

>: Should You Be Buying Banks Right Now?

Thursday, June 18, 2009 / Bob De Dea

Progress in the Financial Services Industry

Item 1:

On June 10, the Treasury Department announced that 10 large banks could start repaying their Troubled Asset Relief Program (TARP) loans -- \$68 billion worth.

Here was the reaction on Wall Street: <Yawn>.

Financial stocks lumbered along with little change. Those who said they'd repay the government's TARP funds saw their share prices decline since the announcement, including **U.S. Bancorp**(down from \$18.10 to \$17.86 as of June 17), **American Express**(\$26.69 to \$24.69), **BB&T** (\$22.21 to \$22.23) and **Morgan Stanley**(\$29.26 to \$28.10).

Other banks are still holding billions in government goodwill (er, I mean *equity*), including **Bank of America** (share-price movement over the same period: \$11.98 with a big bump to \$13.72 on the 12th, then down to \$12.73), **Citigroup**(\$3.48 to \$3.45) and **Wells Fargo** (\$24.91 to \$24.40).

Item 2:

This week, President Obama revealed his plan to reshape regulation of the financial industry. He proposed that the Federal Reserve act as "overlord" of large financial institutions to ensure higher capital standards and closer scrutiny of their practices.

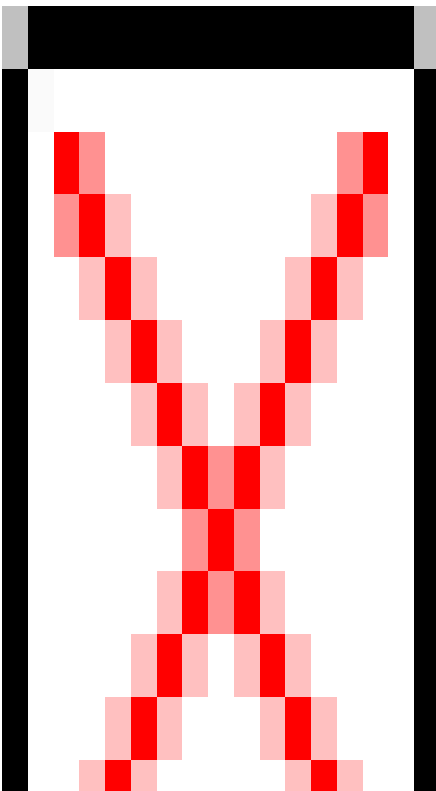
(Aside: If an institution, financial or otherwise, by its collapse poses a risk to the entire system, and is therefore deemed *too big to fail*, then in my opinion *it's just too big!* That's what the anti-trust laws -- still on the books but not widely enforced since Ronald Reagan's tenure in Washington -- are for.)

Also, the plan sets up a new "national bank supervisor" under the auspices of the Treasury Department, and a Consumer Financial Protection Agency that, among other things, will evaluate mortgage products and improve home loan disclosure rules.

Do all these significant developments signal that it's time to add bank stocks back into your portfolio?

Before I answer that question, let's examine some compelling information that helps me make decisions about where to allocate my investment dollars.

Sector Hunter to the Rescue



aren't familiar with *Sector Hunter*

, the percentage refers to the reading of a sector's Bullish Percent Index chart. For more about Point & Figure charting and the BPI, read my three-part series [starting here.](#))

