

GETTING TECHNICAL

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The Scale Is Tilting Toward the Sellers

By MICHAEL KAHN

Chart resistance levels and other signals suggest that the stock market is ready to turn downward.

PICKING TOPS AND BOTTOMS is always a risky game, and I have learned that the hard way. But finding likely places for those tops and bottoms to occur is still a worthwhile exercise.

Two weeks ago, I wrote here that a 1213 trading level for the Standard & Poor's 500 would be the place to expect a pickup in selling pressure (see Getting Technical, "[Fuzzy Lines and the Big Picture](#)," April 7, 2010). As of midday Wednesday, the S&P 500 was trading at 1202.

Looking back on the charts, it was the final chance for investors to exit the market in September 2008 before the bottom fell out. In technical lore, it now represents a place where investors who "rode it out" get a second chance to get out before, in their minds, a market swoon takes place again.

To be sure, it is far from a guarantee of anything. It is just a look into the psychology of the market, which, in this case, has started to show a reluctance to accept good news as an excuse to rally. Poor performance on good earnings, for example, suggests that the news was already baked into the market; only extremely good news would get the bulls excited.

For example, of the notable companies that reported better-than-expected earnings over the past week, a good deal of them saw their stocks lower in price shortly after the news was released.

There were exceptions, of course as [Citigroup](#) (ticker: C) and [Apple](#) (AAPL), to name a few, were up nicely. Many, however,

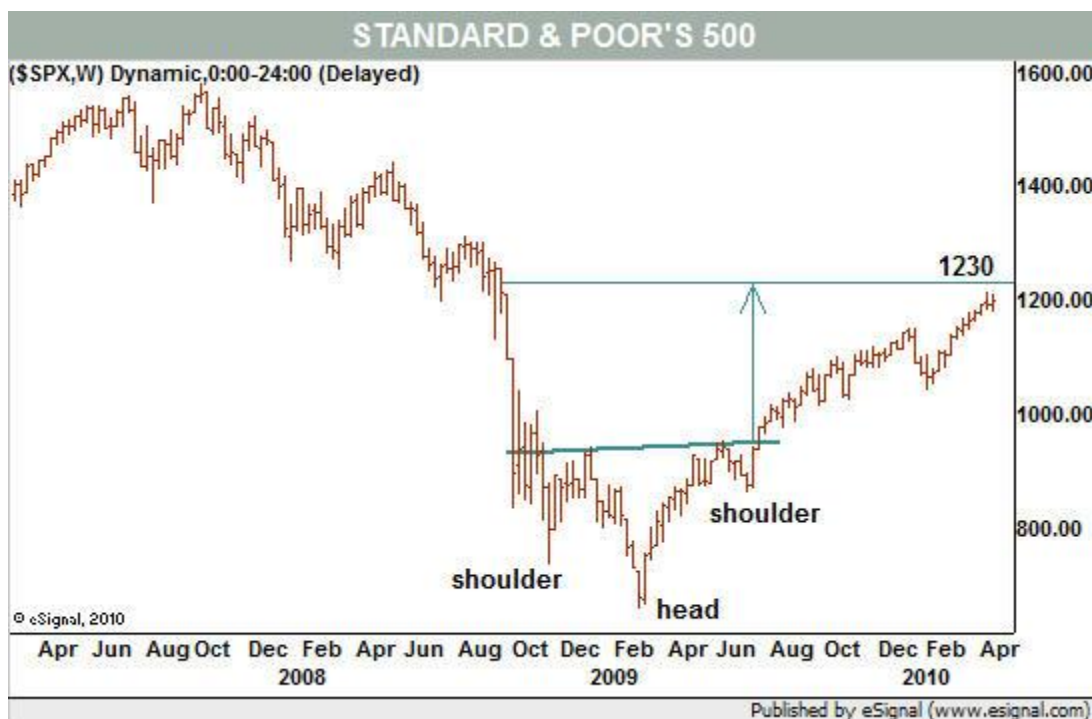
were lower and the list includes [International Business Machines \(IBM\)](#) and [Bank of America \(BAC\)](#).

On the charts, there is another reason to look for an increase in selling pressure. By measuring the size of technical patterns, we can get an idea of how far prices can move if and when those patterns are broken. The theory is that investors get used to the size of swings within the patterns and expect the same size movement once the patterns end.

For example, if a stock traded between 50 and 55 for several weeks and then moves above the top of that range, investors look for a price target of 60. The five-point range translates into a five-point upside target.

For the S&P 500, the March 2009 turnaround became the center of a large reversal pattern. Even novice chart watchers will see an inverted version of the ubiquitous head-and-shoulders pattern between September 2008 and July 2009 (see Chart 1). The top of the pattern, or neck line, was at 950, in very round numbers.

Chart 1



By measuring the height of the pattern and projecting it up from the breakout point, we get a target, again in round numbers, of 1230. The measured upside target coincides with standard chart resistance within a reasonable margin for error and that increases its significance.

The Nasdaq presents a slightly different picture but it is also in an area where selling pressures could build (see Chart 2).

Chart 2



The November 2008 and March 2009 lows formed the base of a "double bottom" or "W" pattern, and we can measure upside targets just as well from it. One phenomenon I have found is that measured targets tend to occur at integral multiples of the pattern height. In the stock example above, that would suggest targets of 60 and 65.

The Nasdaq's second target is roughly 2465. As mentioned two weeks ago in this column, a selling zone exists at 2550, again a price level where sellers became active in the past. With current trading smack in the middle of these two levels, it would be

reasonable to expect the trend to run into problems, and indeed it did last week.

The bottom line is that most major stock indexes are now at or near levels where the balance between buyers and sellers can change to favor sellers. It is no guarantee of a top, but investors should be aware of the rarified air in which they are operating.