No Billionaire left Behind!

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The Monthly Market Commentary Report

Disclaimer

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"Strange times are these in which we live when old and young are taught falsehoods in school. And the person that dares to tell the truth is called at once a lunatic and fool."

Plato

"He who knows nothing is closer to the truth than he whose mind is filled with falsehoods and errors."

Thomas Jefferson

"My own education operated by a succession of eye-openers each involving the repudiation of some previously held belief."

George Bernard Shaw

"You can't expect a boy to be vicious till he's been to a good school."

Hector Hugh Munro (better known by his pen name "Saki")

"Formal education will make you a living; self-education will make you a fortune."

Jim Rohn

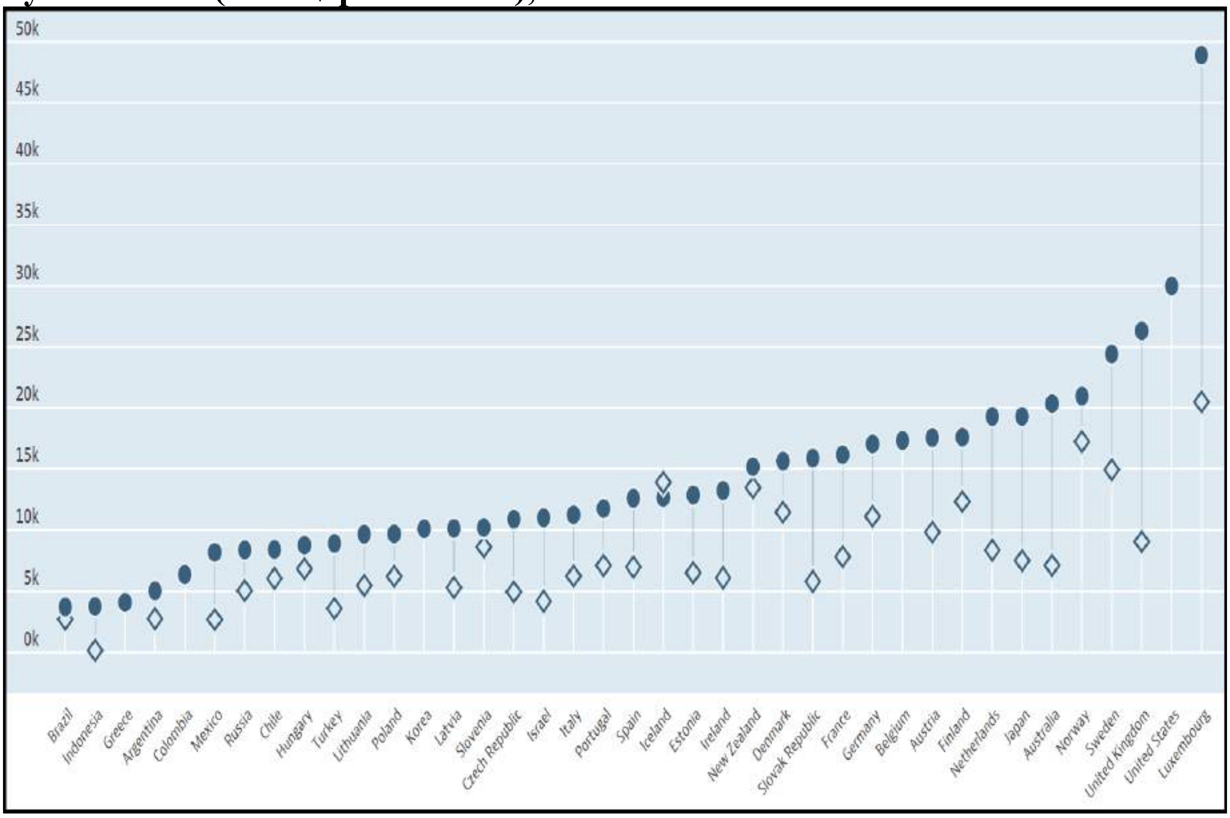
"Great books are great teachers; they are showing us every day what ordinary people are capable of."

Robert M. Hutchins

In the context of income and wealth inequality in the US, some of the new-rich billionaires (a large number of which made their money through the asset inflation, which the Fed created with its quantitative easing policies) now provide advice on how to reduce the inequality. Usually, the advice (I am not sure it is well-meant) centers on higher taxes for the super-rich (except for their own taxes, which they hope to lower with even more loopholes), and education. Specifically, these billionaires seem to *know* how the government should spend more money on education. I find these proposals quite amusing except for the fact that spending on education may have actually contributed to growing wealth and income inequality.

It seems the US is already spending far more on education than any other OECD country (see Figure 1). Unfortunately, the productivity of education (spending per student and academic achievement) seems to confirm that the US has not only an extremely expensive educational system, but also one that produces poor results (see Figure 2). [I concede that US education produced at least one genius: he sits in the White House.]

Figure 1: Annual Education Spending (Tertiary/Early Childhood Education) by Countries (in US$ per student), 2016



Source: OECD

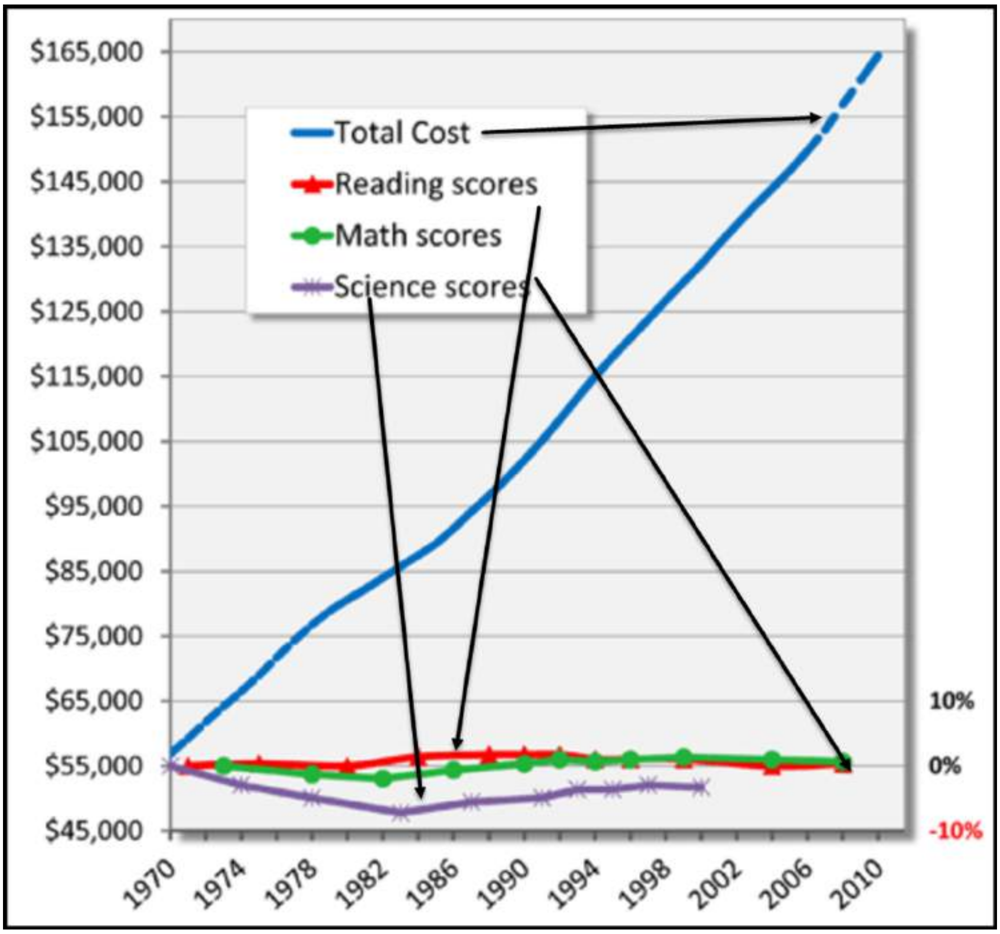
Figure 2: 2018 Final Ranking of the World's Best Education Systems

1. South Korea
2. Finland
3. Norway
4. Russia
5. Hong Kong (PRC)
6. Japan
7. Estonia
8. Latvia
9. Israel
10. Sweden
11. Lithuania
12. Denmark
13. Ireland
14. Taiwan Province (PRC)
15. Kazakhstan
16. Slovenia
17. Georgia
18. Singapore
19. Cyprus
20. China (PRC)

Source: OECD, New Jersey Minority Educational Development (NJMED) Organization, www.worldtop20.org

I am always skeptical about these sorts of rankings (especially finding Russia, Latvia, Estonia, Lithuania, Kazakhstan and Slovenia ahead of Singapore), but there are numerous other studies which seem to confirm that the US spends an increasing amount of money on education with poor outcomes (see Figure 3). This is also true of health care where the US government spends far more on a per capita basis than the OECD average but where the quality is no better than in other OECD countries.

