

Lumbar
& Kellner

INSIGHT

S&P 500 4,110 * Dow Jones Industrials 32,767 * 30 year U.S. Treasury Bond 3.71%

THE ABNORMAL YIELD CURVE

“Will the coming recession be painful enough to kill inflation?”

Sufferin’ Succotash! What kind of ugly, dystopian question is that??

Lots of economic indicators suggest that we’re slowly sliding into a downturn. A mild and modest downturn, because so many industries have already declined a bit; at this point they don’t have far to fall. The 2008 recession was deep because *both* mortgage lending *and* home construction were pumped up like hydrogen balloons.

Hiring is still strong, at least in restaurants and other services, and there are a few other signs of strength. The Build Back Better legislation (hilariously renamed the Inflation Reduction Act) is boosting the construction of factories.

On the other hand, lots of economists are troubled by the fact that the banking system started shrinking before the recession even got underway. When the bank runs started, tens of millions of bank customers suddenly realized that they were still receiving very low, *offensively low*, interest rates

on their short-term deposits. Now banks have to offer better rates, their profits are falling, and business people have to pay much higher rates to get loans. Less business investment means that GDP will be lower, and our standard of living will be lower.

The pandemic stimulus caused inequality to rise. Wealthy people saw their stock portfolios soar, while inflation hurt the poor—and a hundred million good citizens who saved carefully and spent carefully. When GDP declines, the pain is felt by rich and poor alike.

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UNDER THE INFLUENCE

“As China continues to assert its economic might, it is using the global social media ecosystem to expand its already formidable influence. The country has quietly built a network of social media personalities ... The influencer network allows Beijing to easily proffer propaganda to unsuspecting Instagram, Facebook, TikTok and YouTube users around the globe. “You can see how they’re trying to infiltrate every one of these countries,” said DTAC President Clint Watts of Microsoft. “It is just about

volume, ultimately. If you just bombard an audience for long enough with the same narratives people will tend to believe them over time’”

—Associated Press

Russia and China have long believed that Europe is irrelevant as a world power, because it underfunds its military forces in favor of generous social spending. Social spending has slowed the GDP growth of Europe, and military spending has shriveled, as a % of that

smaller GDP. Social spending has undermined the work ethic, and crowded out investment in future growth, jobs, and wealth. Just as Alan Greenspan predicted.

Our competitors want the same for us. They’re trying to influence our media to weaken our military, tarnish the concept of democracy, exaggerate racism, create divisiveness and despair, and weaken our economy. Russia worked hard to influence our 2016 election. Researchers

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THE ABNORMAL YIELD CURVE

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Short-term interest rates are a LOT higher than long-term rates. Investors keep buying long-term bonds at high prices and low yields. They're gambling that short-term rates will drop like a rock, in a painful recession. The yield on a 10-year U.S. Treasury bond is only 3.7%, at a time when super-safe Treasury Bills yield 5%.

We think the recession will be milder, and that inflation is hard to kill. *"San Diego is giving a series of pay raises totaling nearly 23 percent to more than half its workforce" (San Diego Union Tribune).* Retired Americans just got an 8.7% Social Security increase!!

We also think that the Fed will hold short-term rates near 5% for a year! Today's "inverted" yield curve will prove to be an *abnormal* yield curve. The yield on that 10-year bond will have to rocket higher to get us back to "normal".

If we're right, **bond prices will fall, drastically.** Bond funds will lose value, again. Mortgage rates will soar past 8%. Growth stocks, and the shares of companies that need to borrow, will decline. ■

"It seems the U.S. has a virtually open Southern border yet restricts highly qualified people from immigrating legally. Isn't this backward?"

— Peter Keeble, in a letter to the *Wall Street Journal*.



FROM THE FED

"In 2021 we stated that inflation is transitory. In 2023 we stated that the banking system is resilient and sound. What we *meant* to say is:

Inflation is Resilient and Sound and The Banking System is Transitory.

Please accept our apologies for any confusion."

— A timely statement from the *Federal Department of Regret @ agnostoxxx*

Bigger Better Blunders

Putin's mistake in attacking Ukraine probably altered the course of history. For the better. He reawakened Europeans from their slumber—the kind of slumber that required a stupendous rescue effort by America in World War II—and our own politicians have awakened as well. We are *so very fortunate* that Ukrainians are fighting the battle on behalf of the free world, and we're lucky that Russia proved to be so much weaker than anybody expected.

