Retirement Lifestyle Advocates

RADIO PROGRAM

Expert Interview Series

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Dennis Tubbergen:

Welcome back to RLA Radio. I have the pleasure of chatting once again with Dr. A. Gary Shilling. Many of you will recognize Gary as a returning guest. He has been a Forbes columnist for 40 plus years, he is a regular contributor to Bloomberg. In fact as I'm recording this he just posted Gary Shilling's Guide to the Post-Pandemic Economy, Part 3, which I read. And Gary, welcome back to the program. It's always a pleasure to catch up with you.

Dr. A. Gary Shilling:

Same here Dennis. Thanks.

Dennis Tubbergen:

Well, and I will mention too that Gary publishes a terrific newsletter called Insight. And if you'd like to learn more about the newsletter go to agaryshilling.com or you can get a complimentary copy by calling his office at 888-346-7444. I'll give that number again before this segment is over. So Gary I've got to get your take on this, the inflation rate even when measured by the consumer price index is very, very high. What's your inflation forecast moving ahead?

Dr. A. Gary Shilling:

I think it's going to calm down. I'm of the opinion, and this is the Fed's view and I don't always agree with them but, I think a lot of this is temporary. It's really supply chain bottlenecks and economic reopening friction. Now the real question though is, will this spawn inflationary expectations? And you might recall that's what we had in the 1970s when people thought, hey, prices are going up I better buy now, last chance. And of course that meant that inventories were depleted, productive capacity was strained, so prices went up, suspicions were confirmed, and that meant that people bought even more and it was a self-feeding cycle.

Dr. A. Gary Shilling:

We haven't had that, it hasn't developed so far. But that's the risk, that's the thing that I'm looking for. But if we don't get that then I think the inflation situation is going to calm down. And I continue to believe, Dennis, that the primary driver of inflation is excess demand. And when you have excess supply, you have deflationary pressures. And right now, of course, we continue to have excess supply because China and other Asian economies are huge, huge producers but very, very parsimonious consumers.

Dr. A. Gary Shilling:

It's the saving gluts, the supply as a result worldwide exceeds demand. You look at China, their consumer spending is a percentage GDP is 42%, in this country it's 69%. Almost twice as much. They're big savers and that saving glut is a counterpart of excess supply. So I think fundamentally you have very strong deflationary pressures, and I think they will reassert themselves after this current spat of inflation because of supply chain bottlenecks and the frictions of reopening economy subside.

Dennis Tubbergen:

You know Gary, I've interviewed a number of bright people here on the program who are of the opinion that the Fed's quantitative easing or currency creation, if you will, are going to lead to those inflationary expectations and have people accelerate purchasing and get out of the dollar. And there's some pretty dismal forecasts among some pundits out there. What would your perspective be relating to those positions?

Dr. A. Gary Shilling:

Well first of all, the dollar has been very strong lately as I'm sure you're aware, so it's quite the opposite. Things can change, but so far there's no evidence of that. And also of course people, consumers have saved the vast majority of the three rounds of fiscal stimulus they got in response to the virus. In the middle of last year they saved 75% only spent 25%, the one in December they saved even more, 76%, and the one this past March they saved 78%. So people have saved, they have not spent that money. I think that the pandemic just scared a lot of people.

Dr. A. Gary Shilling:

And the Federal Reserve Survey show that 16% of millennials don't have 400 bucks in reserves to handle contingencies. So I think that we're going to continue to see high saving, moderate spending. And as a result, we're not going to see those kinds of pressures which many people are forecasting. But of course you know they've been saying that ever since the stimulus in response to the virus started really a year and a half ago. But so far, there's no evidence of that and I don't see why it's going to suddenly change.

Dennis Tubbergen:

Well if you're just joining me, I'm chatting today with Dr. A. Gary Shilling. His website is agaryshilling.com, and his terrific newsletter, Insight, is a complimentary copies available to our listeners today by calling 888-346-7444. So Gary, the Fed has recently announced that the taper will begin. 15 billion a month and that's going to continue. As I recall, you can correct me if I'm wrong, but back in 2018 they started to taper, markets didn't like it and they quickly reversed course. Is this the real thing this time?

Dr. A. Gary Shilling:

It certainly has been advertised. I think after the taper tantrum, as we called in 2018 when Ben Bernanke was Fed Chairman, these guys at the Fed I think they really had gotten scared. And there's been plenty of discussion and anticipation, but that doesn't mean there isn't going to be effect. And what's really at stake here is how much speculation, how much excess leverage, how much borrowing? And financial problems are always, regardless of the root of them, they're always magnified by leverage, by financial leverage, excess borrowing. And of course that's what you've had with so much money pumped out there by the Fed.

