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The Kaufman Report

Trade what you see, not what you think.

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Thursday February 26, 2009 **Closing prices of February 25, 2009**

Stocks finally rallied from extreme oversold levels Tuesday and recorded a 90% up day. Did Bernanke's optimistic comments spark the rally? If so we are surprised because this is the guy who for so long said the sub-prime problem would be contained and would not spread to the rest of the economy. He must have meant the solar system economy because it sure has been a problem here on Earth. Stocks tried to follow through Wednesday but were repelled at resistance levels. The S&P 500 and the Dow Jones Industrials last week had their lowest weekly closes since 1997 and need to rally to prevent their lowest monthly closes since that same year. A sharp relief rally is possible at any time. Unfortunately it is being anticipated by every market observer. The lack of any type of oversold bounce causes us to reiterate our frequent warning from last October that a market that doesn't respond to oversold conditions is dangerous. The short-term, intermediate-term, and the long-term trends remain down. This continues to be an opportunistic trader's market, with adept traders able to take advantage long or short.

We recently wondered if the government is running out of ammunition. Based on the market's responses to all the recent government plans maybe we should hope that is the case. Our elected officials should have to take their own version of the Hippocratic Oath, keeping in mind that when dealing with a sick patient their first responsibility is to do no harm. The stimulus package should include money directly back to the taxpayers but doesn't because the politicians want to increase their own power. The mortgage default solution is unfair and un-American. The argument that it helps the property values of those subsidizing the "at risk" borrowers is silly. That only matters if you need to cash out of your house soon. Even those who are moving will sell for less but also buy for less. This plan will create chaos and resentment. Stop manipulating free markets. That's how this mess was created. Government is not the solution, it is the problem.

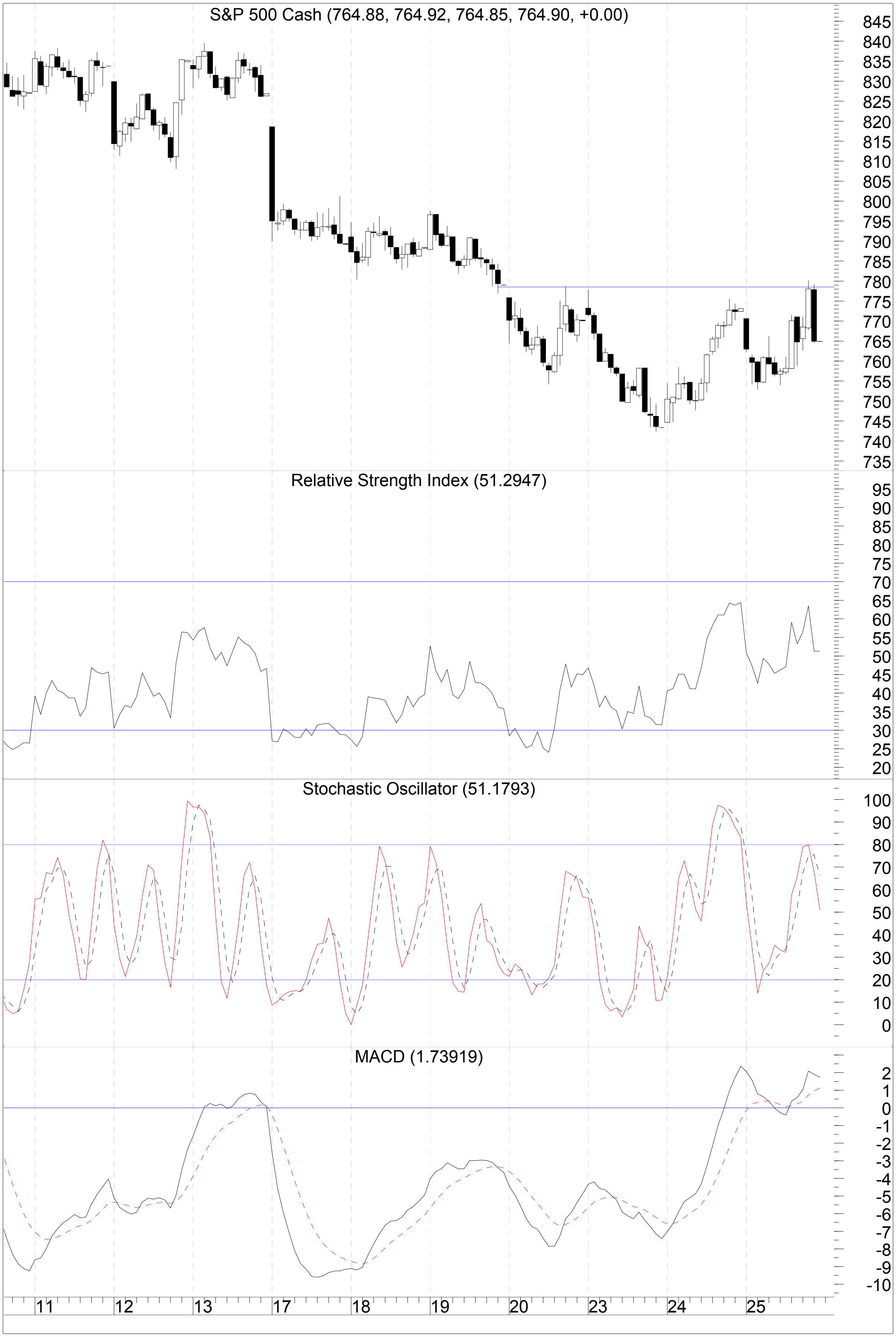
The S&P 1500 (173.26) was down 1.136% Wednesday. Average price per share was down 1.83%. Volume was 123% of its 10-day average and 128% of its 30-day average. 19.43% of the S&P 1500 stocks were up, with up volume at 43.01% and up points at 15.44%. Up Dollars was 7.24% of total dollars, and was 20% of its 10-day moving average. Down Dollars was 107% of its 10-day moving average. The index is down 7.47% in February, down 15.45% quarter-to-date and year-to-date, and down 51.38% from the peak of 356.38 on 10/11/07. Average price per share is $20.55, down 52.46% from the peak of $43.23 on 6/4/07.

