LVRAG
Daily Risk Appetite Gauge

Equity Index Futures Trading Recommendations

2nd October 2024

"Stay SHORT/Tighten Stop Loss"

Email: info@longvieweconomics.com

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

- Stay 1/3rd SHORT S&P500 December futures (entry was at 5,820 earlier this week).
- Tighten the stop loss to 1% above entry (i.e. to 5,878.25 from 5,936.50 yesterday).

Rationale

The S&P500 sold off sharply yesterday as the oil price spiked intraday (in anticipation of, and following on from, the Iranian attack on Tel Aviv and other parts of Israel – FIG 1). Oil was up 2.5% in the regular session; was over $5 higher intraday from its sub $70 low point; and is currently 6.6% above yesterday's low (FIG 1a). Not surprisingly the weakness in risk assets was widespread with 23 of the 28 top level US indices that we track, lower on the day; eight of the 11 S&P500 sectors weaker (energy, utilities & comm services were the exceptions); and weakness across most European markets. Chinese stocks listed in HK have, overnight, continued to buck the trend of the rest of the global market (e.g. Hang Seng +8.3%).

With Israel vowing a response ("Iran made a big mistake tonight and will pay for it"; source: Israeli PM Netanyahu comments yesterday), the risk of escalation is high. To an extent, though, oil prices have already priced that into markets. The degree of escalation, however, is a clear 'known unknown'. **In that sense it's a two-way risk** (i.e. if Israel's response is measured, some of the risk premium might come out of the oil price - equally continued escalation will likely push the oil price even higher).

Short term models retain a clear SELL bias (FIGs 2 – 2c). Those models are highlighting the extent of this recent rally (i.e. the 6.5%, 16-day rally in the S&P500 through to Monday's close) and therefore its **vulnerability to negative newsflow**. Over recent trading sessions, market participants had become greedy (i.e. with risk appetite models reaching SELL a few days ago); technically equity markets have become overbought (e.g. see technical scoring systems); that overbought set-up was also evident at a sector and single stock level (as highlighted in recent Daily publications with sector and single stock technical and momentum models – e.g. FIG 1d); whilst downside put protection has been low – both in the broader market and in the tech centric NDX100. Volatility (both VIX & VVIX - FIG 1e) has also picked up. Medium term models are also on/close to SELL (e.g. see combined 'short & medium' term risk appetite scoring system – FIG 1f). The **models backdrop, therefore, supports an expectation of further downside in risk assets**.

With that weakness in the S&P500 over the past 24 hours, the **futures are trading at the bottom of their recent 8-day trading range** (i.e. 5,730 – 5,830, FIG 1b). They are also sitting on a key long term support level (intraday highs 19th September and mid-July, FIG 1c). In terms of other risks for the equity market, yesterday's macro data highlighted the ongoing slowing of the US economy – with a weak ISM manufacturing employment sub index and weak construction spending (which had been one of the key beneficiaries of fiscal spending in 2022 & '23). In that respect, further key data later this week (including ISM services & non-farm payrolls) are also key risks. Bitcoin, a key liquidity indicator, has also rolled over from the top end of its recent downtrend channel – FIG 1g.

We **recommend STAYing SHORT** S&P500 futures given the SELL bias of the models and the risk of escalation (as well as potentially troubling US macro data). We also recommend tightening the stop loss to 1% above entry (from 2%) reflecting the two-way nature of the oil price risk (i.e. much of the geopolitical risk premium could already be in the price), as well as the fact that the S&P500 is currently sitting on a key support level.

