

## Reversal...How We Got Here

In December markets took the third scenario breaking the major indices below their spring support levels and declining to the area of the target levels indicated by the breaking of the 2016-18 trendline. The DJ Industrials got within 450 points of its target, the S&P 500 and Nasdaq fell to their targets and the Russell 2000 and Toronto Composite undercut their projected targets.

We may not have seen the expected heavy volume into the December 24<sup>th</sup> low however, internally the numbers were heavily biased to the downside: in the final three days into the low, downside volume totaled over 80% of upside plus downside volume each day, with the 24<sup>th</sup> at 88.34%, just a shade below the 90% level.

These downside extremes were followed by two 90% up volume days on the 26<sup>th</sup>—when pension funds rebalanced their stock/bond allocations (effectively a massive short squeeze/Christmas gift for the algos & HFTs) and again on January 4<sup>th</sup> when the markets interpreted Fed Chairman Powell's statement as the Fed caving into market demands to soften/end rate hikes. Thus with indices, stocks, technical and sentiment indicators in the depths the markets have some catalysts to latch onto to provide upside traction, break the downside momentum and produce the strongest start of a year since 1938. Solid breadth, including a powerful "Breadth Thrust" signal (an exponential 10-day moving average of advancing stocks on the NYSE divided by the sum of advancing plus declining stocks. When the moving average moves from below 40% to above 61.5% within a period of 10 trading days the signal occurs indicating a reversal following severe market weakness), and strong up/down volume. The result: an 18-day spurt from the low.

### Where to Next?

Probabilities favour a bottoming sequence setting in – a prolonged trading range with one or more tests of the recent low along the way, as seen last year following the plunge in February. But it is important to recognize the fourth quarter decline was much more significant and damaging than last year. Thus investors should anticipate a lengthy, choppy period of repair to allow indices, sectors, groups & individual stocks time (weeks to months) to rebuild new bases of support and claw through overhanging resistance (selling pressure), as well as still declining moving averages and falling trendlines.

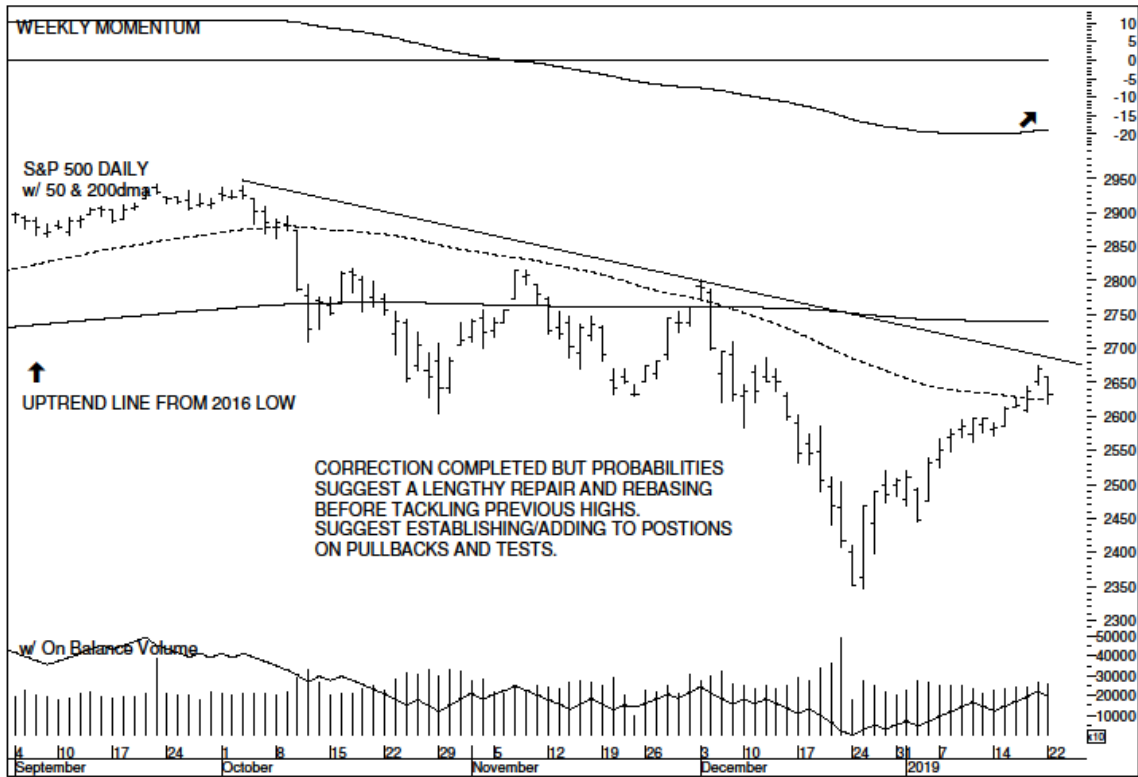
The current sharp bounce off the low is being enhanced by Q1 EPS reports and rumours around U.S./China trade talks pushing indexes into areas of heavy overhead resistance in the 2700-2780 zone on the S&P 500. We feel all this 'noise' is actually exaggerating the actual recovery. This is evident in that overall volume has not shown the explosive characteristics of big reversals and has actually been declining since the December 26<sup>th</sup> liftoff. This indicates there is less power and investor commitment behind this move & leaves markets vulnerable to a pullback. Tuesday's 84.25% down volume and the increase in volatility Wednesday tends to confirm investors are more skittish than one would expect on such a reversal.

As we have maintained throughout the fourth quarter decline we expect another upleg to follow once the corrective/bottoming process is completed.

We suggest investors not chase stocks with so much 'noise' present in these markets. Rather, take small positions in favoured names and build one's position across the expected trading range/bottoming sequence.

Seven names with positive relative strength, rising On Balance volume and momentum reversing from decline are included in the accompanying charts.

