



MEDALLION
WEALTH MANAGEMENT

October 2021 Market Commentary

Free Ride

*The mountain is high, the valley is low
And you're confused 'bout which way to go
So I flew in to give you a hand
And lead you into, the promised land*

https://www.youtube.com/watch?v=JAFyvePcR_o

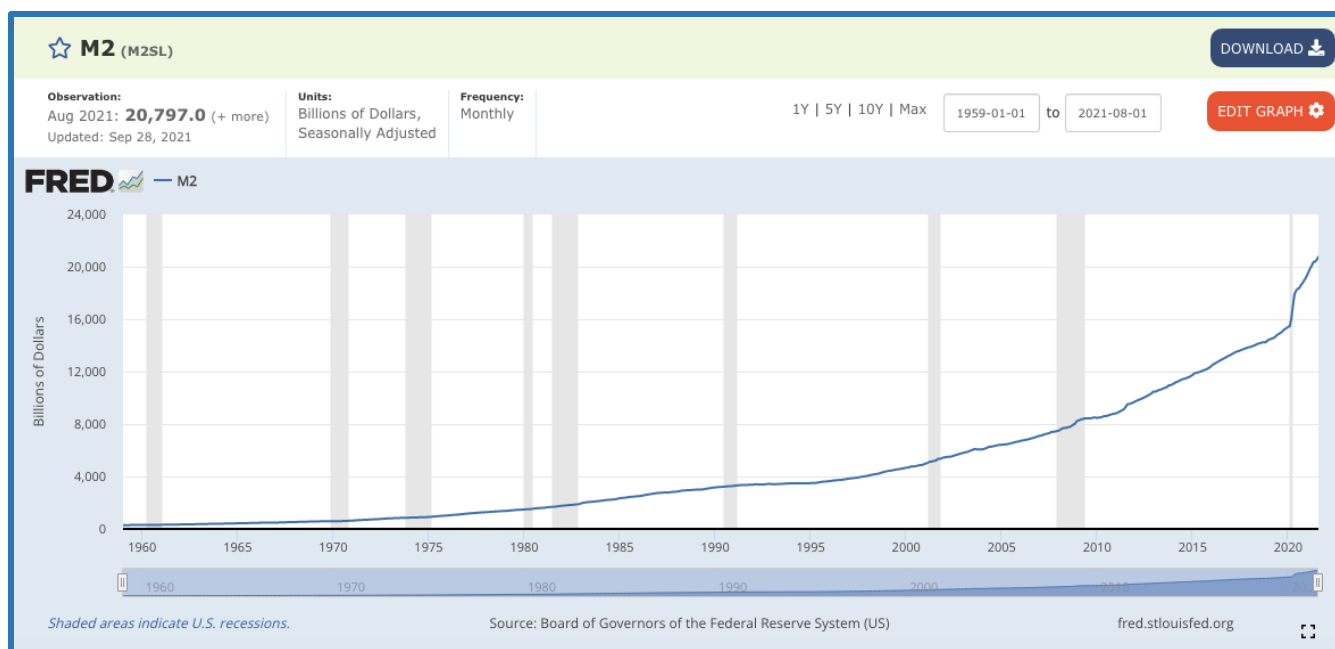
Free Ride by Edgar Winter Group

“Free Ride” economics (also known as Modern Monetary Theory), the new economic school of thought, is starting to take hold, and I must say it certainly is appealing. Who doesn't like unlimited supplies of free money, and debt that never has to be paid off. That's like saying you don't like rainbows, puppies, and unlimited supplies of calorie free ice cream sundaes. The theory argues that countries that issue their own currencies can never run out of money the way people or businesses can. It has long been a fringe economic theory, but is getting more traction and support from democratic progressives like Rep. Alexandria Ocasio-Cortez, and Nancy Pelosi.

Even our President has gotten on the “Free Ride” train while trying to sell his whopping \$3.5 trillion plus social infrastructure plan. At a recent press conference President Biden said, *“Every time I hear this is going to cost A, B, C, or D—the truth is, based on the commitment that I made, it's going to cost nothing, because we're going to raise the revenue.”*

In other words, if you pay for something that makes it free. It doesn't matter where that money comes from, whether its higher taxes or unlimited debt issuance. It's free. Hey honey, look at all the stuff I got at the mall. Don't worry, it was free, all I had to do was give them my credit card!

