



SG Capital Research

Global Market Insights

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

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Market Strategy Global (A # 1) - SPX – Closed @ 1224 – Wkly change (+16 points)

Analysis of Broad Market that includes

- 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 , DOW MT
- Secondary Market Analysis for SPX clues – NASD, NYSE, RUSS
- Sector Analysis for SPX clues – IYR, XLU
- Time / Cycle Analysis- Bradley Cycle, 4 yr Cycle,
- Advance / Decline Internal market behavior – A/D – NASD , SPX
- Sentiment Analysis with Extreme character – ,AAII, NAAIM, VIX, TICK
- Global Market Analysis for SPX clues – FTSE, CHINA, AUSS (New)
- 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**

- *We recommend Fully Hedged on Long positions that were triggered at POM 12 @ SPX 1020 in July 2010 and / Or at last POM 13 @ 1045.*
- *Via accumulations in the "SETUP - PQV VALIDATED EQUITY INDEX – EQWT (from Sec E – MAEG) , with desired price points & scaled entry @ the Mean Confluence Zone on these weakest Equities in Setup #2. This would capitalize on current situation (Within RA / RI framework for Risk management) .*
- *Our current " SETUP –PQV EQWT EQUITY " Hedged Index is at **-6.26 % Drawdown v/s 12.36 %** SPX Longs during post POM 14 extension in same timeframe.*
- *No Net Short Position" till POM 15 Re- run is triggered. Therefore we have been on sidelines post SPX -1105 move*
- *The price Equilibrium and favorable Risk / Reward opportunity will come at POM 13/ 12. This area we would be interested again*

• SPX Signals & Price Projections

- **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 1250-1280. We could very well trigger POM 15. Meanwhile we continue to remain POM 14 since SPX 1105,**
- **Our Pull back from here should be to 1130 (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)**
- **Due to seasonality 1160- 1150 SPX may hold first time around for the bounce.**

• Daily SPX - “ Trend Adjusted Signal”

3x3 /9EMA – Momentum Break Indicator – Long @ 1228 SPX

- **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%**
- **DOW still has to trigger so still divergence**

Currently “ Trend Adjusted Signal “ has Reversal stop @ 1178 SPX & DOW 11430.

Sym	Posn	Close	Reversal
DJ	Short	11372.5	11430.5
SPX	Long NEW	1228.69	1178.34

The Line Break Indicator is purely mechanical Indicator and has proven good for Momentum and Extensions of the markets. Tight trading ranges tend to cause whipsaws, therefore participating in multiple markets can help for diversification in SPX & DOW. (The drawback of strategy is that it can whip saw).

- **Market Insights**

This acceleration into the SPX to higher levels of overvaluation as long as the Fed is providing the buying power during QE2. Over the month starting on Monday the 13th, the Fed will be buying \$105 Billion worth of securities. The middle of the week passed that the Fed injections POMO were propping the stock market up. By this we did not get the close weekly below 1210 to trigger bearish signal. Also time T termination has extended beyond 9th Dec expiration.. However, signs of weakness are appearing, including bearishly-diverging money flow in the small- and Dow.

The broad market indices are testing recovery highs, near resistance and vulnerable to a selloff over the next several weeks except the possibility of little delay due to seasonality into the New Year." We got a minor pullback in stocks to 1173 , then a resumption of the uptrend. This wave up is likely to top soon, However EURO which is closely correlated with SPX move wants to bounce. Once the EURO tops out then SPX should as well.

So, despite the market could be setting up for a correction, The SPX appears to be aiming for a December expiration right around the 1250 major pivot first especially a Diagonal pattern has kicked in again. .

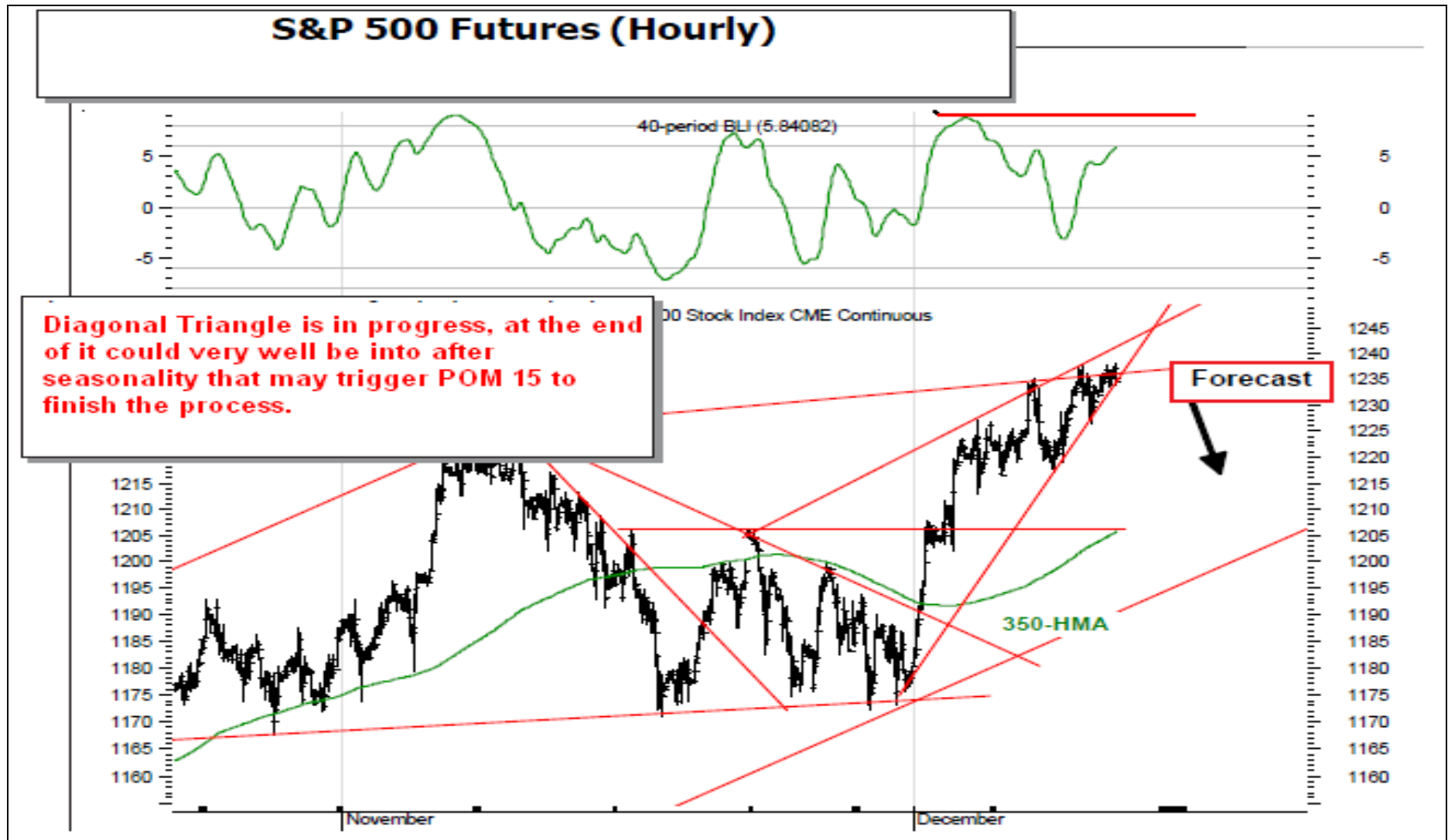
EURO v/s SPX

Chart below on EURO suggest where it could bounce to get the clue on SPX topping , look for 1.34 to revisit with RSI failing on reverse bounce at 50. Volume study suggest so far VTO is declining on bounce, We think at swing point volume could fail as well . Wait and see



Primary Market Analysis - SPX – HRLY – Trend lines & HMA

Short term, the SPX may be forming a diagonal triangle, which is a pattern which is always completely retraced once it finishes. If it were not for the Fed injecting buying power into the stock market, the SPX would be heading much, much lower. As it is, though, when the force of fiat money meets SPX, it is expected to complete the Apex of the Triangle and could very well signal POM 15.



