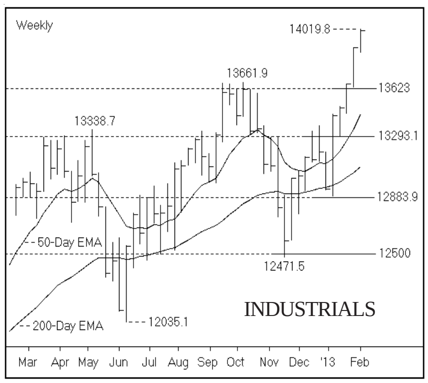
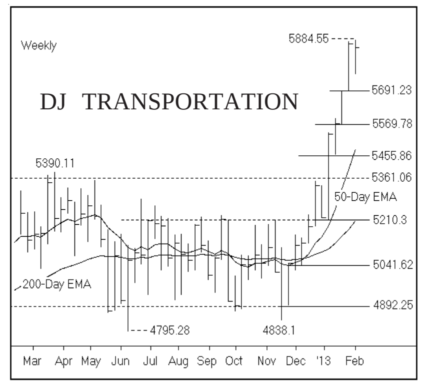
The KonLin Letter[TKL]

TECHNICAL REVIEW

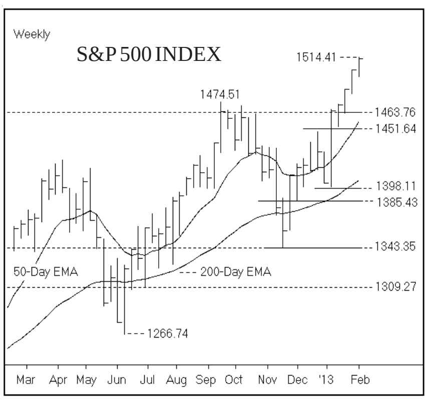
February 2013

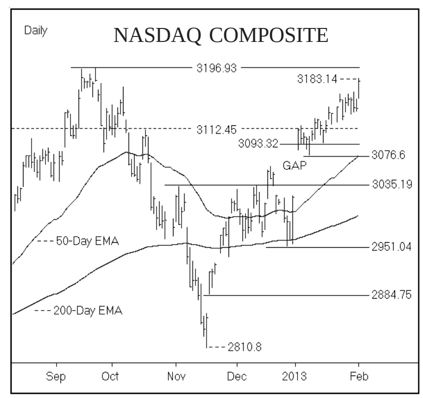
(continued from page 1) While the **U.S. ISM MANUFACTURING INDEX** rose to 53.1 in Jan., the **PHILLY FED MANUFACTURING INDEX** *contracted* to a -5.8. In addition, the **NY EMPIRE STATE MANUFACTURING INDEX** dropped further to a -7.78, making it six consecutive months of a *deepening* contraction. The nation's **MANUFACTURING SECTOR,** which makes up about 12% of the **ECONOMY** and nearly 6% of **NEW YORK'S,** is not firing on all eight cylinders. **OBAMANOMICS**—slow to *non-existent* **GROWTH**—is responsible for the **ECONOMY** consistently *underperforming* expectations. It's **SOCIALISM** at its best! **NEW HOME SALES** *plunged* 7.3% in Dec., but still *surged* 20% last year from its'11 record low. After 48-mos. of **DEPRESSION,** the **HOUSING INDUSTRY** appears to be turning the corner, but even with **HOME PRICES** up, *anemic sales* will not provide the *robust* **STIMULUS** of the past. Not until the **FORECLOSURE** problem is completely dealt with can we have a *sustained uptrend* in the **HOUSING SECTOR.** However, the recovery in **HOME PRICES** increases the household "*wealth effect.*" The psychological lift from *wealth creation* is the catalyst for **CONSUMER SPENDING,** causing investors who remained on the sidelines with an *abundance of cash* to jump back into the **MARKET** in *fear* of missing a **NEW BULL MARKET. STOCK MUTUAL FUNDS** saw $6.8 bil. pour into **FUNDS** during the first 3-wks. of '13 after an *exodus* of $287 bil. from the start of '09 to the end of '12.



