Monthly Commentary 3rd May 2018

Following a difficult first quarter, global equities rose in April, up 1.7% on aggregate as measured by MSCI World in local currencies. Europe and Japan led the way up with the US the only major market that was only slightly up. World bonds were almost universally down and commodities had another strong month with oil leading once again. The financial news that is increasingly making the headlines is the strength in the USD, which rose almost 2% in April as measured by the USD Index.

With world trade being so much in the news, currency exchange rates are affecting equity markets, which seem to have become more negatively correlated with each country's exchange rate. The FTSE was bolstered by 6% in April, while pound sterling reversed its prior YTD strength to end the month down almost 2%. Views on where the dollar is heading are mixed, with many pundits saying that the recent strength will continue for a while but within the context of a more secular downtrend for the USD. Go figure!

Fear and the markets

While most equity markets rebounded in April, it seems that there is still a lot of fear among investors. Below is a headline from the Wall Street Journal (April 27) that says investors are voting with their feet.

Stock Funds Suffering Big Outflows as Rattled Investors Rush to the Exits

Investors are dumping U.S. stock funds at one of the fastest paces in a decade as rising market turbulence erodes confidence in the nine-year-old bull market.

There is no doubt that there is much more fear this year than in 2017. And indeed, fear sells. As Daniel Gardner wrote in his book "The Science of Fear": *Fear sells. Fear makes money. The countless companies and consultants in the business of protecting the fearful from whatever they may fear know it only too well. The more fear, the better the sales.*

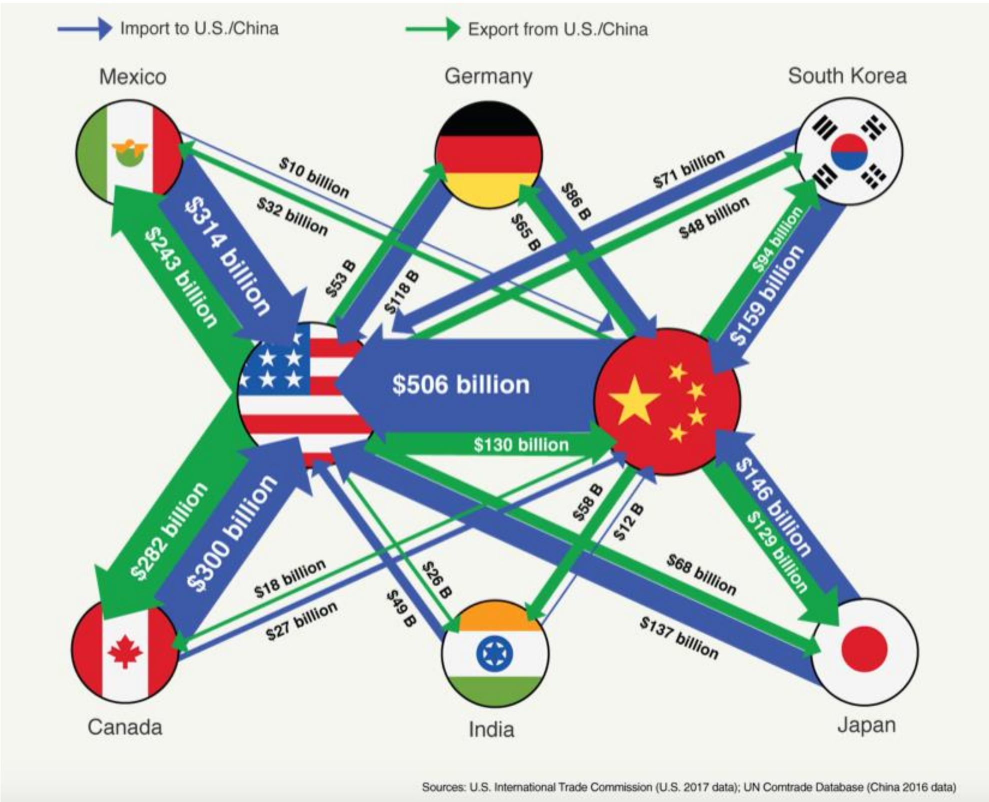
So is it this fear that is causing all this worry that is leading to redemptions? Partially, we would say "yes". But fear is not new and as Warren Buffet put it:

In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497.

And that was a while back. The Dow has actually more than doubled since then despite the multitude of fears. Point made.

Trade in pictures

With talk of the US imposing tariffs on trade, we thought it would be apt to present the below graphic of some major trade flows.



Any conclusions drawn from this would be simplistic, but here are a few:

- The lopsided trade in goods between the US and China is probably what the US administration is trying to address. Of course, it is not as simple as the raw numbers might suggest. This does not include services. Nor does it include components. So, for example, iPhones made in China and exported to the US include the value of the finished product as a 100% export from China to the US. Yet, more than 80% of the iPhones' components are imported by China from abroad. Additionally there are restrictions to some US exports to China.
- The trade between the US, Canada and Mexico is larger than between the US and China. Perhaps that is why NAFTA (the North American Free Trade Agreement) is being renegotiated.
- India is not exactly a big trading nation when considering the size of the country's population.
- Germany has a big trade surplus. Surprise.

In the end, we are of the opinion that it is not in the best interests of the USA to initiate trade wars. Somehow there will be compromises and trade will continue to add to global growth in a meaningful way. We, and most investors globally hope we are right.

The Elgin Analysts' Team