Jeff Snider: I agree with Janet Yellen and Jay Powell

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Erik: Joining me now is Alhambra Investments Chief Investment Officer Jeffrey Snider. Jeff has prepared a terrific slide deck to accompany today's interview. Registered users will find the download link in your research roundup email. Now if you don't have a research roundup email, it means you haven't registered yet at macrovoices.com. Just go to the homepage at macrovoices.com Look for the red button that says looking for the downloads.

Jeff, I am really really looking forward to this interview with you because you are one of the absolute smartest guys that I know and you particularly understand the dollar funding system internationally. And for any listeners listening who are perhaps new to MacroVoices and are not aware. At macrovoices.com/edu for Eurodollar University, you can find a detailed series where Jeff explains the entire international global US dollar funding system, the Euro dollar system, which I think is going to play a role in today's discussion. The topic of which will be inflation and particularly Jeff, just about all of the smartest macro guys I know have kind of flipped from the deflation camp into the secular inflation camp.

Just last week, we had Ole Hansen on this program describing how the lack of investment in oil producing resources is likely to lead to a very significant oil price shock to the upside in coming years. And of course, oil prices, energy prices are one of the biggest drivers of inflation. I think we've gotten to the point Jeff, where the last two men standing are you and Dr. Lacey Hunt. We're trying to get Dr. Lacey Hunt back on the program. Our producers are working on that. But let's start with our own Jeff Snyder, who knows the Eurodollar system. So well. Why is it Jeff with everybody else saying hey, look, secular inflation is just so clear. There's so many reasons to think that the MMT crowd is going to keep printing money, debasing currency and so forth, has to lead to runaway inflation someday. You're saying no you don't see it? How come?

Jeff: Well, there's two things here Erik. By the way, thanks for having me back on to try to explain what's going on here. Because I think, you know, inflation is the one topic that everybody wants to talk about for very good reason. And when I say you know there isn't inflation happening this year, people are like, wait a minute come on. The CPI is at 6.2% in October, which is the highest been 30 years. How can you possibly say there's no inflation? And the answer is we have to define our terms. We have to we have to be specific about what it is we're actually talking about. And the one part of it is what you just said, Erik, which is, you know, debasing the currency, money printing, and that gets to the heart of what we're really want to talk about. But there's other things involved too, specifically to start with, you know, when we look at the CPI. Is the CPI always talking about inflation? Is it always reflective of actual inflation? Or is there possibly very different underlying circumstances that could be creating consumer price bubbles or consumer price deviation? That's the first thing.

When we look at the CPI, is the CPI really just an inflation index or is it a consumer price index, where consumer prices could be moved by other factors that aren't inflation? And you know, it's understandable why people would think that it's only the other. That CPI is always inflation, because that's really how everybody talks about it. And it's true, not just to the public, but also central bankers and economists. You know, they do all sorts of studies, for example, about the CPI and what's the best predictive model of the CPI because, you know, obviously, we have a good interest in trying to figure out. If we do see consumer prices rising, is it going to last? Is it going to go on forever? Is there any sort of secular trend there? And so these academic models, take a look at the CPI is if every CPI is exactly the same and so their conclusions are usually about what is the best predictor of the CPI? And I don't think that's really the right question to ask because, again, there are different types of situations where consumer prices could be reacting or be responsible from other different factors. Very different factors that lead to very different conclusions and all sorts of different implications.

So if we get into the slides here, that's really our goal here. It was started on slide three is we look at the CPI, we look at consumer prices, what we're really interested in is, is it just consumer prices rising or is inflation responsible for why consumer prices are going up? And what the you know, the academic, economist, you know, mainstream orthodoxy tells you is that there really isn't a good way to sort out predictive CPI values. It's really pretty much a crapshoot. They figured the best methods is by using professional economists who use econometric models. You know, things like the blue chip economic survey because they have a more, at least a decent track record of predicting the CPI.

And you look at some of the other factors, they looked at, you know, some of the other ways of predicting consumer prices. Among the worst they say is financial markets, or bond yields, which is kind of a, what we're trying to get at here, which is do bond deals predict the CPI or do bond yields react only to inflation in the CPI. And so that's really where we're gonna start. If we go to slide four, throughout history, consumer prices have been driven by very different factors at very different times. We're very much familiar with the 1970s and the great inflation. And so we're kind of led to believe that anytime the CPI accelerates, it's because of inflation. As you said before printing too much money, currency devaluation, that kind of thing. But in truth, you have to go back before 1955. But usually, when the CPIs went up, it had nothing to do with monetary printing. It had nothing to do with money printing or excess currency. And a perfect example of that is 1950-51.

