SMI The Trend Letter

Friday, January 15, 1982

MARKET TRENDS

Since early December, the market as measured by the Wyckoff Wave has been losing the positive tone it had prior to that. First there was an extended period early in December when the Wave tried and failed to break out of its trading range on the upside. This was followed by a drop back toward the middle of the range, which gave the previous failed attempt the appearance of an upthrust. This negative indication was confirmed on January 5 when an effort to resume upside progress was decisively turned back. Since then, the Wave has been firmly in the grip of a short term down trend, which in recent days has become oversold. In spite of this, trades on the long side even for the short term trader cannot be encouraged. His trend is clearly down and that is the side of the market he should trade. The current oversold position should be used as an opportunity to lock in profits already established.

Longer term traders and investors are likely to be viewing the action of the past month and a half with concern, but panic is not yet in order. Whenever the market remains in a trading range for a relatively long period of time and is unable to make the break in the direction that seems indicated by the action, it becomes vulnerable to some type of important test that will prove whether or not the market has been making its efforts in the right direction. Often this is a shakeout, but it must be an important effort in the other direction that fails to gain the following needed to get a sustained move in the direction of the test underway.

What we have seen during the past two weeks on the downside could be called a shakeout, but this seems to be stretching the definition. A shakeout normally will hit the market very suddenly and without any warning. Afterwards, the recovery is usually quite rapid. None of this seems to apply to the current reaction. Therefore, we need to look at the other possibility, which is a wearing out process. This will be proven as the Wave returns to the bottom of the trading range. Is there a divergence? Has the downside objective been reached? Is the market oversold? Positive answers to these questions would tend to indicate the end of a wearing out process.

There is one final possibility that should not be overlooked. The recent decline could be a sign of weakness. There has been good downside progress and the volume has remained relatively strong. A sign of weakness is confirmed by a reduced volume rally to a last point of supply. This could be the rally that is indicated by the currently oversold condition. Therefore, it must be watched very closely. Potential previously established in the 2700 area does indicate a substantially lower objective. What we are seeing now may be the beginnings of the second phase of that decline.

STOCK TRENDS

Since our last examination of the issues that make up the Wyckoff Wave, there has again been a substantial shuffling from the standpoint of relative strength and weakness. The two issues that had been the most negative looking a month ago are now the strongest. Those that were the strongest have weakened somewhat, but remain relatively strong from a longer term perspective. If all we are seeing here is a new round of rotation, the general market will remain locked in the trading range. However, if all the stocks can be placed into a negative scenerio in spite of the instances of short term strength, we would be best advised to identify the potential short candidates for possible action in the near future.

Exxon is perhaps the best example of a wearing out action within the trading range. In its slide back to the bottom of the range, this stock is actually ahead of the market. This likely means that its day of reckoning may come sooner than that of the general market. At this point, Exxon is being squeezed by an extremely strong support level and the supply line of a relatively short term supply line. Two downside objectives have already been fulfilled. This fact in combination with the solid support around thirty should help the stock shake itself free from the downtrend, but time will tell. Long positions cannot be advised as yet, but those who have been short on a short term basis should consider locking in their profits.

General Electric is one of those previously strong stocks that has weakened considerably in recent weeks. It is still managing to hold on at an important halfway point, which is positive, but an important support line was broken this week and an obvious down trend has taken shape. The objective of the current decline appears to be between 52 and 54. That suggests the stock will not break the crucial support at fifty-one, but is not yet at the bottom of its current decline.

Immediately, GE should be vulnerable to a rally. This is based on the oversold position within the down trend and the condition of the general market. Should this be used as a buying opportunity? Probably not. It is likely to be only a normal correction in a down trend. The short term trader would do better to look for a rally to fifty-seven and then consider shorting. The longer term person might want to follow the same strategy, but this should be considered only if the rally results in a substantial broadening of the count and lowering of the downside objective.

One of the two stocks that has experienced an amazing turn around in the past month is General Motors. What we need to do here is determine whether the improvement is real, or only a big build up to an even bigger let down.

The most positive accomplishment of the past month was the breaking of the major supply line. Second to this would probably be the development of an intermediate uptrend. Although these are very positive developments, they are not the whole story, which is why this stock cannot be considered an automatic buy. The most

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disturbing development is the action of January 8th and 11th, which appears to be an upthrust and not a breakout. This is made even more disturbing by the action of January 13, which appears to test the upthrust and results in a downside objective of thirty-one. If the market should now try to rally and GM is held between 39 and 40, it should be considered as a short candidate.

I.B.M. is the other stock that has become very strong recently. It still looks good. It is in an uptrend and appears to have a higher objective. The problem here is that the uptrend may be in trouble and the higher objective something that may not be reached. The reason for fearing this can be found in Monday's action, which has all the makings of a buying climax. What needs to happen now is a test of Monday's high that is unable to resume the advance. This would define a new trading range and perhaps lead to the end of the uptrend.

The fact that early strength does not guarantee continuing strength is proven by Merrill Lynch. Up until the middle of November, this stock has been very strong. Now, however, it is firmly entrenched in a down trend. In addition, the downside potential seems to be saying that this stock is going to make a significantly lower low. There is no reason at this point to consider buying this stock. If anything it should be shorted on a reduced volume rally back to the supply line.

