John Thomas Financial
14 Wall Street, 23rd Floor
New York, New York 10005
wskaufman@johnthomasbd.com
www.kaufmanreport.com

The Kaufman Report

Trade what you see, not what you think.

Wayne S. Kaufman, CMT
Chief Market Analyst
(800) 257-1537 Toll Free
(212) 299-7838 Direct

Monday March 1, 2010 **Closing prices of February 26, 2010**

Last Sunday we said we had become more bullish due to some positive technical developments, but that caution was advised in the short-term due to stocks having become overbought and some negative divergences which had appeared. Stocks sold off sharply early in the day Tuesday and Thursday, and in each case investors came in to buy the dips. At the end of the week the S&P 500 fought its way back from a test of support at the 1085 area on Thursday to challenging resistance at the 1106 – 1107 area Friday.

Bulls should be heartened by the way stocks held up in spite of negative news. Housing and Consumer Confidence numbers were negative, initial jobless claims were worse than expected, and the sovereign debt issue is unresolved. Not to mention continuing problems at AIG and Fannie Mae. All in all, it was a reasonable response to an overbought condition, which no longer exists.

Also supportive of the bullish case is the performance of the small and mid-cap indexes. Both are still up year-to-date, and while the larger-cap laden S&P 500 is fighting to get back above its 50-day moving average, the mid and small-cap indexes do not have that problem. It is usually helpful for equities when these indexes do well, as it shows investors are willing to assume more risk and liquidity is not a problem. Also of interest were last week's sector leaders, Financials +1.45%, and Consumer Discretionary, +0.82%. **Consumer Discretionary was the leading sector for February, +5.30%, and made a 52-week high on Friday!** Don't consumers know what terrible shape they are supposed to be in?

We are not saying the market is out of the woods yet. We are entering an important period. Major indexes are at an inflection point, just under resistance. Next week we will see the reaction to Greece's bond auction. The FOMC meets on March 16th. At the end of March the Fed ends its $1.25 trillion program of purchasing mortgage backed securities backed by Fannie Mae, Freddie Mac, and Ginnie Mae. At the end of April the homebuyer's tax credit is due to expire. Less widely discussed is an IMF report due in April on an international financial transaction tax. In addition, we now have to worry about the Bipartisan National Commission on Fiscal Responsibility and Reform, which may simply be a smokescreen with the purpose of helping the government raise taxes. The end of March is also the end of the first quarter, and the last two weeks of the month will contain earnings pre-announcements. **Not to be forgotten is the history the month of March has for being a time of major turning points for equities.**

In summary, we are somewhat bullish short-term due to a lack of sellers, negative sentiment, and technical signals which have preceded rallies recently. Unfortunately we are in a period where economic and political visibility is limited. **Therefore, we continue to classify this as a bifurcated trader's market until proven otherwise**.

Based on the S&P 500 the short-term trend is up, intermediate-term is down, and the long-term trend is up. This is a short-term trader's market, with adept traders able to trade long or short depending on conditions. Investors need to be aware of sector rotation and should not hesitate to move out of lagging stocks and sectors and into leaders. Should recent positive technical signals be reversed, we would become defensive.

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S&P 1500 Data: (Data available daily at John Thomas Financial)

P/E: 19.23 Percent over 10-sma: 58.27%. Percent over 50-sma: 55.00%
13-Week Closing Highs: 96. 13-Week Closing Lows: 39. 52-week closing highs: 65
Kaufman Options Indicator: 0.97 Put/Call Ratio: 0.875 New High Reversals: 25. New Low Reversals: 3
Volume: -6% versus yesterday. 102% of the 10-day average. 90% of the 30-day average.
Up Stocks: 45.04%. Up Volume: 58.37%. Up Points: 51.91%. Up Dollars: 58.40%, 58% of 10-sma. Dn Dollars 85% of 10-sma.