Put/Call Ratio: 0.847. Kaufman Options Indicator: 1.02.
The spread between the reported earnings yield and 10-year bond yield is 59%, and 176% based on projected earnings.
Reported aggregate earnings for the S&P 1500 peaked in August 2007 at $19.18 and are now at $8.09, a drop of 57.82%. Estimated aggregate earnings peaked at $21.95 in February 2008 and are now $14.08, a drop of 35.85%. The spread between reported and projected earnings is near the widest the level in years. If investors believed the estimates stocks would be much higher.
456 of the S&P 500 have reported 4th quarter earnings. According to Bloomberg, 59.8% had positive surprises, 8.8% were line, and 31.4 % have been negative, a high number. The year-over-year change has been -34.7% on a share-weighted basis, -17.8% market cap-weighted and -23.1% non-weighted. Ex-financial stocks these numbers are -15.2%, -5.9%, and -8.8 %, respectively.
Federal Funds futures are pricing in a probability of 100% that the Fed will *leave rates unchanged*, and a probability of 0.0% of *raising 25 basis points to 0.50%* when they meet on March 18th. They are pricing in a probability of 94.0% that the Fed will *leave rates unchanged* on April 29th and a probability of 6.0% of *raising 25 basis points*.

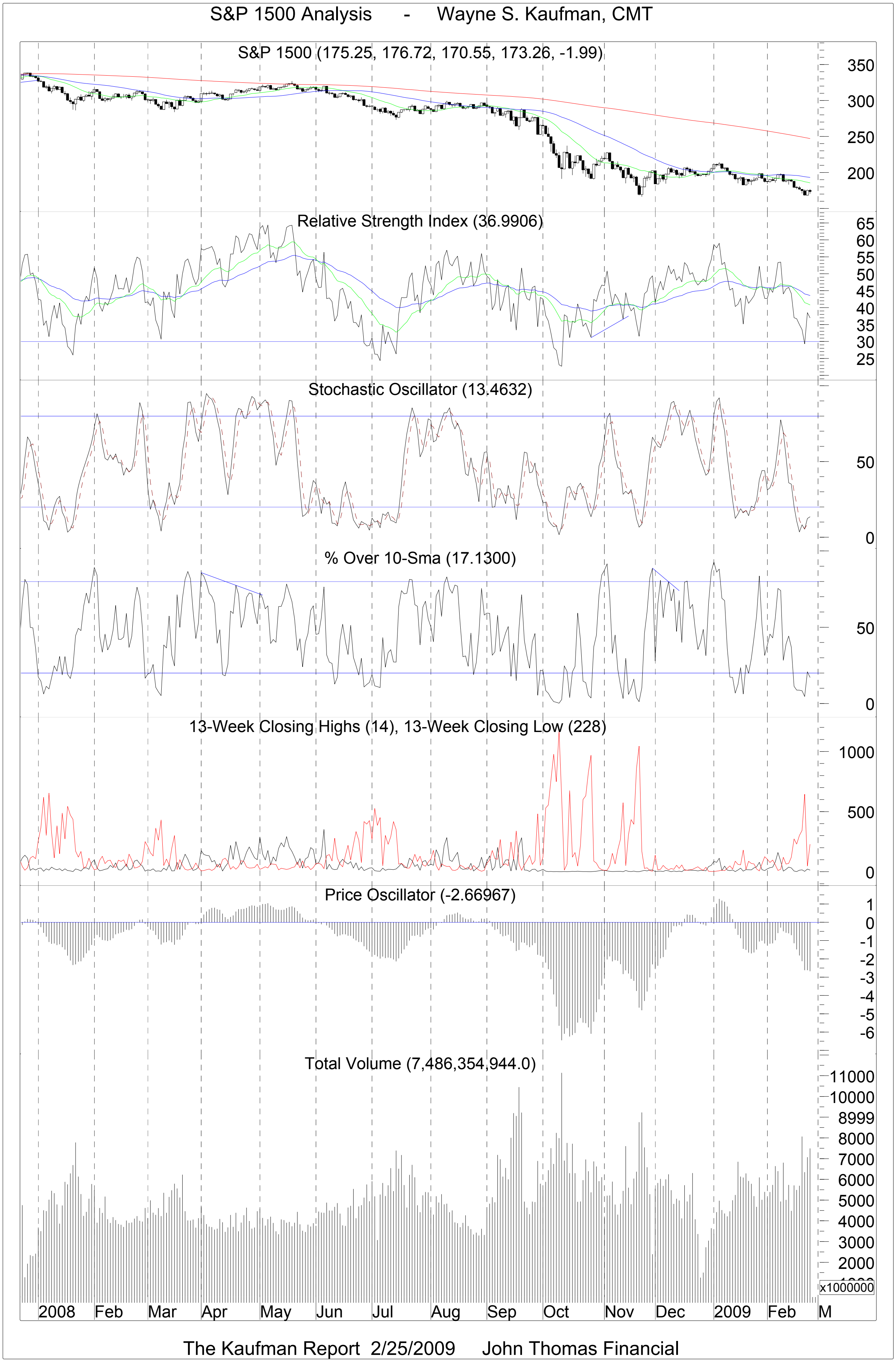
IMPORTANT DISCLOSURES

The S&P 500 has not been able to rally much from an extreme oversold condition. After rallying intra-day Wednesday it was repelled by resistance at the 780 area. A break above that should take it near 800.

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



The horizontal line on the intra-day chart shows the resistance at the 780 area. There is some resistance just under 800, but the most important resistance is at the bottom of the gap at 818.61 from 2/17. The intra-day pattern is an inverse head and shoulders that does project up near that gap.

