

Daily Market Notes

Market Update: Building on the strong gains of last week, the market started out this week with a very strong upside burst yesterday, which resulted in the best three day market performance since July 15-17th. What made the gains more astounding was that it was the second day out of the past three that the Dow advanced by +203 points, and it did this last Thursday as well, the day before the jobs report as well.

DJIA: 10210
S&P 500: 1089
Nasdaq: 2145

10YR T-Note: 3.49%
EUR/USD: 1.496
Gold 1102
Crude Oil: 78.17

As was discussed in yesterday's notes, the statement out of the G20 meeting that they will keep stimulus in place worldwide was the primary upside motivating factor, which means that interest rates are going to stay low in the U.S. and around the world for a long time, the dollar will continue to stay weak and so gold and other commodities raced higher because of this. If this is a formula for continued stock market gains, namely a weak dollar and higher inflationary items like gold and crude oil, then it would seem that equities cannot continue to thrive with these dynamics at work. This does not mean that stocks cannot continue going higher, but it would appear that the grind is going to get more difficult as the higher levels are attained.

Prices Current as of
1:42 PM
Source: Bloomberg

Donald M. Selkin
 Chief Market Strategist
 (212) 417-8017
dselkin@nationalsecurities.com

It was interesting that on Friday, when the Dow was up only +17 points, the VIX declined by a much greater what was to be expected amount of -1.24 points. However, the relationship normalized itself because with yesterday's Dow gain of +203, the VIX declined by a smaller than normal -1.04, which meant that for the two days, the Dow was ahead by +220 while the VIX was down by -2.28 points, an almost perfect configuration for the 100/ -1 Dow/VIX relationship.

Jason Wotman
 Research Analyst
 (212) 417-8264
jwotman@nationalsecurities.com

The financial stocks, which have lagged badly lately, finally got their act together yesterday, with nice gains from the Dow banking and insurance components. Apparently the Federal Reserve said that those banks deemed short of capital in May have raised their reserves enough to withstand the risk of slower economic growth. These gains along with continued strength from the large Nasdaq technology leaders assured that things would be firing on all upside cylinders.

With earnings season winding down, of the 430 S&P companies that have reported, 83% of them have beaten the analysts estimates, which would be the most ever, and

Daily Market Notes

this has certainly been one of the factors accounting for the upside surge of the last six days after the market underwent a two-week correction of -5.4%.

After six straight days of gains by the S&P, things are cooling off a bit today, as a poor Nasdaq/Dow ratio, which saw the Dow be up by +34 points at its best level while the Nasdaq was only up nominally, has led to modest declines in all of the major averages as this is being written. And apparently these declines are being attributed to the fact that the dollar, heaven forbid, is actually strengthening a bit as the Euro seems to be having difficulties maintaining itself over 1.50, although on the other hand it does not really weaken too much from these levels either. And oil prices, which are trying to get closer to where they should be in terms of supply and demand instead of being maneuvered higher like a currency, are also lower, heaven forbid as well. And apparently this is also bearish for stocks when inflationary indicators trend favorably. As we have mentioned many times, perhaps the real reason for stocks being down a bit is that they cannot continue to advance when these outside markets constantly go higher, instead of these higher outside markets supposedly being bullish for stocks.

Along these lines, it is interesting to read the explanations for today's modest setback from market observers. They first say that lower stocks are lessening the demand for riskier assets like non – U.S. currencies. Then the next one says that a stronger dollar is lessening demand for stocks! So you really cannot have it both ways, as these sorts of explanations have been prevalent for almost the entire bullish move we have had in stocks for the past eight months, but the rationale for these types of explanations gets twisted in terms of which item is leading, and which one is following? Are stocks leading the outside markets of Euros, gold and oil, or are the outside markets leading stocks?

Perhaps a better explanation is that the economic recovery must show more consistency in order to propel stocks higher, not what the price of oil is doing or not doing on a day to day basis. And as we said in yesterday's notes, all of those Hurricane Ida explanations for oil's supposed price rise went out the widow fast

Daily Market Notes

today, as oil is dropping despite oil companies taking advantage of this situation by “removing non-essential personnel”, etc. which become basically self-serving statements in order to get the price higher.

There is no doubt that the weaker dollar has helped the prospects of certain companies, as those which generate more than half of their revenue abroad have beaten those doing business only in the U.S. by 27%. This proves that the falling dollar makes American goods more competitive overseas and boosts revenue when foreign currencies are repatriated back to the U.S.

And the best thing that can happen today is that the market finishes somewhat higher even though the Euro and oil prices stay lower. This would show that there are other reasons why stocks go up without the outside push of these other markets.

The earnings season is winding down, with over 430 of the 500 S&P companies having already reported, but there are some important ones next week and here is the lineup – tomorrow: AMAT, DNDN, M; Thursday: ATK, KSS, JWN, URBN, Dow components DIS and WMT; Friday: ANF, A, JCP. One can see that the list is heavily weighted with retailers, which always report late in the earning season.

This week’s economic numbers are on the light side, and this is a relief after all of the drama of the Fed statement and the jobs report this week – Friday: September trade balance and U. of Michigan mid-November Consumer confidence Survey.

Of the 430 S&P companies that have reported so far for the third quarter, 83% of them have beaten the estimates, and this will be a record high for any one quarter.

So far in the third quarter, profits are down -15%. During the second quarter, profits declines for stocks in the S&P 500 were -29%. This is after a first quarter decline of -33%. According to the analysts, the expectation is for 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. According to the analysts, for 2010, earnings are projected to increase by +26%, followed by earnings increases

Daily Market Notes

bulk of it is supposed to come from financials, because the comparisons to the disastrous 4Q of 2008 should allow for good upside. According to the analysts, 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. According to Bloomberg Financial, 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 currently for growth in the +3.5% range. This is the first time that there have been four straight quarters of negative growth since records have been kept since 1947.

Daily Market Notes

Disclosures

Don Selkin is the Chief Market Strategist at National Securities Corporation, member FINRA/SIPC, (NSC) and provides the Fair Value analysis for CNBC each morning. The commentary provided in this Market Letter is intended to provide our customers with timely market analysis and should not be considered a research report. This Market Letter may contain, and is limited to: Discussions of broad based indices; Commentaries on economic, political or market conditions; Technical analyses concerning the demand and supply for a sector, index or industry based in trading volume and price; Statistical summaries of multiple companies' financial data, including listings of current ratings; and, Recommendations regarding increasing or decreasing holdings in particular industries or securities. This Market Letter does not make a financial or investment recommendation or otherwise promotes a product or service of the firm. This Market Letter contains only news, facts, and commentary on information previously reported from a news source believed to be accurate and reliable by the author. These news sources include the following: {Bloomberg Financial, Reuters, Associated Press}. It is possible that at any given point in time, the author, NSC, or one or more of its employees or registered individuals associated with NSC, may hold a position, either long, or short, as well as options, bonds, or other instruments in the companies noted in this report. This Market Letter is intended strictly for current National Securities Corporation customers only.