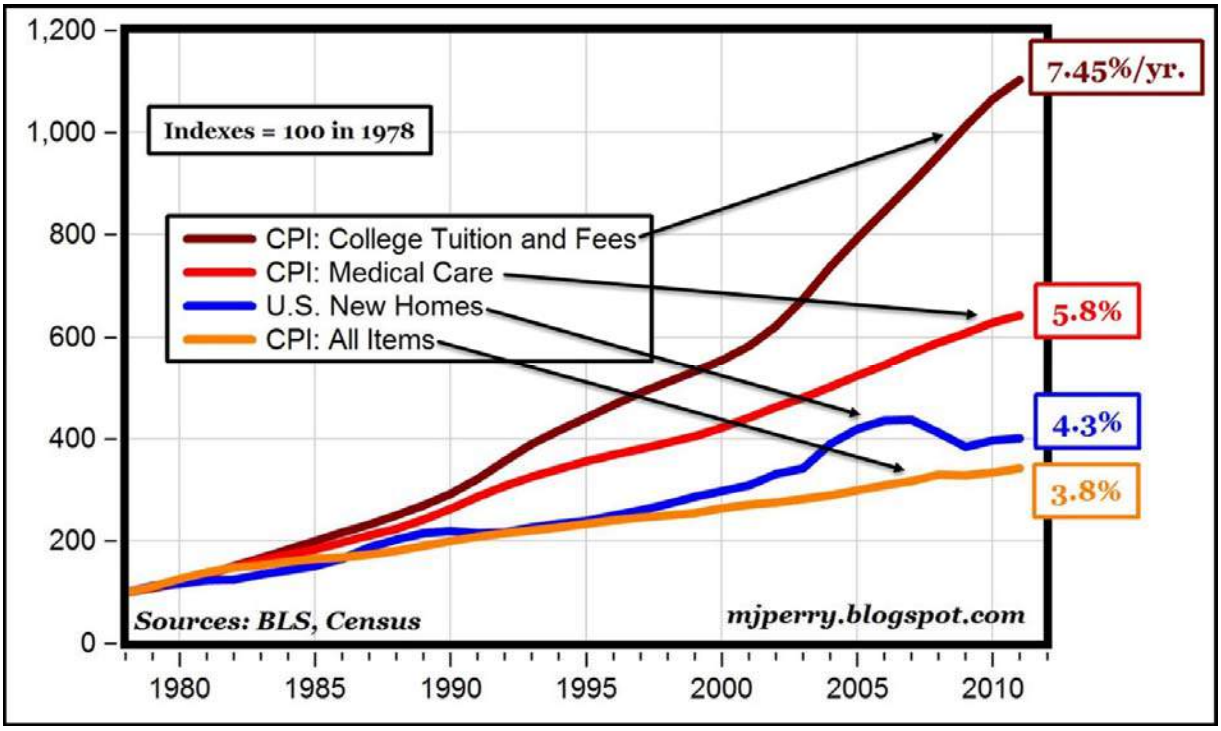
Figure 3: Trends in inflation-adjusted Cost of a complete K-12 public Education ($ scale), and Achievement of 17-Year Olds (% scale), 1970 – 2012



Source: Andrew J. Coulson, Director, Cato Institute Center for Educational Freedom ("Total Cost" is the whole amount spent on the K-12 education of a student graduating in the given year).

The reason I am revisiting education in the US (I wrote about this sector previously) is, as just mentioned, that some of the billionaires think wealth and income inequality can be reduced through better education, and also because of a *Wall Street* article (see April 11, 2019) which argues that *College Wouldn't Cost So Much if Students and Faculty Worked Harder* by Richard K. Vedder. [Richard Vedder is a Senior Fellow at the Independent Institute, Distinguished Emeritus Professor of Economics at Ohio University, and the author of *Restoring the Promise: Higher Education in America*.] I find the title of Professor Vedder's article very appropriate because it is a fact that college tuition costs have risen far more than medical costs and the CPI (see Figure 4).

Figure 4: College Tuition versus Medical Care versus Home Prices versus CPI: All Items 1978 – 2011



Source: Professor Mark J. Perry's Blog for Economics and Finance

Vedder: "One reason college is so costly and so little real learning occurs (see Figure 3) is that collegiate resources are vastly underused. Students don't study much, professors teach little, few people read most of the obscure papers the professors write, and even the buildings are empty most of the time.

The New York Federal Reserve says more than 40% of recent college graduates are "underemployed," but many already are while in school. **Surveys of student work habits find that the average amount of time spent in class and otherwise studying is about 27 hours a week. The typical student takes classes only 32 weeks a year, so he spends fewer than 900 hours annually on academics—less time than a typical eighth-grader, and perhaps half the time their parents work to help finance college.** [MF: I assume that students at engineering, law and medical schools need to work far more.]

It wasn't always this way. As economists Philip Babcock and Mindy Marks have demonstrated, students in the middle of the 20th century spent nearly 50% more time—around 40 hours weekly—studying. They now lack incentives to work very hard, since the average grade today—a B or B-plus—is much higher than in 1960 when the average grade-point average of around 2.5 implied a typical grade of B-minus or C-plus.

I'm part of the problem: I've been teaching for 55 years, and I assign far less reading, demand less writing, and give higher grades than I did two generations ago.

Learning takes time, so the diminution of effort surely means students are learning less. Snippets of data confirm that suspicion. Sociologists Richard Arum and Josipa Roksa have demonstrated, using the Collegiate Learning Assessment, that the typical college senior has only marginally better critical reasoning and writing skills than a freshman. Federal Adult Literacy Survey data, admittedly somewhat outdated, shows declining literacy among college grads in the late 20th and early 21st centuries. A civic literacy test administered by the Intercollegiate Studies Institute shows appalling gaps in knowledge, with seniors knowing very little more than freshmen. Only 24% of graduates know that the First Amendment prohibits the establishment of an official church.

As for the faculty, the Education Department doesn't publish annual data on teaching loads, but some hard data plus considerable anecdotal evidence suggests the typical professor is in class around one-third fewer hours than his 1965 counterpart. At my mid-quality state university (Ohio University), I taught three courses a week for nine hours in 1965; my colleagues today teach only two courses for six hours. At some top-flight research universities, senior professors may teach only one course.

The excuse is that professors today are publishing more research. True, but why? Mark Bauerlein at Emory has documented that in English (literary criticism), the volume of research is immense—but little of it is often cited or even read. [MF: I doubt anyone reads all the papers that are published by researchers at the FED.] Why should professors reduce their teaching loads to write papers for the Journal of Last Resort? **Diminishing returns have long since set in**.

The litany of underused resources goes on. In 1970 at a typical university there were perhaps two professors for each administrator. Today, there are usually more nonteaching administrators than professors."

MF: According to the analysis of federal figures, by the New England Center for Investigative Reporting in collaboration with the non-profit, nonpartisan social-science research group the American Institutes for Research, "The number of non-academic administrative and professional employees at U.S. colleges and universities has more than doubled in the last 25 years, vastly outpacing the growth in the number of students or faculty, according to an analysis of federal figures. **The disproportionate increase in the number of university staffers who neither teach nor conduct research has continued unabated in more recent years, and slowed only slightly since the start of the economic downturn, during which time colleges and universities have contended that a dearth of resources forced them to sharply raise tuition.**

In all, from 1987 until 2011-12—the most recent academic year for which comparable figures are available—universities and colleges collectively added 517,636 administrators and professional employees…..'There's just a mind-boggling amount of money per student that's being spent on administration,' said Andrew Gillen, a senior researcher at the American Institutes for Research. 'It raises a question of priorities.'

Universities have added these administrators and professional employees even as they've substantially shifted classroom teaching duties from full-time faculty to less-expensive part-time adjunct faculty and teaching assistants, the figures show…….

Part-time faculty and teaching assistants now account for half of instructional staffs at colleges and universities, up from one-third in 1987, the figures show" (emphasis added in each instance).

Vedder: "Even the buildings don't work very hard. Most classrooms and faculty offices are deserted in June, July and August, and often for much of May and December. Even in peak academic months, classrooms are typically seldom used in late afternoons and often not on Fridays.

To be sure, there are many exceptions. On some campuses, students study much more. Engineering majors probably work much harder than communications or gender-studies majors. And there are professors who are in their offices more than a few hours a week. Students in law and medical schools often work very long hours. Many hard-science researchers spend much time in their labs.

