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DJIA: 10,483

It Wasn't Contained . . . We Did Need Capital. So should read the tombstone of this financial crisis when it finally ends. In the meantime, they just keep falling, the latest being the aptly named WAM-U. Less aptly named was Golden West Financial, which for Wachovia (4) proved anything but golden. Before Monday's Citigroup (20) deal (and this morning's Wells Fargo (36) news), Wachovia rallied from a low of 8.5 on 9/17 to a high of 24 two days later. It plunked to 10 five days later and a low of .75 the next day. If as we believe the charts tell a story, the story here is one of severe psychosis. Wachovia's weakness among other things helped produce Monday's rout – 96% of stocks down and 97% of volume down. If you missed just the last five minutes, you missed a 5% drop in the S&P. Similar to the washout day on 9/17, Monday's weakness was followed by an impressive rally the next day. Making a low can be a process, a series of washout days and recoveries, and the recent action seems part of that process. All this will lead to a new beginning, as this last new beginning, financial leverage and the like, comes to an end.

We all understand that the stock market, like any market, is a function of supply and demand. It's important to remember, however, that when it comes to making a low in stock prices, supply is more important than demand. Stock prices don't stop going down because of buying, they stop going down when the sellers are out of the way. What gets the sellers out of the way is bad news, a reason to sell. No one is going to sell, let alone panic out of stocks, without a reason. In a perverse sense Monday's legislative debacle might have been positive in that it instigated selling rather than knee-jerk buying on "good news." Also, you can't underestimate the importance of price. These days dribbling down a few hundred points a day doesn't really put the fear of god in anyone. Seven hundred points, though, that's different. Seven hundred points makes the banner line of the NY Times and gets those TV trucks in front of the Exchange. Come to think of it, we can't remember seeing those trucks when we weren't close to a low.

Meanwhile, Lehman, Bear Stearns, WAMU and Wachovia (4) have bitten the dust, and that's sad. But if you don't own these stocks, there's no real pain. As we're fond of saying, it's not a bear market until they sell my stocks. For all the financial turmoil behind Monday's 780 point decline, many Bank stocks held reasonably well. By contrast it was Tech, especially big and sacred Tech like Apple (103) and Google (395); that got walloped. The "tech-laden" NASDAQ was down almost 10%, its biggest daily drop since 2000. For months now portfolio managers are brimming when they tell you they're out of Financial stocks. Well, if enough of them are in fact out, that might explain why most Financials put in a low in July – they got sold out. At the same time, if many are sitting there complacent in Googleland, that changed Monday. Bear markets get around to everything, the last typically being big-cap stocks that dominate the market averages. In the end there's no place to hide and, coupled with bad news (global slowdown), that's reason to sell/panic.

For the last year it has been the Financials, and everything else. That's still very much the case, but since July there has been a dramatic role reversal. We're still dealing with a financial disaster du jour – Wachovia, WAMU – but most Financials, especially most banks, made their lows in July. At the same time, the global slowdown has become a dominant factor in stock prices, the effects being felt from Tech to Fertilizer. One dramatic example of the shift is the action in Transports where the recent weakness has been dramatic, 9% on Thursday alone, this despite weakness in Oil that has been similarly dramatic. The good news is that this too will pass. Look no further than the Financials which, despite the ongoing crisis, have stopped going down. The real world doesn't have to get better, it just has to get discounted.

We're getting there. The VIX moved above 48 Monday, a level consistent with bear market bottoms. Other volatility measures, S&P volatility and intraday volatility are similar. Volatility occurs at tops and at bottoms – we'll stick our neck out, this isn't a top. Volatility is the result of a market in a bottoming process. The market is oversold on a medium term basis – only 13% of NYSE stocks are above their 200 day moving average, even more extreme than the 19% at the October 2002 low. For all markets, only 12 stocks made a daily New High Wednesday – there's little left standing. Bullishness among futures traders has dropped to 26% compared to a 10 year average of 48%, and Put/Call Ratios show a similar shift. A lot of money was made in commodity stocks in the first half of the year, since then a lot of money has been lost in commodity stocks, and a lot of that Thursday. Getting to what had been the year's winners is another part of getting to a good low. We're getting there but, as you've noticed, it's a process.

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