STOCK MARKET INSTITUTE Founded in 1931
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TRENDS AND TRADING RANGES

Monday, October 18, 1982

On Thursday, September 30, the Wyckoff Wave entered a new spring position as had been anticipated. The next day it began a positive response to that position. A positive response to a spring is normal. What is not normal is an upward explosion out of the spring position. We know now though that this is exactly what happened. Two explosive rallies in a period of two months may be a record setting performance. Certainly, nothing like this has happened in many years, or has it?

Unfortunately, we investors and traders seem to have short lived memories. Perhaps this is why we spend so much time relearning past lessons. The last time the market had an explosive advance was only two years ago. How explosive was it? The current up move has thus far produced a gain of forty-three percent on the Wyckoff Wave. Between April and November in 1980, the Wyckoff Wave surged upward by forty-five percent. It is true that the 1980 advance took about three times as long as that which we have witnessed during the past two months, but the fact remains that it was relatively a larger move. Therefore, we should not throw up our hands in despair over what the market has done lately and conclude that it just cannot be analyzed. Anything the market can do can be analyzed. Anything that can be analyzed can be traded intelligently.

One way to analyze the market's performance is to compare it to the last spectacular upside performance in some detail. We have already seen that the 1980 advance was approximately of equal magnitude, but that it took longer. There is, however, much more that can be said. The difference in the amount of time involved in the two moves does not automatically make one advance more constructive than the other. Longer is not necessarily better and shorter is not necessarily better.

We know that the market tends to discount what it feels the future will bring. That being the case, we can see that during the move up to point "a" in 1980 the market's perception of the future was very optimistic. On the move up to point "b", during which the future anticipated prior to point "a" became reality, the market was still discounting a positive future. However, on the third thrust to point "c", the reality that the market was facing made further discounting of an anticipated positive future impossible. The move was over. How does this relate to what has happened during the past two months?

The current market has had a first phase to point "A" during which it discounted an anticipated postive future. It has also had a second phase to point "B". It is on this move that we can start to see some potentially signficant differences from the 1980 experience. The current phase B has shown more power and has made a larger advance than phase "b" in 1980. What might account for this? The answer appears to lie in the effort versus result relationship. In 1980, the first phase lasted much longer and apparently consumed a much greater percentage of the available effort. Therefore, when phase "b" began, there was relatively little to fuel the fire and when phase "c" began the fire started to go out.

Phase "A" of the current move required less effort to achieve its result. This was a potential problem going into the correction to phase "a" but the recent spring and oversold condition took care of that. The ability of the current market to produce a greater effort during phase "B" suggests that there will be a phase "C" at some point. Before then, however, phase "B" needs to be corrected. Although the Wave and O.P. are in harmony in terms of both having made a higher high at point "B", there is some lack of harmony that needs to be resolved. The effort on the move to "B" was greater than on the move to "A", but the result was not. This is the immediate reason for a correction. A longer term reason for a correction can be seen in the fact that the Wave is now higher than its 1980 peak but that the O.P. is not. The timing of a resolution to this type of long term divergences is often impossible to determine, but the success of phase "C" depends on it. The only way the move up from August can turn into the biggest bull market in thirty years as some are predicting is if the Wave and O.P. do a better job of moving in harmony. If continued, the lack of harmony present at the end of phase "B" will destroy the advance. This will occur during phase "C". That is why trading on the long side from this point forward will involve more risk. It is still worth considering, but only in stocks with clearly defined higher objectives that match the magnitude of the Wave's maximum upside objective of 3575. The end of phase "B" had an obvious buy anything mentality about it. This is a disturbing negative factor and probably will not produce positive results in phase C.

As mentioned, the lack of harmony between the Wyckoff Wave and O.P. Index during phase "B" is reason to now look for some type of correction. This lack of harmony is especially obvious on the daily chart. Also obvious on this chart is the dangerously overbought condition of the Technometer that resulted from the move up to point "B". The fact that the market became much more overbought at "B" than at "A" should not be taken as an indication that the correction to phase B will be more severe than the correction to phase A. That is not the function of the Technometer. What it does tell us is that the certainty of a correction to phase B is much greater. This in turn tells us something about trading strategy.

Suppose a long position is held and has been since August, or June, or one of the other reaction lows of the trading range. Now, suppose that position has under performed the market. With the market now facing an almost certain correction, this type of position is vulnerable. It should be protected with a close stop, or given back to the market with the idea of being reestablished later if the stock weathers the correction well.

What type of correction might we expect to phase B. We should begin by expecting what is normal. That is a halfway reaction on decreasing volume. Halfway in this case is at about 2720. We are already seeing substantially lower volume, but further contraction seems to be in order. A halfway correction, providing it is accomplished quickly, will respect the current uptrend and provide a good buying point. It will also bring a more rapid beginning to phase C. A more extended halfway correction could produce a problem. The Wave has already reached an important upside objective. That means that the move may be over. If the market now breaks its support line, the chances of phase C being very successful will be greatly reduced. Therefore, a halfway correction that breaks the support line will provide a buying opportunity in only a limited number of stocks. These will be those that maintain their uptrends and have higher objectives. All other stocks should be viewed as candidates for selling during phase C.

In view of what happened during the correction to phase A, we cannot overlook the possibility that the correction to phase B will be abnormal as well. The action from October 11 through October 13 appears to have stopped the advance and provides the potential resistance level for a new trading range. The bottom of the current reaction will provide a potential support level. Following that, a rally to a lower top will confirm a new trading range.

An advancing market that corrects an upward phase with a trading range rather than a reaction is indicating just how strong it really is. In these cases, it is normal to expect the break to come in the direction of the established trend. Therefore, if the action of the next week defines a trading range, we should begin by looking for a break on the upside. Another spring action would do just fine. However, we should not close our eyes to anything else that may happen during the trading range. Upthrusts, for example should never be dismissed. In addition, we need to keep an eye on the support line of the uptrend. A horizontal correction in an advancing market is positive, but only if it does not break the trend. Should the trend be destroyed, the market will be equally able to move in either direction.

The intraday picture does not show us anything we have not already noticed. It does, however, help to confirm some of them. Those who were buying early last week when the pacing of trading was so feverish that the tape could not keep up should expect at least some short term disappointment. We can see that the October rally had three thrusts. The second one was somewhat less productive than the first, but it is the third thrust that suggests immediate additional progress is unlikely. This will be confirmed by an attempt to resume the rally that fails to make a new high.

It is common to hear people talk about the current market as if nothing like this has ever happened before. In terms of the exact details this may be true, but in terms of the more general concepts this market has happened before. It is these general concepts that should be our guide for the future and they are now telling us to be careful. The risk on the long side of an advancing market increases as the advance progresses. This is especially true when the general public has been induced to buy. The inability of the tape to keep up with the trading in recent days implies an enormous number of small trades. These represent the general public entering the market. There is likely to be a third phase to the advance, but with the general public already being drawn into the picture, the purpose of the third phase may be much more negative than either of the first two.

GROUP ANALYSIS

During phase B of the advance, all of the groups made good upside progress including those whose reason to do so was questionable. This is evidence of people looking for bargains. To the general public, a bargain is usually equated with a low price. A true bargain in the stock market is something much different. Price is not even a factor. What is important is the trend, the position in the trend and the potential and how these relate to the general market. The low price approach to bargain hunting may have worked during phase B. It probably will not work in phase C and there is even some question whether those for whom it is now working will be able to say that when their positions are finally liquidated.

All but one of the groups have well defined uptrends. Unfortunately, none of them have positions within those trends that warrent action on the long side. The current placement of the various group indexes within their trends suggest taking profits, or being prepared to ride out a correction.

The aerospace group, which had been a leader in the first phase, did poorly during the second phase. It did make a higher high, but under performed the general market. It is now reacting off an overbought position. In view of its lagging performance on the previous rally, a more severe correction than that experienced by the general market is a distinct possibility. This is not likely to be a prime candidate for participation on the long side in phase C.

Airlines over corrected the first phase and consequently failed to make as much upside progress in the second phase as did the general market. The group did not become overbought and is already showing signs of much lower volume on the reaction that has just begun. These are positive signs. They indicate some potential for participation in phase C, but are not likely to be the best candidates. Being selective will be important, Northwest will probably be the best selection.

When we think of the auto group, it is natural to think of it as being made up of General Motors and those other two stocks. The group performed with the market on the last rally. It should be a candidate for participation in phase C. If so, it is those other two stocks that should be given most of the consideration. General Motors has shown too much willingness to give back its recent gain. This is not the characteristic of a stock that is likely to go much higher.

The banking group was the real surprise of the recent rally. It is now dangerously overbought and, therefore only a candidate for profit taking. In view of the strength shown, this should be an area for participation in phase C providing the group does not give back all of its gain.

Building materials have a good uptrend, but are overbought. A correction is in order. The advance here has been on balance orderly. A correction back to about 2200 on low volume should produce a new buying opportunity. This appears to be an area where riding out the reaction can be justified.

Although the chemical group has reached one upside objective, there is additional potential available. The group is now overbought and therefore not a good buy, but it could be around 2440. This would be after a correction similar in character to the first. The result would be a continued positive picture worthy of consideration for phase three of the advance.

The computer group is a problem. It participated well in the first phase, but seems to have lagged the market in the second phase. However, it does not have an overbought condition to correct. A return to the area of the previous top on lower volume would suggest selected action on the long side if accomplished in the face of an oversold market. In considering this group, is should be remembered that IBM has a long term objective into the 90's.

Avoid the diversified group. It has shown great strength, but its uptrend will be difficult to maintain. If broken, the entire up move could be corrected. Better opportunities exist elsewhere.

The electronics group is a high technology area that can be considered for participation on the long side in a third phase to the advance. This is based on the strength already shown and the harmony with the general market. It also assumes that the uptrend will be respected. If not, look elsewhere. This is a volatile group. Trading against the trend in this area only invites disaster.

Insurance and bank stocks tend to move together. Like the bank stocks, the insurance issues have made a good gain. The plus for the insurance stocks is that their overall advance has been more orderly. The question now is whether they can sustain the most recent gain. Thus far, there appears to be too much of a willingness to give back that gain. The uptrend may be put in jeopardy. If it fails, do not consider these stocks for future long positions.

The machinery group is one that shows the disturbing buy anything attitude that appears to have taken hold in the second phase of the advance. There is no good reason to be long in this group now and its potential in a third phase is questionable. If a long position is held in this area, it would be wrong to sell as the group corrects, but if a lower top is made on the next rally selling will be in order.

The metals stocks represent another example of over correcting the first phase and under performing on the second. This does not usually make for substantial progress. There is a plus here, however. It is the character of the uptrend, which appears sustainable. Continued progress from this point is likely to be slow. New positions are questionable, but holding long positions as long as the trend is respected can be justified.

The oil group is a candidate for phase three long positions. It can be considered as a buy around 3360 on low volume. Its ability to break above this important resistance level indicates that strength is beginning to return to this area. A successful test of the penetrated resistance would suggest continued strength and a reason to buy.

The final group, semiconductors is a problem. Its second phase performance did not live up to that of the first. This leaves it vulnerable to a more serious correction now and an even more questionable performance in a phase three. Restrictions on new long commitments in this area should be tight. Buying should be done only in an oversold market no lower than the halfway point on low volume providing the uptrend is still being respected. The reason for being so careful here is the volatility of the group. Mistakes in this area tend to be more costly than in others.

