



Playing the Investment Piano With Both Hands – Part 3

Saul Seinberg

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BI Online Chapter



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The Roles of Fundamental Analysis and Technical Analysis

- Using fundamental analysis and a growth methodology, we follow BetterInvesting principles to buy shares of companies that meet BI selection criteria or sell shares of companies that do not
- However, as described in Part 1 of this series, the fundamental data needed to analyze a company is only updated quarterly and is often otherwise stale, fundamentals don't account for psychological market pressures
- Technical analysis helps overcome such issues and thereby supplements the primary fundamental based analysis we use
- In other words, fundamental analysis helps identify the companies whose shares we want to buy or sell while technical analysis plays a supporting role and assists us in deciding when to buy or sell those shares



Prior Technical Analysis Topics

- In Part 2 of this series, we reviewed the two main types of charts in use today (bar charts and candlestick charts) and several predictive chart patterns found on these charts, along with individual stock indicators, support and resistance areas
- We also noted the need to confirm patterns and signals
- In this presentation, Part 3 of the series, we'll look at several additional TA topics that are different than the categories previously discussed
- It is important to keep in mind that effective technical analysis welcomes the intelligent combination of the patterns, indicators, signals and techniques discussed in this presentation series



New Technical Analysis Topics

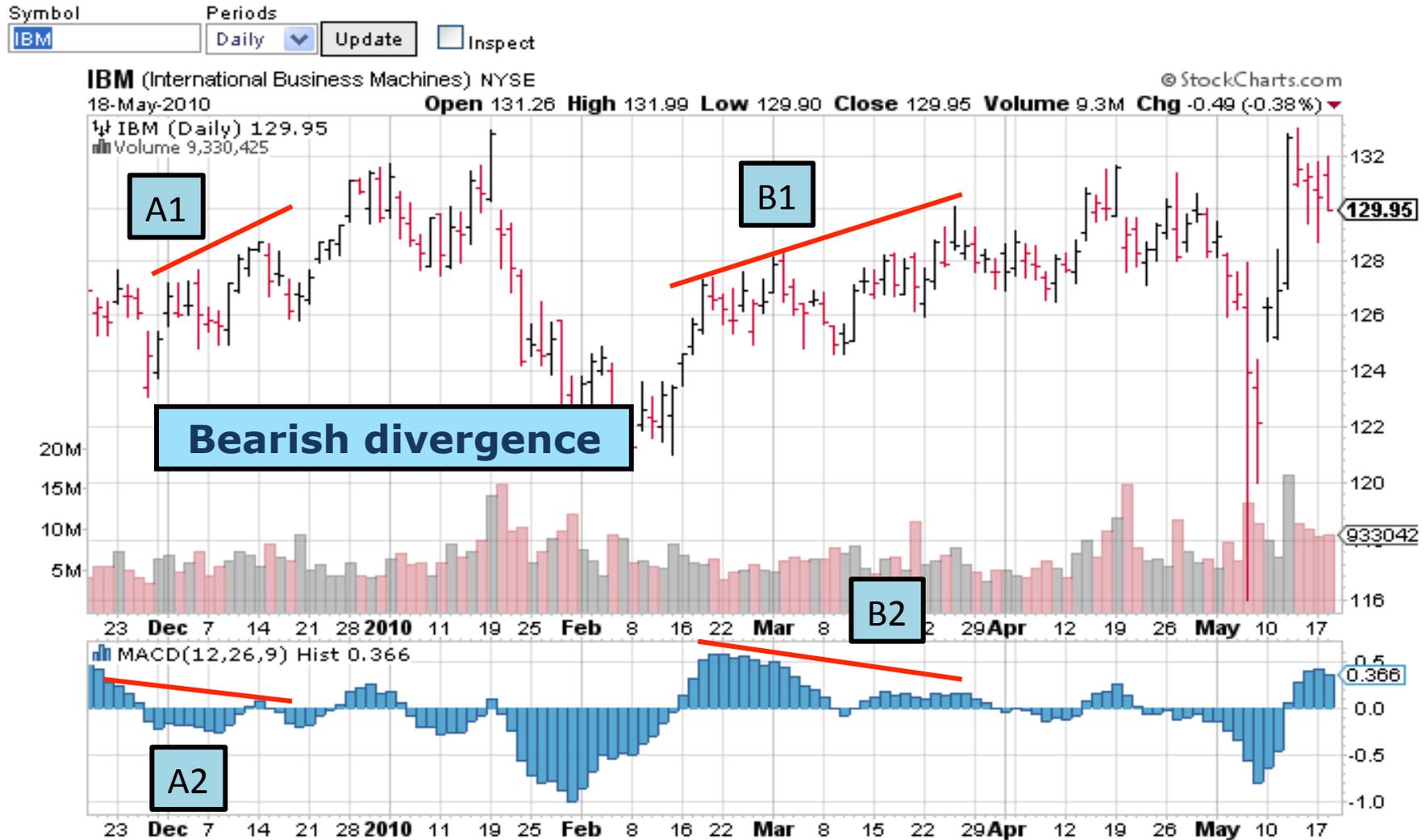
- Playing The Investment Piano – Part 3 topics
 - Divergence
 - Market Sentiment Indicators
 - Relative Strength + Relative Performance
 - Putting It All Together
 - FA+TA Example 1 (PLOW)
 - FA+TA Example 2 (ESS)
 - FA+TA Example 3 (BEAT)



Divergence

- Divergence based signals are effective and should influence a buy or sell decision when present
- Divergence occurs, and buy and sell signals are created, when a price chart trend is opposite to a trend shown by an indicator
 - Bearish divergence occurs when the price chart trend is up and the MACD histogram trend is down
 - Bullish divergence occurs when the price chart trend is down and the MACD histogram trend is up
- When a divergence situation appears, you should expect the price chart to follow the indicator trend
- The possible change in the price chart will usually not be immediate and may take a few weeks to develop

Bearish Divergence



Bullish Divergence (HD)

