CABANA WEEKLY MARKET COMMENTARY

NOVEMBER 19, 2018

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

U.S. equity markets ended last week down despite a rally mid-week. As of Friday, the S&P 500 was down 1.2%, the Dow was down 2.3% and the Nasdaq was down 1.9% for the week. The S&P and Nasdaq remain below their 200-day moving averages, while the Dow managed to stay just above it. Defensive equity sectors such as consumer staples, healthcare and utilities continue to outperform cyclical sectors such as consumer discretionary and industrials. Technology remains the weakest of the bunch after being a leader over the past eighteen months. Small caps are underperforming large caps. Interest rates have pulled back in response to equity weakness and are now touching 3.10 on the 10-Year Treasury Note. This gives support to bonds and other interest rate sensitive assets, such as REITs and dividend payers. International equity markets remain weak, as they have all year. In sum, the only factors we have in our favor, are seasonality (November and December are traditionally strong months for the stock market) and a potential "reverse head and shoulders pattern" in the S&P 500. A "reverse head and shoulders pattern" is a bullish technical price pattern, which could be developing. We would need to see the S&P close above $282 for it to be confirmed. We are a long way from there as we closed last week at $274. I have done some research on intermarket relationships prior to entering bear markets and came upon some similarities between what has occurred in 2018 and what occurred in 1990. Early in 1990, bond prices turned down sharply in response to rapidly rising rates. This created a negative divergence between stocks and bonds and was a precursor to falling equity markets later in the year when the Dow fell 17%. Additionally, following a worldwide selloff in equities early in the year, U.S. equities rebounded to new highs while the rest of the world failed to do so. The U.S. became the only market with its head above water. That qualified as a "global equity divergence" and was not a good sign. This year we have witnessed these exact scenarios. I have commented on these conditions many times over the past few months and things have not improved. The one difference in the set up today, is that in 1990 (and also leading up to the 1987 crash) the cause of the rising interest rates was rising commodity prices and a weak U.S. dollar. This year, we have seen the opposite. Commodity prices are in check and the U.S. dollar is strong. The cause of the rising rates currently is normalization of monetary policy in response to improving economic conditions in the U.S. Whether this underlying catalyst makes things different remains to be seen.

Last week's market commentary is available for download here.

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