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Steering through truths and half-truths

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In defensive driving, we learn how to handle unpredictable situations on the roads. We learn how to "jam brake" or more correctly, jam on the brakes, which is the sudden and forceful use of our cars' brakes in the event of an emergency.

We are prepared to "jam brake" if we need to. However, as of now, we do not need to as our investment strategy is based on the assumption that a potential black swan scenario of major conflict or even nuclear destruction arising from actions from North Korea or the major powers will not happen.

I will move to cover another area which has been circulating around the media – the fight against "fake news". My advice to my readers is not to be carried away with every news which come your way. It is not necessary to follow all the news and it is certainly not advisable to try to follow everybody. Which is more important, which is more serious – a glass half empty or a glass half full? There is more than one way to analyze a situation and statistics can lie, if you want to massage them (or the interpretation of the same data) to your benefit.

I will update on some "old" topics which I have discussed at many of my seminars. In this article, I retain some assumptions: whereas the world may be sceptical of economists, we can still make use of some of the hard work done by economists; whereas economic theories are continually being tested and challenged by academia and private sector analysts, some statistics and behavioural observances are still useful in social sciences.

In the extract from the International Monetary Fund's July report (Refer to Table 1), we see that the IMF is projecting improvement in economic growth for this year but slower growth for some major countries next year. A couple of downward revisions by the IMF is noted for the United States and the United Kingdom for this year but we are still expecting healthy growth for both countries. The Eurozone is also projected to grow, by a healthy 1.9%.

As I write, the Dow Jones Industrial Average has yet again reached a new high of 22,557.60. There has been much scepticism on the performance and outlook for the US stock market, with concerns that the Dow has been driven by technology stocks and that valuations are "lofty". I think much of these concerns are exaggerated and that valuations will be lower when corporate earnings grow at a faster rate than share prices. I have read of earnings projections which show that forward valuations are lower than historical averages. To be fair, I think it is not easy for analysts to make earnings projections or for investors to make an investment call on technology stocks. I find that Price-to-Earnings, Price-to-Book or Price-to-Cash Flow can be poor yardsticks to use in investing in these stocks.

On technicals, there are always tops and bottoms, even if they are called "intermediate" tops and bottoms. There are also "corrections" and "consolidations" in our investment journeys. Notwithstanding these market behaviours, I think we are in a multi-year uptrend for equity investing on the back of continuing economic improvement and corporate earnings growth.

There is also scepticism on the ability of the US central bank in reducing its balance sheet. The situation reminds me of the heightened fears over the figures flashed on the US National Debt Clock. I think these sceptics are missing the point. If we were to see it positively, the US Federal Reserve has decided that the time is right to reduce its stretched balance sheet, just as it decided that it was time to start raising interest rates.

In this respect, although I am not positive on the outlook for the US dollar, the US currency is expected to find some support or further rebound from the recent weakness on expectations of higher interest rates. On the flip side, gold and silver prices, which tend to move in opposite direction to the US dollar and interest rates, are not likely to show significant strength in the near term.

Table 1. Overview of the World Economic Outlook Projections

(Percent change unless noted otherwise)

	Year over Year						Q4 over Q4 2/		
	Estimate		Projections		Difference from April 2017 WEO Projections 1/		Estimate	Projections	
	2015	2016	2017	2018	2017	2018	2016	2017	2018
World Output	3.4	3.2	3.5	3.6	0.0	0.0	3.2	3.5	3.7
Advanced Economies	2.1	1.7	2.0	1.9	0.0	−0.1	2.0	1.9	1.9
United States	2.6	1.6	2.1	2.1	−0.2	−0.4	2.0	2.0	2.3
Euro Area	2.0	1.8	1.9	1.7	0.2	0.1	1.8	1.9	1.7
Germany	1.5	1.8	1.8	1.6	0.2	0.1	1.8	1.9	1.5
France	1.1	1.2	1.5	1.7	0.1	0.1	1.2	1.7	1.5
Italy	0.8	0.9	1.3	1.0	0.5	0.2	1.1	1.1	1.0
Spain	3.2	3.2	3.1	2.4	0.5	0.3	3.0	3.0	2.1
Japan	1.1	1.0	1.3	0.6	0.1	0.0	1.6	1.2	0.5
United Kingdom	2.2	1.8	1.7	1.5	−0.3	0.0	1.9	1.4	1.4
Canada	0.9	1.5	2.5	1.9	0.6	−0.1	2.0	2.3	2.0
Other Advanced Economies 3/	2.0	2.2	2.3	2.4	0.0	0.0	2.5	2.1	2.7
Emerging Market and Developing Economies	4.3	4.3	4.6	4.8	0.1	0.0	4.2	4.9	5.2
Commonwealth of Independent States	−2.2	0.4	1.7	2.1	0.0	0.0	0.6	1.5	2.0
Russia	−2.8	−0.2	1.4	1.4	0.0	0.0	0.3	1.5	1.8
Excluding Russia	−0.5	1.8	2.5	3.5	0.0	0.0	. . .	. . .	. . .
Emerging and Developing Asia	6.8	6.4	6.5	6.5	0.1	0.1	6.3	6.6	6.5
China	6.9	6.7	6.7	6.4	0.1	0.2	6.8	6.4	6.4
India 4/	8.0	7.1	7.2	7.7	0.0	0.0	6.0	8.0	7.6
ASEAN-5 5/	4.9	4.9	5.1	5.2	0.1	0.0	4.8	5.2	5.2

Source: IMF, July 2017

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