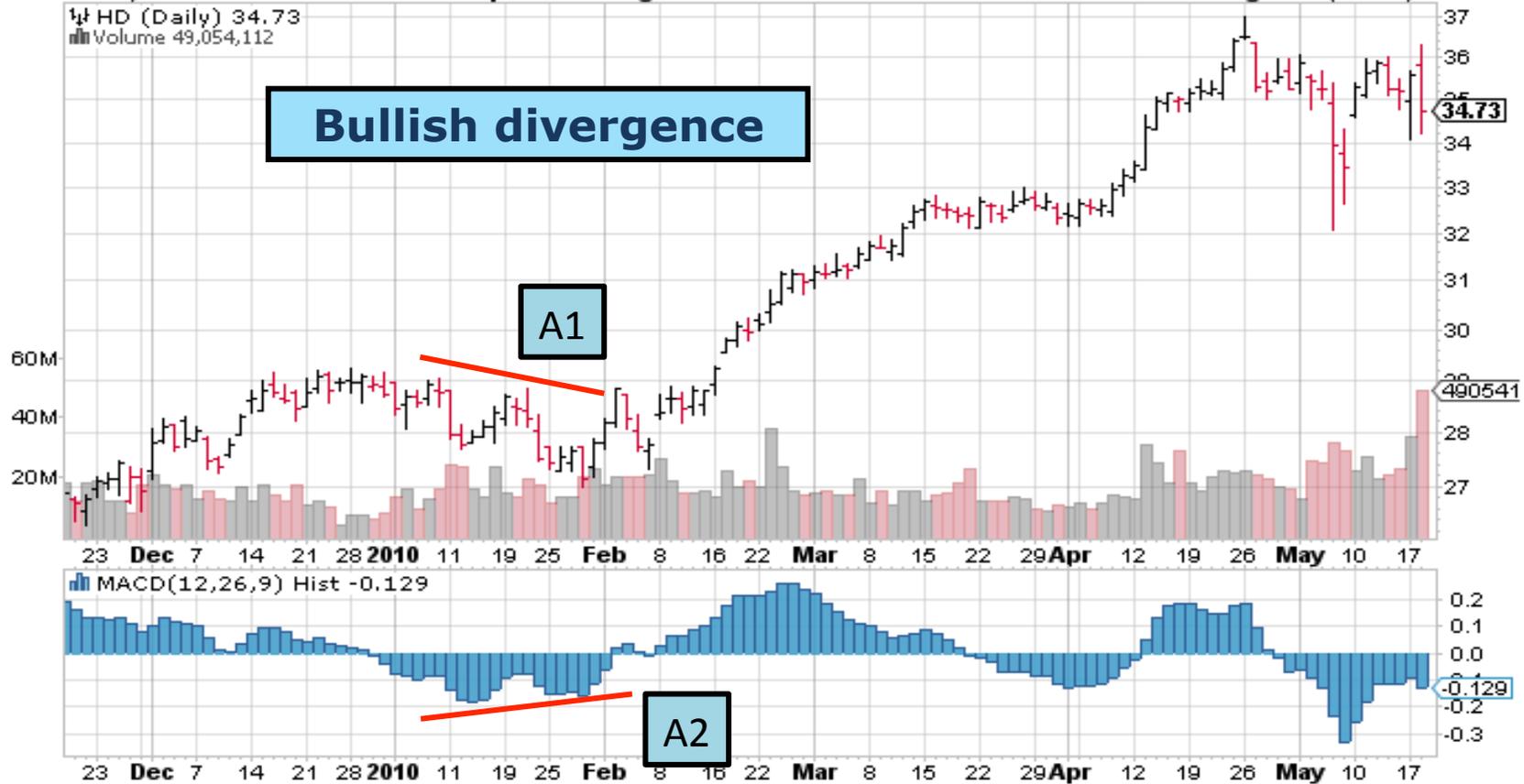
Symbol Periods Inspect

HD (Home Depot, Inc.) NYSE
18-May-2010

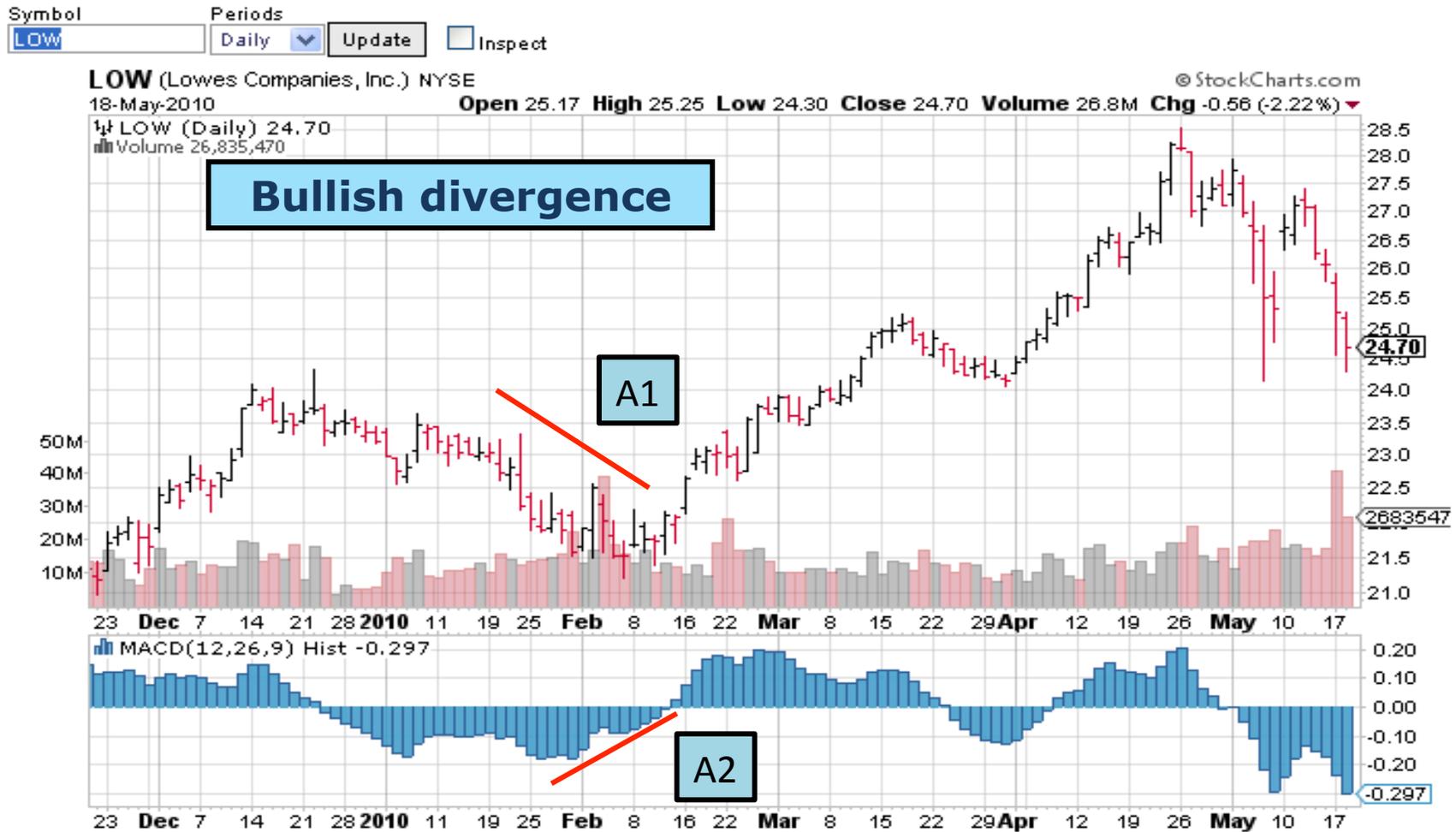
Open 35.81 High 36.30 Low 34.23 Close 34.73 Volume 49.1M Chg -0.86 (-2.42%)

