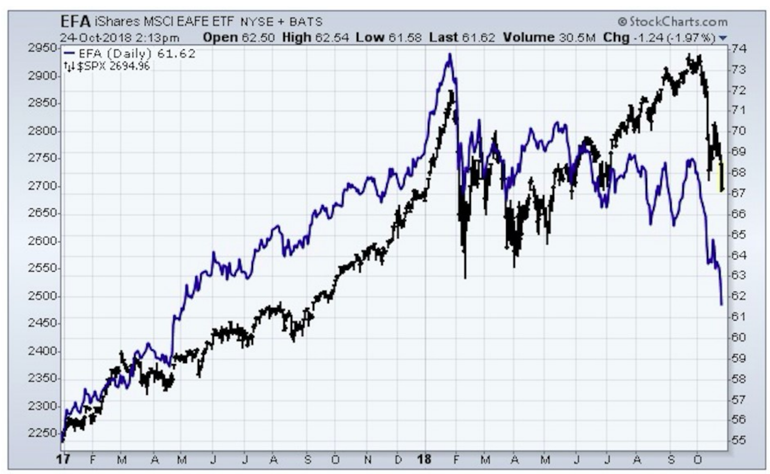
A snapshot of last week's market performance and what to watch in the week ahead from Chadd Mason, Cabana CEO and co-founder.

Last week selling accelerated across all equity markets. This occurred despite relatively strong earnings reports by the majority of companies. Additionally, 3rd quarter GDP numbers beat expectations, coming in at +3.5%. Consumer spending made up the bulk of the growth, which is generally a good thing seeing as the consumer makes up some 70% of the domestic economy. The consensus says that as long as the consumer is spending we are not headed for recession. All in all, it appears that markets have taken the position that things simply can't get any better than they have been over the past twelve months, and we are seeing deterioration from the lofty positions we have enjoyed. Investors are thus assessing the relative value of assets in a more moderate growth environment moving forward. The stock market is a leading indicator of the economy and as of market close on Friday, more than 75% of all stocks on the NYSE were trading below their 200-day moving average. This fact alone is not a good sign. Chart 1 below shows the divergence over the past three months between the S&P 500 and emerging markets. Chart 2 below shows the divergence over the past three months between the S&P 500 and other developed markets. We have seen a pronounced shift away from growth and high beta assets to defensive equities such as consumer staples, healthcare and utilities. Yields have also pulled back precipitously and bonds, treasuries and other income proxies have outperformed riskier assets over the past few weeks. Clearly, investors are becoming more and more cautious. International equities continue to lag and are now in bear market territory. I have mentioned this in several commentaries over the past few months and my fear that we would eventually be pulled down with them may be coming to fruition. We need other world economies to participate in the growth story for the U.S. stock market regain its footing. Likewise, I am hopeful that our Federal Reserve is aware that the relentless pursuit of raising rates is causing real problems internationally. We are still within the boundaries of a normal correction as part of a much larger secular bull market. We are also in deeply oversold conditions whereby a large and quick rebound in stock prices is likely over the next few weeks (if not sooner). The response to that rebound may very well tell us whether we have seen the top of the market for the current cycle. If investors start selling into strength as opposed to buying weakness, we will know that things have changed. For now we remain cautiously bullish and will avoid making predictions, but will take it as it comes.

(click to view a live version of this chart)

Chart 1



(click to view a live version of this chart)

Chart 2

G. Chadd Mason
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