November 17, 2018

10:28 AM EST

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Inside this issue

Intro to Canaries in the Coal Mine

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Let me start Canaries in the Coal Mine (CCM) Q4 2018 by explaining how it works and why it is important for our newer readers. First, there's nothing extra special, super secret or proprietary involved. You can look at the same charts I do for free online on Yahoo or Stockcharts. CCM is a simple way to assess the long-term health of a bull market. It doesn't forecast, predict or do anything timely other than warning us that a bear market is approaching.

Bull markets do not end and bear markets do not begin when all is healthy in the stock market. There are always warning signs. The problem is that sometimes, warning signs come and go without any downside. However, like with hurricanes, I would always rather be too prepared than not prepared.

After the Q1 correction, I pounded my fist at every juncture, TV segment, newsletter and blog post that the bull market was absolutely not over and that new, all-time highs were coming. I was so confident because at the January peak, all of the canaries were alive and reasonably healthy. Bull markets do not die when the canaries are still breathing.
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As many of you know, I have gone to a quasi online calendar so you can book an appointment when you want to and not just when we're in the office or respond to your email. For now, I do not include evening meetings nor early morning ones, but I will try and accommodate as best I can.

If you would like to schedule a meeting, Skype, FaceTime or call, please click on the link below and give it a try. My calendar is now open through November.

https://schedulewithpaul.as.me/

Don't forget about our blog, **www.investfortomorrowblog.com** for shorter-term analysis.

You can sign up to receive notifications when a new blog has been posted here.

http://www.investfortomorrow.com/BlogAlerts.asp

Index Canaries Breathing Easily

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Let's start with the major stock market indices. I have listed the Dow Industrials, S&P 500, S&P 400, Russell 2000 and NASDAQ 100 in sequence. The CCM analysis doesn't care about any price action other than what's happening at new highs. That's the only place where warnings are given. I intentionally created the charts to allow you to view all of 2018 so you could see how well everything looked at the January peak and be able to compare that to the most recent high on the right side of the chart.

As you scroll down, I want you first to just focus on the left side in January. You can see that all five major stock market indices made new highs at roughly the same time, the pillar of health and sustainability.

Now, start the scroll again but focus on the most recent new highs on the right side of the chart. Basically, all major indices were behaving fine with the exception of the Russell 2000 Index which peaked about a month earlier. While that's a warning sign, it's not a serious one nor anything like what we saw at the peak in 2000 and 2007.
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Equities
Other Intervals
IBM
1
5
60
Daily
Tick
(DIA - SPDR DOW JONES INDUSTRIAL AVERAGE ETF,D) Dynamic,0:00-24:00
Dow Industrials
270.00
268.00
266.00
264.00
262.00
260.00
258.00
256.00
254.00
252.00
251.57
250.00
248.00
246.00
244.00
242.00
240.00
238.00
236.00
234.00
232.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec
2018
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Published by eSignal (www.esignal.com)


Equities
Other Intervals
IBM
1
5
60
Daily
Tick
(SPY - SPDR S&P 500 ETF,D) Dynamic,0:00-24:00
S&P 500
294.00
292.00
290.00
288.00
286.00
284.00
282.00
280.00
278.00
276.00
274.00
272.00
270.75
270.00
268.00
266.00
264.00
262.00
260.00
258.00
256.00
254.00
252.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec 2018 Feb Mar Apr May Jun Jul Aug Sep Oct Nov
Published by eSignal (www.esignal.com)

Equities
Other Intervals
IBM
Daily
Tick
(MDY - SPDR S&P MIDCAP 400 ETF,D) Dynamic,0:00-24:00
S&P 400
375.00
370.00
365.00
360.00
355.00
350.00
345.00
340.00
337.29
335.00
330.00
325.00
320.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec 2018 Feb Mar Apr May Jun Jul Aug Sep Oct Nov
Published by eSignal (www.esignal.com)


(IWM - ISHARES RUSSELL 2000 ETF,D) Dynamic,0:00-24:00
Russell 2000
Published by eSignal (www.esignal.com)