Just as strange, and strangely fortunate, has been Xi Jinping's inability to recognize that it's in his interest to push hard against Putin's War. His ambassadors compounded the problem with arrogant comments that alarmed neighboring nations and the West. If China was trying to lull all of us into a stupor they've badly blundered. ■

The USS Gerald Ford, our newest aircraft carrier, is powered by two Bechtel nuclear reactors that, according to Engineering.com "could run without stopping to refuel for 20-25 years." The 100,000 ton ship has four propellers, each weighing 30 TONS. They're driven by 350,000 horsepower, which can power the ship "faster than 34 miles an hour" (probably more like 50 miles an hour, but it's a secret).



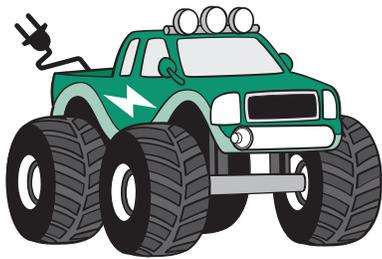
4,500 people live aboard.

U.S. Navy sailors have been living cheek-by-jowl with nuclear reactors for 67 years! We're not afraid of nuclear power, but how would you like to sleep 10 feet from a nuclear reactor for six months, living in a steel tube at the bottom of the sea? The nuclear-powered submarine USS Nautilus first put out to sea in 1955. ■

INVEST NOW!

Most investors will be allowed to contribute \$6,500 to their IRA or Roth IRA accounts in 2023. Those over the age of 50 can contribute \$7,500. This is a terrific time to put funds into any type of investment account, because there should be excellent opportunities to buy in the months ahead.

If you wait to establish the account, you'll find yourself filling out paperwork after the market has already jumped 20%. **Or 30%!** In the stock market good things can happen really fast, but only the brave are able to take advantage. ■



Car buyers often prefer cars and trucks with a high Miles-Per-Gallon rating, but they never see a comparable metric for electric vehicles. They just want to know the battery range. Auto manufacturers have an incentive to make vehicles with huge batteries, and that means very heavy vehicles.

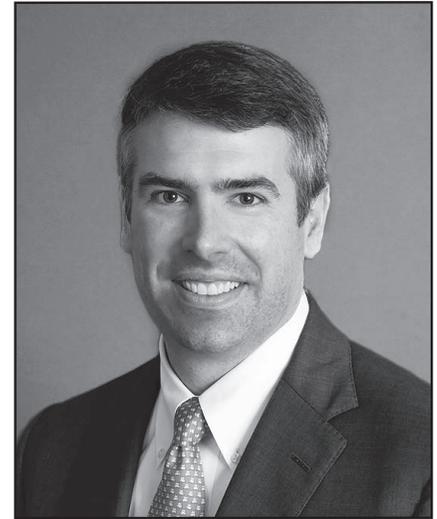
A Honda Accord weighs less than 3,300 pounds, but a Tesla weighs 4,500 pounds, and the electric Ford F-150 Lightning weighs more than 6,000 pounds. American cars and light trucks already weigh 1,000 pounds more than the European average. Expect them to get even heavier. ■

GO GLOBAL

Rising interest rates will make today's investments look less attractive, because better opportunities with bigger returns will become available. And rising inflation will shrink the value of any dollars that you receive in the future from dividends or sale proceeds.

So what can we do? Let's skate to where the puck is going. We can get ahead of the game by seeking out stocks with higher dividends that are selling at bargain prices. Stocks that pay high dividends, and have large enough earnings to pay even more, are likely to hold their value better than expensive growth stocks.

Foreign currencies might hold their value better than the U.S. dollar if massive deficit spending and inflation continue. And there's a world of foreign stocks that can be purchased at better prices than the ones on our shores. According to Vanguard, the Vanguard International High Dividend Fund



Jay Conway, CFA

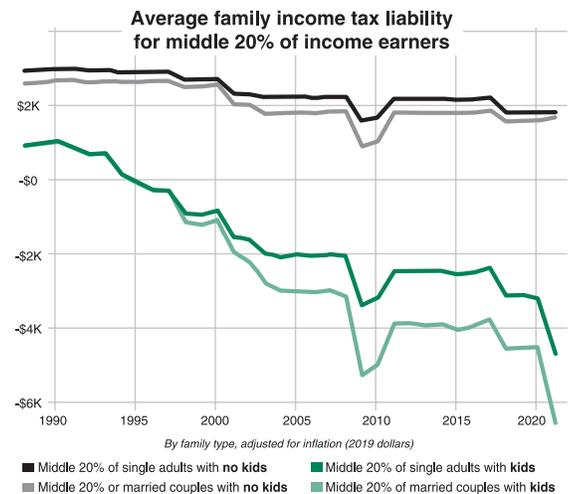
(VYMI) trades at only 8.9x last year's earnings. That's an "earnings yield" of 11.2%!

