Leavitt Brothers

Weekly

Jason Leavitt jason@leavittbrothers.com	Sunday, December 4, 2016

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The market's idiot mode rally off the pre-election bottom has ended.

The rally wasn't a surprise - after all, the market's overall trend had been up for several years - but the one-directional nature of it was. There were no dips and almost no pauses - just steady buying to push all the indexes (except the Nas 100) to all-time highs.

Now the market is resting. In the grand scheme of things, a rest is normal and healthy and tends to set the stage for further gains. Weak longs sell and shorts re-establish positions, and then after everyone has been lulled to sleep, the market suddenly comes to life again.

I'm operating under the following scenario. The market trended up for several years. Then it traded mostly flat for about seven months heading into the election. Then, once the election passed, the uptrend re-asserted itself.

Yes there are lots of cross currents - interest rates, wars, geopolitical stuff, a change in power in Washington - yet in the end the market has continued up. If you trade or invest based on what should happen, you've probably been on the sidelines for years. But if you simply looked at the charts and admitted the trend was up, you're long and happy, even though you may not be happy with what's going on in the world. Don't let an opinion prevent you from making money or growing your portfolio.

OPEC members have agreed to cut production; it's the first cut since 2008. Oil responded with a 10% jump, and many oil stocks surged 10-30%. I've liked the group for a long time - since first going long in January, I've had exposure most of this year - sometimes big, somethings small - and continue to like it. I'm not 100% confident crude will break out and run, but at the very least we should be able to buy dips and take some profits on rallies and just keep going back to the well until it stops working. Eventually a high oil price will choke off economic growth, but we're far from that; we may be extremely far from that. For now gas prices remain low, giving people some extra disposable income for the holidays, and tempers are less likely to flair in the Middle East while OPEC members make a few extra bucks/barrel.

A rate hike at next the next FOMC meeting (Dec 14) is a virtual lock, so it's safe to say it's being priced in. There will be no surprises, but Wall Street will want to discern if this is a one-and-done situation (like last December) or if this will be the start of a new trend.

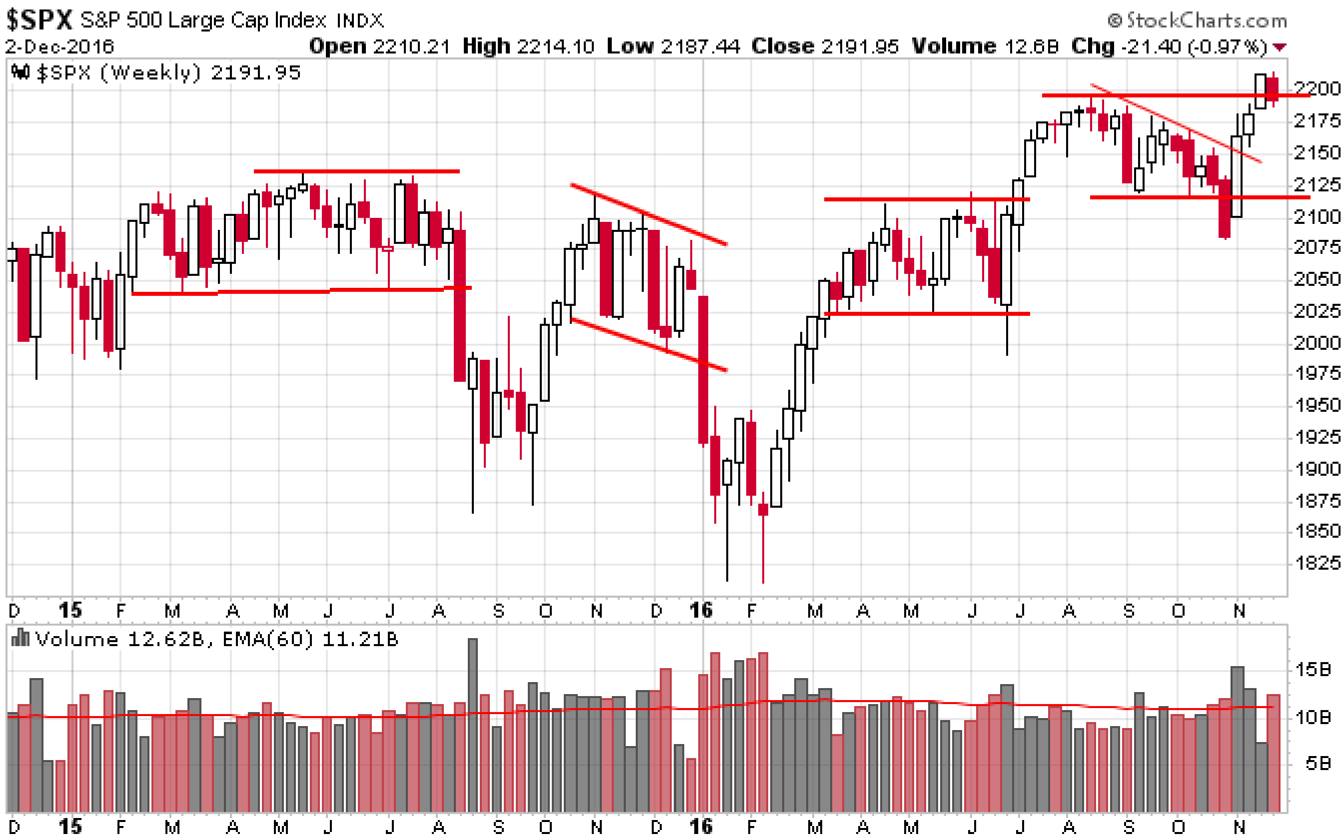
I like the market; I like what I see. But there's one thing that's starting to bother me. That's the performance of quality big-cap tech names. Facebook. Amazon, Google, Apple, Intel, Alibaba and many others are not just lagging, they're trending down below their declining 50-day moving averages. These stocks don't have to lead, but they can't lag too much. It's doubtful the market can rally much without these names at least flattening out. And unfortunately, because of their size, it will take a massive amount of buying for this to happen. This isn't a case where the charts can be painted positive. There needs to be a lot of buying for them to shore up.

Other than this, I like the market and believe after the current dip is over the indexes will regain their strength and move to new highs again in 2017. Beyond that I'm not committing to anything. I'm kind of leaning towards a blow-off rally that gets everyone excited...and then a top forming, which will last many months. For now I'm focused on the next leg up.

