

EQUITIES PERSPECTIVE

December 19, 2008
DJIA: 8,605

A Yen . . . for the Euro. A yen for the Euro, a yen for the Yen, a yen for just about anything other than the dollar. And so it goes when the Federal Reserve will “employ all available tools,” and cut interest rates to the bone. The hope is that low Treasury yields will encourage investors to take on some risk, a bit ironic after what we’ve been through, but necessary to get things going again. Of course if a foreigner doesn’t trust buying U.S. corporates and if Treasury debt is near 0%, why hold dollars? And so the Fed’s Tuesday pronouncements sent the dollar plummeting, and currencies like the Euro and Yen soaring. But there was more to it than that. While we all pretty much realize that rates don’t matter, stocks had a good day; breadth was better than 5-to-1 and volume the best since the 5-to-1 rally a week earlier. The other winner after Tuesday’s news – Gold.

As it has been most of this year Gold is simply the inverse trade of the dollar. But Gold has some merits of its own. From the sentiment side, the correction that began back in March has turned traders very negative while, as it happens, the dollar rally that began July has turned sentiment positive to a similar extreme. So the dollar is an overly crowded buy trade, Gold an overly crowded short trade. And, in terms of mean reversion, the Gold ETF (GLD) was recently at an oversold extreme while likewise the Euro/Dollar ratio was at an oversold extreme. Perhaps most importantly, Gold is virtually the only commodity where the overall trend remains up. Compare Gold, for example, to Oil, where everyone is trying to catch a bottom and, of course, they’re yet to be accommodated. Meanwhile, Gold’s correction or consolidation seems relatively well contained. The last secular bull market in Gold from \$35 to over \$800 in 1980 included several corrections similar to this one, including one from \$200 to \$100 that lasted over a year.

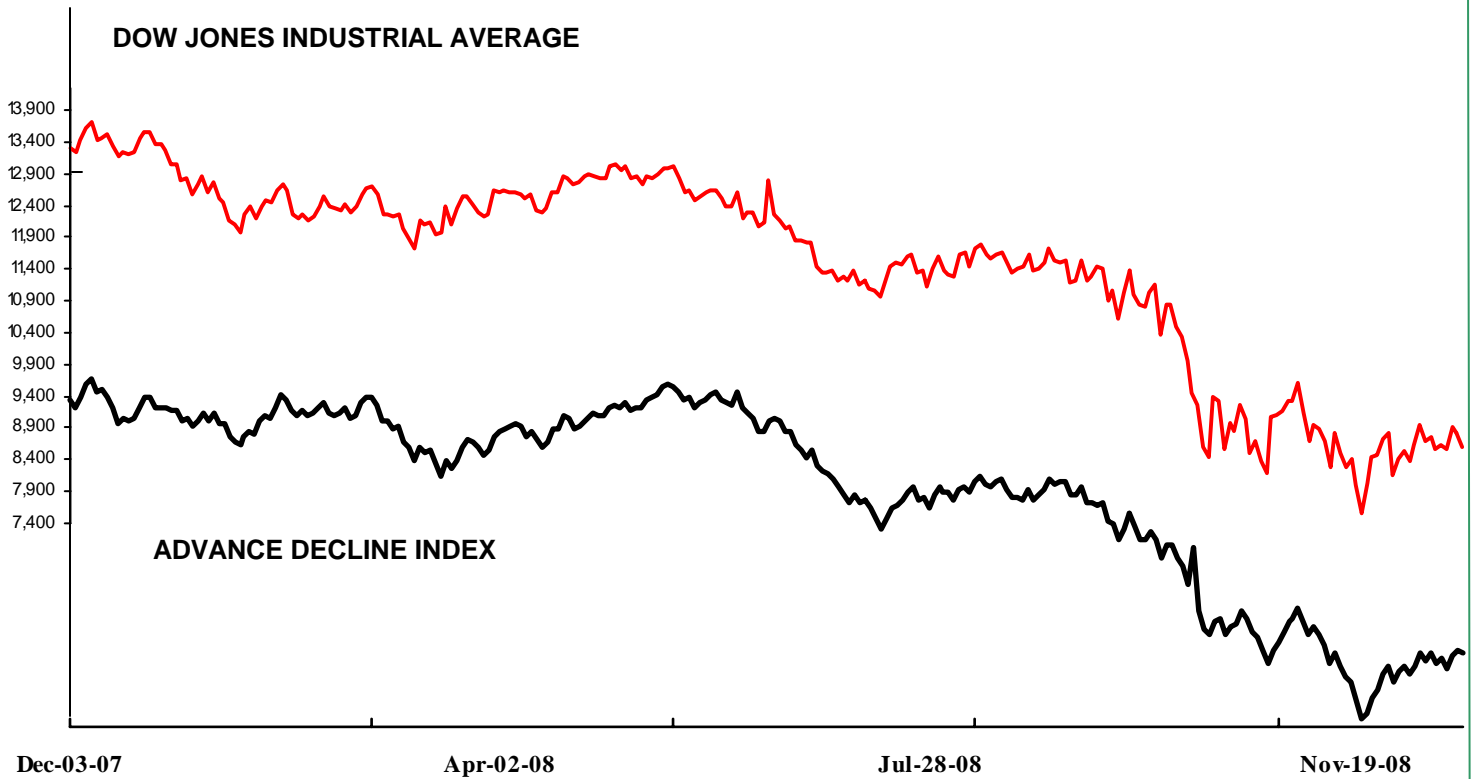
We love to say it’s not the news but how the market reacts to the news. We love it so much we could say it again. But there is a simplistic logic to it – a market that ignores bad news, a market sold out, a market where bad news is discounted, that market wants to go up. That’s the market telling a story. The news the last two Friday mornings, the employment number and the failure of the auto bailout, was enough to make you want to go home. After down openings both days, the market closed 300 points higher on the 8th and 65 points higher on the 12th. That’s not to say this Friday may not be different, but you have to admit the market has done a pretty good job of holding together. The market has a better feel to it. The VIX or Volatility Index has dropped below 50, a change we think is a big positive. The VIX in its way measures fear and fear is a characteristic of market lows. But after these lows, things should calm down and the fear dissipate to confirm the low. So there does seem something to the market’s better feel.

