CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

January 1, 2017

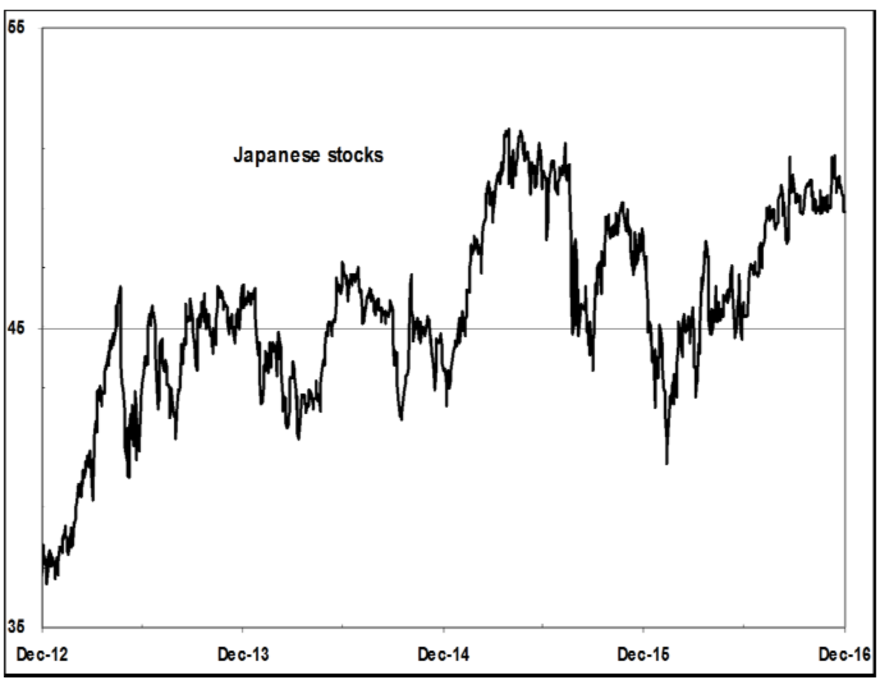
Uncertainty as the Year Turns

After a perplexing 2016, we enter 2017 with a new president about to take office. Stock markets rallied after his unexpected election.

What's next?

2016 is in the books, a tumultuous and surprising year in politics. The June referendum in Britain about leaving the European Union--a very unwise political gambit by David Cameron--was expected to result in affirmation of the UK's continuing in the EU. Nope. Then, in our own presidential election, the widespread belief, which I shared, was that Donald Trump was barely a serious candidate for the Republican nomination and that, once having secured the nomination, he would likely fail in the general election. Wrong again. The very confident prediction of stock market analysts as the November election approached was that, if Mr. Trump should win, the stock market would fall. Oops. The stock market rallied sharply from election day until mid December, when it began to level off.

Given this, is it plausible to make predictions about 2017? There is one prediction about which one can have reasonable confidence: Uncertainty lies ahead. The *post hoc* explanation for the rally was that the incoming Trump administration, supported by Republican majorities in both houses of Congress, would cut burdensome regulatory requirements on businesses, commence large-scale infrastructure projects, and reform tax policy, especially by cutting taxes on corporations. Indeed, some of this may be accomplished and the result may be that corporate profits rise, underpinning the US stock market. A president may, without Congressional approval, change some existing regulations. However, for many, statutes prescribe the means to regulate and de-regulate. Changing regulations may require public comments and the changes may be challenged in courts. Reformation of tax policy is a legislative matter. Congress enacts tax legislation; a process that surely takes time. And, as for infrastructure spending, Congress barred Obama administration attempts at public works; Republican leaders in both houses have fairly recently expressed disapproval of more infrastructure spending. Mr. Trump, though now a Republican, is not cut from the same cloth as most Republican House and Senate members, and many policies he put forward during his campaign are not traditional Republican ones.



As a result, the somewhat euphoric stock market reaction to Mr. Trump's election may not be well founded or it may have been premature. We will know more about all this after January 20th when we see the interplay between Congress and the new administration and when we see what precisely Mr. Trump puts forward.

By

Jack Mayberry

On the first page is chart of Japanese stocks, which receive singular support from Japan's central bank. Among other assets, the central bank is buying Japanese equities. We have an investment in Japanese stocks.

Another uncertainty may arise from actions by adversarial countries to 'test' the new president. Consider China: it has asserted control over vast areas of the South China Sea, far greater than recognized by international law. The United States has resisted China's efforts by sending its naval vessels into such areas. Shortly after his election, Mr. Trump had a telephone conversation with Taiwan's president and, afterwards, disparaged the One China Policy, to which the United States has subscribed since the late 1970s. He suggested that adhering to it might be subject to negotiation. Thereafter the Chinese navy picked up a US underwater drone within international waters but within the area that China claims as territorial waters. The vessel was returned to the United States in a day or two, but China appears to be sending a message to Mr. Trump. What might it do after January 20th? Consider also Mr. Trump's campaign threats to impose large tariffs on Chinese goods. As president, Mr. Trump could do so on his sole initiative. A trade war between the world's two largest economies is an unnerving prospect.

North Korea? It has frustrated the efforts of President George W. Bush and of President Obama, joined by Japan, Russia, China (without much vigor), to stop its nuclear bomb and intercontinental ballistic missile development programs. What might the young President Kim Jung-un try next? Russia? Mr. Trump made admiring comments about Vladimir Putin during his campaign and since his election. He has mocked the conclusions of the US intelligence community that it was Russia that hacked various political entities and persons and sought to influence the election. One suspects that Vlad the Revanchist takes the actions he does not out of warm personal regard for Mr. Trump, but because he deems the actions to be in Russia's interests. When the ostensibly admiring Mr. Trump is sworn in, what may Russia do?

Unexpected geopolitical disturbances may present Mr. Trump with some head-scratching dilemmas. But the strength of the US economy and the steady stewardship of monetary policy by the Federal Reserve and the other major central banks will likely keep financial markets reasonably healthy.

I put forward these ideas not so much to discuss US politics and geopolitics, but to note the vulnerability, at least for the next few months, of the stock market. Notwithstanding this vulnerability, the US economy is strong, employment is still growing well and, happily, wages are increasing after a long, long spell. Although higher labor costs necessarily reduce corporate profits and, to that degree, suggest less robust stock market valuations, there is another side to this coin: To the extent workers are paid more, after a long period of rather depressed compensation, that is morally a good thing. Economically it is a good thing also, in that with increased pay will come increased spending and a generally stronger economy. The stronger economy will strengthen corporate profits and will support higher stock prices. A virtuous circle.

