

Daily Market Notes**Market Update :**

DJIA: 11727

S&P 500: 1213

Nasdaq: 2582

10YR T-Note: 1.98%

EUR/USD: 1.34

VIX: 35.91

Gold: 1719

Crude Oil: 98.87

Prices Current as of
1:15PM

Source: CNBC

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Yesterday was the third day in a row when the stock index futures were higher in the overnight session but decided as the morning wore on that the path of least resistance was lower, and sure enough those lower futures resulted in the Dow hitting an early 139 point loss on the various European concerns. And once again, these concerns were offset to some extent by the continuing stream of better economic reports about the U.S. economy, as October Industrial Production rose to its best level in three months and the November Homebuilder's Index rose to its highest since May 2010.

Market action was very similar to Tuesday, when a lower opening was followed by an afternoon rally, with the Dow reaching a 12 point gain at its best level at 1:50pm, and once again the various market experts now said that the better economic reports here were taking precedence over the ongoing European difficulties. These gains started to fade and at 3:15pm the Dow had turned that fleeting advance into a small decline of 36 points when things went into one of those sickening very late in the day collapses, and after all of the damage was done, the Dow ended with a large decline of 190 points. In a sense, this type of action was also similar to what happened on Tuesday as well, as the Dow fell apart in the last 30 minutes or so and turned an 85 point gain into an eventual advance of only 17.

And as if the market does not have enough negativity out of Europe to deal with on a day to day basis, it was hit at that 3:15pm collapse time with a statement from the Fitch Ratings Agency to the effect that U.S. banks have "manageable direct exposure" to the stressed European markets of Greece, Ireland, Italy, Portugal and Spain, but "further contagion poses a serious risk", thanks a lot. They also added that unless the Eurozone debt crisis is "resolved in a timely and orderly manner, the broad credit outlook for the U.S. banking industry could worsen."

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These negative comments put a huge damper on what had been the ability of the market to recover from those lows as mentioned above, and the early recovery was motivated by a statement from a Fed official who said that the Fed may need to coordinate with the E.C.B. on fighting turmoil in the credit markets. This comment was able to offset the early stock losses which were partly attributed to a statement from the Bank of England that the failure to resolve the European debt turmoil could lead to “significant adverse effects” on the global economy, which is sort of what Fitch said later in the day. In addition, Italy’s largest bank apparently asked the E.C.B. to broaden the types of assets that they would accept as collateral. This had the effect of dramatically weakening the bank stocks here as well, not that they need additional reasons to continue the downside misery that they have been in.

Adding to investor’s woes was that crude oil prices, which we have been warning about were sneaking up for the past several weeks, finally broached the psychological \$100 a barrel level with a disturbing close at \$102.50 a barrel, which was a five-month high and supposedly the reason for this large move was that a re-direction of pipelines will allow more West Texas Intermediate crude oil to be shipped out of the Cushing, Oklahoma storage facility. This means that the supply tightness there will be alleviated and will now allow its price to catch up to the much higher Brent crude prices, and isn’t this great for the consumer?

In the meantime, most European yields continued to rise, but the important Italian 10-year yields actually declined a bit to end right on that magic 7% level. Also giving some mid-day support which was taken away by the late slide was that Mario Monti was sworn in as Italian prime minister and finance minister in an unelected government that will now be charged with imposing austerity to prevent that country from falling further into the abyss.

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In addition, the new Greek prime minister Papademos won a confidence vote in parliament and received a mandate to implement budget cuts which will be necessary to obtain the financing in order to prevent further damage to their economy and to try to keep Greece in the E.U.

And naturally the Euro led our stocks around once again, as it opened down .0090 points to 1.343 and then when the Dow reached its best level of the day it also got to its high at 1.355, before falling back to its lows as stocks collapsed into the close.

In addition, market attention has turned to France, as their 10-year yields have risen from 2.54% in early October to 3.69% yesterday, which has caused consternation that one of the better economies in Europe is under pressure as well, and it was reported that the five largest U.S. banks have \$114 billion in loans, deposits and other assets tied to French banks, which could explain why the bank stocks here were so weak.

