

Friday December 19, 2008

Closing prices of December 18, 2008

Stocks continued their drop from overbought levels Thursday in what has so far been a relatively quiet quadruple witching options expiration week. So far the attempt to break through the 50-day moving average is unsuccessful, and the S&P 1500 is pinched between it and the 20-day moving average just below. The index is at an inflection point and needs to move above the 50-day soon to keep the rally intact. A move below the 20-day and the low of 12/12 will break the pattern of higher lows and make us reconsider the probabilities of testing the November lows. With our options indicator showing bullishness on the part of options buyers, a break of the 12/12 low could begin a sharp move down.

The S&P 1500 (200.43) was down 2.084% Thursday. Average price per share was down 1.74%. Volume was 100% of its 10-day average and 92% of its 30-day average. 31.92% of the S&P 1500 stocks were up on the day, with up volume at 21.25% and up points at 20.42%. Up Dollars was 7.01% of total dollars, and was 8% of its 10-day moving average while Down Dollars was 165% of its 10-day moving average. The index is down 0.98% month-to-date, down 24.64% quarter-to-date, down 39.51% year-to-date, and down 43.76% from the peak of 356.38 on 10/11/07. Average price per share is \$23.58, down 45.45% from the peak of \$43.23 on 6/4/2007.

The Put/Call Ratio was 0.900. The Kaufman Options Indicator was 1.09. The spread between the reported earnings yield and 10-year bond yield is 154% and 297% based on projected earnings. These are unheard of levels. The dividend yield on the S&P 500 recently moved higher than the 10-year bond yield for the first time since 1958.

Reported aggregate earnings for the S&P 1500 peaked in August 2007 at \$19.18 and are now at \$10.55, a drop of 44.99%. Estimated aggregate earnings peaked at \$21.95 in February 2008 and are now \$16.52, a drop of only 24.74%. Analysts have obviously been very late in lowering estimates. If investors had any confidence in current earnings estimates stocks would be much higher than they currently are.

498 companies in the S&P 500 have reported third quarter earnings. According to Bloomberg, 58.1% have had positive surprises, 9.7% have been in line, and 32.3% have been negative. The year-over-year change has been -18.3% on a share-weighted basis, +5.3% market cap-weighted and -2.7% non-weighted. Ex-financial stocks these numbers are 10.1%, 23.7%, and 15.8%, respectively.

Federal Funds futures are pricing in a probability of 82% that the Fed will leave rates unchanged, and a probability of 18.0% of cutting 25 basis points to 0.00% when they meet on January 28th. They are pricing in a probability of 67.9 that the Fed will leave rates unchanged on March 17th, and a probability 18.1 of raising 25 basis points to 0.50%.

The short-term trend is up, while the intermediate and long-term trends remain down. We reiterate that this continues to be an opportunistic trader's market, with adept traders able to take advantage long or short, but the long-term downtrend must still be respected. Investors should not hesitate to move out of laggard sectors and stocks and into leaders.