We had what was essentially a very classic supply shock, which was, you know, the North Koreans invaded South Korea on June 24 of 1950. Within a couple of weeks, American consumers went to every store they could find and started buying everything imaginable, because they understood that pretty soon, the US government was going to start redirecting economic resources until the warfighting effort when the US finally joined the Korean conflict.

And so it was very much like World War II where consumers understood that the availability of goods is going to be restricted. And so it created this massive bottleneck, where consumers went absolutely nuts buying everything they could possibly buy, while it was still available. At the same time, the supply side was not able to keep up with that demand, because number one, it was a shock or a true shock in the fact it was unpredictable. But also as more and more resources were taking away from the consumer sector and channeled into the defense industries. It was again, supply just could not keep up with demand.

And so in terms of small economic prices, from around July 1950 to February 1951, the Consumer Price Index accelerated to at that time, which was at an annual rate of more than 12%. So it wasn't money printing, it wasn't you know, the currency devaluation even though the Federal Reserve was convinced that it was. The Federal Reserve actually provoked a political crisis to gain its independence from the Treasury Department, because those at the Fed were absolutely concerned this rise in consumer prices was inflationary, therefore, it was going to continue unless they were able to gain independent monetary policy. But they again, they got the inflation thing wrong. They didn't look at the CPI as a supply shock. And the level of CPI puts what we're seeing today to shame. Again, the annual rate of 12%. That was a massive burst of consumer price inflation. But it wasn't really inflation. It was actually just a surprise shock.

Erik: Okay, hang on a second Jeff, because you're making this distinction. You're saying it's not really inflation in the sense of okay, it technically it's not monetary inflation, something else was driving that extraordinary increase in consumer prices that you agree did happen starting in 1950-51. That did happen. You're just saying it wasn't monetary inflation? Is that correct?

Jeff: Yeah, that's what we're trying to get at.

Erik: But here's what I'm hearing. It sounds to me like you're arguing my side of this, because what I see is okay, so maybe it's not monetary inflation. But what I see is we just had a global pandemic, which caused this crazy event that wiped out a whole lot of the US shale production capability. We now have an ESG trend, which says that we're going to vilify extractive industries, whether that makes any logical sense or not, we're going to punish them by not investing in them. So we're not doing any investment in new oil production resources. So all of those things add up Jeff, to say, in my mind, we've got huge increases in energy prices on the near horizon coming our way. That would be a factor that has nothing to do with money printing, but has everything to do with consumer prices going to the moon in the near future.

And at the same time, we have for now, at least, the Democrats control the White House, and the Congress. I just had a listener pointed out to me over the weekend that, you know, probably in 2022, the Democrats will lose control of the Congress. So that'll change things a little bit. But still, all of this MMT stuff is super popular. Lots and lots of politicians want to print more money, and particularly they want to get it out to Main Street not to Wall Street. These all sound like we're putting more money in consumers pockets to drive prices up. And you're right. It has nothing to do with money printing and currency devaluation. But I think that those factors are very much in play to set up a great big secular inflation.

Jeff: Look, I agree with you, Erik that, you know, again, when I say it's not inflation, I'm not saying consumer prices haven't gone up and they might not continue to go up a little bit further. What I'm saying was with without the monetary component. Without actually being true inflation, and I hate using that term, but inflation is a monetary phenomena as we'll get to. Without that monetary component, excess currency if you want to do Quantity Theory. What happens is you have a sharp spike in prices for other non-economic reasons, as you just described, but then the economy is forced to adjust to it. In other words, we're robbing other parts of the economy by having to pay higher prices at the pump, for example. And eventually that's where the inflationary trend always breaks down as it did in 1950-51. Once the consumer stop buying all those goods, inflation stops because it wasn't really inflation.

And if we're going to be paying $200 a barrel for oil, that's going to rob consumers have so much discretionary power that other parts of the economy are going to suffer in a deflationary way that is going to balance out what's going on in oil prices. So it's not going to be a secular inflation trend, because it can't be a secular inflation trend without the monetary component. And if we get, if you fast forward to what I'm getting at here, in the slide deck, we'll go to Slide five now. You know, again there's a difference when it comes to inflation versus other stuff. There's non economic factors. And really, you know, even as the BLS pointed out not too long ago, inflation behaved very differently from around 1955 forward until around 2007 simply because there was the monetary system behind it. It allowed inflation to react very differently than it had previous to 1955, as I'm showing in the 1950 example, which is that consumer prices tend to lump together in these supply shock spikes that never lasted because there was no monetary component. And the best way we can sort out between these various versions of consumer price index increases, what's inflation, or what's it from other non economic factors is simply by using the bond market and bond yields.

