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THE "YOU MAY NOT KNOW REPORT"

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Economic Update and Outlook – Mid-Year 2021

By Dennis Tubbergen

To say there is a lot going on in the economy, in financial markets and with monetary policy would be a severe understatement. In this issue of the "You May Not Know Report", I'll do my best to give you a report on where we are presently and where I believe we go from here.

Let's get started.

The big economic news presently is the emergence of inflation. Many of us have been talking about this inevitability for a long time. Excessive money creation means inflation.

As I recently discussed with RLA Radio guest, Karl Denninger, money creation doesn't immediately lead to inflation, but it does eventually. Chart 1 (page 2, top), from www.ShadowStats.com illustrates the money supply.

Notice the straight up move on the chart representing a radical increase in the money supply beginning in 2020.

It's now apparent that we are seeing the effects of that immense level of fiat money creation.

The St. Louis Federal Reserve Bank publishes M2 money supply. The chart (page 2, middle) illustrates.[1]

Notice from the chart that the M2 money supply has increased to more than $20 trillion in April of this year, up from a bit more than $15 trillion at the beginning of 2020.

Chart 1: *Annual U.S. Money Supply Growth*

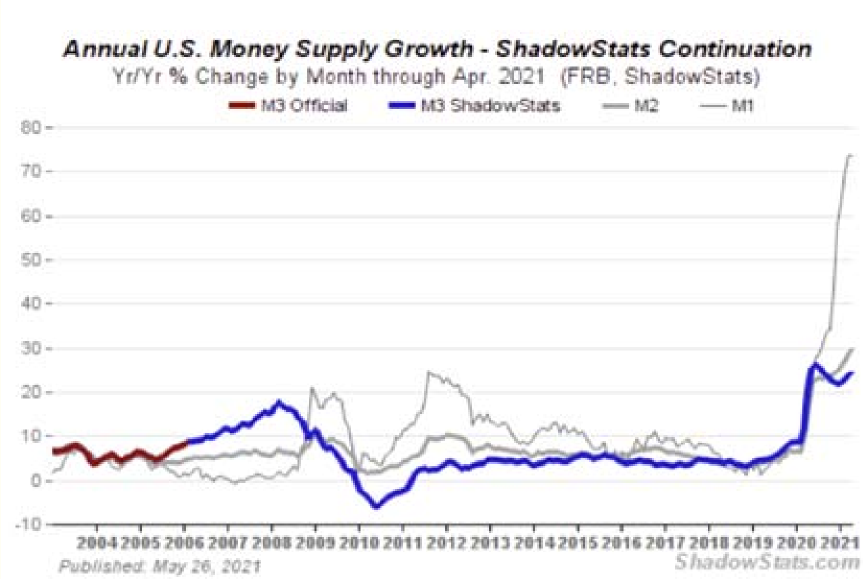


Chart 2: *M2 Money Supply*

When the money supply increases at that pace, inflation has to be the ultimate outcome.

Now that inflation has arrived, what has the Federal Reserve's response been?

As anyone who has followed the Fed for any length of time knows, if the reported data looks bad there are one of two actions the Fed has taken historically.

One, they change the way the data is reported.

Or, two, they quit reporting the data.

In this case, predictably, the Fed chose the latter. This[2] from David Kranzler of Golden Returns Capital (red font added for emphasis):

> *Ben Bernanke, outgoing Fed Chairman 2014:*
>
> ***"Fostering transparency and accountability at the Federal Reserve was one of my principal objectives when I became Chairman in February 2006."***
>
> *Janet Yellen, 2013 as Vice Chairman of the Fed:*
>
> ***"Recently I used the word 'revolution' to describe the change from 'never explain' to the current embrace of transparency in the FOMC's communication."***
>
> *Fed Chair Jerome Powell, 2018:*
>
> ***"In a democratic system, any degree of independence***

brings with it the obligation to provide appropriate transparency. In turn, transparency provides an essential basis for accountability and democratic legitimacy by enabling effective legislative oversight and keeping the public informed."

Over the years, I've learned to keep one hand on my wallet and one hand on my physical gold and silver safe when a Fed official promises more transparency.

