A Month-Long Week

Comrade Lenin used to quip that in history "there are decades where nothing happens, and there are weeks where decades happen."

Change the decades to months and weeks to days and he might as well have been talking about markets. Cause I don't know about you but I feel like last week lasted all quarter…

According to Factset, the Dow posted one of its worst weeks in history.

Periods of Dow's worst weeks (week ended)	Weekly % Change
1) Oct. 10, 2008	-18.15
2) July 21, 1933	-15.55
3) Sept. 21, 2001	-14.26
4) May 17, 1940	-14.21
5) Feb. 28, 2020	**-13.56**
6) Nov. 8, 1929	-13.52
7) Oct. 23, 1987	-13.17
8) April 8, 1932	-12.86
9) Oct. 7, 1932	-12.42
10) Sept. 16, 1932	-11.93
11) Oct. 2, 1931	11.82
12) Dec. 22, 1899	-11.36
13) Nov.19, 1937	-11.24
14) June 20, 1930	-11.12
15)May 27, 1932	-10.95

Source: Dow Jones Market Data

I was expecting a selloff and volatility due to the absurdity in positioning and sentiment but I have to say, I was not expecting it to play out quite like this. But that's the market for you. Always finding a way to surprise...

Luckily, we were decently positioned and didn't take it on the chin too badly. Our long bonds and heavy cash position mostly hedged out our puking equity plays. We went from being up roughly 14% YTD to an even 10%. I'll take it, considering the SPX was plumbing double-digit YTD losses before Friday's end of day ramp up.

The big question on all of our minds now is "where do we go from here?"

Is this a dip that should be bought or the start of something more sinister?

That's an incredibly difficult if not completely impossible question to answer at the moment. And that's because unlike the yield curve inversion scare last year, the repo-rate hysteria, or the following consensus recession calls, all of which could be easily disproved if one knew where to look. The coronavirus represents a real potential left-tail risk event.

COVID19 could very well end up being the catalyst that pushes our hyper-leveraged global economy over and into the abyss. Or not.

It depends on how it all unfolds. And right now there's no way to know. Like I said in Friday's Musings, this virus has blown wide the cone of plausible outcomes.

So while a selloff had become inevitable because of the rampant speculation and complacent risk-taking. The extremes at which it occurred are due to the market slowly waking up to the new reality we now find ourselves in.

In the short-term, we should expect the market to swing wildly as we're now firmly in a bull volatile regime. But looking out longer-term, the future is murky… the potentialities many…. And the driving variables numerous.

We started 2020 with leading economic indicators finally turning up from their deep troughs reached last year. This would have led to at least one final boom in markets and the global economy.

COVID19 already ensures that this V-shaped recovery will be U-shaped at best, and L-shaped at worse.

This is because **in acting to minimize the human toll of this virus, we maximize the economic one.**

And failure to do the former is likely to ensure a much greater cost to both down the line. It's a damned if we do, damned if we don't, situation that we now find ourselves in.

I'm writing a note where I'll dive into much greater detail on the potential costs and outcomes of the virus later this week. Today, I want to mostly focus on the question of where markets are headed over the short-term.

Technicals: Trapped Bulls

Bulls trapped in ill-timed longs, bears kept out of good shorts, HUGE engulfing bearish reversal candles, massive damage to the tape, lots of buried bodies, and a potential start of a cyclical topping process.

These are a few descriptors that speak to the battering that was done to the technical picture last week.

Let's take a look at the SPX first.

