

ACTIONABLE IDEAS FOR THE ACTIVE INVESTOR

ALPHA INSIGHTS

WEEKLY PLAYBOOK

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“Inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output.”

~ Milton Friedman

STOCK MARKET INFLATION

With respect to Friedman's quote, we are currently engaged in a test of this proposition. Beginning on June 1st, the Fed will begin the process of reducing the size of its balance sheet or Quantitative Tightening (QT). The plan presented on May 4th calls for a reduction of \$402.5 Billion or 4.5% by year-end, then another \$1,140T or 13.3% in 2023. Based upon the prior glidepath for equities relative to QE, it would appear that the market has already priced in the initial foray of QT. If allowed to follow its logical course, the Fed's eventual balance sheet reduction back to pre-COVID levels would likely be accompanied by a lower stock market price of SPX 2250.



Source: mcoscillator.com

BUYING OPPORTUNITY OF A LIFETIME?

Looking back over the history of the S&P 500, there have been eight so-called, “buying opportunities of a lifetime.” These price lows coincided with valuation lows that were rarely seen again. From the 1932 low to the 1982 low, these valuation levels equated to mid-to-high single digit P/Es as measured by the Shiller CAPE ratio. From 1987 through 2009, that valuation floor expanded to a low-teens P/E equivalent. In 2020, the low was defined by a CAPE ratio of nearly 20x. Today, the current CAPE ratio is 31.3x, in an environment of high inflation, slowing growth, and tight financial conditions!



Source: StockCharts.com

S&P 500 TREND ANALYSIS: BEARISH

The S&P 500 has declined by over 13% YTD. Last Friday's close marked the lowest weekly close since the start of the bear market. The breach of key trend and moving average support levels, coupled with the bearish inflection below chart support at SPX 4300, if sustained, projects a measured move to approximately SPX 3500. Only a sustained bullish inflection above key resistance at SPX 4637 would invalidate the immediate bear case for stocks.



Source: StockCharts.com

PREFERRED ELLIOTT WAVE COUNT

Make or Break = SPX 4637

Cycle Wave V of (III) Terminated at SPX 4818

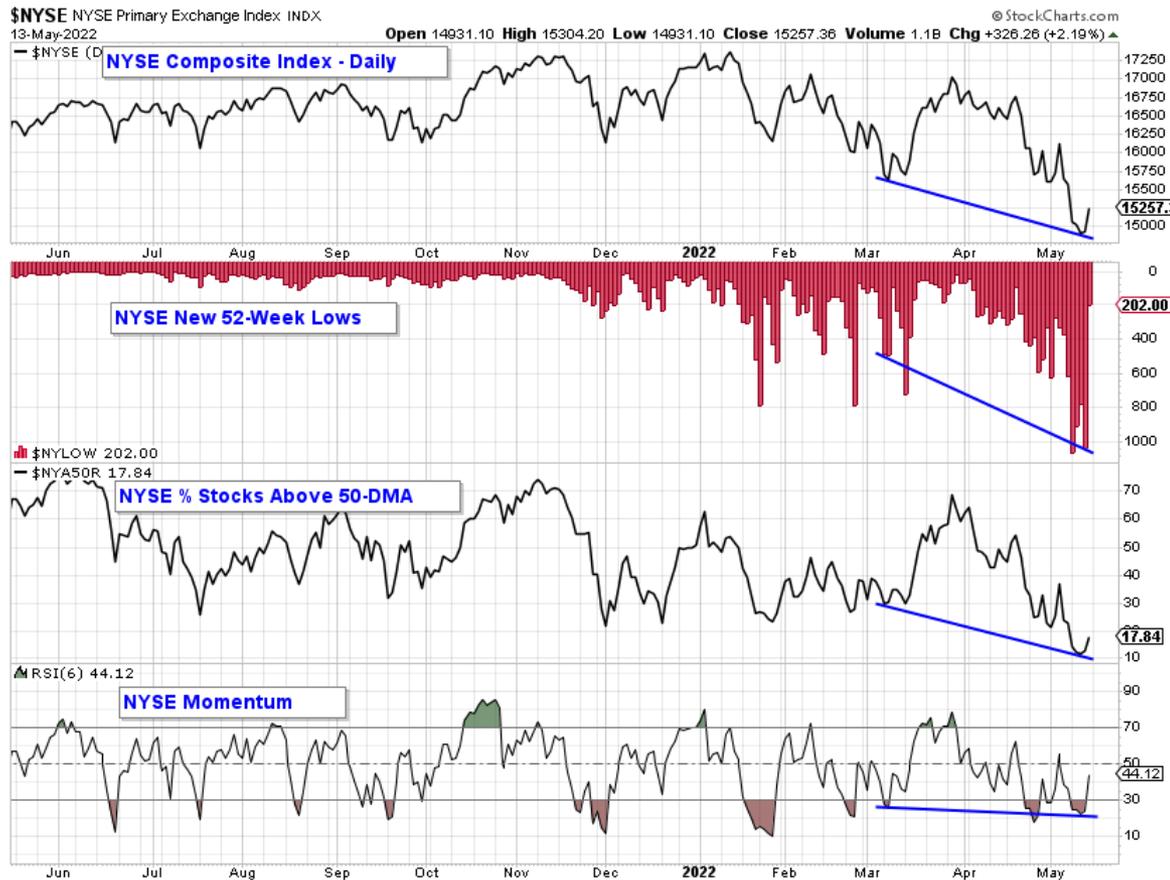
Intermediate Wave 3 of (a) Down in Progress



