HERITAGE CAPITAL LLC

Invest for Tomorrow. Live for Today.™

While this is a longer than usual Fed update and it's without charts, I promise you that reading the whole thing will be worth your while, if even only for the entertainment.

Here we go. Cue the media's hype. "The single most important Fed meeting, perhaps of All-TIME!"

Oh brother.

Model for the Day

Let's start with the model for the day. As with every Fed statement day, 90% of the time stocks stay in a plus or minus .50% range until 2pm before the fireworks take place. With pre-market action indicating a much higher open, the opportunity is there for a momentum trade to the upside from the open until 2pm or even 4pm although I have to admit that given recent activity, I am a bit gun shy about pushing the envelope intra day. I want to give proper attribution for this Fed trend and I am pretty sure data miner extraordinaire, Rob Hanna and his supercomputers at Quantifiable Edges, shared it with me.

Panic Without a Rate Hike

Moving on to today's meeting, the market says there is a 75% chance that Jay Powell & Company raise interest rates today. Frankly, that number seems on the low side. The post-Greenspan Fed has done an incredible job of repeatedly telegraphing moves well in advance of the meeting. I think the market could panic if the Fed just stopped raising rates because stocks have fallen 13%. I think that would signal something newly ominous on their radar screen which could cause a massive move lower in stocks.

Rather, if the Fed wanted to help the markets, I think they would hike rates today and then change their commentary and remove "continued, gradual rate increases", perhaps even offering the path of one additional hike in 2019. Of course, we know that Powell et al are "data dependent", until markets seize up and them the Fed think it can rescue them.

Relentless and Unusual Selling of Stocks

It's certainly no secret that stocks have been under pressure this week, this month and this quarter. Corrections happen from time to time. Always have, always will. Stocks corrected 10%+ in Q1 2018, Q1 2016, Q3 2015, Q3 2011 and Q2 2010. They were all bull market declines that mightily shook the trees and confidence, but led to new highs.

What's different here is a few things. First, selling of this magnitude in December has only been seen one other time in history and that was 1931 as the Smoot Hawley Tariff Act was instituted. It's not exactly the greatest analog as The Great Depression was unfolding, but before you ask, NO; I do not believe we are on the precipice of anything remotely similar.

Stocks are also not only selling off on good news, something we don't often see in bull markets, but there really hasn't been a slew of bad news. Selling has been relentless since December 4 without any rally developing at all. The market is also not responding to a myriad of indicators that would ordinarily turn stocks around, whether this remains an old bull market or a nascent bear market. We will certainly see sooner than later which environment the stock market is currently in.

Recession Coming in Late 2019 to Late 2020

The economic data in the U.S. may be decelerating, but it is certainly not close to recession as many people are now forecasting based on the stock market's action. It feels like stocks are trying to say something that the majority of data are not indicating just yet. Credit card and auto delinquencies are beginning to rise and housing has weakened substantially. The job market looked to have started to roll over, but the last weekly jobless claims fell significantly. I am sticking by my call for a mild recession beginning sometime between Q3 2019 and Q3 2020.

What's a little unnerving or even puzzling is that crude oil has completely collapsed. The notion that it's just a supply glut is nonsense. Crude oil doesn't plummet 39% because there is extra supply. Sorry. That's just wrong. Now, just because crude is crashing also doesn't imply impending economic doom. We saw a similar collapse from mid 2014 to early 2016. It's something to keep an eye on.

Janet Yellen & Jay Powell Are to Blame

Let's get back to Jay Powell and the Fed. Longtime readers know that I was a very big fan of Ben Bernanke while I called Alan Greenspan the single worst Fed chair ever, or at least on par with Arthur Burns from the 1970s. I call it like I see it. For several years, I have been a very vocal critic of Yellen and Powell for trying to land a 747 on a postage stamp by raising interest rates AND selling fixed income assets, now to the tune of $600 billion a year. This is the story least argued in the media. In the history of the world, no central bank has ever had the temerity to believe it could accomplish this without consequences.

Cue our Fed with Yellen and Powell.

This group is and has been either arrogant or ignorant or both. Look, the Fed is behind 90% of the recessions. They begin a rate hike cycle and push and push until the landscape is so fertile for recession that all it takes is a little spark. They did it leading up to the financial crisis. They did it during the Dotcom burst. They did it in 1990 with the S&L Crisis and Iraqi invasion of Kuwait.

