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TRIPLE CROWN WEALTH MANAGEMENT GROUP

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It's getting late

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So, it pretty much feels like we're in this latest flimsy backdrop for finding another "valid" reason for stocks to go even higher still, i.e. the ongoing negotiations for a 5th new covid fiscal splooge of printed dollars, no matter how diminished those odds now stand for any movement on this subject until after the election and perhaps until the late January inauguration. When in fact, I'm pretty certain stocks just keep levitating from any discerning, reasonable and historically normal tether to their underlying fundamentals because central banks have long since spent all other options inclusive of ever allowing the return of real price discovery to be allowed to take hold. Now that their accrued bubbles are so incredibly massive and intractable, alas, they have no options remaining but to simply gun money supply to the heavens lest their bubbles burst. And given the magnitude of said massive bubbles, such an event would almost surly result in utter global financial and social chaos. However, so as to continue to mine for some remaining thread of normalcy for which they can assign to their broken era of bubbles run amok, hope of another massive round of fiscal stimulus appears to have for now taken the place of last year's flimsy logic when hopes of that "greatest trade deal ever" with China was deemed to be a "valid" reason to gun a myriad of stock valuations beyond anything ever seen including prior bubble peaks of 1929 or 2000.

I know some readers believe I have been too critical of the quality of the post-financial crisis bull market all the way up thru the pre-pandemic February highs of this year, and prior to the interim shutdown of the U.S. economy and the subsequent collapse in Q2 GDP. But I would hope that most of you can see now exactly what kind of global financial system, stock and bond markets we really have. Unfortunately, it has taken a pandemic and yet another wholly unprecedented globally wealth – cleaving coordinated responses by the globe's major central banks for it all to finally crystallize before the eyes of even the most casual market observer.

Index	Sept. 30 2020	YTD%
S&P 500	3363	+4.1%
Dow Industrials	27,782	-2.6%
Nasdaq Composite	11,168	+24.4%
Value Line Arithmetic	6235	-6.3%
Russell 2000	1508	-9.6%
U.S. Dollar Index	93.88	-2.9%
Gold (ounce)	$1889.00	+24.5%
Silver (ounce)	$23.49	+31.8%
Amex Gold Bug Index	326.96	+35.1%
Oil (NYM Lt Sweet/barrel)	$40.22	-34.1%
30 Year Treasury Yield	1.46%	-.93%
10 Year Treasury Yield	0.69%	-1.23%
2 Year Treasury Yield	0.13%	-1.57%

The S&P 500 is an un-managed index of 500 widely held stocks. The Dow Jones Industrial is an unmanaged index of 30 widely held securities. The Russell 2000 index is an un-managed index of small cap securities which generally involve greater risks. There is no assurance these trends will continue. The NASDAQ Composite Index is an unmanaged index of all stocks traded on the Nasdaq over-the-counter market. The Value Line Composite Index is composed of all of the companies that are included in the Value Line Investment Survey. The Dow Utility Average is an unmanaged index comprised of 15 utility stocks. The Amex Gold BUGS (Basket of Unhedged Gold Stocks) Index is a modified equal dollar weighted index of companies involved in gold mining. Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Past performance does not guarantee future results. Commodities and currencies investing are generally considered speculative because of the significant potential for investment loss. Their markets are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising. U.S. government bonds and Treasury bills are guaranteed by the U.S. government and, if held to maturity, offer a fixed rate of return and guaranteed value. U.S. government bonds are issued and guaranteed as to the timely payment and interest by the federal government. Treasury bills are certificates reflecting short-term (less than one year) obligations of the U.S. government.

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Weighed against the prevailing evidence of the severely impacted global and U.S. economy from the ravages of the global coronavirus pandemic this pandemic had essentially made landfall at a point in time where the business cycle was already as long in the tooth as any other in history, global debt levels were also higher than any other time in history relative to global GDP and U.S. stock market valuations by many very prominent historical valuation metrics (Market-cap-to-GDP, S&P Enterprise Value-to-Revenue, etc.) had never been higher. That was in February before most Americans even realized what they were up against with the rapidly spreading coronavirus. Can you truly say without smirking that for one of the most expensive debt ladened stock markets in history, pre-pandemic, and now with a subsequent collapse of over 30% (annualized) for Q2 GDP, as well as collapse in corporate earnings, that any of this makes sense absent the fact that the globes prominent central banks have simply stuffed financial markets to the gills with enough conjured-up fiat money for it to have occurred?

