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TheMarketMessenger.com turns two years old in a week and, in commemoration of the event, we've been offering a Free Pass for the period Jul 6 - Jul 20, '09 ...

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The Free Pass expires on Jul 20, which means that you still have five days to make use of this opportunity. So don't wait any longer and, if you haven't done so already,

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## Head & Shoulders Tops Obliterated

*The following article was provided as part of an extended Nightly Commentary piece in our Members Area, last night...*

For a couple of weeks, the eyes of the trading world were on a head & shoulders top that had developed on the minor trend of the broad market indices. There was a break out of the pattern early last week. In the 3 days that followed, no follow-through had resulted. It was only a matter of time, most had thought. A new week was set to begin, earnings season was about to get into full-swing; it had seemed like a further drop was virtually inevitable.

Three days into the much-awaited week, not only has the H&S top on the minor trend proven false, but it has virtually been obliterated. The markets, which had taken around 5 weeks to trudge towards the lows of the minor trend correction, have taken just three days to recover around three-quarters of the losses.

With the broader indices now not far away from minor and/or intermediate highs, it would be easy for the trader who does not have a keen realization of history and of the charts to be gung-ho about this action, lay all his/her cards on the table and jump onto the bulls' bandwagon no-questions-asked.

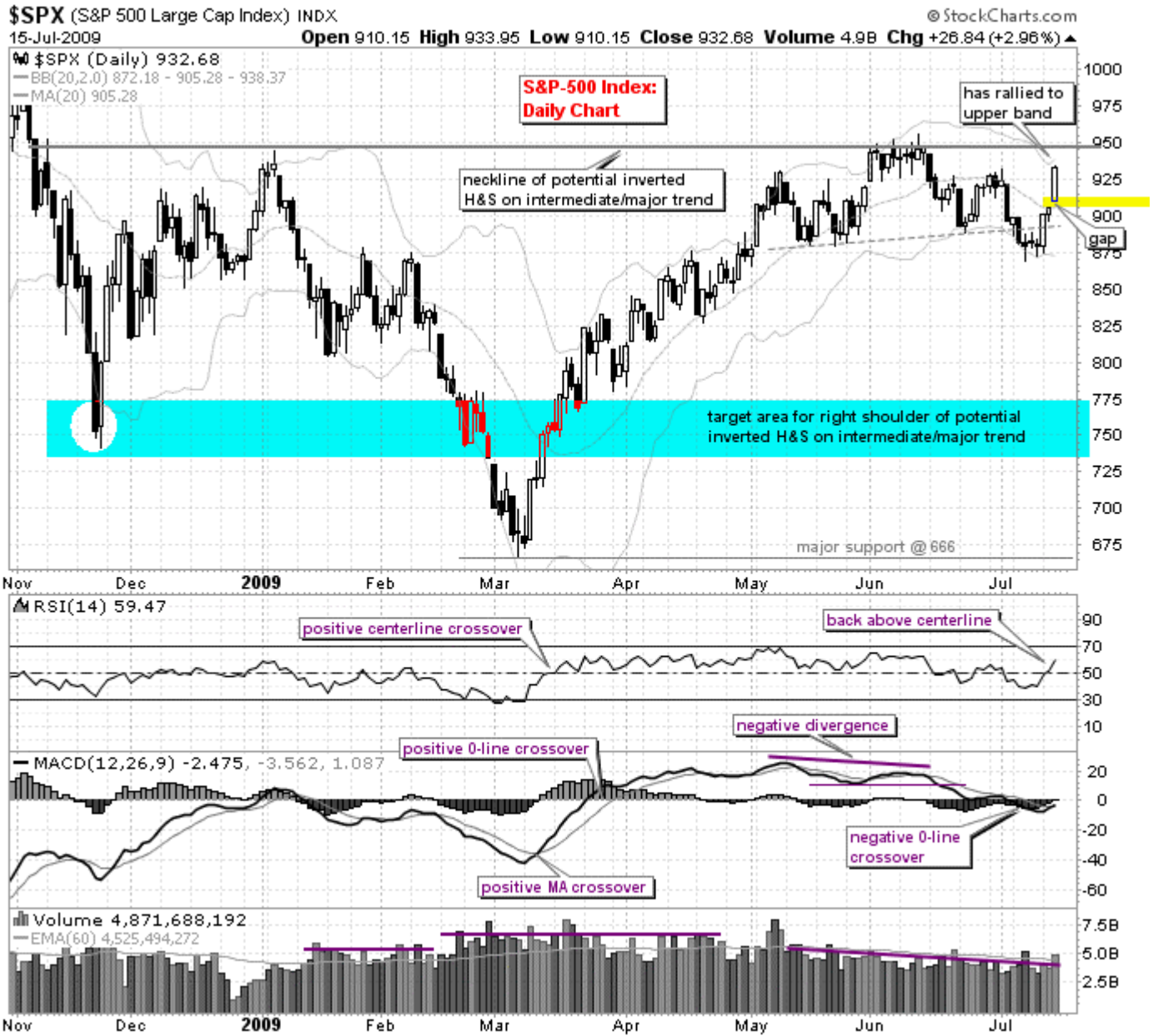
In tonight's commentary, we'll lay out a couple of reasons why expecting a continuation of the rally over the short-run might be a setting up for failure.

