A Different Sort of Presidential Cycle

***e*Research Corporation** is pleased to provide a weekly commentary, authored by Tom McClellan, entitled "The McClellan Chart-In-Focus", which is a free technical analysis article published each week.

In this article, Mr. McClellan examines the relationship between the S&P 500 and new-president market cycles.

The article is reproduced below, beginning on the next page, or you can use this link to go to the article directly:

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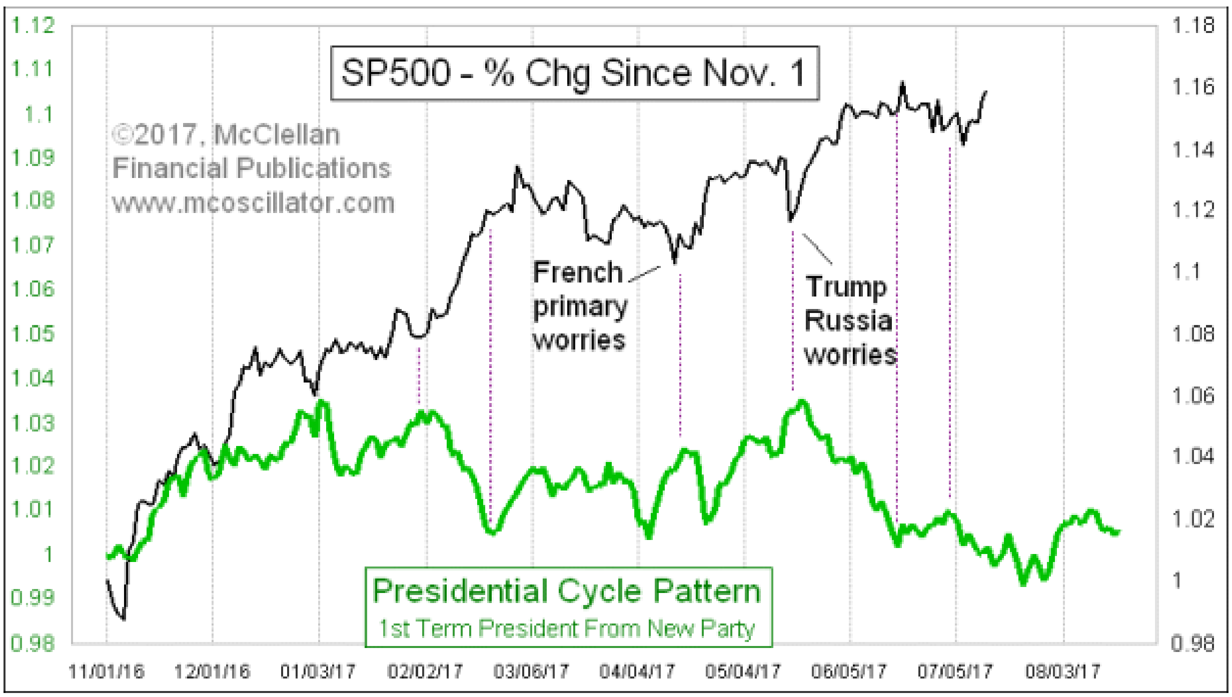
The McClellan Chart-In-Focus

by Tom McClellan (bio at end)

A Different Sort of Presidential Cycle

It is, by now, an overused phrase to say that we are in a different sort of presidency right now. Befitting that theme, we are seeing a really different sort of behavior in the market relative to the Presidential Cycle Pattern.

This week's chart shows a version of our Presidential Cycle Pattern that is constructed by averaging together the stock market's performance only in periods when there is a new president from a different party than the last one. We have found that the market's personality differs quite a bit according to whether there is a new sheriff in town from a different group than the last one, versus a status quo type of president.