Kind regards,

The team @ Longview Economics

FIG 1: Brent oil futures vs. S&P500 Dec futures (inverted) – 5-day TICK chart

FIG 1a: Brent oil futures 5-day TICK chart

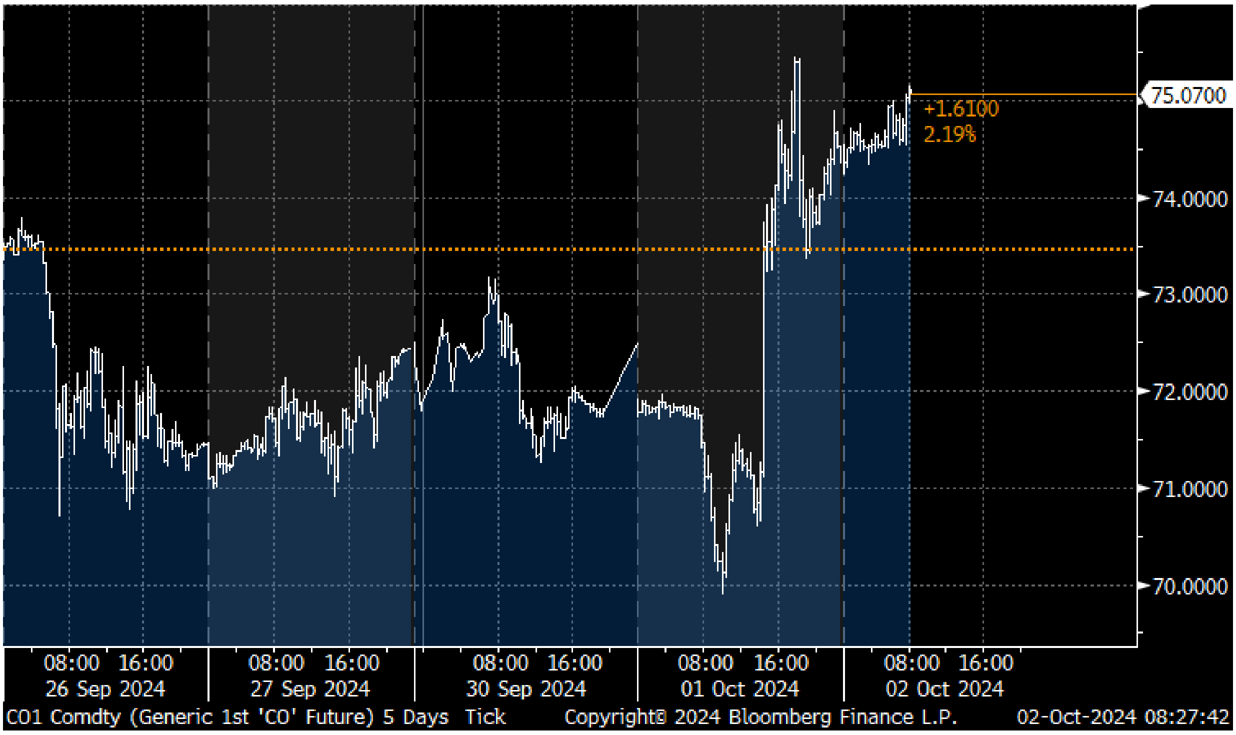

FIG 1b: S&P500 futures 10-day tick chart shown with overnight price action

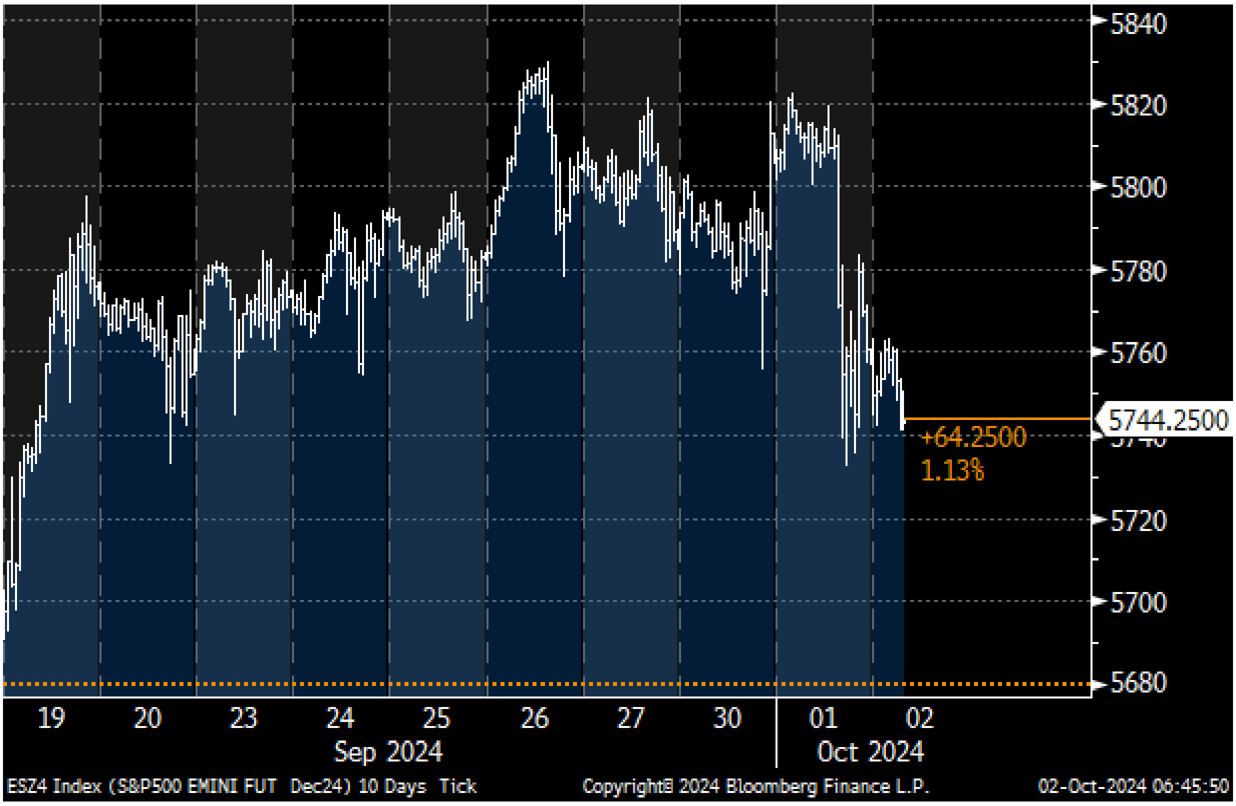

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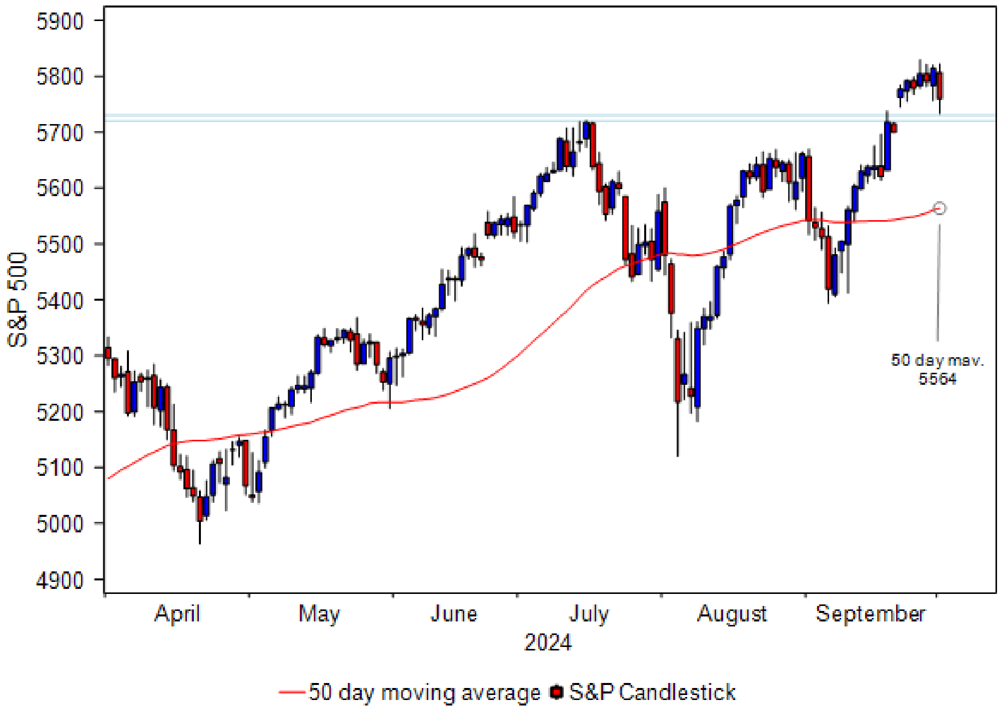
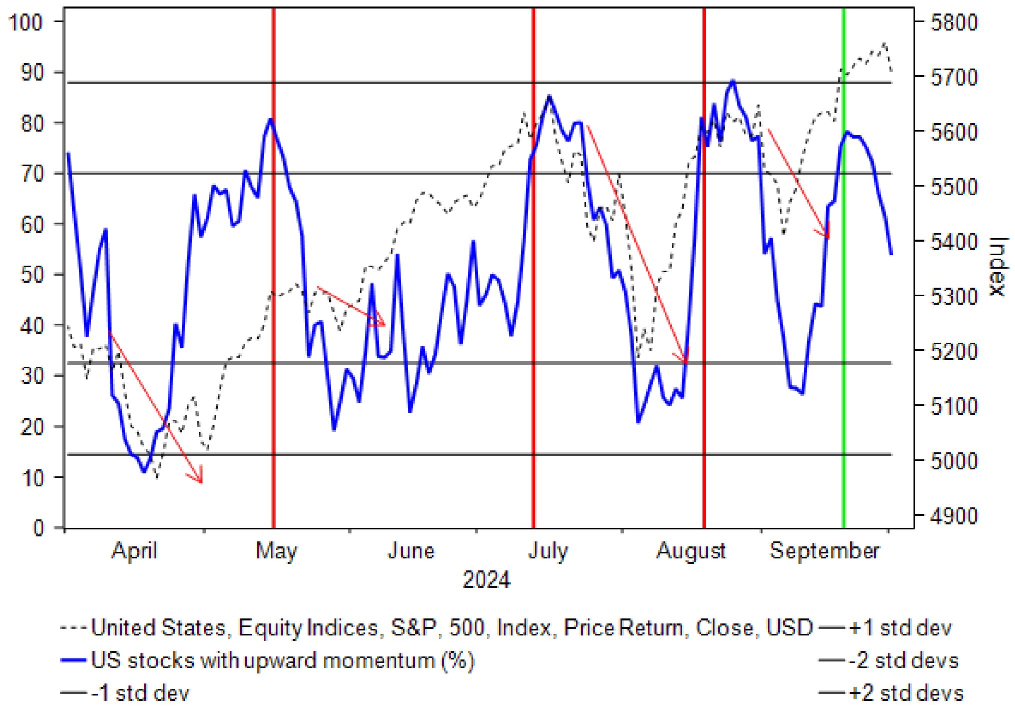
FIG 1c: S&P500 futures candlestick shown with its 50-day moving average



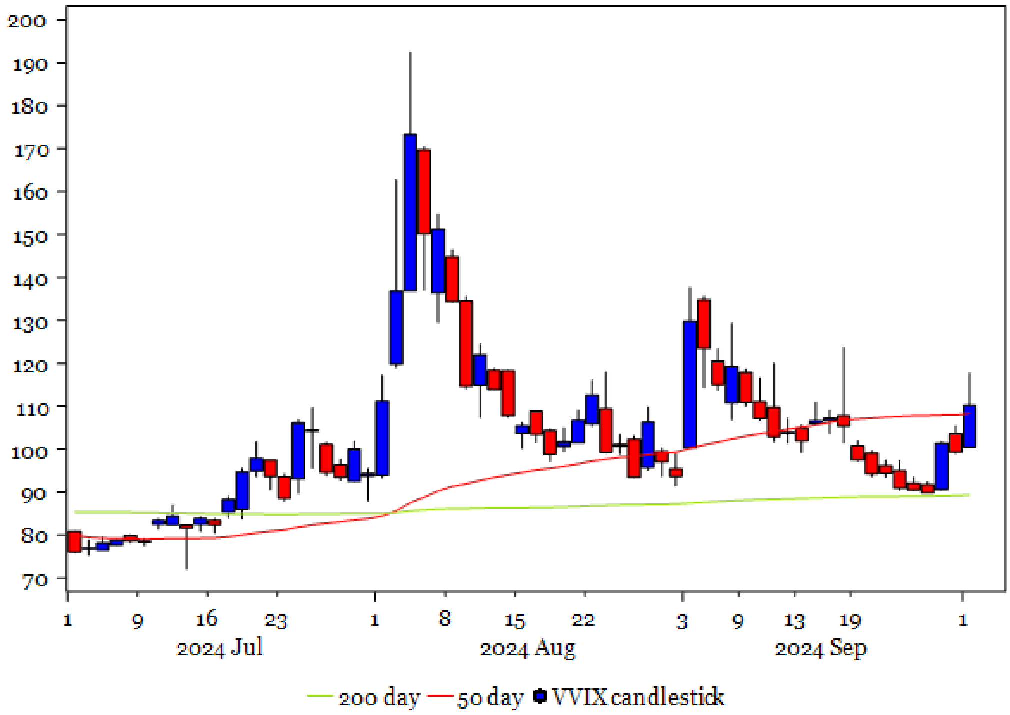
Source: Longview Economics, Macrobond

FIG 1d: S&P500 single stocks with upward momentum (scored & aggregated) vs. S&P500



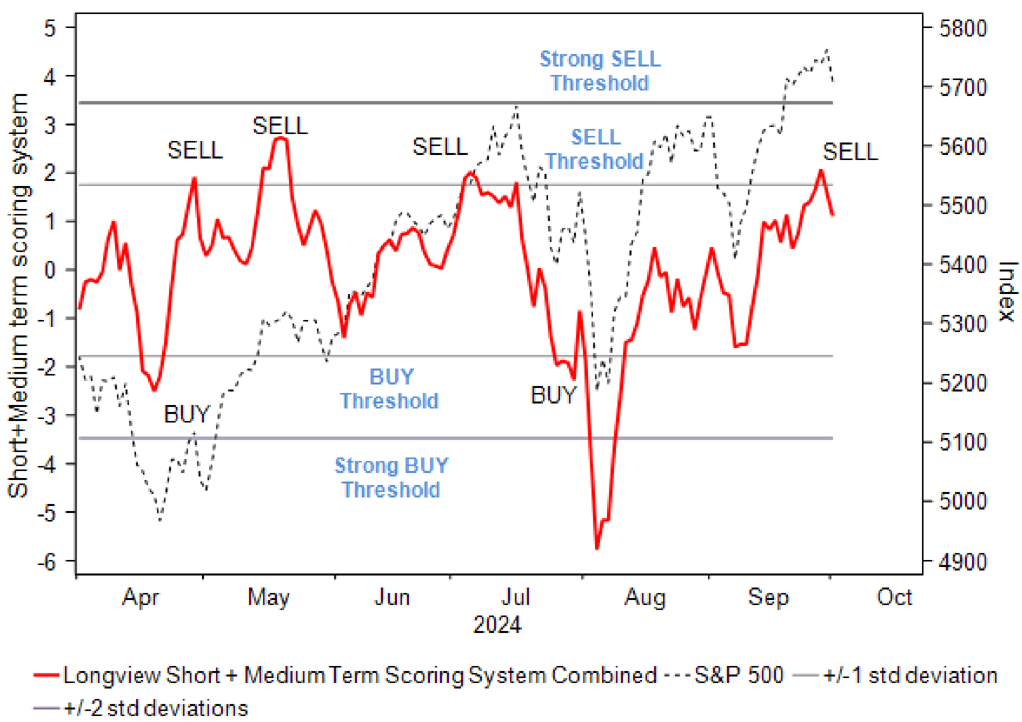
Source: Longview Economics, Macrobond

FIG 1e: VVIX candlestick chart shown with key moving averages



Source: Longview Economics, Macrobond

FIG 1f: Longview combined short PLUS medium term **'risk appetite'** scoring systems vs. S&P500



Source: Longview Economics, Macrobond

FIG 1g: Bitcoin candlestick shown with key moving averages and recent downtrend channel

