Leavitt Brothers

Weekly

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Two weeks ago the market posted its biggest gain of the year. It followed up the gain with another 1.3% last week that closed the S&P about 5 points from its all-time high. When dividends are considered - and they should be - the index is already at an all-time high.

A 2-day, 100-point S&P drop was all the bears could manage after the Brexit vote. Since then, the SPX has rallied 6 of 8 days and recaptured the entire loss.

There are many things working against the market right now.

The UK is leaving the EU, and there's a possibility the entire EU unravels. Banks in Italy and other countries are on shaky ground. Even strong countries like France have taken on massive amounts of debt. The sum of all these should at least cap the market's upside, but they haven't mattered. The US market has completely shaken everything off.

Earnings in the US have declined, but this hasn't mattered either. Either the market doesn't seem to care or it's assuming the recent earnings season was just an aberration.

The internals have weakened some. Several indicators are doing great; others hint at some weakness beneath the surface. But this hasn't mattered either. Here we are within 5 points off the all-time high.

Many big bellwether tech stocks have been dead money for a while. Apple, Netflix, Google, Microsoft and many others have lagged the overall market the last few months.

Meanwhile, risk-off assets (utilities, REITs and many safe-havens such as Procter & Gamble and Johnson & Johnson) are doing great. And gold and silver, which tend to do well when the world's financial institutions are in trouble, are practically going parabolic.

On any given day there's potentially big news looming from Europe...the internals have come down some...and money is rotating from risk-on to risk-off assets. Yet the market doesn't care. Here we are near all-time highs. It makes no sense, but at the same time it makes perfect sense.

The market trades in anticipation of what's in the pipeline 6-9 months down the line...but in the near term it trades based on the current psychology of the market's participants along with the supply/demand balance. If too many get stacked on one side, a move that makes no sense to the other side often plays out.

There are perma bears out there (they don't deserve to be named), who are permanently gloom and doomers and always think the world is coming to an end. But when George Soros and Stanley Druckenmiller join the chorus with their own negative comments, the market either falls hard or you get an hysterical squeeze up. I think there's a legit possibility the latter plays out.

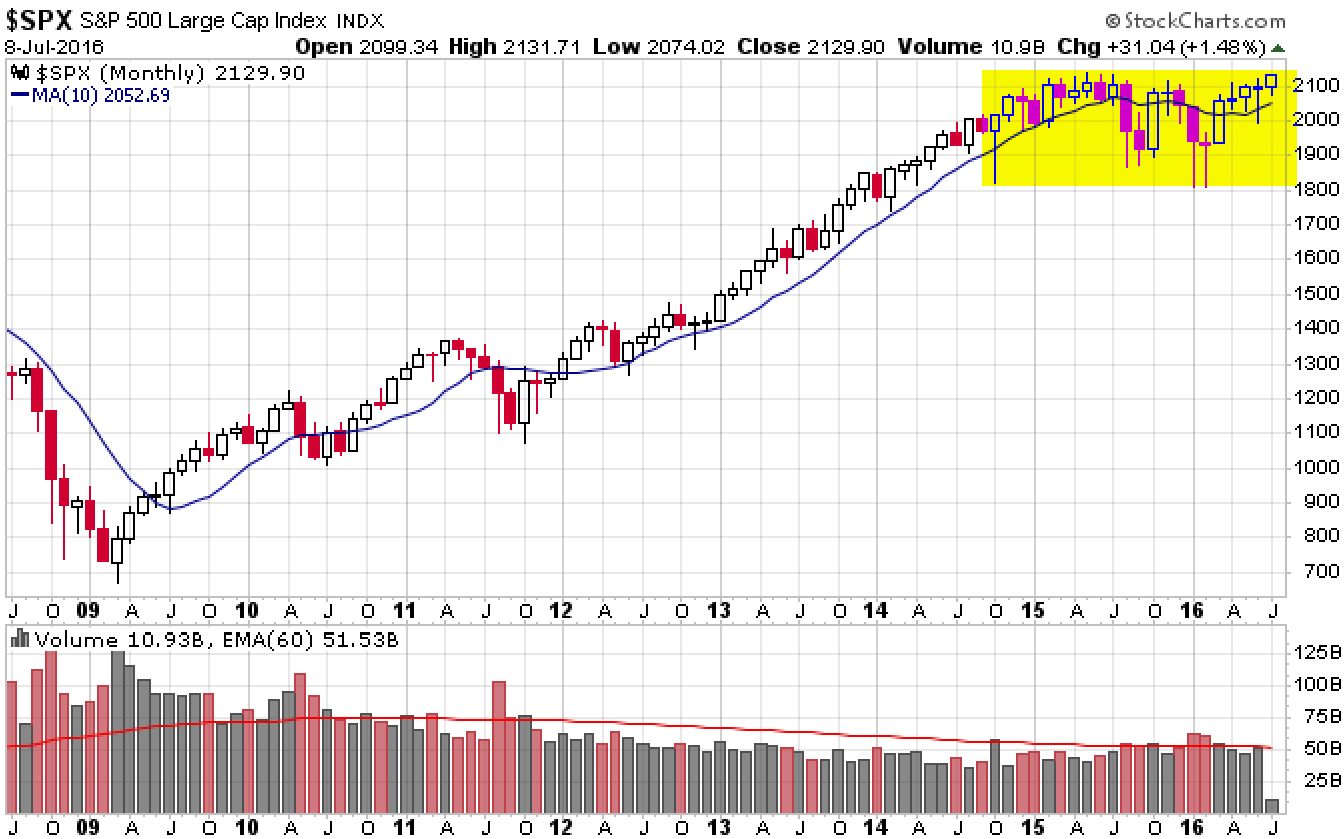
Bonds remain strong, so bond yields are very low - low enough to be unattractive (although they're a heck of a lot better than the negative yields in Europe). This helps the market.

With the uncertainty in Europe the Fed might only do one more rate hike this year, but I'd say odds favor no more. This also helps the market. Low rates at the bank help in the same way low bond yields help...they cause money to be put to work in the stock market because it's the only place one can get a decent return.