Our central bank, by raising short-term interest rates by one quarter of a percent last month, signaled its view of the strength of the US economy. At its December meeting, it suggested that 2017 would see three more quarter-percent rate increases. This contrasts with the situation in Japan and Europe, where economies are weaker and whose central banks are still engaged in aggressive monetary easing and asset purchases. These differences in monetary policy and economic activity account for the strength over the last two and one half years in the US dollar. The divergent policies of the developed countries' central banks suggest that the dollar will become somewhat stronger in 2017. It is also probable that the decent economic strength in the US will persist; indeed, if the hoped-for Trump policies come to fruition, the rate of growth may increase. In Europe and Japan there will probably be modest growth, as well.

Despite weaker growth in Europe and Japan, their stock markets offer better value than does the US market. In part, this arises from the weaker performance of those markets over the couple of years when compared to the American market. We have a modest investment position in Japanese stocks already. Given the large positions in cash and bonds in many of Core's clients' portfolios, we have the funds available to add to these investments when opportunity presents itself.

The festive season draws to a close soon. We wish to express our gratitude to you for the opportunity you have given to Core to supervise investment of your capital and to wish you a happy, healthy, peaceful and productive new year.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

February 4, 2017

Mr. Trump Begins

By

Jack Mayberry

The beginning weeks of the new administration have been bewildering and unsettling. Mr. Trump's ongoing commentaries via his Twitter account show an impetuosity inconsistent with the seriousness of the office he holds. He evinces a disregard for the decades-long alliances that the United States has nurtured carefully and successfully in the post-World War II era. The disparagement of NATO and of our key European allies, the bulwark of America's preservation of peace in Europe, is alarming in the context of Russian revanchism and aggression. Picking fights with China by trivializing its 'One China' policy is needlessly provocative and counterproductive.

The ban on entry of people from seven majority Muslim countries is, apart from being dreadful policy, an example of ill-considered action that caused havoc at airports around the world and engendered angry opposition from across the political spectrum in this country. At the end of the week, a federal court stayed enforcement of the ban temporarily, pending consideration of the legal and constitutional issues raised by the order. Mr. Trump's persistence in spouting utterly transparent falsehoods, including about the numbers who attended his inauguration and the suggestion that he would have won the popular vote but for the millions of illegal votes, directly undercuts the authority he needs for the office he holds.

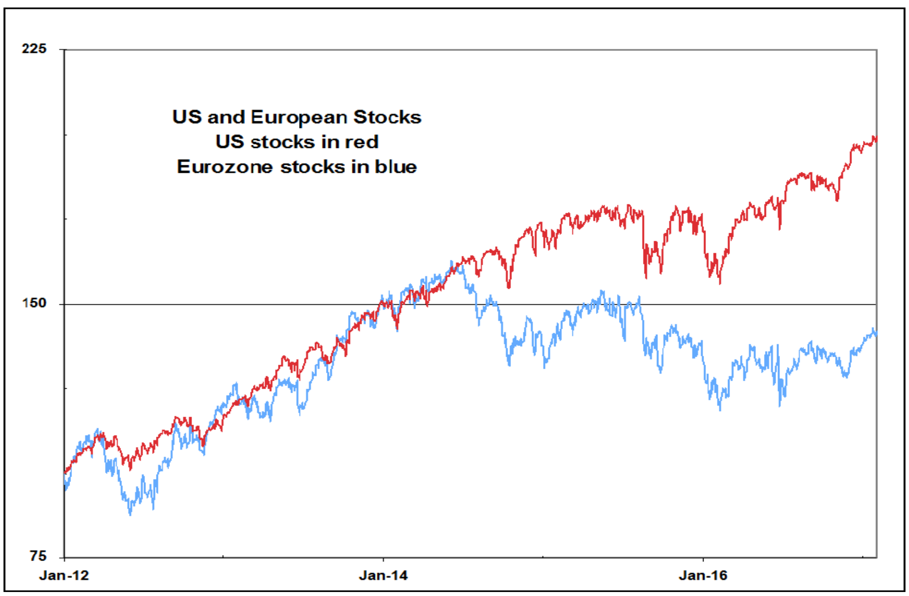
I have no wish to address political matters in these letters that are meant to be discussions about investing. However, given the presidency's centrality to many things in our world, including financial markets, it is rather difficult to write meaningfully about investments while ignoring the havoc unfolding in Washington.

The salient issue as I see it is the crisis that will very likely result from the administration's recklessness and the Faustian bargain that Congressional Republicans struck with Mr. Trump. The agreement seems to be that Congressional Republicans will ignore his financial conflicts and violation of the Constitution's Emoluments Clause, in exchange for the his support for legislative actions dear to the Republicans in Congress. These include its cherished tax ideas, the weakening of banking regulations, and more.

Although Republican members of Congress will not take Mr. Trump to task for financial corruption or violation of the Emolument's Clause, those issues and others will be before a number of federal courts. They will unavoidably arrive at the center of American political discourse. We watched this movie before in the Watergate era of the early 1970s; before too long, we will be watching the remake. Maybe the process will unfold smoothly; maybe not too much damage will be done to America's democracy. Let us hope.

The economy and the markets. The administration's efforts to undo regulatory restraints on various industries continues to provide support for stocks in these industries. In the week just past, Mr. Trump took aim at the drug-testing regime for new pharmaceuticals and undertook to cut the time and cost needed for drug trials. With Congress, Mr. Trump's administration is in the process of rolling back bank regulatory rules developed after the financial crisis. Big banks have lobbied hard against the Dodd-Frank regulations; they wish to take us back to the bad old days when the actions of major banks gave rise to the biggest financial crisis and deepest recession since the Great Depression. Whether the proposed banking de-regulation is in the interest of citizens is open to question. What is not open to question is that the banking industry finds de-regulation to be an unalloyed good thing. The stock market casts its vote with the banks.

Although the subject seems slightly trivial when measured against the political mayhem, we can report that the US economy remains reasonably strong and the economic growth is well-balanced. Another quite strong employment report on Friday exemplifies this. Moreover, economies are growing in Japan and Europe, as well. After several years earlier this decade, when the Eurozone crisis appeared ready to blow the lid off things, a relative calm prevails there and we can expect economies in the developed world to continue to grow at a decent pace.



The adjacent graph illustrates the difference in US and European stocks in the last few years. The Eurozone crisis suppressed economic activity and its uncertainties caused European stock markets to lag the US market from the middle of 2014. Although Europe has its own share of political uncertainties now—consider the Brexit vote and the rise of right-wing parties in many countries—there is economic growth now. Core has abstained from investments in European stocks for some time, but there appear now to be good value and prospects in European stocks. We anticipate making investments there.