S&P 500 Daily

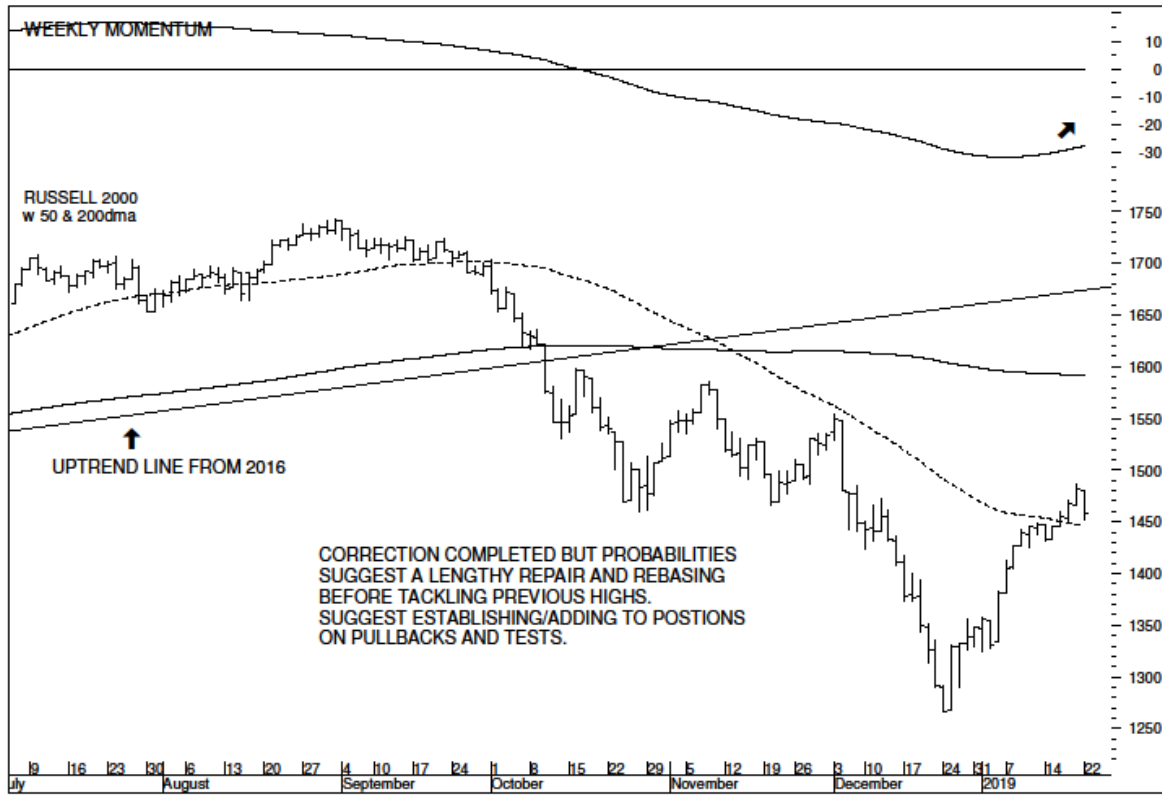


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Russell 2000

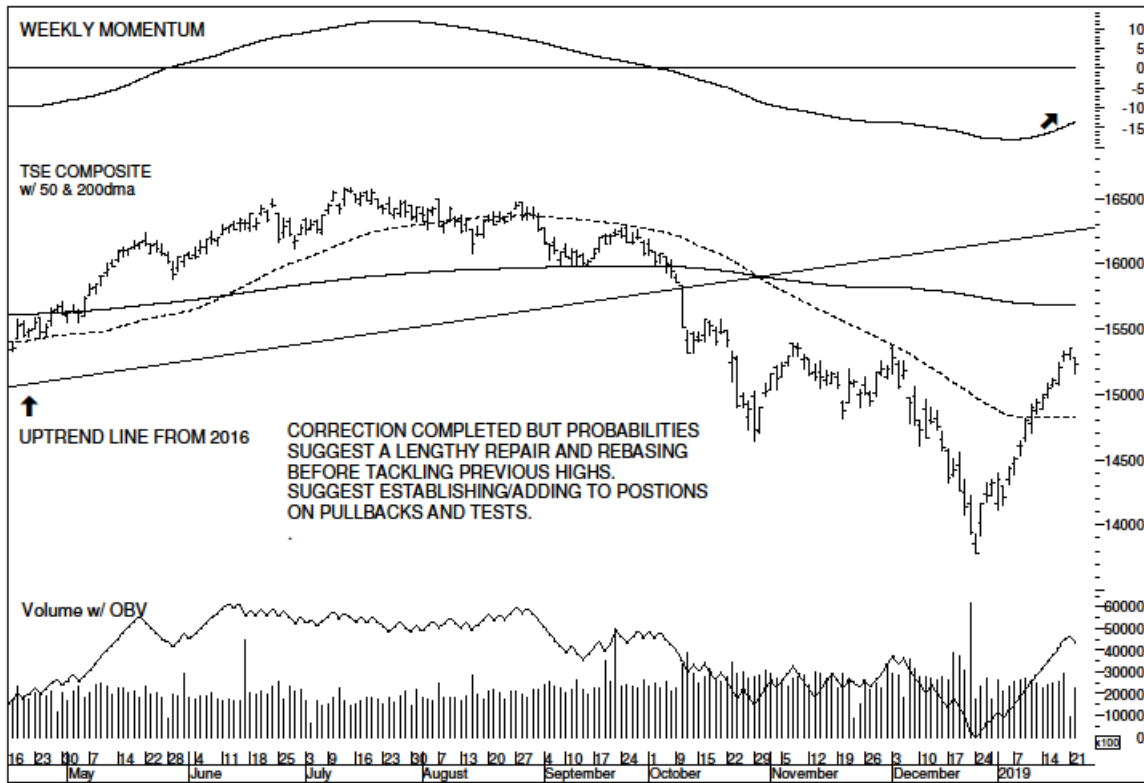


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TSX Composite

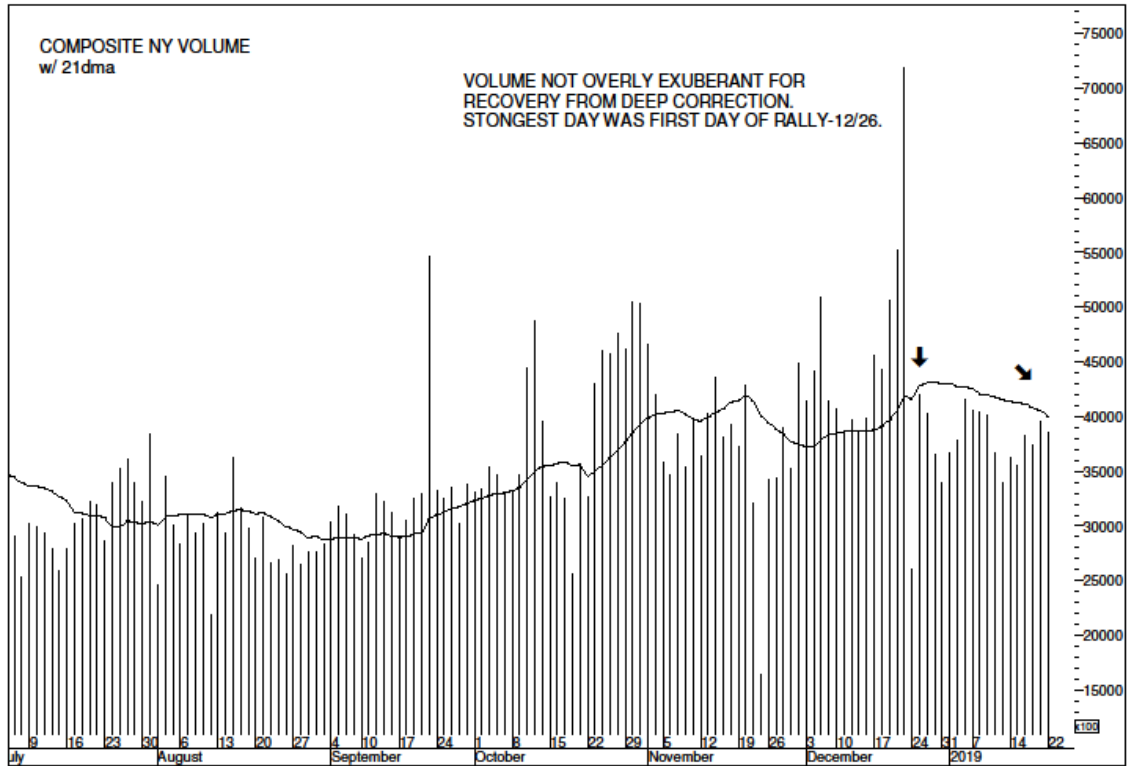


