June 2023

Volume 7, Issue 6

THE "YOU MAY NOT KNOW REPORT"™

A PUBLICATION OF RETIREMENT LIFESTYLE ADVOCATES

Is The Federal Reserve About to Face the Music?

By Dennis Tubbergen

After a decade and a half of easy money policies ostensibly to stimulate the economy, the realities of these policies are now coming to light.

These policies, originally put forth as temporary, became permanent as the Federal Reserve went from creating $85 billion per month initially to trillions about ten years later to attempt to prop up a weak economy that was further devastated by economic shutdowns.

Now, over the past year plus, as the Fed has been increasing interest rates to battle inflation, the economy is once again weakening.

The reality is that an economy addicted to and dependent on artificial stimulus, like any other addict, feels good when the easy money is flowing, but quickly goes into withdrawal when the stimulus is withdrawn.

This addiction analogy is a good one in that an addict requires more of the substance to which he is addicted to get the same feeling. An alcoholic needs more booze to get the same feeling. A drug addict requires more of the drug to get the same feeling. And, an economy addicted to easy money requires more easy money to get the same economic good feeling.

Eventually though, the addict comes to the realization that he can't duplicate the feeling he once had no matter the quantity of the substance he is ingesting to get the feeling he craves.

The economy works exactly the same way, it takes more easy money to create each subsequent bubble and at a certain point, the economic bubble cannot be reproduced.

That may be where we now find ourselves.

After the last Fed meeting, Chairman Jerome Powell stated that future increases in interest rates would be dependent on the data. This[1] from "Reuters":

Federal Reserve Chair Jerome Powell said on Friday it is still unclear if U.S. interest rates will need to rise further, as central bank officials balance uncertainty about the impact of past hikes in borrowing costs and recent bank credit tightening with the fact that inflation is proving hard to control.

In carefully scripted remarks at a Fed research conference in which Powell was interviewed by a top U.S. central bank staffer, the Fed chief reiterated that the central bank would now make decisions "meeting by meeting," but also flagged that after a year of aggressive rate increases, officials "can afford to look at the data and the evolving outlook to make careful assessments."

"We face uncertainty about the lagged effects of our tightening so far, and about the extent of credit tightening from recent banking stresses," Powell said during a panel session at the conference in Washington. "So today, our guidance is limited to identifying the factors we'll be monitoring as we assess the extent to which additional policy firming may be appropriate to return inflation to 2%."

"The risks of doing too much or doing too little are becoming more balanced and our policy adjusted to reflect that," Powell said. Ahead of a June 13-14 policy meeting "we haven't made any decisions about the extent to which additional policy firming will be appropriate."

U.S. policymakers remain on the fence about their upcoming policy decision, and will receive important jobs and inflation data in coming weeks that could sway the debate within the central bank's rate-setting Federal Open Market Committee.

Powell said he felt that data so far "support the committee's view that bringing inflation down will take some time." He noted, for example, that some of the factors that may keep inflation elevated, such as the tight labor market, have yet to ease - particularly in the service industries where inflation is proving more persistent.

Policymakers are facing other constraints as well in offering clear guidance on the next meeting. Regardless of the data, the Fed is unlikely to raise interest rates if a down-to-the-wire political standoff over the U.S. federal debt ceiling remains unresolved. If an actual U.S. debt default is the result, the central bank may even be pushed towards emergency steps to ease the burden on the economy.

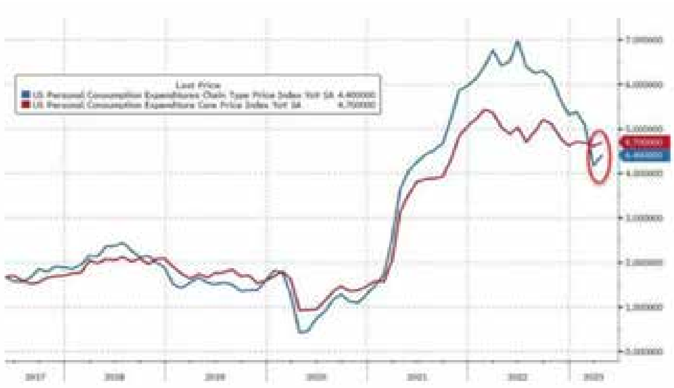
Powell's comments overall "were consistent with our takeaway from the May post-meeting press conference, which was that, while the (FOMC) wasn't sure whether further tightening would be necessary at some point, the committee's base case was a June pause," LH-Meyer senior economist Kevin Burgett wrote.

