



## >: Chris Rowe's Market Wrap Up August 11, 2008

Monday, August 11, 2008 / Chris Rowe

Did you see Chris Rowe's most recent market wrap up?

Every Monday afternoon at 6:30pm EST. he's posting a SUPER FAST market wrap-up for those of you who want to take a quick peek at the market, and go back to enjoying your life!

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?Profit from the Trend?

A handwritten signature in black ink that reads 'Chris Rowe'.

Chris Rowe

Chief Investment Officer

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## Economic Calendar for the Week of August 11 - August 15

### Wednesday, August 13

*08:30 Retail Sales*

#### Release Details

- \* Importance (A-F): This release merits an A-.
- \* Source: The Census Bureau of the Department of Commerce.
- \* Release Time: 8:30 ET around the 13th of the month (data for one month prior).
- \* Raw Data Available At: <http://www.census.gov/svsd/www/advtable.html>.

The retail sales report is a measure of the total receipts of retail stores. The changes in retail sales are widely followed as the most timely indicator of broad consumer spending patterns. Retail sales are often viewed ex-autos, as auto sales can move sharply from month-to-month. It is also important to keep an eye on the gas and food components, where changes in sales are often a result of price changes rather than shifting consumer

demand.

Retail sales can be quite volatile and the advance reports are subject to rather large revisions. Retail sales do not include spending on services, which makes up over half of total consumption. Total personal consumption is not available until the personal income and consumption reports are released, typically two weeks after retail sales.

## Highlights

- \* June retail sales rose 0.1%. Excluding autos, they were up 0.8%. Both numbers were a bit shy of the market's expectations.

- \* Excluding gasoline sales, retail sales declined 0.5%. Much was made of this fact and it was interpreted to mean there wasn't any discretionary spending during the month. Also, it was regarded as a sign that the impact of the fiscal stimulus checks isn't working. Those views were wrong on both counts. If you exclude auto sales, as well as gasoline and grocery store sales, you'll see that retail sales were still up 0.2% versus May.

- \* Retail sales, excluding autos, were up 5.5% versus the same three-month period in 2007. The gain supports the idea that the fiscal stimulus is providing a real boost to spending in the face of well-documented macro pressures.

## Big Picture

- \* Consumer spending has remained resilient in the face of lower home prices, higher gas prices, and stagnant to slightly lower employment levels. Retail sales were trending flat to up a bit in the first quarter. Spending has picked up a bit in the second quarter as the fiscal stimulus kicked in. Real personal consumption expenditures were up at a 1.1% annual rate in the first quarter, but solid gains in retail sales for April and May suggest the second quarter growth will be closer to 2.5%. Spending will get a major boost starting in May with the \$110 billion in fiscal stimulus sent to individuals. Retail sales should partially reflect this in May, but even more strongly in future months. A consumer led recession simply never developed, and spending is now turning higher.

## Thursday, August 14

08:30 *CPI: Consumer Price Index*

### Release Details

- \* Importance (A-F): This release merits a B .
- \* Source: Bureau of Labor statistics, U.S. Department of Labor.
- \* Release Time: 8:30 ET, about the 13th of each month for the prior month.
- \* Raw Data Available At: <http://stats.bls.gov/news.release/cpi.toc.htm>.

The Consumer Price Index is a measure of the price level of a fixed market basket of goods and services purchased by consumers. CPI is the most widely cited inflation indicator, and it is used to calculate cost of living adjustments for government programs and it is the basis of COLAs for many private labor agreements

as well. It has been criticized for overstating inflation, because it does not adjust for substitution effects and because the fixed basket does not reflect price changes in new technology goods which are often declining in price. Despite these criticisms, it remains the benchmark inflation index.

CPI can be greatly influenced in any given month by a movement in volatile food and energy prices. Therefore, it is important to look at CPI excluding food and energy, commonly called the "core rate" of inflation. Within the core rate, some of the more volatile and closely watched components are apparel, tobacco, airfares, and new cars. In addition to tracking the month/month changes in core CPI, the year/year change in core CPI is seen by most economists as the best measure of the underlying inflation rate.

## Highlights

- \* Total CPI jumped 1.1% from May and is up 5.0% year-over-year. Core CPI, which excludes food and energy, jumped 0.3% and is up 2.4% year-over-year versus 2.3% seen in May.

- \* Energy and food prices, not surprisingly, were the drivers of total CPI. The core number picked up due to larger increases in the indexes for shelter and tobacco and smoking products, as well as an upturn in the apparel index.

- \* Food and beverage index 0.7%; Housing index 0.5% (owner's equivalent rent 0.3%); Apparel index 0.1%; Transportation index 3.8% (gasoline 10.1%); Medical Care index 0.2%

- \* We're still not seeing a strong pass-through of the inflation seen at the wholesale level, yet the core trend year-over-year moved in the wrong direction in June for a jittery market.

