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SIGNS OF THE TIMES:

Last Year:

"This is why I moved quickly on an American recovery and reinvestment plan that will immediately jump start job creation and growth."

– Wall Street Journal, January 2009

Then when it was uncertain if the ***"green shoots"*** were hooking up Obama stated the Recovery Act ***"wasn't designed to work in only four months...It was designed to work over two years."***

– Quote from Bloomberg, July 11, 2009

At the recent G20 confab Obama pleaded for yet more "stimulus", but as the world is discovering interventionists will continue to spend other peoples' money until it is all gone.

Our view has been that the huge intrusion into the financial markets added some six months to the enthusiastic rebound consequent to a classic crash.[1] This seems to have recorded an important top in late April.

In a July column last year, Pat Buchanan wrote:

"In the Declaration of Independence, Thomas Jefferson called George III a tyrant for having 'erected a multitude of new offices, and sent thither swarms of officers to harass our people and eat out their substance'."

Sadly, it seems that President Obama is out to turn Independence Day into Dependents' Day.

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This Year:

"RBS tells clients to prepare for 'monster' money-printing by the Federal Reserve."

– Telegraph, June 27, 2010

[1] Should any investment intellectuals read this – a financial crash is a "Minsky Moment".

"As Confidence Erodes, Earnings Give New Hope"

"Analysts Maintain Faith in Profits"

– Financial Post, July 6, 2010

Perhaps this suggests a new buzz phrase for Wall Street economists – "A profitable post-bubble contraction".

"Insatiable Energy Demand"

– New York Times News Service, July 6, 2010

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STOCK MARKETS

On the near term, a brief relief rally has been likely to run into next week. However, this action is part of a stair-step decline following a very significant top in April.

The latter accomplished the "Rolling Top" that Ross was looking for and our April 22 edition reviewed our **Checklist For A Top**. This included ***"Is it up when it should be?"***, ***"Are there signs of excess?"*** and ***"How sound is the fundamental story?***.

The answers were ***"Yes!"***, ***"Yes!"*** and that the "story" was that Keynesian stimulus had prevented Depression 2.0. On the second "Yes", there were many indicators with the most blatant being the Nasdaq reaching the greatest overbought since 2000, which was a fateful year.

The 2007 top was even more fateful. On most recessions the high in the stock market leads the high in the economy by around 12 months. In so many words, the cycle for share certificates leads the cycle for business activity.

But, at the end of a great financial bubble the pattern is critically different. Essentially, the stock market and the economy peak at the same time. On the four bubbles from 1720 to 1825 the evidence is informal, but since the 1873 example the NBER has determined the troughs and peaks of the U.S. business cycle.

The greatest financial mania in a generation blew out in September of 1873. The NBER determined that the recession started in that October. In 1884 leading economists began to describe the long contraction as the "Great Depression". This was likely the first usage of the term. It lasted until the business-cycle low in 1895. Ironically, this was analyzed as such until as late as 1940.

On the next example, the stock market peaked in September 1929 and the recession began in that August.

On our example, the stock market set its high in late October, 2007 and the NBER set the start of the initial recession in that fateful December.

Using this history as a guide, rather than the imaginations of interventionists, one would conclude that the business rebound that accompanied the natural rebound out of a crash would fade as the stock market rolled over.

May recorded the sharpest decline for that month since 1940, credit markets also took a hit and some orthodox economic reports have beat street estimates – on the downside. Levente's BondWorks on Monday provided a good review.

Technically, the ChartWorks had the last rally target at 1133 on the S&P and 1131 was reached. Then taking out 1040 would formally set the downtrend. The low at the 1011 level on Bleak Tuesday accomplished this and once this week's bounce is over the decline should resume.

The next target is last summer's correction low at the 890 level. Major support is at the March 2009 low of 666 and there are some reasons why such a low is possible.

Ross's "Presidential Model" for this year called for a high in late spring and a significant low later in the year.

A very long term approach notes that every great financial mania has been followed by a long contraction that can prompt massive political change. As individuals have to "tighten their belts" they will look at the extravagance at all levels of government and will force austerity upon all levels of government.

The next phase of the contraction will reveal that there is no amount of stimulus that can overwhelm a post-bubble revulsion for most forms of credit. Particularly the usual innovations in credit. This time around the feature of the "new era" has been derivatives.

The next few months will be interesting – especially as the establishment discovers that their theories and practices have been futile. Some may despair, others will claim that government agencies needed to be bigger and smarter.

At that point interventionist economists will be caught between a crock and a hard place.

Other Considerations

Three weeks ago we noted that the Baltic (BDI) was close to breaking down. It has, and it continues its plunge, suggesting that international trade in dry freight is slowing.

The high was 4209 on May 26 and at 2018 the slump now amounts to 52 percent. What's worse is that the plunge has been accomplished without even one day of rest or uptick. That is 29 consecutive trading days.

A severe, but not as relentless, plunge from the high in May 2008 gave us an alert that summer to the fall crash. Or in more polite terms – the Minsky Moment.

The conclusions to great financial manias have been methodical with the key signal provided by the reversal in spreads and the curve, to mention only a couple of items. The initial stock market crashes have also been methodical and include an important distinction.

This is outlined on the front page and that is at the end of a bubble the recession starts virtually with the bear market. This was the case in 2007, and now that the stock markets have turned down this should be accompanied by a down turn in business activity. This is happening and the crash in the Baltic is providing dramatic confirmation.

Wall Street pundits are again discussing the "Double Dip" outlook for the economy, but looking over our shoulder we see that the recession started on schedule in December 2007 and it is doubtful that the NBER can conclude that it has ended.

In which case the first post-bubble recession continues.

Recent financial events have turned our overall view to cautiously pessimistic.

Link to July 9, 2010 'Bob and Phil Show' on Howestreet.com:

http://www.howestreet.com/index.php?pl=/goldradio/index.php/mediaplayer/1704

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