

Watch the Banks

Hi Everyone,

The 2007 market decline began during Halloween week. It began with the comments made by Meredith Whitney, then a relatively unknown analyst at CIBC Oppenheimer.

First the market slid and then it really blew up over the fear of a financial meltdown. We had that meltdown, and then it was countered by the actions of the Fed and Uncle Sam.

The current rally began in March of this year in a misguided reaction to the some what skewed stress tests and the pending changes in accounting rules to enable banks to make their books appear better than they probably were. Then the rally petered out, the Dow slid 10%, technical analysts were pounding the table about how we are going to retest the lows, and Meredith Whitney spoke once more.

What she said was that Goldman Sachs would beat Wall Street's earnings forecast, and that many other banks would do fine during the rest of the year. But, she went on to say that there would be problems in 2010, as earnings and asset deterioration became prominent again, thanks, in part, to the unemployment she saw rising to 13%.

The market decided to be selective and listened to the first part of Whitney's comment, but not the second -- ergo, the current sharp pop up in financial stocks lifting the entire market with them.

So, what's the moral of this story?

Going forward, we need to continue to watch the banks to determine the direction of the overall market. I'm not a market timer, I stick to fundamentals, but all of us in some ways and to some extent time the market as we make buy and sell decisions.

The point to take away from this discussion is: When the banks begin to roll over, they will take the market with them.

SHORT-TERM MARKET OUTLOOK

The market's bias to the upside may appear to be running out of steam, **but it is not**. It's struggling on light volume to punch through a very tough technical ceiling. If that doesn't happen then the S&P 500 could start a slow and steady descent. If it does punch through the S&P **could rise another 10%-15%**.

A great many professional money managers have only dabbled in this trading rally and they're bound to be getting itchy. I believe they're increasingly taking a bullish view of the market and getting more involved.

Further, the charts, volume (and my gut) tell me that the market will continue up slowly in August and spike after Labor Day. Then we'll enter the perilous month of October.

CONCLUSION

I would urge everyone to be slower to leap to conclusion that all is well and be more open-minded about the potential economic and financial road maps, keeping in mind the forces at work in the background.

For the short term we will continue to trade a market that wants to go up. While keeping a wary eye on bank performance and how Wall Street views that performance. Ultimately, as the banks go so goes the market.

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