INDEX CHARTS

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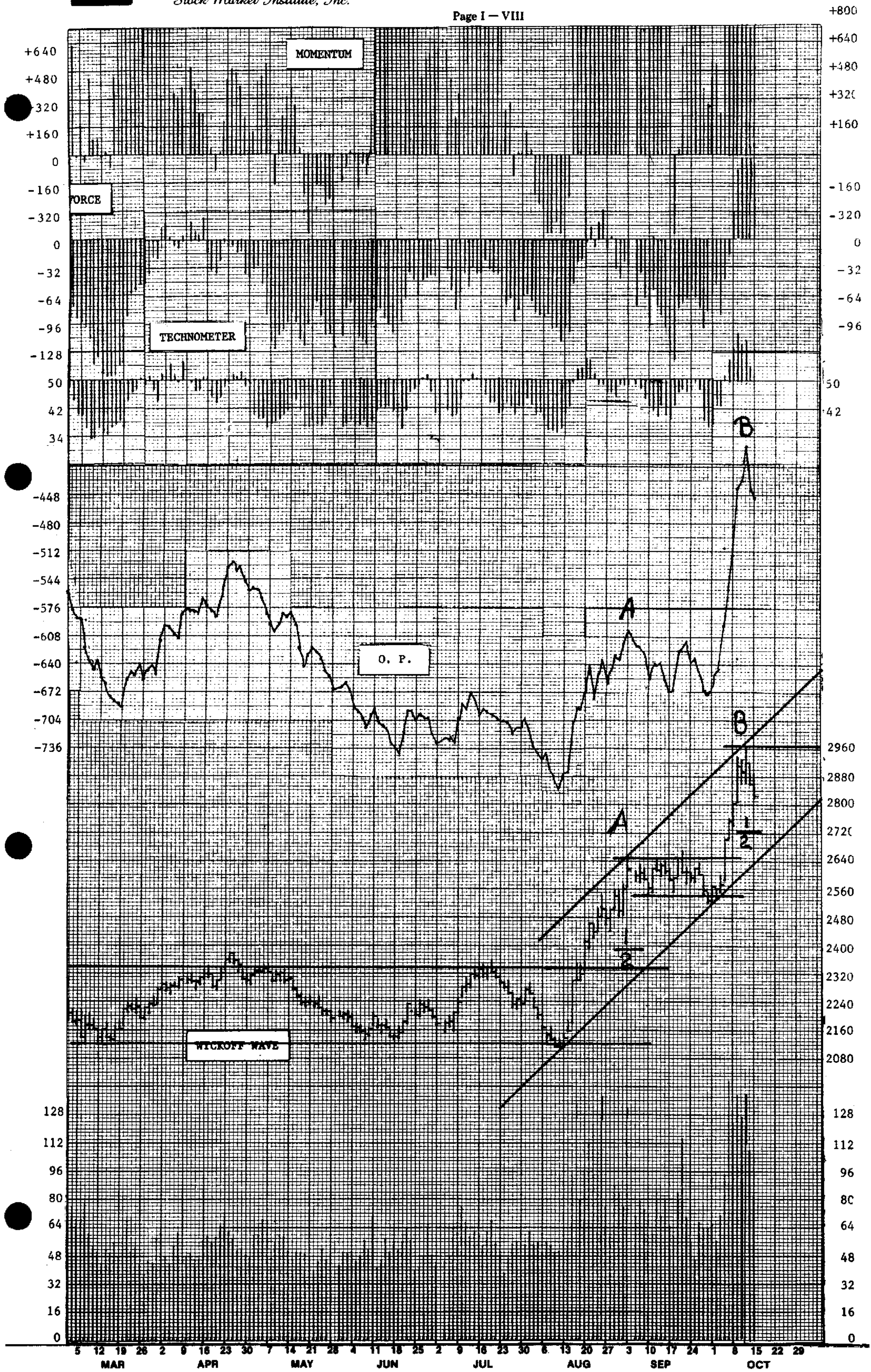
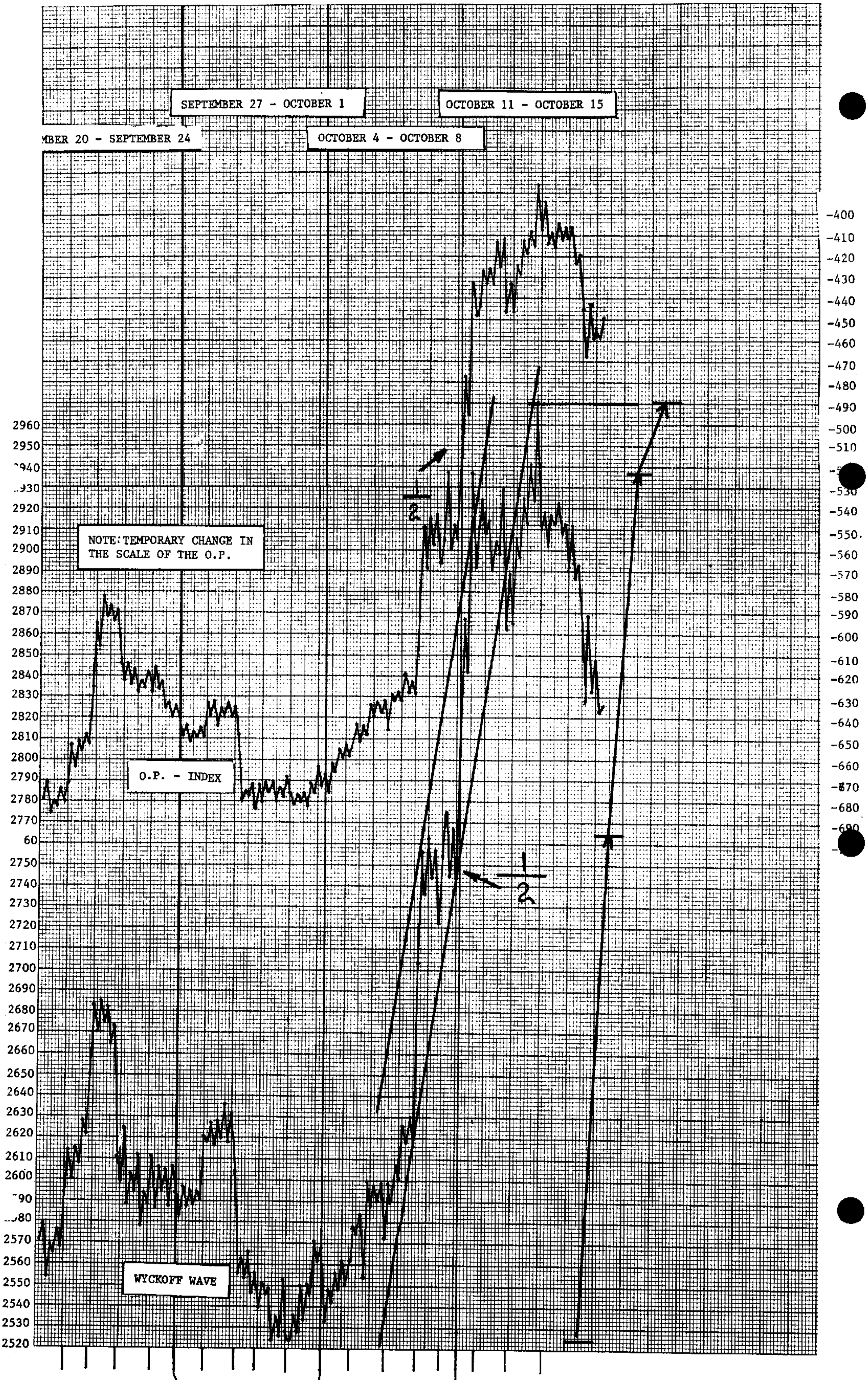



SEPTEMBER 27 - OCTOBER 1
OCTOBER 11 - OCTOBER 15
BER 20 - SEPTEMBER 24
OCTOBER 4 - OCTOBER 8
NOTE: TEMPORARY CHANGE IN THE SCALE OF THE O.P.
O.P. - INDEX
WYCKOFF WAVE

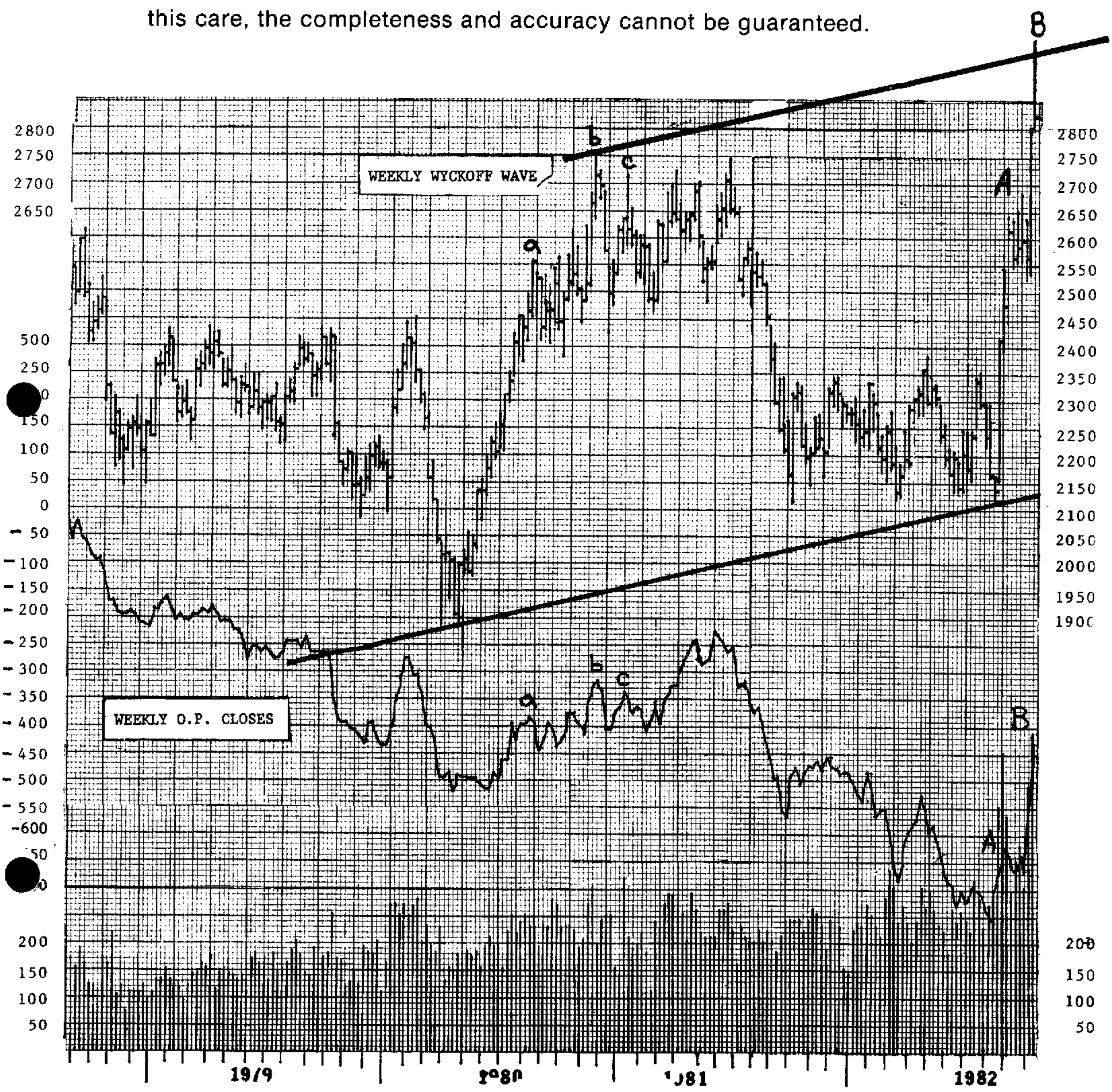
INDEX CHARTS
STOCK MARKET INSTITUTE, INC.
OCTOBER 13, 1982

SMI/WYCKOFF INDEX CHARTS

This set of SMI Index Charts is published weekly and is available only to subscribers of SMI's DAILY STOCK REPORT / PULSE of the MARKET or SMI's CHARTING SERVICE. It contains the following charts:

- Weekly Wyckoff Wave
- 50-Point Modified Wyckoff Wave
- 25-Point Modified Wyckoff Wave
- 3-Point of the 10-Point Modified WW
- 10-Point Modified Wyckoff Wave
- Two Point Modified O-P
- ½-Point Time Index
- Trend Barometer/O-P
- Intra-Day Wave Chart
- 5-Point Modified Wyckoff Wave
- Group Indexes

In our desire to insure the accuracy and reliability of these charts all statistical data is checked and cross-checked. However, even with this care, the completeness and accuracy cannot be guaranteed.