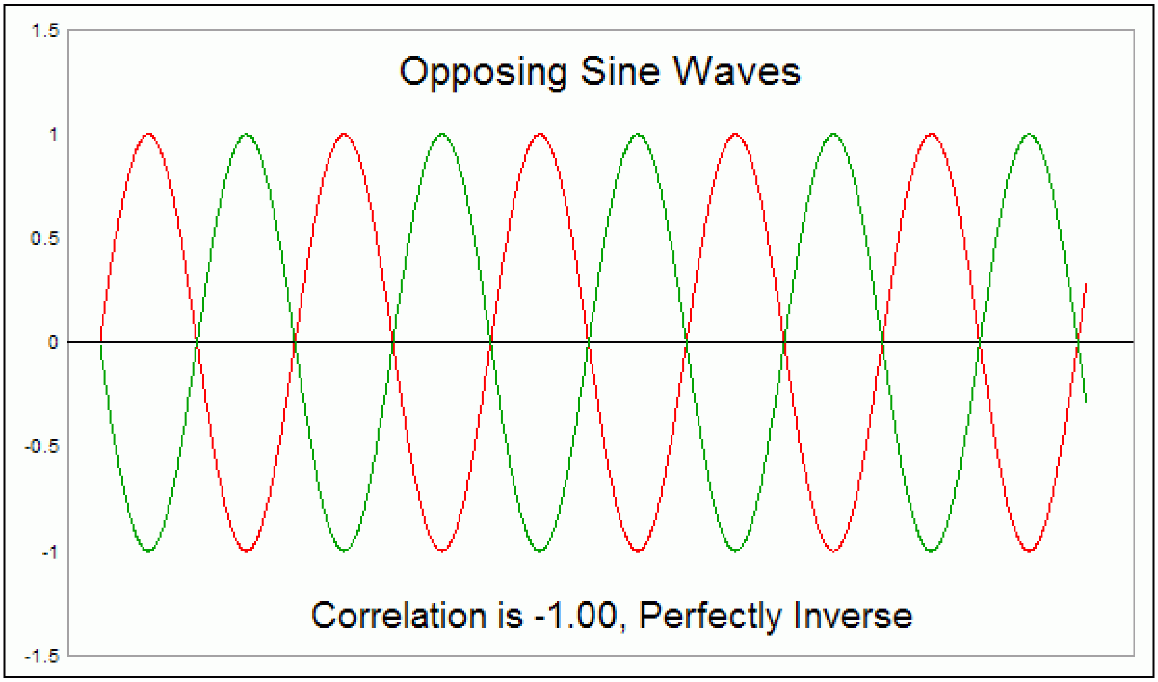
Normally, a new president from a different party brings a market rise, at least until May of the first year, just on hope that everything is going to be better. Then, as investors realize that all of their hopes are not getting realized right away, that hope turns into disappointment, and the market declines during the summer and into autumn.

What we are seeing this time is a rise, all right, but it is continuing now into July, and investors are not yet showing disappointment. That is a verbal story. But, if you look closely at the chart, you can see that the S&P500 has been zigging and zagging all at the wrong times, according to the Pattern. In other words, the correlation has been inverse.