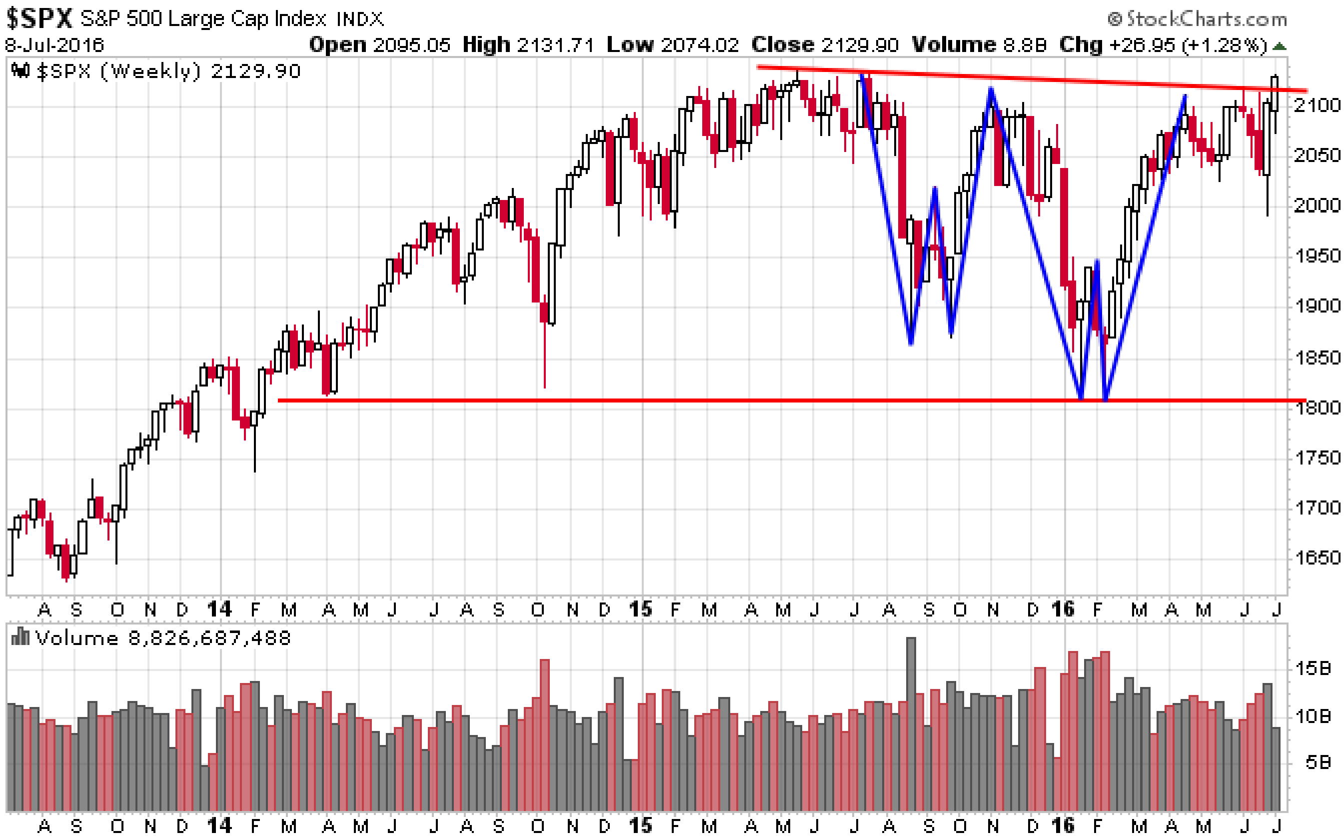
I don't like the rotation to risk-off assets, but the Fed will remain accommodative, and the psychology of the market (there are lots of bears and under-invested bulls) tells me a breakout and rally is more likely than a big drop. Let's get to the charts and see what they say.

Indexes

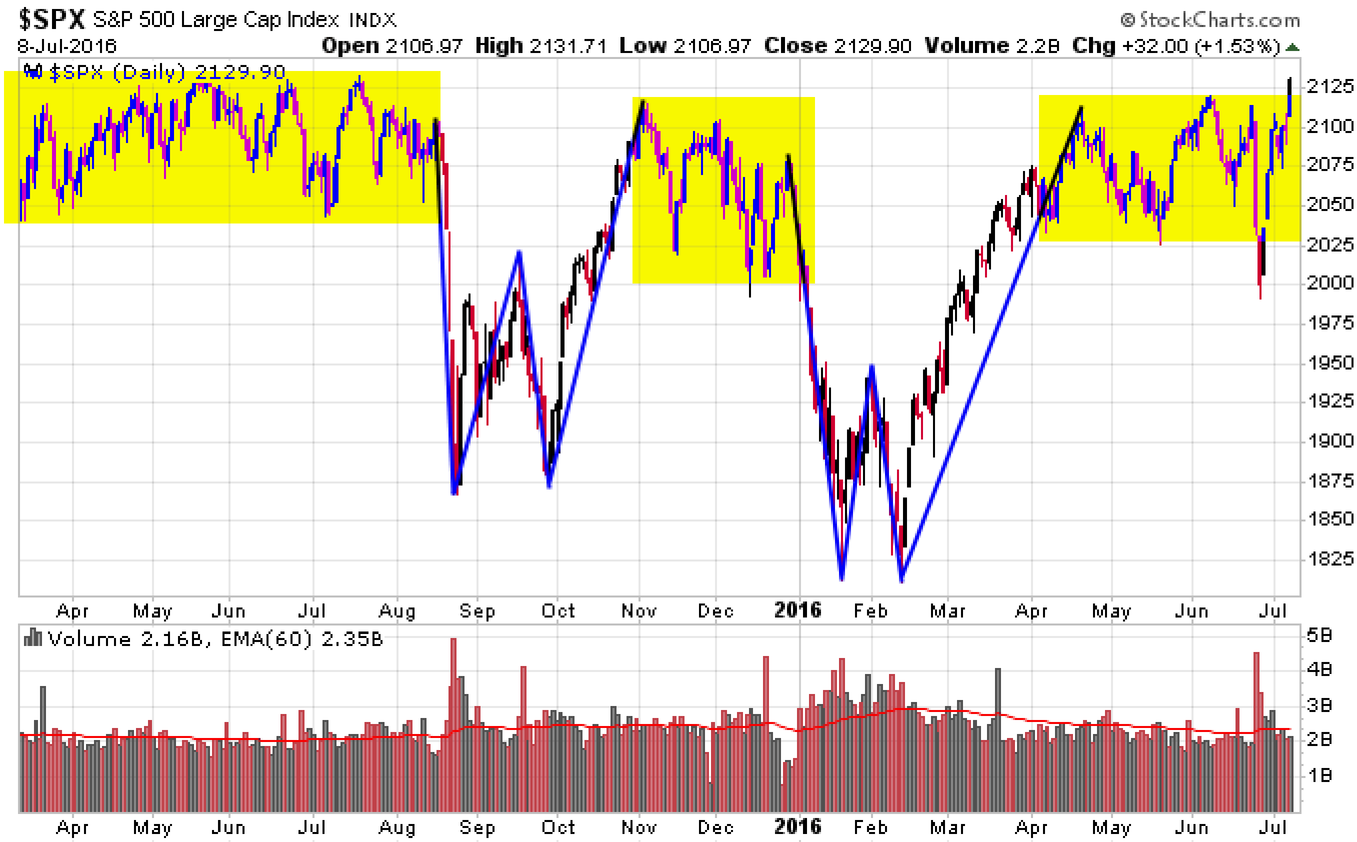
The S&P 500 Monthly: It's a little early to post a monthly chart, but oh well. A massive rally that saw the S&P triple has been followed by about 20 months of consolidation. There is nothing wrong with this. Anyone who is bearish doesn't know how to read a simple chart. The size of the pattern (300 points) measures up to about 2400.



The S&P 500 Weekly: Back-to-back up weeks have put the S&P at its highest level since last summer. Overall I still consider this to be a consolidation pattern. We need a clean breakout and enough separation to allow for a pullback before we can declare the next leg up to be underway. But you can't wait for a breakout to get long. If you do, you'll want a pullback, which will never happen, and you'll be stuck standing on the platform while the train pulls away in the distance. While the market is in consolidation mode, you have to get long the out-performers.



The S&P 500 Daily: It looks like we got a false move down and now a breakout. Classic TA says we need follow through before the breakout is confirmed. One step at a time. So far, so good.

