

FRIDAY, OCTOBER 13, 2023

Well, hello and welcome to this week's Dividend Cafe. It has been quite a week and in a lot of ways, a very somber one. I don't refer to the market, which is actually up and up quite a bit. If you go back to where the bottom was last Friday and where I'm speaking right now, we're not at the close of the day in the market yet on Friday. So maybe things change before the close. But from an intraday Friday of last week to intraday Friday this week, the Dow is up by 850 points. But what I refer to in terms of this time of kind of somberness is obviously the massive attack on Israel by the Hamas terrorist organization last Saturday, and that has now created a significant hotspot and uncertainty around the Gaza Strip, and indeed a significant portion of what will happen out of the Middle East. I wrote the written Dividend Cafe this morning very early from my apartment here in the city and I made the comment that it's interesting to me that so many of these things seem to happen, I affiliate a lot of the major events over the last 20 plus years, 25ish years in New York and for me around markets I more recently, the opening salvo of the COVID what became this long shutdown and all the things that followed But being in New York that week as markets were utterly collapsing and walking through the city early in the morning It felt like a ghost town and eventually leaving the city of my family and thinking we'd be gone a week or two and ended up being a few months and all That stuff but that wasn't a terrorist attack per se.

The events of 9/11 are obvious when you talk about market sensitive events and catalysts to a lot of market uncertainty, obviously we know the great financial crisis the fall of Lehman

FRIDAY, OCTOBER 13, 2023

and these things are all centered right here with Wall Street and the financial center and I was heavily present in that time. So I just, I don't know, it may not be something other people think about the same way I do, but I associate a lot of these things with being here and there's a sense in which I believe that what happened this week with the Hamas attack on Israel really does require a bit of a refresher in history, and it's not specific to 9/11. It's not specific to COVID. It's not specific to the Great Financial Crisis. It's very different because those things were all market events, and this has not been a market event yet. It could become one, and I'm going to talk about how that could end up happening. But as of right now it's just this awful human tragedy of violent aggression and hate and against our democratic ally and friends. And you, the reason I refer to the uncertainty going forward is that I don't think anybody really believes it's over. I don't think anyone believes that, Israel is gonna stop until they understandably seek to protect themselves, their own interest and eradicate those who had done this.

And I think it's that could go in a number of different directions. And right now, markets are obviously dealing with a lot of other things. Primarily the drop of bond yields, which has rallied bonds and rallied stocks, which have been heavily correlated asset classes for some time. And that did not change at all this week.

And so perhaps that's all that stocks have experienced this week as a little piggyback with the bond market. But. It also

FRIDAY, OCTOBER 13, 2023

could change very quickly if you end up getting some sort of issue between Israel and Iran or there is a secondary retaliatory attack from the retaliation from the initial attack.

And we don't really know. And I, so it just provoked me this week to think about how investors, the people I speak to. Nobody wants or should want any geopolitical advice from me. The foreign policy ramifications of this are not my area of specialty. I remain interested in the sense that I think all people who strive to be thoughtful and all people who are patriots have some sort of discernible belief system in their life, which I don't know how many people I'm describing anymore.

But, I do want all those things, but I'm not an expert in foreign policy. And yet I do have a responsibility to apply all these things to portfolio management, to real investor outcomes on behalf of our clients. And so coincidentally, I was walking this morning to a symposium that had not happened in person last couple of years around all the COVID stuff, but that I had I have attended in person every year since the financial crisis here in New York and been a part of the particular speaker.

He's been a mentor of mine since I entered the business. And so I did the Dividend Cafe this week to combine a lot of these things. New York, the events of that took place in Israel, market potential fallout around geopolitical distress, foreign policy disruptions, and the takeaways that have meant so much to me out of my friend Nick Murray.

FRIDAY, OCTOBER 13, 2023

So that's what we're going to talk about here. Let me just basically say that I think everyone listening and watching knows what took place last weekend at the updated numbers right now are that it was over 1300 Israelis killed on the day of that's the most killed in a single day. In from, in Israel, from an action like this of any day since the Holocaust and over 3000 were wounded as well and we don't even really know how many are hostages, but they believe that number to be 97, and that number could end up proving to be higher or lower. By the way, there are, as of press time, 27 Americans that are known to have been killed. Originally, they thought it was 8, then I think it went to 14, then it went to 22, now updated to 27 and there are 14 that are missing. So those are either presumed to be potential hostages, or God forbid, also possible additional fatalities. An isolated terror attack, you could refer to as just another act of savagery without deeper connections to nation states, without some of the ramifications that this does.

