Intermarket Analysis & Review: 02-20-20

We are adding a NEW REPORT we will be rotating on Thursday's which looks at the intermarket analysis between various asset classes, commodities, rates, and currency. The goal is to identify opportunities in areas which may be breaking historical correlations, or are confirming changes in trends.

What Is Intermarket Analysis?

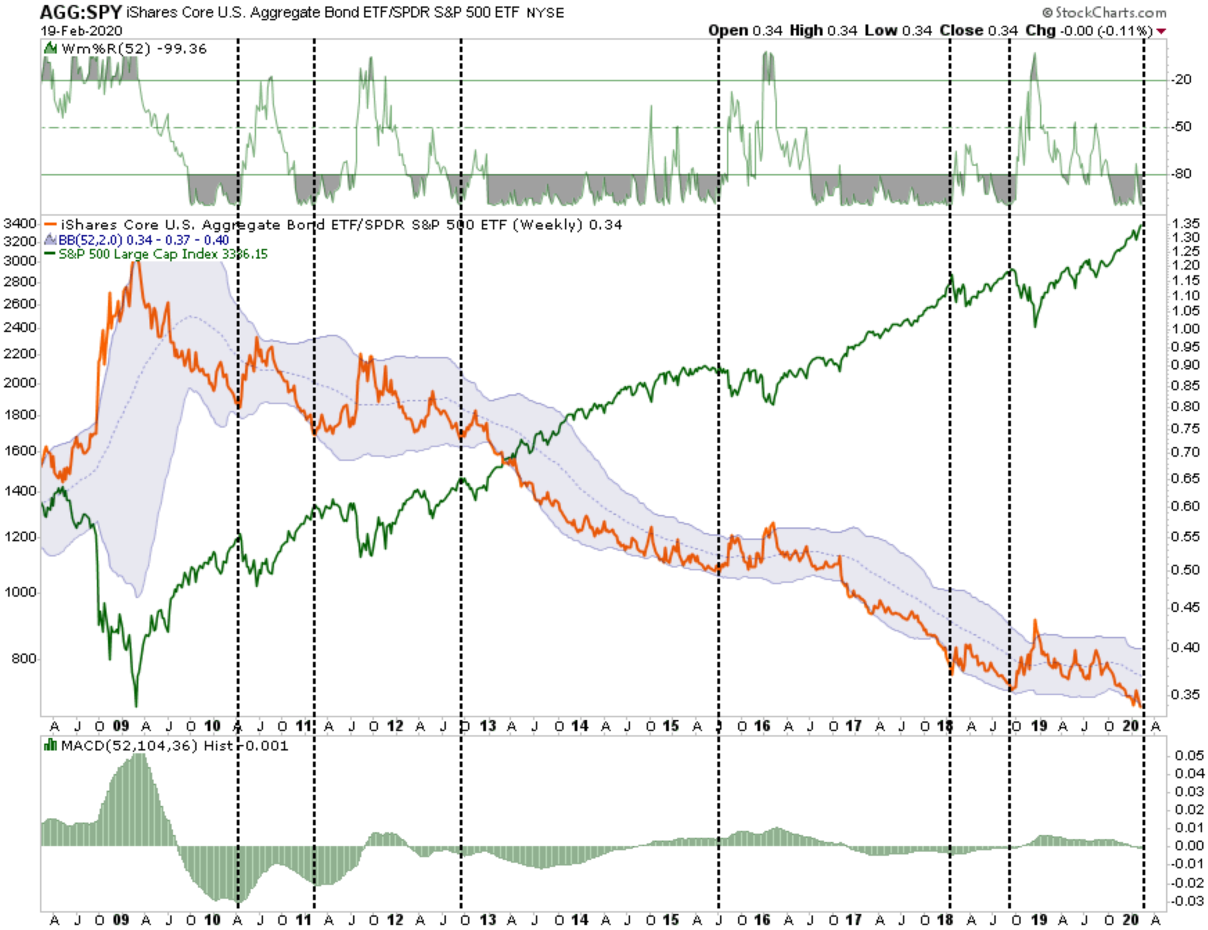
Intermarket analysis is a method of analyzing markets by examining the correlations between different asset classes. In other words, what happens in one market could, and probably does, affect other markets, so a study of the relationship(s) can prove to be beneficial to the trader.