The situation in Japan is somewhat similar. We have Japanese stock investments now; we think that valuations and prospects for Japan to be favorable, as well. We may add to these.

These are fraught and uncertain days in the political realm. Will political turbulence spill over into the economies of the developed countries? Will this turbulence upset financial markets? It may. We do not know in prospect. There are certainly good reasons for caution in investing. But we should keep in mind the resilience of our large economy and the arc that bends toward a good future. Crises come and crises go. With effort and persistence, America makes its way past present grimness toward a more enlightened future, notwithstanding the dark fears propounded by Mr. Trump.

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CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

March 25, 2017

Politics... cannot be ignored

Once again, we must ground our investment discussion in the political context. Three matters loom large and undercut the confidence investors expressed after Mr. Trump's election.

The unsupported allegations by our new president that his predecessor had wired-tapped his campaign and Trump Tower in New York are one. The second is the question of Russian interference in last year's election and the Trump campaign's coordination with Russia. The last is the failed attempt to 'repeal and replace' Obamacare.

These undercut confidence in the new administration and put in doubt the continuation of the 'Trump rally.'

By

Jack Mayberry

Previously I have expressed reluctance to write about politics in these letters about Core's investing for its clients. But politics looms so large in US markets these days that to avoid the discussion is to write an investment letter devoid of meaning. So, here we go again. First the politics, then its relationship to investments.

Politics. Matters now include our new president's recent allegation that his campaign and the Trump Tower were subject to surveillance ordered by President Obama. He offered no evidence for this and it has been roundly denied by the FBI, by British intelligence organizations (dragged into the matter by Mr. Trump's subordinates), and by officials at the head of US intelligence agencies last year. Investigations are underway by Congressional committees. The Republican and Democratic leaders of the investigations report that there is no evidence to support Mr. Trump's allegations. James Comey, head of the FBI, concurs. In effect, Mr. Comey and others say that Mr. Trump lies about this.

The second political matter involves reports that the Russian government interfered with last year's presidential election to aid Mr. Trump's campaign and to damage Mrs. Clinton's. The further allegation is that the Russian interference was coordinated with the Trump campaign. This week, Mr. Comey confirmed in Congressional testimony that the FBI has been investigating this matter for eight months. A good deal of information bearing on these quite serious questions has become public. Foreign interference in our elections is grave; participation by a campaign in that interference can be deemed treasonous. This week we learned that the FBI is conducting a criminal investigation of the president's campaign.

The third is the failed attempt by Mr. Trump and House Speaker Paul Ryan to repeal Obamacare and replace it with a hurriedly put-together substitute. The principal 'merits' of the Republican's proposed bill included a major tax cut for the wealthy financed by dropping health care for the needy. Note that after Mr. Trump made a concerted effort to get recalcitrant Republicans to vote in favor of the legislation, it was withdrawn yesterday from consideration and no vote was held. This is a failure by the President and the Speaker to bring to fruition important legislation in which they both invested a big pile of their political capital. The failed project may well render upcoming matters—tax 'reform' and infrastructure spending—rather more difficult to accomplish.

From politics to investments. Mr. Trump's election as president was not expected. But, when the votes were counted, global financial markets switched gears and stocks--particularly in certain industries--began a big rally. For exam-

The rally in bank stocks showed the potency of the hoped-for de-regulation of banks and the weakening of Dodd Frank.

ple, bank stocks rose rapidly on the belief that the Trump administration and the Republican-dominated Congress would undo a good bit of the financial regulation enacted after the financial crisis, the Dodd Frank law. The banks consider Obama-era regulation after Dodd Frank to hamper their desires to do what they will with other people's money. (Indeed, it did.) The new administration can change some regulations and\or simply fold arms and cease enforcement of others. Financial markets anticipated this and bank stocks flourished after the election. And not only bank stocks: At its recent peak, the broad US stock market, as measured by the S&P 500 index, had rallied by 12 percent since Election Day.

The three pillars of the Trump rally have been de-regulation, tax 'reform,' and infrastructure spending. With the political headwinds, tax 'reform' and public works spending seem less likely.

Investors also expected that the Republican-controlled Congress and the Trump administration would (a) de-regulate other industries, as is probably unfolding somewhat beneath the radar, (b) enact tax 'reform' to favor the rich and business interests, and (c) stimulate the economy with big infrastructure spending (formerly known as public works). These three broad factors propelled the post-election rally. Until the sharp selling on Tuesday, the S&P had gone some 109 sessions without a decline of one percent, a placid and persistent rally. It may be the case that the failure of stocks to gain since the beginning of March and this week's sharp selling squall arose from the realization that the political problems discussed in the opening paragraphs will forestall tax 'reform' and the trillion dollar infrastructure building promised by Mr. Trump in his campaign. Without these hoped-for goodies, the fuel for the Trump stock rally has weakened.

Europe and Japan offer opportunities for investment less troubled by the chaos in Washington. Core's investments there are performing well; we expect to add to these.

Elsewhere in the world. The US stock market makes up about half the total capitalization of all the world's stock markets, although the US economy and the US-domiciled companies comprise quite a bit less than half the world's economic activity. For lots of reasons the US stock market looms as large as it does. Some has to do with the political role the US plays with its extraordinary web of global alliances; some with the US reputation for the rule of law and respect for its judicial process; some with its fairness and leadership in global affairs; some with the role of the US dollar as the world's reserve currency. The present administration appears to be turning its back some of these, by disparaging NATO, by antagonizing allies (consider Germany, Mexico and Australia), by picking fights with China, the principal rival power to America, and by denigrating its co-equal branch of US government, the federal judiciary, in the judiciary's review of the patently unconstitutional Muslim bans put forth as executive orders by Mr. Trump. Unless and until we observe Mr. Trump's support for the various pillars of US strength, it is wise for investors to look beyond US markets.

Europe and Japan are the principal markets of world's other developed economies. As noted in recent letters, stock markets there and their economies have been weaker than America's. And, whereas the Federal Reserve, our central bank, has been tightening monetary policy in recognition of favorable economic conditions here, the European Central Bank and the Bank of Japan are still fully engaged in easing monetary conditions to support those economies and--whether intentionally or no--to support their stock and bond markets. These efforts bear fruit: Economies in Europe and Japan are growing and the growth is being reflected in their stock markets. Europe has its own political problems, somewhat akin to those presented in America, including the British vote to leave the European Union, and the rise of 'populists' and authoritarian figures somewhat resembling Mr. Trump in their appeal to the frustrated. Notwithstanding this, the long underperformance of Japan and Europe stock markets, when measured against America's, is turning. For defensive, as well as for opportunistic reasons, we plan to increase our investment allocation to Europe and Japan.