© StockCharts.com

HD (Daily) 34.73
Volume 49,054,112



Bullish Divergence (LOW)





Market Sentiment Indicators

- Every self-respecting technical analyst uses a sentiment indicator or two
- Sentiment indicators are used to identify levels of overall investor optimism or pessimism in the financial markets; also referred to as “top down” analysis
- There are many market sentiment indicators used every day by all types of investors
- When sentiment indicators lean too far in either direction, we can expect that a reversal will occur; when is always the question!
- Some investors hold back when top down is discouraging, others don't care and focus on individual investments, “bottoms up”; your choice!



Market Sentiment Indicators

- How much we let the value of a sentiment indicator influence us depends on how strictly we adhere to a top down approach
- It's tempting to follow your individual stock study analysis despite what top down advises when you are satisfied with the results of your stock study
- However, if you have reservations about buying, holding or selling a stock in the face of market weakness, then it's definitely appropriate to use a sentiment indicator or two to resolve your stock study conclusion



Market Sentiment Indicators

- Sentiment indicators help provide a top down, contextual feel for the markets
- It usually takes an initial effort to understand sentiment indicators and what their results mean
- Thus, it's best to pick one sentiment indicator and stick with it for awhile and get to know how well it works for you
- Note that many investors use sentiment indicators without realizing it; e.g. "What is DJ-30 or S&P 500 doing today?"



Market Sentiment Indicator Examples

- Here are some widely used sentiment indicators
 - Market Averages (DJ-30 or S&P 500)
 - Percent above or below SMA of a market index
 - Advances vs. Declines (number of stocks in each category)
 - Advancing Volume vs. Declining Volume (volume of stocks in each category)
 - Put/Call Ratio
 - Short Ratio
 - VIX
- There are other sentiment indicators in use besides the above examples



Sentiment Indicators - % Above SMA

- StockCharts provides charts of the main indexes that illustrate a unique view of the 50, 150 and 200 day SMAs for the index they measure
- These charts respectively indicate the number or the percentage of stocks in a market index that have closing prices above their respective 50, 150 and 200 day SMA values
- A relatively high or low number or percentage shows overbought or oversold conditions as a percentage of the associated SMA
- Long term investors may just stick with the % above for a 200 day SMA although use of the 150 day SMA yields quicker signals



Use Of Sentiment Indicators

- It's best to use the index and SMA term that suits your investing style and portfolio holdings
- Growth investors are best served by the 200 day SMA in measuring the sentiment of an index
- In StockCharts, I've found that the \$NYA200R (percentage) and \$NYA200 (number) charts produce helpful results for longer term investors; I sometimes use \$NYA150R (% or ratio) to get earlier signals
- On occasion, I also use the \$NYA50R to obtain a shorter term (50 days) view of the NYSE; gives a better feel for shorter term index activity



Use Of Sentiment Indicators

- In using the “% Of Stocks Above Their SMA” sentiment indicator, the key factor is the level shown on a particular day and your view of how much higher or lower the index or market segment being measured can go
- When the “% Of Stocks Above Their SMA” sentiment indicator reaches very low or very high values, it’s likely that those values cannot continue at such levels
- Thus, a change in the opposite direction can be expected to occur

% Of NYSE Stocks Above 200 SMA

Symbol Periods

\$NYA200R (NYSE % Above 200MA) INDX © StockCharts.com
22-Jun-2009 **Op** 56.65 **Hi** 56.65 **Lo** 56.65 **Cl** 56.65 **Chg** -8.66 (-13.26%) ▼



