The Harmonic Trader Report Monthly

October 2015

"Patterns into Profits!"

October 12th, 2015

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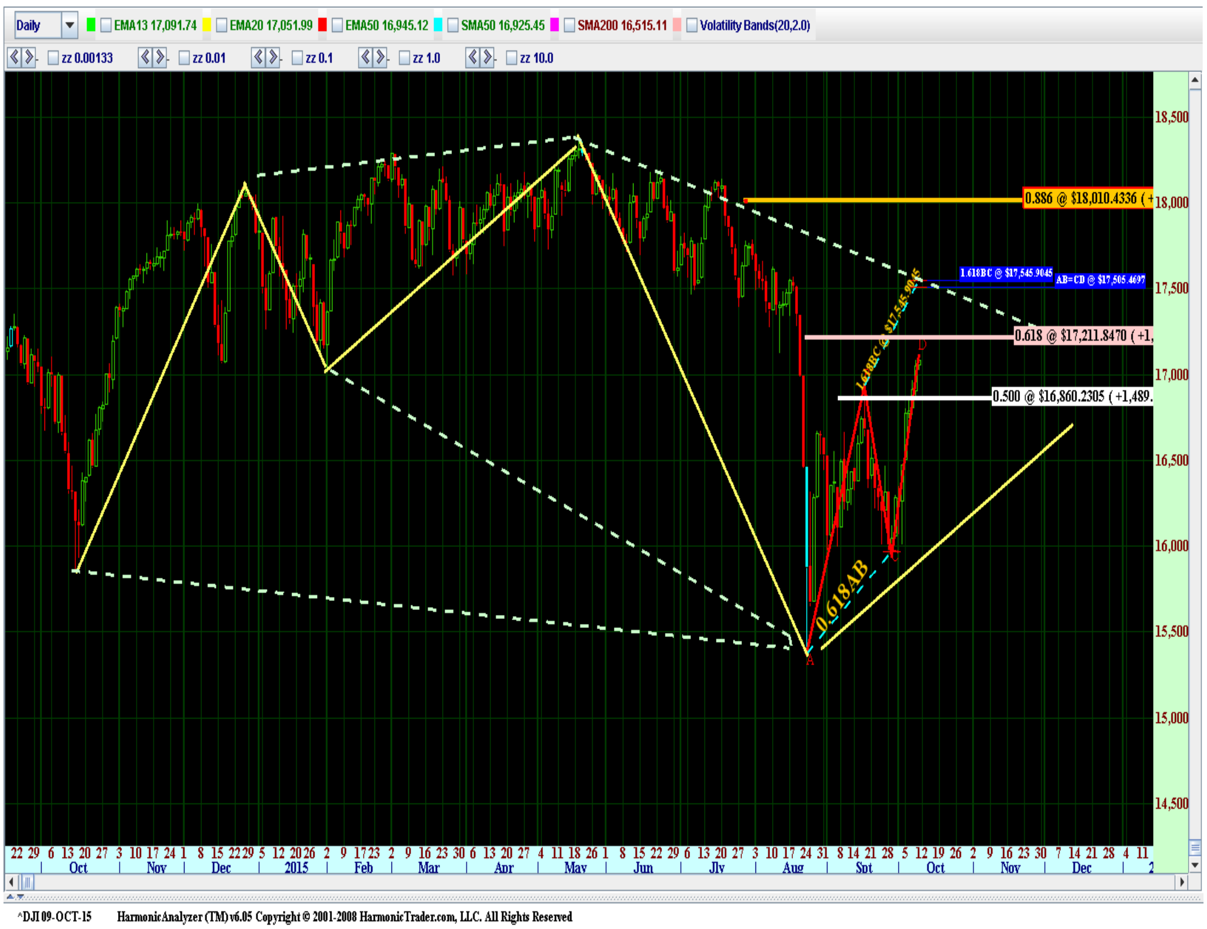
House of BRICs

For quite some time, we have addressed many substantial structural signals that are unfolding currently. The most compelling of these assessments are the overwhelming harmonic patterns in the NASDAQ and the SP500. Now the Dow Jones Industrial Average is triggering technical breakdown signals that most people understand. The German DAX and XLE Energy ETF are showing signs that further retracement is required to resolve their current downtrend. Less significant but still important to U.S. markets, the BRICs are dead with Brazil down 80% from its all-time high, Russia ditto, India not as bad at 30% and China 60- 70% lower.

The other disconcerting technical fact of these recent breakdowns is the inability to recover much of the 2008 losses - especially in China. These are long-term technical breakdown. It seems that the NASDAQ, S&P 500, German DAX and Dow Jones Industrial Average are the few remaining long-term bull markets that still have yet to retrace in earnest. I do believe that the German DAX is starting to crack. It is not a good sign when a market peaks out the way it has and retraces so quickly to a 38.2% pullback. I addressed that market in last month's report. This is a clear case where the simple consideration of time can signal the severity of the move at hand. Although this initial breakdown will require several more months to completely confirm the larger move at hand, the rapidity and severity of this year's action, in particular when the DAX index peaked at 12,200 and retraced 20% quickly thereafter suggests that the rally itself was severely flawed. The same can be said for China, Russia and Brazil. Fueled by the surging price of oil a decade ago, these countries wasted their resources and their markets have paid the price.