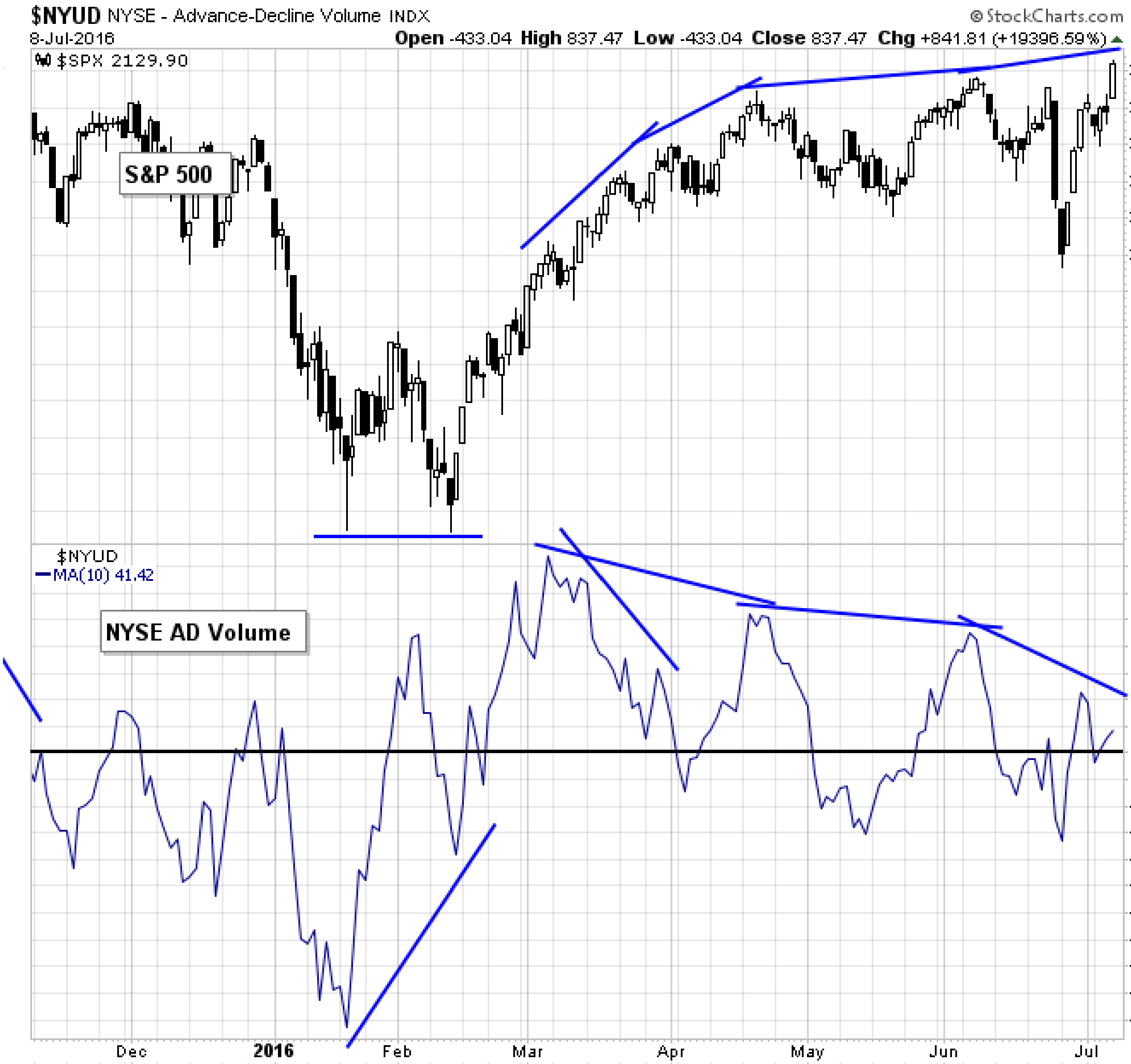


Indicators

S&P 500 vs. 10-day MA of NYSE AD Line: The S&P has jumped to its highest level since all-time highs were put in place last summer, but the 10-day of the AD line has not matched the movement. Divergences take time to play out - see March and April where a divergence formed but the market pressed higher for three more weeks - so nothing is imminent. But the bulls will want to see the AD line quickly catch up.

S&P 500 vs. NYSE Cumulative AD Line: Despite the quick post-Brexit plunge, the cumulative AD line maintained its steep accent. This chart has told us all along the market was in good shape internally. At no time has it moved like it did last summer when it trended down while the market traded range bound.

S&P 500 vs. 10-day MA of NYSE AD Volume Line: The 10-day of the AD volume line is sitting at 0. There was so much selling after the Brexit vote, it has taken a full eight days just to counter the force. A negative divergence is going to form. The question is: What happens after the five post-Brexit days fall off the calculation? Will we get a healthy print indicative of a healthy market?

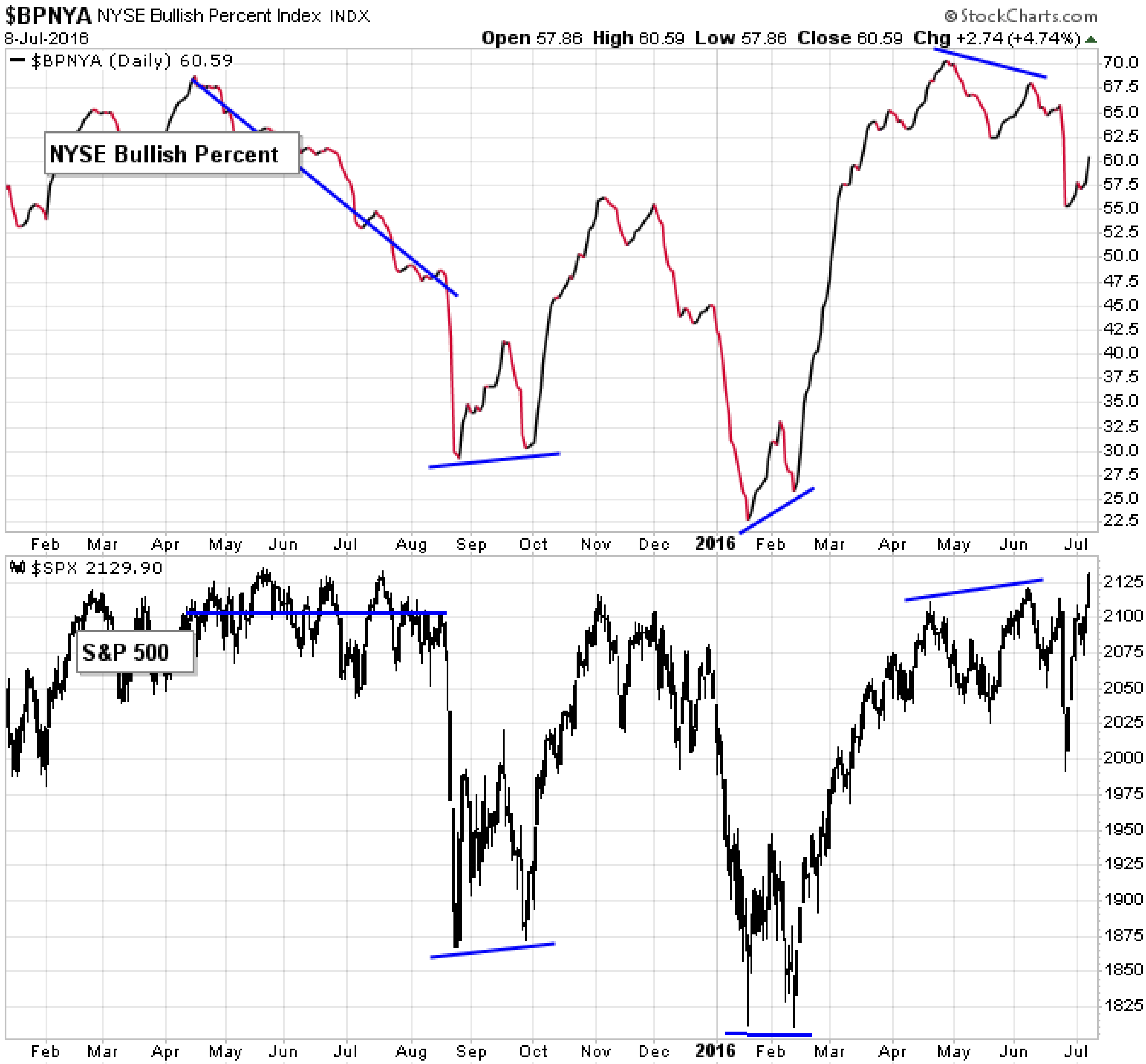


S&P 500 vs. NYSE Cumulative AD Volume Line: The cumulative AD volume line hasn't been as strong as the AD line (thanks to some lagging big caps (AAPL, MSFT, NFLX, etc)), but it has not trended down during the entire consolidation period. Nothing here hints at beneath-the-surface weakness.

