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# The Kaufman Report

Trade what you see, not what you think.

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Monday April 21, 2008

Closing prices of April 18, 2008

We have discussed the improvements in the intermediate-term picture in stocks recently. The overall picture remains mixed, but last week's strong rally built on the recent strength as the Dow Jones Industrial Average broke out of its sideways channel.

The obvious, important question to investors is whether or not this is just a bear market rally, or is this the start of a new long-term up trend? Again, the overall picture remains mixed. The short and intermediate-term trends are bullish, with longer-term indicators bearish. Our strategy is simple. We have stressed that this is a split market. We believe that investors can profit by buying companies showing high relative strength while keeping in mind that a down trend can resume at any time.

In the long-term, the trend remains down, and this remains a bifurcated, risky, opportunistic traders market with adept traders able to enter long and short. Whipsaw risk is very high. Investors need to be alert for sector rotation and not be afraid to move out of lagging stocks and sectors and into leading ones.

Federal Funds futures are pricing in an 98% probability that the Fed will cut rates another 25 basis points to 2.00%, and a 2% probability of a 50 basis point cut to 1.75% when they meet again on April 30<sup>th</sup>.

So far 101 companies have reported first quarter earnings. According to Bloomberg 57.4% have had positive surprises, 9.9% have been in line, and 32.7% have been negative. The year-over-year average change has been -37.0% on a share-weighted basis, -16.2% market cap-weighted, and -26% non-weighted.

The S&P 1500 (314.62) was up 1.792% Friday. Average price per share was up 1.67%. Volume was 114% of its 10-day average and 100% of its 30-day average. 82.54% of the S&P 1500 stocks were up on the day. Up Dollars was 255% of its 10-day moving average and Down Dollars was 10% of its 10-day moving average. For the week the index was up 4.33% on increasing but below average weekly volume.

Options expire May 16<sup>th</sup>. The FOMC meets April 30<sup>th</sup>.

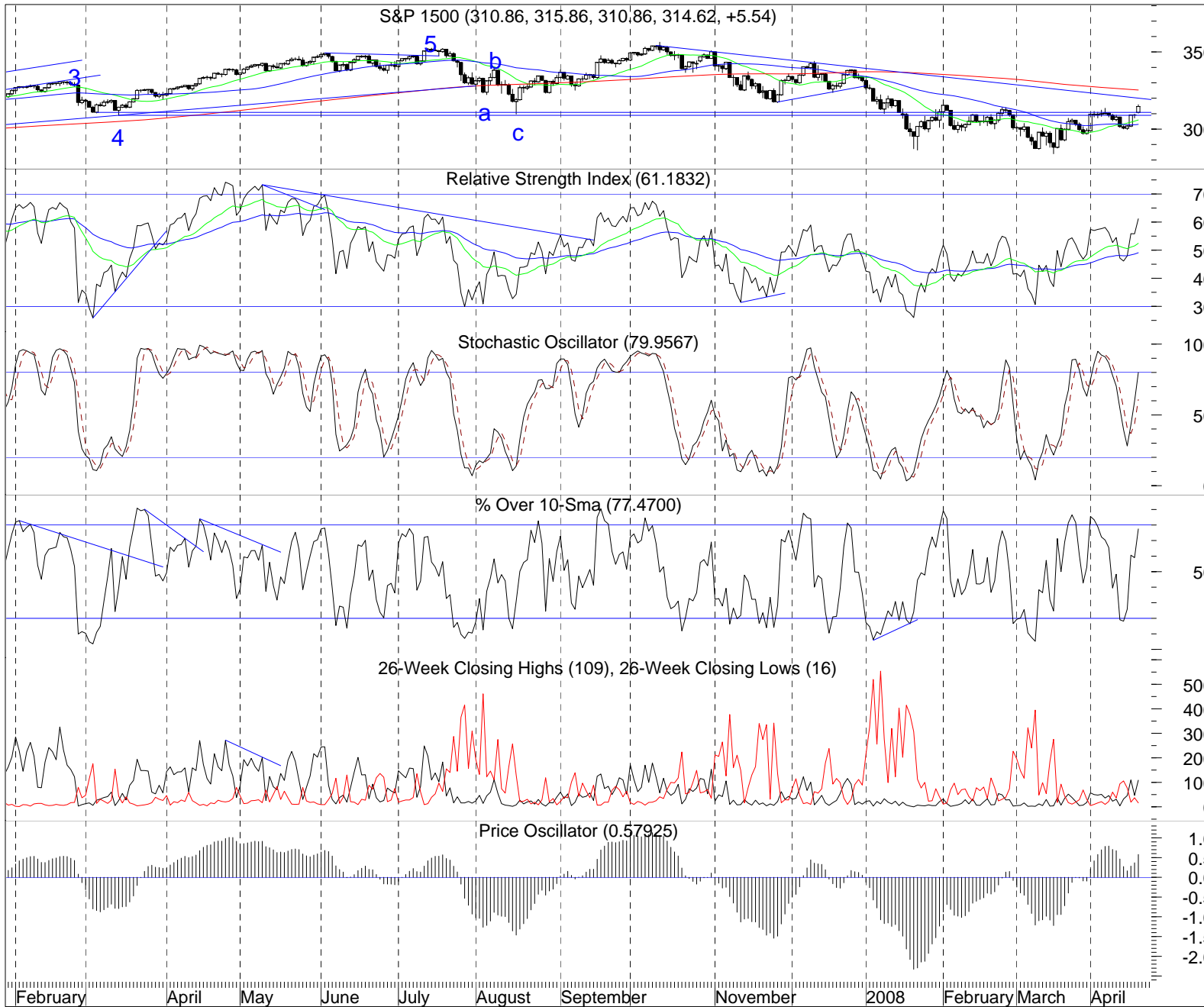
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S&P 1500 Analysis - Wayne S. Kaufman, CMT



