

The Kiplinger Letter

FORECASTS FOR EXECUTIVES AND INVESTORS

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Dear Client:

Washington, Sept. 6, 2019

U.S. farming is increasingly high-tech, relying as much on satellites as seeds and tractors. Further innovations hold greater promise: Drones, robotics, artificial intelligence and the like. But how fast will farmers take to them?

AG What constitutes “precision farming,” the catchall term for the technology, some of it decades old, that’s reshaping agriculture? The growing use of satellites and sensors, for one, to help steer tractors, monitor crop yields, map various data and precisely apply fertilizer, water and other inputs. Slow but steady growth of such tech has already boosted farm efficiency and profitability.

Expect agriculture to become even smarter. Drones with longer battery lives will allow farmers to survey their fields without ever setting foot in them. Autonomous tractors will seed fields in the spring. Robots will pick fruits and vegetables in the fall. Artificial intelligence will help sort through reams of data...on yield, soil, the weather, you name it... and offer specific recommendations to farmers.

The potential benefits are huge. By 2050, precision agriculture technologies could reduce farm operation costs by \$25 per acre, while also mitigating the damaging environmental effects of farming, such as runoff from overfertilization. Yields, meanwhile, could rise as much as 70% in that time.

But many challenges lie ahead. One is persuading farmers of the benefits. Farmers are pragmatic, but also cost-conscious. And investing in new technology, some of which may take several years to reach its full potential, is often expensive. Size is also a factor. Larger farms...with at least 2,900 acres...are already more likely and financially able to adopt precision farming tech than their smaller competitors.

Another: Providing the necessary infrastructure. Over 20 million Americans still lack access to broadband internet, including many farmers in rural areas. Efforts to close the digital divide have seen some progress, but more remains to be done.

In the end, precision farming will also be big business, mushrooming into a \$43-billion industry by the mid-2020s. The agricultural drone market alone is expected to reach \$1 billion in size by then, up from \$338 million in 2016.

Smaller upstarts will challenge agribusiness giants, on data especially, where farmers may be more inclined to trust local retailers than the likes of Monsanto and John Deere. Both firms have invested in or outright bought promising start-ups: For example, John Deere’s purchase of Calif.-based Blue River Technology in 2017.

Globally, such advancements will be key to feeding a growing population, projected to reach over 9 billion people by 2050, up from roughly 7.5 billion today.

Economic Forecasts

GDP growth

2.3% in '19 and 1.8% in '20, down from 2.9% in '18

Interest rates

10-year T-notes staying below 2% until trade war ends

Inflation

2.3% at end of '19 as new tariffs affect consumer goods, up from 1.8% now

Unemployment

Ending '19 at 3.8%, from 3.7% currently

Crude oil

Trading from \$50 to \$55 per barrel in October

Federal deficit

Rising to 4.5% of GDP in '19, '20, '21, from 3.8% in '18

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JOBS

The Aug. jobs report wasn't spectacular, with only 130,000 jobs created. But don't overlook the positives it showed. Wages were up at a solid pace... 3.5% year-over-year for nonsupervisory workers, which helps fuel consumer spending. Hours worked rose. The share of the population employed is the highest since 2008. Most of the trouble spots are unsurprising: Manufacturing and retail jobs. Overall, the report shows an economy that is slowing but still fairly healthy.

U.S. ECONOMY

When it comes to consumers' mood, just how confident are they these days? It depends on how you ask them. One widely watched confidence measure took a big hit in Aug. The other major gauge shows confidence near an all-time high. So what's going on? Are consumers optimistic...and eager to spend...or aren't they? News about tariffs and stock market volatility spooks shoppers. That effect showed up in the University of Michigan's Aug. survey, which focuses on such factors. But ultimately, most folks tend to base their spending decisions on jobs, and whether the labor market is healthy. That's what the Conference Board focuses on when it conducts its surveys. Given the decent Aug. jobs report, odds are most people will be upbeat about the economy, even as stocks gyrate and the trade war deepens.

GLOBAL ECONOMY

International trade is still growing. But that growth is becoming anemic after years of robust expansion. This year, expect global trade volumes to increase by just 2.6%. That follows gains of 3% last year and 4.6% in 2017. Back at the turn of the century, total global shipments were rising by 8% per year. Mounting tariffs aren't helping the situation. Companies operating in China are scrambling to shift supply lines, which can be a slow and expensive process. It's not merely a case of tariffs hurting trade, though. The present slowdown started long before the U.S.-China feud. One reason: The proliferation of automation has made it more economical to produce goods in the country where they're sold, instead of relying on cheap labor abroad. That's a trend that won't end anytime soon.

