accumulating the stock in the first place and is the first phase of distribution on their part). **The point at which this "reaction" stops will become important, as it is this point which must not be violated after the stock begins its next leg up.** If it is, there may not *be* another leg up.

These drives upward should all be accompanied by good volume--not necessarily great volume, but enough volume to keep the price moving. Consider that once you've got your car moving, you don't

need to give it much gas to keep it moving, but you do have to goose it from a standing position to get it going, or from a cruising status to pass somebody who presents an obstacle to you (a level of resistance?). **Any bouts of profit-taking or near-term shyness about busting through a resistance level should be accompanied by lower volume.** If volume increases, you may have a problem. If it increases dramatically, we're not talking typical profit-taking here. Act accordingly.

The pattern of these moves may resemble arrow-heads--move up a lot, pull back a little, move up a lot, etc. However, they may also look like a series of ascents interrupted by plateaus (like a Mayan pyramid). **These plateaus, or bases, or congestion areas, require just as much attention as the profit-taking pullbacks, for one of these plateaus is likely to be the final resting place before the rocket makes its return trip to earth** (you may want to look at Rectangles again), or at least alters its course to an earthward direction. How accurate you are in determining which of those plateaus is going to be the last stop will depend on how well you can spot **distribution.**

Before getting into distribution, however, there is one other stunt which the stock may pull on its way up and which may cause you grief. At some point during the markup phase, the stock will swoop upward in a ski-lift-turned-on-its-end sort of **climax run** in which volume explodes, the price soars skyward, short-sellers scramble to cover, "over-extension" acquires a whole new meaning, and green newbies everywhere are rubbing their hands with glee when they ought to be sweating bullets (this particular phenomenon is linked to all sorts of sexual metaphors that we won't get into here; you can probably guess what they are). If you're ever lucky enough (or unlucky enough, depending on how it all turns out) to be caught up in one of these rocket rides, keep in mind what happens to rockets when they run out of fuel.

It's not pretty.

Remember that volume is a two-edged sword. As stated earlier, you can have too much of a good thing at breakouts. Likewise, **if it seems as though you're getting too much of a good thing after your stock has run for a while, start thinking "top".** Even if your stock doesn't launch itself into a climax run, take the market's temperature. If there seems to be a general consensus that your stock's price can only go higher, locate the exit door even if you're not quite ready to lunge for it.

Distribution

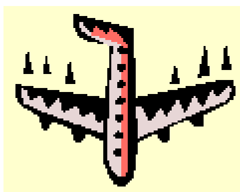
At some point, demand will not only diminish, but dry up. As the Street puts it, trees can't grow to sky. Buyers have run out of greater fools, and no one is willing to pay a higher price for the stock, at least for now. On the other hand, there aren't a great many people who want to sell, either. They like the stock, want to hold onto it, think it's worth what's being asked for it, and are willing to wait for a new wave of demand, spurred perhaps by news or rumor or earnings. Some may want to sell, and there may be buyers who are willing to pay the ask, but there aren't very many, if any, who are willing to pay anything higher.

So there it sits, and if its angle of ascent was 45 degrees or less, it may sit for quite a while. **Your task is to determine whether the stock is just resting, or whether it's sharpening its machete in preparation for cutting you off at the knees**. The angle of ascent, as just has a lot to do with danger level (the steeper it is, the more vulnerable the stock becomes to the withdrawal of experienced buyers). So does a careful analysis of the relationship between price and volume. **It is here and on the way up to here that distribution (a process whereby the accumulated store of stock is sold at the highest possible price) takes place, not on the way down,** and unless you enjoy wedgies, learn to recognize the signs.

As an upward move deteriorates, price spreads narrow and less price progress is made from day to day. Determining whether or not this is a result of the stock's meeting supply will help you decide whether an ensuing reaction is profit-taking or a mad dash for the exits. If volume remains strong, the stock is most likely meeting supply (distribution), and whatever shares are offered to the market as a result of profit-taking will be absorbed by this demand (as long as nobody gets spooked) and the stock will resume its advance (but watch that trendline). If, however, volume diminishes as spreads narrow and progress is less and less, or if volume was strong and is now diminishing, it is more likely that demand is diminishing as well, and trouble may be coming 'round the corner PDQ.

