



# SG Capital Research

Global Market Insights

## **Research Note – Weekly Market Strategy Global (A # 1)**

**MAEG- WKLY MKTSTR- GL- POM -SG 2011 # JAN 31**

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## **Market Strategy Global (A # 1) - SPX – Closed @ 1276 – Wkly change ( - 8 points)**

Analysis of Broad Market that includes – **Jan 1<sup>st</sup> 2011 – SPX 1257 ( up 1.5%)**

- **Primary Market** SPX ( or SPY) & DOW ( DIA) as main market driver and
- **Secondary Markets** NYSE, NASD ( or QQQQ), RUSS ( or IWM) .

We have picked up charts (below) that has some distinct characteristics and values from last weeks observation at Inflection points based on our assessment:

- **Detail Coverage**

- Daily Trend Adjusted Strategy - 3x3 / 9EMA – **DOW, SPX**
- Primary Market Analysis – **SPX, MID, ST , LT**
- Secondary Market Analysis for SPX clues – **NASD, RUSS,**
- Sector Analysis for SPX clues – **IYT, BKX, SMH**
- Time / Cycle Analysis- **Bradley Cycle, 4 yr Cycle,**
- Advance / Decline Internal market behavior – **A/D – SPX**
- Sentiment Analysis with Extreme character – **TICK , VIX**
- Global Market Analysis for SPX clues – **CHINA, AUST, FTSE, EEM,**
- Appendix - History of past SPX –POM Signals & Key Criteria

- **Objective**

*Focus is on the Short & Intermediate term turning point of the SPX via POM's Price projections. POM is Unidirectional Judgmental Model, It utilizes multiple input signal via the Global Inter market Analysis (GIC), Price & Quality Volume (PQV), Pattern Recognition ( PEC) , Cycles, Internal & External price equilibrium points to assists in output signals . POM is supplementary Analytics to add value to RA/ RI Framework for Risk Management.*

- **Trading & Investment Conclusions**

**Our start point 2011 in SPX @ 1257 – Current Indicators**

- **Long Side –**

- POM 12 Calls – **None** so far this year.
- Trend Adjusted Signal – Sold at SPX 1276 from Jan 1<sup>st</sup> 1257.

- **Hedge Longs / Risk Management for Downside Corrections -**

- We recommend fully Hedge on long positions via the SETUP – PQV Hedge Index, we have a **Drawdown – 2.0%** with Setup 2's & PQV – CZ Validated Equities ,
- Model Avoided Setup's 4's completely hence minimizing drawdown and maximizing mental capital ( either due the CZ – PQV – NON- validation or the underlined Index did not confirm to POM 15 sub criteria's of its own )

- **Net Short –**

- POM 15 Calls – **None** so far Triggered this year ( 8 of 20 Sectors have reached CZ / PQV & 6 More Sectors pending tests)
- Our Target has remained for SPX 1280 ( Monthly close for highs) , Pre – Lehman Crash Area tests

## • SPX – POM Signals & Price Projections with Setup Index ( update)

- UPSIDE Target - ( **Monthly close below 1280 should be a good signal** ). POM 15 for Net Short has not Triggered. Although this extension is counting time the best case scenario would be the highs of Pre – Lehman crash price tops 1280 on Monthly . We could very well trigger POM 15. Meanwhile we continue to remain POM 14 since Jan 1<sup>st</sup> 1257 ( Our new reference point for 2011).
- DOWNSIDE Target - SHORT TERM - SPX 1220 first then , Daily Bearish Wedge has the downside target of 1175. On Intermediate term Our Pull back from here should be to 1130 - 1145 ( This area is false break top side driven by QE 2). The natural equilibrium price is at 1125, which also happens to be the GOLDER CROSS ( SETUP 1) @ 1120. Volatility will increase in this area. Its too early to tell if something more serious ( let us wait and watch )
- EQUILIBRIUM Price - favorable Risk / Reward opportunity will come at POM 13/ 12. This area we would be interested again
- Our TREND ADJUSTED SIGNAL closed below our price points of Reversal 1276 up 1.5%, since the 1<sup>st</sup> of Jan 1257 ( our new reference point for 2011 ), Our Reverse Buy would be Trigger close above 1299

## • Daily SPX - “ Trend Adjusted Signal” – Stopped out close under 1285

### 3x3 /9EMA – Momentum Break Indicator –

- For Bull case - Previous long exit was on 11/17 at 1193 from 1105 entry 09/05 for 8%
- For Bear case - SS from last Sell Signal at 1193 to 1225 = - 2.6%
- For Bull case – Current long position from 1228 to 1276 = 4.0 % & from reference point 2011@ 1257 = 1.5%

Currently “ Trend Adjusted Signal “ is Flat on Long side but would **Trigger BUY Signal - close above 1299**

