INNER CIRCLE

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The Absolute Best Way to Invest in America Today

Last week, we looked at Bill Bonner's Doom Index.

Although the index is sounding the alarm on overvalued S&P 500 stocks right now, it was surprisingly positive on the near-term prospects for the Main Street economy.

This week, we take a closer look at what's been happening in Main Street America.

I caught up with Nick Rokke, a chartered financial analyst who spent two years as Bill's head of research at *The Bill Bonner Letter* and who is now the lead analyst over at *The Palm Beach Daily.*

This week's expert just put boots on the ground in the Rust Belt — and found an industrial renaissance going on there

You see, Nick just returned from a tour of the Rust Belt. He put boots on the ground in his home state of Wisconsin as well as in Illinois, Ohio, Indiana, Michigan, and New York.

His mission: to find out whether President Trump's "America First" economic policies will help bring back manufacturing jobs… and spark a U.S. industrial renaissance.

Buy "America First"

Each week at *Inner Circle,* we bring you the best big-picture investment ideas from the global network of analysts Agora founder Bill Bonner has put together over his more than 30 years in the financial publishing business.

That mission doesn't often take us to Menomonee Falls, Wisconsin… Middletown, Ohio… Detroit, Michigan… or Buffalo, New York.

But according to Nick, there's a big-picture investment opportunity in the Rust Belt that almost nobody is talking about.

And if you own U.S. stocks, you need to know that there's a lot more to America than doom and gloom.

Because, as Nick explains below in this week's Q&A, the kind of big, internationally focused business most people are buying — the kind listed on the Dow or the S&P 500 — carries big risks in the Trump Era.

IN THIS WEEK'S ISSUE:

Instead, you should be focusing on smaller industrial firms that make and sell their products in the U.S. – what Nick calls "America First" stocks.

Q&A With Nick Rokke

Chris Lowe (CL): You recently put boots on the ground in the Rust Belt to get a better sense of whether President Trump's "America First" policies will bring factory jobs back home. What did you learn there?

Nick Rokke (NR): I learned that American industry is doing a lot better than most folks think. There is a manufacturing renaissance in the Rust Belt. This confirms what the Doom Index I helped put together for Bill Bonner is saying. [Catch up here.]

CL: Where did you start your trip?

NR: My first stop was in Wisconsin, just outside of Milwaukee in a place called Menomonee Falls, not too far from where I grew up. I went there to talk with a fund manager called Brian Rafn. He's the manager of the Morgan Dempsey Small/Micro Cap Value Fund.

Brian's fund invests mainly in small-cap industrial firms – the kind President Trump vowed to protect from offshoring. So it was a great way to get some expert input into what's going on with these businesses.

Brian's an interesting guy. He's a big gun enthusiast. When I met with him, he was strapped with a loaded handgun. And he was open about supporting Donald Trump for president. But when I asked him if Trump's policies had brought jobs back to America, he told me that jobs had started coming about before Trump took office.

That was surprising. It's certainly not the picture you get when you listen to the talking heads on TV.

CL: If it isn't the new administration that's responsible for the jobs coming back, what is the cause?

NR: Brian listed five reasons. The first, and probably the most important, is that China's cost advantage is shrinking. About 20 years ago, the average wage for a Chinese factory worker was about 25 cents an hour. Today, it's about $3 an hour – a 1,100% increase. Over the same time, American workers have seen only a minimal pay rise.

CL: So profit margins are compressing in China…

NR: Exactly. A lot of labor-intensive jobs went to China because wages there were so low. The cost per hour to make something in China used to be one-fiftieth the cost to manufacture it in the U.S. Now, it's more like one-fifth the cost.

The second factor helping bring jobs back to the U.S. is the amount of piracy that goes on in China. Chinese companies often make counterfeit versions of the products they manufacture for U.S. companies.

When you set up a Chinese factory to produce something, there's a law that says that at least 50% of the parts that go into your product need to be made in China. An American company that wants something made in China has to first teach the Chinese how to make the parts for it. That makes it extremely vulnerable to piracy.

Even Apple is running into this problem. For instance, one Chinese manufacturer has made a knock-off copy of the iPhone 7. It's pretty much the same thing as an Apple iPhone. You can't tell them apart. But it sells for about $47 instead of $650.

