EQUITIES PERSPECTIVE

June 17, 2016
DJIA: 17,733

Rates unchanged … stocks go down? The Fed tells you one piece of data doesn't matter. Then they get a piece of bad data and it does matter. How's that credibility thing going? It's little wonder the market looks so confused. By confused we also mean strange. Thursday the market rallied 280 points from the morning low. This time, however, those Advance-Decline figures lagged, leaving the more typical negative pattern of strength in the large-caps and weakness in the rest. Now we're back to normal bad versus what has been abnormal good. The abnormal good is the incessant string of new highs in the Advance-Decline Index versus the incessant inability of the S&P to reach its own new high, not that it hasn't been trying. How can all those stocks go up most days and the S&P not break out? The answer seems to be they go up, but they don't go up a lot.

Instead of just measuring stocks up or down like the Advance-Decline Index, QCHA measures by how much. It's not just about direction, the QCHA is about the degree of that direction. The QCHA peaked back in April 2015 and is yet to surpass that peak. This isn't to say the market is weak, it's just not as strong as Advance-Decline figures would have you believe. An old-fashioned breadth divergence – strength in the averages and lagging breadth – that's a weak market. That is the pattern that sinks ships, or at least ends rallies. The divergence between the Advance-Decline Index and QCHA Index, a cumulative total, is strange but not necessarily harmful. For either to diverge against the Dow or S&P, that would be harmful. Meanwhile, less esoteric divergences persist as well. Few things are less esoteric than the Transports, and some would say few are less important. However, the Transportation Average does represent a broad smattering of economically-sensitive stocks and it peaked in late-2014. And then there is the Russell 2000, which measures secondary stocks. It peaked in mid-2015 and again in late-2015, both of which remain.

Brexit isn't exactly new news, but suddenly it's all the rage as a market driver. Economists are universal in their vote to stay, but Brexit is about more than just the economy. The bloke on the street is thinking about immigration, which adds a whole dimension beyond economics to the logic and possible outcome. Enough of our "two cents," let's talk real money. The polls are one thing, the betting parlors another. The latter, the money, is betting on the no-go vote. The Investors' Intelligence Survey, which we allude to from time-to-time, offers a warning sign when bulls greatly outnumber bears. However, it is a measure of market letter writers and, trust us on this one, what do they know? More worrisome, it's a "survey." We rarely mention Put-Call Ratios, but we follow them – the buying and selling of Puts and Calls. Both measures are useful but if the truth be known, we will always lean to what people/investors actually do, versus what they are saying. So when it comes to Brexit, we vote with the money.

The VIX, or Volatility Index, often is criticized for being late. By the time it moves, the market already has moved, leaving one to say – thanks for that. It is a better guide to market lows than to market peaks in that you are never going to put in an important low until fear, that is, the VIX, spikes. Fear produces selling and selling produces the liquidity for a market turn. It's not buying, it's getting the selling out of the way that makes a low. In the event, the pattern in the VIX this time has been unusual. After spending three months – though it seemed longer – below 17, the VIX finally has spiked. The odd thing is it has done so while volatility in stocks has declined. In the past this pattern has led to poor short-term performance or, in other words, the VIX became anticipatory. As a timing indicator the VIX is tricky. A high VIX is good, but how high – there's no magic number. When a low is in, it's a decline in the VIX that will confirm it. These days, of course, the VIX has a lot to do with Brexit.

Brexit isn't discounted, regardless of whether the vote is stay or go. It's one of those known unknowns, which should make for a volatile week. Inverse ETF volume jumped this week and on Thursday, accounted for almost 10% of NYSE volume. In this case however, there's no evidence that this is the "smart money," and much of this no doubt is hedging against long positions. With stocks above their 10-day moving average down around the 20% level, this is where stocks should make a stand, all things being equal – which they're not. Troublesome are those patterns in stocks above their 50-day and 200-day averages. They say the recovery is over. However, even if all things were equal, we doubt a big decline is at hand just yet. We lean to a more traditional scenario where there's finally a rally to a new high in the S&P, but one with, finally, poor Advance-Decline numbers and maybe a little speculative binge. In other words, a bull market top like the good old days.

