

# MORNING NEWS CALL

REUTERS

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## TOP NEWS

### • Euro zone trade surplus widens in June, inflation flat in July

The euro zone's trade surplus widened in June from a year earlier and from the previous month as imports continued to fall, the EU's statistics office Eurostat said.

### • Dell's quarterly profit plummets amid buyout brawl

Dell Inc, the PC maker embroiled in a takeover battle between its founding CEO and activist investor Carl Icahn, on Thursday reported a 72 percent slide in quarterly earnings as PC sales extended their downward spiral.

### • Applied Materials sees foundry customers delaying orders

Chip gear maker Applied Materials said it expects foundry customers to hold back spending in the current quarter as they switch to making smaller chips.

### • Maersk ups shipping forecast as container profit jumps

Danish shipping and oil group A.P. Moller-Maersk reported a smaller-than-expected drop in second-quarter net profit aided by a sharp improvement in its container shipping unit and costs.

## BEFORE THE BELL

**U.S. stock index futures** pointed to a higher open on the last trading day of the week, but **global markets** were on course for their biggest weekly fall in about two months as encouraging economic data reinforced views that the Federal Reserve's stimulus program might end soon. The **dollar** rose against a basket of currencies, drawing support from benchmark **U.S. treasury yields** that jumped to two-year highs in the previous session. Housing starts, building permits, labor costs, productivity and U/Mich sentiment data are on the economic calendar. **European shares** traded mixed, while **Asian markets** closed negative. **Brent crude oil** steadied above \$109 per barrel, consolidating after a week of strong gains. **Gold** inched higher and the precious metal headed for its biggest weekly gain in a month.

## REUTERS INSIDER

### World At Risk: Germany votes, Merkel wins - but with whom?

Merkel is set to win September's election, though she will need a coalition partner. But little will change in policy towards Europe, says Alastair Newton, Senior Political Analyst at Nomura. [To watch more, click here](#)

## DOW 30 HITS & MISSES

(A quick glance at company results showing whether they beat, met or missed analysts' consensus estimates, according to Thomson Reuters I/B/E/S)

• **Wal-Mart Stores Inc** (WMT). Q2 EPS: actual \$1.24, expected \$1.25; Revenue: actual \$116.9 bln, expected \$118.5 bln

## STOCKS TO WATCH

### Moves

• **PNC Financial Services Group Inc** (PNC). The company on Thursday appointed Andrew Feldstein, founder of hedge fund BlueMountain Capital Management, to its board of directors. Before founding BlueMountain, Feldstein was head of structured credit at **JPMorgan Chase & Co** (JPM), where William Demchak, who is now PNC's CEO, also worked.

## INSIGHT

### COLUMN-Long bull market in Fed faith faces taper

For the first time in more than three decades we may be entering a period of declining faith in the Federal Reserve. If the Fed does begin to taper in coming months, slowing its bond purchases as many expect, it will mark a tacit acknowledgment of the limits of the power of monetary policy. By extension, it would also mark a decrease in the power or willingness of the Fed to control the prices of financial assets.

This realization - that the Fed can't always play Santa Claus and FOMC day isn't a sort of secular Christmas - will hit investors hard.

On the evidence, this realization is already dawning.

Gold jumped by 2.37 percent on Thursday, while the dollar fell and government bond interest rates continued to march higher. Ten-year Treasury yields touched 2.76 percent for the first time since July of 2011. At the same time the S&P 500 index fell by 1.4 percent.

Conventional wisdom on Thursday was that bond yields were rising and stocks falling because new economic data made a September taper more likely. Jobless claims last week did fall to close to a six-year low, while consumer prices rose by a small but meaningful amount in July. That's significant, especially the inflation, as the low and falling inflation we've had seemed to call for more stimulus rather than less.

"Are we at the low water mark for inflation? Maybe, and if the Fed even suspects this is the case, they will be even more eager to end asset purchases and normalize policy," Tim Duy, an economist at the University of Oregon and noted Fed watcher wrote in his blog.

"Bottom Line: The realization continues to grow that whether it is September or October or December, the end of asset purchases is now in sight."

