New Highs or Double Top?

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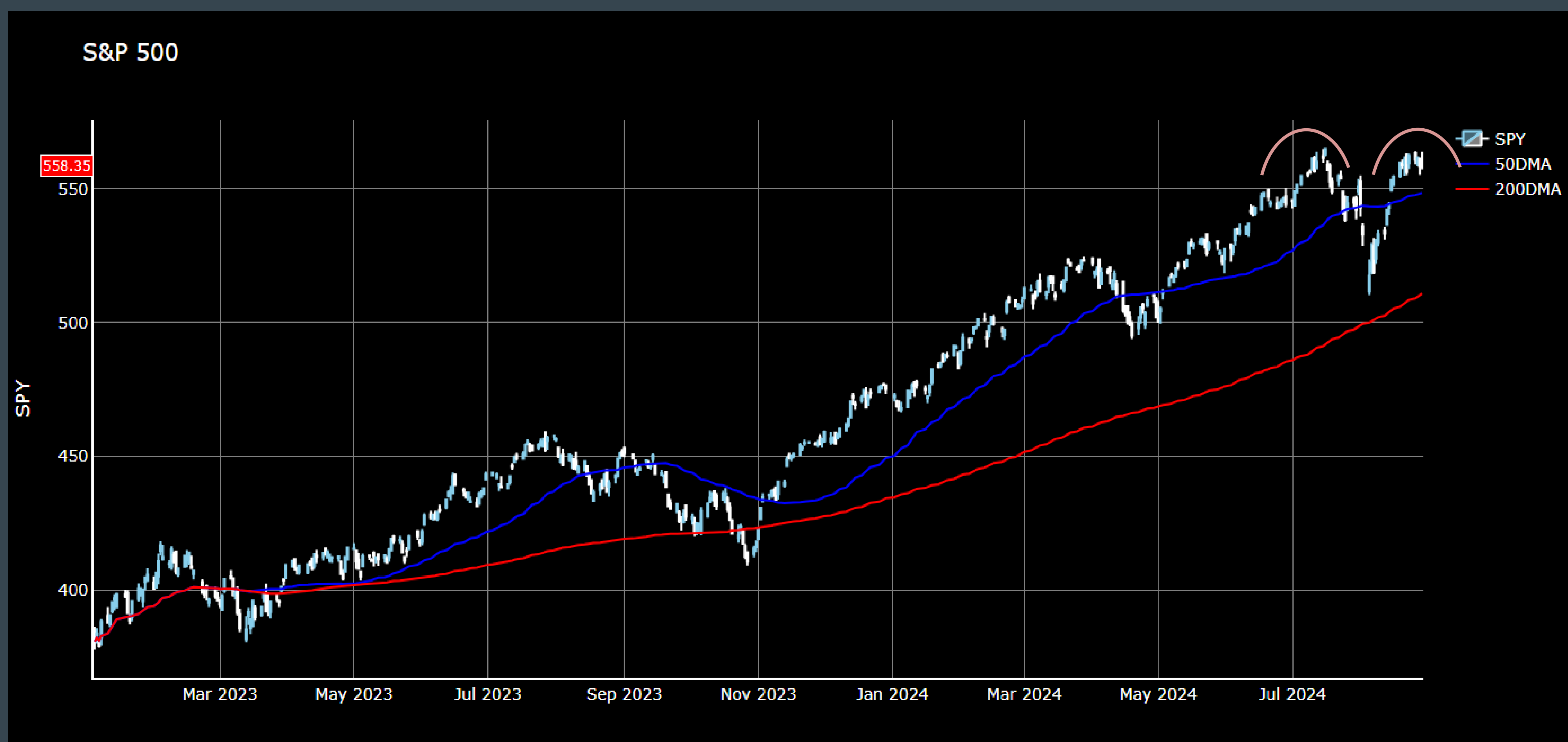
Growth concerns continue to be deferred as the GDP revision for Q2 was adjusted upward to 3.0% from the initially reported 2.8%. The revision higher was largely driven by consumption, which is surprising given how many companies have been reporting challenges faced by consumers. However, it's clear that the resilience of higher-end consumers, buoyed by asset prices near all-time highs, should not be underestimated. The Fed is acutely aware of this dynamic, understanding that supported asset prices translate into sustained consumption and growth. This upward revision led to some selling pressure in long-term bonds, with TLT reflecting this shift, and 10-year yields hovering around 4.0% once again. The key event to watch next week will be the release of the August Nonfarm Payrolls report, with expectations set at 163,000 jobs. July's report, which came in below expectations at 114,000, was a catalyst for the recent 9.5% market correction. At that time, we highlighted that, despite the weaker headline number, the labor market's underlying dynamics were not as robust as the broader consensus suggested. However, a single report of 114,000 was not cause for immediate concern. We anticipate heightened volatility around Friday's report, but it's important to note that a trend of sub-100,000 or negative job reports would be required to signal a more imminent recession.

