Scotty C. George
Chief Investment Strategist

October 29, 2018

Market Outlook:

Shock waves

It's impossible to know what is in the *heart and mind* of a corporate executive, but we can measure precisely the effect of their *actions*. After reviewing the compiled data from last week's 3rd quarter earnings reports the thing that stands out most significantly is that stock repurchasing and share buybacks remain the primary drivers of share price performance in this climate of (still) low interest rates. Bear in mind that a significant portion of these executive's compensation is linked to the (upward) price momentum of their company's shares.

But what happens when the momentum stops, such as what is occurring lately? Might it trigger a landslide of insider selling?

No matter the reason, the people in control of the money continue to exert an enormous amount of alchemic influence over the direction of the financial markets. It used to be that the primary, and definitional, causes for market performance were *demand* and *sales*. No longer. They seem to be playing a secondary role in equity price performance.

Add in the fact that political and diplomatic turmoil all across the globe is tipping the psychological scales, and you might easily see how the market could "blow up" despite improving fundamentals.

And yet, even as the market has experienced some recent weakness, an enormous amount of sequestered cash is serving as a kind of "support" for the averages as the cash is being deployed for additional share buybacks.

What used to be an orderly flow of money now feels strangely disjointed and manipulated. This disjointedness seduces investors into greater risk-taking in an effort to squeeze every last drop out of their pursuit for wealth-building.

Look forward, not back

As interest rates rise, however, a new chapter in risk management strategies is being created. Last week's earnings reports clearly indicate that as the cost of raw materials, wages, benefits and other expenses increases, the ability to widen the profit margin diminishes. The higher cost of financing all corporate purchases, decisions, and capital expenditures heightens the volatility for stocks and other asset classes. **The uncertainty that ensues will likely create a faster flow of money in/money out in the market. Stock trading profits are more likely to result in quicker sales at the top, while capitulations could cause a wave of bottom fishing at the nadir.**

In either case, we know that volatility is likely to amplify.

The euphoria of the past few years has a new complement....a kind of ominous, sterner examination that overarches all sectors of the economy. As stated earlier, despite the improving fundamental data, psychology and cycle phase momentum still exert a very powerful influence over the direction of confidence and market activity.

Besides depressing some of the euphoria investors felt during the post recession recovery, higher interest rates also offer us the chance to diversify portfolio balance. Using short term time deposits to enhance portfolio returns is an outstanding strategy for deploying cash currently held as a surrogate (default) to buying stocks. In the long run, this might even prove to be a positive force for building cash reserves that later will be used for discretionary purchases.

The landscape of tighter money is borderless. Global central banks are coming to the conclusion that they led this horse to the water, but *couldn't make him spend!* Consumers and businesses alike are playing it close to the vest with their money right now, while concerns about the breadth of economic expansion are magnifying.

Monetary policy is obviously a very complex matter. It is also a fluid narrative that requires us to have an open mind, a specific investment discipline, and the realization that trading in the short-term is a less successful method for generating portfolio wealth than taking a top down, multidimensional approach to financial security.

In other words, stop trying to force a square peg into a round hole, and start to capitalize upon the growing changes we see around us.