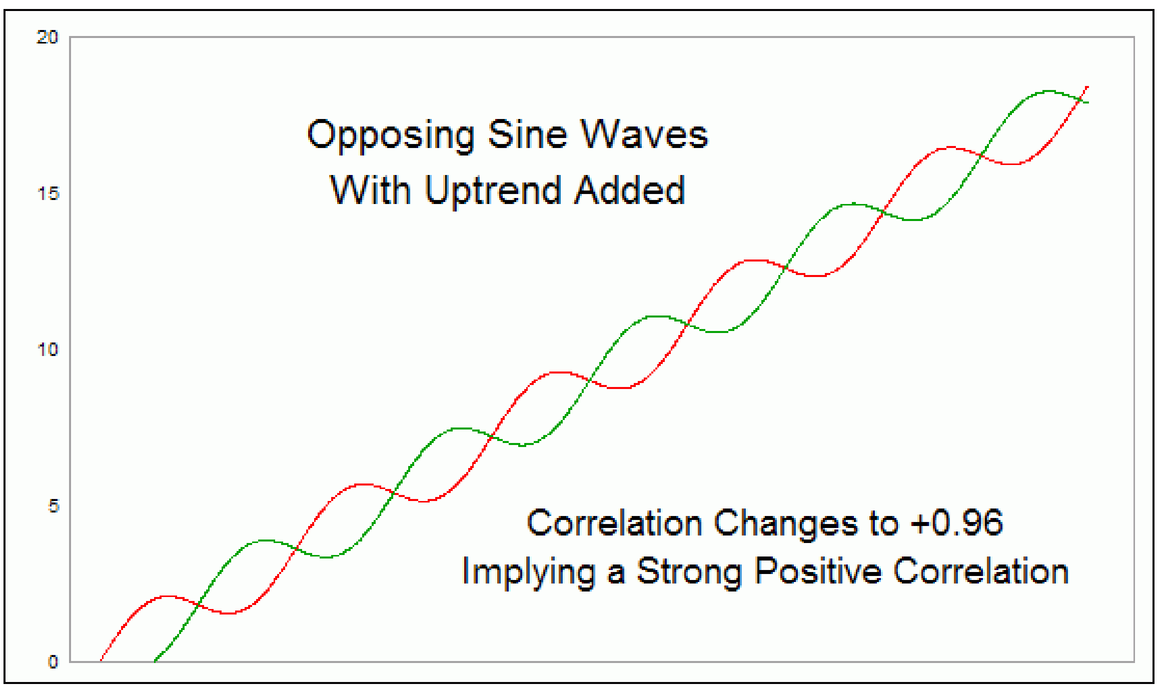
That statement is only true when one looks at a certain time-frame. The overall path of the S&P500 has been higher like it was supposed to, but the minor pattern has been inverse.

This revisits a point I wrote about in August 2010, under the headline of "Correlations May Not Be What They Seem". The point is that having a trend in the data makes an inverse correlation seem positive, both visually and quantitatively.

Here are a couple of charts from that article. The first shows a perfect inverse correlation:



But, if we add an artificial uptrend to that inversely correlated data, the calculation of a correlation coefficient flips to a strongly positive one:

