2020 Holiday Special with Ronald Stoeferle and Grant Williams Part 2

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Erik: Macrovoices episode 252 was pre-recorded on December 14, 2020. I'm Erik Townsend.

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There won't be any market wrap or postgame segment this week. Instead we'll be bringing you part two of our holiday special, in which we're taking a deep dive on the topic of fiat currency being debased in real value. Patrick Ceresna will host the series, and I'll be acting as a panelist alongside both Grant Williams, author of the Things that Make You Go Hmm newsletter and producer of the Grant Williams Podcast, and Ronni Stoefele, publisher of the In Gold We Trust report and fund manager for Incrementum.

In last week's episode, we began with a review of the major events of 2020, then discussed the topic of fiat currency debasement at a high level, before moving on to distinguish fiat debasement from inflation. We then discussed which trading strategies are appropriate to hedge each of these separate and distinct phenomena. We even pondered whether Bitcoin is replacing Gold as the favored store-of-value hedge against fiat debasement.

This week we're going to return to the distinction between inflation and fiat debasement, and then talk through a long list of hedging trades against each of those risks, ranging from precious metals to bitcoin to farmland to base metals and crude oil.

We'll be back to our regular format with a market wrap and postgame segment on January 7th.

Patrick, let's dive right back in where we left off last week…

Patrick: All right. So now let's go back to Jeff Currie's distinction between fiat debasement and monetary inflation and talk about the best trading strategies for those two outlooks. Specifically, I think we really owe it to ourselves and our listeners to question what could go wrong with the trading strategies we each favor.

So here's how I want to do this.

First, we'll discuss fiat debasement and fiat debasement alone and, setting the topic of inflation aside for now, let's focus on how to trade debasement. I want each of the panelists to state their views and their own hesitations or reservations about what could go wrong.

But then I want to ask everyone to critique everyone else's views so we can really challenge ourselves to consider how things could play out differently and where things could backfire.

So, Erik, let's start with you.

Erik: Well, if we're talking debasement, that means what you have to do is trade into your scarcity asset of choice, which has got to be either gold or crypto. And I don't think I can bring myself to do the crypto thing because, frankly, I just think this is a very, very misplaced trend.

And it's not just gold and other precious metals. That's a little bit of a stretch, though, because the big argument for silver is more of an inflation argument and particularly that silver is likely to be consumed in the buildout of solar capacity and green infrastructure building.

So I think gold is really the asset for me as far as fiat debasement.

If I was going to consider anything with crypto, it would be maybe calls on bitcoin, just to participate in what I think is a crazy tulip mania of bitcoin.

But if it breaks out above its previous all-time high and starts to show some upside momentum, I think it could easily double from here. And it's a double on silliness and insanity, not on any logical fundamentals. But it's got a lot of momentum behind it.

There's a lot of people that are very hyped up about it to not participate in that just because you've got some judgment about the rationale of it. And maybe I don't want to be in bitcoin, but I'd consider some bitcoin calls.

But that's really the speculative side of it. The hedge, I think it's all about gold.

And my personal hope is that the action in bitcoin will cause – a big breakout in bitcoin I think could cause a big downdraft in gold because people start giving up on gold. Maybe that gets us all the way back down to $1,350. And, if so, I think it's a fantastic buying opportunity.

Patrick: Ronnie, what's your take on that?

Ronnie: Well, I think one of the most important things that we haven't talked about yet is the US dollar. And, from my point of view, we are at the beginning of a big dollar bear market.

I know, of course, that the concepts, the milkshake theory of our mutual friend Brent Johnson – but just having a look at the chart of the dollar index but also just the US dollar against the Japanese yen, against the Canadian dollar, against the Australian dollar, but also against the British pound and the Russian ruble, I think that the US dollar will go lower.

Of course, at the moment I think if you have a look at positioning, net short positioning, the US dollar is at record highs. And I think that the sentiment in general is pretty negative. But from my point of view, it is primarily the US dollar weakness which is the main trigger for this commodity bull market.

Let's face it, the fundamental case for copper, for uranium, for iron ore, for silver is there for a while. But now I think the weakness in the US dollar has really been the trigger for those bull markets emerging.

And we always said it is gold that moves first, then it is the silver market, then it is the broader commodities base, and then it's energy. And now even uranium is rising big time.

So I think also having, of course, a look at the upcoming new administration in the US, I think we are at the beginning of a big bear market in the US dollar. And let's face it, for economic growth, for emerging markets, for commodities, that's a pretty good environment. And, actually, it seems that the whole world wants and needs a weaker US dollar.

Patrick: All right. Well let's go to Grant now. What's your way of approaching the debasement? And what do you think of both Erik's and Ron's view?

Grant: I had a very interesting conversation, as I mentioned earlier, with Fred Hickey a couple of weeks ago. And Fred was talking about how he morphed from a technology analyst, writing a letter called the *High Tech Strategist*, which it did right the way through the internet madness, right the way through the 1999 dot-com boom.

And he talked about how in essentially the early 2000s he took a look at what had happened. He called that bubble – well he traded it spectacularly and made himself an awful lot of money.

And he recognized in 2001 (I think it was) that the problem he was going to face going forward was one of debasement, was one of protecting the purchasing power of his wealth. And it was that recognition and that realization that made him look at gold, that made him realize that gold was the answer to that problem. And that gold mining shares were, if you like, call options on that problem.

And so what he did was he took a look and he realized that that was going to be his problem for decades to come. And here we are, two decades later, Fred is still writing *High Tech Strategist*. He's still facing the same problems.

And having that understanding that this was going to be a multiple-decade problem, Fred has had a call position in gold which was designed to protect him from debasement. And he's been able to trade around that in the mining shares. At times of great stresses he's been a buyer. At times of great strength he's been a seller.

