



MARKET COMMENT

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THE RETURN OF THE KING

By: Jim Pearce

The King is alive!

No, I am not talking about Elvis Presley. Despite what you might have heard in *Men in Black*, he did not go to another planet so he is not coming back.



What I am talking about is cash (not Johnny, either), as in the old saying "cash is king."

Ever since the Fed pushed interest rates close to zero after the Great Recession, cash has taken a back seat to equity. Nobody wanted to hear how much money you had. Instead, owning shares of high-multiple stocks like Tesla and Amazon became the faddish currency of the Wall Street intelligentsia.

If you admitted to holding a lot of cash, you were thought to be either too chicken or too stupid to ride the bull market to an early retirement. That is, until last week when the reality of rising interest rates started making cash look a whole lot smarter.



I know what you're thinking. "Hey, all last week's correction did is move me back to where I was three months ago. I will gladly take that in exchange for the huge gains I have received leading up to then."

That's fine, but that is missing the point.

The reason the stock market dropped 12% of its value in only two weeks is not that some coked-out hedge fund manager fat fingered too many zeros at the end of a sell order. In fact, it's just the opposite. Last week's decline was a perfectly rational response to a growing set of data points that suggest higher inflation is on the way.

What that means is that a dollar received a year from now will be worth less than a dollar received today, and dollars received many years in the future will be worth a lot less.

This is Your 2018 Wake Up Call

For all those investors out there still holding onto to shares of overvalued momentum stocks, it's time to get serious about how much downside risk you're willing to take, and how much cash flow you'll need from your investments to make ends meet.

I realize that is not as much fun as wondering how soon it might be until one bitcoin is worth a million dollars (spoiler alert: not in your lifetime). But sooner or later you are going to want to retire (if you haven't already), and then the fun and games will come screeching to a halt.



To be clear, I don't think the stock market is about to crash. Recently, I have been calling for a correction in the 10 - 20% range so if I am correct then we are already halfway there. When the yield on the 10-year Treasury note crosses above 3%, the current correction should be complete.

However, I also do not believe that as soon as it is over the stock market is going to revert to its previous pace of breakneck growth. It was a nice run while it lasted, but I think it is over.

The recently enacted tax cut will add at least a trillion dollars to the federal deficit, and if the currently proposed Trump budget plan is passed then the shortfall will get even worse. That means the federal government will have to issue more debt to cover its expenses, which in turn will drive interest rates higher.

It has been a long time since anyone bragged about owning value stocks, but I believe that day is coming back, too. Companies that generate a lot of positive cash flow and share it with their shareholders via dividends and stock repurchases will come back into vogue.

I know, that is a hard argument to make to investors that have become used to earning 10%+ on their stock portfolios every year. My friends tease me for being a "Debbie Downer", but I feel it is my duty to warn them before they learn the hard way.



In my role as Director of Research for Investing Daily, I spend a lot of time thinking about what we can do to help our subscribers achieve their financial goals. And right now, I think owning stocks that pay out a lot of cash to their shareholders is one of the best ways to do that.

Long live the king!

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