Although there are many prevailing theories of the economic issues plaguing global growth, it is clear that the repricing of assets remains in this readjustment phase that will require many months to establish fair valuation. Over the past six months, this process spread from Emerging markets to Asia and now Europe with the U.S. equity indices in a perfect position to rollover on the long-term charts with precise daily triggers at hand.

Dow Jones Industrial Average (^DJI): Daily
Bullish Shark>Bearish 5-0 with Bearish AB=CD

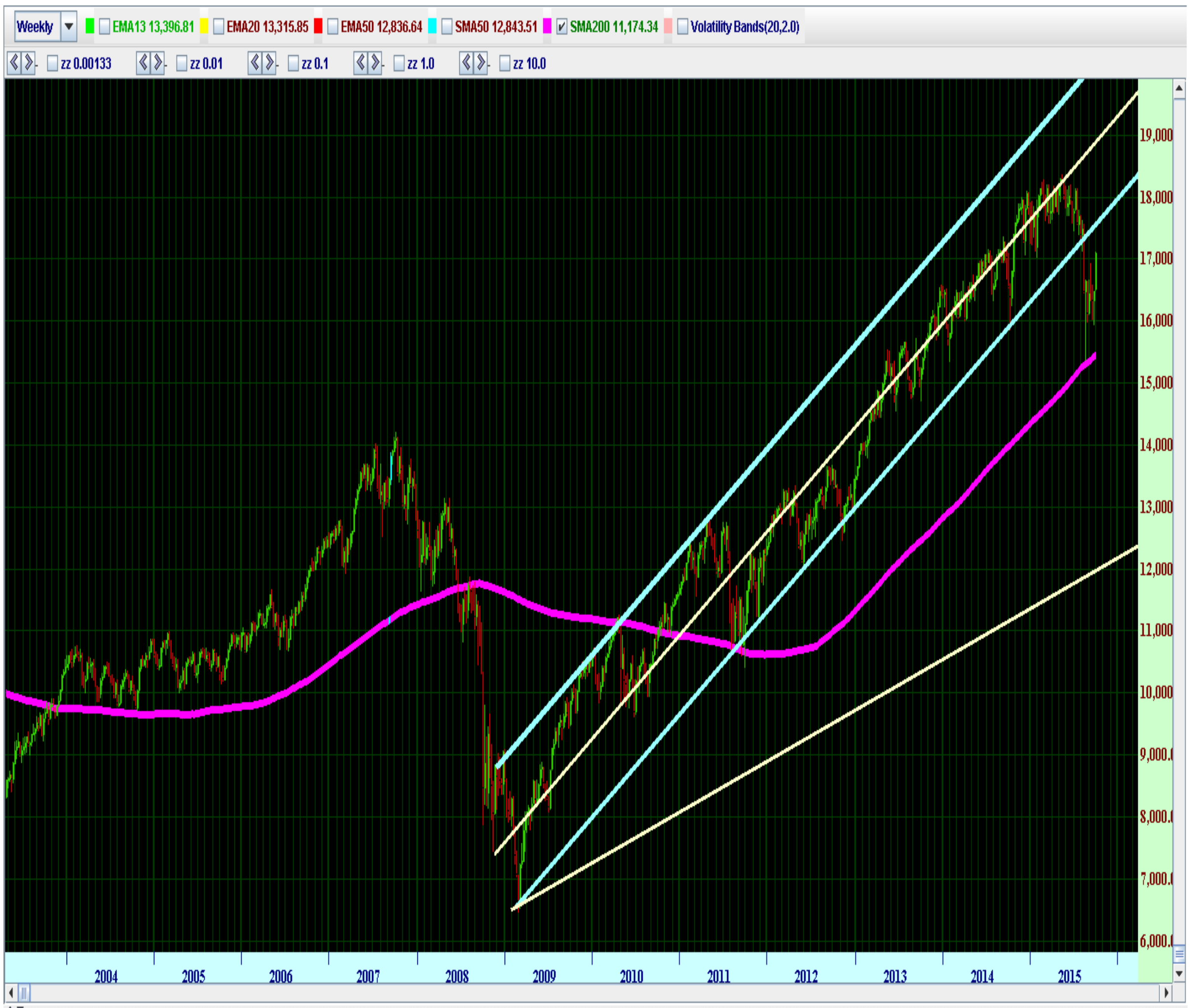


Although I have not reviewed the Dow Jones Industrial Average recently, the index has followed a similar structure as the S&P 500. Although the Industrials exceeded last October's low, the index formed the same Bullish Shark structure. These patterns typically retrace to test a 50% bounce of the prior leg. This establishes a 5-0 structure while the Bearish AB=CD points to a slightly higher resistance target around 17,500. The entire range of resistance is capped by the

88.6% retracement at 18,000. The most important structural consideration completes just above the 17,500 level with an exact time projection around October 20th. The index will drift higher to test this area but it would be a substantial opportunity to sell within this reversal.