Right after Bernanke promised more transparency, the Fed decided to no longer report the M3 measure of the money supply. The U.S. is the only major industrialized country that does not report M3.

With Jerome Powell at the helm, earlier this year the Fed quietly obscured the distinction between the M1 and M2 money supply measures, making it almost impossible to distinguish between bank demand and term deposits.

This is important because each classification provides information about the relative liquidity of the banking system. Now that distinction is impossible to assess.

Tuesday (May 11) the Chicago Fed announced that it would discontinue publishing the Midwest Economy Index after the Jun. 30, 2021, release:

"Our researchers' standard approach for estimating the Midwest Economy Index (MEI) has become increasingly ineffective. As of early May 2021, we have determined that it will not be appropriate to publish the MEI's results after the middle of the year."

What is the Fed trying to cover up by eliminating this economic report? ***Interminable economic weakness masked by economic indices that show nominal gains which are primarily attributable to the price inflation effects of money printing rather than an increase real economic activity.***

Make no mistake, the economy is much weaker than the politicians, Fed officials and Wall Street animal are willing to admit. And much of what is reported as increasing economic activity reflects little more than the effect of price inflation on the input components of the various indices.

1970's stagflation on steroids.

As such, ***the Fed is removing the trail of evidence and is preparing to take its money printing to a new level, in an a tragically flawed effort to stimulate real economic growth.***

While inflation is undeniable, there is another trend taking place that makes the inflation even more dangerous. As Mr. Kranzler notes in his piece, the economy is not strong. In real terms the economy is contracting.

In case you missed it, Kranzler makes a very important point. He says that when increasing economic activity is reported, it is the direct result of price inflation (or currency devaluation) rather than being attributable to real economic growth.

Mr. John Williams of www.ShadowStats.com (referenced above) tracks the economic output of the United States, typically measured by Gross Domestic Product. As John explains on his website, the headline or reported GDP number refers to the most recent quarter's annualized quarter-to-quarter rate of change. In other words, the headline number is the annualized GDP number if the most recent quarter-to-quarter change was compounded for four consecutive quarters. What this means is that the latest quarter can be reported as a positive

Chart 3: *GDP Annual Growth*

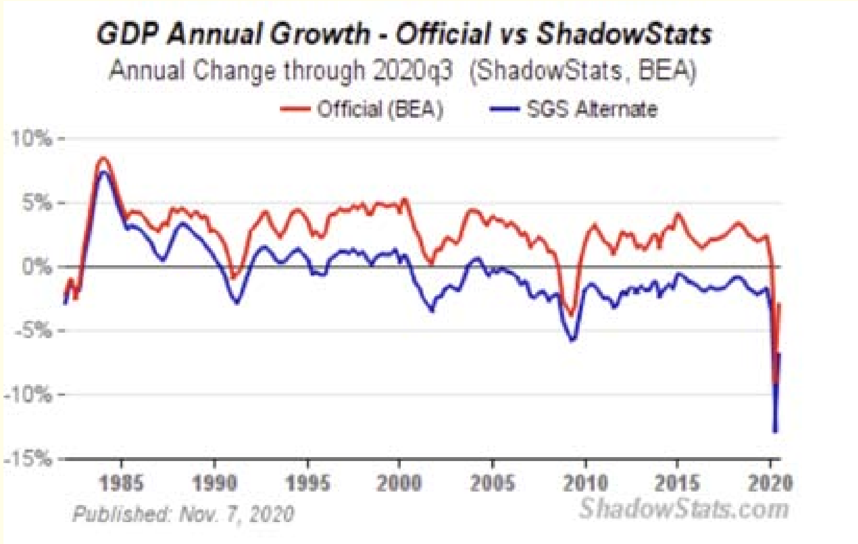
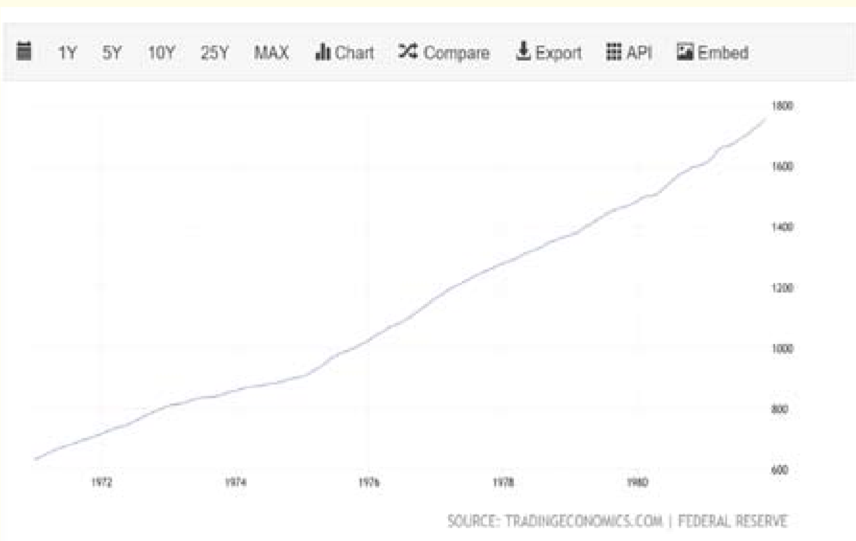


