

Daily Market Notes**Market Update:**

DJIA: 9836
S&P 500: 1072
Nasdaq: 2151

10YR T-Note: 3.45%

EUR/USD: 1.476

Gold 1011

Crude Oil: 69.03

Prices Current as of
12:14 PM

Source: Bloomberg

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After having had the nerve to decline a bit on Monday, stocks took a look yesterday at the dollar making a new low against the Euro, oil and gold shooting higher – and decided that this was bullish because so-called “risk aversion”, which appeared a little on Monday, completely disappeared yesterday and it was off to the upside races once again.

Why a weak dollar and higher oil and gold prices is bullish for stocks can be argued about forever, but we have heard the positive reasons since early March as all of these items have moved lockstep together to the upside – higher commodity prices are a sign of worldwide economic recovery, investors are moving out of the supposed “safe haven” of the dollar into riskier assets like equities, and the low interest rates here in the U.S. mean that the dollar has assumed a new role as the “funding” currency in which investors borrow cheaper dollars to fund their purchases of higher yielding currencies like the New Zealand and South African ones.

As we said yesterday, the more this process goes on, then the stock market’s valuations will have little to do with traditional financial metrics and will become almost another commodity to be bought and sold on the basis of the aforementioned dynamics. Not that we are complaining about the steady rise in stocks since early March, but unless the U.S. economy shows consistent growth, especially in the areas of jobs and housing, further gains might become more difficult than the ones achieved so far. And of course there is always the seasonal possibility in the September-October time frame for a more serious correction, although we believe the further we go into this time period without one taking place, the less of a threat this occurrence becomes.

Yesterday finally saw some good earnings to break the streak of poor ones that the third quarter reporting period had started out with, and all of those companies who reported better than consensus were rewarded with higher prices. In addition, the large financial stocks took a leadership role as well, and this is what one wants to see in terms of sustaining the uptrend.

Daily Market Notes

As stocks rose to new recovery highs for the year, the VIX declined to 23.08, and this is getting closer to its downside support level of 22.48, which means that the Dow can still rise around 60 points before resistance to further advances would theoretically set in.

It was pointed out that the S&P is now 20% above its 200-day moving average and this overbought condition has taken place in 1932, 1938, 1975, 1985 and 1986. On every occasion in the past, this overbought situation led to pullbacks of 12% on average three months later before an eventual recovery led to average gains of 13% one year later.

Ahead of today's all-important F.O.M.C. policy statement, at which we believe the federal funds rate will be kept at its current level of zero to ¼%, the major averages started out with nominal gains, with the Nasdaq doing relatively better than the Dow due to unrelenting strength in the large technology stocks that have powered the +36% advance for that index this year. Then at 10:30am when the bearish oil inventory report was released and crude oil declined by as much as -\$3 a barrel and gold and the Euro declined as well, stocks decided to follow lemming-like to the downside, and this is a perfect example of that symbiosis that we have spoken about so much lately. Instead of lower energy prices being construed as a positive for consumers and therefore the economy and stocks since consumer spending makes up 70% of G.D.P., we feel this knee-jerk reaction to the downside is getting to the point where it is almost laughable, just as when stocks rally when these outside markets push to the upside, like what we saw yesterday. And naturally it is the oil stocks, which have been real laggards this year, leading the way down, along with some industrial and materials stocks as well.

More importantly, what acted as a resistance factor to further advances in stocks was that the VIX got as low as 22.88 earlier in the session when stocks were on their best levels of the Dow being ahead by +11 points.

It is also encouraging that more earnings reports came in today on the positive side,

Daily Market Notes

with the large diversified food manufacturer and an electronic component manufacturer doing well on their numbers.

We believe that equities will now drift with perhaps a slight downward bias until the 2:15pm Fed statement and once again we urge people not to trade right after the announcement is released, as we have generally seen the markets get very volatile for the next 30 minutes or so until the market decides which way it wants to go into the close.

As we said yesterday, we believe the only drama will be in the Fed's statement which could say that "tight" bank credit is slowing down growth, and this is the result of the Fed ordering banks to raise more capital and toughen their lending standards, something that many of us have personally witnessed this past year. This restricted bank credit could mean that the economic recovery in the U.S. will be slower than the Fed anticipates, which is the main reason that rates will be kept close to zero for a long time and this could be one of the reasons why the dollar has been under so much pressure as investors gravitate toward the higher yielding currencies. Ironically, we believe this syndrome has been responsible for the stock market moving higher.

Another item to keep our eyes on will be the statement as to whether or not the Fed will decide to extend the end date of the \$1.45 trillion program to buy mortgage backed securities, and this program is now set to expire at the end of the year. There is also the question of whether or not they will slowly reduce the size of the purchases.

This week's earnings scorecard continues with more third-quarter earnings reports trickling in, and there will be an important one tomorrow night with RIMM coming out with its numbers - tonight: BBY, Thursday; COMS, FINL, RIMM, RAD; Friday: KBH.

In addition to this afternoon's F.O.M.C, announcement, the week finishes off with

Daily Market Notes

Thursday: August existing home sales; Friday: August durable goods orders, U. of Michigan final September Consumer Sentiment Survey and August new home sales.

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 -20% decline in the third quarter, before a rousing gain of +62% 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.

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 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 some modest growth in the +1 to 2% 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: {PROVIDE SOURCES}. 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.