But I think having that understanding, that long-term view of what he was trying to ameliorate has enabled him to have the right position and trade around it rather than chase things up and down, which is something that anyone new to the precious metals markets almost has to do as a kind of entrance fee into the game. I mean, it's a very painful space to try and learn without understanding history.

So I think if we're right that the problem we are going to face is currency debasement initially, followed by inflation, and we try and put some kind of timeframe on that, then it helps us understand what the right course of action is.

And, to me, gold remains the best core asset to provide that protection that you want against these twin problems, one which is likely to follow the other.

But understanding that gold is the solution to that debasement problem actually frees you up to then think about tactical positions in inflation hedges, whether it is copper, whether it is energy, whether it is raw materials.

It allows you to view them as tactical allocations because you've really set aside a portion of your portfolio to deal with what you really believe to be the main threat. And that is debasement.

So I think once you do that, you look at these things in a wholly different light. You can look at raw materials. You can look at industrial commodities. You can see the froth in them. And you're not wedded to those positions because you've got your protection on in gold for the debasement issue.

You can trade the inflation wave, knowing that that gold will actually help you if the inflation becomes a problem. Yes, okay, maybe it won't be the single best hedge against it, but I guarantee it won't hurt you in an inflationary environment.

So I think that the most important thing is to understand the problem you're facing, put a timeline on it. How long do you think it's going to be a problem for? If you think it's only going to be a short-term problem, then do you really need to take these precautions?

I suspect it's going to be a long-term problem and that dictates the action you take. And to me that's a very pragmatic and a very sensible way of dealing with the issues we face right now.

Erik: Ronnie, I want to ask you about the dollar view. Because, first of all, from an economic standpoint I get it. Like, the argument for the dollar debasement, yup, makes sense. I understand. I think I agree with you.

But from a trading standpoint, I can't even think about shorting the dollar. And the reason is simply that am I smart enough to figure out that the dollar is going to underperform against other fiat currencies, when I'm not exactly sure, between with Janet Yellen at the Fed and Christine Lagarde at the ECB, who knows who is going to win the competitive devaluation war?

What I do know is that fiat currencies all around the world are going to be devalued in real terms against precious metals.

So, as much as I want to agree with you and say, yes, I think the dollar is probably headed down, I almost don't care from a trading standpoint because, to me, the trade has to be long precious metals. And I invest in dollars, so it's gold against dollar. If you like gold against euro, fine.

But I don't see why you would want to make the bet on the dollar underperforming against other fiat.

Ronnie: I see your point. And it is definitely – you know, having a bearish view on the US dollar or having a positive view on the euro is definitely not that contrarian anymore. I always do my 10 forecasts at a big precious metals conference in Munich. And last year I said that the euro will trade to the US dollar at 1.17 and I was kind of ridiculed. And I thought, okay, that's a pretty good sign.

Now, everybody was talking about the euro breaking below parity and so on and it became differently.

But I think now we are seeing – and that's what Madame Lagarde already said at her last press conference, that they are closely monitoring the continued appreciation of the euro.

Now, of course it is pretty difficult for the ECB to generate inflation while your currency is appreciating. Because the ECB has only one mandate and this is price stability. So we have to be very careful with that view, I totally agree.

And I think when it comes to gold, for example, we see that fiat currencies are devaluing versus gold at a different pace.

So this year, for example, gold is up in euro terms I think 12% while in dollar terms it's up 21%. But on average over the last couple of years, the devaluation of currencies – be it the US dollar, the British pound, which was obviously a bit weaker, but also the euro, the Swiss franc, the Canadian dollar – was roughly 10% per year on average.

So I agree to your point.

But I think technically, if we have a look at the Dollar Index at how it's trading recently, I think this looks like a really horrible chart. And I see it really breaking down below this 89.9 support level.

Now, I think that when it comes to the currency question, I totally agree you want to have currencies that cannot be inflated at will. And that, of course, brings us to gold but also perhaps to bitcoin.

But going forward, I just see that there is so many measures taken in the US that would confirm my bearish view for the US dollar. It is this move from monetary QE to fiscal QE. It is the move of average inflation targeting that we don't see in the eurozone, for example. It is this very, very aggressive expansion of the broad monetary aggregates, which is slightly more aggressive in the US than over here in the eurozone.

And I think this MMT gaining in popularity – and, by the way, I thought it was brilliant to invite Stephanie Kelton – I really enjoyed listening to her view and I think it's very, very important to exactly listen to those people that don't confirm your view, that have an opposite view.

But I think this MMT trend gaining so much in popularity, and also the fact that Janet Yellen will become the new head of the Treasury, which is another sign for this MMT development becoming more mainstream, I think this all sounds pretty dollar bearish to me.

So, on a relative basis, I think that we'll see more weakness of the US dollar. But structurally I'm not a big bull in the euro or any other fiat currency.

Patrick: Ok the whole discussion we just had was about fiat debasement specifically. Next I want to do the same thing for the topic of inflation. That's coming up next, right after this message from our sponsor…

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Patrick: Okay, that discussion was specifically about fiat debasement. But now let's do the whole thing over again for inflation.

So we'll start with each panelist's view on how to best hedge the inflation we think is likely coming. Then we'll do a group critique of what could go wrong. So, Erik, let's start with you on your take on inflation and how to hedge it.

Erik: Well, I think this is really, really important because, on one hand, I think that the certain thing right now is the fiat debasement side. I really am convinced this time around that it is going to lead to inflation. But I said that 10 years ago. And I'm not going to say I'm wrong. I'm really, really, really early when I said that 10 years ago.

So if we're really going to have the inflation now, and I think that it has the potential to become bigger than 1970s degree of runaway inflation and stagflation, it's going to be a really big deal.

And it's going to be really, really important to be on the leading edge of that.

On the other hand, I've been wrong for a lot of years thinking it was about to start any day now.