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Composite Volume

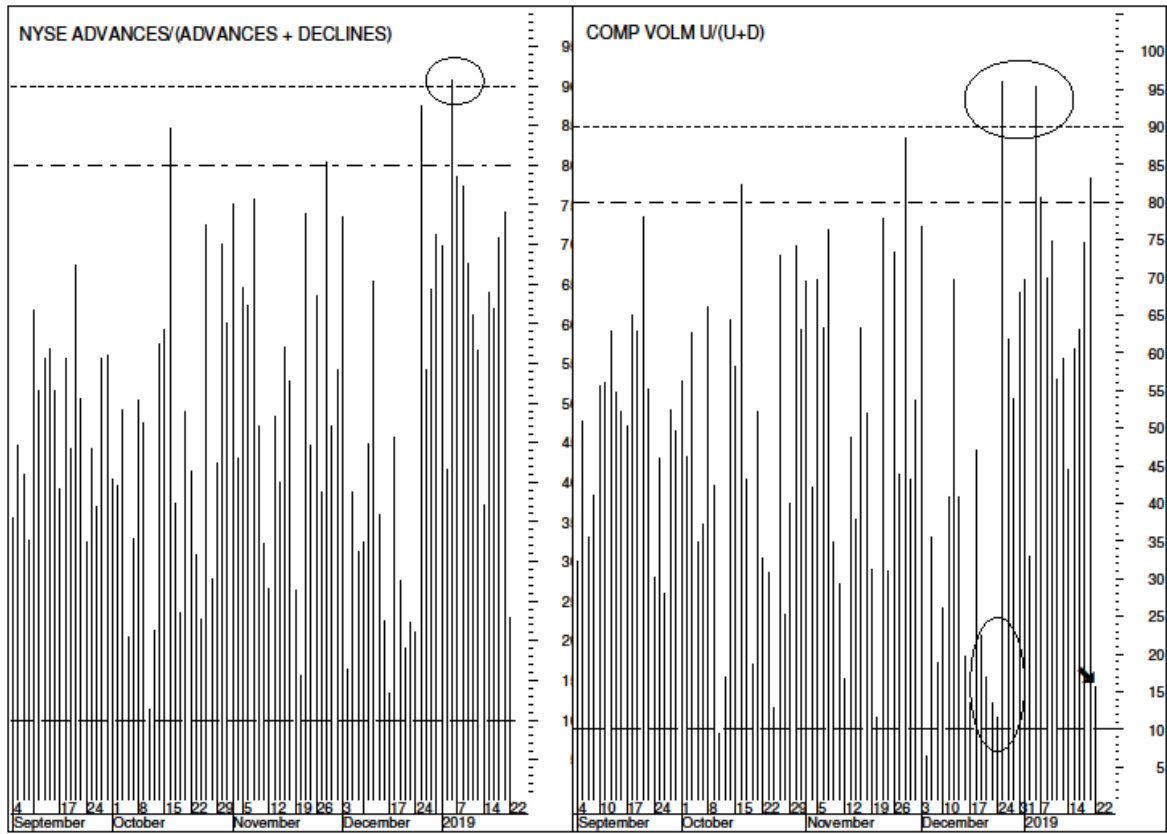


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Advance/Dcline Lines

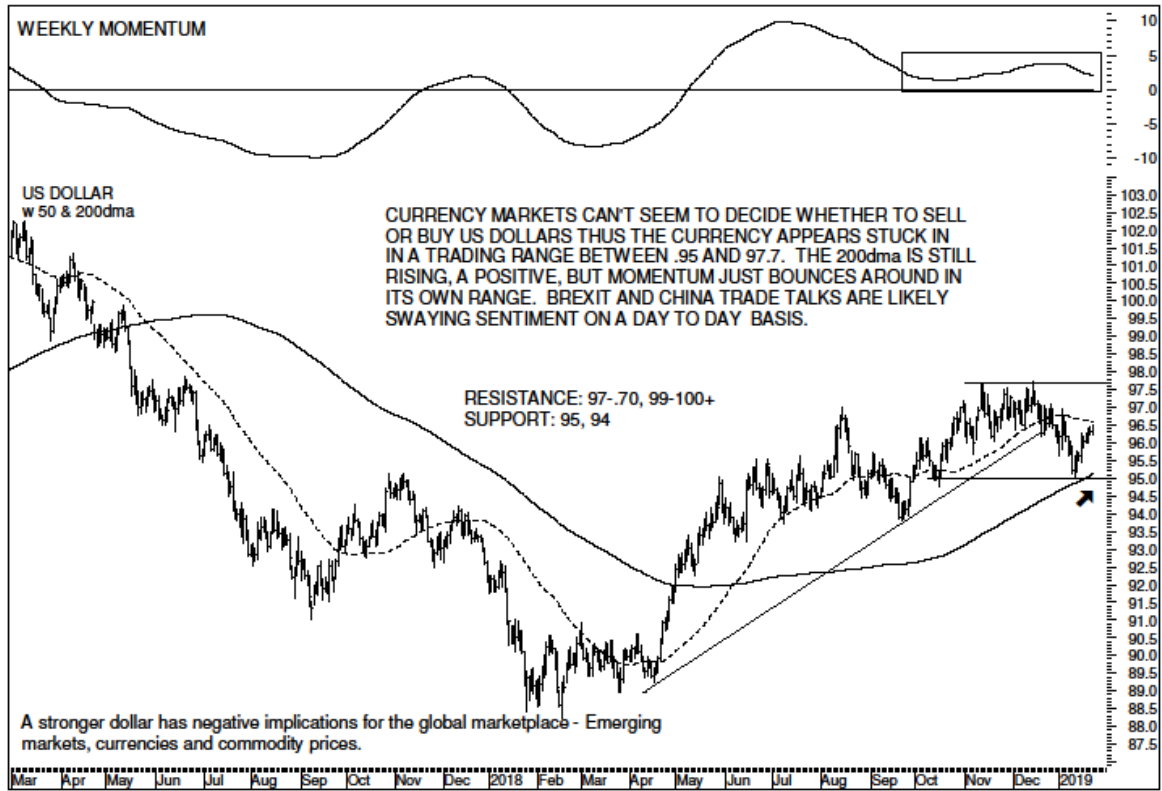