% Of NYSE Stocks Above 50 SMA

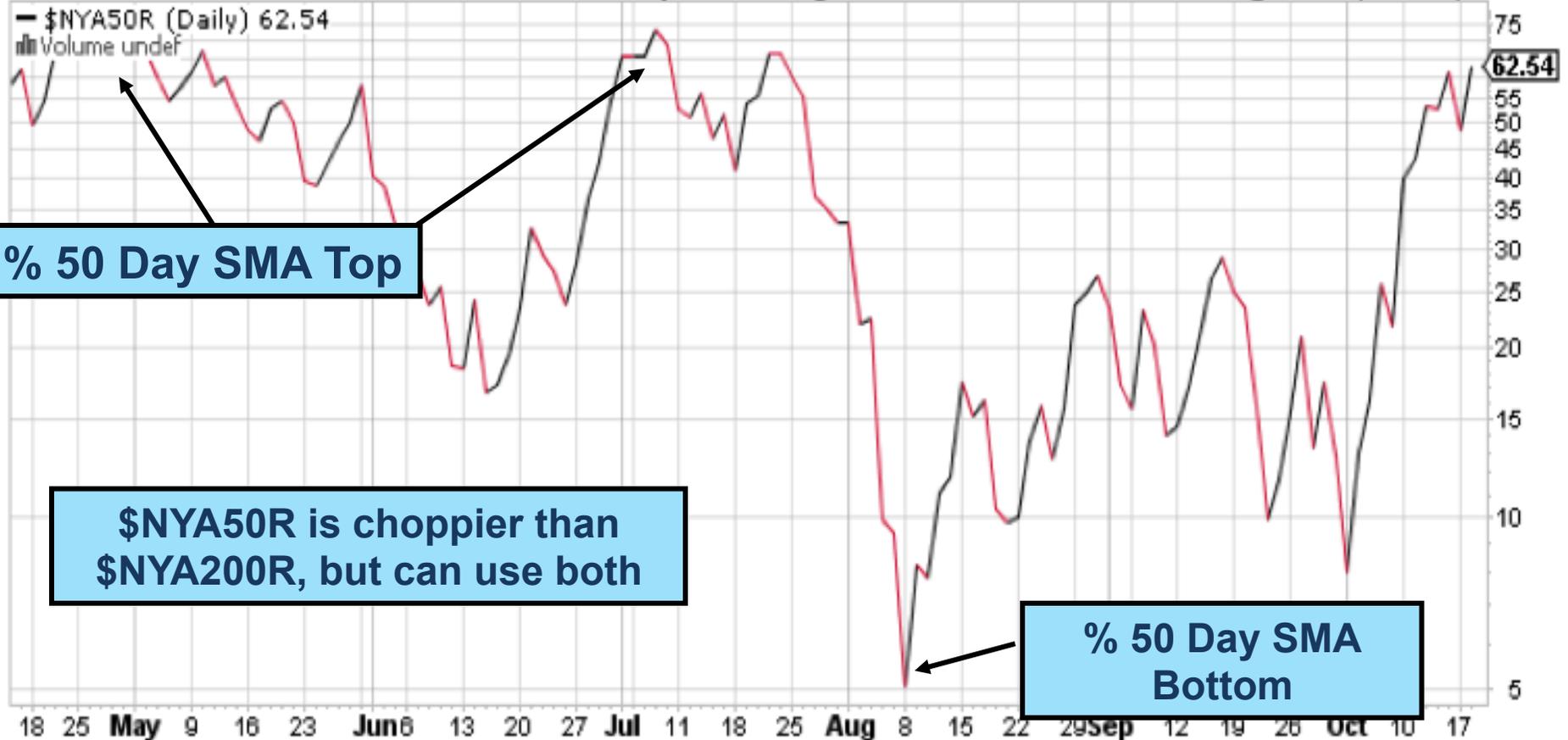
Symbol Periods Inspect

\$NYA50R (NYSE Percent of Stocks Above 50 Day Moving Average (EOD)) INDX

© StockCharts.com

18-Oct-2011

Open 62.54 High 62.54 Low 62.54 Close 62.54 Chg +13.82 (+28.36%) ▲



% 50 Day SMA Top

\$NYA50R is choppier than \$NYA200R, but can use both

% 50 Day SMA Bottom



What is Relative Strength?

- Relative Strength (RS) measures how well a stock, fund or index of choice is performing relative to another market index, sector, industry, stock or fund
- Relative Strength should not be confused with the Relative Strength Index (RSI), another popular technical analysis indicator, which measures how a stock, fund or index is performing with respect to its own past performance



What is Relative Strength?

- This part of the presentation will examine how Relative Strength can be employed by a typical growth, fundamental analysis based investor
- We will then do likewise for relative performance, which seeks to determine the best performer in a pairing or group of stocks, indexes or funds
- Relative strength is the basis of momentum investing



Why Care About Relative Strength?

- Wouldn't you want to pick a stock in a sector or industry that is outperforming the market as well as other sectors or industries
- If so, you should be very interested in relative strength and relative performance which relies on price based past performance
- Relative strength based investing gave rise to an increase in ETFs and analysts that specialized in momentum investing



Why Care About Relative Strength and Performance?

- Several academic studies have indicated that stocks with higher relative performance outperform their peers going forward
- Other studies have shown that from 65% to 95% of a stock's performance is fairly well correlated to its sector's performance
- In other words, relative strength and relative performance add two useful metrics to an investor's TA arsenal of tools



What is Relative Strength and Relative Performance?

- Relative Strength is an excellent tool that can be used to supplement stock studies and comparisons with only a modest amount of investor study and experience
- Relative performance can steer you to a better choice in a sector or industry
- StockCharts offers a useful charts and tools for displaying and working with relative performance situations



Relative Strength In Action

- For Relative Strength examples in this presentation, I will compare
 - AFL to \$SPX (S&P 500)
 - AFL to XLV (Health Care Spider)
 - AFL to UNM (Competitor)
- Relative Strength requires separate chart

Unlock Intraday Charting

Create 1-min, 5-min, 60-min intraday charts and more!

Become a StockCharts Member

Free Trial

Symbol Period

AFL Aflac, Inc. NYSE
4-Dec-2020

Open 45.41 High 46.35 Low 45.30 Close 46.29 Volume 4.8M Chg +0.60 (+1.31%) ▲



Default SharpChart for AFL

Top Chart Section

Chart Attributes

Period Range Bar Gap Extra Bars
Daily Fill the Chart 5 0

Type Size Color Scheme Up Color Down Color Legends
Candlesticks 700 Default - Auto - - Auto - Default

Volume: Overlay Full Quote Price Labels Log Scale Solid Candles Color Volume Smoothed Lines Y-Axis Labels Zoom Thumbnail

Update

Turn Volume "Off"

Overlays

Parameters

Simple Moving Avg 50
Simple Moving Avg 200
- None -

Update

Clear All

Turn SMAs "Off"

