Elgin
the investor's choice

Market Commentary 6th February 2018

Since our monthly commentary only 4 days ago, markets have taken a decided turn for the worst. As we write, most major markets have fallen 7-8% from their highs. They might fall even further in the short term. In that commentary we argued that there is more good than bad in assessing the markets' direction. We believe that this is still the case.

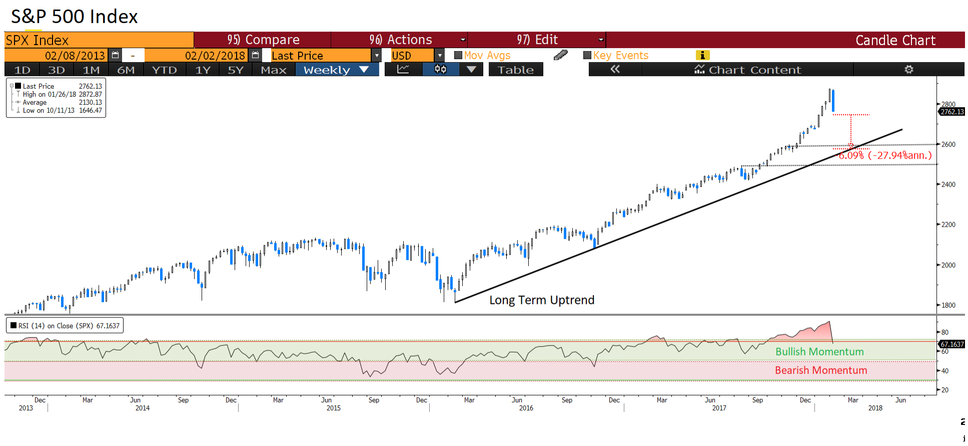
We quote from the commentary: *"…in a bizarre way it (a 5-10% correction) would be welcome as it could shake off some of the market excesses and build a base for continuing strong market returns in the medium term…"*

Why do we think this is not the beginning of a new bear market in equities?

Despite almost everyone decrying record high US valuations in recent months, it is important to note that recessions, and not valuations, trigger bear markets. We do not see any signs of a pending recession, especially in an environment with such strong corporate earnings growth and low unemployment.

Additionally, there are three indicators that we follow that do not point to anything more than a correction.

Firstly, to define the word "correction", it is a drop that does not result in a change in the primary trend that we study. As you can see from the chart below the primary long-term trend is still intact. The S&P500 Index can fall 6-7% further and still be in an uptrend. Furthermore, our momentum oscillator (RSI), which shows the strength of the trend, is still in Bullish territory. Having said that, what we are experiencing now is just a correction back to the primary trend, which is healthy in any trend build-up.



The other two reasons are the behaviour of gold and high-yield bonds. Gold is considered a safe haven in times of turmoil and investors normally rush to buy it when all else is selling off. High yield bonds are considered “the canary in the coal mine” for equities, and a large drop in their value often serves as an early warning signal that markets have much further to fall. Since the US market peak on January 26th, equities have fallen almost 8%, while high-yield bonds dropped less than 2% and gold actually fell rather than rise. See the graph below. SPY (-7.90%) is the S&P 500 ETF and HYG (-1.89%) is the US high-yield ETF. Gold fell 0.74%.

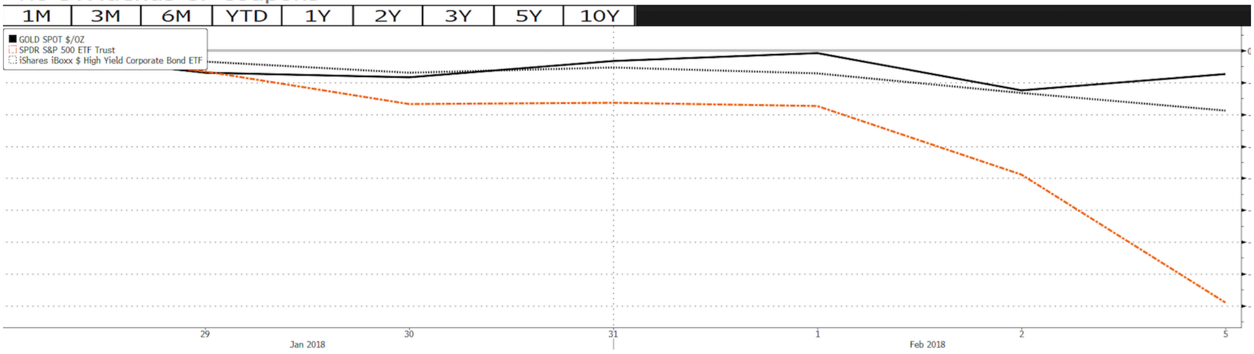
GOLDS Comdty Comparative Returns

Range 01/26/2018 - 02/05/2018 Period Daily No. of Period 10 Day(s

	Security	Currency	Price Change	Total Return	Difference	Annual E
1)	GOLDS Comdty	USD	-.74%	-.74% *	7.16%	-23.81
2)	SPY US Equity	USD	-7.90%	-7.90%		-95.05
3)	HYG US Equity	USD	-2.30%	-1.89%	6.01%	-50.15

*No Dividends or Coupons

1M 3M 6M YTD 1Y 2Y 3Y 5Y 10Y



To conclude, it is never comfortable when markets sell off so rapidly. It is also disconcerting to see portfolios inevitably suffer as a result. We are sticking to our strategies of diversification and managing client portfolios according to their risk profiles, while populating them with what we consider to be top funds.

This too shall pass….

The Elgin Analyst Team

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