## Content

Secular Booms

Regenerative Eras

Central Banks

Boomers vs. Millennials

Final Thoughts

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# May 2020 Market Commentary

### "It's not about being afraid; It is about being prepared" - Christopher Cole of Artemis Capital

Every once in a while, I'll read something that really blows my hair back and makes me think "Holy S^&t", I have so much still to learn in this business after 17 years. Christopher Cole's recently released paper The Hawk and the Serpent is a must read, especially if you're looking build and protect multi-generational wealth as we are at Koa. This month, I will try pull a few choice ideas from this dense and informative read, but there's just no way to dive in fully in just a couple of pages. The average advisor in our industry is 52 years old and was in elementary school during the last stagflationary bear market of the 1970's. Most advisors have only been invested in markets where interest rates have been falling while asset values of Stocks, Bonds and Real Estate have been up and away.

Effectively the purpose of Chris' paper is to build an outline for an investment strategy not for this year, or even this decade, but for a century. In it he shows pretty effectively how investors fall into the trap of "Recency Bias" – plainly we assume that asset classes will generate returns and produce similar volatility moving forward as they have in recent history. Fortunately for the sake of this paper, Chris has data on Stocks, Bonds, Real Estate, Gold, Commodities and Volatility that stretch all the way back to the 1920's, so his points are not only thought provoking but backed up by what counts – data. His study of this data has led him to the conclusion that economies and markets pass through phases of Secular Booms (1947 to 1963 & 1984 to 2007) and what he calls Regenerative Eras (1929 to 1946 & 1964 to 1983). If you noticed above, he feels the most recent Secular Boom ended in 2007… an investor might question that opinion as the US Stock Market has continued to make new highs, regaining the 2007 highs back in 2013 and has since pushed to new highs. But Chris' view is that Central Banks in trying to save the global economy from the abyss of the 2008 financial crisis have only delayed our march down one of the paths of tail risk – Deflation or Higher Inflation.

In our current predicament with the demand shock that has been caused by the Corona Virus, ZIRP (Zero Interest Rate Policy) would signal that the immediate risk is one of deflation. Under deflation, falling asset prices wipe out investor nest eggs as we experience falling rates, lower growth and debt defaults. Central Banks in turn move to negative rates and quantitative easing. However, periods of deflationary pressure can easily reverse depending on the actions of Central Bankers and Policy Makers and effectively yank the economy out of the ditch of deflation into the opposite ditch of higher inflation. Under this regime, rising hard asset prices also wipe out savings and the value of cash. These inflationary periods are marked by higher interest rates but still slow growth and ultimately end in fiat default and helicopter money.

The question investors have to ask themselves is – do you want to bet that the next 10 to 20 years are going to look like the boom times of the 1984-2007 time period or has the pendulum already started swinging the other way and we are in a 1964 to 1983 time period… we just haven't realized it yet? While the history books will ultimately tell us, who was right many decades from now, my best guess is we are in a period of secular change that is going to require a Regenerative Era. We currently enjoy historically high valuations on all of the commonly held assets classes by investors – Stocks, Bonds and Real Estate. We have the highest Corporate Debt to GDP levels ever. We have 17 trillion in negative yielding Govt. Debt globally. We have the lowest capital gains rates and highest income disparity in American History. I hope you enjoyed the boom times, because they were good to the Boomers! Chris writes, "A new period of secular decline began with the great recession and will likely end in entitlement defaults, helicopter money and monetization of budget deficits".

Boomers vs. Millennials the coming battle. While it seems odd to think grandparents will be in a war of wealth with their grandchildren, let's run through some interesting ideas on the topic. Boomers (Defined as ages 56-74) will be drawing on 28 trillion in retirement assets to live on; assets grown during a 40-year demographic and debt super cycle. Boomers applaud the current actions of the Federal Reserve to buy just about any asset they want in the bond market which has effectively helped to prop up assets in the financial markets. Boomers represent the lion share of wealth in our country and 23% of the populace. Millennials (Defined as ages 24-39) who represent 26% of the populace by contrast will likely be the first generation to be poorer than their parents. With many carrying what amounts to mortgages to pay for their higher educations, they will be in support of populist policies like printing money and giving it directly to people (Rather than buying financial assets). Don't be surprised if an idea like UBI (Universal Basic Income) gains a hold as the govt. has just recently been sending out $1200 "Stimulus" checks to the majority of the populace. In contrast to Boomers, Millennials are incentivized to support policies that redistribute wealth (Higher taxes on earnings and capital) which creates inflationary pressures which ultimately destroys the value of their debt.

While not knowing how the deflation/inflation debate will play out – what we do know is our clients' primary holdings and building blocks of their wealth – Stocks, Bonds and Real Estate may be in for a rougher ride than clients have experienced during their period of wealth accumulation. As their financial advisor we will have some difficult decisions to make – do we keep them allocated as we always have during our/their investment lifetimes and potentially suffer dismal returns or do we build in assets/strategies that they are not familiar with and have not done well in recent history but have done better in other "Regenerative Eras" like the 60s through early 80s? Clients are not accustomed generally to owning large allocations in metals/commodities or owning volatility. We will have to do what we can in the months and quarters ahead in broaching these topics and having these conversations with our clients. It's a difficult thing to get an investor to invest in something that hasn't made money in recent history – but perhaps our clients will realize that we are in a period of sea change and investing in assets that are not yet broadly owned will be our ticket in trying to not only survive but thrive in the coming decade.

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