STRATEGIES, TRENDS AND NEWS FOR TODAY'S INVESTORS SPRING 2020

Lumbard & Kellner INSIGHT

S&P 500 2,954 * Dow Jones Industrials 24,597 * 30 year U.S. Treasury Bond 1.46%

FOMO

If you tell people that there's a shortage of something they'll ***want some***. Toilet paper, soup, pork chops, Nutella … you're going to get a buying panic. Lately we're even seeing it in the stock market. Pajama-clad investors drink mimosas at noon, open their laptops, cancel their hotel and airline reservations and use the proceeds to buy … hotel and airline stocks.

At least, that's the way it seems. But it's important to note that *most* stocks are still way down. The S&P 500 would be down much more than 10.1% if not for the oversized influence of a tiny number of huge stocks that barely budged. Microsoft, Apple, Amazon, Alphabet, and Facebook now make up more than 21% of the S&P 500. They're also part of the top ten stocks in the Nasdaq, which drive 44% of its valuation! Take a broader view, and you find that the 1,900 stocks listed on the New York Stock Exchange are down 18% this year. Energy, autos, and banks are down almost 40%.

Interest rates are lower, so ***the stocks of companies with unaffected earnings should be higher;*** but only a few are. These stocks have declined, despite two raging rivers of money flowing through the canyons of lower Manhattan – one from the Fed, and the other from the Congress. Consumers and CEOs are at home sitting on their hands; but that money WILL go somewhere.

There were more than a few upside surprises in the earnings reports of April, and we're not just talking about Facebook and Google.

Hundreds of stocks leaped upward on surprisingly positive earnings. And many of these, such as Corning, homebuilder D.R. Horton, specialty-chemical-maker Kraton, Lockheed, and MetLife are still selling at prices far below their highs.

At the market low on March 23rd you didn't need to guess at any of this, because investors were dumping shares indiscriminately in a panic. If everyone around you is afraid, the stock market is about to bottom. It doesn't matter what the news is, or what the circumstances are.

John Templeton's dictum, ***"buy at the point of maximum pessimism"***, fits ***every*** situation. Honestly, you won't be able to distinguish "extremely painful"

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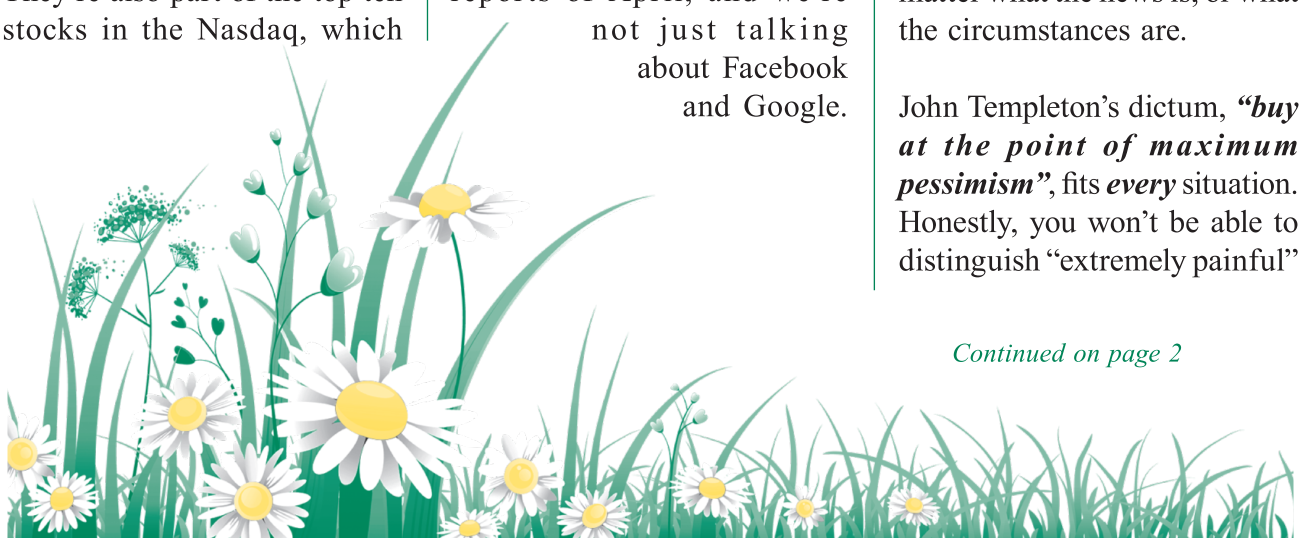

FOMO

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from "maximum pain", but that should always be your goal. It's ***never*** "different this time".

