Market Update: Perspective on Korea Noise

Good afternoon,

As expected, several clients have called or emailed to ask about the current North Korean situation and recent modest % correction/pullback we've seen in equity markets in North America over the last few months. Here are my thoughts in summary point form and a bit more detail below:

- **The long term, secular bull market in stocks remains fully intact** (see chart below). There is no risk of a U.S. recession in 2017 and near zero risk in 2018 (bear markets in stocks ALWAYS coincide with economic recessions—no recession means no bear market in stocks). All of the fundamental credit "flags" or warning signs (such as an inverted yield curve and widening credit spreads) are absent. This is a technical correction from over bought market conditions, stretched valuations and for CDN clients, pressure from a recently stronger CAD$. It will end. And the longer term bull market cycle we are currently in will resume until we near a point of risk for the next cyclical downturn or recession.

- **Portfolios remain positive for 2017 still—**while the TSX index is down around -2% for the year so far.

- **We own a diverse basket of high quality U.S. & CDN growth companies**—and any stock weakness is a chance to buy (add to portfolios) NOT sell! Recent quarterly earnings from our names like Raytheon, Facebook, JP Morgan, Google (Alphabet), Open Text, Paramount Resources, etc., have been outstanding and some stocks like Raytheon (defense) and Paramount (energy) have bucked recent weakness and moved higher. Dumping these growth names out of an emotional panic would be a mistake.

- **Corrections are normal!** We've had more than a dozen of them since this cyclical bull market began in 2009—and the S&P Index keeps moving higher. It is true that some of the bigger names are a significant driver of the headline indices, but breadth below the surface (# of stocks advancing) remains solid with broad participation despite some recent softness. The leading market behavior of the financial stocks (the "generals" of the market) remains strong, a key sign we look for in a healthy bull market.

