CHART PATTERNS

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MARKET UPDATE

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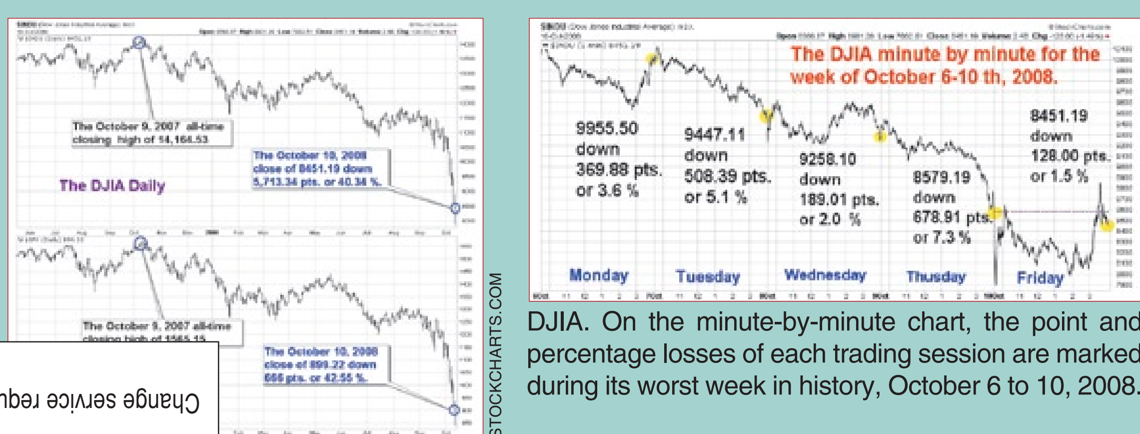
S&P 500 DAILY VS. S&P 500 ONE-MINUTE



DJIA. On the minute-by-minute chart, the point and percentage losses of each trading session are marked during its worst week in history, October 6 to 10, 2008.

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"The Current Financial Crisis Offers the Absolute BEST Conditions For Trading, Lots of Movement, which provides unprecedented opportunities."

Interview Dr. John Meyer — A Trader Using AbleTrend 7.0

Dr. Meyer, how long have you been trading?
I've been trading in the futures markets for 10 years.

What do you trade?
I day trade the S&P e-mini and trade FOREX on daily charts.

What is your occupation?
I am a radiologist (MD).

How many other trading software programs did you use before using AbleTrend?
I have used several other software programs but none has the power of AbleTrend. Specifically, none of the others has the power to find trend changes early and reliably and, then, to follow the market very precisely. Using the default settings, AbleTrend lets a trade develop and controls potential losses well. A trade needs to "BREATHE." The market tells the trader where it is going so that he or she can confidently follow it and make money. The program does this in real time better than any human can!

I have used Bill Williams' "Profitunity" indicators but they are imprecise and tend to build a large pyramid that crashes against a position. I tried Advanced GET, but Elliot wave trading does not follow a market but tries to impose a "wave" pattern. Tom Joseph admits that this "wave" pattern does not actually exist in a market 40 to 50% of the time. I tried using other Elliot wave trading programs but the same problem exists. No one can control the market. The market tells the trader what it is doing. I used Kwikpop indicators, including their "special proprietary indicators," but there are too many indicators and the charts are cluttered.

I tried all the standard indicators, which are packaged in trading software, but they are all confusing. I tried using CQG with the very expensive add-ons, including those of Tom Demark, but there are too many things to watch. AbleTrend is simple to use and gives a true picture of what is happening and likely to happen.

A trader does have to have knowledge of the market and chart patterns, but I find that AbleTrend is MORE RELIABLE than my personal reading of the charts most of the time.

I have used John Ehlers cycle finding methods, but they are similar to Elliot wave software in that they try to impose themselves upon the market rather than let market show what it is actually doing.

In your opinion, what are the main differences between other software programs and AbleTrend?
One of the main differences between other software programs and AbleTrend is that AbleTrend has the truest dynamic support and resistance indicators that I have ever seen (trend 2). These indicators work fine with default settings.

What are the most important factors in trading? How does AbleTrend help?
I have found that the most important things in trading are: (1) Finding the trend early, (2) SUPPORT and RESISTANCE in real time, and (3) Entering on retracements to control losses. It is also important to STAY IN THE TREND. AbleTrend shows me how to do these things with precise accuracy and elegant simplicity. The software you have developed has the most accurate support and resistance levels I have seen. They indicate the pivots in advance. This feature alone is worth the price.

One additional important thing is AbleTrend helps one to control one's emotions and (often wrong) "gut" feelings about the patterns. AbleTrend gives one confidence to enter and exit positions. AbleTrend also gives one confidence to STAY IN a position.

Were you able to find good trades during the current financial crisis? Could you give an example?
The current financial crisis offers the absolute BEST conditions for trading, lots of movement, which provides unprecedented opportunities. I have attached two examples of AbleTrend giving buy/sell/stop signals on the Trade Station platform.

Do you have the confidence to use AbleTrend in trading for years to come?
I have the confidence to use AbleTrend to make a good living day trading and position trading. Thanks to all of you who toil for us in the trading community. I am a senior radiologist in a busy, high quality practice in Atlanta. I love the markets and I love trading. AbleTrend has given me the confidence to trade for a living when I soon retire from active medical practice.

Interviewed by Grace Wang, Head of Customer Relations, AbleSys

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— Dr. Harvey J Saff

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TRADING NOW

We can think of the 2007–08 financial crisis as another lesson in history. If you look back at the history of the financial markets, you will see that similar crises have occurred from time to time. During a healthy market rally it is easy to forget that because of credit expansion, markets will take a nosedive. This is all the more reason to keep a close watch on the technical indicators that show when a trend is reversing. Conversely, during a bear market, we are anxiously watching for technical signs of the start of a bull market. So at this point, have the markets hit their support level and are they ready to bounce off it? Or is what we are experiencing merely a correction?

There are several techniques you can apply to your charts to determine if the markets are indeed turning around. In this issue of **Traders.com**, we offer several articles that discuss how you can identify the bottom of a market. Take a look at "The NYSE Composite Has Bullish Divergences In Two Time Frames" by Donald W. Pendergast, "Getting Ready For A Bottom" by James Kupfer, "Financials Start Last Leg Down" by Alan R. Northam, "October 2008 Or October 2009?" by Koos van der Merwe, and "Looking For The NASDAQ Bottom" by Alan R. Northam. These are just a few that will tell you what to look for to determine when a market has hit bottom and is ready to start a new leg up. Then, of course, you will need to look at other sectors such as the financials, the homebuilders, the commodities, and bonds to determine whether we are indeed at the end of the cyclical bear market. And we have included articles on these topics such as "Moment Of Truth For XLF" by Arthur Hill, "Homebuilders SPDR Turns Down" by Alan R. Northam, and "Is Gold Still Golden?" by James Kupfer.

And that is only a fraction of the useful articles you'll find here and at our online publications, *Traders.com Advantage* and *Working Money*, or even STOCKS & COMMODITIES magazine. Take a look at our website and see what we have to offer. Check us out — that will enable you to:

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And you can find more Traders.com/Advantage articles at **www.Traders.com** to help you stay in tune with the markets. Perusing these articles will help you remember that markets have fallen before over the decades and even the centuries, and they will again, and by keeping that in mind, you can make your way through the darkness of these volatile times.

Jayathi Gopalakrishnan

Jayanthi Gopalakrishnan,
Editor

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INDEXES

MACD

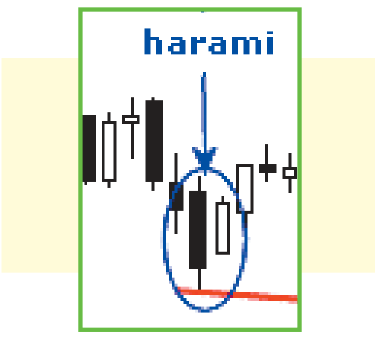
A Major Support Test For The Nikkei

by Arthur Hill

The Nikkei is trying to firm near its March lows, but momentum has yet to turn up and traders should watch for a signal line crossover in the MACD.

Tradable: $NIKK

Figure 1 shows weekly candlesticks over the last two years. The Nikkei 225 ($NIKK) remains in a clear downtrend with a series of lower lows and lower highs. A harami formed with the March low and the index moved below this low with a spike below 12,000 in September. Despite the dip below 12,000, the index recovered and is attempting to firm near the March low. Firmness is one thing. A bounce is another.



While the index breached its March low, the moving average convergence/divergence (MACD) (5,35,5) held above its March low for a potential positive divergence. Instead of the usual (12,26,9), I shortened the short moving average from 12 to 5 and lengthened the long moving average from 26 to 35. The signal line moving average is set at 5 (versus 9). This makes the indicator more sensitive to price movements. Despite a higher low and positive divergence working, the momentum oscillator has yet to actually turn up and move above its signal line. At the very least, a move above the signal line is needed to show improving momentum and confirm recent firmness.

Figure 2 focuses on daily prices with the positive directional Indicator and minus directional Indicator. The overall trend is down and -DI (red) remains well above +DI (green). Except for a head-fake in late August, -DI has been above +DI, and this corresponds with the three-month downtrend. The gap between +DI and a -DI is quite wide, and further strength is needed to close the gap and forge a bullish crossover. This would likely coincide with a trendline break and argue for a challenge to the May–June highs in the Nikkei. ■

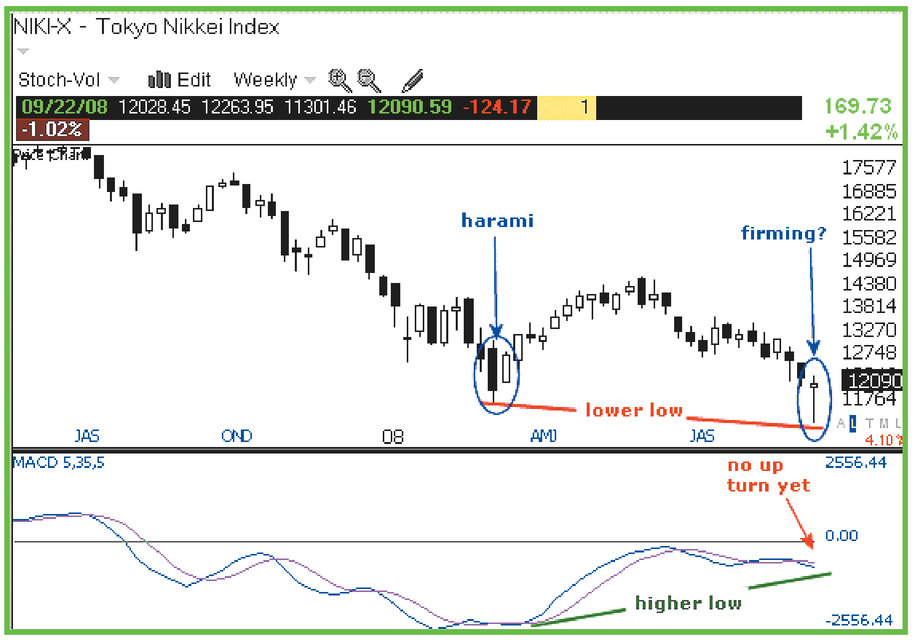


FIGURE 1: $NIKK, WEEKLY. Here are the weekly candlesticks over the last two years. The index remains in a clear downtrend with a series of lower lows and lower highs.

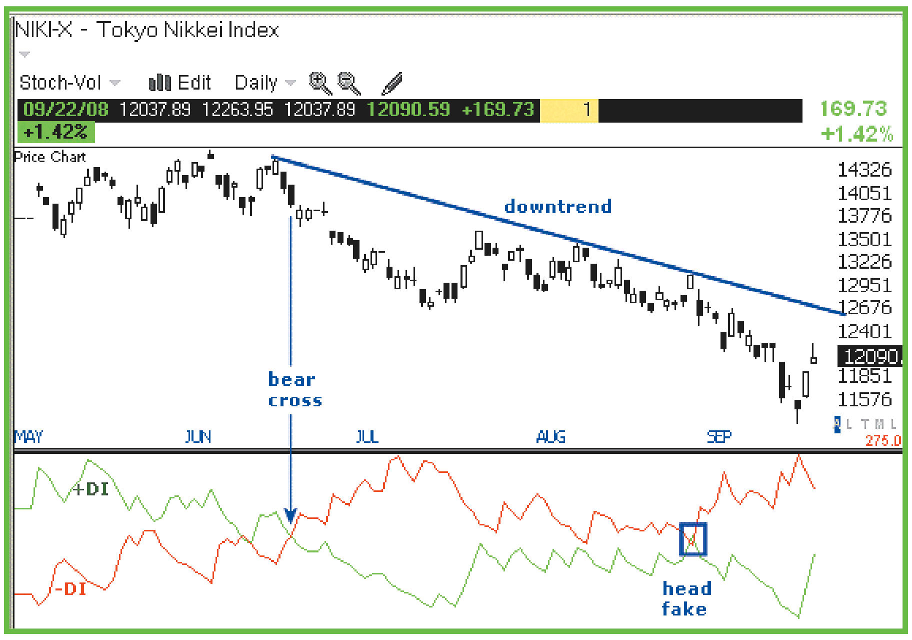


FIGURE 2: $NIKK, DAILY. Note that the overall trend is down and the -DI (red) remains well above the +DI (green).

ELLIOTT WAVE

QQQQ Breaks Key Support

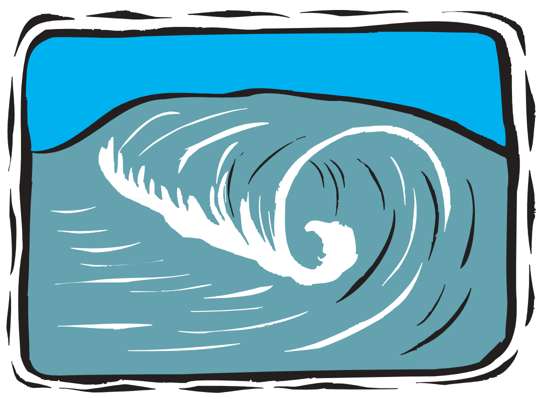
by Alan R. Northam

The QQQQ has now broken below key support drawn off the mid-March price low, confirming that crash wave (3) of 3 is now under way. The target price for the completion of the crash wave is calculated to be $28.03. However, once the crash wave is complete, this market will still make a lower low before a major bottom is in place.

Tradable: QQQQ

I have written several articles on the QQQQ, and I encourage those reading this article to refer back to those for background information. My last article was entitled "QQQQ Crash Coming?" and describes the market as entering into the crash wave. In that article I said, "Expect QQQQ to sell off rapidly from here on out."

As of today, the crash wave has not been confirmed by the breaking of key support drawn off the March low. Figure 1 shows that from the market top late last year, the market has traded in the downward direction to complete wave 1 down in mid-March of this year. From that time, QQQQ moved higher into early June to complete corrective wave 2. Upon completion of wave 2, wave 3 down got under way and is now subdividing into five waves. Wave 3s are noted as the wave that traverses the greatest distance in the shortest amount of time. Wave 3 down then started to subdivide and completed subwave (1) in mid-July. The market then entered into another short-term correction to complete subwave (2) of wave 3 down. This then set up subwave (3) down. I call this the crash wave because wave 3s move the



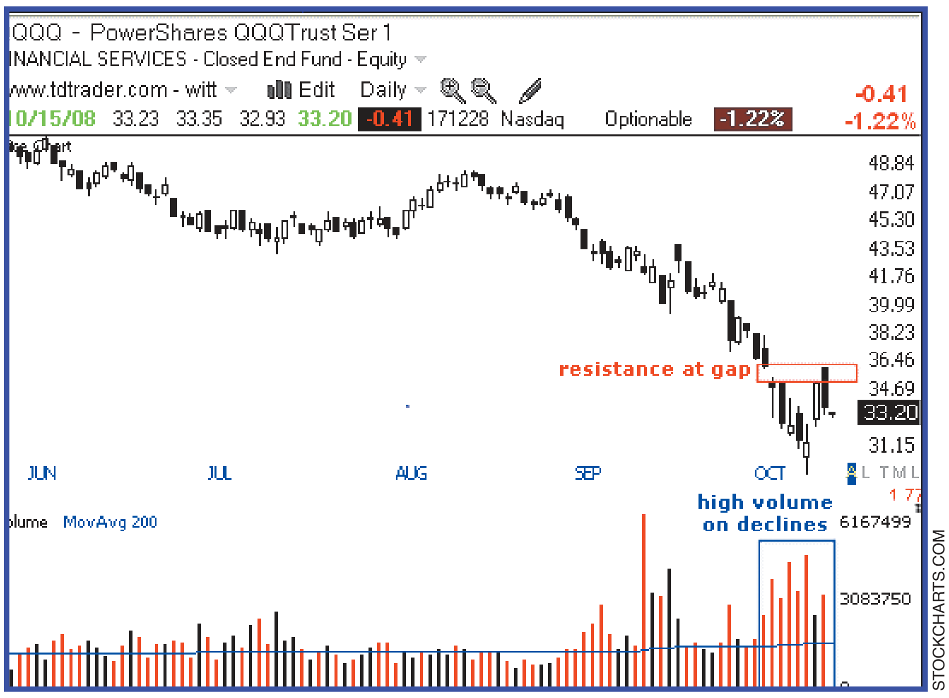


FIGURE 1: QQQQ, DAILY. This chart shows the Elliott wave count and that this market is currently in wave (3) of 3. This chart also shows that QQQQ has broken below key support drawn off the mid-March price low.

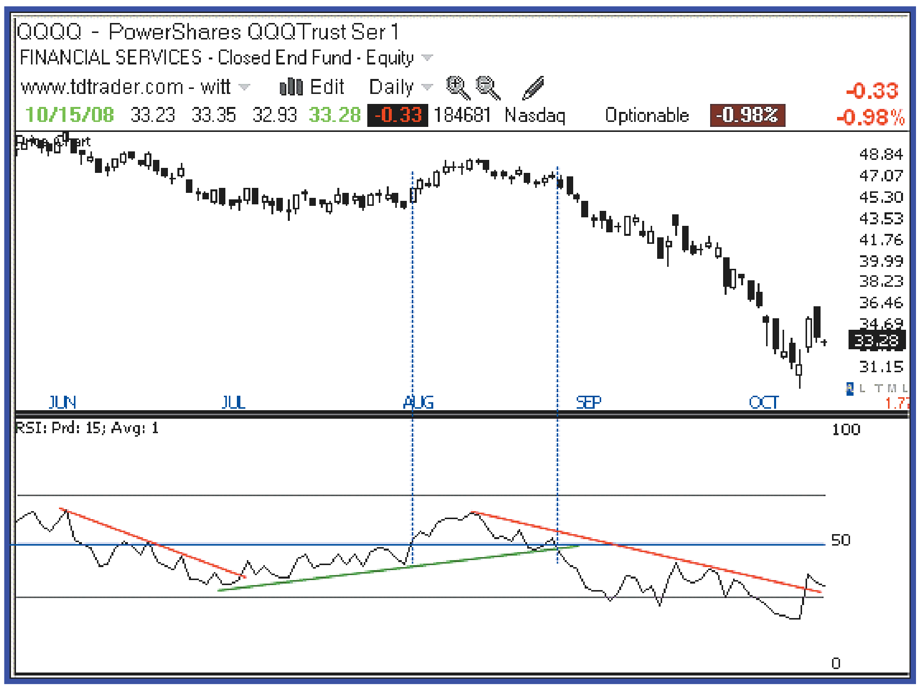


FIGURE 2: QQQQ, 10-MINUTE. This chart shows that this market has formed five waves in the downward direction, indicating that the downward trend is under way and that this market is not still in a corrective rally.

furthest in the shortest period of time and with the market now being in subwave (3) of wave 3 down, the downward momentum accelerates much more quickly. In mid-September, the QQQQ broke below key support off the mid-March low. The breaking of this line of support confirms that the crash wave is in progress and this market is headed for much lower ground.

After having broken below key support, the QQQQ made another short-term bottom and has been moving upward over the last several days. Subwave (3) is now subdividing into yet five smaller subwaves, wave i down, ii a corrective wave, iii down, iv another corrective wave, and a final wave v down. Of these five smaller subwaves, wave i down is now complete and corrective subwave ii also looks complete. This now sets the market up for another third wave down, subwave iii that already looks to be under way. This sets up the market for subwave iii, of subwave (3) of wave 3 so the crash wave should now really start to accelerate to the downside in the very near future.

In Figure 2, I have shown the details of subwave ii and sub-wave iii. In this figure, take note that subwave iii down has subdivided into five smaller waves to the downside. When the waves unfold in five waves in the direction of the major trend, which in our case is down, it then confirms that the major trend has resumed. Note also that the market is now in a short-term corrective mode and looks to have completed corrective waves a and b of a flat correction. I have drawn in wave c, which is needed to complete this short-term correction before the crash wave can resume.

In my previous articles on the QQQQ, I have shown how I have calculated the target price for the completion of the crash wave. This target price still stands and is calculated to be $28.03. However, the market normally likes round numbers, so I would expect to perhaps see the crash wave as ending somewhere around $30. Once the crash wave is complete, then this market will enter into a wave 4 correction followed by a final wave 5 down to new lows.

In conclusion, the breaking of the key support level off the mid-March price low has confirmed the crash wave. This also confirms that the major trend is still down and the market is not in the process of making a market bottom at this juncture. Once crash wave 3 is complete, the QQQQ will undergo a wave 4 market correction, followed by a final wave 5 down before we can even think of a major market bottom as being put in place. Figure 2 also shows the market is currently in a short-term market correction that should see the QQQQ rise to about $41.50 before the crash wave resumes. ■

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FLAGS AND PENNANTS

NYSE Composite Index Breaks Down Further

by Chaitali Mohile

The NYSE Composite Index has broken the bearish flag & pennant pattern.

Tradable: $NYA

The NYSE Composite Index has been forming lower highs since October 2007, gradually entering an intermediate downtrend. From the third lower high at 9600, $NYA took a nosedive. The index lost more than 1,200 points during this decline and entered sideways action.

The consolidation range narrowed further, forming the bearish flag & pennant pattern. This pattern is a continuation of an existing downside move as the pattern breaks in a downward direction. $NYA consolidated for approximately eight weeks. The volume during consolidation has also been reduced. In Figure 1, the index has already broken down from the bearish continuation pattern.

After this breakout, the possibility of the pullback looks difficult as the strong support of previous low of 2007 is also breached.

The target can be calculated by measuring the length of the declining rally and subtracting it from the breakout level. Therefore, the length is 9600 – 8200 = 1400; subtracting 1400 from the breakout level at 8200, we get the target of 6800.

The moving average convergence/divergence (MACD) (12,26,9) is in negative territory, and the average directional movement index (ADX) (14) is also bearish. The downtrend is well developed with high selling pressure, so the trend would continue to move further. The relative strength index (RSI) (14) lacks strength to initiate any bullish action. Hence, all the indicators are highly bearish.

According to Figure 1, the low made in the second week of September 2008 was 7400. So the next potential support for the descending rally would be 7400, and after violating this support the target can be achieved.

Considering the bearish indicators, the target looks achievable. In addition, the current problems in the US economy would add weakness and drag the index lower. Any pullback rally from the lower levels would be choppy due to support turned to resistance.

Thus, the NYSE Composite Index would continue the downward rally and the intermediate downtrend would sustain its momentum.