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CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

June 4, 2017

Stocks March Higher, Quietly

Markets are ignoring geo-political problems and the chaotic situation in Washington. Expectations for favorable tax and infrastructure legislation have been forgotten. The focus instead is on the steady economic growth and rapidly growing corporate profits. These are lifting stock markets.

Since I last wrote one of these letters, stock markets in the US, as well as in Europe and Japan where we have substantial investments, have pushed higher. The placid advance in stock markets has unfolded despite the chaotic activities of our radical president, the investigations relating to Russian influence during the presidential campaign, and alarming missile launches by North Korea. This provides yet another example of the insouciance of investors about the impact of political events. To a large degree, financial markets assess the short-term impact of geopolitical events and ignore those that seem unlikely to have a big impact in coming months. Is North Korea's development of atomic bombs and intercontinental ballistic missiles whose range is designed to include California alarming? Of course. Mr. Obama is said to have told Mr. Trump in their post-election day meeting at the White House that North Korea would be Mr. Trump's biggest and most difficult foreign problem. However, market participants judge that North Korea will not launch nuclear weapons toward the US or elsewhere in coming months. Hence, no need to take defensive investment actions now; doomsday is, at the very least, months away.

As written in recent *Core Comments*, the stock market rally sparked by Mr. Trump's election was predicated on the idea that at least three things would happen with Republican control of the White House, the Senate and the House of Representatives. Firstly was the expectation that de-regulation of banking and of environmental things would stimulate heretofore restrained-by-regulation industries. Secondly was proposed public works spending that might be as much as one trillion dollars. Thirdly was anticipated tax 'reform,' whereby taxes on the rich and on corporations would be cut. In the aggregate and individually, these actions were expected to stimulate growth and to enhance corporate profits, all to the benefit of the stock market. As it has developed, a good deal of de-regulation is entirely within the control of the Trump administration and has been proceeding apace. Although legislation will be required to undo much of Dodd-Frank, an unwillingness by the present administration to enforce aspects of Dodd-Frank is enough to lift many regulatory restraints.

However, the general chaos in the White House and the difficulties in repealing and replacing Obamacare render it more difficult to enact tax 'reform' or infrastructure legislation. As a result, the impetus for the ongoing advance in stock prices must come from elsewhere. Some candidates: Economic growth in Europe, Japan and the US has been reasonably strong, at least by recent standards. As a result, corporate profits, especially in America, have been on the upswing, after modest slowing in the last year and more. And, importantly, the still exceptionally stimulative monetary policies of the leading central banks provide a strong tailwind for asset prices. Although the Federal Reserve is

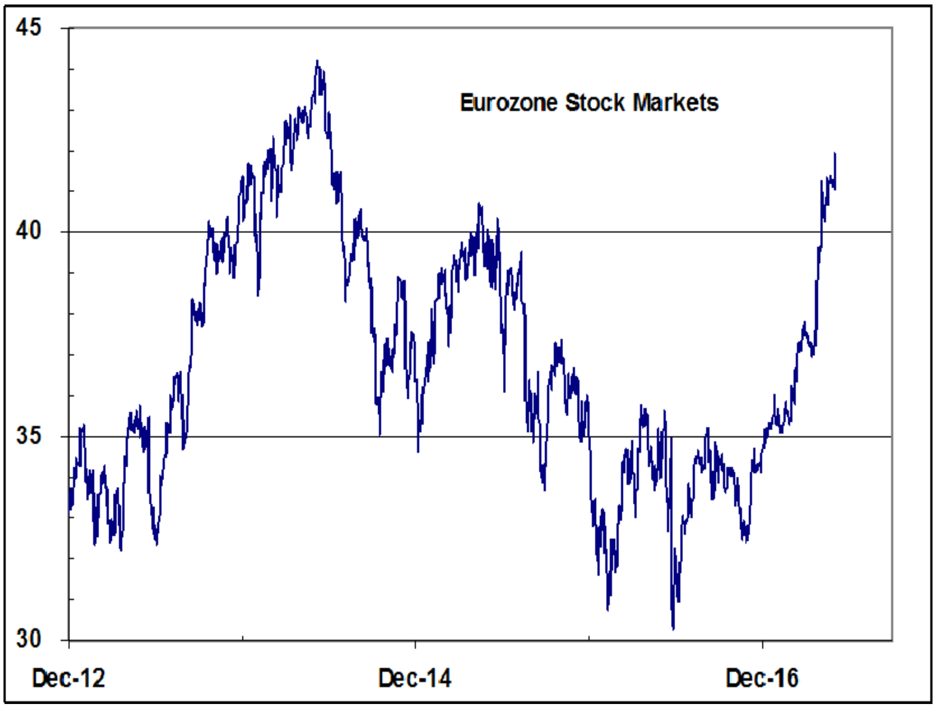
By

Jack Mayberry

Europe and Japan enjoy modest economic growth and are cheaper than America's stock market.

Core has been increasing clients' investments in Europe and Japan.

slowly raising the short-term rates it directly controls and although it is no longer expanding its balance sheet with its 'Quantitave Easing' bond purchases, it continues to by US treasuries at a rate of some $30 billion per month to replace the maturing securities it holds. Meanwhile, the European Central Bank (ECB) and the Bank of Japan (BoJ) are buying new securities in huge quantities, with the result that, in the last year, the ECB, the BoJ and the Fed have purchased $1.8 trillion dollars in securities, providing enormous liquidity and support for stock and bond markets in developed countries. Thus assets on the balance sheets of the Fed, the ECB, and the BoJ now total more than $12 trillion, up from about $3.4 trillion before the financial crisis of 2008 and 2009. It is hard to overstate the importance of this ongoing central bank largesse to stock and bond markets.



Europe and Japan. In Core's letter in early February, I presented a chart to illustrate by how much US stock markets had outperformed those of Europe. The Euro crisis of 2012 and 2013 stopped stock European stocks markets, while the US market kept moving fitfully upwards. Now, with the ECB acting aggressively to keep the Euro intact and European economies growing, with the recent elections in France and the Netherlands in which challenges from the nationalist far-right parties have been seen off, Europe appears to be stable politically and its stock markets are catching up with America's. And, by comparison with US markets, Europe's offer better value and lower prices. Capital is moving to Europe in growing amounts with increased confidence.

The situation in Japan is different; there has not been a crisis with its currency, long seen to be the primary haven, even more so than the dollar, in times of uncertainty. But its poor demographics—an aging society essentially closed to immigration—its on and off deflation and its chronically weak economy all have restrained its economy and its stock market. But Japan's present prospects are also favorable and it too presents value when measured against the US stock market. Core has been increasing its investments in Europe and Japan and we anticipate good returns from these.