Source: StockCharts.com

NYSE COMPOSITE INDEX INTERNALS

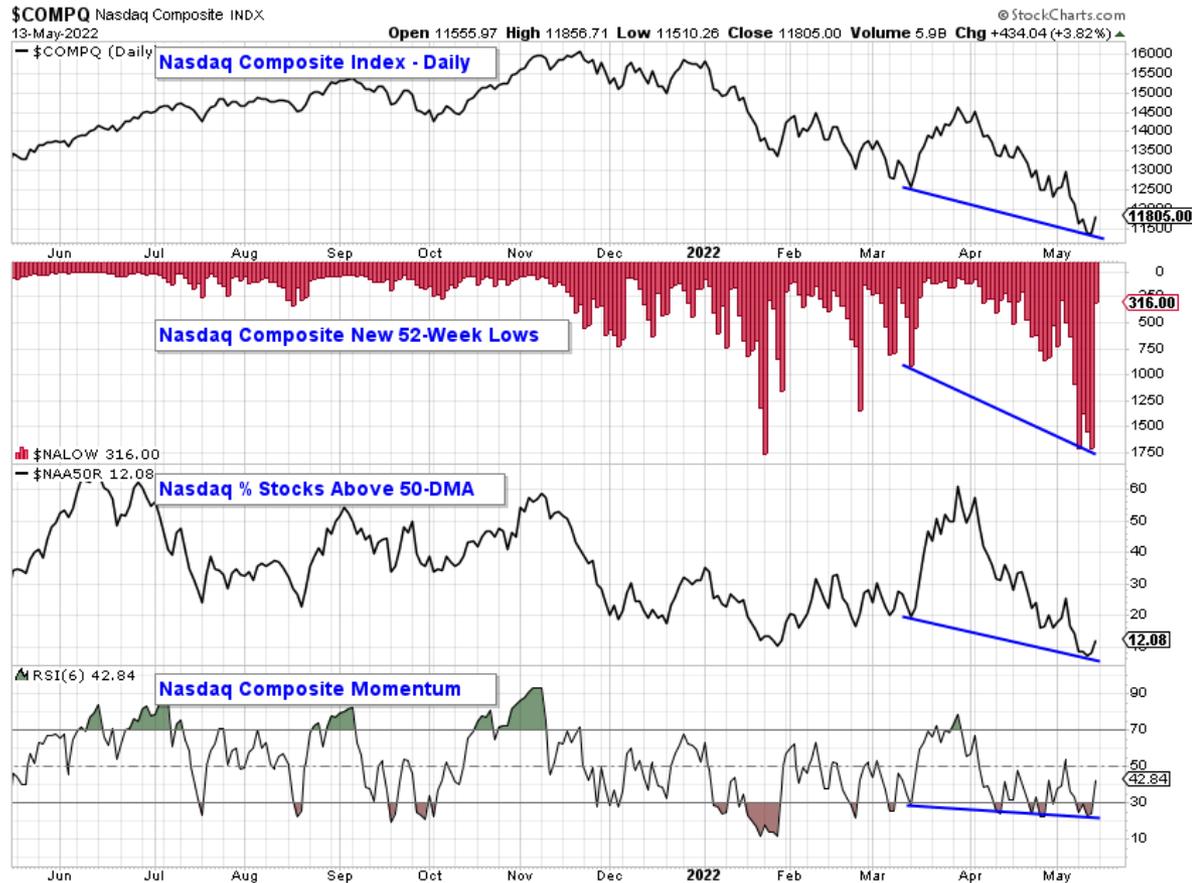
The NYSE Composite index is comprised of over 2,200 listed stocks trading on the big board including 360 ADRs. As the price of the index made a lower low last week vs. its March 8th low, under the hood, multiple measures of breadth and momentum confirmed the move by posting their own lower lows. Included among these were the number of new 52-week lows, the percentage of stocks trading above the 50-DMA, and the 6-day RSI momentum oscillator.



