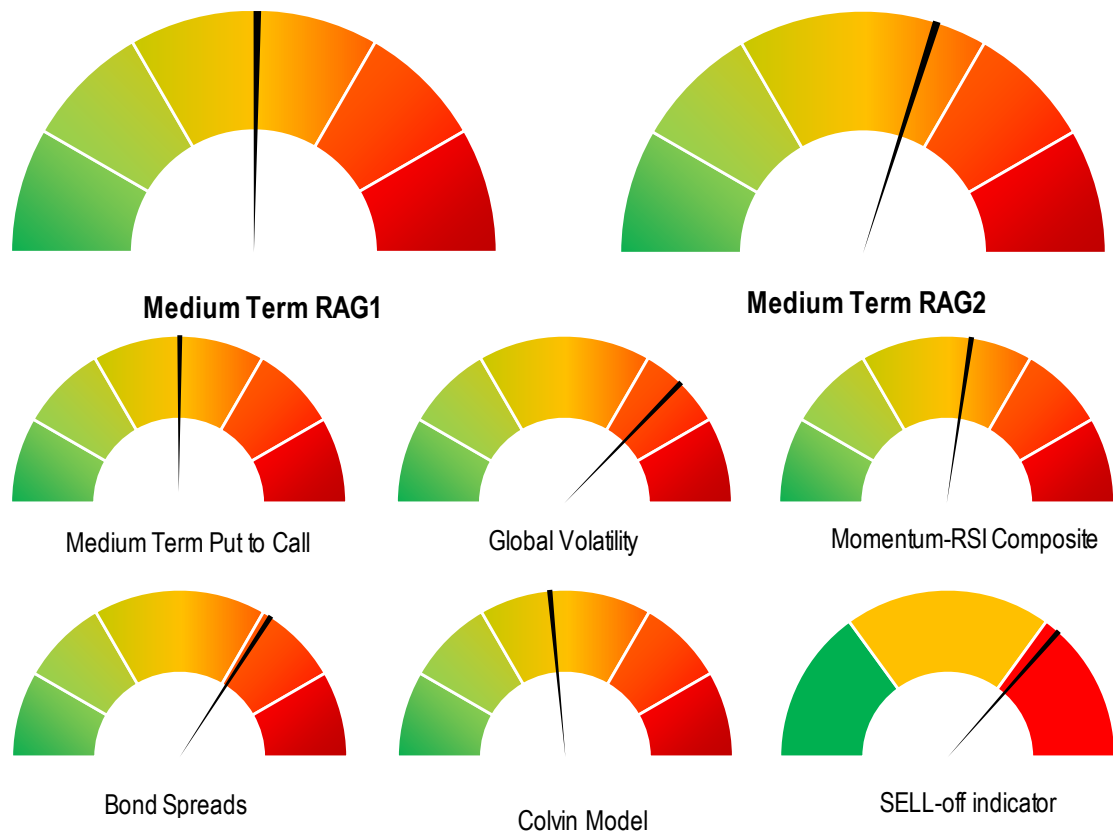***For explanations of indicators please see page 10***

Section 1a: Summary of indicator signals**

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

RAG1   RAG2

Shortest term RAG   Calls less Puts   Breadth
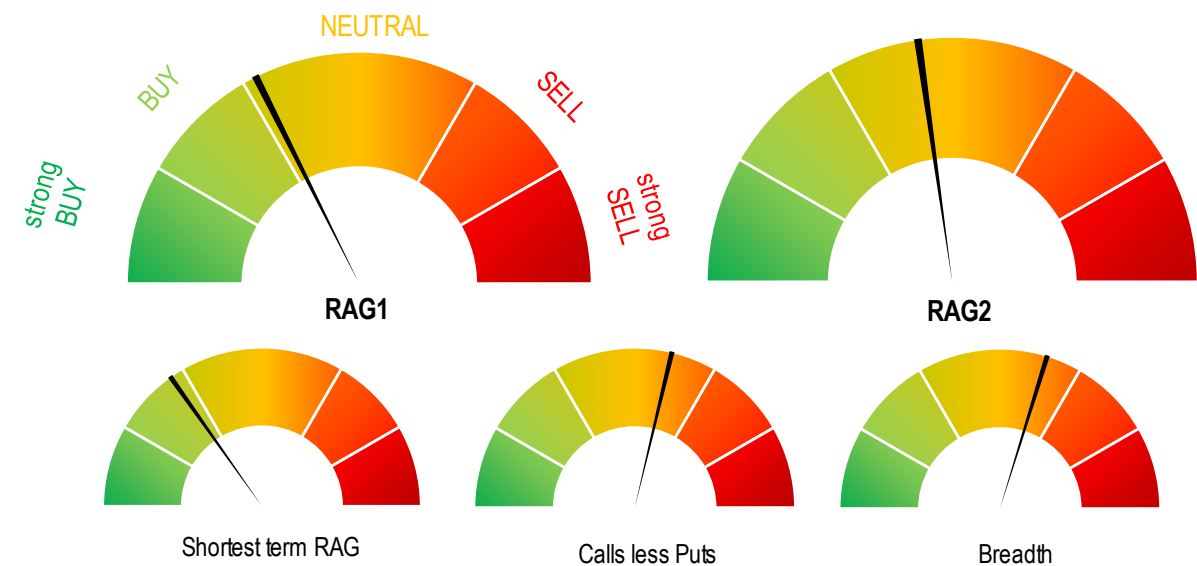
Source: Longview Economics

