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Oversold in Hell, Overbought in Dreams

July 4, 2011

DOW

May 15, 2011
"All taken together, the US markets can roll off a cliff whenever it feels like it, and one's strategic positioning and cash management should reflect that."

May 29, 2011
"Like the Yen, the price chart and its technical indicators seemingly dried up, causing me to cover shorts this past week as well. But for how long?"

"The maximum upside potential I see is 12,800 {12,650 is near term initial stop (if not the whole short term move)},..."

"A final technical note: When indicators become so oversold, it is often sign of trend change, more than any buying opportunity: rookies beware! Simply, ALL taken together in this section, there will be an utter debacle in the stock market, as forecast earlier this year."

Following the above commentary, the Dow did indeed spike up to just under 12,600 to complete wave-2 of 3 (please see annotated Dow chart on page 4), which had already begun in the 2nd week of May and which concluded Thursday June 23.

It is evident why long term portfolio positioning must be aligned for a dramatic bear market and it is equally evident that when indicators of all stripes (please revisit the May 29 Dow section's technical indicators and related commentary) become as oversold as they did, that there has been a cyclical trend change, which jibes with prior commentary that a 1,000-point decline tends to tip off a larger decline to come (whereas 300-500-point drops tended to be false starts that were mere corrections).

The outrageously oversold indicators of all stripes have become overbought on the back of the wings of dreamland, as traders pray that Greece will be something to forget, rather than keep forever in mind as the ominous indicator that it in fact is. This past week's dramatic short covering rally was accompanied by hopes of economic recovery; the story was manipulation, and nothing more.

The Dow has already rallied 70% and has provided an entry point for short term (3-month) traders to go short using corresponding strategies. I forecast a pullback followed by a rally that consumes time more than price. Whatever happens, the pattern will have been one that fools most of the traders into not being short at all at....until it is too late.

This rally has been comprised of 3-wave patterns, while, I suspect, the 3rd and concluding leg of this countertrend rally will have been a time consuming 5-wave advance (which will NOT be the longest wave---definitely a fooler).

The just completed 2-month beating took indicators to devilishly oversold levels that no intelligent investor should forget, especially since simple technicians will have drawn the wrong conclusion regarding the broad ultra-oversold readings.

As an aside, the Dow's low of June 23rd smacked of a bottom when the 200-point smash left traders wondering as to whether to blame the release of oil and decline in oil stocks or Greece's woes. That sort of foolishness tends to mark the conclusion of technically-driven factors as the remnants of the decline's causes are flushed-out.

With many positive short term divergences, a 5th-wave failure to the downside felt intuitively right and logically correct.