But there is expected blowback here from a very highly capable and resourced nation, and that is the democratic former government that is Israel. And I think they feel an existential and indeed a very passionate burden to protect themselves for very obvious historical reasons and very obvious and admirable forward looking reasons.

It's not merely an economic story but when you look at the capacity of where this could go, it could become an economic story, a market story, something of investor concern very easily. And so that's why Dividend Cafe has to address it. I think that

FRIDAY, OCTOBER 13, 2023

The idea of Israel handling it on their own, they're really capable, they're really resourced, and they are going, I believe, to approach this with all the tenacity that a country determined to protect itself should, would, and can.

And yet, remember there are 9 million people and they're surrounded by 500 million other people who are not democratic nations and who a very significant portion of which desire their eradication. And so, they don't have a lot of great options that doesn't involve the support of western allies, including that of their friends in the United States.

And I think that that some form of escalation above just, airstrikes on the terror group of Hamas, it's very likely and as a press time there keeping with Geneva and protocols, for example, they ordered, I think it was 1100 Palestinians to evacuate northern Gaza, which presumably reflected their intent to be doing something there.

I airstrikes or maybe a ground invasion, which is what I think more and more forecasting. I don't know where it's gonna go, the news accounts don't, and I probably have better resources I'm talking to than your basic newspaper would and my sources that I'm speaking to don't know, and so, all I can tell you is, that there's, this isn't done.

I pray that the violence and hatred or the hurt damage done to Israel from the Hamas side is done, but I think this thing has more innings here ahead and I would not read into the markets

FRIDAY, OCTOBER 13, 2023

33,000 to over, I think we're at 33,850 as I'm speaking now, that's a big move and it may not be indicative of where things are going from here.

The markets can move up or down for a lot of different reasons. It's not single or mono causal, but I also want to bring up oil. It dropped four to five percent in the immediate aftermath. It dropped a little later in a week on Thursday, but then this morning was back up. And as I'm speaking, it was around 86 a barrel.

I don't think oil between 75 and 90 is in a market impact zone. I don't think it becomes a very big deal. It's oil way, way down from here. That is probably indicative of either massive global demand erosion, which is absolutely nowhere in sight. Or massive glut of supply, which is nowhere in sight.

And so the risk is skewed to the upside, and that risk well above 90, getting to the hundreds. That could have come even if none of this with Hamas Israel had ever happened. And it may very well come because in the aftermath of Israel's situation, that Iran's capacity or ability for daily output drops significantly if right now they're above three million barrels per day, which they are in terms of addition to world to global supply, and that comes down below two million or one million a day, then you know, you're looking a big price impact, not to mention other potential supply shocks.

FRIDAY, OCTOBER 13, 2023

So there's a lot of reasons that upside risk exists to oil, not just Middle Eastern, but it's another one that one may or may not materialize. But when you add that to the other things that we already know are happening that, I think that there, it creates second, third, fourth order effects that could very much complicate the Middle East situation, and the risk curve is definitely pushed up in terms of where oil prices may go.

So I put a chart in [dividendcafe.com](https://dividendcafe.com) of oil prices movement over about five decades worth of various economic events, but also Middle East and geopolitical events. And look, there's been times of huge demand factors forcing oil way down. Obviously 2008, 2020 with COVID was a pretty good one. And excess supply points like in 99, 2014, late 2014 into 15 was a big one.

And you've seen oil spike around invasions and geopolitical distress, war events, 1980, 1990, 2010, Arab Spring starting and of course in 2022 with Ukraine, Russia. So oil's been very responsive to geopolitics a lot over the years. And I think that this is a heightened risk in what was already a risk out of these Middle East developments.

The question is contagion and I think of contagion as when there's a debt event, and one party not being able to get paid by another party threatens their ability to pay a third party. And the impact to the third party, who is not a part of the debt event, Now it becomes a part of the debt event because of this counterparty risk that one or two or three steps down hits them.