Short term market timing models are mostly rolling over from SELL signals……

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

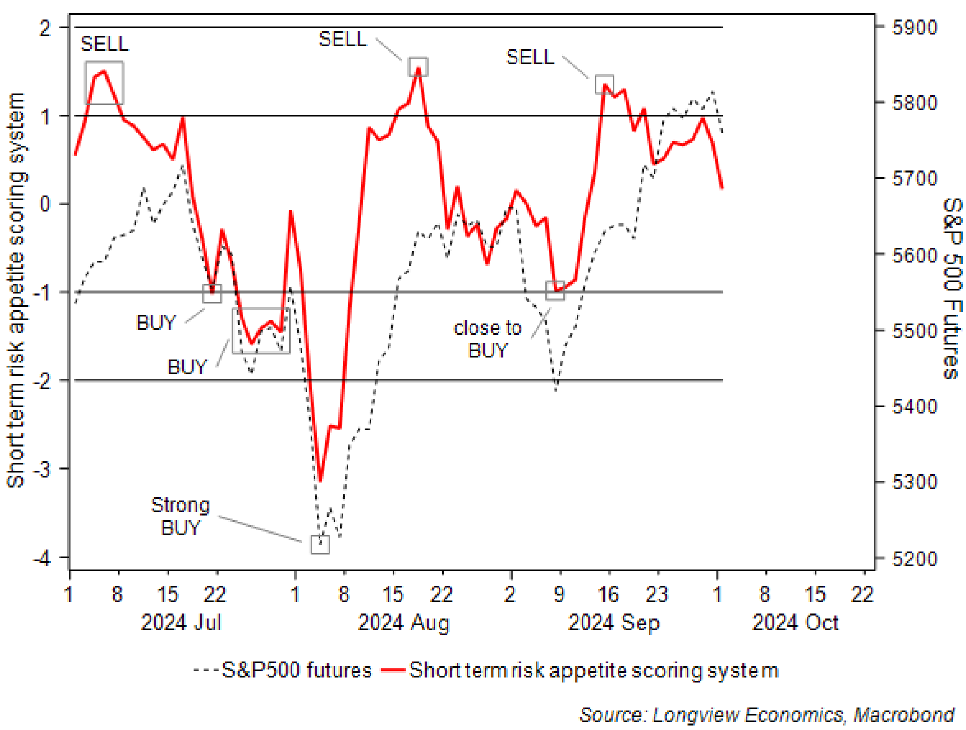


FIG 2a: Longview combined key **'risk appetite'** models (RAG1 + RAG2) vs. S&P500

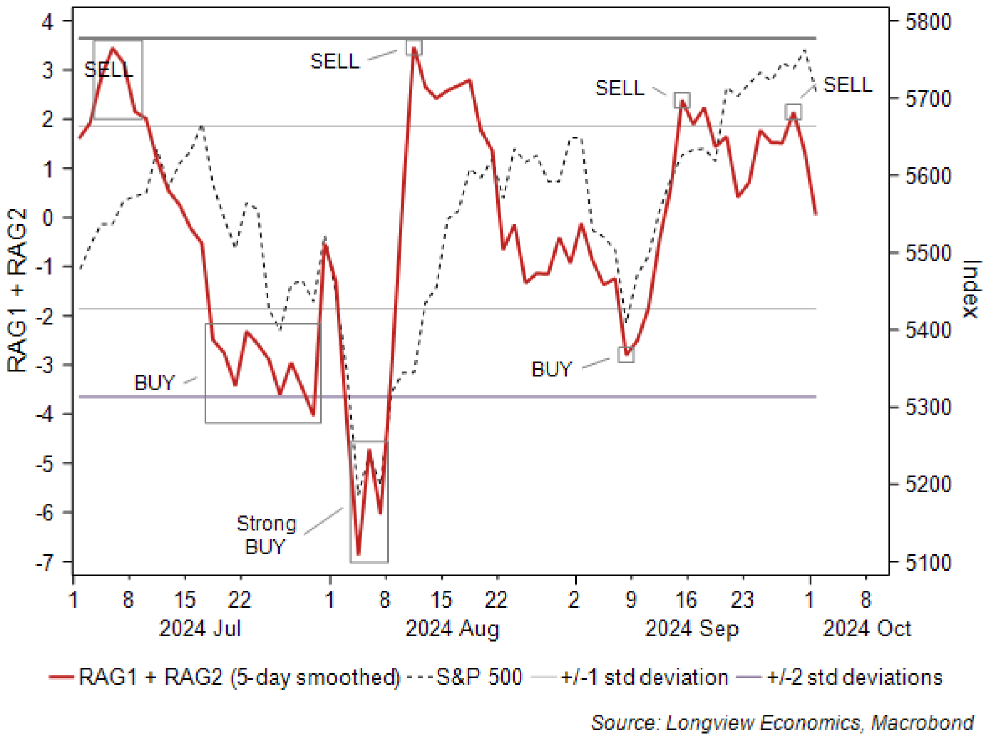


FIG 2b: Longview S&P500 short term **'technical'** scoring system vs. S&P500 futures

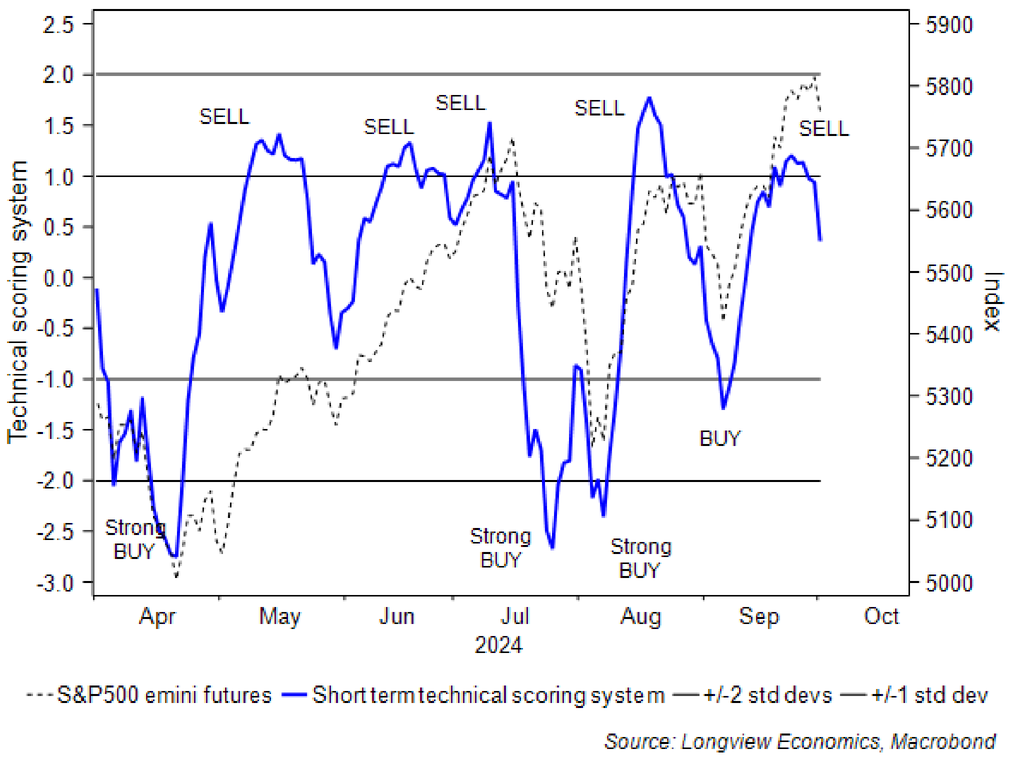
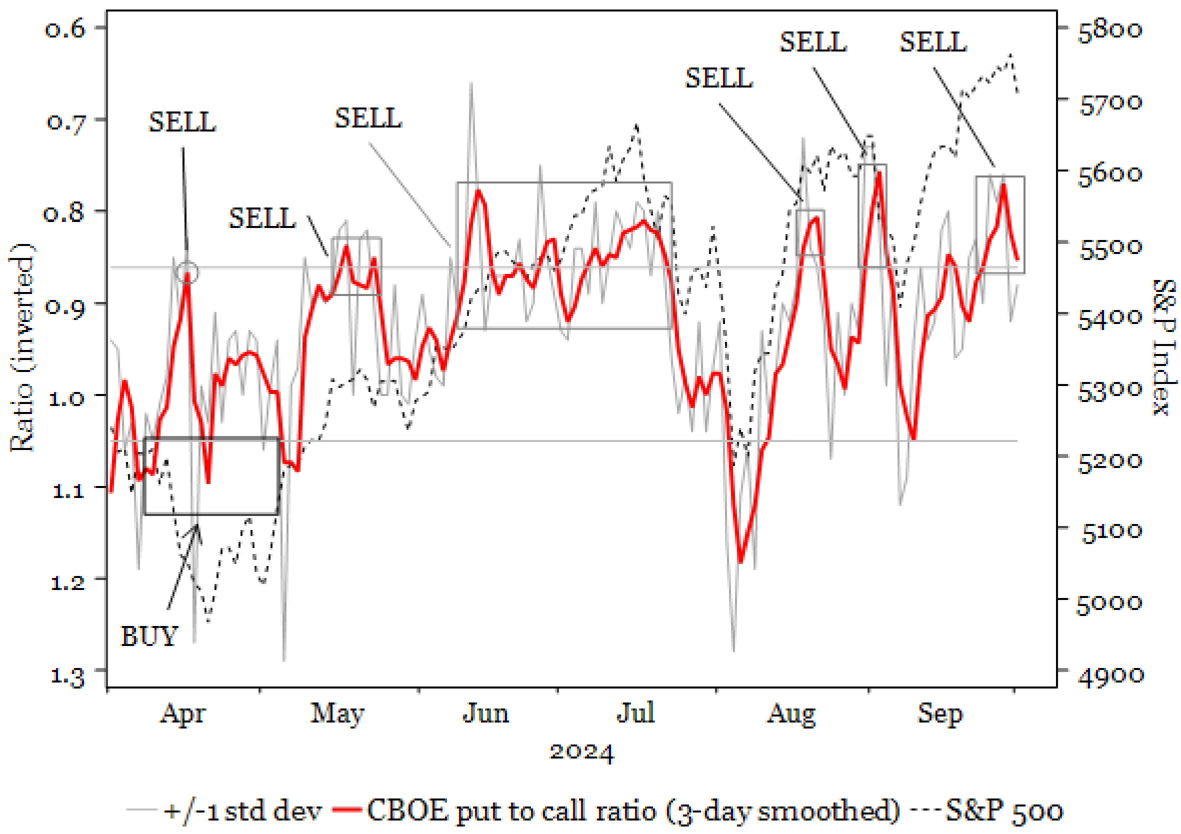