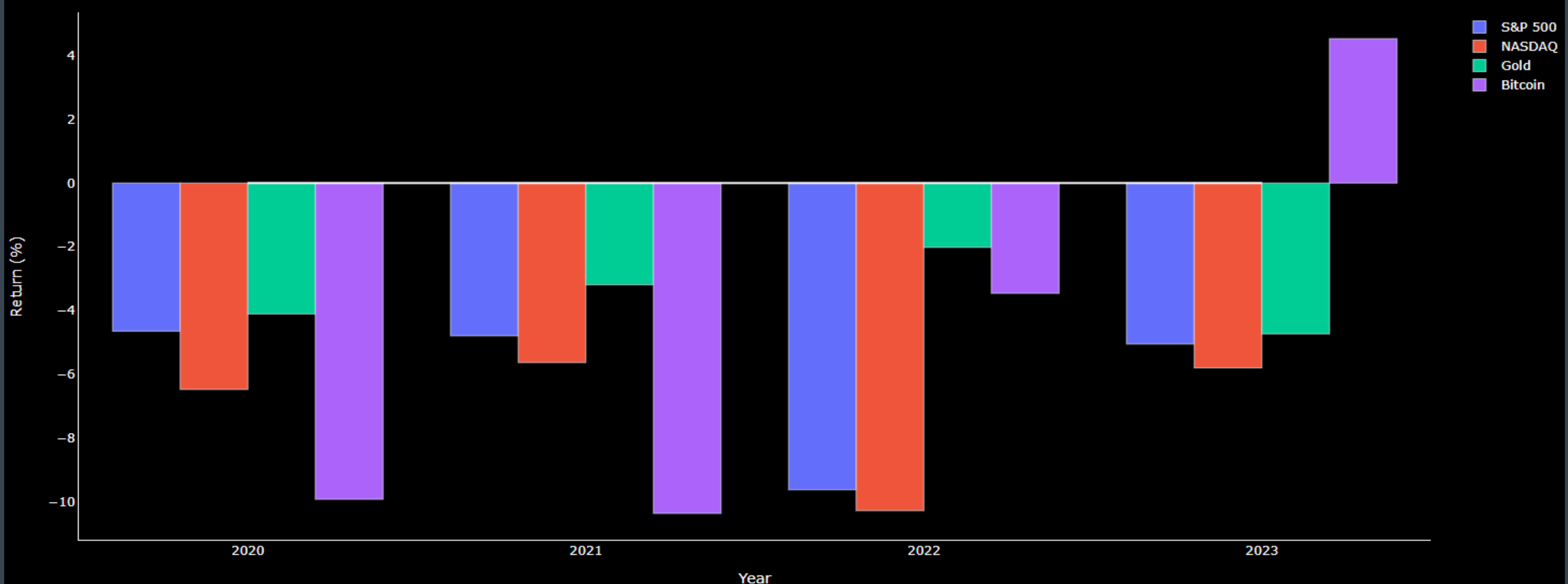
The S&P 500 has nearly recouped the entirety of the correction experienced over the past month, though it has stalled just shy of reaching all-time highs. As noted last week, sectors outside of Technology have played a pivotal role in both stabilizing the market at its lows and driving the subsequent V-shaped recovery. This sector rotation becomes particularly evident when examining the Equal Weighted Index (RSP), which has already reached new highs. The key question now is whether the broader market will follow suit and break through to new highs, or if we are instead on the verge of forming a double top—a question we'll explore further in this analysis.