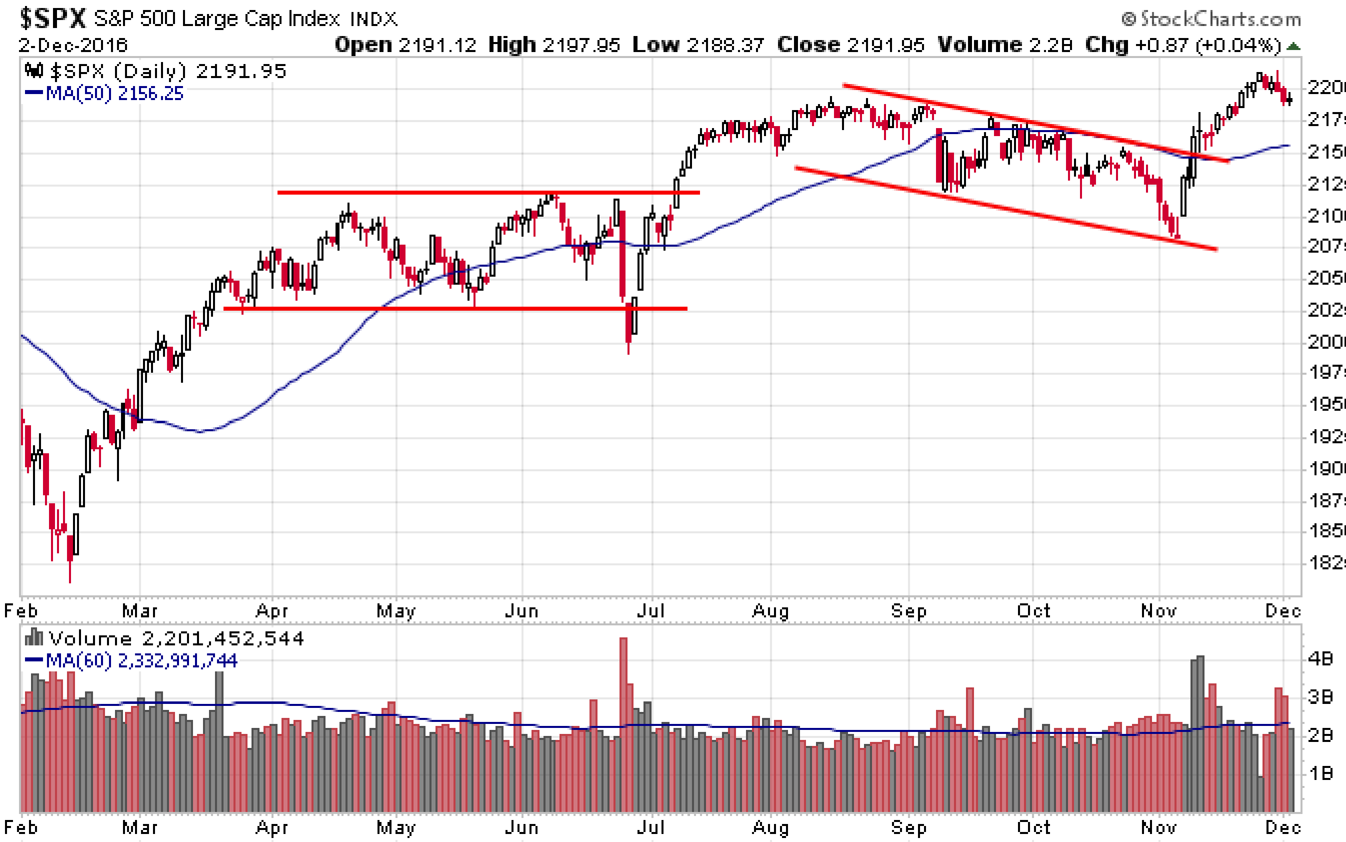
Let's get to the charts and see what they say.

Indexes

The S&P 500 Weekly: The S&P took out the low of its pattern and reversed...then it took out the high of its pattern and might be reversing again. It took so much energy just to get to the top of the pattern, there was nothing left for a follow through. Overall things still look good. Don't fight a dip in the near term.