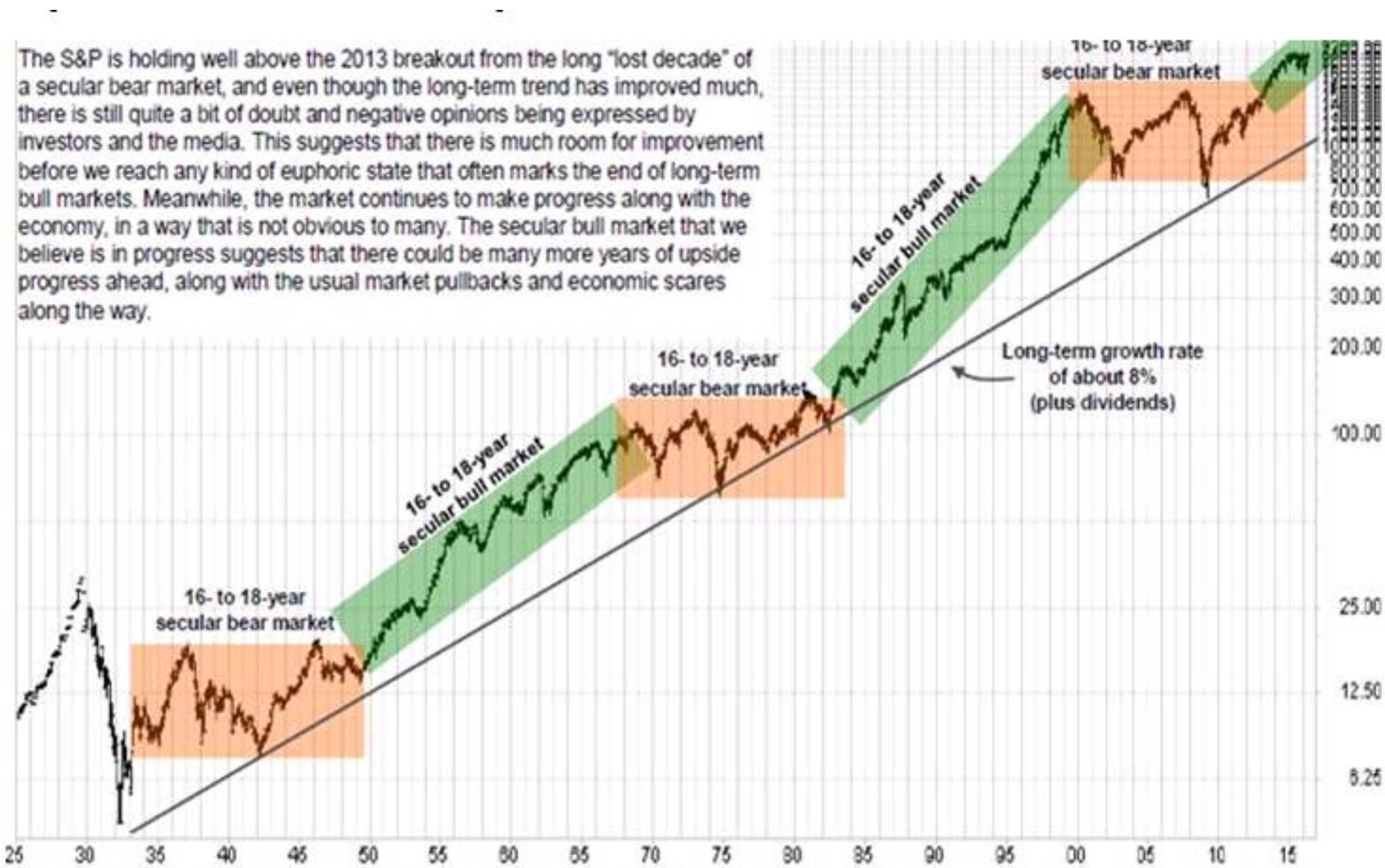
- **The U.S. equity markets continue to outperform Canada**! On weakness, I would look to add more U.S. exposure, not less; the U.S. equity markets beat Toronto (TSX) every year from 2011 to 2015 with Toronto beating U.S. side in 2016 (a one off thanks to a spurt in mining/gold/energy stocks). In 2017, the U.S. equity markets are once again beating Canada's TSX. This is the same pattern we saw during the long term, secular bull market from 1982 to 2000, where aside from a few years, the S&P 500 and Dow beat the TSX index nearly every year over nearly two decades. The United States remains a far more diverse, dynamic, capitalistic, and competitive economy than Canada (more so going forward as Canada's debt, taxes and regulations rise). So yes, my U.S. positions come under a currency headwind as the Canadian "peso" rises towards 80 cents, but as I have said of late, this CAD$ strength is NOT a long term, sustainable event. Owning great U.S. companies in USD will remain a key part of having a well-diversified portfolio for clients.

Finally, please take a close look at this long term chart of the S&P 500 Index below (the U.S. index that tracks the 500 most successful global companies) courtesy of Jeffrey Saut, Raymond James's chief investment strategist. This is a 100 year chart. You can see a series of long term, secular "stair steps" where markets move up in powerful trends and then take a break and trade sideways with several bear markets (recessions) along the way. Stepping back, this looks like a series of up steps (bull markets) followed by sideways, choppy consolidation periods (landings on the stair case). The 1930s and 1940s were marked by a major long term bear market (following 1929-1932) that after the 1932 bottom, hit a second higher bottom in 1942/43; from there a new secular bull market was born in the early 1950s which ran to a peak in 1965.

From 1966 to 1982, we see another long term secular bear market marked by inflation/high interest rates & Vietnam war. A new bull market was born in the summer of 1982, making itself apparent by 1983 when a new up market began which ran to March 2000. The Dow went *from under 1000 in 1982 to over 14,000 by early 2000*. Then, we see another bear market from 2000 to 2013! AND YES, ONCE AGAIN—the SAME PATTERN! A major break out in Spring 2013, above 1570 on the S&P 500 Index, to where we are TODAY at 2445.

How long will this secular bull market last? On average they run 14-16 years, so this puppy is only 4 years old. Depending on where we measure from, Mr. Saut thinks this bull market has at least another decade to run!

THIS is the bigger picture. Korea is noise. Will there be war?? Who knows—but I think that is highly unlikely. There is too much for the U.S. and the global economy to lose. In the end, NK will keep its nukes and the world (Trump included) will be forced to live with this reality.



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