

Daily Market Notes**Market Update:**

The market once again showed that post 3pm resiliency for the second day in a row yesterday. Remember that on Wednesday, in the last hour things rallied to close at their best levels of the day, and yesterday the same dynamic took place.

DJIA: 10275**S&P 500:** 1091**Nasdaq:** 2147**10YR T-Note:** 3.32%**EUR/USD:** 1.487**Gold** 1135**Crude Oil:** 77.48

For most of the day, the Dow was down in a range of between -30 to -40 points, and holding at those levels and not really getting any worse. Then with around one hour to go in the trading day, the major averages were able to cut their losses to nominal ones with the Dow ending with a loss of only -11 points, its first setback this week while the Nasdaq finished with a -10 point decline. It was this weakish Nasdaq/Dow ratio that was partly responsible for keeping things under pressure in the first place, as many of the outstanding technology performers took a minor day off for a change after many of them had made new highs for the year.

Prices Current as of
11:39 AM

Source: Bloomberg

This better performance of the larger stocks lately is illustrated by the fact that both the Dow and S&P are virtually at their highs for the year while the Russell 2000 Index is well off of its high, as investors rotate back into the bigger names. We have seen this in the past couple of days in particular, as those two old Dow warhorses, the largest software provider and the largest integrated oil company, have both attracted a lot of attention and recommendations lately, and once again today they were the two stocks that led the upward charge late in the session.

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They were joined by the financials, which have done better this week despite their being talked down by the widely quoted analyst on Monday. Since that time, they have proceeded to find their footing once again and were primarily responsible for the Dow not getting any worse than a -40 point loss. And they also contributed to the late upward charge as well, with a large Dow financial being the standout all day on a recommendation with a very high price target from a prominent hedge fund manager. The other financial components of the Dow also did their part to hold the fort even when the rest of the market was down, and improved as well as everything came back from their worst levels late in the day.

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The market was able to shrug off a poor October housing starts report, the worst one

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in six months, and a weaker building permits number as well. The latter is an indicator of future activity so this was not the kind of number one would have liked to see if you believe in a housing market recovery. The October C.P.I. number was basically a non-event. Of course the housing number assures that the Fed will be on hold for a very long time, as one of the governors said in a recent speech and we mentioned the contents of it yesterday as well, namely that he believes that rates might not increase until 2012. This presents the Fed with a very difficult choice of how to prevent inflation from creeping higher as the dollar will not be able to really gather any upside momentum if interest rates are going to stay at these record low levels for at least another 2 ½ years. This could present them with real policy dilemmas going forward.

An interesting dynamic yesterday was the fact that the VIX declined as did the Dow as well. This is not what one wants to see, but the best explanation for this is that since we are in the options expirations week and there will be many puts going out worthless, perhaps more than usual because so many stocks and indexes themselves are virtually at their highs for the year, what we probably saw was investors selling out of these soon to be worthless puts and calls in order to salvage any kind of money out of them before they go out at zero on Friday. This happens quite often during expiration weeks and it is certain that this situation will soon correct itself when we will have a day when the averages are higher and the VIX does not decline as much as the averages go up in order to correct the imbalance that resulted from today's dynamic between the two items. Or we could have a down day where the VIX goes up more than the market goes down.

Today we are getting the latter of the two scenarios, as the market is declining big-time in early trading, but the VIX is up much more than the Dow is down, currently at -160 and up +2.50 respectively. So this corrects the strange imbalance from yesterday, and let it be said once again that the worst possible scenario that one wants to see is a lower Dow and a lower VIX as well, which we got yesterday as explained above, and perhaps a foreshadowing of today's poor market performance.

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Why the market is down today seems to be normal profit-taking ahead of tomorrow's options expiration, and as we always point out, the market almost always declines at this option expiration time in order to get as many calls as possible to expire worthless. We will go into this in more detail tomorrow, and point out the strike prices with the largest open interest that will be worth nothing by tomorrow afternoon.

Of course, there are the boiler-plate explanations for any triple-digit market decline, and the usual one is that the historic equity rally this year has "outpaced prospects for economic growth". Another explanation is that the rally which put the price/earnings ratio for the S&P to its highest level in over five years already reflects forecasts for a 25% increase in corporate earnings next year. So take your pick.

There were more specific reasons being put forward for the decline, and one is that there was a downgrade of the semiconductor stocks by a large house, and whatever happened to the supposedly wonderful vibes that were put out after the latest earnings report from the largest semiconductor manufacturer? The other reason offered for today's decline is that the health insurance stocks are getting sold off because the U.S. Senate finally finished their health care reform bill and are getting ready to vote on it this weekend.

And naturally, as equities decline, the Pied Pipers, otherwise known as crude oil, the Euro, copper and even almighty gold, are selling off in lockstep with the decline in equities, because now investors have, at least for today, become more "risk averse" after months of becoming less risk averse. So be it.

It is somewhat ironic that stocks are getting sold off to the extent that they are because the two economic reports today actually came in better than expected, with October L.E.I. rising to a two-year high and recording its seventh straight month of gains, and the November Philadelphia Fed Index also hitting a two year best level as well, as it rose for the fourth straight month.

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Third quarter results continue to come in better as the earnings season winds down this week. Around 80% of S&P companies have beaten the analyst's estimates, and this is the highest since records began being kept on this in 1993.

The earnings season is almost over, and this week once again the list is heavily weighted toward retailers, although there are a few technology type companies as well: tonight: DELL, DBRN, FL, GPS, INTU, PDCO, SCVL, ZUMZ; Friday: ANN, DHI, SJM.

So far in the third quarter, profits are down -15%, as 80% of the 440 S&P companies that have reported have beaten the estimates, which is a record. 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 of +22% in 2011.

We have now seen nine 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 three quarters of 2009. Earnings have never been down for nine consecutive quarters.

We have had four consecutive quarters of negative G.D.P. growth which started in the third-quarter of 2008, and extended through the first two quarters of 2009. Projections for the third quarter are currently for growth in the +3.5% range. According to Bloomberg Financial, 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

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.