# How to Improve Attention to Detail During Market Corrections

by Erik Grywalski

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This review will **help you break up the market into three (3) different stock categories to better track market corrections**.

What's the major benefit of doing this exercise on a consistent basis?

**You will improve your attention to detail during market corrections**.

I've learned a lot from my own research and one of the things that's apparent is that **attention to detail is very important when it comes to the stock market**.

When I've missed important events, it's mainly because I wasn't paying attention to the market.

Breaking up stocks into different categories will help you stay in gear with the market because **you'll be checking each stock category for important facts once a week**.

This does require weekend work, but weekends are a great time to review the prior week's price action.

The market is closed, but the workweek is not over if you want to stay up to date on the market.

**The main objective is to find out what went on in the market** by reviewing as many facts as you have time for during the weekend.

Are bases being built?

Are a majority of stocks hitting new highs?

or

Is there distribution creeping into specific sectors?

As mentioned, all of the answers to these and other important questions are found by examining facts.

The more facts you review, the more ready you'll be for a potential change in the market's direction.

**What exactly are facts and why are they vitally important?**

Facts are simply the price and volume action of the market that's found on a stock chart.

The market's price and volume action is equivalent to a majority opinion on a stock because it involves **investors from around the world**.

Therefore, **stock charts serve as an unbiased assessment by the majority of investors** and are very hard to argue with if you want to be on the right side of the market.

Does the market see a stock as bullish (uptrend), bearish (downtrend) or neutral (base/sideways trading)?

With this is mind, are personal opinions worthwhile?

As you may know, there are many personal opinions on the stock market at any given time.

Personal views usually don't reflect the market because they're based on one opinion and include very few facts.

That's why they are often wrong.

For instance, an individual might be bearish on the market only because they are short a particular stock.

Unfortunately, the market may not be ideal for shorting stocks and this reveals that the individual's opinion (bearish) is not based on objective market facts.

**By examining market facts, you'll always have a majority opinion to consult and that's why stock charts are necessary to get better information on a stock.**

Think of it this way, would you rather consult one opinion (personal view) or many opinions (stock chart) when your hard-earned money is on the line?

Here's a good example of the importance of market facts (stock charts).

Do you remember the **May 6, 2010 Flash Crash**?

**Did you know that there was a lot of distribution (selling) in the market for the week ending 04/30/10?**

If you'll recall, that was the week *before* the **Dow Jones Industrial Average crashed 1,000 points intraday**.

Many were caught off guard by the May 6th decline, but the week ending April 30, 2010 was very negative for a market that hit new bull market highs earlier in the week (Monday 4/26).

Although May 6th certainly wasn't expected, it wasn't a surprise given the prior week's negative price action.

For example, leading semiconductor stocks experienced a significant amount of distribution for the week ending 04/30/10.

Former market leaders Aixtron (AIXG) and Veeco Instruments (VECO) are good examples to review.

Both were growth stocks focused on producing semiconductor equipment involved in the production of LED lights.

Technically, they finished near their lows and showed heavy distribution for the week ending 04/30/10 (see charts 1A & 1B).

Specifically, VECO had the most distribution in nearly a decade (10 years) and AIXG had its heaviest volume week since it went public in early 2005 (5 years).

That factual information was very important after their large advances and was a warning to heed from the market (majority opinion).

As it turned out, the market declined 20% by early July 2010 after the negative price action on 04/30/10.

In fact, both VECO and AIXG were in the early stages of topping and eventually fell 65% and 75%, respectively.

**Historical Stock Chart Examples 1A & 1B**: AIXG and VECO (Week Ending 04/30/10)

Click to enlarge 1A

Click to enlarge 1B

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The semiconductors are just one example of using the majority opinion (market facts) to stay on the right side of the market.

There are many more examples of negative stock price behaviors for the week ending 04/30/10, but I won't discuss them here.

Please excuse my digression, but I wanted to be sure that you were aware of the critical nature of facts.

Remember, **facts represent the market's opinion and the only way to get facts is to look at the market (use stock charts)**.

