



Alternative Facts

John M. Gustafson – 31 December 2020

"This time we aren't fighting the Yankees, we're fighting our friends. But remember this, no matter how bitter things get, they're still our friends and this is still our home." - Atticus Finch

Looking back at my archives of eleven-plus years writing these notes in this setting, things veered from the strictly financial, into a blend of finances and politics as our current schism began about eight years ago. That divide has grown to a place where the Hatfields and McCoys have switched sides of the field, but carry on the same arguments, as if it isn't simple as can be to find them arguing the exact opposite position only a few years ago.

My hope is that when we get to the other side of this morass, the quote I lead with above will be remembered. 2020 has been a disaster for many people and there is plenty of blame to go around, but the biggest issue is that everyone has seemed to forget that we are all Americans and the fate of one state or party cannot be unaffected by the other. I realize that both sides reading this are going to immediately blame the other – and that's the point, the same actions that got us here will not get us out. Please keep that in mind to help 2021 be far better for everyone... (pushes soapbox back under the podium)

"The truth is rarely pure and never simple." - Oscar Wilde

Another true oddity of the year just ended is that we have shown that our "economy" is actually two vastly different pieces in the same ecosystem. After expanding for 127 months, things came to an abrupt halt in February when the issues of the pandemic first came to light and then the crack in the border between these two pieces became a chasm.

The Fed's swift action of crashing rates back to zero and opening the liquidity spigots quickly turned the tide for large corporations. It wasn't just people catering to online shopping or things people can do to recreate outside, it was also any large corporation who could suddenly borrow almost for free and allow them to survive and pivot. That, however, didn't do anything for small businesses.

Bars, restaurants, mom & pop shops and even small manufacturers of less than 50 employees – which are the core for most American communities away from major population centers were decimated. The CARES Act which kicked off the PPP loan program and installed several tax

breaks for purchases was a help, but the politics once again got in the way and the teams couldn't agree on what was the right path forward.

The Fed action also didn't mean that temporarily furloughed employees wouldn't become permanent cuts. We had that precise situation occur in the fashion industry here in the Columbus area. Thousands of corporate headquarters employees were furloughed as retail operations closed up for a couple of months across the country. However, well over 1000 became permanent layoffs in August – locally, not counting those lost across the country. (Conveniently after the requirement of the PPP program to keep payroll stable through June.)

“In politics, stupidity is not a handicap.” - Napoleon Bonaparte

Another issue that has grown out of the past decade – and become amplified and weaponized via social media – is the fact that “news” is now a profit center for companies, therefore Americans really don't have “news” available to them anymore. I read papers and sources around the globe as I review our investments and all countries have a bias to their media, but it's fairly well known which way they lean and you can take it from there to apply your grains of salt.

Tribal-America likes to deny that *my* favorite news channel or social media feed is biased or can be manipulated – and everyone else's is nonsense propaganda. Clearly that isn't true either...

The larger infection that has blossomed in 2020 is identity politics. Republicans used to scoff at Democrats who played such games, but recently have jumped in full force and both sides now wallow at the grievance trough. Not sure how that benefits the country, though it makes one “feel” better. Our entire political world and much of society has become Festivus, with daily “airing of the grievances.”

“Never attempt to win by force what can be won by deception.” - Niccolò Machiavelli, The Prince

By pointing all this out, I'm not trying to veer completely out of my investment lane – I promise this all relates. I'm also sure that most of you reading this note are keenly aware of these factors. I simply want to make sure they are front of mind as I delve into where this leads the markets and our economy.

The misinformation and outright disinformation (the “firehose of falsehoods”) isn't simply infecting politics, it is changing the way Americans view the world. (and the way the world views us) It is not possible for large corporations to continue to thrive solely via cheap credit and having the ability to offload expenses (i.e. people) if general demand dries up.

The public markets did have reason to rise to this point after the devastating initial drop in the spring; once recognizing the actions of the Fed and earlier bills in Congress were the proper safety net bridging the gap to make things feel somewhat normal. Now however, we find ourselves in a different place...

“I use emotion for the many and reserve reason for the few.” - Adolf Hitler

The stock and bond markets in the U.S. in 2020 were the beneficiaries of constant emotions that clouded reality. The artificial personal and corporate stimulus allowed people to think the turnaround was coming soon, only to be pushed out another week or month, over and over.

Finally, with the multiple COVID-19 vaccines flowing across the globe, we can at least see the light at the end of the tunnel. However, the small business damage has been done and once again our dysfunctional politicians in D.C. are fighting about nonsense and blame.

Tribalism has swapped sides once again and those who ignored deficit spending en masse while things were booming are now suddenly feeling frugal. As mentioned in previous missives this year – an economic crisis and unemployment caused by outside forces through no fault of the American people is *exactly* the time the Federal Government should use its full faith and credit borrowing capacity to plug the economic holes in our ship. Despite the historically low rates, the demand for US Treasuries remains as strong as ever.

Of course it will all need to be paid for somehow, but that is a conversation for the future. After 9/11, we simply came together to find a solution and course of action (whether you liked it or not) and worried about the finances later. Many prominent economists – including the chairman of the Federal Reserve multiple times - have stated unequivocally that if we don't provide aid now, we risk a deep recession similar to 2008 in the coming months. It is far easier to deal with low-rate debt than with massive, systemic unemployment caused by thousands of companies that simply disappear.

