Dash of Insight

AN ECLECTIC APPROACH TO BETTER TRADING AND INVESTING

Weighing the Week Ahead: Can a Trade War be Avoided?

The economic calendar is normal, and we have a four-day trading week. Last week's big stock decline will surely be on the minds of many. With measures and counter-measures, threats and rhetoric, the trade issue will command the attention of all. The punditry will be searching for signs of compromise, wondering:

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Last Week Recap

Three weeks ago, WTWA asked whether a trade war was underway. I opined that there was plenty of room to pivot away from the initial actions against steel and aluminum. That is what happened. This week the question arises again, and in a more serious form.

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The News

Each week I break down events into good and bad. For our purposes, "good" has two components. The news must be market friendly and better than expectations. I avoid using my personal preferences in evaluating news – *and you should, too!*

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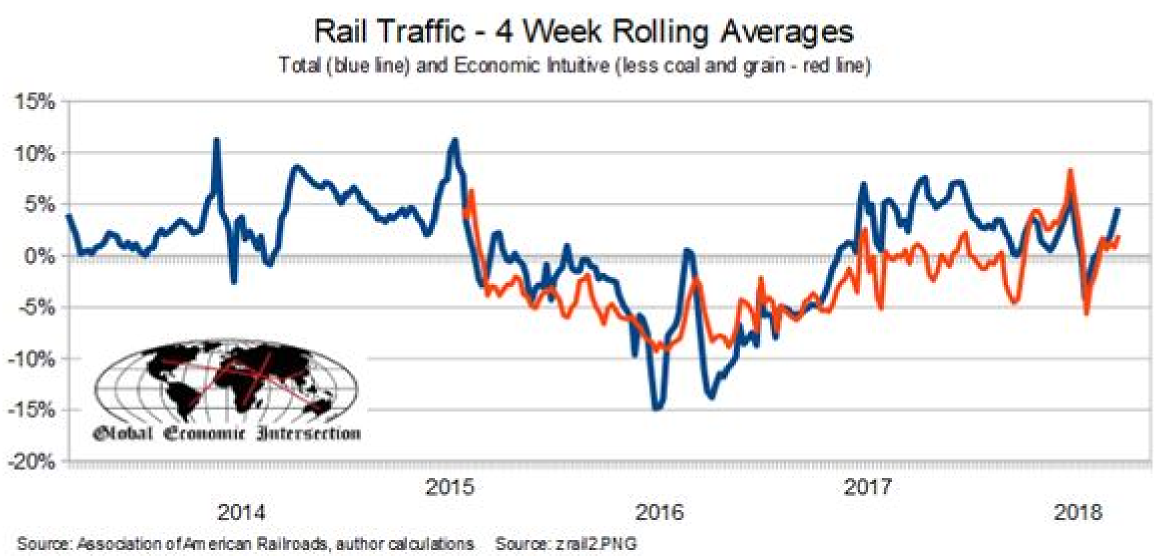

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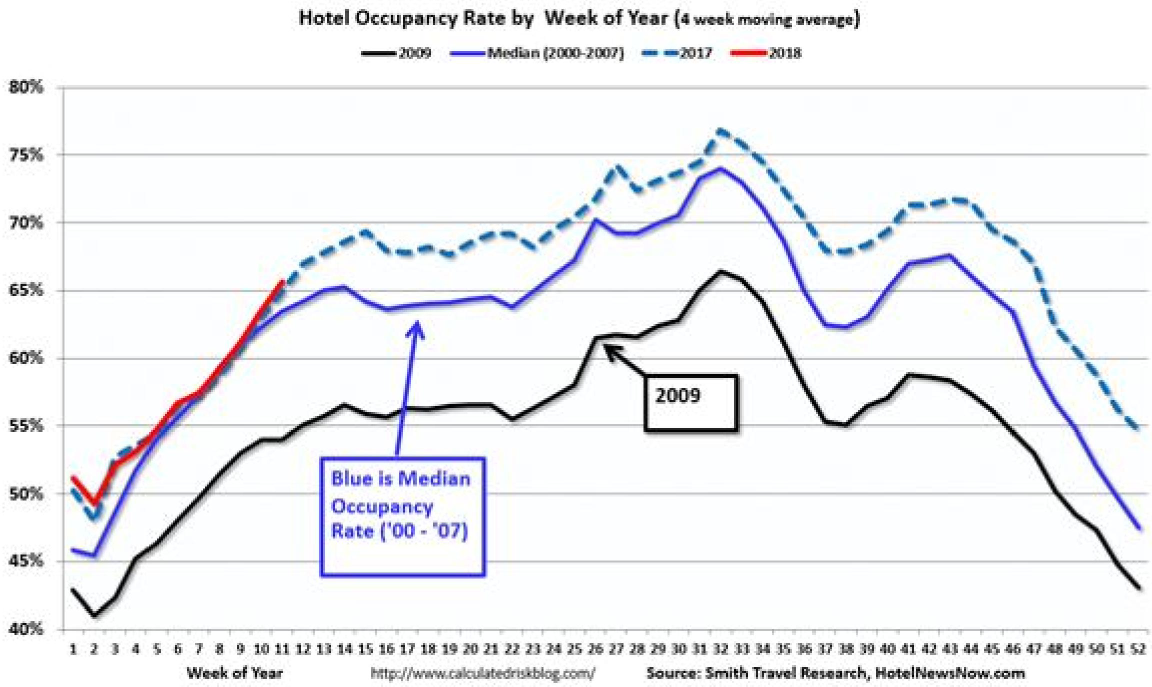

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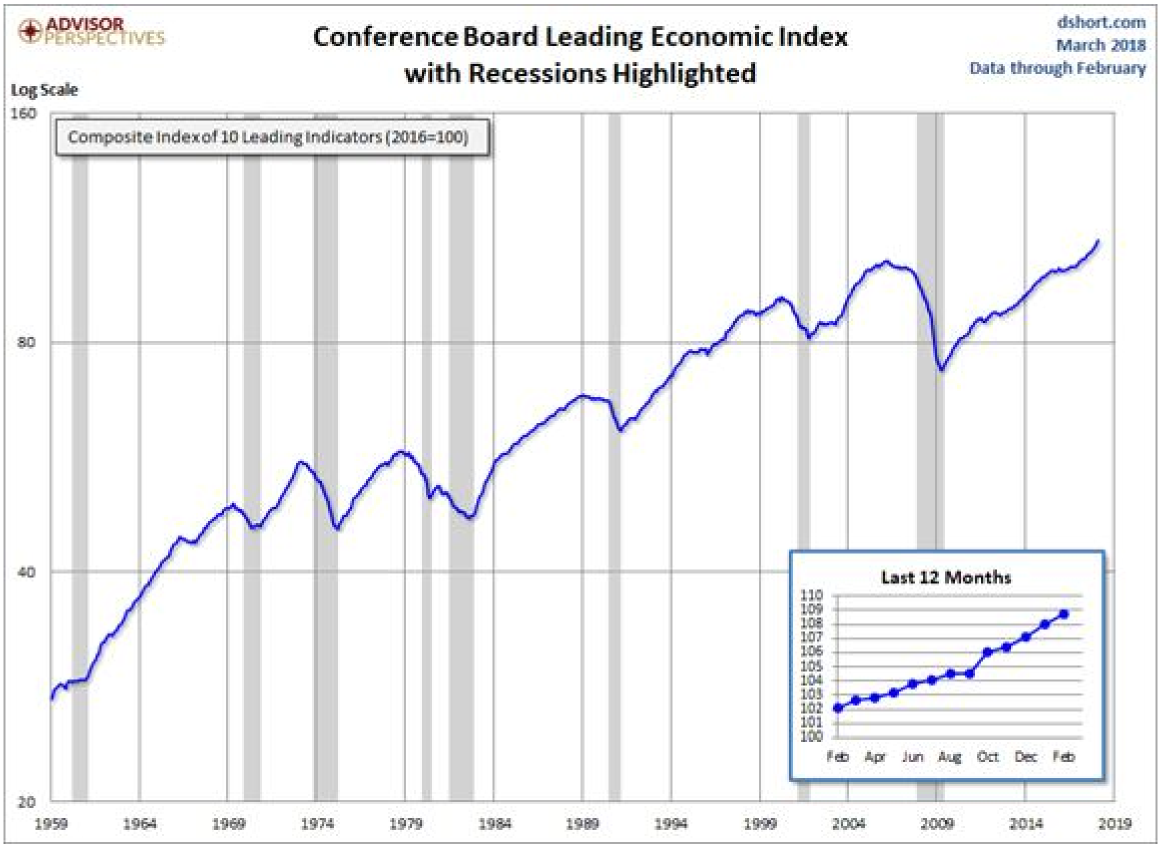

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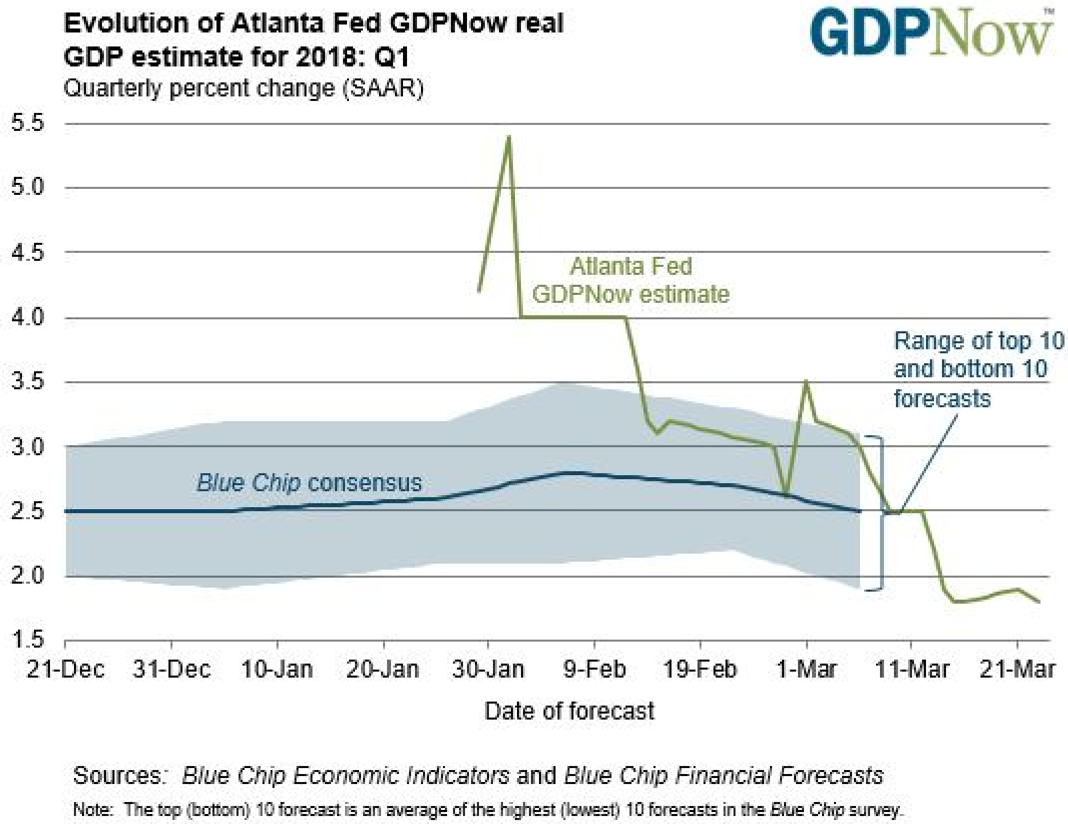

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Facebook. Not protecting data. Not responding effectively. Not creating a convincing solution. Background – The Verge. Seriousness – Medium.

