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INSIDE STORY

BE CAREFUL WHAT YOU ASK FOR

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~ Cicero, 106–43 B.C.

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BE CAREFUL WHAT YOU ASK FOR

The following is an imagined dialog with the Roman philosopher Cato.
It was written by the orator and statesman Cicero who lived from 106–43 B.C.:

Scipio: *“When Gaius Laelius and I are talking, Marcus Cato, we often admire your outstanding and perfect wisdom in general, but more particularly that growing old never seems a burden to you. This is quite different from the complaints of most older men, who claim that aging is a heavier load to bear than Mount Etna.”*

Cato: *“I think my young friends, that you are admiring me for something that isn’t so difficult. Those who lack within themselves the means for blessed and happy life will find any age painful. But for those who seek good things within themselves, nothing imposed on them by nature will seem troublesome. Growing older is a prime example of this. Everyone hopes to reach old age but when it comes, most of us complain about it. People can be foolish and inconsistent.”*

I have a confession to make. I found myself at the end of the first quarter of 2016 needing to write a newsletter and for the first time in memory I had no idea what I was going to write. So instead of writing I read *The Wall Street Journal* and I fell upon this quote. According to The Journal, the classicist Philip Freeman has published a new translation of this ancient dialog. As I read the short excerpt, inspiration struck.

What could possibly better sum up where we are today in our national discourse than this conversation which took place more than two thousand years ago? In all that time human nature has not changed.

Nowhere is this as clear as in our politics. In both major parties we see a large shift to what economists refer to as populist policies. These are policies that sound good as sound bites, but often have very adverse consequences – consequences which the same policy-maker

will often rail against. The analogy I have used in the past is like telling a five-year-old that they can eat all the candy they want without ever having to eat their vegetables. Five-year-olds love that idea. They also love the idea of growing big and strong. Of course as adults we recognize that those policies are inconsistent, but try convincing a five-year-old of that.

As I have been writing, one of the leading candidates for president has been on television complaining about Ford Motor Company’s plans to build a plant in Mexico. He finished by saying we can’t allow that to happen. Think about that for a second. We – the United States of America, home of the brave and land of the free – cannot allow a private company to build its plant where it wants to build it? Here is the real kicker: this candidate is running in the party that claims to be for smaller government and more freedom, and he is currently winning among those

supposedly freedom-loving people.

Trade has always been one of those issues upon which populists can pounce. Protectionism, the policy of building trade barriers – like a wall, for example – was a major contributor to the Great Depression. This fear of outside competition is nothing new. Trade, however, is a net positive, and for most of our history has been one of our strengths. Prior to our current globalization movement, trade within the U.S. was a major advantage to us globally. Civics classes are not what they used to be and many people have forgotten that our nation is a federation of 50 independent states. Our ability to trade freely between the states has long been one of America’s secrets to success. That was a huge incentive to our cousins in Europe to create the European Union, so that Europe as a whole could compete with the U.S.

Why does trade work? Think about it in the micro sense. Let’s say you have

a family of four and a long list of weekend chores. The yard has to be mowed, bathrooms cleaned, laundry done and dinner cooked. Does each member of the family mow one fourth of the yard, clean their section of the bathroom, do only their laundry, and then cook four different dinners? Or, are different duties split up among the group? At the micro level it is easy to see how everyone benefits from working as a team. That is really all trade is about.

Trade as a whole is almost always a net job creator, but there is often someone who no longer has a job to do. Trade creates jobs for the transportation industry. Goods made in one place and sold in another must be moved. Trade lowers the cost of goods creating more demand and helping the retail industry. But, if something that was made here is now made somewhere else, then those jobs are lost.

From an economic perspective this is not a bad thing. We want to be rid of some jobs. My wife's family has a cabin in Virginia. It is heated by a stove and a fireplace. Meals can be cooked on the grill outside or on a wood burning stove. Chopping wood is a job that has to be done every day you are there. It is a neat thing to do for a day or so, then you start to realize that losing some jobs may not be a bad thing.

Creativity takes time. We marvel today at the technological advances mankind has made in such a short period of time. My grandmother grew up in a world where cars were a novelty. Her first phone was a "party line," and anyone could join in to a conversation. Today, ten-year-olds have smart phones and the FBI has to hack into one to get any information. Why have we come so far in

such a short time? Because we lost our jobs on the farm. When it became more effective to trade with a farmer than to be one, people with great ideas were allowed to pursue them. The legendary economist Joseph Schumpeter referred to this process as creative destruction.

Granted it is hard to see. It is as hard to see as it is for the five-year-old to understand why broccoli is better to eat than chocolate. It can also be harsh, and we should do what we can to help those impacted. This is why civilized societies have for the last hundred years or so offered various safety nets. Those nets have varying degrees of success and come with their own issues. This is why policy should be an adult conversation. These issues are real and need to be thoughtfully addressed.

While trade is a bi-partisan movement this year – isolation is the one thing both parties seem to agree on now – it is not the only populist issue. Free college is another good example. Really, "free" anything is a good example. My grandmother's generation understood that free did not exist. The old saying, "There is no free lunch," exists for a reason. That does not stop some politician from insisting that something needs to be free of cost just about every election cycle. One of those things this year is college.