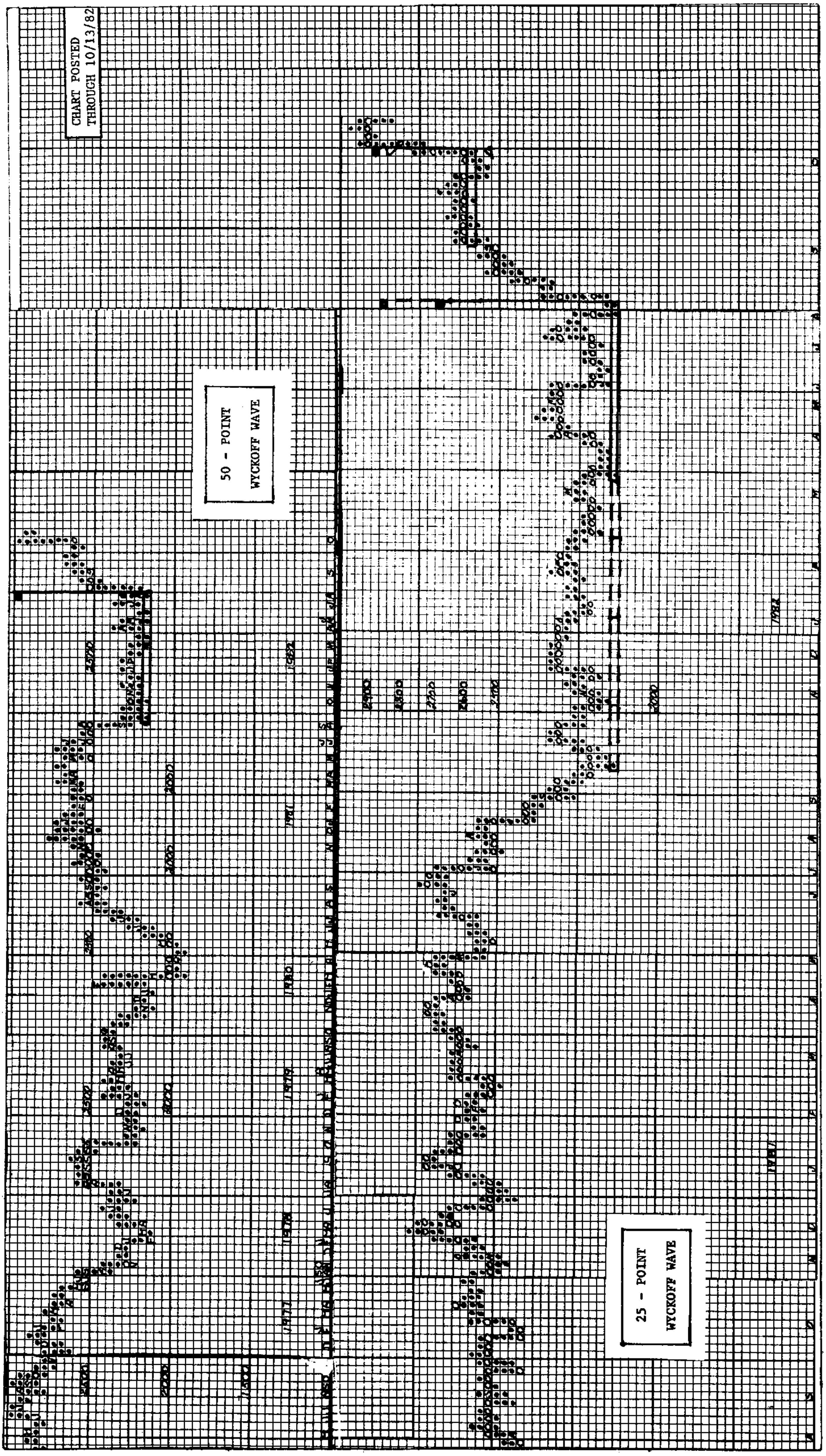


CHART POSTED THROUGH 10/13/82
50 - POINT WYCKOFF WAVE
25 - POINT WYCKOFF WAVE

SMI

INDEX CHARTS

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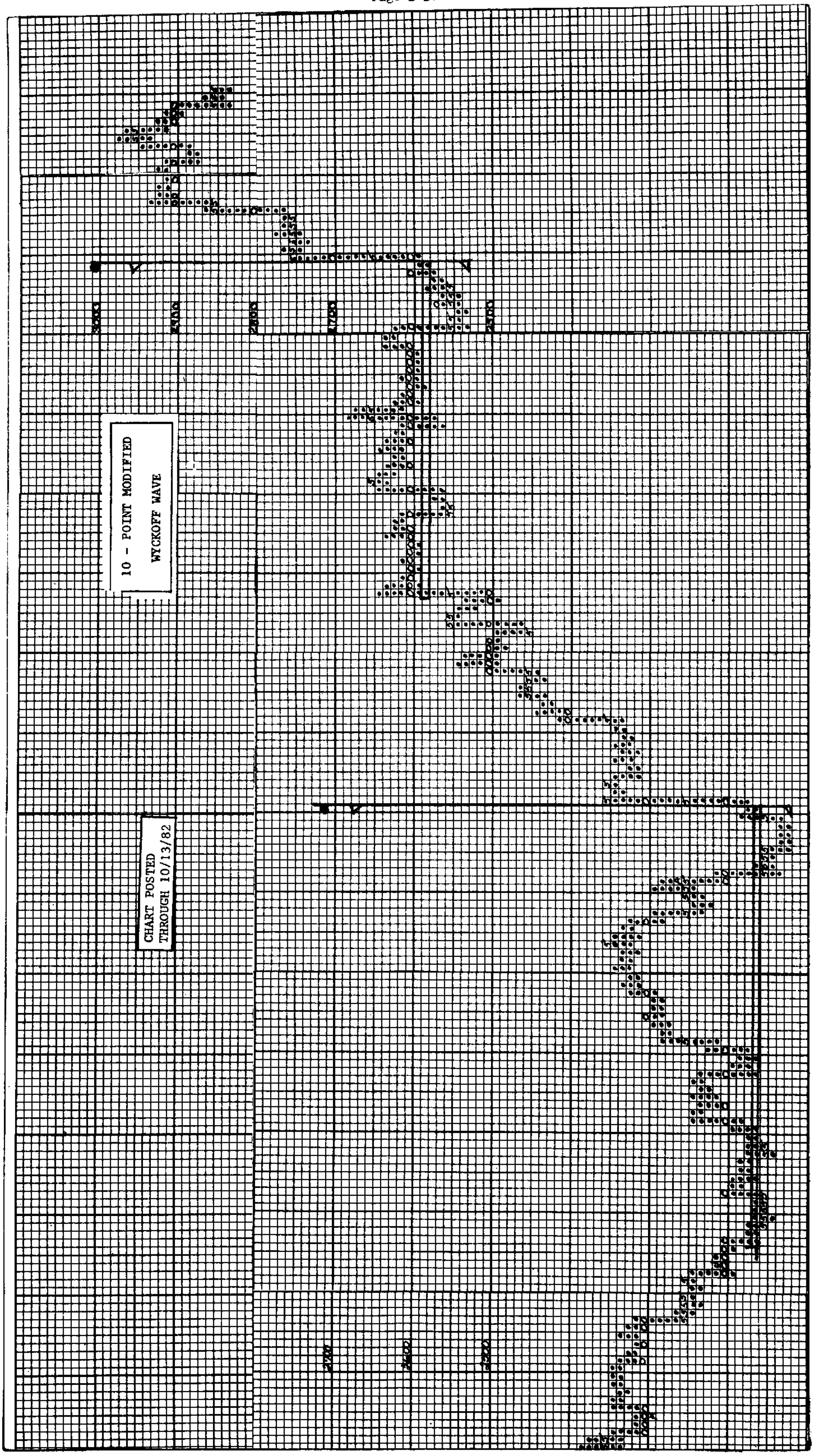

