MV Capital Management Midweek Market Commentary

Catalysts

February 22, 2013

For several weeks now – really since the torrid pace of the January rally slowed to a more measured gait in February – market observers have spoken of the absence of a catalyst to move things more definitively in one direction or another. This week we got, if not a full-throated catalyst, at least a handful of reasons for investors to back off from recent highs and once again hold the S&P 500 at bay below the 1527 level it had finally surpassed this past Tuesday. The question is whether these past few days are indicative of a near term defensive crouch or whether the market will shortly resume its winning ways.

So what brought about the dour spirits? First of all, the release of the latest Fed minutes on Wednesday revealed a higher than average level of unease among policymakers about the potential ill effects of the QE3 program that has been going on since last fall. This program has been dubbed "QE4ever" by the market wags, and so anything that hints at taking the patient off the IV drip of easy money is bound to create some gloom. To add to the down mood a handful of signals came in showing Europe's immediate economic prospects looking somewhat grimmer than expected. The latest GDP numbers show the Eurozone as a whole heading towards a 0.3% contraction this year as opposed to the 0.1% growth the European Commission had predicted at the end of 2012.

There's little doubt that Fed stimulus and stability in Europe are key drivers for continued growth in equity indexes. However this week's news didn't seem to pack the kind of punch that could catalyze an extended downturn. After all there was no announcement that the Fed actually plans to curtail QE3 any time soon. The ECB's "whatever it takes" stance is as much intact today as it was last week. More likely the mini-downturn (and the corresponding spike of nearly 20% in the VIX over Wednesday and Thursday) reflects the kind of tentativeness about which we have spoken in previous posts when indexes flirt with long term resistance levels. The S&P 500 is still well above its 100 and 200 day moving averages and is trading generally higher as the week draws to a close.

One thing to keep an eye on as February draws to a close is whether the latest Kabuki matinee in Washington spills over into market sentiment. The unfortunately named sequestration involving deep spending cuts across vast swaths of the budget appears likely to come into effect shortly. Lawmakers on both sides of the partisan divide appear to be far away from anything remotely resembling a deal. That doesn't seem to be making much of an impression on the markets, but the fact is that if all the cuts go ahead as planned there will be an economic impact. Presumably investors, having seen this elaborate pantomime play out over and over again, assume that something will take place to prevent – or at least forestall – a worst case outcome. We will see how the sentiment tracks as the hour approaches.

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