Germany is on the brink of recession as its export-reliant economy reels. German GDP contracted in the second quarter and may well do so again this quarter. Other European countries depend heavily on the Continent's top economy, since so many German carmakers and other firms have supply chains that stretch into central and eastern Europe. If Germany catches a cold, its neighbors can, too. Surprisingly, France is holding up well and may offset Germany's weakness. Tax breaks and other stimulus measures Paris enacted to quell recent social unrest are putting more money into consumers' hands. Berlin may end up doing likewise in order to ward off a deeper downturn...a difficult choice for its deficit-wary leaders, but feasible since the country runs a healthy budget surplus and can afford to spend.

HOUSING

Falling interest rates are propelling a wave of mortgage refinancing. With the average rate on a 30-year home loan at its lowest in three years, homeowners are taking advantage: Refinancings are up 224% since the start of the year and 40% in just the past four weeks. About 35% of homeowners could save a bundle by refinancing now...10 million could cut their rate by at least 0.75 percentage points. Rising refi activity in 2019 will mark a sharp turnaround from the drops of recent years.

Fannie Mae and Freddie Mac can now consider new types of credit scores when purchasing home loans from institutional lenders. Until now, the two agencies have required lenders to use Fair Isaac Corp.'s FICO score to evaluate borrowers. New regulations will enable lenders to use alternatives, such as credit scoring systems developed by VantageScore, which take account of more of a borrower's credit history. The policy is a win for nonbank lenders such as Quicken Loans. Nonbanks now dominate the mortgage market. They say that using a wider array of credit scores will open the mortgage market to more of the 45 million people who lack a FICO score.



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SHUTDOWN

Congress must act fast to avoid a government shutdown as it returns from its annual late-summer break. Uncle Sam's fiscal year ends on Sept. 30, and a bill is needed to fund federal agencies for the coming year. Partisan bickering will make any compromise on a funding bill difficult. The most likely scenario: A short-term measure that buys more time. Such a continuing resolution, or a series of them, would drag out the debate well into fall. Without a funding bill or a CR, the federal government will close on Oct. 1. Last winter, the record 35-day partial shutdown was a political loser for both parties, but it was especially damaging for President Trump and the GOP.

Trump hasn't said much about negotiations yet. That won't last long. His proposals, such as funding for a border wall, have scuttled past deals. His unpredictability complicates matters for lawmakers eager to avoid a shutdown.

CONGRESS

Lawmakers will also take up gun violence legislation upon their return to Washington. Significant gun control measures, such as a full ban on assault weapons, are off the table. But after several recent mass shootings, Congress will focus on strengthening background checks for firearm purchases and so-called red flag laws that take guns away from people deemed dangerous.

Trump has backed off tightening background checks after his initial show of interest. He's now mostly focused on keeping guns from mentally ill people.

A red flag bill isn't certain, but it has the best chance of becoming law of any of the options discussed. Background checks are a long shot, at best.

Senate Majority Leader Mitch McConnell (R-KY) is the legislative gatekeeper, and he'll thwart attempts to pass major gun control measures, as he has in the past.

Congress's recess hasn't reduced the energy of pro-impeachment Democrats. More than half of House Democrats back impeachment or an impeachment inquiry. House Judiciary Com. Chairman Jerrold Nadler (D-NY) will continue his fight with the president, including a new round of subpoenas for former administration and campaign officials in order to compel testimony on a range of Trump activities.

But impeachment will go nowhere unless new damning allegations arise involving Trump. House Speaker Nancy Pelosi (D-CA) has so far resisted the calls to move forward on impeachment. Pelosi is laser-focused on the 2020 elections.

POLITICS

Ga. will be in the unusual position of electing two senators in 2020 because of GOP Sen. Johnny Isakson's retirement at the end of this year, due to health concerns. Gov. Brian Kemp (R) will appoint a Republican as a replacement for Isakson. The state will then hold an election in Nov. 2020 to fill the remainder of Isakson's term, which ends in Jan. 2023. It's not clear whom Kemp will choose. The other Ga. senator, Republican David Perdue, will be defending his seat next year.

Look for Republicans to keep both seats and continue their Ga. dominance.

But Democrats will make it competitive, despite lacking high-profile options. Ga.'s most prominent Democrat, Stacey Abrams, says she won't run for either seat.

HEALTH CARE

Insurance premiums in Obamacare exchanges will stay flat for 2020 plans for the most part, about the same as this year. At most, expect modest hikes, well below the eye-popping 25% increases in each of the past two years. Big drops may be seen in some states, mostly due to reinsurance programs, whereby states pay for a portion of high-cost claims. Colo. and Del. are seeing about 20% decreases.

Insurers are expected to expand their participation. Twelve states will add at least one insurer to their exchanges. No insurers have said they are pulling out of any market. In 2018, insurers saw record profits. 2019 should be almost as good.



