Economic Update

Broadleaf Partners, LLC

Bear Market Bubbles

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New unemployment claims came in at 345,000 this morning. The bad news is that 345,000 more people lost their jobs, but the good news is that there has been a clear inflection point in the rate of change. A couple of months ago, new claims peaked at over 600,000. Many forecasters expected this morning's number to come in at around 500,000.

The unemployment rate, on the other hand, continues to increase, hitting 9.4%, the highest levels since the early 80's. Historically, the unemployment rate has been a lagging indicator, often increasing for 6-9 months after a recession is officially over. This means that you can still be bullish about the stock market even though the unemployment rate may be increasing. As we said in previous updates, the market was likely discounting an unemployment rate as high as 10% and perhaps even substantially more than that when it hit the newer lows in early March.

Stocks are quoted up this morning on this positive news. It will be interesting to see if they can hold these gains or if we'll see a bit of profit taking after such a strong run. While some consolidation wouldn't surprise us, we believe the market can make additional progress this year and think a target of 1100 on the S&P 500 remains within reach, about fifteen percent additional upside from current levels.

In the course of the last year, we've had one of the worst performing markets on record, an environment that conjured fears of a second Great Depression like no other. While the economy remains very weak, wouldn't it be amazing, if in hindsight, things really weren't so different this time?

In an era of recurring asset bubbles -- tech stocks, housing stocks, commodities -- sometimes I wonder if what we've just been through was one of the economy's first "bear" bubbles -- exaggerated prices, only in reverse this time. Investment bubbles, at their base level, are always caused by "fund flows gone wild", a term we coined to describe the bubble like action in oil and other commodities in a CNBC appearance about one year ago.

With the proliferation of readily available products and strategies that can and do short the market, it would make some sense that a "bear" bubble would be far more possible in today's investment world. Add the fact that many of the products that short the market use leverage -- sometimes 3 to 1 -- and you have a key ingredient common to asset bubbles of all types.

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In pointing out this possibility, I don't mean to minimize the carnage that has occurred in the economy -- the GDP declines in the last two quarters have been both staggering and real. At the same time it could be said that the fundamentals for technology, housing and commodity companies were quite staggering during their halcyon days. In hindsight, they didn't last.

Historically, bears have hibernated through long, cold winters, emerging from their caves during springtime well rested and skinny. Today's bears might be different. They may be very active during long, cold investment winters, gorging on the flesh of the fallen and getting fat and happy in the process.

Today's bears can be greedy. And as surely as we're human, we know how that story ends.

Kindest Regards,

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