



## MARKET COMMENT

### EVIDENCE SUGGESTS THAT THE MARKET IS ONLY HALF-WAY THROUGH THE CURRENT UP-MOVE

July 13, 2010

The markets proved once again that when yours truly leaves the Continent, the market goes South (even when we go East!). During the last 10 days we spent a few days in London to see clients and a few days in Brussels and Bruges for some (well deserved) R&R. So, as said before, the markets obliged!

Here are some thoughts on the recent market action.

1. Was the sell-off strong enough and long enough to negate our positive long-term bullish outlook? *No*. To support this, we need only to look at the average investor who is sitting in a large cash/T-bill position, whether in Toronto, New York, London or Brussels!
2. Was the sell-off strong enough to create an absolutely powerful over-sold condition? *Yes*. My mentor of many years ago insisted that the best over-sold signal is given when the markets (as measured by the combination of the Dow, S&P and NASDAQ Indices) are down for an uninterrupted 10 days in a row. These signals come about once every 2 years or so, but when they occur, they signal an extremely over-sold condition and more often than not lead to higher market levels within a few days (\*). Such an event has just occurred, as the markets were down 10 days in a row ending on July 2nd. We are awaiting the action of the next few days.
3. The S&P 500 Index overshot the support level mentioned in our recent publications (1040), but by just a minute amount. At the same time, the S&P/TSX Index held the published 11,000 level by a similar minute amount. Should we worry about these minute amounts? They usually don't mean much.
4. The 200-day Moving Average (200dMA) flattened in both countries, when the data from 200 days ago (late September 2009) was replaced by recent data. This is worrisome, as the start of an actual downturn by this indicator would suggest trouble ahead.
5. Statistics supporting the heavily over-sold status of the markets (as supplied by Investor Intelligence) show that the stocks above their respective longer-term moving averages are at an extremely over-sold level of 11.9% (July 6th data). Also the Bullish Advisors have declined to 37% from a recent high of 56% and the Bearish ones have increased to 34.8% from a recent low of 17.5%.
6. The MACD (Moving Average Convergence/Divergence Indicator) shows a bullish positive divergence (or non-confirmation): while the markets reached a lower low (July 5th vs. May 21st), the MACD had a higher low.
7. The 50-day moving average of the S&P 500 declined below its 200-day moving average on July 1st, creating a "death cross" (this did not occur in Toronto). By now, everyone is aware of this (it is all over the media) and heralds it as an ominous event. In our experience, this signal is only valid at the end of a bull-market, not half-way through it. For example, there was a "death cross" in July, 2006 (half-way in the bull-market) when the S&P 500 stood at 1265, on its way to the all-time high of 1576. Obviously the signal was wrong. The next occurrence happened in December, 2007, when the S&P 500 was at 1484. This occurred at the end of a long up-move and the Index then declined to a low of 667 in March 2009. By the way, no one talked about it at the time!



Evidence suggests that a), the market is only half-way through the current up-move and b), when everyone agrees it is already discounted.

8. There was no Dow Theory sell signal, the Transports did not decline below their February lows, even though the Industrials did.

9. Activity to date very much resembles that of 40 years ago, when the Dow Industrials declined from November 1968 to May 1970 (18 months), rallied to April 1971 (11 months), corrected to November 1971 (7 months) and then went on to a new all-time high in January 1973 (14 months). Compare this to a decline from October 2007 to March 2009 (17 months), a rally to April 2010 (11 months) and our forecast of the next low in October 2010 (6 months), as described below (by the way, should the similarity continue, it would suggest the next top in the December 2011/January 2012 period).

(\*) This phenomenon led me to create a "Net Day Index", which is featured on the Metastock system.

### **OUTLOOK**

1. Some stocks have seriously violated support and fell below their respective 200dMAs, forcing us to close these positions. However, the majority of stocks on our BUY&SELL lists continue to show their mettle by refusing to violate their support or their 200dMA. These should be the most likely to outperform in the future and the ones to acquire at this time.

The defensive nature of the market is demonstrated by the strength in the Discretionary, Telecom, Utility and Gold Sectors in both Toronto and New York.

2. In the short-term, the S&P500 and S&P/TSX should rise to correct their recent declines. Proof of strength will come if they exceed the 1100 and 11,600 respective levels (see dates below). Failure to do this would be a very negative sign.

3. In our recent publications and presentations we forecasted a narrow trading range for July and August and a weak September/October, which should be the spring-board for a strong year-end rally (see dates below).

4. Now that the second quarter (2Q), the window dressing, the July holidays, etc. are over, we anxiously await the middle of July, when the majority of 2Q earnings will be announced. It would be more bullish if the markets idled to this date, instead of running ahead to discount any good news.

5. Important dates to look for:

- The 21-day cycle matured on July 2nd, right on time. The next dates for this cycle are July 23rd, August 13th and September 3rd.
- The current 105 day-cycle will mature on September 3rd, at the same time as the 21-day cycle, making this an important date.
- The current 39-week cycle will mature on October 15th.

***This could mean an early September high and a mid-October low.***

**Ron Meisels**