U.S. policy makers had already squandered any chance of being able to manage their way thru another crisis without suffering another significant blow to the Federal Government's balance sheet and forcing the Federal Re-

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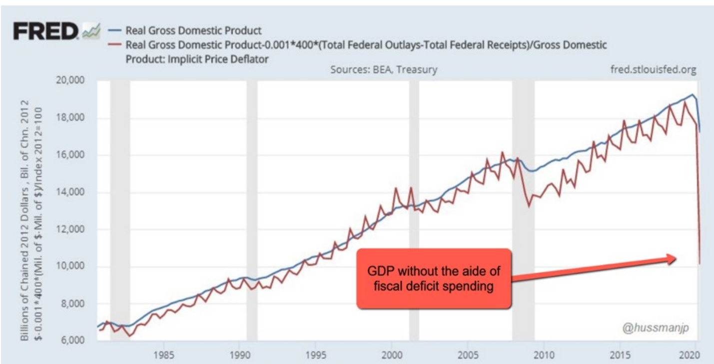
serve to once and for all abandon any hopes of extricating themselves from a policy paradigm of mere *hope and pretend* (that this is all normal). Following the budget busting 2017 corporate tax-cuts, the prospect of needing to finance even more vital financial assistance for those most impacted by the pandemic is not a comfortable feeling for anyone also concerned about the rapidly deteriorating fiscal state of the U.S. government. You can see below the degree to which even the historic crash in Q2 GDP would have looked like absent the massive splooge of fiscal deficit spending necessary to cushion the blow. That massive collapse depicted by the red line below is calculated by taking the traditional calculation of annualized GDP (Gross Domestic Product) but then subtracting the massive fiscal infusion of extra spending as if it were also on an annual basis. Essentially, that depicts the true collapse in U.S GDP absent the massive hole-plugging accomplished by temporary fiscal *borrowed* stimulus. Clearly, the fiscal burst of government stimulus that we saw in Q2 was never believed to be sustainable for another three consecutive quarters. But you can see how much worse the reported and still historic collapse in Q2 GDP would have been without the hole filling assistance of all of that deficit spending Covid financial aid that was spent in April thru June and has since mostly dried-up.



Red line is real annualized U.S. GDP less real annualized federal deficit spending (calculated as 4 x the quarterly total of federal outlays less reciepts, not seasonally adjusted, deflated by the GDP implicit price deflator). Factors: 0.001 $million= $billion. 400 due to deflator scaling.*

Real annualizes GDP v. Real annualized GDP, less annualized fiscal spending, 1980-Current (Source: St. Louis Federal Reserve/John Hussman)

Alas, even as economic activity has bounced significantly from the lows of late April when air travel, hotels and indoor dining were essentially totally shuttered for roughly 6-weeks, the number of Americans currently employed is still roughly 25-million less than in February. Absent additional "hole filling" fiscal aid, you don't think the economic data wont get significantly worse over the next few months and late into the fall and winter without more deficit spending? Again, its sad that we're in this position, but perhaps our legislators should have been readying the Federal balance of payments situation in the years leading up to this instead of giving more tax breaks to corporations and billionaires? Again, we were on our way to recording a second consecutive annual Federal deficit above $1-trillion prior to any of this.

A recent report published by Jesse Felder in his excellent Felder report highlighted pretty much what I've described above in his report titled, <u>*This Is What 'Fiscal Dominance' Looks Like*</u>. Always an excellent brief read, Felder reminds us of his report back in the early fall of last year when Powell and the Fed were forced into providing unusual quantities of liquidity thru their use of overnight repurchase agreements with banks. Again, this was prior to any of us ever hearing of Covid-19. Felder argued at the time that the Fed's unusual step of needing to provide record amounts of overnight banking liquidity was not technically a return to quantitative easing as many had described it. This was even though the operations resulted in one of the most rapid expansion of the Fed's balance sheet ever on a monthly basis from last September thru this February. Again, this was occurring without there being any clear indication of a rapidly fading economy, even though it had clearly decelerated from its 2018 corporate tax-cut sugar high. Instead, Felder described the unprecedented operations as the Fed simply acting as the lender of last resort for the Federal Government, amidst rapidly rising debt levels, associated with those 2018 tax cuts. Felder says bluntly, "*It was, in its purest form, a commitment to monetize that amount of debt that could not be absorbed by the market."* However, over a year later and with the legislative urgencies associated with trying to buttress some of the most excruciating financial strains associated the pandemic on top of its pre-pandemic, debt-soaked and bubble-centric economy, and in an election year no less, Felder opines that we have traversed from *lender of last resort* for the Federal government, to one best described as, "*fiscal dominance."* This, as described by Felder, is where the Fed has essentially been forced to abandon its prior mandates of policy steered by its pursuit of *"stable prices"* and "*full employment*." Felder explains that this is now, "*a scenario in which a country's debt grows so large that the central bank is forced to abandon whatever ostensible mandate it has been given for a new, unspoken one: print as much money as is required to fund the government and prevent a debt spiral,"* and thus, the Fed is now no longer "*master of its own domain*," so to speak and is instead now being forced into a game of '*follow the leader*.' In his report, Felder cites a clarifying explanation of this from the former Chief Economist of the BIS (Bank for International Settlements), William White, who explained it this way, '*At some point, people realise that the government can't support the debt burden without going back to the central bank to print more money. This is a tipping point.'* Felder declares, "*We have now reached that tipping point."*