Dow Jones Industrial Average (^DJI): Weekly
Ten Years

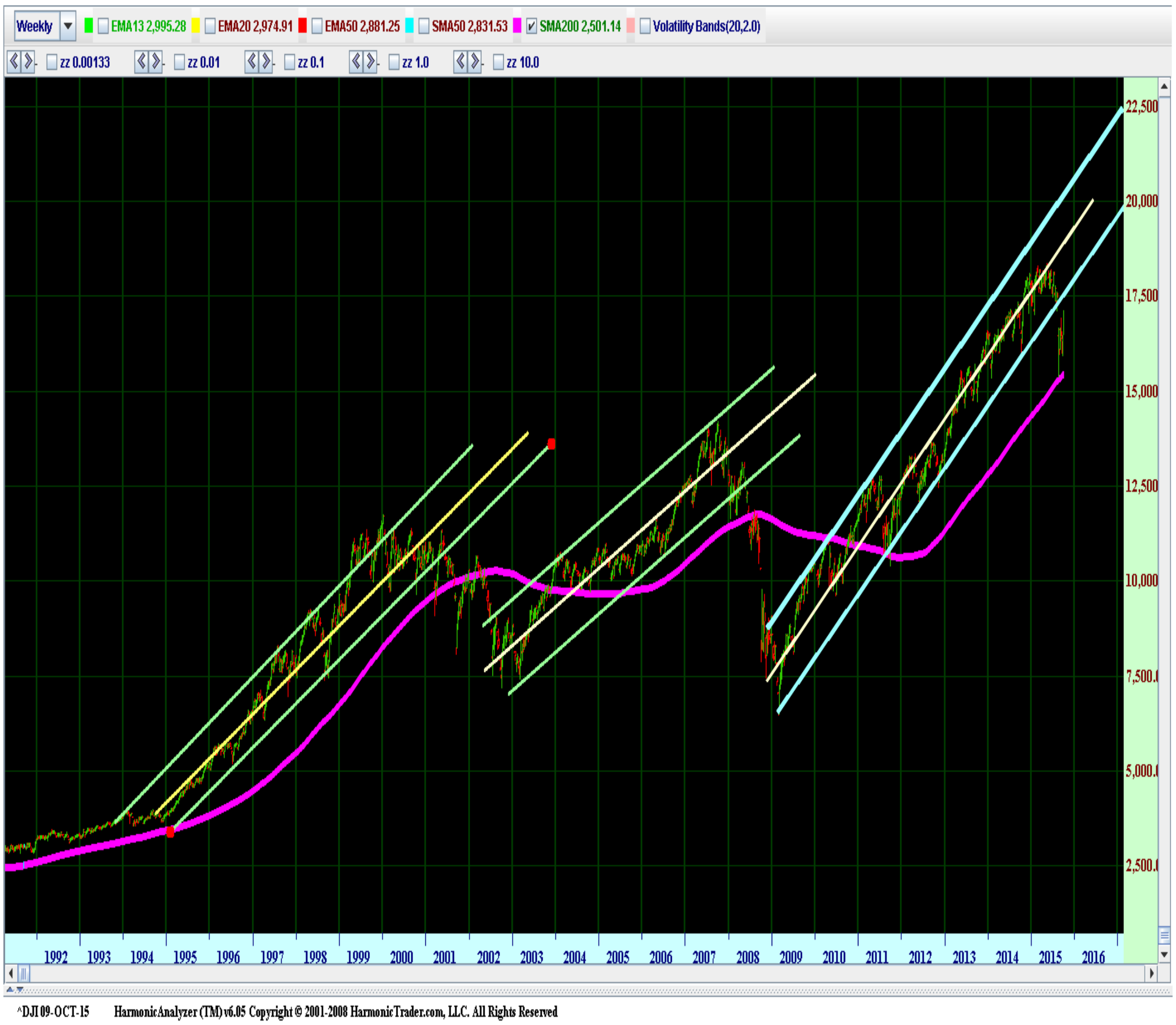
The Dow 30 has been the first major US equity index to crack its seven-year bullish trend channel. The following chart shows the weekly price action going back 10 years. The decline in August violated this channel but was able to bounce off of the 200-day moving average.



