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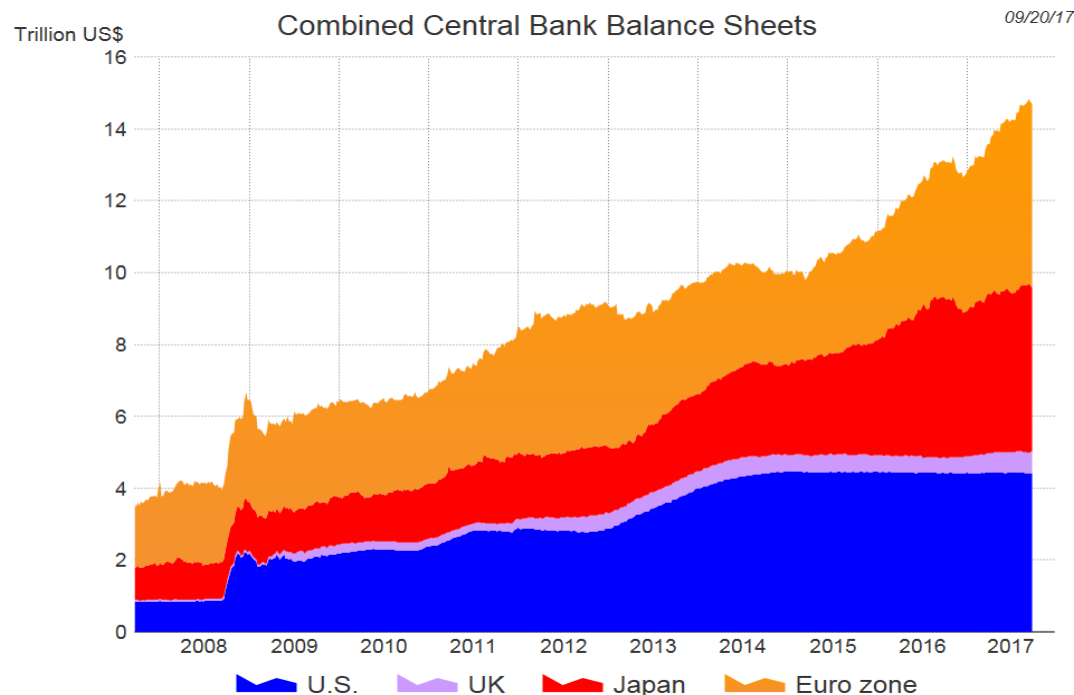
What We Worry About...

Our recent weeklies have focused on addressing what we believe are the concerns of our readers and reconciling them with our positive outlook for stocks. Despite that, we are often asked what we do worry about. Here are five things:

1. Excessive focus on what's Urgent, not enough on what is Important. We worry that our clients will focus too much on what appears URGENT (North Korea, and other current headlines) and not enough on what is IMPORTANT – getting comfortable with an investment plan that can navigate crises. Of course we worry about unintended outcomes from events like North Korea's current war of words with the US, but we do so in the hope that our clients trust us to assess the risks and act in accordance with our risk management disciplines if necessary. Determining the right long-term asset allocation is the key to long-term investment success. In our view the right asset allocation is the one you can live with through both crises and good times, without being too fearful or too greedy.

2. The Unwinding of QE and complacency in the bond market. The Fed has been deploying unconventional (some might say experimental) monetary policy since the great recession of 2008/9. They have done it successfully in our view, judging by the upward trajectory of the economy and corporate earnings and the downward trajectory of unemployment, all with no increase in the trend of inflation. Their success has caused the other major central banks to follow their lead creating some \$15 trillion in global central bank balance sheets. Starting with the US, the next few years will likely see unwinding of balance sheets, which will involve selling bonds. We think bond investors have become overly complacent and may not be prepared for greater volatility and slightly higher rates as those balance sheets are unwound. However, we believe rates will not rise far enough to end the bull market stocks, especially overseas where the ECB (European Central Bank) and the Bank of Japan are still buying bonds and increasing the size of their balance sheets as our chart below shows. (Please see Strategic View from Sept 25th *The End of "QE" Means Higher Rates, Resilient Stock Markets and Volatility*)

EUROPE AND JAPAN HAVE BEEN THE GROWTH DRIVERS SINCE 2014.



Source: Thomson Reuters Datastream, RiverFront

We worry that our clients will focus too much on what is URGENT and not enough on what is IMPORTANT, namely getting comfortable with an investment plan that can navigate crises.

In our view the right asset allocation is the one you can live with through both crises and good times, without being too fearful or too greedy.

3. **Being perceived as ‘perma-bulls’.** We have been strategically bullish about global stocks since early 2009 based on our Price Matters assessment of expected returns. As a result, our commentary has tended to be optimistic, and we have sought to calm investors’ nerves during periods of volatility. Notably, our current technical read on market structure is also echoing our constructive fundamental read. However, we are not ‘perma-bulls’, meaning we do not have a permanent optimistic outlook on the market. If stocks become overvalued on our asset allocation framework or enter sustained downtrends, our disciplines and our commentary will likely change. We have been consistently cautious about longer maturity, high quality bonds as they seem to us to offer poor risk/reward at such low yields. While our worst fears regarding higher rates have not been realized, returns on high quality, long maturity bonds have been low now for several years. We continue to expect stocks to do better.
4. **Clients with longer time horizons holding too much cash.** We worry about the following irony: by being too conservative today an investor misses out on the most powerful force in investing which we believe is *time*, and subjects themselves to the higher likelihood they will need to take more risk later on in order to try and achieve their goals, when they can least afford to do so. Alternatively they might be forced to lower their expectations if they want to remain with a very conservative allocation.
5. **US Stocks ‘Melt-up’.** While many of our clients worry about a meltdown, we worry as much about a rise to levels significantly above trend. Why worry about such a strong US market? Well, when assets become overvalued, it is hard to know when it will end, but the subsequent bear markets tend to be severe. Also, psychologically that kind of excessive bull market eventually draws in investors/speculators that often end up losing money. We believe our Price Matters discipline will assist us in identifying the dangers but we know from 1997-1999 that these kind of markets can cause investor ‘greed’ just as bear markets produce ‘fear’ and both can lead to investors abandoning a well thought out plan. International markets are far enough below trend that a melt-up scenario is not currently relevant in our view.

WHAT WE DON’T CURRENTLY WORRY ABOUT

1. The global economy. We believe a global synchronized and sustainable recovery is in place and that current policy intentions are likely to keep it going for several years. This has led to positive earnings surprises and strong stock markets, in our view. The momentum in most economies across the world suggests to us that a recession is still quite some time off in the distance.

2. Central Banks determination to avoid deflation. Deflation is the enemy of the debtor. We believe Central Banks have clearly realized that in an era of excessive government debt, erring on the side of creating a little too much inflation makes sense. So far, the main consequence of potentially inflationary policy has been the inflation of asset prices such as stocks, bonds and property.

3. The impact of Washington on the stock market. Between the election last November and President Trump’s first speech to Congress in February 2017, the stock market became very excited about the potential for policies designed to increase economic growth. The reality of governing has proved challenging for the President and Congress. What the President hoped to achieve in his first nine months has so far fallen short of expectations. That said, he has reduced regulation and is likely to achieve corporate tax reduction, both of which we think should be positive for stocks. There was also concern that his policies on trade with China could have a negative impact on the market; however, the situation in North Korea has offered China the chance to side more with the US, which should help them when it comes to trade.

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