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Super Mario

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I have been cautious on the markets for quite some time. However, I think I should be clear, I do believe that so long as central banks around the globe keep injecting more stimuli, this should fuel economic expansion, and with this growth, the equity markets should fare just fine. Massive amounts of stimuli thus far has perhaps only modestly increased economic growth and most would agree that the laws of diminishing marginal affect are at play with each additional injection. Oh and by the way, Mario Draghi, also known as Super Mario, the President of the European Central Bank (ECB) recently increased the stimulus program in Europe, and lo and behold, the stock markets rallied.

Although each injection of stimuli has had a marginal and perhaps fleeting increase to economic growth, the stock markets have fared much better, rallying on news of each additional stimulus. Having said that, I believe that the North American stock markets are overvalued and that low rates and stimulus have likely been the catalyst. For the most part, central banks thus far have been relying on monetary stimulus now that “zирp” has been replaced with “nirp”, (or zero interest rate polices have been replaced with negative interest rate policies), in many regions, and with little success, support is growing for fiscal stimuli. In fact, Canada’s Trudeau has already begun to steer in this direction.

The difference between fiscal and monetary stimulus is really from where it is derived and its capabilities. Central banks engage in monetary policy, raising and lowering interest rates (and although historically very rare), injecting stimulus by purchasing bonds, when they deem necessary. Fiscal policy is engaged through the government, raising or lowering taxes and spending on things such as bridges, roads and programs. In my opinion, fiscal stimulus should have a more direct effect on the economy, but both fiscal and monetary stimulus, are tools utilized to help stoke economic growth.

On Thursday March 10, 2016, Mario Draghi announced that the ECB would increase the monthly purchases of bonds, including corporate bonds from €60 billion to €80 billion. This form of stimulus, often referred to as quantitative easing, is intended to inject liquid cash into the system through the purchase of bonds and simultaneously lower the cost of capital due to the increased demand for bonds.

It appears that we continue to tread in this period of perilously low global economic growth, dare I say deflation, coupled with periodic injections of stimulus and corresponding, but un-lasting, better growth as it manifests itself through the system. Look around, this has not exactly been a healthy economy, with rates now negative in parts of the world and quantitative easing the norm in many regions. However, opportunities should continue to avail themselves. Now given this economic backdrop coupled with expensive markets, I do believe that investors should continue to employ caution, but for those who are able to find select businesses with solid fundamentals at good prices, I think will be rewarded.

Thank you kindly for reading my thoughts and I look forward to your feedback.

Sincerely,
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