Sector Canaries Warning

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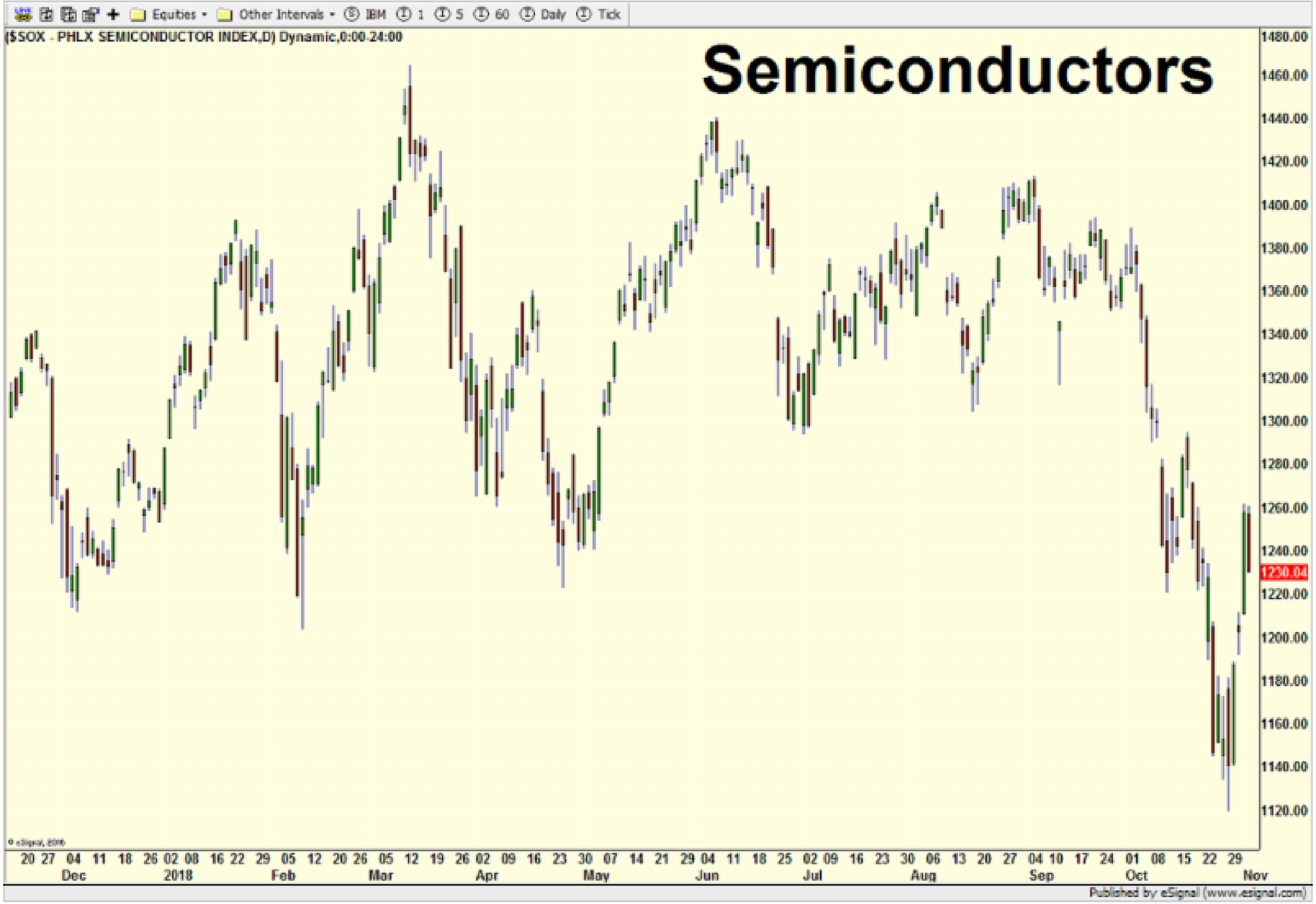
Now that you have the idea of how the CCM work, let's turn our attention to my four key stock market sectors with the same analysis in mind. First, you can see that new highs were made in all four sectors around the January peak, a pillar of health and sustainability.