IMPORTANT DISCLOSURES

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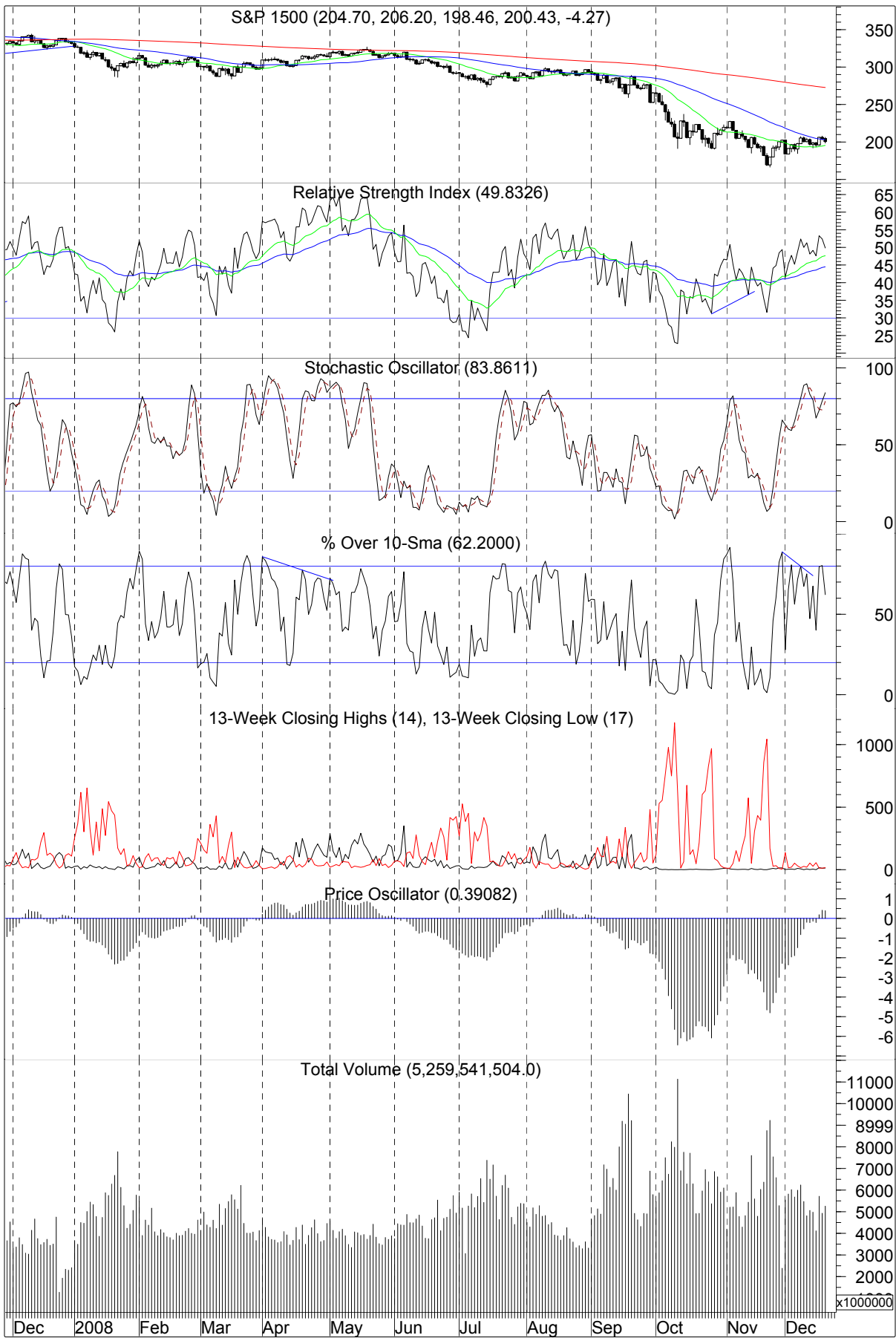
S&P 1500 Analysis - Wayne S. Kaufman, CMT

S&P 1500 (204.70, 206.20, 198.46, 200.43, -4.27)



The S&P 1500 has pulled back under the 50-sma (blue). A move under the 20-sma (green) and the low of 12/12 will be bearish and make us consider the chances of retesting the November lows, which we have said would not be broken in 2008.

