Lookout Report
from S&P Valuation and Risk Strategies

Third-Quarter Results May Look Great, But Declining Future Earnings Expectations Are Disconcerting

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The Lookout Report provides cross-market and cross-asset views based upon the unique combined capabilities of S&P Valuation and Risk Strategies, S&P Index Services, Capital IQ, and S&P Leveraged Commentary and Data. Published by S&P's Valuation and Risk Strategies research group, the Lookout Report is a compendium of current data and forward looking insights from leading S&P market specialists. Key areas of focus and differentiation include aggregated corporate earnings, market and credit risk evaluation, capital market activity, index investing and proprietary data and analytics. Featuring interpretations of the investing horizon, the report previews the issues most likely to drive market expectations or cause a disturbance in the weeks ahead.

With more than three-quarters of S&P 500 corporations having reported third-quarter earnings, index members are well on their way to notching the eighth consecutive quarter of double-digit earnings growth. The third-quarter earnings growth rate has steadily increased to 17% from about 12.5% at the start of earnings season. Investors pay extremely close attention to quarterly earnings, which represent periodic report cards on how corporations are performing relative to longer-term investor expectations for future profits, in our opinion. If corporations either meet (or preferably beat) current-quarter consensus earnings expectations, then investors typically remain reasonably confident that firms will also meet future expectations, barring recession.

At face value, while strong third-quarter earnings are clearly a near-term positive development for the equity market, we are also keeping a close eye on calendar-year 2012 consensus earnings expectations, which are simultaneously heading in the opposite direction. Calendar-year 2012 expected earnings had been steadily increasing this year--reaching a peak of $113.41 per share on July 29. Since then, the S&P Capital IQ consensus estimate has dropped to as low as $107.85 on Nov. 1.

We believe that the U.S. stock market is currently in the process of adjusting its inherent valuation to much more moderate forward-looking earnings expectations (see chart 1 and table 1). The combination of better-than-expected current earnings and declining forward earnings expectations is not necessarily problematic for investors, as long as the result is a "soft landing" to respectable levels for future earnings expectations. However, the prospect of stability in the forward earnings estimate will depend greatly on the perceived ability of the U.S. and global economy to maintain growth momentum and avoid recession.

Stabilization of S&P Capital IQ 2012 consensus earnings expectations somewhere within a range of $105 to $110 per share, combined with an underlying U.S. GDP growth rate of 2% or higher, should underpin the bullish case for equities. Combined with a historically modest 12x forward price-to-earnings (P/E) multiple, the $105 to $110 range for 2012 earnings suggests a first-quarter 2012 target range of 1,260 to 1,320 for the S&P 500 Index. The emergence of a healthier economy could return expected earnings to where they were as recently as late July, and might even warrant a more optimistic P/E multiple as well. Likewise, in an environment

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where forward earnings expectations are already declining at a disconcerting pace, rising recession risks will only further reduce expected future earnings, sending many remaining bulls running for cover.

Recent U.S. economic data, notably the healthy 2.5% advance estimate for third-quarter GDP and the better-than-feared October employment report (nonfarm payrolls added 80,000; unemployment at 9%) have helped suppress investor anxiety regarding near-term risks of recession. However, investors will likely require sustained constructive updates on the economy before optimism fully returns to the marketplace.

Chart 1

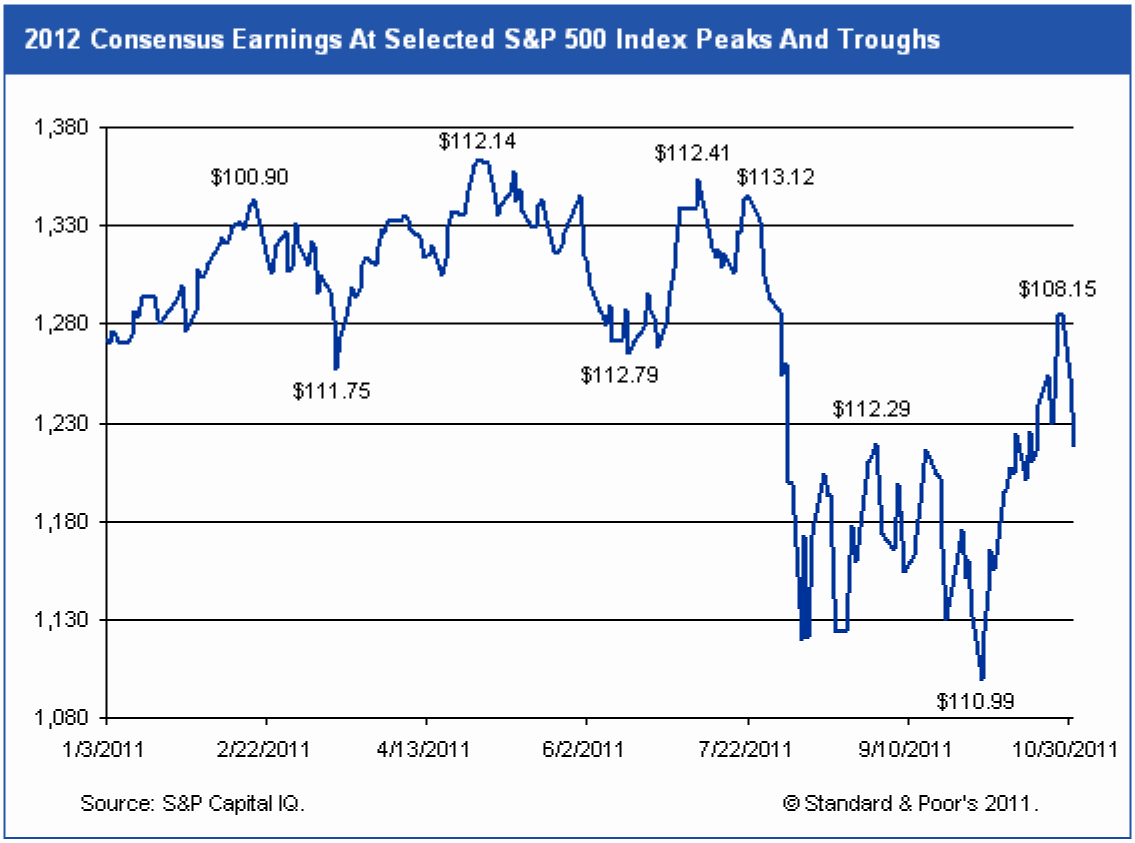


Table 1

S&P 500 Expected 2012 Earnings Per Share At Selected Market Peaks And Troughs

	S&P 500 Index	2012 earnings per share expectations ($)
2/18/2011	1,343.01	110.90
3/16/2011	1,256.88	111.75
4/29/2011	1,363.61	112.14
6/15/2011	1,265.42	112.79
7/7/2011	1,353.22	112.41
7/22/2011	1,345.02	113.12
8/31/2011	1,218.89	112.29
10/3/2011	1,099.23	110.99
10/28/2011	1,285.09	108.15

Source: S&P Capital IQ.

Inside This Issue:

The Broad Macro Overview

Strong third-quarter S&P 500 profit growth is being overshadowed by declining 2012 earnings expectations. Recently improving U.S. economic data and diminishing near-term recession risks, highlighted by today's healthy 80,000 rise in October nonfarm payrolls that were also backed by a substantial 102,000 cumulative upward revision to the prior two months, are counterbalancing declining forward earnings expectations. However, investors likely require sustained pro-growth news on the economy before optimism fully returns to the marketplace.