Chart 4: *Increase in Money Supply (1971-1981)*



annualized rate of growth while the actual annual rate of change is negative.

Chart 3 (this page, top), courtesy of www.ShadowStats.com, shows that GDP or economic output is contracting.

Keep in mind that GDP is contracting even when it's measured in US Dollars that have been devalued through excess money creation.

Bottom line economically speaking is this – we are now looking at stagflation which is inflation combined with economic contraction.

There is only one way to cure stagflation, stop inflation by reducing the money supply and then endure the inevitable recession that follows. If you're old enough to remember the 1970's, you've lived through the stagflation cure.

This time around there is one additional dynamic that may be the most significant. Fiat currencies may be on their last legs.

Long time readers of this report undoubtedly know that it was in 1971 that the US Dollar officially became a fiat currency. That's when the link between the US Dollar and gold was eliminated.

Chart 4 (this page, middle) shows the increase in the money supply that occurred from 1971, when the US Dollar became a fiat currency to 1981. Notice that the M2 money supply about tripled over a 10-year time frame.

We have seen the same rate of growth in the money supply since the financial crisis with one difference; the rate of growth has been much more extreme this time.

That can only mean a more extreme outcome in my view.

In the 1970's, there was no talk worldwide about moving away from the US Dollar as the world's reserve currency. That is not the case today.

Russia has now openly stated that she is moving toward gold and away from the US Dollar.

This[3] from "Zero Hedge":

> *Following a series of corporate cyberattacks that American intelligence agencies have blamed on Russian actors, Russia's sovereign wealth fund (officially the National Wellbeing Fund) has decided to dump all of its dollars and dollar-denominated assets in favor of those denominated in euros, yuan - or simply buying precious metals like gold, which Russia's central bank has increasingly favored for its own reserves.*
>
> *Finance Minister Anton Siluanov made the announcement Thursday morning at the annual St. Petersburg International Economic Forum.*
>
> *"We can make this change rather quickly, within a month," Siluanov told reporters Thursday.*
>
> *He explained that the Kremlin is moving to reduce exposure to US assets as President Biden threatens more economic sanctions against Russia following the latest ransomware attacks. The transfer will affect $119 billion in liquid assets, Bloomberg reported, but the sales will largely be executed through the Russian Central bank and its massive reserves, limiting the market impact and reducing visibility on*

what exactly the sovereign wealth fund will be buying.

Just a few days ago, we reported that the Russian parliament had just authorized the sovereign wealth fund to buy gold through the central bank. However, the central bank reports its holdings with a six-month lag, making it impossible to determine its current holdings.

Russia's gold holdings eclipsed its dollar reserves last year despite a halt in gold purchases. This was partly due to an increase in the value of its gold holdings with the rise in gold prices, and partly a function of the central bank's continued efforts to shed dollar assets.

While politics may play a role in this decision, from my perspective, it's a lot simpler than that. One look at a price chart of the US Dollar Index tells the story.

Note on Chart 5 (below) that from January of 2020 to the present time, the US Dollar Index has declined by more than 12%.