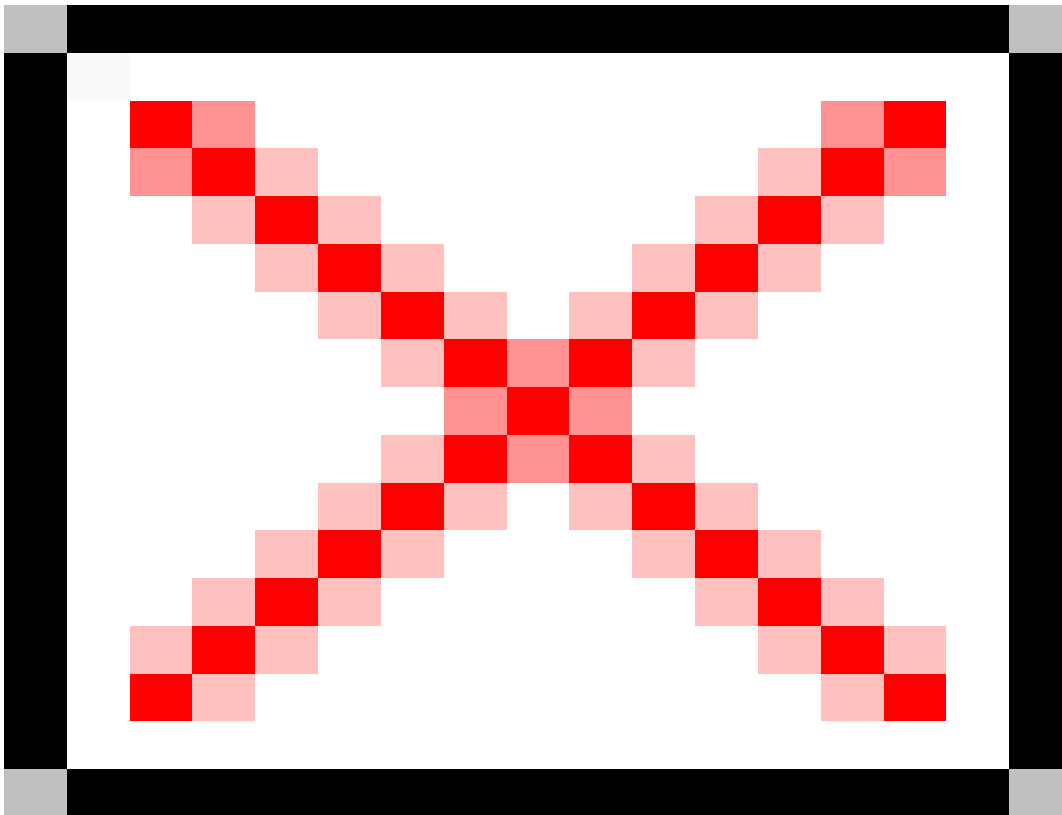
Now, in the past, I've cautioned against the 30% alerts, since the market has been so extreme this year. I liked playing the 70% sell signals (and *Sector Hunter* just put in two of them on Tuesday and one on Wednesday; guess who's got open positions).

What's interesting here is that the sector has been on a **Relative Strength Sell Signal** since the July 14, 2008, alert at the bottom of the above list. (A Relative Strength sell signal is issued automatically by *Sector Hunter*, following a proprietary set of criteria.) This was followed by a **Rotation Alert** issued on March 4, when the 10% buy signal came out.

However, the sector's relative strength *did not* shift to a buy signal. In fact, a Relative Strength sell signal alert came out the very same day, which cautions us to treat the position as a trade.

In other words, even at the bottom of the BPI (below 10%, typically a prime time to buy into a sector), the sector was on a Relative Strength *sell* signal. You don't want to go long against a measurement as important as Relative Strength. Therefore, any positions taken in a security in the bank sector are best treated as short-term trades.

It turns out, if you'd bought at the March 4 alert, you'd have done well. Here's the bank sector's BPI as of today. (The chart is dated June 10 but the information hasn't changed):



We can see that, if you'd missed the 10% signal and played the 30% signal (on March 19), you'd still have made some money. (Caveat: The alternative securities listed in the 10% and 30% alerts were different, except for two Exchange-Traded Funds.)

I've highlighted the bottom support level and the resistance levels. Notice that the current 58% reading is at the last point of resistance. (The next resistance level is around 66%, from August 2005 to May 2006.)

