STRATEGIES, TRENDS AND NEWS FOR TODAY'S INVESTORS AUTUMN 2022

Lumbard & Kellner INSIGHT

S&P 500 4,110 * Dow Jones Industrials 32,381 * 30 year U.S. Treasury Bond 3.51%

PATIENCE

It's too soon to buy stocks, bonds, commercial real estate, single family homes, antique cars, baseball cards, crypto, or just about anything else. Yes, it's been a long wait. And yes, you might be able to pick up a few nickels and dimes by jumping in and out of markets at the right times. BUT, we are NOT rebounding from a recession. The recession is still ahead of us. We have NOT vanquished inflation. The Fed is still tightening monetary policy, and it needs to do that. Don't fight the Fed!

It's entirely possible that the market will just bump along, with every sharp rally followed by another sharp and scary drop. Lots of sound and fury, signifying nothing. Or maybe it will go below the lowest low of 2022, and a glum gloom will rule the land.

How about a nice cup of tea? ■

The Federal Debt grew from $20 trillion to $30 trillion in just FOUR YEARS.

$20.2 Trillion in 2017
$21.5 Trillion in 2018.
$22.7 Trillion in 2019
$27.7 T in covid-year 2020
$29.6 Trillion in 2021

As we write these words it's at $30.7 Trillion. This burden will fall most heavily on today's students, and the younger members of our work force. If the Treasury has to pay interest on $31 Trillion, at a 4% interest rate, Congress will have to cough up $1.24 Trillion in interest every year! The White House Budget Office projects that the nation will collect just $4.9 trillion in taxes in 2023. ■

Inequality has increased. Inflation-adjusted average weekly earnings declined 3.6% in the 12 months through July. The same workers who provided food, clothing, water, shelter, and power to those who sheltered at home during the pandemic are feeling pain. Those at the very bottom of the ladder have been hit even harder because food and rent loom so large in their budgets.

The good news is that in the last few weeks wage increases have begun to outstrip inflation. If the next recession is more than a few months away the working classes might be able to dig their way out of this deep hole.

That good news about wages comes with a **caution** flag for investors. Rising wages will push inflation higher and squeeze corporate profits. ■

The Penn-Wharton Budget Model says that over the course of 10 years the Inflation Reduction Act will reduce deficits by $264 billion. The same source says that student debt cancellation will cost $605 billion — IF student debt cancellation stops with this year's crop of students. Gifts to the semiconductor industry will cost $135 billion. Early in this fiscal year the infrastructure bill added $548 billion in new spending.

If you net it all out, more than a trillion dollars ($1,024,000,000,000) will be added to deficits and the debt, above and beyond the rapid, unceasing growth of entitlement programs. ■

Paul K. Wright, CFA

STAGFLATION

We are firmly in a housing recession. Sales of new homes have fallen **50%** from their peak in mid-2020, from an annual rate of more than a million new homes sold to just a bit more than 500,000.

You can also say that GDP declined in the first half of the year, but the economy was not and is not in a recession. The National Bureau of Economic Research is not going to declare a recession when almost 400,000 jobs are created every month!

Most industries are healthy. But you can ignore the "0%" inflation rate reported in August. Gasoline and other fuel prices fell steeply, partly because 42,000,000 gallons of oil are being pumped out of the Strategic Petroleum Reserve every day. That won't continue past the elections in November.

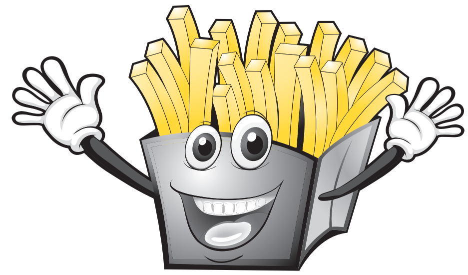
The true inflation rate is probably somewhere in the neighborhood of 5%. Consumers are still sitting on $2 trillion in "above-normal savings" amassed during the pandemic, much of it from government payments. The willingness of our cash-stuffed consumers to buy goods at any price has pushed up corporate profits in the United States. In Great Britain profits actually fell. The Economist says that this is because British consumers weren't flooded with government checks.