So if we go to Slide six, as you can see before 1955, the bond yields stayed very low, which was consistent with the deflationary aftermath of the Great Depression, because we got to remember interest rate fallacy. Low yields denote tight money, not loose money. And so low yields before 1955 were a signal that despite three massive shocks in the CPI, three huge double digit increases in consumer prices. They were only ever concentrated into temporary, short, transitory periods of time, because they were not real inflation, they were simply supply shocks that when they ran their course, consumer prices then returned to the baseline, which, judging by bond yields, these were, you know, non-monetary inflation, not money inflation, so it's not real inflation. That all changed around 1955. This euro dollar system introduced, got introduced in various ways. And it started to leak back into the domestic United States system. And look what happened, lo and behold, the bond markets sniffed out the inflation before it ever showed up.

And if you go to Slide seven, you can see the bond yields were starting to rise years before the great inflation, the actual great inflation start, which the great inflation I think pretty much everybody knows nowadays was a monetary event. It was exactly the classic case of too much money chasing too few goods, and bond yields were absolutely spot on throughout not just the initial period. But if you go to Slide eight, you can also see how bond yields predicted the ups and downs during the Great inflation themselves. And what's interesting is not only are bond yields at least you know, months ahead, if not years ahead of actual monetary inflation. Again in 1973, we had the oil price shock with the OPEC embargo, which bond yields correctly saw as that's another supply shock that's being piled upon this underlying monetary inflation that had already driven yields upward and already driven CPI upward in a sustained manner. So what the bond market is telling you through this first half in the second half of the Great Inflation is that is a very useful tool for sorting out what is the money supply problem, the real inflation versus what is these non-economic factors. And if they're not economic again, what are long term bond yields all about was Irving Fisher said more than a century ago, long term bond yields are growth and inflation expectations.

So even if there's a secular non-economic reason behind consumer prices, then long term bond yields would see that it somehow is, okay, that's something I got to factor if I'm owning a 10-year US Treasury and I expect non-economic consumer prices to be accelerated and some secular trend to continue for 10 years, then I've got to factor that into how I'm viewing my holdings of US Treasuries. So if the Treasury market says whatever's going on in the CPI is not going to affect the long run, then the bond market is essentially discounting these different factors which lead to this ability to sort out different CPIs one from the other. Is it monetary? Is it actual inflation? Or is it something else that isn't going to last. That isn't going to impact the long run? I think people can probably understand where we're going with this. But flash forward to slide nine, we're getting into the 21st century. And again, the bond market has done a very good if not perfect job of sorting out what CPIs represent monetary inflation, which are just transitory supply shocks or transitory shocks for other factors.

Erik: Okay, Jeff, I just want to get this straight because it sounds to me if I plan to have you back on this program one year from today, like we've kind of got a setup where I might say, Jeff, you said there was gonna be no inflation but now gasoline prices are $7.23 a gallon and you might say, Yeah, but that wasn't inflation. Is that where we're headed?

Jeff: It sounds like a cop out, doesn't it? But yeah, you're right. That's what we're saying is the bond market has looked at the 2021 CPI spike and says this is not money printing, this is not inflation. This is something else. And you're saying that there's something. You're agreeing with me right Erik? You're saying that I agree, this is not money printing, this is not... This is...

Erik: I agree, this is not strict monetary inflation. But I still think that an energy led price shock is coming, which is going to dramatically increase first energy prices, and then almost everything else has energy as an input cost. So the price of everything else goes up. That results in even more unhappiness with lower income consumers particularly. And it leads I think, at that point to money printing, real monetary inflation as a government response. The way they respond to people can't afford that $7 gasoline is they print up a bunch of money and give it out as handouts or transfer payments of some kind to support the economy. And if you listen to what Joe Biden said about inflation, he said, listen, don't worry about it. Because we're going to pump so much money into this economy, it's not going to matter. And everybody who understands inflation rolled their eyes and said oh, my God, I can't believe he said that.

Jeff: Well, they don't understand inflation.

Erik: Take him at face value. What he's saying is what they're going to do in response to inflation, excuse me, what they're going to do in response to consumer price increases, particularly around energy is they're going to generate real inflation. They're going to print up a whole bunch of money, and you're going to get the inflation that you're saying is not coming.

Jeff: The bond market says it's not happening. In fact, the bond market is unequivocal about how such a low probability that it is it's not even worth paying much attention to. Look, I mean, I just went through more than what 75 years of history and it goes back further. We go over a century of history when the bond market has been spot on. Time and again sorting about long run consumer price changes, what is inflation, what is not inflation, what is the non-economic factors we need to pay attention to over the intermediate, long run and which ones we don't? And right now, the bond market is unequivocal saying, yeah, Biden may say these things, but it's not going to happen. And there's a very specific reason it's not going to happen.

