THE VIEW FROM PRINCETON

Market Commentary ♦ April 2013

"THERE'S A CHANGE IN THE WEATHER
THERE'S A CHANGE IN THE SEA
FROM NOW ON, THERE'LL BE A CHANGE IN ME"

(Lyrics by Billy Higgins, 1921)

Memory cannot recall a time when so much of public commentary has been so enduringly at odds with reality as that in recent years. This unreality formed a significant market influence – and is slow in disappearing. Filtering through and coping with the contentiousness of politics and the self-serving claptrap of commentary from Wall Street (broadly defined) became a necessary task. Thus, through 2012, we fully minimized the several putative "double dips" in the economy expected by others that didn't happen, as well as the so graphically conveyed foreboding 2013 "fiscal cliff" that suppressed anticipations in 2012, but fading in 2013.

This all was corollary to the several years of worry fomented by the Greek crisis. Reduced to reality, Greece was not nearly so much of the problem as the licentious profligacies of banks and large trading entities. The gross national product of Greece in worldwide consequences would seem to be little more important than that of Hazard County, Kentucky (eastern Kentucky, if you don't know). Since there are many small aspiring nations, there will ever be sovereign debt crises so long as such opportunistic trading (via short selling and the creation of derivative instruments) by large trading entities is allowed. This was prophetically expressed by the President of Mexico (in the mid-1990s, when American funds had trashed the peso) in saying Mexico is just the first of other small nations to be victimized by modern capital markets. Slowly, an atmospheric change evolves from episode after episode of irresponsible banking that eventually might impose thoughtfulness in deeper and in more benign social terms, both for America and for interrelationships among nations.

If stripped of ulterior or personal prejudice, the landscape can be seen as highly supportive to equity valuations, helped – not diminished – by the gains of last year. Improved visibility and changed attitudes will allow more relevant observations in world changes beyond the range of parochial financial attitudes. These are fundamental and as pervasive as air and water; too huge and too omnipresent to attract attention.

The revenues reported quarterly by publicly owned corporations always provide reality checks that are far more useful than government data – which are late, and adulterated with collection errors and imposed imputations. The recent flow of reports show increased scatterings of specific shortfalls, and an overall slowing of pace, countered partially with a spreading improvement in long-afflicted areas such as residential housing (including related providers), and improvements in state and local governmental budgets and hirings. Considering that the final months of 2012 were furiously slammed by Hurricane Sandy, suppressed by the foreboding "fiscal cliff" of 2013, and by the railings and roilings of national politics, this flow of corporate reporting (for the year and final quarter of 2012) is reassuring. The depressing effects of the "fiscal cliff" showed generally, especially through the electronics industry. The multitude of discreet components that commonly move through intermediate distributors toward final-product manufacturers were weaned and leaned very apparently, which now supports increased orders for restoring normal supply chain quantities of inventories.

The fundamental factors sustaining growth are prevailing over concerns, and months ago the American economy attained the normal commercial evolvement of synergistic interactive regenerative relationships. One of the more conspicuous supportive influences for equity valuations is seen in the increase in merger and acquisition activity. Already, 2013 is off to a massive – possibly record – year. Prices have been at substantial premiums to quoted market prices, showing that these professional purchasers think the selected shares are cheap. This cross references like opinion to other shares as the reinvestment of money paid for purchased shares usually flows into other shares. As additional support, announced share buy-ins and dividend increases exceed prior experience.

Moving from the vastness-vague of universal concepts to industry-by-industry, we would cite several radical significant changes expected in America pertaining to energy, employment and jobs, health and relateds, and especially infrastructure. Investors should be sure that in each of these designations, the changes for prospective years are fundamentally — even radically — different from years past. The aromas of change brought to mind that "oldie goldie" popular song of the early 1920s and enduring for decades with iterative versions:

For, there's a change in the weather, there's a change in the sea,
So from now on there'll be a change in me,
My walk will be different, my talk, and my name,
Nothin' about me's gonna to be the same,
I'm gonna change my way of livin', and if that ain't enough,
Then I'll change the way that I strut my stuff,
'Cause nobody wants you when you're old and gray,
There'll be some changes made today,
There'll be some changes made.

Recall! Let it capture you! Enjoy!

I. For energy, following decades of price increases for fuels, there is now a broadly embedded downtrend of long duration in the prices of liquid fossil fuels, and correlatively across the broad fuel-related and chemical-related spectrums. The decades-long uptrend that was created out of our national policy has ended. What could be more radically different than this? A long downtrend in the cost of fuels has more pervasive social sponsorship than a tax reduction. Everyone and every industrial entity benefits from a lower cost of fuel (except fuel providers, of course).

Support for these surmises is made evident almost wherever you look. It was part and parcel of our national policy to constrain drilling at home, to build inventories in the salt domes of the southern Gulf States, and above ground in Cushing, Oklahoma. National policy could be summarized as keep our own reserves, import from others, and raise prices as we go. That attitude is reversing, coincident with market forces from huge new discoveries of oil (especially under sea water) and from the discovery of available natural gas through hydraulic fracking not so far from major population centers of America. Expectantly, this extends by 30% or more the total available American reserves of natural gas. Rarely has anything of this scale ever happened. Moreover, the means of delivering natural gas allows it to be shipped over waters as never before in increasing scale, which means that natural gas becomes more nearly an international commodity rather than accessible largely through pipelines.