However, at the most recent high, semiconductors and banks were already in downtrends and not looking so hot while consumer discretionary and transports were doing just fine. Banks and semis are vitally important to the survival of the bull market. If they don't right the ship sooner than later, I will become more concerned about a much larger decline in stocks.



Equities
Other Intervals
IBM
1
5
60
Daily
Tick
($SOX - PHLX SEMICONDUCTOR INDEX,D) Dynamic,0:00-24:00
Semiconductors
1480.00
1460.00
1440.00
1420.00
1400.00
1380.00
1360.00
1340.00
1320.00
1300.00
1280.00
1260.00
1240.00
1230.04
1220.00
1200.00
1180.00
1160.00
1140.00
1120.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec 2018 Feb Mar Apr May Jun Jul Aug Sep Oct Nov
Published by eSignal (www.esignal.com)

Equities
Other Intervals
IBM
1
5
60
Daily
Tick
($BKX - KBW BANK INDEX USD,D) Dynamic,0:00-24:00
Banks
118.00
116.00
114.00
112.00
110.00
108.00
106.00
104.00
102.00
100.00
98.83
98.00
96.00
94.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec
2018
Feb
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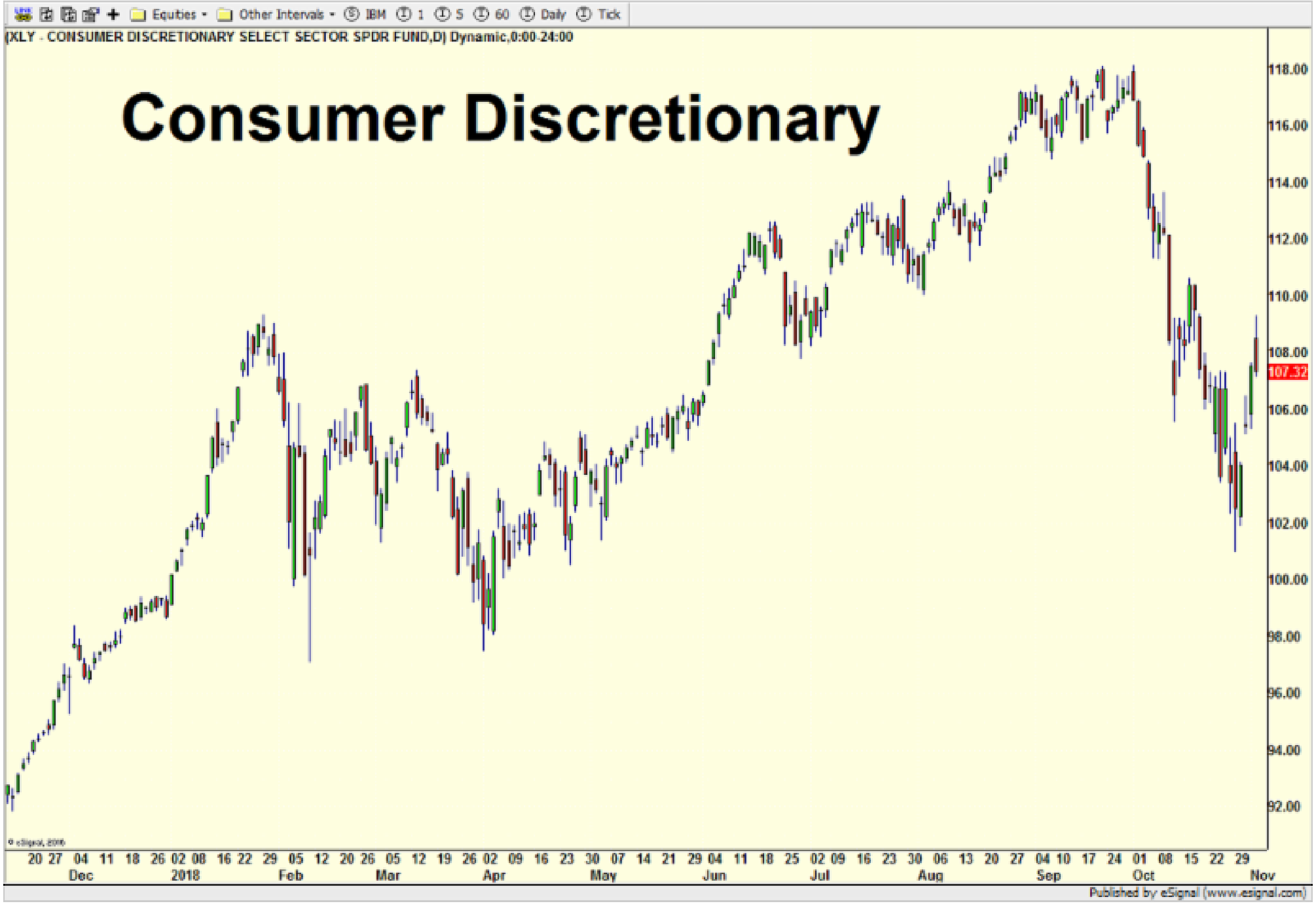
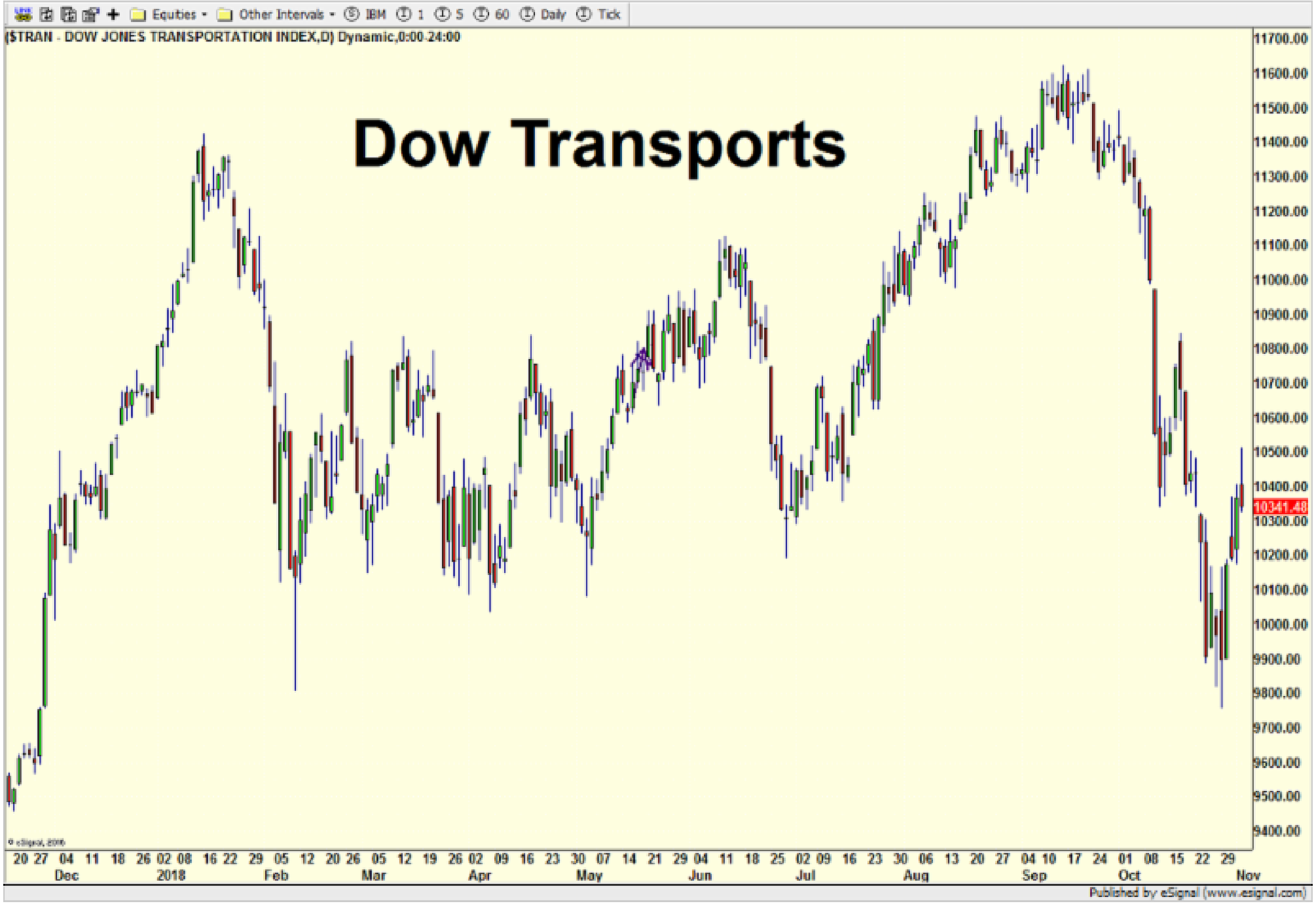
Nov
Published by eSignal (www.esignal.com)