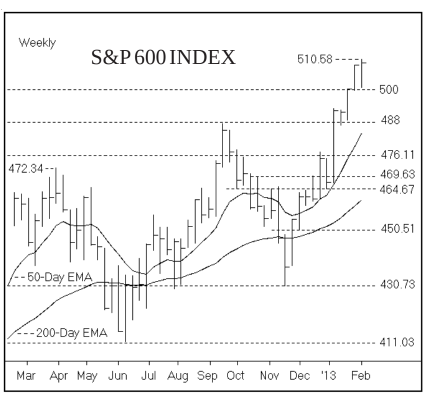


Look at the *shaded* area of last month's *long-term* monthly charts after *failing* at 14000 in '07, the **DJIA** is punching up through *long-term overhead resistance* and must close above 14198.1. All support levels for the **INDEXES** are indicated on their respective charts, with the **50** and **200-DAY EMAs** also adding to support. The **S&P 500** is *lagging* while the **DJTA** (more economically sensitive) clearly *smashed* through significant *overhead resistance,* eclipsing its'07 peak, normally a **BULLISH** sign for the market. If the **DJIA** can *exceed* its'07 peak, it would be further confirmation that the **STOCK MARKET** is headed higher. However, the **NASDAQ COMPOSITE** is the only **MAJOR INDEX** yet to exceed its Sept.'12 peak, which is a *short-term* **NEGATIVE DIVERGENCE**. In fact, it's been lagging the *broader* **MARKET** for over 5-mos. *signaling caution,* but I believe it will break above the 3196.93 level and join the rest of the **MAJOR INDEXES.** For the most part, **DIVERGENCES** over time work themselves out for the better.





The **S&P MID-CAP 400**, **S&P 600 SMALL-CAP's** and **RUSSELL 2000** all made significant *new all-time highs,* and together with the **DJTA,** continue a leadership role, a **BULLISH** sign for the **MARKET** as a whole. The **STOCK MARKET'S** *explosive rally* since mid.-Nov., from *peak-to-trough,* saw both the **DJIA** and **S&P 500** *surge* 12%, the **S&P 600** up a *stunning* 18% and the **TRANSPORTS** up a *whopping* 21%. These are *huge* moves in a short time and justify a corrective period. Nevertheless, while stocks remain in an *uptrend,* **MOMENTUM** has *slowed,* which is not uncommon after a *sharp* up-leg. Many **INDEXES** and **STOCKS** are showing *indecision* through Japanese **CANDLESTICK ANALYSIS** that usually foreshadows a *short-term reversal.* And when 80% of stocks are above their **50-DAY MA** (currently at 90% after hitting 93.4%), the light is flashing red. Likewise, with the **200-DAY MA** at 88.6% and trading at 29% above its **200-DAY LINE,** the caution bells are ringing loud and clear. This does not mean that the market is going to crash. Between now and May the **TAX** and **CUT** battle will cause increased **VOLATILITY.** In fact, the **DEFICIT** will *surge* again instead of declining. With the first two months of Washington's FY'13 reported, the **DEFICIT** is on track for $1.7 tril. If the White House doesn't get their act together and stop their *reckless* **SPENDING,** the **BOND VIGILANTES** will send **INTEREST RATES** *surprisingly higher.*



Actually, **TREASURY YIELDS** are *smashing* through *overhead resistance* levels *reversing* long-term downtrends. Last year, **TKL** *alerted* you about the **10-YR TREASURY YIELD** *breaking out* and for the first time last month cleared 2% not seen since Apr.'11. Remember, *strength* in **TREASURY YIELDS** is **BULLISH** for stocks because **BOND TRADERS** *expect* a growing **ECONOMY.** Even with the *contraction* in **Q4 GDP, TREASURY YIELD** *ignored* the **GDP** report and moved higher *signaling* **TREASURY BONDS** will move lower. If it was a *false breakout,* we will know soon enough as the **BOND YIELD** will *sink* into the 1.5% area, which will indicate further **ECONOMIC CONTRACTION** and the **STOCK MARKET** plummeting. The **MIGHTY GREENBACK** is threatening to drop below its 4-mos. lows, which will be *short-term* **BEARISH**. Most of the **$** *weakness* comes from **EUROPEAN CURRENCIES** with the **EURO** most *influential* surging to its highest level in a year. Also, Japan's aggressive **QE** program to *induce* **INFLATION** to *combat* **DEFLATION** that has gripped their **ECONOMY** for nearly 20-yrs. causing the **YEN** to *plunge* has kept the **$** from weakening further and sooner.