Reading between the lines, it seems that Mr. Powell and his cohorts at the Fed may be setting the stage for a policy pause and then a reversal.

In my view, this has been the highest probability outcome since the Fed announced a policy of tightening.

Interesting that this possible policy pause or reversal comes at a time when inflation is not even close to being contained. This was confirmed with the most recent PCE inflation report. This[2] from "Zero Hedge":

One of The Fed's favorite inflation indicators - Core ***PCE Deflator - disappointed the doves, printing hotter than expected*** *(headline and core both +0.4% MoM vs +0.3% MoM exp), pushing the YoY inflation signals higher...*

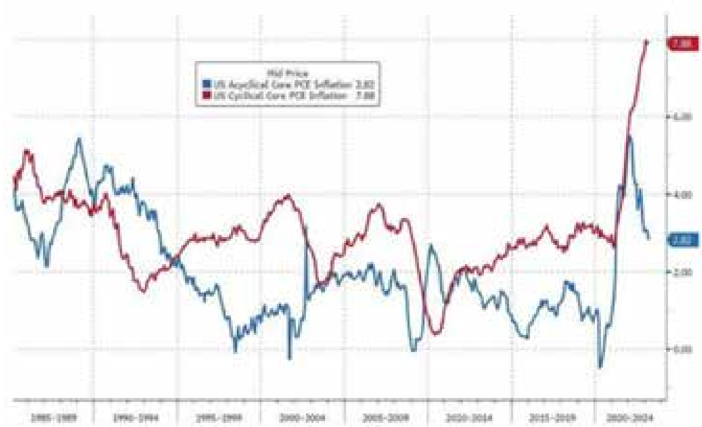


Source: Bloomberg

Even more focused, is the Fed's view on Services inflation ex-Shelter, and the PCE-equivalent shows that is very much stuck at high levels...

Source: Bloomberg

However, while acyclical core inflation continued to slide, cyclical core inflation dipped very modestly but remains extremely high. Cyclical core PCE inflation, which tracks inflationary pressures that are linked to the current economic cycle, is at the highest on record going back to 1985.



Source: Bloomberg

Core inflation is at the highest level since 1985, yet the Fed may be taking a pause or reversing policy. Does that make sense if the goal is to get inflation under control?

Of course not.

Will the Fed continue with interest rate increases as a result of this new data?

Maybe. We'll have to wait and see.

No matter what the Fed does near-term, the long-term outlook remains clear with only two possible outcomes.

The Fed, as I have noted previously, is between the proverbial rock and a hard place. If the central bank continues to increase interest rates, the already weak economy gets weaker.

On the other hand, if the Fed reverses policy and begins to pursue easy money policies once again, the inflation monster gets bigger and scarier.

Two options.

