Making Information Useful

A GUIDE FOR R.I.S.E. XII

RedefiningInvestmentStrategyEducation

Stocks:

1) **Tugging on Superman's CAPE** – This tells you about the very long term potential of the stock market. We follow Robert Shiller's (of Yale) data on CAPE or Cyclically Adjusted Price to Earnings. Instead of looking at forward earnings or even recent earnings, Shiller instead follows the market's earnings over an extended period of time. His data can be found at http://www.econ.yale.edu/~shiller/data.htm. Our research suggests that this ratio can tell you quite a bit about the next 10 years. When the ratio is low (less than 15) it suggests opportunities are ahead for stocks and historically we've seen the next 10 years average 10.4% a year. When CAPE is over 15 the average yearly returns are only 3.8%. When the ratio is high it does not mean that it is impossible to make money in stocks but rather that an active approach is needed.
2) **Disapproval** – Voter attitudes often mimic the unrest of the consumer. High levels of disapproval usually lead to poor returns. We examined Gallup's data going back to the 1950s. We find if the presidential disapproval rating is low (less than 40) stocks make 10.1% over the next 12 months. If disapproval is high (over 40) then stocks underperform and average a return of 5.5% over the next 12 months.
3) **Congress is Adjourned** – This is a short term indicator. Congress makes many rules (about 80,000 pages are proposed each year). Simply put, the stock market performs better when Congress is out of session and not creating mischief. Since 2006 we find when Congress is out of session stocks have averaged a 10% compound annual return. When Congress is in session? Stocks have averaged a -8.4% compound annual return

Economy:

1) **Gridlock is Our Friend** – Since the time of Bill Clinton, our economy does much better if neither one of our political parties control the White House, Senate, and the House of Representatives. Too many laws are created. While well intentioned they have negative consequences for the economy. When there has been gridlock in Washington, we find GDP has grown 27% faster and that unemployment is lower.
2) **Beware the Four FED Horsemen of the Apocalypse** – The regional FED reports do not get enough attention. In particular we suggest following the FED reports for Chicago, New York (Empire), Richmond, and Philadelphia. If one is reporting a negative number it means we have one FED Horseman of the Apocalypse present. If all four are negative… Well, it's usually bad news! Historically, 62% of the time Industrial Production fell over the next six months.
3) **The Single Best Economic Indicator** – Perhaps the best single indicator for the economy comes from the Economic Cycle Research Institute or ECRI. Their leading indicator for the economy is released weekly at http://www.businesscycle.com/. Since 1968, if the ECRI number is negative we find Industrial Production typically falls by 0.7% in the following six months. If the ECRI number is positive, the Industrial Production typically gains 2.2% in the next six months. A BIG swing indeed!

James Investment Research, Inc.

Investing for a lifetime.