Hello Everyone,

This headline ran across my computer screen late last week.

### *Ray Dalio Warns A "New Paradigm" Is Coming: "Buy Gold, Sell Stocks"*

Dalio is no crank. He is one of the largest hedge fund managers in the world. $18.4 billion under management.

From that headline we can assume:

- He has been re positioning his portfolio for many months…maybe even a year. It takes time to reallocate billions without disrupting markets…or giving your hand away.
- His portfolio cannot be 100% gold. So, other "inflation sensitive" investments likely accompany his gold holdings.
- He believes currencies are in play and Central Banks do not have the control they used to have

Of course, even Wall Street "legends" can be wrong. Still, it's nice to know our thinking is embraced by people who know a lot more than we do.

Full Story here---

https://www.zerohedge.com/news/2019-07-17/ray-dalio-warns-new-paradigm-coming-buy-gold-sell-stocks

Today's missive revisits the share buyback theme we have discussed periodically in the past. It fits another piece into Dalio's "new paradigm" puzzle.

I hope it helps you see the investment world a little more clearly.

Signed, Your Investment-Puzzles-Are-Sometimes-Difficult-But-When-The Picture-Comes-Into-View-Very-Gratifying Financial Advisor,

Greg

# KKOB 07.22.2019 Share Buybacks Revisited

**Bob:** So, Greg, we're staying on the theme of "super-low-interest-rates"----and how they've encouraged companies to buy shares of their own company stock.

Apparently, when you brought this up last week, you got some good feedback---- as well as some questions---right?

**Greg:** I did. Your listeners certainly get it in principle. So, today let's cite some real-life examples---it might make the financial landscape a little clearer. And let's use Apple stock to make our point.

Over the past four quarters, Apple has spent ***$75.1 billion*** on share buybacks. Over the past five years, that number jumps to ***$284 billion***.

**Bob:** OK, wait. Before we go on. Let's do a quick reset. When companies buy their shares back, that shrinks the number of shares available to the public. Right?

**Greg:** Right.

**Bob**: So, let's pretend, Apple's ***profits per share*** jumped 15%. That doesn't necessarily mean Apple's overall profits went up that much since there are fewer shares.

I mean, Apple's total profits may have gone up only 2%----but since Wall Street only cares about ***profits per share***, buying shares back really helps boost the stock price.

**Greg:** Exactly. But, with Apple a funny thing is happening. Even with the share buybacks, their stock is down 16% since last October when that last market correction started. That's raising some eyebrows.

In fairness, some "buyback-heavy" companies like Oracle and Cisco have seen their share price rise nicely. But, Bank of America and Pfizer are experiencing the same thing as Apple.

Anyway, this phenomenon is new. Over the past several years, share buybacks almost always raised the stock's price. Now, it's lumpy.

**Bob:** OK So, this may seem a simple question, but where do companies get the money to buy their shares?

**Greg:** It's a great question. You can either take the money from your company's cash box---- or you can borrow it. Most borrow. Again, let's look at Apple. Apple has heaps of cash, yet they still borrow money to buy shares because interest rates are so low. The thinking is, "Why not take advantage of the free money?"

Bottom line--most companies borrow to buyback. And trillions have been borrowed and spent this way over the past 8-10 years.

**Bob**: Ok, so stocks are way up---- but so are debts.

**Greg**: Smart guy.

**Bob:** If I did this---if I borrowed money to buy stocks---even at low interest—my wife wouldn't be very happy. Because, if stocks go down, I still owe the money….low rate or not.

**Greg**: Right. This is how you can have the stock market hitting new highs but with corporate debt levels at 1929-ish levels when compared against GDP.

Anyway---as an investor---you can choose to look at this situation in one of two ways.

First: *"Hey, the management and the board believe in their company. They know more about the firm than I do. Therefore, I'm buying, too.*

Or...option 2.

*"Hey, these guys are trying to hide some underlying weakness in the firm. Overall profits have stalled, so they are borrowing money to buy back shares to bamboozle us into*

*thinking they are growing faster than they really are. Oh, and, they get bonuses based on share price."*

**Bob:** So, the answer is---I guess it probably depends on the company. Some are probably doing well, and others not so much.

**Greg:** That's my take. And that's why artificially low interest rates have made investing more difficult. If rates were at 5%, "borrowing to buyback" wouldn't work as well.

But here we are. Almost everyone has done it. That means if the Federal Reserve were to raises rate, paying higher interest on all that debt would be a huge drag on stocks going forward.

**Bob:** I can see that. I guess that's another reason they want lower rates heading into 2020.

**Greg:** I think so. So, next week, let's come at this in a slightly different way. The shale/oil industry will hit the spotlight—especially since it is so important to New Mexico.

**Bob:** Looking forward to it. How do people reach you?

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