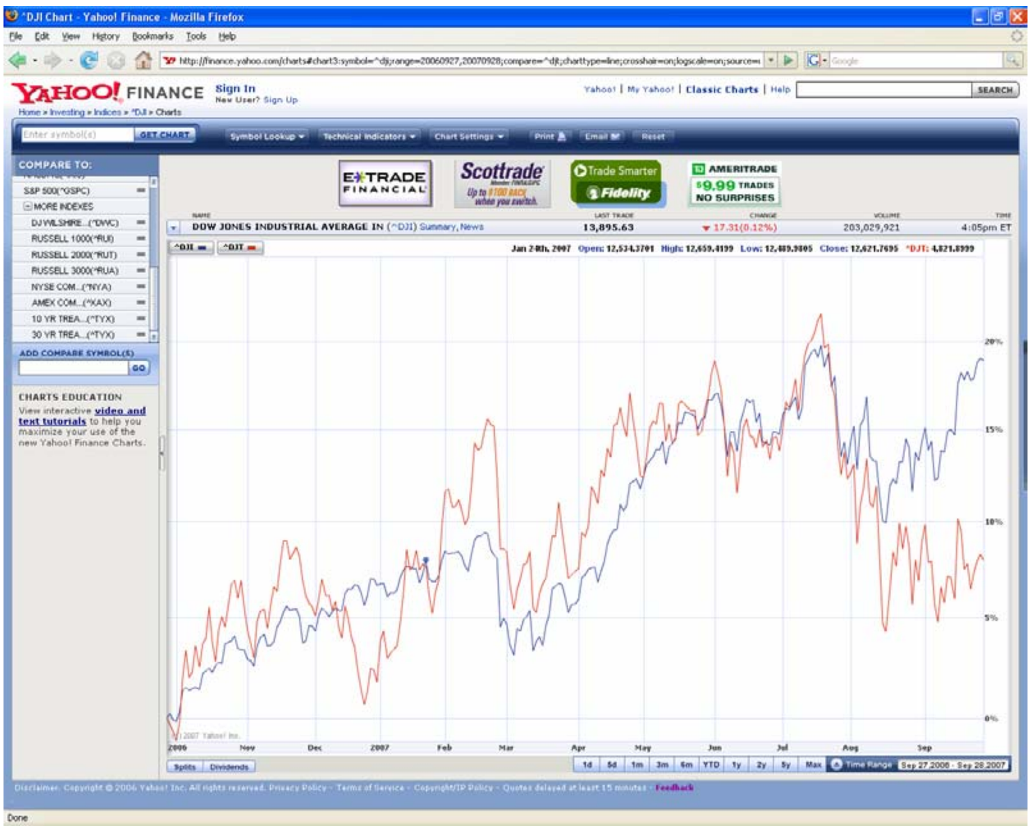
The Dow Theory

by Randall Ashbourne

Dow Theory states that price rises in the industrials – the DJI – must be accompanied by similar price rises in the transportation index – the DJT – for any rallies in the overall stock market to be sustainable.

If the DJT is not keeping pace with the DJI, a state of "negative divergence" is said to exist.

And that's exactly what we have at the moment.