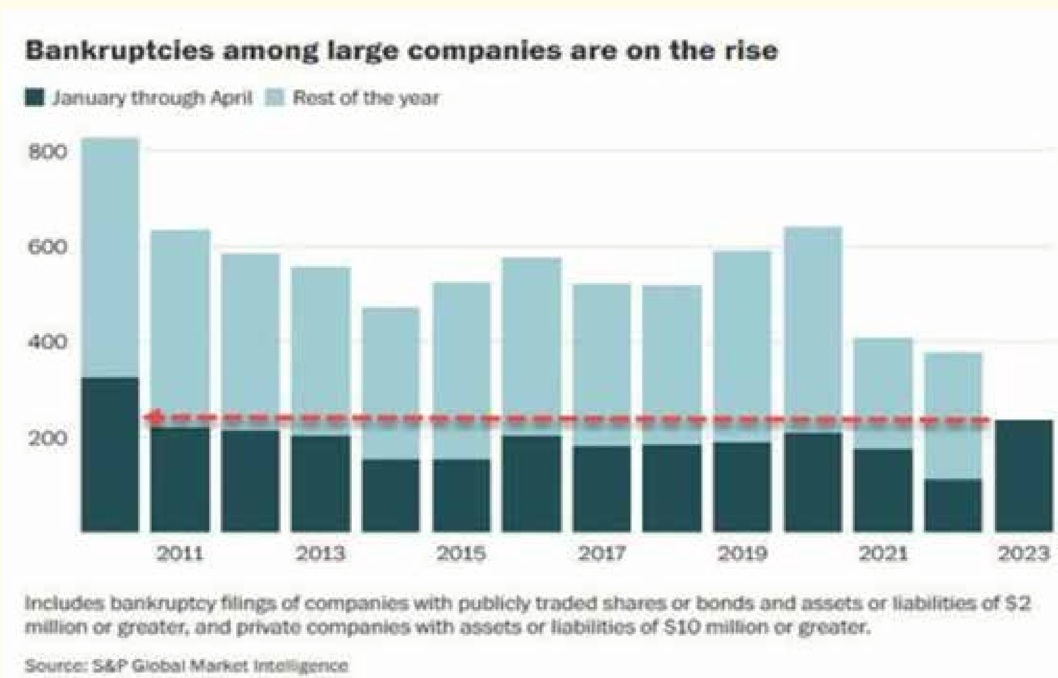
Both bad.

Perhaps the Fed will decide to sacrifice the purchasing power of the US Dollar to attempt to prop up a sick economy?

There are many reasons for the Fed to take such action.

U.S. corporations are filing for bankruptcy at the fastest pace since 2010. This from "Zero Hedge":

> *One would not know it from looking at the S&P which just hit a 2023 high, but there is a bit of a bankruptcy crisis sweeping the US where companies are filing for bankruptcy at the fastest pace in 13 years, in a clear sign of a tightening credit squeeze as interest rates rise and financial markets have locked out all but the strongest borrowers.*
>
> *The increase is most visible among large companies, where there were 236 bankruptcy filings in the first four months of this year, more than double 2022 levels, and the fastest YTD pace since 2010 according to S&P Global Market Intelligence.* (See chart below.)
>
> *Several large recognizable companies with hundreds or thousands of workers have filed for bankruptcy protection in recent weeks, including Bed Bath & Beyond and Vice Media, although their financial troubles predated the recent economic turmoil.*



The bankruptcies did not slow down in May, when just the past week saw eight companies with more than $500 million in liabilities file for Chapter 11 bankruptcy, including five in a single 24-hour stretch last week, making this the busiest week for chapter 11 filings so far this year. In 2022 the monthly average was just over three filings.

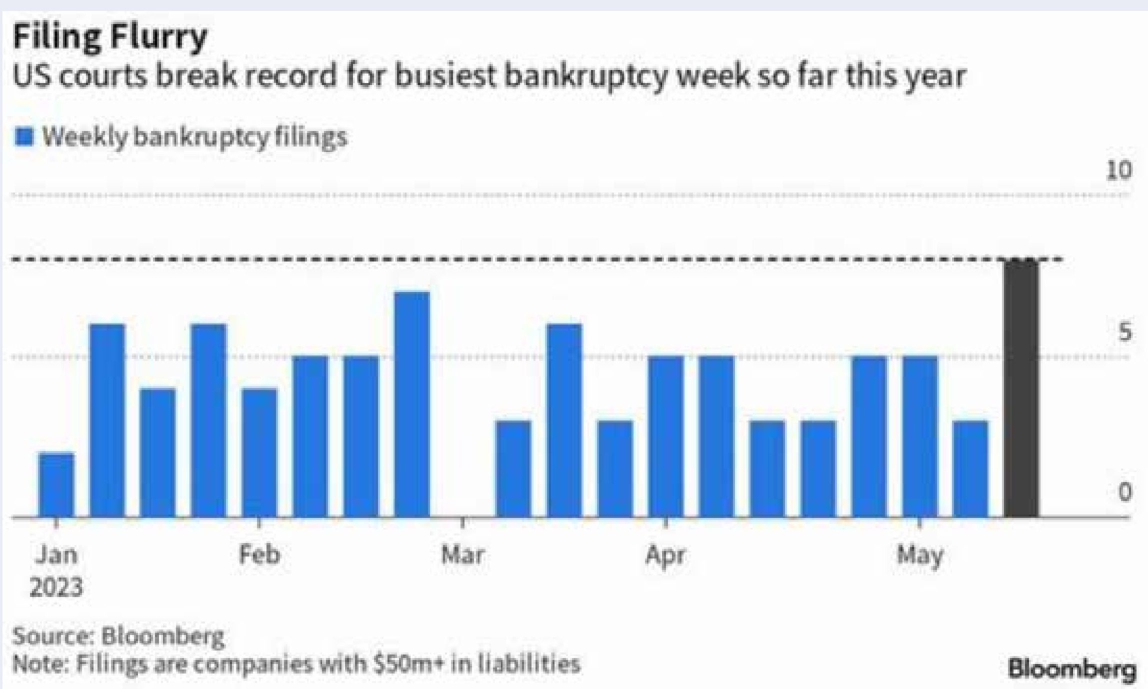
Last week's eight large filings, those with at least $50 million of liabilities, included those of now defunct woke "media empire" Vice Media, Envision Healthcare and Monitronics International. Prior to last week, the busiest seven-day stretch this year belonged to a week in late February that saw firms including Covid-19 testmaker Lucira Health, generic drugmaker Akorn and former SPAC Starry Group kick off insolvency proceedings. (See chart below.)

