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Inside this issue

Even More Relentless Selling

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So much for not sending another edition this year.

The third most asked question this month has been if I think the markets are repeating or rhyming with 2008 which is actually 2007-2009. My emphatic answer is NO. The financial crisis was a generational event and I don't believe we will see a repeat of the entire banking system on the verge of systemic insolvency nor 50% - 70% market declines for many, many years to come. That whole analog just plays really well in the media as fear juices ratings.

Let's move on to what ended up being one of the single strongest selling waves on record and it's still only 13 days old. Most selling waves last at least another week. From December 3rd through December 24th, the major stock market indices saw relentless selling almost day in and day out. But really, the period since December 11th was one for the ages.

Every single day, the stock market closed lower than where it opened. On my colorful charts, that means every day was red. That's 10 straight days! My intra-day data doesn't go back before 1980, but that's an all-time record. During that period, stocks closed in the lower 50% of their daily high to low range every single day as well. That's another record.

Below, you can see what I am referring along with where stocks could end up bouncing.
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It has been the single worst Decembers since 1931. 1931! That's pretty bad. This is supposed to be a time when no one really sells.

Given how "heavy" stocks have acted and how strong the downside momentum has been, history suggests the bottoming process will be complex. In all likelihood, that will be the theme of the first quarter of 2019. The initial momentum bottom should form any day now with a violent and sharp countertrend move to the upside following.

If you look back at the chart above, you can see where I think the first bounce heads. The odds of stocks just finding a single point in time as the ultimate bottom are slim. And if that ends up being the case like post 9-11 on September 21st, then I think stocks will end up rallying and then significantly exceeding that low by mid-year.

Extreme Selling Leads to Rare & Immediate Reaction

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After already discussing the legendary selling wave stocks experienced this month through December 24th, one of the sub models within our big stock market model triggered a scenario based on historic levels of overdone selling that has only been seen a handful of times since 1980. Each and every time, stocks saw significant gains almost immediately, even when in the context of a bear market.

You can see all of these on the charts below with the arrows pointing to the triggers, including the most recent one at the close on December 24th. If this sub model works anything like past instances, stocks should be rallying before the week is over. If stocks continue to crater, it will be yet another case in what is becoming a very long line of failed studies and indicators this month.


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2016


2018

Prospects Strong for a Powerful Santa Claus Rally

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All month I have heard the pundits say that the Santa Claus Rally has failed or that Santa failed to call so bears will come to Broad and Wall, popularized by Yale Hirsch of Stocks Trader's Almanac fame. What incenses me is that those people just blurted and babbled nonsense. The Santa Claus Rally (SCR) doesn't begin until the last five days of the year and continues for the first two days of the next year. In other words, it literally just began at the close on the 21st.

As I look at the prospects for a SCR, there are two pieces of information I look at. First, is the stock market up or down for Q4 to date? And second, is the stock market up or down year-to-date? In today's case, both answers are down.

Since 1950, there have only been 7 cases where both periods have been down heading into the SCR. Not surprising, most were during bear markets. In 6 cases, the SCR was up and 5 of the 6 saw significant gains. Only 1977 saw a very small SCR loss.

Is This a New Bear Market?

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The second most asked question this month from clients I have met with and spoken with has been whether stocks are now in a bear market. That all depends on how you define a bear market. The media somehow decided that declines of 20% or more are bear markets.

Even if I agree with that definition, I don't find it helpful. So many times, declines of 20% are often right at the worst levels. 1990, 1998 & 2011 come to mind. All three of those declines were also fairly quick, roughly three months from peak to valley. 2000-2002 and 2007-2009 were much different bear markets in both magnitude and duration, 50%+ in price and more than one to two years in length.

Other folks use a fresh 18 month low in stocks to define a bear market. That works for some as well. I am not as absolute in my definition. The first thing I look for is a series of lower highs in price and lower lows. In other words, a clearly defined downtrend that a child could spot. From there, I get a little more complex.

In the 1990s we created a model that flashes red when a series of average prices all turn lower together and price is below those average prices. So it warns after a significant decline has already taken place. In 100 years, that model never missed labeling a bad market. That's all well and good. However, the problem is that it also flashed red many times when a 10-20% bull market decline had set in and was close to ending. In other words, it warned many more times than true bear markets had set in.

Today, stocks have clearly seen a series of lower highs and lower lows since October 1. That didn't surprise me. However, we have also seen our internal model flash red for both the S&P 500 and NASDAQ 100 for the past two weeks, joining their S&P 400 and Russell 2000 cousins. The last time this occurred was during the first few months of 2016 as stocks were finding a major bottom before an 18 month surge.Today doesn't seem like 2016, but we will obviously know more after the first rally.

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