Source: StockCharts.com

NASDAQ COMPOSITE INDEX INTERNALS

The NASDAQ Composite index is comprised of over 3,700 domestic and international stocks listed on the NASDAQ stock market. As the price of the index made a lower low last week vs. its March 14th low, under the hood, multiple measures of breadth and momentum confirmed the move by posting their own lower lows. Included among these were the number of new 52-week lows, the percentage of stocks trading above the 50-DMA, and the 6-day RSI momentum oscillator.



Source: StockCharts.com

MARKET BREADTH IS NOT DIVERGING

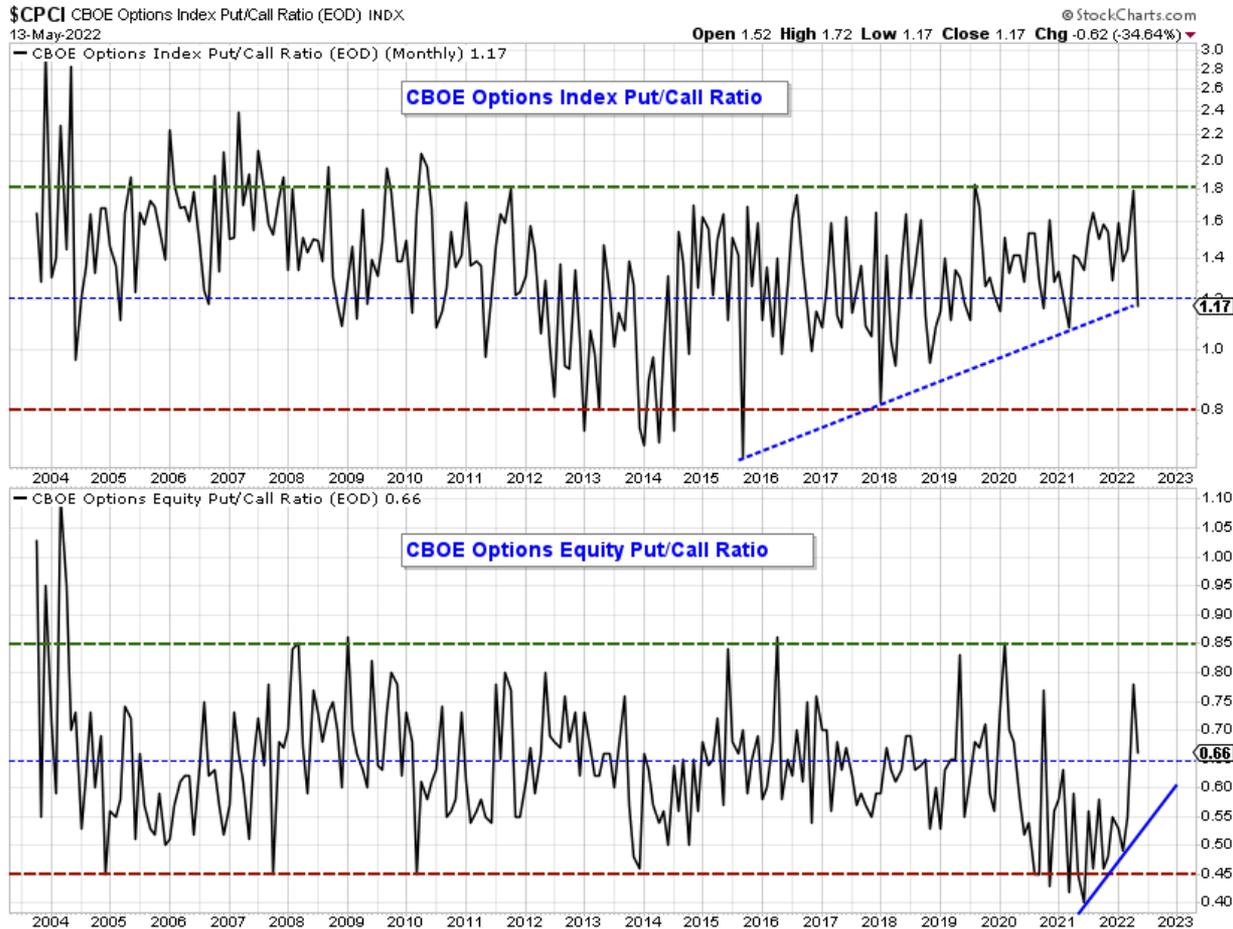
Both the NYSE and Nasdaq Composite Cumulative Advance-Decline Lines hit new lows concomitant with the indexes.