- Intermarket analysis is a method of analyzing markets by examining the correlations between different asset classes.
- A simple correlation study is the easiest type of intermarket analysis to perform, where results range from -1.0 (perfect negative correlation) to +1.0 (perfect positive correlation).
- The most widely accepted correlation is the inverse correlation between stock prices and interest rates, which postulates that as interest rates go up, stock prices go lower, and conversely, as interest rates go down, stock prices go up.

Each week we will highlight a few of these intermarket relationships which have caught our attention.

Please feel free toEMAIL MEany other intermarket relationships which you think are important and I will try and include them.

Rates Vs S&P 500

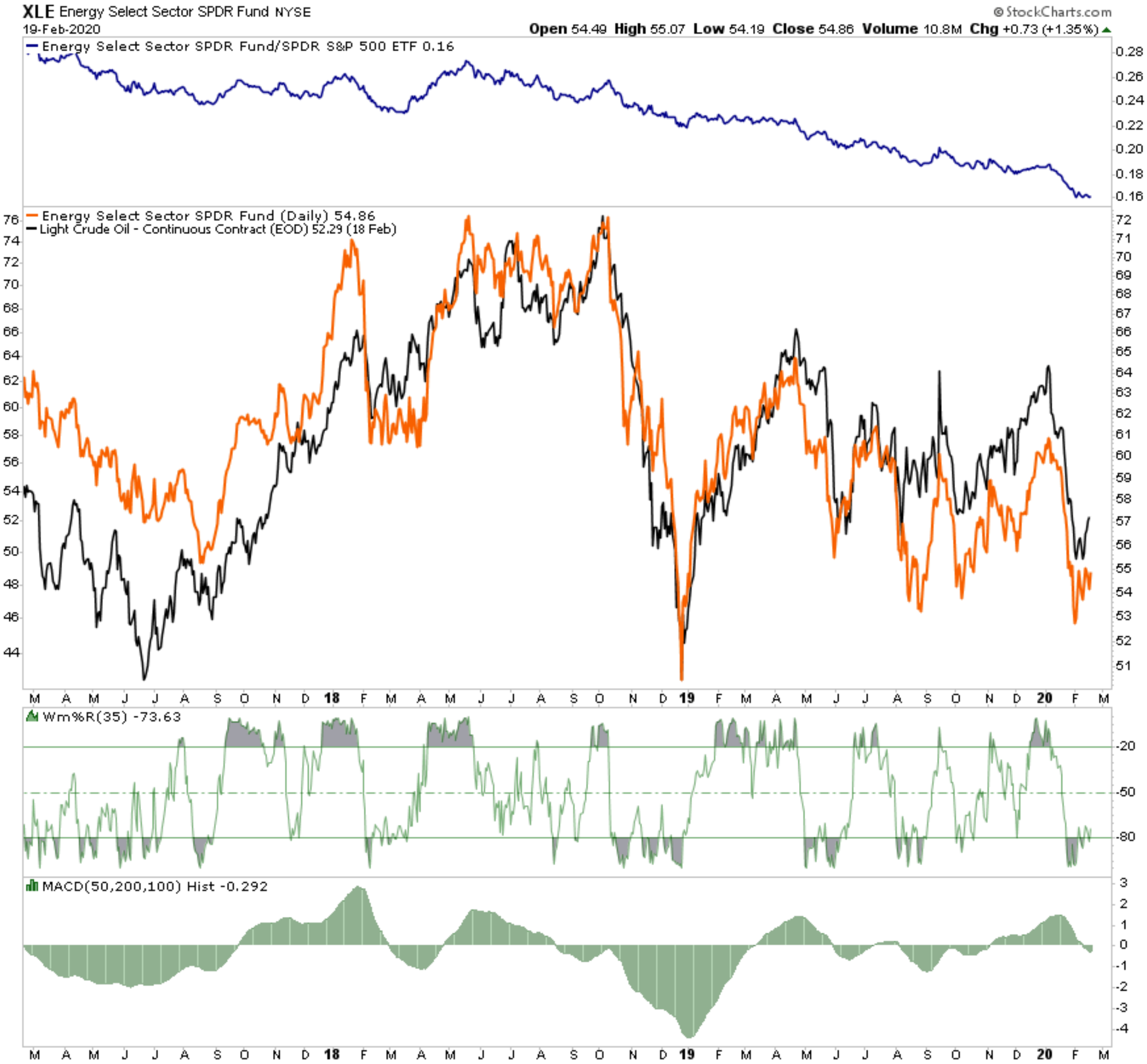