When there's fear and uncertainty investors look to the stock market itself for clues. They study yesterday's prices, hoping that the market is trying to tell us something helpful. **It's not.** If you insist on seeing the stock market as an intelligent and sentient being, you're better off seeing it as an evil genius. It's trying to get you to buy high, and then sell at the worst possible moment.

We believe that the economy will be back to "normal" in 2022. If that's true then the stock market will be back to normal next year, or even sooner. Some people will buy in time to catch the whole rise, and some won't.

The uncomfortable thing is that you're in competition with other investors to pick the right moment. If you wait too long somebody, or a million somebodies, will jump ahead of you in the line and force you to buy after the rebound.

It's ***risky*** to take money ***out*** of the market. ■

Have you been studying charts, trying to discern what the market is trying to tell us? This is what the kindly Mr. Market ***really*** looks like.

BARGAINS

At the start of the pandemic we held too many financial and small-cap stocks, and we sold too little before the panic began in earnest. We regained ground by buying at the bottom at insanely low prices. Why should the shares of government contractors, with bombproof earnings, decline? Lower interest rates should mean higher prices. So we bought Northrop Grumman, added to Lockheed and FedEx, and bought homebuilder D.R. Horton, drywall supplier GMS, and General Motors.

We boosted our buying power by selling Walmart and Zoetis, big winners that had hardly declined at all. Then we purchased Applied Materials and homebuilder M.D.C. Holdings. We sold a couple of holdings that might get caught in the energy vortex, and studiously avoided airlines, hotels, restaurants, nursing homes, retail and office real estate, shared cars and offices, and cruise ships. It's scary out there!

BIG DIVIDENDS

We haven't been buyers of electric utilities, REITs, energy partnerships, or other popular "income" stocks. But big yields are popping up all over, simply because stock prices have declined:

AT&T, a leader in the 5G revolution, yields **7.1%**; more than 4 times the yield on the best one-year CD. And HBO Max launches soon!

Corning yields 4.2%. Gorilla Glass, catalytic converters, glass for TVs and laptops, fiber-optic cable …

MetLife gives you 5.5%, almost ***four times*** the yield on a 30-year Treasury bond!

Homebuilder **M.D.C. Holdings** yields 4.4%.

Moody's gives a AA3 rating to **Prudential,** but at just 1/3 of book value, fresh off a 10% dividend increase, it yields 7.7%. ***Get a piece of The Rock.***

Takeda, which bought our shares of Boston-based Shire, yields 4.4%.

Singapore Telecom yields 5.3%. That's ***forty-one times the yield on a U.S. Treasury bill***. Telephone service in the fourth-richest country in the world is not going to go away!

FLASH FROZEN

In March the U.S. economy simply stopped, in a way that we've never seen before. The response from the Fed, Congress, and the Treasury also broke all records for speed and size. The recovery won't be swift or pleasant, but it might be underway now.

That's right. ***The recession has ended, or it will end in the next few weeks.*** Recessions end when GDP stops falling, even if there's still a year of pain and unemployment ahead of us. The decline of GDP was so steep, and so sudden, that we're already bouncing along the bottom.

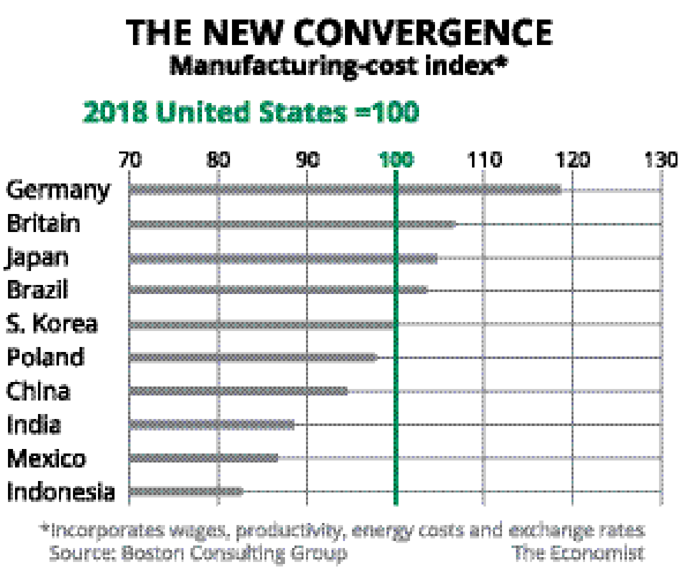
The outlook for the economy and the markets is intertwined with the nation's fear of the virus. The number (and urgency) of vaccine, monoclonal antibody, and antiviral programs is unprecedented. We can also say that reports from the hardest-hit countries (Spain, Italy, the U.K., France, and Belgium) have improved dramatically. Sweden, which never closed its economy, has reported fewer deaths per million than any of these countries.

