Bears vs Bulls, or vice versa?

A Global Macro Review

by

stockcuberesearch

Contents

Summary

Equity Indices:

The regional leaders maintain strong uptrends; however, there are now fewer indices outperforming the S&P 500.

Equity Sectors:

The leadership is also becoming thinner at the sector level, as defensive sectors lose downtrend momentum relative to the cyclicals.

US Dollar:

The dollar has rallied to correct the extension from its 2009 downtrend, highlighting the possibility of basing action.

US Yields:

US 10yr Yields remain beneath 4%, the level above which we anticipate a switch away from equities. The US Yield Curve also continues to highlight favourable short-term conditions.

Sovereign CDS Spreads:

Sentiment towards sovereign debt has worsened, highlighted by basing action outside Europe and acceleration within.

Conclusion & Strategy

- The trends of regional indices are generally deteriorating relative to the US in the short-term, as the leaders unwind their extensions.
- Whilst economic conditions remain broadly beneficial for markets, the headwind of negative sentiment is beginning to create doubts.
- We anticipate a period of range-bound trading with a downward bias for the next 3 – 6 months.
- It will be crucial to avoid being whipsawed by the volatility.
- Our strategy is simply to monitor regional and sector indices relative to the S&P 500: we are broadly looking to buy non-G4 indices against the S&P 500 but will not do so until there is evidence of uptrend reassertion.

The Case for the Bears

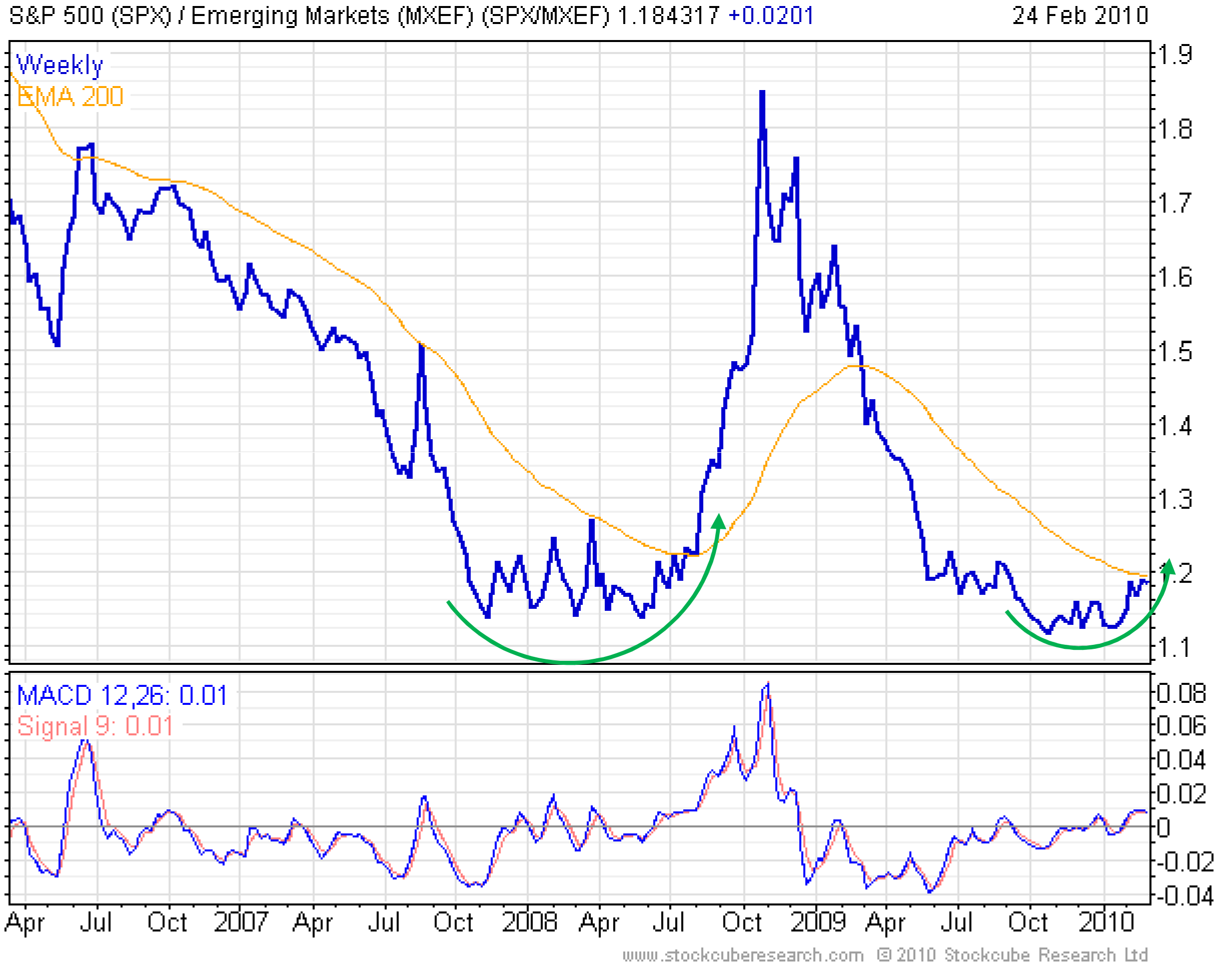
- The Emerging Markets have broadly lost momentum having unwound the 2008 / 2009 extension.
- Defensive sectors becoming range bound relative to the cyclicals as they attempt bases.
- US Dollar has put in a higher low, highlighting the possibility for basing action.
- Sovereign CDS spreads basing / accelerating highlight bearish sentiment.

