Stocks to track mortgage woes and CPI

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By Ellis Mnyandu

NEW YORK (Reuters) - Troubles in the subprime mortgage sector could put Wall Street on edge next week just as investors look for key economic data, including the Consumer Price Index, to shore up the market's nascent recovery after its recent plunge.

Fanning concerns about the sector that lends to home buyers with poor credit is this past week's precipitous slide in the stock of New Century Financial Corp. (NEW.N: Quote, Profile, Research) amid fears that the lender could file for bankruptcy protection.

The subprime lender said on Thursday it had stopped accepting new loans. Even after saying it had lined up $265 million in funding, New Century disclosed it was negotiating for further relief.

Investors worry that fallout from rising loan defaults in the subprime market could hurt consumer confidence as lenders tighten credit amid the housing slowdown.

Wall Street keeps a close watch on the moods and habits of consumers because their spending is a key driver of U.S. economic growth and corporate profitability.

"The worst thing that could happen to any economy is the loss of confidence," said Med Yones, president of the International Institute of Management, an economic research and forecasting group in Las Vegas.

He said the bursting of the real estate bubble and high consumer debt were a major worry and "if people started to think there may be a lot of bankruptcies (in the subprime lending market), then you're going to see the stock market sell off."

SUBPRIME TIME

Next week could give Wall Street more insight into the extent of the subprime lending woes as Goldman Sachs Group Inc. (GS.N: Quote, Profile, Research), Lehman Brothers Holdings Inc. (LEH.N: Quote, Profile, Research) and Bear Stearns Cos. Inc. (BSC.N: Quote, Profile, Research) are due to kick off the quarterly earnings reporting season for big investment banks next week.

Wall Street's big banks buy mortgages from lenders and package them into mortgage-backed bonds.

"The possibility of (New Century) declaring bankruptcy is certainly raised by what they said" this past week, said Michael James, senior trader of regional investment bank Wedbush Morgan in Los Angeles.

"I think the potential fallout from what might happen with New Century over the weekend and its effect on the fixed-income market are certainly part of the" worry, James added.

On Friday, stocks finished mixed as concerns about the subprime mortgage market took a toll and offset some of the optimism created by data showing the U.S. economy added 97,000 jobs in February.

For the week, all three U.S. stock indexes rose, with the Dow Jones industrial average (.DJI: Quote, Profile, Research) up 1.34 percent, the Standard & Poor's 500 (.SPX: Quote, Profile, Research) up 1.13 percent and the Nasdaq Composite Index (.IXIC: Quote, Profile, Research) up 0.83 percent. With these gains, both the Dow and the S&P 500 broke a two-week losing streak.

CPI AND CONSUMER SENTIMENT

But besides fretting about housing woes, investors will brace themselves for a barrage of economic data that could yield crucial clues about the health of the U.S. economy and the future direction of U.S. interest rates.

The week's most closely watched data is likely to be the Consumer Price Index for February, due on Friday. Economists polled by Reuters have forecast an increase of 0.3 percent in February's overall CPI, after January's

0.2 percent gain.

Excluding volatile food and energy prices, February's core CPI is seen up 0.2 percent. In January, it rose 0.3 percent.

A preliminary look at March consumer sentiment also will be provided on Friday by the Reuters/University of Michigan Surveys of Consumers. The consumer sentiment index is forecast at 90.0, down from 91.3 in February.

Another report that will get attention on Friday will be the Federal Reserve's February data on industrial production, forecast to gain 0.2 percent after a 0.5 percent drop in January, and the capacity utilization rate, pegged at 81.3, up from 81.2 in January.
On Thursday, Wall Street will get the U.S. Producer Price Index for February, which measures wholesale prices. The forecast: Overall PPI, up 0.5 percent in February, compared with January's drop of 0.6 percent. Core PPI is forecast to rise 0.2 percent in February, matching January's gain.

With inflation on Wall Street's mind, investors will continue to keep close track of the price of oil. On Friday, U.S. crude for April delivery (CLJ7: Quote, Profile, Research) slid $1.59 to settle at $60.05 a barrel on the New York Mercantile Exchange on profit-taking after a recent rally. For both the week and on Friday alone, NYMEX April crude was down 2.6 percent.
On Tuesday, February retail sales will be released. Economists forecast overall retail sales rose 0.3 percent last month, both including and excluding auto sales.

The retail sales report will come on the heels of Friday's healthy jobs numbers, which suggested consumers may be in the mood to spend.

On Monday, Federal Reserve Board Governor Randall Kroszner is scheduled to speak on "Inflation Dynamics" at a conference for the National Association for Business Economics.

GET READY TO SWING
This past week marked Wall Street's attempt to reverse a slide it suffered a week earlier as the diminishing appetite for risk and concerns about economic growth triggered a flight to safe-haven assets such as U.S. Treasuries, wiping out the stock market's gains for 2007.
The rebound has been punctuated by rising volatility, raising doubt about its sustainability.
But money managers and analysts said longer term, the stock market is still poised to rack up gains this year as share valuations fall into line with expectations.

"Over time, you have to realize that the reason you get superior returns in the market is because you have to endure higher volatility. That's the price of admission," said Rafael Resendes, co-founder and president of The Applied Finance Group, a capital market research and consulting firm in Fresno, California.

"For the investors, I would say nothing has changed, except maybe you reevaluate your asset-allocation scheme, maybe buy more on the dips," Resendes said. "But for a trader, obviously, there's going to be a lot of opportunities that arise as the market readjusts and gets used to a world of higher volatility."

And speaking of volatility, next Friday marks the quarterly expiration and settlement of four different types of March futures and options contracts -- a convergence known as quadruple witching.
Fasten your seat belts.

(Wall St Week Ahead runs weekly. Questions or comments on this column can be e-mailed to: ellis.mnyandu(at)reuters.com)