Pittston is very similar to Merrill Lynch. It is a formerly strong stock that has become quite weak. It does not appear to be as bad off as MER, however. What makes the difference is the downside objective, which is twenty-one. That means there is only about two points to go, so shorting does not make much sense. The objective also indicates that the important support level should hold. In this stock, the testing of that support is the next thing to anticipate. Any trading at this point seems unwise.

Last time we spoke of UAL as being a major disappointment. Since then that has turned into a major disaster. The critical support area between seventeen and eighteen has not held. This has opened the door to the count at the twenty level being worked out on the downside. Such a development could take the price down to ten dollars. This is an important decline and worth participation on the short side. The place to establish short positions is on a rally back to the major supply line.

Finally, we have UK which is something like General Electric. It is a stock that was strong but has now lost most of this strength. The loss in the case of Carbide seems to have been greater, which makes it less of a candidate for the long side even though it is currently in an oversold position. As we have seen with some of the other stocks, this seems to be a case where it would be better to let the oversold condition be corrected and then consider selling short. The downside objective here appears to be 43 to 44, so short selling is probably only for the short term trader.

INDEX CHARTS

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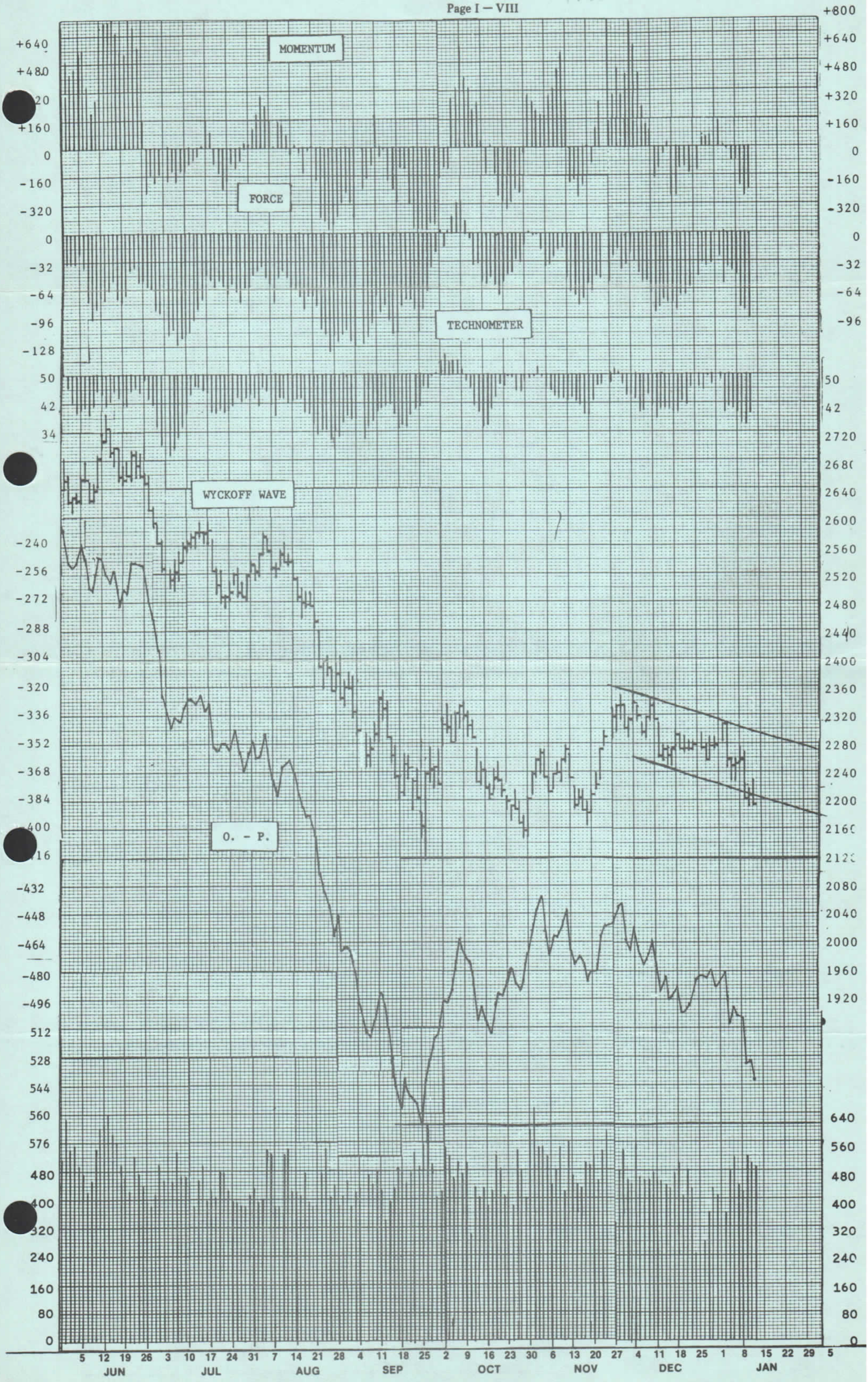

