Lookout Report
from S&P Valuation and Risk Strategies

European Credit Concerns Counteract Strength In U.S. Retail Sales

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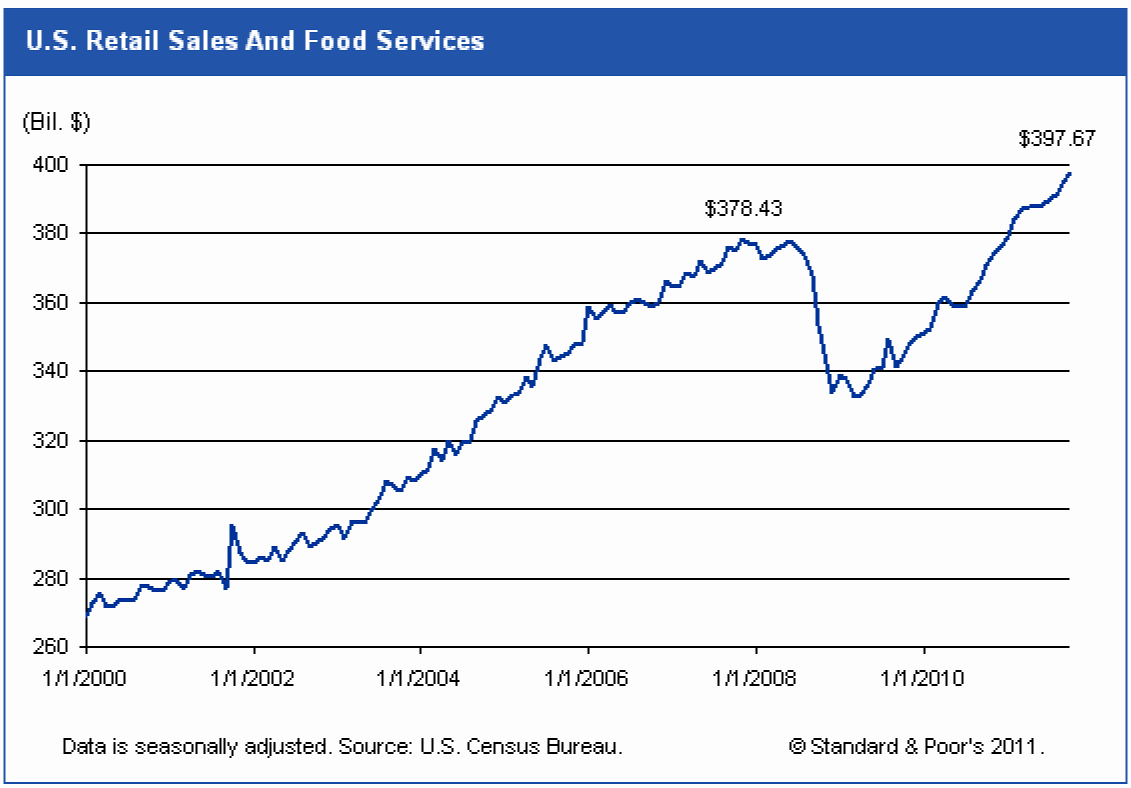
The Lookout Report provides cross-market and cross-asset views based upon the unique combined capabilities of S&P Valuation and Risk Strategies, S&P Index Services, Capital IQ, and S&P Leveraged Commentary and Data. Published by S&P's Valuation and Risk Strategies research group, the Lookout Report is 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.

Following a very strong 1.1% monthly gain in September, U.S. retail sales rose by an additional 0.5% in October to $397.7 billion, setting yet another all-time record high for this data series. Continuing the trend of 7% to 8% year-over-year growth, retail sales have set new records each month this year, excluding May, when sales marginally decreased to $387.5 billion from $387.7 in April (see chart 1). Through the economic "soft patch" that started in the second quarter, which led to talk of recession in the third quarter, steadfast U.S. consumers continue to do their part in keeping the U.S. and global economy (through imports) moving forward. We believe that consistently strong retail sales data are at the core of the buy-on-weakness investor psychology that has repeatedly brought investors back to the equity market throughout 2011.

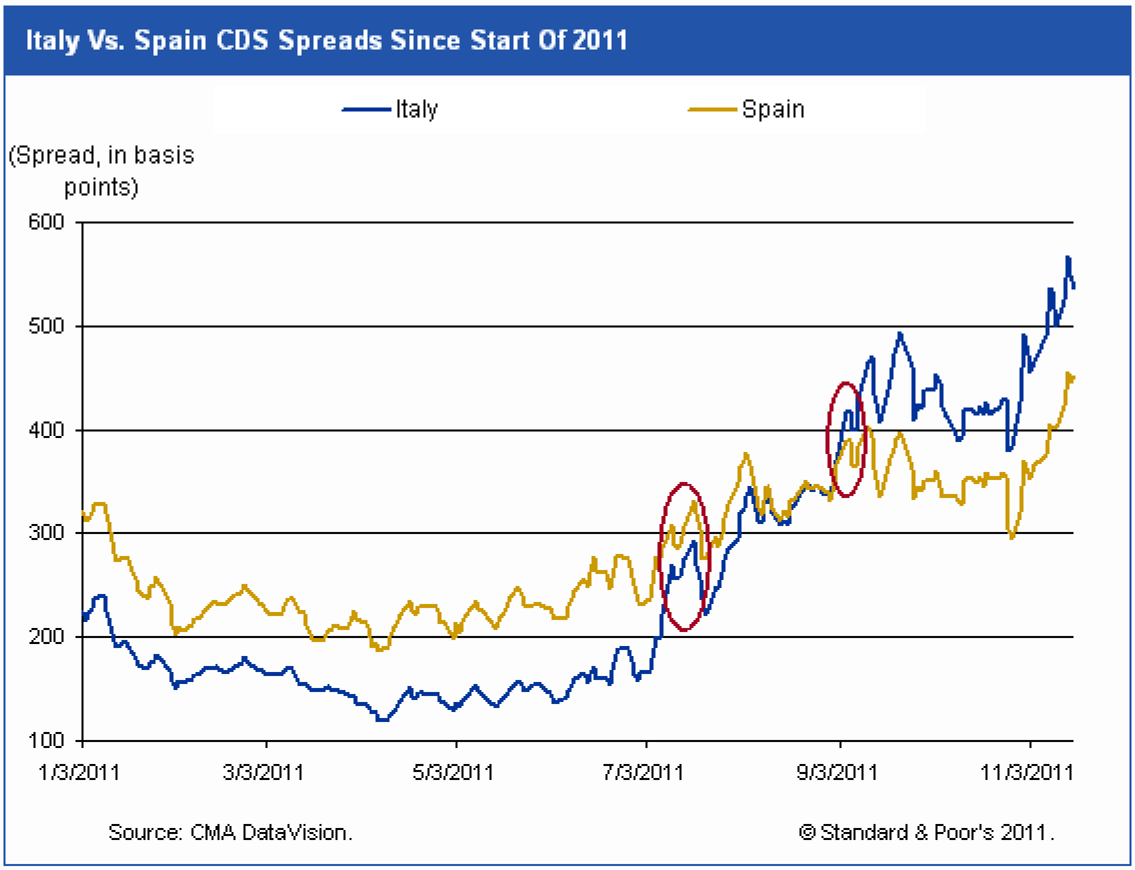
Chart 1



November 18, 2011

European sovereign fiscal solvency represents the opposite end of the spectrum for investor psychology this year. After spending most of 2011 fretting over the solvency of Greece, investors have now turned their collective attention toward larger concerns such as Spain and--especially--Italy. Credit default swap (CDS) spreads for both of these countries posted new 2011 highs in mid-July, with Italy's CDS spread exceeding that of Spain by early September (see chart 2). Italy and Spain have both recently posted new record high CDS spreads in excess of 500 basis points (bps) and 400 bps, respectively, which--for perspective--is now in line with the CDS levels associated with Greece in April 2010.

Chart 2



Simmering risks of another global banking crisis--this time from fiscal concerns in Europe--have repeatedly short-circuited the stock market's attempts to sustain rallies this year following successive quarterly reports of much better-than-anticipated S&P 500 corporate earnings. As credit concerns surrounding Europe escalate, so do risks of a credit-induced recession for the European economy. This is a legitimate concern for anyone invested in U.S. equities, since nearly half of contemporary S&P 500 corporate revenues originate from non-U.S. sources.

As long as U.S. macroeconomic fundamentals like retail sales remain strong while European fiscal anxiety continues to rise, investors will likely continue to trim net-exposure to risk assets following periods of market strength, but then look to reenter the market on weakness. How far risk asset prices can increase will depend on the net-balance between these two opposing forces of influence. Prospects for the U.S. economy may appear to be improving, but European credit concerns unfortunately are spreading and reaching new highs in the absence of a workable solution, according to the recent CDS spreads associated with both Italy and Spain.