State and local government can ban evictions, but all that does is push the burden onto the landlords - most are small companies, not corporations. Those owners have mortgages, need income and like the many Americans who rent their properties, have failed to properly save for a rainy day.

“Because there are three classes of intellects: one which comprehends by itself; another which appreciates what others comprehend; and a third which neither comprehends by itself nor by the showing of others; the first is the most excellent, the second is good, the third is useless.” - Niccolò Machiavelli, The Prince

Beginning back in September, Goldman Sachs ran a video series for institutional investors that brought in experts to discuss the economy, the upcoming elections and how to get out of the slump brought on by COVID.

One presentation I watched just after the election featured old political hacks, Rahm Emanuel and Andy Card. Those guys didn't historically agree on much, but they did both agree on this call that the only way to get any form of cooperation to move critical legislation forward is to bring back “earmarks.”

Everyone hates them and complains that it's simply pork-barrel spending, BUT they were allowed 2011 – killed-off at the beginning of this damaging period. It is what led to something I have lamented many times – both sides of the aisle now view a 65% “win” as a 100% “loss” and it is about power and control, not about moving the country forward. It certainly hasn't curbed wasteful spending, only altered who gets to do it.

To give an example or two as to what kind of difference this might make to help get our economy back on its feet – the last “infrastructure bill” was under George “Dubya” Bush in 2005. We also haven't built a new airport in America since 1995! It's in Denver – look it up...

All of my friends in SC aren't surprised with all the things named after Strom Thurmond, PA has expressways and interstates named after Bud Schuster and WV features multiple bridges, buildings and roads named for Robert Byrd. Probably not necessary to put names on such things, but it's clear who brought the money back from Washington for the projects.

Sadly, both politicians in the current environment need to be bribed to take action (as they always have based on my previous examples) - but that seems like a much more pleasant situation than we find ourselves currently. Gridlock is great as long as everything is humming along - as it was prior to 2020 for a decade - but now we need action to avoid further crippling damage.

“You don't pay taxes - they take taxes.” - Chris Rock

On another one of the GS calls, they had three strategists discussing the economics of the deficit and such. They did agree that because of the overspending of the past decade, a portion of the Corporate tax cut would need to roll back. However, they did not give the doomsday scenario popular in the media. The corporate rate cut was from 36% down to 21%, which did exactly what was hoped – cause U.S. Corporations to repatriate *\$Trillions* parked overseas. Most believe a bump closer to 27% is likely.

Unfortunately, Congress, proving once again that they are more like the fabled Grasshopper than the Ant, spent wildly when things were going well. Each quarter of the past few years (both before and after the tax cut) flooded our Federal coffers with record revenues. It has never been a revenue issue – it's a spending issue and remains so to this day.

Again, there is an upper limit, but that is not a concern in the middle of the storm if you want to safely see the other side.

“It could probably be shown by facts and figures that there is no distinctly native American criminal class except Congress.” - Mark Twain

If we can get past January 6th without significant, debilitating violence being fomented around our election, it is my hope that the rhetoric can subside for a little while to make some significant

changes. As stated multiple times, “hope” is not a strategy, so therefore we are going to make some portfolio adjustments early in the new year.

Predicting what anyone in current politics will do is also a fools errand, so the changes I’m working on now are to try and mitigate any potential damage caused by political inaction and continued economic deterioration on the front-lines, regardless of how corporations react.

This will mean slightly less exposure to US stocks – of all sizes. Likely a return to more Asia exposure. An area that has worked for the past several years to move their dependence on America as a consumer, driven by uneconomic trade policies, to newly developed areas of the globe previously ignored. If there is a non-violent country looking to expand economically in Africa or South America, there is now tons of Chinese and Indian money sloshing around to help them move forward. They are literally creating consumers for their goods.

If the Congress makes positive, necessary moves outlined, our portfolios will still participate, but if the infighting never ceases and things spiral downward, the external opportunities should help minimize that damage. The elevated levels of cash we have held, despite the lack of yield, didn’t hinder us much in terms of overall returns for 2020 and certainly moderated the volatility.

As with any situation, chaos can bring opportunity and the extra cash on hand can help us take advantage. This too shall pass and we need to be able to ride out whatever may come.

“Games are won by players who focus on the playing field – not by those whose eyes are glued to the scoreboard.” - Warren Buffett

The good news from all this recent Sturm und Drang is that the election actually showed that America is more moderate on most things than any media outlet – MSM or socials – would lead anyone to believe. The Democrats still have a slight majority in the House, but overall *lost* eleven seats and the Senate shifted left by two – depending on the GA election next week. Nancy and Mitch are still in charge, but neither one has a hammer.

Despite the messaging, if you focus on the players on the field, moderation may actually have a chance and we can back away from what has mutated from a two-party democracy into operating as a single-party, parliamentary system. Stay tuned...

With all that said, we move into 2021 looking for the positives, planning for the negatives with good wishes for happiness and good health to all of our clients, friends and family

Thank you as always for your trust and your business. Stay safe & healthy and we’ll talk in person again soon. Cheers!

A handwritten signature in black ink, appearing to read "J.M. Gustaf". The signature is fluid and cursive, with a large initial "J" and "M".