Sand Spring Advisors LLC

Seasonal Pause?

by,

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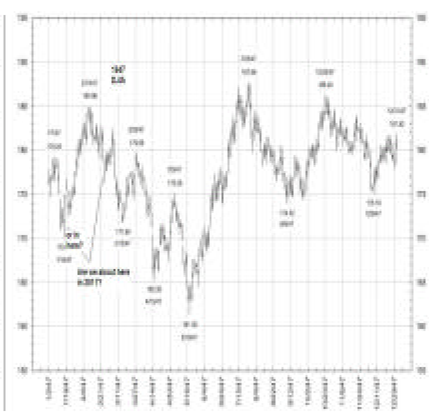
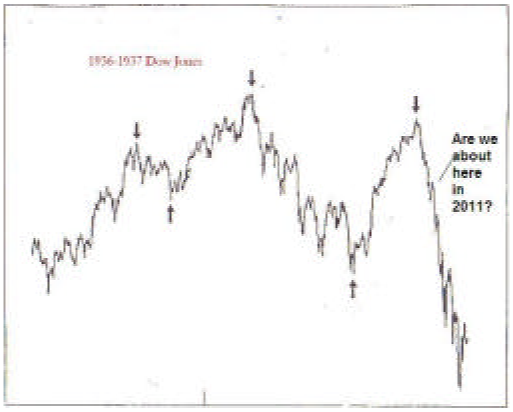
As you may appreciate by now, I have been waffling for sometime now between two bearish analog paths for the equity market.

The first is a "chop-chop stumble pattern" similar to late 1946 into early 1947. It starts with a triple top formation and sharp decline that is then almost fully retraced with back-and-forth gyrations that eventually end in new lows (later in 1948 -- not shown -- or equivalently in late 2012).

2011 vs 1946-1947

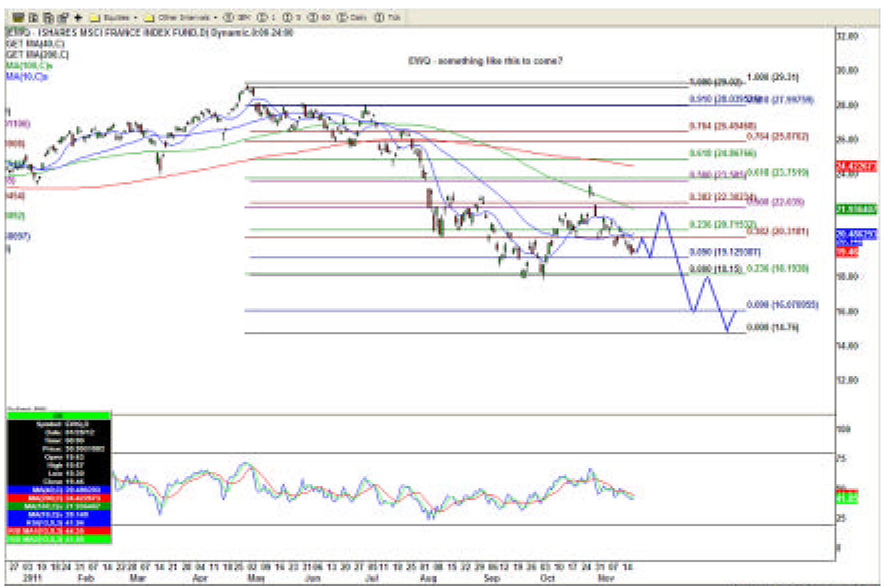


The other is a more dramatic decline that has the entire 2000-2011 topping pattern of the weekly DJIA chart looking oh-so similar to the daily topping pattern left previously by the DJIA across 1936-1937.



The Economic Cycle Research Institute (ECRI) recently stated that most of its leading indicators have slipped back into recession mode. Noteworthy to the second potential analog above is that U.S. unemployment rate has never been as high as it is presently at the start of a recession except in one prior instance: 1937.

Elsewhere, I continue to believe that Europe still has new lows to come – with its ultimate decline from mid-2011 highs only about half completed at present. GDP per capita in Italy is lower today than it was a decade ago; productivity growth has been anemic. Italy – with or without austerity measures enacted – simply cannot grow its way out of debt. The European debt crisis is likely to continue limping along into 2012. While a reprieve is possible over the next six weeks, watch for more problems come January.

