WEEKEND READING
Shedding the light on what's happening - our world - our finances - our times

THE SKY WAS FALLING?

We took a break last week from publishing the Weekend Reading. Catching up this week.

Of course, the week we're not commenting, markets – according to media - **'*MELTED DOWN*'**. It all kicked off on Monday last week with the S&P500 dropping to an intra-day -4.25% low from the Friday Aug 2 close. Media screamed the sky was falling, and trotted out the usual dancing market bears proclaiming, 'A recession is upon us this fall'. It was the beginning of the end. We didn't think this was so. We made no sells into that decline.

Then news flowed out that the S&P -4% decline had more to do with the equivalent of a huge margin call on the Yen Carry Trade. Clever types running hedge funds (for a fat fee) borrowed in Yen, paying 0% on the borrowed funds, converted the Yen loan proceeds to US dollars (sell Yen/Buy USD) using the resulting US cash to then purchase US equities. This package is typically leveraged. It was all so much fun…until it wasn't. The Bank of Japan – horror of horrors – raising short-term interest rates from 0% to 0.25%. The increased Yen rate caused the Yen to rise against the US dollar. The rising Yen made the Yen loan more expensive. The resulting significant losses were amplified by leverage. Margin calls suck!

As the carry trade players all rushed to unwind at the same time, stock prices for their favored MAG-7 NASDAQ darlings flopped 10%. The yen gains added another 10% loss. Given the concentration of these names within the S&P500, that index sagged to a low of -4.25% on the day.

Allan Brooks Energy Musings for August 9 provides more detail.

The sharp rise in the yen value turned profitable carry trades into money losers.

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Practically all of those doing this over crowded trade from 4th July is looking at massive 20% loss in just a month's time.

I just quickly typed it. Let me know if i made some mistakes here. The actual carry trade is a bit more complex and will involve 2 more steps.

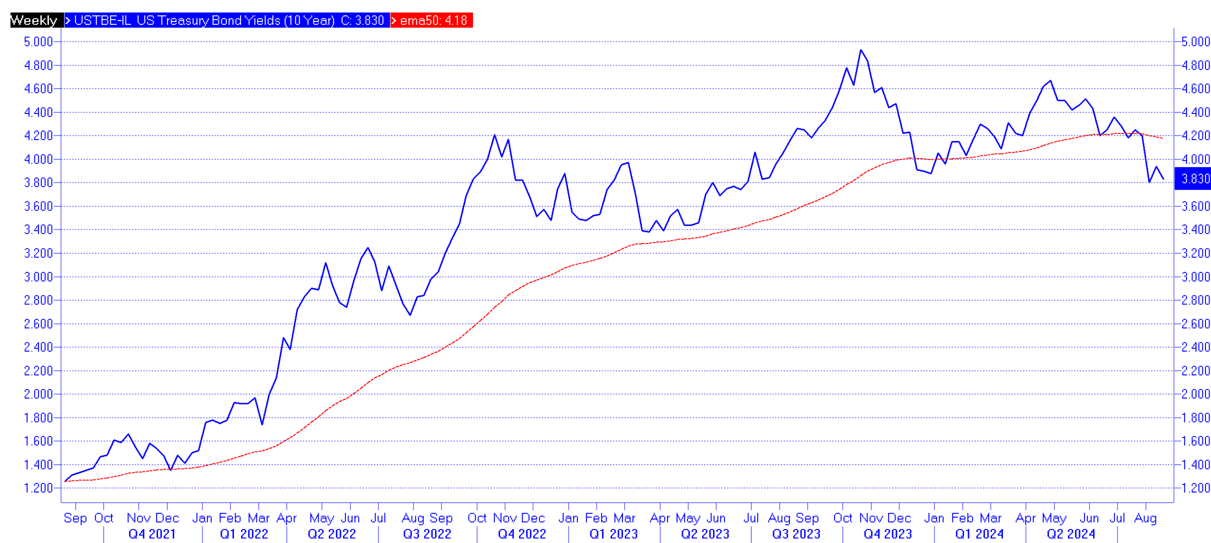
Dollar Yen @ 4th July	160
Capital Borrowed in Yen @4th July	16000000
Interest Rate (%)	0.00
Equivalent Amount in $	100000
Invested in Nasqad Index @ 10th July	18650
Nasqad @ 5th Aug	16776
Dip in Nasdaq Valuation (%)	10%
Resultant $ Amount	90000
Dollar Yen @ 5th Aug	142
Equivalent Amount in Yen	12780000
Net Yen Loss	3220000
% Of Loss (%)	20.125

As we hadn't joined the previous Magnificent 7 party, we saw minimal effect on our holdings. Keep 'Don't do stupid' on a sticky note near your monitor.