Like trade, this is an understandable target. The cost of higher education is absurd. Too many young adults have been saddled with questionable degrees and huge student loans. The tuition at Wake Forest University was approximately \$12,000 the year I graduated. After graduation I purchased a Toyota Camry, which cost \$16,000. Today a similar Camry

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Still chugging along. Fourth quarter GDP was up 1.4 percent. We expect the first quarter number to be a little higher but still in our new-normal range. Is anyone else getting bored with this? We have been stuck at this low rate of growth for almost eight years now and there is no sign of it ending anytime soon.

The official unemployment rate is 4.9 percent in February. The labor force participation rate is improving so there continues to be slow growth in jobs.

Inflation has ticked up with CPI coming in at 1.0 percent in February. The Fed remains on hold after their first interest rate hike last year. We think they will have a difficult time continuing to raise rates as there is little sign of inflation and growth remains very slow. +

REVIEW of ECONOMY

Volatility is the name of the game.

Markets have become extremely volatile in the absence of proprietary trading. The worst start in history was followed by a rebound and we ended up about where we started. The S&P 500 is up 1.3 percent for the quarter and the small company Russell 2000 index is down 1.5 percent.

Bonds rallied during the early year stock selloff and ended the quarter up 3.03 percent. High yield bonds ended the quarter up 3.35 percent. Many of the energy company bonds which had caused concerns in the high yield market rallied as oil prices bounced off the bottom.

The dollar hurt international investors last year but saved us in the first quarter. International stocks still finished down 2.9 percent as measured by the MSCI EAFE index, but they were down 6.4 percent in local currencies. +

REVIEW of MARKET

MARKET *forecast*

Volatility is likely here to stay for a while. As frustrating as that is, we remain confident in the longer term. Valuations on equities are attractive on the whole and the economy is still chugging along. It is a rough ride but we still believe it will end in a positive direction.

Emerging markets have real economic issues but valuations have become very attractive. Small company stocks are finally getting back into normal valuation bands. Caution is in order but that is a good long term sign.

Bonds remain our biggest concern over the long term, but they are still a shelter in the storm when the market does go down. +

» *Continued* –

costs around \$23,000. Tuition at Wake Forest is a little more than \$44,000 – that is just tuition mind you. Total cost of attendance is approaching \$60,000 per year. This brings to mind another legendary economist, Herbert Stein, who has an economic law named after him. Stein's law states that, "Things that can't go on forever, don't."

Higher education cost must come down, but in the meantime let's just make it free. We will waive our magic wands and poof – free education. This increasing belief that things can and should be free is horrifying. Cost is precisely the tool free economies use to balance supply with demand. It is what allows for prudent decision-making.

Ironically, this belief centers on the first issue, trade. In a world where everyone had to provide everything for themselves, they understood cost. Only with the benefits of trade do we forget that free doesn't exist. My children have no idea that water isn't free. Just the other day they were supposed to be cleaning our deck from the pollen when a water fight broke out, soaking both my children and my neighbor's kids as well. While they were having a great time lots of water was being wasted. My wife went out and informed them that water is not cheap.

There are still too many places in this world where children spend much

of their days having to fetch water from the river and carry it home. They know all too well that it is not free, nor to be wasted. No resource is free. The truth is, what the politicians really want is someone else to pay for it. Of course in the economic history of the world, nothing allows inefficiency and higher cost more than a system where the consumer is not the one paying. In fact, one of the primary elements which has led to the huge rise in the cost of higher education is the ability to have someone else pay for it, at least up front, through the use of student loans.

While this populist movement is cause for concern, it is also understandable. Real people have been hurt by things like trade and the high cost of higher education. There are many other economic issues we could use as examples. People are angry in many cases, and frankly they don't know who to direct their anger towards. So one side blames the "one percent" and the other side blames "Washington elite."

We have not changed. Just like the ancient Romans who wanted to grow old but complained about old age, we want our modern life with easy access to cheap goods, but we complain about free trade. We want higher education for all but we don't want to pay for it. In the effort to have it both ways we often make things worse. This is the

danger. Populism makes easy promises but brings with it economic disaster. It is like promising that one can grow old without any of the concerns of old age. It sounds great but does not work out in real life. A nation cannot fight against the laws of economics any more than an aging person can fight against nature.

Our role at Iron Capital is to manage our clients' investment portfolios. We don't like to weigh in on things like politics and frankly we are proud to have a diverse group of clients. But as the late Senator Daniel Patrick Moynihan was fond of saying, "Everyone is entitled to his own opinion, but not his own facts." Regardless of whether our next president approaches the issues of today from the right or the left, we need someone who will approach them as an adult.

Cato finished his conversation thusly, "So if you compliment me on being wise – and I wish I were worthy of that estimate and my name – in this way alone do I deserve it: I follow nature as the best guide and obey her like a god.... Fighting against nature is as pointless as the battles of the giants against the gods."



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