The Outlook: Aug. 15, 2018

The market's Turkish nightmare . . . and the rest of the world's facts-on-the-ground.

The market has been wallowing in another "end of the world" moment lately: triggered this time by the collapse of the Turkish lira. It's hard to find a nice picture of the lira—which has fallen 40% against the dollar this year, and 20% in a couple of days lately—but it's easy to find pictures of the damage the market's end-of-the-world mood has done to some of our core holdings lately. Micron and Transocean, below, capture the mood; and if we re-labeled either chart "Turkish Lira" we'd see a fair enough picture.

Micron: One Month

Transocean: One Month

It is the nature of the market to wallow, fairly often, in end-of-the-world moods. The world doesn't actually end, most of the time. Once in a great while a market wallow turns out to look far-sighted, looking backwards, when the world really does get into fairly serious trouble. But the great crowd of speculators whose daily actions wash through the market, and push prices wherever the crowd hopes or fears they'll go—for a while—is not a crowd of far-sighted geniuses. The crowd contains a lot of clever people . . . but "clever" does not mean "wise" or "sensible," for any one of us, or for a mob of any size. On those very rare occasions when a market spiral appears to have forecasted some calamity, what really happened was that the "facts on the ground" concerning the real-world calamity kept unfolding, and kept scaring the market more thoroughly along the way.

So good investors always face the question: "Is there something really bad going on out there, whose torturous unfolding over the coming months will gradually turn the market's wallow into a death spiral?"

Let's tackle that question with extreme brevity, but in two parts: first the U.S.; then the rest of the world. Courtesy of economist Scott Grannis, below, we see one solitary indicator (among the hundreds needed to understand the whole picture.) Most jobs are created by "small business." When we glance at the chart below, we see a picture which is a mirror of most of those hundreds of indicators: fairly spectacular sustained improvement since the Calamity of 2008 – 2009. Like the other hundreds, the "small business hiring plans index" has forged ahead with ebbs and flows for 10 years, withstanding a truly amazing number of "end of the world" moments and market-wallowing moods. That solid picture of growth and strengthening confidence is so much like most of the rest of the crowd of economic indicators that we can let it stand alone, this afternoon, as all we need to know about the health and strength of the U.S. economy.

Cummins' CEO, Tom Linebarger, (about whom Theresa will write tomorrow) had this to say just two weeks ago:

> *Our view is the earnings of the company are incredibly strong. Our incremental margins are good. And we don't think we're at the peak. We think we've got quite a bit more room to run. And, by the way, in each cycle, down cycle, we do better and strengthen again each up cycle. So we do believe, in fact, that our stock is a good investment now. So, it's all three of those things and thanks for giving me a chance to talk about that.*
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> *And I think in the U.S, I do, I'm very worried about the inflationary effects, but the economic numbers now are good enough that people seem to be driving right through it. So I guess mostly what I'm worried about now is when and if things turn down, how bad is that and are we going to have inflation and economic downturn at the same time because of, because the inflationary effect. So, again I'm worried about that. But right now it is just not visible anywhere. People are busy. They're buying stuff there. Fleets are, as Rich said, fleets are so busy and making so much money, they're just busy buying trucks and trying to put more trucks to work and find drivers. So far so good is what I'm seeing.*

"So far so good" is actually about all we can expect any of those hundreds of economic indicators to tell us. Things change; tomorrow can be worse than today. But regardless of how gloomy this market gets about Turkey, the U.S. "facts on the ground" confronting the market are remarkably solid, and remarkably widespread across the business and consumer worlds.

Next comes the rest of the world: is something really bad going on out there?

Well, it's pretty bad in Turkey, whose dictator has piled burdens on the economy for years, and printed money to keep Turkish voters happy until the point when he needn't care about their opinions anymore. He's been approaching that point lately. But 15% - 20% inflation and interest rates are a problem he will have to care about, unless he chooses to follow the Venezuelan blueprint for economic

destruction. If he does, Turkey's position as the world's 17th-largest economy means Europe will feel pain, and other "developing" countries scattered around the world will face the possibility of a "run" by the markets from their currencies, bonds and stocks. (That's what the market is wallowing about at the moment, pretty much.) But there is a big difference between Turkey's position and the positions of many other "developing" countries. India, for example, has seen an experimental "run" on its currency lately, on the grounds that its economy has trade deficits and other weaknesses. But it's very far from Turkey: beginning with the Indian central bank's $400 billion of foreign exchange reserves—which is strong even for a nation of India's size.

In Outlook's opinion, what's really going on "out there" in the rest of the world is a picture showing some pockets of weakness and risk, but mostly showing a broad range of economic and financial strength, from "poor" in the weak pockets to "rather good" in many more corners of the world. What's really going on in the markets, therefore, is normal behavior. It's wallowing in another end-of-the-world moment right now. But most of the world, led by the U.S. economy, is not perched on some cliff-edge waiting to be shoved off by a far-sighted market, into a death spiral carrying our sacred fortunes along for the one-way ride. It is still trudging ahead along the same rocky upward path it has followed since 2009. Our companies are exceptionally strong, and mostly valued emphatically cheaply by the market. When that's the state of things, we must hold and buy more. That would pay off even if this turned out to be one of those truly rare far-sighted moments, for the market. We doubt it very much, so we'll hang on and keep buying.

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