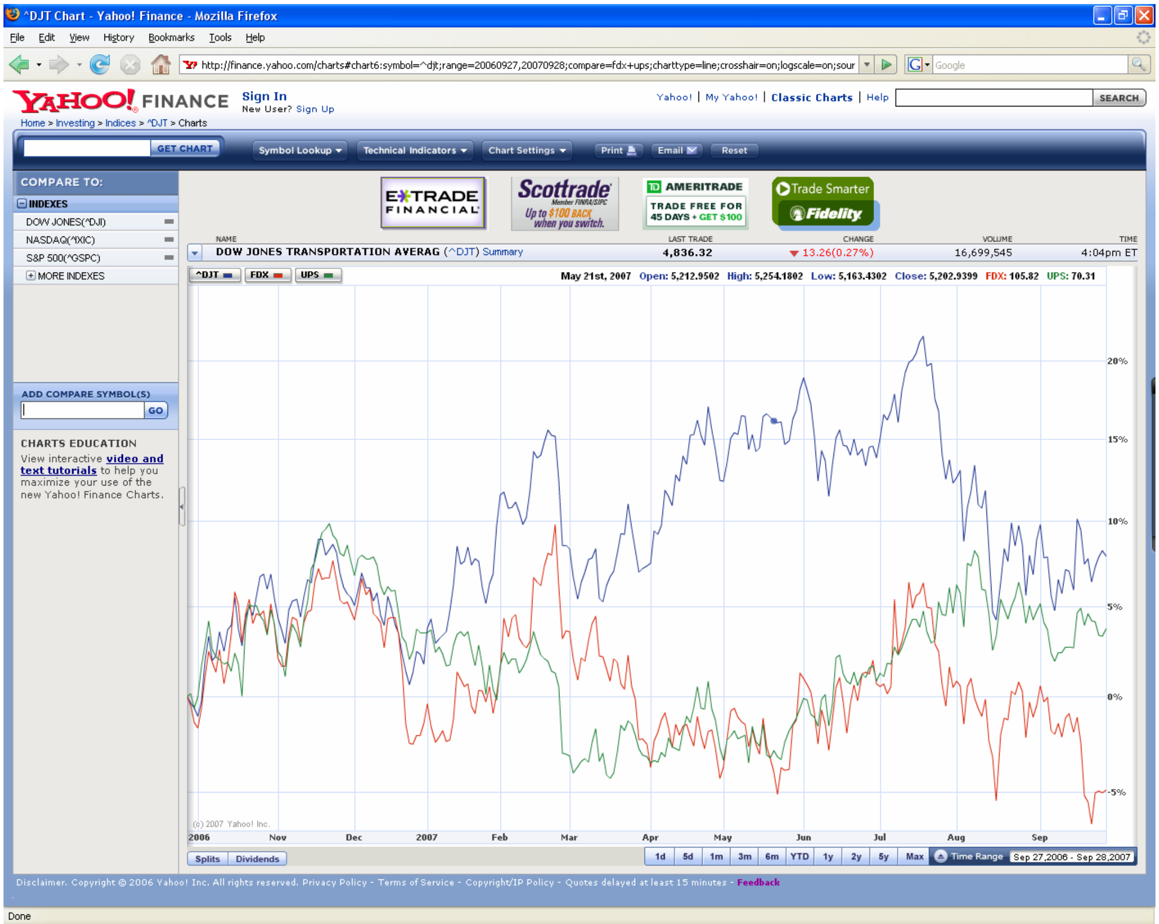


For a long time, the transport index (red line) has been keeping pace with the industrials (blue line). But, since the fall in July, the DJT has not shown nearly as much resilience as the DJI.

The reasoning behind the theory is simple and dates back to the days when one could be expressed as "factories" and the other as "railroads". The trains shifted the stuff the factories made. Therefore, if the trains weren't shifting as much stuff – either the orders from customers were dropping off, or the factories were making too much stuff which would end up causing a glut and, eventually, a big drop in production.

Two of the most-watched companies within the Dow Transportation Index, the DJT, are UPS and FedEx.

And, thanks to the free technical charts available online at www.finance.yahoo.com, we can see exactly how those companies are holding up against each other – and the DJT.



And we can see instantly that while the DJT hasn't made the same strong recovery as the DJI, UPS and FedEx have been having an even worse time of it for the past several months.

UPS, however, is showing stronger signs of recovery than FedEx.

