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## Is It Safe?

Posted by David Gaffen



Is it safe? (Source: Paramount)

Like **Laurence Olivier's sadistic dentist in Marathon Man**, it's a question on the minds of many, particularly those looking at the big financial stocks and seeing their declining price-to-earnings ratios and book valuations to levels that would **normally be considered attractive**.

The patterns witnessed throughout most of the year in the homebuilding stocks — a steady downward trend punctuated by brief spurts of buying from hopeful souls attempting to predict the bottoming-out in those stocks — **appears to be taking root in the financial names now**. Buying interest surfaced in those shares in late September and early October, as some, comforted by the rebound in various indicators of credit-market stress, believed the worries overdone.

That proved folly as banks and brokerages have struggled ever since — **but before long, optimistic types will likely try again, basing their bullishness on a variety of factors**, be they fundamental, technical, or emotional. “The natural inclination is to try to catch falling javelins,” says Bill Greiner, chief investment officer at UMB Asset Management in Kansas City. “But that’s a strategy that doesn’t make sense at this stage.”

So, what are investors looking at? Here are a few facets of the financial sector's turmoil that some are trying to use as gauges to sound the all-clear signal:

- **Valuations: Citigroup**

now sports a price-to-earnings ratio of 8.85, while **Morgan Stanley's** sits at



Is it time to buy, or time to die? (S

6.58. Peruse any group of analyst reports these days, and you'll find those that talk about attractive valuations and book values right now. However, says Mr. Greiner, but **“it's hard to analyze them for what they're truly worth right now.”**

- **More writedowns.** This is perhaps the most nebulous aspect. Some are calling for \$100 billion in writedowns, but are they sitting around with a spreadsheet adding them up? Investors thought they had achieved clarity a handful of weeks ago, but they hadn't. **The crack-up of Merrill Lynch** and Citi has resulted in a further pullback in these shares, but other investment banks remain tight-lipped. And after that, it's not as if these writedowns mean companies resume their pre-blowup rate of revenue growth.
- **Analyst sentiment.** In some ways, says Chris Johnson of Johnson Research Group, the time to buy is when analysts finally give in and lower ratings en masse. This downgrade brigade has occurred in fits and starts, with a few more today as Wachovia lowered its rating on **Goldman Sachs** and Goldman lowered the securities sector. **“It was only a little over a month ago you saw an upgrade in the sector,” Mr. Johnson says. “That captures the attitude that's been out there.”**
- **Scalps:** It may seem strange, but part of the way one can tell excess in a sector has been cleaned out is **through pink slips to top brass**. This one is actually taking place —



Charles Prince of Citigroup and Stan O'Neal of Merrill Lynch have both been tossed — but it remains to be seen whether other head honchos will find themselves out of work before long.

- **Dip-Buying Evaporates:** Mr. Johnson notes that homebuilders seemed to consistently draw buyers on each 3% to 4% decline, which didn't prove fruitful to anyone but the most nimble of traders. **Once investors here start to figure that out, perhaps that's a signal.**



In any event, predicting the end of a bear run in a sector is not easy — it's often longer than many believe. “The amount of debt that was created and the amount of garbage floating around **attacks the very fabric of our economy and our banking system**,” writes Bennet Sedacca of Atlantic Advisors, on Minyanville.com. **“Can we reflate our way out of it? Doubtful.”**

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