After 2014 party, US investors may face hangover

NEW YORK: Revelers ringing in of the new year need to watch out for the next day's hangover. And investors may experience a similar feeling early in 2015 after a two-year run that has propelled US stocks up by nearly 50 percent. Headed into the last trading day of 2014, the S&P 500 has gained nearly 13 percent on the year, shaking off concerns about valuations thanks to improved economic growth and a very accommodative US Federal Reserve. Add in dividends and the advance is 15 percent.

However, the S&P 500's forward price-to-earnings multiple - based on 2015 earnings expectations - is at about 17 now, exceeding the 15-year average of about 15. It means that a pick-up in profits growth may be essential if the market is to continue to add to its historic gains. And yet Wall Street analysts' estimates for S&P 500 earnings growth for coming quarters are languishing in the mid-single digits.

With the Fed ready to begin raising interest rates for the first time in a decade, and the strong dollar providing a headwind for companies with overseas operations, a lot will depend on whether the recent strong growth in domestic demand can drive corporate profits higher than those estimates. Whether consumers and companies benefit enough from lower oil prices to more than offset the effects of the slide on the energy sector is also critical.

"Multiples almost always go down when the Fed raises rates - you're going to have to depend on earnings," said Jim Paulsen, chief investment strategist at Wells Capital Management in Minneapolis, which has $345 billion in assets under management. The S&P 500's forward price-to-earnings ratio sat at about 13 times at the beginning of 2013; it is now closer to 17, according to Thomson Reuters data.

Since 1940, such a level is associated with S&P returns (excluding dividends) of about 5 percent over a 12-month period, according to data from Citigroup. The high valuation concerns are starting to have some impact on trading. Stocks have been noticeably more volatile in the last few months; the CBOE Volatility Index, or VIX, has averaged 15.4 over the past 12 weeks, compared with 12.6 at the end of August.

Share Buybacks

If the Fed tightens, the higher rates will not only raise financing costs generally but would also be a deterrent to borrowing to do the share buybacks that have helped to propel earnings per share growth and stock prices gains in the past few years. With such artificial support crumbling, corporate America will have to rely much more on demand from domestic customers to drive earnings growth. Europe is expected to grow at just above 1 percent in 2015, according to Reuters data, Russia has been slammed by oil's decline, and China and other major emerging markets are struggling with weak demand as well.

Switching to more of a reliance on sales growth rather than the Fed's cheap money may not be an easy transition. Fourth-quarter estimates have plunged in recent weeks, largely in the energy sector as crude oil prices have cratered. Annual growth is now expected to come in at 4.3 percent for the S&P 500 in the fourth quarter, down from a forecast of 11.1 percent growth on only Oct 1.

Citigroup's chief equity strategist Tobias Levkovich, in a note on Tuesday, said estimate cuts in the next few weeks, when companies typically warn if they expect to report disappointing results, could lead to some reversals and volatility, as "some of the late 2014 S&P 500 gains appear to have been borrowed from 2015's returns," he wrote.

In perhaps a sign of things to come in the energy sector, Civeo Corp, which builds temporary housing for oilfield workers, said revenue could fall by one-third due to falling crude prices, and cut its workforce and suspended its dividend. The company's shares lost almost 53 percent Tuesday. Earnings expectations for S&P 500 companies for the first half of next year aren't that encouraging: First- and second-quarter earnings growth estimates currently stand at 5.3 percent and 5.9 percent, respectively.

"If you don't feel that you have the earnings wind at your back, and you don't have the monetary policy wind at your back, why pay more than the prices people have paid in many cases since 2000 for stocks?" said Mike O'Rourke, chief market strategist at JonesTrading in Greenwich, Connecticut. That said, earnings expectations coming into 2014 turned out to be far too pessimistic: On Dec 31, 2013, the forecast was for per-share earnings of $120.89 on the S&P 500. With fourth-quarter earnings season approaching, actual and expected earnings were $126.50 per share, according to Reuters data.

So far in the fourth quarter, expectations have fallen largely due to the energy industry's woes, but sectors that could benefit from lower fuel costs, particularly the consumer discretionary sector - which includes many retailers - have not seen an attendant pickup in expectations. That sector is currently forecast to grow 8 percent for the quarter, down from 13.9 percent estimated on Oct 1.