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Week of March 26 - March 30

Date	ET	Release	For	Actual	Briefing.com Forecast	Briefing.com Consensus	Prior	Revised From
Mar 27	09:00	S&P Case-Shiller Home Price Index	Jan		6.2%	6.3%	6.3%	
Mar 27	10:00	Consumer Confidence	Mar		130.0	129.5	130.8	
Mar 28	07:00	MBA Mortgage Applications Index	03/24		NA	NA	-1.1%	
Mar 28	08:30	Adv. International Trade in Goods	Feb		-$74.0B	-$74.2B	-$74.4B	
Mar 28	08:30	GDP - Third Estimate	Q4		2.7%	2.6%	2.5%	
Mar 28	08:30	GDP Deflator - Third Estimate	Q4		2.3%	2.3%	2.3%	
Mar 28	10:00	Pending Home Sales	Feb		2.3%	2.5%	-4.7%	
Mar 28	10:30	Crude Inventories	03/24		NA	NA	-2.62M	
Mar 29	08:30	Personal Income	Feb		0.5%	0.4%	0.4%	
Mar 29	08:30	Personal Spending	Feb		0.3%	0.2%	0.2%	
Mar 29	08:30	PCE Prices	Feb		0.2%	0.2%	0.4%	
Mar 29	08:30	PCE Prices - Core	Feb		0.2%	0.2%	0.3%	
Mar 29	08:30	Initial Claims	03/24		233K	230K	229K	
Mar 29	08:30	Continuing Claims	03/17		NA	NA	1828K	
Mar 29	09:45	Chicago PMI	Mar		61.0	62.0	61.9	
Mar 29	10:00	Michigan Sentiment - Final	Mar		101.8	102.0	102.0	
Mar 29	10:30	Natural Gas Inventories	03/24		NA	NA	-86 bcf	

Next Week's Theme

The economic calendar is normal but squeezed into a short week. Last week's market decline has certainly captured attention. With general agreement that trade issues are the underlying cause, expect people to be asking:

Can a trade war be avoided?

There are hundreds of good articles on this topic. I have culled some of the best for those who want to learn more about the background, key issues, and stakes.

Good background on trade wars: Bloomberg and Fortune CEO Daily. From Clay Chandler in Fortune:

> New York Times *correspondents Sui-Lee Wee and Keith Bradsher argue Beijing's relatively muted response to Trump's tariffs so far reflects Xi Jinping's confidence that, in a trade showdown, Trump will be the* first to blink.

> *Chinese officials have hinted that they are prepared to impose retaliatory penalties on purchases of* Boeing *aircraft (for which they could easily substitute aircraft from AirBus), US soya beans (for which they could easily substitute soya beans grown in Brazil and Argentina) and US-made automobiles. The threat to limit imports of US soya beans is particularly astute; China buys 70% of US soya bean exports and the counties that are biggest soya bean producers are located in states that were crucial to Trump's electoral victory.*

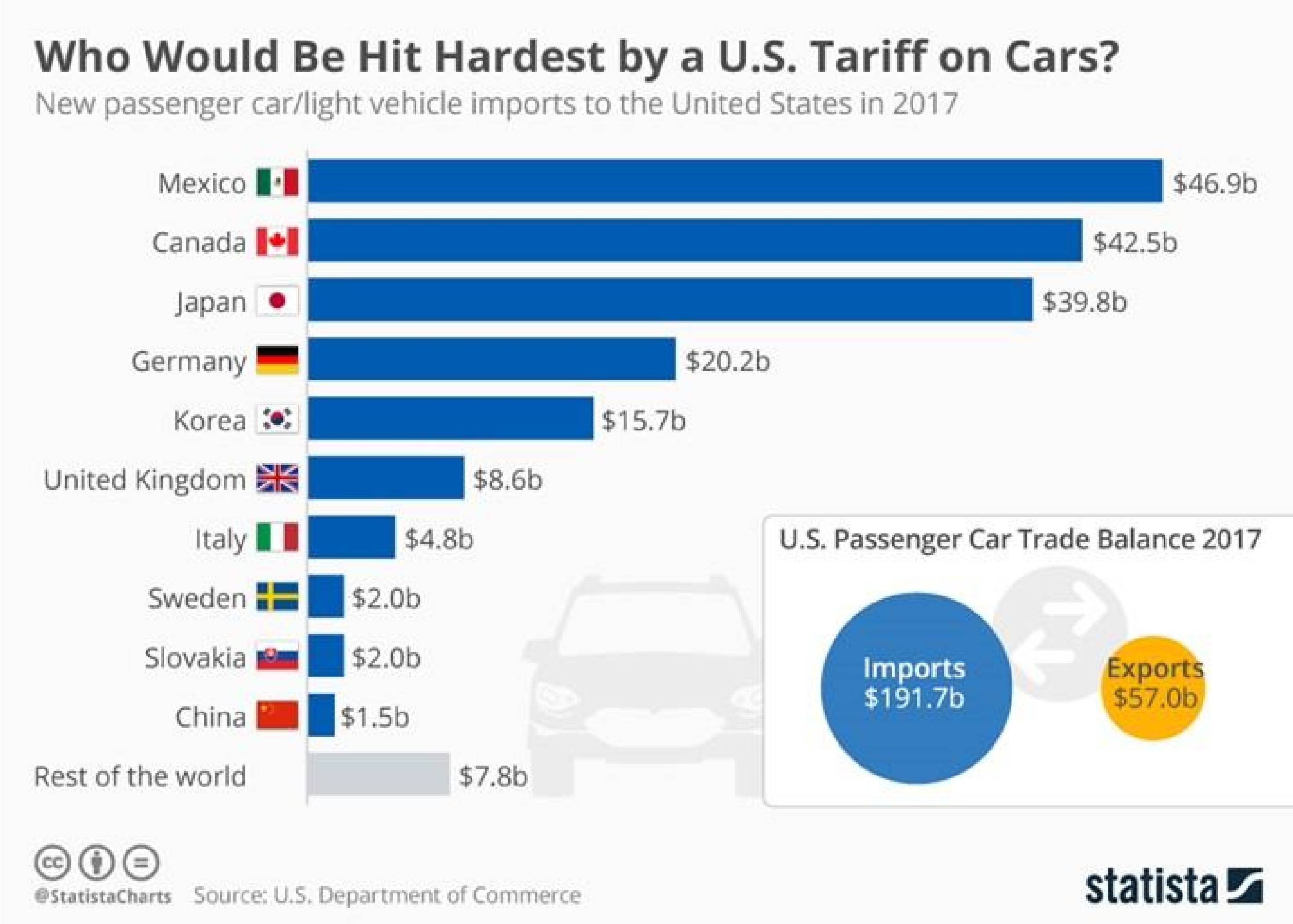
> *Will Xi blink first? Or has Trump overplayed his hand? We're about to find out. But my hunch is that China is in a much stronger bargaining position than the author of "The Art of Deal" imagines.*

The economic importance of China. (GEI)

Year of data	Commodity	China's % of Global Demand	Source
2017	Cement	59%	Statista
2016	Nickel	56%	Statista
2017	Coal	50%	NAB
2016	Copper	50%	Global X Funds
2017	Steel	50%	World Steel Association
2017	Aluminum	47%	MC Group
2016	Pork	47%	OECD
2017	Cotton	33%	USDA
2017	Rice	31%	Statista
2017	Gold	27%	China Gold Association, WGC
2017	Corn	23%	USDA
2016	Oil	14%	Enerdata

Note: Because this data is not all in one easy place, it is sourced from many different industry associations, banks, and publications. Most of the data comes from 2017, but some is from 2016.

Industry impacts – Cars (Statista via GEI).



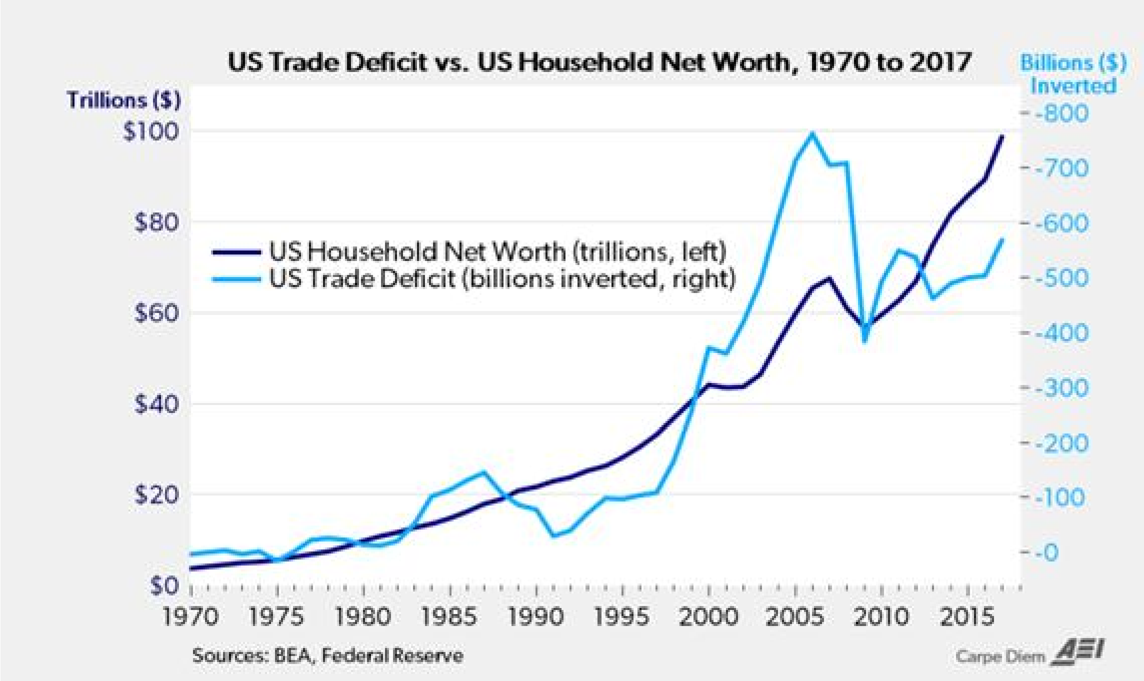
China started the trade war. Greg Ip analyzes key background on the problems and why current policies are not enough.