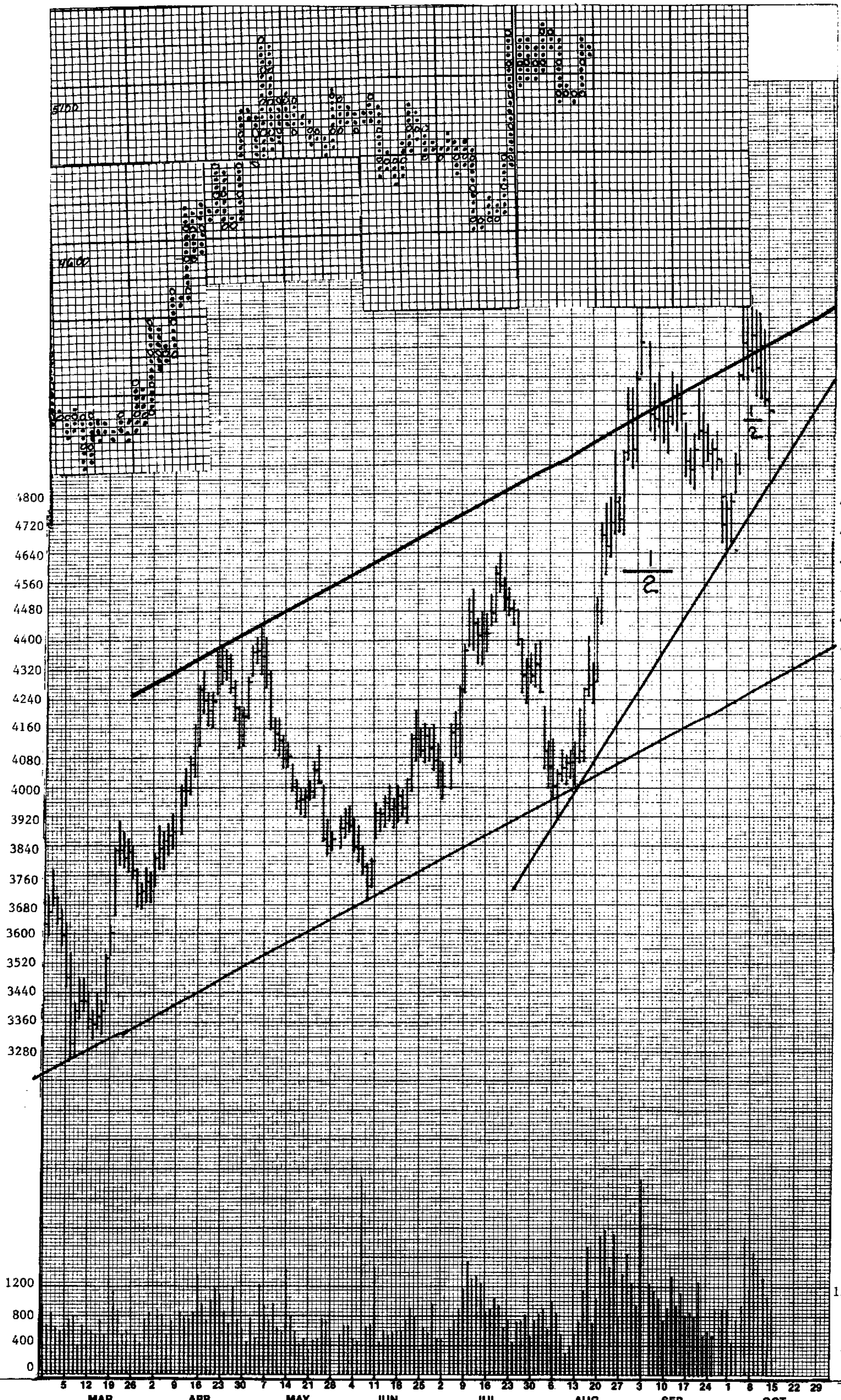
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SMI

INDEX CHARTS

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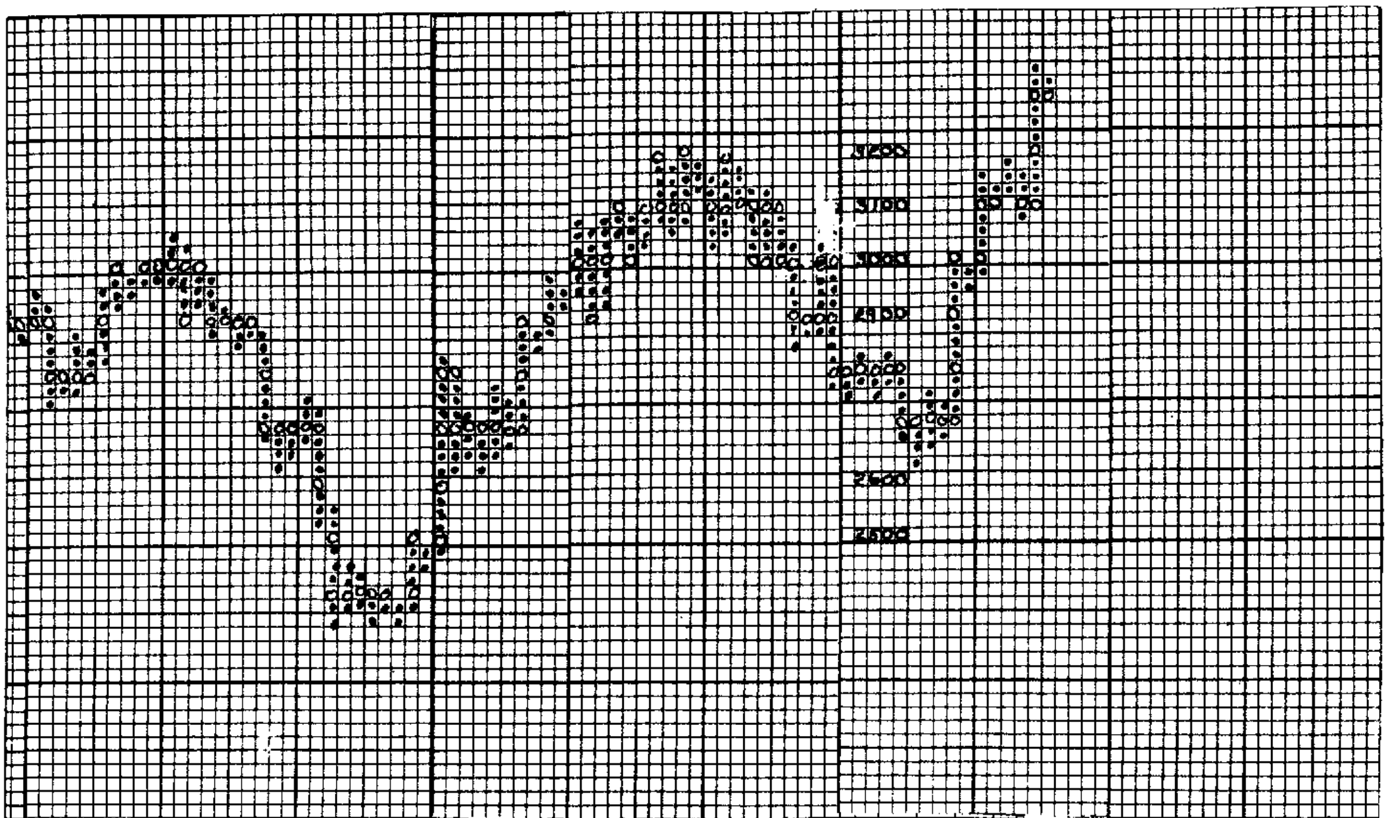
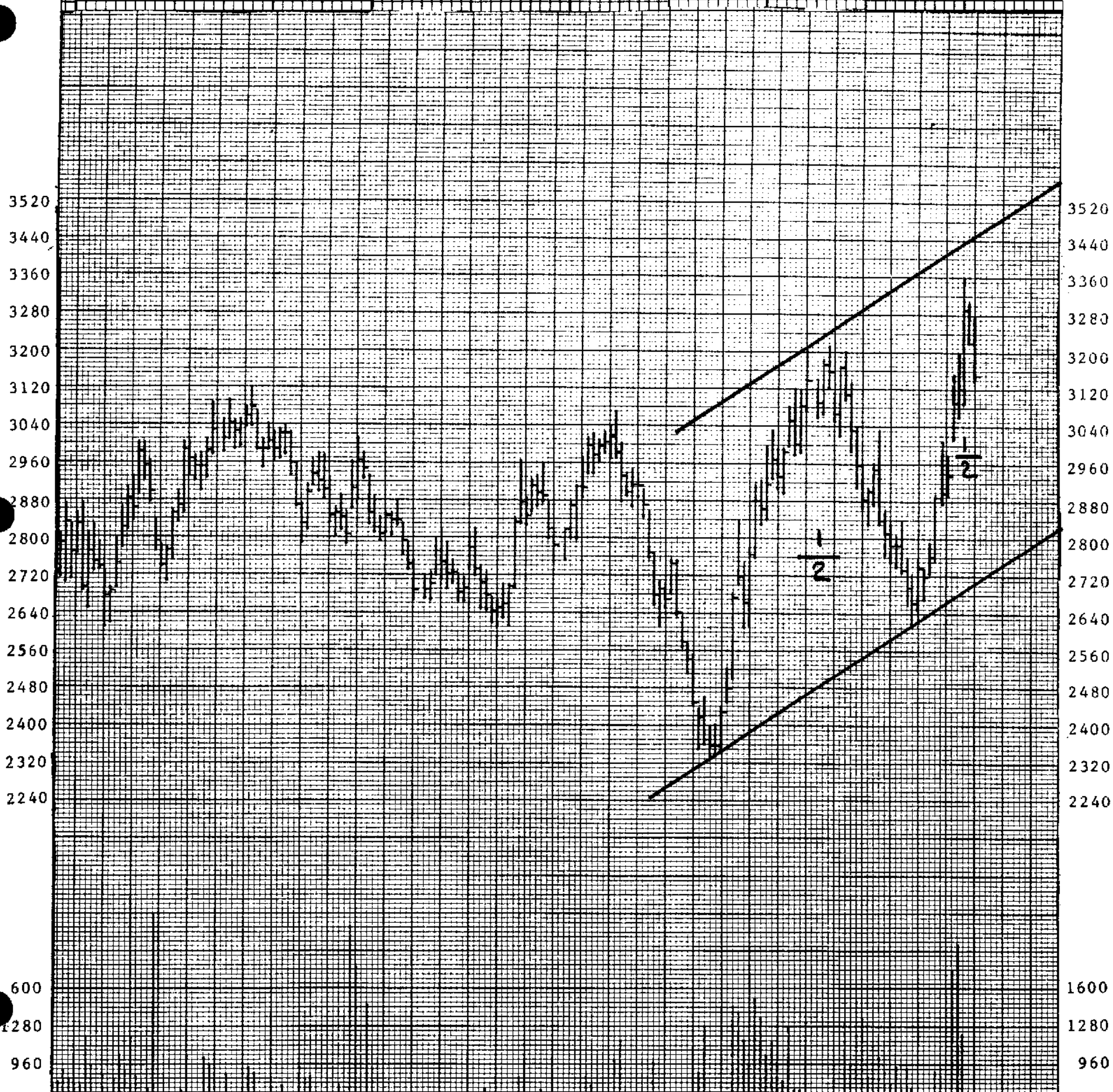
AIRLINE GROUP
6(7TW+2PSA+4DAL+3NWA+4UAL)