2020 is obviously going to be a bad year for the economy, and even in 2021 corporate earnings will be lower than those of last year. Some industries will be permanently damaged as a result of the changes in work practices and consumer preferences that will result from the pandemic. Entire office buildings could empty out, as companies learn to manage employees who work remotely, and city dwellers might flee to the suburbs the way that they did in the 60s and 70s.

The markets will anticipate any improvement. They might look a few months ahead, or more than a year ahead. There are no simple rules. What we do know is that Congress and the Federal Reserve are pumping more money than ever into the economy, faster than they ever have before. They're throwing dollar bills off rooftops, hoping to keep most American businesses alive until consumers are brave enough to eat out again.

Paul K. Wright, CFA

Many of those rooftops are in Lower Manhattan. Paper money has been falling like confetti in the streets of Wall Street. If this pushes the stock market higher, they won't object. An overenthusiastic stock market will just be a cost of doing business. ■



American manufacturing costs ("100" in the graph at left) are now much closer to those of other countries. Our neighbor Mexico has some of the lowest costs in the world.

Please do not send wire instructions by email. It's not safe! A postcard would be much safer. It's OK to send the bank's address and routing number, but **do not put your account number in an email!** We'll be happy to take your call.

SENSIBLE SHOES

In weeks when the stock market goes **UP**, investors think it's a sign that the recession will be short. Or maybe Wall Street is looking past the valley to the better earnings ahead.

When stocks go **DOWN** they worry that it's a sign of future trouble. They quickly dump the stocks of mid-sized companies, small companies, retailers, financials, autos, and anything else that ***other*** investors might consider selling. The stocks decline, which in turn alarms Wall Street. The fact that ***these*** shares are declining must be a sign of approaching disaster! ***2008 again!***

This has been hard on value investors. After a few rounds of these panics money was pulled out of "value" funds and investment firms, causing further liquidation of these underpriced stocks; and a deeper decline. Even more money was invested in FAANG. The expensive stocks became *very* expensive, and the inexpensive stocks became very cheap.

This huge swathe of the market has been burdened by a persistent fear of a coming recession, but now it's ***here***. We're in a new business cycle now!

The gigantic bubble of the 1990s has faded into memory, but in those years lots and lots of stocks were *falling*. It's true! As the tech stocks roared upward to insane heights, boring companies with big dividends were *crushed*.

Then the tech stocks collapsed. Slowly, then faster. The unloved shares rose from the ashes. They rose continuously for years and years. ■

One index … two indices?

How can a slim chance and a fat chance be the same?

If the plural of tooth is teeth, why isn't the plural of booth beeth?

AP Photo/Thom Baur

"When a SpaceX Falcon Heavy reaches orbit, it will have burnt about 400 metric tons of kerosene and emitted more CO2 than a car would in two centuries."

– Bloomberg.com.

SpaceX is owned by the brilliant, innovative, and offbeat Elon Musk, who says that he's spending billions on space travel because humans will destroy the earth's atmosphere and we'll all have to move to Mars.

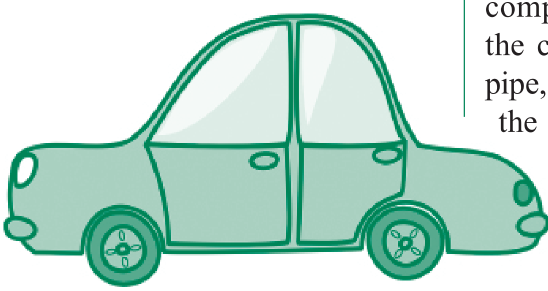
He'll destroy the earth's atmosphere all by himself if he tries to move just half the citizens of California to Mars. The atmosphere of Mars, by the way, is 95% carbon dioxide.

