



## Something to Think About

A couple of weeks ago, we raised a little cash in the vast majority of our client accounts. In the grand scheme of things, it was relatively minor across the board. While we would ordinarily send out an email detailing our actions, we didn't this time as we didn't want anyone to misprocess our actions as "the sky is falling." Thus far, the trade has been mostly a wash in terms of overall portfolio performance.

Currently, the general consensus of our investment team is we would be more inclined to reduce our overall allocation to equities than add to it, at least in the short-term. However, no one believes a massive correction is imminent either. The reason is pretty simple: the economy appears poised for continued moderate/mediocre growth. This should provide a base, of sorts, for corporate earnings. As long as this remains in place, another 2008 or even 2002, which is what most investors fear, isn't terribly likely outside of a major, global conflagration.

Even so, in order for the markets to have another strong leg up, two things must happen: 1) 1Q 2017 reported earnings have to come close to or exceed some pretty lofty expectations, and; 2) at some point in the not so distant future, Washington HAS to start addressing and/or tackling some measure of meaningful tax reform. I am not sure which is more important than the other, as they are both critical.

First things first, it is too early in the 1Q earnings season to make a clear determination, but initial observations suggest things are at least okay. Tax reform? As I type, I am not clear on where that stands other than the somewhat vague promises about 'later this year' and 'not before August or September.' Perhaps I have missed a story with specifics or didn't get the meeting invite from the White House; I don't know which.

With the stock market waiting on pins & needles for these good things to happen, stuff like dropping the 'mother of all bombs,' sending warships across the Pacific, and lobbing Tomahawk missiles at bad guys has distracted investors, um, a little. Throw in not calling out China for currency manipulation, which is exactly what pegging the yuan against the dollar is, and it would be curious IF the markets were still as ebullient as they were to start the year.

Hey, I am not casting aspersions at the Administration and/or these individual actions, as I am less political than many people may believe. I am just waiting for the train to leave the dern station on the promised, meaningful pro-growth agenda. In my opinion, in case you couldn't guess, the chief item on said agenda is and should be significant tax reform....specifically a sharp reduction in corporate tax rates.

I guess I want to get sick of winning, or something, and I ain't yet. Admittedly, we are still early in the game.

Closer to home, even the folks at the New York Times noticed Robert Bentley, the former Governor of Alabama, resigned this week in the face of an ongoing scandal. In case you missed it, the press had taken to calling him the 'Luv Guv' due to his purported affair with a staffer and his attempts to conceal it. I use the word purported as I mercifully wasn't witness to any of it.

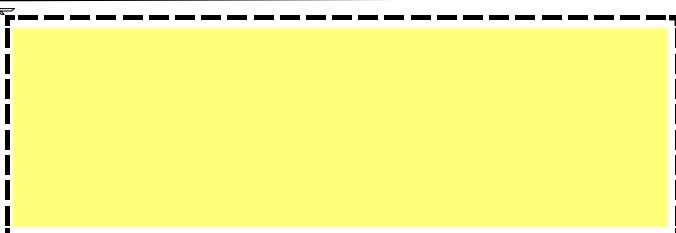
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In the long history of rulers and politicians, Robert Bentley certainly wasn't the first to act, shall we say, inappropriately in this manner. Let's just say there have been any number of veritable Casanovas in the halls of power. However, it seems the populace and press are far more forgiving of such behavior when the leader in question is, in fact, a leader. FDR is a good example. If not that, well, folks seem to turn a more blind eye when things are pretty good economically. When neither of these are present, I think you get the picture.

*The next section of this article might be something of a bore for folks not from Alabama. However, it has merit because any state could be next.*

For years, I have maintained the highest and best use of any Governor is to be the state's top salesperson. Every primary aspect of their job requires an ability to sell, whether it be getting an agenda through the legislature or attracting outside business and direct investment. Finally, they have to sell themselves to the electorate, and to do so they have to be both memorable and likable.

