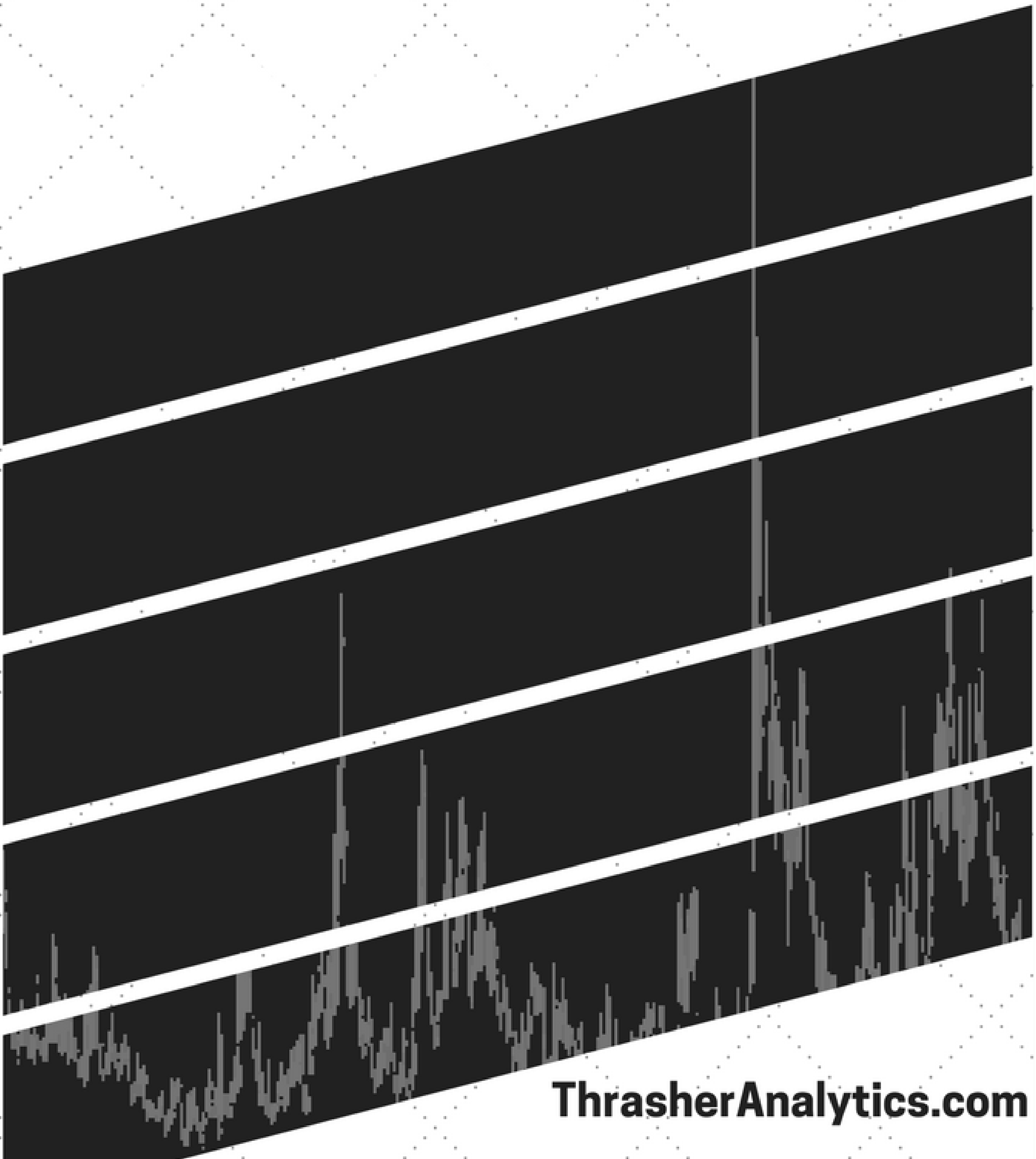
THRASHER ANALYTICS

BI-WEEKLY RESEARCH & ANALYSIS



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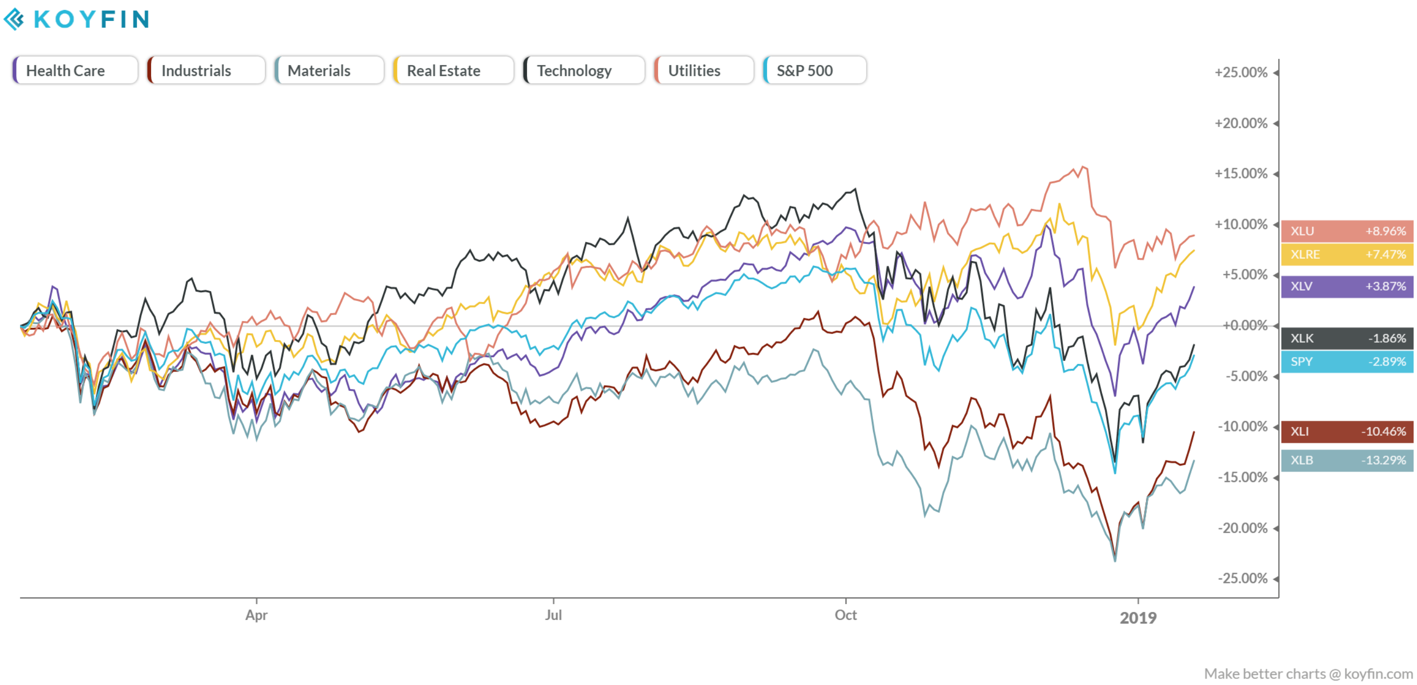
Sector Dashboard