Elon and his wife Grimes (née Claire Elise Boucher) have named their new baby " X Æ A-12 Musk ". X for a variable that is unknown, Æ because it's the way elves spell A.I., which stands for Artificial Intelligence (but also means "Love" in Japanese), and A-12 for their favorite airplane. Elon says that Æ is pronounced "Ash" while Grimes, who came up with the name, says that it's pronounced "A.I." ■

CHANGES AHEAD

The pandemic is accelerating a lot of trends that were already underway. Brick-and-mortar retailers had already been staggered by Amazon, and a trickle of bankruptcies will now turn to a flood.

The media loved to talk about the Sharing Economy, but it doesn't look quite as compelling now. WeWork? We working from home now. VRBO? Renters and homeowners are angry about the new fees. Uber? No thank you! Right now it's a wonderful thing to own a car, because it's a personal bubble—a safe space—in which you can travel the world.



Office buildings and office REITs are also an area of concern, now that everyone has learned how to work remotely. Michael Heric of Bain & Co says that this has caused many companies to actually *accelerate* the pace of automation. Companies that billed their customers manually have had to quickly implement software to do this job, because their employees are working from home. The same thing is happening with the payment of bills.

Software and artificial intelligence are reducing the number of people needed in accounting, human resources, and other departments. For years our economy has been unbalanced, with a heavy emphasis on consumption and very little investment. A more balanced and efficient economy will be wealthier, with lower consumer prices and higher profits, but it means higher unemployment in the short term.

New technologies in oil and gas have had a bigger U.S. economic impact than any dazzling technology you can think of. They'll leave a lasting benefit to consumers in the form of low energy prices. Wildcatters will also leave a legacy of red ink and crippling debt. Employment will shrink, and energy-related service companies will shrink. So will the companies that make drilling pipe, machinery, drilling fluid, and the like.

Will consumers return to restaurants, hotels, and air travel? Yes. Maybe sooner than you think, but there will be bankruptcies.

So what will grow? Everything else. The Treasury, Congress, and the Federal Reserve intend to borrow and print enough to bring GDP up off the floor, and push it past knee level in 2021. Maybe waist level! Some families have already received $4,400, and even Social Security beneficiaries are getting big checks.

All that money has to go somewhere, and the effect will be magnified by low prices, especially on gasoline. Pickup truck sales might surprise to the upside. Housing and renovation will boom, fueled by low interest rates. Wealthy Americans will spend and invest to create jobs. There's pent-up demand for dental work, eye exams, haircuts, yoga, and Pilates. There's gonna be a lot of fresh asphalt.

Drew D. Kellner, CFA

What the world needs now is entrepreneurs. **There is an unlimited demand for personal service!** We'll spend on food,

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For decades we've been publishing the performance of an account that pays fees, and never adds or withdraws money. It's currently valued at $1,165,528, down from $1,308,411 at the beginning of the year. These years have been hard on value investors, and hard on those who invest overseas; but the portfolio is worth a good bit more than five times its $217,974 value on December 31, 1999, near the top of the tech-stock bubble. For further information please see our website, www.Lumbard.com.

CHANGES AHEAD

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personal care and beauty, fitness, wellness, health care, pet health care, pet beauty, Pilates for pets,

recreation, gardening, life insurance, appliances, furniture, home entertainment, performing arts, gas-guzzling boats and recreational vehicles, *repair and maintenance*, sailboats, rockin' stone walls, and trips to Quebec City.

What would you do with an extra $5,000? You'll think of something. ■

5G

"Huawei has warned that its survival is at stake following the US government's latest efforts to cut the Chinese company off from international semiconductor supplies."

– The Financial Times.

Washington fears that Huawei's low costs will allow it to dominate next-generation telecommunications, and fears that the Chinese government will find ways to use their gear for spying. The Economist suggests that trying to destroy Huawei (and pushing China to develop its own chips) is like trying to stop a river from flowing. A better idea would be to imitate the inexpensive mobile network that Rakuten just launched in Japan by substituting software for expensive hardware. Its current 4G generation uses software and equipment from Red Hat (IBM) and Cisco. And 5G service is coming, with help from Intel, Robin.io and some other American companies you've never heard of. ■

"The S&P 500 Index delivered its worst ten-year return, negative 3% per year, over the ten years ending in February 2009.

