

Daily Market Notes**Market Update:****DJIA:** 10103**S&P 500:** 1099**Nasdaq:** 2175**10YR T-Note:** 3.39%**EUR/USD:** 1.495**Gold** 1056**Crude Oil:** 78.76

Despite oil prices rallying to a new high for the year on Friday, which is supposed to be good for stocks because it shows that there is “worldwide economic recovery” even though consumers suffer because it costs them more to fill their gas tanks and heat their homes, the stock market did what it usually does on an options expiration session – go down so that as many buyers of calls as possible can lose their money. We also noted that the largest semiconductor company, which everyone was raving about earlier in the week on its supposedly strong earnings report, actually ended up on Friday lower than it was before the ostensibly good numbers were released. Believe it or not, the same can be said for two other Dow stocks whose numbers got the market excited last week to new yearly highs but whose stocks fell below where they were before their strong reports were released as well – the large aluminum manufacturer and a very prominent financial company.

Prices Current as of
1:58 PMSource: *Bloomberg*

So what this might be showing is that the tremendous run up in equity prices might have already discounted the good earnings that are now coming out after the stock prices have gained so much. This might be a limiting factor to the kind of advances we have seen this year, especially as the VIX keeps declining to new yearly lows day after day. In fact, not counting today, the VIX has declined for 10 straight days to its lowest level in 13 months. And if stocks end the day higher the VIX will have dropped for 11 days in a row.

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Friday saw the market go lower, aside from the dynamics of the October options expiration as mentioned in the first paragraph, because of poor reports from two financial giants and Dow components – another large diversified banking institution and a large diversified technology, media and financial services company - and from another Dow giant – the giant provider of computer solutions through the use of advanced information technology, which kept things under pressure all session. Not even a very strong performance from the largest search engine giant could stem the overall downward pressure on stocks, as the Dow closed slightly below the magic 10,000 number after two closes over that level on Wednesday and Thursday.

After the weakness on Friday, the market is starting out the new week with a strong

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move to the upside, on no news, just a continuation of the bullish perceptions that arise when the dollar continues to decline, oil moves to new highs and gold prices maintain themselves over \$1,050. The ostensible reason for this ongoing optimism is that the earnings reports to be released this week will come in better than expectations, as 34 of the 41 S&P 500 companies that have reported so far, or 83%, have beaten expectations. More than 130 S&P companies will be reporting this week, and we have listed the more important ones below

As this is being written, the Dow has now gained around +100 points after starting out just a bit higher. Financial stocks, which started out lower, are now nominally higher after the New York Fed said that it is working on what are called reverse repurchase agreements, which are ways of draining reserves from the system. It is a de facto way of tightening which means that the financial markets are functioning better. Of course, one would like to think that such an operation would be supportive to the dollar, but it keeps going on its merry way lower on the “good news is bad news for the dollar” syndrome, or the lessening of risk-aversion out of the supposed safe haven of the dollar into more risky assets like higher yielding currencies and stocks themselves.

With the VIX close to 21, it is difficult to now make new projections as to how high the market can go, but it would appear that major support should come in at the under 19 level, which was the low back in August of 2008 before things collapsed, so this means that the Dow could still rise another 230 points or so from current levels before a new overbought situation would occur. This assumes that the market will get this high in the first place, although it is obvious that declines so far have been contained after relatively small percentage losses, as there has not been a correction of as much as -10% since the bullish move began more than seven months ago. So the earnings picture starting this evening, with AAPL and TXN reporting, should do a lot to give the direction for the remainder of the week.

The earnings parade unfolds this week with – tonight: AAPL, TXN; Tuesday: BK, CAT, DD, ISRG, JEF, PFE, STT, KO, UTX, YHOO; Wednesday: AMGN, EBAY, LLY,

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GENZ, BA, WFC; Thursday: 3M, T, BMY, CME, EMC, JNPR, LH, MCD, MRK, PM, POT, UPS, XRX; Friday: HON, MSFT, SLB.

So we have 10 Dow companies reporting, in addition to the all-important AAPL. And just like last week, there will be much excitement because of these reports.

This week also has economic reports, and they are: Tuesday: September P.P.I., September housing starts; Thursday: September L.E.I.; Friday: September existing home sales. It would appear that they will take a back seat to the earnings numbers.

Of all the companies that have reported earnings for the third-quarter so far, 82% of them have beaten their estimates, compared to 72% for the second quarter, so this is encouraging.

It should also be pointed out that when the S&P has been 20% above its 200-day moving average, as it was only in 1932, 1938, 1975, 1985 and 1986, and as it was recently, the market underwent an average decline of -12% over the next three months before being higher by +13% a year later.

During the second quarter, stocks in the S&P 500 reported profit declines of -29%. This is after a first quarter decline of -33%. The projection is for a -23% decline in the third quarter, before a rousing gain of +63% for the fourth quarter, when the comparisons to the fourth quarter of 2008 should be somewhat easy to overcome. The only problem with this projected gain is that the bulk of it is supposed to come from financials, because the comparisons to the disastrous 4Q of 2008 should allow for good upside. For 2010, earnings are projected to increase by +26%, followed by earnings increases of +22% in 2011.

We have now seen eight straight quarters of profit declines for companies in the S&P 500, starting with the last two quarters of 2007, all four quarters of 2008 and the first two quarters of 2009. Earnings have never been down for eight

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Earnings have never been down for eight consecutive quarters. If earnings do come in lower for the third quarter of 2009, this will be the first time ever that there have been nine consecutive quarterly profit declines.

We now have four consecutive quarters of negative G.D.P. growth which started in the third-quarter of 2008, and has now extended through the first two quarters of 2009. Projections for the third quarter are for growth in the +2 to 3% range. This is the first time that there have been four straight quarters of negative growth since records have been kept since 1947.

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Disclosures

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