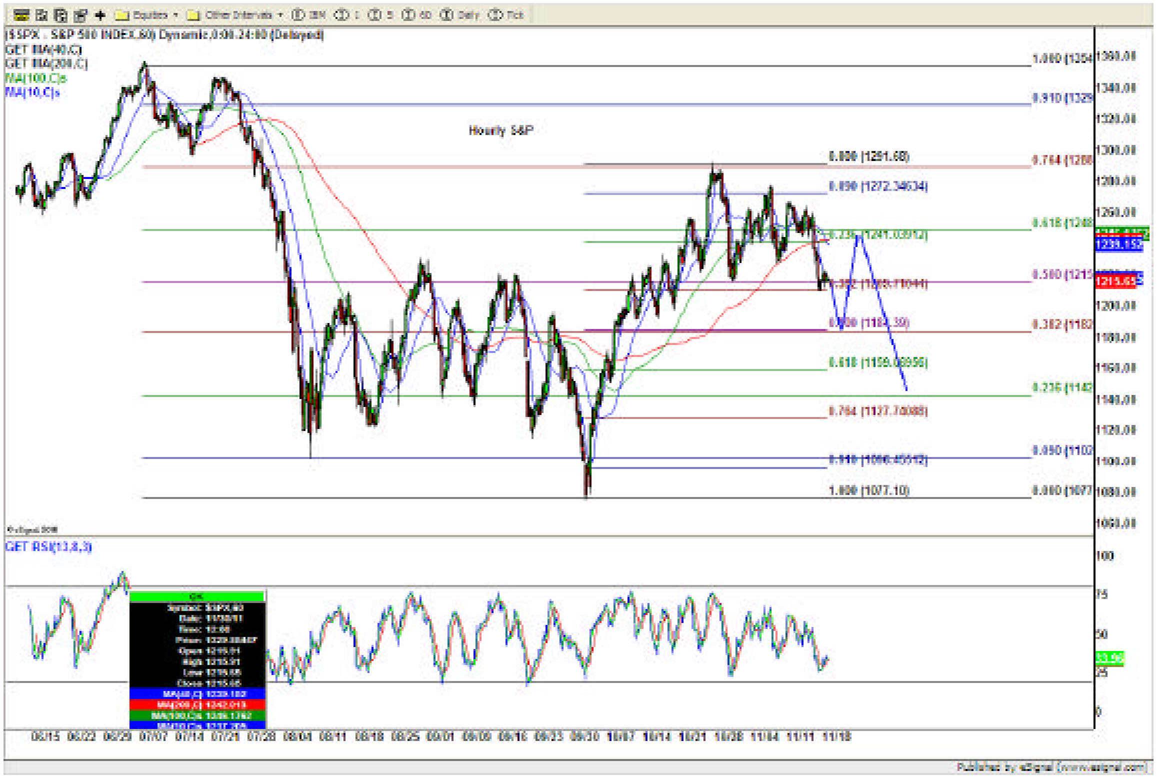


The key <u>problem</u> that I face with any of the above views is one of <u>seasonality which tends to hurt bearish views at this time of year.</u> The pace of trading already was dead slow this past week (even on a market decline, for a change), and with Thanksgiving and Christmas coming, I can easily imagine the markets offering up one more short-term levitation before the eventual price destruction transpires.

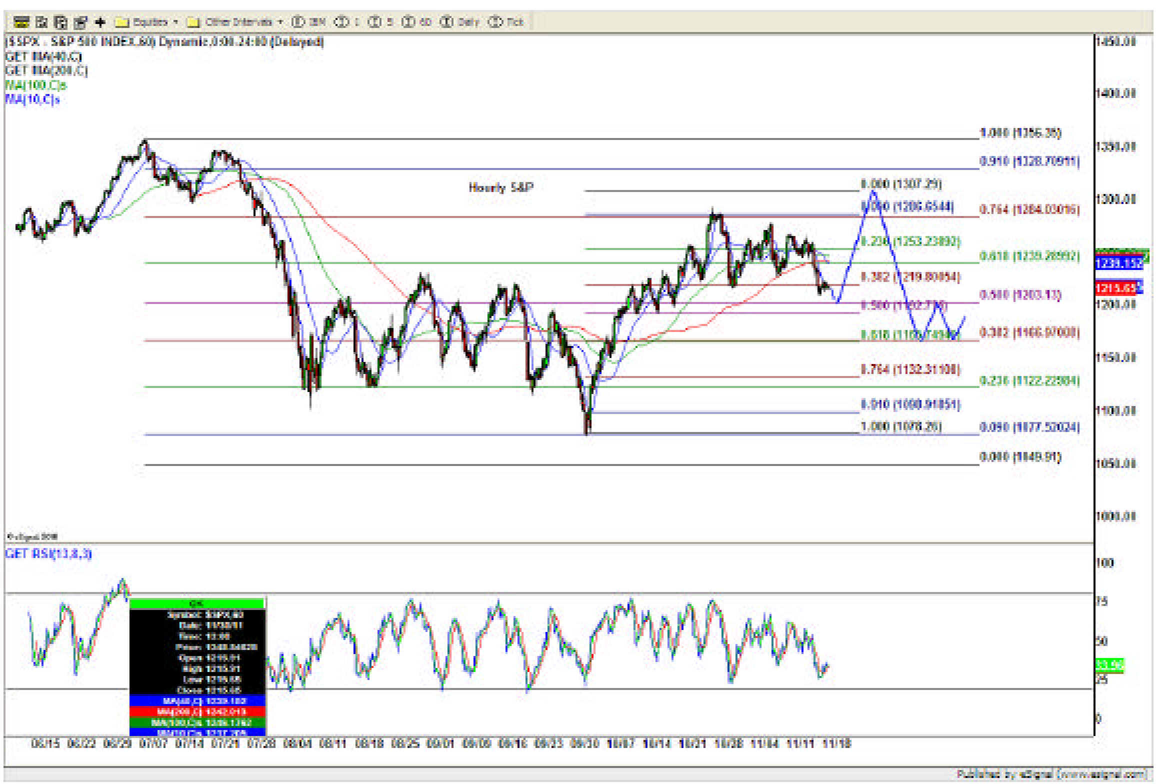
Can't you just feel the momentary moment of joy forthcoming when the Congressional super-committee actually passes some sort of budget deal at the last moment on Thanksgiving eve? Hurrah! -- even if -- in the end -- cutting the federal budget will likely be bearish for stocks, not bullish. With the U.S. Government already representing over 30% of the U.S. economy, when the last party in town starts to slow its spending, so too will corporate profitability be pressured. Equity P/E's may not seem unreasonable at present, but what happens when the "E" portion of that calculation retreats from peak earnings?