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

Medium Term RAG1   **Medium Term RAG2**

Medium Term Put to Call   Global Volatility   Momentum-RSI Composite

Bond Spreads   Colvin Model   SELL-off indicator

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

RAG1 is NEUTRAL

Source: Longview Economics, Macrobond

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

RAG2 is NEUTRAL

Source: Longview Economics, Macrobond
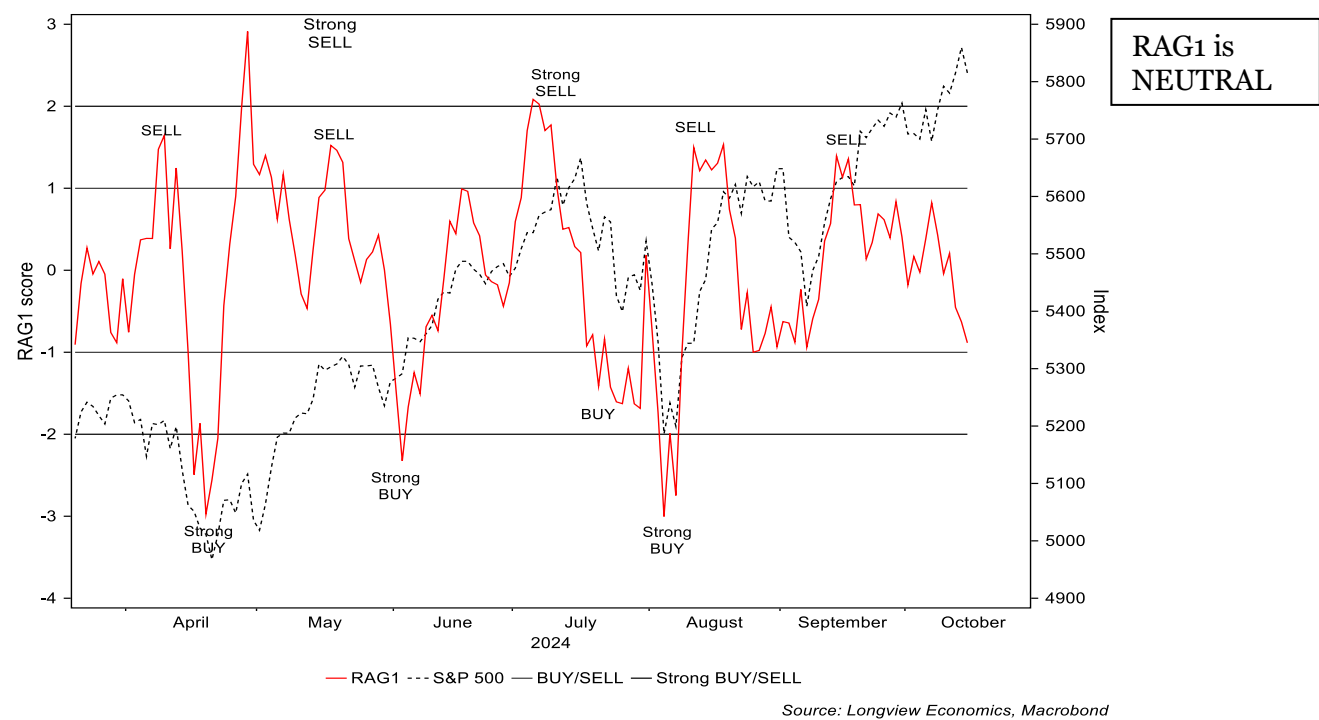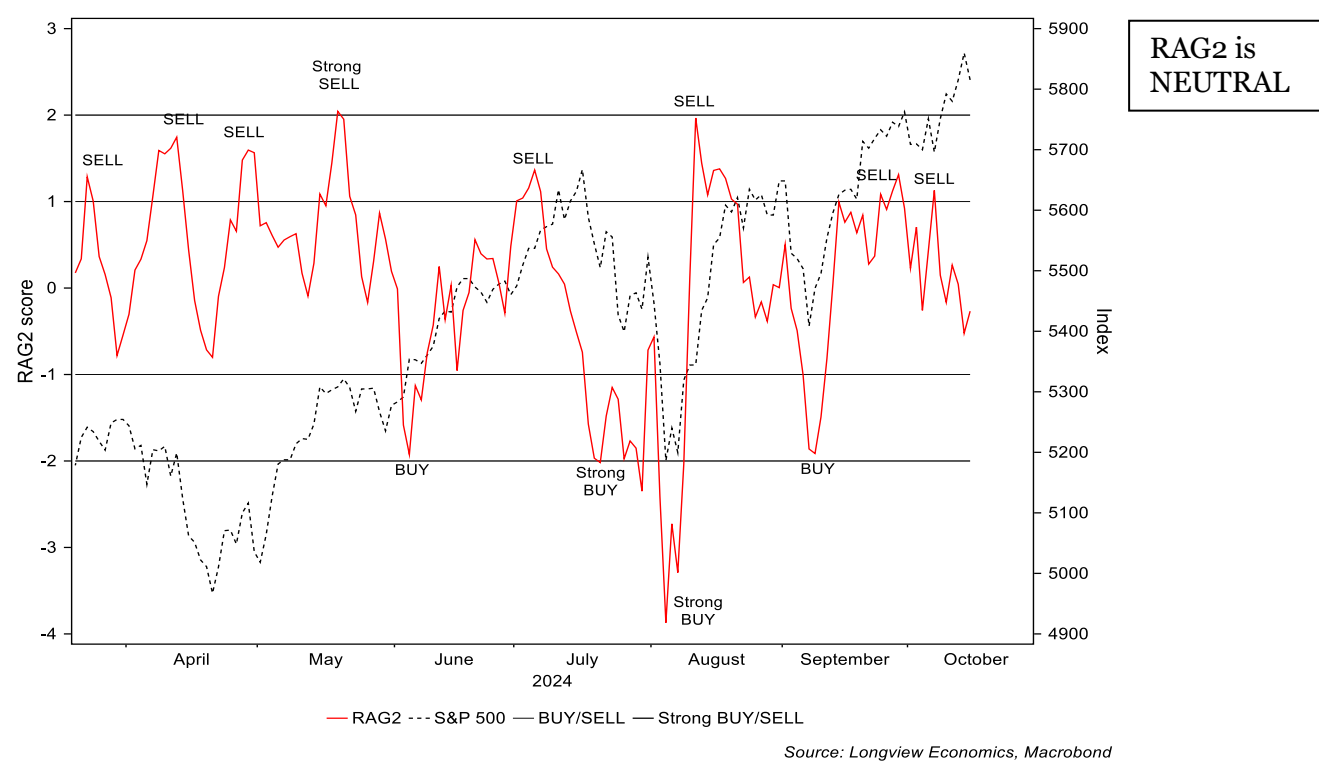
For explanations of indicators please see page 10