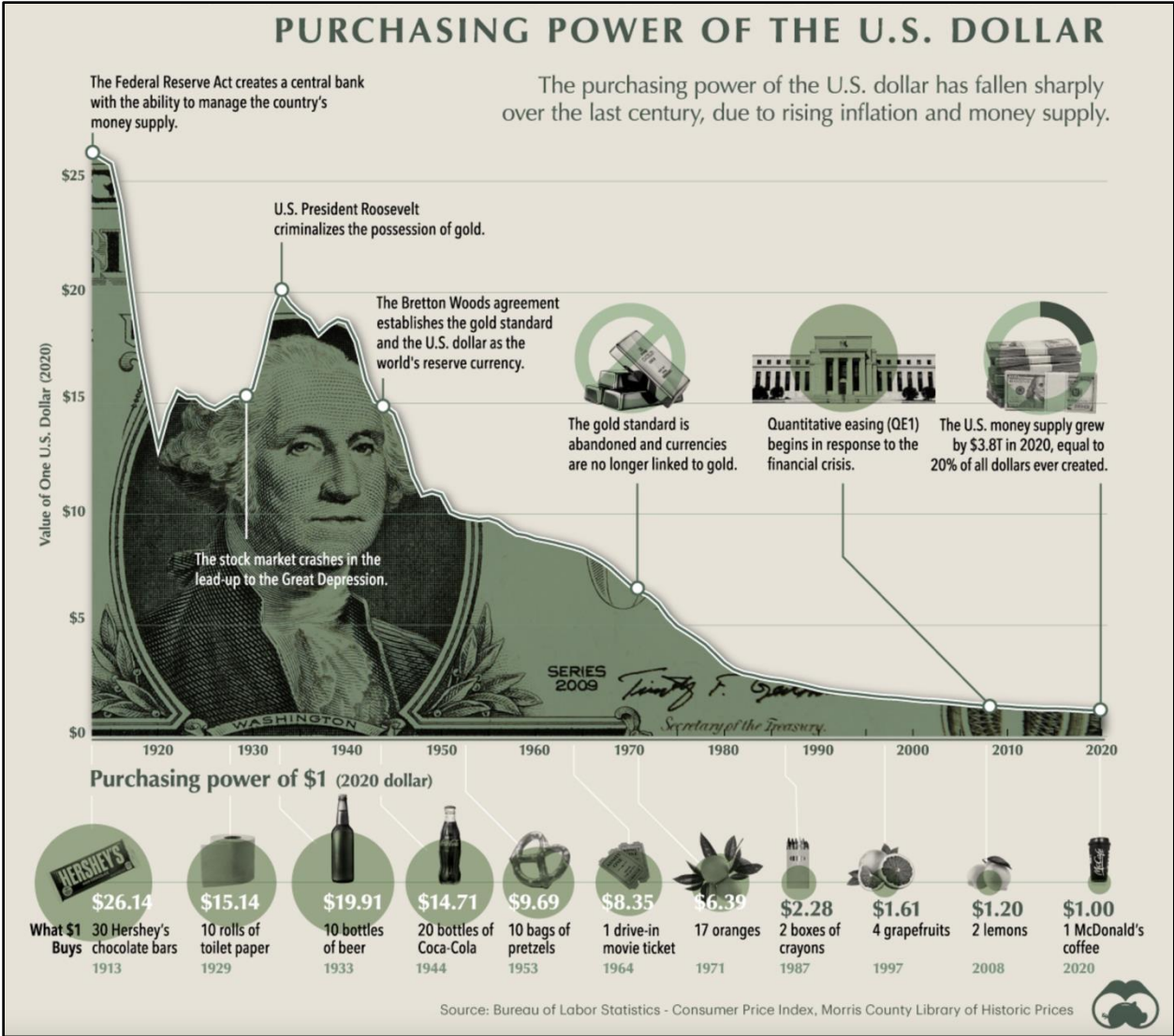
And who can blame them from starting to think this way, our Treasury and Federal Reserve have shown that they can issue debt and print currency to purchase that debt at an unprecedented rate. The most commonly referenced gauge of a country's money supply is M2, which measures cash, short-term deposits, and money market funds. Recently our M2 reached \$20.5 trillion, which is up from \$15.4 trillion in January 2020, **meaning that 25% of all US dollars in existence has been created in the last 18 months.**