Yet how many Novembers and Decembers have I attempted to be short equities over the past two decades, and almost always regretted the attempt? It has always seemed like a giant struggle. From somewhere in its bag of tricks, the market always seems to bow to the bulls over this time period.

Zooming into the short-term hourly fractal rhythm of the S&P 500, are we going to do something like this over the Holiday season?



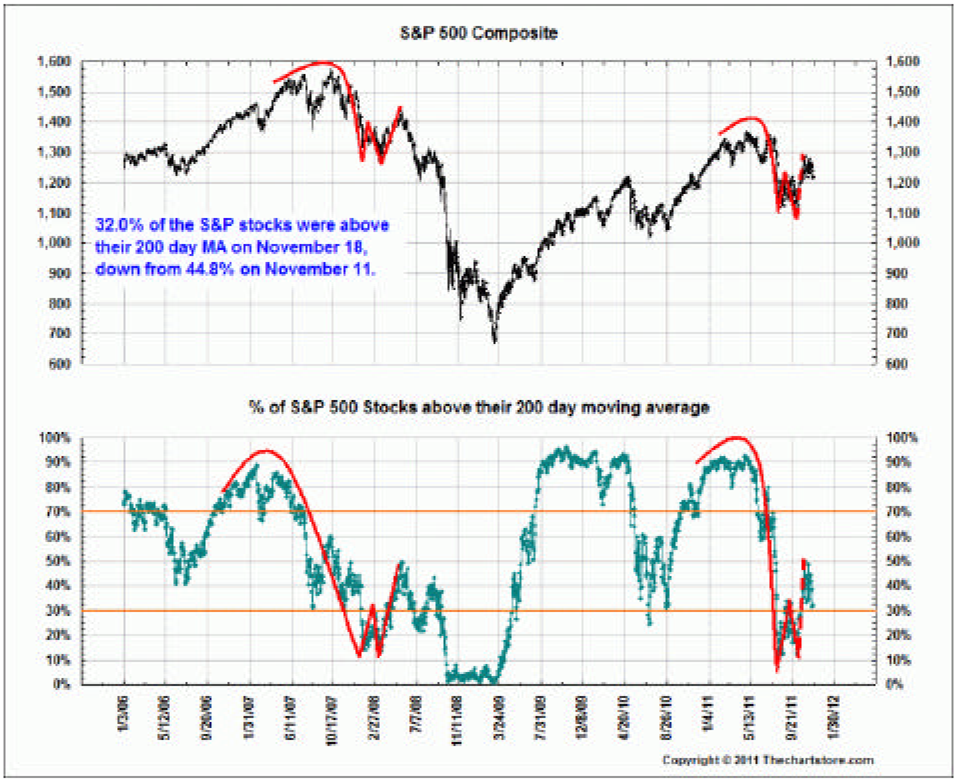
Or perhaps something like this?



Short-term, I am a buyer of the S&P around 1167 and a seller around 1307 – if either of those extremes ends up being touched. To be honest, <u>it is harder to anticipate the immediate jiggles in between</u>

these two extremes. If we do in fact meander through the last 6-weeks of the year without undue weakness, this will likely set up an explosion to the downside in January 2012.

The overall pattern also remains very similar to that of the 2007 top – almost a fractal miniature in motion. The only question is how much time the market may still need to back-and-fill before the eventual "wush" to the downside when an Elliott 3-wave transpires.