Despite the caution, few are calling for a bear market given the U.S. economy's acceleration. An early December Reuters poll of Wall Street strategists forecast the S&P 500 hitting 2200 at the end of 2015. After December's big gains, that suggests just a small rally amid a year of short-term advances and retreats. That said, it's not as if 2014 didn't have its rough spots, either, and yet the year is ending with a flourish.

"In the spring of 2014 the market went nowhere for three months. In the summer through the fall the market went nowhere, and the market at its bottom in October was unchanged for the year," said Dan Greenhaus, chief strategist at BTIG LLC in New York. "The question is whether the general environment is supportive of higher stock prices, and the answer is still yes." — Reuters

US tobacco auctions all but snuffed out

DANVILLE, Kentucky: Tripp Foy's sing-song chant rang out like a sentimental oldie for die-hard farmers clinging to the old way of selling tobacco, as a small procession of buyers shadowed him down long rows of reddish-brown leaf piled in bales. Farmers who have spent their lives tending the aromatic crop in their fields find comfort in Foy's rat-a-tat style, part of an auction system that's been all but snuffed out by another way of selling tobacco after years of declining smoking rates. "It's kind of in our blood," said tobacco farmer Walter Browning. "But I'm about bled out."

This tobacco-belt tradition, once as much a part of Kentucky's fabric as bourbon or horse racing, is fading away - and it's taking the maestros like Foy with it. "The chant of an auctioneer can sound as good as a song," said Foy, 63, who has spent four decades auctioning tobacco in Kentucky - the nation's top burley producer. "You can walk down a row and you can almost dance to the tune of the sale."

Years ago, multiple auctioneers plied their trade in each of the state's biggest burley markets as sales seasons typically stretched from late autumn until March. The competition for top auctioneers was fierce as warehouse operators looked for any edge to pull in more business from farmers. Now, most burley is sold under contracts between farmers and tobacco companies. Contracting sprung up a decade ago after the demise of a federal program of price supports and production quotas that guaranteed minimum prices for most of the 20th century.

The new system cut out warehouse operators as middle men. Tobacco companies typically don't disclose how much contract leaf they purchase or for how much to avoid tipping their hand to competitors. Excess world burley tobacco supplies and lower demand are driving down prices, said University of Kentucky agricultural economist Will Snell. Last year's crop averaged $2.06 per pound. Quality leaf sold under contract is still fetching prices in the $1.90s to $2 a pound this season, he said. But selling non-contract burley, especially lower-quality leaf, is "going to be a struggle," he said.

Droves of farmers got out of tobacco as US smoking rates declined. The number of US tobacco farms dropped from 124,270 in 1992 to 16,234 during the last federal crop census in 2007. Burley, once a $1 billion crop in Kentucky, now generates about $300 million for the state's remaining growers.

Despite the setbacks, a handful of auction markets have stubbornly hung on. Supporters say they provide a necessary alternative for tobacco farmers unable or unwilling to sign contracts or unhappy with prices offered by the companies at contract receiving stations. About 400,000 pounds of tobacco were available last month on the opening sales day at the Danville warehouse, where Foy presided as auctioneer. Jerry Rankin, the warehouse operator, plans twice-weekly auctions for larger supplies of non-contract leaf. Rankin bought up some of the burley when bidding by leaf dealers was too low. Rankin bought it on speculation, hoping to sell it to tobacco companies or dealers. He expects all the leaf to wind up in cigarettes.

Demand, Prices Depressed

Total output in burley-production states is forecast at 211 million pounds this year, with Kentucky accounting for an expected 161 million pounds. Some Kentucky farmers found out in the spring they had been dropped from production contracts, after buying tobacco plants and preparing ground, Rankin said. They went ahead with the crop, putting millions more pounds of leaf in the auction system at a time when demand and prices are depressed.

"These growers grew it in good faith and did a good job doing it, and they're spinning their wheels," Rankin said. "Some of them are going to go under." Other than Foy's familiar chant, little else resembled opening days from the era when every bit of leaf went through the auction system. Grim-faced growers watched their burley sell for paltry amounts - generally $1.25 or $1.30 a pound. "It's a sad day," said farmer Leland Turner. "I never thought I'd see the time when tobacco would be so cheap."

Prices improved slightly in follow-up sales at the Danville warehouse, to an average of $1.35 to $1.44 per pound, Rankin said. But that's not nearly enough to cover expenses for the crop, unless farmers and their families did all the work themselves. Years ago, the auctions signaled the promise of money filtering through small towns and big cities alike. For farmers, it was the anticipation of a big pay day. If early prices were good enough, the payoff came right before Christmas. Bankers and merchants kept tabs on how high the bidding went.

