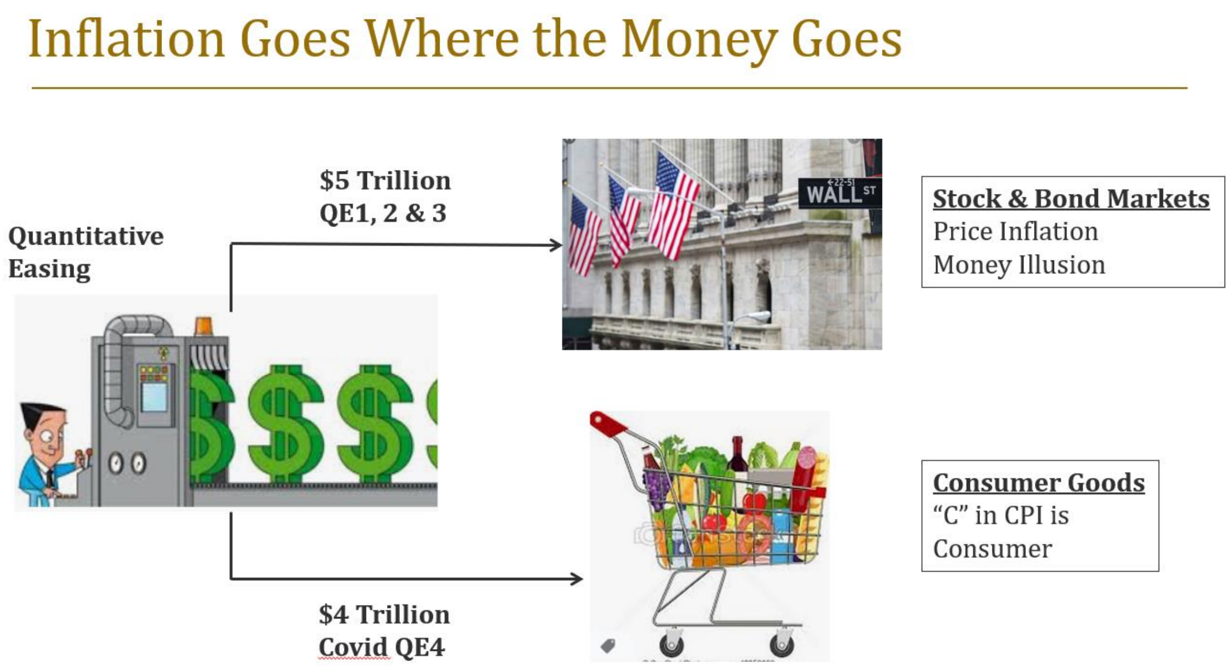
We Have Had Serious Inflation and It Will Get Much Worse

- Money printing has not moved the CPI inflation needle so far, but that will change with Covid-19 relief.
- Inflation follows the money. The first 3 rounds of Quantitative Easing (QE) has pumped $5 trillion into stock and bond markets. Security prices are inflated with newly printed QE money. Investors suffer money illusion.
- QE4 is pumping another $4 trillion into the economy, but this time much of it will buy goods and services, driving up consumer prices and moving the CPI needle way up.



The big inflation question has been: Why is there no inflation while the Fed is pumping $trillions into the economy? The standard answer is "Because there is no velocity." The correct answer is "Because the consumer price index (CPI) does not measure this form of inflation." The Fed has bought bonds with the $5 trillion in QE, and sellers of those bonds have bought their own stocks in stock buybacks. All of the inflation has been in stock and bond markets, so the CPI has not moved at all.

But this new round of QE, dropping $4 trillion by helicopter into the hands of citizens, will flow to consumer goods, so the CPI will increase. Everything is inflated – security markets and consumer goods and services.

Inflated stock and bond prices

No one questions the success of QE in buoying up stock and bond prices, creating an unprecedented run-up in gains. We have enjoyed the longest market recovery on record. Unfortunately, this has created the biggest wealth divide ever by making the rich a lot richer. But this will change when QE is unraveled, and inflation is removed from security prices. We witnessed this in the fourth quarter of 2018, when initial QE unravelling drove stock prices down by 15% right away – the Fed got burned bad. In other words, the great divide can be erased by reversing the printing presses, sucking that money out of the securities markets.

This is a precarious position for the government and the economy. How much money can the US print? Experts fear a "Debt Spiral" triggered by increases in interest rates beyond the Fed's control that will force even more money printing to pay interest on the debt. It will not end well. The newest round of QE to provide Covid-19 relief exacerbates the problem and puts inflationary pressures where they will be measured.

Inflated consumer prices

US GDP is $20 trillion. The first 3 rounds of QE put $5 trillion into securities markets, and this newest round (QE4) adds another $4 trillion, much of which will inflate commodity prices. That is $9 trillion recently added to more than $25 trillion in debt in a $20 trillion economy. The US is bankrupt.

This could not happen at a worse time for the country's 78 million baby boomers. Approximately 55 million of these baby boomers are living on Social Security, so the big question is will Social Security inflation adjustments be maintained in a system that is forecast to become bankrupt in 2029.

Conclusion

Economists warn of deflation in the aftermath of Covid-19, and that may happen for a short period of time in the CPI. But no one can deny that $9 trillion of fairly new money sloshing around in a $20 trillion economy has to lead to inflation.

As security prices decline, the usual defense will not work because inflation will erode the value of cash. Inflation-protected securities should help, as well as investments in real goods like commodities, precious metals, and real estate.