Quoting economist Mohamed El-Erian, also a frequent guest on CNBC, in a recent Bloomberg article titled, <u>*Fed, Central Banks Will Find Exit From Massive Stimulus Impeded,*</u> El-Erian laments, "*They are increasingly on what I call a no-exit paradigm*." In the same article former Fed Governor Randal Kroszner cited the obvious. Having implicitly encouraged record debt issuance amidst a totally falsified global interest rate backdrop amidst the 10+ years of overt interest rate manipulations which have sent a continuous and relentless string of errant transmission signals throughout global markets concerning default risks, and inflation (which continues to be under reported so as to give the central banks political cover for their misdeeds), Kroszner warns, its *"going to make it difficult for central banks to raise rates when they feel the need to do so,"* due simply to the god awful accrual of global debt loads. European Central Bank President Christine Lagarde, also quoted in the story, unfortu-

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nately opined on something that suggests we are already where she doesn’t want to go. Legarde opined, *“We have to steer clear of what would be regarded in popular parlance as fiscal dominance.”* Too late.

As longtime readers are aware, I had opined from day-1 when Ben Bernanke introduced broadscale QE to the once proud U.S. economy, once you take a step down that path, there is no turning back. We are now so far down that path, any bread crumbs left as a means to retrace our path have since been consumed by the jungle critters. There’s no goin’ back now. Felder concludes that, “*Investors should understand that this is a marked change from the monetary policy of the past in which the Fed could pursue its dual mandate without being hindered by fiscal policy. Fiscal policy is now officially taking the wheel and the dual mandate is taking a back seat.”*

While our political environment suffers from an acute lack of rigorous critical thought, our markets continue to suffer from the same; conditioned by the relentless efforts of global central banks whose single goal, seemingly can now be described as trying to blur and obscure real price discovery. What comes of this are such logic-challenged manifestations that insult all capacities of deductive reasoning. Perhaps the most obscene of these distortions is the abundance of debt that now trades on global markets with negative yields. The lacking of critical thought is only reinforced by the unprecedented level, size and scope of global central banking interventionist policies which seemingly flatter the absurd. Again, remember last year’s “*trade deal going great*” algo bait dangled in front of markets all of last year? Hope of that pending trade deal ran cover for a drastically slowing economy and almost no corporate earnings growth. Since the close of the year, following the second stoutest performance of the S&P 500 since 1998, and ending the year with valuations rivalling the 2000 tech bubble, we have since suffered a global pandemic, GDP suffered its largest quarterly collapse ever, S&P earnings have collapsed, the pandemic marches on and consumer apprehensions continue to linger. But the dangling “*trade deal going great*” carrot has been seamlessly replaced with “*vaccine development is close*,” and, “*stimulus deal is close*.” We now not only have by far the most overvalued stock market in history by a multitude of historical measures, this is also occurring amidst a backdrop of perhaps the most uncertain economic conditions in modern history. The encroaching general election amidst the most rancid political environment perhaps ever, with seeds of doubt as to the integrity of the outcome of that election now being sown by a sitting U.S. President, combined, marks a point in history for the most absurd misallocation of capital in world’s history (my opinion).

