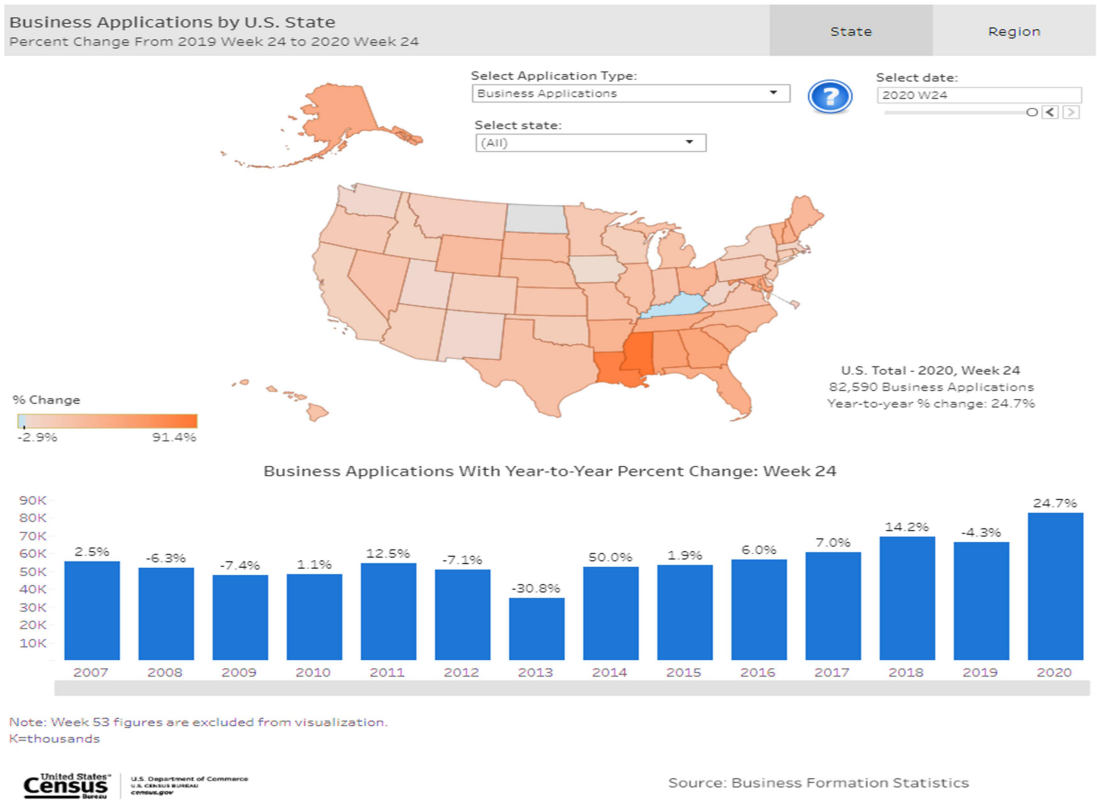
Market Watch with RMH

The U.S. Economy is robust and always changing as it should and that would be the way we would wish for it to be. Samuel Rines from Avalon Advisors wrote an excellent report on the Dynamism of the U.S. Economy, several of his thoughts follow:

- **Dynamism is not dead. From a year ago, business application are *up 24.7%*. That will benefit employment as the recovery takes hold.**
- "Most of those businesses will not produce jobs". Typically, that might be a meaningful critique but not this time. Business applications with planned wages are higher by 6% from a year ago.
- Why does this matter? A common misconception about the U.S. economy is that "small businesses" create the jobs. It is actually young business and start-ups that drive employment.
- This bodes well for an employment comeback during the recovery. It is certainly not a instantaneous employment reaction. But it is a positive.



