Equity Index Futures Trading Recommendations

21st October 2024

"BUILD SPX SHORT positions (on strength)"

Email: info@longvieweconomics.com

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

- Move ¼ SHORT S&P500 December futures on strength, i.e. at 5,918.00;
- Increase to ½ on further strength (i.e. 2% above that level at 6,036.00);
- Place stop loss 3% above combined entry (at 6,156.50).

Rationale

The market pushed higher again last week, with further gains in major US equity indices, as well as certain other assets like gold (+2.4%), silver (+3.0%) and Bitcoin (+9.8%).

The general sense in markets is that those moves reflect Trump's recent momentum in the polls (with betting odds moving meaningfully in his favour in the last few weeks). Yesterday's update from 'FiveThirtyEight', for example, has Trump winning 53 times out of 100 (with Harris winning 47 times out of 100). Equally, Nate silver (Silver Bulletin) also switched, at the end of last week, to favour a Trump win. With that, we've seen strength in various cyclical ('Trump trade') assets like financials (and others, e.g. crypto), which are expected to benefit from more business deregulation, more fiscal stimulus, and generally more stock market friendly policies (i.e. compared to a Harris Presidency).

Some assets, though, are acting in a contrary manner (to that thesis). The US dollar, for example, has been strong recently (with the DXY up 4% since late September). The Trump policy intention, though, is to weaken the dollar to boost exports. Equally the rates market has been broadly stable since early/mid October, despite the inflationary impact of Trump's fiscal and trade tariff polices. Elsewhere, oil service stocks have fallen over the past fortnight.

To some degree, recent equity market strength is explained by stronger than expected earnings (albeit we are still early in the season). Of the 72 S&P500 companies that have reported, 55 of them have surprised to the upside (76%), on average by 6.2% (i.e. by more than the typical 4% earnings season 'surprise'). That's likely to have somewhat underpinned the market in the near term.

In our view, though, a more compelling explanation of recent market strength is the one laid out in last week's Longview on Friday:

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"…since early August there has been an ongoing asset allocation switch -> out of government bonds and into equities, with that **switch triggered by technical factors.** Specifically that bonds were overbought in August and equities (after the initial August pullback) were oversold.

Those factors are readily evident from simple technical models – e.g. see figs 8 & 9 in the appendix.

Critically, though, **they have now reversed**. That is, bonds are oversold (following on from the back-up in yields since mid-September); whilst equities are overextended to the upside…"

Source: Longview on Friday, published 18th October 2024: "Signs of Market Exuberance PLUS Where Have all the Fiscal Hawks Gone?"

That's consistent with the message of our medium term models, which (continue to) **generate a clear SELL message**. In particular, our SELL-off indicator is now on a reading of +26. It's therefore warning of a wave of risk aversion in global markets (see FIG 1); downside hedging in portfolios is low (FIG 3); the outstanding volume of single stock call options is high (FIG 1a) and, as such, near term complacency in markets is elevated. Elsewhere sentiment is bullish (a contrarian SELL signal, FIG 1c) and our medium term risk appetite scoring system is on SELL (FIG 1b).

Short term models, as highlighted on Friday, are more mixed. That is, some are on/approaching SELL levels (e.g. see the short term VIX RSI, which is now close to its SELL threshold, FIG 1f). Others are neutral/mid-range (albeit mostly with a SELL bias – see FIGs 2 – 2e).

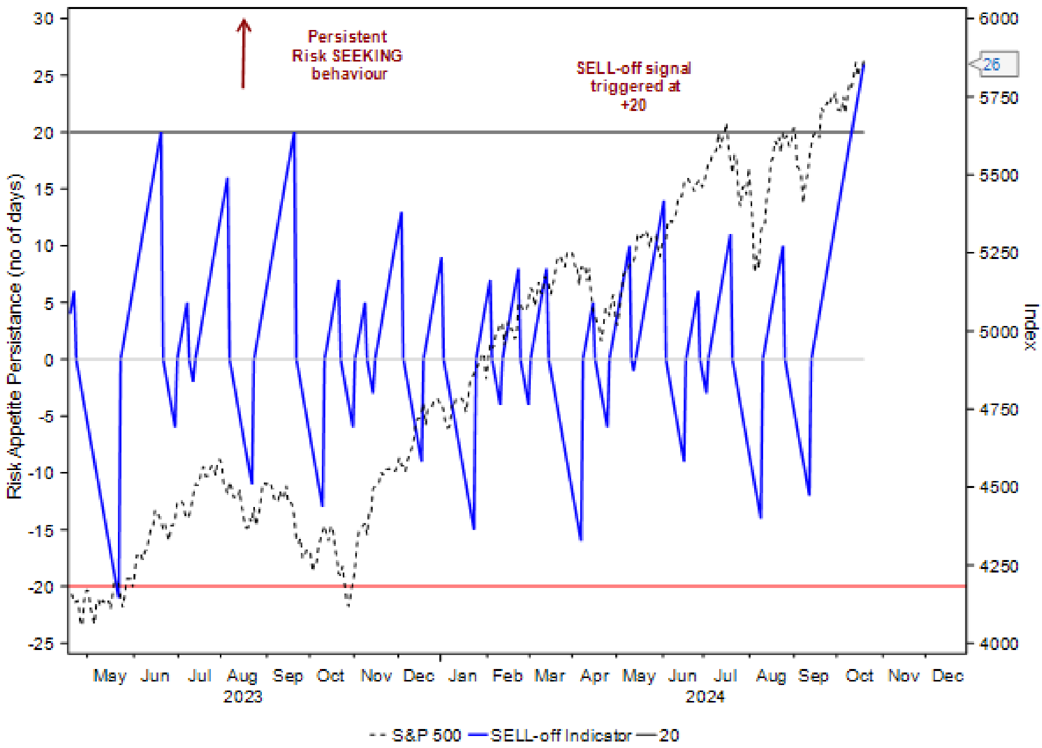
Overall, the case for a pullback in equities/risk assets is building, given the clear SELL message from the medium term models. As such, and with short term models giving a mixed message, the risk reward favours looking to build SHORT positions on strength (if forthcoming – please see above for detailed recommendation).

Risks, as always, are multiple and include the possibility that US equities continue to squeeze higher into the election. History, though, suggests that's unlikely (i.e. with equity market volatility usually picking up into election days). Please see below for a summary of today's macro data, key events, and earnings reports.

Kind regards,

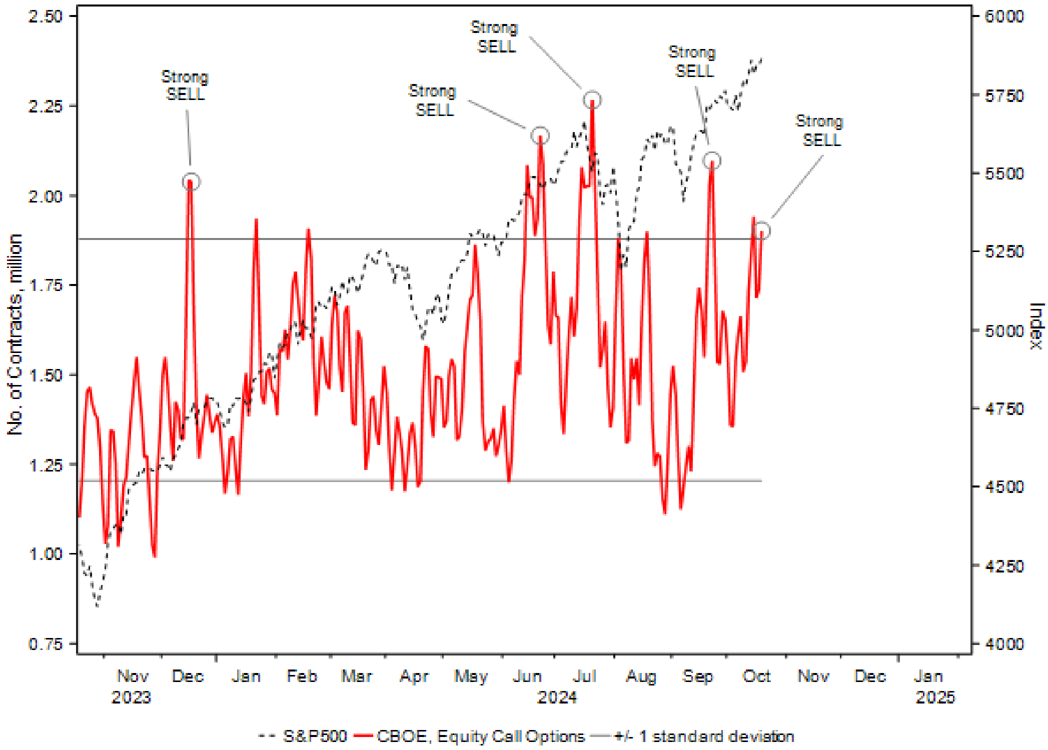
The team @ Longview Economics

FIG 1: Longview SELL-off indicator vs. S&P500



Source: Longview Economics, Macrobond

FIG 1a: US CBOE single stock call options (no. of contracts, smoothed) vs. S&P500