Inside This Issue:

Macroeconomic Overview

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Economic And Market Outlook: Earnings In North America And Europe

While S&P 500 retailers reported a robust third quarter on increasing strength in consumer spending, the fourth quarter will be even more telling as the holiday season determines how willing shoppers are to spend their discretionary income. Meanwhile, analysts in Europe continued to lower their consensus calendar-year 2011 expectations for the S&P Europe 350 Index, now at their lowest level since the start of the third quarter.

S&P Index Equity Commentary: Everything Is Beautiful, At Least On Paper

Overall, third-quarter numbers for the S&P 500 Index are good on both the balance and income sheets, with strong earnings and cash flow helping to drive the current market. Operating earnings and as reported earnings both set records, both with or without the special valuation gains reported by the bulge bracket firms, and topped the previous records set in the second quarter.

Leveraged Commentary And Data: The Gap Widens Between U.S. And European Leveraged Loans

Since Europe's debt crisis flared anew in August, European loans have traded off relative to U.S. paper. On Nov. 10, the average price of loans in the S&P European Leveraged Loan Index (ELLI) stood at 85.24% of par, seven points inside that of the U.S.-based S&P/LSTA Leveraged Loan Index (S&P/LSTA Index).

R2P Corporate Bond Monitor

In the fixed-income markets, risk-reward profiles--as measured by our average Risk-to-Price (R2P) scores--increased from Nov. 1 to Nov. 14. Scores stabilized or increased across the board, except for the industrials and energy sectors in Europe (which decreased by 4% and 7%, respectively).

Market Derived Signal Commentary: Retailers' CDS Spreads Reflect Positive Sentiment

Over the past month, the average credit default swap (CDS) spread for retailers tightened 35 basis points (bps), or 4.6%, to 272 bps, compared with the overall consumer discretionary sector, which tightened 12 bps, or 0.6%, to 261 bps, according to CMA DataVision. The average spread for retailers places the group in speculative-grade territory, 18 bps wide of the 'BBB-' consumer discretionary benchmark.

Capital Market Commentary: IPO Activity Is Strong In The Information Technology Sector

This week marks one the busiest weeks of the year for IPO activity. As the total number of offerings continues to increase, the information technology (IT) sector is poised to reach its highest level for IPO activity in several years. The current pace of activity for the IT sector suggests the full-year 2011 IPO total could eclipse the 2010 total.

S&P Index Commodity Commentary: Energy Vs. Non-Energy

Commodity prices have shown strength in November despite equity weakness and dollar appreciation. However, rapidly increasing energy prices and declining industrial metals prices have done little to alleviate the already poor economic outlook reflected in the S&P GSCI Index in 2011.

Quantitative View: All Or Nothing--Tough Times For Active Managers

We found that strategies such as capital efficiency are nearly perfectly correlated (-.81) with market direction. In other words, when the market retreats, these strategies perform well. When the market rallies, strategies focused on volatility and price momentum turned in the best performance. Valuation and analyst expectations have shown the weakest relationship, particularly in October, to market direction.

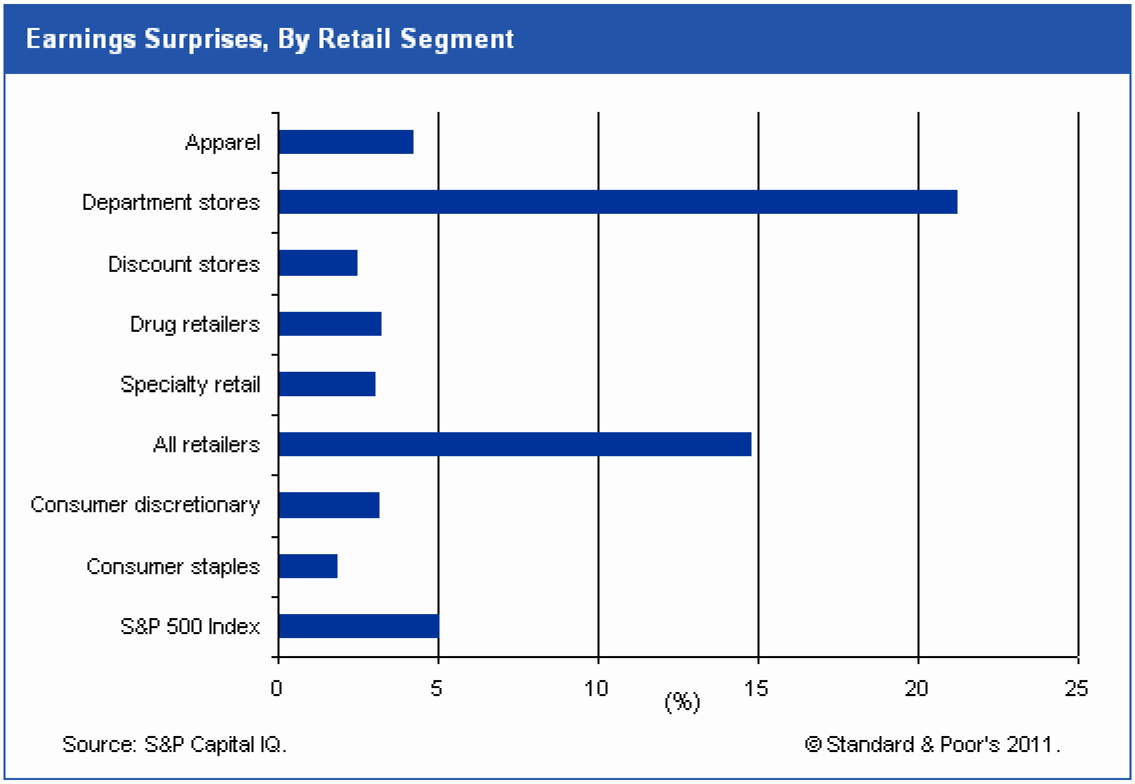
Economic And Market Outlook: Earnings In North America And Europe

North America

While the peak of the third-quarter earnings season has come to an end, many retail stores released their earnings results over the last two weeks. Among the 33 S&P 500 retailers from the consumer discretionary and consumer staples sectors, 15 closely followed companies have reported results since Nov. 9, 2011. S&P 500 retail firms span four main industries: specialty retail, multiline retail, textiles, apparel and luxury goods, and food and staples retailing. Of the 31 retailers that have reported so far, 22 exceeded estimates, six missed, and three met, bringing the total of retailers that exceeded the S&P Capital IQ estimates to 71%, higher than that of the consumer discretionary sector (68%), the consumer staples sector (65%), and the S&P 500 Index (66%).

Retailers are divided into five categories: department stores, discount stores, apparel stores, drug retailers, and specialty retailers. The department stores have the largest positive surprise (21.24%) of any sector, surpassing the consumer discretionary sector (3.19%), consumer staples sector (1.87%), and the S&P 500 Index (5.07%) (see chart 3).

Chart 3



Macy's Inc. primarily drove the growth in the department store segment, reporting a surprise factor of 102.52% and year-over-year earnings growth of 300%. The company attributes its strong third-quarter performance to a number of factors, including the "My Macy's localization of our assortments and shopping experience; omnichannel integration across stores, online and mobile; and MAGIC Selling and associate coaching programs to strengthen customer engagement," CEO Terry Lundgren said. "Bloomingdale's also enjoyed a strong quarter, both in stores and online, as customers have continued to respond to bridge and designer merchandise." The company also raised its full-year 2011 guidance to $2.70 to $2.75 per share from $2.60 to $2.65 (provided on Aug. 10), higher than the consensus estimate of $2.11. However, Macy's fourth-quarter guidance of $1.52 to $1.57 is lower than the consensus of $1.61.