If I were deciding whether or not to buy in now, and if I were looking only at the BPI, I would wait until that resistance was broken and the BPI shot higher. I would give up a little profit for the sake of a bit more certainty. I would also keep tight stop losses and cash out when I felt the profit was sufficient, *because* (as I explained above) *the sector's still on a Relative Strength sell signal.*

Technical Analysis Sheds Some Light

Now, for something completely different, let's look at a weekly line chart of the BPI over the last 10 years:

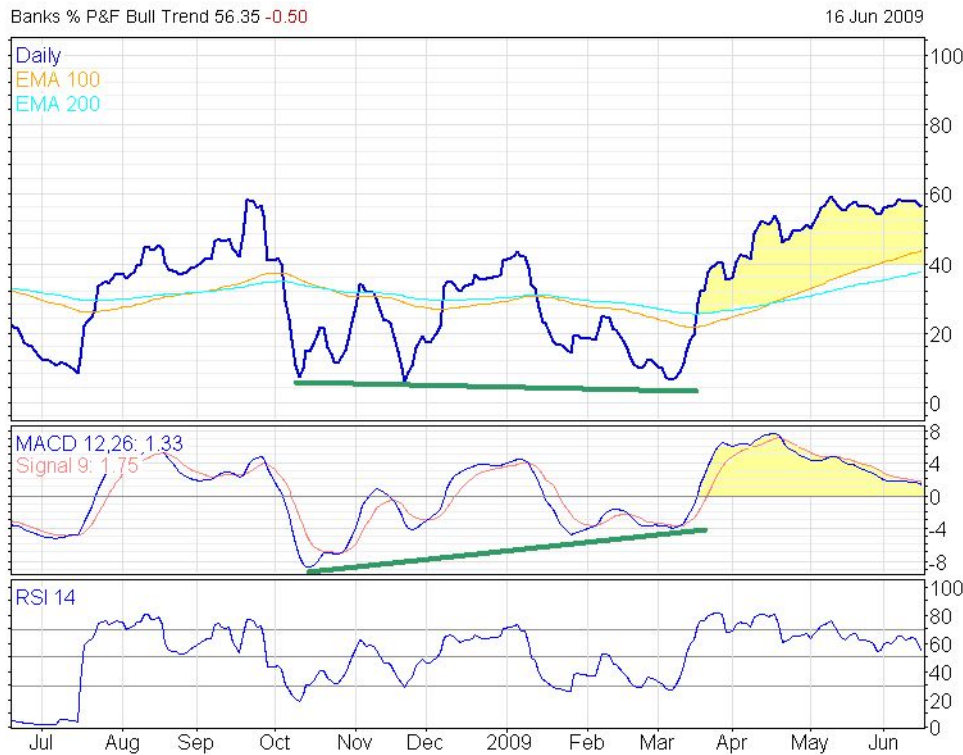
RSI breaks from below 50 to above 50 and stays there.) The past two periods are labeled "July 18 - Sept. 19" (2008), and "Dec. 12 - Jan. 9" -- spans of two months and one month, respectively.

The current period, since March 20, is shaded in yellow. This three-month period is the longest run above these moving averages since the five-month period between Oct. 8, 2004, to March 4, 2005.

The difference, however, is the sheer *pitch* of the recent angle upward, and the fact that the MACD has started a downward trend (paralleled by the RSI). Now the MACD *could* bounce, but I wouldn't hold my breath for that.

Having said that, there is a positive divergence in the MACD.

Let's zoom in:



Looking at the yearly picture gives us more clarity. The difference between the BPI and the MACD is a little less drastic from this perspective. (I'd still keep my eyes peeled for a MACD crossover to below zero. And an RSI crossover to below 50.)

So ... "Should You Buying Banks Right Now?"

For me, banks are still the unwanted child of the stock market. Until the credit crisis resolves itself, and until the sector BPI shows that it can break through resistance at 58% (and doesn't get stuck at the 66% resistance level), will you find me investing in this sector on the long side?

I wouldn't bank on it.

P.S. This article was written on Wednesday, June 17. At the end of that day, the NYSE BPI changed to a column of O's. Also, both the NYSE BPI for the percentage of stocks above the 10-week moving average and the percentage above the 30-week moving average moved to a column of X's. Those of you who've been reading The Tycoon Report for a while know that this 7% move in the NYSE BPI signals a significant change toward a bear market. One more reason *not* to be investing in financial stocks right now!

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