The Coming Economic Crisis

February 13, 2021

by Peter Glickman

The Chinese character for crisis

Introduction

We live in a time of rapid change. It can be frightening or exciting; frightening if you are unprepared, exciting if you have planned for it. World-changing, economic events are coming. I'll show you what is behind them and bring you to understand, not only how to survive the crisis, but how to flourish in spite of it.

You have seen brick and mortar stores closing. Covid has played a part, but it has only accelerated the crisis. It was happening before Covid.

Financial freedom appears to be moving further and further away. It is harder to provide for children's college tuition, second homes, and retirement.

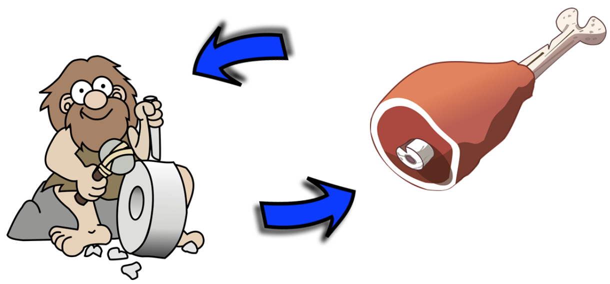
The prices for food, gasoline, entertainment and housing have been growing steadily over time. According to the US Government Bureau of Labor Statistics, you needed $680.73 in February 2020 to buy what $100 would have bought in February 1970! Put another way, the dollars in your savings account lost 86% of their value since 1970.

What is the source of these things? Can you reverse them? Let's look at the fundamentals behind this crisis.

A brief, but interesting history of money

There are two parts to the definition of money. The first is that money is something that Is broadly accepted as payment. This is called a means of exchange. An employee agrees to accept money for his work. A merchant agrees to accept money for his goods. The second part of the definition of money is it is a store of value. It will hold its value over time. Fresh eggs spoil. A new car depreciates.

Trade is based on exchange and exchange is most often accomplished with money. *currency* is another word for money. The root of *currency* is *current*, which emphasizes the *flow* of trade back and forth.



Barter

Trading one item for another is called barter. Before currency, a chicken farmer had to trade his fresh eggs for the other things he needed, like bread, shoes, etc. However, the rancher would not accept 1,000 fresh eggs for his new calf. They would go bad long before he could eat them or trade them to others. The problem with barter is that you have to find someone right then who wants what you have.

Gold dust

Gold was the next great advance. It was something everyone would accept and would not spoil (lose value) over time. Gold was stable and didn't spoil. Now the chicken farmer could sell his eggs for gold, accumulate enough of it, and buy a calf. But gold nuggets and bags of gold dust aren't all equal. It was not possible for the rancher to say he would sell one calf for 10 gold nuggets because the nuggets are not all the same.

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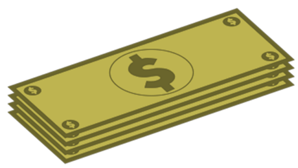
Minted coins