The market can absorb a short-term correction in the Technology sector, but over the long term, it requires sustained participation from these key names to continue moving higher. The challenge is that other sectors have become such a small portion of the index relative to Technology that their ability to influence the broader market is limited. Currently, Technology accounts for about 45% of the S&P 500 and is facing resistance at its 50-day moving average (DMA). This situation underscores the concentration risk we've previously highlighted, where a few key players—namely, the "Magnificent 7"—hold disproportionate sway over the market's direction. As these names consolidate, a more nuanced approach to portfolio positioning than just owning the market is necessary to continue capturing upside potential.

Over the past few weeks, we've supported the soft landing narrative, drawing parallels to the 1990s—the last time the Fed successfully achieved a soft landing. In that scenario, rate cuts became a catalyst for a renewed rally, provided the labor market remained resilient. However, in our search for alternative perspectives, we've found evidence suggesting that, despite the market retracing most of the recent correction, there could be another leg lower or a retest of the lows based on historical patterns and seasonality. We wanted to present that possibility here:

As we enter September, we reviewed the performance of various assets over the past four years, focusing on the S&P 500, Nasdaq 100, Gold, and Bitcoin. Our analysis revealed that out of these four assets, only Bitcoin had a positive September and that was last year. The S&P 500, in particular, has shown consistent declines during September, with losses of 4.6% in 2020, 4.8% in 2021, 9.6% in 2022, and 5% last year. Historically, September has not been favorable for market participation. However, this year differs from previous ones, as rate cuts are anticipated this September, which could influence market dynamics differently than in the past.