Equities
Other Intervals
IBM
1
5
60
Daily
Tick
(XLY - CONSUMER DISCRETIONARY SELECT SECTOR SPDR FUND,D) Dynamic,0:00-24:00
Consumer Discretionary
118.00
116.00
114.00
112.00
110.00
108.00
107.32
106.00
104.00
102.00
100.00
98.00
96.00
94.00
92.00
20 27 04 11 18 26 02 08 16 22 29 05 12 20 26 05 12 19 26 02 09 16 23 30 07 14 21 29 04 11 18 25 02 09 16 23 30 06 13 20 27 04 10 17 24 01 08 15 22 29
Dec 2018 Feb Mar Apr May Jun Jul Aug Sep Oct Nov
Published by eSignal (www.esignal.com)



Liquidity Canaries Better Than Expected

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The last few canaries come from off the beaten path and focus on liquidity. High yield or junk bonds are first and I am showing two different charts. The first one is an ETF which trades like a stock while the second one is an excellent proxy for the sector, the PIMCO High Yield Fund. The ETF is more concentrated in the most liquid high yield issues while the mutual fund is much more diversified.

Looking at the right side of the chart you can see that both high yields proxies saw new highs recently when the stock market indices and sectors did, another good sign.
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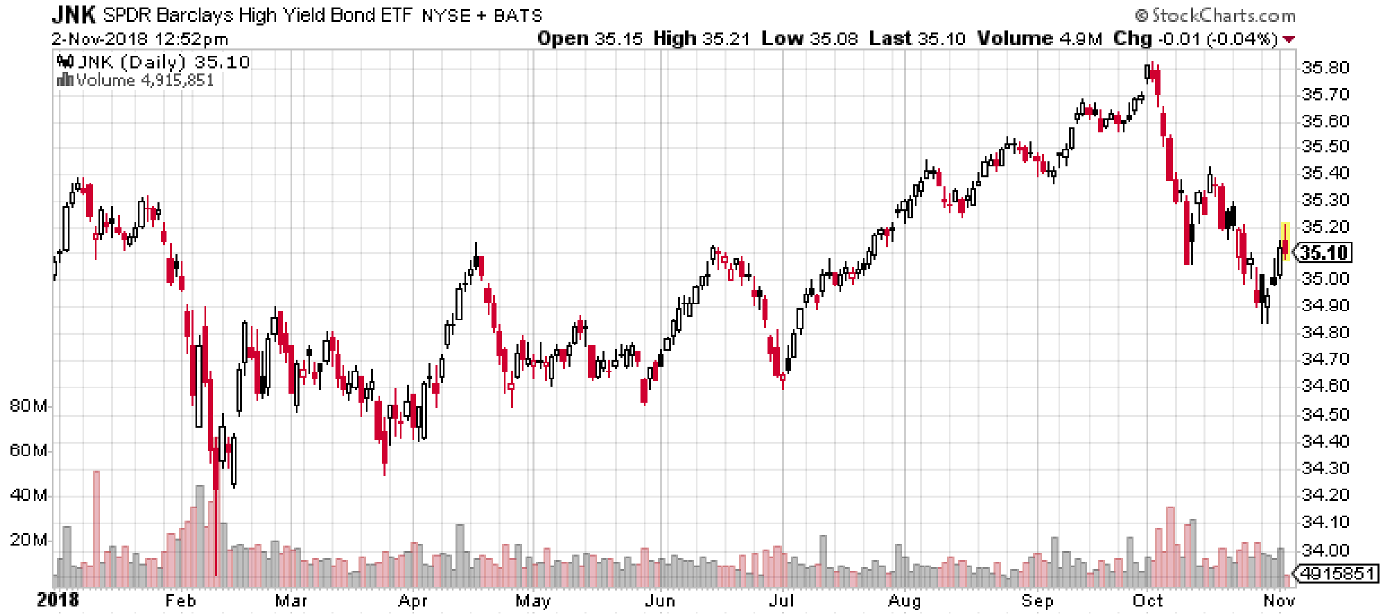
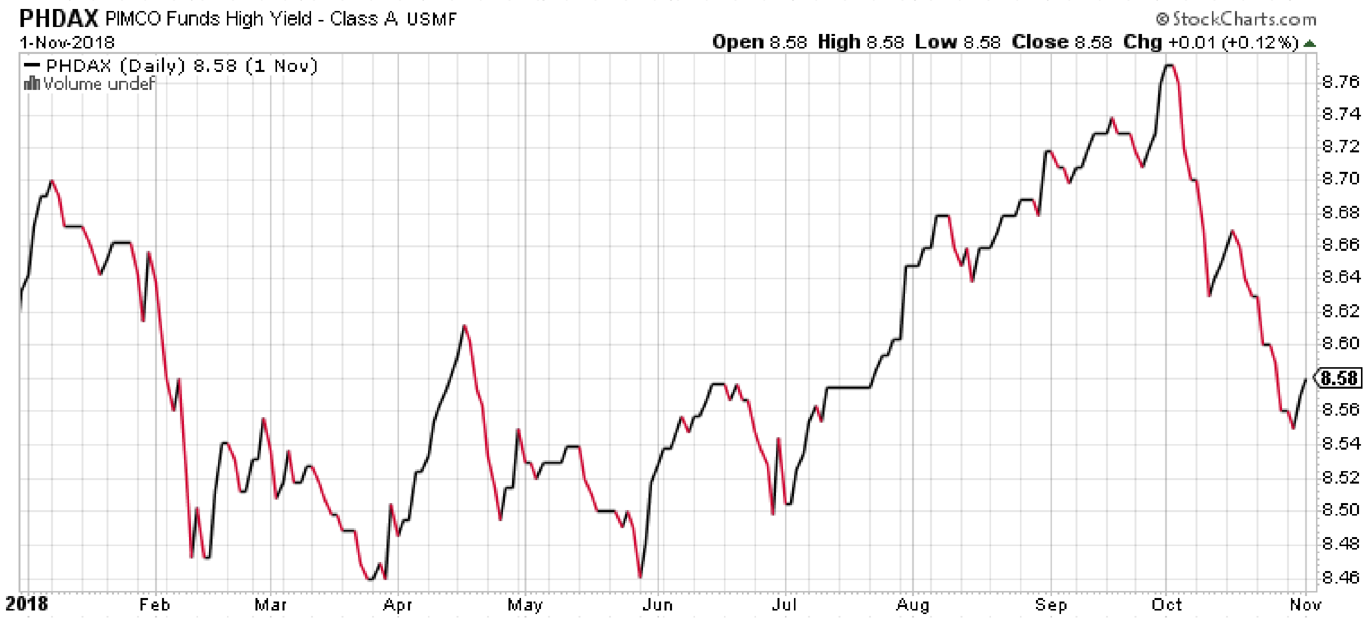