FRIDAY, OCTOBER 13, 2023

That's what contagion risk is normally thought of in a financial market context. And with oil or excuse me the kind of foreign policy of this, it's what happens now between Saudi Arabia and Iran? What does China end up doing? If there are hostages killed, what does the U. S. end up having to do?

There's a lot of uncertainty here. And I'm setting the stage for what I want to say about the history of all this. But the contagion risk could be country by country contagion. And you're talking about a very vulnerable spot already. And so when we think about this from an investor standpoint, being prepared for the notion of unexpected contagious events.

Now, some would say, well, look, why don't we just sell everything and go to the sideline? And again, I think that in one week, you got an example.

In one week, you got an example of why that could be very dangerous. Markets had been selling off in September, and you actually had quite a rally this week despite all these events. And one could argue it's 5%, one could argue it's 50%, that nothing ends up coming of this in the markets as a result of Israel doing what it has to do.

There's no way for anyone to give a number other than pulling it out of a hat. It could be 80%, it could be 20%, no one knows till we know. And then when we know it, the number either becomes 0 or 100 very quickly, right? I guess what I would say

FRIDAY, OCTOBER 13, 2023

is, as uncomfortable as it may be, I'd encourage you to think about this in the context of before last Saturday.

Was Israel threatened by neighbors who hate it, or neighboring groups, organizations? that hate them before last Saturday? Oh, they sure were. And has there been significant uncertainty in the Middle East before last Saturday? I think that's safe to say. So, the evil isn't new, the barbarism isn't new, this particular event is new, but the reality of human nature is, right now, a risk going forward.

It was the events, it explains the events of this week, and it has been present. for a long time before last Saturday. And it is an embedded part of what we call the risk premium in markets. And risk premium is simply that premium of return. We want to do something with our investments above the risk free rate.

And so risk premium has to price in a lot of things at once. And one of the things that price is in is the reality of human nature. I'm talking about the existence of evil, the potential for barbarism, unpredictability, the uncertainty. Of what can be a very dangerous world that isn't new. And that is a part of the risk premium that all investors seek, whether they know it or not.

That's the kind of miracle of market risk pricing and discounting. So I made a little list to Dividend Cafe, just saying, okay, I'll only isolate this. More or less since I was born. Now, I'm getting up here to be 50 years old pretty quick and only

FRIDAY, OCTOBER 13, 2023

isolating to the Middle East. And the last 50 years, you actually had quite a bit of things happen outside the Middle East, too.

We'll just go ahead and ignore the whole Soviet Union thing, the Cold War, the significant amount of issues that we can go to in Africa and South America and Europe and other parts of Asia. The whole Vietnam War thing and Southeast Asian we'll just stick in the Middle East. And I'm going to read through this real quickly because it's a lot.

And by the way, I'm doing it from, I did it from memory. I'm right now reading from what I put in Dividend Cafe. But I know as a fact I could have come up with a lot more incidents. But I think you'll get the idea. In the last 50 years, speaking to Middle East, vulnerabilities. We had the Munich Olympic massacre, the young Kapoor war in 1973, the Arab Israeli war, seven day war, a full revolution in Iran in 1979, the U.S. Hostage crisis that was outside of that followed that 1979 when, The revolutionaries took our hostages after President Carter said he would let the Shah in America. A decade long almost, I think it was about eight years, civil war between Iraq, not civil war, a neighbor war between Iraq and Iran, a civil war that was over a decade long, really, in Lebanon, that 1982, 83, would frequently lure in United States, including one particular massive Beirut bombing.

The assassination of Egyptian President Amr Sadat. A plethora of hijackings that were internationally infamous. The TWA, 1985. The Akil Lora in 1985. The Abu Nadal, the Pan Am 103,

FRIDAY, OCTOBER 13, 2023

the Air France flight in 1994. Then you, of course, you had the first Gulf War after Saddam Hussein invaded Kuwait in 1990, the Gulf War beginning early '91.