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US Dollar

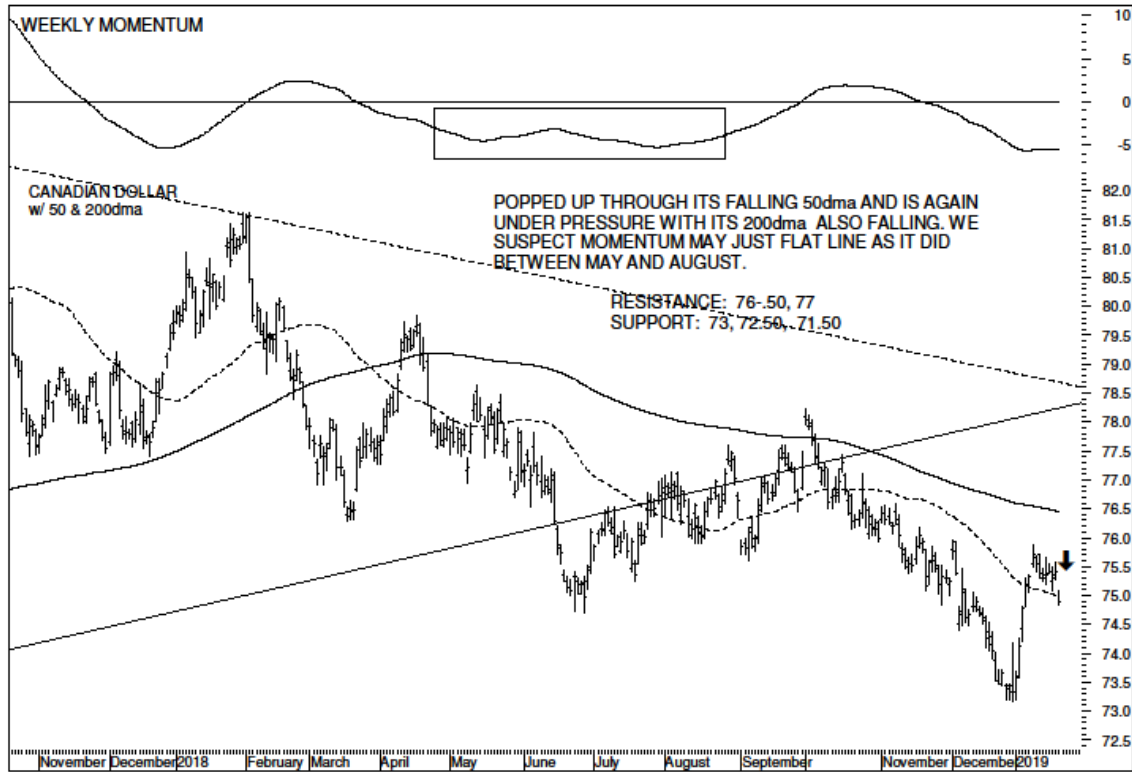


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CDN Dollar



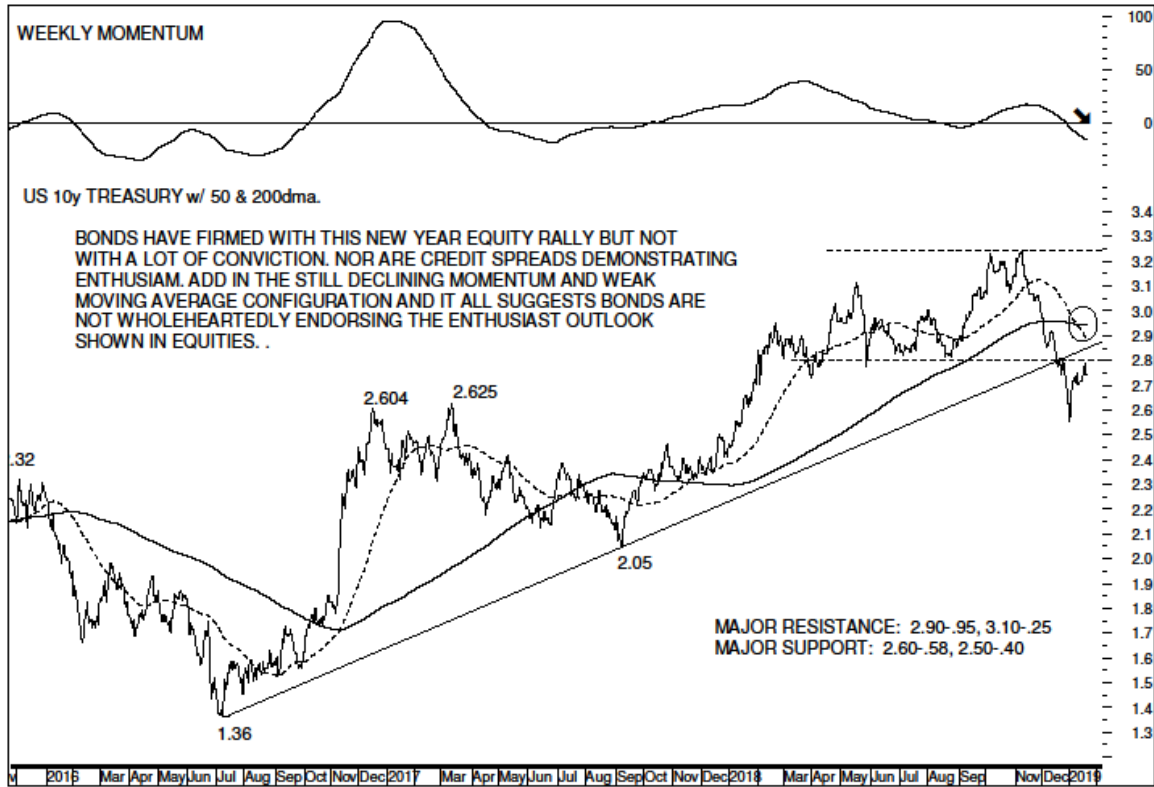
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10y Treasury

