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Consumer Discretionary Sector Shows Enormity of the Beat-Down

***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 analyzes the market action of the consumer discretionary sector versus the consumer staples sector and concludes the ratio decline is over-done.

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Bob Weir, CFA
Director of Research

November 29, 2018

The McClellan Chart-In-Focus

by Tom McClellan (bio at end)

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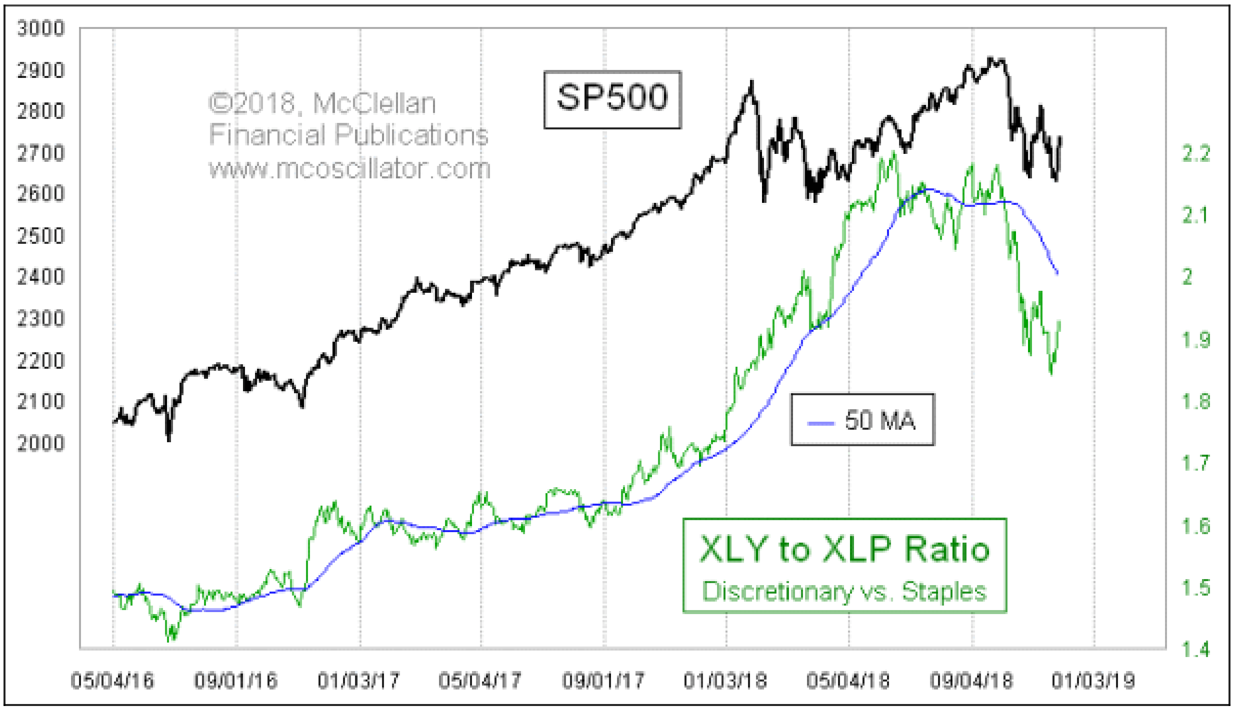


Investors' appetites for risk-taking can be measured with the comparison of the Consumer Discretionary sector versus the Consumer Staples sector.

The big shift in their behavior recently shows the huge abandonment of risk appetite in October to November 2018, but it also creates a huge oversold opportunity.

The staples companies make things which consumers need all the time; our use of tooth paste and toilet paper does not vary much with the state of the economy. But if economic prospects are looking grim, we might exercise "discretion" by not buying a new pair of $200 Nike sneakers, or a new car.