If we go to slide 10 as Milton Friedman said in 1963 as he was touring India, inflation is always and everywhere a monetary phenomenon. Now, he didn't make the statement as sort of a I'm just conjecturing here or this is a theory I had bouncing around my head. He made the statement, he just wrote a monetary history. So he made the statement as an acknowledgment of empirical fact in reality. So inflation is everywhere a monetary phenomenon. In nearly 60 years since he said that everything is only validated what he was saying, especially the later 60s and 70s of the great inflation that, look, we know what inflation is, inflation is money. And inflation means long run problems. And if it's a long run problem, the bond market is going to find out about it, and it's going to trade upon it. And if the bond market says there is no long run inflation here. There is no money printing then that's a pretty good historically validate a gauge that says no matter what's going on in the short run, we're going to shrug our shoulders and ignore it because there are other problems that supersede what's going on.

And as I said before, yes, we could have gasoline prices become extraordinarily expensive and painful. But all that's going to do in the absence of money printing and currency devaluation. All it's going to do is create other economic problems and other parts of the economy that are going to balance it out. So that these so called secular trends never become secular in the first place. Again, this is the judgment of the bomber. It's not me saying this, I'm telling you what bond yields are saying, and again, this has been a reliable, historically validated, empirically established indicator, which right now is saying, yeah, we hear all of the stuff that you're talking about. We see oil prices going up, we see the CPI at 6.2%, and used car prices being 1/8 of the increase in the October CPI. But that's not inflation and inflation is what we'll have to look at over the long run, not the short run.

Erik: Okay Jeff so we're still in agreement that there is a good chance that energy prices in particular go to the moon from here, but it's not inflation, and then that gets transmitted into the rest of consumer prices going up dramatically but it's not inflation...

Jeff: No, it's not what I am saying at all.

Erik: ...despite well, wait a minute. I mean, it sounds like what you're saying. And then what I'm saying in reaction to that is the President of the United States went on television and already announced his intention of how he's going to respond to inflation is by throwing money at it. So that says to me, they're going to print money.

Jeff: No, they're not going to print money. They don't know how and again, we've heard all this stuff before. The numbers have gotten bigger. I mean, we're having the same arguments we had in 2009 and 2010. It's really just the same thing. And the reason the bond market skepticism is because it's been empirically validated time and time again. Yeah, who cares what Joe Biden has to say he doesn't control money. That's really the whole point here is that inflation is all about money. And I'm not saying energy prices will go to the moon. I'm saying energy prices can be temporarily elevated in extremely painful ways. But that pain that consumers will feel because of rising gasoline prices will rob other parts of the economy vitality and economic activity such that you'll have one sector of the economy that's nominally growing massively because of inflation and prices, because prices are going up but that is going to depress other parts of the economy. And over time, neither the energy trend nor the economic trend can survive that kind of split personality. You can't have rising energy prices and have economic growth continued for very long, because, again, history has shown what happens in those situations is you end up with a really nasty recession or contraction within very short order. And that necessary recession and contraction is nasty as it gets reestablishes a very different consumer price environment, which is not inflationary.

In fact, it ends up being deflationary. Consumer prices, including those of energy gasoline will fall very quickly when we get into that sort of situation. So if energy prices continue to go as they are now, absent of the money printing, which is not there. I don't care what Joe Biden has to say the market says unequivocally, the guy has no clue. Just like Jay Powell has no clue. Just like economists don't have any idea what goes on in the monetary system. The bond market is telling you, unequivocally, no matter how high energy prices get in the short run, it's not going to stick around for the long run, because it just cannot. It's not actual inflation. It's a temporary trend that's based upon, as you said, supply factors and supply shock factors alone. And because of that, it's not an economy wide, it's not a global situation that's going to last for very long, because it can't. Without the money printing, you can't get it.

Again, Milton Friedman in 1963, this was not you know conjecture, it was empirically based. And the best way we have of telling us what is going on in the monetary system, what is going on in the real economy, not just today. But what is the best type of information or real time argument that we can make about what the future is likely to look like when you know, the 10-year US Treasury is now what 1.6% Even though it's up over the last couple of weeks, I mean, that is an incredibly low rate. And I haven't even got to real yields yet, which are unbelievably ugly. So what the bond market is saying, this is not me, this is the bond market is saying and the bond market, by the way, that's the people who actually do the money in the global Eurodollar system. So they're already telling you, the money's not there, the money's not going to be there at any real probability for the future. And so this is an inflation, this is just like the pre-1955 supply shocks where once they run their course, they will run their course and the CPI will eventually go back down and energy prices will eventually go back down. Whether or not that's triggered by a recession or not, that remains to be seen.

