WELLINGTON SHIELDS & Co.
MEMBER NEW YORK STOCK EXCHANGE

EQUITIES PERSPECTIVE

September 16, 2016
DJIA: 18,212

When things change … change your mind. So advised none other than Keynes, himself not a bad investor. The advice, of course, is a thinly veiled admonition to cut your losses. While always sage advice, it's not clear for the market as a whole that the time is here. Certainly there's a change – the unusually persistent lull is history and there's a change to weakness, particularly in terms of stocks up versus down. Long the market's best feature, Friday's 20-to-1 down day and Tuesday's 8-to-1 follow-through are awakenings that can only be described as "rude." Yet, is it more than a market so tightly wound – 50 days without a 1% move – that something had to give? Time will tell, to coin a phrase. The backdrop may be serious but not yet dire. Indeed, the backdrop seems more like that of last June than it does those preceding important declines.

There's little surprise that this "Fed speak" decline and last June's Brexit weakness seem similar. Sharp declines usually do. Friday's near 400-point Dow decline compares to a 600-point down day last June, while Friday's 20-to-1 downside breadth ratio compares with 6-to-1 back in June. More importantly, both markets became oversold or stretched to the downside – in both instances stocks above their 10-day average reached the 10% level. Both declines also produced a spike in the VIX, and the recent weakness also has seen a significant pickup in inverse ETF trading, that is, hedging or shorting. More than the declines per se, a more important similarity is the backdrop from which they began. Absent in both cases is a divergent background from which significant weakness usually begins. Certainly the background has some issues, but the Advance-Decline Index and the QCHA A-D Index made new highs last week and there were 450 12-month New Highs – not the backdrop for a big decline.

We have suggested many times that it's not weakness that gets markets in trouble, it's the weak rallies that follow. This seems particularly relevant here in that those Advance-Decline numbers have dug themselves quite a hole, at least short term. A poor recovery there would lead to more important problems. First things first, we have to get through Wednesday and the Fed meeting. If they are data dependent, given the data you wouldn't expect a hike. However, they seem to want it so badly, a hike wouldn't surprise us. The futures market puts the odds of an increase at only about 25%. So an increase would come as a surprise and likely result in a negative reaction. It's hard to believe that a quarter-point really matters, but last Friday suggests it does. It's hard to believe it matters but look at what happened to the Homebuilders last Friday. It should be good for Banks, despite the fictitious accounts. Good, of course, is relative if the overall market reacts badly.

We would suggest that few are expecting some sudden outbreak of world peace. And regardless of the outcome of the election, rising defense spending seems a given. Therefore, defense stocks make sense except for the fact that we are talking about the stock market. When it comes to the stock market, simple logic or what makes sense, rarely matters. To wit, since mid-July-August, the primary Aerospace-Defense stocks have performed poorly, and in the case of Lockheed (239), horribly. The same might be said of stocks like Martin Marietta (178) or Vulcan Materials (110), where project funding is already in place, and yet the stocks peaked at the end of July. Granted the stocks are correcting with uptrends still in place, and we all deserve a rest from time-to-time. Still, we never like to see leadership areas give it up, so to speak. Think of last year's leadership group, the Biotechs, their peak in July, and the market's subsequent problems.

Since mid-August, another worrisome part of the background has been the volume pattern. There are so many ways to trade, volume is hard to measure. However, we're not interested in absolute volume but, rather, whether it rises or falls day-to-day. If you look at advance-declines on days when volume rises, there should be a rising pattern, an uptrend. Healthy markets rally on rising volume and fall on declining volume. Stock marketwise, that's as close as it gets to the riddle of existence. And, indeed, that is what the market did until the middle of August. Since then there has been a significant change – the uptrend has turned to downtrend. As per the above, breadth itself has some considerable recouping to do. For any recovery to prove durable, it should be accompanied as well, by rising volume.

