2-Year Yield and Fed Funds Finally in Balance

DISCLOSURE: *The contents of this report were researched, analyzed, and written by Tom McClellan of* ***McClellan Financial Publications****, and were put into this report format, published and distributed by* ***eResearch Corporation****.*

eResearch Corporation is pleased to provide a weekly commentary, authored by Tom McClellan, entitled "The McClellan Chart-In-Focus", which is a free technical analysis article published each week.

In this article, Mr. McClellan says that it is incumbent on the Fed to gets its Fed Funds target in step with the 2-year T-Note yield.

The article is reproduced below, beginning on the next page, or you can use this link to go to the article directly: <Ctrl-Click> **HERE**

You can also visit the McClellan Financial Publications Home Page at the link below. This is a subscription service, and there are two publications which can be subscribed for: (1) **The McClellan Market Report**; and (2) **The Daily Edition**.

Here is the link to the Home Page: http://www.mcoscillator.com/

***e*Research** was established in 2000 as Canada's first equity issuer-sponsored research organization. As a primary source for professional investment research, our Subscribers (*subscription is free!!!*) benefit by having written research on a variety of small- and mid-cap, under-covered companies. We also provide unsponsored research reports on middle and larger-sized companies, using a combination of fundamental and technical analysis. We complement our corporate research coverage with a diversified selection of informative, insightful, and thought-provoking research publications from a wide variety of investment professionals. We provide our professional investment research and analysis directly to our extensive subscriber network of discerning investors, and electronically through our website: www.eResearch.ca.

Bob Weir, CFA
Contributing Analyst

Note: All of the comments, views, opinions, suggestions, recommendations, etc., contained in this Article, and which is distributed by *e*Research Corporation, are strictly those of the Author and do not necessarily reflect those of *e*Research Corporation.

April 12, 2019

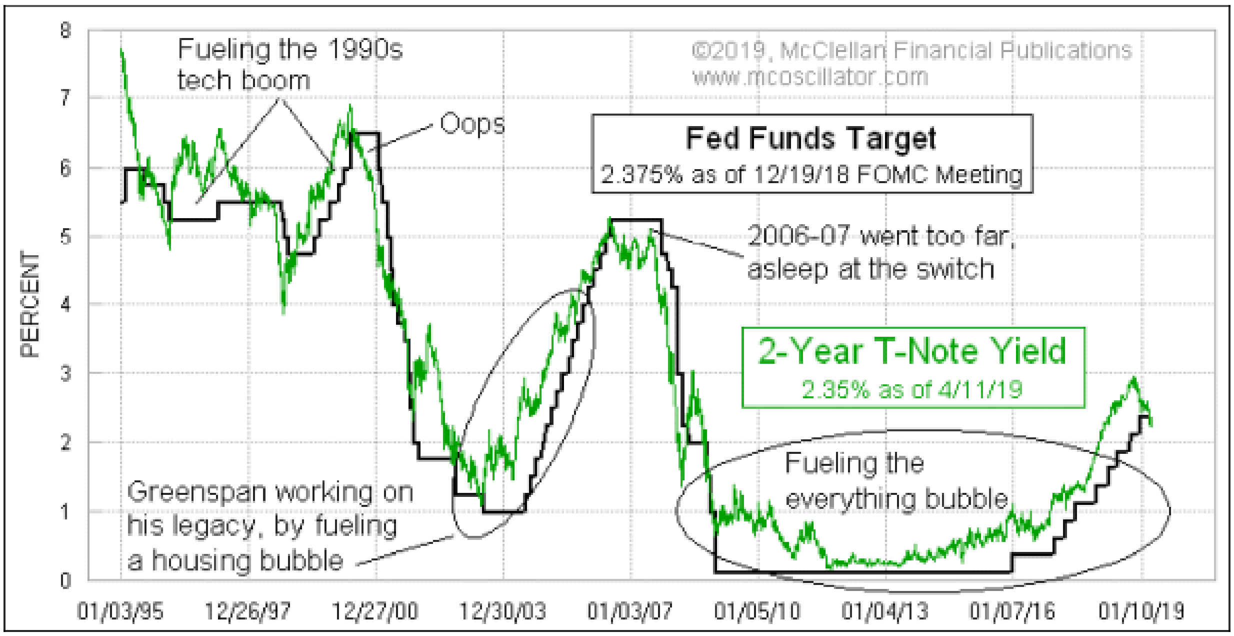
The McClellan Chart-In-Focus

by Tom McClellan (bio at end)