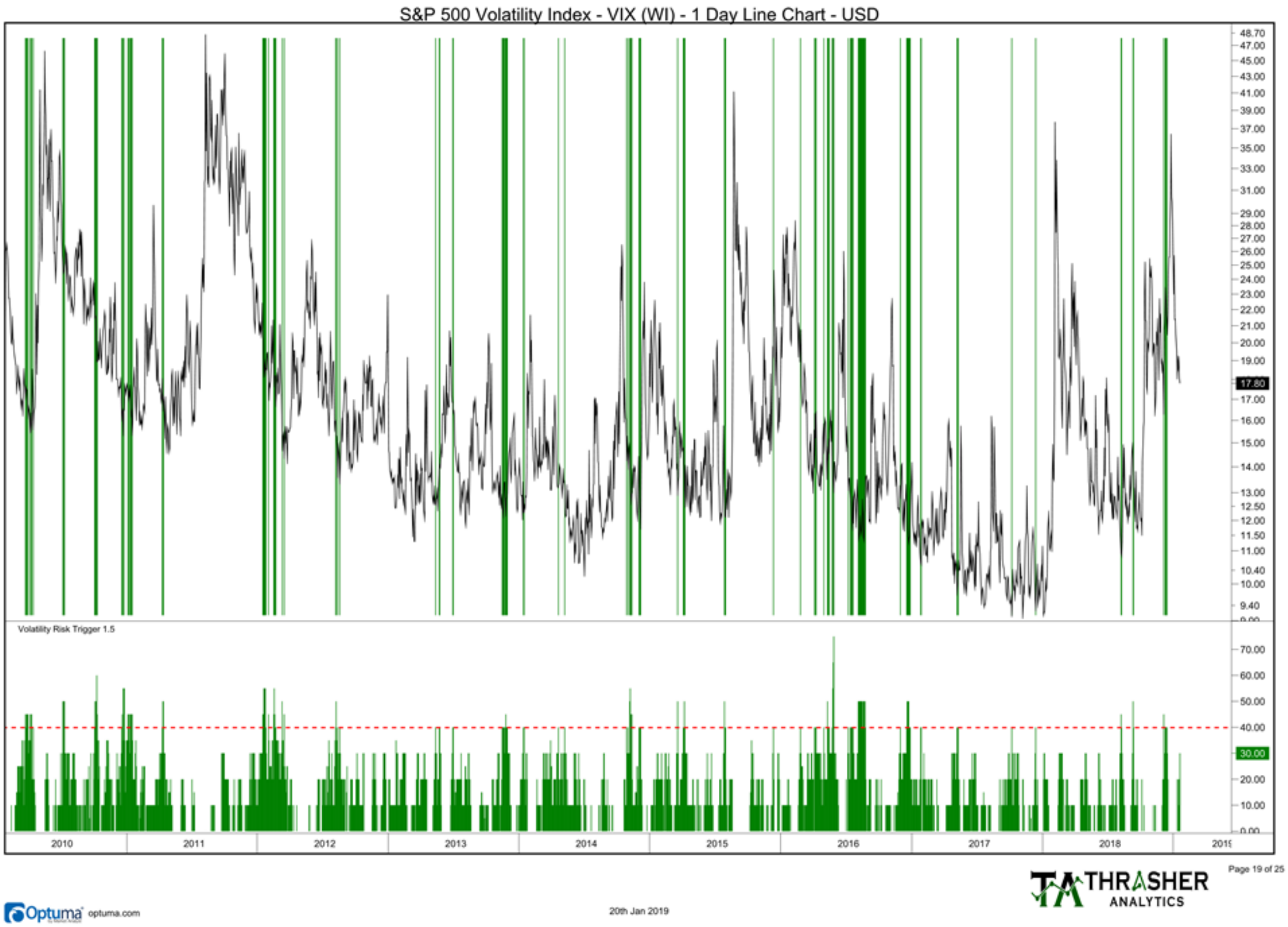


Long vs Short Sector Matrix

1D 5D MTD 1M QTD 3M 6M YTD **1Y** 3Y 5Y

	+ XLY	+ XLP	+ XLE	+ XLF	+ XLV	+ XLI	+ XLB	+ XLRE	+ XLK	+ XLC	+ XLU
– XLY	-	-9.1%	-17.3%	-12.6%	0.6%	-13.2%	-16.0%	4.1%	-4.9%	-3.1%	5.6%
– XLP	10.0%	-	-9.1%	-3.9%	10.7%	-4.6%	-7.6%	14.5%	4.6%	6.6%	16.1%
– XLE	21.0%	10.0%	-	5.7%	21.8%	5.0%	1.6%	26.0%	15.0%	17.2%	27.7%
– XLF	14.4%	4.1%	-5.4%	-	15.2%	-0.7%	-3.9%	19.2%	8.8%	10.9%	20.8%
– XLV	-0.6%	-9.6%	-17.9%	-13.2%	-	-13.8%	-16.5%	3.5%	-5.5%	-3.7%	4.9%
– XLI	15.3%	4.8%	-4.7%	0.7%	16.0%	-	-3.2%	20.0%	9.6%	11.7%	21.7%
– XLB	19.0%	8.2%	-1.6%	4.0%	19.8%	3.3%	-	23.9%	13.2%	15.3%	25.7%
– XLRE	-4.0%	-12.7%	-20.6%	-16.1%	-3.4%	-16.7%	-19.3%	-	-8.7%	-7.0%	1.4%
– XLK	5.2%	-4.4%	-13.1%	-8.1%	5.8%	-8.8%	-11.7%	9.5%	-	1.9%	11.0%
– XLC	3.2%	-6.2%	-14.7%	-9.8%	3.9%	-10.5%	-13.3%	7.5%	-1.9%	-	9.0%
– XLU	-5.3%	-13.9%	-21.7%	-17.2%	-4.7%	-17.8%	-20.4%	-1.4%	-9.9%	-8.2%	-

VOLATILITY RISK TRIGGER (VRT)



The Volatility Risk Trigger continues to be 'under construction' to a slight degree as I work on getting it recoded at Optuma. I've updates its current (albeit uncompleted) form in the chart above. A few of the underlying tools have triggered but the VRT itself is still below its threshold. The volatility futures curve has become extremely flat recently as it works its way out of backwardation following the large move higher in front month VIX contracts in December. But even with the bullish price action in equities, traders appear to remain cautious in their vol position, continuing to give premium to front month contracts relative to further out on the curve.

Broad Market Commentary

In my letter two weeks ago I shared the above chart with the note that we could see equities continue higher into the 2018 February/November area around 2600. Since then, the market has continued to rally and the S&P 500 has recovered roughly 50% of the loss since the September high.

The next level traders will be focusing on is the 200-day Moving Average (red line) which currently resides at 2741 for the S&P 500. The RSI has taken out its prior counter-trend highs set in November and December, which is a positive development as helps diminish the potential for a bearish range being formed in momentum had the indicator been unable to get past the 55(ish) level.

Volume has been below average for most of the move off the December low until Friday. However, Friday was an option expiration day, which can inflate volume data beyond “normal” trading activity. With that, I’d like to see some more above average positive days as a sign that institutions have in fact returned to equities and are assisting in pushing stocks higher.

