

A bump in fuel costs and a slump in housing can't halt market climb

But analysts also see shaky days on horizon

By Robert Gavin, Globe Staff | July 15, 2007

Home foreclosures soaring? Oil nearing \$74 a barrel? Gasoline prices topping \$3 a gallon? So what.

Wall Street again shrugged off some pesky consumer costs and finished a strong week as the Dow Jones industrial average soared more than 300 points in two days and moved within striking distance of 14,000. The blue chip index closed Friday at a record 13,907.25.

The late-week rally, which began Thursday with the biggest one-day gain in nearly four years, is the latest sign that a strong global economy and improving US conditions are trumping concerns about the slumping housing market and rising energy costs.

The Dow has gained more than 600 points since early June, and more than 1,400, or 12 percent, for the year. The broader Standard & Poor's 500 Index is up 9.5 percent for the year.

Analysts said a combination of a solid global expansion, moderate US inflation, and low interest rates means stocks are poised to move higher. However, bad news on housing and energy could still spark deep sell-offs, and analysts expect the market to swing up and down through the rest of the year.

"There are still some rough days a head," said Jim Swanson, chief investment strategist at MFS Investment Management in Boston.

But if anything, this bull market has shown it can weather rough days and come back roaring. It rebounded from a 416-point plunge in February and, more recently, a nearly 200-point drop June 7.

"For all the gyrations, the economy is on a moderate growth track," said Stuart Hoffman, chief economist at PNC Financial in Pittsburgh. "I expect the market is heading higher, maybe not another 10 percent, but continuing its two steps forward, one step back" pattern.

In addition to strong global growth, the bull market has been sustained by a resilient US economy. After expanding at an anemic 0.7 percent annual rate in the first quarter, the US economy is expected to grow in the second quarter at an annual rate well above 3 percent, according to economists.

Employers have been adding an average of 145,000 jobs a month this year, and the jobless rate has slipped to 4.5 percent. Wages are rising, too, supporting consumer spending, which accounts for more than two-thirds of economic activity.

Meanwhile, inflation remains under control, and interest rates, while higher than a few years ago, remain relatively low.

"The market is absorbing the fact that the economy is rebounding," said Nariman Behravesh, chief economist at Global Insight, a Waltham forecasting firm.

This week's rally was sparked Thursday when some of the nation's biggest retailers, including Wal-Mart Stores Inc., reported better-than-expected sales in June. Investors viewed those results as a sign consumer spending is solid, despite gasoline prices of about \$3 a gallon and falling home values.

On Friday, investors were cheered by a Commerce Department report that businesses are rebuilding inventories, which typically boosts manufacturing. The University of Michigan also reported that consumer sentiment improved significantly in early July, viewed as another support for consumer spending.

"The market has come to the realization that the consumer is holding up," said Richard Hoyt, market strategist at KDV Wealth Management in Minneapolis. "There are good economic fundamentals, the foremost of which is job growth."

Strong global growth, meanwhile, is fueling corporate profits and subsequently stock prices since the biggest US companies have extensive international operations. For example, EMC Corp. of Hopkinton and Genzyme Corp. of Cambridge each generate more than 40 percent of their revenues internationally.

China's economy is growing at double-digit rates, while Europe and Japan's economies have picked up steam in recent years. Japan's economy, for example, is projected to grow 2.8 percent this year, compared to 2.2 percent in 2006, according to Global Insight. This growth has boosted demand for US products. Exports hit a record \$132 billion in May, the Commerce Department reported.

As a result, analysts are expecting US corporations this month to report another quarter of solid profits.

Profits of corporations included in Standard & Poor's 500 Index grew nearly 8 percent in the first quarter, according to Thomson-First Call, a financial research firm. That followed 14 consecutive quarters of double-digit profit growth.

These consistently strong profits have left corporations awash with cash, which in turn is also helping to boost stock prices. Many corporations have used the money to buy back stock, reducing the number of shares outstanding and increasing values. Some have used the money to acquire other firms, which also can drive up stock prices.

Also helping to fuel mergers and acquisitions are global interest rates, which, while rising, remain at attractive levels.

"All that money has to find a home," said Jim Weiss, president of Weiss Capital Management of Concord.

And one place is the stock market, Weiss said. Like other analysts, Weiss said he expects the market to swing up and down as it grapples with the housing downturn but ultimately to move higher.

"As long as interest rates don't spike on a long-term basis," he said, "the market has some more to go."