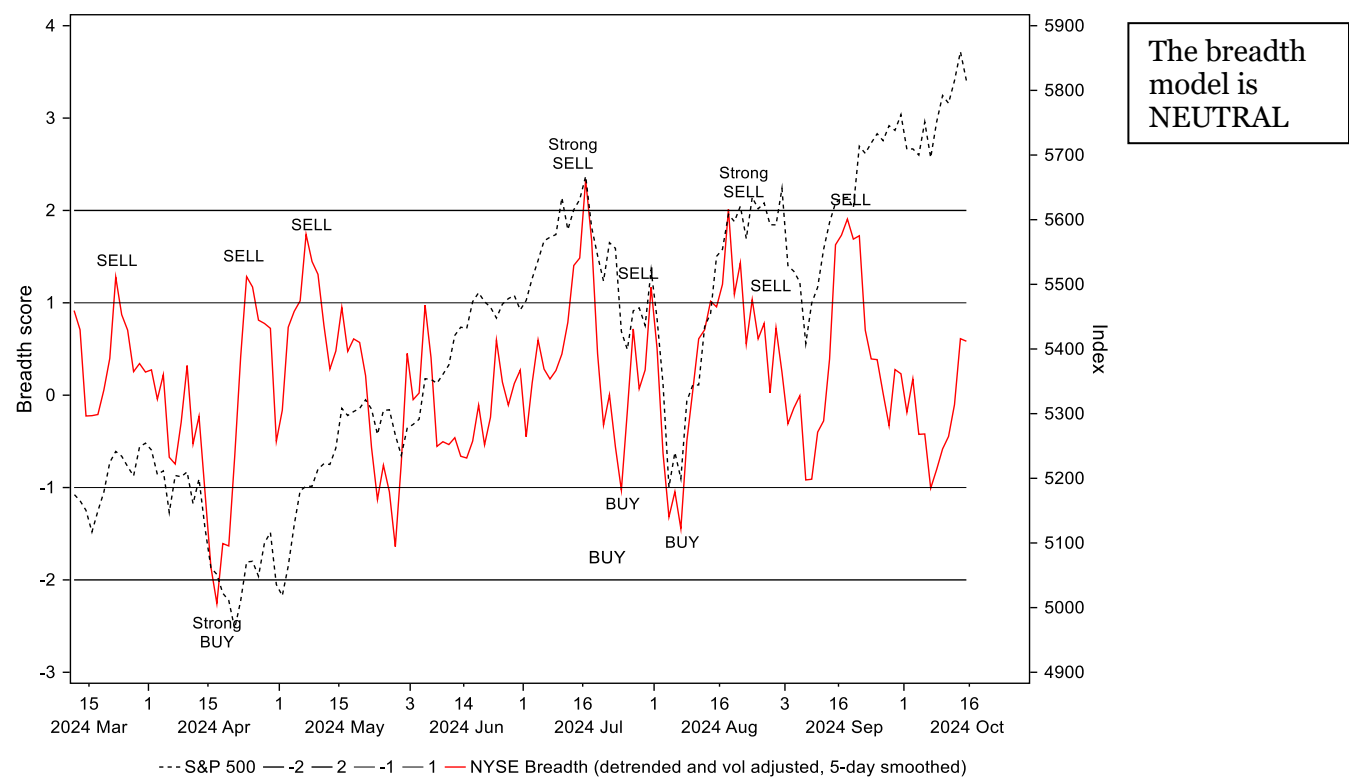**Fig 2c:** Shortest term RAG (i.e. using a 3 day moving average) vs. S&P 500

Shortest term RAG is on BUY

Shortest term RAG --- S&P 500 —— BUY/SELL —— Strong BUY/SELL

Source: Longview Economics, Macrobond
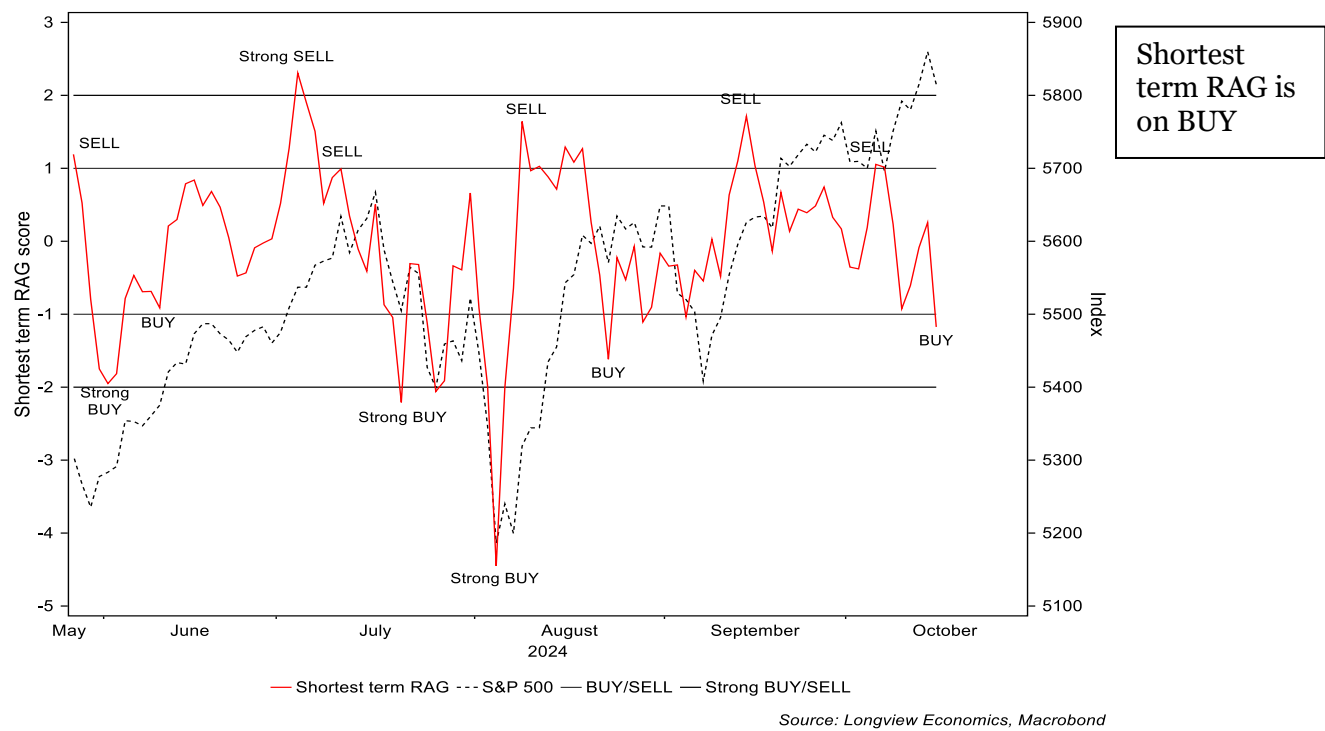
Fig 2d: CBOE calls less puts (5 day moving average) vs. S&P500