Comparing The Recent Move Higher to Market History

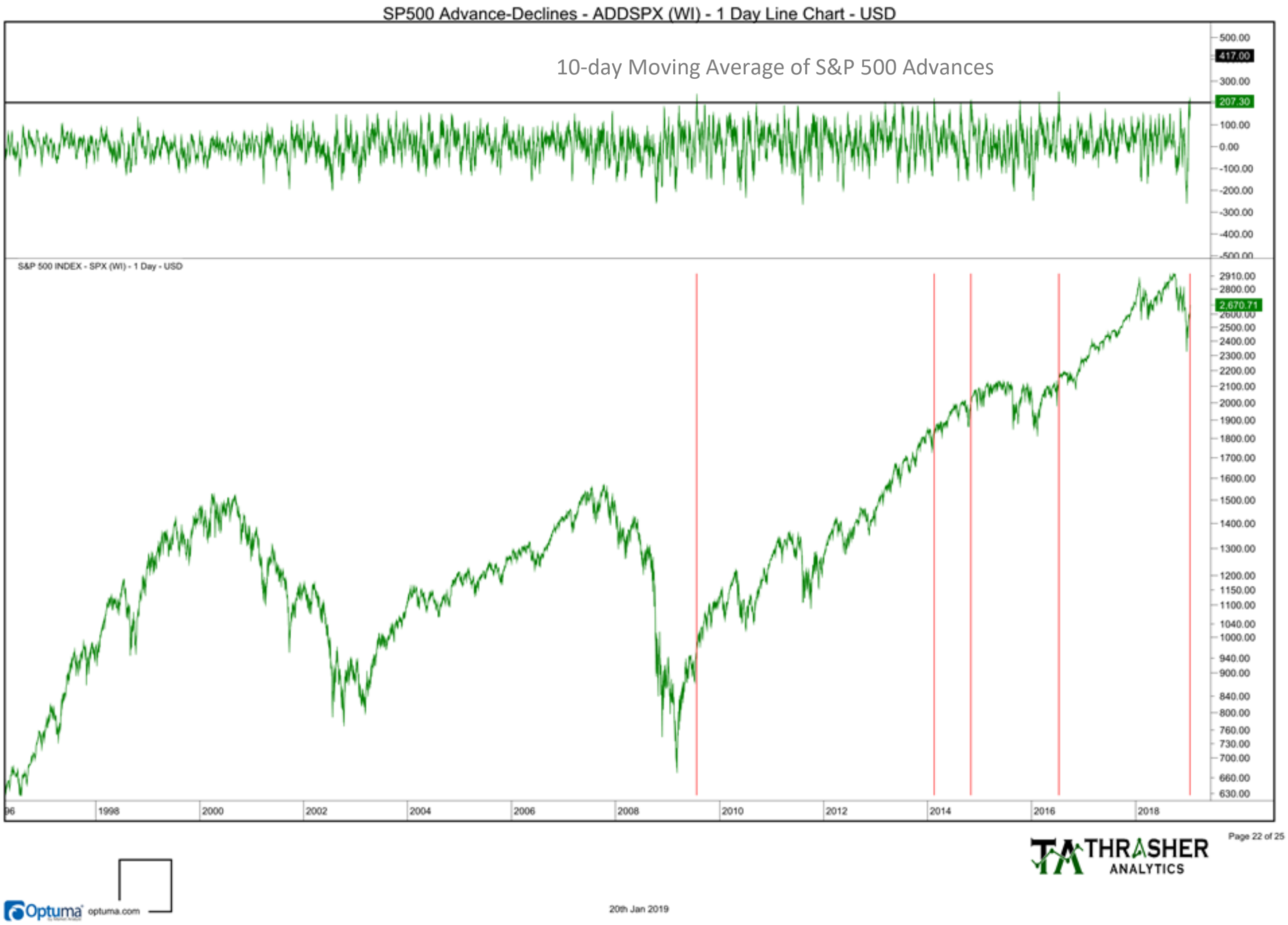
U.S. equities have had a solid run over the last 17 days, with the S&P 500 rising over 13% off the late-December low. To put the move in context I've built a study (shown above w/ green vertical lines) going back to 1950 when the S&P 500 has risen by over 13% in 17 days and the z-score slope is greater than 2, meaning the 1-month slope of the S&P 500 is two standard deviations greater than the slope of the index over the prior 100 trading days.

While this is a fairly narrow study, it's something we've seen occur at several important lows in market history. In fact, the last time the market moved this much, this fast was off the March 2009 bottom, and before that was in 2002, which was preceded by several instances during the dot-com bear market, right after the 1998 decline, then again after the 1990 down trend and in 1982 and 1974

Taking this study a step further, only a few of these occurrences occurred under the 200-day moving average, meaning while the market was still in what many would classify as a down trend then we're left w/ the '74, dot-com bear market, 2002 low, and 2009 low. In '74 equities did retrace a large chunk of the initial move off the low, the three occurrences in 2001 and 2002 saw the market move higher for a few more weeks before continuing to move lower until September 2002, with the occurrence in October '02 being after the bear market bottom but still saw a retrace to make a higher low. And of course we know what the market did in 2009.

So when still below the 200-MA, many of the past similar price moves saw some backfilling but not right away. This would suggest we may not be completely out of the woods yet, but an argument could be made that we may not see an exact retest like in '74, when the market declined and made a higher low before continuing to trend higher

