Trend & Cycle: The Long View – October 2022

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All values in U.S. dollars and priced as of market close on October 3, 2022 unless otherwise noted.

For Important Disclosures, see page 28.

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Wealth Management

Trend & Cycle: The Long View – October 2022

Long-term secular equity cycles

- The repetitive 17-year generational cycle remains positive and suggests that the secular bull market could last into the mid-2030s with potential, based on the prior two secular bull markets, for the S&P to move toward 14,000. Uptrends, however, are not linear and regularly have cyclical bear markets, similar to what is underway in 2022 with US equity markets testing important support.

The current 4-year market cycle

- The current 4-year cycle that began in 2020 peaked at the beginning of 2022 and remains in an established downtrend challenging the lower end of the 25+% uptrend channel that has been in place since the 2009 lows. The current decline is in line with the average <u>cyclical</u> bear market that developed during prior <u>secular</u> bull markets of the 1950s–60s, 1980s–90s and 2010s. Market cycles are influenced by two main drivers starting with central bank liquidity, which is currently being removed, and the outlook for economic and earnings growth, which is increasingly viewed to be at risk of weakening. Monthly momentum indicators, tracking 2- to 4-year cycles, remain negative for most markets and while working toward oversold levels, they have yet to bottom. This data suggests there is more volatile market behavior ahead before a sustained uptrend takes hold, which our 4-year cycle work suggests is not until well into 2023/early 2024.
- From a tactical trading perspective, most markets are again oversold short-term with potential to begin bottoming in line with favorable Q4 seasonality and with mid-term election years often supporting a rebound. Our expectation continues to be that equity markets will begin to stabilize/bottom near current levels similar to prior 4-year cycles that bottomed near rising 4-year/200-<u>week</u> moving averages. However, we believe that a decline below the recent lows and rising 200-week moving averages would raise the risk of further downside, with next support for the S&P near 3500 with additional risk toward 3200.

Global Markets – MSCI EAFE, MSCI Emerging Markets (EM), MSCI Europe, and Toronto TSX

- 2022 corrections continue testing next support with Europe showing early signs of improving relative performance while the TSX has pulled back into important support near 18-19K with early signs of stabilizing.

Trend & Cycle: The Long View – October 2022

INTEREST RATES

- **US 10-year yields** – Uptrend intact but overbought tactically and beginning to pause just under a key technical level near 4.0%.

CURRENCIES

- **US Dollar Index (DXY)** – Uptrend intact but also overbought with very early signs of pausing under a key technical level near 113.
- **Canadian dollar (CADUSD)** – Corrective trend continues with CADUSD testing support at 0.757, with next support at 0.7393.
- **British pound (BPBUSD)** – September's collapse is bouncing from near the 1985 lows just above par (100) with 1.14-1.18 resistance.

COMMODITIES

- **Commodity Index (CRY)** – Pullback from important resistance near the 62% retracement level continues.
- **Copper** broke below important support near 400, retraced 50% of the 2020–21 bull market and is attempting to bottom near 330.
- **WTI Oil** – Consolidation/pullback continues with WTI showing very early signs of bottoming tactically near 77.
- **Gold** is challenging important support near 1676 which needs to be recaptured to keep it from completing a longer-term top.

MARKET, SECTORS, and INDUSTRY GROUP CYCLES

- September's weakness undermined almost every market with most indices extending their bearish downtrends. The next few weeks are likely pivotal as the major US equity indices test important support near their rising 4-year/200-week moving averages as short-term trading indicators, tracking 2-4 week swings, are now deeply oversold and poised to bottom.
- We continue to expect a very volatile Q4 heading into the mid-term elections with a seasonal rebound likely, which could prove to be part of a broader cycle low developing for more offensive groups. Biotech, along with some of the former high P/E, high momentum stocks that led in 2020 and the early part of 2021, have stopped going lower which may be the very early stages of a bottom developing in some groups.

US equity generational cycles lasting roughly 16-18 years

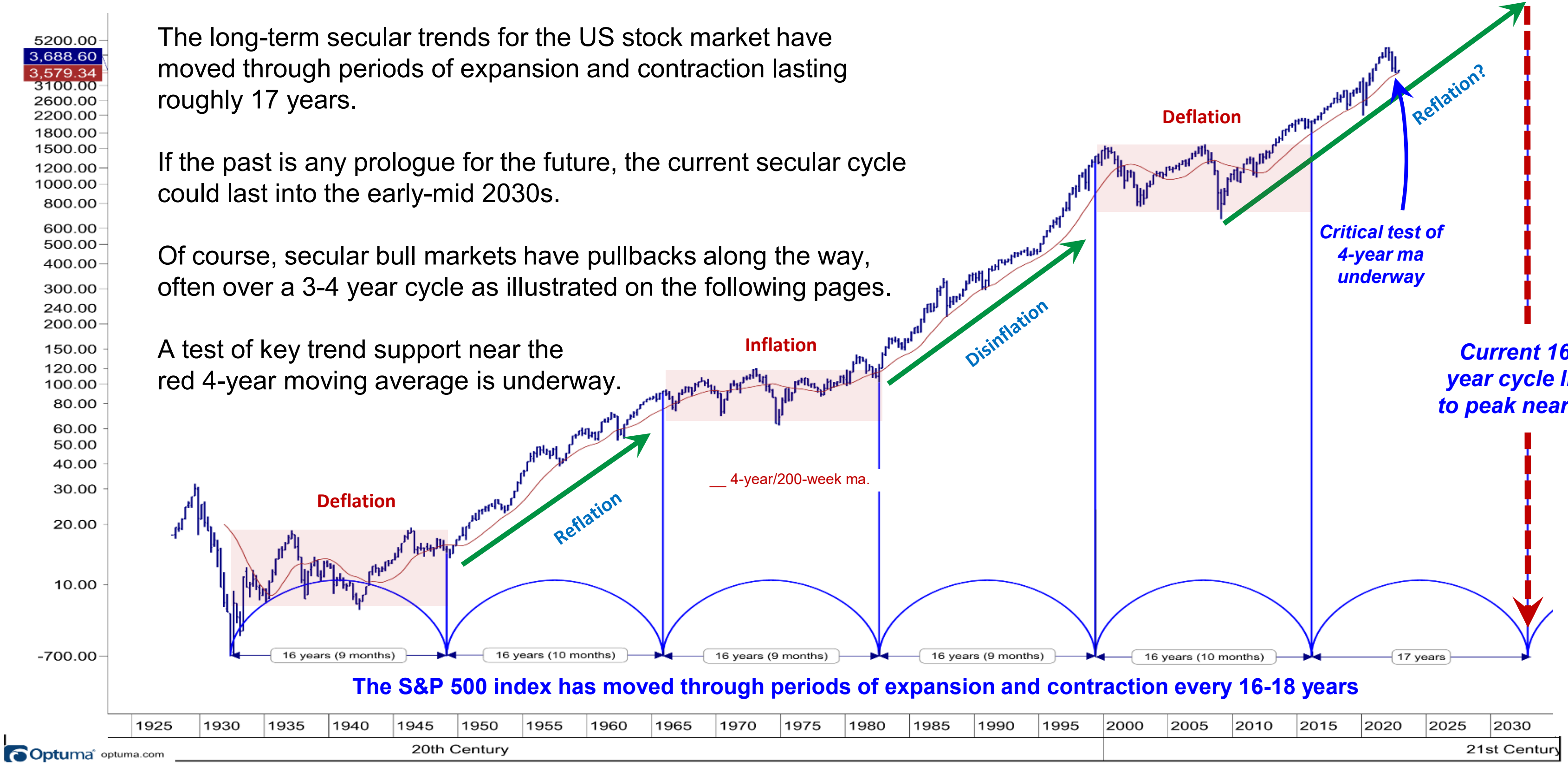
S&P 500 Index

The long-term secular trends for the US stock market have moved through periods of expansion and contraction lasting roughly 17 years.

