WELLINGTON SHIELDS & CO.
MEMBER NEW YORK STOCK EXCHANGE

EQUITIES PERSPECTIVE

April 6, 2018
DJIA: 24,405

A great rally … all one day of it. We are referring to Tuesdays 389 point Dow rally but the reference as easily might be to last Thursday's 255 point rally or the prior Monday's 667 point rally. All of them technically sound – better than 3-to-1 Advance Declines – and all of them followed the next day by a sharp decline, though Wednesday managed to right itself in the end. One day, even a technically strong day, rarely proves meaningful. Indeed, many of the best one-day rallies have occurred in bear markets. Still, we don't recall a pattern quite this extreme, one where 3-to1 up-days are followed by 3-to-1 down-days. Monday's decline was of such an extreme that not one of the NASDAQ 100 stocks was positive on the day. This specific extreme is rare and has led to positive days as we saw Tuesday. The net from this pattern also has an upward bias but, as you can imagine, with more than a little volatility. Like Tuesday the market has set-up to rally, can it follow through?

It's difficult to see follow-through to any rally without leadership. Amazon (1452) and Facebook (159) have turned into plague carriers. Netflix (294) and Google (1028) are doing the guilt by association thing. All this can change in a heartbeat, of course, as news follows price. When the stocks start moving up again, bad news will be good again or, at least tolerable. Surprising and disappointing has been the lack of replacements. Energy shares seemed to have a chance, but as yet aren't quite making it. Even more disappointing has been the Financials. The Fed raised rates which was supposed to leave the Banks, especially, in their happy place. We noticed not much happened, just as not much has happened there all year. A break of the recent lows would change those trading ranges to downtrends. We worry this is one of those trades that made so much sense it became crowded. You know what happens when trades become crowded.

The Fed is tightening and that has never been a good thing for stocks. By now we've all been reminded that Reagan cut taxes in 1981 but Volcker pushed the economy into recession. Reagan also embarked on tax reform in 1986 and a year later Greenspan helped trigger the sharpest market correction since the October 1929 collapse. This time around tightening is more than just about interest rates. The idea that you can reverse quantitative easing without consequences seems wishful thinking. If QE's purpose was to encourage risk and expand credit, Quantitative Tightening should do the opposite. Certainly this could be a problem for a market conditioned all this time to free money. Throw in the problems with Facebook and Amazon, and the "tariff tiff", and the fundamental backdrop is not the best. We bring this up because it comes at a time when the technical backdrop also has deteriorated. The S&P has been hovering around its 200 day average for a couple of weeks now. A break there changes good to evil, so to speak.

This week's momentary break of the S&P 200 day got so much attention it seemed destined to be a non-event. The next break will matter and, of course, be ignored. A break by 2% isn't a bad rule, even better is a move by the 50 day below the 200 day. All the gains in stock prices happen when the 50 day is above the 200 day. The real worry here goes beyond the S&P and its 200 day. Rather, it's about the S&P components and, for that matter, stocks generally. With only about half of the S&P's components, and fewer stocks generally above their own 200 day averages, the market isn't as strong as the S&P makes it look. It's the kind of divergence which eventually will lead to problems and, therefore, how this number recovers will be important. As a practical matter, with only 50% of stocks in uptrends, that is, above their 200 day, it is that much harder to make money.

If one thing is clear it is that the volatility valley of 2017 is gone, and likely will stay gone. Over the last 50 days more than half saw the S&P up or down 1%, including 9 of the last 10 – one of the most volatile periods in 70 years, according to SentimentTrader.com. Particularly over the medium term, these periods were followed by positive returns. Then there was Wednesday's dramatic reversal, another pattern which typically leads to higher prices. The market had its chance to go down but did not, suggesting the sellers finally may be exhausted. We might note, too, at least for that day the market got back to its old pattern of ignoring bad news. Two to one Put to Call buying at the open Wednesday is another positive sign. Still, it all comes down to follow-through. No matter how good, there are no reliable reversals, or one or two day rallies. They are only good in the perspective of the rally which follows. Meanwhile, Aerospace/Defense continues to respond well.

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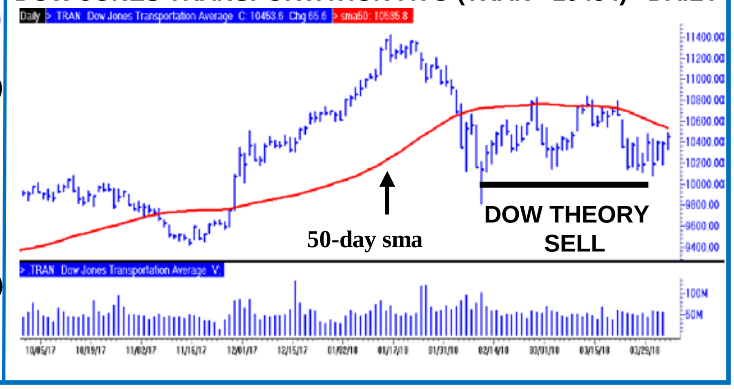
S&P 500 (SPX – 2663) – DAILY

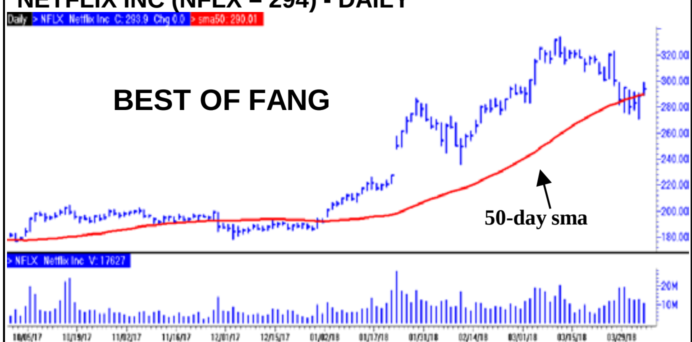
NASDAQ 100 (NDX – 6595) – DAILY

S&P 500 -% OF STOCKS ABOVE THEIR 10-DAY MA - DAILY

DOW JONES TRANSPORTATION AVG (TRAN –10454) - DAILY

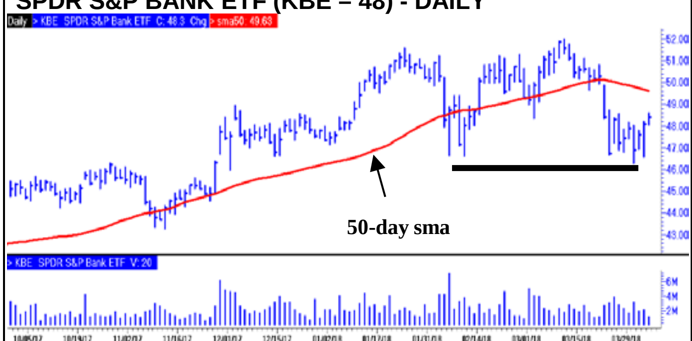


NETFLIX INC (NFLX – 294) - DAILY



NORTHROP GRUMMAN CORP (NOC – 360) - DAILY

SPDR S&P BANK ETF (KBE – 48) - DAILY



SELECT SECTOR SPDR TR - ENERGY (XLE – 69) - DAILY

NIKE INCORPORATED (NKE – 70) - DAILY

EDWARD LIFESCIENCES CORP (EW – 141) - DAILY