If you're not using stocks charts, you're not able to tell what the majority of investors are doing in the market.

Now that you've had a chance to understand the importance of market facts, let's get into the three (3) categories of stocks that can help you better track market corrections.

Before starting this exercise, you should take every stock (operating companies only) in the market or just the liquid stocks (if you prefer) and arrange them into the following groups by industry group/sector:

**Category 1** - Stocks Basing

**Category 2** - Stocks Breaking Out

**Category 3** - Stocks Refusing to Base

I know that this is a lot of work, but you'll be better off after it's done because your stock list will be broken up into specific categories that allow you to evaluate the market using specific facts.

You can use Excel or an equivalent software program to log your observations on the stock market.

Each weekend, you can update your file with the new changes.

**Category 1 - Stocks Basing**

Category 1 will allow you to keep track of stocks/groups that are setting up in bases. A base often forms during a market correction and is a precursor of market leadership. With this category, **you'll better recognize the groups that have the potential to break out in a leadership role for the market**. Conversely, **you can monitor the groups that may breakdown if the group/market takes a turn for the worse**.

What are these stocks doing on a weekly basis and do you see any of the base behaviors described here?

Generally speaking, **you can put a stock into the basing category** after **it closes below its 10 Week MA for the first time since the start of its uptrend** (see chart 2A).

While there's no guarantee that it won't rebound and continue higher in the following weeks, the first close below the 10 Week MA often precedes a stock's basing phase (see chart 2B).

**Historical Stock Chart Examples 2A & 2B**: AK Steel (AKS) and '06 Steel Stock Leadership


Click to enlarge 2A

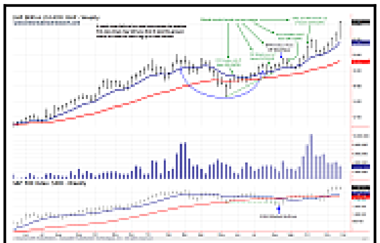

Click to enlarge 2B

I've also noticed that sometimes the market will hit new lows within a correction, but a stock that's basing doesn't (see chart 3A).

This bullish divergence is important. Is it related to a specific industry group (see chart 3B) and what might this say about the economy/market?

**Historical Stock Chart Examples 3A & 3B**: BHP Billiton (BHP) and Group at the '04 Market Bottom


Click to enlarge 3A


Click to enlarge 3B

When a stock breaks out of a base, you can move it into the next group (Category 2).

### Historical Fact on the Importance of Bases:

The **1991 Bull Market** started with base breakouts en masse. For the week ending 01/11/91, stocks from different sectors were set up in mature bases that looked ready for liftoff. This was very bullish and their future leadership out of those bases helped the market rally 45% (Nasdaq) in only 3 months. The big market rally began in earnest on 01/16/91 and included many base breakouts for the week ending 01/18/91.

**Category 2 - Stocks Breaking Out**

Category 2 will **help you gauge the market's health and see what stocks/groups are breaking out before and/or during a market rally**.

A base breakout tells you that a stock may be setting up to lead the market higher.

Keep in mind that base breakouts can happen as the market is hitting new lows (Leading Base), on a rally off a low (Bottom Base) or after a low is already established (Reinforcing Base).

I wrote about the **Base Cycle** here.

This fact about the market shows you why it's a good idea to search for stocks that are breaking out regardless of the market's current condition.

You might learn something about the market by identifying what stock/group is breaking out.

When a stock breaks out of a base, it will usually do one of three (3) things:

1. Roar Higher
2. Grind Higher
3. Fail

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A lot of what happens to a stock depends on the market environment.

What does the stock do after it breaks out (go higher or fail)?

Is there follow-through in the subsequent weeks (see chart 4A)?

Follow-through (an additional accumulation week that quickly occurs after a high-volume breakout week) is nice to see, but it isn't required for a stock to be successful.

Are there other group members coming up the right-hand side of their bases (Category 1) and getting ready to break out with your stock in a group leadership role (see chart 4B)?