By comparison the S&P 500 trades at 20x last year's earnings, so it offers just a 5% earnings yield. And a paltry 1.55% dividend yield. Over the past year the dividend yield on VYMI, despite its portfolio of solid names such as Novartis, Roche, Toyota, and Siemens, has been 4.4%. There's plenty of room for big dividend increases in the future. ■

"The 2017 Tax Cuts and Jobs Act reduced the average tax bill by around \$900."

— USA Facts

Middle class families with children used to pay income taxes, and now they receive money from the IRS.



Source: Treasury Department

USA FACTS

UNDER THE INFLUENCE

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from 4 countries, publishing on Nature.com, concluded that they were clumsy and ineffective; but they're still at it. And China is surely more capable.

This is a cheap and easy way for the Red Dragon to control countries that it sees as adversaries. Salaries for 140,000 loyal communists—*1/100th of 1%* of the Chinese population—would be peanuts in comparison with the cost of building the military might needed to seize Taiwan and Guam, and control the western Pacific. Peanuts, if the result is less discussion of Hong Kong, the Uighurs, the Tibetans, and the Falun Gong.**

They're building their military might anyway. China had 100 intercontinental ballistic missiles in 2020, and now has more than 450.

They are winning. It doesn't matter whether their agents, chatbots, and deepfake photo factories are responsible, because the US military is now smaller, kinder, gentler, more politically correct, and less capable. We've reduced military spending as a % of GDP, and done things that slowed the growth of our GDP. Greater social spending has hollowed out the military, increased our nation's debt, and pulled money away from investment in things

that will make our economy larger, stronger, and more competitive with China.

Increased social spending hasn't even made us happier. Tens of millions of our young people are filled with anxiety and a sense of despair. Hundreds of thousands have died of overdoses on drugs that were made with chemicals imported into Mexico from China, and then sold very cheaply in the United States.

Influencers are helping us to redefine rights and needs to include food, clothing, medical care, housing, and transportation. We're now committed to "helping" children, parents, students, their grandparents, and their great-grandparents. Everybody. It's a vote-buying politician's dream!

Shouldn't all those trillions have brought us at least a little bit of peace, love, and good will? ■

LUCKY

If you have good health, and you live in this country, *you are one of the luckiest people in all of world history.* That's true even if you're spectacularly unattractive and you were unjustly jailed for walking on a road in Colorado.

In this **Time of Gloom** it can be hard to remember that. It's hard, even when you're eating exquisitely-delectable food while looking at the coruscating screen of the supercomputer you carry in your pocket. This is an era in which everyone, even rock stars, princes, and Meghan Markle, are competing to prove that they are victims. If you work on your victimhood for just a few days you'll find that you've become monstrously unhappy.

An Attitude of Gratitude Is The Key To Happiness.

Lots of Americans know this to be true. A WSJ/NORC poll of 1,019 adults recently concluded that older people, and women of all ages, were more likely to describe themselves as very happy. The very-happy people don't attach a high importance to money, and most of them—two-thirds of them—described themselves as religious. ■

** *David Kilgour, a former Canadian Secretary of State, is the author of Bloody Harvest: The Killing of Falun Gong for Their Organs.*



THE POST-WORLD-WAR II COLLAPSE

The United States turned back the Nazi tide in World War II by creating an awesome economic engine from the ashes of the Great Depression. According to Ken Burns, the United States produced “297,000 aircraft, 193,000 artillery pieces, 86,000 tanks and two million army trucks”, often incorporating brilliant new technology. After the war the economic situation looked hopeless. Economists were sure that the economy would collapse because we would have scores of factories and shipyards without any orders and therefore no employment.

What really happened is that the economy grew! Soldiers and sailors had saved their wages, and there was a huge pent-up demand for automobiles, homes, and consumer goods that had not been available during the war. The federal government had a huge debt, but paid it off by slashing spending to levels that would seem impossible today.

Many economists believe that government spending is essential to keep our economy growing, and that it's a good idea to increase our debt a little bit every year to help this along. Our post World War II experience shows that the economy can roar even when government spending is shrinking, debt is shrinking, and we are running massive budget surpluses. ■

FREE TRADE?

Protectionism is growing, all ‘round the world, and it’s going to hurt world GDP growth. Standards of living, for rich and poor alike, will advance at a slower pace.