Economic And Market Outlook: Earnings In North America And Europe

Despite economic uncertainty, S&P 500 companies have continued their trend of strong corporate earnings this quarter. Meanwhile, corporate analysts continued to lower their earnings forecasts for European companies despite progress to resolve the debt crisis in the region.

Leveraged Commentary And Data: After An Early Plunge, The High-Yield Market Reverses Sharply In October

The high-yield market saw two extremes in October, with a sharp sell-off at the beginning of the month and a broad and robust rally into the end of the month. Encouraging economic figures and positive news out of Europe--as leaders there worked toward an agreement to address the debt crisis--fueled the rally.

R2P Corporate Bond Monitor

On the fixed-income markets, risk-reward profiles--as measured by our average Risk-to-Price (R2P) scores--deteriorated in October, breaking the slowly improving trend in most of the sectors that began in September. Scores decreased across the board, except for the energy sector in the U.S. and the industrials sector in Europe.

Market Derived Signal Commentary: Challenges At Home And Abroad Pressure China's CDS

Compared with many sovereign spreads, China's spread remains relatively low risk. However, the trend over the past year, likely spurred by a combination of internal and external factors, makes us cautious. We think the CDS will continue to be subject to volatility in the near term.

Capital Market Commentary: Recent IPO Firms Are Posting Solid Earnings

The recent crop of IPO companies has delivered impressive earnings results. Among the 74 total (excluding closed-end funds and REITs) firms that went public this year, 23 have recently reported third-quarter 2011 results, according to S&P Capital IQ. Of those, 18 exceeded consensus earnings expectations.

S&P Index Commodity Commentary: Lower Rates And Non-Income Producing Assets

Following sharp declines in September, commodity prices have recovered along with other risk assets in the fourth quarter and are gaining additional support from sustained lower interest rates in the U.S., a surprise rate cut by the European Central Bank (ECB), and anticipated rate cuts in China.

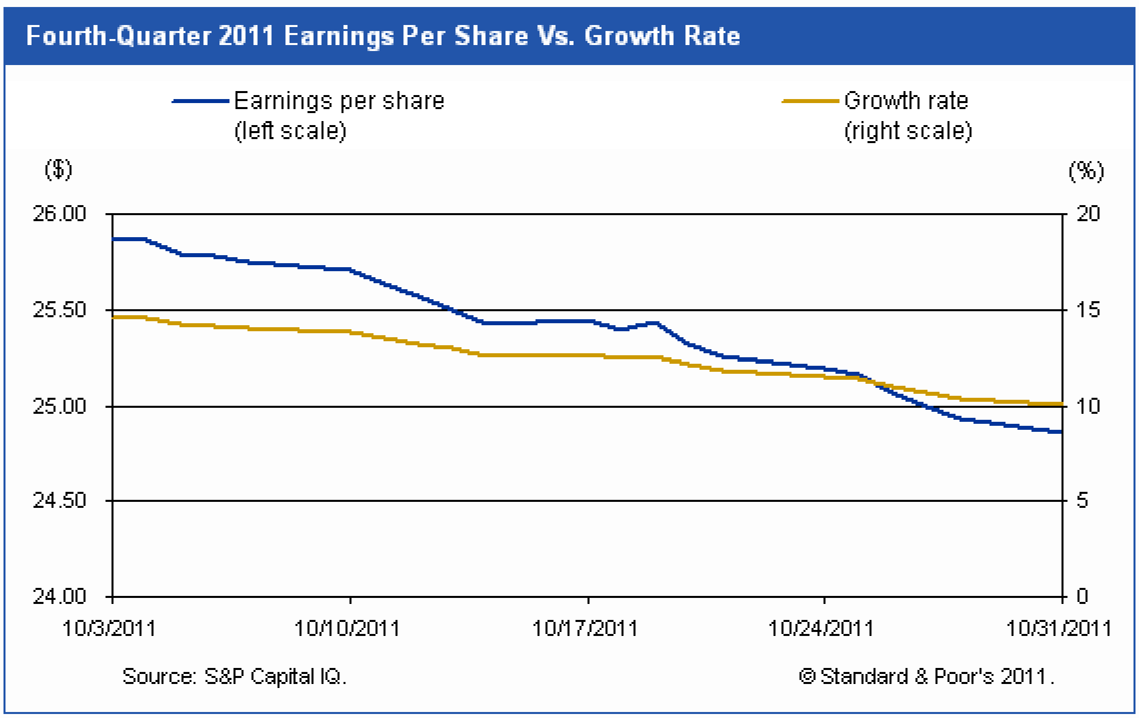
Economic And Market Outlook: Earnings In North America And Europe

North America

Despite economic uncertainty, S&P 500 companies have continued their trend of strong corporate earnings this quarter. Of the 428 companies that have reported results, 65% beat expectations, propelling the third-quarter expected growth rate to 17%. And while markets have rallied on these results, many investors are now looking ahead to the fourth quarter and beyond.

Concerns about fourth-quarter growth have slowly set in. Once expected to be the ninth consecutive quarter of double-digit earnings growth, estimates have dropped into the single digits (see chart 2). At the beginning of the calendar quarter on Oct. 3, fourth-quarter growth was estimated at 14.55%; as of Friday, the estimate had declined to 9.21%.

