Infomail

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Bracing for September

"There are two kinds of forecasters: those who don't know and those who don't know they don't know"

John Kenneth Galbraith
(Wall Street Journal, Jan 22, 1993)

Coming off a month (August) which saw the US market indices have their worst performance since May 2012, everyone is back at it and bracing for September, which as the media reminds us ad infinitum, is statistically the worst month for equities.

There are many items on the docket, each of which on their own can have an impact, but as a group could have a much larger one. Notably, Syria is taking the forefront, but more as a political uncertainty rather than a big economic impact.

The US Federal Reserve is expected to begin its "tapering" of the purchase of securities from a reported $85 billion per month to something less than that, but the US jobs numbers released Sept 6th may have an impact. They showed the mighty US economy is barely creating any sustainable jobs trends, and more importantly, the "participation" portion of the data is the worst since 1978, meaning more and more are simply relying on a monthly government cheque of some form instead of going out and actively looking for work.

Speaking of the Federal Reserve, item number three would be the announcement of Ben Bernanke's replacement as chair, with rumours that Janet Yellen and Larry Summers lead the pack, but even names like Timothy Geithner have popped up. Considering since 1980 there have been only two changing of the guards at that position (Volker to Greenspan, Greenspan to Bernanke) while there have been five Presidents (Reagan – Bush 1 – Clinton – Bush 2 – Obama) reinforce how important the appointment is.

Finally, sometime in October, the USA will hit its debt ceiling once again, and given how the last two were dealt with by Congress no one is holding their breath for a rational resolution.

Watching the reaction to news of late, it seems the markets have come to grips with the Federal Reserve tapering its bond asset purchases. After all, any purchases going on at all should still be considered "simulative" policy. Although many see the purchases main goal to fund the government's relentless spending and to spark the housing market's revival, in my opinion, the sooner they cut back, the better. One must remember that the Fed cutting back and tapering asset purchases is not the same as the Fed raising rates. Most likely that will be late 2014, early 2015.

Sure we've even used the analogy that it's like taking the training wheels off because the economy is getting its legs. But the fact is, as a parent, we all know they still can fall when those training wheels come off. The current Fed seems reluctant to let the US economy tumble through any turns even though it's a natural part of the process. If there is a change at the top of the Fed, will that still be the case?

Today, Congress reconvenes and there are many decisions to be made, first up being Syria. It will be interesting to see if the GOP will green light an attack on Syria, which now just seems to be an act to reduce the President's embarrassment.

Then Congress has the battlefield of continuing resolution (which must be resolved before October 1st), followed by the debt ceiling in mid October, then the kicking in of Obamacare. In between, the next Fed meeting is September 17th/18th, where to taper or not will be the headline.

In the meantime, global manufacturing PMI numbers were the best in some time, even in Europe, and China's showed its first expansion in four months.

It's a less than perfect environment, but ironically it's the best we've seen since 2007, and that's what markets are detecting: Things are getting better, albeit slowly:

- The US economy has had a major and historical 5 year cleansing
- Global financial/bank capitalizations are the best in years

- S&P 500 company balance sheets (especially cash portion) are best in decades
- Household debt is still high, but reducing
- The S&P 500 has had a good run, but still sits at 14X earnings when the historical average has been 15X

The “brilliant” forecasters that have been crying wolf (wrongly) for almost 5 years now, will continue to be wrong.

The sooner all markets can get away from central bank money printing, and focus on the economics of people getting it done in a disciplined yet aggressive manner, the better it will be for investors around the world. Add to that the fact that if and when the current US President stops “politicizing” the US economy, and just get out of the way, great things can happen.

Stay tuned,

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P.S. I would be remiss without adding a word about September 11th. This week is the 12th anniversary of that horrible day which, whether one realizes it or not, changed all of our lives forever. It is the day we realized the two great oceans no longer kept our way of life safe from those who wish to do it harm. We are reminded of it every time we go through an airport, and it is a day our generation should never forget.