

EQUITIES PERSPECTIVE

September 29, 2017
DJIA: 22,381

Are we seeing volatility ... or movement? To look at the major averages, other than a little selloff in August and a little rally in early-September, it has been more trading range than movement. When it comes to volatility, the numbers say there is none—we are about to end the month with the least volatile September on record, according to SentimenTrader.com. This seems surprising, or are we all just too focused on those high-priced FANG stocks? Then, too, pretty much everything is high priced these days—can you remember the last stock split? Those of us of a certain age can't help but live with a certain dread of October. You'll be glad to know, however, history doesn't suggest there's a volatility payback for low volatility in September. In terms of movement, no volatile selloff in September typically means no volatile rebound in October. Imagine that, you can't have it both ways. Then, too, as we've said many times, if the market always followed the script, this would be coming your way from the South of France.

The real surprise this month has been Small-Cap stocks. Since dropping below its 200-day moving average in mid-August, the Russell 2000 has rallied three-quarters of the time to a new high. Hand-and-hand with this rally in small-cap stocks has been the performance of the Advance-Decline Index, which now has rallied 18 of the last 21 days, a rather stunning feat—go you Banks and Oils! Bull markets don't die of old age, yada, yada. They die when all the money is in and this shows up in a narrowing market. The narrowing, history shows, begins with small-caps and, hence, divergences between the A-D Index and the price averages. The big-cap averages are the last to give it up. So when we speak of new highs in the Advance-Decline Index not being the backdrop for big problems, this is what we mean. At market peaks, typically there is a group of stocks that drives the big-cap averages higher—the nifty-fifty, or the dot-coms, or whatever. For now, the market averages aren't exactly kicking it here.

“Nightmare” is the word that comes to mind when it comes to Energy this year. Things became so bad that in August, more than half of the S&P Energy sector reached 12-month new lows. So bad that in this case, it was good, suggesting a “washout.” If stocks, indeed, are washed out, they should rally, and so they have. Within a couple of days, there were no 12-month lows in the sector and the stocks have continued to recover, rallying some 20 of the next 25 days. In the process, the sector ended its run of six months below its 200-day moving average. Not every “washout” as described above results in a new bull market, but the degree of strength in this case is encouraging in this regard. The big Internationals probably have the best patterns, the Drillers will have the best moves, especially on a percentage basis. This probably is the most homogenous group we can think of—when they go, they all go.

We came across a chart the other day that made us think that maybe there is speculation. We don't know the stock, we don't know the company, but we do know that at its recent peak around 75, it was almost 4x its 50-day moving average. Like the famous can of sardines that was for “trading” and not for “opening,” someone on Wednesday opened Veritone (37) and the stock went from being up about 10 to down about 20. This isn't the kind of reversal that is easy to survive. Fortunately, this is a rarity, though a few of the hot Biotechs are becoming a little stretched as we speak. In an overall sense, speculation is absent. The NYSE recently released the August data on margin accounts, showing a small increase from July and a more eye-catching increase of 17% from August a year ago. Given that the S&P is up 14% during this period, this is not a big concern. It's also not like 2000 or 2007 when margin debt grew almost irrationally, regardless of what stocks were doing. Finally, it's when margin debt stops growing that it's time to worry.

So which counts, the Dow's 54-point drop on Monday, or the Dow's 56-point rally on Wednesday? To make the answer more difficult, allow us to point out the advance-declines were positive and by the same amount on both days—good for a down-day, not so good for an up-day. Pretty much the same is true of the NAZ, where the FANG have fallen and are having trouble getting up. By the looks of that Amazon (956) chart, it could take a while. The market has conditioned everyone to sharp comebacks in these stocks, maybe too much so—most haven't made new highs since July. Biotech seemed to be taking up some of the “hot stock” slack, but a number of the big-caps there have lagged. As a result, the unweighted XBI (86) has outperformed the weighted IBB (331) of late. Last week Nvidia (176) looked the place to be, this week it's Royal Dutch (60). This market is less about direction than it is about rotation.

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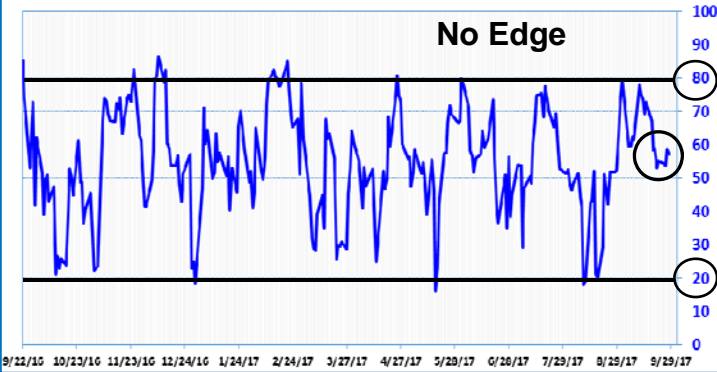
S&P 500 (SPX - 2510) - DAILY



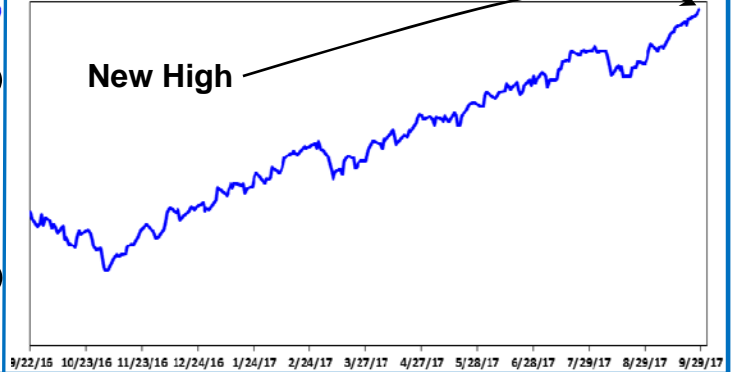
NASDAQ 100 (NDX - 5933) - DAILY



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



ADVANCE-DECLINE INDEX - DAILY



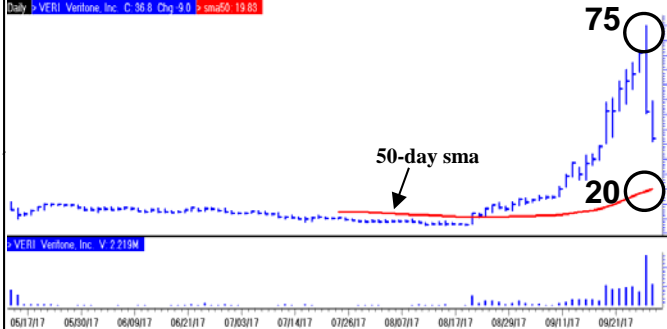
ROYAL DUTCH SHELL PLC (RDSA - 60) - DAILY



TRANSOCEAN LTD. (RIG - 11) - DAILY



VERITONE, INC. (VERI - 37) - DAILY



AMAZON.COM INCORPORATED (AMZN - 956) - DAILY



RUSSELL 2000 INDEX (RUT - 1488) - DAILY



SPDR S&P BIOTECH ETF (XBI - 86) - DAILY