The Number of Advancing Stocks Rises to Near Record Level



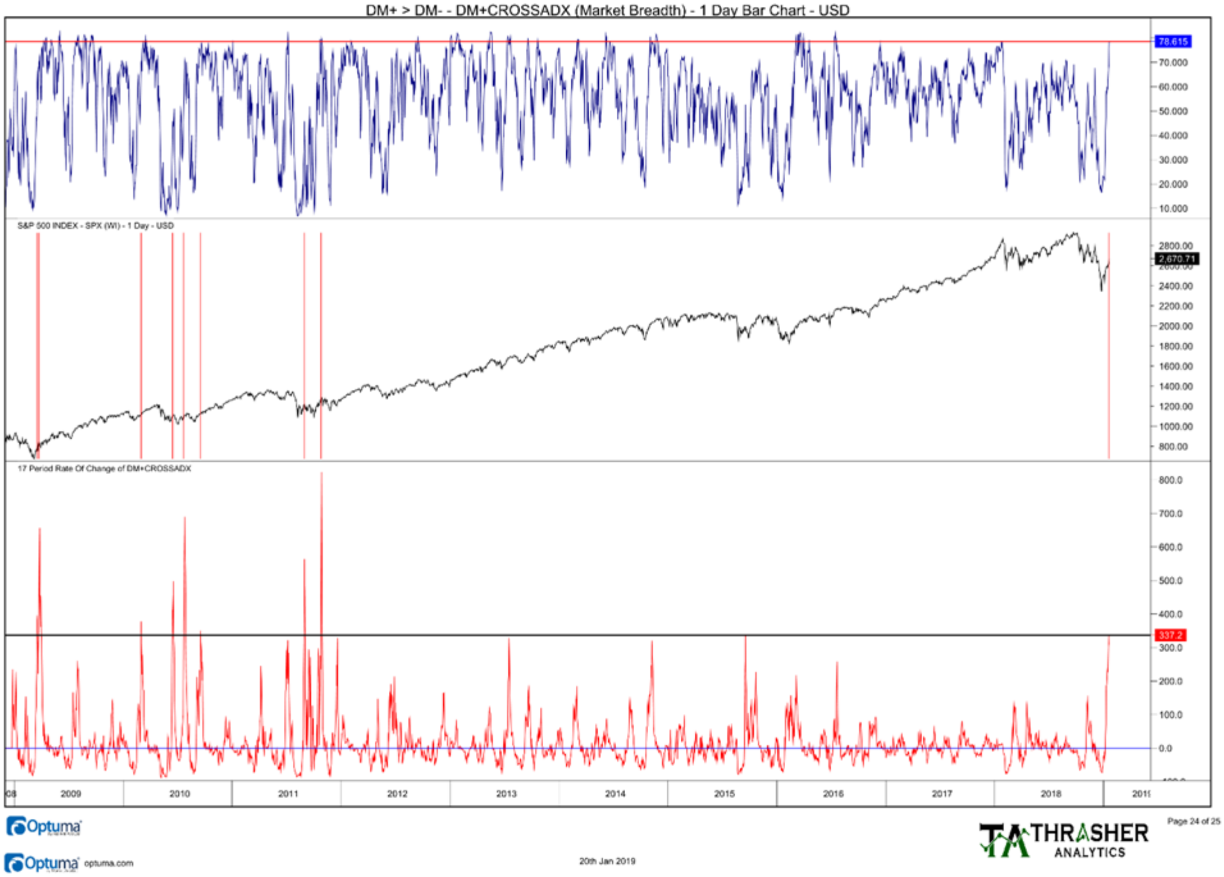
The above chart shows the S&P 500 with the top panel displaying a 10-day Moving Average of the number of advancing S&P 500 stocks. Going back to the early 90s, there have only been four previous occurrences of this many stocks rising within the S&P 500 as measured by a smoothed 10-day MA. Each of these examples saw the market continue to move higher, with no immediate retest or backfilling occurring. Based on the strength of the internals, this would give additional weight to the belief the market has made an important low.

Strong Rise in % of Stocks Above 20-day Moving Average

Continuing the analysis of the strong move off the December low, the above study takes a look at another view of the market breadth, this time at the percentage of S&P 500 stocks trading above their 20-day Moving Average. While less focused on the actual percentage of stocks above the short-term MA, the bottom panel charts the 17-day rate of change of the breadth data. Having going from less than 1% of the S&P 500 above the 20-day MA to 94% as of Friday, that's a huge move that occurred in less than a month.

So looking back since the 90s, there's been just five previous instances where the % of stocks above their 20-day MA has risen this much over just 17 days. Three of them occurred during the whipsawing action of the 2008 bear market, again after the first 2011 low and finally after the first low in 2015. Each of these occurrences saw the market continue to move lower (2008) or retest the first low of the down trend (2011 and 2015). This gives some credence to the idea that while the move off the Dec. low was strong, with broad participation, the market could still backfill and retest the prior low or create a higher low.

Large Rise in Positive Trend Strength



Like we just did with the rate of change of the % of stocks above the 20-day MA, we can also look at the degree in which S&P 500 stocks saw their trend strength flip to bullish, as measured by the DM+ rising above the DM– of the ADX trend strength indicator, which will dub 'trend breadth.' The top panel of the chart shows the percentage of S&P 500 stocks with a bullish ADX reading (DM+ greater than DM-), which as of Friday was at 78.6%, a level that's been reached numerous times since 2008. In the bottom panel I've shown the 17-day rate of change, which has hit its currently level just a handful of times since the 2009 low.

In early '10 the market continued higher for several months until the 'flash crash' down trend which saw several large rises in 'trend breadth' but saw some short-term weakness soon follow. Then again we had the 2011 double bottom with a sharp move in 'trend breadth' before the second low and again two months later before a higher low was put in.

