John Thomas Financial
14 Wall Street, 5th 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

Tuesday May 27, 2008 **Closing prices of May 23, 2008**

Last Sunday we pointed out potential negatives in the market, and said that the one that concerned us the most was the narrowing of the spread between the 10-year bond yield and the earnings yield of the S&P 1500 based on the current P/E. We pointed out that it had reached the same level it was at on July 23, 2007, the beginning of a sharp correction. Stocks moved higher early last Monday, then began a drop which ended with the S&P 1500 being down 3.37% for the week.

Last Wednesday the bearish rising wedge pattern we have been highlighting was finally resolved with a downside break, which accelerated that afternoon and caused the index to close below its 20-day moving average for the first time since April 14th. We said at the time the move down could find a stopping point at the 310 – 311 area (1370 area S&P 500) which is the 38.2% Fibonacci retracement of the rally from the March low to the May 19th high, and will be in the area of the 50-day moving average. The 50% retracement is the 306 area (1348 area S&P 500).

Volume Wednesday was above average, while it decreased Thursday and was even lower during Friday's broad sell off. Wednesday's large volume may have been due to so many market watchers being aware of the support line of the bearish rising wedge being broken and trading accordingly.

Spreads between bond and earnings yields have widened again to the best levels since May 9th. On that date the S&P 1500 closed at 314.75. This highlights the key issue facing equities. After first quarter earnings reports gave investors hope for a change in the down trend in earnings, will oil prices and inflation be the factors which keep current and forecast earnings on their inexorable march lower?

In the short-term stocks are getting oversold. Sentiment, based on our proprietary options indicator, is slightly negative. We are in a period where seasonality is positive until early June. Therefore, we do not believe there is a lot of down side in the near-term, and a bounce can take place at any time. However, until it is proven that the market can resume its recent short and intermediate-term uptrend with broad participation, we are back to calling this a bifurcated, opportunistic trader's market, with adept traders able to take advantage long or short.

Federal Funds futures are pricing in an 90% probability that the Fed will *leave rates at 2.00%,* and a 10% probability of *cutting another 25 basis points to 1.75* when they meet again on June 25th.

The S&P 1500 (312.53) was down 1.301% Friday. Average price per share was down 1.25%. Volume was 91% of its 10-day average and 89% of its 30-day average. 12.86% of the S&P 1500 stocks were up on the day. Up Dollars was 3% of its 10-day moving average and Down Dollars was 257% of its 10-day moving average. For the week the index was down 3.37% on slightly increasing but below average weekly volume.

Options expire June 20th. The FOMC meets June 25th.

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

The Kaufman Report - 5/24/2008

The S&P 1500 broke down out of the bearish rising wedge last week and fell through the 20-sma. It is still above the 50-sma which is at 310.