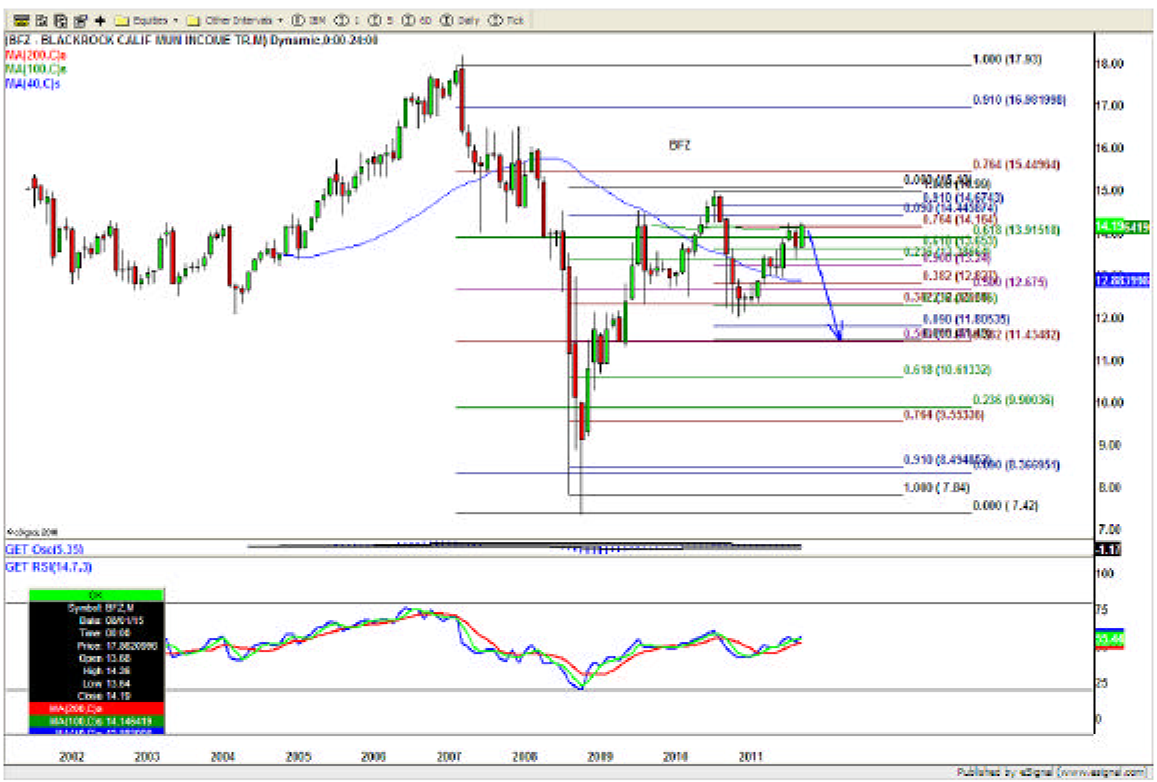


From a cycle perspective, our late October 22nd-24th cycle window was somewhat unsatisfying or at least unclear. If the cycle arrived a few days late, then one could point to the October 26th high in financial stocks as potentially important, but I generally don't like bending my cycle dates that much – particularly on highs. The next minor pi cycle dates will be March 1, 2012 (probable minor low); July 10, 2012 (probable minor high); and then November 17, 2012 (my call for a more major low).

One interesting cycle tidbit pointed out to us by a reader is that the September 6, 2011 high in gold was exactly 1047 days (pi * 1000 * 1/3) from the October 24, 2008 low in gold. This may mean that this high will be lasting. Certainly gold is psychologically where a great deal of excess remains. People are "hiding" in gold even while debt deleveraging transpires. Debt deleveraging does not imply run-away inflation. The central bankers worldwide would certainly like to perpetuate a world living on credit, but are they just pissing into the wind with their monetary QE tactics, while $100+ trillion of total global debt servicing and unwinding pushes against them? Any whiff of actual austerity implementation in Europe and actual budget cutting in the U.S. is bearish gold. I am not positioned in this market at present, but I am watching it carefully.

And then of course there is China – that huge economic experiment in motion where housing & infrastructure investment is currently outpacing any demand or long-term ability to pay for such. The good news on the FXI etf chart longer term is that there is a clear missing high above the 2007 peak. The bad news is that first there is tons of resistance between 39.50-40.50, and a chart pattern that suggests a fall across 2012 to as low as 22.65. For those itching to buy China, this latter level will be the opportunity to do so – but not now. In the short-term we would sell any Holiday period rally – if offered – towards the 40 level.

More will follow as usual by e-mail. Shorts in BFZ should also continue to work on a slow-burn basis.



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