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William Rutherford

OP-ED: What to do with your money amid deficits, inflation and economic growth

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With the U.S. economy growing at 6.4 percent and current inflation estimated at 2.3 percent, investors are left to wonder what is happening.

Are we too late to invest? Are we too early? Is this an inflationary economy? Is it a Goldilocks economy (not too hot, not too cold)? Where should we invest? In precious metals? Bitcoin? What about bonds, stocks or commodities? Where does the COVID-19 virus fit into this scenario? These are all pertinent questions, for which there are no simple answers.

Similar to the mess that ensued from the financial crisis of 2008-09, the ramifications of the virus are omnipresent. First, inflation. Currently, the Federal Reserve estimates an inflation rate of 4.2 percent for calendar year 2021. This is no easy rate to peg. There is the rate at the store, or the gas pump, or the stated rate by the Fed, or the PCE inflator that the Fed prefers, but there is no one certain rate. Thus the published rate has many imperfections.

What is inflation and why does it matter? Inflation is the decline of purchasing power of a given currency over time. It matters because businesses and consumers make purchasing decisions based on the perceived rate of inflation: The higher the current rate of inflation, the more likely a business or consumer is to buy, thus fueling more inflation.

Also, the Federal Reserve makes interest rate decisions based on the rate of inflation. If inflation is higher, the more likely the Fed is to raise interest rates. The Fed does this because it does not want inflation to "run away." Conversely, if inflation is too low, the Fed might lower interest rates to avoid deflation. The Fed prefers inflation to deflation, because it believes that an economy is healthier if inflation runs about 2 percent.

Business is interested in the rate of inflation, not only for purchasing and investment decisions, but because borrowers believe the rate of inflation influences the Federal Reserve's decision on interest rates, which will impact borrowing costs, the rate of return on investment, and therefore the value of an investment over time. If rates are low, investors are willing to pay more for an item. If rates are high, purchasers are willing to pay less for an item. In other words, why pay more for something if it is likely to decline in value?

The yield on the 10-year U.S. Treasury note is thought to be a proxy on the value of money, and a proxy on interest rates generally; that is because that Treasury is thought to be a risk-free investment backed

by the full faith and credit of the United States of America. However, that faith wavers in inflationary times; thus the concerns about bond rates and inflation rates.

Currently, the rate of inflation is influenced by the retreat of the virus, resulting in the so-called post-COVID reopening trade in the economy and stock market. The economy appears quite strong, as consumers resume spending after quarantining during the virus shutdown. This reopening and surge in spending can be thought to be inflationary. However, looking under the hood shows other information.

For instance, auto sales have been vibrant, but the sale of used cars appears torpid. A shortage of chips has pushed up auto manufacturing costs, but the decrease in miles driven has caused auto sellers to lower prices in order to move inventory. This results in a murky rate of inflation for this sector. The picture also is mixed for other sectors, such as housing. Geography is a major factor, as demand increases in the southern and western states and weakens in many urban areas.

Even so, it is pretty clear that prices are going up. Just this week, the U.S. Postal Service announced that the price of a postage stamp is rising from 55 cents to 58 cents, which will result in increased mailing costs for individuals and businesses.

So, what should an investor do in an inflationary environment? Historically the answer has been to buy THINGS, and go into debt. Buy things to attain ownership, which may cost more tomorrow, and go into debt to repay money borrowed with a less valuable currency.

When I worked in Germany, a colleague told me of an incident during a period of runaway inflation in Germany. I call it how to turn a cow into an egg. Her family owned a cow, which they sold. They went to town to shop. Her mother wanted a pair of shoes, but could not make up her mind which pair to buy, so they left with plans to return the following day. By then, they could not afford the shoes because the price had gone up. Her mother then focused on a dress, but could not find one in her size. Again they left without a purchase. The next day they returned to find they could afford neither shoes nor a dress. They could afford only an egg, so they bought it with the proceeds from the sale of the cow. Thus their cow became an egg. That is what inflation can do. It was an extreme case, but German inflation was extreme.

So, if you are going to buy something, what should you buy? Gold is usually seen as an inflation hedge, but it is a store of value, and not necessarily an investment. As a commodity, gold is subject to price variation and manipulation; there are no earnings behind gold to shore up value. Indeed it may cost money because there is a storage cost. Similar things can be said of other precious metals such as silver or platinum or of blockchains like Bitcoin.

How about safe and secure bonds? U.S. Treasurys are thought to be the safest investment in the world, backed by the full faith and credit of the U.S. Treasury, which incidentally gets weaker every year as the deficit balloons.

Real estate? Perhaps, but there are maintenance costs and holding costs, not to mention supervisory efforts. Of course there are other asset classes, including collectibles such as art or postage stamps. Each has its own benefits, but also its own costs. Some are not so fungible, meaning they cannot be exchanged or turned into cash easily. Liquidity is something that investors like.

I continue to believe that U.S. stocks are the best asset class for the major part of one's savings. Even with its shortcomings, in an inflationary environment, stock ownership in a diversified portfolio of

growing companies traded on the major money center exchanges provides the best opportunity for keeping pace with rising costs and ease of fungibility/liquidity.

William Rutherford is the founder and portfolio manager of Portland-based Rutherford Investment Management. Contact him at 888-755-6546 or wrutherford@rutherfordinvestment.com. Information herein is from sources believed to be reliable, but accuracy and completeness cannot be guaranteed. Investment involves risk and may result in losses.

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