

Fishing for a bottom

We are fast approaching (if not already 'in') an opportune moment to be buying stocks with a timescale for holding of 6 months or less. The last two weeks have seen few (if any) stocks drawn from my "Breakout scan", a strong sign that an intermediate term bottom is in place. Looking at the side-by-side performance measures (Table 1), one can see parallels from May of this year with August 2004 and October 2005.

In table 1, the top tier reflects the performance of my Breakout picks (left three columns) and my Gold member picks (right three columns) for the periods of August 2004, April 2005, October 2005 and May 2006 (current). Plays highlighted in white, or labeled "-100%" are still in play and have reached neither stop or target price. Beneath each trade performance period is the NASDAQ performance for this period.

It should be added, the trade performance for my Gold Member picks for August 2004 is undermined by the high number of short trades recommended at this time. If these losses were reversed so as to reflect "buys" then long side performance would have been substantially improved. However, I left the returns 'as-is' so as not to confuse matters. Gold member picks performed significantly better in April and October 2005.

Given the parallels, what should one be looking for in the market:

- The clearest signal to go long has come on a 'buy' trigger in the MACD. Note how both "Breakout" and "Gold Member" stock performance improves after this signal is made and how a corresponding 'sell' trigger is seen as a good time to stick with what you got and be cautious on entering any new positions.
- Near term slow stochastics [14,3] are the first indicator to signal a bottom. We can see already, that this signal has been given for the NASDAQ in May 2006. However, it is prone to whipsaw as occurred in August 2004 and April 2005 and one must treat this signal with a measure of caution.
- A significant retest of recent lows may not occur; in 2004 there was a small doji at 1,840 which was the extent of the retest of 1,750. In April 2005 a new low was completed on a bullish hammer. In October 2005 it was a higher low on a bullish harami at the 200-day MA.
- The three main moving averages: 20-, 50- and 200-day MAs are an important reversal point for a correction from the initial bounce. In August 2004 the 50-day MA was support on its first pullback. In April 2005, the 20-day MA was the resistance area for the bounce. In October 2005, the 50-day MA marked the pullback point. In May 2006 it could be the 200-day MA or the 20-day MA; watch action at these averages closely.

What of expected returns?

Figure 2 gives the average returns for each day after “Day 0”, i.e. the first day we see a series of three “x”s in the “Breakout” stock columns (not the “Gold Member” columns), for August 2004, April 2005, October 2005 and an average for the three months combined.

Looking at the average return for all three periods, one can see the best performance from stocks inside the first 30 days from “Day 0”, with “Day 12-Day 22” perhaps the best time to be buying stocks. If one is to translate this to May 2006, “Day 0” falls on May 18th, putting Day 12 on May 30th and Day 22 on June 9th. If there were only one time in the year to buy (well, likely two given the frequency of these set ups), then the next couple of weeks could be it (due diligence needed of course).

Leadership shapes up early in a market, well before the crowd gets involved. Don't ignore stocks which pop up at new highs (n th day or 52-week) over the next couple of weeks. Be nimble, don't be afraid to cut loose one position to go looking for another. There is no shortage of negativity out there and talk of a repeat 1987. Such events may, or may not occur – but when markets present up bargains they should be bought. If the bounce unravels then the risk taken at this time will be low (due to the proximity of support).

Best bet now is to wait for that all important MACD trigger “buy” in the NASDAQ.

Figure 1. Top tier shows individual performance of “Breakout” stocks (left column) and “Gold Member” stocks (right column) over 2-months. The time of reference is the first day my “Breakout” scan drew no candidates, as marked by the series of “x” on a grey background. Lower tier shows the NASDAQ performance for these time periods.