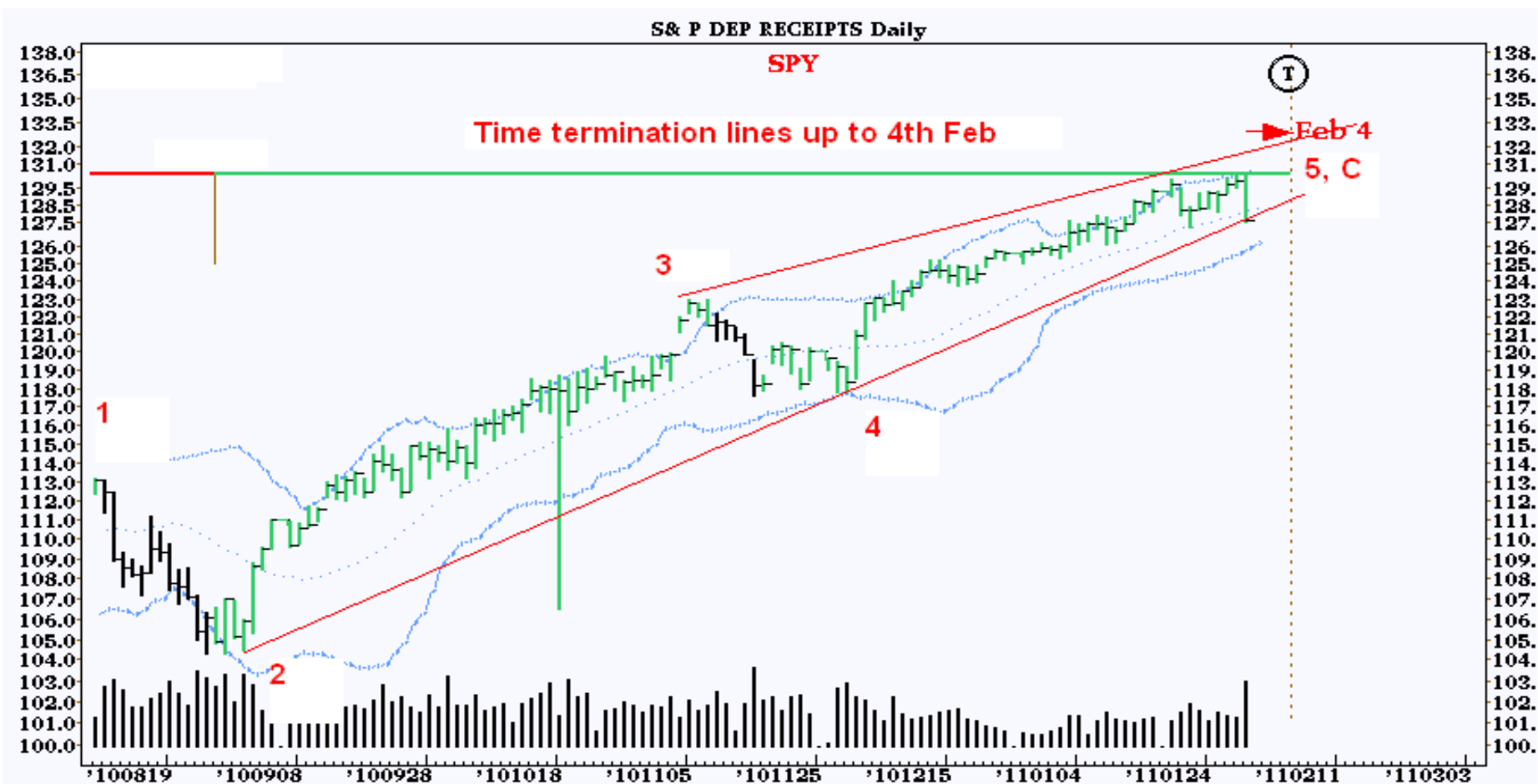
## • Market Insights

- *As pointed out last week & in Sector Analysis, the CZ – PQV in Russell, Transport, Materials, NASD, XRT and SMH proved its merit and fractured on the spot twice while the Blue chips and SPX which were showing life and finally snapped. Internationally it has similar price validation same several weeks ago, failed CZ – PQV tests for EEM, EWA, EWH as indicated in Sector Analysis.*
- *On SPX Price Performance side we had another quick 25 point drop expected into 1270, after touching the Wave 5 and C. as indicated in Chart last week Call it minor Jan correction . The indicators call for another bounce, move higher going into early February in Majors . But, that may be the final rally move off the March, 2009 lows before a resumption of the major trend to the downside.*
- *We are still looking for POM 15 on SPX for Net Short position, it comes in after the first break and failing rally. Till we get a that scenarios, We would work with CZ on all the weaker broken down sectors of topping while awaiting for any Exhaustion in SPX to Trigger POM 15.*
- *Seasonality for January month end is usually very Bullish, however our Short term Cycle work turns Bearish ( See the chart below)*
- *On Monthly January did not prove negative as in past years however as February begins, since 2007 -2010 SPX has negative returns of (-3.45) % and 2003 – 2006 has (+0.36) % ( See the chart below)*
- *In the next bounce in SPX, few of the Broken down sectors should lag the market, Transports ( IYT – see chart below) tends to Lead / Lag market in Both Directions. China's danger to the world market with Emerging markets Interest Rate rise and Rampant Inflation. ( See charts of CHINA, EEM below)*

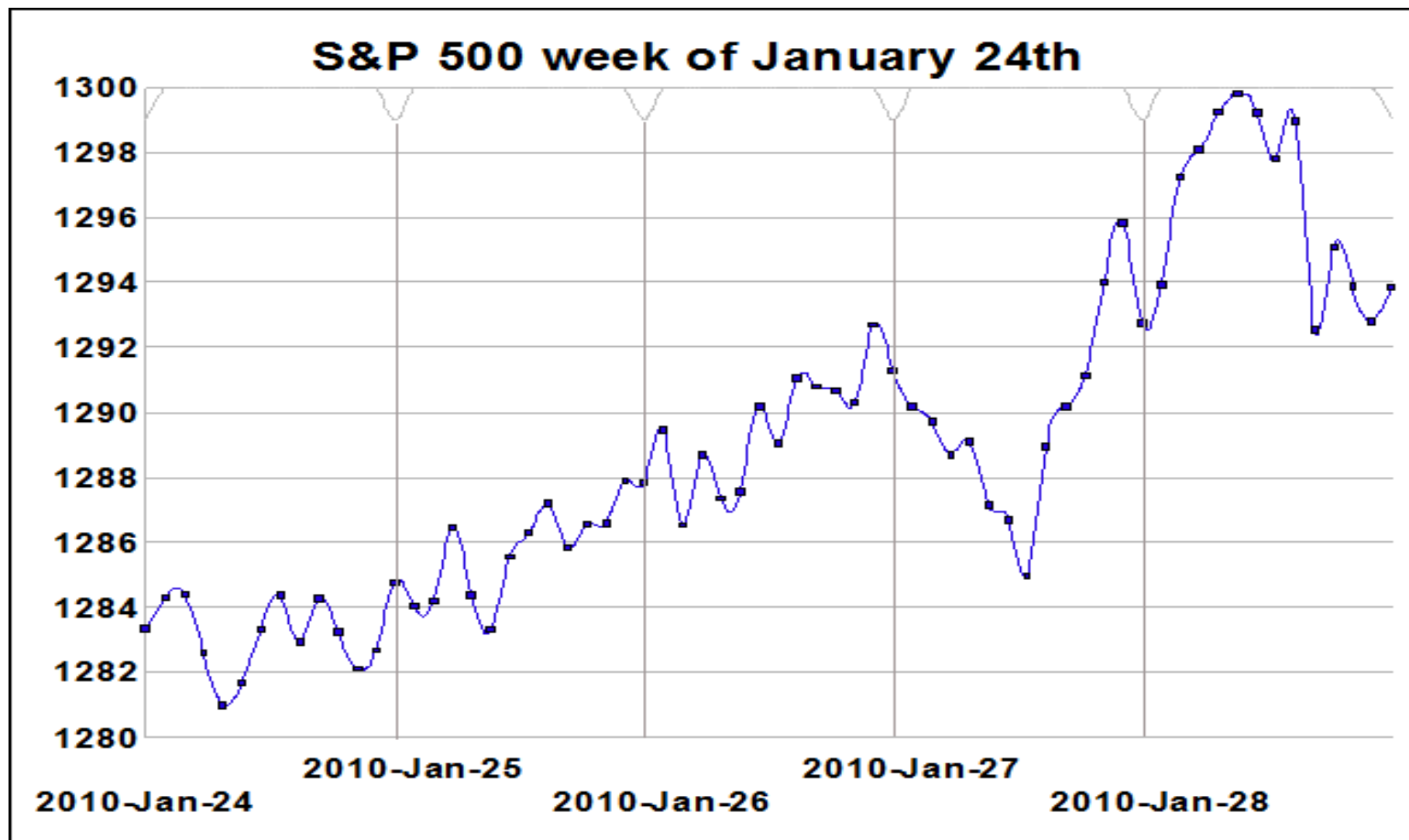
## Primary Market Analysis -

### SPX – ST

According to the count shown on Momentum measurements, wave 5 rally / wave C was finished and for big move downside. We think market may give another run up before the larger correction sets in . There is Time termination T on 4<sup>th</sup> February. Intermediate the early March, 2-year anniversary of the 2009 low some times those historical turn dates gets to be meaningful ( This can very well be lower highs or Secondary if not the top).



**THIS WEEK ON CYCLES – Turns Bearish**



## SPX – TRIN - SHORT TERM

*We did go to +300 tick that coincided with 5<sup>th</sup> wave & C wave and market snapped back. The little room that was left from 270 to 300 was achieved for the decline. Key Short term condition is complied.*



## SPX – TRIN - MID TERM –

*Intermediate term view of SPY dating back to mid 1998 with the 100 day moving average of the TRIN in the upper window. At previous intermediate term tops the 100 MA of the TRIN produced a divergence where the SPY marked a higher highs and the 100 MA TRIN will made a higher low. SPY Pull back and now in the next rally we should produce the negative divergence like the previous occasions. This condition to be complied soon.*

*Earlier 2 weeks prior we complied with the 160 on summation Level Indicator in TRIN which pointed out in earlier commentary..*