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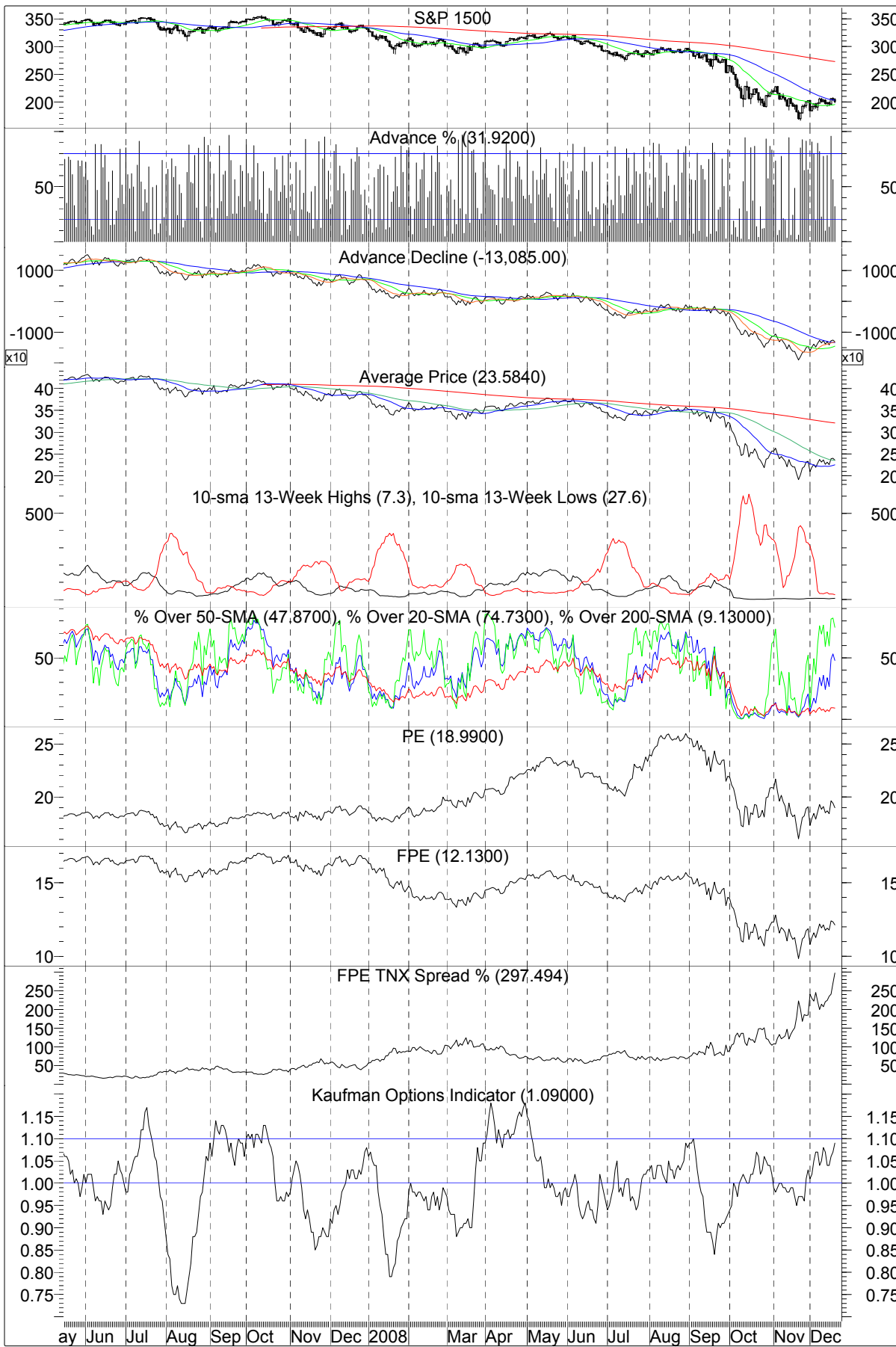


Our momentum indicators are still at high levels leaving stocks vulnerable to a deeper pull back.

Our price oscillator is over the neutral line for the first time since August. We need to see it move higher into positive territory in order for the up trend to have staying power.

Volume expanded Thursday.

S&P 1500 Analysis - Wayne S. Kaufman, CMT



31.92% of stocks traded higher Thursday.

P/E ratios are moving sideways.

Spreads between bond and earnings yields have reached record levels and don't seem to matter at all.

Our options indicator is moving higher as options buyers are becoming bullish. Too much optimism can leave stocks vulnerable to a drop.