In total, twenty-seven large debtors have filed for bankruptcy so far in 2023 compared to 40 for all of 2022, according to figures compiled by bankruptcydata.com.

Among all types of companies, large and small, the increase in bankruptcies is somewhat more muted, with filings remaining below pre-pandemic levels and historic norms, according to Mark Zandi, chief economist at Moody's Analytics. However filings, especially among large, unprofitable companies, are ramping at a frenzied pace as interest rates rise, pandemic-era government support dries up and sales growth slows amid a cooling economy.

There were about 16,200 bankruptcy filings among all types of companies in U.S. District Courts in the first quarter — up from 12,200 a year earlier, but still well below the 21,000-or-more-a-quarter in the pre-pandemic period, data from Moody's Analytics shows. Even those pre-pandemic numbers were relatively low in historic terms, in part because low interest rates made it easy for companies to borrow.

Now, ***S&P Global forecasts that the 12-month trailing default rate for speculative-grade securities will jump from the***



current 2.5% to 4.5% by early 2024.

"The era of low interest rates and pandemic-related government support programs helped keep companies afloat that may have otherwise had few other options," S&P analysts said of their large-company data. "Now that interest rates are back to pre-Great Recession levels and pandemic support programs are largely over, we're seeing a fresh uptick in a possible sign that companies are running out of time."

Yields on junk bonds have more than doubled from less than 4% in mid-2021, as measured by the Bloomberg US High Yield Index. The Fed has warned that lenders could further contract the supply of credit to businesses after recent turmoil in the banking sector.

As we've discussed previously, consumers are increasingly relying on credit cards to meet living expenses. US credit card debt now stands at a record-high $1 trillion. This[4] from "Market Watch":

The first-quarter dip never happened. Some observers say that's a problem.

Credit-card balances hit $986 billion in the fourth quarter last year and remained largely unchanged in the first quarter of this year, the Federal Reserve Bank of New York said in its most recent quarterly report on household debt. It looks increasingly likely that credit-card debt is on track to hit the $1 trillion mark this year, and experts say that this number could be an indicator of a looming economic downturn.

This has raised eyebrows among some observers, because people typically pay off their debts from the holiday season in the first quarter of the year. That did not happen this year. This was the first time credit-card debt did not make its customary dip between the fourth and first quarters since the end of 2000 and the beginning of 2001, New York Fed researchers said. That was a recession marked by the end of the dotcom bubble.

"Although inflation is slowing and wages are starting to rise, inflation is still squeezing people's budgets," said Mary Eschelbach Hansen, a professor of economics at the American University in Washington, D.C., and author of "Bankrupt in America: A History of Debtors, Their Creditors, and the Law in the Twentieth Century."