The S&P 1500 moved above its April and end of February highs. In doing so it ended a pattern of consecutive lower tops, and is now working on a pattern of higher highs and higher lows.

The RSI is at its highest level since October, although it is still under the 65 level which is bear market resistance.

The stochastic is nearing but not yet overbought.

The percent over 10-sma is also nearing overbought. Less stocks are above their 10-sma than in early April, showing slightly increasing selectivity.

26-week closing highs are at the highest level since December.

Our price oscillator, a good indicator of trends, is positive for the longest time since September.

S&P 1500 (310.86, 315.86, 310.86, 314.62, +5.54)



The S&P 1500 has broken out of a reverse head & Shoulders pattern. In doing so it ended a pattern of lower highs. It broke the February highs intra-day but not on a closing basis. There is more resistance above in terms of price, a down trend line from the October highs, and the 200-sma.



The Dow Jones Industrials broke out from the sideways channel they have been in. They are still below the 200-sma (red line) and the down trend line from the October highs is just above.



The Dow Jones Transports continued their breakout from a reverse head & shoulders pattern. Last week's breakout in the Dow Industrials confirms the breakout in the transports, and is a bullish signal. From a chart perspective the difference in the two indexes at this time is the DJIA is still below its 200-sma while the Transports are above theirs (red line). A move above its 200-sma by the DJIA after last week's breakout will have many technicians declaring a new bull market.

