"The End is Nigh...Hopefully"

Panic mode has returned to the stock market for the first time since last October, convincingly breaking us out of the sideways consolidation pattern in the S&P 500 that we have written about all year. With the action of the last few days, we are now at a 10-month low in the market and have FINALLY experienced the much-discussed 10% intraday correction in the S&P 500, the first since early 2012. This correction has been, admittedly, long-overdue based on historical market patterns, and because we have not seen one in so long, it appears many investors have forgotten that stocks do go down from time to time without it resulting in a major market crash. And despite the worry right now, we still believe it is more than likely that we have already seen the worst of the fall when you consider some of the indicators we follow are already at or near historical extremes and the fact that more than half of the stocks in the United States have already experienced a 20%-loss bear market. Also, the mini-crash yesterday qualified as a 90% downside day on the NYSE, with more than 90% of issues declining on the day and almost 97% of the volume taking place on the downside – about as extreme as those stats ever get. The charts on the following pages also support our view that we are at or near the end of the correction, although volatility will likely continue into the foreseeable future, making it all the more important that you have an investment plan in place and manage individual positions before they go too far against you. And please keep the long-term in perspective if you truly are a long-term investor. These corrections are tough to live through, but when you look back in time through the history of the stock market, these little blips are very insignificant when put into context and generally represent a very good buying opportunity.

“It is not entirely clear what causes deep market corrections, but without them many of the best performing long-term investors would have never achieved their spectacular returns.”

-- Peter Lynch
S&P 500 is VERY Stretched

With the action yesterday, the S&P 500 is now more than 5 standard deviations away from its 50-day moving average, an extremely oversold reading that has not been seen since the 1987 stock market crash. During this bull market, great buying opportunities have come when this indicator has gotten even 2 or 3 standard deviations below the 50-day, so a move of this magnitude might end up being among the best you are ever going to see.

Source: IndexIndicators.com
Number of New Lows is EXTREME

At the height of this bull market, there were about 800 more stocks on the NYSE making new 52-week highs compared to the number making new 52-week lows. That difference has contracted for all of 2015, but with the action recently, it has fallen to levels not seen since the worst of the 2008 market collapse. More than 1500 more companies on the NYSE made new lows yesterday than made new highs, once again illustrating just how oversold the entire market is at the moment.

Source: Stockcharts.com
VIX Spiked HARD

While one of the big stories in 2015 has been the back-and-forth market action, this volatility really had not been captured by the most common way investors measure volatility – the VIX. Generally, readings over 20 indicate increased volatility, but, up until last week, we had spent much of the year far under this important level. Well, that has very quickly changed, with the VIX spiking up to 53 yesterday, a level not seen since near the market bottom back in early 2009. The move was so large that the VIX is now the best performing major futures contract, YTD, according to FINVIZ.com. And in the process of spiking, it also broke up through a downward sloping trendline that had capped the VIX over the past few years. So an increase in downside volatility might be in the cards going forward.

Source: Stockcharts.com
Good Luck Finding Top Performers

During the worst of the collapse yesterday, only about 15% of stocks on the NYSE were above their respective 200-day moving average. Historically, intermediate-term bottoms generally occur when this indicator falls into the 10%-15% range, further strengthening my belief that it is likely we have seen the worst of this sell-off. With 85% of stocks already struggling, there does not seem to be much more room on the downside. The current readings are the lowest since 2011.

Source: IndexIndicators.com
Put/Call Ratio Higher Than in 2008!

The Put/Call Ratio is often used as a contrarian indicator, meaning, when it gets too high, investors are likely overly bearish since they are buying many more puts than calls. Spikes in this indicator tend to coincide with market bottoms, and the readings we have right now are higher than at any point in this bull market and even more bearish than at the height of the 2008 financial collapse. Extreme sentiment, indeed.

Source: Stockcharts.com
So Where Does That Leave Us?

While I do think the near-term bottom is in, if we do see a continuation of the sell-off, there are a couple of support areas for the S&P 500 that should provide a boost to the bulls. The October closing low at 1862 could prove to be important, as could the area around 1815 since that marked not only the October intraday low, but also proved to be significant back in early 2014 and late 2013. On the upside, the former support levels should now act as resistance, meaning 1974-2000 could slow the bounce, as well as the area around 2040. The good news, though, is that the sideways action we saw for much of this year has allowed some very important long-term trendlines to keep moving up, potentially giving us more upside now that we have sold off.

Source: Worden TC2000

Past performance does not guarantee future returns. The S&P 500 is an unmanaged index of the largest 500 stocks by market capitalization in the U.S. markets.
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