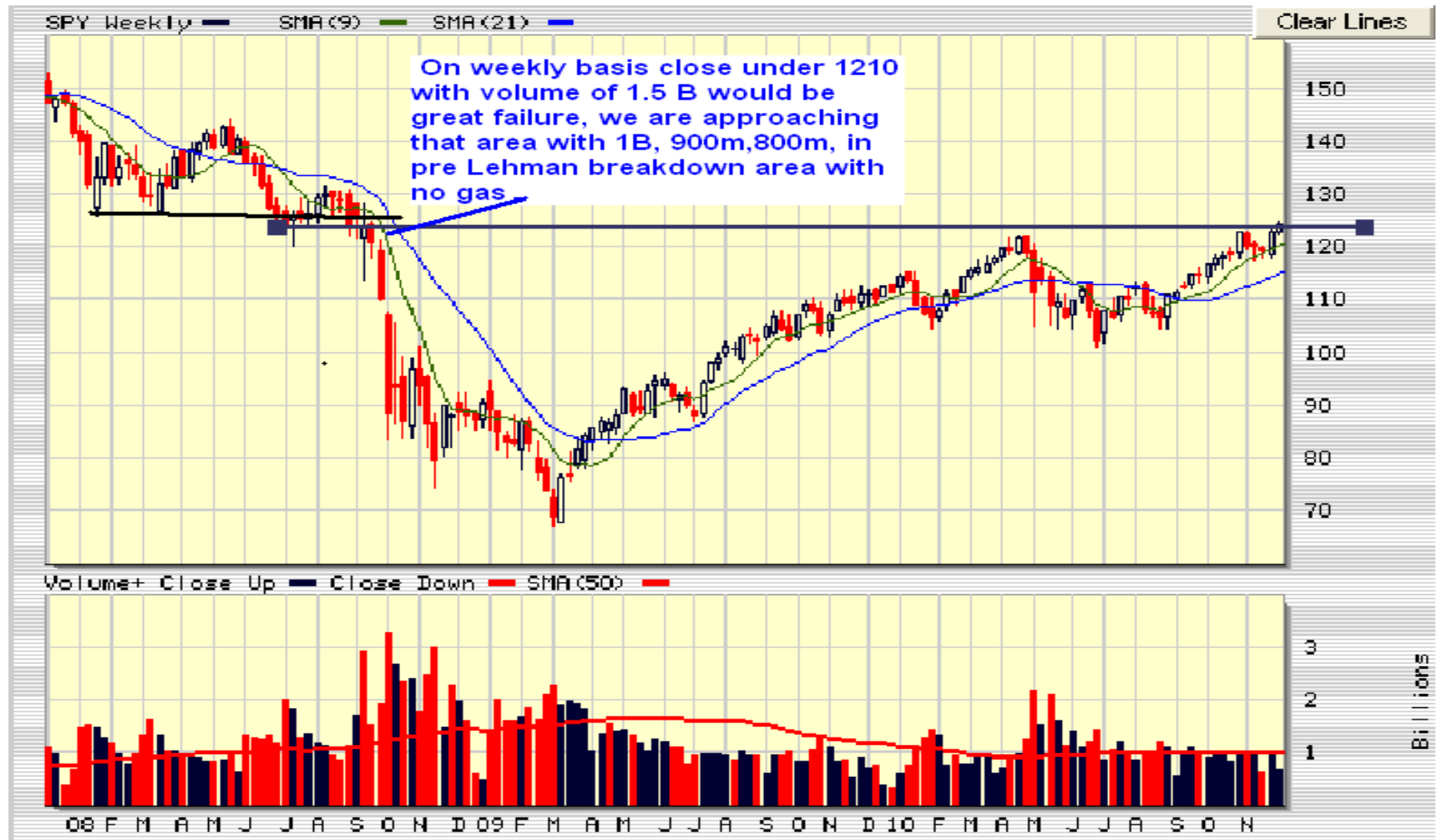
SPX – HRLY – Wave

Friday may have seen the completion of the third wave within the five-wave pattern. In any case, wave iv should be relatively shallow and followed by a wave v rally that reaches either 1240 or 1260 and completes the pattern: Our 3X3 / 9 EMA – Trend adjusted Signal triggered at 1228 to play this Trend of Diagonal Triangle. This might very well be Santa as Money Mangers wants to get the last bit before they move in other direction. This Hrlly pattern also has highest probability of failing as well