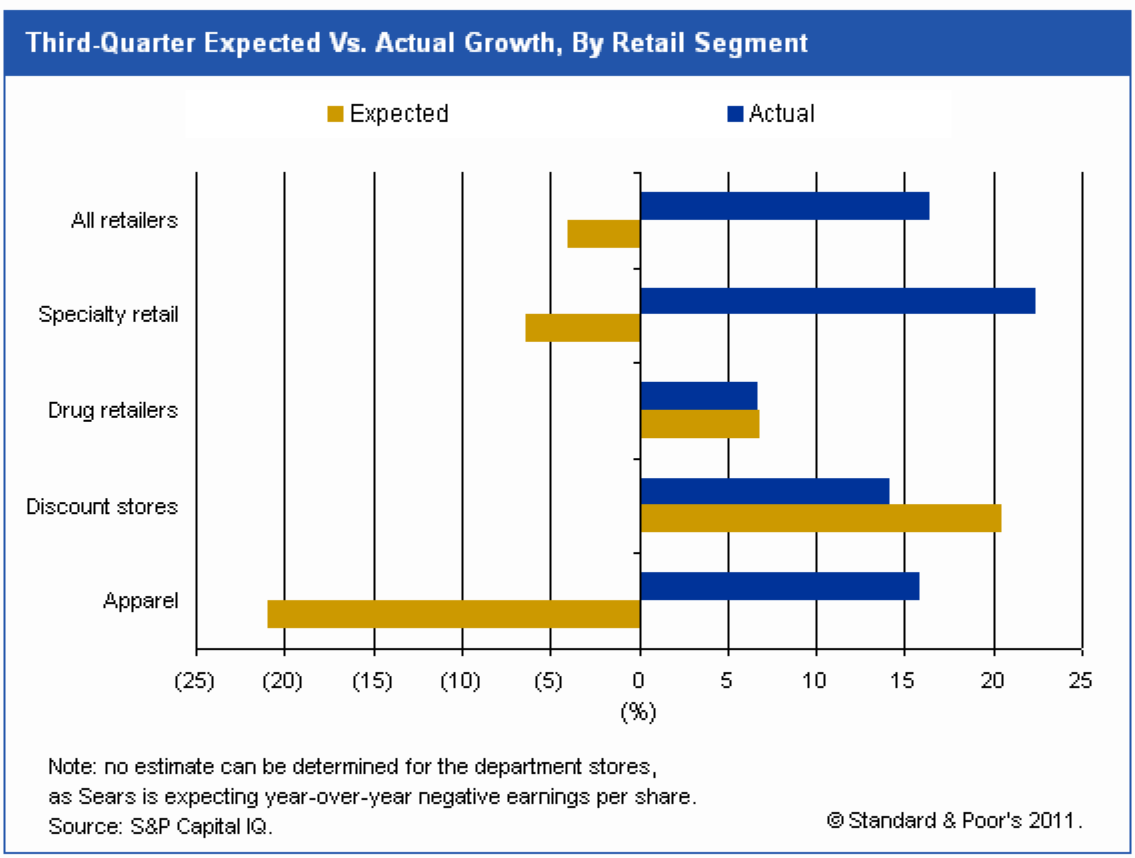
On the opposite end of the spectrum, discounters are reporting the lowest surprise factor (2.53%) of any segment, suggesting consumer spending is improving as shoppers choose to shop at the pricey department stores over the discounters. When consumers feel comfortable with their economic situation, they typically shop at department stores, where the goods are more expensive, rather than the discounters. Within the discounters, both Costco (1.68% lower) and Wal-Mart Stores Inc. reported negative surprise factors (0.78% lower). Both of these retailers are often a favorite in an unstable economy. On the other hand, high-end discount store Target Corp. leads the group with a 17.90% earnings surprise and 28% year-over-year earnings growth.

While the apparel sector performs second best among the retail categories with a 4.61% surprise, the sector also includes the worst performing company, Abercrombie & Fitch Co. (negative 20.43%). This company is considered a high-end teen retailer, and is typically a good barometer for teen spending and thus the economic stability of their parents. However, during the 2011 back-to-school season (July to September), which falls in the third quarter, department stores were able to offer better discounts and promotions to their customers, while Abercrombie & Fitch admits it struggled with cost challenges.

While retailers reported a robust third quarter on increasing strength in consumer spending, the fourth quarter will be even more telling as the holiday season determines how willing shoppers are to spend their discretionary income. So far in the third quarter, nine retailers have issued negative guidance, six positive, and two in line with analyst expectations, resulting in a very low negative-to-positive (N/P) ratio of 1.5, compared with a N/P ratio of 2.1 for the overall S&P 500 Index. Overall, analysts expect a strong fourth-quarter earnings growth rate of 12.31%.

While this may all seem like positive news for retailers, it is important to note that department stores, the category with the highest growth in the third quarter, is poised to post a decline of 1.41% in the fourth quarter. On the flipside, the discounters, which had the lowest growth rate in the third quarter, are estimated to post the strongest numbers next quarter (34.66%). Given the much higher-than-expected earnings per share figures reported this quarter, it is possible that this trend of surprising to the upside could continue next quarter. If we look back to the beginning of the calendar quarter (July 1), analysts expected this group of 33 companies to report a year-over-year decline of 4.48% (see chart 4). However, retailers ended the quarter with 16.47% growth. Analysts initially estimated that department stores would post the weakest growth rate due to poor expectations from Sears Holding Corp. (the actual growth rate can't be calculated due to negative earnings per share expectations and actuals from Sears). However, due to Macy's 300% gain, the category ended up with the highest growth rate of any segment. This could suggest, despite current estimates (which analysts may revise higher in light of recent positive surprises), consumer spending will remain strong throughout the end of the year.

Chart 4



Europe

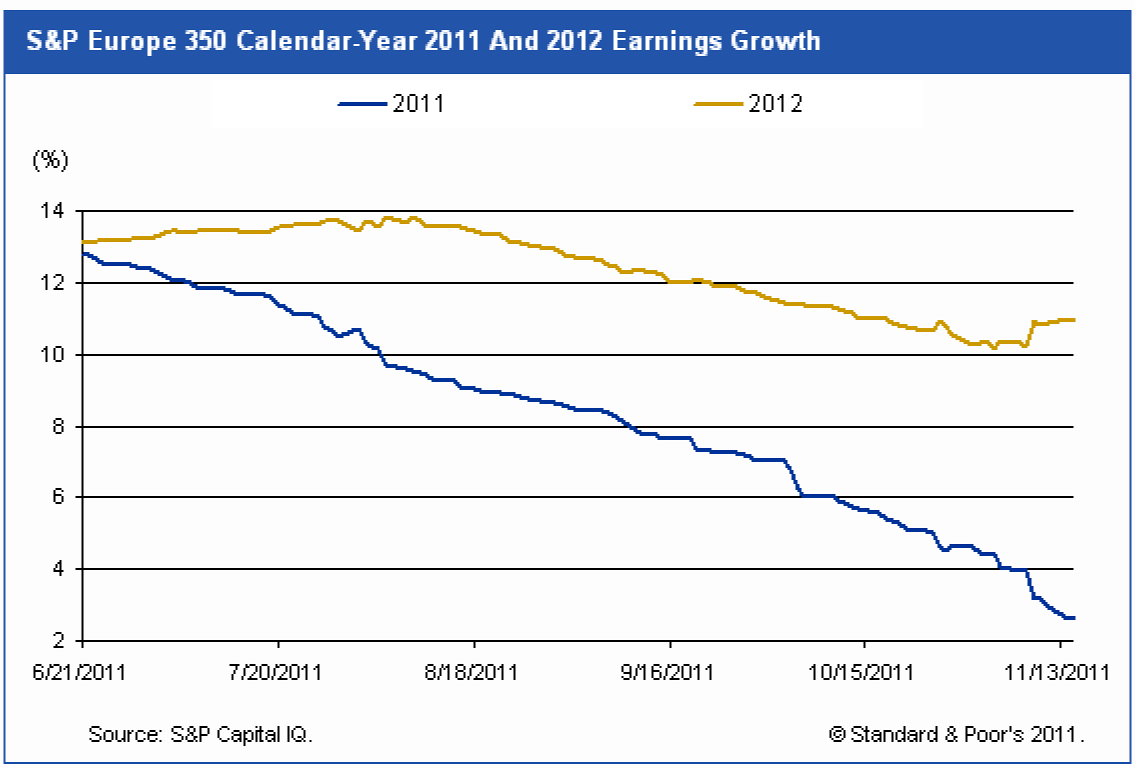
Over the two week period ended Nov. 11, analysts lowered their consensus calendar-year 2011 expectations for the S&P Europe 350 Index by 1.6% to €96.81 from €98.43 on Oct. 28, falling to their lowest level since the start of the third quarter, according to S&P Capital IQ. Consensus expectations for S&P Europe 350 calendar-year 2012 earnings decreased by 1.3% to €107.34 as of Nov. 11, compared with €108.78 on Oct. 28.

Considering the European Commission's (EC) latest 2012 GDP growth forecast of just 0.5%, the outlook for the European economy appears to be somewhere between slow growth and renewed recession. Last week, the EC drastically cut its 2012 GDP growth forecast for the 17-nation eurozone to 0.5% from 1.8% and its 2011 forecast to 1.5% from 1.6%. Analysts expect more bad economic news as they have lowered 2011 and 2012 earnings forecasts for S&P Europe 350 corporations since early summer.

For the past two weeks, the financials sector saw the largest cuts to 2011 and 2012 earnings estimates of any sector. Analysts also continued to significantly lower earnings forecasts for the cyclical materials and industrials sectors.

Although analysts have been lowering 2012 earnings forecasts, we believe the 2012 corporate earnings growth rate of 10.88% is still robust. While the 2011 growth rate has declined substantially to 2.92% from 12.77% in June, analysts are still quite optimistic about next year's earnings growth (see chart 5).

Chart 5



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S&P Index Equity Commentary: Everything Is Beautiful, At Least On Paper

Overall, third-quarter numbers for the S&P 500 Index are good on both the balance and income sheets, with strong earnings and cash flow helping to drive the current market. Operating earnings and as reported earnings both set records, both with or without the special valuation gains reported by the bulge bracket firms, and topped the previous records set in the second quarter. Cash flow also ran high, but it is yet unclear whether it will eclipse the previous record from the second quarter.