SMI **INDEX CHARTS**

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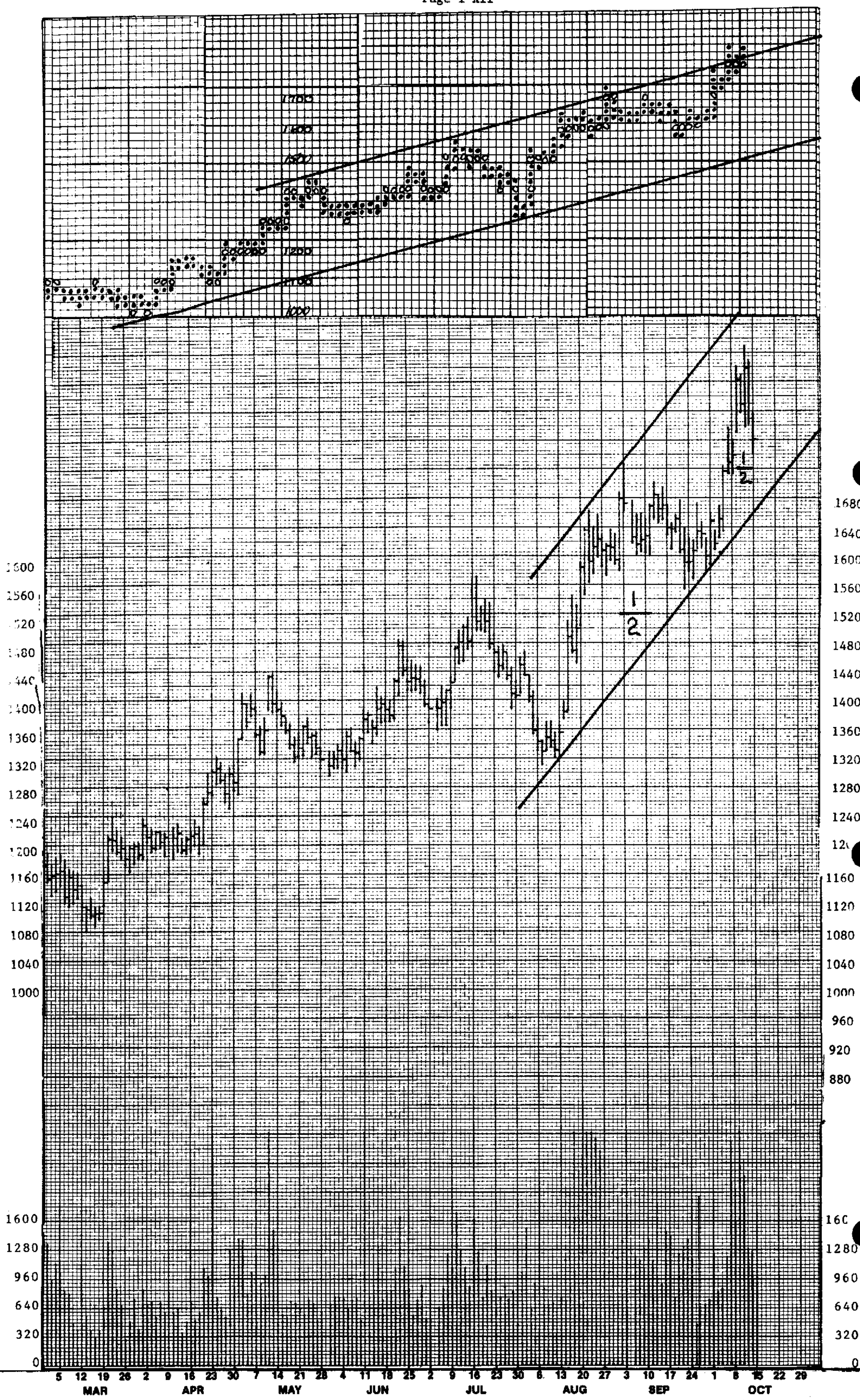
6(11C+3F+2GM)



BANKING GROUP
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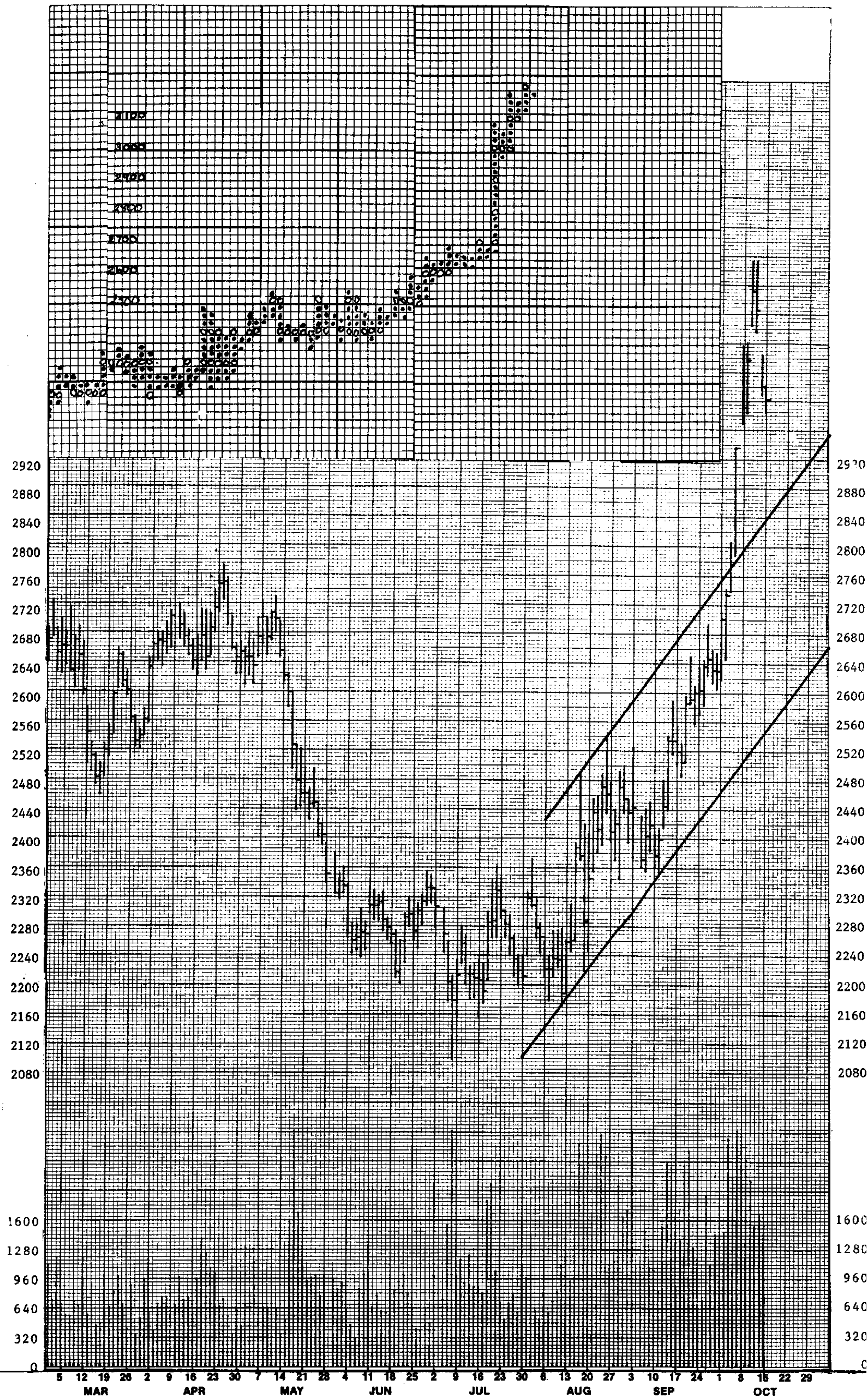

BUILDING MATERIALS GROUP
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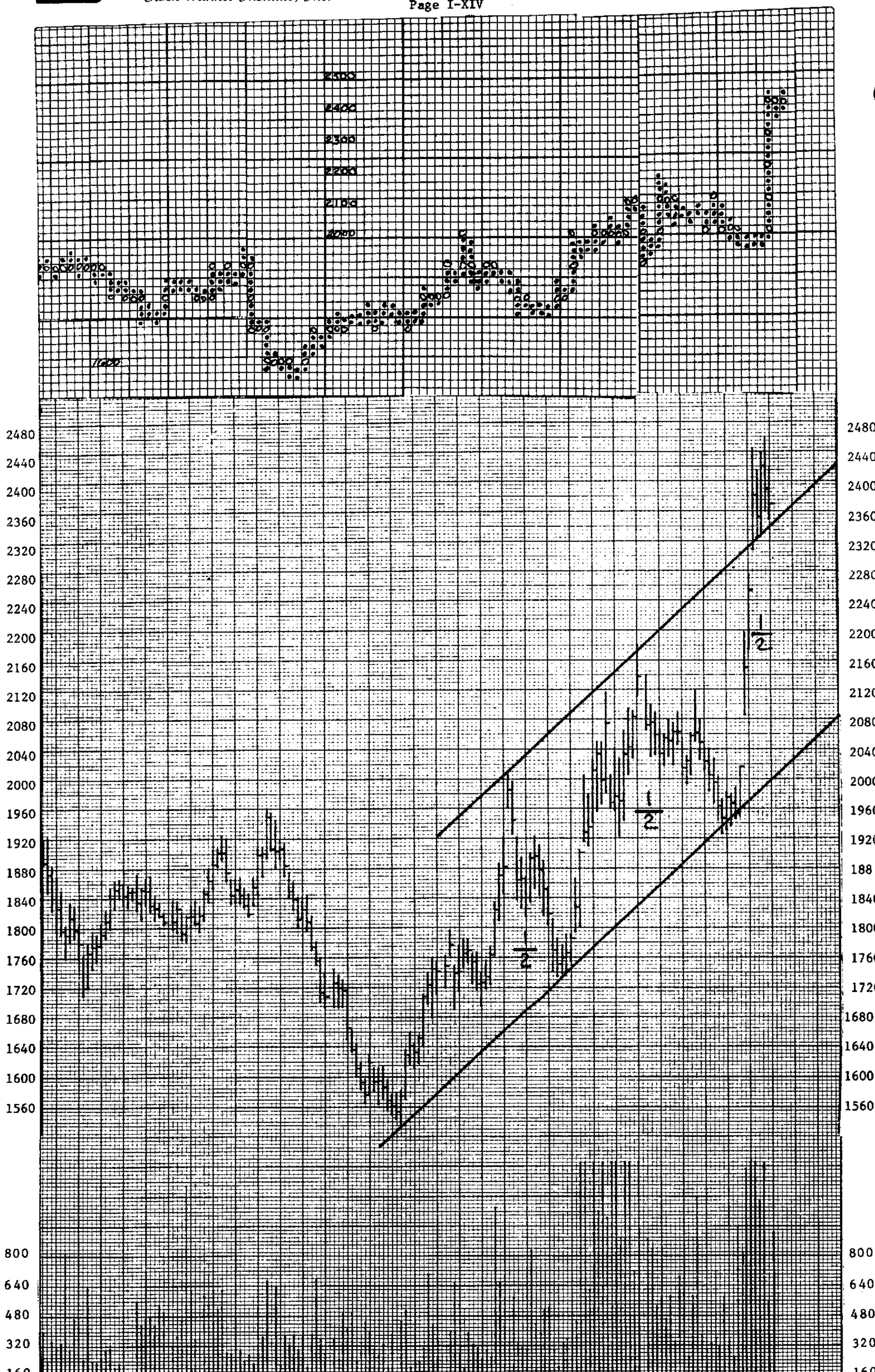