Dr. A. Gary Shilling:

Now it's not going into spending, the turnover of money has collapsed even though the money supply is going through the roof, but a lot of it is going into speculations. And that's the $64 trillion question is, are we going to see a lot of blood on the floor as all these things...? You have individual investors, green investors and they think they're master of the universe, they've opened into GameStop and the AMC. And of course, then you got what I think is even a Ponzi scheme is Bitcoin and other cryptocurrencies.

Dr. A. Gary Shilling:

They've moved in with gay abandoned and think they're really punishing the professional investor. So, you've had a huge amount of speculation out there and the risk is that the Fed even modest moves toward taking away some of the punch. And that's what William McChesney Martin, Fed's Chairman many decades ago he said, "The role of the Fed is to take away the punch bowl just when the party gets rolling." Well the Fed has been very reluctant to do that. They basically an arm of the treasury, they've been largely financing the Federal deficit.

Dr. A. Gary Shilling:

And you had the Greenspan put early on the idea that Wall Street could put bad positions, in other words, unload them on the Fed. And then the Bernanke put and the Yellen put and now the power put. So there's been a lot of expectation that the Fed will continue to bail things out and I think that's led to a tremendous amount of speculation. So there is possibility that as the Fed tightens, that things are going to reverse dramatically.

Dennis Tubbergen:

So Gary, give me your take on the health of the U.S. economy. Are we heading for recession here?

Dr. A. Gary Shilling:

The one interesting area and one that we're looking at and probably going to write up in our December newsletter, Insight, is the anticipatory borrowing an inventory building that's going on. There's been this mortal fear of not having enough stuff for Christmas. And so people have been buying ahead, retailers have been encouraging people to buy ahead. You saw we just had reports from Walmart and Target that their inventories have really leaped.

Dr. A. Gary Shilling:

And this is really reminiscent of what happened after World War I. Price and wage controls came off, the wholesale prices doubled overnight, everybody saw them going up forever. So there was tremendous excess borrowing, spending, orders, double and triple ordering, and then all the good showed up. And as a result, we had the sharpest recession on record in 1920, 21. I don't know we're headed quite that far, but it is reminiscent of that where you have this huge build up and anticipation.

Dr. A. Gary Shilling:

There isn't going to be enough supply, and the bottleneck problems with the supply chains have been the root of that. And as a result we could have a situation where we're going to see some setbacks as people realize that they bought ahead, they don't need all those. They bought their Christmas gifts early and the stores are going to be stuck with excess inventories that they're going to have to unload with discounts.

Dennis Tubbergen:

Yeah. We've got just a couple minutes left in this segment, but I would like your opinion on what's behind these quits? I mean, when you take a look at the number of people leaving their jobs in the months of August and again in September, I mean we have record numbers like over 4 million people quitting their jobs. What in your view is driving this new trend?

Dr. A. Gary Shilling:

Yeah. Well that's one of 12 changes with the pandemic that we went into detail in our November newsletter. It's the idea there has been a real change in people's attitude towards work. And people now want to work remotely, they don't like the commutes, and you find more people are quitting. You've had a huge surge about a million and a half people over 65 have retired early more so than the trends would indicate. And a lot of people are really in effect saying, "Wait a minute. I'm not sure I really want to work that much. Jobs are plentiful, I can quit, I can easily find a new job."

Dr. A. Gary Shilling:

And of course at the current situation the labor markets are tight, so there's more job offers than there are people available. So you are getting that situation at the moment. Now is this going to continue? I think it'll probably calm down, but at the moment there's people are really feeling their oats, if you will, and that they can quit because there's plenty of jobs out there. If the economy continues to grow, hey, that condition could continue. But is it if I suggest we get after Christmas and there is a slow down, because there's been a lot of pre-buying and so on, then you could find people or saying, "Wait a minute. There are not that many jobs out there I better hang onto the job I have."

Dennis Tubbergen:

Well my guest today is Dr. A. Gary Shilling. You can learn more about his work at the website, agaryshilling.com. And the phone number to call his office to get a complimentary copy of his terrific Insight newsletter is 888-346-7444. I'll continue my conversation with Dr. Shilling when RLA Radio returns. Stay with us.

