WELLINGTON SHIELDS & CO.
MEMBER NEW YORK STOCK EXCHANGE

EQUITIES PERSPECTIVE

February 16, 2018
DJIA: 25,200

There's the low … and there's the recovery. This may seem a distinction without a difference, but in this market it's likely to prove quite a difference. A low seems pretty clearly in place. As another distinction, we would say the low was a week ago Monday—the low in terms of downside momentum rather than the Thursday low in terms of price. Following the Monday low was the obligatory volatility and "testing,"—call it what you like—that goes with these violent sort of declines. Thursday was the scary day, leaving you to wonder whether we were about to snowball into a series of 1,000-point declines. In retrospect, Thursday's 1,000+ point decline was less intense in terms of selling than was Monday's 1,000+ point decline, at least in terms of the QCHA data—the percentage change in the average stock. Friday was another multiple swing day typical of a bottoming process, this time with a big up close.

In the weakness, there were three days of downside advance-decline numbers of 8-to-1. By almost just about any standard, those are "washout" numbers. Washed out means all the selling is done and if, by definition, all the selling is done, stocks should rise almost as though in a vacuum. After a washout type of low, you would expect at least one 5-to-1 up day, or a couple that are close. Wednesday was a great day, from DJ down 150 to DJ up 250 despite bad news, but 2.3-to-1 was disappointing. The world isn't perfect, including market lows. Still, this does seem another reason to expect a test of the lows. A "test" is typical of these volatile market turns, and is simply a way of saying another move back to the lows. The key to a successful test isn't about price—prices sometimes move lower in a test. What you want to see is less downside momentum—fewer stocks making new lows, a not so bad QCHA and so on.

A mere two weeks ago the term "VIX" brought with it a yawn. Since then, the term has conjured up its name, the "Fear Index." The fear isn't about what it measures, the fear is about what is going on in this index. The index itself, dare we say, is behaving in what seems a normal fashion. Rising from 15 to 50 is not without precedent, the index having done so in May 2000, August 2011 and, more recently, August 2015. All were associated with fearful selling and market turning points. The problem this time around is in those instruments created by Wall Street to take advantage of a prolonged period of low volatility. When that period ended a couple of weeks ago, it ended hard in instruments that short volatility, like SVXY (13), down almost 90% and the XIV (6), down even more. While conspiracy theories have arisen, even if just another "crowded trade," you can see how dislocations likely took place. It was almost a Black Swan sort of event, and those pass. Meanwhile, the VIX itself has dropped sharply, which is a positive sign.

Aerospace/Defense stocks have been stellar performers for quite a while. True, the stocks went through a pause from late last October to early-January, but even bull market stocks deserve a rest. These are bull market stocks, being in near perfect uptrends since 2013. They're not just tied to North Korea or some such thing, though they can trade as a bit of a hedge. The recent action in these stocks seems impressive as well. In the scheme of things, their corrections have been shallow, and they've seemed quite resilient with any let up in market weakness. When markets make a low, everything recovers. As Edson Gould sarcastically quipped at the end of the bear market in 1974, buy every fourth stock on the NYSE. Stocks that hold up the best show the best relative strength and tend to go on to lead in the subsequent recovery. Aerospace/Defense has led all along and this seems likely to continue.

First they won't stop going down, now they won't stop going up. From being pleased that you sold, to now worrying about how to get back in. Will they "test" those lows, or won't they? Markets don't go straight down and markets don't go straight up, but this is the second time in as many weeks that this one has made you wonder. Markets like this typically do revisit the lows, but it's not something carved in stone. Price gains have been impressive, advance-declines, not so much, leaving us to favor the test scenario. Meanwhile, to be or not to be, to coin a phrase—more importantly, where to be? Leadership often changes after these corrections, though it's a little early to say. The FANG stocks have become a bit troublesome, particularly Facebook (180), and Northrop (357) is outperforming even Netflix (280). Cisco (44) was impressive this week, leaving us to still favor retro-names Microsoft (93), Nike (68) and eBay (43).

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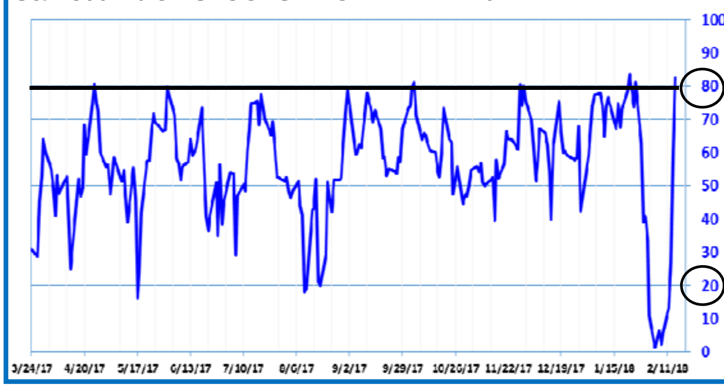
S&P 500 (SPX – 2731) – DAILY