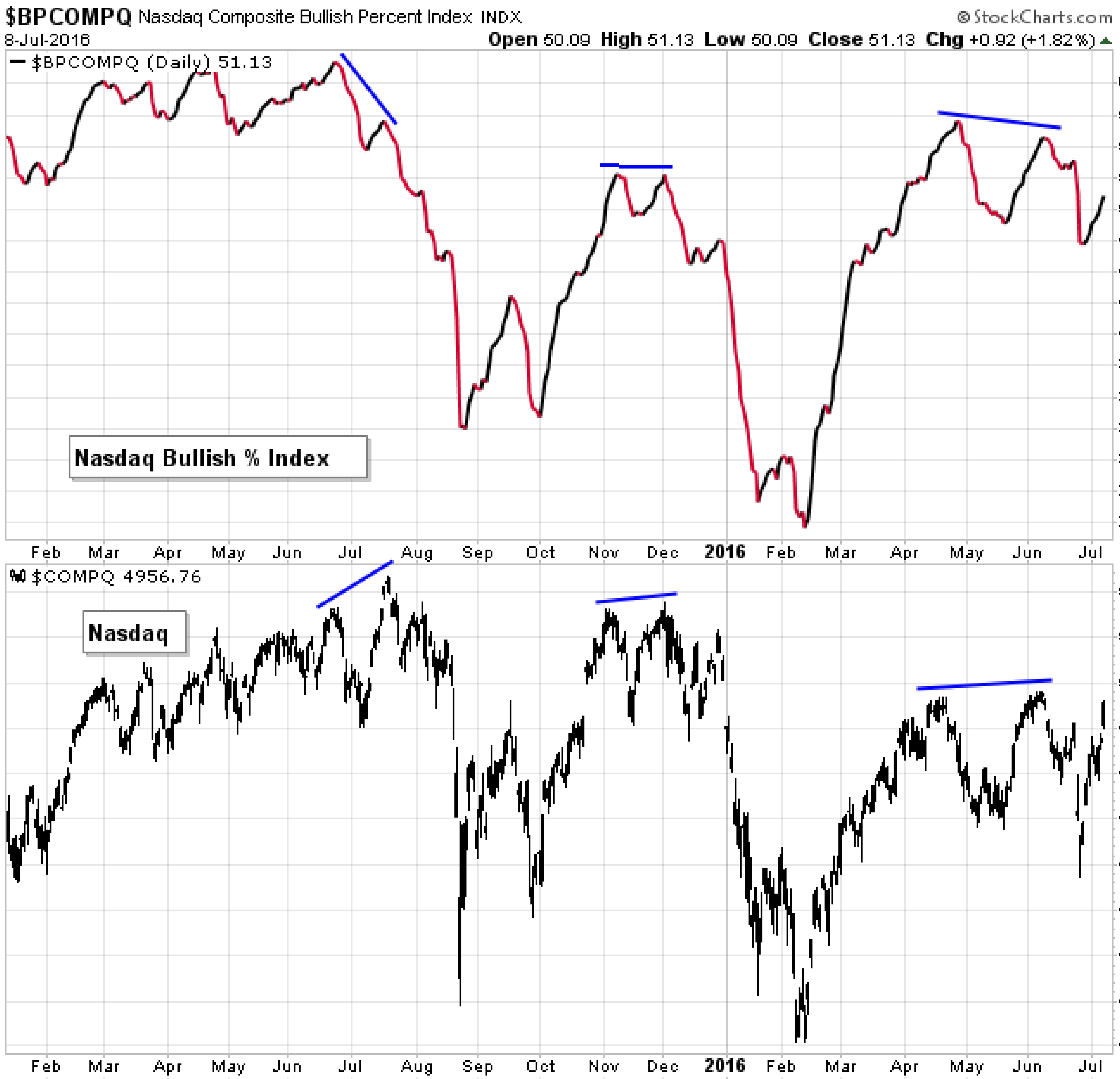
S&P 500 vs. NYSE New Highs: This is the highest print in new highs since 2013, and it's the highest level attained by the 10-day since the same time period. Leadership might not be coming from traditional sources, but it's coming from somewhere. The baton wasn't dropped...it was passed to some unexpected runners.

NASDAQ vs. NASDAQ New Highs New highs at the Nas, which have lagged the NYSE, continue to show more life. The 10-day has yet to take out its previous high, but we're currently getting the highest single-day print since last July.

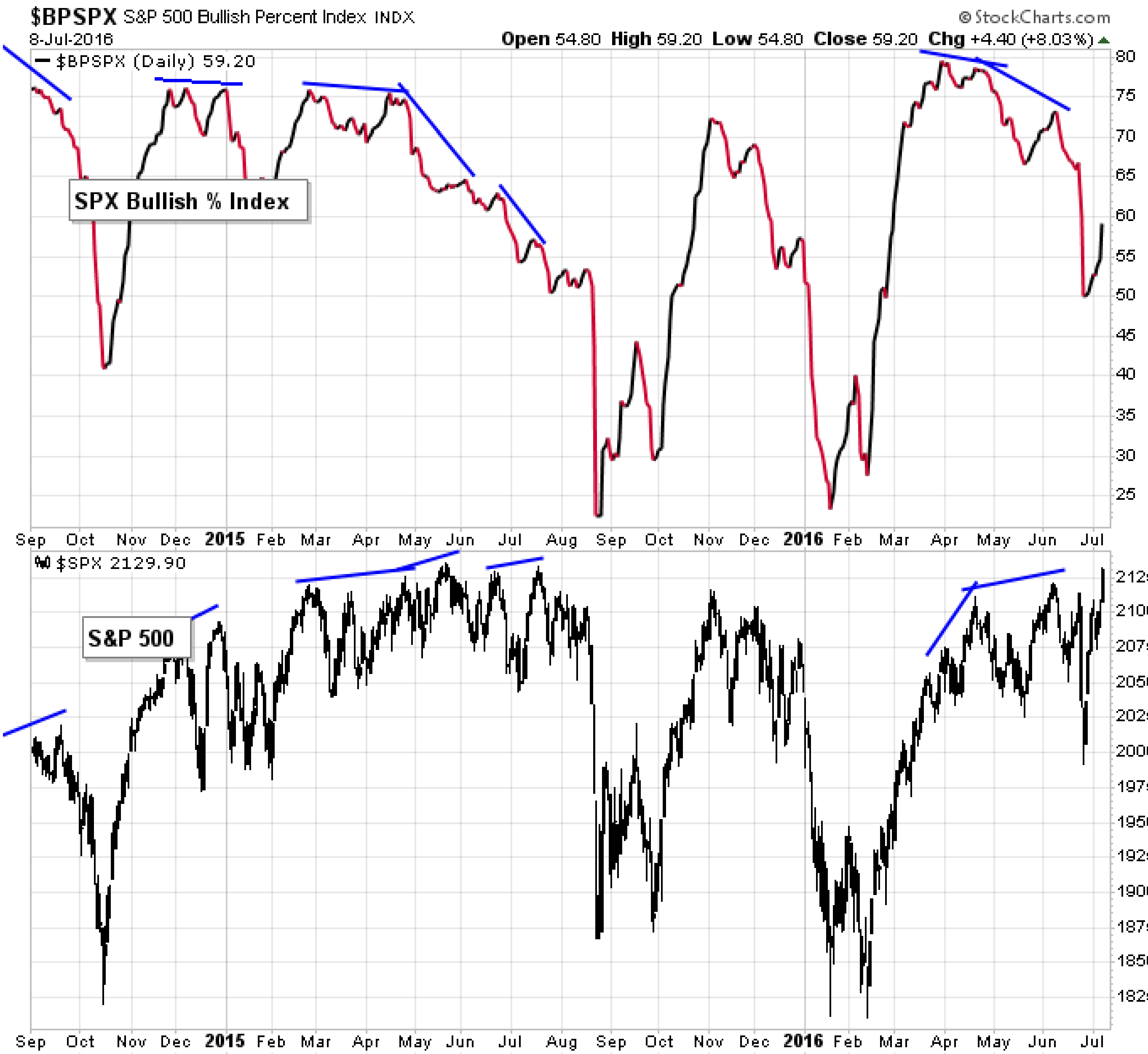
S&P 500 vs. NYSE Bullish Percent: Despite the S&P moving to a new high, the bullish percent at the NYSE remains in a downtrend. This indicator measures the percentage of stocks within a group that have buy signals on their point-n-figure charts. It seems as though many stocks gave up their buy signals after the Brexit vote, and some have still not recovered them yet.