There was no festive mood as this year's sales opened at the Danville warehouse. An ag credit lending agency supplied doughnuts for the few dozen people on hand. Rankin gave a short speech, thanking the farmers for their business. For some of the growers looking on, the end of the line was coming into focus. Browning said he already decided this year's crop would be his last. He has a factory job and used his tobacco income to pay property taxes, but he wasn't sure he would get enough to cover the bill this year. "You spend a lot of time on it for what little I get," he said. "Instead of going on vacations with my wife, I'm hauling tobacco."

Foy's own schedule has slowed considerably. Years ago, he presided over tobacco sales for nine months out of the year across the eastern US. Now, he auctions tobacco only at a handful of warehouses in Kentucky. He estimates only a couple of auctioneers besides him remain. "I don't know that I'm the last of the breed," he said. "But unless the industry changes, the ones that are tobacco auctioneers now, when we're all dead and gone, there won't be any more." — AP

DANVILLE, Kentucky: In this Nov 18, 2014, photo, auctioneer Tripp Foy (right) hands a tobacco purchase ticket to a buyer at an auction. — AP

CARACAS: Venezuelan President Nicolas Maduro speaks during a press conference at Miraflores presidential palace on Tuesday. — AFP

Recession-hit Venezuela vows New Year reforms

Foes scoff at Maduro • Inflation tops 63%

CARACAS: President Nicolas Maduro vowed on Tuesday to reform Venezuela's Byzantine currency controls in early 2015 as part of a six-month plan to shake Venezuela out of recession, but foes accused him of incompetence and inaction. After sitting on GDP data all year, the Central Bank announced that OPEC member Venezuela had entered recession, with the economy contracting in each of the first three quarters: by 4.8, 4.9 and 2.3 percent, respectively. Confirming Venezuela as the region's worst-performing major economy this year, the bank also said 12-month inflation reached 63.6 percent in November, the highest rate in the Americas.

Maduro, 52, who won election last year to replace his socialist mentor Hugo Chavez, blamed political opponents for damaging the oil-dependent economy with months of street protests earlier this year. Maduro vowed to head up a six-month plan to turn around the economy in 2015 by reducing inflation-inducing liquidity, boosting international reserves, cutting unnecessary costs, and reforming the three-tier foreign exchange system.

"We are going to perfect the currency system," he told a news conference, without giving much further detail on that or the other measures. "2015 will be a year of economic recovery ... great economic transformation." Opponents quickly slammed Maduro's comments as devoid of detail and real solutions for the ailing economy. "Yet again, no announcements. He doesn't know what to do," opposition leader Henrique Capriles fumed. "Today makes clear to all Venezuelans that with Nicolas we will not escape the chaos." Venezuela, whose last recession was from 2009-2010, has been handicapped by the plunge in oil prices. Venezuelan crude, which provides 96 percent of hard currency revenues, has halved from mid-year to $46 per barrel.

'Economic War'

Venezuela's central bank had not published inflation data since August. The figures released on Tuesday put September inflation at 4.8 percent, October 5.0 percent and November 4.7 percent, compared with the same months of 2013. The bank said opposition demonstrations during the year had disrupted both distribution and production, causing an inflationary spike and the GDP decline. The demonstrations sparked Venezuela's worst political violence in a decade. Forty-three people, including protesters, security officials and Maduro backers, died.

Chavez-era welfare policies have long been popular among Venezuela's poor, and the bank said social indicators were all improving despite the poor GDP data. It said extreme poverty was down to 5.4 percent of households in 2014, half the level before Chavez came to power, while unemployment fell to 5.9 percent. "Despite the protests and economic war during 2014, Venezuela's economic indicators have improved," Maduro said. "This economic war, this fall in the oil prices, is a great opportunity for economic change. 2015 is the year of opportunity, for great change in the economic model."

Many analysts have been recommending a unification of Venezuela's currency controls and a rise in gasoline prices that are the cheapest in the world. But Maduro has balked at such measures so far, perhaps wary of a social backlash prior to a crucial vote for a new parliament next year. Russ Dallen, head bond trader at investment bank Caracas Capital Markets, said he counted Maduro using the phrase "economic war" 63 times during Tuesday's news conference. "The speech was long on excuses and short on adjustments," he said. "If Maduro had a million dollars for each of his excuses, Venezuela's economic problems would be solved."