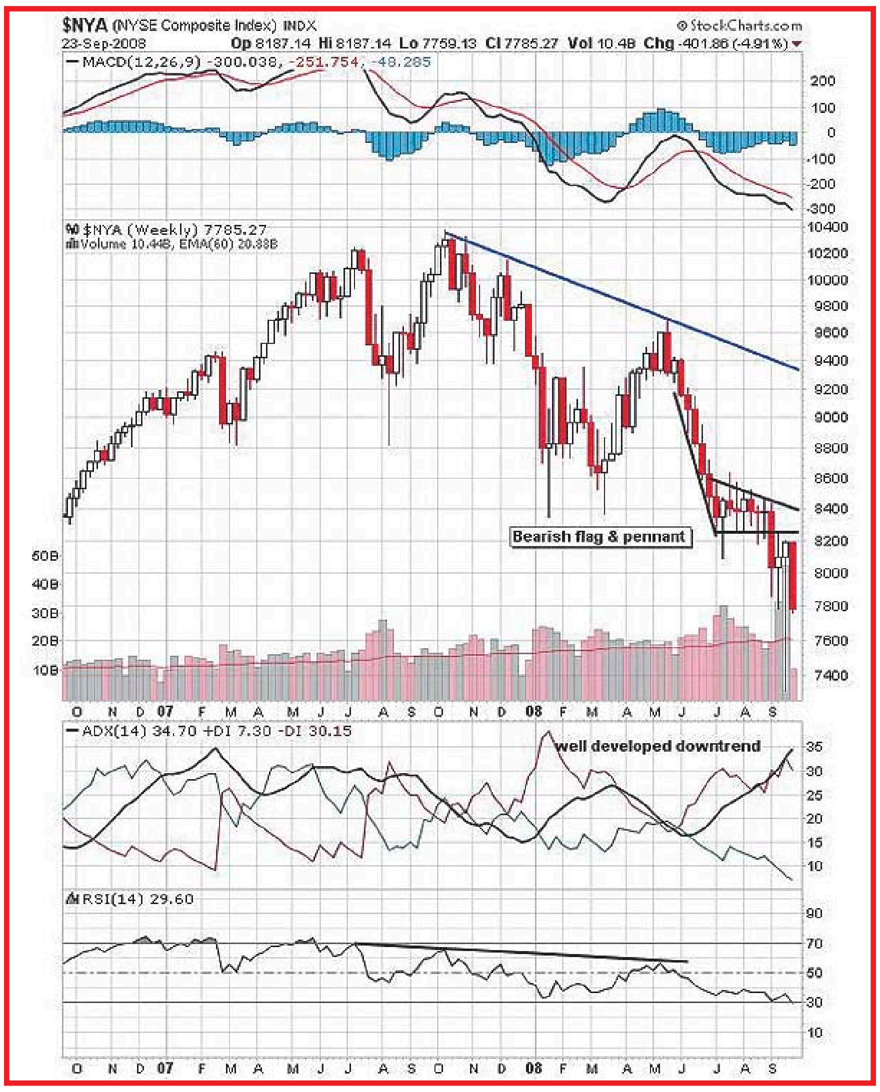

FIGURE 1: $NYA, WEEKLY. This chart shows the breakdown of a bearish flag & pennant pattern.

FIBONACCI

Further To Fall On The S&P 500

by James Kupfer

As I write this, the S&P 500 is down more than 3% to 1172. With the broad market continuing to fall, when might we see some relief?

Tradable: S&P 500

As seen on the weekly S&P chart in Figure 1, it is clear that we are in an established downtrend. I've drawn two trendlines on this chart, both in purple. Both are drawn using either the highs or lows, as I tend to do that instead of using closing prices. If you overlay the trendlines they both have almost an identical slope, which is relatively common. In this instance, they create a nicely defined channel in which future price action can be expected to occur within.

Also shown on the chart are two additional features. The first are the Fibonacci retracement levels drawn from the September 2002 lows to the recent market top. We have clearly already broken through the initial support at 38.2%. The market did drop through the 50% retracement, but then bounced above it. Next comes the 61.8% retracement level that is still significantly below the market's current price levels. The other chart feature is the dark green line drawn at the August 2004 low.

Given that it is improbable that the market will hold the 50% retracement level support zone, we need to identify the next likely zone for a bounce. In my estimation, the next logical zone is where the 61.8% Fibonacci level and the August 2004 bounce coincide at roughly 1070. Assuming this occurs over the next few weeks, I think we are likely to also see the bottom (purple) channel line having extended itself down to this same price zone as well. That convergence of three levels of support would provide a natural place for prices to reverse, if only for a few weeks or months.

FIGURE 1: S&P 500, WEEKLY. The two trendlines on this chart are both drawn using either highs or lows. If they are overlaid, you would see that they both have almost an identical slope.

The Selloff Tsunami

by Ron Walker

The Dow Jones Industrial Average put in its worst week in history. Is the tsunami of selling over?

Tradable: $INDU

Just one year and one day after its all-time closing high of 15,164.53, made on October 9, 2007, the Dow Jones Industrial Average (DJIA) dropped an eye-popping 5,713.34 points and has lost 40.34%. The Standard & Poor's 500 (S&P 500) has had an unholy fall of 666 points or approximately 42.55 % from its all-time closing high of 1,565.15, which was also made on October 9, 2007. These figures and percentage calculations are from closing high to closing low. Their fall from grace can be seen over the past year in Figure 1. After the DJIA put in the worst week in its 112-year history, the S&P 500's 666-point drop seems like a fitting number to be associated with this diabolical disaster.

The market is purging itself of the poison that the government has inflicted on it by subsidizing the housing market via Fannie Mae and Freddie Mac. Now they sit on the balance sheets of banks, which led up to a locking-up of the credit markets in the last few weeks. With the passage of the $700 billion bailout package, there is still great uncertainty as to how it will be implemented, adding further anxiety to investors. Thus, this shock & awe-type campaign against the stock market has literally bombarded and assaulted global markets everywhere. The market meltdown could be stabilized once the Bush administration lays out a plan of action. Such actions could include the injecting of capital into the banking system and/or buying straight and preferred shares in the financial sector, which would put money on the banks' balance sheets, giving Uncle Sam a stake in the banks.

Mr. Toad's Wild Ride isn't just a ride at Disneyland! It is exactly what happened last Friday, on October 10, 2008. There were more back-and-forth swings that day on the DJIA than any other time in its 112-year history. In Figure 2, these swings started the day with the DJIA opening in a freefall, dropping 697 points just five minutes after the opening bell. Then by 10:12 a.m, prices erased all losses and inched up into positive territory momentarily. Then for the next few hours, prices staggered, falling first 512 points and then rallying back up 275 points in less than an hour. Prices lowered after that rally attempt faltered and the DJIA racked up steep losses again, spiraling down 606 points by 1:50 p.m. By 3:36 p.m., prices made a breathtaking climb higher and managed to rally up 928 points as traders picked up stocks before the weekend, putting the DJIA in the positive column by 322 points.

But as the last 10 minutes of trading occurred, the DJIA pulled back into negative territory, closing the day down 128 points or 1.49%. It's not surprising that the DJIA ended the session posting the largest price swing in history of 1,019 points (Figure 2), given this amusement park atmosphere.

It was a week of record events for the DJIA as it also posted its worst week in history. This was the worst week in the 112-year history for the DJIA and the stock market as a whole, with the S&P 500 losing a record 200 points or 18.20%. And the DJIA lost a staggering 1,874 points or 18.15% for the week. Over the last two weeks, the DJIA has shed 2,688 points. And in the last eight days of its consecutive losing streak, the DJIA has gotten just over a 2,400-point haircut. Whether a bottom has been put in is a matter of opinion, but given that the stock market is made up largely of fear and greed, we may have put in a tradable bottom. The stock market has worked like game shows, Greed and Fear Factor. As the bottom fell out of the stock market last week as fear ran rampant, it may begin to rise on balance as greed set in as investors gobbled up stocks that were just massacred in this tsunami selloff.

Extreme caution should be used if any bottom appears with reference to long-term position trading, because greed may take prices up for the short term in a rubber band rally, but it may be built on quicksand. This is clearly a day/swing trading environment. ■

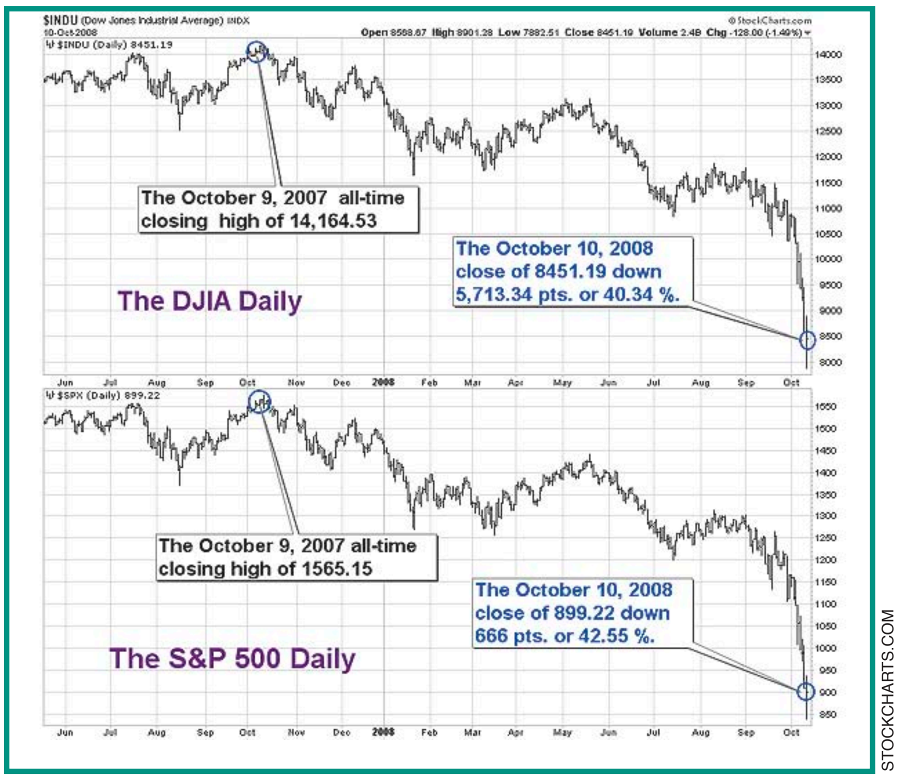

FIGURE 1: DJIA, DAILY. The DJIA and the S&P 500 are both down over 40% since their closing all-time highs made on October 9, 2007.

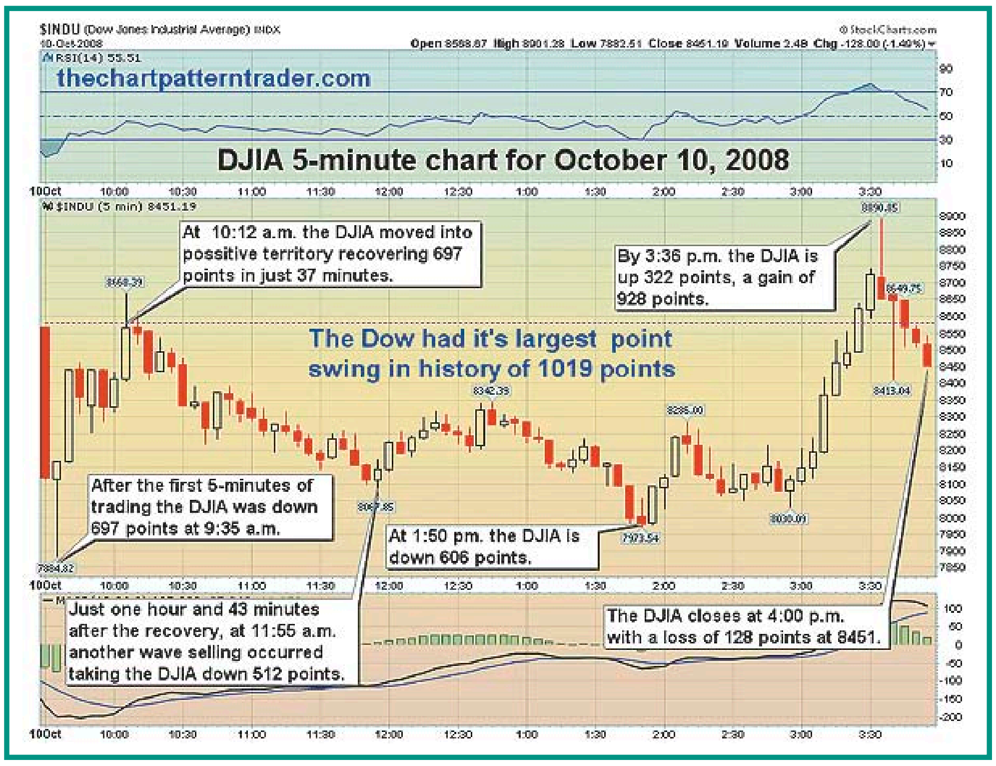

FIGURE 2: DJIA, FIVE-MINUTE. On October 10, 2008, the DJIA had the largest point swing in its 112-year history. The wild swings ended the session with a range of 1,019 points. The rallies made after 9:35 a.m. and during the last hour were most impressive. These sudden changes of mood and behavior in prices reveal that the bulls and the bears were fighting it out for control of the market.

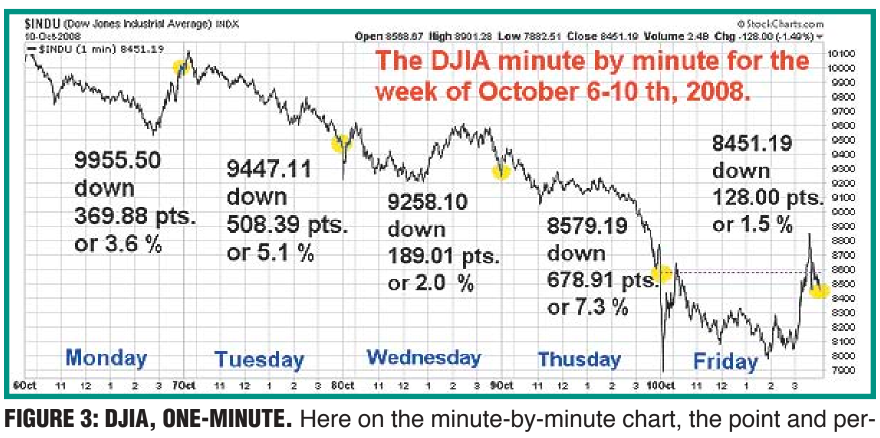

FIGURE 3: DJIA, ONE-MINUTE. Here on the minute-by-minute chart, the point and percentage losses of each trading session are marked during its worst week in history, October 6 to 10, 2008.

The NYSE Composite Has Bullish Divergences In Two Time Frames

by Donald W. Pendergast Jr.

Like every other broad market index, the NYSE Composite has taken a severe beating. However, signs of life on both the daily and weekly time frames suggest that a significant low has been made.

Tradable: .NYA

Think of the NYSE Composite index (.NYA) as a gigantic version of the more commonly tracked Standard & Poor's 500. It covers many more stocks, and even though it closely correlates to movements in the S&P 500, for my money, the .NYA provides a better overall view of the broad US market. The view lately, of course, has been anything but picturesque as the fabled index hurtled southward. Having bottomed out for the moment, however, thoughtful analysis suggests that the .NYA has entered into a period of consolidation that may eventually wash a good deal of the fear factor out of the markets. The charts, as always, tell the tale best.

The weekly chart of the .NYA (Figure 1) provides graphic evidence of the severity of the selloffs since last autumn. At the top of the chart is the composite internal strength indicator, which is a weighted mix of the advance-decline line, new highs-new lows, up volume-down volume, rate of change, and a few other oddities, the sum of which provides an excellent view of the market's overall health. Having bottomed at an all-time low a couple of weeks ago, it's now attempting to turn higher. Other evidence suggesting a low may be in place: there is positive price-momentum divergence on the weekly stochastic and the ultimate oscillator. Finally, the 78.6% Fibonacci retracement and the major long-term support line (red horizontal line) have combined to keep a solid floor under the .NYA, effectively putting an end to the freefall that began in July 2008.

The daily chart of the .NYA (Figure 2) also demonstrates signs of meaningful positive price-momentum divergences in both the moving average convergence/divergence (MACD) and the ultimate oscillator. If a higher low prints, followed by a break above the most recent (to be determined) high, the uptrend will be confirmed. Should that happen, expect the blue zone between 6600–6800 to offer major overhead resistance, particularly because of the confluence of key Fibonacci resistance levels, the October 14th high and the location of the mighty 50-period exponential moving average (EMA).

The "hard right edge" of the charts give us a few extra clues every day, but the bulk of of a technical analyst's evidence for likely trend projections can only be found in the complex relationship between price, proportion, pattern, and time, using monthly, weekly, and daily charts to confirm what trader Jesse Livermore referred to as the line of least resistance. From my perspective, the line of least resistance on the .NYA, for the time being, is higher.

But not radically higher, because this bear market isn't over by a long shot. ■

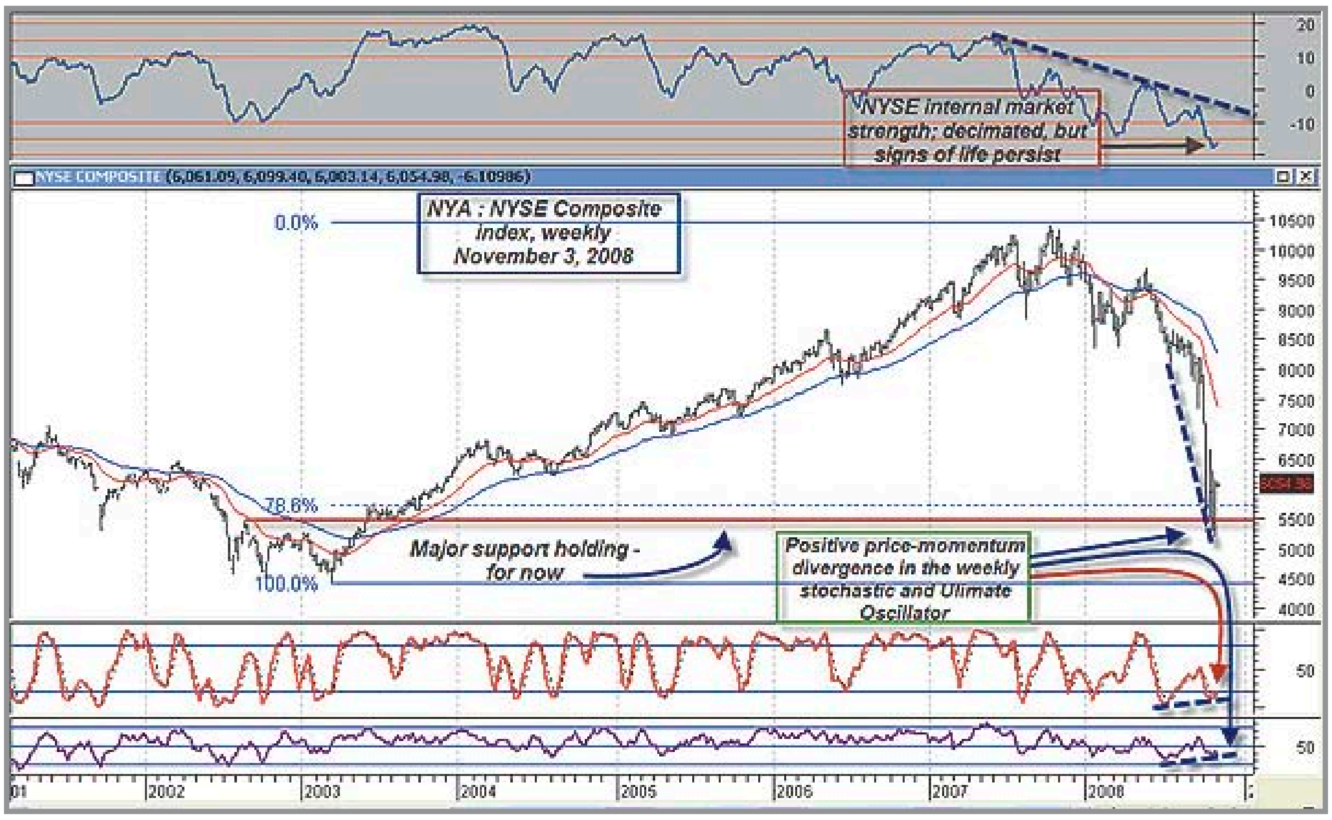

FIGURE 1: NYA, WEEKLY. Major support on the .NYA, holding for now.

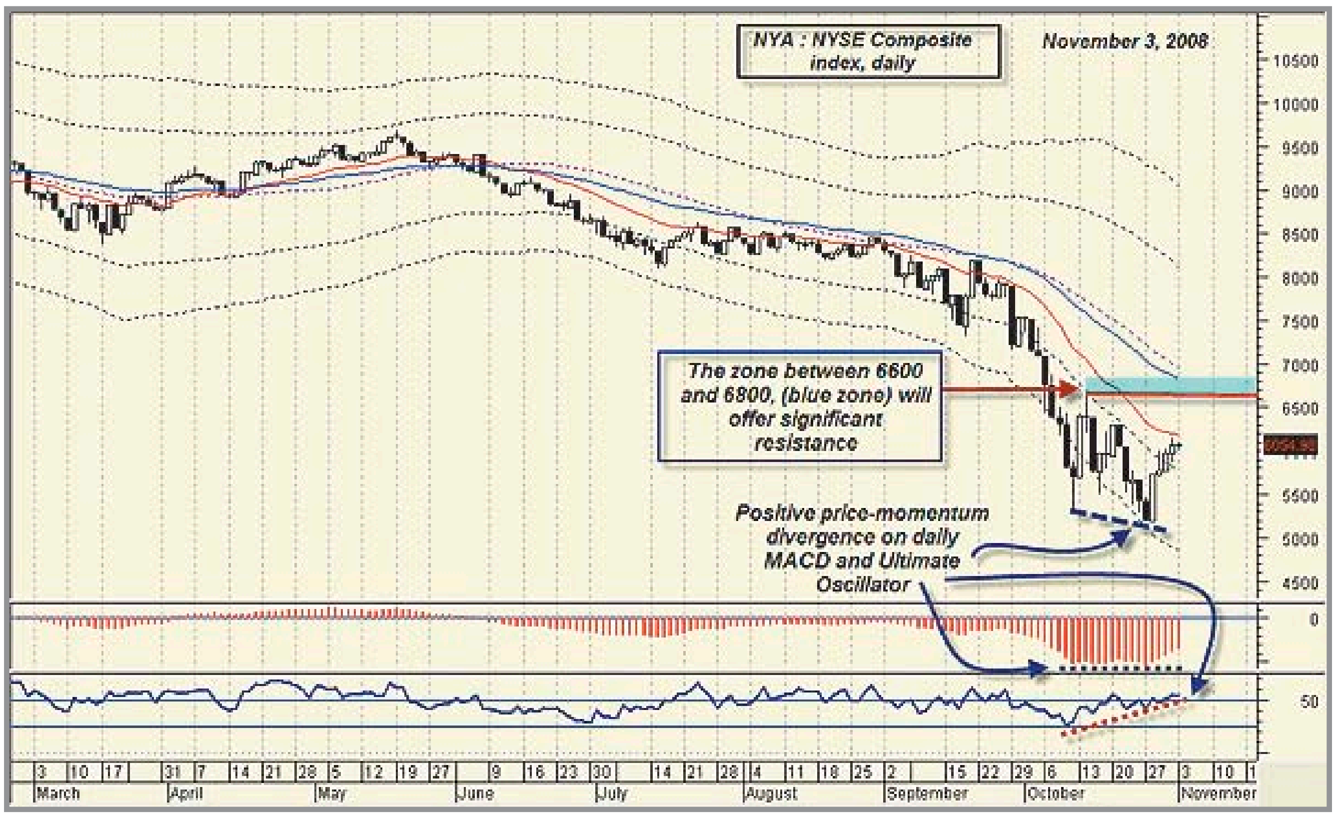

FIGURE 2: NYA, DAILY. Bullish price-momentum divergence on the daily NYSE Composite.

