Asset Management

News or Noise: Has the Market Rally Run Out of Gas?

By David Fisher, Chief Investment Officer

After a powerful five-week rally, it was time for a pause in global equity markets last week. The slight backtracking by members of the Federal Reserve was the catalyst for this inevitable reassessment by investors. That said, the rally has proven to be fairly robust and, by many accounts, the strongest since 2014. We especially like the moves by more economically sensitive companies, such as transport stocks, industrials and energy producers. As usual, there are numerous reasons to be worried—global growth slowdown, terrorism, Brexit votes, the Federal Reserve, China—but those are all known threats. The trajectory of the markets over the coming months likely boils down to economic data and the results of corporate earnings that start in two weeks.

Below, we touch on a couple of important stories from last week that we classify as noise and end with a short technology piece—one that we think will take time to develop but will be newsworthy.

> **"The media is on fire over the release of the Oculus Rift, with projections ranging from 'this will change the world' to skeptics who think the hype will flame out."**

No. 1: Is the Current Rally for Real?

☐ News ☑ Noise

Two weeks ago the Federal Reserve seemed to make a clear and specific point of "pausing" rate normalization. It appears that some members of the Fed are having second thoughts on that decision, especially given the recent data on inflation. St. Louis Fed governor James Bullard, who is well recognized as one of the more middle-of-the-road governors, said last week that another rate hike "may not be far off." This raised questions about whether he meant as soon as the April meeting. Other members of the Fed also tried to downplay the market's focus on "dot-plots." Much was made of the change in expectations for 2016 rate increases from four to two by the average of the Fed governors at the last meeting.

The result of all this confusion was that the dollar rose as concerns of a "too quick" Fed crept back into the markets. In the coming week, at least four Fed governors will make public comments. It could be that these statements will lead to more clarity, but if recent comments are any guide, it may be more likely that they lead to more confusion. In our opinion, the Fed is not likely to fully reverse the March announcements at its April meeting and raise rates, especially without a press conference at that meeting. The June meeting is the next logical date for a rate increase, but that meeting falls four days before the Brexit referendum vote, which seems like reason enough for a delay. Thus, we suspect that the next rate increase won't come until sometime in the third quarter—plenty of time for the market to continue its recent upside move.

No. 2: Investor Hubris Creates Chaos at Storied Firm

☐ News ☑ Noise

In a letter to investors last week, Bob Goldfarb retired as CEO from famed investment firm Ruane, Cunniff & Goldfarb. The firm is recognized as one of the most influential investment managers of the last 50 years and is also known as the firm that Warren Buffett recommended to his investors when he closed his hedge fund in the early 1970s.

The firm has been rocked by an ill-fated investment in Valeant Pharmaceuticals. The firm became the largest investor in Valeant and at the stock's peak had 36% of the firm's $21 billion in investor capital in this single holding. The firm historically has invested in a concentrated portfolio, but even for them, this became an outsized position. The only other position that grew to more than 30% in their history was Berkshire Hathaway itself. The firm vigorously defended the position in a letter to investors last fall, but with the stock declining 70% since that time, the pressure on the firm became unbearable. Late last year, two longtime directors of the firm's mutual fund (The Sequoia Fund), one of whom was personally selected by Buffett, resigned. Goldfarb and the senior analyst who covered the position both departed last week; and when Roger Lowenstein, the Chairman of the firm, was asked about Goldfarb's responsibility, he answered, "He was CEO of the firm. Bob was responsible."

Fair or not, a 45-year track record in managing money was destroyed based on a single mistake. Now with the departed individuals taking the fall for the mistakes, the firm will try to rebuild its reputation. For the rest of us, this is another lesson in how hubris can be the single-most damaging character trait for investors.

No. 3: Oculus Rift Finally Ready for Retail

☑ News ☐ Noise

After years of anticipation, the Oculus Rift virtual reality headset launches for retail this week. "This will start the modern era of modern VR," claimed *Forbes* magazine over the weekend. Following the Oculus Rift, HTC and PlayStation will launch headsets this year. Over the weekend, the first pre-order was personally delivered by Oculus founder Palmer Luckey to get maximum buzz in the IT media world.

The media is on fire, with projections ranging from “this will change the world” to skeptics who think the hype will flame out. I wrote about my first VR demo about a year ago. Even though the system I was using was fairly rudimentary, I did get the feeling that VR is much more transformational than I had anticipated. Certainly, gaming applications will be the first to take off, given the price points. Beyond that, it may take time for slower-moving industries like traditional media, education and corporate training to fully adopt VR. Mark Zuckerberg of Facebook admitted as much last fall when he warned that “this is going to grow slowly.” But then again, the Internet grew slowly at first as well. We would put our chips on the side of “world changing” at this point.

What Is News or Noise?

Like most of you, we are inundated with information on our phones, in our email inboxes and on the Internet. Clearly, the world doesn’t need another investing blog to reprocess stale information or reformat the day’s useless headlines. Thus, in our investment blog, “News or Noise,” we’ve taken up the challenge of sorting through the infinite bits of background noise and seeking the few truly newsworthy nuggets of information. What are the stories today that are likely to be meaningful for investors in the future? A very small number of headlines are important, and of those, many are immediately processed by investors. Only a tiny fraction of all the new data is truly relevant and underappreciated.