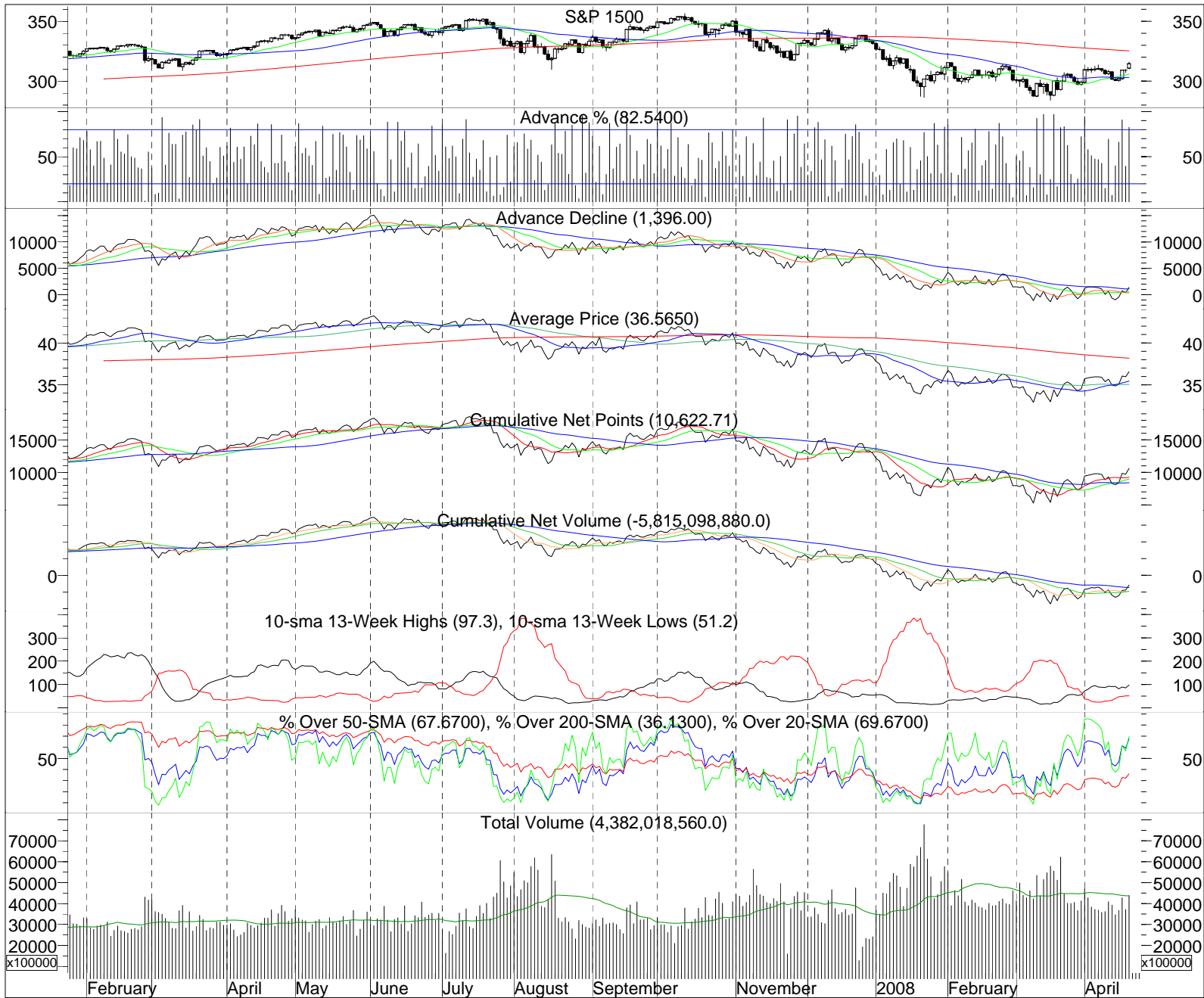
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S&P 500 Cash (1,332.20, 1,395.90, 1,324.35, 1,390.33, +57.50)



The S&P 500 remains below its 40-week (red) and 80-week (purple) moving averages. The 40-week has just crossed below the 80-week. The last time this happened was March 2001. The 20-week moving average (blue) crossed under the 80-week in February. The last time that happened was December 2000. The patterns of these moving averages then and now are eerily similar.

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



82.45% of the S&P 1500 traded higher Friday, a good follow up to Wednesday's 91%. In March we said the multiple days over 80% was bullish.