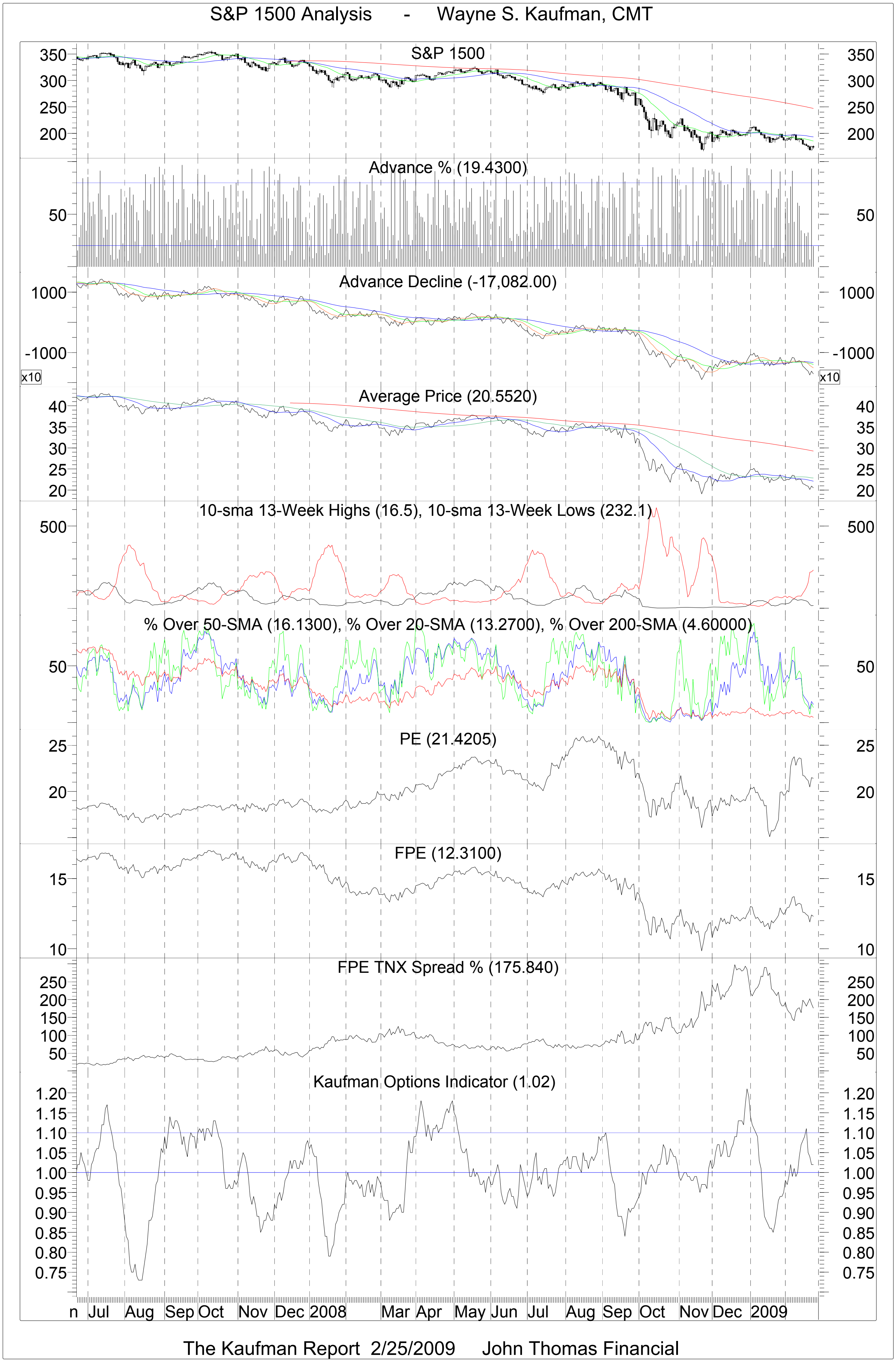


Our short-term momentum indicators are at low or oversold levels.

New lows far outpaced new highs Wednesday. Even on Tuesday's 90% up day lows were greater than highs.

Our price oscillator remains decidedly negative.

Volume expanded during Wednesday's down session.



19.43% of stocks traded higher Wednesday.

Average new lows continues to expand.

The P/E ratio is still high relative to the last five months.

Our options indicator has dropped to just above the neutral level. This is not an area where important bottoms are made, but small rallies can begin.