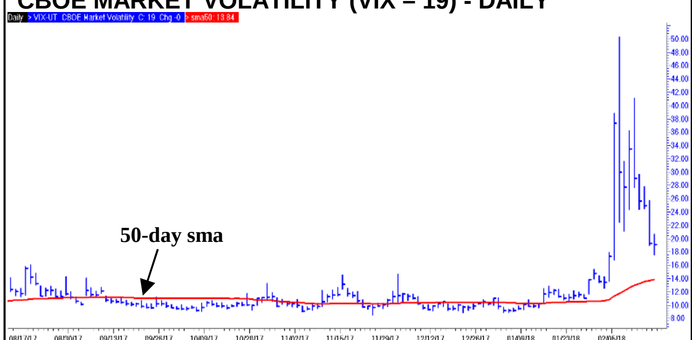
NASDAQ 100 (NDX – 6795) – DAILY

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

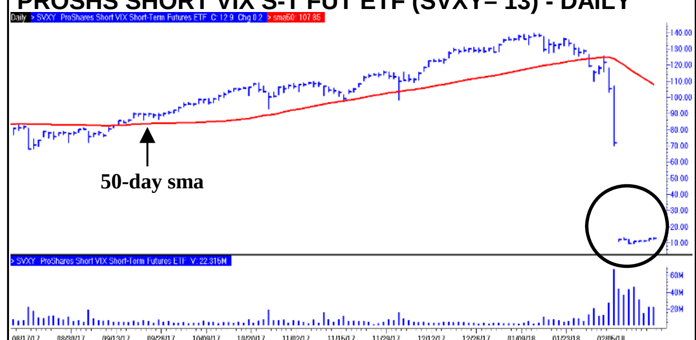


S&P 500 -% OF STOCKS ABOVE THEIR 200-DAY MA - DAILY

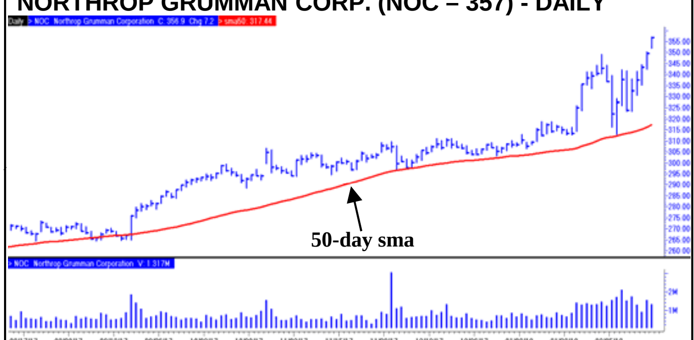
CBOE MARKET VOLATILITY (VIX – 19) - DAILY



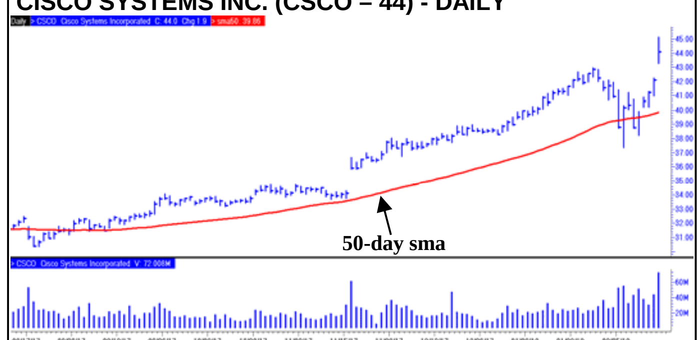
PROSHS SHORT VIX S-T FUT ETF (SVXY– 13) - DAILY



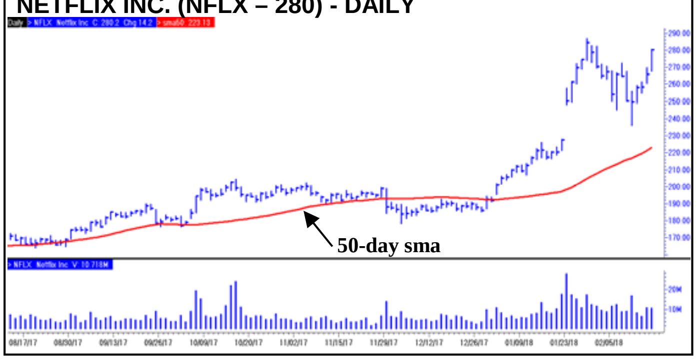
NORTHROP GRUMMAN CORP. (NOC – 357) - DAILY



CISCO SYSTEMS INC. (CSCO – 44) - DAILY



NETFLIX INC. (NFLX – 280) - DAILY



FACEBOOK INC. (FB – 180) - DAILY