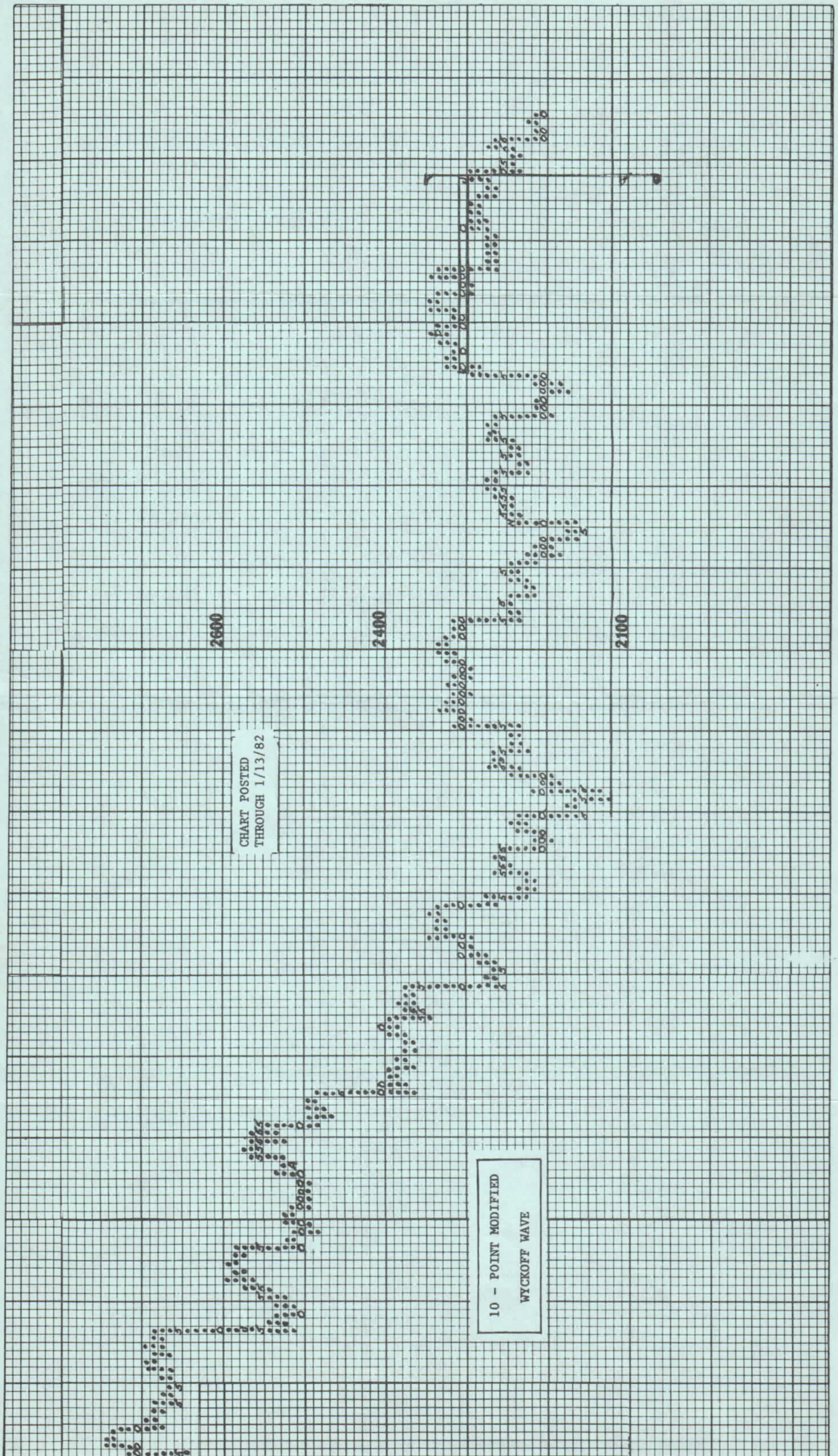
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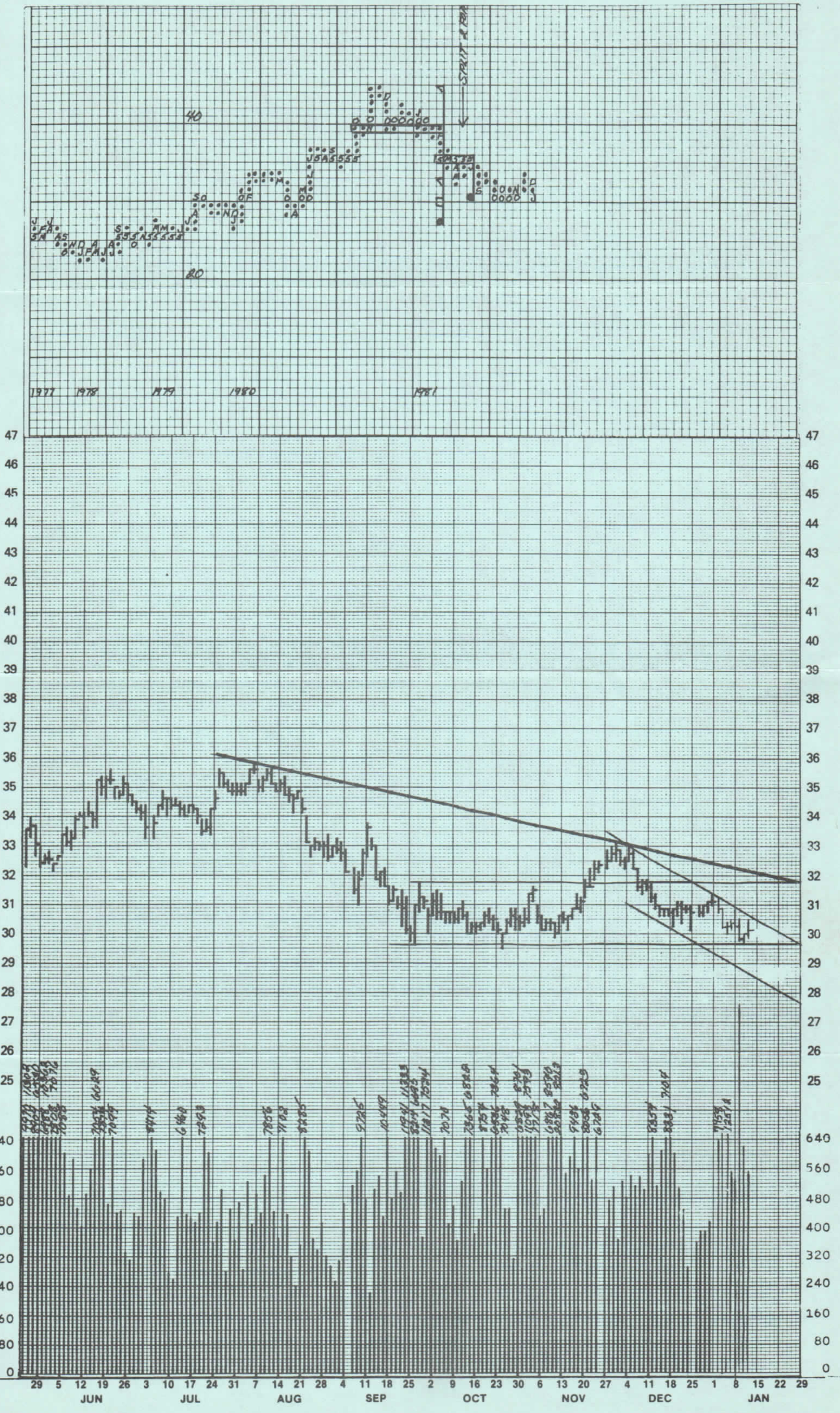

