

Hope Now . . . Foreclose Later. “Hope Now” is Treasury Secretary Paulson’s effort to save some mortgage borrowers from facing the consequences of their bad decisions, at least for five years. The deal is meant to stem the likely flood of foreclosurers when “teaser” rates expire. In life hope is a wonderful thing but when it comes to markets, not so much so. In markets it’s better to sell than to hope. Rather than hope what most of these borrowers need is “Forgiveness Now” – even at the teaser rates many can’t afford the houses they live in, not to mention that many homes already are worth less than the amount owed. But more important in all this, it’s simply never good to mess with markets. Think of the disastrous history of price controls or the near ten year depression in Japan when regulators there encouraged banks to sit on the rot. And then there are those unintended consequences. If they’re going to change the rules on you, why would anyone in their right mind write another mortgage? So, more problems for the housing and the mortgage business. Rather than a five year plan why not think ahead, make it twenty-five.

On the happy news mortgage insurer MBIA (28) moved to a new low Wednesday. But, then too, Fannie Mae (39) cut its dividend and rallied sharply. On the whole, most Financial and Housing related shares at least are holding or moving higher. That because the problems are over, of course not. But the market is this discounting thing and at some point the bad news gets discounted. These stocks, already stretched to the downside, very likely have stopped going down on more of the same bad news, at least for now. As the Toll Bros. (21) report today makes all too clear, homebuilding is no longer the Homebuilders’ biggest problem, now it’s the real estate. But despite the company’s first quarterly loss in 21 years the stock rallied. At some point stocks stop going down on the same bad news and that’s a positive sign, at least while it lasts. And if these Financials are where all the market’s problems began, that’s not such a bad sign for the market. And it’s likely to last through this seasonally favorable period.

So just when was it that everyone started to believe the usually unreliable ADP employment report? Apparently it was Wednesday morning when stocks moved higher from the get-to. And if, indeed, the economy is humming along, doesn’t that bode poorly for the additional rate cuts that the market wants? In effect, the market rallied without the benefit of any good news, it rallied because it wants to go higher. We like that because it says something about this rally, rather than those driven by this or that “good news.” Much the same happened last week when stocks rallied. Then it was the likelihood of more rate cuts, and that’s news? Besides, the S&P (1485) is still below where it was on September 18 (S&P 1520) when the Fed cut for the first time in five years. Could be that things have changed. With most of the problems these days off balance sheet, we’d say that’s likely. Still, for now the market seems to have picked a direction, and any excuse will do.

As we’ve noted many times, there are plenty of bad Novembers but not so many bad Decembers. We see a counter-trend rally in this seasonally positive period, with possible weakness when the Fed does cut, followed by more problems down the road. The weak stocks got stretched to the downside and the strong stocks didn’t break. All the housing and subprime talk turned sentiment one-sided, though short term so rather than a major low. The VIX or Volatility Index, a measure of fear of sorts, reached levels comparable to August but as we know, August wasn’t a major low. And NYSE stocks above their 200 day moving average recently dropped to an oversold level of 29% and, in doing so, actually positively diverged from the 24% of August. Good enough for a rally, but these numbers can go lower and stay there before important turning points. There’s plenty of deterioration in the technical background – Financial stocks, for example, are basically through for a long, long time. And then there are the yet to be corrected Googles (700), and the like.

But there is some good news. Cigarette smoking, apparently, doesn’t cause cancer. That according to the Altria (78) chart, which will always be Philip Morris to us. The fact is, MO is but one of many “defensive stocks” to act better these days. It’s one thing for such stocks to act well during market weakness, but for that to continue marks a bit of a change. Indeed, if we showed you a chart of Apple (189) and Colgate (79) it’s not so easy to tell which is which, though Colgate has been the better of late. Add to that the better action in Merck (59), despite disappointing news Tuesday, and Johnson & Johnson (68) and there could be something to this defensive theme, something more than temporary. Then, too, the real theme may not be defense at all. With foreign investing all the rage, these multinationals let you foreign invest without ever leaving home.

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