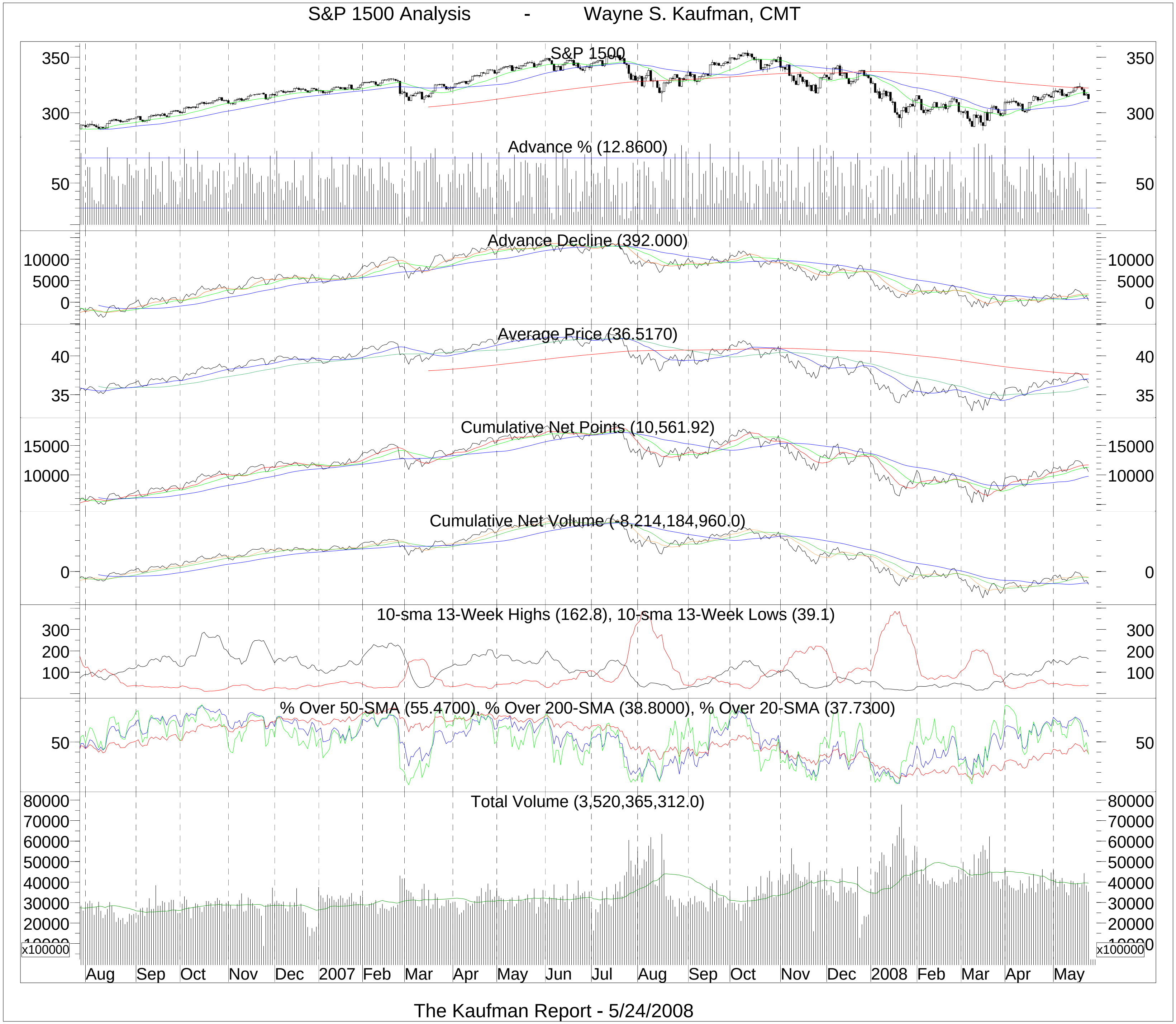
Our oscillators are at low levels and are almost oversold.

New lows are once again greater than new highs.

Our price oscillator, which is a good indicator of trends, is still in positive territory.

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

After breaking out of the bearish rising wedge to the downside the S&P 1500 dropped through its 20-sma but is still above the 50-sma (blue). It stopped exactly at the down trend line (not shown)connecting the October top and the December 11th top. The 50-sma and the 38.2% retracement level are both at 310.



Only 12.86% of the S&P 1500 traded higher Friday.

The AD line did not confirm the end of April early May breakout in the S&P 1500 index, and is now below all the moving averages.

Their is still a big spread between the 10-day moving average of 13-week highs and 13-week lows.

