When the extraordinary becomes the expected, the likelihood of disappointment is high.

The stock market hemorrhaging continued late last week for a variety of reasons. Included were the deteriorating economic outlook both in the United States and abroad, the mounting threat of crisis in the Euro Zone, and the end of the Fed's Operation Twist looming at the end of June. But although deteriorating economic and market conditions may be raising hopes that a fresh round of Fed stimulus may soon be on its way, investors will likely be forced to wait some time before they receive any further monetary support.

Monetary stimulus programs such as Quantitative Easing (QE) and Operation Twist (OT) are considered extraordinary measures to support the U.S. economy and financial markets. With interest rates already pinned at effectively 0%, Fed policy makers have resorted to these programs as a way to provide additional stimulus in an effort to thwart the full blown collapse of the financial system.

Following the disappointing May jobs report on Friday, some are now speculating that more Fed stimulus is now assured. Some go even further to project that an announcement may come as soon as the upcoming FOMC meeting on June 19-20.

<u>Will the Fed come to the rescue, yet again?</u> In comparing the current situation to the previous times the Fed moved, it probably will take extreme changes in the level and direction of the jobless rate, GDP, or the US Stock market to prompt Fed into action. At the moment, the U.S. economy and financial markets are currently far from operating at negative extremes. Here are a few basic points to support this idea.

1) Jobs: The U.S. economy ADDED +69,000 jobs in May. Sure the latest report released on Friday was disappointing, but we still ADDED jobs for the month. And since the beginning of 2012, the U.S. economy has ADDED +823,000 net new jobs. To put this into comparative context, the U.S. economy LOST nearly 6 million jobs in the year prior to the launch of QE1 and LOST another 303,000 jobs in the months leading up to the announcement of QE2. So while far from strong, it is needless to say that we are operating nowhere near any extreme conditions in employment that would justify rushing out with even more stimulus.

2) GDP: U.S. economic growth INCREASED by 1.9% in the first quarter. Yes, it does represent a deceleration from the 3.0% reading from the prior quarter at the end of 2011, but it still represents an INCREASE. Once again, an economy that is still expanding hardly represents a circumstance where extraordinary measures are required from a monetary policy perspective.

3) Stock Market: The U.S. stock market as measured by the S&P 500 Index is still up +2.6% on a total returns basis. Yes, there has been a brutal correction, falling roughly -9% from its recent peak at the beginning of the second quarter, but at this point, it cannot be construed as flashing a 'recessionary warning'.

The fact that investors are even contemplating the idea that the Fed is poised to soon provide more stimulus highlights an even greater dilemma facing policy makers going forward. The extraordinary has now not only become the ordinary but also the expected.

When the Fed launched QE1 back in early 2009, it was done so with very good reason. The global financial system was teetering on the brink of collapse.The Fed did their job by taking swift action and pulling the global financial system back from the edge. But it was with the announcement of QE2 in 2010 and Operation Twist in 2011, where the Fed drifted way off track. Both times the Fed felt compelled to preemptively pour on more stimulus at the first signs of any renewed weakness. These two later policy actions have created an unhealthy expectation among investors. Extraordinary measures such as QE and Operation Twist are no longer for extreme emergencies. Instead, they are now simply expected, as the belief now firmly exists that the Fed will charge in with more of these special stimulus programs the moment the pace of economic growth ticks lower or the stock market sheds several percent over a few months. The notion of the normal business cycle has been lost in the process.

This Thursday, all eyes will be on Fed Chairman Bernanke as he addresses Congress on the economy. Will he hint of further stimulus or will he take a pass? Yes, conditions have deteriorated, but have they declined enough to warrant extreme measures?

What will it take to get the Fed to move? The best reading to monitor may be the U.S. stock market which often leads the economy. Typically, a peak to trough decline of -17% to -20% gets serious attention from the Fed and has prompted action. Given that the stock market has only sold off by -9% from its recent peak and is still positive for the year, suggests that we could have much further to go on the downside before we can reasonably expect the Fed to intervene.

Portfolio Strategy:

Weakening fundamentals in US economic data, no resolution to the Euro debt issues, and a breakdown in key market indices have prompted the following:

- a reduction in total risk exposure
- an increase in High Yield bonds to provide income
- raise some cash to reinvest at lower levels.

The next point of clarity may come in late June after the Greek Elections and the Fed meeting.