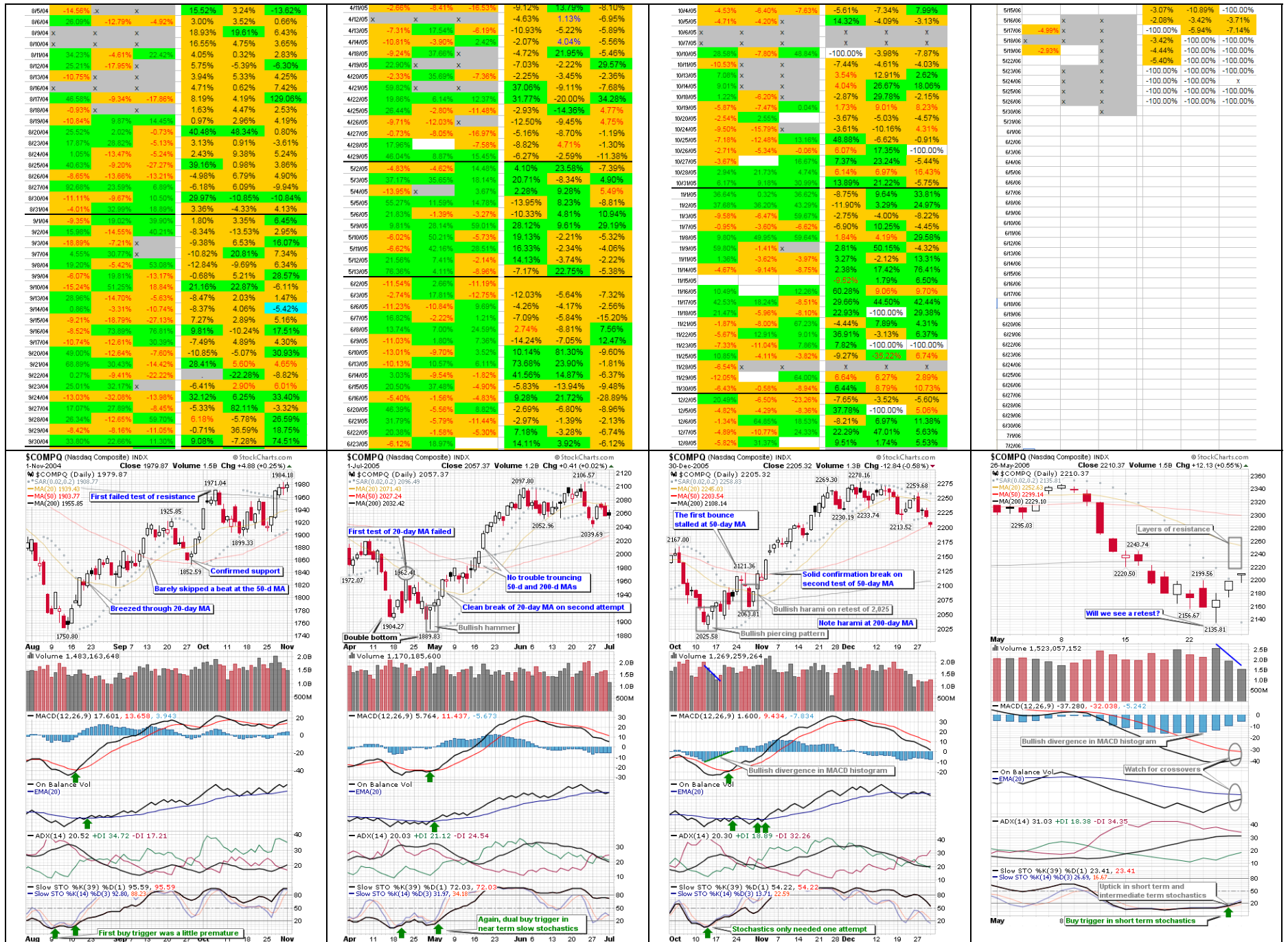
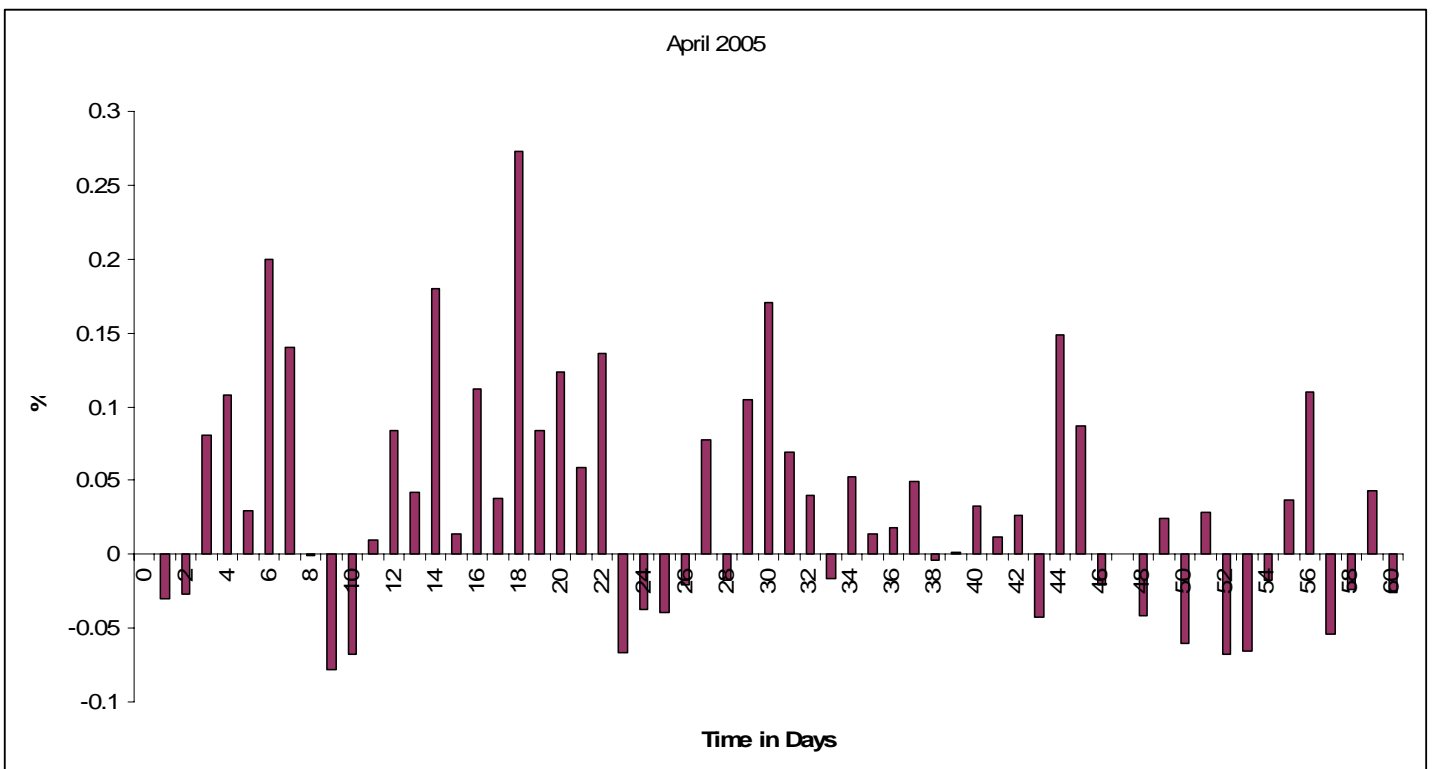
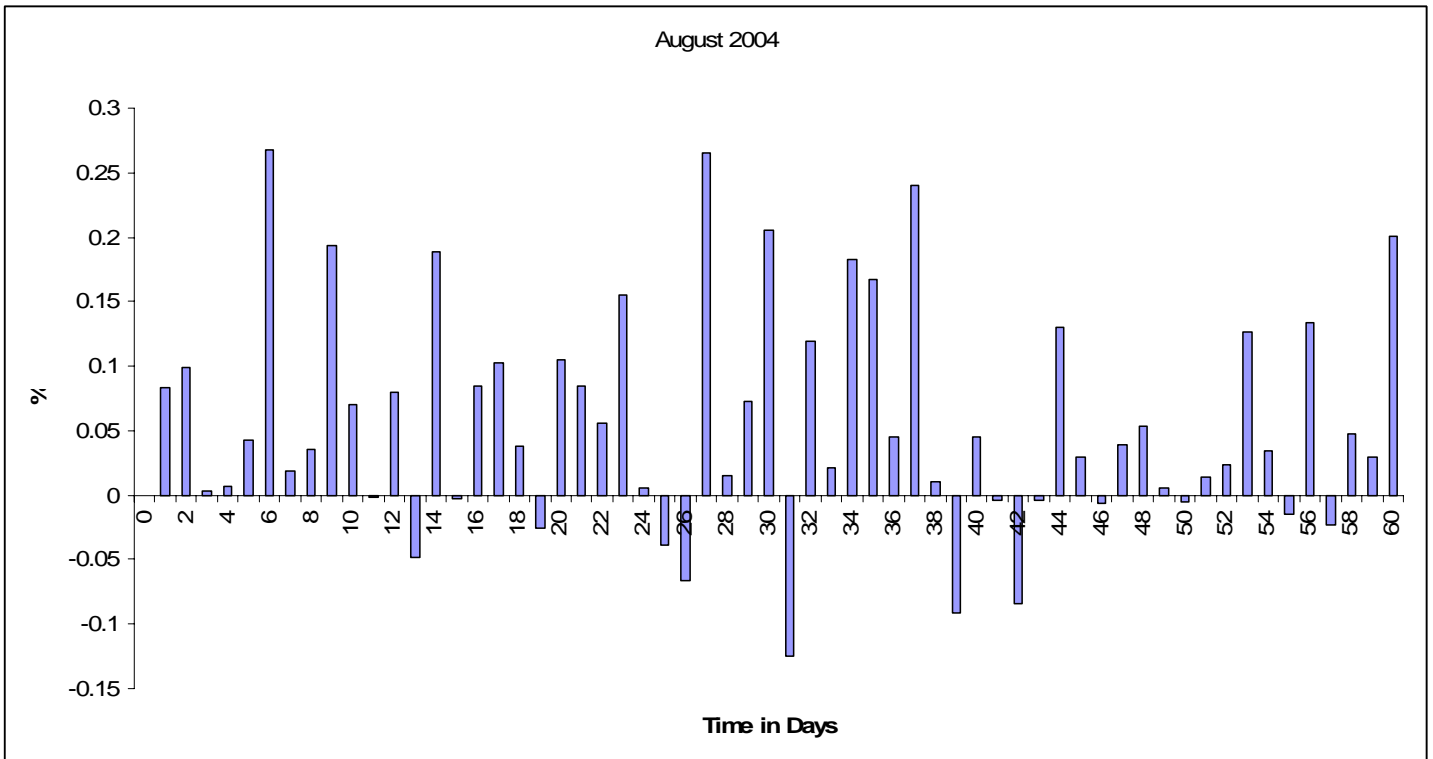
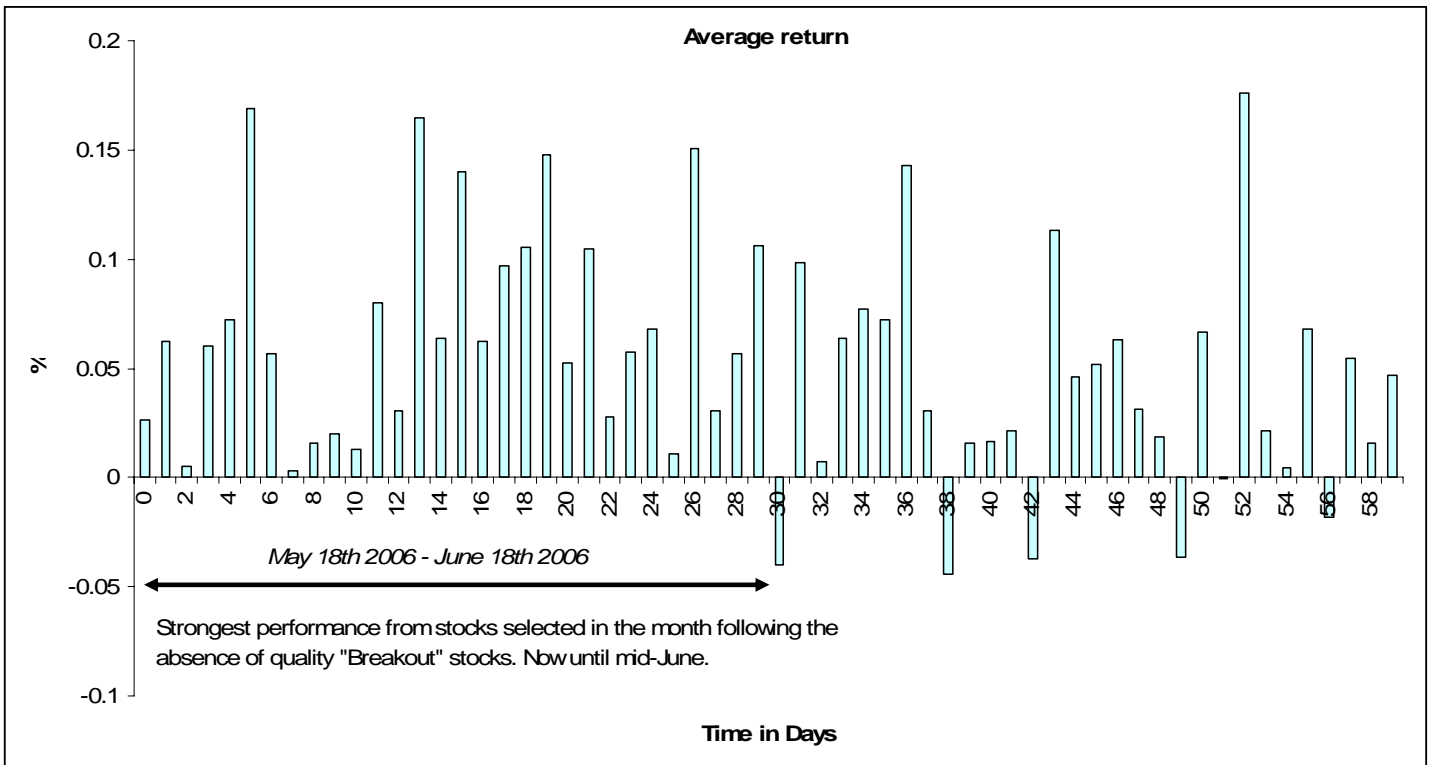
