CIBC PRIVATE WEALTH

TOP GUN

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By Brahm Satov

For most who have watched Top Gun, they have likely wanted to be the best of the best. For me, it was not about being an elite fighter pilot, after all, I am afraid of heights. But to be the best of the best in terms of portfolio management. After all, my dad did not have a good experience when it came to his financial advisor so when he passed in 1999, I decided that one day, I would try to become a great advisor. I was recently asked, if I was given a huge sum of money what would I do, and my reply was exactly what I am doing. For those country music fans, much like Luke Combs, "Doin This". This profession to me, is very important, I may not be flying at Mach speed, but I am striving to protect and build people's financial future and to me, there is honour in that.

Many have wondered if the downturn in the stock markets is over, and for anyone that has a crystal ball, please let me know. I did mention in one of my newsletters not long ago that for those who successfully moved largely to the sidelines for this downturn, well done. However, they were only halfway there. As we know investing in great business over time, tends to produce remarkable results. But when do we get back in? It is at times like this, where you may want to take heed of one of Warren Buffett's mantras, "the stock market is a device for transferring money from the impatient to the patient".

Look for many investors they have seen their portfolios fall by 20% or more and when the economy does improve and stock markets recover, it may take them years to get back from those losses, but for those with minimal losses, recovery should be quick. Moreover, many have discussed the advantages of being in the markets when they are moving higher, however I think it is more important to be out of the markets when they are plunging lower. For those who enjoy math, they may smile as they know the rationale for this belief.

Some have called me recently to ask if I think it is time to move back into the markets. Let me be clear, although I do still expect many reflexive rallies or bear market rallies, and often they are steep, I don't think this correction is over just yet. For those with courage, timing and perhaps luck, they can try to ride those uplifts in the markets, however I believe Sir Isaac Newton's first law applies in times like this. "An object in motion tends to stay in motion until an external force acts upon it". I believe we have started a negative feedback loop in terms of corporate earnings. This loop works like this and is the opposite of a healthy economy, companies have lower sales as consumer spending slows, companies then let people go, consumer spending or sales slow further, more people are let go, etc. To end this negative feedback loop, I believe we need a significant external force, likely central bank intervention, but in my opinion, higher rates will certainly not do the trick. (As higher rates further constrain the economy.) In my opinion, nor will a pause in raising interest rates.

Given that many call to ask, I should also address our housing market, and after all housing is a great leading economic indicator. With sales volume down over 40%, many in this sector have already suffered severe setbacks. How would you feel if your income was down 40% or more? So, for those who think it unlikely that the economy has weakened, I suggest you speak to someone in that sector. I continue to believe a recession is highly likely. With higher interest rates and lower sales volume, home prices could be expected to fall and like the stock markets, they to will need a force to turn them around, like lower interest rates, likely coupled with QE.

I think inflation will come and go in line with ultra-low rates and QE. As liquidity comes out of the system, I believe prices will regulate. In terms of the rising rate environment, I do believe that we are either at an inflection point or close to it. If this is the case, that rate increases seize, the next move will be expected to be lower and to me, this will mark the beginning of the next phase. That is where interest sensitive investments should outperform, like bonds. I believe, this phase, of lower rates as economic weakness drives rates lower and fixed income outperform could last for some time, until central banks actively and successfully reinvigorate the economy.

Since 1950, the Fed has been through 14 hiking cycles, 11 resulted in recession. So, the Fed has done a much better than average job of creating recessions when they are raising rates, like they are doing now. Just about 80% chance of recession when the Fed is raising rates. The 2-year bond is now yielding more than the 10-year bond, in other words the yield curve is "inverted". Another harbinger of a recession. Stock markets perform poorly in recessions. I watched Top Gun 36 years ago, I was 19 years old, and we entered a recession shortly thereafter in January of 1987. The stock market and housing market plummeted in that downturn. It was certainly a difficult time for many families, including ours. I like to think that people learn from history. Given the likeliness of a recession and difficult markets, if you are not holding more cash than usual, than perhaps in one of these reflexive rallies, you should consider raising some. Watching Top Gun 2, brought me back to those days long ago, and how far we have come, I am humbled and thankful to be here and doin' this.

Sincerely,

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