

Daily Market Notes

Market Update:**DJIA:** 9887**S&P 500:** 1055**Nasdaq:** 2070**10YR T-Note:** 3.50%**EUR/USD:** 1.485**Gold** 1088**Crude Oil:** 79.90Prices Current as of
2:13 PM

Source: Bloomberg

After last Friday's downside debacle and subsequent sharp rise in the VIX to its highest level since early July, most of the market "experts" interpreted this as bearish for stocks because investors were naturally "rushing into buying puts in order to protect their downside" and were willing to pay high prices for the privilege of doing so. And then there was the bearish talk of market indicators breaking below various moving averages, which is also supposed to be bearish, etc., etc., etc.

But let us also remember that the market almost always declines on the last trading day of the month, and even in this bullish year it has been lower on seven of the 10 end of month sessions, so what else was new on Friday? There were various reasons put forth for the decline, such as the September personal spending report that showed a decline for the first time in five months, and there were also some negative interpretations put on the U. of Michigan Consumer Sentiment Survey for the end of October as well. As a result of last Friday's declines, the market put in its worst weekly performance since mid-May and both the S&P and Nasdaq broke their string of seven consecutive monthly advances, which was a rare historical event in and of itself. But the Dow actually closed higher for the month by a whopping .45 points, its fourth straight monthly advance.

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On Monday, just to show the bearish contingent that they should not get too smug about their lower price targets for stocks, things started out strongly to the upside as a result of the good earnings report from a major U.S. auto manufacturer and also some better than expected economic numbers, which included the October ISM Manufacturing Survey, and this rose to its best level in more than three years; September Construction Spending which unexpectedly increased +0.8% and September pending home sales rose +6.1%. From an early gain of as much as +146 points, the Dow actually declined to a mid-day loss of as much as -34 points, led down by the financials, as a Fed official said that "Although conditions and sentiment in financial markets have improved in recent months, significant stress and weakness persists."

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One could see that things were not going to be able to hold the higher levels because the Nasdaq/Dow ratio was poor when the market was on its highs, and as we all know, this relationship will not allow the market to continue on the upside. But after this sharp intraday sell off, stocks got their act together and the Dow was able to climb back to a closing gain of +76.

On Tuesday, the market was also struggling intraday despite none other than Warren Buffett purchasing the 77% of a holding company that operates a railroad system in the U.S. and Canada that his company does not already own, and a takeover of a tool manufacturer by a tool supplier, and these actions helped the shares of all the stocks involved. In addition, the dollar started weakening again which helped the price of oil and gold rise, the latter to a record high as India bought gold from the I.M.F., an astounding move as they waited for these high prices to do so. The Dow Transports posted their best gain in seven months because of the abovementioned activity. But the financials slipped once again, this time because of a report that the British government will have to put more money into a diversified Scottish bank. But by the end of the day, most of the large financials here were able to eke out small gains.

It is interesting to note that for the third month in a row, starting on September 2nd, October 2nd, and now November 2nd, this past Monday, the VIX hit its highest level during that very late month-very early new month time period, as the market for some reason has gotten sold off sharply during this time frame for three months running. For instance, after a hysterical close on Friday of 30.69, which was an astounding gain of 23% from Thursday's close, the VIX actually hit an intraday high on Monday of 31.84 before falling back once again under 30 as stocks came back from their worst intraday levels as described above.

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Today has started out strongly as the October ISM Non-Manufacturing Survey came in for the second month in a row above 50, which shows expansion in the sector of the economy that covers 80% of G.D.P. The friendliest part of the report was that the new orders component reached its highest level since October 2007. There is also the belief by investors that the F.O.M.C. will keep rates at a record low for an extended period. Hopefully, they will also say that they are not worried about inflation at this point and that all of their stimulus into the economy has shown signs of reviving growth. Of course, this has once again weakened the dollar and allowed gold prices to keep rising to record highs. And in the sometimes bizarre way of investor thinking, some health care stocks rose because of the Republican gubernatorial victories in New Jersey and Virginia, which in this way of thinking could bolster opposition to the health care legislation currently in front of Congress. And once again we urge people not to trade right after the 2:15pm Fed announcement as things will get very volatile both up and down before the market decides which way it wants to go into the close and this will not be until around just before 3pm.

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. This week also sees many companies reporting earnings, although they are not so much of the heavyweight variety as we have already seen: tonight: Dow component CSCO; Thursday: ATML, NILE, CAH, CBS, CTL, CROX, CVS, DYN, FBN, HAIN, HOC, IGT, MGM, PWE, PLUG, RRGB, SLE, SBUX, SMG, TM, UL; Friday: LPNT

The economic data is going to be very important, highlighted by the Fed statement later today after their two-day meeting that will leave rates unchanged again and we also have Friday's October jobs report. We will talk about the jobs report in more detail tomorrow. So these are two potentially market moving items that must be paid attention to.

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It should also be pointed out that when the S&P has been 20% above its 200-day moving average, as it was only in 1932, 1938, 1975, 1985 and 1986, and as it was recently, the market underwent an average decline of -12% over the next three months before being higher by +13% a year later.

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 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: {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.