July 22, 2011

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Daily Market Notes

Market Update:

DJIA:	12686
S&P 500:	1344
Nasdaq:	2852
10YR T-Note:	2.97%
VIX:	17.31
EUR/USD:	1.435
Gold	1602
Crude Oil:	99.64

Prices Current as of 12:45 PM

Source: CNBC

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Despite the potential gloom and doomsters out there who have been making ominous predictions of one sort or the other if the European rescue packages do not solve the issues in the various weak countries and if the U.S. debt limit ceiling and budget cut issues are not resolved satisfactorily before that August 2nd deadline, the markets have taken quite the opposite view lately.

Following Tuesday's first 200 point Dow gain this year and the best overall market performance since early March, things yesterday decided once again that the path of least resistance was higher in a big way. After a better start on a decline in the four-week moving average of weekly jobless claims and slightly better readings from the June L.E.I. report and the July Philadelphia Fed Index, things exploded to the upside as the Dow reached its best level of the day at 12:45pm with another large gain of 179 points. From this best level, it spent the rest of the afternoon maintaining most of those advances and ended with a closing gain of 153. Breadth numbers were very strong as well, with a 4 to 1 upside ratio and the VIX declined by exactly as much as it should have relative to the Dow's advance, falling by 1.53 to 17.56.

And let us all remember that on Monday's somewhat panicky low, the VIX got as high as 21.93, and that the high 21's has been a big resistance level for the past month or so, which has meant that every time the VIX gets that high, stocks are oversold and due for a rally which we have certainly seen since Monday's low, as the Dow has improved by 455 points since that time.

Ironically, on such a strong day, the two Dow stocks that did report their numbers were both lower, namely the largest semiconductor maker and an aerospace and building materials maker. But strong results from a rail transportation company helped the Dow Transports approach their best levels of the year and the numbers from a major investment bank caused that stock to rally and carried the other beaten-down financials to strong gains for the second day in a row.

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Reacting to developments on the Euro-front, the Euro rose to the highest level in two weeks against the dollar as officials there said that European governments may expand the region's bailout funds and accept a temporary Greek default, which would have the effect of reducing concerns about the contagion spreading to other countries. There were times during the day that the dollar did recover its worst losses on conflicting reports from various sources that the President and the Republican leadership had reached a budget accord, which the White House then denied. The French President stuck in his two cents by re-iterating his support for the Euro, saying it is an "irreplaceable" achievement of Europe, despite much opinion to the contrary, especially from those countries whose economies are in dire shape.

The policy would be to keep any period of Greek default as short as possible. Any new bonds that will be issued could be backed up by top-rated securities sold by the European Financial Stability Facility, whatever that organization is supposed to be.

The Treasury market here fell sharply for the second day amid the report that E.U. leaders may accept a temporary Greek default and ease the terms on bailouts to other cash-strapped countries, which would supposedly lessen the appeal of the "safety" of U.S. bonds. As a result, the yield for the 10-year Note backed up to over the 3% level once again, and they have been trading in a narrow, volatile range of between 2.87% and 3.05% in recent sessions, as the political and economic implications of the various rescue packages manifest themselves. These yields were also hurt by Standard & Poor's repeating that there is a one-in-two possibility that it will cut the AAA rating if the U.S. government has not agreed on a "credible solution" to the nation's debt level, even if it raises the debt limit in time to avoid a potential default. The administration signaled that it may accept a short-term increase in the U.S. debt ceiling if an agreement on cutting the budget deficit is imminent.

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After yesterday's upside fireworks, things are taking a breather today, similar to what they did on Wednesday after Tuesday's moonshot as well. The Dow is being hurt by weak results from a machinery maker and telecom member, although two other members are doing well – the diversified technology and financial services company and the hamburger fast food chain, the latter at a new all-time high. And that item which in a sense perversely controls what goes on in the U.S. market, namely the Euro, is declining as now there are concerns over the rescue plan to allow their $440 billion Euro rescue fund to buy debt of other stressed nations in an attempt to try to contain damage in Spain and Italy even as they were willing to allow a temporary Greek default.

And in their recent neurotic back and forth pattern, U.S. Treasury yields are declining once again on hopes that the President is getting close to an agreement with lawmakers to cut the budget deficit, raise the borrowing limit and avert a default. Depending on what day of the week it is, the bond market has conflicting reactions to basically the same news, as for example yields rose yesterday when this same news was out there – go figure. So once again, the 10-year yield is below 3% in that back and forth pattern that we have been pointing out.

The Dow has been lower for most of the session, negatively influenced as mentioned above, and reached its worst level of the session with an 80 point loss at 10:30am, from which it has managed to work off more than half of its losses. The Nasdaq, on the other hand, is ahead by 15 points as this is being written due to unrelenting strength in the large mobile telecom and computer maker, in addition to the largest Internet search engine companies, both here and in China, in addition to others. Breadth numbers are negative at a 13/16 ratio and the VIX is lower despite both the Dow and S&P being down as well, which is not so great because it puts it closer to support. It is currently at 17.20, a loss of .36.

Of the 121 S&P companies to have reported so far, 83% of them have beaten the estimates, and the calendar for next week includes the following – Monday: BA, BIDU, NFLX, TXN; Tuesday: 3M, AMZN, BWLD, HSY, JNPR, LMT, OXY, UPS, X; Wednesday: AET, MCO, SBUX, V, WFM; Thursday: AOL, ADP, AVP, BMY, CL, DD, XOM, K, MET, ROK, TWC; Friday: CVX, MRK, NEM. This means that we hear from 6 Dow companies.

We will list the economic calendar on Monday, but obviously the main economic event will be the approach of that August 2nd deadline to raise the debt limit and all the accompanying drama that will surround it, in addition to the latest twists and turns from Europe.

And to repeat what was said recently, the market has now taken on a resemblance to last year, when things reached their highs in late April, and then took a dive in May and June, which marked the lows for the year, and it was the same causes last year as well, with European sovereign-debt issues responsible for much of the comedown, although let us also remember that we started the decline this year from higher levels, which left the market more vulnerable to some sort of setback from the misplaced mind-set of higher commodity prices somehow being good for stocks. Let us hope that this year also sees the market low during this time period as well. And one sign for optimism in this regard is that the May and June declines this year were nowhere near as severe as they were last year and July was actually an up-month before another decline in August.

The S&P trades at 12.4 times forward earnings, which could bring a measure of support to stocks. Earnings were $85 in 2010 and are projected to be $105 for 2011, according to the analysts who follow these companies. The average P/E multiple for the S&P going back to 1954 has been 16.2. Since 2006, the average P/E multiple has been 14.7

For all of 2010, earnings increased by +38%, which was the most since 1995. For 2011, first-quarter earnings gained +19% and are projected to gain +9% for

the second quarter as reported by Bloomberg Financial and the 14% projected gain for 2011 would be the largest two-year advance since the period ended in 1995. The highest ever earnings for the S&P in one year so far took place in 2006, at $88.

After four consecutive quarters of negative G.D.P. growth, we now have seven consecutive quarters of positive growth, starting with the third-quarter of 2009, every quarter in 2010 and the first quarter of this year, according to the Commerce Department. For all of 2010, G.D.P. rose at a 2.9% rate, which was the highest since 2006 after a decline of 2.6% in 2009. For 2011, the prediction is now for G.D.P. growth of 2.5% and it is 3% in 2012, although estimates for this number vary widely and are constantly changing.

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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.