What about a ***retaliatory spiral***? (MarketWatch)

Corporate leaders are asking for moderation in the Trump policy. (WSJ)

US allies urge trade peace. (WSJ)

Economists broadly agree on the value of free trade, without reference to any specific agreement. Here are two excellent analyses of the current issues – first-rate analysis in a non-partisan fashion. Prof. Marty Finkler describes six false premises to the new US policy. Here is a chart on the trade deficit and economic well-being.



Prof. Menzie Chinn cites a better measure of the trade balance, reflecting the value added. Check out the full post for complete analysis and charts.

> *The more relevant (from an economic perspective) variable is the amount of* value added *traded. In an era of global supply chains, bilateral final goods balances can be misleading. The value added series takes into account the fact that about 50% of the final good exported from China incorporates foreign content.*

Trump policy is keeping everyone guessing. This includes allies, markets, and industry. (NYT)

As usual, I'll suggest my own interpretations in today's Final Thought.

Quant Corner

We follow some regular featured sources and the best other quant news from the week.

Risk Analysis

I have a rule for my investment clients. ***Think first about your risk. Only then should you consider possible rewards***. I monitor many quantitative reports and highlight the best methods in this weekly update.

The Indicator Snapshot

Risk Indicator	Current	Last Week	Last Month	Last Quarter	Interpretation
Valuation					
Ten-year note yield	2.81%	2.84%	2.87%	2.49%	
S&P 500	2588	2752	2747	2683	
S&P Forward Earnings	158	158	158	143	
S&P Earnings yield	6.12%	5.75%	5.74%	5.32%	
Equity Risk Premium	3.30%	2.91%	2.88%	2.84%	High
Economy					
C-Score	404	444	440	407	9 MoRecession Prob about 15%
*Leading SuperIndex**	0.45%	0.39%	0.49%	0.71%	3-4 MoRecession Prob
BCIp	89.4	85.3	86.5	100.0	No recession indicated
SLFSI	-1.116	-1.108	-1.146	-1.527	Very Low Risk
Anticipated Inflation	2.08%	2.08%	2.12%	1.93%	
VIX	23.34%	16.59%	18.72%	9.62%	
Historical S&P Volatility					
Last Five Days	18.72%	5.48%	14.01%	5.16%	
Last Twenty Days	17.41%	13.96%	26.53%	6.59%	
Technical Health					
Short-term	2	3	4	1	Bullish
Long-term	1	1	1	1	Strongly Bullish
Overall Outlook	Str. Bull	Str. Bull	Str. Bull	Str. Bull	
Sources: Stlouisfed.org, RecessionAlert.com, iMarket Signals, fundamentalis.com, and NewArc Investments, Inc. ©2018					
	*SuperIndex is the public value, delayed one month				

Short-term trading conditions improved again this week. Once again this shows why you need objective indicators rather than relying on your impressions about events. We continue to monitor the technical health measures on a daily basis.

The long-term fundamentals and outlook have been unchanged through the recent bout of volatility.

The Featured Sources:

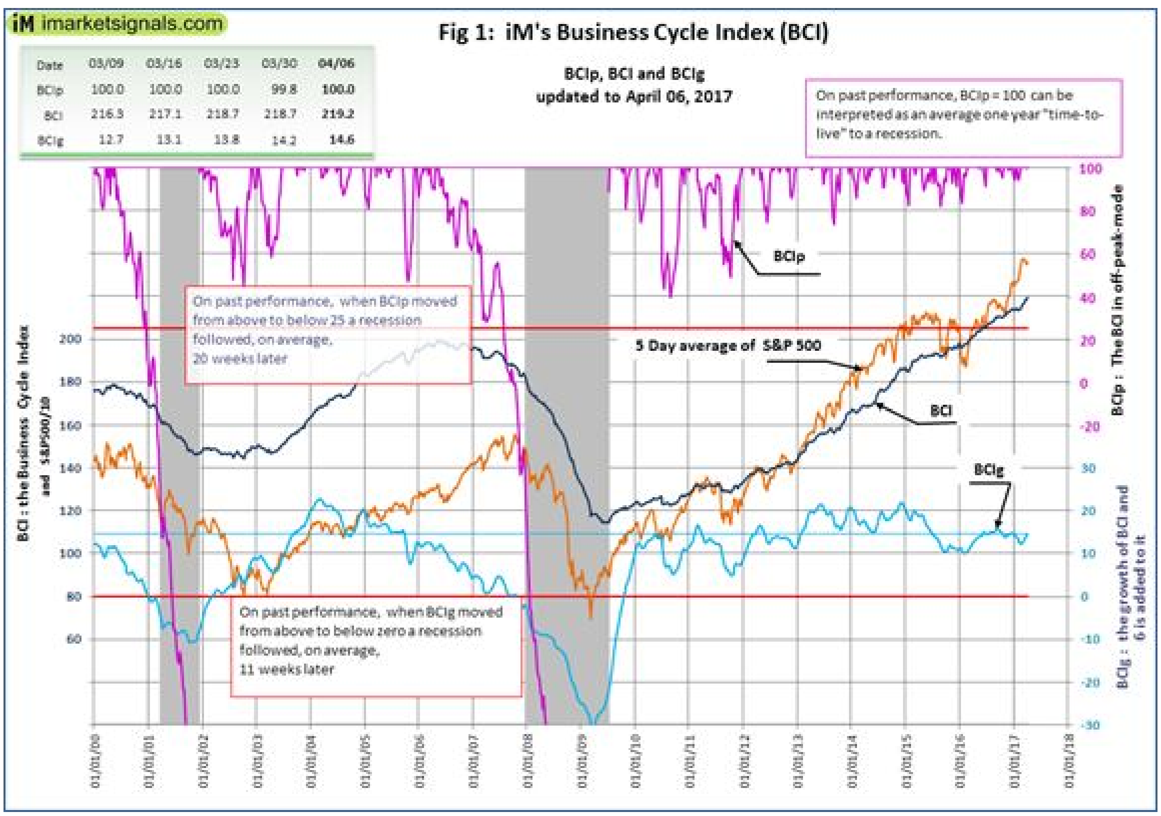
Bob Dieli: Business cycle analysis via the "C Score.

RecessionAlert: Strong quantitative indicators for both economic and market analysis.

Brian Gilmartin: All things earnings, for the overall market as well as many individual companies.

Doug Short: Regular updating of an array of indicators. Great charts and analysis.

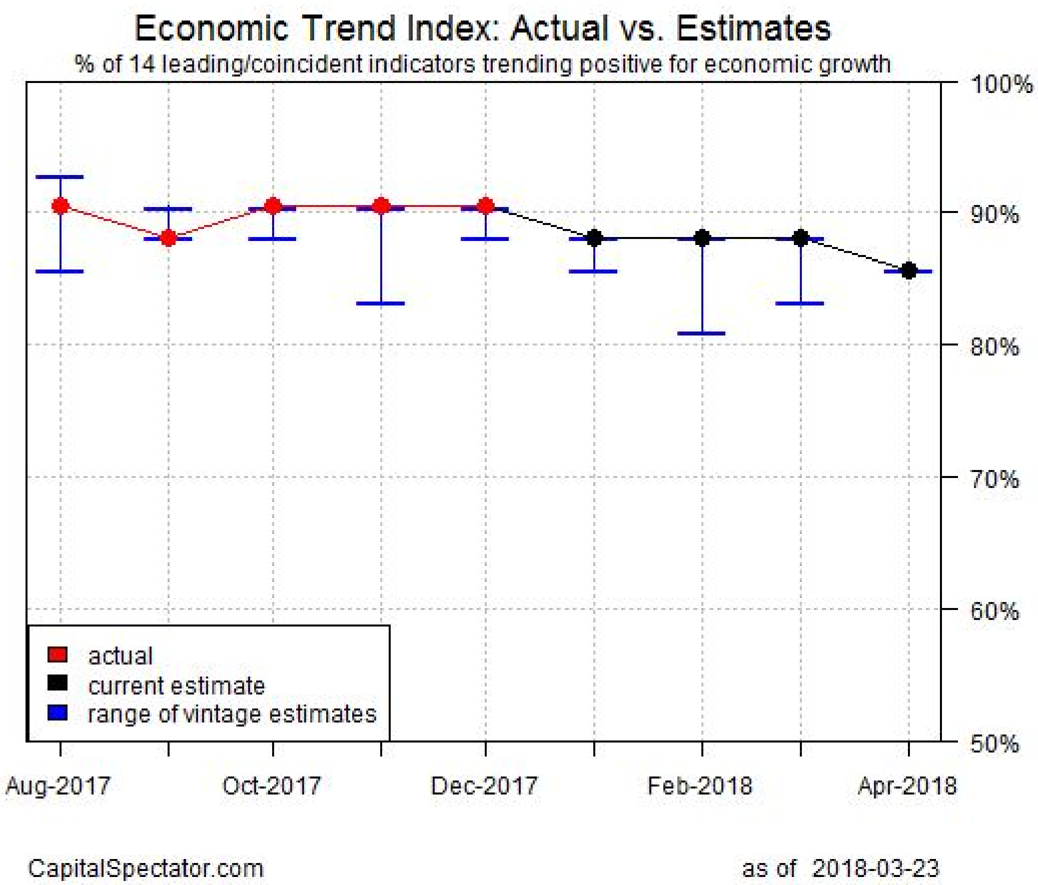
Georg Vrba: Business cycle indicator and market timing tools. None of Georg's indicators signal recession. His business cycle index, which we use in the Indicator Snapshot, is no longer "on the peg" at 100, but does not indicate a recession.



Guests:

Brian Gilmartin provides further color on the S&P earnings yield jump. He reviews the underlying numbers as well as the technical picture.

James Picerno has updated his business cycle report, showing a solidly positive macro trend through February. Here is his economic trend analysis.



And also, James notes a comment from the new Fed Chair, Jerome Powell, questioning the usefulness of yield-curve inversion as an indicator of the economy. That is something to watch!