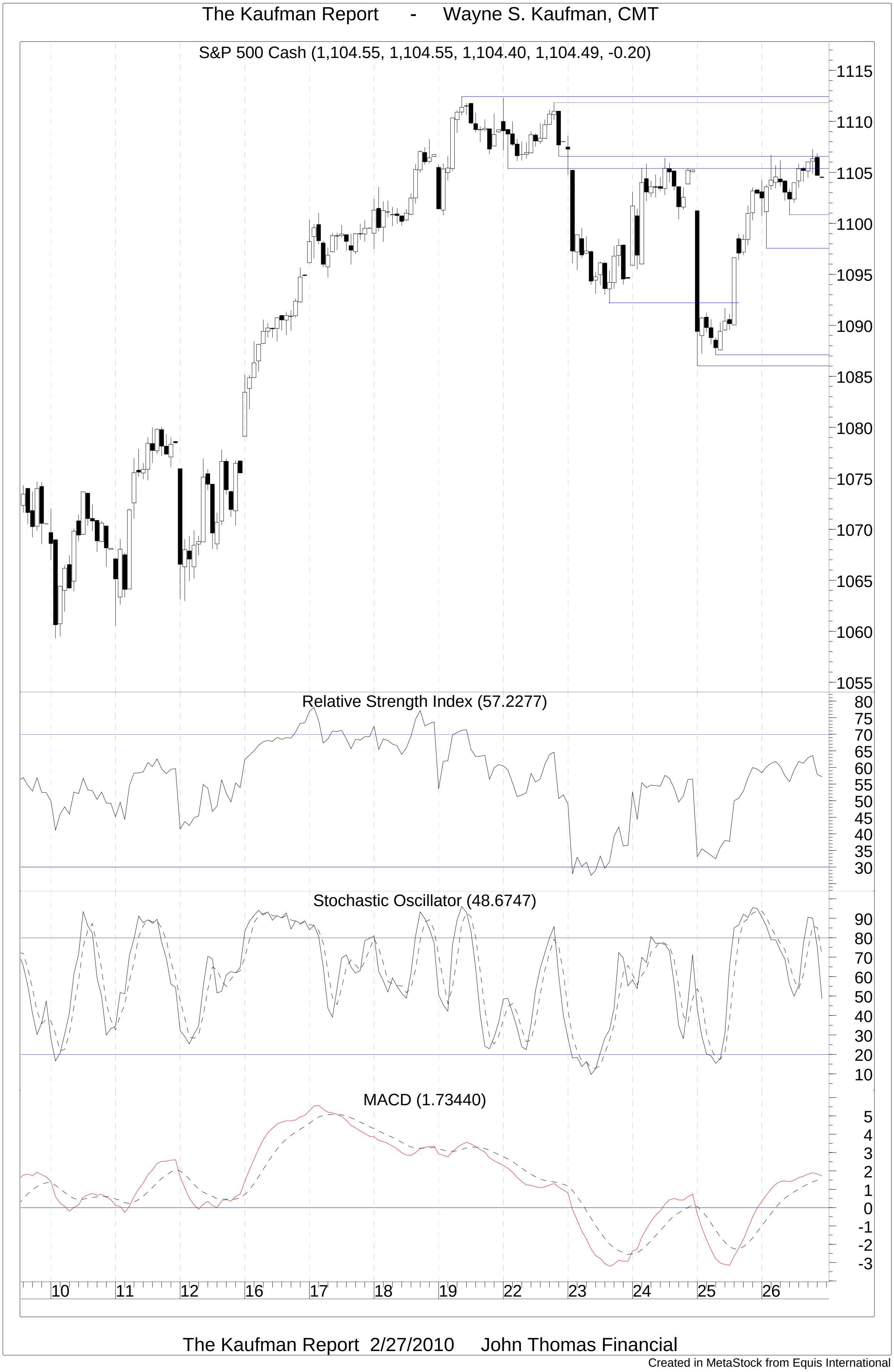
Earnings: 482 of the S&P 500 have reported so far this earnings season. 72.6% have had positive surprises, 10.4% have been in line, and 17.0% have had negative surprises.

Federal Funds Futures project a 64.0% probability of no change to the current 0.25 % target rate and a 36.0% probability of a cut to 0.00% when the FOMC meets on 3/16. For the meeting of 4/28 the probabilities are 62.3% for no change, 33.9% for 0.00%, and 3.8% for 0.50%.

	Daily	WTD	MTD	QTD	YTD
Bank of New York Mellon ADR	0.68%	-0.85%	0.53%	-6.04%	-6.04%
Nasdaq 100	0.32%	-0.25%	4.46%	-2.24%	-2.24%
NYSE Composite	0.31%	-0.68%	2.20%	-2.09%	-2.09%
Nasdaq Composite	0.18%	-0.25%	4.23%	-1.36%	-1.36%
S&P 500	0.14%	-0.42%	2.85%	-0.95%	-0.95%
S&P 1500	0.12%	-0.40%	3.08%	-0.69%	-0.69%
S&P Midcap 400	0.06%	-0.24%	5.06%	1.61%	1.61%
Dow Jones Industrials	0.04%	-0.74%	2.56%	-0.99%	-0.99%
S&P Smallcap 600	-0.28%	-0.26%	4.22%	0.62%	0.62%

	Daily	WTD	MTD	QTD	YTD
Financials	0.71%	1.45%	3.41%	1.88%	1.88%
Industrials	0.38%	-0.19%	4.57%	3.31%	3.31%
Consumer Discretionary	0.24%	0.82%	5.30%	2.19%	2.19%
Telecom Services	0.17%	-1.10%	-1.29%	-10.50%	-10.50%
Energy	0.16%	-2.07%	1.87%	-2.72%	-2.72%
Health Care	0.14%	-0.35%	0.01%	0.43%	0.43%
Information Technology	0.07%	-0.78%	4.03%	-4.77%	-4.77%
Materials	0.04%	-2.43%	4.22%	-4.81%	-4.81%
Consumer Staples	-0.53%	-0.69%	2.70%	1.42%	1.42%
Utilities	-0.74%	-2.41%	-1.86%	-6.87%	-6.87%

