A Market Note: Price Gets Made At The Margin...

I've got a short and sweet one for ya. Just wanted to outline (again) why I think we're likely in the bottoming process and about to embark on a multi-week rally, at the *least*. Along with what we need to look out for as a signal.

Here's what's I'm tracking:

Sentiment/positioning at bearish extremes:

- BofA Bull & Bear nailed down at zero
- MO Trend Fragility indicator pinged zero recently
- Major US Indices Net CoT Speculative position at bearish extremes
- AAII, II, NAIIM Exposure, and Put/Call ratios have all hit bearish extremes within last 2-weeks
- HF net positioning recently fell to 18%
- Aggregate US Index Fund Flows recently hit just 1%
- Google searches for "recession" near all-time highs

Supportive technicals:

- Breadth so bad its good: % of stocks > 200 fell below 20%
- Price recently hit > 2stdev below 50 and 200-day moving averages
- Bonds showing bottoming action (yields down)
- Growth names starting to show relative strength
- Many markets, sectors, names at lower monthly Bollinger Band
- Down 1H + large down Q historically = tendency towards large reversion

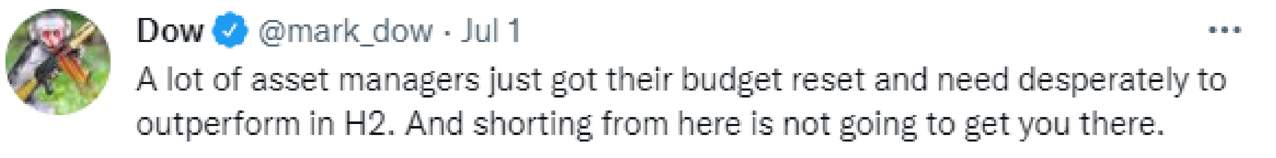
Supportive Fundamentals:

- Insiders net buying is at levels that typically precede lows
- Net buybacks (buybacks - issuance) of $682B is the largest on record
- Perception of growth / EPS slowdown is overblown and a symptom of the Great Convergence
- Nominal GDP will prevent the earnings slowdown from being too severe
- Consumer spending on services (leisure, travel) is strong and not indicative of recession
- All signs point to core inflation rolling over right as Fed at peak hawkishness

For the last two weeks I've been outlining why I think the market is putting in tradeable multi-week bottom. The action continues to give me more confidence that this is probable. This is why we're going to start adding back some more risk.

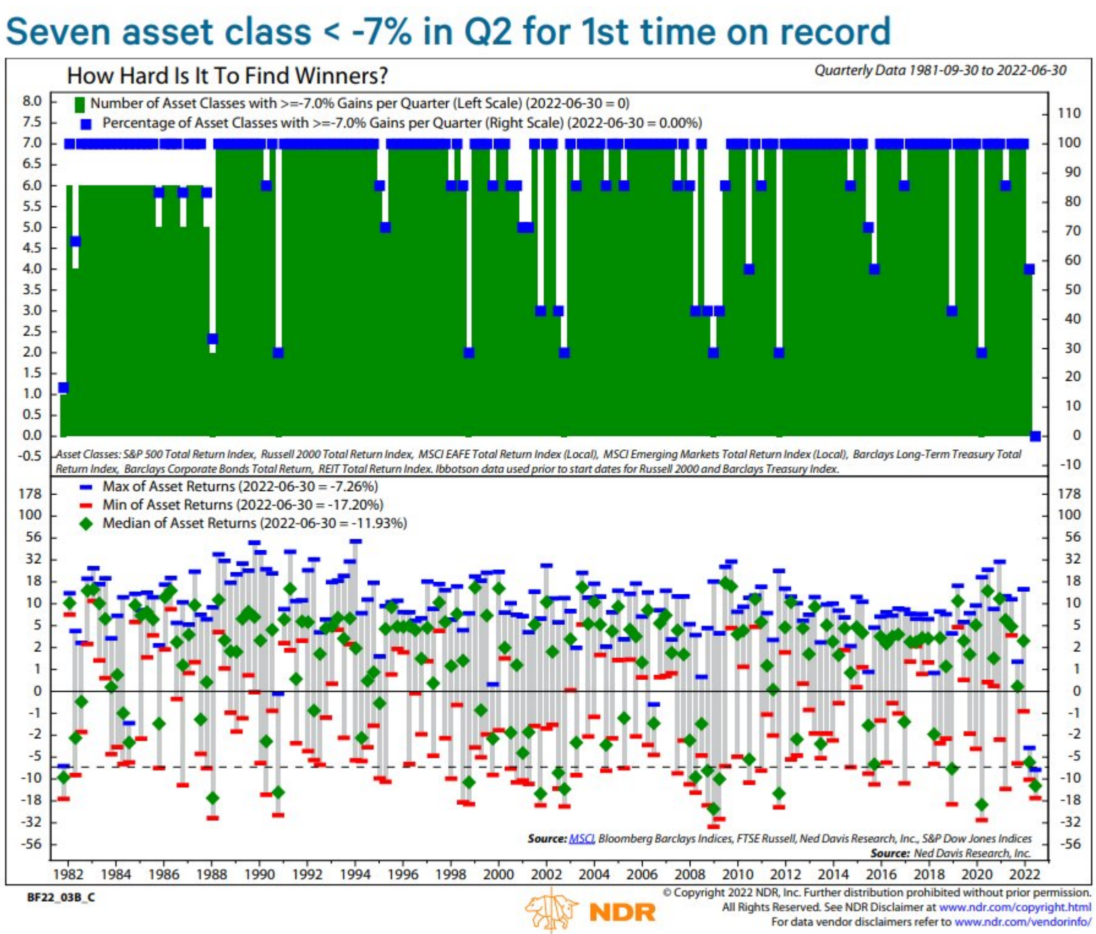
Here's a few thoughts and charts on the points above. Along with some trades we're executing and some things we need to look out for that would make us question our *big bear market rally* thesis.

