CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

August 2, 2020

Progress in July...
...And a New Investment

Still the Coronavirus infections and deaths in the United States worsen, while Congress and the administration delay a fiscal response to ameliorate economic damage that has befallen households, municipalities, states, and businesses small and large. Because of continued strong performance of our two principal investments, long-term US Treasury bonds and gold, Core's accounts increased by another 4 percent in July. (As always, there is variation among individual accounts.)

Core's principal investments—long-term US Treasury bonds and gold—have done very well this year, indeed very well for the last two years. Further appreciation lies before us.

Early last week, gold achieved an all-time high exceeding the previous high from 2011. As I write, gold is up by about 30 percent for the year to date, while our long-term Treasuries are up by 26 percent. By contrast, the American stock market, as measured by the S&P 500, is up by all of 1 percent. A few points about gold: it has a 90 percent inverse relationship to real (that is, inflation-adjusted) 10-year Treasury yields, which have been declining sharply, and a 90 percent positive relationship to the size of the Fed's balance sheet. Thus as interest rates fall, gold appreciates; as the Fed balance sheet increases (as it has this year from $4 trillion to $7 trillion), so does the gold price. The Fed's balance sheet is almost certain to rise further as it tries to overcome the huge collapse in demand occasioned by the disease. Gold prices have a 67 percent positive correlation with the federal government's budget deficit to GDP ratio. With the weak economy and the unprecedented federal borrowing, this ratio will continue to rise and gold will follow it higher.

The 30-year US Treasury now yields 1.2 percent, a surpassingly low level. (Yields and prices move inversely; as yields on bonds fall, prices rise.) How much further can these yields fall and the corresponding bond prices rise? As of this week just passed, $15 trillion of bonds in developed countries trade with negative yields. The Federal Reserve has been clear that it will not let yields for US Treasury bills, notes and bonds fall below zero. But, as inflation continues to fall with the collapse in demand occasioned by the disease, it seems likely to me that the yields on long-term Treasuries will continue towards zero and the prices of these Treasuries will keep rising. We are sticking with this investment.

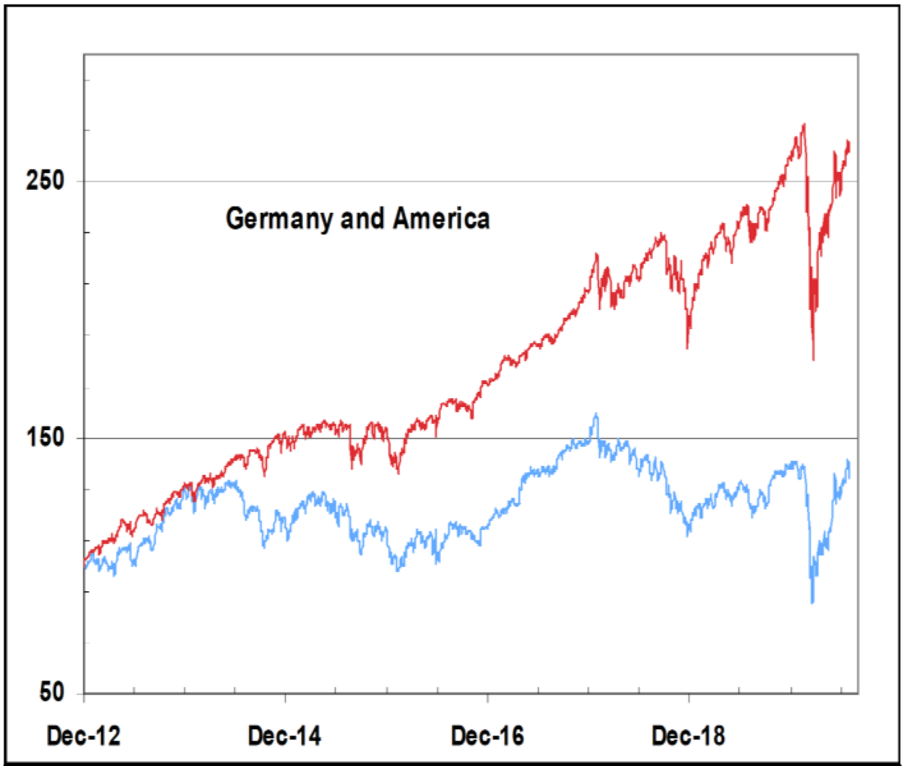
By

Jack Mayberry

Core made a new investment recently by purchasing German stocks via an exchange-traded fund. A number of factors persuaded us to make the investment. One is the effectiveness of Germany's actions in the pandemic. The haphazard American approach to the Coronavirus causes infections to spread across much of the country and deaths to rise. By contrast, Germany began public information campaigns on January 24th, prior to the first infection in

Germany. An effective lockdown and careful reopening beginning in May have kept cases in Germany very low and permitted a so-far well-controlled resumption of economic activity. In America, new infections per million people have doubled to 200 from the worst of the levels in March and April when New York and New Jersey were suffering so greatly. In Germany, the rate of new infections per million is about 10. Deaths are averaging about 5 per day in Germany, as against more than 1000 in America. I am mindful that cases are beginning to rise anew in Germany and that this weekend featured an angry demonstration in Berlin against the virus-control regime. The Coronavirus is an opportunistic and effective spreader, but the means of slowing its spread are well known and generally observed by Germans.

Germany has handled the pandemic in far better fashion than has America. This will speed Germany's economic recovery. Moreover, German stocks are far cheaper than American stocks.



Germany is, of course, an export power-house and might be seen likely to suffer as the globalization of trade wanes. However, some two thirds of Germany's exports go to other European markets, likely shielding it from the rising nationalistic trends that restrain trade. Additionally German stocks have lagged the appreciation that American stocks have enjoyed for several years, making the relative valuation of German stocks far superior to American. The nearby chart shows the S&P 500 in red font and Germany's index in blue, both rebased to 100 as of December 31, 2012. Any number of other comparisons besides stock prices would show that German stocks offer far better values than do American. German stocks are cheaper by any measure than US stocks and, as a result, are less risky.

It might be remarked that there is no German Apple, Google, Amazon or Microsoft, the companies that have taken US stocks so high. True. But if one strips technology stocks out of the S&P, one still sees a huge outperformance by the other American stocks as against German ones. American outperformance was not always so: From the end of the dot.com bear market in 2002 and until 2008, German stocks very sharply outperformed US stocks.

The desperately awful US approach to the Coronavirus will continue to depress economic activity here while the numbers of the newly-infected and of deaths rises as they have in the last six weeks. Under these circumstances, it is likely that Europe generally and Germany especially will see a faster recovery from the economic detonation that was occasioned by the Coronavirus and the lockdowns. Dr. Fauci has given us encouraging words about the likelihood of a vaccine late this year or early next. If and when this happens, it likely that stock markets will present real opportunity. Until then, gold and long-term Treasuries will continue to buoy our portfolios.

CORE Comments

CORE ASSET MANAGEMENT
PO Box 1629
108 Caledonia Street
Sausalito, California 94966
(415) 332-2000 • (800) 451-2240
fax (415) 332-2151
www.coreasset.com
info@coreasset.com