	Daily	WTD	MTD	QTD	YTD
Diversified Financials	1.15%	1.91%	5.48%	0.20%	0.20%
Consumer Durables & Apparel	0.81%	0.86%	6.83%	4.81%	4.81%
Media	0.50%	-0.24%	4.80%	-1.15%	-1.15%
Capital Goods	0.49%	-0.66%	4.40%	4.21%	4.21%
Banks	0.40%	1.31%	-2.01%	6.70%	6.70%
Health Care Equip & Services	0.36%	1.03%	1.55%	1.65%	1.65%
Insurance	0.29%	1.01%	3.58%	3.86%	3.86%
Technology Hardware & Equipment	0.24%	-0.70%	5.21%	-3.77%	-3.77%
Telecom Services	0.17%	-1.10%	-1.29%	-10.50%	-10.50%
Energy	0.16%	-2.07%	1.87%	-2.72%	-2.72%
Transportation	0.13%	1.80%	6.16%	2.25%	2.25%
Retailing	0.06%	1.93%	6.06%	2.55%	2.55%
Materials	0.04%	-2.43%	4.22%	-4.81%	-4.81%
Pharmaceuticals, Biotech & Life Sciences	0.03%	-1.04%	-0.76%	-0.18%	-0.18%
Software & Services	0.02%	-0.66%	1.90%	-6.09%	-6.09%
Automobiles & Components	0.01%	3.35%	8.76%	13.08%	13.08%
Real Estate	-0.01%	0.32%	5.53%	-1.25%	-1.25%
Consumer Services	-0.07%	-0.70%	2.35%	1.72%	1.72%
Commercial & Professional Services	-0.24%	-0.18%	2.31%	-2.85%	-2.85%
Household & Personal Products	-0.36%	0.23%	3.14%	3.07%	3.07%
Semiconductors & Equipment	-0.44%	-1.46%	6.53%	-4.19%	-4.19%
Food, Beverage & Tobacco	-0.59%	-1.65%	2.47%	-0.02%	-0.02%
Food & Staples Retailing	-0.60%	0.46%	2.75%	2.84%	2.84%
Utilities	-0.74%	-2.41%	-1.86%	-6.87%	-6.87%



The 30-minute chart of the S&P 500 shows it gapping down on Thursday but fighting back to a resistance zone at the 1106 - 1107 area by the close Friday.

Momentum indicators are neutral at best.

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The weekly chart of the S&P 500 shows it followed through to the upside after printing a bullish engulfing candle three weeks ago, and now has stayed above the 20-sma for a second week. It did print a hanging man candle, which can be bearish, but which also requires confirmation by the next candle to be bearish.

We pointed out last week that the last two time there was a bullish engulfing candle accompanied by a positive stochastic crossover from a low level (March and July) stocks rallied nicely. This potential is still intact.

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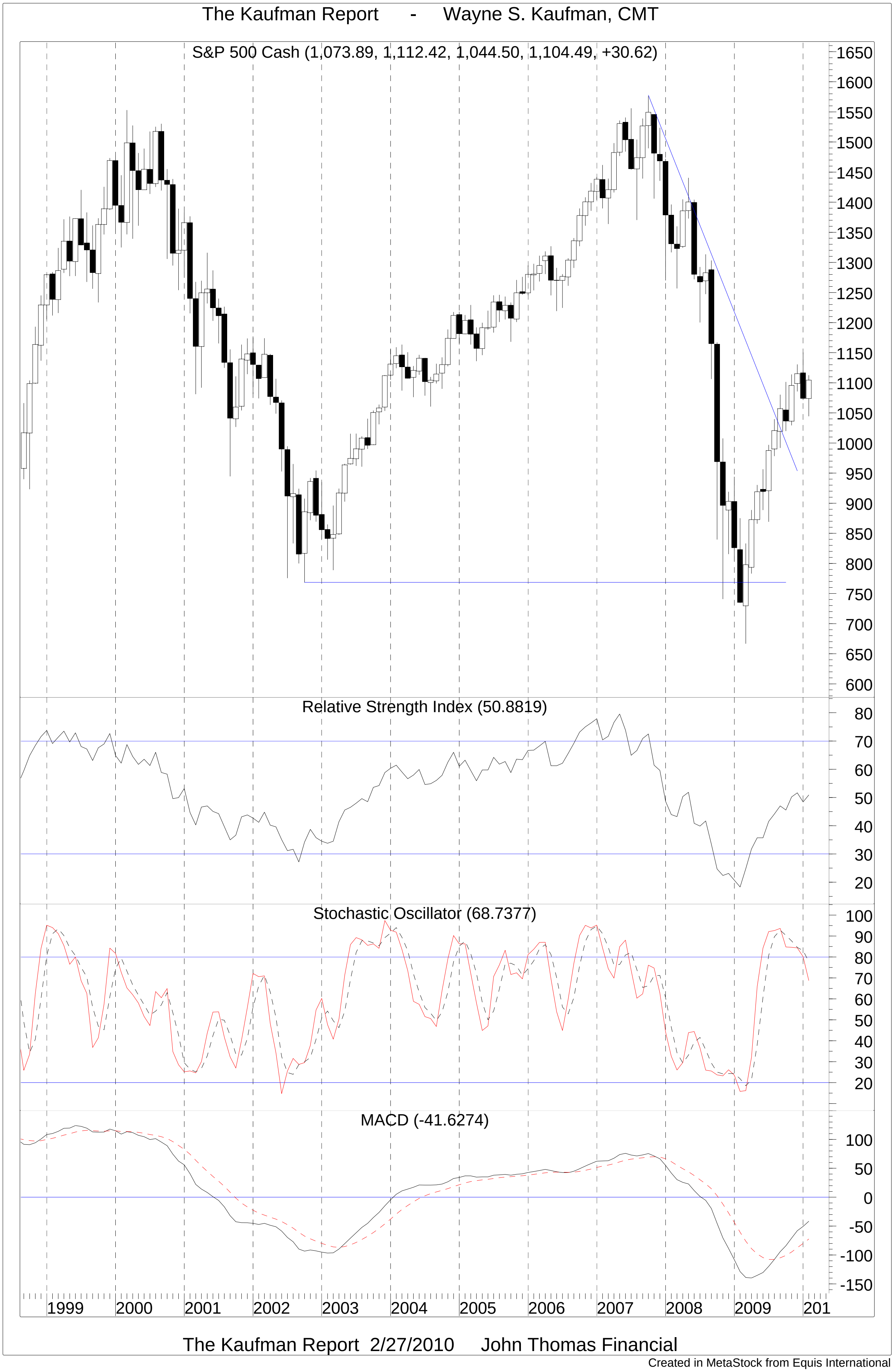
The S&P 500 ran into resistance in the form of the 50-sma on 2/19. It pulled back to support at the 20-sma on 2/25, printing a hammer candle before bouncing back up to the 50-sma. Hammers are bottoming candle. There is a resistance zone up to 1,114.81. After that there is another zone at 1129 - 1131.