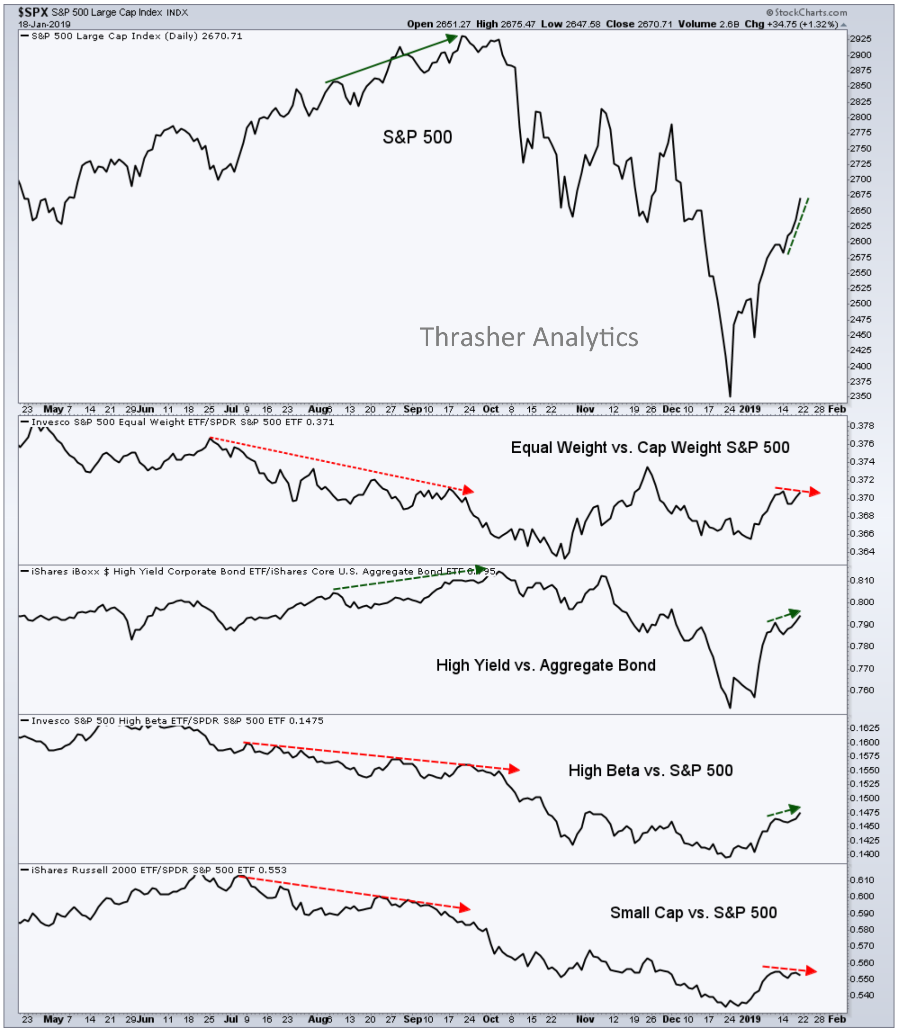
It's now been several years since 'trend breadth' has seen this kind of strength in just a short period of time. With a small sample size, similar to the past few charts I've shown, the market did experience a few retests and a higher low before the up trend was continued.

Where Do We Go From Here?

As I've shown, the data is fairly mixed on historical market behavior based on how stocks have traded off the December low. In my prior letter I noted the extremely bullish reading in the number of advancing stocks on January 4th and that historically we saw a rally continue in equities but that we still saw a rest after the same bullish breadth thrust occurred after the initial '11 low. Knowledge Leaders Capital did an interesting study of past instances of the market declining 15% in a "waterfall" like pattern, meaning no counter-trend rallies and found 20 such examples. The average rally retraced 57% of the downtrend (a little more than we've retraced currently), counter-trends bounced on average 11.9% (we're at about 14% right now) and 100% of the examples saw a retest of the initial low or at least a higher low formed (as in Dec. '02). The most recent examples they noted were 2011, November '08, October '08, and December '02. December 2002 and 2011 also match up with the first chart I showed with the study of slope and rate