MORNING BRIEFING
December 21, 2015

May the Force Be With You!

The next Morning Briefing will be sent on Monday, January 4, 2016.
We wish you all the best during the holidays and the year ahead.

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Strategy: The Force vs. the Dark Side. We saw Disney’s “Star Wars: The Force Awakens” on Saturday. My forward-thinking wife reserved seats for our family two months ago. I enjoyed the movie and review it below. It’s a huge hit that could earn well over $1 billion. Yet Disney’s stock price dropped 4% on Friday as investors sold on the good news, as well as on the bad news that an industry analyst cut his price target on the stock.

It was that kind of week last week. The S&P 500 rose 3.0% from Monday through Wednesday as investors anticipated a “dovish tightening” by the Fed, which is exactly what the FOMC delivered on Wednesday. However, the stock index dropped 3.3% on Thursday and Friday, closing the week down 0.3%. It has also been that kind of year so far. Consider the following:

(1) Lots of commotion. There is still time for a Santa Claus rally. However, Joe and I expected the stock market rally to continue following that script after Fed Chair Janet Yellen’s dovish press conference. It still could in the eight remaining trading days of this year. The S&P 500 is down 2.6% ytd, but with lots of volatility, especially among the sectors (Fig. 1, Fig. 2, and Fig. 3).

Only four of the 10 S&P 500 sectors are up ytd, while the rest are down: Consumer Discretionary (7.4%), Health Care (3.0), IT (2.6), Consumer Staples (1.6), Telecom Services (-3.7), Financials (-5.5), Industrials (-7.0), Utilities (-10.0), Materials (-12.6), and Energy (-25.2). Among the 10 S&P 400 MidCaps, only Health Care has a positive return so far (Fig. 4). Among the S&P 600 SmallCaps, only Health Care and Utilities are in positive territory (Fig. 5).

(2) Some headwinds. What are the problems weighing on stocks, and will they persist in the new year? The JP Morgan trade-weighted dollar continued to strengthen after the Fed lifted the federal funds rate on Wednesday (Fig. 6). It is now up 20% since July 1, 2014. The price of a barrel of Brent crude fell to $36.88, matching the previous cycle low at the end of 2008 (Fig. 7). In other words, both continue to weigh on corporate earnings.

Nevertheless, Debbie and I don’t see much more upside or downside in the dollar. Over the next few weeks, we expect that Fed officials will say they are in no rush to hike rates again anytime soon. After
all, they also should be concerned that the ongoing strength of the dollar will weigh on US economic growth and keep too tight a lid on inflation. The price of oil does seem to be falling into a bottomless well, but the plunge in prices should shut off more supply. Meanwhile, it’s somewhat encouraging that the CRB raw industrials spot price index and the price of copper didn’t plunge along with oil last week (Fig. 8 and Fig. 9).

As Joe and I have noted before, the earnings picture is brighter excluding the Energy industry. In addition, so far, the strong dollar hasn’t weighed as heavily as we expected on overall earnings. While it is nearly impossible to measure the effect of the plunge in oil and other commodities prices on users, it must be a significant plus for all consumers, most businesses, and many economies.

The biggest headwind may simply be valuation. On Friday, the forward P/Es of the S&P 500/400/600 were 15.7, 16.2, and 17.1 (Fig. 10). After a seven-year bull market, stocks aren’t cheap. So the upside in the S&P 500 will be determined mostly by earnings, which should grow next year.

The question is: How much can they grow? Joe and I still are estimating 7.6% to $127.00 per share next year and 7.1% to $136.00 in 2017. Admittedly, those are optimistic projections and will require a continuation of financial engineering including stock buybacks, M&A, and restructuring. If that earnings outlook plays out, the P/E could rise a bit, and the S&P 500 could hit 2300 by the end of next year.

(3) Plenty of pessimism. While valuation multiples are high, sentiment remains relatively downbeat. Last week’s Bull/Bear Ratio, which is compiled by Investors Intelligence, fell to 1.28 from 1.63 the week before (Fig. 11). Based on recent conversations with some of our accounts, my sense is that the consensus is relatively pessimistic about next year. A few are concerned about the US experiencing a “stall recession.” This scenario is the subject of this week’s Barron’s interview with economist David Levy. The title of the article is “The Global Recession of 2016.” Levy has often been on the Dark Side.

