

EQUITIES PERSPECTIVE

April 17, 2009

DJIA: 8,125

Opting out of becoming the Post Office . . . Goldman gives back the dough. The Goldman news, however, apparently didn't outweigh a weak retail sales number, resulting in Tuesday's moderate selloff, one of the few to see volume expand. It was also one of the few times the market hasn't reacted to good news or, for that matter, reacted to bad news. No market's perfect but, this one has been close. Down days per se are rare, in terms of breadth only eight since March 9, and never more than two at a time. The market has been stubbornly strong, defying expectations for the "overdue" correction. No doubt it's those expectations that have contributed to the ongoing strength. The market doesn't accommodate the majority, good markets don't give you a good chance to get in. That said, of those eight down days, a few saw a pretty good pasting and, of course, there will be more. For now, however, it's going up like it went down.

Given the run you often hear it said the market is very "overbought," that is, extended to the upside. While it may little matter, we don't quite see it that way. Technicians all have their favorite indicators, among them oscillators that move between overbought and oversold levels. To each his own, but among others we like to look at the spread between the S&P 500 and its 10-day moving average, obviously a short term measure. As it happens, this indicator isn't exactly oscillating in its typical manner. The oscillating, so to speak, is pretty much between neutral, and moderate rather than extreme overbought levels. We all know the market is strong, but this indicator suggests that it's strong in a contained sort of way. On a medium term basis we like the percent of NYSE stocks above their 200 day moving average. Reflecting the devastation, this measure was at 1% in November, an all-time low, and 2% as recently as early March. It has been creeping up and currently stands at 25%. That improvement is a big positive. But if you consider the typical range in this measure is between 20% and 80%, there's plenty of potential improvement left. On a medium term basis, the market is not at all overbought.

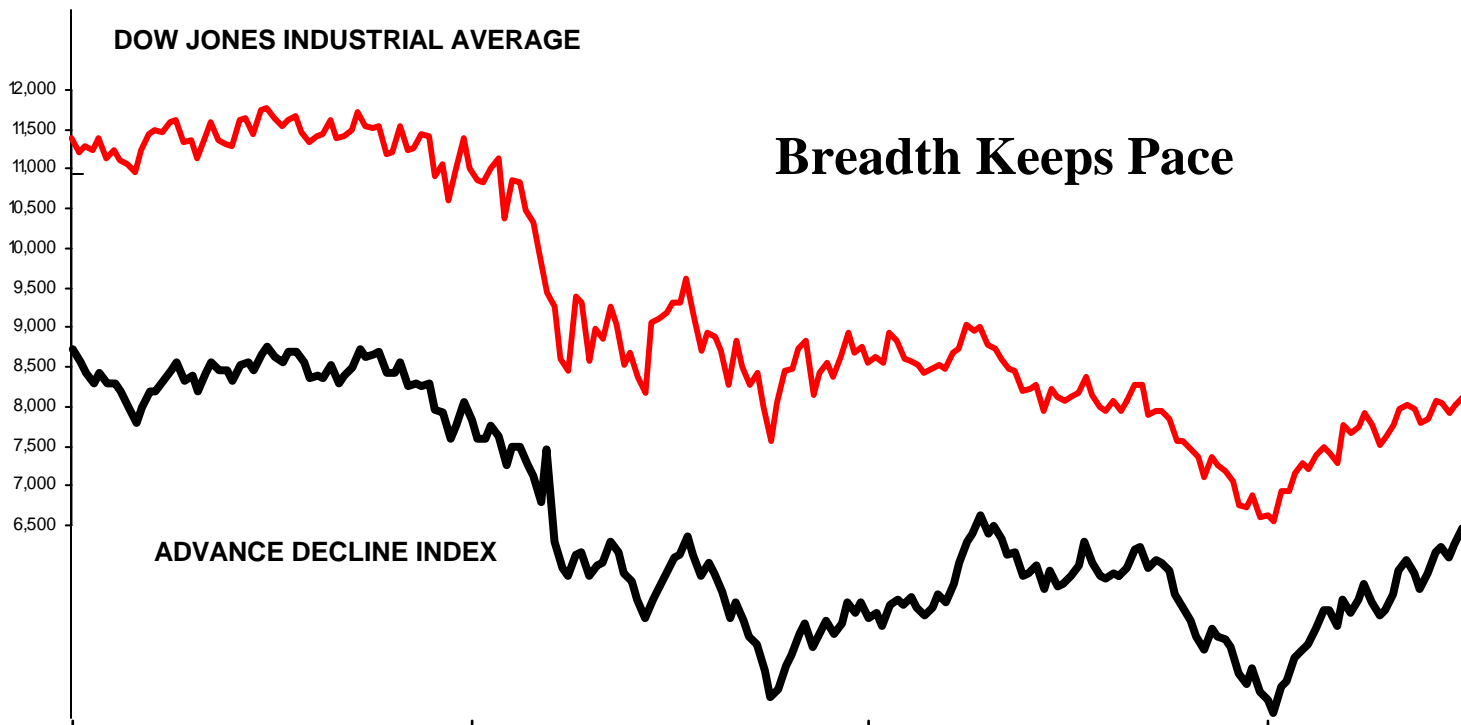
The key to this market, or any market, is just the basics. Volume should expand in strength, showing a real buying interest, and contract into weakness. Of the eight down days since early March only three saw volume expand, one of those being Tuesday. However, Thursday's rally with expanding volume seems once again to have gotten things back on track. The other key is market breadth or the action in the average stock versus the stock averages. This market will eventually have a correction, you heard it here. And it would be nice if any weakness was modest, and volume contracted in the weakness, showing no real selling. But more important than the weakness is the ensuing recovery. You don't want to see a light volume recovery, that is, a recovery with no real buying. And you don't want to see a rally with poor breadth, a rally in the averages without the participation of most stocks. When there's divergent action between the averages and market breadth, only bad things happen.