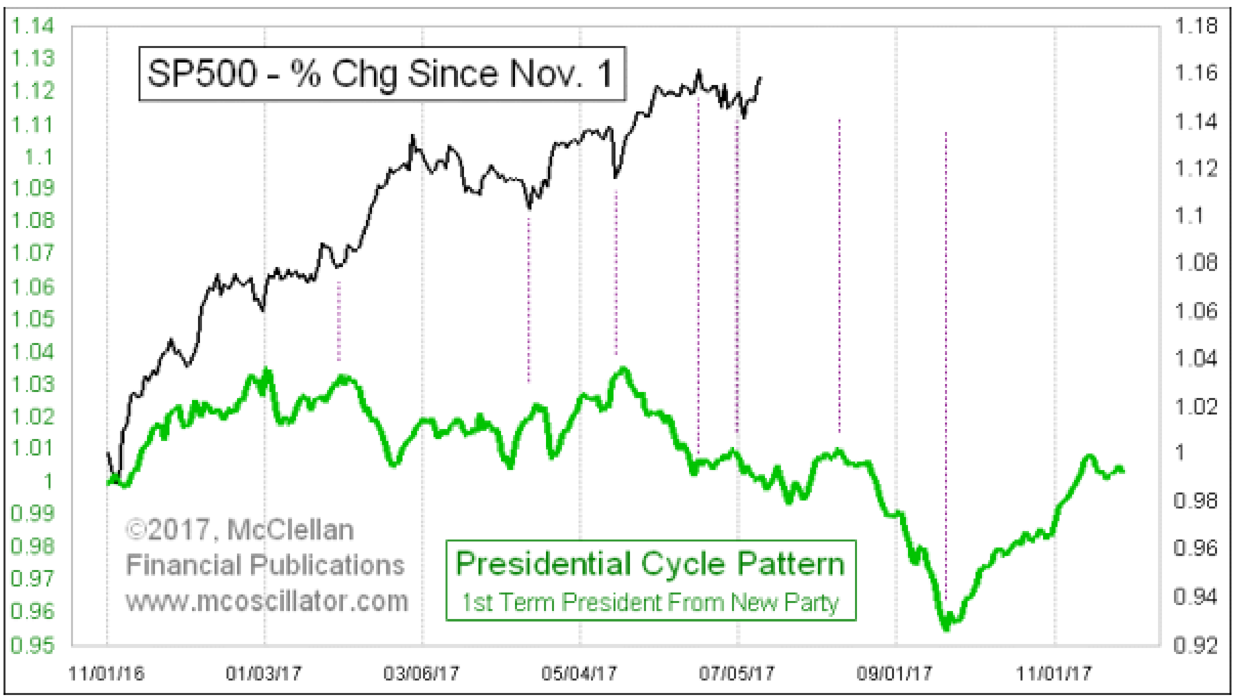


The point in reviewing these principles is to see past the 8-month uptrend in the first chart, and notice the inverse relationship in the smaller movements, even as there is an overall uptrend. That overall uptrend can disguise the inverse movement on the shorter time scale.

With that point firmly in mind, we can see that the S&P500's movements have been backwards from what the schedule says. There is your different sort of presidency, and different sort of price response. The S&P500 bottomed at the end of June, just when this Presidential Cycle Pattern said that a minor top was supposed to be seen. And now the market is rising at a time when the Pattern says prices should be falling.

All of this inverse behavior would be concealed from those who look just at quarterly or monthly returns data. You have to look at the chart closely to see the insight. And the immediate message is that prices should continue higher for much of the rest of July.

A longer-term chart shows that this autumn will get even more interesting, assuming that the inverse correlation of the minor patterns remains inverse.



If it does remain inverse, then the Pattern's decline into late September should mean a strong advance for stock prices then. But here is the caveat: If you ever count on a relationship remaining inverse, that is when it can flip again and fool you. So you must keep a watch on it, and notice if it "disinverts".

Tom McClellan

Editor, The McClellan Market Report

BW: Information on Tom McClellan and *The McClellan Market Report* and *The Daily Edition* follows on the next page.

ABOUT THE AUTHOR

Tom McClellan

Tom McClellan has done extensive analytical spreadsheet development for the stock and commodities markets, including the synthesizing of the four-year Presidential Cycle Pattern. He has fine-tuned the rules for inter-relationships between financial markets to provide leading indications for important market and economic data.

Tom is a graduate of the U.S. Military Academy at West Point, where he studied aerospace engineering, and he served as an Army helicopter pilot for 11 years. He began his own study of market technical analysis while still in the Army, and discovered ways to expand the use of certain indicators to forecast future market turning points.

Tom views the movements of prices in the financial market through the eyes of an engineer, which allows him to focus on what the data really say rather than interpreting events according to the same "conventional wisdom" used by other analysts.

In 1993, he left the Army to join his father in pursuing a new career doing this type of analysis. Tom and his Father spent the next two years refining their analysis techniques and laying groundwork.

In April 1995 they launched their newsletter, The McClellan Market Report, an 8-page report covering the stock, bond, and gold markets, which is published twice a month. They utilize the unique indicators they have developed to present their view of the market's structure as well as their forecasts for future trend direction and the timing of turning points.

A Daily Edition was added in February 1998 to give subscribers daily updates on their indicators and also provide market position indications for stocks, bonds, and gold. Their subscribers range from individual investors to professional fund managers. Tom serves as editor of both publications, and runs the newsletter business from its location in Lakewood, WA.

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