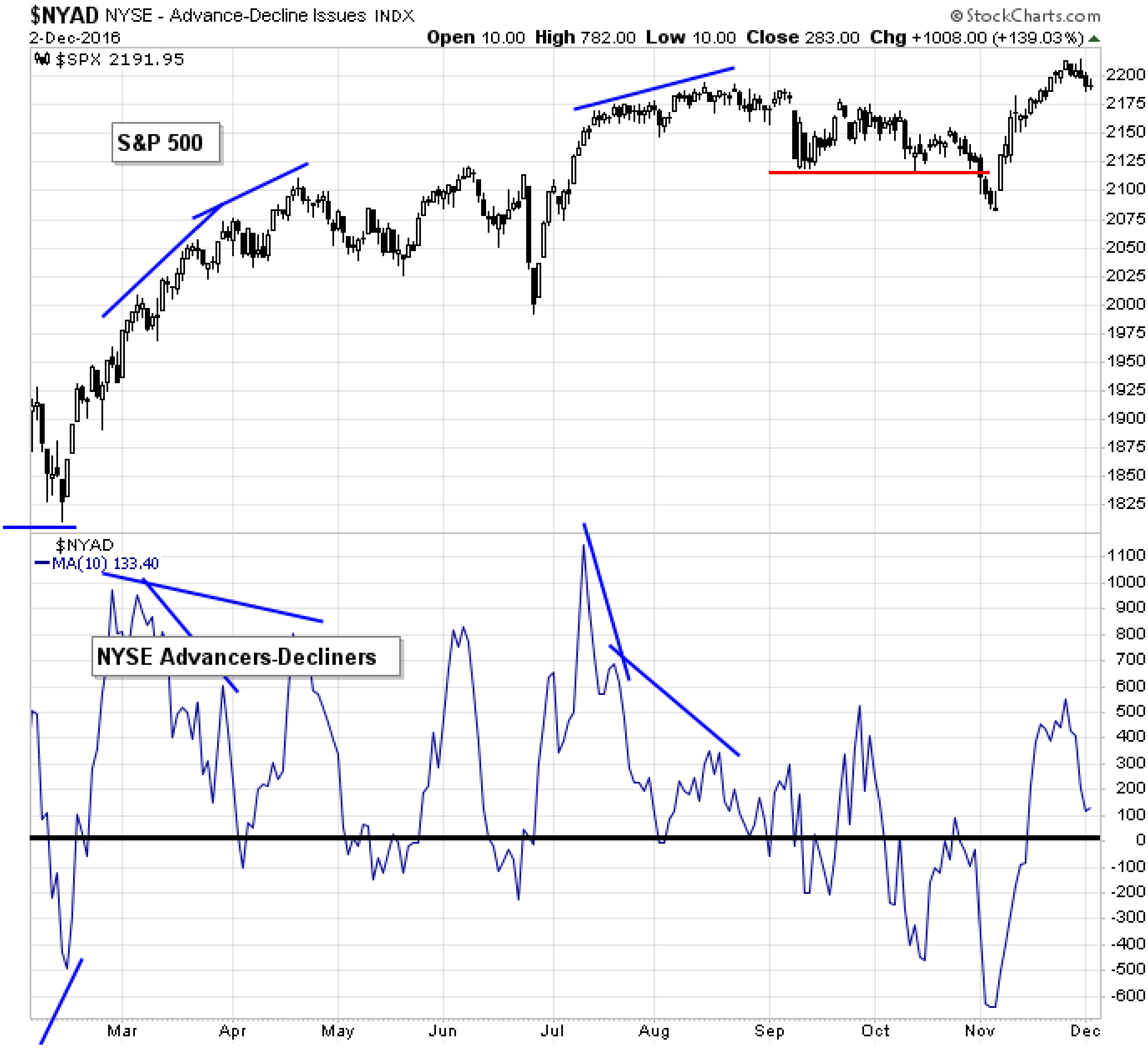


The S&P 500 Daily: The daily S&P looks very constructive. A rally starting last February led to three months of consolidation, and then a post-Brexit rally led to another three months of consolidation. The trend is obvious and undisputed; the only frustrating part has been that most of the gains have been put in place in a small number of days.



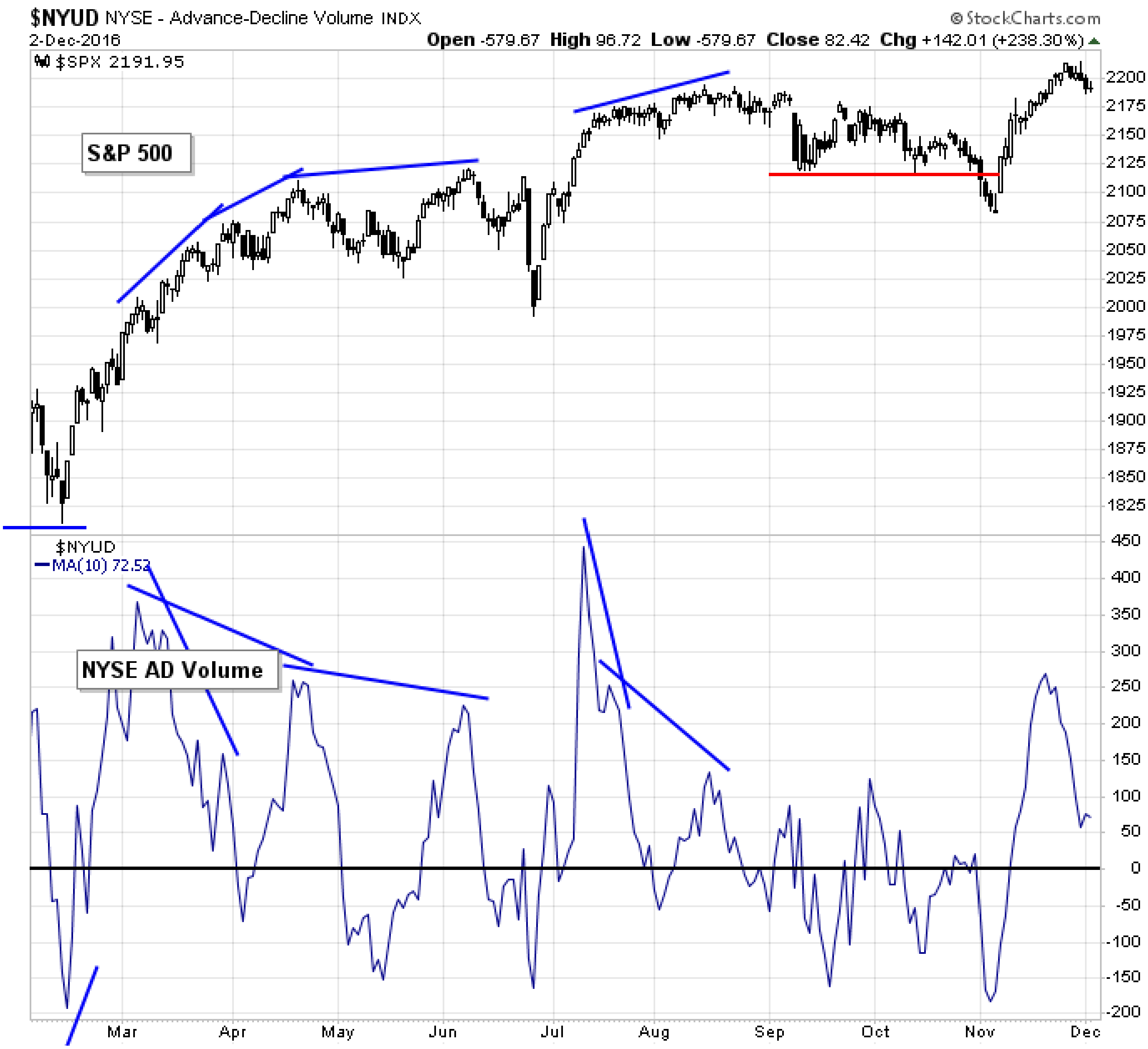
Indicators

S&P 500 vs. 10-day MA of NYSE AD Line: Three weeks of rallying prices got the 10-day of the AD line well above zero but not close to previous highs near 1000. Advancers beat decliners, but they didn't dominate. Now the AD is heading down. This is fine. Going forward let's see if it can find support near zero and then if it can move to a higher high on the market's next leg up. A negative divergence would not be good.



S&P 500 vs. NYSE Cumulative AD Line: Despite the S&P moving to a new high, the cumulative AD line could not match the move. Advancers on this most recent leg up did not dominate in the same way decliners dominated on the way down. It's notable.

