Charles Merrington
Executive Financial Services (Pty) Ltd

Authorised Financial Services
Provider Licence Number 12833

CME0001AA

CMEFS WEEKLY INVESTMENT NEWS

12 JUNE 2020

Hello and welcome to this week's edition of Investment News.

Before we go into this week's discussion, let's see how the CMEFS Flexible fund has done for the year thus far as compared to the All Share Index (ALSI)

Fund	Last week Thursday	This week Thursday
ALSI	-6.02%	-5.98%
CMEFS Flexible Fund	-0.56%	-0.61%

We are now well into doing our switch out of the Coronation Balanced Defensive Fund (as this is where all the damage is being done) into either the Coronation Jibar+ Fund, or where this is not available on the relevant platform, then into a Money Market Fund.

Again, we have no idea how this Covid-19 thing is going to play out in the end from an economic point of view, which accounts in large part for this switch away from any form of risk.

And now to this week's news which to some extent I think confirms the unpredictability of the environment out there.

For those of you who watch the news out of the United States regularly, you will have seen President Trump going on about the sudden and unexpected turn-around in the US unemployment rate.

This was because, on Friday, June 5, the Bureau of Labor Statistics reported that U.S. nonfarm payrolls jumped by 2.5 million in May, following a (***downwardly revised***) loss of ***19.7 million*** jobs in April. (Go back and don't miss the bits in bold italics)

Given that America is still the largest single global economy, the world immediately went berserk and threw a stock market recovery party, causing a massive rally in stock prices globally.

This was surely an indicator that "the worst was over" and things were now finally "getting back to normal" with America "as usual" leading the way.

Well, um…sorry to spoil the party…and hope you have recovered from your hangover, but it seems that all is not as it seems.

In the Household Survey, which is used to calculate the unemployment rate, the Labor Department admitted that survey takers ***mistakenly counted 4.9 million furloughed workers as employed***, but did not correct the data, ostensibly "to avoid the appearance of political manipulation." Accordingly, the reported unemployment rate was 13.3% for May. ***The corrected data would show a 16.1% unemployment rate.***

So basically a whoopsy here. But a big one.

But wait. There's more.

Hussman Funds further reports that even that figure does not reflect the ***4.7 million workers who have abruptly dropped out of the civilian labor force since March***, and are not included because they are not presently looking for work.

And more yet…

This from Coronation Fund managers.

In so far as the US economy is concerned, there is a massive bill coming that will have to be paid somehow.

The US already spent roughly ***a year's tax revenue on Covid-19 relief*** and their politicians are debating adding about as much again in a further round of fiscal support.

The Federal Reserve Board's balance sheet is expected to expand from ***US$4 trillion at the start of 2020, to around US$12 trillion by the end of 2021.***

For context: it grew, through three rounds of quantitative easing, from less than US$1 trillion before the Global Financial Crisis in 2008 to around US$4 trillion in 2014.

The payment of this bill will be spread across society, partly in the form of an increase in direct taxes, but also through more subtle forms of financial repression.

The term 'financial repression' was first introduced in academic literature during the early 1970s, and became popular as a description of the expansionary fiscal policies adopted in much of the developed world in the early 2010s.

A simple definition of the concept is a set of policies that result in ***savers earning negative real returns*** to reduce funding costs for lenders — both government and private.

This often coincides with weaker currencies and higher inflation.

One of the great challenges in the current investment environment is that much of the world finds itself in a similar position at exactly the same time, creating a more treacherous path for investors seeking to preserve their wealth.

We have already seen an example of financial repression locally, with SA policy interest rates moving from 6.5% in January (around 2.5% real), to 3.75% today, which is, at best, in line with expected inflation.

But not taking tax into account of course.

Which, if brought to account, only makes matters worse.

Keep in mind that it is a foregone conclusion that those of us who are going to be lucky enough to remain in employment or receive some sort of an income throughout the whole period of the pandemic ARE going to pay a LOT more in taxes.

Prepare yourself for this.

This makes cash a significantly less attractive asset class and means more conservative investors need to recalibrate their expectations for the years ahead.

I would add the words “big-time” to this statement.

Notwithstanding the above and the low yields to be expected out of cash going forward, I believe this is a time to preserve capital and not to expose oneself at all to the very real risk of a major stock market crash, possibly of the order of 50%-60% or so, which I sincerely hope ***does not*** happen.

It is for this reason that I have decided to exit equity altogether and to take cover in cash, until the way forward becomes a lot clearer than it is at the moment.

Frankly, no-one knows how all of this is going to play out.

We’ve NEVER been here before.

It’s scary.

It’s fun being part of an “historic time” in human history, isn’t it?

I hope you enjoyed the read.

Until next time then, do take good care of yourselves.

Kind regards, Nine, Charles, and all of us at CMEFS.