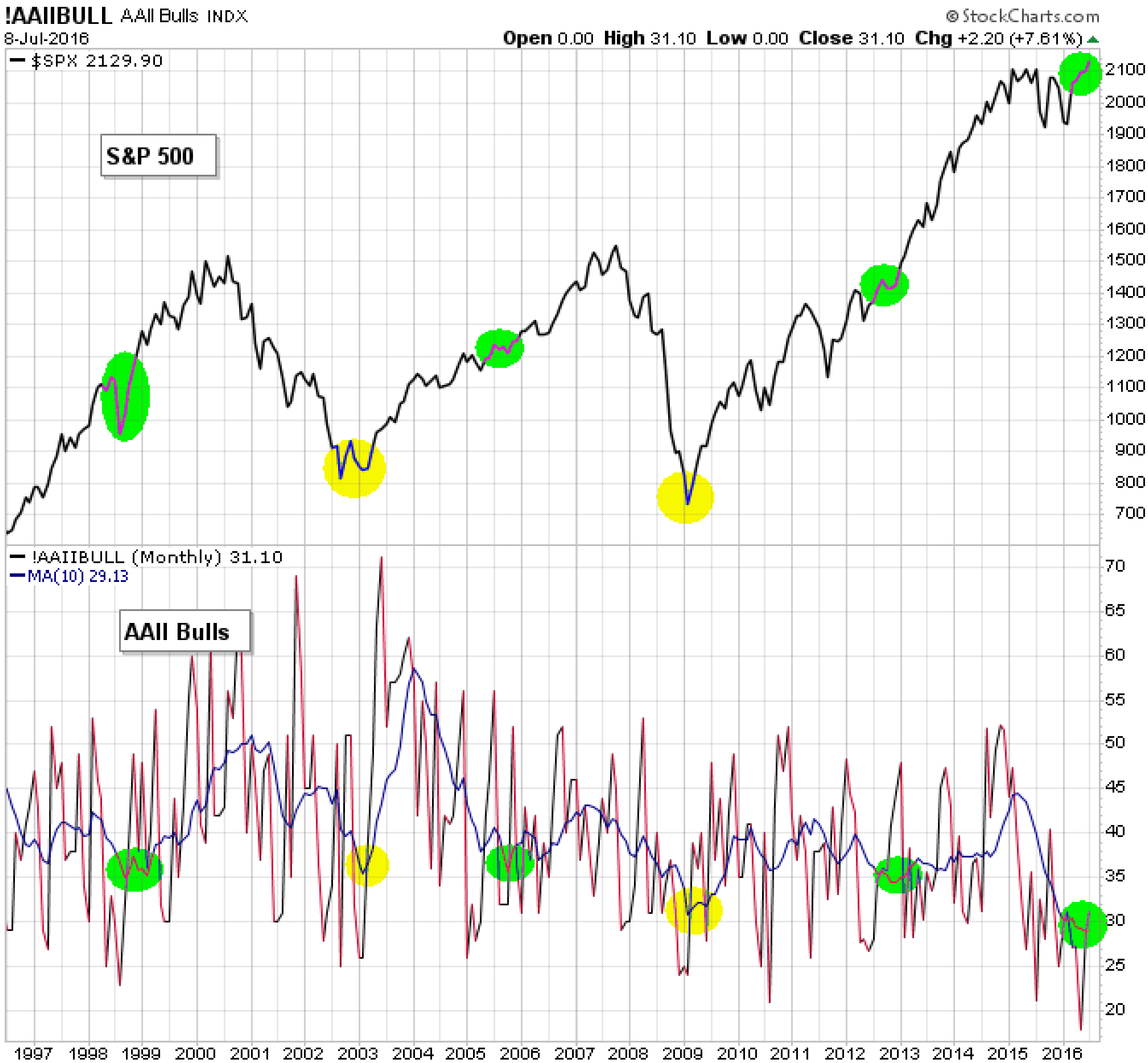
NASDAQ vs. NASDAQ Bullish Percent: The Nas bullish percent is in better shape but has still put in a lower high and lower low. I'll be more forgiving here because the Nas itself has moved similarly.



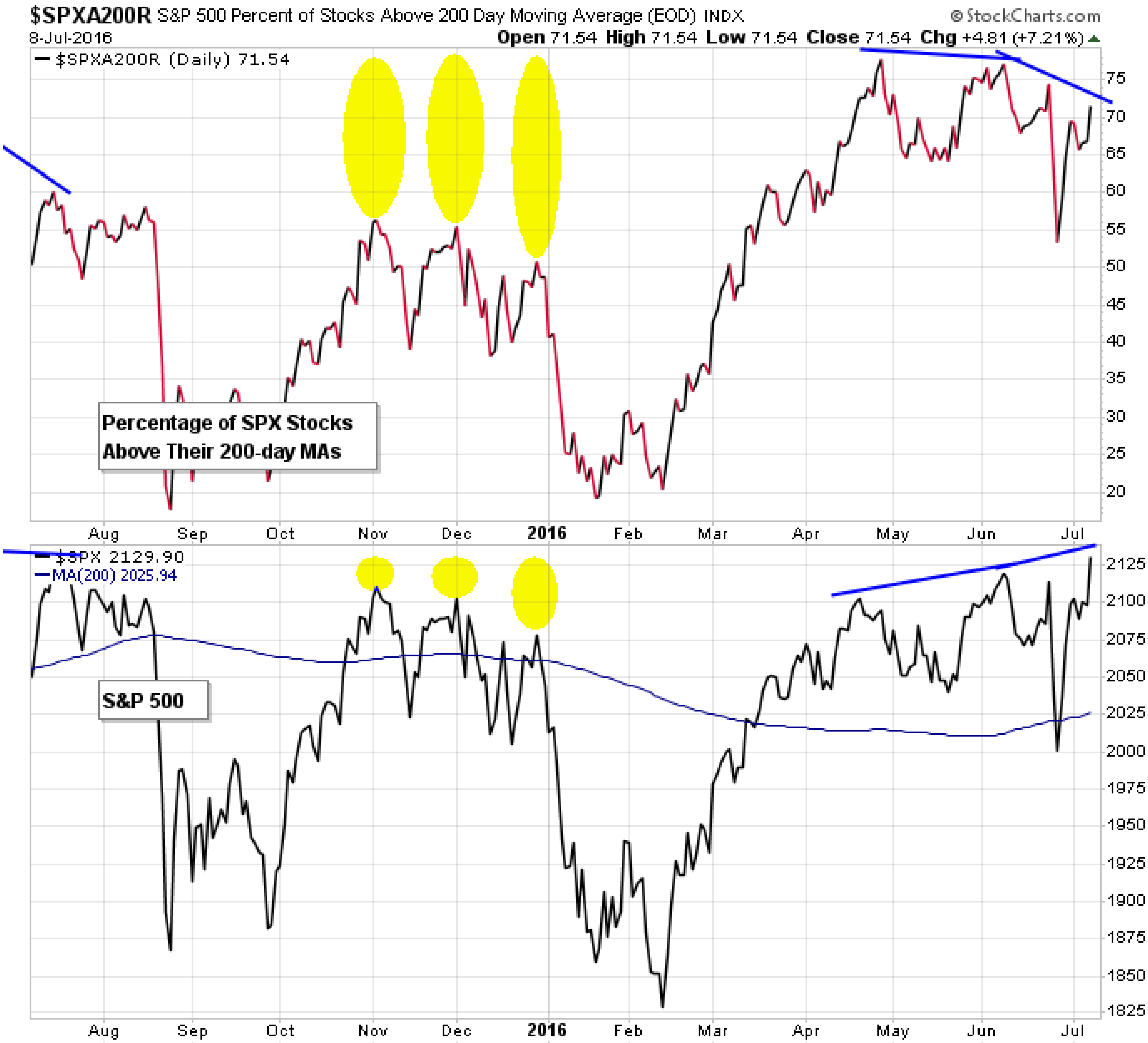
S&P 500 vs. SPX Bullish Percent: The S&P bullish percent is flashing an obvious warning. While the index now sits near its all-time high, less than 60% of SPX stocks have buy signals. The bulls need to see rapid improvement here.



