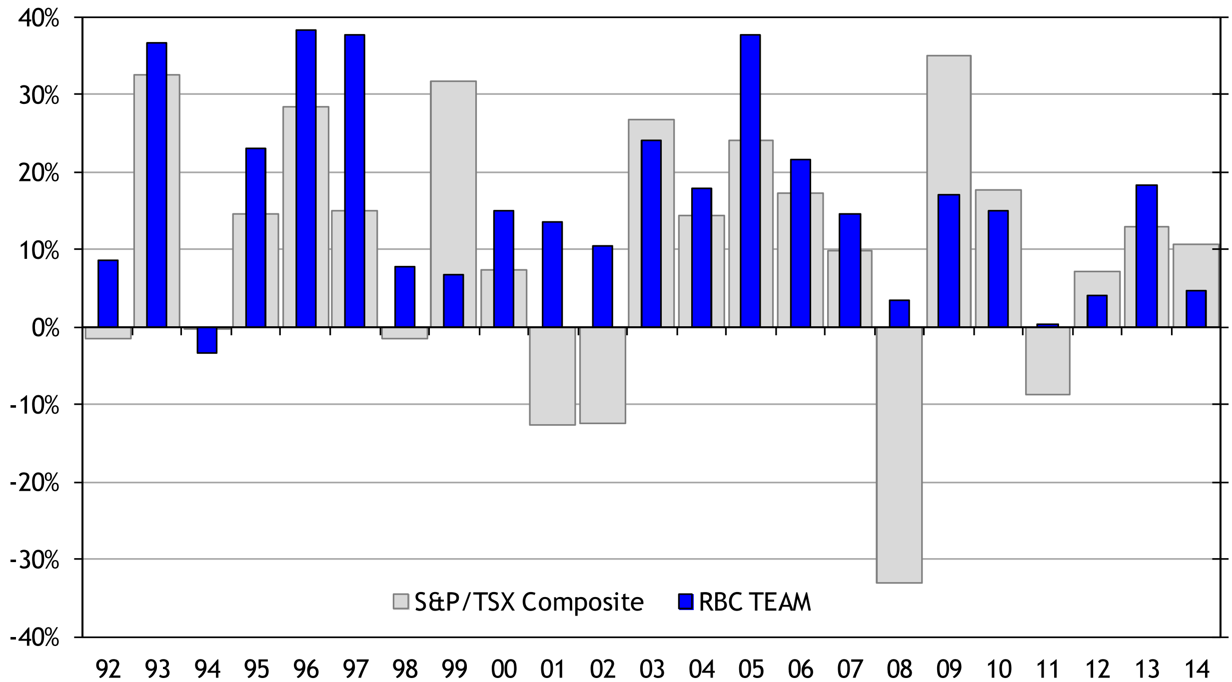
April 6th 2015

"Won2One" with Nick Foglietta

Tactical Equity Income Model Portfolio Record



Tactical Equity Income Model Present Conditions:

TEAM Model Asset Allocation:	**50%** Equities/ **50%** Fixed Income
S&P/TSX 60 Closing Value:	15,026
TSX 200 Day Moving Ave:	14,913
% Above/Below 200 Day Moving Ave:	**0.76%**

Levels for change: 100% stocks - **TSX 15,644** and 100% fixed income – **TSX 14,164**

Weekly Quote

"*The job before Congress is to bring the fear of God back to Wall Street*" – Jim Grant, *The Interest Rate Observer*

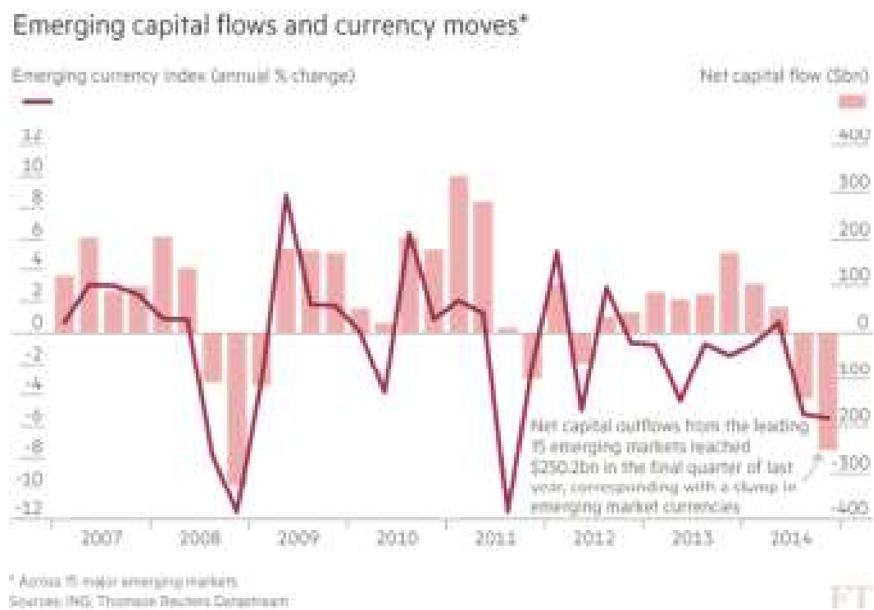
Emerging Markets…Follow the Money!

