Zanetti Monday Missive 2023.05.29
Inflate or Die

"Inflate or die."
~ Richard Russell, Dow Theory Legend

Hello Everyone,

As I write this on Sunday morning, the business headlines read, “Debt Ceiling Deal Between White House and GOP Reached In Principle.”

Whew! That was a close one. (Sarcasm)

The reality is this: our monetary system is structured to accumulate ever higher levels of debt. Our debts cannot shrink. Ever. When politicians talk about “reducing spending” or “paying down the debt,” they are talking gibberish. It is impossible. If debt were to contract, the entire system would collapse.

Here’s why.

Although you often hear the lament, “We just print money out of thin air;” technically, that is wrong. We do not “print” money into existence. We “borrow” money into existence.

In the old days—prior to the creation of the Federal Reserve in 1913---the US Treasury Department issued our currency. And, in accordance with the Constitution, that money was backed by gold and silver. Those days are long gone.

Today, a private corporation (with shareholders and a board of directors) issues our currency. That corporation is called the Federal Reserve. Think of the Fed as a contractor to the US Government.

The Fed creates dollars as currency and then loans those dollars with interest (!) to Uncle Sam. So, money isn't printed into existence, it is borrowed by us (or loaned by them) into existence.   And this is why our debts can never be reduced---much less paid off.

Imagine this. Imagine the first dollar ever being created by the Fed. That dollar had to be repaid by US taxpayers.   And here is the important part. With interest.

"But Greg," you ask, "Where do the dollars for those interest payments come from?"

"Great question," I say. "The Fed must create more dollars, so we have the money to pay the Fed back with interest."

Then you might reply, "But wait! That's crazy! They'll just keep creating more and more dollars and getting more and more interest. They have no incentive to ever stop creating more dollars. This is a Ponzi Scheme! A fraud! A corrupt system! How could the government allow this!?"

And I would say, "You're right. It is a Ponzi scheme...a scam…a fraud. But remember, the more dollars the Fed creates, the more dollars the Government gets to spend. And like all Ponzi schemes, once 'the flow' of dollars reverses, the Ponzi collapses. Until then, the guys at the top benefit."

And, you might say, "So all this talk of debt ceilings is flim-flam.   There is no ceiling. Flow can't reverse. Because no one wants to be held responsible for a collapse. So, we will inflate….or die."

And I say, "You sound like Richard Russell. Oh, and besides the interest on the debt, the Fed also gets paid a 6% annual dividend. Guaranteed."

And you say, "Auuuuggghhhh!"

So, my intrepid missive readers, let's move on.

Trillions more will likely be flowing soon. What does this mean to you and your investments?   Maybe it's not what you think.

Once the final debt-deal is struck, the Treasury department is going to need cash fast. A trillion dollars (really) will be needed to plus-up Uncle Sam's checking account, so our 'gub-mint" can pay its bills. Where will that cash come from?

The Treasury Department will sell Treasury bills, notes, and bonds (Government IOUs) to anyone who will buy them. Where will these people/institutions get the cash to buy the governments IOUs? Probably from the same place you get cash. The bank.

For example, picture, say, $50 billion in cash earning 2%-3% at a bank. Now, Treasury Secretary Janet Yellin, says, “Hey Wall Street. Hey world. I have a trillion dollars of Treasuries for sale paying 5%! Come and get ‘em!”
Previously printed (errr... loaned) cash now leaves banks to buy more US Government debts.

“But, Greg,” you say, “Aren’t the banks already dealing with depositor flight? I mean we all saw what happened to Silicon Valley and First Republic.”

And, I’d say, “Yes. Debt expert, Ari Bergman over at Penso Advisors, and the risk management teams at Bank of America, are already expressing concerns that the debt ceiling deal may have banking aftershocks we didn’t anticipate.”

“Oh, and I forgot to mention that on June 15th quarterly corporate and individual estimated tax payments are due. Where do corporations and “regular Joes” get money to make tax payments? Yup. The banks. Thus, more cash leaving the banks to pay Uncle Sugar.”

And you’d say, “But if more banks fail, won’t they create even more money to bail them out?”

Me, “Correct.”

You, “Auuuuggggghhhhh!”

So, to wrap this up. In the weeks/months ahead, here is what I expect.

We are going to see a series of seemingly unconnected crises develop.

Too much impaired debt + too many financial bubbles bursting + too many inept policy decisions + a war gone awry, will all conspire to keep the “shock” headlines coming. This will be tough on stock and credit markets. These crises are already baked in.   We just haven’t seen people, or institutions, acknowledge them yet.

Therefore, despite last month’s correction, the trend is still with us. Be right. Sit tight.

Signed, Your For-You-Men-Who-Think-You-Are-Pregnant—Congratulations!-It’s-A-Beer! Financial Advisor,
Greg

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