

Tuesday October 21, 2008

Closing prices of October 20, 2008

Stocks rallied broadly Monday as the S&P 1500 rose 4.71%. All ten S&P sectors were up sharply led by energy and materials which were up 11.15% and 8.15%, respectively. Volume was light, and the put/call ratio was 0.81 showing options buyers becoming bullish.

Our strategy is as follows: we are buying stocks breaking out of recent oversold ranges while keeping in mind the primary down trend of the market. We are aware of the bearish pennant which is forming and the possibility of another move down, and if triggered we will enter short using inverse ETFs as a hedge. The key point is that with many market statistics having recently reached historic oversold levels, valuations at the best levels in years, and governments around the world carpet bombing financial markets with liquidity, we do not want to miss what could become a meaningful rally. However, good entry points, stop losses, and selectivity are important.

Reported aggregate earnings for the S&P 1500 peaked in August 2007 at \$19.18 and are now at \$11.57, a drop of 39.68%. Estimated aggregate earnings peaked at \$21.95 in February 2008 and are now \$18.32, a drop of only 16.54%. Analysts have obviously been very late in lowering estimates, and have also been way too optimistic. *If investors had any confidence in current earnings estimates stocks would be much higher than they currently are.* The earnings numbers jumped up recently as Lehman, Fannie and Freddie were unceremoniously kicked out of the S&P indexes, highlighting the old expression that sometimes less is more. We are waiting for GM to be kicked out of the Dow.

106 companies in the S&P 500 have reported third quarter earnings. According to Bloomberg, 56.6% have had positive surprises, 16.0% have been in line, and 27.4% have been negative. The year-over-year change has been -34.0% on a share-weighted basis, -18.7% market cap-weighted, and +0.8% non-weighted. Ex-financial stocks these numbers are 8.8%, 15.8%, and 28.4%, respectively.

Federal Funds futures are pricing in an 58.0% probability that the Fed will cut rates 25 basis points to 1.25%, and a 42.0% probability of cutting 50 basis points to 1.00% when they meet on October 29th. They are pricing in a 58.0% probability that the Fed will cut rates 25 basis points to 1.25% at the meeting on December 16th, and a 42% probability of cutting 50 basis points to 1.00%.

The S&P 1500 (213.31) was up 4.71% Monday. Average price per share was up 4.6%. Volume was 66% of its 10-day average and 71% of its 30-day average. 86.7% of the S&P 1500 stocks were up on the day. Up Dollars was 202% of its 10-day moving average and Down Dollars was ¾ of 1% of its 10-day moving average.

The short, intermediate, and long-term trends are down. We reiterate that this continues to be a bifurcated, opportunistic trader's market, with adept traders able to take advantage long or short, but the primary downtrend must be respected. Investors need to be alert to sector rotation and should not hesitate to move out of lagging sectors and stocks and into leaders. Options expire November 21st. December options expire the 19th.

IMPORTANT DISCLOSURES

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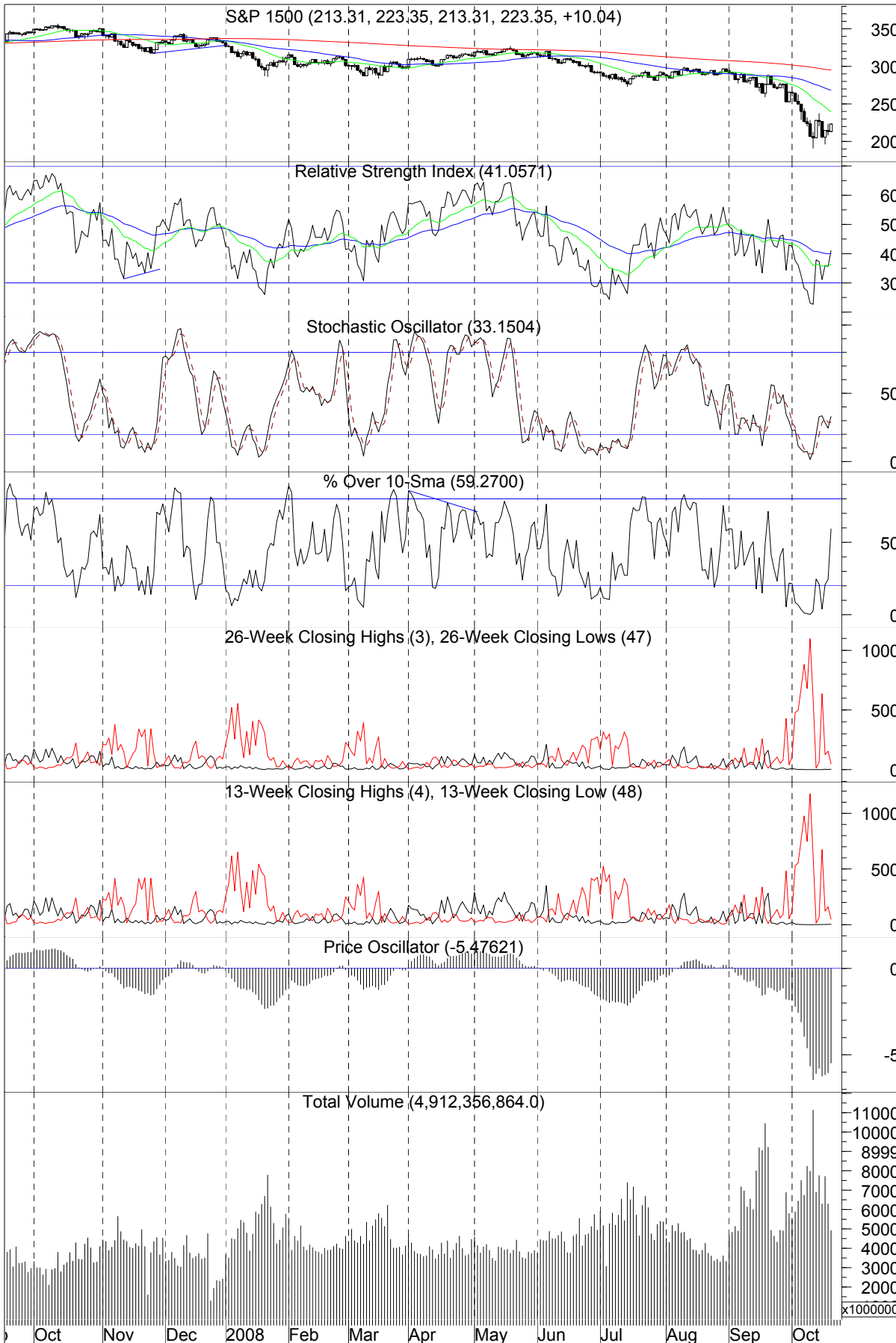
S&P 1500 Analysis - Wayne S. Kaufman, CMT