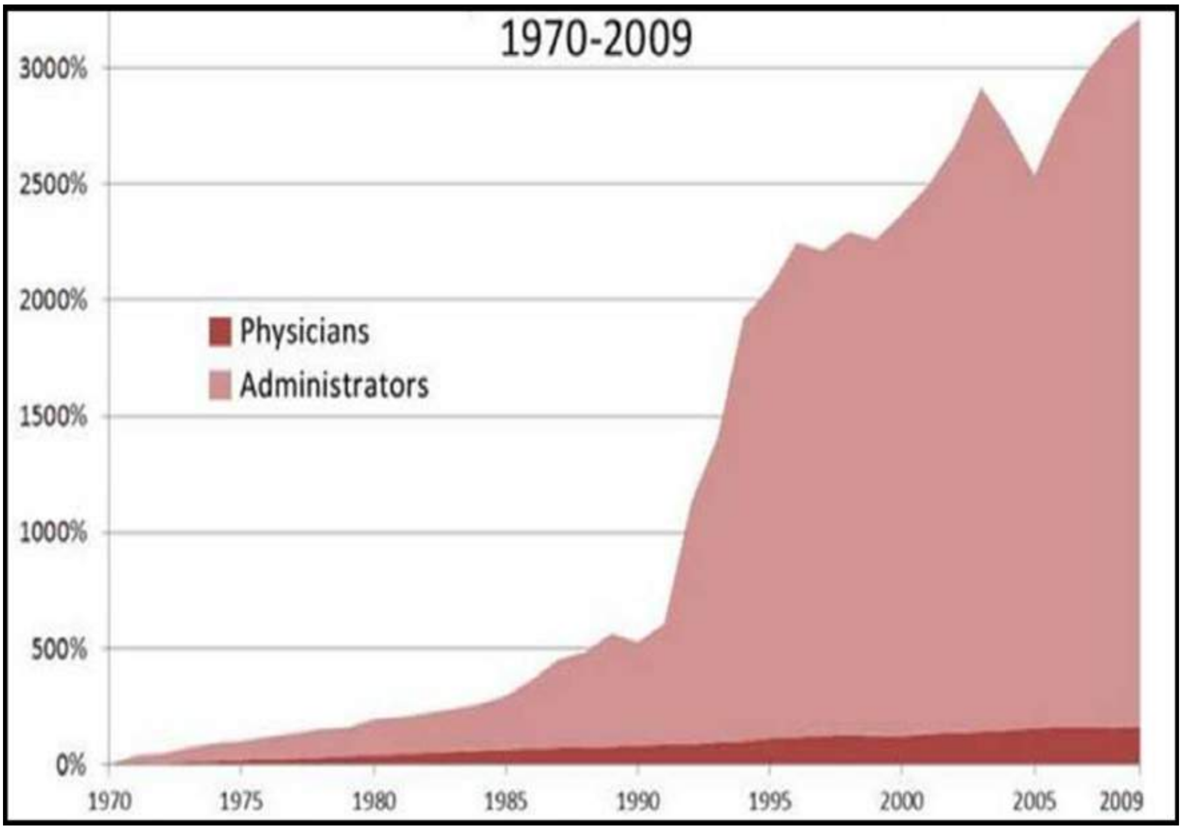
Still, Time Use Survey data from the Labor Department suggest that students spend more time on recreation and partying than on academics, and most professors are not often found during daytime hours in the office, classroom, laboratory or the library. [MF: I have great sympathy for this time allocation as it is better not to learn anything than falsehoods. Thomas Jefferson: "He who knows nothing is closer to the truth than he whose mind is filled with falsehoods and errors."] Where are they? What are they doing? Why can't students and faculty show the same work ethic that made our market-disciplined nation the wealthiest place in history?" (emphasis added in each instance).

MF: Above, Vedder pointed out that, "**The disproportionate increase in the number of university staffers who neither teach nor conduct research has continued unabated in more recent years**"…. What I find interesting is that disproportionate increase in the number of administrators is not confined to schools and universities but is evident in practically every industry. One of the more stunning cases is the explosion of administrators in the health care industry (see Figure 5). Vedder explained above that in 1970 at a typical university there were perhaps two professors for each administrator. Today, there are usually more nonteaching administrators than professors. I forgot where but a reader recently made some comments on a blog about government spending. He opined that, "high taxes don't make for a better society. If it did, NYC, Philadelphia, Boston, Chicago, San Francisco, and all of New Jersey would be utopian societies. Instead, people are fleeing them. The vast majority of taxes today are used by politicians to buy votes and cement special interest support. Take school taxes. 2/3 of it goes to salaries, benefits and pensions. Practically nothing goes toward "the children." [Reminds me of charities like the Red Cross – *ed. note*.] Philadelphia spends over $20,000 per child per year with dismal results. Catholic schools, in the same neighborhoods, at 1/3 their costs have dramatically better results.
Teacher unions are some of the most powerful unions that exist. No democrat could be elected without their support. So poor teachers cannot be fired, failing schools cannot be changed, disruptive children cannot be disciplined and school choice is a fantasy."

MF: In the health care industry, it is not much better. The ratio of administrators has exploded compared to the number of physicians (see Figure 5).

In my opinion, in both cases, of the education and of the health care industry, the cost have increased far above the CPI Index (see Figure 4) because of more government regulations, which forced educational institutions to increase the number of their administrators. I also assume that schools, universities and the entire health care industry are also faced with soaring insurance costs because of endless litigations over malpractices. The fact is simply that the US spends almost twice as much as European countries on a per capita basis on both education and health care (see Figure 6).

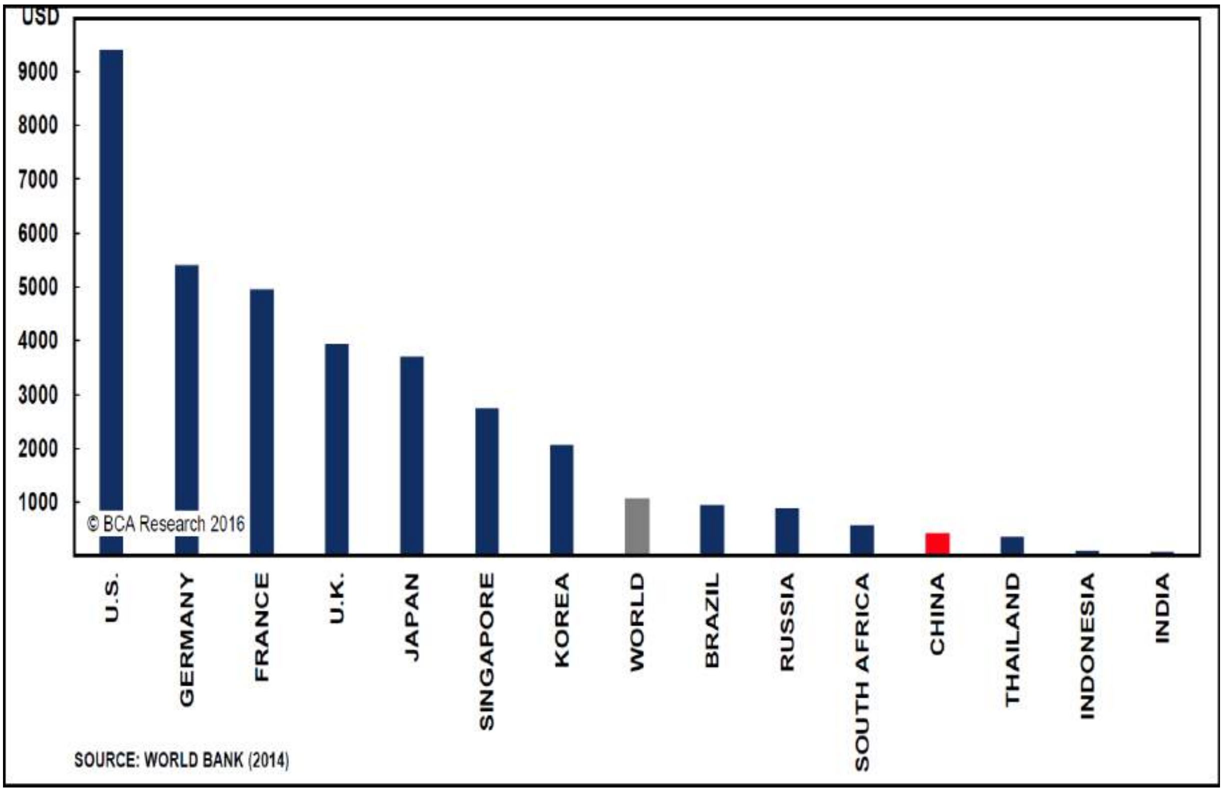
Figure 5: Growth of Physicians and Administrators, 1970 – 2009



Source: Bureau of Labor Statistics, NCHS; and Himmelstein/Woolhandler Analysis of CPS

What prompted me to write once again about education is not only that so many billionaires are recommending for the government to spend more money on education and Richard Vetter's article about how little students spend time on studying and professors on teaching, but also a Bloomberg article by Noah Smith entitled *The Great American College Boom Is Winding Down* (see Bloomberg April 18, 2019).

Figure 6: Health Care Expenditures per Capita in US Dollar, 2014



Source: World Bank, The Bank Credit Analyst

According to Smith, "The for-profit college industry is collapsing. The Chronicle of Higher Education reports that during the past five years, more than 1,200 college campuses have been closed -- an average of about 20 every month. Of those that shut, 88 percent were for-profit, and their students amounted to 85 percent of those affected by the closures: Enrolment at four-year for-profit colleges is in free fall, dropping 13.7 percent from fall 2014 to fall 2015, 14.5 percent the following year, and 7.1 percent the year after that. **Perhaps the only surprising thing was that it took this long**. For-profit colleges have long been plagued by poor performance - a 2012 study by economists Kevin Lang and Russell Weinstein found no earnings premium from attending a for-profit university. Follow-up studies yielded similar results. But the price tag for these colleges was high, and students were encouraged to take out lots of loans to pay it. **The inevitable result**

was a generation of for-profit college students with poor employment prospects and a mountain of debt."

MF: This is an important point in the discussion about wealth and income inequality. There is a large difference in income and assets for students that completed their studies with "mountains of debts," which they accumulated because of student loans, and students who completed their studies without debts because they either had parents who had saved for their children's education or **because they themselves worked in part-time jobs while studying** (see Figure 7).

