SHIELDS & COMPANY
MEMBER NEW YORK STOCK EXCHANGE

EQUITIES PERSPECTIVE

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DJIA: 12,284

Monoline . . . isn't that a disease? If nothing else the credit mess has served to expand our vocabularies. First there was "subprime," 2007's word of the year, and now there's "monoline." Of course "monoline" isn't at all what the word suggests. This isn't some reference to insurers who write but one type of insurance. The reference here is to those insurers who write but one kind of insurance and that kind is the wrong kind, that is, bond insurance. For that matter there's nothing wrong with bond insurance if it's insurance on municipal bonds, which don't really need insurance anyway. The problem, like most problems these days, arises from insurance written on the myriad of mortgage derivatives. And if the insurers should lose their AAA ratings, as is threatened, then what they insure could lose their ratings, and so on. And then there's the auction-rate municipal bond market, something most of us never heard of until the last few days when that too became a crisis. At a more mundane level KKR, a unit of famed private equity giant Kohlberg Kravis Roberts, delayed repayment of mortgage related debt for a second time. The credit markets still seem broken, but for now the stock market doesn't seem to care.

What may be most important in the midst of the ongoing financial crisis is that financial stocks, those stocks you would think most effected, continue to hold. The Financial ETF, XLF, and the Regional Bank ETF, RKH, offer good proxies here. Much like the overall market, however, holding is about all they have done lately. That's good in light of the news, but it wouldn't take much to send either back to the lows. Any break to the upside from these little trading ranges, however, could set the stage for another leg up for the market. For now at least the stocks have stopped going down on every little piece of bad news, and that's what you would expect of an important low – the news stays bad at a low, but it has been discounted. And we still think these Financial stocks are key to any important overall low. They got us into this mess, they have to get to that point where the mess gets discounted. They're not going to come back to be market leaders, but coming out of these little trading ranges to the upside would seem a positive.

Financials aren't the only thing holding, the whole market is stuck in a holding pattern. The averages like the Dow are stuck somewhere between the January 22 low and the February 1 peak. Overall daily New Lows have stayed pretty tame at less than 200, a good sign that most stocks are holding. Even the Semiconductors, which Tuesday looked about to break, managed to pull themselves together the last couple of days. That chart, however, is still teetering, and for that matter so too is the NASDAQ Composite. Breadth there, by the way, made a new low on Thursday. With the exception of Research In Motion (107), which rallied Thursday, the Apples (121), Amazon's (70) and Google's (503) have had virtually no rally, and look about to add a leg down. This handful of stocks was the NASDAQ driver for most of 2007. That's likely to remain the case in 2008, only this time to the downside. The idea of "recovery" doesn't apply to the NASDAQ. Indeed, dead cat bounce seems more appropriate.

Stocks may be going nowhere but commodities have been surprisingly strong. Surprising, that is, if you believe that we're in the midst of a global slowdown. Not so surprising perhaps, if you believe the Fed will continue to lower rates and the dollar continue to fall. There is just a tad bit of a dilemma there – lower rates and help the economy, or lower rates and raise the price of gas and everything else. That's why we turned down that position at the Fed, sticking instead with the charts. And the charts show a bit of a discrepancy between what's going on in commodities, the stuff, and the commodity stocks. Oil is a perfect example, but for that matter so too is Gold. USO is a measure of Oil the commodity, while XLE is a measure of Oil the stocks. As you can see, there's quite a disparity, a divergence as it were. Much the same divergence exists between GLD, Gold the actual bullion, and GDX, the Gold Mining stocks. It's tempting to believe the stocks will catch up with the respective commodities, but more often than not they don't. Like most divergences, more often than not it's a warning, likely for both.

Holding up in the face of bad news, including Wednesday's CPI report, is one of our favorite things. Strong markets ignore bad news, weak markets ignore good news, and so on. Then too, holding up isn't going up. The market looked on its way to a good day Tuesday, but faded into the close. The market looked on its way to a bad day Wednesday, but rallied into the close. Thursday was Tuesday again, so go figure. Thursday's near 3-to-1 negative breadth, however, likely means we're in for another test of sorts. But there are no important divergences – big board breadth has kept pace with the market averages – and that seems important. While we see this as a bear market rally, the overall picture still looks a bit too technically healthy to add a new big down leg just yet. That may not prove true for the NASDAQ, though, with the Apple's and so on threatening to break. For the overall recovery, however, without some telltale negative technical signs like divergences, we're inclined to give it the benefit of the doubt.

