Seeking Alpha

Report from Europe: Markets Fret Over the Dreaded W

by: The Mole

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U.S. stocks extended a global drop as concern grew that the rally has outpaced the prospects for economic growth. The yen and the dollar strengthened, oil tumbled and yields on Treasury three-month bills turned negative for the first time since financial markets froze last year.

There was some bearish chat from two of the market's heavy hitters. Bill Gross, who runs the world's biggest bond fund at Pacific Investment Management Co., said the "systemic risk" of new asset bubbles is rising as the Federal Reserve keeps interest rates at record lows while queen of the banking analysts, Meredith Whitney, said Thursday that bank stocks are "grossly overvalued."

So, after largely ignoring a plethora of disappointing data earlier in the week, markets look decidedly weaker overnight (even though the data was perhaps ironically somewhat more encouraging). European bourses were weaker from the open and lost further ground after US markets opened. Some negative broker commentary from Bank of America / Merrill Lynch on the tech sector didn't help matters.

But I suspect that the accumulation of disappointing construction sector reports of late, culminating in Thursday's US housing starts and permits data, means that investors are reluctant to drive markets to new highs this side of Christmas. According to the MBA, 14.41% of mortgages are now at least one payment overdue or already in the foreclosure process. Two-Year Treasury Bond yields have hit 2009 lows today, a sure sign that traders think the odds on that overhyped V-shaped recovery becoming a W have shortened considerably.

Friday, after a quiet start, market talk of a Ukranian default has sent the stocks firmly into the red. ECB commander in chief JC Trichet also made some comments to the effect that the sluice gates in Frankfurt will eventually have to shut and the banks weaned off the methadone of more or less unlimited liquidity. US house builder DR Horton has come in with a big miss and is off 7% while retailer Gap is trading up on a 25% increase in profits while department store chain Dillard's is up 4% after a broker upgrade from Deutsche to a buy.

Today's Market Moving Stories

- Overnight, Asian stocks fell for a fourth day, the longest losing streak since July, and the South Korean won led regional currency declines after companies from Dell (DELL) (off 6.4% pre-market) to Sony (SNE) (down 2,.5%) posted results that disappointed investors. The won lost 0.3% to 1,160.2 after reaching a two-week low. Australia's S&P/ASX 200 Index slid 1.3 percent after the initial share sale of Rio Tinto Group's (RTP) coal unit raised less than expected.
- U.K. house prices will probably fall next year, and it may take until 2014 to return to the levels at the 2007 peak of the country's biggest housing boom, according to a Bloomberg survey. Nine of 14 economists and real estate brokers surveyed said they foresee a decline in 2010 after a surprise rebound this year. They predict an average drop of about 1.6%, with estimates ranging from a loss of 10% to a rise of the same magnitude. British Land, Hammerson, Redrow and Taylor Wimpey are all weaker today on the back of this.
- A recovery in U.S. housing will have to wait at least until next year. The outlook for the home market dimmed this week as residential construction and mortgage applications fell and loan delinquencies reached a record. New home sales may begin to pick up by the start of the so-called spring selling season,

said Toll Brothers Inc. (TOL), the largest U.S. luxury homebuilder. Existing house sales may take longer. Residential construction and property sales led the way out of the previous seven recessions going back to 1960, said David Berson, chief economist of PMI Group, the mortgage insurer in Walnut Creek, California.

Central Bankers and Barbie

It has been quite a remarkable fortnight for some of the most noted former hawks amongst the central banking community. The latest Pauline conversion comes from Dallas Fed President Richard W. Fisher (a self-confessed inflation hawk). But yesterday he opined that “Inflation is obviously not the issue,” adding that “there is so much excess capacity out there.”

“A depreciating dollar – a gradually depreciating dollar – doesn’t necessarily add an enormous inflation impulse.” Fisher called on the Barbie doll for supporting evidence. “10% of the value of a Barbie doll priced at retail comes from China. The rest of it is all added on through the distribution system, merchandising and margin. So you would have to have an enormous move in that currency to inflate the price of Barbie dolls.” Hence, “it is not necessarily true that a depreciating dollar leads to significant inflation impulses."

As for the economy, firms are neither hiring nor investing and are unlikely to do so “until they see the whites of the eyes of recovery.” Fisher cited the October jump in the unemployment rate and said the real rate “is worse than the 10.2%, we all know that.”

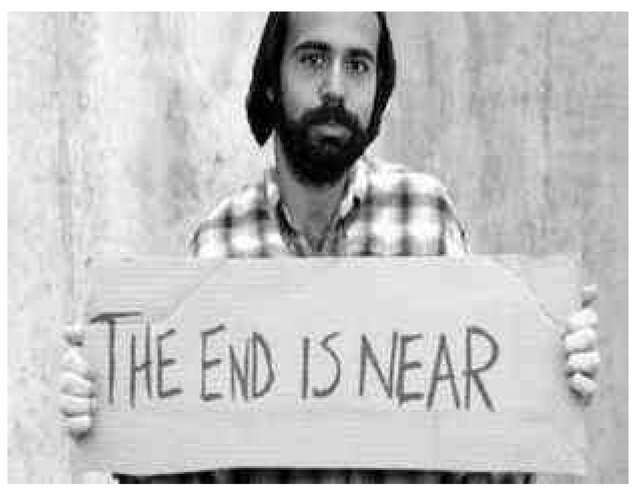
“A lot of people have just given up looking for work,” he said. “Unemployment is too high, and it will be a long time in coming down.”