Source: Longview Economics, Macrobond

FIG 1b: Longview **medium term 'risk appetite'** scoring system vs. S&P500

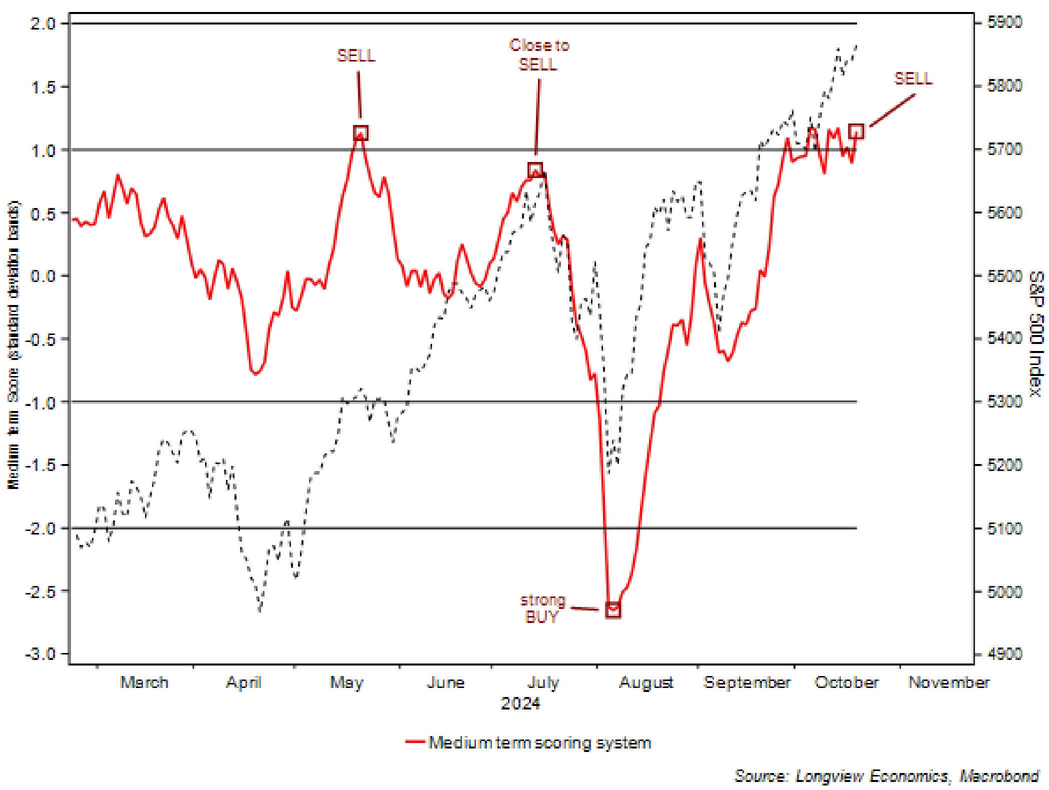


FIG 1c: Hulbert NASDAQ sentiment index shown with NASDAQ composite index

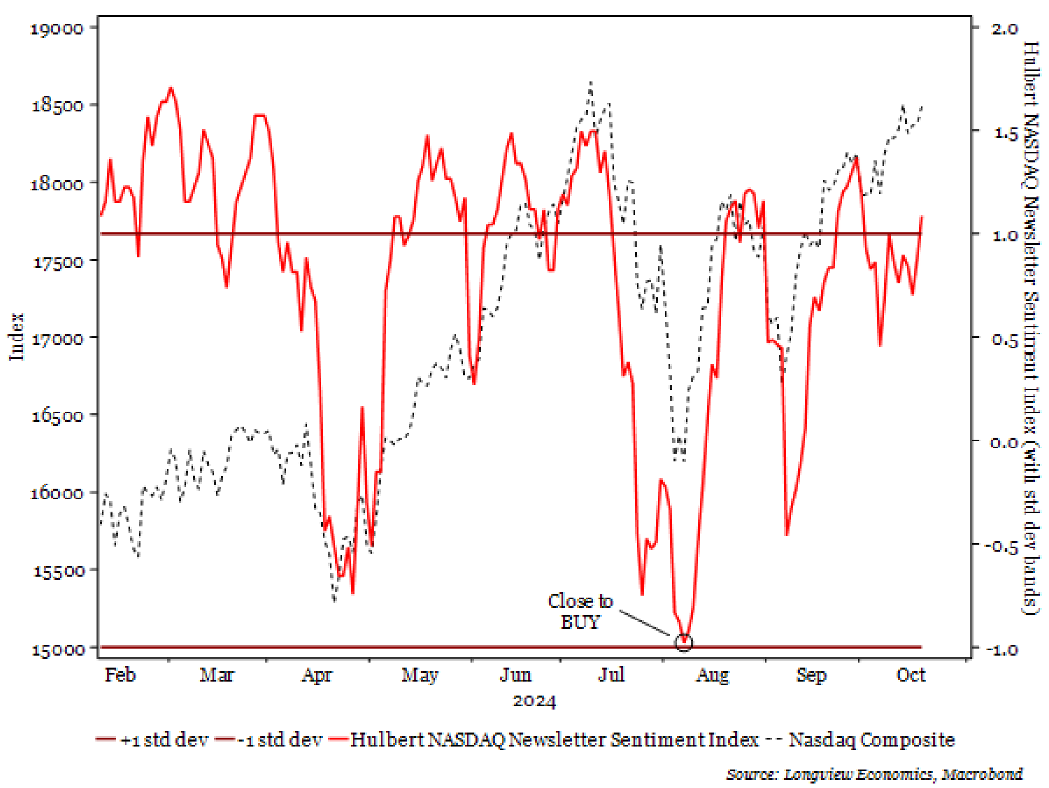
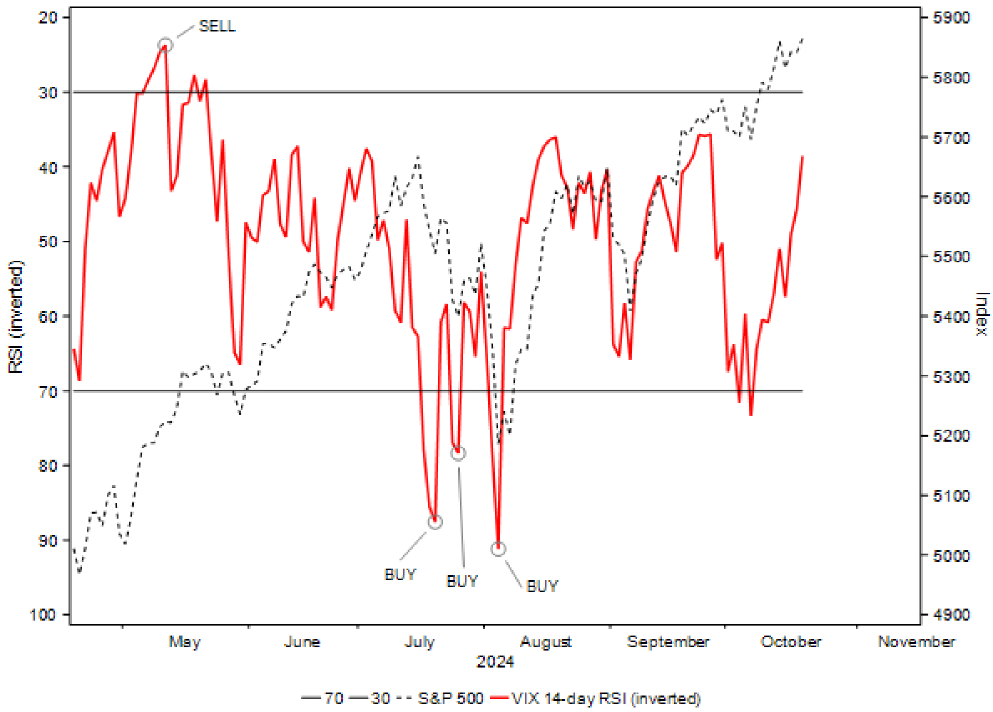


FIG 1d: S&P500 futures 10-day tick chart shown with overnight price action

FIG 1e: VIX candlestick shown with 50, 90 & 200 day moving averages (%)

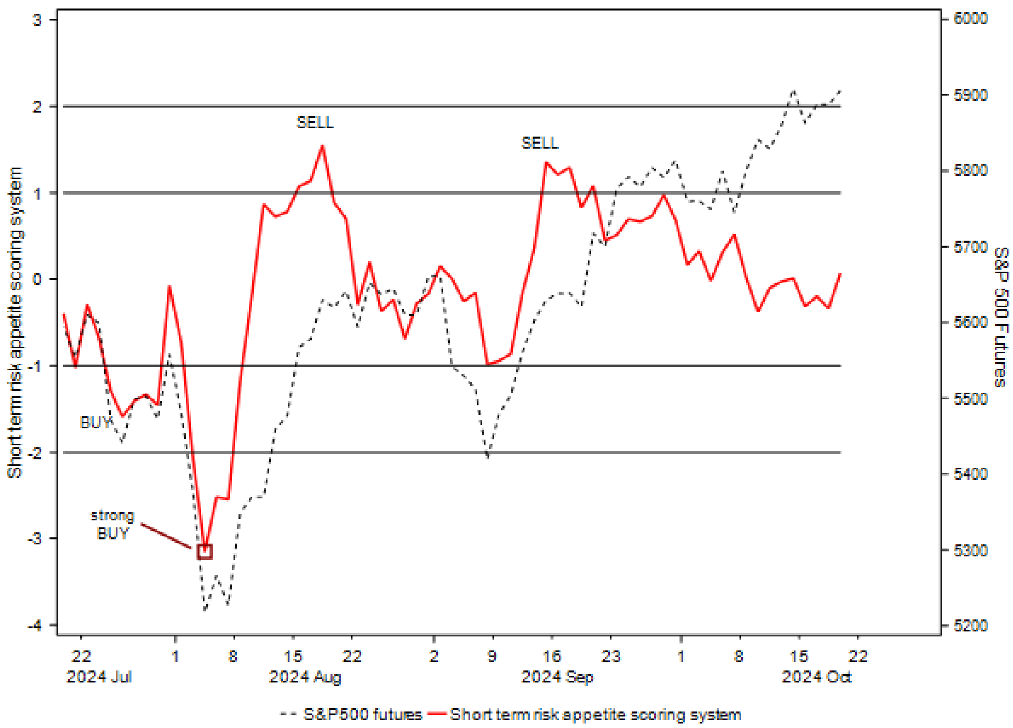
FIG 1f: Short term (14 day) VIX RSI (NB scale INVERTED) vs. S&P500