FIG 2c: CBOE put to call ratio (1 & 3 day smoothed with standard deviation bands) vs. S&P500

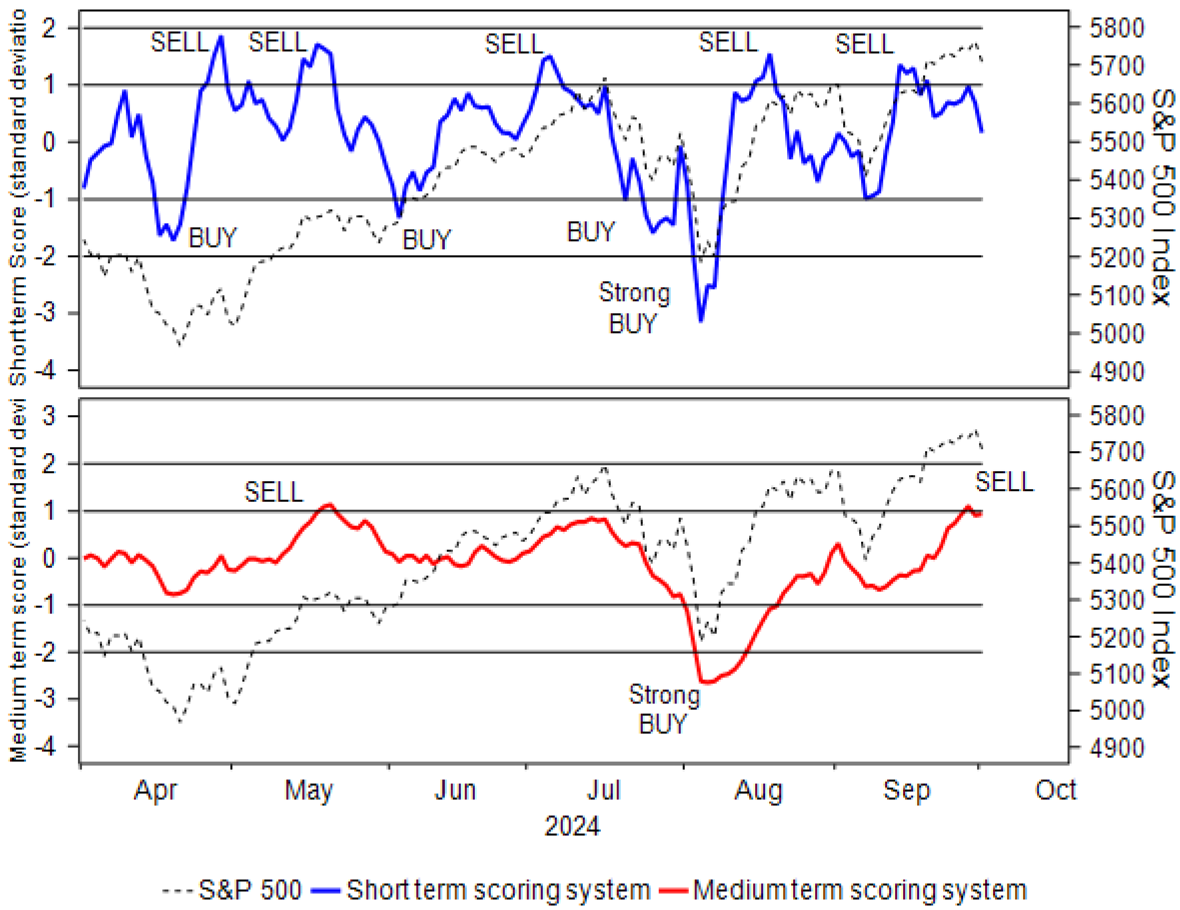


Source: Longview Economics, Macrobond

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

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

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



Source: Longview Economics, Macrobond

Key macro data/events

Key data today include: Japanese money supply (Sept, 12:50am); Japanese ESRI consumer confidence (Sept, 6am); Spanish unemployment change (Sept, 8am); Italian unemployment rate (Aug, 9am); **Eurozone unemployment rate** (Aug, 10am); **US ADP employment change** (Sept, 1:15pm).

Key events today include: Market holidays in China on account of National Day (Tues – Fri); Bank of England publishes FPC summary (10:30am); speeches by the ECB's Guindos, Kazaks & Simkus in Riga (8:15am – 10:45am), Lane in Frankfurt (10:30am), Elderson in Dublin (12pm), Holzmann in Vienna (3pm) & Schnabel in Freiburg (5:45pm); speeches by the Fed's Hammack, Musalem & Bowman at the Community Banking Research Conference (2-4pm) & Barkin on the Economy (5:15pm).

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 on 5th September 2024. If you are not on the distribution list and would like to receive these reports pls email info@longvieweconomics.com.

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Daily Risk Appetite Gauge

1 – 2 Week View on Risk

2nd October 2024

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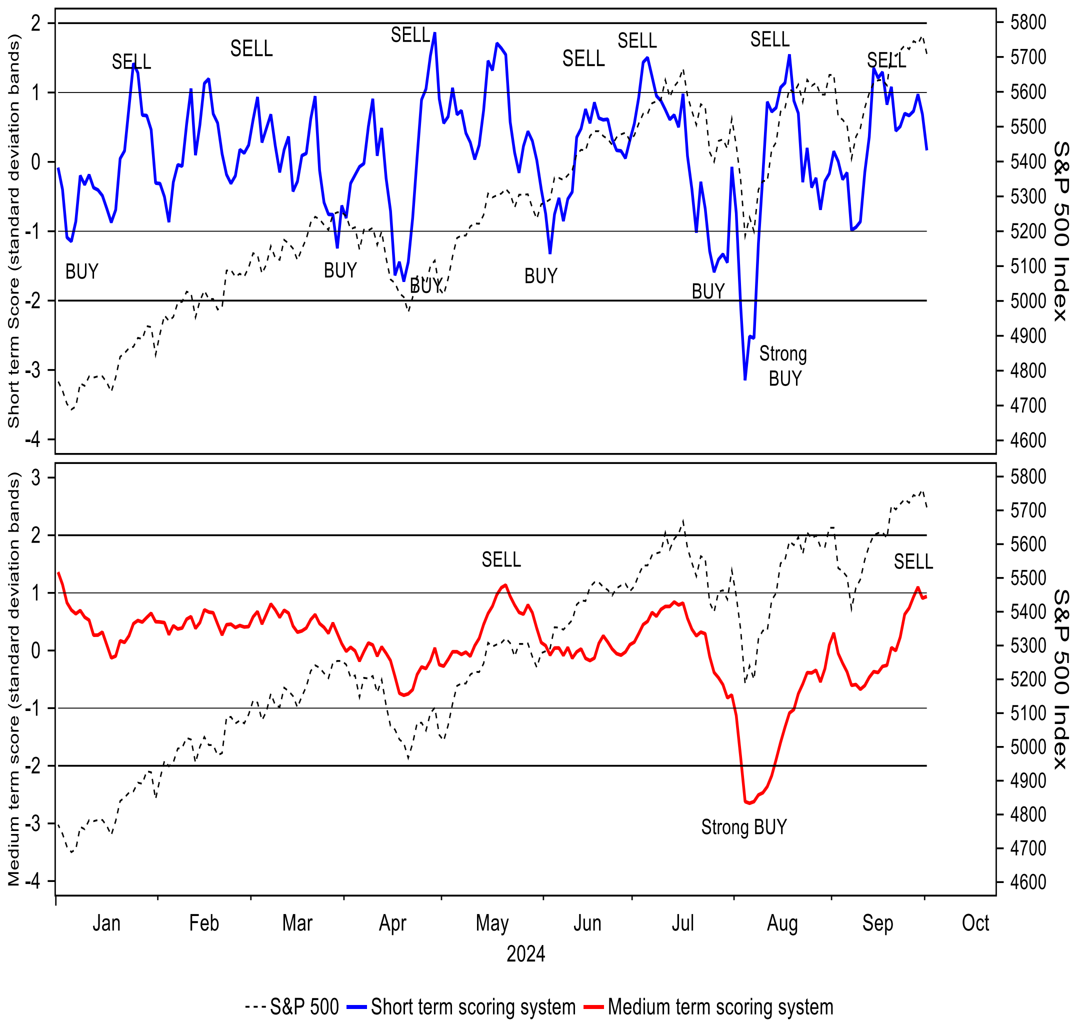
Section 1: Longview Scoring Systems (short & medium term*)

