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Daily Market Notes

Market Update:

DJIA:	**12615**
S&P 500:	**1341**
Nasdaq:	**2841**
10YR T-Note:	**3.18%**
VIX:	**17.04**
EUR/USD:	**1.421**
Gold	**1499**
Crude Oil:	**100.09**

Prices Current as of 12:45 PM

Source: Bloomberg

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For the third day in a row and the second straight day this week, the market did better yesterday, and the primary reason for the advance was attributed to the fact that commodity prices also rose for the second day this week. So once again, what I believe is that sick mantra that has become the primary investment theme of the past several months, namely that higher commodity prices are bullish for stocks, held sway for the second day this week as well.

The Dow started out higher and basically never looked back, as it maintained gains of between 40 to 50 points for the bulk of the day, when at 2:45pm it made an accelerated upside move to show a 97 point gain at 3:30pm before ending with a closing advance of 75 points. Breadth numbers showed a very positive ratio of better than 4 to 1, and this was courtesy of the fact that the Nasdaq/Dow ratio was also strong for the second day in a row, and the Nasdaq closed with a 28 point advance as a result. This was courtesy of strong gains in some of the high-fliers, such as the largest E-commerce stock at a new all-time high, and despite a pathetic performance from the largest software company (so what else is new?) after its takeover of Skype.

For the second day this week as well, the VIX declined by more than it should have relative to the Dow's gain, as it declined by 1.25 to 15.91, which puts it around 1.60 points away from its ultimate downside support level of 14.30. And one can also argue that the strange rise of the VIX on Friday to as high as 19.80 when the major averages were up all day after the jobs report, also set the stage for the advances of the past two days as well, as let us remember that when the Dow and the VIX both go up, this is bullish because it puts the VIX further away from support while the market is going higher in any event, and how many times have we seen this take place.

Also helping was the fact that the Chinese April trade balance showed an $11.4 billion surplus as exports hit a record high, four times the amount that the experts had predicted. This ostensibly shows that worldwide economic

strength is present. In addition, there was further "good news" as Greek bond yields declined sharply and this is supposed to illustrate greater confidence in that country's messed-up economic situation. In addition, merger and acquisition activity has now reached $884 this year, which is a 26% increase from last year and is always taken as a sign that companies see value in other companies. And as we come to the end of the first-quarter earnings season, of the 423 S&P companies that have reported, 72% of them have beaten their projections.

Never mind that crude oil reached its best level of the day at the same time that the Dow reached its high as well, with a gain to $103.88, but even worse was the fact that gasoline rose by the most since July 2009 and the "explanation" was that the high water levels on the Mississippi River caused some shipping docks to be shut down, which has supposedly led to the disruption of supplies. In addition, gasoline inventories are at a 22-month low because of the changeover from winter blends to summer blends due to a change in the emission standards of these different blends. The flood situation took on more urgency because 13% of domestic output is located in Louisiana, right where the flood waters are approaching. And let us not forget that the reversal in the Euro from starting out the day with losses which then turned into gains was also used as the "explanation" for the gains in various commodities, which is the "new normal" that we are in, and this of course is bullish for stocks as well.

So let's see now, just as stocks rose yesterday because higher commodities are a good thing, today the reason being offered for the decline is that these same commodities are now lower, courtesy of a weaker Euro and a stronger dollar, heaven forbid. Apparently these higher commodity prices are not so good after all, as the Bank of England said that inflation remains "uncomfortably higher", which means that they might raise rates later this year. In addition, there were some reports that showed that inflation in both Germany and China was higher than expectations, and to top it off, Poland, of all places, had the nerve to "unexpectedly" increase its benchmark interest

rate, whatever that is.

Now wait a minute – does this mean that higher commodity prices are not so good for stocks after all, as we have been told since the start of Q.E.2 that higher raw material prices are good for companies, and this is why stocks have been moving up at the same time that commodities have been going to these outlandish levels as well. So now we are seeing crude oil prices going back down close to $100 a barrel again, and this is supposed to be bad for equities and consumers? And how about those gasoline prices, which rose by that huge amount yesterday as mentioned above and are down today by more than 6% after an unexpected gain in inventories in today's report and as one news organization put it, "speculation that prices rose too high without confirmation that flooding on the Mississippi River will cut supplies." So what does one say to those astute investors who bought after gasoline prices were ahead by almost $10 yesterday? – to go check out the flooding levels on the Mississippi themselves?

At its low, the Dow was down by 90 points, hurt by losses in those industrial and energy stocks which tend to rise when the Euro and commodities go higher, and then take it on the chin when these items go the other way like today. The Dow is also being hurt by a weak report from the theme park and entertainment company as well. One group of stocks that has done much better lately is the consumer defensive types as investors start to perhaps shift out of these industrial and energy issues that have done so well until recently, and this group would include such Dow components like its pharmaceutical components and restaurant chains. And the VIX is up by less than it should be relative to the Dow's decline, ahead by only .42 to 16.33 as the Dow is lower by 80 points as this is being written. The Nasdaq is trying to hang in there, down by only 9 points due to another new high in the E-commerce stock, gains by the largest Internet router and switcher maker ahead of its report tonight, in addition to others here and there.

The March trade deficit also widened by more than expected, to $46.2 billion, the widest since June, as a result of these high oil prices making imports gain more than what turned out to be record exports. This could have the effect of lowering the first-quarter G.D.P.

Economic reports this week are not as dramatic as last week, and we get: Thursday – weekly jobless claims, April P.P.I., April retail sales; Friday – April C.P.I. and preliminary May U. of Michigan Consumer Sentiment Survey.

The S&P trades at 13.5 times forward earnings, and 15.5 times current earnings, as 2010 earnings are going to be $85 for the S&P and $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.

For all of 2010, earnings increased by +30%, which was the most since 1995. For 2011 the analysts are forecasting increases of +12% for the first-quarter of 2011 and +16% for the entire year, as reported by Bloomberg Financial and this would be the largest two-year advance since the period ended in 1995. This means that S&P earnings for 2010 were $85 and projected to be $97 in 2011. This would equate to around a 14% gain this year. The highest ever earnings for the S&P in one year took place in 2006, at $88.

After four consecutive quarters of negative G.D.P. growth, we now have six consecutive quarters of positive growth, starting with the third-quarter of 2009 and continuing with every quarter in 2010 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 G.D.P. growth of 3.1% and it is 3.9% in 2012.

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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.