Calls less puts model is NEUTRAL

—— 2 —— -2 —— -1 —— 1 --- S&P 500 —— Calls less puts model

Source: Longview Economics, Macrobond
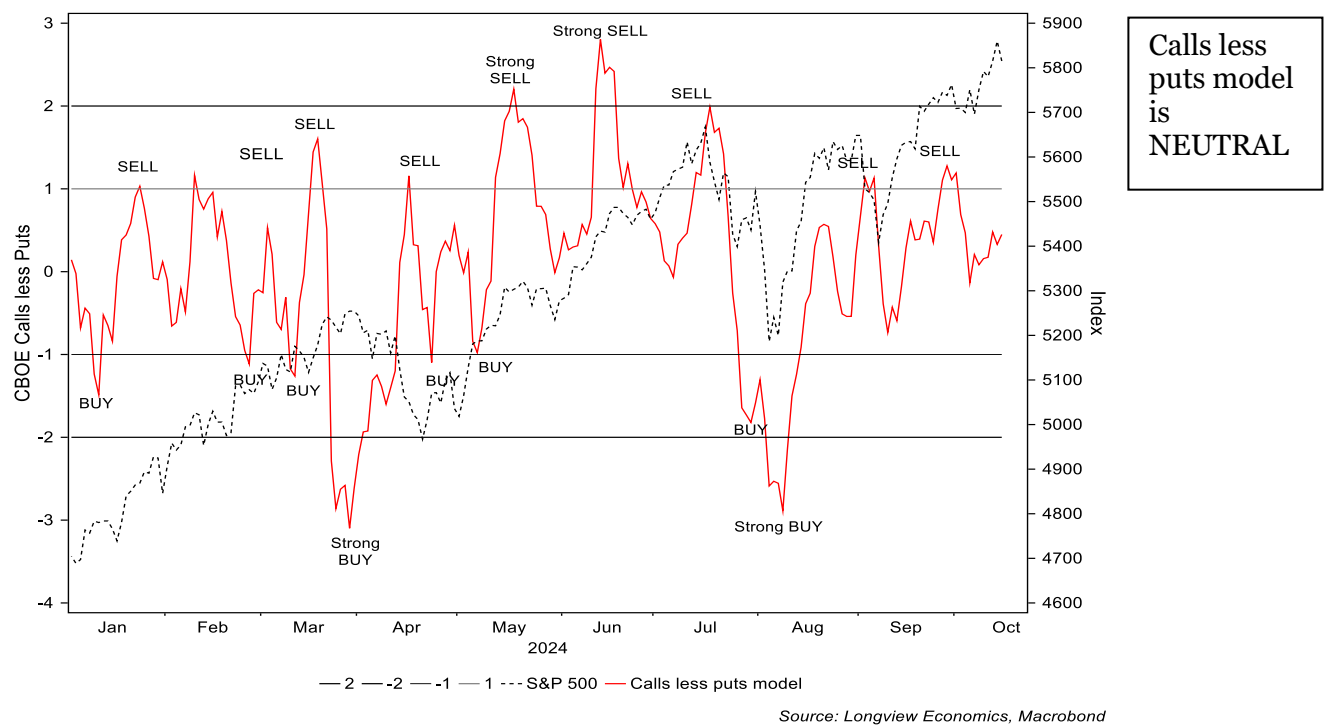
For explanations of indicators please see page 10

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

The breadth model is NEUTRAL

--- S&P 500 — -2 — 2 — -1 — 1 — NYSE Breadth (detrended and vol adjusted, 5-day smoothed)

Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

Section 3: Medium term (1 – 2 month) outlook

Fig 3a: Medium term RAG1 (1 – 2 month view) vs. S&P 500
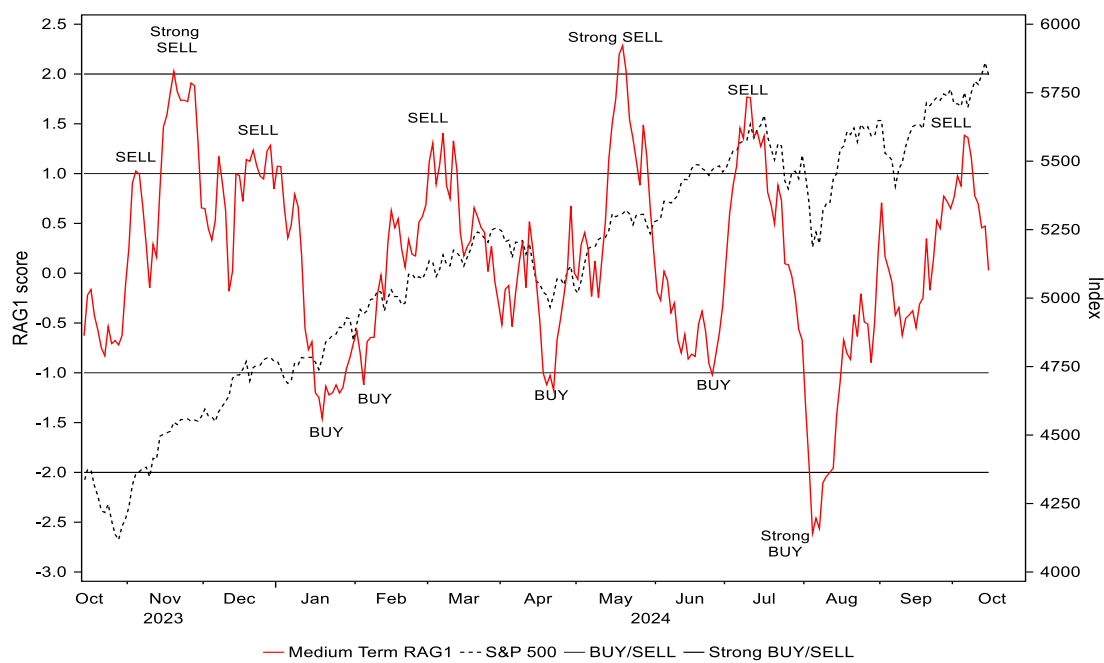
Medium term RAG1 is NEUTRAL