^DJI 09-OCT-15 HarmonicAnalyzer (TM) v6.05

Dow Jones Industrial Average (^DJI): Weekly Twenty Five Years

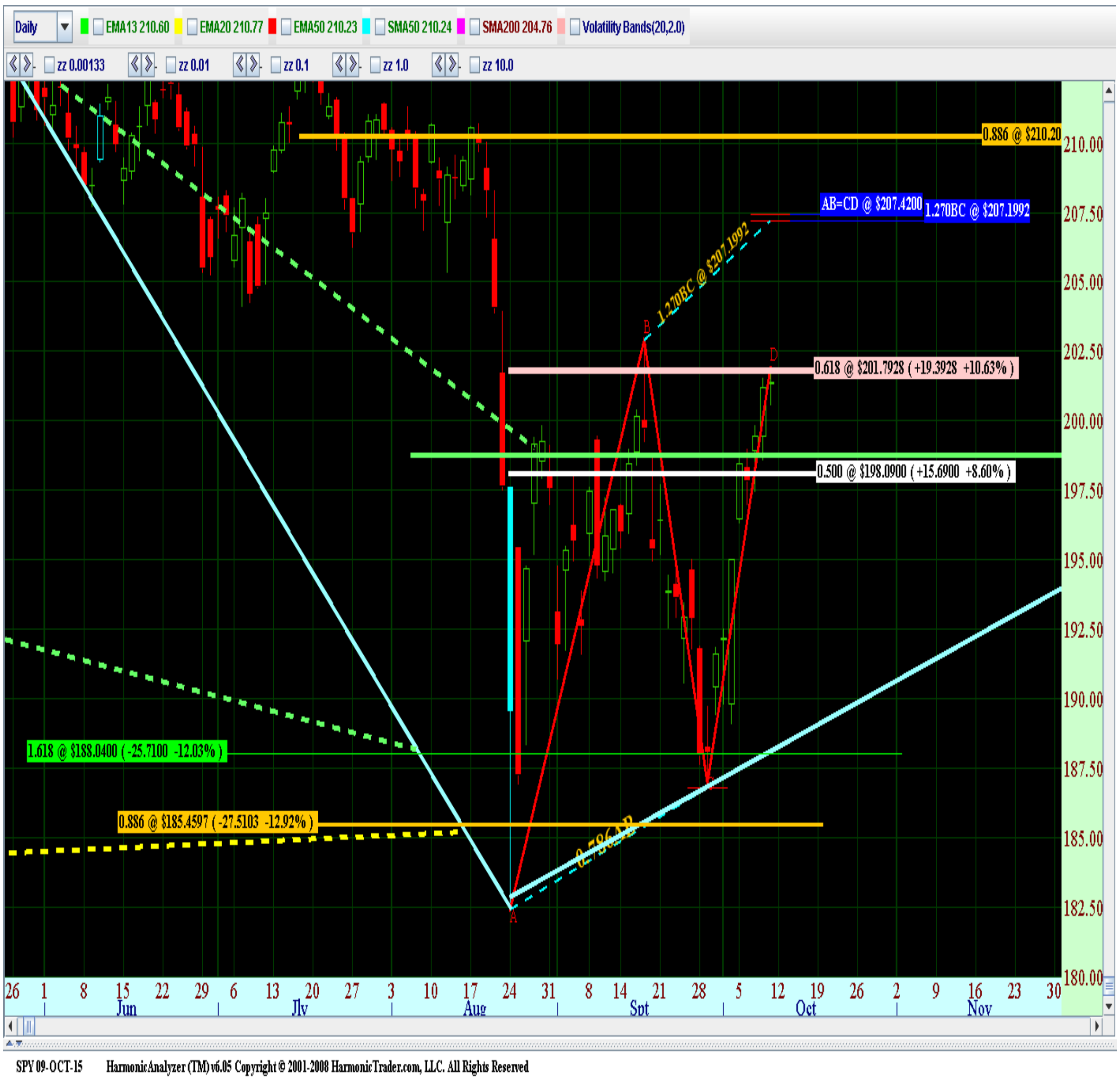
The interesting aspect of such a long-term violation is the fact that we have seen this before. In 2000 and 2008, the index violated its multi-year trend channel and ultimately the 200-day moving average.



These long-term signals are increasingly apparent, especially as the index grinds sideways during this consolidation phase. This market does have some room to go to the upside but not much, and it is pressed against this confirmed technical signal of a violated trend channel. After the 200-day moving average is confirmed, every person on Wall Street will begin to cite this factor as the primary reason to be bearish. For me, the trendline is enough and the other Harmonic Trading measurements confirm the current reality.