Combined with the upgrading of gas and oil to chemicals and other products, exports will supplant imports big-time, further assured by the significantly more conservative use of fuels and the subsidized sponsoring of alternative sourcing of fuels. You might hope Congressional representatives would factor these considerations into fiscal planning which are many times more important than their vacant, heated bickerings.

II. A new national policy is evolving also that is a radical reversal in the form of infrastructure repair and building. References to the decaying bridges, the insufficiency of roads, and the insufficiencies of some other public works is compellingly apparent. This would not be net costly in social terms; rather, it would provide net savings. Imagine the time and dollars that would be saved when you can traverse metropolitan areas at more than 15 mph, or stalled with engines running. The annual savings would exceed a trillion dollars. Or, the airplanes waiting on the runways to take off, or those being held up from landing by runway congestion. There is another hundreds of billions of dollars of saving. And, when you look at our public transportation system, it is so inadequate for us; and, many of those who visit from afar, think of us as some sort of a backward nation. So, public transportation is also in for a boost as an alternate to delays on the surface through private vehicles.

III. The exportation of jobs to less developed nations and to Asia is slowing dramatically. Our interest rates no longer give Asians a several-hundred basis points or more advantage (as in decades gone by) in high-capital, low-labor-ratioed manufacturing such as semiconductors, textiles, electronic end products, and even automobiles. Dissimilar taxes and subsidies will come under increased scrutiny, and the unevenness reduced. Also, there is likely to be less immigration than the astonishing quantities of very recent years, which, in effect, take jobs from persons who have been citizens in this country for years. Expect, also, a new emphasis on infrastructure spending to be combined with job opportunity sponsorship. The foregoing will all be interactive and mutually regenerative.

IV. Another, to be sure, reversal of trend will be a reduction in military expenditures. The retreat will be more conspicuous in spending beyond our borders. Yet, a large portion of military expenditures will come under a new analysis for justification. This will release human and financial resources toward infrastructure here at home where it is so badly needed for having been neglected for so many years.

V. Also expect a slowing of population growth in America, some reduction in the birth rate while the demographic bulge of elderly will be going on in increased numbers. Meanwhile, we have large industries that experienced little or no recession, owing to underlying self-sustaining forces. Most noteworthily it is the healthcare realm – huge and ever increasing. Medical care will be made more available throughout the world. Agriculture, ever America's trump suit, faces ongoing years of increasing output. Broadly considered to include all related aspects and support services, agriculture is ever our largest single industry, by far.

The sourcing of energy from a variety of technologies and discoveries is more dynamic than in the memory of any of us, for its breadth and totality of expenditures. Lodging, travel, entertainment goes on as though there is a fundamental demographic affinity that crosses national borders and runs throughout our large domestic economy.

This simplest and easiest sponsorship that our national government can give in financial leadership is simply to guarantee the credits of revenue bonds issued by state and local governments to improve their facilities for transportation, for education, for improving health facilities, and other aspects where government participation is important and welcomed, and use is regionally confined. While Federal expenditures will be constrained, expenditures by state and local governments will be rising. If the healthcare program were run differently, there could be perhaps a trillion a year saved. If the military were run differently, there could be perhaps a trillion saved. If we conduct our energy conservation appropriately, we perhaps could save another trillion there. And, Americans do not have to wring their hands in anxious wonder concerning where the money is coming from. The money is already sitting idle in huge amounts. A trillion dollars held by corporations overseas is locked over there because of tax considerations. It is pretty easy to find a way to bring that home.

With all things considered here at home, the economy has moved into a period when it is self-sustaining, self-regenerative, and moving ahead. Slow and steady are key descriptive words, and both are supportive to equity investing. Now it is not all roses. When has anyone ever had the world just as wanted? That is not a condition of human existence, personally or nationally. Many economies are vulnerable to events. There is ferment from the Mediterranean eastward that is beyond prediction, and there are attitudes toward America and possible strikes against America that are sobering to say the least. But these do not have the mass nor the influence to take down the improvements that are going on in Central Europe, in Eastern Europe, in Russia, in China, in the western hemisphere, and throughout the huge continent of Africa, to say nothing of the exporting nations of Australia, New Zealand, Indonesia, Malaysia, the rim of Asia, and others. The pieces of the world are ever more moving coordinately together, though at times rose-colored lenses are needed to see this. Virtually all of the world's stock markets are interrelated in price responsiveness.

For several years, our views have been highly divergent to much that we see and hear elsewhere, and quite opposite to the doomsday prognostications of David Stockman (Director of Budget for President Reagan) that has been given such a high profile of attention. As always, change is the name of the game – especially so now, as relief ensues from the traumatized years. Rarely does it pay to bet against the vigor and endemic growth of America.

As ever, with earnest intent and best wishes,

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