Any defense company, or any company that makes any kind of leading-edge technology, is not going to go over there and have their products made anymore because they know their products are going to be ripped off and stolen. You used to be able to weigh that up against the cost savings. But with Chinese workers being paid well all of a sudden, it isn't worth it anymore.

CL: What other factors did Brian talk to you about?

NR: The third factor he listed is that consumers want to get their hands on new tech gadgets as fast as possible. If you have a product that ships from China, it takes a month or longer for it to get into the hands of U.S. consumers. If you have a gadget that's made in America, on the other hand, it can beat the Chinese-made product to market.

Patriotism is also playing a role. As Brian put it to me, "It's just the patriotic thing to do to bring jobs home." People are starting to realize that and buy American more. So when companies create jobs at home instead of overseas, it's good for business.

Finally, there's automation. Robotic technology is getting better every year. So the cost advantage of having cheap workers is eroding. Combined with the ability to get goods in the hands of consumers faster, it's getting to the point where it's more profitable to produce in America.

It's no longer the Henry Ford model. You don't drop out of high school, go onto a production line, pull a lever or something, and do that repeatedly day after day. That means the jobs that come back won't necessarily be the same jobs that left. They'll be higher-skilled jobs – the people who set up the manufacturing line… the people who make the robots that make the products.

As Brian put it, "Most of these jobs coming back are going to require at least a two-year degree." They're not going to be for the high school dropout. They're going to be for someone who wants to continue their education and do a two-year university course to learn a new skill.

CL: Sounds like it's not legislation coming out of Washington that's bringing jobs home. It's stuff that's happening completely outside of Washington's control.

NR: Yes and no. Jobs were coming back *despite* all the extra regulations the Obama administration was throwing onto businesses. If you now have a pro-business White House coming up with reasonable policies, jobs should come back even quicker.

CL: Where did you take off to after Wisconsin?

NR: I stopped to talk with a *Palm Beach Daily* reader, Tim W., who owns a pizza restaurant in New Lenox, Illinois. It was your typical American pizza place. Walls plastered with posters of movies that had been filmed in Chicago – *The Blues Brothers, Risky Business,* and *Ferris Bueller's Day Off*.

We talked about the struggles American small-business owners are going through. The big issue that came up was health insurance costs, which skyrocketed over the past couple of years because of Obamacare. Tim paid $1,700 a month for a pretty lousy policy for him and his family.

When I started my tour of the Rust Belt, the main question I had was whether President Trump's rolling back of regulations would help bring back jobs. What I discovered was that small-business owners are just as concerned about rising health care costs as they are about rising regulations.

If you're shelling out $1,700 a month on your family's health care premium, you can hardly be expected to take a gamble and set up a new business. Tim reckons that alone is stopping new businesses from forming. If the cost of health care premiums comes down under Trump, that's going to be a positive for American businesses.

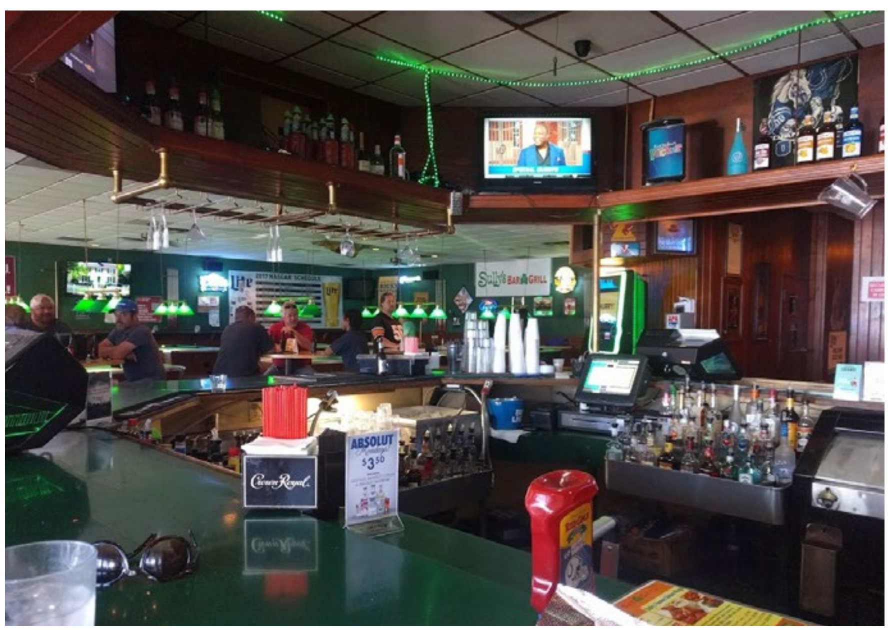
CL: Where did you head to next on your trip?