If the past is any prologue for the future, the current secular cycle could last into the early-mid 2030s.

Of course, secular bull markets have pullbacks along the way, often over a 3-4 year cycle as illustrated on the following pages.

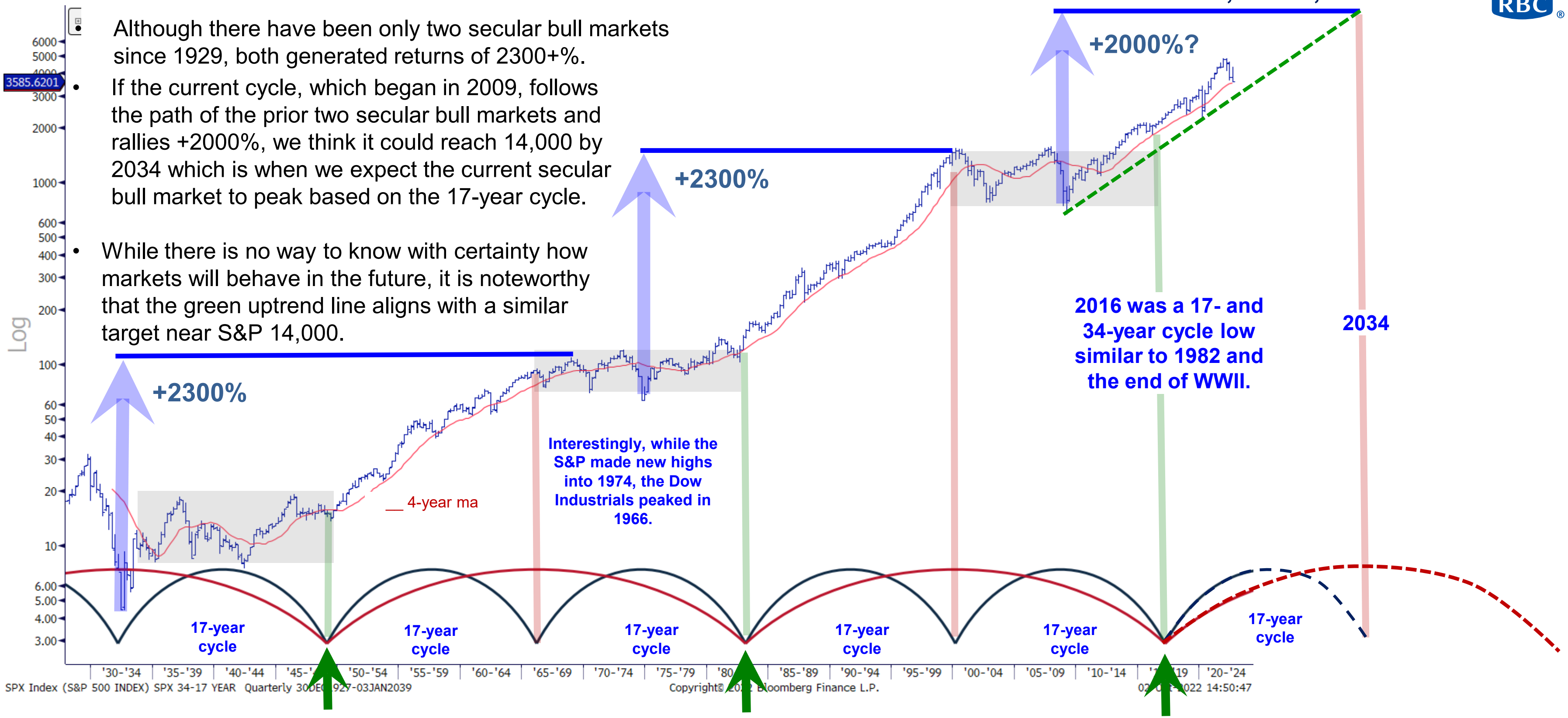
A test of key trend support near the red 4-year moving average is underway.



Source: RBC Wealth Management, Bloomberg, Optuma

S&P 500 – Could the S&P rally to 14,000?

- Although there have been only two secular bull markets since 1929, both generated returns of 2300+%.
- If the current cycle, which began in 2009, follows the path of the prior two secular bull markets and rallies +2000%, we think it could reach 14,000 by 2034 which is when we expect the current secular bull market to peak based on the 17-year cycle.
- While there is no way to know with certainty how markets will behave in the future, it is noteworthy that the green uptrend line aligns with a similar target near S&P 14,000.



Source: RBC Wealth Management, Bloomberg, Optuma

S&P 500 and a repetitive 4-year cycle – 2024 likely the next up cycle

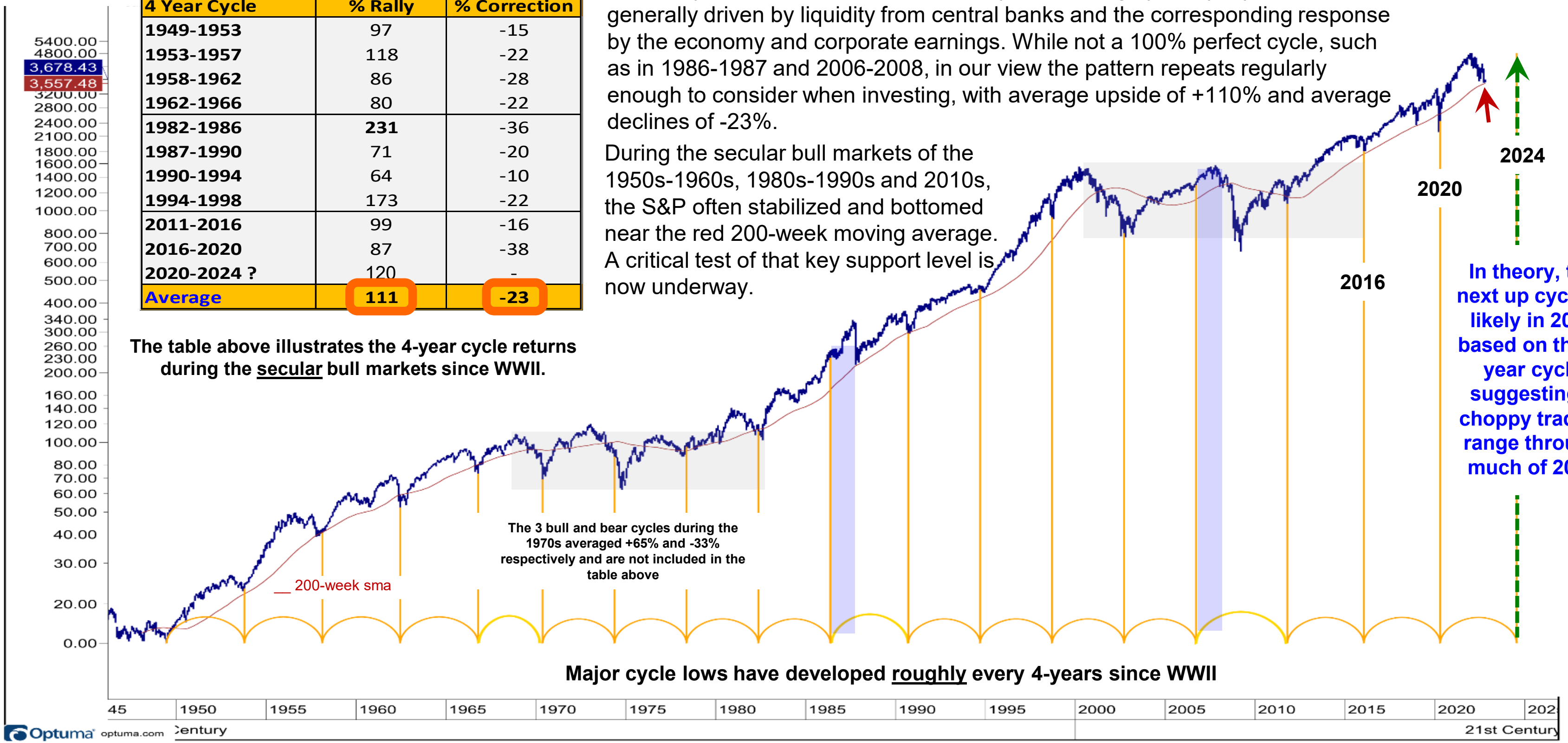
4 Year Cycle	% Rally	% Correction
1949-1953	97	-15
1953-1957	118	-22
1958-1962	86	-28
1962-1966	80	-22
1982-1986	**231**	-36
1987-1990	71	-20
1990-1994	64	-10
1994-1998	173	-22
2011-2016	99	-16
2016-2020	87	-38
2020-2024 ?	120	-
Average	**111**	**-23**

