How to manage a technical bounce

This document was written in October and November, 2009 by Pascal Willain as part of a training program on the use of the Effective Volume tools.

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The author is French speaking.
This report has not been proof-read for the proper use of English language.

A technical bounce means that there first has been a pull-back down to a natural support, which is exactly what happened last Friday.

As usual, the best way to manage this situation is to follow the money.

Two types of eager investors will come into this market:

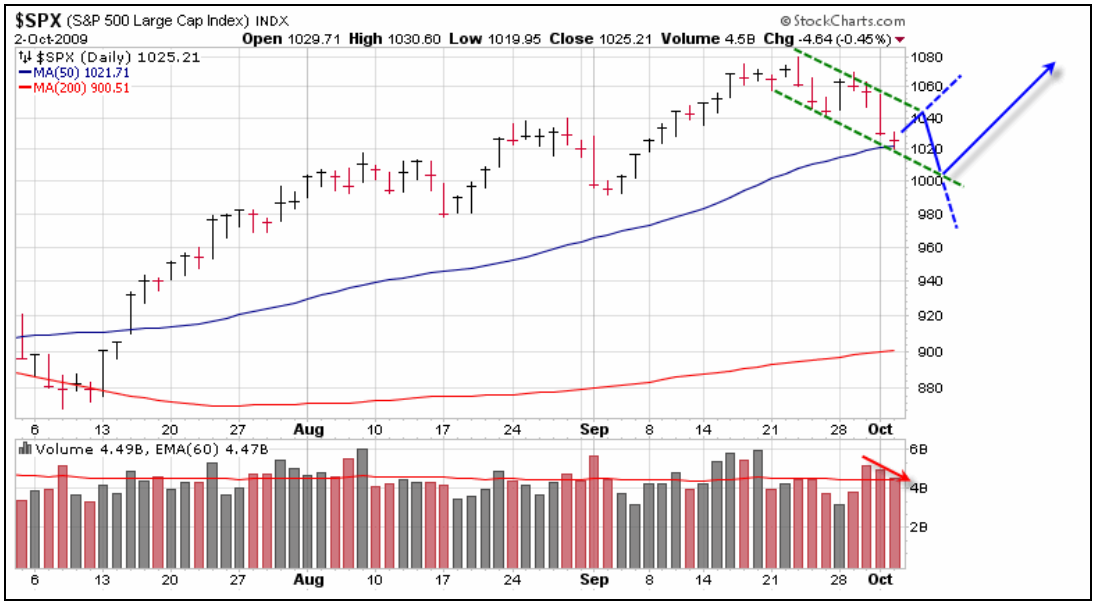
1. **Institutional investors** who missed to buy leaders will want to start or re-build a position.

It might be interesting to look at the list of leading stocks and find those with the best potential. The EV method says to buy those that are back at value (Between the Lower Boundary and the neutral zone) and for which LEV is not negative. The list is here below. It would be interesting to go through that list and note the plays that you would believe are the most probable to move up. Also consider standard TA. (Please first note that you will need to first log)

http://www.effectivevolume.eu/content/Stocks_C/Leaders.php

2. **Short players** who will want to cover their position.

A first list of potential short squeeze plays is simply the list of shorts that I proposed last Friday. Except for COST that I covered, none of the other possible short ideas reached their shorting zones since these were rather far from their respective Thursday closing price. I placed the shorting target far because I expected a technical bounce in the market that would lift all the stocks, including most of the shorts candidates.



Another way to locate potential short squeeze would be to look at the stocks that had a very negative extension on the TEV at the close of Thursday, but that attracted money (LEV positive) on Friday.

(See the Filters section for the Short_Squeeze filter)

I also advise you to have a look and note the most promising of these plays. I will do the same and will publish my list tomorrow or Monday before market opens.

