# Trend & Cycle Roadmap

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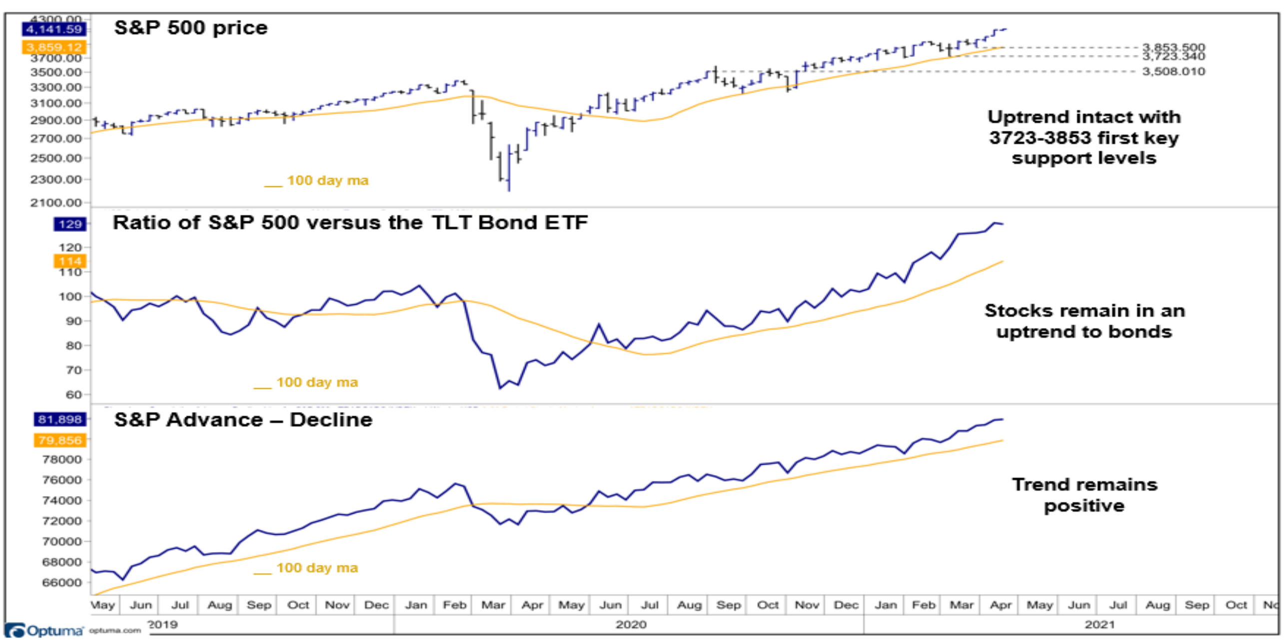
## A look at equity trends, stalling bond yields, and small-cap growth lagging large-cap growth

After the S&P 500 surge last week, we don't think it's surprising investors are asking us whether the market is overbought and ready to start a correction. In the short term, trading indicators tracking two- to four-week swings have moved into overbought levels suggesting to us a pullback is likely toward the end of the week or early next week. Beyond some near-term volatility, the more important question is whether the bigger underlying trend is showing evidence of reversing and turning negative.

To help answer that question, we use the three panel chart below to look at the technical behavior of the market from three different angles. First we look at the current trend of the S&P 500 (top panel), second we see if the relative performance trend versus bonds is changing (center panel), and third we review the advance-decline to see if most stocks are advancing with the market trend or not (bottom panel). The yellow 100-day moving average in each panel serves as a simple but effective proxy for the underlying trend.

So far, all three trends remain positive, and while there is always a concern a correction is pending, we think there is insufficient technical evidence to support turning bearish yet. As Peter Lynch, the famous 1980s portfolio manager, once said, "More people have lost money waiting for corrections and anticipating corrections than in the actual corrections." Until these trends change, we recommend staying the course!




Source: RBC Wealth Management, Bloomberg, Optuma

RBC Capital Markets, LLC/Portfolio Advisory Group
All values in U.S. dollars and priced as of April 13, 2021 unless otherwise noted
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**Revisiting the pause in interest rates** - We are revisiting the interest rate chart again today given the technical setup heading into this week's broadly anticipated Consumer Price Index (CPI) report that was released yesterday (April 13) and the subsequent reaction by the bond market.

A high CPI reading was widely anticipated with many investors expecting a surge in rates. As we noted here the past two weeks, U.S. 10-year rates have pushed into an important overhead band beginning at the 50% retracement level of the 2018–2020 decline. In addition, the weekly Relative Strength Index (RSI) momentum indicator in the bottom panel has moved from oversold levels in March 2020 to overbought levels in April 2021 and is showing increasing evidence of peaking and turning down.

Does this mean that the bigger uptrend is over and rates are headed meaningfully lower? No, we believe that conclusion is premature. However, as we noted here the past two weeks, uptrends are rarely linear and tend to follow a stair-step pattern, so a pullback by rates from current levels is not overly surprising. Trend support is currently near the 15-week moving average at 1.40%, illustrated in green below.

