WELLINGTON SHIELDS & CO.
MEMBER NEW YORK STOCK EXCHANGE

EQUITIES PERSPECTIVE

February 9, 2018
DJIA: 23,860

Bear market start … or bear market end? While everyone worries about the former, the look has been that of the latter. Bear markets don't begin with some dramatic gut-wrenching decline. Rather, that's how they end. Bear markets begin in an almost prosaic orderly way, with stocks and groups peaking a few at a time. This is why that Advance-Decline Index, among other measures, is important. It typically leads the stock averages by four months or more. In this case, the peak in the A-D Index was just January 23rd. Bull market peaks are a process, not some waterfall decline like we've seen recently. What we've seen recently looks more like the kind of "washout" or climactic low you would expect at the bottom of a bear market. What we saw even last week was the worst week in two years after one of the best—not the start of something, but a reaction to something. In the market's own inimitable way, an over-reaction.

The weakness has taken many measures to extremes. Stocks above their 10-day moving average, with a typical range of 20%-to-80%, reached 1.4% on Monday. Also on Monday, all of the NASDAQ 100 components were down on the day. The VIX had its second biggest jump ever. The good news there, the subsequent risk/reward over the next six months was overwhelmingly positive. Similarly, consecutive 2% losses after a new high saw the market rally at least 6% over the next six months. And then there was last Friday's semi-rout—with '87 in mind, something we never like to see. As the worst decline in six months, and coming off a new high in the averages, precedent called for a down Monday, which we got. On three of the other four such times since 2009, Monday marked the low, according to SentimenTrader.com. So the market had at least a few things going for it as we looked in the eye of a 500-point lower opening on Tuesday.

Up openings in down markets never seem to work, another hopeful sign Tuesday. After a multiple swing day, the Dow and S&P 500 closes seemed another hopeful sign. The lack of follow-through Wednesday and Thursday has surprised us. This still could be part of the bottoming process, and certainly part of that process will be a so-called "test of the lows." In this case, the proximity to Monday's washout would be unusual. Then, too, what's usual these days? Part of this, including the "washout" Monday afternoon has that mechanical look like the last time the ETFs became mispriced. In this case, the so-called volatility ETFs seem at issue, and to this point at least some have self-destructed—look at the hit to CBOE (111). We've long thought ETFs are like portfolio insurance when it comes to risk. Both are supposed to hedge risk while, instead, they can increase it. Sell an ETF and the underlying securities need be sold, and so on, and so on.

It's a sad commentary when Thursday's drop of 1033 points was only the second worst day of the week. What looked to be a good open proved once again, there are none in down markets. These openings have become a story unto themselves. In days of yore, those being January, S&P futures opened regular trading hours higher than the prior day's close 25 of 30 days. If you buy into the idea that the first hour of trading is "amateur hour," that might have proved a warning, though rewarding while it lasted. Now instead of gapping up almost every morning, stocks are gapping down almost every morning—seven of the eight sessions through Wednesday. Historically this has been a sign of too much emotional selling and, unlike January's emotional buying, has proven a good sign. All of this still can be part of a bottoming process, but keep in mind Jesse Livermore's advice—sell down to the sleeping point.

When the volatility dust finally settles, a major problem will remain—rates are moving higher. Say what you will, history is pretty clear that stocks do well when rates are falling and they do poorly when rates are rising. They say this time is different because overall, rates remain low or they're rising because the economy is doing so well. You have to ask yourself, do you really want to go with "this time is different?" The fact that the Advance-Decline Index peaked just a few weeks ago says there's more time left in the bull market. How profitable that time will prove depends on how well the advance-declines dig themselves out of the hole they've dug. Again, it's not the weakness, it's the weak recoveries that get you. A low here—and there will be one—will require a test of the low and lots of volatility. In its way, Monday may yet turn out to have been the low, what's needed is some upside confirmation.

