Market Update

Sector Rotation: July	
Technology	XLK
Consumer Disc.	XLY
Communication	XLC

Notable Breadth Data:	
SPX >50MA	60.79%
SPX >200MA	39.01%
Nasdaq >50MA	82.52%
Nasdaq >200MA	74.76%

Fixed Income Rotation: Q3	
Muni Bond	MUB
High Yield Corp.	HYG

Index & Sector Adaptive Trend	Up Trend	Down Trend
SPX	X	
QQQ	X	
XLF		X
XLY	X	
XLK	X	
XLV	X	
XLU		X
XLP	X	
XLI		X
XLRE		X
XLE		X
XLB	X	

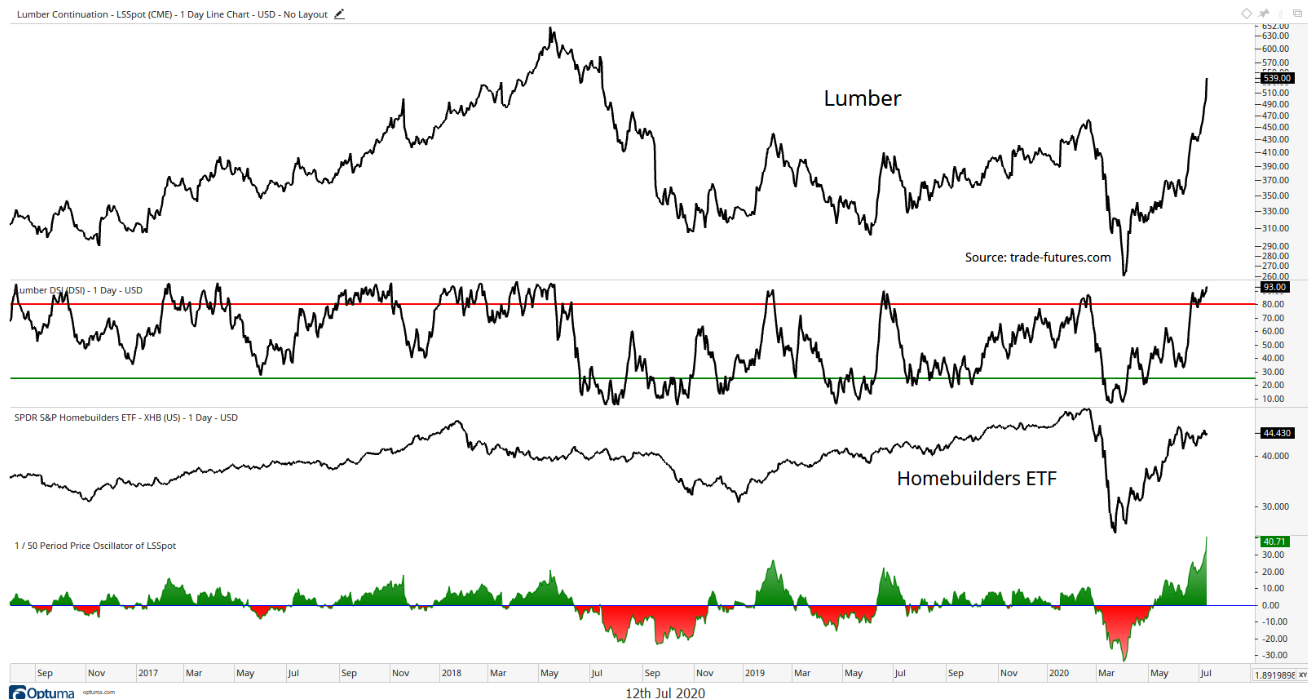
Daily Sentiment Index	% Bullish	5-day MA
S&P 500	85%	85%
Nasdaq 100	93%	90%
Nikkei	76%	73%
VIX	15%	18%
10yr Treasury	60%	60%
5yr Treasury	53%	52%
CRB Index	71%	74%
Gold	80%	86%
U.S. Dollar	35%	35%

Green<25% Red>80%

source; trade-futures.com

***Crude Oil**: remains below the March 13 gap. Sentiment has steadily declined, currently at 60% bullish after being above 80% in early June when price was at similar level.*