But we're already seeing some signs that that's the case. You know, this global growth scare that's emerging, even in the mainstream narrative. We're seeing a lot of these, you know, transitory effects as transitory, because without the money printing, it just won't last. And that's really, you know, moving forward in the slide deck here, from 13 you know, to 14 to 15, 16, 17, and beyond. What I'm showing people is that, what is the monetary system saying. What is it looking at, and the theme this year has been, as you point out Erik, it's been inflation, inflation, inflation and for people to pay attention to the Federal Reserve or even broadly monetary conditions. It's been too much money, too much money, too much money, whether the bank reserves, the reverse repo, any number of things. Yet, when you look at these indications, not just the bond yields. And it's not just US Treasuries, either. These are bond yields all over the world. But we have tick data, we have Chinese data, we have all sorts of data that tells us that it's not inflationary money in 2021. It's the opposite. We have deflationary conditions rising throughout this year, which eventually lead into a some sort of downturn, if not global recession, which will end any secular price trend and energy and everything else real quickly. So the entire monetary system and the markets that trade off them. Again, they're unequivocal and saying that whatever's happening in this consumer prices right now is not going to last. It can't last.

Erik: Jeff, I have to comment on slide number 14, because boy, every doomsday blogger on the Internet back around 2009-10-11-12 was writing the same story, which is you better watch out because what's coming is foreigners. Foreign holders of US Treasuries are going to divest their US Treasury holdings. When that happens, it is going to outright crash the US Treasury market, we're going to have hyperinflation. My favorite word that people love to misuse of the US dollar. It's coming as soon as those foreigners divest their treasury holdings. Well, guess what? As you show in this chart, they were exactly right that foreigners were going to divest their treasury holdings at wholesale just outright.

Jeff: They were dumping, Yeah, they dump them!

Erik: Dumped them! And there's no hyperinflation and I don't think that the phenomenon that we're seeing right now as a result of that, what happened there? And what does it mean? Why What, why didn't the dumping of foreign holdings of US Treasuries cause a crash in the bond market back when you saw this activity happening, and now we're getting some inflation at a time when it looks like foreigners are actually starting to reinvest at least slightly in the treasury market, that seems backwards.

Jeff: it is backwards and it's a fundamental misconception of how the global monetary system works. And, again, it's understandable why people would say this, at least start to think about it, because it sounds intuitive, right. And if we've been told for years that without foreign buying of US Treasury specifically, but also US dollars more broadly, that those markets would be toast. Without the foreign demand for treasuries, screw it, the treasuries are going to be worthless, because we need foreigners because of people's theories on capital accounts and things like that. But in the Eurodollar system, as you can see, clearly in the chart here, what actually happens in reality is that when there's more dollars in this offshore monetary system, flowing all the way out, you know, through the vast corners of the global system, what happens is, they end up in official hands of the central bankers or finance ministries and those central bankers and finance ministries, they like to create a pile of reserves, which they think are some form of insurance against a $1 shortage.

In 1997-98, you know, Asian financial crisis type situation, and they like to invest those dollars in low risk, high liquidity assets, like US Treasuries. So those things are always related. More dollars flowing in the Euro dollar system, more dollars end up in foreign official hands, more dollars end up being reinvested by these foreign officials in US Treasuries, in particular, also agency GSE debt as well. So as you can see, you know, foreigners tend to have problems when there's dollar problems in the global Euro dollar system that started in August of 2007 and continued in 2008, which was nothing more than a global dollar shortage. And if you have a global dollar shortage, obviously, there's fewer dollars flowing through these foreign central banks, which means they can't buy as many treasuries as they might have beforehand. And so, in the rare in more extreme situations of a $1 shortage, these foreign reserve managers actually have to sell their treasuries to try to make up their dollar shortfall that the Eurodollar market isn't doing. That we have tightness in the Eurodollar market that causes problems for local banks and central banks sell, they liquidate their reserve assets to try to supply dollars temporarily to the market.

And so by the time we get to 2014, that global dollar shortage from the global financial crisis proved to be a series of crisis, a series of shortages, not a one off limited in 2008-2009. But 2014 wasn't a particularly bad one that especially hit emerging markets like China, and the Chinese and other foreign countries decided they needed to, they needed to react to this growing dollar tightness by selling their US Treasuries. It wasn't because they hated Treasury. It wasn't because they hated the dollar. It wasn't because they hated the Federal Reserve's printing money. In fact, they were reacting to the opposite of money printing, they were reacting to tight money. So whenever you see foreigners, particularly central banks, and in foreign officials institutions selling treasuries, what that means is that there's a tightness of dollar funding outside the United States, as well as inside but mostly outside the United States. So it's a very good signal of tight money.