Country Leadership

The Emerging Markets have broadly lost momentum having unwound the 2008 / 2009 extension.

This chart shows the S&P 500 has lost downtrend momentum relative to the broad EM group and has corrected back to its 200 day moving average.

The ratio may attempt base formations as in early 2008; the bottom window shows that momentum is improving.



Country Leadership

Brazil has lost momentum from its uptrend relative to the S&P 500.

The chart to the right shows the ETFs ($) as a ratio, which highlights the potential failure beneath resistance. The ratio has corrected to its 200 day moving average.

Malaysia has also lost momentum from its uptrend relative to the S&P 500.

The chart to the left shows the ETFs ($) as a ratio, which highlights the potential top formation. Similarly, the ratio has corrected to its 200 day moving average.

Defensive sectors vs Cyclical sectors

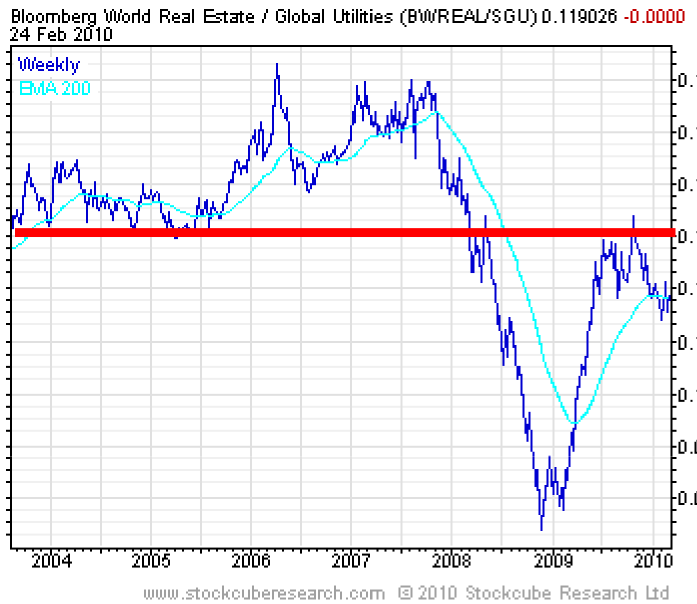
Within equity sector indices, trends are also losing momentum. The ratios of defensive sectors relative to cyclical sectors are losing momentum as shown in the chart to the right, which shows possible basing action in the ratio of the Global Utilities index relative to the Global Materials.

The ratio has lost downtrend momentum above support at its 2008 lows and exhibits bullish momentum divergence.

Defensive sectors vs Cyclical sectors

The chart to the right shows a Global Real Estate index relative to the Global Utilities index.

The ratio has rallied into resistance from the bottom of its range in ‘pre-Crunch’ times and has subsequently unwound to its 200 day moving average.



The Materials sector in India has rallied back into resistance from the top of its range in ‘pre-Crunch’ times.

Although the short-term uptrend currently remains firm, short-term momentum characteristics indicate some momentum loss.

US Dollar

Although it didn't reach 2008 levels, the US Dollar index has rallied in 2010, to correct its extension from its 2009 downtrend.

In the short-term, momentum has become more positive but now the index is already becoming extended from its 200 day moving average to the upside.

Sovereign CDS Spreads

The sentiment towards sovereign debt has generally worsened during 2010. The focus has clearly been on European contries but globally CDS spreads have been rising.

The chart to the right, shows the Spanish CDS, which has rallied to retest its early 2009 high.

The Australian CDS spread, below, is much lower in its range but also shows evidence of basing action.