Figure 7: Median Net Wealth (25-34 year Olds), 1989 and 2013 (adjusted to 2013 dollars)

25-to-34 year-olds	Degree without Debt	Degree with Debt	No Degree
1989	$125,572	$86,547	$16,322
2013	$75,000	$6,600	$7,750

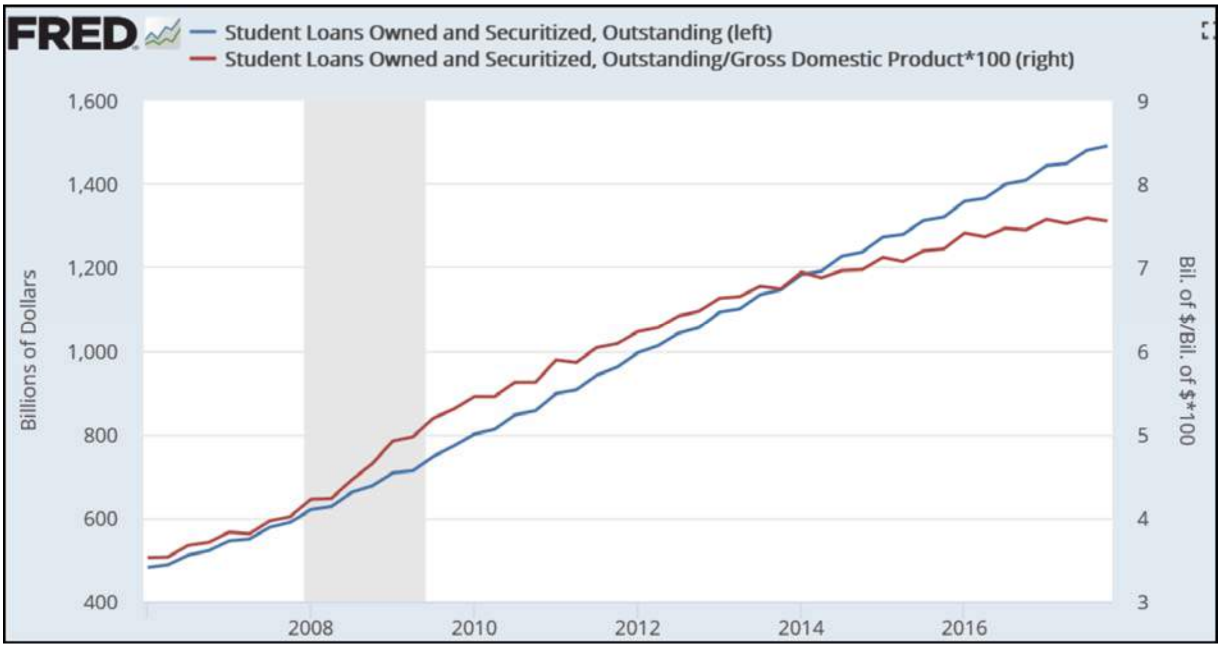
Source: Young Invincibles, Analysis of Survey of Consumer Finances (adjusted to 2013 dollars)

From Figure 7, we can see that for the 25 to 34-year olds the median net wealth in real terms declined between 1989 and 2013. However, if you look at the column under "Degree with Debt" you will notice that between 1989 and 2013 there was a complete collapse in median net wealth. The reason for this collapse in net wealth is that student loans have exploded (see Figure 8). Student loans are a form of financial aid that are *supposed* to help students access higher education. Student loan debt in the United States has been growing rapidly since 2006, rising from $480.1 billion (3.5%) of GDP in the first quarter of 2006 to nearly $1.56 trillion by 2019, roughly 7.5% GDP. [Student loans usually must be repaid, in contrast to other forms of financial aid such as scholarships, which never have to be repaid, and grants, which rarely have to be repaid. Some experts contend that the increased usage of student loans has been a significant factor in college cost increases.] According to Wikipedia, "approximately 45 million people have student loan debt. [Compared to most nations, student loans play a significant role in U.S. higher education. Nearly 20 million Americans attend college each year, of whom close to 12 million – or 60% – borrow annually to help cover costs.] In 2018, the average student loan borrower owed $37,172 in student loans at the time of graduation, an increase of $20,000 from 2005. In 2017, Americans owed approximately $552 billion more on student loan debt than they owed on credit card debt.

Student loan debt is unevenly distributed. Approximately 30 percent of all college students do not incur debt. Student loan defaults are disproportionately concentrated in the for-profit college sector. The schools with the highest amount of student loan debt are University of Phoenix (owned by Apollo Education Group), Walden University, Nova Southeastern University, Capella University, and Strayer University. [As an aside, University of Phoenix students owe more than $35 billion in student loan debt, the most of any US college. In 2014**, University of Phoenix was highlighted in a Time.com article entitled *'The 5 Colleges That Leave the Most Students Crippled By Debt'*** – *ed. note.*]

In 2018, the National Center for Education Statistics reported that the 12-year student loan default rate for for-profit colleges was 52 percent. The 12-year student loan default rate for African Americans going to for-profit colleges was reported to be 65.7 percent."

Figure 8: Outstanding Student Loans in the US, 2000 – 2018



Source: Federal Reserve Bank of St. Louis

Noah Smith of Bloomberg: "Meanwhile, a whiff of dubious marketing hung about the industry, with DeVry University being forced to pay a $100 million settlement for misleading prospective students about the economic benefits of attending.

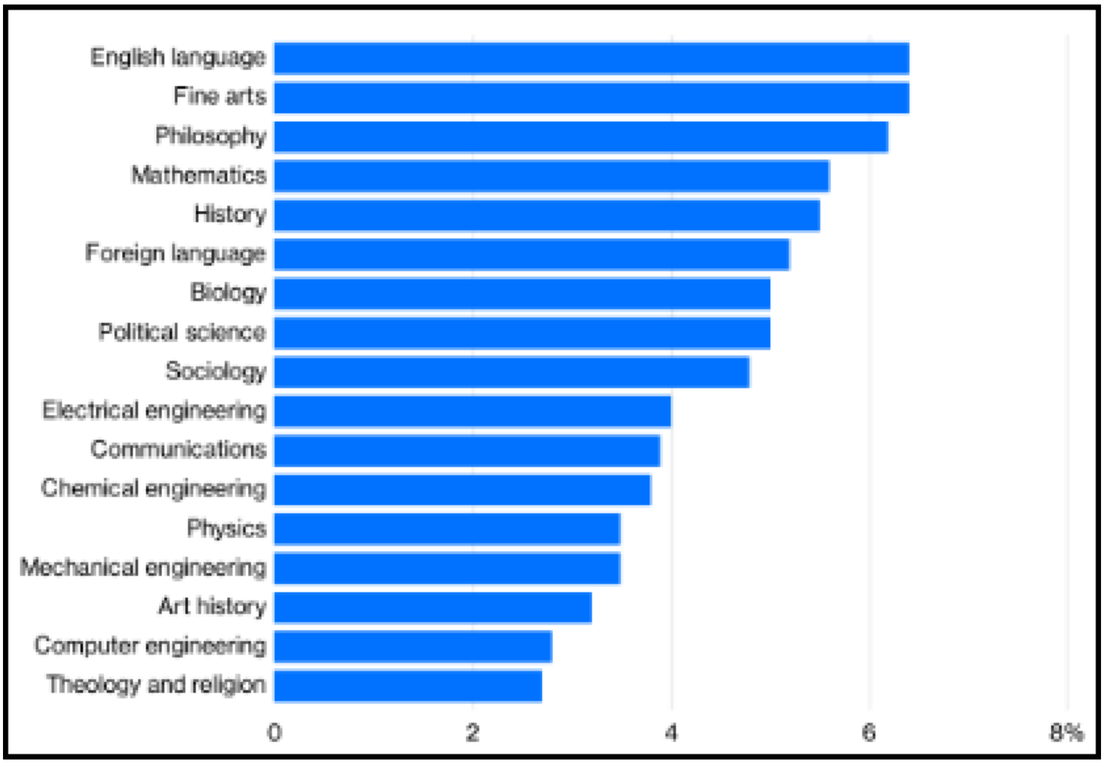
The winnowing of the for-profit college industry shows that although it can take years for poor quality and high prices to reduce demand in the education sector, eventually it does happen. Fortunately, for-profits only account for a relatively small slice of undergraduate education -- perhaps about a tenth. **The more important question is whether the carnage among for- profits is a harbinger of similar declines for non-profit and public colleges**."

MF: Above, Smith stated that, "a whiff of dubious marketing hung about the industry." In fact, the for-profit education industry is fraught with unethical, immoral, and fraudulent practices. Several publicly listed for-profit companies including Apollo Education Group and Corinthian Colleges were some of the short sellers' favorite targets. [Corinthian Colleges was closed by the State of California in 2015. Then California Attorney General, Kamala Harris, stated that Corinthian Colleges targeted single parents who were close to the poverty level, a demographic that its internal documents described as "composed of 'isolated,' 'impatient,' individuals with 'low self-esteem,' who have 'few people in their lives who care about them' and who are 'stuck' and 'unable to see and plan well for future,' through aggressive and persistent internet and telemarketing campaigns and through television ads on daytime shows like Jerry Springer and Maury Povich." The company was founded in 1995. By 1999, it was taken over by some Wall Street financiers. It went out of business in 2015.] Apollo Education Group was founded in 1973. It went public in 1994. [In 2008, Apollo Group formed a joint venture with Carlyle Group (a politically well-connected group), called Apollo Global, to make international acquisitions. Apollo also purchased schools in Mexico and Chile.] In October 2011, Apollo Group still had a market capitalization of $5.36 billion, but following declines in attendances at its schools and falling earnings as well as numerous law suits, it was taken private in 2016 by Najafi Companies, a Phoenix firm, the New York-based Apollo Global Management and, the Vistria Group of Chicago for $10 per share, compared to its high of $89/share in 2009.