NR: From Illinois, I went to Indianapolis. I chose to go there because Indiana has seen a lot of high-profile factory layoffs recently.

Last October, the Rexnord factory, which makes industrial bearings, announced it was sending 300 jobs to Mexico. The Carrier factory down the street, which produces heating and ventilation systems, announced 600 layoffs starting this summer. And Saran Industries, which does industrial finishings and machine work, and commercial food equipment maker Welbilt have also shut down factories in Indianapolis, cutting about 100 jobs each.

These factories were all in this neighborhood near the airport. And there's this one neighborhood bar there, Sully's Bar & Grill, right between two of the biggest factories that are closing down. I wanted to go there to see what locals were saying about the factory closures.

What I learned from them was surprising because the people I talked to there were pretty upbeat about the economy. They said that if they were fired, they could find another job right away.



The view from Nick's barstool at Sully's Bar & Grill

I also talked to the bartender, a woman called Tammy Jo. I asked her how business was going. I thought for sure the bar would be struggling in an area where there are all these layoffs and companies shutting up shop. But she was like, "No, business is great. We have companies taking out food for lunch. Workers are coming here after their shifts end. The only thing that hurt our business was a smoking ban from four years ago." She was still upset about it.

I thought this was just an anomaly. So I went for a drive around the neighborhood. And I saw more "Help Wanted" signs than I could count. I lost count somewhere in the teens.

CL: What was the next stop on your tour?

NR: Next, I went to Middletown, Ohio. I wanted to check out the AK Steel plant, the country's most productive steel operation. The plant sits on 2,791 acres. And it employs about 3,000 people in a town of 48,000. If it went away, the entire town would be devastated.

CL: What did you talk to people about in Middletown?

NR: Mainly about how steel tariffs are helping the city – despite what many people think. The problem is the Chinese are making too much steel. And they're trying to dump it on U.S. markets. To keep our steel companies and businesses running, we have to put a tariff on steel products that get dumped here.

Again, this is something that predates Trump. Last year, the Obama administration put a huge tariff on Chinese steel. But Team Trump expanded it in February of this year.

CL: Aren't trade tariffs what Bill Bonner calls win-lose deals? In other words, they are not deals you voluntarily enter into. Governments impose them on businesses. In this case, steelmakers in China are losing out and Middletown is winning. It's a redistribution of pain, in other words.

NR: You have to decide which pain you can tolerate. You can have an American steel town devastated because China is dumping subsidized steel on our markets. Or you can have people who buy steel products pay more.

I'm a libertarian. I hate the idea of tariffs. They're best avoided. But if the Chinese government subsidizes its steel industry, like it's doing now, it has the capability to put other countries' steel plants out of business because Chinese steel will be so much cheaper to buy.

But that's not the free market, either. It's a Chinese government subsidy distorting the free market. Slapping a tariff on subsidized Chinese steel is not ideal. But it's a retaliatory measure.

If it was all private companies making steel... and no governments getting involved... you could make a case for just leaving everyone alone and letting the lowest-cost provider win. But when you have a foreign government subsidizing production, you have to step in with a retaliatory measure. Otherwise, that government will end up monopolizing the entire industry. And that's hardly a free-market outcome.

CL: Your next stop was Detroit. The city symbolizes the hollowing out of U.S. manufacturing and the social problems that come with that. What were your impressions?

NR: I was expecting to see only abandoned factories, broken neighborhoods, and vacant blocks. Don't get me wrong. They're still there. What surprised me was how well the economy is recovering.

The 2008 crash and the Great Recession that followed absolutely devastated Detroit. It didn't look good for the city at all. Then a guy named Dan Gilbert, who owns Quicken Loans, bought up some property downtown and relocated 1,700 of his workers there.

Since then, more companies have followed, bringing thousands of new jobs, and the downtown area is starting to pick up. In the riverfront district, you see a lot of condos, apartments, and green space under construction.

I was driving around the different neighborhoods with this guy Dale Brown. He was another interesting character. He's the founder and CEO of a private security company called Threat Management Center.

He started the company a little over 20 years ago. It's basically a private security force. When he started out, it was just him going into the ghettos to clean them up with a rifle and his dog. Now, his company protects entire neighborhoods.