Stocks and bonds play an interesting *"risk on/risk off"* relationship over time. As shown above while stocks are extremely outperforming bonds currently, the relationship is now suppressed to levels where a reversion would be expected. This suggests that we will likely see a a correction in equity prices, and a rise in bond prices (yields lower), in the near future.

Small Cap Vs Large Cap

Small cap stocks have not participated in the rally over the last year as earnings growth slows and money has rotated to chasing the largest large-cap names for both safety and liquidity in an extremely stretched market. With small cap stocks more affected by global supply disruptions, expect a correction in small cap stocks. Very likely, given the historical relationship, this correction will occur in concert with a correction in large cap stocks as well.

Energy Vs Stocks Vs Oil



Energy has been underperforming the major markets for quite some time. Of the few sectors in the market today that may represent some level of value, energy may be one of them. Not surprisingly, there is a very high correlation between oil prices and energy stocks. Currently, both the commodity and energy are extremely oversold.

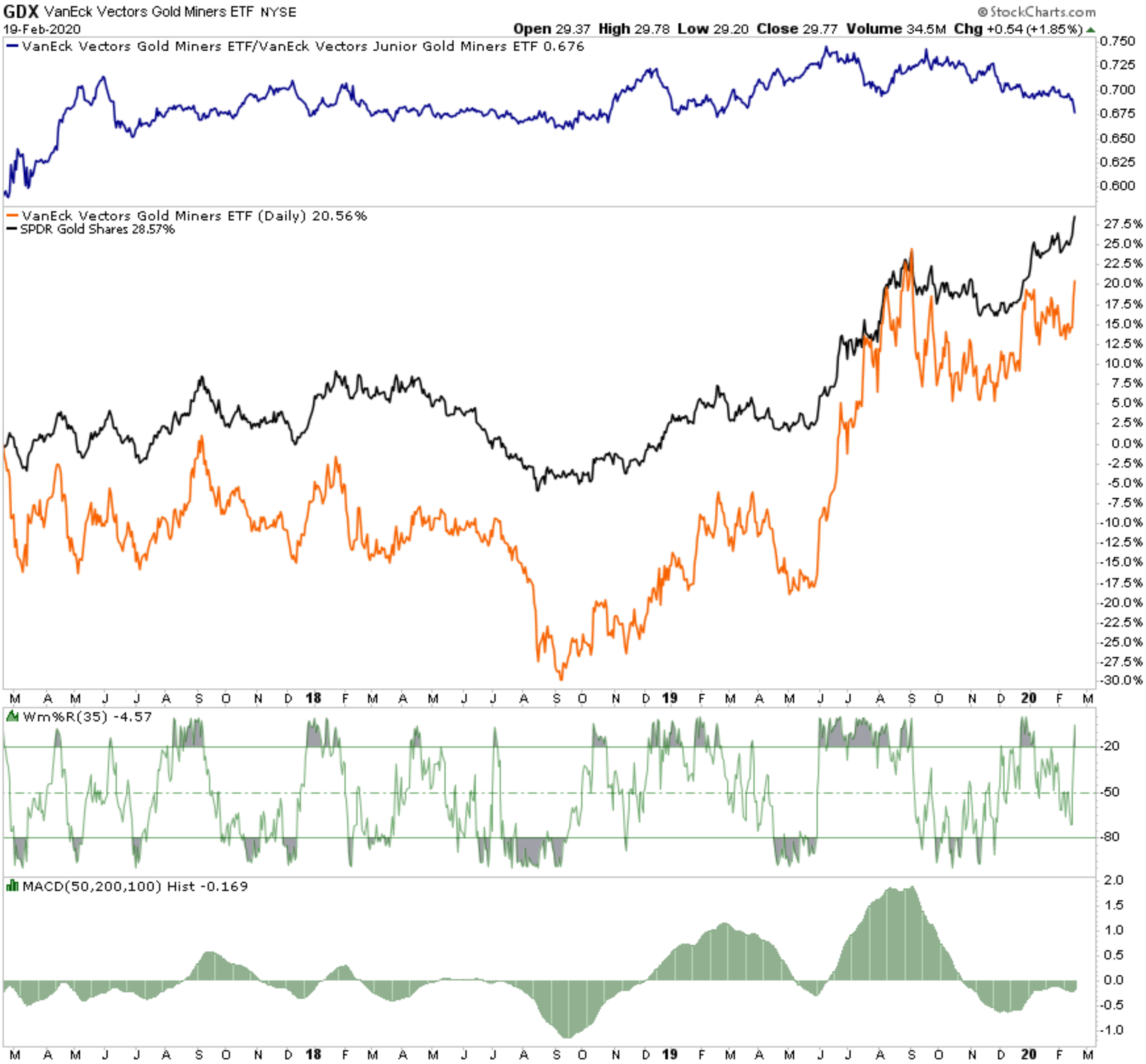
However, expectations of a weaker dollar, due to ongoing Federal Reserve interventions, could be a boost to oil prices in 2020, however, there are still many deflationary pressures weighing on the sector. Given the extremely low correlation between energy stocks and the markets, we could well see a rotation into energy in the year ahead. Keep a watch on our sector report weekly for updates on positioning.