Today's report is going to seem a bit distant from my usual topics. Emerging market bond levels don't appear to be a hot topic for Canadian investors on the surface. But I can assure you the connection is actually quite direct.

Let me outline a few facts summarizing these bond markets:

1. The main emerging markets we speak of are Brazil, Russia, India, and China. (BRIC). But, in recent years, much of northern Africa, the rest of South America, and smaller Asian nations have grown quickly to make "emerging markets" quite a large sum of economic activity on the whole.
2. In 10 years, emerging market debt has grown from near zero to US $2 trillion.
3. Emerging market overall growth has slipped from 5.8% to near 4% over the past 18 months…and continues to decline!

In short, debt has shot up vertically and, most of the time between 2005 and 2013 GDP grew at more than 7%. All of this good news has come on the back of fresh money overflowing from established nations and landing in emerging markets. The process has worked much like the water that spills over the edge of a cup that is full and continues to have water poured in it.



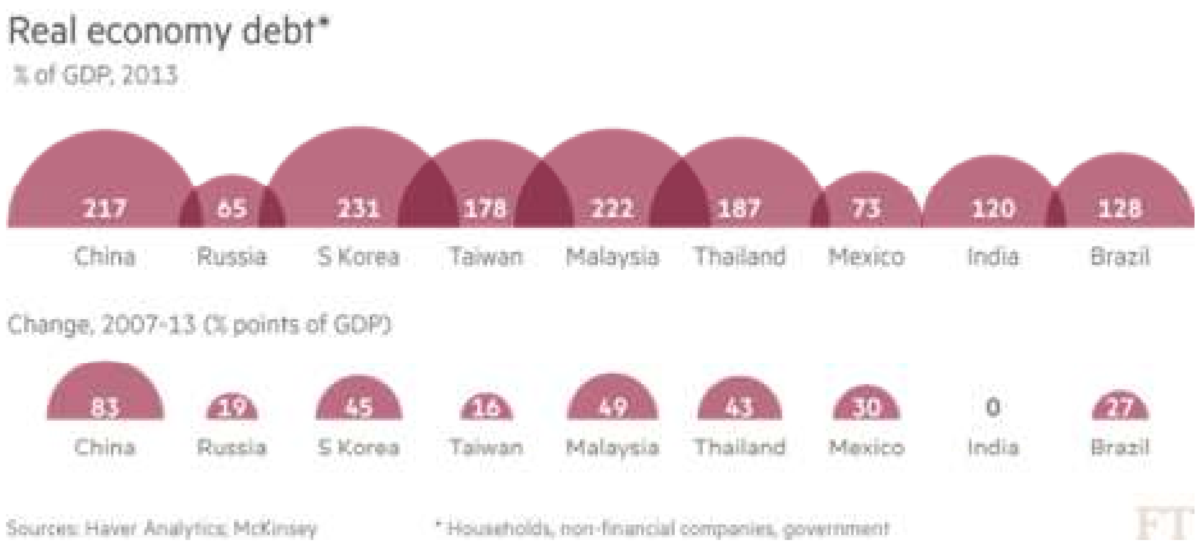
The chart above shows the net capital flows on a quarterly basis for the past 8 years. You can see that the EM currency index (red line) has suffered since 2012 but the case for strong outflows of capital only got going in the third quarter of 2014. (pink bars)

OK…a little quiz. What else started to happen in the late summer of 2013?

All you who said the US dollar took off to the upside get a gold star!

So here comes the key to this section of the editorial. **<u>There is a direct relationship to the net capital outflows emerging market nations experience and the amount of debt they have!</u>**

Next we look at "**<u>real economy debt as a percent of GDP"</u>** in emerging markets.



