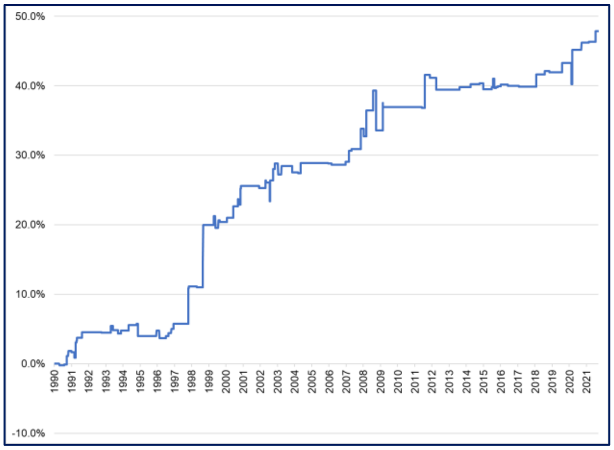
Monday, December 20, 2021

Til Tuesday

The Turnaround Tuesday (TT) model is likely to be in play at the close today. The model is: If stocks down Thursday and Friday, and down more than 1.5% on Monday, buy at the close on Monday and sell at the close on Tuesday. The model has a 64% win rate since 1990 with a sample size of 40 and an average return of 0.60%. Average daily returns overall are just +0.04%, so TT is a meaningful effect. Average returns are 17X normal and median returns are 4X normal. The weaker result for median returns is explained by very large up days on TT. These skew the average.

The results are not sensitive to the parameter you pick for the Monday move. Here, for example, is the return of the strategy: *go long SPX at Monday close if SPX down Thursday, down Friday, and down >0.5% Monday.*

Return of long SPX on TUE after (THU↓, FRI↓, MON <-0.5%)



Why is this result so consistent?

1. Media has a negativity bias and after Thursday, Friday down, the weekend media will be full of negative stories. This triggers a fear momentum trade on Monday. Longs bail, and speculators go short.
2. Momentum wanes by the end of Monday (people have had an entire day to sell). Tuesday is a short squeeze day.
3. Also note that any three down days in a row is somewhat rare in stocks. Stocks tend to go up. That's why permabears keep dying. Stocks have been in a relentless up trend since 1982. There have been some epic bear markets, of course, but if you look at a long series of data and study any particular patterns, almost everything you look at in stocks will have a strong upward bias due to the trend in the data. Still, TT is not a product of trend, it's a very strong result.

If you're new to AM/FX, email me if you would like more info about TT and why it works (I've been writing about it for 15+ years).

Exploring the alternative hypothesis

I have been mostly bearish stocks for the past month or so because I believed the Fed pivot was underpriced and the withdrawal of stimulus is the most important story for risky assets. But I like to keep an open mind. So … What is the bull case?

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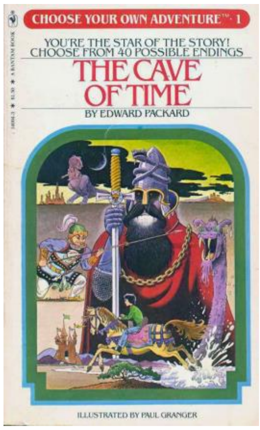
FX

Brent Donnelly

bdonnelly@spectramarkets.com
(212) 398-6230



If you go long ES, turn to page 88
If you stay flat, turn to page 114

Current Views

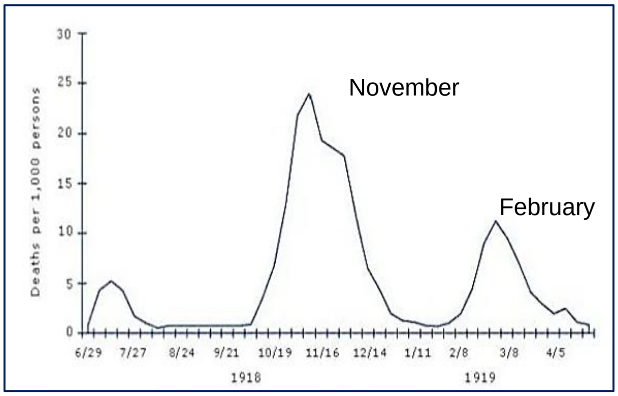
If ES is <4587 at 4 p.m. close, go long
Stop loss at entry minus 1.4% (a bit more than one day average range)

