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Daily Market Notes

Market Update:

DJIA:	**10281**
S&P 500:	**1092**
Nasdaq:	**2177**
10YR T-Note:	**3.37%**
EUR/USD:	**1.469**
Gold	**1142**
Crude Oil:	**72.80**

Prices Current as of 1:27 PM

Source: Bloomberg

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Just as on Friday we saw a classic case of the old "good news is bad news syndrome" after a very good jobs report, yesterday we saw how a poor Nasdaq/Dow ratio can prevent the market from holding onto its early gains.

In the morning, the Dow had advanced by as much as +54 points, but the Nasdaq was ahead by only +6 points, which is much less than the 20% needed by the Nasdaq for the market to go all the way on the upside. As things eased off of their early morning highs, by mid-day the Dow was ahead in the high 20's but the Nasdaq slipped into nominally negative territory. And one just knew what was going to happen next, namely a continued weakening, and sure enough the Dow ended with a nominal gain of one point while the Nasdaq ended down by -5 points, although breadth numbers were slightly positive due to a gain from the small-cap Russell 2000 Index.

Around this time, Chairman Bernanke delivered a speech in which he tried to dispel the foolish notion being circulated around the investment world that because Friday's jobs report was so much better than consensus that the Fed will be forced to push ahead its timing of an interest rate increase. This line of thinking had led to a tremendous strengthening of the dollar, and as a result, there was a sharp drop in commodity prices, particularly gold, which finally got its comeuppance, and also crude oil prices, which after many attempts to maneuver them higher, are finally reflecting a price more in line with the supply/demand fundamentals, which probably point to a price between $60 and $70 a barrel.

So what Bernanke did yesterday was to bring a touch of reality back by saying that the U.S. economy faces "formidable headwinds" and repeated the language of the last Fed statement in November that he foresaw an "extended period" of low rates and said inflation might subside while joblessness may fall at a pace that is "slower than we would like." If this is not a prescription for keeping interest rates at their current record low levels for a very long time, then I do not know what is. And of course the federal funds rate futures traders, who in their infinite wisdom pushed up the chances for a rate increase to as early as June 2010 after Friday's strong jobs report, started pushing it way back to very late in 2010 or even into 2011 once again. Initially stocks reacted positively to his comments, because let us remember that on Friday they had come off of their best levels because of the supposed fear of rate hikes. So now that Bernanke said that no rate hikes were in the offing, equities initially moved up again. But then investors said, wait a minute!, Bernanke's comments show that the economy is going to remain weak, so that is now negative for stocks.

So in other words, if the economy is showing signs of getting stronger as on Friday, this means that the Fed will have to raise rates, and this is negative for stocks, but if the Fed says that rates are going to stay at current record low levels, then this is also negative for stocks because then this shows that the economy is weak. What all of this means is that the predictions for a year-end rally, which was universally expected as most "experts" called for the major averages to end the year much higher than where they are now, are a bunch of nonsense. We have consistently pointed out that the Dow/VIX relationship was saying that the Dow's maximum upside objective is 10,600 while last week's four days in a row of intraday failures over 10,500 shows that the best we can hope for between now and the end of the year is a Dow between 10,500 to 10,600. Not that this is anything to be ashamed of, but rallies to above higher levels than these are simply not going to happen.

And sure enough, today's market is getting sold off to the downside, as a reduction in Greece's debt rating (remember last year the country of Iceland was the villain) and more problems in Dubai are giving investors more worry that global credit markets are not in the kind of shape that people thought that they were in. There was also bad news from two Dow components, with the large fast-food worldwide restaurant chain saying that global sales showed the smallest increase in five years in November and the large diversified manufacturing company forecast a profit that met analysts' expectations but said that an economic recovery is taking place "slowly". For its efforts, the stock is also being sold off. In addition, the nation's largest supermarket chain, made a profit warning. This is offsetting the fact that the large package and freight deliverer, whose activities reflect to some extent the overall condition of businesses, raised their profit forecast.

The VIX is rising by around the same amount that the Dow is falling, so the projected theoretical high on the Dow still remains the same as what was pointed out above. Otherwise it appears as if the negativity today is too great to inspire a move to positive territory so the best that we can hope for is that the Dow losses remain no worse than double-digit levels. The only positive sign is that the large technology stocks, which had been lagging lately, are showing some signs of life and that is helping the Nasdaq/Dow ratio to be decent on the way down, and this will hopefully prevent a complete meltdown.

After all of the drama caused by last week's economic reports, this week takes a bit of a breather in that regard, and the lineup is as follows: Thursday: October trade deficit; Friday: November retail sales, December mid-month U. of Michigan Consumer Confidence Survey;

As the third quarter earnings season is over, profits are down -14%, as 80% of the S&P companies did manage to beat 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.

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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 +2.8% 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.