Noah Smith: " Why might demand for college be weakening? One reason is that there are simply fewer young people in the country these days: The reversal of Mexican immigration probably has something to do with that. Meanwhile, falling fertility rates will do even more to thin out the ranks of the young in the decades to come. U.S. universities could make up the difference by allowing in more international students, but President Donald Trump’s anti-immigration policies and attitudes have made that difficult; enrolment from overseas is now in decline.
The strengthening labor market might also be pulling a few young Americans

away from college, though so far that trend seems to be very slight.
Another possible factor is that prospective college students may be learning to distinguish between the economic opportunities afforded by various college majors. Overall, the earnings premium for a bachelor's degree has remained constant or continued to rise, depending on how it's measured. But those overall numbers conceal large differences by field of study: Unemployment rates also differ greatly between majors: This may be why college students are avoiding humanities majors (see Figure 9). But it could also mean that some prospective college students who don't want to major in fields like science, technology, engineering, math, health or business might avoid college entirely, or be unwilling to attend more expensive schools…"

Figure 9: College Major Unemployment Rate for recent Graduates, January 2018



Source: Statista, Bloomberg Opinion
[The low unemployment rate among Theology and Religion graduates may be due to the fact that hardly anyone still studies these subjects.]

Smith: Enrolment at four-year public and non-profit colleges has remained essentially unchanged during the past two years…… Whatever the reason, if the decline in demand for college continues, it could be bad for many regions of the

U.S. For more prestigious universities, falling undergraduate applications need not crush their plans for expansion. Most of the local economic benefit of a university comes from research, not from education. But a number of small towns owe their economic health to modest local colleges whose main activity is teaching; if these shrink or disappear due to falling college demand, the trend of local economic decline could accelerate. Government programs to make college more affordable for lower-income Americans can help prop up enrolment in these vulnerable areas. But universities also need to help by cutting costs. Addressing administrative bloat and other sources of inefficiency will allow public and non-profit colleges to make enrolment a more attractive proposition."

MF: For my non-US readers I need to explain that universities such as Yale, MIT, Stanford, Harvard, etc. are all so-called "non-profit" universities although, as Annie Lowrey explained under the title *Take Away Harvard's Nonprofit Status* (see Intelligencer of September 9, 2014) that, "There's an old line about how the United States government is an insurance conglomerate protected by an army. Harvard is a real-estate and hedge-fund concern that happens to have a college attached. It has a $32 billion endowment. It charges its rich students — and they are mostly from rich families, with many destined to be rich themselves — hundreds of millions of dollars in tuition and fees. It recently embarked on a $6.5 billion capital campaign. It is devoted to its own richness. And, as such, it is swimming in cash…."

[What prompted Annie Lowrey to write the article was that Harvard had just received the largest-ever gift of $350 million about which she was critical. Please also note that most journalists are leaning towards socialism – *ed. note*.]

Lowrey: "'But, wait!' you might say. 'That $350 million is going to support an educational institution with tremendous public spillover! Harvard does basic scientific research! It teaches doctors! It studies cells and stars and history and it educates underprivileged youths!'

True, true, all of it. Still, from a purely utilitarian perspective, there are causes that need that $350 million more. Groups like GiveWell are devoted to figuring out where a dollar does the most good. It recommends initiatives like deworming in very low-income countries. Harvard, at the same time, is spending a billion dollars upgrading its coeds' convenient, riverfront housing. If it wanted to maximize its $32 billion worth of utility, it could, say, admit more students, especially poor ones, reduce its focus on property development, and double down on its focus on research, which currently makes up $800 million of its $4.2 billion in annual operating expenses.

But there is a way to encourage the university to do that, or at least to ensure that it is also contributing more to the public good. That is to take away some of

Harvard's tax exemptions, as suggested by legislators in Washington and Massachusetts, as well as a number of economists. The idea is that such megarich schools hoard funds and real-estate, tax-free, to the detriment of local communities or federal coffers, a situation that could be remedied with a wealth tax on endowments over $1 billion, property taxes, or a tuition sales tax.

Harvard and other universities are the Platonic ideal of nonprofits in a technical sense, and thus exempted from paying taxes like businesses do. The school does not distribute its operating profits as dividends. It has no shareholders. It does not exist to make anyone rich. Yet nevertheless, it is rich, as are a several other universities in its cohort. Harvard manages about $32 billion, Stanford about $19 billion, and Yale about $21 billion (emphasis added).

All that money can have some perverse effects. Harvard, for instance, has purchased a tremendous amount of land in Cambridge and the surrounding towns — pushing up real-estate prices without contributing much, if anything, in property taxes. If the school lost its nonprofit status, it would owe the state of Massachusetts $80 million a year. (The $350 million donor owns $100 million of real estate in Harvard Square, by the way.) For now, it owes close to nothing on its land or its investment portfolio.

Were it to face the burden of some taxes, Harvard might shift its strategy. And 'if donors knew that the money they bequeathed to their alma mater would partially or fully be heading to the state,' wrote the Harvard Crimson debating the issue back in 2008, 'they would think twice before writing that check.' Exactly."

MF: I began this report by saying that all kinds of billionaire experts think that the inequality which causes the current social tensions in the US and other Western democracies should be addressed with more spending on education. I quoted Richard K. Vedder (*College Wouldn't Cost So Much if Students and Faculty Worked Harder*), Noah Smith (*The Great American College Boom Is Winding Down*), and Annie Lowrey (*Take Away Harvard's Nonprofit Status*) because I wanted to show some of the problems associated with education and specifically that the educational institutions are a racket-like organization, which most likely contributed to the rise in income and wealth inequity. As I insinuated above, some of the for-profit educational institutions were fraudulent and who preyed on poor people (see Kamala Harris comments above) with aggressive marketing campaigns and exaggerated claims about the career prospects of their students.

Naturally, they also encouraged these people to finance the education of their children with student loans, which were highly profitable for the lender. Over the years, I had numerous young readers of this report telling me that the biggest mistake they ever made was to study and incur large student debts, which they had problems repaying. [Figure 7 above, clearly shows the difference in wealth between students who were in debt and those who were debt free.]

While I am extremely critical about the business models of the for-profit college industry (I used to follow both Apollo and Corinthian rather closely) we also need to be fair. As Vedder pointed out above, the average amount of time students spends in class and otherwise studying is about 27 hours a week. "The typical student takes classes only 32 weeks a year, so he spends fewer than 900 hours annually on academics—less time than a typical eighth-grader, and perhaps half the time their parents work to help finance college."

In other words, it looks as if a large number of students nowadays are completely disinterested to study hard and to acquires skills that would help them later in life earn a decent living. Also, to be fair to the for-profit college industry we must realize that it competes with non-profit and non-tax paying colleges, which puts them at a huge economic disadvantage. As Annie Lowrey showed above, Harvard and other Ivy League schools are *non-profit* on paper, but in practice they and their teaching staff are profit-driven. Professors at famous universities often reach star status and earn high incomes because of the books they publish, and their speaking engagements and consulting agreements. Furthermore, a large number of universities receive funds from China and have set up universities in China (in return they do not bring up Chinese human rights abuses in Tibet and Xinjiang). There is nothing particularly wrong about these practices, but should the institutions, which benefit financially from this capitalistic behavior be tax-exempt? [Should churches and all kinds of foundations be tax-exempt? I do not think so but I understand some of the arguments in favor of these institutions tax-free status.]

Going back to the idea that wealth and income inequity could be addressed by spending even more money on education, my view is that money is not the problem in the US but that the efficiency and the productivity of the educational sector must be improved. [Just look at Figures 1 and 2 where it visible that Europe's Nordic countries spend half as much on education per capita but achieve far better results.]

However, as long as so much money flows through the American educational system (a better description would be to use "as long as so much money flows through the American educational racket") abuse, corruption, fraudulent and unethical practices will flourish, and will even be encouraged by Wall Street, and prevent any meaningful reforms (see Figure 10).