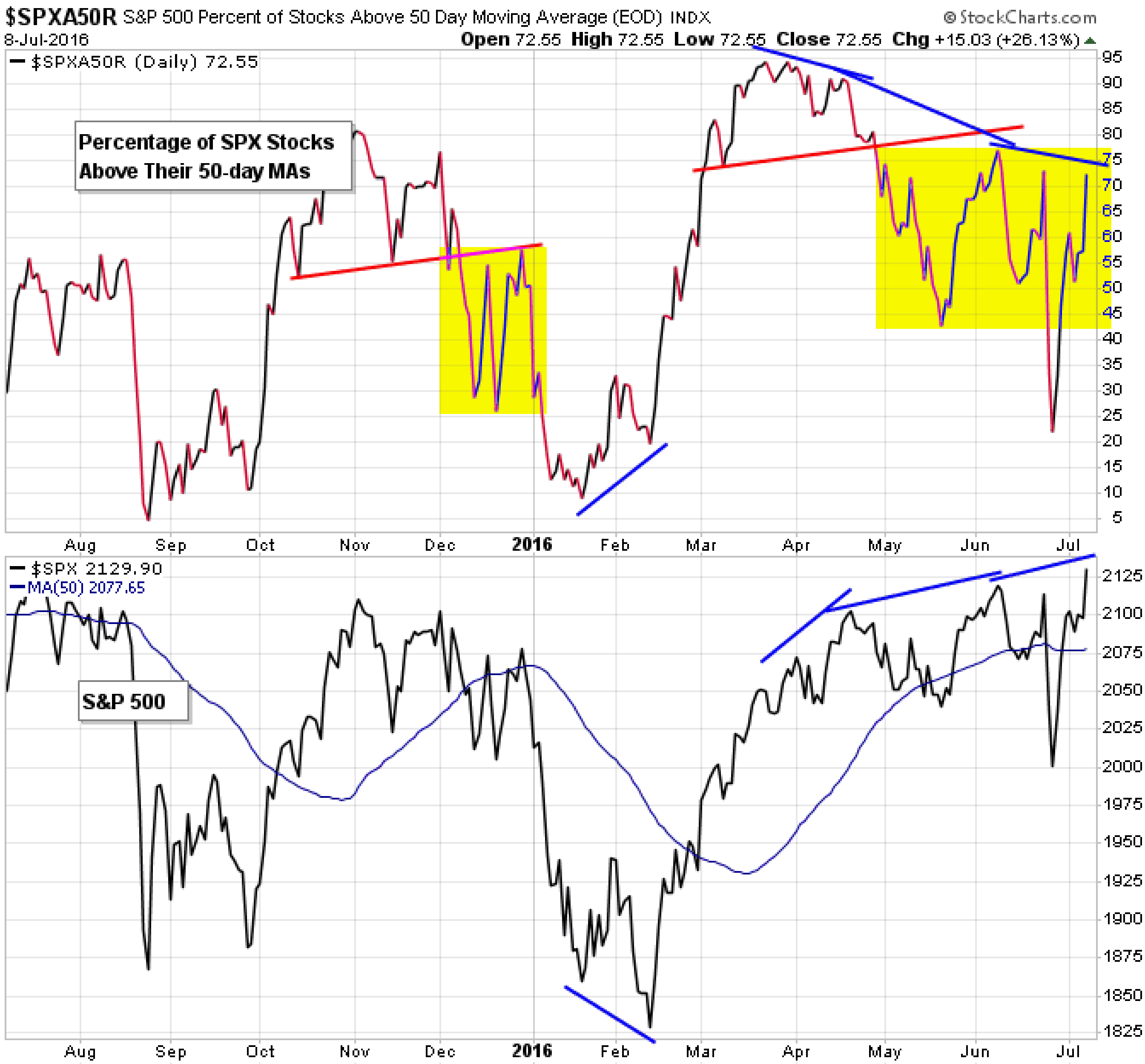
S&P 500 vs. AAII Bulls (monthly): This is what I alluded to in the open. There's a lot of negativity out there. The 10-day of the AAII bulls is at its lowest level in 20 years. Previous low prints have coincided with major market lows (yellow) while other bottoms acted as nothing more than pauses within uptrends (green). In either case, low prints have led to higher prices.



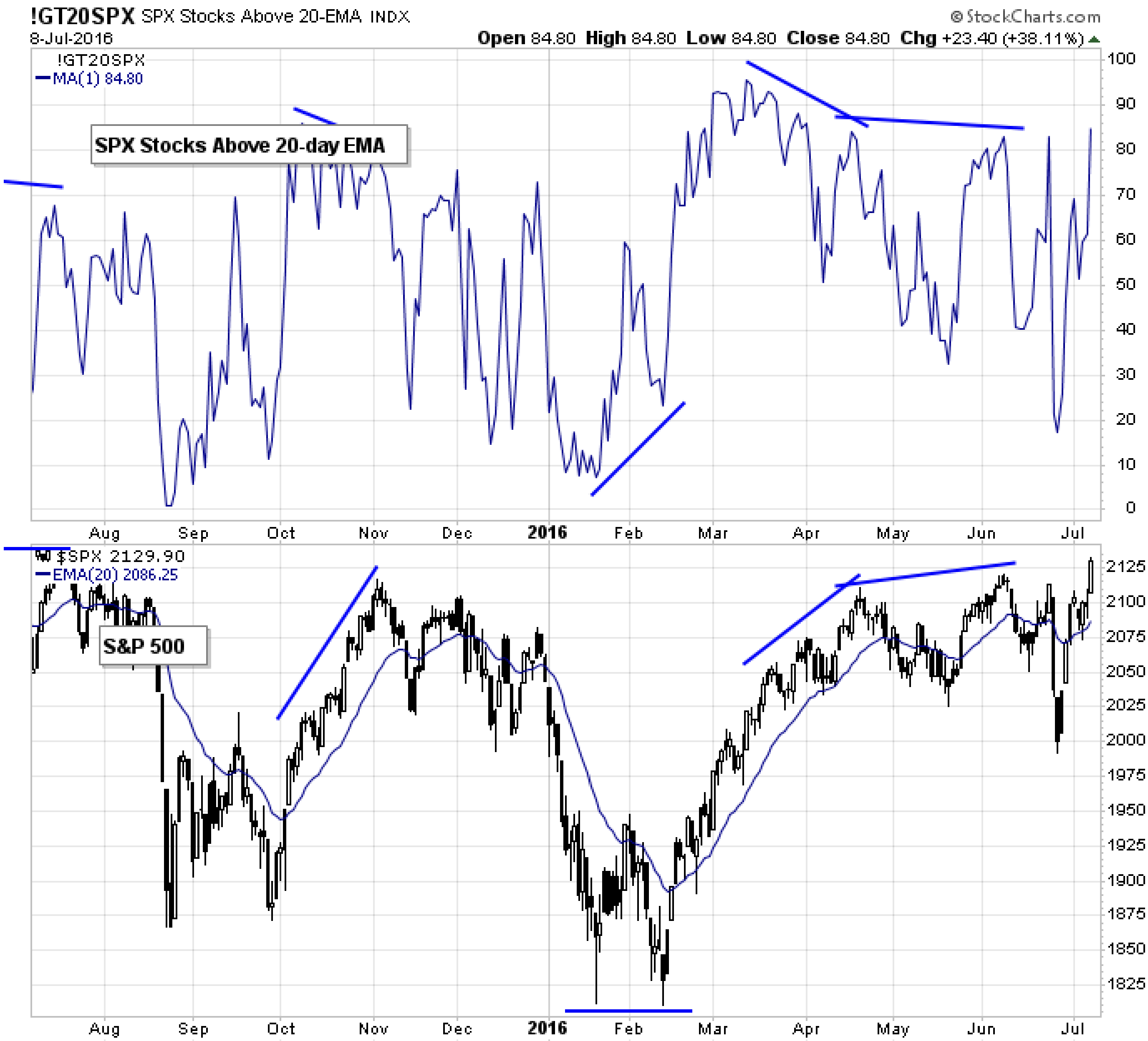
S&P 500 vs. Percentage of SPX Stocks Above 200-day MA: Here's another negative divergence among the breadth indicators. The S&P pushed to a new high, but less SPX stocks are trading above their 200-day moving averages than the last rally in early June. It's notable. Many stocks fell below their respective moving average after the Brexit vote, but not all of them have recovered.



