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By Tom Aspray
Technician

Get In and Out of Trades at the Right Time

Japanese rice traders have used technical analysis and candlestick charts since the 17th century. Many traders spend so much time trying to remember the often complex names given to the individual candle chart formations that they miss the trade. The different names often cause confusion as they are not able to determine whether they should be buying or selling.

One of the simplest candle formations is the doji which is formed when the open and closing price are close to the same. In *A Candle Trigger for Market Bottoms* and *A Candle Trigger for Market Tops* I discuss the two very reliable doji trading setups John Person developed. After using candle charts for over 25 years I have found his method for generating doji-based buy or sell signals to be the most reliable candle chart setups I have ever encountered.

I have stressed the importance of only buying stocks that are performing better than the S&P 500 for quite some time. For those who trade the short side of the market, choosing the stocks that are acting weaker than the S&P 500 is the best strategy. In *Profiting from Multiple Time Frame Sector Analysis* I discuss how you can use this technical tool on the daily, weekly, and monthly data to identify both the strongest and weakest stocks.

For over 80 years, many successful investors and traders have realized that volume should play an important role in their analysis. In *Volume Always Precedes Price* I will show you how I use volume to gain valuable insight on whether the smart money is buying or selling. This can give you the opportunity to get in and out of trades at the right time as it is a distinct advantage to be buying or selling ahead of the crowd.

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Technician

A Candle Trigger for Market Bottoms

In the next trading lesson I discuss the low close doji formation (LCD) that was created by trader John Person, which is in his book *Candlestick and Pivot Point Trading Triggers*.

Of course, John also taught me about his high close doji (HCD) trigger, which I have found equally as valuable as the LCD, particularly when it is confirmed by the volume analysis. Since I was first exposed to this technique, there have been numerous times when I looked at a market that had dropped sharply or risen strongly only to realize that a LCD or HCD had been triggered at the turning point.

In this article, I will look at the HCD trigger in-depth and show how the use of multiple time frame OBV analysis can confirm the price action.

Just as the case with most technical methods, the signals from the monthly data are often the most powerful. They can often help one catch moves that last many months or even a year. This first chart of **Bank of America** (BAC) has two excellent examples of LCDs, as well as a HCD that formed in early 2012.

In April of 2010 BAC made a high of $19.86, a low of $17.41, and closed at $17.43. The following month (point 1) BAC closed at $15.41 which triggered a LCD. Over the next six months, BAC declined and eventually reached a low of $10.91. This was a drop of 29.2% from the May close.

BAC closed higher in December 2010 but the next month formed another doji, point 2. The pattern of the OBV was much different, as this doji was at the 2010 high, the OBV had also made a new high, so there were no negative divergences. Two months after the LCD was confirmed, the OBV dropped below its WMA.

As the doji was forming in January 2011, the OBV was just rallying back to its declining WMA (point 3), which is typically a very negative formation. The close in March 2011 was at $13.33, which was below the January low of $13.40. This therefore confirmed a LCD.

BAC closed December 2011 at $5.41, which was a drop of over 59% from the March close. That month BAC formed a doji with a monthly high of $5.95. In January 2012 BAC closed at $7.13, which triggered a high close doji or HCD. The risk was to under the December low of $4.92.

The monthly OBV formed a slight positive divergence at the lows and by the end of February 2012 had clearly moved above its downtrend, line a, and its WMA (see circle). At this point, the stop could have been moved to under the January low of $5.62.

Let's look at this same time period for BAC on a weekly basis. The chart shows that in the final week of 2011 BAC formed a doji (line 1). Over the prior six weeks, the OBV had been forming higher lows (line b) while prices had formed lower lows (line a). The OBV moved above its WMA a week before the doji was formed (point 3).

The doji high was $5.58, and the next week (point 2), BAC had a close of $6.18 and therefore triggered a weekly HCD. The stop would have been under the doji low of $5.27, making the risk much more favorable on the weekly HCD signal than it was on the monthly.

Of course, this method like the LCD can work on any market and by traders or investors. This daily chart of the **Direxion Financial Bear 3X ETF** (FAZ) provides quite a few good examples but I will focus on just two. On March 29, 2012, FAZ formed a doji as it had fallen from a high of $219.76 in November 2011 to a low of $79.80.

For both the LCD and the HCD, the most valid signals come after significant rallies or declines. Three days later, another doji was formed at point 1 with a high of $83.56. The OBV had already moved above its WMA, and the following day, FAZ opened at $84.28 and closed at $85.20, so a HCD was triggered.

Four days later, FAZ hit a high of $95.12 before it reversed course. By May 1, 2012, FAZ had a reached a low of $80.20 which was just above the late March lows at $79.68 and $79.80. Since there was no new low in price, a bullish divergence in the OBV was not possible but the OBV was acting stronger than prices as indicated by line c.

During the three days after the HCD was formed, FAZ rallied to a high of $95.20. But then, just two days later, it closed back at $85.84. Anyone who has traded these triple leveraged ETFs should accept that they are not for the faint hearted. If one is fortunate enough to get a double digit profit in just a few days, those profits should definitely be taken.

On May 2, 2012, another doji was formed (point 2) with a high of $85.64. The next day, FAZ closed at $86.08 so a HCD was again triggered. The OBV had moved above its WMA, and a couple of days later, it also moved through its downtrend, line b.

Just 11 days later, FAZ hit a high of $116.20 as the OBV was acting very strong. After a six-day correction, FAZ again

moved higher and briefly exceeded the 127.2% Fibonacci retracement target from the correction which was at $119.91. This also corresponds to chart resistance from March 2012, line a. The OBV did not confirm those highs as it formed a negative divergence, line d.

