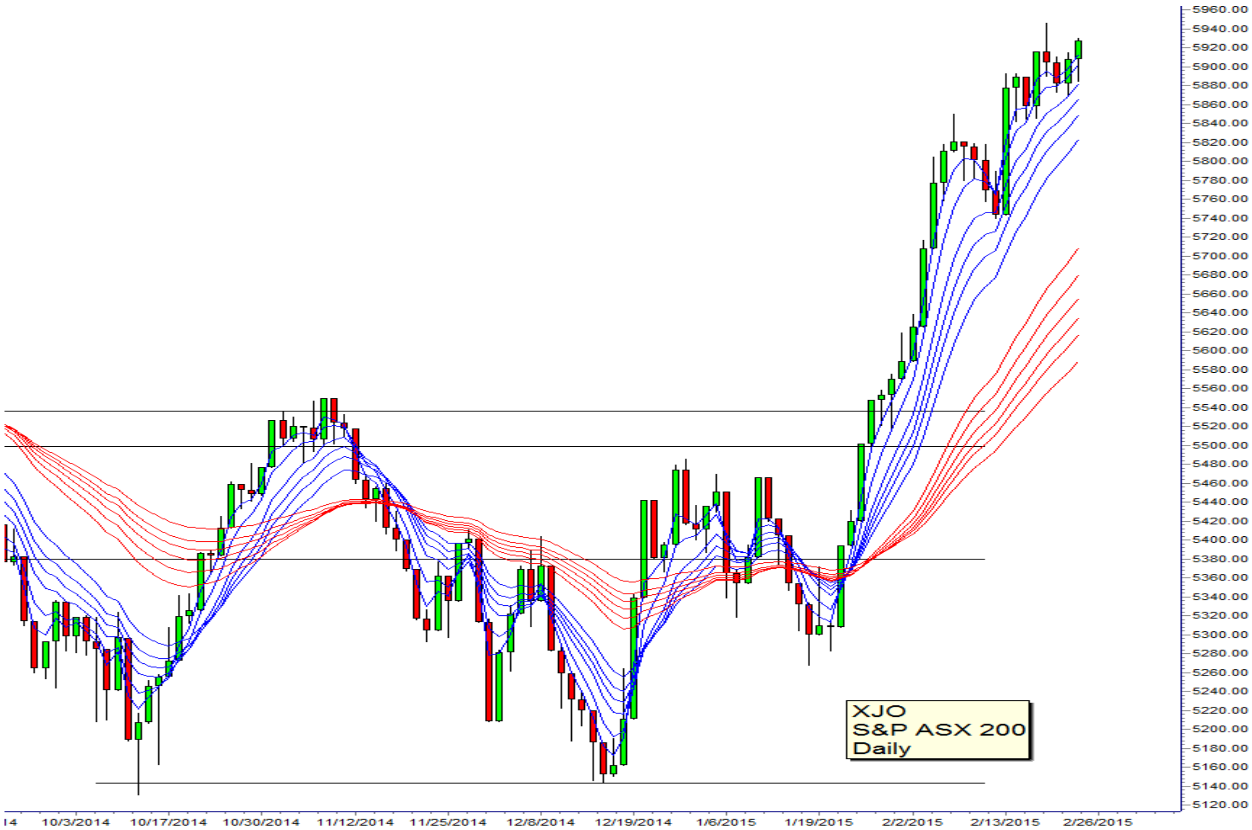
S&P 200, AUSTRALIA

By Daryl Guppy

There is limited trading in the region this week due to the Chinese New Year holiday so we look at Australia. The upward momentum appears almost unstoppable – and that's a major concern. It doesn't stop us from trading it, but it injects a note of caution. Its tight stops as the rocket ride continues. If we are lucky the fast run may end with a wild consolidation pattern that is similar to what has happened with the Shanghai Index.



The upside target for this rocket ride is 5950. This week it was almost achieved. The upside target is calculated from the monthly chart of the XJO. It uses the width of the long term trading band between 4000 and 4990. This trading band dominated the market from July 2009 until July 2013. The breakout above this level suggests that any retreat will use this level as a support point.

The monthly chart sets 6150 as the next upside resistance level.

The overreaction to the rate cut flags a vulnerable economy so we continue to treat this as a trading environment rather than an investment trend. The main concern is that this explosive volatility sets the scene for a continuation of very fast rallies and retracements. Its difficult for traders and impossible for investors. We have to adapt to the new market environment.

The breakout is too far and too fast. Caution is required and this means using stops to protect profits. This still very much has the behavior of a rally. The biggest risk continues to be time in the market. Trends have become inherently unstable and short lived with rapid changes in trend direction. Get caught on the wrong side of this rally when it retreats and traders will be hammered. These are ideal conditions for derivative trading where returns are boosted with leverage.