Source: StockCharts.com

INVESTOR SENTIMENT: MODERATING

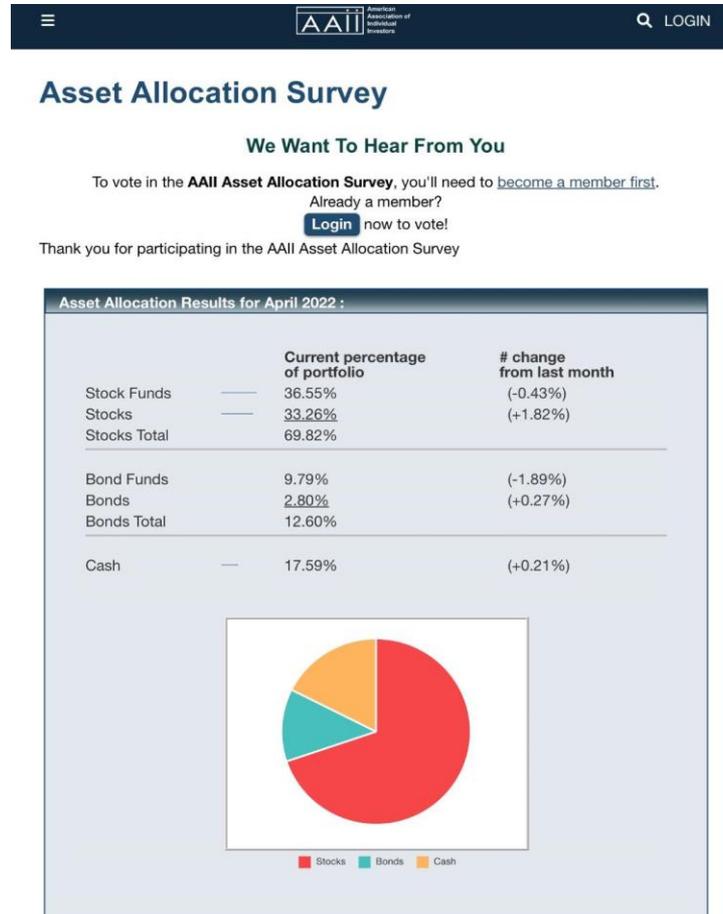
Options positioning has moderated dramatically, as traders went from being record put buyers to neutral in just a week. Below we see how the change breaks down between the index and equity Put/Call ratios. Notably, the index Put/Call ratio is now challenging its six year uptrend, suggesting that fear is moderating.



