

EQUITIES PERSPECTIVE

September 4, 2009
DJIA: 9,345

Wouldn't lie to you . . . but how about a Fib? In this case, a "Fib retracement," that is, the likelihood prices will retrace an original move and find support or resistance at a key Fibonacci level. Leonardo Fibonacci was an Italian mathematician, and the sequence he discovered is simply the sum of the two preceding numbers – 1, 1, 2, 3, 5, 8 and so on. What's important is the quotient of the adjacent numbers, rendering the proportion 1.618 or its inverse .618, the "golden mean." This ratio can be used to describe anything from atoms to the most advanced patterns in the universe. For example, if you divide female honeybees by male honeybees in any given hive you get 1.618, though we wouldn't try it at home. As for the stock market, the golden mean typically is translated into three percentages – 38.2, 50 and 61.8. As it happens, the rally from the March lows in both the Dow and S&P have pretty much completed a Fib retracement of the bear market – 41% versus 38.2%, and so far the market has stalled. And, if you draw a circle around the great pyramid at Giza, adjusting the decimal point the circumference is the exact number of days in a year – which has nothing to do with anything.

So is some 12th century mathematician to blame for the market's recent setback? Well, it's as good an excuse as any and whatever the reason, the market is stalled and has been, one can argue, since early August. Sure the averages rallied to new highs in late August but few stocks did so, and if they did they did so briefly. We could show you the charts of more than 50 strong stocks, IBM (116) for example, that have done nothing since late July. For we former altar boys the question now becomes, quo vadis – are these consolidation patterns preceding higher prices, or distribution patterns preceding weakness. Time will tell, to coin a phrase, but already there has been some disturbing weakness, the Banks being one example. A generally liked stock like Caterpillar (45) seems another. Then, too, Motorola (8) broke out, so go figure. New Lows are negligible suggesting no weakness at the weak end, and that's positive. But a lot of strong stocks now act tired and that's worrisome.