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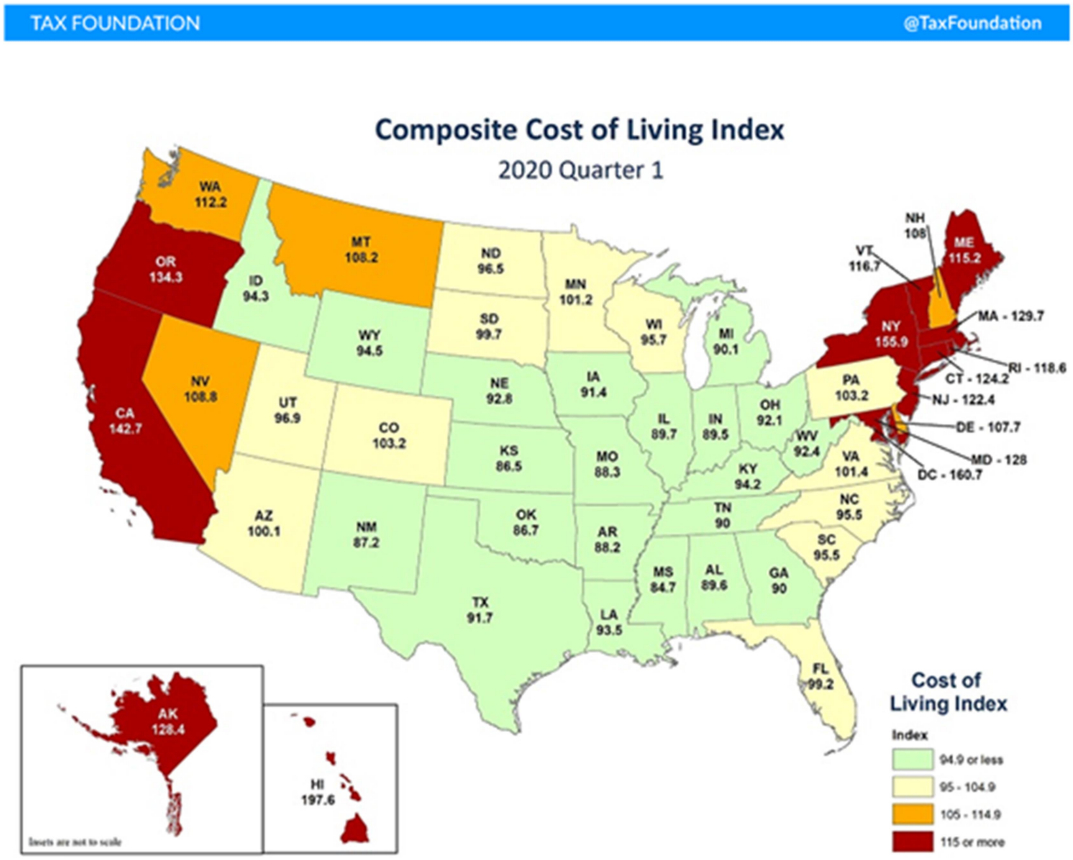
The other question that must be asked, is where will the job creation be? Looking at the Composite Cost of Living Index, Arizona is in a good spot, not the lowest, however far from the highest! A lot of the higher prices states are seeing outflows of individuals and businesses. Looks like the south and the middle parts of the country are our engines for growth.

