



Expectations Creep

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Today's generation of college students have it easier, at least in one respect, than any of their predecessors. Over the years, college professors had made it easier for students to get good grades, a phenomenon known more commonly referred to as "grade inflation." The reasons for this erosion of expectations continue to be debated, but there is ample data showing that the trend toward more generous grading is real.

Today, a similar phenomenon plagues economic expectations.

Expectations have crept lower.

Take this fall as an example. 158,000 jobs were created in September and 104,000 jobs were created in August. Then the U.S. Department of Labor released monthly payroll numbers for October stating that 80,000 jobs were created. Bloomberg reported that analysts were expecting 90,000 new jobs – so what we got was pretty close.

Creating 80,000, or 90,000, or even 100,000 jobs does not even keep up with population growth. We need about 150,000 new jobs each month just to keep up with the expanding pool of potential workers. And we saw a decline in the rate of – already insufficient – job creation of the previous two months.

At the same time, the S&P 500 rose 10.9% in October, reportedly on the momentum of economic reports that seemed to beat expectations. Looking more closely at the reports, however, a disturbing trend is clear: economic numbers are beating progressively lower expectations.

Numbers are better when the growth rate rises year over year. In the case of job creations, the baseline number we need is at least 150,000 jobs/month just to *stay even* relative to population growth.

I took a sample of economic reports each week from October 3rd to November 30th (Table 1). Of the 24 reports, nine reports were sandbaggers – meaning the expectations were significantly below the previous month.



DATE	STATISTIC	ACTUAL	EXPECTATION	PREVIOUS	Did Actual Number Beat Easy Expectations
OCTOBER					
10/3/2011	ISM Manufacturing	51.6	50.5	50.6	Yes
10/4/2011	Factory orders	-0.20%	-0.10%	2.40%	Did Not beat
10/5/2011	ADP Employment	91,000	45,000	91,000	Yes
10/5/2011	ISM Service	53	52.8	53.3	Yes
10/7/2011	Nonfarm Payroll	103,000	60,000	0	Yes, beat difficult Expectations
10/7/2011	Wholesale Inventories	0.40%	0.50%	0.80%	Did Not beat
10/14/2011	Retail Sales -Ex Auto	0.60%	0.30%	0.10%	Yes, beat difficult Expectations
10/17/2011	Industrial Production	0.20%	0.20%	0.20%	Did Not beat
10/19/2011	Housing Starts	658,000	595,000	571,000	Yes, beat difficult Expectations
10/26/2011	Durable Goods orders	-0.80%	-1.00%	-0.10%	Yes
10/26/2011	New Home Sales	313,000	300,000	295,000	Yes, beat difficult Expectations
10/31/2011	Chicago PMI	58.4	58.9	60.4	Did Not beat
NOVEMBER					
11/1/2011	ISM Manufacturing	50.8	52.1	51.6	Did Not beat
11/3/2011	Factory orders	0.30%	-0.20%	-0.20%	Yes
11/2/2011	ADP Employment	110,000	100,000	91,000	Yes, beat difficult Expectations
11/3/2011	ISM Service	52.9	53.8	53	Did Not beat
11/4/2011	Nonfarm Payroll	80,000	85,000	103,000	Did Not beat
11/9/2011	Wholesale Inventories	-0.10%	0.50%	0.40%	Did Not beat
11/15/2011	Retail Sales -Ex Auto	0.60%	0.20%	0.60%	Yes
11/16/2011	Industrial Production	0.70%	0.40%	0.20%	Yes, beat difficult Expectations
11/17/2011	Housing Starts	628,000	604,000	658,000	Yes
11/23/2011	Durable Goods orders	-0.70%	-0.90%	-0.80%	Yes
11/28/2011	New Home Sales	307,000	312,000	313,000	Did Not beat
11/30/2011	Chicago PMI	62.6	57.5	58.4	Yes
SOURCE: Briefing.com and Yahoo					

For example, look at the ADP Employment report on October 5. Employment was expected to decline to 45,000. Actual employment came in at 91,000, exactly what it was the previous month. The *expectation*, however, was far below what it had been the previous month, making the storyline around this data much more upbeat.

In October, only four of the 12 statistics solidly beat expectations that were above those of the previous month. In November, only two of the 12 statistics accomplished this same feat. Just as many statistics came in below expectations as well as below the previous month's report. And four statistics in October and five statistics in November beat expectations that were easy compared to the previous month.

Just because analysts say it is better does not mean it is better. As expectations creep down, we lose our prospective on what we really need to create economic growth.



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