# SPX

9 DMA & 50 DMA cross should get the momentum Traders out of the Market



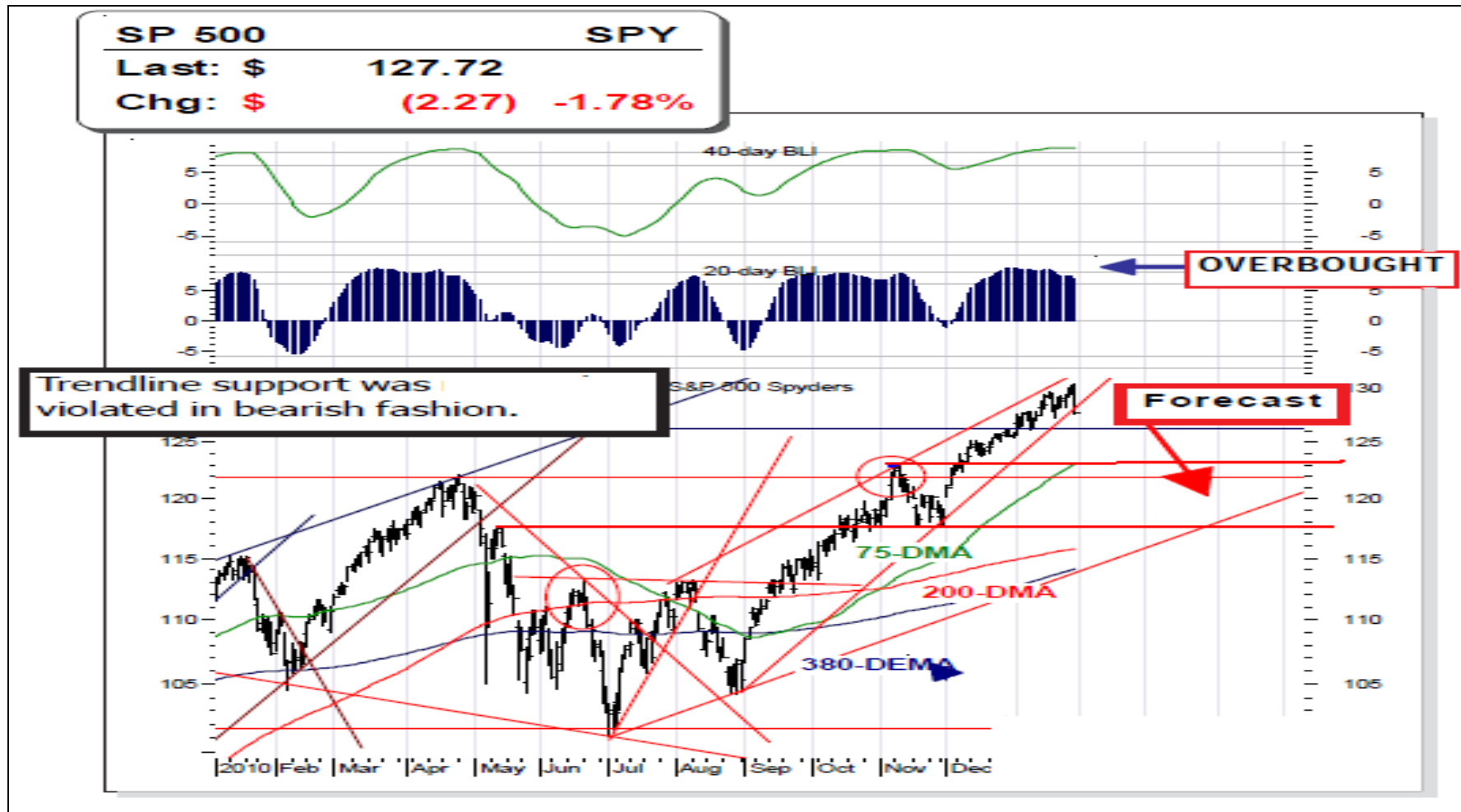
## SPX – MT

*MACD has turned down & Rolled over . RSI is clearly topped diverging, Volume picked up on decline, if the Trend lines ( indicated holds even with higher volume, we should have another rally that should give us divergences on all our Indicators . A normal pullback would bring the SPX back to 1225 in green. . We will monitor the VTO and Volume study for the tests. .*



## SPX – MT - MA's & Trend lines

The last Bearish wedge failed but the Trend line has broken , On Trend Adjusted signal stop at 1285 is triggered. Our Target back to 1230 target first and then daily Wedge indicated at the base is 1180 and then finally to the false breakout area as our downside targets 1135 ( the last target may take time and not in straight line) . 1280 is material resistance, and we'll look for a correction to develop then assess the market condition once this level is achieved. The 20-D and 40-D models are showing signs of turning.



# SPX – LT – wkly **Bigger Picture – NO CHANGE – Volume declined on weekly test**

## And closed below 1280

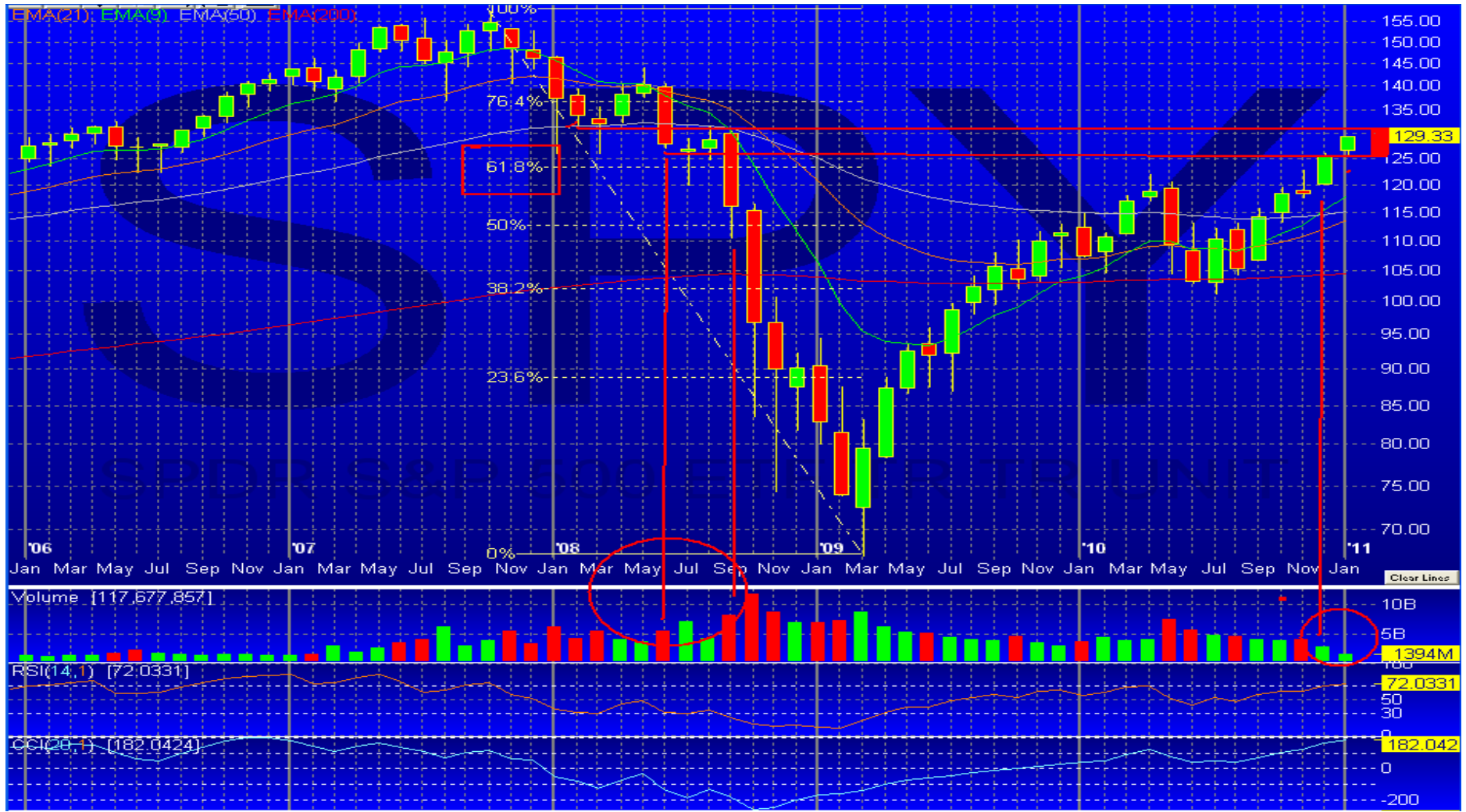
The weekly bars show the market trading at the highest level in more than two years and in a potential resistance zone marked by the early 2008 low near 1270 up to the summer high near 1280 (see lines). The S&P 500 has also retraced two-thirds of the 2007/2009 decline which often acts as a resistance level. More importantly, the RSI line on weekly ( which is more critical to achieve ) has reached the overbought 80 level for the first time since April and diverging. If nothing else, that may be a warning that the market rally has reached a point where it's in need of a pullback

The volume is contracting , This week we are into these area on SPY with 800k v/s 1000 and v/s 2.0B required by Benchmark for confirmed breakout. This is the 4<sup>th</sup> failure . There is a larger bearish wedge on Declining volume.