In addition, if a stock pulls back after a breakout, it will usually hold its 10 Week EMA and move higher (see chart 4A).

Does this take place?

As you can see, there are many details that you need to keep track of, but I didn't say that this was an easy process.

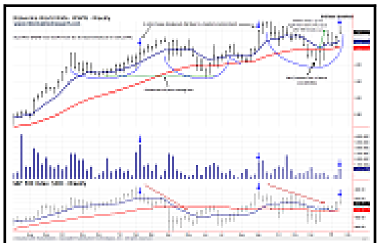
**The goal is to improve your attention to detail by keeping track of important market facts**.

With this exercise, **you'll be focused on the market and will not require much help to determine what the market is doing because you're looking at unbiased facts (the market)**.

However, you will only improve your attention to detail if you are able do the work and put in the time.

**Historical Stock Chart Examples 4A & 4B**: Nike (NKE) and Wolverine Worldwide (WWW) '94-'95

Click to enlarge 4A



Click to enlarge 4B

I've also studied stocks that break out during a market rally off a low (see chart 5A) and avoid failure when the market eventually hits new lows (or pulls back) in a correction.

This is positive because the stock is resisting the market's decline.

The stock may even pull back on top of its most recent base when the market hits new correction lows (see chart 5B).

This is important to recognize because it shows that some underlying stocks are showing strength while the market is making new lows.

**Historical Stock Chart Examples 5A & 5B**: Yahoo (YHOO) Breaks Out and Holds During '98 Retest

Click to enlarge 5A

Click to enlarge 5B

**Historical Fact on the Importance of Base Breakouts:**

The **1982 Bull Market** began in late August 1982. However, retail stocks were breaking out of bases and rallying as the general market continued to print new lows months before its early August '82 bottom. This was an important clue to identify because retail stocks tend to lead at the beginning of an economic expansion.

**Category 3 - Stocks Refusing to Base**

Category 3 can **help you judge the strength of the correction at the time you review the market**.

For example, would technology, retail or financial stocks ignore the market (refuse to base) and hit new highs ahead of the market if the correction was really that severe?

Probably not, but keep in mind that things may change.

You should change if the market changes (technically).

**I put stocks into this category if they consistently close above the 10 Week EMA during a market correction**. This is easily noticed because a stock closes above its 10 Week EMA, but the market can't.

While it's true that a stock can form a base by staying above its 10 Week EMA, it's very common for stocks to establish a base trough well below the 10 Week EMA when the market is correcting.

A base trough can occur at the 40 Week EMA or even below this key moving average, which is not a bearish indicator.

Which groups refuse to base? Are they early cycle groups (tech, retail and financial) or mid to late cycle groups (industrial, materials and energy)?

Stocks that refuse to base cannot only help you evaluate the strength of the correction, they can also help you understand whether or not bases within the same group have potential to break out and move higher (see chart 6A).

If the stocks that refuse to base remain strong, then the basing group members may break out later (see chart 6B).

While there's no guarantee that stocks that refuse to base will remain strong, they can help you identify potential market leadership.

If a stock loses strength and closes below its 10 Week EMA, you can place it in Category 1 (Stocks Basing).

**Historical Stock Chart Examples 6A & 6B**: RF Micro Devices (RFMD) Tips Off Semis in '99

Click to enlarge 6A

Click to enlarge 6B

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**Historical Fact on the Importance of Stocks Refusing to Base:**

The **2010 Market Correction** began in May and ended in late August 2010. Throughout this bearish period, some technology stocks refused to base with the market correction. Tech stocks that did base, broke out and rallied higher *before* the market bottomed in late August 2010. The market eventually reached new bull market highs in November 2010 and went higher until May 2011.

To summarize, following the market accurately takes a lot of work to stay on top of things.

**Breaking up stocks into three (3) categories will help improve your attention to detail during market corrections**.

Specifically, you'll be more aware of what stocks/groups are basing, breaking out and refusing to correct (base) during a period of market weakness.

This will help you stay focused on the market because this exercise stresses the importance of using market facts and this can only be accomplished with chart reading.