Daily momentum indicators look positive.



The monthly chart of the S&P 500 shows stocks making a lower high and a lower low in February after January's bearish engulfing candle.

There is a negative crossover by the stochastic from the overbought zone but the RSI and MACD have room to move higher.

The daily chart of the Nasdaq 100 shows it couldn't get through resistance in the form of the 50-sma (blue) but found support at the 20-sma (green). In the last three sessions the close was higher than the open.

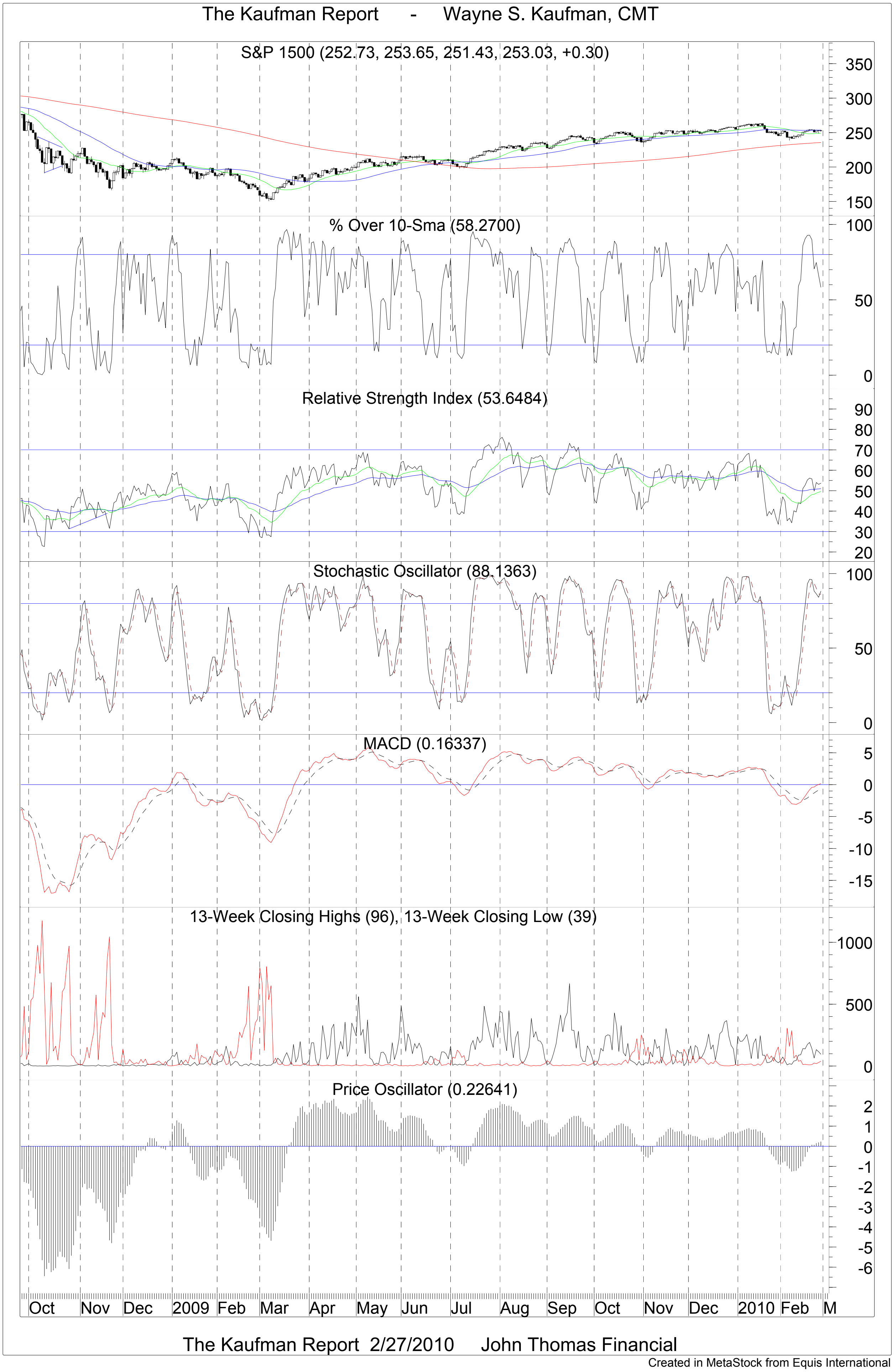
Daily momentum indicators look poised to move higher.

