Current Comments
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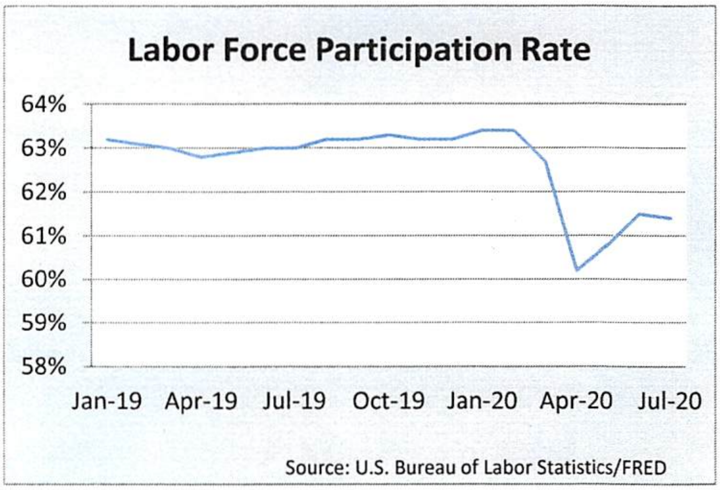
Following a dramatic decline in March this year, U.S. Equity Markets have begun to rise after one of their sharpest drops in history. The S&P 500 Index is beginning to push new highs, and many equity indices have rebounded a lot. Technology generally persevered and is growing strongly. Restaurant shares as well as entertainment and arts-related issues have declined a lot, yet some are rebounding back. Shopping centers are experiencing structural decline. New York Real Estate is weakening in many areas, as did most REITS. Overall, many valuations appear generous. Overly generous valuations would be vulnerable to sustained increases in interest rates, which does not appear likely to happen any time soon.


Figure 1. Icarus Prepares to Fly Close to the Sun

However, there is a huge divergence between recent returns of growth and value issues. Usually they are fairly similar, yet currently the difference in average returns between the asset classes is over 25%. The last time the difference was this large was back in 1999 to 2000 before the Internet collapse. Some note that if one takes out the 5 or 10 strongest issues, generally encompassing the FAANG stocks (Netflix, Amazon, Facebook, Apple, etc.), the returns of the index are much less. For some, this is a cause for concern;

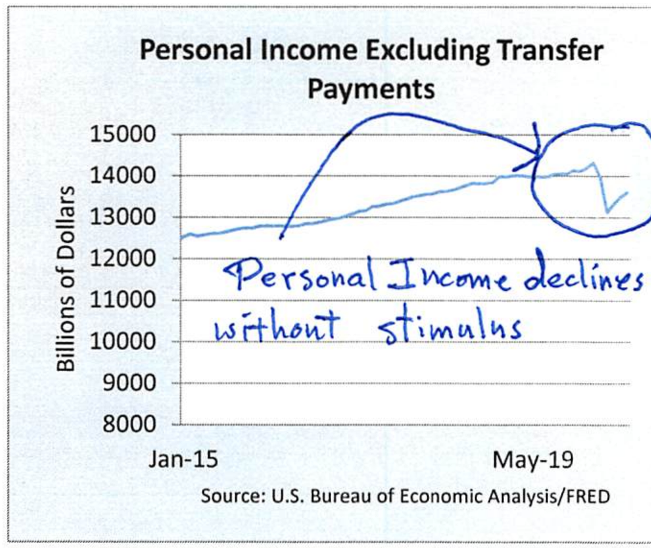


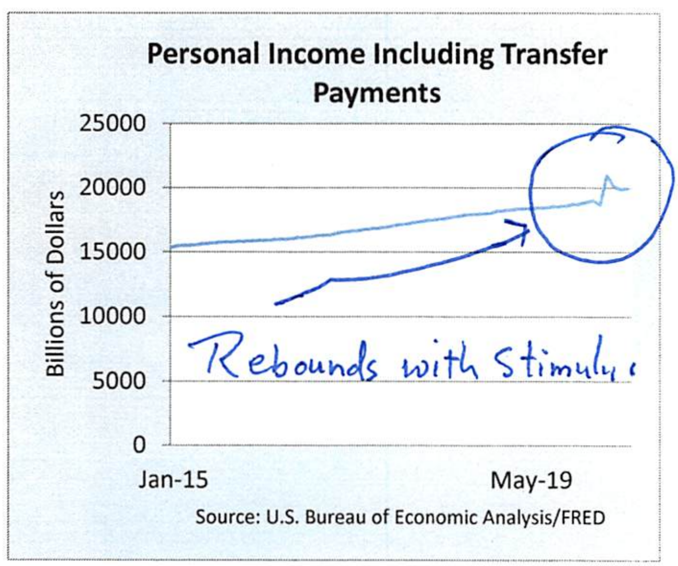
for others, it reflects economic reality as Amazon is dramatically encroaching on retail malls and other traditional sellers. There is a notable divergence between financial markets and the real economy. Markets look ahead, and many look at the real economy to define their future path. The U.S. Economy was seriously dented by the coronavirus. U.S. GDP declined at an annual rate of 32% in the second quarter (or about an 8% decline for the quarter) to an annual rate of $19.5 trillion. Unemployment rose to 14.7% in April, and has since declined to 8.4%. A decline in the Labor Force Participation Rate may have softened the recent blow.