Source: StockCharts.com

ACTIONS SPEAK LOUDER THAN WORDS

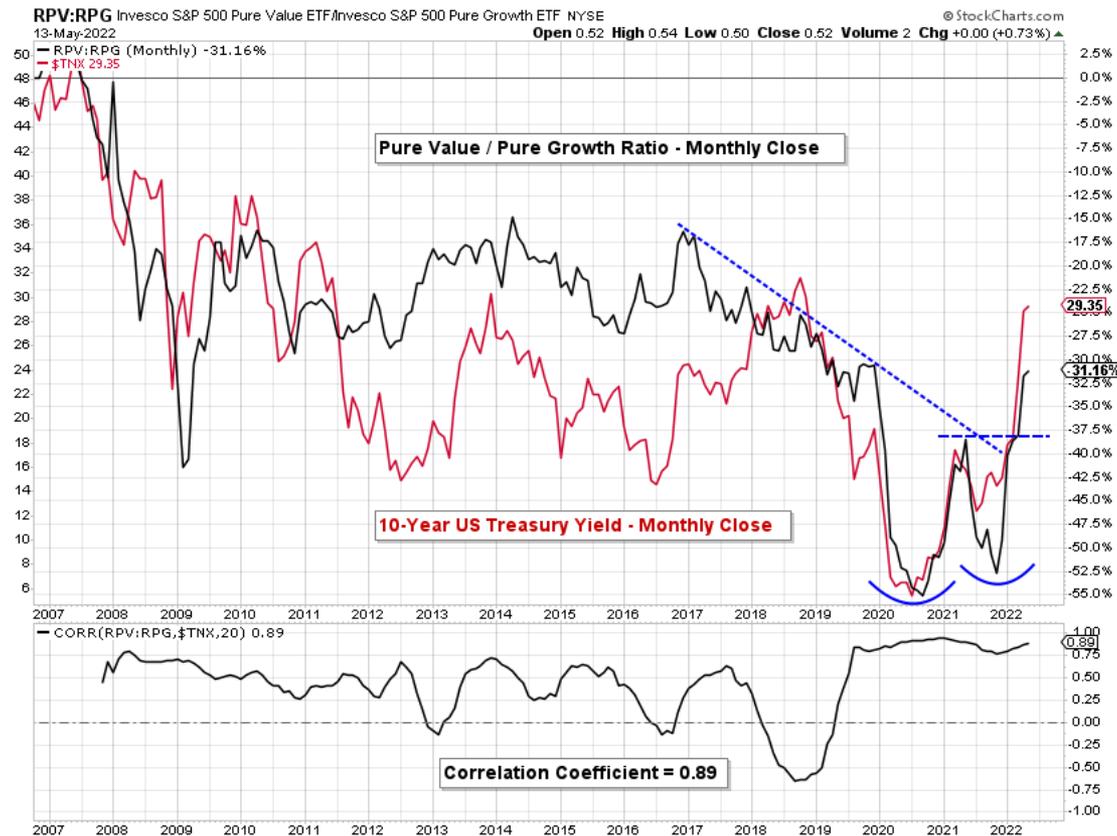
The AII sentiment survey has been notoriously bearish. Yet, despite their bearish opinions, individual investors have rarely been more fully invested than they are today at 69.8% equities. With the exception of a few quarters during the dot-com bubble, the AII asset allocation survey is never above a 70% equity allocation and has averaged 62% equities going back to 1987.