It is extremely important at this point to focus on the price-volume relationship, unless you

enjoy holding the bag (it is also extremely important at this point that you not take any vacations). Watch where the stock begins to hesitate. Does volume begin to pick up when the stock closes closer to its lows? Is each successive low lower than the one previous? If and when the stock rallies, is volume higher or lower? Are rally attempts stopped (met by further supply) at the same place each time? Does each attempt end lower than the one previous? If volume promptly decreases when the stock begins to roll over, it's unlikely that the market is ready to kick it down the stairs, but **it's important to note the quality and character of rally attempts.** If each one is coincident with stronger volume, but is stopped at or near the same place each time, then a considerable amount of supply needs to be worked through. Again, this is part of the distributive process, and it may be taking place at some older level of resistance, but **distribution is not necessarily a death sentence for a stock.** It simply refers to the process whereby elephants unload sizeable portions of their accumulated store. As long as demand is sufficient, they can exit entirely and the stock will go on its merry way building a Stairway To Paradise.

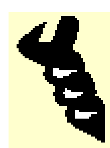


On the other hand, **if volume picks up on the downside, you've got a problem.** Some investors will hold the stock and wait to see where the reaction stops. If it stops at an important support level, wonderful. If it blows through that support level, they sell. In a volatile and nervous market, this strategy can have its drawbacks, since the stock may not be taking its leisurely time to telegraph all this information. It may, in fact, sink like a stone without giving any warning whatsoever. Which is why **smart money learns how to recognize distribution and to sell at the same time the *rest* of the smart money does.**

On the third hand, there is always the possibility that your worries are for naught, and that the stock is merely basing again. Evaluate this base just as you did the last one when the stock was being accumulated, though this base may be considerably shorter. Ask yourself the same questions and note the same phenomena. If volume declines and continues to fade away during reactions, not much stock is available for sale, even at the lower prices asked at the bottom of these reactions. If the price ranges widen, the closes move higher toward the highs, and volume gradually increases, you should most likely get back on the bus for the next leg up. Beware, however, of the red-spotted **thrust.**

Thrusts

Thrusts are a particularly ugly feature of bases in which distribution is taking place. **They are designed to sucker amateurs into thinking that the stock is getting ready to advance again** when, in reality, the elephants are merely harvesting the wallets of the unwary so that they (the elephants) can unload whatever they have left before they catch that plane for Barbados.



Thrusts are pretty much the same as shakeouts, only in the opposite direction--a spike in volume, a rapid move upward, perhaps even a close near the high. But, like the shakeout, there's no follow-through. The novice, thinking he's "missing the move", jumps in all innocent and dewy-eyed, at which point the floor collapses beneath him and he drops down the rabbit-hole. The price drops back into the base or below and, before you know it, we're on a sleigh-ride to perdition.

How do you detect a thrust? It's unlikely, though possible, that demand sufficient for a genuine breakout will just appear out of nowhere without any warning whatsoever. Any such move should be viewed with suspicion. If you can't get in within 5% of the buypoint, pass. Even if you can, don't take any magazines into the bathroom. Stay in front of your computer and watch to see that the bottom doesn't fall out of the "advance". If you're using daily charts, you may want to consult an intraday chart (if you're already using intraday charts, check a shorter bar interval). If any of this activity looks the least bit suspicious, start exercising your trigger finger to place that "sell" order if necessary. **Do not hang onto the stock if it closes at or near the low for the day, much less below your purchase price.**

Markdown

At the end of a base or congestion area which has been used for distribution, the price either continues to advance on the wings of new demand, or we enter the markdown phase. The markdown phase is the most depressing and often terrifying part of the entire cycle, unless you specialize in short sales. It is here that hopes are dashed, doubt turns to fear and fear to panic, and Tiny Tim gets trampled in the rush to the exits. The elephants are done, investors who bought in during the just-completed base and have no profit whatsoever will be (if they're smart) the first to get the hell out, and absolutely no one is supporting the price anymore, except perhaps for green newbies and a few truly clueless individuals who seize this "opportunity" to average down. **Supply is thrown onto the market, as evidenced by widening price spreads, increasing volume, and increasing downside deterioration.**