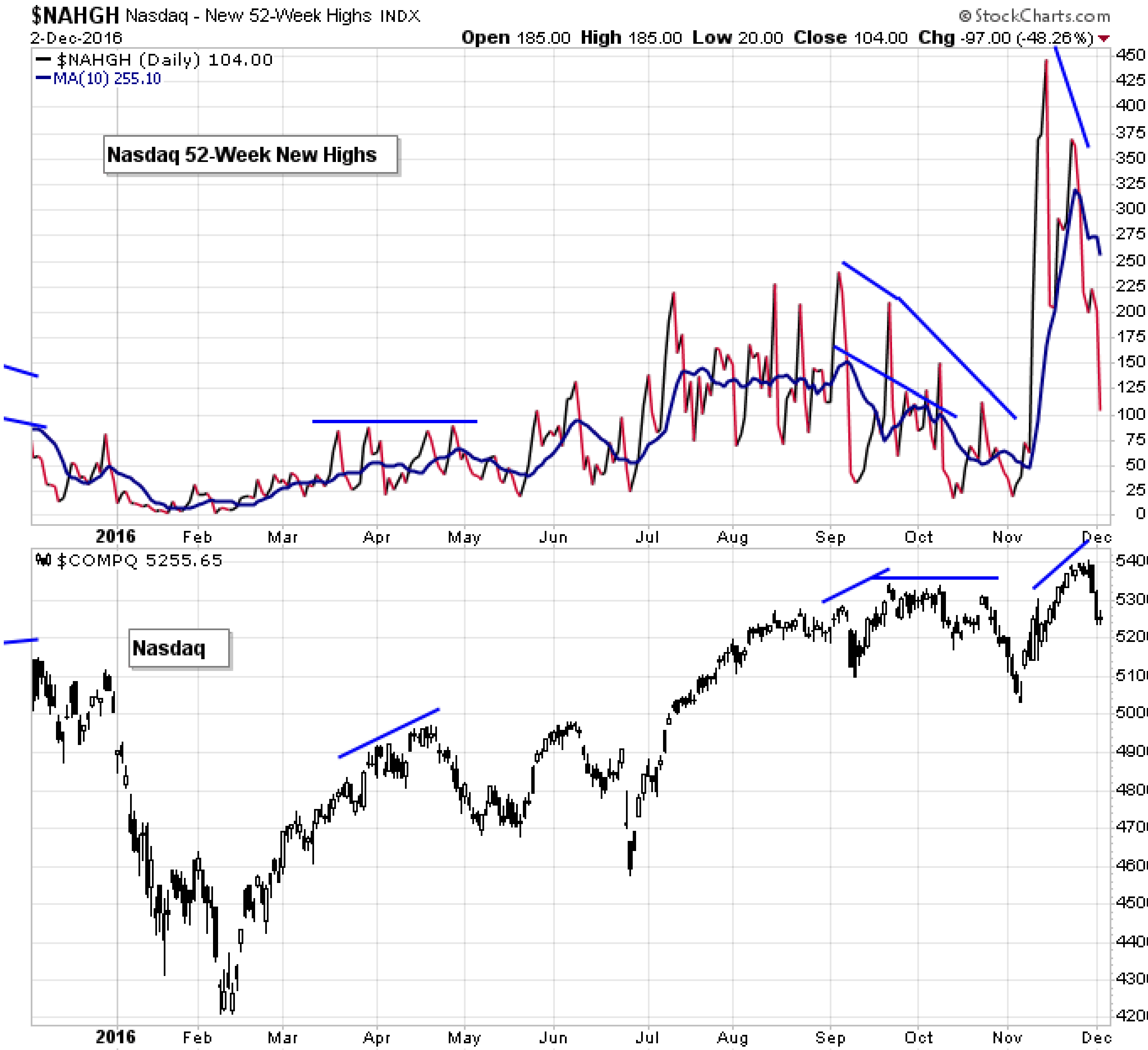
S&P 500 vs. 10-day MA of NYSE AD Volume Line: The AD volume line also could not match previous high water marks, despite the market moving vertically for three weeks. Now it's heading down. It gets more leeway with penetrations of zero. Still, a dip to zero or slightly below would be considered normal for a market correcting within an uptrend. Beyond that, a bigger dip would hint at trouble brewing beneath the surface.



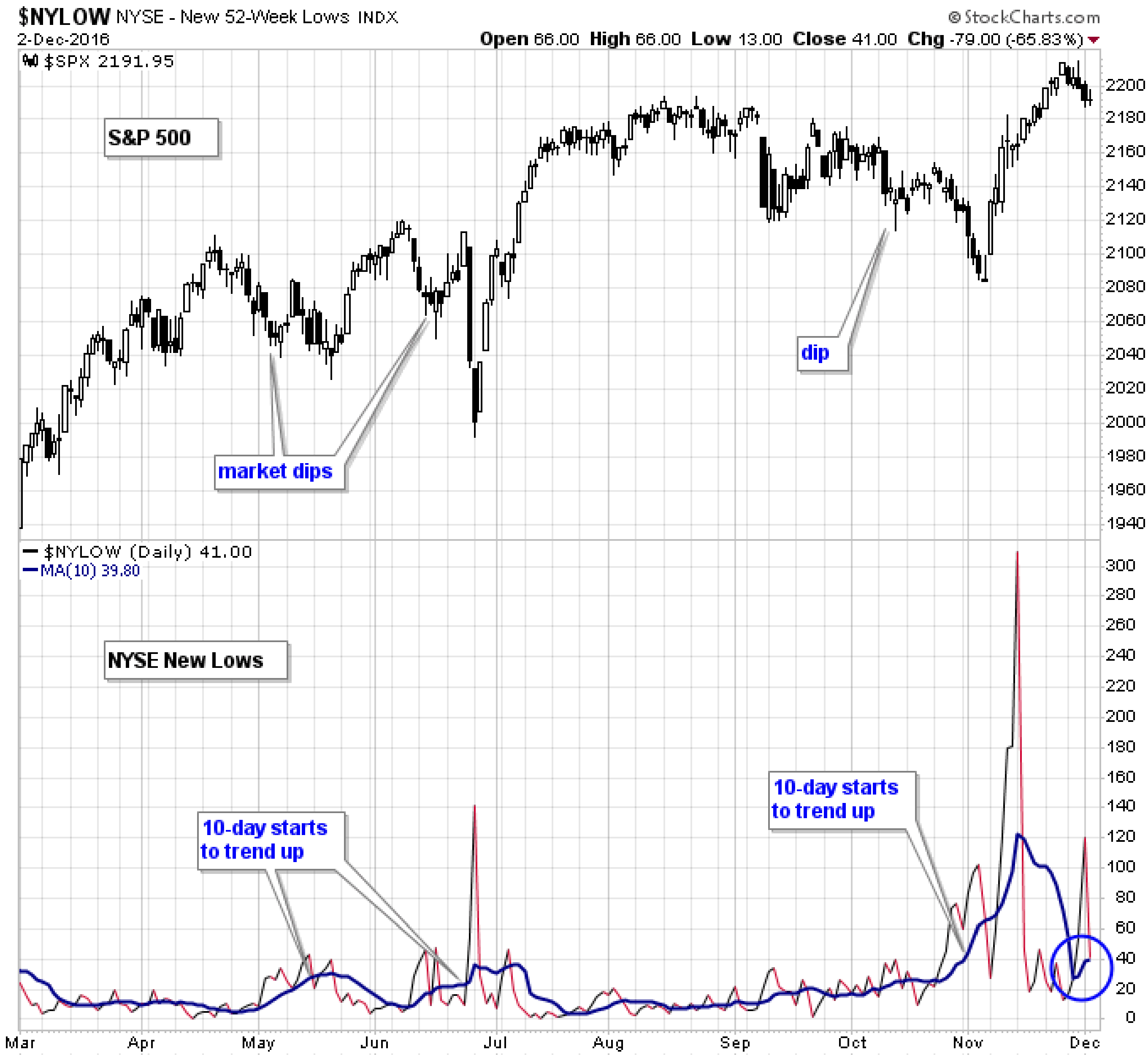
S&P 500 vs. NYSE Cumulative AD Volume Line: The cumulative AD volume line roared to a new high. Very odd considering small caps have led and [high-volume] big-cap tech stocks have been weak. This should result in the AD line being stronger than the AD volume line. It's curious.