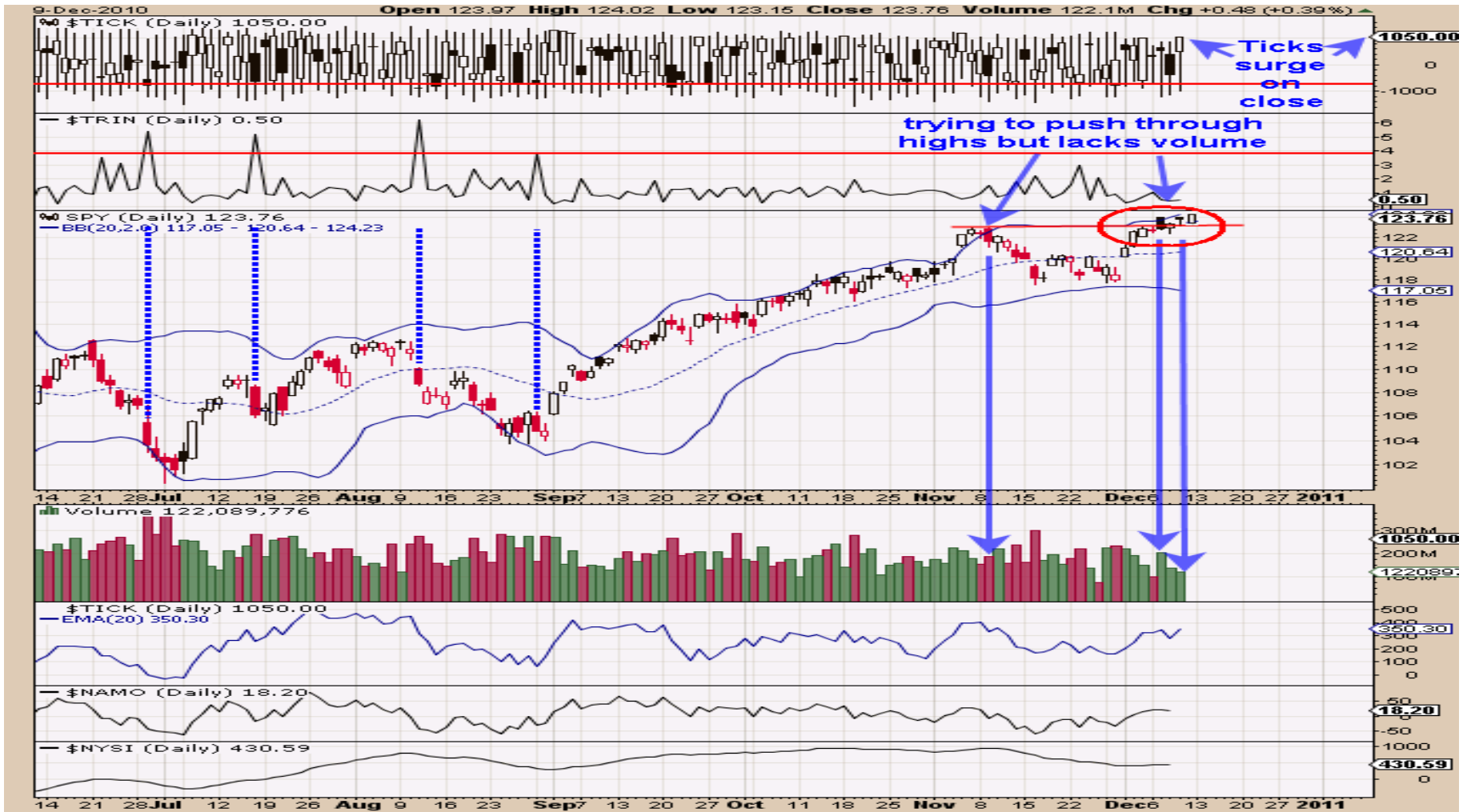
SPX – Price & Volume – LT

Currently SPX is double topping, entering into the Lows of 2008, Lehman's Crash dates , already passed through the Flash crash area on lighter volume etc. Last week we were looking for test of 1225 on weekly close under 1220 on lighter volume we did not get. ROC has diverged negatively . For benchmark (See the criteria for final failure within the chart notes)



SPX – MID TERM – Price & Volume

Now Zoom in to daily's after Fridays close, SPY tested the previous high of two days ago but volume was lacking to push the market higher. (but we did not get the close under suggest the prices can go higher even on false) . **But critical issue is the ticks surged on the close + 1060 which can be a warning that market is becoming exhausted.** Next week is option expiration week and the week before (this week) sometimes can be difficult to judge. With today's minor bounce up with light volume to test the high two day's ago suggests a pull back is not far off.



SPX – MID TERM – Waves

Since we made a higher high this week, we re counted the wave. SPX could be on the verge of a 5th wave, which suggest either way , we could have decline sooner than we think .The time termination on this top is 8th December . SPX is marching time over Poly trend lines.



SPX – TRIN - MID TERM

We showed this chart on last Monday and have updated Friday. There is more widening going into this ratio. This is the Trin/SPY ratio. When both the red and blue line is falling on the TRIN/SPY ratio then market rises and vice versa. When the Red line separates from the blue line in a large degree then expect a coming reversal in the market. It also appears that the wider the separation in the red and blue line the larger the move in the market. The TRIN/SPY ratio only picks out the larger moves in the market. Notice that the June and July 2009 and January February 2010 declines failed to even make a blimp on this ratio. However it has done a good job of picking the major moves in the market (see chart). . Right now both lines are trending down and suggest the bigger trend is up but the separation is getting wide which is warning that the bigger trend may not be far from a reversal. When both lines turn back up it will suggests the market has topped. Short term we expect the gap on spy near 120 to be touched.



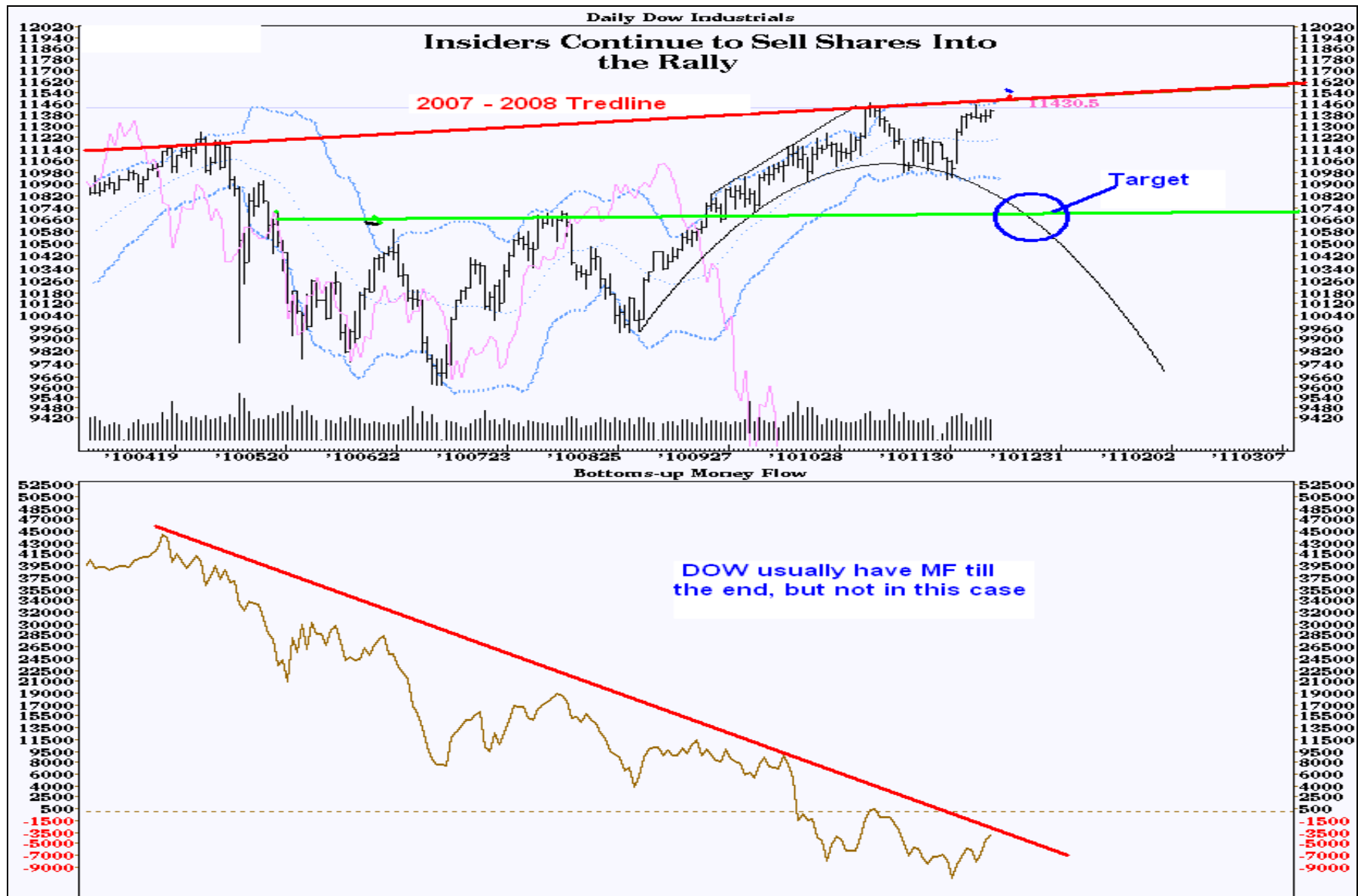
SPX v/s TLT

Bond are on verge of oversold. The Chinese, who had formerly been liquidating their holdings of US bonds, should come back now buying US bonds once again as they finally realize that buying euro-denominated debt for diversification purposes was definitely a very bad idea. When that scenario happens SPX should reverse. We have seen similar Inverse relation in past as indicated in chart below. Rally Bond and Fall in SPX



DIA - ST - MARKET GENERAL

The major bearish divergence here is not just the fact that money flow remains near its lows while the average is flirting with a new recovery high. The average is very close to a long term resistance line, formed by the significant lows of 1982, 1994 and 2003. That line was broken in 2008 and has yet to be successfully since.



