EQUITIES PERSPECTIVE

August 4, 2017
DJIA: 22,026

You go your way, I'll go mine … so said the Industrials to the Transports. We're not about to preach Dow Theory, we're here to simply say that, like all divergences, historically this is not good. You might argue, to a considerable extent the Industrial Average itself is diverging. Of the Dow's recent 300 points or so, roughly 200 were Boeing (238). As for the Transports, the Dow Theory made some sense when it was just about the Rails. What some coal-carrying Rail has in common with Southwest Air (56) is hard to see. That said, there is nothing left standing in the Transports—not the Rails, Airlines or even the Truckers of late. And then there's FedEx (209), a company you would think is in touch with the economy, and it looks lower. The Semiconductors also are diverging, a group we would argue is even more economically sensitive. Meanwhile, everyone is all giddy over Dow 22,000?

Divergences don't matter until they matter, this market being a good example. Most important to us is any divergence between the Dow and the Advance-Decline Index, which so far is absent. Thanks to Boeing, there is the idea of a divergence within the Dow, and there is the idea of a divergence within the S&P. Unlike the Dow, which is price-weighted—the higher the price, the greater the impact—the S&P is market-capitalization weighted—the higher the market cap, the bigger the impact. Analysts have looked at equal-weight indexes for years and usually they don't show much. In this case, however, an equal-weighted index of the S&P shows a surprisingly different picture versus the S&P that everyone uses—it hasn't been keeping up. A ratio of the two just hit a 52-week low. Large-cap stocks typically are the last to give it up and this shows up in measures like the Advance-Decline Index. In this case, it's showing up in the S&P itself, and seems another warning sign.

Apple (156) is impressive, though it's doing little more than following the historical script of rising into a product launch. If the script persists, expect a selloff at the launch. At least so far, Apple, not the "A" in FANG, hasn't done much to help there. Since last Thursday's reversal, it has been a struggle. Say what you like about the FANG stocks, they have been the leaders, so the reversals there are not a good thing. Apple is important too for its cadre of suppliers, that is, what have been the diverging Semis. Maybe it is Apple's world and the Semis just live there. Absent the Apple/Semi drama Wednesday, a number of stocks had trouble on their own. Coherent (217) is a stock that has gone from about 80 to 280 since the start of 2016, pretty much defining the term "stretched." And prior to earnings Tuesday, it didn't look bad—it looked like one of those where you probably could squeeze out one more trade—or maybe not. Wednesday the stock sank 60 points, or 22%. When it's over in these stretched stocks, it can be over in a hurry.

Remember the movie, The Graduate? Instead of "Plastics," think "Lithium." According to AutoNation's chief Mike Jackson, we're about to see electric cars from every manufacturer. Think electric, think batteries, think Lithium. Like just about everything, there's an ETF (LIT-32) for this. Gaming of the Take-Two Interactive sort, has been around for a while. For gaming as a business, it's a whole new world out there, something apparent in the price action of stocks like Activision (64), Electronic Arts (119) and Take-Two (89). What has helped is the evolution to a spectator sport, as well as cutting out the middle-man, in this case GameStop (22). In a market where choices have thinned, shall we say, the Defense sector still seems attractive, where you once wanted to be part of the "agenda," you now want to be immune to the agenda, or suffer the on-and-off again routine Financials have been through—though they still look good.

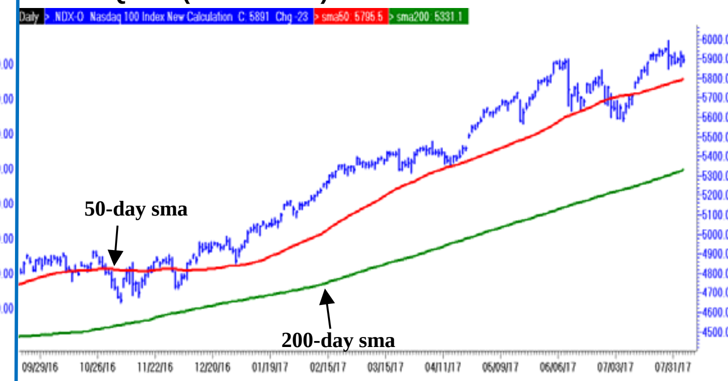
Last Thursday's downside reversal following the Facebook (169) report, produced no dire consequences. So far the same seems true of Wednesday's reversal on the Apple report. Should we believe the market never will go down and any weakness is a chance to buy? Or should we believe that this is the market's way of conditioning everyone before it finally does take a hit? The Advance-Decline Index reached a new high a couple of days ago and, as someone never tires of saying, this isn't the backdrop for important weakness. Then, too, we could have a sharp, if brief, selloff followed by a divergent-riddled recovery. This may sound like we're looking for trouble, but the fact is the market has some problems. The FANG or leadership is stalled despite some good news, Semis are breaking after failing to match the highs in the Averages, Biotechs are weak and Health Care generally has backed away from breakout points. Finally, the Russell 2000 broke its 50-day moving average Wednesday, as the S&P made a new high.