Dennis Tubbergen:

Welcome back to RLA Radio. I'm your host, Dennis Tubbergen. I'm chatting today with my returning guest, Dr. A. Gary Shilling. Gary has been a long time Forbes columnist. He has also got some terrific opinion pieces now that you can find on Bloomberg. And you can learn more about his work at agaryshilling.com as well. He's got a terrific Insight newsletter, and he'll give our listeners a complimentary copy if you call 888-346-7444. So I'd encourage you to do that at as well.

Dennis Tubbergen:

Gary, given everything we talked about in the last segment, I want to get your take on debt levels. Because a lot of the research that I've been doing, a lot of the articles I've been reading seem to indicate that credit card debt is at all time high, student loan debt at all time highs, automobile debt, mortgage debt. A lot of this so-called economic growth seems to be perhaps debt-fueled consumption when you look at the numbers. So correct me if that's an incorrect perception or just give me your take on that.

Dr. A. Gary Shilling:

Well I think it has. You have to tear it apart. There's no question that you've had huge increases of financial leverage, if you want to put it that way. And what you're pointing out, credit cards, auto loans, and student loans of course have been way out of sight. Now the other side of the coin there is mortgage debt. And ever since the financial crisis and the subprime mortgage collapse in 2008, people have been working off their mortgage debt. Some of it was simply write-offs. Those mortgages had to be written off by the lenders, but a lot of it was people were much more concerned about having big loans on their houses.

Dr. A. Gary Shilling:

So the overall numbers don't look that extreme. But as you point out, some of these areas have shown a lot of increase in debt levels. And I think this is indicative of this general attitude of there's plenty of money around, why not borrow it? The Fed has been flooding the market with liquidity, and it hasn't really gone into purchases of goods and services it's gone into finance. I think it's what's pushed the stock market really starting in 2008 and even more so since the pandemic had early last year.

Dr. A. Gary Shilling:

And this money is floating around and lenders want to lend it, they want to make a return on the funds, and borrowers are only too happy to take down the loan. So you have built up a lot of this and it a risky envioronment. We're not up to the levels we were with subprime mortgages right before their collapse which started in 2007. But we're at levels that are certainly not very comfortable.

Dennis Tubbergen:

So Gary last time we talked which was about five months ago, you were, I'll just say you were bearish on stocks. You were not, as I recall, buying stocks. Has your position on that changed?

Dr. A. Gary Shilling:

Well, yeah. We've had a very heavy position in treasury bonds which have been doing well on balance. And so we are long stocks. We use portfolios we manage, we use exchange-traded funds. We're top down we're not stock pickers, we're looking at the more the aggregate level. And so we're using exchange-traded funds on the S&P 500, for example, and that in part is simply a hedge against our big bond position. But overall I still have a lot of liquidity. I think those stocks are in nose bleeding altitude. And boy, if there's any real hiccup here I hope I can beat that. Hope I beat the mob to the door.

Dennis Tubbergen:

Well let me ask you, as you break down the S&P 500 and look at the 11 sectors that make up the S&P 500, do you have any favorites?

Dr. A. Gary Shilling:

Well I think it's more a question of what you're least suspicious of. And I think that the areas that are the most vulnerable and the ones that I avoid the most right now are the growth stocks. Here's the rationale, their earnings, their big earnings are way, way out there many years out. And the way they're valued by a lot of people is discounting those future earnings. In other words saying, what are those future earnings worth today given current interest rates? Well the lower the interest rates the more of those future earnings are worth today.

Dr. A. Gary Shilling:

But if interest rates go up, then the discounting rate is higher and the future earnings are worth a lot less. I mean if for example, if you've got $10 of earnings 10 years out and your discount rate is 1%, it's worth 91 cents today or $9.10 cents today. But if the discount rate is 6%, it's only worth about five bucks. So I think that the growth stocks are vulnerable from that standpoint. And that's quite a part from what their earnings are doing and their performance in their areas. So that's one area I think is vulnerable.

Dr. A. Gary Shilling:

Some of the other areas that you have to be concerned about are some of the financial areas, the banks. They are in a lot of businesses but they are affected by the differences between the interest rates at which they borrow and those at which they lend. And short rates this is typical when the Fed tightens or rising faster than longer rates. Actually longer rates have come down and short rates have gone up and that squeezes their margins. These are what you call spread lenders, so I think they are at risk.

