Sound Money Need Not Be Heard. So Why So Noisy?

Paul Lobosco, 4-19-21

On the surface, markets appear healthy, certainly in nominal terms. Earnings are strong, profits margins are enjoying the deflationary impact of technology, and major indexes are performing well. These are some positive forces in the market. The purpose of this piece is to seek the truth of what lurks BELOW the surface.

Investing today is nothing like it was 20 or 30 years ago. Seriously. The criteria for making sound investment decisions are very different. Price Discovery- the basis of bottoms-up investment analysis- has been overtaken by Momentum and Passive investing, each of which thrive in an *unsound* monetary system. Investors have to take, usually without knowing or even caring, *substantially* more risk today for the same expected return, especially if such a return were in a sound money system.

What is the Federal Reserve Up To?

The stock market's success appears *almost entirely dependent upon the Federal Reserve and other Central Banks*. This means greater State control of our economy, and less Capitalism. Does this imply the market will go down, or worse, collapse? A collapse is always a possibility we must consider and try to prepare for. It does seem, however, that a collapse would be more likely in a *free* market. We have not been in a free market, and there is clear proof. The Fed's balance sheet is now up to $7.9 trillion. This means that, through its stated mandate of maintaining stability, the Fed has had to acquire $7.9 **Trillion** of assets that the market simply could not absorb. Click HERE for more. It's pretty scary, and the Fed is unlikely to stop.

In Capitalism, NO failure is the BIGGEST failure. It's as if the Fed is saying "We will not allow the market to go down". That is not Capitalism. We exist and invest in an alternate universe today, a system that looks much more like Socialism for the rich, and confiscation for everyone else. Taxation without representation, a/k/a "The Road to Serfdom", with a commensurate rise in civil unrest. Jeff Booth does an outstanding job of explaining these dynamics in a video that can be found HERE. It is a great listen, especially for those interested in the concept of money.

There have been attempts by the Fed to reduce their balance sheet in the past decade. They were not successful. When market participants sensed a growing supply of those assets, they ran for cover. In September of 2019, the Fed was forced to reverse its tapering course and increase their balance sheet again just to ward off panic. Then came Covid, and its Balance Sheet was off to the races. We are moving trillions of dollars around like it's Monopoly money. Why does this matter to you and me? Because the Fed's Balance sheet is *our taxpayer liability*.

Post-Pandemic: It's Been Fed "All-In"

The Covid pandemic exacerbated this balance sheet problem for sure. But it did not *cause* it. The pandemic gave the Fed and politicians the cover they needed. They could, in concert with the U.S. Treasury, print many trillions and claim it was necessary to get through the pandemic and its after-effects. I'm sure another story is forthcoming that will justify the Fed's continued actions. They've already assumed a larger role in combating climate change- something that strains their scope of authority, but which gives them cover, yet again, to justify asset purchases and print trillions more. Let's not forget that no one at the Fed was ever elected. Whatever intentions the Fed may have, the net effects of their actions include the following:

- Current 'stability' they seek will lead to greater future IN-stability. That is the mathematical tradeoff. We could easily see *negative* interest rates before long;
- The Fed's backstop role has created large-scale complacency in the market, with many investors (especially young ones) having no clue what a true bear market looks like;
- Malinvestment is on the rise. With the Fed as a backstop, we are seeing all kinds of market distortions. Gamestop is a prime example. Special Purpose Acquisition Vehicles, or SPACs, are also a product of easy money malinvestment. The reason these SPACs are public is because private money like venture capital wants nothing to do with them, Nor do underwriters. So the SPACs bypass the entire process and rely on a Greater Fool- the public;
- Savers are being punished, while borrowers are being rewarded. This is the exact opposite of a healthy system, and a function of Fed monetary policy;

- The 60/40 stock/bond portfolio is no longer relevant, as bonds appear to offer little return, and in some areas, a negative return (and just wait for *Fedcoin*!);
- While Central Banks can theoretically keep the stock market propped up with money printing, they will ultimately have to sacrifice their currency to do so.
- Most importantly, Fed policy may result in significant Inflation, or even Stagflation (high inflation with high unemployment and a weak economy). Some will point to the Consumer Price Index and say that inflation is muted. Don't believe them. Inflation can be measured in terms of lost purchasing power. For example, first time home buyers cannot afford to buy a home as easily as 20 years ago, despite mortgage rates being near all-time lows. The government doesn't see that as inflation, but it is. The CPI, as I have stated many times, is misleading at best. There are countless examples.