But she said she doubts that the biggest problem is people splurging on gifts over the holidays or postpandemic "revenge travel" that they are now unable to pay off. "It seems likely that part of the fourth-quarter run-up in balances went towards groceries and other everyday bills rather than holiday expenditures, and folks are having a harder time paying that back," she said.

Others shared her concerns. "I see several worrying trends here," said Ted Rossman, senior industry analyst at Bankrate.com. "Credit-card debt is something that's easy to get into and hard to get out of. More people carrying balances at higher rates for longer periods of time is definitely a bad combination. We're seeing more people financing day-to-day essentials on credit cards."

Poll: Cost of Living Increases Nearly 50% In Last Ten Years

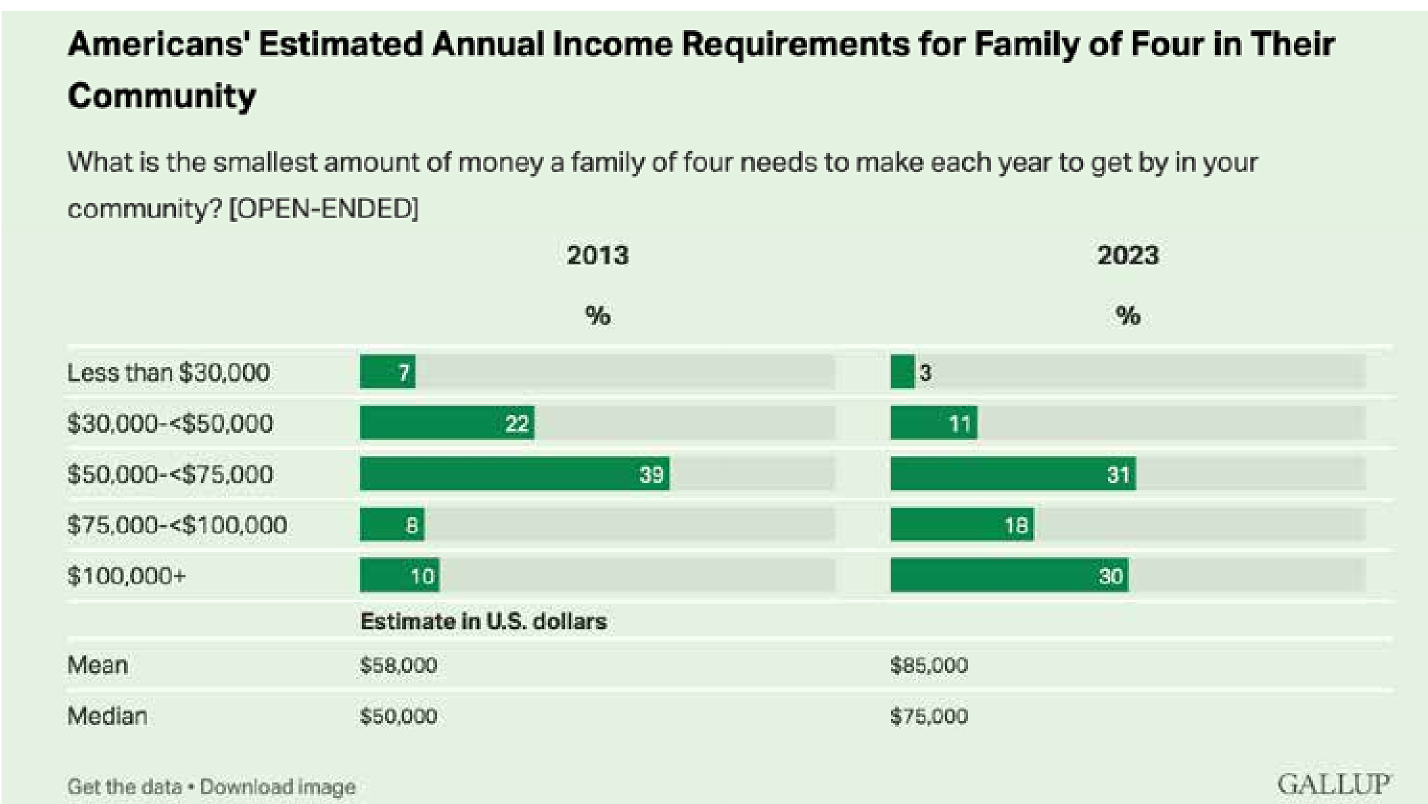
According to a Gallup poll of Americans, the average annual income that an American family needs to 'get by' has increased nearly 50% since 2013. This[5] from Gallup:

Americans, on average, estimate that a family of four needs a minimum income of $85,000 annually to "get by" in their community, marking a considerable increase from a decade ago. The past decade has witnessed not only an increase in the average income required but also a notable shift in the upper range of income expectations.