Source: Longview Economics, Macrobond

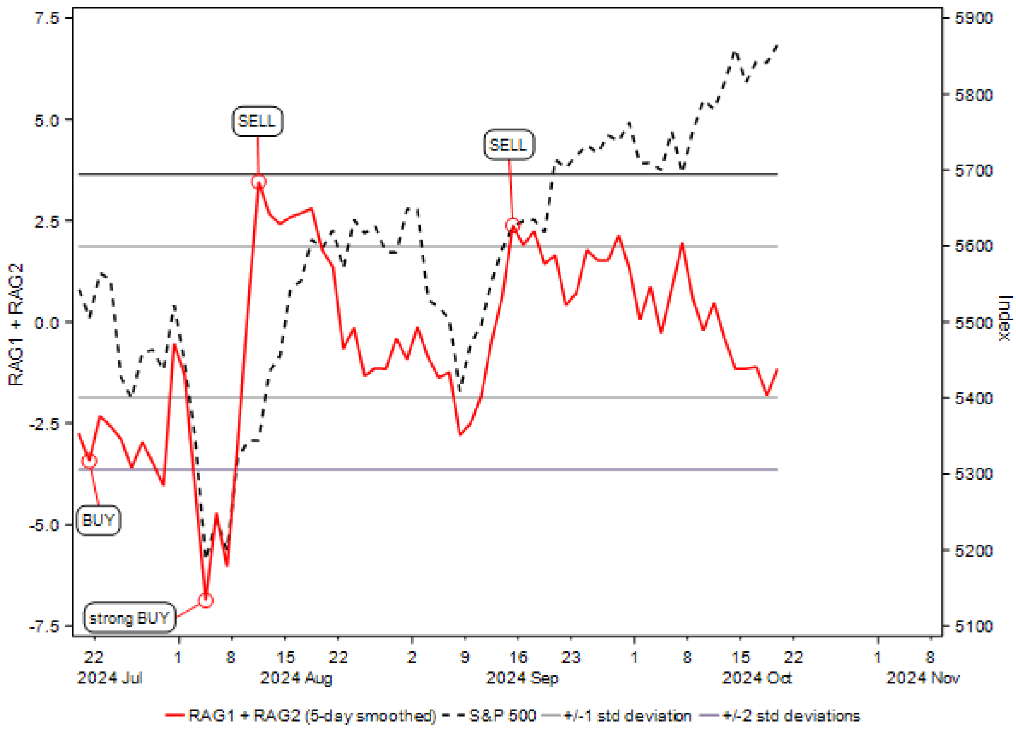
Short term market timing models are more mixed……