On the other hand, the Force is still with economic growth, according to the latest Index of Leading Economic Indicators, as Debbie discusses below. The index rose 0.4% m/m during November to a new cyclical high, matching the previous cycle high (Fig. 12). The Index of Coincident Economic Indicators rose to yet another record high last month (Fig. 13). In a previous analysis of this indicator, we concluded that the history of the past five cycles implies that the next recession may not occur until March 2019. That’s consistent with our case for a secular bull market in stocks. (Click ★ to add Leading & Coincident Indicators to MyPage.)

(4) Sad news, Virginia. I asked Joe to assess the likelihood of a Santa Claus rally. He came back with the following, which raises some doubts about the prospect: “The S&P 500 needs to rise 53.36 points, or nearly 2.7%, to 2058.91 in the last eight trading days to beat 2014’s closing price of 2058.90. How likely is it that we could see a year-end rally? It’s a moonshot. Six Apollo missions had men walk on the moon between 1969-1972, but the S&P 500 has registered an eight-day yearend rally of at least 2.7% only five times since 1928. In the 87 years since 1928, the S&P 500’s last eight days were positive just 15 times (17%) and down 72 times (83%).

“The market was up as much as 6.1% in 1991 and fell as much as 10.0% in 1937, for an average eight-day loss of 1.4% since 1928. During its best stretch, the S&P 500 rose six times in the 11 years from 1928-1938, but then fell for 34 straight years from 1939 to the last Apollo mission in 1972. Recent history has not been much better--the market has risen only once (a 1.7% gain in 2011) in the 15 years since 2000.”

Yes, Virginia, there is a Santa Claus, but he may not be as bullish for stocks as widely believed. This year, Santa’s portfolio may be mostly in Treasury bonds.
The Great Disruption: From Brawn to Brain. Last Thursday, Jackie and I introduced a new long-term theme, “The Great Disruption,” which we will be exploring in 2016 and beyond. It is increasingly obvious that technology is disrupting business models. That’s what it has always done. It just seems to be doing it faster and in more industries than ever before. Last week, we focused on technological innovations that are disrupting the energy and finance industries.

In the past, technology disrupted animal and manual labor. It speeded up activities that were too slow when done by horses, like pulling a plow or a stagecoach. It automated activities that required lots of workers. Assembly lines required fewer workers, and increased their productivity. The focus was on brawn. The Great Disruption is increasingly about technology doing what the brain can do. Today, Melissa and I extend our analysis of The Great Disruption to the implications of the rise and proliferation of smart machines.

Smart Machines I: LOL or COL? Robots with artificial intelligence are coming. Should we laugh out loud--happy that they will do lots of our dirty work? Or should we cry out loud--fearing that they will take away all of our jobs? Perhaps the most significant disruptive force at the forefront of technological innovation is the meeting of machines and hyper-connected systems, according to a March Wired article. “Smart machines” are the birth child of this powerful combination. There isn’t a single agreed-upon definition for them yet. That’s probably because they are undergoing major development for a multitude of applications. In essence, smart machines are computing systems that are capable of making autonomous decisions, like robots and self-driving cars.

Like smartphones, smart machines are about to penetrate the world in a major way. In 2014, industrial robot sales increased by 29% to the highest level recorded for one year, according to the International Federation of Robotics. We humans can laugh about it or cry about it. Either way, the robot revolution is going to disrupt the way we work. Here are a few compelling reasons why the coming of robots is so important:

(1) Cost of a bot. At least two different types of manufacturing robots can currently be purchased for the cost of about a low-salaried employee. Baxter, the world’s first dual-arm collaborative robot for manufacturing, has a current base price of just $25,000, as listed on the Rethink Robotics website. Foxbots, also used to perform routine manufacturing jobs, cost about $20,000 per year, according to the December 2014 Harvard Business Review (HBR). Still, the fully loaded cost of purchasing and operating a robot varies widely across applications.

Several industries are on the verge of reaching, or have already reached, the point where it’s cheaper to employ robots than humans, according to a BCG note. For example: “A human welder today earns around $25 per hour (including benefits), while the equivalent operating cost per hour for a robot is around $8 when installation, maintenance, and the operating costs of all hardware, software, and peripherals are amortized over a five-year depreciation period. In 15 years, that gap will widen even more dramatically,” the analysts calculate.