So the way I'm approaching this is oil is a position that I have a huge long exposure in already because I'm primarily an oil trader. And a lot of my oil trades are not long-term buy-and-hold positions. But I do have buy-and-hold positions in back-of-curve time spreads – Z1, Z2 spread on West Texas Intermediate crude oil futures for people who are following that trade, which has performed incredibly well since we first talked about it on MacroVoices.

That's as much inflation exposure as I want until I see inflation really starting to happen. And not just I think it's coming but I see it's really coming.

And when that happens I want to be in a position to really put on all those inflation trades once I get confirmation that it's really happening.

I'm spending a lot of my time right now really thinking about what that means. Because I think it's heavy exposure to mining. But not more precious metals, more focused on copper, particularly because I think we're going to see infrastructure buildouts that are very much about electrifying the economy. That's going to require a huge amount of copper.

I think that silver is going to be a more important precious metal because, as solar energy gets more and more important, silver gets consumed in producing some types but not all types of solar panels. That's going to be an important inflation hedge.

But really I feel like I don't have the portfolio figured out in terms of exact allocations of what percentage to this and what percentage to that.

And some of these things, like base metal mining, I don't know the difference between Freeport-McMoRan and other mining companies. I don't know enough about fundamentals of those industries to really be a stock picker myself. So I'm trying to figure out exactly how i'm going to approach it.

But my feeling is you want to be in the currency debasement trade right now, you want to have some kind of inflation hedge. And you want to be ready to dramatically increase your inflation hedge on confirmation that that big wave of inflation that I and a lot of other people expect really does show up the way we expect it to.

So that's the way I think about it.

I'd be particularly interested in Grant and Ronnie's perspective both on that strategy but also how do you really figure out how to build out that inflation hedge strategy that's not about precious metals and currency debasement but it's about the expectation of a pickup in the velocity of money and eventually getting to the point where we have a self-reinforcing wage and price-inflation spiral?

When that starts, my prediction is it's going to take a lot of people by surprise and accelerate very quickly. And you're not going to want to be left behind. You're going want to be ready and say I planned for this, I know exactly what my trades are, I'm ready to put them on.

And I'm not ready. I want to be ready. And I'm not there yet.

Patrick: All right. Well, let's go to Ronnie first then. What's your inflation trade and the way you'd put perspective and, as well, what you think of Erik's perspectives?

Ronnie: Well, Erik touched on the topic of velocity. And I think this is really something crucial going forward.

I had a conversation with Mark Bristow, the CEO of Barrick Gold, and he asked me, well, do you think once we get the vaccine against COVID that should put an enormous amount of pressure on the price of gold? And I said, yes, short-term it will because there will be major shifts happening in allocation. It will be this back to normal trade.

But it also means that velocity will pick up at one point, because what we are facing now is this uncertainty, it is this loss of trust in the future. Nobody is making big investments at the moment. Nobody is making any travel plans.

So I think now with the vaccine, all this uncertainty will disappear over the next couple of months. And this will mean that the velocity, or as the Austrian School of economics would call it, the demand of hold money will change. And it will need an enormous amount of liquidity that was created over the last couple of months.

So from my point of view, this should definitely be inflationary. While at the moment I think more and more people are getting a bit concerned when it comes to inflation, but it is not really on the radar screens yet.

And I think that few people – that's what our friend Luke Gromen once said – few people believed the Fed could tame inflation in 1979 and few believe that the Fed can spur inflation in 2020.

So we are seeing some sort of a reverse Volcker.

I think that this move to average inflation targeting was really something that was underreported, because it happened in August and nobody really cared about it. But I think this move from an inflation target to an average inflation target is really big news.

Back in the days, we had 2% inflation as the ceiling. Now, as inflation was undershooting over the last couple of years, the Federal Reserve is very, very open and it's saying we want inflation rates to overshoot. And once we go to 4–5%, it will not automatically mean that we will raise rates. So this is basically the recipe for negative real rates over the next couple of years.

Of course, that should provide a pretty positive environment for gold. But also – and that is what we are playing as a diversified inflation portfolio. It should be pretty beneficial for commodity currencies. It should be positive for emerging market equities. It should be very positive for the silver space. We are sometimes putting on trades long commodity producers versus short importers. We have got some tips.

And I think that – of course, gold is a pretty obvious inflation hedge. But by creating some sort of a diversified inflation portfolio, I think you are just reducing the volatility that you are seeing, for example, in the gold-mining market. So our approach is clearly diversified.

Now, why am I so positive for a new commodity cycle? I think, first of all, investors are deeply underweight. I don't know any big investors saying we are massively overweight real assets such as commodities. And then, I think they are just generationally cheap, both compared to their own history but especially compared to other assets.

So I think real assets over financial assets, that's really the big shift that we are seeing for the next couple of years as one of the big trends.

Patrick: All right, Grant. Let's circle to you. Inflation trades and what is your impression of both Erik's and Ronnie's views?

Grant: Well, I think the interesting thing here is that we are talking about a major paradigm shift. We've been investing in a deflationary environment for essentially 40 years. And what we're talking about here is a secular shift back to an inflationary environment, which we haven't seen, realistically speaking, since the 1970s – apart from that little spike we saw in commodity price inflation in the 2000s.

And if you look at a chart of interest rates going back thousands of years, you'll see that that inflation spike in the 1970s was absolutely the outlier. Interest rates, as one can quite understand, have trended down always because man is always looking for cheaper money and finding ways to produce that.

So the inflation spike is the outlier.

And so because of that, you've actually been given a great opportunity, and what is – if we're pragmatic about it and step back and be pretty basic about it – a pretty simple opportunity here. If I told you you were going to have inflation, what would you do?

Well, you know what? You would short the long end of the Treasury curve and you'd buy commodities.

Well, guess what. The long end of the Treasury curve is at or near all-time highs. And commodities are at or near all-time lows. I mean, you have the perfect setup.

And the reason you have the perfect setup is precisely because people have been expecting this to happen for the last 40 years and it hasn't.