On this weekly chart of **Google, Inc.** (ALPHABET) (GOOG), I would like to concentrate on the doji that formed the week ending April 22, 2011, point 1. GOOG had corrected from its high at $642.96 in early January 2011 and had dropped down to form the doji between the 50% and 61.8% Fibonacci support levels. This was also well above the uptrend, line a.

The doji high was at $530.88, and the following week, GOOG closed at $544.10 triggering the HCD. The stop would have been under the doji low at $519. But what is missing from this analysis?

I hope that many of you noticed that in the prior commentary there was no analysis of the OBV. This is a good example of why I find the OBV to be such a valuable tool in determining the strength of both LCD and HCD triggers. Oftentimes, but not always, the OBV will help you identify the most worthwhile signals.

The chart below also includes what happened in GOOG in 2011, as well as detailed analysis of the OBV. It should have been apparent that while GOOG was making a new high in 2011 (point 2), the OBV was forming lower highs, line a. Weekly divergences in technical indicators like the OBV are generally quite significant.

The weekly OBV broke important support, line b, in early March 2011, which confirmed the negative divergence. This is highlighted by vertical line c. The lower lows in the OBV (point 4) confirmed that it had started a new downtrend.

As GOOG was rebounding in the middle of April (line d), which was just two weeks before the doji was formed, the OBV was acting very weak and making new lows. These were a series of strong warnings that this HCD was not going to work out. The stock dropped another $50 per share before it bottomed in June of that year.

Home Depot, Inc. (HD) was one of the bull market's big winners rising from a 2009 low of $17.49 to recent high of $71.45. In 2009 HD was making a gradual series of higher highs and in December 2009 the OBV finally broke through its long-term resistance at line a.

The OBV was in a solid uptrend for some time as HD closed in December 2009 near the year's highs. In January 2010, HD declined forming a doji at the end of the month, point 1. The doji low at $27.19 was just above the 50% Fibonacci support at $26.88, which made it a high probability entry level.

The doji high was $28.09, and the following week (point 2), another doji was formed with a close at $27.98 but a high of $29.05, so no HCD was triggered. The following week (line 3), HD closed at $29 triggering the HCD from two weeks earlier. A stop should have been used under $27.19, which was the initial doji low. The OBV also had broken its short-term downtrend, line c, which supported the bullish case.

The following week, point 4, prices started to accelerate to the upside. At the end of April 2010, HD peaked at $37.03. The OBV had peaked two weeks earlier and therefore formed a negative or bearish divergence, line d, at the highs. Three weeks later, the OBV dropped below its prior low, which confirmed the bearish divergence. Over the next ten weeks, the stock eventually dropped below the late January lows.

I closely follow the Select Spyder ETFs and have written about them frequently in the past "Best Sector Bets For New Year." When I see that a sector has bottomed out using both the OBV and relative performance analysis, it becomes a sector that I focus on for individual stock picks.

In the summer of 2010, the **Select Sector SPDR Energy** (XLE) was making lower lows, line a, as it reached $48.56 in early July of that year. The OBV bottomed in early June and was forming a positive or bullish divergence, line c. On the first rally off the lows, a doji was formed with a high of $54.72.

The next week XLE closed at $55.64 completing the HCD with a stop under the doji low of $53.23. The OBV just barely made it above its WMA on the rally before it reversed the next week as the stop would have been hit. This doji might have been excluded as it was formed after a three-week rally from the lows, not after a protracted decline.

Another doji was formed on the week ending August 27, 2010, point 1, with a high of $52.72 and a low of $50.33. The following week, XLE closed at $54.20 triggering the HCD with a stop under $50.33. The OBV completed its bottom three weeks later as the downtrend, line b, was broken confirming the bullish divergence.

For the next nine weeks XLE made higher lows, and while it formed a doji in early December 2010, XLE did not close below the doji low. In early March 2011, point 2, another doji was formed with a low of $76.29 and a high of $79.08. The following week XLE closed at $75.11 triggering the LCD. A stop above $79.08 should have been used.

This, of course, could also have been used as a signal to exit long positions, even though the OBV had confirmed the recent highs. After trading as low as $72.90, XLE rebounded sharply making a new high at $80.97 in early April 2011 with a new closing high of $79.99. Therefore, the stop would have been hit.

Four weeks later, XLE had a closing high of $80.48, which was not confirmed by the OBV as it had formed lower highs, line b. The following week, there was a bearish engulfing pattern on high volume, which confirmed the divergence and dropped the OBV below its WMA. The following week, the OBV made another new low confirming a downtrend and a major top. This was discussed in the May 2011 column "Big Oil's Big Top."

So how can you implement both the LCD and HCD into your analysis? There are several free services on the Internet that will allow you to scan for dojis. What I have done in the past is to run weekly and monthly scans for dojis as part of my watch list.

One stock that showed up at the end of April 2013 was **Procter & Gamble** (PG) when it formed what is called a gravestone doji as it opened the month at $76.85 and closed at $76.77 with a high of $82.54 and a low of $76.35. The monthly relative performance had formed lower highs, line a, which is a sign of weakness. The OBV on the other hand did break its downtrend above its WMA.

In the past, I have pointed out both the HCD and LCD when appropriate and I hope you will take the time on your own to see if it is something that can improve your results. I think it will and recommend that you also read John's article on HCDs, if you have not already, since he is the expert on their use.