(2) Ideal vs. idle workers. “Automation is inevitable. It’s a tool to produce abundance for little effort. We need to start thinking now about what to do when large sections of the population are unemployable through no fault of their own. What to do in a future where, for most jobs, humans need not apply,” said a C.G.P. Grey YouTube video as quoted in a 9/5 Barron’s thought piece. In the same regard, HBR warned that “we will soon be looking at hordes of citizens of zero economic value. Figuring out how to deal with the impacts of this development will be the greatest challenge facing free market economies in this century.”
Robots ultimately may make better employees than humans in a lot of ways. They don’t need to take bio breaks, eat lunch, go home to see their families, or sleep. And you won’t find them making trips to the water cooler, getting involved in office politics, or otherwise losing focus from assigned tasks. They can work anywhere and won’t hesitate to relocate. They can operate in dangerous environments without requiring employers to worry about lawsuits. They won’t care, complain, or get frustrated unless they’re programmed to do so—nor learn to on their own.

Seriously, though, companies are sure to reap productivity boosts and labor cost savings from the use of robots and other smart machines, especially as they become smarter and more affordable. On its Q3 earnings call, Amazon executives touted the benefits of using robots over the cost: “[The] capital intensity [of our fulfillment centers using robots] is offset by their density and throughput. So it’s a bit of an investment that has implications for a lot of elements to your cost structure, but … pairing our associates with … robots to do some of the hauling of products within the warehouse has been a great innovation for us. We think it makes the warehouse jobs better and … our warehouses more productive.”

It’s not easy to estimate just how many human jobs will be replaced by robots. A 2014 Gartner presentation indicated that one in three jobs will be taken by smart machines by 2025. According to a lengthy 2013 Oxford paper, around 47% of total US employment is at high risk of automation over the next decade or two. Two high-tech industry pundits writing in HBR recently forecasted that nearly 30% of today’s workforce will be of no economic value by 2025. Forrester’s less extreme projection is that “16% of jobs will disappear due to automation technologies between now and 2025, but … jobs equivalent to 9% of today’s jobs will be created.”

Net, net, lots of jobs will be automated, but new kinds of jobs will be created too. Indeed, an engineering degree may be required for humans to remain competitive in the workforce. Of course, humans are still required to create and enhance robots as well as attend to their ongoing maintenance. Further, creative humans with soft skills unlikely to be matched in the robot world will certainly be more likely to be employable than low-skilled laborers. Before we know it, most humans at least will be required to work alongside robots.

Smart Machines II: They’re Here! As smart machine technology becomes more affordable and more widely adapted, it’s unlikely that any industry or occupation will remain untouched by its transformation. Robot labor has already had a transformational impact on goods-producing industries. More slowly adapting to the use of robot workers are service-related industries. However, many service-oriented fields are on the cusp of rapid transformation based on recent advances in robotic engineering. Let’s take a look at some examples by field.

(1) Manufacturing. Foxconn, the world’s largest contract manufacturer, initially installed 10,000 robots in 2011 and is now doing so at a pace of 30,000 per year. The robots are used to perform routine manufacturing tasks including spraying, welding, and assembly. During the summer of 2013, Foxconn’s CEO said at the company’s annual meeting: “We have over one million [human] workers. In the future we will add one million robotic workers.” (For more on this, see the prior-mentioned HBR article.)

(2) Apparel. Another production example, SoftWear Automation, an Atlanta-based start-up, is changing the way apparel is produced, as discussed in an 11/23 WSJ article. So far, SoftWear’s SewBots can do basic sewing tasks with a few human workers attending to them. Their engineers are working on getting the bots by next year to produce garments from start to finish.

(3) Logistics. In March 2012, Amazon announced its acquisition of Kiva Systems for $775 million. “Amazon has long used automation in its fulfillment centers, and Kiva’s technology is another way to
improve productivity by bringing the products directly to employees to pick, pack and stow,” according to the press release. Fast-forward to the online retailer’s Q3 earnings call, when Amazon executives said that 30,000 bots were being used in 13 fulfillment centers. That’s double the 15,000 they had in 10 warehouses at the end of 2014. And their intent is to use robots more widely.

(4) Transportation. In the 12/17 Morning Briefing, we discussed the proliferation of self-driving cars in detail. Recently hitting the roadways of Germany was a test of a semi-autonomous truck. Oh, and, let’s not forget the drones! We have heard a lot about Amazon’s testing of drones for end-to-end product delivery. (By the way, drones have many other applications outside of logistics. See Internet analyst and venture capitalist Mary Meeker’s slide #81-86 and 187-190 for more.)