So we're at a point in time where – Erik said he wanted confirmation and I think he's right – but, really, if you look at the price commodities are at, I think you can start to position yourself with energy in natural gas and oil. You can start positioning yourself in basic materials. You can start putting that position on now to the extent that you have tolerance to be wrong for a period of months.

You will get plenty of chances to get in. But if you look at the charts of basic materials, the CRB raw materials index, you'll see it's turned and it's definitely broken out of a trend and it's starting to move higher.

So I think it's safe to start easing your way into these positions. If you want to wait for confirmation like Erik, that's fine. But, for me, the one side of that trade that you're going to have problems with, even though it's an incredibly appealing prospect, is being short the long end of the curve.

Being short the long end of the curve, you are going to be somewhere where I don't think that's a position you can set and forget. Because you are going to have to fight the Fed every step of the way.

There will be some tremendous profits to be made.

But you will have to be ready to take those profits off the table because we'll end up with yield-curve control, we'll end up with all kinds of things because, given the state of US government finances, there is absolutely no way they can let interest rates rise past a certain point. And that certain point is actually not that far away from where we are now.

So, even though you've been given a 5,000-year positioning opportunity, that's something you're going to have to be very nimble with. And you're not going to be able to ride a 5,000-year trade. Although I bet the other way.

Commodities, on the other hand, I suspect offers a much better and potentially more peaceful ride north than the bond yields do south. So I'd totally be looking at that.

I think being positioned in gold right now, oil, natural gas, even uranium is finally starting to move – but, unlike Erik, I don't think it's too early to start establishing positions in these things.

And, obviously, the one advantage that you have right now that you didn't have in the '70s are ETFs, which give you a very simple way for low cost to be (quote unquote) long commodities.

You don't need to go to the futures market. You don't need to go into the commodities space. You don't need to get complicated. And you can buy low-cost ETFs, which give you broad exposure. And you can pick and choose the kind of parts of the commodity spectrum you're going to be exposed to and do it very, very simply.

And I would suggest if you're ready, then I wouldn't leave any sleep over starting to establish positions. And if you're not ready than I would start, as Erik said, trying to understand which commodities you want exposure to and working out the most sensible way for you to gain the exposure you want.

Erik: Grant, I just want to clarify one point, which is I'm already very, very long energy. And therefore I'm already in the inflation trade because I'm an energy trader. What I said was simply I don't want to go into other assets that I have less familiarity with for the sake of diversifying my inflation trade until I've seen that confirmation.

But the other point I want to come to is one I think you actually clarified at the end of what you were saying when you said long commodities and short the long end of the curve.

If we go back to the day that rates bottomed after World War II, if you got it right exactly perfectly to the day, you picked the low moment in interest rates because you're a perfect bottom caller, you would have waited 10 years for interest rates to meaningfully appreciate from there.

So I think for the reasons you said, we're stuck with low interest rates for a long time. Shorting the long end of the curve, as much as it's appealing, feels like we're at a 5,000-year low in interest rates and it's time to do that. I think you could be waiting a long time.

Whereas, if you see trillions of dollars of infrastructure buildout that is already basically a done deal – you can't build infrastructure without raw materials. That means copper and other commodities are going to come into very strong demand very soon.

So I just think the commodities side of what you said is much more timely than the short the long end of the curve side of it.

Grant: Yes, which is exactly what I said. I said If you were looking for the perfect trade, it's a very simple trade. It's short the long end, long commodities. But short the long end of the curve is not going to be an easy place to be.

And the commodity side is way, way easier. And you've got so many more vehicles to do it in. So I agree. The trade is simple. But one half of that trade is not going to be an easy place to be and you're going to be fighting the Fed the whole way. So why bother?

Erik: Okay, it's the "why bother" part that I didn't hear the first time. So, yes, we're in agreement. The trade here is long commodities. And at some point when that momentum gets going and you really think that there is reason to be on the short side of the long end of the curve, wait until that trade really starts happening.

But I don't see how it can happen for the next 10 years. We're stuck with low rates for the reasons you said.

Patrick: Okay, from the discussion it seems that precious metals, cryptocurrency, base metals like copper, and energy all come into consideration here.

So next I want to go into more detail about those markets. So let's start by talking about what's going on in these precious metals and whether gold, silver, and other precious metals are the best plays.

And so, Ronnie, is this story all about gold or is silver the better play? And if so, why? And what about platinum and palladium?

Ronnie: Well, I think starting with gold it's been a pretty good year. And gold perfectly did its job. It's up 21% in US dollar terms. It's up 13% in euro terms. It's up 18% in Canadian dollars. And so on.

And I think what is even more important is the fact that gold perfectly stabilized your portfolio in the extremely volatile weeks in March and April.

I once said – you know, I'm from Austria and, for some reason, I really enjoy watching Austrian football, or soccer as Americans would say. So I made the comparison of gold being a very, very reliable defender in your portfolio.

I don't know, Grant. What are the best English defenders? Sol Campbell, Rio Ferdinand, John Terry, something like that?

Grant: We don't have many good defenders.

Ronnie: But they're better than the goal keepers.

So I think gold perfectly did its job. And I was a bit confused when people in the last couple of weeks, they were really frustrated with the price of gold. And I said, you know, guys, don't be too greedy. It's been a fantastic year for gold. And I think it's just taking a breather.

Actually, when gold hit new all-time highs, I would say like 95% of the comments I got from friends and colleagues was, okay, now it's already too expensive. I will wait for the correction.

Of course now in the correction nobody's buying. But it is a relative game. And, relative to monetary growth, relative to other asset classes, from my point of view gold is still dirt cheap.

So I think the point in time when I would really become bearish gold would be the point when we see real rates rising significantly. But I just don't see that coming.

