April 2024

THE "YOU MAY NOT KNOW REPORT"™

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Is It Growth or Just Cash Flow?

This question occurred to me recently as I was reading a report on U.S. economic growth.

The report, optimistic in its tone, stated that the US economy grew by $334 billion in the 4th quarter of 2023. That's a good number; at least on the surface.

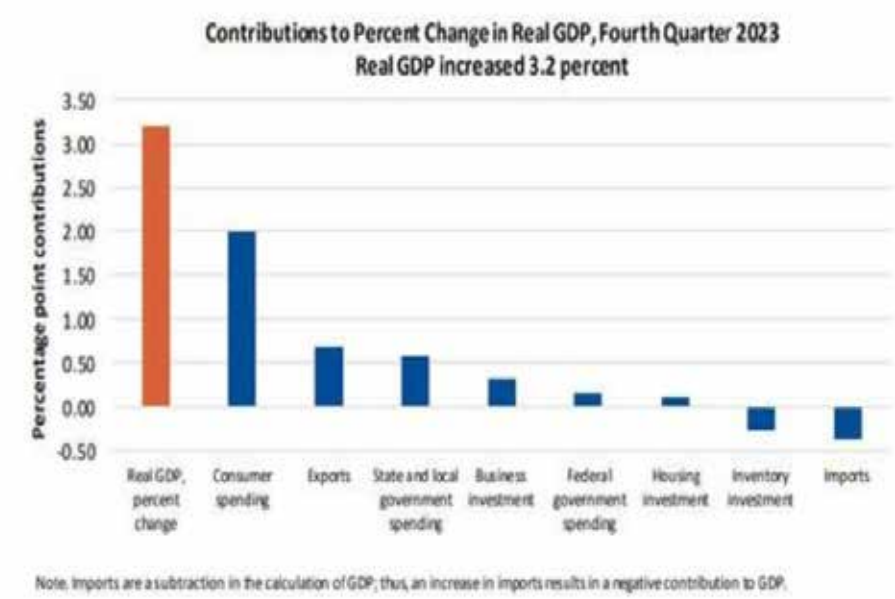
Digging in to the numbers though, it's pretty clear that this respectable growth number isn't really growth at all. To quote my recent radio guest, Michael Pento, it's just reporting more rainbows which are fantasy rather than reality.

The Bureau of Economic Analysis reported that the increase in GDP in the fourth quarter reflected increases in consumer spending, exports, and government spending both at the state and local level[1].

Imports, which reduce GDP, also increased.

Examining the GDP numbers more closely, consumer spending increased for health care, food services and accommodations.

This chart is from the article referenced above.



Personal consumption spending contributed 2% to GDP bottom line, which makes sense in an economy that is driven 70% plus by consumer spending.

Here's the only problem with these seemingly rosy numbers, this spending was driven more than 100% by debt accumulation.

One visit to the US Treasury's "Debt to the Penny" website confirms as much[2]. On September 30, 2023, US Government 'official' debt was $33,167,334.0444,723.16[1]. That's a lot of zeros, so let's label the debt at about $33.2 trillion.

On December 31, 2023, total debt was $34,001,493,655,565.48[1]. Again, let's just call that about $34 trillion.

The increase in debt was about $800 billion. For readers that want to be more precise, the number is about $834 billion.

Debt increased by $834 billion, and the economy grew by $334 billion. That means that the government borrowed $2.50 for every $1 of economic 'growth' in the US economy.

Here's a dose of reality for you – that's not growth.

To make the point, let's assume that I earn $100,000 per year. That's my income or personal GDP (gross domestic product). Now, let's say that I go borrow another $100,000.

That means that my personal cash flow increased by $100,000 in that particular year. But, did my income or personal GDP double?

Obviously, no.

Since I'm obligated to pay back that $100,000 loan, it will be a drag on my future income or personal GDP. I'm borrowing against future production to improve my cash flow presently, but down the road I will be required to pay the proverbial piper.

Whenever that day comes, my income or personal GDP will take a hit. And, the longer I play the game of borrowing to improve current cash flow, the bigger the future hit will be.

In past issues of the "You May Not Know Report", I've discussed the debt realities facing the United States in detail. Simple math tells us we are past the point of no return and the only way to keep the cash flow going is to borrow until there are no lenders other than the Fed at which point currency creation or devaluation will be used.

Another Sign the 'Everything Bubble' May Be Ready to Burst

This past month, I was reading a piece that made me relive the (rather distant) memories of perusing car ads as a college-age young man, trying to figure out how to afford my dream car.