SMI **INDEX CHARTS**

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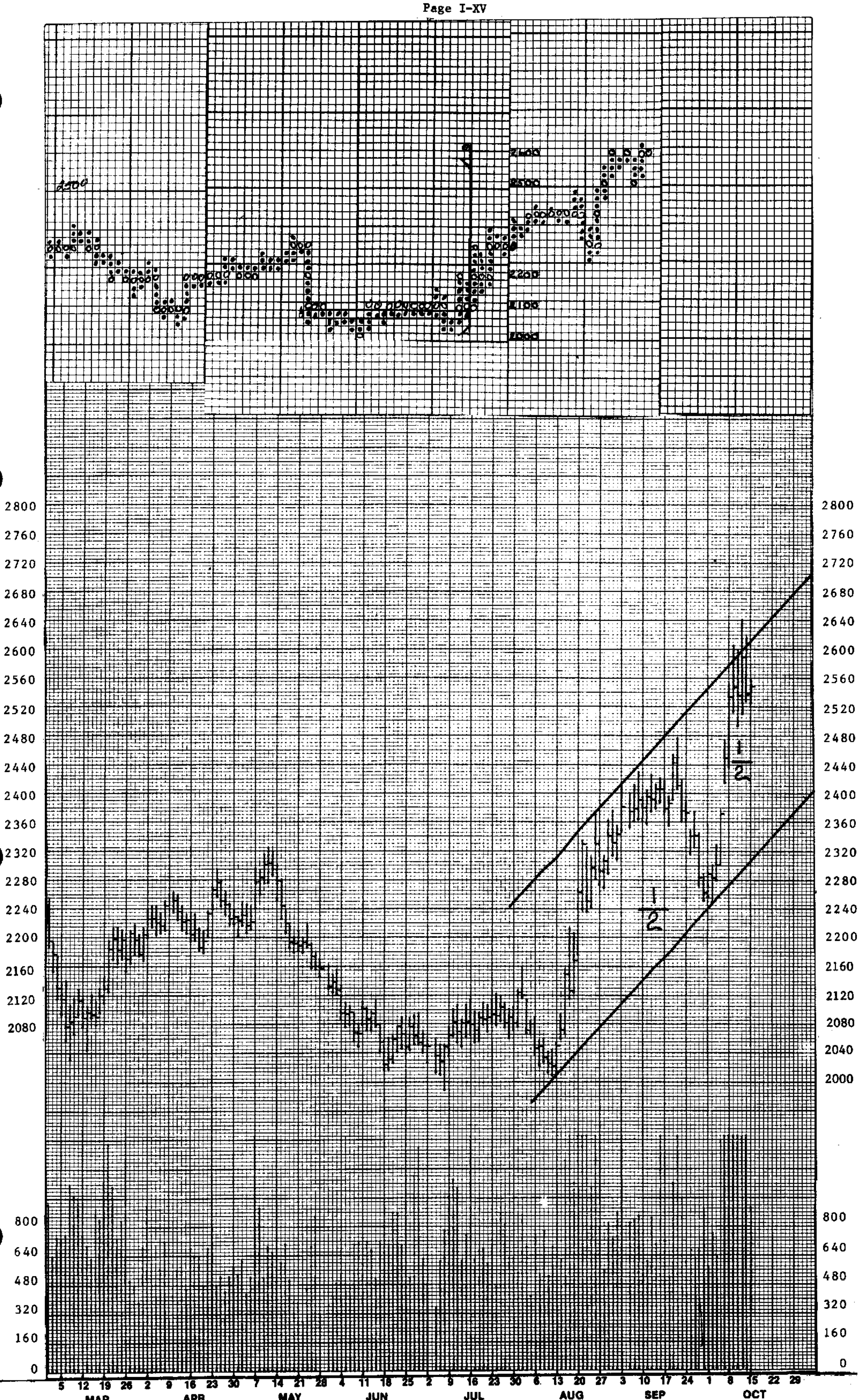
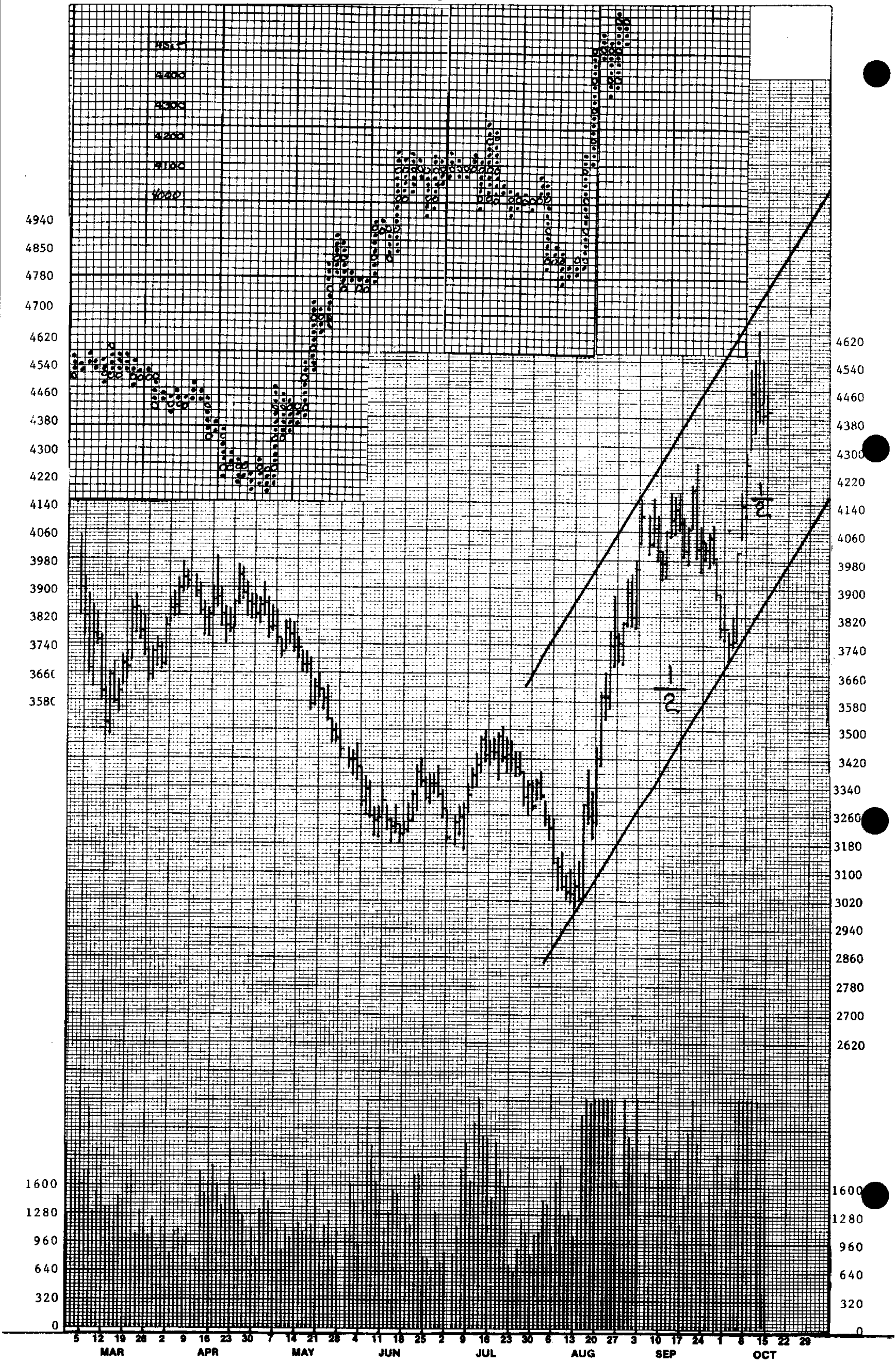
CHEMICAL GROUP
2(6ALD+9DOW+6DD+3PG+5UK)

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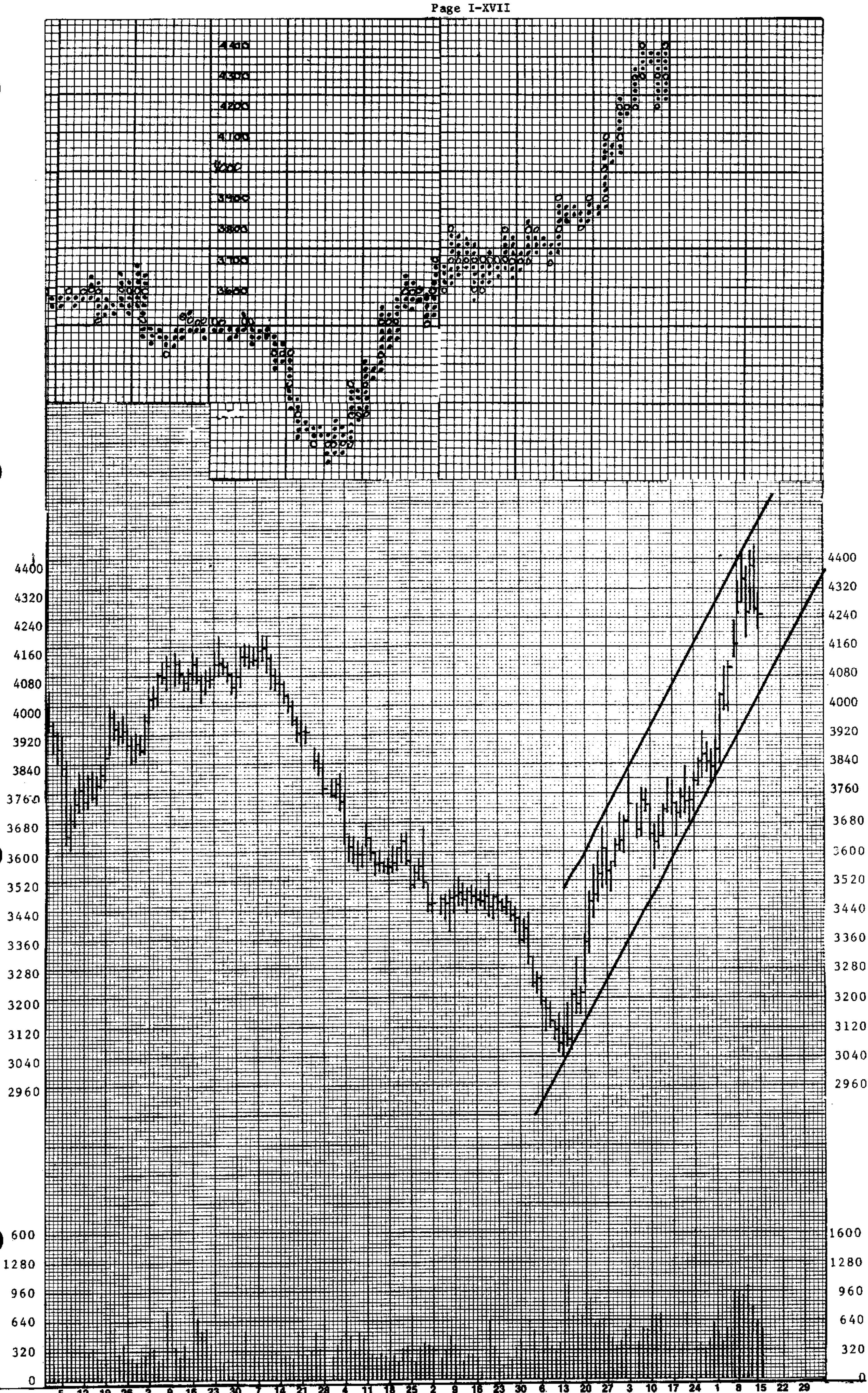
DIVERSIFIED GROUP
6(7GW+3NWT+2LTR+2DKI+4WMB)