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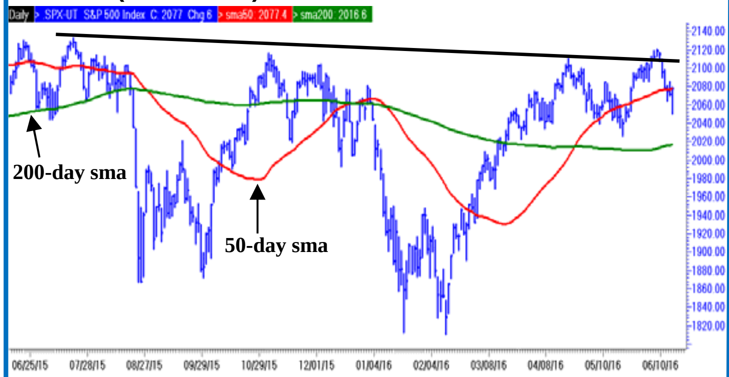
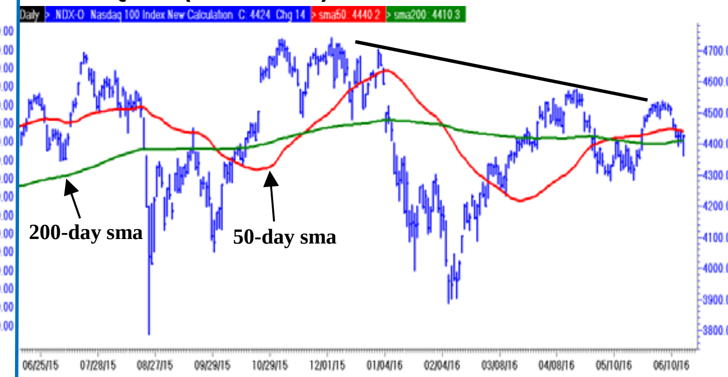
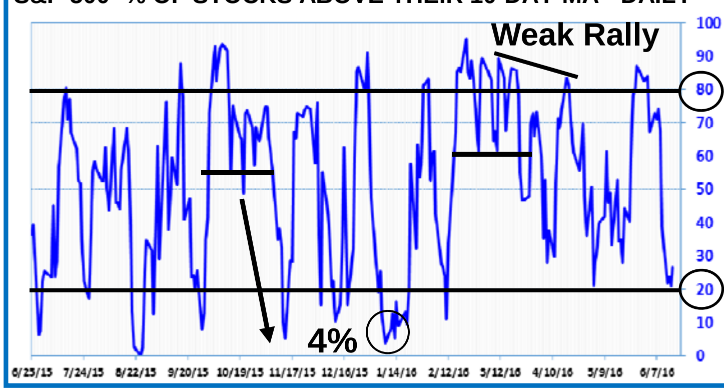
S&P 500 (SPX – 2078) – DAILY