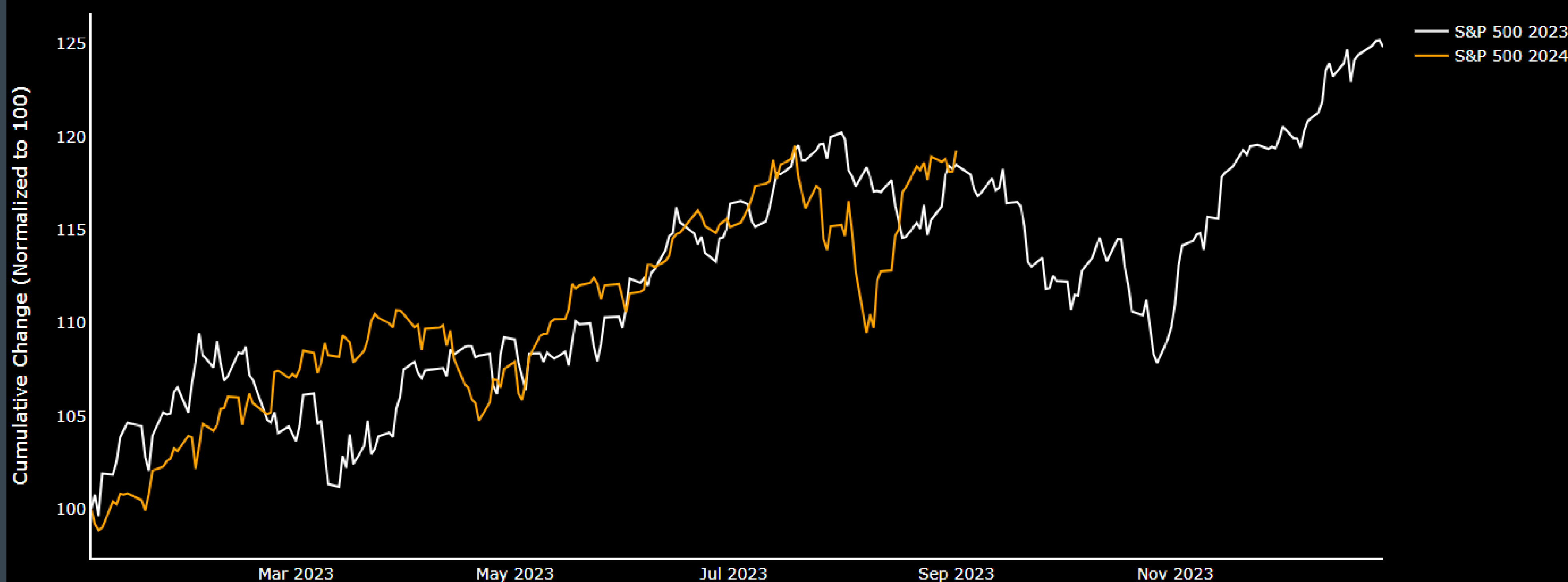


The U.S. Dollar has declined from 106 to just above 101 over the past two months. The relationship between the Dollar and stocks is dynamic, but in recent years, they have generally moved inversely. The Dollar's recent downtrend has played a role in helping stocks rebound from their correction lows. However, the Dollar now appears oversold. The weekly chart, with Bollinger Bands, indicates that the Dollar has broken through its lower Bollinger Band, a move that historically has been followed by a rally. While we believe the Dollar will ultimately continue to weaken as the Fed gears up to cut rates, in the short term, we anticipate a bounce before the next leg lower. This potential Dollar rally could exert pressure on the broader indexes.

We continue to focus on the 10-Year Yield, particularly the level of 3.78%. This level has been tested multiple times following the disappointing Nonfarm Payrolls report and the unwinding of the Yen Carry Trade. So far, it has held, with yields climbing back toward 4%. The movement of yields has been closely tied to the Dollar, so a push toward the 50 and 200 DMA for the 10-Year Yield would likely drive the Dollar higher as well. If Friday's Nonfarm Payrolls report comes in hotter than expected, it could lead to a repricing of the 150 bps in rate cuts that the market currently anticipates over the next six months, potentially sending the market lower.

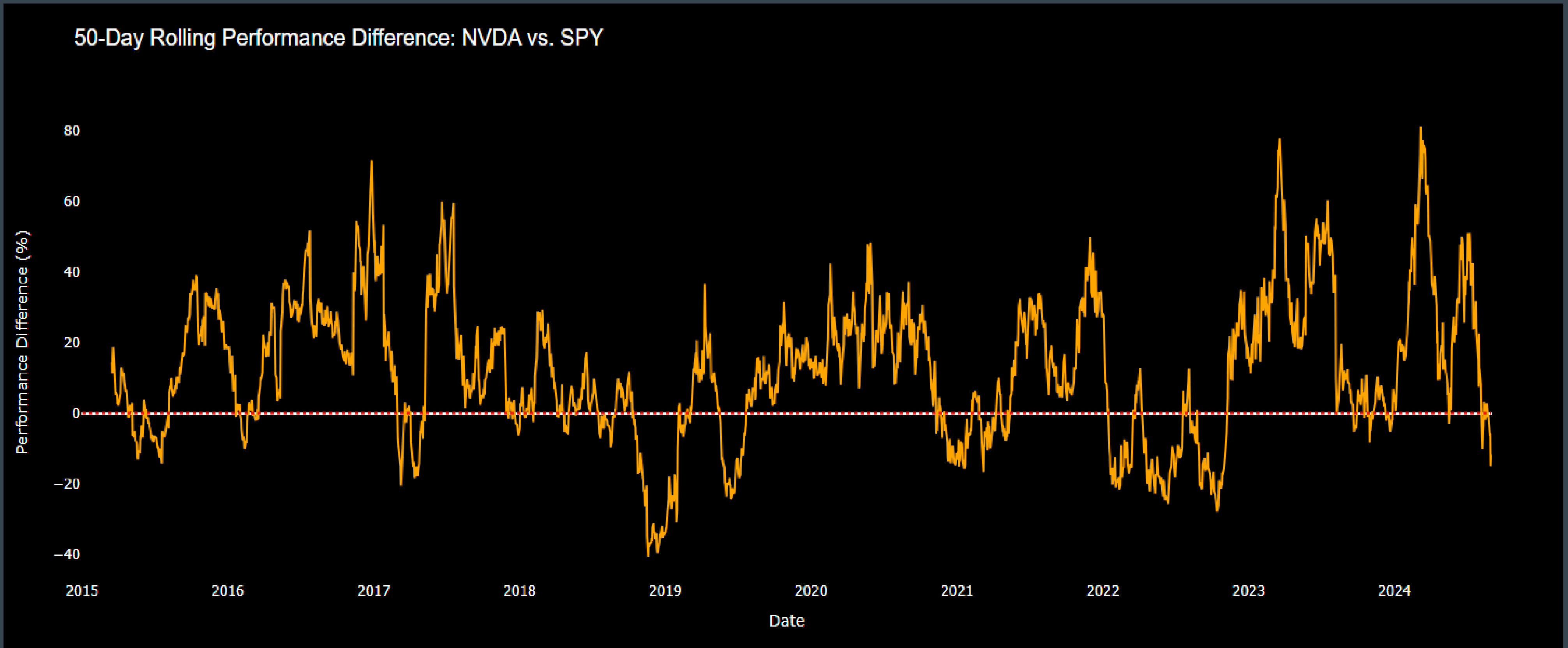
Volatility spiked early this year, with the VIX reaching 65 in August. Seasonality suggests that the volatility is far from over. We're in an election year, and markets traditionally dislike uncertainty. The outcomes of the upcoming elections, including the composition of Congress, are still unclear, adding to market jitters. Coupled with slowing growth and a Fed that is expected to cut rates, this creates a recipe for heightened risk. Despite this, the VIX has dropped back down to 15 as of Friday, making protection relatively inexpensive. The probabilities favor increased volatility through October.