Reassessment triggers and take profit will be outlined tomorrow if the trade is entered and not stopped out by then

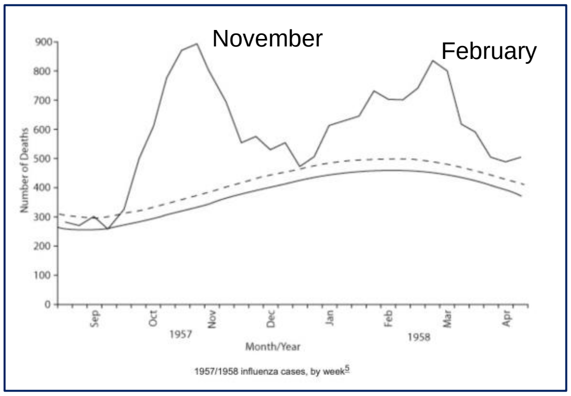
Short ETHUSD @ 4210
Stop loss 4902 / Take profit 3010
(From MacroTactical Crypto #4)

1. Micro: Turnaround Tuesday is a strong reason to go long stocks at today's close if SPX closes down today.
2. Omicron sell off unlikely to be sustained. COVID is following a similar seasonal pattern to the pandemics of 1918, 1957 and 1968 and it is highly likely that cases and deaths will peak in the next four to eight weeks. Markets are forward looking and can easily look through this despite the scary transmission rates, disappointing vaccine efficacy, and the harrowing endlessness of the pandemic. The overall economic impact of this wave is likely to be small and temporary even if the physical and mental health costs are enormous. Note that one unfortunate reality in these charts is that while October/January is the peak risk season for pandemics, there was a final spring wave of cases and deaths in both March 1919 and March 1958.