The weekly chart of the Nasdaq 100 printed a hanging man candle last week. These are bearish candles but require confirmation from the next candle.

The stochastic has a positive crossover from a low level.

The monthly chart of the Nasdaq 100 printed a bearish engulfing candle in January. Even though February was up 4.46% for the month, the chart still has a lower low and a lower high.

The stochastic is crossing over negatively from a high level. This doesn't have to end a rally, but it does argue that big gains are unlikely in the short-term, and some consolidation is necessary.



After hitting 92.87% on 2/19, the percent over 10-sma is now 58.27%. Getting over 90% is usually a sign of strength.

Positive MACD crossovers from low levels have been good for equities.

Our price oscillator, a good indicator of trends, has moved back into positive territory.

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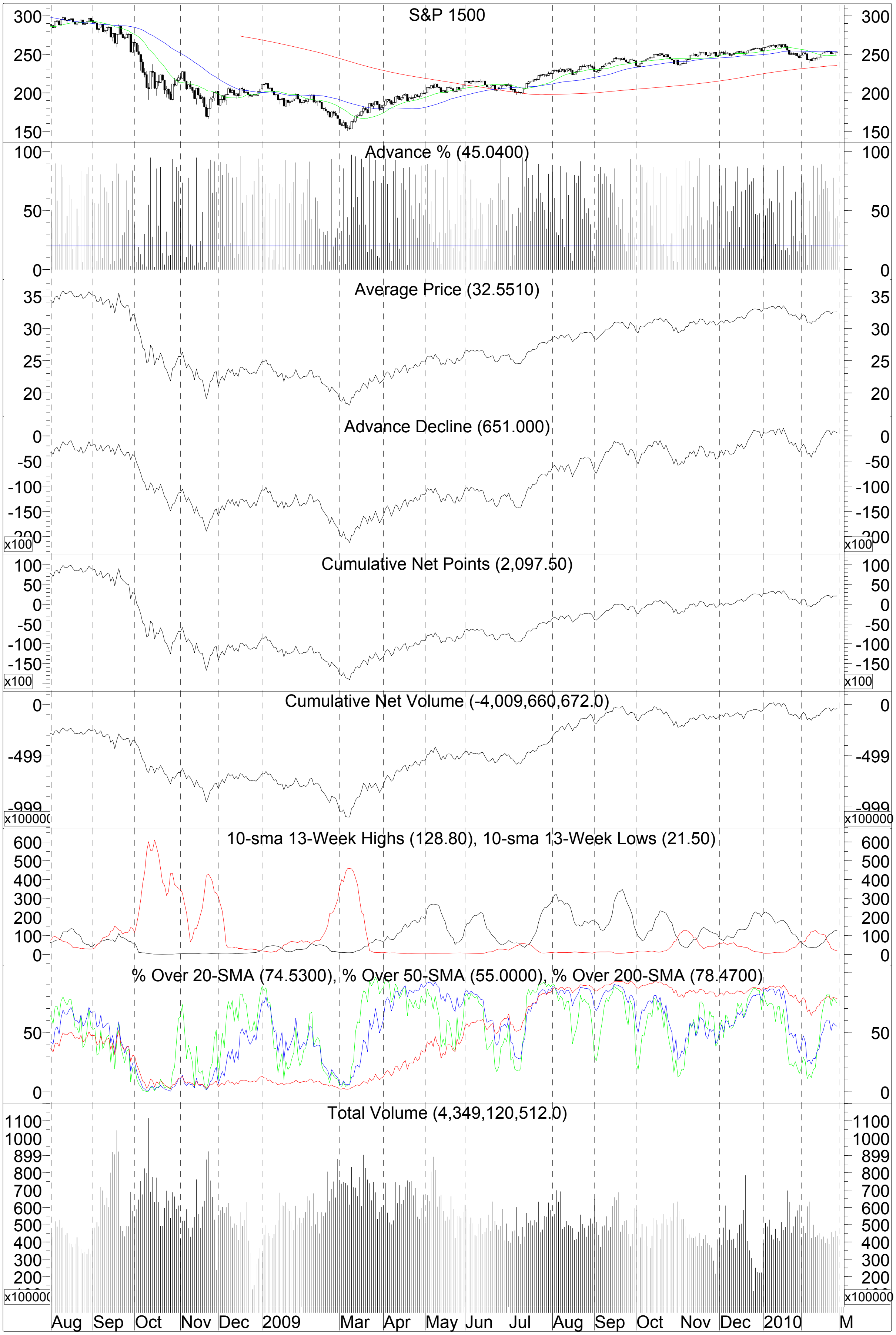

