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In This Issue

Fed Minutes Reveal that the “Doves” are Itching to Ease
The Global Slowdown Continues to Concern Investors
Stat of the Week: The U.S. Housing Market is on the Mend

The Fed May Provide Monetary Easing “Fairly Soon”

By Louis Navellier

The market’s six-week winning streak came to an end last week with a small (0.5%) drop in the S&P 500. We will likely see one more week of these “dog days” of August, characterized by light trading volume and sideways motion. With the distraction of political conventions over the next two weeks, I suspect that the stock market will continue to meander listlessly until the August payroll report (released September 7), followed by the possibility of QE-3 coming out of the FOMC meeting September 12-13.

Fed Minutes Reveal that the “Doves” are Itching to Ease

The stock market was rattled last week after the Congressional Budget Office (CBO) warned that the U.S. economy will contract in 2013 if the scheduled tax hikes and spending cuts go into effect in January. As a result, the outcome of the next election remains crucial to clarifying the underlying economic outlook.

There was widespread speculation last week that the Fed would step in to rescue the U.S. economy if our economic growth rate continues to decelerate. This speculation was confirmed in the minutes of the latest Federal Open Market Committee (FOMC) meeting, released Wednesday. The minutes revealed that the Fed stands ready to provide “additional monetary accommodation…fairly soon, unless incoming information pointed to a substantial and sustainable strengthening in the pace of economic recovery.”

Of course, those words were recorded on August 1, when the economic news looked far gloomier than it has been recently. Since most economic indicators have been improving, I suspect the Fed may not act.

Either way, all eyes will be on Fed Chairman Ben Bernanke next Friday when he gives a speech at the Fed’s annual conference in Jackson Hole, Wyoming. Complicating matters further, the Republican Presidential candidate Mitt Romney reconfirmed last week that he does not plan to reappoint Bernanke as Fed Chairman. In addition, the Fed is now led by a majority of “doves” that President Obama appointed, so perhaps some of them may have a wee bit of politics in the back of their minds as they vote to ease.

The next FOMC meeting is scheduled for September 12-13, right after the August jobs report comes out on Friday, September 7, so if there is any Fed action, it will most likely be announced on September 13. Usually, the Fed does not like to act immediately prior to a Presidential election, since the Fed wants to be neutral, but if the doves vote for immediate easing, that could boost the President’s re-election chances.

The Global Slowdown Continues to Concern Investors

On Thursday, HSBC announced that its preliminary China Purchasing Managers Index (PMI) declined to a nine-month low of 47.8 in August, down sharply from 49.3 in July. Since any reading below 50 signals a contraction, it appears that China continues to suffer from the ongoing global slowdown. As demand from the rest of the world continues to reduce its exports, China is plagued with a rising inventory glut.

In Europe, Markit Economics announced that its preliminary Purchasing Managers Index (PMI) for the euro-zone was 46.6 in August, essentially unchanged from 46.5 in July. According to Markit, these readings are consistent with a 0.5% to 0.6% decline in third-quarter GDP. Germany has been bucking this negative trend, but Germany is also in danger of contraction, with its PMI hovering near a three-year low.

The official line from German Chancellor Angela Merkel is that Germany stands ready to help Greece "as much as we can," but she turned down Greece's latest plea for more time to implement an austerity plan. French President Francois Hollande also said that he wants Greece to remain in the euro-zone, but these leaders can hardly say otherwise, in public, since there is no clear exit plan for Greece. The next logical step would be to cut off aid to Greece and force them to make the painful cuts Germany is demanding.

We have now come to the point where most investors have already discounted the possible departure of Greece from the euro-zone. Most investors are now more focused on the likely fate of Italy and Spain.

Stat of the Week: The U.S. Housing Market is on the Mend

Very little economic news was released last week, but the National Association of Realtors announced last Wednesday that July's sales of existing homes rose 2.3% to a seasonally adjusted annual rate of 4.47 million units. With the inventory of unsold homes at 2.4 million, the supply overhang is now down to just 6.4 months. Better yet, the median price of existing homes is up 9.4% in the past 12 months, to $187,300.

On Friday, the Commerce Department announced that new orders for durable goods rose 4.2% in July to $230.7 billion. This came on top of June's 1.6% rise in durable goods orders but, as always, the details in the durable goods report revealed that the strength in July was due primarily to surging orders for aircraft. Excluding transportation orders, durable goods orders fell 0.4% in July and by a revised 2.2% in June.

Complicating matters further, durable goods orders have been artificially distorted by defense orders in recent months. Now, analysts fear that those defense orders will soon decline due to mandatory defense cuts scheduled for 2013 if Congress does not find a way of avoiding the impending "fiscal cliff."

Despite the usual media diet of fears and false alarms, I wish you and your family a happy and peaceful Labor Day weekend! The next MarketMail will come to you on Tuesday, September 4. I'll see you then.

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