TRADING Basics

# Market breadth

*Breadth indicators are designed to reflect the market's "internal" strength by comparing the number of rallying vs. declining stocks.*

BY ACTIVE TRADER STAFF

Breadth is a term applied to data or calculations other than those based on price — most commonly, comparisons of the number of stocks rising vs. the number falling, but also sometimes incorporating volume. Breadth indicators are sometimes referred to as the market's "internals" — implying they reflect internal strength or weakness that might not be evident directly in price — and many traders look to various market breadth tools to confirm or discredit the existing trend.

Examples of breadth measurements include the number advancing vs. declining stocks, advancing vs. declining volume, new highs vs. new lows, and combinations of these data. Also, a number of derivative indicators have been developed using these numbers — various ratios, moving averages, and oscillators based on breadth data.

The most commonly promoted "confirming" application of market breadth is for advancing stocks to outnumber declining stocks when the market is rising, and vice versa when the market is declining. A deviation from this pattern — for example, declining stocks outnumbering advancing stocks when the market is rising — is typically interpreted as a sign of internal weakness in the trend. Traders also sometimes look for specific "divergences" between price and a breadth indicator to indicate a turning point — for example, price making a higher high when the indicator makes a lower high.

Some of the most common breadth indicators include:

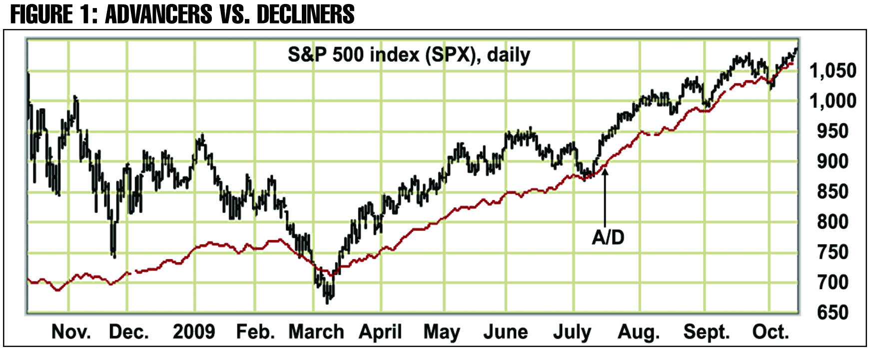
- **The advance-decline line (A-D line):** A day-to-day running total of the number of stocks that have closed higher on the day (advancing) minus the number of stocks that have closed lower on the day (declining).

- **52-week highs/lows:** On a given day, the number of stocks making new 52-week (one-year) highs vs. the number making new 52-week lows.

- **The Arms Index (TRIN):** The ratio of the number of advancing stocks to declining stocks divided by the ratio of the volume of advancing and declining stocks.

- **TICK:** A real-time measurement of the difference between the number of upticking NYSE stocks vs. the number of downticking NYSE stocks (stocks trading at a price higher than the previous trade vs. those trading below it). "TIKI" is the symbol for the same indicator calculated on Dow Jones Industrial stocks. Many data services also supply the TICK for Nasdaq stocks.

**FIGURE 1: ADVANCERS VS. DECLINERS**




The A-D line is a running total of the number of stocks closing higher on the day vs. those closing lower on the day.

Source: BigCharts.com

Figure 1 shows a daily chart of the S&P 500 index with the advance-decline line.

The commonly ascribed roles and usefulness of these and any other indicators should be viewed cautiously until you have performed extensive research and testing of a particular indicator application. What indicators are *supposed* to do — and what they do in isolated instances — can be very different from what they do over the long term. The first three articles in the "Related reading" box include historical test results for certain breadth indicator applications.

## Related reading

**"Catching the market's breadth"**
*Active Trader*, October 2008.
Detailed historical analysis of what the market does after days when there's a big difference between advancing and declining stocks.

**"The 52-week high-low difference"**
*Active Trader*, September 2008.
Imbalances between the number of stocks making 52-week highs vs. 52-week lows are tested to see if they identify market turning points.

**"Indicators that work — but not like you think"**
*Active Trader*, June 2002.
Analysis of the advance/decline ratio (ADR) and the Arms Index (TRIN) illustrate the reality of applying indicators in the market.

**"Indicator Insight: Advance-decline line"**
*Active Trader*, June 2001.
A Trading Basics article describing the advance-decline (A-D) line, a breadth indicator designed to measure aspects of supply and demand not always reflected directly in price.

**"Technical Tool Insight: New highs/new lows"**
*Active Trader*, March 2002.
A Trading Basics article outlining 52-week new highs/new lows.

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