

Daily Market Notes**Market Update:****DJIA:** 10016**S&P 500:** 1068**Nasdaq:** 2108**10YR T-Note:** 3.51%**EUR/USD:** 1.483**Gold** 1094**Crude Oil:** 77.14Prices Current as of
1:18 PM

Source: Bloomberg

The market action on three of the first four days this week was a perfect illustration of the importance of paying attention to the Nasdaq/Dow ratio on days when the Dow is advancing by triple digits. On Monday, Wednesday and yesterday, the Dow was up by around +150 points intraday. Yet on Monday and Wednesday, it failed to hold these levels and finished well below the highs. Yesterday, the Dow was not only able to hold this 150 point higher level, but was able to build on those gains to finish with an extremely strong closing advance of +204 points, its best showing since July 23rd. And as those who read these comments should be aware of by now, the reason for the failure to hold the best levels the first two times was that the Nasdaq/Dow ratio was poor on Monday and Wednesday, as the Nasdaq could only gain around +15 points the first two times, meaning that its advance was only around 10% of the Dow instead of the 20% needed to sustain an up-move of this magnitude. Yesterday the Nasdaq was the leader on the upside, as it was always ahead by more than 20% against the Dow. This is the reason that the market was not only able to maintain its advances all day, but finish with a spurt to the highs at the close.

Donald M. Selkin

Chief Market Strategist

(212) 417-8017

dselkin@nationalsecurities.com

Of course, this brings up another point that I have tried to get across, and that is the worst thing one wants to see is a major market advance heading into an important number, which of course is today's jobs report. This is a similar dynamic that we see when a stock rallies into its earnings and then even if the news is positive, it goes lower because the advance has already discounted the good news. In other words, the bar for continued market gains is very limited by an advance of the nature of what we saw yesterday, as it did not seem that the positive market inputs that were reported justified a 200 point Dow gain.

Jason Wotman

Research Analyst

(212) 417-8264

jwotman@nationalsecurities.com

The first positive input was that three important technology companies reported better results, which motivated the large technology leaders to do well also, and all of them had sold off somewhat during the market correction of the prior two weeks. Another positive was that the weekly jobless claims declined to their lowest level since January, which gave hope to the belief that the labor market was improving. Finally, third-quarter non-farm productivity rose by a very large +9.5%, and this was the largest increase in six years. But did all of this justify a gain of this magnitude,

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and this is where the potential problem lay for today's reaction to the jobs numbers. And even though the October numbers were in line with consensus at a loss of -190,000, which was the smallest since August 2008 and the prior two month losses were revised to show 91,000 fewer losses than had previously been reported, the bad news was that the unemployment rate went above the psychologically important 10% level to 10.2%, which is the highest since April 1983. This is now the 22nd straight month of job losses, which is the longest on record dating back 70 years.

The initial reaction to these numbers obviously concentrated on the unemployment number, but after an initial decline of -68 points and a poor advance/decline ratio, the averages battled their way back to gains of as much as +38 Dow points and a commensurate gain in the Nasdaq. Two large diversified financial Dow components got some brokerage upgrades, and this is helping the Dow to hold steady. Unfortunately, the strength in these two is not helping the other Dow financials, and this is acting as a deterrent to a better Dow advance and when things sell off, these are the downside leaders. But they have improved somewhat from their worst levels as the day is moving on. The Nasdaq is being supported to some extent by a new high in one of the major technology components, continuing to build on its strong earnings report, and a good performance by the largest Chinese internet company, which has breached the 400 level after a decline to 350 when its recent report was released. Breadth numbers have now improved to just about even. So it would appear as if the battle between small gains and somewhat larger losses will take place as the day moves on, but considering the extent of the gains during the first four days of the week, any Dow loss in the double digits would be quite acceptable.

The one troublesome thing here is that the VIX is losing ground relative to the Dow which means that the upside price targets now have to be lowered. For instance, even when the Dow was at its highest level the VIX was down by much more than it should have been, and when the market was lower so was the VIX, which is not a good combination either. So if the 20.10 VIX level is going to be the stopping point, then the market's upside potential has been reduced somewhat by this type of action. Of course, if we get another day like last Friday when the VIX explodes much more to

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the upside than it should, then this would create another bullish situation as what happened this week after that ridiculous VIX upside moon shot on that day.

And what is also encouraging is that the market was able to make a very strong gain yesterday and is holding its own today despite the fact that oil prices were down yesterday and are really getting sold off today, finally coming more in line with the supply/demand fundamentals instead of just blindly following the Euro either to the upside or downside, as gold has done lately, and gold has been in its own upside sort of unstoppable world recently as it makes new all-time highs close to \$1,100.

The earnings season is winding down, with about 400 of the 500 S&P companies having already reported, but there are some important ones next week and here is the lineup – Monday: DISH, ERTS, FLR, PCLN, ROK; Tuesday: BZH, BOBE, CYD, FOSL, WTW; Wednesday: AMAT, DNDN, M; Thursday: ATK, KSS, JWN, URBN, Dow component DIS; Friday: ANF, A, JCP. One can see that the list is heavily weighted with retailers, which always report late in the earning season.

Next 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 378 S&P companies that have reported so far for the third quarter, 84% 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 -18%. 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

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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 growth in the +2.7 to 3.2% 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

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.