

The Horsch *Business Report*



Helping you grow your career, company, and economic wellbeing



LARRY HORSCH

INTRODUCTION

We continue to have historic events happening before our eyes in U.S. stock market volatility, historic inflation, rising interest rates, and the Ukrainian-Russian War.

We stated in our Interim *Report* dated June 1, 2022, that gun rights were restricted by the Constitution to government-appointed militias. We stand corrected in that the Supreme Court has ruled that individuals have the right to bear arms.

As always, we request you call your friends about the *Report* who might find it helpful. Our website is listed below for those who would like to view the *Report* online. For printed copies send an email to Larry@HorschReport.com.

THE ECONOMY

Overview

The U.S. and European economies are slowing with continuing supply chain issues, high inflation, and low consumer confidence in the U.S. In Europe, the Ukrainian-Russian War is very unsettling generally.

The Federal Reserve, by raising rates by three-quarters of a percentage point, shows determination to address the 40-year high inflation. Unfortunately, the discussions about a soft economic landing after the Fed moves are really just a faint hope, with growing odds of a recession in late 2022 or 2023.

While it may seem discouraging to discuss a recession in the medium term, let's remember

that business cycles, both up and down, are part of the free-enterprise system, which has built America's high standard of living versus the world's standard of living.

WASHINGTON SCENE

The Trump Situation

Donald Trump has three major legal issues facing him:

- The January 6 House Select Committee is now revealing fairly compelling testimony that could put him in a position of being a conspirator or a co-conspirator of causing the January 6 attack, which could either put him in prison and/or bar him from holding Federal office.
- The Secretary of State in Georgia has a recording of Trump asking him to create the exact number of votes needed for him to win in Georgia. If proven, this is interfering with a national election.
- Two New York governmental groups are sponsoring different inquiries about Trump and his family overstating their financial assets to obtain large bank loans and other benefits. Here, we believe that prosecutors are on shaky ground in the bank loan area because banks have experts who know as much or more about commercial real estate values as the Trump family and are not influenced by a super salesman's approach to valuations.

If the sedition charge is proven, then the Republican Party will be looking for a new leader for the 2024 election (oddly enough, the Democratic Party may also be looking for a new leader for the 2024 election, with President Biden's age and low poll ratings.)

An Insight to Courage

Representative Kinzinger of Illinois, who is a Republican on the January 6 House Select Committee and has chosen not to rerun in the

fall because his district was jerrymandered, noted something special as he introduced a hearing on the January 6 event. He shared the following observation (paraphrased): "As a veteran of the Afghanistan War, I realized fully what it meant as a member of the U.S. military to put one's life on the line to defend the U.S. Constitution. I would encourage my Republican colleagues to realize they are not risking much as perceived by the citizens of this country to put their jobs on the line for the sake of defending the U.S. Constitution as we study the attempt to overthrow the Federal Government." (You may have to be a veteran to fully appreciate these thoughts.)

Federally Funded School Debt

As the Federal Government loans to students has reached about \$1.6 trillion, the Biden administration is considering forgiving some of this (they have already forgiven an amount where the educational institution's activities were considered fraudulent). Trial balloons have been floated, but some legal scholars doubt the President has the power to forgive any debt by himself.

All this mess could have been avoided by modeling the student loan program after part of the Small Business Administration loan program, which involves the originator of the loan, a local bank, which analyzes the requests, and, if approved, the bank invests in 10% of the loans. We skipped all of that in the student loan program and allowed colleges / universities and students to forward the loan requests with no analysis and receive a check on behalf of the student for enrollment. Most importantly, there is no analysis of the student's major field of study involved nor any analysis of the possible income that could be generated from a job in that field in order to pay back the loan. Nowhere in the civilized world do people borrow money on this basis.

ELSEWHERE

College Enrollment

Statistics are now being reviewed that indicate lower-level colleges and universities have lost significant enrollment in the past decade. In some cases, tenured faculty are being fired and course offerings eliminated due to limited enrollment. After decades of growth in enrollment at colleges/universities in the U.S. supported by massive Federal lending programs, cited earlier, the country is coming to grips with the reality that many students with marginal scholastic performance in high school shouldn't attempt to go to a four-year institution only to drop out and be liable for a large federal loan. A strong economy has highlighted the fact that jobs such as plumbers, carpenters, electricians, etc. can create a decent standard of living without going into debt. More students coming out of high school and their parents are becoming aware of this. In tracking back college tuition at a private local college, we learn that tuition has been growing at 8% per year over 50 years, which is substantially beyond the general U.S. inflation rate.