The central bank said Venezuela's balance of payments posted a surplus of $6.8 billion by the end of the third quarter, with a current account surplus of $899 million, and the capital account showing a deficit of $568 million. Venezuelan exports, of which oil accounts for more than 90 percent, fell 14.2 percent to $19 billion in the third quarter, while imports were down slightly, by 1.4 percent, to $12.2 billion in the same period. — Reuters

US opening of oil export tap widens global market battle

WASHINGTON/NEW YORK: The Obama administration has opened a new front in the global battle for oil market share, effectively clearing the way for the shipment of as much as a million barrels per day of ultra-light US crude to the rest of the world. The Department of Commerce on Tuesday ended a year-long silence on a contentious, four-decade ban on oil exports, saying it had begun approving a backlog of requests to sell processed light oil abroad. It also issued a long-awaited document outlining exactly what kinds of oil other would-be exporters can ship.

The administration's first serious effort to clarify an issue that has caused confusion and consternation in energy markets for more than a year will likely please domestic oil drillers, foreign trade partners and some Republicans who have urged Obama to loosen the export ban, which they see as an outdated holdover from the 1970s Arab oil embargo. The latest measures were wrapped in regulatory jargon and couched by some as a basic clarification of existing rules, but analysts said the message was unambiguous: a green light for any company willing and able to process their light condensate crude through a distillation tower, a simple piece of oilfield kit.

"In practice this long-awaited move can open up the floodgates to substantial increases in exports by end 2015," Ed Morse, global head of commodities research at Citigroup in New York said in a research note. The action comes at a critical juncture for the global oil market. World prices have halved to less than $60 a barrel since the summer as top exporter Saudi Arabia, once a staunch defender of $100 oil, refused to cut production in the face of surging US shale output and tempered global demand.

By opening the door to US crude exports, the administration is offering a bit of relief to some domestic drillers that have said that they are forced to sell their shale oil at a discount of as much as $15 a barrel versus global markets as fast-rising domestic supplies overwhelm local demand. But the impending swell of U.S. petroleum into global markets may intensify what many analysts say is a pivotal oil market war, with Saudi Arabia and the Organization of the Petroleum Exporting Countries (OPEC) unwilling to yield ground. Now they will face even greater competition beyond US shores.

If they can boost selling prices by even a dollar or two, oil producers in places such as the Eagle Ford of Texas will be better able to withstand the slump in oil markets. Morse said US condensate exports could rise from 200,000 bpd to as much as 1 million bpd by the end of next year. "This has an interesting impact on the current confrontation between Saudi Arabia and shale," he said. Among those most at risk from the US shale exports is Nigeria, which pumps similarly light, sweet oil. The OPEC member has already lost the US market to shale, with its exports falling from more than 1 million barrels per day to next to nothing; now it will face US competition in Europe and Asia, too.

Just the FAQS

The Bureau of Industry and Security (BIS), which regulates US export controls, has come under enormous scrutiny over the past year because of growing pressure to clarify confusing regulations on exporting crude. While untreated crude oil is generally banned from being exported, refined fuels such as gasoline and diesel can be freely sold abroad. The question that has bedeviled US producers is how the rules apply to "processed condensate," ultra-light oil that has been heated through a very basic refining unit.

On Tuesday, the BIS said it had given permission to "some" companies to ship treated light oil but did not give details about what it had approved. Two energy companies, driller Pioneer Natural Resources and mid-stream firm Enterprise Products Partners , have been regularly exporting processed condensate since the summer after receiving a private permit from the BIS. But several dozen other companies that also raced to file similar requests were left waiting, with no timeline for action.

The agency also released its first ever written guidance on the rules themselves in the form of frequently asked questions (FAQs), clarifying a series of detailed questions that had clouded efforts to move forward with substantial exports. The document gives "considerable discretion" that could allow for rising export volumes in the future, measures that could narrow the price gap between U.S. benchmark WTI crude and global marker Brent, said Kevin Book, managing director at ClearView Energy Partners LLC. On Tuesday, the Brent/WTI spread narrowed by more than 50 cents to around $3.70 a barrel. In its guidelines, the BIS said that most goods can be shipped abroad "without a license" - a reminder that some analysts read as encouraging shippers to "self-classify" their condensate, as Reuters reported earlier.—AFP