

EQUITIES PERSPECTIVE

November 16, 2007

DJIA: 13,110

Attention Wal-Mart shoppers . . . 42-43 is bedrock. On Tuesday Wal-Mart (46) said profits rose more than expected, and the stock rose sharply. In truth, the rally had nothing to do with fundamental stuff like earnings, the stock rallied because it never goes below 42-43. Other than "0," Wal-Mart and 42-43 have to rank as the world's longest running, functioning support area. And it's a good thing since, in what has been more or less a long running trading range, that support has endured its fair share of "tests." We can't quite accept that Wal-Mart was responsible for Tuesday's 320 point Dow advance, and we can't quite accept that at an important turning point volume would decline, even versus the bank holiday prior day. As always time will tell, to coin a phrase, and so far it hasn't told anything especially good. An up-opening Wednesday was followed by a fade and then weakness on Thursday. Good rallies usually don't look back, they don't give you a good chance to get in. By that standard Tuesday looks like a bounce, and not a good rally.

Given the nature of unresolved divergences, we've had in mind that the weakness would get around to everything, the commodity stocks, the agriculture stocks, and the sacred techs like Apple (164). And, indeed, for three days there, that seemed to be happening, the strong turned weak. In three days Apple tanked 32 points. Of course, Tuesday alone the stock recouped a full half of that loss, and more than 70% of the loss at Wednesday's peak, before reversing to close down on the day. Much like the market itself, the question now is whether that was it for the downside. When we've spoken of these divergences and the idea of "getting to everything," somehow what we had in mind was a little more than three days of weakness. Of course, things don't have to be black and white. It could be that these stocks just stall out here, and with them the market, as we drift rather than rally through the upcoming seasonally strong period. For sure, however, if these stocks start to take out Monday's lows, and several are close, 150 for Apple, 626 for Google (629) and 104 for Research In Motion (104), that wouldn't be good for them or the market.

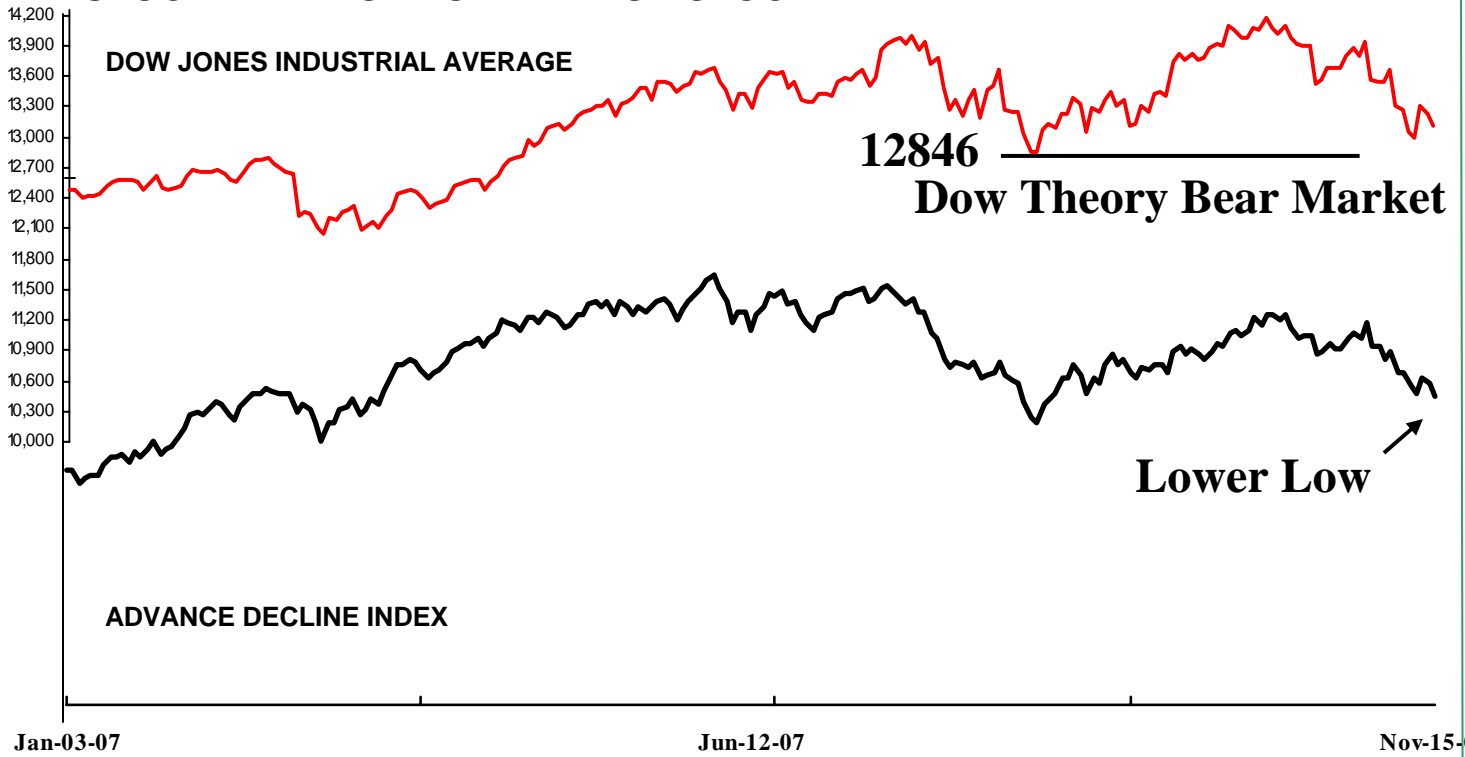
All that glitters isn't Gold, time was it was Copper as well. While the precious metals have hit multi-decade highs recently, Copper hasn't joined in. Copper is often seen as a key barometer of economic activity because of its industrial applications in everything from pipes to electronics. With inventories apparently piling up and prices under pressure, the specter of a global economic slowdown is lurking. These days, of course, everything comes back to China, and they haven't been buying. In the case of China, however, the issue seems less about slowdown and more about destocking. In the event, weakness in the commodity hasn't really hurt a stock like Southern Copper (117), at least not until very recently. But that's not the case when it comes to Steel. Whether it's about the global economy or China's self-sufficiency, most of the stocks do not act well. Too bad for the Steel stocks you may say, who cares? At its June peak U.S. Steel (93) was up 70% on the year. The Steels and other nonprecious metals have been very much a part of the commodity bull market, the commodity bull market very much a part of the equity bull market. Together with a few other areas, that too seems to be fading.