A Candle Trigger for Market Tops

Some of today's most popular technical indicators or trading methods can be traced back to a specific inventor but they are often not given credit by today's traders and analysts. As an "old school technical analyst," I have always felt it was important to give the inventor the proper credit

Some of you may be familiar with what is referred to on most quote systems as the TRIN but should really be called the ARMS Index after its creator, Dick Arms. I fought this battle many years ago on the precursor to CNBC, and they did change it for a while, but it did not last.

That is the same reason that I have tried to give Joe Granville credit about on balance volume or Welles Wilder when I have talked about the RSI or ADX. I was first exposed to candle charts in 1989 when I was given a copy of *The Japanese Chart of Charts* by Seiki Shimizu during a speaking trip to Japan.

Though I found this book quite interesting, I did not really start to apply the methods until much later. At the time, candle charts were virtually unknown in the US, but over the next few years, Steve Nison and Greg Morris both wrote excellent books on candlestick charting. Then I was introduced to a candlestick formation that I have found to be one of the most valuable in identifying market tops or bottoms.

I have always been intrigued by doji formations, which is characterized by the open and close being at approximately the same value. It typically is interpreted as a sign of indecision but then John Person shared with me his high and low close doji triggers, which are in his book *Candlestick and Pivot Point Trading Triggers*. The HCD is also discussed in this article by John.

These do not form at many market highs or lows, but when they do, I have found them to be extremely helpful in determining both entries and exits. The low close doji or LCD will be the focus of this week's article and I will look at the high close doji or HCD in a subsequent article.

As with many technical methods, the longer time frame charts give the most reliable signals. Volume plays an important role in my work, and when volume analysis is added to the LCD signals, it often validates them, making the investor or trader even more confident. Of course, Joe Granville's on balance volume is my favorite volume indicator and it is particularly insightful when it is analyzed in multiple time frames.

In the upper left of the chart is a typical doji formation. When the close of the next candle is below the low of the doji, then a low close doji signal (LCD) is triggered. In order to be valid, John's method requires that the lower close must occur within three bars after the doji. For those selling short based on this trigger, a stop is placed above the doji or most recent high.

This monthly chart of the Dow Industrials shows that a doji (see circle) was formed in October 2007 as the Dow opened at 13,895, had a low of 13,407, and closed at 13,930. The high for the month was 14,198.

In November, the Dow Industrials closed at 13,371, which was below 13,407 so an LCD was triggered. On the bottom of the chart, it is evident that the volume increased in November 2007, point 1, which indicates there was more selling in November than there was buying in October of that year.

In this second chart, I have included the monthly OBV with its 21-month WMA. I have highlighted the doji at point 1. As I noted, the November close generated an LCD and the Dow also closed lower again in December 2007.

The close in January 2008 at 12,650 (point 2) was also below the prior two month's low. This weakness was confirmed by OBV as it dropped below its WMA (line 4) and its uptrend, line a, was also broken (point 4). The OBV stayed below its WMA until the end of July 2009.

The weekly chart of the **Spyder Trust** (SPY) covers from early 2011 though October 2012. The week ending May 13, 2011, point 1, a doji was formed. The OBV had peaked in early March of that year and then formed a bearish divergence, line a, as it was forming lower highs while SPY was forming higher highs.

The week the doji formed, SPY closed at $133.39 and the OBV dropped below support (line 2). This confirmed the divergence, point 2. The low of the doji was $133.39 and the next week another doji was formed with a close at $133.61. The following week, SPY closed at $133.51, which was still above the first doji low.

Finally, the week ending June 3, 2012, SPY closed at $130.42 triggering a low close doji as it was below the low of both dojis. The stop would have had been above the early May 2012 high at $137.18 and $137.86 would be 0.5% above the high.

The SPY eventually made a low of $107.43 in early October 2012. The rally continued until the end of March 2012 and while a doji did form in early 2012, there was never a close below its low. The week ending March 30, 2012, another doji did form, point 3, with a low of $139.09.

The following week, the SPY made a new high at $142.21 and then closed a bit lower but well above the doji low. However, the second week after the doji, the SPY gapped lower and closed the week at $137.14, which was well below the doji low.

The **Spyder Trust** (SPY) moved sideways for the following three weeks before it dropped sharply. The OBV stayed above its WMA until the week ending May 18, 2012, and in this instance, was not helpful in confirming the doji. The SPY made a low of $127.14 in early June of that year, and by the middle of the month, the OBV was back above its WMA.

One of the dominant stock stories of 2013 was the plunge in the stock of **Apple, Inc.** (AAPL). The weekly OBV of AAPL broke through its resistance (line a) in February 2011 as the stock accelerated to the upside.

As AAPL pushed above the $700 level in September 2012, it formed a doji (point 1) with a high at $705.07, which was very close to the quarterly R2 level at $705.21. The close the following week at $667.10 was well below the doji low of $693.62.

Two weeks after the LCD, the OBV dropped below its WMA and the next week it also broke its uptrend, line b. The OBV did not form any divergences at the highs and oftentimes it will not. The daily OBV also did not form any divergences but a daily doji was formed on September 20, 2012, and AAPL closed below the doji low two days later.

Next, let's look at a weekly chart of the **Vanguard MSCI Emerging Market ETF** (VWO), which formed a doji the week ending August 6, 2010, with a high of $43.04 and a low of $42.20 (point 1). The next week, VWO closed at $41.31, triggering the LCD. A stop 0.5% above the high would have been at $43.26. Over the next nine days, VWO hit a low of $40.06 before spurting to the upside with a high of $45, which would have hit the stop.