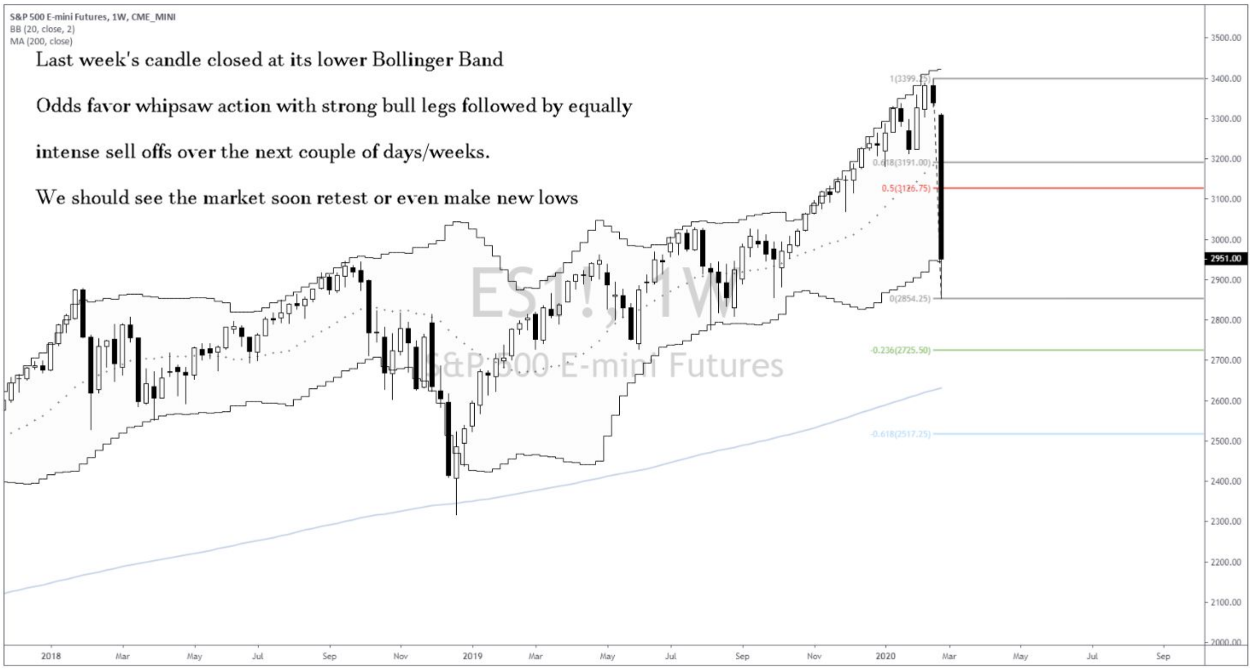
Last week I talked about how the market was in danger of putting in a very bearish engulfing pattern on the monthly prints if it failed to strongly recover into the end of the week. It did not and we now have a strong sell signal bar on the monthly chart of the S&P.

February's candle took out all of the market's gains since September, closing below the 3,000 support level. This is following January's bearish Doji candle after a four-month-long buy climax.

On a weekly basis, the SPX closed at its lower Bollinger Band. The market is incredibly oversold on a short-term basis.

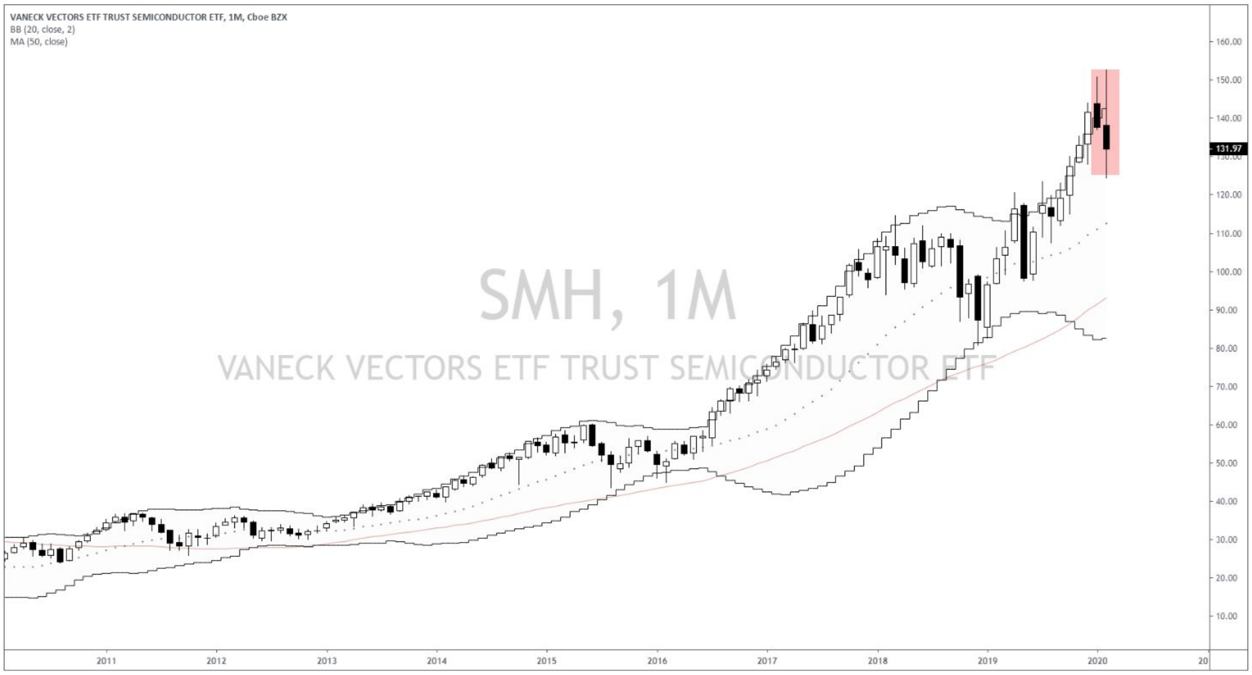
We should expect fast whipsaw action in the days/weeks ahead as trapped bulls get out of their underwater longs on bounces and bears take profits on their shorts.