- Secondary Market Analysis for SPX – POM clues – NASD, NYSE, RUSS

NASD . *A slight bearish divergence on new highs warns of slowing momentum. The leading stock in NDX is Apple, and selling pressure in that stock is warning that tech has limited upside .*



NYSE

According to the technical indicators, we should have a top in this general area. With the Composite right at the upper trading band and diverging bearishly against the money flow index, the fact that it's also at the upper channel line says caution is warranted despite the Fed's support.



RUSS

Russell showed that sellers were anxious to liquidate their holdings last week. This is a warning from a leading sector that the going is getting tough.



- Sector Analysis for SPX – POM clues – IYR, XLU

We found two weak sectors whiles SPX is at highs, XLU AND IYR UNDERPERFORM BROADER MARKET (We need to find Individual stocks within RA / RI framework for Shorts in PQV)

IYR

Real Estate peaking in early November and breaking support with a decline below 54. The ETF bounced back to 56, but the pattern looks like a rising flag and the ETF broke flag support on Thursday. The indicator window shows the price relative peaking in early September and moving lower the last three months. REITs are underperforming the broader market (SPY).



XLU

Utilities (XLU) battling trend line support the last two weeks. While SPY moved to a new high in early December, XLU remained well below its late October high. The price relative confirms relative weakness. XLU has been underperforming SPY since the beginning of September. (We need to find Individual stocks within RA / RI framework for Shorts in PQV)



- Time Cycle Analysis

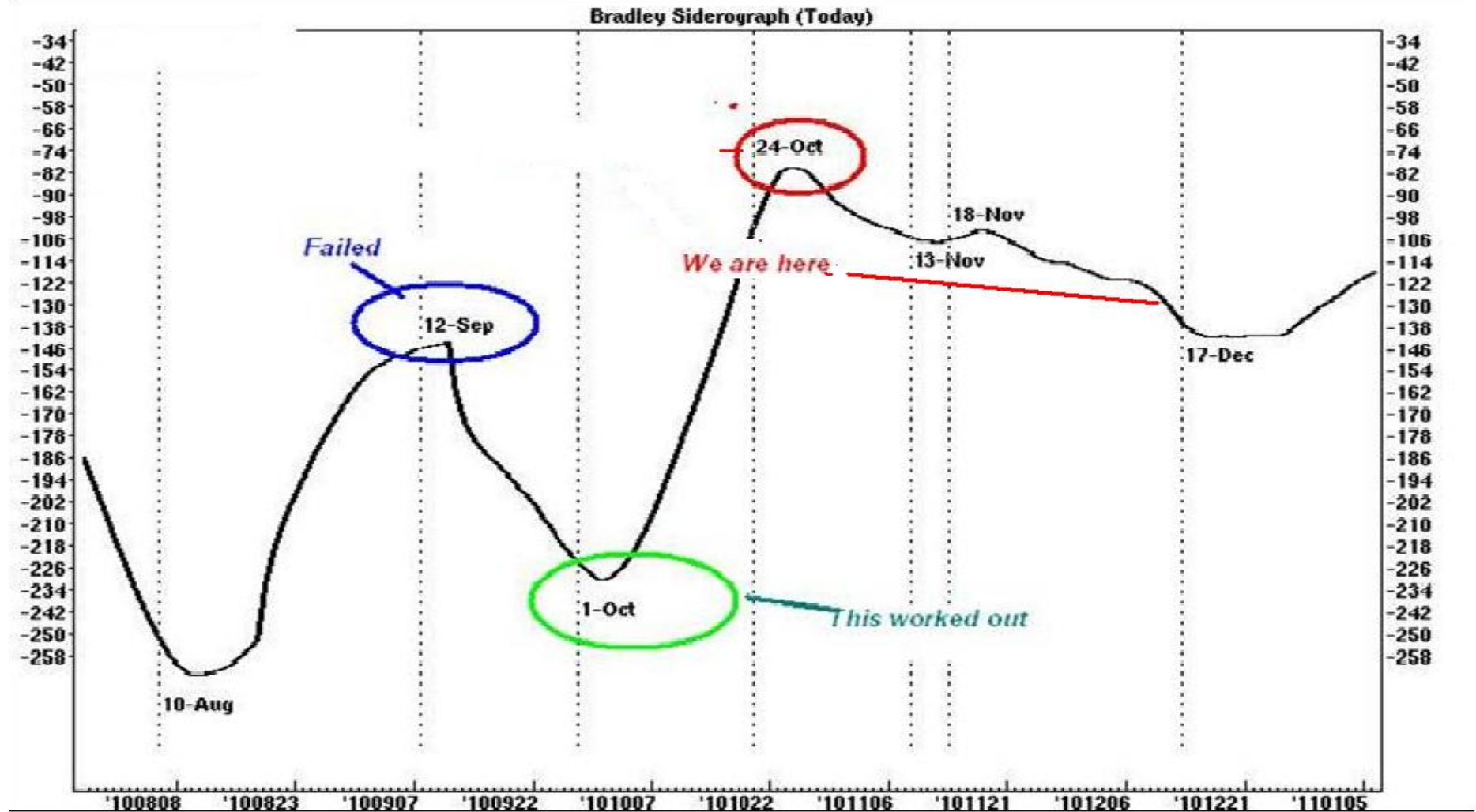
Our Time - cycle Analysis is based Seasonality, Calendar events, Astros Harmonics, Geomagnetic (including Bradley Model) & T – Termination. Based on current market condition our observation points out the following condition

Various cycle summary & dates

- Main - T – Terminations – Extended - Bearish. (But hasn't proven)
- **The seasonal pattern** is for the market to rally from 1ST Nov to 30 th April is till in tact. (Bullish)
- The Bradley is on 24th Oct to 17th Dec (Bearish) (But hasn't proven)
- **4 Year Cycle** , positive influence to begin 12th Nov t till 24th Dec (Bearish)
- COPPER Cycle – (Bearish)
- OIL Cycle – (Bearish)