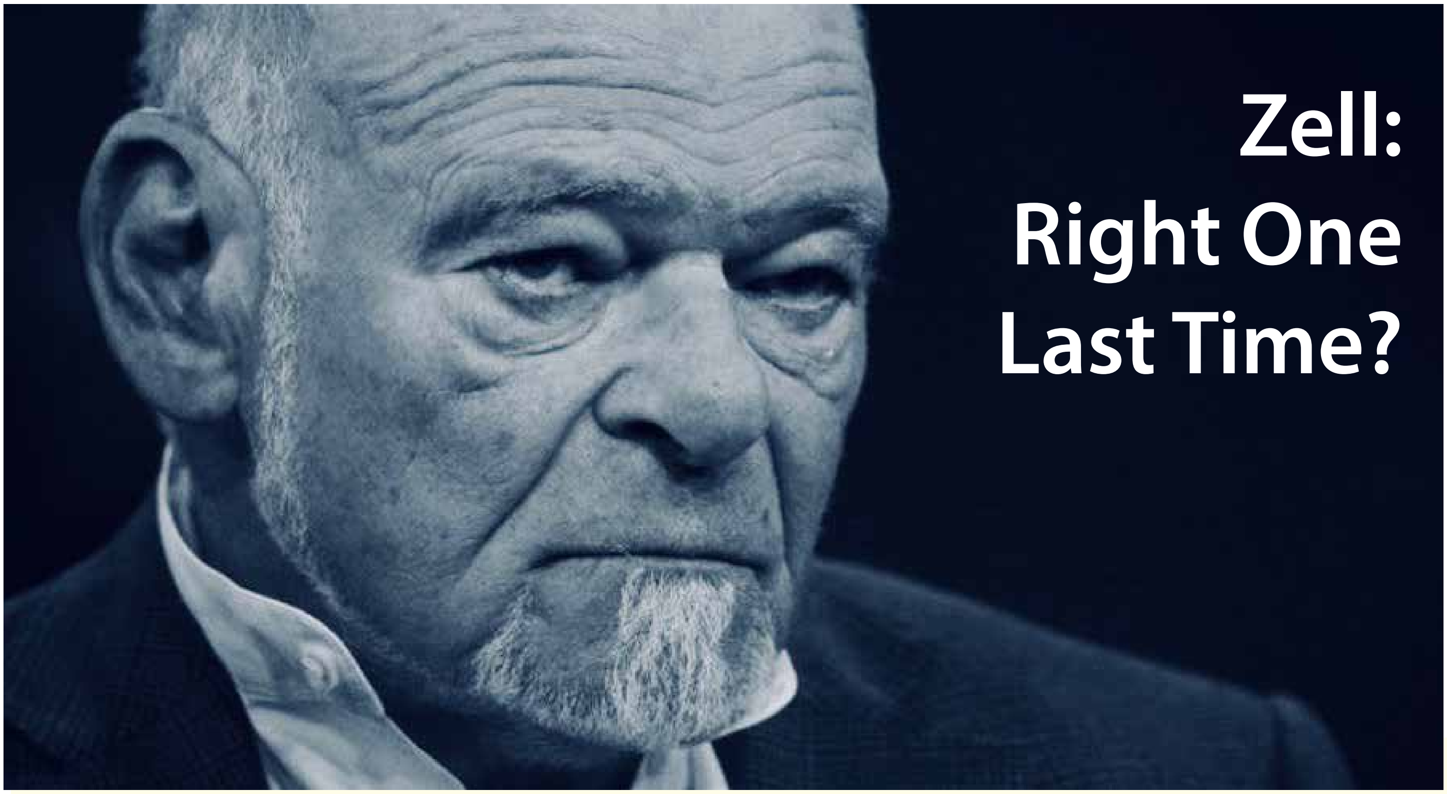
During that time, the proportion of Americans who believe that a family needs more than $100,000 to get by has tripled to 30%, while 18% now estimate it to be between $75,000 and $99,999, and 31% think it is $50,000 to $74,999. Half as many Americans now as in 2013 believe a family of four can get by on less than $50,000 annually. This includes 3% who estimate a figure lower than $30,000, and 11% who cite a figure between $30,000 and $49,999.