Here, prices rose faster than wages. That means that our workers were taking it on the chin for the benefit of consumers and investors. Unlike the comfortable classes, the bottom 20% have less cash than when the pandemic started.

Now the tables will be turned. Their wage increases will drive inflation higher in the next few months, and force the Fed to be even tougher.

This will be a long-drawn-out process. Rising wages will cut deeply into corporate profits. Higher inflation will force the Federal Reserve to tighten credit, raise interest rates, and squeeze the economy. The Fed has never been able to stop inflation like this without causing a recession.

They've already announced that they will withdraw $95 billion from the economy every month, by allowing bonds to mature in their huge bond portfolio—and burning all the proceeds in a metaphorical furnace. ■



A recent survey of 3,222 people conducted by the medical information website Drug Genius found that they'd be willing, on average, to give up *four years of their lives* to have the pleasure of continuing to eat fast food.

Hawaii, Montana and North Dakota residents are willing to give up an almost-unbelievable 12 years.

"The best estimates are that Medicare and Medicaid pay hospitals on average about 87% to 90% of the actual cost of care, often lower in high-cost areas like New York City. Hospitals then shift costs onto private insurers, which tend to pay more than 140% of costs, according to data from the American Hospital Association."

— The Wall Street Journal.

If solar and wind were cheaper than fossil fuels, there wouldn't be any need for the $369 billion in green energy subsidies offered by the Inflation Reduction Act. And poor countries would be eagerly employing solar and wind instead of using fossil fuels.

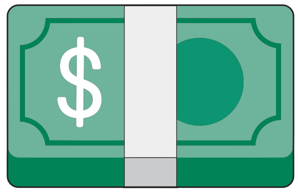
That's not happening. So it's not true.

PBR

In March we bought Petrobras (PBR - $13.90), the Brazilian oil company, which was trading at rock-bottom prices despite the energy shortage. The company pays big dividends because its majority shareholder, the government, wants them to. If you include the upcoming September payout our dividends for just 6 months will be equal to a startling **37.5%** of our purchase price!

"Bank of America today announced a new zero down payment, zero closing cost mortgage solution for first-time homebuyers, which will be available in … Black/African American and/or Hispanic-Latino neighborhoods in Charlotte, Dallas, Detroit, Los Angeles and Miami."

— PRnewswire.com. Zero down payment, zero closing cost mortgages for minority communities…. It worked so well for banks and hapless homeowners in 2008 that they're bringing back a similar program to help us in 2022. You would think when you step on the rake and get the handle to the face once that you wouldn't keep doing it.



Electric vehicles will only be eligible for Inflation Reduction Act subsidies if their metals and minerals come from the U.S. or allied nations. This was happy news for our copper-mining stocks, which had been bloodied by global economic weakness. Electrification, yeah!

Of course, renaming the Build Back Better climate bill "The Inflation Reduction Act" isn't going to bring inflation down. The transition to green energy will suck up labor and materials, causing their prices to rise. And the Manhattan Institute believes that switching to solar and wind power would require that we increase mining by more than 1,000%.

The last remaining nickel mine in the U.S. will close in 2025, but the Interior Department just killed a huge new underground mine in northern Minnesota that had been in the planning and permitting stage for *fifty* years. The Duluth Complex is said to hold 95% of U.S. nickel reserves, as well as copper and platinum.

"Why should a trucker, who didn't go to college, have to pay off a lawyer's student loan debt?"

— Senator Tom Cotton

Drew D. Kellner, CFA

OCTODECUPLED

Our Benchmark account, an actual fee-paying client account, started this difficult year at $1,922,181. It's down 2%, to $1,884,220, but it could be worse. The S&P 500 is down 13.8%, and the Nasdaq 100 is down 21.9%. The portfolio is still worth more than 8 times its $217,974 valuation on December 31, 1999. For further information please see our website, www.Lumbard.com.

Defensive Stocks

Some of our stocks have been swinging around wildly, but our shares of Lockheed Martin (LMT - $418.64) and Northrop Grumman (NOC - $482.30) have been towers of strength. No, we didn't expect a war, or a surprising surge in military spending. They're steady-Eddie, "defensive" stocks, and their prices should have been higher to reflect that.