In sum, conditions in the economies of Europe, Japan and America are favorable. The favorable conditions are being reflected in increasing earnings by corporations and, as a result, in higher prices in stock markets. As we near the middle of this calendar year, these favorable conditions and higher stock prices seem likely to persist for the rest of this year. As always, external conditions can change things and, with our rather unpredictable president, the political situation in Washington has the potential to upset the apple cart. Perhaps we are a bit sanguine, but at present and as portfolio values rise, we are fairly relaxed about things.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

July 21, 2017

A Placid Year Passes the Halfway Mark

Stock markets in the US, in Europe and in Japan have grown steadily this year. Political disturbances and the absence of promised, pro-growth policies from the Trump administration and the Republican Congress have not disturbed financial markets.

The US dollar has fallen, particularly against the euro. Subdued inflation trends in the US have caused many to expect that the tighter monetary policy by the Fed will be slower than the Fed suggests.

Without too much conviction, we think the Fed will keep to its course and the dollar will strengthen again.

By

Jack Mayberry

Modest but constructive progress continues in the markets. Despite our volatile and disruptive president, alarming and dangerous actions of North Korea, and the confounding inability of the Congress to make legislative progress, the US stock market has moved forward in an undisturbed way. This week, it reached new highs again. And in Europe and Japan, where Core has significant stock investments for clients, stock markets have been also been strong, indeed, stronger than the US market. In the US, corporate profits grow at a decent pace, while the economy moves forward at an unexciting but steady rate. Similarly favorable conditions obtain in Europe and Japan.

The dollar and the euro. To us, the surprise this year has been the weakness of the dollar against both the euro and the yen. The US dollar continued to strengthen in second half of last year, largely because the Federal Reserve was beginning (ever so gradually) to raise short-term interest rates while the European Central Bank (ECB) and the Bank of Japan (BoJ) were engaged in massive programs of quantitative easing (QE) and seemingly a very long time away from any tightening of monetary policy. This quite reasonably and directly caused US interest rates (low though they be in historical terms) to rise a bit and almost to assure that US rates would be meaningfully higher than those in Japan and Europe for a long time to come. Higher rates in the US attract capital to dollar securities and draw capital from the low-interest rate regions of Europe and Japan. Thus the dollar appreciates in value against those currencies.

Not so this year. The euro fell to $1.04 late in 2016--a huge decline from the $1.40 to $1.60 range that prevailed a few years ago. But this year, the euro has strengthened to $1.16. The view seems to be that with sustainable economic growth across the Europe, the ECB will in a short time begin its own normalization of monetary policy, raising short-term rates and slowing its bond-buying program. To my mind, the strength of the euro is unlikely to last. Despite low inflation in the US, the Federal Reserve will likely continue its gentle rate-raising process and will probably begin to reduce its huge mountain of securities purchased in its own quantitative easing exercise. In my view, it will be quite a long time before the ECB begins monetary tightening. Hence, US interest rates on short- and on long-term securities will rise while European rates remain vanishingly low. The result will be a stronger dollar and a weaker Euro.

America First. This was the slogan Mr. Trump used successfully in his campaign; his policies since taking office are often framed with that term. It is puzzling, to put it mildly, to consider the isolation of Mr. Trump in the recent G20 meetings in Hamburg and to wonder how his policies and conduct advance the America First project. Mr. Trump has withdrawn the United States from leadership of the world, leadership nurtured by all presidents of both parties since the end of the Second World War. He sunders the broad and deep web of alliances that America has developed and nurtured over decades and diminishes the standing of the country with his impetuous behavior and malign rants against women and the press.

While campaigning, Mr. Trump breezily promised that his administration would undertake policies that would raise America's economic growth rate (GDP) to 4%. For a long number of years, America's GDP has been well below that; since the Great Recession ended, it has been about 2%. Economists rolled their eyes with Trump's 4% prediction. In his budget outline and projections for the next ten years, his Treasury Department predicts 3% growth, by which America's federal deficit would be reduced to zero. The bipartisan Congressional budget office, duty bound to analyze it, predicts the deficit will stabilize at about $700 billion per year, whereas it has been $450 billion in the last twelve months, remarking that, because details about possible policies are unavailable, it cannot analyze "their macroeconomic effects or the budgetary feedback that would result from those effects."

Trump administrations projections of more rapid economic growth seem more like political puffery that reality-based economic modeling.

As discussed in previous letters, the hoped for policy changes--tax 'reform' and infrastructure spending, among others--have languished in the chaotic beginning months of the administration, marked by its unwelcome and unsuccessful efforts to 'repeal and replace Obamacare.' Thus, stimulus to growth is on hold while the administration considers (and threatens) policies that will likely cause growth to slow. Consider the economy-slowing effects of imposing tariffs on steel; consider the effects of Mr. Trump's wall and renegotiation of NAFTA, the North American Free Trade Agreement.

Monetary policies of the major central banks have provided a very good deal of support for bonds and stocks. In the coming years, there is every possibility that central banks will tighten monetary policies. Tighter policies will be headwinds for the markets.

Central Bank Assets. Since 2009, the Federal Reserve and the other major central banks have engaged in unprecedented monetary policies, including QE by which the central banks buy enormous quantities of bonds. There is serious disagreement about the extent to which QE has supported the real economy. We need not address that matter here. What is beyond dispute is that QE has had an enormously positive effect on the market for bonds and for stocks around the world. Bond prices and stock prices have reached historic highs in developed countries. The S&P 500 has appreciated by 57% from its highs in October 2007 before the financial crisis and by 272% from its lows in 2009 in the depths of that calamity.

This is well and good. But what happens in the years ahead as the central banks try to 'normalize' their monetary policies by raising short-term interest rates (as the Fed has already begun) and by reducing the assets on their balance sheets. In total, the four principal central banks, the Fed, the ECB, the BoJ, and the Bank of England, hold some $14 trillion of assets, up from about $4 trillion in 2007, before the crisis. For the Fed, the numbers are $800 billion in 2007 to $4.5 trillion now. The Fed has begun to write and speak about how it intends--slowly and gently--to reduce its balance sheet.

Tightening of central bank monetary policies, already underway by the Fed with its four increases in the fed funds rate, is very consequential. Abrupt changes can certainly be expected to cause turbulence; we saw this in May 2013 when then Fed Chair Ben Bernanke first discussed reducing ('tapering') the rate at which it would continue to buy government securities. The 'taper tantrum,' as it came to be called, caused a sharp bout of selling in bonds. Tighter monetary policy is still some way off in time and its consequences do not loom before us now. In time, though--perhaps in a year or two--we can expect central banks to begin the reversal of the ultra-loose, ultra-accommodative monetary policies that have characterized the post financial-crisis era. A new world will then be upon us.