The latest average of $85,000, from an April 3-25 Gallup poll, is notably higher than the federal poverty line for a family of four, which is currently $30,000.

In 2013, the average estimate was $58,000, and the federal poverty line for a family of four was $23,550. Accounting for inflation and the subsequent change in purchasing power, Americans' 2013 estimate translates to $75,668 in 2023 dollars. Their 2023 estimate therefore reflects an increase of about $9,000 in perceived family needs beyond what inflation alone would account for.



Zell: Right One Last Time?



Real estate investing legend Sam Zell recently passed on. Right up to the time of his death, Mr. Zell was doing interviews and making his economic and investing forecasts. As John Rubino recently wrote[6], Mr. Zell's forecasting track record was uncannily accurate:

> *I'm old enough to have followed Sam Zell during the second half of his storied real estate career. And in that time he's been right in a big way on the major financial turning points. At the bubble peaks of 1999 and 2007, for instance, he sold most of his commercial real estate and loaded up on cash. Then he swooped back in at the subsequent bottoms and bought up distressed assets for pennies on the dollar. That's how you become a legend.*
>
> *Sam died this week. But despite his apparently failing health, he was doing interviews right up to the end in which he once again predicted a crash and claimed to be selling off his properties.*
>
> *There's one from three months ago in which he says, "I've never seen the Fed get lucky"… "Prepare for higher costs… " and "The real estate industry has to deal with all kinds of things related to an unrealistically low cost of capital."*
>
> *In an interview from two months ago: "We're in this mess because the Fed didn't do their job." … "This is the Weimar Republic." … "The correction is going to take a lot longer than people expect."*
>
> *Assuming Sam Zell was right again, another 2000 or 2008 (or something worse) is headed this way. Real estate and stocks will tank, and bonds (the Weimar reference) might follow. The smartest investors will stockpile cash and return to the market when there's blood in the streets.*

Deflation Upon Us?

Inflation, technically defined, is an increase in the money supply.

Deflation is the polar opposite of inflation, a contraction of the money supply.

Ever since the time of the Great Financial crisis, world central bankers have been engaging in quantitative easing programs (a.k.a. currency creation programs) to stave off deflation,

Since all currencies in the world today are fiat currencies and are loaned into existence, additional currency could be created by central bankers by reducing interest rates and encouraging borrowing. The more consumers borrowed and the greater the velocity of money, the more currency that was ultimately created.

After the financial crisis, central banks resorted to creating currency out of thin air, a process that was dubbed quantitative easing. This currency creation accelerated until the Fed was forced to reverse course and increase interest rates and slow the pace of currency creation to attempt to get inflation under control.

Now, as a result of that reversal in policy, the money supply is contracting at a pace not seen in the last 28 years!

This[6] from Mises:

> *Money supply growth fell again in March, plummeting further into negative territory after turning negative in November 2022 for the first time in twenty-eight years. March's drop continues a steep downward trend from the unprecedented highs experienced during much of the past two years.*
>
> *Since April 2021, money supply growth has slowed quickly, and since November, we've been seeing the money supply repeatedly contract for five months in a row. The last time the year-over-year (YOY) change in the money*