Source: Longview Economics, Macrobond

Fig 3b: Medium term RAG2 (1 – 2 month view) vs. S&P 500
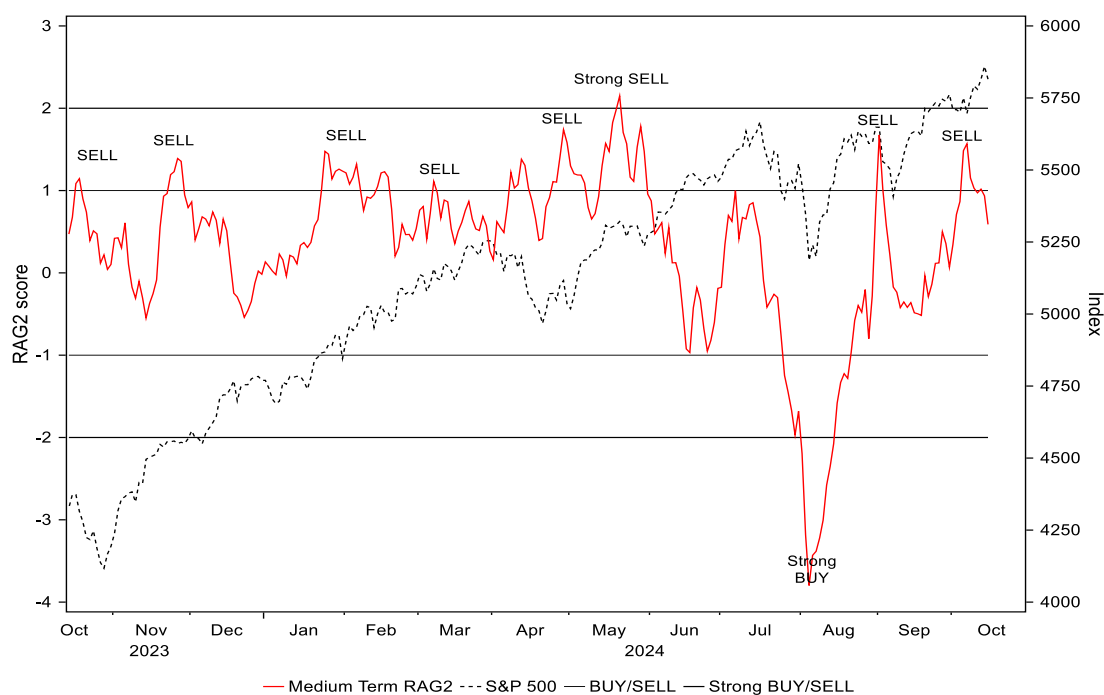
Medium term RAG2 is NEUTRAL

Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

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

The SELL-off indicator is on SELL

Source: Longview Economics, Macrobond
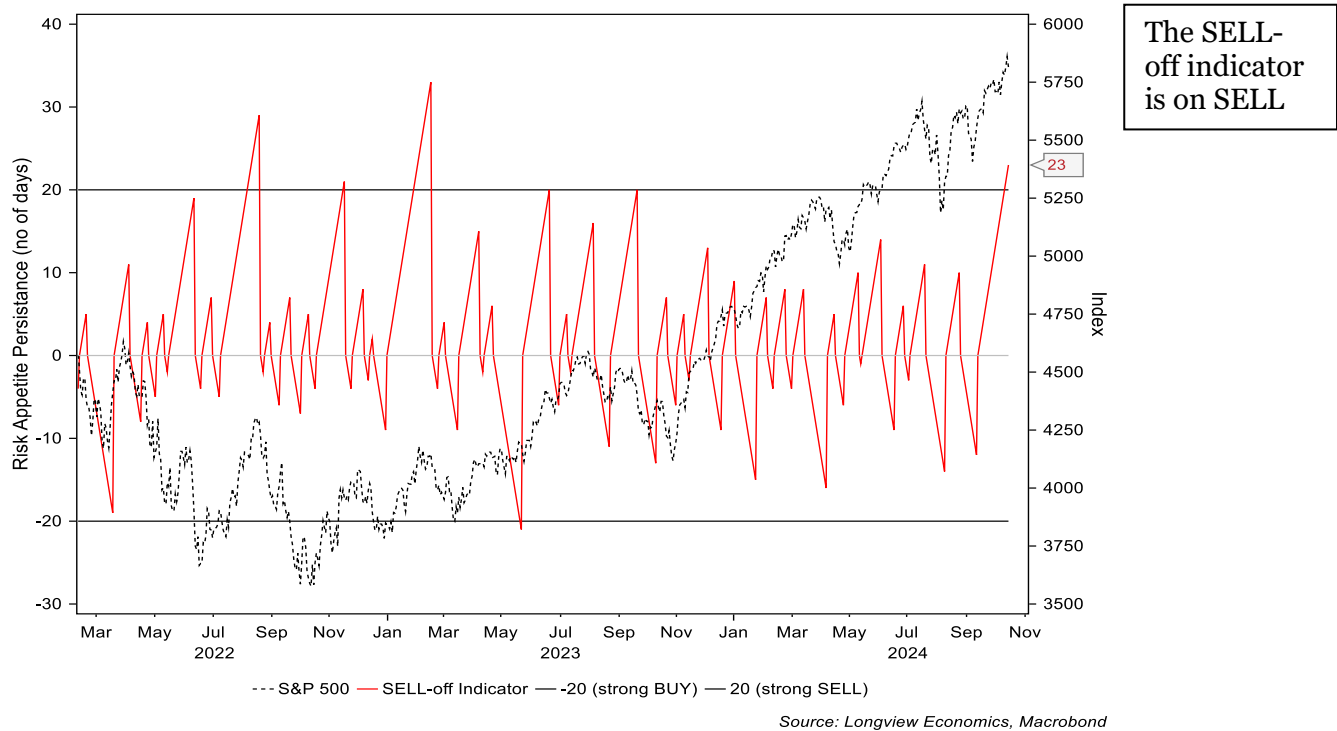
Fig 3d: CBOE put to call trend deviation model vs. S&P500