Looking forward, fourth-quarter operating estimates have declined 4.4% since the end of September, and may fall short of third-quarter results, leading to what would be the first sequential quarterly decline since the fourth quarter of 2008. However, the estimates would still be 13.1% higher than in fourth-quarter 2010 and would represent the third-best quarter on record. Stock buybacks are running 31% ahead of second-quarter 2011 and 61% ahead of third-quarter 2010. The pace has picked up substantially, but companies still appear to be matching employee options, meaning that share counts have not been reduced. Excluding the financials sector's 7.2% share increase, however, the share count is slightly lower, indicating some count reduction and providing a boost to third-quarter earnings per share.

On an issue basis, there has not been much share count reduction reported as of yet, as companies appear unwilling to purchase additional shares at full cost. However, the pace has picked up, and the Amgen-financed $5 billion Dutch auction has garnered attention. Cash is running 2.8% ahead of the record from second-quarter 2011 of $976 billion, meaning there is the potential for a 12th consecutive quarterly record. Investors should note that the cash value represents 10.5% of market value and 68 weeks of expected 2012 operating income. Even with so much cash on hand, companies have primarily continued to spend conservatively. When firms finally start to use funds, massive spending--especially if it is for expansion--could cause manufacturers to start hiring, which we believe would be a catalyst to economic growth in the U.S. Capital expenditures are running 9.1% ahead of the second quarter. This year has benefited from a temporary tax write-off of new equipment, which means the fourth quarter will get some of the expected first-quarter 2012 buying as the deduction expires. Companies appear to be spending mostly on maintenance and not expansion, which speaks poorly for future growth and jobs. Dividend increases remain the bright spot. Year-to-date S&P 500 actual payments are up 15.4%, with the 12-month indicated rate up 16.0%, still 5.6% off the all-time high rate set in June 2008.

Pensions continue to be severely underfunded. With the S&P 500 Index lower by 0.5% year to date and the Global S&P BMI down 8.4% (developed off 7.0%, emerging off 17.5%), it doesn't appear that companies would meet their 2011 pension return expectations, even if all the fixed-income allocations were in U.S. Treasuries. When you add in lower interest rates (the lower the interest rate the higher the discounted liabilities), more cash payments will be needed. Potentially, we could post a record pension underfunding for 2011. The current record is from 2008, at $308 billion underfunded; 2010 was $245 billion underfunded, with 2007 $64 billion overfunded.

Overall, companies are in good financial shape but remain wary of the economy and their own product sales. On paper, fundamentals appear solid, but prices will remain volatile until uncertainty is reduced in the market. However, 2012 earnings are expected to post a 10.6% gain, which, while they appear rich, we note that S&P 500 companies have found a way to live through 9% unemployment and reluctant corporate and consumer spending to still post record earnings.

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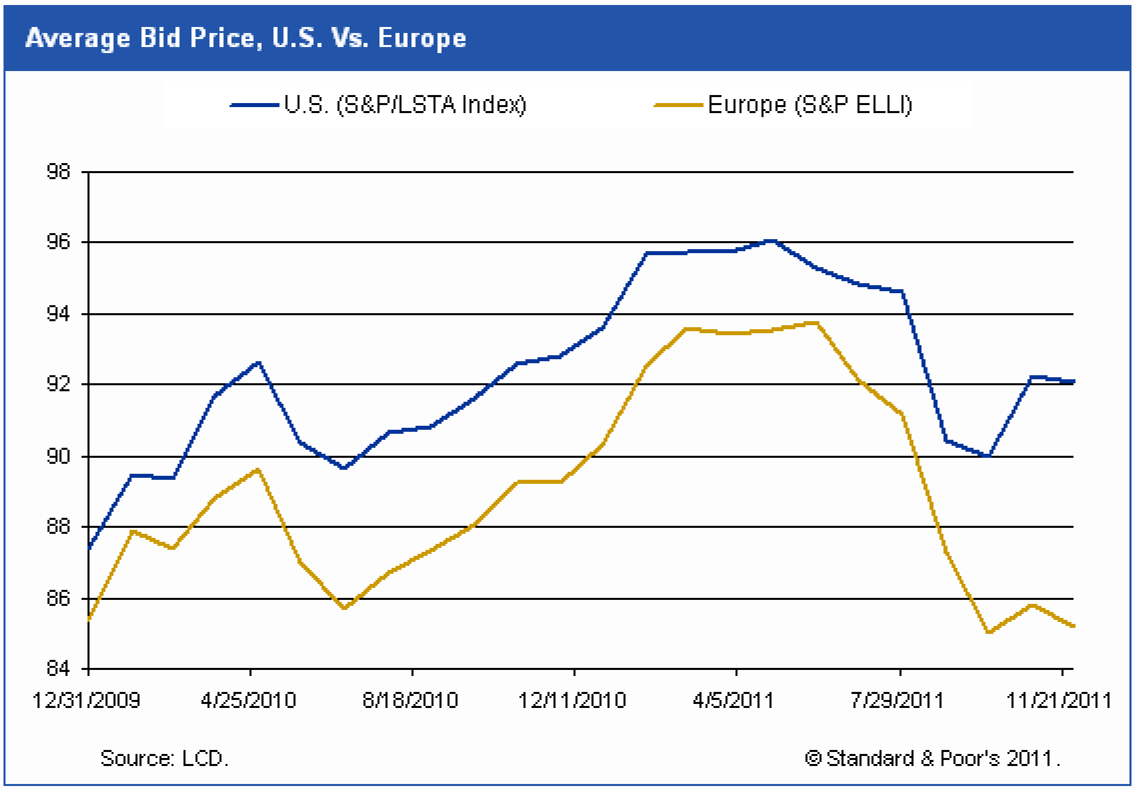
Leveraged Commentary And Data: The Gap Widens Between U.S. And European Leveraged Loans

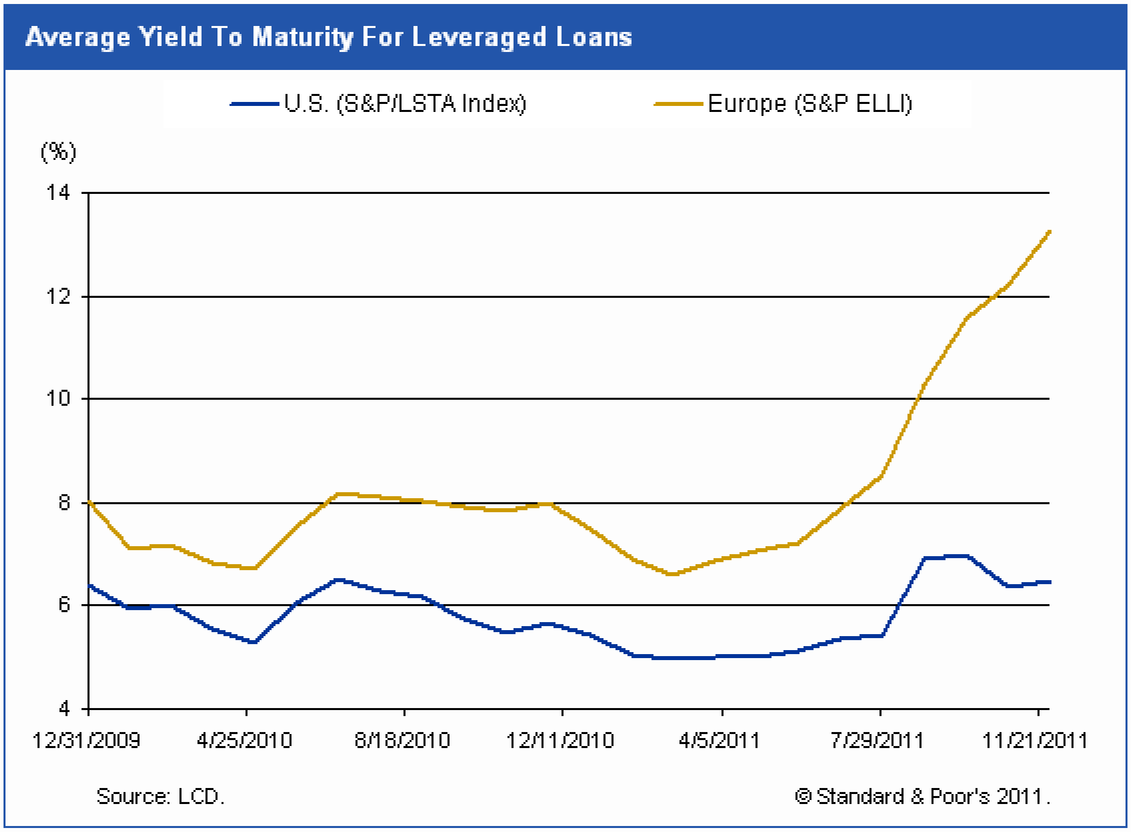
Since Europe's debt crisis flared anew in August, European loans have traded off relative to U.S. paper. On Nov. 10, the average price of loans in the S&P European Leveraged Loan Index (ELLI) stood at 85.24% of par, seven points inside that of the U.S.-based S&P/LSTA Leveraged Loan Index (S&P/LSTA Index). That is the widest price gap in two and a half years, up from 2.7 points at the end of June (see chart 6).