FACTORIES

Businesses are pulling out of China. But they aren't flocking to America to set up new production facilities. Washington's tariffs on Chinese goods make manufacturing in China less attractive and up the incentive to reshore jobs that had been taken out of the U.S. Some firms have done just that: 145,000 jobs came back to American shores last year, according to one estimate. But the pace of reshoring is slowing now as companies eye lower-cost countries such as Vietnam.

A few factors make manufacturing in the U.S. a tough sell. Among them: The strong dollar, which makes American exports less affordable abroad. The lack of skilled workers... a chronic problem cited by U.S. manufacturers. And the sheer size of the Chinese market. Large manufacturers in particular want to operate in China not just for the cheap, abundant labor, but also for proximity to an increasingly vital market...more than a billion people aspiring to a better life.

BREXIT

The three-year-long drama known as Brexit may be coming to a head, finally. U.K. Prime Minister Boris Johnson is doing everything in his power to force the country to exit the European Union by Oct. 31, with or without a deal that would regulate trade and other relations between London and Brussels. But the effort has cost him the support of some Conservative lawmakers he needs to maintain his majority. He'd like to call new elections to solidify his grip on power, but probably won't be able to make that happen before the Oct. 31 Brexit deadline.

Still, don't be surprised if the Brits find a way to delay a decision yet again. Opposition to a no-deal Brexit is fierce in some parts of the country. No British PM has been able to take the plunge yet or ink a deal that a majority in Parliament accept. The EU would likely entertain a further delay...anything to keep the bloc intact.

FINANCE

Passive funds continue to attract more of investors' money. Index funds raked in \$458 billion last year, while active funds lost \$301 billion. The exodus has slowed some this year, but it continues: Actively run mutual funds lost \$42 billion of client money in the second quarter of 2019. Their main appeal... the chance to beat the market...is struggling to compete with passive funds' low costs.

By 2025, money held in passively run funds will equal that in active funds. Recently, index funds and exchange-traded funds had a 36% share of the market. One possible worry: Higher volatility in market swoons. With so much cash automatically following a benchmark, sell-offs could become sharper and deeper.

Cryptocurrency investors, beware: The IRS is going after crypto tax cheats. The Service has sent out letters to taxpayers who may not have paid taxes on gains they made investing in cryptocurrencies such as bitcoin, or who didn't properly report those gains. So far, 10,000 such letters have gone out, some requiring a response within a certain amount of time. IRS is also concerned that electronically filed returns in recent years have almost never disclosed transactions made in cryptocurrencies.

Crypto fans are upset with the agency, arguing that its previous guidance was unclear because it treated bitcoin and its ilk as property that gets bartered among users, not as real currencies. Lawmakers have also pushed for the agency to clarify the tax treatment of cryptocurrencies in response to their growing popularity.

Yours very truly,
Knight/Kiplinger
THE KIPLINGER WASHINGTON EDITORS

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We Rank the Online Brokers

In Kiplinger's 2019 ranking of online brokers, the overall winner is E*Trade, with Interactive Brokers and Fidelity close behind. But the best brokerage for you may depend on how you invest, how often you trade and the services outside of buying and selling you need. Most of the firms on our list excel in at least one area. For example, Firsttrade does not charge commissions to trade stocks, ETFs, mutual funds and options. Interactive Brokers offers the most robust mobile app. TD Ameritrade provides the most impressive array of tools. Charles Schwab wins for most-budget-friendly advisory service. Fidelity is our top pick for breadth and quality of investment choices. For our full rankings, see kiplinger.com/links/brokers2019. **KPFM**

Dividends Take a Breather, But Don't Fret

Fat dividend increases appear to be temporary hostages to the current political, economic and market instability. That doesn't mean we're turning negative about dividend funds or high-yielding stocks, or that we're gloomy about the future size of cash payouts. Utilities and real estate investment trusts (REITs) continue to resist whatever news sets off sudden stock market sell-offs, so don't abandon either sector. By and large, exchange-traded funds that concentrate on either low-volatility or high-dividend stocks have not been hit as hard in mini-crashes as the broad market indexes. We recommend Invesco High Yield Equity Dividend Achievers (symbol PEY, 4.5% yield as of September 3), JPMorgan U.S. Minimum Volatility (JMIN, 2.3%) and Legg Mason Low Volatility High Dividend (LVHD, 3.5%). **KII**

Manage Your Portfolio in Retirement

Your portfolio will need the kind of long-term growth that stocks can provide in order to keep up with inflation in retirement. The experimental Consumer Price Index for the elderly (CPI-E), a government index that gauges the rise in prices for households age 62 and older, averaged 1.86% annually over the past decade, slightly higher than the general inflation rate. The right investment mix for you depends on how much risk your nerves can handle, along with your other assets and sources of income. But consider a diversified portfolio with 40% to 60% in stocks. There is an elevated risk of a bear market on the horizon, which can be devastating if it strikes early in retirement. To minimize that risk, reduce your exposure to stocks as you head into retirement. When the market falls, you can use that opportunity to buy stocks at lower prices and boost your holdings to your previous threshold. **KPFM**

Equifax Settlement

If you're counting on a payoff from the Equifax settlement, you'll probably be disappointed. Although a total of about \$400 million has been set aside for customer restitution, the actual amounts available for different settlement options—such as free credit monitoring services and credit monitoring reimbursement—vary by option.

