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TFA Monthly Newsletter

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Portfolio Investing — What is the New Normal?

By John Ulrich, CFP, President & CEO of Ulrich Investment Consultants

We have asked John Ulrich of Ulrich Investments to author this month's newsletter. Ulrich Investments is an independent investment advisor focused on high net worth individuals, family offices, institutions and has been serving Indian Country for over thirty years.

Many investment firms refer to the "new normal," which is a term that was popularized to describe the economic conditions following the financial crisis of 2007-2008 and the aftermath of the 2008 to 2012 global recession. The term has since been used widely to describe an environment which was previously considered unfathomable, and which is now commonplace.

While we believe there are some changes to what is considered "normal" that are warranted, we do not believe that investors should simply accept that certain basic tenants of the capital markets have suddenly dramatically changed. More importantly, we believe it is necessary to understand whether these changes in the capital markets are cyclical (short-term) or structural (long-term). In the end, valuations and profits matter, and understanding the implications of these market forces are paramount to navigating the "new normal" successfully.

In our view, a major driver of the "new normal" has been the decrease in interest rates and in the availability of debt. Ten years ago, the global financial system experienced extreme turmoil, resulting in unprecedented measures by central banks in order to provide much-needed liquidity and significantly lower interest. The result - global debt has sky-rocketed from $116 trillion to $247 Trillion.

The markets have accepted lower interest rates as part of the new normal; however, there are "cyclical" as well as "structural" issues that we believe need to be addressed.

1) Central banks will stop borrowing — Eventually, central banks will deal with the massive amount of global debt that has been created, which will result in a change in inventors' preference for investing in "risky assets." This will likely cause disruption in the financial markets.

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IN THE NEWS

Indian Pueblo Cultural Center Receives $1M Grant For Native American Makerspace & Incubator
10/1/19 – NativeBusinessMag.com

Suquamish Tribe's Construction Arm Lands $99 Million Navy Contract
10/7/19 – KitsapSun.com

Judge Dismisses Final Claims In Suite Against Elk Grove Casino
10/9/19 – BizJournals.com

San Manuel Band Of Mission Indians Agrees Stadium Partnership With Raiders For New Las Vegas Home
10/15/19 – WorldCasinoNews.com

Cedar Greens, The Jamestown S'Klallam Tribe's Holistic Cannabis Outfit, Opens In Washington
10/15/19 – NativeBusinessMag.com

Judge Strikes Down Pope County Ordinance Requiring Casino Vote
10/29/19 – ArkansasTimes.com

California Tribes Impacted By Wildfires
10/29/19 – IndianCountryToday.com

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2) Negative interest rates won't last forever — Germany's 10-year Bund is around -0.34%. That's right, the investor pays $1,000 and gets $966 back at the end of 10 years. This can't work long term. Currently, there is over $17 trillion of global debt with a negative yield. Because the US has some of the highest yielding debt from a global perspective, the increased demand from foreign buyers has resulted in very elevated valuations.

3) Less passive investing — Passive investing ("indexing" – like buying the S&P 500 index fund) has outperformed Active investing ("security selection" – picking individual stocks) over the past ten years, which has attracted more funds to market cap weighted indices, pushing market caps and valuations higher for a handful of securities. This means certain securities, say companies included in the S&P 500, have higher valuations than the underlying fundamentals support. We believe that this is more of a cyclical shift than a structural shift. Ultimately, indexing should result in capturing "market return." This will result is the need for more scrutiny in terms of investing in both stocks and bonds to gain superior returns. Over long periods of time, a combination of both passive and active management will be essential.

4) Lower public market returns — We believe returns from the public markets will likely be lower than what many have become accustomed to, resulting in lower expected returns. Public markets have become more efficient, and in some cases, more volatile.

5) Search for higher returns — We believe that lowered return expectations from public markets highlight a need to look for opportunities to enhance risk-adjusted returns.

6) More private investing — A major structural shift that has occurred in the capital markets has been the growth of private investing in both the equity and debt markets. In 2009, there were approximately 4,600 companies owned by private equity managers. As of December 31, 2018, there were approximately 7,900, and growing. Alternatively, the number of publicly traded US stocks has fallen to around 3800 from roughly 8000.[1]

7) Increased negotiation — Private markets give investors the potential to earn higher returns because they are inefficient, there are a limited number of participants, fewer opportunities to dispose of assets, limited availability of information, and higher transaction costs, or barriers to entry. As a result of these features, buyers in private markets can negotiate the prices of assets and translate managerial competence into added value.

Going forward, we believe the shift to private markets is necessary for investors to earn superior returns with a magnitude and consistency that is not achievable in efficient public markets. However, this type of investing requires financial acumen, significant due diligence and ongoing monitoring. Further, in order to negotiate, an investor must know what is possible – requiring a current, market-wide view. Buyers must be prepared to give up liquidity in exchange for outsized long-term performance.

We (TFACP) would like to thank John Ulrich for sharing his observations with respect to the new normal. Given the shift towards private investing, and the significant expertise to approach this type of investment, we highly encourage tribes to seek out qualified support. As always, if you have any questions, please feel free to reach out to us. We would be happy to provide help and suggestions with respect to the appropriate financial advisory support.

[1]Source: International Monetary Fund, Federal Reserve, Kleiner Perkins Pitchbook, Standard and Poor's.

ULRICH Investment Consultants

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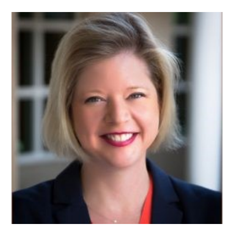

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