THE IFA's Wealth Gram

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Two "Hot" Paths for S&P 500 from Mid-Summer to the Fall!

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In the April WealthGram, between two paths we preferred the red one, which was bullish from April to the summer of 2018. That same red path is still on display unchanged till January 2019. For 2019, the red path will be subjected to changes depending on what happens this fall, if an expected four-year cycle low re-emerges in the US Equity market. As we explained during our GSCGI conference of last 22 June, it is a big "IF" as this four-year cycle, also called in the US Presidential Cycle, seems to have vanished or may have been overcompensated by other cyclical forces in 2006, 2010, 2014, so that there has not been clearly major dips in those years. That has been amazing as this cycle was well documented for over 100 years till 2002. While technical analysts know that they have to give more weight to the patterns of the tape, it is amusing to envision a potential evolution of the price pattern, which could also fit with the re-emergence of this famous, but for the last 16 years forgotten cycle. Here we do not discuss why it should or not reappear. It is like "Religion", everyone has one or none.

Right now the S&P 500 is still above the rising trendline drawn on the log chart from the weekly second closing low near 1850 in Q1 2016 and the low 2083 in November 2016 *(US presidential election)*, which started the parabolic rise ending at 2872 in January 2018. It is even nearing the upper about flat weekly Bollinger Band *(2844)* with higher highs at **2830** a few days ago above the previous ones at 2817 of mid-July and 2791 of mid-June. It also made higher lows *(last major pullback at 2692)* along positive, but very slowly rising MACD and again overbought Stochastics, which would be displaying a bearish divergence **if** the S&P 500 would reverse below 2800 in the coming days. If the S&P is able to make other higher highs above 2830, possibly toward 2844-52 or even up to 2872, then such bearish divergence may disappear. But bearish divergence on weekly Stochastics usually works well, when the price is well established within a trading range. This is the case currently with about flat Bollinger Bands *(2847-2588)*.

Another type of divergence would be the inability of the VIX *(12.43% on 24 July)* to make a lower low below 11.90% *(corresponding to previous S&P high at 2791 in mid-June)*, while the S&P is now above 2816. This would suggest that the market expects VIX to rise seasonally during the period July to mid-October.

Compared to our April analysis, on the upper panel, the Relative Strength (RS) of small caps versus S&P 500 is making a pause after a higher high, while the RS of emerging market ETF EEM versus S&P 500 has extended its decline almost back to the support area of quarter one 2016. On the contrary, the RS of Nasdaq100 versus S&P 500 in red dotted line *(mostly representing the technology sector)* has extended to higher high after a pause ending in early April, which indeed allowed the rebound of the S&P as we expected on April 1. As the US market breadth, which was widening till the end of June, is possibly slowing its expansion right now, the S&P 500 is trying to retest its January high mainly thanks to the leadership of fewer stocks "FAANG" and thanks to the rising, though pausing in July, RS of the technology sector. Also, the financial sector may also help the rise of the S&P in the near future as US 10-year yield is rising from the bottom to the top of its range near 3%. But a sustained break out above 3% is not our preferred case as we called for a retest of 2.75% during the fall after a failure of the S&P 500 to reach the former high of 2872, because it is stalling just below the about flat weekly Bollinger band *(2847)* or because it creates a sudden weekly reversal below 2800. The first area of support should be the upper cloud *(2700)*. A break below the lower cloud *(2600)* may open more trouble along the two red and green paths *(see below graph commentary)*. Red path is unchanged since April for 2018 and still assume about a retest of 2872, before dipping into a correction of 10 to 14%. Green path is more bearish as the S&P 500 would fail to reach 2872 and decline 15% to 20% well below 2500. Then seasonality *(or the economy)* should help launch a rebound in the last quarter. What will happen in 2019 depends much on the price pattern till the fall. Indeed 2018's question remains "when to hedge or what to hedge".

Graph:

Chart of S&P 500 in weekly candles with Ichimoku cloud and VIX represented in orange dotted line behind the S&P 500 candles. On the upper panel is displayed the rising Relative Strength (RS) of small caps Russell 2000 versus S&P 500 in green dash line, the RS of emerging markets versus S&P 500 in orange solid line and the RS of Nasdaq100 versus S&P 500 in red dotted line. On lower panel, MACD is positive, though rising slowly while the weekly STO is rising again in an overbought area with risk of displaying a bearish divergence if the S&P 500 reverses below 2800. The red path has not been changed for the rest of 2018. For 2019, the red path will be subject to changes depending on what happens this fall, if an expected four-year cycle low may re-emerge. The green path is a slightly more bearish version than the red path in case the top at 2872 is not reached in coming weeks.

Source: Stockcharts.com / Red and Green Paths are provided by BEST.