Insight for Traders

Our discussion of trading ideas has moved to the weekly Stock Exchange post. The coverage is bigger and better than ever. We combine links to trading articles, topical themes, and ideas from our trading models. Each week we explore a topic of current interest, drawing upon trading experts. This week we asked, "How long was your learning curve?" We discussed some stock ideas and updated the ratings lists for Felix and Oscar, this week featuring the NASDAQ 100. Blue Harbinger has taken the lead role on this post, using information both from me and from the models. He is doing a great job, presenting a wealth of new ideas and information each week.

While my intent is to focus on traders, long-term investors may benefit from a better understanding of what the issues are for traders.

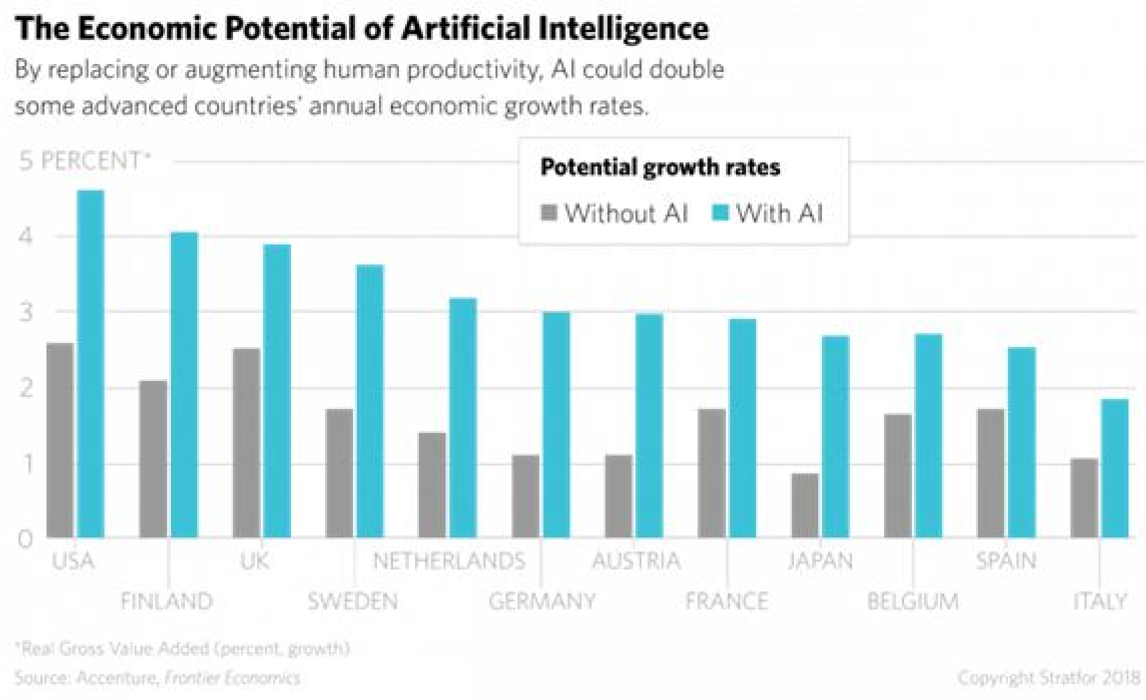
Insight for Investors

Investors should have a long-term horizon. They can often exploit trading volatility! I remind investors of this each week, but now is the *time to pay attention*.

Best of the Week

If I had to pick a single most important source for investors to read this week it would be this stimulating analysis by Mark Fleming-Williams of STRATFO (via GEI). The title emphasizes the big returns from the tax reform legislation, but the scope is much broader. There is analysis of the resulting implications for debt, the possible impact on bonds, the interaction with demographic trends, and a discussion of artificial intelligence.

There are several themes for investors to consider, beginning with what he calls the "cashbergs." The impact of increasing artificial intelligence is also a great theme.



Stock Ideas

Carnival (CCL) gets the nod from D.M. Martins Research. I agree with the pro-cyclical thesis and I like the support from baby-boomer vacationers.

The energy sector? Hale Stewart takes his usual approach, combining fundamental and technical analysis. He concludes that the stocks will follow the increase in oil prices.

Nike? (NKE). Stone Fox Capital says "no." D.M. Martins thinks the stock looks "even better" after the earnings report. Reading two good reports on the same stock is a great way to do your homework.

Time for another look at MLP's? Dividend Sensei discusses some interesting high-yield opportunities contending that the market is wrong.

Dividend Champions, Challengers, and Contenders have been updated by David Fish. Join me in following him to track all these opportunities.

Personal Finance

Seeking Alpha Senior Editor Gil Weinreich continues his excellent series. While theoretically aimed at advisors, there are many themes of interest for individual investors, especially this week! I especially enjoyed his warning about why scams seem so foolish (actually a necessary condition to find the right audience) and why some bad investments are even attractive to the "non-gullible." Gil cites a nice piece from Adam Hoffman going into more detail. Interesting reading, and maybe something that will save you from a bad idea.

Mrs. OldProf's approach just cuts the scammer off after a few seconds – if she even answers the phone. She ruthlessly deletes unknown emails.

Abnormal Returns has a special Wednesday focus for individual investors. There are a variety of ideas, and nearly always something you will find useful. I especially liked Jonathan Clements' helpful discussion of retirement calculators, including a good one to try.

Strategy

Blue Harbinger helps you determine the right level of cash to hold based upon your needs. As usual he provides some interesting ideas to help your choice of approach.

Tom Armistead, whose sensible thinking generates some great quantitative analysis, notes the elevated level of the Michigan Sentiment Index and links it market values and CAPE. He carefully notes (and I agree) the importance of inflation levels. He disagrees with my advice about ignoring politics, suggesting that current conditions call into question the DCF for the next ten years.

I clearly need to elaborate on this topic. I expect my asset allocations to change several times in the next ten years. Only those committed to a buy-and-hold strategy need to think this way.

Watch out for

"Defensive" sectors. Brian Gilmartin shows the results in consumer staples, widely regarded as defensive. In markets like we have seen recently there is no real discrimination in selling. Brian considers the top names in consumer staples. You will be surprised at the results of these safe-haven, dividend names.

Final Thoughts

Three weeks ago, I started closer coverage of the trade issue with this post. There was little attention at the time to a subject less titillating than the gossipy stories. As exemptions were made in the steel and aluminum tariffs, the trade story lost traction. With China now playing a leading role, this week's stock market decline reflected the concerns of many.

What NOT to consider

The analysis of many "experts" is very shallow. It is important to watch this, because these people are the average traders and fund managers.

- "There's multiple things going on, and none of it good," said Larry X, managing director of international equity trading at company Y. "Six months ago, everything was good and you couldn't find a reason to sell stocks. Now you can't find a reason to hold them," he added.
- A leading CNBC contributor who took a brief and unsuccessful fling at running a hedge fund is also worried about all the headwinds now, as opposed to a few

weeks ago.

These people are driving the market. Meanwhile, the fundamentals of earnings, inflation expectations, and recession odds have improved. No wonder so few funds outperform the market. Impressionistic reaction to headlines should not drive your decisions.

For investors, it matters little who is responsible. We should focus strictly on the implications for financial markets. As a citizen, it is fine to take a principled stand on intellectual property, for example. If your personal citizen side prevails, your investment side had better sell stocks.

Recent Trump proposals have been stated and then modified after the reaction. The same thing might happen here, but I would not even venture a guess on this one.

What to Watch

A trade war could lead both to inflation and to lower economic growth, a nasty combination. Unlike many other elements of the "headline risk" we always see, this is something which has ***direct implications for corporate earnings.*** So far, the various threatened policies are of modest size (in comparison to the overall economies and markets). There is still time to negotiate and reach a face-saving conclusion. There is not yet an impact on the foundations of the stock rally: growing corporate earnings, low inflation expectations, and no recession in sight.

You should not make a big asset allocation decision because others, less grounded in the data, are selling their stocks. Do not substitute their fear for your own analysis.

That said, the trade situation is serious. Signs of softening of positions would be the most positive. Do not expect this to happen overnight.

I'm more worried about:

- Trade issues. The Commerce Department is recommending increased tariffs on steel and aluminum. Opinion within the Administration itself if mixed, with trade

war warnings. Jonathan Swan (Axios) provides good coverage.
- Cybercrime, including attacks by various governments.

I'm less worried about:

- The Fed. The Powell approach continues a policy of gradual change with an eye on the data.
- Chinese bond purchases. China has a current accounts surplus with the US and must invest the dollars somewhere. US Treasuries remain an attractive choice; US equities are a principal alternative. Even an end to Chinese bond purchases would not represent a significant problem. For more details, check out my recent post on this topic.

> *[Do the economic challenges seem complicated and threatening? You might find help in my paper on the top investor pitfalls, or my suggestions about managing risk. Just write for our free information on these topics. While they describe what I am doing, the do-it-yourself investor can apply the same principles. These are available for free from main at newarc dot com].*


oldprof / March 24, 2018 / Uncategorized / 1 Comment

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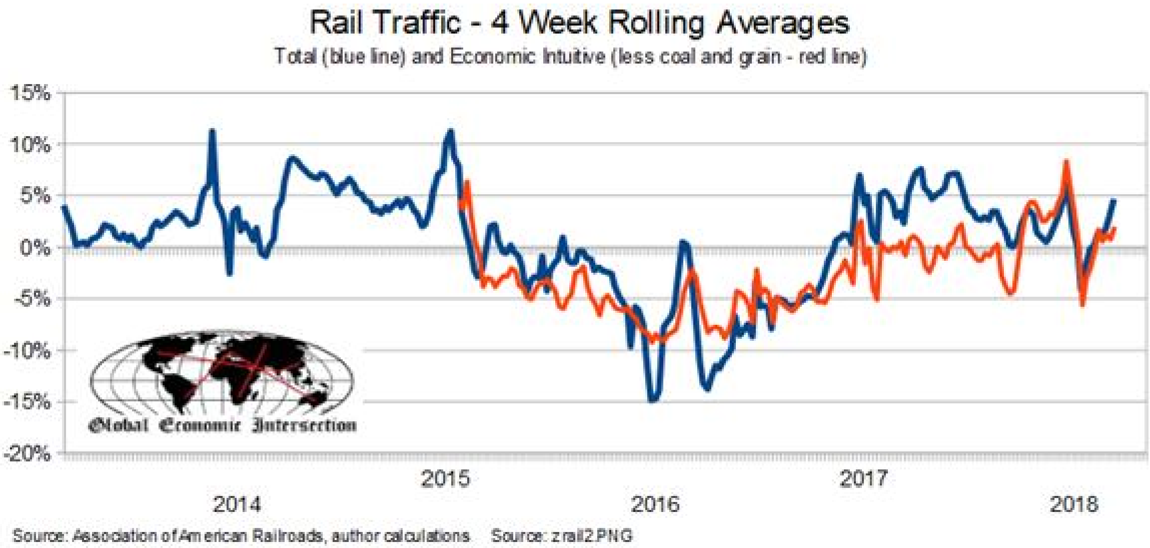

