

Tischendorf Letter Issue 11: New Theme 'Gold Mining Stocks'

February 7, 2016

Hello members!

Before we look at the new theme that is emerging, I am talking about gold miners, I want to address the current situation in the markets. The key for survival in the past 4-5 weeks has been **'flexibility and the ability to change one's mind'**. I stayed bullish going into 2016 and gave the market the benefit of the doubt. That is, until the technicals told me that the bullish view couldn't be held up anymore. Then, bearish price action and set-ups not working at all forced me to change my mind. Successful trading is not about predicting, being right or being wrong. It is about making educated guesses when odds are in your favor and adapting and changing one's mind when the facts change. When they change, our job as traders is to go with the flow and act decisively.

Avoid seeing what you WANT to see.

The statement above is a great description of what is going on right now. For now, longs are trapped. The great majority of traders have not experienced any severe bear market in their lifetime, let alone the brutal decline of tech stocks in 2000. They are buying falling knives because they perceive current prices to be **'bargains'**. This is buying motivated by opinion not facts. They **'want to see bullish set-ups that are not there'**. They might get away with it once. It might even work several times in a row. But ultimately, this is a flawed 'strategy' and a sure-fire way to the poorhouse. Sticking to the process and a rules based approach to trading is the best way to protect your capital.

The price moves on Friday are typical for extremely weak markets. **LNKD – LinkedIn** and **DATA – Tableau Software** produced huge gaps to the downside after they released earnings. They basically got cut in half and lost almost 50%. Sellers are now in control. The news i.e. the actual numbers they released are completely irrelevant for traders. The only thing that is relevant is **the market's reaction to news**. If a stock is in a downtrend and disappoints, the current market is absolutely unforgiving. Anything can be construed as an excuse to liquidate. That is why last week I stressed the fact that during bear markets or corrections **'strength is used to sell into'**. The recent price action of FB – Facebook, GOOGL – Alphabet and AMZN – Amazon is a prime example for that phenomenon.

Market expectations for Monday:

Stocks like **TSLA – Tesla**, I covered the technical situation extensively, have developed incredible downside momentum. TSLA, along with lots of other stocks, you wouldn't believe it, are now trading at new 52 week lows and closed the week near their respective lows. Take the current market action and the fact that TSLA will announce earnings on Wednesday and you have a situation that could lead to massive selling. Holding a down trending stock into earnings during bearish markets is a death wish. As a general rule, a stock's performance on a Friday is a good reflection of what to expect in the near future as traders have to hold over the weekend. On Mondays the Friday trend often sees follow through. In the current situation that means that if we see more downside on Monday, it could be very painful. In a nutshell, we could see more forced selling and massive liquidation of long positions.

Remember: A simple rule stating you are not allowed to hold positions trading below their respective moving average 50 will make sure you avoid almost all catastrophic declines.

New theme: Gold miners with bullish price action

Notice I didn't say 'new bull market'. For that to happen we need a lot more price evidence. A technical concept I have explained quite a few times in the past, I also expanded on that concept in my interviews, is the slope of the moving average 200. The great majority of gold miners did cross their MA 200. But most of these MA 200 lines are still trending down. This typically is NOT a situation that produces the best run-away moves. The very best moves occur when all the stars are aligned. For that to occur the MA 200 would have to be in an uptrend. With downtrending MA 200 lines we often see a retest until the MA 200 can catch up with price action and slowly start to trend up as well.