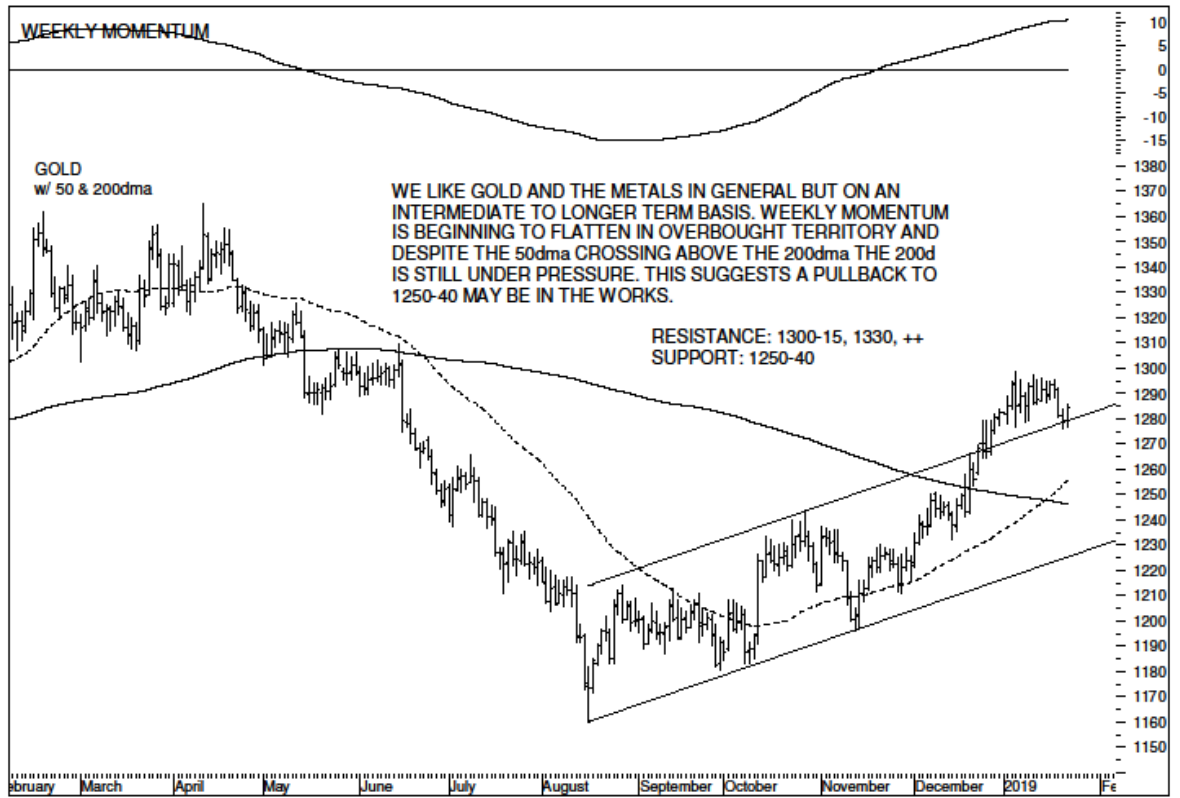


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Gold

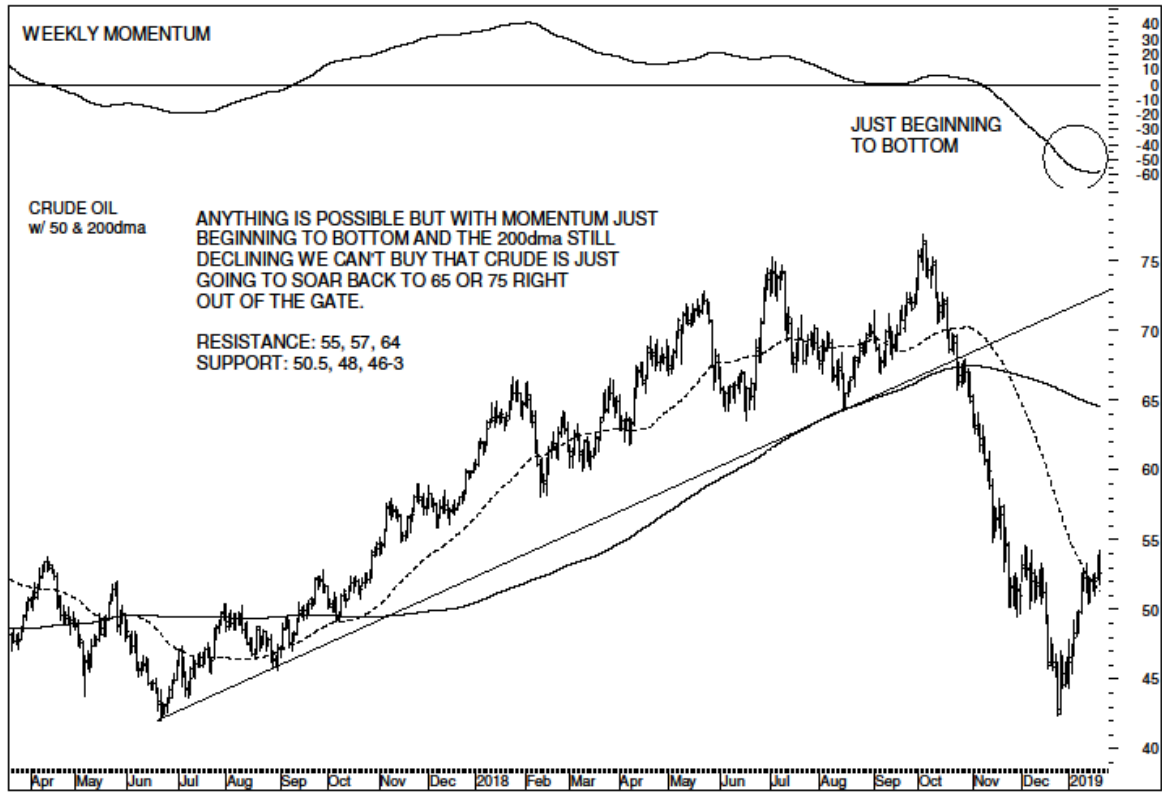


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Crude Oil

