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First Trust

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Monday Morning Outlook

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Easy Money Will End Recession

The Federal Reserve is following possibly the most accommodative monetary policy of its 96-year history. The economy and stock market are floating on a sea of liquidity. That's all that really matters right now.

Through Friday, this sea of liquidity had lifted the Dow Jones Industrial Average by 22.5% in less than a month, with the NASDAQ up 27.8%, and the S&P 500 up 24.5%.

For us, this is the real deal. But pessimism is so rampant that it is hard for many investors to believe that this rally can last. When it was reported last Friday that the US lost 663,000 jobs in March, it was almost too much for many investors to take. Since December 2007, the US has lost 5.1 million jobs. These job losses have pushed the unemployment rate up from 4.9% to 8.5% - the highest rate since 1983.

These horrible jobs data have many asking: How can any kind of economic recovery take hold? How can stock prices continue to rise? The thinking is that with people losing jobs, spending will fall, which will lower production causing more layoffs, sending the economy down again.

But this is not the way the economy works. If jobs were the catalyst for all economic change, then the economy would never stop expanding if jobs increased; nor would it ever stop contracting when jobs fell.

Don't take this as a sign that we do not care about job losses – they hurt. They are personal. And when unemployment rises above 7% or so, just about everyone knows someone who has lost a job. But, in the past, the unemployment rate has been much higher than it is today and yet the economy recovered and the stock market boomed anyway. Unemployment is a lagging indicator.

In fact, the best historical precedent for what the US economy is living through today is the mid-1970s. Between December 1973 and May 1975, the unemployment rate jumped from 4.9% to 9.0%. This recession included a 43% drop in the S&P 500 during the bear market of 1973-1974.

But the stock market bottomed in December 1974, and even though the unemployment rate increased from 7.2% to 9.0% in the first five months of 1975, the S&P 500 jumped 34%.

The major factor behind all that volatility in the economy and the stock market was the Federal Reserve's monetary policy. The Fed hiked the federal funds rate from 3.3% in early 1972 to 12.9% in July 1974. Then, the Fed reversed course and cut the funds rate to 5.2% by May 1975. This rollercoaster monetary policy caused a bust and then a boom.

While the current recession was not caused by excessively tight money, it is very clear that with the federal funds rate near 0%, monetary policy is extremely easy. Money supply measures are surging – in the past six months, M1 is up 25.2% at an annual rate, currency outstanding is up 15.4%, checking account balances are up 74.2%, and M2 is up 15.9%. To top this off, the Fed has announced a $1 trillion plan to basically print money and buy assets including treasury bonds.

There is an old investor saying – "Don't Fight the Fed," and today is clearly a time that we should take heed of our forefathers' advice. This sea of money is impossible for the economy to ignore.

Home sales, retail sales, auto sales, oil and other commodity prices, the CPI, the PPI, the Baltic Freight Index, and the stock market are all signaling that this money is working its magic. It takes about six months, but when the Fed injects money into the economy, spending increases. It always works. And this time, there is also a rebound in velocity taking place at the same time.

The end result is that the stock market and the economy are being lifted on a sea of liquidity. A V-shaped recovery. Very soon, the recession will officially end. This is not a dead cat bounce, and it's not government spending. It's easy money, plain and simple.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-7 / 2:00 pm	Consumer Credit - Feb	-$3.0 Bil	**-$4.2 Bil**		$1.8 Bil
4-9 / 7:30 am	Int'l Trade Balance - Feb	-$36.0 Bil	**-$37.6 Bil**		-$36.0 Bil
7:30 am	Import Prices - Mar	+0.9%	**+2.3%**		-0.2%
7:30 am	Export Prices - Mar	+0.0%	**+0.4%**		-0.1%
7:30 am	Initial Claims - Apr 4	660K	**663K**		669K
4-10 / 1:00 pm	Treasury Budget - Mar	-$150.0 Bil	**-$151.4 Bil**		-$192.8 Bil