Source: aaii.com

VALUE STILL LEADING GROWTH

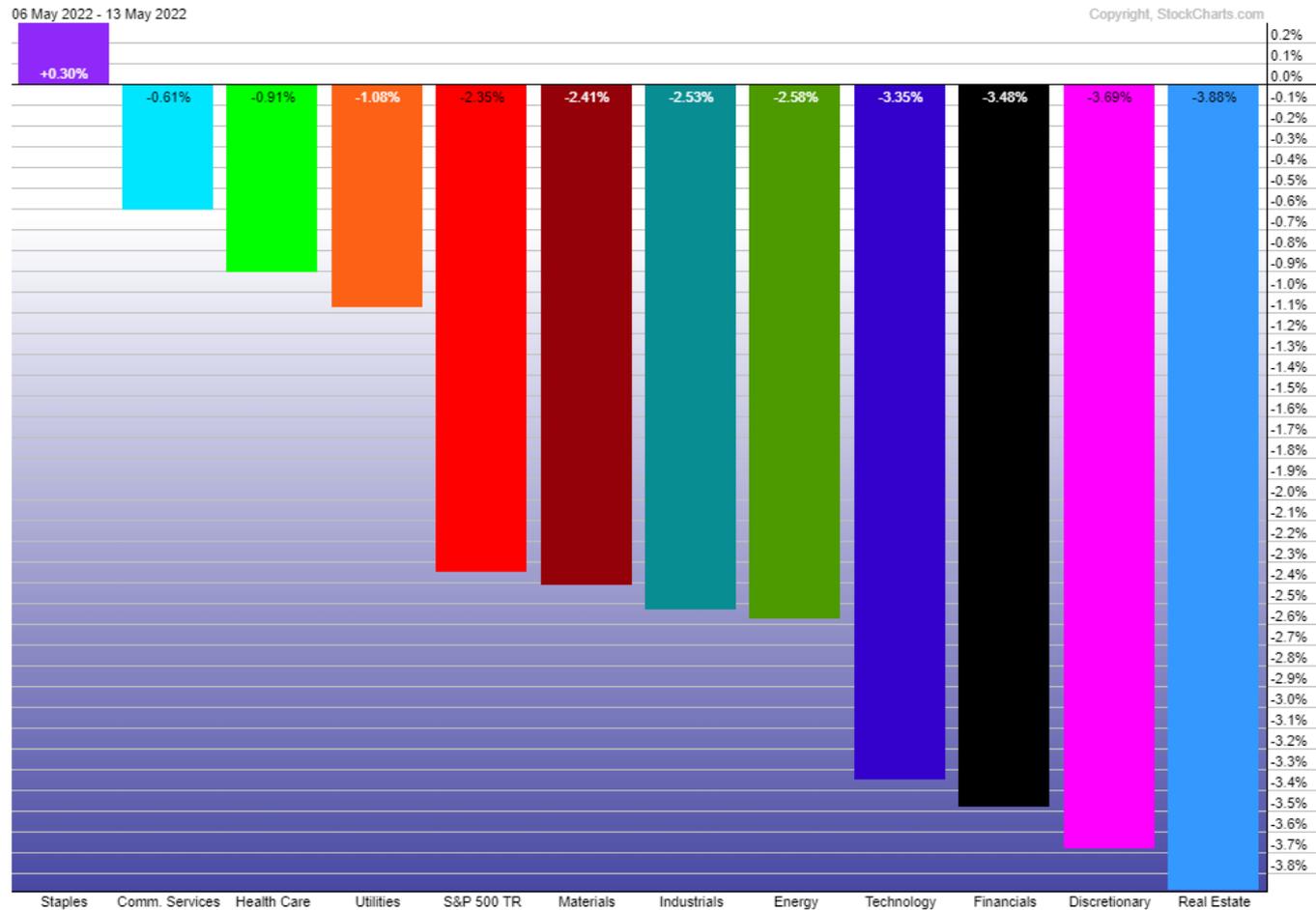
The Pure Value-to-Pure Growth ratio has maintained a tight correlation to 10-Year Treasury yields since 2008. Most recently, as rates began turning up in late 2021, the ratio began to reassert itself, breaking out above key trend and chart resistance levels. Based upon the strong historical relationship between these two series, we suspect that if rates continue to move higher, or even just remain elevated, then the ratio should continue to favor value stocks over growth stocks.



Source: StockCharts.com

SECTOR LEADERSHIP: DEFENSIVES

Weekly performance comparison of the 11 S&P 500 cap-weight GICS sectors.