Make no mistake about it, our long-term bias is for a big rally that will eventually recover a good portion of the bear markets losses over the next 6-12 months. In fact, we believe that within a year's time, indices such as the S&P-500 and the Dow could quite likely be trading at twice the levels at which they were trading at the lows, earlier this year. However, we're not completely convinced that there will not first be a decent correction of the rally from the March lows.

In line with our **long-term bullish bias** and **short-term neutral/bearish bias**, we've provided around 12-15 long-term trading picks, tonight. (You'll have to sign into our members' area and access tonight's [Nightly Commentary](#) in order to view the picks. So if you're not currently a member, please take the opportunity to [Sign up for YOUR FREE PASS](#) and do so).

Without further ado, let's start with the charts of the indices...

S&P-500 Index - Daily Chart...



After today's nearly 3% gain, the S&P-500 has - astonishingly - rallied from its lower bollinger band to within a few points of the upper band, in three days flat. Moreover, for the first time in this sequence, volumes have been slightly above average. Not only has the all-important 20dMA been taken out (obviously), but RSI has moved back above its centerline and in fact all the way to the 60-line. In doing so, the index has nullified two important sell signals (those generated when prices moved below the 20dMA and when RSI made a negative centerline crossover).

In fact, if you take away the bollinger bands, this looks like a potential buy signal on the minor trend... It may turn out to be such but we'd be very, very cautious of falling for a potential trap. Not only is it important to remember that intermediate resistance at 950 is going to pose a challenge, but it is also important to note that in pushing the index from its lower band to its upper band in one fell swoop, the bulls may have shot themselves in the foot, because the upper band is not (at least for now) rising strongly.

Also do not fail to notice that the index has left a gap on the chart as of today's open. This index rarely, if ever, leaves an unfilled gap on the charts.

As such, there is a good chance that resistance will be found again and that this could end up proving to have been a bull trap. In fact, that is almost exactly what happened during the formation of the right shoulder in the '02/'03 H&S bottom (see chart below).

*S&P-500 Index - Daily Chart - H&S Bottom During '02/'03 bear market...*



The chart above shows the action that took place between June '02 and June '03 on the S&P-500.

Notice the similarities between the current action and that seen during the turn of the year '03 (highlighted area). Notice how the index had retested the intermediate resistance level of 955 or so in late-Nov, before losing ground over the next few weeks, only to then blast off from the lower band to the upper band in just a handful of sessions?

Surely, traders would have been ultra-bullish at that stage as well, only to find the index selling off badly over the next two months before finally forming a bottom, which proved to have been the trough of the right shoulder, in early-March and then starting another huge rally that eventually lead to a breaking of the neckline of the inverted H&S pattern on the major trend...

Could history repeat itself? Don't be completely surprised if the markets start to roll over again, before perhaps putting in a bottom for the ages, several weeks from now...