The table above illustrates the 4-year cycle returns during the secular bull markets since WWII.

US equity markets have established a cycle low roughly every 4 years, generally driven by liquidity from central banks and the corresponding response by the economy and corporate earnings. While not a 100% perfect cycle, such as in 1986-1987 and 2006-2008, in our view the pattern repeats regularly enough to consider when investing, with average upside of +110% and average declines of -23%.

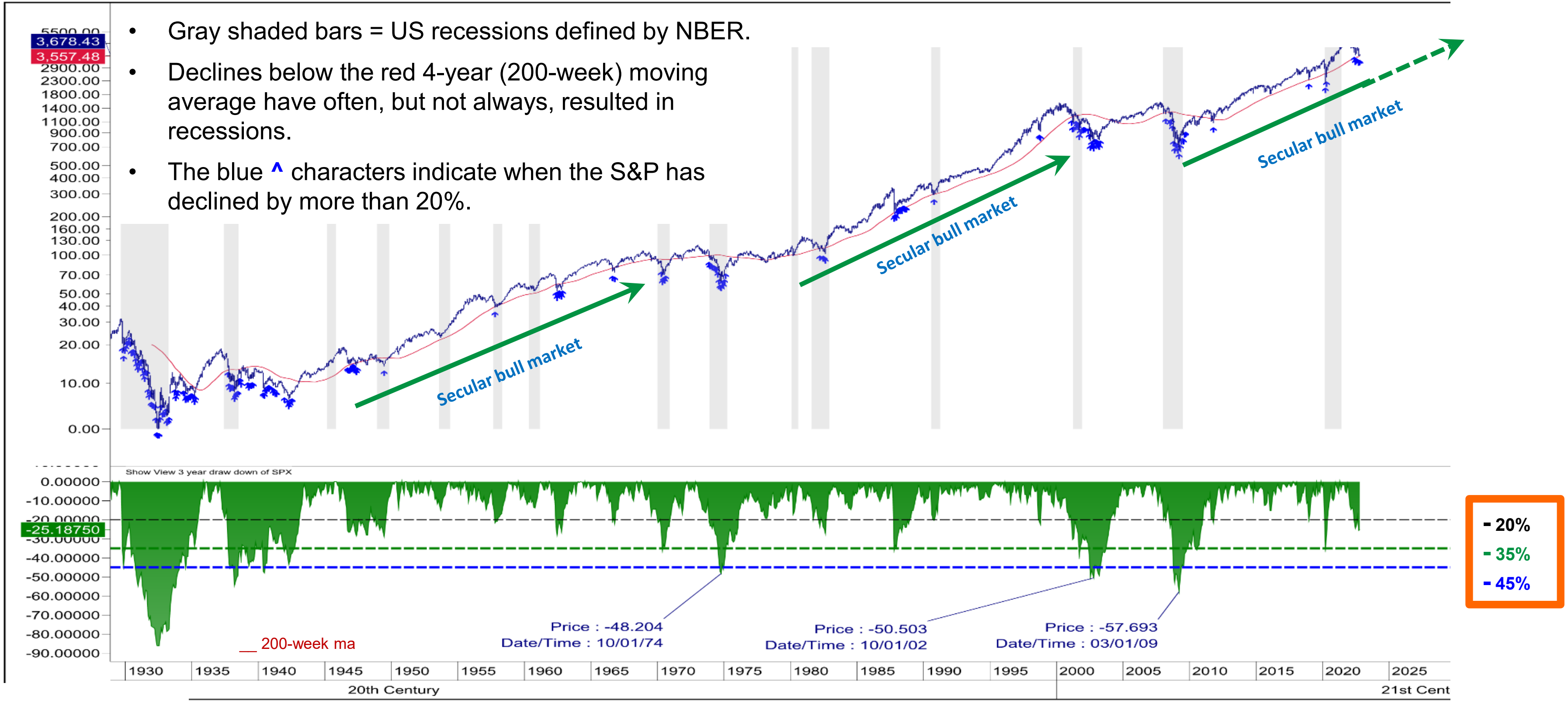
During the secular bull markets of the 1950s-1960s, 1980s-1990s and 2010s, the S&P often stabilized and bottomed near the red 200-week moving average. A critical test of that key support level is now underway.

In theory, the next up cycle is likely in 2024 based on the 4-year cycle suggesting a choppy trading range through much of 2023



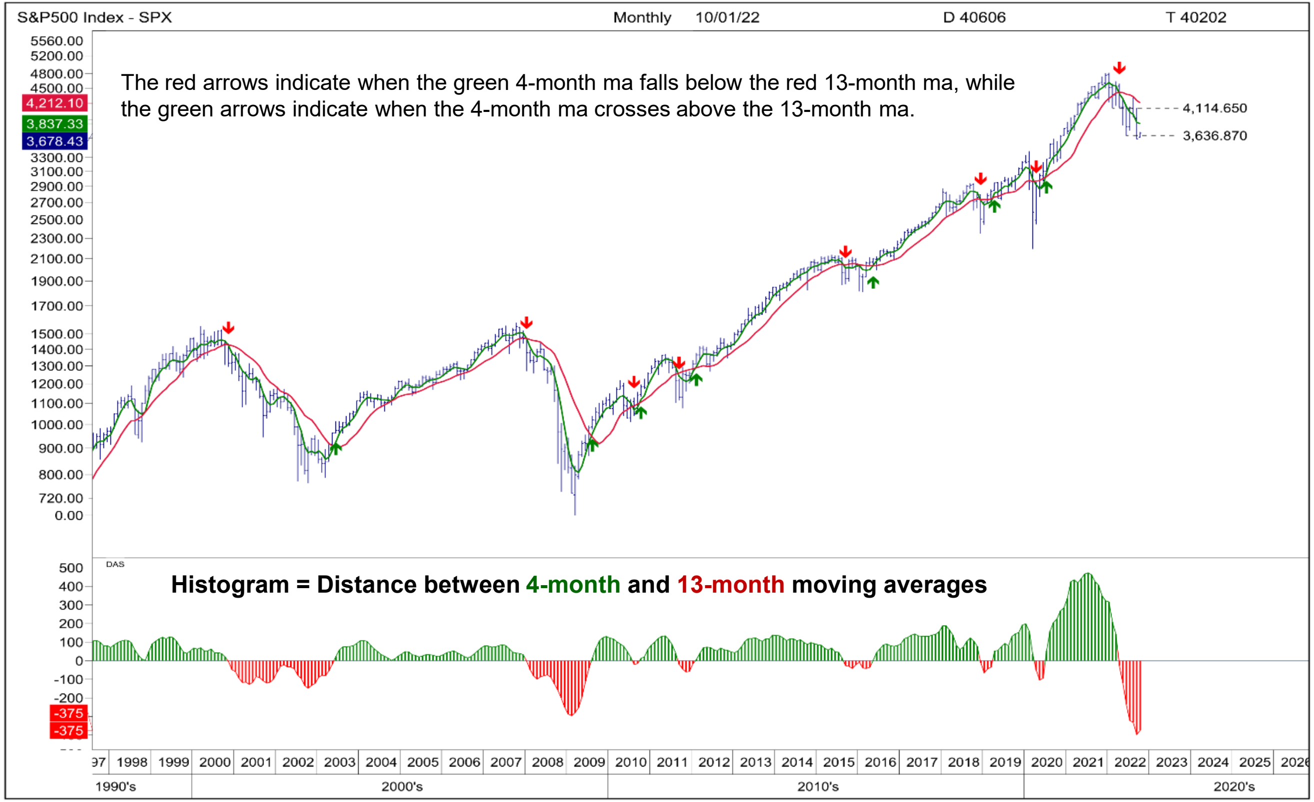
Source: RBC Wealth Management, Bloomberg, Optuma