Standard and Poor's 500 ETF (SPY): Daily
Bearish AB=CD Pattern

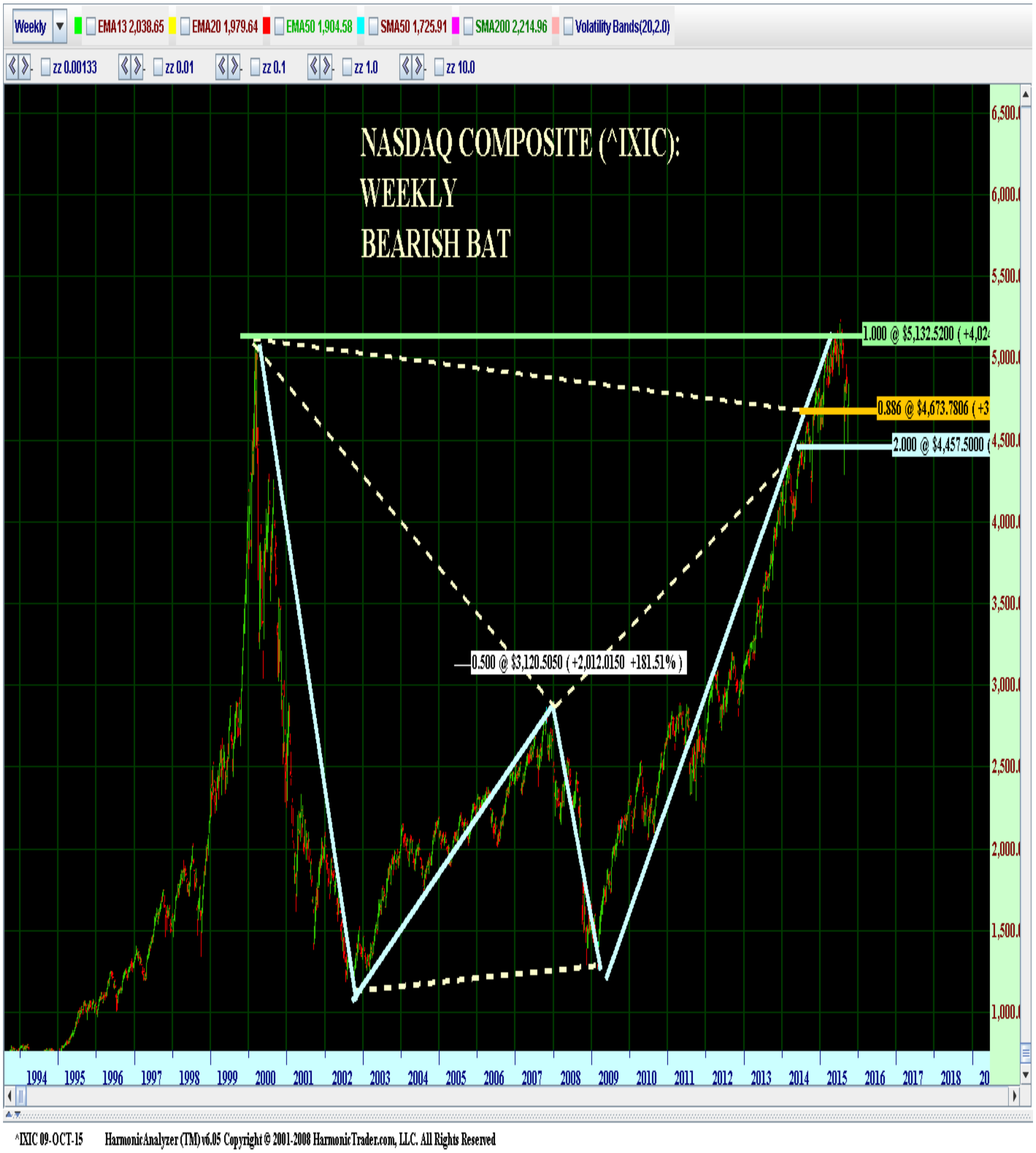
Similar to the Industrials, the S&P 500 has stabilized at the completion of the bullish shark. After the August low, the index has formed distinct structures that are close to marking an important make or break resistance.



The S&P 500 ETF is poised to complete a Bearish AB=CD at 207.50. Combined with an important 88.6% retracement, the price action is heading towards an important resistance level, especially after the significance of the 1.618 decade extension that marked the recent all-time high at 213.40.