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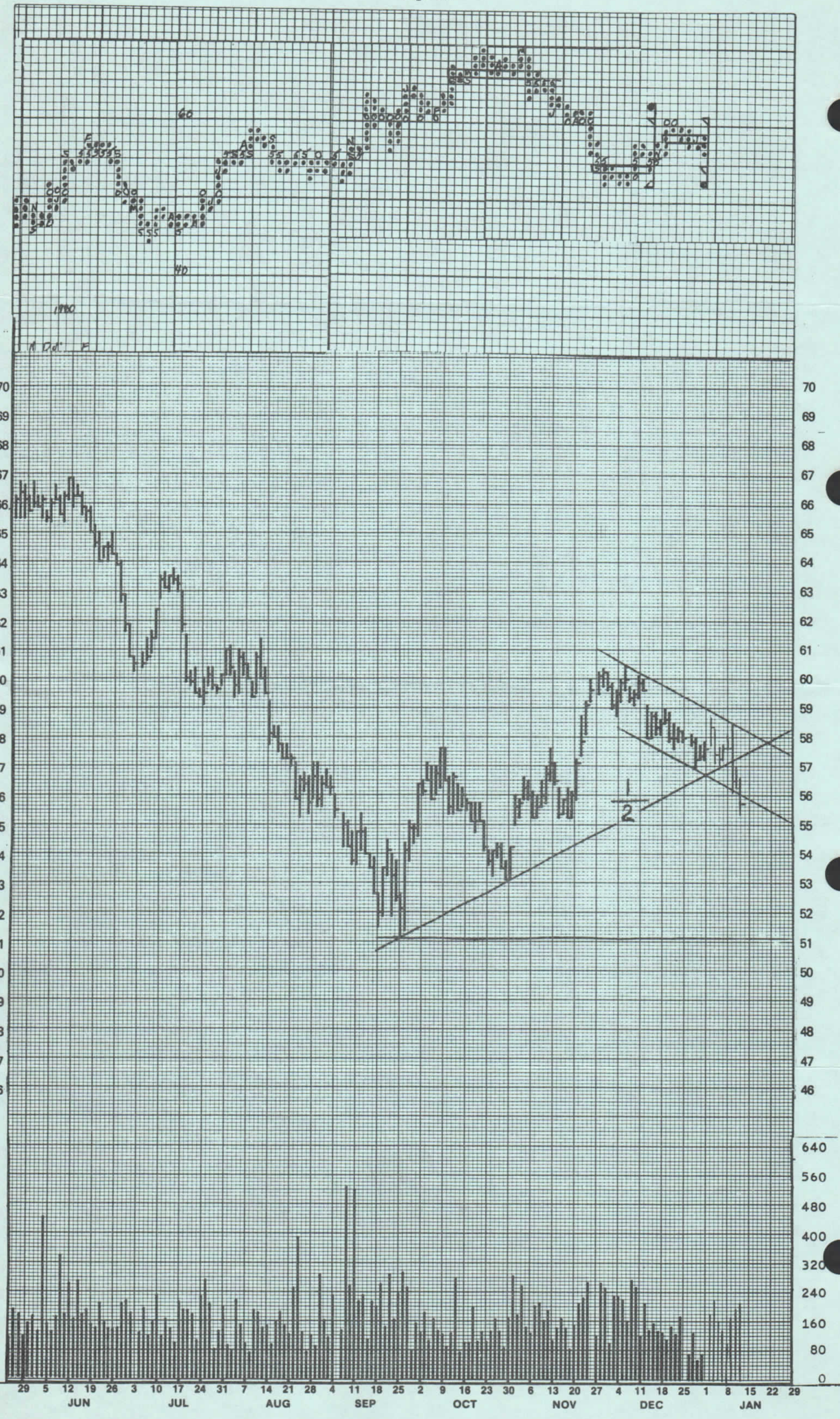

