Near-Term Correction Probable

***e*Research Corporation** is pleased to provide an article by Keith Richards of **VALUETREND**.

In this article, Mr. Richards provides three reasons why he believes the market is due for a correction very soon.

This article was written prior to the market opening on Monday. At the Monday close, the S&P 500 had dropped 0.67% and the S&P/TSX Composite had fallen 0.89%. As I write this late-morning on Tuesday, the S&P 500 is off 0.77% and the TSX is down 0.66%. Mr. Richards, you are very prescient!

The article is reproduced below, beginning on the next page, or you can go directly to it at the following link: ***http://www.valuetrend.ca/neartermed-correction-probable/***

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Monday, January 29, 2018

Near-Term Correction Is Probable

By: Keith Richards (bio at end)

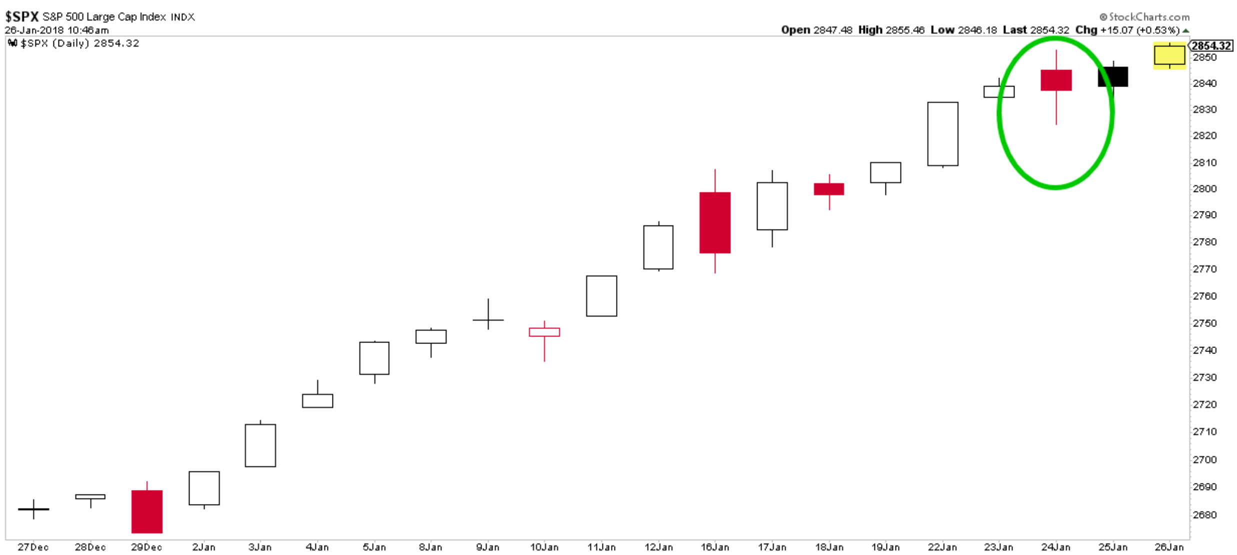
I have beaten the subject of an overbought market to death lately, so no need to rehash on my mid- to long-term chart observations. Visit **this blog** or **this blog** or **this blog** to get a clear picture of what I believe might be the longer-term picture.

Today, I would like to look at the real nitty gritty stuff. We will start with a basic candlestick formation that the S&P 500 has been showing over the past few trading days. The spinning top is a formation signalling confusion in the market. High wicks with a small body in the middle tell us that market participants were excited and buying at one point during the day, then scared and selling during another point of the day, but ultimately decided to close the day pretty close to its opening price. Big emotional swings create tall wicks and long tails.

Note on the chart below the high and lows of January 24th in particular (green circle). This is a classic spinning top. The 23rd and 25th were also small bodied days, but did not truly look like spinning tops. Nonetheless, you can see the confusion of late via these candlesticks.

If the market puts in a classic reversal candle such as a "hammer" or inverted hammer (which is very powerful as a market top signal), or something like an "engulfing pattern" or an "evening star" (also known as an island reversal), we could see a near-term pull-back for the S&P 500.

Please read my book *Sideways* for the basics on these and other candlestick patterns.