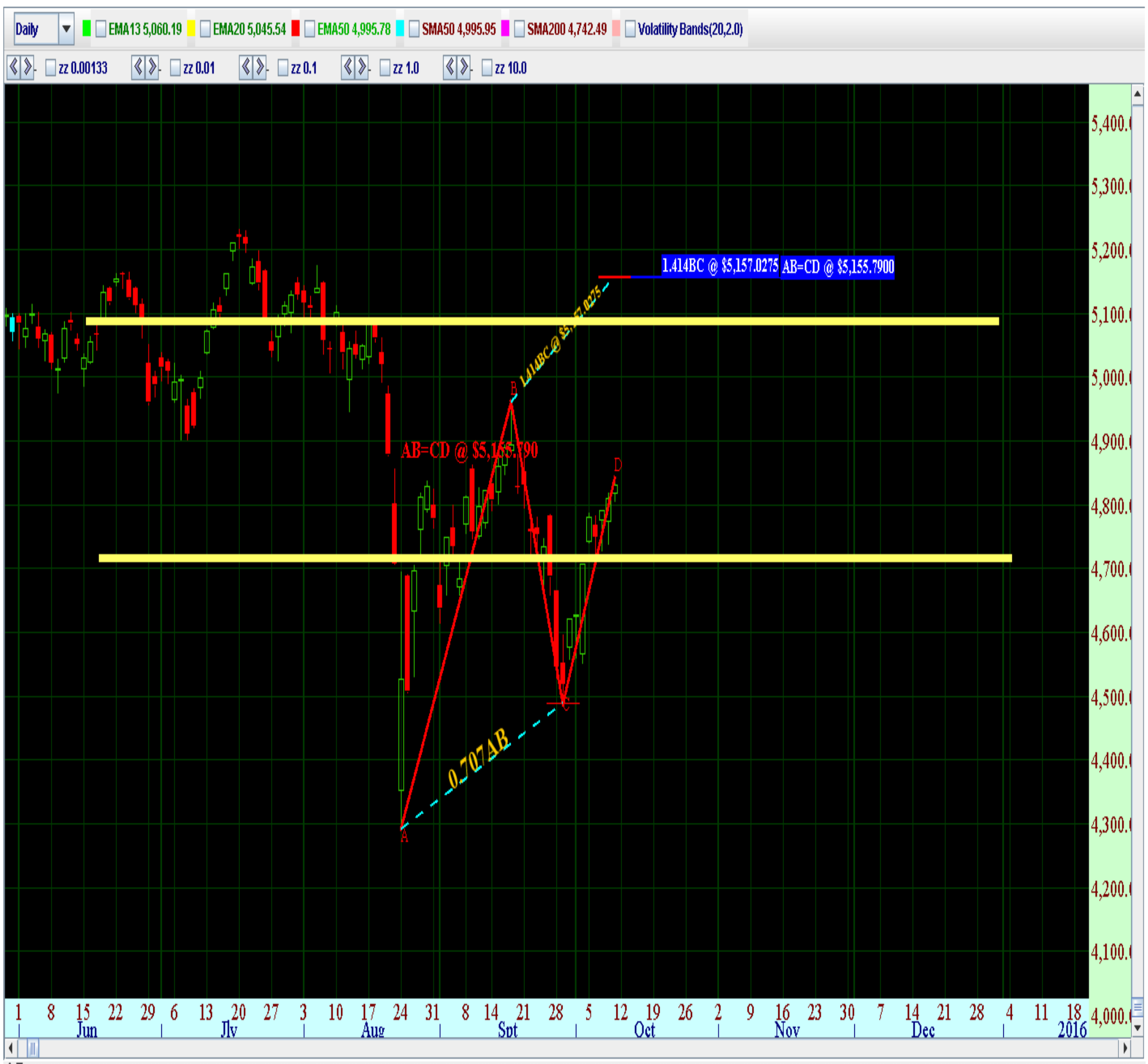
NASDAQ Composite Index (^IXIC): Weekly
Bearish Bat

The NASDAQ possesses the largest structure of all the indices with the Bearish Bat that is retesting the peak at the 5000 level.



NASDAQ Composite Index (^IXIC): Daily
Bearish AB=CD in Bearish Bat Potential Reversal Zone (PRZ)

This daily pattern represents the short-term trigger for an accelerated decline. Although I am watching this entire resistance closely, the weekly pattern has completed and the long-term price action is deteriorating at an ideal structural completion point. As I mentioned previously, this index required nearly a year before beginning its bear market retracement in 2000. Now, the daily chart is showing a Bearish AB=CD pattern in the potential reversal zone of the 15-year structure.