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



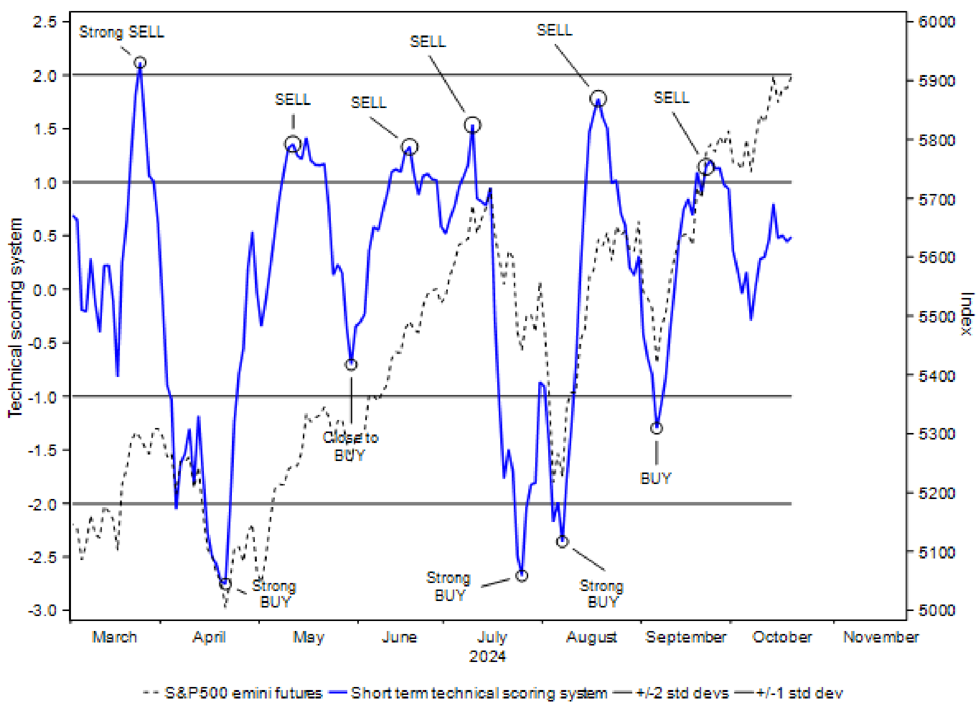
Source: Longview Economics, Macrobond

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



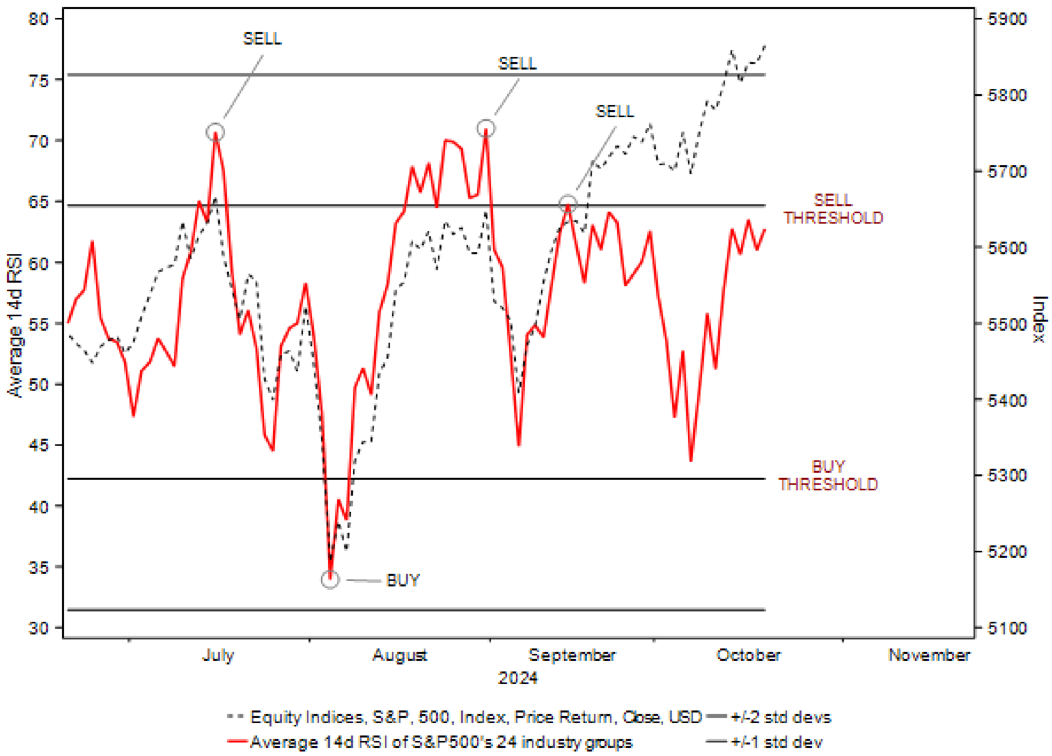
Source: Longview Economics, Macrobond

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



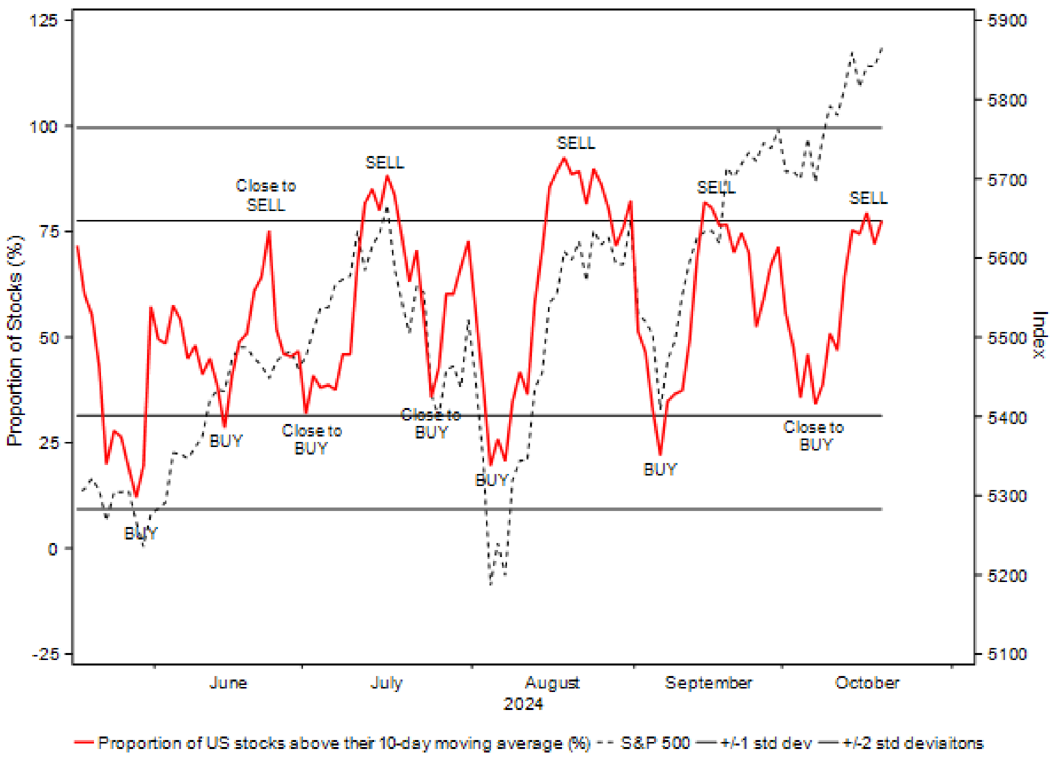
Source: Longview Economics, Macrobond

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



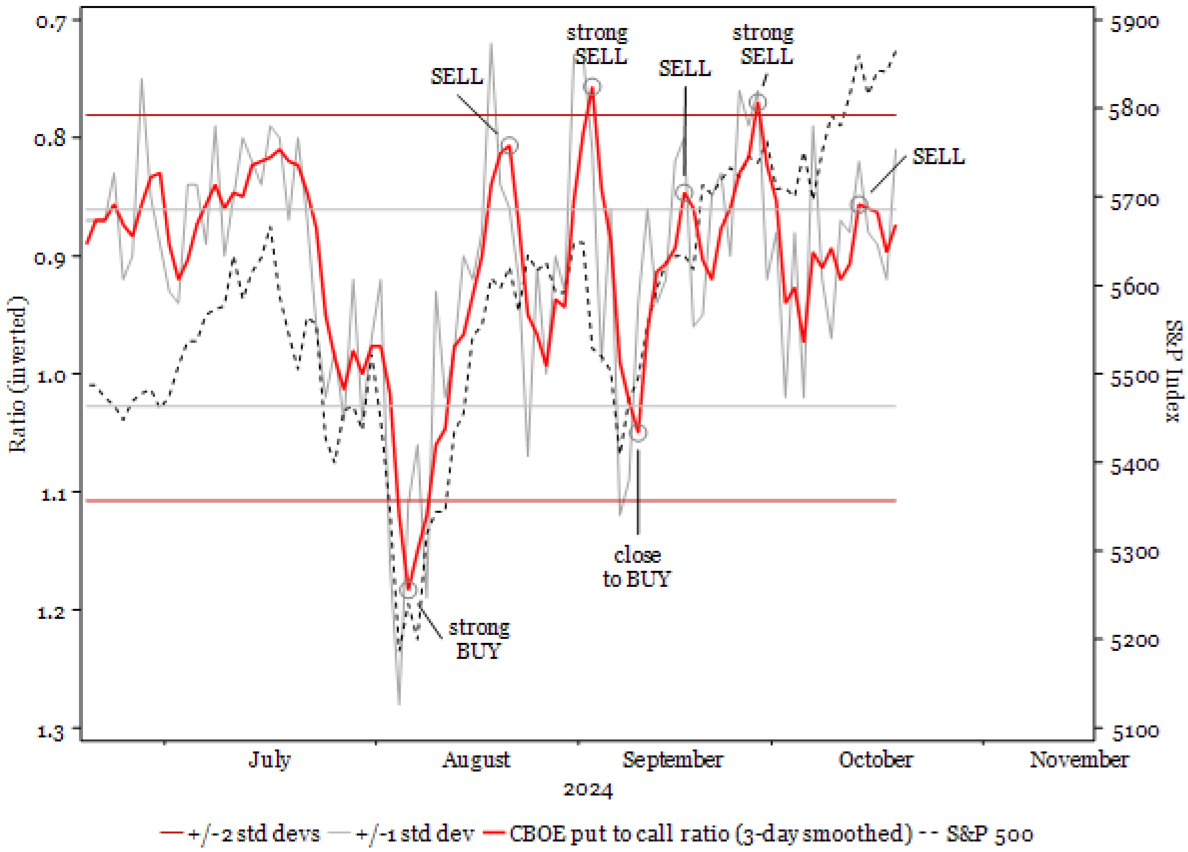
Source: Longview Economics, Macrobond

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



Source: Longview Economics, Macrobond

FIG 2e: CBOE put to call ratio (1 & 3 day smoothed with standard deviation bands) vs. S&P500

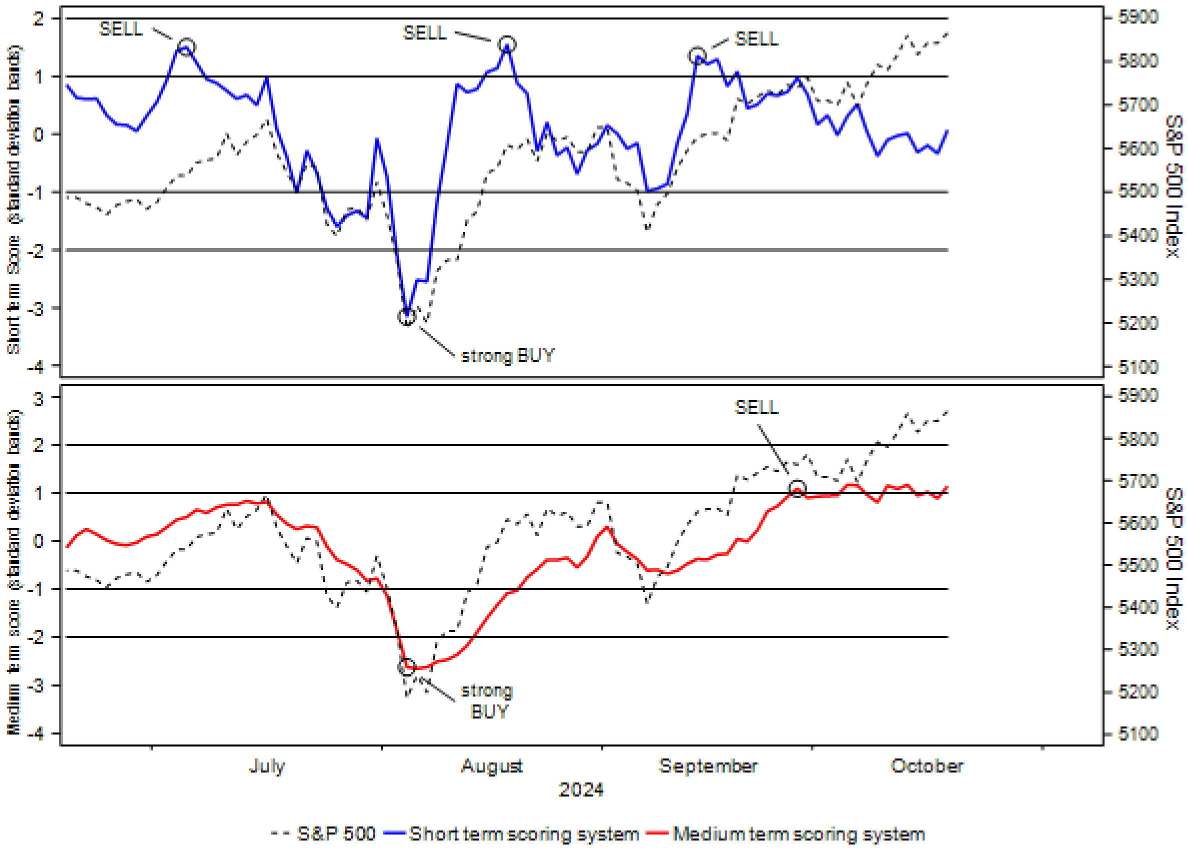


Source: Longview Economics, Macrobond

Key Longview Scoring Systems (chart below):

Short term (1 – 2 week) scoring system: **NEUTRAL**
Medium term (1 – 4 month) scoring system: **SELL** (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: UK Rightmove house prices (Oct, 12:01am); **German PPI** (Sept, 7am); **US Conference Board leading index** (Sept, 3pm).

Key events today include: **PBoC policy decision** (1 & 5 year LPR, 2am); speech by the RBA's Hauser at Fireside chat (2am); speech by the ECB's Simkus in Vilnius (8am); speeches by the Fed's Logan at SIFMA annual meeting (1:55pm), Kashkari in Townhall event (6pm) & Schmid on the Economic and monetary policy outlook (10:05pm).

Key earnings today include: Sandvik, UltraTech Cement.

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 10th October 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