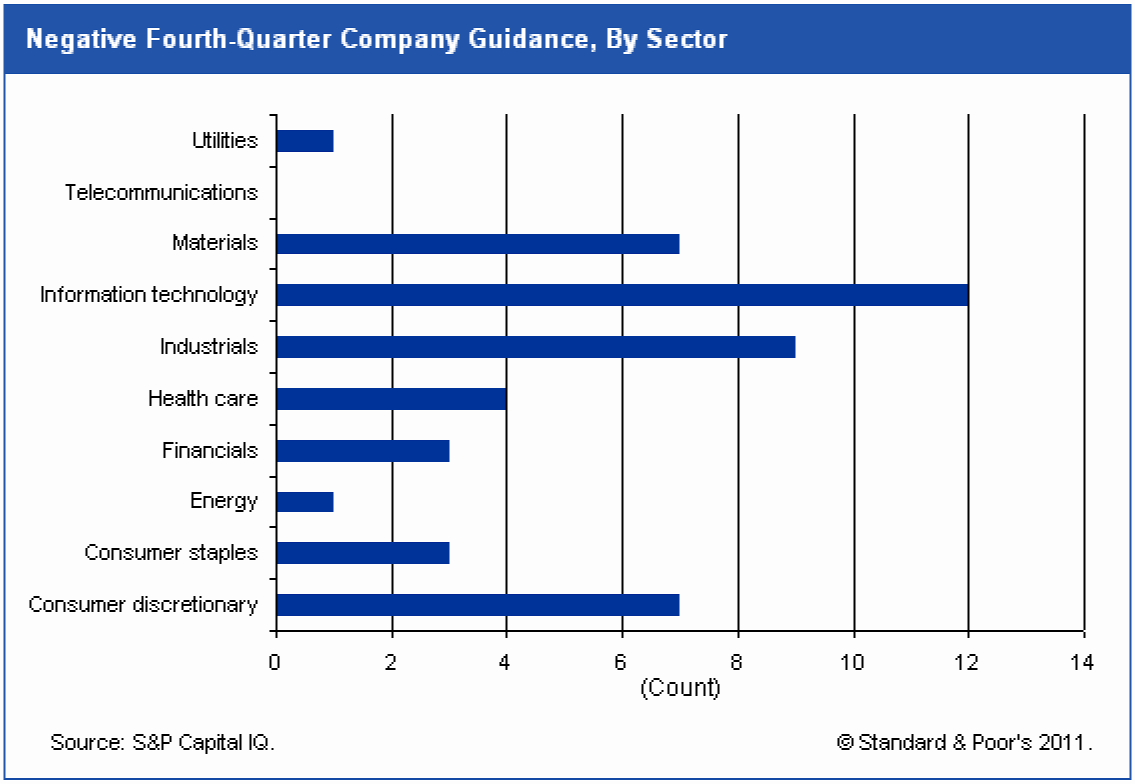
Chart 2



This sharp decline in estimates is especially worrisome as the fourth quarter reporting season is still two months away. However, the large amount of negative guidance from corporations appears to warrant the downward revisions. Of the 78 companies that have issued fourth-quarter guidance, 47 were negative, 22 positive, and nine neutral. These numbers resulted in a negative-to-positive (N/P) ratio of 2.1, meaning that for every one company that provides a positive outlook, 2.1 companies issued negative guidance, much higher than the 1.7 figure for the third quarter and higher than the historical average of 2.0.

This high N/P ratio can be attributed primarily to four sectors. In the information technology sector, 12 companies provided negative guidance, followed by nine in industrials, seven in materials, and seven in consumer discretionary (see chart 3). Not surprisingly, these are the sectors that likely have all of their orders in for the remainder of the year, and therefore have a clearer picture of fourth-quarter results. Consequently, companies in these sectors have lowered guidance because they aren't seeing the same demand in the fourth quarter that they saw in the third quarter.

Chart 3



However, analysts are not just sharply lowering estimates for the fourth quarter--they've also lowered expectations for the first three quarters of 2012. Since Oct. 3, analysts have cut first-quarter, second-quarter, and third-quarter growth estimates by 3.25%, 3.04%, and 6.17%, respectively (see table 2). Expectations for fourth-quarter 2012 have increased by 2.05%, an indication that analysts expect moderate economic growth by the end of the year. The sectors that are expected to decline by the greatest degree in 2012 are the same as those for fourth-quarter 2011.

Table 2

Analyst Estimates Since Oct. 3

	--Quarterly changes (%)--				
	4Q2011	1Q2012	2Q2012	3Q2012	4Q2012
S&P 500	(4.69)	(3.25)	(3.04)	(6.17)	1.42
Energy	(4.67)	(6.36)	(7.22)	(13.25)	(5.41)
Materials	(19.46)	(8.03)	(5.39)	(5.96)	17.67
Industrials	(3.58)	(2.48)	(2.11)	(7.57)	1.11
Consumer discretionary	(4.81)	(2.02)	(2.14)	(0.97)	2.68
Consumer staples	(3.28)	(1.00)	(0.73)	(2.74)	1.00
Health care	(2.09)	1.07	0.14	(3.48)	1.06
Financials	(9.11)	(6.00)	(5.92)	(9.15)	3.47
Information technology	(1.24)	(1.61)	(0.56)	(2.78)	2.12
Telecommunication	(15.87)	(12.42)	(7.76)	(9.79)	5.63
Utilities	(4.20)	(0.40)	(0.28)	(3.71)	4.01
Ex-financials	(3.92)	(2.68)	(2.50)	(5.59)	1.08

Source: S&P Capital IQ.

Analysts have cut estimates the most for materials, telecommunications, financials, and energy since Oct. 3. Materials and energy, the two growth leaders for most of 2011, can no longer depend on the large year-over-year benefits they received from higher commodity prices. While prices of WTI crude are still higher on average for fourth-quarter 2011 ($87.12) than they were in the year-ago period ($85.59), those prices have fallen significantly from the $95 per barrel average in the first quarter of this year. Similarly, steel prices (domestic hot-rolled coil), have fallen since the beginning of 2011, but still remain higher year over year. During October, steel prices averaged $702 per short ton, compared with the $554 average for fourth-quarter 2010. However, the price has dropped nearly 8% since the beginning of the year. In addition, many companies in both of these sectors stated in their quarterly reports that demand was down from the first half of the year.

Estimates for 2012 declined sharply for financials, a sector that managed to do much better than expected in the third quarter despite the unfavorable macroeconomic climate. The sector growth rate has been reduced by 5% or more for the upcoming four quarters, but despite this, the S&P Capital IQ consensus still expects the second-strongest growth rate next quarter at 17.12%.

The telecommunications sector, with the exception of the third quarter, has been a laggard for the majority of this year. With only nine companies in the sector, a loss by one company can have a large affect on the entire sector. Of the nine companies, seven have already reported for the third quarter, and only one (CenturyLink Inc.) beat estimates, while three missed and three met. These poor results, plus the companies' own uncertain outlook, makes the sector a target for further cuts by analysts.

The future of 2012 growth estimates all depends on forthcoming economic indicators and the results of the final 15% of S&P 500 companies left to report third-quarter earnings. Today's employment report was a little disappointing, but not devastating, as nonfarm payrolls came in slightly lower than expectations of 90,000, with 80,000. On a positive note, the unemployment rate edged lower to 9.0%, from the consensus estimate of 9.1%, which was also the rate for the prior month.

Europe

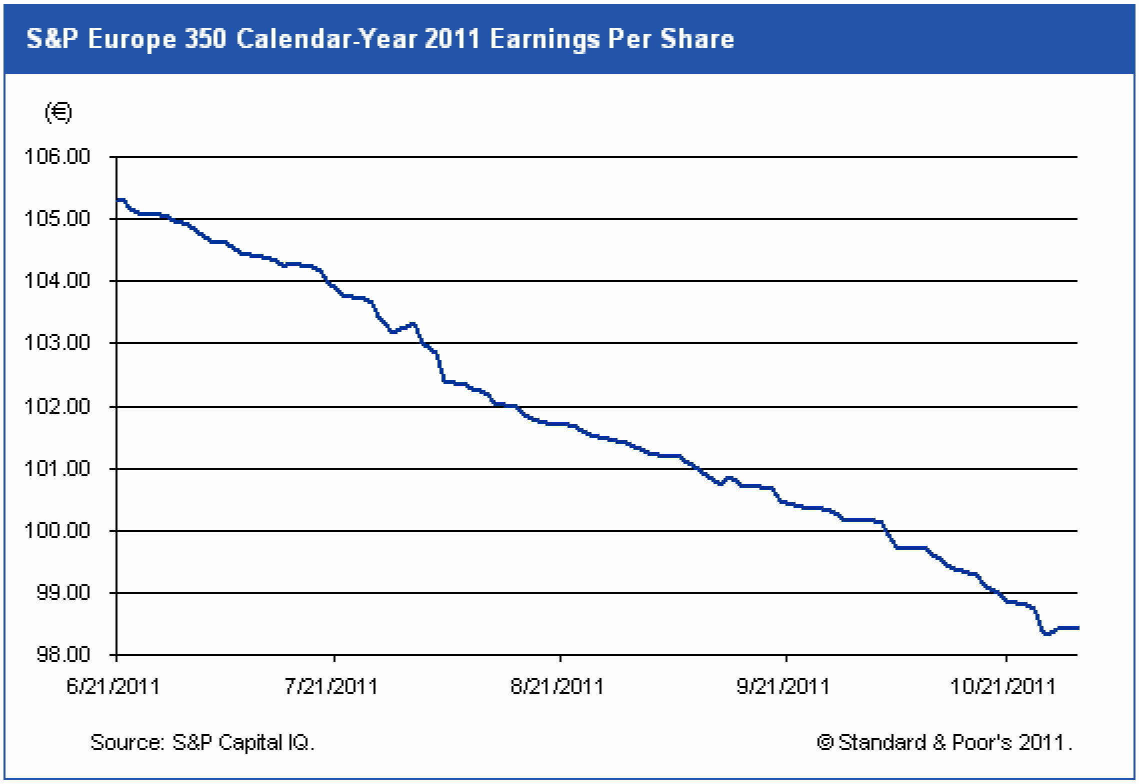
Over the two-week period ended Oct. 28, analysts continued to lower their consensus calendar-year 2011 expectations for the S&P Europe 350 Index to €98.41 from €99.40, a 1% drop to the lowest level since the start of the third quarter, according to S&P Capital IQ data (see chart 4). This continues the longstanding trend, which, for instance, reduced 2011 anticipated earnings from €105.14 at mid-year 2011. Consensus expectations for S&P Europe 350 2012 calendar-year earnings decreased by 1.4% to €108.52 as of Oct. 28, compared with €110.34 on Oct. 14.