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



Short term scoring system is NEUTRAL

Medium term scoring system is NEUTRAL

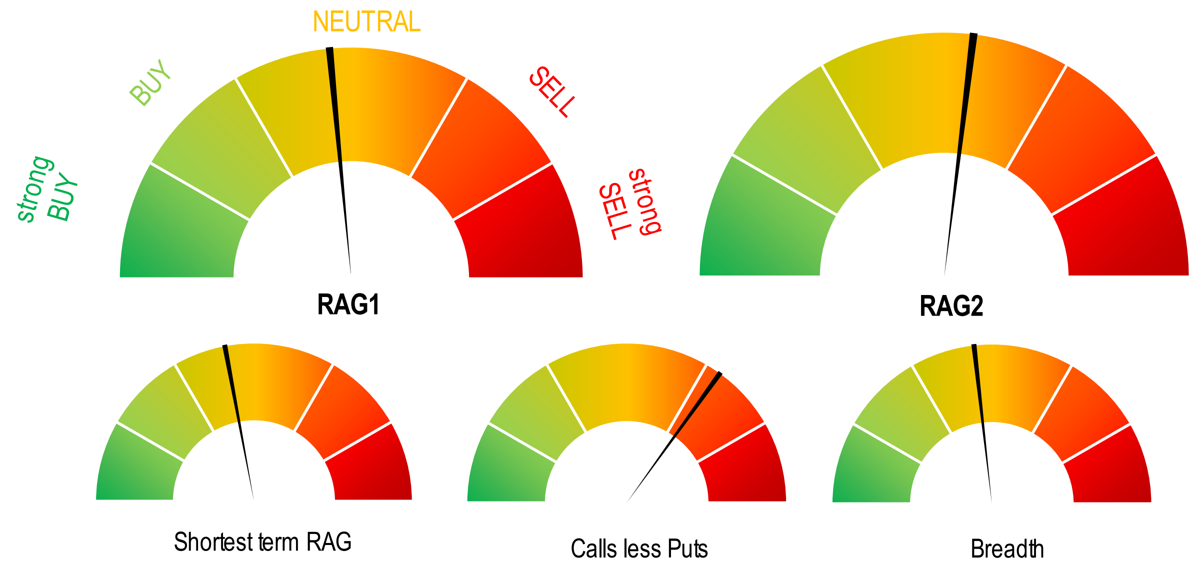
Source: Longview Economics, Macrobond

*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

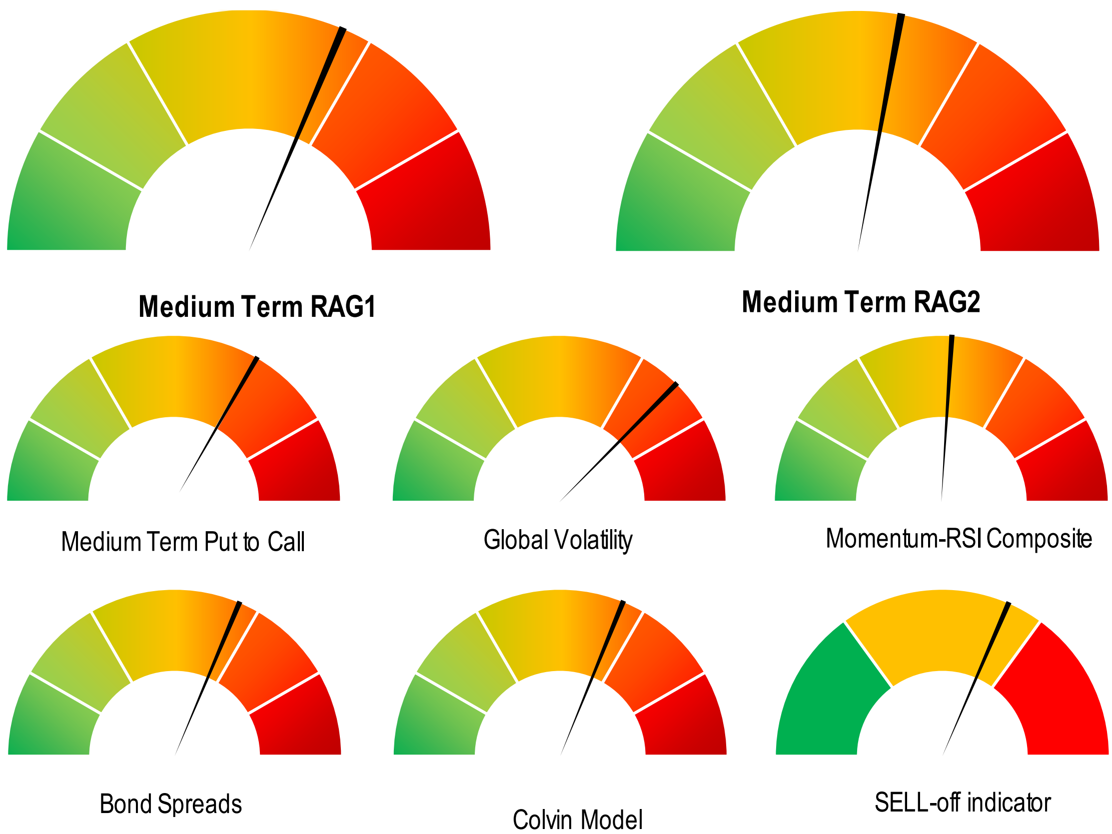
Section 1a: Summary of indicator signals**

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



Source: *Longview Economics*

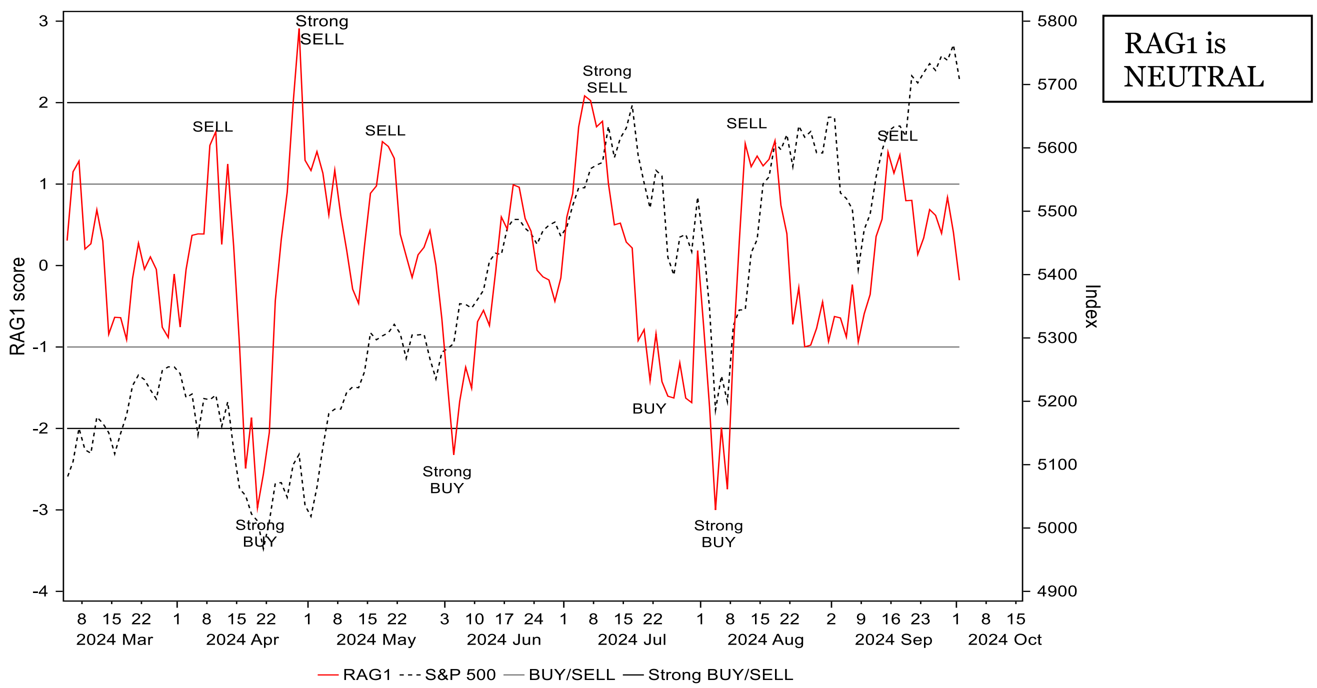
Fig 1b: Medium term models – shown as gauges using standard deviation bands



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

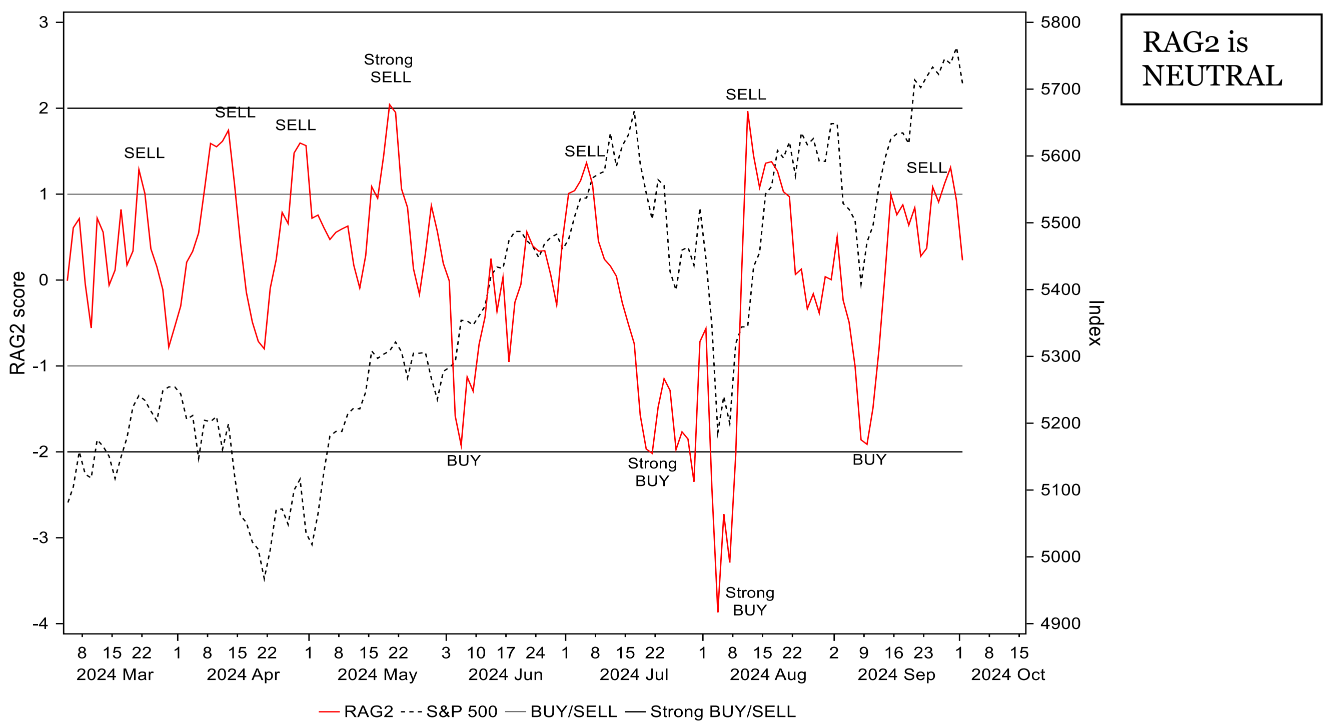
Section 2: Short term (1 – 2 week) trading models