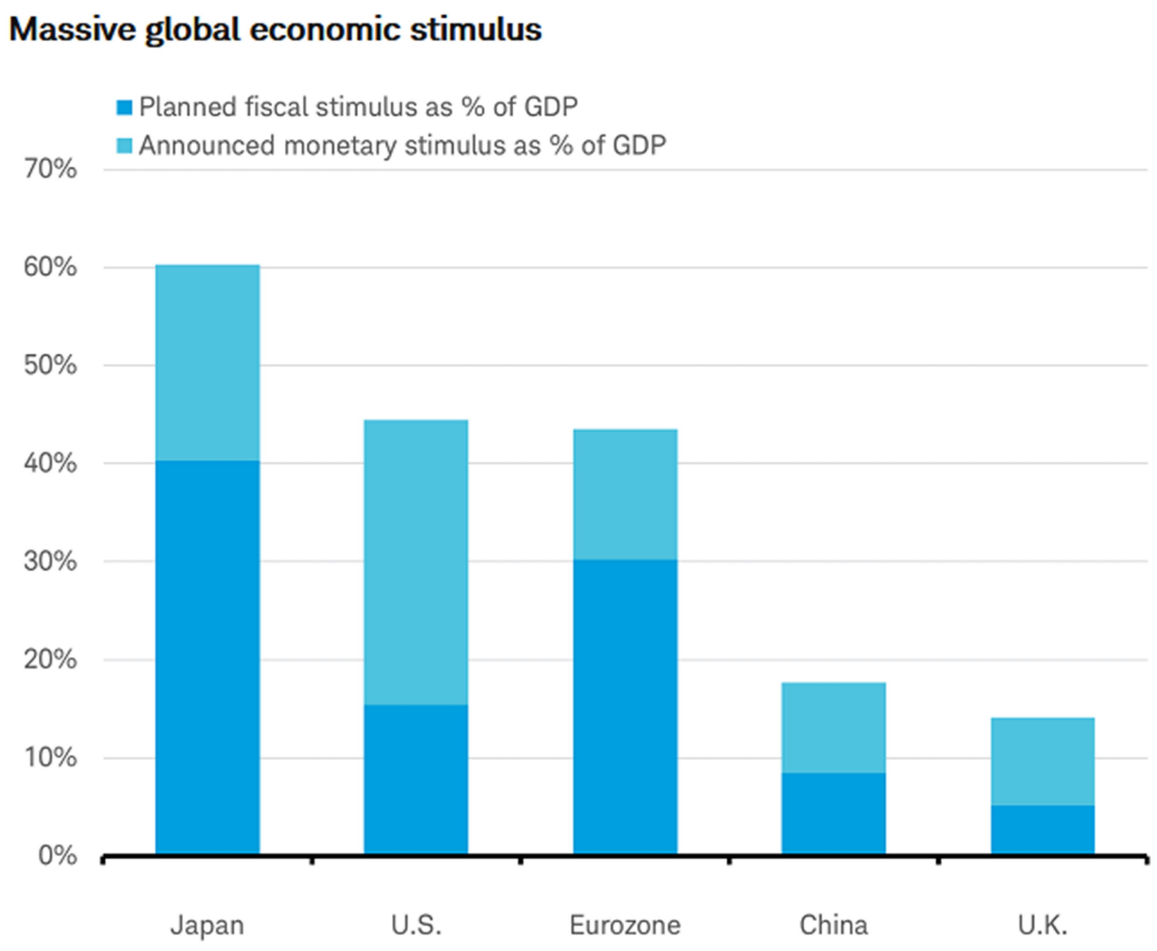


In summary from Samuel Rines article, **"it cannot be emphasized how critical the continuation of this trend is for employment. Young businesses are the employment creation engines of the U.S., not small businesses. Young companies simply happen to also be small businesses. If there is one reason to feel better about the future of U.S. employment, it is this data"**.

One of the favorite mantra's of investment professionals is "don't fight the Fed". Last week the U.S. Federal Reserve (Fed) committed to leaving the Fed Funds rate at or close to zero for an extended period of time. For those not familiar with the Fed, they must realize the Fed has a dual mandate:

- The stabilization of Employment and Inflation.
- By keeping interest rates low they believe will help spur employment growth, and increase inflation simultaneously.

Staying with this theme of not fighting the Fed, we look at the chart of **"Massive global economic stimulus"** provided to us in the chart below from Charles Schwab. We need to keep in mind the stimulus is intended to support businesses as the economy reopens.



Source: Charles Schwab, official policy announcements from start of February through June 6, 2020.

Charles Schwab warrants a word of caution as it appears the Global Recovery is on its way. Investors need to watch for the following:

- A slowdown in the pace of recovery as some restrictions linger, evidenced by the still stringent lockdowns in many major countries.
- A second virus wave resulting in another official lockdown or an unofficial behavior shift, where people no longer feel safe to leaving their homes.
- A return to the U.S.-China trade war as rhetoric spills over, undermining the hard won Phase One trade deal from mid-January.
- Ongoing civil unrest may weigh on the confidence of consumers and their spending, the largest driver of the economy.
- An above-average summer hurricane/typhoon season (along with other natural disasters) that could damage coastal areas, and slow their recovery.
- There are likely plenty of additional concerns besides those listed above. The start of new economic cycles are usually vulnerable and subject to risks.