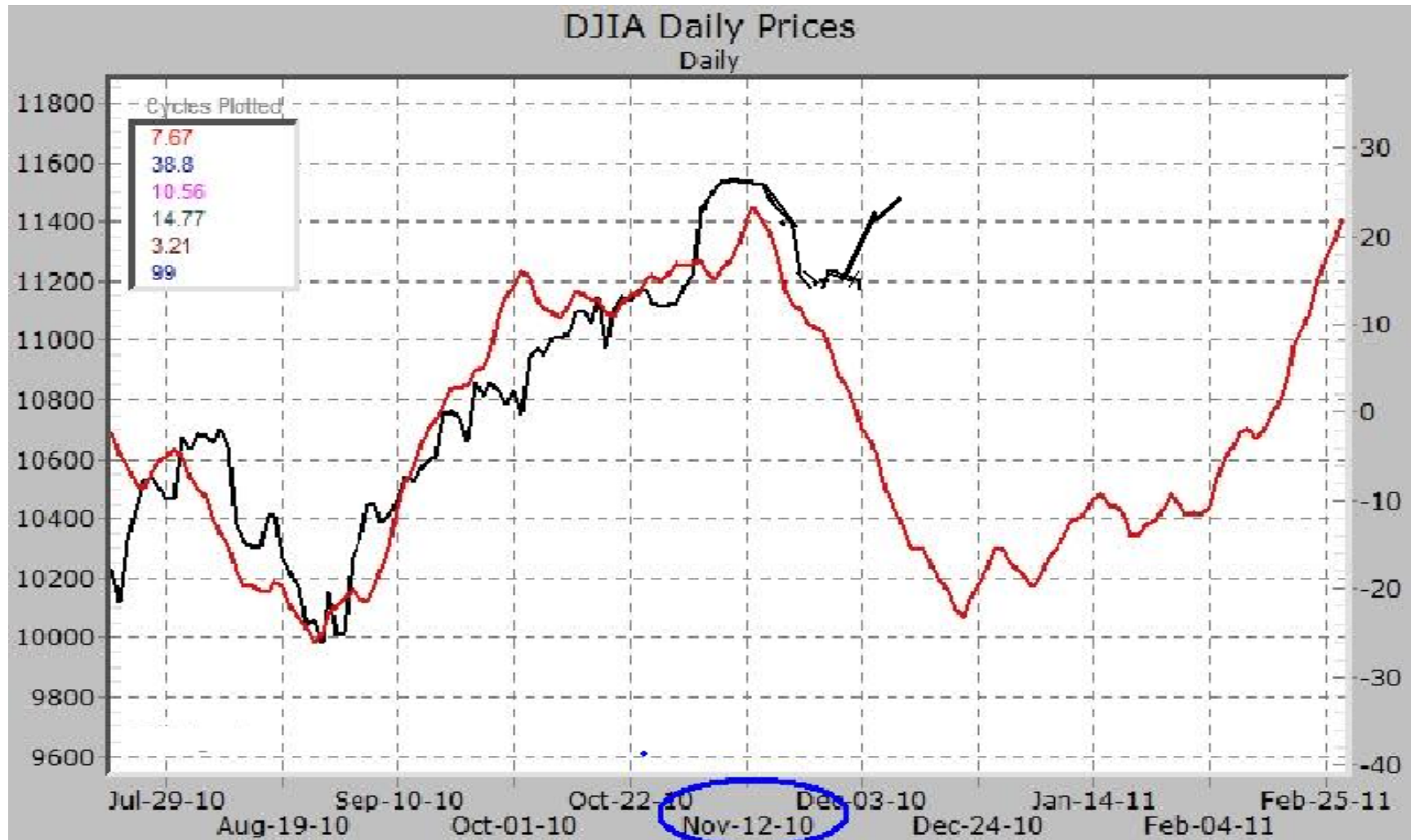
The Bradley Model – Bearish-Cycle in progress 24th Oct - 17th Dec = 5 days left

If the Bradley is still relevant, it is pointing toward a change-in-trend on 17th Dec in Downtrend. (This Model hasn't worked well for stocks consistently except the last trend but worked well for Bonds consistently).



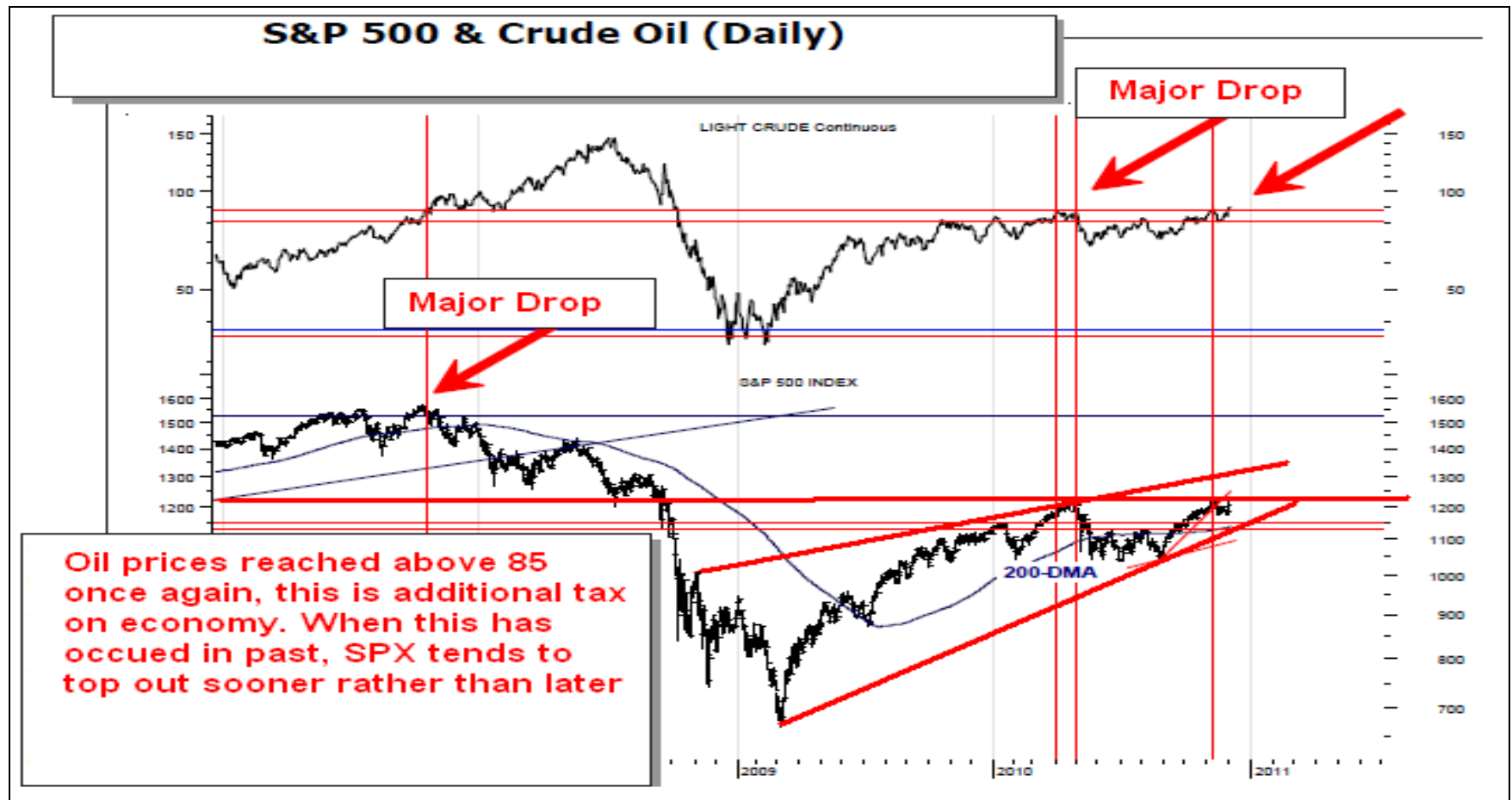
The 4 Yr – Price path Cycles – Bearish - Cycle in progress till 24th Dec = 10 days

Further projections peaking from 12th Nov till 26th Dec in downtrend by 4 yr cycle.



