

Something to Think About



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COMMON CENTS

I got a number of emails in response to last week's newsletter, and let me say one thing: I am not advocating the US Treasury blithely print a bunch of additional money. No; the point was the quickest cure for deflation and a crippling strong currency is to simply make more of it, and pronto. Quantitative easing and deficit spending are as slow as molasses by comparison.

Then, I would like to add: what a difference a week makes! No, we probably aren't completely out of the woods, but the mood of the market seems to have changed pretty dramatically in a relatively short period of time. In truth, while we aren't expecting massive results this year, we made no bones about it to our clients: unless something completely unpredictable happens, something way out of the ether, the markets will likely be higher at the end of the year than they were before this week's rally.

That wasn't an out on a limb prediction, as much as putting a reasonable level of profit growth and an historically acceptable Price/Earnings multiple into an equation. Should the dollar continue its lazy stroll lower against other major trading currencies, 2016 could end up being better than anyone originally expected. After all, negative currency translation effects have put the screws to what should have been more robust profitability at many US multinational corporations. We are talking about tens of billions of dollars 'lost' to US investors due to the accounting of foreign currencies.

If we can only keep our currency from rallying 9.3% and 12.8% like it did in 2015 and 2014 respectively! The best way of doing that is to keep the Fed on the sidelines. No, before I get any emails, I am not advocating kidnapping Fed officials or even blockading their access to FOMC meetings. However, modest GDP and inflation numbers until the rest of the world catches up would be nice, really nice.

Yep, a tidy little 5% rate of decline in our currency would be good for what 'ails' us. You know, the more I think about it, the angrier I get at the Fed for starting a tightening cycle well after our currency had gone through the roof and the yield curve flattened as much as it had. To that end, the spread between the yield to maturities of the 2 year US Treasury and the 10-year was 2.647% on 12/31/2013. It was 1.407% on 11/30/2015.

In other words, the markets had already done a lot of the Fed's work for it. Overseas demand for US dollars had been so strong, there was no way inflation would rear its ugly head, at least not to worrisome levels. Throw in an employment to population ratio of 59.6% relative to the 30-year average of 61.8%, and you have to wonder just what part of the Fed's so-called 'dual mandate' was so compelling as to threaten corporate America with an even stronger US, read reporting, currency!?

Want to balloon our trade deficit and reduce corporate earnings? Ratchet up the overnight lending target in the face of less than compelling evidence, and wait for good things to happen.

However, the Fed took backseat this week to the clamor over Apple's encryption software. Consider this passage from theguardian.com published yesterday, 2/18/2016:

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Any sufficiently advanced technology is indistinguishable from magic.

Arthur C. Clarke

Something to Think About Cont.

“Two weeks ago, the FBI called Apple’s headquarters in Cupertino, California, with a jarring message: the agency wanted Apple to help them hack an iPhone. Apple refused.

The request stepped up a level on 16 February when a federal magistrate ordered Apple to help the FBI unlock a single iPhone – the phone belonging to one of the killers in the December mass shooting in San Bernardino, California. Apple again refused.

But this carefully planned legal battle has been months in the making, US officials and tech executives told the Guardian, as the government and Apple try to settle whether national security can dictate how Silicon Valley writes computer code.

Both sides expect the ensuing legal battle to have far-reaching implications that will touch on encryption, law enforcement, digital privacy and a 227-year-old law from America’s post-colonial days.’

Apple’s actions in this case require some context. In September 2014, Apple introduced new encryption into its iPhone operating system that would make it mathematically impossible for the company to unlock them for investigators. This was a departure from the past, when investigators could get access to a device if they sent it to Apple headquarters with a search warrant.

The shift was in response to increased digital privacy concerns and distrust of America’s digital spies following revelations from former National Security Agency contractor Edward Snowden.

Since then, FBI director James Comey has been trying to figure out a way around the software as he and Apple’s Cook have traded barbs publicly and privately. Comey hit a snag, however: the Obama administration didn’t want to pick a fight with one of America’s most popular – and valuable – companies.”

As I type, it appears the tech industry is siding with Apple, and a protracted, politically charged battle will undoubtedly unfold. At first blush, the average American might wonder why Apple won’t cooperate with the Feds in this case. I can certainly understand this, as I initially wondered the same thing.

Then I wondered: here we have an organization, the US Federal government, which has sent men to the moon, missions to Mars, split the atom, has a \$4 trillion budget, can kill people from outer space, and spends over \$50 billion each year on so-called non-military intelligence AND it can’t hack into a single, lousy iPhone?

One word: unbelievable.

Is it a question of can’t or won’t, on both sides? From outward appearances, it would seem the government is incapable of deciphering Apple’s encryption. Surely they can, right? Or is it they just don’t want to bother with doing it? One has to wonder, and the longer the government keeps fighting the company the more you have to think it simply isn’t able to do it. And, yet, there are hackers around the world capable of breaking into mainframes with more firewalls than you can imagine....even the Federal government’s.

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Something to Think About Cont.

I don't know about you, but I think this is a great commercial for Apple's technological prowess. "Buy an iPhone...the FBI, CIA, and NSA can't hack into it." Here I was thinking they could do so all along, but maybe I have seen too many Jason Bourne movies.

In truth, this is an amazingly slippery slope. While the government's request may seem reasonable in light of the recent tragedy in San Bernardino, is it really so hard to imagine this precedent, if it comes to that, opening a Pandora's Box of sorts? Of course not. It could go from national security interest to public interest to general good in no time flat. The problem with that is all of those terms are sort of nebulous, completely subjective, and, besides, just how many judges and magistrates are there in the United States who get to interpret such things? Further, just how difficult is it to get a search warrant? Oh, then we have a whole bunch of subjective terms like reliable witness, probable cause, and public interest.

Of course, the kneejerk reaction is: it doesn't matter unless you are hiding something. Perhaps, but what is the old expression: one man's trash is another man's treasure? What might seem innocuous to you might be some big smoking gun to an overzealous bureaucrat who has been able to tap into your phone in the name of the public good.

This whole situation reminds me of a few lines from the very funny movie **Raising Arizona**. If you haven't seen the movie, no amount of my explaining the plot will help you. If you have seen it, you will immediately understand my point here:

Nathan Arizona Sr.: I got the cops and the Federal BI out there lookin' for my boy...

Leonard Smalls: Cops won't find your boy. A cop couldn't find his butt if it had a bell on it.

Leonard Smalls: You want to find an outlaw, hire an outlaw. You want to find a Dunkin' Donuts, call a cop.

So, yeah, the word unbelievable sticks with me. It is unbelievable Apple's technology/encryption is so robust the government can't figure it out. That doesn't compute, pun intended. What's more, it is unbelievable the various spying/security agencies don't have some criminal mind types working on hacking stuff all the time, and I mean a whole regiment of them. Shoot...give some kid at Cal Tech \$100K to break into the thing; it is worth a shot.

In the end, all of this makes me very happy we are overweight technology and own Apple in client accounts. Simply put, the US technology industry is the best in the world, and if you don't believe me, just ask the FBI.