I included this example to reinforce the reality that nothing works all of the time but also to illustrate that all trades need to be managed when they move in your favor. The fact that the weekly OBV had moved above its WMA as the doji was forming might have kept you out of the trade.

At the end of April 2010, VWO formed another doji, point 1, and the following week VWO closed at $48.74, which was well below the doji low of $49.95. The formation of the doji was accompanied by the formation of a negative divergence in the OBV, line a, as it made significantly lower highs.

The OBV marginally broke its support, line b, several weeks before the doji was formed. After the LCD was triggered, the OBV dropped below support and its previous low (point 5).

The stop on a short would have been above the high from the week after the doji at $50.92. Seven weeks after the LCD, VWO stabilized in the $46 area and rallied as high as $49.65 before forming a second doji at point 4.

VWO plunged the next week and closed at $43.65, which was well below the second doji low of $47.61. By early October 2011, VWO had made a low of $34.21.

The **Powershares QQQ Trust** (QQQ) is a good example of how a weekly LCD can also be used to tell you when long positions should be sold. This is also true of the previous LCD examples.

Determining when to sell is often a very difficult decision for investors and an LCD can often protect more of your profits on a long position than a stop. The QQQ hit a low of $60.04 in early June of 2012 and by the week ending September 14 it hit a high of $70.43.

The uptrend in the weekly OBV, line a, had been broken two weeks earlier (point 1). The OBV formed a negative divergence at the highs (line b) and the week ending September 21, 2012, the QQQ formed a doji (point 2). The doji's low was $69.87, and the following week, the QQQ closed at $68.57, which was a LCD.

Two weeks later, with the close at $66.68, the OBV dropped below its WMA. If one had been looking just at the charts and was not aware of the negative OBV signals, the logical place for a stop would have been under the September 4, 2012 low at $67.42. So exiting longs based on the LCD could have saved you over $1 per share.

Of course, the same methods can be used on intra-day charts, but it requires much closer monitoring of one's positions. This 15-minute chart of the June 2013 E-mini S&P 500 futures reviews the trading from April 2 through April 4, 2013.

Between 5:30 and 6:00 am on April 3, 2013, the futures formed two dojis (point 1) with a low of 1567. Two bars later, the close was at $1566.50 generating an LCD. The doji high was at 1567.75 so a stop above 1570 would have been reasonable.

During the first 15 minutes of the regular session the support at line a was violated and one's stop could have been moved to breakeven or lower. By 11:00 am, the futures had dropped below the weekly pivot at 1555.75. Before the market close, the weekly S2 level at 1547 had also been reached. In terms of managing the trade, covering part of the position at the weekly pivot and more or all at the weekly S2 would have been an appropriate strategy.

When I am scanning charts, I almost always look at candles, and one of the things I look for are dojis. When recommending new long positions, I feel that the HCD formation, combined with the relative performance and OBV analysis, can increase the odds in your favor, but be sure you pay proper attention to the risk. In those instances, when a doji coincided with a divergence in the OBV, I have found that the signal is even stronger.

Profiting from Multiple Time Frame Sector Analysis

There is continued debate as to what sectors offer the best potential. It is important to look at each of the sectors from a monthly, weekly, and daily perspective in order to get a clear outlook whether you are a trader or investor.

The monthly charts, as I discussed in this Trading Lesson, can be very helpful in determining the major trends. They are also very useful in identifying key levels of support as breakouts of the monthly ranges are often quite significant.

In December 2012's Sector Stages 12-Year Breakout, I noted that the trading range in the S&P 500 Health Care Sector, that went back to 2000, had been resolved in 2012.

It is also important to look at both the weekly and daily analysis of the sectors. Often the negative readings from the daily analysis will allow one to spot good entry points when the weekly studies are positive.

Select Spyder Sector Review					
	1st Quarter	2nd Quarter	3rd Quarter	2013 Change	Oct. 2013
Financial Select Spyder (XLF)	11.1%	6.8%	2.4%	26.8%	4.4%
Technology Select Spyder (XLK)	4.9%	1.0%	4.8%	17.0%	5.4%
Industrial Select Spyder (XLI)	10.2%	2.1%	8.8%	28.3%	4.7%
Materials Select Spyder (XLB)	4.4%	-2.1%	9.5%	16.8%	4.4%
Energy Select Spyder (XLE)	3.3%	11.0%	4.5%	25.4%	4.6%
Consumer Staples Select Spyder (XLP)	14.0%	-0.3%	0.3%	22.0%	7.0%
Health Care Select Spyder (XLV)	15.4%	3.5%	6.3%	32.8%	4.7%
Utilities Select Spyder (XLU)	12.0%	-3.8%	-0.7%	11.5%	4.1%
Consumer Discretionary (XLY)	11.7%	6.4%	7.5%	33.3%	4.3%
Spyder Trust (SPY)	10.0%	2.4%	4.7%	23.8%	4.9%

First, let's look at the quarter by quarter performance for 2013, as well as how the Select Sector ETFs performed in the 4th quarter. Two of my favorite ETFs as we started 2012, the **Select Sector SPDR Health Care** (XLV) and the **Select Sector SPDR Consumer Discretionary** (XLY), were the top gainers in 2013.

They were up 32.8% and 33.3%, respectively, and both showed solid gains for the month of October. The **Select Sector SPDR Health Care** (XLV) registered the best quarterly gain as it was up 15.4% in the first quarter.