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CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

September 29, 2017

The Quiet and Productive Year Continues

As autumn begins and we enter the year's final quarter, the quiet in markets and the fairly steady, if gentle, upward march in asset prices persists. This has been an unusual year: politics has been contentious and volatile, through the unstinting efforts of our provocative president, while financial markets have been placid, quite undisturbed by threats of from North Korea and general political noise. My recent letters could be repeated here with little editing.

The American stock market has continued to push to new highs every few weeks, including today, and European stock markets have been stronger still. Japan, where we also have investments, has been a bit weaker but still productive. We noted in *Core Comments* several weeks ago our surprise about the strength in the euro . It has drifted about two percent higher since I offered my prediction that the dollar would reassert itself. I still expect the dollar to resume its advance, interrupted early this year. So far, happy economic growth in Europe has outweighed the effects of diverging central bank policies. The Federal Reserve has four times raised the short-term interest rates and has announced that in October it will begin to reduce the securities it holds on its balance sheet. By contrast, the European Central Bank (the ECB) continues to buy securities ('Quantitative Easing') and to expand its balance sheet. It will probably be quite some time before the ECB raises rates, hence the difference between higher rates in the US and lower in Europe will most likely widen further.

A hoary old investing rule holds that one should not bet against central banks. So far this year, those who have bet on the euro and against central banks are ahead. For our part, Core has some of its European and Japanese stock investments hedged into dollars; some are unhedged, giving direct exposure to the euro and the yen.

As expected, at last week's meeting of the Federal Open Market Committee, the Fed laid out its plans for slowly reducing its $4 trillion dollar balance sheet, and it suggested that it would likely raise the Fed funds rate by another quarter percent at its December meeting. Slowly, carefully, and with full disclosure of its plans, the Fed is in the process of 'normalizing' its policies. Short-term rates will probably reach 3% and long-term rates will rise as well. At present, short rates are about 1% and the ten-year Treasury bond yields 2.32%. We can expect both to rise in the coming year to 18 months, implying lower bond prices.

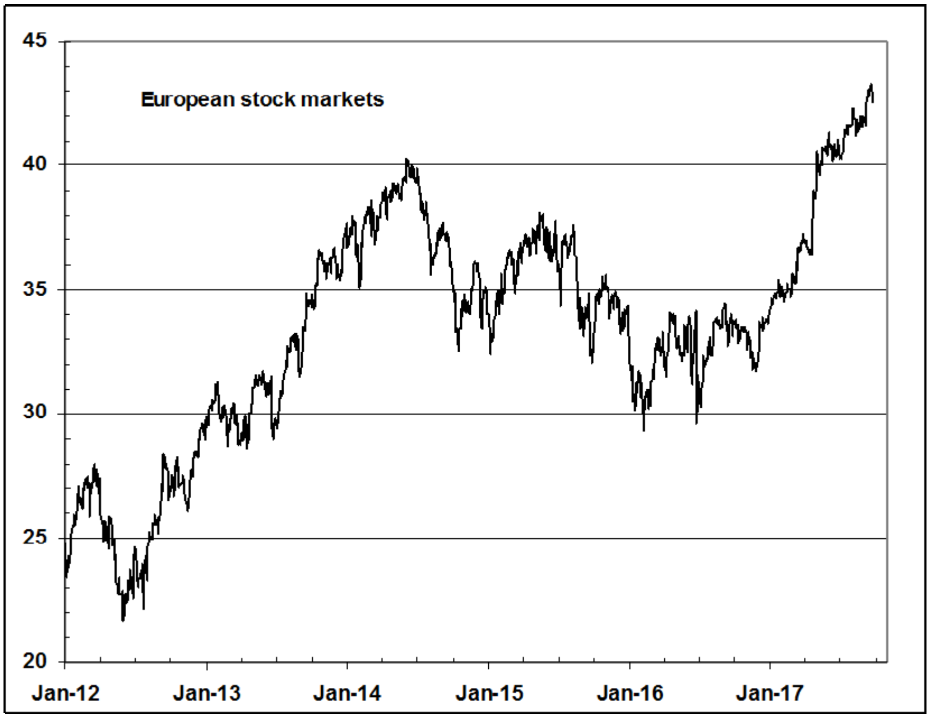
By

Jack Mayberry

With economic growth steady, inflation well contained, and corporate profits growing, we can expect further gains in stock prices in the US. Similar factors obtain in Europe. Hence, a somewhat greater than normal allocation to equities is in order; they are likely to do better than bonds over the next six to twelve months. It is often observed that this is a quite long bull market in stocks and a long period, at least in the US, of economic growth. Does the longevity itself suggest that a recession and a bear market for stocks is at hand? Doubtful.

The chart below shows an index of large company European stocks. After substantial losses from 2014 to 2016, European stocks have rallied sharply. In our view, further appreciation lies ahead.

The German election. After Brexit and Trump's election, there has been well-warranted concern about the rise of populist, nativist, hard-right politicians in Western democracies. Earlier this year, fears for those issues in Europe were dampened by elections in the Netherlands and, especially, in France, where Emmanuel Macron was elected president by a decisive margin over Marine Le Pen. But in Sunday's German elections, Germany's AfD party became the first right-wing party to take seats in Germany's parliament since the Nazis. The pro-Nazi, anti-immigration rhetoric of the AfD gives rise to considerations of a 'Fourth Reich.' Although Angela Merkel won her fourth term as Chancellor, her party and the Social Democrats both lost votes as compared to earlier elections. Perhaps the mantle of European leadership shifts to France and Mr. Macron, from Germany and Ms. Merkel



US tax 'reform.' We have written about the limited extent to which the market-friendly policies on which Mr. Trump campaigned have been realized—and how little that seems to have mattered to the stock market. Infrastructure spending and tax 'reform' have not come before Congress; the administration and Congressional Republicans have devoted their energy to attempts to strip the poor and the sick of medical coverage. But with the latest failure to 'repeal and replace' Obamacare this week, Mr. Trump and Congressional leaders turn their attention to cutting taxes on corporations and rich individuals. Although Mr. Trump spoke about the proposed tax plans this week, information about its content is still limited. From what can be discerned, however, tax cuts would flow to largely to the rich and to big corporations. For example, owners of tax pass-through entities—partnerships, S corps, and LLCs—will now be taxed at 25%, whereas most such taxpayers have been paying 39.6%. State and local tax deductions are to be eliminated, hurting tax payers in states like California and New York. The alternative minimum tax, which has swept many rich taxpayers back onto federal tax rolls, is to be discontinued. Similarly, the estate tax, long in the sights of rich Republicans, will be kaput.