Chart 6



This trend has driven a wedge between the prospective yields offered by European loans versus those on offer in the U.S. As of Nov. 10, the average yield to maturity of the ELLI was 13.54%, compared with 6.5% for the S&P/LSTA Index--a 604 bps difference, up from 254 bps at the end of June and by far the highest on record (see chart 7).

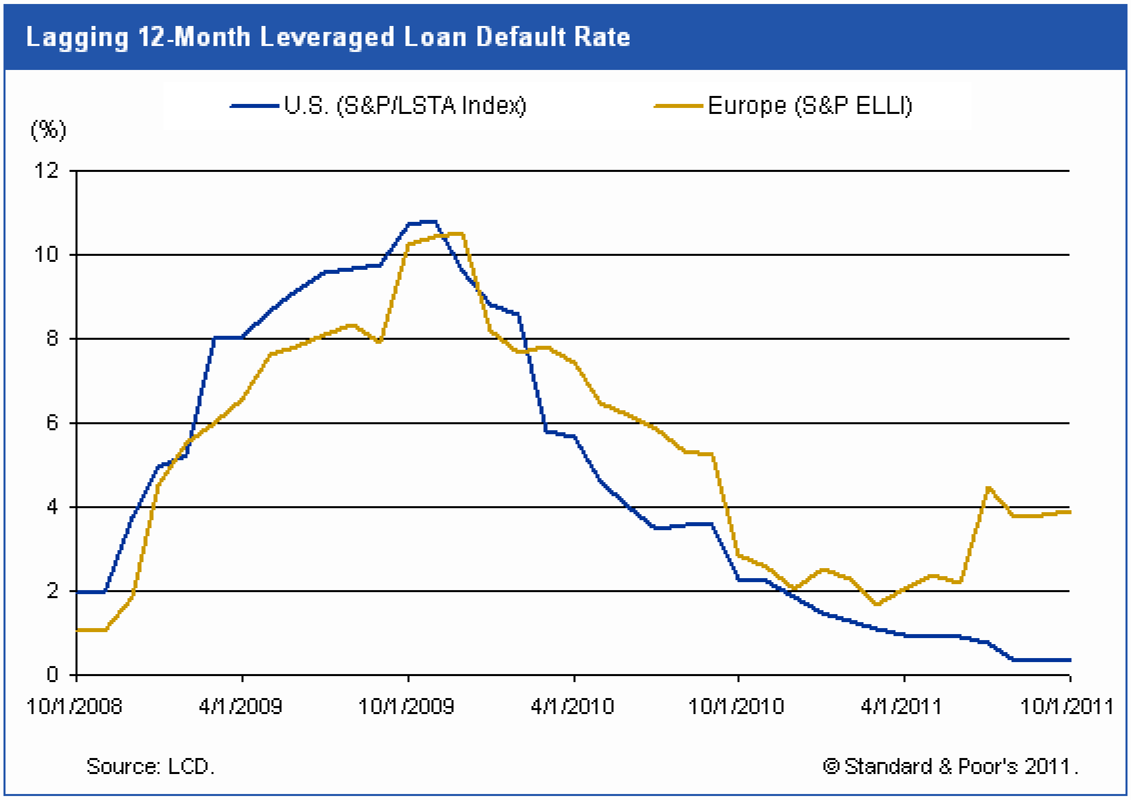
Chart 7



Proximity remains a prominent factor, among other concerns. Europe's sovereign debt woes have affected the European capital markets (loans included) more than markets in the U.S. For example, the S&P 500 Index stood at 1,260 on Nov. 12, roughly unchanged from the 2010 close. The FTSE Index, by contrast, is 6.3% lower over the same period. At the same time, U.S. high yields returned 3.13%, versus a decline of 2.16% for Europe, according to the Bank of America Merrill Lynch High-Yield Index. Loans have followed suit, with the S&P/LSTA Index up 1.62% and the ELLI down 0.21% through Nov. 10.

In terms of microeconomic factors, strong fundamental and technical conditions have also benefited the U.S. loan market in 2011. For example, the default rate in the U.S. fell to a microscopic 0.32% in October, versus 3.91% in Europe--the widest difference on record (see chart 8).

Chart 8



Economic growth in the U.S. has exceeded that of Europe. Most recently, U.S. year-over-year GDP growth reached 2.5% in the third quarter, versus just 0.4% across the eurozone, with even the larger economies of northern Europe slowing.

On a technical basis, the U.S. loan market also holds the upper hand. Bolstered by muscular retail subscriptions during the first half, visible capital flows into the U.S. market via loan mutual funds and collateralized loan obligation (CLO) issuance totaled $26 billion during the first 10 months of 2011. The data for Europe are not as scientific, but it's clearly a less robust story. First, the European market has little in the way of direct retail product. In addition, CLO issuance east of the Atlantic--recently hampered by Europe's regulatory skin-in-the-game rules--totals just €860 million so far this year, versus $10.5 billion in the U.S.

Looking ahead, managers say they see Europe as an opportunity--albeit one fraught with clear and present risks. European banks are selling assets in response to stricter capital requirements, which has captured the attention of U.S. private equity firms that sense potential bargains, as noted in the New York Times DealBook blog on Nov. 11. Likewise, a growing number of loan managers say they are exploring the wide yield opportunities in the European market. Of course, this information is anecdotal. But in 2011, LCD News reported that no fewer than four U.S. managers have either bought European loan shops or hired professionals.

First, GSO Capital Partners and Ares featured heavily among the U.S. shops acquiring European outfits this year, with the former scooping up AIB Capital Markets' CLO business and Harbourmaster Capital, and the latter honing in on CLO businesses of Octagon and Indicus. More recently, Black Diamond Capital Management announced its acquisition of GSC Group's European CLO businesses. But not all have adopted the acquisition strategy, with Crescent Capital Group instead putting down roots with the launch of its European credit strategy, hiring Christine Vanden Beukel as managing director to lead Crescent Credit Europe.

Given the dearth of visible new-issue supply in the U.S., managers believe this trend will accelerate in early 2012, barring an escalation in Europe's sovereign debt crisis or a surge in U.S. new-issue volume. Also worth noting is the fact that no new-issue supply is expected in Europe for the remainder of 2011, with very limited visibility into next year as well.

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R2P Corporate Bond Monitor

As the eurozone now threatens to fall into another recession, market participants have begun to more closely monitor third-quarter eurozone GDP data.

Expansion in Germany (third-quarter GDP growth of 0.5%) and France (0.4%) helped to keep the European economy growing in the third quarter, according to statistics agency Eurostat. On Nov. 15, 2011, Eurostat reported that real GDP increased by 0.2% in the third quarter (the same as in the second quarter) in both the eurozone and in the European Union (EU).

In comparison, the U.S. economy grew 0.6% in the third quarter, while the Japanese economy grew 1.5%.

In the fixed-income markets, risk-reward profiles--as measured by our average Risk-to-Price (R2P) scores--increased from Nov. 1 to Nov. 14 (see tables 1 and 2). Scores stabilized or increased across the board, except for the industrials and energy sectors in Europe (which decreased by 4% and 7%, respectively).

In the U.S., scores increased by 15% mainly due to a decrease in the probability of default (PD) and bond price volatility by 11% and 6%, respectively, combined with option-adjusted spreads widening by 8 bps.

In Europe, scores increased (4% increase) mainly due to a decrease in the PD and bond price volatility by 5% each, combined with an OAS widening of 9 bps.

Table 1

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

	Scores (%)	OAS (bps)	PD (%)	Bond price vol. (%)
Consumer discretionary	13	15	(8)	(8)
Consumer staples	13	(4)	(27)	(4)
Energy	17	8	7	(8)
Financials	3	6	(3)	(6)
Health care	14	10	(37)	3
Industrials	13	(1)	(3)	(7)
Information technology	12	12	3	(3)
Materials	9	4	(11)	(8)
Telecommunication services	21	20	(22)	(13)
Utilities	33	6	(5)	(3)

Change as of Nov. 14, 2011, from Nov. 1, 2011.

Table 2

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

	Scores (%)	OAS (bps)	PD (%)	Bond price vol. (%)
Consumer discretionary	8	13	9	(13)
Consumer staples	8	(4)	(39)	(1)
Energy	5	6	10	(4)
Financials	5	11	2	(9)
Health care	7	4	(10)	(8)
Industrials	(4)	6	5	(4)
Information technology	13	21	(11)	0
Materials	0	7	(6)	(10)
Telecommunication services	5	13	(25)	(5)
Utilities	(7)	10	12	3

Change as of Nov. 14, 2011, from Nov. 1, 2011.

