

Insight

Much Ado About Nothing

DOUGLAS HOLTZ-EAKIN | MAY 20, 2010

Markets dropped sharply early today, with observers attributing the decline to the coincidence of two pieces of bad news: a drop in the index of leading indicators and higher-than expected new claims for unemployment insurance. Huh?

- The index is not "news" it is a compilation of known economic facts that markets have already had the chance to digest. There is no reason for economic observers to be "surprised" in any way by the data.
- New claims jumped by 25,000 to 471,000, thus raising the 4-week moving average to 453,500. Now, the numbers themselves are news (although week-to-week developments are famously noisy), but the fact that the labor market is weak is not. More importantly, recent events are bad news for the economic outlook:
- The Senate continues to labor over financial regulation reform. Unfortunately, with every amendment it gets worse and the threat of a renewed credit crunch rises.
- Europe's sovereign debt crisis continues to evolve and markets are digesting the implications of a "bailout" that is more like a Band-Aid, a weakened European Central Bank, and widening risk spreads.
- Equity markets are repricing risks and raising the cost of capital.

The bottom line: The labor market and growth outlook is weak and policy actions are making it weaker.