In presenting the tax plan this week, Mr. Trump made the point that it is about tax cuts, not tax 'reform.' His candor is welcome. The overall plan favors the wealthy and its likely effect will be to increase the federal budget deficit. Republicans have generally opposed higher budget deficits, especially when they are caused by spending to support the poor. In the realm of tax cuts however, fiscal conservatives are mute. Investment implications are favorable for stocks, less favorable for bonds. But, what will be the outcome? Can the Republicans in Congress and the White House actually enact what is proposed? This year's experience suggests otherwise.

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CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

November 14, 2017

Changing of the Guard at the Fed

The recent nomination of Jerome Powell to lead the Federal Reserve is consequential. More consequential are the several nominations that will follow this one.

Given the exceptional importance of the Fed to the US and the global economy and its profoundly influential role in the stock, bond and real estate markets, it is hard to overstate the significance of the nominations Mr. Trump will make.

By

Jack Mayberry

In these *Core Comments,* I have often remarked that our central bank, the Federal Reserve, is the largest factor in the markets for stocks and bonds, both in the United States and for the world as a whole. Thus, the chair of the Fed, now Janet Yellen, is widely regarded as the single most important actor in global economies and asset markets. Dr. Yellen's four-year term expires in February and, contrary to the four-decades long tradition of reappointing Fed chairs for a second term, President Trump has nominated Jerome H. Powell, a governor of the Fed, to succeed Chair Yellen.

The nomination of Mr. Powell appears designed to continue--and not to disrupt--the policies the Fed has pursued under Dr. Yellen's leadership. Mr. Powell has never cast a dissenting vote against the policies adopted by the Fed in his five years as Fed governor. Mr. Trump had put forward others as possible nominees, others who would likely have been quite disruptive, indeed. However, the full scope of the administration's plans for the Fed will not become clear until Mr. Trump makes further appointments.

Other Fed openings. The principal leaders of the Federal Reserve are its governors, of whom there are meant to be seven. At present there are only four, Dr. Yellen, Mr. Powell, Randal Quarles and Lael Brainard. Since Mr. Trump's inauguration, two Fed governors have resigned and Mr. Trump has appointed one new governor, Mr. Quarles, as Vice Chairman for Supervision. As such, Mr. Quarles is now the Fed governor with primary responsibility for bank regulation. Mr. Trump has three Fed governor vacancies to fill. Moreover, we learned only last week that William Dudley, the president of the Federal Reserve Bank of New York, will resign by the middle of next year prior to the end of his term. As president of the New York Fed, Mr. Dudley is a permanent member and Vice Chairman of the Fed's Open Market Committee, which sets its monetary policy, arguably making the New York Fed president the second most important member of the Federal Reserve.

Mr. Trump's administration has been avid for deregulation of banks, as have most Republican members of Congress. It is, therefore, entirely possible that, despite the nomination of Mr. Powell as the new Chairman, a nomination that, on its face, argues for continuation of existing Fed policies, we may see in the next year a Fed that reflects Republican views for lax banking regulation and that is much more 'hawkish' about monetary policies generally.

Because of uncertainties about the monetary policies the Fed will pursue, the large number of vacancies at the Fed gives the Trump administration scope for shaping these policies. It is worth pointing out that Mr. Quarles, Mr. Trump's first nominee, and Mr. Powell are both former partners of The Carlyle Group, a prominent New York-based private equity firm, and that neither is an economist by training. In this respect, they are somewhat typical Trump administration appointees, rich white men who are not specialists in the fields over which they are given authority. If Mr. Powell is a nominee for 'continuity' of policy, as is said, why did not Mr. Trump choose the better qualified incumbent, who really would continue the Fed's policies? To pose the question is to answer it: Mr. Trump prefers a rich white man, and not a woman, to be the world's most important economic policy maker.

In light of strident opposition from Republican members of Congress after the financial crisis to the policies of Dr. Bernanke and Dr. Yellen, we may well find that new Fed appointees are ones with a mission to undo recent policies and relax the Fed's bank regulatory policies and actions. Given that the financial crisis was brought about in substantial part by acts of loosely-regulated banks, and given that millions of Americans lost their homes, or their jobs, or both in the crisis, we may come to see a destructive tilt to upcoming Federal Reserve policies.

The Fed's role in the aftermath of the financial crisis was enormous and, in my view, constructive and necessary.

Many disagree with the view that the Fed's actions have been useful and effective. Opposition to them is especially high among Republican members of the House and Senate.

Current Fed policies. As things stand now, the Fed is in early- to mid-stages of 'normalizing' the extraordinary monetary policies put into effect during and after the financial crisis of 2007 to 2009. During the crisis, the Fed cut the short-term interest rates it controls directly, the Fed funds rate, from 5% to zero. At zero Fed funds (and money market funds) stayed until December 2015, when the Fed began a glacially slow process of rate increases. Rates are now 1% and another quarter point increase is expected in December.

Apart from cutting interest rates to stimulate economic recovery after the Great Recession, the Fed also undertook what came to be called Quantitative Easing ("QE"), whereby it purchased for its account US Treasury bonds and mortgage-backed securities. Prior to the crisis, the Fed held $800 billion of Treasury bonds; by the end of its QE program, its assets stood above $4 trillion. The purchases removed from circulation some $3.5 trillion new dollars to the economy. Critics of the Fed characterize QE as the 'printing of money' and disparage the lowering of interest rates as providing an artificial stimulus to the economy. Many predicted that the Fed's actions would cause 'hyperinflation.' Of course, the inflation predictions have been unrealized; by contrast, a principal concern of the Fed has been the persistence of low inflation and risk of deflation.

Beginning in October, the Fed began a slow process of reducing assets it holds, by reducing the reinvestment of proceeds from maturing bonds. Although the Fed has been forthcoming about its monetary policy actions and plans, it is unknown—to us and, one suspects, to Fed policy makers—how high will be raised Fed funds and by how much the Fed's bond holdings will be reduced. With such consequential Fed decisions ahead, Mr. Trump's appointments loom large.

Meanwhile, in financial markets, the steady advances in stocks have continued since our last *Core Comments*. Since that end-of-September letter, US technology stocks and Japanese stocks have led the way; overall stock markets in the US and in Europe have also continued to be strong. Forward-looking economic reports suggest that the US economy is improving its rate of growth. As a result, the likely beginning of the next recession seems well off into late next year or later. Thus, we can have somewhat larger than typical portions of stock investments in the portfolios we manage.

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CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

December 31, 2017

A Quiet and Productive Year Draws to a Close

Global stock markets rose in price throughout 2017 in a year marked by consistently positive monthly returns.