# SPX – LT – Monthly - Bigger Picture – NO CHANGE – We are looking for close below 1280 this month of Jan

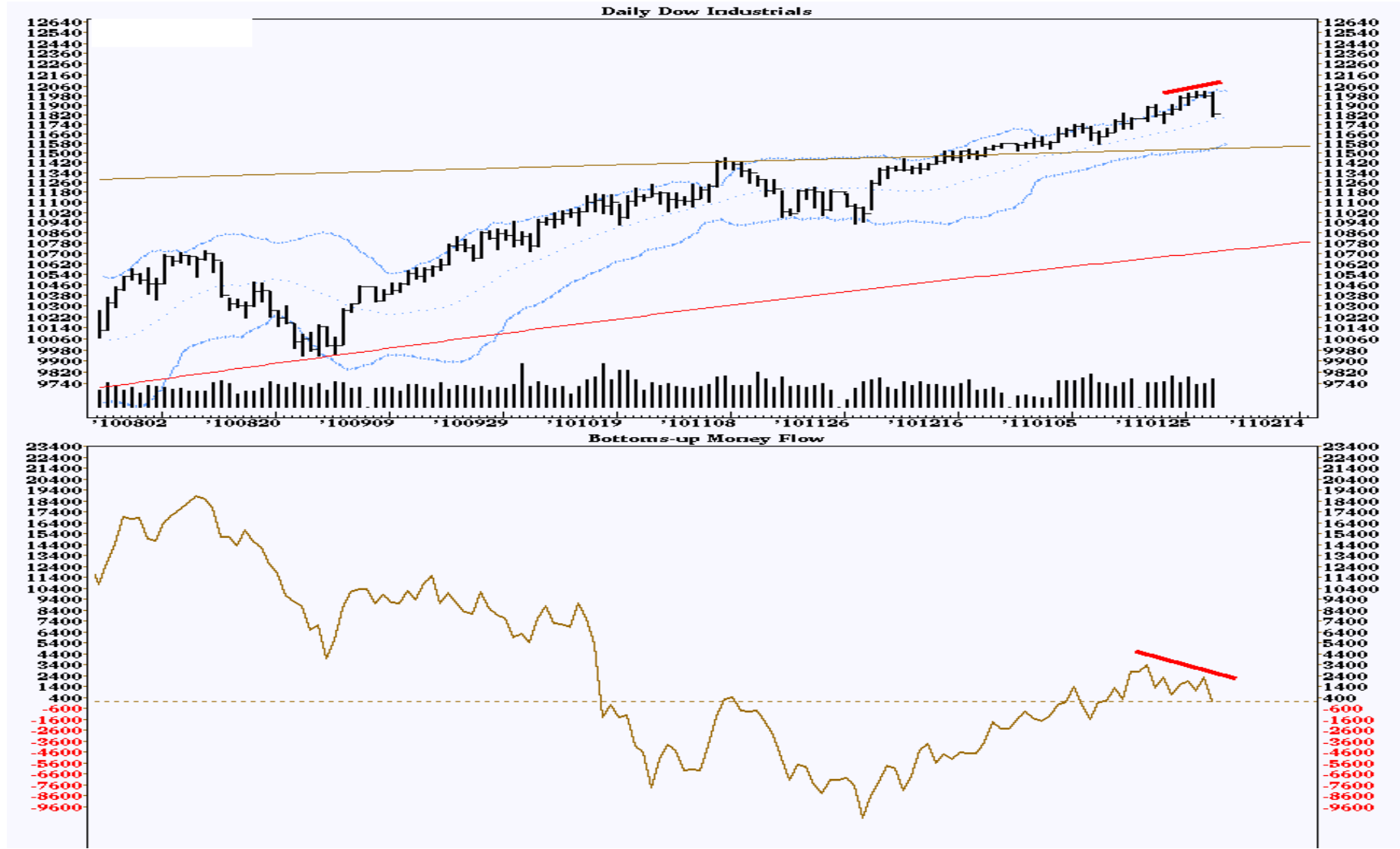
The Monthly RSI above 70 is very hard to achieve, we are currently in that area as indicated in red, approaching with lighter volume. The Leman Crash month is more visible here. If we close below 1280 this month, it should be rejection on monthly basis. We are in 61% retracement area which suggests the market may be trading range from 1280 to 1135 for some time .



- Secondary Market Analysis for SPX – POM clues – DOW , NYSE, RUSSEL

DOW –

*DOW cracked last week with line break indicator break , Diverging money flow. Even generals are exiting*



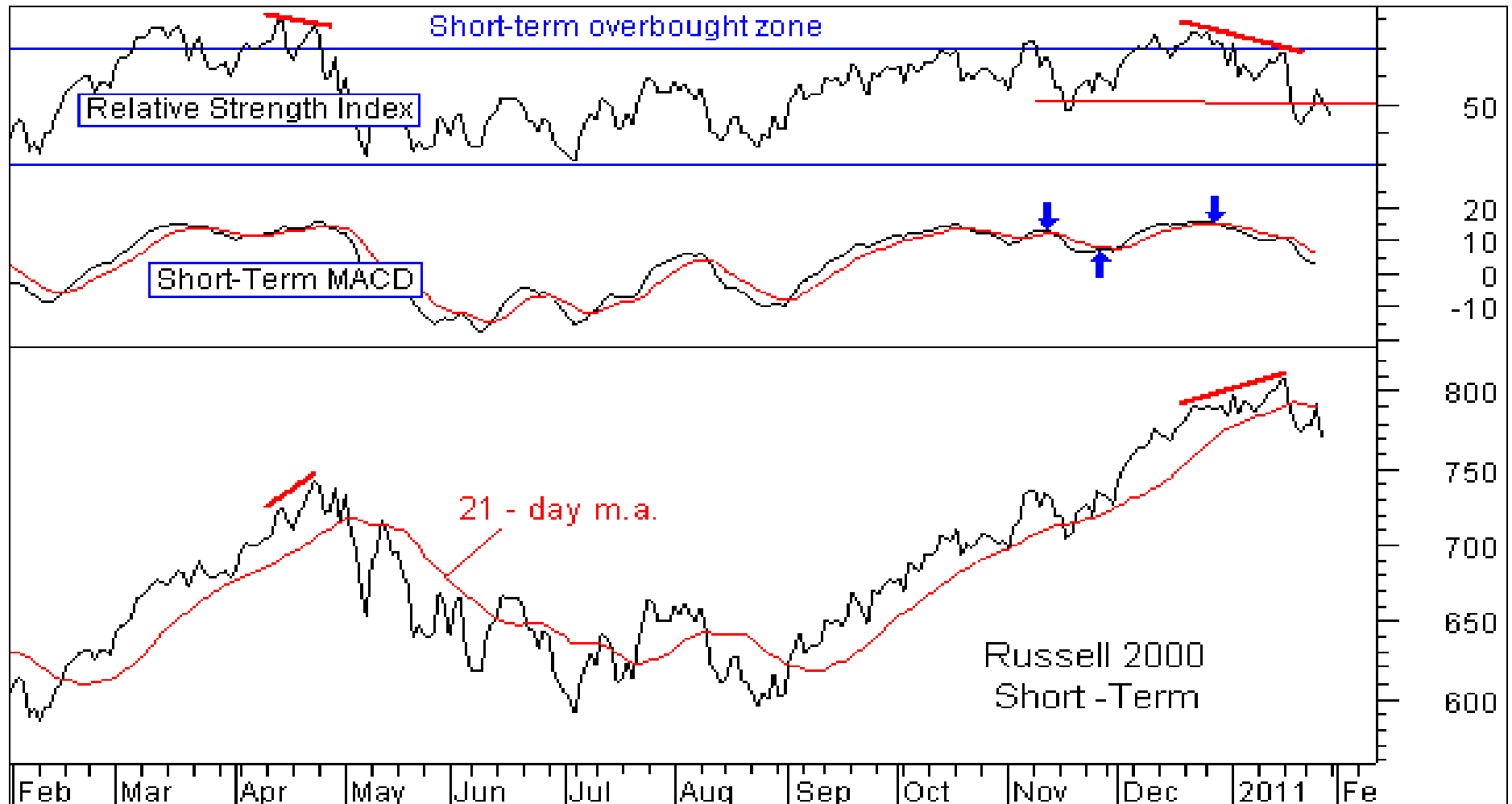
# RUSSEL

On Short term currently at the critical point above Poly trend line either for another bounce or quick below it . However Russell had high volume with Bearish engulfing and a Re test that failed , it gave few warning signs as a part of topping process within CZ of PQV price criteria that was triggered.



