BUSINESS CYCLE DEVELOPMENTS

If the historical averages hold up, the Fed should abandon an easing posture by the 4th qtr.

Here's the rationale for such a position. The Fed has stated they are waiting for the unemployment rate to decline to 6.5%. A cyclical peak for the *Average Weekly Initial Claims for Unemployment Insurance* typically occurs an average of one month before the trough in the economy, whether the ensuing downturn is a recession or slowdown. An average of 11 months after the *Initial Claims* have peaked the Fed has started to raise the Fed Funds rate, or starts responding to rising economic growth. To date, the *Initial Claims* peaked, for this cyclical slowdown, in November 2012, or one month after the economy started to improve in October 2012. Extrapolating these experiences would center a policy change for the Fed in the fourth quarter of 2013.

It be could argued that there are some good reasons to push policy change into 2014-15, per Fed remarks, but the facts are different. There are two fat-tailed observations in that 11 month average. Burns admitted he held off tightening until after the 1976 election, lengthening the Fed hike to 25 months after the *Initial Claims* peaked. The effect of the *RTC Improvement Act* of 1991 dampened economic activity 22 months after a peak in *Initial Claims*, which also held policy in check (see table).

INITIAL CLAIMS LEAD A ECONOMIC TROUGH & FED FUNDS HIKE

PEAK: INITIAL CLAIMS	ECONOMIC TROUGH	MONTHS LEAD (-) LAG (+) TO I.C.	FED TIGHTENS	MONTHS LEAD (-) LAG (+) TO I.C.	UNEMPLOYMENT RATE @ FED HIKE
2/61	2/61 (R)	-0-	8/61	+6	6.6%
4/67	7/67 (SD)	-3	8/67	+4	3.8%
10/70	11/70 (R)	-1	4/71	+6	5.9%
1/75	5/75 (R)	-4	2/77	+25 ◄ A. BURNS FED ELECTIONEERING FOR '76 ELECTION.	7.6%
5/80	7/80 (R)	-2	8/80	+3	7.7%
9/82	12/82 (R)	-3	3/83	+6	10.3%
9/85	7/85 (SD)	+2	11/86	+14	6.9%
10/89	7/89 (SD)	+3	GULF WAR #I PREVENTS FED HIKE – WAR CAME 9 MO. AFTER INS. CLAIMS PEAK.		
3/91	3/91 (R)	-0-	1/93	+22 ◄ RTC ACT (12/91)	7.3%
3/96	1/96 (SD)	+2	3/97	+12	5.2%
10/01	11/01 (R)	-1	DOT-COM BUST IN 3/00 & S&P 500 PEAK IN 8/00 PRE-EMPTED A FED HIKE.		
4/03	8/03 (SD)	-4	1/04	+9	5.7%
11/06	11/06 (SD)	-0-	BEAR STEARNS FUNDS CLOSE (6/07) – SUB-PRIME CRISIS STOPS ANY FED HIKE.		
3/09	6/09 (R)	-3	2/10	+11	9.8%
8/10	11/10 (SD)	-3	1/12	+17	8.3%
11/12	10/12 (SD)	+1	? ?	? ?	? ?
	AVERAGE:	**- 1 mo.**		**+ 11 mo.**	**7.1%**

ALL DATA ARE MONTHLY AVERAGES. [R] RECESSION; [SD] SLOWDOWN.

The current Unemployment Rate is 7.7%. So how many months does it take to work the rate down to 6.5%? About 60% of the time, when the Fed tightens, the Unemployment Rate is above the current Fed target of 6.5%. Many times when they tightened and the Unemployment Rate was above 6.5%, it never fell below 6.5% because of another impending recession (i.e. 1980 & 1982) or like the period today, where the U.S. is still reeling from the sub-prime crisis. Assuming no economic or fiscal stumbling blocks ahead, the average time to reach the 6.5% rate is seven months or the 4th qtr. of 2013!