GETAnalysis RESEARCH

July 13, 2013

Federal Reserve Backs Down – Stock Markets Jump! & Then Flinch

WRITTEN BY: ASHOK DHILLON

Ashok Dhillon has 40 years of front-line business experience in Canada and International markets. He incorporated his first construction company in 1974, and since then has founded and led companies in construction and international power development.

Over the last 20 years Mr. Dhillon, has led and worked with top Canadian talent in the legal, engineering and accounting firms, such as Fasken Martineau, Russell & DuMullen, Stikeman Elliott; Hatch, Moneco Agra, New Brunswick Power, SNC Lavalin; and Ernst & Young, Arthur Anderson, and Grant Thornton. And in London, worked with Perkins Couie and Morgan Grenfell. Mr. Dhillon's companies have partnered and worked with Pan Canadian Oil & Gas, WestCoast Energy, TransCanada Pipelines, and international companies such as AES, Enron Power, Hyundai Heavy Industries.

Mr. Dhillon has worked and negotiated with highest levels of Governments in Canada and India. He has pursued and won mandates to develop power plants in Canada, and foreign jurisdictions such as Hungary, Iran, Pakistan and India with uncompromising ethical standards. His extensive experience in securing and negotiating multi-hundred million and billion dollar mandates in power project development, gives him in-depth knowledge and intuitive insights into macro and micro, national and international, geo-political and economic realities and trends.

Mr. Dhillon has been invited to speak on international business at various forums, including as an expert witness for the Standing Senate Committee, Government of Canada, on "The Rise of Russia, China and India".

Federal Reserve Chairman Ben Bernanke did exactly what we had written about a few days ago. He came on and took the pains to reinforce the inversion of economic fundamentals by backing away from the tapering. Even though a gradual tapering starting this fall would have been prudent and based on the current U.S. economic reality, instead his resolve to do the right thing buckled in the face of the power of the stock markets and its players. By reassuring everyone that the taps of easy cash would remain open indefinitely, he contributed to widening the gap between global fundamental economic realities, and the continuing asset market speculation.

Upon being reassured by the most powerful Central Banker, that the party isn't going to be over anytime soon, the markets jumped, and just about every asset class gained, contributing to the New York Stock Exchange setting another record high yesterday. Talk about irrational exuberance!! The fact that the economic realities have not changed a bit didn't bother the stock markets as they have been detached from economic reality for some time now. The unabated torrent of money gushing from the Federal Reserve and the other Central Banks into the global financial system is continuously boosting the asset markets and skewing fundamental economic realities, thereby adding to risks inherent in such markets.

That torrent of liquidity so power-boosting the markets has been a mere trickle to the underlying economies. This trickling effect is reflected in the daily signs of national and global economic weakness, the anemic job creation numbers and ironically, the justification for continuing stimulus requirement. In some economies the weakness is of a 'critical-condition' kind, and the joblessness numbers are of such levels that in 'normal' times they would be unthinkable. Therefore considering the fact that in 5 years of unprecedented stimulus spending by the global central bankers, there being such little effect on the 'Main Street' economy, why a better stimulus model, such as direct investment in infrastructure and industry building isn't adopted, as after the 'Great Depression'. And after all, China, for decades achieved double digit growth through direct infrastructure investment, rather than bond purchases.

The stimulus model being used by the Western bankers is stoking fast rising asset bubbles rather than fostering strong economic growth. For that reason the frustration of the general public in most countries is mounting, as they watch helplessly from the sidelines, those who had crashed the financial system, and brought on the seeming endless global economic recession, once again gain the control of the leavers of endless cash and easy profits, while the public continues to struggle, are threatened with additional belt tightening and reduction of services in the name of needed austerity. Banks and markets are flooded with endless printed cash for 'as long as needed', and as markets soar the economies continue to scrape the bottom, struggling to maintain questionable gains, and inflicting fear and pain on the populations in the both the developed and emerging economies.

As we said in our last post, the fundamental laws cannot be flaunted or broken for an indeterminate period of time before a violent natural reaction takes place to right the imbalance. It's natural for the stock markets to anticipate and reflect the economic conditions, 6 to 9 months prior to them occurring, that market behavior is historic and well documented. But the current market action is not predicting economic performance 6 to 9 months from now, it is being driven solely by the Central Bank largess, which hasn't till now and cannot possibly in the coming 6 to 9 month period boost economic growth enough, to justify the almost consistent 'record setting' new market highs.

Therefore with the active indulgence of the Federal Reserve and the Central Banks, the imbalance in our economic universe continues to build, and corrective reaction when it takes place, will of necessity be reflective of the magnitude of the imbalance.