

The Outlook: June 29, 2019

The Big Picture

Let us step back, halfway through 2019, and see the Big Picture as clearly as we possibly can. The Big Picture, remember, always comes in 2 halves, hence 2 questions:

1. What is the health of the real economic world, which we sometimes call “Main Street?”
2. What’s in the mind of the investment world: “the market,” for short?

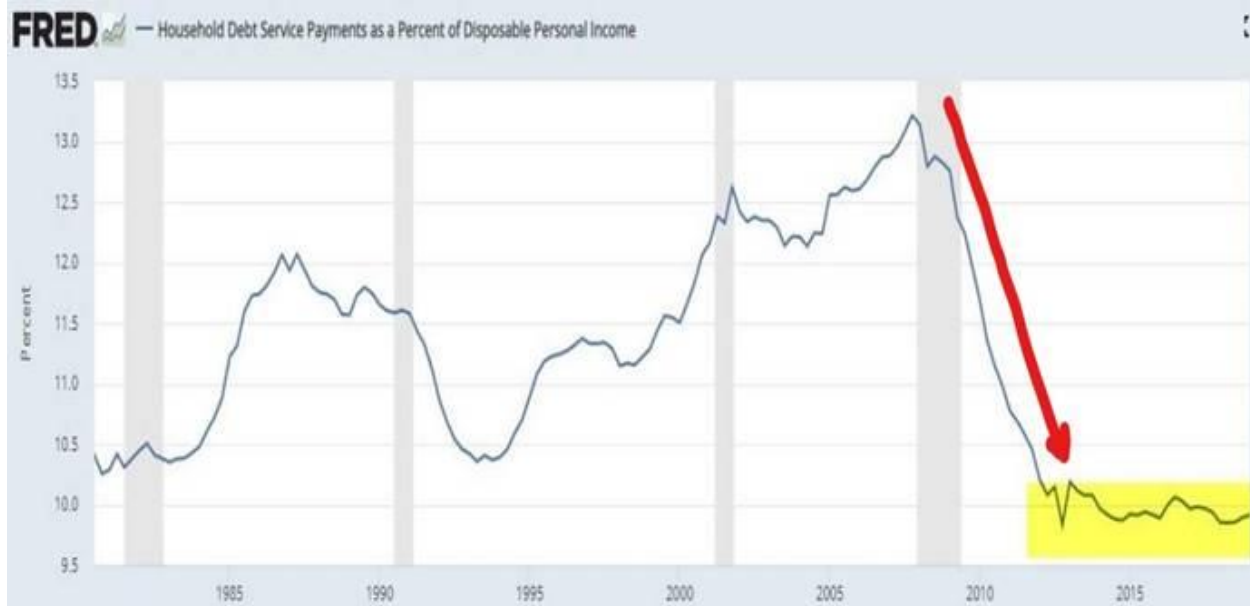
Of course those 2 worlds are connected . . . but they’re profoundly different. The first is the world of companies and individuals at work every day and—in all free-market, competitive economies—doing the best job they possibly can to financially better themselves and their businesses, every day. 99% of all those companies and people know exactly what they need to do, each day, to keep moving toward that goal . . . and they would regard any moments spent wondering how a billion other people are thinking or feeling as a waste of time.

The investment world, on the other hand, is entirely different. The markets which bring together buyers and sellers of financial assets are, at bottom, a vast collection of people who are intensely concerned with “how a billion other people are thinking or feeling” at the moment. The collective actions of those billion people determine how much each one of them is worth . . . moment by moment. We all understand, don’t we, just how strongly that changing value of our money pulls on our thoughts and feelings whenever we walk through the investment world, wondering what to do. But it doesn’t just “pull.” It quite often and easily wrecks our ability to think clearly about whether those moment-by-moment values pegged by the market actually make sense, or not. In a nutshell, when our own money is on the line, fear (or sometimes greed) stands right next to us, whispering that there’s surely something wrong with our judgment of sensible value, when a billion other people disagree.

