

BEGINNING OF THE END OR END OF THE BEGINNING?

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As markets continue to become more and more distorted on the upside, every once in a while, a sign appears which makes one believe a serious change is underway. The question always becomes: is this the beginning of the end or the end of the beginning? For low these many years it has been the latter. How about now? When these seemingly turning points arrive, I always think of my good friend and fellow Kansan Wayne Angell, former Federal Reserve member and chief economist for Bear Stearns. Markets require trust and confidence to be viable. Such is the case now as it is accepted dogma that what was once a policy of too big to fail has now morphed into no one can fail. Behind the curtain that Dorothy was seeking on the yellow brick road to Oz lies the Federal Reserve, the buyer of last resort.

Now, back to Wayne. While with Bear Stearns, much of his time was spent making speeches and attending client meetings. Spreading the gospel, if you will. Don't get me wrong, Wayne was and is a very bright man of good character, but here's the rub. In a lawsuit against Bear Stearns, Ace Greenberg—Wayne's boss and Wall Street heavyweight—said in his testimony that Wayne's comments were always just show and Bear Stearns did not pay any attention to what he thought. What an endorsement from one's boss. OK, what's the point? We have a monetary policy conducted by the Fed, engineered by academic economists who don't have a clue as to what they are doing and what they have done. In essence they have made addicts of us to a point where we have no fear, no idea of value, believing in the wizard behind the curtain that is sure to come to our rescue if trouble be fronts us. Ace says no one is behind the curtain.

The possible tell referred to the above (sign) is the billions of dollars now flowing out of the junk bonds. It has been underway bit by bit, but appears (sign) to be accelerating. This tells me that some of the speculative players want out the door while it remains open at decent prices. We have had other previous periods where this took place (the end of the beginning). This one seems more likely to be the beginning of the end, but we shall see.

There is a reasonably positive correlation between junk bonds and common stocks. Please note chart #1 below. The sector is considered a key proxy for the stock market, the

correlation is near perfect with the S&P in terms of direction. This year, the S&P 500 has outperformed, but continues to move in the same direction. Note the move as of late.

I continue to be amazed by the 20%+ advance in stocks since the election a year ago. For several years, there was little to no advance as seen in chart #2. What has happened fundamentally since the election, in my opinion, does not warrant such a move. But, who pays attention to the fundamentals?

Chart #1



Chart #2