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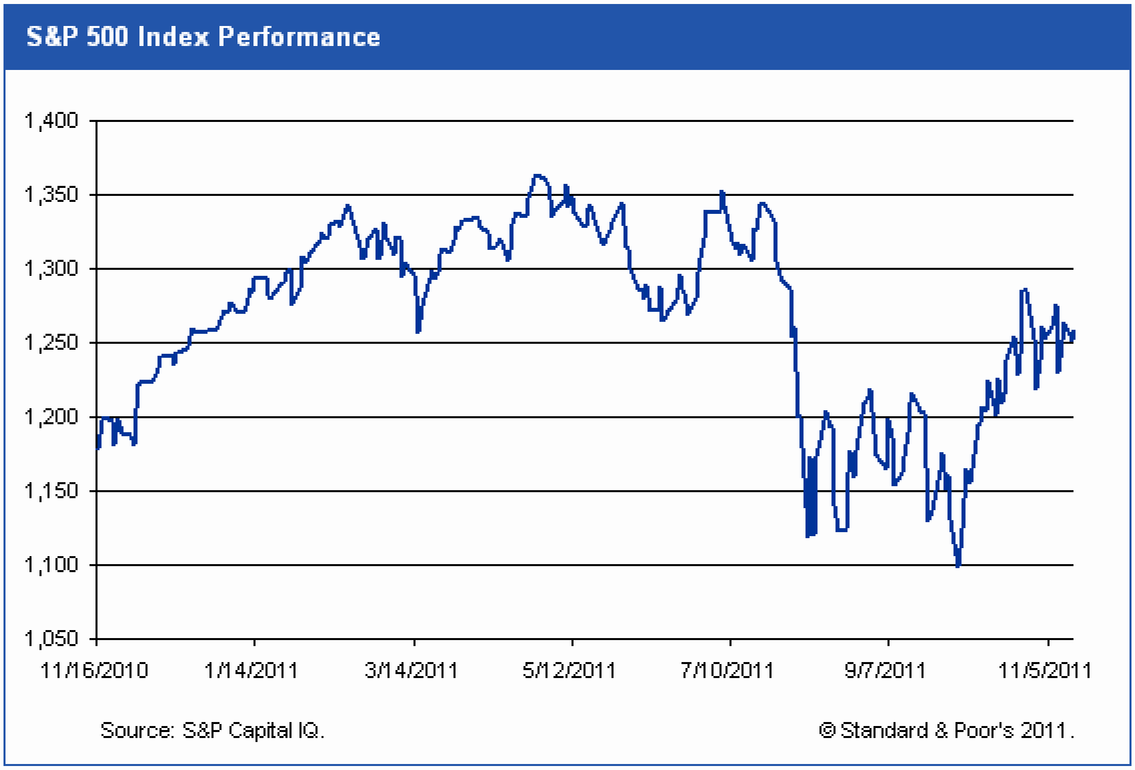
Market Derived Signal Commentary: Retailers' CDS Spreads Reflect Positive Sentiment

Despite ongoing concerns in the market about the strength of the U.S. economy, GDP reached a record $13.353 trillion on 2.5% growth in the third quarter. In addition, U.S. retail sales in October climbed to an all-time high of $397.7 billion, extending the 2011 trend of record-setting months, excluding May. On Tuesday, the U.S. Census Bureau reported a 0.5% increase in sales, up 8.2% from a year ago, supporting our view that the U.S. economy is in a slow but sustainable recovery. Looking forward, Standard & Poor's Ratings Services said Monday it expects a modest increase in U.S. holiday sales, "with shoppers opening up their wallets to make this the second consecutive up year."

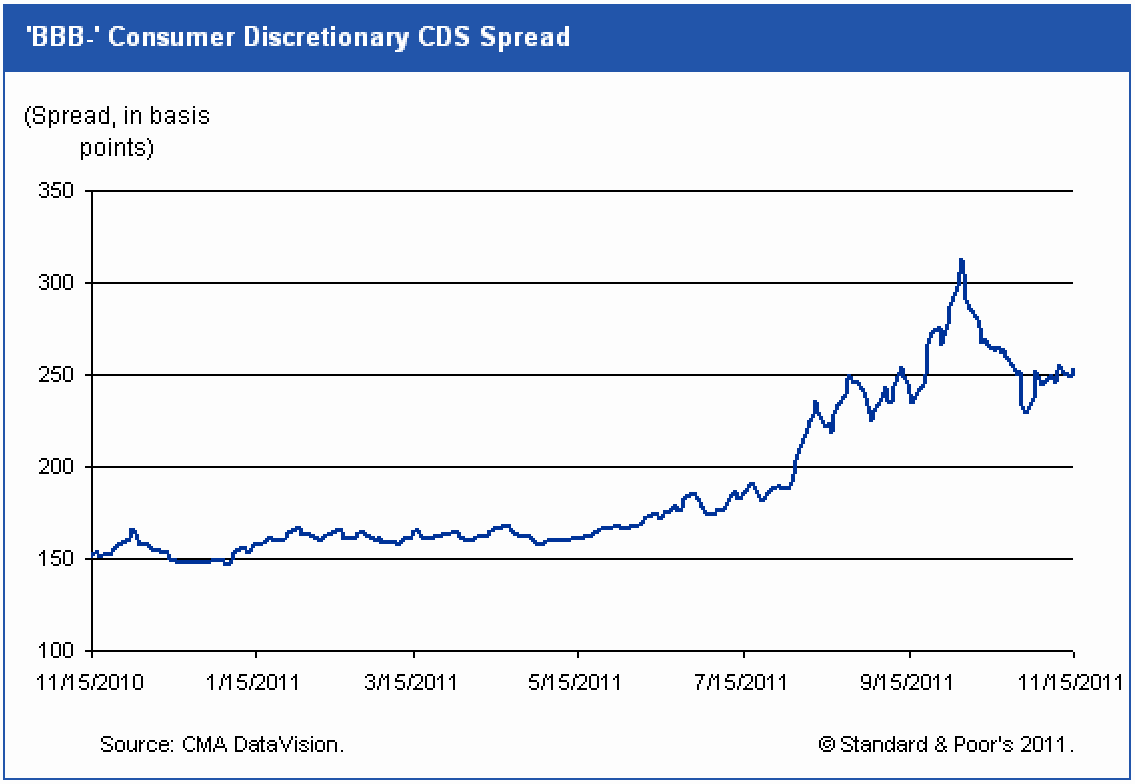
As we noted last week, although not all aspects of the U.S. economy have recovered and the eurozone debt crisis is muting optimism, retail sales, initial jobless claims, and ongoing strength in corporate earnings are providing enough positive signals to boost the market (see "Market Intellect: What Does The Future Hold Now That U.S. GDP Has Recovered From The Financial Crisis?," published Nov. 10, 2011, on the Global Credit Portal). The S&P 500 Index is up nearly 5% over the past month and well off its low of 1,123.95 (Oct. 4, 2011) over the past year (see chart 9).

Chart 9



We wanted to see if positive sentiment was reflected in the five-year credit default swap (CDS) spreads for U.S. retailers. We found that over the past month, the average spread for this group tightened 35 basis points (bps), or 4.6%, to 272 bps, compared with the overall consumer discretionary sector, which tightened 12 bps, or 0.6%, to 261 bps, according to CMA DataVision (see chart 10). The average spread for retailers places the group in speculative-grade territory, 18 bps wide of the 'BBB-' consumer discretionary benchmark.

Chart 10



The top 10 tightest and widest spreads were not concentrated in any one area of retailing (see table 3). Electronics retailer RadioShack Corp. widened the most over the past month, by 188 bps, or nearly 50%, to 567 bps, while the luxury department store chain Saks Inc. tightened the most, by 71 bps, or 13%, to 478 bps. In each case, the spreads were far wide of investment-grade territory.

Table 3

Top Tightest And Widest Spreads For U.S. Retailers

	S&P credit rating	Market derived signal rating	Industry	CDS (bps)	Change (%)
Top 10 tightest spreads					
Target Corp.	A+/Stable	aa-	General merchandise stores	57	3.7
Home Depot Inc.	A-/Stable	a+	Home improvement retail	65	(0.5)
AutoZone Inc.	BBB/Stable	a	Automotive retail	66	3.8
TJX Cos. Inc.	A/Stable	a-	Apparel retail	83	3.0
Lowe's Cos. Inc.	A-/Negative	bbb+	Home improvement retail	103	25.0
Nordstrom Inc.	A-/Stable	bbb+	Department stores	114	3.1
Macy's Inc.	BBB-/Stable	bbb	Department stores	140	4.1
Kohl's Corp.	BBB+/Stable	bbb	Department stores	141	16.9
Expedia Inc.	BBB-/CWNeg	bbb-	Internet retail	184	(1.7)
Staples Inc.	BBB/Stable	bb+	Specialty stores	208	23.0
Top 10 widest spreads					
Office Depot Inc.	B-/Stable	b-	Specialty stores	913	17.0
Toys "R" Us Inc.	B/Stable	b	Specialty stores	735	2.2

Table 3

Top Tightest And Widest Spreads For U.S. Retailers (cont.)					
Neiman Marcus Group	B+/Stable	b	Department stores	612	(6.9)
RadioShack Corp.	BB-/Stable	b+	Computer and electronics retail	567	49.8
Saks Inc.	BB/Stable	b+	Department stores	478	(13.0)
Dillard's Inc.	BB-/Stable	bb-	Department stores	395	(6.1)
Best Buy Co. Inc.	BBB-/Stable	bb-	Computer and electronics retail	391	20.0
J.C. Penney Co. Inc.	BB+/Stable	bb+	Department stores	271	(2.9)
The Gap Inc.	BB+/Stable	bb+	Apparel retail	250	(3.9)
Limited Brands Inc.	BB+/Stable	bb+	Apparel retail	216	(3.9)

Source: CMA DataVision.

