Weekly Market Review

***e*Research Corporation** is pleased to provide a review of the markets by Eddy Elfenbein of **Crossing Wall Street**.

Mr. Elfenbein introduces his commentary with the following quote from Charles Munger of Berkshire Hathaway.

"It is waiting that helps you as an investor, and a lot of people just cannot stand to wait."

Read Mr. Elfenbein's analysis and market comments on the following pages.

Information about **Eddy Elfenbein** and **Crossing Wall Street** is provided at the end of this article. You can also learn about **Crossing Wall Street** by going to its blog website at: http://www.crossingwallstreet.com/.

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Bob Weir, CFA
Director of Research

March 10, 2017

Crossing Wall Street: Weekly Market Review

by Eddy Elfenbein

BW: We have taken only an extract of Mr. Elfenbein's latest weekly article. If you wish to read the entire article, which includes stocks in his recommended portfolio, there is a link provided below.

Thursday marked the eighth anniversary of the start of the great bull market. Not only is this one of the longest and largest bull markets in history, it is also one of the most hated.

I have to confess, I did not personally experience many of the other great rallies, but I doubt they were greeted with as much hostility as the present bull run. Over the last eight years, the S&P 500 has gained 246%. Yet, it seems that from Day One, people have claimed that it was crazy bubble-induced by the Fed, and was due to pop any moment.

They have been wrong, wrong, and wrong. Naturally, you will not hear any apologies. But I am happy to say that by keeping our heads while everyone else was losing theirs (and blaming us!), we did not lose our focus.

In this week's issue, I want to look at some of the issues affecting Wall Street at the moment. It looks as if Janet Yellen is going to raise interest rates next week, but suddenly, the stock market is not so worried about inflation.

Also, for the first time this year, oil dropped below $50 per barrel. The Trump Trade is suddenly on the ropes! What does it all mean?

No, The Stock Market Is NOT A Bubble

Commentators love to proclaim that the stock market, and every market really, is a bubble. Hey, it is an easy call to make. You are rarely held accountable if you are wrong. Also, you have an easy out. If the market goes higher, then you can always say that the bubble and ensuing crash will be that much worse. The crash is always just around the corner.

I will let you in on a little secret. The stock market is rarely a bubble. Don't get me wrong—the market takes its lumps. You can expect a 20% sell-off every few years. But

that is not necessarily a bubble.

For example, the big bad bear market of 2007 to 2009 was not, in my opinion, preceded by a bubble. By that, I mean that I do not believe equity valuations were excessive. Prices largely reflected fundamentals. The problem is that the fundamentals crashed. Sure, there was a bubble, but it was in real estate. Or more precisely, it was in credit, which manifested itself in real estate. But stocks? Nope, nothing crazy.

For those of you who remember 1999-2000, now *that* was a bubble. The valuations had no bearing on reality. The flimsiest companies were going public. Why? Well, they were being funded! No one wanted to be left out. "Your company is nothing but a URL and a sock puppet? Here, take a few billion dollars."

That is what a bubble is all about. The tech bubble was so intense that it actually pulled money away from sensible value stocks. I remember that several REITs were yielding over 10% or 12%. My point is that a bubble is not merely elevated valuations but totally crazy, insane valuations. That happens, but it is rare.

Now back to this market, and let us bust out some math. The S&P 500 closed Thursday at 2,364.87. Last year, the S&P 500 earned $106.64 per share. That is the index-adjusted number. The issue is that profits last year were held back for a variety of reasons, and we should expect a decent earnings rebound this year and next.

For 2017, Wall Street currently expects the S&P 500 to earn $130.67 per share. For 2018, the expectation is for $148.35 per share. Let me add an important caveat: Wall Street's earnings are notoriously optimistic, especially that far out. It is typical to see estimates gradually pared back as earnings day approaches.

With that in mind, I think the Street's estimates are reasonable, and that is what we are looking for. If the Street's estimate for 2018 is accurate, that means the S&P 500 is currently going for 16 times next year's earnings. To my mind, that is a bit above average, but it is hardly excessive. Let us also remember that earnings estimates could be too pessimistic. The earnings estimates for Q3 and Q4 of this year are already higher than they were at the start of the year. It has been a while since I have seen estimates go up!

So, the more pressing concern for us right now is not excessive prices, but the threat of a recession. Fortunately, that too does not appear to be on the horizon. If anything, growth may be ramping up this year. I am also relieved to see some bullish economic reports recently. Consumer confidence, for example, just touched its highest point since July 2001. Job growth is strong, and interest rates are still low.

We will get the jobs report later this morning, but Wednesday's ADP was very good. I will be more concerned about the threat of a recession when interest rates get higher. The good news is that we are still a long way from that happening.

Let me summarize by encouraging you not be scared out of the market. We will see some ups and downs. After all, that is what markets do. But there is no reason for us to expect any severe troubles for the next several months. Investors should concentrate on a portfolio of high-quality stocks.

Get Ready For Another Fed Rate Hike

A few weeks ago, Janet Yellen testified before Congress on monetary policy. At the time, Wall Street was pretty sure that the Fed was not going to raise interest rates in March. Since then, several events have come together which have convinced traders that a March rate hike is in play. We had Janet Yellen all but admit that she's going to raise rates again next week. The Fed's meeting will be next Tuesday and Wednesday, March 14-15.

