StraightTalk
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"Live, From New York, It's…"

No, it's not Saturday Night Live, and it was not New York. It was Orlando, and the first live, in-person Raymond James conference in over two years!

Aside from the obvious pent up demand to get together with other like-minded advisors and friends, I was excited for the networking and sharing of ideas. As always, the five hundred or so of us that attended the conference enjoyed sessions with thought leaders from inside and outside of the firm on topics ranging from asset management and technology, to practice management and the politics in Washington, DC.

Of course, the pandemic and the global governmental response to it was also a topic, with the consensus being that the world population will not tolerate going through another lockdown. The investment managers that have rolodexes full of biotech and big pharma executives were uniformly confident that, while not vaccinated to the level that we should be, our country has reached herd immunity. The idea that we will end Covid is not realistic, instead, the historic pattern of pandemics is that they become endemic, and we learn to live with variants and breakouts in the same way we live with the flu each year.

Speaking of learning to live with (or adapt to) a changed world, the great corporations of America have finished one of the most explosive twelve months of earnings growth in half a century. The ability to pivot, utilize technology, work remotely, and respond to the demands of a changed workforce and customer meant the sharpest recovery from recession on record. One fact related to that stood out – today's level of cash held by the S&P 500 companies would, if it were an economy, rank number eight in the world! I cannot recall a time in my career when companies were as well-capitalized as they are today. The historic high levels of corporate cash, combined with the historic low rate of interest on their debt puts most of these companies on extremely solid footing, which bodes well for the long run.

Speaking of the long run, I had the distinct privilege of hearing Dr. Jeremy Siegel, Ph.D., Professor of Finance at the Wharton Business School, and author of the bestselling book, "Stocks for the Long Run" in his sold-out session. (I also had a proud dad moment when my daughter Grace, a business major at USC, was able to join me to hear him speak!)

Dr. Siegel pointed out a number of important technical trends – the most meaningful of which was the current inflationary trend, and he predicted accurately that the Federal Reserve would need to speed up their withdrawal of support and rate hike timelines. The lag between the spike in money supply (what economists call M1 and M2) and inflation has been 12-24 months throughout history. In plain English, this means he was expecting inflation to remain an issue through early 2024 before beginning to subside. His expectation of the total increase in prices over the next few years was 20-25%, which is significantly more than the rate of increase during the last two decades, but also significantly less than the 150% increase during the late 1970s and early 1980s inflationary period.

He also pointed out a couple of important correlations between inflation and stock market performance throughout history. The first of which is that *inflation has not been bad for stocks*. The simple economic reality is that most companies can pass on most kinds of cost increases to the end consumer, thus protecting their profit margins. While that may not feel good to the consumer at the cash register, as owners of these companies, we do not want them to give up profits by keeping prices flat in a rising cost world. Instead, we expect them to control costs as they can, and use their pricing power to maintain profitability. One of those costs (labor) is currently going up because of the changing nature of work after the virus. However, another of those costs (interest on debt) is at all-time lows, also because of the pandemic. Dr. Siegel's

expectation was that stock returns in the near future will be a bit lower than the long-term average, but twice as good when compared to returns from bonds.

His math was pretty simple – with prices, earnings, and interest rates where they are today, his expectation is for stocks to return 4.5% per year *after inflation*. That is less than the long-term annual average of 6.8% *after inflation.* However, the difference between stocks and bonds has averaged between three and four percentage points (again, after inflation) over the last two centuries. With bonds paying what they do today, and inflation where it is, bond yields *after inflation* are expected to be negative 4%. This is more than 8% less per year than stocks for the near future!

Aside from Dr. Siegel, I was also able to hear another standing-room-only speaker, the Chief Equity Strategist at Federated Hermes, Phil Orlando. Phil is an accomplished speaker, who is also not afraid to make a prediction and stand by it. His first prediction was 4,600 on the S&P 500 by the end of this year, followed by 5,300 at the end of next year.

His other predictions ranged from Fed Chair Jerome Powell being re-appointed, Lael Brainard being appointed Vice Chair, and the three remaining open seats being filled by President Biden early next year, to Christmas spending being up 10% this year, almost triple the normal seasonal increase. He also pointed out that the largest political party in America today is now those that identify as “independents.” That block makes up 36% of voters, with the Democrats and Republicans both at 31.5%. This has profound implications in policymaking, and for the mid-term elections. His political prediction was that the Republicans will win the House next year, and the Democrats will keep their Senate majority.

Mr. Orlando’s comment on taxation also caught my ear – the most recent data from the IRS is from 2018, and it shows the divergence on income, and income taxes. The rich are indeed getting richer, and at a faster rate than any time in the last century. However, the share of income taxes paid by that group is also growing to all-time highs. The top 1% of working Americans now pay an astounding 40% of all Federal income tax dollars collected, and the top 10% pay 71% of all income taxes. This leaves 50% of all working Americans paying only 3% of income taxes collected. He pointed out that many other taxes, like sales and property taxes, hit the bottom half of working Americans proportionately harder, and that we desperately need a better tax collecting system. He also predicted this was not likely to happen!

Another session I enjoyed enormously was on disruptive technology. Our Chief Information Officer highlighted our own cyber security efforts, pointing out that 2 million emails each day are picked off from their intended recipient. This staggering amount, which is 75% of our daily email traffic, is flagged and diverted using artificial intelligence (A.I.) because those emails contain malware, spyware, or some other harmful element. Raymond James is also now using 75 robots in our back office, and there is now a test pilot program using Google glasses to make zoom meetings much closer to feeling like being in the same room.

I also heard from a growth fund portfolio manager on the ever-increasing pace of innovation in technology. He listed two specific examples that, in the theme of combatting the negative news narrative of the day, I thought were worth sharing. The first was that Gregor Mendel initially defined the laws of genetics in 1865. Then, 88 long years later, Watson and Crick discovered the double helix DNA structure. Another 37 years later, the human genome project was launched, and just 13 years after that, the human genome sequence was completed. In other words, science and technology are not just improving – they are speeding up. In addition, the sequencing cost per genome back in 2003 was $90 million each, while today it is just $689.

Cloud computing was the second example. He pointed out that the “cloud” was formed in 1997, and two decades after formation, cloud services spending hit $117 billion annually. It was projected then, that just four years later (in 2021) cloud spending would grow by another $80 billion. That actual spending number more than doubled to over $312 billion this year.

My takeaway? Things are good, and getting better. And getting better faster. Remember that good news takes awhile to see, and that bad news is more provocative, but fleeting. Our future remains bright…

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