Hello Everyone,

Traditionally, January 6th is called the Epiphany…or in Europe and South America, Three Kings Day. It celebrates the day when the wise men came to adore the Savior. All was calm and all was bright.

January 6, 2021 was neither calm nor bright.

I'm not so sure things in the world of finance are calm and bright either. Today's missive continues down the path of what is driving both the economy and the markets. Is it organic growth or something else?

I hope you find it edifying.

Signed, Your Hoping-More-Wise-Men-And-Women-Appear-On-The Scene-Soon Financial Advisor,

Greg

KKOB 2021.01.08. Is Our Economic Growth Organic…or Debt Driven?

Bob: So, Greg, on Monday we looked at company profits. And, because of Covid, we saw that profits are back to where they were 15 years ago.

That makes sense to me knowing how we shut down the economy.

But the disconnect for me was this. The stock market went the other way. As profits went down, stocks went up. So, now we have the situation where profits are at 2005 levels, but stocks are 300% higher than where they were 15 years ago.

Greg: I know. So, our conclusion was something else was driving stock prices besides profits. And while it could be a coincidence, the market's rise has mirrored the money printing by the Federal Reserve.

But today, let's go another direction. And let's start with some good news.

Since 2007, the US economy (our GDP) has grown from $14.5 trillion to $21.5 trillion. That's a seven trillion (!) dollar gain----or about a 50%---which is pretty good for a mature economy like ours.

Now, over those same 14 years, the stock market---and I'll use the S & P 500---has grown over 160%. So, Bob, that means the stock market has grown over three times faster than the overall economy.

Bob: But I would think the stock market should sort of track the economy. But maybe there is another explanation. I mean, everything today is international. So, did the world economy grow faster than ours? And could that explain why US stocks grew so fast? Especially for our big multinational companies.

Greg: Great question. And I wondered the same. So, I looked it up. World GDP in 2007 was $58 trillion. Last year it was $88 trillion. So, basically the world economy grew slightly faster than the US economy. So, that doesn't explain it.

So, let's look somewhere else…and a subject your poor listeners have heard me harp on for the past 3 ½ years. And that's debt.

And yes, there is a reason I started today's stats in 2007, because that is when the housing bubble started to pop.   And it's right after that the powers-that-be decided the best way to handle the crisis was to print money and rack up the debts.

Thus, since 2007, our total debt obligations have gone from $52 trillion to $82 trillion. Oh, and total debt obligations include everything from government debt to corporate debt to consumer debt.

Bob, the point is, while there has been some nice organic growth in the economy, it is also clear our GDP (and the stock market) have been propped up by ever growing debt obligations financed by artificially low interest rates.

Bob: So, Greg, that brings me back to the point I made on Monday. If zero percent interest rates and money printing are now vital to keeping both the stock market and the economy going, then we really can't go back to normal.

I mean, if we had 5% interest rates–or, if we tried to balance the budget–then all that external "financial juice" would dry up. That means any chance of a recovery goes up in smoke….especially as we try to claw back from Covid.

Greg: I think that is solid analysis. Which is why I don't believe you will see our money wizards take their foot off the stimulus gas anytime soon. In short, if the authorities get their way, the debts will rise, and interest rates will stay near zero.

So, let's play this out investment wise.

The outcomes will likely be:

- Pressure on the dollar. We are already seeing this. That trend will just continue.
- Rising prices. Inflation is already creeping into the American psyche. Just ask anyone who has filled a shopping cart recently.
- Commodity prices---think timber, aluminum, cotton, soy beans, stuff like that–should do well.
- You can add precious metals to that list, too.

Basically, Bob, the direction you and I identified a few years ago will continue…and I believe, accelerate. There is a lot of potential energy that must be expended before this trend exhausts itself.

Bob: It's only January 8th and I'm already exhausted. Good report. How do people reach you?

Greg: Yes. Quite the start to the year. My number is 250-3754. Or go to my website at zanettifinancial.com.

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