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S&P500: Fairy Tale or Parabolic Rise?

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While many are celebrating in a Swiss mountain resort the global economic recovery via the media, the S&P500 is extending its rise to 2856, which is taking the form of a parabolic rise. As the Eurostoxx50 is underperforming the S&P500, as shown in its declining relative strength *(green dotted line on the upper panel),* it may give the impression that this current global bull market is not so dramatic. Though, since December, the rising Relative Strength in emerging markets is telling us that higher-risk equity markets are even more frenzied. But few seem to care about it, as the good economic background reassures the crowd.

As it is rather difficult to foresee the top of a parabolic move, it may be easier to just wait for the market to spike up and reverse to call the top afterward. But investors need to differentiate the beginning of a bull move and its end. Many of the classic signs – for example a deterioration of breadth, developed by the art of technical analysis – are not signaling an imminent top. Thus the main thinking of many investors is that the current rise will be corrected only by a pullback of 1% to 2% and then followed again by higher-highs. Only a few are concerned by a decline of 5%. Let's see on the weekly chart of the S&P 500 since March 2016 how the price and the momentum are behaving.

First, note that the Volatility Index (VIX) is displayed behind the price *(orange dotted line)*. The VIX remains just below a declining trend line joining the weekly top near 22% in November 2016 and the following much lower peak near 16 in August 2017. In last November and December, the VIX made lower highs and lower lows even under 9%. But, in the end of January, the VIX is making a higher high near 12% above the previous peak at 11%, and this despite higher weekly closes on the S&P500. This is a clear sign that volatility will rise and that a temporary top is not far away on the S&P500. Of course, the weekly momentum is firing on all cylinders, as the MACD is rising in a parabolic fashion telling us that momentum is still accelerating on a weekly basis. And this signals that the other momentum measure, the weekly Stochastics, could remain in overbought area for a while. So why any worry?

Graph: *S&P500 Weekly Candles with Ichimoku cloud showing a parabolic rise.*

VIX is represented in orange dotted line behind the S&P price candle. On the upper panel is displayed the declining Relative Strength of Eurostoxx50 versus S&P500 in green dash line, and the rising Relative Strength of emerging EEM ETF versus S&P500 in black solid line. On lower panel, MACD displays a parabolic rise reaching a level not seen in 18 months, while the weekly STO is in an overbought area since October.

Source: Stockcharts.com

The price pattern is taking a parabolic shape, which can be seen as support trendlines can be drawn at a steeper rate of ascent. The rise is so fast that for 4 weeks it has closed above the upper weekly Bollinger Band currently at 2827. This happens very rarely at the end of a bull market, and is usually seen only on a rebound following a severe bear correction. So at least we know that the current price parabolic rise is rather rare.

The S&P500 open on 22 January was 2809, thus a close below 2809 would produce a weekly reversal and call for a pause, which may retrace 38% of the rise from 2542 to 2857, namely toward 2737 or a 4.2% decline. But the real last support was in December near 2670, or much closer to a retracement of 62% or a steeper decline or 6.5%. That is the issue of a parabolic rise without intermediate corrections, as the last support area is much further away from the current price than in a normal linear bull market. In each of the following weeks, investors will need to keep in mind the weekly open and monitor it to see if a weekly close will break it! Then, when the correction starts, we may have to remember to look for a support area as the odds are still high, from a technical view point, that later in 2018 a higher-high will be seen.