Of course Thursday’s 220 point decline on the GE (16) news may seem to call into question this whole idea of ignoring bad news. However, with less than 500 net declining issues and flat volume, Thursday wasn’t exactly what we call killing them. The prior day saw a 100 point decline but with a net of 500 advancing issues or, in other words, no decline at all. And then there was Tuesday’s rally, a 90% up day and any other way you slice it, a good day. So the momentum may not be great, but what there is remains to the upside. And weakness still seems relatively well contained – diminished volume and that sort of thing. The polls of futures traders still show them fighting the rally, another positive. Moving above the recent trading ranges, and the respective 50 day moving averages (around 9000 in the Dow), wouldn’t guarantee a big move, but it would be another sign that things are on track. And it’s the second half of December, a time they go up.

After a year like this one we didn’t need Bernie for Christmas. Come to think of it, what’s with these Bernie’s, Madoff, Ebbers, Cornfeld? A year of paying for greed and stupidity is one thing, but blatant fraud seems a little much. One of the observations, the inconsistencies, as it were, about Bernie was his amazing consistency. Thinking of that, we were reminded of course, of what used to be the pinnacle of consistency, General Electric (15). Here’s both a multinational and a conglomerate which, nonetheless, could tell you every January within pennies what yearend would bring. They told you, they did it. Of course, they did it thanks to GE Capital (“The Bank”) which is to say the consistency was managed. Now that device, GE Capital, has itself become a drag on the company. It’s one of those what goes around sort of things.

Frank D. Gretz

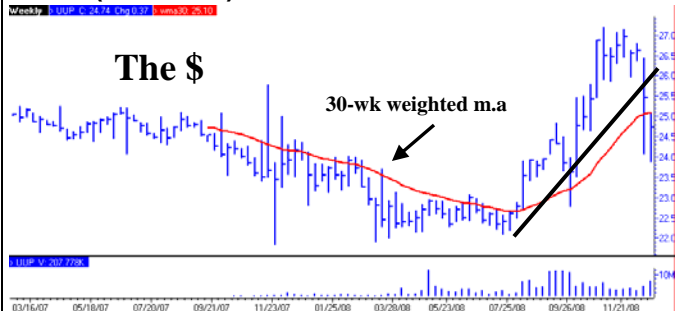
STOCK AVERAGE VS. AVERAGE STOCK



YEN (FXJ - \$112) - WEEKLY



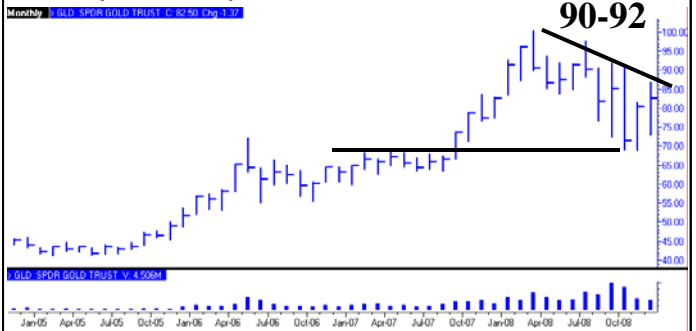
THE \$ (UUP - \$24) - WEEKLY



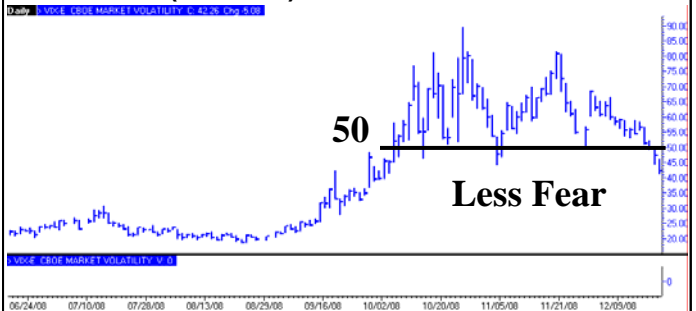
OIL (USO - \$33) - WEEKLY



GOLD (GLD - \$84) - MONTHLY



VOLATILITY (VIX - \$47) - DAILY



GENERAL ELECTRIC (GE - \$16) - DAILY