(5) Restaurants. In a video of a recent Tokyo expo showcase, robots can be seen chopping carrots, mixing ingredients, icing a cake, and wrapping sushi rolls. The clip is titled: “Japan’s chef of the future is a robot.” In the US, the CEO of Panera Bread, a casual dining chain, said on the company’s Q3 earnings call: “Labor is going to go down … as digital utilization goes up, and--like the sun comes up in the morning--it is going to continue to go up … much as you are seeing it happen in Panera today.”

(6) Medicine. The Da Vinci robot is just what the doctor ordered. The four-armed surgeon-operated robot has already transformed the way patients are operated on in a UK hospital, as described in a 5/8 Guardian article. “You can rotate the instruments 360 degrees, so they are more dexterous than the human hand,” said the hospital’s robot coordinator. “We are going into places now that we couldn’t get into before.”

(7) Entertainment. The 12/14 Bloomberg showed a picture of a very creepy-looking robotic baccarat dealer named “Min” at a demonstration in the headquarters of a Chinese entertainment company. Currently, Min can only deal cards, but she’s in the shop to be programmed for interacting with customers. In the near future, robots like Min are expected to be introduced in US casinos.

Smart Machines III: Your New BFF. Indeed, there are certainly many other examples where robots can and will be utilized in the near future. Additionally, lots of new technologies that don’t require physical bots per se are automating jobs in service-related fields like journalism and finance. The point is: The robot revolution isn’t coming, it’s already here--and it’s everywhere! Today’s most impressive humanoid robots possess a variety of soft skills that can be leveraged in a multitude of ways across industries. Here are a few intriguing examples:

(1) Best frenemy. Japan’s Softbank’s cute-young-boy-like robot named “Pepper” demonstrated the ability to identify human emotions on stage at the WSJDLive 2015 conference. Like many of today’s smart machines, Pepper is also able to integrate various developers’ software applications to enhance “his” growing list of useful skills, like taking a selfie, as seen in a 2/15 Japan Times YouTube video.

Not all robots are cute, though. “Russia and China are building highly autonomous killer robots” was the title of a 12/15 Business Insider article. While a robot army may sound like a concept in your favorite science fiction movie, it may soon become a reality. A Russian defense contractor has said it will show prototypes of combat robots within two years, noted the article.

(2) Back to pre-school. Machines are learning the way toddlers do at Berkeley’s technology research hall. There, robots can be found playing with Legos, wooden spoons, model planes, and a set of square and round pegs, recounted Bloomberg in a 9/2 special feature. BRETT, a child-like robot, even takes pauses to think as he discovers the world!
Winning games. Google’s DeepMind AI team has invented a computer that can learn to play and beat humans at video games, as they presented in a 2/26 Nature science journal letter. So robots now are capable of engaging in reinforcement learning, i.e., using cognitive functions to determine how to act in specific environments. In other words, they can program and train themselves.

Walk in the woods. Google’s Boston Dynamics has a robot named “Atlas” that’s mastered the balance and other abilities required to take a stroll through the woods. Though not perfectly nimble yet, Atlas is undergoing training similar to military boot camp. “Researchers kick the robot, throw weights at it or make it walk over rock beds to observe how well it adapts to challenges,” reported the 8/18 NYT.

Hazardous work. The earlier-mentioned Baxter robot has undergone testing in a simulation as lab assistant for Ebola workers, thereby reducing the risk of contagion. PackBots were utilized to search for victims in places where humans couldn’t go at the 9/11 disaster zone. Just last week, the WSJ reported that new robots have been deployed at the scene of Japan’s Fukushima nuclear meltdown to aid in the decontamination process.

Movie. “Star Wars: The Force Awakens” (+ +) (link) is the seventh in this series of movies about the all-too-predictable outlook for humans and comparable intelligent life from other galaxies: Inevitably, there will be more wars with weapons that can wipe out more of us. There will always be a “Supreme Leader” with his storm-troopers fighting rebel forces somewhere in the universe. The first movie in the series appeared during 1977, or 38 years ago. No wonder the latest one was a bit like going to a high-school reunion and catching up with old friends—who are much older now—like Mark Hamill, Harrison Ford, and Carrie Fisher. Only the robots and Chewbacca haven’t aged a bit. The latest movie was a well-done homage to the original.