But odds favor a retest of last week’s lows within the next couple of weeks.



Semis (SMH), our bellwethers and general leaders of broader market trends, also put in a bearish engulfing bar for February. This is following January’s bear bar, a full reversal after trading above its monthly Bollinger Band, and a micro double top pattern.

Odds favor followthrough to the downside on the monthly timeframe.



Equally brutal technical damage has been done to the leaders of this market. Microsoft (MSFT) put in a monthly bearish engulfing reversal candle following a parabolic rise and a move above its upper monthly Bolling Band.

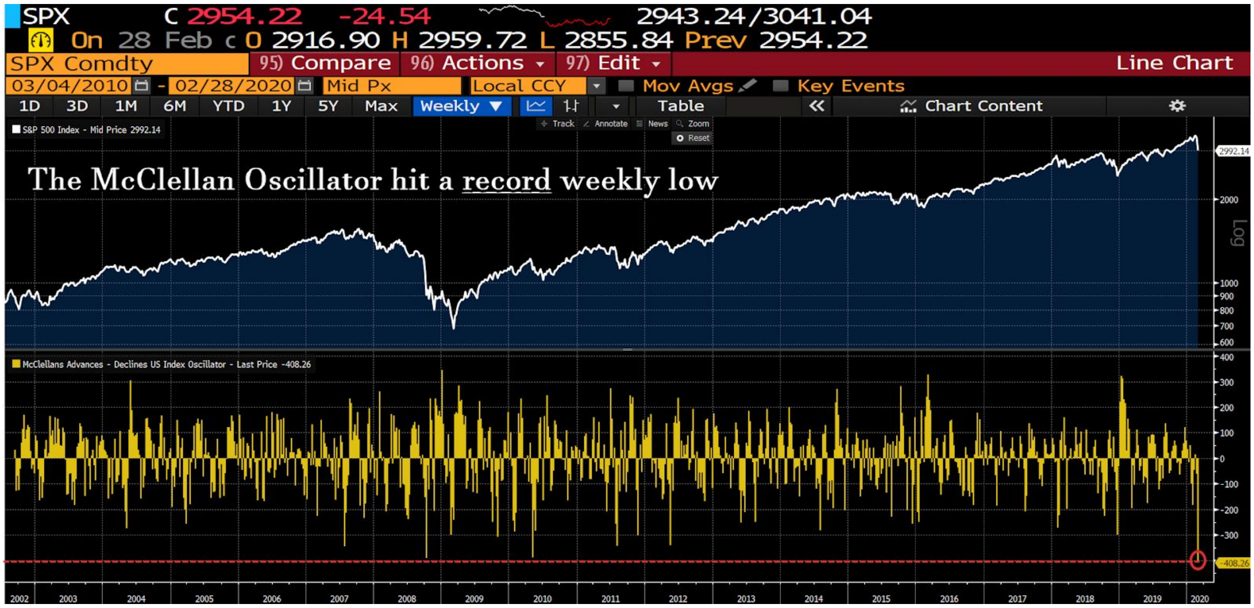
> "Parabolic advances usually go further than you think, but they do not correct by going sideways." ~ Bob Farrell

JP Morgan (JPM) reversed all of its gains from its breakout last year, closing below the neckline of its H&S continuation pattern.