S&P 500 vs. NYSE New Highs: New highs at the NYSE have held up. It's a good sign. Despite the market pulling back all last week, many individual stocks remain strong.

NASDAQ vs. NASDAQ New Highs New highs at the Nas diverged from the Nas - the Nas put in a higher high while the number of new highs put in a lower high - and then fell hard last week. Things are fine now, but we'll get a lot of info on the next rally attempt. Do new highs expand again? Will the 10-day (blue line) take out its previous high or diverge from the price action.

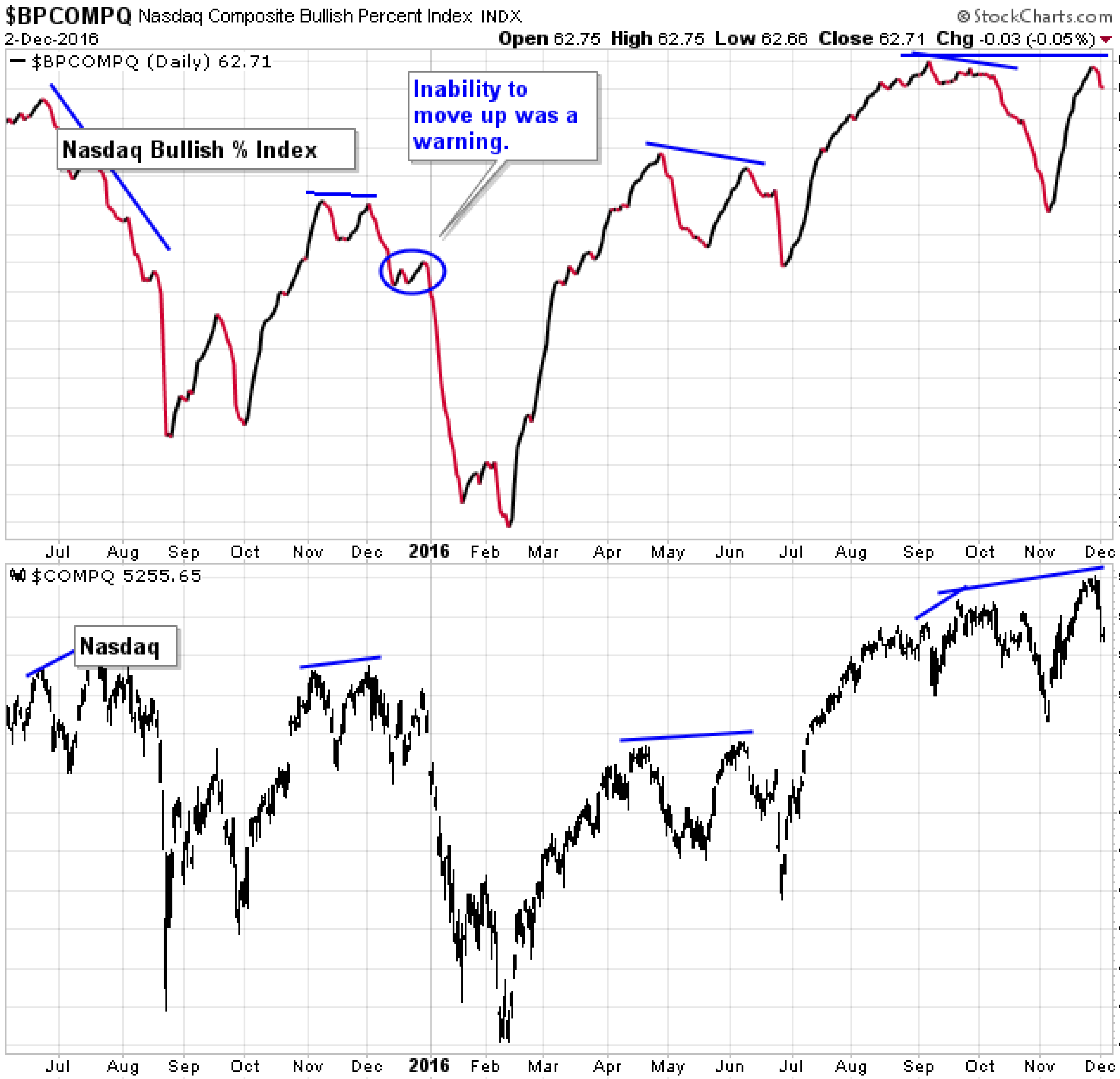


S&P 500 vs. NYSE New Lows: Despite the market only being fractionally off its all-time high, it's notable new lows have moved up. This tends to happen as a top is being formed and often leads to a correction. At the very least is a suggestion to be careful.