CALENDARS

US. Mon: Chicago Fed National Activity Index 0.15. Tues: Real GDP & Price Deflator 2.0%/1.3%, Corporate Profits, FHFA House Price Index 0.4%, Existing Home Sales 5.35mu, Richmond Fed Manufacturing Index. Wed: Personal Income & Consumption 0.2%/0.3% Headline & Core PCED 0.0%/0.1%, Consumer Sentiment Index 92.0, Durable Goods Orders Total and Ex Transportation -0.5%/0.0%, New Home Sales 503k, MBA Mortgage Applications. Thurs: Jobless Claims 270k, Weekly Consumer Comfort Index. Fri: None. (Bloomberg estimates)

Global. Mon: Eurozone Consumer Confidence -5.7. Tues: Germany GfK Consumer Confidence Survey 9.3, Japan Small Business Confidence. Wed: France GDP 0.3%/q/q/1.2%/y/y, UK GDP 0.5%/q/2.4%/y/y, Canada GDP, Canada Retail Sales, BOJ November Meeting Minutes. Thurs: Japan CPI Headline, Core, and Core-Core 0.3%/0.0%/0.8% y/y, Japan Household Spending -2.2% y/y, Japan Jobless Rate 3.2%. Fri: Japan Leading & Coincident Indexes, Japan Housing Starts 892k. (DailyFX estimates)

PERFORMANCE & ASSET ALLOCATION

Global Stock Markets Performance (link): The US MSCI index dropped 0.3% last week, ranking 33rd of the 49 markets as 30 markets rose in US dollar terms—compared to 30th a week earlier, when it tumbled 3.8% as three markets rose. The AC World ex-US index outperformed, rising 0.3% versus a 3.2% decline a week earlier. The best-performing regions last week: EMEA (1.9%), EM Asia (1.5), EM Eastern Europe (1.0), and EMU (0.4). The week’s worst: EAFE (-0.2) and EM Latin America (0.2). South Africa and Colombia were last week’s best performers among countries, with gains of 13.1% and 6.9%, respectively. Last week’s biggest decliners: Brazil (-4.0) and Czech Republic (-3.4). The US MSCI ranks 31/49 so far in December with a 3.7% decline, slightly behind the AC World ex-US’s 3.3%
decline. Just 9/49 countries are positive so far in December, and all of the regions are negative mtd, with EM Asia (-1.9) down the least and EM Eastern Europe (-7.4) down the most. December’s best-performing countries: Egypt (6.1) and Pakistan (2.0). December’s worst performers: South Africa (-10.7) and Russia (-10.2). The US MSCI ranks 12/49 ytd with a decline of 2.6% versus the AC World ex-US’s 9.2% drop; seven of the 49 markets are positive ytd. All regions are negative ytd now, but EMU is the best performer with a drop of only 4.1%; EM Latin America continues to rank the worst (-31.8). The best country performers ytd: Hungary (32.4) and Denmark (19.2); the worst: Greece (-62.5) and Colombia (-46.4).

S&P 1500/500/400/600 Performance (link): All three market-cap indexes moved lower again last week as 10/30 sectors rose, better than the prior week when all 30 sectors fell. LargeCap (-0.3%) was down for a second straight week as MidCap (-1.0) and SmallCap (-0.5) dropped for a third week in a row. These declines leave LargeCap 5.9% below its May 21 record high, MidCap 11.2% below its June 23 record, and SmallCap 10.7% below its June 23 record high. Compared to their August 25 lows, LargeCap is 4.8% higher and SmallCap is up 1.0%, but MidCap is now 0.1% below. Among the three market-cap groups, 18/30 sectors are above their August 25th lows compared to just 3/30 several weeks ago. Energy is the only LargeCap sector trading below its August low compared to seven sectors below for MidCap and just two for SmallCap. SmallCap Energy (-6.9) fell the most last week followed by MidCap Energy (-5.9). LargeCap is down 3.6% so far in December, beating the SuperComposite (-3.9), MidCap (-5.9), and SmallCap (-6.2). The leading SuperComposite sectors in December: Consumer Staples (0.1) and Utilities (-0.2). December’s SuperComposite laggards: Energy (-12.4) and Materials (-7.2). LargeCap is the best performer ytd, albeit with a decline of 2.6%, with SmallCap (-4.7) and MidCap (-5.3) just recently starting to lag. Consumer Discretionary is the top SuperComposite sector performer ytd (5.2), ahead of Health Care (3.7) and Tech (2.5). These SuperComposite sectors are down the most ytd: Energy (-26.1), Materials (-14.1), and Utilities (-9.6).