Now if the Fed tapers because it has succeeded, then the logic holds that a taper is bad for financial assets but the central bank retains its ability to use policy to drive prices in the direction it wishes to affect the economy. That is a bedrock belief for many investors, allowing them to sleep well at night secure in the notion, however false, that the financial universe is run by a benevolent



## Results

- **Applied Materials (AMAT).** The chip gear maker said it expects foundry customers to hold back spending in the current quarter as they switch to making smaller chips. The company forecast fourth-quarter adjusted earnings of 16-20 cents per share. Analysts on average were expecting earnings of 21 cents per share on revenue of \$2.14 billion. Net income fell to \$168 million, or 14 cents per share, in the third quarter from \$218 million, or 17 cents per share, a year earlier. Excluding items, it earned 18 cents per share.
- **Dell Inc (DELL).** The PC maker embroiled in a takeover battle between its founding CEO and activist investor Carl Icahn, on Thursday reported a 72 percent slide in quarterly earnings as PC sales extended their downward spiral. For its fiscal second quarter, it reported sales of \$14.5 billion, flat from a year earlier and surpassing the \$14.2 billion analysts on average had expected. Net income fell sharply to \$204 million or 12 cents a share, compared to \$732 million or 42 cents a share in the year-earlier period. Meanwhile, Carl Icahn will ask a Delaware court to fast-track his lawsuit against Dell, a key thrust in his months-long effort to derail CEO Michael Dell's controversial \$24.8 billion offer to buy and take private the company.
- **Nordstrom Inc (JWN).** The luxury retailer on Thursday reported lower than expected revenue in its second fiscal quarter as comparable sales at its department stores slipped, prompting it to lower its full-year sales and profit forecast. Comparable sales in the quarter ending Aug. 3 rose 4.4 percent from the year-ago period, below the 6.8 percent increase analysts were expecting. Overall sales rose 6.4 percent to \$3.1 billion. It now expects full-year earnings per share of \$3.60 to \$3.70 per share, down from \$3.65 to \$3.80 per share. Net income for the fiscal second quarter rose to \$184 million, or 93 cents a share, from \$156 million, or 75 cents per share a year earlier.

## In Other News

- **Boeing Co (BA).** The company has traced the incorrectly assembled engine fire extinguishers on 787 Dreamliners to the manufacturing of bottles at a supplier's facility while saying there were no risks to flight safety, WSJ reported. The problem was first discovered during pre-flight maintenance of a jet at Tokyo airport. Meanwhile, Canada on Thursday ordered airlines to inspect emergency beacons on a broad list of aircraft for possible wiring problems that could lead to a fire. The order from Transport Canada comes after a fire broke out on July 12 at London's Heathrow airport aboard a parked Boeing owned by Ethiopian Airlines.
- **BHP Billiton (BHP).** The company said U.S. authorities have laid out grounds for possible enforcement action against the top global miner for corrupt practices, stepping up a four-year probe linked partly to its 2008 Olympics sponsorship. It has been under investigation by the Securities and Exchange Commission and the Department of Justice since 2009, mainly over exploration activities that had been terminated and its hospitality at the Beijing Olympic Games.
- **Deutsche Bank (DB), Goldman Sachs (GS) and Morgan Stanley (MS).** The banks have held talks with China's Huarong Asset Management Corp to invest in its \$1.5 billion stake sale ahead of the company's expected initial public offering next year, FT reported. Huarong plans to raise up to \$2 billion by selling a stake of 15-20 percent, Reuters reported in June. The FT, citing people close to the Huarong process, said in its report that the company would pursue a Hong Kong listing.
- **International Business Machines (IBM), Oracle Corp (ORCL) and EMC Corp (EMC).** China's Ministry of Public Security and a cabinet-level research centre are preparing to probe the companies over security issues, the official Shanghai Securities News said. The report follows revelations by former U.S. spy agency contractor Edward Snowden of widespread surveillance by the National Security Agency and his assertion that the agency hacked into critical network infrastructure at universities in China and in Hong Kong.

power which tends to err on the side of asset owners.

## A NEW WORLD

You can hardly blame them for believing that, indeed the last 30 years have conditioned investors so that they do.