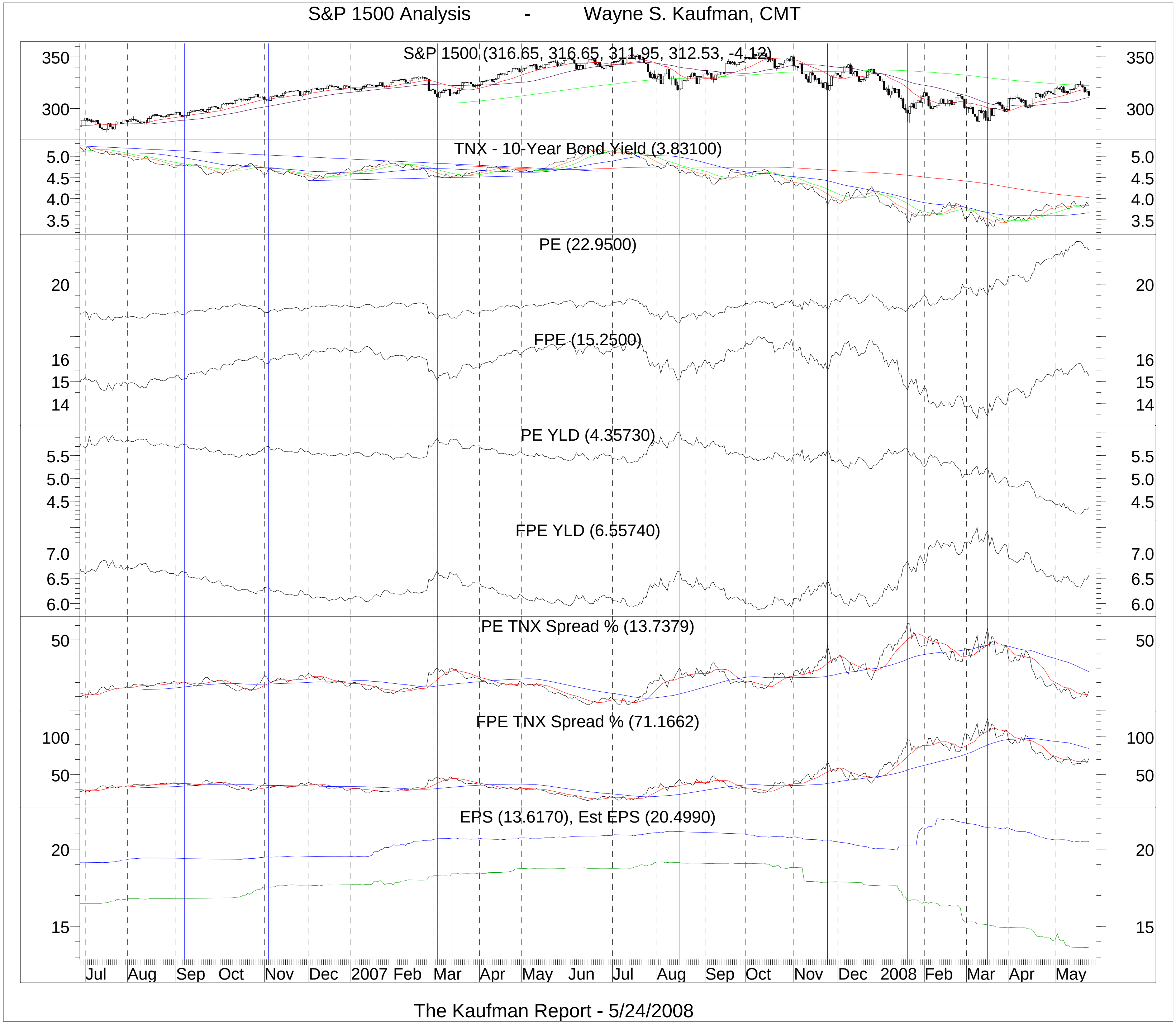
Volume was decreasing and below average Friday.

Our proprietary options indicator is now in negative territory, although only slightly. This should keep the current pull back from being too deep.

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

The Kaufman Report - 5/24/2008

Our 10 and 20-day statistics of demand (green) are lower than the statistics of supply (red). However, so far supply has not been expanding greatly. Demand has contracted more than supply has increased, as can be seen by comparing the 10-day to the 20-day statistics. In other words, so far buyers have stepped to the sidelines more than sellers have become more aggressive.