Free trade was a bedrock principle for most of the free world, for decades. World GDP grew and flourished, and billions of people were pulled out of poverty. China was allowed into the World Trade Organization in 2001, but it cheated again and again.

We had to respond, but now we’ve gone too far. Only 16 electric-vehicle models will qualify for \$7,500 (or \$3,750) federal subsidies, and they’re all American made. No European, Japanese, or Korean cars will qualify. Those nations are furious. Retaliation is likely. ■

Indonesia and India are large, fast-growing nations that are benefiting from the exodus of European and American companies from China. They import and export, but that trade is modest in comparison with GDP. The World Bank says that in 2021 exports were 21.4% of GDP for India, and 21.6% of GDP for Indonesia; if that sounds like a lot, you’ll be surprised to learn that the world average is 29% (and the average for the Euro area is 49%).

When the world economy is soft it’s better to be an island. Or a nation of 17,000 islands, or a huge subcontinent surrounded by towering mountains and an ocean.



Drew D. Kellner, CFA

The shares of the Matthews India Fund sell for \$23.50, exactly the price they were at in 2014. That’s very misleading! The fund pays out big capital gains dividends that keep the price in a narrow range, while putting cash in the pockets of investors. This also puts capital gains on the tax returns of investors

Good investment performance causes painful taxation. We feel your pain, but there’s no good way around it! And we find that our efforts to reduce taxation usually hurt performance. It’s better to grin and bear it, or grimace and bare your teeth. ■

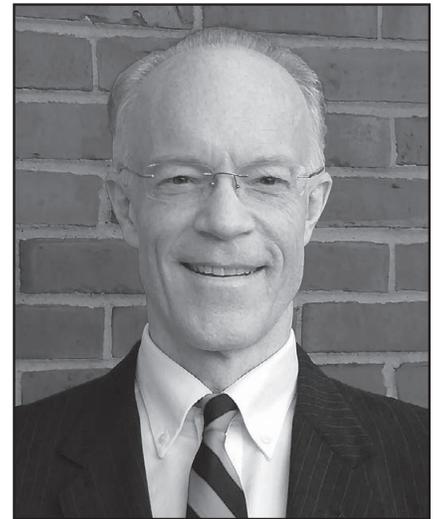


“America’s budget deficit is set to balloon as its population ages, the cost of handouts swells and the government’s interest bill rises. We estimate that deficits could reach around 7% of GDP a year by the end of this decade—shortfalls America has not seen outside of wars and economic slumps. Worryingly, no one has a sensible plan to shrink them.”

“... All told, the picture is forbidding. Take America’s Inflation Reduction Act, which was supposed to reduce deficits. Its green tax credits were forecast to cost \$391 billion over a decade, but are now expected by Goldman Sachs to cost an eye-watering \$1.2 Trillion.”

“... All this makes tax rises inevitable. And more taxation makes it crucial to raise money in ways that are friendly to economic growth... America lacks a value-added tax and China sorely needs its long-promised property tax. Carbon emissions should be taxed sufficiently everywhere, which would also encourage the private sector to invest more in decarbonisation and thereby reduce the need for public spending to that end.”

— *The Economist*



SUBSIDIES FOR THE WEALTHY

You can get a tax credit—a fat check in the mail—for buying a heat pump. Mini splits and other heat pumps might save you a ton of money on heating and air conditioning, so that’s a twofer! But why are we borrowing money and committing generations X, Y, and Z to pay for 30% of the cost, even for wealthy people? *Mostly* wealthy people, because citizens of modest means aren’t likely to leap forward, checkbooks in hand, to pay for the other 70%. The prices of all these things, unsurprisingly, have gone up a lot.

The well-to-do are also getting fat checks for buying electric cars, and putting in thick insulation, new hot-water heaters, wood stoves, and solar panels.

— John Lumbard, CFA

In the United States each of us puts 15.3% of each paycheck into Social Security and Medicare. Your employer puts in half and you put in half; but if you’re self employed you have to put in 15.3%. Any way you look at it, it’s just tax because these funds are NOT set aside to fund your retirement. They’re spent immediately by the Congress, because the “trust funds” lend the money to Congress by purchasing U.S. Treasury bonds. The bonds

in the Social Security trust fund are worthless IOUs, because they are loans *from* our government *to* our government.

In Australia your employer puts in 9.5%, and you add whatever you want to put in. It’s your “Super” account, which allows you to invest in common stocks and mutual funds, just like an American IRA. 20 years from now Australians will be far wealthier than Americans.

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