I remember seeing ads for nice cars that were advertised for sale with the desperate owner, upside down in their vehicle, looking to find someone to 'take over payments'.

Now it seems, some commercial office buildings are being offered for sale with the same terms.

Canada Pension Plan Investment Board has recently participated in three deals where the fund liquidated its interests in commercial office buildings at deeply discounted prices[3]. The real shocker was the pension plan selling its interest in a Manhattan office tower redevelopment project for just $1, with the buyer assuming the outstanding debt; effectively a 'take over payments' sale.

This is not an isolated case. The commercial real estate sector may be terminally ill. Defaults on commercial real estate loans have now risen to a 14-year high[4].

Commercial real estate loans are more susceptible to interest rate increases than residential real estate loans. While most residential real estate loans have a fixed payment and a fixed rate of interest, that is typically not true of commercial real estate loans.

Commercial real estate is real estate that is usually used only for business purposes like office buildings and shopping malls to offer a couple of examples. Commercial real estate loans are typically amortized for a longer period than the loan repayment period, requiring refinancing at some point which subjects the borrower to interest rate increases.

Rising interest rates over the past couple of years have seen default rates on commercial real estate loans rise. In that sense, it's similar to what we saw during the financial crisis of 2007–2009.

But the problem has the potential to exceed the size of the problem during the financial crisis[5]. During the financial crisis, distressed commercial real estate debt peaked at about $150 billion. Presently, there is $216 billion worth of real estate with the potential for financial trouble. That conclusion comes from MSCI Real Assets and is based on late payments and slow leasing.

A report[6] by "Visual Capitalist" released in 2023, informed the public that nearly 1 billion square feet of office space was vacant. In the report, Manus Clancy, senior managing director at Trepp, estimated that five in ten office towers are at risk of defaulting each month.

That's a big statement!

In response, many city planners are looking to convert some of this vacant office space to housing[7].

Is this a viable solution to the increasingly inevitable commercial real estate crash?

Not according to Goldman Sachs[8]. Goldman says prices have to drop by 50% to make converting office space to residential space financially feasible. In that statement lies the answer to the question.

Commercial office space converted to residential space is not financially feasible unless the price of commercial real estate crashes.

While residential real estate is not as ugly as commercial real estate (at least presently), there are signs that it is slowing.

Wolf Richter, of "Wolf Street", frequently comments on the price of residential real estate. In his recent piece[8], Richter published a chart of the Case-Shiller House Price Index, the most commonly used index to track the price of residential real estate. I've republished that chart here (Chart 1, bottom left).

If you're wondering if housing is in a bubble, just look at the chart, you'll get some perspective as to the size of the current housing bubble compared to the bubble in housing at the time of the financial crisis.

If you notice the right-hand side of the chart, you'll notice a 'double top', a fairly reliable technical pattern that occurs at market tops.

While there is no guarantee that the residential real estate market has topped here, there are some early signs that it may be.

Richter points out in his article that the Case-Shiller Index has now declined for a couple consecutive months. This from his piece:

> *The overall home price index for the 20 metros that today's S&P CoreLogic Case-Shiller Home Price Index covers declined by 0.6% from the prior month, the second month in a row of declines.*
>
> *The index formed a double-top with the first peak in June 2022 and the second peak in October 2023. The close-up of the 20-Cities index shows the double-top, and now the beginnings of the downward slope off the second top.*

Chart 2 (bottom right) is a bar chart of the Case-Shiller House Price Index.

Notice the two months of declining prices at the right-hand side of the chart.

While it is still early, it seems that the 'everything bubble' may be showing signs of a decline.

The question is if more rate cuts by the Federal Reserve or more quantitative easing (currency creation) will reflate the bubble.