And what you can see in 2020 and 2021, is that yeah, we had a little bit of reflation up until around April of this year, and ever since then has been going the opposite way. So we've had tightening in the Eurodollar system, which has led to, again, renewed a little bit of renewed selling, but you know, once the selling starts, it becomes difficult to stop. So it's following US

Treasuries or selling treasuries. It's not, you know, it's not a negative for the Treasury market. It's a negative sign for the monetary system. And as you can see those things go together, because what have Treasury prices done since 2014, just like the dollars exchange value, both have gone up dramatically, because we're talking about deflationary money embedded within all of those processes.

Erik: Okay so let's talk about what you think is going to happen because it sounds like what you're saying is you agree with me and Ole Hanson that the lack of investment in producing oil resources is likely to lead to a oil price or energy price shock, which will probably be transmitted into a broader consumer price shock, but you're saying okay, that's not monetary inflation, and it's going to result... Essentially it sounds like it'll bring on a recession, which is deflationary, and everything corrects, is that what happens or what happens from there?

Jeff: Yeah, I think the energy prices make a bad situation that's already bad, makes it that much worse and more painful. Because again, You know, consumers are paying more at the pump, and they're doing so... It's not like their wages or their pay is rising to match the prices that they're paying. And it's not just, you know, obviously gasoline or energy prices, we see it in all sorts of supplies shocked driven markets, just for regular consumer goods, for example, you know, automobiles another perfect example, which, you know, I have a couple of slides for that. But yeah, that's what the market judgment is saying. We have on the one hand, not only do we not have the money printing that makes it in monetary inflation or inflation going forward, we actually have the opposite trend starting to develop, which is deflationary or tightness in the monetary system. We see this in any number of indications, data in markets, including, by the way, inflation expectations in the TIPS market.

If you go to slide 18, slide 17 you see the rising dollar. Rising dollars always a negative sign, that's always a sign of tight money, just as it was in 2018 when the Reserve Bank of India's Governor Urjit Patel got to, you know, saw funding dry up in the dollar markets so badly, while everybody was convinced that was going to be an inflationary period, he saying, what, the hell, you know, out here in the rest of the emerging markets, dollar funding has evaporated. That's a rising dollar you equate with tightness in money, as you would something's going on the Chinese People's Bank or China's balance sheet, which are, you know, dollar deposits are being demanded from their local banks. And even in just you know, TIPS market. We see a surge in short run inflation expectations, but yet the TIPS curve, or the inflation breakeven curve itself, is upside down. And lately it's upside down in absolutely record fashion, which is the market saying short run CPI long run less CPI, which you get to slide 19, which is longer run inflation expectations, the five year-five year forward rate, and you can see even today, even as short run inflation breakevens in the TIPS market are through the roof.

Long run inflation expectations remain in that same post 2014 state that like official selling their US Treasuries is more deflationary or disinflationary than it is inflationary. So every part of the Treasury market as well as the global bond market is uniformly saying, this is not inflation, and whatever's happening in terms of the CPI. It's not going to last very long. And that's a term of art and you're right to you know, that's sort of a cop out to Erik, because you say, well, it's not going to last very long. And the question immediately is, well, how long is it gonna last? If you're saying it's temporary or transitory? How long might it last? And the thing is, we don't really know. But the market is almost positive, it's unequivocal that it's not going to last. And, you know, historically speaking, some of these supply shocks could go on for a year or more.

Erik: Jeff, as I look through the next few slides in the deck, I see that you're saying a lot of the same things that I'm saying in terms of there are factors which you're right, they're not technically monetary inflation, per se. But I think there's going to be an energy price led consumer price increase, and it's going to result in a broader, you know, the cost of energy is an input cost to almost everything. So broader cost of everything from shipping to widgets to you know, office supplies is going to go up. And I see all of that coming. You're saying that technically, that's not being driven by monetary inflation. But I'd like to challenge your conclusion that what it leads to, is okay, you said people's wages are not going up. So it's going to end up being deflationary because the economy can't afford it. And those high energy prices cripple everything?