LED light bulbs are changing the world. The impact of mini-splits and other heat pumps might be even greater, because in most parts of the world they can handle all heating and cooling needs at low cost without demanding a lot of electricity.

Mini-splits are very frugal, but they increase *electric* demand because they replace fossil-fuels. The same is true of electric cars. Drive one if you haven't had the chance yet! Also true of lawn mowers, chain saws, school buses, and trucks. It's a huge amount of additional demand for electricity, and it's going to be more than the pundits think.

If you save ton of gas money by switching to an EV, you're going to drive an even bigger vehicle than you drive now. A Ford F-150 Lightning weighs 6,015 pounds, twice the weight of an average car and ***way more than three times*** the 1,620-pound weight of the 1990 Chevrolet Geo Metro. One of our clients had a Geo, and it got 50 miles to the gallon. Not kidding.

California suffered rolling blackouts in 2020, and recently consumers were urged to refrain from charging their electric cars during peak demand hours. Voters don't like blackouts, so the governor of California just agreed to cancel plans to close its last (carbon-free!) nuclear plant. MIT and Stanford scientists had pointed out that replacing the plant with solar panels would require killing every living thing on 90,000 acres of land. That's more than the land in Hollis, Brookline, Amherst, Milford, and Pepperell. In Japan, Belgium, Germany, and France the lives of more than *thirty* nuclear plants have just been extended.

California will ban the sale of gas generators in 2028, gas lawn mowers in 2024, and gas-powered cars in 2035. Honda and Ford say that it's no longer possible to build EVs as cheaply as gas-powered vehicles. This is another sharp stick in the eye to the working classes, who won't be able to afford the 22,000-watt gas-fired generators (better hurry!), solar panels, and Teslas that have been required by law. ■

"Inflation remains voters' biggest worry, and they understand Washington's role in feeding it. Only recently they watched General Motors and Ford hike the prices of electric vehicles by $6,000 to $8,500—roughly pacing the $7,500 tax credit the Biden "inflation reduction" law bestows. Cause, effect. Millions of American parents read Mr. Biden's Wednesday loan announcement as news that they will be paying $10,000 more for tuition next year (and the year after that, and after that) as colleges reap the loan windfall."

— Kimberley Strassel, in the Opinion section of The Wall Street Journal

We took this photo during a weekend trip to Gloucester. On a calm night one of the blades fell straight down and broke in half.

The 27,000-pound, 160-foot-long blade had been spinning around, attached at only one end, for 10 years. The tower was 492 feet tall before the blade fell off. Weatherman Peter Lovasco, who lives nearby and heard it fall, said that it "Sounded like building after building collapsing on top of each other.'" ■

Customs and Border Patrol, July 2022 Monthly Update

"In total, there were 199,976 encounters along the southwest land border in July, a four percent decrease compared to June... Encounters of unaccompanied children decreased 13 percent, with 13,299 encounters in July compared with 15,255 in June."

CBP total encounters, 2022 to date, through July: 2,242,413

— CBP.gov. The population of New Hampshire is 1,355,000.

OVERPRICED

Healthcare spending in the US is out of control. Medicaid was drastically expanded in the Covid-19 relief bill in March of 2020, and now covers an additional 24 million people at a massive cost to taxpayers. At this point we have a disorganized mishmash of government programs that comprise more than half of all healthcare spending. It's almost as if we've intentionally wrecked the healthcare system.

The White House Budget Office projects that the federal government's six health care programs will cost $1.7 trillion 2022. But that doesn't include all the money that states have to kick into Medicaid, nor does it include all the state and local government spending on healthcare and health insurance for their employees. Total all that up, and you find that "government" is currently paying more than $2 trillion per year.

