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Daily Market Notes

Market Update :

DJIA:	**12050**
S&P 500:	**1252**
Nasdaq:	**2677**
10YR T-Note:	**2.02%**
EUR/USD:	**1.35**
VIX:	**31.47**
Gold:	**1772**
Crude Oil:	**101.62**

Prices Current as of 1:20PM

Source: CNBC

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When I listened to yesterday's "explanations" for why our stock market started out with losses, I thought I was at a betting parlor handicapping a European soccer tournament, as statistics such as the following were thrown out as "reasons" why U.S. stocks were moving to the downside – the "spread" between French and German 10-year yields widened out to 190 basis points, the German-Austrian spread was out to 192 basis points, the Belgian-German spread was at 313 basis points, while the German-Spanish spread was out to 458 basis points, all of which were apparently record wide yield differentials. This was supposed to show that a crisis situation in regards to the ability of these countries to fund their deficits was reaching panic proportions. Oh, and let's not forget the latest bad boy in the Eurozone, namely Italy, where those pesky 10-year yields went back above the 7% danger zone, which as everyone should know is the level at which the original bad boys of Europe, namely Greece, Ireland and Portugal, all had to be bailed out.

As a result of these record wide yield spreads, the S&P futures had the nerve to decline by as much as a huge loss of 18.40 points even before trading in the U.S. got underway. Cooler heads then prevailed as a series of economic reports continued to show that the U.S. economy was not in danger of falling into a double-dip recession, as the most nervous of the nervous nellies have been yapping about since the downgrade of the U.S. credit rating began the unnerving of markets worldwide. These reports showed that October retail sales rose by more than expected, with spending on consumer electronics showing a substantial advance; the November N.Y.State Empire Manufacturing Survey showed the first increase after four straight months of declines, and the October P.P.I. showed that overall prices declined and the core rate excluding food and energy was unchanged. Unfortunately, this survey was taken during the time that crude oil prices had declined to their lows of the year at $75 a barrel and the large rise lately in these prices is going to come back to haunt the markets next month, but more on that later.

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The irony of yesterday's market action was that all of the negative vibes out of Europe that were used as the reason that the Dow hit its low at 11:30am with a 77 point loss were then replaced with the fact that our market did better because of the good economic reports. Now wait a minute – all of these reports were released at 8:30am and the market still went lower. So yesterday's market action was a classic example of how expert observers just "fish" for a reason to explain what the market does based on any reason that fits the action after the fact.

Regardless of the supposed "explanations", one could see that things were going to get better because the Nasdaq went positive first around 12noon while the Dow was still lower by 50 points, and when things are coming off of the lows, when the Nasdaq goes positive first there is a strong propensity for the Dow to follow on the upside, which is exactly what happened as the afternoon wore on. As a result, the Dow was able to achieve an 85 point gain on its high at 3:30pm before another one of those strange very late collapses, and it ended with a closing advance of only 17 points. Now it is true that there were some extenuating factors in distorting the Dow to the downside, such as the highest priced energy component by itself accounting for 22 negative Dow points and the largest retailer was responsible for 10 negative points.

The ratio did stay strong as the Nasdaq ended with a 29 point closing advance and breadth numbers were at a positive 19/11 ratio. The VIX did not really cooperate, as it ended nominally higher by .09 and it was not dropping as much as it should have relative to the Dow's better showing in the afternoon.

And when all else fails to explain why our market declines or advances on any given day, all one has to do is look at the Euro, which reached its low of the day at 1.3500 when our market was also on its low in the morning and then was able to move up from that level to finish at 1.3538 which was still a loss of .0090.

Perhaps it is wishful thinking, but for the first time in a very long time our market was able to do better despite the Euro being lower for the day, but today once again our market is dancing to the tune of the Euro, which is the pattern basically for over a year now. And the reason that the Euro was able to move off of its worst level yesterday was that the new Italian Prime Minister, Monti, is supposedly going to succeed in forming a new government that will have some success in battling the debt crisis.

But the item that is starting to work its malicious effects regardless of whether stocks rise or fall lately is crude oil, which has been in a very steady upward pattern as it continues to advance from the $75 low it reached on October 4th when stocks were on their yearly lows as well, and it got as high as $99.37, an advance of $1. And lest we not forget the ominous implications of this, it was crude oil at $114 in late April that was partly responsible for putting a fast end to the stock market advance at that time.

Today is taking on some similarities to yesterday in the sense that our stock index futures got blasted to the downside early because of ongoing bad news from you-know-where, as the Bank of England Governor said that Britain faces a "markedly weaker" economic outlook and the German Chancellor said that her country is prepared to cede some national sovereignty to the E.U. in order to achieve closer economic and political ties. And once again, those spreads as mentioned above pushed out even wider, as the French-German differential is now close to a full 200 points, heaven forbid.

As a result, the Dow declined to its worst level right off of the opening bell with an early 139 point loss, but was able to cut that loss to "only" 22 points at its best 11:30am level before falling back to a loss of 55 points as this is being written. And the you-know-what also came off of its worst level during this time frame as well, from as low as 1.346, which was the lowest in five weeks, to over 1.352, and here we go again.

And similar to yesterday as well, some economic reports here came in better than expected, with the October C.P.I. showing an overall decline, which will be reversed next month because of energy prices, October Industrial Production and Capacity Utilization coming in better than expected and the November N.A.H.B. housing index rising to its best level since May 2010. So combined with yesterday's good retail sales report, this is further evidence that the U.S. economy is not going to fall into a double-dip recession. Obviously with stocks at very attractive valuations, if the obsession with Europe could ease off, our market has the potential to do much better.

And lurking not so much in the background anymore are crude oil prices, having breached above the $100 a barrel level to trade as high as $102, would you believe it, on the apparent reversal of some pipelines which will now be able to carry crude oil between the Cushing, Oklahoma storage depot and the Gulf Coast, which means that the excess capacity of West Texas intermediate crude oil at that facility can now be alleviated and as a result, this price will be able to "catch up" to the much higher Brent crude oil price, and isn't this the last thing that American consumers need to hear?

Since the Euro has been lower for three straight days, one can see that our market really wants to spring to the upside if we can ever get a day when the Euro would rise, as the end of the earnings season for the third-quarter has shown an overall 15% gain in profits on an 11% advance in revenues. These better earnings plus the decent economic reports means that our market should be much higher if not for the overhang from Europe, especially with these ridiculously low bond yields that compete for investor's attention.

With earnings season for the third-quarter just about over, this week's calendar will be light and dominated by retailers, and lineup finishes with: Thursday: DLTR, GME, GPS, CRM, HNZ, and KIRK.

Economic reports will be more important with a heavier lineup as follows: Thursday – October housing starts and building permits, weekly jobless claims; Friday – November Philadelphia Fed Manufacturing Survey and October L.E.I.

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

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.