Keep in mind that the US Dollar Index is not an absolute measure of the purchasing power of the US Dollar, instead it is a relative measure that compares the purchasing power of the US Dollar to the purchasing power of the six major trading partners of the United States.

A better measure of the absolute purchasing power of the US Dollar can be discovered through personal experience in making purchases. Using that as your metric, one can understand why the international move away from the US Dollar continues.

Currently, it seems that the money creation is poised to continue. That will mean more inflation.

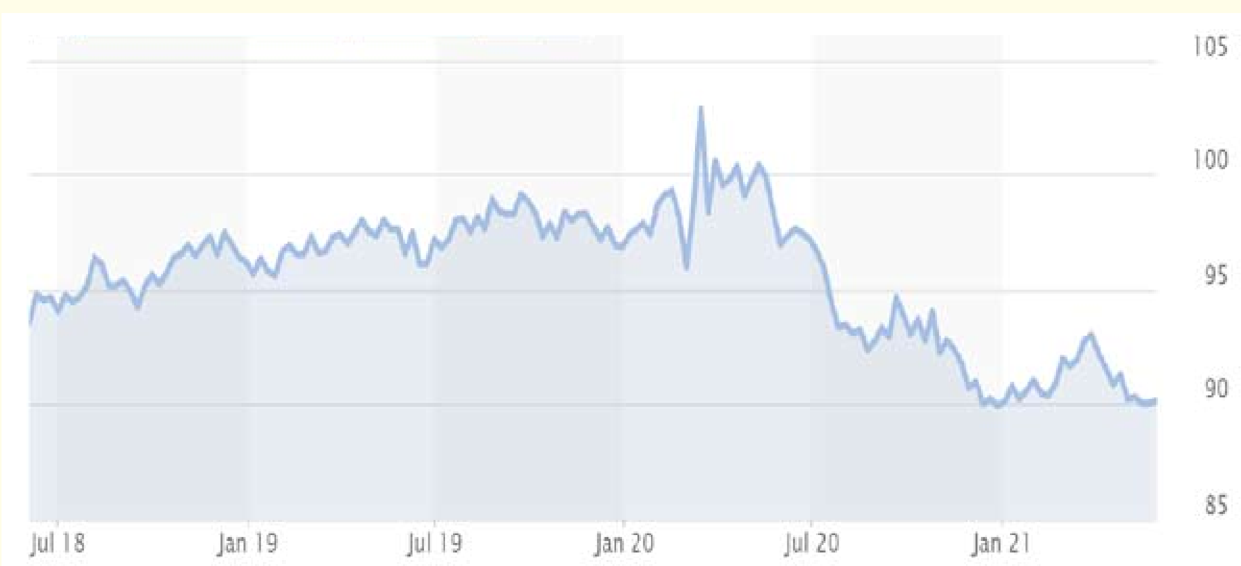
Ultimately, as I have often stated, the money creation will stop. History teaches us that it always does.

The questions are when will it stop and how will it stop?

In my view there are only a couple possible scenarios.

One, there is immense political pressure placed on politicians and the Fed to get inflation under control. While getting politicians to act somewhat responsibly may seem more like a pipe dream than reality, this could actually be a

Chart 5: *US Dollar Index*



possibility at some point in the not-too-distant future.

Inflation, or stagflation affects lower income workers to a much greater extent than it does higher income workers since they have to spend an ever-greater percentage of their income on necessities like food and housing.

When basic living essentials become unaffordable for many lower- and middle-income Americans, there could be a call for the Fed to take action. Since the Fed has only one tool – money creation, their only choice will be to stop money printing or slow it down significantly.

That will bring on the deflationary collapse.

Two, the Fed continues to print to the point that confidence is lost in the currency. History teaches us that when confidence in a currency is lost, those who are using the currency begin to look for alternatives.

Should money creation continue long enough to get to that point, a new currency system will have to emerge, and the deflationary collapse will begin.

In my view, we are quickly approaching one of those two outcomes.