Think of the NYSE Composite index (.NYA) as a gigantic version of the more commonly tracked Standard & Poor's 500. For my money, the .NYA provides a better overall view of the broad US market.

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This article was first published on 11/4/2008.
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CYCLES

Getting Ready For A Bottom

by James Kupfer

Does history say anything about the potential for a bottom, given that the Dow Jones 30 is down more than 20% this month?

Tradable: DJIA

Figure 1 is a chart of each time since 1915 that the Dow Jones 30 has closed more than 20% down for the month. Based on this data, it is unlikely that October 2008 will close lower than we are currently. Even if it does, history suggests that it will likely be a good time to buy for at least the intermediate term.

There have been 1,125 months since January 1915, and only seven of those months closed down more than 20%. That is a mere 0.6% of all the months. Could it happen again now? Sure, but it is not exceptionally likely. This is perhaps the strong piece of data suggesting the market is at or nearing a near-term bottom.

During the seven periods listed in the chart, three of the subsequent months had gains following the loss. While those odds are clearly not great and we are clearly working with a very limited dataset, there are a few additional items of interest.

December 1929 through February 1930 were all up months. July and August 1932 had gains of 26% and 35.8%, respectively, and these gains took the DJIA above the peak from April 1932. It took only three months to surpass the peak from March 1938 after the market bottom that same month. The five months after May 1940 were all up.

All in all, 1987 was the only period I found in which the subsequent month was not up or at least the next few months following the 20% drop were not consequentially up. This is still a trader's market and under no circumstances would I suggest blindly buying and holding for a bounce that may or may not occur, but with any hope, these limited analyses will remind the reader that logic should rule their decisions, not fear. ■

Month	Close	Next Month
10/1929	-20.4%	-12.7%
9/1931	-30.7%	+7.6%
4/1932	-23.7%	-20.0%
5/1932	-20.0%	-4.25%
3/1938	-23.7%	+12.9%
5/1940	-21.7%	+5.1%
10/1987	-23.2%	-8.0%

FIGURE 1: DJIA, SINCE 1915. This chart shows each time since 1915 that the Dow Jones 30 has closed more than 20% down for the month.

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This article was first published on 10/20/2008.
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FIBONACCI

How Far Up?

by James Kupfer

Fibonacci retracement levels can help target how much of a bounce we may get in the Dow Jones 30.

Tradable: DJIA

Assuming the low of October 10, 2008, at 7882 marked a short-term bottom in the Dow Jones 30, where might we be headed from here? Of course, that can be a difficult question to answer, but Fibonacci retracement levels can indicate where likely reversal points lie. In particular, I find it useful to look for "clusters" of Fibonacci levels to help identify these key support or resistance points.

In identifying the key Fibonacci levels, I look for major turning points on weekly charts. In Figure 1 are two spreadsheets in which I have calculated a number of major turning points and their respective cluster of Fibonacci retracement levels.

As you can see, the two primary clusters above where the DJ30 is currently trading are approximately around 9400 and 9880. Given the close on October 28, 2008, at 9065, there is still some upside potential left in the market. It is likely that the DJ30 will surpass the initial resistance level at 9400, given that the market reached as high as 9794 on October 14, just four days after what at this point appears to be a short-term bottom. Therefore, the 9870–9880 level is the next real target.

As a bounce (hopefully) materializes, it will be important to watch the price action to see how things progress. Assuming the market makes it near the 9880 level, there are a few other non-Fibonacci indicators of resistance that may come into play that can be identified later. The bottom line, however, is that any bounce that may occur is doing so in a bear market and should generally be considered an opportunity to reestablish short positions. Only a move above 10,500 would be cause to doubt the ongoing existence of the bear. ■

	August 2008 - October 2009	October 2007 - October 2008
Major High	$ 11,867.00	$ 14,198.00
Major Low	$ 7,882.51	$ 7,882.00
Difference	$ 3,984.49	$ 6,316.00
Fibonacci Ratio	61.8%	76.4%
Fibonacci sub-value	$ 2,462.41	$ 4,825.42
Fibonacci Target Level	**$ 9,404.59**	**$ 9,372.58**

	May 2008 - October 2008	August 2008 - October 2008	October 2002 - October 2007
Major High	$ 13,136.00	$ 11,867.00	$ 14,198.10
Major Low	$ 7,882.00	$ 7,882.51	$ 7,197.00
Difference	$ 5,254.00	$ 3,984.49	$ 7,001.10
Fibonacci Ratio	61.8%	50.0%	61.8%
Fibonacci sub-value	$ 3,246.97	$ 1,992.25	$ 4,326.68
Fibonacci Target Level	**$ 9,889.03**	**$ 9,874.76**	**$ 9,871.42**

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FIGURE 1: FIBONACCI TURNING POINTS. There are a number of major turning points and their respective cluster of Fibonacci retracement levels.

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This article was first published on 10/30/2008.
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TRADE THE TRIANGLE

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Triangles in Action

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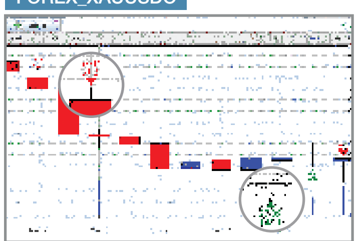
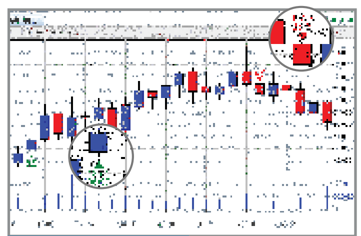


NYSE_ALK

2008 Q1-Q2 Triangle Returns

James River Coal Co.	JRCC	208.34%
Fuel System Solutions	FSYS	160.90%
Vision Sciences	VSCI	126.60%
Duvernay Oil Corp.	DDV	85.88%
General Motors	GM	52.89%
Heating Oil	HO	49.98%
Wheat	ZW	38.6%
Crude Oil	CL	35.29%
Sugar #11	SB	23.92%
Soybean Meal	ZM	23.73%

*Results using our suggested "Trade Triangle" technique.



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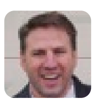
Member Success Stories



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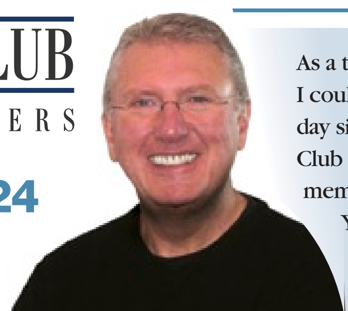

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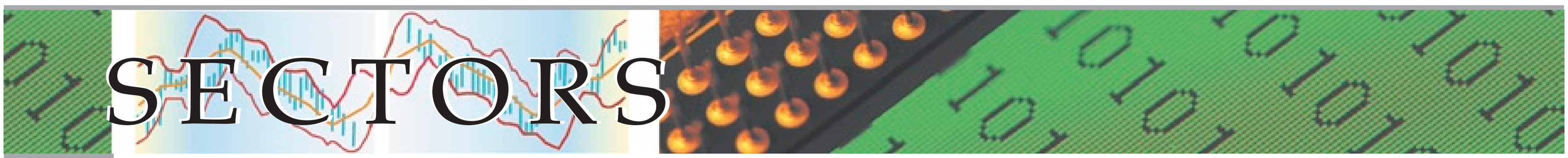

ADXR

Moment Of Truth For XLF

by Arthur Hill

After forming a rising wedge over the last two months, the financials SPDR declined sharply and is dangerously close to a continuation breakdown.

Tradable: XLF

Figure 1 focuses on the rising wedge. The financials SPDR (XLF) bottomed in July and retraced around 62% of its prior decline with a rising wedge advance over the last two months. XLF peaked this week and declined to the lower trendline over the last four days. A break looked imminent with a weak open on September 11, but XLF recovered by the close and the trendline is holding for now.

The bottom indicator shows the positive directional indicator (+DI) and the negative directional indicator (-DI). These are part of J. Welles Wilder's average directional movement index (ADX). As their names imply, +DI and -DI can be used to determine direction. A bullish bias exists when +DI is above -DI and a bearish bias when -DI is above +DI. Overall, these two have been trading flat the last few weeks and I am looking for an upside breakout for the next signal. A +DI breakout would be bullish, while a -DI breakout would be bearish.

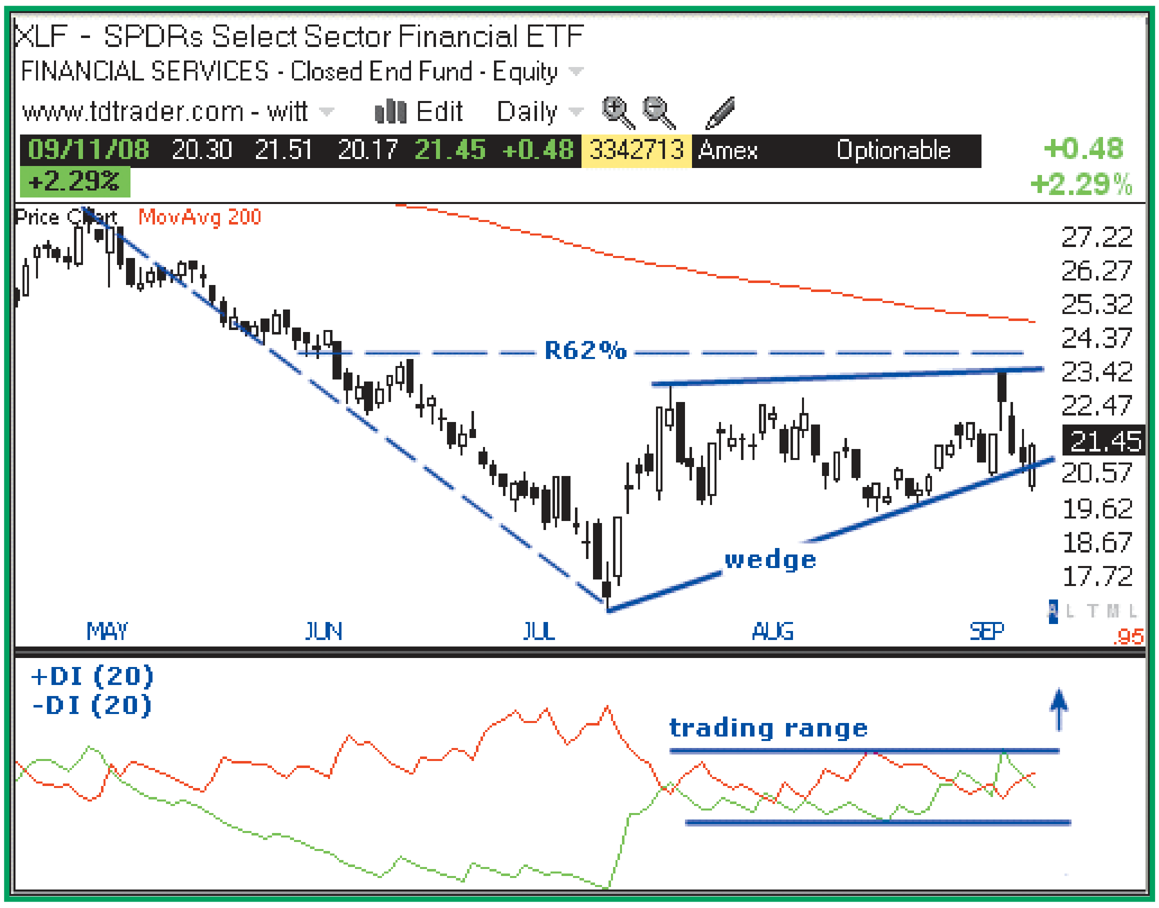

FIGURE 1: XLF, DAILY. This SPDR bottomed in July and retraced around 62% of its prior decline with a rising wedge advance over two months.

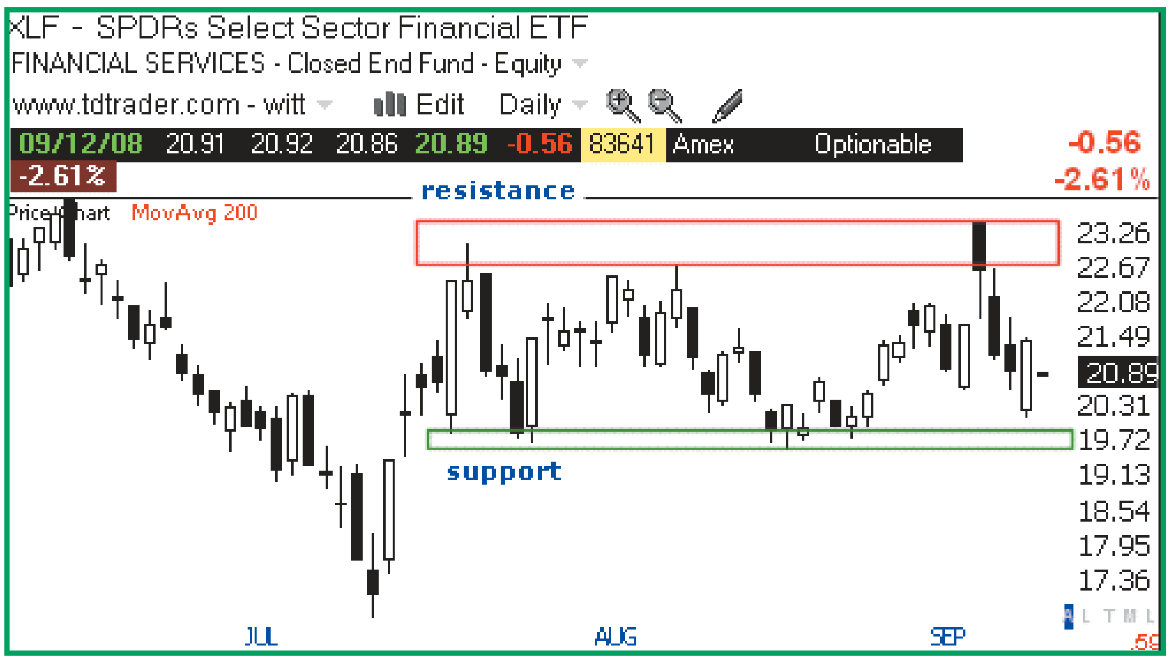

FIGURE 2: XLF, DAILY. A trading range formed after the July surge.

Figure 2 focuses on a trading range that formed after the July surge. XLF has a support zone around 19.5 and a resistance zone around 23. With the ETF trading at support, a big test is at hand. A break below support would also reverse the rising wedge and point to lower prices. This would also likely to be accompanied with a -DI breakout. Such a combination would be bearish for XLF, and this ETF is at its moment of truth. To hold or not to hold, that is the challenge. ■

A bullish bias exists when +DI is above -DI, and a bearish bias exists when -DI is above +DI.

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This article was first published on 9/12/2008. See www.Traders.com for more.

ELLIOTT WAVE

Homebuilders SPDR Turns Down

by Alan R. Northam

The market correction for XHB is over, and this homebuilder index has now resumed its selloff in the direction of its major trend.

Tradable: XHB

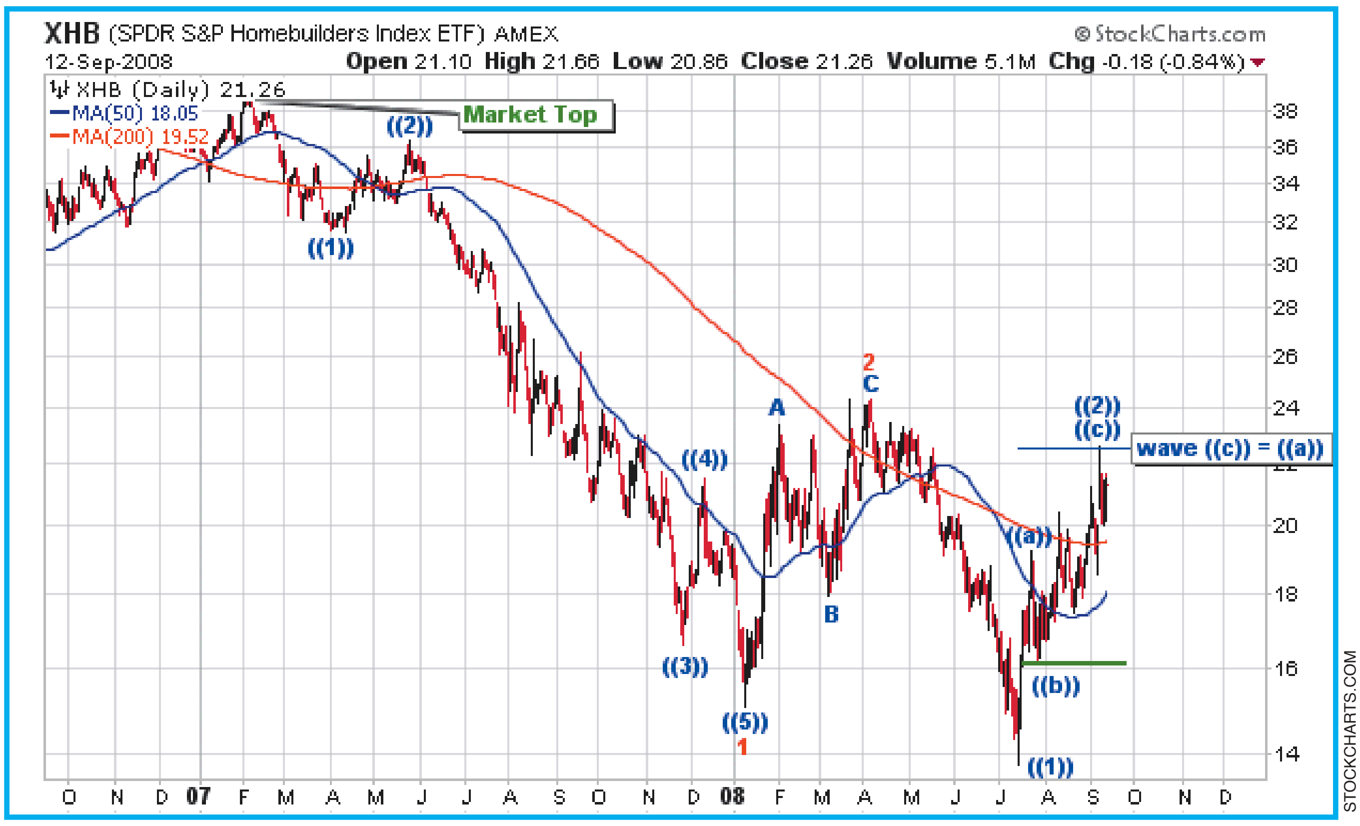


FIGURE 1: XHB, DAILY. This bar chart shows the major bull market top and the Elliott wave count. This chart shows that XHB has unfolded in five waves down from the market top. These five waves define the direction of the major trend as being in the downward direction.

FIGURE 2: XHB, 60-MINUTE. This chart shows the market correction for XHB that started in mid-July. This chart also shows the Elliott wave count showing the market correction as unfolding as an abc market correction.

The SPDR S&P Homebuilders Index ETF (XHB) formed a major bull market top in February 2007. Since then, XHB has been trading downward, completing a five-wave move in early January 2008.

These five downward waves determine the trend of one larger degree, which is also down. What this means is that these first five waves, from the market top in February 2007 to January 2008, form a larger wave 1 of the next larger five waves that will also unfold in the downward direction.

Wave 2 of this larger degree of trend was also complete in early April. With the completion of the larger waves 1 and 2, the larger wave 3, which is also unfolding in the downward direction, has been under way since early April.

Wave 3 is now unfolding in five smaller waves and are labeled ((1)), ((2)), ((3)), ((4)), and ((5)). The double parentheses indicate that ((1)) is called circle wave 1 and so forth.

The chart shows that circle wave ((1)) was complete in mid-July and that circle wave ((2)) now looks complete as well.

One way to determine if circle wave ((2)) is complete is to measure its length from the low of circle wave ((b)) and if it is equal to the length of circle wave ((a)), then that is a signal that it could be complete.

I have shown where circle wave ((c)) is equal to circle wave ((a)) as a short horizontal blue line of the chart labeled "wave ((c)) = ((a))." This method gives the typical length in price movement to complete circle wave 2 but is not a hard and fast rule. Circle wave 2 can end before price rises to this level or may even end at a higher price level, but typically, wave c is equal in price length to wave a. For a more accurate determination of the completion of circle wave 2, it is necessary to look at the smaller time frames.

Figure 2 is that of the 60-minute chart of XHB. This chart shows the wave structure of corrective circle wave ((2)). As can be seen from this chart, corrective circle wave 2 has unfolded in an ABC wave structure.

Zigzag wave structures are a very typical pattern for second waves and unfold in three waves. The first wave is wave a and unfolds against the major trend. Since wave a has unfolded in the upward direction, it tells us that the major trend is in the downward direction. Wave b then unfolds in the direction of the major trend and wave c unfolds against the major trend, just as wave a does.

Note that circle wave ((c)) has unfolded as an expanding diagonal wave pattern. Expanding diagonal wave patterns unfold in five waves, as shown on the chart. Note that all five waves look to be complete, and thus completing the expanding diagonal wave pattern. Expanding diagonal wave patterns are terminal wave patterns, and when they develop, they signal that the upward corrective move is over. So we have a complete ABC zigzag corrective pattern and an expanding diagonal wave pattern, both signaling the end of the market correction. As a confirmation signal I have shown a horizontal green support line drawn off the low of circle wave ((b)). If XHB moves below the low of circle wave ((b)), it will signal that the downward trend has resumed.

Another way of determining if the move up from the mid-July low is over is by looking for a five-wave

FIGURE 3: XHB, 10-MINUTE. This chart shows the Elliott wave count. The five waves in the downward direction, in the blue box, show that the market correction off the July low has ended and the downward selloff has resumed.

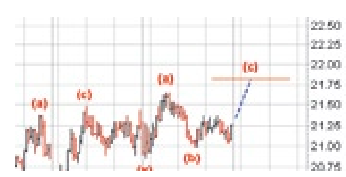
Markets move in five waves in the direction of the major trend and in three waves in market corrections.

move of a small degree of trend in the downward direction after the completion of circle wave ((c)). Markets move in five waves in the direction of the major trend and in three waves in market corrections. To look at the small degree of trend, it is necessary to zoom in once again on a smaller time frame.

In Figure 3, I have shown the 10-minute time frame. This chart shows the completion of circle wave ((2)) in early September and the five smaller nonoverlapping waves that follow. These waves are labeled wave (i), (ii), (iii), (iv), and (v). These five waves point in the direction of the major trend and are signaling that the corrective move off the mid-July low is now over and the downward direction of the major trend has resumed (I have highlighted this area in a blue box). Note also that upon completion of the fifth wave in the downward direction, XHB has entered into another market correction that is moving against the major trend.

This corrective structure is unfolding as a double abc zigzag corrective wave pattern with the final wave (c) yet to unfold. I have drawn a red horizontal line at the price point where wave (c) should be complete. Again, this line is drawn off the (b) wave low and is the same length as wave (a). Once wave (c) is complete, the market will once again turn down and start to unfold in another five waves in the direction of the major trend, which is down. To confirm that wave (c) is over, I have again drawn a green horizontal support line off the low of wave (b). A move below this support line will confirm that the upward market correction is over and the downward trend has resumed. Please note that market corrections can always extend into more complex wave structures, although these are not high-probability situations. Typically, when a double zigzag is complete the corrective move is over, but we must be aware of this possibility.