That's more, on a per-person basis, than Canada pays for ***100%*** of its health care. If we adopted the highly rated and efficient New Zealand system, lock, stock, and barrel, *we could pay for it with just part of what our **federal** government is laying out now.*

"Insurance" was created to protect your finances from catastrophic events. Our "health insurance" does that, but it's *also* an expensive and complicated way to pay for small, routine expenses. Even annual checkups and routine care pass through a "cluster" of complicated systems, burdening doctors and nurses and generating a blizzard of paperwork. The Annals of Internal Medicine says:

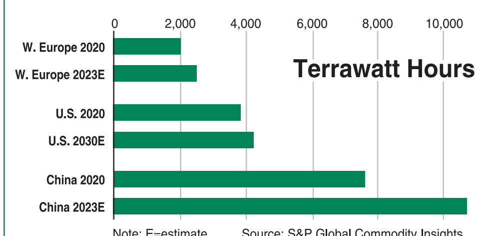
"Over one third of all healthcare costs in the U.S. were due to insurance company overhead and provider time spent on billing, versus about 17% spent on administration in Canada." Simply reducing our administrative burden to the Canadian level would save more than $675 billion per year!

The Canadian, Kiwi, and UK national healthcare systems all allow for citizens to pay for private health insurance over & above what the government provides. Let's imitate them—they're better at this than we are—and create a single payer for all baseline medical expenses. Every checkup, virtually all prescription drugs, every lab test, MRI, X-ray, regular dialysis treatments, mental health, etc. should all be paid for by the government. That would eliminate all the paperwork, tracking, and administrative burden.

This would make way for lower cost insurance plans that would cover only major medical expenses. Surgery, cancer treatment, and catastrophic accidents fit naturally with "insurance" because they are rare. And hundreds of thousands of the 594,000 Americans who now work in health insurance will be freed to end poverty and climate change, save future generations from the federal debt, and cure cancer.

Jay Conway, CFA

Our healthcare system gets more expensive and less effective every year. That means it's getting easier and easier, politically, to make a major improvement! ■



If Europe were to cut its electric power consumption by 100%, that wouldn't come close to offsetting the expected *growth* of power consumption in China in the next few years. Over the next 20 years, India will *also* need to increase its power capacity by enough terawatts to power all of Europe.

Bjorn Lomborg of the Copenhagen Consensus Center, using Rhodium Group estimates, says that the U.S climate legislation will reduce global emissions of carbon dioxide by 1% to 3%, and thus predicts ocean levels "somewhere between 0.006 and 0.08 inch lower in 2100 than they would have been."

BULL

After the tech-bubble peak in 2000 "The Nasdaq composite declined nearly -80% over two years and during that time saw bear market bounces of 40%, 27%, 43% and 51%."

— J.C. O'Hara, MKM Financial.

Some say that a 20% gain is enough to declare a bull market. In the midst of a mind-numbing 80% Nasdaq collapse there were *three* super-bull rallies that exceeded 40%!

"We should be clear that there is no plan to eliminate any student debt. There is a plan to transfer that debt to those who don't owe it."

— Frank M. Wagnon, in a letter to The Wall Street Journal

GAS

It's a natural

Natural-gas-fired peaking plants have become the essential "battery backup" for solar and wind power. There's no other way to offset the loss of wind power for a month, as the U.K. learned a year ago. So we've long had investments in Kinder Morgan (KMI - $18.74) , a natural-gas pipeline company that pays more than 6%, and Golar (GLNG - $27.65, which owns ships that produce LNG in the middle of the ocean). In the last year we added Arc Resources, northwest of Calgary (ARX on the Toronto exchange, or AETUF - $14.22), and Antero Resources (AR - $41.30), which has holdings in Ohio, PA, and WV. Each holds decades' worth of good acreage for producing gas, propane, and butane. ■

If a client's account has too little in stocks we buy, and if it has too much we sell. "Too little" is too risky. "Too much" is too risky too.

WHERE HAVE ALL THE WORKERS GONE?

"The supply of workers has been shrinking. The labor force is about 600,000 smaller than in early 2020, when Covid-19 triggered a deep but short recession. It is several million smaller if you adjust for the increase in population."

— The Wall Street Journal.

If you adjust for population growth, according to Barron's, the U.S. is *seven million* workers short of pre-pandemic levels. They can't all be living off their relatives. How are they supporting themselves? Did large numbers of Americans learn to navigate complex welfare systems? Or did they learn, while receiving government pandemic checks, that it's profitable to work "off the books and under the table?"

There is good news. Bitcoin millionaires are returning to the workforce!

"Guy on jeopardy was just introduced as a "stay at home uncle'"

— @Lizzym03

— John Lumbard, CFA

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