While we find the overall tightening trend positive, individual spreads within the retailers group offered a mixed view. Some of the tightest spreads widened over the past month and some of the widest spreads tightened, showing how important company-specific factors are to the credit market's perception of risk. However, we will revisit the retailing group periodically, as market conditions warrant, to see if the group's average spread begins to trade tight of the speculative-grade ratings category.

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Capital Market Commentary: IPO Activity Is Strong In The Information Technology Sector

IPOs

This week marks one the busiest weeks of the year for IPO activity. As the total number of offerings continues to increase, the information technology (IT) sector is poised to reach its highest level for IPO activity in several years. Specifically, 19 U.S. IT companies have completed IPOs so far in 2011, compared with 22 for all of 2010, according to S&P Capital IQ (see table 4). The current pace of activity for the IT sector suggests the full-year 2011 IPO total could eclipse the 2010 total. If so, this year will stand as the best year for IPO underwriting for the IT sector (based on the number of issues) since 2007, when firms completed 33.

Table 4

Leading U.S. Information Technology IPOs By Percent Change From Offer Price

Closed	Issuer	Value (mil. $)	Offer price ($)	Day close* ($)	Change (%)
6/8/2011	Fusion-io Inc.	233.7	19	34.90	83.7
5/18/2011	LinkedIn Corp.	352.8	45	78.49	74.4
7/26/2011	Tangoe Inc.	87.7	10	14.59	45.9
3/24/2011	ServiceSource Corp.	119.4	10	14.51	45.1
7/19/2011	Zillow Inc.	69.2	20	28.57	42.9
11/8/2011	Imperva Inc.	90.0	18	25.65	42.5
6/16/2011	Bankrate Inc.	300.0	15	19.88	32.5
10/13/2011	Ubiquiti Networks Inc.	105.6	15	19.71	31.4
8/10/2011	Carbonite Inc.	62.5	10	11.63	16.3
3/16/2011	Cornerstone OnDemand Inc.	136.5	13	14.63	12.5

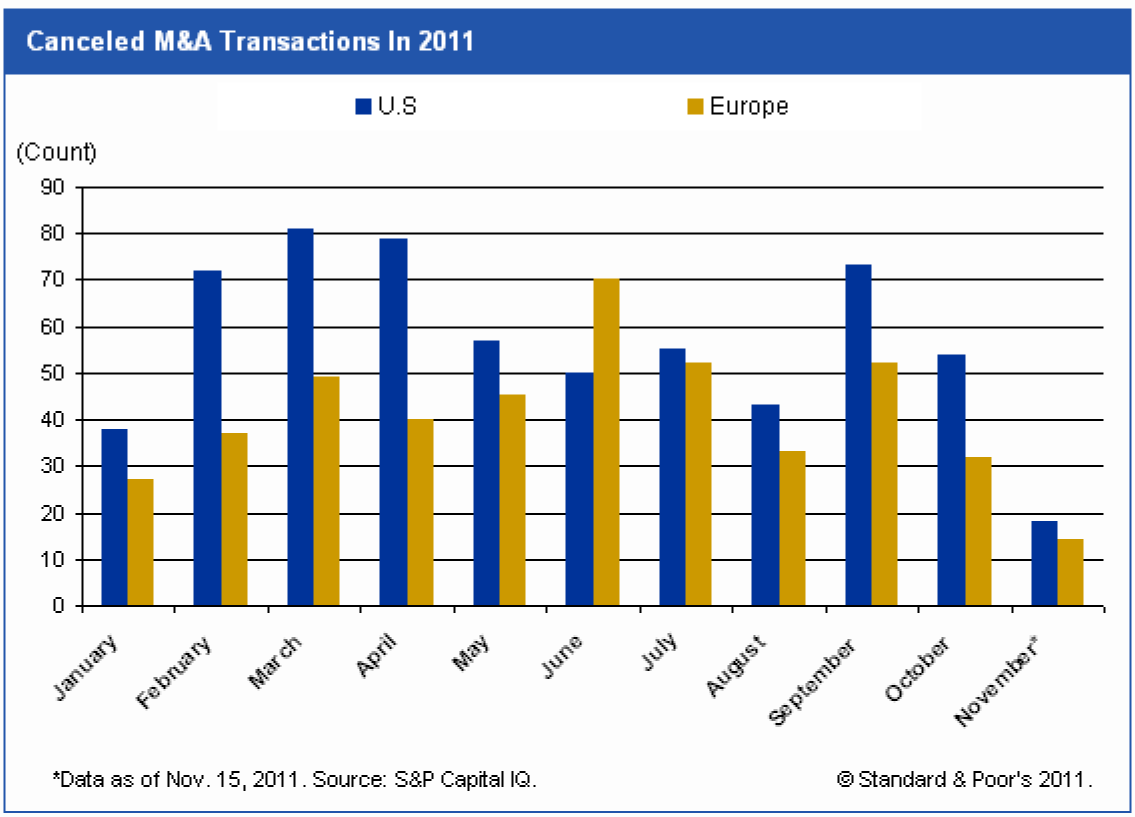
*Data as of Nov. 14, 2011. Source: S&P Capital IQ.

M&A

The pace of merger and acquisition (M&A) deal cancelation is easing both in the U.S. and in Europe, according to S&P Capital IQ data. Both regions are on track for their lowest count of canceled M&A transactions since the start of the year. As of mid-November, just 18 U.S. and 14 European M&A deals have been scrapped during the month (see chart 11). Following a drop in canceled deals in August, the number of terminated deals increased in September for both regions, followed by a return to declining cancelations last month.

In terms of mega-deal cancelations, it has been almost two months since the last canceled U.S. deal of over $1 billion, when Icahn Enterprises L.P. offered to acquire the remaining 90.6% stake in Clorox Corp. for $9.2 billion in cash on July 14, 2011 (canceled on Sept. 24, 2011). As for European deals, U.K.-based security and alarm service company G4S PLC's offer to acquire Danish facility management service firm ISS A/S from EQT Partners AB, Goldman Sachs, and others for $9.24 billion in stock and cash on Oct. 17, 2011, was terminated Nov. 1, 2011, because shareholders disapproved the deal.

Chart 11



Debt

As the end of the year approaches, the pace of debt-related securities CUSIP orders appears to be easing. Specifically, following strong identifier requests in September and October for upcoming debt offerings, the October count for domestic corporate debt CUSIPs dropped, according to data from CUSIP Global Services. Weekly debt CUSIP requests have slowed in many categories, including domestic corporate debt, certificates of deposit, and short-term municipal debt. On the other hand, weekly municipal CUSIP orders have essentially held firm, while international debt identifier demand increased (see table 5).

Table 5

Selected Debt-Related Securities CUSIP Requests

	Week ending Nov. 11, 2011	Week ending Nov. 4, 2011
Domestic corporate debt	130	472
CTF DEP (maturities less than one year)	55	156
CTF DEP (maturities over one year)	78	295
Municipals	365	383
Muni long-term note (more than one year)	3	6
Muni short-term note (less than one year)	24	41
International debt	34	28
PPN domestic debt	50	50
Total	739	1,431

Source: CUSIP Global Services.

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S&P Index Commodity Commentary: Energy Vs. Non-Energy

The S&P GSCI Index recovered in the fourth quarter, posting an increase of 13.81% with help from a monthly gain of 3.71% through mid November. Year to date through Nov. 16, the index appreciated 3.23%. Although the S&P 500 Index fell 1.13% so far this month and the U.S. Dollar Index appreciated 2.43%, energy returns fueled gains in the S&P GSCI.