SMI **INDEX CHARTS**

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ELECTRONIC GROUP
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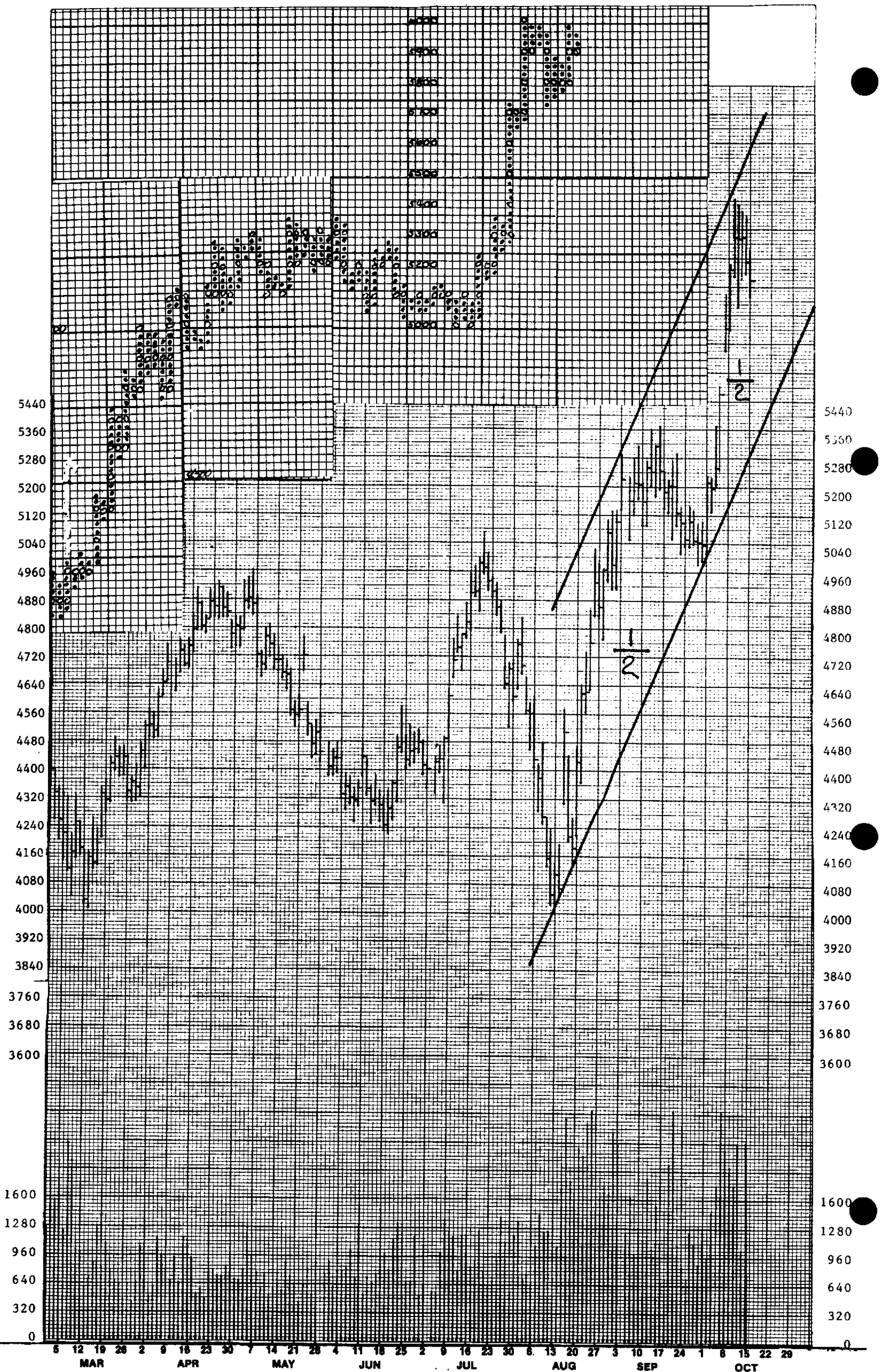

SMI **INDEX CHARTS**

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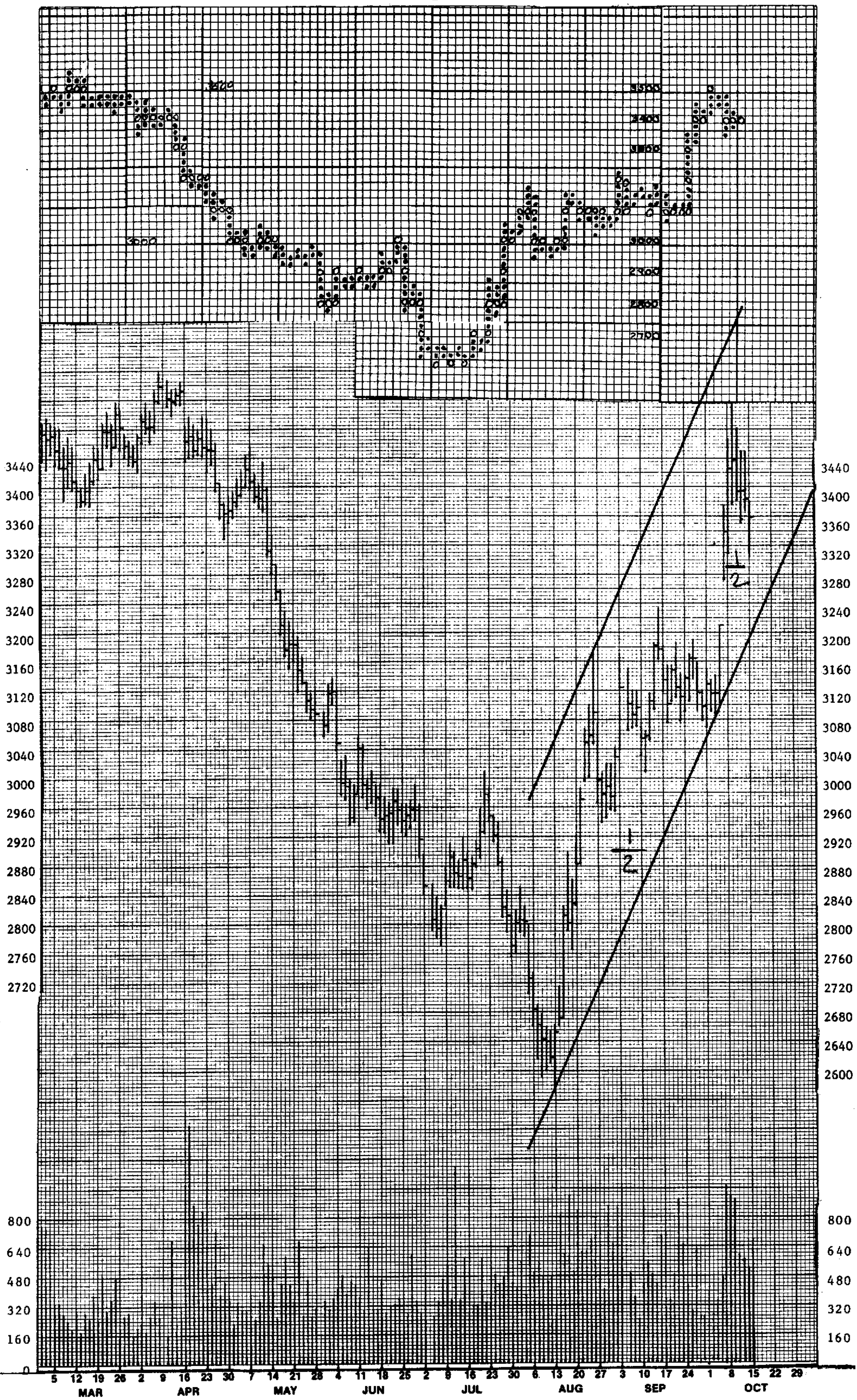
INSURANCE GROUP
4(4.5AET+4.5FG+3LNC+4MMC+8TIC)



INDEX CHARTS

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MACHINERY GROUP
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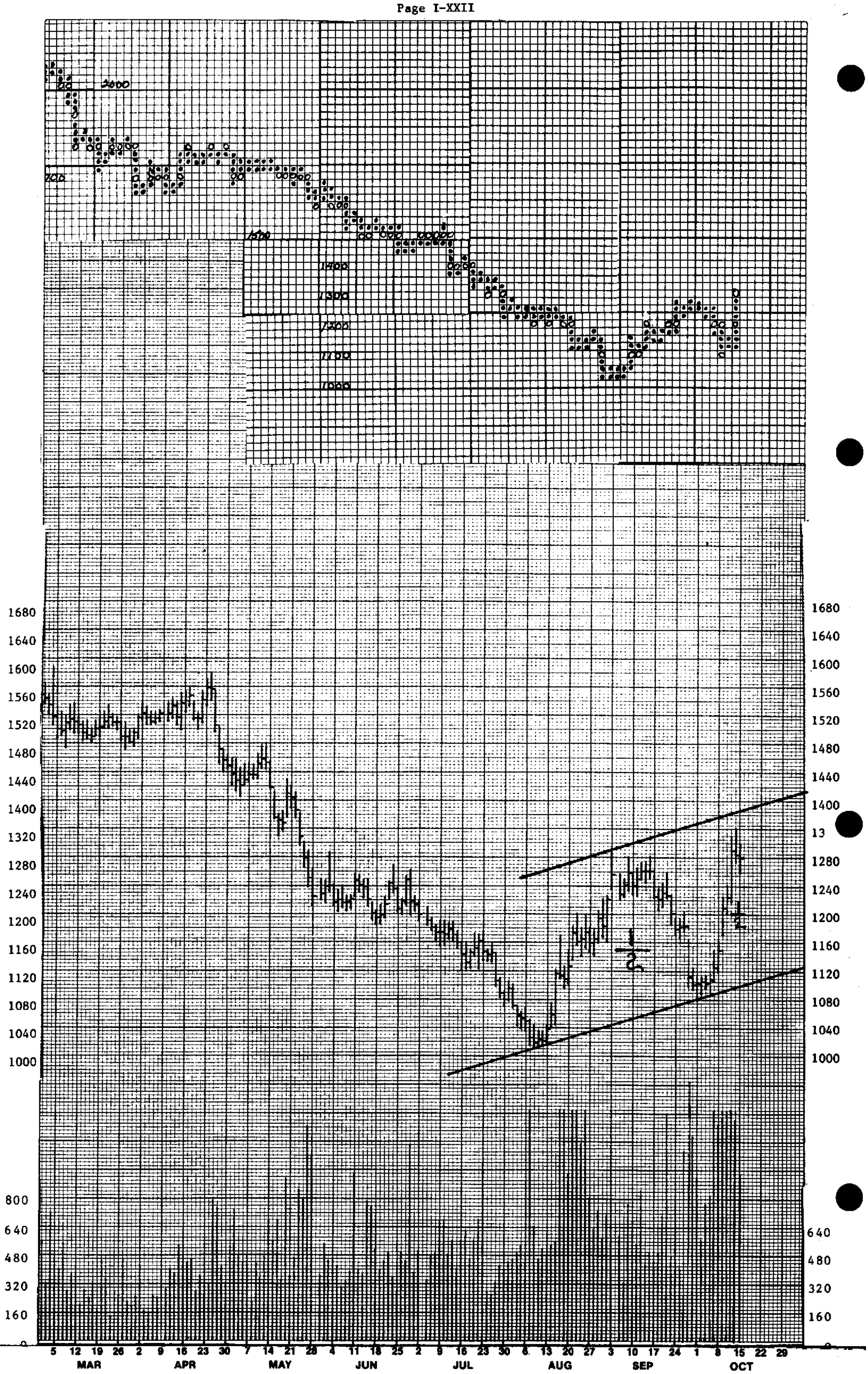