Default Chart Attributes
For AFL

Indicators

Parameters

Position

RSI Above
MACD Below
- None - Below

Update

Clear All

Leave RSI and MACD as is

Bottom Chart Section



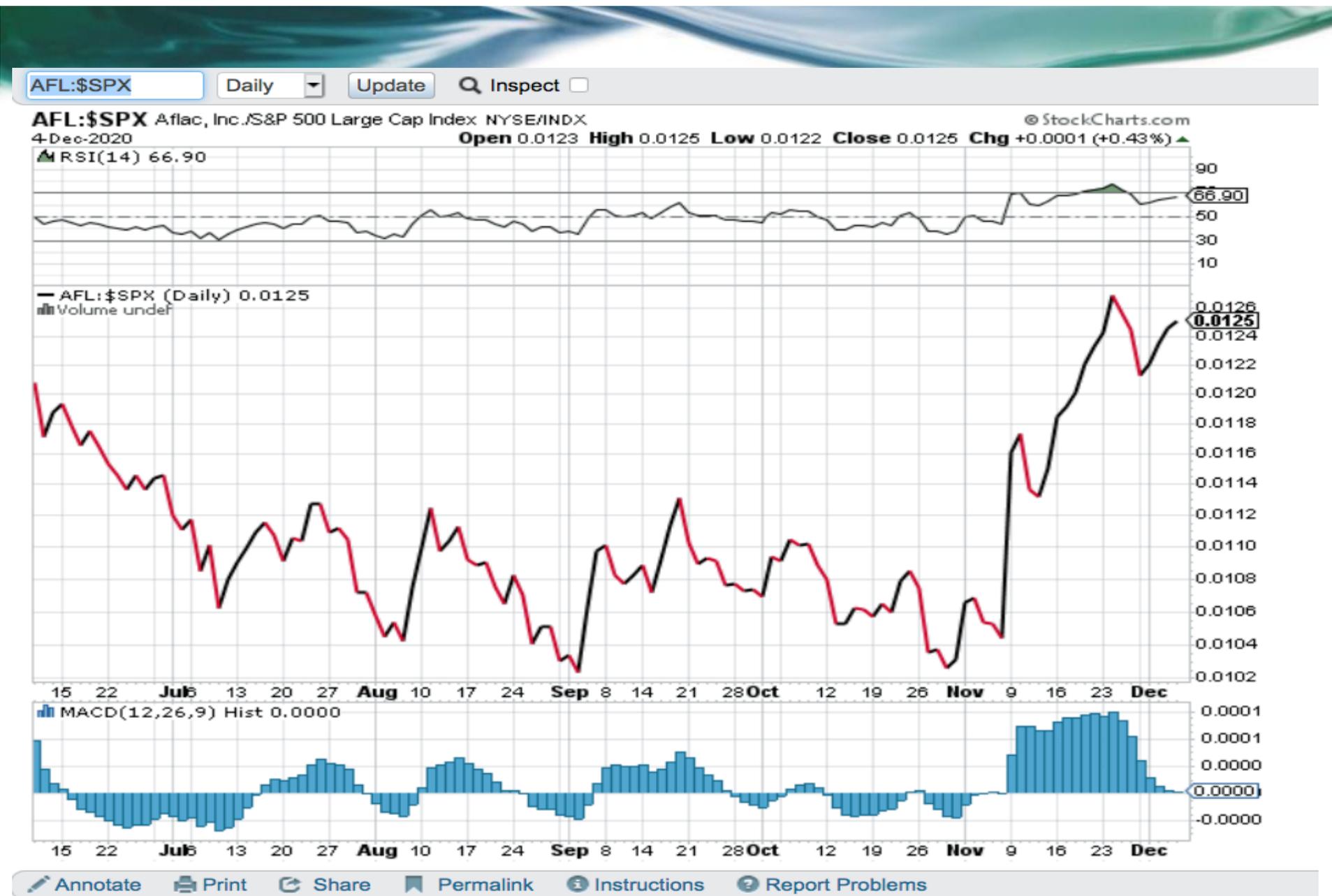
Relative Strength In Action

- In StockCharts, the relative strength chart compares two items using a joint symbol formed from the symbols of the two items of interest joined by a colon; such as “X:Y”
- To compare the relative strength of AFL to the S&P 500, we would type “AFL:\$SPX” in the symbol box
- That compares AFL to S&P 500 over the defined time span; ignore other indicators



Relative Strength In Action

- If the relative strength chart is trending up, then the first symbol in the symbol combination is performing better
- If the relative strength chart is trending down, then the second symbol in the symbol combination is performing better
- The black and red portions of the trend line show that the first symbol is outperforming if in black and underperforming when in red



Relative Strength AFL vs. \$SPX

Symbol

Period

AFL:XLV

Daily

Update

Inspect

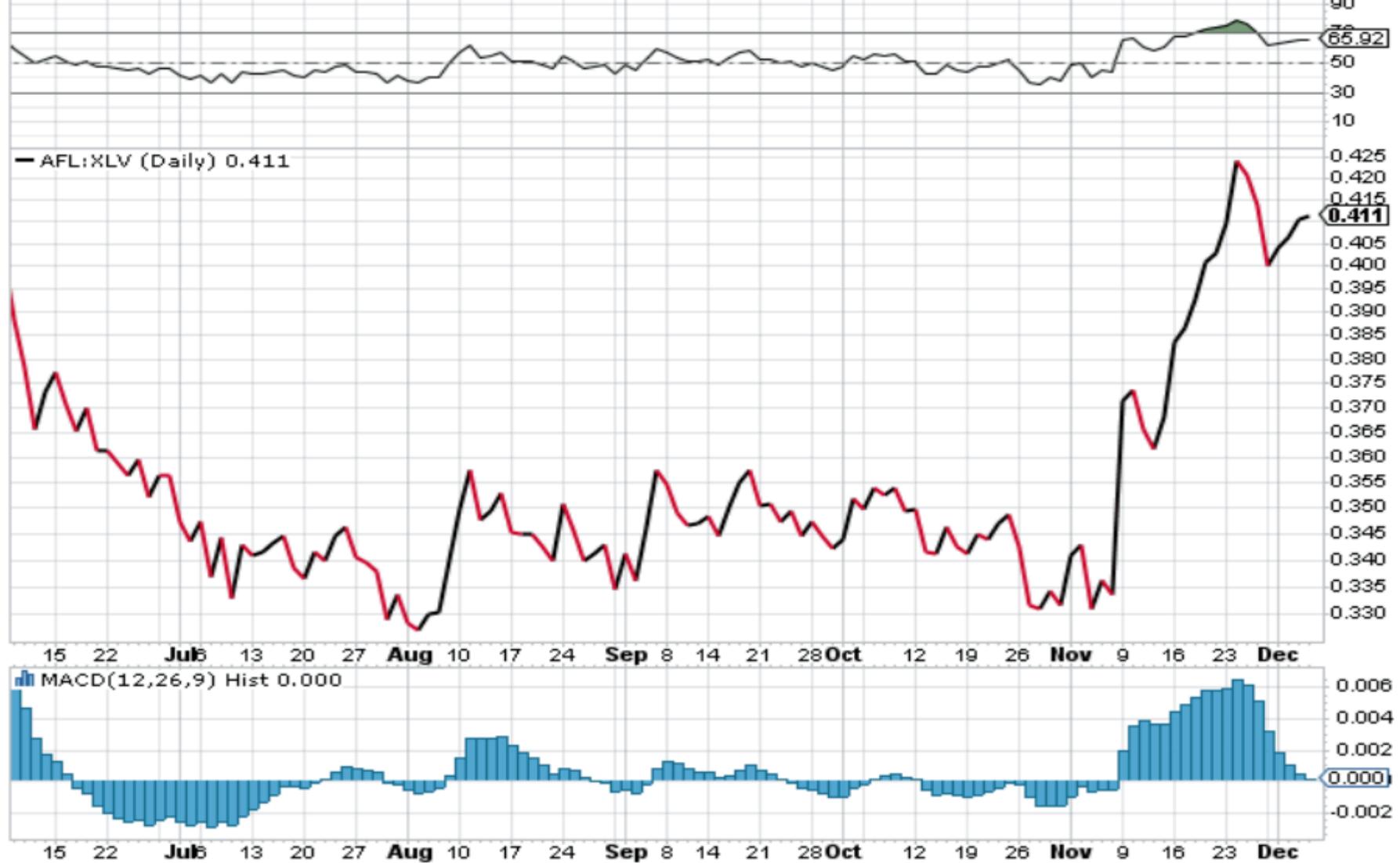
AFL:XLV Aflac, Inc./Health Care Select Sector SPDR Fund NYSE