To start, Mark Dow made the following point.



This feels true to me and is also supported by the data.

Net HF positioning is at *18%*, according to our [Trend Fragility dashboard]. 60/40 portfolios just had their worst first half since 1932. Seven asset classes fell more than 7% for the first time since at least 1981 (see NDR chart below). Funds have been clobbered this year. Careers are on the line. And everybody is now under positioned. **That's a lot of potential fuel for a move higher.**



Mean reversion potential is high…

Stocks and breadth are deeply oversold as I pointed out in the Dozen last week (link here). When 1H and 1Q returns have been this poor, the following quarter(s) tend to see strong returns. This is because there's a lot of potential for mean reversion in this tape.

15%+ Quarterly Drops for the S&P 500: Post WW2

Quarter	Quarterly Drop (%)	Next Quarter (%)	Next Half (%)	Next Year (%)
Sep-46	-18.83	2.27	1.40	1.00
Jun-62	-21.28	2.78	15.25	26.70
Jun-70	-18.87	15.80	26.72	37.10
Sep-74	-26.12	7.90	31.19	32.00
Dec-87	-23.23	4.78	10.69	12.40
Sep-02	-17.63	7.92	4.04	22.16
Dec-08	-22.56	-11.67	1.78	23.45
Mar-20	-20.00	19.95	30.12	53.71
Jun-22	-17.02	?	?	?
	Average	**6.22**	**15.15**	**26.07**
	Median	**6.34**	**12.97**	**25.08**

Another way to think about this is from the perspective of the Narrative Pendulum.

When recession chatter is consensus… When *everyone* has taken down risk and is holding high levels of cash… When *everyone* knows inflation is high and sticky and that the Fed is Volker level hawkish… And when *everyone* understands that there are plenty of good reasons to be bearish the market… It only takes a marginal amount of disconfirming news to dramatically swing price in the other direction. That is how mean reversion in markets works and why trends move in sine waves.

