

Hello Everyone,

The stock market has a different feel now. The trading for most of 2018 reflected a market where the professionals were trying their best to squeeze the last bits of gain out of an ageing (9 year) bull market. Most didn't do so well.

In the last few weeks, however, the trading appears to be reflecting the thought that the highs are now behind us---and it's time to get defensive. Note, over the past few trading sessions, the Dow has fallen 1600 points while gold is up \$30/ounce. Of course, a few weeks does not a trend make...we'll see.

Today's missive uses GE and GM to make a point about the broader market----and how stock buybacks may be contributing to the market's recent weakness.

I hope you find the below transcript enlightening.

Signed, Your KKOB-Finally-Sold-The-Friday-Spot-To-Someone-Else-So-I'm-On-Only-Once-A-Week-Now
Financial Advisor,

Greg

KKOB 12.10.2018 GE and GM

Bob: So, today we are going to talk about the generals---General Electric and General Motors. American giants---but both are struggling.

Greg: They are. So, the question is why? And, I know many will immediately jump to, "Oh, it's those unions!" Or, "They make bad cars!" I am, however, going to offer another possibility. Share-buybacks.

And, Bob, I know you've heard me harp on the potential problems surrounding share-buybacks for over a year now, right?

Bob: I have. So, don't tell me----let me try to puzzle through this. Here's what I know. When the Federal Reserve dropped interest rates to zero, lots of companies were able to borrow money---almost for free.

However, rather than using that money to modernize, or get more efficient, many firms used the borrowed money to buy their shares

back. Of course, when they did that, the number of shares available to the public fell. With fewer shares available, that helped push up the stock price. And, as the stock price rose, the company officers and board members all got big year-end bonuses.

Greg: Wow. You've been listening! A++. OK, so now for the final exam. What is a potential problem with this strategy?

Bob: Well, you still borrowed the money, so, at some point, you must pay it back. I mean, eventually, you'll need to come up with some cash.

Greg: Bingo. So, here's the GE situation. Over the past several years, they repurchased \$40 billion (yes billion) of their own stock at prices between \$20 and \$32 per share. But their stock didn't go up. Today, it's at \$7. That translates to---ohhh, \$23-\$28 billion in losses. Oh, and like you said, they still owe the billions they borrowed. Anyway, GE's total debt is now north of \$115 billion, and GE is technically insolvent. Nice work boys, I hope you enjoyed those bonuses.

Bob: OK. So, a bunch of questions. What does General Electric do now? And then switching gears---what about General Motors? I mean GM took taxpayer money. And, you're telling me GM bought back shares---but maybe with taxpayer money!? And, now they want to layoff all kinds of people?! No wonder Trump is mad.

Greg: Right. OK, so first back to GE---they're now saying paying off debt is their number one priority. Duh. But that means a long slog ahead, because as they pay down debt, that means less money to bottom-line profit...and investors don't like lower-profits.

Next, yes GM, was also reckless. They spent \$14 billion to buy back their shares at inflated levels. Thus, they are down in their "investment" as well. So, their solution is to close plants and fire people. And, yes,

President Trump is furious...and, I don't blame him...this did not have to happen.

Bob: OK. I get all that. But, you've kind of cherry-picked two companies that have both had issues for a long time. I mean, not all share-buybacks were bad. And, it is a company's job to do everything it can to boost shareholder value. Right?

Greg: Wow, Bob...nice job! You're right...and you're right. I did cherry pick two to make my point. And yes, public companies have an obligation to increase shareholder value.

I guess, my answer to that would be any company's goal should be to maximize long-term shareholder value. In many cases, however, I believe the "zero-percent-interest-rate-driven" share-buybacks were a short-term sugar high. The question now is---- how does Corporate America come off that high?

Or, putting it another way-----how many companies in 2019 are going to say, *"Uhh, we need to pay debt back, so expect our bottom lines to shrink for a while."* And, could this be one of the reasons the overall market is starting to weaken? And, if that is the case, then money will move to companies and sectors not burdened by excessive debt...and therein lies the opportunity for your listeners in all this.

Bob: Of course. I get that. Anyway, I always get a headache when I come off a sugar high. How do people reach you?

Greg: My number is 508-5550. 508-triple-5-zero. Or, go to my website at zanettifinancial.com

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