Medium term put to call model is NEUTRAL

Source: Longview Economics, Macrobond
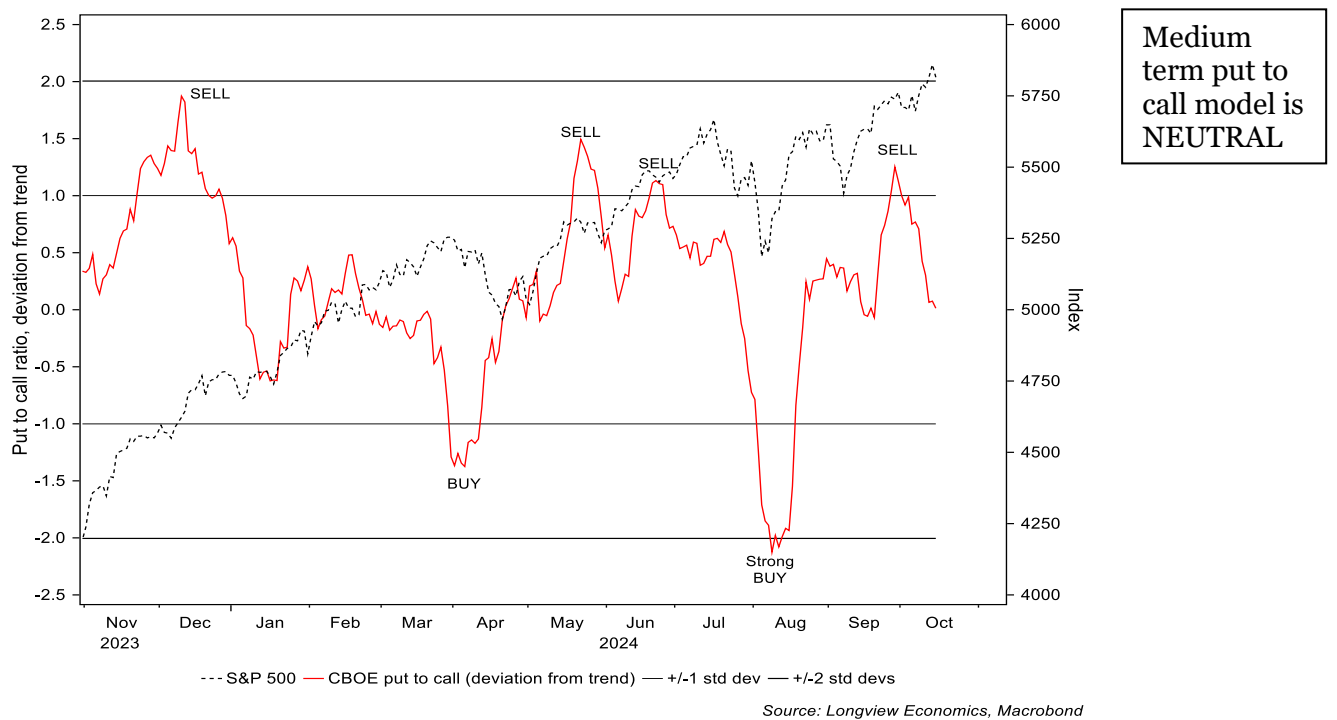
For explanations of indicators please see page 10

