

## THE SEXTANT REPORT

9<sup>th</sup> October 2008

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This research material has been prepared by Daniel Goulding through independent research facilities and contains an independent view to ABN AMRO Morgans Limited.

Rig Ship for Silent!

We are in close proximity to a bottom in terms of time.

My technical work is a synthesis of four factors: price action (the waves), internals, sentiment and time.

### THE WAVES



*Elliot Wave Theory is a form of technical analysis named after Ralph Nelson Elliott. He concluded that market prices unfold in repetitive cycles that give rise to specific patterns. Essentially, the market is alternating between five and three waves at different degrees of the trend. Bull moves unfold in 5 waves, 1-2-3-4-5. Corrections unfold as 3 waves, A-B-C.*

4282 remains the minimum target for the benchmark Aussie equity index, the S&P/ASX 200 (XJO) as per my report *Rig Portfolio for Dive*, published 12 August. In that report I provided unequivocal evidence that the bottom was not in for Aussie equities.

Perusing the charts, the evidence suggests a bottom will take place between 4000 and 4200.

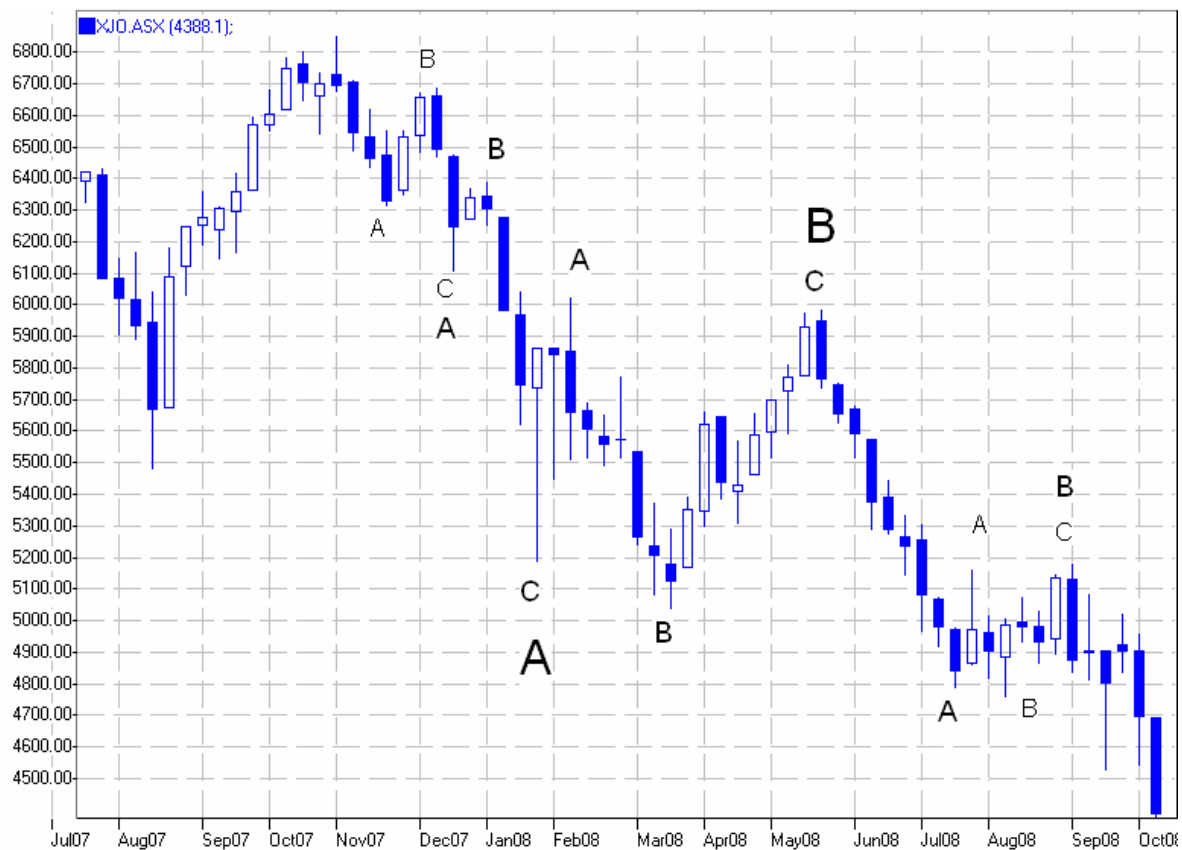
October 10, 11, 14 and 27 are of significant interest as a bottom. For more information, see section *Time*.

