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Holiday Wrap-Up

A look back at 2014 thus far

Presented by Thomas Cymer CFP® CRPC®

The year in brief. When 2013 ended, few Wall Street investment strategists had high hopes for the market - the thought was that the S&P 500 would post a single-digit advance for 2014. In fact, a Birinyi & Associates survey of said strategists produced a consensus forecast for a 5.8% gain for the index this year. Well, here we are with 2014 drawing to a close and the S&P has doubled that expectation - on the eve of Thanksgiving, it was up 12% YTD. The U.S. economy looked pretty good in comparison to many others this year, and Wall Street outpaced quite a few of the overseas markets. The dollar strengthened, which hurt the broad commodities market. The housing sector (inevitably) cooled off, but sales were still up year-over-year. Investors ended up worrying more about the Ebola virus than the end of the economic stimulus provided by the Federal Reserve.[1,2]

Domestic economic health. 2014 brought a notable reduction in unemployment, healthy job growth, and renewed consumer spending and confidence. It also saw the Fed wind down its third round of quantitative easing under a new chair, Janet Yellen.

In the 12 months ending in October 2014, U.S. payrolls expanded by an average of 222,000 hires per month. The jobless rate - 6.7% at the end of 2013 - fell further to 5.8% by October. The U-6 rate (measuring the unemployed and underemployed) declined notably as well in those 10 months, going from 13.1% to 11.5%.[3,4]

Two respected consumer confidence barometers have seen big improvements. Year-to-date, the Conference Board's consumer confidence index is up 10.6 points, ending November at 88.7; the University of Michigan's index of consumer sentiment gained 6.3 points on the way to a final November mark of 88.8.[5]

Personal spending - the great driver of the economy - rose 2.5% in the second quarter and 2.2% in the third quarter after a poor Q1. Those spring and summer gains contributed to the best six months the economy has seen in a decade. U.S. GDP reached 4.6% in Q2 and 3.9% in Q3.[6,7]
According to the Labor Department's Employment Cost Index, wages had increased 2.1% over the 12

months ending in September. That wage growth outpaced the Fed's PCE index, which measures inflation in terms of prices tied to consumer spending; the PCE index was only up 1.4% in a year as of October, well below the central bank's 2% annualized target. Falling gas prices also effectively put more money in consumers' pockets; on November 24, AAA calculated the mean price of a gallon at $2.81, a 4-year low.[6,8]

Global economic health. The economies of China and the eurozone regularly failed to meet expectations during 2014, and Japan slipped into another recession.

As fall arrived in Europe, the United Kingdom was looking at 3% annualized GDP but the economies of Germany, France and Spain were seeing less than 2% growth. European jobless rates ranged from 5% (Germany) to more than 25% (Greece). Deflation risk and the threat of another euro area recession began to emerge. By October, eurozone yearly inflation was down to just 0.4%, even as the European Central Bank cut interest rates to 0.05% and bought covered bonds.[9]

Disappointing GDP and manufacturing index readings from China triggered several down trading days this year. The Chinese economy appeared headed for its poorest year since 1990, with annualized GDP slowing to 7.3% in Q3. In November, Chinese manufacturing activity failed to expand for the first month in six. After shrinking a disastrous 7.3% in Q2, Japan's economy unexpectedly contracted another 1.6% in Q3.[10,11]

World markets. Just before Thanksgiving, a *Wall Street Journal* snapshot of global stock indices showed the S&P 500 outperforming many European indices but being outpaced by key Asia Pacific indices. In Europe, the DAX was up just 3.2% YTD, the CAC 40 just 2.0% and the STOXX 600 just 5.5%; Russia's RTS index was down 26.9% for the year. The S&P was also ahead of Canada's benchmark S&P/TSX index (+10.7% YTD) and some notable emerging market bourses - the Bovespa was +7.9% on the year, the IPC All-Share +4.0% and the Dow Jones Americas +10.2%. In the Far East, the truly subpar indices were Australia's ASX (-0.3% YTD) and Korea's KOSPI (-1.5% YTD). India's Sensex was up 33.9% YTD coming into Thanksgiving, the Nikkei 225 6.9%, the Shanghai Composite 21.3%, the KSE 100 (Pakistan) 23.6% and the PSEi (Philippines) 23.7%. On the other hand, the Hang Seng was only up 2.3% for the year and the Dow Jones Asia-Pacific just 0.3%.[12]

Commodities markets. From this past New Year's Eve to Thanksgiving Eve, the U.S. Dollar Index gained 9.5%. With the greenback showing such strength, most commodities had it rough this year. Oil was not only hurt by the dollar, but by a sustained lack of demand. The day before Thanksgiving, a barrel of West Texas Intermediate crude was worth just $73.69; the price had dropped 21.3% in 12 months. There were also huge 12-month descents in the prices of heating oil (21.6%) and gasoline (24.9%). Natural gas prices were up 12.4% year-over-year, aided by concerns over supply disruption through pipelines headed through war-torn Ukraine.[13,14]

By Thanksgiving, gold futures were down 3.7% from a year earlier, with the yellow metal worth $1,196.60 an ounce on the COMEX. Silver was at $16.55 an ounce, down 17% in 12 months. Copper had lost 8% over the past year, platinum 10.4%. Coffee was the huge winner among all marquee commodities, with futures jumping 76.7% across 12 months. Other ag futures were looking at the following annualized gains and losses: wheat, -13.2%; corn, -9.5%; soybeans, -21.5%; cocoa, +4.5%; cotton, -24.6%; sugar, -7.0%.[14]

Real estate. Year-over-year sales gains and price gains had slowed by the fall, but mortgage rates declined again. National Association of Realtors data showed a 2.5% annualized rise in resales as of October. The median sale price was $208,300 in October; the year-over-year gain in that category has averaged 5.8% so far in 2014 compared to 11.5% in 2013. NAR's October pending home sales index revealed a 2.2% annualized rise.[15,16]

Annual price gains moderated sharply: by November, the latest 20-city S&P/Case-Shiller Home Price Index (September) showed only an 4.9% advance across 12 months, as opposed to 12.4% in the March edition released in May.[5]
As of last month, new home buying was up 1.8% on an annualized basis with the median sales price at $305,000. Housing starts were up 7.7% year-over-year as of October.[17,18]
The average interest rate on a 30-year home loan fell to just 3.97% in Freddie Mac's November 26 Primary Mortgage Market Survey. Contrast that with a 4.53% average interest rate on those mortgages on January 2 and you can see why many real estate analysts see a pickup in home buying in the next few months.[19]

Looking back...looking forward. Right now, just a few Wall Street strategists have announced their market forecasts for 2015, and they don't expect a great year (as was common in 2012, 2013 and 2014). On average (according to Birinyi & Associates), they see the S&P 500 rising 4.8%. They could be proven wrong once more. To prove them wrong, the market has to overcome a couple of significant and ongoing challenges. Can it keep its momentum in the face of presumptions that the Fed will presently raise interest rates? Can it shake off the economic disappointments that regularly seem to arrive from the eurozone, Japan and China? If so, you may see another solid year for equities.[1]

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Citations.

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