THE RAE LIPSKIE PARTNERSHIP™ PRIVATE WEALTH MANAGEMENT

Random Gleanings

The state of Vermont has taken the **remote-worker trend** to another level. In an attempt to build up its declining tax base, the government will be offering a $10,000 tax credit in 2019 to 100 high-income professionals who apply to move to Vermont while maintaining their jobs remotely in another state. This approach is also known as beggar-thy-neighbour.

Is your **TV viewing** stuck in the 1080p resolution era? If you have missed the quadruple jump in resolution to 4k, don't despair as another quadruple leap to 8k will be in the stores soon. Ironically, like 4k, this resolution revolution won't really do much for your viewing pleasure as there are few input sources at that level and apparently it is difficult to see much difference anyway. Isn't technology wonderful?

In this time when everything seems to be speeding up, the **game of baseball** is stuck in the slow lane. Baseball purists might still love the three-hour grind, but the younger set is tuning out and tinkering with intentional walks and mound visits hasn't helped much. Enter a pair of academics who have devised a Catch-Up Rule which allows the leading team only two outs instead of three. Intensive historical research suggests the average winning margin would drop by a run and the playing time by 24 minutes. Play ball! … faster.

In a similar vein, the American Economics Association has declared that published **economic papers** are too long, having tripled in length on average over the past four decades. We concur, as it exhibits the lazy writing that creeps into reports and reminds us of this multi-attributed greeting: "If I had more time I would have written a shorter letter."

General Motors sells a lot of cars, nearly 10 million of them last year, which was up about 25% from ten years ago. The composition of sales has changed markedly, and remarkably, however, with sales in China having quadrupled to overtake the U.S. as GM's number one market. Just another example of the dramatic impact China has had on global markets.

That impact has been particularly noticeable in the **travel market** which has seen international arrivals double since 2000 to 1.3 billion in 2017. There are several reasons for this increase, including economic growth and affordable pricing, but the U.N. claims that China has accounted for 80% of the increase in dollar value of global tourism over the past ten years. Amazing.

Do you bake with **vanilla**? If so you are likely well aware that the price of the popular spice has quintupled in recent months. This has resulted from a 'perfect storm' of lowered supply due to a cyclone in Madagascar, supplier of 80% of world demand, that cut production by one-third at the same time as commercial users have been using much more pure vanilla in their confections. It will take some time for supply to recover so you can count on expensive chocolate chip cookies for a while yet.

The Wall Street Journal reported recently that the first known **stock quotation tables** were published in 1786 in the Massachusetts Centinel. That was a long time ago, 232 years to be exact, and it got us to thinking about the magic of compound interest and the implications of long-term investing. If you could time travel and had $10 to invest back then, or you had smart ancestors, that $10 investment would be worth today:

- $65 million at a 7% return
- $4.8 billion at 9%
- **$40 billion** at the long-term average 10%

Two morals to the story: 1. Small percentage points matter when it comes to long-term investing and 2. For your great, great, great etc. grandchildren, go out and put $10 in the market today.

THE LEARNING CORNER

What is a stock buyback?

Stock buybacks, or share repurchase programs, are a second avenue open to corporations, beyond dividend payments, to return cash to shareholders. It is a topical issue currently since Goldman Sachs estimates that record earnings and cash flows will lead to U.S. buybacks amounting to a record $1 trillion (yes, trillion) this year and Apple alone has announced a $100 billion program. The mechanics normally include a company announcement indicating the intention to buy shares in the public market, the actual purchase of those shares over time and the elimination of the purchased shares from the company's books. It is up to individual shareholders to decide if they want to sell their shares during this period (the company is just another buyer in the market), making this form of cash distribution different from dividends which go to all shareholders.

There are benefits as well for those who retain their shares, including price support for the stock from the corporate buying and, with fewer shares outstanding, higher per-share earnings which, in turn, support higher dividends and stock prices. Further, there can be some comfort in the perception that the company sees attractive value in the stock you hold. Still, these programs are not without controversy as critics contend that corporations should be investing their cash in plant, equipment and labour instead to sustain a viable future. We will give the last word to Warren Buffett on the topic: "When stocks can be bought below business value, it is probably the best use of cash."

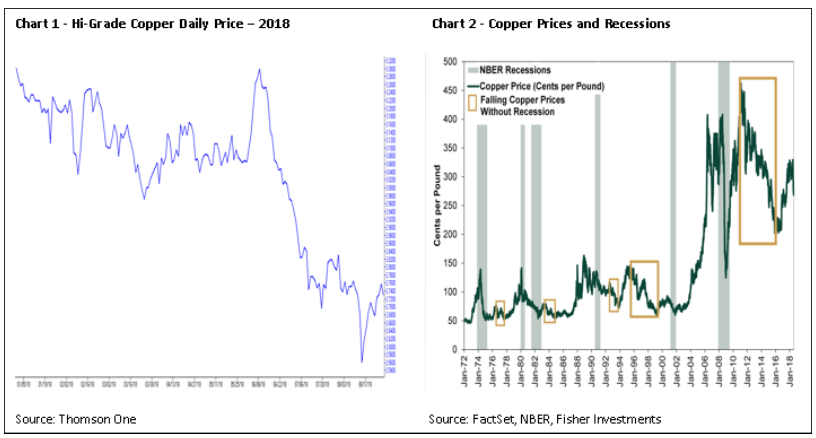
CHARTING OUR TIMES

Dr. Copper – The Commodity with a Ph.D in Economics?

