

Tuesday December 30, 2008

Closing prices of December 29, 2008

Stocks traded lower again Monday on another light volume day. The S&P 500 remains just under its 20-day moving average hanging on to support from 12/22. A move below the low of 12/12 will greatly increase the probabilities of testing the November lows. Our proprietary options indicator has spiked to its highest since April 30<sup>th</sup>. The 5-day moving average of the put call ratio is at the lowest level since 1/2/07. Too much bullishness on the part of options buyers leaves stocks vulnerable to a sharp move down if the 12/12 low is broken. In addition, 5-day Bollinger Bands are at their narrowest level since April, suggesting a sharp move is due at any time. With options buyers showing so much optimism, indexes below important moving averages, and buyers being so reluctant, we think probabilities favor a move lower. Still, traders need to be alert to the possibility that the New Year, extreme valuation levels, and the huge pile of cash on the sidelines will bring renewed demand for equities.

The S&P 1500 (196.75) was down 0.522% Monday. Average price per share was down 1.27%. Volume was 69% of its 10-day average and 52% of its 30-day average. 23.4% of the S&P 1500 stocks were up on the day, with up volume at 27.11% and up points at 18.1%. Up Dollars was 7.32% of total dollars, and was 10% of its 10-day moving average while Down Dollars was 126% of its 10-day moving average, in spite of the low total volume. The index is down 2.80% month-to-date, down 26.02% quarter-to-date, down 40.63% year-to-date, and down 44.79% from the peak of 356.38 on 10/11/07. Average price per share is \$22.97, down 46.87% from the peak of \$43.23 on 6/4/2007.

*The Put/Call Ratio was 0.94. The Kaufman Options Indicator is 1.17. This indicates too much bullishness.*

*The spread between the reported earnings yield and 10-year bond yield is 151% and 293% based on projected earnings. These are unheard of levels. The dividend yield on the S&P 500 recently moved higher than the 10-year bond yield for the first time since 1958.*

Reported aggregate earnings for the S&P 1500 peaked in August 2007 at \$19.18 and are now at \$10.36, a drop of 45.98%. Estimated aggregate earnings peaked at \$21.95 in February 2008 and are now \$16.21, a drop of only 26.15%. Analysts have obviously been very late in lowering estimates. If investors had any confidence in current earnings estimates stocks would be much higher than they currently are.

498 companies in the S&P 500 have reported third quarter earnings. According to Bloomberg, 58.1% have had positive surprises, 9.7% have been in line, and 32.3% have been negative. The year-over-year change has been -18.3% on a share-weighted basis, +5.3% market cap-weighted and -2.7% non-weighted. Ex-financial stocks these numbers are 10.1%, 23.7%, and 15.8%, respectively.

Federal Funds futures are pricing in a probability of 74% that the Fed will leave rates unchanged, and a probability of 26.0% of cutting 25 basis points to 0.00% when they meet on January 28<sup>th</sup>. They are pricing in a probability of 63.4% that the Fed will leave rates unchanged on March 17<sup>th</sup>, and a probability 20.3% of cutting 25 basis points to 0.00%.