of change of the move off the December '18 low. Which leads to continue to hold a degree of expectation that this move higher won't be straight up without some form of backfilling and pot'l retest occurring. As I said in my last letter, I continue to be opened minded to let the price action dictate my bias but I believe it's important to recognize historical market action and recognize the potential outcomes that could play out in the next few weeks. So where do we go from here?

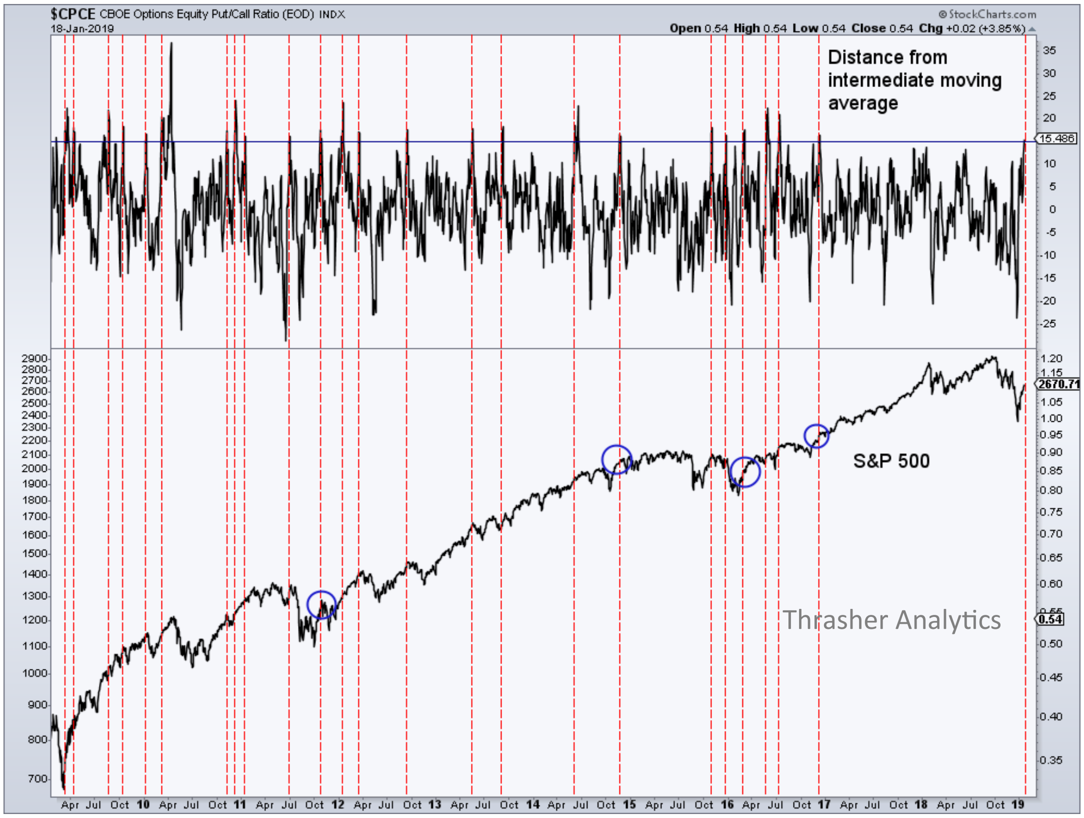
As of Friday, the 100-day MA, the 200-day MA, and the 1-year average for the S&P 500 are all clustered around 2736-2741. When we see clusters like that it can create a magnet for price but also a tough wall of resistance to get past. We saw this happened in December '15 too off the Sept. '15 low the market moved higher into the moving average cluster before continuing lower into early '16. In 2011 after the retest in October the S&P rose into the 200-day MA before sinking in November to make a final higher low before moving higher into March 2012. That type of price movement makes sense to me and also lines up with a few of the VRT triggers being met, which means we could see stocks continue to rise a little while longer before sellers step back, forcing some give back of these gains before a higher low or retest is formed. We'll see what happens.