© StockCharts.com

4 Dec-2020

Open 0.404 High 0.412 Low 0.403 Close 0.411 Chg +0.001 (+0.24%)

RSI(14) 65.92



Relative Strength AFL vs. XLV

Symbol Period

AFL:UNM Aflac, Inc./Unum Group NYSE

© StockCharts.com

4 Dec-2020

Open 1.872 High 1.911 Low 1.867 Close 1.908 Volume 1 Chg -0.044 (-2.24%)

▲ RSI(14) 41.36

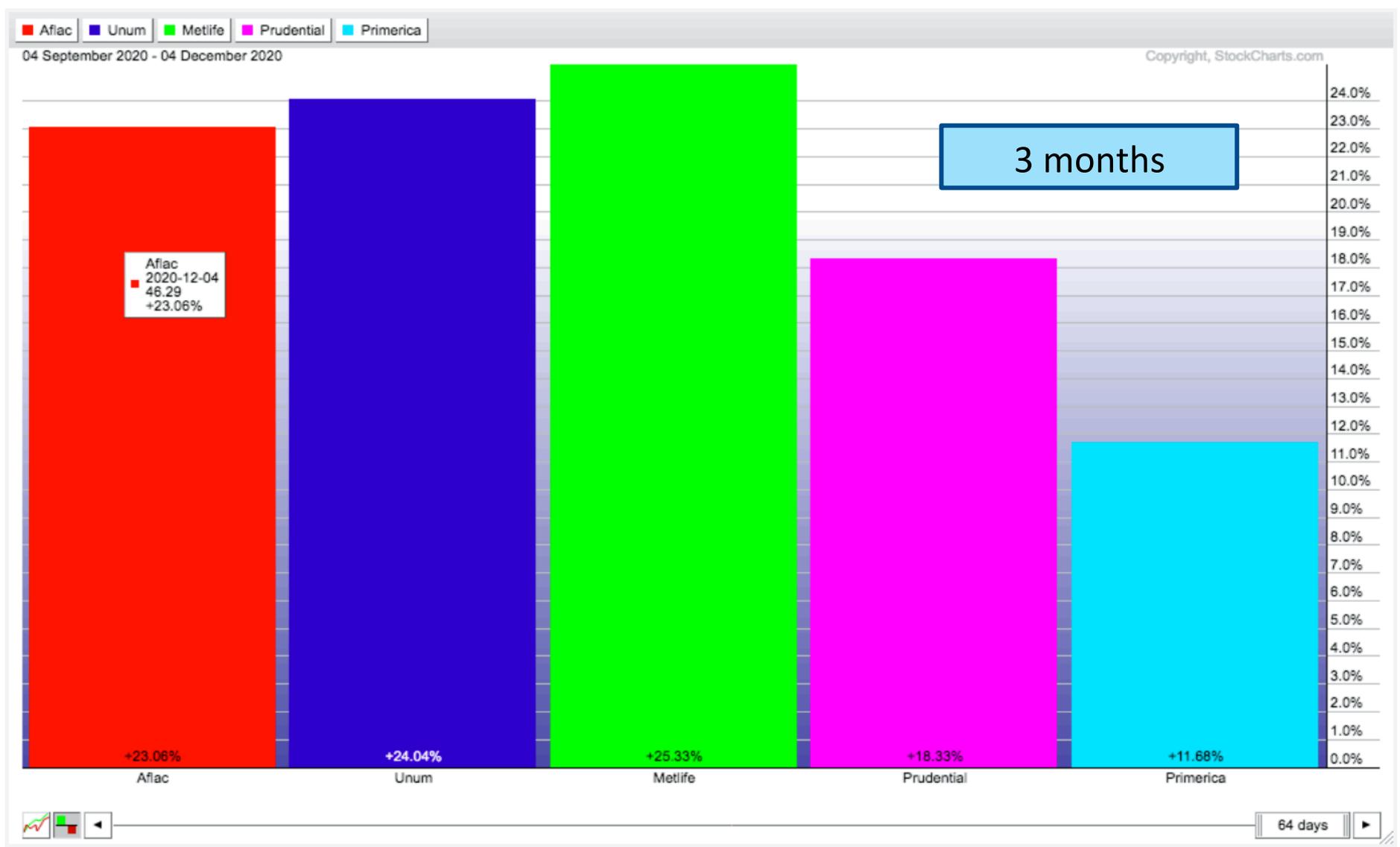


Relative Strength AFL vs. UNM

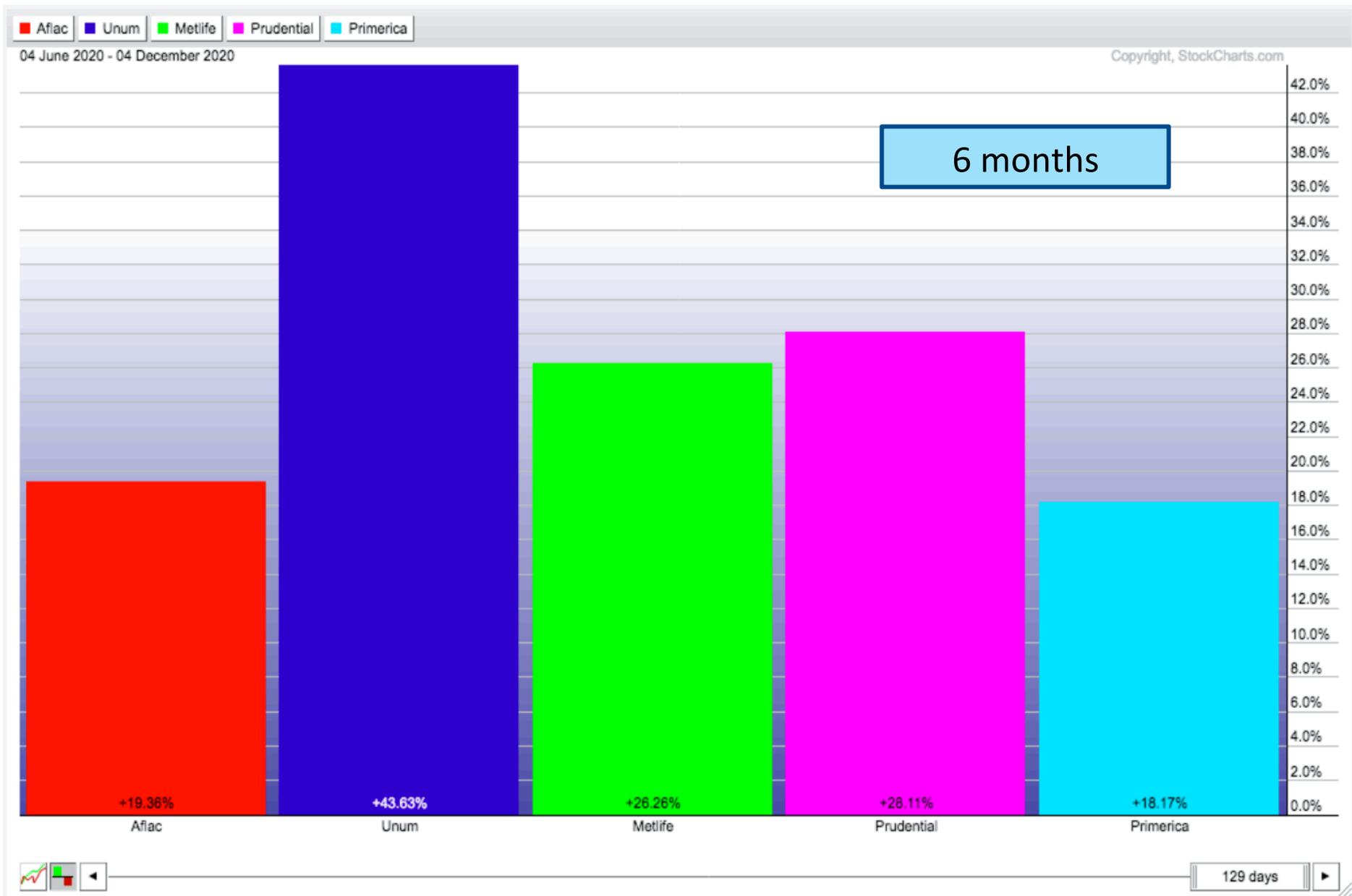


What is Relative Performance?

- Relative performance charts or PerfCharts, are available on the free side of StockCharts; they use a different chart
- They were discussed in Part 1 of this series; slides 42 – 52
- Relative performance charts are a helpful way to display relative strength results for pre-defined sets of stocks, indexes
- Excellent starting point for review of individual or club portfolios



Relative Performance Of AFL Competitors 33



Relative Performance Of AFL Competitors 34



Saving SharpCharts At StockCharts

- The free service at StockCharts doesn't permit a user to save their SharpCharts, particularly a chart's indicator set-ups and defaults
- You can annotate charts, but annotations not saved in free side of StockCharts
- After your chart is set-up as desired, say for WBA, scroll to "Permalink" at bottom of chart, click that link and bookmark the result; creates a template
- When you return to StockCharts, open the bookmarked link and change the stock symbol to reuse the chart set-up you previously created for WBA; Permalink can be used over and over

Saving StockCharts



Annotating Charts





Chart Setup For StockCharts

- The default chart, called a SharpChart, that you get at the StockCharts site is usable, but not as helpful as a setup modified to your preferences
- After your chart is set-up as desired, you can do the Permalink save as described on the previous slides, but what should a workable setup look like