The worst twenty years delivered a positive return of 6.4% a year. This occurred over the twenty years ending in May 1979."

– The Balance

THE WORKING POOR

Last year 40 million Americans worked in the restaurant, airline, and hotel industries, including a **huge** number of low-income workers. If the charming inn you stayed at last October files for bankruptcy, the person who cleaned your room will be out of a job. The same is true for dishwashers, busboys, and the people who work in the wee hours to clean restaurants and offices. For their sake we need to find a way to bring down the level of fear.

IMMUNITY

Qatar has reported 22,000 cases of coronavirus. On a "per million people" basis that's 7,500 cases, which puts Qatar in the top ranks of nations in terms of the reported spread of infections (which, of course, is a tiny fraction of the true number of infections). But Qatar has only experienced 13 deaths, or 5 per million citizens.

Obviously it's a good thing to have a small number of deaths, but it's easy to forget that it's also a good thing to have a large number of immune citizens in your population: those who have recovered from an infection, perhaps never knowing that one occurred. Some claim that immunity doesn't last, but if that's true you're going to need a vaccine shot every few weeks for the rest of your life!

Taiwan and South Korea have done a wonderful job in tracking and suppressing the virus, but Qatar is better positioned for the future.

CRAZINESS!

The price of a share of **Netflix** (NFLX - $453) is more than a hundred times the company's earnings per share in 2019, and fifty-five times the earnings estimate for 2021. But even those tiny earnings can't support a dividend (the yield is 0%), reduce debt, or provide cash that piles up in the company's bank accounts. Each year Netflix spends it all, and billions more, on new TV programs. The company's debt grew from less than a billion in 2014 to five billion dollars in 2017. In just the next two years it jumped to ***$15 billion!***

Over that same time span the debt of **MetLife** (MET - $33) *decreased* from $20.5 billion to $14.5 billion. MetLife pays a huge dividend, and it also spends cash to buy back shares; 20% of the company in the last six years. Shareholders who used to own 10% of the corporation now own more than 12.5%, *and* they received shares of the spinoff of Brighthouse Financial in 2017.

Since the spinoff earnings have grown 50%—the company just thrashed its earnings estimates—and book value has grown from $54 to $77. The stock sells at 43% of book value. Netflix sells at 2,200% of book value.

So, which would you rather own? MetLife at 5.5 times earnings, with a 5.5% dividend, or Netflix at 55 times "earnings" that need to be put in quotes? ■

May 6 (Reuters) – "Norwegian Cruise Line Holdings Ltd has raised over $2.2 billion through debt and equity offerings … The company warned on Tuesday that it might not have funds to keep its business running for the next 12 months."

SERIOUSLY? Who would lend money to a ***cruise line?*** And why would they tell everybody that they're about to go bankrupt before asking for loans?

'BURBS

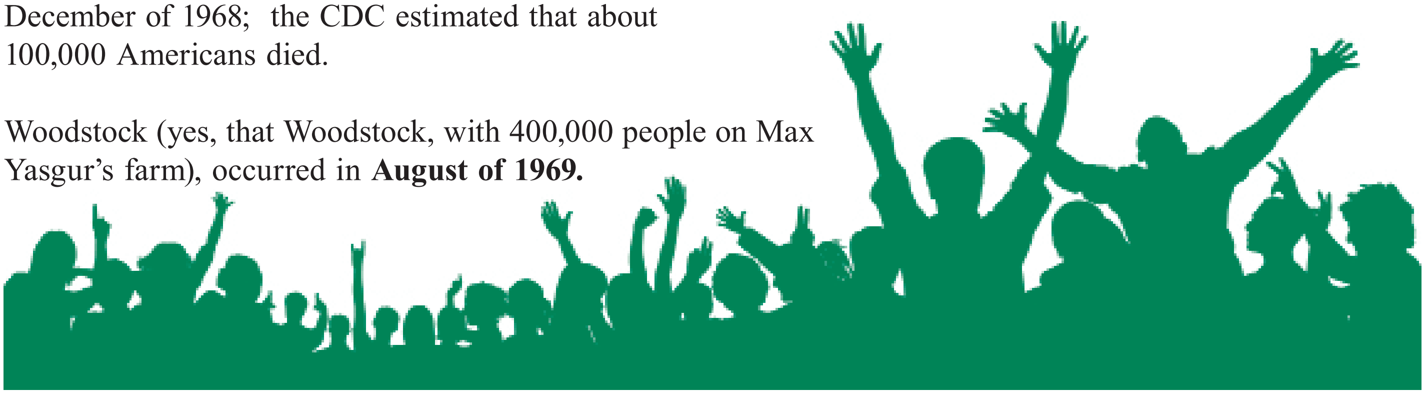
Big cities were hit hard by the pandemic. Offices, apartment buildings, subways, and buses are often "enclosed, with poor air circulation and a high density of people". Not as bad as your local pub, but lots of people are dreaming about owning house with a white picket fence.