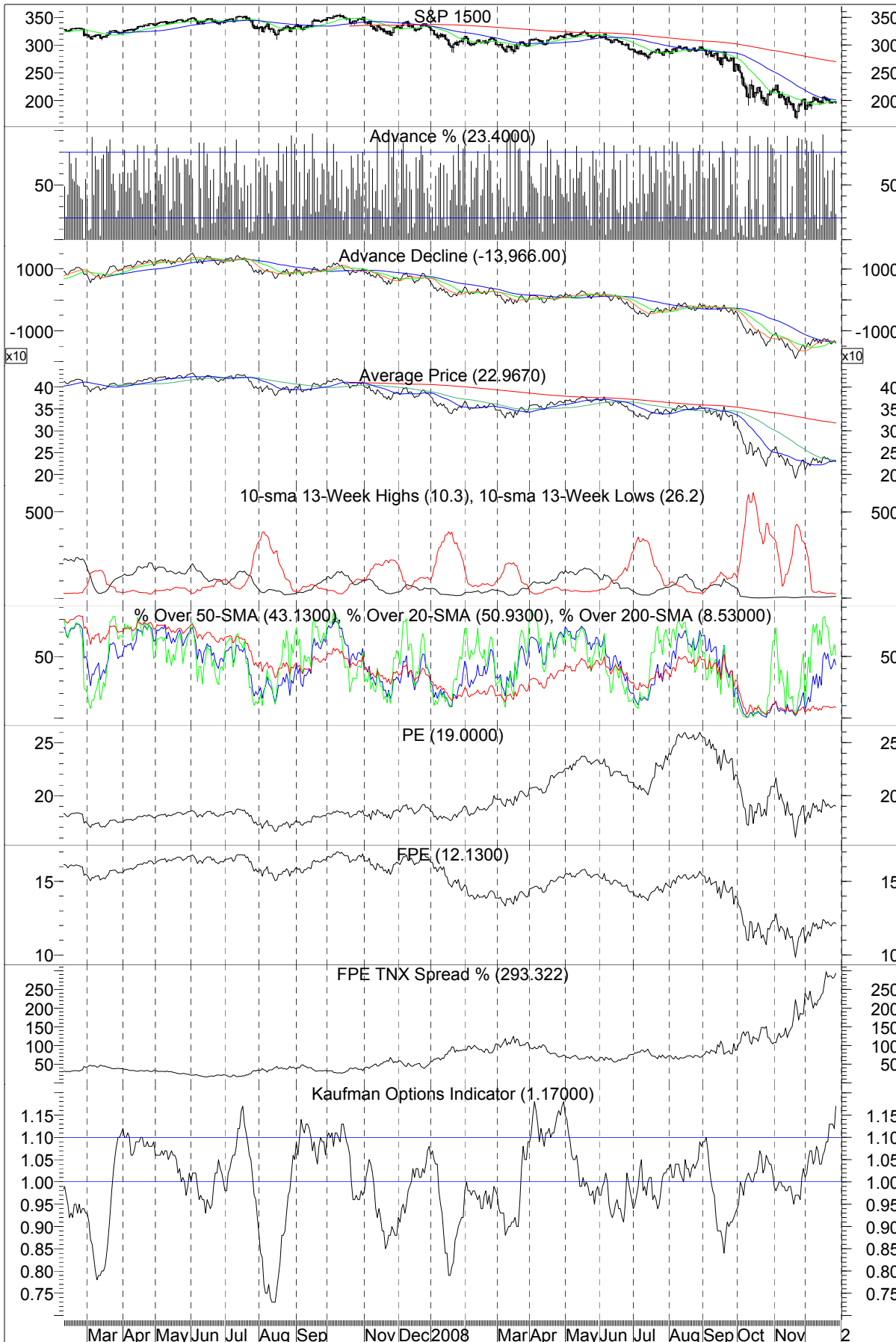
The short-term, intermediate and long-term trends remain down. We reiterate that this continues to be an opportunistic trader's market, with adept traders able to take advantage long or short, but the long-term downtrend must still be respected. Investors should not hesitate to move out of laggard sectors and stocks and into leaders.

## IMPORTANT DISCLOSURES

I, Wayne S. Kaufman, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject issuer(s) or securities. I also certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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