The Oil Cycles

Oil prices are heading higher wouldn't take a lot of price rise to offset the stimulus. If oil prices rise it would slide economy back into recession. We've chart of the SPX / Oil . We find it interesting, for once crude oil passes through the 85, then the SPX tends to top out in the near-future. In 2007 this occurred at the October-2007 high. In April of this year, prices moved this high, and the SPX topped. Now, we find oil passing 85 . Hence, we are on guard . .



- Advance / Decline Internal behavior Analysis

Our A/D Analysis is based on 3rd 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

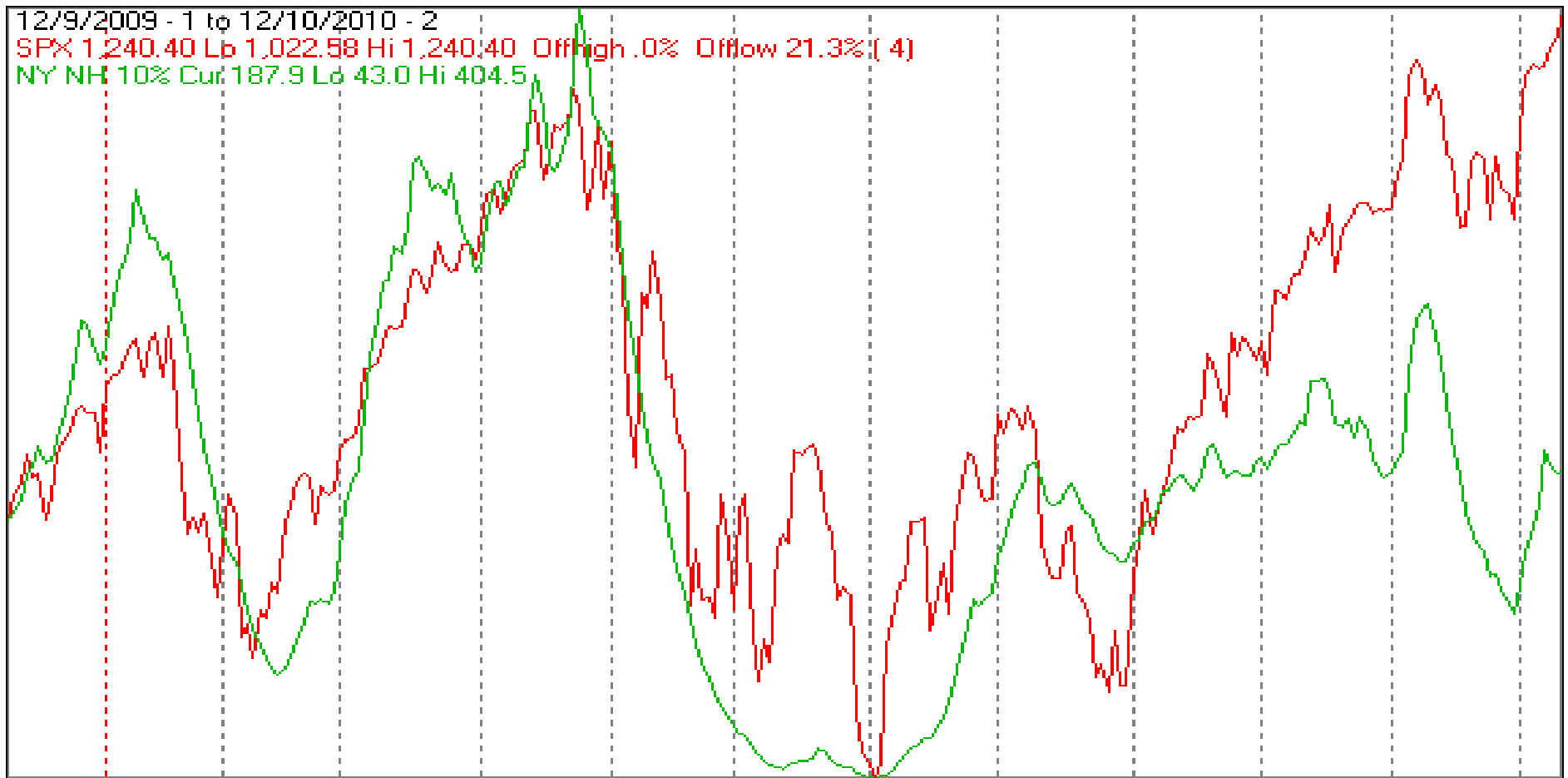
NASD – A / D - . NON-CONFIRMATIONS IN NASDAQ BREADTH...

The chart below covering the past year showing the NASD in blue and NASD's new highs in green. **NH continued to lag.**



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

The chart below is similar to the one above except it shows the (SPX) in red and NH new highs. The pattern is similar. NH continued to lag.



NASD – . NON-CONFIRMATIONS IN NASD BREADTH

To give you a historical perspective, the chart below covers the past 5 years.. This indicator has an extremely negative bias so a short term show of strength and Intermediate term as we are seeing now is significant.



- **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 2nd / 3^d 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 ,

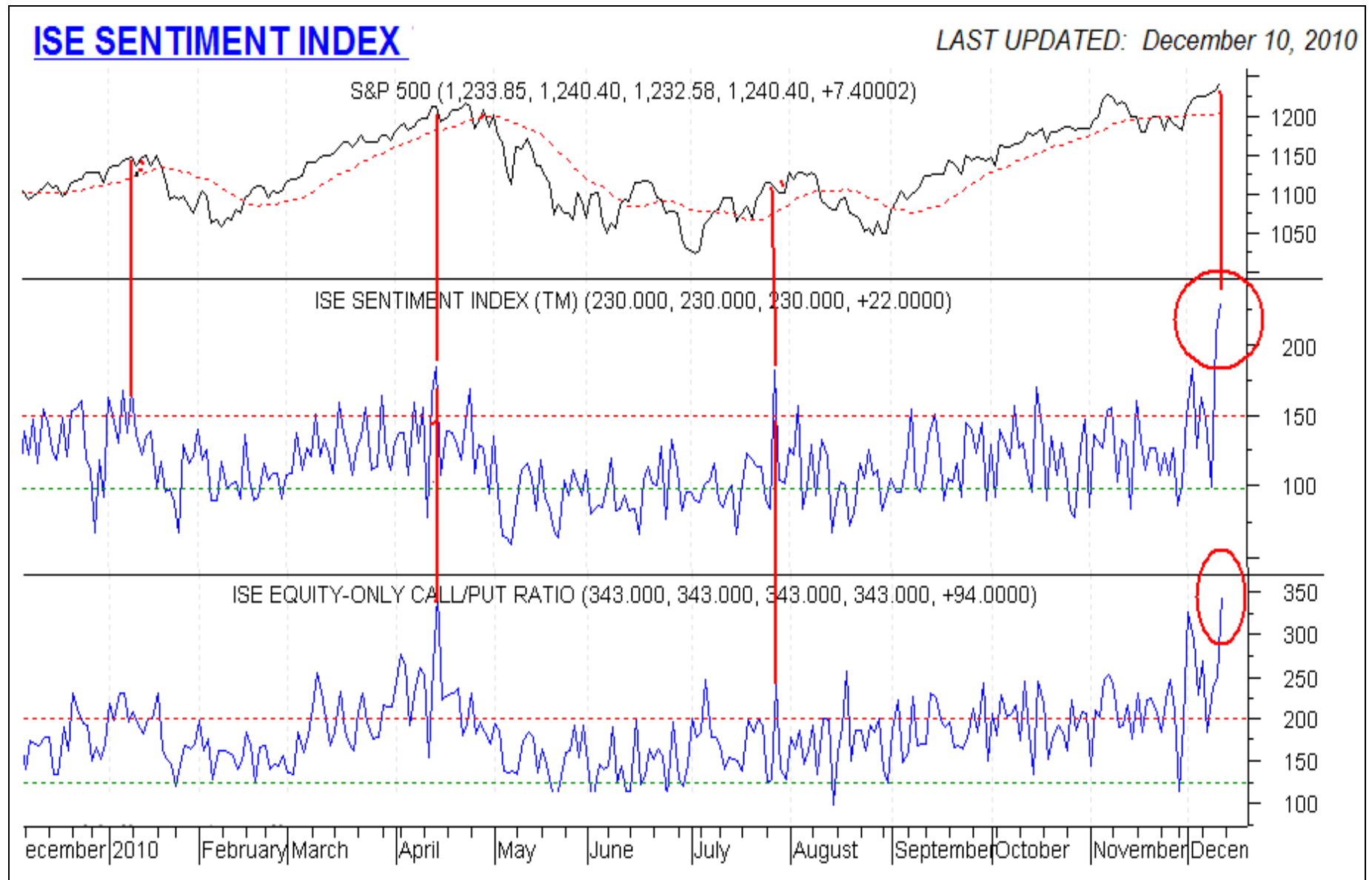
Based on current market condition and the probability of Indicators we point out the **EXTERME INDICATOR ONLY** as a observation points.