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



Source: Longview Economics, Macrobond

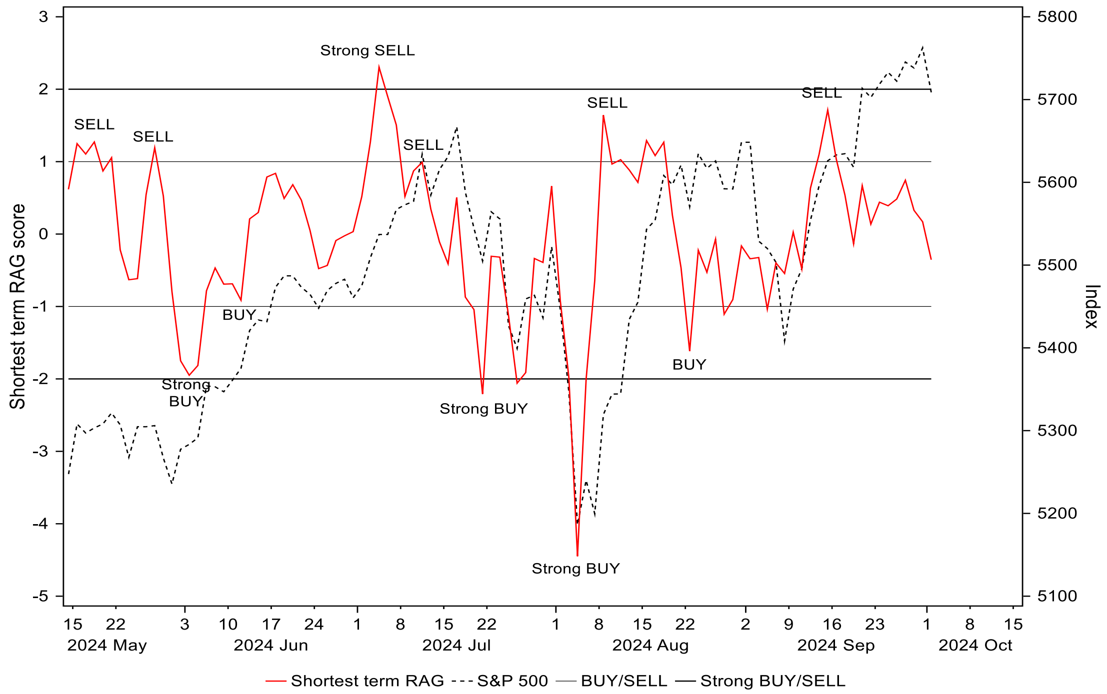
Fig 2b: RAG 2 vs. S&P 500



Source: Longview Economics, Macrobond

For explanations of indicators please see page 10

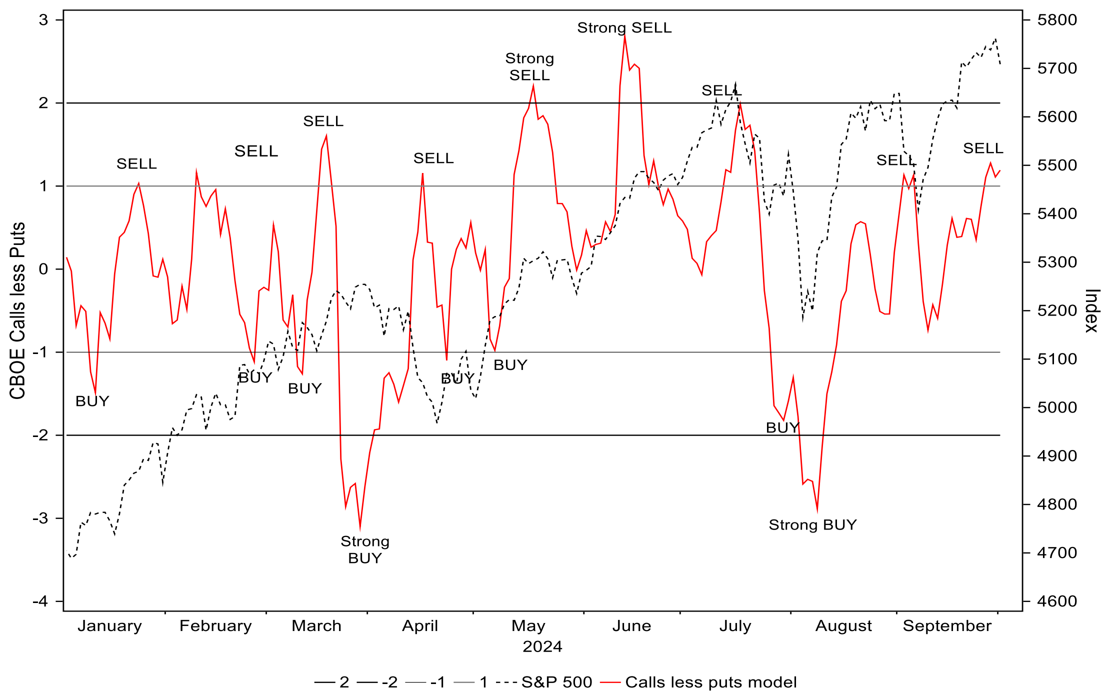
Fig 2c: Shortest term RAG (i.e. using a 3 day moving average) vs. S&P 500