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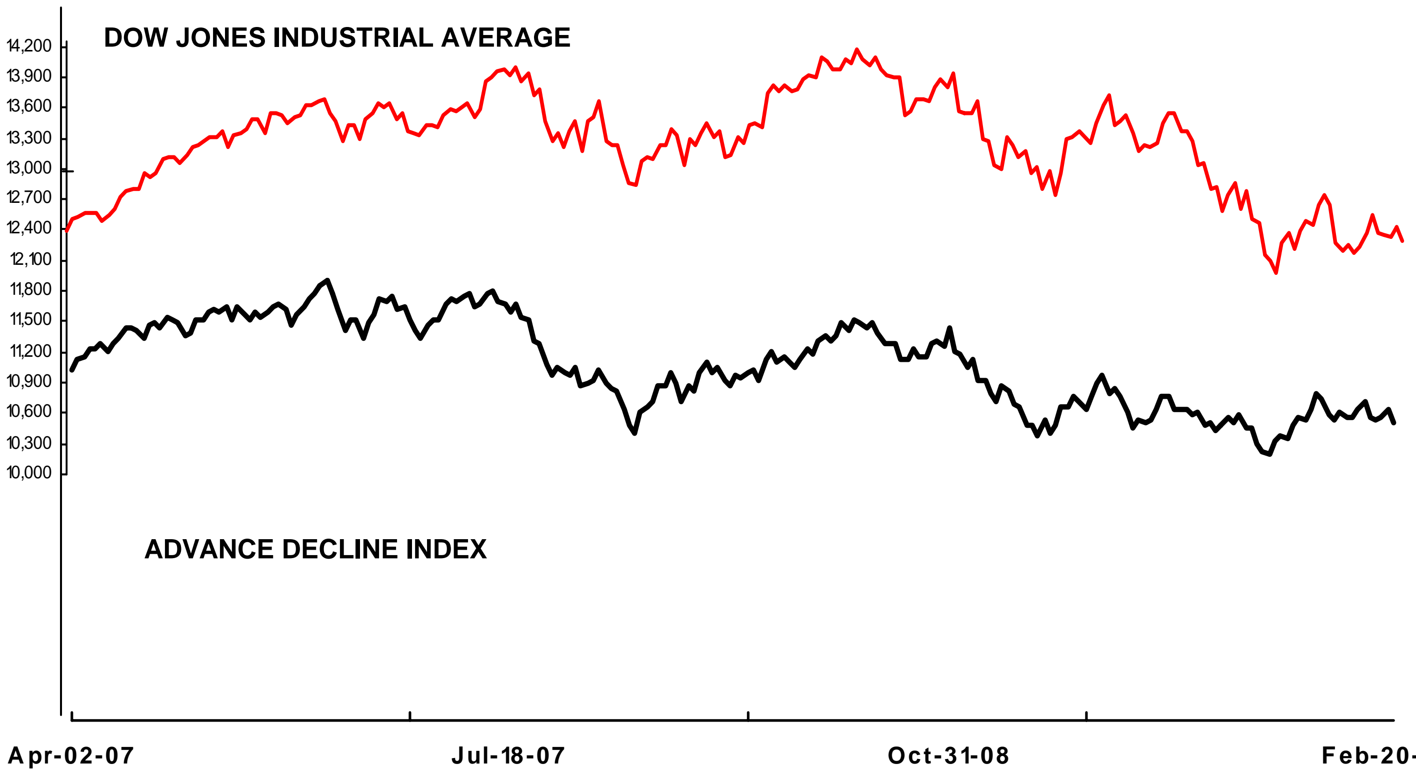
STOCK AVERAGE VS. AVERAGE STOCK
DOW JONES INDUSTRIAL AVERAGE
14,200
13,900
13,600
13,300
13,000
12,700
12,400
12,100
11,800
11,500
11,200
10,900
10,600
10,300
10,000
ADVANCE DECLINE INDEX
Apr-02-07
Jul-18-07
Oct-31-08
Feb-20-08

FINANCIAL INDEX (XLF - 27) – DAILY
50-day simple m.a.
Holding

SEMICONDUCTORS (SOX - 352) – DAILY
50-day simple m.a.
Like Most Stocks - Holding

NASDAQ COMPOSITE (COMP - 2300) - DAILY
50-day simple m.a
NAZ Breadth At New Lows

APPLE (AAPL - 122) - DAILY
50-day simple m.a
Teetering

OIL (XLE - 74) - DAILY
50-day simple m.a.
Diverging From The Commodity

GOLD (GDX - 51) - DAILY
50-day simple m.a.
Diverging From The Commodity