Lower- and middle-income households are already beginning to feel the inflationary heat. This[4] from "Zero Hedge" (emphasis added):

> *A United Nations index of world food costs climbed for a 12th straight month in May, its longest stretch in a decade, rising to the highest in almost a decade, heightening concerns over bulging grocery bills.*
>
> *All five components of the index rose during the month, with the advance led by pricier vegetable oils, grain, and sugar.*
>
> *Month after month, the UN's Food and Agriculture Organization's food price index continues to soar to levels not seen in a decade.* ***Soaring food prices have tremendous implications on societal trends and may result in unrest in emerging market countries if trends persist.***
>
> *For May, the FAO Food Price Index, which measures monthly changes for a basket of cereals, oilseeds, dairy products, meat, and sugar, surged to an average of 127.1 points in May, 4.8% higher than in April and 39.7% higher than in May 2020.*

In 2019, households in the lowest quintile of income spent $4,400 annually on food which represented 36% of their income[5]. Doing a little simple math and applying the nearly 40% increase in the FAO Price Index over the past year, one concludes that these lower income households are now spending about 50% of their income on food.

That's a substantial increase.

Sadly, fuel costs, energy costs and housing costs have all also increased. That puts a large number of US households in a position where they cannot afford basic essentials.

Much of the population doesn't buy the Fed's argument that inflation is 'transitory'. The number of Google searches for "inflation' has dramatically increased last month[6]. This from past RLA Radio Program guest Peter Schiff:

> ***According to Google Trends, searches for the word "inflation" hit the highest level since 2004 between May 9 and May 15. That's as far back as the data goes. Google charts trends numerically and during that time period interest in "inflation" went all the way up to 100.***
>
> *If you look all the way from 2004 until the end of 2020, pretty much all the searches were pretty consistent at about 50. And now, in the*

beginning of 2021, is where we shot up from 50 all the way up to 100. So, something changed in 2021 that resulted in all these people all over the United States deciding independently that they were going to search inflation."

So, why are they doing that?

Well, because they're worried about it! If it was transitory, would they care? They care because it doesn't seem like it's transitory."

On the other hand, the Federal Reserve continues to ignore the signs that inflation is here to stay and pretends it's transitory.

We can't just pretend and play make-believe and hope the problem goes away. *Because they tried that with the mortgage problem. Even though it was obvious that subprime was the tip of a huge iceberg, the Fed kept saying, 'Don't worry. It's contained,' because they were hoping that if they denied the problem, maybe it would go away. Well, they're doing the same thing again with inflation. They're telling all the people who are so worried about inflation, 'Hey, don't worry about it because it's just transitory.' Well, it's as transitory as subprime was contained."*

In fact, the Fed is driving inflation through its monetary policy and debt monetization.

Through the first 7 months of fiscal 2021, the US government collected about $2.1 trillion in taxes but spent about $4.1 trillion.

That means $2 trillion was borrowed and basically funded by the Federal Reserve. And these are the official numbers. The unofficial numbers are even worse."

And consider this: the deficit through the first 7 months of 2021 is higher than the first 7 months of 2020, which included the depth of the COVID recession.

The government is spending even more money and running even bigger deficits now, when the economy is supposedly in recovery, than it was when it was still in recession, which again proves that there isn't a recovery at all. It's phony. The only reason the economy looks like it's recovering is because the Fed is printing all this money to artificially stimulate it. But the way you see the truth is to look at the increase in prices that the Fed is still denying exist. They don't want to acknowledge that inflation is not transitory because then they have to acknowledge that it's the recovery that's transitory because it doesn't actually exist, and inflation is going to kill it."

This puts the Fed in an awkward position. Typically, the cure for a recession is inflation. But how can the Fed cure a recession caused by inflation by creating more inflation?

The Fed's 'go to' strategy of reducing interest rates quit working after the financial crisis when interest rates were reduced to zero with little positive benefit. Consequently, the Fed began the 'emergency' and 'temporary' action of money creation.

As I noted at the time and in my 2011 book "Economic Consequences", money creation always puts an economy on the slippery slope of a collapse. While money printing can temporarily stave off the inevitable collapse, the collapse always, eventually, inevitably comes about. Money printing makes the eventual collapse worse than it would have been had money creation not been pursued.

When money printing quits working, there is no other strategy remaining.

We are getting close to that point in my view.

If you are a long-term reader of this report, chances are good that you are already utilizing some form of the two-bucket approach to managing money. This approach has you dividing your assets into two buckets of assets with each bucket allocated to achieve a specific outcome. One bucket of assets to protect from the continued and perhaps intensifying inflation and the other bucket allocated to attempt to keep assets stable in a collapse.