Shortest term RAG is NEUTRAL

Source: Longview Economics, Macrobond

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

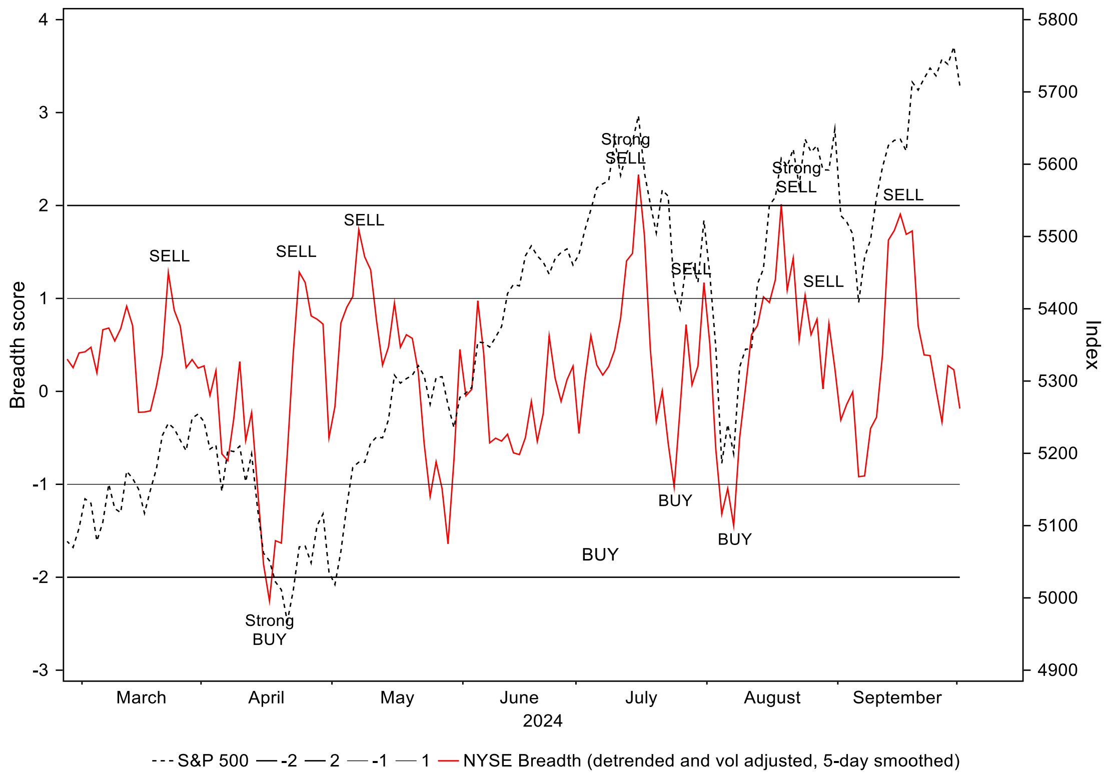


Calls less puts model is on SELL

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



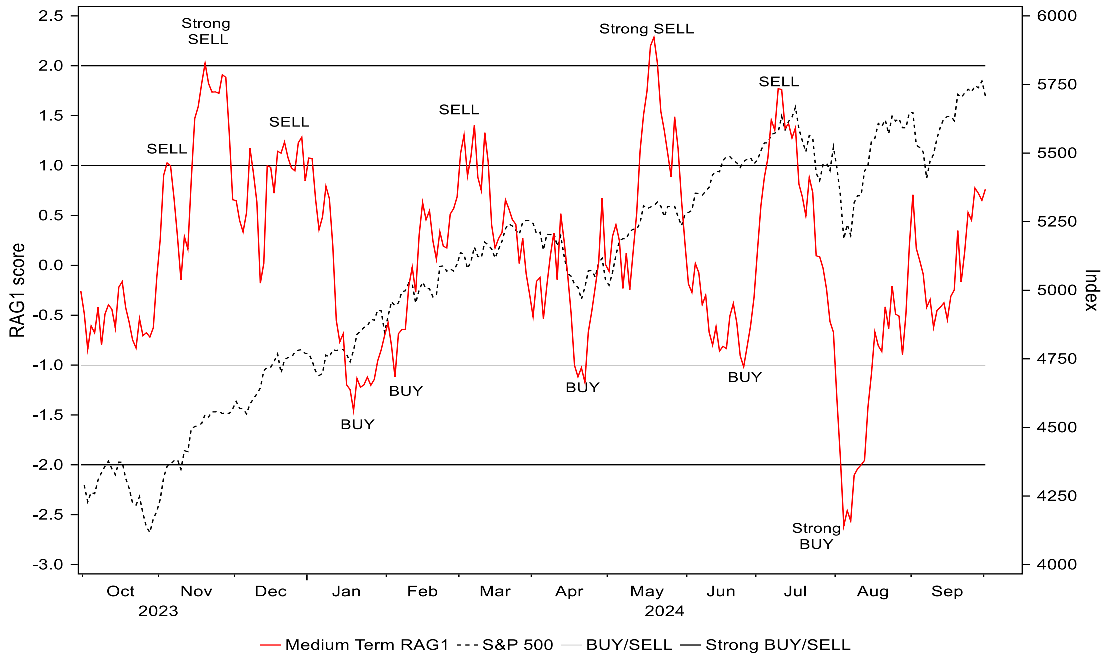
Source: Longview Economics, Macrobond

The breadth model is NEUTRAL

For explanations of indicators please see page 10

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

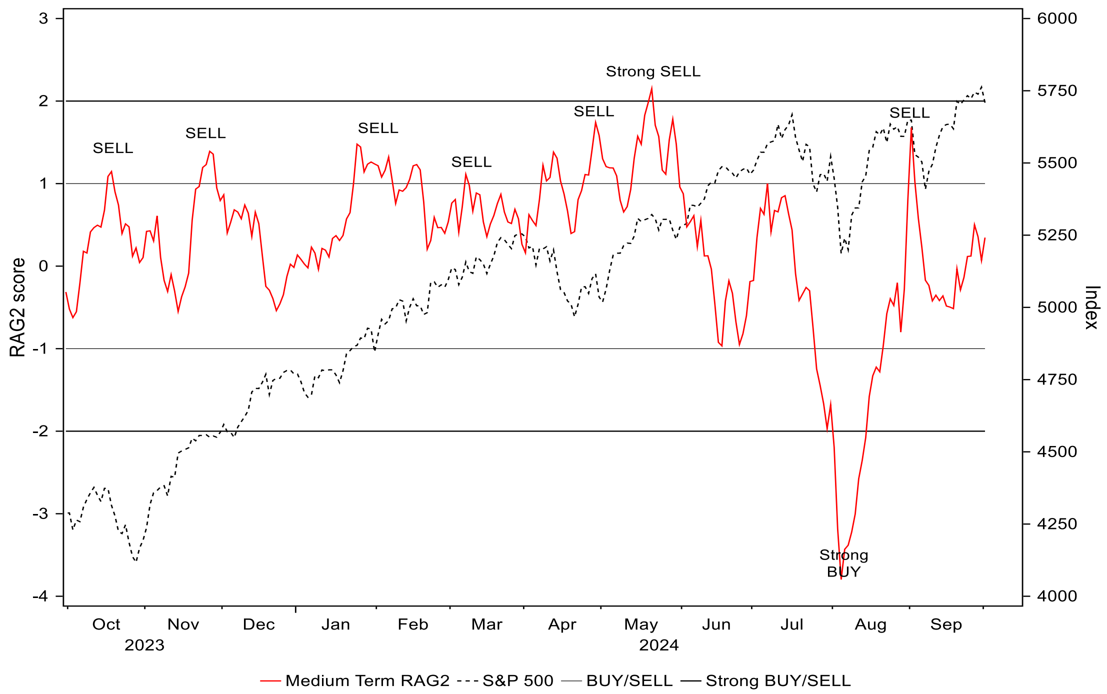
Fig 3a: Medium term RAG1 (1 – 2 month view) vs. S&P 500



Source: Longview Economics, Macrobond

Medium term RAG1 is NEUTRAL

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

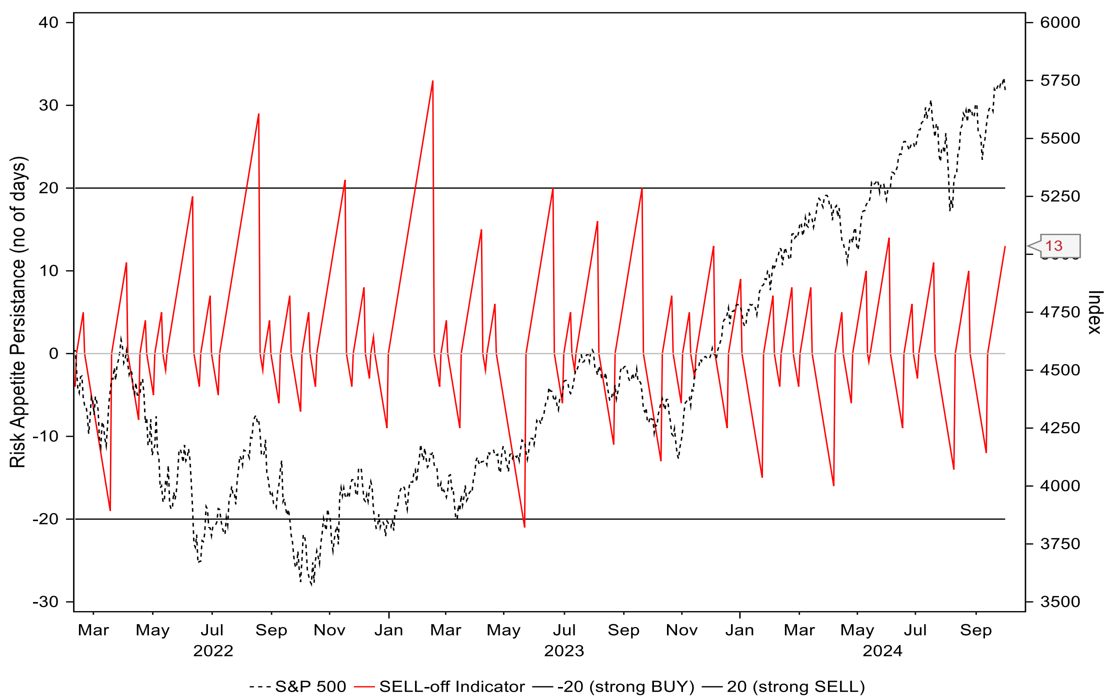


Source: Longview Economics, Macrobond

Medium term RAG2 is NEUTRAL

For explanations of indicators please see page 10

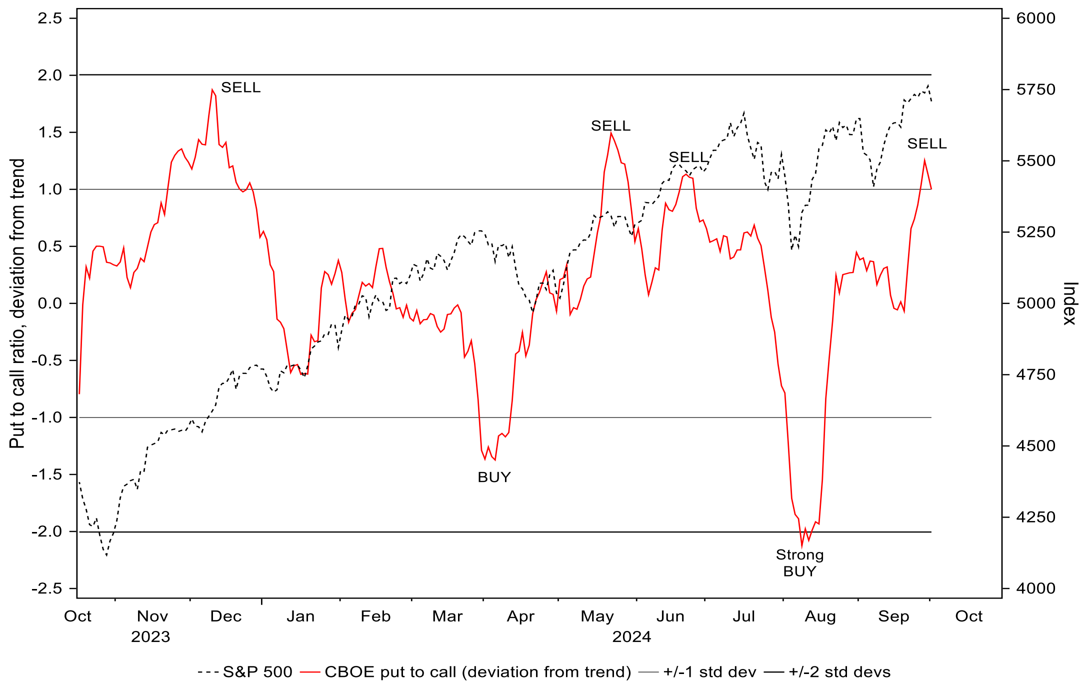
Fig 3c: SELL-off indicator (shown vs. S&P500)



