Hello Everyone,

***When did flattening the curve become until we find a cure?*** David Portnoy, founder of Barstool Sports.

Good question.

Today's missive, however, tries to answer another question. How can you have inflation and deflation at the same time? How does that work? I took a shot at this dilemma last Friday, but came up a short. Today, I'll try to fill in the blanks.

As usual, this is meant to give you a better understanding as to what lies ahead…or what is almost upon us.

Signed, Your So-How's-Your-2020-So-Far? Financial Advisor,

Greg

# KKOB 05.15.2020 How Can Money Be Destroyed?

**Bob:** So, Greg, I know you wanted to move on to Phase 3 of the Inflationary Cycle. And, the story about "***Even the Cows Have Earrings***" was a pretty funny introduction.

But, my understanding is some listeners want some more explanation about what happens in Phase 2. And that is the phase you see us entering now. Right?

**Greg**: Right. And, last Friday, I probably should have given your listeners a better explanation.

In Phase 2 of an inflationary cycle you'll see both inflation and deflation operating side-by-side. The inflation part is easy to understand. The authorities print too much money and we see prices rise.

So, Bob, the question is, how can we have deflation simultaneously?

**Bob:** And deflation is where prices and wages collapse. That's what happened in the 1930's during our Great Depression.

**Greg:** Right. But, back then, we were on a gold standard. Not now. Today, we loan money into existence. I know that sounds weird but trust me…that's how it works.

Anyway, if you can ***create*** money via loans, it follows then, that if that loan defaults, money is then **destroyed**.

Let's use some real world examples to make the point:

- 63 percent of Americans have a mortgage.
- Total mortgage debt is now north of $10.3 trillion
- Next, there are roughly 260 million passenger vehicles registered.
- Over 100 million of them were bought using loans, amounting to $1.2 trillion.
- Credit card debt totals $3.9 trillion with an average balance of over $9,300.

All those trillions were loaned into existence. Meanwhile, 45% of adult Americans have no savings.

So, Bob, we all know what Covid19 policies have done to the economy. What do you think the odds are that all of those trillions will be repaid?

**Bob**: Not good. Some are already walking away. I can see a wave of defaults coming not just with individuals, but also with corporate America. I mean, JC Penny, Hertz Rental Car, Golds Gym, Sachs Fifth Avenue, and a bunch of others are already filing for bankruptcy protection.

**Greg:** Right. So, as loans default, it's as if that money just disappears into a black hole. It's destroyed. That's very deflationary.

**Bob:** But the government is compensating by printing trillions. And they are farming it out to almost anyone with a pulse. Wouldn't that counteract the destruction?

**Greg:** That's the theory. My concern is, I don't think we are compensating as much as we are substituting.

The difference is this.

When people earn money, there is a relationship between money and production----or, money and service. An honest transaction was engaged and completed. Value was added.

However, when you ***substitute free money*** fresh off the printing press, ***in exchange for no product or service***, what you are really saying is both your work (or lack thereof) and your money are worth nothing. This is what the socialists haven't figured out yet. They have everything backwards.

The money in your wallet is really nothing more than paper---or digits on a plastic card. What gives it value is the work, effort, & production you earned. Without that, we're Zimbabwe.

In short, money does not give your work value. Your work gives money value.

**Bob:** So, this is why Phase Two of the inflationary cycle is so confusing. Money is being created by the electronic printing press, but simultaneously being destroyed by a collapse in debt repayments.

**Greg**:  Yes.  That's it.  And the free money just contributes to an economic dystopia the Bible calls "unjust weights and measures".

So, how does this Covid19 saga end?  It depends.  If we go back to work and there is a reasonable recovery, we will avoid the Phase 3--hyperinflation.  The honest relationship between money & work, value, and production will be reestablished.

If, however, we stay closed and substitute ***money for nothing***, the outcome is certain.  And, no it's not your chicks for free.

We will dramatically devalue the currency.  Inflation will win. Because, while *there is a limit* to debt owed, *there is no limit* to the amount of currency that can be created with strokes on a keyboard.

**Bob:**  Great report and I liked the ***Dire Straights*** reference.  How do people reach you?

**Greg:**  My number is 250-3754.  Or, go to my website at zanettifinancial.com.