S&P-500 Index - Daily Chart - *current action (potential H&S Bottom) projected paths...*



Over the weekend, we'd shown you a chart that provided a projected path for the S&P-500, assuming that the index was trading within a large inverted H&S pattern (as it very often does when forming long-term bottoms). The original projection is shown in red in the chart above.

The action that has taken place over the past couple of sessions has brought about the need to alter the projected path. While no one has a crystal ball that gives a perfect idea of what is to come, one can make educated guesses.

Assuming (and, once again, remember that these projections assume that an inverted H&S-type formation is taking place) that the index is undergoing formation of an inverted H&S pattern, the most bullish of projections (green line on chart) would be a case wherein the index has nearly finished forming the right shoulder of the pattern, goes on to break the neckline within the next few sessions, and thereafter moves towards the target of 1245+. Traders with long positions would love for this scenario to play out of course. However, if it does, it will leave a lop-sided pattern on the charts (remember that H&S patterns typically need to display some sort of symmetry between their left and right shoulders). If a breakout is imminent, it will leave a right shoulder that not only lacks a depth, but also a duration that would show symmetry with the left shoulder.

If, on the other hand, the index follows a path similar to the '02/'03 bottom, we'll soon see a move back towards the 750- level, before the final bullish reversal takes place (sometime in August), and thereafter a testing - and perhaps a breaking - of the neckline sometime in September. The blue line on the chart above, depicts this projection.

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Okay, a few of you might be thinking "these guys are only laying out the bullish scenarios; what about the possibility that there will be a move to new major lows below 665 on the S&P." Here's our response to that line of thought...

While traders need to be prepared for the worst, sometimes it is best to take things into perspective and arrive at an understanding of what exactly the "worst" scenario is...

For example, we like to ask ourselves the following question from time to time: "*Would we regret it more if we were to miss shorting before a xx% drop, or being long during a xx% rise?*"

Now, if the xx in any given circumstance were to be small, say 5-10%, we'd probably not been too perturbed with one outcome or the other. However, if the expected move were to be large, say 50%+, then it's a different matter altogether.

Why is that important in the current context? Look at it this way... Say the index were to fall to 750, over the coming weeks. Put yourself in the situation of possibly being on the wrong end of a 500-pt (66%) rally over a 6-12 month period thereafter (moves of such a magnitude -or larger - have often taken place after the handful of 50%+ declines in the major indices over the past century)...

Only once in the last century has there been a bigger decline than the Oct '07 to Mar '09 decline in the U.S. markets. Given that the move in question came during the "Great Depression," it should be ignored for now. Based on current evidence, as bad as things may seem, one would have to be a conspiracy theorist to assume that we are facing another Depression and, therefore, that the indices will fall much below their March-lows, which marked a 58% decline from the Oct' 07 highs. (That is not to say that they cannot. It is simply a statement that reflects that the odds for a further drop, especially of a sustained decline, are not great.)

In a nutshell, we're of the belief that holding onto a core position of long-term bullish positions would be a wiser choice than say long-term bearish positions. And any bearish positions should be of a short-term nature, with a tight leash kept on any such bearish positions.