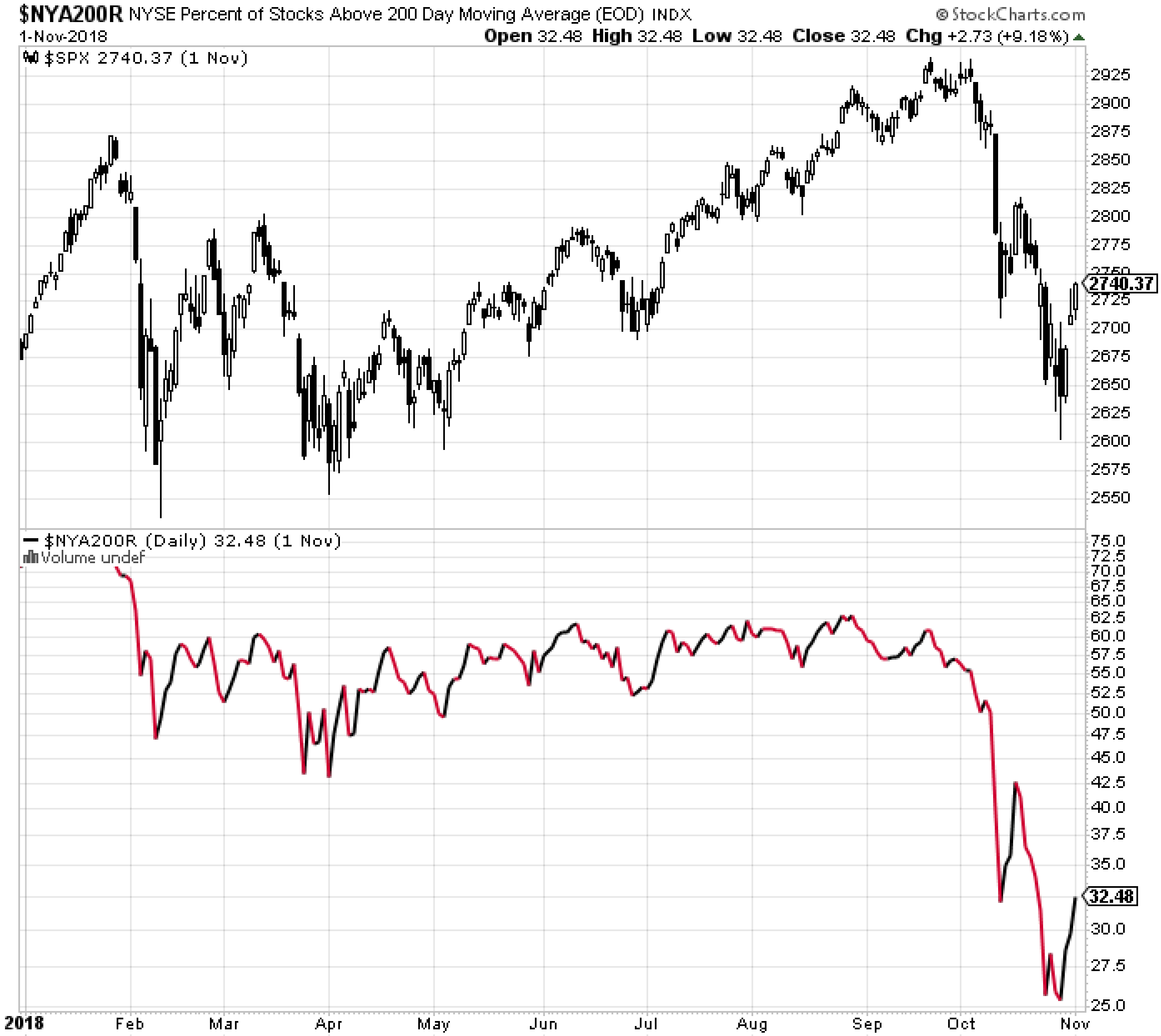


One of my favorite canaries is next, the New York Stock Exchange Advance/Decline Line which essentially tells us about the participation in rallies and declines. It takes the net number of stocks going up and down on a given day and adds to the previous tally. This indicator peaks and warns almost every time a bear market is near. In the chart below, I first show the S&P 500 with the NYSE A/D below.