- For starter purposes, we save some of the default indicators and view, but change others



Chart Setup For StockCharts

- I'd start by keeping RSI, the candlestick price chart, MACD Histogram and time frame
- Next, I would retain the 50 and 200 day moving price graph averages
- I would move Volume to a separate block
- Then I would add the Chaikin Money Flow
- I would keep all the indicator defaults and then click "Update" to make these changes
- At this point, you can click on "Permalink"

Setup - Modified Top Of Chart



Setup – Modified Chart Attributes



[Annotate](#)
[Print](#)
[Share](#)
[Permalink](#)
[Instructions](#)
[Report Problems](#)

Chart Attributes

Period	Range	Bar	Gap	Extra Bars				
Daily	Fill the Chart	5	0					
Type	Size	Color Scheme		Up Color	Down Color	Legends		
Candlesticks	700	Default		- Auto -	- Auto -	Default		
Volume:	<input type="checkbox"/> Full Quote	<input type="checkbox"/> Price Labels	<input checked="" type="checkbox"/> Log Scale	<input type="checkbox"/> Solid Candles	<input checked="" type="checkbox"/> Color Volume	<input checked="" type="checkbox"/> Smoothed Lines	<input checked="" type="checkbox"/> Y-Axis Labels	<input type="checkbox"/> Zoom Thumbnail
<input type="button" value="Update"/>								

Overlays

	Parameters
Simple Moving Avg	50
Simple Moving Avg	200
- None -	

Indicators

	Parameters	Position
RSI	14	Above
MACD Histogram	12,26,9	Below
Chaikin Money Flow (CMF)	20	Below



Using The Personalized Chart

- The default chart has been modified and a third indicator (CMF) added to help with confirmation; various other changes made to personalize the chart
- We're now going to take a look at three stocks recently recommended as buys by IAS to see if playing the piano with both hands helps make those buy decisions a little easier to carry out
- The three stocks are:
 - PLOW (11/20)
 - ESS (9/20)
 - BEAT (10/20)