Large Cap Growth Vs. Value

Over the last few years, as the Federal Reserve has been continually intervening into the financial markets, large cap growth, and primarily momentum, have dominated the returns versus value oriented stocks and sectors.

With the historical correlation between growth and value at historically low levels, we are potentially seeing an early rotation into value from growth. It is too early to make a full commitment to value in portfolios, but starting to add value to a growth portfolio makes a lot of sense. Currently, everything is extremely overbought *(both value and growth)* so caution is advised.

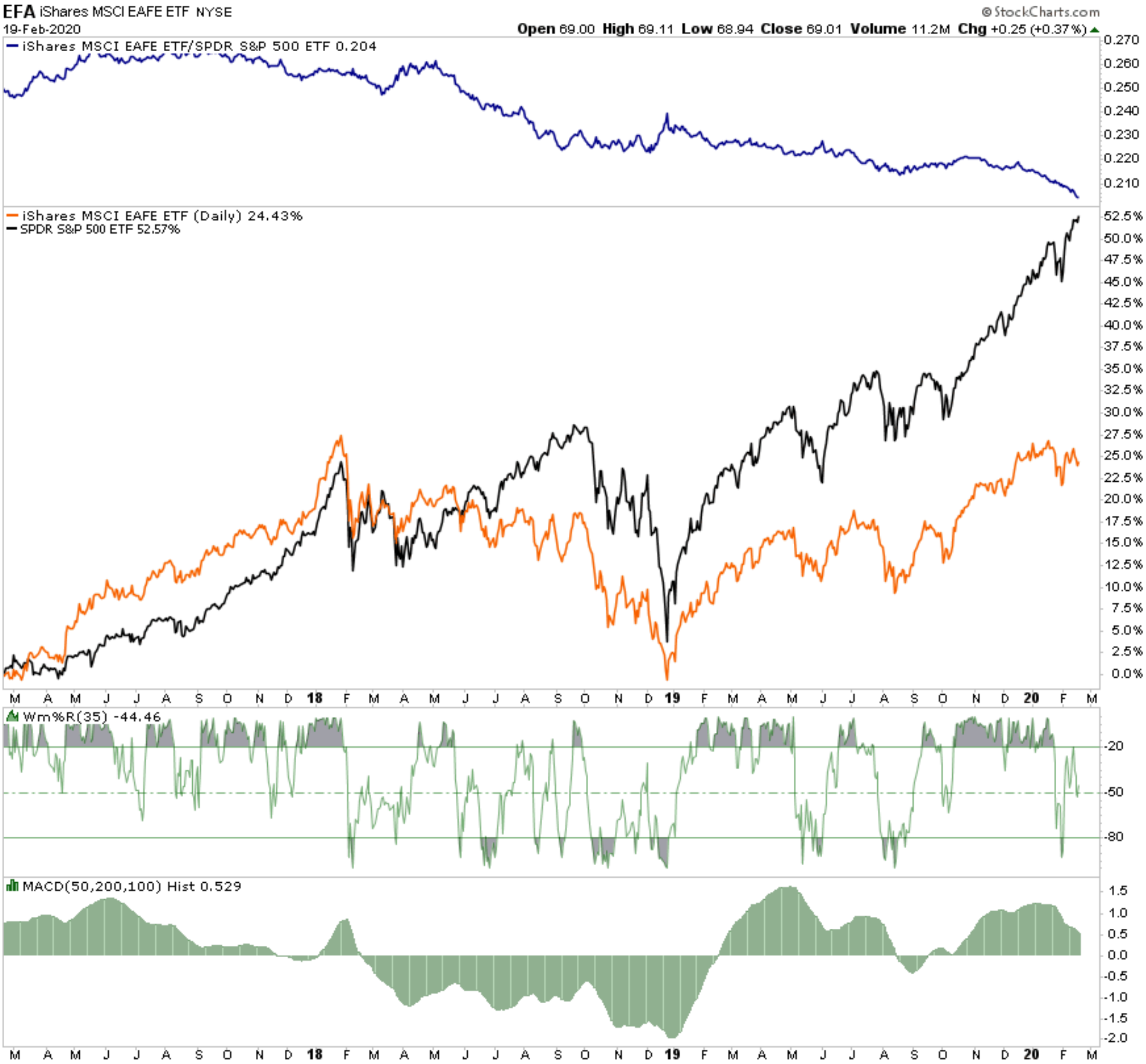
Gold Miners Vs Gold



We have been long gold and gold miners for a while since gold bottomed earlier in 2019. However, currently, gold miners are very overbought but are in the process of reversing their "*sell signal"* from October of last year.

With the Federal Reserve pumping in liquidity, concerns over inflation have returned which is good for gold. While we are long gold miners, the junior miners have begun to outperform the majors. There is much more risk in the junior miners due to balance sheet concerns, but in a *"risk on"* market that seems to matter little. **Keep a watch for our weekly Portfolio Position reports for updates on our gold and related holdings.**