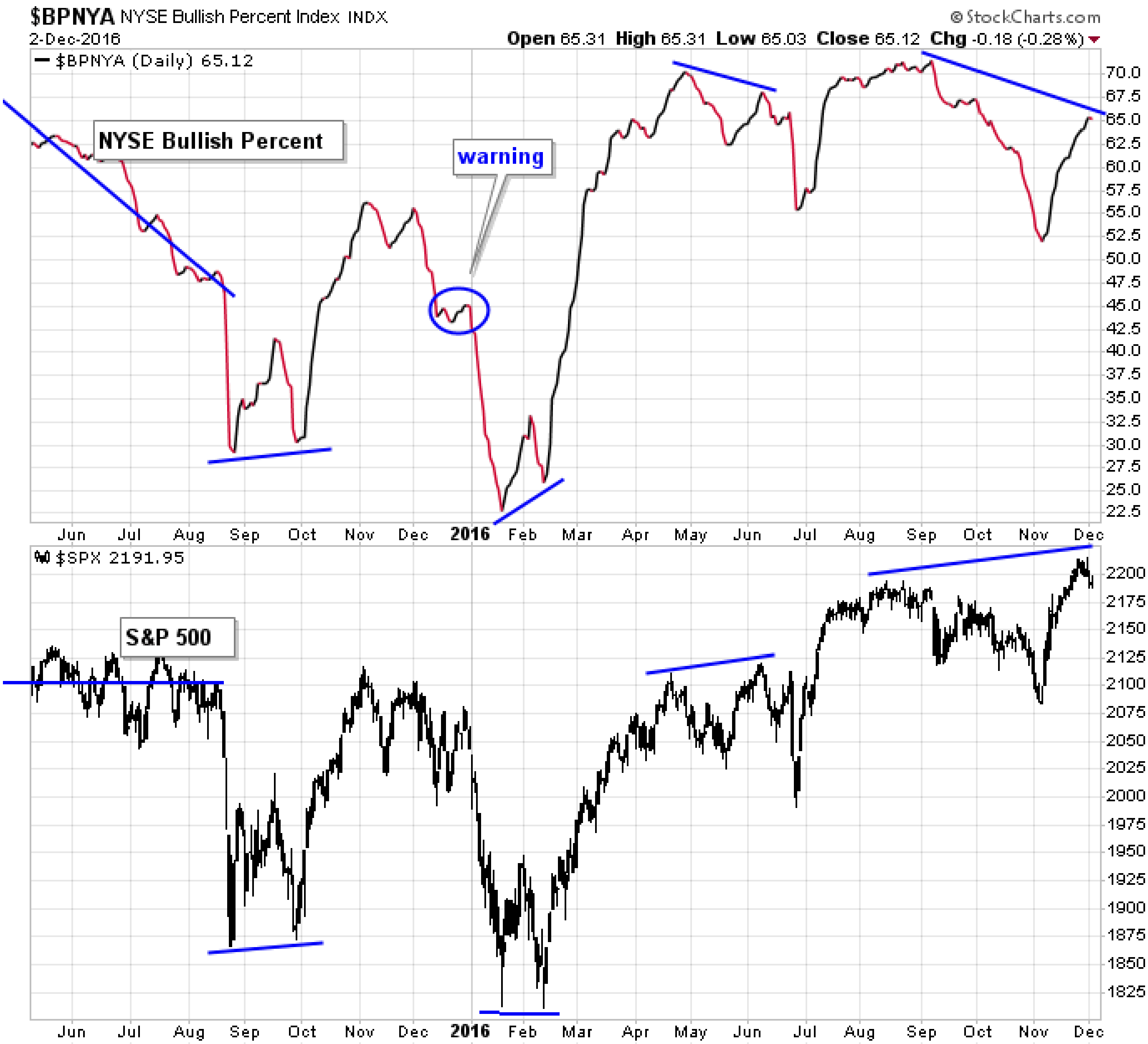


NASDAQ vs. NASDAQ New Lows New lows at the Nas have also perked up. You could argue we've already gotten a dip...but an argument can also be made the dip hasn't been big enough or lasted long enough.

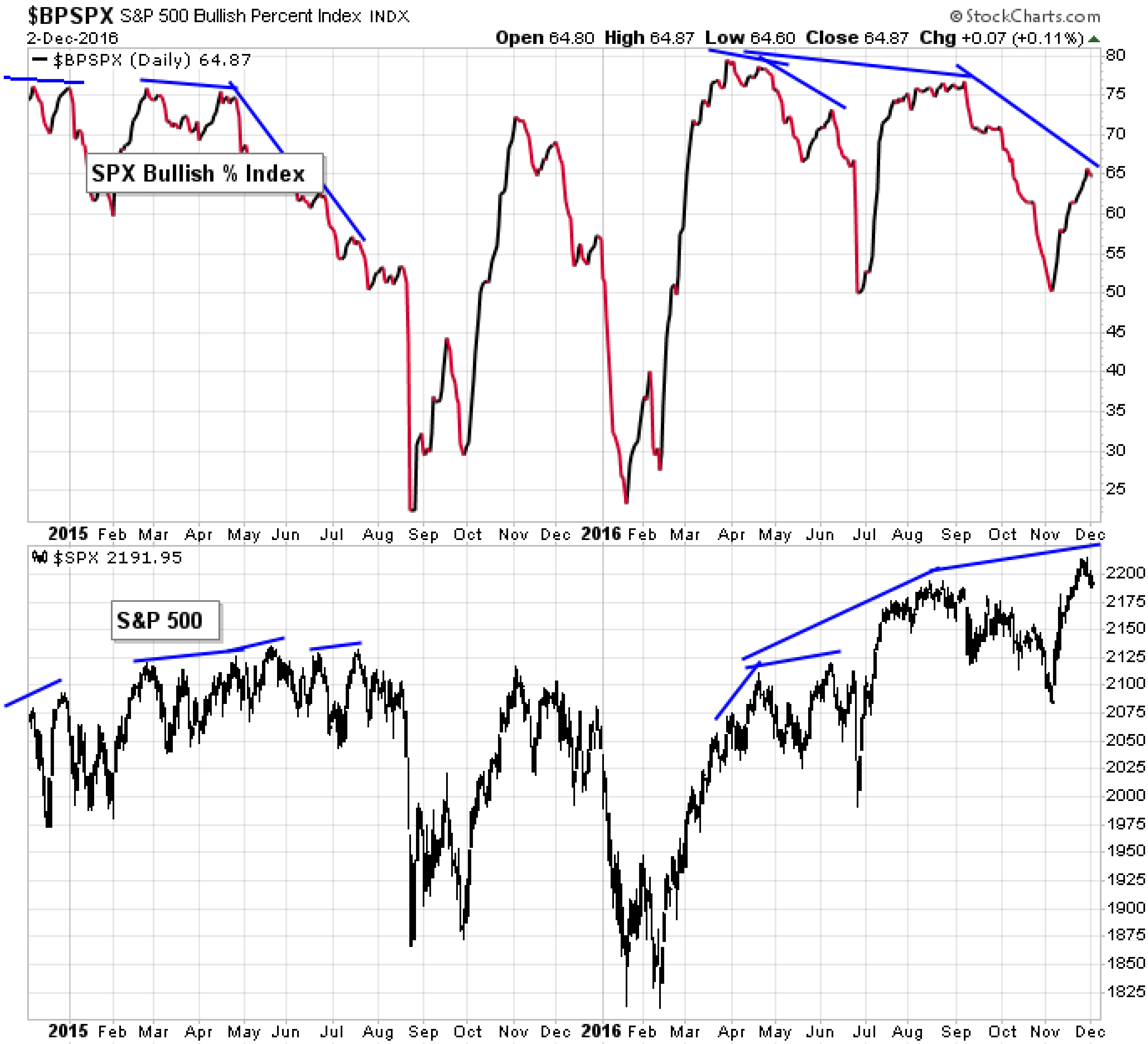
NASDAQ vs. NASDAQ Bullish Percent: The Nas bullish percent moved to its previous high, but couldn't take out that high despite the Nas itself registering an all-time high. The divergence is notable. And if you think the indicator can't mathematically move higher than 65, you don't have to go back far to see prints in the 70's.