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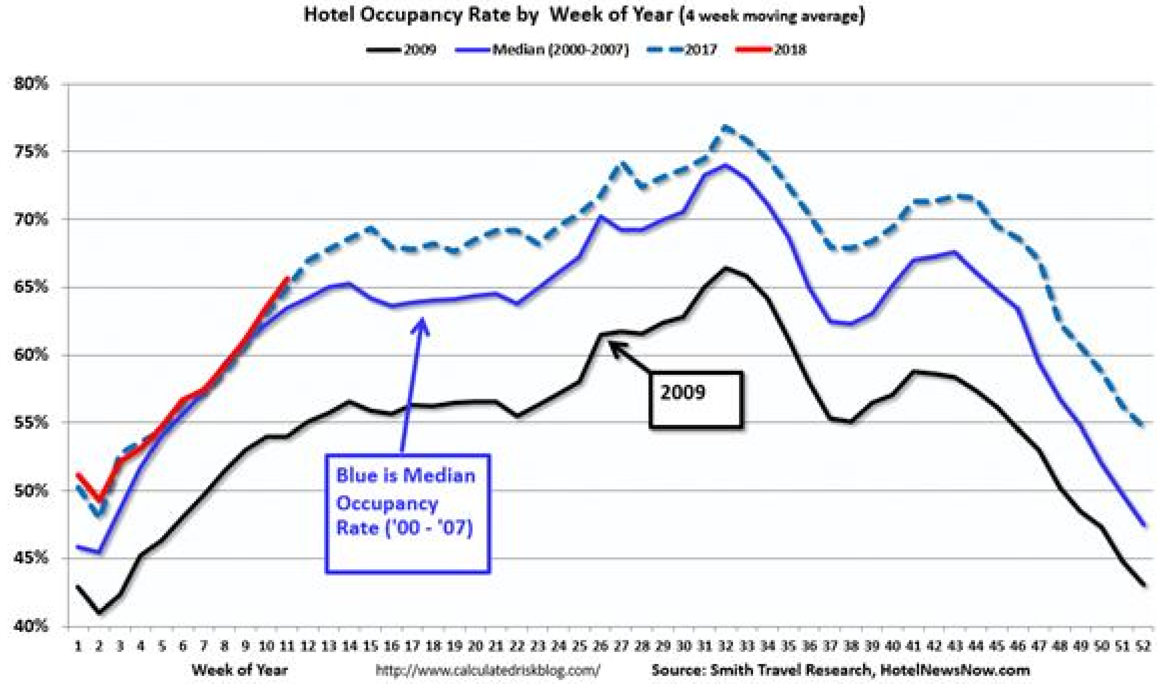

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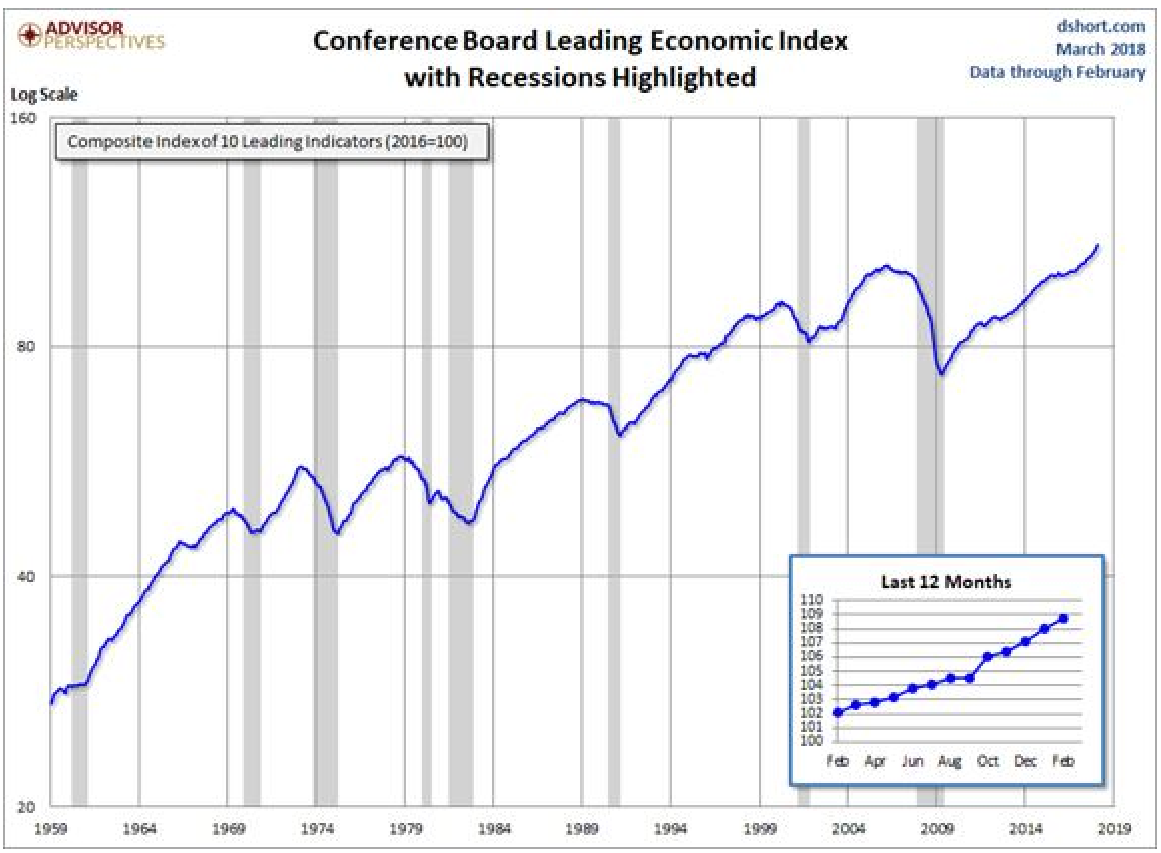

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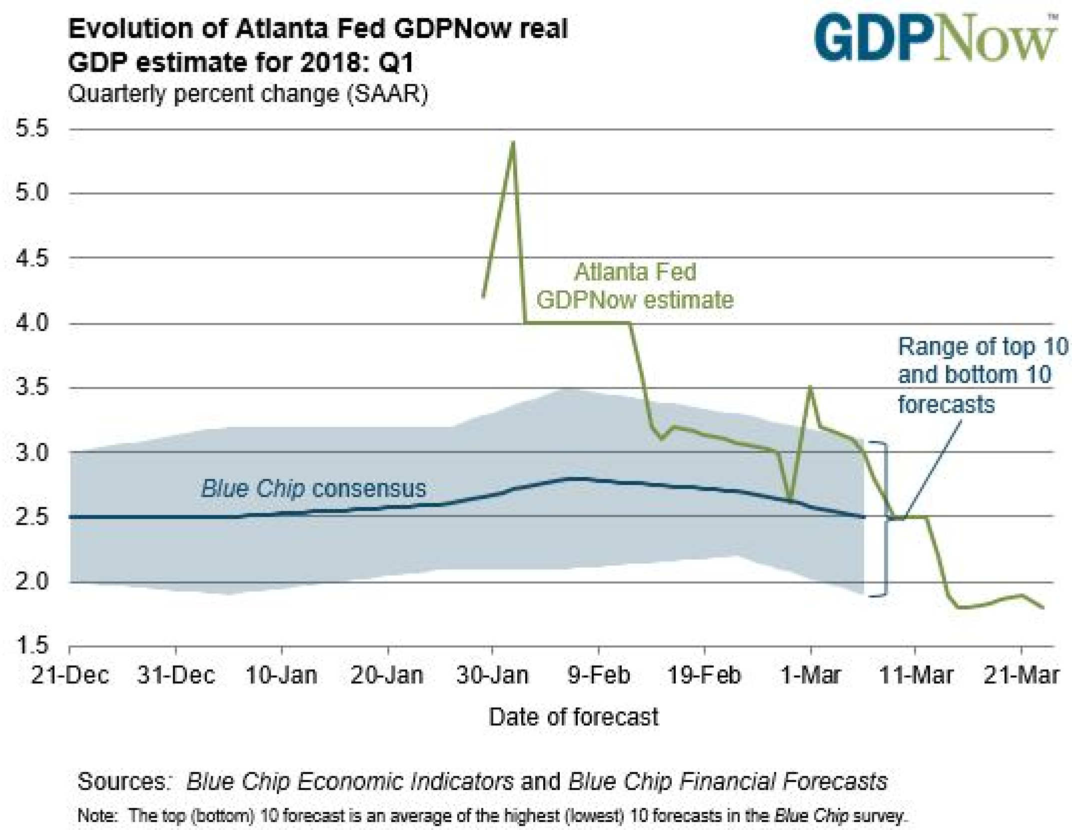

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Mar 27	10:00	Consumer Confidence	Mar		130.0	129.5	130.8	
Mar 28	07:00	MBA Mortgage Applications Index	03/24		NA	NA	-1.1%	
Mar 28	08:30	Adv. International Trade in Goods	Feb		-$74.0B	-$74.2B	-$74.4B	
Mar 28	08:30	GDP - Third Estimate	Q4		2.7%	2.6%	2.5%	
Mar 28	08:30	GDP Deflator - Third Estimate	Q4		2.3%	2.3%	2.3%	
Mar 28	10:00	Pending Home Sales	Feb		2.3%	2.5%	-4.7%	
Mar 28	10:30	Crude Inventories	03/24		NA	NA	-2.62M	
Mar 29	08:30	Personal Income	Feb		0.5%	0.4%	0.4%	
Mar 29	08:30	Personal Spending	Feb		0.3%	0.2%	0.2%	
Mar 29	08:30	PCE Prices	Feb		0.2%	0.2%	0.4%	
Mar 29	08:30	PCE Prices - Core	Feb		0.2%	0.2%	0.3%	
Mar 29	08:30	Initial Claims	03/24		233K	230K	229K	
Mar 29	08:30	Continuing Claims	03/17		NA	NA	1828K	
Mar 29	09:45	Chicago PMI	Mar		61.0	62.0	61.9	
Mar 29	10:00	Michigan Sentiment - Final	Mar		101.8	102.0	102.0	
Mar 29	10:30	Natural Gas Inventories	03/24		NA	NA	-86 bcf	

Next Week's Theme

The economic calendar is normal but squeezed into a short week. Last week's market decline has certainly captured attention. With general agreement that trade issues are the underlying cause, expect people to be asking:

Can a trade war be avoided?

There are hundreds of good articles on this topic. I have culled some of the best for those who want to learn more about the background, key issues, and stakes.