Longtime market watchers will recognize the title of this section as something that investors historically paid heed to. Investopedia describes it as follows:

"*The term Doctor Copper is market lingo for the base metal that is reputed to have a Ph.D. in economics because of its ability to predict turning points in the global economy. Because of copper's widespread applications in most sectors of the economy — from homes and factories to electronics and power generation and transmission — demand for copper is often viewed as a reliable leading indicator of economic health.*

The downturn in the price of copper recently (-17% in 2018 YTD) has led to speculation that this brainy commodity may be predicting trouble for the markets (Chart 1).



However, the good Doctor's track record leaves much to be desired. Chart 2 highlights periods of declining copper prices and associates those with recessions. While copper has certainly declined sharply <u>during</u> recessions, it hasn't done too well at <u>predicating</u> recessions. Take the period from Feb 2011 to Jan 2016 when copper dropped nearly 60% - those who heeded the Doctor's warnings during this time would have missed out on a big chunk of this bull market.

To take it one step further and relate it to the stock market, the correlation between copper and the stock market is essentially zero, meaning that movements in one tell you virtually nothing about shifts in the other. In fact the long term correlation is actually slightly negative which indicates that falling copper prices have more often been associated with <u>rising</u> stock markets than <u>declining</u> ones (as is the case in 2018).

Today's leaky copper price would appear to be a valid reflection of a strong U.S. dollar and a softening of growth in China (which consumes 50% of global copper production), along with the reality that it takes very little copper to grow today's First World economies as they increasingly are driven by services rather than manufacturing. As a stock market predictor though – not so much.

IN THE OFFICE

Earlier this summer we welcomed Robin Stanton to our portfolio management team. A graduate of the University of Toronto and a CFA Charterholder, Robin brings extensive experience working with institutional and individual investors as VP at CBRE Caledon Management, and VP of Investments at AGF Investments.

Robin is an active volunteer in our local community, and serves as a member of the Investment/Pension Committee for the Kitchener-Waterloo Community Foundation, Wilfrid Laurier University, and Grand River Hospital.

Raised in the Kawarthas (Fenelon Falls), he is an occasional skier and golfer and avid cyclist, who is participating in the 6th Annual GTA Gran Fondo (125 km!) this Sunday, September 9th. He is reconciled to being a better cyclist than golfer.

Robin is the proud father of daughter Lauren, who recently participated in her first Equestrian Show at Old Orchard Farm. Robin, his wife Cindy, and daughter are residents of Kitchener.

We are:

Ken Rae, CFA

Brian Lipskie, CFA

Ted Brough, CFA

Taylor Echlin, F.C.S.I.

Jim Harper, FCPA, FCA

David Martin, CIM

Andréa Miljkovic, CFA

David Paleczny

Derek Rae, CIM

Rick Vandermey, CFA

Dave Brune, CFA

Alex Stoody, CIM

Robin Stanton, CFA

Thomas Pick, M.B.A.

The RaeLipskie Partnership provides discretionary "fee-only" portfolio management for high net worth individuals, endowments and charities.

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THE BIG PICTURE

As the second quarter of earnings season comes to a close, we thought we'd dive into the numbers to determine whether we are justified in maintaining our bullish stance on stocks or whether the many detractors of this "most hated" bull market were right to exercise caution.

We recognize that it can be difficult to maintain a positive outlook when many in the news media focus only on the negatives that exist globally (take your pick: trade uncertainty, flattening yield curve, rising debt burdens, and many more). However, there will always be a reason NOT to invest. We live in an imperfect world and our job as investment managers is to recognize this and weigh our clients' needs with the risks that are out there. And while pundits can talk about the risks and the negatives, we prefer to look at the evidence which shows up each quarter in the form of corporate earnings.

As it happens, things aren't so bad. Second quarter earnings for the S&P500 rose 24.6% year over year. And for those worried that market growth is being driven by only a handful of stocks (Amazon, Google, Apple, etc.), the reality is that all 11 sectors reported growth, demonstrating that Corporate America's earnings power is broad-based. While many detractors cited Trump's tax cuts as the reason for what they believe to be a temporary earnings boost, revenues (which are unaffected by taxes) were also strong. Revenues rose 9.9% in the second quarter which was the most since the third quarter of 2011. Again, the revenue growth was also not sector specific as all sectors' revenues save the Utilities sector grew in the second quarter. Canadian stocks also saw consistent revenue and earnings growth but given that half of our market is either Energy or Financials, we think the U.S. is a better proxy for gauging growth globally.

We believe there is further room for the bull market to run as sentiment is nowhere near euphoric and there exists plenty of opportunity for uncertainty to drop which should allow stocks to climb the proverbial wall of worry. We see this as corporate earnings continue to beat expectations, as the yield curve continues to be positive which incentivizes bank lending, and as trade worries dissipate. Indeed as this goes to press, details are beginning to emerge on the United States' trade deal with Mexico and our Foreign affairs minister is back at the table trying to get a deal done for Canada. Markets abhor uncertainty but as uncertainty is removed, the market is likely to chug higher.

QUOTE of the DAY

"A consensus means that everyone agrees to say collectively what no one believes individually."

Abba Eban