# RUSSEL

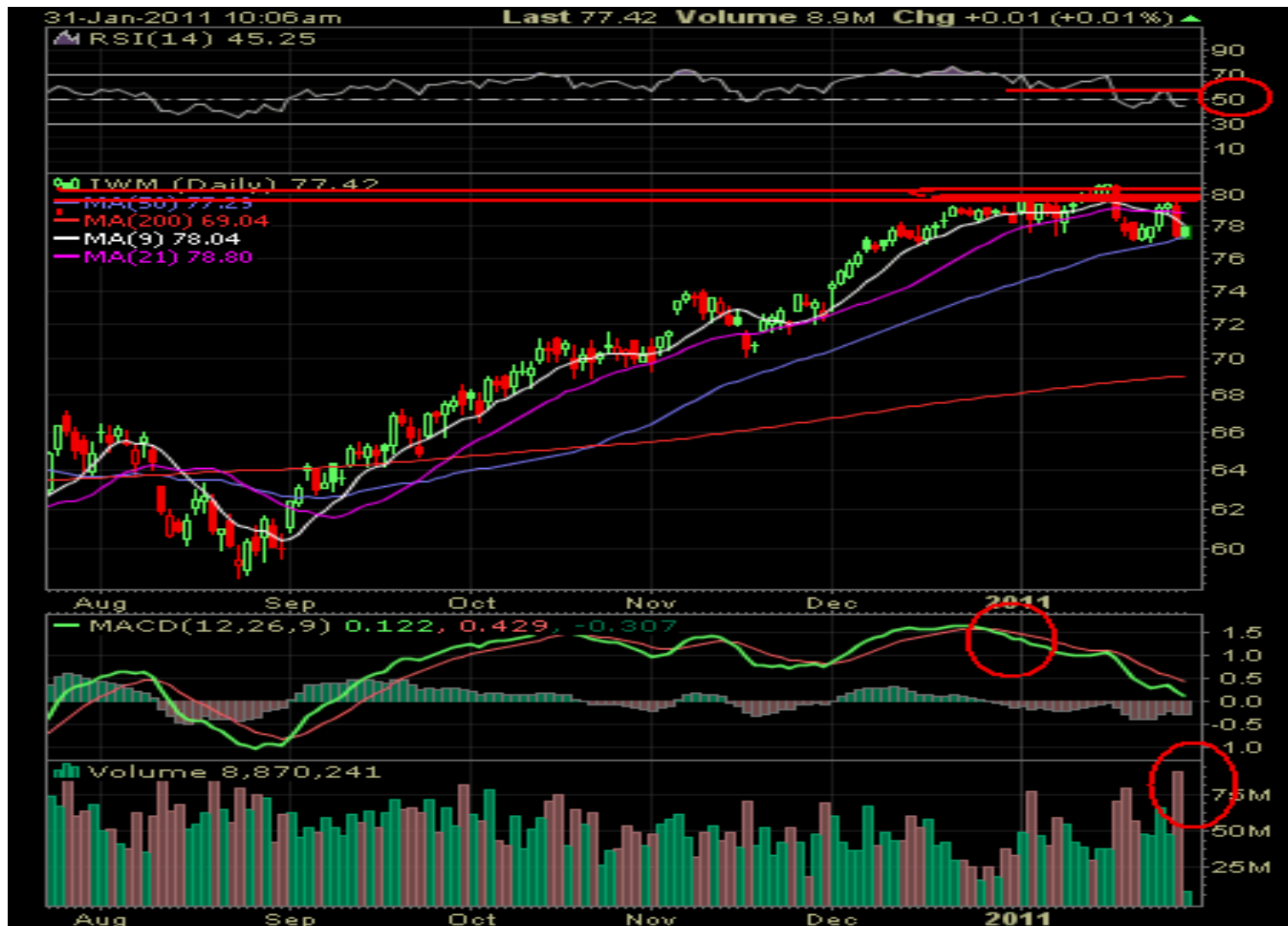
The Russell broke below the previous support at its 21-day and could not rally past that last week, and RSI & MACD has rolled over / rolled over to the downside.





## IWM - MID TERM

*The CZ marked in Red below proved its merit on primary and secondary test in PQV – Validation in sector Analysis. MACD has rolled over and Index broke the 21 & 50 D on heavy volume, RSI now in bearish territory.*

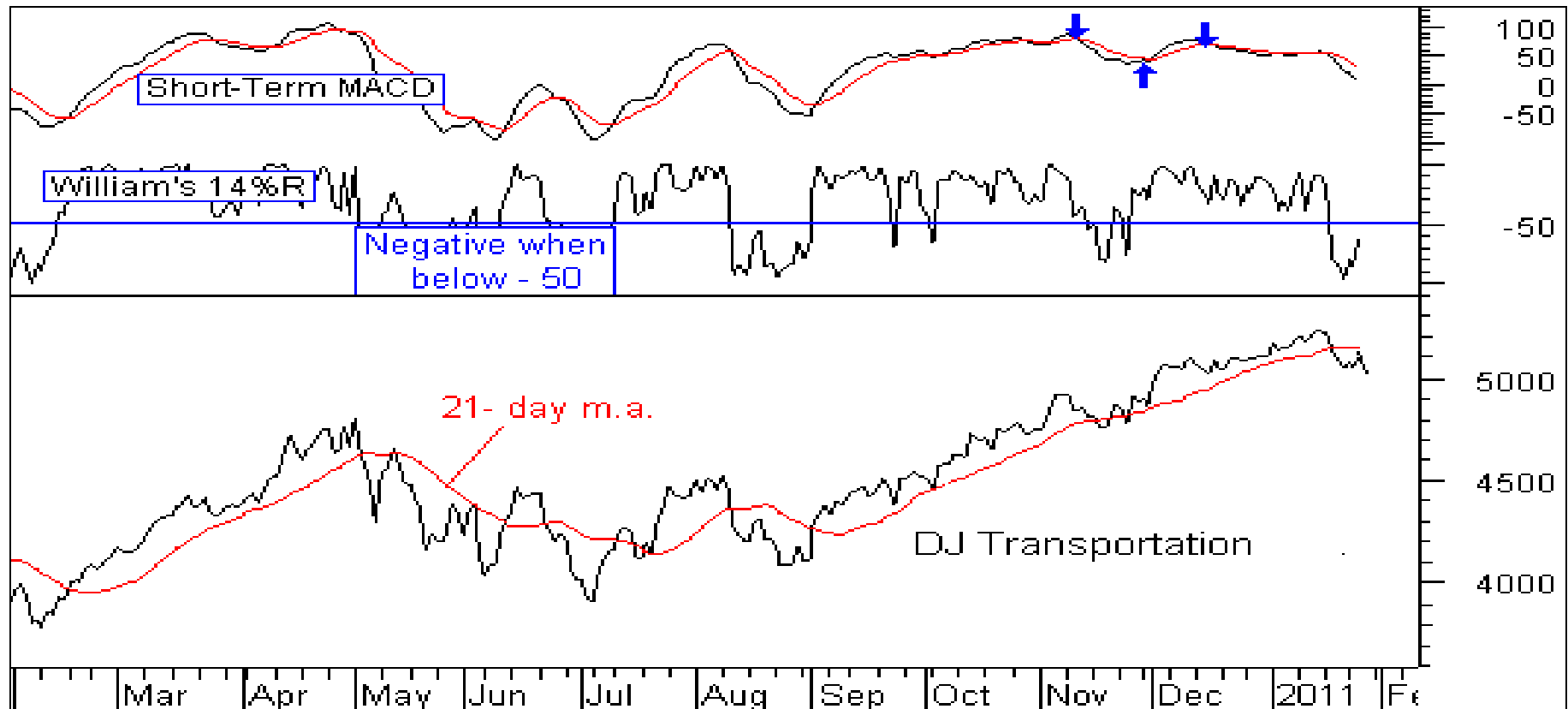


- Sector Analysis for SPX – POM clues – IYT, BKX, SMH ( 2 lead Sectors)

*IYT, BKX & SMH are the Lead Sectors on radar either for market tops or Bottom, Money flow into these are very critical for market advances.*

## IYT

*DJ Transportation often leads the market in both directions. And short-term indicators turned and the index has dropped below the previous short-term support at its 21-day m.a. and MACD potentially rolling over. The prices are above its 200 MA ( See next chart below) that usually results in a correction down at least to the m.a.*



**BKX** *BKX right on the other side of Poly Trend and diverging bearishly against the money flow index. This leading sector is very weak and warning of problems to come. Not much interest in Bank stocks in spite of the SPX rally.*



## • Time Cycle Analysis

Our Time - cycle Analysis is based Seasonality, Calendar events, Astros Harmonics, Geomagnetic (including Bradley Model) & T – Termination. Based on current market condition our observation points out the following condition