If you have spent time or money since September 2017 dealing with the breach, you can request reimbursement for up to 20 hours spent on reclaiming your identity at a rate of up to \$25 per hour. For other expenses, such as accounting fees, customers can ask for up to \$20,000 in restitution. But consumers will generally be expected to document their damages and time spent dealing with the problem.

Those who have already signed up for credit monitoring can claim reimbursement from another pool of money, but the actual payment will likely be a fraction of the advertised \$125 per person. We recommend applying for 10 years of free credit monitoring instead. To apply for reimbursement, go to www.equifaxbreachsettlement.com. **KPFM**

How to Navigate Investing Overseas

Foreign stocks are an essential part of a well-diversified portfolio, but they have taken investors on a harrowing ride in recent years. A growing number of funds that focus on low-volatility stocks offer wary shareholders a low-risk way to approach these uncertain markets and potentially outperform their high-volatility counterparts over the long haul. We recommend the following five exchange-traded funds and mutual funds, which all deliver a less bumpy ride than broad international markets: Invesco S&P International Developed Low Volatility ETF (IDLV); iShares Edge MSCI Min Vol EAFE ETF (EFAV); iShares Edge MSCI Min Vol Emerging Markets ETF (EEMV); Vanguard Global Minimum Volatility Fund (VMVFX); and iShares Edge MSCI Min Vol Global ETF (ACWV). **KPFM**

Is Your Vacation Destination Safe?

News reports about terrorist attacks, rampant crime or an unsettling string of deaths in an idyllic destination may give you pause when selecting your next vacation spot. But for most travelers, the actual risks—including petty theft, traffic accidents and gastrointestinal problems—are more mundane. Go to <https://travel.state.gov> and click on “Travel Advisories” at the top of the home page to review the U.S. Department of State’s advice for travelers. Be aware that the advisories err on the side of caution. You can also sign up for safety alerts at <https://step.state.gov>. For an extra layer of security, organize your trip through a travel agent or tour operator. **KPFM**

It Will Be Harder to Take Medical Write-Offs

Starting with 2019 returns filed next year, the adjusted-gross-income (AGI) threshold for deducting medical expenses as itemized deductions on Schedule A of federal income tax returns rises from 7.5% to 10%. The 2017 tax reform law gave taxpayers a two-year reprieve from this tax hike. But that reprieve ended last year. There’s still a possibility Congress may act to extend the 7.5% AGI threshold for another year or so, but we won’t know for certain until closer to year-end. **KTL**

Help Grandchildren Pay for College

As college students head back to school this fall, many grandparents may want to help their grandkids pay for education costs. With the annual gift-tax exclusion, each grandparent can give up to \$15,000 to each grandchild in 2019 without reporting it on a federal gift tax return. But if you pay for tuition directly or give money to your grandkids, that money may reduce eligibility for financial aid, so wait until after a four-year student’s sophomore year; at that point, the money won’t affect financial aid because the Free Application for Federal Student Aid (FAFSA) form only assesses income from two years prior. If you contribute to a 529 college-savings plan that you own, it could help reduce your state income tax but may impact your grandchild’s financial aid eligibility if the money is used for their college costs. But you may be able to roll over the account assets to a parent- or student-owned 529. Wait until after the FAFSA is filed to do the rollover, so it is not reported as an asset. **KRR**

Kiplinger Podcast

Have you listened to Kiplinger’s weekly podcast yet? Each new episode of Your Money’s Worth has down-to-earth insights on saving for retirement, cutting your tax bill, investing for growth and income, maintaining good credit, and more. Every episode begins with some news you can use, such as how to get a deal on a new car or where your teen can stash his or her summer job money. The main segment features an in-depth interview with an expert; a recent episode covered what is causing the recent bout of market volatility and what you can do about it. The final segment is a quirky mix of deals, wild PR pitches and financial fact and fiction. Learn more and subscribe at kiplinger.com/links/podcast. **KIPLINGER.COM**

Taxpayer Roadmap

If you want a sense of how complicated our current federal tax system has become, look no further than the taxpayer roadmap, a graphic representation for navigating the tax system. It was designed by Nina Olson, the recently retired head of the IRS Taxpayer Advocate Service. It looks like a subway map with multiple transit lines to represent steps such as tax preparation and filing, IRS return processing and screening, audits, appeals, collection, and litigation. Go to kiplinger.com/letterlinks/roadmap to view the blueprint. **KTL**