HedgeFolios Strategy Advisory

"The Agenda Overpowers All Negative Factors… For Now"

11-16-2023

Our Current View:

Tuesday's big rally was reportedly due to the marginal declines in the important CPI components. It provided an excuse for the HFT (high frequency trading) to rally the market and cause a massive short squeeze, fueled by algo trading outfits with some help from Wall Street.

We assume that this rally serves the profit motive of HFT, while at the same time helping Wall Street to sell large positions in underwater stocks before year-end. There just wasn't enough volume the past weeks to accomplish that. To unload big positions, they need to entice strong buying.

Now the short-covering, helped along by the bulls, is providing that volume. Tuesday once again saw the most highly shorted stocks (i.e. worst fundamentals) as the biggest gainers.

Yet, that doesn't mean the rally won't last longer than typical bear market rallies. We expected high volatility from now until year end and now we are getting it. But with Tuesday's strength, this rally is destined to last longer than the typical short squeeze.

Stocks cooled off today after their 2-day spike as the large cap indices were mildly changed. The S&P 500 ended the day up 0.1% while the NASDAQ Comp was up a fraction. The DJI settled 45 points lower for a -0.1% loss.

However, the Russell 2000 retreated 1.5% today, the biggest mover among the major averages. Normally we would say this suggests the market will see further selling ahead. However, given the Russell's big 5.6% gain the past two days, today was likely just breather.

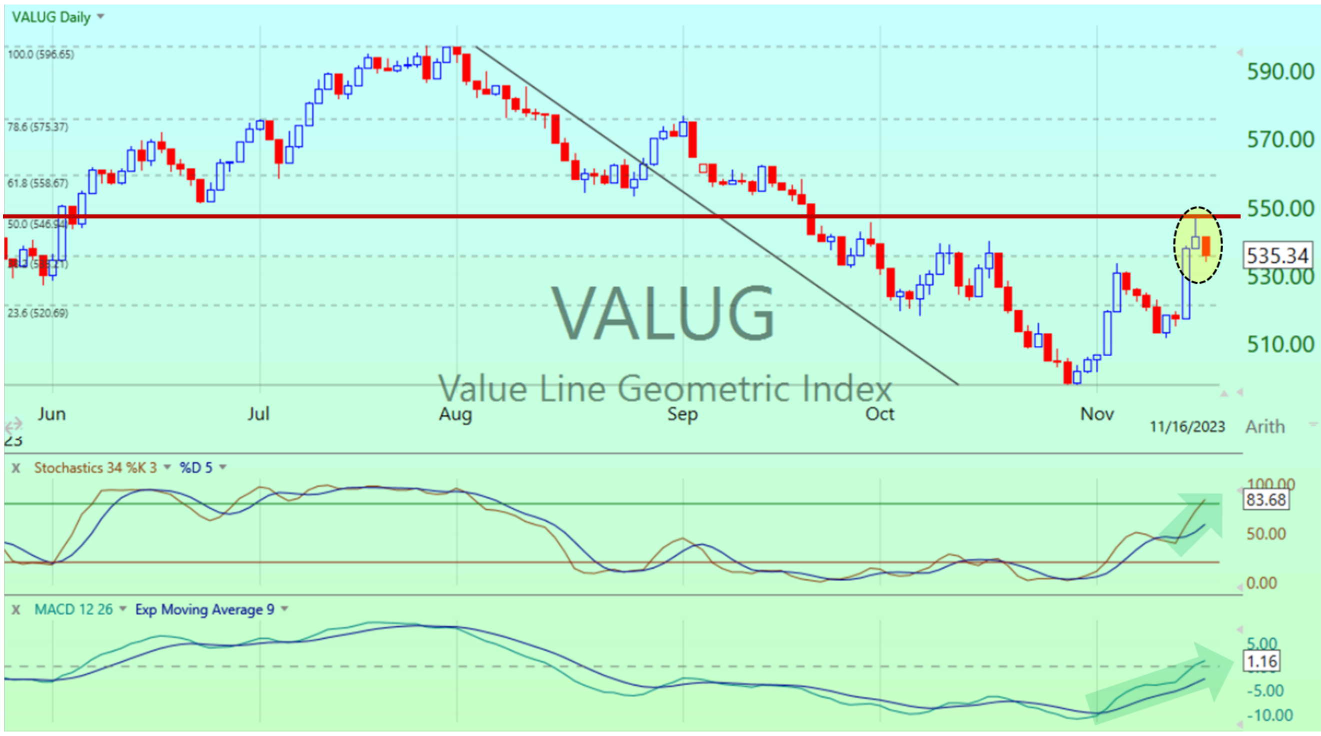
The daily chart of the IWM (Russell 2000 ETF) ran into resistance from its 50% retracement of the August to October decline yesterday (red horizontal line), leaving a negative candlestick.