Dale gave me an example of one neighborhood he watches called Palmer Woods. It was Detroit's premier

The offices of Threat Management Center in Detroit

neighborhood back in the city's heyday. But it started to struggle back in the early 2000s, and people had to leave. They couldn't even sell their homes. They just vacated them.

When Dale took over in 2010, there were 33 vacant houses in the neighborhood. When Dale and I drove through it, there were only two. Dale went in there, made the neighborhood safer, and people started to come back because the houses there are very nice.

As a result, Dale told me that property values have skyrocketed. Being an analyst, I wanted to verify this myself. I looked at Zillow, the online real estate database. And sure enough, since 2010, property values in Palmer Woods have gone up 100%.

CL: Sounds like most of the places you visited are doing much better than you expected. Did you come across any bad news stories on your trip?

NR: Yeah, Buffalo, New York. It's drowning in regulations from the liberal state government. You see, there are so many people living in New York City, it controls the state government. As a result, New York state has this stupidly high state income tax. It puts a bunch of regulations on businesses, too.

That's why businesses that start in Buffalo or New York City tend to leave when they get big. The last one to do that was Tyson Foods. It was headquartered just outside of Buffalo. But it left for Arkansas because of all the taxes and regulations. It took 500 jobs with it.

The big hope that the people I met in the Rust Belt have for the Trump administration is that it will move in the right direction in terms of removing regulatory burdens and lowering the cost of health care premiums. It hasn't happened yet. But if it does, I expect the U.S. manufacturing renaissance to pick up even more steam.

CL: Right now, that seems like a big "if." Team Trump is still fighting a lot of powerful swamp critters in Washington.

NR: That's true. But the folks I met in the Rust Belt were just ecstatic that the new regulations have come to a halt. They can now move forward knowing there's not going to be more regulations piled on every year.

CL: What advice do you have for *Inner Circle* members based on your experience in the Rust Belt?

NR: As I mentioned earlier, my trip confirmed what Bill's Doom Index has been saying – that the U.S. economy is in better shape than most people think. That makes American businesses that make and sell their products in the U.S. great investments.

One way to profit from this is to simply buy small-cap stocks. Small caps tend to be newer businesses than their large-cap counterparts. Expanding internationally is not something most small-cap companies have thought about yet.

These are what I call "America First" companies. They don't need to worry about border taxes affecting their profits.

[The exact definition varies, but a large-cap stock is one whose "market cap" – the total value of its outstanding shares – is more than $10 billion. A small-cap stock has a market cap of between $300 million and $2 billion.]

To give you an idea of what I mean, about half of all revenues of the large-cap companies that make up the S&P 500 comes from overseas. The average small-cap stock on the Russell 2000 Index – the benchmark for U.S. small caps – gets less than one-quarter of its revenues from outside the U.S.

And as I told you the last time we spoke [catch up here], if we do get more trade wars, it could help the little guys. With less competition from abroad, smaller companies should be able to sell more goods at home.

My favorite way to play the "America First" theme is the Vanguard Small-Cap Value ETF. It invests on your behalf in 800 small-cap U.S. companies. And it charges an annual fee of just 0.2% a year.

What to Do

Chris here – If you haven't already, consider adding some shares of the Vanguard Small-Cap Value ETF (VBR) to your portfolio.

If Nick's thesis is correct, as the U.S. manufacturing renaissance continues, VBR is going to deliver much higher returns than the more foreign-focused large-cap stocks most people own.

Meanwhile, take the doom and gloom stories you hear in the mainstream press with a pinch of salt.

As Nick's tour of the Rust Belt reveals, the mainstream press is deeply out of touch with what's really going in America today.

Until next week.

Regards,

Chris Lowe
Editor, *Inner Circle*

P.S. Do you live in a Rust Belt state? Do you own a business there? Do you have a personal story to share about what's really going on there? Send your insights to feedback@bonnerandpartners.com. I'd love to hear them and share them with your fellow members.

P.P.S. Each week, we're adding bonus content about one of the biggest profit trends we're tracking at *Inner Circle* – the rise of cryptocurrencies. Last week's essay focused on the reasons behind the price volatility of ether, the crypto-asset behind Ethereum. This week, a deeper dive into what Ethereum is all about. It's all in our Crypto Corner on the next page.