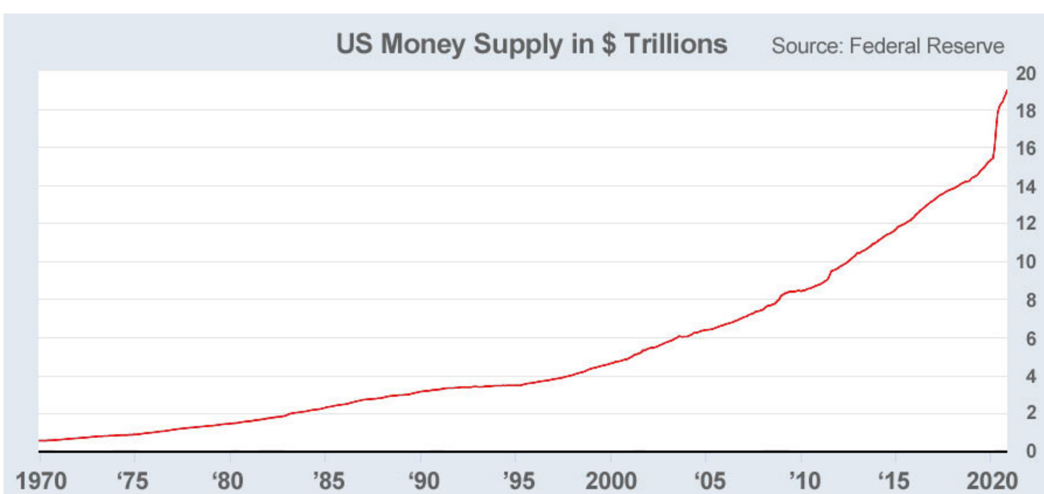
The invention of minted coins to standardize the weight of gold and silver was the next advance. The picture of the king on one side and the stamp of the royal mint on the other guaranteed the coin was gold and the standard weight. Now the rancher could tell the farmer how many gold coins he wanted for his calf. This was a great advance for trade. However, if you were buying a very expensive item, like a castle, it required many wagons of gold coins and a troop of soldiers to protect the wagons.



Paper money

Paper money solved that problem. The man who wanted to buy a fortress could write an order to the man guarding his gold (his treasurer) to pay the agreed upon amount of gold on presentation of the order. This was later expanded to money orders, checks and paper money.

From 1863 to 1933, US dollars were called gold certificates and promised the bearer actual gold. In 1933, the U.S. government ended the exchange of dollars for gold for US citizens. This was done so the government could print more paper money to handle the Great Depression. Sound familiar? Notice the vertical rise in 2020 when the government printed more money to fight the economic effects of Covid.



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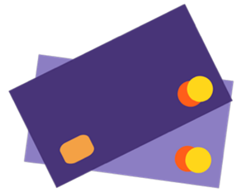
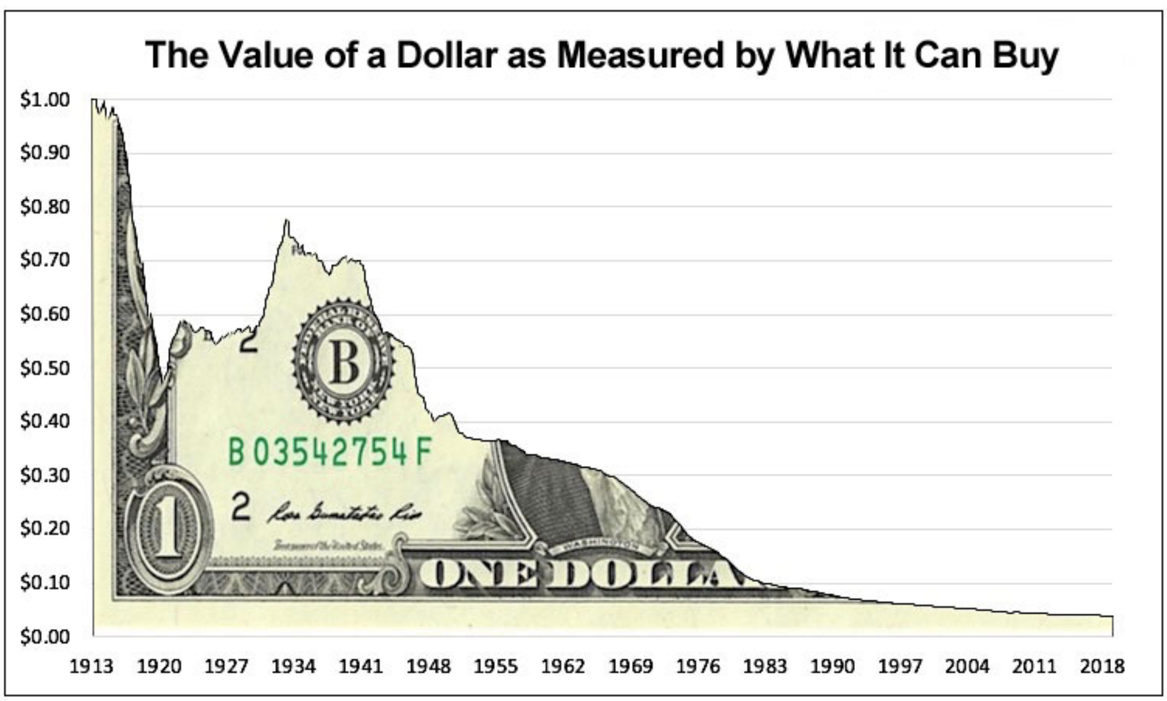