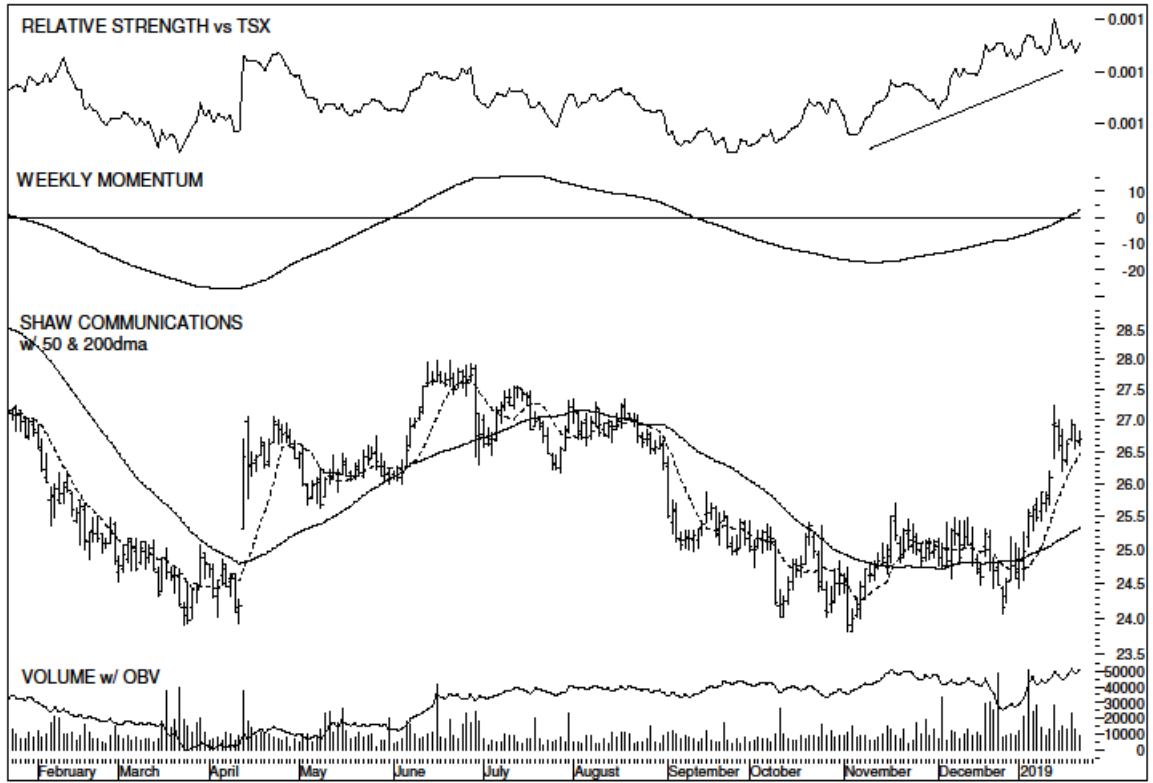


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Enbridge



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TC Corp.