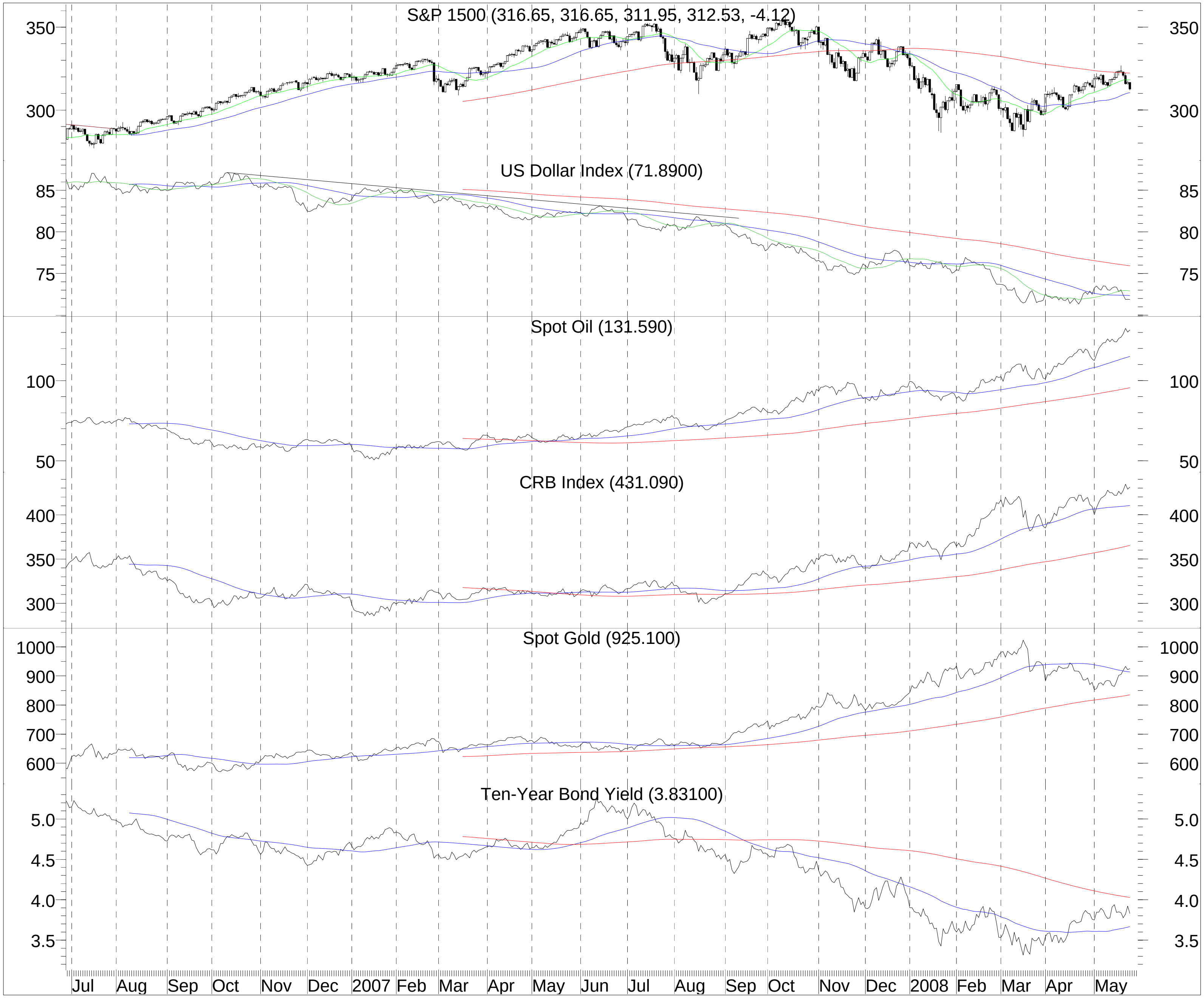
The 10-year bond yield has been moving higher but has resistance in the 200-sma which is at 4.03.

After hitting the highest levels since 2003 the P/E ratio is starting to drop.

Spreads between 10-year bond yields and earnings yields are widening again after hitting levels where drops have occurred in stocks.

Current and forecast earnings are still moving lower, but seem to be leveling off. If forecast numbers stop dropping that should help prevent stock prices from dropping too much.

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



The U.S. Dollar Index has fallen back below its 20 and 50-sma and remains in a long-term down trend.

Oil and commodities continue to make new highs but gold has been lagging.

The S&P 500 got up to the 400-day moving average (purple) but could not get through. The 400-day average was support during the recent bull market, holding even when the 200-day was broken. Now it has become resistance. Unfortunately the 200-day (red) is below the 400-day, which is where it was during the 2001 - 2003 bear market.

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

The Dow Jones Industrial Average made a double top at the 13,135 area and has fallen through its 20 and 50-day moving averages.