Economic growth in major economies, strong corporate profits, low inflation and favorable central bank policies all contributed to these gains.

The year just ended is notable for the consistency of the stock market gains month after month, for the fact that European and Japanese markets outperformed the US and for the placidity of it all. Day-to-day variation in US stock prices is the lowest since 1964 and the second lowest on record. The calm in stock markets is the more striking in the context of political upheaval in the US and the notable risk of nuclear war between North Korea and the US. Steady and robust returns in Core's clients' portfolios in the course of 2017 are most welcome; may they continue in 2018!

As the year has unfolded, we have commented in these letters about various factors that have contributed to the fine stock markets. These include 'synchronized' global growth (i.e., the fact that all the world's major economies are expanding), strong gains in corporate profits, low inflation, and accommodative monetary policies by the world's major central banks. As for this latter point, although the Federal Reserve is raising short-term rates and has begun to reduce the level of assets on its balance sheet, its so-far mild monetary tightening is offset by the continued extremely loose policies of the European Central Bank and the Bank of Japan. Both of these central banks continue to buy bonds ('quantitative easing') and to keep short-term interest rates anchored near zero. Indeed, many European and Japanese bonds have negative yields.

The newly-enacted tax legislation is intended to spur the economy and raise wages. Maybe.

It may be unneeded fiscal stimulus that will have minimal effect on the real economy while it fattens the purses of big companies and those already wealthy.

As for global growth, China and India are expected to grow at 6.5% to 7.5%. The major developed economies, including the US, most western European countries, Canada and Australia will likely grow at more than 2%. Britain and Japan will probably grow more slowly than in 2017, but still at about 1.3%. The present forecast for growth of corporate profits of the 500 big US companies that comprise the S&P 500 index is 12%. Yields on long-term bonds remain very near their historic lows. Given these factors, it is reasonable to think that stock markets will climb further as we enter 2018.

The tax legislation. As the year ended, tax legislation was enacted. Notably, it cuts corporate income taxes substantially and lowers rates on personal income taxes. Its Republican authors contend that it will increase corporate capital spending and wages. If so, higher consumer spending will follow and economic growth will accelerate. Should things unfold this way, we can expect the Fed to raise rates and to reduce its balance sheet faster than now anticipated, probably resulting in stock market selling and far greater volatility in stock prices than we saw this year just ending.

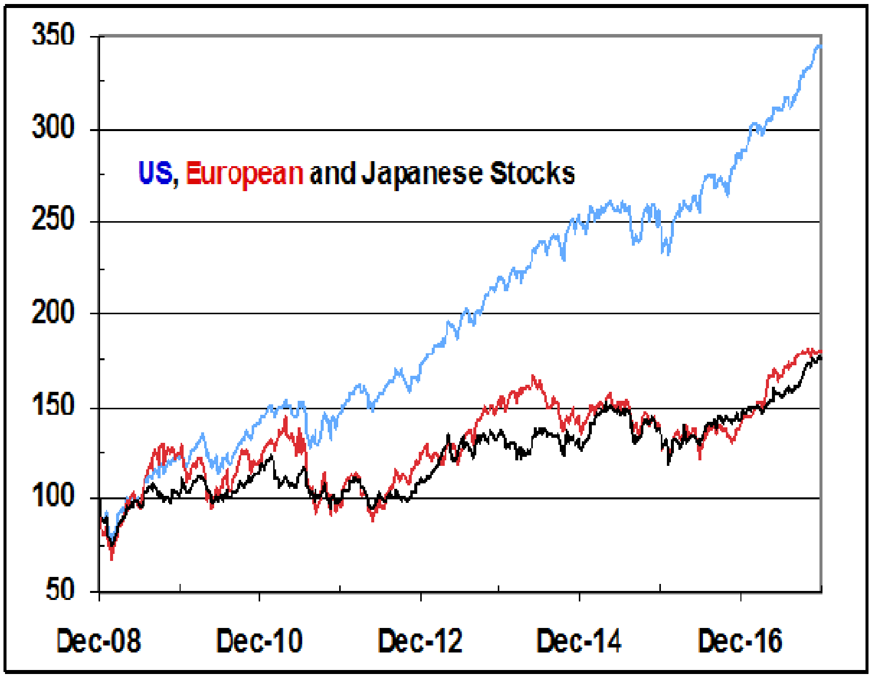
By

Jack Mayberry

Another possible outcome, more likely than the one noted above, is that lower corporate taxes will result in higher dividends to shareholders, more stock buy

In 2017, Japanese and European stocks markets outperformed even the strong US market. Expect more of the same in 2018.

backs and increased spending on corporate acquisitions. In this scenario and without higher wages and capital spending, economic activity will be largely unmoved by the tax legislation. The Fed will move slowly with its interest rate increases and shrinking of its balance sheet. Bond yields will stay low and bond prices high; stocks will likely continue to increase. Economic stimulation from tax cuts will be muted. The characteristics we have observed for several years, including modest economic growth, low interest rates, low inflation and supportive central banks, will prevail, all to the benefit of asset markets rather than the real economy. We may get an indication of corporate plans during the upcoming weeks when corporate earnings are announced. At least some corporations will likely reveal what effects the tax legislation will have on their profits and what plans they have in light of the changed tax regime.



Foreign markets. As noted, European and Japanese markets gained more in 2017 than the US. This follows the long period since the financial crisis during which the US market surpassed foreign markets by a large margin. The nearby chart shows the performance of US, European and Japanese stocks from the end of 2008 to the end of 2017, showing by what extent the US stock market outperformed those in Europe and Japan. (The graph shows the indices rebased to 100 as of the end of 2008.)

Although it is not clear from the graph, in the last year, Japan and (especially) Europe outperformed US markets. Valuations of stock markets in Europe and Japan are more favorable than those here, corporate profits are robust and, as noted, their central banks are continuing their aggressive bond-buying programs, providing a tail wind for asset prices. Our expectation is that we will continue to hold substantial European and Japanese equities in the portfolios we supervise and that their returns will exceed those in the US.

One oddity of 2017 arose in currency markets, in which the US dollar fell in value against most Western currencies and the Euro rose quite markedly. This is odd in that currency movements generally (but not always) reflect differences in short-term interest rates. Thus, in 2017, when US short rates rose, while rates in Eurozone countries remained near zero, the rising Euro and falling US dollar proved an exception to the general pattern. Mr. Trump complained during his campaign about the strength of the dollar; perhaps he can take credit for weakening the dollar. Whether the dollar will continue its mild descent while other currencies strengthen is known but to the gods, and perhaps to Mr. Trump.

At all events, from us at Core, the best wishes to you and your family for a healthy, bountiful and peaceful 2018.

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