Dudack Research Group
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DJIA: 39593.66
SPX: 5268.05
NASDAQ: 16387.31

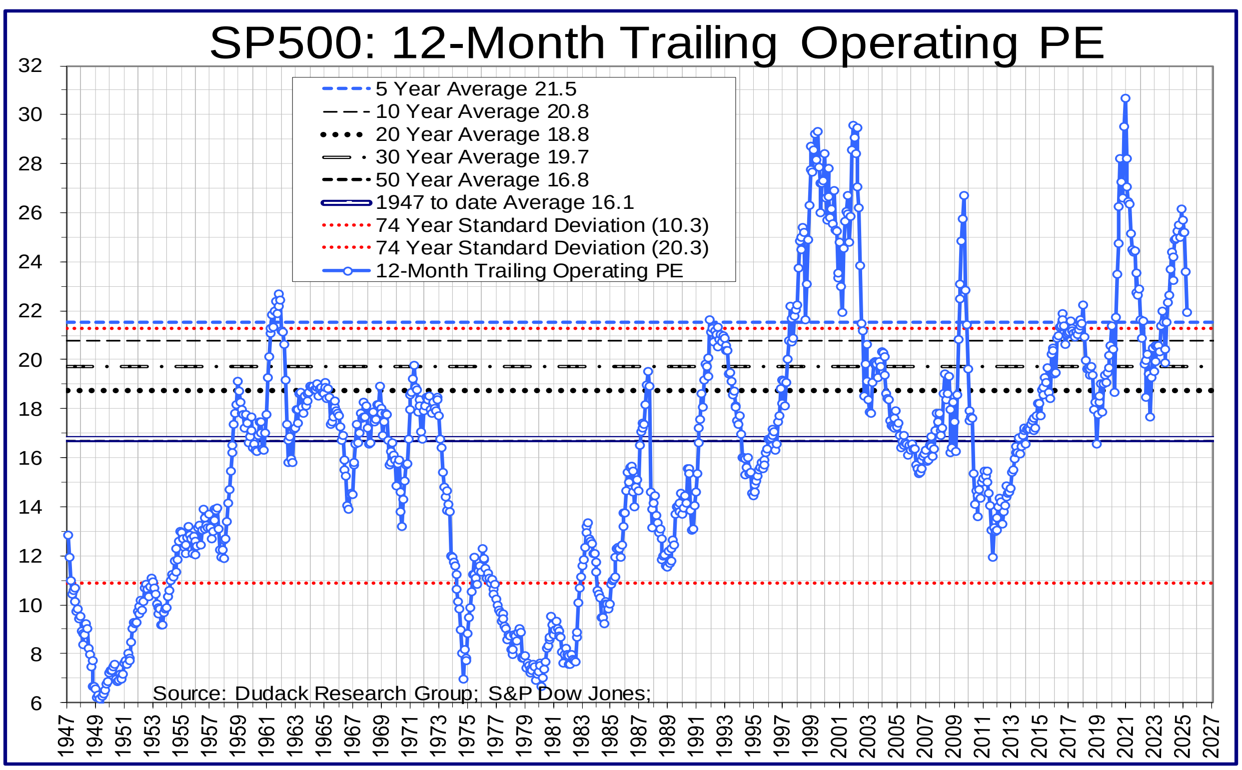
# Direct from Dudack

## Checking on Valuation

Despite Thursday's 587.58 point decline in the Dow Jones Industrial Average, NYSE volume was back in line with the 10-day average and downside volume was 84% of total volume. This was well short of the 91% down day seen on April 4. In sum, the equity market is retesting last week's low on lower and less intense selling pressure. This is positive from a technical perspective.

As we noted yesterday *"It would not be a surprise if some hedge funds continue to face liquidity problems in the near future. Therefore, investors should expect more unwinding and more volatility in the days ahead."* The recent turmoil seen in the financial markets plays havoc with highly leveraged portfolios and leverage has the potential of creating forced buying and forced selling. More importantly, it can lead to severe liquidity problems for some money managers which could translate into more panic selling. In other words, some market moves are liquidity-driven and not economically driven, and it is important to understand there is a difference between the two. Liquidity-driven declines are short dramatic downdrafts and represent opportunities, whereas economically driven moves can be longer lasting moves.

In terms of economically driven moves, this week marks the start of first quarter earnings season and earnings forecasts will play a major role in the market's stability or instability in the weeks ahead. In times of extreme stress and uncertainty, it is helpful to look at the history of trailing PE ratios at market lows -- not to define a price target -- but to look at worst case scenarios. The current trailing PE ratio is 21.9 X and the long-term average is 16.1 X. The 16.1 multiple is too low, in our view, since the current 2.4% inflation rate is below average. The trailing PE ratio at the September 2022 low was 17.6 X and with the S&P/Dow Jones earnings estimate for the end of the second quarter currently at $244.62, this translates to SPX 4305. The intraday low on April 7, 2025 was 4835, or 11% above SPX 4305. (Note that the 10-year average trailing PE is 20.8 and the 20-year average is also higher at 18.8 times.) The current 12-month forward PE is 17.3 times and already below the long term average of 17.8 X. In summary, as the equity market retests its recent low, it is also defining good long-term value.



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