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Lies, damn lies and stockbrokers.

Andrew Smithers, chairman of Smithers & Co, a firm that advises on international asset allocation, gives a tongue-in-cheek guide to the not so noble art of stockbroker economics.

There is a vast difference between the economics propounded by economists and that contained in the writings of stockbrokers. This should not cause surprise, as the purposes are completely different. Economists are in pursuit of the truth and stockbrokers of commissions.

The first principle of stockbroker economics is that all news is good. A typical example comes from changes in profits and interest rates which, to some degree, rise and fall together. In weak economies brokers claim that falling interest rates will drive up shares and in strong economies they argue that rising profits will do so.

The second principle is that the stockmarket is always cheap. This requires more flexibility than the first principle and is achieved by inventing meaningless measures of value, such as the bond yield ratio, and using whichever one of these absurdities happens to give the most bullish answer at the time.

The third principle is to make baseless claims without worrying about their validity. A recent favourite has been "profits are rising because of cost-cutting". As this and similar claims cannot be justified either theoretically or pragmatically, they are either not supported at all, or only by the use of data mining.

Data mining is the key technique for nearly all stockbroker economics. There is no claim that cannot be supported by statistics, if these are carefully selected, particularly if they are restricted to a limited period, rather than using the full series available.

Time exposes claims based on data mining. The claims need not, however, then be discarded. They can be put into the pending tray with the standard excuse that "the relationship has broken down." While this cannot be logically distinguished from "there never was a relationship" it has two great advantages. First, it sounds a great deal better, and second, it demands less effort to reuse old nonsense than to invent new follies.

It has been rightly remarked that statistics will always confess if tortured sufficiently.

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Poacher-turned-gamekeeper Andrew Milligan, head of global strategy at Standard Life Investments, explains why he thinks Andrew Smithers (above) is wrong to take such a black-and-white view of stockbrokers.

Much of what Andrew Smithers says about stockbroker economics is valid. Data mining, careful choices of periods when producing charts, discovering "new" relationships - these are

all the tricks of the trade, indeed ones I myself learned many years ago when I was an economist on the sell side. However, I fear that Smithers himself falls into the trap of hyperbole. The true situation is not quite that black and white. I suggest three important points should be borne in mind.

First, there are many professional economists of considerable integrity who work for global broking houses, and who produce detailed good-quality research on topical issues. As analysis of economic headline issues in the major economies is now well covered, for example by the newswires, more of the capacity of the economics community has moved on to other topics, such as understanding financial market regulation, credit and derivative markets or the emerging economies.

Second, while there are many strategists, especially at Wall Street brokers, who conclude that the equity market will generally rise, by no means all can be tarred with that brush. Many experienced strategists do alter their asset allocation calls. Indeed, I know of a number of economists and strategists who prefer to act as Cassandras to the industry, warning investors not to make a mistake and buy a certain asset.

Lastly, experienced recipients of stockbroker research are well aware of the biases and distortions that Smithers so critically points out. This is why many larger houses have their own internal research capabilities, both in terms of economics and other key drivers of financial markets.

Understanding how and why brokers act allows their work to be put into perspective. The relative changes in the strength of the signals coming from stockbroker research - that is, how strongly or weakly they are putting forward their case - can provide important information for the buy side about shifts in investor sentiment and the balance of risks and opportunities.