Well, let's try a thought experiment. What if we take the President of the United States and his word, he says he's going to throw money at the problem of inflation, which is not usually what most textbooks tell you to do with inflation. But I think we should take him at his word. Suppose that what they do is they say, look, we got to let inflation run hot, because we've got to do something to devalue the real purchasing power of the national debt. We've got to get the national debt under control. The way to do that is to inflate it away. If we inflate it away, it's going to damage the lower end income people in society the most. So hey, let's use this new MMT stuff and just print up a shitload of money and hand it out and say, look, yeah, we're gonna let inflation run hot. And we'll identify some boogeyman overseas who doesn't look like us. Hey, OPEC+, it must be their fault and let's blame the Russians too. Because you know, Russians, they're to blame for everything.

Jeff: And the Chinese.

Erik: Oh, yeah, that's right.

Jeff: You have to get the Chinese in there.

Erik: It's the stinking Chinese and they're stockpiling of oil. That's got to be part of this. And those stinking Russians and those OPEC, those Arabs, ooh, bad guys. Okay, we've got lots of Boogeyman. We've got lots of people to scapegoat and blame. And what we're going to do is say the Biden administration has got your back. We're gonna take care of hardworking Americans by printing more money and exacerbating it. Maybe it wasn't monetary inflation when it started, Jeff, but I have complete confidence in the people in Washington DC to respond to this by saying, we're going to print up enough money to turn it into monetary inflation. And what we're going to do is a whole bunch of transfer payments and handouts in order to buy off the populace so that they don't, you know, blame us for this. We'll blame the monetary inflation for people who have savings that are losing the value of their savings, we'll blame it on foreigners who don't look like us, there's plenty of those to choose from. And we'll just print money like it's going out of style with MMT in order to basically provide government transfer payments in order to solve that problem that doesn't lead to a deflationary result. And that's where you get to, I think, potentially not only secular inflation, but maybe even the beginnings of runaway inflation, not quite hyperinflation, but it could really start to run away to the point where they can't control it. That's what I see on the horizon. What's wrong with that theory?

Jeff: Well, again, I go back to the bond market. The bond market hears and it has discounted everything that you've just said, because the bond market isn't some kind of, you know, some centralized person, some enlightened philosopher in the room staring at computer screens and listening to chats and things like that. The bond market is everywhere in everything. It's essentially a broad based information system, sort of like big data that is situated very close to the real economy. It actually is the big banks who run the monetary system as it is currently constituted, and it has looked at your situation looked at your scenario, and it is pricing it as essentially a 0% chance of happening. Well you never say never. So maybe it's a you know, a 1/10 of 1% chance of happening. But as I said in earlier, we have this information stream. This information sorting mechanism, that tells you something very specific about the future. It looks at the long run, the same long run, that you're looking at Erik, using the same information that you're using. Pricing, these, you know, hypothetically pricing these scenarios in the same way that you are. And it's saying there's not a real realistic chance. The money isn't there.

Erik: Well, wait a minute, why is the bond market saying that. Why is it not that the bond market is saying well yea all that stuff I just described could happen. But as part of that, the Federal Reserve's going to continue printing money to also buy bonds in order to keep interest rates...

Jeff: It doesn't print money. It gets back to do you understand what actually printing money means, because I don't think people do?

Erik: Okay, well, let's not get hung up. Let's assume that there is another big round of quantitative easing, so that we're creating bank reserves and that that is depressing the long term interest rates and keeping those bond yields down, so it's suppressing it.

Jeff: No no no, it is absolutely not, that is not happening, and that has never happened. bond yields react most of the time opposite of quantitative easing. Erik, you got to just look at a bond yield chart. And it shows you that when the Fed is buying bonds, interest rates tend to rise not fall. And when the Fed stops buying bonds, it's not just the Fed you can look at the ECB. Look at German bond yields in 2018 and 2019. German bond yields were falling as Mario Draghi stopped buying German bonds, they kept going down. The Fed does not control the industry and the Federal Reserve nor any central bank is controlling any interest rates right now. They are not artificially depressing the bond market. That's not how this works. And you could even ask the central bankers themselves. Read the literature on quantitative easing, it all uniformly says bond market sets the interest rate and the yields in the real economy. And yields, as we all know, are about growth and inflation. So you can't just wave your hand and dismiss these low yields as some kind of artificial signal that the Fed wants to send. That it's artificially depressing yields. That's just not happened and it hasn't happened. The bond market is independently assessing growth and inflation opportunities as it has since there's ever been a bond market. And it's saying, we see all of these things and we agree in uniform, that we don't see consumer prices breaking out some secular trend for reasons of money or not money.

Erik: Okay so your argument is basically the bond market is essentially always right, or almost always right, and how accurate does the history in your estimation, prove that out?