Now, going forward I think that the big story is investors' demand. We saw in fourth quarter until December, ETF holdings, for example, were down around 4 million ounces. But, in general, 2020 has been a year with a tremendous amount of investors' demand.

And I think that, longer term, the investor base for gold has clearly broadened. And positions have been pretty resilient. We are seeing over here in Europe that more and more investors are adding gold to their strategic positions to protect portfolios in this negative real-rate environment. And also perhaps to hedge against a weak dollar.

So I would say that the renaissance of gold in institutional portfolios is really the big trend and the big shift that we are seeing in 2020.

And, as I've said, the big driver going forward will become inflation.

I think the number that we just saw of negative-yielding debt that's now $18 trillion – and I think that we just saw Portugal joining the club of 10 years of negative yields.

So I think once inflation really becomes a concern, there will be an exodus out of this $18 trillion in negative-yielding bonds. And, of course, it will flow into the traditional inflation hedges, like gold for example.

Now, when it comes to silver, silver is some sort of a derivative of gold. It is up 34% in US dollar terms and 24% in euro terms. So not too shabby. And I think what Erik said before, that's totally right. The fundamental case for silver is probably even more compelling than for gold.

This year for the very first time in its history, we had a special chapter on silver that our mutual friend Emil Kalinowski helped us write. And I think the fundamental case for silver is fantastic, especially when it comes to this whole green stimulus theme.

All those environmentally oriented fiscal policies should mean a very, very supportive environment for the solar industry. And from my point of view, it will create much more demand for silver in the whole clean-energy chain.

So that's one of the points why I'm pretty confident regarding silver on a relative basis. And I think it's interesting that the gold-silver ratio held reasonably well despite the selloff that we saw in gold in the fourth quarter.

And we're also seeing silver ETFs have shown some resilience in the face of the selloff in gold.

So I think once gold makes the next leg up, I think silver will probably trade above 30. And now the gold-silver ratio is trading at 76 (so one ounce of gold you get 76 ounces of silver).

I think that gold can easily trade at $2,500 in the next 12 months. If the gold-silver ratio comes down to 40, that would mean a silver price of US $62. So I think from a risk-reward perspective, silver might even be the better trade at the moment.

Patrick: All right, Grant. What's your take when we're talking about broader precious metals? Is silver the better play? Or what about platinum and palladium?

Grant: Yes, again, I think it's really important to understand what we're trying to accomplish here because we've spent an awful lot of time here today talking about strategies to protect yourself from what are potentially multi-year, multi-decade-long problems. Certainly debasement has been for several decades now.

And then there is the trading side of this. And so they are two very, very different things. And if you understand that –

You want to start trading the mining stocks, for example. You have to understand the kind of heartache that that can bring you. And so having that long-term understanding of what you're trying to accomplish, I think, will help inform you better in terms of your entry points and exit points.

Because you can look at the gold mining stocks, when they're beaten down you tend to have an understanding of the longer-term picture and so they look more valuable to you because you're looking at a long-term problem.

Likewise, when they've run too far, you have a reference point in what you're trying to accomplish and you can see how they've overrun and it's easy to take things off the table.

So with that being said, I think here today, with gold having come off having kind of failed at $2,100 back to $1,800 – Erik thinks he can see a path down to $1,350. I don't see that path. I'm not saying he's wrong. But I don't see that path myself.

I'm looking at the long-term opportunity that gold offers at $1,800. If it gets down to the $1,700s, it offers an even better opportunity to me. So I'm very happy to buy the mining stocks here.

I think the mining stocks have dramatically improved their businesses. They're in much better shape than they've been probably any time in the last 25 years. And, more importantly I think, the management understand the mistakes they've made.

Now that's not to say if we get a really frothy gold price, and if we had the kind of move into gold we've seen into bitcoin and the attendant press and coverage that it gets, then I guarantee that some of these mining CEOs would revert to some of their bad habits. But I think for the time being they understand this.

So owning some of the gold mines, owning some of the Newmonts, the Agnicos, the Carleton Lakes, the Pretiums of the world, makes an awful lot of sense right now.

Silver, as Ronnie said, it's turbo-charged gold. You're going to have to be able to stomach a lot more volatility. But, again, if you have a long-term view about inflation, then that volatility in the silver-mining stocks against the context of what you're trying to achieve by being long silver as inflation hedge makes it easy to stomach those downturns.

So anyone that's thinking of investing in these, if you're looking at individual companies, you have to get to understand the assets, the countries they're in, the mines themselves.

You have to understand the management. Don't ever invest in a mining stock where you don't hold the management in high regard. Be very careful in mines whose assets are in somewhat shakier jurisdictions. There is a whole checklist.

And if you read people like Fred Hickey, if you read some of the more prolific gold commentators, you'll start to understand those.

But going into precious metal mining stocks as a simple way to express an inflationary view, it's a lot more complicated than that. There are excellent companies and there are poor companies.

And you want to make sure that you own the former and stay clear of the latter. And that doesn't come without doing an awful lot of reading and research. And I think it's beholden on everybody who wants to do this to do that research. It will pay off in spades in the long run.

Patrick: Erik, what's your take on the precious metals. How would you add to that?

Erik: Well, Patrick, actually I have a couple of questions for Grant and Ronnie first on the metals themselves before we come back to the stocks.

As far as gold is concerned, it's my largest position. I really believe strongly in it.

Slight correction, Grant, I'm hopeful for $1,350. I think it's very unlikely. The only way I could see it happening at this point would be if bitcoin really takes off and gets a lot of press and a lot of people are just like, oh, my God, bitcoin is the new gold. It's the thing. And people panic out of their gold.

That's where I think we could, maybe, if we're lucky ,get that chance. And, boy, I sure hope it happens. I don't think it's the base case though. I don't think we're necessarily going there. I'm just hoping for it.

Going back to gold versus silver though, I really want to ask you guys about this because there is nothing more important than invest in what you actually understand.