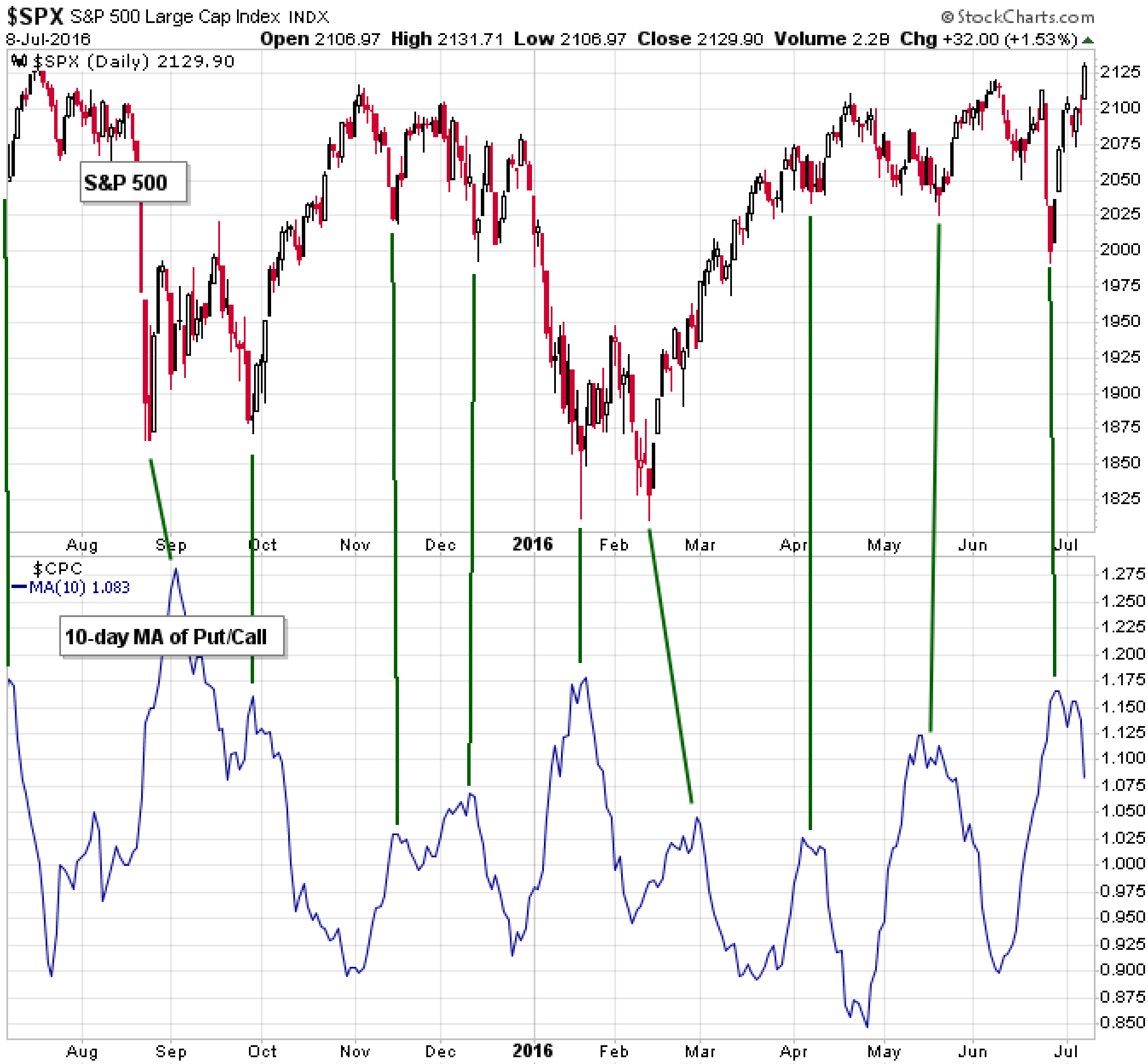
S&P 500 vs. Percentage of SPX Stocks Above 50-day MA: The percentage of SPX stocks above their 50-day MA has been weak-ish for two months, but it improved a bunch last week. With the S&P itself being about 50 points above its own MA, the fact that 73% of SPX stocks are above their 50's isn't bad. Remember, whether the S&P is at a new high is much less important than where it is relative to its moving average. Based on this, the indicator can improve some, but it isn't doing too badly.