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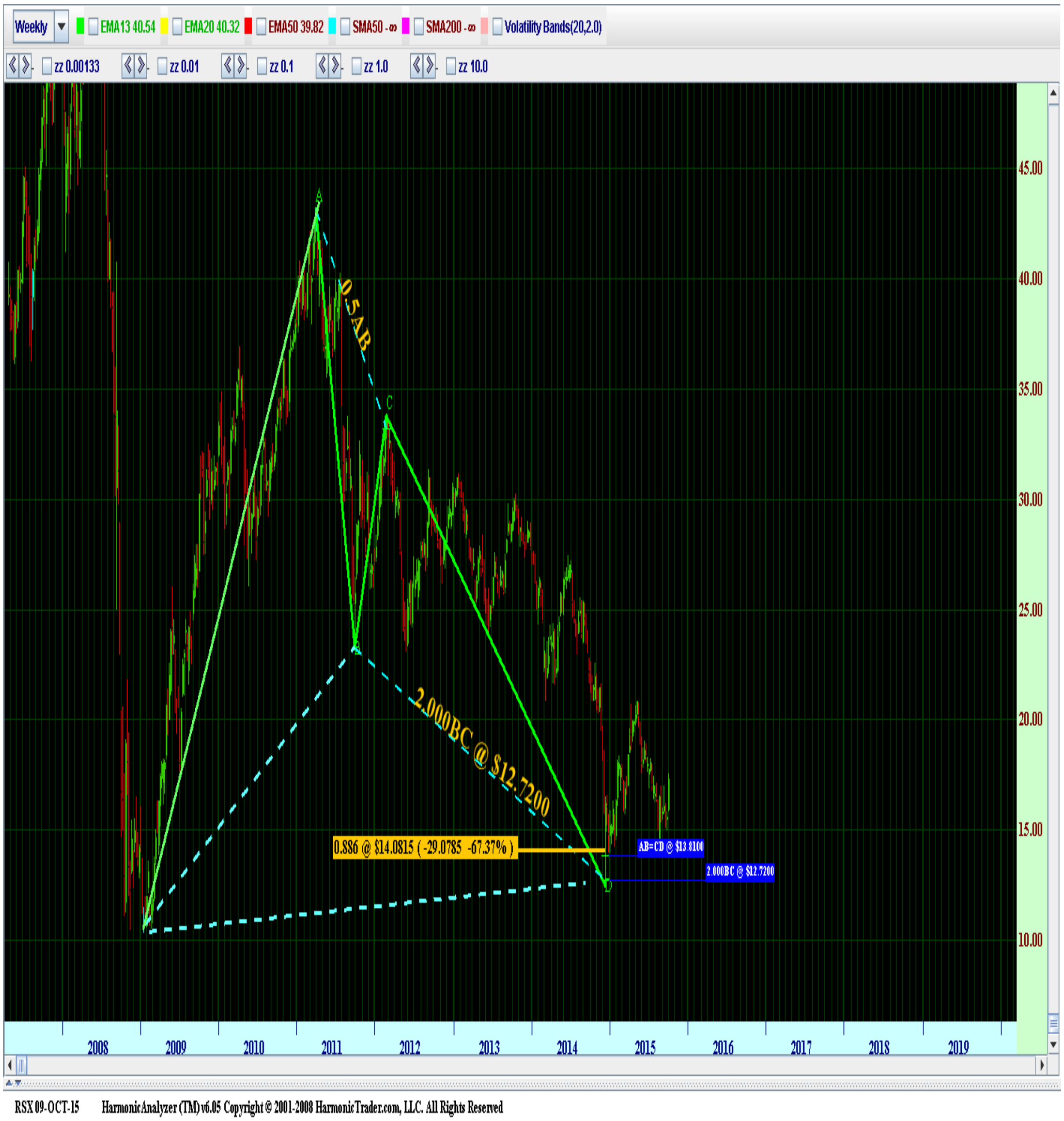
NASDAQ Composite Index (^IXIC): Weekly 2000

Although it does seem that this overall bear scenario will take time, we do have historic precedent that resembles the current situation. At the top of the NASDAQ Composite in 2000, the initial reaction after testing 5000 for the first time required nearly 6 months of consolidation before the larger bear market was confirmed. During this time, the NASDAQ Composite traded solidly above the 4000 level for quite some time before losing 75% two years later. I do not think that the overall bearish possibility of this current harmonic resistance is as severe due to the fact the 2000 peak was parabolic in nature. The past three years have been "aggressive" but not parabolic – at least not to the degree the NASDAQ was 15 years ago.

Much like the situation in 2000, I do believe that the larger reversal will require more time and likely consolidate in a +/-5% range until early next year. There is a clear possibility that the markets could even close the year nominally positive and begin to head lower in earnest in January.

