FINANCIAL PREPAREDNESS

"One of life's most painful moments comes when we must admit that we didn't do our homework, that we are not prepared." ~ Merlin Olsen

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The Plandemic Nearly Destroyed Investing

This week I've been updating my list of stocks that cut (usually eliminated) their dividends as the result of the government's response to the COVID-19 "pandemic." Those unfounded, disingenuous, extreme and tyrannical policies didn't lay waste to just lives, livelihoods, communities, education, mental health and our humanity. They also destroyed massive amounts of wealth at an unprecedented pace and nearly destroyed investing itself. This issue explains why.

Just like business is about making money (free cash flow, not reported earnings), investing is about receiving some of that free cash flow in the form of (ideally, increasing) dividends.

Yes, in theory, investors can benefit from stock buybacks, but invariably, corporate management uses free cash flow to buy back shares when times are good and their stock is already richly valued, just so they can exercise their stock options at an artificially high price. Afterwards, the stock quickly reverts to the market price, so the only shareholders who benefit from that are the ones who sell at that time. Management virtually never buys back shares during hard times when their stock is a bargain because they're trying to conserve cash (and their own paycheck).

Stocks that don't pay a dividend have value for at least two reasons. First, theoretically, eventually, the stock may start to pay dividends. For companies that have a low (or negative) return on invested capital, a long history of not paying dividends, low insider ownership, empire-building or featherbedding management, or sponsor workshops on how to "resist capitalism," this is not bloody likely.

Which leads us to a second possible reason why a stock that doesn't pay dividends may have value: its liquidation value, or what would be left after all of its assets were sold and all of its liabilities were satisfied. Due to limited information, the extremely small size of this market and the fact that a company in bankruptcy is a distressed seller, often there is virtually nothing left over for the shareholders. And if a company is heavily indebted, like so many are today after years of artificially low interest rates that encouraged them to binge on debt, there's even less of a chance that anything will be left for shareholders.

So companies that don't pay a dividend are basically dead men walking, and investors should therefore focus on dividend-paying stocks.

However, when the government shut down the economy in 2020, corporate revenue (as well as free cash flow) collapsed, which required hundreds of companies to reduce or eliminate their dividend. Stock prices (rightfully) collapsed as a result. Many of these companies went bankrupt, never to return.

Some became zombie companies, kept alive by the government's corporate welfare.

Some companies slashed their dividend to $.01 per share, which is a joke and an insult to shareholders, but it allowed them to still be considered by indices, mutual funds, ETFs and institutional investors that require a stock to pay a dividend.

I'm sure some companies didn't really need to cut their dividend, but used the opportunity as cover to get off the treadmill of having to pay cash to their shareholders each quarter.

Some companies simply stopped increasing their dividend each year, which during a time of high inflation means that the dividend is constantly being cut in real terms.

Some companies have only recently (after three years) reinitiated a dividend, but usually they are only about a third of what they were before.

The Great Financial Crisis of 2008 and the Plandemic of 2020 were like great earthquakes that made a large, existing fault line successively wider and deeper. Each time, the Fed and the government filled in the fault with millions of tons of paper currency, which made the ground appear level and even safer than before. At every level of society (government, corporate, consumer), people binged on the cheap debt offered by the Fed as an incentive to build near the fault line. Hell, in some cases, interest rates became negative, so some borrowers were actually *paid* to borrow money.

In such an environment, considerations such as dividend yield become almost superfluous. It reminds me of the investors who bought apartments in China 10-15 years ago who never bothered to rent them out because they were going to make such a large capital gain that any rental income would be *de minimis*. So artificially low interest rates over a number of years trained investors to believe that dividends weren't necessary for a successful investment experience, which caused them to bid up assets that pay little or no dividends. Who cares about a 3% dividend yield when you can make huge capital gains from cryptocurrencies, FAANG stocks, Tesla, pot stocks, meme stocks, SPACs, ARK ETFs, NFTs, stock options, etc.?

But below the surface, pressure from moving tectonic plates continues to accumulate, and one day, perhaps with little or no warning, there will be an epic earthquake that will exceed all known previous earthquakes by at least an order of magnitude.

So what would happen to such high-flying securities (including stocks that don't pay a dividend) if there was an unexpected, cataclysmic financial earthquake, and investors suddenly recalled, “Oh yeah, the value of an asset really is the present value of its future cash flows.” They would all come tumbling down like a tall skyscraper in San Francisco during the next Big One. No bids, just splat.

A long history of dividends paid, however, is *prima facie* evidence of at least possible if not probable future cash flows, which would greatly soften the blow. Dividends are strong circumstantial evidence (“as when you find a trout in the milk” ~ Thoreau) that a company is profitable, that it's confident in its immediate future, and that the interests of management are at least somewhat aligned with those of shareholders.

The bottom line is that due to the policies of the Fed and the government during and since the Plandemic, the next stock market crash/bear market/financial crisis will be severe, dramatic and prolonged. Beware of investments that give you nothing but a story. After doing this professionally since 1995, my B.S. detector is at a permanent maximum setting, so I require cash on the barrel in the form of dividends.

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