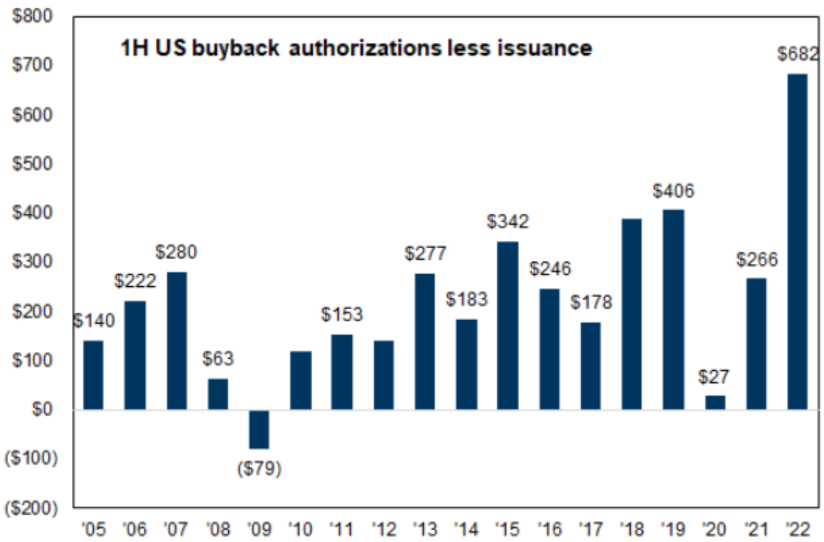
Markets are MADE at the margin… This is why they so often seem to defy reason. It's how embedded expectations and narrative/positioning cascades work. If you understand this, then you're already 90% ahead of the game.

Not to beat a dead horse but yields continue to be the key.

We need them to stay *below* their recent ceiling and move sideways or lower. This is so far playing out as bonds have gone on a decent rally. We'll need to watch and see how they react to the first strong up move in stocks. If they start selling off hard again. We'll want to pare back risk. If they only trade slightly lower, we'll want to press our longs a bit. If bonds keep a strong bid and we get confirmatory breadth thrusts, we'll want to *really* press our risk.

Fundamentals aren't *that* bad…

The *persistent bid* in this market is strong. Net buybacks hit record highs in the first half of the year. This is an important cyclical driver of market returns. Read my write-up on how to think about this dynamic here (chart below from GS).



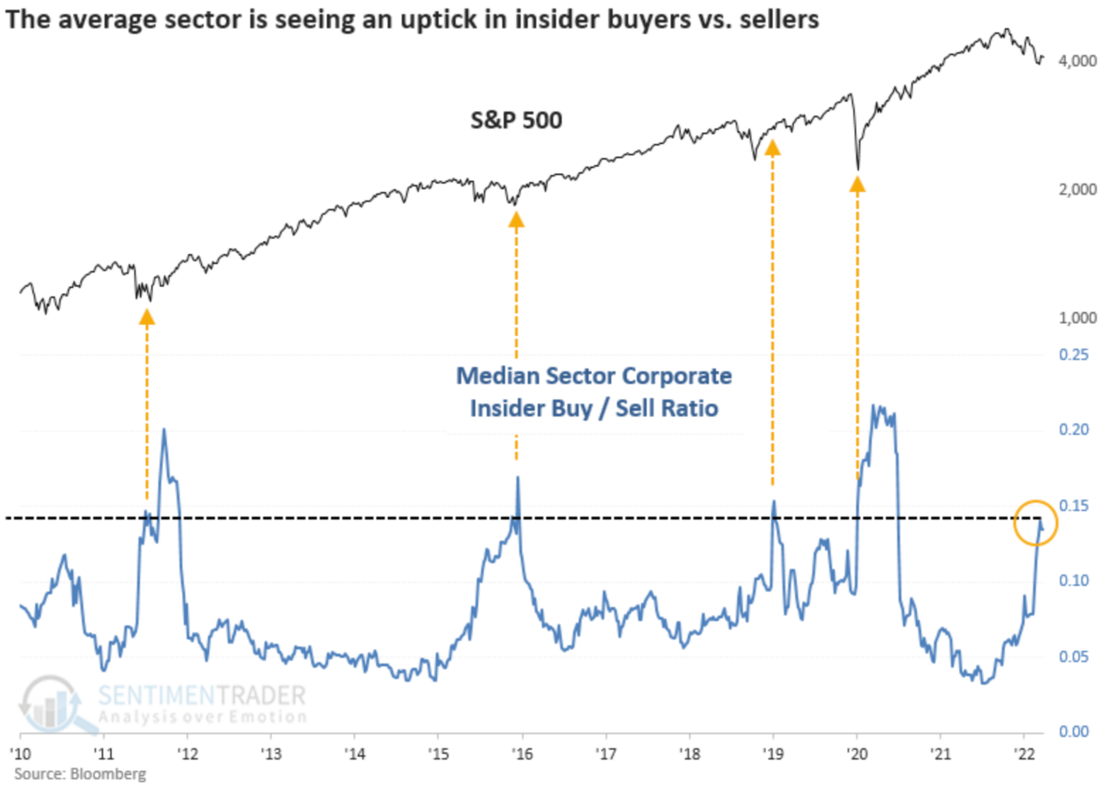
Most of what the bearish consensus point to as signs of an inevitable recession, are in fact just another symptom of the bizarro economic environment we're in.

