TOCQUEVILLE

Sell The Rumor, Buy The News

BY ROBERT KLEINSCHMIDT ON *JUNE 17, 2015*

Investors have been selling the rumors lately, inverting the old adage. Rumors of a Greek default and a Fed rate hike have sent investors panicking for the nearest exits. But, will they buy the news? Who knows, but they should.

I cannot think of two better advertised negative events than these, all the more so for their triviality. Greece is a country that peaked around 400 B.C. and is of no economic importance, even to Europe, much less the world. On top of which, Greece has already defaulted more than five years ago. Neither the word “default” nor the word “bankrupt” have the slightest bit of meaning if they can be neutered merely by someone providing more loans to repay the existing ones. Indeed, a recognized Greek default might even have the salutary effect of alerting governments of the need to tailor fiscal policies so that spending and revenues bear some relationship to each other. If European—and U.S. and Japanese– governments could learn THAT, a Greek default should qualify for the Nobel Prize for Economics.

As for a rate hike, bring it on! No rate hike is worth the agonizing that the markets have witnessed over the past several months, particularly one that takes the Fed Funds rate from zero to twenty five bps.

A hike of this magnitude is not even a rounding error and should make no difference whatsoever to the few borrowers in corporate America waiting on a loan. As for mortgage rates, they are so low by any historical standards, that a modest bump in the Fed Funds rates will still leave them near record lows.

It is true that labor force participation rates remain low and wage growth continues to stagnate. It is also true that despite a big break to consumers in the form of lower gasoline prices, discretionary spending has continued to languish. But in my opinion, the reasons for its languishing have little to do with interest rates. Yet unemployment is below 6% and housing starts continue to improve, while permits for future home construction are at their highest levels since 2007. Perhaps more importantly, any risk of a meager hike sending the economy into a tailspin has to be weighed against the highly distortive effects of such a prolonged easy money policy and the systematic risks it could be creating.

Eventually, training wheels do more harm than good. The status quo, in Europe and at the Fed, I believe, has stopped having the desired effect and it is time to move on, free from the fear of illusory calamities. The real catastrophic events are the ones you never see coming. These two have been visibly coming for far too long. Better to put them in the rear view mirror. And buy the news.

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