September 17, 2015

11:38 AM EST

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Will They or Won't They

I truly cannot wait until September 17th at 2:01 PM. At that time, the Federal Open Market Committee, aka, the Fed, will make a decision about interest rates. I don't know anyone who isn't completely exhausted from all of the Fed talk over the past few months. It's enough already. How many times do we need to see "Countdown to the Fed Decision", "Special Report: The Fed", "Breaking News...", etc. Are there no other business stories worthy of being discussed in the media?

Here's the deal. Unlike almost every other interest rate cycle change, the odds of a rate hike on Thursday are really about 50-50. The Fed has laid the groundwork for the markets to expect a rate at some point since Ben Bernanke's famous Taper Tantrum speech more than two years ago. However, something keeps getting in the way.

Should the Fed raise short-term interest rates?

The market has already done so on the 10 year treasury note to the tune of 37%. Yes, you read that correctly. The 10 year yield has risen from 1.675% in February to 2.30% as I type this. And that's not counting the move from 1.40% back in July 2012.

Since 2008, my thesis has been and continues to be that the Fed should not raise interest rates until the other side of the next recession. This is your "typical" post-financial crisis recovery that's very uneven. It teases and tantalizes on the upside and frustrates and terrorizes on the downside. Another recession, albeit mild, is coming over the next few years. That's okay. We'll get through it. On the other side of it, our economy should get back to trend or average GDP growth, not seen since pre-2008. This could also coincide with Europe getting its fiscal act together after another sovereign debt crisis.

Anyway, I don't believe the Fed should raise rates and I will guess that they don't raise rates today. Inflation is nowhere to be found. Rumor has it that the Social Security Administration is using 0% for the 2016 COLA increase to social security benefits. Yes, I know all about the conspiracies to limit COLA increases to help the budget, but just look around you. Transitory things like energy and grains have collapsed. Wage growth is woefully pathetic. Money velocity has been in the perfect downtrend since 1998.

While the dollar has been very stable for the past six months, that comes on the heels of a 20% rally (huge in the currency market) over the prior 9 months, which can be considered a quasi-rate hike. The very dovish IMF and ECB are begging and pleading on hands and knees for Janet Yellen to leave interest rates alone. Think of all that emerging market debt denominated in dollars that has been hammered by dollar strength and will likely get much worse. Think about the currency imbalances with the dollar appreciating so mightily. A rate hike here will not be good for our struggling trading partners in Canada and Mexico.

Why raise interest rates?

I have heard some pundits use the word "credibility". The Fed needs to hike rates to either preserve or establish credibility. I am sorry, but that's idiotic and doesn't need any further rebuttal. Some believe that an unemployment rate of 5.1% represents "full" or "maximum" employment and that a rate hike is necessary to cool the jobs market. Another reason I totally dismiss as unfounded. How about the labor participation rate at 62.80%, a 38 year low?!?!

Finally, there are those who believe our economy is growing strongly enough to warrant a rate higher than 0%. To me, that argument at least has merit and I can't easily rebut it. The recovery remains uneven, but GDP is growing. I wrote a strongly worded piece after Q1 GDP printed so poorly that I totally dismiss it as yet another bad seasonal adjustment and that I thought Q2 and Q3 would print between 2% and 3%. I was wrong. It's even better. However, with that, let's not forget that wage growth remains awful and inflation is non-existent.

Interestingly, while Fed members have given speeches all over the place all year, Chair Janet Yellen has been uncharacteristically silent of late. You would think that if the Fed was about to raise rates, Yellen would be stumping with at least some trial balloons or hints. The rate hike argument has persisted for two years and without it, there hasn't been any negative consequences. Why not continue to wait...

Market Reaction to Fed Decision

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The big lingering question regarding the Fed meeting after the decision is how to properly position portfolios. If you thought it was tough to get an edge on the rate decision, the markets' reaction is even more so, which is why I would absolutely not advocate making wholesale changes ahead of the announcement. It's one thing to flip a coin on the decision, but it's a whole other thing to get the markets' reaction correct as well.

The four possible scenarios are below.

Rate hike and rally
Rate hike and decline
No hike and rally
No hike and decline

Before pondering that, I saw a few Tweets that suggested Yellen could raise rates with dovish comments or leave rates alone and offer hawkish comments. And if the Fed doesn't raise rates now, we will be having this same discussion before the December meeting. It's enough to make you head spin!

Regarding stock market reaction, the very short-term sentiment indicators still have sufficient enough pessimism to support further upside. If I had to lean, that's the direction the odds favor right now, but I certainly would not bet the farm on it. Good thing for me since I don't own a farm!

Should stocks spike higher on the news and follow through, I will view that as a selling opportunity rather than a momentum buying opportunity, which should be the minority opinion.

Upcoming Appearances

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CNBC's Squawk Box - September 30th 6:05 AM

Yahoo Finance - Live Show - September 30th Noon

Fox Business' Making Money with Charles Payne - September 30th 6:00 - 7:00 PM

You can view most of the past segments by clicking below.

Media Appearances

(http://www.investfortomorrow.com/InMedia.asp)

Investment Quotes/Adages To Live By

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"The only easy day was yesterday."

- The U.S. Marines

"When in doubt, get out!"

"If it's obvious, it's obviously wrong."
-Joe Granville

"It's ok to be wrong, but it's not ok to stay wrong."

"This time is different."

"The markets require the patience of a dozen men."
-Robert Rhea

"Luck is the residue of effort."

"The most bullish thing a market can do is go up in the face of bad news."

"The most bearish thing a market can do is go down in the face of good news."

"The market can stay irrational longer than you can stay solvent."
-John Maynard Keynes

"Government is best which governs least" - Thomas Jefferson

Inflation is the one form of taxation that can be imposed without legislation.
-Milton Friedman

"You cannot legislate the poor into freedom by legislating the wealthy out of freedom. What one person receives without working for, another person must work for without receiving. The government cannot give to anybody anything that the government does not first take from somebody else. When half of the people get the idea that they do not have to work because the other half is going to take care of them, and when the other half gets the idea that it does no good to work because somebody else is going to get what they work for,that my dear friend, is about the end of any nation. You cannot multiply wealth by dividing it." - Dr. Adrian Rogers, 1984
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"Bear markets seem to be divided into three phases: the first being the abandonment of hopes upon which the final uprush of the preceding bull market was predicted; the second, the reflection of decreased earnings power and reduction of dividends, and the third representing distressed liquidation of securities which must be sold to meet living expenses. Each of these phases seems to be divided by a secondary reaction which is often erroneously assumed to be the beginning of a bull market."
- Robert Rhea

"Free enterprise is a rough and competitive game. Nobody too big to fail. Nobody too small to succeed. It is a hell of a lot better than government control." - Ronald Reagan via Dan Kennedy

"A government big enough to give you everything you want is big enough to take everything you have." - Gerald Ford via Dan Kennedy

"The problem with socialism is that, sooner or later, you run out of other people's money." - Margaret Thatcher

"Diversification alone is no longer sufficient to temper risk... You need something more to manage risk well."
- Mohamed El-Erian

"A little bit at a time adds up to a lot in no time"

To Your Financial Success,

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