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## **The Broadening Top Appears Yet Again!**

**By Anthony M. Cherniawski, Manager**

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I first became aware of a potential broadening top formation last August, as my cyclical studies suggested a peak in August followed by a potential decline into the fall of 2009. That was not to happen, but I remained piqued by the continued behavior of the DJIA shown in the chart below. It seems that the upper trendline defined the top of each new rally as it attempted each new high. So I kept track of the formation as a matter of routine to see what would happen next.

Finally, in December a new broadening formation began to appear. I warned about it and, sure enough, the market declined in mid-January. That's broadening top formation number 2. Finally, in the last couple of days, a subscriber warned me about yet another broadening formation developing in the major indexes. This time I think we really have trouble at Broad and Wall.

Edwards & Magee, in **Technical Analysis of Stock Trends** point out the salient characteristics of what they refer to as the "Orthodox Broadening Top." They conclude, "*The Orthodox Broadening Top has three peaks at successively higher levels and, between them, two bottoms with the second bottom lower than the first. The assumption has been that it is completed and in effect as an important reversal indication just as soon as the reaction from its third peak carries below the level of its second bottom.*" (p. 155)

John J. Murphy, in his **Technical Analysis of the Futures Markets** suggests, "The volume pattern also differs in this formation. In other triangular patterns, volume tends to diminish as the price swings tend to grow narrower. Just the opposite happens in the broadening formation. *The volume tends to expand with the wider price swings.*" (p. 150) Many analysts can attest to that, since we have seen volume spikes on both up and down days.



John Murphy goes on to say, “This situation represents a market that is out of control and unusually emotional. Because the pattern also represents an unusual amount of public participation, it most often occurs at major market tops. **The expanding pattern, therefore, is usually a bearish formation.** (p. 150)

I disagree with the “unusual amount of public participation.” A recent [article](#) in the Financial Times suggests that, “...pension funds, hedge funds and retail investors – have not been net buyers of equities. And (he says) the most likely explanation for this anomaly in the biggest stock market rally since the 1930s is that

major investment banks are the anxious buyers.” And with taxpayer money, I might add.



We finally look at the most recent pattern to discern any differences. Today’s action prompted me to issue a crash alert to my subscribers. John Murphy says it best. “While the third peak usually moves higher than the first two peaks, the last peak will on occasion either stop at the top of the second peak or not quite reach it. In such a situation, the analyst is given some additional **early warning of market failure**, and the pattern actually begins to resemble a head and shoulders top with a declining neckline.” (p. 152)

The last head and shoulders pattern may be just the tip of the iceberg. It appears to warn of imminent failure of the entire broadening top pattern, in my opinion. This is why I have included the daily chart with the three successively larger broadening formations. It may be that one or more of them may be activated in due course resulting in a cascading decline at each activation of the successively larger broadening formations.

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Thank you and good trading!

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