Just because money is “free” doesn’t necessarily mean that it doesn’t come at a cost. You see, generally when you have excessive amounts of money circulating through an economy it needs to find a home. Prices for assets appreciate as investors use excess cash to purchase stocks, bonds, etc. The wealth gap grows as those who own assets see them appreciate, and those who don’t own assets see their cost-of-living appreciate. In other words, massive stimulus leads to inflation.

Inflation is good if you are a borrower, since you repay your debt with deflated dollars. And since governments are by far the largest debtors, they are perfectly happy with inflation. In fact, the stated goal of the Federal Reserve is to devalue the dollar by 2% per year. Currently they are happy with that number running much higher than 2%.

As the chart below shows our U.S. dollar has been in a steady decline ever since we’ve gone off the gold standard.

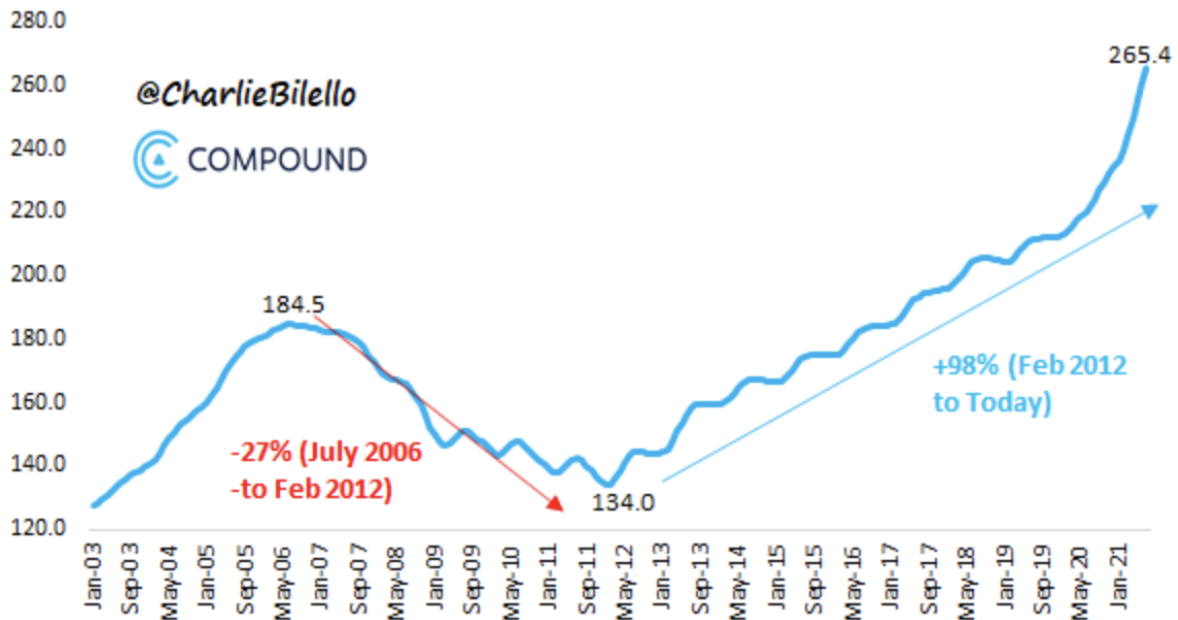


For us average citizens a little inflation isn't horrible, as long as our income keeps up with inflation, and our standard of living doesn't decline. The problem arises when inflation accelerates but isn't matched by an equally accelerating amount of economic growth. This is what appears to be happening now.