One of the 3rd quarter's weakest performers, the **Select Sector SPDR Consumer Staples** (XLP) had done the best in October as it showed a gain of 7.5% through October 30, 2013. The **Select Sector SPDR Materials** (XLB) was lagging the S&P 500 in the first half of the year, with its small gain of just 2.1%, but rebounded nicely in the 3rd quarter as it was up 9.5%.

It is also surprising that the **Select Sector SPDR Technology** (XLK) was one of the worst performers in 2013 as it was up just 17% through September of that year. So which sectors looked the best for the long-term and which appeared to show the best intermediate-term opportunities?

The first step in the process is to look at the monthly relative performance and on-balance volume analysis for each of the sector ETFs. There are only two, the **Select Sector SPDR Health Care** (XLV) and the **Select Sector SPDR Consumer Discretionary** (XLY), where the monthly relative performance made new multi-year highs in past months.

The monthly chart shows that the **Select Sector SPDR Health Care** (XLV) made higher highs in nine of ten months. The quarterly R2 resistance was at $53.20 (see table) with the monthly starc+ band for November 2013 at $55.00. The R2 resistance was at $55.18.

The monthly relative performance made new highs in July 2013. The monthly OBV (The Best Volume Indicator) broke through year-long resistance, line c, in March 2012 and made a new high in October of that year. It was well above both its steep uptrend (line d) and its rising WMA.

The daily studies exhibited some signs of weakness as the OBV showed a negative divergence going back to the September 2013 highs while the RS line was locked in a trading range. There was first good support in the $49.50-50.20 area.

Within the healthcare sector, there are two major sub-sectors and industry groups. In 2013, some were acting stronger than the major sector while others were weaker. The **DJ US Pharmaceutical & Biotechnology Index** (DJUSPN) was up 36.5% for that year. That was just over 4% better than the XLV but almost 13% better than the **Spyder Trust** (SPY).

This weekly chart from 2013 shows an upward sloping channel, lines a and b. The resistance is at 545, line a, and the weekly starc-+ band. For November of that year, the monthly starc+ band was at 549.20 and there was good support in the 500-520 area.

The relative performance peaked in April 2013 and did not confirm the new highs. It was still above its WMA and support at line c. The OBV did seem stronger as it looked ready to make a new high after testing its steep uptrend, line c, well above its WMA. The daily studies (not shown) failed to confirm those highs.

The **DJ US Health Care Providers Index** (DJUSHP) peaked at 862 in September 2012 and it was down 5.3% from the highs. In 2013 it was up 27%.

At that time, the weekly starc- band was at 782 with the 38.2% Fibonacci retracement support at 757. The 50% retracement support was at 722. The weekly relative performance did confirm the September 2013 highs but formed lower highs, line e, before breaking its support. The RS line then tested its longer-term uptrend, line f.

The weekly OBV also confirmed the new price highs and showed no signs of a top as it turned up from its WMA. The weekly OBV broke through resistance at line g early in 2013. The daily technical studies are solidly in the sell mode and have been since the first week of October 2012 with the OBV showing a series of lower highs and lower lows.

This monthly chart of the **Select Sector SPDR Consumer Discretionary** (XLY) shows the close above the major monthly resistance, line a, at the end of September 2013. It closed higher for every month in 2013 with the starc+ band for November at $65.47. The next quarterly R1 resistance was at $65.04, so that was the next upside target zone.

The monthly relative performance bottomed in February 2009 and then stayed above its rising WMA. It also held well above the support, line c, that connected the 2009 and 2012 lows.

The monthly OBV formed a nice bottoming formation in 2012 (see circle) and then blasted through resistance at line d in April 2013.

The weekly analysis (not shown) was also clearly positive as the rising 20-week EMA was tested during the early October 2013 correction. The daily analysis on the XLY did show some minor divergences but it would have taken a drop in the OBV below the early October 2013 lows to suggest a deeper correction was underway. There is initial support now at $61.50-$62 with the quarterly pivot and more important support at $59.79.

The consumer discretionary sector includes companies in a wide range of industry groups such as automobiles, auto parts, retail, specialty retail, media, as well as hotels and restaurants. I found the best breakdown of the industry groups and the stocks that are in them on Bloomberg (here is the link).

The only liquid ETF that follows this sector is the **SPDR S&P Retail** (XRT). It has 98 stocks and is well diversified with the ten largest holdings making up just 11% of the ETF. The monthly chart (not shown) continued to act very strong as both the relative performance and OBV were positive and well above support.

This weekly chart of XRT shows that it tested and held the rising 20-week EMA on three occasions since June 2012. It then stood at $80.12, which was below the quarterly pivot at $80.99. The October 2013 low was $79.11.

The August 2012 highs were exceeded with a high at $85.04. The weekly starc+ band was at $87.75 with trendline resistance, line a, at $88.88. The monthly starc+ band was $89.97. The relative performance showed a clear pattern of higher highs but then it was back below its WMA. A decisive break below the RS line, below the lows going back to May 2013, would have suggested it was no longer a market-leading sector.

The OBV exceeded the highs that were made in early August 2013. The WMA then flattened out a bit and the uptrend, line d, represented good support. The bullish readings from the monthly and weekly OBV meant the multiple time frame OBV analysis was positive.

The daily studies did not confirm the highs as the OBV failed to surpass both the August and September highs.

The third best performing sector for 2013 was the **Select Sector SPDR Industrials** (XLI) as it was up 28.3% and was recommended on September 16, 2013. The ETF approached the quarterly R1 resistance at $49.02. For November, the starc+ band was at $50.75 and the chart showed a nice pattern of higher lows, line a.

There was minor support at $47.50-$48 and the September highs. The quarterly pivot was at $45.66 with the rising 20-month EMA at $40.99.