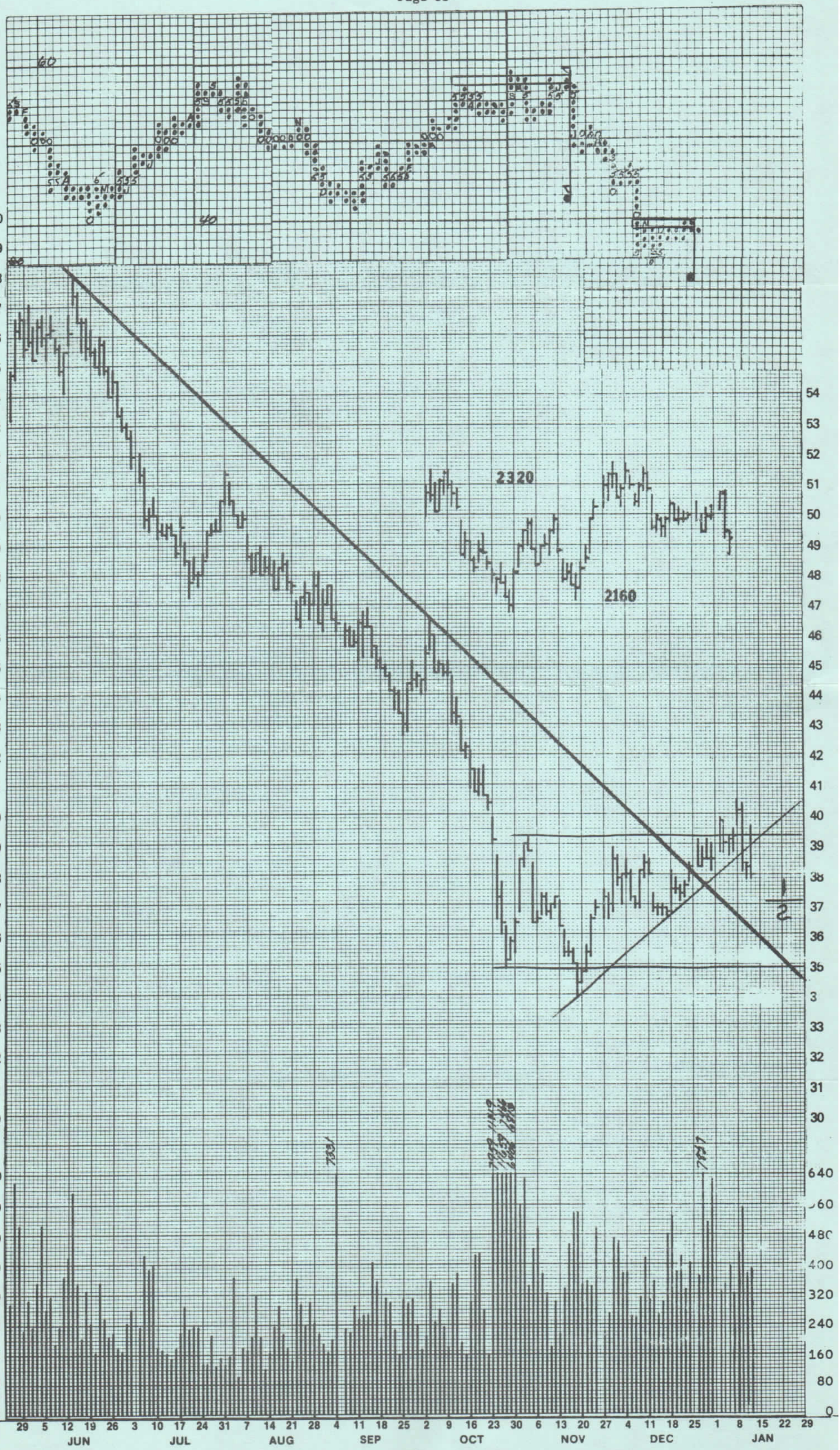
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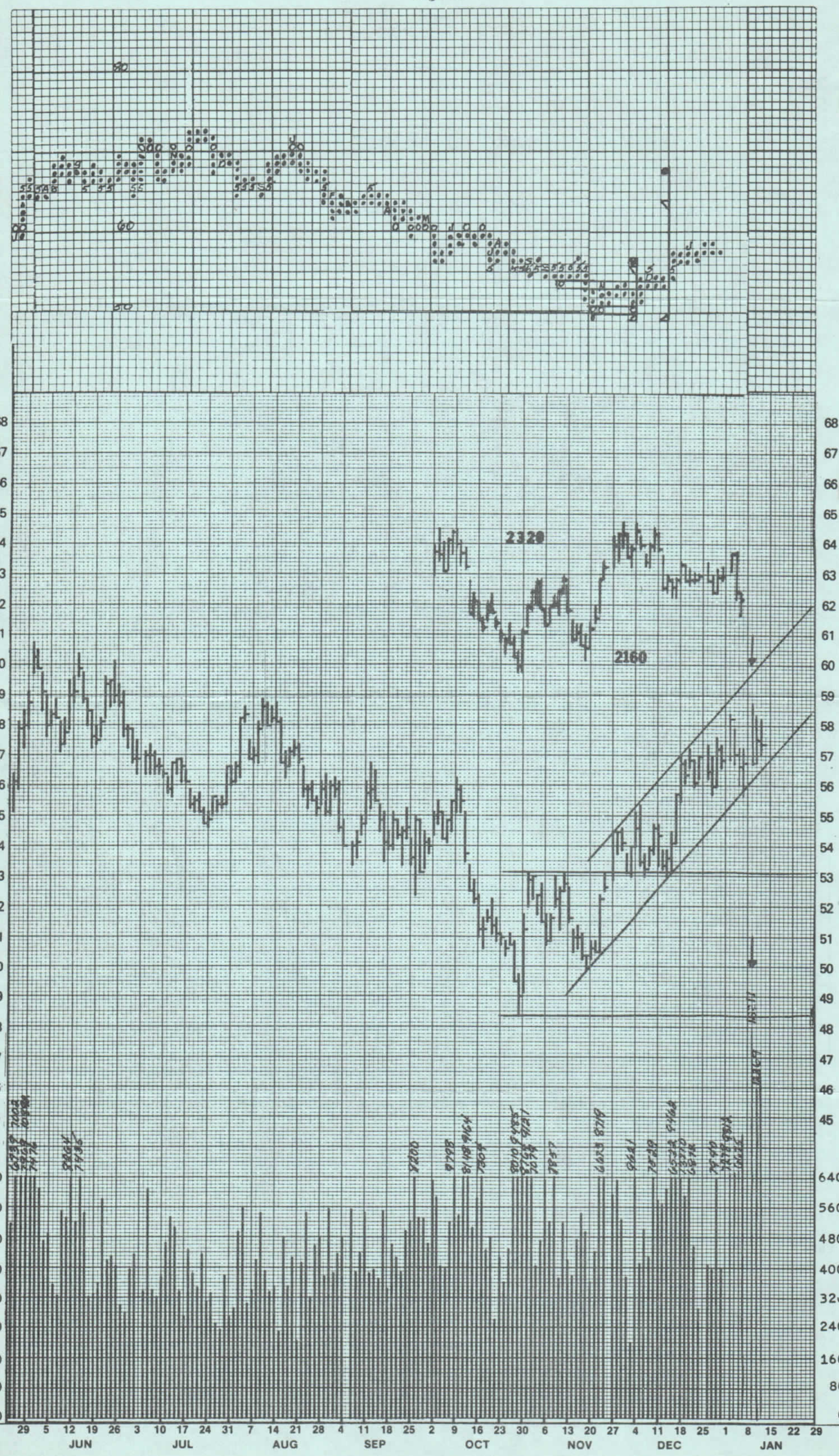