Wealthy New Yorkers were already moving to Florida. The Wall Street Journal says that a New York State resident with a $5 million income will save $394,931 in annual taxes if he or she moves to Florida. ■

Taiwan Semiconductor (TSMC), which makes some of the world's most-advanced chips for Nvidia, Qualcomm, and AMD, will build a $12 billion 5-nm fabrication plant in Arizona. TSMC is nearly 20% of our Taiwan ETF (FLTW - $26). It's a big customer of Applied Materials (AMAT - $54).

According to the Encyclopedia Britannica , the **1968 - 1970 pandemic** "originated in China in July 1968 and lasted until 1969–70" and "resulted in an estimated one million to four million deaths". It reached the U.S. in December of 1968; the CDC estimated that about 100,000 Americans died.

Woodstock (yes, that Woodstock, with 400,000 people on Max Yasgur's farm), occurred in **August of 1969.**



THE MAGIC MONEY TREE

Our federal government has been running huge deficits ever since 2009. In 2020 "huge" ballooned to "stupendous", and hardly anyone seems to care. Yes, we need to keep the economy from collapsing during the pandemic, but will we then work towards a balanced budget?

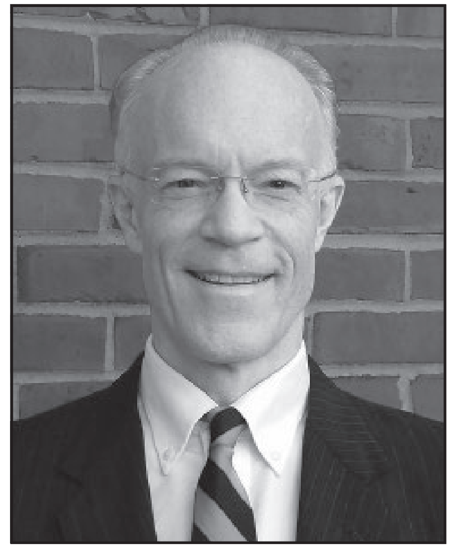
Not likely. Lots of politicians believe that the government will always be able to pay off its debts by printing more money, and the last two "Modern Monetary Theory" economic rescues have given them the courage to shout it from the rooftops. Wags call it the Magic Money Tree, because it's a justification for nearly unlimited spending. There will be rainbows, and cute puppies, and nobody will ever have to work again!

Few of the incumbents have a problem with this right now, because they're buying votes for re-election It's bi-partisan! In 2020 we'll spend more than ***twice*** as much as we collect in taxes.

So what's the catch? Inflation. It's been so low that economists have been puzzled, but that doesn't mean that it will never emerge again. Once it gets started it's very hard to stop. Do you remember the ***20%*** interest rates engineered by Paul Volcker?

Venezuela has been printing money, trying to meet the many spending promises that Hugo Chavez and Nicolas Maduro made to win votes. The Central Bank of Venezuela estimates that prices increased 53,798,500% between 2016 and April of 2019.

That's ***54 million percent!*** ■



INDIA

"The Indian government has reportedly reached out to more than 1,000 U.S. firms in China since mid-April, particularly makers of medical equipment, food processing and auto parts … India is also reportedly developing a land pool the size of Brunei for foreign firms, a move intended to address the chronic difficulties faced by companies with land acquisition."

– Geopolitical Futures.

Land reform has been a big topic in India for many years, because urban renewal and industrial construction have been almost impossible. How big is Brunei? 2,226 square miles, or 97 times the size of Manhattan. This is **BIG.**

– John Lumbard, CFA

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