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Vice President

"By The Way"

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The current market brings to mind the old saying about being an airline pilot; it involves long stretches of boredom punctuated by moments of sheer terror. The S&P 500 continues to trade within the parameters of a well-defined range and has been unable to establish any clear direction, that's the boring part. However, within that range we have experienced violent swings that scare the heck out of us, but just as quickly fade away and have no lasting impact. Almost all of these episodes have been driven by geopolitical events. President Trump (or as one guy nicknamed him Donald Whipsaw) has been responsible for much of it: NAFTA: on – no off; Trade war with China: on – no off; Summit with North Korea: on – no off – no on again. Who knew that having a twitter account was a requirement to trade the market. Several of my more conspiracy theory friends swear he is trading his own account in front of these tweets.

Last week the President was pushed to the back, and events in Europe took center stage as reason to press the panic button. It's been quite a while since the news was full of references to the "PIGS" (Portugal, Italy, Greece and Spain) and the fear that an economic or political disaster might take place in one or all of those countries. With the exception of Brexit, things have been mercifully calm until now, but government corruption in Spain and the inability to find a suitable Prime Minister in Italy brought that narrative back to the fore. With political chaos comes the risk of economic turmoil, and we see that reflected in the sudden decline in Italian bond and stock prices. In times of such disruption, populism and anti-Euro rhetoric rises dramatically. The prospect that political parties which propose to leave the E.U. might well win control of government is becoming more plausible. No one knows how the drama will play out, but lets not overreact, we have been down this road before. Italy hasn't had a stable government since Mussolini. It must be difficult to be the German government that must continue to financially prop-up its weaker sisters to keep the Union intact and be obligated to send good money after bad.

The frenzy surrounding the Italian "crisis" did provide me with a lesson in how commentators use data to promote their own agenda. Those pundits urging a panic reaction present Chart "A" which displays the violent rise in bond yields brought on by the recent news. However, if one seeks more context and looks at the longer term (Chart "B") the latest surge seems much less frightening.

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In my last letter I suggested that it was almost a sure thing that the Democrats would win a majority in the House of Representatives (a potential negative for markets); well let's just say I may have spoken too soon. Amazingly, despite the President's ability to put his foot in his mouth and the continuing revelations coming out of the Mueller investigation, Mr. Trump's approval rating has risen markedly from a low near 33% to 45% today. Now recent polls show the Republicans will lose only 6 seats in the House as opposed to the December 2017 poll which predicted a loss of 46 seats.

I haven't spent much time recently writing about the Chinese economy and with some reason. While China remains the world's second largest economy and a key factor in the level of global trade, the country has quietly progressed along its desired path from an investment driven economy to a more consumer driven one. The transformation is far from over, but so far the government (being authoritarian helps) has managed it well. For example, annual GDP growth is now less than 7%, down from the double-digit rates of a decade ago yet without losing control and falling into a recession. Now though, given the trade and tariff skirmishes with the U.S., there is more risk that the growth path could be disrupted. As an aside, I was fascinated to read that only 23 years ago in 1995, China's GDP was less than 2% of global GDP; today it is over 18%. That is impressive growth and represents a formidable opponent for the U.S. today and into the future.

I wonder if I'm overthinking, searching for reasons to be more positive on Canadian stocks; commodities are looking strong, and when mines and oils are strong, funds flow into Canada. We know this country is well beyond the "hewer of wood, drawer of water" stage, but that reputation is still alive in the global investment community and could be the simple reason for Canadian stocks to find a bid. Don't bet the farm just yet.

This letter is lacking in hard numbers, or a strong call, but as someone wrote recently today's market is "at the mercy of the headlines" and therefore it is what it is. My market outlook has not changed (although I still waffle with the ups and downs of the indices). Fundamentals, particularly corporate earnings remain strong, and thus I remain warily bullish waiting for the market to break out of this range and give me reason to be more definitive.

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