Sophie's Financial Choice?

Ron Paul was one of the first and only politicians to advocate consistently for sound money. His message goes back over a generation. He saw the writing on the wall as soon as we went off the gold standard in 1971. Paul warned of the snowball effect of increasing deficits. Well, those deficits have snowballed to over $28 trillion of U.S Federal Debt (the sum total of annual deficits). At 130% of annual GDP, that is grotesque and unsustainable. There is a wise contingent of Ron Paul disciples, strategists who see today's writing on the wall. I will list many of them at the end of this piece. While they do see the truth and identify the problem, no one seems to have a viable solution. Indeed, there are no easy answers, just strategies to develop.

So why can't the Fed just print trillions of dollars, wipe away ALL our debt and live happily ever after? Because that is not how money works. If there is $1 in existence and you print another dollar, then the cost of the good $1 bought yesterday will rise to $2.00. It seems to me that the Fed's plan is to get other countries to pay as much of that extra dollar as possible. This is the concept of "Inflating away the debt".

The most important saying I've heard recently is "***We will either default on our debt or default on our currency***". Clearly, money printing actions taken by the Fed have been supportive of the debt, since the prospect of default on U.S. Treasuries is unthinkable. So we are left with a default on our currency, an outcome *which I view as increasingly likely in the intermediate term.* This applies not only to the U.S. Dollar, but to FIAT currency all over the world. In fact, the Dollar may get stronger for a period of time, as other currencies fail first. The debt problem is global, and the solution- if you can call it that- throughout much of the world has been for each country to devalue its currency. This is also known as a ‘Race to the Bottom’.

Real Money is Hard to Debase

The conclusion here is that your dollar is losing purchasing power at an increasing, perhaps alarming, pace. ***The owners of fiat currency (Dollar, Euro, Yen, Pound, etc…) are all STARVING for sound money that cannot be debased.***
Gold, for thousands of years, has been that source of sound money. I believe it will be again. We went off the gold standard ‘temporarily’ in 1971, nearly 50 years ago. We have been riding the wave of global reserve currency status to historic wealth confiscation and indebtedness. Well, that tide is turning. What was a blessing is becoming a curse. Being the world’s reserve currency may hurt the U.S. most of all.

There are theories suggesting that Gold and Silver prices are being kept artificially low though market manipulation. I offer no clear proof of that, but it sure does make sense to me. Click HERE to listen to one such theory from Chris Powell. The average person cannot buy an ounce of gold for close to the price it is being quoted in the market. Premiums up to 20% are common. So it appears spot prices of both Gold and Silver should be materially higher. We have, unsurprisingly, already begun to see a surge in commodity prices. This would suggest a ‘sticker shock’ inflation number in the near future accompanied by Negative Real Rates. That is bullish for precious metals. What would cause the Gold thesis to be wrong long-term is if the U.S. successfully grows its way out of its debt trap and the Fed’s Balance Sheet can be tapered off into the market successfully. I view that outcome as highly unlikely, even impossible in mathematical terms. Thus the bullish case for gold and silver.

Lost purchasing power, combined with artificial suppression of the Gold Price, goes a long way to explaining the insane rise in the price of Bitcoin, which is often likened to digital gold, and which cannot be manipulated in the same way as Gold due to its decentralized nature. Bitcoin is a topic for another day. Suffice it to say Bitcoin is also risky, but it’s not going away. It will likely be part of the solution.

Gold and Bitcoin both offer the chance of leveling the monetary playing field, where a unit of exchange today is basically the same unit of exchange tomorrow. Each has its merits and its shortcomings. Gold and Bitcoin will likely battle it out for a while, with each staking a claim to its role in the future of money. Each can serve as anchors in a future monetary system where the U.S. Dollar's role will be severely diminished. This, combined with our country's persistently high trade deficit, will likely lead to significantly reduced purchasing power.

