

EQUITIES PERSPECTIVE

June 06, 2008

DJIA: 12,604

So you got out of Bear Stearns . . . but not Lehman? Lehman (33) dived 15% intraday Tuesday, closing down almost 10%. The late day rally came as the company denied rumors that it had sought Fed funding, indicating instead that its capital was adequate. While there's no reason to think otherwise, that was pretty much what Bear said a week before they went under. To forestall any further such unfortunate events we now have the Primary Dealer Credit Facility, where a primary dealer can go for central bank financing. Sounds pretty fail-safe but, a primary dealer can get central bank financing only for its investment grade securities. In other words, it protects against liquidity runs, provided your securities aren't subprime, so to speak. All this after they told us that subprime was "contained." The real issue, of course, isn't whether these financial problems are contained, clearly they're not. It's whether these ongoing problems are discounted, already priced-in. By the look of Financial stocks recently, it would seem not.

The Financials (XLF) have broken the March uptrend and seem to be closing in on the March lows. Even worse is the Regional Bank Index which already is at a new closing low and barely budged in Thursday's rally. While its Lehman that's in the news, it could be that some of these regional banks have problems as yet not completely recognized. The problems affecting the Financials so far have all pretty much related to securitization. But there would seem plenty problems outside securitization, like good old fashion mortgages, construction loans and the like. In the event, it was the Financials that got the market's problems started. Its one thing for them not to be rallying but quite another if they're not even going to hold the March lows. That just seems another drag, and not an insignificant one, on a market that has looked a bit fatigued in any case.

For some time it pretty much has been the commodity related stocks and everything else, with the Financials far down the everything else category. The commodity stocks have cooled a bit but the Tech sector, and particularly the Semis, have come along to take up a leadership position of sorts. Tech, as it happens, is once again the largest S&P sector by market cap. As a consequence the NASDAQ has turned into the best of the major averages being "Tech-laden," as they like to say. Unlike the S&P which broke its uptrend and has struggled below its 200 day moving average, the NASDAQ Composite remains in its uptrend, modestly above the 200 day. The NASDAQ 100 Index, the 100 largest NASDAQ stocks, is better still. For all the better action in these averages, however, NASDAQ breadth is hovering around its lows, and that low already is below the March low. This kind of divergence has become almost the hallmark of the NASDAQ, and can go on as long as, well, Apple (188), Google (583) and the rest go on. Clearly, though, the strength is a bit misleading.

The Energy trade has been hard to kill, but not for want of trying. There have been a couple of reversal days along the way which so far have proven less lethal than they looked. Obviously the China driven commodity demand isn't going away anytime soon and, as they say, they're not making more of the stuff – OPEC output is less than it was three years ago. In the short run, however, everything is subject to setbacks. There are six commodities, for example, down 20% or more, with Lead and Zinc down 50% each. And then there's the sentiment side. At the recent peak of \$135, \$150 was thrown around like a sure thing. And, in just the last week or so, Oil was on the cover of both BUSINESS WEEK and the ECONOMIST, the proverbial bell ringing if we ever heard one. Even the biggest and best uptrends stall and/or have corrections. The crowded and extended Energy trade seems due.

The Commodity leadership is extended. The weak end of the market, the Financials, are weaker. True Tech stocks are acting much better, even by-gone names like Cisco (28) and Oracle (23). What seems most important is that when the market rallies, most stocks act well. Maybe not most Financial stocks, but as measured by market breadth, the average stock acts as well as the stock averages. And that's just not how big problems begin. While the averages have stalled recently, we're more focused on what the rallies look like. We're looking for the weak rally – up in the averages but poor breadth. Volume wasn't special, but Thursday's 200 point gain with almost 4-to-1 breadth wasn't exactly the weak rally we're referring to. Still, one day's action is rarely important. Nine of the NASDAQ's biggest up days of all time occurred during the bear market of 2000-2003. The market is struggling, but still acting well enough.

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STOCK AVERAGE VS. AVERAGE STOCK

