The S&P just hit a new high, but the bond market, Netflix and Caterpillar are sending worrisome signals.

The stock market came roaring back to life after the debt ceiling was raised last week, but now looks like it needs a little rest. The bullish trend that began almost one year ago remains intact, but as they say, nothing moves in a straight line. And that means investors do not have to chase the market right now.

The Standard & Poor's 500 reached the top of a ragged rising trend channel Tuesday (see Chart 1). A rising trend channel is simply a trendline drawn through a rally's lows and a parallel line drawn through its highs. At the top of the channel, the rally tends to stall and prices head back down to the channel bottom. It's nothing more than the normal ebb and flow in a bull market.

I call the current trend channel ragged because its borders are not parallel. However, the spirit of the pattern is quite visible with regular highs and lows forming borders that are close enough to straight
lines. Technical analysis purists will object to this classification, but sometimes we just have to let the market speak rather than trying to impose rigid order on it.

On the chart, it suggests the S&P 500 is within a few days of a short-term top if it did not already peak Tuesday. But there is no evidence at this time that the lower border of the channel will break to the downside. That means investors should do some homework now, looking for stocks that pull back gently on low volume, and wait for the market to find its footing over the next week or two.

Of course, it is rarely that simple. There have been a few troubling developments recently, including the intraday collapse Tuesday of one of the market's most impressive leaders, Netflix (ticker: NFLX).

While its trading action created a very negative technical event, I think the psychological impact on the market was worse. The high-profile, sexy names leading the advance are no longer bulletproof, and even though the broader market closed higher on the day, the leadership ranks have been damaged. It does not help when we also get a slew of giant earning-induced moves in both directions at the same time. As an example from Wednesday's action, for every Boeing (BA) jump up, there is a Caterpillar (CAT) jump down. Such manic behavior beneath the surface suggests the market is unstable despite the overall rising trend.

The bond market is also flashing a warning signal. Long-dated Treasury bonds have broken out to the upside, which suggests a flight to safety is underway despite the many analyst calls to take more risk—meaning buy stocks.

The iShares 20+ Year Treasury Bond ETF (TLT) moved higher from an inverted, or upside down head-and-shoulders pattern Thursday, Oct. 17 (see Chart 2).

Chart 2

iShares 20+ Year Treasury Bond ETF
The date is notable, not for what might have been said in Washington or on Wall Street but for analytical reasons: In the immediate aftermath of the debt and budget agreements in Congress, stocks took off to the upside while bonds eased lower. We can blame bond weakness on the prospect of another budget battle in January, thanks to the temporary nature of the deal.

But on Oct. 17, bonds sprang to life, even as the euphoria in the stock market continued. Chris Kimble, proprietor of the technical analysis oriented Kimble Charting Solutions, noted that the setup—the upside down head-and-shoulders—has appeared only four times in the past seven years and each time it led to a substantial rally.

Using a chart of the 10-year Treasury yield (which moves in the opposite direction from the price), he also pointed out that these patterns took place at the upper border of a long-term trend channel. That suggests lower yields ahead and higher Treasury note prices.

With bond sentiment very bearish, the rise in bond prices is even more impressive. And that suggests a bit more nervousness over the stock market than we can see on the surface just one day after it reached new highs.

The major trend in the stock market is still to the upside and while short-term factors suggest it is time for a normal pullback, the psychology of the market seems ill at ease. The bulls remain in control, but it might be wiser to let the market rest to let it work out some of its issues before hopping back on the bandwagon.

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