I wonder why China is doing so much worse than India these days? I think the graphic above gives us an excellent clue!

Let's keep this simple…**If money keeps leaving emerging bond markets interest rates will rise and liquidity will suffer. At $2 trillion in size, emerging market distress would become difficult to contain.**

The money leaving emerging markets has picked up in pace the past 9 months. We will continue to monitor this situation and relate it to the Canadian investor.

In a related development, I believe there is a connection between the conditions in emerging markets and the new Asian Infrastructure Investment Bank (AIIB). If this term is new to you today it will not be for long!

Mohamad El Erian of PIMCO fame, called the development of the AIIB "tectonic" in magnitude. Larry Summers of US Treasury fame stated "AIIB could be a historical event along the timeline for the US dollar dominance."

If you are interested in more details about the AIIB please Google it. There is a lot of background information here (far too much for me to include in this weekly) and what I think is most fascinating is it is getting noticed WITHIN the US!

To finish this week some interesting and fun stories and charts.

Sometimes You Just Gotta Smile ☺

And why would anyone pay their mortgage?

"[Rudolfi's] working-class neighborhood is a short drive from Coconut Grove, a wealthy waterfront enclave of Miami. Her bedroom opens up onto a pool, shaded by palm trees. ***Outside her house, she parks a small motorboat she named Mermaid. The property includes an adjoining house that she rents out…***

In November 2009, her mortgage servicer at the time, Aurora Loan Services, a unit of the now-defunct Lehman Brothers, filed to foreclose on her house.

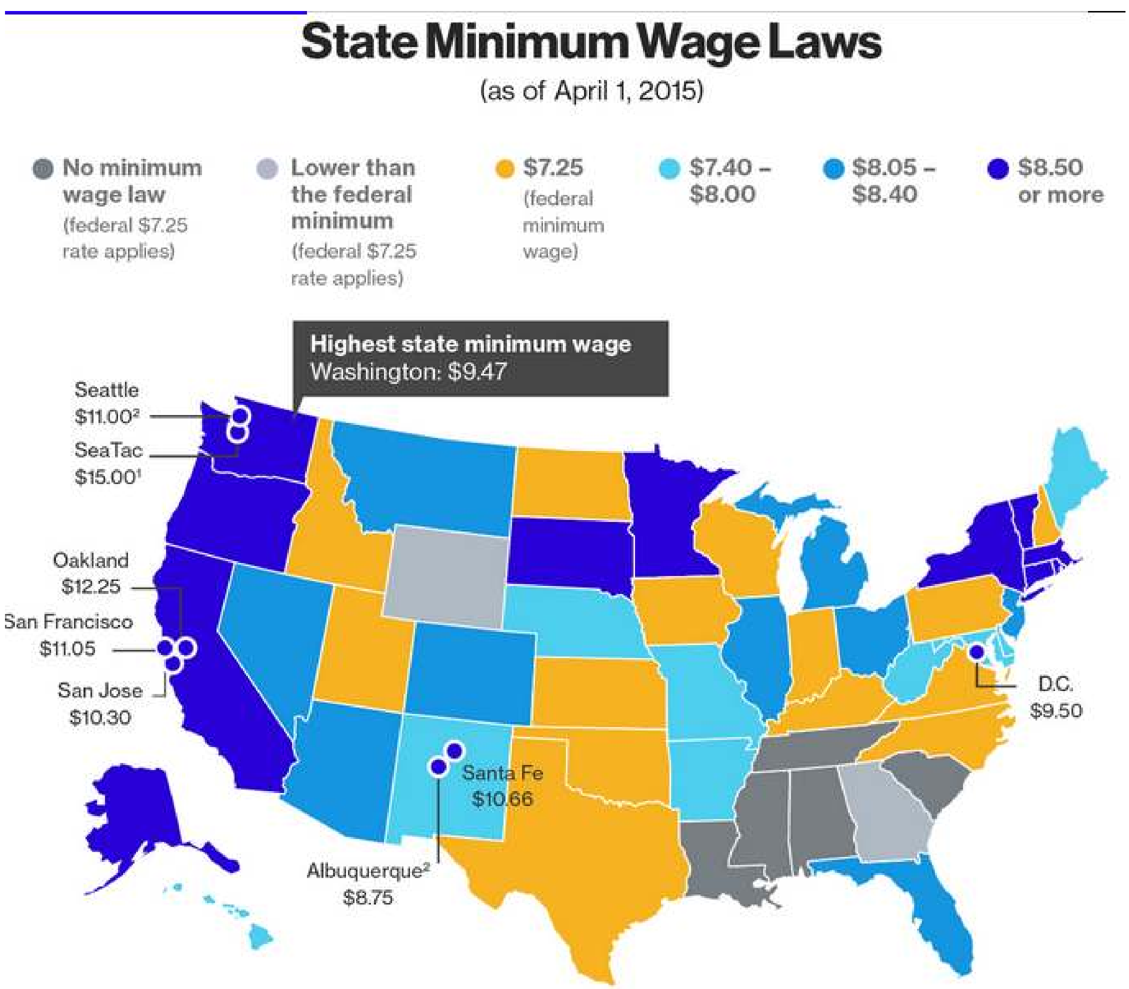
Instead of making her roughly $1,300 monthly mortgage payment, she pays her lawyer $500 a month to represent her in court.