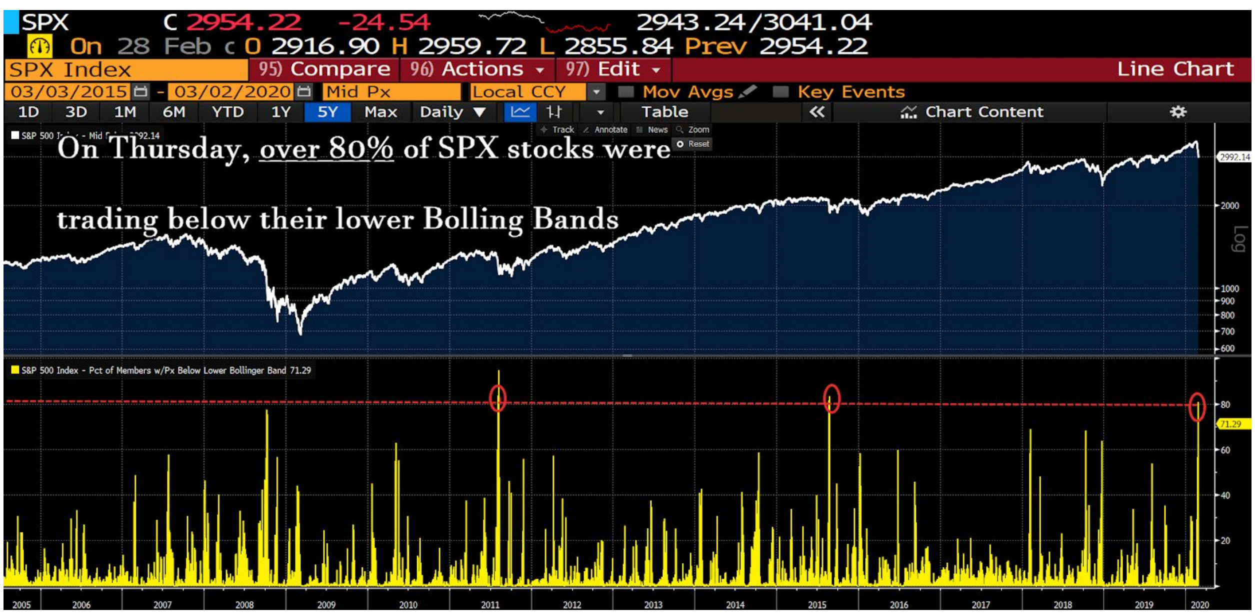
Gold put in a bearish reversal bar for February with a long tail on top. It finished the month below its open the critical 1,600 level it had broken above just last week. It’s still in a clear technical uptrend but we could see some extended consolidation here.