INDU ↓ 12523.21 +108.87 i
Index GPO
At 11:08 Op 12412.07 Hi 12545.99 i Lo 12404.08 i Prev 12414.34
INDU INDEX
Save Chart
Hide
GPO - Bar Chart
Page 1/10
Range 01/03/11 - 07/01/11
Upper Bar Chart
Mov. Avgs 200
Currency USD
Period Daily
Lower None
Mov. Avg
Events
Last 12523.21
High on 05/02/11 12876.00
Average 12198.99
Low on 03/16/11 11555.48
SMAVG on Close(200) 11820.4258
1
2
3
4
5
13000
12000
11500
11000
Jan 14
Jan 31
Feb 14
Feb 28
Mar 15
Mar 31
Apr 15
Apr 29
May 16
May 31
Jun 15
Jun 30
2011
Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2011 Bloomberg Finance L.P.
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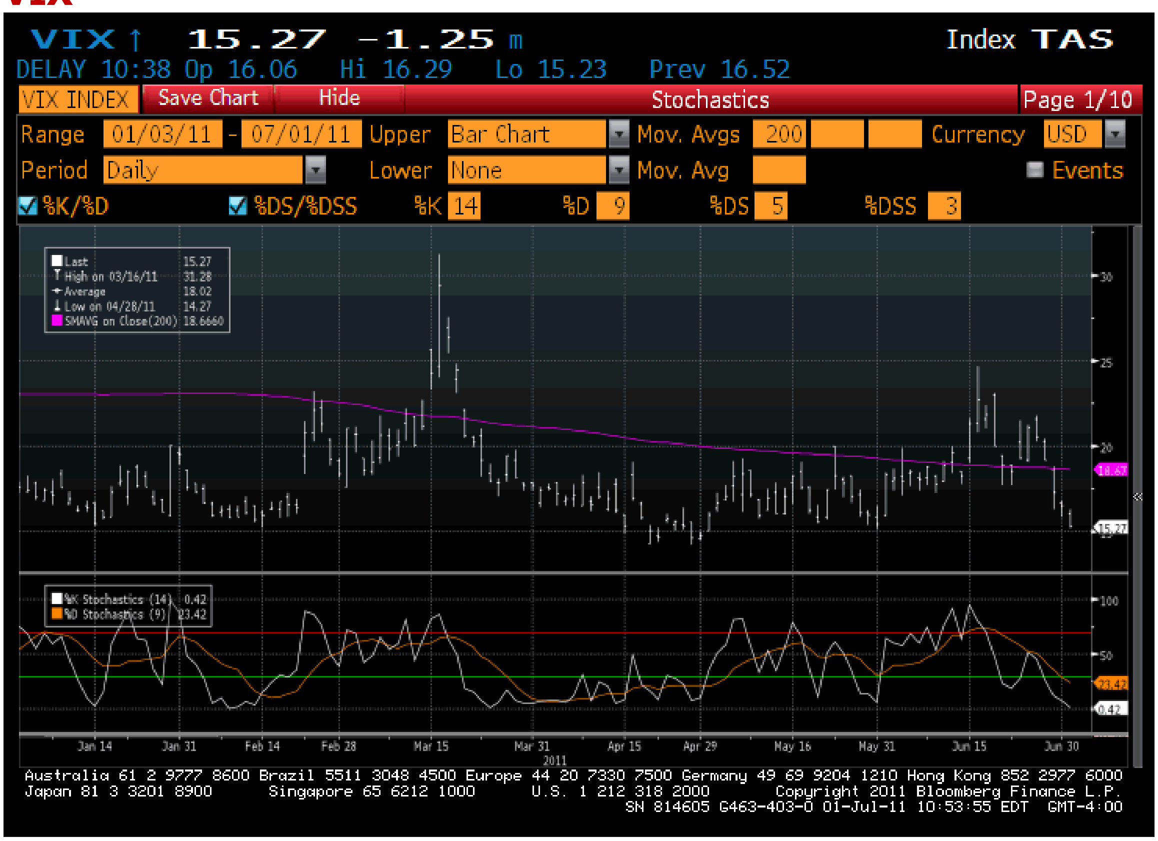
VIX


VIX ↑ 15.27 -1.25 m
Index TAS
DELAY 10:38 Op 16.06 Hi 16.29 Lo 15.23 Prev 16.52
VIX INDEX
Save Chart
Hide
Stochastics
Page 1/10
Range 01/03/11 - 07/01/11
Upper Bar Chart
Mov. Avgs 200
Currency USD
Period Daily
Lower None
Mov. Avg
Events
%K/%D
%DS/%DSS
%K 14
%D 9
%DS 5
%DSS 3
Last 15.27
High on 03/16/11 31.28
Average 18.02
Low on 04/28/11 14.27
SMAVG on Close(200) 18.6660
30
25
20
%K Stochastics (14) 0.42
%D Stochastics (9) 23.42
100
50
Jan 14
Jan 31
Feb 14
Feb 28
Mar 15
Mar 31
Apr 15
Apr 29
May 16
May 31
Jun 15
Jun 30
2011
Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2011 Bloomberg Finance L.P.
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The **6-month daily VIX** chart on the preceding page illustrates last week's smash to its neckline support at 15, where it also formed a right shoulder to the chart's head of this April's 2nd half.

ASSET ALLOCATION

The breakdown remains:

50% gold
25% Swiss Franc
25% US Dollar

Sid Klein