***Lumber**: Lumber futures have had an extremely strong rebound from the March low, up 105% through Friday and are now trading 40% above their 50-day moving average, the highest ten year high was set in early 2019 at 25%, before prices dropped back to the prior 2018 low, a decline of 30% in a couple of months. Since 1972, lumber prices have only been this stretched one previous time: 1993, after rising 40% above the 50-day, lumber rose another 12% before prices got cut in half as they moved swiftly lower from the March peak to the July bottom. Sentiment for lumber has also risen substantially, at 93% bullish, the highest level since the prior major peak in lumber back in May 2018. Homebuilder stocks are of course highly correlated to lumber prices, so if we do see a reversal lumber, it would likely produce negative price action for many homebuilder companies and the Home*



***SPX**: The S&P 500 is now 9.6% above its 100-day moving average. The Equity index hasn't seen a run like this since the Jan. '18 peak when it got to 9.8% above the 100-day MA. The one caveat we don't want to ignore however is that price got stretched based on this measure several times after the March '09 low, when price moved aggressively higher. Minor pullbacks of a few percent occurred when this happened after the March '09 low, but nothing significant. Price still sits below the June 10th low, before the 6% drop that began the multi-week consolidation. I'll repeat what I've said in several letters since then, until we can clear that gap and more-or-less the 3230-level high, equities are prone to whipsaw and risk/reward becomes less attractive. However, above that level then equities enter an air pocket of declining volatility and open air of lack of technical resistance back to the February high.*

***Breadth**: The breadth picture for the Nasdaq and S&P 500 remains mixed. The Nasdaq 100 has 81% of stocks above the 50-day MA but the broader Nasdaq Composite sits at 57%, showing the strength of those largest companies. The average Nasdaq 100 stock is 10% below its prior 52-week high, weaker than it was in June even though the index has powered on to new highs. The percentage of S&P 500 companies at a 6-month high peaked just over 8% but finished Friday at just 3.9% even though the index closed at five week high (but still below the prior June high). We're seeing a broadening out of winners and losers with the average 10-day correlation of S&P stocks at 0.47, the lowest level since April 24th. This decline in correlation gives stock pickers an advantage to find opportunities for alpha capture.*

***Momentum**: The divergence concern remains with the Nasdaq, just 39% of S&P stocks are showing a bearish divergence and 27% are showing a bullish divergence. 55% of Nasdaq stocks currently have a bearish divergence and only 10% have a bullish momentum divergence. The Energy sector shows 50% of stocks with a divergence, financials also have a higher amount than others.*

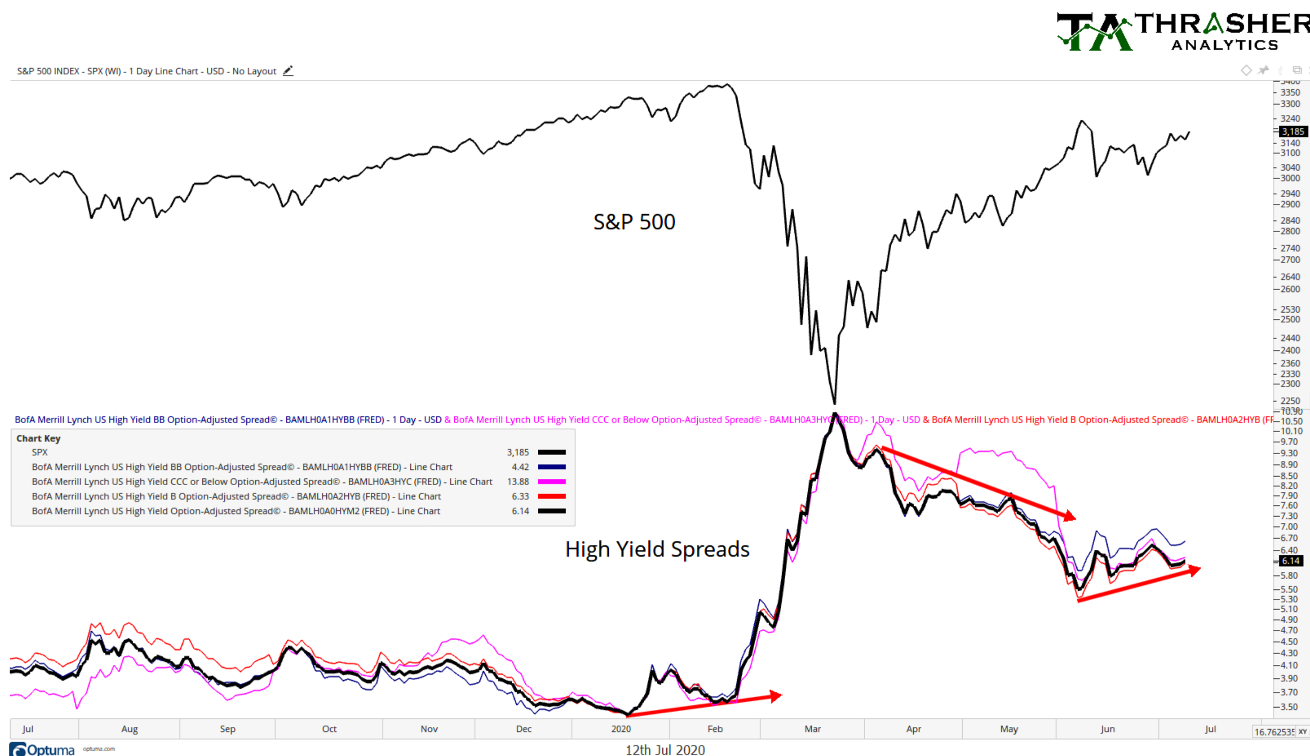
***Coronavirus**: Without diving into the deep hole of virus data and pretending to be an expert, when it comes to financial markets what matters most is what the market deems important and right now the rising infection data has not seemed to face equity traders. Charlie McElligott of Nomura referenced in a recent podcast interview who speaks to clients that pay experts for special insight into the infection data, "out outside of the US – so particularly in Northern Italy and China – there is some focus being paid to hospital studies from infectious disease teams that are showing that the type of COVID patients that they are seeing now are very different from the ones they were seeing*

