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Explaining 2019: getting lucky . . . or earning it.

There is one day left in 2019, and the market has returned about 31%. That makes it a pretty spectacular year, according to most of the investment world. It also makes 2020 pretty dangerous, according to the same world. The usual waves of 2020 Forecasts are upon us, along with the usual waves of 2019 Explanations. Not all, but most of these Forecasts and Explanations are very much alike. They amount to:

2019 Explanation: "We Got Lucky!"

2020 Forecast: "Look Out Below! (And Don't Say We Didn't Warn You.)"

Of course each story carries a more dignified headline than those, and plenty of high-sounding analysis underneath. And that brings us straight to the $64,000 Question, today: "How on earth does a normal investor—who over the years has been much too busy with non-investment career, family, and the general business of life to learn how to see the holes in all the "We Got Lucky!" and "Look Out Below!" commentaries—figure out what to do?" When, for example, she hears her investment manager saying something profoundly different than "We Got Lucky!" and "Look Out Below!", how does she decide who to trust?

The answer, of course, is the same as with all kinds of tough decisions in life, when we have to choose which fork in some road to take, and we have to make the choice with less-than-perfect knowledge of the pros and cons. Yup, we use some cross between our life experiences, our basic understanding of the subject, and our gut instincts. And even though we at Outlook, for example, have been studying the investment world for 42 years or so . . . in the end we do the same thing.

We think the "We Got Lucky!" explanation of 2019 is nonsense. That explanation goes something like this:

- "Driven mostly by 3 straight interest-rate cuts by the Fed, stocks surged in the second half of the year, with the markets hitting a series of record highs and investors enjoying one of their best years this decade."

- "The Tech Sector has benefited most from the buying frenzy, surging 48% and providing the leadership the market needed to overcome the Trade War. Yet half of that stunning gain came from only 2 companies—Apple and Microsoft—which is a warning for 2020."

- "The corporate tax cuts gave one last boost to earnings."

- "The trillion-dollar federal deficit unleashed a wave of government spending which kept the economy going."

Notice the common theme? We owe it all to external forces, without one word about what America's companies might have done all by themselves, to possibly justify the "buying frenzy." Why not? Here it gets profound. Because different people see the world completely differently. Most of the wave of experts writing those "We Got Lucky!" explanations of 2019 really believe the only things that matter are

"Big Trends," or "External Forces." Why? We can only guess it's because most of them have spent their careers not "in the arena" (in Teddy Roosevelt's immortal words), overcoming real-world obstacles bit by bit and building real-world roads to the future one brick at a time—but as expert critics rendering opinions about what's happening in Main Street's arena, without ever being there in person.

Let's shine a light on Outlook's "profoundly different" view of how things work, with just one picture: of Microsoft, since the "External Forces" folks brought it up first.

Microsoft in the Arena: Stock Price (blue); Dividends (orange); Earnings (red)

That is a long-term picture. That green circle might be called "Microsoft Struggling Through the Swamp." It lasted for 8 years or so. It took much of that time for the company to build a new road to the future, having been left at a dead-end, more or less, by Mr. Gates and Mr. Ballmer—the founders. All kinds of "Big Trends" and "External Forces" were rampaging through the economy and investment world through those years—from zero interest rates to giant government spending—but they didn't fix Microsoft's problems, or lay a single brick on its road to the future. And as we might expect when a company spends 8 years in the swamp, nobody in the investment world—truly *nobody*—thought Microsoft actually might build a promising road to the future. It was an aging elephant and unlike the long-ago legend of IBM, it wouldn't dance again.

But it did . . . as the green "skyrocket" arrow illuminates. With a new CEO the company changed itself, using its strengths to create cloud and many other services for corporate America which were hardly imagined by Mr. Gates. It did not matter what the Federal Reserve was doing; how big federal spending might be; or even what the whole U.S. and world economies were doing. The U.S. economy, of course, was growing steadily from 2009 to 2016—and the rest of the world grew too, though mostly more slowly. It didn't help Microsoft much, during its Swamp Years. What helped Microsoft was its payoff from

those years of struggle: outstanding new products and services, which a tidal wave of businesses felt they needed to buy.

Hence the picture above: 400% to 500% growth in profits, dividends and stock price, mostly in the past 4 to 5 years.

"We Got Lucky!" in 2019, say the press and crowds of expert commentators. "Nope," says Outlook. "We earned it as investors, because our companies earned it as operating businesses." Not all of them were as spectacularly successful as Microsoft . . . but many of them have done even better than Microsoft at climbing out of their swamps, and many of them have every bit as much potential as Microsoft's green skyrocket arrow, when it comes to their business performance and their stock returns in the several years ahead.

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