A priori, the title of Fisher’s speech was not market moving, “Addressing ‘Too Big to Fail’,” and effectively the speech holds little immediate interest for me. Fisher instead made a splash with a simultaneously released MNI newswire interview, followed by a series of off the cuff remarks at the Cato Institute. Fisher sees "enormous excess capacity" and “significant deflationary forces worldwide,” according to the off the cuff remarks on the newswires. At the same time, Fed policies carry “great and unprecedented risk”, while it is `fortunate’ that US debt is being financed at low rates, suggest Fisher. Those are risks that the Fed is still very much ready to run. Bravo!

Some Good News For Irish Financials

European Union regulators have approved Ireland’s revised plans to guarantee bank deposits and debt to stabilize its financial industry. “The new guarantee scheme will give credit institutions in Ireland access to medium-term state-guaranteed financing and provide Ireland with an effective means of restoring confidence in the financial markets, while at the same time limiting distortions of competition,” EU Competition Commissioner Neelie Kroes said in an e-mailed statement today. The new guarantee excludes subordinated debt and extends to instruments with a maturity of as much as five years, the EU said.

Equity News



- Dell Inc., the world’s third-largest maker of personal computers, reported earnings that missed analysts’ estimates after it lost market share and higher PC component costs cut into profit. Third-quarter net income fell to $337 million, or 17 cents a share, from $727 million, or 37 cents, a year earlier, Dell said today in a statement. Sales declined 15% to $12.9 billion. Analysts surveyed by Bloomberg predicted profit of 27 cents and sales of $13.1 billion. Chief Executive Officer Michael Dell is focused on boosting profit over winning PC market share and is counting on a “major upgrade cycle” next year to spur demand. Dell lost the No. 2 spot in the back-to-school shopping period, though its shipment decline wasn’t as big as in the previous quarter. The shares have gained 55% this year.
- General Electric Co. (GE) and Vivendi SA (VIVEF.PK) are between $1 billion and $2 billion apart in their valuation of Vivendi’s stake in NBC Universal, possibly hurting chances of a rapid resolution to a stand-off

that is holding up Comcast Corp.'s (CMCSA) planned bid for a majority holding in NBC, the Financial Times reported, citing people familiar with the negotiations.

- Infineon Technologies AG (IFX), Europe's second-largest maker of semiconductors, will consider acquisitions as large as 1 billion euro next year, Platow Brief reported, citing comments by Chief Financial Officer Marco Schroeter. Infineon may sell shares and bonds to finance the acquisitions and is looking at companies in Europe and the U.S., the newsletter cited Schroeter as saying.
- Brandon Adams, who teaches behavioral finance at Harvard University's Department of Economics, says some of the best candidates for Wall Street trading jobs are the professional card players at FullTiltPoker.com and similar Web sites. "They've essentially been the survivors in the system, a very difficult system where 95% of people lose money," the 30-year-old Adams, who plays at the site, said in a telephone interview. "An increasing number of hedge funds and brokerages are scrutinizing professional poker to find talent and analytical tools, according to financial recruiters including Options Group, a New York-based executive-search company. Susquehanna International Group LLP, the Bala Cynwyd, Pennsylvania-based options and equity trading company, uses poker to teach strategic thinking.

Looking Ahead

Next week's Thanksgiving holiday in the US is the defining event in terms of influences on the price action. Thursday's national holiday – which often forms the basis of a very long weekend – is likely to be preceded by a gradual depletion in liquidity as investors square-up and take to the sidelines. In fact, with US stocks ceding ground yesterday and with Dow Jones futures prices pointing to a weak open today, that process may have already begun. With year-end on the horizon, investors may in any case be keen to lock-in profits from a seven-month-old bull run and will certainly not be willing to miss an opportunity that was denied them in the aftermath of last October's crisis. As such, perhaps the bigger uncertainty is just how investors will react once they return to their desks after the Thanksgiving 'weekend.'

Certainly, a period of consolidation is long overdue in many emerging markets, where there are numerous examples of year-to-date gains in excess of 100% (the Hang Seng, Merval for example). Hong Kong chief executive Donald Tsang said this week that " … with zero, or near zero interest rate policies, we see a repeat of rapid carry trades and leveraged capital flows that are once again creating asset bubbles in the emerging markets". However, unfortunately for Mr. Tsang and his counterparts, it has been made abundantly clear this week, by a succession of Fed officials, that low interest rates in the US will be in place for some time to come. Just how long any period of consolidation would last under these circumstances remains to be seen.

And Finally…

- Whoops: Stocks Now 20%+ Overvalued
- A staggering tale of the kind of incompetence and unintended consequences that happen when the government gets involved in the Free market: "FHA Loans Help Three Broke Dudes Buy A Million-Dollar Building In San Francisco"
- Football, French style…the hand of Gaul.

Road Trains: Genius Or Guaranteed Pile-Up?

Disclosure: *No positions*