- **The Health of Main Street.**

In the U.S. there is only one possible word: “good.” In most of the rest of the world, it’s anywhere from “tolerable” to “pretty good.” The picture below is just one single temperature reading among the dozens or hundreds available . . . but it still captures the essence of Main Street’s health in the USA.

Household Debt Burden at a 40-Year Low



That plunging red arrow says, “This is what people and companies do, when they’ve been scared to death. They go all out to make sure it never happens again.” The Financial Calamity, deep recession and shocking bear market of 2008 – 2009 scared us to death, all right . . . but then we proceeded to *do* something about it. This chart is labeled “Households,” but it truly captures the spirit of the same self-preserving actions taken by all kinds of companies in the last 10 years. Banks, for example, which were at the very heart of the Calamity, just made the news again last week when all 18 “big banks” passed the Fed’s “stress tests,” allowing them to hike their dividends and share buybacks (again.) The financial strength of the U.S. banking sector today is so far beyond what this particular banker saw 15 years ago (when he left the banking industry) that words fail us—particularly since we bankers of 15 years ago *thought* our industry was historically strong, back then.

These changes matter very much, as we think about Main Street’s health. In all the world’s history of economies and markets, the most genuinely frightening recessions, depressions and bear markets have always been wrapped around “too much debt, too weak banks.” On Main Street USA we do not have that problem today. Main Street Paris, Berlin, Beijing, Seoul, or Tokyo (and all the rest) do not stand on America’s rock-solid ground . . . but most of those Main Streets have their own red arrows of improving financial strength, over the decade, even if less strong than ours.

So “tolerable to good” describes the actual global health and strength of Main Street. But what are those billion mind-readers in the investment world thinking and feeling about it?

- **Today’s Market: the State of Mind of the Other Billion.**

In the U.S. there is only one possible description. It has fit for the last 10 years, and it still fits today: “Mostly cautious. Easily frightened.” Those are the right words, regardless of the countless authorities who have spent the 10 years explaining to us that the right words ought to be, “Exuberant!” or “Misguided!” or “Dangerously Suicidal!” (which does get our attention, when Fear whispers it in our ears.)

Investors and speculators argue every day about “value.” Today’s large-market price/earnings ratio of about 16, for example, means “distinctly optimistic and probably over-valued” to pessimists, and “quite reasonable, and near long-term averages” to optimists. It won’t help us much to explore their arguments. This is better:

Since January 2018: Up 11%, Down 20%, Up 17%.



The red arrow (2018’s fourth quarter) tells its story: “Easily Frightened!” It was the market’s worst “Trade War Nightmare” episode so far. Regardless of today’s “Let’s talk again” headline from President Trump and Chairman Xi, it probably won’t be the market’s last Trade War Nightmare. (At Outlook we suspect we have years of them on the way.) Those billion players in the investment world absolutely do not know what the “Trade War,” however it turns out, will actually do to Main Street. Nobody does, including the sharpest-penciled economists in the world, many of whom have been dead wrong, so far, in exaggerating the damage they thought “Trade War” should already have done to Main Street.

“Trade War” is something new, hence triggers our fear of the unknown. But Outlook’s judgment is that the market’s “easily frightened” state of mind shows a typical market departure from good sense and clear thinking about value. Global Main Street is solid, by and large, and in general it is not carrying around the ticking time bomb of “too much debt, too weak banks.” So when fearful unknowns like “Trade War” come around the corner, they may do some damage but they’ll have a very hard time running Main Street and Wall Street right off a cliff, as the Calamity did in 2008 – 2009.

So the Big Picture shows us very much the same thing it’s shown for 10 years: “Most U.S. companies exceptionally strong. Most U.S. companies backing up their financial strength with steady growth in cash

paid to shareholders. The market still “cautious, easily frightened.” Valuations (both in the U.S. and globally, interestingly enough) emphatically cautious for the vast majority of big companies, even if downright “exuberant” or even “dangerously suicidal” for a relative few.”

It's not a very cloudy picture. It's pretty clear. For Outlook's clients, we're holding and buying more shares whenever we can.

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