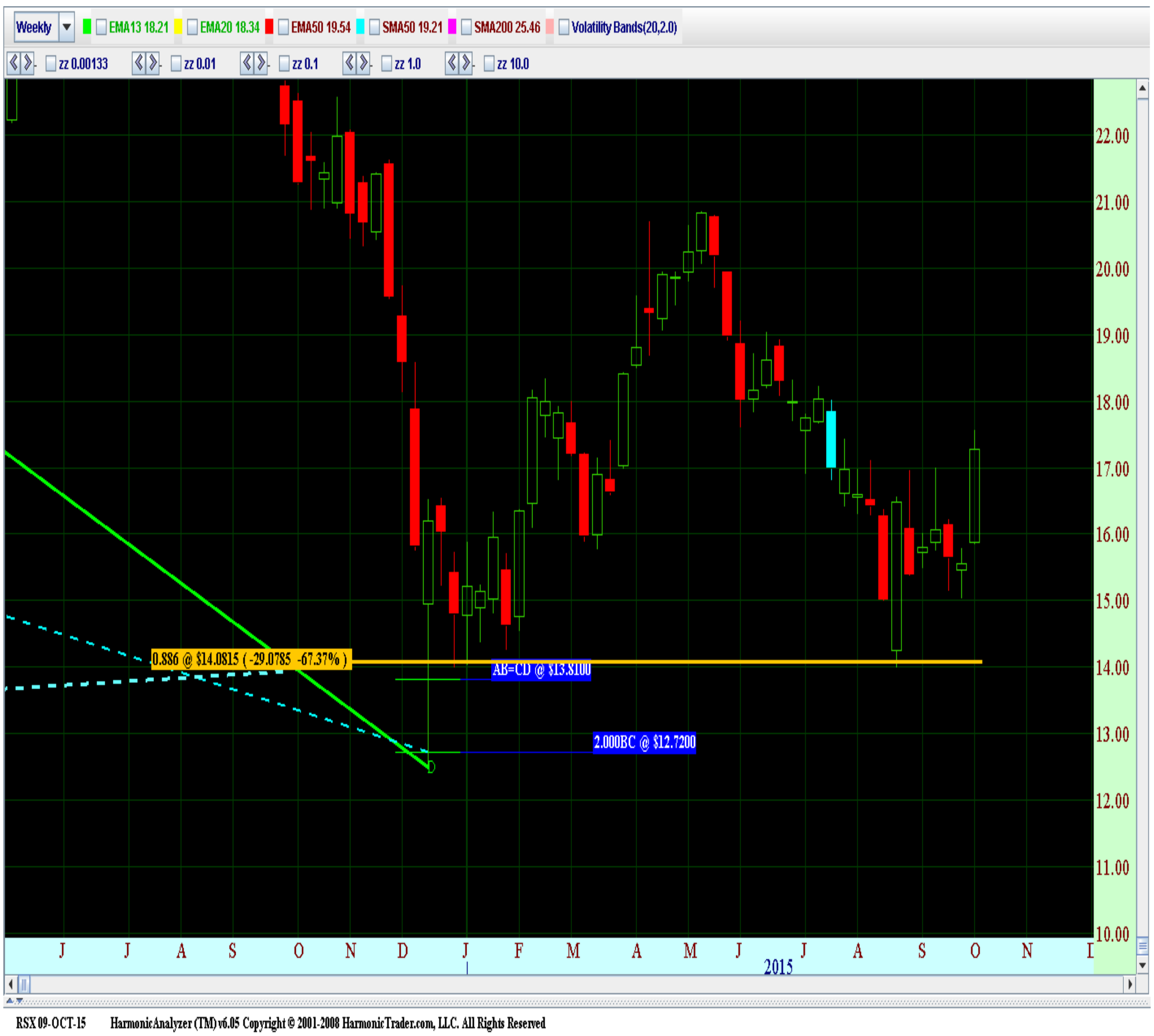
iShares Russia ETF (RSX): Weekly
Bullish Bat

Despite its catastrophic decline, I cannot ignore the recent completion of a Bullish Bat pattern on the weekly chart. The Russian market actually completed its long-term bottom a year ago just under the $14 level, as it reversed on the week it tested the entire harmonic support zone. Most notably, the 88.6% retracement of the 2008 low defined the critical target for the five-year bear market.



iShares Russia ETF (RSX): Weekly
Bullish Bat Potential Reversal Zone (PRZ)

This is a remarkable structure considering the length of time it required to complete and the distinct symmetry that it possesses. Despite all of the negativity, the price action should be closely monitored over the next several weeks. Although such a pattern definitely represents a trading opportunity, I am more concerned with how this structural situation resolves itself going into the beginning of next year.



Despite the rampant bearish signals in many other markets, I find it quite remarkable that the RSX possesses such a defined bullish structure. The longer term ramifications will unfold relatively soon. Clearly, a violation of this pattern would represent another sign that this market will need years not months to recover. At a minimum, the Bullish Bat provides a measurable situation that can be defined precisely. Perhaps this market represents the possibility of an eventual recovery? It is too soon for such a conclusion. Either way, the market still needs more time to rectify the damage done. But, I would keep an eye on this ETF.

October Conclusion

I believe that the fate of the QE bull market of the past six years will unravel over the next few months. It is important to remember that this is a process and it will take time. Depending upon the current consolidation and resolution of weakening long-term action, a bearish scenario is actually the only structural consideration for the next few months, as the various harmonic resistance levels continue to be quite clear. For the United States equity markets, any corrective price action over the next several weeks will challenge critical all-time resistance levels. As I mentioned in a report a few months ago, the first half of the year was the least volatile in a century with back-to-back 0% returns in the first and second quarter. Countered by an extremely active second half, this "calm before the storm" backdrop that preceded the current peak now looks quite ominous.

The market is in the midst of an important technical zone – probably the most important of the past seven years. Undeniably, the continued breakdown in the European markets might be the penultimate signal for the United States. Regardless, these conditions dictate that immediate allocations focus more on the trouble ahead in 2016 than nominal returns for this year. The market is committed to recovering what it can from the August demise in this "last gasp" quarter. The longer-term consequences of this QE adjustment phase will clearly accelerate on a breakdown of the recent lows. For now, the current relief rally is running into these critical aforementioned structural signals and it is all poised to be resolved before year's end.

Please feel free to contact me at HarmonicTrader@HarmonicTrader.com, as I welcome your comments, questions and suggestions. If you are a trial member or wish to receive future reports, please sign up here:

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Best Regards,

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By Scott M. Carney

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