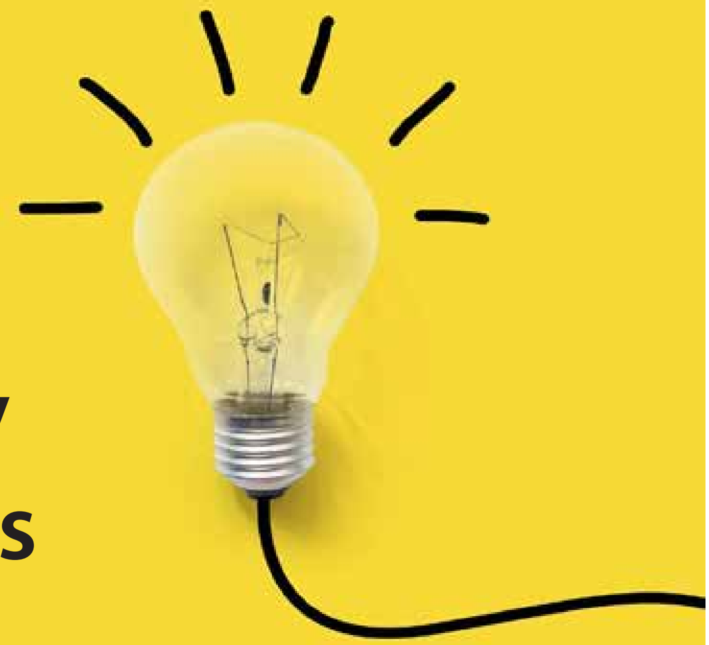
supply slipped into negative territory was in November 1994. At that time, negative growth continued for fifteen months, finally turning positive again in January 1996.

During March 2023, the downturn accelerated as YOY growth in the money supply was at –9.9 percent. That's down from February's rate of –6.6 percent, and far below March's 2022's rate of 7.1 percent. With negative growth now falling to near –10 percent, money-supply contraction is the largest we've seen since the Great Depression. At no other point for at least sixty years *has the money supply fallen by more than 6 percent (YoY) in any month.*

As we've discussed in this publication previously, private sector debt levels when measured as a percentage of economic output are greater now than at the onset of The Great Depression. For that reason, this massive money supply contraction is not surprising.

It also illustrates the fact that the Fed cannot get interest rates back to a more 'normal' level without causing a massive recession/depression.

June 2023 Special Report



Current Economy Income Strategies

This month only, we are making available a free report titled, "Current Economy Income Strategies".

This month's report will outline current economy income strategies to consider in light of the current economic environment. Inflationary policies causing consumer price inflation with the threat of severe deflation from excessive debt levels make income planning particularly precarious presently.

The June 2023 special report outlines income strategies that incorporate inflation and deflation hedge strategies. If you are retired or planning for retirement, the information in this report may be especially useful.

To request this report for you or someone you know who might appreciate it, use one or all of the postage-paid reply cards included with this month's newsletter to request this month's special report.

This report is available only during the month of June.

Time Deposit Rates

At the time of publication, these rates were valid:

1-Year	4.30%
2-Year	4.50%
5-Year	4.80%

Call the office for details at

1-866-921-3613

Resources to Help You Stay Informed

All these resources are available at the Retirement Lifestyle Advocates website: www.RetirementLifestyleAdvocates.com.

The "Portfolio Watch" weekly newsletter. Each week, I give you an update as to where we are economically speaking and in the financial markets and where we are going based on my analysis.

The weekly "Headline Roundup" webinar. Replays are available on the website. "Headline Roundup" happens every Monday live at Noon Eastern Time. To get an invite to the live event, give the office a call at **1-866-921-3613**.

The weekly "RLA Radio" show and podcast.

We also have the RLA app available. All these resources are also available on the app.

You can download the YOURRLA app for free by visiting the app store (either Google or Apple) and searching under YOURRLA.

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

Sources

1. https://www.reuters.com/markets/us/feds-powell-spotlight-pressure-grows-fish-or-cut-bait-rates-2023-05-19/
2. https://www.zerohedge.com/personal-finance/feds-favorite-inflation-indicator-re-accelerated-april
3. https://www.zerohedge.com/markets/us-corporations-are-filing-bankruptcy-fastest-pace-2010
4. https://www.marketwatch.com/story/americans-are-not-paying-off-their-credit-card-debt-we-should-be-concerned-6db9ffe6
5. https://news.gallup.com/poll/506405/americans-say-families-need-000.aspx
6. https://rubino.substack.com/p/real-estate-icon-sam-zell-right-one