And then there's the Energy sector, another part of the market's leadership. Like Gold, Energy is at a disadvantage because of investor sentiment – bullishness is high, it's a crowded trade. But when it comes to Energy stocks, they may well be at another disadvantage, a divergence as it happens. We all know oil has been strong and all the talk of \$100 oil may well have killed that move. But what has been a bit surprising is that the stocks have not been as strong as the commodity. The U.S. Oil Fund (USO 72) reflects the price of the commodity and therefore only peaked a week or so ago. The XLE (72), which reflects the price of oil stocks, peaked in mid-October, diverged in oil's rally a week ago, and subsequently broke below the recent trading range. That likely spells more trouble for the stocks, especially given the high level of bullishness.

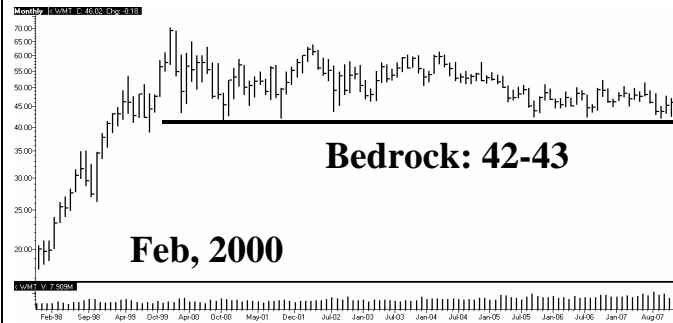
As good or bad as any one day may look, we've long observed that one day's action is never of itself important. Tuesday's rally was impressive but, particularly after Thursday's weakness, apparently not important. The major averages are still above Monday's lows, but both on the NASDAQ and NYSE breadth is not. Financial stocks are above the Monday lows, a change that could be important since that's where the problems all started. Fannie Mae (43), however, has broken sharply, potentially not a good sign for the rest. Wal-Mart has held its gain, but JC Penney (44) has broken sharply on the back of its first quarterly profit decline in 4 ½ years. They say never count out the consumer, but Department Stores are 196 out of 197 groups tracked by IBD. With the Transports already below the August lows, a similar move by the Industrials would signal a bear market under the rules of the Dow Theory, if you happen to believe in that sort of thing. There's still plenty of risk. Perhaps more importantly, with only 33% of NYSE stocks in uptrends, above their 200 day moving average, the odds of success on the long side aren't so wonderful.

Frank D. Gretz

STOCK AVERAGE VS. AVERAGE STOCK



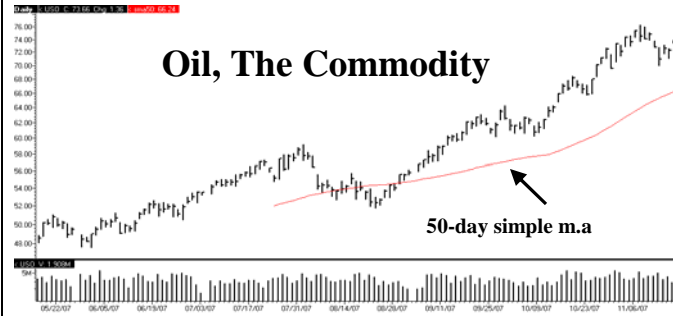
WAL-MART (WMT - 460) - MONTHLY



APPLE (AAPL - 164) - DAILY



OIL FUND (USO - 72) - DAILY



OIL (XLE - 71) - DAILY



US STEEL (X - 90) - DAILY



FINANCIAL INDEX (XLF - 31) - DAILY