And I'm not sure I understand this one. Because I had read articles years and years and years ago saying silver is really, really important because it's a precious metal but it's also used in, you know, photography and this long list of things, including solar cells.

And then a few years later, I remember reading something that said, yes, they used to use it in solar cells but not so much anymore.

And now I'm seeing articles saying green revolution, solar energy, silver is the place to be because silver is used.

So are we really sure that silver is still used in modern generation solar cells? Or did it just used to get used in solar cells? Because I don't have a fully clear understanding of that one.

Ronnie: I think it's a good point. And I think when it comes to silver loadings in PV cells, for example, you can see the technological advance. Currently, we only need 20–25% of what we needed a decade ago.

So I would never say that silver is the metal that I see as most attractive just because of this whole green stimulus wave.

I think it is one feature. But primarily I'm seeing it as some sort of a momentum play on gold. And I know that many in the silver industry will hate me for that.

But I agree. I think that I just cannot see gold going to $1,350 and the price of silver skyrocketing. I don't see that decoupling.

So, primarily, from my point of view, I see it as a monetary metal. I see it as more of an inflationary metal. But I think all those supply-demand issues are just an additional driver.

And we have explained those drivers from the supply side but also from the demand side in our last report. And I think they are interesting for the fundamental case. But I think they are not the primary drivers, if that makes sense to you.

Erik: Okay, so I need to learn more about how much fundamental demand really exists on the green side of silver. But I do need to diversify. I've got way too much concentration on gold, which I really should diversify into silver and gold. And I need to learn more about the fundamentals of the green energy aspects.

Platinum and palladium, I go back to my rule is invest in what you understand. Platinum and palladium, as far as I'm concerned, is for people who really are knowledgeable about how they get used in catalytic converters and diesel, whatever it is that the palladium gets used in. And I don’t know about that stuff so I don’t touch it.

So, as far as the metals are concerned, for me it’s all been gold. I need to diversify into silver and I’m intentionally not touching platinum and palladium because I don’t know enough about it.

Moving on to where Grant was going, which is the mining shares. I have to admit this is an a real – where I’d really like to get the other guys’ perspectives on. Because I feel like a lot of people, the reason they favor the mining shares over the metal itself is they see it as a leverage play.

Okay, a lot of people are not comfortable trading with leverage. I trade oil futures all day long, so I’m very comfortable using leverage in commodity futures.

If what I want to accomplish is leverage on the price of gold, I just increase the number of gold contracts that I have in my account. I don’t see that it makes sense for that reason.

The reason, primarily, that I’ve started investing in the mining shares is I think a lot of the private placements that are available in new junior companies that are just getting going really offer a significant opportunity to get a better deal than you would get in public markets.

So as an accredited investor being able to participate, I just participated in one of Marin Katusa’s private placements in a company that I could have bought it, it’s already trading on the public exchange. But it was basically the same price as what it’s trading right now for on the public exchange.

I could buy it in a financing where, as an accredited investor, I get a half warrant for free in exchange for taking a four-month lockup on the shares. So I can’t trade the shares for four months. In exchange for giving up that liquidity, I get a free half warrant, which is very, very significant in value to me.

I wasn’t going to trade the shares for those four months anyway. So it didn’t cost me anything and I get free value.

I favor the mining shares when I can get a private placement on them. I’m not sure that I understand, other than a leverage play, why I would want to diversify beyond the metal itself into the shares other than if I can buy them right in a private placement.

And I’d love to get feedback from both Grant and Ronnie on what I might be missing there.

Ronnie: Well, I agree. For our funds, we do lots of private placements as well. I think when it comes to the mining space – I just had a look at the sentiment. The Gold Miners Bullish Percent Index is down to 34 at the moment, a level that we haven’t seen since March.

Then we are seeing that the tax-loss-selling season will be over pretty soon. So I think it's a pretty good point in time to reconsider gold and silver miners, from a technical point of view.

If we have a look at the performance of the mining shares, I think they did pretty well. I mean, the HUI, the gold miners index started the year 2020 at 230. Then it dropped to almost 150. And more than doubled within six months to 360. So that already shows you this enormous volatility of the market.

Now it is trading at 290, roughly, which is the same level like in the year 2013 when gold was trading at $1,350.

So I am seeing a pretty interesting valuation when it comes to the miners.

If you have a look at price-to-cash flow, over a period of 30 years it was only in 2019 that price-to-cash flow for the miners was lower. If you have a look at price-to-EBITDAR, same picture.

And you now I have had, I think, hundreds of meetings with mining executives this year. And there are so many virtual conferences nowadays. And I was really impressed with, I would say, most of the meetings.

So the producers are expanding their margins. We're seeing that dividends are being raised. We're seeing that most companies are pretty disciplined when it comes to their gold price assumptions. So they see the price of gold over the next couple of years at, like, $1,300 to $1,500.

I think that the sector has weathered the whole COVID crisis very, very well. We have seen, of course, temporary shutdowns. But I think they managed it really well. We are seeing that ESG is taken very, very seriously.

So, from my point of view, the gold-mining industry is probably at its healthiest shape in a decade. And valuations don't really reflect it yet.

Now, it is still a pretty small sector. We have seen lots of private placements. And some of them were really rubbish, I have to stay. But still –

I had a look at that just yesterday. The top 15 North American gold producers have a market kept so small that Apple currency is 10 times larger and Facebook is almost four times larger. So if there is really big investment flows coming into gold-mining equities, I think it will have an enormous impact.

And let's face it. We saw Berkshire Hathaway buying a stake in Barrick Gold this year. We know that Buffett has a complicated view when it comes to gold. But obviously he sees tremendous value on the balance sheet of Barrick Gold.

So I think the sector really learned its lessons. I think they are now at the very, very healthy position. And therefore we have been, over the last couple of weeks we have put in some stink bids for high-quality names that we like.