Chart 1

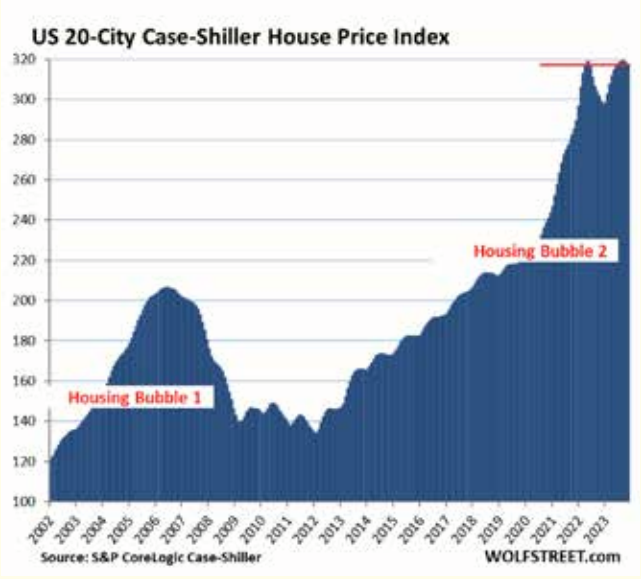
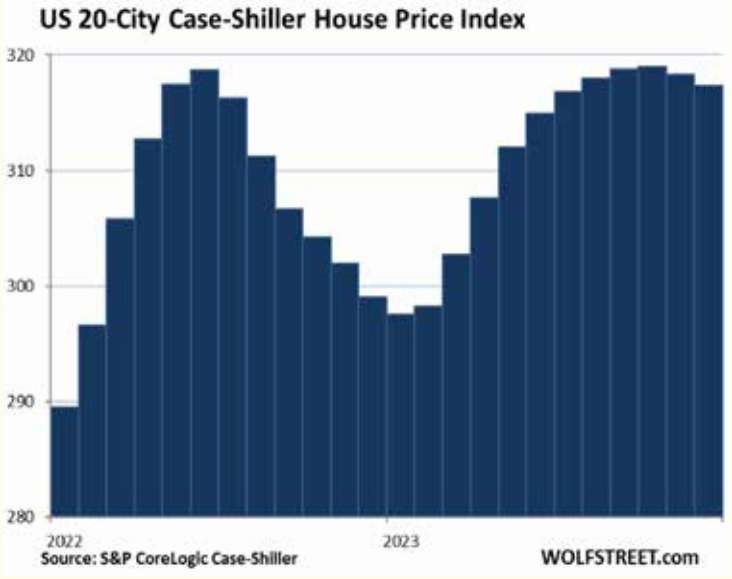


Chart 2



Is the Penny Now Obsolete?

It probably comes as no surprise that the US penny costs more than one cent to reproduce. According to an article published on "Schiff Gold", it costs the US Treasury three cents to produce. This from the article[10]:

It's no surprise to readers of this site that metals are often worth more than fiat currency. Gold, silver, and other precious metals are known for their value. But sometimes fiat currency can't even compete with zinc.

The US penny, which is primarily made of zinc, costs roughly three cents to produce and is only worth one cent according to the federal government. This is the opposite of what has generally happened historically. Generally, governments produce currency that is worth far more than the cost of producing it. Imagine printing a one-hundred-dollar bill which costs far less than a hundred dollars in materials and printing costs. The profit from this is called seigniorage. With pennies, the US Government is practicing reverse seigniorage. This loss of money from producing pennies is one of the arguments for abolishing the US penny. There are other arguments against the penny such as the claim that it's worth so little compared to the typical American wage that is makes no sense to denominate prices in pennies, would anyone argue that the United States needs a coin worth a half a penny?

In fact, the United States used to have a half-cent coin which was abolished in 1857 for being worth too little. A half-cent in 1857 would be worth approximately 18 cents today. That of course is more valuable than not only the penny but the nickel and dime as well.

Of course, when it comes to monetary policy and politics, optics is everything. I don't look for the penny, nickel, or dime to be abolished any time soon as much sense as it would make (the cost to make a nickel and a dime exceed their face value too). Doing away with those coins would be an admission that the inflationary policies of the politicians and the policymakers at the Federal Reserve have been a failure.

Credit Contracting? As Far as Auto Loans Are Concerned – Yes

One of the first symptoms of debt excesses is failure of banks. Last year, we saw the failure of Signature Bank, Silicon Valley Bank, and First Republic Bank to name a few.

I expect more bank failures lie ahead. As the April issue of the "You May Not Know Report" is going to print, New York Community Bank appears to be in trouble reporting that the bank's fourth quarter losses were $2.4 billion worse than previously reported[11].

Forgive the sarcasm, but that's a monster accounting error.

The bank has ousted its Chief Executive Officer and a board member in response and stated it has identified what the bank called "material weakness in internal controls."

Maybe that's bankspeak for "monster accounting error".

The bank had already reported a "surprise loss" of $252 million for the fourth quarter and slashed its dividend, now the bank has disclosed that it took an additional loss of $2.4 million.

