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Weekly Market Update October 14, 2009

We are nearing our 1100-1120 target and we believe there is a high probability of reaching these levels by the end of this week. Recall that we thought we could reach these levels by mid-October, where from a timing perspective an inflection point in the markets should occur given that there is a confluence of time cycles coming due. Now that we are nearing our targets we will change our stance in U.S. equities from short-term bullish to short-term neutral at the end of this week, coinciding with expiration. We are seeing enough red flags from a technical standpoint to warrant caution going into next week.

At these levels we believe the risk/reward favors the downside, but we will not turn outright bearish given that the uptrend remains intact and the price action has thus far not shown signs of reversal. We will monitor the price action over the next few days before we adopt a more aggressive stance.

The bullish trend for equities and bearish trend for the US dollar remain intact, but we are seeing signs that point towards potential reversals with intermediate term implications.

The US dollar is sitting on critical support, which warrants a watchful eye. Our long US dollar call still stands, with stops just under the 75 level in the DXY (**Chart 1**). It looks as though the dollar is trying to break its intermediate trend, but if we break that level to the downside, we could reach 72 over a short period of time, which would imply new highs in the stock market during earnings season. That said, we have formed another bullish divergence with RSI, so the next few trading days are going to be critical for the dollar. A change in intermediate trend here should have bearish implications for equities and commodities.

Another recent development is that previous leadership such as large cap tech is starting to underperform the broader market. The large cap tech sector has been a leader in the last few months, but has begun to deteriorate in terms of relative outperformance, and we now see a lower high in the relative chart. (**Chart 2**)

In our last update, we mentioned that while we were still short-term bearish for copper and crude, that we must respect current market action (especially since we had started the final surge upward in equities) and that we would have to acquiesce to bulls in the short-term should price break above ~73 for crude and ~283 for copper. Despite both commodities going above those levels, other signals are weak, and we thusly must relegate ourselves to the sidelines for a few days to see how things shape up. Crude has broken out of a "triangle" consolidation pattern opening the door to the next long-term pivot level at ~78.3, which will be major resistance that it will likely have a difficult time overcoming. Copper so far has staged a "failed" breakout and is trading once again below the 50 day moving average as the technicals continue to deteriorate.

Technical Analysis & Strategy

Based on client feedback, we will now be providing brief comments on several key sectors with our normal Weekly Market Outlook.

Technical Sector Observations

BKX (Financials) – Technically room to the upside to reach more critical resistance level at ~51. Bearish divergence with daily RSI.

XOI (Energy) – Nearing 38.2% Fibonacci retracement level from the highs in '08 at ~1092. Bearish divergence with daily RSI.

OSX (Oil Services) – Testing 38.2% Fibonacci retracement level from the highs in '08 at ~204. Bearish divergence with daily RSI.

IXI (Industrials) – Overcame critical resistance at ~252. Technically short-term constructive. No divergences. Bullish positive reversal signal with RSI

IXR (Consumer Staples) – Reached overbought levels on weekly and daily time frames. No technical deterioration is evident at this point.

IXB (Materials) – Technically room to the upside. No technical deterioration.

DRG (Pharmaceuticals) – Failed and has found resistance from the 50% retracement from the highs in '07 at ~295. Clear bearish divergence with daily RSI.

BTK (Biotech) – Broke above long-term resistance area at ~885-895. That area is now providing support. Potential for more upside as long as that area holds.

DJR (Real Estate) – Failed at the 38.2% retracement level at ~182 from the highs in '07. Bearish divergence with the daily RSI. So far holding 50 day moving average.

NDX (Technology) – Testing long-term resistance and pivot level at ~1745. Reached overbought levels on weekly and daily time frames in RSI. Bearish divergences with daily RSI.

SOX (Semiconductors) – Failed at long-term resistance pivot level at ~335. Reached overbought levels on weekly and daily time frames. Bearish divergences with daily RSI.

UTY (Utilities) – Broken below support of its prevailing short-term uptrend, and fallen out of a bearish wedge pattern. Bearish divergences with daily RSI.

Active Short-Term Trading Ideas

Long DXY (Dollar) with short-term target of 81-82. Stops at 75.

Short EURUSD (Euro) with target of 1.38-1.4. Stops at 1.505.

Short UTY (Utilities) with target of 340-345. Stops at 412.

Short IBOV (Brazil) with target of 55,000. Stops at 65,500.

*Stops on a closing basis

Technical Analysis & Strategy

Chart 1: DXY Index Daily with RSI



Chart 2: NDX Index and SPX Index Relative Strength



Technical Analysis & Strategy

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