Modified Chart – PLOW



Modified Attributes – PLOW

Chart Attributes

Period	Range	Bar	Gap	Extra Bars					
Daily	Fill the Chart	5	0						
Type	Size	Color Scheme	Up Color	Down Color	Legends				
Candlesticks	700	Default	- Auto -	- Auto -	Default				
Volume:	Separate	<input type="checkbox"/> Full Quote	<input type="checkbox"/> Price Labels	<input checked="" type="checkbox"/> Log Scale	<input type="checkbox"/> Solid Candles	<input checked="" type="checkbox"/> Color Volume	<input checked="" type="checkbox"/> Smoothed Lines	<input checked="" type="checkbox"/> Y-Axis Labels	<input type="checkbox"/> Zoom Thumbnail
<input type="button" value="Update"/>									

Overlays

Parameters

Simple Moving Avg	50
Simple Moving Avg	200
- None -	
<input type="button" value="Update"/> <input type="button" value="Clear All"/>	

Modified attributes are the same for ESS and BEAT

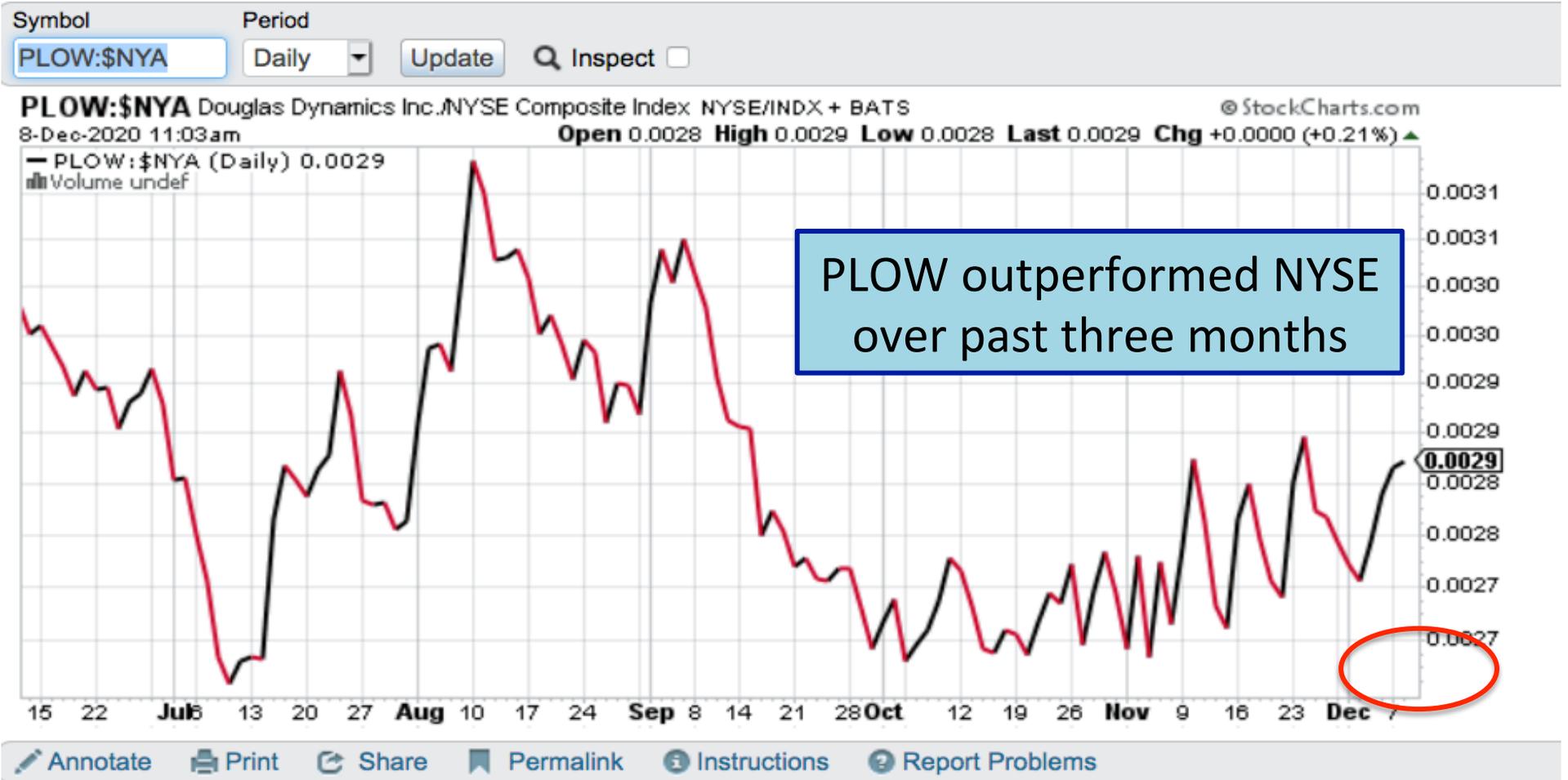
Indicators

Parameters

Position

RSI	14	Above
MACD Histogram	12,26,9	Below
Chaikin Money Flow (CMF)	20	Below
<input type="button" value="Update"/> <input type="button" value="Clear All"/>		

PLOW Relative Strength v. NYSE



Modified Chart – ESS



ESS Relative Strength v. NYSE



Modified Chart – BEAT



BEAT Relative Strength v. NYSE





Summary

- It pays to remain aware of divergence even when reviewing charts for other reasons
- If you're having difficulty picking from two or more investments, remember to look at relative strength and relative performance of possible investments
- Reduce time span to give better view of candlesticks
- Standardize on a chart layout and set of indicators
- Give your layout and indicators a chance to work, but don't be reluctant to experiment and try other charts/indicators over time
- Looking for confirmation between patterns or indicators is still an important thing to do
- If you're not sure, move on, always other opportunities



Future Presentations Vote For Top Three

- Options for Fundamental Investors <A
- Dividend Growth Investing <B
- Trailing Stop Loss Orders <C
- Asset Allocation Based Investing <D
- Trend Analysis <E
- Price Chart Gaps – Friend or Foe <F



**Playing The Investment Piano With
Both Hands**

Questions ?

saul.seinberg@gmail.com