washingtonpost.com

Falling Oil Prices Boost Stocks After Volatile Week

By Renae Merle and Simone Baribeau
Washington Post Staff Writers
Saturday, August 9, 2008; D01

U.S. stocks rebounded yesterday as crude oil prices continued a slide that helped offset deepening losses at mortgage giant Fannie Mae.

The Dow Jones industrial average climbed 302.89 points, or 2.65 percent, to close at 11,734.32. That more than wiped out Thursday's 225-point drop and left the index up 408 points, or 3.6 percent, for the week.

The volatile week reflected continued concerns about declining retail sales and the country's economic outlook, analysts said. That was tempered by declining oil prices that have raised hopes that consumers will be drawn back into their cars and to shopping malls.

The broader Standard & Poor's 500-stock index gained 30.25, or 2.39 percent, yesterday to close at 1296.31. The technology-oriented Nasdaq composite index gained 58.37 points, or 2.48 percent, to close at 2414.10.

"The main thing putting a fire under the market is that crude oil prices continue to come down. That is lifting everything that is not in the energy patch," said Brian Bethune, an economist for Global Insight.

Crude oil prices settled at $115.20 yesterday, down $4.82 a barrel on the New York Mercantile Exchange. Prices are down $30 a barrel from their July high.

Oil prices have been falling for several weeks because of declining U.S. fuel demand. That, coupled with a stronger U.S. dollar on economic concerns in Europe, helped bring down prices even further yesterday, analysts said. The U.S. Dollar Index was up 1.7 percent yesterday.

Some economists think the dollar has reached its low against the euro, while others such as Merk Investments chief economist Joseph Brusuelas think otherwise. "We are not convinced," he said. "We would not be surprised if over the next few weeks, the dollar resumed its extended period of depreciation."

A European economic slowdown could further sap oil demand and put the struggling U.S. economy in a better light, analysts said. "There is a perception that when you compare the U.S. economy to the economies of the euro zone and the United Kingdom, we look pretty good," said Ed Yardeni, president of Yardeni Research. "There is a perception that they are falling faster into a deeper recession and that we, in the U.S., are muddling through."

The decline in oil prices is overdue, said Fadel Gheit, an oil analyst with Oppenheimer. Prices are still up 22 percent for the year and 72 percent compared to a year ago, he said.

"The market is celebrating a $5 drop in oil prices, but we're not out of the woods yet," Gheit said. "Oil prices are still $50 [a barrel] more than they should be."

Declining oil prices also helped the airline sector, which has been hard hit by soaring fuel prices. Continental Airlines shares jumped 12 percent yesterday, and United Airlines' parent company saw a 16 percent increase.

The rally extended to the financial services sector, despite a dismal earnings report from mortgage giant Fannie Mae. Its stock fell 9 percent in trading yesterday. Freddie Mac closed virtually unchanged at $5.90, up 1 cent, after reporting Thursday that losses from foreclosures and other failed home loans nearly doubled during the second quarter.

But other firms in the financial sector continued a rebound. Lehman Brothers gained 5.4 percent and Merrill Lynch was up 2.9 percent. "I am a little surprised that this rally has persisted as much as it has," said Sean Ryan, a banking analyst at Sterne Agee in New York.

And analysts are predicting more bad news as unemployment rates increase and the retail sector struggles with declining consumer spending. "Banks are only starting to work through their housing problems," Ryan said.

Yesterday's rebound could be wiped out by a drumbeat of negative economic news next week, when retail sales figures and industrial production figures are scheduled to be released. "These are not going to be drastic declines, but declines nonetheless," said Bethune from Global Insight. "That is not a good start to the third quarter."

Meanwhile, the Labor Department reported yesterday that worker productivity, measured by an employee's hourly output, rose 2.2 percent in the second quarter. That was slower than in the first quarter, when it rose 2.6 percent. Economists had expected a 2.5 percent increase as layoffs forced the remaining workers to do more, according to a Bloomberg survey.

But the 2.2 percent increase is a healthy rate that should help ease pressures on the Federal Reserve to increase interest rates, analysts said. "Strong productivity growth should mean that inflation would abate and the Fed would be able to leave interest rates alone" as the year progresses, said Peter Morici, professor at the University of Maryland business school.

The Labor Department also revised its first-quarter productivity growth estimates for non-financial corporations from 4.6 percent to 1 percent. That could indicate that the increase in productivity levels may not continue indefinitely, analysts said. "If you keep cutting hours and the economy doesn't bounce back, falling output due to a reduction in demand will result in a decline in productivity," Brusuelas said. "That's the concern."

Labor costs, another indicator of inflation pressures, rose 1.3 percent during the second quarter, compared with 2.5 percent the previous quarter.

View all comments that have been posted about this article.

You must be logged in to leave a comment. Login | Register

Submit

Comments that include profanity or personal attacks or other inappropriate comments or material will be removed from the site. Additionally, entries that are unsigned or contain "signatures" by someone other than the actual author will be removed. Finally, we will take steps to block users who violate any of our posting standards, terms of use or privacy policies or any other policies governing this site. Please review the full rules governing commentaries and discussions. You are fully responsible for the content that you post.