We got failed for some. And then I'm really, really confident when it comes to gold miners and many of them will make decent free-cash flow. They will pay out nice dividends even if we stay at a similar price level like now.

So we don't need gold to go 30% or 40% higher. I think those companies at the moment are really, really stable. They are solid. And we are seeing tremendous value.

Patrick: Grant, do you have anything to add to that?

Grant: Let me just add to that point of Ronnie's that Buffett trimmed his position in Barrick by half within, I think, a month of buying it, which I thought was interesting.

But it's so true, Ronnie. These companies are in great shape. They really do offer as good a value as I've seen in terms of the health of their balance sheet, the mental health of their management, and also the beaten-down sentiment. I mean, these things are still somehow unloved, despite what's going on.

And if you do – I hate to keep harping on the same point, but if you do stand back and think about the problem that gold is a solution to, Erik, you are exactly correct. They are a leverage on owning gold.

But, given the level at which these companies are trading, the good companies, you can buy leverage at a really respectable price. And if you have the right viewpoint, it's easy to trade that leverage, take profits, spin the profits into the metal itself, and trade these things the right way.

The problem comes when you think that gold-mining stocks are a get-rich-quick scheme. They're a bring-you-to-tears-quick scheme and a get-rich-slow scheme.

Patrick: That covers precious metals. Next I want to move on to real estate and other hard assets. That's coming up next, right after this message from our sponsor

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Patrick: Okay. So let's move on to hard assets now, everything from farmland to the basic materials: copper, iron ore, battery metals, even energy.

What's your position on all of that? Let's start off with you, Grant.

Grant: For me, I love the idea of farmland. But as a productive investment, not owning farmland via ETFs, which you can do through private-equity vehicles. There are ways to do it through farmland funds. And there are some really good ones, including one run by my old boss in Singapore, Steve Diggle.

But I love the idea of owning farmland, of owning a farm, of giving yourself a chance to be self-sufficient. You look at guys like Mike Krieger, who left New York City 10 years ago, moved out to Colorado, and bought a farm and is farming. And look at Chris Martenson, similar. There are plenty of people who have done this.

And it not only provides you a tremendous hedge, but it also is an extremely positive life change for people, I think.

And with the ability to work from home now so dramatically increased, I think that the possibility of farmland as an investment is going to be a really, really good one going forward.

I think commercial real estate, there are vehicles you can do that through, including some companies which are remarkably cheap, good, commercial real estate companies. But I think you have to be very careful with real estate.

Ronnie talked about the correlation with real estate and inflation. So real estate as an inflation hedge, particularly at the point in the cycle we're in, I think is tricky.

And, look, I think we've covered the basic commodities. I think they do offer good inflation hedges. And I think it's both a very simple and a very complicated trade.

It's as complicated as you want to make it.

You have the ability to buy ETFs, which gives you very simple exposure to exactly the qualities you want or the basket you want. Or you can, if you have the expertise of someone like Erik, you can construct very complicated trades to squeeze every ounce of [INAUDIBLE] out of them.

It really depends on how you want to do it.

Patrick: All right, so let's go to you Ronnie. What's your take on looking at all these hard assets in one basket?

Ronnie: Well, I think there are tremendous opportunities. We don't have a strong view on farmland, for example. I just had a look at the Bloomberg Agriculture Index. It's now trading at 43. In 1997, it was trading at 140.

I see some up trend. But it's clearly not something that we are seriously investing in because it's not our expertise. I think when it comes to base metals like copper, iron ore, but also the battery metals, I think there is some really nice opportunities.

I talked about this Vegan Climate ETF already. But from a value point of view it is absolutely clear that this green revolution will have an impact.

And if you have nickel mines for example, some of them trade at free-cash-flow yields of 10%. So if you compare it to Tesla, for example, it's like 30 times more expensive. Without nickel, there would be no batteries for Tesla. If electrification is really happening, we'll need lots of nickel and lots of copper.

And we're seeing similar valuation gaps between the producers of solar panels or wind turbines and producers of iron ore, aluminum, or silver, for example. So from my point of view, some of the mining stocks are really some sort of free options on this green revolution.

Let's have a quick look at different commodities. We like copper at the moment. But still I think, from a technical point of view, we're a bit ahead of fundamentals. We have rallied to an eight-year high at 350.

I think from a fundamental point of view, we expect deficits in the copper market to widen. But at the moment, there might be some destocking coming from China, which would be some headwind for the next couple of months.

When it comes to the battery metals, I think it's pretty interesting that once this whole COVID topic is getting less interesting for markets, I think one of the big topics will, of course, be this Build Back Better.

And I think that – for example, over here in the European Union, that's basically the only thing that Madame von der Leyen stands for is, really, this green wave, this green movement. So they are putting in a tremendous amount of government subsidies. And it works.

When it comes to EV, the EV share in France, Germany, Italy, Spain, and the UK, it has increased to 15% in November. So 15% of all new cars that are being sold are electric vehicles. That's a pretty big chunk of the market. Germany has the lead with a 20.5% share followed by the UK at roughly 17%. So we are seeing big moves in this direction.

And my tax accountant, he said, well, if you want to buy an electric car do it now, because it is so heavily subsidized it's incredible. So I expect this trend to continue.

Obviously cobalt should profit from it. But we don't have a very strong view on cobalt. It's a bit of a tricky market with most of the supply coming from DRC, obviously.

I like the lithium market at the moment. It seems that prices have bottomed.

And I really like the nickel market. And I think if we assume 40% of new car sales in 2030 to be EVs I think this will be a big, big driver for nickel demand. It should more than double until 2030.

So I think it's important to understand this market because on the supply side only 50% of all mines can actually produce a battery-ready product. So most of the supply growth is coming from Indonesia. But most of the part is actually not usable for batteries. So we see some sort of a supply squeeze ahead in the nickel market.