Good background on trade wars: Bloomberg and Fortune CEO Daily. From Clay Chandler in Fortune:

> New York Times *correspondents Sui-Lee Wee and Keith Bradsher argue Beijing's relatively muted response to Trump's tariffs so far reflects Xi Jinping's confidence that, in a trade showdown, Trump will be the* first to blink*.*

> *Chinese officials have hinted that they are prepared to impose retaliatory penalties on purchases of* Boeing *aircraft (for which they could easily substitute aircraft from AirBus), US soya beans (for which they could easily substitute soya beans grown in Brazil and Argentina) and US-made automobiles. The threat to limit imports of US soya beans is particularly astute; China buys 70% of US soya bean exports and the counties that are biggest soya bean producers are located in states that were crucial to Trump's electoral victory.*

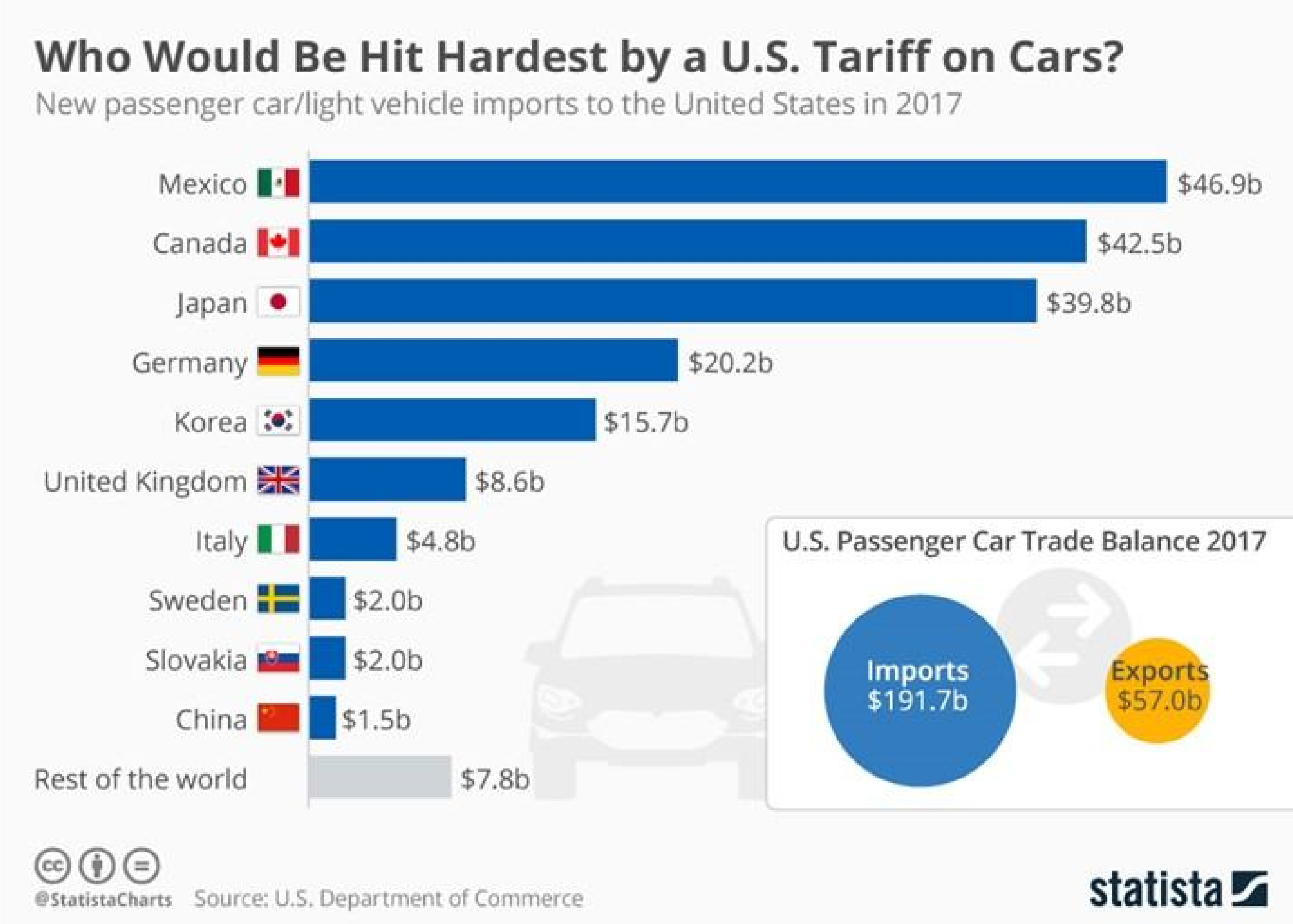
> *Will Xi blink first? Or has Trump overplayed his hand? We're about to find out. But my hunch is that China is in a much stronger bargaining position than the author of "The Art of Deal" imagines.*

The economic importance of China. (GEI)

Year of data	Commodity	China's % of Global Demand	Source
2017	Cement	59%	Statista
2016	Nickel	56%	Statista
2017	Coal	50%	NAB
2016	Copper	50%	Global X Funds
2017	Steel	50%	World Steel Association
2017	Aluminum	47%	MC Group
2016	Pork	47%	OECD
2017	Cotton	33%	USDA
2017	Rice	31%	Statista
2017	Gold	27%	China Gold Association, WGC
2017	Corn	23%	USDA
2016	Oil	14%	Enerdata

Note: Because this data is not all in one easy place, it is sourced from many different industry associations, banks, and publications. Most of the data comes from 2017, but some is from 2016.

Industry impacts – Cars (Statista via GEI).



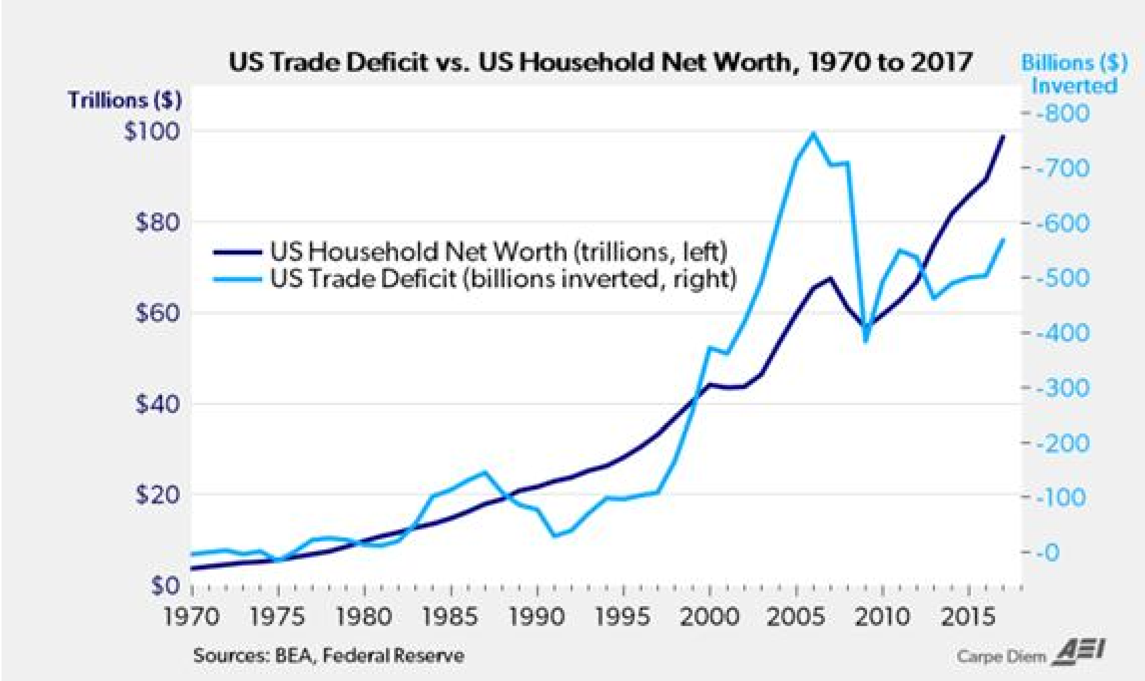
China started the trade war. Greg Ip analyzes key background on the problems and why current policies are not enough.

What about a ***retaliatory spiral***? (MarketWatch)

Corporate leaders are asking for moderation in the Trump policy. (WSJ)

US allies urge trade peace. (WSJ)

Economists broadly agree on the value of free trade, without reference to any specific agreement. Here are two excellent analyses of the current issues – first-rate analysis in a non-partisan fashion. Prof. Marty Finkler describes six false premises to the new US policy. Here is a chart on the trade deficit and economic well-being.



[Prof. Menzie Chinn cites](#) a better measure of the trade balance, reflecting the value added. Check out the full post for complete analysis and charts.

> *The more relevant (from an economic perspective) variable is the amount of* value added *traded. In an era of global supply chains, bilateral final goods balances can be misleading. The value added series takes into account the fact that about 50% of the final good exported from China incorporates foreign content.*

Trump policy is keeping everyone guessing. This includes allies, markets, and industry. ([NYT](#))

As usual, I'll suggest my own interpretations in today's Final Thought.

Quant Corner

We follow some regular featured sources and the best other quant news from the week.

Risk Analysis

I have a rule for my investment clients. ***Think first about your risk. Only then should you consider possible rewards***. I monitor many quantitative reports and highlight the best methods in this weekly update.

The Indicator Snapshot

Risk Indicator	Current	Last Week	Last Month	Last Quarter	Interpretation
Valuation					
Ten-year note yield	2.81%	2.84%	2.87%	2.49%	
S&P 500	2588	2752	2747	2683	
S&P Forward Earnings	158	158	158	143	
S&P Earnings yield	6.12%	5.75%	5.74%	5.32%	
Equity Risk Premium	3.30%	2.91%	2.88%	2.84%	High
Economy					
C-Score	404	444	440	407	9 MoRecession Prob about 15%
*Leading SuperIndex**	0.45%	0.39%	0.49%	0.71%	3-4 MoRecession Prob
BCIp	89.4	85.3	86.5	100.0	No recession indicated
SLFSI	-1.116	-1.108	-1.146	-1.527	Very Low Risk
Anticipated Inflation	2.08%	2.08%	2.12%	1.93%	
VIX	23.34%	16.59%	18.72%	9.62%	
Historical S&P Volatility					
Last Five Days	18.72%	5.48%	14.01%	5.16%	
Last Twenty Days	17.41%	13.96%	26.53%	6.59%	
Technical Health					
Short-term	2	3	4	1	Bullish
Long-term	1	1	1	1	Strongly Bullish
Overall Outlook	Str. Bull	Str. Bull	Str. Bull	Str. Bull	

Sources: Stlouisfed.org, RecessionAlert.com, iMarket Signals, fundamentalis.com, and NewArc Investments, Inc. ©2018

*SuperIndex is the public value, delayed one month

Short-term trading conditions improved again this week. Once again this shows why you need objective indicators rather than relying on your impressions about events. We continue to monitor the technical health measures on a daily basis.