S&P 500 – 1940-2022 with drawdowns from 3-year highs



Source: RBC Wealth Management, Bloomberg, Optuma

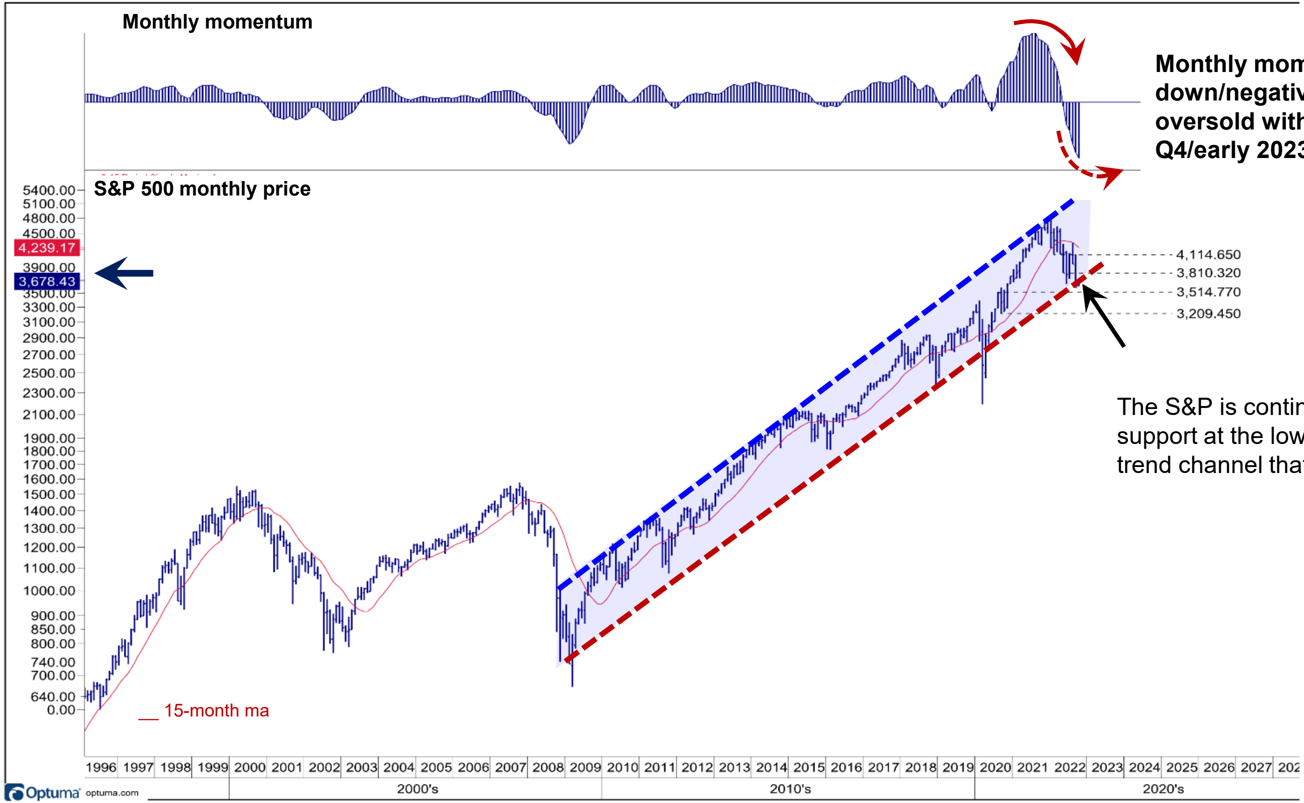
S&P 500 Index – Monthly with 4- and 13-month moving averages



- The shorter-term trend for the S&P, represented by the green 4-month moving average (ma), remains below the longer-term trend, represented by the red 13-month ma, confirming an ongoing downtrend.
- Support is near 3600, followed by 3500 then 3200 with 4100-4200 ongoing resistance.
- The histogram in the bottom panel is green when the 4-month ma is above the 13-month ma, and red when the 4-month ma is below the 13-month ma. This indicator continues to confirm that the S&P is in a downtrend and would need to flip green to signal that the trend is turning positive again.
- This indicator is showing early signs of becoming oversold with potential to bottom in the coming months.

Source: RBC Wealth Management, Bloomberg, Optuma

S&P 500 Index

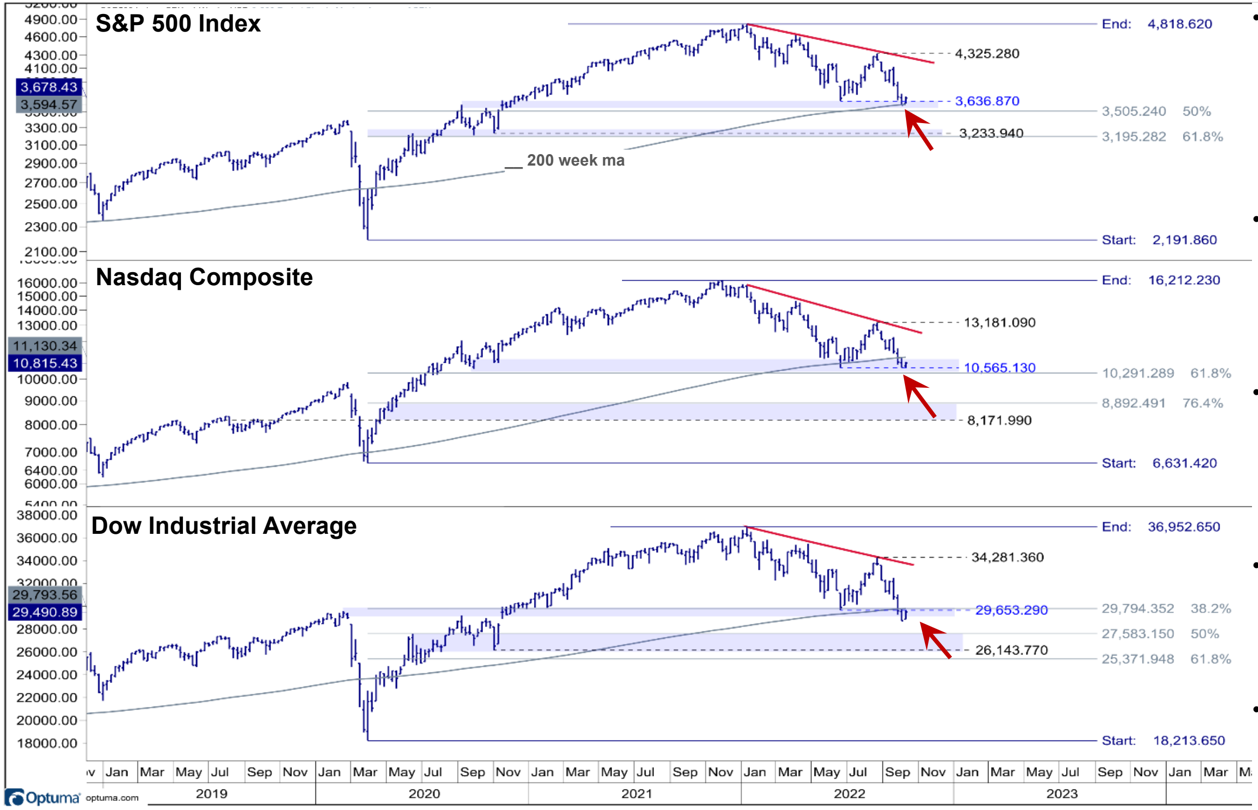


Monthly momentum remains down/negative but is becoming oversold with potential to bottom in Q4/early 2023.