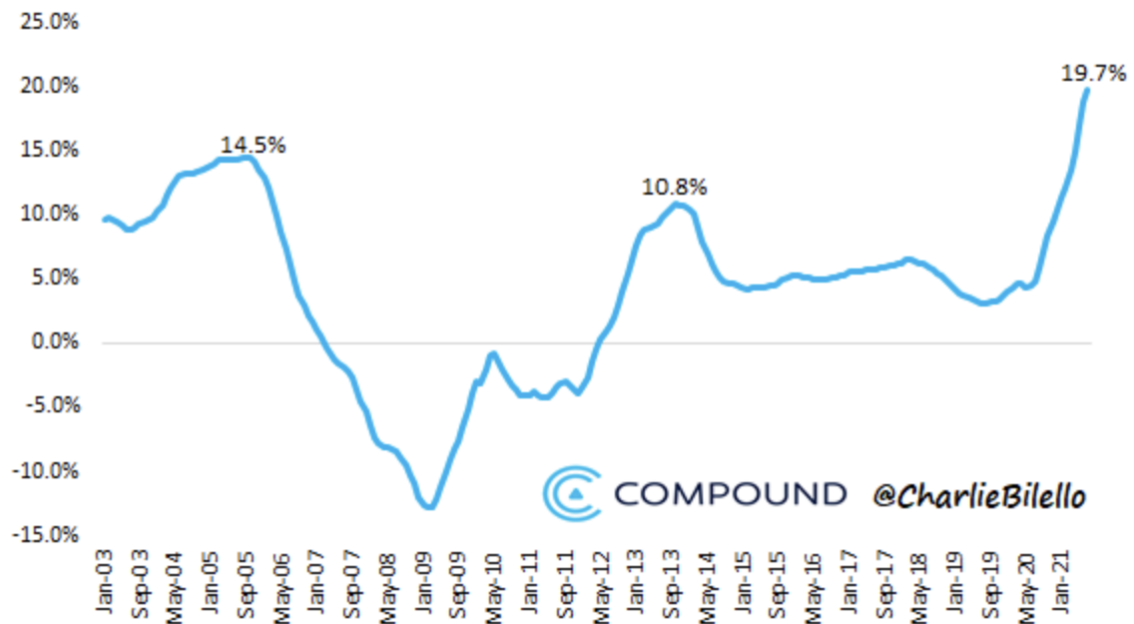
Stock prices have appreciated by about 16% annually over the last 10 years, and home prices have appreciated 7% annually, while wages have only increased by 2.5% annually.

Chairman Powell believes that our current inflationary spike is transitory, and that it will soon dissipate. But the markets are starting to worry that his definition of "transitory" is looking more and more permanent, and that we are entering a period of stagflation. Stagflation is higher levels of inflation (not necessarily higher interest rates) and slow economic growth.

S&P Case-Shiller US National Home Price Index (Jan 2003 - July 2021)



S&P Case-Shiller US National Home Price Index (YoY % Change)



Third Quarter Review –

After a tough September with stocks falling 4.66% on the S&P 500, they were still able to eek out a small gain in the third quarter and are now up by 15.91% year-to-date. As interest rates have risen slightly, bonds have struggled mightily, and most fixed income benchmarks are negative on the year. The persistence of inflation and supply-chain challenges, lukewarm economic data and the potential contagion from the collapsing Chinese real estate developer Evergrande have put a damper on growth prospects entering the fourth quarter.

We've been on a "Free Ride" ever since the Great Financial Crisis, zero interest rates, quantitative easing, and ballooning debt levels. Now with our current pandemic we have doubled down on the Modern Monetary Theory of free money. We are living in the greatest economic experiment of all time. Is there really a "Free Ride" or will there be a very big bill to pay?

I don't pretend to know the answers, on one hand I'm hoping it all works out swell, but on the other I'm invested conservatively in quality stocks, short duration bonds, and an ample amount of cash. It's been a hell of a ride, but the only successful long-term investors have been the ones who survive.

***All over the country, I'm seeing the same
Nobody's winning, at this type of game
We gotta do better, it's time to begin
You know all the answers
Must come from within***

Be careful out there,

Chris Wiles, CFA



Where Trust is Earned

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