The long-term fundamentals and outlook have been unchanged through the recent bout of volatility.

The Featured Sources:

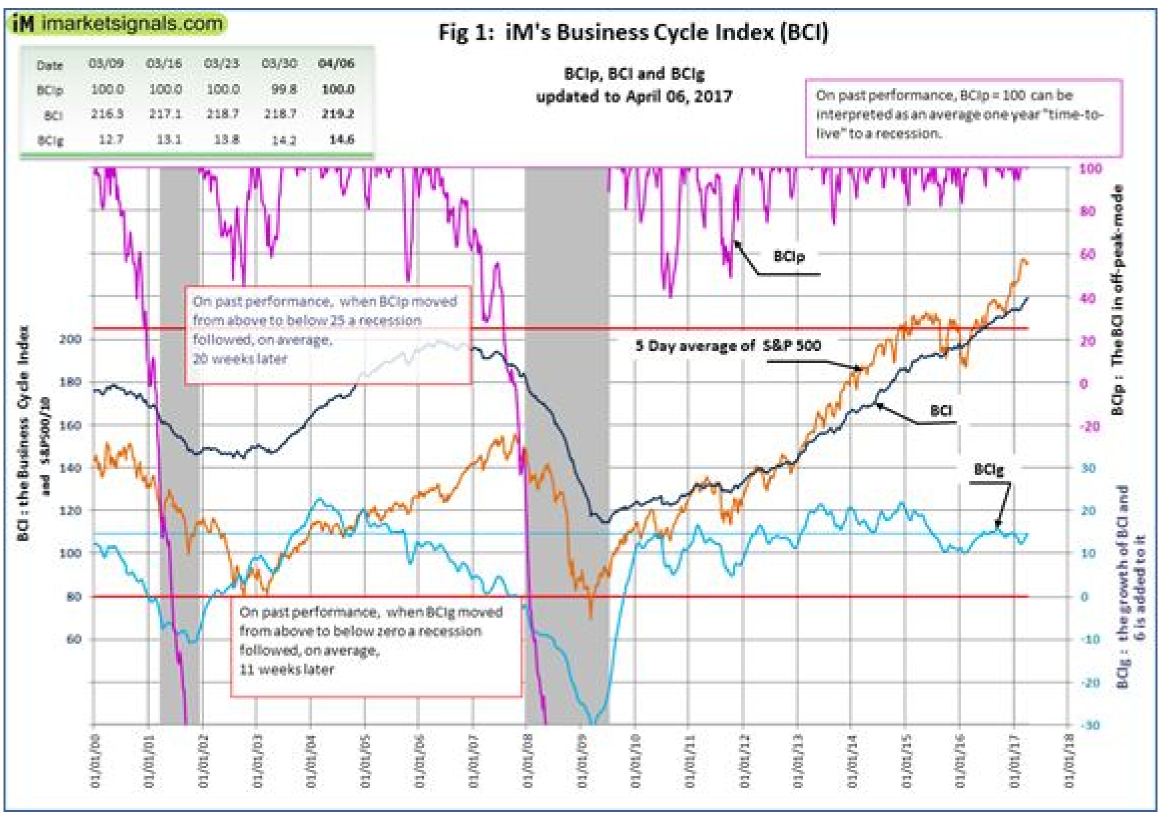
[Bob Dieli]: Business cycle analysis via the "C Score.

[RecessionAlert]: Strong quantitative indicators for both economic and market analysis.

[Brian Gilmartin]: All things earnings, for the overall market as well as many individual companies.

[Doug Short]: Regular updating of an array of indicators. Great charts and analysis.

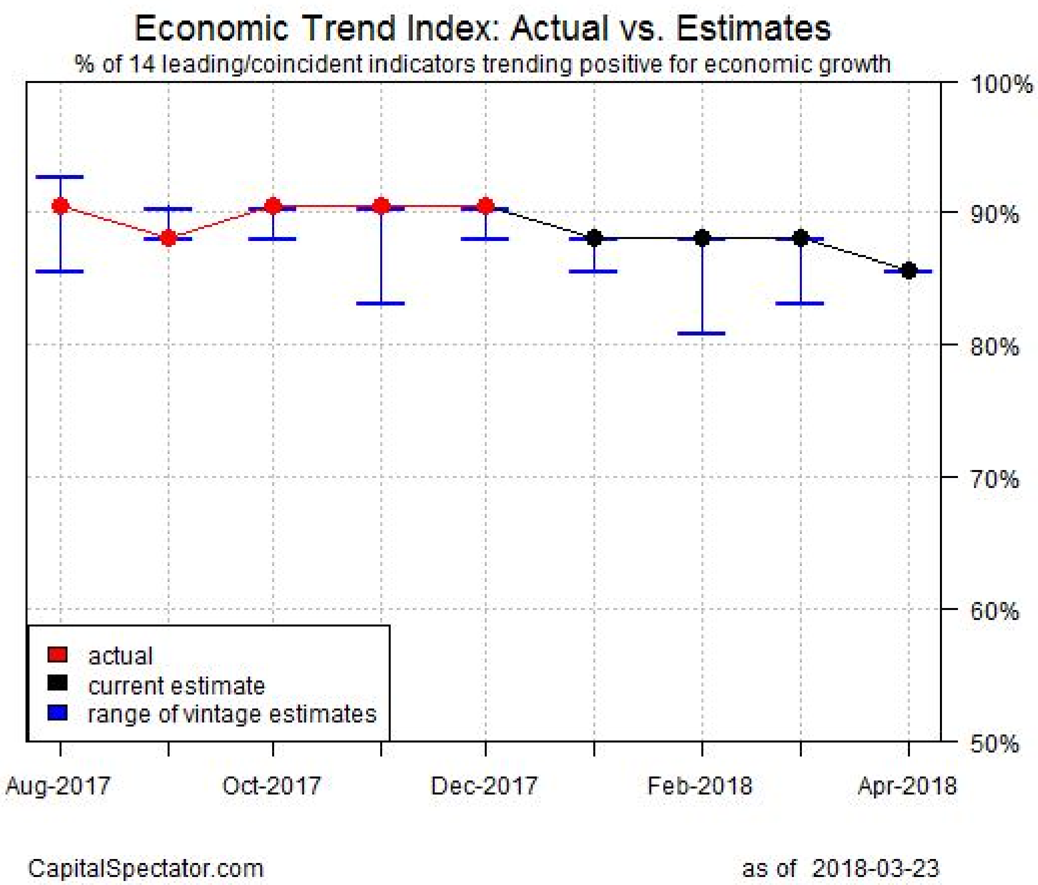
[Georg Vrba]: Business cycle indicator and market timing tools. None of Georg's indicators signal recession. His business cycle index, which we use in the Indicator Snapshot, is no longer "on the peg" at 100, but does not indicate a recession.



Guests:

Brian Gilmartin provides further color on the S&P earnings yield jump. He reviews the underlying numbers as well as the technical picture.

James Picerno has updated his business cycle report, showing a solidly positive macro trend through February. Here is his economic trend analysis.



And also, James notes a comment from the new Fed Chair, Jerome Powell, questioning the usefulness of yield-curve inversion as an indicator of the economy. That is something to watch!

Insight for Traders

Our discussion of trading ideas has moved to the weekly Stock Exchange post. The coverage is bigger and better than ever. We combine links to trading articles, topical themes, and ideas from our trading models. Each week we explore a topic of current interest, drawing upon trading experts. This week we asked, "How long was your learning curve?" We discussed some stock ideas and updated the ratings lists for Felix and Oscar, this week featuring the NASDAQ 100. Blue Harbinger has taken the lead role on this post, using information both from me and from the models. He is doing a great job, presenting a wealth of new ideas and information each week.

While my intent is to focus on traders, long-term investors may benefit from a better understanding of what the issues are for traders.

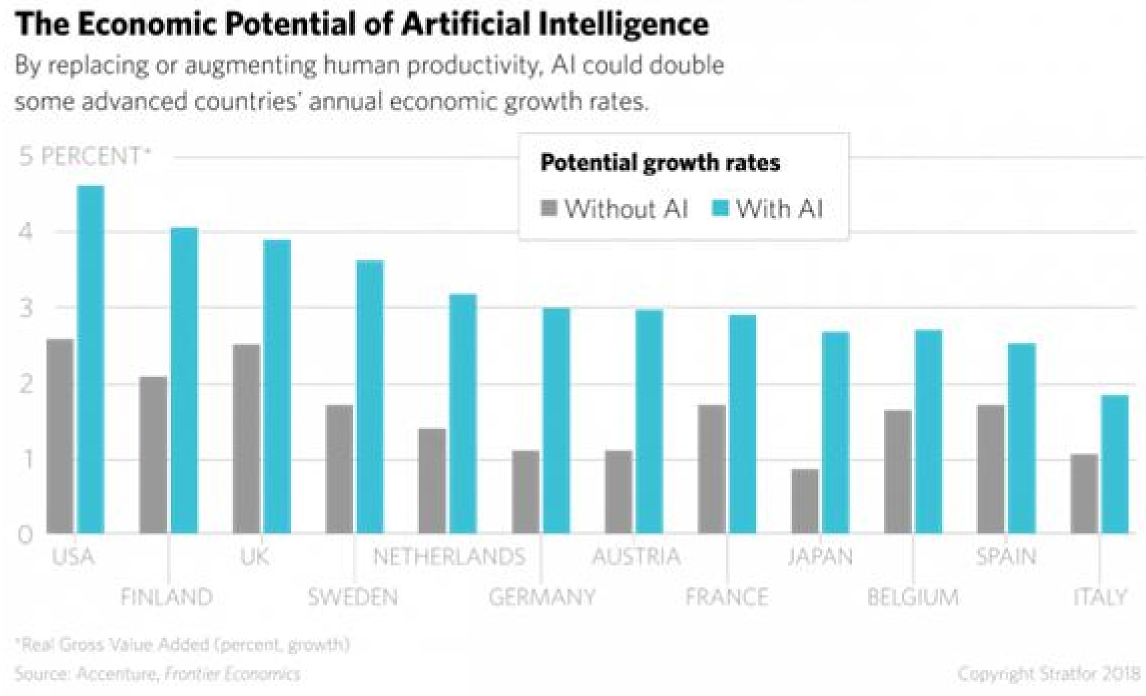
Insight for Investors

Investors should have a long-term horizon. They can often exploit trading volatility! I remind investors of this each week, but now is the *time to pay attention*.

