The Market in Review

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This week's articles and insights

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"Not only is my short-term memory horrible, but so is my short-term memory."

- ***(can't remember who wrote this)***

Your Index Report

	Current	Last Week	Year-to-Date
Dow Jones Ind. Avg.	24,715	- 0.47%	- 0.02% (almost exactly where the Dow began the year!)
S&P 500	2,713	- 0.54%	- 1.47% (+ 3.86% in $CDN)
TSX	16,162	+1.12%	- 0.29%

Leapfrogging

It is an interesting time to be an investor. I don't recall a period when there was as much geopolitical tension in every corner of the world. Not only do we have sabre-rattling in North Korea and the Middle East – the usual flashpoints – but the Greeks and the Turks are testing one another in the Aegean once again, and the Balkan nations are chafing at the constraints of the 1995 peace accords. In Europe, Britain's "Brexit" from the European Union is emboldening countries such as Italy to consider doing the same.

America has traditionally been the diplomatic adult-in-the-room when it comes to calming global squabbles. They may not be this time around.

We as investors are the ping pong balls caught in the middle, bouncing between terror and complacency. The market has held up much better than anyone could have expected.

Meanwhile, there are some fascinating trends happening today that are worth mentioning.

The concept of "leapfrog technologies" came to public notice when the cell-phone arrived on the scene. Third world nations that had not built the infrastructure for traditional landline telephones adopted mobile phones quickly and 'leapfrogged' the poles-and-copper-wire technology widespread in more developed nations. Emerging countries have always used newer technologies to leapfrog their established competitors, and starting from zero is often an advantage.

The train, for example, was invented in Europe, but America soon passed the Continent in miles of track because there were no roads to cross or land titles to argue over. Japan had to start from scratch after World War II and used western factory technology to make small, fuel-efficient cars for its narrow roads. The country quickly became the world's leader in compact cars when oil prices spiked.

Just fifteen years ago, China was primarily an agricultural nation. Most roads were dirt or gravel and few people were connected to the outdated phone system. The country largely missed the first wave of cell-phones in the 1990s and didn't embrace mobile technology fully until the advent of the smartphone, ushered in by Apple (**NASDAQ AAPL**) in 2007. By 2016, 94% of Chinese ages 18 to 34 owned a smartphone (Pew Research).

Back to leapfrogging. A remarkable invention that western societies fully embraced in the 1970s through today was the credit card. The US alone held over 1.49 billion cards when usage peaked in 2007 – about four cards per person, on average (source: US Census Bureau). Today, Visa (**NYSE V**) is one of the most profitable companies on the planet.

Though it was fully embraced here, it was not a worldwide phenomenon. In the credit card boom years of the 1980s, when we were more concerned about *charging* our dinners, the average Chinese person was worried about just *finding* dinner. Today, few people in China have a Visa card.

What do they use instead? China has 1.4 billion people. Over 500 million of them (one-third of the population) uses Alipay, the digital payment system from Alibaba (**NASDAQ BABA**). Close behind is WeChat Pay, the phone-based payment system built upon the popular WeChat messaging service. Never heard of these? You will someday. China's mobile payment market is closing in on US $5 trillion per year (source: Forbes). These two giants are ahead of Apple Pay and Google Wallet and will be fierce competitors when they lock horns with their US counterparts.

Apple Pay does not compete with Visa and MasterCard (yet). Instead, it uses the credit card networks. It stores your cards inside the iPhone and uses them when you tap the phone on a terminal to pay. It is used by 127 million people worldwide, so it is catching up to the Chinese companies. Google Pay also uses the credit card networks and is about one-quarter Apple Pay's size.

As the decline in credit card usage continues due to debit cards and electronic payments, we are closely watching which companies end up on top. Visa was a much smaller company when its long expansion began decades ago. The "next Visa" may be Visa itself, in combination with mobile phone companies like Apple and Google (**NASDAQ GOOG**).

Markets in May

The month of May is supposed to begin the "Sell in May and go away" period for markets. Stocks traditionally do better from November through April than from May through October.

This year, however, Canada's TSX index fell -3% before dividends during the "best six months" while the S&P 500 made a paltry +2.5%. The TSX has jumped +6.31% in just the last month, thanks to rising oil prices, almost doubling the S&P 500's +3.4%.

Perhaps the calendar is backwards this year, and the worst six months will become the best. The “seasonal worst six months” period is off to a strong start.

The economy in the US continues to sizzle. One measure of activity is the Morgan Stanley Truckload Index, which measures flatbed capacity in the trucking industry. Costs are rising.

"We have not seen a rate environment like this for a long, long time, if ever, " said the CFO of Melton Truck.

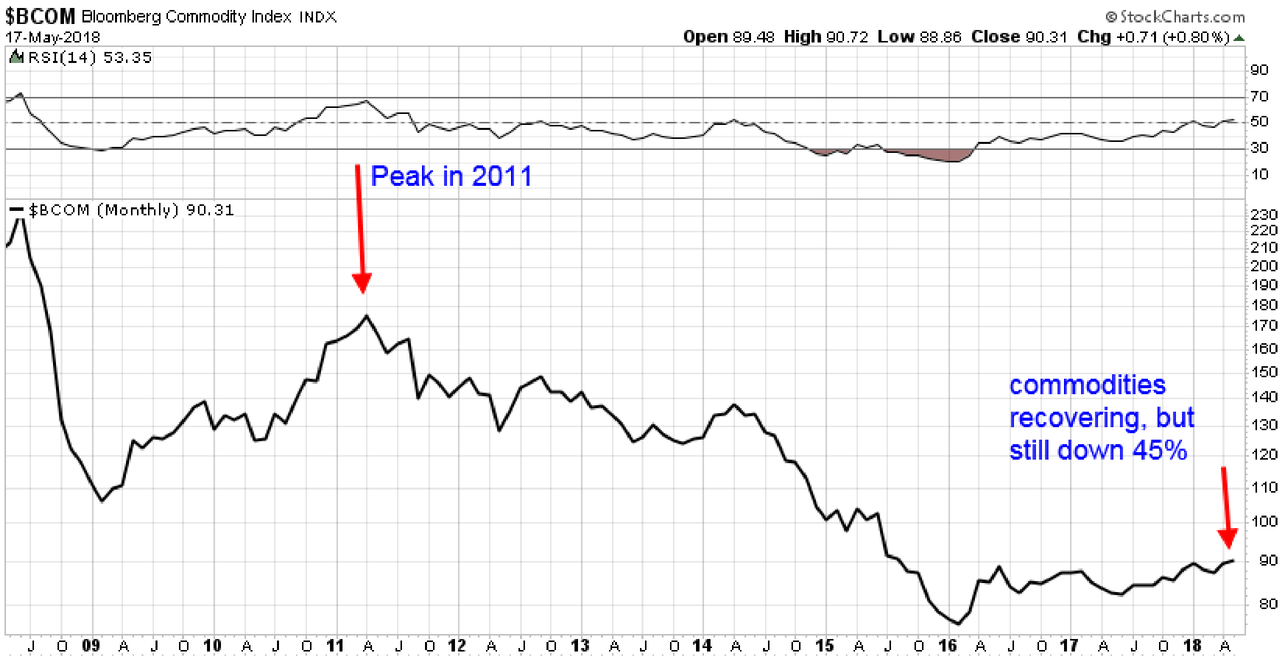
“I've never seen anything like this in more than 30 years in business. Volume was at least manageable a year ago. We were doing well and rates were good. But now it's out of control and we can't keep up,” echoed the CEO of Brenny Transportation.

(source: Almost Daily by Jim Grant)

A New Dawn for Commodities?

The rapid rise in oil prices this year has prompted us to dig more deeply into the world of commodities. Ever since the peak in 2011, investing in hard assets has been a poor trade.

Everything from wheat to corn to oil looks the same – a grinding decline since 2011:



The old saying in the oil patch is “the cure for low oil prices is low oil prices”. Low prices mean fewer profits, less production, and a decline in exploration. Low prices also lead to higher consumption which, in time, leads back to higher prices. The same feast-and-famine dynamic holds true for every commodity.

The world consumes about 35 billion barrels of oil and liquids per year (source: IEA), which means we have used up approximately 210 billion barrels since the peak six years ago. Meanwhile, we have only discovered between 100 and 110 billion barrels (mostly shale oil), meaning we have “used up” about 100 billion barrels from our global reserves. To put this in perspective, this is over half of the proven resources of Alberta’s oil sands (165 billion barrels).

Therefore, even with the miracle of the shale oil discoveries, we are using more than we are finding every single day. Oil prices may rise further in the years ahead, as a result.

There is little agreement on this, however. Many point to the rapid rise of renewable energy sources, such as wind and solar, which will replace oil consumption. These are being adopted at a rapid pace, especially in places like China and India, and displacing coal. Even with the recent rise, energy stocks are socially shunned and underowned in most portfolios.

It is important to note that a rise in commodity prices often coincides with rising global tensions, as well as the industrialization of large emerging nations. The

1970s were a time of regional wars (Vietnam, Israel, India and Pakistan, Angola, Afghanistan), which crimped supplies and may have led to regional hoarding. Whatever the reasons, the Goldman Sachs Commodity Index quadrupled from 1971 to 1980.

Countries industrializing also gobble up a great deal of cement, metals, and energy. When China exploded in the first decade of the 2000s, the Goldman index tripled in price.

Today is not the 1970s, but it seems there are tensions wherever you look around the world. And while China may be closer to the end of its industrialization, India is just beginning. Economists place India today where China was in 2001 – right at the point where its growth began to accelerate. India is building roads, power plants, airports, and growing its military to keep up with China.

A commodity we have long been fascinated with is uranium. It is the best energy source to combat climate change (zero carbon emissions), has the highest power-density of any material on Earth, and yet also produces the most toxic by-products. It has fallen from US $70 per pound in 2011 to US $20 per pound today. Why such a plunge? Global deflation, overproduction, and the Fukushima meltdown after the tsunami in Japan. Japan shut down all 50 of its nuclear reactors, leading to a global glut of uranium. Only 5 have been restarted, with 21 more in the restart approval stage. Germany shut down 9 of its 17 reactors as part of its own green power shift. Throw in the decommissioning of Russian and US nuclear warheads to create even more uranium fuel, and you have a price collapse.

If you wonder why investors hate commodities today, look no further than sad old uranium.

Under the surface, though, conditions are improving. Since 2011, when uranium prices began their sharp decline and reactors began closing, China built and started 25 reactors. Not enough to replace those closed in Japan and Germany, but they are just getting started. China has 58 more under construction and planned, and a further 179 reactors proposed (source: World Nuclear Association). This excludes any new-builds in India.

Just as with oil, when prices collapse, supplies get shut in. Both Canada and Kazakhstan (two of the largest producers) have closed mines in the last two years. As a result, global uranium markets could shift from surplus to deficit as early as next year. Few investors can name more than one uranium stock, and even fewer care to try. It is a forgotten sector with just a handful of companies barely clinging to life.

If interest rates are any guide, the recent rise suggests we are leaving the long cycle of deflation. We may not yet see inflation return for another decade, but rising commodity prices could occur well before then.

Not many investors are positioned for such an event.

Thank you for your referrals this month! They are always handled with great care and discretion.

Where Memory Resides

Most of us will experience some form of memory decline as we age. Names and words that flowed easily in our thirties don't come to mind quite as readily in our sixties. It is a normal part of aging.

However, the scariest form of memory impairment is Alzheimer's disease. This is a condition where plaques form in the brain and gum up the synapses, leading first to memory loss and then complete neural impairment. The "Big A" is a terrifying prognosis.

It is also one of the biggest areas of research today. With global populations aging rapidly in every nation from Italy to China, there is a worldwide imperative to find a treatment. Much of the work revolves around memory.

Just where do we store what we remember? Since the 1940s, scientists have believed memories are stored in synapses – the connections between the neurons. The plaque that clogs the brain in Alzheimer's impairs these synapses and kills off our memories forever…or so we thought.

A recent Science Daily article discusses experiments by California scientists to transfer the memories of sea snails through RNA. RNA is the chemical messenger that is active inside the neuron cell. It suggests memories may be encoded chemically in RNA inside the neuron, and not outside in the synaptic connections. This means that memories might be covered up and hidden by the

Alzheimer's plaques, but not necessarily lost (at least in the initial years). Memories may also be able to be transferred or even saved, if the RNA itself can be manipulated.

All research is subject to revision and failure and this could be no different. This study, however, is sure to turn some heads in terms of renewed hope. Not just to stop Alzheimer's, but even to reverse it.

Here is the link to read further:

https://www.sciencedaily.com/releases/2018/05/180514151920.htm

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Prices shown are as of close May 18th, 2018.