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MARKETBEAT

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Four at Four: Party Time?

Posted by David Gaffen



• Did the market experience its moment of clarity Tuesday? In the struggle to define market action, some asserted that very view, and Wednesday's rally in the financial sector bolsters that analysis. Greg Fierman of Top Gun Financial Planning declared Tuesday's action to be "capitulation, baby," noting the 469 million shares that changed hands in the Financial Sector Select SPDRs ETF, a number that far surpassed any day of trading during the Bear Stearns blowup. And bank stocks soared today, bolstered by the solid earnings report out of Wells Fargo & Co., which gained 33% after increasing its dividend. The SEC's crackdown on naked short-selling added to the bullish fervor, but some remained wary. "I wish it would have gone down further; I wish it would have had a bigger washout," says **Joe Saluzzi**, co-head of trading at **Themis Trading**. "It could have cleared the decks a bit more. I wouldn't be surprised if another shoe drops and it heads back down south again." The rapid ascent of the likes of Fannie Mae and Freddie Mac, along with big declines in the Proshares Ultrashort Financials ETF (which fell 22%) was enough evidence for some, but with many more financial-services firms due to report earnings, the euphoria could be short-lived. On who does this depend? Banks, of course. "Whether this is a short squeeze or genuine rally we'll see. For it to be a genuine rally it has to be led by financials," says Simon Baker, president and founder of Baker Avenue Asset Management.



- The market gets a double dose of financial earnings Thursday, with J.P. Morgan Chase leading off before the opening bell, and Merrill Lynch & Co. following the close. The order of the releases indeed makes it more likely that the market will have a positive reaction to earnings tomorrow, as Merrill has been a consistent disappointment to the markets for the past few quarters. “If some financial firm gives a bad report we’re going to see the market drop again, and I think we’re going to see these gyrations for the future,” says Barry Taylor, CFP and portfolio manager at Bingham, Osborn & Scarborough. Analysts have engaged in a game of “how big will the write-downs be?” with most settling in the \$4 billion to \$5 billion range for the brokerage, which still has heavy exposure to collateralized debt obligations and residential mortgage-backed securities. The company is reportedly going to sell its stake in Bloomberg LP, and along with its stake in BlackRock, is considered among its most valued assets, but that’s what happens in bad times — people sell what they can, not what they want. “We view a sale as a negative given that these positions were one of the few remaining positives of the MER story amid the consecutive quarterly losses,” wrote Wachovia’s Doug Sipkin, in an analysis last week. Merrill is expected to lose \$1.91 a share; the worst-case estimate is Oppenheimer’s forecast for a \$4.21-per-share loss; the most optimistic is Fox-Pitt Cochran’s bet on a 70-cent loss.

- There was significant bullish options activity in Barr Pharmaceuticals today, motivated in part by expectations that the company’s settlement discussions with Sanofi-Aventis regarding Barr’s drive to launch a generic nasal spray. Sanofi makes Nasacort, and sued Barr in 2006. Analysts at Cowen & Co. today wrote that the settlement would open an opportunity for Barr, because “there have been no other challengers to Nasacort... other challengers would be litigated and a 30-month stay would likely apply.” The share ended the day modestly higher, gaining 1.6%, but significant activity in the August out-of-the-money call options was seen as investors started to set up for the possibility of the stock gaining momentum in advance of a positive outcome of the settlement. Shares closed today at \$46.82 apiece, and more than 8,000 call options at the \$50 strike changed hands, compared with about 3,000 existing contracts, suggesting a bullish outlook.

- The Wall Street Journal reports that Microsoft, still looking for a way to topple Google (or at least provide some kind of actual competition for ad revenue), is looking at a possible tie-up with Time Warner’s AOL (just what it needs...another adrift media company to partner with). The companies have discussed this over a period of months, as an alternative to the Yahoo deal, and shares of both companies were strong, with Microsoft gaining 4% and Time-Warner rising 5.3%. However, the discussions are said to be preliminary (which means Microsoft is probably not badgering Time-Warner to do what it wants just yet). Then again, Yahoo is also apparently pursuing AOL, to try to gain more leverage in this Internet thing. The jokes about MicroHoo might need to be modified into MicroAOLoo or something, but since Google continues to drink everybody’s milkshake, it doesn’t really matter. Wake us up when an actual deal happens.