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

Global volatility indicator is on SELL

Source: Longview Economics, Macrobond
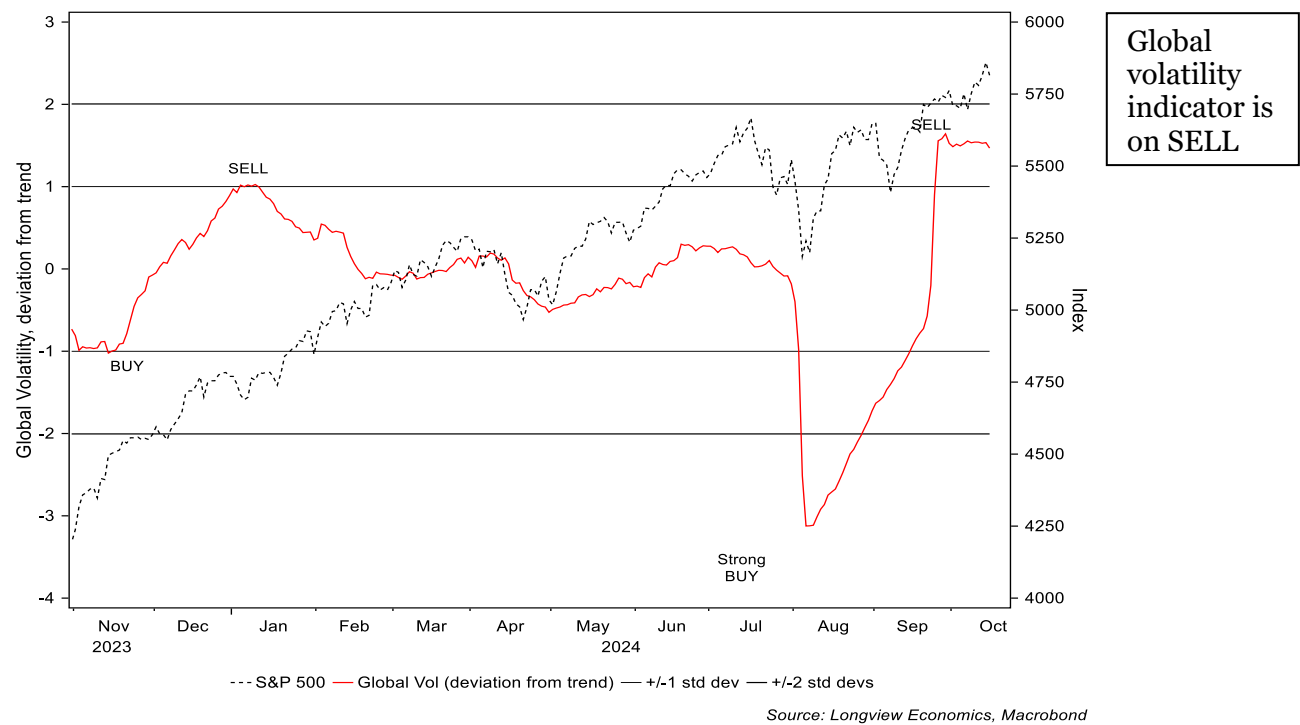
Fig 3f: Longview Momentum-RSI composite model vs. S&P 500
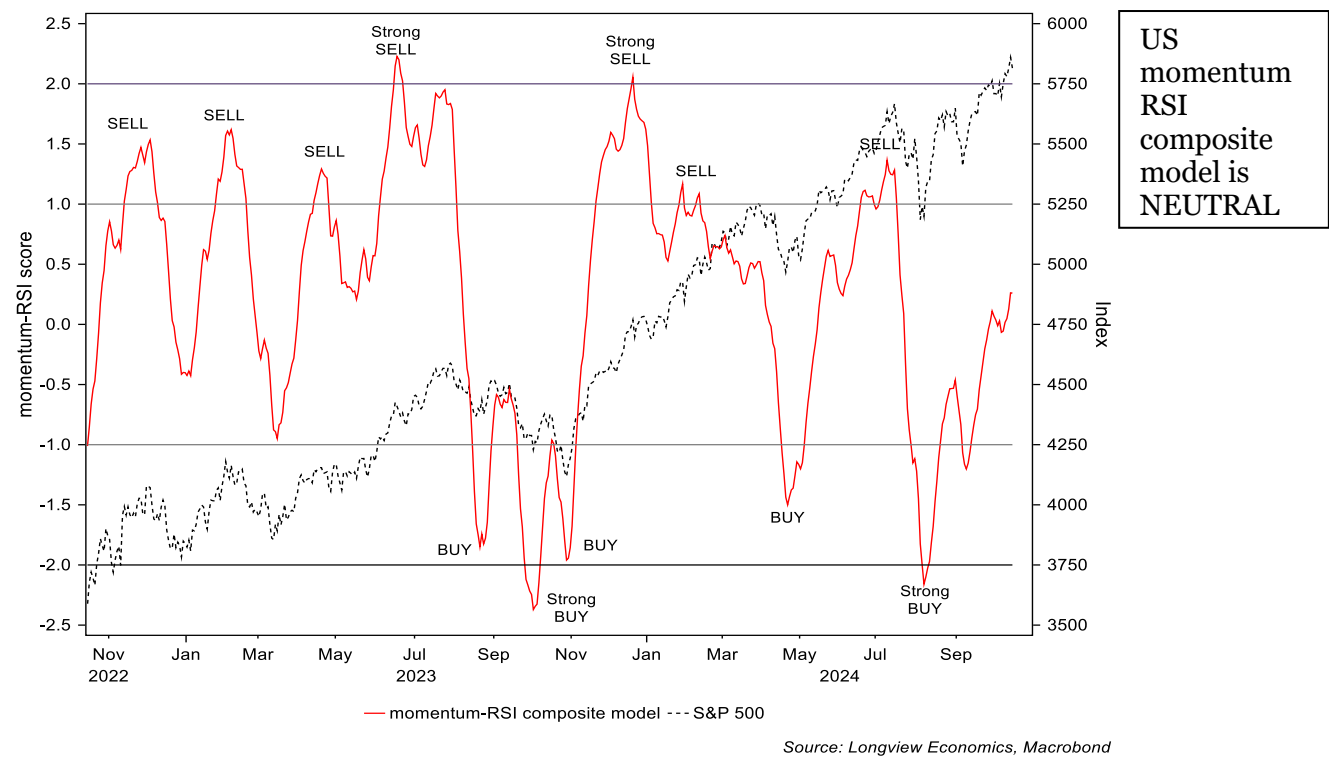
US momentum RSI composite model is NEUTRAL

Source: Longview Economics, Macrobond

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

--- S&P 500   —— Bond Spread (deviation from trend)   —— +/-1 std dev   —— +/-2 std devs