Retail sales fell sharply in March, surprisingly so. Just as surprising, however, has been the strength in retail stocks. Based on IBD's rankings, the group vaulted from 124 four weeks ago to 10 on Tuesday. During that time Macy's (11) and J.C. Penney (25) were up 93% and 88%, respectively, Nordstrom 89%. The recent weakness in the stocks seems less about "retail sales" and more about these out-sized moves. At its peak on Monday Macy's was some 50% above its 50-day moving average, a lot for any stock, for Macy's a whole lot. Whether these stocks are in the throes of discounting, a good Christmas seems questionable. However, it does seem clear that back in November they pretty much had discounted, no Christmas, ever. But the real key here was the March low, holding as it did well above the November low. And the March strength seems to confirm the November washout, and the subsequent test in March. As per the above, the stocks are extended. But they should have more to go regardless of "retail sales."

Another group with similar credentials is Semiconductors. Like Retail, the washout low was November, a higher low Feb-March, and a sharp rally since then. And, as the Intel (15) guidance suggests, the outlook here, too, is anything but clear. But so it goes at turns, all of that seems to have been discounted back in November, hence the higher low in March and subsequent rally. Like retail sales, the Intel (16) news proved a catalyst for a little correction here as well. But, like retail, nothing terminal. The NASDAQ 100 also held its November, suggesting a favorable outlook for Tech generally. By comparison, consider the Financial or Bank Indices, where there were lower lows in January, February and March. The rally has been sharp, but the overall pattern much less favorable. And that's pretty much what you would expect. Groups that lead in one cycle don't come back to lead in the next. By the time any sector gets to a market-cap of 20-25% of the S&P – Oil in the early 80's, Tech in the late 90's, and Financials recently – it's a sign they're over-loved and, more importantly, over-owned.

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STOCK AVERAGE VS. AVERAGE STOCK



Jul-01-08

Nov-19-08

Apr-15-09