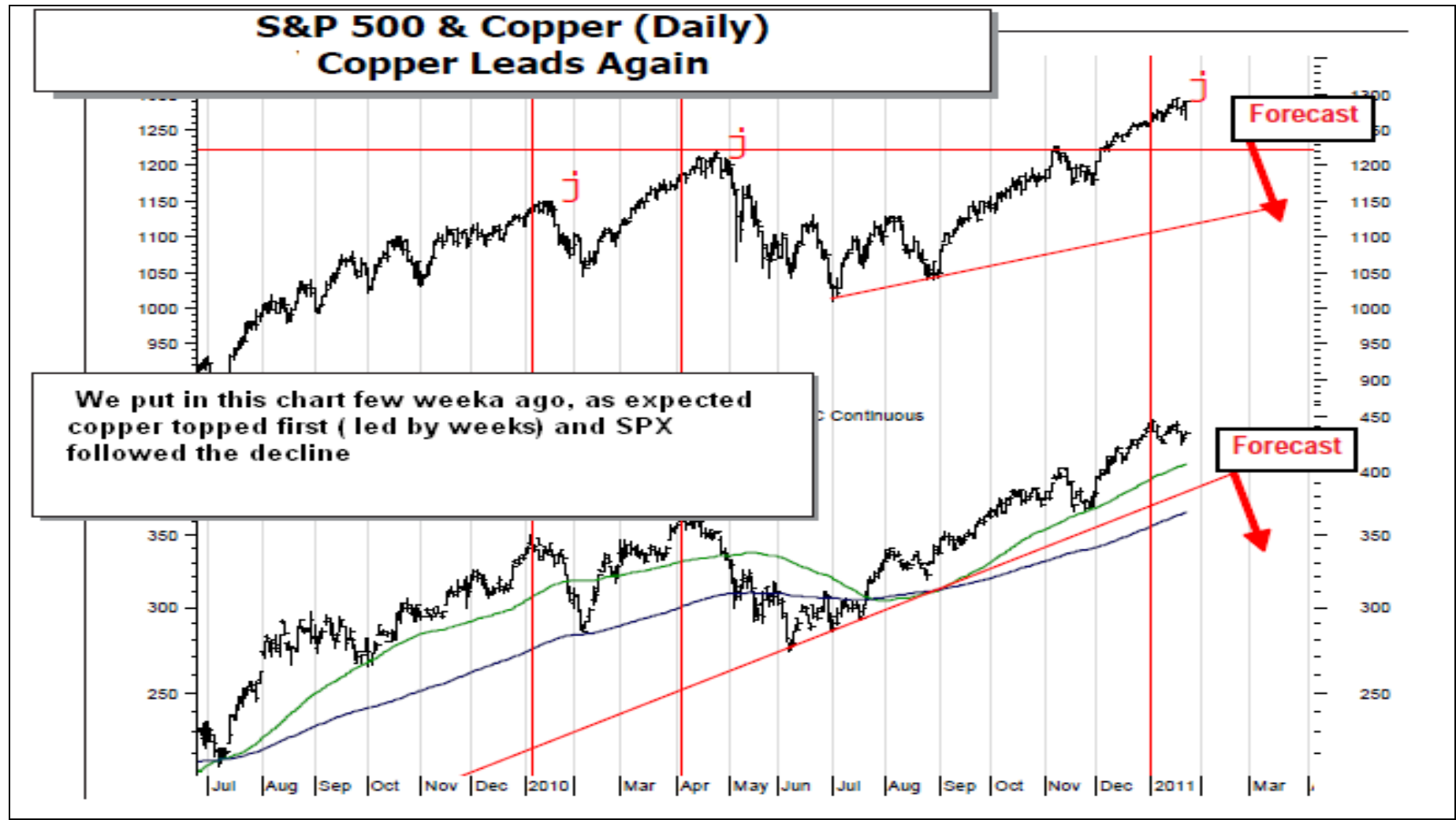
### Current upcoming Cycle dates

- *Past 6 yrs since 2004, NASD has dropped every year from 8<sup>th</sup> Jan to 31<sup>st</sup> Jan with average -3.5% loss worst being -7.5%.,*
- *8<sup>th</sup> Jan also coincides with CITI Group study for Major market top 2011-2012*
- *2011 is 3rd year of the presidential cycle and historically has positive returns*
- *Time cycles are concerned, is forecasting a January peak in the stock market and a decline to mid-February, which fits very well with the extended condition of this market.*
- *Earnings Cycle to begin very soon, Last January, April, July had triggered the Selloff, however the September it did not work . We would certainly like to see the impact post 15<sup>th</sup> January if the good earnings are already priced in or not*
- *Our own Study for January in (2003 – 2006) Uptrend & (2007 – 2010) Sideways Market.*

From 2003 - 2006		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
Average	-0.25%	0.36%	-0.40%	1.41%	1.55%	0.73%	0.57%	0.76%	0.72%	2.07%	2.43%	2.37%	13.00%	
From 2007 - 2010		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	
Average	-4.24%	-3.45%	3.71%	4.99%	0.36%	-3.94%	2.53%	0.28%	1.71%	-3.44%	-1.60%	2.06%	0.32%	
<b>Average</b>	<b>-2.25%</b>	<b>-1.54%</b>	<b>1.65%</b>	<b>3.20%</b>	<b>0.95%</b>	<b>-1.60%</b>	<b>1.55%</b>	<b>0.52%</b>	<b>1.22%</b>	<b>-0.68%</b>	<b>0.42%</b>	<b>2.21%</b>	<b>6.66%</b>	

## SPX v/s Copper –

*Copper topped out 2 weeks prior to SPX in past tops , we noted this chart 2 weeks ago highlighted that correlation. , JJC (Copper ETF validated CZ – PQV at that time in Sector Analysis.*



## The Bradley Model – Turns Bearish 1<sup>st</sup> JAN 2011 till 28<sup>th</sup> FEB

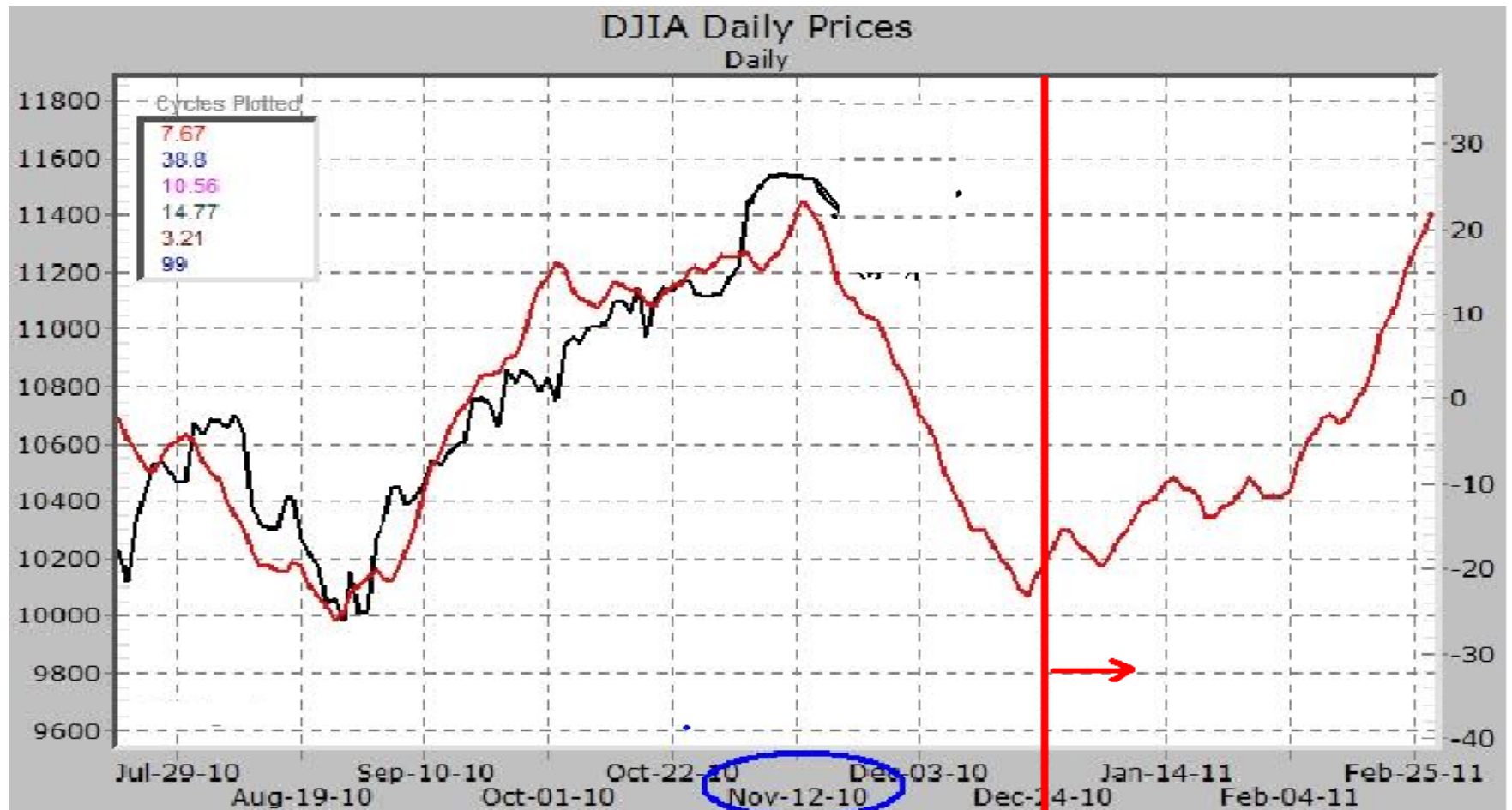
If you look at the model on a long term basis, it also provides a very good outline of what should happen (not always what will happen) over a period of months ( We will retain this chart and monitor with SPX )