Take a look at the September to October period. While stocks and junk bonds were heading higher, this indicator did not, a clear warning sign. Some people call it a divergence while others call it a non-confirmation. I just call it a warning.

The main problem with this indicator is that warnings signs can last a long time. This indicator peaked in April 1998 but the stock market ran higher for 23 more months with a 20% decline thrown in between. In 2007, this indicator only gave three months warning. Right now, we are dealing with a one month warning which I consider to be too short to be significant.

The next indicator is similar to the one above in that it tells us about the internal health of the stock market. In the case below, we are looking at the S&P 500 in black with the percentage of stocks in uptrends below that. Generally speaking we want the indicator to remain firm above 50%. After a decline, we want to see this indicator above 55% to signal an all-clear.



Looking at all of the canaries, there are only a few warning signs with banks and semis being the only serious ones. In this case, stocks should recover and see new highs over the coming few months. Dow 27,000 is the absolute minimum. Five straight closes above Dow 27,000 could set the stage for 30,000 in 2019.

As I said after the Q1 decline, it will be the next new high that really needs to be examined. The new high after the Q1 correction produced warnings and stocks are in the midst of a decline, but not a bear market. I do believe that Dow 27,000 is going to see more warnings than the recent high and possibly warn of a bear market. Stay tuned.

Upcoming Appearances

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Yahoo Finance Midday Movers - December 5th 11:30 am - 1:00

FOX Business Making Money - December 5th 2:30 pm

You can view most of the past segments by clicking below.

Media Appearances

(http://www.investfortomorrow.com/InMedia.asp)

Investment Quotes/Adages To Live By

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"In God we trust, all others bring data."
- The Elements of Statistical Learning

"The only easy day was yesterday."

- The U.S. Marines

"When in doubt, get out!"

"If it's obvious, it's obviously wrong."
-Joe Granville

"It's ok to be wrong, but it's not ok to stay wrong."

"This time is different."

"The markets require the patience of a dozen men."
-Robert Rhea

"Luck is the residue of effort."

"The most bullish thing a market can do is go up in the face of bad news."

"The most bearish thing a market can do is go down in the face of good news."

"The market can stay irrational longer than you can stay solvent."
-John Maynard Keynes

"Government is best which governs least" - Thomas Jefferson

Inflation is the one form of taxation that can be imposed without legislation.
-Milton Friedman

"You cannot legislate the poor into freedom by legislating the wealthy out of freedom. What one person receives without working for, another person must work for without receiving. The government cannot give to anybody anything that the government does not first take from somebody else. When half of the people get the idea that they do not have to work because the other half is going to take care of them, and when the other half gets the idea that it does no good to work because somebody else is going to get what they work for,that my dear friend, is about the end of any nation. You cannot multiply wealth by dividing it." - Dr. Adrian Rogers, 1984

"Bear markets seem to be divided into three phases: the first being the abandonment of hopes upon which the final uprush of the preceding bull market was predicted; the second, the reflection of decreased earnings power and reduction of dividends, and the third representing distressed liquidation of securities which must be sold to meet living expenses. Each of these phases seems to be divided by a secondary reaction which is often erroneously assumed to be the beginning of a bull market."
- Robert Rhea

"Free enterprise is a rough and competitive game. Nobody too big to fail. Nobody too small to succeed. It is a hell of a lot better than government control." - Ronald Reagan via Dan Kennedy

"A government big enough to give you everything you want is big enough to take everything you have." - Gerald Ford via Dan Kennedy

"The problem with socialism is that, sooner or later, you run out of other people's money." - Margaret Thatcher

"Diversification alone is no longer sufficient to temper risk... You need something more to manage risk well."
- Mohamed El-Erian

"A little bit at a time adds up to a lot in no time"

To Your Financial Success,

Paul Schatz
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