TS Model Portfolios

Timely Analysis for the Informed Investor

March 2023

SPX rally is likely a bull trap

Overview: Mixed strength

Though we have been waving a red flag about the stock market for several months now, the cracks that we expected to see at this junction, have largely been delayed.

One key indicator that is starting to percolate is the CBOE Volatility Index (VIX). This real-time index represents the market's expectations for the relative strength of near-term price changes of the S&P 500 (source: Investopedia). It generates a 30-day forward projection of volatility and in particular, the degree of fear among market participants.

The VIX appears to have found support around 18 over the last 12 months (**Chart 1**).

Chart 1

The S&P 500 has dropped for the last three weeks among elevated US inflation fears and the outlook of additional Fed rate hikes.

Earnings are going to be the next battle front for the S&P 500. As valuations are currently high and stocks remain under pressure from hesitating earnings. Presently, about 94% of companies in the S&P 500 have reported Q4 earnings. About 68% have topped Wall Street expectations. This is a weaker beat rate than usual.

We note that bull traps are a false signal and typically feature a flattening out in earnings outlook between two or three quarterly earnings reports.

TSX outlook: Holding on to gains

Investors continue to assess the impact of higher interest rates on the Index into mid-year. The energy sector, one of the largest industry groups in the TSX, has continued to stagnate with ongoing weak oil prices (holding near $72) and natural gas prices plunging in Q1 nearly 65%.

On the opposite side, Canadian banks profitability remains steady. Higher interest rates from the BoC, will only benefit as their net interest margins improve as loan activity is still progressing strongly.

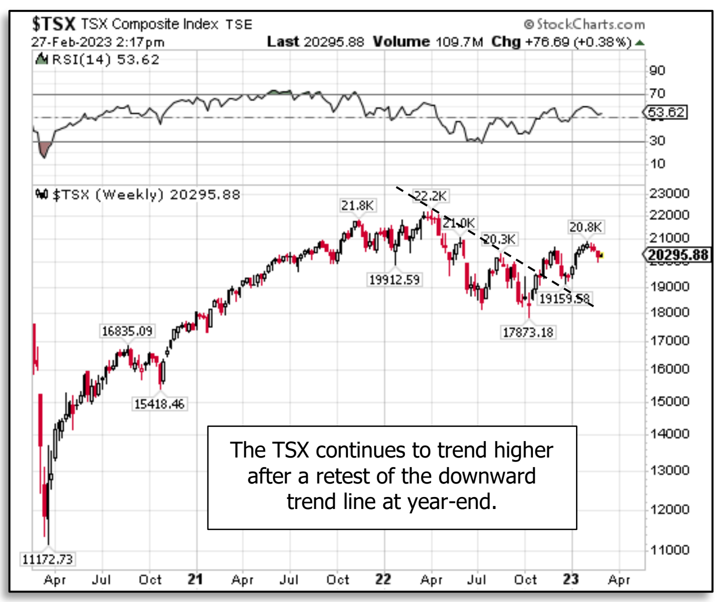

Chart 2

The Bank of Canada's decision on interest rates at the first meeting in 2023 was for a 25bps increase, was widely anticipated by the market signalling the end of aggressive interest rate hikes.

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