Things, however, are a bit more complicated. While retail sales in aggregate have been fine, if not compelling, recent earnings from Wal-Mart and Macy's appear to point to a U.S. consumer taking the month of July off. At the same time, industrial production is going sideways, and the Philadelphia Fed index of general business activity in the mid-Atlantic region more than halved in August from July, to just a 9.3 reading. New orders halved and shipments actually contracted.

All of this points to a Fed which is thinking longingly about taper despite a signal lack of success of its extraordinary monetary policy. And while the central bank stresses that a tapering isn't a tightening, higher interest rates make that harder and harder to swallow.

Remember, a tapering may occasion the first significant market reversal in many years brought on by the Fed wittingly, as opposed to by accident. Not that the Fed wants markets to go down, but rather that it may finally feel that the risks and costs of a pro-financial asset policy outweigh the benefits.

This would be something entirely outside the experience of most working investors and analysts. It will come, if it does, as a big shock.

Think of the past decades - the Long-term Capital Management bailout, the dotcom bubble, the aftermath of the dotcom bubble, the housing bubble and finally, the "rescue" of the economy in the wake of the financial crisis. All of these included as a central feature Fed policy which tended to indulge market runs and attempted to soften market falls.

None of this is to say that the Fed's ability or commitment to fight inflation is in doubt, only the widespread faith in it as an institution which can somehow magic into being excellent returns for investors, while standing by to clean up their messes.

This change in market psychology will be, on the whole, a good thing.

It will, however, tend to push downward swings in risk assets a bit harder. This leads to the next question: if the Fed tapers and the market swings down violently, will it return to form and seek to cushion once again?

If so, the Fed may find its credit with investors all tapped out.

--By James Saft, Reuters columnist  
-- The opinions expressed are his own

**ANALYSTS' RECOMMENDATIONS**

- **Bally Technologies** (BYI). Deutsche Bank raises target price to \$73 from \$55 after its fourth-quarter results
- **Freescale Semiconductor** (FSL). Morgan Stanley starts with underweight, view its premium multiple as unwarranted relative to margins, and expect a slower turnaround than the market appears to be pricing in
- **Kohl's Corp** (KSS). Deutsche Bank raises target price to \$46 from \$41 on valuation
- **Perrigo Co** (PRGO). JP Morgan raises target price to \$150 from \$132, expects room for multiple expansion from current levels post assumption of **Elan Corp** (ELN)
- **Williams-Sonoma** (WSM). Morgan Stanley raises target to \$64 from \$63, expect strong second-quarter results as it benefits from new concept growth and international expansion

**ECONOMIC EVENTS**

- 08:30** Housing Starts for Jul: Expected 0.900 mln Prior 0.836 mln
- 08:30** Build Permits for Jul: Expected 0.945 mln Prior 0.918 mln
- 08:30** Productivity for Q2-P: Expected 0.6 pct Prior 0.5 pct
- 08:30** Unit Labor Costs for Q2-P: Expected 1.2 pct Prior -4.3 pct
- 09:55** Reuters/UMich Sentiment for Aug-P: Expected 85.5 Prior 85.1
- 09:55** Current Conditions for Aug-P: Expected 98.0 Prior 98.6
- 09:55** Expectations for Aug-P: Expected 76.0 Prior 76.5
- 10:30** ECRI Weekly Index for 08/09: Prior 131.8

**COMPANIES REPORTING RESULTS**

- No major corporate earnings scheduled for the day.

**CORPORATE EVENTS**

- 12:00** Microchip Technology (MCHP). Annual shareholder meeting

**EXDIVIDENDS**

(Amount rounded off to two decimal places)

- **Bunge Ltd.** (BG). Amount \$0.30
- **Energizer Holdings Inc.** (ENR). Amount \$0.50
- **Honeywell International Inc.** (HON). Amount \$0.41
- **Macerich Co.** (MAC). Amount \$0.58
- **Moody's Corp.** (MCO). Amount \$0.25
- **QEP Resources Inc.** (QEP). Amount \$0.02
- **ResMed Inc.** (RMD). Amount \$0.25
- **Timken Co.** (TKR). Amount \$0.23
- **Walgreen Co.** (WAG). Amount \$0.32

*(All analysts' estimates are according to Thomson Reuters I/B/E/S)*

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