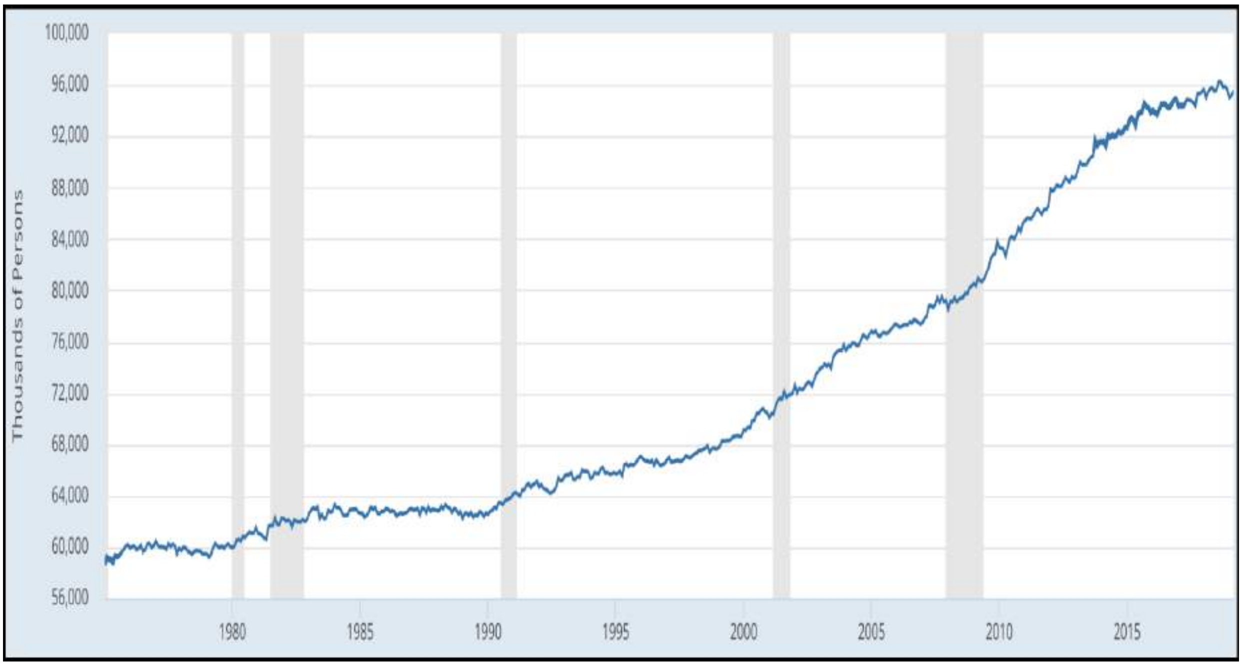
Figure 10: Approval of Student Loans and Admissions at US Universities

Source: Mike Baldwin, Andrews McMeel, www.cornered.com
[Please note that for the admission at top universities the cases are filled not with beer but with bank notes.]

As an aside, French President Emmanuel Macron just announced that he would under pressure from the Yellow Vest protesters shut down Strasbourg's Ecole Nationale d'Administration. [The school was founded by Charles de Gaulle in 1945 to train a post-war elite drawn from across social classes. However, over time it became a symbol of the French establishment.] Macron explained that the move was not about 'stigmatising' the school where he himself and three of the

previous five Presidents were educated but about opening up the civil service which he called 'no longer meritocratic.' [Will the American socialists and world improvers one day also demand the closure of Ivy League universities?]
I hate to use harsh words and to be overly critical but aside from some elite schools the American educational system seems to be an expensive failure. Otherwise how would you explain the large number of working age Americans who are not in the labor force? (see Figure 11). [My friend Grant Noble who publishes an excellent daily comment opined: "Education and healthcare take up about half of our economy and both are almost complete frauds" - gnoble@sbcglobal.net]

Figure 11: Working Age Americans not in the Labor Force, 1973 – 2019

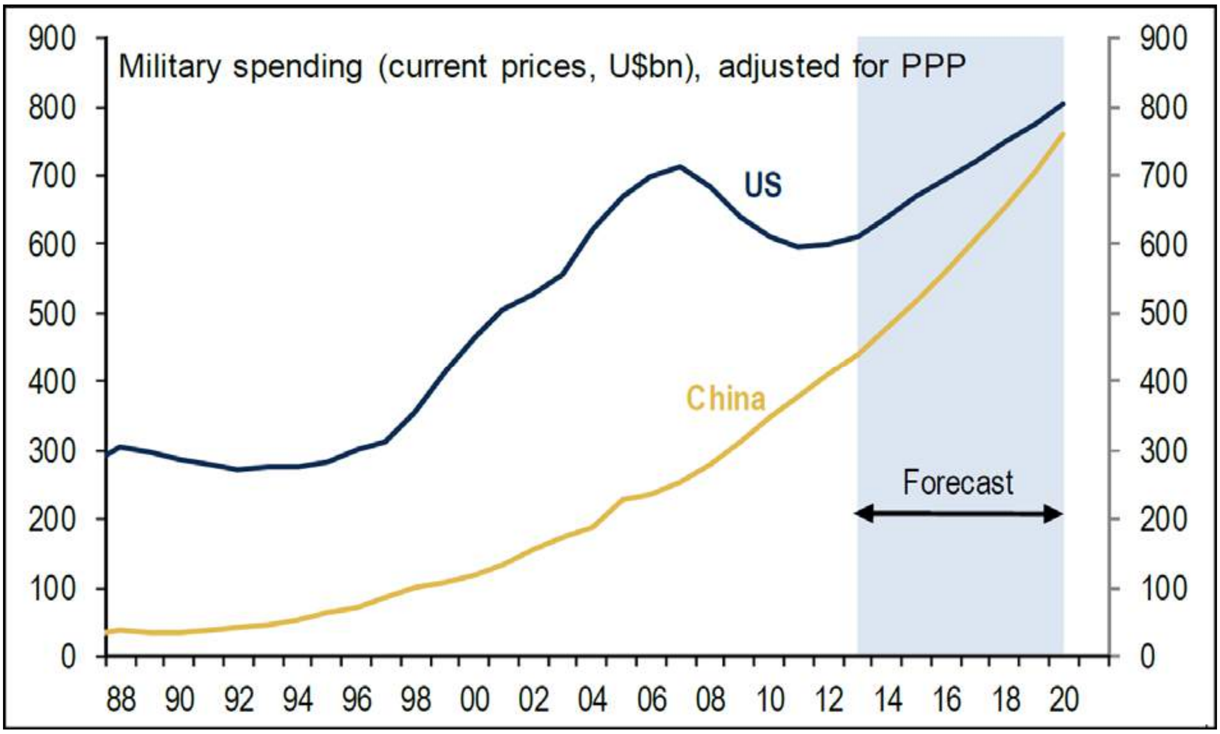


Source: US Bureau of Labor Statistics, Federal bank of St Louis, Michael Snyder, The Economic Collapse [Please note the rapid increase in people not in the labor force after 2000.]

Companies want to hire employees but cannot find suitable people because they have the wrong skill sets (or more likely no skills at all). Therefore, we can see that the working age Americans are not in the labor force for macro-economic reasons (unemployment is at a record low – at least according to published statistics). But they are *not* in the labor force because their skills do not match the demand side for labor, which increasingly requires special skills.

Now, let us assume that the US education system is an expensive failure and let us further assume that it is a microcosm of two other large sectors of the US economy: healthcare, and government and especially defense. I then ask myself why these sectors are so bloated, expensive, and inefficient. The answer is that these sectors have enormous political power because of their size. Furthermore, since these sectors generate huge profits for their insiders (numerous billionaires) these powerful people have zilch interest to change the status quo. [The guiding principle is that "No billionaire should be left behind.] I purposely included the military complex because although the defense department spends far more than any other country in the world its inefficiencies will become a problem as China boosts its defense expenditures (see Figure 12).

Figure 12: Military Spending (current prices, US$ billion), adjusted for PPP, 1988 – 2019



Source: Ajay Kapur, BofA Merrill Lynch Global Research, SIPRI, IMF

I should add that in January 1961, shortly before retiring, President Dwight Eisenhower gave the nation a dire warning about what he described as a threat to democratic government. He called it the *military-industrial complex*, a formidable union of defense contractors and the armed forces: "In the councils of government, we must guard against the acquisition of unwarranted influence, whether sought or unsought, by the military-industrial complex. The potential for the disastrous rise of misplaced power exists, and will persist."

As I explained above, "misplaced power" also exists in the educational and health care sectors where costs have not only risen far in excess of the CPI but are also the highest in the world on a per capita basis (see Figures 4 and 6). However, all these sectors (including defense) are now being scrutinized by voters and their representatives, and are under pressure to cut costs, which accounts for the recent weakness in their stock prices (see Figure 13). [Bernie Sanders as President would be extremely negative for the health care sector.]

Figure 13: UnitedHealth Group (UNH), 2016 – 2019

Source: www.stockcharts.com

The Health Care Sector ETF (XLV) is down 9% from the October 1, 2018 peak and is no higher than it was in January 2018. At the same time, the NASDAQ Biotechnology ETF (IBB) is down 20% from the July 2015 high and down 12% from the October 1, 2018 high (see Figure 14). I am bringing the health care sector up because it clearly shows that although some US stock indices have made new highs most stocks are far below their highs in 2018 or even earlier.

Figure 14: Biotechnology ETF (IBB), 2014 – 2019

Source: www.stockcharts.com

Furthermore, the all-time favorites of 2018, the FANG and related stocks have not been able to exceed their late summer/autumn 2018 highs (see Figure 15). The

NYSE FANG Index is still down by 10% from the July 2018 peak. However, the FANG Index could still make another high driven by just one single stock. I am mentioning this because the Philadelphia Stock Exchange Semiconductor Index (SOX) recently made a new all-time high (5% above the March 2018 high), but only very few semiconductor stocks made new highs (see Figure 16).

