

EQUITIES PERSPECTIVE

May 1, 2009
DJIA: 8,168

Pigs can't fly . . . but swine flu? It's always something. If the Banks don't get you the swine will, or is that redundant. Who knows the ultimate outcome of this most recent curse, but the outbreak comes at what would seem a critical time for the U.S. economy. Recent releases like Consumer Confidence are among some faint signs of improvement, the "green shoots" as they're fond of saying. Looking to the SARS crisis as precedent, there would seem ample reason for concern. During that period Hong Kong underperformed global markets by 15%, and the market's relative performance didn't improve until more than two weeks after the number of new SARS cases had peaked. With that in mind Monday's big down opening hardly seems surprising. Indeed, what does seem surprising was the good close that day, and the strength the rest of the week, particularly Wednesday. What can you say, they want to go higher.

They want to go higher and that, seemingly, regardless of any news. Take Wednesday's GDP report, a more than expected 1st quarter decline of 6%. On the news the market rallied more than 200 points, before closing up 170. Too bad GDP wasn't down 12%. You might wonder how the GDP report could be construed as good news. Indeed, how can much of anything these days be construed as good news? To begin to understand all this that seems unreasonable, you have to remember the market isn't the economy, stocks aren't earnings. In the long run they are, but certainly not at important turning points. Especially at such points, it's all about supply and demand. When stocks are sold out, the news is always bad, that's how they got sold out. And sold out, no more sellers, means it doesn't take all that much buying to run them up. The October "washout" low, the November test, the March test, all in their way suggest a market that was sold out.

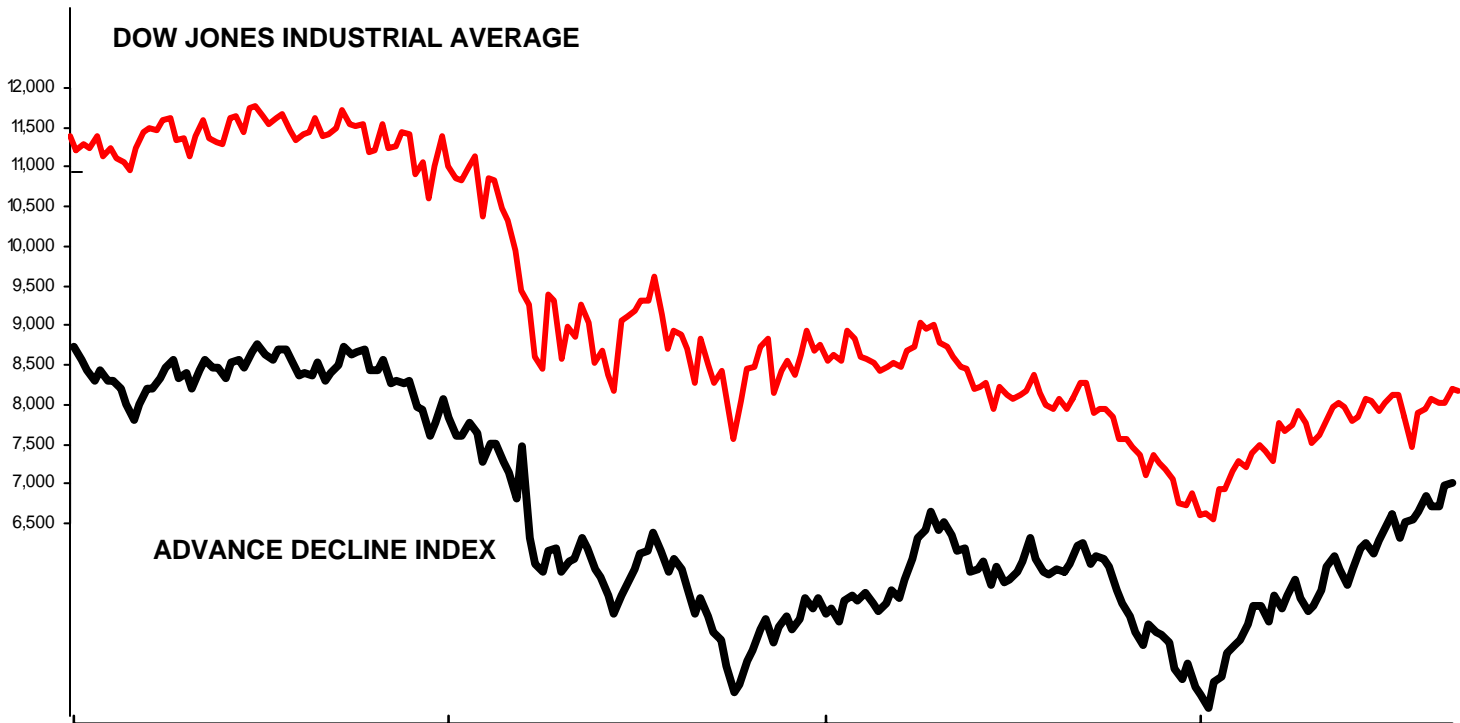
The market rallies unexpectedly, the market gives up very little and, yet, the feeling is it's not to be trusted. Back in the fall of '07 anyone would have jumped at the chance to buy the market down 50%. And why not, the biggest worry back then, how funny is this, was that interest rates might rise. The world looked fine though, in technical terms, there were signs of trouble – Financials had peaked 5-to-10 months earlier, more than a bit prophetic. Speaking of prophetic, might the market now see the same, but opposite, sort of thing that was difficult to see in the fall of 2007? Consider, part of the recent GDP report showed real inventory plunged the equivalent of 0.9% of GDP. In the past, similar plunges have been associated with the end of recessions. And, unemployment claims on a four week basis are down 12000. According to the ISI Group, unemployment claims have correctly marked the end of every recession since 1982 – a 40,000 decline in claims having called the turn within a month.

It could be the recession is ending, or it could be a new bull market has started. Bull market, bear market rally, whatever, they're going up. And they're doing so impressively – good volume and even better breadth. Volume expanded in Wednesday's rally and despite Thursday's fade, breadth was positive. Most remain skeptical and even those bullish now seem caught up in looking for the elusive correction. Indeed, there's been a correction, but the correction, which was more sideways than down, only served to increase the pessimism a bit. Meanwhile, the lack of public buying of mutual funds is virtually without precedent. Cash flow was a minus \$27 billion in March, and has averaged a minus \$20 billion per month in the last 12 months. By comparison, there was a positive cash flow of almost \$21 billion per month during the 1998-2000 period. This reflects an amazing degree of pessimism among this group of investors and, of course, also reflects a considerable amount of potential demand. If the past is a guide, opinions will change before the recovery is over.

A couple of key words these days are "better," as in better than expected, and "beat," as in beat estimates. While there is definitely a better tone to things, much of that has to do with the rally – news follows price. After all, it's not every day a major car company files, and no one seems to care. We harbor doubts about an economic recovery, but not the recovery in stocks. Momentum like this doesn't turn on a dime. The "average stock," market breadth, acts better than the Dow, and that's just not how the market gets in trouble. The lack of even a couple days of weakness admittedly is surprising. Then, too, it's said good markets don't give you a good chance to get in. Financials of course have had stunning rallies, but Tech seems the real leadership. It seems likely too we'll get back around to commodities in a bigger way – steel, ag and oil. Those have lagged recently, but the charts show a lot of potential.

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STOCK AVERAGE VS. AVERAGE STOCK



Jul-01-08

Nov-26-08

Apr-29-09