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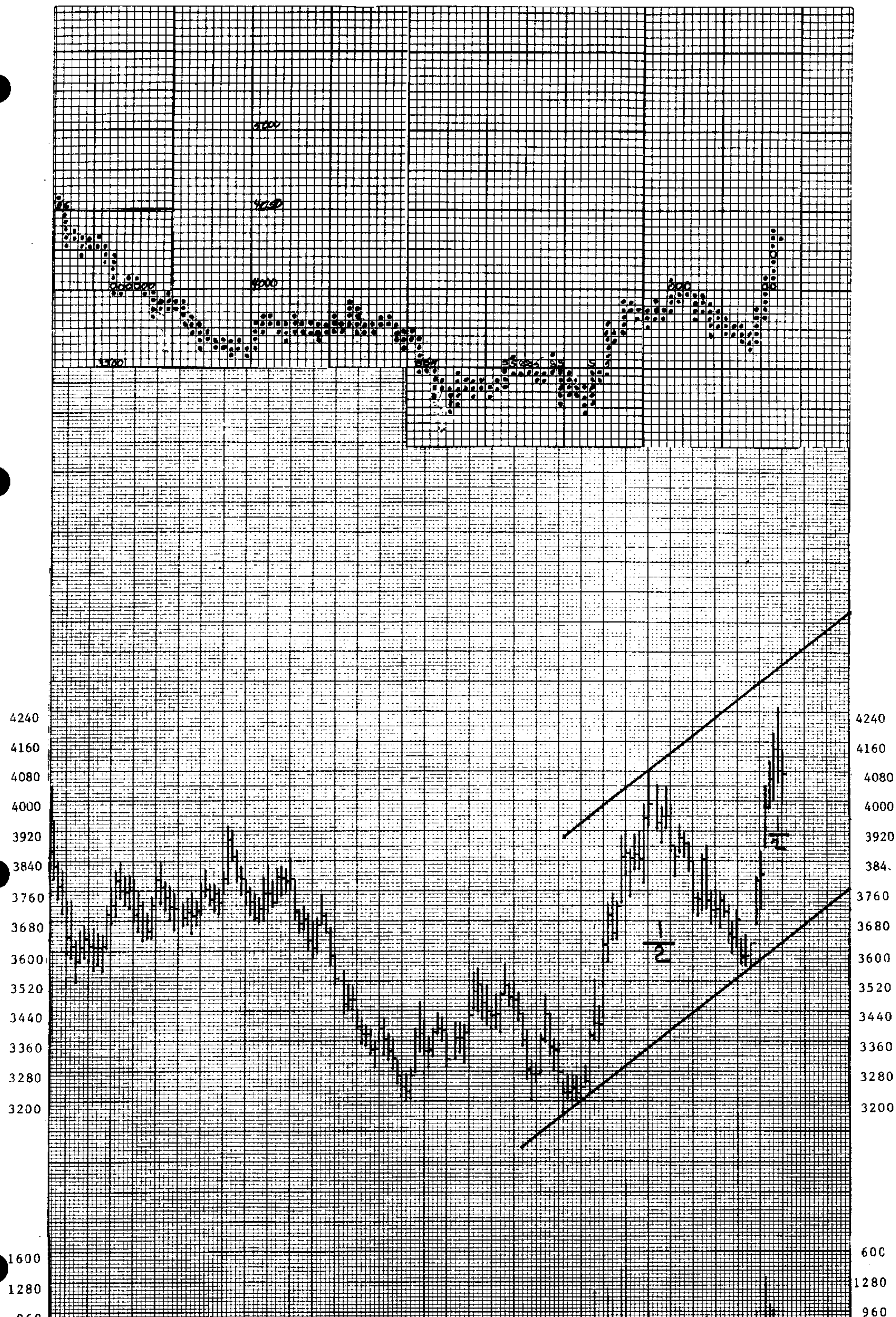

INDEX CHARTS

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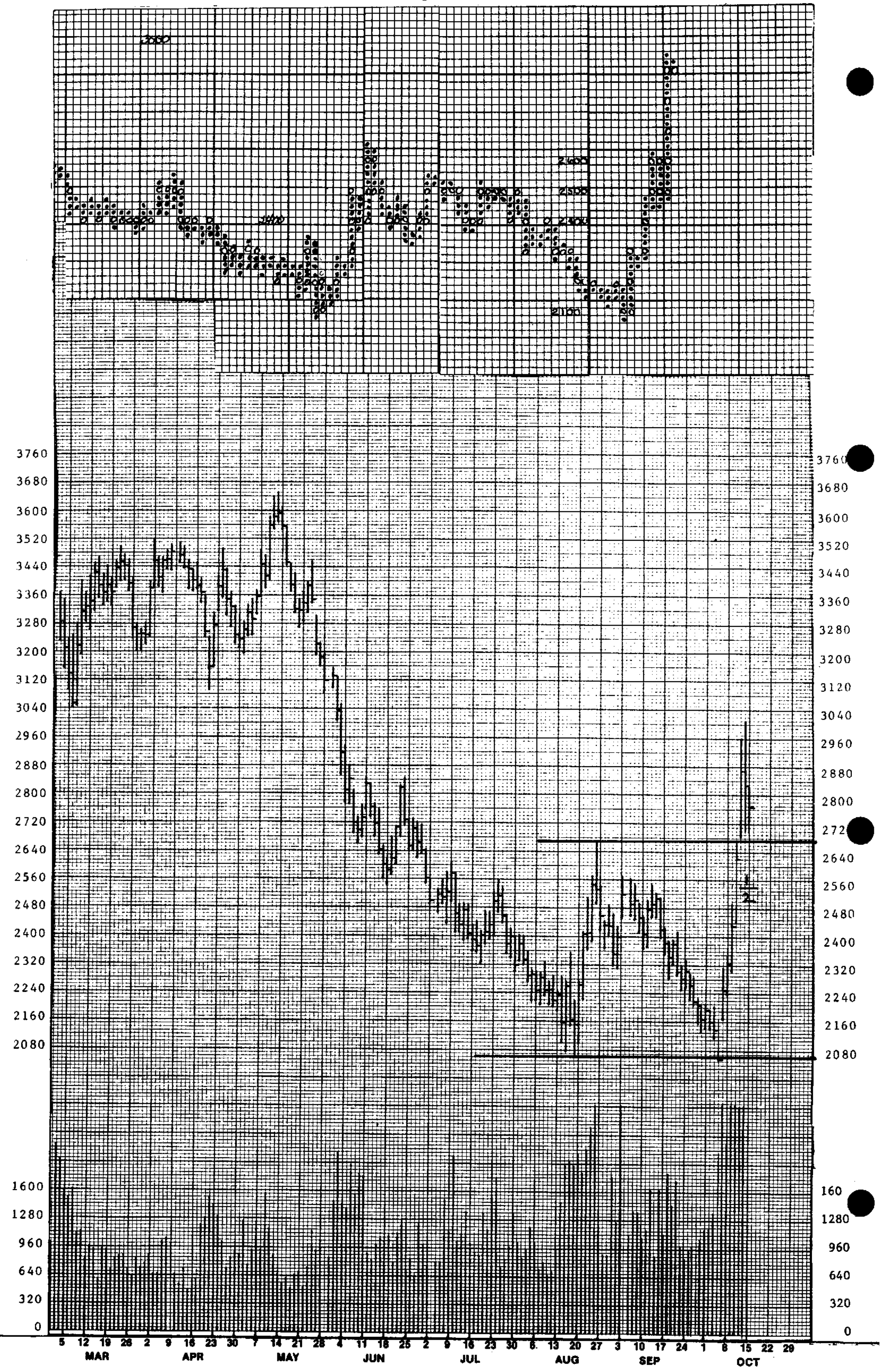
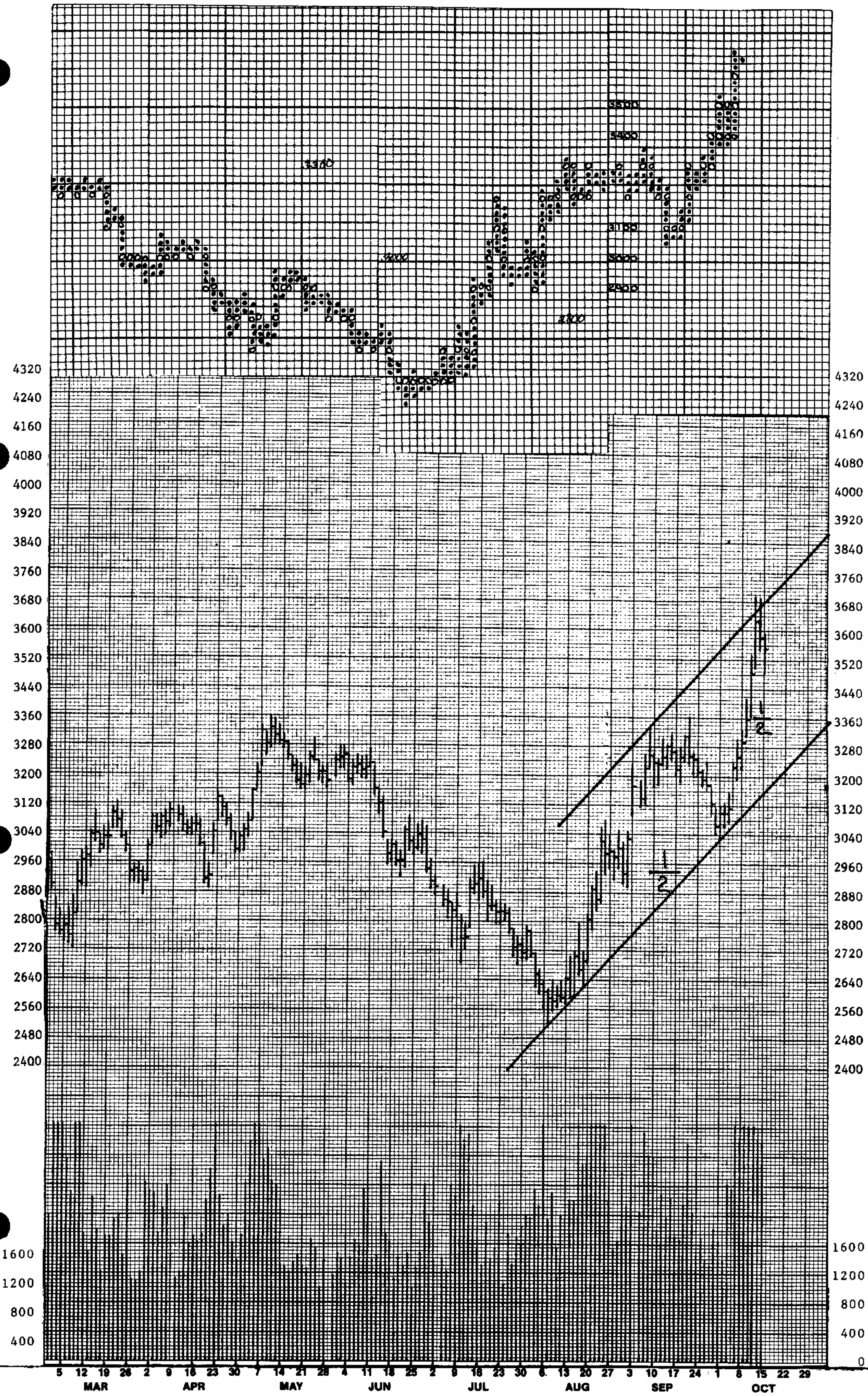


OIL GROUP
3(6ARC+6XON+8MOB+6SD+6SN)



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SEMI-CONDUCTOR GROUP
3(7AMD+4MOT+12NSM+2TXN+24UTR)