Equity Risk Appetite



The current picture of risk appetite looks fairly supportive for the latest move higher in stocks. High yield and high beta are both show confirmation for the higher highs in the broad equity market. However, it appears the trend in stocks is leaving some smaller companies behind. The equal weight and the small cap relative performance has begun to diverge slightly. We'll need to see some more price action to get a better feel for how risk appetite is shaping up, but at this point things look like they are doing alright, and breadth (not shown) has been supportive as well.

Big Decline in Equity Options Put/Call Ratio



Put/Call ratios can be quite noisy so I treat it like other piece of sentiment data, focusing on it when extreme levels are reached. With the strong advance in equities, traders have been showing a lack of interest in owning puts, sending the put/call ratio lower, creating a large gap between the 5– and 60-day moving averages, which is just a simply way of looking at a smoothed version of the ratio and it's relation to recent past, as shown in the top panel of the chart above. The red dotted lines indicate past occurrences of the 5-day average of the put/call ratio falling below the 65-day MA by at least the amount as of Friday.

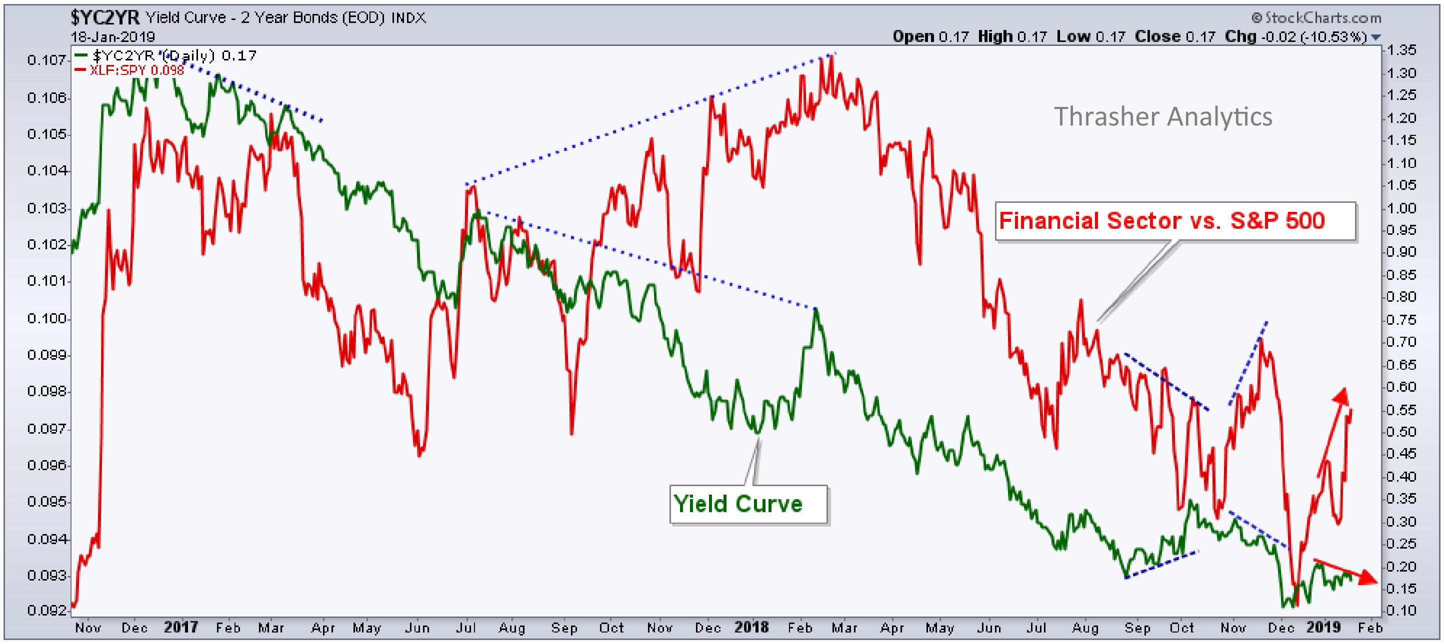
As you can see this has happened quite often since the 2009 low. The specific dates I want to focus on are the 2011, 2014, and 2016 examples. These are when the put/call ratio saw a large move coming off a significant down trend, similar to what's taken place in the market recently. 2011 saw a higher low soon follow, 2014 saw stocks move higher and then trade sideways into 2015, early '16 saw stocks continue higher as did late-2016. While the sample set as a whole provides a mixed picture of what stocks did soon after, some seeing mean-reversion lower, others preceding trends higher, Looking at past down trends shows us the market was able to ride this bullish sentiment higher, which each ('11, '14, '16) seeing stocks move higher.

