Access Investment Advisors Inc.
4400 Calumet Avenue, Suite 201
PO Box 697
Manitowoc, WI
54221-0697

920.683.9901
FAX: 262.364.2147
www.accessinvestmentadvisors.com

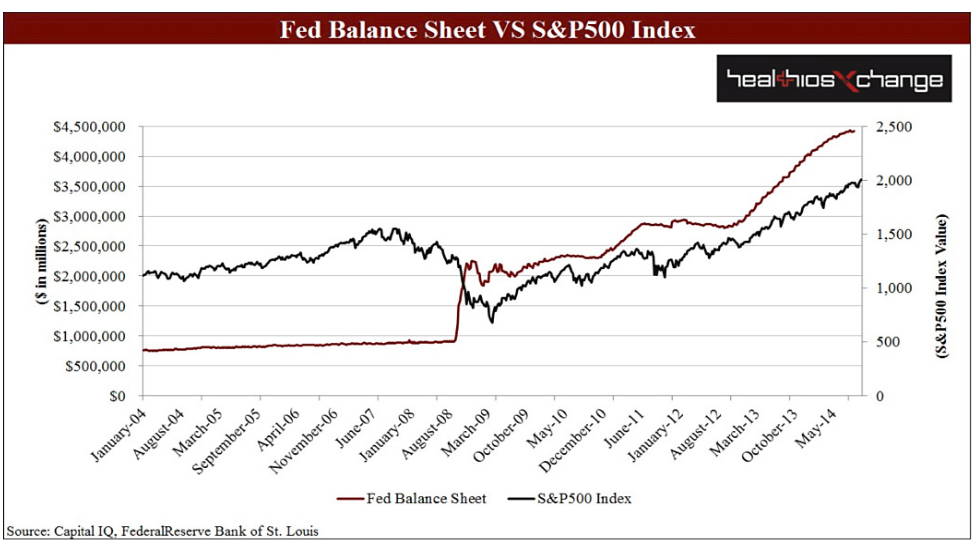
October 2014

The Great and Powerful OZ

"Force is all-conquering, but its victories are short-lived" – Abraham Lincoln

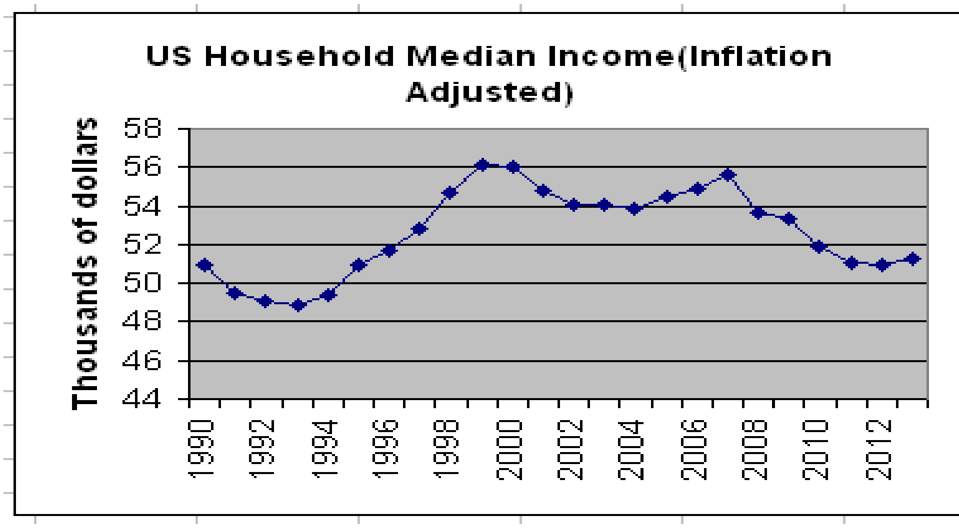
The above quotation has been widely credited to Abraham Lincoln, but there is some dispute as to whether he actually said it. Notwithstanding who said it, attempting to change an outcome by using overwhelming pressure may work in the short run, but odds are it won't last. Anyone who has had children, or has been around them for any length of time, recognizes the futility of attempting to change behavior by force. There may be some temporary adjustment, but unless the child can see the ultimate benefit of making the change (other than avoiding another 10 whacks with the hairbrush) it is unlikely that the desired change will stick.

Not that financial markets are like children (wait a minute), but the same principal is involved when attempting to manipulate them. Below is a chart of the Federal Reserve Balance Sheet (brown line) graphed against the S&P 500 (black line). Up until 2008, the "Fed" had pursued a relatively neutral policy of credit expansion. In 2008 all of that changed. Believing that swift and significant action (force) was necessary, the Fed stepped in and began policies designed to aggressively lower interest rates and expand available credit. Notice the reaction of the financial markets to this intervention since that time. There is a 90% correlation between the Fed's activity and the movement of the S&P 500, meaning that if you want to know how the stock market is doing, check on what the Fed's been up to.



(over)

Great you say. But affecting stock prices was not the stated objective of the Federal Reserve in pursuing this strategy. The objective was to get our economy back on track, Americans back to work, and to steer our country back on the path to prosperity. Below illustrates what the Fed is ultimately trying to influence.



This data, provided by the US Census Bureau, is rather sobering. Although the data reporting time lags about 12 months, it is clear that the average American family is no better off economically today than it was back in the late 90's. People certainly have their own opinions as to why this is the case, but the fact that it is happening is undeniable. The Fed is pushing on a lever (forcefully) hoping that this lever will pull on other parts of the economy. Ironically though, the only substantial result of this effort has been to re-inflate prices in the same assets that Alan Greenspan (then Federal Reserve chairman) spoke about when he uttered the now somewhat famous phrase "irrational exuberance", to describe bloated prices of stocks, bonds and real estate.

Given the state of household incomes, it comes as no surprise that in an August Wall Street Journal/NBC Poll 64% of respondents were "Dissatisfied" with the state of the economy against 35% that were "Satisfied". The same group was asked if they thought that life for their children's generation would be better than it had been for them. A record 76% did not believe that it would be better (when asked in 2007, the number was 60%).

It remains to be seen whether the efforts of the Federal Reserve will have a lasting, positive impact on the US economy. Thus far the Fed can point to its successful campaign to keep interest rates (artificially) low and asset prices (artificially) high. Its most recent former chief, Ben Bernanke, asserts that without the Fed's intervention the recession would have been much worse (a conveniently unprovable proclamation). What is clear is that financial markets are not trading on fundamentals or free market dynamics, but rather artificial forces propagated by Federal Reserve policies both here in the US and abroad. When this force is removed, it will likely be Janet Yellen exhorting us to "pay no attention to that (wo)man behind the curtain".