What does Currency Debasement Look Like?

I have often posed the following question: What is the point of a stock like Starbucks doubling in value over 5 years if the cost of Starbucks coffee does from $3.00 to $20.00? Not to single out Starbucks, but this is the direction our global economy is headed. Notably, it is U.S. household wealth that is most under attack.

A second question is: Where would the stock market be without the Fed supporting it? Well, no one knows the exact answer, but we all can sense it would be lower. My best guess is about 40-50% lower. This gives me a rough gauge as to how things might begin to trend if the Fed does stop expanding its balance sheet and reduces it instead. Or, if they begin monetary tightening. Again, highly unlikely, but possible.

Most everything you hear from Jerome Powell and the Fed is rooted in their understanding that the monetary system needs a reset. This is behind their introduction of a digital currency, a/k/a *Fedcoin*. Such a currency would have a *relationship* to the Dollar, but would not be *equal to* the dollar. That is a critical distinction. The U.S. Dollar will have a role in whatever new currency exists, but its power will be diminished. Some are even talking about a GLOBAL digital currency (GDC). This might be the product of the International Monetary Fund, or IMF. While a global currency would surely have merits, it may hurt developed economies like ours and lead to greater global instability if implemented. The long-term winners might be, somewhat ironically, the emerging market economies. Why? Because, as the term implies, they are "E-Merging". The Western World, saddled with incomprehensible debt, is comprised of "SUB-Merging" economies.

Jerome Powell, Fed Chairman, has recently changed his public tune considerably. It wasn't long ago that he said "we're not even thinking about thinking about raising interest rates". He stated that on several occasions. Now, he says that a raise in rates from the Fed is "highly unlikely" in 2021, with a hint that rates may rise in 2022. He's trying to prepare the market for what is inevitable. I suspect that, even if they raise rates, the Fed will still have to increase its balance sheet. Why? Essentially, the

Treasuries owned by foreigners will be sold or redeemed (already happening). Thus, the Federal Reserve is the buyer of last resort, of ONLY resort. Each Dollar the Fed's Balance sheet increases becomes the burden of the U.S Taxpayer. This is called 'The Japanification of America', of the entire Western world.

The Good, The Bad, The Reality

We are in a period of ultra-easy earnings and revenue comparisons. Q2 2021 earnings will surely shine vs. Q2 2020. The same will hold true for Q3 and probably Q4. It is quite possible that, while supportive of stocks, such anticipated earnings increases are largely priced into stocks. What will 2022 comps look like? What happens if rates rise, or if Inflation accelerates? These are some questions the market will be grappling with the rest of 2021 at a macro level.

The Great Financial Crisis of 2008 is very much still with us. The problem is not only unsolved, it has worsened via the kick-the-can approach. With it, so too have the wealth gap and the level of civil unrest worsened. How nice it would be if the debt could just disappear, but math is not magic. It is getting harder to see anything but an explosive resolution, both financially and sociologically. Only the Central Banks' all-in approach has kept the House of Cards from collapsing so far. Virtually every person named below agrees that there is a reckoning forthcoming. Many of them, like me, believe the reckoning will be through Inflation and currency reset. Several others think it will be through a deflationary collapse, which would involve a serious market decline. Please call my office for more info: 732-450-1212. - PL

List of Sources for this Newsletter: Mike Green (Logica), Jeff Snider (Alhambra), Brent Johnson (Santiago), Steven VanMetre, Danielle DiMartino Booth (Quill), Russell Napier, Grant Williams (RealVision), Stephanie Pomboy, Raoul Pal, Adam Taggart (Peak Prosperity), Keith McCullough (Hedgeye), Nomi Prins, Lynette Zang (ITM Trading), Willem Middlekoop, Lacey Hunt, Luke Gromen (FFTT), Ray Dalio (Bridgewater), Jim Rogers, Cathie Wood (Ark), Peter Schiff (Europacific), Lyn Alden, Alasdair Macleod (Goldmoney) and Jeff Booth (The Price of Tomorrow). I am grateful to the persons above, each of whom shares his or her expertise freely. I strongly encourage everyone to explore their discussions on YouTube.

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