Figure 15: NYSE FANG Index (NYFANG), 2017 – 2019

Source: www.stockcharts.com

In fact, of the 30 components of the SOX Index, I am only aware of three stocks that recently made new highs: QUALCOMM (QCOM), Taiwan Semiconductor (TSM), and Intel (INTC). QUALCOMM, however, is still down 15% from the 2000 high and TSM and Intel - following the weakness over the last few days - are lower now than in January 2018. [Intel is also down 32% from the 2000 high.] As an aside, Nvidia (NVDA), the undisputed darling of the millennial investment community in 2018, and a component of the SOX Index is down 39% from the October 2, 2018 high. [Investors who want to short some equities should consider shorting the SOX Index.]

Figure 16: Philadelphia Stock Exchange Semiconductor Index (SOX), 2017 - 2019

Source: www.stockcharts.com

I want to stress that a stock index can make a new high with *only* one or just a few stocks making new highs while the majority of stocks languish far below their earlier highs. [This oddity makes it easily possible to manipulate the market. In fact, observing the US stock market action every day rather closely, my suspicion is that someone is manipulating not only economic statistics but also the stock market. Now, I happen to know somebody who is obsessed with the stock market and only measures the success of his company, which happens to be – aside from tweeting endlessly - the running a rather large country, by the increase in stock prices.]

Also, I have to say that the performance of the SOX Index so far in 2019 is one for the history books. The fundamentals of the semiconductor industry have been deteriorating since the last quarter of 2018, but the SOX Index happily ignored the worsening outlook and climbed in 2019 a new high. [Although down from the recent high, the SOX Index is up 45% from the December 26 low.]
But my readers should not think that the diverging performance between stock and fundamentals are unique to the semiconductor sector. www.sentimentrader.com recently published a chart showing the divergence between "Wall Street Target Price Changes" and "Wall Street Analysts Earnings Estimate Changes" (see Figure 17)

Figure 17: Wall Street Analysts have been raising price Targets on S&P 500 Stocks while lowering at the same time Earnings Estimates, 2018 - 2019

Source: www.sentimentrader.com

We can see from Figure 17, that usually earnings estimates and changes in target prices (as well as stocks) move in concert. The recent diverging trend will have to correct shortly. Either earnings estimates will recover or price targets and stocks will decline. Lately, we have seen that stock prices are *not* immune to disappointing earnings. On Friday, April 26, Intel (market cap: $234 billion) fell 9% in one day to $52 (high in 2000: $75). Xilinx (XLNX) fell 15% in two days.

Furthermore, I have written before about Illinois Tool Works (ITW) and 3M (MMM, market cap: $110 billion) being excellent *global* economic indicators because both companies serve just about every industrial and consumer market around the world.

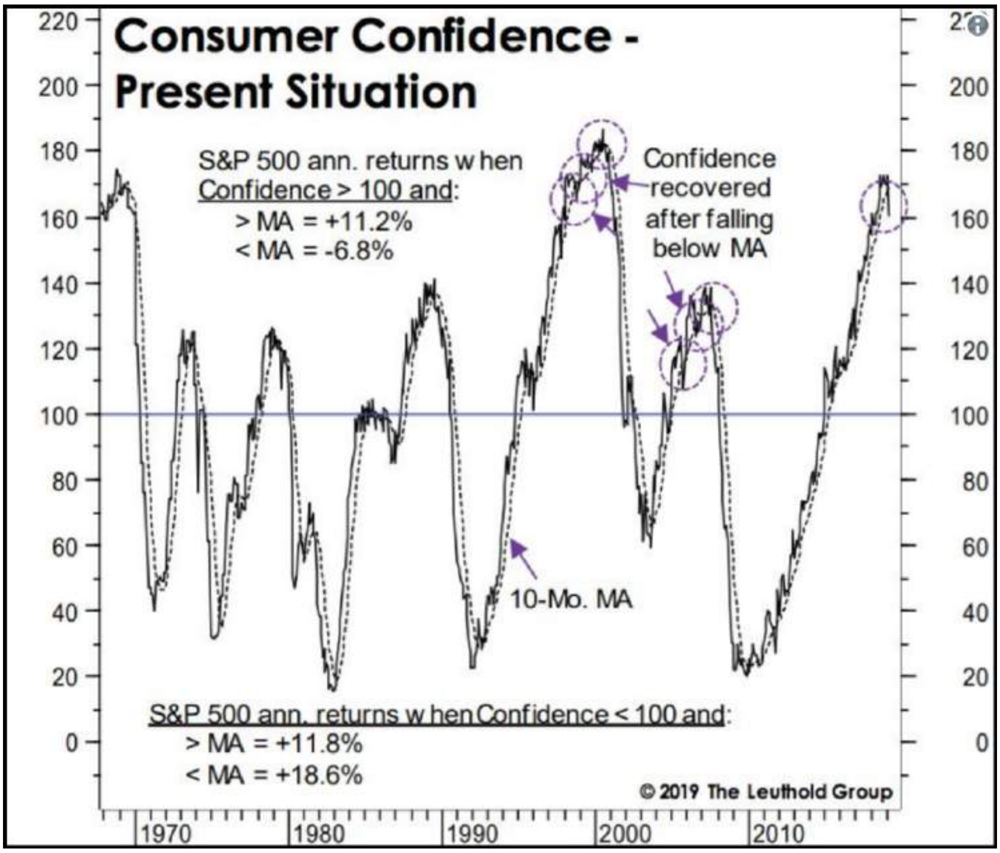
Well, on April 25, 3M (MMM) dropped by 11% in one day (see Figure 18).

Figure 18: 3M (MMM), 2016 - 2019

Source: www.stockcharts.com

What is interesting about MMM being one of the most reliable global economic indicators is that the stock peaked out on January 26, 2018, and never since approached this high ($260), even though the S&P 500 eked out a marginal new high on September 21, 2018 at 2940 (intraday high). MMM, which down 27% from the January 2018 high seems to indicate that the global economy has slowed down considerably and that some industrial and consumer markets are already in recession. This fact seems to be also confirmed by express delivery companies such as FedEx (FDX) and UPS (UPS) - both down 32% from the January 2018 highs (on April 25, 2019 UPS fell by 8%). But not to worry! Americans are an optimistic lot and are confident about the economy and equities moving higher (see Figure 19). However, we can clearly see that high readings of Consumer Confidence coincide with stock market tops whereas low readings accompany market lows. Moreover, future stock market returns are far lower when consumer confidence is above 100 than when consumer confidence is below 100 (see Figure 19).

Figure 19: Consumer Confidence – Present Situation, 1968 - 2019

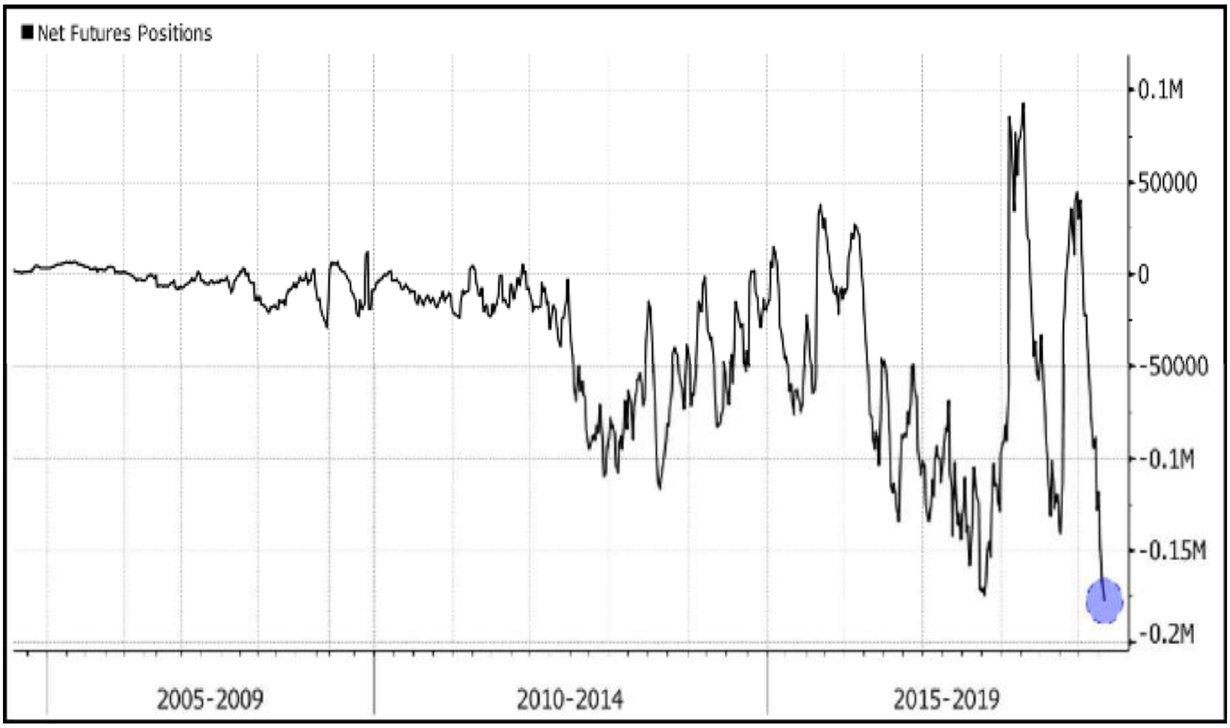


Source: The Leuthold Group, Jesse Felder, The Felder Report

18 months ago, I was negative about the outlook of cryptocurrencies (including Bitcoins) because just about everybody I knew at Linda Bar in Chiang Mai, a bar I frequent, told me that they were making money trading cryptocurrencies. [I bought some Bitcoins earlier this year when the price dropped

below $3,500.] More recently, I met several people that told me that they were "trading volatility." In this context I found a Bloomberg article interesting, which stated that hedge funds were "shorting the VIX at a Rate Never Seen Before" (see Bloomberg of April 26, 2019). Bloomberg: "As equities surge to all-time highs, volatility has all but vanished. Hedge funds are betting the calm will last, shorting the CBOE Volatility Index, or VIX, at rates not seen in at least 15 years (see Figure 20). Large speculators, mostly hedge funds, were net short about 178,000 VIX futures contracts on April 23, the largest such position on record, weekly CFTC data that dates back to 2004 show. Commonly known as the stock market fear gauge, aggressive bets against the VIX are, depending on your worldview, evidence of either confidence or complacency…..**The VIX rose this week, but still remains below 13 – more than 30 percent below the gauge's average over the last 20 years**. While the VIX inched higher, so too did stocks, the S&P 500 rising to a new record" (emphasis added).

