Interest Rates Will Stay Low Forever

The primary mandate of the US Federal Reserve was price stability. They have been anything but successful. From the origins of our currency system under Alexander Hamilton (the real guy, not the play) in 1792, until the Federal Reserve was created in 1913, gold was stable at $20.66 per ounce. With gold now around $2,000 per ounce, our currency has depreciated 99% under the Federal Reserve.

In 2012, the Fed approved a formal goal of 2% inflation. In a landmark change announced in late August 2020, the Fed announced they were dropping their long-standing practice of pre-emptively raising interest rates to head off higher inflation, and accepting periods of inflation in excess of 2%. For practical purposes, interest rates will stay low for a very long time.

What does this mean for you?

In the good old days, risk-free Certificates of Deposit and Treasury bills paid 4% to 5% interest or even more. Now they pay a fraction of that amount. You will have to save more and work longer, possibly 5 years or more longer.

Prudence suggests that everyone have cash reserves in case of an emergency. It is generally recommended that someone still working have at least 6 months of living expenses in risk-free investments such as cash, checking, money market, etc. If you are retired, you should have at least 3 years of living expenses in risk-free, highly liquid investments.

Otherwise, the traditional asset allocation of bygone times of 60% equities (stocks) and 40% bonds is by and gone. For the foreseeable future, fixed-income will be producing almost no income. If a 10-year US Treasury pays 0.7% interest and inflation is 2% per year (or higher, maybe much higher), you are guaranteed a loss of more than 1% purchasing power every year. Now you can see why Warren Buffett calls 30-year US Treasuries "Certificates of Confiscation."

A standard metric of investments is the P/E, or Price to Earnings ratio. In the 20th century, the average P/E for US stocks was 16 to 17. In general, the higher the P/E, the more speculative the investment. A C.D. or Treasury bill paying 5% interest has a risk-free P/E of 20 (100/5). In early September 2020, the 10-year US Treasury paid 0.67%, giving it a P/E of 149 (100/0.67). Now you can see why Jim Grant of *Grant's Interest Rate Observer* calls Treasuries "return-free risk."

Entities that rely heavily on fixed-income investments, such as foundations, insurance companies, endowments, and pension funds (including your pension fund) will find it increasingly difficult to meet their obligations.

So, you must put your money somewhere. I suggest that you put less of your hard-earned and saved money in paper assets, and more in real assets.

(1) Stocks are real assets. They represent people and ideas and factories and buildings that produce goods and services. The average stock in the S&P 500 and Dow Jones Industrial Average pays a dividend higher than the 30-year Treasury, and many companies pay solid, dependable dividends of 3% or higher.

Of significant importance to the stock market is the concept of the "Greenspan put," named after former Federal Reserve Chairman Alan Greenspan. Basically, the Federal Reserve will do whatever it takes to support the stock market. "Don't fight the Fed."

(2) Real estate. With more people working from home, and the rise of e-commerce, office and store-front rental property may be problematic. But residential real estate is on fire, with many properties receiving multiple bids above the asking price. There has been a deficit of new home construction for more than a decade, and with the ultra-low interest rates, prices have gone bonkers. A second home, vacation or recreational property may also be considered. As the old saying goes, "They're not making any more land."

(3) The #1 driver of the price of gold is real interest rates, the nominal rate (the rate you receive) minus the rate of inflation. If a C.D. pays 5% and inflation is 1%, the real interest rates is (+) 4%. When real interest rates are positive, gold, because it pays no dividend, is not competitive. When a C.D. pays 0.5%, and inflation is 2%, the real interest rate is (−) 1.5%. People turn to the precious metals (and other hard assets) to preserve wealth. I hope you will consider owning physical gold, with one ounce US Gold Eagles as your core holding, kept in your personal possession in a safe deposit box at the bank (I will discuss safe deposit boxes in an Editorial in the near-future).

Since the beginning of my financial writing, I have recommended everyone place 5% to 10% of their entire net worth in "portable wealth." If, for whatever reason, you cannot pull the trigger to buy gold bullion, then I encourage you to put that money into quality collectables, such as art, jewelry, diamonds, numismatic coins, rare books, or even baseball cards or comic books.

(4) The seemingly never-ending money creation by our Federal Reserve and other central banks is Modern Monetary

See page 159 for disclosure information.

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Theory in real life. It has never been done before. It is an experiment. No one knows how it will end; a deflationary crash, hyperinflation, a panic. But it will end. However, it shakes out, being in debt makes you vulnerable. Please make every effort to be debt free (which is good advice at any time).

Disclosures

Dr Doroghazi is not a registered financial advisor under federal law or any state law. The advice provided is of a general nature, and should not be interpreted as personalized or individualized to your specific portfolio.

Acknowledgment

Dr Robert Doroghazi is a retired cardiologist who trained at the University of Chicago, the Massachusetts General Hospital, and Barnes Hospital. Warren Buffett said his book *The Physician's Guide to Investing: A Practical Approach to Building Wealth* should be "required reading at med schools." To sign up for a free trial to *The Physician Investor Newsletter,* visit www.thephysicianinvestornewsletter.com

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