2-Year Yield and Fed Funds Finally in Balance

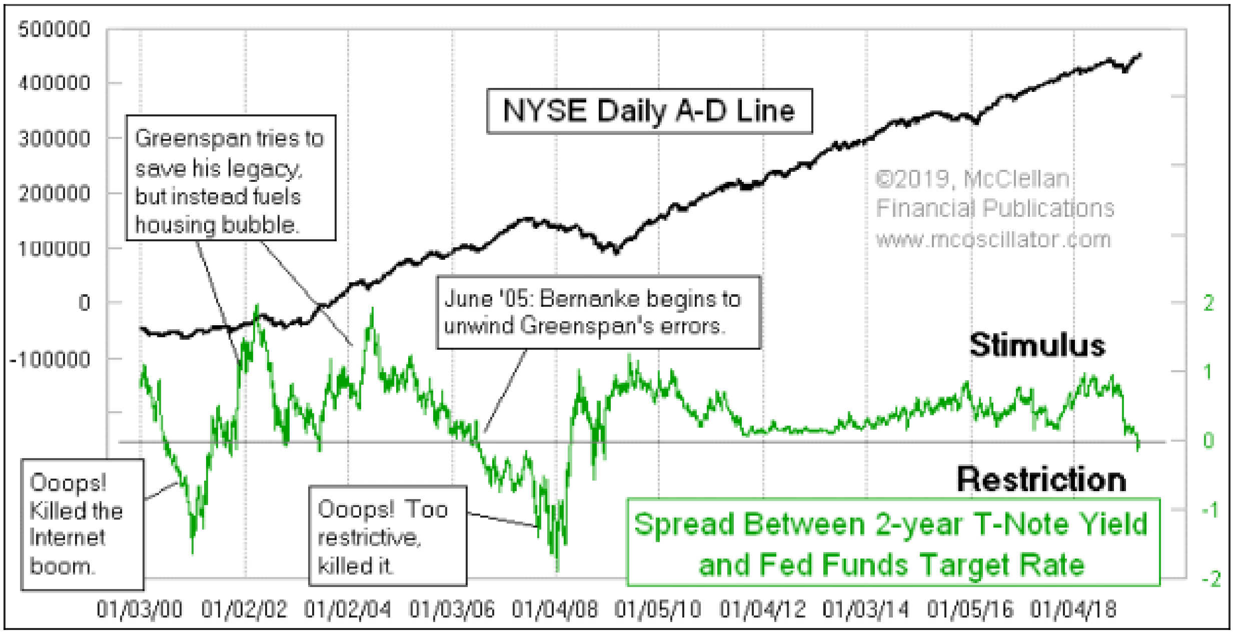
I have long advocated for the FOMC getting out of the business of setting short term interest rates and, instead, they should out-source that job to the 2-year T-Note yield. While that out-sourcing might put several American PhD economists out of work, I am okay with that, because it would give us the benefit of having more efficient monetary policy, with less severe bubbles and depressions.

This week's chart compares the Fed Funds target rate (**black** line) to the 2-year T-Note yield (**green**).



When the **green** line is above the **black** line, then that means the Fed is setting the Fed Funds (FF) target rate too low, and that is a condition which tends to be very stimulative to the financial markets. Impending depressions are signaled when the 2-year drops well below the FF, and the Fed is slow to respond to that. So, if the Fed really wanted to dampen down the excessive stimulus and restriction, then the FOMC Policy should be to keep the FF as close as possible to the 2-year yield all the time.

This next chart helps to make this point about stimulus and restriction. It compares the spread between the 2-year and the FF rates to the NYSE's A-D Line, which is one of the best indicators of financial market liquidity.



Generally speaking, when the spread is positive, that is enormously stimulative to the stock market, and eventually to the economy. A downward excursion into the "restriction" zone is what creates problems. But those problems do not necessarily have to commence upon the first foray into that "restriction" zone.

In the middle of the above chart, we can see that this spread first went negative in May 2006, but the bull market continued for another 17 months before the liquidity problems finally became a problem.

The NYSE's A-D Line topped in June 2007, and price indices made their final top in October 2007.

Back in 2000, this spread went negative for the first time in June 2000, which was after the Nasdaq's bubble top, but before the real ugliness of the bear market which resulted from that Internet Bubble collapse.

Getting back to the neutral point between stimulus and restriction means that the Fed is finally transitioning to a neutral state with monetary policy. That could be just a waypoint en route to a restrictive policy. If the 2-year T-Note yield continues to fall, and if the FF target rate does not respond in kind, then that could similarly make for problems several months from now.

However, if the Fed can somehow manage to keep their target close to where it should be, then perhaps we can finally get to enjoy that Goldilocks economy so many have dreamed of. I do not hold out much hope that the Fed will get that right, because I do not believe any of the FOMC members are actually going to read this. Or, if they do, they are not likely to believe that "the market" could know more than they do, what with their fancy degrees and all. But there is always hope for a better outcome someday.

Tom McClellan, Editor,

The McClellan Market Report

BW: Information on Tom McClellan and *The McClellan Market Report* and *The Daily Edition* is is provided below.

ABOUT THE AUTHOR

Tom McClellan

Tom McClellan has done extensive analytical spreadsheet development for the stock and commodities markets, including the synthesizing of the four-year Presidential Cycle Pattern. He has fine-tuned the rules for inter-relationships between financial markets to provide leading indications for important market and economic data.

Tom is a graduate of the U.S. Military Academy at West Point, where he studied aerospace engineering, and he served as an Army helicopter pilot for 11 years. He began his own study of market technical analysis while still in the Army, and discovered ways to expand the use of certain indicators to forecast future market turning points.

Tom views the movements of prices in the financial market through the eyes of an engineer, which allows him to focus on what the data really say rather than interpreting events according to the same "conventional wisdom" used by other analysts.

In 1993, he left the Army to join his father in pursuing a new career doing this type of analysis. Tom and his Father spent the next two years refining their analysis techniques and laying groundwork.

In April 1995 they launched their newsletter, The McClellan Market Report, an 8-page report covering the stock, bond, and gold markets, which is published twice a month. They utilize the unique indicators they have developed to present their view of the market's structure as well as their forecasts for future trend direction and the timing of turning points.

A Daily Edition was added in February 1998 to give subscribers daily updates on their indicators and also provide market position indications for stocks, bonds, and gold. Their subscribers range from individual investors to professional fund managers. Tom serves as editor of both publications, and runs the newsletter business from its location in Lakewood, WA.

#####