Secure Retirement
Peace of Mind is Real Wealth

March 2020

Economic Update, March 2020

Gold & Treasuries in a Crisis

by Richard Morey

This month' report will be short and simple. It's coming out early because we need to focus on getting fully invested. The once-in-a-career opportunity I have been warning about seems to have arrived.

The opportunity in question involves owning gold and long Treasuries through a crisis. Thus far, through February 21, we have made 13.3% in our long Treasury investment, which is the PIMCO 25+ Year Treasury Strip ETF).

We began this year with just under 10% allocated to long Treasuries, and ended the week on February 21 with 28% allocation, having made additional purchases on January 29, February 20 & 21. Another purchase was made today, on February 24. Two additional purchases are planned to bring it to 40% total allocation.

The other investment is gold. Gold began the year at $1,521 an ounce and ended last Friday, February 21, at $1,645 an ounce, for a gain of 8%. (Gold mining stocks are up only approximately 3.5%, which is why we switched into primarily owning pure gold a few weeks ago.) We began the year with 13.5% in precious metals, since increased to 22%, and we will have our full 25% allocation soon if markets continue to be turbulent.

There is a very good reason gold and long Treasuries continue to shoot up, and it is that **the world economy appears to be in the beginning of a very large and ugly crash.**

I've been focused on the embedded losses throughout the U.S. corporate debt market, and corporate debt markets worldwide. I have said, without reservation, that this will lead to what is called a debt liquidation event throughout our entire business sector, resulting in a crash in asset prices.

Please note the junk corporate debt index we monitor had not gone down as of February 21 (the lastest reading from FRED (Federal Reserve Economic Data) from the Federal Reserve Board). Even though it certainly looks as if a recession is now likely, until the lowest-quality corporate bonds begin to dramatically fall in price we cannot confirm this is truly the end for this business cycle.

That being said, we should now soon find out who is correct, i.e. Secure Retirement or Wall Street. Perhaps the largest amount of low-rated business debt in U.S. history will turn out to be miraculously immune to market forces forever. Perhaps it's actually really good when the engine for world growth, called China, comes screeching to a halt, along with who knows how much of the world.

For over 20 years I have struggled understanding one question in economics, which is whether or not all recessions must be caused by external shocks. Depending on one's definition of 'external shocks,' I have tended to believe the correct answer is no. Instead, I side with those who believe that, when markets become sufficiently off-balanced, nearly anything can pop them. The specifics of the external event are, from that perspective, relatively meaningless.

Having said that, if you wanted to pick an external shock sufficient to bring an economy down, **a global pandemic would be at or near the top of the list.**

Despite the obvious spike in fear (see long Treasury and gold prices), stock investors have continued to believe Fed money-printing is the only meaningful variable in stock prices. As a result, if they own the stock of a company that has their sales and profits slashed because their stuff is made in China, or their customers are in China, this is actually a good thing because the Fed will print more money. Today's investors believe it's impossible for stocks to fall if the Fed prints money.

This faith in Fed money-printing is literally the last thread people are holding onto. They will end up greatly disappointed when they realize, too late, that short-term asset prices are determined by the willingness of investors, and especially banks, to speculate with their money. The moment that flips, Fed influence completely disappears. Then, as Warrett Buffett famously said, we get to see who was swimming naked, i.e. which companies were sustained only by debt.

This thread called faith in the Fed could break at any moment,
by which time I want to be fully invested (65% of our total in long Treasuries and gold, plus 35% in alternative mutual funds designed to profit when volatility rises). Of course, if the Coronavirus situation should subside before the world economy fully tips over, gold and Treasuries might fall quite a lot. In that case, we will automatically sell shortly after the top.