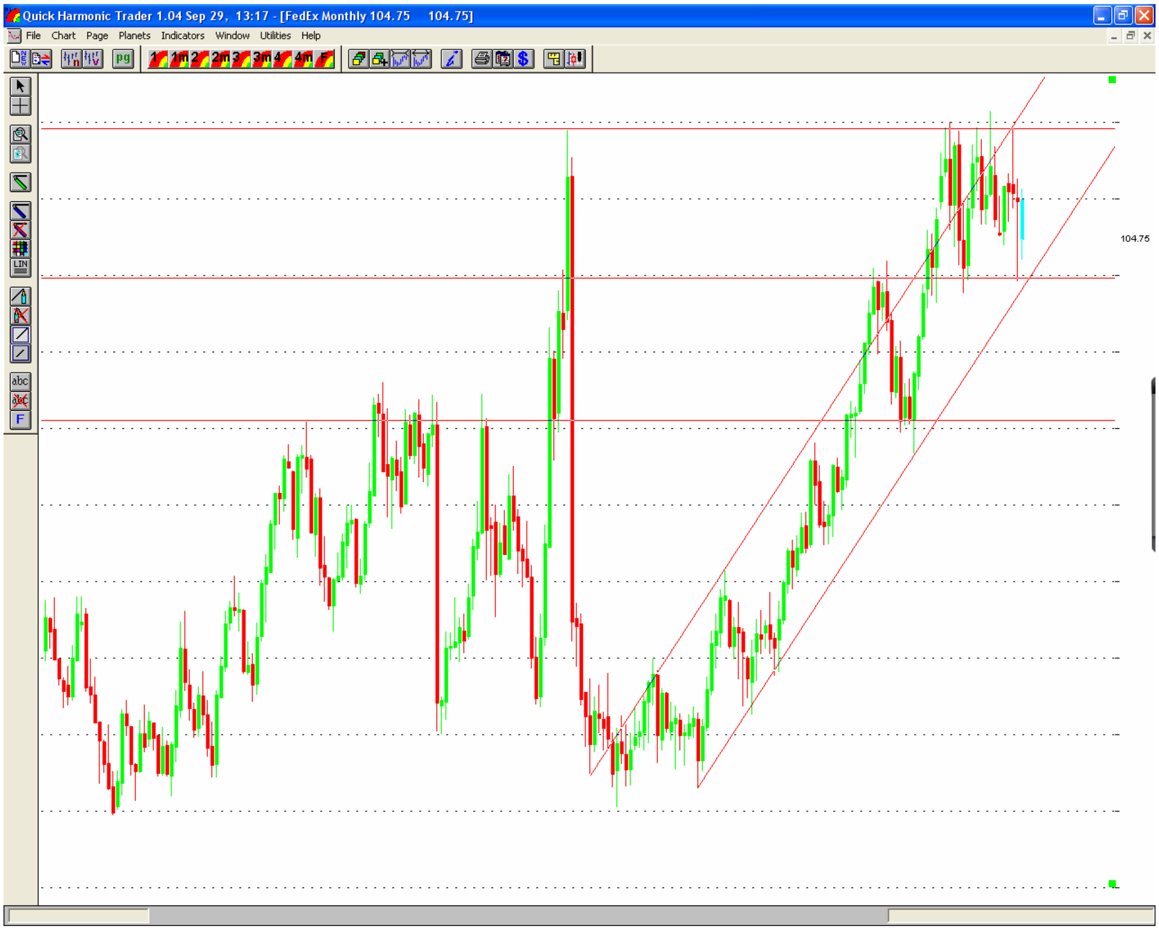
Now, if the astrological implications for FedEx are correct, the implications for a rise in its share price over the next few months aren't just a good sign for FDX as a company – but the health of the whole U.S. economy!

The first thing we need to do is look at a long-term, monthly chart for FDX to see where it is, technically speaking, in its own cycle.

Now, at least in this first glance, FDX is not looking too healthy. It has been struggling since April of 2006 to surpass that spike High it made way back in April of 1999.

The MACD line is giving us a Sell signal – and from a significant peak. And the RSI has not confirmed the strength of the breakout attempts FDX has been trying to make for the past 18 months or so.

We need to get another perspective on this chart to try to get a better handle on where FDX is going.



Now, this view of the monthly gives us a little more room for optimism because FDX is well inside the uptrend channel it started climbing in 2001. In fact, if anything, it looks as if it got a bit ahead of itself in 2006 … and needed to go sideways for a while to build a Time base before launching into any new Price phase.

These long-term Time phases are always followed by an explosive move in Price – as we can see from the force of the sudden drop from those three thrusts to break through resistance before soaring to a sudden spike in 1999.

So far, so good … FedEx has bounced from the support/resistance line created by that peak in late-2004/early-2005 … and we do not have long to wait to see if it is going to repeat that very regular pattern it has been in since 2001 of bouncing strongly upwards from its multi-year trend line.

The weekly chart is a little ambivalent. The 12 EMA has crossed below the 72 EMA and the stock price itself has actually dropped below its 100 EMA

On the positive side, there are some signs of emerging positive divergence between our indicators and the price. The MACD line appears to be in the process of making a shallower trough … even though the price is lower than its previous trough. The MACD histogram also is showing an inclination to develop a higher trough – and the RSI is at a level from which we could expect it to recover.

And to add to the positive omens, we can see a couple of significant weekly price bars which are standing tall on their long tails.

So far, we have some conflicting views, technically, about where FedEx is heading next. What we do know is that it has spent well over a year oscillating between $100 and $120 and that it is currently at the lower end of that price range. Any positive astrological aspects at all could be expected to drive it back up towards the top of the range.