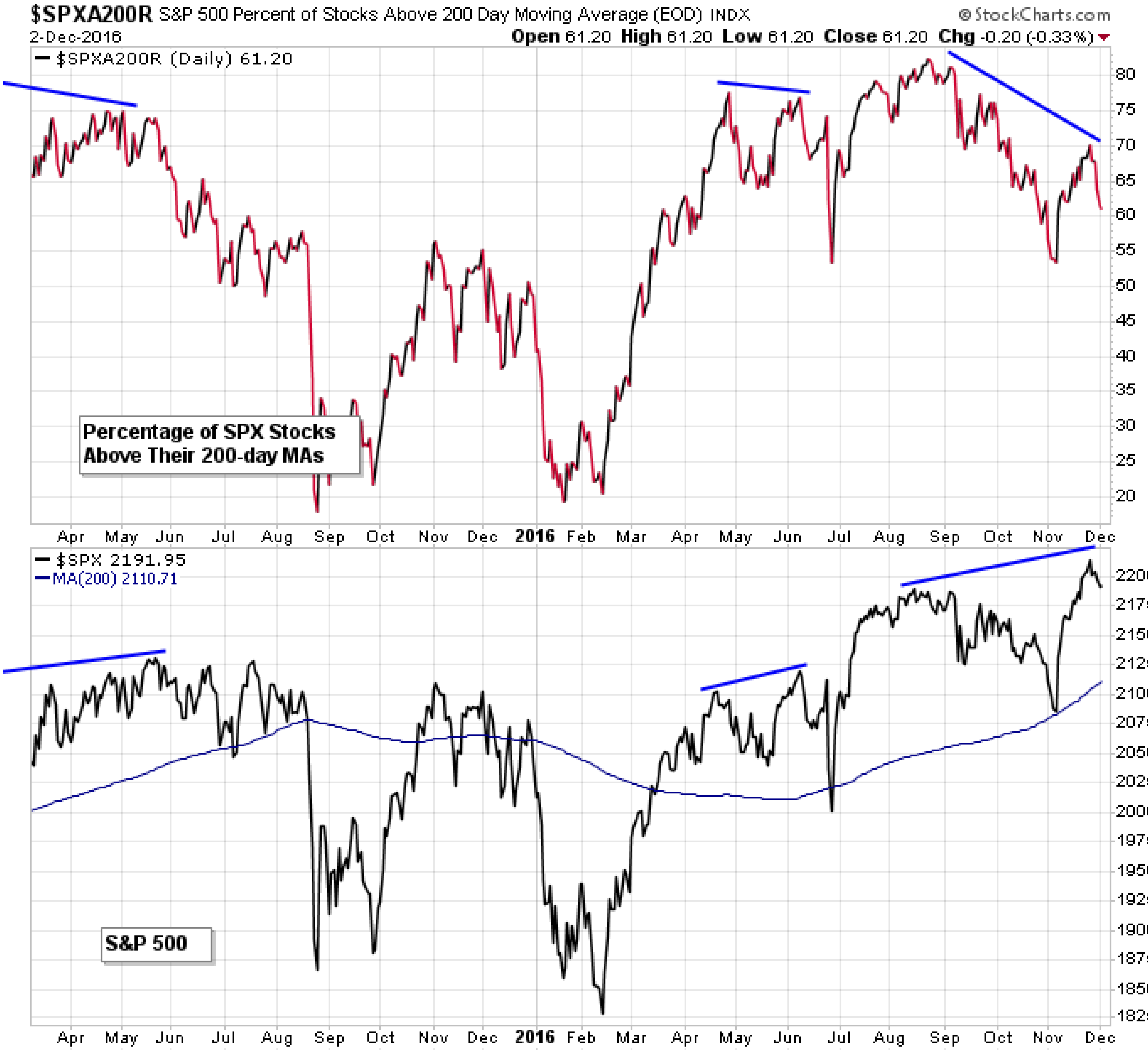
S&P 500 vs. NYSE Bullish Percent: The bullish percent at the NYSE is putting in a negative divergence. It's somewhat reminiscent of last November/December when a similarly big rally wasn't matched with buy signals from point-n-figure charts.



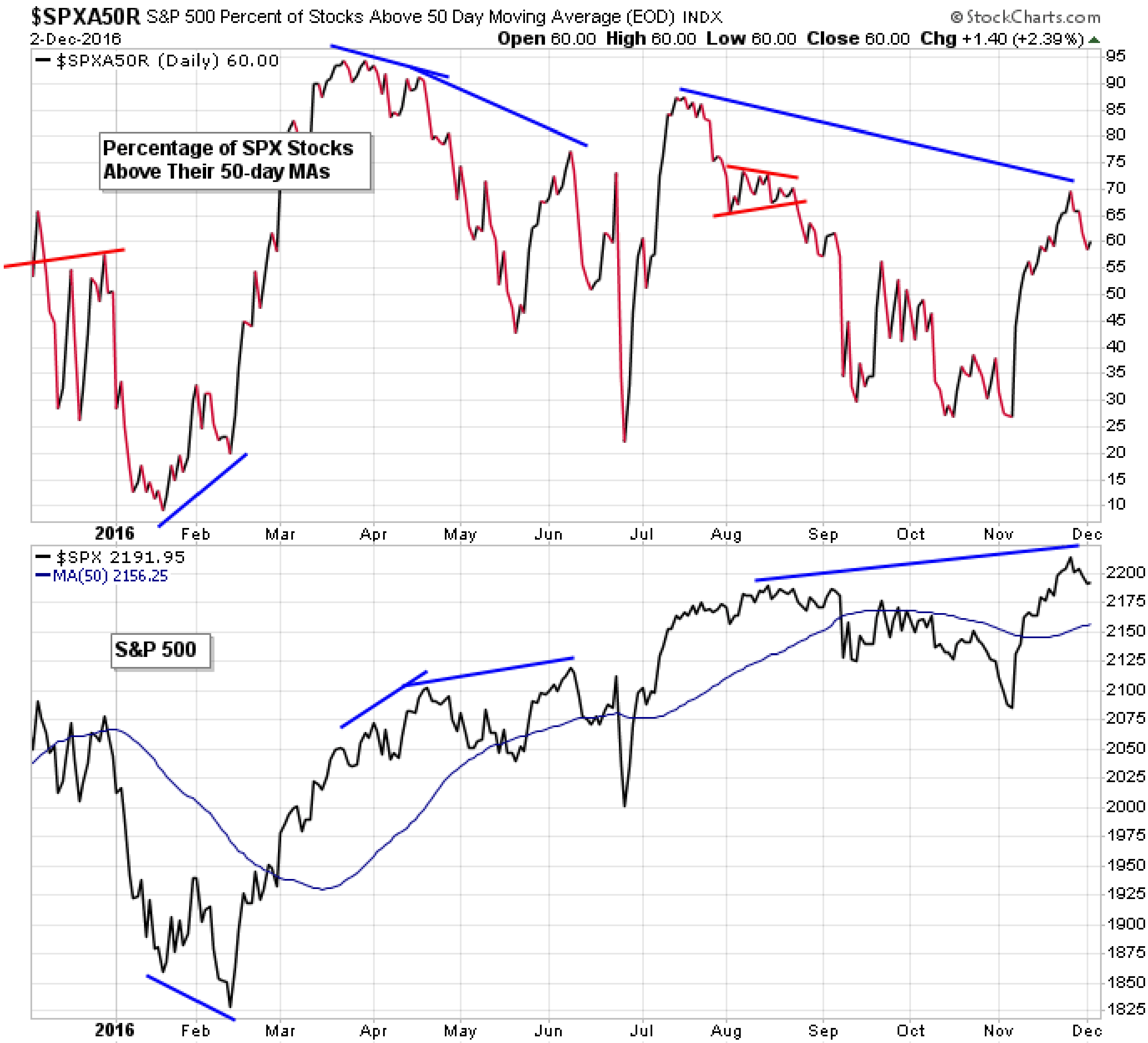
S&P 500 vs. NYSE Bullish Percent: There's also a very obvious negative divergence forming at the S&P 500.