Internals: Record-Breaking

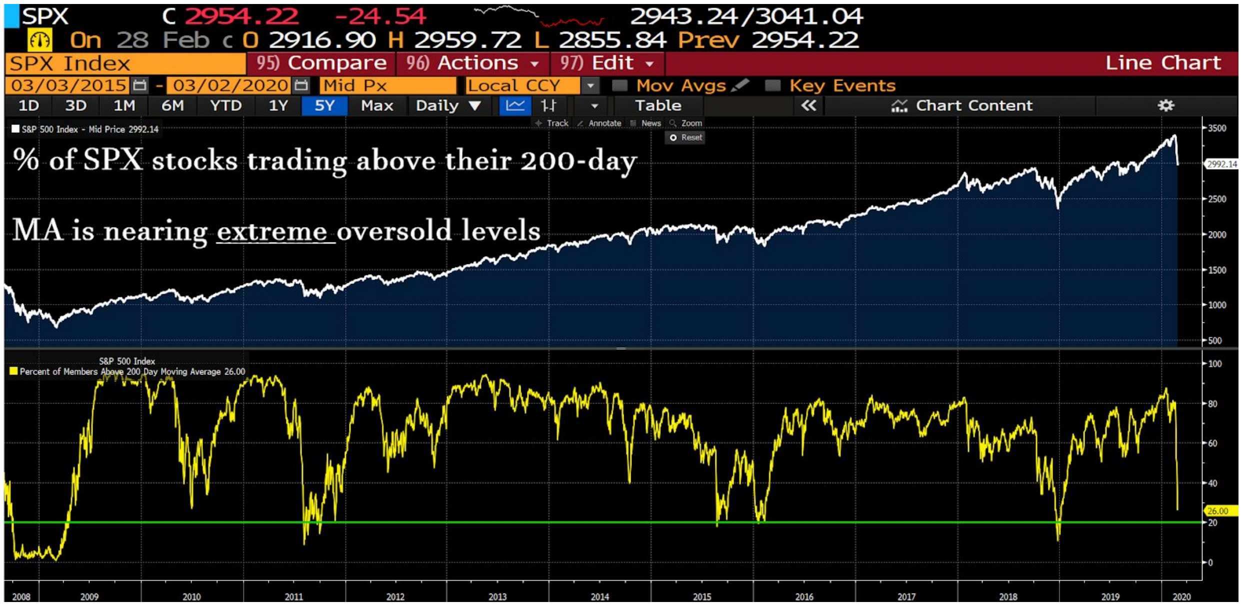
The McClellan Oscillator, which measures advancing versus declining issues hit a record low last week.



At one point last week over 80% of S&P stocks were trading below their lower Bollinger Bands. That's only happened two other times over the last 15-years.

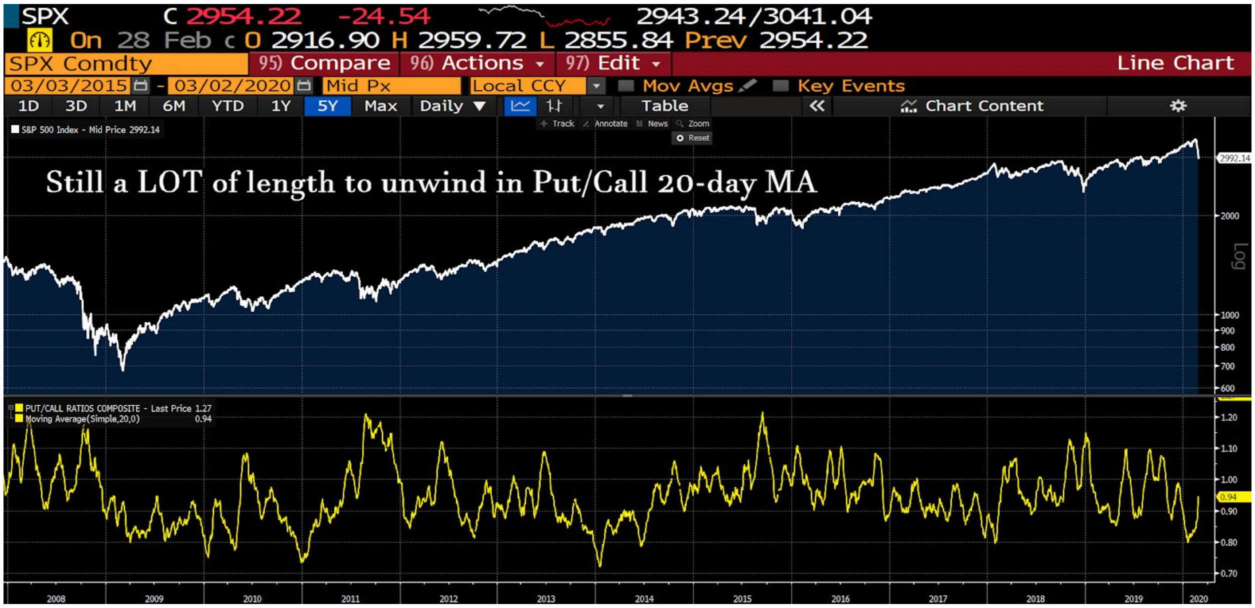


The percent of stocks now trading above their 200-day moving average is at 26%. 20% or below typically marks the bottom of selloffs outside of recessions.