THE INNER CIRCLE TOP 6

Ride the cannabis legalization wave – A wave of cannabis legalization is sweeping across the globe. Buy cannabis stocks (5/12/17).

Follow the Golden Ratio – Middle-aged big spenders are the biggest population group, and U.S. stocks will benefit. Dollar-cost average into U.S. stocks (4/21/17).

Prepare for peak globalization – U.S. stocks with a lot of overseas revenues will get destroyed. Buy these "America First" stocks instead (3/10/17).

Cybersecurity splurge – Governments, banks, and companies around the world are spending big bucks on cybersecurity. Get ready for a rally (12/8/16).

Bullish on bitcoin – Cryptocurrencies are the "new gold" (7/21/16). Use them to bet against the doomed fiat money system (9/15/16).

Defense stocks for a bellicose era – The world is experiencing a rise in militarism. Go long defense stocks (11/5/15).

Crypto Corner

What Is Ethereum? | By Chris Lowe

The newest and most exciting big-picture investing idea we cover at *Inner Circle* is the rise of cryptocurrencies such as bitcoin.

It's also the most controversial and least understood idea we cover. So for the next several weeks, we're featuring special bonus essays to bring you up to speed on what the cryptocurrency space is about.

Last week, we looked at the price volatility of ether, the crypto-asset that "fuels" the Ethereum computing platform. This week, more about what that platform does and why it's so important.

Ethereum is commonly referred to in the mainstream press as bitcoin's "closest competitor." But Ethereum doesn't compete with bitcoin. Instead, it's an important evolution of the technology that powers bitcoin, the "blockchain."

A blockchain is a decentralized database that runs across many connected computers around the world.

The big breakthrough is that blockchains are tamperproof. Once a new record is added, it can't be deleted or replaced.

The Bitcoin blockchain is pretty basic. It records currency transactions like a traditional ledger. The Ethereum blockchain is more powerful. It's not limited to recording currency transactions. It can be programmed to run all sorts of complex software applications. As Ethereum inventor Vitalik Buterin describes it:

> Whereas Bitcoin is sometimes described as a "worldwide ledger," albeit restricted to recording the balances of one specific currency, Ethereum can be viewed as a "world computer": a place where anyone can upload and run programs that are guaranteed to be executed exactly as written on a highly robust and decentralized [...] network consisting of thousands of computers around the world.

In other words, Ethereum allows you to establish trust with strangers when entering into all kinds of deals.

Here are a couple of examples of what one of those tamperproof software applications might do...

Let's say Mary wants to sell her house to Mike. Using a software application on the Ethereum blockchain, the title deeds for the home are automatically transferred to Mike when Mary receives a certain amount of cryptocurrency.

Because the application running on the Ethereum blockchain is tamperproof, Mike and Mary can trust that the deal will be fair.

Ethereum applications can also interact with physical devices that are hooked up to the internet.

For instance, if Mary wants to rent Mike a bike, she can put a "smart lock" on it – a lock that is connected to the internet. Then she can write some code that unlocks the smart lock for a pre-agreed length of time when Mike sends her a pre-agreed amount of cryptocurrency.

Once you understand that Bitcoin is about recording transactions in tamperproof currency balances... and that Ethereum is about running these tamperproof software applications... you see how meaningless it is to frame Ethereum as Bitcoin's competitor.

Bitcoin and Ethereum both run on blockchain technology. But saying they compete with one another is like saying eBay competes with Google because they're both run on internet technology.

Ethereum is better understood as an evolution of Bitcoin. It's not just about transferring currency. It takes the technological breakthrough of the blockchain and builds on it to allow for many more different real-world applications.

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Our goal is to help you connect the dots in a broader way between what's happening in the world and how you should be strategically positioned in your portfolio.

In your weekly *Inner Circle* dispatches, you'll find the best ideas our "brain trust" has to offer.

From time to time, you'll also find "deep dive" Q&As with world-renowned experts outside of our immediate network.

You can find the full archive of *Inner Circle* dispatches on the password-protected website here. And you'll receive the latest weekly dispatch direct to your inbox at midday ET every Friday.

You can find the library of special reports here. This is packed with actionable ideas and how-to guides – everything from how to prepare for a bank run to why you should buy gold now to how to make sure your children have a good grasp of investing.

If you have any questions about your membership… or comments on the ideas you read about in your weekly dispatches… you can contact the *Inner Circle* team anytime at feedback@bonnerandpartners.com.

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