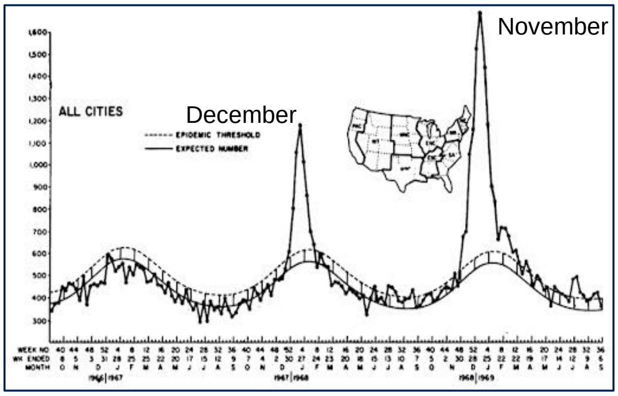
1918 deaths



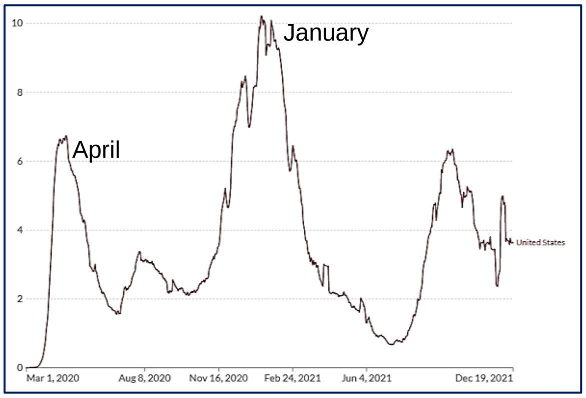
1957/1958 cases



1968 cases



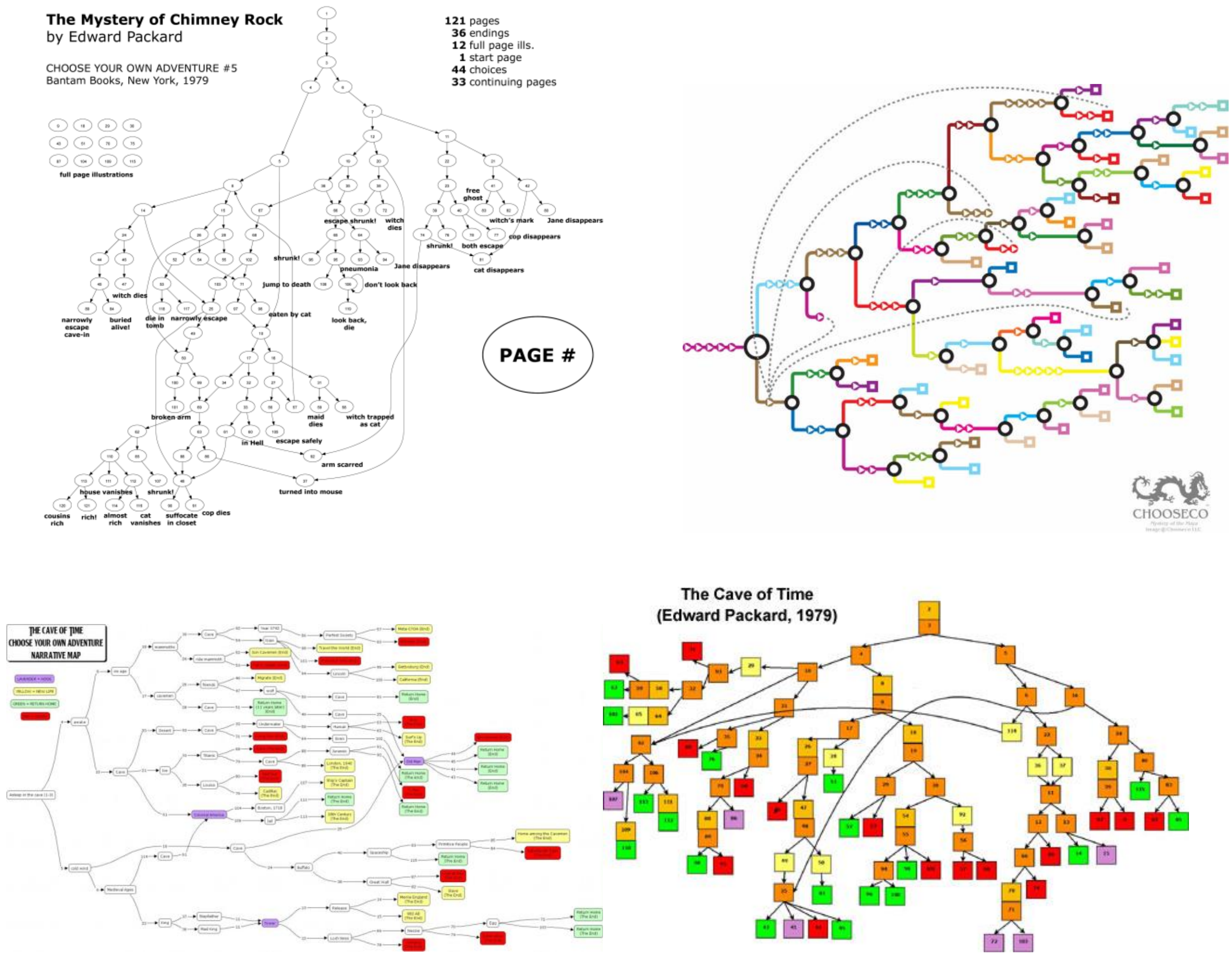
2020/2021 deaths



3. Peak Fed hawkishness and peak inflation may have arrived? Another punt of the BBB plan over the weekend pushes oil lower again overnight. Lower oil and fiscal drag should both exert some downward pull on inflation in 2022. The curve is pricing in so little Fed normalization, I'm not sure we're at peak Fed yet, but certainly it's a reasonable view, especially if you believe commodity prices have peaked and growth will slow in 2022.
4. Fed is still accommodative. The analogy to 2013 could be correct as that taper tantrum was a great opportunity to buy stocks. The Fed stayed extremely accommodative for years after that and stocks mostly rallied from 2013 to 2018. If real rates are set to remain low forever, stocks don't need to sell off that much. That is, if the Fed can never go to restrictive territory due to the demographic and debt problems facing the developed world, this rate hike cycle could be incredibly short and the terminal real rate might remain negative the whole time.

The bullish arguments for stocks are OK but not amazing to me. As we pivot out of the greatest monetary easing experiment the US has ever seen with inflation above 6%, the Fed put is lower than people think. The tech hype and momentum and retail inflows have been rabid. As such, I remain in "sell rallies" mode in stocks. BUT, I'm always nimble. **I see an opportunity for a tactical bull trade through the Christmas period.** Therefore, I added the bullish ES trade to the sidebar. Have a visually appealing day.

good luck ⇅ be nimble



Selected visualizations of plotlines from the Choose Your Own Adventure books.

https://samplereality.com/2009/11/11/a-history-of-choose-your-own-adventure-visualizations/

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