Third Party Research September 14, 2018

Weekly Market Review

***e*Research Corporation** is pleased to provide a review of the markets by Eddy Elfenbein of **Crossing Wall Street**.

Mr. Elfenbein introduces his commentary with the following quote from Charlie Munger (Berkshire Hathaway):

"A lot of people with high IQs are terrible investors because they have got terrible temperaments. You need to keep raw, irrational emotion under control."

Read Mr. Elfenbein's analysis and market comments on the following pages.

Information about **Eddy Elfenbein** and **Crossing Wall Street** is provided at the end of this article. You can also learn about **Crossing Wall Street** by going to its blog website at: http://www.crossingwallstreet.com/.

***e*Research** was established in 2000 as Canada's first equity issuer-sponsored research organization. As a primary source for professional investment research, our Subscribers (*subscription is free!!!*) benefit by having written research on a variety of small- and mid-cap, under-covered companies. We also provide unsponsored research reports on middle and larger-sized companies, using a combination of fundamental and technical analysis. We complement our corporate research coverage with a diversified selection of informative, insightful, and thought-provoking research publications from a wide variety of investment professionals. We provide our professional investment research and analysis directly to our extensive subscriber network of discerning investors, and electronically through our website: www.eresearch.ca.

Bob Weir, CFA
Director of Research

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September 14, 2018

Crossing Wall Street: Weekly Market Review

by Eddy Elfenbein

BW: We have taken only an extract of Mr. Elfenbein's latest weekly article. If you wish to read the entire article, which includes stocks in his recommended portfolio, there is a link provided below.

In this week's *CWS Market Review*, I want to cover some recent economic news, including last week's jobs report and this week's subdued inflation report. I also want to touch on an overlooked issue, which is the spreading chaos in emerging markets. This isn't getting the attention it deserves.

The "Raise-Less" Recovery

Last Friday, the government reported that the U.S. economy created 201,000 net new jobs in August. That is basically in line with the current trend. Over the last seven years, the economy has created 17.3 million new jobs. That is an average of 205,000 per month. Officially, the unemployment rate is 3.9%. The current unemployment rate is lower than it was in *every single month* during the 1960s, 1970s, and 1980s.

While that is good news, there are some weak spots to note. Not as many Americans are in the workforce as there were a few years ago (although this trend is not as bad as some alarmists would lead you to believe). This trend may soon change. This week's report on job openings was an all-time record. There were 6.9 million job openings in July. That is the highest since the data series started in 2000. Another report from small businesses showed that more companies are having trouble finding new workers, and Thursday's initial jobless claims report was another 49-year low.

The other weak spot in the economy is wages. You would think that with emerging labor shortages, there would be an increase in worker pay. While there has been some improvement here, it is not much to celebrate. In the last year, average hourly earnings are up 2.9%. The last economic recovery was described as a "jobless" recovery. This one seems to be a "raise-less" recovery.

As investors, wage growth is important to us because that is where future business revenue comes from. We want to see more shoppers. This leads us to the issue of inflation. With subdued wages, there has not been much pressure on consumer prices. On Thursday, Wall Street had been expecting the August CPI report to show an increase of 0.3%. Instead, it came in at 0.2%. In the last year, inflation is running at 2.7%. The number is a bit skewed

because inflation ran slightly hot in late 2017. Over the last six months, inflation is running just under 1%. Expect to see that 2.7% number trend lower over the next few months,

I also like to look at the inflation report for “core prices,” which excludes food and energy prices. In August, core inflation rose by just 0.08%. That is the second lowest report since January 2015. This really tells me that inflation is not a problem. The bond market continues to be quite happy with the current state of things. The 10-year Treasury is still below 3%. I don’t think a lot of bond watchers thought that would happen.

All this leads us up to the next Fed meeting, which is scheduled for September 25-26. The odds are roughly 99.9999999% that the Fed will raise rates at this meeting, although I could be low-balling it. Another rate increase would bring the target for Fed funds up to 2% to 2.5%. That would bring real rates (meaning, after inflation) all the way up to 0%. Real interest rates have been negative for 14 of the last 17 years.

There is also a chance another rate hike could finally invert the yield curve. The spread between the two- and ten-year Treasuries is currently just 21 basis points. That is close to being the lowest point in 11 years. A rate hike in December is still an open question, although I seem to be in the minority. Wall Street is nearly convinced the Fed will move again. I am not so sure. While the economy is definitely improving, there is still not much in the way of pricing pressures. The futures market even thinks there will be a third hike coming in May.

Chaos in Emerging Markets

While the U.S.A. still looks mostly good, some economies overseas are crashing on the rocks. This happens every few years, and it looks to be happening again. So far, the main culprits are Argentina, Russia, South Africa, and Turkey. With any crisis like this, there is always the worry of contagion, which means watching the meltdown spread from country to country.

