The US Equity Market: So Far So Good, But…

By Didier Darcet

TrackMacro ™ is a software tool providing equity risk signals in 40 countries

Download TrackMacro for PC from the company website
Download TrackMacro for iPad from the Apple Store

In March 2017, TrackMacro artificial intelligence program is telling us that 40 countries out of 40 are in a “Risk On” mode for equity markets. The whole world is equity friendly and has been so for seven months in a row. But can we deepen the analysis to understand how the system thinks?

TrackMacro combines seven macro-economic rules tracking major economic observables in a systematic manner. The rules and the combinations are identical for 40 markets.

The system has been very accurate in spotting country equity risks during the last 18 months of its out-of-sample trial period.

In 2016, investors switching equity exposures to government bond holdings when advised by TrackMacro would have doubled their return in a global portfolio. They would have contained as well their maximum drawdown to 3% to 4% vs. 18% to 20% for the benchmark, which is the primary objective of the system.

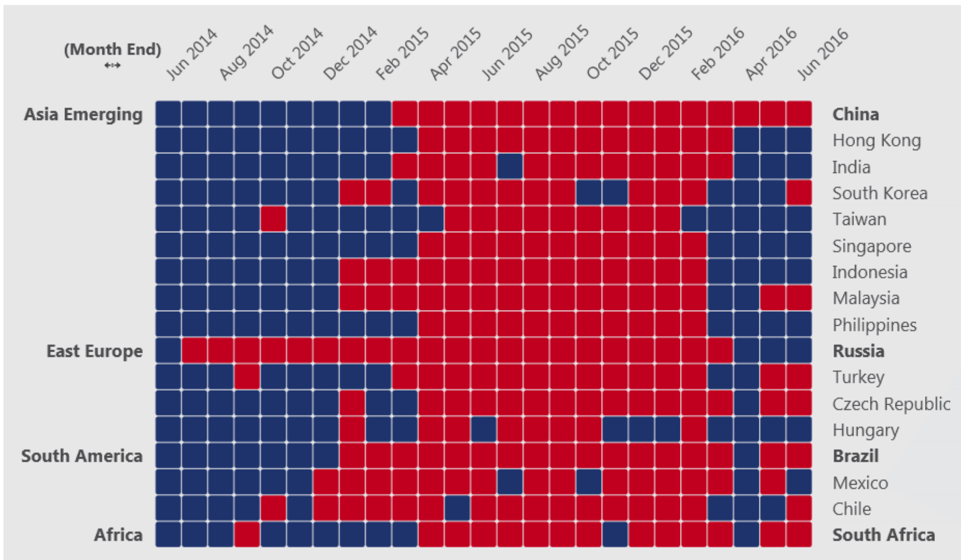
The worst markets are the best opportunities for the program. No surprise about that: TrackMacro is a risk system, not a valuation system.

Here are the model outperformances in such markets in 2016, in local currencies:

- **Japan**: +21.6% vs. +0.2%
- **Italy**: +19.1% vs. -6.6%
- **China**: +6.4% vs. -10.5%

Between mid-2015 and mid-206, the system identified a series of deflationary shocks, spreading from local markets to the entire world. At first, the collapse of oil prices affected Russia, then Norway, then Mexico and Chile. A few months later many countries in Asia turned red on the back of a shortage of USD liquidity and slowing activity.

Fig1. “Risk On” (in blue) and “Risk Off” (in red) signals by TrackMacro



Ten to thirteen months following the initial risk signal in Russia, developed economies started to be affected by a deterioration of world trade. TrackMacro, who knows nothing about Brexit or US Presidential election, had made its own interpretation based on macro factors and flows.

Today the US market is back to positive territory. Even though the system does not make any forecast longer than one month, TrackMacro users can make their own interpretation of the signal at longer time scales. US equities are today only supported by a growing world trade. The other macro rules are neutral of negative: the USD is not cheap any more, neither the equity markets, the crossing of growth and inflation is inconclusive and the wealth effect of asset prices is over. If the world trade weakens, the US will turn red.

So far so good, but the system’s preference for equities is fragile.