## The 4 Yr – Price path Cycles – Turns Bullish - 28<sup>th</sup> DEC to End FEB

( We will retain this chart and monitor with SPX )

NEXT TWO MONTHSON CYCLES - BULLISH



- **Advance / Decline Internal behavior Analysis**

*Our A/D Analysis is based on 3<sup>rd</sup> derivative complex A/D Oscillator instead of conventional A/D Line , secondly it needs to be conformed by the % of stocks above critical SMA's divergences. Based on current market condition our observation points out the following condition*

**SPX – NH - . NON-CONFIRMATIONS IN SPX BREADTH...**

**( METHOD 1 – Excluding the Bonds, ETF's and **Large cap Equally weighted**)**

*- The chart below covers, showing the SPX in red and trend of NYSE new highs: Low Ratio (NY HL) in Blue. NY HL moved sharply lower last week.*

**NASD (OTC) – AD Price line - . NON-CONFIRMATIONS IN NASD BREADTH...**

*NASD doesn't have ETF and Bond funds , Equally weighted AD line . The multi month high in NASD, HL is significant because this indicator has a decidedly negative bias*

***A/D Line Indicators will start communicating on next bounce, that should give a good indication of quality of bounce***



- **Sentiment Analysis**

*Our Sentiment Analysis has “Intermediate & Short term” composition. We evaluate ( 8- 9) Indicators for sentiments out of which some are working well for Short term and other for Intermediate terms These are either Numerical Indicators as the Investors sentiments is expressed through purchases of the market*

*The Numerical we track are Tick, TRIN Arms, Put / call ratio, VIX Transform volatility (all 2<sup>nd</sup> / 3<sup>rd</sup> derivatives) , Rydex flow, Insiders activity. The Emotional / Survey sentiments we track Investors Intelligence sentiment Advisors sentiments. etc. All these are Integral part of POM composition ,*

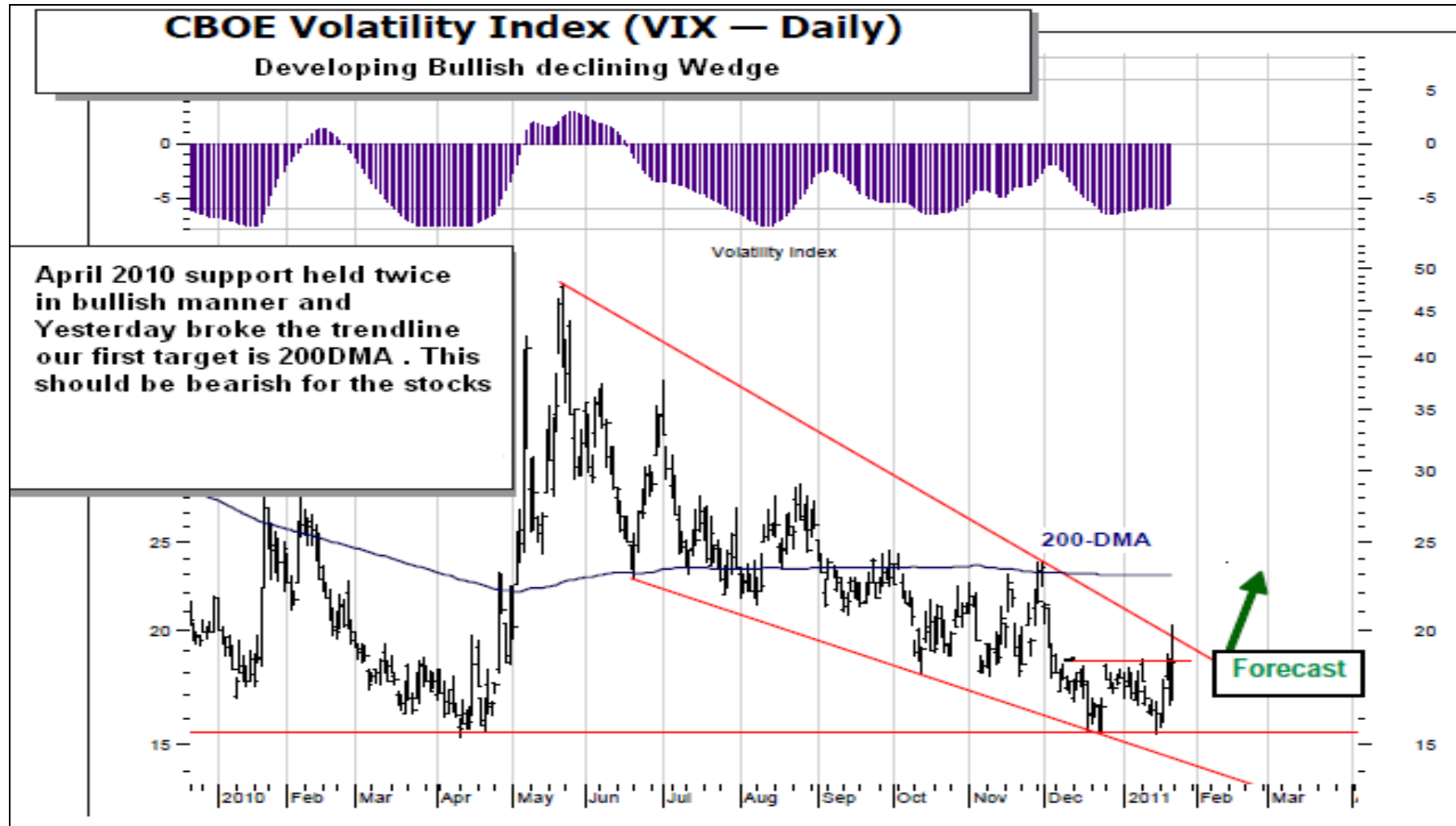
*Based on current market condition and the probability of Indicators we point out the **EXTERME INDICATOR ONLY** as a observation points.*

## **EXTERME INDICATORS**

- . **Sentiment ( Short term) has reversed** Our Mathematical Indicators such as **OEX Ratio, ARMS, TRIN, TICK, VIX** in their first and second derivatives have reached areas where at least a meaningful pull back has happened.
- **Commercial Hedgers** are at extremes Net position where the Previous tops have occurred
- **Rydex NASD Bull Ratio** are at Positions where the Previous extremes tops have occurred
- **AAll @** at Positions where the Previous extremes tops have occurred
- **Insiders Selling @** at Positions where the Previous extremes tops have occurred
- **Speculator Buying @** at Positions where the Previous extremes tops have occurred
- **Mutual fund cash levels are at 3.5 percent — very close to their all time low of 3.4 percent.**

## VIX – MT - This is very significant

*VIX Broke out the Declining Trend line surging 25% with sign of strength after several bottom tests. Since October, the VIX index with sentiment of options players, has been in the zone of extreme low fear seen at each of the rally peaks, see last April peak and in the last two weeks declined to the lower limit of that zone*



## VIX – Bigger Picture

*The below is self explanatory shows it all at various critical bottoms.*



- Global Market Analysis for SPX – POM clues – AORD,CHINA

### AORD

*This is looking more bearish as it is trying to form a diagonal triangle. The massive selling, reflected in the volume oscillator, suggest the risks are rising on the downside. This market has yet to exceed last April's high while most other markets are well above their highs of almost a year ago. This reflects the possibility that weakness in China.*

*EWA- 2 weeks ago reached our CZ and validated PQV test, to capitalize on AORD move*



## .CHINA - MID TERM

*The triangulation in the Chinese market has a standard bearish interpretation . Triangles are continuations and the continuation would presumably be to the downside to the CZ levels as Indicated in the Sector Report last week. China continues to be danger to world markets.*