All four countries have different reasons for the mess they are in. Argentina borrowed too much. The peso got clobbered, and their Fed has had to jack up rates to 60%.

In Turkey, President Erdogan has made just about every bad economic decision you can. He recently said, “If they have dollars, we have our people, our righteousness, and our God.” Apparently, the bond market prefers the dollars. On top of that, President Trump has doubled tariffs on Turkish steel and aluminum. Erdogan has also named himself the head of Turkey’s sovereign wealth fund, which I am guessing, will not reassure foreign investors. To give you an idea of the kind of building that has been going on, when Erdogan became president 15 years ago, there were 50 shopping malls in Turkey. Now there are over 400.

With Russia, the country has been steadily isolated from the global economy. The ruble has been hammered against the dollar. Interestingly, Russia does not have that much debt relative to GDP. Their problem is that they cannot turn to financing from foreign investors. That means much of their investment must come from inside, i.e., from spending targeted for something else.

I want to be clear that these problems aren't much of a threat to us. If anything, our conservatism is probably helping us when compared to the chaos of these economies. The major **Emerging Markets ETF** (EEM) is down about 20% from its January high.

There tends to be a familiar script with financial crises. A country borrows too much. At some point, the bond market has had enough. Bond yields soar, and the currency tanks. That leads to political upheaval as inflation takes hold and the central bank raises rates to defend the currency. There are a zillion different permutations, but that is the general idea. The only way to solve the mess is by making hard decisions. You cannot cheat debt investors forever.

We should keep an eye on these issues. So far, I doubt they will continue to spread, but when markets turn manic, you never know where it will end.

Next week should be fairly quiet for economic news. However, I will be on the look-out for the housing-starts report, which is due out Wednesday morning. Then on Thursday, we will get existing-home sales and the jobless-claims report. The following week should be even more eventful, as the Federal Reserve has a two-day meeting. Expect to see another rate increase from the central bank.

Be sure to keep checking the blog for daily updates, and I will have more market analysis for you in the next issue of *CWS Market Review*!

- Eddy

BW: In the rest of the newsletter, Eddy reviews the earnings announcements of the companies on his Buy List. You can read about them and the entire article by clicking on the following link:

http://www.crossingwallstreet.com/archives/2018/09/cws-market-review-september-14-2018.html

Named by CNN/Money as the best buy-and-hold blogger, Eddy Elfenbein is the editor of Crossing Wall Street. His free Buy List has beaten the S&P 500 for the last six years in a row. This email was sent by Eddy Elfenbein through Crossing Wall Street.

BW: Information on Eddy Elfenbein and Crossing Wall Street follows on the next page.

ABOUT THE AUTHOR

Welcome to Crossing Wall Street

I started this Web site to help individual investors. I have to admit that I *love* the stock market. I think I must be an addict. In my opinion, the stock market is one of the greatest inventions in history. The stock market is simply the most consistently successful way to make money over the long term. Even after the financial crisis, stocks have still beaten every asset category over the long haul—bonds, commodities and real estate.

While the stock market may bounce around from day to day, and even month to month, the long-term trend has always been higher. Over the last 35 years, stocks have gone up 35-fold. And since the end of World War II, the stock market is up an amazing 120,000%. I wish I had been around! That was the beginning of an American financial revolution. Today, weare at the beginning of a *global* financial revolution. That is why I think the next 70 years will be even better.

The key to doing well on Wall Street is actually very simple: Buy and hold shares of outstanding companies. But too many investors never learn this valuable lesson. Or if they do learn it, they learn it the *hard* way. That is where I come in. I want to help investors avoid the mistakes that separate successful investors from those who always find themselves spinning their wheels.

There are lots of pitfalls on Wall Street. From shady companies that are more popular than they are profitable to a mutual fund industry that is more interested in its fees than serving investors. Todayis investors must be careful.

At Crossing Wall Street, I give investors my free and unbiased view of the market. I probably analyze dozens of companies every week. I am always looking over income statements and balance sheets. I've spent several years collecting my list of the best companies to own. This is my current Buy List. I've included a description of each company and its current share price. These are the ones that I make the most effort to follow on the site, but please feel free to ask me my opinion on any stock. I don't receive compensation from any of the stocks I recommend. Also, I don't "short" any of the stocks I criticize. At any time, I may own the companies on my Buy List. All of the information on this site is free and unbiased. I also have a section for Frequently Asked Questions that will help you learn more about Crossing Wall Street.

Please feel free to e-mail me. I enjoy getting feedback from investors. I am happy to give you my opinion on any stock or investing in general. I should warn you that I cannot give out personal portfolio advice, but all other topics are fair game. You can also check out some of my favorite links.

- Eddy Elfenbein

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