China

In the last RMH Market Watch, one of the items that we are keeping our eyes on is China. The Bank Credit Analyst feels that China is susceptible to several shocks due to covid-19 (the pandemic):

- China no longer primarily channels its savings into export manufacturing, instead investing at home. China's total debt**, public plus private** has surpassed many developed nations despite the country's lower levels of development and wealth.
- China can manage this debt as it prints its own currency, keeps a closed capital account, and has shifted to a primarily domestic economy. Debt is less manageable than from before the crisis. Nominal growth has fallen below interest rates, implying that in the midst of a crisis, debt can't be serviced for the economy as a whole. Growth will revive, but will run at a lower rate than before the crisis, and debt servicing will be a recurring problem for small or inefficient businesses.
- The pandemic and recession will pass thanks to the massive government intervention. What will remain is the concern that China will grow old before it grows rich. **This will be a huge risk to the regime in the long run.**
- The unemployment rate in China has been elevated; however job losses are concentrated in the labor intensive, low skilled manufacturing and service sectors (just like the United States). **The lower income workers account for over 50% of the population, however their share of the country's wealth is minimal compared to the top 10%.** Households in the **bottom 40%,** essentially have no discretionary income.
- China will need the **top 40%** of their population to be the driver for the discretionary and luxury market.

The last two points above took a lot of time to sink in with regards to China's actions of late. 40% of 1.3 Billion citizens means 520 Million people to drive the economy. That leaves 780 million people at the bottom, and in an unhappy state, which now gives me an explanation of some of China's actions of late:

- Abrogating the Treaty with the United Kingdom (UK) with regard to the handover of Honk Kong and the rule of law which was supposed to last 50 years starting in 1997, without consulting the UK.
- Having a border tiff with India in the disputed area of the Himalaya's where they attacked with clubs (barbed wire and bayonets attached to clubs, threw rocks and several people off a cliff), so they would not violate the agreement from the 1960's about using modern weapons, guns, etc. The Indians were unprepared, and at least 20 were killed, prisoners have now been exchanged. The Indian Army went out and ordered lightweight body armor, armed accordingly, and as a result talks were started.
    - was this over water, as both countries are short of water?
    - or was this over the fact India encouraged global manufacturing to their country instead of China?
        - The sad thing about the point above is that India needs China as a source of raw materials for anything in the medical industry.

Observations on a client trip to the Northeast. It was cheaper to rent a Ford 150 than a car, the truck gets 22mpg at 75 mph, rides well, good stereo system to listen to podcasts, and at 2 feet higher off the road, one gets a nice view. I can now see why they sell so many pickups! Traffic was busy on I-90, rest stops empty and shops inside mostly closed (I was reacquainted with Burger King for breakfast and coffee, and

had forgotten why I had stopped going) and hotels running at 40 – 50%. Saw a number of factories that had hung signs saying "we are hiring".

Airport concourses with the exception of Midway/Denver were pretty empty, people all wearing masks and a lot of the businesses inside closed. Southwest Airlines policy is to have the middle seat empty and mandatory mask wearing on the flight, nice.

In a suburb around a golf course there were at least 20 projects for home improvements, including at least three new builds of at least $750k - $1mm.

From talking to others here in Tucson/Scottsdale, there seems to be a trend in home improvements. Good to see elsewhere in the country, although my sample size is small, and could be flawed.

Things that we are keeping our eyes on include the following:

What steps are we doing at RMH?

- We are looking at the portfolios and rebalancing where necessary.
- We are taking advantage of tax loss selling to lower future capital gains.
- We are looking at what insiders are doing with some of the stocks we have purchased.
- We are talking with portfolio managers on a one to one basis and participating in conference calls.

If there are ever any topics you wish us to explore, please let us know. ***We are here to help and guide you through these times.***

We thank you all for taking the time and reading "Market Watch." It is meant as an educational piece on the always evolving markets. It is something we plan on providing every month, and your feedback is very important to us.

On a personal note, RMH is now in the position to bring on new clients and please be sure to share this informational letter with whomever you wish. RMH's focus is on the customizable investment needs of individuals, families, and foundations. We enjoy working with our clients to better understand their goals, values, and passions for what is important in their lives. In expanding our client base, we look forward to working with people who share these same desires

Richard Mundinger, CFA

Samuel Rines, Avalon Advisors: Dynamism is not Dead, June 19, 2020
Charles Schwab 2020 Mid-Year Outlook: Global Stocks and Economy
RiverFront Investment Group: "Fed up With The Yield Curve"
Merk Research: Nick Reese, CFA: U.S. Business Cycle Report
Bank Credit Analyst
https://economictimes.indiatimes.com/news/defence/india-recovers-from-the-shock-of-nail-studded-clubs-gets-ready-to-get-even/articleshow/76442476.cms?from=mdr
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