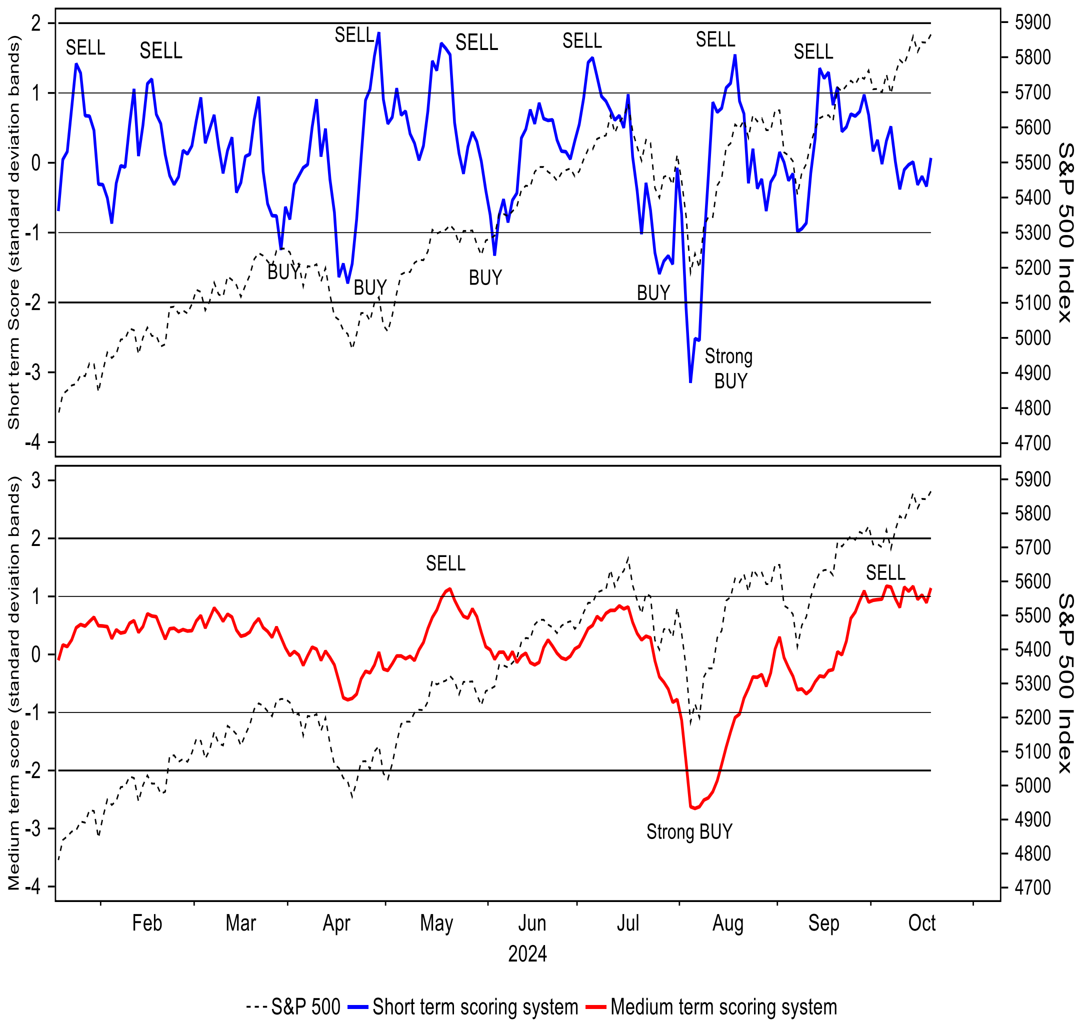
1 – 2 Week View on Risk

21st October 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



Short term scoring system is NEUTRAL

Medium term scoring system is On SELL

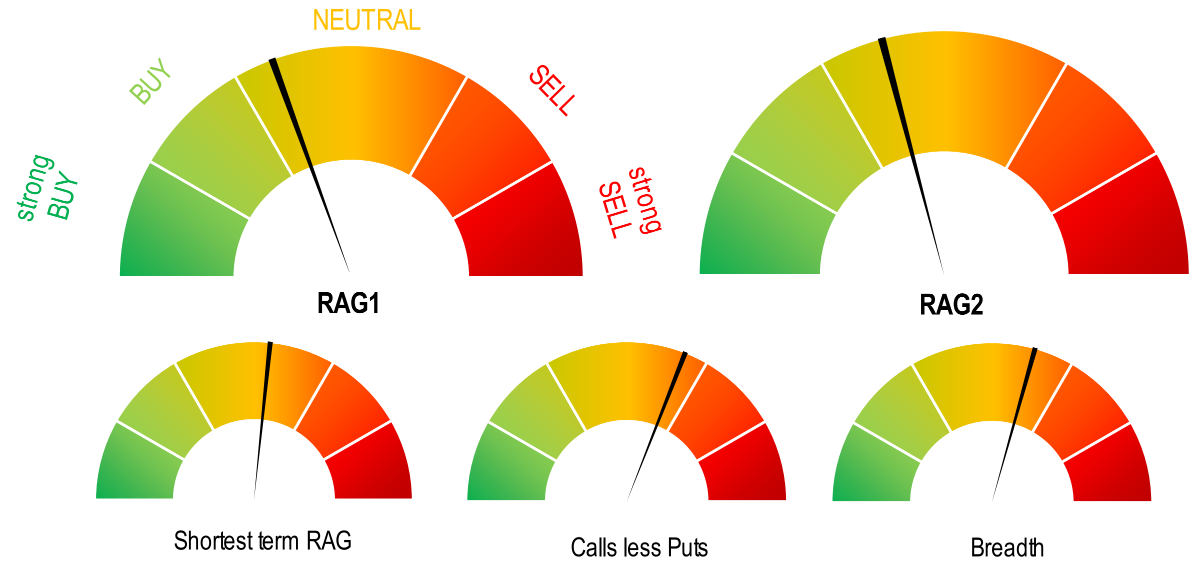
Source: Longview Economics, Macrobond

*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

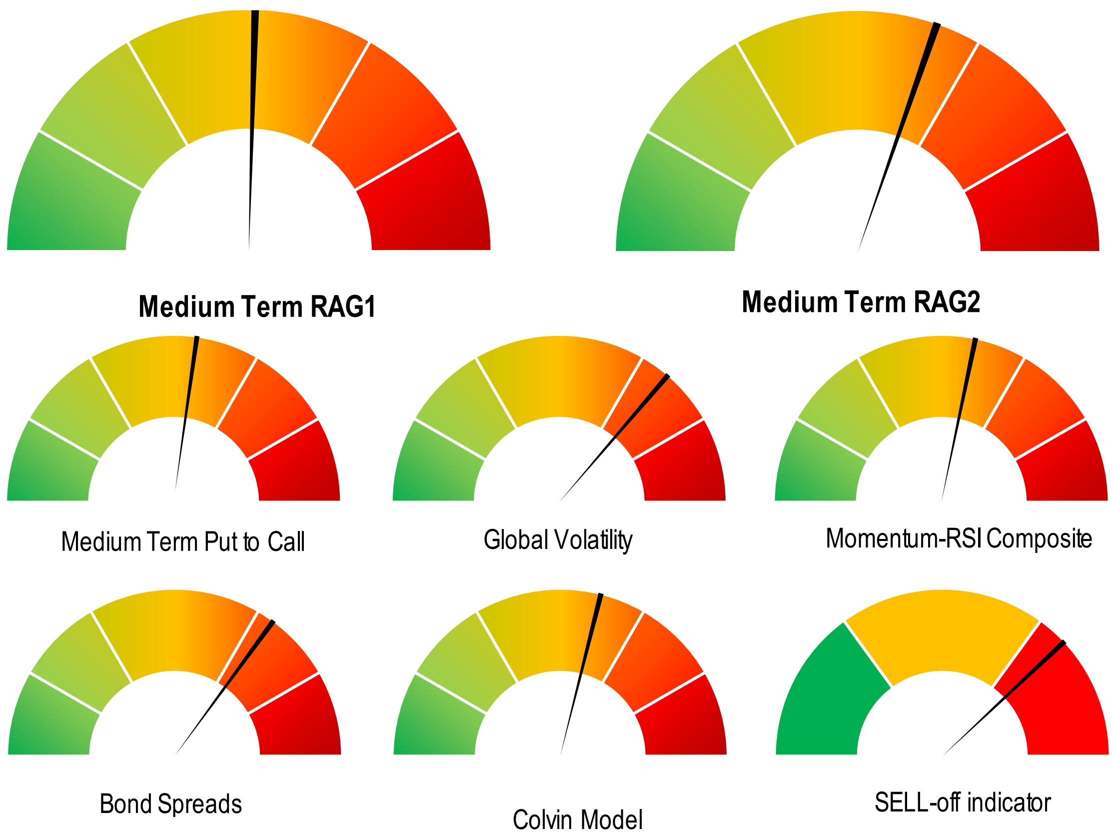
Section 1a: Summary of indicator signals**