Many longer-term readers and clients have already allocated some of their inflation bucket assets to precious metals. That strategy has worked out well for those that have used it.

Until the money creation stops, I would expect that owning metals with some of your portfolio will continue to be advisable.

When owning precious metals, it is important that one owns the physical metal to eliminate counter-party risk. But there is another reason as well; there is a growing price disparity between the price of 'paper' gold and silver and 'physical' gold and silver.

The simple reason is that 'paper' gold and silver can be created out of thin air by futures traders. Physical gold and silver cannot be created or printed from thin air. Demand for physical metals is increasing as more precious metals investors are realizing that physical metals may offer some protection against inflation without counterparty risk. That is not true of paper gold or silver.

The US Mint recently acknowledged that there is a shortage of physical silver[7] (emphasis added):

> *The United States Mint is committed to providing the best possible online experience to its customers.* ***<u>The global silver shortage has driven demand</u>*** *for many of our bullion and numismatic products to record heights. This level of demand is felt most acutely by the Mint during the initial product release of numismatic items. Most recently in the pre-order window for 2021 Morgan Dollar with Carson City privy mark (21XC) and New Orleans privy mark (21XD), the extraordinary volume of web traffic caused significant numbers of Mint customers to experience website anomalies that resulted in their inability to complete transactions.*
>
> *In the interest of properly rectifying the situation, the Mint is postponing the pre-order windows for the remaining 2021 Morgan and Peace silver dollars that were originally scheduled for June 1 (Morgan Dollars struck at Denver (21XG) and San Francisco (21XF)) and June 7 (Morgan Dollar struck at Philadelphia (21XE) and the Peace Dollar (21XH)). While inconvenient to many, this deliberate delay will give the Mint the time necessary to obtain web traffic management tools to enhance the user experience.* ***<u>As the demand for silver remains greater than the supply, the reality is such that not everyone will be able to purchase a coin</u>.*** *However, we are confident that during the postponement, we will be able to greatly improve on our ability to deliver the utmost positive U.S. Mint experience that our customers deserve. We will announce revised pre-order launch dates as soon as possible.*

Recently, on the RLA Radio program, I chatted with Alasdair Macleod about how paper gold and silver can be created literally out of thin air. Mr. Macleod discussed regulation changes that are coming that would put a stop to this practice. These new rules will be in effect in Europe by the end of June and effective in the UK by the end of the year.

In my view, this rule change as well as the economic conditions we've discussed in this month's issue could be extremely bullish for precious metals. If you would like to discuss adding metals or more metals to your portfolio, feel free to reach out using the contact information below and we'll schedule a complimentary call to answer your questions.

Finally, this month, I would be remiss if I didn't address the rent moratoriums expiring at the end of this month. This has the potential to be the pin that pops the bubble.

This[8] from CNBC (emphasis added):

> ***More than 10 million Americans, or 14% of U.S. renters, say they aren't caught up with their housing payments****, meaning many could be at risk when the national moratorium on evictions expires in under a month.*
>
> *That finding comes from data collected by the Census Bureau between May 12 and 24 and analyzed by The Center on Budget and Policy Priorities. The CBPP also found that more than 26% of Americans continue to have trouble meeting their usual expenses, and around 9% couldn't afford enough food.*
>
> ***With so many renters still behind, the number of evictions could rise steeply when the Centers for Disease Control and Prevention's eviction moratorium lifts on June 30. That protection will have been in place for 10 months.***
>
> *Although the policy hasn't reached all renters, it's reduced the normal number of eviction filings over the same time period by at least a half, according to Peter Hepburn, an assistant professor of sociology at Rutgers University-Newark and a research fellow at The Eviction Lab.*

Should 10 million Americans get eviction notices, the impact on the economy could be devastating.

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If you know of someone who might appreciate getting this information during these challenging times, feel free to have them download the free app as well.

If you have questions when downloading the app or would like assistance, feel free to call the office. Our office phone is **1-866-921-3613**. Our office phone is answered 8 to 5 Monday through Thursday and 8 to Noon on Friday.

Sources

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