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.**

Sentiment Extremely Bullish - ISE

Reported by CFTC from Traders Sentiments



Sentiment Extremely Bullish - EXTEREME INDICATORS TALLY

Reported by CFTC from Traders Sentiments

We've seen in twice so far in the past year, right before the January and April peaks.



- Global Market Analysis for SPX – POM clues – FTSE, CHINA, AUSS

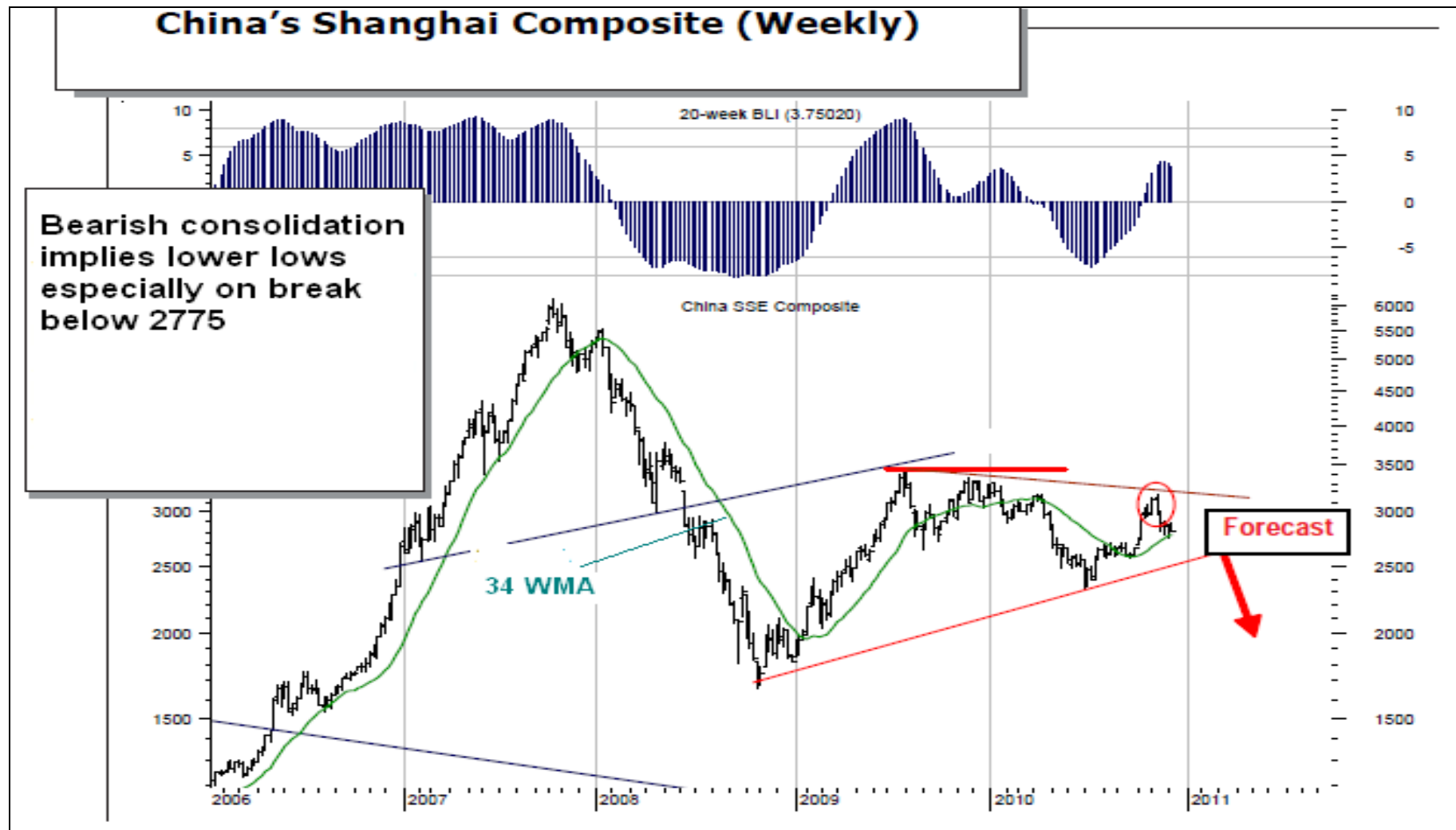
FTSE

Bullish divergence at the last low but diverging again (see the notes within the chart)



