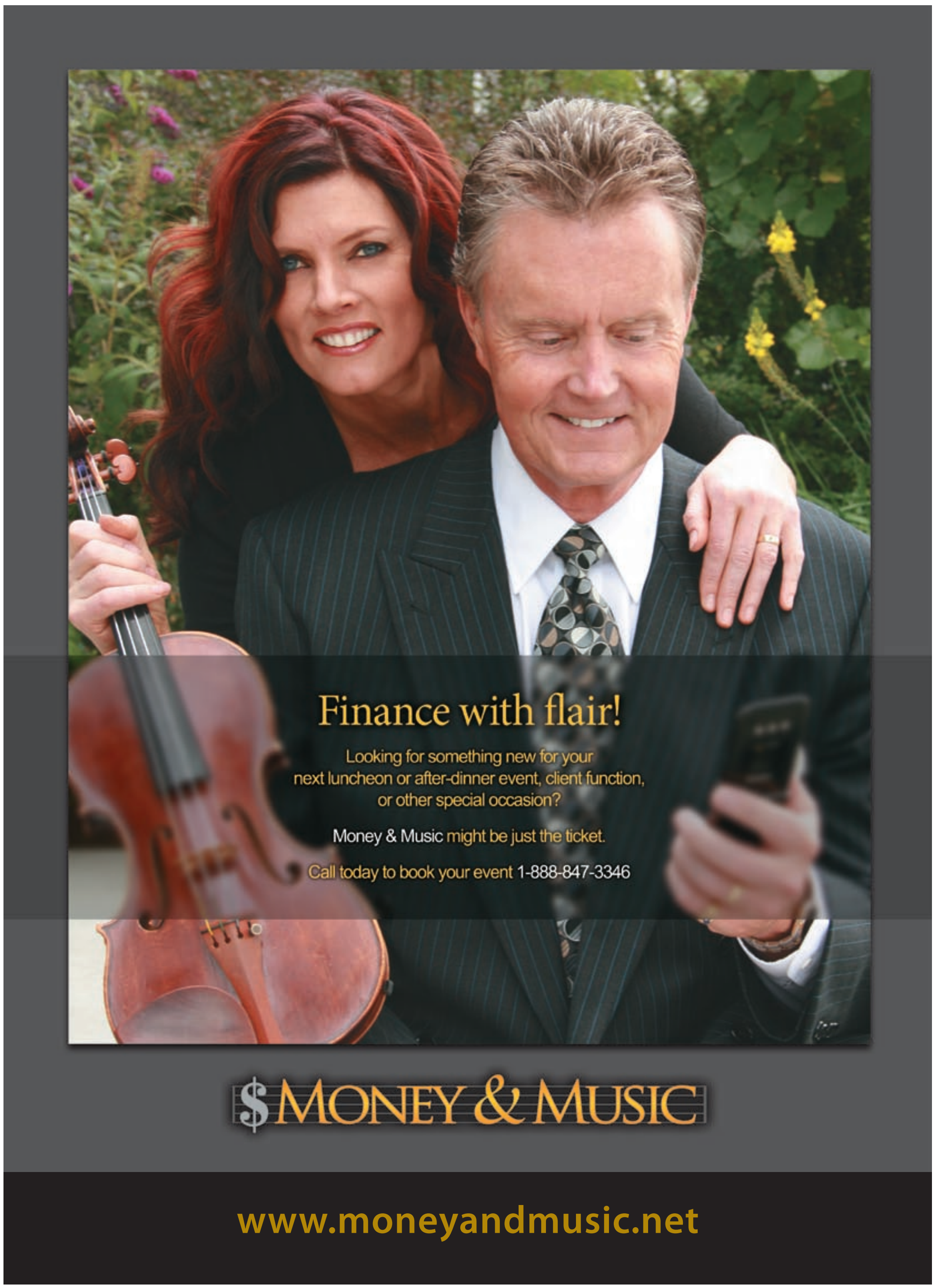
Money & Music

Written by Jeff Thredgold, CSP, President, Thredgold Economic Associates

We are very pleased to announce a new video and web site for our *Money & Music* program. My wife, entertainer and recording artist Lynnette Thredgold, and I have presented this program many times during the past few years and would love to present it at your next event.

Take a look at our website…www.moneyandmusic.net. Watch videos, listen to music, read reviews, and learn more about this unique offering that audiences are raving about.



Tea Leaf

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Your guide to understanding today's economy and financial markets

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Zip…Nada…for the Moment

U.S. consumer inflation continues to be absent, still impacted by the sharp decline in energy costs of the past nine months. Where we go from here remains one of the most critical questions on the minds of financial market players.

The Consumer Price Index (CPI), easily the most followed of all inflation measures, declined 0.1% in March 2009, coming in below expectations. More importantly, the CPI has now declined 0.4% during the latest 12-month period, the first 12-month decline in consumer inflation since 1955…a period of 54 years.

Two Contrasting Viewpoints…
Plus a Middle Road

Rampant Inflation

Highly vocal critics of the Federal Reserve and the Obama Administration argue passionately that the current mix of monetary and fiscal policy is prone to disaster, i.e. rampant inflation. They suggest that the more than doubling of the Fed's balance sheet from roughly $875 billion before the financial crisis to more than $2 trillion now…done with newly created money…is the height of irresponsibility.

Adding insult to injury in the eyes of the inflation wary are the unprecedented budget deficits to be run this year and for years to come. The inflation wary suggest that the ownership of gold, other commodities, and real estate are the preferred places to keep one's financial assets.

A Run of Deflation

The other vocal camp suggests that one need merely look at the Japanese example in the early 1990s for a whiff of what is to come. The bursting of Japan's real estate and asset bubble roughly 17 years ago led to a serious eight-year battle with the deflation disease, i.e. declining prices for assets of all types.

While declining prices for homes and land and commercial real estate and stock prices and manufactured goods and services might sound like a good thing, it is quickly followed by declining wages and declining incomes. Significant amounts of spending are also delayed as people assume that prices will be lower if they wait longer.

Is that not what is happening in dozens of residential real estate markets today? Potential homebuyers and investors are excited about much greater values in markets today, where home prices have fallen 30%…40%…50%…, but aren't many waiting for even further declines before they make an offer?

The deflation camp points to declining home prices; declining values of commercial real estate in many, many markets; major slack in labor markets; and global recession as a menu for deflation in coming years. Their desired investment portfolio favors fixed-rate notes and bonds, especially those issued by the U.S. Government and highly rated companies.

In the Middle

The third view is that we will muddle our way through in regard to inflation pressures in coming years. The Fed will shrink its balance sheet back to more normal levels when financial flows improve by selling assets it has been buying. The process is not that difficult.

In addition, bond investors will remain so inflation sensitive that they will force the Fed's hand, if necessary, to tighten monetary policy significantly in order to keep inflation at bay.

We have been here before during the late '70s and early '80s. The Fed responded at that time with a major monetary tightening to fight off double-digit inflation that engulfed the economy. The middle road, worst case scenario suggests that the current massive Fed ease of 2008/2009 could be followed in 3-5 years by a major tightening to corral inflation pressures…

…the only sure thing is that inflation will not be allowed to get out of control

Jeff

"TEA"ser

Before you criticize someone, walk a mile in his shoes. That way if he gets angry, he'll be a mile away and barefoot.

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