The S&P is continuing to stress test important support at the lower end of a roughly 25% wide trend channel that began in 2009.

Source: RBC Wealth Management, Bloomberg, Optuma

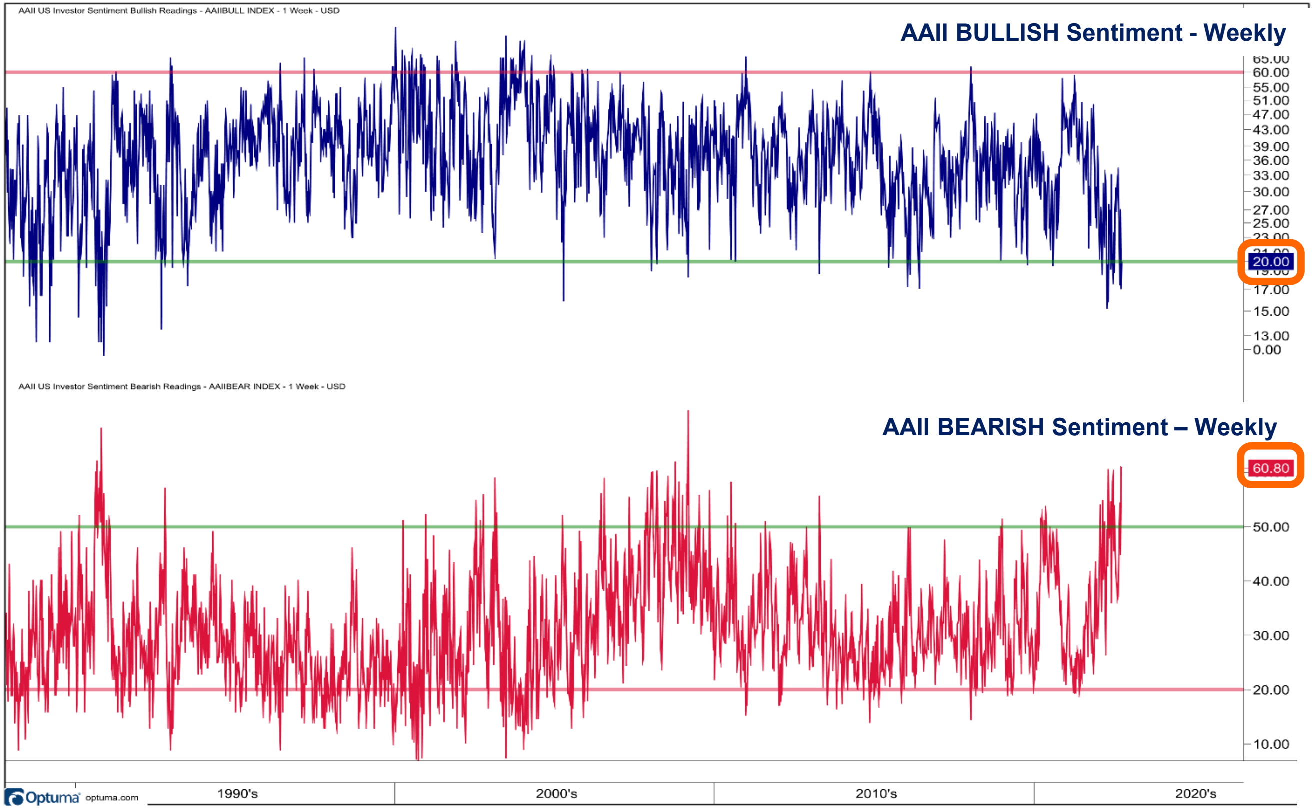
S&P, Nasdaq: Critical test of the June low underway near 200-week ma's. Dow breaks support.



Source: RBC Wealth Management, Bloomberg, Optuma

- September's weakness has seen US equity markets challenge important support between their summer lows and rising 200-week moving averages. While the S&P and Nasdaq are testing those ranges, the Dow has slipped below both those key levels.
- As we have discussed in previous notes, a successful test and rebound from near the rising 200-week ma and summer lows would be an encouraging signal that a cycle low may be developing.
- A growing list of technical indicators (DeMark, momentum, positioning) are signalling oversold conditions heading into early October suggesting a rally will likely develop in early-mid October.
- While a bounce appears likely, it is too early technically to conclude that either a cycle low is completing or that the 2022 bear market downtrend is ending.
- Should equity markets break below their summer lows and rising 200-week mas, next support is at S&P 3505 then 3200, Nasdaq 10,291 then 8,892, Dow 27,583 then 26,143.

AAII US Investor Bullish and Bearish Sentiment (contrarian indicators)



Source: RBC Wealth Management, Bloomberg, Optuma

- AAII Bullish Sentiment is again falling toward extremes not seen since the 1990s.

…while…

- …AAII Bearish Sentiment has surged back toward pessimism not seen since the 2008 Financial Crisis.
- These sentiment indicators are viewed to be contrarian, with current levels consistent with levels that often support a market rebound.

MSCI EAFE – Monthly with relative performance vs the S&P 500

- Monthly momentum, tracking 2-4 year swings, remains negative and has yet to bottom as the MSCI Europe, Asia and Far East Index (EAFE) continue to correct from a broad resistance band (highlighted in red).
- EAFE has broken below two key support levels between the 50-62% retracement of the 2020-20221 rebound and is now testing next support near 1600.
- Short-term, an oversold rally appears likes in October.
- EAFE's relative performance versus the S&P 500 remains in a longer-term downtrend with no meaningful evidence of reversing to the upside, which is needed to support overweighting EAFE.