The Case for the Bulls

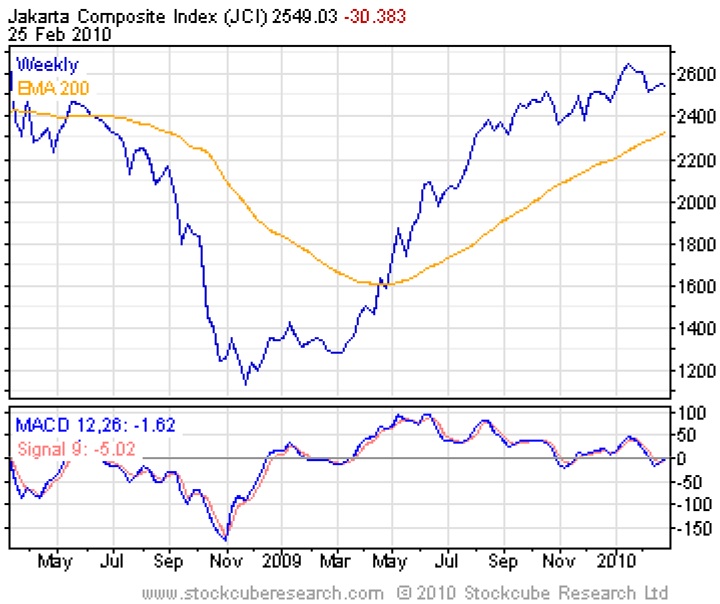
- The uptrends of the global equity leaders remain intact.
- US 10 yr Treasury Yields remain beneath 4%, the level above which we anticipate US equities will struggle.
- The US Yield Curve highlights the current bullish conditions for global markets.

Uptrends Broadly Intact

These two charts show that the leader's uptrends remain intact.

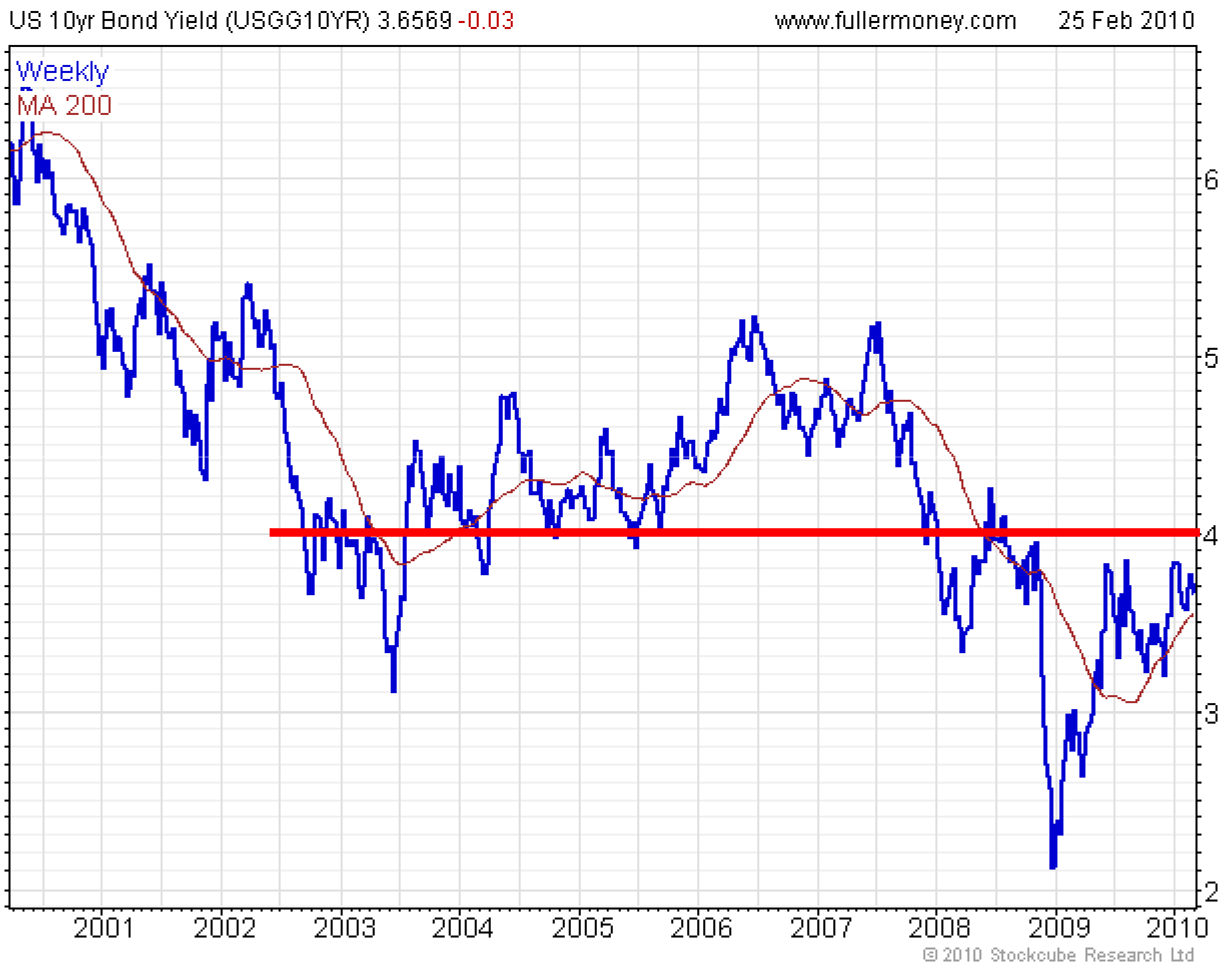
The chart to the right shows the Indonesian JCI, a leader in Asia, maintains its uptrend and currently consolidates its recent breakout.