Federal fiscal policy provided stimulus. The Congressional Budget Office projects a $3.3 trillion federal deficit this year. Without the additional fiscal stimulus, personal income would have declined.

Policy Response

Economic theory would call mainly for federal fiscal stimulus, which is certainly occurring. This time, the current administration has implemented a large amount of fiscal stimulus. The federal deficit this year is projected to be $ 3.3 trillion. The follow-on stimulus bill is not yet passed. I find my attention being drawn to the wider economy, and also more to geopolitical aspects.

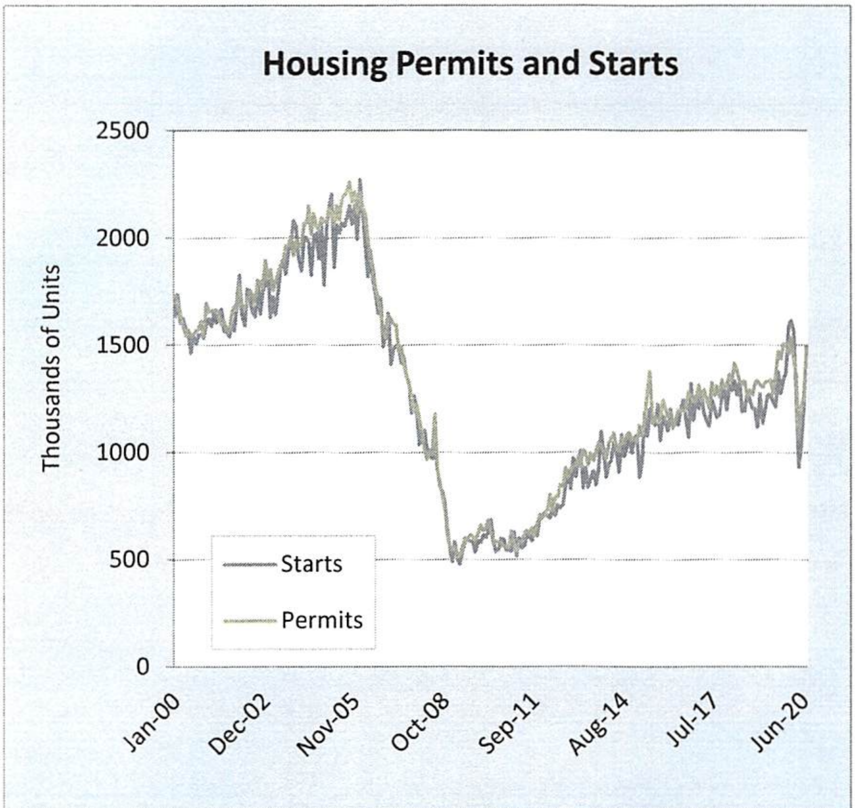




Housing

We have a very accommodative monetary policy, and the Fed has lowered interest rates. One effect of a decline in interest rates is lower mortgage payments for a given mortgage amount.

There are some deeper changes taking place in housing. One major factor was the first tax revision during the current administration, which capped the deduction for mortgage interest for investors who itemize. This increases the after-tax cost of living in some of this higher income states (such as New York and California) and creates an economic incentive (one factor only, though) to move to other states. If we can't deduct the interest on a $6 million dollar mortgage, what good is it? However, people migrating from California to Nevada or Arizona were more likely to be middle and lower income individuals. Higher income New Yorkers were more likely to move to California than they were to Mississippi, Arizona, or New Mexico. Perhaps motivated by housing cost differentials, more people were living in Oregon, Idaho, or Nevada and commuting to jobs in California. Many moved to Nevada or Arizona so they could afford a home with earnings from employment in California.



