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WEALTH MANAGEMENT

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Questionable Statistics

Examining historical data can be useful in discovering trends.

When past information is collected and compared with more recent information, the differences may, or may not, lead to insights regarding the change of underlying conditions.

For example, comparing auto mileage and prices of cars from the 1970's to those of today may exactly have little relevance because the technological changes and capabilities are too different to be meaningful.

Commonalities like correlation do not necessarily indicate causality.

As of the end of 2022, the 'Superbowl Indicator', which suggests that a NFC victory in the Superbowl predicts a positive S&P 500 Index for the year, has been correct 73% of the time over the last 45 years. [1]

Virtually no one really thinks there is a causal relationship between the Superbowl and the S&P 500, but the result is frequently mentioned in the press near game time.

New and different outcomes can emerge from similar data, or different outcomes from dissimilar data that is incorrectly assumed to be the same. Sometimes this is because the differences have been overlooked due to the use of 'pruning algorithms' where leaving out what we think is 'irrelevant data' might lead us to errors in forecasting.

Mark Twain's saying that, "It's not what we don't know that gets us in trouble. It's what we know for sure that just ain't so." [2]

Among my favorite things that we know ‘for sure’, but may not be true are:

> The Home-Owner Equivalent Rent, this statistic is a 35% determinant of the shelter component of CPI ---The Bureau of Labor Statistics surveys homeowners each month and inquires at what price they would rent their current residence. Since 65% of homes are owned by people either outright or with mortgages, their opinion wouldn’t have any effect on their own housing cost or on the housing cost of anyone else, yet it is widely quoted. [3]
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> Another is the currently well accepted thought (slightly less well accepted since the FOMC meeting of Jan. 31, 2024) is that Federal Reserve Open Market Committee will cut the fed funds rate several times in 2024 as a confirmation that their inflation reduction policies have worked. [4]

The Fed’s mandate from congress is to maintain stable prices and full employment. An interest rate cut in the Fed Funds rate could have the opposite effect—stimulating the economy and increasing inflation. [5]

Creating or even simply promoting a strong economy is not part of the Fed’s mandate. The Fed was set up in 1913 to be the country’s ‘lender of last resort’ in an effort to minimize the destructive crashes and recessions that occurred frequently in the early industrial age due to, some think, the illiquidity caused by the raising of capital to bring in the harvest.

Despite the guesses of the TV commentators about how many cuts the fed will enact this year, the answer may be none or few.

If we have slowly declining inflation, still above their target of 2%, there may be no need to do any further tightening, but also no immediate loosening.

We continue to look to invest in companies that can prosper and thrive in an environment of stable, low, but non-zero interest rates as we have in the past.

In our view, we are returning to normal. It has been fifteen years since 2008 when former Fed Chair Bernanke rescued the mortgage bond market with zero interest rate policies. We don’t think this will be repeated. In our opinion, a normal interest rate is a 10-year U.S. Treasury yield of 5% to 6% where it has been historically for most of the last 100 years.

We are also of the opinion, that investing in individual companies and their equities continue to offer opportunity in this environment.

Please call to discuss examples that may fit your individual objectives.

Sincerely,

James P Dretler
Senior Portfolio Management Director
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1. James Chen, ‘Super Bowl Indicator: Premise and History’, https://www.investopedia.com/terms/s/superbowlindicator.asp#:~:text=The Super Bowl Indicator is an example of purely fun,
2. Think Independent, Mark Twain ‘It ain’t what you don’t know that gets you into trouble, https://www.thinkindependent.com.au>aint-dont-kno
3. U.S. Bureau of Labor Statistics,‘Measuring Price Change in the CPI: Rent and Rental Equivalence’, bls.gov/cpi/factsheets/owners-equivalent-rent-and-rent.htm
4. ‘Stocks End Lower After Fed Signals Rate Cuts Not Imminent’, Wall Street Journal, https://www.wsj.com>livecoverage>fed-meeting-fomc-interest-rate-january-2024
5. ‘Breaking Down the Federal Reserve’s Dual Mandate’, Investopedia, https://www.investopedia.com>Federal Reserve

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