The collapsing regional Fed surveys and manufacturing data are the direct results of the inventory glut. The inventory glut is the result of companies ordering too many goods because they over-extrapolated demand for those goods. The demand for those goods was temporarily boosted because of COVID and lockdown policies and a forced shift in consumer demand from services to goods.

And now we're experiencing a great convergence as demand for both reverts back to trend. This is why manufacturing indices look recession but travel bookings, leisure spending, etc.. are all looking, well, not recessionary.

So I'm of the belief that once this inventory glut gets ironed out, we'll find that the consumer and thus the economy, are not in completely horrible shape. Still slowing, sure… but maybe not as severely as many predict. Again, price gets set at the margin. **This is a game of degrees. And degrees have leverage when there's strong consensus like we're seeing now.**

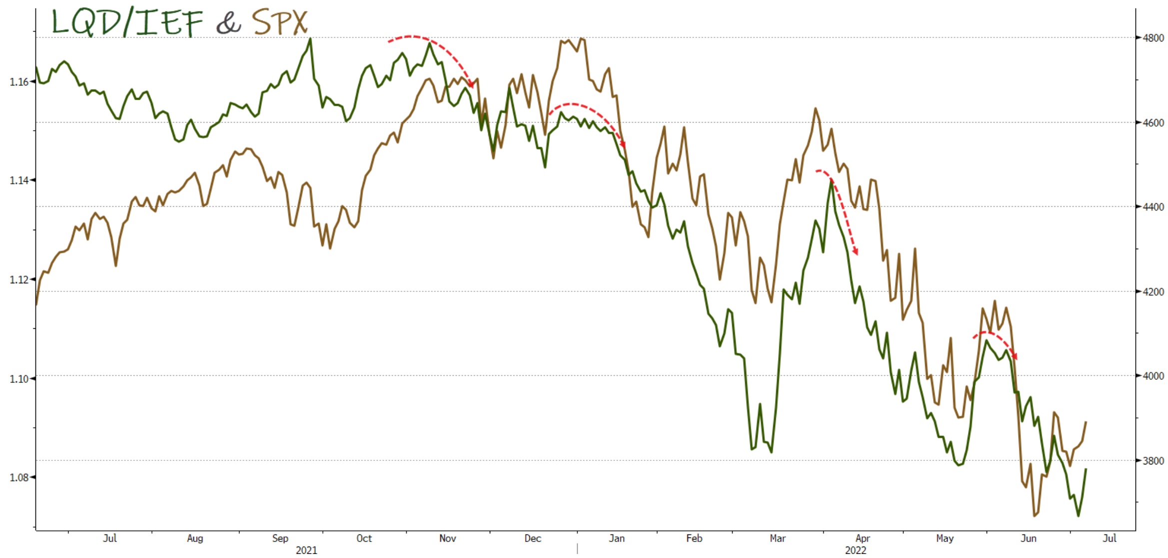
Lastly, insiders have been big net buyers in this selloff. Like all data points, this isn't a surefire signal. But historically, insiders tend to be decent timers of the market.



So what do we need to watch?

Well, we need to keep a close eye on bonds. Make sure they don't start selling off too hard as stocks rise (as I mentioned in our previous note).

We want to watch credit spreads. LQD/IEF needs to hold its current bottom and confirm any move up in stocks.



And we want to watch risk-on leads such as BTCUSD (though crypto may have lost its signaling value as it's on its way to becoming a dead asset) and Semis relative to SPX (SMH/SPY) as both should lead/confirm the trend up and will likely peak and turn over before the move is done.