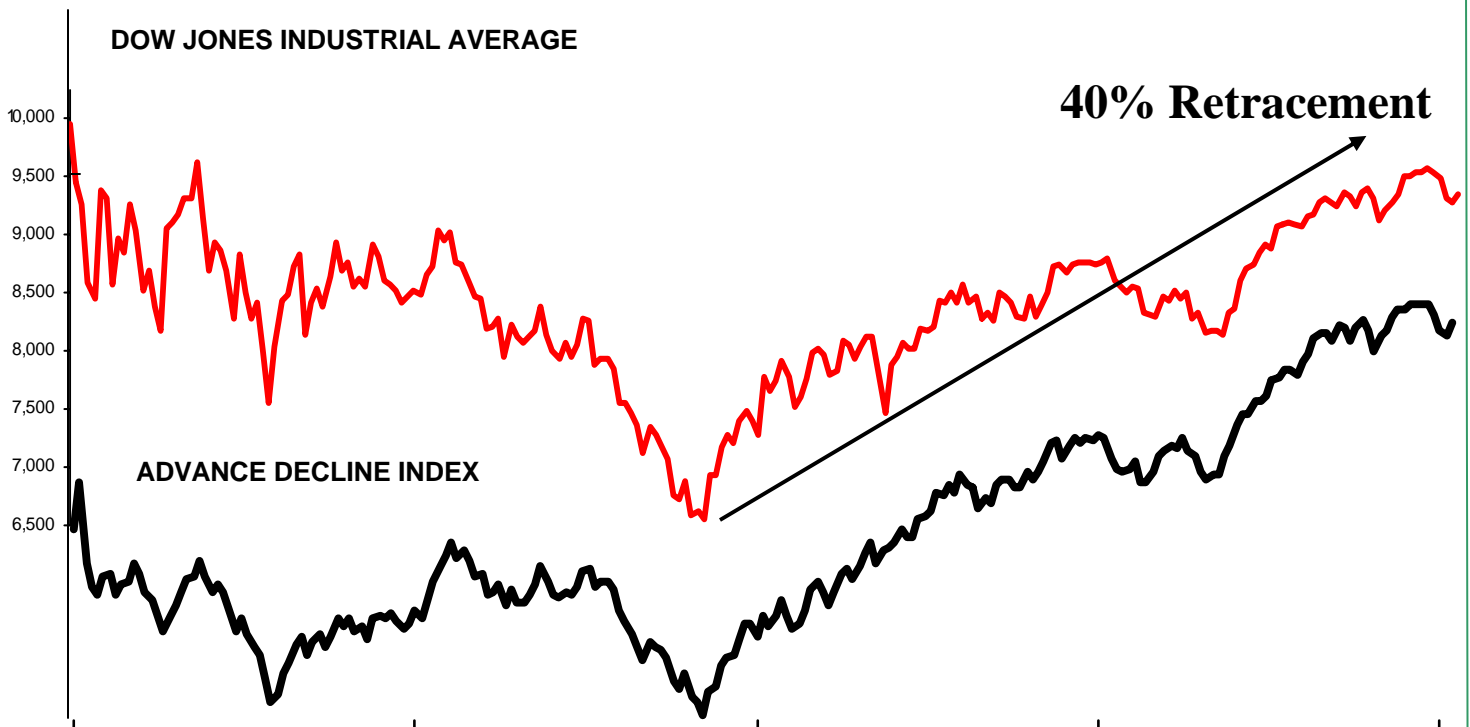
There's still plenty of reason for optimism, particularly in an overall sense. After all, most now agree the recession has ended, and history suggests most of the stock market's gains come between the market's low and the end of a recession. So, some slowdown in the market's recovery is expectable. And there were no important divergences at the recent high, as the Advance Decline Index and NYSE stocks above their 200 day moving average also reached new highs. That's a background that rarely precedes significant weakness. The short term pattern of course is different. Aside from the drop in the averages below their recent ranges, if Tuesday's 186 point selloff is just another blip like the 186 point selloff on 8/17, like then it should prove equally brief. Very short term the unemployment report could also provide some insight. Recently the market has ignored a lot of seemingly good economic news. If, in turn, the market can ignore a bad number, that would be a good sign. Perhaps most importantly, however, we wouldn't want to see the market ignore a good number.

No doubt on the back of China's 7% loss in August, commodity stocks like the Oils have struggled. A couple of weeks ago that seemed about to change but, apparently not. In a worldwide recovery, so they say, that seems a bit surprising, though in terms of commodities the world might come down to China. However, unencumbered by China, Gold had a bit of a breakout on Wednesday. You might argue the breakout differs little from that of early August though, at least in terms of the GLD ETF, this time volume was impressive. Also, the move was confirmed by the GDX ETF, Gold stocks versus the commodity, which also had volume. All that said the overall pattern, as per a weekly chart, is still a conundrum, but one with a whole lot of potential. Everyone always tries to explain rising Gold prices – a weak dollar, inflation worries, geopolitical threats, and so on. When it finally comes out of this 18 month consolidation, Gold will go a lot higher simply because it is, after all, in an overall uptrend.

While Flu season is yet to begin, it's little surprise that most Flu stocks already have attracted considerable interest. Some of these are pretty much the names you would expect – Baxter (56), Glaxo (38) and Novartis (40). Not surprisingly, the best performers have been more esoteric names like Novorax (6) or Vical (5). It could be, however, that the index is missing more mundane beneficiaries like the Drug Stores, rather than just the Drugs. And, as it happens, both CVS (36) and Walgreen (33) have acted quite well. Even WalMart (52) acts better. Typically a "play" on this or that is pretty much a waste of time. By the time you get around to it there's easily as much risk as reward – most rightly figure out there's not that much benefit to the companies, or it's a one shot benefit anyway. However, in what is a generally strong retail sector anyway, simple might work as a Flu play.

Frank D. Gretz

STOCK AVERAGE VS. AVERAGE STOCK



Oct-06-08

Mar-23-09

Sep-03-09

