Summa Global Advisors

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Climbing the Wall of Worry

This six-year bull market continues to climb a wall of worry, as the familiar Wall Street saying goes. Equity investing is a difficult task. In 2011, Richard Bernstein, a noted money manager, stated that, "This cycle is the biggest wall of worry I have ever seen or will ever see in my entire career." He continues, "It seems no one wants to believe in the stock market in the United States. People don't accept that the American economy may actually be strengthening. And they go for emerging markets, which are wildly overpriced." Bernstein maintains that there is no reason why investors should be avoiding American stocks, as the economy is clearly strengthening and corporate profits rising.[1]

Roger's Wall of Worry		
US ECONOMY	EURO ZONE/ GREECE DEFAULT	RUSSIA/PUTIN
DOMESTIC STOCK MARKET VALUATIONS	CHINA	CORPORATE EARNINGS
JAPAN'S QE	COMMODITIES PRICE COLLAPSE	MIDDLE EAST UNREST

As many investors recognize, the wall of worry is constructed of a number of serious concerns. In the same April 2011 New York Times article, David Rosenberg, an economist with Toronto-based Gluskin Sheff, takes a ferociously bearish position. Rosenberg agreed with his colleague, Bernstein, in his opinion that emerging markets were overpriced at the time, yet disagreed with much of the rest of his analysis. Rosenberg believed that the increase in American stock prices was largely generated by the expansionary monetary policy of the Federal Reserve. Other global events have also impacted the American bull market, including geopolitical peril in the Middle East and North Africa, severe danger of sovereign debt default in Europe, surging oil and food prices, and a sluggish economic recovery that has necessitated intervention from the Fed.

Global turmoil persists in forms as diverse as political and economic unrest to global warming and natural disasters. Recent debacles include the February 2014 Ebola outbreak in West Africa, the Syrian civil war, the ISIS rebel crisis in the Middle East, and the exporting of ISIS extremism elsewhere. Additionally, military aggression, orchestrated and initiated by a bellicose Mr. Putin, is especially dangerous. The Crimean and eastern Ukraine invasions by Russian Special Forces have a significant risk of leading to greater conflict. Recent Chinese naval expansion in the South China Sea is also a dangerous military stance.

Economically, the recent establishment of the Chinese-sponsored Asian Infrastructure Investment Bank (AIIB) will endeavor to challenge the U.S. dollar for global priority in the future. However, there is concern regarding the strength of the Chinese economy and the speculation which drove high Chinese stock and real-estate prices. As the world's second largest economy, this is now of significant importance to the global economy. Global commodity prices have been negatively impacted with a substantial decline in the prices of oil, copper, iron, and other goods. Japan, the world's third largest economy, has implemented quantitative easing (QE) in an attempt to leverage the economy after 20+ years of deflation. The results of this economic stimulation remain to be seen, but should this economic experiment stall, the Japanese yen is at risk of devaluation.

The euro zone economy, as a block, has about the same GDP as the U.S., and appears to be recovering. Europe has also implemented QE, however, it is far too early to see the impact of the increased money supply on its economy. Europe, excluding Greece, has had relatively flat economic growth. The European economy is strained by other factors such as high unemployment, Muslim population explosion, and an influx of illegal immigrants.

As the world's largest economy, the U.S. continues to grow at a slow rate. Wages have begun to increase; unemployment is near 5%, declining from a 10% high in 2009. The drought in the western states may impact food prices. Domestic equities and bond valuations remain high by historical norms and are a concern to some analysts.

As we enter the second half of 2015, there are a number of issues to contend with. In order for equity prices to advance further, positive corporate earnings and positive political and economic events will be required both domestically and internationally.

Footnotes:

1. http://www.nytimes.com/2011/04/17/your-money/stocks-and-bonds/17stra.html?_r=0