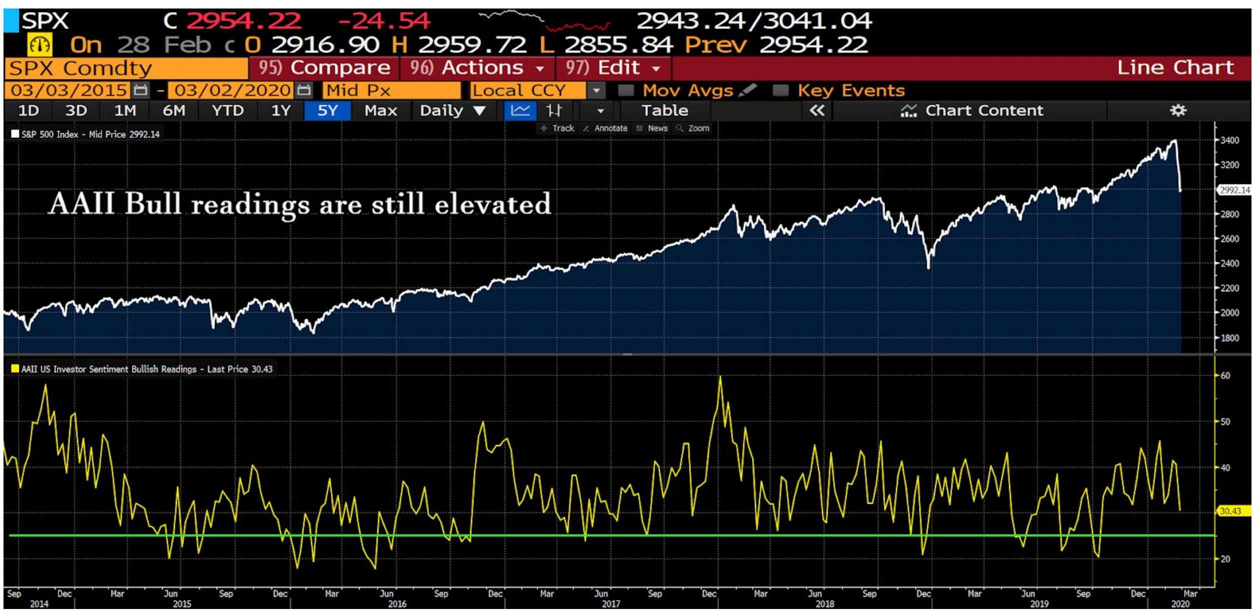


The 3-month Put Implied Volatility on the SPX hit an 8-year high on Friday as investors panic bought protection into the close.

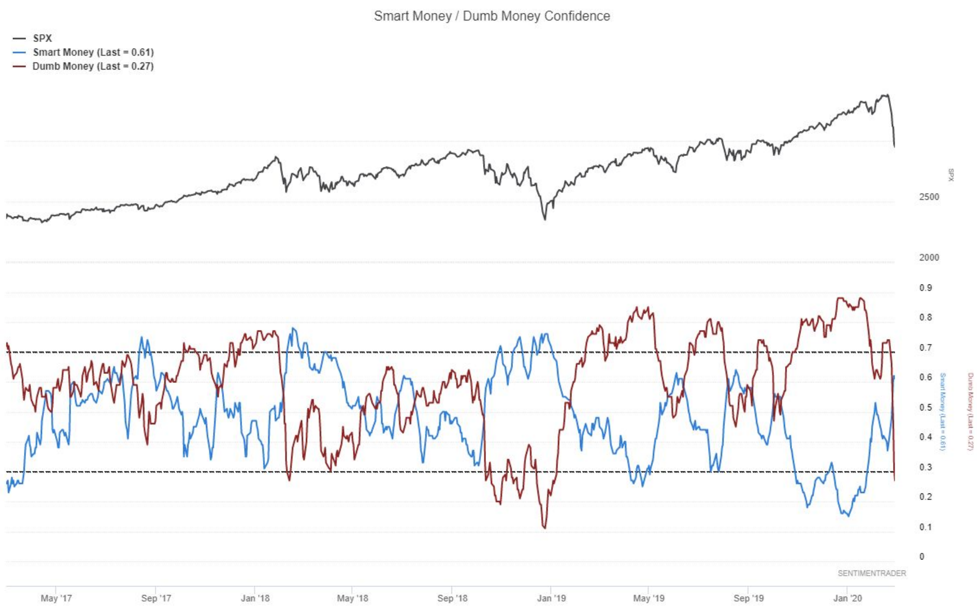
A long-term look at the Put/Call 20-day moving average shows there's still plenty of length that needs to be unwound.