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



Source: *Longview Economics*

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

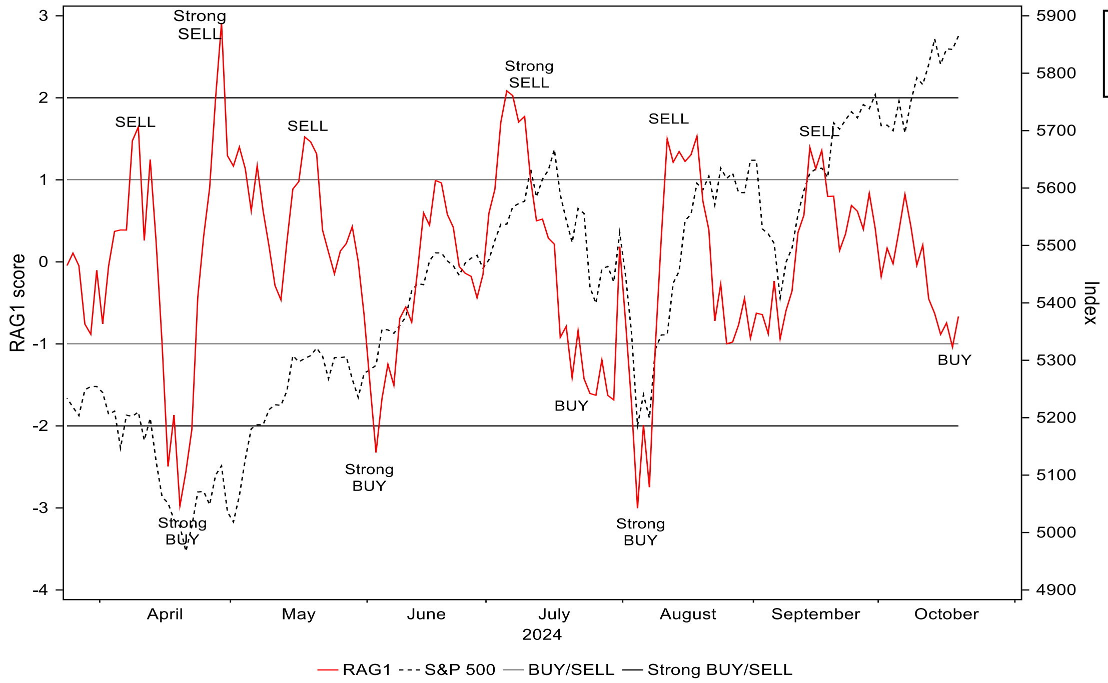


Source: *Longview Economics*

**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

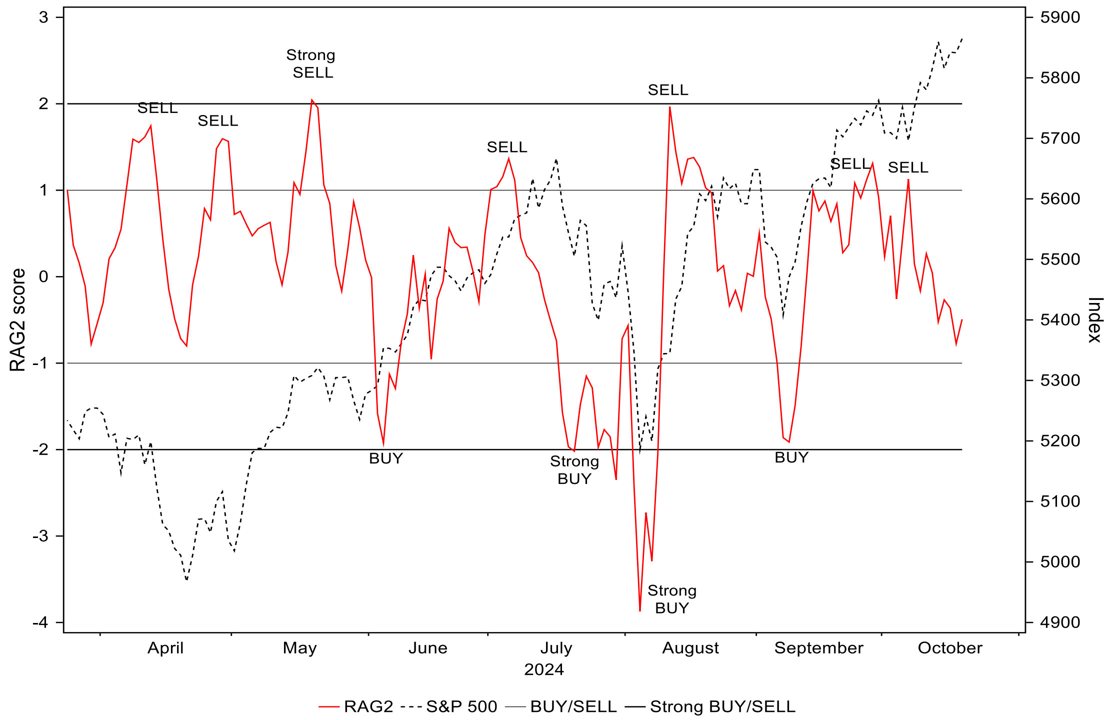
Fig 2a: RAG 1 vs. S&P 500



RAG1 is NEUTRAL

Source: Longview Economics, Macrobond

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

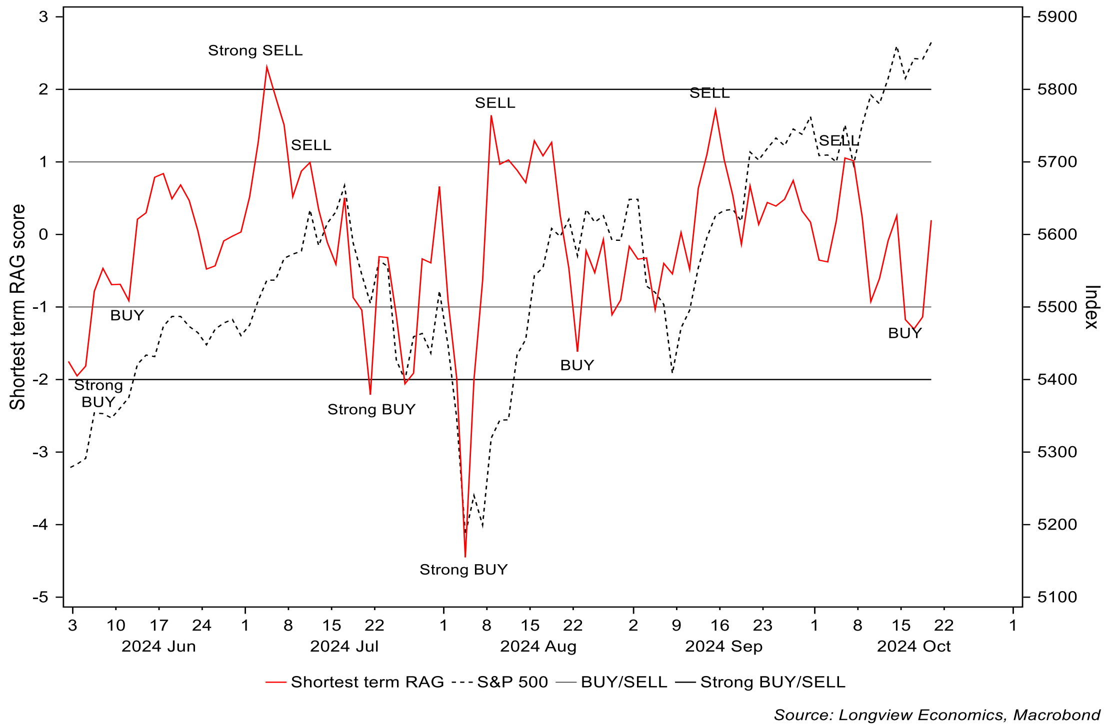


RAG2 is NEUTRAL

Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

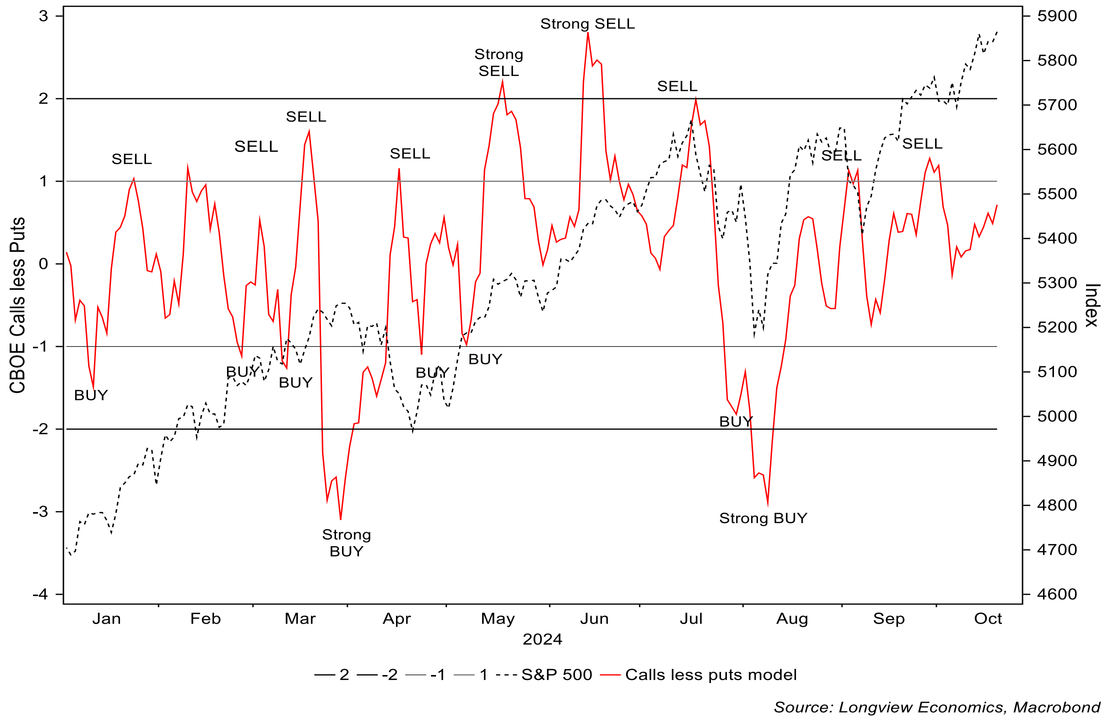
Fig 2c: Shortest term RAG (i.e. using a 3 day moving average) vs. S&P 500



