

The Horsch *Business Report*



Helping you grow your career and your company



LARRY HORSCH

INTRODUCTION

The important news coming out of Washington and Wall Street is of historic importance. We hope to capture the essence of what is happening in this Report.

As always, we look forward to your comments via our website listed below.

THE ECONOMY

Overview

As of this writing, President Biden's \$1.9 trillion coronavirus relief package has passed the House, but it appears they will try to pass it in the Senate without Republican support. This means that some of the money is going to citizens who don't really need it, running up the national debt needlessly. This amount of spending will jumpstart the economy as the COVID-19 virus comes under control. Putting these two factors together means a stronger fourth quarter this year than originally estimated, and, hopefully, a more normal 2022.

Inflation, as noted elsewhere in this Report, is once more becoming an issue with such large deficit spending, but the Federal Reserve still will accommodate the recovery until the job market becomes healthier.

It is encouraging to see more vaccine production and distribution to get the country fully vaccinated. The recent Johnson & Johnson addition will be helpful, with other companies adding vaccines in the future.

WASHINGTON SCENE

The Fight for Control of the Republican Party

We believe that most of us would like a healthy two-party system in the United States. At the moment, though, the Republican Party is at war with itself.

As President Trump departed Washington for Mar-A-Lago, he took with him a big pot of money to be used for political purposes. Surveys show that Republicans support him at the 90% level. At the recent CPAC meeting, he identified those he expects to defeat in the Republican Party in the 2022 election.

Trump antics in office, particularly his role in the 1/6/21 attack on the Capitol, are causing traditional Republicans to leave the Party. Recent polls suggest that the Republican Party has slipped from 29% to 25% of all voters.

Rebuilding the Republican Party won't be easy with a significant percentage of Republicans believing Trump's wild idea that the 2020 election was rigged and that he won all states by substantial margins. At this point, we are looking at a Trump version of the Republican Party that increasingly appears to be a cult. (In a cult the leader sets all the rules and anyone breaking the rules is ostracized. There is no exchange of ideas.)

In a recent interview with a TV news reporter, Thomas Friedman of the NY Times was asked if he could see a common thread that connected the various groups that stormed the Capitol on 1/6/2021. He responded that those involved:

- Had historically no power and they enjoyed getting power
- Generally, had not been successful financially and are frustrated and angry
- Were mostly men who had not experienced the hand of a good woman

It is possible that the traditional Republican

Party may have to form a third party, as awkward and complicated as it may be. It would split the conservative vote and give the liberals greater power in the short term.

The big outside factor affecting all of this is Trump's legal outlook. He is being charged in various courts with sexual harassment / rape, interfering with elections, and running a criminal business inside the Trump organization. The legal problems, along with growing financial difficulties in his business, could require an increasing amount of his attention. While going to jail for interfering with an election may make him a martyr in the minds of his followers, being found guilty of the other charges would diminish his stature generally.

For the traditional Republican Party to gain traction, it needs to rally around a new leader. While Mitch McConnell may be regarded as a candidate, his age and history of saying "no" to most ideas won't help his cause. Somewhere in the pack of seven or eight Republicans in Congress who have challenged Trump and John Kasich (former governor of Ohio) there will be an answer.

Place your bet on those who won't support outrageous tales like Trump's promoting the rigged election. We've all been told from childhood that if you don't tell the truth, people won't trust you and you'll have few friends. That fundamental guidance still applies today.

President Biden's Activities

As suggested in earlier Reports, President Biden is picking the low-hanging fruit in rejoining the Paris Climate Accord, the Iranian agreement to stop Iranian nuclear power, the World Health Organization, and has made overtures for more cooperation with NATO and America's traditional allies.

In engaging FEMA and National Guard units to assist in COVID-19 vaccinations, he is moving us closer to a solution and in the process

accelerating an economic recovery.

His \$1.9T recovery funding has passed the House and may need to be trimmed in the Senate to pass. Unfortunately, the bond market is already reacting to possible future inflation caused by such large deficits, which can have a negative impact on an overpriced stock market.

