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Smogged In

All investing of course is about the future, but when the future is so smogged in with pollutants, it's hard to make an investment decision without instantly having second thoughts. Most of the serious pollutants in 2017 seem to be political.

As the Canadian economy slowly rebounds from the crash in oil prices, it now faces having to renegotiate NAFTA. European companies expect 2017 to be a "best ever" year for earnings. But what happens if France elects a far-right government, if Angela Merkel is not re-elected, if Britain negotiates such an attractive exit deal that other countries are encouraged to exit the EU? Or if North Korea decides to do something incredibly stupid with their atomic toys?

In the United States, the economy has reached full employment. The dollar is stable, having retreated from its highs. The President has promised business friendly initiatives including lower corporate taxes, less regulations and lots of infra-structure spending. To most analysts, the stock market is in overbought territory. Politically the country is sharply divided over President Trump himself, probably because of his bullying demeanor and off-hand insults freely awarded to all who dare disagree with him publicly. The political division is at least as sharp as it became during the Vietnam war. When a political leader himself, more than his policies, becomes the focus of division, investors should be wary. A crisis may soon follow. When Hillary Clinton was called upon during the election campaign to say something nice about Donald Trump, she replied "I respect his children."

Clearly investors have a problem. Rising interest rates make bonds unattractive. The U.S. Federal Reserve promise at least two rate hikes in 2017. The yield on five-year government of Canada bonds barely matches the rate of inflation. When the inflation rate includes food, fuel and taxes, the rate of return is negative. Hence many individuals and institutions are more in the stock market than they would normally be simply because the dividends from stocks and distributions from income trusts give a positive rate of return. Ironically, their over-commitment to the stock market helps keep it in overbought territory.

In spite of the problem, the self-serving wisdom from most of the financial industry remains: Don't try to time the market. Like most clichés passing for advice, it is only right some of the time. As of mid-February 2017, it would seem to apply only to those who have no investments or have the wherewithal to hire someone to invest for them.

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Healthy financial markets, ones that will attract new financial commitments, are largely based on a widely-accepted view of a stable future. Or, there could be a crisis that causes investors to panic and drive prices to oversold territory. Panics cause financial misery, but they also create opportunity. As a colleague of mine used to preach to clients during uncertain markets, “Your money won’t rot in the bank.” Unfortunately, not a true statement when inflation was running at more than 10%.

More than ever, investors need to guard and grow their capital because they will likely need more for retirement than they anticipated. People are living longer. Healthcare costs are rising. The cost of assisted care for the elderly is skyrocketing. Most economists expect low interest rates to persist for a few more years, which means cash flow from income investments will grow slowly, if at all. Because they were never properly funded, government assistance programs for retirees are running out of money. There is a shortage of people in the work force to support the government care for the elderly. Personal tax rates will have to rise to take care of the shortfall. Those who choose early retirement may be making a serious mistake.

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