MV Capital Management Weekly Market Flash

The Planets Align

May 2, 2014

This has been an unusually busy week for the world of top-down investment analysis. Four headline events took place in the space of the past five days: the report on 1Q14 GDP, the Fed Board of Governors meeting, a release of the ISM manufacturing index and, to cap it all off this morning, the monthly jobs report. All of this alongside a steady drip-feed of corporate earnings to digest. How did we do?

At first glance the results would seem to be a mixed cocktail of numbers indeed, in particular, a much lower reading on GDP than expected, contrasted by a barnstorming jobs report. Truth be told, there are some green shoots and some dark clouds. But the overall take-away this week is a positive contribution to the economic recovery story. How the markets process it, of course, remains to be seen as the month of May evolves.

Jobs, Wages and the Labor Force

The headline jobs numbers were impressive. Non-farm payrolls added 288,000 new positions in April, and the unemployment rate fell to 6.3%. Growth was strong in business services and healthcare, but also in construction – perhaps surprising given talk of a slowdown in the housing market. Wages trended up by a little – 1.9% - but enough to stay slightly ahead of inflation. The big negative in the jobs report is the continued decline of the number of Americans participating in the labor force. 806,000 left the job market, sending the labor force participation rate down to 62.8% from March's 63.2% - both low by historical standards. Even here, though, there was something of a silver lining. The long term unemployment rate fell as a percentage of the overall number of unemployed, with 287,000 new jobs for those who have been out of work for more than six months.

False Negatives

"Jobs Friday" is always a circus of pundits and pontification, but the earlier release of the 1Q14 GDP estimate drew far less curiosity. The figure of 0.1% was sharply lower than the consensus estimate of 1.1%, but observers replied with a shrug and two words: "harsh winter". Buttressing that benign reaction was the higher than expected increase in the ISM manufacturing index to 54.9% from March's 53.7%. Analysts following first quarter earnings results saw a bevy of decent results. With 372 S&P 500 companies reporting as of May 2 the average blended growth rate is 1.6%. Expectations just two weeks ago were that average 1Q14 earnings would be negative. Meanwhile, the Fed voiced its own confidence in the pace of recovery and continued with the QE tapering process.

The composite picture, in our opinion, is a good one. This does not mean, of course, that markets are certain to kick into high gear (thus far, reaction to the strong jobs numbers has been basically flat). But it appears increasingly hard to make the case for a serious drawdown threat. There are still plenty of X factors in the global economy and geopolitical landscape that could appear and cause problems. But our base case remains largely where it was at the beginning of the year: modestly positive performance with perhaps a handful of contained pullbacks.

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