The S&P's flop quickly reversed last week as the grownups opened their wallets. Thursday Aug 15 saw the S&P up 7.4% from the Monday Aug 5 intraday lows. Not selling was the right thing to do.

One reason we've continued to own stocks is our call on declining interest rates. So far so good.

US Treasury Bond 10-year yields – weekly ranges – 2 years



Source: Refinitiv, NBF, Hilberry

August 16, 2024

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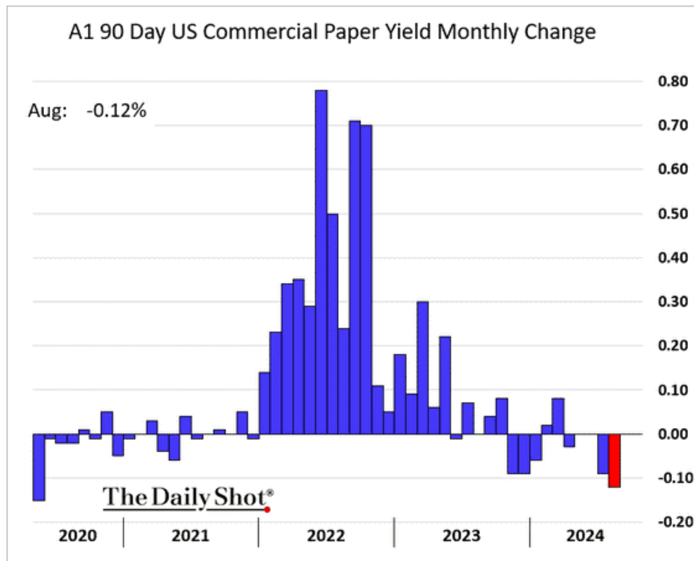
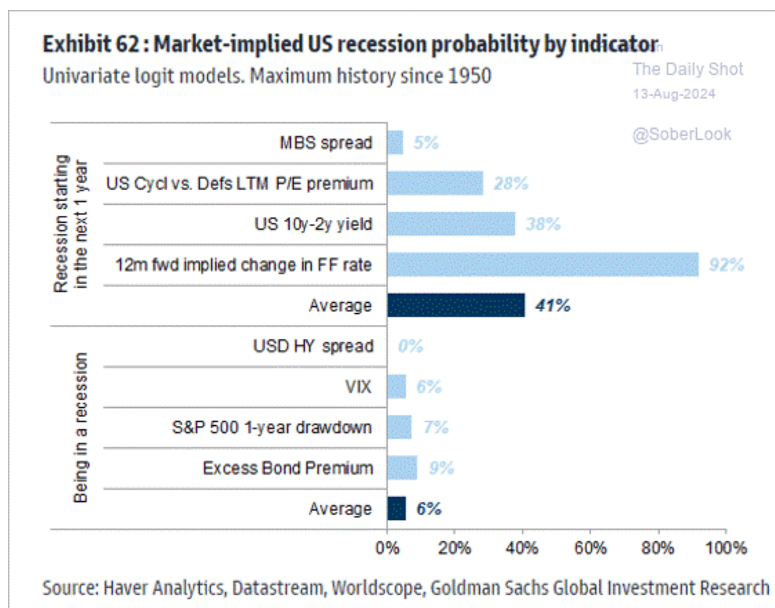
WEALTH MANAGEMENT

After peaking around 4.9% in Oct/2023 US 10-year rates have been pricing in falling inflation. We believed this would lead to lower short-term rates. It's taken longer than we thought. Lower rates are finally coming.



