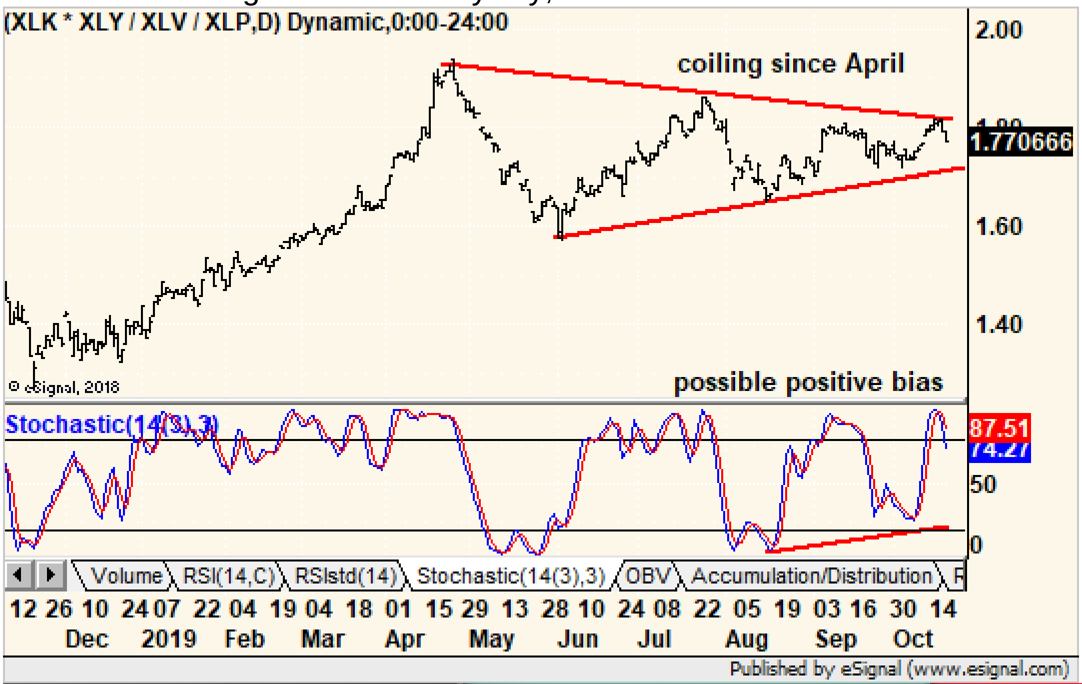
RIA Advice

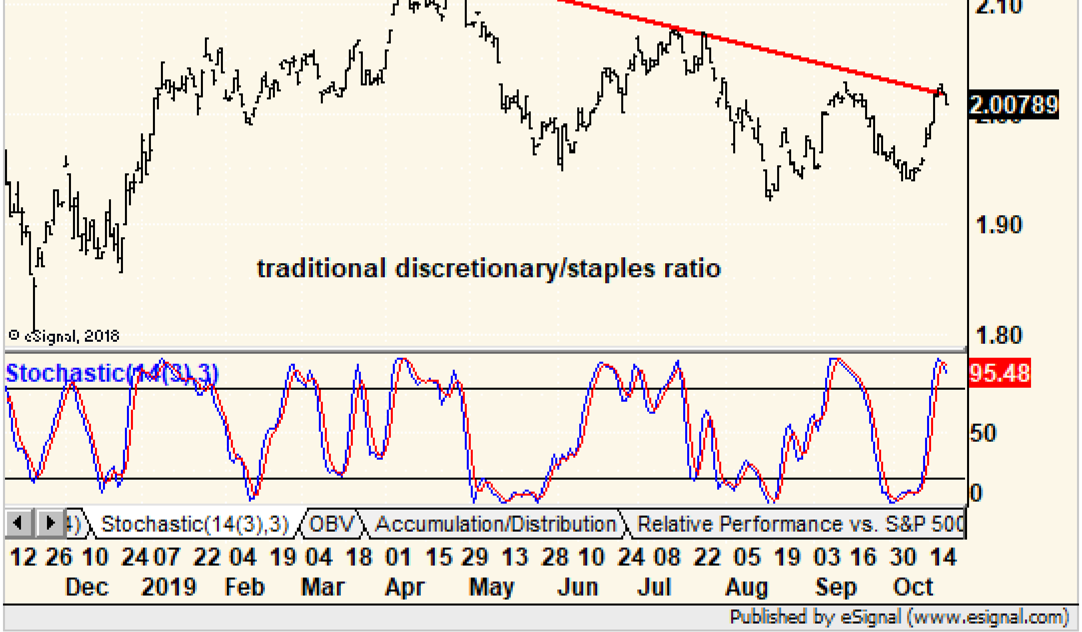
Fundamental analysts love ratios. Earnings per share, price to book, profit margin ? you name it, they?ve got it.

But technical analysts like ratios, too, and one of them is telling us that this bull market is not over yet. Many years ago, a technical analyst named Boris Simonder, with whom I've lost touch, showed me his offense/defense index, which he created from a proprietary classification of stocks deemed part of the "offense," such as technology, and stocks deemed part of the "defense," such as consumer staples. I adapted it to use standard SPDR ETFs and have been following it ever since.

Here's the formula: (XLK * XLY) / (XLP * XLV) or, if you prefer: XLK * XLY / XLP / XLV That's tech and consumer discretionary in the numerator and consumer staples and health care in the denominator.• And you may have noticed that it is an expansion on simpler XLY / XLP ratio many analysts now use. We can argue on the specifics and you may think you want to substitute utilities for health care or some other tweak. Go ahead and float that boat but for this missive, I'll stick with what's been doing OK for me. Anyway, take a look at this chart:



That's a nice coiling pattern for my version of the offense/defense index. And you might think that we're in a small decline within that pattern right now. I agree. But stochastics applied to the ratio shows a higher low on the last price swing lower. For regular stocks and indices, that suggests a bit of internal strength and there is no reason why it should not apply here. Of course, we have to wait for the actual breakout to declare the bulls to be in charge but this is certainly a better picture than that of the traditional discretionary / staples ratio:



This also looks like resistance is at hand and it shows no encouragement in stochastics. Perhaps the lack of lower low in Sep/Oct is bullish but I'd like to see the index hold near the trendline and then make the breakout attempt. Consider this one more, albeit small, bit of evidence that this bull market is not over yet.