*Larger picture - 50 % Bounce is still a Bear Market . Shanghai has been very weak recently, At a critical point at 2950 , Converging trend lines & EMA's produces a formidable resistance .*

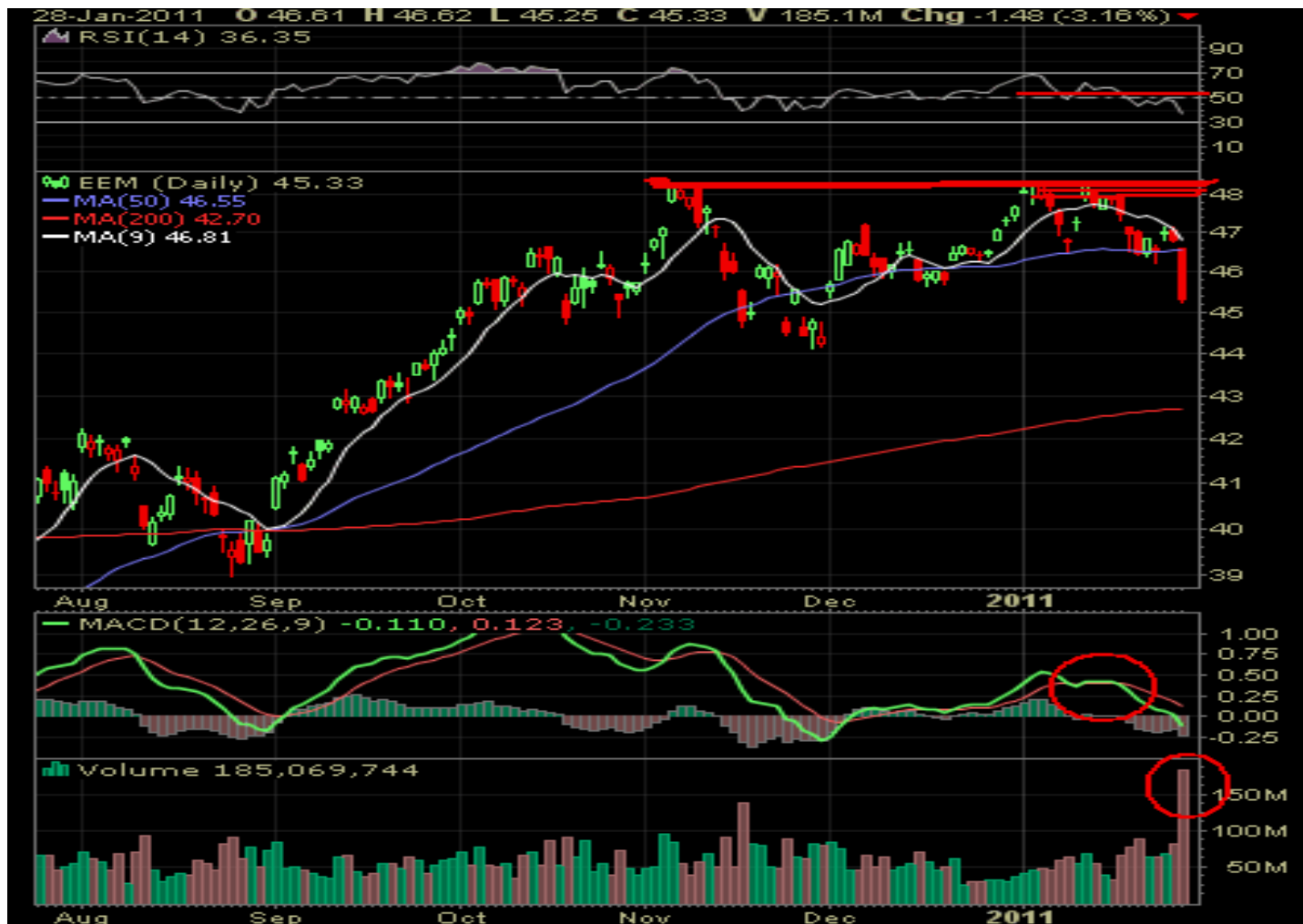
*We have EWH & EEM at the CZ – PQV to capitalize on this move.*



## EEM - MID TERM

*MACD has rolled over and Index broke the 21 & 50 D on heavy volume, RSI now in bearish territory. Our CZ- Validation test was at Red lines indicated in charts below.*

*The emerging markets had been underperforming US past month. Asian markets leading global markets into a correction, with rising rates and rampant inflation .*



## FTSE - MID TERM

*The FTSE is clearly in a short term downtrend, the volume oscillator is able to form an distribution pattern ( declining bottoms. Bounces certainly possible but breaking the lows on volume. After placing a lighter volume double top.*



# Appendix

## On closure of 2010,

As we begin 2011, let us Summarize 2010 and put the year behind us. The Aggregate POM Signals for the Full year on absolute basis irrespective of the SPX market moves. Our review is to attempt to do better in the following year as best as we can within our limitations and capabilities.

- Long Side – We had ( 4) clear POM 12 to POM 14 ( 7.5% FEB, 7.0% MAY, 10% JULY, 9.5% AUG) = Total of 34% up move
- Hedge Longs / Risk Management for Downside Corrections - We had ( 4) , POM 14 to POM 13/12 ( 9% JAN, 8% JUNE, 8% AUG & In the last Qtr extended move we had – 5% Drawdown) = Total of 20% Risk management move
- Net Short– We had (1) Clear POM 15 to POM 13 – April / May for decline of 9% = Total move of 9%
- In last 4Q , 2010 – We began tracking “ Trend Adjusted Signal” 3X3 / 9EMA - on Long Side - post POM 14 ( 8% & 4% ) = Total move of 12% .

### History - “ SPX – POM Signals & Projections”

- 2010 YTD– This year, we have had (3) clean TREND SIGNALS rise from “ POM 12 to POM 14 “ for LONG IDEAS
- FEB - 7.5% ,
- MAY - 7.0%
- JULY - 10.0 %

And (1) POM 15 to POM 13 ( drop of - 9% - April /May ) for Net Short Ideas

(3) Risk Managed POM 14 declines to POM 12 or 13

- JAN - ( drop of - 9 % )
- JUNE - ( drop of - 8 % )
- AUG -- ( drop of - 8 % )
-





## POM criteria for Implementation on SPX

- POM is rated from 10 to 15
- POM 14 , 15 ( is Sell Signal) and 12 , 11 ( is Buy Signal ) both are the Actionable Area whereas POM 13 is A Neutral Signal for Risk management
- On way UP move, POM 13 signifies to STOP executing additional “New Buys” that was initiated at POM 12 or POM 11 levels
- On way DOWN move, POM 13 signifies to STOP executing additional “ New Short Sells” that was initiated at POM 14 or POM 15 levels
- (Bear Markets) POM 15 is for - Net Short & POM 14 is for - Hedge Longs
- (Bull Markets) POM 15 is for -Hedge Longs & POM 14 is for - Partial Hedge
- POM 12 & 11 is for Net Long
- POM 10 is Climatic Crash low Buy Signal to add to Net long position (Rear event)

## Daily SPX - “ Trend Adjusted Signal”

- 3x3 /9EMA – Break Indicator

*The process utilizes the cumulative Algorithm of price trails 3x3 / 9EMA input signals for Trend formation. This signal tends to work well in Market extensions (i.e. Post POM 14).*

*This Methodology is implemented by Program Traders especially in Momentum extensions and diagonal triangle formation Trend-following system which bases its reversal signals on breaking a significant closing Break Indicator I to confirm the new trend. ( it's important to use a stop if you act on a signal). The reversal price is generated on the close of a bar. (The drawback of strategy is that it can whip saw).*

### INTERNALS OF 3X3- 9EMA – Break Indicator.

*The line break indicator has captured the post POM 14 Moves on a mechanical basis. Although can't guarantee it will continue. But, even if it misses on occasion , it's still is the best indicator we've ever seen in Market for extensions.*

*Tight trading ranges tend to cause whipsaws and those are environments where trading multiple markets can help for diversification, in SPX & DOW. The reason is that we have a purely mechanical indicator, our line break indicator, that is much better to use. That indicator has proven extremely good over the past several months in many markets in many extensions.*

*As a reminder of how simple this indicator is, when the market closes above the "break" price level, the indicator is ""bullish"; when the market closes below the break price, the indicator is then "bearish". at the close*

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