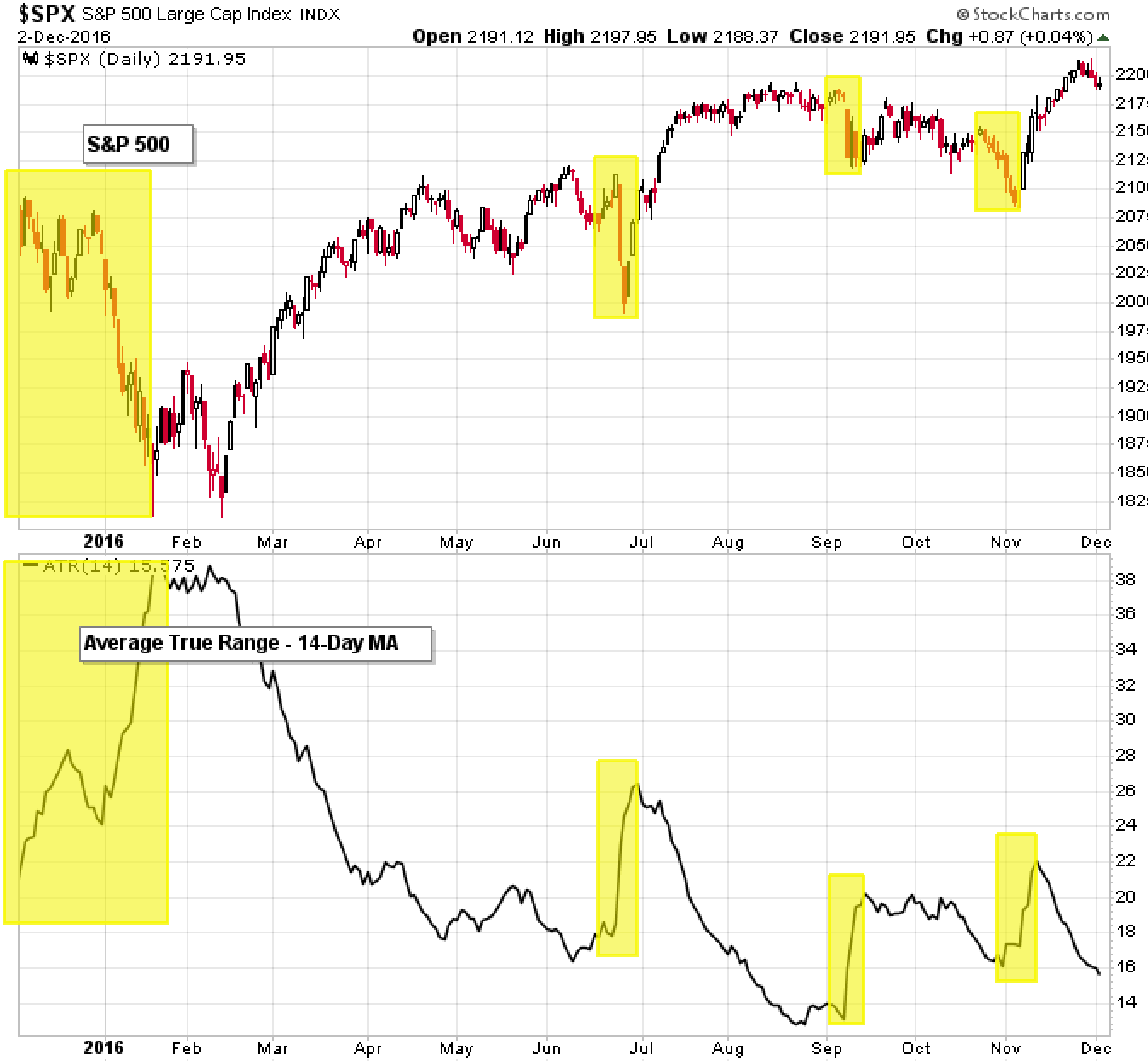
S&P 500 vs. Percentage of SPX Stocks Above 200-day MA: The percentage of SPX stocks above their 200-day moving averages has not kept up with the S&P. There's no excuse for this. If the overall market bounces off its 200 and rallies for three weeks to a new high, individual stocks should do the same, but it's not happening at the rate the bulls would like. It is definitely a warning.



S&P 500 vs. Percentage of SPX Stocks Above 50-day MA: The percentage of SPX stocks above their 50-day MAs improved a bunch off the pre-election low but still couldn't match its previous highs. Unless more stocks participate, the market's upside will be capped.



S&P 500 vs. 14-day Average True Range: The ATR continued down last week. This is a good sign for the intermediate term.



US Dollar: The dollar has been in consolidation mode. Even if it drops to 99, the previous high and the up-trending 50-day MA should bring buyers to the table.

US Dollar vs. Relative Strength of Russell 1000 vs. Russell 2000: If you're concerned about the strong dollar getting stronger, here's a chart that will give you some relief. When the large caps under-perform the small caps, which is the current situation, dollar rallies have been halted or reversed.

The Bottom Line

The market remains in good shape overall, but in the near term there are many warnings.

The AD line and AD volume line couldn't climb very high.

The bullish percent charts have formed negative divergences.

The percentage of stocks above their 200- and 50-day MAs hasn’t come close to matching their previous highs - another sign the rally didn't have broad-based participation.

Last week's rest is likely not over.

I like the market overall, but I don't like it in the near term.

Be careful on the long side. A pullback should be welcomed. It'll set up a possible end-of-year run.

Have a great week.

Jason Leavitt
Jason@leavittbrothers.com