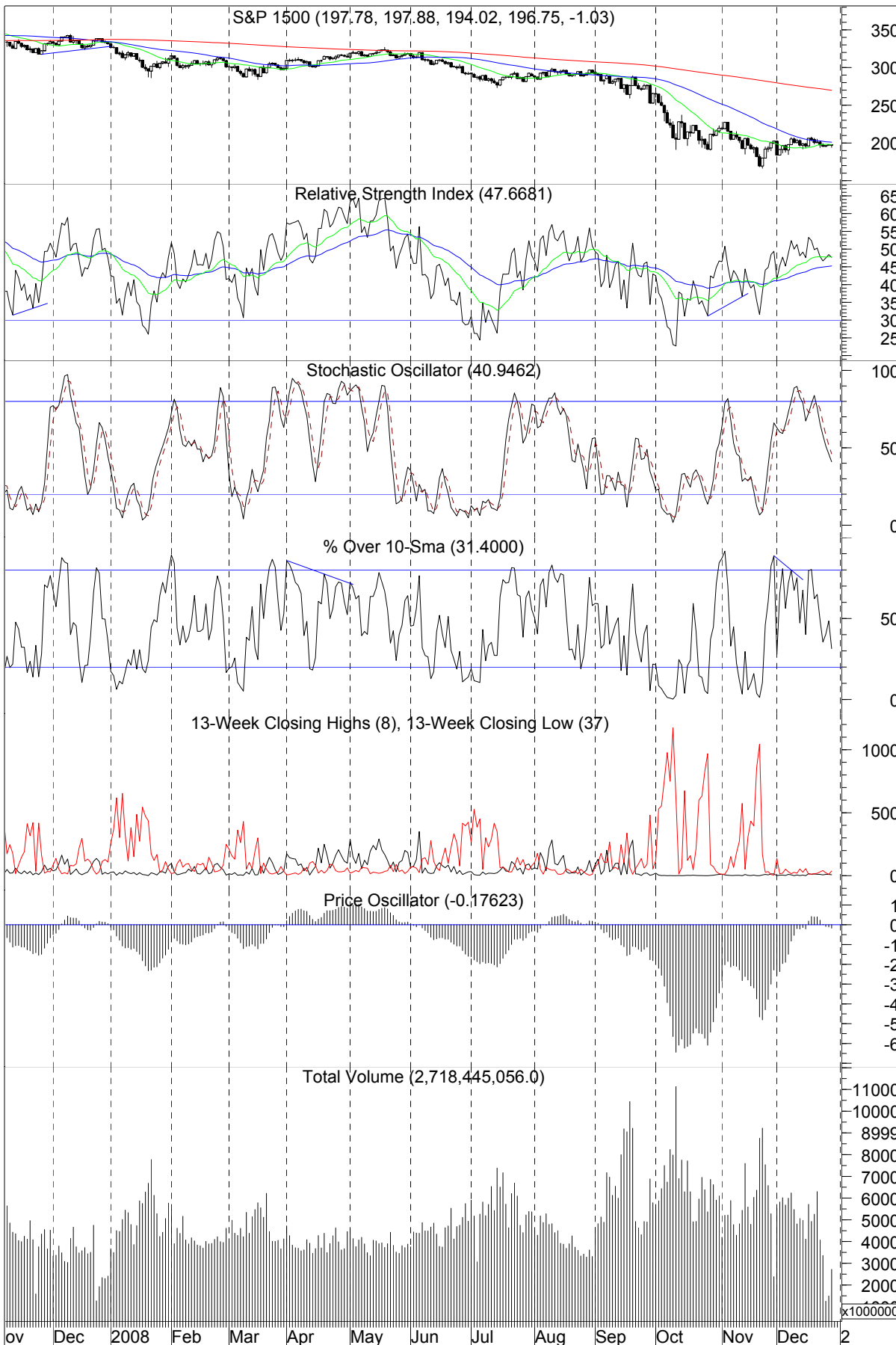
23.4% of stocks traded higher Monday.

P/E ratios remain range-bound.

Spreads between equity and bond yields remains at historic levels and don't seem to matter.

Our proprietary options indicator is showing extreme optimism on the part of options buyers. It is at the highest level since 4/30. This leaves stocks vulnerable to a drop.

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



Our momentum indicators are not yet oversold.

Our price oscillator has dipped back into negative territory.

Volume remains very low, which is typical this time of the year.

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

S&P 500 Cash (872.37, 873.70, 857.07, 869.42, -3.38)



The S&P 500 remains just under the 20-sma. Monday's low of 857.07 is almost identical to the 857.09 of 12/22, so this is an attempt to find support at that level. This is also still above the low of 12/12 at 851.35. 851 takes on further importance since it is also the 38.2% retracement of the rally from the 11/21 low to the 12/17 high. A break of 851 would target the 50% retracement at 830. With 5-day Bollinger Bands at their narrowest level since April, a sharp move soon is likely. With options buyers so bullish recently, we think the probabilities favor a move lower.