THE DANA VIEWPOINT

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*Dow: 18,019*

# Catch-22

Oil has been the big issue with investors so far this year. The price of a barrel of crude oil has dropped from $108 last June to $45 recently. That's a 58% drop, huge by any measurement. This is a boon to consumers as the price of gas at the pump has dropped from as high as $5 a gallon in some parts of the country to as low as $2 a gallon in other parts of the country. Consumers will also have lower heating costs this winter, which so far has been a cold one. Much of the money being saved will be spent on goods and services, which will boost our economy. In addition, transportation companies (FedEx and UPS) will save money, which can be spent in other areas of the economy. Airlines (Delta, UAL) will benefit also. Perchance they might lower airfares and attract more travelers who will spend more money elsewhere. All good, right? Well there is a catch, a catch-22 if you will; you may remember Yosarian trying to get out of the Army by pretending to be insane. The catch-22 was if you were trying to get out of the Army you couldn't be insane. The catch-22 in the oil equation is that lower prices mean lower profits for the drillers. That in turn means worker layoffs and a drop in spending for equipment. In addition to falling prices of oil company stocks, investors could face a cut in dividend payments. Some smaller independent drillers have or are contemplating bankruptcy. The Saudis, largest oil producers currently, have said that at $60 a barrel or less, drillers using new technologies could not extract oil profitably. The price of oil in the last week has rebounded to $53 a barrel. Investors are in a quandary here, whether to buy oil stocks or stocks of retail or transportation companies. It is unlikely oil will rebound to $100 a barrel anytime soon. A range of $60-$65 a barrel seems reasonable. However, until the price stabilizes you can expect the price of oil to contribute to the price volatility of the stock market.

What about the stock market? In addition to oil, stocks are being buffeted by the Federal Reserve's comments and inaction. The economy continues to improve. The private sector added 257,000 new jobs in January and wages are showing signs of improving. The unemployment rate ticked up to 5.7%. That's OK as more people who had given up looking for work reentered the workforce. These people obviously sense an improving job market. While GDP grew at a 2.6% rate in the fourth quarter, down from 5.0% in the third quarter, it was a reasonably strong number. Investors are concerned that when the Fed increases rates, the six year bull market will be toast. The Fed may have put themselves in a box with their stimulus programs and by

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keeping interest rates too low too long. This allowed investors to pile into common stocks in search of returns. Investors are a skittish lot and deservedly so with all of the uncertainties in the world. A quarter point rise in rates will not stall the economy, nor would a 1% rise in rates. Remember in the early 1980’s the prime rate reached 21% and inflation was running in excess of 10%. Paul Volcker, the Fed president at the time, advised President Reagan to do nothing about interest rates as he felt rates would seek their own peak and then drop.

It is not the Federal Reserve’s job to try and control interest rates across the maturity spectrum. Their mandate is price stability in order to allow for maximum economic output. The Fed may not even raise rates this year. Yet, after every Fed meeting, investors hang on their every word. This adds to market volatility. The Fed has too much power and they should not be micromanaging interest rates. That’s not in their job description. However, they are doing it and investors must recognize the Fed’s current importance in the marketplace. Do not be afraid of rising interest rates. It may just be the time when corporations and small businesses see it as a time to expand.

A Mess - trying to put two pounds of feathers in a one pound bag. That’s the Eurozone. Many of their members are facing a two-edged sword: recession and deflation. They are trying to print their way out of these twin problems, and it’s Keynesian economics at its worst. Big government, high taxes, and run the printing press. It doesn’t work and it’s not working. They are just forcing their investors to invest in the U.S. They will not give Greece any more credit and Greece may drop out of the European Union - just another uncertainty facing U.S. investors and adding to our market volatility.

Old timers like to say the market likes to climb a “wall of worry”. By that measurement this market has further to go.

**Random Thought for February 2015:** “Never be afraid to try something new. Remember that a lone amateur built the Ark. A large group of professionals built the Titanic.”

Dave Barry, Humorist



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