45.04% of stocks traded higher Friday.

The AD line is only 896 net advances from msking a new high, which would be very bullish.

13-week closing highs continue to be more than lows.

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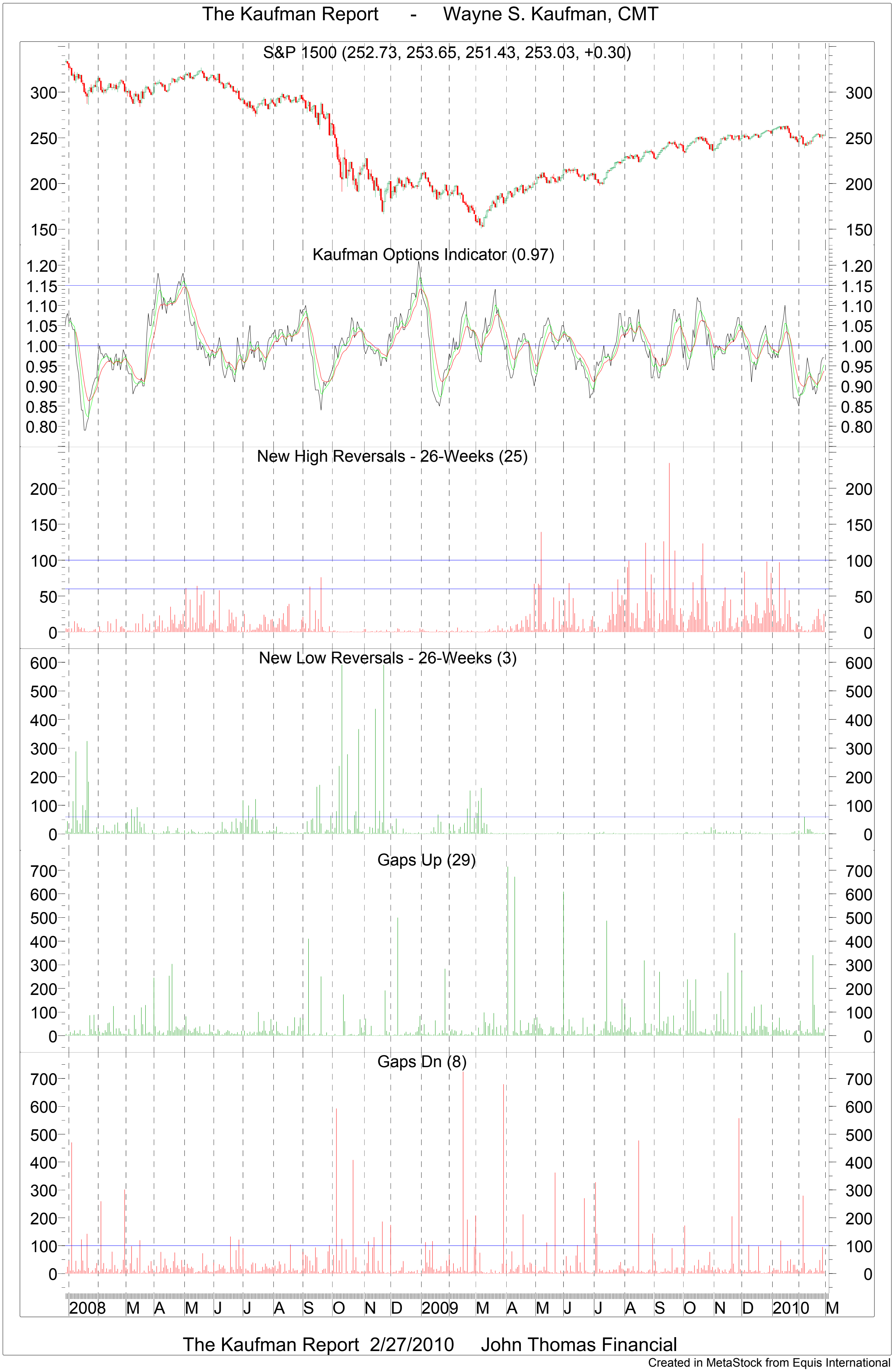
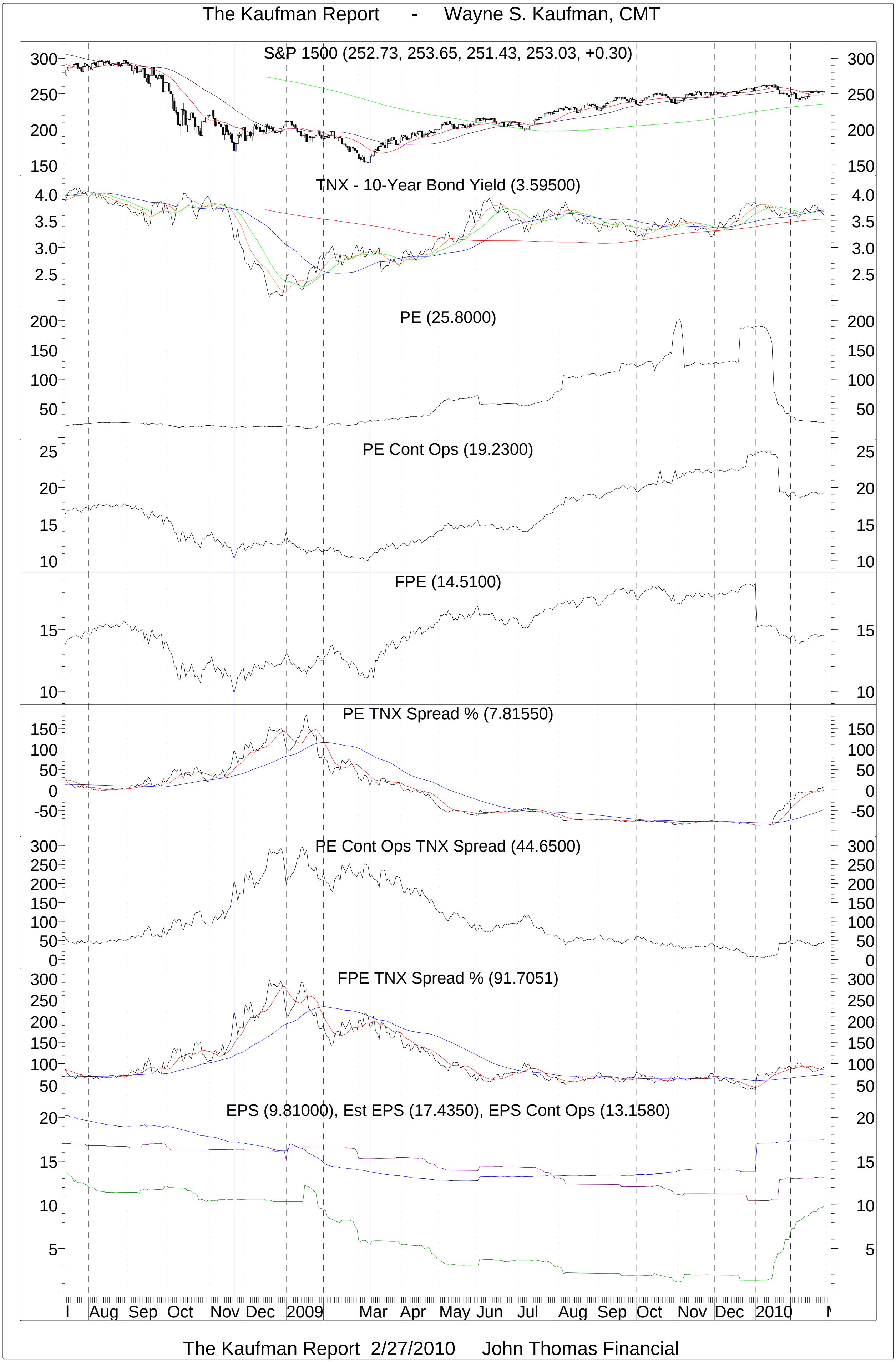


Our proprietary options indicator has moved higher after hitting very low levels, but is still showing pessimism.