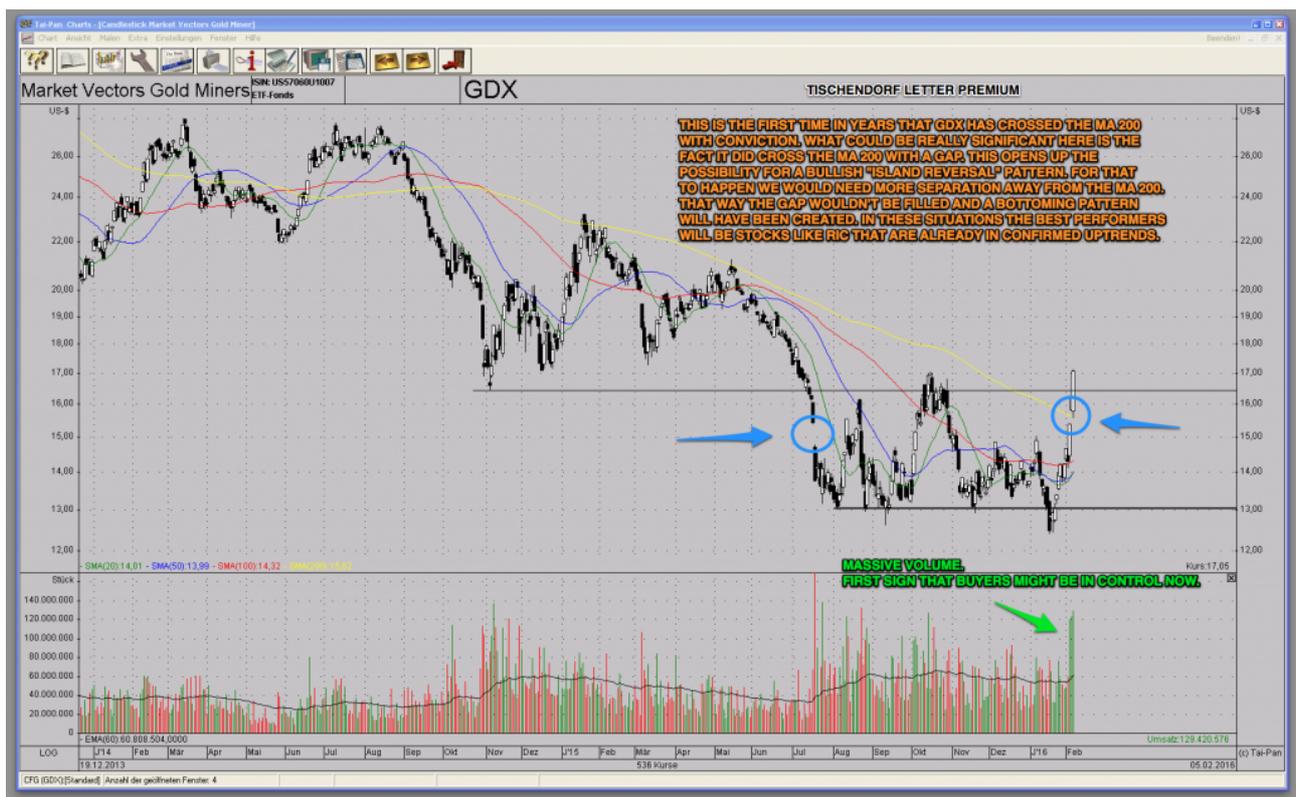
There are special situations though, where a new trend starts and looks a lot like a short squeeze. The initial run is often ignored because traders still have a bear market mind-set. Then they notice the strength within the sector and wait for the first pullback. The problem with that approach is twofold: Sometimes we have a situation where traders wait for a pullback that never comes. Or, the pullback happens much later than expected and leaves traders behind with no exposure to the new trend.

Another important technical concept I want to talk about is the fact that bull markets reward '**moderate chasing**'. It is really simple: Bull markets make it difficult to get in. If you want to get in you often have to be willing to chase a bit. Buying on pullbacks works as well, but when the pullback finally comes, the window of opportunity closes very fast.

This brings us to the **GDX – Gold Miners ETF**. The chart has crossed the MA 200 with conviction and volume is really ramping up. The strength of the current up move is impressive to say the least. Is it a short squeeze or something that is signaling much more strength to come? It is too early to tell, but if we see more weakness in the markets on Monday, more strength with gold miners on Monday seems like a high odds proposition. This would achieve more **'bullish separation'** away from the MA 200. The best protection, as usual, is to go with the technically best set-ups. That is, gold miners that have been trending up for more than a year and that have a **MA 200 that is trending up** or has at least been flattening out for some time. These stocks will encounter less selling pressure when the first pullback comes and they have the potential to really fly as they have less overhead resistance.

Remember: The best traders tend to buy into the strongest stocks. This leads to what is known as **'Strength begets more strength'**.

Click on **GDX – Gold Miners ETF** chart to enlarge:

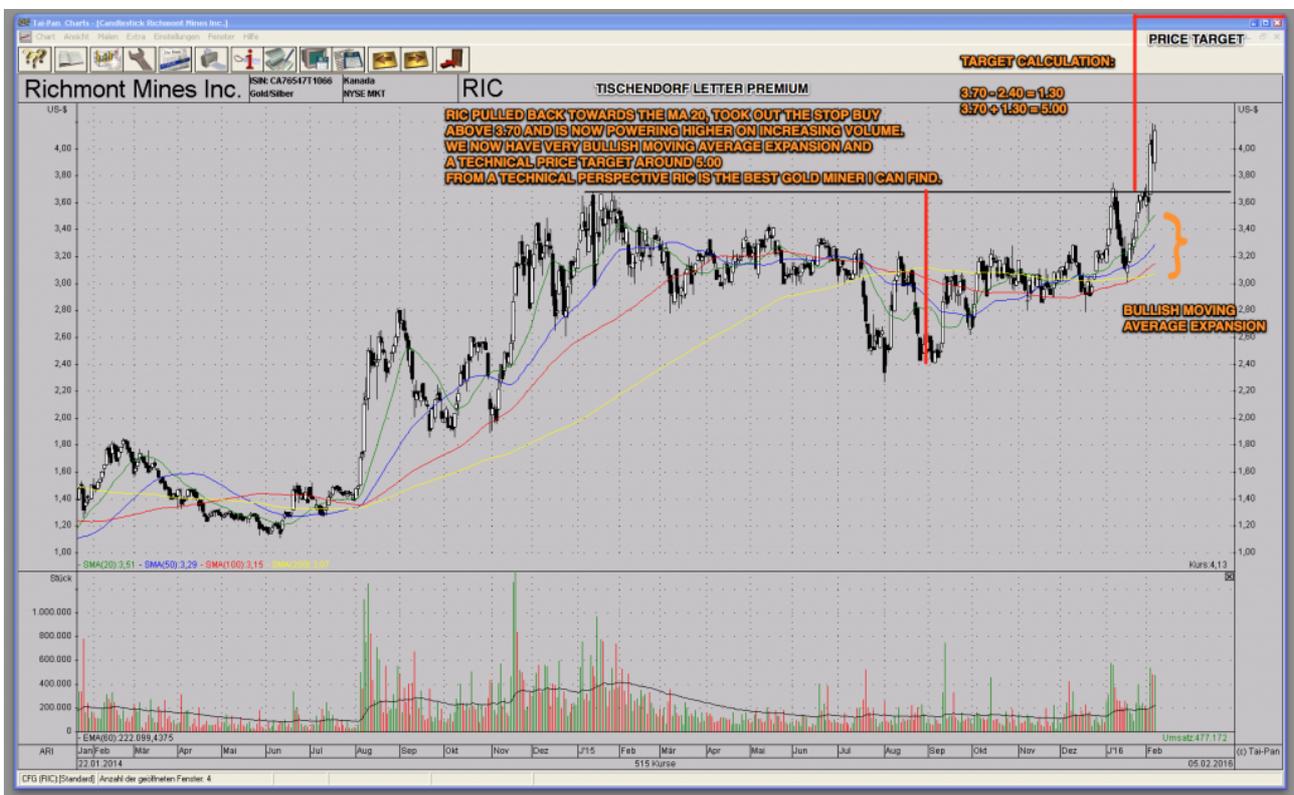


As you can see in the annotations above, we might be witnessing a very bullish pattern in the making. This pattern actually prompted me to devote this issue mostly to gold miners. The pattern at hand might very well turn out to be a bullish **'Island Reversal'**. Island reversals are topping or bottoming formations and signal the beginning of a new trend. Again, it is very early

days, but the technicals tell me to seek exposure. Over time, provided the charts offer more confirmation, I will ramp up exposure.