While it is painful for these colleges / universities to adjust to this new reality, we simply say welcome to the real world.

MANAGEMENT

Overview

The big ongoing challenge for business management in the U.S. is to determine what is the right combination of working in the office versus in the home. The risk is that the wrong combination will increase turnover of current employees and reduce the effectiveness of recruiting new employees. Having had substantial exposure to working from home after two years of COVID issues, many employees will not be easily talked out

of the simplicity and reduced expense of working from home. At the moment these two ideas are essentially involved in a grand experiment that will be refined over time.

Breaking Up Larger Businesses

Recently, the Kellogg Company announced breaking up its \$14 billion business into three parts: breakfast cereals, snacks, and plant-based products. Naturally, the CEO of Kellogg chose to lead the largest and fastest growing part of the business – snacks.

Conglomerates functioning in many industries had fallen out of favor on Wall Street many years ago. The exceptions that are distinguished as conglomerates were Berkshire Hathaway under Warren Buffett and Teledyne under Dr. Henry Singleton. It is less common for a one-business multi-brand industry company to break up and take advantage of the greater dedication of employees to a more focused company created in a breakup.

It is very difficult for a CEO of a multi-industry or multi-sector company to generate employee enthusiasm across multiple industries or sectors. Employees simply have little interest in other parts of the business. In addition, it breaks the company into different pieces to add incentives in equity form that relates directly to what the employees are working on. We doubt the employees in Kellogg's breakfast cereals care much about what is happening in the plants-based business, yet any equity incentives historically have been based on all of these product areas in a one company setting.

The China Issue

We are reaching a point where most U.S. corporations operating in China or importing from China are reassessing their current position since China is moving from an international competitor to a political enemy of the U.S. China is causing havoc in the

South China Sea and is conducting continuous air exercises in a threatening fashion near Taiwan. It increasingly appears to be a rogue nation.

While our attention at the moment internationally is focused heavily on the Ukrainian-Russian War, let's be clear that the larger long-term threat to liberty is not Russia, but China with economic power many times that of Russia.

Overall, American businesses will need to find new sources of goods and markets elsewhere in southeast Asia.

INVESTING

Overview

As we enter the final stages of the stock market decline in the U.S., extreme speculative activities are being crushed.

We cited this book once before, but a review of the book *Extraordinary Popular Delusions and the Madness of Crowds* by Charles Mackay, which was originally published in 1841 and updated in 1932 and 2018, is a great study in gross speculation over the years always leading to a later collapse. It would seem that it is a dream for many who think they can invest in things they know little about and in the process, they could eliminate the need for ordinary hard work.

Is it Knowable?

Warren Buffett has often challenged investment analysts attempts to forecast something which is too difficult to address (example: do we know if the Dow Jones Industrials in 10 days will go up 2.5%?). He prefers to work on things where his talents can be applied with likely successful outcomes.

In recent years many of the short-term traders are engaging in activities that are essentially unknowable, which, unfortunately, they have learned the hard way.

Value Investing

We are seeing a return to value investing, which is based on investors focusing on what they are getting from an investment (income and capital appreciation), rather than focusing on what is going up in price, regardless of what continuing value they receive from the investment.

During the long series of bull markets since the Great Recession, over 10 years ago, we've drifted away from value investing and are currently rediscovering it. Most of us trained in economics, accounting, and management of companies obviously prefer to invest in things we understand and that represent good value for the investor.

After a long drought, value investing is being led by Warren Buffett of Berkshire Hathaway and others onto the center stage. If the U.S. stock market continues downward, we will all hear more about value investing.

PARTING SHOT

President Zelenskyy of Ukraine has displayed unusual courage and leadership in leading his country's efforts to fend off a Russian invasion. Some would liken him to Winston Churchill in the early part of WW II. In a world full of politicians without much courage, it is inspiring to see this type of leadership.

Might we all aspire to such leadership if we were to face a similar challenge.

Happy 4th of July!

Respectfully submitted,



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