

Daily Market Notes

Market Update:

DJIA: 10969
 S&P 500: 1152
 Nasdaq: 2465

10YR T-Note: 1.92%

EUR/USD: 1.36

VIX: 40.22

Gold 1868

Crude Oil: 85.95

Prices Current as of
 12:50PM

Source: CNBC

Special Comment: We sent out this past Friday afternoon our annual revision of the ETF glossary, and this extensive report lists around 400 of them and should be used as a reference guide to different sectors of this rapidly growing area of investment.

The worst thing about Wednesday's upside moonshot was that the last 45 upward Dow points were completely contrived in the last eight minutes of the session, most likely due to some kind of exotic maneuvering with ETF's or other types of instruments. Unfortunately, this left the market vulnerable yesterday to some sort of giveback of those contrived very late gains. And on the old "chickens coming home to roost" theory, this is exactly what happened because unfortunately we should all remember that the market declined overall in August and it has declined overall so far in September, which means that the near-term trend is lower. That is why unfortunately these nice rallies that take place from time to time do not appear as if they want to become the norm.

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But the market did try to hang in there for most of the day, as an early 45 point Dow decline turned into a gain of as much as 62 points at 11:15am, but the rest of the market was not cooperating, as breadth numbers were negative at that time. For the rest of the morning and early afternoon the Dow traded in a narrow range and was 20 points lower when none other than Fed Chairman Bernanke took to the podium at 1:30pm, and as my grouchy old great-uncle used to say – "So what did you accomplish?"

In a speech on the U.S. economic outlook, he mentioned that the Fed has a "range of tools that could be used to provide additional monetary stimulus". In addition, he added that the prospect of an "increasing fiscal drag on the economy in the face of an already sluggish recovery highlights one of the many difficult tradeoffs currently faced by fiscal policymakers." This was another attempt to transfer blame for failures to get the economy going again to someone else, namely the Congress, and this blame-transference is the

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oldest bureaucratic trick in the books. He also added that he saw “little indication that the higher rate of inflation experienced so far this year has become ingrained in the economy”, which certainly means that interest rates are going to stay near record low levels for a long time. He said that this stability in inflation expectations was the result of resource slack that exists in the U.S. labor and product markets. And given the large share of labor costs in the production costs of most firms, subdued unit labor costs should be an important restraining influence on inflation, he added.

So what did the market do after it heard these pronouncements? It went straight down from the time of the 1:30pm speech until the close and ended with a 119 point loss, and breadth numbers continued to deteriorate with a closing negative ratio of 1 to 3.4. The VIX rose by just about what it should have relative to the Dow's decline with an advance of .94 to 34.32. And it was fitting justice that the Dow was lower by only 70 points at 3:45pm when it did the complete opposite of what was described above, as it gave back those 45 manipulated upward points of the day before as mentioned above to now lose another 49 points in addition to the 70 at 3:45pm to end with that 119 point decline.

And sure enough, the bond market saw that weakness in stocks as another reason to rally, and yields declined back closer to their recent lows on the longer 10 and 30 year maturities. And to add more misery to the credit markets worldwide, the cost of credit default swaps in Greece rose to a record high, as it was announced that their second-quarter G.D.P. declined by 7.3% after a drop of 8.1% in the first-quarter. As a result of this further dismal news, the Euro took a major beating with a decline to below that 1.40 support level that had held for several months.

Then the O.E.C.D., which is short for Organization for Economic Cooperation and Development, lowered its forecast for economic growth here to 1.1% for the third-quarter from 2.9% and to 0.4% growth in the fourth-quarter from an

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original forecast of 3%.

After yesterday's weak close, things started out under more pressure today, as the President's speech last night on his job creation bill for \$447 billion did not inspire much confidence among investors. But the main negative today is once again unfortunately focused on Europe, as German officials said that their government is preparing plans to shore up banks in the event that Greece defaults and this is the last thing that the markets need to see. In addition, there was a resignation from a top E.C.B. official over differences of opinion about how to fight the debt crisis.

The Euro declined to its lowest level since March with another large loss to 1.367. Greek two-year notes rose to 57%, the highest ever in the Euro era, as did their credit-default swaps. Germany's emergency plan if Greece defaults involves measures to help banks and insurers that face a potential 50% loss on their Greek bonds if the next help measure of Greece's bailout is withheld.

As a result of all these negative inputs, the Dow started out with a loss of around 200 points and then tried to stabilize with a move higher to a decline of "only" 120 points or so at 11:15am when things took another downward leg to a loss of more than 300 points as this is being written, its low level of the day. Not even a patriotic remembrance of 9/11 earlier in the day at the New York Stock Exchange and the hope for a rally because of that could overcome the negativity that the overseas difficulties are presenting to investors.

The VIX is getting the jitters once again, as it rises by almost 6 points to over 40, which is twice as much as it should be relative to the Dow's current decline. And the yield on the 10-year Note has now fallen to a new record low of 1.87% as the flight to quality continues.

Of course it goes without saying that the market must at least make a stand at these lows and that nothing disastrous comes out of Europe over the

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weekend. There are several important economic reports here next week which we will list in Monday's daily notes but these could or could not be influenced by what happens overseas.

The S&P trades at under 12 times 2011 earnings, which could bring a measure of support to stocks. Earnings were \$85 in 2010 and are now projected to be \$96 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 the first half of 2011, earnings gained +18 as reported by Bloomberg Financial and the 16% overall 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. For 2012, earnings are now projected to be \$104 for the S&P.

After four consecutive quarters of negative G.D.P. growth, we now have eight consecutive quarters of positive growth, starting with the third-quarter of 2009, every quarter in 2010 and the first quarter and second quarters of this year, although these numbers are weaker than earlier estimates, according to the Commerce Department. For all of 2010, G.D.P. rose at a 3% rate, which was the highest since 2006 after a worse than originally estimated decline of 3.5% in 2009 and an overall decline of 0.3% in 2008. For 2011, the prediction is now for G.D.P. growth of 1.5% and it is 2% in 2012, although estimates for this number vary widely and are constantly changing.

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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.