Short-Term Breadth Has Begun to Diverge

While we've seen a great move off the December low, with broad participation of individual stocks, the rise in breadth has begun to lose some steam. The top panel shows the 2-week Moving Average of the NYSE Advance-Decline Line and the bottom panel is the 5-day total of new highs being made on all the major exchanges. Both of these indicators began to decline several weeks before the September high. Being short-term in nature (specifically the top panel 5-day MA of the A-D Line), they can provide a quick look into the participation level of the market within a trend.

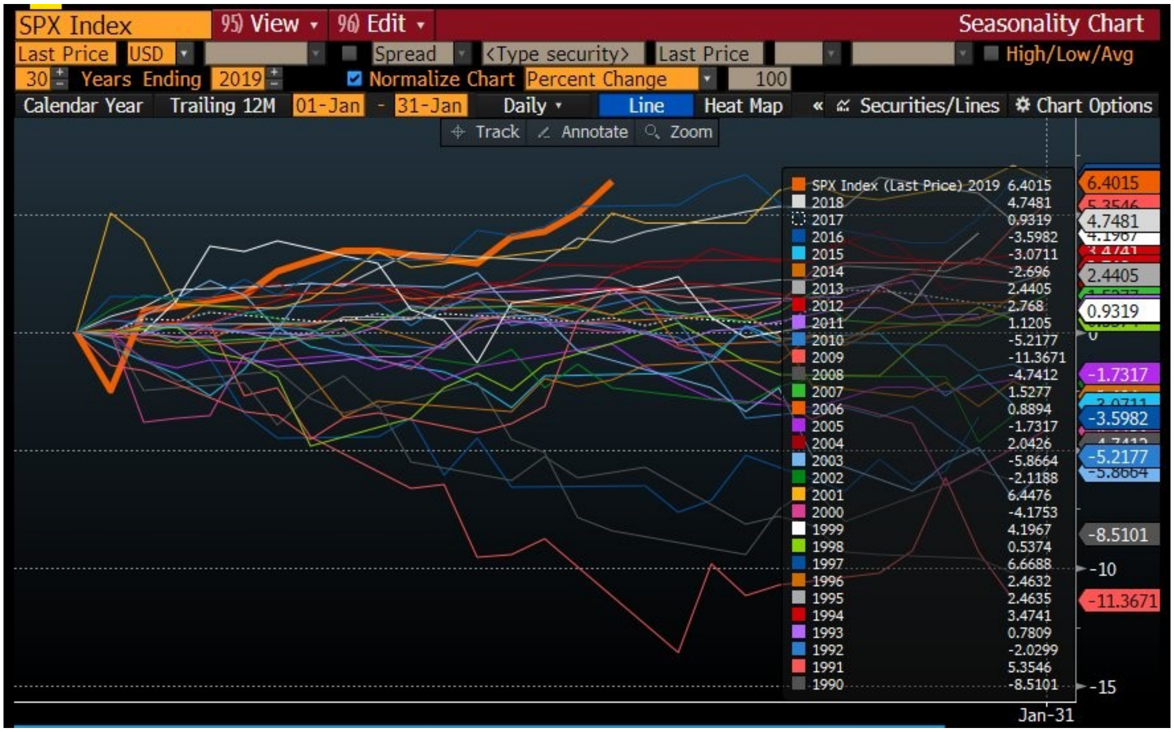
As the S&P 500 made a continued move up last week a lower high was made in the A-D Line and the 5-day total of new highs began to turn flat. This suggests that the bullish price action since Wednesday has been on the back of fewer (notably mega cap) stocks. While the divergences are extreme in duration or degree, I felt they were worth mentioning as stocks may be getting a little exhausted since the Dec. low and markets may not in fact move in a straight line back to 2900 as many would like to hope for.

Yield Curve Is Not Confirming the Strength in the Financial Sector



Once again we have a divergence being built up in the strength in the financial sector relative to the trend of the yield curve. The last time I discussed a divergence here was in early December before we saw a large move lower in relative performance of XLF vs. the S&P 500. Since then, financials have rallied again and most recently seen relative performance improve on the back of several bank earnings announcements. However, the yield curve has not seen the same level of strength, having actually made a lower high since late-December. While earnings season can provide some jet fuel for individual equities, the broad trend of the fixed income market will continue to be important for the financial sector and bulls will want to see the yield curve steepen soon to give some confidence that the recent strength in XLF will not be short-lived.

Extremely Strong Start to 2019



The above chart comes from [Pat Hennessy, CMT]() who shows the YTD performance for the S&P 500 over the last 30 years, with 2019 being in orange. The first three weeks of the year has been one of the strongest on record (at least over the last three decades). Just last year traders were noting the extremely strong January move in equites and 2019 has basically said "hold my beer" as it out-paces 2018, Pat noted that we've hit the 6.5% level a week before we did last year! With that, we all remember how that strong January finished out, with the VIX-explosion in February and a quick move lower as mean-reversion took hold and washed out some of the stretched indicator readings we were experiencing back then. That's not to say we repeat the 2018 move but I find it quite interesting that we've already bested last January within the first three weeks.

DISCLAIMER: