

"If you can keep your head when all about you are losing theirs".

Rudyard Kipling begins his poem "If" with a challenge to his fictional son; "If you can keep your head when all about you are losing theirs". In these difficult and demanding times such a challenge confronts us all. The morning news brings with it threats of war and disease, high inflation, the end of democracy as we know it, and of course the spectre of bear markets. In such an environment maintaining one's composure and ability to think rationally is a tough task. It seems a requirement now that all theories be expressed loudly and in the extreme. The middle ground can be a lonely place these days. The situation is made worse and intensified by an onslaught of opinions (often presented as facts) from "experts" and the media, who seem to conveniently forget the awful track record of humans in general and themselves in particular to foresee the future. Stock market prognosticators are particularly susceptible to this failing, myself included. (Although I like to believe I feel bad and humbled when I am wrong.) Not so Jeremy Grantham who was on tv this morning gloating about predicting the current market decline without mentioning he's had the same outlook every year since 2013. There's also a lengthy list of pundits who have been forecasting high inflation for over a decade, but do not seem embarrassed to say "I told you so" now that inflation is here. I could go on but suffice it to say there are almost infinite examples of bad information or misinformation that have only served to confuse us all.

The decline in approval of President Biden over the course of his first year in office is not only startling but a cause for concern. Real Clear Politics aggregates various polls and reports that Biden's approval ratings currently stand at 41% approval and 55% disapproval. He obviously can't be held solely responsible for all the problems of the electorate, but as former President Harry Truman famously said "the buck stops here". The Afghanistan debacle was the major turning point for the President's ratings, but there have been other examples where he has seemed weak or ineffective. He came to office

with a reputation for understanding how the U.S. Congress works and having a good relationship with the opposition in the person of Republican Senate Leader Mitch McConnell. To say the results have been disappointing is an understatement. With the exception of the passage of a pared down infrastructure bill, no meaningful part of the Democratic agenda has passed into law. Not only has the President failed to win over any Republicans, but he hasn't been able to control certain members of his own party. His perceived weakness is seen as a concern for global friends and allies and an opportunity for countries such as Russia, China, Iran and North Korea to test his resolve. The mid-term elections are only 10 months away and Mr. Biden badly needs some legislative success and a decrease in the rate of inflation or the Republican party seems almost assured of regaining control of Congress.

It's a bit of a shock to realize that less than six months ago the Federal Reserve remained firm in its belief that inflation was "transitory", that the economy still needed more stimulus, and that an increase in regulated rates was still a long way off. (Another reminder to not believe everything you see or hear.) Now that the U.S. rate of inflation has reached 7%, Mr. Powell and company have done a quick 180 turn and consensus is that the Board will raise rates at least 3 times in 2022. Stock markets that had enjoyed the huge increases in money supply and extremely low interest rates are reacting nervously as you might expect. It remains to be seen if the Fed will stay firm in the fight against inflation or weaken if financial markets or the economy begin to suffer a serious decline. Given the Fed's recent reversal of policy, it probably doesn't make sense to bet too heavily one way or the other, but if history be your guide, the majority of the time the Fed has instituted a series of rate increases the result has been a recession.

Nevertheless, inflation is very real (as we all are aware when we go shopping, it's not just an esoteric economic release) and like

it or not needs to be addressed. One fear is that it can become psychologically self-fulfilling as consumers over-buy to avoid the next price increase and in so doing increase demand and therefore prices. The media is not helping the situation by unnecessarily fueling inflation and supply chain fears. A recent Canadian Press article that also appeared on several news channels had the headline: "Grocery Store Closures Loom". If one didn't take the time to read the complete article you might have hustled right out and started loading up on goods. However, if you did read further, you would have seen "only in rural and remote areas", "only temporary", and an admonition to "avoid panic buying". It seems to me that hoarding would be less of a concern if the media avoided such headlines.

I have noted companies using kinks in the supply chain and higher costs to announce price increases. That's all well and good if those increases compensate for the higher costs, but in several instances profits and margins have improved dramatically, suggesting they are taking unfair advantage of the current environment. Shippers also appear to be using their leverage, given the supply chain problems, to pad earnings. The most egregious example I've seen is that Daimler's A.P. Moller-Maersk, the world's second largest container carrier, is expected to report earnings for 2021 that will be higher than the last 9 years combined. These kind of policies are not helping in the fight to tame inflation.

As I wrote earlier and I'm sure you are keenly aware, markets are nervous and extremely volatile. That's hardly a surprise given Omicron, inflation, the Ukraine, interest rates etc., but the S&P 500 has yet to capitulate. A decline of 10% such as we are currently experiencing is the norm in bull markets, but we are hanging on by our fingertips. Investors are worried enough that serious risk-off trades are taking place; e.g. over 40% of the NASDAQ stocks are down more than 50%; crypto currencies have declined by a similar amount (the new Mayor of New York has lost about 20% of his first paycheck by taking it in crypto coins); and the small cap Russell 2000 is 20% lower than the high reached in early November last year. If I can mix a couple of metaphors; I have battened down the hatches, but not thrown in the towel.

Given the current abundance of negativity, I enjoyed the following tweet from Adam Grant, a business psychologist at the Wharton School: "Informed optimism doesn't mean you only look at the bright side. It means you don't overlook the bright side. If you won't see possibility, you can't solve problems. If you can't imagine a best case, you don't make things better. The greatest antidote to fear is grounded hope".



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