S&P 500 Sectors and Industries Performance (link): Five of the S&P 500’s 10 sectors moved lower last week as the index fell 0.3%. That compares to all 10 sectors falling a week earlier when the index tumbled 3.8% for its worst decline since the late August sell-off. The index is now 5.9% below its record high, but that’s up 4.8% from its 2015 low of 1867 on August 25. Last week’s best sector performers: Utilities (2.7%) and Telecommunication Services (1.3). Last week’s biggest underperformers: Materials (-3.0) and Tech (-1.3). The S&P 500 is now down 3.6% so far in December with eight of 10 sectors lower. Consumer Staples is the best performer mtd with a gain of 0.4%, followed by a 0.1% rise for Utilities. December’s worst performers: Energy (-12.0) and Materials (-6.8). The S&P 500’s ytd decline of 2.6% is up from a ytd decline of 9.3% at the August 25 correction low, and not far off its peak ytd gain of 2.6% at its record high on May 21. Four sectors are positive ytd and outperforming the S&P 500, the same as a week earlier: Consumer Discretionary (7.4), Health Care (3.0), Information Technology (2.6), and Consumer Staples (1.6). The biggest ytd laggards: Energy (-25.2), Materials (-12.6), and Utilities (-10.0).

Commodities Performance (link): Five of the 24 commodities we follow rose last week, down from seven rising a week earlier. Last week’s best performers: Sugar (3.6%) and Soybeans (2.2); the biggest laggards: Natural Gas (-8.8) and Lean Hogs (-6.5). Ten commodities are higher so far in December, up from two rising for all of November. December’s leaders: Aluminum (3.9) and Wheat (2.4). December’s worst performers: GasOil (-17.5), Brent Crude (-17.4), and Natural Gas (-16.4). Seven commodities were positive for all of last year, seven were positive ytd at the end of Q2, and now just three are in the black ytd: Cocoa (11.8), Cotton (5.7), and Sugar (4.0). The worst ytd performers: Nickel (-42.1), Heating Oil (-37.9), and Brent Crude (-35.8).

Assets Sorted by Spread w/ 200-dmas (link): Spreads between prices and 200-day moving averages (200-dmas) rose last week for 2/24 commodities, 8/9 global stock indexes, and 9/30 US stock indexes
compared to 7/24 commodities, 1/9 global stock indexes, and 0/30 rising a week earlier. Sugar and Cocoa are trading at 15.1% and 3.9% above their 200-dmas and are the only commodities doing so. Nickel improved the most w/w among commodities (up 1.8ppts to -23.8%). GasOil trails all commodities at 31.7% below its 200-dma, but Natural Gas was the worst performer w/w as it fell 6.5ppts to -29.2% below its 200-dma. Commodities’ average spread weakened w/w to -14.5% from -11.9%. All nine global indexes continue to trade below their 200-dmas, but eight improved w/w. Brazil was the only country to weaken w/w, albeit barely--by 0.5ppt to -9.7%--and is now the lowest of the global indexes. Japan still leads the global indexes at 1.0% below its 200-dma, well ahead of South Korea (-2.5) in second place. The global indexes’ average spread improved to -5.3% from -6.7%. Seven of the 30 US stock indexes trade above their 200-dmas, unchanged from a week earlier, as their average spread fell to -5.2% from -4.3%. SmallCap Utilities still leads all US stock indexes at 6.3% above its 200-dma, followed by SmallCap Telecom (3.9). At the other end of the spectrum, SmallCap Energy continues to lag the US stock indexes and all assets at 34.1% below its 200-dma and was the weakest last week, as it slipped 6.1ppts. LargeCap Utilities was the strongest, rising 3.6ppts to -0.6%.