Jeff: As I just went through in the entire first half of a presentation, it's pretty damn accurate. You know, the bond yields started rising in anticipation of the great inflation, The Great inflation. So we're moving into a second grade inflation and bond yields are not moving in anticipating a second grade inflation. Why not? What has changed what has changed? And you can't answer the Federal Reserve because that's lazy analysis Erik. You haven't even looked. All you need to do is look at a yield chart and to know that the Federal Reserve does not have much of an impact on on yields. It's exclusively growth and inflation expectations that are being set in the market. And as I said before, the market is not some narrow click that has, you know, that's trying to price some political agenda. It is a very broad based global monetary system. It's the market that trades closest to the global monetary system that tells you what's going on in terms of money. What's going on in terms of the real economy? What everybody thinks is going to be happening in this marketplace for the foreseeable future.

Now, it's, of course, it's not perfect. It's not it's, you know, it's not a crystal ball. But historically speaking over the last century and more, it has been the best, most useful, most accurate tool for assessing inflation potential, not CPIs. But inflation potential. And that's what we're really talking about here. And so yeah, the bond markets judgment right now, is that for the last year or so that we've been hearing about all this stuff. For the last year that we've seen the supply shock develop, and for now that we have these 6.2% CPI, that's the highest in 30 years, the judgment hasn't changed. The bond market still says, this is not economic stuff. It's painful, it's causing enough pain on top of a bad deflationary situation that is likely to result in an adjustment in the real economy that nets out over time to not inflation.

Erik: Okay. So to summarize, you're saying that you do agree that a significant increase in consumer prices led by energy is very possible, but because the bond market is telling us that it is not anticipating that turning into monetary inflation, you think that Janet is essentially right, that it is transitory, it's going to happen. We're gonna see that big energy lead increase in prices, but it's not inflation, and it's all going to reverse because it's going to lead to pressure on the economy that takes us the other direction.

Jeff: Yeah. I love how you framed it that way, putting me on the same side as Janet Yellen.

Erik: That was pretty evil wasn't it.

Jeff: Yeah, I know. You had to smile a little bit when you did that. No, it makes me tremendously uncomfortable. To be you know, to say I agree with Jay Powell and Janet Yellen. But you know, they might be right for the wrong reasons. But yeah, and again...

Erik: Ok we got a title for this episode. “Jeff Snider, I agree with Janet Yellen and Jay Powell.”

Jeff: Clickbait clickbait! No, no, no, no, but it's sad but true. And I think, you know, she's right for the wrong reasons. And your summarization is correct. I think we have the supply factors, we have a classic supply shock that's developed. And especially over the last couple of months, it's becoming extremely painful. And it becomes more painful by the day and by the week, that eventually without the money printing without actual money in the economy. In fact, we have deflationary money in the global economy. That's why the bond yields are so low, it's not the Fed, it's the fact that the bond market is saying, again, broad survey of actual real time economic conditions that whatever happens in energy markets, it's not going to lead to runaway secular inflation.

Erik: Jeff, I can't thank you enough for another terrific interview. But before I let you go, I want to touch on a few of the other things that our listeners can do to follow your work. The first, if you haven't done it already, is definitely listen to Eurodollar University, which is several hours. I've forgotten how many of Jeff's analysis and explanation of how the offshore wholesale US dollar funding system really works. And I've got to say in all of the interviews that I've done on macro voices over the years, we've got a lot of opinions, a lot of viewpoints, and there's always somebody coming back saying. Oh, that guy doesn't know what he's talking about. Ole Hanson doesn't even know what he's talking about. David Hay doesn't know what he's talking about. And usually people come back and say, Jeff Snider, that guy's over my head. I'm not sure what he's talking about. So I haven't heard the argument that says Jeff's wrong. I've just heard the the.. we don't know what he's talking about. And I think Eurodollar University is a great place to start. But also tell us a little bit more. You and our good friend, Emil Kalinowski are producing your own podcast. What's that about and where can people follow it?

Jeff: It's really an extension of what you and I started out doing Erik, which is Eurodollar University trying to explain the monetary system. And yea we have our own podcast that you can find on YouTube. It's called Eurodollar Universitiey Making Sense, where we try to make sense of money printing, CPIs, bond yields and all you know, Federal Reserve policy and all these other things. Again, you can find it on YouTube, you can find it on wherever you get your podcast downloads to.

Erik: And that all builds on the work that we did at macrovoices.com/edu, which is really the very first place to start. And also, of course, you guys manage money at Alhambra Investments. You can find information about that at Alhambrapartners.com. Jeff, I can't thank you enough. Patrick Ceresna and I will be back as MacroVoices continues right after this message from our sponsor.