My preferred count of the bear market for Aussie equities is depicted below. In the optimistic outcome, we are in close proximity to a bottom in both price and time.

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### Weekly Chart of the XJO

Source: Iress



*My preferred count. I have the bear market of 2007-08 unfolding as a double zigzag. We are in c of C. An intermediate bottom will be in place once C completes.*

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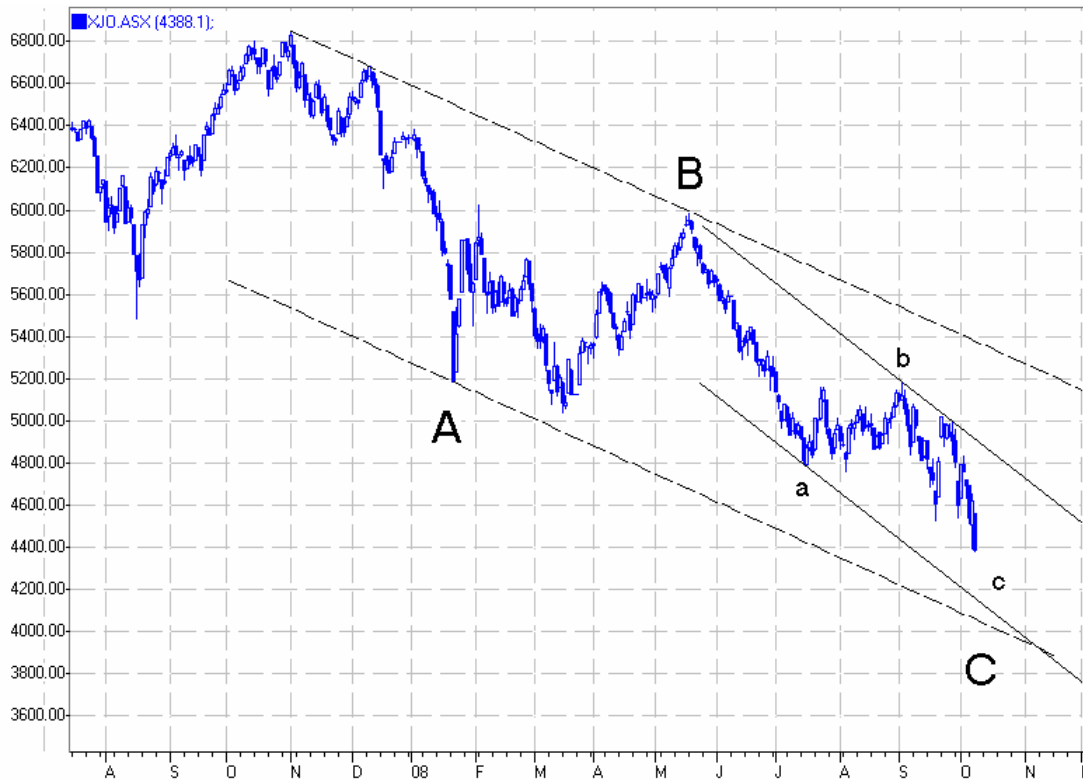
When analysing a zigzag correction, a bottom can often be ascertained with recourse to channel lines. The daily chart below highlights the two channels of interest. Ideally the correction should complete in the vicinity of the lower channel lines, which intersect late October near 4000.

Another pointer to 4000 or thereabouts is the likely magnitude of c. Typically c is the same magnitude as a, otherwise it is usually related by a Fibonacci number such as 0.618 or 1.618. If a of C = c of C, the specific target is 4067.

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### Daily Chart of the XJO

Source: Iress



*The current downturn should tag at least one, if not both, of the lower channel lines to complete a bottom.*

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Once the upcoming bottom is in place, a nice rally should take place. In the most pessimistic outcome, I would be targeting at least 10 per cent before turning bearish again. In the most optimistic outcome, a new bull market would ensue. The most likely outcome is perhaps somewhere in the middle. With luck, we can squeeze 30% or thereabouts before sounding the alarm again.

## INTERNALS



*The internals of the market are akin to the vital signs for a human being. While a person can appear healthy on the outside, a calm exterior may belie an unhealthy interior. Deteriorating vitals tend to provide an early warning that something is amiss. The same can be said for the market. Market internals can reveal hidden strength or weakness long before it becomes apparent in the headline index.*

The McClellan Oscillator (MO) is my favourite short-term gauge of breadth. It is derived from the number of advancing and declining issues in a given market.

The NYSE and NASDAQ MOs hit new lows, thereby nullifying the bullish divergence. However both MOs are oversold, suggesting a strong bounce is possible, perhaps probable. Not shown.