So a bit of poetic justice we suppose for an investment banking community and a complicit Federal Reserve who facilitated the creation of a modern day tulip mania which lined Wall Street's pockets even as it put Main Street (which was itself all too eager to finance a McMansion and a Hummer) on a path to ruin. But in the end, the Susan Rudolfis of the world ask: *"What are you gonna do?"...*

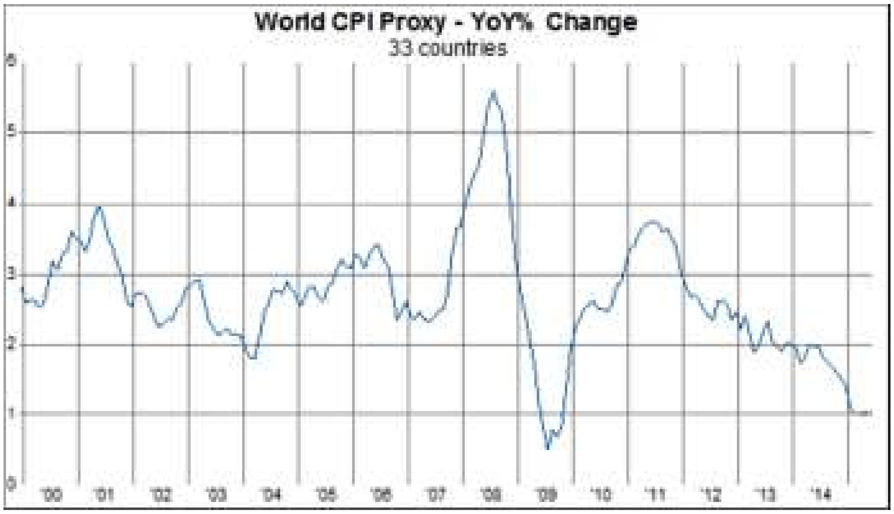
"I screwed up and they screwed up, so now what?" she said.

Nick Comment: Real life is stranger than fiction sometimes!

Below is a chart showing the minimum wage policy across the United States. No wonder why there are 50,000,000 Americans on Food Stamps (SNAP).