Whether he can convert his theory of bipartisanship into action in the near term remains to be seen. It obviously is very important in getting broad support for future legislation.

Biden's initial thinking of taxing capital gains as we tax ordinary income to help pay for all the extra spending is a mistake. He is failing to appreciate the risk-taking needed to create capital gains, which is central to innovation and a better standard of living for all Americans (more on this in the next Report¹).

MANAGEMENT

Overview

The concept of delegation is being broadened by employees working at home and communication by Zoom rather than in-person meetings. This will be a good idea if the employer is satisfied that the employees are getting their work done as expected. There are substantial savings for the employer to reduce its rental of expensive office buildings and centralized meetings. There are some time and money savings for the employee for not spending on traveling for work.

Creativity

In earlier Reports, we noted that employee's creativity is at its peak in the morning hours. If you can convert driving time to creative time by working at home, this is not a small matter, particularly at the upper management level and in departments relying on significant creativity to move the organization forward.

At the upper management level, problems arrive at the manager's desk that have not been solved by others. The key to solving these problems often involves allowing the creative side of the brain to take over. Many top executives do not return emails or phone calls in the early morning hours, which allows them time to work on problems in a quiet setting.

INVESTING

Overview

There has been one big item missing in the investment discussions in the last year as interest rates have plummeted, especially for US government bonds. For valuing US stocks in the long run, fundamental analysts have been trained to develop a forecast for a company's earnings five to 10 years in the future and discount the result using a government bond rate to arrive at a present value. They then compare the present value to the price of the stock at the moment to determine if it is a good value or not.

In the process of doing the above, very few have put "guardrails" around the use of the government bond rate to avoid extreme answers on the question of value. "Guardrails" are the selection of maximum and minimum government bond rate in calculating present value. If a minimum rate of 3% is used as a "guardrail", with current bond rates below 1.5% (6% as a maximum rate), you get valuation answers that overvalue stocks. As an investor you get whipsawed when government bonds go to more normal levels. This is exactly what is happening today.²

Market Manipulation

We are witnessing the final stages of the crazy speculative event carried out by amateur investors promoting the price rise of a company that often has very average results in order to make a quick profit. A little history:

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- In 1929 the stock market crash was caused partially by a few sophisticated investors “cornering the market” in a few stocks to drive up the stock prices and later dump them on unsuspecting smaller investors since there were no laws to prevent it.
 - In the early 1930s, the SEC was formed to prevent this practice, and Joseph Kennedy (John F. Kennedy’s father) was chosen to head the SEC, since FDR thought it took a “wily speculator to catch a wily speculator.” Once the law was passed, market manipulation was illegal.
 - Today, with the aid of social media, thousands of small investors are ganging up on a company stock to push it upward and make a quick profit. While it is more complex to track violators in such large numbers, it is extremely easy to prove guilt by obtaining social media evidence. This is simply market manipulation and it is illegal.
 - All the “little guys versus the 1%” with a Robin Hood focus is nonsense, just as mobs storming the Capitol believing they are patriots is nonsense. They will all have a sufficient time to reflect on this when they are in jail.
 - Politicians who want Congress to stand up to protect small investors simply don’t understand market manipulation.
 - The SEC has been slow to move on this. The law is very clear.

PARTING SHOT

With a few glitches in manufacturing the COVID-19 vaccine and a lot of glitches in distributing it, the process of getting us immune to the virus is moving the economic recovery from the third quarter to the fourth quarter of 2021. Much will depend on how the current variants of the COVID-19 virus can be handled by today’s vaccines.

There is a light at the end of the tunnel, but the tunnel is longer than forecasted.

Respectfully submitted,



Larry Horsch
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¹ As a professional manager of investments in most of his career, the author has substantial experience in addressing this topic, particularly high-risk projects.

² Warren Buffett, one of the godfathers of long-term fundamental investing, uses “guardrails” to avoid this problem.