Source: Longview Economics, Macrobond

Shortest term RAG is NEUTRAL

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

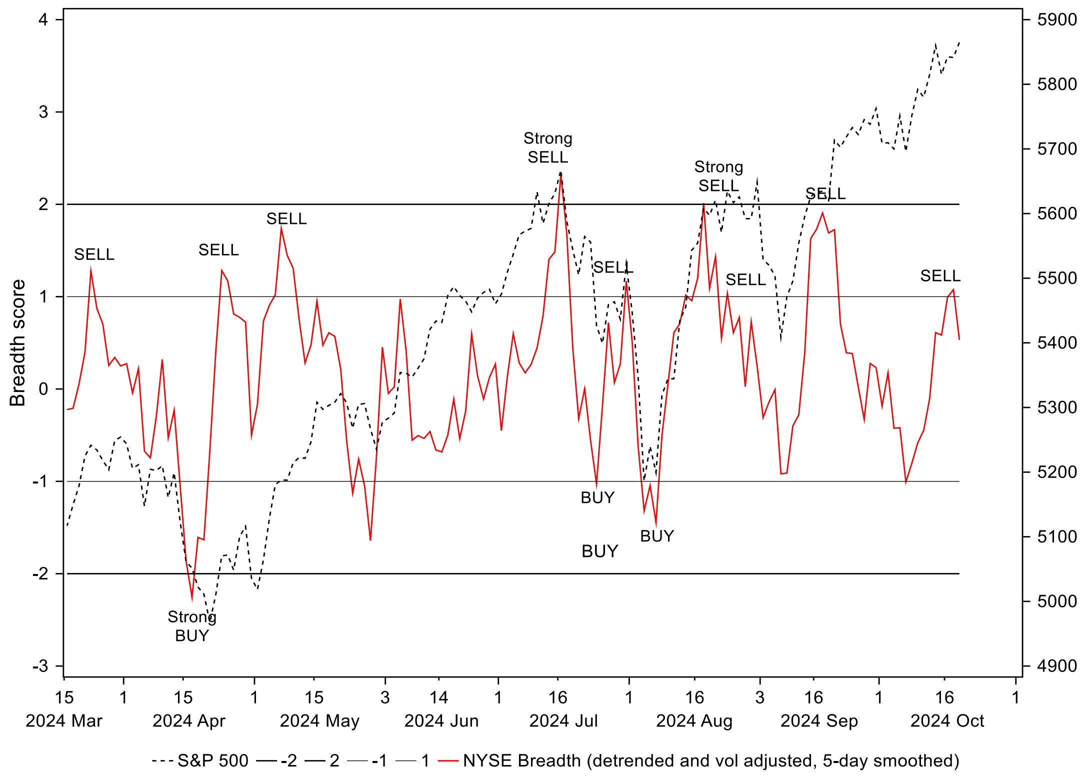


Source: Longview Economics, Macrobond

Calls less puts model is NEUTRAL

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 NEUTRAL

For explanations of indicators please see page 10

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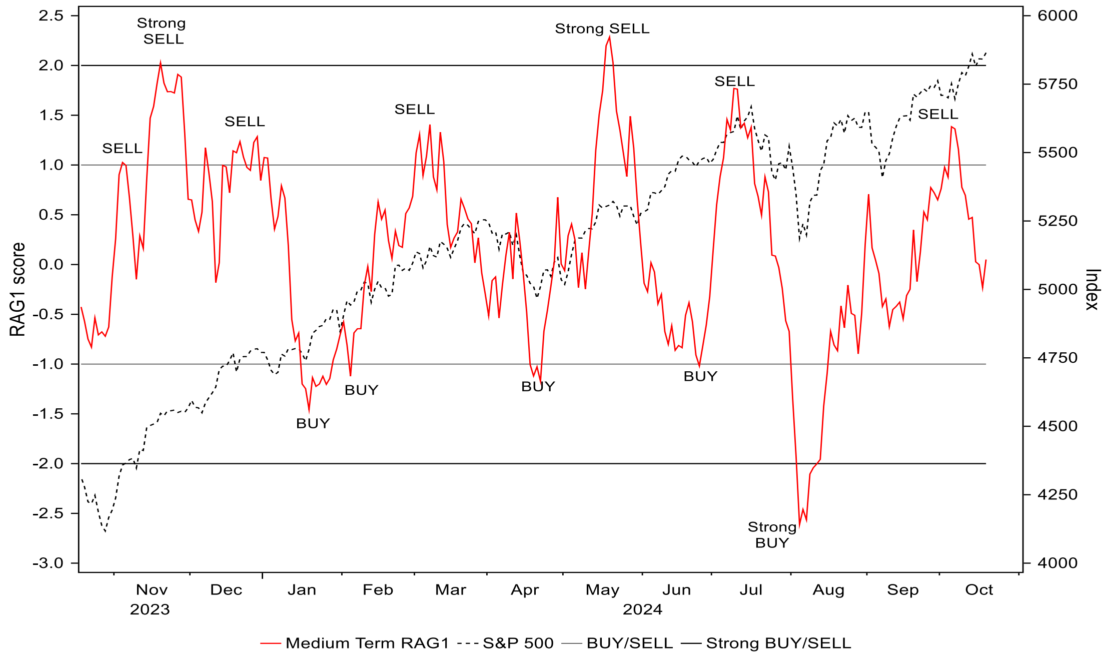
Section 3: Medium term (1 – 2 month) outlook

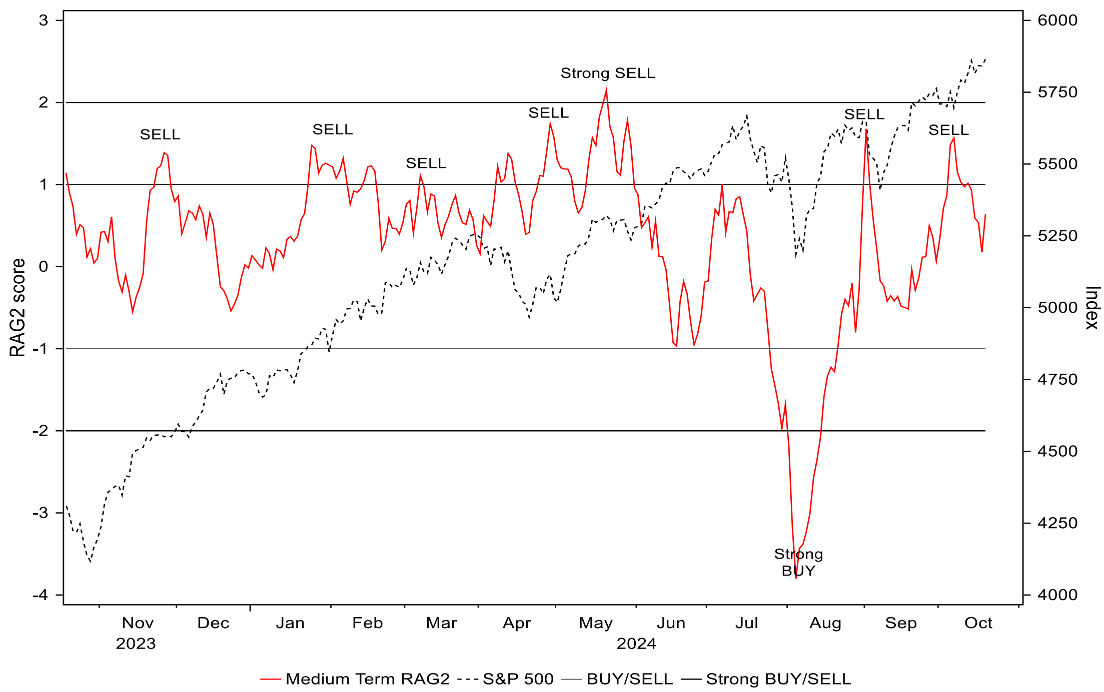
Fig 3a: Medium term RAG1 (1 – 2 month view) vs. S&P 500



Source: Longview Economics, Macrobond

Medium term RAG1 is NEUTRAL

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

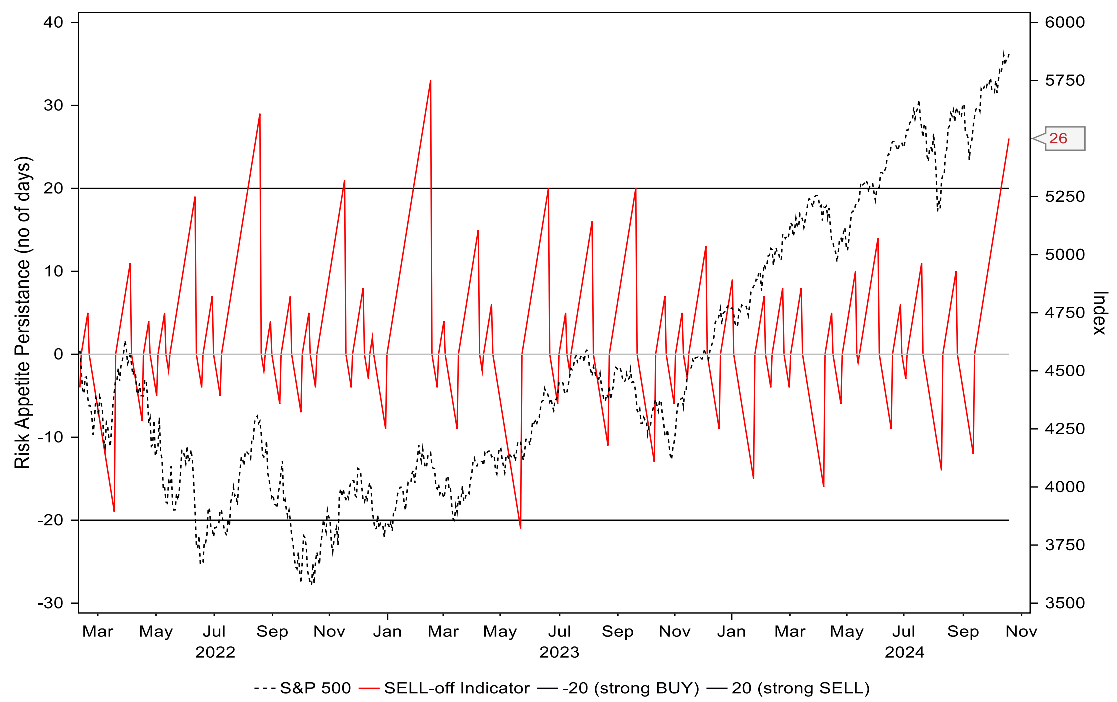


Source: Longview Economics, Macrobond

Medium term RAG2 is NEUTRAL

For explanations of indicators please see page 10

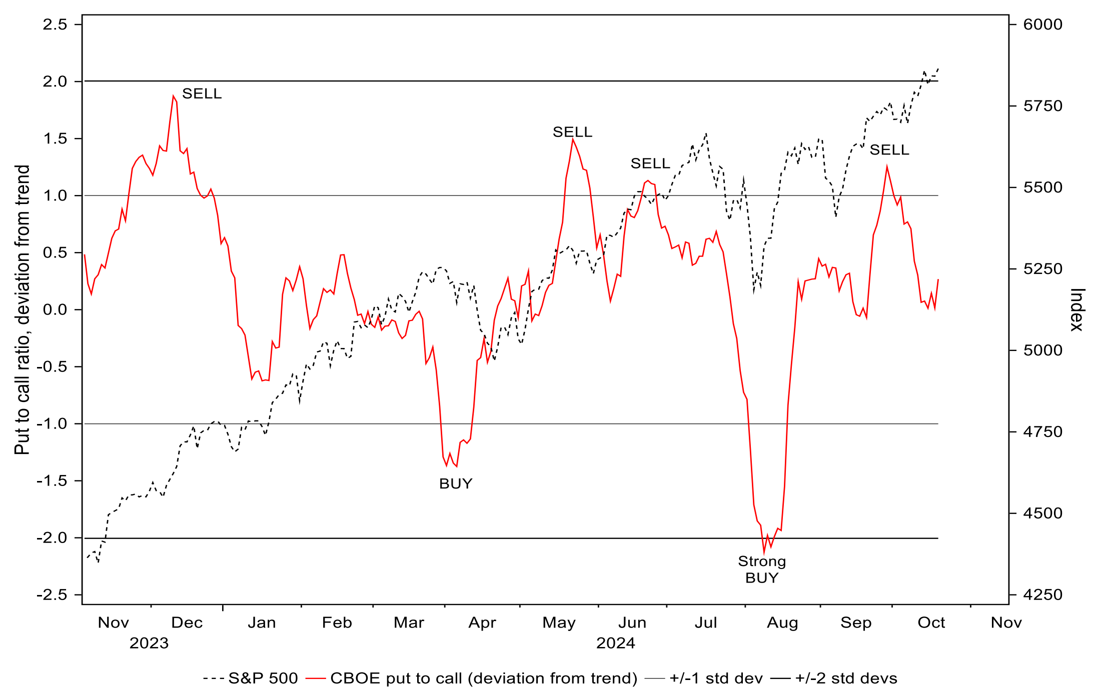
Fig 3c: SELL-off indicator (shown vs. S&P500)



