

## EQUITIES PERSPECTIVE

August 8, 2008

DJIA: 11,431

Doing nothing . . . did a lot. Too much praise can't be given to the Fed for Tuesday's rally. After all, they did nothing. At its June 25 meeting the Fed said downside risks to growth had "diminished somewhat." This time they said "downside risks to growth remain" and, the outlook for inflation is "uncertain." So, not only did the Fed do nothing, they pretty much said nothing, meaning the market rallied for the best of all reasons, it wanted to. Like many such days there was little to fault – 3-to-1 breadth and expanding volume. There are, however, many such days, many of them in this and other bear markets. Given the action Wednesday and Thursday, there's no real evidence of the kind of buying surge you might expect were this a new bull market. Still, Tuesday provided a nice follow-through to the July 15 low. Thursday's selloff likely started a little correction, but overall the market still seems soldout enough to hold the July lows.

Aside from Tuesday's outsized price gain, volume rose and that's important. Market volume is often underrated and can be an important clue, particularly when it comes to a tiring uptrend. When the market rallies it's important that breadth is good and volume expands. If volume expands but breadth is flat, that's a sign of churning. If breadth is good but volume fails to expand, that's a sign of lagging buying interest. It was that pattern that evolved from mid-April to the end of May, a prelude to the June weakness. Recently the pattern hasn't been bad. In the eleven rally days since the July low volume has expanded in six cases, and breadth has been good. It's important, too, that in weakness volume contracts, a sign the selling isn't intense. In the six down days since the July low volume contracted four, including the 283 point loss on 7/24, the 240 point loss on 7/28 and the 206 point loss on 7/31. However, volume did expand on Thursday's weakness, but that compared to Wednesday's unusually light volume. Stay tuned.

One sector's loss can be another sector's gain, in this case the weakness in Oil has done wonders for Airline shares. Then, too, the better action could reflect the decision by some to offset high fuel prices by charging for water. Could charging for the lavs be next? Of course, here's an industry that couldn't make money when Oil was \$20/barrel, so obviously Oil's recent weakness won't be much help. Still, we've all come to expect a knee-jerk rally in these shares on any Oil weakness. The difference this time is that from a short term perspective, the charts aren't half bad. And think about sentiment, is there any group more underloved? The poor Airlines don't even have their own ETF! It's stomach-turning just to think about buying an Airline, and clearly little rationale. However, the Airline business and the Airline stocks are two different things. Stocks are paper, when they get sold out, they rally – it's supply and demand.

For the Financials, the bad news just doesn't stop. Wednesday it was Freddie Mac (6) and Thursday it was AIG (24). Easy to say in retrospect, but was anybody really expecting good news out of these two? Be that as it may, neither exactly ignored the bad news, Freddie dropping almost 20% and AIG more than 15%, of course that following crushing declines. Still, all is not lost here. AIG and Freddie, like all of the Financials, have had a nice recovery recently and, in that sense, already were susceptible to some weakness regardless of the news. More importantly, the Financial ETF remains in its uptrend and above the late July low around 20. Holding that low seems important, as does eventually moving above the 7/23 peak around 23. The recovery in the Financials still seems the key to the overall market's recovery.

Far more disturbing than the weakness in AIG and Freddie was Thursday's selloff in Wal Mart (57). WMT is still a good overall chart but the false breakout, downside gap and pullback well into the base, are not what you want to see out of one of the market's leaders. Meanwhile, the correction in Oil and other commodity stock still seems in place, though some of the Oil stocks are actually a bit extended to the downside. The market still seems to have put in a low and most stocks have made lows – even AIG and Freddie are holding their July lows. But in one of those be careful what you wish for kind of things, it's still not so easy to make money. After all, now that they've already had a good rally, do you really trust the Financials? For the overall market, it's just about the numbers. When it's up breadth should be good and volume expand. When it's down volume should contract.

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# STOCK AVERAGE VS. AVERAGE STOCK