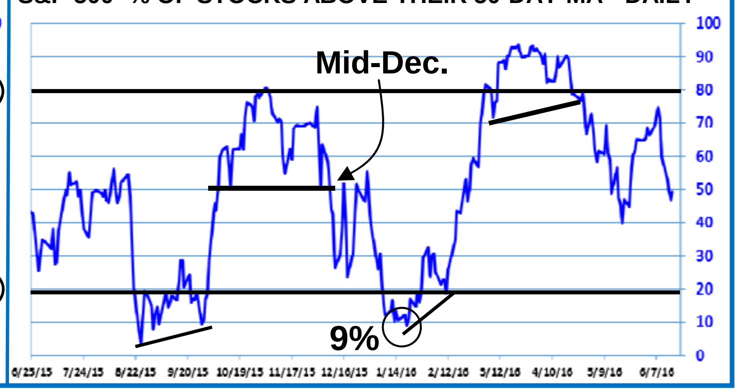
NASDAQ 100 (NDX – 4424) – DAILY



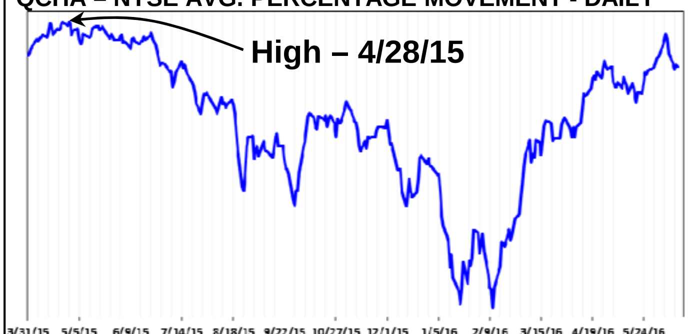
S&P 500 -% OF STOCKS ABOVE THEIR 10-DAY MA - DAILY



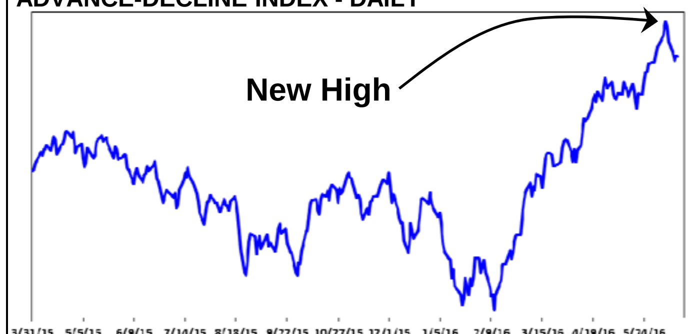
S&P 500 -% OF STOCKS ABOVE THEIR 50-DAY MA - DAILY



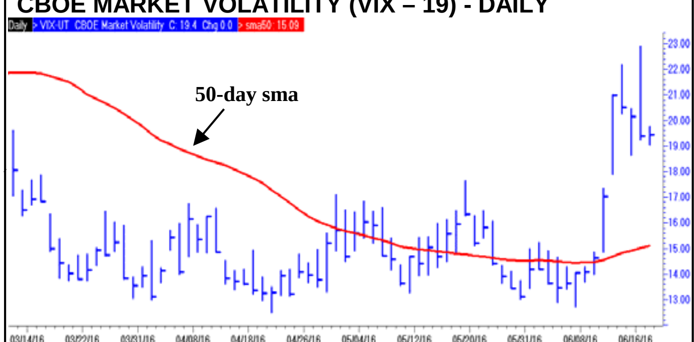
QCHA – NYSE AVG. PERCENTAGE MOVEMENT - DAILY



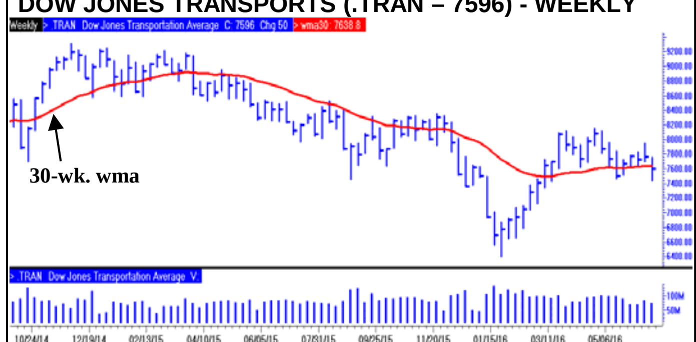
ADVANCE-DECLINE INDEX - DAILY



CBOE MARKET VOLATILITY (VIX – 19) - DAILY



DOW JONES TRANSPORTS (.TRAN – 7596) - WEEKLY



SPDR S&P BANK ETF (KBE – 31) - WEEKLY

DEUTSCHE BANK A G (DB – 15) - WEEKLY