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New Order Polemic

Sometimes, any theory which espouses spontaneous, random market behavior gets put to the test. Conversely, it is my belief, and my science, that markets, while certainly influenced by exogenous and disparate events, are not random at all, but rather quantifiable and somewhat predictable.

The past two years have certainly been a statistical aberration to that notion, but not in any way un-measurable or undefined.

While the *supply* side of the economy has been expanding, the *demand* curve has been quite restrained. As a result, spontaneous discretionary spending behaviors have largely been imperceptible. Despite heavy influences and persuasions from monetary and fiscal authorities, consumer spending has been a bore, and not consistent with producing the kind of vibrancy and enthusiasm that austerity and cheap money policies might usually expect as their legacy. Incentives are only as good as the value people place upon them, and in this instance discretionary spending has not been inspired.

"Free money" and the "free market" are not free. Nor have they been the progenitors of wealth-building we might have expected to see as an outcome emerging from this past recession.

Instead, the markets are hung up on creating capital gains at any cost... layoffs, accounting engineering, and budget cuts, for example. This obsession has set the stage for a continuous downward trajectory in the standard of living for the less-affluent, diminished expectations for their heirs, and created a kind of disposable underclass of citizens, goods, and services. Profit at any cost, indeed *has* a cost.

I would argue that the stock market's recent success induces repeatable, oftentimes vile, outcomes such as class warfare and structurally inefficient production. Witness, for example, the glut in oil production worldwide or the housing boom several years back. We are simply obsessed with making more, of anything, simply because we can. If it seems "normal" that we just indiscriminately discard those who fall short, or can't or won't participate in the global marketplace, then maybe we have to look at our own value systems and ask *"at what point are we creating too much stuff?"*

A fair race is not necessarily where the winner is the fastest. It is one in which everyone follows the same rules for getting to and finishing the race.

While it is entirely appropriate that subjective evaluation of success is different for everyone, our greatest contribution to the planet would be to ensure that no one voice or special interest represents a greater value than any other.

Markets

Today, a significant percentage of the globe finds itself beset by problems and internal conflicts that have a direct bearing upon the well-being of its citizens. Guns and revolutions are not the things we have in mind when we think about economics, free markets, and providing our platform with comfort and opportunity. In fact, because of the burden placed upon governments by war and terrorism, global production capacity has become terribly skewed.

Demagogues and dictators who promise religious salvation, or jobs, or panaceas for poverty are only using the "rest of the world" as scapegoats. But rather than increasing the production schedules of their populations, the unequivocal net effect has been to stifle GDP. Thus, selected regions of our planet are running behind schedule in providing education, healthcare, housing, food, quality of life, and peace of mind to their citizens.

Even as the global recovery accelerates, the rewards have mostly been heaped upon a select few. While the private sector has effectively been able to manage its budgets, the public sector has become gridlocked by austerity, ideology, and plain old politics. It was praiseworthy that we were able to avert a global banking collapse in 2007-2008, but today we find that those institutions that survived the crisis seem somehow unwilling or unable to reinvest and/or lend their capital. They don't realize that they not only are the holders of our money, but they also hold the key to our expectations and aspirations for a better future.

The retention of money by the banks costs the economy by limiting projects and hope. Their failure to take a longer term perspective of risk is sullied by the follies of their previous lending practices, thus ruining the velocity of what could be a faster moving economy. Because of them, the rest of us are partially stymied by policies (fiscal and monetary) that are short sighted and apprehensive. Watching the "experts" be tight with their money also influences our spending habits. Heck, if they are going to be frugal, so then should we. And despite fancy banners and balloons at the local bank, no matter how inexpensive it is to borrow money, you can lead this horse to water, but you can't make him *spend!!*

A massive redistribution of wealth is occurring right in front of us, but not the kind which forewarns of gloom and doom. Money localizes with money, making the capitalists feel better about themselves and the things they possess. However, the stage is being set for a change in our social contract because many people are not having their basic needs met, and that could seriously impede the global recovery.

When this condition exists, as indeed it has during other periods in our history, political discourse becomes more harsh, less compassionate. "*Aren't we, after all, responsible only for ourselves?*", say many of us. Ethics have become disposable in this survival climate. Bureaucrats argue for "local" needs, *against* an altruistic mindset which seeks common ground for everyone. Certain belongings are becoming more expensive because things are hoarded and more closely held, and in the case of commodities, more difficult to find and depleting in quantities.

While it is certainly advisable always to be biased against profligate spending, limitations upon civic spending can only be supported if those limitations lead to responsible allocations of law and order, food, and the common good. A balanced budget is always preferable to taking on debt, but alleviating chaos by being creative and proactive on behalf of citizens is preferable even more.

Summary

How come so many of the world's stock markets have been doing so well in the face of such underwhelming confidence and limited breadth of participation? Are bull markets impervious to fundamental inconsistencies, full speed ahead always?

The answer might lie in the temporary displacement of the bond market because of low interest rates. Professional investors and traders are the embodiment of a narcissism that believes that traditional investment in energy, infrastructure, emerging markets and business formation are less desirable than a reasonable rate of return and collecting "unrealized" portfolio gains. They appear to worry less about the rest of us...the environment, energy alternatives, agricultural shortfalls, global disease pandemics, housing and homelessness....than making sure that their stakeholders are rewarded with fatter portfolios.

All the while, stocks have proven them correct as a suitable alternative to capital spending. There really is no other game to play.

There is no end in sight to this "paper profit" mentality, either. My measurements show an array of sectors not yet having participated in the capital gains bonanza. Because we know that there will always be "rotation" in the markets from productive sectors reaching full potential back into the laggards, we can quantify the flow of funds and anticipate the valuation potential of the markets. Absent a suitable alternative in bonds, investors are likely to stick around a bit longer in the stock market.

During the next few months, the relative performance of equities is less likely to be influenced by long term objectives, remaining mostly oriented towards immediate and quicker capital appreciation with relatively little drawdown. A return to long term demographic "theme" investing is difficult to sustain in an environment of hysteria and hyperbole.

More significant, though, would be to see a recognition of moral and ethical responsibility between the markets, investors, and their community. That kind of seismic shift would resonate with the public, and help to create dialogues that might provide solutions to economic and social problems which heretofore have been thwarted by the basest of human behaviors.

Suggested Balanced Account Asset Allocation Q2, 2015:

Equities: 65%
Fixed Income: 15%
Cash: 20%

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