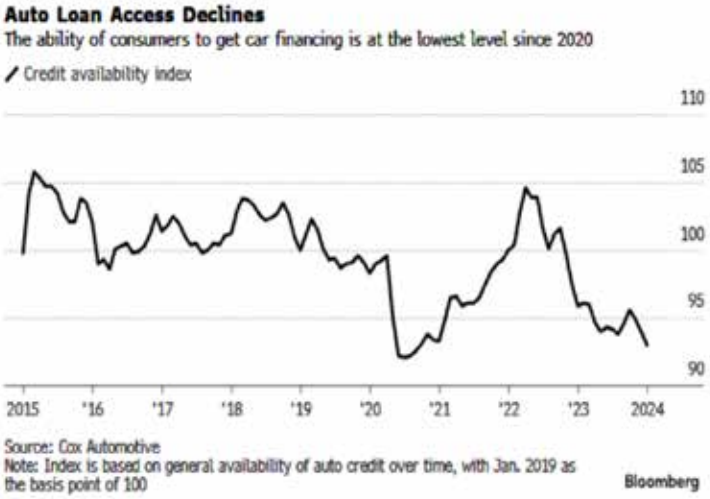
Another symptom of excessive debt is tightening credit. As default rates rise due to debt excesses, banks begin to pull back and become more stingy with credit. That is happening presently. This[13] from "Zero Hedge":

As borrowers struggle with making their $1,000 monthly car payments, banks with auto financing units are swiftly adjusting to stricter credit conditions by turning down many prospective buyers, further complicating the process for consumers to secure auto loans.

According to Bloomberg, "That's freezing out buyers with lower credit scores who can't afford a large down payment, while Americans with healthy finances are having more trouble than usual securing loans."

New data from Cox Automotive shows access to auto credit has tumbled to the lowest level since August 2020. The approval rate for loans is down 1.6% year-over-year.

Note from the chart here, reprinted from the article, that it's now more difficult for consumers to get auto loans than at any time since 2020.



It's not a coincidence that it was at that point massive currency creation began to take place and "helicopter money" flooded the economy.

Now, as loan paybacks are beginning to falter, banks are reacting.

While the delinquency numbers are not at epidemic levels (yet), they are 12% higher than at the beginning of 2020 and 23% higher than the 15-year average. And they are rising.

Survival Bunker Business is Flourishing

Some of the top 1% of the wealthiest Americans are now sparing no expense to create luxurious survival bunkers.

Really.

This[12] from "The Hollywood Reporter":

On the heels of Sam Esmail's apocalyptic thriller "Leave the World Behind" and December news reports that Mark Zuckerberg is constructing a 5,000 square foot bunker under his ranch on the island of Kauai, the business of fortified shelters is booming.

Adding more fuel to the flames: escalating armed conflict around the globe and, closer to home, the ongoing onslaught of mass shootings and an increasingly fractious political landscape leading up to the presidential election on November 5.

The one-percenters who can afford to pull out all the stops for self-preservation are doing so more than ever – often in a fashion that goes way beyond the submerged corrugated metal units seen on reality shows like Nat Geo's "Doomsday Preppers".

Aiming to protect themselves from potential threats including civil unrest, cyber-attacks, nuclear bombing, power grid failure, and drastic climate change events, many work directly with general contractors to build kitted-out end-times bunkers., while others call on a handful of specialized companies.

"It got really busy, and it seems like the phone hasn't stopped ringing' World War III seems like it's coming," shares Ron Hubbard, CEO of Texas based Atlas Survival Shelters, who noted that the news about Zuckerberg's bunker "caused a buying frenzy." He's currently constructing a $7.5 million bunker for a client in Oklahoma that is in the design phase.

Robert Vicino, founder of Del Mar, California-based Vivios, which creates underground survival shelters, agrees: "Now that Zuckerberg has let the cat out of the bag, that's got other people who share his status starting to think, "Oh God, if he's doing that, maybe he knows something that I don't, maybe I should seek this out myself. But it's no secret that the one-percenters and top-ranking government officials have been in on this bunker idea for a long-ass time. The pandemic was a huge driver of interest in sales; then all the global concerns and issues at home are another boost. We're here to provide peace-of-mind solutions." Other moguls enamored by bunkers include billionaire and former PayPal CEO Peter Thiel – whose attempts to build one in New

Zealand were nixed in 2022 – and Bill Gates who is rumored to have underground security areas under every one of his homes.