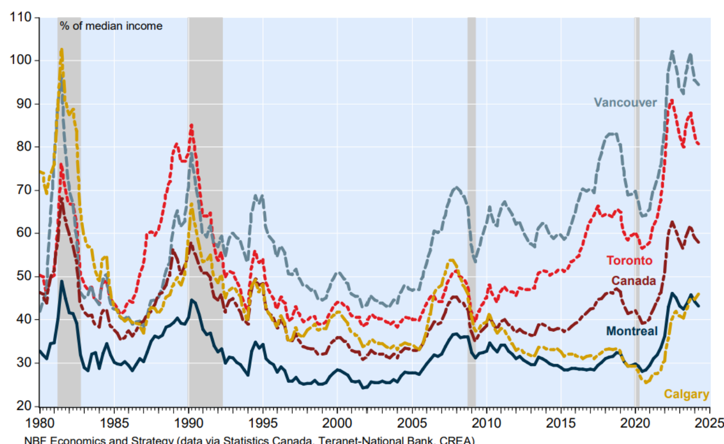
Recession signals are not supporting a major wipe out in the US Economy. There are some indicators leading towards slowing. At this writing, not enough to change our view.



We continue to believe the inflation pulse from COVID-19 policy largess is done, leading to a decline in short-term rates…for now. We've maintained this would not be bad for stocks. We think the next major move in short-term rates is down before the US Election. Regards Trump vs Harris, while it's been fun to watch, we don't see the Nov/2024 outcome as binary for stocks. When Trump was in, stocks did okay. When Biden/Harris were in stocks did okay too. Our guess is Mr. Trump will be defeated - again. Polls say Mdm Harris might be the first female US President. We're not convinced that will matter…for the stock market. It shouldn't!! Meanwhile, back at the ranch...lower rates are helping Canadian housing.

Q2/2024 National Bank Housing Affordability Monitor: Aug 15, 2024

"Q2 2024 marked a second, albeit smaller, improvement in affordability. The amelioration was relatively widespread with 8 of the ten markets covered experiencing a decline in mortgage payment as a percentage of income (MPPI). The most significant improvement occurred in Hamilton, where a home price decline compounded on the broader trend of lower interest rates and rising incomes. On the flip side, Edmonton and Calgary saw rising home prices largely offset any relief. Overall, the composite improved with slightly higher prices not enough to offset the decline in mortgage interest rates and higher incomes. Still, the housing market remains unaffordable with the latest progress bringing the MPPI (Monthly Mortgage Payment to Income-SH) *to 57.9%. Looking ahead, falling mortgage interest rates will likely be the main driver for improvements in affordability. So far, the decline in mortgage interest rates was precipitated by both expectations of rate cuts and the materialization of easing by the Bank of Canada. Given the deterioration in the growth outlook and the weakening in inflation and the labour market, we expect further central bank easing of 150bps over the next 12 months. Although the policy rate and mortgage interest rates do not always follow in lockstep, this development would provide a significant alleviation of the financing burden. At current income and home price levels, it would bring affordability halfway back to pre-pandemic levels. There is the risk, however, that lower interest rates could lift home prices, especially considering the current population boom. That said, between the payment shock from upcoming renewals and the rising unemployment rate, we do not expect much vigour in home prices for the next 12 months."*



Full Q2-2024 Housing Monitor Report

While housing affordability is a problem, it is also a sign of strength. I'm from Detroit. I'm here to tell you be careful in wishing for 'more affordable' (IE cheaper) housing.

Canada's problem isn't a lack of ability to build or a lack of land to build on. Regulations are THE elephant in the room no politician wants to address. One suspects there are many single family house owners in Burnaby who are quite content with house prices thank you very much. They realize the lack of development in their area protects their lifestyle, keeps an open parking spot on the street in front of their house, keeps traffic down all while driving up the value of their house. The high barrier-to-entry maintains a cozy upper income neighborhood. They resist densification tooth and nail. As most building is controlled at the municipal level, Federal and Provincial politicians can huff and puff but there won't be blowing any single family dwellings down to build sky scrapers in Kerrisdale anytime soon.

If we can't build, how about increasing disposable incomes? You know...maybe governments concentrate on helping their citizens improve their purchasing power. Oh right. That regulation thing again. Increased purchasing power only happens through increased productivity. Increased productivity results from decreased costs. That implies cutting taxes, bureaucracy and red tape. That's no fun for government budgets. Nope.

Lately, if one makes 'too much money' there's the risk of rising into the category of *'the rich who aren't paying their fair share'*. Success is punished by higher taxation. Ballooning government deficits say this approach isn't sustainable.

Rant Closed

Have a Great Weekend

Steve & Anna Hilberry

August 16, 2024

FOR THE RECORD August 15, 2024 close

DOW INDUSTRIALS:	40,563
S&P 500:	5,543
S&P/TSX COMP:	23,032
WTI:	$77.90
LOONIE IN $USD:	$0.7280 $US

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