Weak amounts of the virus versus that of Phase 1." So while infection data is rising, maybe these international studies suggest the death rate will not stay as correlated as we saw earlier this year and if death rate don't rise materially then potentially the risk of another economic shutdown stays off the table in the U.S.

***Leadership**: Cloud tech, software, biotech, and semiconductors continue to move higher, finishing last week at or near their highs. This is where buyers have been focused and squarely paints the heroes of this market's story.*

***Volatility**: the elevated VIX has held back institutional money managers from deploying more capital to equities with their risk models acting as a leash pulling back the dog. A continued move lower in volatility, especially realized vol will 'unleash' the beast and provide fuel for equities moving higher. This is a big deal and could allow institutional investors to join the Robinhood party, increasing equity ownership. The VRT has moved up, but still remains below the necessary threshold to warn of a volatility spike. VVIX has been under greater pressured than spot VIX, finishing last week at its 19th percentile while VIX is at its 22nd, 9-day at 14th and 3-month at 28th. The VIX future curve has spot VIX at a 3.7 point discount to 3-month volatility, the largest spread since December 2016. A big part of this spread is due to the election kink that shows up due to extremely high premium being given to volatility around the election. The market seems to have high expectations that November will bring high volatility like it did (briefly) in 2016.*

***Bonds**: High Yield Spreads have been trending higher, each rating spread is now well off its prior June low as shown in the chart below. Is the bond market showing some stress and concern over the upcoming Q2 earnings season? Maybe. If we see equities break out above the June high and economic data continue to improve, the spreads needs to end this trend of higher-lows and begin relaxing again as they had been doing since March, taking down the premium being demanded for high yield debt.*



***Gold**: The entire world seems to be focused on gold right now. I last wrote about gold in April, just as it began to consolidate for over a month and went nowhere. Now it is risen out of its consolidation and challenged $1800/oz, the '12 high. There's little fundamental or technical argument that can be made against gold, but one issue I'd take with the precious metal is just the fact that it doesn't seem anyone out there doesn't love gold right now. Sentiment seems hot with the $1800 breakout which we closed on Friday at $1802, just two dollars above the key level. If this level doesn't hold, which it very well may, but if it doesn't then I think there's a heavy number of recent buyers who will be quite upset and could cause a short-term move for the exits. If we do see $1800 hold then the breakout looks*

I'll be back next Sunday with a chart-focused letter.

Best Regards,
Andrew Thrasher, CMT

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