Bottom-fishing, anyone?

After the waterfall, is now the time to buy? **Ng Ee Hwa** offers an analysis on whether or not now is a good time to bottom-fish.

It has been more than five months since the sharp downtrend in the regional market started. During this period, our widely followed local index – the Straits Times Index (STI) – has corrected by more than 30 per cent from the all-time high of 3,909 achieved on October 10, 2007. To make matters worse for the small investors, many of the popular stocks have fared much worse than the benchmark index. Cosco Corp, the star performer of 2007 has already corrected by a hefty 60 per cent. Many other S-shares (Singapore Exchange-listed China stocks) have similarly suffered such a brutal fate in this bear market. With this severe correction, investors may be tempted to look at buying some stocks considering how low their prices are, compared to their highs achieved just a few months ago – an approach commonly known as bottom-fishing. But with so many uncertainties and rumors circling in the market, is this really the time to start buying? This article will discuss how technical analysis can help in determining whether the awaited turn-around is going to occur any time soon.

From the charts, we can immediately see that the major indices are testing the January 2008 low. This is a key psychological level that should provide support to the market. However, if the January 2008 support level does fall, this augurs badly for the market sentiment and may bring another heavy wave of selling. On a more optimistic note, assuming this psychological support level does hold, we may be looking at a range trading market. This is where the market has a chance to build a base (where the bulls and the bears cancel

Chart A

Chart B

each other) or what we commonly call a bottoming action. After such a great fall from grace, it will be very unnatural for the market to make a "V" shaped recovery. Even if it does, it is often unsustainable and only good for the short-term. Let us start by studying the chart of Dow Jones Industrial Average (DJIA).

Chart A shows that the DJIA has broken below the psychological support level of 12,000. We are seeing three possible support levels below it. First, there is a trendline support (red), which was tested no less than two times. This is closely followed by a second trendline support (blue). This blue trendline is the long-term trend support for DJIA. Should DJIA break these two trendlines support, it will likely lead to more heavy selling. Next, Fibonacci 38.2 per cent support stands guard near 11,500 points. And last, a major horizontal support at 11,300 should be the worst case scenario for now. After identifying all the strong support levels, investors are urged not to buy with blind faith with regard to technical analysis. Rather, these are anticipations or what we refer to as market opinion. When an opinion is conjured, it is important for it to be confirmed by market actions. These confirming actions include formation of a candlestick reversal pattern, divergence from an indicator or a bounce off the support As for the resistance levels, the first resistance is seen at 12,180 thereabouts. From Chart A, we can also observe how the index flirted with the 50-day moving average line in the past. Should we test and retrace below the 50-day moving average line, it means that the bears are still in control. On the other hand, if we break above this moving average line, it will be useful to start tracking the 20-day moving average for the anticipated upward price movement. Money flow index is also showing a small positive divergence, this could be an early sign of

Let us now look at chart B, which shows the chart for STI. February 2008 ended on a negative note causing investors to duck for cover as the market came crashing down and broke through the 3,000 psychological support emphatically. It can be observed that when the index was trading near the downtrend resistance line, it had failed to break 3,100 level decisively in two previous attempts. Before STI can attempt to trade towards 3,100 level, it has to overcome the gap resistance at 3,000 first. This gap resistance was confirmed on the 12th of March, 2008 when STI opens at the resistance and closed firmly lower. Based on Fibonacci analysis, the major 38.2 per cent Fibonacci support level has been broken. The immediate support now will be taken from the low achieved in January 2008. If this support is compromised, we may see STI testing the 50 per cent Fibonacci support at 2,570 thereabouts. Money flow index indicator is suggesting there is more room to fall before a decent rebound can take place. **SI**

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