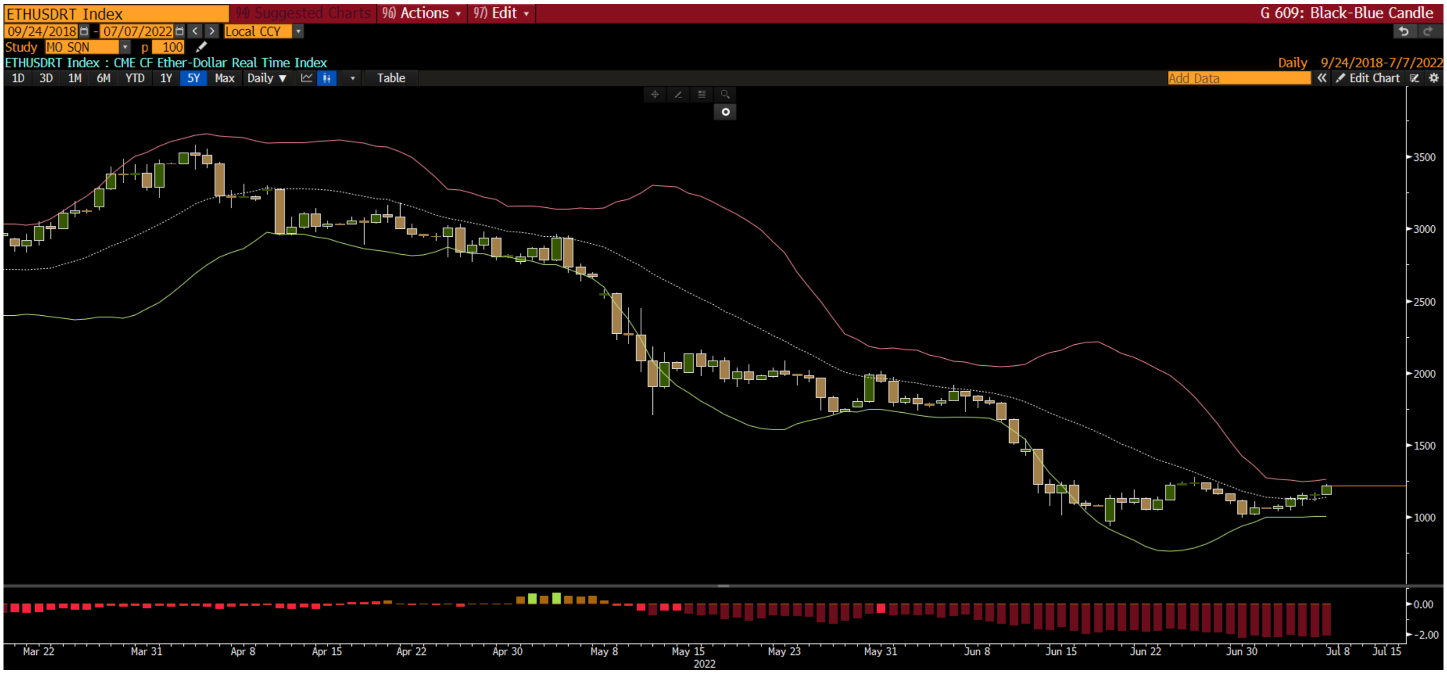
Our Jockeys…

Crude has seen a big shakeout this past month after funds chased price and crowded into energy names in May. And if we don't enter a recession then energy names should recover, and lead the market up.

We will likely get back in [Pantheon Resources (PANR)](). It's still well below fair value. The stock is consolidating at support. This allows us to nest in a tight stop and get some decent size for little risk. We'll send out an alert if and when we do.