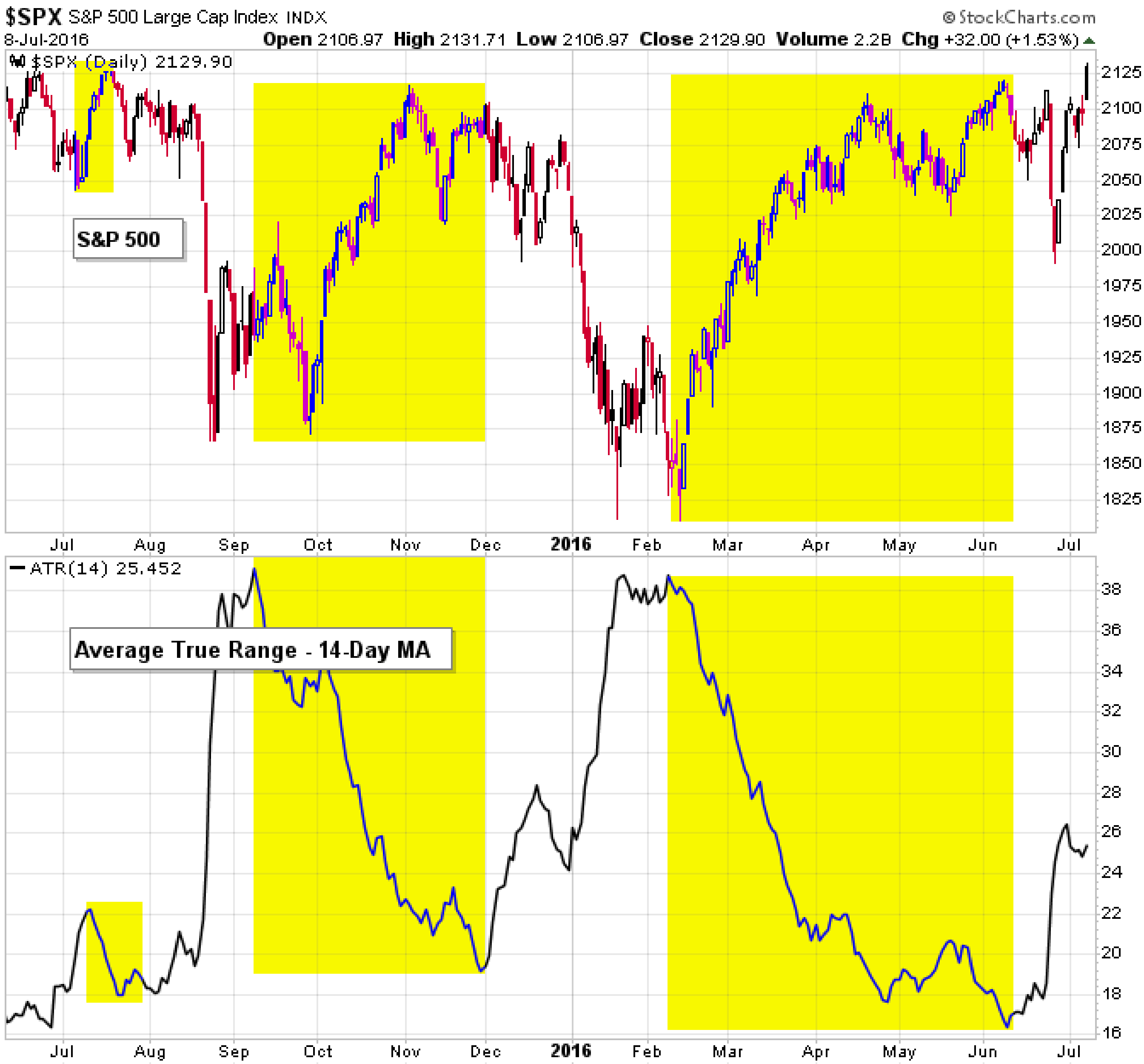
S&P 500 vs. Percentage of SPX Stocks Above 20-day MA: Shorter term, the percentage of SPX stocks above their 20-day MAs is at its highest level since April. Good enough for me.



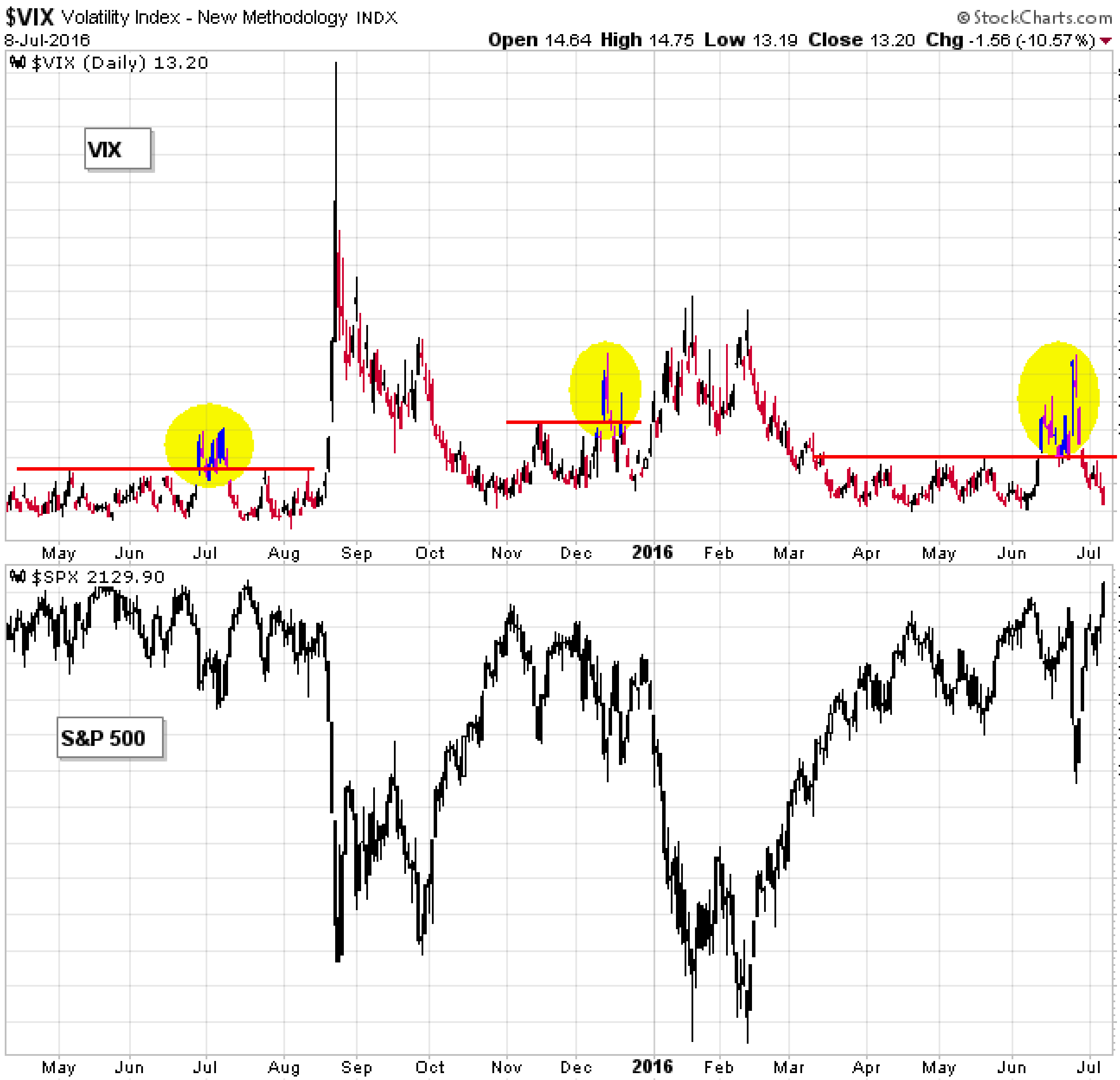
S&P 500 vs. 10-day MA of Put/Call Ratio: The put/call, which tends to move down while the market moves up, is hanging out at an elevated level. This is not what happens in the beginning stages of a rally.



S&P 500 vs. 14-day Average True Range: The ATR, a measure of volatility, which tends to drop when the market moves up, is trading more reminiscent of last December than what is normal for a strong market. To confirm a rally, the bulls will want the ATR to drop.



S&P 500 vs. VIX: I'm going to continue updating this chart because I think it's worth tracking, especially since the ATR and put/call are not yet on board with the market legging up. Previously, when the VIX spiked while the market consolidated, it led to a market correction a few weeks later.



The Bottom Line

Despite all the bad and potentially bad news out there (Brexit vote, declining earnings, massive debt levels, weak financials) the market is within a few points of its all-time high. I guess low rates, stock buy backs and a negative tone are enough to counter the negatives.

The breadth indicators are mixed but in better shape than last week. The strong (cumulative AD and cumulative AD Volume lines) are doing even better, and we got some improvement elsewhere.

This is not supposed to be easy. If you're sitting there thinking: how can the market go up given what's going on in the world, that's exactly why it can go up. The bearish tone means the bears are too prevalent and the bulls are under invested. Both groups will buy dips, and if the S&P does break out and run, both groups will chase higher.

I consider the market to be in a consolidation pattern within an uptrend, but it's very close to attempting to run. Fun times ahead. Barring very negative news, I fully expect the S&P to move up to 2300-2400. Not necessarily right now, but it's coming. You don't think it's possible? That's why it's very likely to happen.

Have a great week.

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