The McClellan Summation Index is my favourite medium-term gauge of breadth indicator. The Summation Index is a derivative of the McClellan oscillator.

While the NYSE and NASDAQ SIs continue to trend lower, a slight bullish divergence remains in place, suggesting that once the upcoming bottom is in place, a strong rally will ensue. Not shown.

The number of new 52 week lows remains disturbingly high. Significant selling pressure continues unabated suggesting new lows dead ahead.

## SENTIMENT



*The market rarely accommodates the majority. As a result, the herd is always leaning the wrong way at important tops and bottoms. Put-call ratios, newsletter surveys and the VIX are useful gauges of investor sentiment.*

Despite the significant decline in recent days, the various put-call ratios from the US have not spiked to levels indicative of excessive fear, and in turn a major bottom. This suggests new lows in the days ahead. Not shown.

While the VIX is at a level conducive to a major bottom, it remains locked in a strong uptrend, boding ill for equities. Not shown.

## TIME



“Time is more important than price; when time is up price will reverse.”  
-- W.D. Gann, legendary trader.

I am looking for a bottom on October 10/11, 14, or 27 given significant market anniversaries, cycles or crash theorems pointing to these dates.

October 27 has two pointers, Carolan’s research surrounding autumn panic declines and Gann’s death zone.

Christopher Carolan won the prestigious Charles H. Dow Award in 1998 for excellence and creativity in technical analysis with respect to his work, *Autumn Panics: A Calendar Phenomenon*. He researched a number of stock market panics in 19<sup>th</sup> and 20<sup>th</sup> centuries and made the startling find that each panic terminated on one of four specific lunar dates: 6-27, 6-28, 7-27 or 7-28. For those uninitiated with the lunar calendar, the first digit represents n<sup>th</sup> new moon after the Spring Equinox, the second digit represents the day. With September out of the way, the applicable dates are October 26 and 27. Given that October 26 is a Sunday, Monday October 27 comes into play as a possible bottom.

Perhaps the greatest trader of all time, W D Gann identified the period of 45 to 49 days or 49 to 55 days as significant in terminating blow off moves and panic declines. Both ranges are derived from the 7 week cycle which Gann referred to as the death zone for equities.

The former range is also based on 45 being 1/8 of 360 degrees (365 days), and 1/2 of 90 degrees, which is an important angle in Gann’s work. Most blow off moves or panic declines last 90 to 99 days with a higher low or lower high occurring on the 45<sup>th</sup> day respectively. From that point, they accelerate into their terminus.

The latter range is also based on the square of 7, an important number in Gann’s work. The square of 7 is 49 (also 7 weeks) giving rise to the death zone of 49 to 55 days. Both the 1929 and 987 stock market crashes occurred between 49 and 55 days after the top.

55 days from the top of the counter trend rally on September 2 targets October 27. It is also 52 weeks forward in time from the top on November 1, thus a complete cycle (with respect to US equities, the NASDAQ topped this date as well). Given two specific pointers to a possible bottom on October 27, we should be on guard for a possible crash into this date. Could we witness a crash? Looking at crash cycle theory, it is possible.

According to the research of Steve Puetz, 8 of the greatest crashes in history had an usual signature. The top prior to the crash occurred within a period of 6 trading days before to 3 trading days after a full moon that occurred within 6 weeks of a solar eclipse. Another qualification is that the first full moon following the solar eclipse is required to be a lunar eclipse. This year we had a solar eclipse on August 1 and partial lunar eclipse on August 16. The second full moon occurred

on September 15. A lower high took place on September 8, 5 trading days before the full moon on September 15. As a result, I believe the crash signature is present in our market. Whether it wreaks havoc on the market or not is another question.

October 10/11 have a number of US market anniversaries pointing to these dates. The S&P 500 topped October 11 last year. The bear bottom for US equities in 2002 occurred October 10. The 1990 bottom for US equities occurred 11 October. Given equity markets worldwide tend to have a little synchronicity, it is possible we trace out a bottom in this time-frame. It could be the final bottom or perhaps only the penultimate bottom.

Last but not least we have the full moon on October 14. Full moons tend to mark lows in the market place. Keep in mind however that this is not a rule as moons can often invert, particularly in panic declines.

Given the analysis above, I believe we are set for a bottom either in the next few days or October 27. There is no way of knowing beforehand which range/date will prevail.

In summary, I believe the XJO is close to a bottom in both price and time.

Till next week ciao.

Bearishly yours,

Daniel

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