AAII Bullish readings are still above the sub 25% levels that typically denote a bottom in sentiment is in.



The Smart / Dumb Money Confidence spread is reverting from extreme levels but still not giving a sentiment buy signal. We want to see smart money well above the 0.7% level.



Conclusion: Chop & Vol

We're deeply oversold in the short-term but we can always become more so. With that said, we're likely going to see the market whip back and forth over the next couple of weeks.
The long-term charts highly favor more sideways to lower action over the following months. It'll likely be at least that long before we have any type of visibility on how this virus will play out, as well.

A bull volatile regime is a good trading environment but not a good investing one. This just means that going forward the whippy price action is going to favor shorter-term tactical swing trading versus long-term positioning.

Of course, if we do somehow get more clarity on the virus soon, and it's positive… then we'll have to expect the rally of a lifetime. That's because we now have yields at all-time lows, risk premia spreads that are nice and wide, central banks a loosening, and governments getting fiscal.

I'll be writing more on the topic this week but I'm currently of the belief that the market is still being too sanguine over the risks this virus represents. I believe the risks of recession within the next 12-months have risen considerably.

If that ends up being the case, then the market may very well be starting the topping process. Market tops last 10-months on average before an official bear market kicks off.

For the first time in a long time, I'll probably start building up a short book over the coming weeks. That is if the situation with the virus doesn't dramatically change for the better.

I'm still willing to play some trades to the long side, such as the TNK trade I pitched on Friday. But, I'll be sizing smaller and will be quicker to take profits.

A number of old industry stalwarts have triggered major sell signals on their monthly charts. Take XOM and BA for example. I wouldn't be shorting in the hole but will look to take some shots to the short-side after large bounces.

We took profits on our 200% of NAV long bond position at the end of last week. Bonds are now incredibly overbought on a short-term basis, and we should expect them to retrace in the next week or two. We're back at our neutral 50% position for now. Our Core gold position has also been zeroed out. I'll re-up it if it can get back above the 1,600 level.

The Four Pillars Portfolio		2019	YTD			
		27.04%	10.01%			
The Core	Fixed Allocation	Market-Timing		Net Position		
Large Cap Equities (/ES_H or VOO)	25%	-25%		0%		
Short-term Bills (/ZT_M or VGSH)	25%	0%		25%		
Long-term Bonds (/ZB_M or TLT)	25%	0%		25%		
Gold (/GC_M or GLD)	25%	-25%		0%		
Big Bets	Thematic	Cost Basis	At Risk	Notional %	Risk Point	Last Price
Albemarle (ALB)	Renewable/value	$69.71	Above B/E	5%	$74.00	$81.85
Centrus Energy (LEU)	Uranium Bull Cycle	$6.69	B/E	7%	$6.00	$7.98
Deutsche Bank (DB)	Europe rebound/value	$8.45	B/E	7%	$8.45	$8.72
Square (SQ)	Growth play	$70.21	B/E	9%	$70.21	$83.33

That's all I've got for now. I'm working on a number of reports that will be getting sent out later this week!

Hit me up in the CC if with any comments/questions.

Your Macro Operator,

Alex