Last week, the European governments agreed to write down 50% of bank holdings of Greek debt and to recapitalize European banks to about €106 billion by June 2012. In addition, leaders planned to increase the main bailout fund to €1 trillion from €440 billion. Despite this progress to resolve the debt crisis, corporate analysts continued to lower their earnings forecasts for the companies within the region, a trend that began in early summer.

For the past two weeks, the earnings consensus for the cyclical energy, materials, industrials, consumer discretionary, and financials sectors decreased the most of the 10 sectors. For all 10 sectors, 2012 calendar-year earnings decreased, while 2011 calendar-year earnings increased for just two sectors.

As the European quarterly reporting season continues, only 44% of companies have already reported. Of these, more than half (58%) have exceeded expectations, and the remaining 42% have missed expectations.

Chart 4



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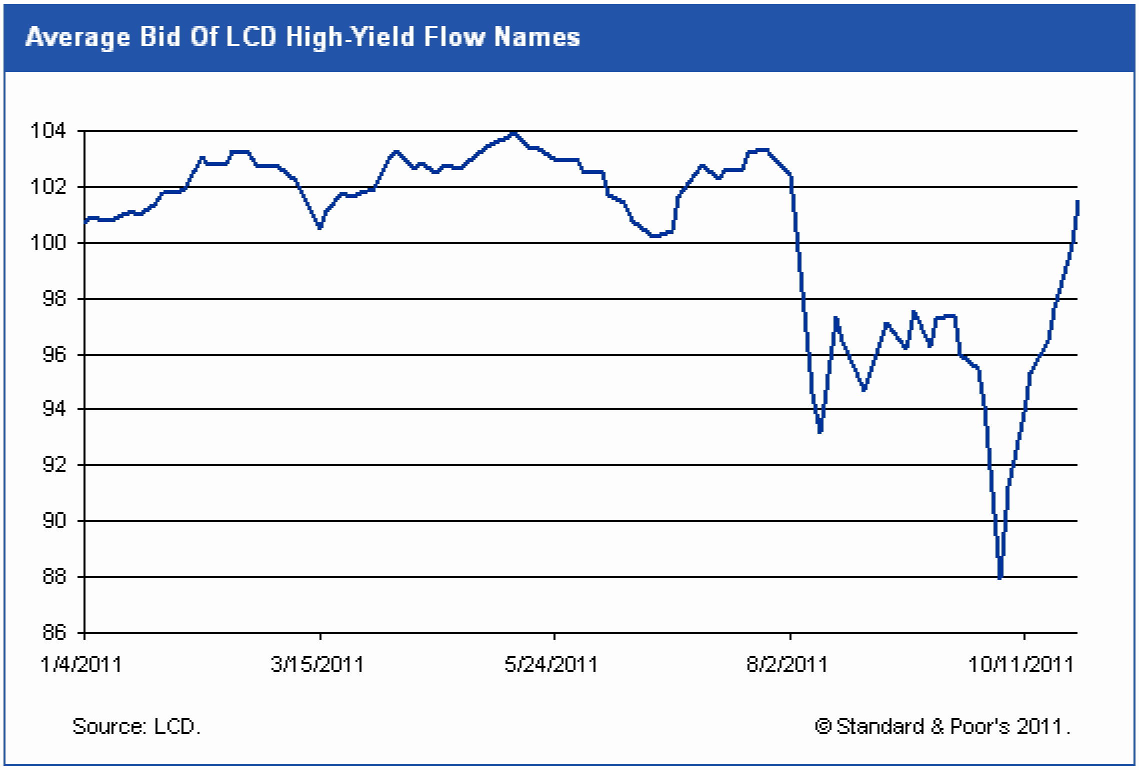
Leveraged Commentary And Data: After An Early Plunge, The High-Yield Market Reverses Sharply In October

The high-yield market saw two extremes in October, with a sharp sell-off at the beginning of the month and a broad and robust rally into the end of the month. Encouraging economic figures and positive news out of Europe--as leaders there worked toward an agreement to address the debt crisis--fueled the rally.

Performance of Leveraged Commentary and Data's (LCD) flow-name bond composite reflected the sharp fluctuations in October. The average bid of the sample of 15 liquid benchmarks plunged 6.2 points in the Oct. 4 reading to 87.93% of par, yielding 10.4% (see chart 5). That was the largest drop on record and left the price component at its lowest level in more than two years. However, it was the last decline recorded in October, and the average bid posted a cumulative gain of more than 13.5 points over the following seven readings during the month.