Similarly, the chart beneath shows the Chilean (IPSA), a Latin American leader, maintaining its strong uptrend since the October 2008 low.



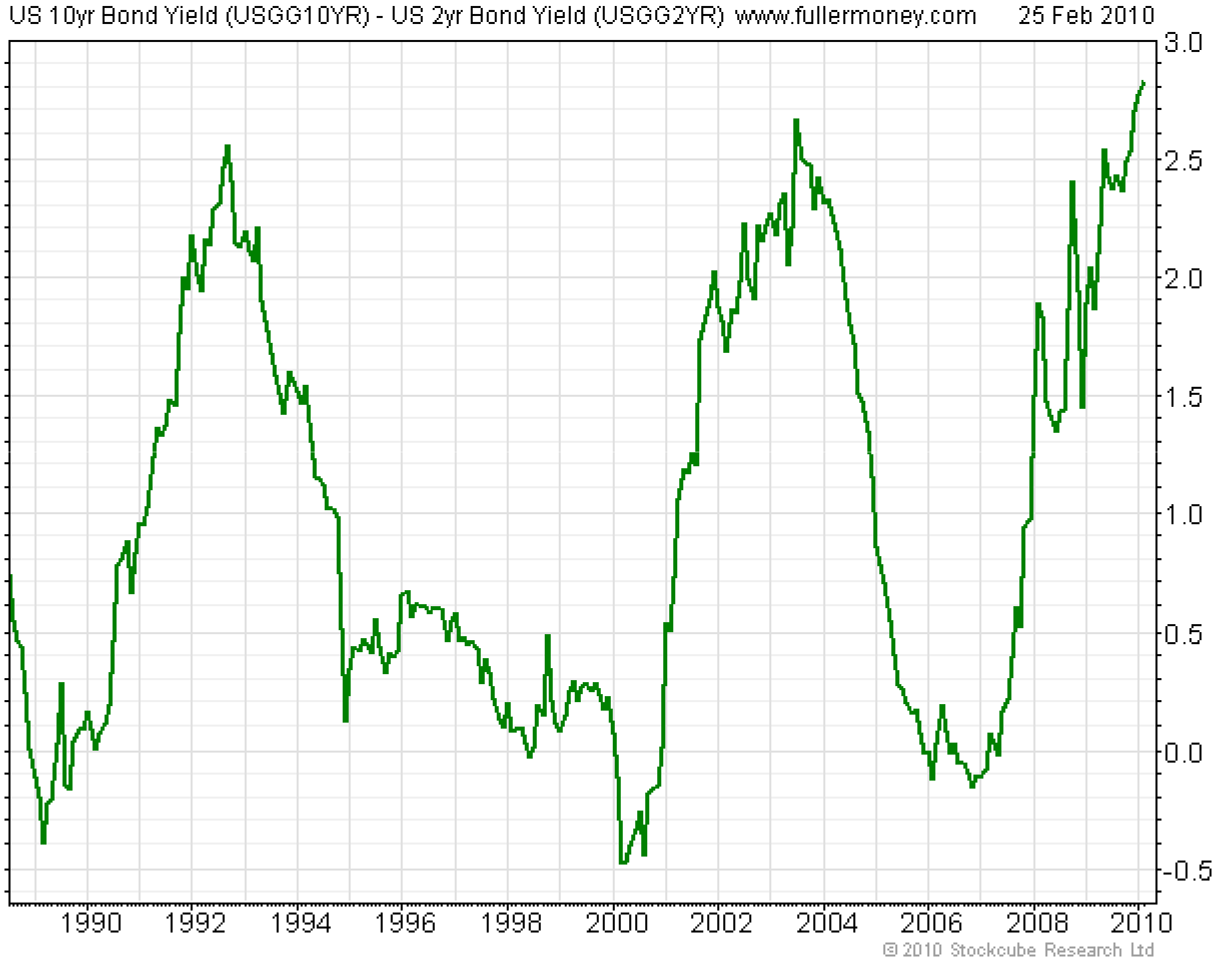
US Yields

The US 10-yr Treasury yield remains beneath 4%, the level above which we anticipate US equities will struggle.



US Yields

The US Yield Curve extends its rally through the previous highs at 2.5. This highlights the bullish conditions for global markets in at least the short term.



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