

>: Profit from the Crash: A Trader's Blueprint

Wednesday, July 16, 2008 / Teeka Tiwari

Editor's Note: Our weekly telephone call to answer your questions has been postponed. Our apologies, but we experienced technical difficulties with the recording this week and the volume is quite low.) [Listen now](#) to hear Teeka answer more reader questions, including ...

- After banks, which sectors might be poised for a collapse?
- Is now a low-risk time to buy oversold stocks?
- Which auto makers will be best positioned to profit as gasoline cars are phased out?

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Note: The following piece was originally published one year ago under the title "Profit from the Upcoming Crash." I am running this article again today, as a critical reminder of how to handle what is going on right now in the markets.

For the past few months, I have been Mr. Cautious both in my weekly Tycoon Report commentaries and with my trading service, Point and Profit. I have been using the recent market strength to cash in multiple profits for my PNP members, and I've actually made no brand new buy recommendations in weeks!

My thesis has been that the market is trading at a dangerously overbought level, and statistically speaking, this has been a poor time to buy stocks.

I use the New York Stock Exchange Bullish Percent (NYSE BP) as one of my tools to gauge risk in the market. The NYSE BP was pioneered by AW Cohen in the 1950's, and is basically an indicator of overall risk in the entire stock market.

A bullish percent chart is simply a measurement of those stocks in a particular sector, index, or market that is trading on a point and figure buy signal versus a point and figure sell signal. This measurement is expressed in a percentage form. You can create Bullish Percent charts for any sector, such as banks, brokers, restaurants, etc.

The New York Stock Exchange Bullish Percent is a measurement of all stocks on the NYSE that are on a P&F buy signal vs. a P&F sell signal. For example, if the NYSE BP were at 74%, it would mean that 74% of all stocks on the New York Stock Exchange were on a Point and Figure buy signal, and 26% were showing sell signals.

Unlike other chart methods, P&F is very black and white. A stock is either on a buy signal or on a sell signal. (FYI, just because a P&F chart is on a buy signal or sell signal does not automatically equate to it being an actionable buy or actionable sell. This is a very important distinction.)

AW Cohen drew some very important conclusions through his careful observations of the NYSE BP. He discovered that readings from above 70% and subsequent reversals below 70% generally coincided with market tops, and indicated a statistically higher risk time to own stocks.

This event has actually just occurred. The NYSE BP has just reversed from 74% down to 68%.

Now, does this mean that the market will go into free fall? Maybe, but not necessarily so. What it does mean is that supply (sellers) now has the upper hand in the market. It means that rallies will in all likelihood be sold into, not bought.

What I do at times like this is reevaluate my entire portfolio. I want to be brutally honest with myself and ascertain which of my holdings I am prepared to stick with through the upcoming soft period, and which of my holdings are straight out speculative plays.

I then purge my portfolio of all purely speculative plays, i.e. stocks that I am playing for an event, or a breakout, etc. Those stocks that are part of my overall long-term portfolio, i.e. those stocks that I feel are experiencing a multi-year above average earnings run, I will generally leave alone and weather the short-term pain of watching them get hit. My reasoning is that the overall long-term gains will generally eclipse any short-term pain I may experience with the position.

My next step is to identify a list of shorting candidates. Typically what I look for are those sectors that are underperforming the broad market. That is, sectors that are exhibiting lower performance than the S&P 500. Once I have my sector list established, I will then look at ALL of the stocks in the sector and attempt to determine which of those stocks in the sector are the weakest.

Once I have that list narrowed down, I will then look for the stock to rally to its 20-day moving average, and at that point, I will place my short position. Do I do it that way every single time? No, sometimes I can just take a look at the chart of a stock and see a fall coming, and I will short it even though it may be in a strong sector. But that would be an exception and not the rule.

When the market bottoms, I do the same thing but in reverse. I will attempt to find those sectors that are outperforming the S&P 500. Now

remember that 'out performance' is a relative term. If the S&P is down 22%, and the Oil sector is down 15%, the Oil sector is still outperforming the S&P handily. I will want to rank all of the sectors' performance relative to the S&P 500. I will then focus on finding the strongest stocks in the strongest sectors.

I will then take partial positions in those stocks when I see them trade at the low end of their trading range. I use both P&F charts and bar charts with Bollinger bands and MACD's to make that determination.

From there the cycle simply repeats itself. We go from oversold back to overbought, and that, my friends, is the simple truth of the stock market.

I would urge you to print this article and refer to it often, and you too will begin to observe for your self the almost comical cyclicity of the stock market.



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