In conclusion, XHB made a major market top in February 2007 and has unfolded in five waves to the downside. Five waves unfold in the direction of the major trend and, as such, is signaling that the major trend for the SPDR S&P Homebuilders Index ETF is in the downward direction. XHB has made a short-term bottom in mid-July and has been in a short-term market correction. Upon examination of two smaller time frames, we have identified that this short-term market correction is now over and the downward trend has resumed. ■



The Bearish Force Sustains For XLB

by Chaitali Mohile

The Material SPDR has been under bearish clouds for more than six months. The moving average resistances and the head & shoulder top may suppress any pullback rally.

Tradable: XLB

The breakdown in early July 2007 converted the 200-day moving average (MA) support to strong resistance. The Material Select Sector (XLB) later consolidated under the newly formed resistance of 200-day MA. In addition, the bearish moving average crossover weakened XLB and therefore formed lower highs. In Figure 1, the arrows show the moving average resistances and the price following the declining 50-day MA. Recently, the 50-day MA resistance was challenged for the third time, but the bearish force discouraged the pullback rally.

The relative strength index (RSI) (14) since July has failed to sustain above the 50 level. The oscillator moved within the range of 30-50, indicating a lack of strength to pull the index higher. So 50 levels can be considered as a strong resistance for any relief rally. The RSI (14) is back to the same level from the oversold area and ready to decline. The moving average convergence/divergence (MACD) (12,26,9) is in negative territory with a bullish crossover. However, the bullish crossover can attract the buying force only if the indicator moves above the zero line. In addition, the average directional movement index (ADX) (14) shows that the positive directional index (+DI) is below 20, indicating poor buying pressure. Though the negative directional index (-DI) has declined from the higher level, the selling pressure is stronger than the buying pressure.

Thus, the resistance and the weakness in indicators on the daily chart is likely to add to the bearish force.

In Figure 2, we can see the head & shoulders top pattern being formed with a neckline support at 36. The breakdown below the neckline would boost the bears and plunge XLB to lower lows. After the breakdown, the 200-day MA would offer an immediate support. As a result, XLB may surge to retest the neckline resistance. The right shoulder is constructed so the trader has to wait for a pattern breakout before initiating any short positions. The ADX (14) shows a developing downtrend, and the MACD (12,26,9) has declined from positive to negative territory. In addition, the RSI (14) also shows the head & shoulders top (bearish reversal pattern).

The major downtrend can be witnessed below the 200-day MA support in Figure 2. XLB would reach the target on breakdown only if this support is violated. The minimum estimated level would be: 46 (head) - 36 (neckline = 10 - 36 = 26. Before opening any short trade, I would request traders to watch the 200-day MA support. Even though the support is established, the bears would continue to hover around XLB and would discard any significant pullback rally. But traders need to be more cautious in such technical conditions.

Hence, the scenario points to a constant bearish force in XLB. ■

FIGURE 1: XLB, DAILY. Here, the arrows show the moving average resistance, and the price following the declining 50-day moving average.

FIGURE 2: XLB, WEEKLY. See the head & shoulders top pattern being formed with a neckline support at 36.

ELLIOTT WAVE

Financials Start Last Leg Down

by Alan R. Northam

The Financials Select Sector SPDR (XLF) made a market top in May 2007 and has been trading in an ABC zigzag market correction pattern since. It now appears that XLF has started the last leg down of the market correction that is correcting the previous complete bull market.

Tradable: XLF

According to the Elliott wave principles, after a market makes a market top it will correct in three waves. These three waves are labeled waves A, B, and C. Wave A retraces or corrects the first part of the total progress made by the previous trend. Wave B then moves in the direction of the previous trend and corrects part of wave A. Wave C moves in the opposite direction as the previous trend and completes the corrective process. Elliott calls this an ABC zigzag wave pattern. Further, wave A normally unfolds in five subwaves, wave B normally forms a smaller ABC zigzag, and the final wave C also unfolds in five subwaves.

Figure 1 shows the weekly bar chart of XLF. This chart shows that XLF made a major market top in late May 2007 after completing a bull market runup from mid-2002. This chart also shows that XLF has since sold off in five waves, completing wave (A) of an ABC zigzag corrective pattern that is correcting the complete previous bull market runup. Figure 1 also shows wave (B) to be complete as well. In Figure 2, the details of the (B) substructure is shown.

Figure 2 is that of the daily bar chart for XLF. This chart shows the detail of wave (B) of the ABC zigzag correction. In this figure, note that wave (B) is made up of an ABC zigzag, which is a normal wave pattern for wave B. In addition, wave C of wave (B) has further subdivided into an abc extended flat labeled a circle, b circle, and c circle. From a more traditional technical analysis point of view, the ABC corrective wave structure may look more like a wide flag flying at half-mast or a corrective trading channel.

If wave (B) is now complete as the wave structure suggests, then XLF is now starting the final wave (C) down. Wave (C) down should unfold in five waves similar to wave (A). Once wave (C) is complete, then the complete bear market ABC zigzag correction will be complete. To build a case that wave (C) down has already started, here's the 10-minute chart in Figure 3.

Figure 3 shows the 10-minute bar chart of XLF from the start of wave (C) down. This chart shows that this market has now formed five waves to the downside and are labeled waves (i), (ii), (iii), (iv), and (v). These five waves are in the same direction as the five subwaves of wave (A) and therefore signal that the downward trend has resumed. During market corrections, waves A and B also contain five subwaves. However, during market corrections, these five subwaves move in the opposite direction to the main trend. This is one way of identifying the start of a market correction. Likewise, we can identify when the market correction is over and the main trend has resumed by looking for a five-wave move in the direction of the main trend, which in our case is down since wave (A) is pointing down.

In conclusion, through the use of Elliott wave analysis, it looks like the Financial Select SPDR has now completed waves (A) and (B) of an ABC zigzag market correction that is correcting the previous bull market in the financial sector. It further looks like the final leg down, wave (C), is just getting started. A close below wave (A) will confirm that this final leg down is truly under way. However, a close above wave (B) will signal that wave (B) is not yet completed. ■

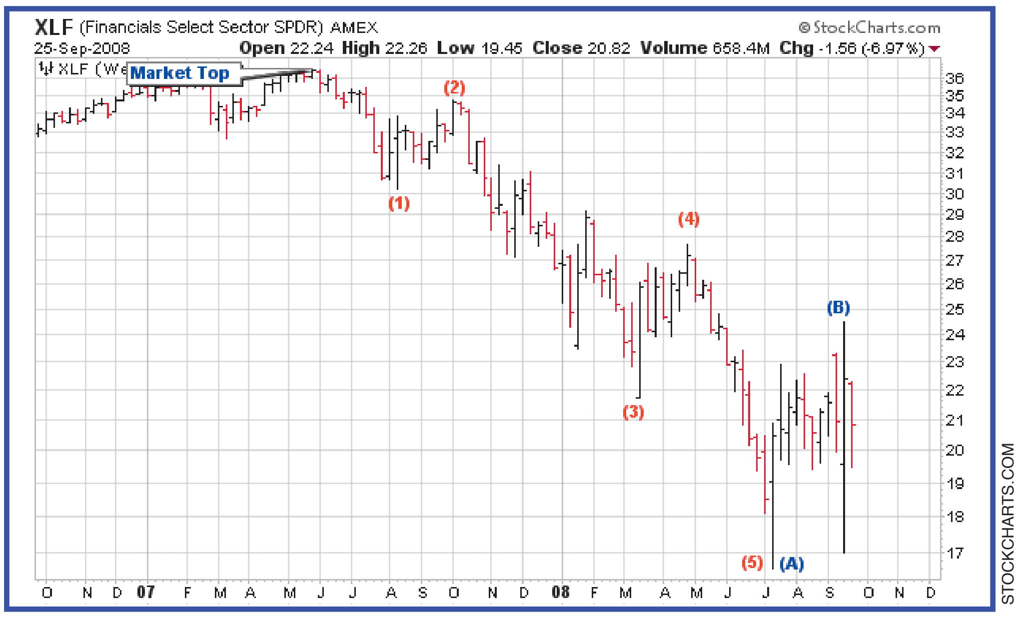


FIGURE 1: XLF, WEEKLY. This chart shows five waves down. According to RN Elliott, the first five waves define the direction of the next larger trend, which in the case of XLF is down. This chart also shows that these five waves down also form wave (A) of an ABC zigzag market correction.

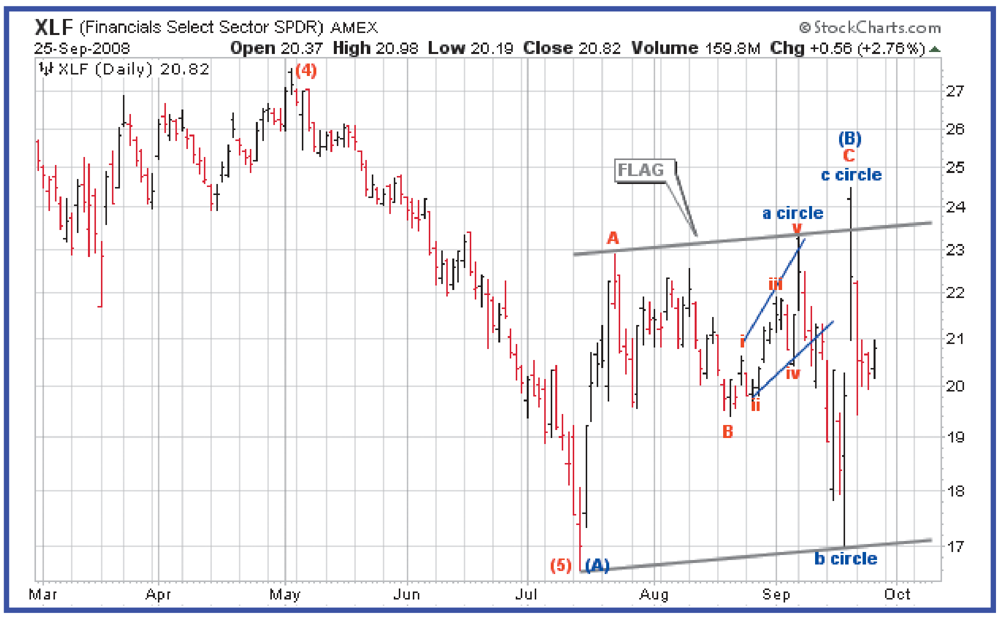


FIGURE 2: XLF, DAILY. This chart shows the detail of wave (B) of the ABC zigzag market correction. Since all the subdivisions of wave (B) have been identified, wave (B) is now complete.

FIGURE 3: XLF, 10-MINUTE. This chart shows five waves in the direction of the main direction of the ABC zigzag market correction. These five waves signal that wave (C), the final leg down of the ABC zigzag market correction, has resumed.

FIBONACCI

Another CRB Support Level

by James Kupfer

The CRB has fallen to a significant Fibonacci retracement level. Look for a bounce near here.

Tradable: CRY 0

Last Monday (October 6, 2008), I reported that the CRB index was approaching a convergence of support zones around 328 that "may help the CRB from falling any further." They did not.

The CRB briefly paused at the support level I pointed out and then proceeded to plummet through it. A little over a week later, the CRB is now at another important support level near 293.

There are two important points of support that the CRB is currently at. First is a 61.8% Fibonacci retracement level drawn between the start of the commodity bull market in November 2001 to its recent top in June/July (Figure 1). This is a very long-term support line that should be of major importance. Second, the CRB is approaching the green support line drawn from the major January 2007 bottom.

While this 293 level is not likely to hold for the long term, it could prove to be a major bottom for the next few weeks to months (Figure 2). Should it not hold, then look out for the next major support level around 250. ■

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This article was first published on 10/16/2008.
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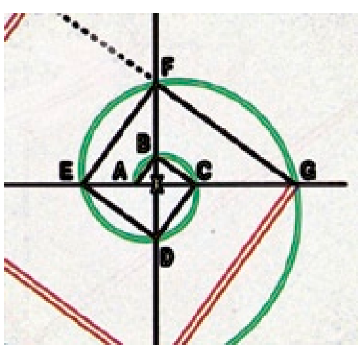
WEALTH-LAB

FIGURE 1: CRB, DAILY. This long-term support line should be of importance.

FIGURE 2: CRB, DAILY. While this 293 level is not likely to hold for the long term, it could prove to be a major bottom for the next few weeks to months.



SUPPORT & RESISTANCE

Bonds Hit Support

by Arthur Hill

The iShares 20+ Year Bond ETF declined sharply over the last five days, but support is at hand and traders should be on guard for a bounce.

Tradable: TLT

Figure 1 shows daily candlesticks over the last five months. TLT broke resistance with a surge from mid-July to mid-September. Bonds came down hard after the Paulson plan was first announced and TLT found support near broken resistance. Bonds then bounced as the stock market tanked in the second half of September. TLT surged to resistance and formed a big bearish engulfing pattern five days ago.

This short-term candlestick reversal pattern was confirmed with further weakness over the next four days, but TLT was trading right back at support and starting to firm. Despite a wild ride since mid-August, the breakout is holding and TLT remains bullish overall. Look for a bounce off support here to continue the bigger uptrend that began with the August breakout.

Figure 2 shows weekly prices and an even bigger uptrend. TLT broke resistance with a surge at the end of 2007. Broken resistance turned into support in 2008 and there were support numerous tests. In fact, the ETF briefly broke support in May 2008 (bear trap) but quickly recovered and held on the next test in July. TLT went on to hit a new high in September and the big trend is up.

There is some concern with two big bearish engulfing patterns over the last four weeks. These show resistance and selling pressure but are not enough to actually reverse the uptrend. Confirmation with further downside and a convincing support break is needed to reverse the trend. For now, these just show resistance. ■

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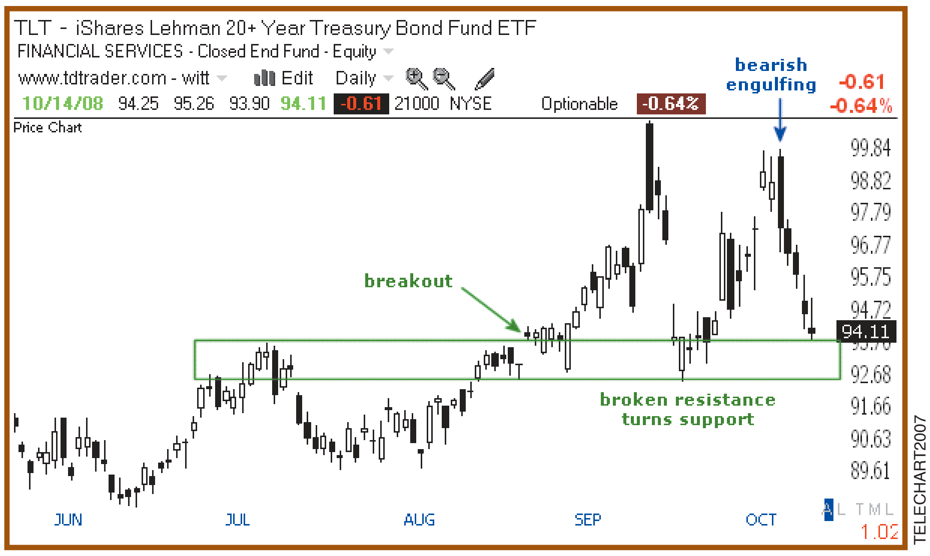

FIGURE 1: TLT, DAILY. TLT broke resistance with a surge from mid-July to mid-September.

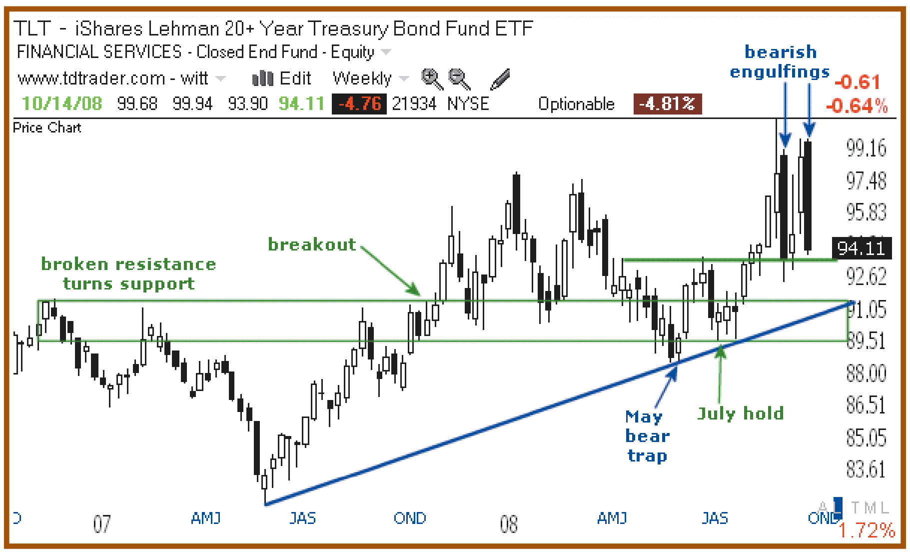

FIGURE 2: TLT, WEEKLY. TLT broke resistance with a surge at the end of 2007.

The S&P 600 Small Cap Index Hits Target

by Chaitali Mohile

The S&P 600 Small Cap Index has reached the target on a head & shoulders top reversal pattern. After the prolonged fall, the index shows bullish signs for the rally.

Tradable: $SML

The S&P 600 Small Cap Index ($SML) formed a head & shoulders top reversal pattern on the monthly chart (Figure 1). The left shoulder was formed in 2006, and the pattern was completed in September 2008. The breakdown target, below the neckline support at 350 levels, was achieved by the end of October. Here, the potential target on the head & shoulders top reversal is calculated by measuring the distance between the highest peak and neckline support, and then subtracting this distance from the breakdown level. Therefore, 350 (breakdown level) – 100 (450–350) = 250. We can see in Figure 1 that $SML moved below 250 (target) in October and rushed back to close at higher levels.

The relative strength index (RSI) (14) gradually moved to bearish levels at 30 from the overbought area. The indicator is not oversold, but if the support is established at 30 levels, the fresh bullish strength may get generated. In addition, $SML has hit the target on the reversal pattern, so a minor relief rally can be anticipated. However, the long-term trend indicated by the average directional movement index (ADX) (14) is bearish. During a downtrend, an index or equity can undergo small rallies.

The weekly chart (Figure 2) would help to reconfirm the bullish rally in the near future. In Figure 2, the 200-day moving average (MA) was strong support for $SML. After the breakdown below the 200-day MA, the index entered a fresh downtrend with robust selling pressure. The index plunged to 260 levels, and thereafter, the descending move slowed down. The recently formed bullish candle with a low at 240 levels has completely covered the previous bearish candle forming a bullish engulfing pattern. This pattern suggests the beginning of a fresh upside rally. The encouraging volume would add strength to the future rally. The relative strength index (RSI)(14) is also ready to surge from oversold territory. Hence, fresh long trades can be initiated with a short-term view.

The negative directional index (-DI) of ADX (14) indicates lessening selling pressure, though the downtrend is developing. This descending selling pressure would definitely energize buyers to carry the bullish rally higher. The relief rally across the globe would give a boost to traders and make the upward move in $SML successful.

Thus, both charts suggest a temporary pullback for the S&P 600 Small Cap Index. ■

FIGURE 1: $SML, MONTHLY. The target on the head & shoulders top reversal pattern is achieved. The long lower shadow of the candle indicates that the index has closed much higher after hitting the target at 250.

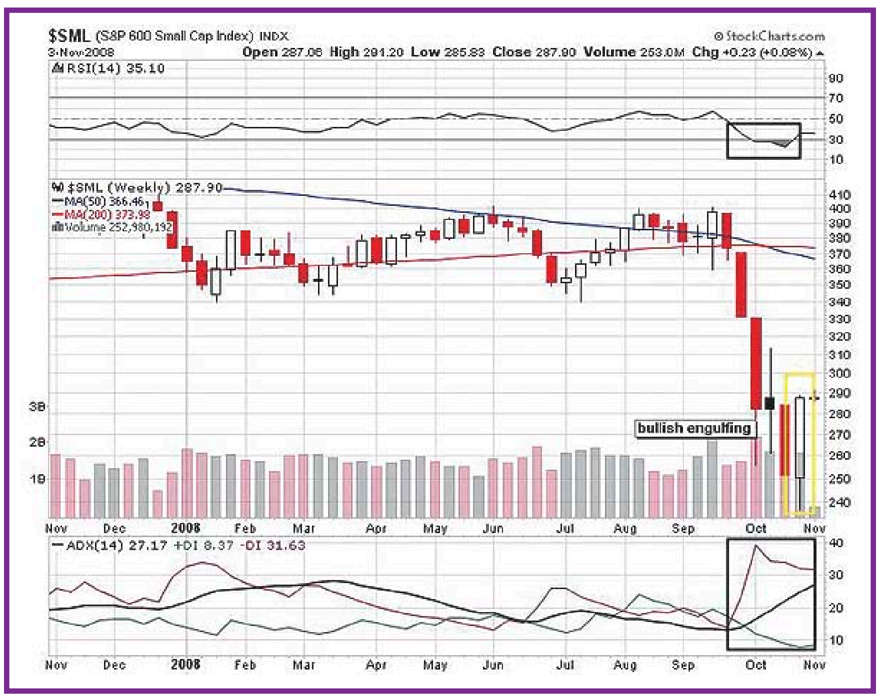

FIGURE 2: $SML, WEEKLY. The bullish engulfing candlestick pattern suggest an upcoming bullish rally. The oversold RSI(14) also support the rally, indicating the possibility of fresh trading opportunity.

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This article was first published on 11/4/2008. See www.Traders.com for more.

ELLIOTT WAVE

Energy Select SPDR Has Peaked

by Alan R. Northam

The bull market in XLE that started in 2002 came to an end in May 2008. XLE has broken the up trendline and is now in a market correction that could see XLE fall to 50 or more.

Tradable: XLE

Figure 1 is a monthly bar chart of the Energy Select Sector SPDR (XLE). This chart shows that over the last six years, the energy sector has been in a long-term bull market. Figure 1 shows a long-term trendline drawn off the monthly price lows from mid-2002 to mid-2003. Figure 1 also shows that the price of energy started to accelerate in mid-2003 and is illustrated by the more steep long-term trendline labeled "accelerated LTTL." This accelerated trend peaked in May 2008 and has been trading lower over the last three months. In July, energy broke down and closed below the accelerated trendline, ending this long-term upward trend.

Upon completion of an upward trend, a market will enter into a correction. These corrections normally occur as an ABC zigzag where wave A is a downward wave and is composed of five waves. Wave A is then followed by a B wave that unfolds in the upward direction and is normally a small abc zigzag. Once wave B is complete, wave C begins and unfolds in five waves and is often the length in time and price as wave A. XLE completed its upward trend in mid-May 2008 and has been in a market correction since. From mid-May to early September, XLE unfolded in the downward direction in five waves to complete wave A of an ABC zigzag correction. Looking at the monthly chart in Figure 1, the corrective waves are not visible, making it necessary to view the daily bar chart in Figure 2 to see the corrective waves.

An astute observer will wonder how you know that wave 5 is now complete. To resolve this observation, it is necessary to go to a lower time frame such as the 10-minute chart.

The 10-minute chart in Figure 3 is shown. This chart shows the detail of wave 5. As can be seen wave 5 has unfolded in five smaller waves -- waves i, ii, iii, iv, and v. Figure 3 also shows that XLE has already started wave B.

With corrective wave A complete, wave B has started to unfold. B waves normally unfold as small abc zigzags and should be complete somewhere near the high of wave 4. I have shown this small B wave ending at the top of the open gap in Figure 2. Markets tend to move up to close an open gap and then immediately turn back down so this is a logical place for wave B to end. Once wave B completes, XLE should then turn back down in five waves to complete wave C. I have shown a target price for the completion of wave C to be at 50. I arrived at this price target by taking the length of wave A and subtracting it. However, should XLE break down below the more shallow long-term trendline shown in Figure 1, then this market could fall to much lower prices.

