THE DANA VIEWPOINT

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Dow: 17,481

The Two Faces of Fear

Central banks and governments around the world just will not give up on monetary policies in an attempt to stimulate economic growth. Some countries are still using quantitative easing and low interest rates which have not really shown much success even here in the U.S. Our economy is growing faster than most of the rest of the world, averaging about 2% since the recession ended in June 2009. That’s not rapid growth compared to previous recoveries since World War II. Nevertheless, it has been enough to push the stock market higher for the last seven calendar years, as the Dow Jones Industrial Average reached its all-time high in May 2015 at about 18,300. The Dow, now approaching 17,500, has two months to reach a new high for a 12 month period. The Federal Reserve is doing its part to keep the party going. While they raised the Fed Funds target rate in December a quarter of a point, the first increase in almost a decade, they left rates unchanged yesterday and lowered their expectations for future rate increases from four to two in 2016. The bond and stock markets reacted positively to the news with the Dow closing at its highest level of 2016. With the forecast for higher interest rates muted, investors continue to be forced to seek riskier assets for potentially higher returns. While high volatility has tested the fortitude of many equity investors so far in 2016, the market has been resilient and one can almost sense fear in reverse. Investors seeking higher returns realize the long term opportunity stocks can provide and are fearful they might miss the current rebound in stock prices.

Now for monetary stimulus on the international front: negative interest rates. Switzerland and Japan already have negative interest rates, and many other countries with slow or no economic growth are considering it. It has even been discussed in our country, but with the stock market recovery creating the wealth effect, that issue will be put on hold for now. Why negative interest rates? The theory is simple. Rather than pay your bank to hold your money (you would pay the bank an annual fee of $10.00 for every $1,000 they held for you with a 1% negative interest rate), you will invest your money in the stock market, a new business venture, or just

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spend it like a good consumer. To take this one step further, some countries are considering eliminating their large denomination notes. Circulation of high denomination notes has been increasing in recent years even in the U.S. With negative or even low interest rates, people are hoarding money rather than spending or investing it, and it is much easier to stockpile $100 bills in your mattress than lots of smaller denominations. It would also make for a less lumpy mattress.

It looks like Saudi Arabia's strategy may have worked. They refused, under pressure from other OPEC (Organization of Petroleum Exporting Countries) members, to reduce their oil production in order to stop the slide in the price of oil. Some analysts thought they were just trying to bankrupt American shale oil producers. Still others thought they intended to inflict pain on Iran just as sanctions were being lifted. Regardless of why, it has been effective. There are many bankruptcies in the oil patch and other companies are just shutting down. With oil prices recently around $30 a barrel, it's tough for most drillers to make a profit. But guess what? By not cutting their production, the Saudis forced oil prices lower until many American oil companies cut back their production, thus gradually reducing the glut of oil on the market and pushing prices back up to about $40 a barrel. Of course, oil is a commodity and is subject to the forces of supply and demand, so oil prices still have to contend with the worldwide economic slowdown. Prices may continue to fluctuate until they reach a level where supply and demand equalize.

Random Thought for March 2016: "Atticus told me to delete the adjectives and I'd have the facts"

- Harper Lee, Author of To Kill a Mockingbird

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