

Daily Market Notes**Market Update:****DJIA:** 9483**S&P 500:** 1023**Nasdaq:** 2015**10YR T-Note:** 3.54%**EUR/USD:** 1.429**Gold:** 955**Crude Oil:** 73.72Prices Current as of
11:03 PM

Source: Bloomberg

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Special comment: These daily comments will resume on Wednesday, September 2nd.

Yesterday saw the market rally for the third day in a row after the drubbing it took on the first day of the week. As we have been pointing out since Monday, investors got so bent out of shape on that day that they foolishly paid very high prices for so-called "downside protection" through the purchase of out of the money puts for the SPX that have now expired worthless, from strikes of 1000 on down.

The factors being attributed to yesterday's advance were that the Philadelphia Fed Manufacturing Survey showed expansion for the first time since last September. This helped some Dow industrial components. The fact that the Chinese stock market was able to advance by the same +4% that it declined the day before (which put it into a supposed bear market) also lent upside enthusiasm to overseas equities. But the big stars of the day were the financials, which got an upside boost on the back of none other than AIG, which did a reverse split of 1 for 20 and now trades at a "respectable" price because of this. The company said that they believe that they will be able to pay back the government and that they hope that they will be "able to do something for our shareholders as well." Remember that they agreed last year to turn over a stake of 80% to the U.S. in exchange for the bailout. This huge rise of +21% in the stock yesterday got the other financials going sharply to the upside, which also helped the Dow and the other major averages. Finally, there was a major upgrade of the largest search engine on expectations for growth in Europe and higher display revenues if consumers increase their spending.

The energy complex actually sold off (except for the expiring September crude oil contract) after sharp gains the day before and the reason offered for this comedown was the fact that both initial and continuing jobless claims were higher than expected, so this was an example of potentially lower consumer spending, which the overall stock market was not buying, at least for yesterday.

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The market so far today is continuing its merry upside journey and the major averages are now at new highs for the recovery move. Things started out on a positive note as European stock markets advanced on news that the German service sector and the French manufacturing sector both showed unexpected gains. This is consistent with the fact that both of their economies showed positive growth this quarter and these numbers were reported earlier in the week.

And just as the bullish plate was set by Europe, the averages literally exploded to the upside even further as the July existing home sales report came in at the best level since August 2007, for its fifth straight month of increases. In addition, Chairman Bernanke made some comments that were considered market friendly as well, by declaring that the U.S. economy is on the verge of a long-awaited recovery. He said that economic activity in both the U.S. and around the world appears to be “leveling out” and “the prospects for a return to growth in the near term appear good”. But he also said that despite much progress in stabilizing financial markets and trying to bust through credit clogs, consumers and businesses are still having trouble getting loans, so the situation is not yet back to normal.

He added that the restoration of the free flow of credit is the most important component to a lasting recovery. As a result, strains in financial markets worldwide still persist and financial institutions face “significant additional losses” on soured investments and many businesses and households are experiencing “considerable difficulty” in getting loans.

When the Dow was on its high of +154, the VIX got as low as 23.91, and this was the level at which it found some support earlier in the week, so the market did ease off of those best levels a bit, but the picture is very strong so far.

Next week sees a number of economic reports, as earnings are literally over – Tuesday: CaseShiller Home Price Index, August Consumer Confidence; Wednesday: July durable goods orders, July new home sales; Thursday: second estimate of 2Q

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G.D.P. ; Friday: July Personal Income and Spending and the final August U. of Michigan Consumer Sentiment Survey.

With earnings season for the second quarter practically over, the results have been a decline of -29% in earnings, but the average profit has topped analyst's estimates by an average of 9.8%, which is historically very high.

Now that the second quarter reporting period is winding down, stocks in the S&P 500 are expected to report 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 and could continue through the third quarter of 2009, although most forecasters are now predicting positive growth for the third quarter. This would be the first time ever that the U.S. economy has contracted for five consecutive quarters, if that were in fact to take place. In fact, 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

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