Source: Longview Economics, Macrobond

High yield corporate bond spreads model is on SELL
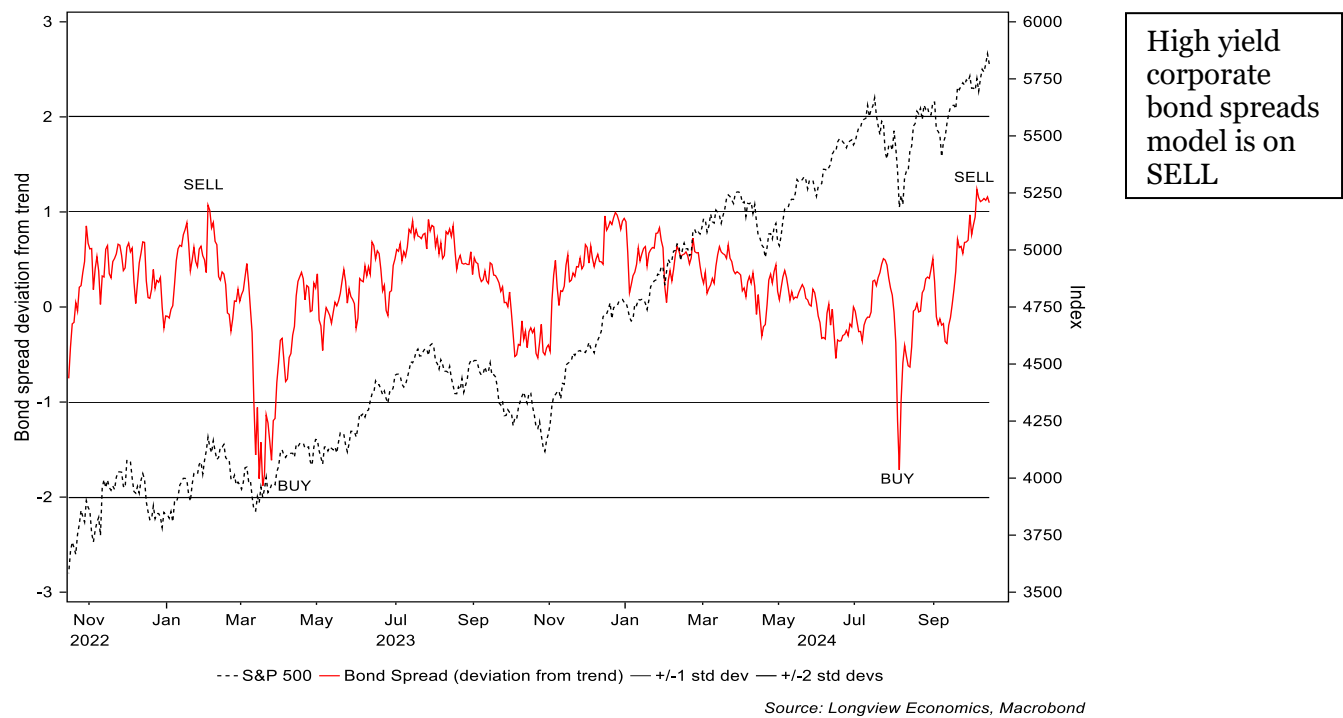
Fig 3h: Colvin model (deviation from trend) vs. S&P500

--- S&P 500   —— Colvin model (deviation from trend)   —— +/-1 std dev   —— +/-2 std devs

Source: Longview Economics, Macrobond

Colvin model – is Neutral
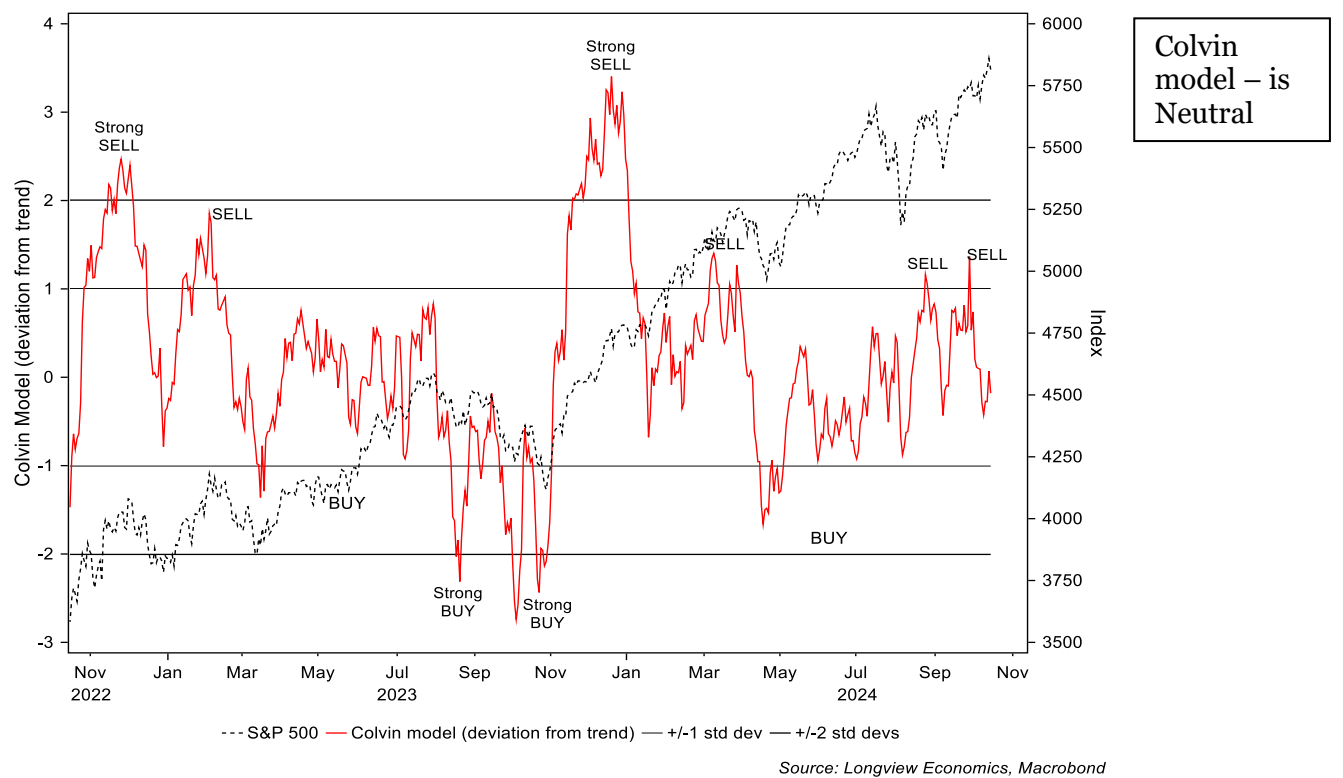
For explanations of indicators please see page 10

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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