**TABELL'S MARKET LETTER**

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Market action this week followed a familiar pattern. Prior to a Thursday pullback, the Dow Jones Industrial Average, on October 30, posted a new all-time high at 1375.57, bettering the 1369.29 peak it had scored a week and a half before, on October 17.

At the time of the mid-October high it was widely remarked, both here and elsewhere, that the performances of the Dow and the broader-based indices had been quite different. A day prior to the Dow's high, the S & P 500, for example, had reached 187.98. This left it almost 4% below its July top of 195.65. The difference is beginning to be erased. The market's second short-term upside thrust this week saw the S & P advance to 190.07, closer to although still a fair amount away from its all-time high of last summer.

Interestingly, the original reason for the dichotomy was removed, on Wednesday, in action taken by Dow-Jones itself. That reason had been the action of General Foods which, in the wake of the announcement of its takeover by Philip Morris, had moved recently some 48% above its mid-July level. This week its acquirer, Philip Morris, was substituted for it in the DJIA.

In an era when cigarettes are being equated with original sin, it would have been inappropriate to have two tobacco stocks in the Dow, and American Brands, therefore, was duly removed. We consulted with Dow-Jones prior to the changes, and AMB's successor, McDonalds Corp. appears to us to make eminent good sense. It was, indeed, one of the issues mentioned in this space as a potential Dow replacement on the occasion of the 100th birthday of the Industrial Average in July, 1984.

This issue having been disposed of, it is our own feeling that the S & P 500 will shortly follow the Dow into new high territory. The broader index's move to 190 this week constitutes an upside breakout from what looks like a head-and-shoulders base formation, with an objective around the 200 level, comfortably above its all-time high figure of last July. Whether or not the S & P will again begin consistently outperforming the Dow, however, is more of an open question. If we assume that the latter averages superior performance is going to continue over the intermediate term, it is necessary to examine the implications, if any, of such action.

A number of commentators, referring to the phenomenon of the DJIA's leading the S & P on the upside, had called it a "divergence". We cannot quarrel with this as English usage, since it is possible for any two numerical series to diverge, and the two averages have, in fact, done so. It should, however, be noted that, within the professional community of technicians, the term divergence is generally taken to mean diverging action between the Dow and measures of market breadth, not other indices such as the S & P 500. Such a condition exists at the moment, will probably continue to exist, and the ramifications of this divergence have been discussed at length in this space. The condition, as we have noted, suggests a market peak likely to be scored at some point in the future, although not necessarily over the short term, since the historic lead time of breadth over the Dow at market peaks tends to be significant. It is this lead time that makes breadth analysis useful. By contrast, however, inferior action on the part of the S & P 500 is of questionable usefulness as a market predictor.

The mistaken impression that superior performance by broad-based indicators is bullish may arise from the fact that such action, with some frequency, has often begun manifesting itself somewhere in the fairly early stages of major upswings. For example, the 500 began to outperform the Dow in late 1982, a few months after the August, 1982 bottom. Although the market had already moved up significantly by that time, the outperformance continued through the fall of 1983 as did the market rise. Superior S & P action reasserted itself in the spring of 1984, shortly before the intermediate-term bottom in July and continued until this summer. A period of Dow outperformance began last May.

The trouble with prior periods similar to May to date is that they have been initiated at widely different points in various market cycles. Occasionally they have occurred well after peaks, and, with equal frequency, they have taken place too far ahead of important highs to be of any use. Reference to divergence, in other words, is best restricted to the classic technician's usage, comparing the Dow with market breadth and not with broad-based indicators.

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| Dow-Jones Industrials (12:00 p.m.) | 1383.14 |
| S & P Composite (12:00 p.m.) | 189.77 |
| Cumulative Index (10/31/85) | 2444.83 |