

Investing with Occam's Razor

Time to get philosophical about the outlook for the market with the help of Occam's Razor. This tool tells us to assume that the simplest explanation is the most likely. Now let's apply that to recent Fed statements for what that tells us about the next move for the stock market (SPY). Along with that Steve Reitmeister shares his updated trading plan to stay on the right side of the action. Read in below for more.

I continue to be amazed by the wide-ranging reaction to the most recent Fed announcement on Wednesday 6/14. I went into detail on this topic in my last commentary:

Powell to Investors: Do You Feel Lucky Punk?

Now given the benefit of a long relaxing weekend, I have come to an even simpler view of things. I will share that in today's Reitmeister Total Return commentary with associated trading plan.

Market Commentary

What came to mind over the weekend was applying Occam's Razor when interpreting the Fed plans and what that means for the economy and stock market.

For those who are not immediately familiar with this philosophical concept, then here is the boiled down version from Wikipedia:

"Simpler explanations are more likely to be correct; avoid unnecessary or improbable assumptions."

In this case the simpler explanation is to take the Fed at their word. That probably 2 more rate hikes are coming and the jobs market will be a casualty in their war against inflation.

I share this insight versus those who somehow think it is more

logical that the Fed is bluffing about their future intentions. That is a long shot friends...and thus seems like a grave mistake to bet on that outcome with higher stock prices.

Remember that an ongoing mission of the Fed going back many administrations is the necessity for clear and consistent communication. This is the best way for investors to act in orderly fashion with the least disruption to the market.

Now consider how consistent Powell and other Fed officials have been on their messaging. Like these talking points that are echoed time and time again at the multitudinous Fed speeches the past several months:

- Inflation is an economic disease that must be eradicated for the long term benefit of the economy.
- There is more work to do to tamp down inflation to 2% target
- 2 more rate hikes likely this year
- Unemployment rate will climb to 4.5% before it improves (yet remember that at NO TIME in history has unemployment rate ever climbed that high without going at least 1% higher. Meaning the Fed is underplaying the likely negative effects of their plans).
- The greater risk is for the Fed to end their efforts too early allowing inflation to rise from the ashes. (Meaning better to create recession than allow inflation to rise again). Which is why they keep saying...
- No rate cuts til 2024
- Recession still the base case

The simpler, and much more plausible explanation, is that the Fed is going to do EXACTLY what they say they are going to do.

If that is true, then it is hard to be bullish. Much more logical to be balanced or straight up bearish given the high probability this ends in recession and reawakening the bear market from its slumber.

For now, investors seem to be pressing pause. That is a bit harder to see with the S&P 500 (SPY) still a notch higher than at the time of the 6/14 Fed announcement.

But once again those numbers are skewed towards gains in the usual mega cap suspects. Looking out to the small and mid caps, both are firmly in the negative column since the Fed announcement.

Also in the negative camp for investor sentiment is the spike in rate hike expectations for the 7/26 Fed meeting. A month ago, only 19% saw another quarter point hike in July. That probability is now up to 77%.

Note that the Fed's favorite inflation gauge is Core PCE which comes out again on 6/30. No doubt that report will adjust the odds once again. So keep your eyes on that.

Trading Plan

The bear market has been firmly in hibernation mode all year long. Dormant...but not dead.

So, for now I think investors are in wait and see mode. No need to advance higher given the gains already in hand. And no need for a nasty correction either. Maybe a modest 3-5% pullback allowing a trading range to emerge between 4,200 and 4,400.

The more serious the Fed is about all the pronouncements above, the more likely a recession is in the forecast which brings with it a return of bearish conditions. A bearish hedge or straight up shorting of the market will be the trading path to profits.

Whereas the more quickly annual inflation appears on pace for 2% or less, without unemployment rising, then indeed the Fed stuck the soft landing. This will be a bullish green light to emerge into the next long term bull market. Risk On growth

oriented investing is what pays the bills here with an overweighting of small caps (given how much they are lagging large caps at this time).

I will continue to monitor the all the relevant inputs to give updates and trading adjustments as the situation dictates.

What To Do Next?

Discover my balanced portfolio approach for uncertain times.

It is perfectly constructed to help you participate in the current market environment while adjusting more bullish or bearish as necessary in the days ahead.

If you are curious in learning more, and want to see the hand selected trades in my portfolio, then please click the link below to what 43 years of investing experience can do for you.

Steve Reitmeister's Trading Plan & Top Picks >

Wishing you a world of investment success!



Steve Reitmeister...*but everyone calls me Reity (pronounced "Righty")*

CEO, StockNews.com and Editor, Reitmeister Total Return

SPY shares fell \$0.22 (-0.05%) in after-hours trading Tuesday. Year-to-date, SPY has gained 14.75%, versus a % rise in the benchmark S&P 500 index during the same period.

About the Author: Steve Reitmeister



Steve is better known to the StockNews audience as “Reity”. Not only is he the CEO of the firm, but he also shares his 40 years of investment experience in the Reitmeister Total Return portfolio. Learn more about Reity’s background, along with links to his most recent articles and stock picks.

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