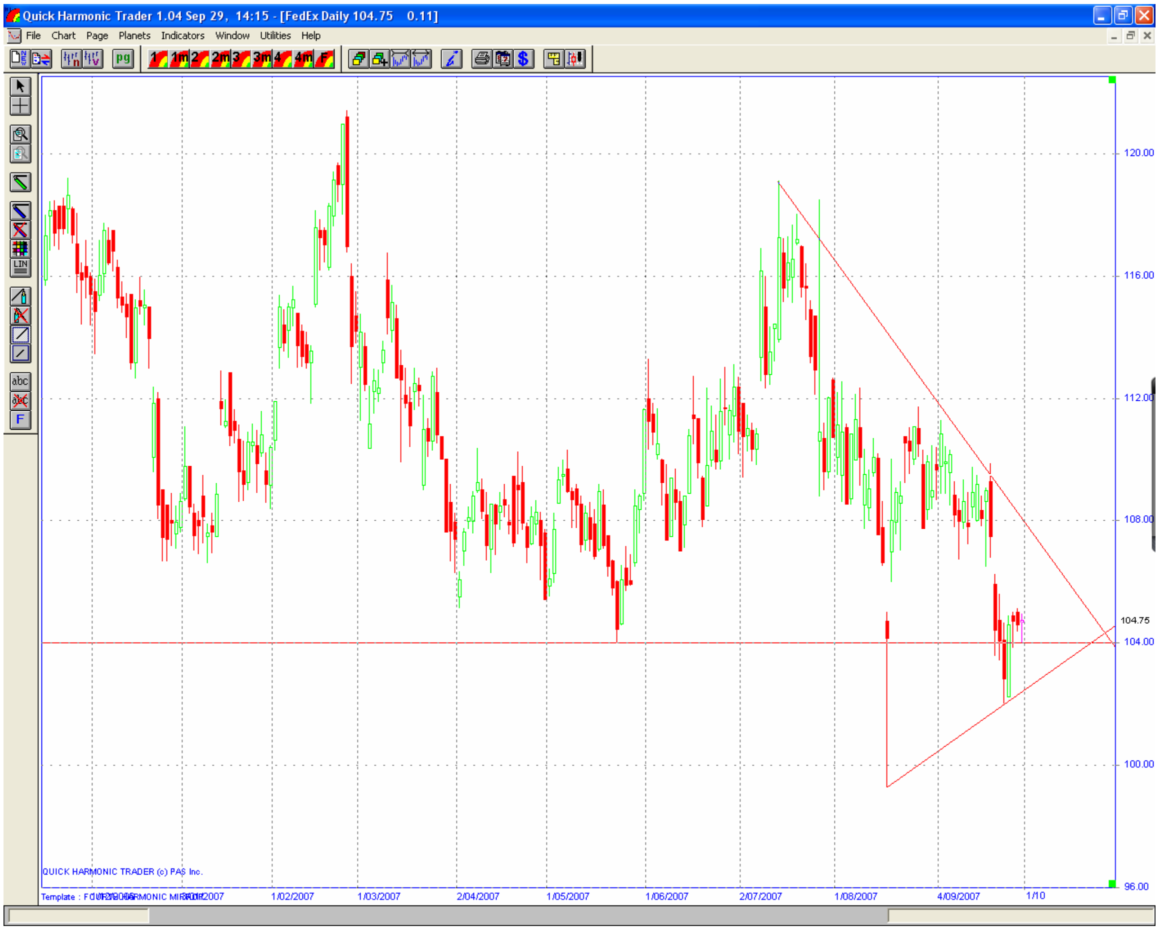
And we know it has spent an awfully long time building up a head of steam – it would not be unusual for it to suddenly explode in one direction or the other, carrying it through either the long-term support, or resistance, lines.

So, let’s see if a look at the daily can provide any further clues about the direction.

Once again, the technicals are not giving us a picture of perfect clarity. But, we can see some signs of positive divergence. The troughs being created by the MACD line and the CCI are not getting deeper, even though the most recent price action is more negative than that one-off plunge price bar from mid-August. The short-term 5 EMA is beginning to level out, even though the 12 and 72 are looking decidedly negative.

The price is at the bottom Bollinger Band – a rough-guide reading that the stock is oversold, which agrees with the RSI reading on our earlier, weekly chart. And the top Bollinger Band has curled down, indicating that the downward movement in the price has come to a stop, at least temporarily.

Now, we’ll have a closer look at the daily chart.



We can see the current price is sitting exactly on a support line – and we can also see exactly where the price needs to go to break out of its short-term constraints. It needs to hold above that short-term trend line … and then break upwards through the trend line which has capped its price since mid-July.

©2007
Randall Ashbourne

***

*QHT Technical Charts created using Quick Harmonic Trader Software, by P.A.S. Astro-Soft, Inc. makers of Galactic Investor Astrology software.