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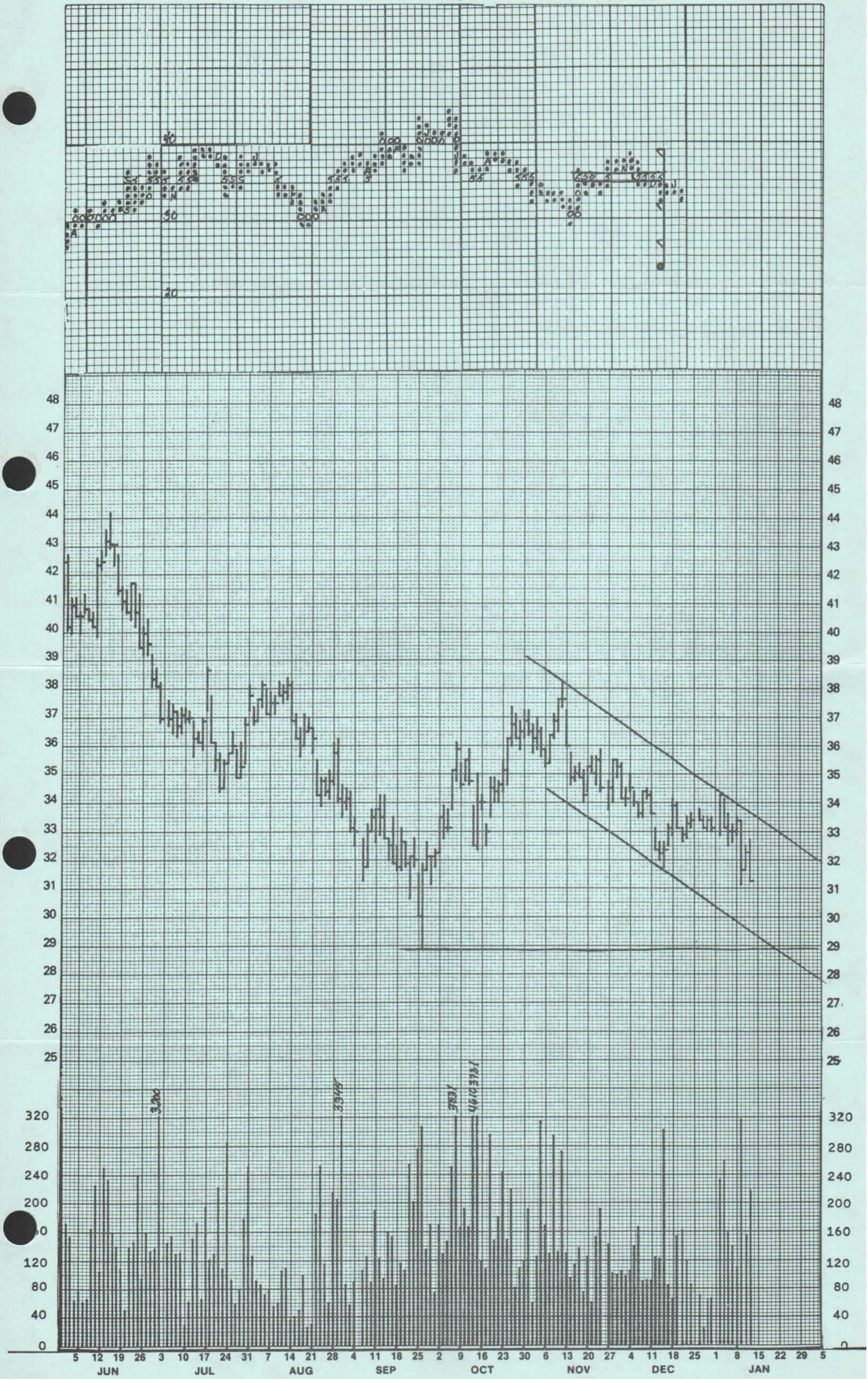