We find this pullback in rates particularly interesting given that recent institutional investor surveys continue to show a consensus view among most professional managers expecting higher inflation and economic growth, overweight cyclical stocks, and underweight bonds.

For equity investors, the movement in interest rates continues to have important implications for the leadership tug of war between cyclical and secular growth. In particular, as rates began to pause over the past few weeks, growth stocks, notably large-cap growth, rebounded from the lows established in March 2021. However, the rebound in growth stocks has not been uniform.


Source: RBC Wealth Management, Bloomberg, Optuma

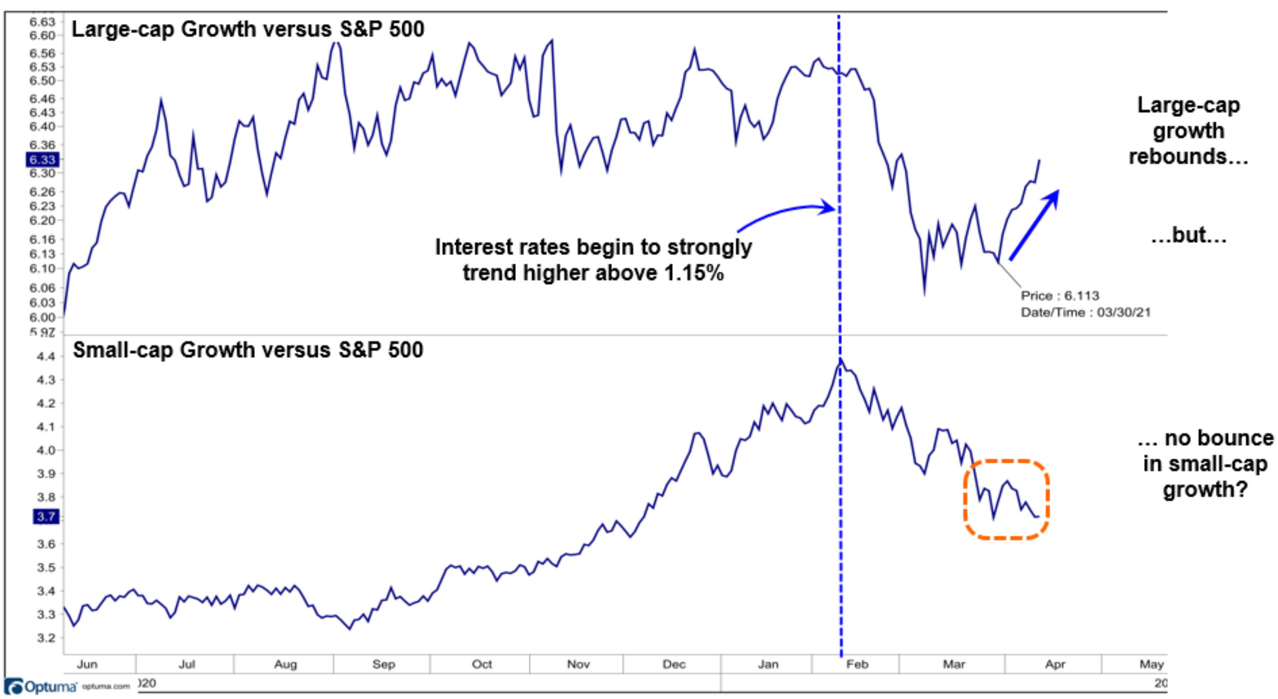
**Small-cap growth diverges from large-cap growth in April** - The chart below illustrates the relative performance of large-cap growth stocks versus the S&P 500 in the top panel, and small-cap growth versus the S&P 500 in the bottom panel.

As interest rates began to trend above 1.15% in February, growth stocks broadly sold off into March. The most recent highs in U.S. 10-year yields were at 1.77% on March 30 which is the same day large-cap growth U-turned to the upside versus the S&P 500, as seen in the top panel.

Interestingly, higher-risk small-cap growth stocks have yet to show a meaningful rebound establishing a divergence—but we think this situation bears close watching in the coming weeks and months. Is this divergence merely temporary given small-cap stocks in general have underperformed since mid-March, or is there a shift to higher-quality, less speculative stocks beginning to develop in the equity market?

To be fair, this is only a short-term divergence at this point but it is one we suggest investors monitor closely in the coming weeks, particularly given the impressive surge that developed in more speculative stocks in fall 2020 and early Q1 2021.

Our recommendation is for investors to review their portfolio holdings after a volatile first quarter to develop exit strategies for the more speculative positions. We view the March price lows for most growth stocks to be the key stop loss levels to control downside.




Source: RBC Wealth Management, Bloomberg Optuma

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|---|---|---|---|---|
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| Hold [Sector Perform] | 559 | 40.68 | 179 | 32.02 |
| Sell [Underperform] | 53 | 3.86 | 4 | 7.55 |

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