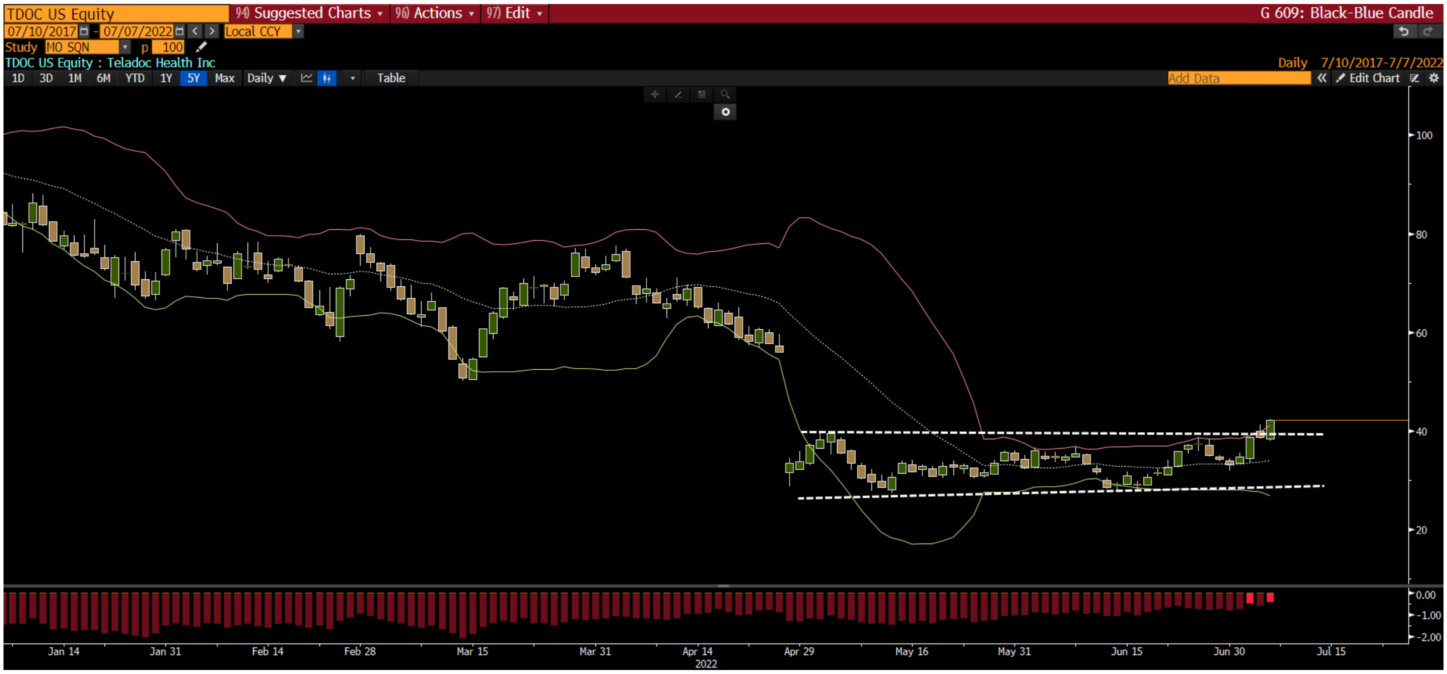
We're going to put on a starter position in the Amazon of South Korea, **Coupang, Inc. (CPNG).** The stock has been showing relative strength for the last two months and has broken out of a base. Growth names like CPNG should lead this rally as long as bonds don't sell off too hard. Trade details below.

BTCUSD and ETHUSD are coiled in a major compression squeeze. And sentiment/flows are at record bearish extremes as I pointed out on Monday ([link here](#)). We'll wait for a confirmed volatility breakout (VBO) first and then we'll put in a buy stop above that bar's high. The crypto-miner MARA is another levered play on this. Short-interest and squeeze potential are significant if we enter a period of risk-on soon.



Teladoc (TDOC) has a reversal setup on the monthly at significant support going back to its IPO price, following a large sell climax bar in April. Scott Miller has a good writeup on them here. He owns shares at much higher prices.

The stock has high short-interest (>20%+) and is breaking out from a multi-month rectangle. If yields stay pinned, this one should close the gap to $55 at least.



Nerdy, Inc. (NRDY) has a less constructive chart setup. But this is a name we're interested in building a larger position in for fundamental reasons. You can read Brandon's write-up on [them here.](#) We're going to throw on a 1% starter position, no stop. And use it as a tracker for now and wait for the chart to develop before adding.

We're also throwing 50bps into [DOTM calls](#) on Halliburton (HAL) as a way to capture an extreme upside scenario in the event that we *don't* enter a recession and the consumer proves more resilient than thought. The calls give us a nice way to capture leverage with low risk in the event of a right-tail outcome. Plus we don't have to manage the position (no stops).

These are just the start. We'll add index futures if we see confirming action over the coming trading days. We're also still eying USDJPY for a potential short. And waiting on precious metals which we believe are setting up for their next major leg. But we need this shakeout to finish first.

Trade Details are below:

Long Coupang, Inc. (CPNG)

Entry: $16.11

Exit: $12.25

At-Risk: 50bps

Long Teladoc, Inc (TDOC)

Entry: $41.98

Exit: $33.75

At-Risk: 50bps

Long Halliburton Jan 24' $60 calls (HAL)

Cost: $1.32

At-Risk: 50bps

We'll be out with more as the action unfolds.It remains a high noise v. signal environment. So we'll be quick to reverse course if proven wrong.

Keep your head on a swivel and stay frosty…

Your Macro Operator,

Alexander