Source: Longview Economics, Macrobond

The SELL-off indicator is NEUTRAL

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

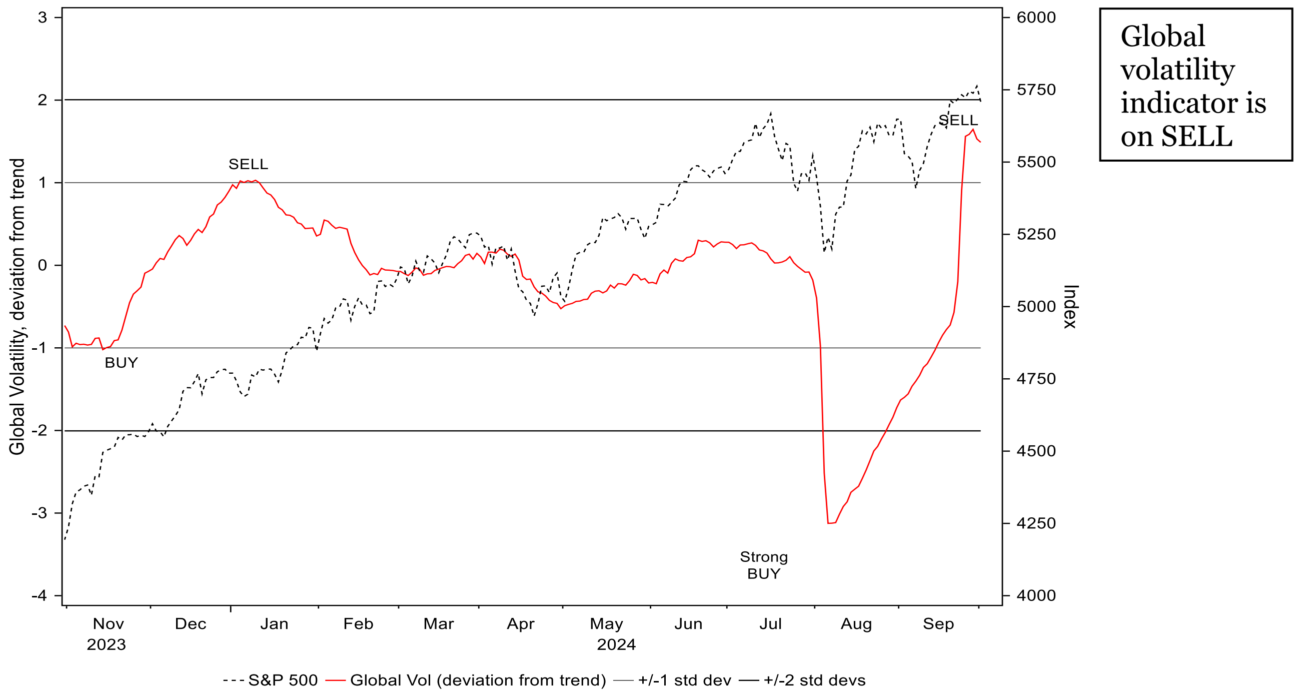


Source: Longview Economics, Macrobond

Medium term put to call model is on SELL

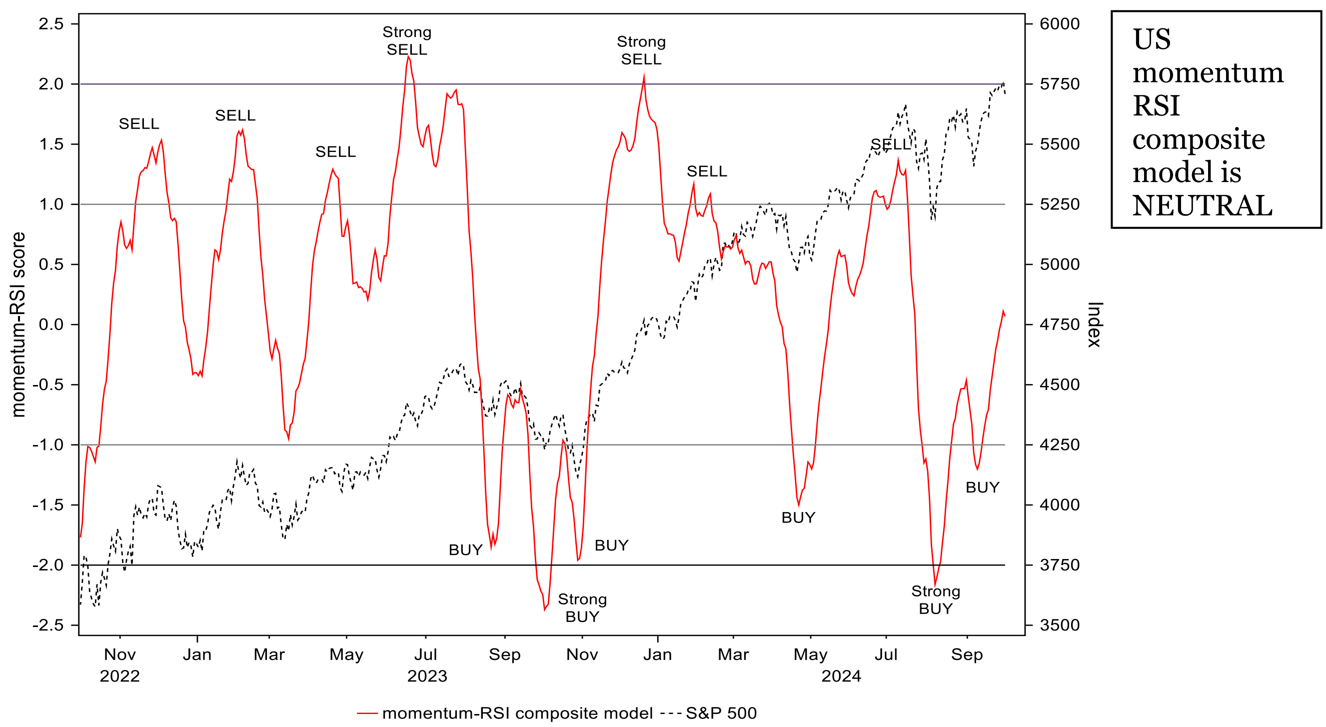
For explanations of indicators please see page 10

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

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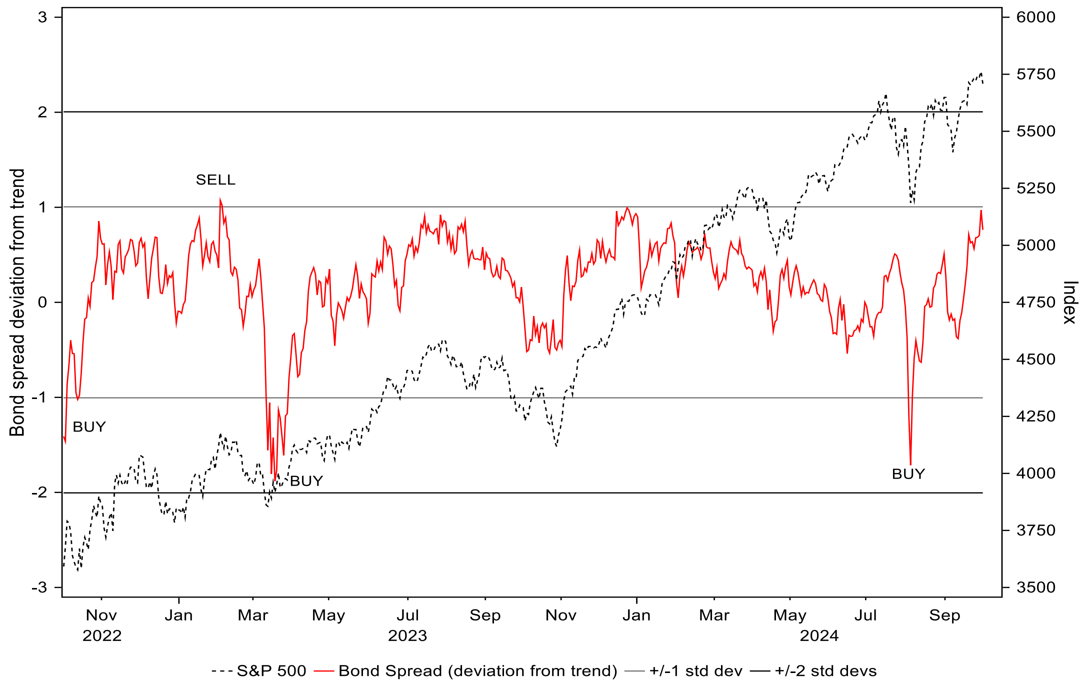
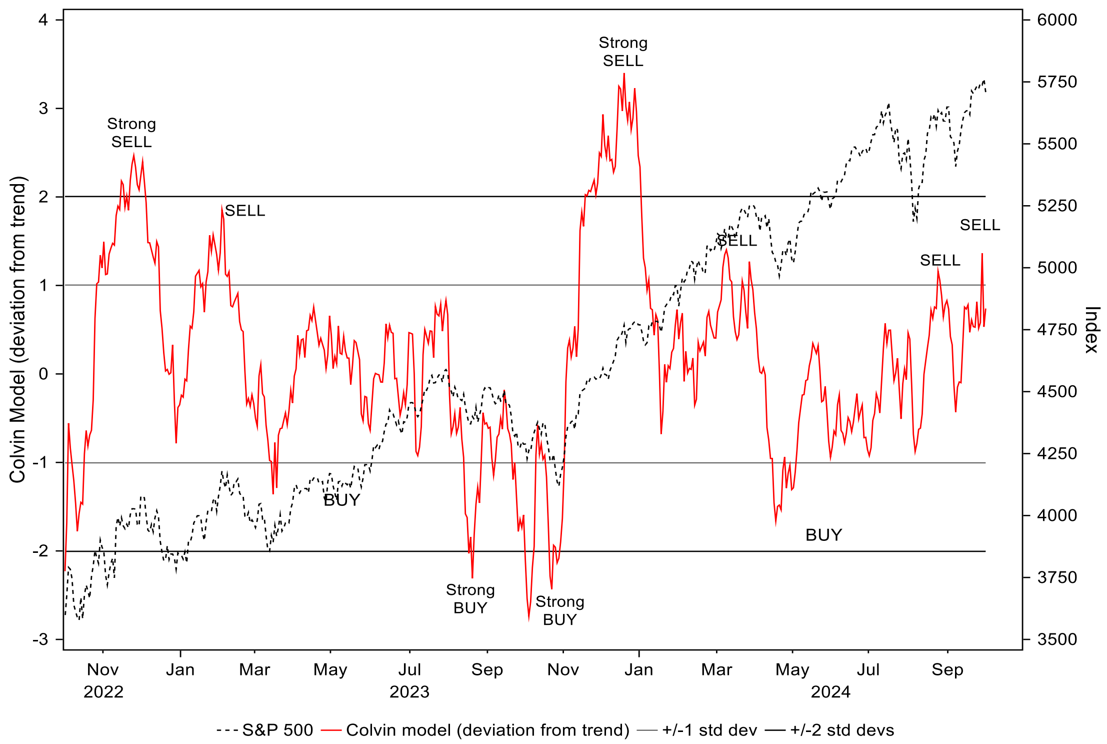
Fig 3g: High yield corporate bond spreads deviation from trend model vs. S&P500



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 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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