## Key Factors

- \* Year-over-year increase in total CPI stands at 5.0% through June. The year-over-year core rate bumped up to 2.4% in June from 2.3% in May.

## Big Picture

- \* The inflation outlook is mixed. Core rates of inflation are moderate, and will remain so, because of weak economic demand. Commodity prices continue to rise. Food accounts for 14.9% of the index, and energy 9.7%. If commodity prices level off, the outlook for inflation is extremely good. If commodity prices continue to rise, the outlook is for moderate inflation. It does not appear as if rising energy prices will lead to higher prices in other categories. Most businesses are not able to pass along this higher cost to a large degree.

## Friday, August 15

09:15 Capacity Utilization

## Release Details

- \* Importance (A-F): This release merits a B-.

- \* Source: Federal Reserve.

- \* Release Time: 9:15 ET around the 15th of the month (data for month prior).

\* Raw Data Available At: <http://www.federalreserve.gov/releases/G17/Current/g17.txt>.

The index of Industrial Production is a fixed-weight measure of the physical output of the nation's factories, mines, and utilities. Manufacturing production, the largest component of the total, can be accurately predicted using total manufacturing hours worked from the employment report. One of the bigger wildcards in this report is utility production, which can be quite volatile due to swings in the weather. Severe hot or cold spells can boost production as increased heating/cooling needs drive utility production up.

In addition to production, this monthly report also provides a measure of capacity utilization. Though the rate of capacity utilization is seen as a critical gauge of the slack available in the economy, the market does not completely trust this measure. Capacity is very difficult to measure, and the Fed essentially assumes that growth in capacity in any given year follows a straight line. One can therefore predict the capacity utilization rate quite accurately based on the assumption for production growth. The 85% mark is seen as a key barrier over which inflationary pressures are generated, but given revisions to these data and the difficulties with capacity measurement, the 85% mark should be viewed cautiously. It would be appropriate to look for corroborating inflation indications from commodity prices and vendor deliveries.

## Highlights

\* Following a 0.2% decline in May, industrial production increased 0.5% in June. That was well ahead of the 0.1% consensus estimate.

\* The utilities component, which declined 2.1% in May, was up 2.1% in June. The mining component also saw a big increase, registering a 1.1% jump in June versus a 0.3% increase in May. The core manufacturing component increased 0.2% following a 0.1% decline in May.

\* The rebound in manufacturing stemmed in large part from a 5.4% increase in the output of motor vehicles and parts, as activity resumed at plants that had been idled during the American Axle strike.

\* Critics will jump on the idea that manufacturing output declined 0.1%, excluding motor vehicles and parts, but it counts here just as it did when it acted as a drag on industrial production during the strike period.

\* Industrial production is up 0.3% year-over-year. That increase is reflective of a weaker economic climate, yet rates as good economic news given the headwinds the economy has faced in that time.

\* Capacity utilization picked up to 79.9% from 79.6%

## Big Picture

\* Surprising resilience in manufacturing is a major reason the period of weak economic growth late last year and early this year did not turn into a recession. Industrial production in June was 0.3% above the year-ago level. In recessions, production tends to drop sharply to well below year-ago levels. For example, just prior to the 2001 recession and through 20021 and into early 2002, industrial production fell every single month. Fourteen straight monthly declines were posted, with an average decline of 0.5% per month. Year-over-year production fell to -5%. This cycle, there have been monthly declines and a leveling off in production, but that reflects considerable resilience relative to the 2001 recession.

*10:00 University of Michigan Consumer Sentiment Index*

## Release Details

- \* Importance (A-F): This release merits a B-.
- \* Source: The University of Michigan.
- \* Release Time: Preliminary: 10:00 ET on the second Friday of the month (data for current month); Final: 10:00 ET on the fourth Friday of the month (data for current month).

The Michigan index is almost identical to the Conference Board Consumer Confidence index, though there are two monthly releases, a preliminary and final reading. Like the Conference Board index, it has two subindexes - expectations and current conditions. The expectations index is a component of the Conference Board's Leading Indicators index.

## Big Picture

\* Consumer sentiment indices get way too much attention. The simple fact is that sentiment does not correlate with consumer spending and thus has little predictive value. Consumer spending correlates with income. US consumers spend virtually all their income. Higher income will lead to increased spending, regardless of sentiment. Sentiment correlates with the highly publicized trends in gas prices, political events, and other exogenous factors. Sentiment is near record lows, yet real (inflation adjusted) consumer spending was up at a 1% annual rate in the first quarter, and will be up at about a 2.5% annual rate in the second quarter. Consumers are simply grumpy as they head off to the mall to spend their income.