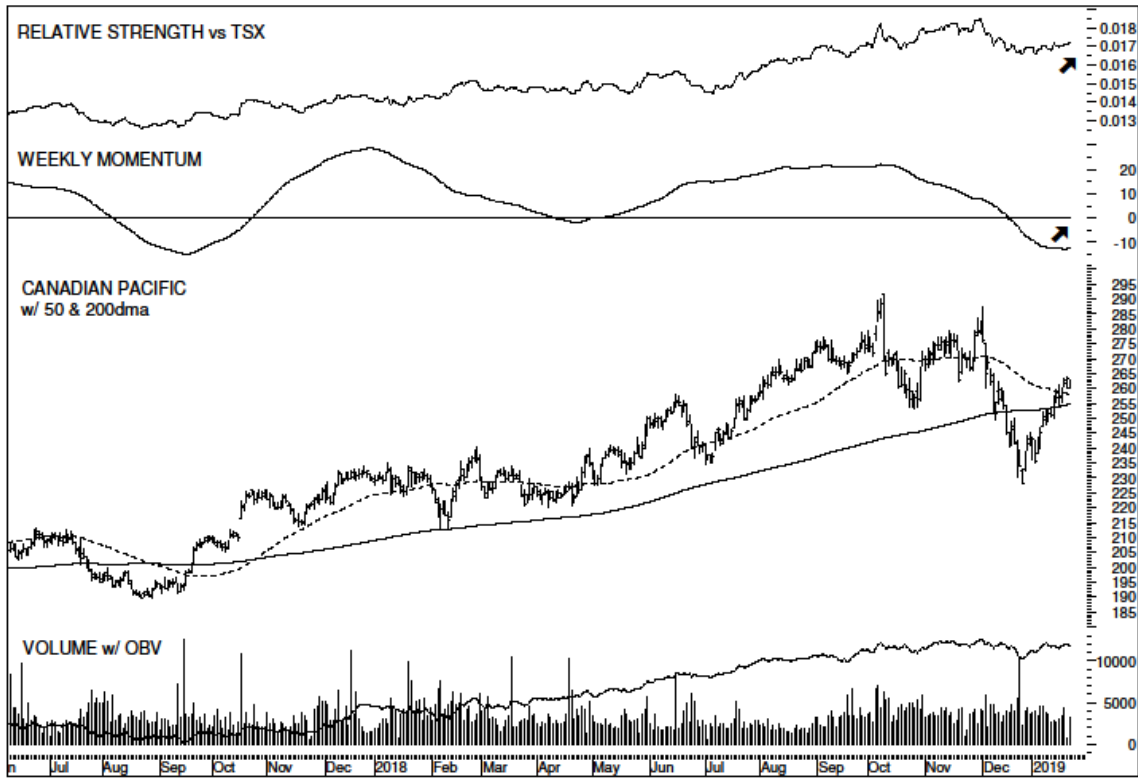


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Canadian Pacific

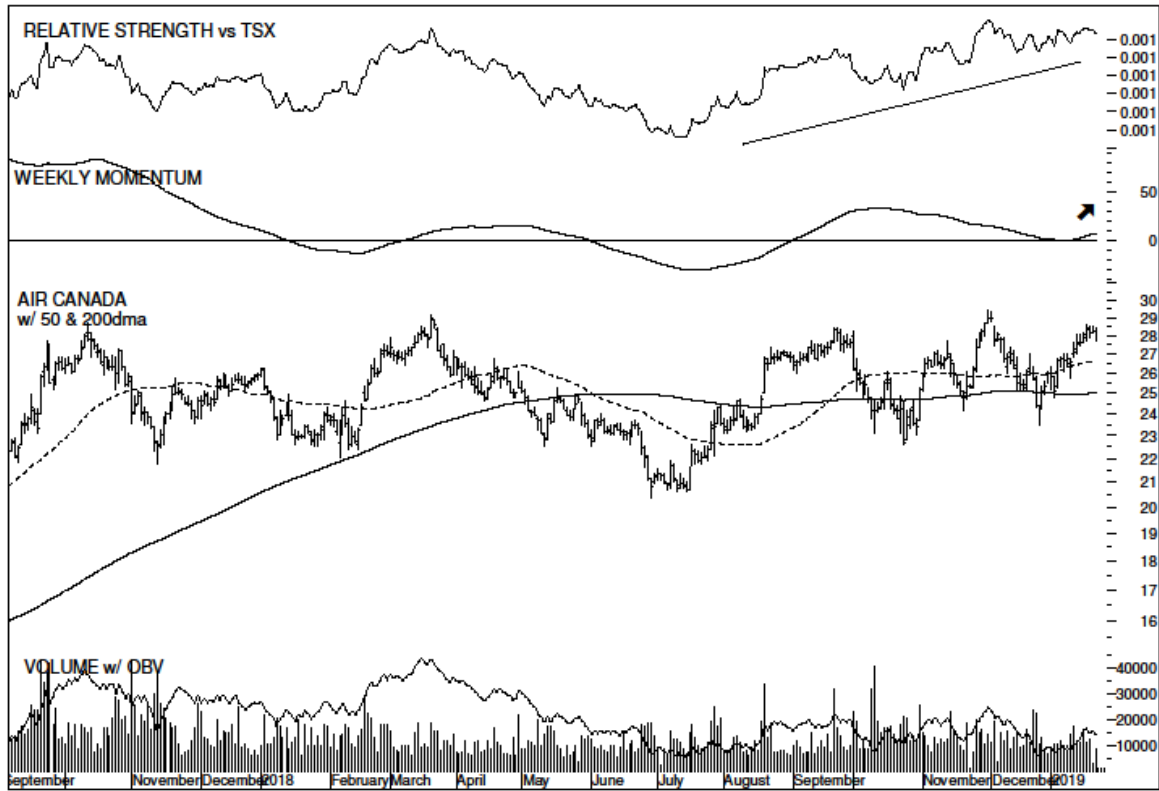


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Air Canada



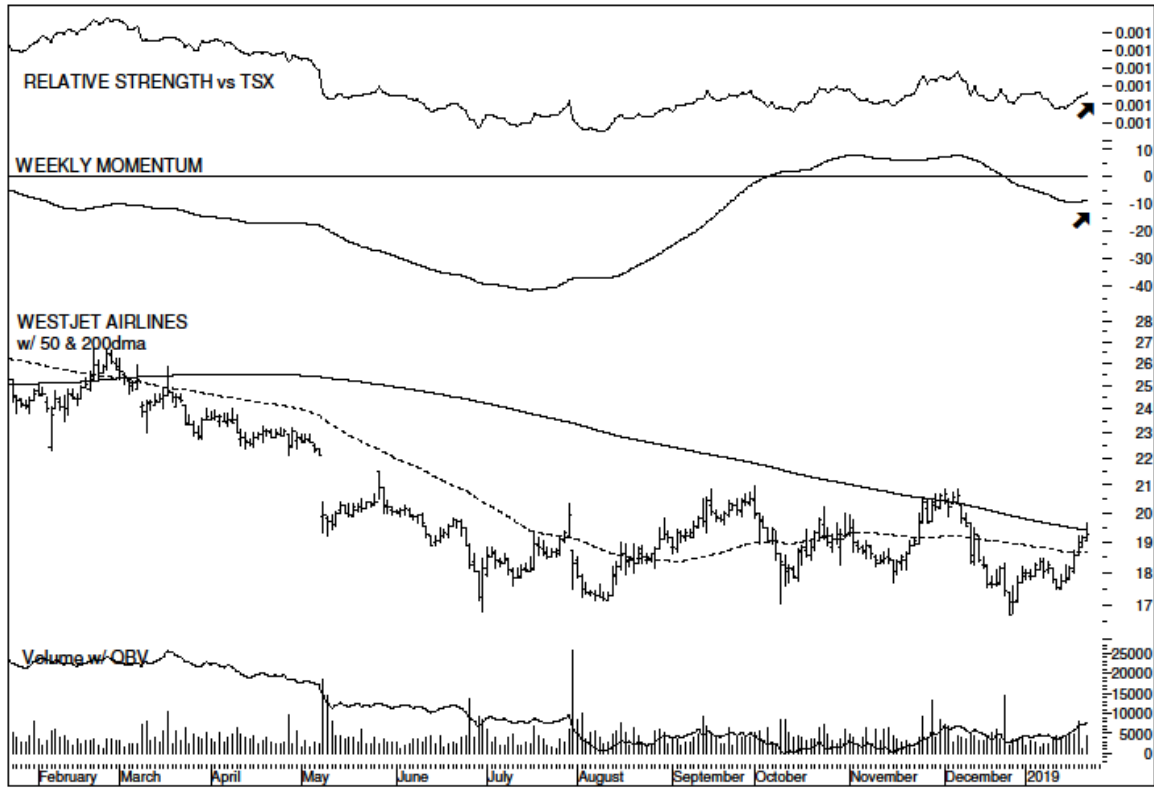