Three weeks ago, we highlighted a chart comparing the market's path in 2023 to its trajectory so far in 2024. The correlation between the two years is strikingly similar. Last year, the market experienced a correction in August, followed by a rebound that failed to reach new highs before rolling over into a lower low. This year, we've seen a similar pattern: a rally into August, followed by a 9.5% pullback, and now the market has stalled at recent highs. If this pattern continues to mirror last year's behavior, we could be facing additional downside as we move into November.



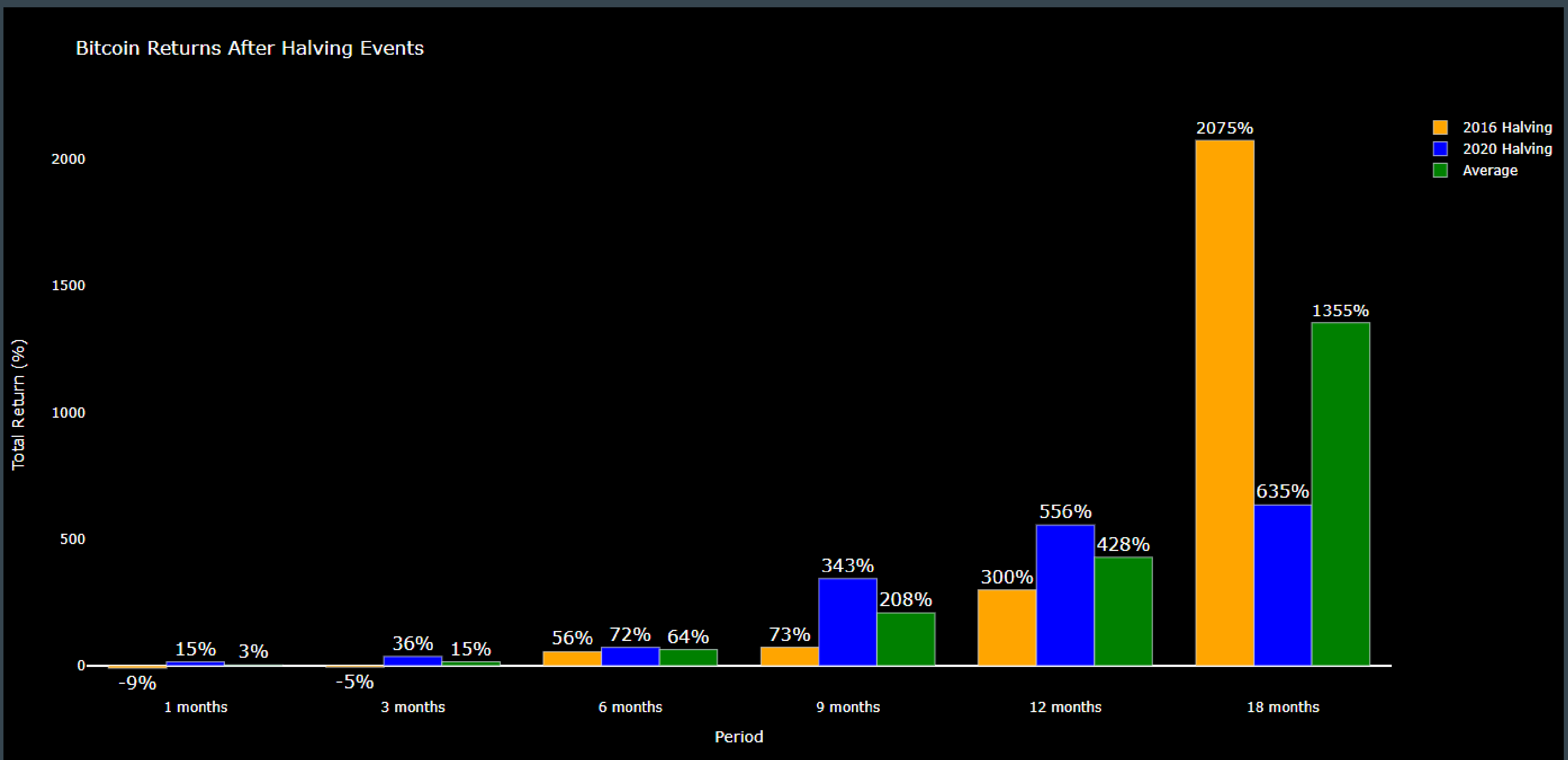
The Tech sector's struggle to rebound can be partly attributed to the performance of Nvidia. A few months ago, a sector rebalancing made Nvidia a top 2 holding, surpassing Apple. Since then, Apple has outperformed Nvidia. The key event last week was Nvidia's earnings report, which turned out to be a classic case of "buy the rumor, sell the news." Despite Nvidia's fundamentally strong performance, the market was unimpressed. Revenues beat expectations by 2.4%, coming in at $30 billion, marking 15% growth quarter over quarter and an astounding 122% year over year. Data Center Revenue, which drives their chip demand and constitutes over 80% of their total revenue, hit $26.3 billion—up 16% quarter over quarter and 155% year over year. While their gross profit margins dipped slightly, they remain robust at 75%, representing a 450 basis point expansion compared to the prior year. Despite these impressive numbers, the stock fell 6% the day after the report. The challenge for Nvidia, and other companies tied to AI, is that they are now priced for perfection. When expectations reach such lofty heights, they become nearly impossible to meet.

