

# Tea Leaf

...weekly since 1976

Your guide to understanding  
today's economy and  
financial markets

March 26, 2008

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## Musings

Written by Jeff Thredgold, CSP, President, Thredgold Economic Associates

This week's *Tea Leaf* is quick commentary on a laundry list of recent developments in the economy and financial markets...

### Higher Stock Prices

The sharp rise in the Dow Jones Industrial Average of the past two weeks to its highest level in nearly a month seems in response to better news emerging from Wall Street. The more aggressive posture taken by both the U.S. Treasury Department and the Federal Reserve in dealing with domestic and global credit market anxiety, as well as steps to support the beleaguered housing industry have also benefited stock prices. Numerous market forecasters are suggesting that we have seen the bottom and that now is the time to add to stock market positions...

...time will tell.

### Bear Stearns

The market collapse of this "top five" investment banking firm is another powerful lesson (like Enron) in the value of investment diversity. Bear Stearns stock traded at roughly \$160 per share in early 2007, and nearly \$80 per share earlier this month, before collapsing to just a few dollars in recent days. The stock traded up to very low double-digits on Monday as JPMorgan Chase & Co. boosted its bailout offer from \$2.00 per share to \$10.00 per share to offset significant resistance. JPMorgan Chase also gained control of roughly 40% of Bear Stearns, effectively putting Bear Stearns under JPMorgan Chase control...

...just wondering how many of the investment professionals at BS had the majority of their retirement dollars in company stock?

### House of Cards

Domestic and global financial markets are dealing with the painful collapse of an enormous credit house of cards that developed in recent years. As noted before, all types of loans—many of dubious quality—were packaged as

loan pools and sliced and diced into a wide array of investment products. Loan packagers (brokers) purchased Aaa/AAA ratings from U.S. credit rating agencies and then sold these Aaa/AAA rated pieces of junk to greed-hungry investors around the globe...



...additional chickens must still come home to roost for many investors, with billions of dollars of additional investment write-downs still to come.

...in addition, the formerly sterling reputations of rating agencies Moodys, Standard & Poor, and Fitch have been seriously tarnished.

### The Budget Deficit

Four years in a row of annual budget deficit declines will now give way to what could be the largest annual deficit on record. Last year's \$162 billion budget shortfall could give way to a deficit approaching \$450 billion this fiscal year, a combination of much slower American economic growth, the \$168 billion fiscal stimulus package recently passed by the U.S. Congress, and additional spending likely to be suggested and approved by the Congress in coming weeks/months...

...as former U.S. Senator Everett Dirksen is alleged to have stated at one point, "a billion here, a billion there... and pretty soon you're talking about real money."

### Commodity Bust

Last week's plunge in overall commodity prices (including gold) was

the sharpest weekly decline in 50 years, according to the Reuters/Jefferies CRB Index of 19 commodities. Gold fell nearly \$100 per ounce to just north of \$900 before stabilizing late Monday and adding a few dollars in value on Tuesday. Gold has been an outstanding investment play over the past 4-6 years. It is also one of the worst long-term investments since 1980...

...timing is everything.

## Aggressive Investment (Part One)

Interesting patterns have developed over the past 10-12 years as one follows where some of the most aggressive investment dollars have been parked. The second half of the 1990s found aggressive investors chasing internet and technology stocks, along with dozens of other NASDAQ stocks. The NASDAQ peaked in early 2000 at roughly 5089, before a sustained downward move of nearly 80% to 1113. The NASDAQ has been above 2800 in recent months and is currently around 2330.

Many aggressive investors who got their hands burned in the NASDAQ in 2000-2002 soon chased residential real estate, with billions of dollars chasing properties, especially in Arizona, California, Florida, and Nevada. Those investors who got in early and didn't stay too long did well. Other investors who waited too long to sell, as well as players who entered those markets in 2006 and early 2007, got hammered. Many are renting out their properties, not being willing to take substantial losses...

...bulls & bears make money. Pigs get slaughtered.

## Aggressive Investment (Part Two)

Some of these aggressive investors, as well as many others around the globe, then began chasing commodities, including gold and silver, oil, copper, agricultural products, etc. Numerous investors also "went long" the euro currency, while also "shorting" the U.S. dollar...

...some of these investors have done well. For their sake, they may also not want to stay too long at the party.

...where are some of these investors likely to go after commodity prices look more and more "toppy?" In my opinion, back to stocks.

## "Government" Actions

Aggressive financial market moves by the Federal Reserve, as well as strong actions taken by the U.S. Treasury Department to enhance government demand for mortgages, have brought into question what might be the "proper" role of the Fed and the Treasury Department. Critics of the Fed would suggest that steps taken recently to provide funding to a larger number of Wall Street firms should have been enacted a few years ago.

Other critics would suggest that the Fed should have at least expanded borrowing options when credit market anxiety first engulfed the global financial community last August. Critics on the other side would strongly suggest that the Fed is greatly expanding its reach into areas that will only lead to chaos, confusion, and inflation down the road...

...the Fed always has critics as to excessive or inadequate actions. What is clear is that the Fed is in uncharted waters, as is the global financial community in general, in regard to frequent "freeze ups" in formerly fluid domestic and global financial markets.

## Existing Home Sales

Don't look now, but sales of existing homes surprisingly rose last month, as opposed to expectations of another decline. The 2.3% increase in home sales was the first rise in seven months...

...maybe, just maybe, the combination of lower home prices in many communities, better credit flows in the mortgage sector, and home buyers who sense bargains just might be a solid recipe for stabilization in this critical sector sooner rather than later.



## "TEA"sers

### Signs

On a repair shop door:  
***We can repair anything.  
(Please knock hard—the  
door bell doesn't work.)***

In an office:  
***Would the person who took  
the step ladder yesterday  
please bring it back or  
further steps will be taken.***

—Scott Friedman, CSP



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