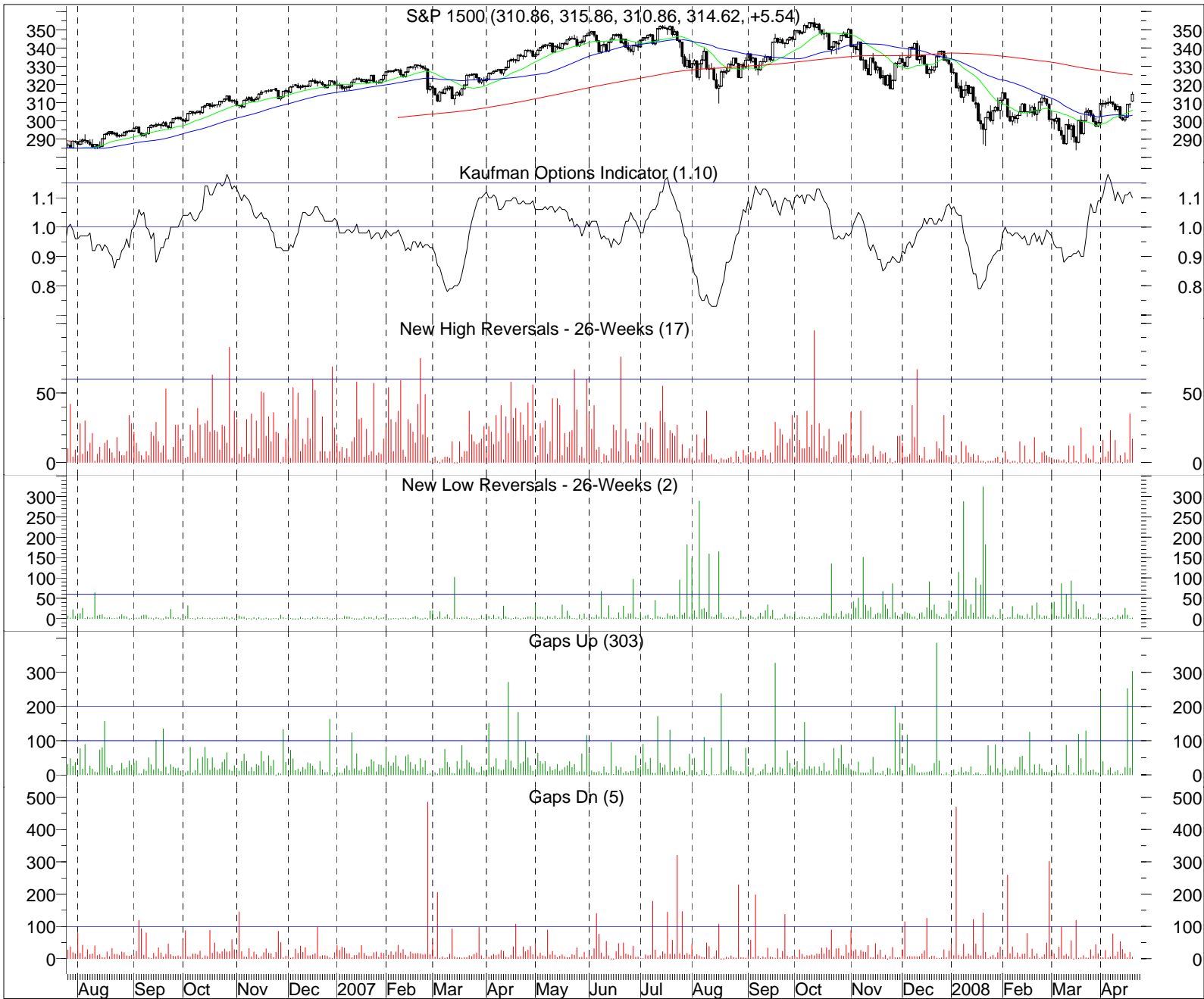
We have a negative divergence in the AD line, which did not exceed its April high. Like the percent over 10-sma, this is showing increased selectivity.

The 10-sma of 13-week highs is the highest since November.

36.13% of stocks are over their 200-sma, the most since December.

Volume has expanded on the recent rally days.