Frank D. Gretz

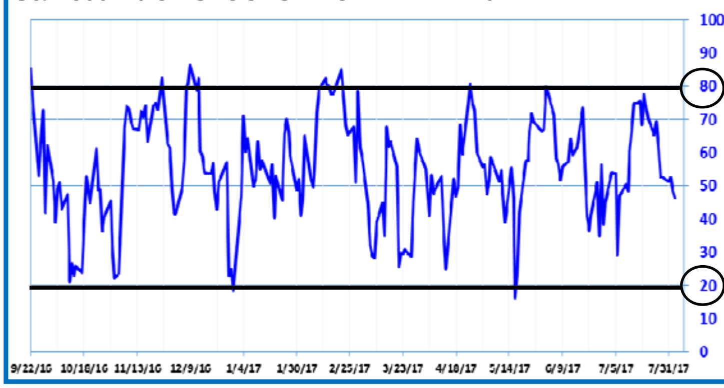
140 BROADWAY NEW YORK, NY 10005 TELEPHONE: (212) 320-3000

S&P 500 (SPX – 2472) – DAILY

NASDAQ 100 (NDX – 5891) – DAILY



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

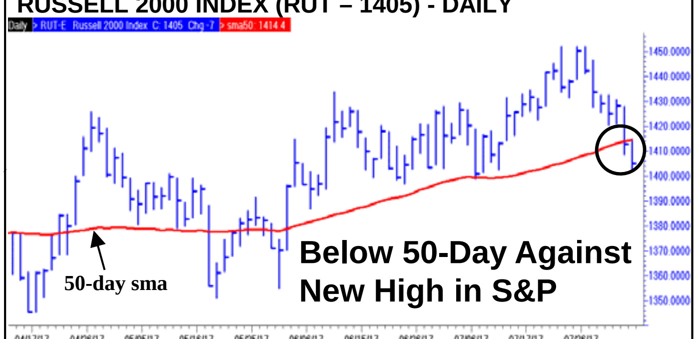


S&P 500 -% OF STOCKS ABOVE THEIR 50-DAY MA - DAILY

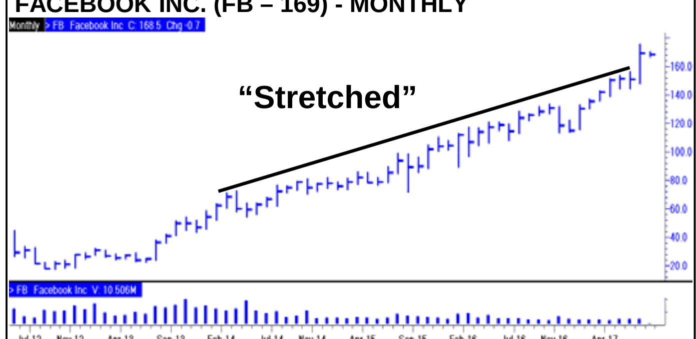
DOW JONES TRANSPORTS (.TRAN – 9202) - DAILY

COHERENT INC. (COHR – 217) - MONTHLY

RUSSELL 2000 INDEX (RUT – 1405) - DAILY



FACEBOOK INC. (FB – 169) - MONTHLY



VANECK SEMICONDUCTOR ETF (SMH – 85) - DAILY

GLOBAL X LITHIUM & BATTERY ETF (LIT – 32) - DAILY