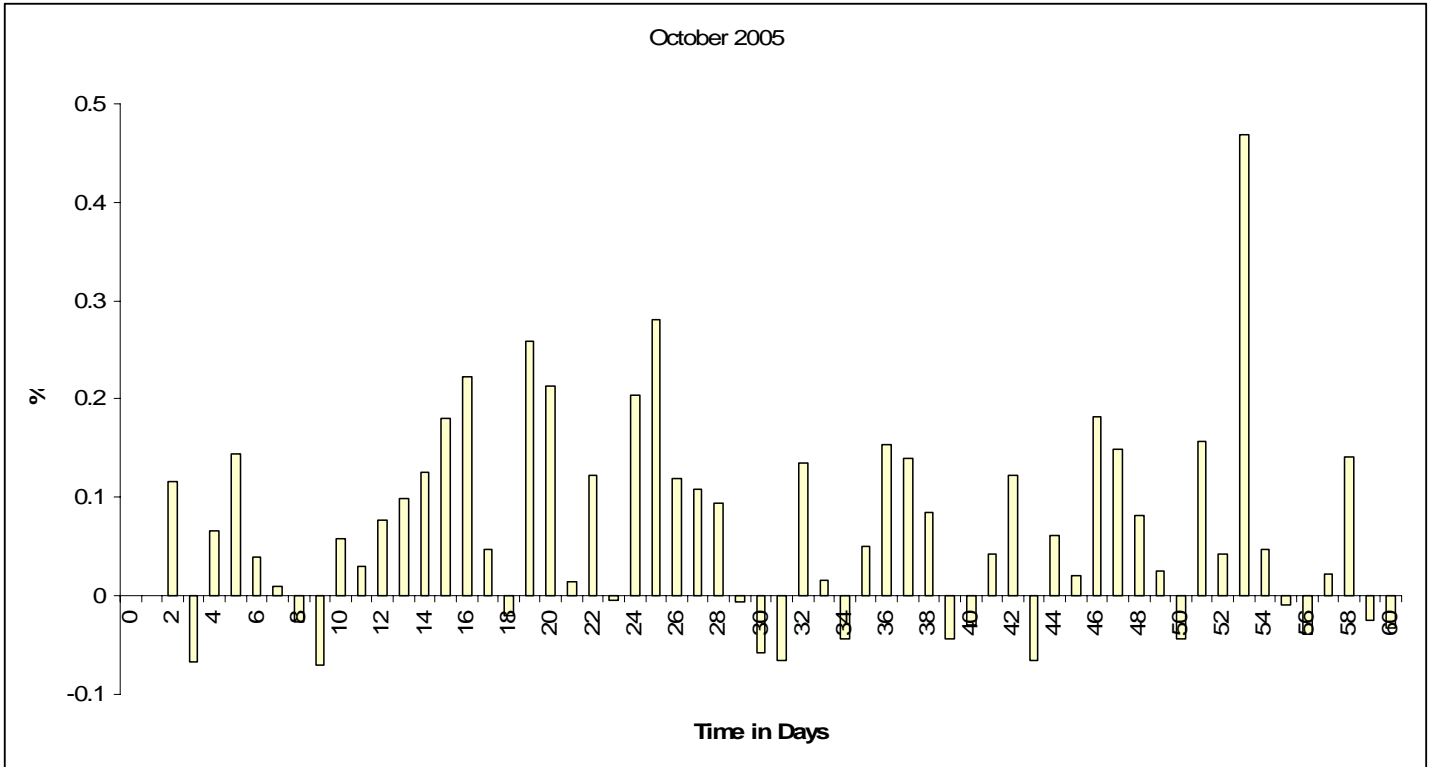


Figure 2. Average % performance/return per trade, of Breakout and Gold Member picks combined, for each day after the first series of “blank” Breakout plays. “August 2004” is represented by August 9th 2004; “April 2005” is represented by April 12th 2005; “October 2005” is represented by October 6th 2006. The current count starts from May 18th 2006; how will it pan out? An average return is presented for the three aforementioned periods.





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