Weekly Commentary by Professor Jeremy J. Siegel

Week of Terrible Data; Stocks, Commodities Hit

9:30 a.m. EDT, 6/3/2011, Philadelphia PA

Rarely have I seen data come in so much below expectations as we experienced this week, from the ISM numbers to today's payroll rising by a disappointing 54k, well below the even sharply lowered consensus (plus downward revisions of 39k to the previous two months). I believe that a major source of the economic slowdown was the sharp rise in oil and gasoline prices that is just beginning to moderate now. Travel and leisure lost 6,000 jobs after gaining 32,000 the month before and 46,000 the month before that. Retail employment was also hit, as consumer confidence waned with rising gasoline prices.

There were technical factors leading to the sharp downward shift in payrolls this month, including going from a 5-week to a 4-week intervals between payrolls and some say an average of April and May data is a better indicator. The loss of government jobs is accelerating, losing 29k this month compared to losses of 19k and 25k in the previous two months. Ultimately I think this is good for the economy, as these jobs, mostly in the state and local sector, are not generally as productive as private job growth, but in the short run these losses do add to the softness in aggregate demand.

Bond yields, as expected plummeted on the news, the ten-year falling below 3% once again. One favorable impact is that oil prices have also sunk, with Brent now trading at $113.60. Inflationary expectations, measured by the ten-year nominal and TIPS yield, have now fallen to 2.25% and are the lowest since January.

Stock futures have also sold off, but I believe the decline in the stock market will be cushioned by the fall in bond yields and commodity prices. If oil prices can stay down, consumer confidence will return and almost all forecasters I follow still have the economy moving to a trajectory of 200k to 250k private jobs per month in the second half of 2011. If Congress gets to some agreement on the debt ceiling, another source of uncertainty will be removed from the market. Stock prices will discount extremely negative events such as a European collapse or a U.S. debt default, even if they have a tiny probability of happening.

If growth continues to slow Congress should be thinking of more stimulus, such as cutting the payroll tax on new workers added by the private sector. And certainly the Fed will keep the language of "extended period" in their directive longer than they had hoped they would have to. But as I mentioned last week, further Fed stimulus, such as QE3, must wait to see if the weakening conditions worsen.