The relative performance was rising solidly well above its WMA. The RS line was well below the highs made in 2011. The downtrend, line b, was broken at the end of August 2013 suggesting that this could have been a market-leading sector in 2014. This would have been consistent with an economy that, at the time, was continuing to get stronger.

The weekly analysis from 2013 (not shown) was positive but the ranges were narrow so a doji could have formed. A close below this low could have triggered a LCD sell signal.

The daily studies showed no signs of a top and this meant that the first support at $47.50-$48 should have held on a pullback.

The **Select Sector SPDR Financial** (XLF) has also had a good year in 2013 as it was up 26.8% despite the problems of some big banks like **JPMorgan Chase & Co.** (JPM) that year. The monthly chart shows a narrow range over four months with a low of $19.34 and a high of $21.04. The major 50% Fibonacci retracement resistance from the 2007 high of $38.15 was at $21.95 with the 61.8% resistance at $25.77.

The quarterly pivot for XLF was at $20.11 with the 20-month EMA at $17.84. The monthly relative performance needed to move above the resistance at line a, to complete a major bottom formation.

The weekly analysis (not shown) was split as the relative performance was in a clear downtrend, indicating this was no longer a market-leading sector. The OBV, on the other hand, did make a new high well above its rising WMA. The daily OBV turned lower but did surpass the September 2013 highs on a rally.

I focused on the energy sector as the **Select Sector SPDR Energy** (XLE) showed a very positive monthly OBV pattern while the relative performance was still below its WMA. The weekly analysis was mixed, which suggested that while the sector should have continued to do well, it was not yet a market leader.

This is similar to the 2013 outlook for the **Select Sector SPDR Materials** (XLB) as its OBV looked good from both a monthly and weekly perspective but the relative performance analysis did not indicate that it was a leader.

The **Select Sector SPDR Technology** (XLK) looked ready to break out on a monthly basis in October of 2013 but the monthly relative performance was still well below its WMA. The weekly analysis did look better and the RS line was very close to completing its bottom formation. The monthly and weekly OBV charts looked very strong and suggested that accumulation was taking place.

If you want to develop your own sector-based strategy, I would suggest that you set aside an hour or two each weekend to do your own research. Look at what the sectors did for the week and whether any significant support or resistance levels were broken. Also, examine the weekly candle charts for any signs of a change in the trend.

Volume Always Precedes Price

This statement is one of the cardinal beliefs held by most technicians. It first came to my attention in the late 1970s when I read Joe Granville's book *New Strategy of Daily Stock Market Timing for Maximum Profit*, where he wrote "stocks do not rise in price unless demand exceeds supply. Demand is measured in volume and thus volume must precede price."

In the early stages of my career, I did extensive testing of this concept and developed my own methods of interpreting the on-balance volume. It is the volume indicator in which I have the most confidence. Over the years, I have explored the OBV in more detail and have discussed multiple time frame analysis of the OBV in The Best Volume Indicator.

In that article, I discussed the long-term bottoming and topping formations in the OBV and why the relationship of the OBV to its 21-period weighted moving average can be so important. I touched on the bullish and bearish setups that I have often observed with the OBV, which is the focus of this trading lesson.

Catching a major low in a stock or ETF is often difficult given the huge number of issues that are traded. I feel that tops are identified more frequently as after a long rally phase, a stock is often watched more closely. Therefore, changes in the volume and price patterns are noticed by more analysts.

In many instances, the OBV will form a positive divergence at a major low but sometimes it does not. These divergences can be explained by a transition where the demand starts to gradually exceed supply as prices reach a low point. Negative divergences at a top are a result of the fact that fewer buyers (lower volume) are pushing prices higher.

Hewlett Packard Co. (HPQ) was one of the least-favored stocks for 2013, but turned out to be one of the winners. On this monthly chart of HPQ, I have included the OBV and volume under the candle chart along with what I call Aspray's OBV Trigger (AOT). It is a histogram plot of the spread between the OBV and its 21-period WMA.

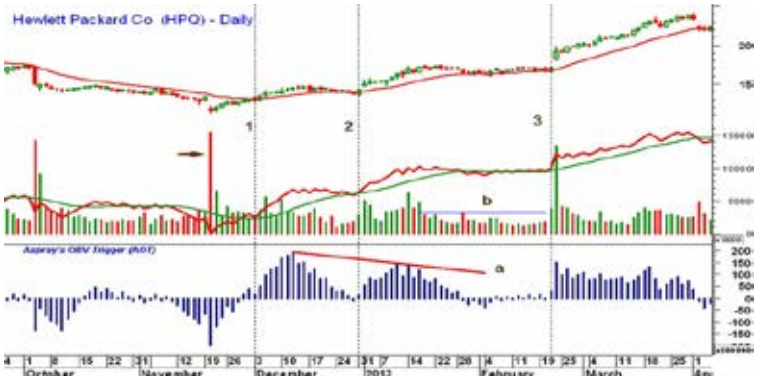
The AOT will often trigger a buy or sell signal by flipping above or below the zero line but it can also identify long-term divergences in the volume patterns that are not evident using the OBV.

As HPQ was making its high in March 2010, the monthly OBV was also making a new high (see arrows). However, the OBV was closer to its WMA, causing the AOT to form lower highs, line b. At the end of June 2010, the AOT first dropped below the zero line. It did reverse the following month, but then triggered a sell signal as it dropped sharply with August's high volume.