Source: StockCharts.com

TOP ACTIONABLE TRADE IDEAS

(One to Three Month Time Horizon)

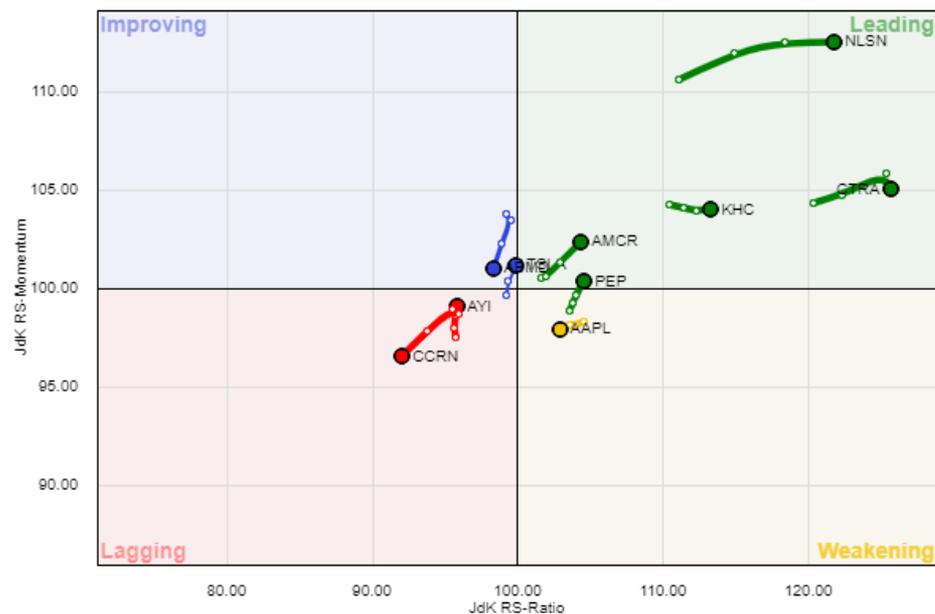
Top Bullish Trade Set-Ups

1. Nielsen NV (NLSN)
2. Coterra Energy (CTRA)
3. Kraft Heinz Co (KHC)
4. Amcor PLC (AMCR)
5. Pepsico (PEP)

Top Bearish Trade Set-Ups

1. Cross Country Healthcare (CCRN)
2. Acuity Brands (AYI)
3. Apple (AAPL)
4. ABIOMED (ABMD)
5. Tesla (TSLA)

Weekly Relative Rotation Graph



Source: StockCharts.com

NIELSEN NV

Reports 3Q22 on August 4th @ 5:00 PM ET



Source: StockCharts.com

COTERRA ENERGY

Reports 2Q22 on August 1st @ 4:05 PM ET



Source: StockCharts.com

KRAFT HEINZ CO

Reports 2Q22 on July 27th @ 7:00 AM ET



Source: StockCharts.com

AMCOR PLC

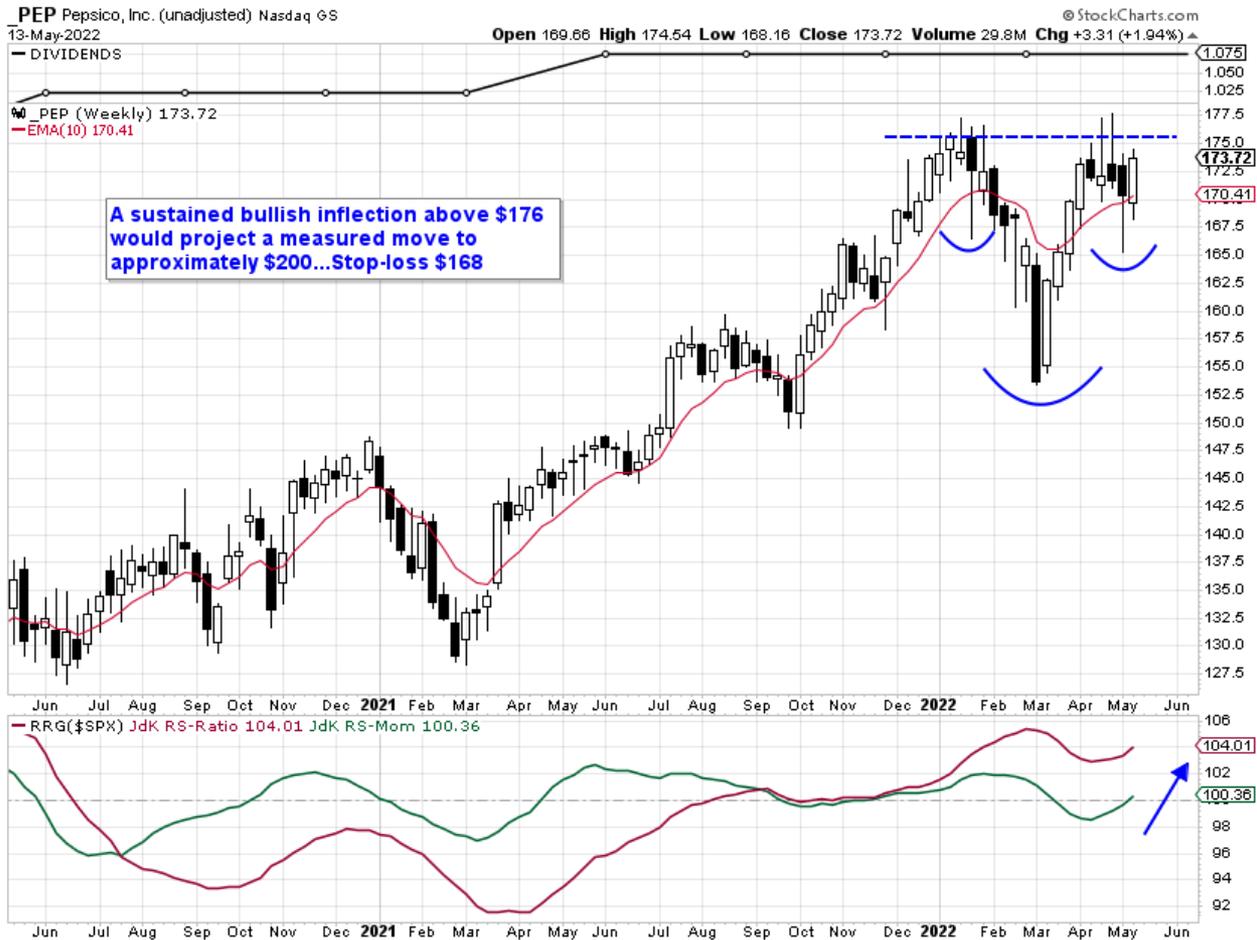
Reports 4Q22 on August 2nd @ 4:10 PM ET



Source: StockCharts.com

PEPSICO

Reports 2Q22 on July 26th @ 6:00 AM ET



Source: StockCharts.com

CROSS COUNTRY HEALTHCARE

Reports 2Q22 on August 3rd @ 4:15 PM ET



Source: StockCharts.com

ACUITY BRANDS

Reports 3Q22 on July 5th @ 6:00 AM ET



Source: StockCharts.com

APPLE

Reports 3Q22 on July 28th @ 4:30 PM ET



Source: StockCharts.com

ABIOMED

Reports 1Q22 on July 28th @ 7:00 AM ET



Source: StockCharts.com

TESLA

Reports 2Q22 on July 20th @ 4:10 PM ET



TRADING & RISK MANAGEMENT

- Our Bullish and Bearish trade set-ups are defined by a confirmed (or expected) breakout or reversal signal with a positive risk skew of $> 3:1$. Not all signals are favorably resolved, but the system has proven positive expectancy, with a profit factor of 2.80:1 since inception (8/1/18).
- The time horizon of 1-3 months is a guideline. We expect to see the trading signal confirmed by significant price action that supports the signal within that time frame, or otherwise canceled via our stop-loss provision. We expect to let our winners run as long as possible.
- Initial stop-loss provisions are volatility based calculations centered upon the average true range (ATR) of the security. Once the 10-week EMA catches up to the entry price, it then acts as the new trailing stop-loss provision (**basis weekly close**).
- Position sizing is an important component of the risk management process. As such, position size should be defined by the maximum adverse excursion (Trade MAR).
- A practical way to implement this concept would be to define your Trade MAR (maximum loss of capital per trade) in advance. Then using the difference between the entry price and the initial stop-loss price, calculate the number of shares that would optimize that constraint for each trade.
- Occasionally, following unusual price action, we will raise our stop-loss to protect gains, or we may increase our price target if a new pattern develops, which allows us to expand upon our original forecast. In either case, subscribers will be notified via an *Interim Bulletin*.

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