The rolling 50 day return of Nvidia relative to the S&P 500 has now gone negative for the first time since it briefly dipped below 0 in November of 2023.



To conclude this week's newsletter, let's touch on the current Bitcoin cycle and where we stand relative to previous cycles. Bitcoin is up over 30% this year but has been trading within a range of $50K to $70K since February—a duration that feels like an eternity for crypto investors who are accustomed to the massive volatility and rapid gains typical of this asset class. Many anticipated a bull run pushing Bitcoin over $100,000 immediately following the halving event back in April, but history tells a different story. If we look back at the last two halvings in 2016 and 2020, significant price surges didn't occur right away. Instead, we are currently on track, performing in a manner consistent with those past cycles, suggesting that patience may be key as Bitcoin continues to consolidate before potentially making its next big move.

Historically, the majority of returns within each Bitcoin cycle have occurred between 9 and 18 months after a halving event. With the April 2024 halving just 4 months behind us, we are still in the early stages of this cycle. A significant Bitcoin rally at this point would be unusual and would break the pattern established in previous cycles.



It's crucial to be mindful of time frames when analyzing market data or considering opinions on market trends. Earlier in this piece, we presented an argument for a stronger Dollar in the short term, driven by technical factors within current market pricing. However, looking more broadly, as we move into the latter part of the year and rate cuts come into play, the Dollar is likely to roll over and weaken. This potential shift would be beneficial for crypto, particularly Bitcoin, as the 4-year debt refinancing cycle has historically coincided with both a weaker Dollar and Bitcoin halvings. This is the environment where Bitcoin tends to thrive.

Bitcoin & Halving Events with USD Index
BTC Price (USD)
USD Index (DXY)
BTC-USD
USD Index (DXY)
Date
2015
2016
2017
2018
2019
2020
2021
2022
2023
2024
100k
10k
1000
110
105
100
95
90

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