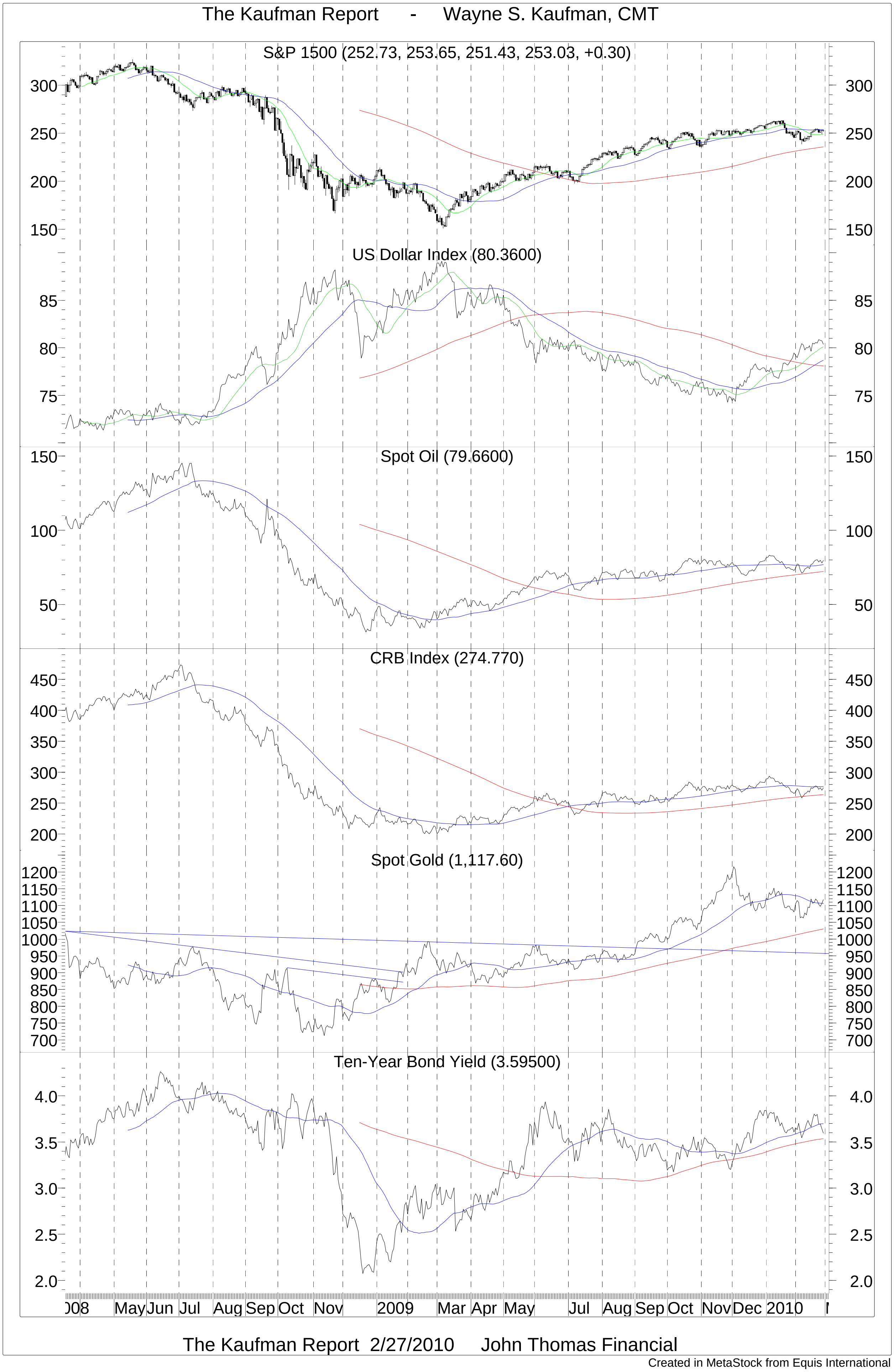
Our statistics of supply (red)versus demand (green) show positive crossovers for all time periods. In other words, demand remains greater than supply. We have commented in recent weeks that sellers are reticent, and a glance at the red lines shows that remains the case. In particular, notice the Up Points versus Down Points section, which gives an unweighted by market cap and unbiased by extreme share volume trading view of supply and demand. Unless sellers become more motivated than they currently are, there aren't currently the signs of longer-term liquidation taking place.



After taking a steep plunge due to earnings reports, P/E ratios are leveling off.

Spreads between stock and bond yields have widened and are at levels which are supportive to equities.

The trend of all our earnings metrics is now higher. Forecast earnings bottomed first, back in May.



Back in December we said the U.S. Dollar Index was trying to bottom, and if it did the 77 - 78 level would be important. As the Dollar rallied it did consolidate in that area. We said a breakout would target 80 - 82. It did breakout in January and spent much of February consolidating in the 80 - 81 zone. There is a negative divergence on the daily chart, so consolidation may be necessary. A break over 81.50 will target the 84.5 - 86.5 zone.

Crude oil remains in an uptrend and has been strong in spite of recend Dollar strength, which shows real demand for oil. A break above the resistance zone at 83.5 - 86.5 will target high $90s or $100 oil.

Gold has recovered its 50-sma and seems poised to move higher. There is resistance at 1131. It is not overbought on daily or weekly charts, so a move above resistance could bring short-covering and spark a further rally. Our one concern is overbullishness by call buyers.

The 10-year bond yield is just above the 200-sma (red). The recent drop has helped equity valuations. A breakout over the 4.10 level would point to higher rates and would probably be damaging to stocks unless accompanied by an improving economy.