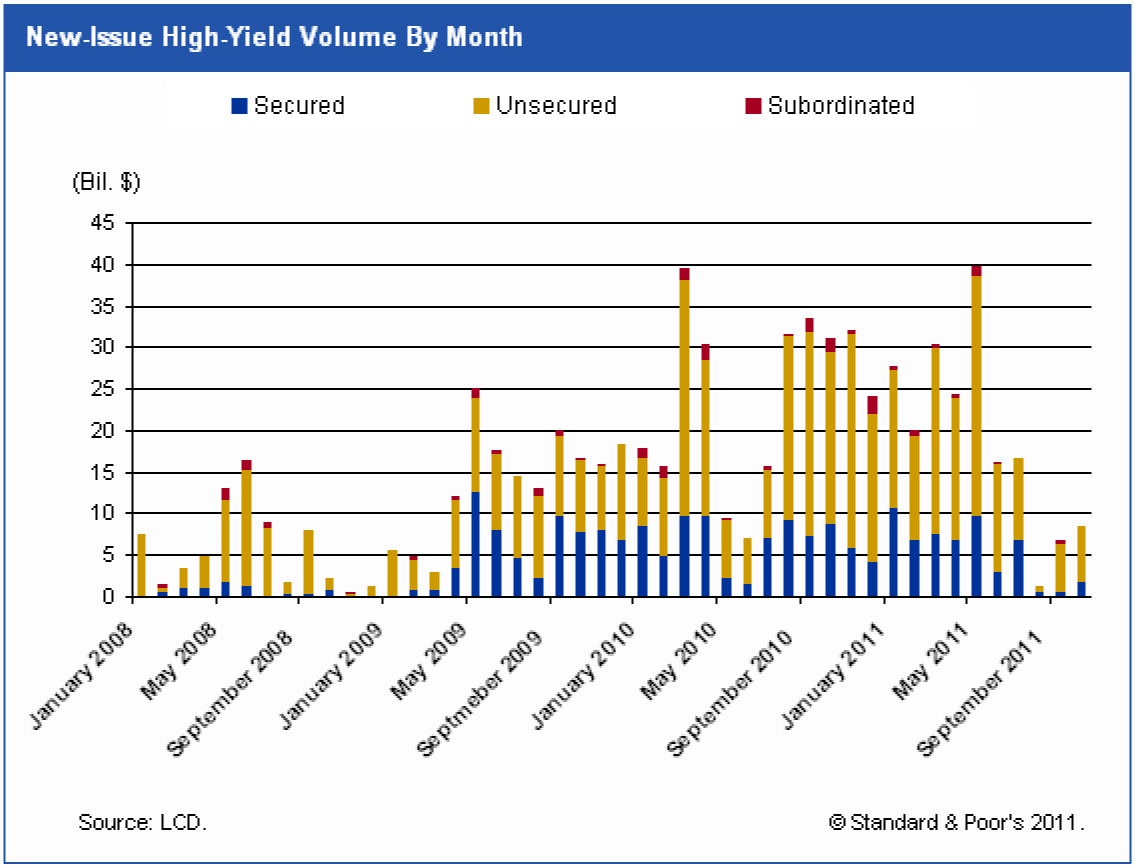
Chart 5



As investors shook the risk-averse sentiment, heavy retail inflows bolstered the rally. For the four weeks ended Oct. 26, Lipper FMI reported net fund inflows of $6.8 billion, which includes last week's influx of $4.2 billion, the largest ever for the weekly reporter group.

The better tone in the second half of the month allowed for a reopening of the primary market. Volume in October rose to $9.4 billion from $6.8 billion in September (see chart 6). However, volume is still much lower than the 2011 monthly average of $19 billion. That left year-to-date volume at $191.2 billion, down 17% from the same period a year ago. For reference, 2011 volume was running 34% higher versus 2010 at the end of the second quarter.

Chart 6



Marked improvement in high-yield over the past few weeks has led to a more active new-issue market in the fourth quarter than expected at the outset. Participants project November volume to build on October's output, and the shadow calendar is again brimming with potential business, stoked by large merger and acquisition (M&A) deals.

The average yield for new issues in October (excluding split-rated deals and Ford Motor Credit's three-year notes) was 8.8%, lower than the 9.3% average for deals priced in August and September combined. Granted, roughly half of this month's volume total was from 'BB' rated issues, but it also included several 'CCC' deals. In a show of demand, follow-on interest in the secondary, particularly over the past week, had many of these issues scoring multiple-point gains in the secondary.

Use of proceeds was fairly diverse for deals last month. Refinancing existing debt accounted for about $4.7 billion of the total, while M&A and leveraged buyout (LBO) activity took $2.7 billion of the pie. Another $1.9 billion was designated for various corporate purposes.

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R2P Corporate Bond Monitor

Through October, market participants remained concerned about the possibility of a disorderly Greek default and exit from the eurozone. Amid a wave of strong earnings reports, leaders are assembling at the G20 summit in Cannes, while the European Central Bank (ECB) recently announced a surprise interest rate cut by 0.25% to 1.25%. According to International Monetary Fund (IMF) Chief Christine Lagarde, leaders are determined to take decisive action in a "coordinated fashion." On Nov. 2, 2011, the day before the G20 summit, French President Sarkozy and German Chancellor Merkel met with Greek Prime Minister George Papandreou for crisis talks and attended a joint press conference.

On a more positive note, China has become an increasingly important part of the eurozone story. In Cannes, Zhang Tao, director of the international department of the People's Bank of China, said that Europe is China's largest trading partner, China-EU relations are very close, and that China views Europe as a key investment area for the foreseeable future.

In the U.S., the Federal Reserve cut its growth forecasts for 2011 and the next two years and did not introduce immediate additional measures to stimulate the U.S. economy as some had hoped. However, the Federal Open Market Committee (FOMC) continues to expect a moderate pace of economic growth over coming quarters and consequently anticipates that the unemployment rate will decline gradually toward levels consistent with their dual mandate for employment and price stability. In addition, similar to the previous quarter, S&P 500 companies' third-quarter results remain strong. Of the 428 companies that have reported, 65% have exceeded expectations.

On the fixed-income markets, risk-reward profiles--as measured by our average Risk-to-Price (R2P) scores--deteriorated in October, breaking the slowly improving trend in most of the sectors that began in September (see tables 3 and 4). Scores decreased across the board, except for the energy sector in the U.S. and the industrials sector in Europe.

In the U.S., although the average probability of default (PD) declined by 20%, scores deteriorated by 5% due to lower corporate bond returns and an increase in market risk. Option-adjusted spreads (OAS) tightened by 19 basis points (bps), while bond price volatilities increased by 23%.

Unlike the U.S., the average PD in Europe increased by 14%. Subsequently, score deterioration was due to both an increase in market risk and in credit risk. The overall PD increase, combined with 7% higher bond price volatilities and 22 bps tighter OAS, explains the 5% score decline.

Table 3

North American Risk-Reward Profiles By Sector--Average R2P Score And Components Changes

	Scores (%)	OAS (bps)	PD (%)	Bond price vol. (%)
Consumer discretionary	(2)	(35)	(18)	25
Consumer staples	(9)	10	(12)	3
Energy	5	(35)	(28)	32
Financials	(5)	(21)	(15)	15
Health care	(10)	(37)	(43)	26
Industrials	(2)	(17)	(24)	20
Information technology	(2)	(9)	(25)	19
Materials	(4)	(3)	(25)	33
Telecommunication services	(6)	(30)	8	38
Utilities	(14)	(17)	(14)	22

Change as of Nov. 1, 2011, from Sept. 30, 2011.

Table 4

European Risk-Reward Profiles By Sector--Average R2P Score And Components Changes

	Scores (%)	OAS (bps)	PD (%)	Bond price vol. (%)
Consumer discretionary	(6)	(7)	(14)	25
Consumer staples	(12)	(21)	109	21
Energy	(2)	(31)	14	(8)
Financials	(4)	(18)	(6)	(2)
Health care	(10)	(2)	20	28
Industrials	5	(25)	(24)	(11)
Information technology	(17)	(41)	32	(13)
Materials	(11)	(38)	15	10
Telecommunication services	(8)	(23)	10	16
Utilities	14	(13)	(12)	5

Change as of Nov. 1, 2011, from Sept. 30, 2011

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Market Derived Signal Commentary: Challenges At Home And Abroad Pressure China's CDS

In an effort to avert a complete meltdown of the euro, eurozone leaders turned to China to help boost the European Financial Stability Facility (EFSF) to €1 trillion. The head of the rescue fund, Klaus Regling, said it was in China's own interest to help resolve the debt crisis, Reuters reported on Oct. 29. China, which has been a buyer of EFSF bonds, is awaiting further details before committing to an investment in what may be structured as a special purpose vehicle. At the end of September, China's foreign exchange reserves stood at a record $3.2 trillion.

