The Disciplined Investor Podcast – Guest Interview Summary

Guest: Tom McClellan

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Fosbach Absolute Breadth Indicator Discussion

Andrew and Tom discussed the Fosbach absolute breadth indicator, which measures market activity by looking at the cumulative sum of daily advancing and declining issues without considering direction. Tom explained that when this indicator reaches quiet levels, typically indicated by a 21-day moving average, it suggests a topping condition in the market, though not necessarily the exact moment of a top.

Market Conditions and Indicators Discussion

Tom and Andrew discussed market conditions and indicators, with Tom emphasizing that while current complacency might signal a potential market move, the magnitude of any move remains uncertain due to various external factors. Tom advised focusing on getting the direction right rather than attempting to predict both direction and magnitude, as market timing secrets are only revealed after the fact. The conversation concluded with Andrew seeking clarification about using a 21-day moving average, confirming it refers to calendar days rather than weeks.

Moving Averages in Market Analysis

Tom explained that when technical analysts refer to moving averages like 50-day or 200-day averages, they are using trading days rather than calendar days, as trading days are what matter for market analysis. He noted that 21 trading days approximately equals one month and recommended using a 21-day moving average for the Fosbach Absolute Breadth indicator. Andrew suggested that the significance of standard moving averages like 50, 100, 150, and 200 days might come from collective investor attention rather than intrinsic market relevance, to which Tom agreed there was truth in that concept and explained that effective moving averages should align with inherent market cycles, using half the cycle period.

Exponential Moving Averages in Trading

Tom and Andrew discussed different approaches to moving averages in stock market analysis, with Tom explaining that exponential moving averages are mathematically superior to simple moving averages due to their reliance on only new data and distance from the moving average. Tom shared how his parents, Sherman and Marion McClellan, and Pete Harlan, a rocket scientist at Jet Propulsion Lab, pioneered the use of exponential moving averages in the 1960s. The conversation concluded with a discussion about oil prices, noting that while the upturn was on schedule, it was overdone due to the Iran war, and they began to explore what the normalization in oil prices might indicate.

Oil Price and Gold Correlation

Tom explained that oil prices tend to follow gold prices with a 20-month lag, based on historical patterns that have worked for decades. He noted that while the recent war with Iran caused oil prices to deviate significantly from this pattern, the underlying upward trend should resume as gold's price movement from 20 months ago indicates. When asked about the 20-month timeframe, Tom acknowledged it works well but couldn't provide a definitive explanation for why this specific lag period is effective.

Market Analysis and Podcast Discussion

Tom explained his market analysis services, including the McClellan Market Report newsletter and daily market updates available through MCOscillator.com. He mentioned that his father Sherman, who is 92 years old, still collaborates with him on the newsletter. Andrew noted that his podcast will celebrate its 20th anniversary in March 2027, and they discussed the evolution of podcasting since its inception in 2007. The conversation ended with Andrew asking Tom about the difference between complex and simple McClellan oscillator structures, though this question was not fully answered in the provided transcript segment.

McClellan Oscillator Market Analysis

Tom explained the McClellan Oscillator, a tool developed by his parents that measures market acceleration, and described how positive and negative readings indicate upward or downward trends. He discussed the importance of complex versus simple structures in the oscillator, noting that complex structures below zero indicate bears are in charge, while simple structures suggest a side is not in control. Tom also mentioned the current market situation, observing that while the NYSE Advanced Decline Line is making new highs, other indicators like high-yield bonds are not following suit, indicating a divided market that aligns with typical bear market patterns seen in the second year of presidential terms.

Market Conditions and Trading Analysis

Tom discussed the current market conditions, predicting a slow and boring period until mid-October with limited opportunities for nimble traders. He explained his analysis of divergences between NVIDIA and the NASDAQ 100 index, noting that when NVIDIA peaks before the index, it often signals weakness in the overall market. Tom also discussed the S&P 500 choppiness index reaching multi-decade lows, indicating the market was due for more nonlinear price movements after a very linear uptrend. When asked about reliable indicators, Tom emphasized the importance of looking at plain bar charts to determine trend direction, while also using various technical indicators like RSI and breadth measures. He concluded by noting that the Federal Reserve's ongoing quantitative easing program is supporting market stability, though any changes to this policy would likely impact market performance.