

Weekly commentary by Professor Jeremy J. Siegel

## Poor Labor Report Mostly Discounted; Low Yields Limit Decline

9:00 a.m. EDT, 10/2/2009, Philadelphia PA



The market had mostly prepared for worse-than-expected data after the jobless claims and the ISM manufacturing data earlier this week. One detail that does take the sting out of this labor market report is that government payrolls were down 53k (perhaps because of problems with seasonal adjustment to the school employment) so that private jobs were down only 210k. Manufacturing payrolls declined as expected, and the workweek was down 0.1 hours. Hourly earnings up only 0.1%, less than expected.

Stocks are undergoing the first meaningful correction that could take the averages down another 5%, at most. I had thought we would have a bounce upward before the correction, but the data for September have been disappointing. The flip side of this softness is that yields on long treasuries have come down considerably, with the 30-year falling well below 4% and the ten year down to 3.12%, the lowest since May. These low yields will limit the downside of this correction. There is too much money on the sidelines and too many investors who have missed the rally and are willing to go in on a correction. I was surprised to see oil jump up yesterday, one of the few times that oil and stocks have moved in opposite directions for many months, but oil and commodities are down so far today. The dollar rallied on the labor market report contrary to the economic expectation that it should decline. The reason for this is that the dollar is still seen as a haven in a slow-growth world, and as risk of a slowdown rises, the dollar rallies.

Bill Gross is getting much play for his "new normal," view of the economy, which predicts slow economic growth. He has said that returns on stocks are geared to nominal GDP growth which he believes will grow at 3% to 4% over the next few years. It is true that the long run returns on equities are geared to inflation and real growth, but what he doesn't mention is that the discount rate by which corporate earnings are discounted are also geared to economic growth, and the slower the growth, the lower the discount rate. This means that the equilibrium P-E ratio in a slow growth economy could be as high as 20 or more. At peak earnings, S&P 500 reached over \$90 per share. Even if one believes that \$10 of that level was from the financial sector that won't come back, that still leaves \$80. A fifteen P-E is an index level of 1200 and a 20 P-E is 1600. The index will open today at 1020.

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