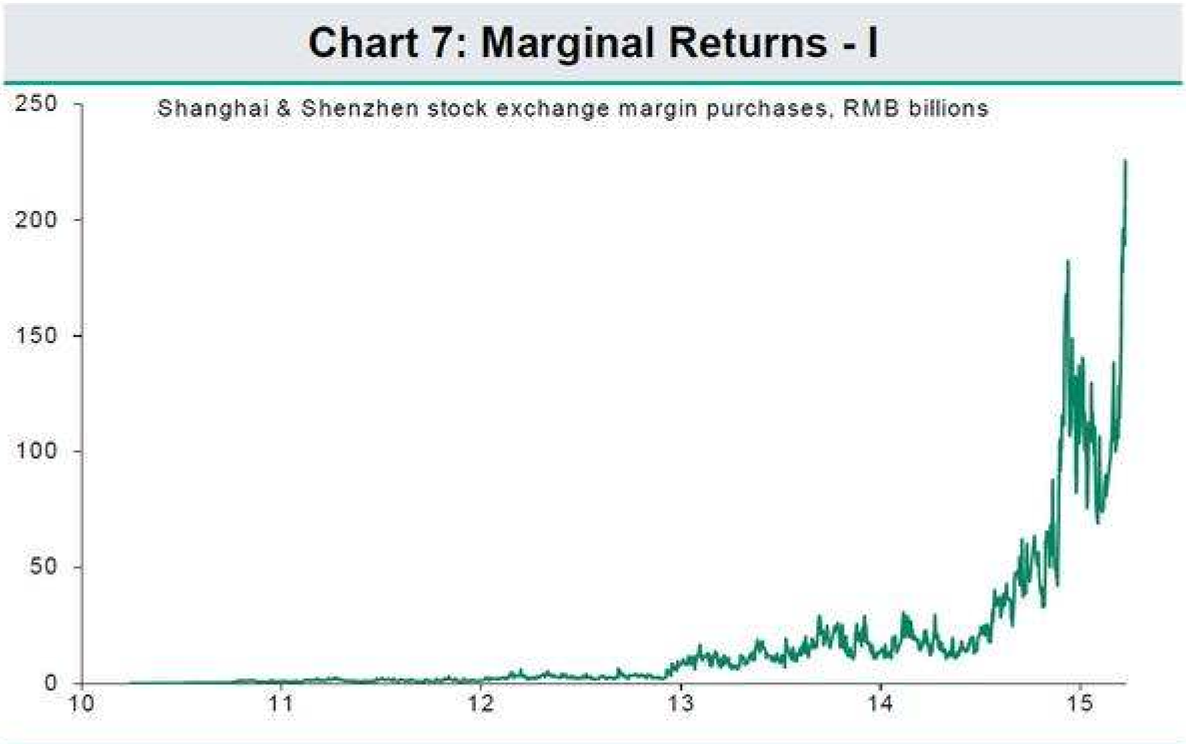


Global inflation is declining…note it is close to where we were in 2009!



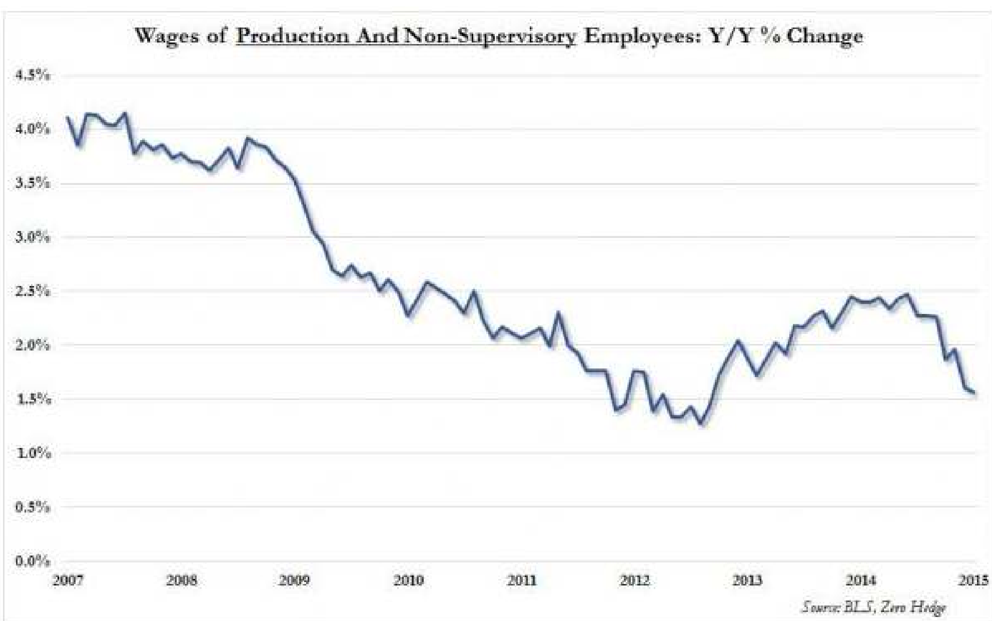
The economic news releases from the US are getting weaker as well. The index below shows the ratio of US economic news releases that are "positive surprises" as compared to "negative surprises".

I found the graphic below rather intriguing. Guess that explains the jump in Chinese stock markets over the past couple of months!!



Source: Macrbond, BNP Paribas

Finally, a look at a wage comparison of “workers” and “bosses”



It is really tough to make a lot of sense out of the economic world today. “Good is bad” because it means interest rates will rise…”bad is good” because it means interest rates will stay lower for longer. Hmmm?

Many of the market BEARS that I read are watching for signs of this relationship to change where “good is good” and “bad is bad” again.

Me, I just sit back and watch with great interest and amazement!

About the author: Nick Foglietta is a Vice President, Investment Advisor at RBC Wealth Management in Nanaimo, B.C., Canada. He has been managing money since 1988.