As a result of the late collapse, breadth numbers reversed to the downside from their best early afternoon levels and ended at a 1 to 3 negative downside ratio. The VIX advanced by only a little more than it should have relative to the Dow's decline with a gain of 2.29 to 33.51, and in a sense when you get days like this, it is better that the VIX really skyrockets in order to create more of an oversold condition.

After yesterday's late collapse, things tried to steady in the early part of the session, but there was one major problem which everyone should have recognized despite what was going on in Europe, and that was a very weak Nasdaq/Dow ratio, and unfortunately we all know who wins that battle. For instance, when the Dow managed to reach its best level of the day with a gain of 42 points and was able to stay positive between 10:30 to 11am, the Nasdaq was lower by around 15 points or so, and that is never a good sign.

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And once again, the economic reports here were better than expected, with weekly jobless claims declining to their lowest level in seven months and October housing starts doing better than predicted and building permits, an indicator of future activity, rose by 11%. But the November Philadelphia Manufacturing Survey did decline somewhat when an increase was expected.

And the Euro, believe it or not, actually started out higher today, up to around that 1.354 level which has prevented it from going higher this week on the miracle that Italian bond yields actually had the nerve to decline as apparently the E.C.B. was buying. But that optimism faded as Fitch Ratings had to stick in its two cents once again by saying that Italy's credit rating may be cut to low investment grade should they lose market access, while their economy may already be in a recession. But they did add that the new government has a "window of opportunity" to carry out the urgent measures needed to lower borrowing costs, along with help from the E.C.B. But despite the decline in Italian yields, the news from Spain was not so good as their 10-year yields rose to the highest level ever of the Euro era.

At around 12:30pm, the Dow virtually fell off of the cliff, with an extremely fast decline from a loss of "only" 55 points to as much as 194 points at its worst level in a period of 10 minutes or so, which has to be one of those sickening incidents that does not seem to conform to what used to be called a "rational market." And as the Dow succumbed to what the Nasdaq was doing, those weak high-priced technology stocks got even weaker. From those worst levels of the day, things have steadied somewhat as the afternoon is moving on. Breadth numbers are horrendous at a negative 1 to 6 ratio. The VIX once again is not panicking and is up by around 2 points relative to the current Dow decline of 170. Once again, if we are going to get these large Dow selloffs, better that the VIX skyrockets in order to create more of an oversold condition.

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At least those sky-higher crude oil prices are coming down, falling as low as \$99, but the problem with that situation is that if this is the only way that we are going to get lower oil prices, . namely though declines in the stock market, then this could become a problem for consumers going into the holiday shopping season.

With earnings season for the third-quarter just about over, this week's calendar has been light and dominated by retailers, and the lineup finishes tonight with: GPS, CRM and HNZ.

For what it is worth, there is a statistic that says the S&P has gained on average 5% in the fourth-quarter after third-quarter losses of greater than 8% since 1924. There is another statistic that says when the S&P declines by 14% or more during the third -quarter, as what occurred this year, it has an 89% chance of advancing during the fourth-quarter. Let's see if history repeats itself this year.

Isn't it enough that around \$10 trillion was wiped off of equity values worldwide in the third-quarter, which one would like to think makes stocks look cheap at current levels, especially given the level of all-time record low interest rates. The argument for stocks being good values here is further enhanced by the fact that despite all of the turmoil on fears of slower economic growth or worse, analysts have actually raised their profit forecasts for the S&P companies for 2011 to a record \$99.38 from \$98.73 in late April when stocks were on their highs, according to Bloomberg. This is somewhat of a strange occurrence, because the rap against stocks lately has been that earnings estimates are too high. So we will have to see who is right on this one.

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 projected to be \$99 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

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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 18% overall projected gain for 2011 would be the largest two-year advance since the period ended in 1995. Third-quarter earnings are projected to now rise by 15%. The highest ever earnings for the S&P in one year so far took place in 2006, at \$88. For 2012, earnings are still projected to be \$104 for the S&P.

After four consecutive quarters of negative G.D.P. growth, we now have nine consecutive quarters of positive growth, starting with the third-quarter of 2009, every quarter in 2010 and the first three 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 1.8% and it is 2.6% 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.