Tom McIntyre's
Weekly Commentary & Outlook

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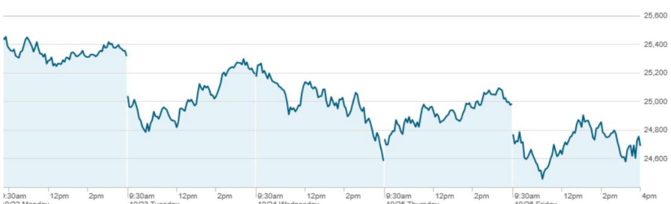
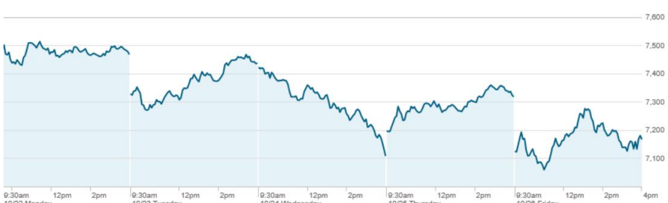
This is Tom McIntyre with another client update as of Monday October 29, 2018.

October cannot end fast enough for investors. Once again, this year, the month has been difficult even as our economy is growing faster than in many years. Pretty good earnings reports are being obscured by some high-profile disappointments among some of the high flyers. This, combined with concerns over rising interest rates, has trumped the overall good news.



Dow 5-day

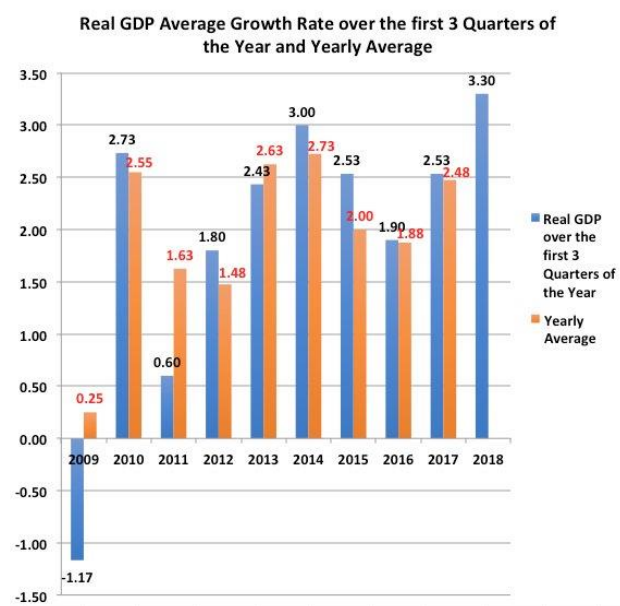


NASDAQ 5-day

As the charts above show the ***Dow Jones Industrial Average*** fell 3% last week while the ***NASDAQ Composite*** dropped nearly 4%. Both indices are now barely positive for the year.

Markets & Economy

The GDP report for the 3rd quarter came in at a 3.5% annual rate. In the chart below, one can see that through nine months this is the best start to the year for the economy since before the financial crisis of 2008. Even better news is that the Fedôs measure of inflation also turned downwards to well below 2%. Once again, the Fed has continuously forecast that stronger growth and low unemployment (reported) would bring about a strong upward swing in inflation. They have used this to totally justify their 7 rate hikes since Donald Trump was elected. Even worse, they seem to think that whatever trend is in place can just continue. Hence, they continue to warn of the many future hikes they have planned.



There are just a few problems with this though. The growth rate in the 4th quarter will be lower, and the bond market knows this. That is precisely why bond prices rose last week despite all the nonsense of the need for higher interest rates. What the Fed should really say if they were to be true to the American people is that they want to micro manage the US economy back down to below 2% growth. Furthermore, they want to put a dent in stock prices as they fear that higher asset prices will cause the same non-problem as people going to work.

These notions are typical of the DC Beltway economic thinking. It is perverse however when one looks at the real world where commodity prices are falling (copper down 17% since early summer) and where the interest sensitive sectors are already showing signs of distress. Housing sales, whether new or used, are simply disappointing and you can thank the Federal Reserve Board. Even the financial sector is struggling, as borrowings are declining, and deposits are leaving their balance sheets to seek higher returns which the Fed has engineered for them.

I find it quite ironic that President Trump is having success in revitalizing the US economy and continues looking for ways to keep the ball rolling. At the same time unelected eggheads are seeking to slow down the economy and perhaps upset investor and consumer confidence by their actions, which are based upon an economy that existed in 1970. Back then the US economy was largely immune to economic issues overseas, but it is not so today. The rising US dollar resulting from the rising US interest rate environment is wreaking havoc in the emerging markets. Even in countries such as Italy, there is trouble brewing as the EU attempts to control sovereign nations through bureaucratic control. It won't work but it could get ugly first.

In any event with other countries depreciating their currencies and enjoying zero percent interest rates there is just so much room for the Fed to continue with its perilous policy. Remember, virtually none of them have ever had real jobs or understand /respect the message of the markets. This has always been the problem for the Fed which was raising interest rates right into the financial abyss of 2008. I still remember being assured many times by the then Chairman that the sub-prime loan issue would never amount to a threat to the system. I learned right there and then, these people are clueless.