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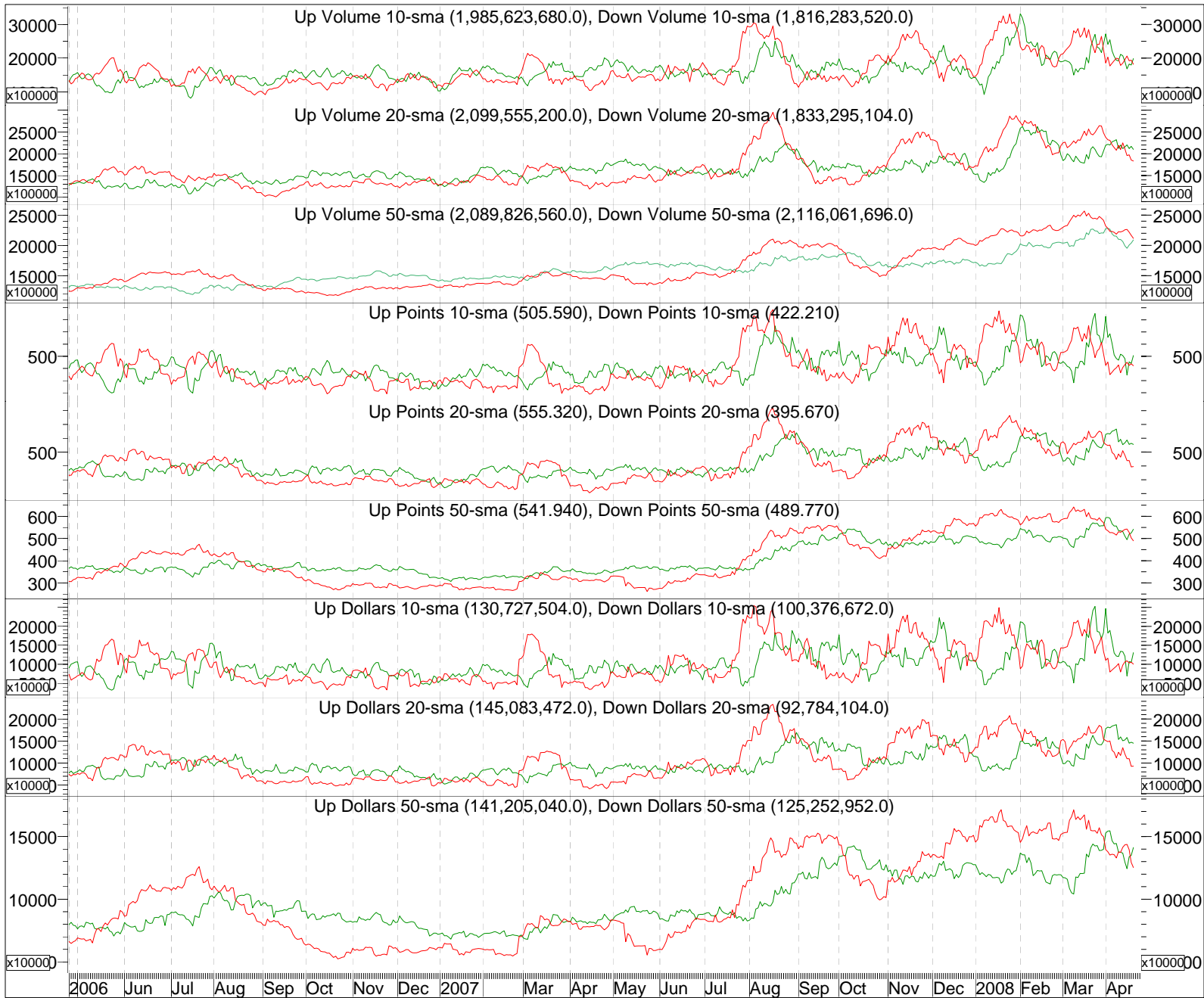


Our proprietary options indicator hit extreme levels of bullishness, which preceded a pull back in stocks. It is still showing a level of bullishness which can leave stocks vulnerable to pull backs, but is at a level where rallies have continued.

Panic-buying was evident last week with two days where a huge amount of stocks had unfilled gaps higher.

