

S&P500—TIME TO HEDGE OR NOT TO HEDGE?

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In August 2022, the S&P500 failed to hold above its 40-wk moving average and reversed down for 2 consecutive weeks. Given the sharp fall in the 2nd week, the sudden rise of the VIX (*orange dotted*) from 20-25% may soon extend toward 30%.

While the rebounding 10-yr US yield from 2.85-3.03 remains well below the near 3.5% peak of June, the Relative Strength (RS) of Nasdaq vs S&P500 (*red dotted*) has stopped its rebound and weakens again as large-cap Technology stocks are pulling back after strong rebounds in July-August. However, small caps have not performed well during the summer as shown by a relatively flat RS line (*green dotted*), which may decline as the S&P500 weakens. The RS line of emerging markets (orange solid) vs the S&P500 shows a small rebound in a downtrend since June, which represents more of a sudden sharp decline of the S&P500 than strength in emerging markets, that have been underperforming developed markets for several months.

As the seasonal weak period of the year approaches, the recent sharp reversal is calling for defensive tactics, as we recall seeing in May—a 3600 target during the fall of 2022. From the current level near 4050, a decline toward 3930 is likely as the VIX may rise further to 30%. Then a minor rebound may take place along the Green Path toward 4150 before renewed weakness till mid-October toward the 3750 area. But given the weak seasonality, the Red Path would call for immediate decline below the 3636 June low, which may possibly extend toward a classic low spike in the 3500-3450 area, before a seasonal rebound of the end of the year.

As seen on the chart, depending on which path the S&P500 takes, the longer-term outlook for 2023 may become very divergent between a bull market for the Green Path or a lasting bear market for the Red Path.

It is now time for long-term investments to “Hedge or Not to Hedge”.

S&P500 chart is shown on a log scale from August 2020 in weekly candles with Ichimoku cloud.
On the upper panel (*green dotted line*), the Relative Strength (RS) of Small Caps vs S&P500, which is almost flat in August 2022, the RS of Nasdaq100 vs S&P500 (*red dotted line*), which is still in a downtrend, and the RS of Emerging Equities vs S&P500 (*orange solid line*) which is rebounding.
On lower panel, negative MACD has rebounded, but weekly STO has crossed down at a higher overbought level than in April 2022. The S&P500 may extend its downtrend toward 395. Then it may follow either the Green Path with a rebound toward 4150 or the Red Path below 3900. Note: both cases envision weakness in September-October along the US mid-term elections' four-year cycle low and the decennial cycle of a year ending in 2.

Source of data:
Stockcharts.com.
Supports line
& parameters
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