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WestJet Airlines

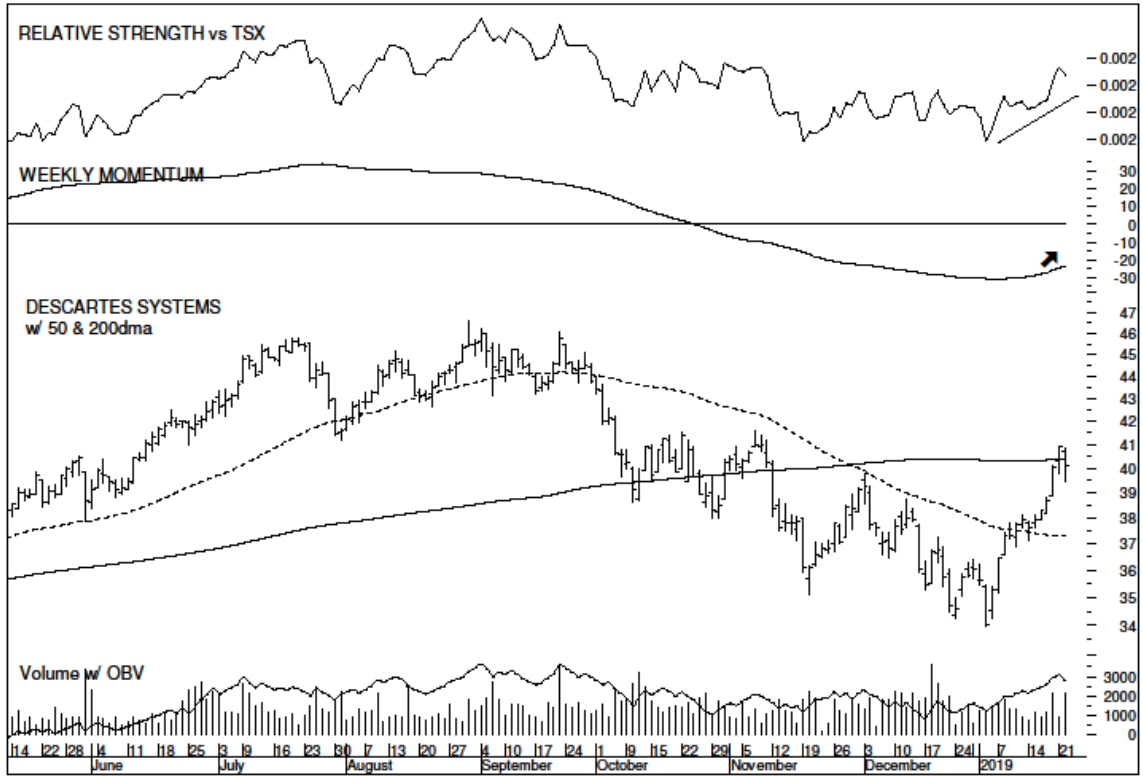


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The Descartes Systems Group



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