

## EQUITIES PERSPECTIVE

December 18, 2009

DJIA: 10,308

An upside breakout . . . at least for five minutes. Monday saw the averages push to new highs. Okay, it was more of a nudge than push, and no follow-through. In a way it's hardly a surprise, there's little momentum anyway and this time of year it's hard to get it going. Still, the market was set up to rally – December option expiration weeks have been positive 24 of 27 years, and FOMC meeting days have been positive seven for seven when the prior day is down. In turn, Thursday wasn't pretty, particularly in terms of volume, though that was the Citigroup (3) fiasco. Good news after Thursday's close from Oracle (23) and RIMM (64) up the odds for some relief Friday, but another failure to respond would be a disappointment. If all else fails there's always the "Santa Claus rally," the strong tendency for prices to rally between Christmas and New Years. Then, too, "if Santa Claus should fail to call, bears will come to Broad and Wall."

Flexing its antitrust muscle, the Federal Trade Commission is suing Intel for what the agency calls a campaign to drive rivals from the market. Sounds like good old fashion competition, especially considering that computer prices have fallen over the last decade, even as computers have become more powerful. In the event, the news proved excuse enough to keep Intel in one of the more erratic ranges we've seen in a while. Still, much like the market, the stock is in a trading range within its overall uptrend – there's hope. And the group action is very much improved, a big change from just early November. Arguably one of the more economically sensitive groups, better action here is an obvious plus. Technically there seems good news as well. Measured by the Semiconductor Index (SOX), the stocks bottomed November a year ago and made a higher low in March when the indices bottomed. In other words, they've led in this particular cycle. Their recent breakout to new highs at least means there's no warning or divergence in terms of the overall market.

Exxon's (69) plans to buy XTO Energy (47) did wonders for Oil stocks, with the exception of XOM which has been pretty much crushed. Exxon carrying the weight that it does in the averages, ironically has contributed to the persistence of the trading range, at least in terms of the upside. That every Oil stock suddenly is a takeover play is as irrational as every Rail being a takeover play when Buffet bought Burlington (98). But the market does have its own way of doing things and the Exxon takeover seems a good enough excuse to rally a group that had been lagging. If not the market averages the deal did help market breadth – there are a lot of Oil stocks. Market breadth, which hadn't really been lagging day-to-day, finally reached its own new high. The Russell 2000 is yet to make a new high and, as usual, of course there's volume – this last week two of the three days volume expanded were down. That, more than anything, is why you still have to call the technical background fragile.

If the market remains stalled, it is at least so far holding. Indeed, since the low in March and the subsequent low in July, even weak stocks have managed to hold. With that in mind it could be that time of year when the weak have their moment, maybe even a couple of weeks in the sun. The so-called "January effect" is the period around this time of year when out of favor stocks catch a break as tax-loss selling winds down. From March to late September the small-cap S&P 600 led the indexes, but that changed in late September when the Dow took the lead. So far in December small-caps have again taken the lead, perhaps owing to the seasonal pattern. Unloved Techs typically get a boost around now but another beneficiary could be the Homebuilders which, in some cases, are down sharply from peaks in September and even November. We find it hard to believe that there isn't another wave of foreclosures out there, but for now things seem to have stabilized – November housing starts matched expectations. The overall pattern in the S&P Homebuilding Index is surprisingly not bad.

"This recovery is fragile. It's tentative, and it continues to reflect an economy that's unstable, unbalanced, uncoordinated and unsustainable." That sounds like something many of us might be thinking but, as it happens, it's a comment about China by that country's premiere. Meanwhile stock prices there, despite the growth, have quietly slipped more than 10%. We're not suggesting we will or need follow China, but if something is running amok even there, it's hard to be too complacent here. Dubai, the dollar unwind, Greece and the rest of them, there's always something. Maybe just good old fashion rising rates. The market can and usually will start down for reasons that were there all the time. Reasons that simply didn't matter as long as the market was going up. That's why it's important to stay on the right side of the trend, lest you find the market down 20% before the reason becomes apparent. There's nothing magical about S&P 1085, the lower end of the range. But against a still fragile background, for discipline sake we would pay attention to a break there.

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# STOCK AVERAGE VS. AVERAGE STOCK

