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Jobs and the Economy Reflect "Goldilocks" (Modest) Growth

By Louis Navellier

The S&P 500 fell 2.9% from Tuesday to Thursday morning last week before recovering to post a modest 0.8% gain for the week. The market liked the Friday jobs report, even though it was merely "OK" (with 175,000 new jobs). It was a "Goldilocks" figure, according to analysts – neither too hot nor too cold – but the good news for stock market investors is that this and many other signs of slower economic growth will likely encourage the Fed to continue its policy of quantitative easing for the time being.

Stat of the Week: 175,000 New Jobs Created in May

Last Friday, we learned that America created 175,000 new jobs in May, beating the consensus estimate of 164,000. The jobless rate ticked up to 7.6%, from 7.5%, since 420,000 people entered the labor force in May. Actually, that is a very good sign, since it reflects the first rise in the "labor participation rate" since last October. That's one reason the stock market rose strongly – up 200 Dow points on Friday.

Keith Lerner, senior market strategist at SunTrust Bank, said, "It was a Goldilocks report. If it was too hot – let's say well over 200,000 jobs – it would have gotten people concerned that the Fed would taper the stimulus more aggressively. Alternatively, if we had something below 100,000 jobs, then people would start worrying about a slowdown. Having a solid number suggests the economy is still recovering, which should support better earnings. But it suggests the Fed won't taper in an overly aggressive fashion."

Speaking of the jobs market, Wednesday's ADP (private payroll) job report said we created a net 135,000 private-sector jobs in May, up from a revised 113,000 in April. Unfortunately, economists had expected 170,000 new jobs, so the ADP report was disappointing. The ADP report is another sign that we are stuck in a Goldilocks job market, indicating continued Fed easing.

The other interesting news on the job front was that on Wednesday, the Labor Department announced that first-quarter productivity growth rose by just 0.5% (annual rate), due mostly to a massive 3.8% plunge in wage compensation. However, that drop seems to be a reaction to the dramatic (9.9%) increase in fourth quarter compensation, due to accelerated bonuses designed to beat the 2013 tax increase. Stephen Stanley, chief economist of Pierpont Securities, said this volatility in labor costs "merely reflects the income-shifting that occurred ahead of year-end, to avoid the higher tax rates that took effect January 1."

Taking the longer view, compensation has risen 2% in the last year, so it appears that the distortions in the fourth and first quarters are due to employers trying to adjust compensation to beat the 2013 tax increases.

Many Other Economic Statistics Reflect "Goldilocks" Growth

The Institute for Supply Management (ISM) shocked many economists last Tuesday when it announced that its manufacturing index declined to 49 in May, the third straight decline, down from 50.7 in April and far below economists' consensus estimate of 51. The ISM's new order index declined sharply to 48.8 in May, down from 52.3 in April, while its production index plunged to 48.6 in May, from 53.4 in April.

That indicator obviously reflects a slowdown in growth, but the other ISM indicator, released Wednesday, reflected fairly "hot" growth. The ISM non-manufacturing index (mostly covering services) represents 88% of the economy, and it rose from 53.1

in April to 53.7 in May, just above the consensus of 53.5. In addition, new orders rose from 54.5 to 56.0, and business activity rose from 55.0 to 56.5. If you average all these "hot" and "cold" ISM numbers, I believe you'll see another example of "Goldilocks" growth.

On Wednesday, the Commerce Department announced that factory orders rose 1% in April, due largely to higher demand for airplanes and vehicles. Orders for durable goods rose by an impressive 3.5% in April.

The other good news was that the Fed's Beige Book survey, released Wednesday, showed that 11 of the 12 Fed districts reported "modest to moderate" growth, while Dallas reported "strong growth." The Beige Book also said that job growth grew "at a measured pace."

The Fed also reported that U.S. household wealth grew by $3 trillion in the first quarter (a 19% annual rate) to reach a record $70 trillion. That means consumers will feel better, due to a revival of the wealth effect (i.e., rising stock and real estate prices). One indicator of rising consumer sentiment is a rise in retail sales. Thomson Reuters reported that same-store sales growth in May was "strong" at the nine retailers that it tracks, led by Costco, which posted 5% same-store sales growth. Ironically, the cover of this week's Bloomberg *Businessweek* calls Costco* "The Cheapest, Happiest Company in the World."

The Dollar Finally Falls, after Rising Too Far, Too Fast

So far this year, the dollar index (DXY) has risen too far too fast – from 79 in February to 84 in May – but it tumbled last week, when the euro and British pound rose almost 2% to the dollar and the Japanese yen rose 3%. The dollar was hardest hit Thursday after both the Bank of England and the European Central Bank agreed to leave their key benchmark interest rates unchanged at 0.5%. Despite Treasury yields rising sharply in the last month, U.S. bonds are no longer so competitive. Since both Britain and the euro-zone have higher real interest rates, big money is moving toward those higher yields.

The strong dollar of the last few months has been hard on U.S. exporters. Last Tuesday, the Commerce Department announced that the U.S. trade deficit rose 8.5% in April. Imports rose 2.4% to $227.7 billion, while exports rose 1.2% to $187.4 billion for a $40.3 billion ($484 billion annual rate) trade deficit.

Previously, the trade deficit was at a three-year low of $17.9 billion in March; then it rose to $24.1 billion in April and $40.3 billion in May. The good news is that petroleum imports (in dollar terms) declined for the third straight month, so the trade deficit could improve as the U.S. becomes more energy-independent.

The dollar is another case of Goldilocks balance: The Japanese yen has expanded too rapidly, causing a rapid fall in the yen and a bubble in Japanese stocks. Meanwhile, the euro has been "too cool," resisting any major program of quantitative easing. The dollar is in the middle – neither too hot nor too cold. Frankly, I am rooting for the dollar to weaken a bit more, boosting the earnings of many multi-national companies, especially U.S. exporters, since a weak dollar lowers the price of U.S. goods in other nations.

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

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