In China, GDP growth continues, though at a consecutively slower pace, through three quarters (9.7% in the first quarter, 9.5% in the second quarter, and 9.1% in the third quarter, according to Bloomberg). The economy expanded 10.4% in 2010. The global economic slowdown has hurt exports, particularly to Europe, which is China's largest market, so risks associated with external factors are a mounting concern. In September, China's export growth rate fell to 17.2% from 24.5% in August.

Internally, consumer price inflation in September declined to 6.1% from 6.2% in August and a three-year high of 6.5% in July. Although the indicator is headed in the right direction, by historical standards, it is quite high--average inflation over the past 10 years was only 1.6%, according to Standard & Poor's Ratings Services.

"Some officials think that excess domestic liquidity is driving up prices and believe that additional quantitative easing in the developed economies could fuel inflation further," Standard & Poor's said (see "Report Card: Asia-Pacific Sovereigns: Is the Positive Rating Trend on Hold?," published Sept. 19, 2011, on the Global Credit Portal). "Therefore, the government has maintained a tight monetary policy despite deteriorating growth prospects in the global economy."

Standard & Poor's expects China's policymaking to be increasingly cautious heading into 2012, as top leadership makes way for the next generation. Current Chinese President Hu Jintao is expected to step down from his role as Communist Party leader in the second half of 2012 and as the president in 2013. Also next year, Premier Wen Jiabao is expected to leave the post he's held since March 2003.

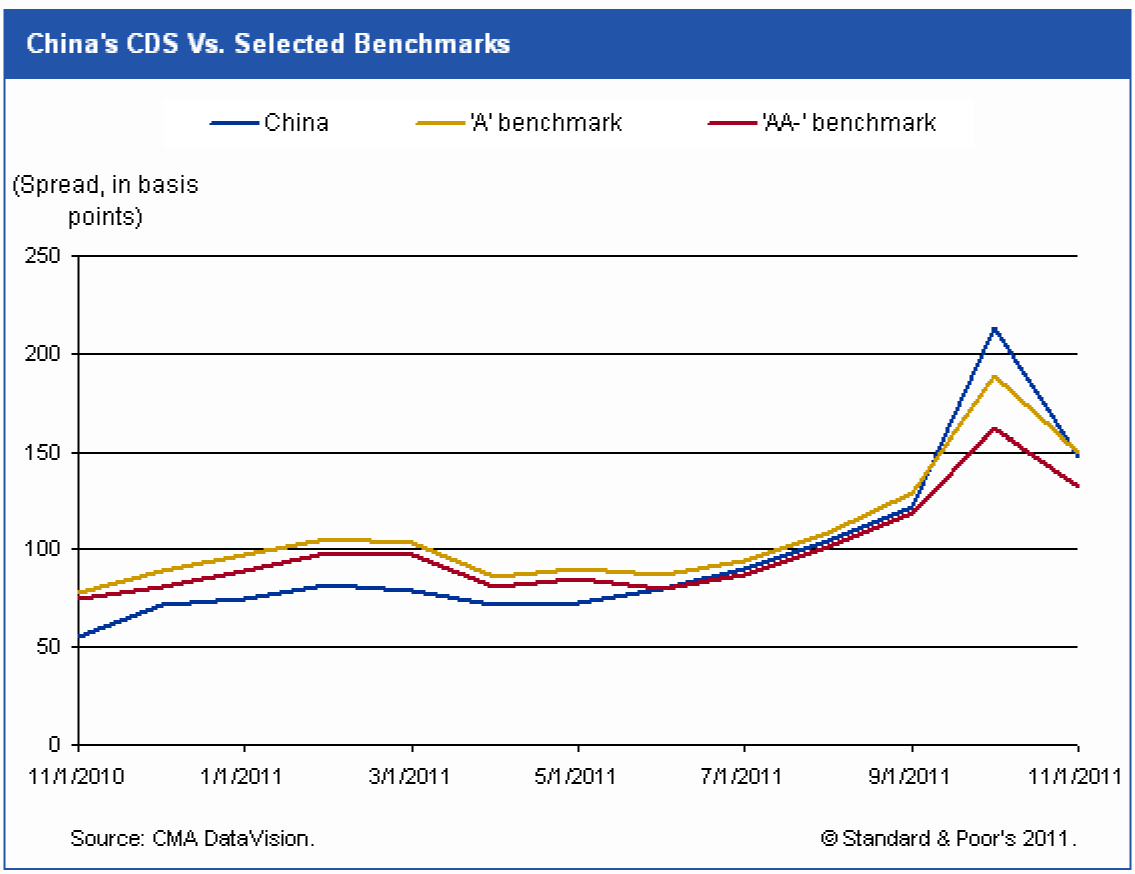
"An abrupt slowdown in the developed economies--more likely now than earlier this year--could lead to another round of layoffs in the export sector," Standard & Poor's said.

"Social pressures could build up if these layoffs happen without a fall in consumer price inflation. The government is likely to face policy considerations that could be much more complicated than in 2008 if another recession hits the global economy. Due to the recent experience of strong credit growth, inflation expectations are higher than before. So, the liquidity unleashed by another round of credit easing could fuel inflation even before it creates jobs."

Standard & Poor's has a rating of 'AA-' with a stable outlook on China, reflecting the country's low debt, strong external assets, and "exceptional" economic growth prospects (see "China's Renminbi-Denominated Bonds Assigned 'AA-' Rating And Greater China Credit Scale Rating Of 'cnAAA'," published Aug. 18, 2011). China's high single-digit GDP growth could be maintained if the country takes steps to improve productivity, which is in many cases burdened by price controls, government interference in business, and the lack of a cohesive set of regulations, Standard & Poor's said (see "Efficiency Gains Could Keep China's Economy On Full Throttle," published Sept. 12, 2011).