In conclusion, the upward trend in the Select SPDR XLE that started in 2002 came to an end in May 2008 and has entered into a market correction. Market corrections normally unfold as a three-wave ABC zigzag affair with wave A of this zigzag now complete and wave B just getting under way. Upon completion of wave B, a final wave C in the downward direction will take XLE to a final low price that has been calculated to be at 50. There is, however, a possibility that XLE could fall to much lower prices. Once the market correction is over, a new bull market in energy will emerge. ■

FIGURE 1: XLE, MONTHLY. This price chart of XLE shows the long-term trendline and the accelerated long-term trendline. Note the breakdown in the accelerated long-term trendline July 2008.

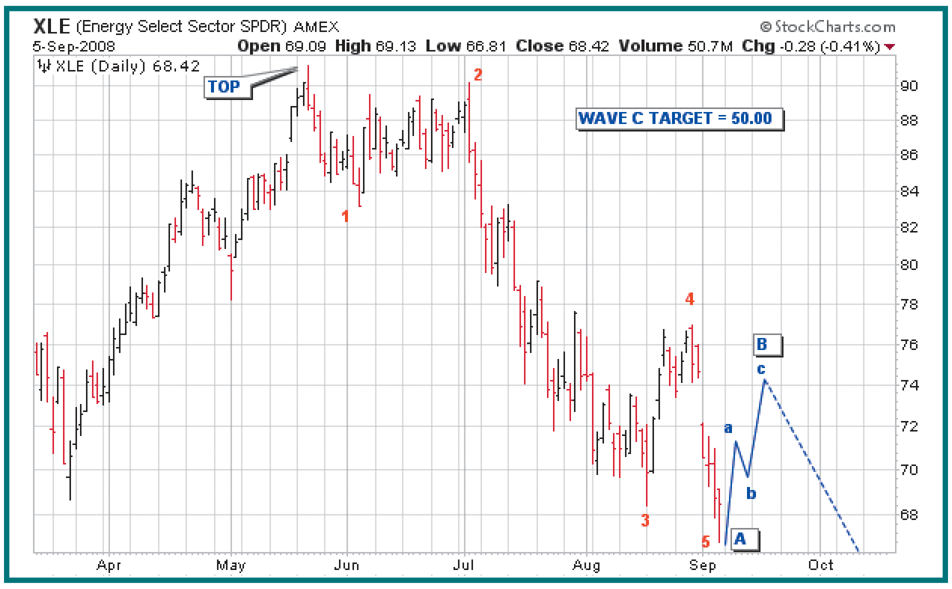

FIGURE 2: XLE, DAILY. This chart shows the five Elliott waves that make up corrective wave A. Note the B wave forecast in blue made up of an abc zigzag and ending at the top of the open gap. Also note that the target price of zigzag wave C is calculated at 50.

FIGURE 3: XLE, 10-MINUTE. This 10-minute price chart of XLE shows the small Elliott waves that make up wave 5 of corrective wave A. Note that wave 5 is made up of five smaller waves showing that wave 5 down of wave A is complete. This chart also shows that corrective wave B has already started.

Utilities Select SPDR Hits Target

by Alan R. Northam

XLU formed a head & shoulders major trend reversal pattern and has hit the price target based upon this pattern. Is XLU now ready to bounce or will it continue lower?

Tradable: XLU

On August 8, I wrote an article entitled "Utilities Select SPDR Head & Shoulders." In that article, I showed the expected price target of $27.00 per share for XLU. I encourage all to read that article for background information and how this price target was arrived. Figure 1 shows a similar weekly chart as was published on August 8. This chart shows the large head & shoulders major trend reversal pattern that took more than one year to complete. Head & shoulders patterns are complete when the neckline is clearly broken. Figure 1 also shows that the price target for XLU has now been reached. Price targets are just that: they are targets and do not necessarily indicate that the particular market will reverse its trend.

Figure 1 includes the relative strength index (RSI). This index shows that it has now fallen below its 30% level, indicating that XLU has been oversold. Normally, when a stock or market has become oversold, it sets itself up for a bounce to relieve this oversold condition. When the market bounces or turns upward, the RSI will move back above its 30% line to indicate that the market is relieving itself of its oversold condition. However, in a strongly trending market, the RSI can remain in oversold territory for quite some time. For this reason, I have also shown the average directional movement index (ADX). ADX (black line) has recently moved above its 30% line, indicating that a strong trend is in place for XLU. Therefore, it is possible for the RSI to stay below its 30% line and may not move above it for quite some time before signaling a bounce is in place.

In Figure 2, I zoom in on XLU by showing that daily price chart. The daily price chart shows that the RSI is below its 30% level signaling that XLU is also oversold on a daily basis. The ADX also shows the XLU is in a strong downtrend on a daily basis as well. Looking at the last daily bar on the chart, note that XLU opened near the top of its range and closed near the low of its range. This indicates that sellers are firmly in control of this market. Also this last bar made a lower high and a lower low compared to the previous bar, confirming that the downward trend is still in force. Note also that the daily bars have been getting longer over the last several days, indicating that the downward trend is gaining momentum. Therefore, by looking at the daily bars there is no indication that the downward trend is about to end.

FIGURE 1: XLU, WEEKLY. This chart shows the head & shoulder major trend reversal pattern. This chart also shows the minimum price target derived from this reversal pattern. This chart also shows the Fibonacci retracement levels as high-probability areas for a market bounce.

To get an idea of the possible lower price level that could stop XLU from trending lower, I refer back to the Fibonacci retracement levels in Figure 1. Figure 1 shows that XLU has traded below the 50% retracement level. This indicates that XLU will most likely continue lower to the 61.8% retracement level, the next likely price level for a bounce to occur. However, should XLU trade through 61.8%, then the final stopping place is the 78.6% Fibonacci retracement price level.

If XLU continues lower from there, then there exists a high probability that XLU will continue to move lower. XLU should then find strong support at the 2002 low.

In conclusion, XLU has now traded down to our minimum price target of $27 per share. However, there is no indication that XLU is about to turn back up. Therefore, expect XLU to continue lower and look for the ADX to turn lower and the RSI to turn upward to signal a bounce to relieve itself of its oversold condition. ■

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FIGURE 2: XLU, DAILY. This chart shows the ADX and RSI. The ADX shows that XLU is in a strong downtrend and the RSI is showing that XLU has become oversold as a result of this strong downward trend.

Oil vs. Airlines: Airlines Poised To Take Flight?

by Donald W. Pendergast Jr.

The Oil Index and Airline Index charts suggest that airlines are the stronger sector of the two — for the moment.

Tradable: XAL

For the past few years, the decision to be long oil/oil services stocks and short airline stocks was a comparatively easy choice to make. As crude oil soared, airline balance sheets came unglued, losses mounted, and their market capitalizations plummeted. Meanwhile, energy services/energy industry outfits like Halliburton (HAL) and Petrobras (PBR) continued to make new highs with ease. See Figure 1.

Then July 2008 arrived, and the entire situation reversed with a speed and violence rarely seen in the financial markets. Crude oil, along with many other commodities, heavily overbought by hedge funds and other deep-pockets speculators, were sold with abandon as the global financial situation precipitated a massive rush to the safety of cash. As the price of oil was crushed, the share prices of most energy/energy services companies were also mashed like soggy cigarette butts on the sidewalks of Manhattan, losing even more in percentage terms than crude did.

The resulting damage is reflected in the weekly Oil Index /Airline Index ratio chart, which is down by approximately 65% since the July high. Generally speaking, the Oil Index component of the ratio (XOI) has been underperforming more than the Airline Index component has been outperforming, although the recent technical action in the Airline Index seems to imply that the worst may be over, and that a modest uptrending phase may be imminent. The XOI/XAL weekly ratio chart also appears to bear this out, even though the large reversal candle off of two important support levels (the Fibonacci 0.786 retracement and a prior major support line) suggests that the ratio could be temporarily oversold. See Figure 2.

The weekly Airlines Index chart (XAL) has a number of interesting technical confluences that suggest that the worst phase of the selloffs are over and that a new uptrending phase (or a double bottom) may be taking root. The three well-spaced down waves are fairly close in ratio (time and price), and many completed bear markets also seem to manifest such price action before hammering out a major low. The bump-and-run moving average convergence/divergence (MACD) action also looks bullish, as does the higher low, established two weeks ago. Overhead, XAL now must clear the recent high at 28.22 and the 50-week exponential moving average (EMA), currently near 27.00. If and when that happens, the Fibonacci 0.382 barrier near 33.35 might be a likely target price for traders.

Finally, let's examine the monthly Oil Index chart, which is the one displaying some of the worst technical damage in recent memory. Down by more than 30% in just three and a half weeks, there appears to be little standing in its way other than a significant Fibonacci retracement level (0.786) and a previous support line. However, given that the index is off by more than 50% since July, the probabilities of a reaction move higher seem to be increasing by the day, meaning that those short the oil index component stocks would do well to tighten their stops and/or consider easing up their exposure to the short side. See Figure 3.

Given all of the technical evidence, the charts for the moment appear to favor the airlines index on the long side and the oil index as a hold/cover situation. ■

FIGURE 1: OIL AND AIRLINES. The oil index/airline index ratio may be due for a technical reaction higher.

FIGURE 2: XAL, WEEKLY. The airline index appears to be in better technical shape than the oil index.

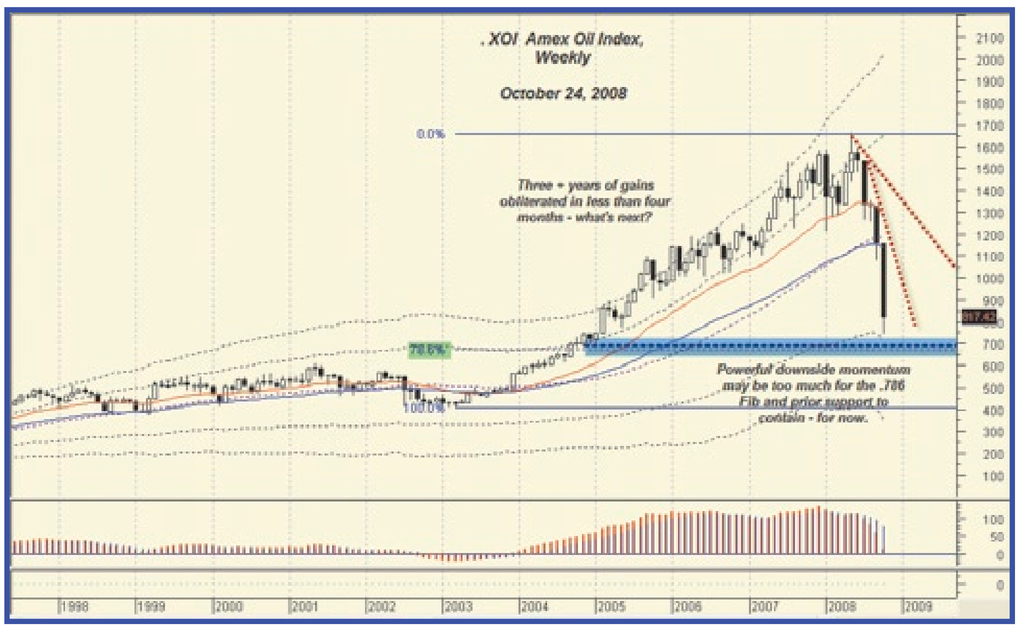

FIGURE 3: OIL, WEEKLY. The oil index has A powerful downside momentum, but a short squeeze could be devastating.

The weekly Airlines Index chart (XAL) has a number of interesting technical confluences that suggest that the worst phase of the selloffs are over.

FIBONACCI

Is Gold Still Golden?

by James Kupfer

Gold appears to be in a prime spot for a reversal.

Tradable: XGLD

Gold has taken a mighty tumble over the last few months, falling from a high of more than $1,000 an ounce to around $735. Now, a convergence of Fibonacci support zones and a significant new support zone at the current price level indicate that this might be a prime time to buy gold for at least a significant bounce.

On the two weekly gold charts seen in Figures 1 and 2, I have drawn significant Fibonacci retracement levels. There is such a clutter of Fibonacci levels that the charts are included primarily just to show where the levels are drawn to and from.

Circles in blue denote the oldest Fibonacci level, starting with the start of the bull market in gold from February 2001 to the recent top in March 2008. The 38.2% retracement level is at $732.42. Next is the retracement level formed between the June 2007 low and March 2008 top, which is shown at the start with a red circle. The 61.8% retracement level for that move is $727.94. See Figure 1.

Moving to the closer view (Figure 2), you can see the light green Fibonacci retracement level calculated between the March 2008 top and April 2008 bottom. In this case, 161.8% of that move leads to a price target of $731. Finally, 123.6% of the move from July to August suggests a price target of $721.46. As mentioned previously and shown as a brown line on the charts is the May 2006 top at $730. As a previous level of significant resistance, it now turns into a support line.

In summary, four different Fibonacci retracement levels and an old support point all indicate that gold is currently at a level of significant support. Four of the five support prices are within $2.50 of each other. The last and least reliable since it is of the shortest time period and a less commonly used Fibonacci number is still within $9 of the other levels. While gold can move lower, like it did last week, without breaking the support levels, prices now appear in a favorable position to buy. ■

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This article was first published on 10/28/2008.
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FIGURE 1: XGLD, WEEKLY. Circles in blue denote the oldest Fibonacci level, starting with the beginning of the bull market in gold from February 2001 to the recent top in March 2008.

FIGURE 2: XGLD, WEEKLY. The light green retracement level is calculated between March 2008 top and April 2008 bottom.

Newmont And The Gold Bugs Are Very Oversold

by Donald W. Pendergast Jr.

After enduring months of record selloffs, Newmont Mining and the Gold Bugs index may be close to a reversal zone.

Tradable: NEM

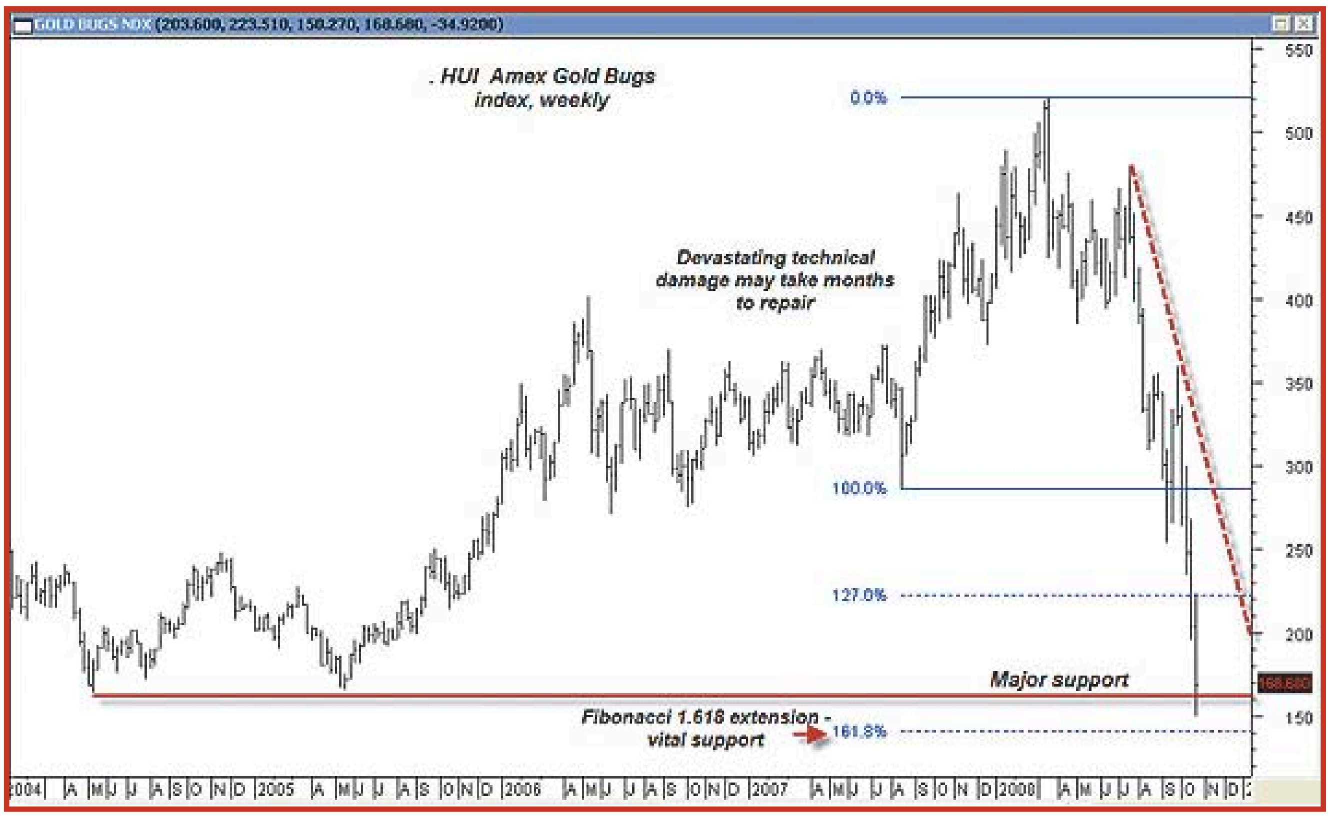

FIGURE 1: AMEX GOLD BUGS, WEEKLY. The AMEX Gold Bugs index could react violently if a short-squeeze were to take place.

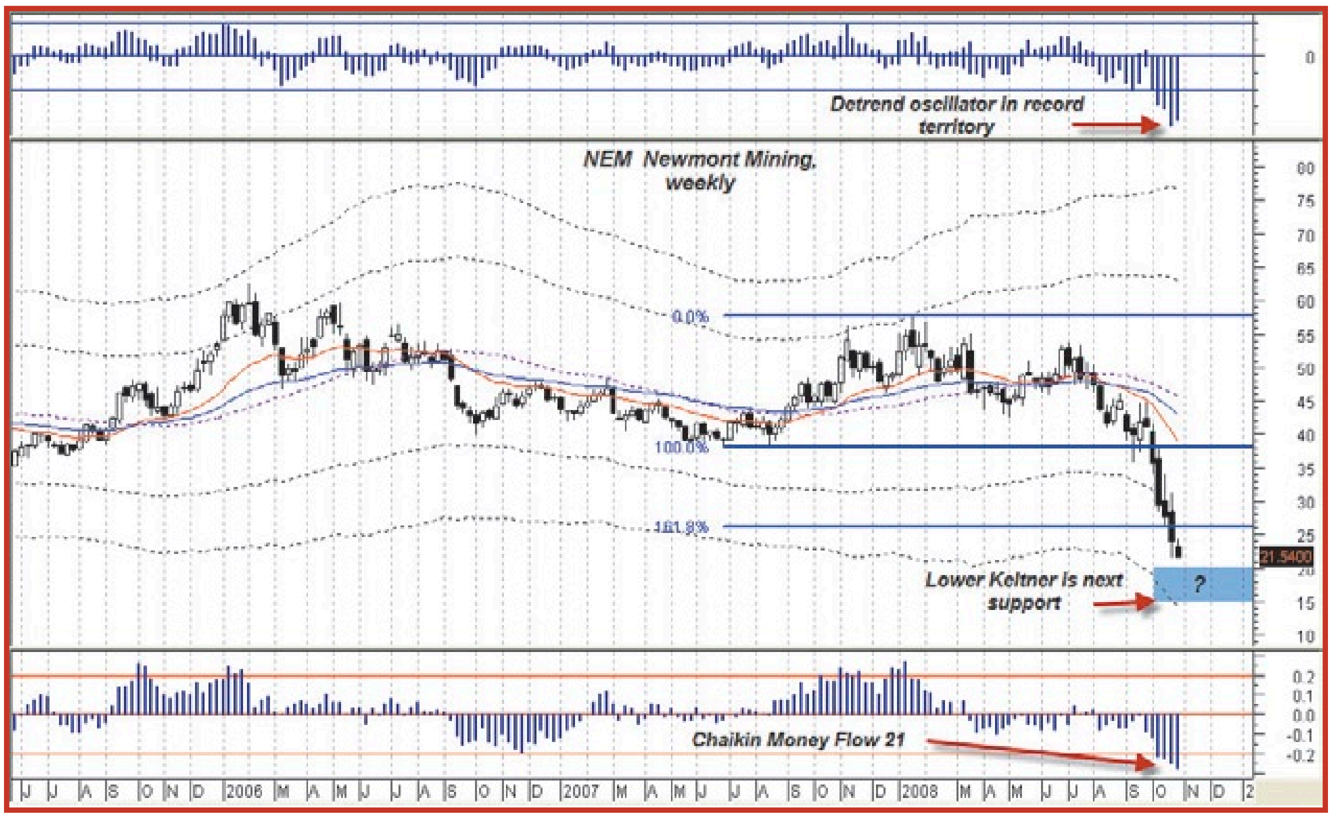

FIGURE 2: NEWMONT MINING, WEEKLY. Newmont Mining's chart offers mixed technical clues.

It's hard to believe that the AMEX Gold Bugs index was over 519 a mere eight months ago, as it has lost more than two-thirds of its index value since those days. Since then, precious metals stocks like Newmont, Goldcorp, and Agnico-Eagle have all been major casualties as the global market selloff in stocks and commodities routed everything in its wake, including these major gold producers. The charts, however, do seem to be offering some hope that a bottom in precious metals stocks may be approaching.

Let's look at the weekly chart of the AMEX Gold Bugs index first (Figure 1); the technical damage is extreme, to say the least, but the index price is still above the major support line that extends back to 2004–05, having completed (for the moment) a successful test of that important price zone. In addition, the price has failed to drop all the way down to the Fibonacci 1.618 extension level — for the time being. If the broad markets put in a firm low soon, expect the Gold Bugs index to bottom at about the same time. If the broad markets keep selling off, well, the 'Bugs might just retrace most of the gains made since early in this decade, no small feat for an index that had been up more than 12-fold since late 2000!

Next, let's examine the weekly chart of Newmont Mining, one of the larger component stocks in the Gold Bugs index — it makes up 11% of the total index value and is a reasonably good proxy for the index as a whole (Figure 2). Newmont has certainly taken a dive, but it's still in better technical shape, having fallen less in percentage terms. Other than that, Newmont presents a mixed picture of technical evidence. Price blasted right through the Fibonacci 1.618 extension level, and there isn't much support between $15–20, although the lower Keltner band, (set at 6 + standard deviations) would likely offer at least some interference on further weakness. On a more hopeful note, the detrend oscillator (the top pane of Newmont chart) is wildly oversold and is in record negative territory. That indicator is also beginning to turn higher, also a potential sign of a bottom.

Given all of the global financial bailouts, $2 trillion-plus now added to the money supply in the United States alone, serious consumer price inflation is a near certainty in the next few years, and that's usually when gold and gold stocks like Newmont begin to earn their keep. So while the current technicals are sobering, the fundamentals for gold and gold stocks still appear to be bright. ■

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This article was first published on 10/29/2008. See www.Traders.com for more.

Oil Hits Bottom

by Alan R. Northam

In a previous article entitled "Is The Oil Uptrend Over?" published on 07/23/08, I wrote that oil could fall to as low as $53 per barrel. Today, I am reporting that oil has fallen to a low of $50.44 and a low in oil could be in place.

Tradable: USO

Figure 1 shows a weekly closing price chart of the United States Oil Fund (USO) since 1999. This chart shows the long-term upward trend in oil. This chart also shows my updated Elliott wave count. This chart shows that wave IV was completed in 1999 and wave V is currently in progress. This chart also shows that a wave 5 circle is now under way and is subdividing into five waves. Once these subwaves are complete, that will also complete a wave 5 circle and a wave V. The importance of this chart is to show that oil has further to go on the upside before another meaningful correction will occur and will most likely take several years to complete. This analysis does not bode well for the economy going forward and shows that we must find alternatives to the use of oil.

