

## Weekly Marketmail

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**Monday, July 29, 2013**

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### **Market Moves Sideways on Mixed Corporate Earnings Reports**

By Louis Navellier

The market was as flat as a pancake last week, with the Dow rising less than 0.1% and the S&P down just 0.026%. Earnings were also a mixed bag with some big-name companies missing badly, while most firms exceed expectations. According to FactSet, 73% of companies beat analysts' earnings estimates and 54% beat sales estimates, but the bad news is that the average positive earnings surprise is only 3.2%, well below the 7% average since 2009. Is this enough growth to keep the bull market rising?

#### **The Journal Bemoans a U.S. Economy "Stuck in Neutral"**

In the last week, we've seen some downbeat reports on the U.S. economy. Last Monday's *Wall Street Journal* featured an article entitled "U.S. Growth Outlook Stuck in Neutral." This article cited (1) weak corporate profits, (2) soft consumer spending, and (3) lagging job growth as reasons for slower GDP growth in the second quarter. The article also critiqued economists' overly-optimistic growth forecasts.

True, some "flagship" companies like Microsoft\* and McDonalds\* reported disappointing second quarter results, but the market rallied when Apple\* announced it will roll out some exciting products in 2014. In other words, the market seems willing to ignore short-term setbacks if there is hope for long-term profits.

Last quarter's strong U.S. dollar also contributed to slower earnings growth for many multi-national companies, since they are being paid in depreciating currencies. Fortunately, the U.S. dollar "cracked" in July, falling over 3.5% to the euro in the last three weeks (i.e., the euro rose from \$1.28 to \$1.33). This drop in the dollar should help companies grow their earnings at a faster rate this quarter than last quarter.

On Thursday, *The Wall Street Journal* featured an article entitled "Bond Investors Turn to Cash," which implied that bond investors are hesitant to jump into stocks. According to Investment Company Institute data, investors withdrew an estimated \$43 billion from taxable bond funds in June – the largest monthly outflow ever recorded – but the proceeds largely went into money market funds, not stocks. We believe that should change, as leading stocks with strong sales and earnings should benefit from the ongoing flight to quality.

#### **Stat of the Week: Durable Goods Orders Rose 4.2% in June**

On Thursday, the Commerce Department announced that durable goods orders surged 4.2% in June, the third straight monthly increase following a revised 5.2% in May and 3.6% in April. The June surge was much better than economists' consensus estimate of a 2.3% rise. As in previous months, a huge (31.4%) surge in civilian aircraft orders caused transportation orders to rise 12.8% in June. Also, unfilled orders rose 2.1%. This rising order backlog will likely help boost durable goods orders in upcoming months.

Despite the surge in second-quarter durable goods orders, most economists' still believe that GDP growth will sink to barely 1% for the second quarter before rising to something like 2.4% in the third quarter. On Wednesday, the Census Bureau announced that June's new home sales rose to the highest level in more than five years, to an annual rate of 497,000, significantly above economists' consensus estimate of 483,000. According to the Census Bureau, the median price of a new home has risen 7.4% in the last year to \$249,700. The supply of new homes has fallen to only 3.9 months based on the current sales pace, so housing starts could start to rise in upcoming months. Homebuilders remain cautious, however, since they fear rising mortgage rates will cut into demand, so the inventory of homes for sale is expected to remain tight, which

may result in a continuing rise in new home prices in the upcoming months.

Finally, on Friday, the University of Michigan/Reuters released its final consumer sentiment index for July. This widely-watched consumer sentiment index reached 85.1 vs. a preliminary reading of 83.9, thereby reaching a six-year high. (This index usually accompanies improvement in consumer spending.)

### Europe May Finally be Emerging from its Long, Deep Recession

Europe appears to be climbing out of its deep recession, which began in late 2011. Economist Ed Yardeni reported last week that the latest Leading Indicators for Europe are turning up. Specifically, the OECD Index for the European region rose to 100.2 in March after 16 consecutive monthly readings below 100. It's especially interesting to note that some of the most troubled euro-zone nations have all crept back above the crucial 100 mark, including Italy, Spain, Ireland, Greece, and Portugal. That's one reason the MSCI Europe stock price index has grown by about 9% since June 24, outperforming the S&P 500.

The London-based Center for Economic Policy Research and the Bank of Italy's Eurocoin indicator also reached their highest level since the first half of 2012. This indicates that Europe is slowly but steadily crawling out of its recession.

Turning to China, HSBC reported last Tuesday that its Purchasing Managers Index (PMI) declined to a "flash" reading of 47.7 in July, down from a revised 48.2 in June. The HSBC China PMI is now at an 11-month low, raising concerns of an Asian economic slowdown, since any reading below 50 signals a contraction. But we should also remember that China's growth has only "slowed" to 7.5% per year, the highest growth rate in the world. Many other Asian economies are also reporting 4% or better annual growth in their most recent quarter, including Indonesia (+6.0%), Thailand (+5.4%), and India (+4.8%).\*

The U.S. needs a strong global economy – particularly in Europe and East Asia –to continue to prosper. With Europe returning to health and Asia growing by over 4%, U.S. corporate earnings should grow faster this quarter than last quarter, especially if the dollar starts to decay again, giving U.S.-based multi-nationals a boost when converting their global revenues from stronger currencies back into dollars.

\*Source for Asian growth rates: *The Economist*, July 27 – Aug. 2, 2013, page 76

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### Marketmail gets updated on Fridays and whenever the DOW closes up or down 300 points or more.

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