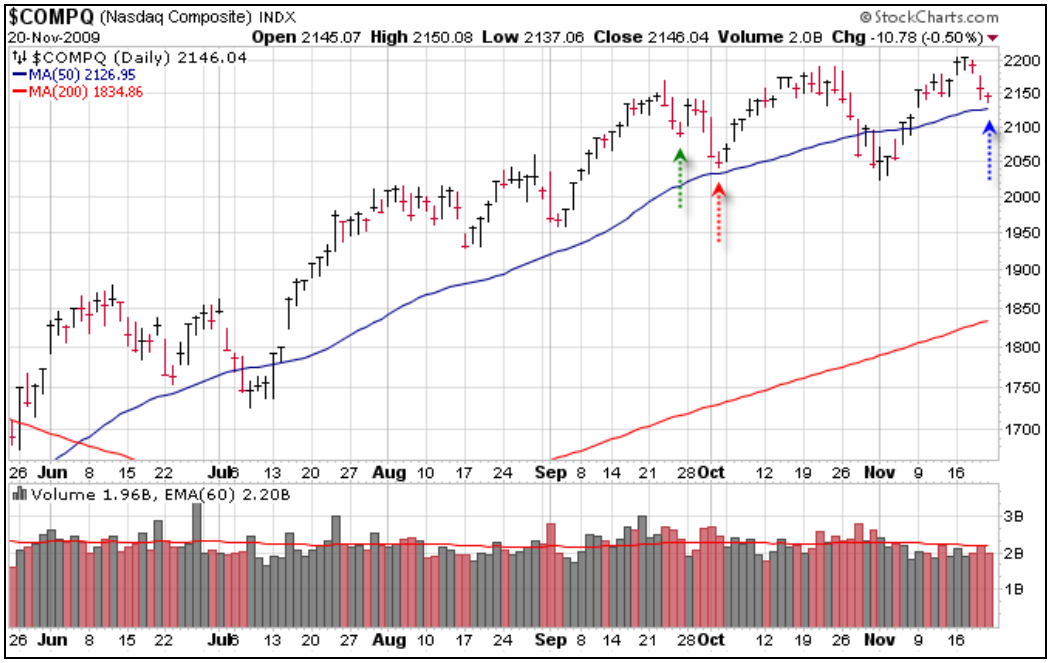
It will be interesting to see which group - Leaders or Squeezed - will gain the most (if we have the technical bounce).

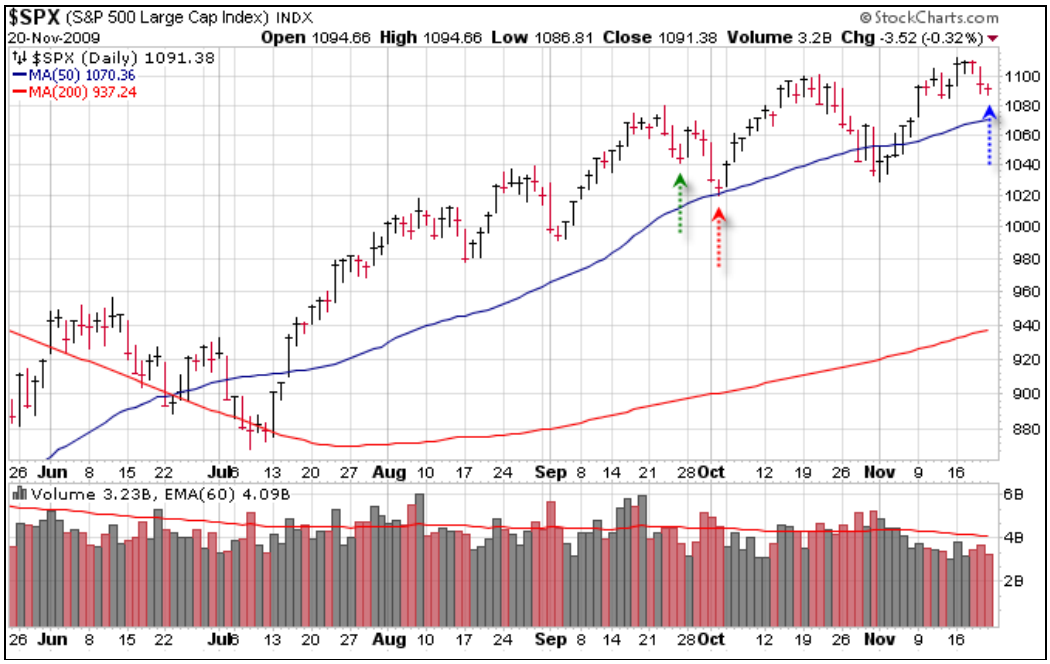
One thing is certain: as soon as the market reverses down, the squeezed stocks will fall back rather quickly, while the leading stocks might stay well above water.