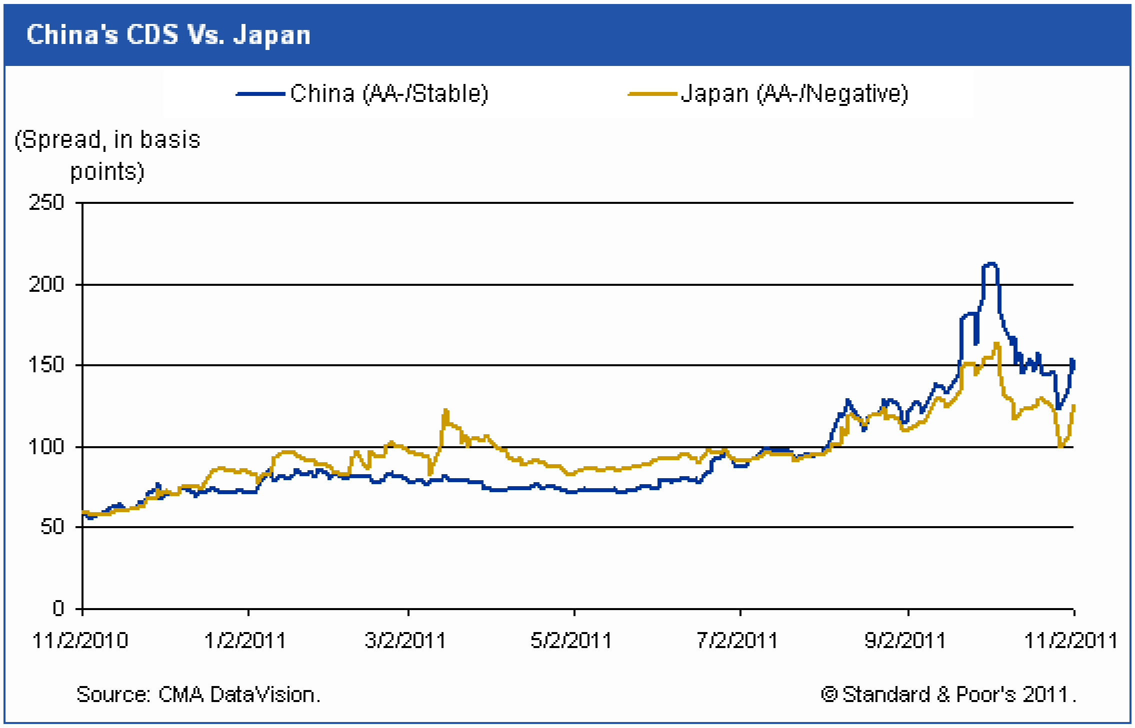
Against this backdrop, China's five-year credit default swap (CDS) spread has nearly tripled over the past year to 148 basis points (bps) as of Wednesday from an average of 55 bps as of November 2010, according to CMA DataVision. The average high over the past year was 213 bps in October 2011; the all-time high was 260 bps on March 2, 2009. The spread is wide of its credit rating benchmark by 16 bps but in line with the Market Derived Signal rating of 'a' (see chart 7).

Chart 7



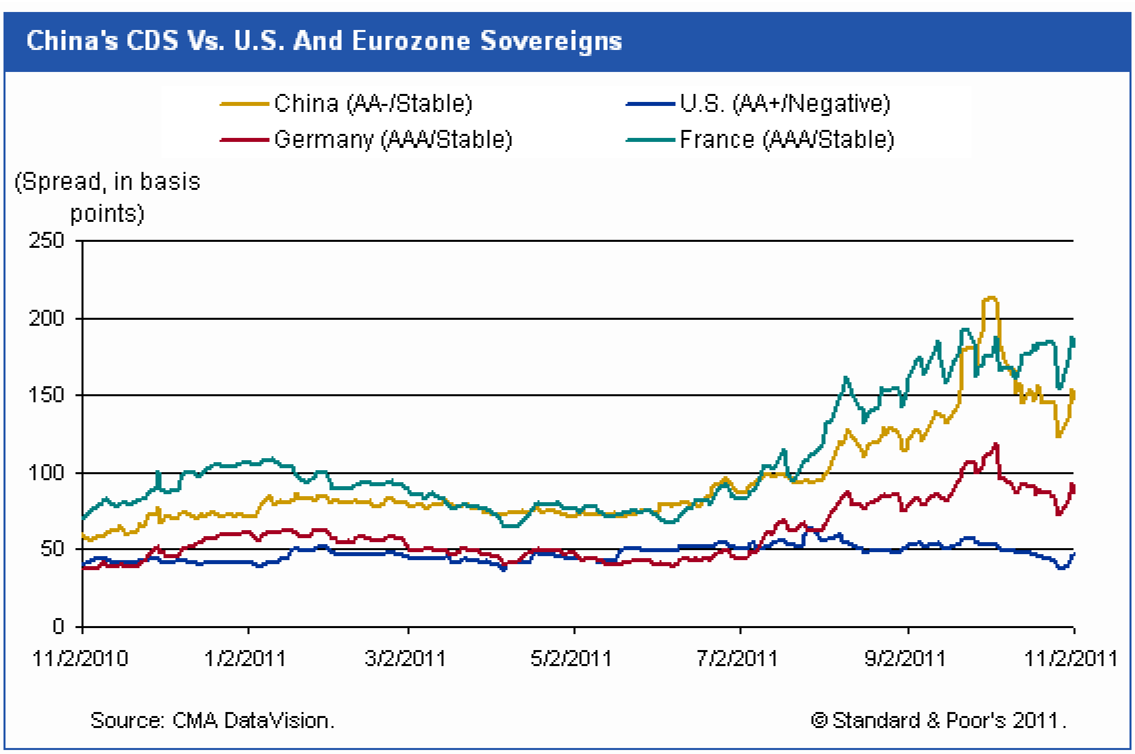
China's spread is currently 23 bps wide of Japan's spread of 125 bps. Standard & Poor's has a rating of 'AA-' with a negative outlook on Japan (see chart 8).

Chart 8



China's CDS is far wide of the spreads for the higher-rated Germany and the U.S., but it is tight of 'AAA' rated France (see chart 9).

Chart 9



Compared with many sovereign spreads (Spain, 359 bps; Italy, 474 bps; for example), China's spread remains relatively low risk. However, the trend over the past year, likely spurred by a combination of internal and external factors, makes us cautious. We think the CDS will continue to be subject to volatility in the near term, so we will monitor its trajectory for any significant deviation.

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Capital Market Commentary: Recent IPO Firms Are Posting Solid Earnings

IPOs

With the completion of Groupon's $700 million initial public offering (IPO), some potential investors have concerns about the offering's relatively small size; the company sold less than 5.6% of its outstanding shares. In fact, a review of S&P Capital IQ data reveals that since 2010, only 11 IPOs priced on major U.S. exchanges came to market with between 0.1% and 5.0% of their outstanding shares. Of those companies, only five have recently traded above the offer price. Still, at the time of this writing, the Groupon shares were trading above its offer price of $20 per share on its first trade day.

Meanwhile, the recent crop of IPO companies has delivered impressive earnings results. Among the 74 total (excluding closed-end funds and REITs) firms that went public this year, 23 have recently reported third-quarter 2011 results, according to S&P Capital IQ. Of those, 18 exceeded consensus earnings expectations, while two met and three missed. Among those the companies that delivered better-than-expected-results, several were previously acquired by financial sponsors, including HCA Holdings Inc., GNC Holdings Inc., and Dunkin' Brands Inc.

Although the pace of issuance has been slow recently, one of last month's offerings--Ubiquiti Networks--ranks among the leading performers among IPOs in the information technology sector this year (see table 5).

Table 5

U.S. Technology IPOs Year-to-Date 2011 Performance

Closed date	Target/Issuer	Transaction value (mil. $)	Latest price ($)	Price per share ($)	Change (%)
5/18/2011	LinkedIn Corp.	352.8	88.9	45.0	97.6
6/8/2011	Fusion-io Inc.	233.7	30.1	19.0	58.4
10/13/2011	Ubiquiti Networks Inc.	105.6	20.5	15.0	36.4
7/19/2011	Zillow Inc.	69.2	26.6	20.0	33.2
6/16/2011	Bankrate Inc.	300.0	19.8	15.0	31.9
3/24/2011	ServiceSource Corp.	119.4	13.0	10.0	30.0
7/26/2011	Tangoe Inc.	87.7	12.2	10.0	21.9
8/10/2011	Carbonite Inc.	62.5	12.2	10.0	21.5
3/16/2011	Cornerstone OnDemand Inc.	136.5	14.3	13.0	10.3
5/25/2011	The Active Network Inc.	165.0	12.8	15.0	(14.9)
4/20/2011	Responsys Inc.	79.4	10.2	12.0	(15.0)
4/14/2011	Ellie Mae Inc.	45.0	5.1	6.0	(15.2)
5/25/2011	Freescale Semiconductor Holdings I Ltd.	783.0	12.2	18.0	(32.5)
2/1/2011	NeoPhotonics Corp.	82.5	5.0	11.0	(54.7)
1/25/2011	Demand Media Inc.	151.3	7.2	17.0	(57.7)
5/10/2011	FriendFinder Networks Inc.	50.0	1.8	10.0	(81.9)

Data as of Nov. 2, 2011. Source: S&P Capital IQ.

