Doug Kass- Is It All A Ponzi?

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On August 10, 2021, Doug Kass shared an article from his Real Money Pro subscription service on Twitter. We think it is well worth the read to better understand the insidious effect monetary and fiscal policy are having on this nation.

Doug Kass:

Expanding on this morning's Bloomberg interview Webster defines a Ponzi scheme as "*an investment swindle in which some early investors are paid off with money put up by later ones in order to encourage more and bigger risks.*" As I suggested in this morning's Bloomberg Surveillance interview, our economic policy is beginning to look that way.

Currently massive government spending - to benefit Americans - is being financed by taking on enormous amounts of debt with which future citizens will be burdened. That debt emanates from unprecedented budget deficits resulting from spending well in excess of tax receipts. Public borrowing has vastly increased private savings at the expense of a soaring national debt.

As a result, despite the pandemic, savings are at an all-time high. Such borrowings would normally lead to higher interest rates to finance them but not this time because the Federal Reserve has largely neutralized them by purchasing $120 billion of Treasury and mortgage-backed securities a month- vastly increasing the national debt. These purchases have kept nominal rates low making financing the deficit less of a burden. Clearly much of the spending has been necessitated by the pandemic but prior tax cuts and future spending plans are responsible for a very meaningful part.

As a result, we live in a world where economic health is to a larger and larger degree, an artificially created illusion and both the stock and bond markets have soared as a result. The question is whether this is sustainable and what the consequences are if it is not...

It is generally recognized that markets have moved steadily higher because of the support of the Federal Reserve with the markets only experiencing very short periods of decline when it looked like that support might be withdrawn. The belief in a Fed "put" protecting the downside has led to a massive growth in riskier investments like SPACs, IPOs, junk bonds, cryptocurrencies, etc.

The Fed's policy has resulted in a massive increase in income inequality. Those seeking to invest the savings occasioned by the federal policies are faced with the option of traditional fixed income securities which yield almost nothing or investing in an admittedly expensive stock market or in other tangible assets. Many/most have chosen asset purchases.

Those already wealthy have enjoyed enormous gains as stocks and homes have risen dramatically while those with modest savings have watched returns from fixed income assets virtually vanish. First time home buyers have been priced out of the market as housing has risen by +20% in the last year. Those with modest or no savings are experiencing real income declines as inflation outpaces nominal wage gains.

As I have noted in the past, the Fed seems more politically motivated than in the past. Years ago, a Fed chairman stated that the Fed should take away the punch bowl when the party was getting too good. We are arguably at that place, but this Fed seems to have abandoned this view and has made no real recognition to the substantial recovery of the economy and the financial markets. In essence, there has been no effort to restrain market enthusiasm and to reintroduce risk into the investment equation.

Time will tell whether the current policy was sound. **At some point in the not-too-distant future, Fed support will end and the correction in the markets could be severe given how expensive they have become by virtually any historic standard.** Were this to happen it would risk the savings of the nation and undermine the soundness of pension programs which have become dependent on the market. Rising interest rates will demand a greater portion of the national budget, restricting other spending options which could benefit the majority of Americans.

So, in a sense, we could be witnessing the biggest Ponzi scheme in history. This risk, especially at current valuations, is extraordinary, and it seems that, with a substantial economic recovery underway, the Fed should immediately begin to reduce itsartificial support which has so distorted the economy and our capital markets.