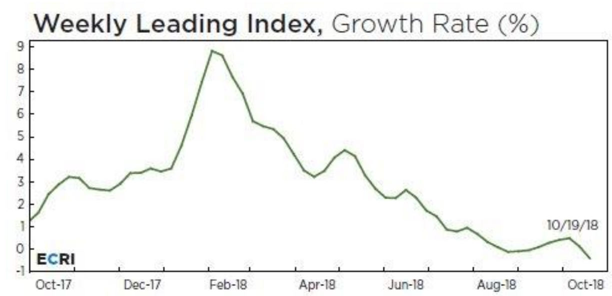
The big picture though, is that many of our names have done spectacularly well in this dismal environment. See our comments below on Microsoft, Boeing and McDonalds. Clearly, these businesses are doing well and positioned better than most of their competitors. Thus, while the day-to-day moves in prices are interesting, their longer-term outlooks should provide all of us with much comfort while the Fed continues its game of chicken with the markets.

What to Expect This Week

Another employment report is due out on Friday. This will be the last one of course before the mid-term elections, so perhaps a few political implications will follow. Basically, given the record low weekly claims I suspect it will be another great report in terms of the unemployment rate but perhaps not so much in terms of job creation and wage gains. This is another area where the Fed continues to err. They think unemployment being low (regardless of the flawed calculation) simply must bring about higher wages and inflation. I have heard this ever since the unemployment rate was in double digits. The Fed has been wrong for the entire period of recovery since 2009, coming up on 10 years. Of course, the Beltway types say not to criticize them, I say they should be held accountable.

Additionally, we will be dealing with more earnings reports as well as the now daily crisis in the world which seems to affect investor sentiment at least in the short run.

Finally, the weekly look at the ECRI's weekly leading economic indicators does not jive with the Fed's view of a strong economy as far as one can see. Frankly, it looks to me like Q4 will be down from Q3 which was down from Q2. Still good but will it be enough to change Fed forecasts. That would send the market into orbit heading into the end of the year.



MSFT one-year

MCD one-year

It was another stellar quarter for **MICROSOFT.** The worldôs largest software maker topped both revenue and earnings estimates with their fiscal first-quarter 2019 results. Earnings per share came in at $1.14, easily outpacing Wall Streetôs estimates of 96 cents, and 36 PERCENT BETTER THAN THE YEAR-AGO QUARTER. Revenues rose 19 percent year over year to $29.08 billion, which topped the Streetôs call of $27.73 billion.

Cloud Computing is once again a shining star for **MSFT**. Sales of its AZURE program grew 76 percent in the fiscal first-quarter, reflecting the Companyôs success in shifting its business toward internet-based computing. Meanwhile, sales of OFFICE 365 were up 36 percent during the quarter, while sales of its DYNAMIC program gained 51 percent. **MICROSOFT's** 1st quarter represents the strongest topline growth the Company has shown in more than 10 years. Shares of **MSFT** jumped more than 4 percent after the earnings announcement. The common stock is 27 percent higher over the past year and has moved back up as the second most valuable company in the US.

It was also another fantastic quarter for **MCDONALD'S.** The DJIA component reported numbers which beat analystsô expectations for earnings and revenue. The fast food giant earned $2.10 per share on revenue of $5.37 billion, topping forecasts for EPS of $2 and revenue of $5.31 billion. These numbers also topped the metrics posted in the previous quarter. A key to **MCD's** success was the US comparable-store sales, which rose 2.4 percent during the quarter. Those sales were driven by growth in product mix shifts and slight menu price increases.

Customers outside of America love to eat at the Golden Arches too. Global sales rose 4.2 percent during the quarter, far better than an expected growth rate of 3.7 percent. This makes it 13 consecutive quarters of positive comparable sales globally. CEO Steve Easterbrook says the Company has made substantial progress in modernizing its stores and is in fact ahead of schedule for US based restaurants. Currently, **MCDONALD's** feeds 68 million people around the globe every day, sells an average of 75 BURGERS PER SECOND, and over 3 TONS OF FRENCH FRIES every minute. Shares of **MCD** are up 7 percent over the past six months.

BA one-year

While MCDONALDSôs is crushing the competition at the breakfast, lunch and dinner table, **BOEING** remains the dominant player in the sky. Shares of the worldôs largest plane maker took off last Wednesday after reporting stronger-than-expected quarterly profits and cash flow. Thanks to soaring demand from airlines and solid defense sales and services, the company beat Wall Street numbers, and RAISED ITS 2018 FULL YEAR SALES AND PROFIT ESTIMATES. Core earnings came in 11 cents above analystsô average forecasts at $3.58 per share. **BA** is raising its full-year profit forecast nearly a dollar higher, to between $14.90-$15.10 a share, and revenue to a range of $98 billion to $100 billion, an increase of about 1 billion.

One great example of **BOEING’s** success is its relationship with CHINESE AIRLINES. The Chinese have contracted to buy 7,690 new planes worth $1.2 trillion over the next two decades to keep pace with booming consumer and business demand. Currently, **BOEING** has delivered 568 aircraft to customers in the first nine months of 2018, up from 554 deliveries at the end of September a year ago. The goal for this year is delivery of between 810-815 planes, which would be an all-time record. This pace of production is substantially ahead of **BOEING’**s rival, AIRBUS. Shares of **BA** have gained 40 percent for shareholders over the past 12 months.