May 17, 2010

Topic: Long-Awaited Correction?

Last August, we started to anticipate a market correction. The indexes had moved up impressively from their March 9, 2009 lows and a pause seemed warranted.

In November, we had to change our opinion, as the adage “the trend is your friend” predominated and that trend remained inexorably upwards.

In February, we thought that the bull run was over as the March 9, 2009 up-trend line was punctured by each of the major North American indexes. But, after an 8% pull-back, the upwards march continued. Right up until Monday, May 3rd.

The week of May 3rd saw a pronounced retracement, although there were significant differences in the relative declines of the various indexes. It appears that there was a flight to safety, to the Big Name companies represented in the Dow, which declined the least. The broader index, represented by the S&P500, did better than the more volatile, technology-laden NASDAQ. The S&P/TSX did relatively better still, largely because of its exposure to gold companies, which performed well in the mini-panic.

We have been saying for quite some time that a 10%-15% market correction would be appropriate in order to set the stage for the next up-leg of the current bull market. If this current downturn is it, then it is not quite half over.

Downside projections, the “Target”, using a 15% drop from the recent highs, would be as follows:

	Recent High	Current (May 14)	% Drop from High	15% Down Target	% More to Target
DJIA:	11,258	10,620	5.7%	9,570	9.9%
S&P500:	1,220	1,135	7.0%	1,037	8.6%
NASDAQ:	2,535	2,347	7.4%	2,155	8.2%
S&P/TSX:	12,322	12,015	2.5%	10,472	12.8%

We remain committed to our expectation that the market will suffer a 10%-15% pullback from the recent highs. We recommend moving to defensive positions, and we would be selling on strength.

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