Dr. A. Gary Shilling:

So I would say that those are the kind of areas I would avoid. And the ones I think I would favor are things that are more routine, things that people are going to buy regardless, food for example, basic commodities. Those are the kinds of things that I think it's a cautious approach, but that's the way I would play it.

Dennis Tubbergen:

So Gary, given the Evergrande headlines that we've seen over the past couple months, do you have concerns about the bond market? And we should maybe clarify your bond position, because that would certainly seem to indicate that you're not expecting a big increase in interest rates.

Dr. A. Gary Shilling:

No, I'm not. I'm not. Now of course there many aspects of the bond market. The one that I've been a big fan of for 40 years, as you well know Dennis, are long-term treasury bonds. And there unless you think the world is coming in an end, you don't really have a credit risk, you don't worry about the Federal Government going out of business. Some people think it might but I think that's a very, very remote possibility. Now it's a very different situation when you're looking at highly leveraged area and you mentioned Evergrande, the Chinese property market extremely vulnerable and that makes a big difference. So you do have a difference within the markets.

Dr. A. Gary Shilling:

Treasuries they not only are basically risk-free, but they are safe havens. And the interesting aspect, and I've had this idea for some time I've been talking about it in our monthly newsletter, Insight, and I think it's beginning to play out, is the idea that people are saying, "The Fed is on the job and they're going to really prevent any inflation from getting out of hand." And so when you look at longer term interest rates treasury bonds, and to be a treasury bond it's got to be issued with over a 10-year maturity.

Dr. A. Gary Shilling:

10 years is a note and under 10 years is considered a treasury bill. But anyway, if you're looking at the longer term issues, they have been strengthening while the short-term interest rates have increased. And I think what that suggests is people are saying, "Wait a minute. The Fed is really going to nip any inflation in the bud here, even if it does develop." And so looking ahead and looking at that longer term picture, we're going to have less inflation, and so that is in effect.

Dr. A. Gary Shilling:

It's flattening what they call the yield curve. The interest rates, this is in the treasuries, starting with treasury bills, three month bills and working out to 30-year bonds. So I think you have a big difference there and the safe haven aspect of treasuries is always, always a winner when you have any kind of financial difficulties. So if you look back early last year with the COVID crisis, I mean the yield on 30-year treasuries virtually collapsed. It went down below 2%, and it's now only about 2% but it had started off about three or 4%. Now that's a huge, huge move in a treasury bond market. So it really did show where people go when they're worried, they go to treasuries and they go to the dollar.

Dennis Tubbergen:

So Gary, time for one last question here, you mentioned commodities just briefly. What's your view for commodities moving ahead? Both the industrial type commodities, as well as agricultural commodities?

Dr. A. Gary Shilling:

Again it's a whole spectrum. Agriculture commodities obviously are very dependent on the weather, much more so than the industrial commodities like copper, aluminum, zinc, tin, et cetera. And the weather is always a bet as to how things are going to shape up, and now of course it's a risk on next year. This year we had considerable droughts in the upper Midwest, and that really curtailed grain production.

Dr. A. Gary Shilling:

I was in North Dakota in August. It's the last state I've never visited and big state for pig keeping and I was up there visiting friends. But you could see the effects of the drought. But in terms of industrial metals, the one thing is that high prices always, always encourage excess production. And if you look at commodity prices adjusted for inflation, they have been in a steady decline from the mid 1800. Occasional spike with wars, oil embargos, and so on.

Dr. A. Gary Shilling:

But what it really says is that, yeah, there's only so much copper in the earth surface, but there's always substitutions, there's better use. Hey, I can remember when serious economists as a grown men and women thought that the telecommunications advances were going to be cut short because there wasn't enough copper in the earth surface to make all the wires you needed. Well guess what? Then they came up with fiber optics made out of silicone, which next to oxygen is the second most prominent element in the earth surface.

Dr. A. Gary Shilling:

So I think that commodities long-term, they aren't really an investment class in my view and long-term betting on commodities going up is just not worked. And it's much more better if you want to be in commodities to assume that they're going to continue the long-term decline.

Dennis Tubbergen:

Well my guest today is been Dr. A. Gary Shilling. His website is agaryshilling.com. If you'd like to get a complimentary copy of his Insight newsletter, just give his office a call at 888-346-7444. And Gary, always a pleasure to catch up with you and have you on the program. Love to have you back down the road. And thank you for joining us today.

Dr. A. Gary Shilling:

I look forward to it. Thank you, Dennis. Bye.

Dennis Tubbergen:

We will return after these words.