Figure 20: VIX Positioning: Speculators' Net Short VIX Positions, 2004 – 2019



Source: CFTC, Bloomberg

Above, Bloomberg stated that, "aggressive bets against the VIX are, depending on your worldview, evidence of either confidence or complacency."

My friend Peter Boockvar (**Peter.Boockvar@bleakleyadvisory.com**) who is a keen observer of financial markets recently stated: "While I'm not an ardent believer of the magazine cover/article effect because the timing of the opposite happening is impossible to predict, it's still worth taking note in terms of gauging sentiment. Over the past few weeks we've seen this:

1)**https://www.bloomberg.com/news/articles/2019-04-17/did-capitalism-kill-inflation**
2)**https://www.bloomberg.com/opinion/articles/2019-04-24/history-s-longest-bull-market-gets-a-new-lease-on-life**

3)**https://www.barrons.com/articles/this-bull-market-has-no-expiration-date-51554510445**

I should add to Boockvar's observations about positive investors' sentiment that a well-known technical analyst, famous for his bearish views about equities, now thinks that the Dow is in an "expanding triangle" formation, and that the final high would likely occur in 2021……

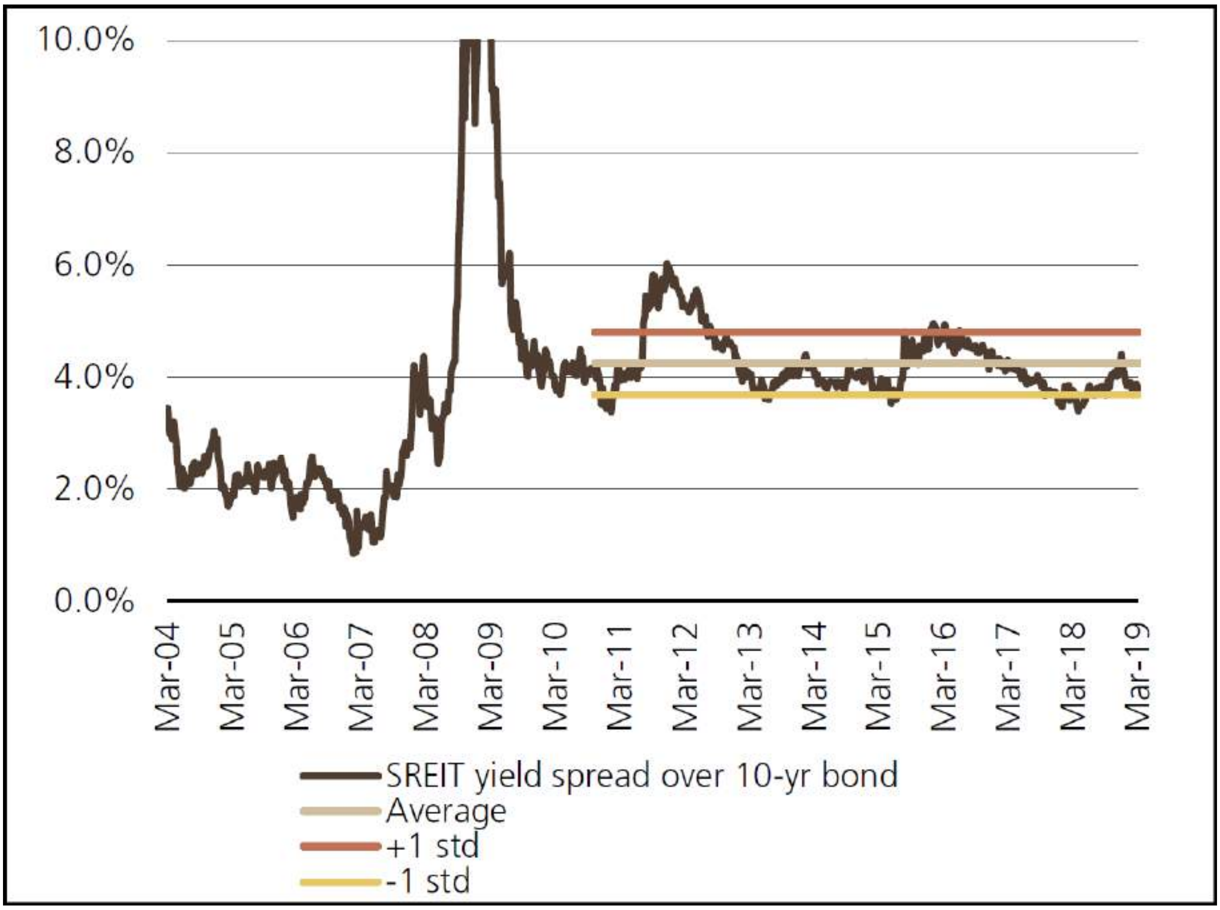
Expanding triangles after a lengthy advance are also called "Broadening Top Formations" and are stock market tops with just about the most bearish price implication that one can imagine. Personally, I doubt the US stock market will move up until 2021 because the market internals look poor and actually continue to deteriorate. **In fact, I think there is a good chance that the US stock market has already topped out, and that a more meaningful correction is dead ahead of us**.

But, let us assume that the bulls are right and that the US stock market continues to move up until 2021. In this scenario I believe that Asian (including Japanese) and European stocks would out-perform the US. Last month, I listed some European financials, which I owned including **Swiss Re (SREN SW), Zurich Insurance (ZURN SW), Swiss Life (SLHN SW), AXA (CS FP), and ING Groep (INGA NA), banks such as UBS (UBSG SW), Credit Suisse (CSGN SW), Intesa Sanpaolo (ISP IM), Banco Santander (SAN SM), Standard Chartered (STAN LN), and Deutsche Pfandbriefbank (PBB GR).** [I am considering buying some French banks.] I mentioned that European stocks were inexpensive compared to *negative* interest rates on European government bonds. I previously mentioned that I also owned Veolia Environnement (VIE FP). Last month, I purchased a position in Suez (SEV FP), a French water supplier and water treatment company.

The other day I received a report by UBS about Singapore REITs, which argued that Singapore REITs were no longer inexpensive and that UBS would recommend a switch from REITs into Singapore banks. [Aside from agricultural commodities and gold shares I do not find any inexpensive assets.]

It is true that following Singapore REITs strong performance some of their attraction has diminished. It is also a fact that Singapore REITs' yield spread over ten-year Singapore Government bonds have declined (see Figure 21). However, under the scenario that the US stock market would continue to move up until 2021 and that "capitalism" killed "inflation" the yield spread could approach the 2007 lows (see Figure 21). Therefore, I am reasonably happy to hold my Singapore and Hong Kong REITs.

Figure 21: Singapore REIT Dividend Yield, 2004 – 2019



Source: UBS

On Friday, April 26, when the US reported strong GNP figures, US Treasuries rallied, which is a *bullish* sign. I still believe that US Treasury yields could decline further as the economy weakens. I admit that the endless US fiscal deficits and the prospect of a weaker dollar are negative factors, which really concern me.

Needless to say, I still hold precious metals and mining stocks. **Whereas most stocks in the US are forming longer term tops, precious metals and gold shares are in corrective phase that will likely give way to a further powerful advance within the next three months**. [My current favorite is Platinum.]

I am enclosing a link to an interview with Kevin Smith of Crescat Capital, which reflect my views as well, and lays out the bear case. [Crescat Global Macro Hedge Fund was up 41% in 2018, and the Crescat Long/Short Hedge Fund was up 32%.] I strongly recommend my readers to take 15 minutes of their time to watch the interview because Kevin Smith is one of the few people who really knows what he is talking about:

https://www.realvision.com/tv/videos/end-of-the-cycle

As explained above, we can no longer trust governments. This applies especially about economic statistics. Therefore, we need to analyze statistical data critically. Niccolo Machiavelli opined:

> **"For the great majority of mankind are satisfied with appearances, as though they were realities, and are often more influenced by the things that seem than by those that are."**