Best of the Week

If I had to pick a single most important source for investors to read this week it would be this stimulating analysis by Mark Fleming-Williams of STRATFO (via GEI). The title emphasizes the big returns from the tax reform legislation, but the scope is much broader. There is analysis of the resulting implications for debt, the possible impact on bonds, the interaction with demographic trends, and a discussion of artificial intelligence.

There are several themes for investors to consider, beginning with what he calls the "cashbergs." The impact of increasing artificial intelligence is also a great theme.



Stock Ideas

Carnival (CCL) gets the nod from D.M. Martins Research. I agree with the pro-cyclical thesis and I like the support from baby-boomer vacationers.

The energy sector? Hale Stewart takes his usual approach, combining fundamental and technical analysis. He concludes that the stocks will follow the increase in oil prices.

Nike? (NKE). Stone Fox Capital says "no." D.M. Martins thinks the stock looks "even better" after the earnings report. Reading two good reports on the same stock is a great way to do your homework.

Time for another look at MLP's? Dividend Sensei discusses some interesting high-yield opportunities contending that the market is wrong.

Dividend Champions, Challengers, and Contenders have been updated by David Fish. Join me in following him to track all these opportunities.

Personal Finance

Seeking Alpha Senior Editor Gil Weinreich continues his excellent series. While theoretically aimed at advisors, there are many themes of interest for individual investors, especially this week! I especially enjoyed his warning about why scams seem so foolish (actually a necessary condition to find the right audience) and why some bad investments are even attractive to the "non-gullible." Gil cites a nice piece from Adam Hoffman going into more detail. Interesting reading, and maybe something that will save you from a bad idea.

Mrs. OldProf's approach just cuts the scammer off after a few seconds – if she even answers the phone. She ruthlessly deletes unknown emails.

Abnormal Returns has a special Wednesday focus for individual investors. There are a variety of ideas, and nearly always something you will find useful. I especially liked Jonathan Clements' helpful discussion of retirement calculators, including a good one to try.

Strategy

Blue Harbinger helps you determine the right level of cash to hold based upon your needs. As usual he provides some interesting ideas to help your choice of approach.

Tom Armistead, whose sensible thinking generates some great quantitative analysis, notes the elevated level of the Michigan Sentiment Index and links it market values and CAPE. He carefully notes (and I agree) the importance of inflation levels. He disagrees with my advice about ignoring politics, suggesting that current conditions call into question the DCF for the next ten years.

I clearly need to elaborate on this topic. I expect my asset allocations to change several times in the next ten years. Only those committed to a buy-and-hold strategy need to think this way.

Watch out for

"Defensive" sectors. Brian Gilmartin shows the results in consumer staples, widely regarded as defensive. In markets like we have seen recently there is no real discrimination in selling. Brian considers the top names in consumer staples. You will be surprised at the results of these safe-haven, dividend names.

Final Thoughts

Three weeks ago, I started closer coverage of the trade issue with this post. There was little attention at the time to a subject less titillating than the gossipy stories. As exemptions were made in the steel and aluminum tariffs, the trade story lost traction. With China now playing a leading role, this week's stock market decline reflected the concerns of many.

What NOT to consider

The analysis of many "experts" is very shallow. It is important to watch this, because these people are the average traders and fund managers.

- "There's multiple things going on, and none of it good," said Larry X, managing director of international equity trading at company Y. "Six months ago, everything was good and you couldn't find a reason to sell stocks. Now you can't find a reason to hold them," he added.
- A leading CNBC contributor who took a brief and unsuccessful fling at running a hedge fund is also worried about all the headwinds now, as opposed to a few

weeks ago.

These people are driving the market. Meanwhile, the fundamentals of earnings, inflation expectations, and recession odds have improved. No wonder so few funds outperform the market. Impressionistic reaction to headlines should not drive your decisions.

For investors, it matters little who is responsible. We should focus strictly on the implications for financial markets. As a citizen, it is fine to take a principled stand on intellectual property, for example. If your personal citizen side prevails, your investment side had better sell stocks.

Recent Trump proposals have been stated and then modified after the reaction. The same thing might happen here, but I would not even venture a guess on this one.

What to Watch

A trade war could lead both to inflation and to lower economic growth, a nasty combination. Unlike many other elements of the "headline risk" we always see, this is something which has ***direct implications for corporate earnings.*** So far, the various threatened policies are of modest size (in comparison to the overall economies and markets). There is still time to negotiate and reach a face-saving conclusion. There is not yet an impact on the foundations of the stock rally: growing corporate earnings, low inflation expectations, and no recession in sight.

You should not make a big asset allocation decision because others, less grounded in the data, are selling their stocks. Do not substitute their fear for your own analysis.

That said, the trade situation is serious. Signs of softening of positions would be the most positive. Do not expect this to happen overnight.

I'm more worried about:

- Trade issues. The Commerce Department is recommending increased tariffs on steel and aluminum. Opinion within the Administration itself if mixed, with trade

war warnings. Jonathan Swan (Axios) provides good coverage.
- Cybercrime, including attacks by various governments.

I'm less worried about:

- The Fed. The Powell approach continues a policy of gradual change with an eye on the data.
- Chinese bond purchases. China has a current accounts surplus with the US and must invest the dollars somewhere. US Treasuries remain an attractive choice; US equities are a principal alternative. Even an end to Chinese bond purchases would not represent a significant problem. For more details, check out my recent post on this topic.

> *[Do the economic challenges seem complicated and threatening? You might find help in my paper on the top investor pitfalls, or my suggestions about managing risk. Just write for our free information on these topics. While they describe what I am doing, the do-it-yourself investor can apply the same principles. These are available for free from main at newarc dot com].*


oldprof / March 24, 2018 / Uncategorized / Leave a comment

Investors Need Not Worry About China and US Bonds

In my role as a long-term investor (trading is a different story) I don't care about Chinese purchases of US Treasuries. You shouldn't either.

The issue is the focal point of the trade war story.

There are multiple reasons, but the most important is rarely mentioned. Stories ask, "Who Will Buy Our Bonds?" as if China is the only market. The (overly) simple heuristic is a market with a handful of participants. Country A borrows from B. B calls the debt. Party A must now, hat in hand, go to C or D or E to ask for a loan.

This analytical error comes when we focus on the result of building and liquidating positions instead of daily market dynamics. What is the correct answer to the "who will buy" question?

> *The buyers will be the millions of individuals (usually through funds) and thousands of institutions that are bidding for US Treasuries every day. Some currently lose out in purchases to Chinese buyers, perhaps because of China's compelling need to invest US dollars. An economist might instead ask:*

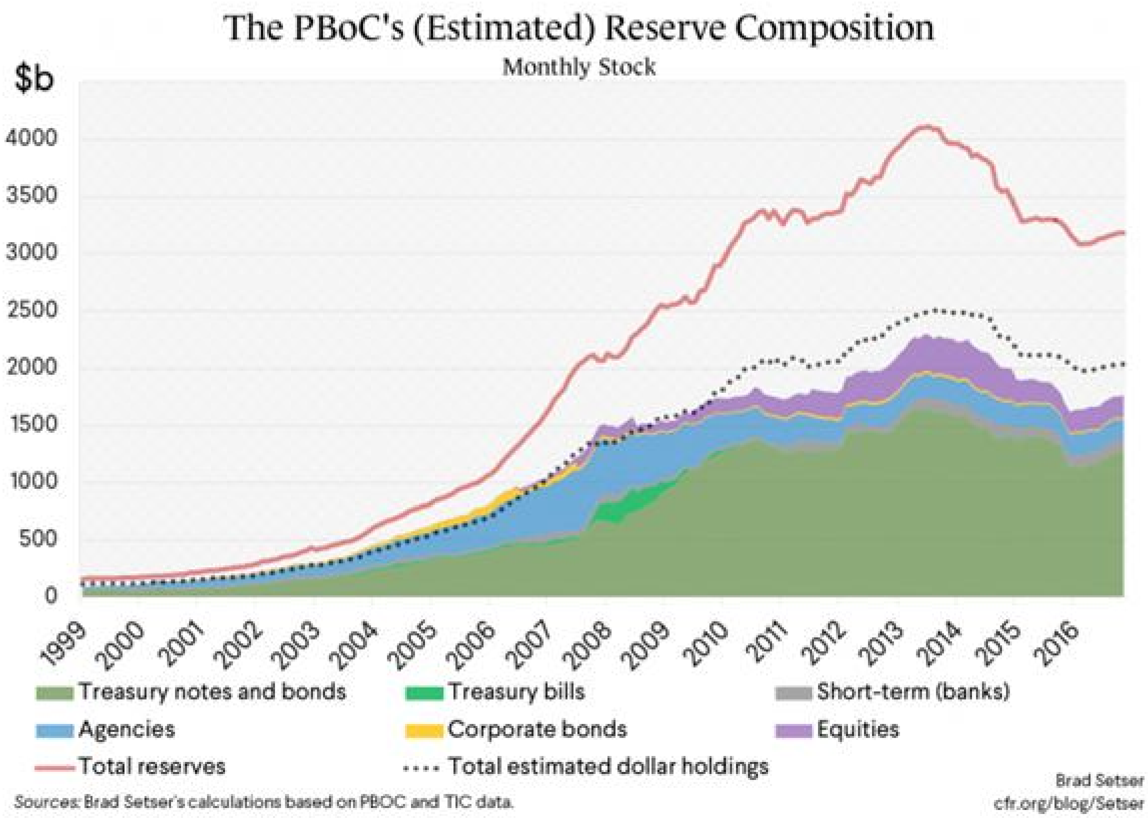
> Suppose a buyer who is relatively insensitive to price was subtracted from the demand curve. What would be the new market clearing price?

This question allows the analyst to include the deep and liquid Treasury market and therefore see the minor effect of trading by even the largest participants.

This basic market analysis is ignored by everyone. I guess it is too sophisticated for the pundits, who personify everything, and too trivial for real economists.

Here are some other reasons:

- China has a current account surplus with the US. That means that the result of trade is an influx of dollars. They must do something with those dollars. Treasuries are a convenient and liquid choice, although they hold US equities as well. (CFR).



- China seeks the best investment for its dollar surplus. US Treasuries are better than the negative-yield European choices. US Stocks are attractive relative to US Treasuries.
- A serious reduction in US investment would require currency appreciation to reduce the current account surplus. This would threaten employment.

Investment Conclusion

Algorithms programmed for trade war and China bond selling can take control at any time. The average trader is using a simple heuristic. Noted bond managers just feed the flames of worry.

The astute long-term investor knows how to quantify potential issues and take advantage of headline-driven headlines.

Further reading, including Treasury market data, analysis, and discussion:

https://dashofinsight.com/fed-balance-sheet-unwind-no-reason-to-worry/

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