THE DANA VIEWPOINT

October 16, 2014
Dow: 16,376

LOOKING FOR MR. GOODBOTTOM

Wow! What a week. The stock market (as measured by the Dow Jones Industrial Average) was up 270 points, then down 300 points, then up 200 and down 450 points on an intra-day basis and finally settled down. We are 5½ years into the bull market that started in March of 2009. Investors had become complacent with the low volatility ascent of stock prices that have seen the market advance over 100%. There have been plenty of headwinds along the way – the herky-jerky implementation of the Affordable Care Act, numerous failed government programs and onerous regulations to name a few. Investors were somewhat cautious but kept buying stocks as there were few attractive options. We know that the economy is in a slow growth mode. We know that Europe may be facing a recession. We know about the turmoil in the Middle East and the Ukraine. The market has absorbed all these headwinds. So maybe it is the Ebola danger that was the straw that broke the camel's back. In any event, the stock market was due for a rest.

So what now? The market is only down about 8% from its all-time high. It just seems like more because we are dealing with bigger numbers (450 points is a big number). Investors seem to have forgotten the 40% drop in 1973-74 or the 40% two day drop in September 1987 or the huge drop in technology stocks in 2000 or the recent 50% correction in 2008-09. An 8% drop in stock prices now pales in comparison. The elusive 10% correction that many traders have been looking for is in sight, but you can bet most traders are not looking to buy this dip but are wondering how they can get out. That's just the psychology that makes markets fluctuate. So where is the good bottom? The Dow is currently trying to make a stand at 16,000 (that's about 8%). A 10% correction would take us to 15,500, but real technical support would come in at 15,000. This is not a prediction. No one knows where the bottom is. There is an old Wall Street axiom that states - never try to catch a falling safe. It's better to let it bounce a few times. The market will resume its uptrend when all the sellers are gone - just like in previous market declines.

The media is doing its part. As usual, they tend to blow things out of proportion. Not to downplay the seriousness of Ebola, but the media would have you think America will come to a standstill. People will stop traveling , especially in airplanes. Airlines will suffer enormous losses. The economy will experience contractions that will spill over into other industries. It's happened before. During the oil crisis in the mid-70s the fear was people would stop driving which would hurt the auto industry. That spilled over into thinking people would stop driving to the fast food places and on and on. Any effects at this point will be temporary. You may see many people, especially on airlines, wearing surgical masks. However, this is

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America, not West Africa. We have far superior medical advancements and medical care institutions.

The stock market was not the only investment area experiencing volatility. The bond market went on a wild ride also. Two weeks ago the ten year Treasury bond was yielding about 2.5%. This week the yield dipped below 2.0% briefly and is currently about 2.1%. As bond prices move inversely to bond yields, investors saw Treasury prices get a lot more expensive.

QE-4 anyone? You can expect the Fed to be making some comments about remaining accommodative and standing ready to act (read print more money and keep interest rates low). The Fed should just stand back for once and let the markets sort this out. Any well-meaning interference will do more harm than good.

And speaking of the Fed, Chairwoman Janet Yellen has come up with a new index to measure the growth of our economy. It's the LMCI-Labor Market Condition Index. It is a combination of the nineteen economic indicators that Ms. Yellen keeps on her "dashboard." This index will be released to the public on the first business day following the monthly employment report. This should be fun. We will need time to see a pattern develop.

In the meantime, stay cool, don't make any rash decisions and stay with the investment strategy that got you this far.

Random Thought for October 2014: "True genius resides in the capacity for evaluation of uncertain, hazardous and conflicting information."

Winston Churchill

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