Al Corbi, president and founder of Virginia-based SAFE (Strategically Armored and Fortified Environments) which caters to custom designs for the uber-rich, notes that many billionaires are particularly focused on how to survive power grid failures, including buying cars and planes that are less reliant on computer interfaces. "A lot of these guys are buying up King Air or older planes that don't have the electric avionics, and keeping one or two older cars built before 1986 in their collection, so they'll still function in an EMP (electromagnetic pulse). The newness as it's shifting from the idea of nuclear ka-boom to protection against local threats. The real threat is the power grid, which is ironically the plot of "Leave the World Behind". In situations like this, sustaining your life is as important as food and water.

The average shelter that Hubbard sells "on a daily basis" – consisting of a prefab modular steel bunker – is in the $200,000 to $400,000 range (It's like buying a Ferrari," he says) and 50 percent of Atlas Survival Shelters clients are women. (Hubbard appeared on an episode of the final season of "Keeping Up With The Kardashians in 2021 in which Kim and Khloe Kardashian tested out one of his 500 square-foot, $200,000 bunkers.)

Maybe it's just me – but the Ferrari sounds like more fun.

Could Your 401(k) Be Gone Within Ten Years?

A recent "Bloomberg" op-ed[13] penned by Allison Shrager is titled, "Your 401(k) Will Be Gone within a Decade".

The opinion piece suggests that the government should kill the 401(k). Here is a bit from the piece:

If you are among the 56% of US workers with a retirement plan, I have some bad news for you: Your 401(k) will be gone in 10 years, tops. Not the money, thank goodness, but the plans themselves.

There has been a brewing intellectual movement to get rid of the 401(k) for several years, with scholars on both the right and left questioning its value. And as the federal government gets increasingly desperate for new sources of revenue, the tax treatment of 401(k) s is a likely target. There are good policy reasons to end it, but the question remains: Will Americans still save for retirement?

All of this cost the government an estimated $185 billion in 2019, or 0.9% of GDP. That's not nothing. And in theory it's justifiable because it creates a powerful incentive to save for retirement. More retirement savings have a triple benefit: for the economy overall, since they fuel growth; for the government, since retirees with income are less likely to be a burden on the state; and, of course, for workers who might not save enough today and regret it later.

Then again, maybe not. The first rumblings that the benefits of the tax breaks may be overstated came in a 2014 study of Danish savers.

Without tax-advantaged accounts, it found, people just put their money in another kind of account. People did save more in retirement accounts, but that's mostly because of automatic paycheck deduction. Subsequent research in other countries found similar results. Not only did the tax incentive fail to encourage more saving; the biggest beneficiaries tended to be the wealthy.

To review: Neither conservatives nor liberals are particular fans of tax-advantaged retirement accounts, and savers appear to be indifferent to them. So, what's the point of a 401(k)?

From my experience, I would take issue with the statement that savers are 'indifferent' to 401(k) plans. The author acknowledges that people do save more in retirement accounts noting that it's due to an automatic paycheck deduction. I would add that an employer match is another incentive.

But, it doesn't surprise me that there are calls to do away with or change how retirement savings will work. A Social Security program that is underfunded might ultimately be the catalyst for changes surrounding retirement plans including 401(k) plans.

While this is nothing more than talk at this point, it may help make the case for some savers to consider Roth IRA's or Roth IRA conversions.

Milei Ends Monster Deficit in Just Nine Weeks

The newly elected president of Argentina, Javier Milei, balanced the country's budget and created a surplus in just nine weeks.

How did he do it?

To paraphrase Nike, he just did it.

"Mises Wire" puts this accomplishment in perspective[14]. The government of Argentina was projected to have an operating deficit of 5% of GDP. In US terms, he closed about a $1.2 trillion deficit and created a $400 billion surplus.

How did he do it?

He cut MANY government agency budgets by 50% while slashing crony contracts and activist handouts.

Mises notes that despite the cuts, the world has not collapsed.

Here is an excerpt from the Mises piece:

Deficits aren't the only win Milei's logged. He's slashed crony regulation, got rid of currency controls, and recently slashed rent prices by removing controls – that actually led to a doubling of apartments for rent in Buenos Aires, slashing rent costs.

Unfortunately, its' not all smooth sailing: a bill to privatize corrupt state-owned companies – to effectively de-Soviet the Argentine economy – was blocked by the socialist opposition who serve the government unions who would lose their jobs.

Meanwhile, a major Melei reform to make it a lot easier to hire people but would hurt unions was struck down by the high court, which said it must go through Congress.