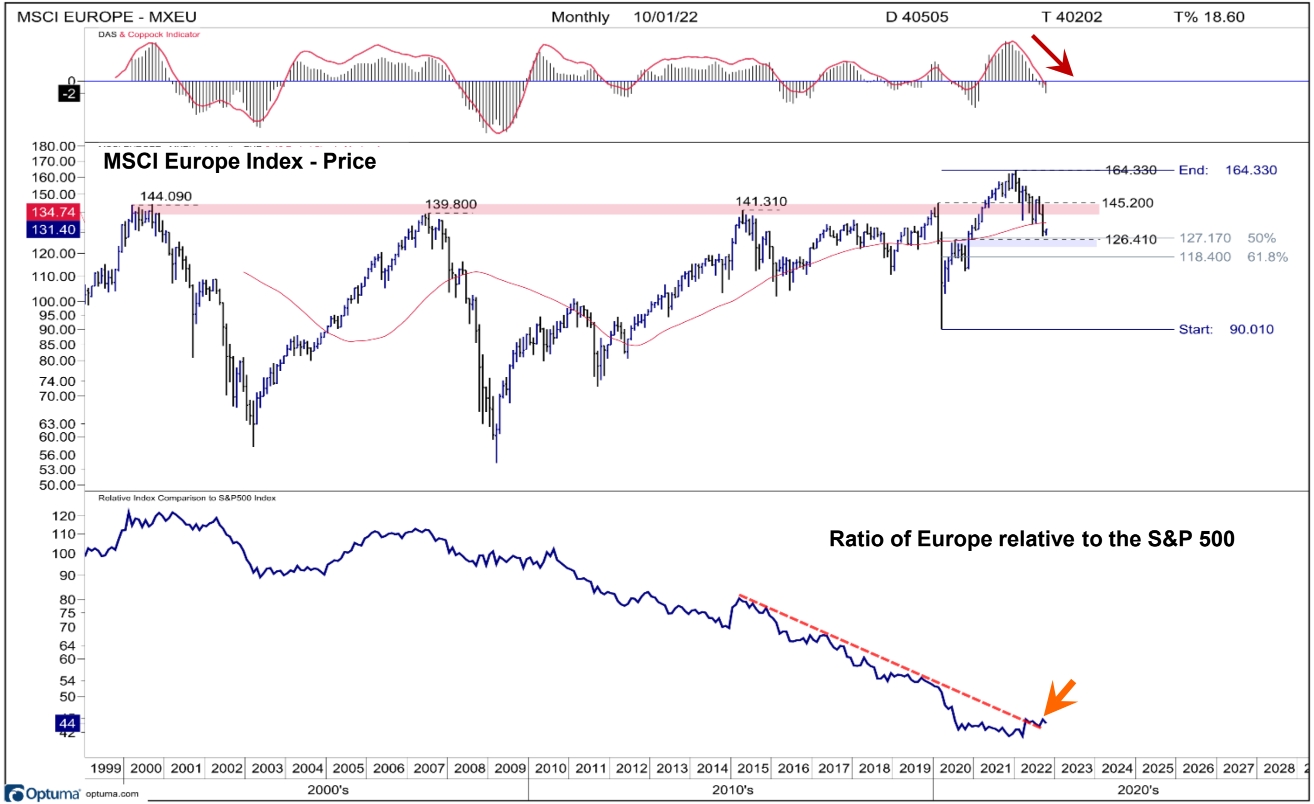
Source: RBC Wealth Management, Bloomberg, Optuma

MSCI Emerging Market Index and relative performance vs S&P 500

Source: RBC Wealth Management, Bloomberg, Optuma

- Monthly momentum is becoming oversold but has yet to bottom and turn up.
- After peaking in early 2021, the MSCI EM has yet to show meaningful evidence of bottoming as it falls below the 50%, 62% and 76% retracement levels of the 2020-2021.
- Relative performance versus the S&P 500 remains in a downtrend and would need to reverse above the red downtrend line to signal a longer-term trend shift favoring EM.

MSCI EUROPE – Monthly with relative performance vs S&P 500



Source: RBC Wealth Management, Bloomberg, Optuma

- MSCI Europe had fallen below important support at 145 coinciding with the upper end of a 20-year trading range in June.
- The MSFI Europe index is now testing next support at its 50% retracement level near 126 but it is too early to conclude a meaningful bottom is developing yet.
- Short-term an oversold rebound appears likely in October.
- MSCI Europe has improved short-term relative to the S&P 500 and is showing very early signs of reversing its multi-year downtrend versus the S&P 500.

S&P/TSX Composite – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

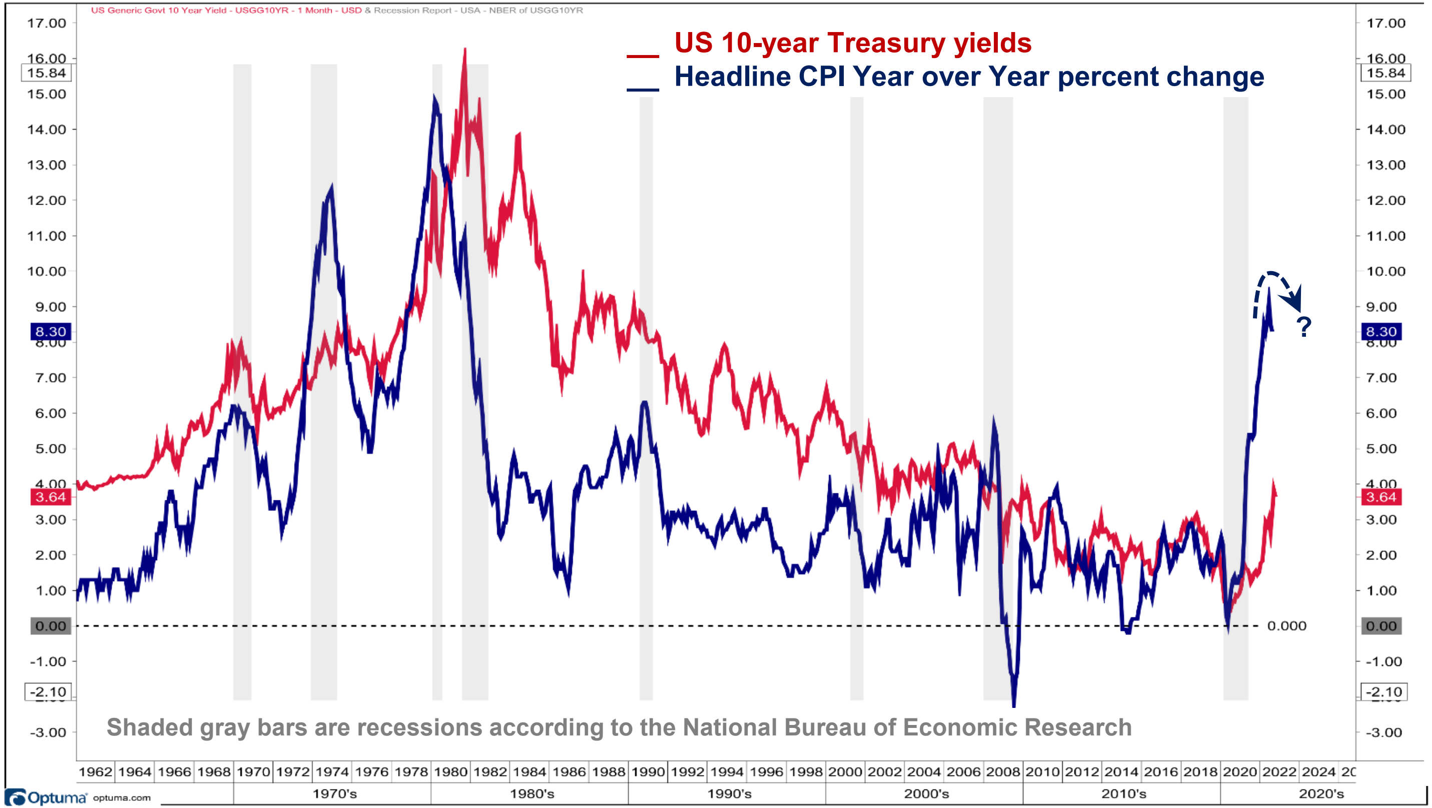
- Monthly cycle momentum remains negative for the TSX as the composite pulls back to test its long-term uptrend support near 18-19K with early signs of stabilizing.

- Relative performance versus the S&P 500 is showing <u>very</u> early signs of improving.

US 10-Year Yield – Long-term

Source: RBC Wealth Management, Bloomberg, Optuma

US 10-Year Yield (red) and CPI Inflation YoY (blue)



- This chart illustrates the US 10-Year Yield (red) along with the year-over-year percentage change in CPI (blue) and with recessions according to the NBER (gray bars).
- Although the sample set is small, year-over-year moves in CPI have generally led to a recession.

