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# Earnings Spur New Highs; Abenomics Gets a Boost

## Friday 9:40 a.m., EDT

I have been saying that all this market needs to break to new highs is better earnings, and so far – and it is very early in earnings season – that has happened. Of the 13 S&P 500 issues reporting since Alcoa, all but 2 (Fastenal and Progressive) have beaten estimates. Most notably, the banks, up to now the weakest sector in the market, have exceeded expectations. Many have reduced reserves for bad loans in the energy sector as a result of the stabilization of oil prices. S&P reports that if their benchmark index rises today, it will be the first full week of all-time highs in over 18 years.

The data continue to support a modest acceleration in economic growth. Today's retail sales numbers beat expectations, and will probably raise Q2 growth estimates to about 2.5%. Early Q3 estimates are for 2%, and if this number is realized, the first nine months of this year will still fall short of 2% growth. The CPI inflation numbers today came in very near expectations although the PPI yesterday were a little hotter than anticipated. None of these numbers will sound a warning for the Fed. Nonetheless, the fear of deflation, so prevalent earlier this year, have certainly faded and eliminates a downside risk for the central bank.

On the monetary front, the Bank of England surprised many by not lowering their policy rate. The BOE said the financial markets had largely stabilized and the lower pound added some inflationary pressures to the UK economy. Internationally, the more important development is Abe's resounding election win in last weekend's elections and the growing anticipation that another round of QE is in the works. The yen is weakening in anticipation and the Nikkei is poised for another move upward. Despite the growing doubts by experts that Abenomics is working, the Japanese people still support his policies.

Treasuries have rebounded as better economic news reduces risk-off sentiment. There is no question that Treasuries (and sovereign debt in general) have been the go-to asset when bad news hits. This gives these bonds a significant negative beta and increases their role as "insurance" assets. The January 2017 Fed fund futures (best predictor of year-end Fed funds rate ) has increased 16 bps from 34 bp after the Brexit vote to near 50 bps today. Although that indicates a 50% chance of one increase this year based on raw data, on risk-adjusted data I estimate the markets are now expecting (about 2 to 1 odds) a single increase, most likely at the December meeting following the election.

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