

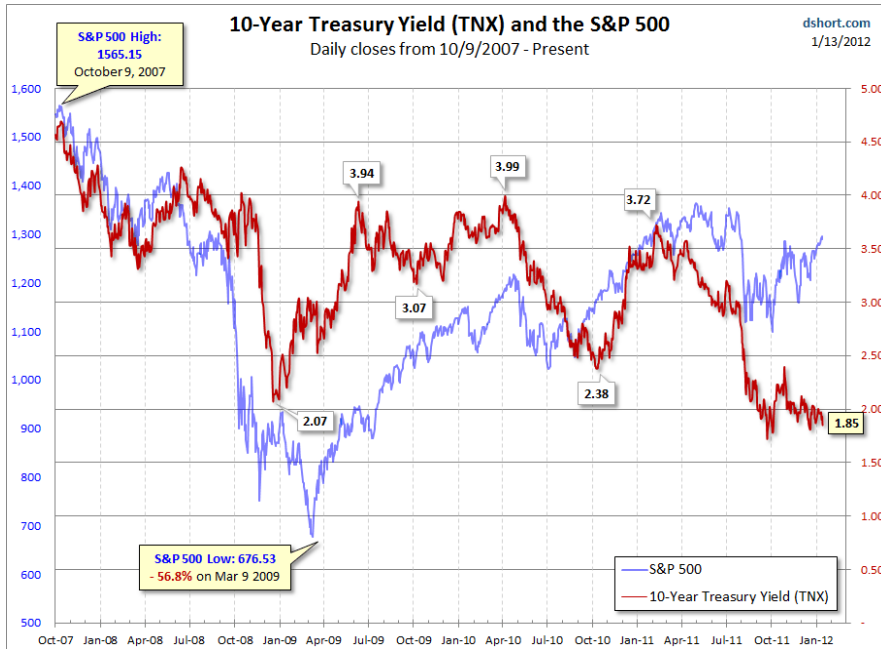
BOTH MARKETS CAN'T BE RIGHT

WEB BUZZ 2012.01.23

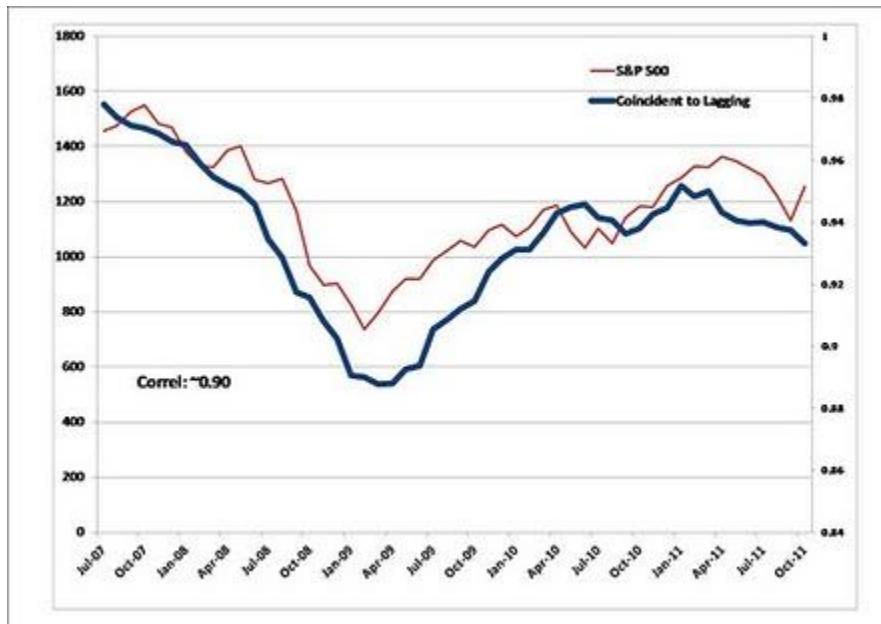
There continues to be much confusion over the outlook for the worldwide economy and particularly as it pertains to the U.S. Most of the confusion centers on which indicators lead, coincide, or lag future economic events. Wall Street, which is most often bullish, pays little attention to which is which. Their entire mantra revolves around low-balling predictions and then buying on “better than expected.”

The old-fashioned leading indicators originated by the National Bureau of Economic Research remain strong - the problem being that some 45% weight is given to financial indicators, which cannot work when the Federal Reserve controls short-term interest rates at 0%. If one disregards these indicators, things look worrisome. We understand that these will be changed later this month for that very reason. As an aside, over the years there have been many financial indicators that have been tested for use as leading indicators. None of them have been reliable. We tested them all. The reason, of course, is that markets are not efficient, despite what nearly all the textbooks teach. That being the case, their usage is of little value.

There is a financial correlation that is in sync most of the time - that being long government bond yields tend to go up with the stock market as well as down. Please note the two charts which display that relationship. Note that over the last six months or so that correlation has diverged. Someone has it wrong. We believe it is the stock market.



Adapted from dshort.com



Adapted from pragcap.com

In our opinion, lower stock prices, lower government bond yields, and economic recession are in our future.