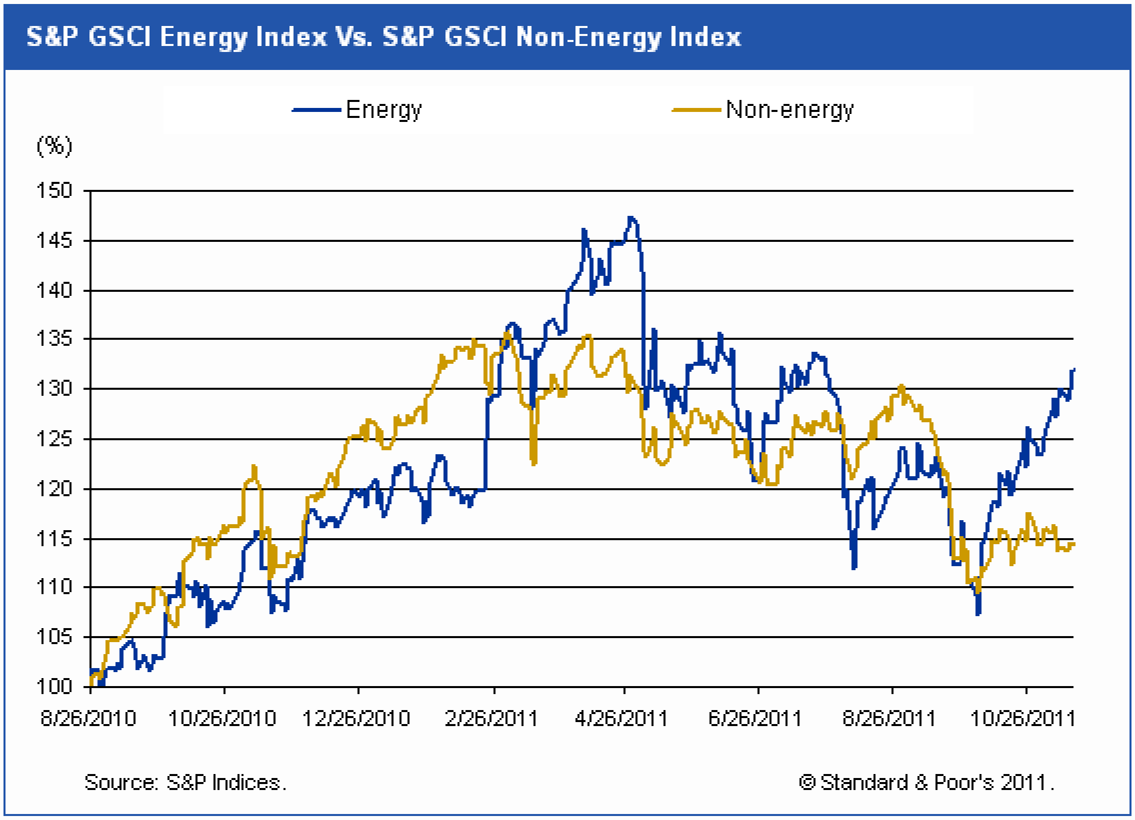
The S&P GSCI Energy Index increased 18.73% in the fourth quarter on the back of a November gain of 5.87%, driven by a sharp rally in WTI crude oil. A decision to alleviate a supply bottleneck at the main delivery point for NYMEX crude futures in Cushing, Okla. boosted the price per barrel of crude past $100.

To the chagrin of cash-strapped consumers in many developed countries, the spot S&P GSCI Petroleum Index rose 15.54% year to date, a gain second only to the 22.66% spot increase in the S&P GSCI Precious Metals Index. The S&P GSCI Industrial Metals Index posted the month's worst performance, with a decline of 3.41%.

The story throughout much of 2011 has been about the strength in energy and subsequent economic repercussions. As of Nov. 16, the S&P GSCI Energy Index posted a year-to-date increase of 9.82%, compared with a decline of 9.97% for the S&P GSCI Non-Energy Index. Earlier in the year, when energy prices spiked, many of the petroleum futures curves remained in contango as the market place anticipated the restoration of supplies. In the fourth quarter, every S&P GSCI Petroleum commodity moved into backwardation, reflecting the market's expectation of sustained tight supply-demand conditions.

Chart 12 depicts the performance of the S&P GSCI Energy and Non-Energy indices beginning on Aug. 26, 2010, one day before Federal Reserve Chairman Ben Bernanke raised the possibility of another round of quantitative easing. Supply and demand are always drivers of commodities, but according to many analysts, extremely low or negative base interest rates in developed countries in the face of rapidly increasing demand in developing countries is a key factor in price appreciation.

Chart 12



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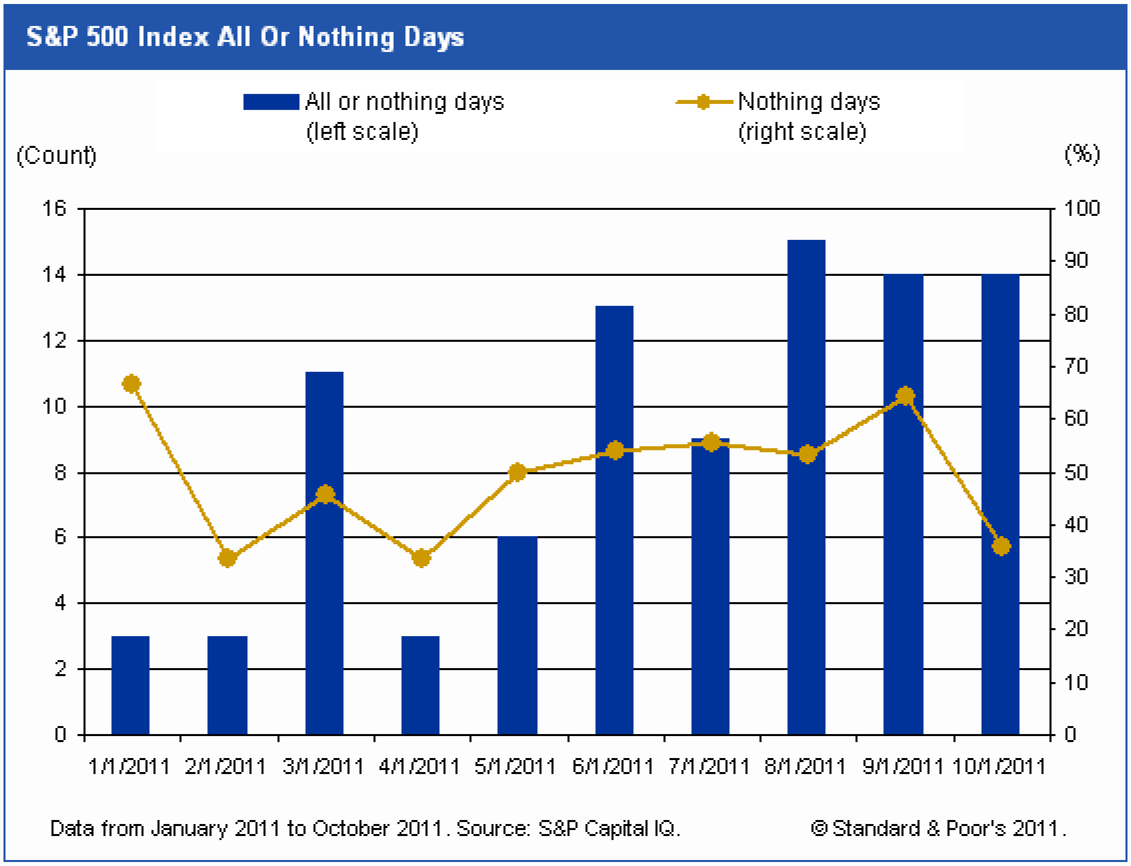
Quantitative View: All Or Nothing--Tough Times For Active Managers

The financial market's preoccupation with the European sovereign debt crises creates a challenging environment for active equity managers who have traditionally made their living on stock selection. When investors become focused on a common risk factor, the correlation between stocks tends to rise. During periods of high correlation, coupled with low return dispersion, the task of correctly identifying winners becomes increasingly difficult. At the same time, those winners' outperformance becomes tighter than normal.

This month, we evaluated the phenomena by totaling the number days in which 80% or more of the stocks in the S&P 500 Index have the same signal. We call these days "all or nothing days." We called the days in which 80% of the stocks in the S&P 500 Index had negative signs "nothing days."

Chart 13 shows the total monthly number of "all or nothing days" for 2011. We characterized 14 of 21 trading days as "all or nothing days" in October.

Chart 13



We examined eight common classes of investment strategies and observed their correlation to market direction. We measured the strategy's effectiveness by ranking stocks according to several factors that describe a strategy and take the spread of the top and bottom quintile of performance (see table 6).

Table 6

Counts

	All or nothing	Nothing
Year to date	91	46
Third quarter	38	22
October	14	5

Source: S&P Capital IQ.

We found that strategies such as capital efficiency are nearly perfectly correlated (-.81) with market direction (see table 7). In other words, when the market retreats, these strategies perform well. When the market rallies, strategies focused on volatility and price momentum turned in the best performance. Valuation and analyst expectations have shown the weakest relationship, particularly in October, to market direction.

Table 7

Correlation Of Strategy Quintile 1 Through Quintile 5 Spreads With Market Direction--Russell 3000

	--Russell 3000 with dividends--			
	July 1 to Oct. 31	**Significance**	**Oct. 1 to Oct. 31**	**Significance**
Analyst expectations	0.22	*	(0.10)	
Capital efficiency	(0.81)	**	(0.86)	**
Quality	(0.81)	**	(0.88)	**
Growth	(0.40)	**	(0.57)	**
Price momentum	0.64	**	0.56	**
Size	0.47	**	0.70	**
Value	(0.31)	**	0.33	
Volatility	0.89	**	0.92	**

*Significant at the 95% confidence level. **Significant at the 99% confidence level. Source: S&P Capital IQ.

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