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.

By

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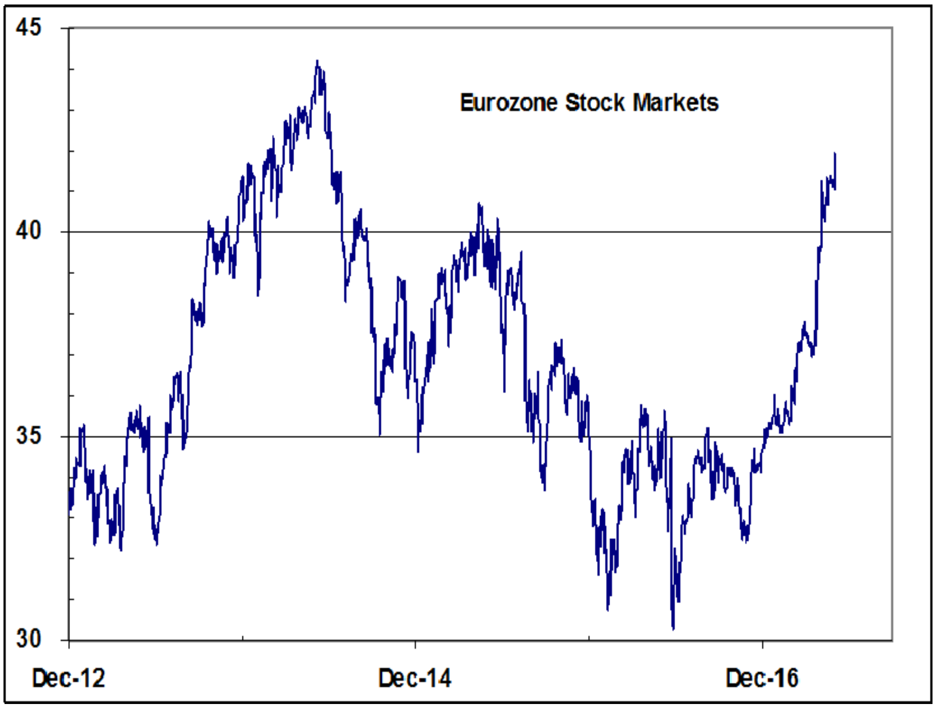
However, the general chaos in the White House and the difficulties in repealing and replacing Obamacare render it more difficult to enact tax 'reform' or infrastructure legislation. As a result, the impetus for the ongoing advance in stock prices must come from elsewhere. Some candidates: Economic growth 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

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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