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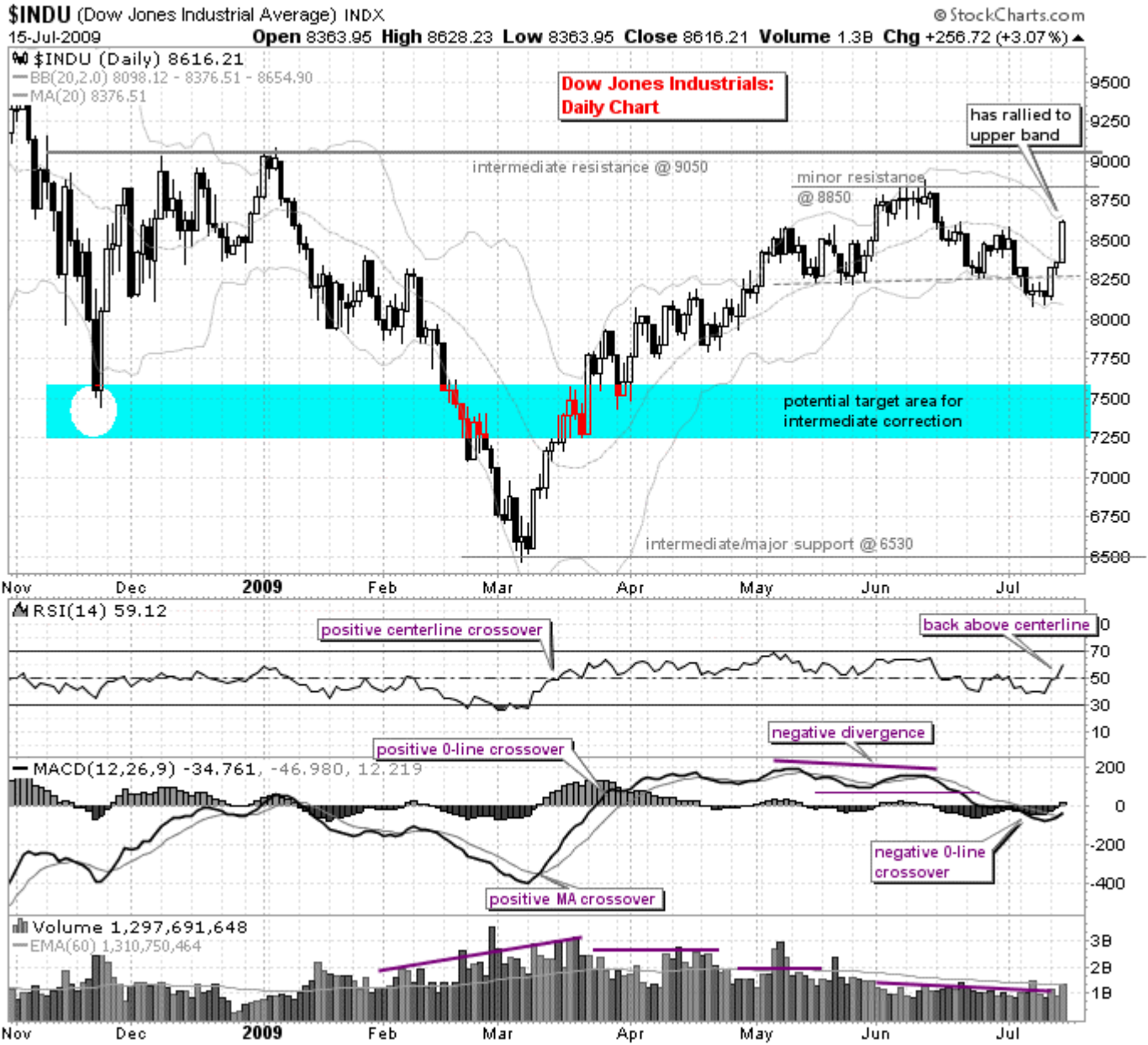
In line with this outlook, we've provided a good number of trading picks that have a 3-12 month horizon in tonight's commentary.

(You'll have to sign into our members' area and access tonight's [Nightly Commentary](#) in order to view the picks. So if you're not currently a member, please take the opportunity to [Sign up for YOUR FREE PASS](#) and do so).

Let's now take a quick look at the daily charts of INDU and NDX...

[continued on next page..]

Dow Jones Industrials Average - Daily Chart...



While the Dow has also blasted through its 20dMA on decent volume, and has seen its RSI reading move back above the centerline, one cannot ignore the fact that the index has smashed up against its upper band and, as such, should find resistance over the near-term. The bulls will be given the benefit of the doubt as long as prices are above the 20dMA, but to assume that the minor trend is anything other than neutral at this point, would be a little adventurous, if nothing else.

[continued...]

Nasdaq-100 Index - Daily Chart...



NDX gained 3.3% today and, as with the other indices has not only blasted past its 20dMA but smashed straight into its upper band. Interestingly, the index showed volume levels well above average for the first time in several weeks.

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That's it for this issue of Purely Technical. Don't forget to [Sign up for YOUR FREE PASS](#) if you haven't had the chance to do so already. There are only 5 days left on the Free Pass Offer...

Have a great weekend!

Asher Pinto

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