The Washington Times
washingtontimes.com

Business

Stocks mark century's first year of gains; With improved jobless figures, 'all needles are pointing north'

By Patrice Hill
THE WASHINGTON TIMES

01 January 2004

The markets were cheered on the last day of trading in 2003 by news of the lowest unemployment claims in nearly three years, adding an exclamation point to a year of spectacular improvement that marked the first up year for stocks since the market's collapse in March 2000.

The Dow Jones Industrial Average and Standard & Poor's 500 index regained much lost ground, rising 25 percent during the year, while the technology-driven Nasdaq Composite Index soared 50 percent. The market's advance traced the dramatic improvement in the economy, which appeared close to recession at the start of 2003 but ended the year sporting its best performance in two decades.

Yesterday, the Dow rose 29 points to 10,454 and the Nasdaq ended - perhaps symbolically - at 2,003 after the Labor Department reported that first-time claims for jobless benefits dropped last week by a seasonally adjusted 15,000 to 339,000. That was the lowest level since President Bush was inaugurated in January 2001. Evidence of improvement in the job market has been eagerly awaited in the markets after three years of job losses that threatened the recovery.

"All needles are pointing north" since the economy emerged with a bang and posted an 8.2 percent annual growth rate during the third quarter, said John Rutledge, a presidential economic adviser and chairman of Rutledge Capital. He believes the remarkable recovery will continue and fuel further gains for businesses and the markets during 2004.

"The economy has reached a tipping point," he said. "Where growth in previous quarters has been spotty and unbalanced, we now see broad growth across the board."

The best profit growth in years sparked the first yearly advance for stocks since 1999 as well as an investment binge by businesses, whose capital spending jumped by 15 percent during the third quarter. "It's a sign that this recovery will last," said Mr. Rutledge, and the return of business spending will "provide a second shot in the arm to the economy and the stock market in the months ahead."

Profit growth was stoked by business cost-cutting, soaring productivity gains and a dramatically weaker dollar, which boosted revenues from operations overseas to record levels. Also important to the stock market, dividend income increased for the first time in decades during 2003, spurred by a big cut in dividend taxes pushed through the Congress by Mr. Bush last year.

While many forecasters had predicted a modest return to growth in the market, last year's strong double-digit gains caught most by surprise and emboldened some to predict another outstanding year. Other Wall Street gurus said market growth won't be as dramatic as last year, but will gain steadily along with the economy.

Ed Yardeni, chief investment strategist with Prudential Securities, predicts the Dow will advance about half as much this year as last. "I think that 2004 will be a good year," he said. "The worst is over and better times are ahead, not only in 2004 but over the remainder of the decade."

Mr. Yardeni sees similarities between this decade and the 1990s, which also started with the economy in recession followed by a slow, jobless recovery. Despite the weak start, the 1990s turned out to be one of the best decades in history for the economy and the stock market.

"There was a George Bush in Washington, D.C., and a Saddam Hussein in Iraq both times," and the two countries went to war in both decades. "Both wars were short," he said. "Stock prices bottomed before the bombing started both times," and prices shot up more than 34 percent in the year afterward.

The 2000s "replay" of the 1990s could be so close as to end with an episode of "irrational exuberance" like the one that led to the market's collapse in March 2000, Mr. Yardeni said.

Barker French, chief investment strategist at Brinker Capital, said he expects low interest rates and solid profit growth to produce stock gains again this year, but is hopeful that the market's progress this decade mimics the steady but sure progress it posted last year.

"We don't want to return to the pattern of the mid- to late 1990s - that is 20 percent or more returns for multiple years - for fear that we would build another bubble," he said. Although the market might do a little better than its historical average of about 10 percent this year as it continues to recoup lost ground, "it's important for growth to be steady but not spectacular."

Joseph Quinlan, chief market strategist with Banc of America Capital Management, expects the market to benefit from an "election- year bounce" just as it benefited last year from a boom that mirrored the historical trend during a president's third year in office.

"The third year of a presidential cycle tends to yield the best average stock market performance," he said. "The fourth year tends to produce the second best performance," as the president's economic program - in this case, big tax cuts and spending increases along with a weaker dollar - works its way through the economy and markets.

The biggest danger for the market this year will arise if the Federal Reserve increases interest rates after having driven them to the lowest levels in more than 40 years, he said. Such a turning point at the Fed historically has ushered in a bad spell for the markets. But rates are so low this time around that the market may not react sharply to a small rise, he said.