This time, the pomposity has been taken to new heights by adding the program of what's been labeled Quantitative Tightening. The Fed is now selling the securities in the open market that they purchased during Quantitative Easing. These sales are effectively interest rate hikes by themselves. The markets and economy cannot withstand the Fed conducting both.

I do find it laughably pathetic that no Fed chair ever warns of recession in advance. They ignore and deny until recession hits and then respond. However, now we have Greenspan and Yellen both forecasting gloom and doom. "Run for cover." "Crisis on the horizon." What a joke! Yellen remarked on her way out of Dodge that she didn't think we would have another financially related crisis in our lifetime. Now, all of a sudden, she sees a series of crisis.

Is this all in the name of selling books? Goosing demand for their 6 figure speeches? Or, do they really believe this, but just outright lied to the public when they were in charge? No matter how you slice it, Janet Yellen and Alan Greenspan are embarrassments.

Trump's Brilliance

I knew that headline would get you. It's not often that people label Donald Trump as brilliant, but I am going to in one regard. While I absolutely detest his politization of the Fed, I do think it was a brilliant strategy to lay blame and prepare the country for a scapegoat. By criticizing, admonishing and disrespecting not only the Fed, but also the guy Trump put in charge, the President has set the stage for one giant game of "I told you so" if the economy does fall into recession with stocks in a bear market in advance of the 2020 election.

By repeatedly challenging the Fed to stop raising interest rates, Trump will be able to blame Powell & Company for any and all economic issues between now and 2020. The President will campaign that he knew this was a path to disaster and he absolutely did not support higher rates. Trump will then call for Powell's replacement after Trump is reelected. And what happens if the economy does not recess? The President will smartly take credit as his policies of tax cuts and reduced regulations were so strong that they were even able to overcome horrific Fed policy.

It really is a brilliant strategy, whether intentional or not although I believe that President Trump will have other things to worry about come 2020 and the election.

To Your Financial Success,

Paul Schatz
President
Heritage Capital LLC

1 Bradley Road Suite 202
Woodbridge CT 06525

203.389.3553 Phone
203.389.3550 Fax

www.InvestForTomorrow.com

Important Disclosure Information

Heritage Capital LLC ("Heritage"") composite performance results represent time-weighted actual performance results for continuously managed Heritage accounts, which individual accounts Heritage believes to be representative of its investment management process (i.e. mutual funds and exchange traded funds) for each specific strategy during the corresponding time period. The composite performance results reflect the reinvestment of dividends and other account earnings, and are net of applicable account transaction and custodial charges, and the separate fees assessed directly by each unaffiliated mutual fund and exchange traded fund holding that comprised each account, and the maximum investment advisory fee that the accounts would have incurred (by applying the Heritage's current investment advisory fee of 2.00% as set forth in its current written disclosure statement) during the corresponding time periods.

Please Note: Past performance may not be indicative of future results. Therefore, no current or prospective client should assume that future performance will be profitable, equal the performance results reflected, or equal any corresponding historical benchmark index. The historical index performance results for all historical benchmark indices do not reflect the deduction of transaction and custodial charges, or the deduction of an investment management fee, the incurrence of which would have the effect of decreasing indicated historical performance results. The historical performance results for all indices are provided exclusively for comparison purposes only, so as to provide general comparative information to assist an individual client or prospective client in determining whether the performance of a Heritage program meets, or continues to meet, his/her investment objective(s). A corresponding description of each index is available from Heritage upon request. It should not be assumed that Heritage account holdings will correspond directly to any such comparative benchmark index. The Heritage performance results do not reflect the impact of taxes.

For reasons including variances in the investment management fee incurred, market fluctuation, the date on which a client engaged Heritage's investment management services, and any account contributions or withdrawals, the performance of a specific Heritage client's account may have varied substantially from the indicated portfolio performance results.

In the event that there has been a change in a client's investment objectives or financial situation, he/she/it is encouraged to advise Heritage immediately. Different types of investments and/or investment strategies involve varying levels of risk, and there can be no assurance that any specific investment or investment strategy (including the investments purchased and/or investment strategies devised or undertaken by Heritage) will be profitable.

Information pertaining to Heritage's advisory operations, services, and fees is set forth in Heritage's current disclosure statement, a copy of which is available from Heritage upon request Performance results have been compiled solely by Heritage, are unaudited, and have not been independently verified. Heritage maintains all information supporting the performance results in accordance with regulatory requirements.