March 7,2018

MARKETS ARE PRICED FOR PERFECTION YET ARE FAR FROM IT!

Good Afternoon To All

We can now add the sudden departure of Gary Cohn from the Trump Team as one more uncertainty for the markets going into 2018. Cohn was perhaps the most cerebral and sound ADULT on the team and his departure now raises serious concerns over more US import tariffs, global trade wars, inflation and ultimately a US recession!

The number of market hurdles keep growing day by day and although there remain “positives” the negatives FAR OUTWEIGH the positives from my vantage point.

The recent surge in volatility tells me that the markets are also sensing this growing list of uncertainties and negatives.

THE NEGATIVES:

#1 A New Fed Chairmen—J Powell

-recall that on his first day as Chair the DOW had a massive sell off and the VIX saw its largest one day move ever!

-we have now had the first new Fed testimony in front of Congress and the market’s declined dramatically as he was surprisingly hawkish (i.e. possible 4 rate hikes in 2018 vs 3)

#2 More Chaos in the White House

-the history books will surely view Trump as a “one of a kind” and so far the markets have turned a blind eye but that may now be changing with Gary Cohn’s departure? I fear worsening global relationships going forward and more trade wars?

-never has a US President NOT visited Canada in the first year…this insular view is not good…

-to quote a very smart and reliable client—“he is running the White House like a business” which means the top 10% win but bottom 90% lose…PLEASE READ the J TEPPER article below as to why US workers are NOT getting any raises….if the middle class fails then capitalism and the economy fails…I do NOT see any improvement in the middle class over the last year and suspect their weak spending will be the nail in the coffin for this cycle especially as the FED raises rates in 2018!

#3 Housing is WEAK

-all the recent data on housing is very poor…this was my one hope for the US but now that mortgage rates have increased I suspect further housing weakness ahead

#4 Auto Sales Weak

-this is a reflection of the weak middle class and over leveraged credit cards and weak wage growth (on top of inflation)

#5 Surprised Economic Weakness in 2018

-this is the minority view but I follow ECRI and they say the US and global economies have peaked and are now rolling over…YET MARKETS are priced for perfection….a worry if this comes true at a time of rising rates

-The Citibank Economic Surprise Index is now negative for the first time in almost two years…this index reflects incoming economic data and whether it is better or worse than expected

-the Chicago Fed Nat Activity Index also reflecting this weakness

-NOW add in the new TRUMP trade wars in 2018 and we could have a problem

#6 Markets Remain Very Frothy

-the total market cap of US companies vs GDP is now at an all-time high of 152% vs 146% during dot.com

-YET there are only ½ the number of publically listed companies!!!...think about that and then READ J Tepper article below please

-the worry for CURRAN is that this frothy valuation is occurring at a time of rising rates and risk…

-the US market is the most expensive with a CAPE ratio of 32x, vs the EU at 22x vs Emerging Market at 18X…and as you all know I have focused on the latter two over the last year when adding equity positions

#7 Central Banks Are Tightening

-we know about the US Fed and the ECB but now even Japan is saying they will start tightening soon…that is the 3 major global players

-what readers need to know is that by many measures the central banks are still in "emergency mode" wrt monetary policy…the FED for example has its fund rate in the 1.25% range and way back in 2000 when Lehman Brothers were in bankruptcy and the US economy was in the worst recession since WW2 <u>the Fed Fund rate was only2%... yet here we are still in emergency mode????</u>

-to me this is UNCHARTED and I worry what 3-4 rate hikes in 2018 will do for the massive Corp debt (esp. the junk bonds) , auto loan debt, credit card debt, student debt, rolling mortgages….

<u>#8 Midterm Elections</u>

-these are just around the corner and historically markets react before these elections in the fall…

THE POSITIVES:

There is no doubt that there are positives (as why else would markets be so frothy???)--

#1 No Recession Seen in 2018…99% of analyst-economist are still saying no recession in 2018 so “buy the dips” is the main strategy which supports higher markets..I am an outlier here as you all know—so we will see

#2 Share Buy Backs are at record levels in 2018 thanks to Tax Reform and repatriation…this will help the bottom line in 2018

#3 Leading Economic Indicators still positive

#4 Unemployment claims still very low and this is a very good leading indicator

#5 Earnings expectation growth for 2018 is at 18%!! If this materializes it “supports” higher markets…but ECRI says caution here

<u>CONCLUSION</u>

As always there are positive and negative economic views which investors must deal with when evaluating and pricing equity markets.

The recent TRUMP Tax Reform is a clear positive for the US Corp bottom line but one has to wonder how much is now priced in, recall that the markets are very forward looking.

From my perch, I see the markets as “priced for perfection” and it really worries me that we are seeing so much volatility in the markets these days. I wonder if this is not the “canary in the coal mine” signal from the markets that all is not well OR AT LEAST that things are starting to turn?

The number of uncertainties (recall in our last communication re the number of “rare” events) keep accumulating on a daily basis it seems…Gary Cohn (the Presidents “most creditable economic advisor”) , new unexpected trade tariffs, a new and hawkish Fed, growing trade wars, NAFTA, future monetary and fiscal policy etc. For example, Paul Tudor Jones recently stated that “a budget deficit of 5% of GDP is unprecedented in peace time outside of recessions” and I will add that we are also at 9 years into a cycle---uncharted, uncharted!!

However, my main anxiety with equities has been the extreme market valuation during a time of massive debt levels and rising rates! This has NEVER been a good time to be full on in equities (especially at year 9 in the cycle…) and my frontal lobe cannot get past this! Buying HIGH always seems like such a bad idea based on history!?

My simple viewpoint is that there is just no way markets are pricing in all this risk and volatility!

Consequently we will remain focused on more defense than offense!

This has been an easier pill to swallow over the last few months as ALL markets have been weak and so relatively speaking we are doing just fine. As we move into the summer I expect more volatility and hopefully a better entry point for our idle cash!

Please make sure you read some of the more important attachments listed below

Terry

ATTACHED PDFs

#1 Jonathan Tepper—**A MUST READ BY ALL CLIENTS!!!**

#2 Gary Shilling—“extreme cation and large cash position”

#3 EPB Macro—Buffett and $116 b in cash—follow his actions folks!!!!!!!!!!!!!

#4 Stephen Roach—brilliant

#5 Gun Control-GREAT READ!!

#6 When Speculation Has No Limits

#7 Fed Debt…

#8 US Fin Condition Index= market top

#9 US savings…big worry for me…where does future spending come from????