Figure 2 shows the Elliott wave analysis of corrective wave (2) that started in July and now looks to be complete. Figure 2 shows that the market correction unfolded as a double ABC zigzag connected together by an X wave. Double ABC zigzag corrections happen occasionally. However, in more rare cases, a market correction can morph into even more complex corrective patterns. Since these cases are rare, there is a high probability that the market correction is now over. To confirm that the correction is over, I have shown a red horizontal resistance level drawn from the high price of wave B and labeled as "key resistance." Should USO close above this price level, then that will be a high-probability signal that the market correction is over and the upward trend has resumed.

As further evidence that the market correction in oil is over, see the 60-minute chart in Figure 3. This chart shows the final wave C of the market correction. I have shown that wave C has unfolded in five subwaves, wave i circle, ii circle, iii circle, iv circle, and v circle. According to Elliott wave theory, wave Cs unfold in five waves and so my analysis agrees with the Elliott wave theory. Following the completion of wave C down, the market has now started to trend upward. It is still too early to determine the structure of the upward trend, so I have shown it as two possibilities. The market could be unfolding as a more complex market correction, so I have shown that the market could be forming an abc zigzag. If USO is going to form a more complex corrective wave structure, then this market should turn back down where wave (c) is equal to wave (a). However, if this market continues higher, then there is a high probability that a five-wave move up is under way. According to Elliott, five waves define the direction of the next larger trend, which would be up.

In conclusion, it looks like oil has completed its market correction and resumed its upward trend. A close above key resistance is necessary to confirm the continuation of the upward trend. However, if the market turns back down at around $60 per barrel, then there exists a high probability that the market correction is not yet over. Either way, oil is either at a market low now or will be at a market low with one more downward leg, after which the next leg of the upward trend in oil will be under way. ■

FIGURE 1: USO, WEEKLY. This chart shows that the long-term upward trend in oil is still in progress.

FIGURE 2: USO, DAILY. This chart shows the Elliott wave count of the latest market correction. This figure shows that USO has now completed a double ABC zigzag corrective structure and key resistance level.

FIGURE 3: USO, HOURLY. This chart shows the detail of the final wave C of the ABC zigzag market correction. This chart also shows that the upward trend is now starting to resume.

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CURRENCIES

RSI

The Dollar Divergence

by James Kupfer

The US Dollar Index is forming a divergence with the relative strength index. Is this a warning?

Tradable: DXY0

The US dollar has been in a fierce uptrend since July 2008. Recently, however, the relative strength index (RSI) has started to diverge with the price action in the dollar. This could well be a precursor of future weakness.

The RSI is a popular momentum indicator that gauges the relative strength of gains or losses in a security. Generally, it is best to see the RSI continually increasing when the price of a security is increasing as well. Just like with a stock, it is best to see a pattern of higher highs and higher lows.

On Figure 1, you will see two sets of lines. Starting with the yellow lines, you can see in the price pane that prices were moving up steadily. However, the line in the RSI pane was flat. This is the first divergence. The second divergence occurred where the red lines indicate. Prices have moved up to a new high, but RSI has not reached a commiserate new high. While a RSI divergence with price is not a sell signal by itself, it is a flashing light warning that something may be wrong.

It is also interesting to note that the dollar index is only about a point away from overhead resistance in the form of a descending 61.8% Fibonacci fanline (not shown). Two previous Fibonacci fan levels at 38.2% and 50% are shown in blue. Note the price action at each level, which would indicate that prices are affected by the fan lines to at least a minimal degree.

Combine the RSI divergence with the approach of the Fibonacci fanline and it is a clear warning that prices might move downward in at least the near term. ■

FIGURE 1: US DOLLAR, DAILY. With the yellow lines, you can see in the price pane that prices were moving up steadily, but the line in the RSI pane was flat.

CONSOLIDATION FORMATION

The Volatile US Dollar

by Chaitali Mohile

During consolidation, the US Dollar Index is likely to enter wild volatile sessions and may retrace to a previous low pivot.

Tradable: $USD

After a huge descending run, the US Dollar Index ($USD) formed a bottom by consolidating in the lower range of 70–74. The consolidation range broke off in July, and $USD entered a fresh uptrend after a long period of two years. Thereafter, the dollar index appreciated, and the trend was well developed. According to Figure 1, the index has recovered to about 50% Fibonacci retracement levels, and the stochastic (14,3,3) also saw a highly overbought area. The 50% Fibonacci retracement level and a declining 200-day moving average (MA) may slow down the dollar growth.

$USD may undergo a volatile consolidation phase in the narrow range of $80–82, as the stochastic (14,3,3) is highly overbought and the trend remains bullish. The stochastic may show shaky moves in this zone that can result in price volatility. The oscillator can remain overbought for some more time, but the price level is likely to fluctuate. In the current financial situation, it looks like $USD may surge above the resistance and appreciate another $2. But before the breakout happens, the index is likely to remain highly sensitive, and in the worst-case scenario, the lower

FIGURE 1: $USD, WEEKLY. $USD is under the resistance of the 50% Fibonacci retracement level, and a 200-day moving average.

$USD may undergo a volatile consolidation phase in the narrow range of $80–82, as the stochastic (14,3,3) is highly overbought and the trend remains bullish.

support of $80 may be challenged.

Figure 2 shows the upward journey of the dollar index since July 2008. $USD had a steep advance rally from the breakout level at $74, reached the high of $80, and retraced to the previous support of $76. $USD established support at $76, and the rally with the target of a previous high of $80 was born. The ascending move was followed by consolidation in the range of $80–82. The breakout failed due to the resistance levels that we saw on the weekly time frame. The stochastic (14,3,3) in Figure 2 is overbought, and the decline below $80 levels would be alarming. The average directional movement index (ADX) (14) indicates a developed uptrend. Therefore, $USD may consolidate in the range of $80–82. But since financial markets currently are full of uncertainty, high volatility cannot be ruled out. ■

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FIGURE 2: $USD, DAILY. The entire bullish rally from July shows $USD is consolidating with the support of $80.

The US Dollar Index: Is A Breakout Or Reversal At Hand?

by Donald W. Pendergast Jr.

After an impressive three-month bull rally, the US Dollar Index is approaching an important resistance barrier: the upper Keltner band on its weekly chart.

Tradable: DX#F

It's been a remarkable run for the US Dollar Index since late July, and there has been only one minor corrective move since then, in late September (Figure 1). As the world disgorged itself of long crude oil, gold, silver, and other commodity contracts, money has been flowing into the dollar at a rapid pace, as traders and speculators feared that the seven-year-long global commodity bull market was finally bursting. Even the euro has retreated, down significantly from its high of 1.60 set earlier this year.

Fundamental explanations aside, that leaves us with this incredible weekly chart of the US Dollar Index (Figure 2). This index has never once pierced, much less closed beyond, its upper Keltner band since 1989, so a close above it would be a very significant event, one that could have a profoundly bullish psychological effect on traders. Conversely, a sharp reversal at or near the band might launch another round of liquidation as traders dump the dollar in anticipation of a sharp selloff. Interestingly, the daily US dollar chart is showing an exhaustion gap today (October 23, 2008), so we may already have a clue as to what the next trend direction may be for the once-mighty greenback. See Figure 2.

Adding another dimension to the dollar situation, the monthly chart of gold is currently sitting near a psychologically important support level — $700 — and current action in the yellow metal suggests that there is plenty of pent-up demand waiting to acquire metal in that price area (Figure 3). Gold typically moves inversely to the US dollar, so it will be fascinating to see how this all plays out in the next few weeks.

Right now, the dollar isn't a buy, nor is it a sell, but existing longs should have already tightened their stops in anticipation of some potentially violent price action. Wise traders will keep a close eye on the US Dollar Index, the price of gold, and the rest of the commodity and currency markets during the coming weeks. There could be major buying and/or short selling opportunities developing in many of these highly volatile, emotionally charged markets! ■

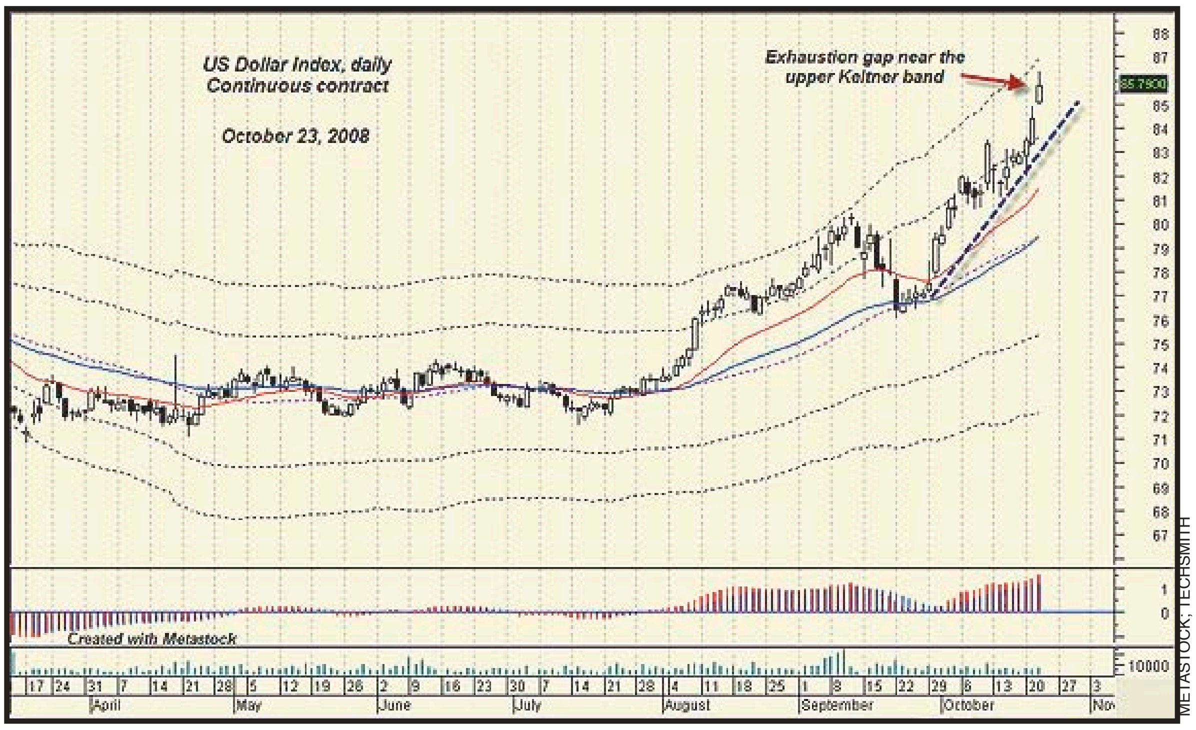


FIGURE 1: US DOLLAR INDEX, DAILY. A daily exhaustion gap near the upper Keltner band may be warning of a potential reversal.

FIGURE 2: US DOLLAR INDEX, WEEKLY. A weekly close beyond the upper Keltner band may imply more gains for the dollar.

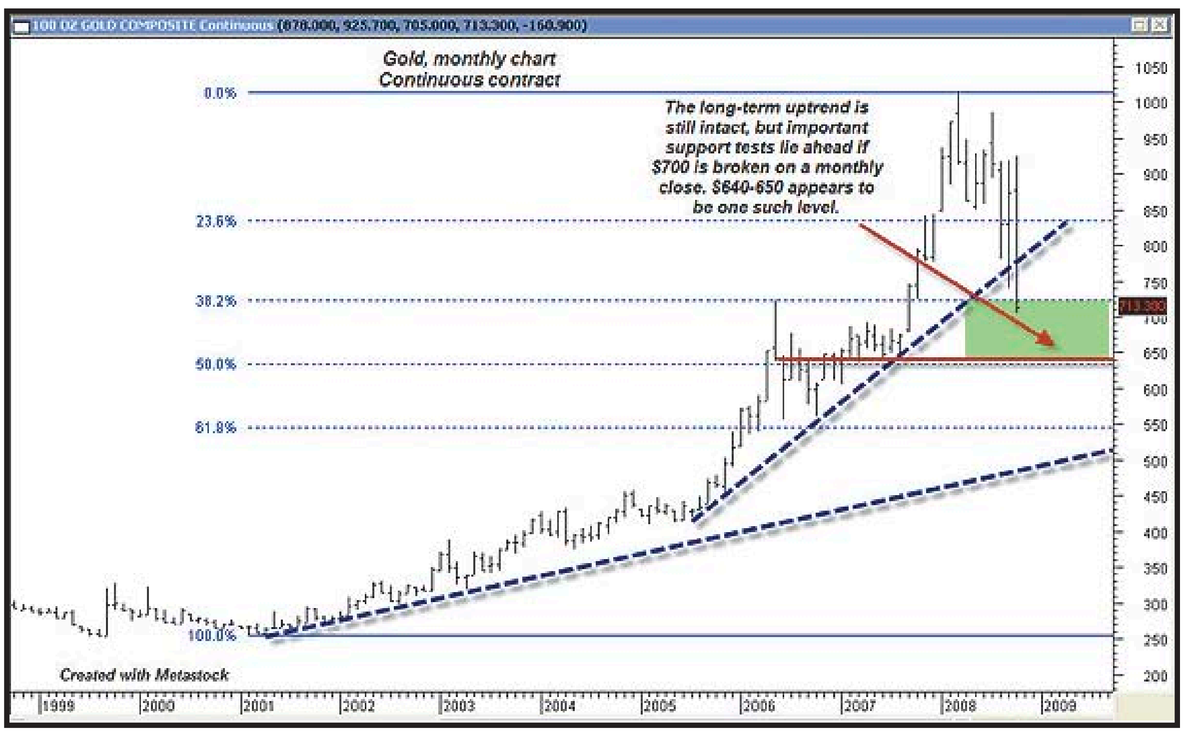


FIGURE 3: GOLD. Gold's overwhelming seven-year uptrend is still intact, but important support levels will need to hold.

Buy, Buy, Buy

by Koos van der Merwe

Has the time come?

Tradable: UDX, TYX

The story goes that before the great market crash of 1929, Joseph Kennedy, father of US President John F. Kennedy, stopped to have his shoes polished. The young boy who polished his shoes gave him advice on what shares he should buy. Afterward, Kennedy walked into his office and sold all his shares, moving into cash. He was wise enough to realize that when his shoe polisher, a young boy with minimal knowledge of the market, could advise him on what to buy, then it was time for him to get out of the market and sell, and he did.

Recently, my ex son-in-law, who knows absolutely nothing about the market, advised me to invest in US Treasury bills. Then he asked me, "What is a T-bill?"

I was stunned. With interest rates falling; with brokers thinking of jumping out of high-rise windows — if they could open them — and with the financial world collapsing all around us, was he inadvertently telling me that the bottom was in sight, and that I should do the opposite of what everyone else is doing? In other words, was he telling me to become a "Joe Kennedy" but at the market bottom, not the top?

Figure 1 is the monthly chart of the US Dollar Index. In it we can see how the index fell as the US dollar weakened from July 2001 to March 2008. Why? It is the result of the world banks selling US T-bills as they looked for cash to prop up their ailing businesses. Then in July 2008, the US Dollar Index started to strengthen. Does this mean that banks no longer had to sell T-bills to find cash because of government assistance, or were there simply no more T-bills to sell? At any rate, from then on, the US Dollar Index started to strengthen, and the relative strength index (RSI) is at overbought levels, suggesting weakness may be ahead.

A look at any currency chart confirms this. I have chosen the euro, and in it you can see how the euro has fallen sharply as the US dollar strengthened across the world as money rushed to buy US T-bills. Now it has fallen below its support line and the RSI hints at oversold levels.

FIGURE 1: US DOLLAR INDEX, MONTHLY

FIGURE 2: EURO, MONTHLY

FIGURE 3: TREASURY YIELD OPTION, MONTHLY

Is the euro suggesting strength once more as T-bills are no longer bought? (See Figure 2.)

Figure 3 is the CBOE Treasury Yield Option, and it shows how from June 2007 the price fell, forming a double bottom in March 2008, rising into June 2008, and forming what many believed was a triple top before falling to form what could well be a double bottom on October 23. The RSI is rising from oversold levels suggesting that T-bills are being bought. A study of the RSI over the recent past showed that it never truly rose above 50 before falling back. This suggests present buying could be temporary.

Protect your cash by buying T-bills. That was the recent maxim as the financial crisis worsened, but it now appears to have changed. Charts and the Joe Kennedy maxim seem to suggest that we should now be contrarian and do the Warren Buffett — look for stocks offering good yields. So it's buy, buy, buy! ■

FIBONACCI

Australian Dollar — Support Test In Progress

by Donald W. Pendergast Jr.

The Australian dollar appears to be successfully testing important support levels now and may be in position to recover as the US dollar falters.

Tradable: Australian Dollar

Currencies, commodities, equities, you name it ... it doesn't matter; everything was dumped along with the bath water during the global financial market rout of the past four months. The Aussie dollar was no exception, having shed as much as 30% against the US dollar early last week. However, the currency is now testing and/or approaching major support levels on both the monthly and the weekly charts (Figures 1 and 2). These are important support levels, and currency traders will be watching closely.

The monthly chart shows how vicious the decline has been, smashing right through three significant support levels established during 2006—08 (Figure 1). This past week, the price dropped below 0.6000, nearly hitting the "maximum retracement" Fibonacci level of 0.786 before rebounding sharply to close at 0.6656. If the 0.5800–0.6000 level holds on a retest, we may witness one of two different scenarios develop:

1 A "V" bottom, which could mean a powerful short-covering rally, or

2 A long, drawn-out A-B-C corrective pattern, with this month's low as point A.

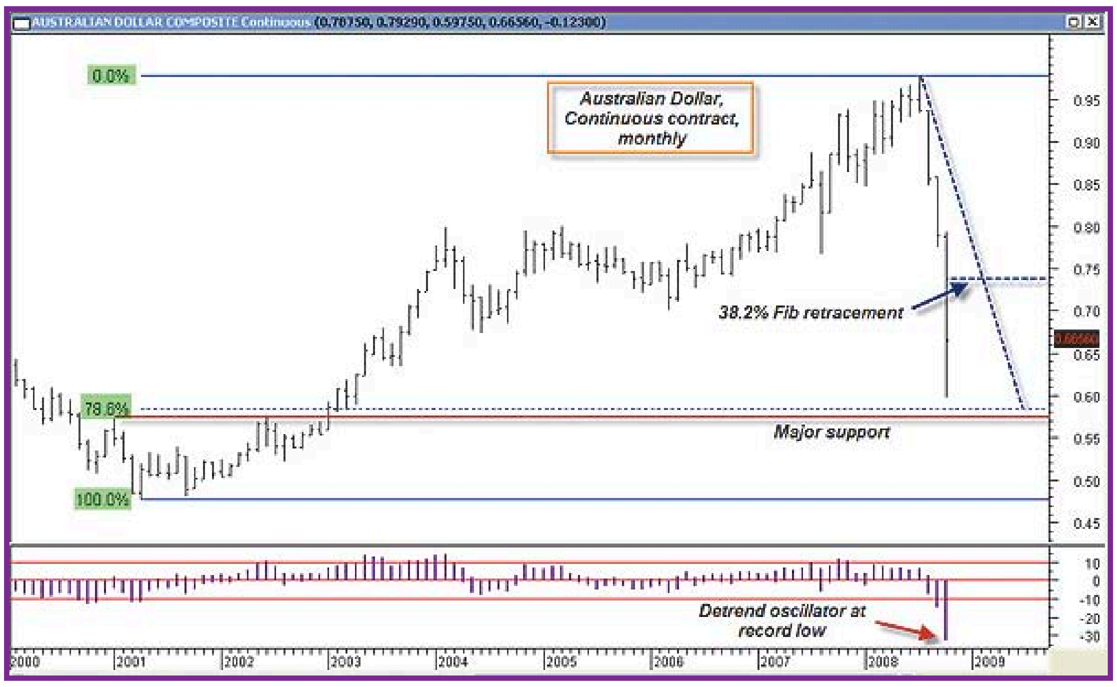


FIGURE 1: AUSSIE, MONTHLY. A successful retest of 0.6000 — will it happen?

FIGURE 2: AUSSIE, WEEKLY. Two distinct Fibonacci levels — telling the truth about support?

Given the outrageously negative reading on the monthly detrend oscillator (more than twice as oversold as it was during the August 1998 global financial crisis), the first scenario, a "V" bottom, might actually have a better than even chance of occurring, but only time will tell.

The Aussie's weekly chart (Figure 2) also features a Fibonacci theme, one that actually confirms the major support evidence on the monthly chart. When two separate Fibonacci grids agree (in this case, a 127% and 161% expansion ratio agree on a support level), the support level is considered to be more significant. It appears to be so in this case, as price rebounded sharply after a brief test of the sub-0.6000 zone. Also of note, the moving average convergence/divergence (MACD) is at its most negative reading ever, with the spread between the signal line and the indicator also in record territory.

The red dots on the chart are the 2.5 * ATR 10 trailing volatility stop. If and when price can close above that level on the weekly chart, the odds are that the downtrend is over and a period of consolidation may be due.

The long-term fundamentals for Australia and its currency appear to be sound, especially in relation to the United States and the US dollar. Australia's plentiful supply of natural gas, uranium, copper, and wheat, combined with its relatively close proximity to growing Chinese and Asian markets, all seem to suggest that the Australian dollar will be an in-demand currency for some time. However, long-term outlooks don't always jive with the "right-now" action on the charts. In the meantime, the Aussie's price action near major support levels should be interesting to watch. ■

CHARTPATTERNS

RELATIVE STRENGTH COMPARATIVE

Could You Have Predicted The Lehman Brothers Disaster?

by Koos van der Merwe

Lehman Brothers lost hope of being bailed out and was forced to announce bankruptcy.

Tradable: LEH

FIGURE 1: LEHMAN, WEEKLY. This chart of Lehman Brothers shows the sharp market plunge.

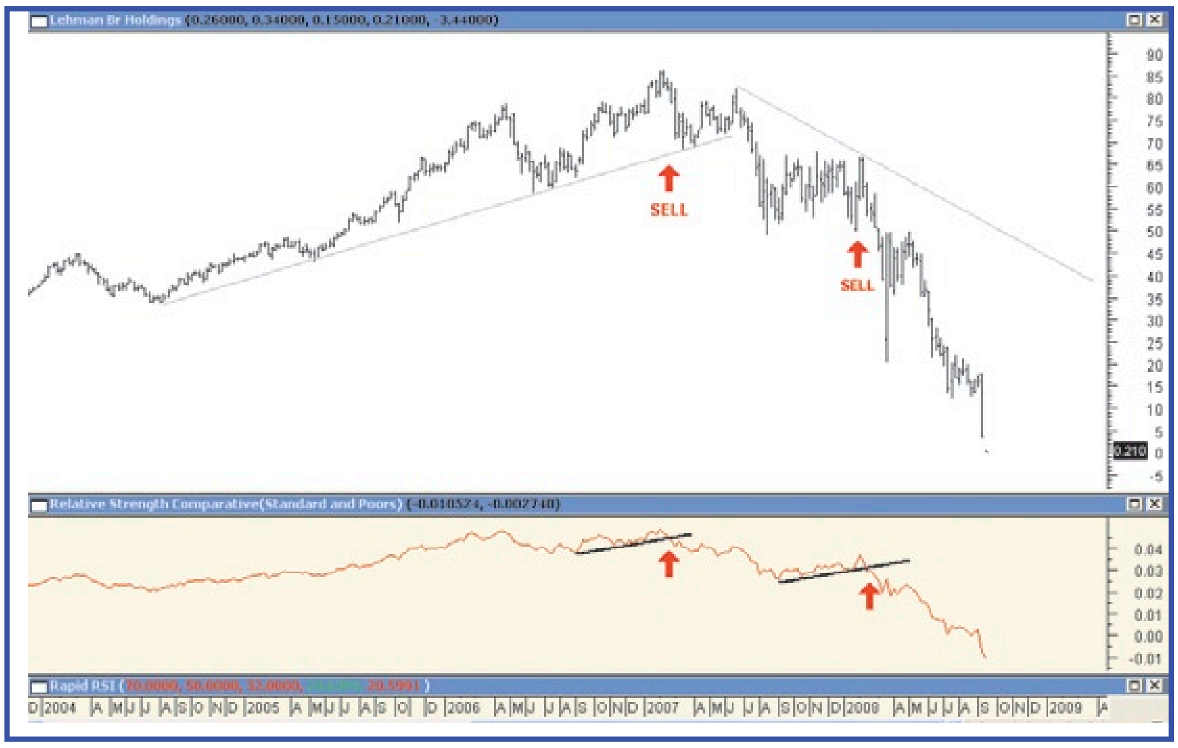
Lehman Brothers is the latest victim of the subprime crisis. Fundamentally, we know what happened, but if you were a shareholder, could a chart have warned you of its downfall?