Source: Longview Economics, Macrobond

The SELL-off indicator is on SELL

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

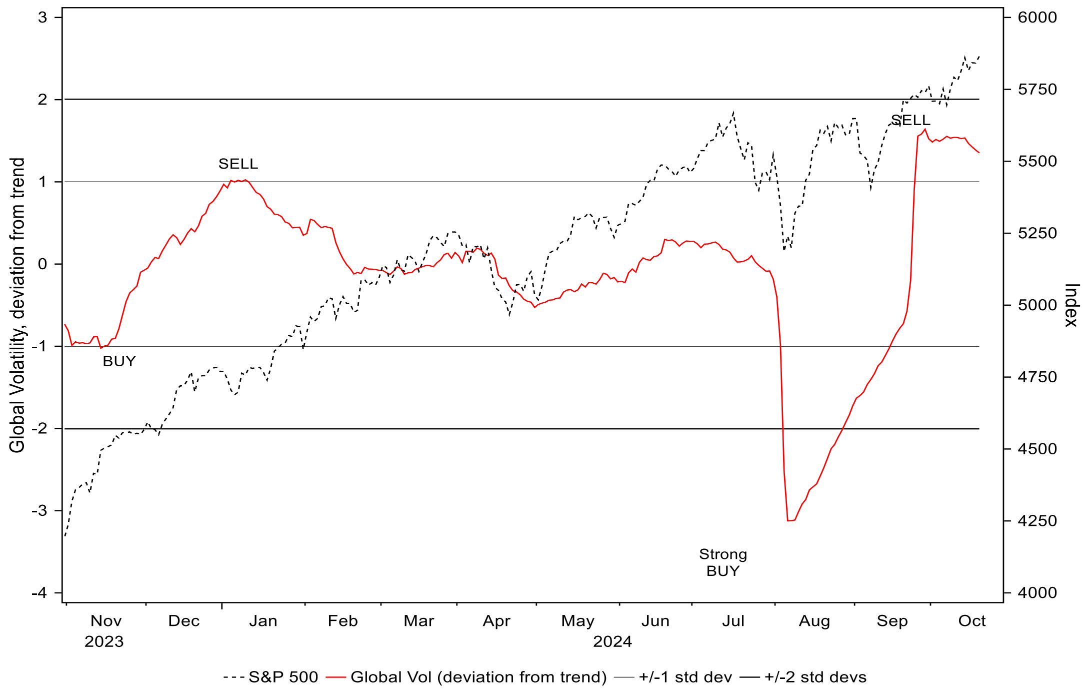


Source: Longview Economics, Macrobond

Medium term put to call model is NEUTRAL

For explanations of indicators please see page 10

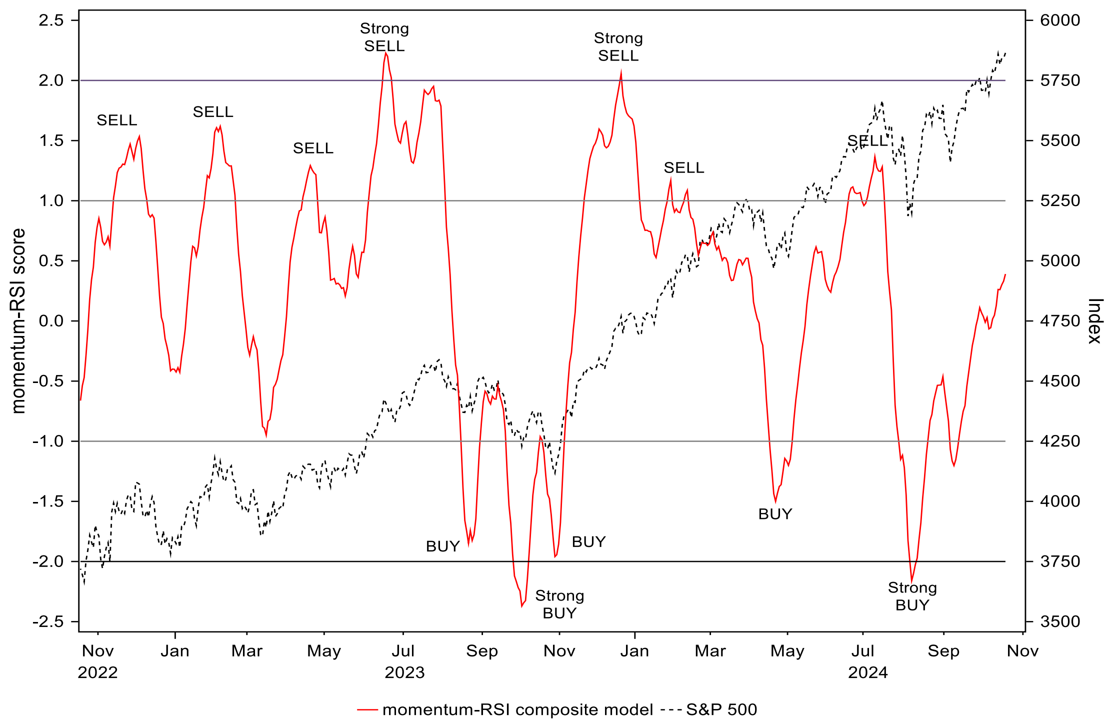
Fig 3e: Global volatility (deviation from trend) model vs. S&P500



Source: Longview Economics, Macrobond

Global volatility indicator is on SELL

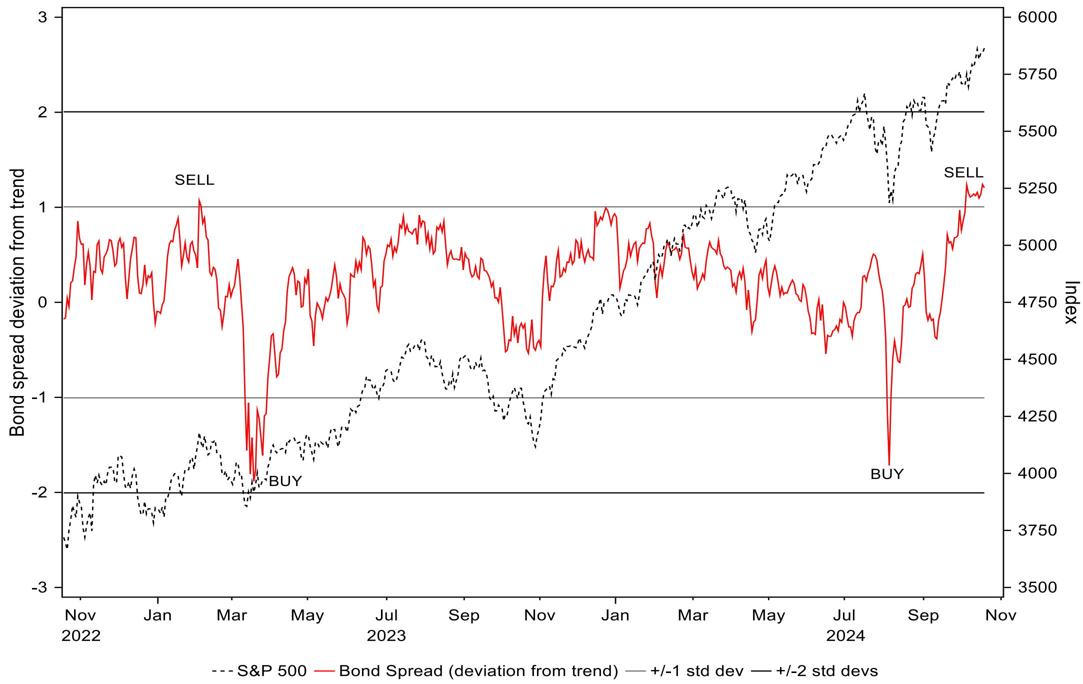
Fig 3f: Longview Momentum-RSI composite model vs. S&P 500



Source: Longview Economics, Macrobond

US momentum RSI composite model is NEUTRAL

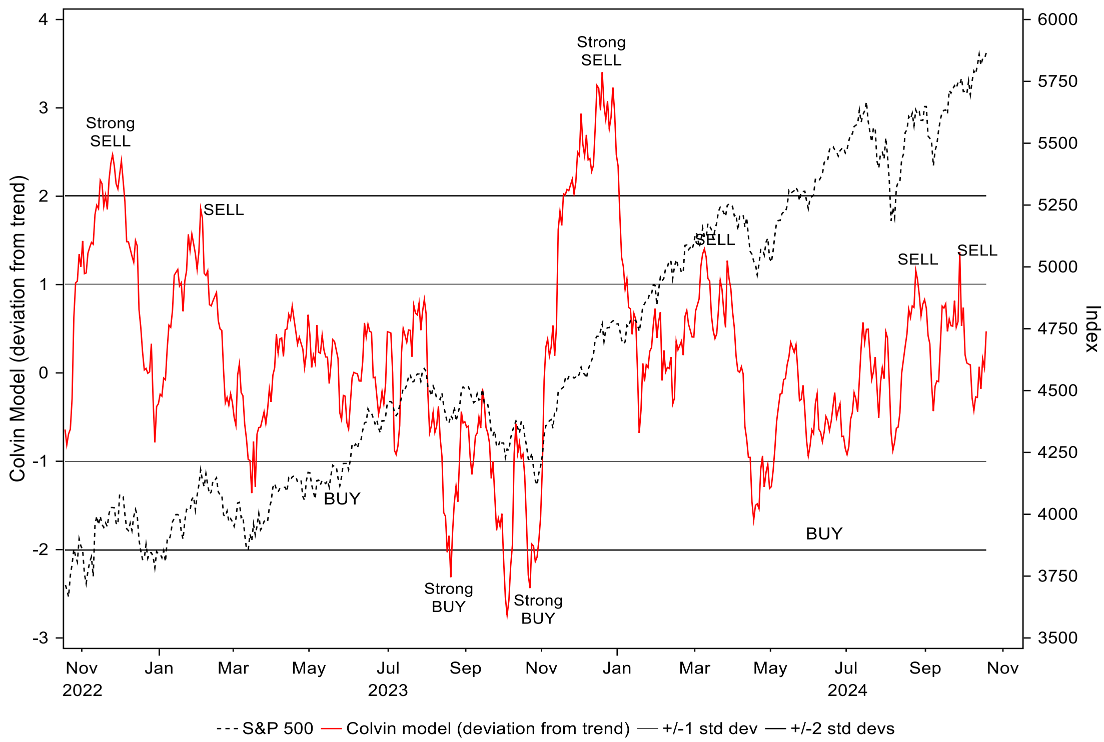
Fig 3g: High yield corporate bond spreads deviation from trend model vs. S&P500



High yield corporate bond spreads model is on SELL

Source: Longview Economics, Macrobond

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



Colvin model – is Neutral

Source: Longview Economics, Macrobond

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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