S&P 500 Technical Indicators (link): A mix of cross-currents best describes the S&P 500’s technical picture. The S&P 500 ended the week lower relative to its 50-day moving average (dma) and 200-dma, but moved back into a Golden Cross as its 50-dma closed above its 200-dma for the first time since August 26. However, the S&P 500’s 50-dma started falling for the first time in eight weeks; its 200-dma is edging lower now after struggling to move higher since late August. The S&P 500 weakened to 2.8% below its now-falling 50-dma from 2.3% above a week earlier, and dropped to 2.7% below its slowly falling 200-dma from 2.4% below its slowly falling 200-dma a week earlier. Its 50-dma relative to its 200-dma improved to a 16-week high of 0.1% from -0.2%. Industrials became the fourth sector to move into the Golden Cross club in the latest week as it joined the Consumer Discretionary, Consumer Staples, and Tech sectors. All 10 sectors still trade below their 50-dmas, down sharply from eight sectors above their 50-dmas two weeks earlier. Three sectors (Consumer Discretionary, Consumer Staples, and Information Technology) trade above their 200-dmas, down from five sectors two weeks earlier: Just four sectors have a rising 50-dma (Health Care, Industrials, Tech, and Telecom), down from eight a week earlier. Three sectors now have a rising 200-dma, up from two a week earlier as Consumer Staples turned upward and joined Consumer Discretionary and Information Technology.

US ECONOMIC INDICATORS

Leading Indicators (link): Leading indicators rose the first two months of this quarter after not posting a gain during the three months of last quarter. The Leading Indicators Index (LEI) increased 0.4%, building on October’s 0.6% gain, to a new cyclical high. It’s only fractionally below its record high recorded in March 2006. According to the Conference Board, “Although the six-month growth rate of the LEI has moderated, the economic outlook for the final quarter of the year and into the new year remains positive.” Five of the 10 indicators contributed positively to November’s LEI, four contributed negatively, while the average workweek was unchanged. The biggest positive contributors were building permits (0.32ppt), the interest-rate spread (0.24), and stock prices (0.11), followed by the leading credit index (0.09) and real consumer durable goods orders (0.02). The new orders diffusion index (-0.13) and jobless claims (-0.08) were the biggest drags; real core nondefense capital goods orders (-0.02) and consumer expectations (-0.01) also detracted from growth.

Coincident Indicators (link): The Coincident Indicators Index (CEI) hit yet another record high last month. The CEI rose for the 20th time in 23 months, up 0.2% in October and 4.7% over the period, and hasn’t posted a decline since January 2013. Three of the four components advanced last month, each once again reaching new record highs: 1) Nonfarm payroll employment climbed 0.1%; it hasn’t posted a decline since June 2010. 2) Personal income--excluding transfer payments--increased for the 24th time in 25 months, up 0.2% m/m and 8.4% over the time span. 3) Real manufacturing & trade sales climbed
0.3% m/m and 7.6% over the past 25 months. 4) Industrial production remains the one outlier, falling 0.6% in October--the eighth decline this year (the only increases were July’s 0.8% and August’s 0.1%).

**Regional M-PMIs (link):** Early indications from regional PMIs suggest manufacturing activity continued to contract this month. Just two Fed districts have reported so far: New York and Philadelphia; we average the composite, orders, and employment measures as data become available. The two regions show the composite index was negative for the fifth month, coming in at -5.2 this month after sinking to a four-year low of -10.3 in September. Philly’s index (from 1.9 to -5.9) fell back into negative territory; New York’s was negative for the fifth month, though has improved steadily from -14.9 in August to -4.6 this month. The new orders measure (-7.8 to -7.3) was little changed, though is up from October’s -14.8, which was its weakest performance since May 2009. New York’s gauge (-11.8 to -5.1) showed orders fell at a considerably slower pace, while Philadelphia’s (-3.7 to -9.5) fell at a faster pace. The employment index (-2.3 to -6.0) posted its third negative reading after a string of positive gains stretching back to July 2013. New York (-7.3 to -16.2) manufacturers cut jobs at their fastest pace since July 2009, while Philadelphia’s (2.6 to 4.1) are starting to higher again, though slowly.

**GLOBAL ECONOMIC INDICATORS**

**Germany Ifo Business Climate Index (link):** "The economic situation could hardly be better in the run-up to Christmas," said Ifo’s president, noting that German manufacturers revised up their production plans. The Ifo business climate index dipped to 108.7 this month, barely changed from November’s 109.0—which was the highest since June 2014. German businesses remained optimistic about the future, but were a little less content about the present. The expectations component was unchanged at its cyclical high of 104.7, while the present situation fell for the third month (to 112.8) since reaching its cyclical peak of 114.9 in August. The expectations component correlates closely with German factory orders and production; the overall index tracks exports more closely. Recent data suggest a pickup in growth.

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