The current argument is that central banks subscribed to one economic philosophy in an expanding economy and quite another in a contracting economy. When things are going well, markets are left alone. When a crisis develops, however, even the merest hint of one, central bankers respond by cutting interest rates in an attempt to stimulate the economy and prevent asset prices from falling. Efficient market theory at its simplest argues that there can be no bubbles, and that central banks should not intervene to restrain speculative excess. The Federal Reserve chairman at that time, Alan Greenspan, refused to prick the dotcom bubble in 1999 even after warning about "irrational exuberance." Ben Bernanke, the current chairman, appears to have learned his lesson, refusing to cut interest rates on September 16.

So would Lehman Brothers have survived if the market had been left to its own devices? Figure 1 is a weekly chart showing how Lehman rose from a humble $3.10 in October 1994 to a high of $86.18 by February 2007. I have drawn in three support lines, showing how the share price rose almost logarithmically to the high. An Elliott wave count shows a fifth wave that is larger than the third wave, suggesting a strength that we now know was a result of low interest rates resulting in overborrowing, chasing incredible profits. Yes, a correction had to follow, and an abc correction did follow, but the c-wave was not within the fourth wave of lesser degree, a suggestion that this was an abc correction in an A-wave.

The first indication that things were not quite what they should have been at Lehman was the fact that the downturn from the fifth-wave high of $86.18 occurred in February 2007, whereas we all know the market only started turning down in July 2007.

Figure 2 is therefore a weekly chart of Lehman Brothers with a relative strength indicator to the Standard & Poor's 500 (SPX). On the chart I have



METASTOCK

FIGURE 2: LEHMAN, WEEKLY. This chart of Lehman shows a relative performance indicator and sell signals.

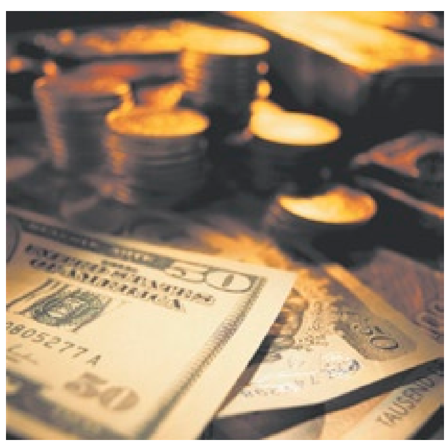
ADVANCEDGET

FIGURE 3: LEHMAN, DAILY. This chart of Lehman shows the increase in volume, on sell signals, and the false buy signals given by the RSI.

highlighted the sell signals given.

Figure 3 is a daily chart, and yes, as you can see from the RSI, a number of buy signals were given on a daily chart, especially the dramatic fall at "a," which many may have taken to be wave C, within the fourth wave of lesser degree. The price fell to a low of \$20.88 and corrected upward to \$50.05, suggesting strength ahead. There was nothing other than volume in the daily chart to suggest the weakness, resulting in the collapse and subsequent bankruptcy. Volume rose as prices fell, suggesting more sellers than buyers.

Michael Carr, in the August 2008 issue of STOCKS & COMMODITIES, wrote an article, "Relative Strength As A Selling Tool." This is the only tool used on Lehman Brothers that would have shown the way. ■



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ON BALANCE VOLUME

CME Holds Its Breakout

by Arthur Hill

The CME Group bucked the market in September with a breakout and continued relative strength points to further gains.

Tradable: CME

CME Group (CME) operates the Chicago Mercantile Exchange (CME) and the Chicago Board of Trade (CBOT). While the markets go haywire, CME acts as the messenger by processing the orders. This makes the group somewhat immune to volatility and uncertainty. CME benefits as long as traders keep trading.

The first candlestick chart (Figure 1) shows CME breaking above resistance with a gap up in mid-September. Broken resistance turned into support and the stock held the breakout over the last few weeks. Technically, there were two dips below support, but the stock recovered immediately and held support for the most part. With the breakout largely holding, I would expect further strength in the coming weeks.

Figure 2 shows a long-term perspective for CME with a few indicators. The stock bottomed in July and pretty much consolidated in August and September. This consolidation formed a base from which to launch an advance. The next target is around 500 and stems from broken support and the March–April highs (red line).

Volume and relative strength favor further gains. Upside volume started increasing in the second half of August and into September. Note how on-balance volume (OBV) surged from late July to mid-September. This move reflects strong volume on up days and further reinforces strength. The bottom indicator window shows the relative strength comparative. This indicator also broke resistance in September and moved higher in October. CME is leading the broader market (SPY) and leadership is important for portfolio managers. ■

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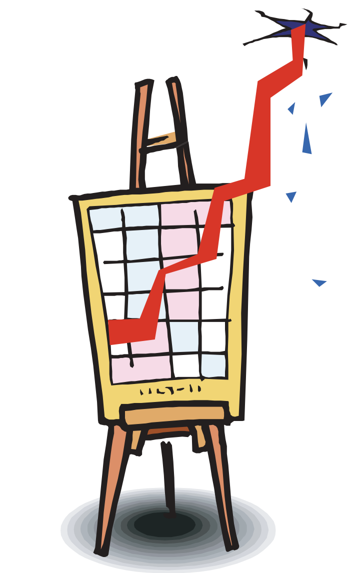

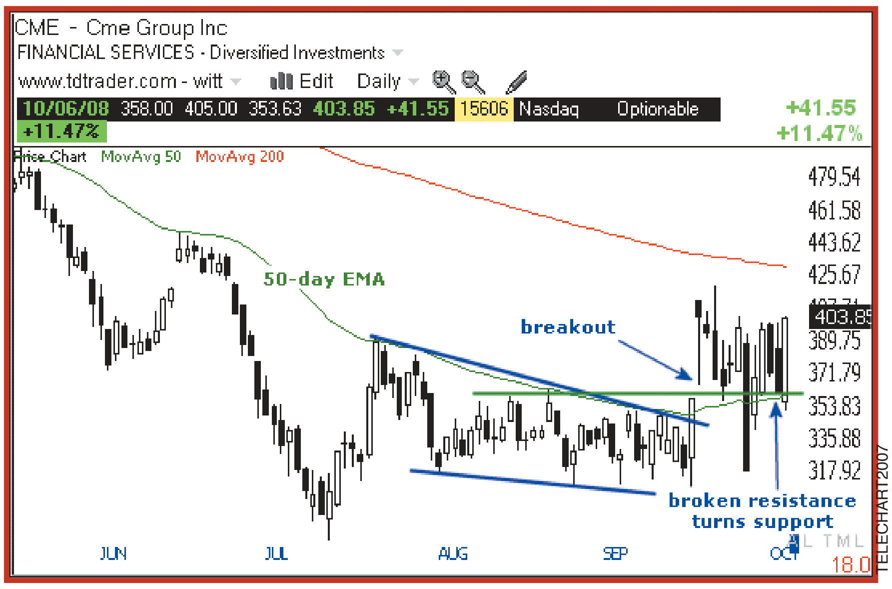

FIGURE 1: CME, DAILY. Here, CME is breaking above resistance with a gap up in mid-September.

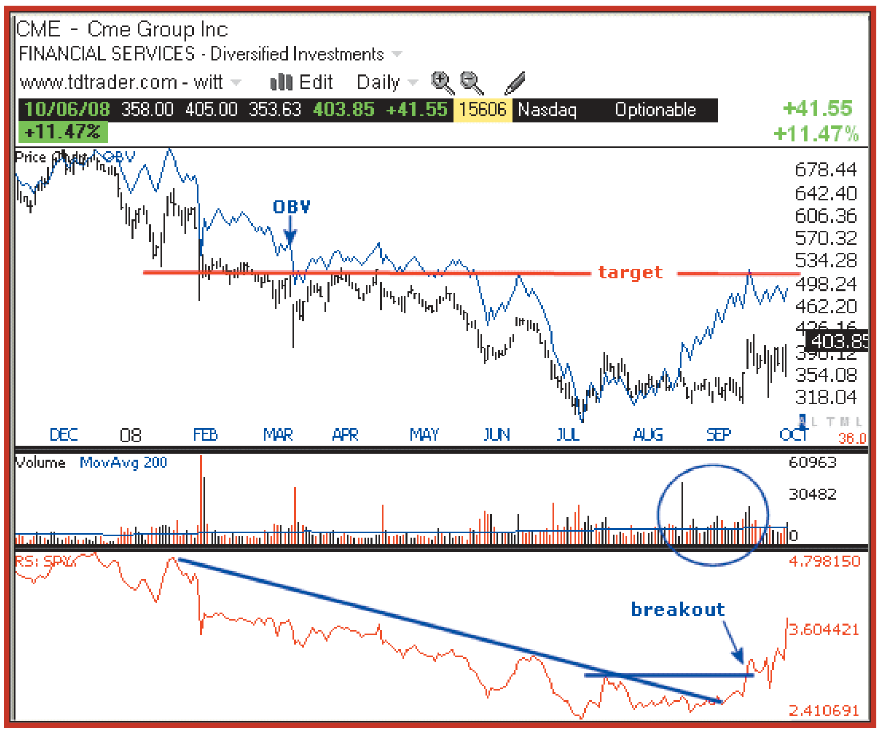

FIGURE 2: CME, DAILY. This stock bottomed in July and consolidated in August and September, producing a consolidation from which to launch an advance.

ELLIOTT WAVE

Looking For The NASDAQ Bottom

by Alan R. Northam

With the NASDAQ now in a bear market trend, it is possible to use Elliott wave theory to forecast when the downward trend will come to an end.

Tradable: $COMPQ

Elliott wave theory states that after a five-wave advance the market will undergo a three-wave market correction. Further, we can state that a major market top always ends with the completion of a wave 5 advance. With respect to NASDAQ, it is a fact that the bull market ended in 2000 with the bursting of the technology bubble marking the top of a secular bull market trend. Therefore, we can conclude that this market top completed a five-wave advance. Following this major market top, the NASDAQ has been undergoing a three-wave market

FIGURE 1: NASDAQ, MONTHLY. This figure shows the secular bull market trend and the market top in early 2000. This figure also shows that the market has been in a market correction over the last eight years and is not expected to end until early 2010 at a price level of 618.

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correction. Three-wave market corrections are composed of one wave down, one wave up, and a final wave down. Ralph Nelson Elliott labels these three waves as A, B, and C, and calls them zigzags. Elliott also observed that waves A and C of a zigzag are typically of equal length. Elliott also stated in his research that once a market correction is over, a new five-wave advance would begin. Therefore, to determine the bottom of the current bear market for NASDAQ, it is necessary to identify the three corrective waves, and once these three waves are complete, then a new bull market trend will begin.

Figure 1 shows the monthly bar chart of NASDAQ. This chart shows that NASDAQ has been in a major bull market upward trend since before 1980. Such long upward trends are known as secular trends and last approximately 25 years. Figure 1 also shows that this secular trend of NASDAQ peaked in 2000 and has been undergoing a market correction over the last eight years. Figure 1 also shows that wave A of the ABC zigzag correction ended in 2002 and wave B in 2007. Wave C of this ABC market correction has now been under way since late 2007. Note that NASDAQ has now broken down below its upward-sloping trendline, confirming that wave C down is now in progress.

Figure 2 is also a monthly bar chart of NASDAQ but shows only the last 16 years. This chart shows the price of NASDAQ at the secular market top, the end of wave a, and the end of wave b. I have also drawn a downward-sloping dotted blue line at the same slope as wave a and the same length. Wave a started in early 2000 and ended in late 2002 and took approximately two and a half years to complete. Given that wave c started in late 2007 and should take approximately two and a half years to complete, wave c should be complete sometime in early 2010. To calculate the expected price of NASDAQ, once wave c down is complete, we take the ratio of 5132.52, divide by 1108.49, and divide this ratio into 2861.51 to arrive at the quotient of 618.

FIGURE 2: NASDAQ, MONTHLY. This figure also shows the monthly bar chart of NASDAQ showing the Elliott wave count. This figure shows that the market is undergoing an ABC zigzag market correction, with wave C now unfolding. Note the time and price target for the completion of wave C and the end of the bear market trend.

We can use the Elliott wave theory tenets to forecast the end of the bear market for NASDAQ. Having identified the length and time of wave a and the end of wave b, it is possible to forecast the time and price for the completion of wave c the end of the bear market for NASDAQ. This analysis shows that we can expect the bear market for NASDAQ to be complete in early 2010 at a price level of 618. Once wave c becomes more fully developed, it will be possible to again use the Elliott wave theory to more accurately determine the end of the bear market for NASDAQ. ■

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CHART ANALYSIS

A Record Rise

by Ron Walker

The DJIA marked the week of October 10 as the worst in its 112-year history. Friday, October 10, also marked its largest swing in history with 1,019 points. In contrast, the DJIA has now started this week by breaking a record to the upside. On October 13, 2008, it put in a record one-day rise, gaining 935.42 points.

Tradable: $INDU, $SPX

Another record breaking day occurred on the DJIA as it put in a record one-day gain, rising 936.42 points or 11.08%, the largest percentage gain for the DJIA since 1933. Meanwhile, the Standard & Poor's 500 gained 104.13 points or 11.58%, posting its largest percent gain in 69 years. The market responded positively when the UK government threw a $64 billion lifeline to three UK banks, with expectations that the US would do the same for its own. After ending eight consecutive down days on the DJIA and the S&P 500, the stock market could now be poised for a short-term rally. The rally comes just as stocks are down for the count after last week's knockout punch. The market is now showing signs that it is waking up out of the stupor that laid it flat on its back as morning star candlestick reversal patterns materialized in this market meltdown. Both averages have formed three-day candlestick reversal patterns. The DJIA got a long black day (red candlestick) last Thursday October 9, followed by a spinning top on Friday. The spinning top formed as the price gapped lower and then produced wild swings throughout the session, which can be observed by the long shadows above and below the spinning top candlestick. A spinning top is similar to a doji in that it represents indecision among investors. The third day of the pattern completed as a huge rally opened the trading session on Monday, October 13.

The S&P 500 had previously formed a two-day reversal pattern last Friday on October 10 called a doji star. A bullish doji star is the first two candlesticks that make up

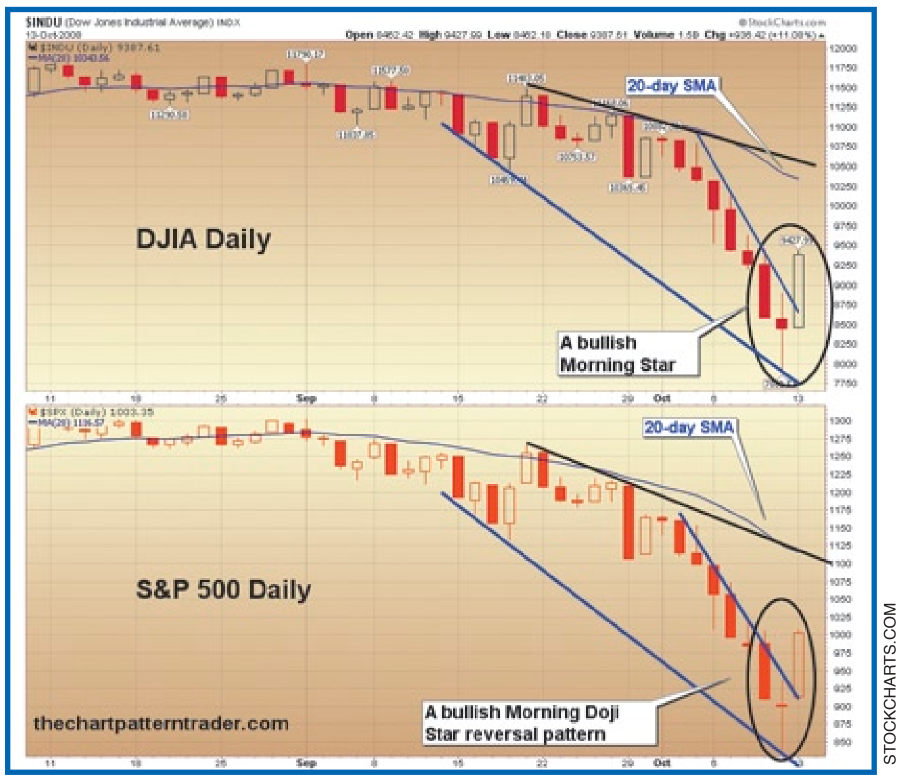

FIGURE 1: DJIA AND S&P 500, DAILY. Both averages have formed three-day candlestick reversals, allowing them to break out of their bullish falling wedge patterns. The upper boundary of the falling wedges are decelerated trendlines. Prices may rise back up to previous original trendlines (black lines) that could be forming a larger pattern known as a descending broadening wedge.

a morning doji star reversal pattern. On the third day, the S&P 500 gapped higher at the opening bell and rallied deep into the candlestick of the first day, with the two-day pattern evolving into a three-day morning doji star. The pattern is confirmed once prices close above the highest point of the

FIGURE 2: DJIA, HOURLY. The bullish falling wedge manifested due to a selloff after a bearish descending triangle broke down. Note the ADX has turned down as the positive and negative DI lines got a bullish cross.

FIGURE 3: S&P 500, HOURLY. Both MACDs on the DJIA and the S&P 500 are rising toward the zero line. If they break above it, we may see the original downward trendline on the daily chart tested. Here, the S&P 5009 and the DJIA have carved out similar price patterns.

three-day pattern. The difference between a morning star pattern and a morning doji star pattern is that the second day of the pattern is a doji. A doji forms when prices have a wide range swing, and essentially, the close and the open are the same. Shadows form when prices fluctuate, moving higher and then lower, or vice versa. A doji looks similar to a cross.

As the averages were putting in these morning star reversal patterns, they also managed to break out of their decelerating downtrends. A decelerated trendline forms when prices fall too quickly and the downward momentum becomes unsustainable. Often, when a decelerating trendline breaks, prices rally back up like a magnet to the 20-day simple moving average (SMA). In a downtrend, the 20-day SMA serves as resistance and prices usually find it a tough hurdle to rise above. The decelerating trendlines are visible on both the daily charts and the 60-minute charts. It is noteworthy that the DJIA formed a bullish falling wedge on the hourly chart and that the decelerated trendline served as the upper boundary to that falling wedge. The falling wedge formed as a result of the bearish descending triangle that emerged in early October 2008.

But what is really fascinating about the price patterns on the DJIA and S&P 500 60-minute charts is that both patterns on the charts (the descending triangle and the falling wedge) make a much larger pattern called a descending broadening wedge. A descending broadening wedge is usually classified as a reversal pattern or a continuation pattern, according to The Encyclopedia Of Chart Patterns by Thomas Bulkowski. If prices rally back up to the upper boundary of the descending broadening wedge pattern, we could see a move that will begin a rally back to the 10,250-10,300 area on the DJIA, and 1075-1100 on the S&P 500.

Some other bullish signs have appeared on the DJIA and S&P 500 60-minute charts, such as the relative strength index (RSI) breaking its downtrend simultaneously with the price charts. The average directional movement indicator (ADX) saw the ADX line (black line) peak and then turn south, while the direction movement indicator (DMI) began converging and getting a bullish cross by the end of the session. When the ADX line peaks and turns lower, it signals that volatility is on the decline and prices will likely rise off oversold levels. Key resistance is at the lower boundary of the descending triangle near the 10,250-10,300 area. It is again noteworthy that the downward trendline of the descending broadening wedge and the lower boundary of the descending triangle intersect near the 10,300 area forming a double dose of resistance. The moving average convergence/divergence (MACD) also got a bullish cross and could see a move above the zero line. However, any rally could be met with more selling pressures once resistance is reached. With the recent wild swings in the market, swing trading is a viable alternative to long-term position trading. ■

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GAPS

QQQQ Hits Gap Resistance

by Arthur Hill

With a failure at gap resistance and bearish momentum, QQQQ remains in a downtrend on the daily chart, and follow-through is needed to complete a reversal.

Tradable: QQQQ

Figure 1 shows QQQQ with a huge decline over the last two months. The exchange traded fund (ETF) clearly became oversold in mid-October and surged with a big advance on October 13. With some carryover the next day, the ETF gapped up and opened in the gap zone. This zone proved to be resistance as QQQQ moved lower the rest of the day and closed with a long black candlestick. Resistance was affirmed and a break above 36.5 is needed to provide follow-through to the big advance.

The indicator window shows some troubling volume patterns. QQQQ declined on high volume for six days (red bars) and then surged on lower volume (black bar). The October 13th surge occurred on the lowest volume over the last eight days. In addition, volume expanded on the October 14th decline, and this is not bullish at all. Volume on up days should exceed volume on down days.

Figure 2 shows QQQQ with 15-day relative strength index (RSI). This momentum oscillator became oversold in early September and QQQQ continued lower into mid-October. The oversold just became even more oversold. This is what happens in a strong downtrend. The RSI broke above the red trendline with Monday's surge but remains below 50, the midpoint for the oscillator. Look for follow-through above 50 to turn momentum bullish. Note that RSI broke its red trendline in early July but did not break above 50 until the end of the month. It may take a while for a momentum breakout. ■

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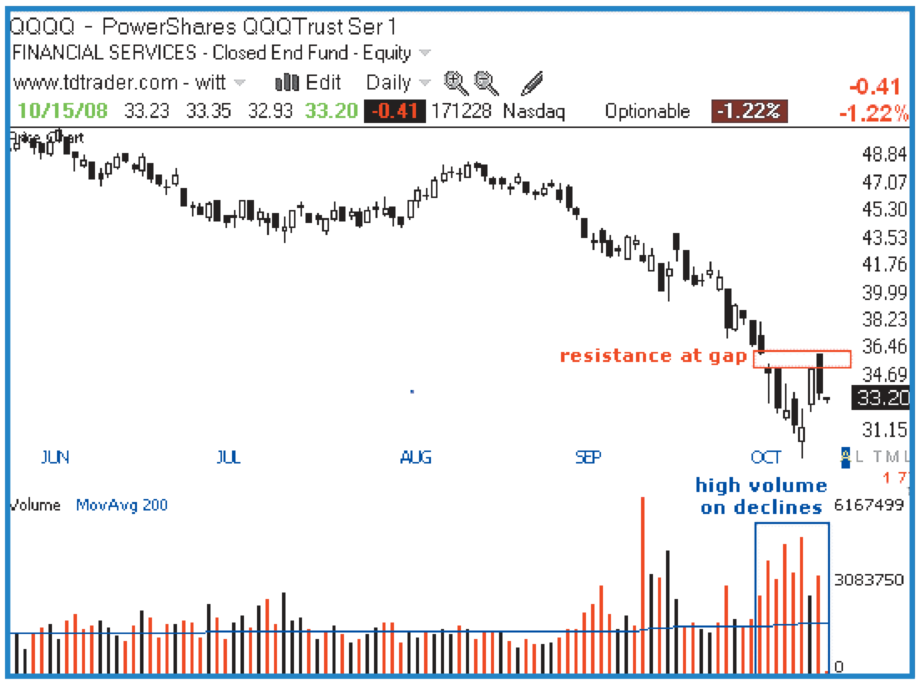

FIGURE 1: QQQQ, DAILY. Note the huge decline over the last two months. The ETF became oversold in mid-October and surged with a big advance on October 13.

