Hello Everyone,

"Mother's Day, Sunday 5/9.
Don't Forget To Buy A Bottle For Mom.
Remember You're The Reason She Drinks!" Sign outside a liquor store.

Inspired by that thought, I got my mom a gift certificate to ***Total Wine*** for Mother's Day. She was thrilled. Hmmm.

Today's missive doesn't have much to do with drinking. But if the Fed's "*inflation is transitory*" premise does not play out, the Fed Governors may want to consider hitting the bottle occasionally themselves.

I hope today's thoughts help you decide if the Fed is going to be right or wrong.

Signed, Your If-Lumber-Keeps-Going-Up-Can-I-Sell-My-House-For-Parts? Financial Advisor,
Greg

KKOB 05.10.2021 What If Inflation Isn't Transitory?

Bob: So, Greg, last week we talked about how the Federal Reserve is saying inflation is "transitory". And not to worry. But you took the other side. You said structural pieces were in place that indicate inflation will be with us for a while.

No offense. But I'd rather have the Fed be right than you.

Greg: I'd rather have that, too. Inflation disproportionality hurts the poor and middle class. And I hate that. So, let's hope the smart men and women at the Fed have their "*transitory inflation*" prediction right.

But what if they are wrong? How would we know—*that they know(!)*---their policies aren't working anymore?

And their <u>*current*</u> policies are this:

- First, keep interest rates low.
- Next, let inflation run so inflation rates are higher than interest rates. But not so much that everyone notices.
- Next, whenever the markets get spooked, prop them up with money printing… errrrr, Quantitative Easing.
- And finally, (and conversely) if markets get too euphoric, tamp them down by pulling money from the system. Or hiking rates. But that goes against step 1.

Bob: I can see everything you just said. The Fed has kept rates low. That has helped housing and stocks. Plus, every time there is a market correction, they step in and stimulate. And just recently they said they are OK with higher inflation rates.

It's quite the balancing act they have going on.

Greg: It is. I don't envy them. The complexities of the current situation have been decades in the making. And the Fed's ability to navigate through all this will be very relevant to your listeners' 401K plans and other investments. Which brings us back to ----- what if they can't keep all the plates spinning?

I mean, let's say inflation grips. What would you expect them to do? How would you know they are changing course?

I would say watch for the following steps:

Step One*: They will say they are willing to change their Quantitative Easing targets. In other words, they will remain at the ready to either crank up money printing or throttle it back if need be.*

The idea here is to "jawbone" the market into believing they have everything under control, and they can respond lightning-quick to any dangers ahead. This is what they are doing now.

Step Two: *Instead of talking about printing money, they will do it. They will intervene in the markets to try to force interest rates of different maturities either up or down.*

For example, if they want one year CD rates to go higher, but 10-year CD rates to go lower, they will use their money printing machine to make it happen. They call this "yield curve control". So, Bob, listen for that phrase.

Bob: Hmm. Yield curve control sounds like a fancy way of saying ***"interest rate control".*** And that doesn't seem like much of a free market.

Greg: You're right. And it isn't. This is why you have paid pros at all the brokerage firms watching every little thing the Fed says or does. When they read the Fed right, there is a lot of money to be made. If not…look out below.

But all that watching and analyzing springs off the assumption the Fed has total control.

But what if they don't?

This is when the next step occurs.

Step 3: The Fed attempts to control interest rates, ***but they can't.*** *The market starts to overwhelm the interventions. Interest rates start bobbing up and down like a kite on a windy day. And nothing the Fed says (or does) matters anymore. The Fed will then have no choice but to shut the whole thing down and regroup.*

But before that thought sparks panic among your intrepid listeners, remember we have shut down markets before to regroup. It happened after the crash of 1987. And again after 9-11. And again, when Lehman Brothers fell apart in '08. And, Bob, the world didn't end.

Bob: Still, I don't like the sound of it. So, what you're saying is when I hear the term ***yield curve control*** my radar should go up. Interesting report. How do people reach you?

Greg: Thanks. My number is 250-3754. Or go to my website at zanettifinancial.com.