In November 2010, the long-term uptrend in the OBV, line a, was tested before HPQ managed a weak rebound over the next two months. This presented an excellent opportunity to get out of long positions or to sell short as the OBV rallied back to its declining WMA (line 1). The AOT never turned positive on the rally and turned lower the following month, giving advance warning of the break in the OBV trend line support, line b.

The AOT hit its lowest level in September 2011 when HPQ traded down to $21.50. The final price low at $11.35 was not made until November of 2012. The OBV made a new low with prices but the AOT formed higher lows, line c, indicating that the selling pressure was not as strong as it was in 2011.

The daily chart gives a different perspective of the November 2012 low when the daily volume spiked to over 154 millions shares as HPQ gapped to the downside, which in hindsight, was the final stage of the panic liquidation. Six days later, the daily OBV moved back above its WMA but soon pulled back to its WMA. The AOT was above the zero line and also corrected but stayed positive. The next day, it turned higher suggesting that the pullback was over.

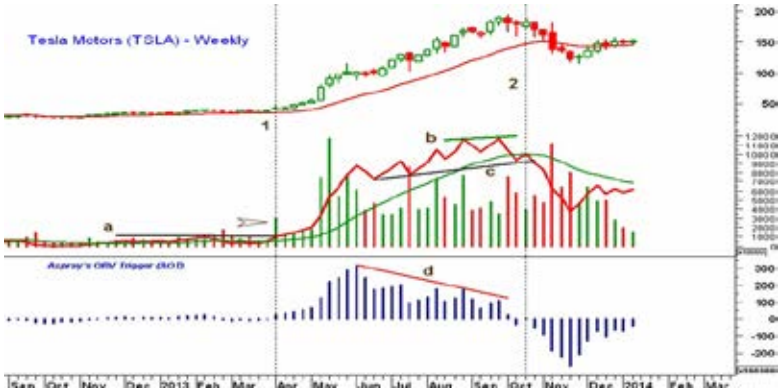


The AOT peaked on December 12, 2012, as HPQ corrected for about two weeks, eventually dropping slightly below its 20-day EMA on December 28 of that year. On that day, the AOT dropped below zero but reversed to positive the following day, line 2. Those who went long before the close were rewarded as the following day HPQ was up 5.4%.

If you are looking to buy a stock or ETF on a pullback, this approach works most of the time. Just wait until the OBV has dropped back to or below its WMA, then watch, and if the stock is higher the next day or week, you can go long especially if the volume has increased. Alternatively, you could go long on a buy stop above a recent high.

In early 2013, the AOT formed a longer-term divergence, line a, and by the end of January, had turned negative. This was the start of a 24-day correction, though surprisingly, there was only one daily close below the 20-day EMA. The volume in February 2013 was low, line b, and the OBV moved above and below its WMA.

Then on February 21, 2013, (line 3), the volume increased to 37 million from an average of 15 million the prior ten days. This moved the OBV out of its range, and the AOT rose to its best level in a month. HPQ closed up over 12% the following day.



One of the hottest stocks for a good part of 2013 was **Tesla Motors** (TSLA). Any news related to its cars quickly moved to the front page in the financial press. From a technical perspective, the volume surge the week of April 5, 2013 (line 1) was very bullish. The OBV moved above the February high, line a, as TSLA formed a doji, closing at $41.37. The AOT was clearly positive but still below its prior peak.

The stock continued higher the following week, closing at $43.75 with both the OBV and AOT improving sharply, confirming the bullish outlook. From the weekly chart, there was little in the way of a pullback over the next seven months as TSLA made a high of $194.50 in early October 2013.

The OBV did confirm the highs, line b, but dropped below its WMA two weeks later. The AOT peaked in May 2013 and then formed divergences (line d) both in August and late September of that year, just before the price highs. The week after the AOT turned negative it bounced back to slightly positive as the OBV moved barely above its flat WMA, line 2. A sell signal was confirmed two weeks later as the OBV support at line c, was broken. Despite the rally, the AOT stayed negative.

In late 2013, the daily chart of **Cablevision Systems** (CVC) was a good example of a daily buy set-up. The stock had been in a well-established downtrend from the August high of $20.16. The OBV was in a clear downtrend, line a, and was forming lower lows (line b). CVC formed three consecutive dojis in late November before the strong surge on November 21, 2013.

The volume was the heaviest since February as the OBV moved above its WMA and the AOT had its highest reading since August of that year. Three days later, the OBV broke through its downtrend (line a) but many probably thought they had missed their opportunity to buy.

CVC had closed above its daily starc+ band and continued to test it for the next two days (point 2). This was a sign to wait as CVC was in a high-risk buy zone. Just four days later, CVC had corrected back to its 20-day EMA. The AOT bottomed eight days later, line 2, but did not drop below zero.

The WMA of the OBV was clearly rising and the 20-day EMA was tested for three more days before CVC again turned sharply higher. It gained over 12% in the next two weeks. CVC has dropped five days from the highs with the AOT now negative.

Cray (CRAY) was a stellar performer for two years as it was up 142% in 2012 and 72% in 2013. It was up over 16% in 2014 as the weekly chart shows the strong close in October of that year.

In 2014, the volume was leading prices since 2012 as the AOT moved firmly back above zero in August of 2012, and the OBV broke through its resistance (line a) the following month. During the post election sell-off in November 2012, the AOT dropped below zero for one week before flipping back to positive (line 1).

In early April of 2013, CRAY hit a high of $23.59 but then reversed to close the week lower and below the prior week's low. On a weekly chart, this is a sign of weakness that is almost always followed by a further decline. The OBV did form a slight negative divergence at the highs (blue line) but the AOT did not drop below zero until May 2013.