In the early fall of 2010, I followed Robert Bentley in speaking at a conference in Prattville. In fact, the organizers gave the former Governor my allotted time slot due to his supposedly busy campaign schedule. At the time, he was the Republican gubernatorial candidate, although still relatively unknown, and folks were very anxious to hear him speak.

I will be charitable and say his remarks were amazingly underwhelming, and mind numbingly so. This to the point of the audience's complete and utter stupefaction, and, yes, I am being magnanimous. Let's just say, after hearing him I wasn't holding my breath anticipating great and wondrous things.

If the proof of the pudding is in its eating, it would seem the population's economic well-being would be a decent benchmark for a state's top official. Admittedly, individual politicians get too much credit for the good times and too much blame for the bad. However, we seem to remember politicians for their ability to deliver prosperity, whether it is fair to do so or not.

So, how have we done in Alabama since 2010?

From the information I found on the St. Louis Federal Reserve's website, the Bureau of Economic Analysis (BEA) estimated per capita income in Alabama was \$34,073 in 2010. This was 84.6% of the national average, and good enough to rank us 40th out of the 50 states. For the previous decade, Alabama had been bouncing around between 40th and 42nd, so this was about on par with recent performance.

According to the BEA, the state's per capita income had increased to \$39,231 in 2016, which is better than a sharp stick to the eye, as most things are. In fact, it represented a 15.14% increase. That is good, right? Well, the official inflation gauges were up a little over 10% during this time, so mediocre is probably a better word in an absolute sense.

Unfortunately, that rate of growth was the lowest of the 50 states, and Alabama's ranking fell from 40th to 46th as a result. While there is a bit of a logjam between 43rd and 47th place, officially only Idaho, New Mexico, West Virginia, and Mississippi are below us in this regard. For grins, our friends to the immediate west saw their per capita income increase 16.74% over the same time frame.

Basically, even Mississippi did better than we did while Robert Bentley was Governor. What's more, this measure grew at the slowest rate in the country, and we dropped 6 places in the rankings. If that ain't enough, our per capita income fell to 79.1% of the national average. Two words: not good.

Clearly, not all of this economic underperformance was Bentley's doing, maybe any, but it happened on his watch. As such, he has to shoulder some of the blame, if not all of it. However, as surprising as his private behavior might have been for many, did anyone really believe he was a charismatic leader? Someone that gets others to do their bidding and have them believe it is their idea? To lead them out of a foxhole?

Truthfully, Robert Bentley was Governor for one primary reason: he wasn't a Democrat in a heavily Republican state. For those of you outside Alabama, at this point in time, the Democratic Party is to our state what the Republican Party is to California or Massachusetts. If he won the Republican primary, Alfred E. Neuman (of MAD magazine fame) would

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be Governor of our state. Now, how Bentley won the GOP primary is still kind of a mystery to me, and probably best left that way.

This has a point. At some point, the markets will want the Administration to start closing some ‘business’ deals. Perhaps investors (myself included) are expecting too much and too quickly, no argument.

Regardless, we are walking a pretty fine line between ennui and ebullience in the markets. As I have written here previously, it would be pretty usual to see significant multiple expansion during a Fed tightening cycle, particularly without some meaningful changes in how we conduct business. Hey, nothing is impossible, I am just saying the odds are against a sudden, sustained economic (and profits) boom when the Fed is raising rates, all other things being equal.

Put another way: without changes to the accounting and/or rules playbook(s), you likely won’t see a sharp spike in corporate profitability when the Fed is making variable rate debt more expensive.

Whew.

In the end, yeah, we raised a little cash a couple of weeks ago, and will probably raise a little more in another couple weeks if we don’t feel Washington is making meaningful progress on a pro-growth agenda....in short order. I am not talking about continued assurances and Tweets. Basically, I don’t want them to START addressing tax reform in August or September. I want it done by then, and it is okay for the powers that be to stay past quitting time AND to drop their pet projects to make it so. It is that important to overall wealth creation in the country over the next, roughly 19 months, if not longer.

19 months? Yeah, that will take us to the first part of November 2018.

## *Disclosure*

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