EQUITIES PERSPECTIVE

January 12, 2018
DJIA: 25,575

Make America great … and the rest of the world even better? For stocks, 2017, indeed, was great. Still, this left the S&P 500 ranked only 23rd among world markets. Eight years of a mixed political record and the worst economic recovery ever didn't stop the stock market from tripling under Obama's watch. The stock market does what the stock market does, logic need not apply. The only logic that matters is that of the market itself—there's money out there to be invested. This is the logic originally behind the "January Effect"—the end of tax-loss selling and new money in the new year to be invested. That there is new money, we contend, shows up in those advance-decline numbers. Rare has been the day with fewer than 1,200 advancing issues, and that takes money. It's not just about the market averages, which, if it were, would be a different story. The average stock acts as well as the stock averages—not how the market gets into trouble.

The market has rallied almost every day for the past three weeks and the three weeks before that. During the past month, there have been only seven down days in terms of breadth. The market hasn't had a 3% correction in a lifetime. Here's an insight—the market is overbought. The real insight is this is not necessarily bad. When the market is in a trading range, overbought means some sort of setback should be expected. Then, too, there are what you might call "good overboughts," where the market becomes overbought and just stays there. These say it's a strong market and the usual parameters don't apply. Our chart of stocks above their 10-day average does as good a job as any in depicting this. It fluctuates between 20% and 80% in a normal scheme of things. It hasn't been around 20% since August, and even moves down to 40% have been relatively rare. Strong markets stay strong.

When Heraclitus (500 BC) quipped you never step in the same river twice, it wasn't exactly his best call. Here we are in 2018 and not all that much has changed, even market leadership. Tech still leads, including the FANG which, after a two-to-three month respite at year's end, aren't all that extended. Stop us if you've heard this before—we don't think this bull market will end without a speculative binge somewhere, likely the FANG stocks. So for completely selfish reasons—we would rather not see the bull market end—we would like to see the FANG somewhat temper their enthusiasm. Then, too, "blow-off moves" typically are relatively exclusive, while, in this case, there are many stocks acting well. Blowoff moves in this or that group don't come along when the Advance-Decline Index is at a new high. Think, for example, of the "nifty-fifty" in 1972 or the "dot-coms" in 2000. It was pretty much them and nothing else.

Rather than oscillators, like stocks above their 10-day moving average, there are other ways to measure the idea of overbought. A bit perversely, the number of 12-month New Highs is one such measure, and it's of relevance here when it comes to the Materials Group (XLB-63). Half the stocks in this group recently reached a 12-month high, typically a sign of buying exhaustion. You may recall the opposite was true of the Energy sector last July, when half of those stocks reached 12-month New Lows, typically a sign of exhausted sellers. After the usual basing, Energy stocks have turned into some of the best performers in the new year. Then there is the dark side of the rise in rates. Utilities are down 10% from the recent high and the Real Estate ETF (IYR-78), about 6%. Meanwhile, Banks they say will benefit and, at least so far, so good.

It has been a while since we've mentioned stocks above their 200-day average, obviously a big picture look. This is another oscillator where 20%-to-80% pretty much tells the tale, but as it is longer term, there is another side to this measure. As we've noted, stocks tend to bottom together, but peak a few at a time. Over the course of a bull market, the number of stocks remaining in uptrends, that is, above their 200-day, tends to diminish, leaving a series of lower peaks. While it seemed such a pattern could be in place a couple of months ago, apparently it's not. That this indicator has made it back to near 80% is surprising in a 9-year old bull market, and positive. Momentum doesn't turn on a dime, it takes time to unwind. If this indicator is the guide it has been in the past, the unwind is yet to begin. In the meantime, let us hasten to throw in the obligatory market letter cautionary clause—the market is due for a correction, yada, yada.

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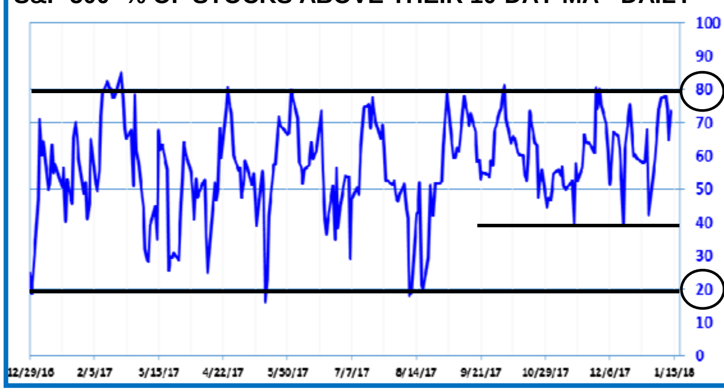
S&P 500 (SPX – 2768) – DAILY

NASDAQ 100 (NDX – 6708) – DAILY

S&P 500 -% OF STOCKS ABOVE THEIR 10-DAY MA - DAILY

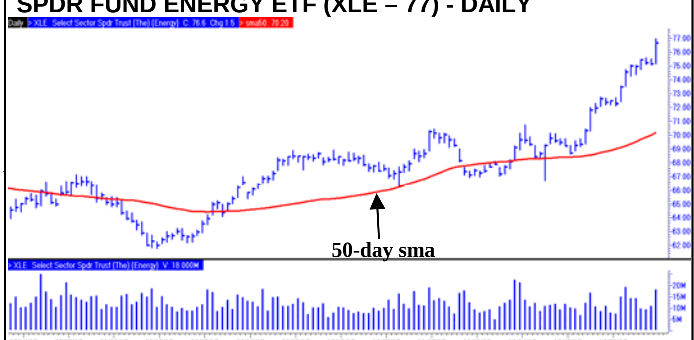


S&P 500 -% OF STOCKS ABOVE THEIR 200-DAY MA - DAILY

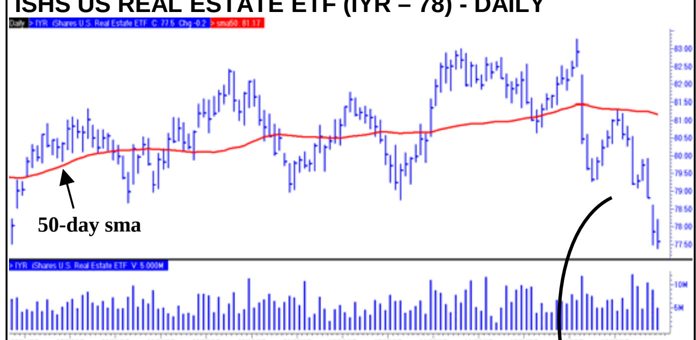
FACEBOOK INC. (FB – 188) - MONTHLY

SPDR FUND MATERIALS ETF (XLB – 63) - DAILY

SPDR FUND ENERGY ETF (XLE – 77) - DAILY



ISHS US REAL ESTATE ETF (IYR – 78) - DAILY



BOEING COMPANY (BA – 328) - DAILY

CBOE INTEREST RATE 10YR TSY (TNX-UT – 25) - DAILY