S&P 1500(213.31, 223.35, 213.31, 223.35, +10.04)



The S&P 1500 remains within the confines of the triangle and the range of the wide-ranging day of 10/13.

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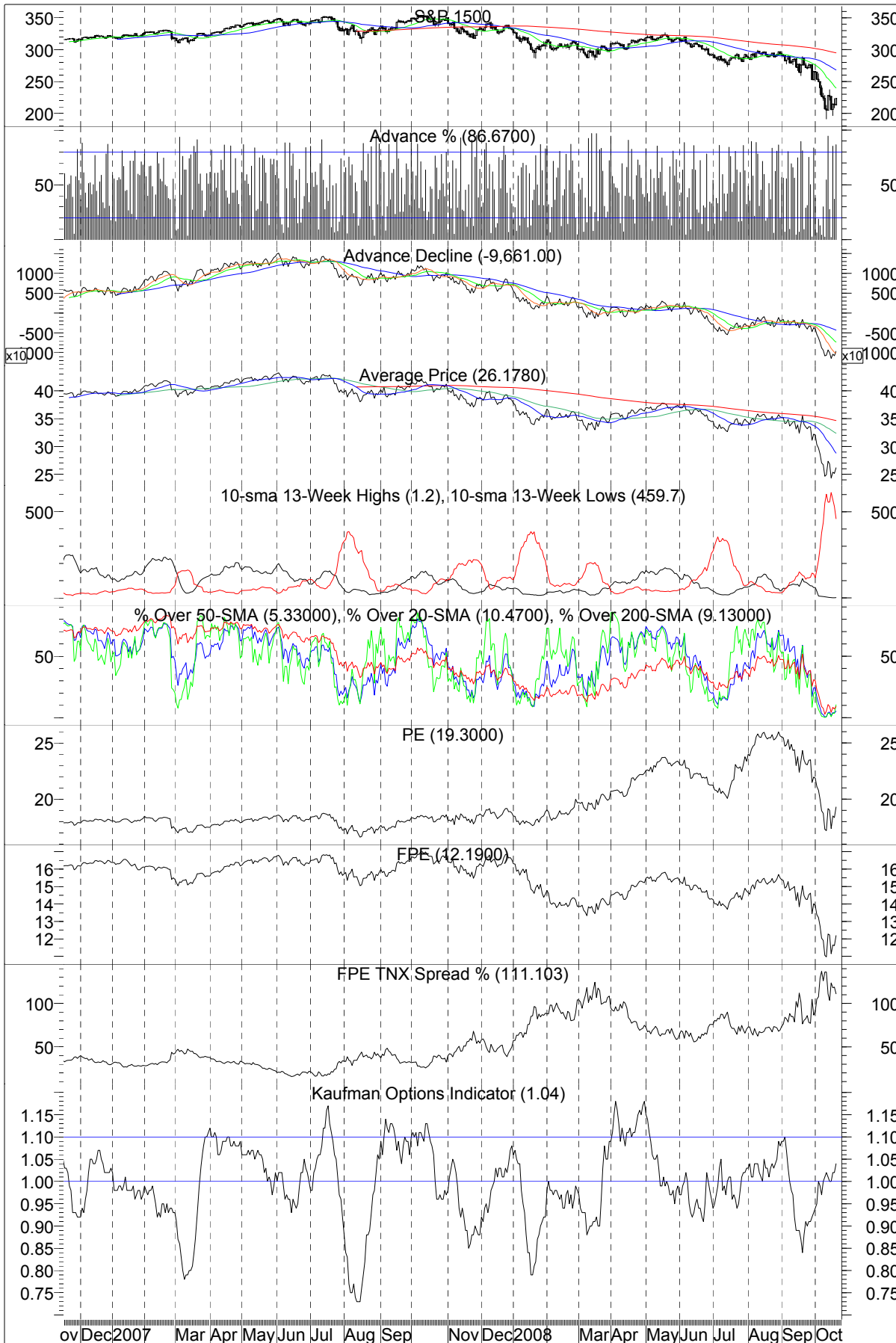


Our oscillators are not yet overbought.

Our price oscillator remains in deeply oversold territory.

Volume decreased quite a bit Monday.

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



86.67% of the S&P 1500 traded higher Monday.

P/E ratios are very reasonable if earnings and projections stabilize.

Options buyers have become bullish, which can put a limit on the upside to this rally.