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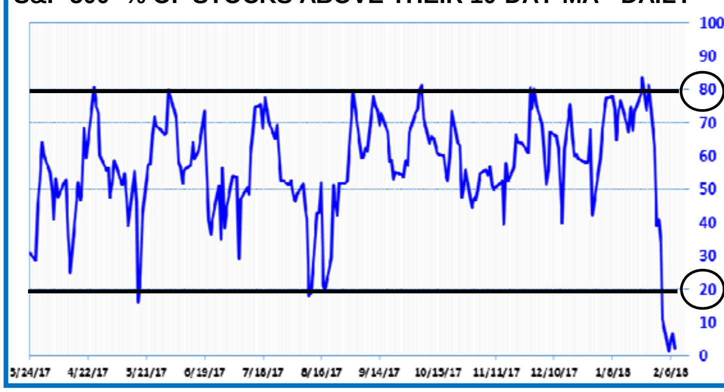
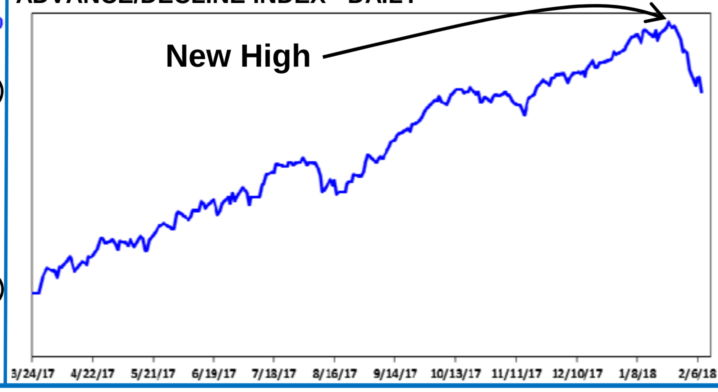
S&P 500 (SPX – 2581) – DAILY

NASDAQ 100 (NDX – 6306) – DAILY

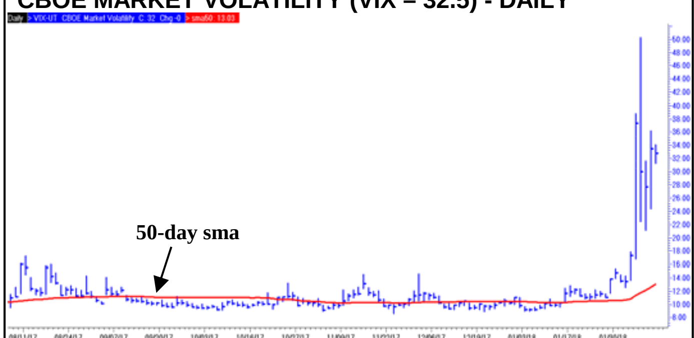
S&P 500 -% OF STOCKS ABOVE THEIR 10-DAY MA - DAILY



ADVANCE/DECLINE INDEX - DAILY



CBOE MARKET VOLATILITY (VIX – 32.5) - DAILY

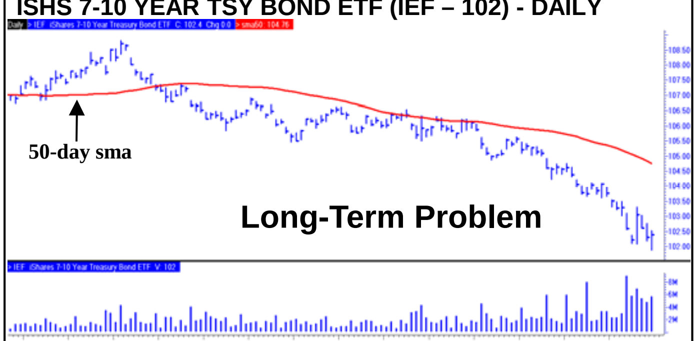


CBOE GLOBAL MARKETS, INC. (CBOE – 111) - DAILY

AMAZON.COM INCORPORATED (AMZN – 1350) - DAILY

NETFLIX INC. (NFLX – 250) - DAILY

ISHS 7-10 YEAR TSY BOND ETF (IEF – 102) - DAILY



SPDR FUND UTILITIES (XLU – 48) - DAILY