If had posed the following scenario to you this time last year what would you had expected the stock market to do? Overnight banking liquidity would begin to seize in August forcing the Fed to ramp-up emergency repurchase operations. The highly anticipated Chinese trade deal would eventually be signed in December, but it would be a shell of its intended goal and then none of what was mandated, i.e. Chinese agriculture and industrial purchase agreements would come even close to being fulfilled. By October (now) trade tensions with China would deteriorate even further. A pandemic would broadside the global economy including a nearly full shutdown of non-essential businesses in the U.S. and Europe during the spring resulting in a more than a 30% collapse in second quarter GDP. All and more of the net U.S. job gains going back over 4-years would be entirely reversed. Hong Kong, a major banking epicenter linking Asia with the West, will fall into chaos and be annexed by China’s Communist Party and Brexit would remain unresolved. An encroaching election in November would pose significant risk including the prospects of the current sitting President sewing doubt as to the validity of its outcome. His opponent, Joe Biden, coupled with the prospects of a flip of power in the U.S. Senate would almost surely result in a full reversal of those 2017 corporate boondoggle tax-cuts which could slice as much as 10% of expected 2021 corporate earnings off the top, per many estimates. Despite this scenario that I’ve laid out for you, how much lower would the S&P 500 and the Nasdaq 100 be this time next year? Again, I'm asking this hypothetical question this time last year. What? Oh, stocks would be higher? Not only higher, the Nasdaq 100 would record one of its most prolific year-over-year rallies in the history of that index. Makes total sense, huh? Again, markets by design seem to conspire to force most people to buy at the top and sell at the bottom but they should be a total afront to all common sense.

Alas. markets have significantly been bastardized from most of their fundamental tethers of real price discovery and are now almost nothing more than a temperature gauge which is effectively nothing more than an amalgamation of all the prevailing current bubble era manifestations. Including the ease at which debt, the current era’s primary growth diver, can continue to proliferate amidst falsified interest rates and obliterated price discovery, ongoing investor confidence in passive investing void of hardly any value rationales, whatever prevailing themes are ably capable of gaming stock buying algorithms and credit markets remaining numbed and subservient to ongoing central bank manipulations and thus acting as an ongoing accomplice to accruing systemic leverage and risks instead of acting as a prudent arbiter of risks, as credit markets are meant to be.

So we’re probably trapped in this bizarro world where real price discovery continues to be run roughshod by all of the above circular self-reinforcing bubble manifestations fomented by this paradigm of unrelenting central banking radicalizations until something simply gives. However, I couldn’t even muster a guess when the central banks lose control. Jim Bianco, President of the firm that bears his name, Bianco Research, recently described an eventual scenario whereby the central banks *might* eventually succumb to the very beast they’ve created:

> *"One of the things that's larger than central banks is the market itself. The Fed wants to let inflation run because they want unemployment to go down. They're sincere about that, but when the bond market decides that inflation is a problem, the Fed is going to be forced to react. Think about it this way: The Fed is like a post, and the market is a horse tied to that post. If you tie a horse to a post, it just sits there, and it doesn't do anything for a while. But a horse is a 1,500-pound animal, and if inflation spooks the horse, it will tear the post right out of the ground and*

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run away. So, yes, the central banks can control the bond market for some time. But when you spook it, it will rip that post right out of the ground and go, no matter what the central banks try to do to tamp down rates…."

Amidst all of this, Congress continues to debate another batch of fiscal bailout funding. As of this writing, nothing has yet been agreed upon. But even if the House and the Senate were able to pass a so-called "skinny" $650-billion package, that would bring the total level of Federal pandemic economic relief to $4.25-trillion, compare that to the lone bill of Federally funded economic or market relief passed by Congress in the midst of the 2008 financial crisis via TARP (Troubled Asset Relief Program). That bill originally authorized Federal spending of $700-billion, but was reduced to just $475 billion when a later bill was passed, the Dodd-Frank Act. So, this perhaps illuminates the degree to which markets and the U.S. economy have become both so incredibly complacent and enabled by ever-increasing doses of both fiscal and monetary stimulus absent any real consideration and appreciation for the privileges we as a country have enjoyed up until now for maintaining the mantle as the globe's currency hegemon and the economy's backing of what for now is still the world's reserve currency. Maintaining that status simply cannot be understated and up 'til now it has provided the U.S. the ability to at times take liberties, fiscally, for which other countries would otherwise be onerously penalized by capital markets and thus are unable to implement without possibly sparking a run on their respective currencies and ultimately ushering-in a bout of rampant inflation. Given the growing complacency surrounding our deficits and fiscal profligacy now emblematic of both parties, I suspect, means that we're just eventually going to find out the hard way what it means to have that mantle eroded or taken away. With that said, I do believe there is a segment of our society that is being pushed to the financial brink and that regardless of the incremental fiscal costs, these folks and entities (some cities, states and municipalities that need funding for vital regional safety net funding) need help now. The cost of not doing so is going to be even more costly to our society at large. Either way, its incumbent that we figure out a way to turn the table on the current brand of out-of-control corporatism whereby nearly all the marginal economic benefits continue to accumulate at the very tip-top of the wealth and income strata.

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