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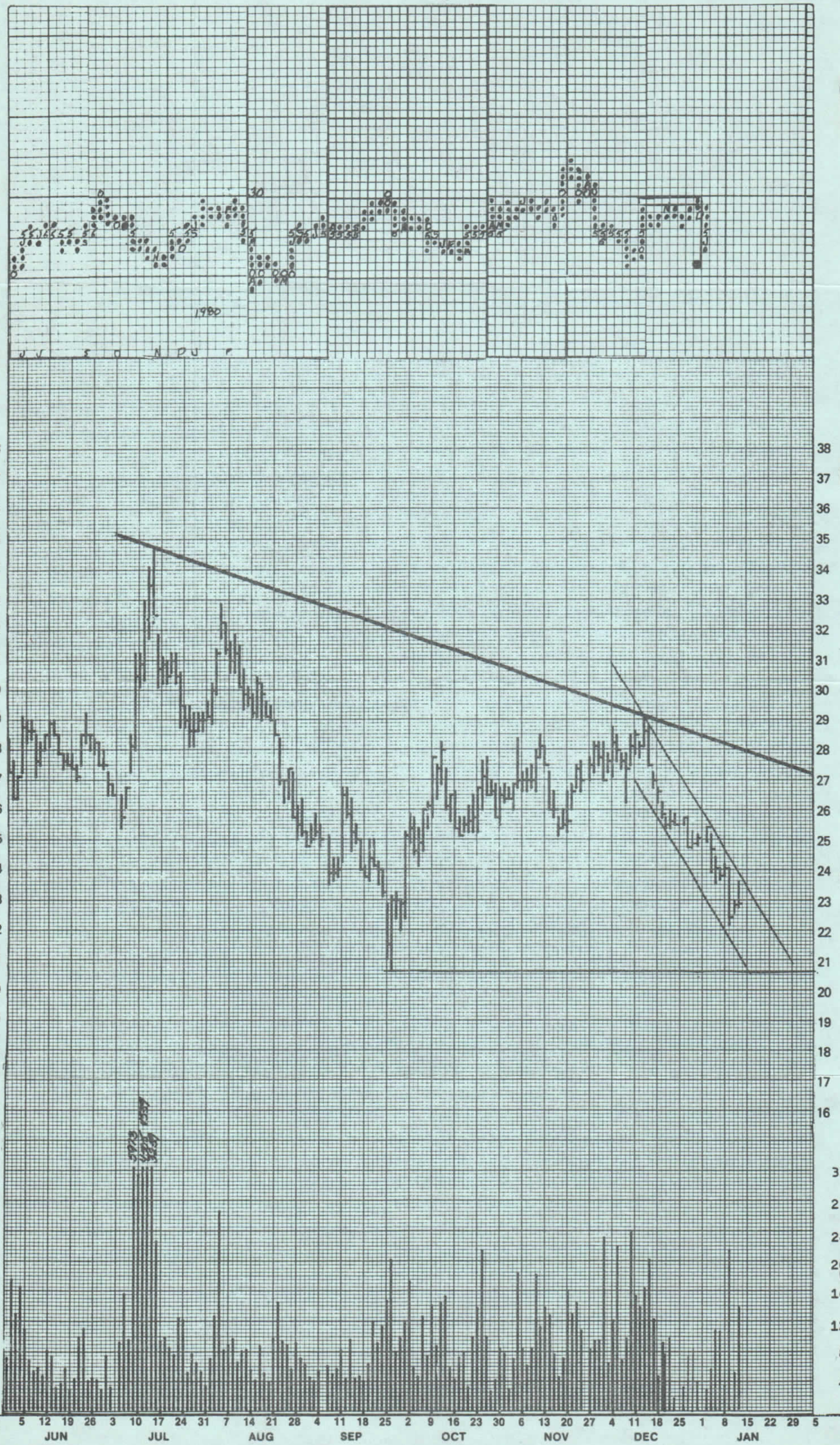