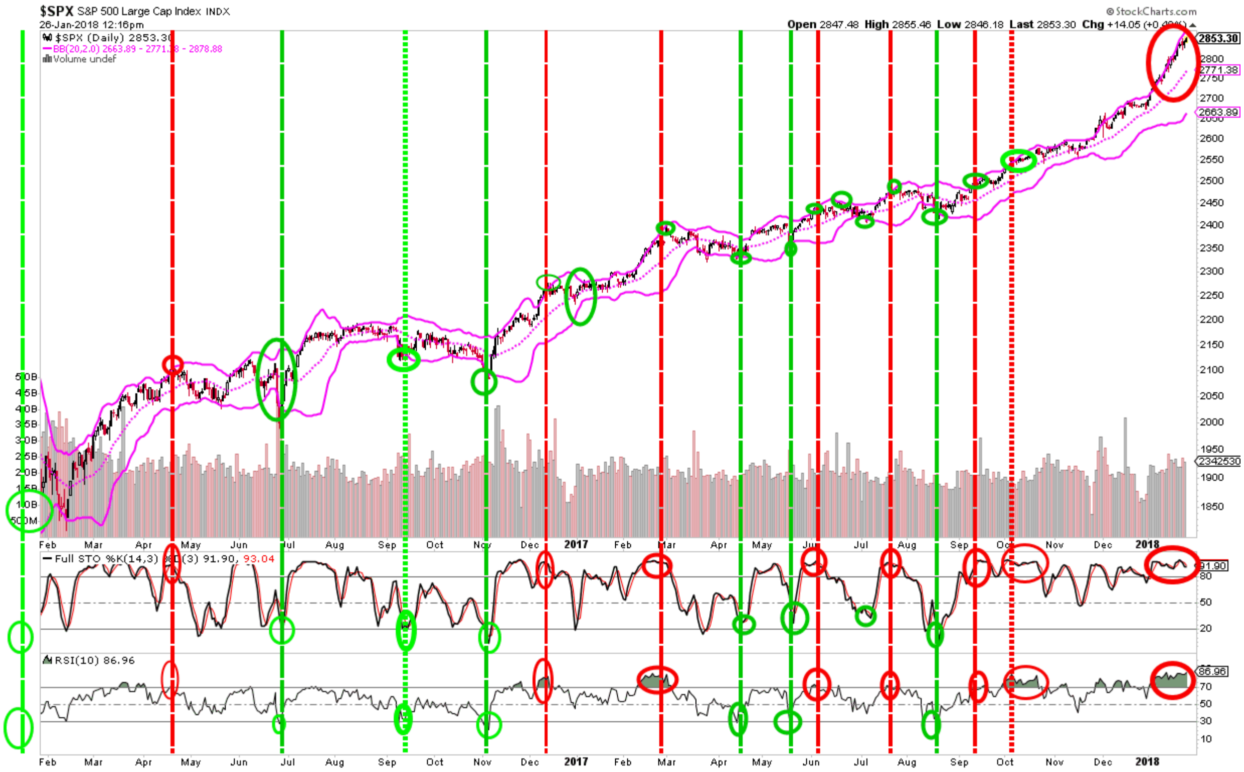


Now, let us look at the S&P 500 vs. the 200-day SMA (simple moving average).

As of Friday, it was 12.5% over the 200-day SMA. I have done studies on the markets when they are 10% or more above their 200-day (or 40-week) SMAs. The net result is that markets tend to consistently retract to a point of less than 10% above the 200-day SMA if they remain over that level for any period of time. This retraction to a sub-10% 200-day SMA level can occur via a sideways action, or a correction. The current level of the market versus this key MA suggests a retraction is imminent.

Finally, let us look at my short-term timing system. This system employs Bollinger Bands, stochastics, and RSI to measure if the market is likely to pull back or rise.

The indicators must trigger overbought or oversold conditions concurrently to issue a buy or sell signal. For the latter half of last year and into this year, we have witnessed a condition of perpetual overbought markets. So, my short-term timing system was of no benefit in catching swings. In fact, there have been no swings for the better part of a year.



Having said that, let us look at the conditions on this short-term timing system now. Will the perpetual motion machine that has been the market take a breather?

Note on the short-term timing chart that the levels of RSI and stochastics are particularly stretched right now. They are exceedingly higher than they were last year. This makes sense, given the parabolic jump the market has taken of late. Despite the market's ability to brush off the overbought conditions of last year, it is likely that the current mega-overbought conditions are unsustainable.

Conclusion

In a nutshell, we have some candlestick formations that are signalling a change in market psychology. We have a market that is stretched over its 200-day SMA that has historically never held for too long. And we have some short term indicators that suggest markets are vastly overbought.

All in, I would bet that we are due for a healthy, much-needed near-term correction very soon.

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See **About The Author** below.

ABOUT THE AUTHOR

ValueTrend Founder and Owner, Keith Richards, has been in the securities industry since 1990. ValueTrend manages over $100 million through a discretionary investment service for high-net-worth clients.

Keith Richards has been in the securities industry since 1990 and is a highly regarded member of the small, exclusive community of Chartered Market Technicians in Canada. Mr. Richard's articles appear regularly in INVESTORS DIGEST, MONEYLETTER, GLOBE AND MAIL, and the TORONTO STAR newspapers.

His appearances on BNN Television have inspired producers to acknowledge him as **"one of [our] most accurate technical analysts."** Mr. Richard's first book, SMARTBOUNCE: 3 ACTION STEPS TO PORTFOLIO RECOVERY, is available in bookstores and directly through his blog page www.valuetrend.ca/blog/. His second book, SIDEWAYS: USING THE POWER OF TECHNICAL ANALYSIS TO PROFIT IN UNCERTAIN TIMES was released in late 2011. He has been critical of the commission-based, follow-the-pack approach to investing – where brokers succeed regardless of performance.

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