The second recent factor is the impact of the coronavirus. Specifically, residential rental rates at the upper end of the market in New York City are declining, New Yorkers are moving to the surrounding suburbs, and some are moving away from congested cities (especially New York) to newly-acquired residences in other states. This means, *ceteris paribus,* more housing appreciation in Western open states like Oklahoma, Idaho, or Arkansas; weakening rents in NYC, and weakening commercial lease rates in NYC.

There are a lot of millennials out there who do not yet own a home, and many of them aren't married yet. As they age, there is more pent-up demand for housing ownership. Additionally, during periods of increased unemployment and recession (such as now), the number of households contracts. Then later as the economy recovers and expands, the number of households increases leading to the demand for more housing. This combined with lower mortgage rates is a force to support more housing starts for new homeowners, held back and dampened by student loan debt. Housing appears about to embark on a period of more solid and sustainable growth.

Federal Reserve Policy

Federal Reserve Chairman Jay Powell recently put forth a reformulation of Federal Reserve policy. The changes may seem subtle, but they are important. The restatement says the Fed will abide by inflation somewhat over 2.0% for a while, if employment has not reached its optimum achievable level. This means interest rates will continue to be semi-permanently low for an extended period. The recent Fed support along with this policy seem to have already resulted in notable asset inflation, but not a general consumer price inflation nor increase in the CPI.

On Cyprus

About three or four years ago (Pre-Trump), I gave a Toastmasters speech on a fellow who had two million dollars in a checking account in Cyprus. Who, or what kind of person would have that, I wondered? Probably a notable one. That led to further research. The holder of that checking account was Paul Manafort. Mr. Manafort seemed to have worked on or completed several deals in his lifetime. Earlier in his career, he had an affair with Deborah Gore Dean, the assistant to the then Secretary of Housing and Urban Development, Samuel Pierce. Paul Manafort worked on a housing grant project that she assisted with. For her assistance on that project, Deborah was subsequently sentenced to about 21 months in prison, eventually serving a year of house arrest. Paul Manafort got about $330,000 in fees and participation interests. Mr. Manafort spent several years working in lobbying in Washington, at Black, Manafort & Stone. The "Stone" in 'Black, Manafort, & Stone' was Roger Stone. Mr. Stone had earlier worked with Ronald Reagan's campaign and with Richard Nixon. Besides lobbying, Mr. Stone is the author of a few books, including The Man Who Killed Kennedy: The Case Against LBJ. In 2000, Roger Stone worked with Donald Trump to create the 'New York Institute for Law and Society' running ads opposing a casino proposed by Native American tribes in the Catskills, which would have competed with Mr. Trump's Atlantic City casinos (Andrea Bernstein, p.109). Roger Stone was fined $100,000 and Mr. Trump was fined $250,000 by the State of New York for running an illegal lobbying campaign. More recently, in 2019 Roger Stone was sentenced to 40 months in federal prison for lying to Congress, witness tampering, and obstruction. President Donald Trump indicated that Mr. Stone "is a quality guy" and a nice person, and he commuted his prison sentence.

Mr. Manafort also worked with or assisted various Russian "oligarchs" who had and have connections to Vladimir Putin, especially Dmytro Firtash in the Ukraine. For Russians, one of the advantages of banking in Cyprus is fairly nonexistent reporting requirements to Russian tax authorities (unlike EU banks).

Geopolitically, Cyprus is an interesting place. It has been owned or ruled by the Turks, the Ottomans, the Persians, the Greeks, the British, the Egyptians, and most recently by the Cypriots themselves. And, Mr. Igor Grechushkin, the ultimate owner of the ship that recently blew up in Lebanon, appears to reside in Limassol, Cyprus. Why would he live there, instead of Moscow or St. Petersburg? Or London?

While not huge, the Bank of Cyprus is the major bank in Cyprus, and Mr. Manafort decided to do some banking there. In 2014, Wilbur Ross owned about a third of the Bank of Cyprus. Mr. Ross is currently the U.S. Secretary of Commerce, and he no longer owns the shares. Those shares are now owned anonymously. Mr. Ross worked to clean up and turn the bank around, decrease Russian influence, and increase profitability.