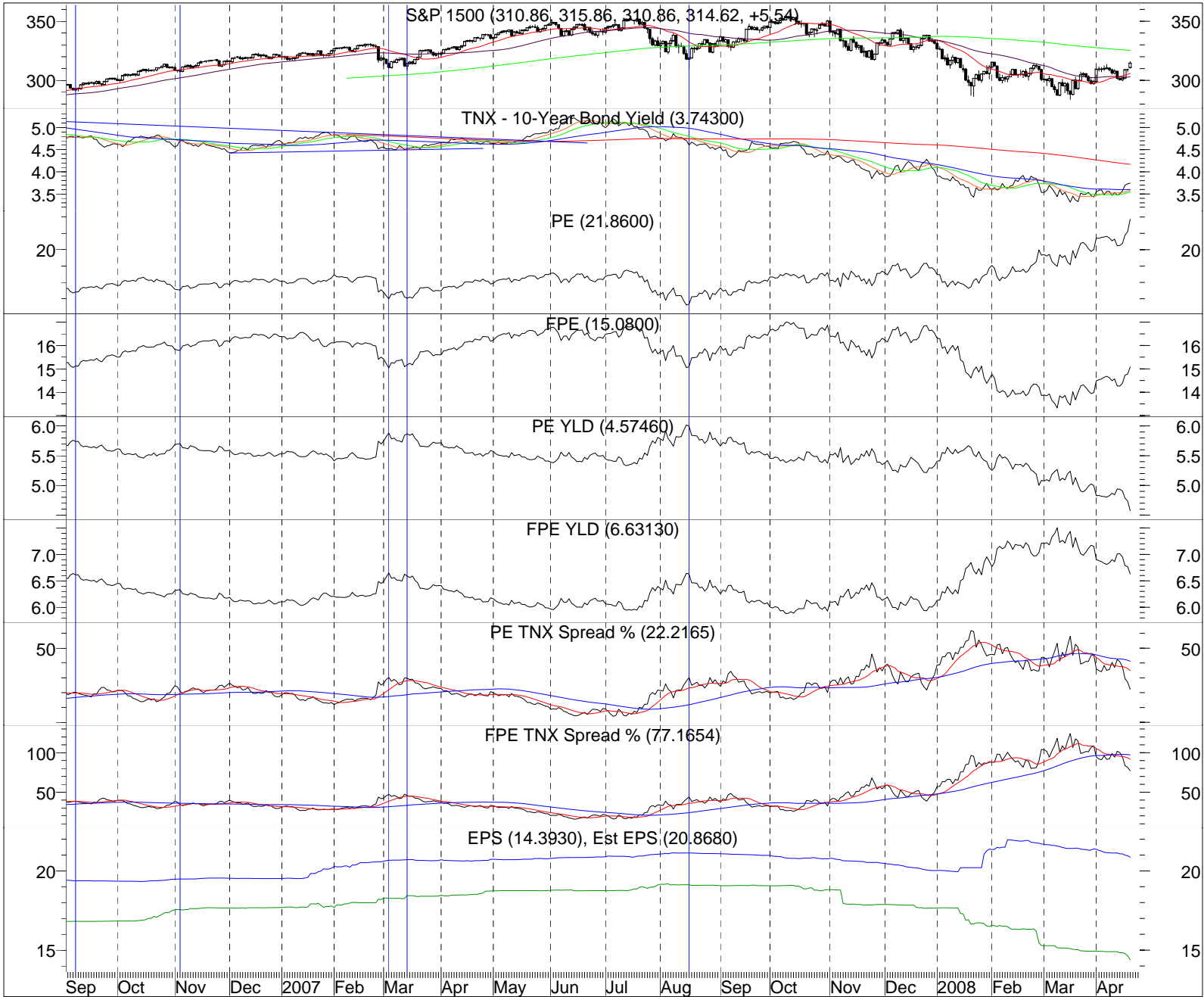


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Our statistics of supply (red lines) and demand (green lines) are showing some positive crossovers. However, this is more due to a lack of sellers than a strong increase in buyers. For example, the 10-day averages of up volume, up points, and up dollars are all lower than their 20 and 50-day averages. To have a bull market we need to see an increase in demand.

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10-year bond yields are above their 20 and 50-sma.

P/Es are rising as stocks move higher and earnings and projections move lower.

Spreads between earnings and bond yields have narrowed as stocks and bond yields rise together. The spread based on the forward P/E is the lowest since mid-January.

Current and projected earnings continue to march inexorably lower.

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