That suggested today would be a down-day for the small caps. That level coincided with its 100- and 200-day m.a.'s (green sloping line and pink sloping line, respectively), which made it stronger resistance.

However, a couple of our technicals still look constructive. The Dohmen Money Flow (middle) and the MACD (bottom) are both climbing higher with the MACD rising into positive territory on Tuesday and staying there.

The broad market VALUG Index was also rejected on its attempt to go above its own 50% retracement level yesterday (red horizontal line). It slipped lower today as shown on its daily chart below. However, technicals remain constructive.

The Slow Stochastics (middle) climbed higher this week and looks positive. The MACD (bottom) has steadily climbed higher since the start of November and is now in positive territory. Thus, any sort of consolidation now should be brief and be followed by a breakout in the VALUG.



However, as we explained to members of our ***Smarter Stock Trader*** and ***Fearless ETF Trader*** earlier this week, we believe the mega-cap tech stocks, which are the primary drivers of the NASDAQ and S&P 500 indices, will lead the way higher into year end.

Looking at the weekly chart, which makes it more important, we see the QQQ (NASDAQ Comp ETF) has climbed back to its July highs. That makes it resistance (red horizontal line).

Today it made a new closing high for the year and its highest close since January 2022. Naturally there will be some hesitation in this price area, perhaps leading to a brief pause and digestion of the rally over the last 3 weeks.

However, we believe it will breakout thereafter and test its record high set in November 2021, which marked the start of the bear market. That resistance is in the 408 area (blue horizontal line, “X”), which is another 5%+ from today’s close.

The internals look constructive (MACD about to crossover to the upside, Fast Stochastics soaring higher), which give us further conviction in the QQQ breaking out into December.

The question is whether the NASDAQ will set a new record by year-end, just 6 weeks away. We think it can given the reasons we mentioned in Tuesday's issue of our trading services:

> *"Big money managers who are positioned with high cash levels thinking that would look good for their clients to see at year end will now have to buy the biggest gainers in order not to look like they missed a move"*

This will be used to get all the "smart" and "dumb" money that's sitting on the sidelines to jump in and celebrate. It will be the perfect trap to set for an early 2024 plunge.

Our HedgeFolios:

We have been very cautious the past several weeks in our positions, without having big exposure during the recent volatility, and now have the cash that can be utilized.

We exited our two inverse ETFs (HDGE, TBF) in our **Opportunistic, Global Equity, and Income** models today. We believe the environment we entered this week sets the market up for a good year-end rally and therefore pushes all the problems that still exist into next year.

Interest rates and Treasury yields are no longer a primary concern for investors. This will have a negative effect on the UUP (Bullish Dollar ETF), which is why we sold out of it today in our **Global Conservative and US Conservative** models.

We also sold the remaining small position in UNG across all 5 models as the oil, gas, and energy sectors are suffering from declining demand and oversupply.

To take advantage of what we think will be a good opportunity for the heavily weighted and widely held "winners" this year (i.e. large cap growth technology stocks) we added QQQ and IYW to all 5 models.

The new positive environment may also trigger the next bullish period for anything related to AI. This could be the launch for a very speculative market period. The Fed will be able to relax a little, thus debt capital should become more available, even for speculation.

This is why we added exposure to the AI sector via the AIQ ETF in our **Opportunistic and Global Equity** models. Leaders in this space have continued to do well and therefore have some good momentum going into 2024.

Inflation hedges like metals, gold, and silver should do well, especially as the danger of a sharp plunge in the US stock market is now on the backburner. We have written in our other research services that we believe that Gold will be at a new record high soon. Therefore, we added GLD to all 5 models today.

Lastly, we increased our allocation to BIL in all 5 models as it pays more than holding cash in your brokerage account (most brokerages pay 0.01% APY on cash held).

We now hold between 25-39% in cash across all 5 models, which we may deploy in the coming weeks if the rally proceeds as we expect it to.

Our Conclusion:

Our work suggests that the engineered year-end rally has started. We believe the agenda, for all the reasons we have given, is to have a rally in the popular stocks into year-end. It may even go beyond year end and into early 2024. All the negatives will be forgotten for a while.

Short sellers will reluctantly cover an increasing number of their short positions, especially those with the worst fundamentals. It is human nature not to close out early using hope as a tool.

Eventually the rally will attract investment buying as money managers can't afford to be left behind. However, we would not go overboard and not be overexposed as high risk most often backfires. At this rate, stocks will become very overvalued again.

Wishing you successful investing,

Bert Dohmen and team