Weekly Commentary **July 24, 2015**

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Earnings Mixed as Commodities Resume Price Declines

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Last week I wrote, "I believe there would have to be unexpected weak data (with respect to both inflation and real output) over the next two months to cause the Fed to defer [increasing rates in September]." Although my bet is still on September as the Fed's liftoff month, the rapid decline in oil and other commodity prices makes that certainty of that date far less than it was a few weeks ago. Today WTI oil traded below $48 and both the Journal of Commerce Index of Industrial Commodities and the CRB Commodity Index hit multi-year lows. These declines have followed a sharp break in precious metal prices, with both gold and silver hitting 5 and 6-year lows.

To be sure, the Fed looks at "core" inflation and has often dismissed fluctuations in commodity prices as "temporary." Nevertheless the persistent decline in these commodities cannot be dismissed by the Fed since they eventually impact core prices. It is still almost two month away from the September meeting. but the market will be looking closely at the statement from next week's FOMC meeting to see if the Fed highlights the commodity price decline as important enough to delay the path of rate normalization.

We are in thick of earnings season and the news is decidedly mixed. Although a very high percentage of firms are beating the "consensus," many are missing their revenue targets and guiding lower in coming quarters. Some tech firms surprised on the upside (Google and Amazon), while others missed expectations (Apple and Microsoft). Apple shareholders are used to beating expectations by a wide margin and when the firm reported lighter than expected I-phone sales, fears began to mount that China could be a drag on sales for a quite a while and reminds investors that the firm must continue to innovate to maintain revenues (I-pad sales are still in a strong downtrend trend). In contrast Microsoft is living primarily off the annuity of its original Windows and Office platforms. Its painful $7.5 billion write-off of Nokia reminds us on how far this company has gone astray in recent years. That write-off lowers S&P 500 GAAP earnings this year by almost $1 (although it will not impact operating earnings). In fact, over the past two weeks, while S&P 2015 operating earnings estimates have slipped only ten cents, GAAP (as reported) have fallen $3 this year's GAAP estimate is now only a few pennies above the $102.31 realized in 2014 (operating earnings are still forecast $2.36 ahead of last year). It is very hard for the stock market to make any progress until the impact of the higher dollar and lower energy price has run its course.