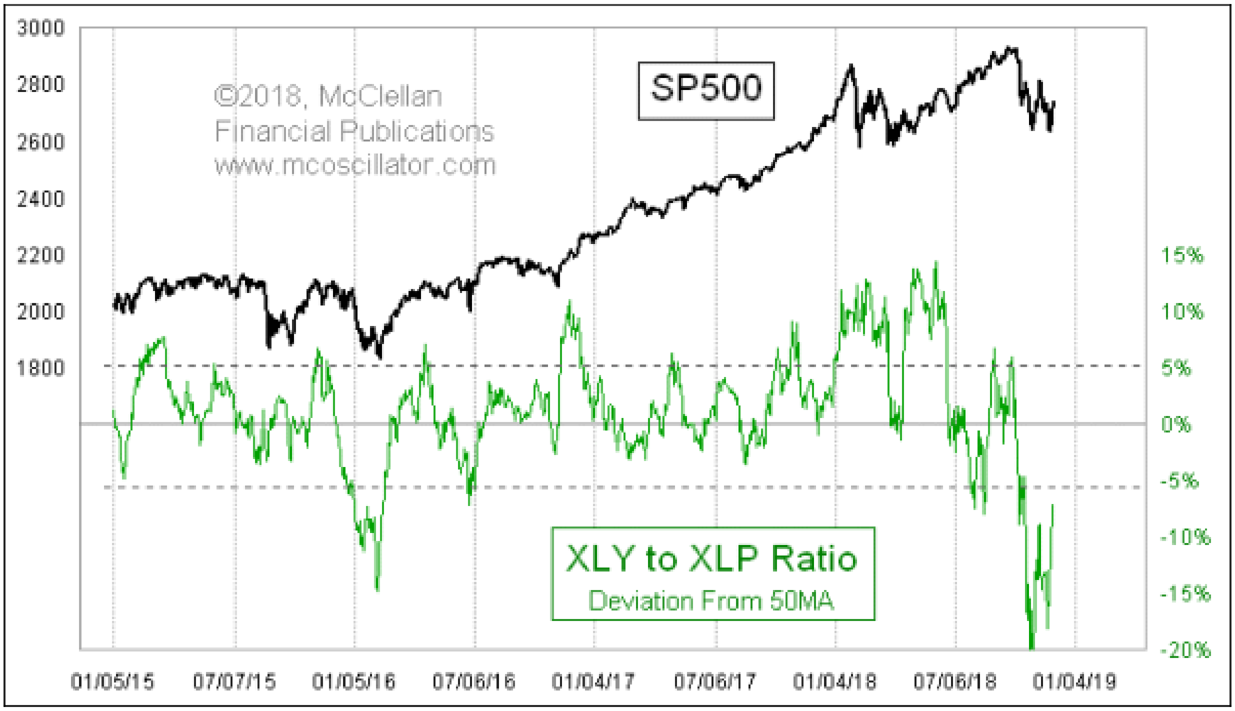
So, if investors perceive a change of attitudes or of spending behavior, they bail out of the stocks of the Consumer Discretionary sector more so than out of the Consumer Staples. That shows up as a movement downward for the relative strength ratio of the two.

My one quibble about how Standard and Poor's has configured the rosters of these two sectors is that Starbucks (SBUX) is the 5th highest weighted stock in the Consumer Discretionary sector. A lot of the Starbucks customers who I know do not consider their spending at that chain as optional.

The relative strength ratio in this week's chart is calculated very simply as the share price of XLY (Discretionary) divided by that of XLP (Staples). When it is moving higher, that means the Consumer Discretionary sector is outperforming Consumer Staples on a relative basis. And this is a condition which is reliably associated with an uptrend for the overall stock market, as modeled here by the SP500.

This relative strength ratio gave us a warning of trouble when its September and October 2018 tops failed to move higher than its June top, showing a bearish divergence. It confirmed that trouble was here when it plunged aggressively through its 50-day moving average (50MA).

By the time that the SP500 made its twin bottoms on Oct. 29 and Nov. 20, the relative strength ratio had fallen so far below its 50MA that it was actually showing a huge oversold condition. This indication can best be seen in the next chart, which shows an indicator measuring how far the relative strength ratio has moved away from its 50MA:



Under normal market conditions, this indicator shows an extended condition when it goes beyond around +/-5%. But at its extreme low in October 2018, it went all the way to -20%, revealing that in a period of just a few weeks, investors had fled thoroughly out of the Consumer Discretionary sector. That reading exceeds even what occurred in the 2008 bear market (not shown here).

With that extreme low posting now yielding to an upturn for this indicator, the message is that the flight out of Consumer Discretionary was so extreme that it just about cannot get any worse. So that means it should only be able to get better (unless the sky really is falling).

Tom McClellan, Editor,

The McClellan Market Report

BW: Information on Tom McClellan and *The McClellan Market Report* and *The Daily Edition* is provided on the following 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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