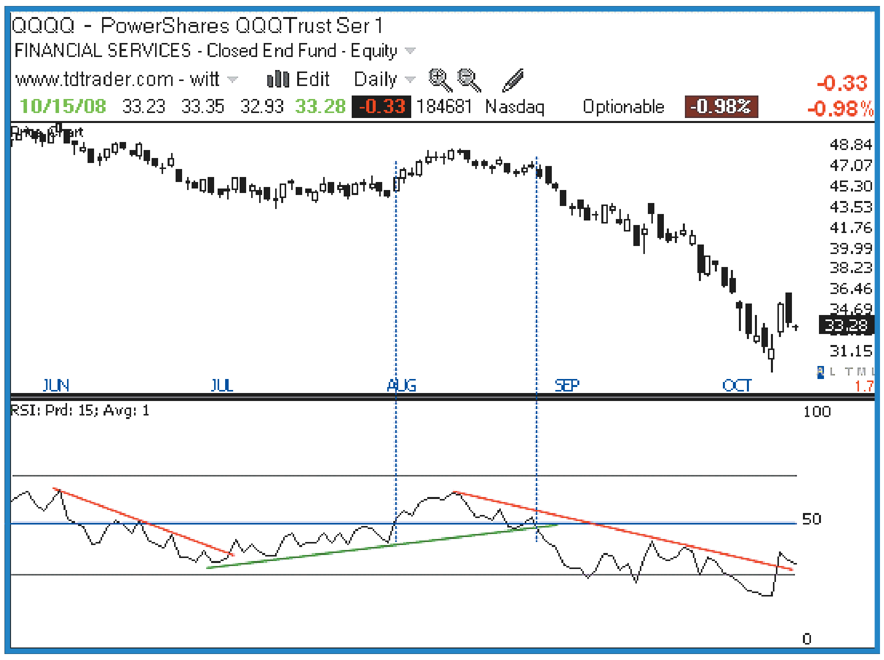

FIGURE 2: QQQQ, DAILY. QQQQ is shown here with 15-day RSI. This momentum oscillator became oversold in early September and QQQQ continued lower into mid-October.

ELLIOTT WAVE

October 2008 Or October 2009?

by Koos van der Merwe

It could be either, but when does Warren Buffett start buying?

Tradable: SPX

The world economy is collapsing around us, with the United States leading the way. The last two weeks have been the most volatile in stock market history, with plummets in the indexes breaking all previous records. The worst financial crisis since the Great Depression is redrawing the boundaries between government and the markets. The stock market crash of October 1929 took over three years for the US government to launch a series of dramatic efforts to end the Depression, starting with Franklin Roosevelt's declaration of a four-day bank holiday in March 1933.

The Depression wreaked enormous damage across the globe, and in Europe led to the rise of Adolf Hitler as he won Germany by taking the country out of its economic misery and leading them into World War II — even more misery.

The landscape of US finance has been radically changed. In little more than three weeks, the American government expanded gross liabilities by more than $1 trillion — almost twice as much as the cost so far of the Iraq war. In Europe we have seen five European banks fail, with European governments falling over themselves to prop up their banking systems. What will the long-term effect of this mess on the global economy be? Another Hitler? And then there is Asia, but that is another story.

Figure 1 is a monthly chart of the Standard & Poor's 500. Will this chart tell us when or where the end is in sight? Remarkably enough, yes — but for the US to be followed by Europe and a very changed world — that is political, not economic.

As you can see, the relative strength index (RSI) is oversold, and from looking at previous oversold positions, in bear markets (past tense), markets reacted in an up move, then a retest of the low before a new bull market started. Note too the date, October 2002. So what is it with

Figure 1 is a monthly chart of the Standard & Poor's 500. Will this chart tell us when or where the end is in sight?

October, and is it going to repeat itself? The chart says decisively yes. Unfortunately, Elliott wave theory teaches us that C-waves fall in a five-wave pattern. On the chart I have shown where I expect the correction upward to end, 1146, because this level has acted as a strong resistance/support level in the past. The fall into wave 5 of wave C is a retest of the low of October 2002 at 814.41. Whether this will actually occur is debatable, but without any doubt, an up move and down move correction after the up move is on the cards, and the timing is October.

So, yes, the market will correct upward, in October. Whether October 2008 or October 2009 is the start of a new bull market, that is the question. ■

FIGURE 1: S&P 500, GANN CHART

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NASDAQ Short-Term Support

by Alan R. Northam

Recent commentary of market analysts has them looking at NASDAQ support as a possible market bottom. However, this is only a short-term area of support with much further to go on the downside.

Tradable: $COMPQ

Figure 1 shows the monthly bar chart of the NASDAQ. This is the same chart I showed in my October 10th article titled "Looking For The NASDAQ Bottom" (see page 40 of this issue). This chart shows that the NASDAQ made a major bull market top in 2000 and has been undergoing an ABC zigzag market correction since. I encourage you to review this article for details on how I arrived at a bear market bottom for the NASDAQ at 618 in early 2010. I show Figure 1 here to give a sense of perspective as to where the market is in relation to its expected bear market bottom. The final bar on the chart is the monthly bar for October 2008, and although the month is only half over the monthly range, this bar is already showing that the market selloff is accelerating.

FIGURE 1: NASDAQ, MONTHLY. This chart shows the Elliott wave count and a price target of 618 in early 2010 as the completion of the bear market.

FIGURE 2: NASDAQ, DAILY. This chart shows the detail of the final wave C to date for the completion of the bear market. This chart shows that the NASDAQ has much further to go before the bear market of the NASDAQ is complete.

Figure 2 is that daily price bar chart for the NASDAQ and shows more detail about where the market is in trek toward its final expected bear market low of 618. This chart shows the top of wave b in October of last year and shows the progress made in the final wave c down. To date, the NASDAQ has completed corrective wave 2 of wave (3) down and is currently in wave 3 of (3) down. Wave 3 down is unfolding in five subwaves, subwave i circle, ii circle, iii circle, iv circle, and wave v circle following the Elliott wave labeling convention.

With the completion of wave iii circle, the NASDAQ has found some short-term support. There are those market analysts who are now looking at this bottom as a possible bottom to the complete selloff from last October. I heard this weekend one of the market analysts, on a local radio station, saying that this could very well be the bottom of the market. However, in my opinion the bear market still has much further to go (see my previous article). With wave iii circle complete, the market entered into corrective wave iv circle that could also be complete. A move below the low of wave iii circle will confirm that corrective wave iv circle is complete and that wave v circle is under way.

Figure 2 also shows two target prices that have been met. The first target that has been met is wave 3 at 1705 and the second is wave iii circle at 1666.41. However, these two target prices are out of order. Wave iii circle should have been completed first and then wave 3, but the order shown are the results of my calculations. This then leads me to suspect that the market is going to move lower to a possible price target for wave 3 that is lower than that of wave iii circle. I have recalculated the price target for wave 3 to be 1467.42, the next lower price target, according to the Elliott wave theory. In addition, with wave iv circle complete, I also calculated the target price for wave v circle to be 1495. According to the Elliott wave theory, once wave v circle is complete, that will also complete wave 3. Looking at the calculated price target for wave v circle and the recalculated price target for wave 3, note how close these two price targets are. This is called a price cluster, and price clusters have a higher probability of occurring that single price calculations. Therefore, there is a high probability that wave v circle will be complete somewhere in the range of 1495 and 1467 that will also complete wave 3 down.

Looking at Figure 2 a little closer, note that the market has now completed wave iv circle, of wave 3, of wave (3). Once wave v circle is complete, then that will also complete wave 3. The market will then undergo a wave 4 correction, followed by wave 5 in the downward direction. Once wave 5 is complete, then wave (3) will be complete as well. Note that I have shown the price target for the completion of wave (3) to be 1409. This forecast was first made on August 8 in my article titled "NASDAQ Double Bottom?" Further, note that the low of wave iii circle is not that far away from the wave (3) target. Therefore, the price target for wave (3) calculated in August still looks like a logical price target for the completion of wave (3).

In conclusion, the recent bottom by the NASDAQ is only a temporary bottom and not the bottom of the market. My analysis shows that the bottom of the bear market in the NASDAQ will not occur until the market has fallen to around 618 in early 2010. ■

SUGGESTED READING

Northam, Allan [2008]. "Looking For The NASDAQ Bottom," Traders.com Advantage, October 10.

______ [2008]. "NASDAQ Double Bottom," Traders.com Advantage, August 8.

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DESCENDING TRIANGLES

A Descending Triangle For QQQQ

by Arthur Hill

QQQQ formed a descending triangle over the last few days, and a support break would signal a continuation of the bigger downtrend.

Tradable: QQQQ

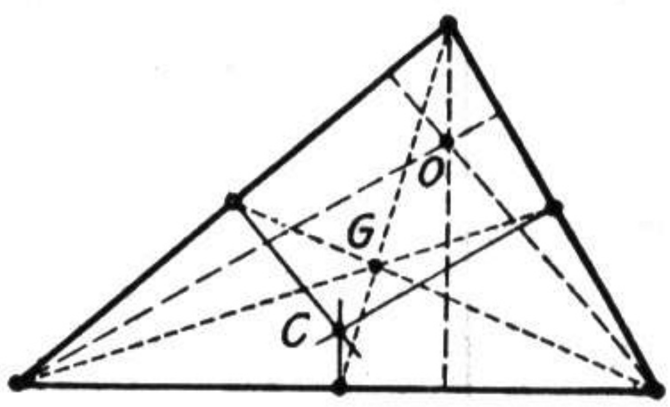
Figure 1 shows the NASDAQ 100 ETF (QQQQ) with a descending triangle on the 60-minute charts. This time frame expands on the last 10 trading days to show the pattern quite well. There are three relatively equal lows around 29.5 and a lower high around 33.5. This lower high shows selling pressure appearing well below the prior high. Sellers came in earlier than the prior high at 36, and this is bearish. The relatively equal lows show the last bastion of demand (support).

A break below support would confirm the pattern and project further weakness. QQQQ was on the verge of breaking support on Thursday, but bounced back with a late afternoon recovery. Another breach would project further weakness toward 23–25. The height of the pattern is subtracted from the support break for the downside projection (36 - 29.5 = 6.5, 29.5 - 6.5 = 23).

Figure 2 shows daily candlesticks with the descending triangle and a falling price channel. The red line shows the descending triangle target around 23. For the channel, I drew the upper trendline first and then the lower trendline was drawn parallel. It extends to around 25–26 early next week, and this area could also act as support. Considering the channel extension and descending triangle target, I would mark the next support zone around 23–25. ■

FIGURE 1: QQQQ, HOURLY. Note the descending triangle.

FIGURE 2: QQQQ, DAILY. Note the daily candlesticks with the descending triangle and a falling price channel.



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S&P 500 Triangle?

by Alan R. Northam

The S&P 500 looks like it's tracing out a symmetrical triangle wave formation, but this may not be a valid wave form. Here's why.

Tradable: $SPX

Figure 1 shows the daily price bars of the Standard & Poor's 500 over the last 18 months. This chart shows that the S&P 500 made a major bull market top on October 11, 2007. Since that time, this large-cap index has been trading lower and has completed waves (1) and (2) of a five-wave formation, according to Elliott wave theory.

With waves (1) and (2) complete, wave (3) down is now in progress to be followed by a corrective wave (4) and a final wave (5) down. Further, wave (3) down is unfolding in five subwaves: waves 1, 2, 3, 4, and 5 with waves 1, 2, and 3 complete. This is known as the fractal nature of the wave theory.

Following the completion of wave 3, it looks as if the S&P 500 is forming a symmetrical triangle. According to Elliott wave theory, symmetrical triangles often form in wave 4. Therefore, if this pattern is a symmetrical triangle, then wave 4 is still in progress, with wave 5 to the downside to follow once the symmetrical triangle has been completed.

To view this developing symmetrical triangle pattern in more detail, it is necessary to go to a smaller time frame. I have chosen the 60-minute time frame for this analysis.

Figure 2 is that of the 60-minute price bar chart of the S&P 500. Here, I have shown the wave pattern that has developed since the completion of wave 3 as a symmetrical triangle. Symmetrical triangles are composed of five overlapping waves and are labeled according to Elliott wave theory convention as waves a, b, c, d, and e. Note that wave d has just been completed and wave e is just getting under way. Once wave e is complete, then that will also complete wave 4 and will initiate the beginning of wave 5 down that will lead to lower prices.

Two things are wrong with this symmetrical triangle, however, that invalidates it as a true symmetrical triangle. First of all, the completion of wave d has fallen below the low of wave b. Both R.N. Elliott, who developed the wave theory, and Thomas N. Bulkowski, who wrote *Encyclopedia Of Chart Patterns*, define a symmetrical triangle as a wave form that produces lower highs and higher lows. Therefore, when wave d fell below wave b, the symmetrical triangle formation became invalid.

Second, R.N. Elliott defines a symmetrical triangle as five waves with each wave composed of three subwaves. When we look at wave d, five subwaves are clearly visible. This also invalidates the formation as a true symmetrical triangle. As a result, I relegate this formation to alternate technical analysis status.

Figure 3 shows my preferred technical analysis of the wave pattern that has developed since the completion of wave 3. I believe corrective wave 4 is already complete and wave 5 down is under way. According to this analysis, wave 5 is subdividing into five subwaves with subwaves (i) and (ii) now complete. This analysis also shows that subwave (iii) down is now under way to be followed by a wave (iv) market correction and a final wave (v) to new lower lows. Once subwave (v) is complete, then that will also complete wave 5 down. Further, once wave 5 is complete, then that will also complete wave (3) down to be followed by waves (4) and (5) (see Figure 1).

In conclusion, the analysis shows that what looks like a symmetrical triangle may not be one at all. One way we will be able to tell is to watch the direction of the S&P 500 over the next day or two. If the market moves higher, then the pattern is most likely a symmetrical triangle, but if the market continues to move lower, then that will invalidate the formation as a symmetrical triangle. However, this is all academic, as both analyses lead to lower stock prices in the days ahead. ■

FIGURE 1: S&P 500, DAILY. This figure shows the Elliott wave count. The wave count shows that the index is currently in wave (3) down and is subdividing into five smaller waves.

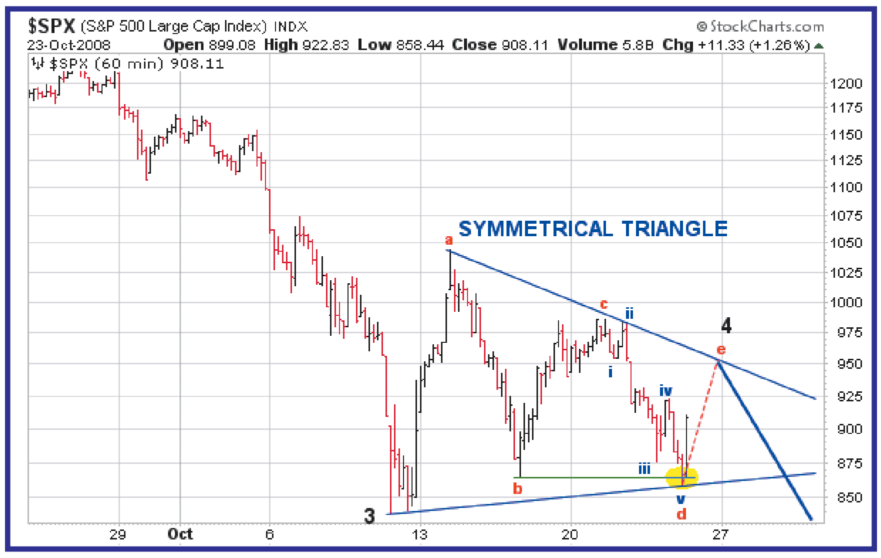

FIGURE 2: S&P 500, 60-MINUTE. Once wave (3) is completed, it will complete wave 4 and will initiate the beginning of wave 5 down.

FIGURE 3: S&P 500, HOURLY. This figure shows the developing wave pattern after the completion of subwave 3 as the completion of subwave 4 with subwave 5 under way. Subwave 5 is also subdividing into five smaller waves. This is the preferred analysis as it does not violate any rules as does the symmetrical triangle analysis.

According to Elliott wave theory, symmetrical triangles often form in wave 4.

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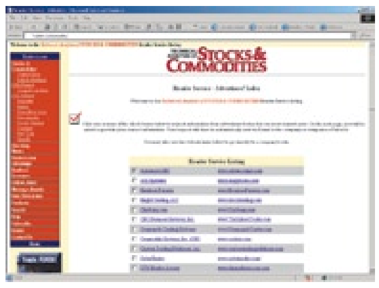

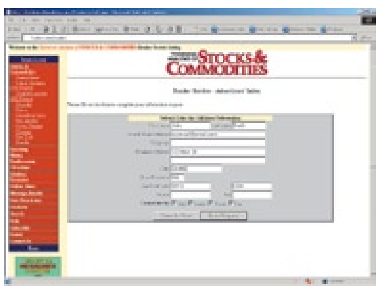

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■

TRADERS' GLOSSARY

DICTIONARY ■

Average Directional Movement Index (ADX) — Indicator developed by J. Welles Wilder to measure market trend intensity.

Breakout — The point when the market price moves out of the trend channel.

Convergence — When futures prices and spot prices come together at the futures expiration.

Cubes (QQQQ) — Traded on the NASDAQ, cubes are ETFs that track the NASDAQ 100 index, which is made up of the 100 largest, most active NASDAQ nonfinancial stocks.

Divergence — When two or more averages or indices fail to show confirming trends.

Directional Movement Index (DMI) — Developed by J. Welles Wilder, DMI measures market trend.

Double Bottom (Top) — The price action of a security or market average where it has declined (advanced) two times to the same approximate level, indicating the existence of a support (resistance) level and a possibility that the downward (upward) trend has ended.

Engulfing Pattern — In candlestick terminology, a multiple candlestick line pattern; a major reversal signal with two opposing-color real bodies making up the pattern.

Exponential Moving Average — A variation of the moving average, the EMA places more weight on the most recent closing price.

Fade — Selling a rising price or buying a falling price. For example, a trader who faded an up opening would be short.

Flag — Sideways market price action that has a slight drift in price counter to the direction of the main trend; a consolidation phase.

Head and Shoulders — When the middle price peak of a given tradable is higher than those around it.

Lag — The number of datapoints that a filter, such as a moving average, follows or trails the input price data. Also, in trading and time series analysis, lag refers to the time difference between one value and another. Though lag specifically refers to one value being behind or later than another, generic use of the term includes values that may be before or after the reference value.

Moving Average Convergence/ Divergence (MACD) — The crossing of two exponentially smoothed moving averages that are plotted above and below a zero line. The crossover, movement through the zero line, and divergences generate buy and sell signals.

Overbought — Market prices that have risen too steeply and too fast.

Overbought/Oversold Indicator — An indicator that attempts to define when prices have moved too far and too fast in either direction and thus are vulnerable to a reaction.

Oversold — Market prices that have declined too steeply and too fast.

Pairs Trading — Taking a long position and a short position on two stocks in the same sector, creating a hedge.

Relative Strength — A comparison of the price performance of a stock to a market index such as the Standard & Poor's 500 stock index.

Resistance — A price level at which rising prices have stopped rising and either moved sideways or reversed direction; usually seen as a price chart pattern.

Retracement — A price movement in the opposite direction of the previous trend

Simple Moving Average — The arithmetic mean or average of a series of prices over a period of time. The longer the period of time studied (that is, the larger the denominator of the average), the less effect an individual data point has on the average.

Smoothing — A mathematical technique that removes excess data variability while maintaining a correct appraisal of the underlying trend.

Stochastics Oscillator — An overbought/oversold indicator that compares today's price to a preset window of high and low prices. These data are then transformed into a range between zero and 100 and then smoothed.

Support — A historical price level at which falling prices have stopped falling and either moved sideways or reversed direction; usually seen as a price chart pattern.

Trading Bands — Lines plotted in and around the price structure to form an envelope, determining whether prices are high or low on a relative basis and forewarning whether to buy or sell by using indicators to confirm price action.

Trading Range — The difference between the high and low prices traded during a period of time; in commodities, the high/low price limit established by the exchange for a specific commodity for any one day's trading.

Trend Channel — A parallel probable price range centered about the most likely price line. Historically, this term has been used to denote the area between the base trendline and the reaction trendline defined by price moves against the prevailing trend.

Trendline — A line drawn that connects either a series of highs or lows in a trend. The trendline can represent either support as in an uptrend line or resistance as in a downtrend line. Consolidations are marked by horizontal trendlines.

Underlying Security — In options, a stock subject to purchase upon exercise of the option.

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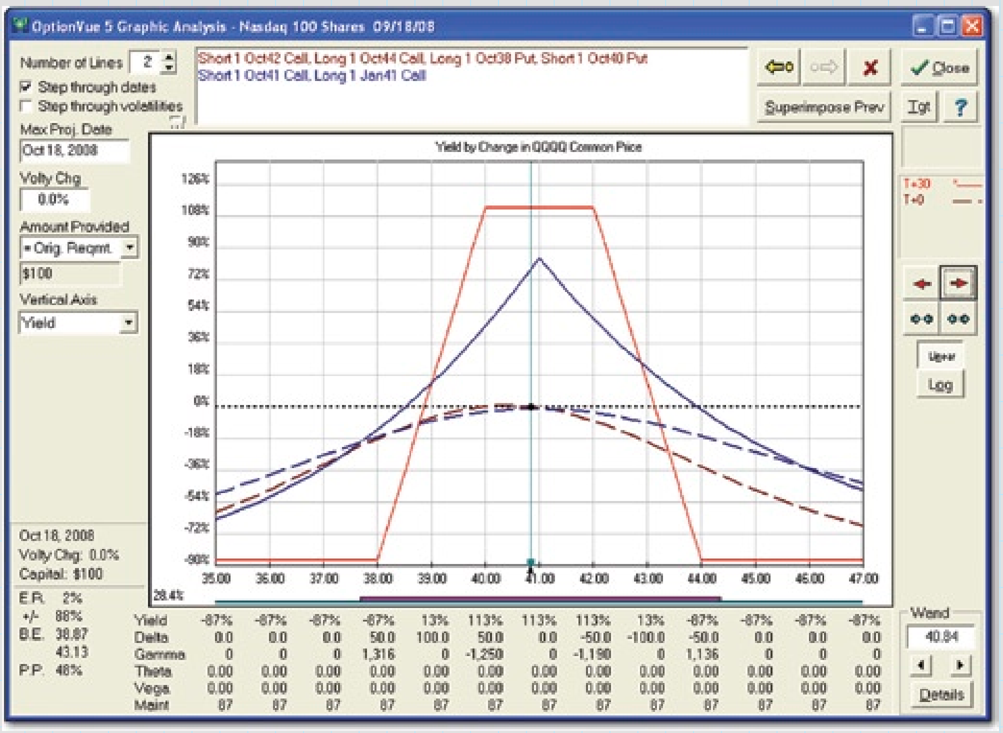

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