Having said that, for the average Argentinian, these are the deck chairs on the Titanic compared to the elephant in the economy: Argentina hyperinflation.

Just last week, the monthly inflation figure came is at 20.6% - on the month. That was a lot better than the outgoing government, but it still left year-on-year inflation at 254%.

Why so high? Partly because Milei had to free up the exchange rate to smooth the path to dollarization – for Argentina adopting the US Dollar instead of the local confetti.

But mostly because the rivers of money printed by the previous socialists continue to run through the battered ruins they left of Argentina's economy. After all, Milei's only been in office for two months.

Milei's reforms will continue to be trench warfare. But his inflation progress is going to be key to retaining support. He just notched a big win with the deficit, but it only stops the bleeding – the patient is still on life support.

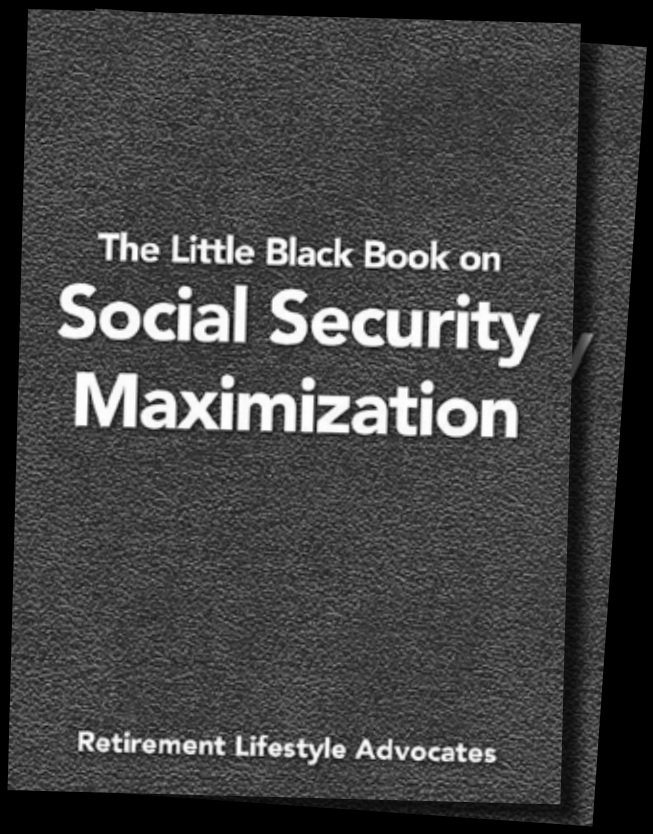
To fully kill Argentina's hyperinflation, Milei would need to make real progress on the dollarization – or dare we dream – a gold standard. On dollarization, that would involve announcing a months-long window for peso assets to be revalued in dollars.

He's been preparing the groundwork so far- the currency controls and the deficits are a big help. And he's surely motivated to do it since dollarization in other countries like Ecuador has 90% public support. But it's a complicated process, and if done badly, he'll be dead in the water.

The stakes are high. And not just for Argentina. If Milei succeeds, he'll be a model for radically shrinking government in other countries in Latin America, in the rest of the world, and even for our spineless goblins in Washington.

April 2024 Special Report

The Little Black Book on Social Security Maximization



During the month of April, we are offering a free book that was a best-seller when released. The book is titled, "The Little Black Book on Social Security Maximization".

If you are looking to maximize your benefits from Social Security, this book is must-reading.

To request a copy of this book for you or for someone who might appreciate it, use one or all of the postage-paid reply cards included with this month's newsletter, or visit:

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Why You Need to Consider Adding Precious Metals to your Portfolio

Gold and silver have always been real money.

As inflation rages and fiat currencies like the US Dollar lose purchasing power, gold and silver can be a great way to preserve purchasing power.

Look at this example.

When Richard Nixon eliminated the convertibility of the US Dollar to gold in 1971, an ounce of gold sold for $35 per ounce and the average cost of a new home was $25,000. At that time, you could buy a new home for $25,000 in cash or 700 ounces of gold.

Fast forward to the present. The average cost of a new home is $380,000. The $25,000 that once bought a home fifty years ago is now not even a down payment on an average new home.

However, the 700 ounces of gold that used to buy a new home now buys 4 average new homes.

Given the current rampant inflation, doesn't make sense to consider metals in your portfolio? IRA, Roth and even 401(k) funds may be used. Visit Densmore.PreciousMetalsBuyersGuide.com to get a free precious metals investing guide.

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