We know of the first World Trade Center bombing in 1993. There was an attempted assassination of President Bush that we didn't know about until later, but that took place in April of 1993 by Iraqi agents. You had hundreds of smaller failed attempts at terrorism around the globe. A mass incident was attempted but avoided because of some failure or prevention, but nevertheless was an attempt at significant human terror. Hundreds. There was the Al Qaeda bombing of the U. S. Embassy in Nairobi in 1998, the Al Qaeda bombing of the USS Cole in Yemen in the year 2000 all giving way to the 9/11 attacks. here in New York and of course the Pentagon and on United States soil in 2001. The Afghanistan war that followed that, it removed the Taliban from power.

Twenty years later resulted in the Taliban coming back to power. All the suicide bombings, car bombings, too many to list out in the West Bank or Gaza often from Hamas themselves or Hezbollah against Israel. You recall the murder, kidnapping and subsequent murder of the Wall Street Journal reporter Daniel Pearl.

The Palestinian Intifada, I believe it was 2002 against Israel. The second Iraq war that we all know about beginning in 03 that lasted through an extended period of time and then

FRIDAY, OCTOBER 13, 2023

resulted in an uprising of Isis which became a massive multi geography venue for very violent terrorism.

There were the drone attacks on Saudi oil fields a number of years ago. And I just can't even tell you how many incidents I surely must be forgetting. I hope there's no major ones I'm forgetting, because it'll disappoint me if my memory's failing me that way. But, certain minor ones I understand.

There's just so many. But I think you get the idea. This is the norm in the region. It's the norm and unstable world, and I'm covering a 50 year period of time in all these different events. And when all this stuff started in the early 1970s, the S&P was at 92. The price level. The 500 companies of the S&P 500 index were at the number 92, and they're currently at 4,350.

In this period of time, the market is up 45X. The earnings of the S&P were 5.50 per share 50 years ago. The current earnings are 220 per share, 40 times. The dividends of the S&P were 3.19 per share, 1970. They're now 70 per share, up 23 times. Now inflation in this period is up about 8x, not 45x. Which is the S&P, not 40X, which is earnings, and not 23X, which is the dividends from the S&P.

But you, who are thinking the way I think, may immediately note, timeless principle applies whether you just want to use the S&P as I did, or where I'm about to go. But, beyond the empirical data, take note that 1970, when you bought the S&P,

FRIDAY, OCTOBER 13, 2023

That dividend yield was 3 percent. You were getting 3.19 of dividends off of an index trading at 92.

Right now, entering the dividend, the S&P, the yield is less than half of that. The total amount of dividends being paid out of the total amount of profits of the S&P is a 32 percent payout ratio right now. It was 58 percent when this started. So take all the principles of what I'm referring to, but plug it in to where there is dividend growth isolation, where your entry yield is not 1.6, but 4 percent where the entirety of companies are growing dividends and the dividend payout is significantly higher. And yet the world turmoil over the last 50 years has done what it's done and apply that right now to, as many of you know the way we think about managing money. I think that context.

Is incredible to think about and speaks to first of all, the gift of intentionality when it comes to managing dividend growth, but really just the nature of how markets absorb the uncertainties of the world. And I think I could have used any global turmoil. I think there will be needs and opportunities to give a similar message in the future.

It doesn't sit around the Middle East. This is the event of the week and it could become an event of several months. I don't know. But I do know this, there is zero chance that the next 50 years don't have a whole lot of bad things just like the last 50. And I only used 50 just to start in the 70s. I think most of the people listening are familiar with a lot of the headline events I just went through.

FRIDAY, OCTOBER 13, 2023

You could go a lot longer than just 50 years to highlight major world events. But markets ability to price in risk, to absorb, to pass through, to rationally. allocate. That's why you're invested. There are various disruptions that come along the way. They're not knowable. They're not timeable. The general reality is evergreen.

It doesn't need to be timed because it was and is and will be. And that is this massive moral infallibility of human nature that leads to atrocities like we saw last week. I don't know what happens next and when I just know that something will. And it ought not to alter a properly constructed portfolio.

It ought not to alter the lessons of history to that end. We work. Thanks for listening. Thanks for watching. And thank you for reading the Dividend Cafe.

---

Due to the publishing time constraints for us to produce our daily missive, podcast, and video, the best we can offer at this time is a machine-generated transcription which contains errors. We will continue to work to improve this service and appreciate your patience with us.