

Daily Market Notes

Market Update :

DJIA: 12162

S&P 500: 1252

Nasdaq: 2638

10YR T-Note: 2.04%

EUR/USD: 1.34

VIX: 27.42

Gold: 1717

Crude Oil: 98.32

Prices Current as of
1:20PM

Source: CNBC

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Oh, no – for the umpteenth time, yesterday’s market had nothing to do with what went on here and unfortunately had everything to do with what went on in Europe, as the fact that U.S. weekly jobless claims fell to their lowest level since February meant nothing, but the conflicting statements out of Europe meant everything.

For instance, after the mixed to better sessions of recent days, the various stock index futures originally signaled a better opening as the Euro jumped to a half-point gain up to 1.346 at 8:30am. This rise in both the Euro and our stock index futures was partly a function of the weekly jobless claims report which came in better than expected. The E.C.B. offered banks as much money as they need for three years and loosened collateral rules at refinancing operations to ease strains in the credit markets. They also said that the central bank will cut banks’ reserve ratios to 1% from 2% and will stop fine-tuning operations at the end of each reserve maintenance period.

But that optimism quickly dissipated as another in the long line of European bureaucrats whose pronouncements tend to hurt the markets more than help them, namely the new president of the E.C.B., said that he did not plan to purchase more bonds with the statement that their bond purchase program was not “eternal or infinite.” The stock futures then added to their losses as the European Banking Authority said that the region’s banks will need to raise \$114.7 billion Euros in fresh capital to weather the sovereign debt crisis.

To no one’s surprise, the Euro took a downside beating from those best levels as well, and sold off to 1.329, and once our stock indexes and stocks themselves saw this, that was all she wrote on the downside as the Dow declined steadily to a 180 point loss in the early afternoon. From this level it was able to fight its way back to “only” a 96 point decline at that difficult 3:15pm witching time, which has now produced market selloffs into the last 45 minutes of the session for the first four days this week, and yesterday was no exception.

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From that nice recovery, the market did a complete negative about-face and collapsed into the close, as the Dow fell to a loss of as much as 229 points with three minutes to go before ending 198 points lower. And for the third day in a row, the Nasdaq lagged badly on continued weakness in its high-priced technology leaders. Breadth numbers were horrible at a negative 1 to 6 ratio and only one Dow component ended higher, namely the large hamburger chain at its best level ever after strong same-store sales out of Asia. The VIX rose by about as much as it should have relative to the Dow's decline, up by 1.92 to 30.59 after spending the previous five days below that 30 level, which is now beginning to define whether or not the market is going to continue to advance or just bang around in its current trading range.

So what happened to cause all of that late-day drama? The rally off of the first low occurred because of a statement to the effect that there will be issuance of common Euro-zone debt or perhaps even running the temporary and permanent bailout funds simultaneously, in addition to giving the European Stability Mechanism a banking license. The rally was stopped dead in its tracks as mentioned above when it was reported that Germany had in fact rejected some measures, including giving the E.S.M. a banking license and issuing common Euro-zone debt. And that was all she wrote, as the market went into this negative hysterical late selloff as described above.

And as our bond market saw all of the negative European hysteria, it decided that things were going to slow down and as a result the yield for the 10-year U.S. Treasury Note declined down to 1.97%. In addition, there is also an interesting technical pattern going on as well, as the S&P failed the first three days of the week at exactly the same level, as the intraday highs were 1267, 1268 and 1267 respectively, none of which were able to hold. The failure at this level corresponds to the 200-day moving average which is currently around 1264, so it appears as if there is selling against this price and this will now be the level that must be overcome if the rally is to continue into the end of this year and into the new year as well.

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After yesterday's late meltdown, wouldn't you know it, some optimism has returned for today's session, as Europe secured what might be perceived as an historic agreement to draft a new treaty for deeper economic integration despite the U.K., which is the region's third largest economy, refusing to join the other 26 countries in a fiscal union. A new treaty could take three months to negotiate and may require risky referendums in countries such as Ireland. The E.C.B. would keep purchases of Euro-zone government bonds capped for now and take no extra dramatic action. Twenty-six of the 27 E.U. leaders agreed to pursue a tougher budget discipline regime with automatic sanctions for those who do not in fact implement stricter controls over spending in the E.U. But Britain said it could not accept E.U. treaty amendments after it did not secure concessions for itself.

In addition to the ostensibly positive news from Europe, stocks have also reacted positively to the mid-month U. of Michigan Consumer Sentiment Survey which rose to its highest level in six months. As a result, the Dow opened higher and has been able to maintain close to its best levels so far, with a gain of 156 as this is being written. Breadth numbers are the reverse of yesterday with around a 5 to 1 positive ratio and the VIX is getting sold off by much more than it should be relative to this Dow gain, with a loss of 3.12 to 27.47, once again below that important 30 area and it must stay in the 20's in order to ensure more stock advances ahead. After a slow start, the Nasdaq is more than holding its own, which if this continues could ensure that the market goes the distance.

The reason for the slower start to the technology stocks were profit warnings from three semiconductor-makers. And in a complete reversal of yesterday as well, 29 of the 30 Dow stocks are higher, the exception being the large chemical company on a profit warning which alone is taking 19 points away from the Dow just by itself.

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The trick today will be to avoid that 3:15pm meltdown time and if things can maintain their current gains, this will now be the second week in a row of a higher market, which hopefully will build some momentum for a year-end rally.

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, although this probability is getting less after the horrible start to November threw things off, but there has obviously been a strong improvement starting last week and moving forward.

The S&P trades at 11 times projected 2012 earnings of \$108, 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

For all of 2010, earnings increased by +38%, which was the most since 1995. For the first three-quarters of 2011, earnings gained +17% 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. Fourth-quarter earnings are projected to rise by 11%. 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 \$108 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.

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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 1.6% 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.