This plunge in May was in reaction to disappointing earnings as CRAY dropped to between the 38.2% and 50% Fibonacci retracement support levels calculated from the early 2012 lows. This area is typically a good buying zone in a correction. The AOT dropped below the zero line for two weeks before reversely sharply (line 2) as an HCD buy signal was generated.

Less than three months later, CRAY was making another new high at $28.58. There was no clear divergence at the highs though the AOT did peak a week early. The AOT drifted lower for the next 12 weeks, finally dropping below the zero line for two weeks in November 2013. The volume was strong the following week (line 3) and the OBV moved back above its WMA. Buyers had another chance in December 2013 as CRAY dropped below its 20-week EMA while the OBV just tested its WMA (point c).

Of course, the AOT works in any market as long as they have adequate volume. The monthly analysis of the **Spyder Trust** (SPY) and **PowerShares QQQ Trust** (QQQ) turned back to positive July 2012 while it was positive all year for the **SPDR Dow Industrials** (DIA).

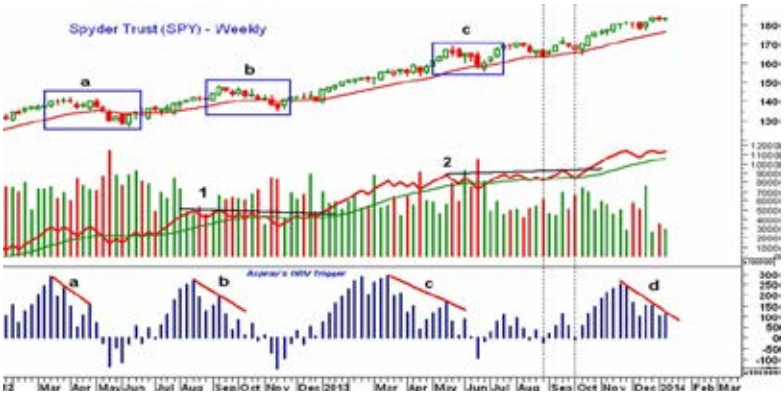
The **PowerShares QQQ Trust** (QQQ) had a sharp sell-off in the fall of 2012 as it peaked in mid-September along with **Apple** (AAPL). The QQQ triggered an LCD the week after the highs and the OBV formed a short-term negative divergence, line a.

The AOT peaked in August and then formed lower highs, line b, and by early October dropped below the zero line. On the volume chart, the selling was quite heavy over the next four weeks as the OBV dropped well below its WMA. By late 2012, the OBV and the AOT had gradually improved as indicated by line c.

In early February of 2013, the AOT moved above the zero line for two weeks before turning negative. The positive signal the following week (line 2) was supported by higher volume than the prior two weeks. The rally over the next nine weeks was gradual, though it picked up steam in early May.

From the May 2013 high at $74.95, the QQQ had a four-week correction that took it back to its rising 20-week EMA. The AOT dropped below the zero line for one week (line 3) in June of that year as the 20-week EMA was tested. In early August, the OBV had failed to move above the highs from earlier in the year and oscillated above and below the zero line. The AOT twice dropped below the zero line (see circle).

The insert of this period shows that the OBV formed a zig-zag pattern during this period as it moved above and below its WMA. The uptrend from the late 2012 lows, line d, was tested but it did hold. The volume increased over the next few weeks, and by September 20, 2013, the OBV had broken out to convincing new highs.



The weekly chart of the **Spyder Trust** (SPY) shows that divergences in the AOT can often also warn of overall market corrections. For example, the AOT peaked in the middle of March 2013 and then started to diverge as prices continued to move higher. The lower close the week of April 13 confirmed that a correction was underway.

From the high to low, this was a correction of 10.5% as by the second week in June, the AOT had moved back above the zero line. The market internal indicators, like the McClellan Oscillator, turned positive soon after the lows in early June.

By July, the OBV had broken out to the upside but started to flatten out by early September as the AOT formed lower highs, line b, while SPY was making new highs. In late October, the OBV dropped below the zero line and it was quite choppy over the next eight weeks. By early in 2013, the OBV had broken out to the upside as resistance at line 1 was overcome.

The OBV on the **Spyder Trust** (SPY) made a series of higher highs and higher lows since early in 2012, which is consistent with a positive major trend. It did warn of a correction in the spring of 2013 as the AOT peaked on March 15 and formed a significantly lower high in May (line c). This resulted in a five-week pullback to the 20-week EMA and a drop of 6.4%.

The SPY made a further new high in August but the OBV did not as it dropped below its WMA several times from August through early October 2013. The OBV finally staged an upside breakout in the middle of October as OBV resistance at line 2 was overcome.

The OBV rose well above its rising WMA but the AOT formed lower highs as it peaked in late November of that year. This increased the chances of a correction as a drop below the December lows in the OBV would be negative. Alternatively, the OBV needed to move above the late November and December peaks to reverse the deterioration.

The OBV and AOT analysis needs to be combined with a careful analysis of support levels, and as always, close attention to the risk. I have found that the monthly and quarterly pivot point analysis, using the methods of John Person, works very well in identifying levels of support.

Oftentimes, these levels will match up well with Fibonacci support levels. After a positive trigger, it is sometimes better to establish a new long position on a buy stop above the market. In the column "3 Buy Setups in a Lagging Group" I identified three trades in the homebuilding sector that had bullish setups after the previous day's close.

Like most technical methods, the set-ups are much more reliable when observed on the weekly or monthly charts.

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