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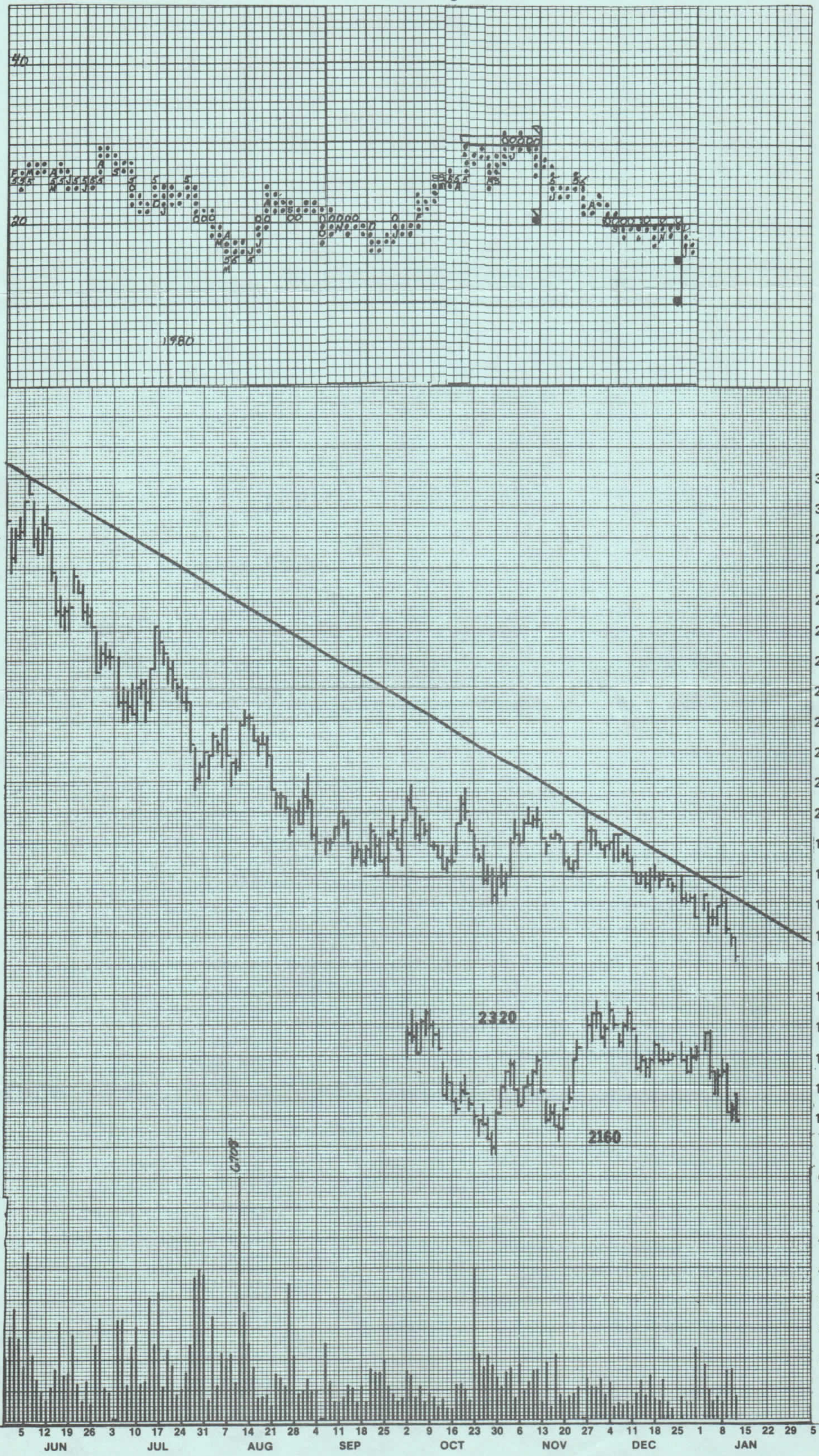

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A.S.E. (p&c)

CHEMICALS