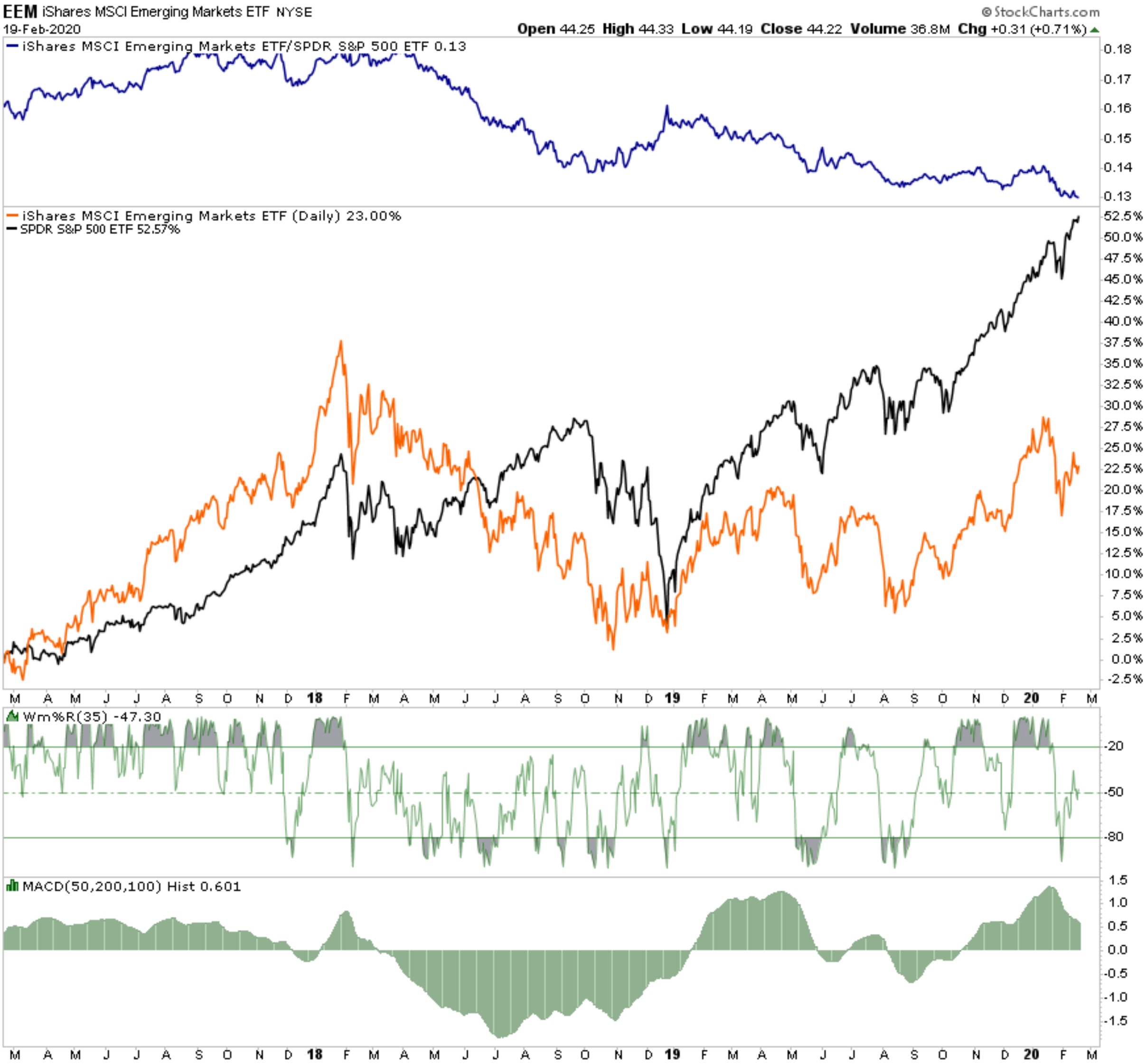
International Vs Domestic Markets



International has lagged domestic stocks since 2010. The previous improvement in relative performance faded quickly, and with a strengthening dollar in the works, there is risk to the sector. While relative valuations are cheaper on the relative basis, slower economic growth is making exposure to international stocks less attractive.

With the correlation between international and domestic markets at historic lows, a rotation bet seems logical. We agree, however, let's wait for confirmation before making large bets. **Watch our weekly Position and Index Reports for updates on our international holdings.**

