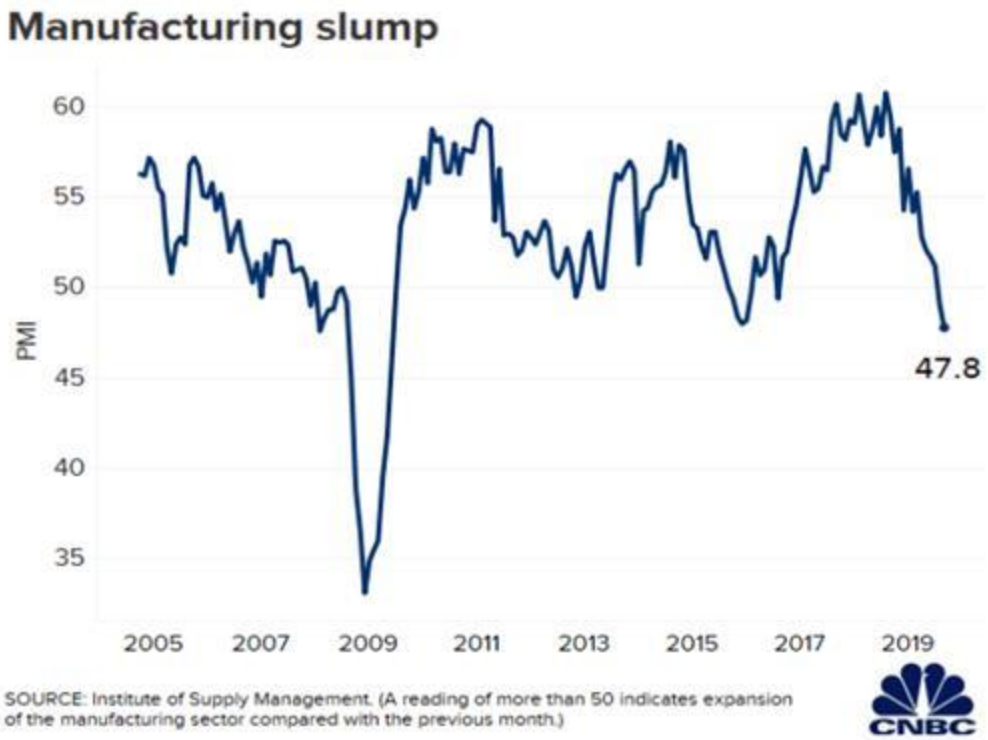
The Outlook: Oct. 22, 2019

Quarterly Earnings Season, and the difference between hurricanes and thunderstorms.

It is very easy to feel, these days, that the investment world's sky is shaking up there, ready to fall on us any day—and the only thing propping it up is the hope that a bunch of politicians around the world will save us by "getting it right" on the Trade Deal, on Brexit, and on boosting Europe's feeble, tottering economy. If that were actually true—if our lives, honor and sacred fortunes were indeed in the politicians' hands—there would be only one right thing to do: sell, yesterday.

It's not true, thank goodness. Our fortunes lie, as always, in Main Street's hands: in the sheer drive of CEO's determined to keep making money and passing out cash to their shareholders, no matter what kind of problems stand in the way; and in the inventiveness of their engineers and researchers, and the likelihood they'll keep producing both minor and major miracles of new technology. That's where our fortunes lie . . . but nobody can blame us for feeling nothing matters except Berlin, Beijing and Washington D.C., given the daily tidal waves of media blather about those political issues.

One of Main Street's burdens—in addition to keeping its nose to the grindstones of management and invention—is all that blather. Wall Street lives and breathes the daily blather, making its living on it; but Main Street can't help but notice it, and be affected by it to some degree, if the media tidal waves are big and strong enough. That's largely why the world actually has seen a slowdown in economic activity over the past year or so. Those politics have been dramatic enough to bother anyone, and when we're bothered or worried enough by any future risk—no matter how vague—we naturally ease up on the gas pedal a bit, until the coast looks more clear. The chart below captures this effect very well.



It's the “ISM Index:” a monthly survey of U.S. manufacturing companies, which asks whether business seems to be going up or down. If the reading is below 50 (like that recent 47.8) it means “down.” Above 50 means “up.” There are ISM charts all over the world showing the same thing since last spring and summer. Germany’s surveys have been particularly depressed; China’s have been “up” but less “up” than ever (which really means “down” as far as skeptical economists are concerned) and Britain’s have lately broken a long streak of “ups” which, since 2016, have amazed the multitude of economists who think “Brexit” must surely mean “Depression” over there. The U.S. has held well over that magic 50 for years, and has been far stronger than most of the world . . . until just now, when that terrible 47.8 number triggered all manner of “Now the Sky Is Really Falling!” headlines to rattle us investors, and even Main Street.

While we’re ducking for cover in the nearest basement, however, let’s take one last backward glance at that chart. Of course, there’s the awful plunge during the Great Calamity of 2008 – 2009. Notice, though, the equally shocking rocket ride to the sky which followed. Within a year or so, U.S. factory companies were trying to keep up with tidal waves of business—and were much too busy to care about the media tidal waves of gloom which never took a single day off, regardless of the striking recovery obvious in all sectors of the economy.

Then we might notice, pausing on the basement steps for a last look, that the survey fell into “down” territory again and again, while the real economy kept on growing from 2013 to 2017. But we see that each plunge into “down” was followed very fast, mostly, by complete reversals into “up.” Last, we see that it got near all-time record “up” ground, beyond 60, for month after month from 2016 through 2018. Then it merely eased off a bit, staying cheerful, until the past few months of caution, and this one month of downright gloom.

What does it all mean? It means that Main Street naturally worries about hard-to-measure risks like Trade War, Brexit and European Stagnation, especially when media frenzy on any of such items approaches hysteria. And it also means that it takes a lot more than occasional caution and worry to actually derail Main Street; to actually make it close up shop and hunker down in the basement because the sky seems to be falling. It happened in 2008 – 2009, because “global panic and bank runs” were a real economic hurricane, requiring shutting up shop and boarding up the windows—for a brief while. But if the Great Financial Panic was a genuine hurricane, today’s “Trade War,” “Brexit,” and “Euro Stagnation” are a few gusts of wind and a passing thunderstorm, by comparison. The gusts and the lightning are quite capable of doing some damage, and we’ll surely notice some, during the Quarterly Earnings Season now underway. But they aren’t a hurricane; they’re nothing like a hurricane. If, instead of being awed by the wind and rain, we notice the continuing invention and never-ending cash creation in our companies (and most others, in the U.S.), that will be perfectly obvious.

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