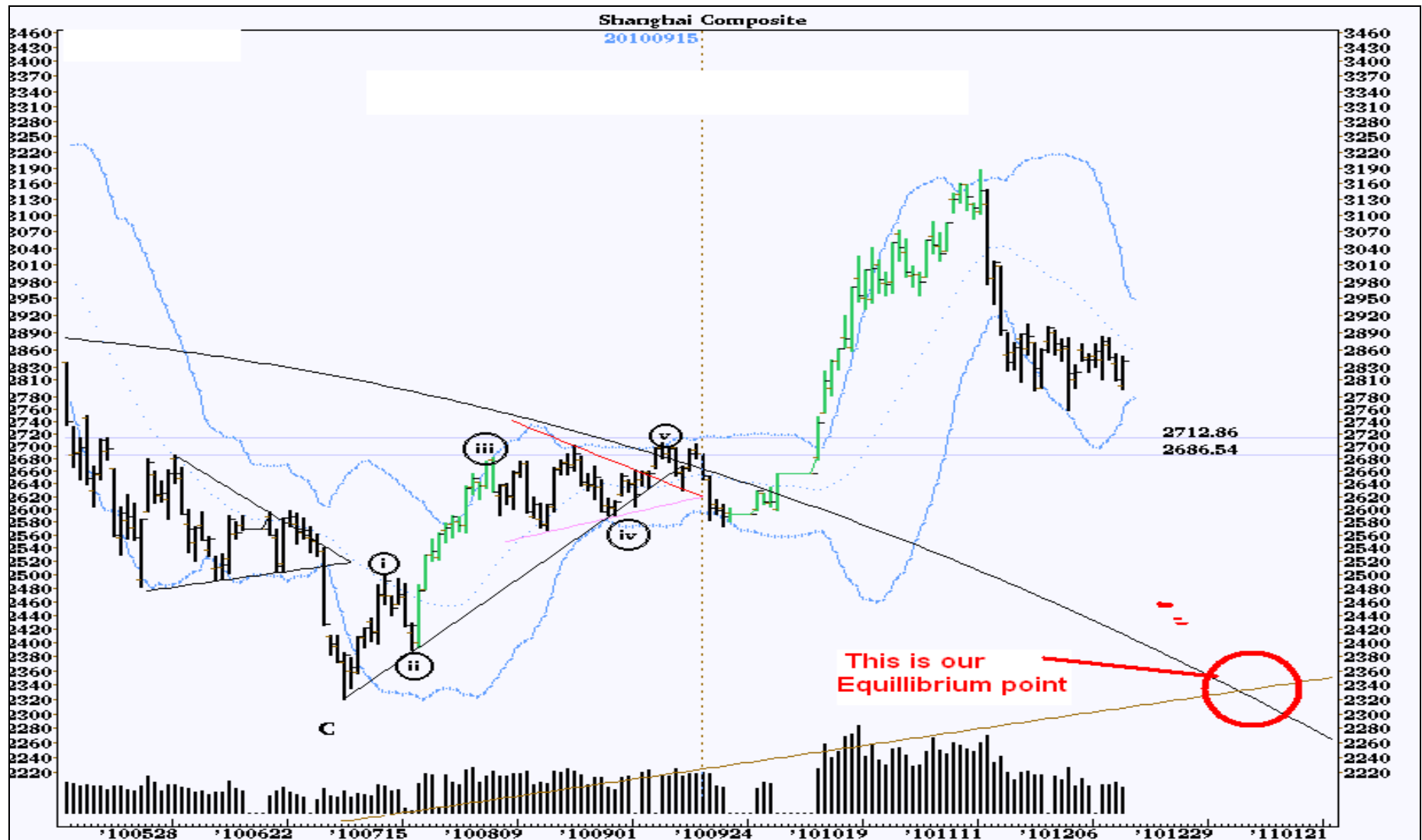
CHINA – MID TERM

China's Index has formed a lower high, and it formed it on a key reversal lower. But our real concern comes with a breakdown below the 34-wma. History has shown that breakdowns or violations confirms lower. The consequences for the world economy of a China hard landing haven't been taken into account yet; nor have they been considered other than by a few savvy Investors. Certainly we'll focus more upon this, for it could very well interact with a European sovereign debt problem/US sovereign debt problem to create the "perfect storm."



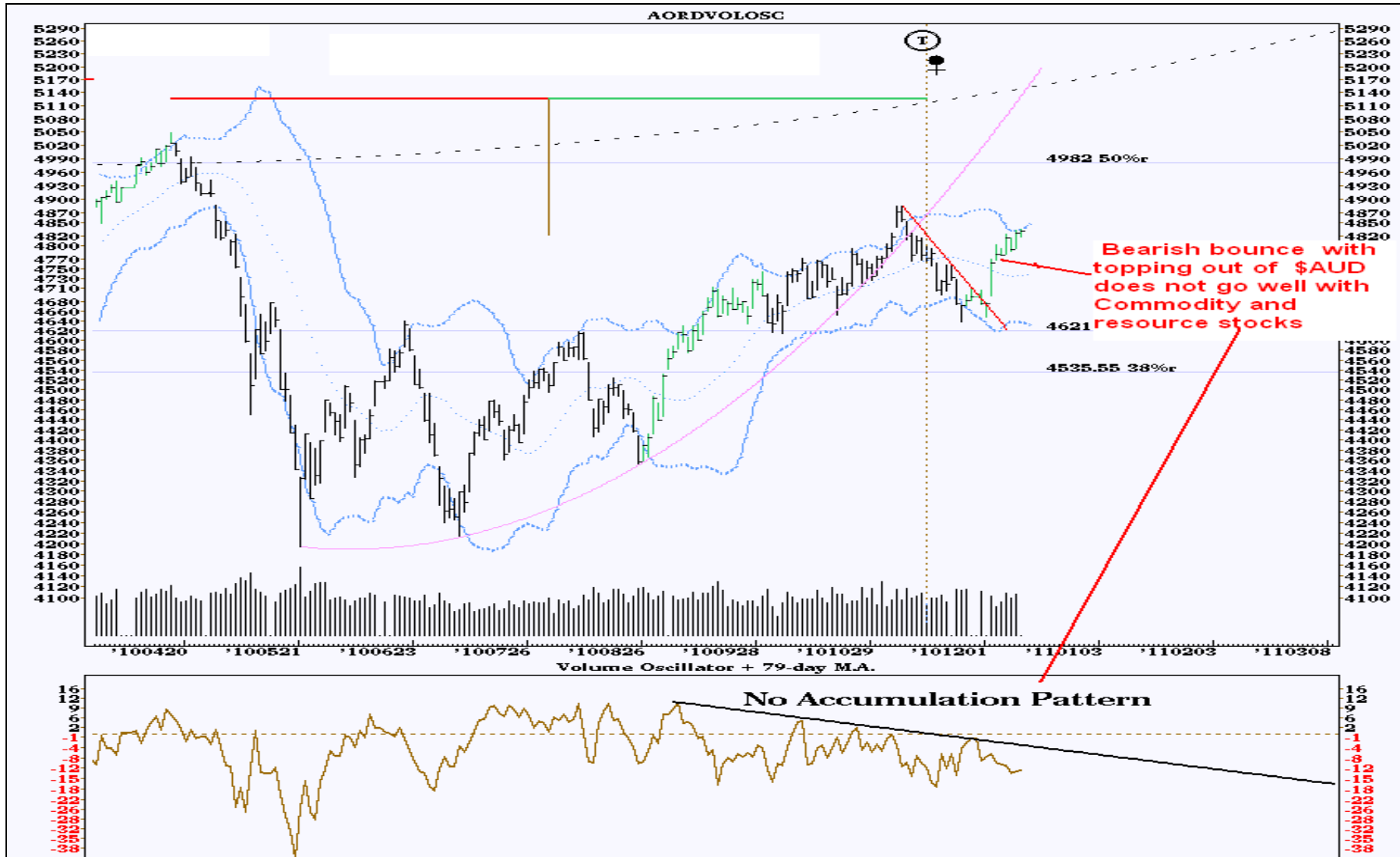
CHINA

It appears that China may find a short term bottom here and rally back. However, if it drops below the prior high at 2705, it means that a major decline is likely. A confirmed downtrend in China would negatively impact many markets, with Australia being a key impact (See below)



AUSS

There is no accumulation here , No QE-2 . This market is way away from upside breakout. The last bounce has been bearish. This does not go well with Commodity, China market and AUD \$.



Appendix

• 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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