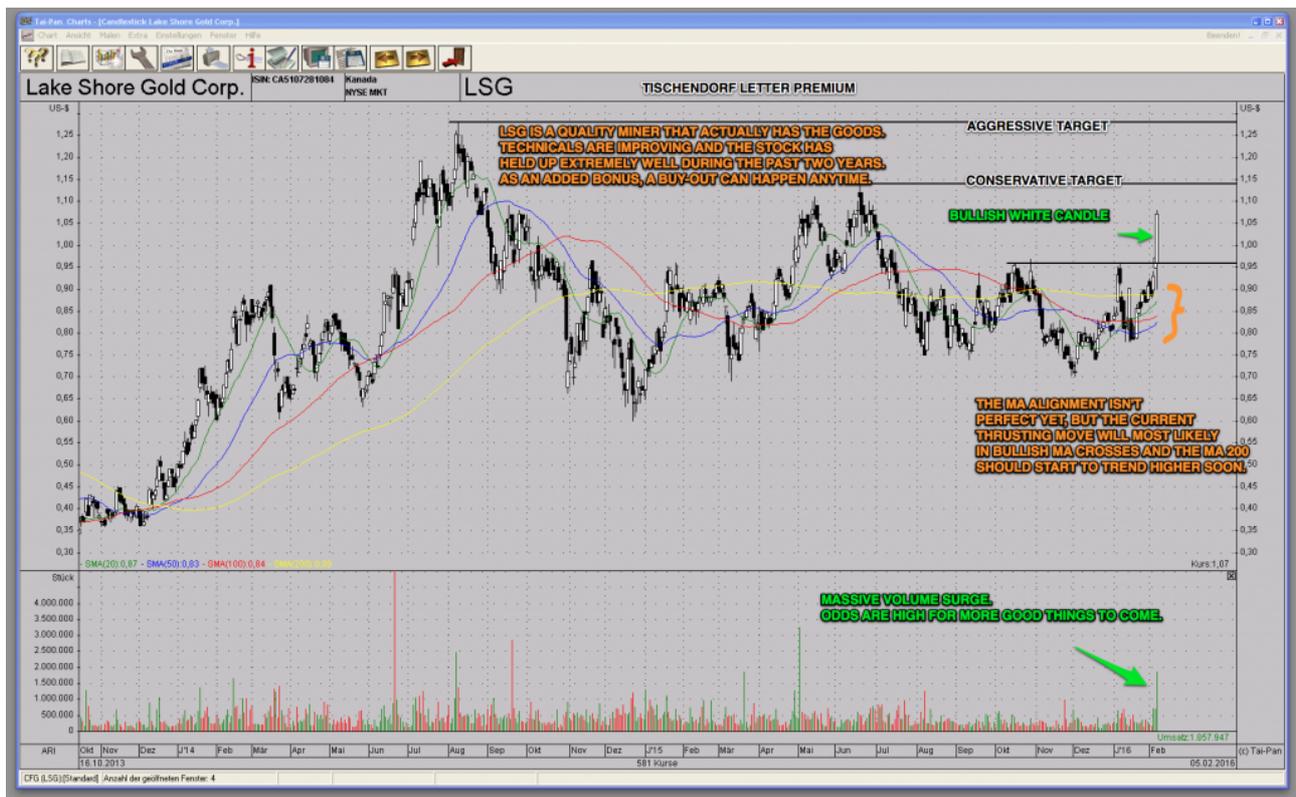
That said, I recently started including gold miners in the watch list at the end of each Letter. Last week I outlined a bullish scenario for **RIC – Richmond Mines** with a stop buy set-up. RIC did exactly what a strong stock is supposed to do. As you all know, when a stock is rewarding me immediately after I buy and thus confirms my original analysis, I do add more. From a purely technical perspective, I consider RIC to be the best gold miner the market has to offer right now. It has consistently shown superior relative strength for more than two years.

Click on **RIC – Richmond Mines** chart to enlarge:



When I have a lot of conviction and the market gives me a green light, I start to get aggressive and look for more exposure with holdings acting well. I then also start to look for other stocks within the same sector. Which brings me to another gold miner I like a lot and started buying into.

Click on **LSG – Lake Shore Gold** chart to enlarge:



Why LSG? Because it is a quality miner. 7 years ago, long-term readers will remember, one of my biggest winners was **WTM.TO – West Timmins Mining** which ended up being bought out by **LSG – Lake Shore Gold**. It is no coincidence rumors of a LSG buy-out are now circulating. Actually, LSG was halted on Friday. The company had to issue a **press release** because it was requested to comment on recent trading activity. This is typical bull market behavior. We have abnormal volume behavior on the upside. This is exactly what you want to see. As traders we do not ask **WHY** a stock is going up. We see that it **IS** going up and we buy. This is exactly what traders did after trading with LSG resumed. They kept buying and the stock closed the day near its high of the day.

The real money in speculation has been in commitments in a stock or commodity showing a profit right from the start. – **Jesse Livermore**

And finally a last quick comment on the **Fiber Optics** sector. Along with Food stocks it was one that held up really well on Friday. **FN – Fabrinet**, which has been on the watch list in the past has the potential to become the leader. **LITE – Lumentum Holdings**, a new issue is holding up extremely well. **NPTN – Neophotonics** also looks like it will set up again. Whenever I see strong stocks like that popping up in my technical scans I take note and add them to my watch list.

Conclusion: The rules of the game never change. When a new bull market starts you want to have as much capital as possible. Protecting financial and mental capital in bear markets is how you accomplish that. It is during the tough times that future winners show their hand. That's why we scan for strength and maintain a watch list with the best stocks the market has to offer.

Watch list:

Watch List Link – Tischendorf Letter Issue 11

Here are the best charts the market has to offer right now. Use it to dig deeper, replenish your own watch list and ultimately come up with your own ideas.



Human behavior cannot be predicted. Distrust anyone who claims to know the future, however dimly. – Max Gunther, Author of **The Zurich Axioms**

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