We can really trace the events back to the election, when Wall Street was taken by the Trump Trade. Or another name for it is the Reflation Trade. The thinking behind the Reflation Trade was that President Trump would press for a large stimulus plan that would boost the economy, and take a more relaxed approach to higher inflation. As a result, Industrial stocks rallied with Materials and Energy shares. At the opposite end, long-term bonds did poorly.

Six months ago, the five-year Treasury was going for 1.24% more than the five-year TIPs. That means Wall Street has been expecting inflation over the next five years to average 1.24%. Now it is expecting inflation to average 1.90%.

Suddenly, this week, the Reflation Trade backed off. The primary reason is that oil is sinking again.

For the first time this year, West Texas Crude slipped below $50 per barrel. OPEC has tried to cut production, but there is still a glut of oil. In the U.S.A., supplies have risen nine weeks in a row and are currently at an all-time record. The price of oil has fallen seven times in the last eight sessions.

The immediate effect of this is that Energy stocks have slipped over the past several days. In fact, the Energy ETF (XLE) is technically in correction territory, which is defined as a 10% drop from its high. What is interesting is that falling oil has previously been tied to a rising stock market. That is what happened in 2014-15. Now it appears to be a negative.

The stock market gapped up last Wednesday, after President Trump's Congressional address. Since then, it has gradually slipped back. The S&P 500 has now gone 82 days in a row closing within 1.5% of its all-time high. The streak very nearly came to an end on Thursday, but it was saved by an afternoon rally.

Over the last few issues, I have warned you to expect to see a modest pull-back. I still think that is quite possible. I simply want you to be aware of what is happening. Most of all, there is no need to panic. If anything, a pull-back would be a great buying opportunity for disciplined investors.

The drop in in the price of oil might cause the Fed to forego a rate hike next week, but don't count on it. The move in oil is too little, too late. Plus, the Fed has already announced its intentions. If it failed to follow through, its credibility would be shot. But if the Trump Trade continues to unravel, it could put off any further rate hikes for this year.

The big jobs report is later today. I think the Fed will raise rates even if the report is below expectations. More importantly will be the level of wages. The FOMC meets on Tuesday and Wednesday. The policy statement will come out on Wednesday afternoon, and it will be followed by a press conference with Janet Yellen.

Be sure to keep checking the blog for daily updates, and I will have more market analysis for you in the next issue of *CWS Market Review*!

- Eddy

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BW: In the rest of the newsletter, Eddy reviews the earnings announcements of the companies on his Buy List. You can read about them and the entire article by clicking on the following link:

http://www.crossingwallstreet.com/archives/2017/03/cws-market-review-march-10-2017.html

Named by CNN/Money as the best buy-and-hold blogger, Eddy Elfenbein is the editor of Crossing Wall Street. His free Buy List has beaten the S&P 500 for the last six years in a row. This email was sent by Eddy Elfenbein through Crossing Wall Street.

BW: Information on Eddy Elfenbein and Crossing Wall Street follows on the next page.

ABOUT THE AUTHOR

Welcome to Crossing Wall Street

I started this Web site to help individual investors. I have to admit that I *love* the stock market. I think I must be an addict. In my opinion, the stock market is one of the greatest inventions in history. The stock market is simply the most consistently successful way to make money over the long term. Even after the financial crisis, stocks have still beaten every asset category over the long haul—bonds, commodities and real estate.

While the stock market may bounce around from day to day, and even month to month, the long-term trend has always been higher. Over the last 35 years, stocks have gone up 35-fold. And since the end of World War II, the stock market is up an amazing 120,000%. I wish I had been around! That was the beginning of an American financial revolution. Today, we're at the beginning of a *global* financial revolution. That is why I think the next 70 years will be even better.

The key to doing well on Wall Street is actually very simple: Buy and hold shares of outstanding companies. But too many investors never learn this valuable lesson. Or if they do learn it, they learn it the *hard* way. That is where I come in. I want to help investors avoid the mistakes that separate successful investors from those who always find themselves spinning their wheels.

There are lots of pitfalls on Wall Street. From shady companies that are more popular than they are profitable to a mutual fund industry that is more interested in its fees than serving investors. Todayis investors must be careful.

At Crossing Wall Street, I give investors my free and unbiased view of the market. I probably analyze dozens of companies every week. I am always looking over income statements and balance sheets. I've spent several years collecting my list of the best companies to own. This is my current Buy List. I've included a description of each company and its current share price. These are the ones that I make the most effort to follow on the site, but please feel free to ask me my opinion on any stock. I don't receive compensation from any of the stocks I recommend. Also, I don't "short" any of the stocks I criticize. At any time, I may own the companies on my Buy List. All of the information on this site is free and unbiased. I also have a section for Frequently Asked Questions that will help you learn more about Crossing Wall Street.

Please feel free to e-mail me. I enjoy getting feedback from investors. I am happy to give you my opinion on any stock or investing in general. I should warn you that I cannot give out personal portfolio advice, but all other topics are fair game. You can also check out some of my favorite links.

- Eddy Elfenbein

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