M&A

While acquisitions of U.S. companies and assets have rebounded this year, so have U.S. purchases of foreign businesses and operations. U.S. foreign merger and acquisition (M&A) activity through the first 10 months of the year is up by more than 56% from the year-ago period (see table 6). Deal volume in three sectors--telecommunications, information technology, and utilities--has more than doubled this year from the year-ago period. On the other hand, U.S. overseas purchases have declined in the energy, financial, and consumer staples sectors. Because a significant portion of the more than $1.1 trillion in nonfinancial S&P 500 short-term investments and cash is held overseas, prospects remain solid for U.S. purchases abroad.

Table 6

Foreign Acquisitions By U.S. Buyers

Sector	January 2010 to October 2010 (bil. $)	January 2011 to October 2011 (bil $)	Change (%)
Telecommunications	1.6	13.3	731.3
Information technology	8.3	28.2	239.8
Utilities	2.5	7.0	180.0
Industrials	15.2	28.7	88.8
Consumer discretionary	15.2	25.4	67.1
Materials	9.0	11.9	32.2
Health care	9.7	11.6	19.6
Energy	5.0	4.9	(2.0)
Financials	19.7	15.8	(19.8)
Consumer staples	4.5	3.1	(31.1)
Other	6.3	1.6	(74.6)
Total	97.0	151.5	56.2

Source: S&P Capital IQ.

Debt

Following back-to-back months of more than 1,000 CUSIP requests for domestic corporate debt securities, October identifier demand retreated to 793 requests, the lowest monthly count since May 2010 (752 orders). While not necessarily a red flag given the strong pace of identifier requests in August and September, the recent results nonetheless may suggest that capital market volume may be lean in the short term. On the other hand, international debt securities CUSIP orders increased in October, marking the first back-to-back month of gains since September 2009 to October 2009. To that end, the past five-month-long slide may be giving way to some stabilization.

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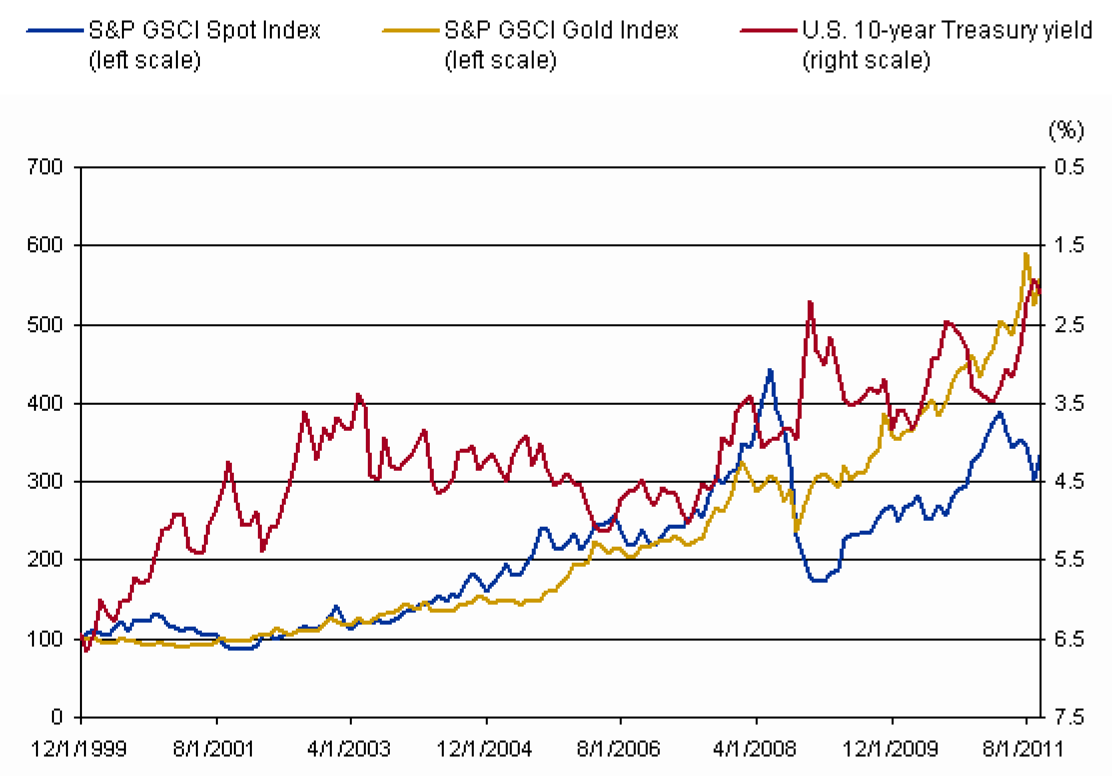
S&P Index Commodity Commentary: Lower Rates And Non-Income Producing Assets

The S&P GSCI gained 8.91% in the fourth quarter as of Nov. 2, recovering from its September swoon and narrowing the year-to-date decline to 0.76%. Strength in petroleum prices, a 9.58% increase in the S&P 500 Index, and a 1.82% decline in the U.S. Dollar Index have supported fourth-quarter gains. Crude oil has been the best performing commodity in the fourth quarter, reflected in the S&P GSCI Petroleum Index's increase of 11.39%, as the futures term structure shifted into backwardation for the first time since 2008. Reflecting tightening supply and demand conditions, all five S&P GSCI petroleum commodities ended the month in backwardation, which has a tendency to boost index total returns due to rolling futures into lower prices on the term structure. Anticipation of lower interest rates in China, a surprise rate reduction by the ECB, along with the reassurance from the FOMC of sustained low base rates, coinciding with the purchase of longer-dated bonds, has provided an additional boost to commodities in November.

Commodities are the most liquid non-income producing assets. Prices are ultimately determined by supply and demand, but base interest rates are a key opportunity cost factor of investing in commodities. While demand continues to increase rapidly in developing countries, most interest rates continue to decline in developed countries, providing an additional boost to commodities. Since the end of 1999, the U.S. two-year Treasury note yield declined from about 6.00% to 0.24% as the S&P GSCI Spot Index increased 231% as of Nov. 2. Lower interest rates have played a roll in appreciating commodities, certainly in the case of the quintessential non-income producing asset: gold. Since base interest rates are near zero in most developed countries, many market participants are looking to the longer-dated bond market for signs of change in the lower rate trend. Chart 10 depicts the similar trends of the S&P GSCI Spot Index, the S&P GSCI Gold Index, and the U.S. Treasury 10-year note yield (inverse). Since the advent of quantitative easing, price increases for many commodities have accelerated, led by precious metals and energy, leading many market analysts to opine that extremely low base interest rates and policies, such as quantitative easing, are providing a substantial boost to commodities.

Chart 10

Selected S&P GSCI Indices Vs. U.S. 10-Year Treasury Yield



Source: S&P Indices. © Standard & Poor's 2011.

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