When it comes to energy, well, Erik, I think you know the market much, much better than I do. I think, just having a look at the numbers, energy stocks at the moment make up roughly 2-1/2% of the S&P, which is the smallest percentage of any group relative to the size of the S&P.

We have seen this big shift out of fossil fuels because ESG obviously is the very, very big topic.

And don't get me wrong, this whole green wave is a wonderful thing. And as a father of three kids I really appreciate the efforts. But I think sometimes people tend to forget the math. So this isn't something that takes 20 years. And it won't happen in two years.

The whole Green New Deal, I think, scared many people in the energy space to death. And I see many, many institutional players, they were just selling off everything that rhymes with fossil fuels because everything in this area is evil.

And it's creating pretty nice opportunities from my point of view.

So, going forward, I think that – well, if I would say I see oil trading at 80 bucks, I think most people would probably ridicule me. It is very, very much of a contrarian view. From my point of view, I see US shale production – the growth from shale production, let's put it that way – being quite constrained.

We're seeing that the rig count remains depressed. We have seen many years of high grading. I think perhaps we have already seen some sort of peak shale. And we probably would need prices to go to $65 or even $70 to bring back a lot of these wells.

I think that the combination of optimism over the COVID vaccine, falling crude inventories, and the extremely defensive OPEC+ should lift oil prices going forward. So I'm seeing it as one of our biggest convictions. And we're seeing, for the service companies but also for the large producers, we're seeing pretty attractive valuations.

And that's the last thing – when it comes to commodities, we are seeing very, very interesting developments in the uranium sector. We are running one uranium fund for many years now. It's been very frustrating. But now it really seems that, yes – I'm a bit hesitant to say – but that this time might really be different and that this fundamental case for uranium now is kind of seen by markets. So we are seeing some pretty convincing breakouts in the uranium space.

Patrick: Erik, do you have anything to add to that?

Erik: Yes. Let me first thank Ronnie for the credit I didn't quite deserve. I'm very knowledgeable about crude oil trading, and particularly time-spread trading in crude oil.

But, honestly,when it comes to really understanding energy markets, and particularly understanding the transformation which is about to occur in this ESG world into greener energy markets – LNG (liquid natural gas) is going to play a huge role, which I'm, frankly, still just learning about.

So I'd say that learning about the role of LNG and the companies that are going to benefit from that, if you listen to my interview on the Smarter Markets podcast with Thom McMahon, that gives a little bit of insight. But I'm really eagerly looking forward to learning more about that.

As far as the other assets are concerned, I think farmland is going to be super-strategic. We've got – the biggest problem the world faces is overpopulation. There is not enough food to feed everybody. We need that farmland. We need it desperately.

The thing is, if ever there was an asset class that falls into that category of only invest in things that you actually know about, farmland, first of all from my interviews with Artem Milinchuk from Farm Together, I really learned that this is an asset class where you need to know what you're doing. Because they think about diversifying.

There's types of farmland that are for crops like almonds that are really a luxury market that are not essential to feed the world.

And they tend to diversify in certain economic events against the soy beans and the corn and the other kinds of farmland.

You've got to know about the different kinds of soil that are appropriate for different kinds of crops. And there's a whole lot to it and I don't know anything about it.

So it's an asset class that you need active management by somebody that really knows what they're doing.

A lot of people say to me, well, buy the farm ETF. Well, I don't know if that's just an ETF that a bunch of guys are shotgun approaching, just buying farmland without knowing it, or if a lot of thought goes into that.

I'm impressed with the work that Artem and those guys do in terms of the fractional ownership market of farmland.

I think when Grant spoke about farmland he was really talking about the lifestyle choice of living on a farm. That doesn't suit my personal taste. I wouldn't live on a farm.

But as far as owning farmland that's rented to farmers, I think it's an important asset class that I don't know enough about in order to do the investment myself. I would do it through a fund.

Battery metals, kind of the same story there. I think battery metals are going to be super-important.

But the big mistake everybody makes is to not recognize that battery technology evolves just like other technology. Everybody is assuming right now that the lithium ion is forever. It won't be. There's new battery chemistry technologies that are being developed that don't use lithium.

What do they use? Well, I don't know because I don't know enough about it.

I imagine someday I'm going to listen to a podcast where this kind of reclusive genius type with the sort of Chris Cole energy comes on but he's an MIT PhD in batteries and he's running a fund that knows all about the fundamentals of where the chemistry is headed, which metals are going to be important, and knows all about it, and he's running a fund to profit from it. I want to find that guy.

Until I do, what I do know about this is nickel gets used in almost all of the different battery chemistry combinations. Cobalt gets used in some of them. I don't know enough about that market.

But I think that these are things that I'd really rather invest through a vehicle that somebody else is managing who knows more about it than I do.

On the other hand, copper is something where I can just look at, I know we have to build out a new electric grid. I know that electric vehicles, no matter who makes them, are going to need copper. I feel like copper has to be in our future.

But, as Ronnie said, right now at this moment, at the end of 2020, copper has had a really good run to, what is it, Ronnie, six-year highs? Something like that?

Ronnie: Eight-year highs, I think.

Erik: This is not a buy-the-dip moment right now in copper. I wish I hadn't missed that one. So the next time we get a buy-the-dip moment in copper, I want to be really diving on it hard. But I don't feel like right now is the moment to pounce on copper.

Patrick: In the interest of time, we're going to have to wrap things up. I want to thank both Grant and Ronnie for joining us. Thank you, Ronnie.

Ronnie: Thank you very much, gentlemen. It's been a pleasure. And Merry Christmas and a happy, healthy, and prosperous 2021. Thank you.

Patrick: And thank you, Grant.

Grant: Guys, thanks for having me on the show. I really enjoyed the conversation.

Patrick: And Erik… That's a wrap on our holiday special!

Erik: Thanks everyone! We'll be back next Thursday, January 7th with our regular format and a terrific guest.