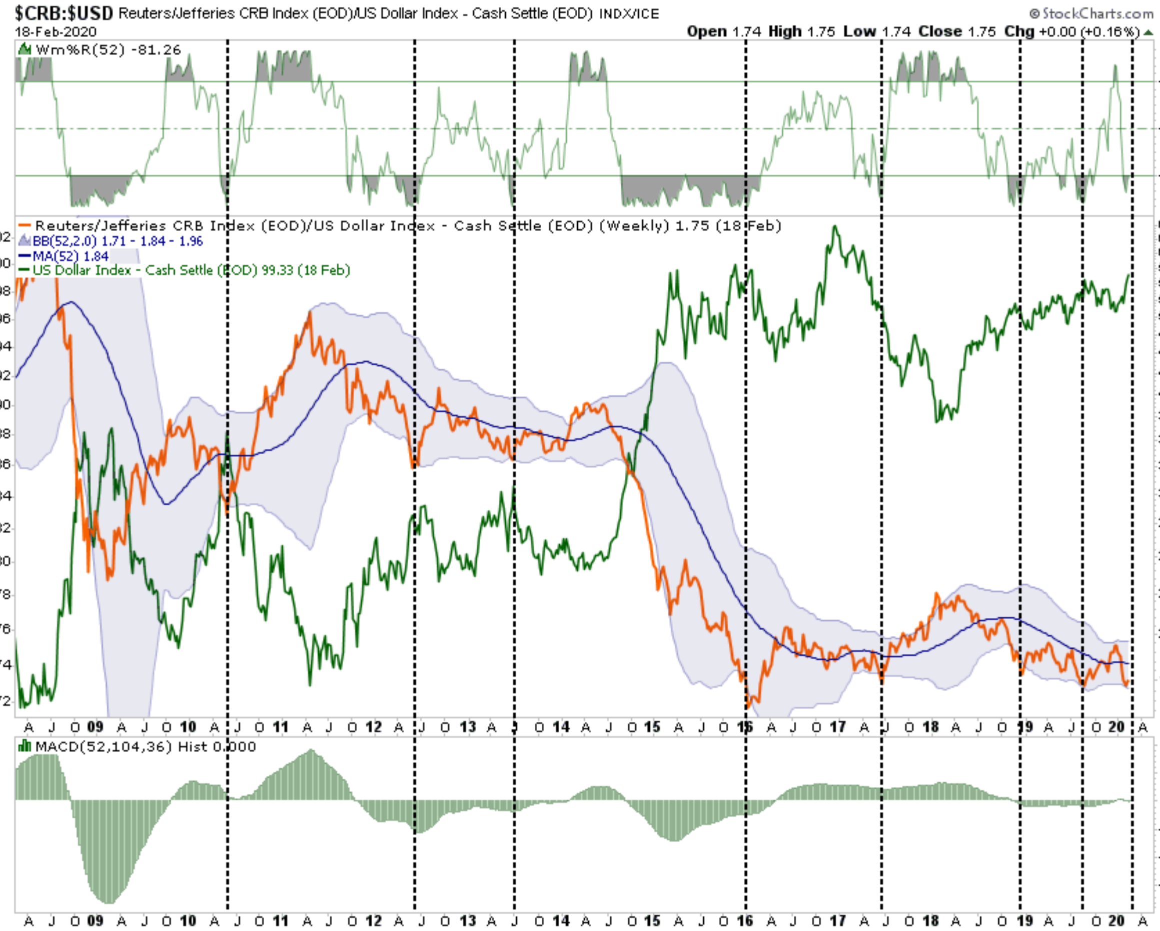
Emerging Vs. Domestic Markets



Emerging markets are exactly the same story as international markets above. Again, emerging markets are extremely extended and the correlation between emerging and domestic markets is improving.

Again, let's wait for further confirmation, and a better entry point, before getting aggressive on the sectors. **Watch our weekly Position and Index Reports for updates on our emerging market holdings.**

Commodities Vs US Dollar



This is probably THE most important chart of the series as the dollar affects not only commodities, but our energy analysis, international and emerging markets, and ultimately the stock market itself.

With the dollar showing some signs of strengthening due to the global virus, there remains a disadvantage to commodities, gold, oil and energy, international and emerging markets. It is too early to bet *"weak dollar"* plays, but the very oversold condition of commodities to the USD suggests we may see an opportunity emerge soon.

Currently, the stronger dollar is weighing on commodities, however, commodities are very oversold short-term. Look for a bounce which starts to show some signs of relative strength, combined with a reversal of the dollar.

Have a great weekend.