Source: RBC Wealth Management, Bloomberg, Optuma, Bureau of Labor Statistics, National Bureau of Economic Research

US Dollar DXY Index – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

- The US Dollar index (DXY) remains a major headwind for risk assets as it continues to trend higher after breaking out above the prior cycle highs in 2016 and 2020 near 103-104.
- A 162% Fibonacci extension of the 2016-2020 trading range is at 113, which is near to where the US dollar index is showing early signs of pausing.
- Above 113 next resistance is at 120-121. Support remains near 103-104.

Canadian Dollar / US Dollar – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

- Monthly momentum remains negative but is moving toward oversold territory as…
- …the Canadian dollar continues to correct from resistance near 0.83–0.84 in June 2021, breaking 0.772 support to challenge its next important support at 0.7571 at the 50% retracement level.
- Next support below 0.7571 is 0.7451 to 0.74 near the 62% retracement level.
- While the CAD-USD is becoming oversold, it is still premature to conclude a longer-term low is in place. Our expectation is for a more durable bottom to develop in Q4/early Q1.

British Pound – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

- The British pound has collapsed back to the lows seen in 1985.
- Although the pound is oversold short-term and beginning to bounce there is insufficient technical evidence to state the final lows are in.
- There is no obvious next support level below 1.05 with par (100) the next likely level in play should the pound fall below 105.
- 1.14-1.18 remains resistance.

Thomson Reuters/Jefferies CRB Commodity Index – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

- Monthly cycle momentum has peaked as the CRB Commodity Index continues to show evidence of turning as the CRB stalls at an important resistance band near the 62% retracement of the 2008-2020 decline at 331.
- This chart suggests the commodity cycle that began in 2020 is likely in the early stages of stalling, with a broad trading range likely to follow well into 2023.
- The CRB index has broken first support at 287 and is now stress testing next support at 266 with 241 next support.
- **Note:** Relative performance versus the S&P has reversed a downtrend that began in 2008.

Copper Futures – Monthly

- Monthly momentum continues to decline but is moving toward oversold levels with potential to bottom in late Q4/early Q1.
- Copper is now testing next support near 332 coinciding with the 2018 highs with early signs of stabilizing short-term.
- The ratio of Copper vs Gold in the bottom panel has turned down under its 2018 cycle highs and remains weak.

Source: RBC Wealth Management, Bloomberg, Optuma

WTI Oil Future – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

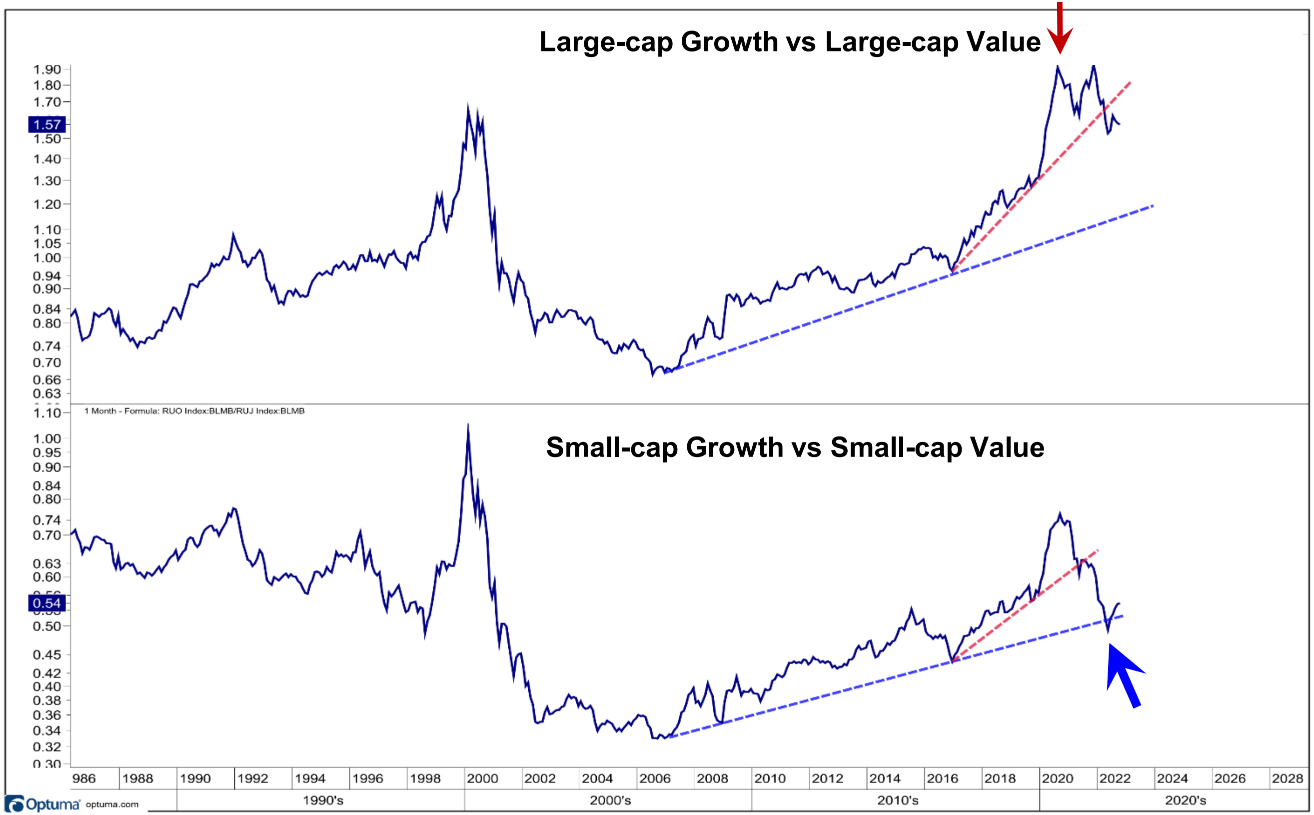
- WTI Oil peaked at 130 in March 2022 and then at 123 in May and has been in a correction since testing next support in the upper 70s.
- Tactical indicators, tracking 2-4+ month moves, are already oversold and beginning to bottom suggesting Oil is likely to be establishing a seasonal low.
- Note: For reference, we are using 10 to be the low end of WTI's long-term trading range for the Fibonacci retracements rather than the temporary spike into negative territory at -40.

Commodities – Gold – Monthly

Source: RBC Wealth Management, Bloomberg, Optuma

- Gold broke below important support near 1670 near its rising 4-year/200-week ma in September but is showing early signs of recovering that key level at the start of October.
- A break below 1670 support raises the likelihood gold is again completing a longer-term top similar to what developed in 2011-2012.
- Next major support below 1670 is at 1375.

Growth vs Value – Monthly



Source: RBC Wealth Management, Bloomberg, Optuma

- Large-cap Growth versus Value has peaked and broken the 2016-2021 uptrend.
- Interestingly, small-cap Growth versus Value has meaningfully diverged from large caps as it has broken the 2016-2021 uptrend and is now challenging its long-term uptrend that began in 2006 with very early signs of stabilizing in Q3 heading into Q4.
- While an oversold tactical rebound in growth appears likely in Q4, it is unlikely the beginning of another multi-year advance.