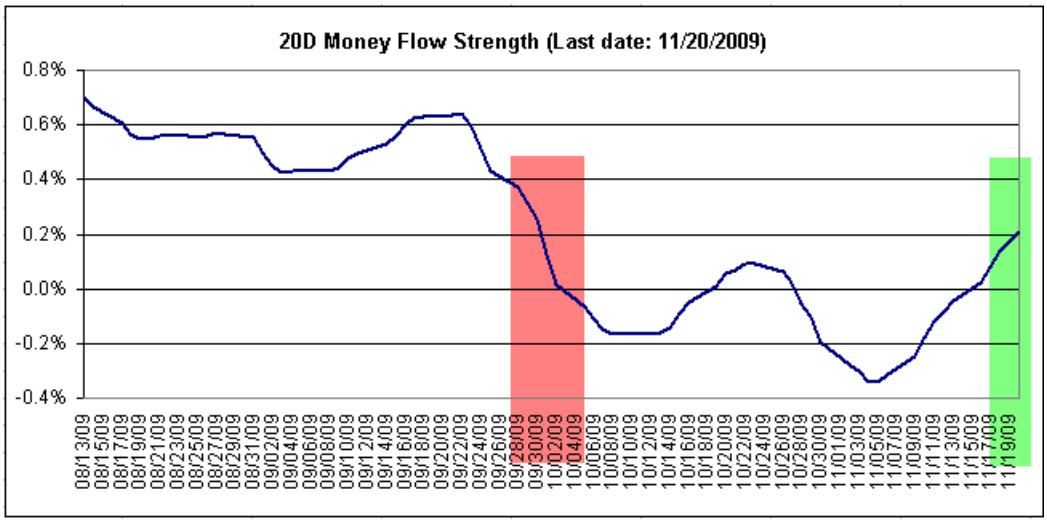
How to manage a technical bounce (Part 2)

I started the first training period on October 1 under the same market conditions: it was on a Friday and the market was showing a reversal, which was confirmed on the following Monday. (I invite you to re-read the page "How to manage a technical bounce" that I wrote at that time). Like many technicians, I like to look at the past to see similar market conditions and what their results were.

You can see in the two figures below that we had two similar positive reversals: a failure on September 26 (green arrow) and a successful one on October 3 (red arrow). It is impossible to tell whether this reversal (If it confirms on Monday) will be successful. The only thing we know is that today, the Money Flow is positive and we are starting a thanksgiving week which statistically has been positive for the markets.







How do we handle the market this Monday?

Do not forget that we are trading a probability. The above analysis shows that we have a good probability that Monday will be a positive day and then either the start of renewed up-trend or a bust.

When buying a stock, the best is to time the buying in conjunction to a support zone on the S&P500 (or on the SPY). Indeed, in the past few years, many stocks and sectors have moved up or down together with the market, as an increasing number of funds have used "baskets of stocks" such as the popular ETFs to take positions.

Our point of reference is the VWAP anchored on November 2nd, the start of the reversal. This level - 108.53 - coincides with the MR1 level of Billy at 108.57 and marks the "last line of defense" of this uptrend.

SPY
SPDRs
(c)monest.net
20 Nov 2009 C: 109.43 V: 132166040
-0.39(-0.36%)
Candles
Volume
--- anchored_candle_vwap(13) 108.53
--- sma(close, 50) 107.17
MR1: 108.57
Daily
111
110
109
108
107
106
105
104
103
102
101
100
99
300M
200M
100M
0
24
Sep
9
16
23
Oct
8
15
22
Nov
9
16

As you might have read in the published statistics, lately, large cap stocks have been attracting more money than the smaller companies. I would tend to "follow the flow of money" and stay with large names. I would avoid Chinese stocks as their MF pattern is not too good. The energy and PM sectors do not show the same positive divergence as other sectors. I would avoid them for now.

Last month, I would have said to first target leaders that are coming back to a value zone. Since many leading stocks broke down recently, the concept is more either to go after sectors/market ETFs or to target large caps stocks that are back to value.

The first general step in stock selections is to go to the filters section of the EV_Training group or to use the following link:

http://www.effectivevolume.eu/index_training.html

The above link takes you to the EV web site but with a different "filters" section. This section is reserved to the EV_Training traders.

What are we specifically looking for?

We are looking to buy stocks that have been pulling back in the past few days but that are not "broken down" (STEC, RIMM are broken stocks. They might move up with the market, but they should not be our main target, because as soon as the reversal reaches a resistance point, short sellers will pile again in these stocks).

The easiest first step is simply to visit the following list:

http://www.effectivevolume.eu/content/Reports/Willain_List.xls

As you might have noted, this list is ranked between 100 and 0. The ranking combines:
- The sector rank (as coming from Billy's sector ranking)
- The Active Boundaries (the measure of value)
- The Large Effective Ratio (the trigger)

Usually, you could buy stocks with a rank above 80 and you could short those with a rank below 20. Filters that meet these criteria are below

http://www.effectivevolume.eu/content/Filters/best_rankings.php

http://www.effectivevolume.eu/content/Filters/worst_rankings.php