Alice In Wonderland

eResearch Corporation is pleased to provide an article, written by Jimmy Mengel, for the Outsider Club.

In this article, Mr. Mengel looks at the lemmings factor.

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This Market Is Going To Eat You Alive

By Jimmy Mengel | Wednesday, March 18, 2015

"Speak English! I don't know the meaning of half those long words, and, what's more, I don't believe you do either!" - the Eaglet

As I told you yesterday, we have been living in an Alice in Wonderland stock market. Things are not quite what they seem...and they keep getting curiouser and curiouser. Not only are the government and the Fed forcing us to play a rigged game, we are also being subjugated by the very language the Fed uses to control the market, no matter what it is actually saying.

Fedspeak has always been an inside joke among those in power. Princeton economist Alan Blinder called the Fed's language "a turgid dialect of English" — a vague and ambiguous way of speaking to ensure a level of confusion in the public so they do not overreact to Fed officials' remarks. We have seen this play out in the last few months regarding the Fed's willingness to raise interest rates. Of course, if Yellen came out and said "we're raising interest rates tomorrow", the market would have a massive sell-off in the wake of the panic. So she has to veil her comments in a clouded fog.

That is why she has repeatedly said we just have to be patient. But, as you well know, patience is a very relative term.

There was a great feature story in the New York Times this weekend that dived into Fedspeak by tapping the talents of several linguists. Here is how linguist Lawrence Solan unpacks that adjective's baggage.

He says that there are three distinctions of the word 'patience':
1) Standing in line at Staples to have a copy made
2) Waiting to see a doctor
3) Waiting to get a mortgage approved

From the Times:

But by now it seems clear that "patient" has become a term of art, a word with a meaning specific to the Fed. That's because the meaning of "patient," like many adjectives, depends on context. "Patient" in the first example might mean five minutes. For the doctor, perhaps a half-hour to an hour. For the mortgage, several weeks.

“When have you waited long enough to have been ‘patient’ so you can politely complain again in the doctor’s office, the copy shop or to your mortgage bank? There is no real answer,” he said.

And that is the key... the word means whatever Yellen wants it to mean on any given day. That gives individual investors like you and I pretty much nothing to go on.

“It is more akin to the language of diplomacy, politeness, tact, innuendo, euphemism, veiled threats, bribes, and oblique sexual come-ons,” according to Harvard psychology professor Steven Pinker.
“Cases in which the content of a speech act is highly fraught,” he explains. Pinker elaborates:

When the chair of the Fed speaks, she knows that she is not just conveying information about the Fed’s plans, but sending a signal that changes the way that millions of people will behave, and how each will expect all the others to behave.

Investors not only interpret the remarks but try to guess how other investors will interpret the remarks. In that regard, her words are like an oath or a pronouncement of a jury verdict or marriage ceremony, or a prayer or a magical incantation — the mere act of uttering them changes the world. So the words take on formulaic meanings, and she is aware of that fact when choosing them.

The fact that the meaning of “patient” can vary so significantly depending on context, and even then may be difficult to pin down, can work to policy makers’ advantage.

That advantage is not to be understated. So let us return to Wonderland with an ex-Fed official to pull all of this together. Former New York Fed economist Richard Alford has made this analogy before, and points out that:

The Fed’s attitude towards its mandate is closer to the attitude that Lewis Carroll’s Humpty Dumpty had toward words, as revealed in this exchange with Alice:

“When I use a word,” Humpty Dumpty said in a rather scornful tone, “it means just what I choose it to mean – neither more nor less.”

“The question is,” said Alice, “whether you can make words mean so many different things.”

“The question is,” said Humpty Dumpty, “which is to be master—that’s all.”

And master the language she has, leaving us to hem and haw about what she means and what the stock market will do in reaction. That leads me to my last — and for investors, most important — takeaway from these overwrought metaphors...

Perhaps my favorite passage from Alice in Wonderland is “The Walrus and the Carpenter.”

Essentially, these two characters have set up an erstwhile Oyster House on the shores of the ocean. But they are in desperate need of the bivalves to stock their restaurant. So they descend into the deep to lure out a crowd of baby oysters to follow them to the surface.

I’ll let Lewis Carroll take it away:

“O Oysters, come and walk with us!”

The Walrus did beseech.

“A pleasant walk, a pleasant talk,
Along the briny beach:
We cannot do with more than four,
To give a hand to each."

The eldest Oyster looked at him,
But never a word he said:
The eldest Oyster winked his eye,
And shook his heavy head—
Meaning to say he did not choose
To leave the oyster-bed.
But four young Oysters hurried up,
All eager for the treat:
Their coats were brushed, their faces washed,
Their shoes were clean and neat—
And this was odd, because, you know,
They hadn't any feet.
Four other Oysters followed them,
And yet another four;
And thick and fast they came at last,
And more, and more, and more—
All hopping through the frothy waves,
And scrambling to the shore.

Remind anyone of investors following the Fed to record high stock prices? Let's finish the poem...

The Walrus and the Carpenter
Walked on a mile or so,
And then they rested on a rock
Conveniently low:
And all the little Oysters stood
And waited in a row.
"A loaf of bread," the Walrus said,
"Is what we chiefly need:
Pepper and vinegar besides
Are very good indeed—
Now if you're ready, Oysters dear,
We can begin to feed."
"But not on us!" the Oysters cried,
"After such kindness, that would be
A dismal thing to do!"
"The night is fine," the Walrus said.
"Do you admire the view?
"It seems a shame," the Walrus said,
"To play them such a trick,
After we've brought them out so far,
And made them trot so quick!"
The Carpenter said nothing but
"The butter's spread too thick!"
"I weep for you," the Walrus said:
"I deeply sympathize."
With sobs and tears he sorted out
Those of the largest size,
Holding his pocket-handkerchief
Before his streaming eyes.

"O Oysters," said the Carpenter,

But answer came there none-

And this was scarcely odd, because

They'd eaten every one.

So, that begs the question: are individual investors simply oysters being led to the slaughter?

When the Fed raises rates, will it wipe out all the ill-gotten gains we have seen over the past six years of this Wonderland bull market? Time will tell, but I will send you off with one warning...

While we oysters count our stacks of pearls
And cheer both to and fro...
When the Walrus comes to feast
We will be the last to know...

Sincerely,

Jimmy Mengel

Jimmy is a managing editor for Outsider Club and the Investment Director of the personal finance advisory The Crow's Nest. You may also know him as the architect behind the wildly popular finance and investing website Wealth Wire, where he's brought readers the stories behind the mainstream financial news each and every day. For more on Jimmy, check out his editor's page.

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