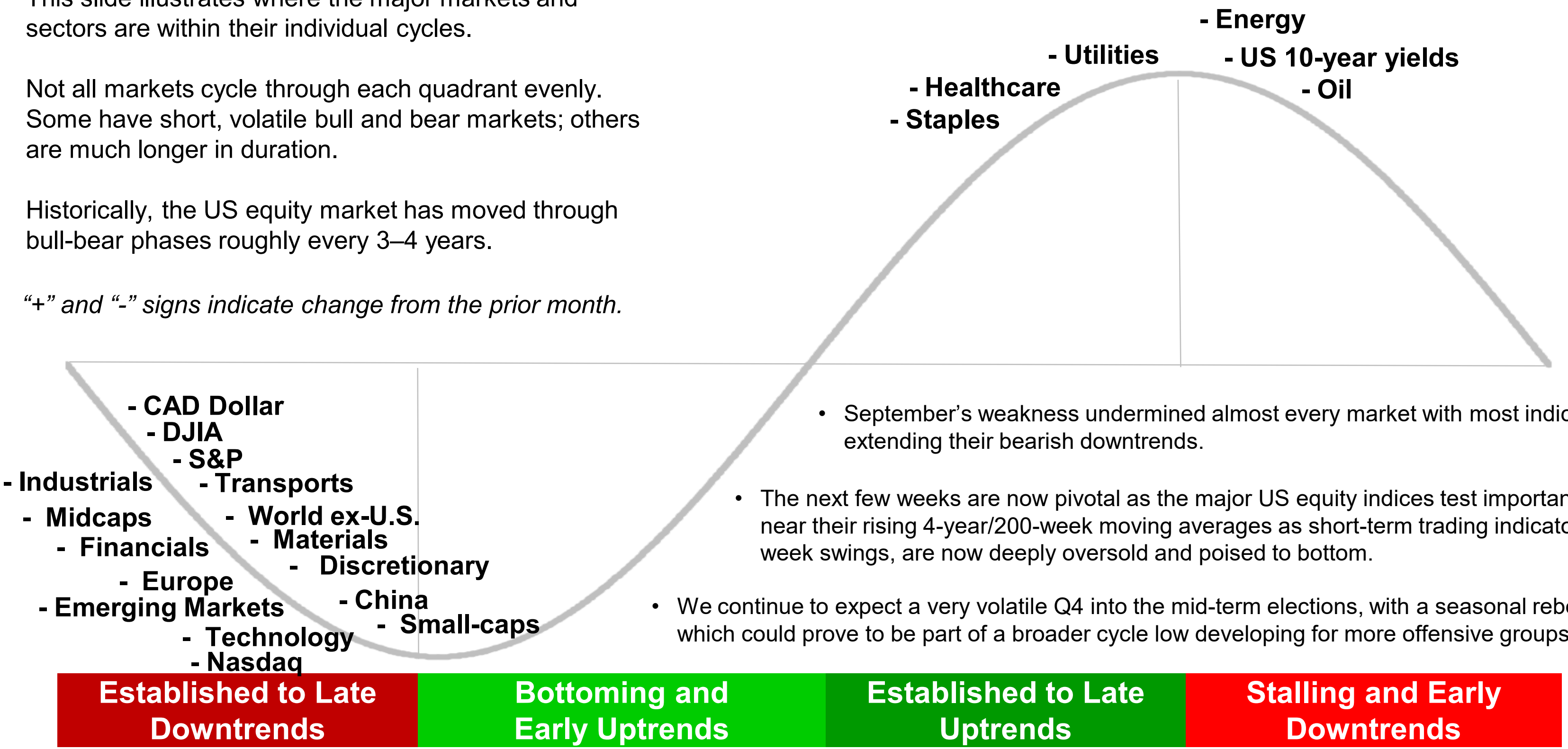
Major markets and S&P sector cycles

This slide illustrates where the major markets and sectors are within their individual cycles.

Not all markets cycle through each quadrant evenly. Some have short, volatile bull and bear markets; others are much longer in duration.

Historically, the US equity market has moved through bull-bear phases roughly every 3–4 years.

“+” and “-” signs indicate change from the prior month.



- September’s weakness undermined almost every market with most indices extending their bearish downtrends.
- The next few weeks are now pivotal as the major US equity indices test important support at or near their rising 4-year/200-week moving averages as short-term trading indicators, tracking 2-4 week swings, are now deeply oversold and poised to bottom.
- We continue to expect a very volatile Q4 into the mid-term elections, with a seasonal rebound likely which could prove to be part of a broader cycle low developing for more offensive groups.

Source: RBC Wealth Management, Bloomberg, Optuma

Industry group cycles

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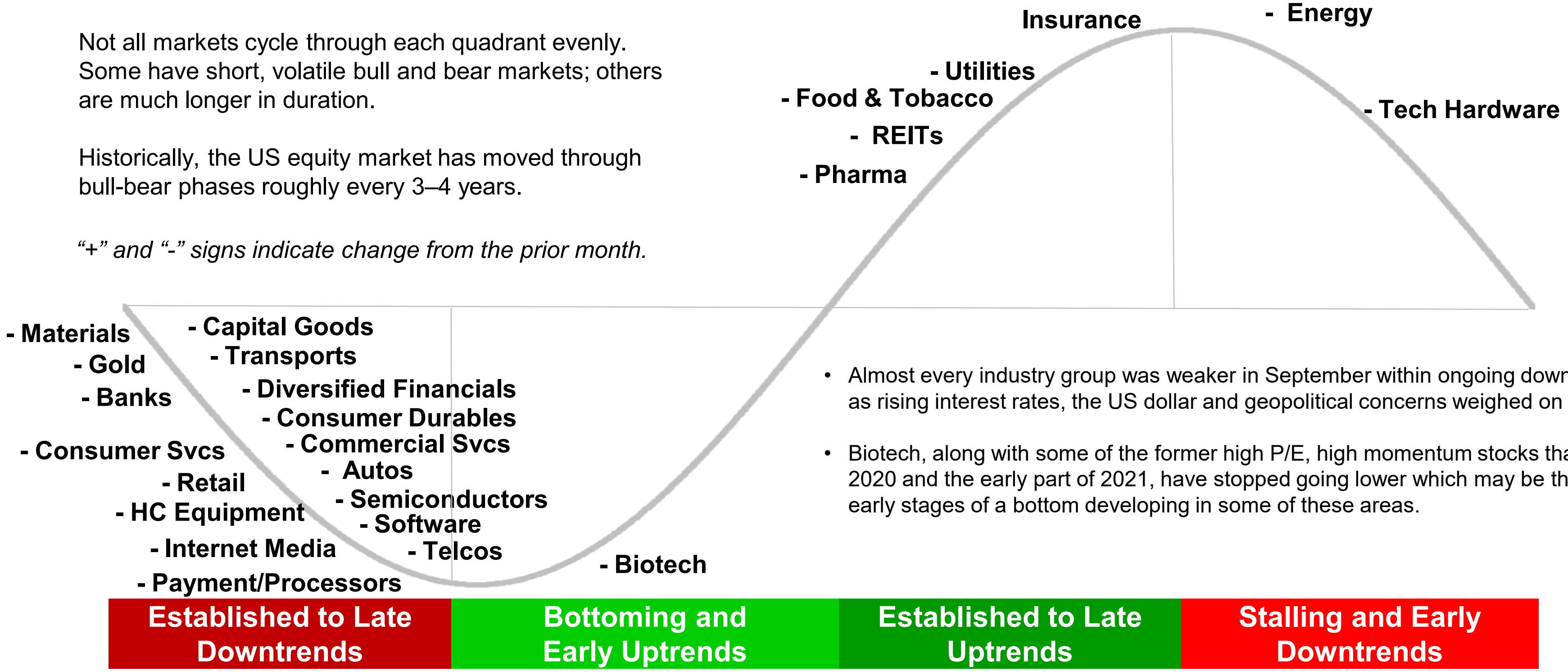

- Almost every industry group was weaker in September within ongoing downtrends as rising interest rates, the US dollar and geopolitical concerns weighed on markets.
- Biotech, along with some of the former high P/E, high momentum stocks that led in 2020 and the early part of 2021, have stopped going lower which may be the very early stages of a bottom developing in some of these areas.

Source: RBC Wealth Management, Bloomberg, Optuma

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Sell [Underperform]	52	3.52	5	9.62

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