In December 2018, a research team from Clark Asset Management visited Cyprus. Cyprus is sort of like Laguna Beach in 1949. On our voyage, we visited the Bank of Cyprus. There are representative offices in Kiev, St. Petersburg, and Moscow. Cyprus shows up several times in the recently released Senate Select Committee on Intelligence Report, Volume V. The Federal Indictment of Paul

Manafort provides insights into the flows of funds from Russia and Ukraine into Cyprus accounts and then out to other places like Virginia, Belize, and Panama. From there, some flows into Trump Organization real estate interests. So, it was an interesting fact-finding trip to Cyprus.

In the past 2-5 years, several writers and researchers have mentioned Cyprus and Mr. Trump. Others, and sometimes the same ones, connect, or allege connections between Russia and Mr. Trump. One could also put Robert Mueller into the mix. I am currently reading, American Oligarchs: The Kushners, The Trumps, and American Greed by Andrea Bernstein. I am also reading Masha Gessen's Where The Jews Aren't: The Sad And Absurd Story of Birobidzhan, an obscure book that provides a unique background look at Russia that may provide insight into Charles and Jared Kushner. If one can read between the lines, Andrea Bernstein's work is a good book. Another interesting publication is the U.S. Senate Select Committee Report on Intelligence, Volume V; a bipartisan report. If one has a bit of patience, there is a lot of interesting detail. Cyprus shows up several times, and Mr. Manafort is mentioned hundreds of time. The other volumes are interesting too, providing an in-depth look into the Ukraine stating unequivocally that the Russian connections, relationships with Trump interests, and the Report were facts and **not** a 'hoax', as the word is defined in Webster's Dictionary. As one reader described it, "it is clear that the Russian government is not our friend, and that the Ukraine is a messy place". And both have connections to Cyprus and Cyprus bank accounts.

Tax Returns

Mr. Trump's presidency has prompted the publication of a few books over the past three years. As events evolve with the current administration, it seems as if there is ***always*** something going on! One issue I particularly note is the disclosure (or not) of President Mr. Trump's tax returns. Mr. Trump appears to have expended over a million dollars to block the release of his income tax returns.

The elephant lounging in the room is Mr. Trump's tax returns. Russia worked to elect him, and it is somewhere close to obvious to many that Mr. Trump and Mr. Putin had plenty of opportunity to discuss financial support to Mr. Trump and the Trump Organization from Russia. Mr. Trump's tax returns would likely hint at this, at the least, and probably much more. It is likely that Mr. Trump's tax returns will not be turned over nor revealed until Mr. Trump is into his second term. So how would an investor make gains with his information? I am not sure.

How to Use Cyprus in Your Financial Affairs

The way to use Cyprus in one's financial affairs is to create or acquire a global business, such as ocean shipping or petroleum exploration or shipping, put it in an offshore LLC, Trust, or corporation, domicile it in Cyprus, and open a bank account in Cyprus. Make sure you do not own this individually, and that the Cyprus bank account is not in your name (rather the global business). The income should be 'earned' outside the nation of Cyprus. Check with your CPA. There are also large accounting firms in Cyprus and in London that would be glad to assist.

The Virus

A smart and appropriate action by our current administration was to contract for and partly fund virus vaccines from at least seven different manufacturers before they are created. Industrial production begins before safety trials are completed. This takes the financial risk off of the producers, enabling them to proceed ahead before they have final confirming testing and trial results. By awarding contracts to 7+ different producers, it is more likely that one or more will be successful rather than picking one and hoping for the best. This approach moves most of the financial risk to the federal government, and accelerates the availability of vaccine by 6-8 months off of creation and production time. This is a sensible approach. The timing is still a source of uncertainty.

Summary

We have a dented economy, which is generously valued by financial markets. Growth is outpacing value, sometimes without a firm foundation. Many observers see vulnerability here, but markets look ahead. Thus, many observers see good times ahead. We have 1) a supportive monetary policy, 2) a very simulative fiscal policy, and 3) a likely virus vaccine sooner rather than later. We have many ingredients of a continued positive contribution of housing to GDP. We already appear to be experiencing asset inflation, without general price inflation. All of which is taking place in a more dramatically turbulent political environment than normal, with some corruption and intrigue tossed in.

And, what will come next?

Clark Asset Management manages investment portfolios on a discretionary basis. Depending on the client, we generally rely importantly on index funds of the S&P 500 and various asset classes. Recently, we have leaned somewhat more to increasing the cash percentages in portfolios. We also plan on tilting a bit more to specific individual issues, rather than index funds for various asset classes.

Thank you for your continued confidence, from all of us here at Clark Asset Management.

Sincerely,

Gary N. Clark, CFA