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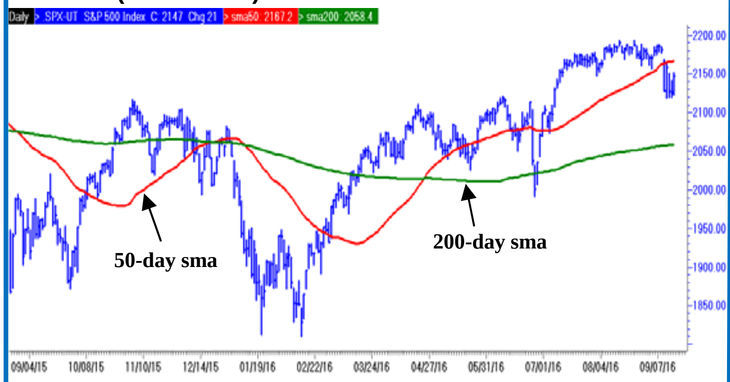
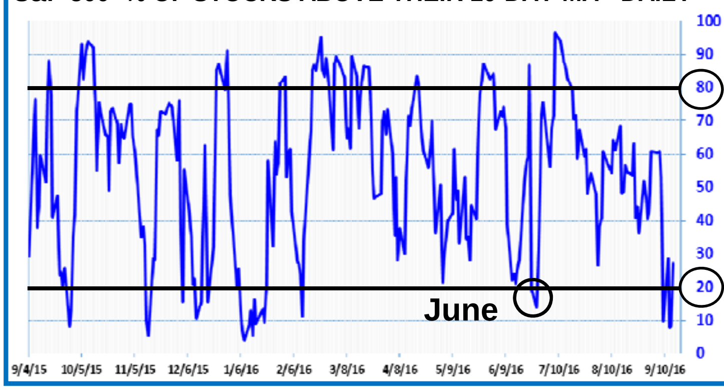
S&P 500 (SPX – 2147) – DAILY

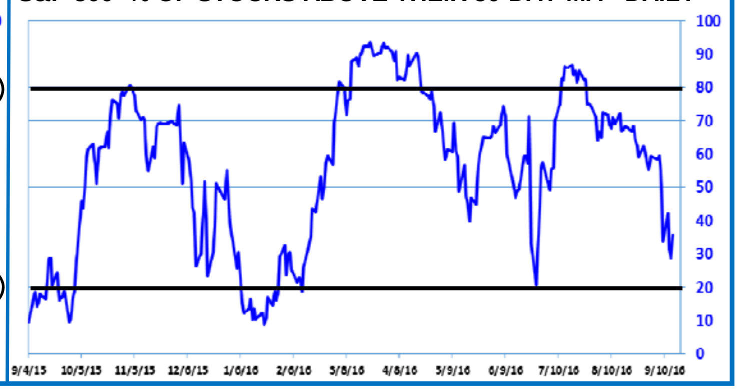


NASDAQ 100 (NDX – 4820) – DAILY

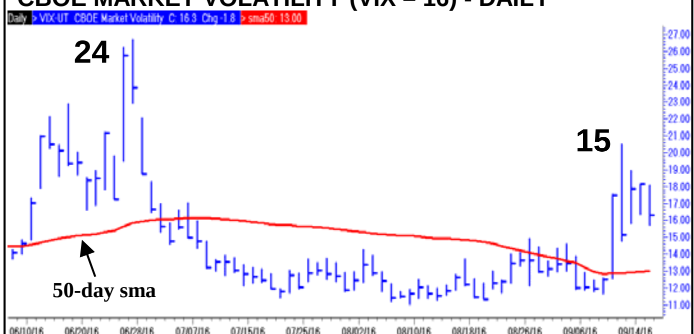
S&P 500 -% OF STOCKS ABOVE THEIR 10-DAY MA - DAILY



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



CBOE MARKET VOLATILITY (VIX – 16) - DAILY

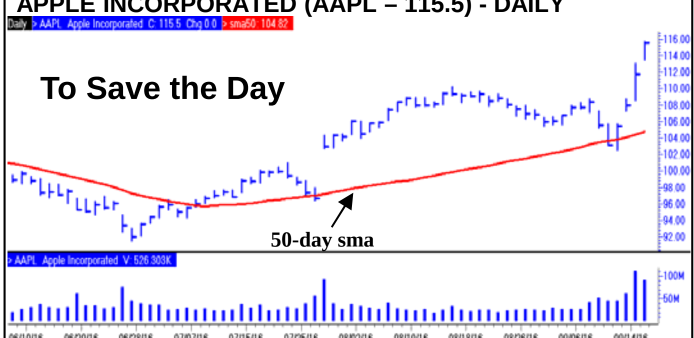


ADVANCE-DECLINE INDEX - DAILY

SPDR S&P HOMEBUILDERS (XHB – 34) - DAILY

ISHS 20+ YEAR TREASURY BOND ETF (TLT – 134) - DAILY

APPLE INCORPORATED (AAPL – 115.5) - DAILY



ALPHABET INC. (C) (GOOG – 772) - DAILY