

Private Wealth MANAGEMENT



Double Trouble: Dollars & Debt

By: Vijay J. Marolia, Chief Investment Officer at Private Wealth Management

People have short memories; especially when those memories are unpleasant. This is becoming clearer to me now that the same people who wanted to sell all their investments earlier in the year, are now trying to double their money in the short term. It seems the fourth quarter of 2008 is all but a distant memory. Amazing, isn't it?

Even more amazing is the surge in stock markets all around the world since the start of the year. Our own S&P 500 is up over 20% while emerging markets are up 60-80%! Who can blame investors for hunting for returns when the cash in their savings account earns barely over 1% (if they're lucky)? And that's before taxes!

Although I do see good investment opportunities in some areas, two dangers continue to worry me—dollars, and debt. But it's not my dollars, or my debt that worries me. I'm worried about our dollars and our debt as citizens of this great country.

I trust we are well aware that our leaders on Capitol Hill (in their infinite wisdom) are very good at spending more money than they have. That's nothing new. But the amount and the speed of that spending are mind boggling.

At the beginning of 2008, our national debt stood at approximately \$9.2 trillion dollars. By the time you read this, it will be approaching \$12 trillionⁱ. But that does not include the unfunded promises we have made to ourselves in the forms of Social Security, Medicare, and Medicaid. In fact, the Peter Peterson Foundation estimates that if we include those promises, our real national debt is actually closer to \$56,400,000,000,000 (\$56.4 trillion)!

That means every household in the country owes approximately \$483,000. In other words, every man, woman, and child has a debt of \$184,000—not including the debt that they actually know about (mortgage, car loans, credit cards, student loans). As you may have observed from your children or grandchildren, it's not easy these days for a kid to come up with \$184,000! It is however very easy for our government, via the electronic printing press at the Federal Reserve. I'll come back to that later...

Of course the problem with debt is that we must pay interest on it. In the fiscal year 2008, our government spent \$412 billion on interest payments alone. To put that in perspective, that same year, the total amount our government spent on education was \$61 billion—that's almost \$7 dollars of interest expense for every \$1 of our children's educationⁱⁱ. It is my humble opinion that many of the fundamental problems our society faces have their roots in that last sentence.

Now, to pay for all this debt, the government must either raise revenues through taxes, or print money out of thin air. It will mostly likely do both. Although we are preparing for higher taxes in the near future, many are not at all prepared for the inflationary consequences that will inevitably arise.

At the end of 2008 the Federal Reserve accelerated the pumping of money into the money supply by crediting excess reserves to the member banks. Before August of 2008, excess reserves made up about 5% of the monetary base (money supply). Now, those reserves make up more than 90%ⁱⁱⁱ. In fact, although the history of this country spans over 230 years, we have somehow managed to double the money supply in just the last 3 yearsⁱⁱⁱ! That is not a typo! Inflation may not be today's problem, but it will be here eventually.

We feel confident that by focusing on the truth and ignoring the hype, we will be able to position our clients to take advantage of the opportunities that will inevitably arise. In the mean time, we wish you and your family a wonderful holiday season and we look forward to seeing you early next year for our annual reviews.

Respectfully,

Vijay J. Marolia, MBA
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ⁱ source: Morningstar

ⁱⁱ source: Board of Governors of the Federal Reserve System

ⁱⁱⁱ source: David Rosenberg of Gluskin Sheff