Credit cards

Paper money was very convenient, but what if you needed to buy something like a house that required more money than you could easily carry? Enter the credit card. One small card in your wallet could now represent small or large amounts of money and was protected by a personal identification number (PIN).

The problem with coins, paper money and credit is that they are all under the central control of the king or central bank. In a perfect world, this would be no problem. However, some might say that in today's world, the king imposes too many taxes and bankers charge too much interest on their loans. Or the king might forbid moving large sums of money out of the country or the banks might reduce the interest they were paying depositors or … even take their depositors' money to bail them out of bad investments!

Inflation



Data Courtesy: St. Louis Federal Reserve

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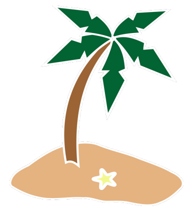
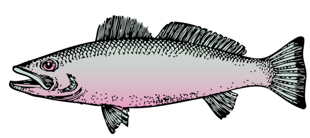
The process of inflation is simply money becoming worth less and less. This can happen fast (high inflation) or slow (low inflation). You see this in a house that was worth $100,000 thirty years ago and is now worth $450,000. Inflation occurs when there is an increase in money without an increase in the things it can buy.



For example, let's imagine you live on an island with 10 people and everyone lives on fresh fish from the sea and suppose you want a pair of sandals. Unfortunately, the sandal maker only eats a few fish each day. If you want to buy sandals after dinner, you may find the sandal maker is not hungry.

The king of this island is a very smart man. (Some say too smart.) So, he created paper currency in the form of IOUs. Each IOU promises the person presenting it one fresh fish. (The king's bodyguards fish when they are not guarding the king. So, the king has extra fish.)



Now, if you need sandals after dinner, you can pay him with IOUs. He can spend those IOUs later to buy fish for a party he's planning for his friends.

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On the same island, is a hut builder. Over the years, he has built a lovely two-story hut on the beach with a view. The king wants this for his palace. Unfortunately, the hut builder wants more IOUs than the king has fish (which are what the IOUs promise).

One morning the king wakes up with a brilliant new idea: he will write more IOUs than he has fish! (I told you some people thought he was too smart.) At first, everything was fine. The king got the hut with a view and the hut builder received IOUs for enough fish for many parties with his friends.

However, after the hut builder's parties, he still had IOUs left over. One day, he decided to buy a pair of sandals. Unfortunately, another islander was already in the process of buying the only finished pair left. Since our hut builder had many more IOUs than the other islander, he offered twice the usual number of IOUs.

Seeing how easy it was to get more IOUs, the sandal maker increased his sandal prices. Seeing this, the hut builder increased his prices and so on. Our little island was now the latest victim of inflation.

Our modern world

Leaving the island behind, let's look at our modern world. The government of a country may want to increase its army, but not have enough money. So, the government borrows several million dollars to do that. A year later, when it is time to pay back the loan, the government wants to build a new dam. Now they have a problem. Should it build the badly needed dam or pay back the loan?

Unfortunately for the citizens of this country, the treasurer of the country is the grandson of the island king. So, he "knows" what to do: just print more money. Then the government can build the dam and pay the loan. The result? The dam gets built and the loan gets paid. Unfortunately, the money of the country is now worth less than before. It buys less, so the citizens of the country suffer as prices rise. When the king borrowed the money to build the army, it cost a family $400 a week for groceries. After printing all the extra money, the SAME groceries cost $600.

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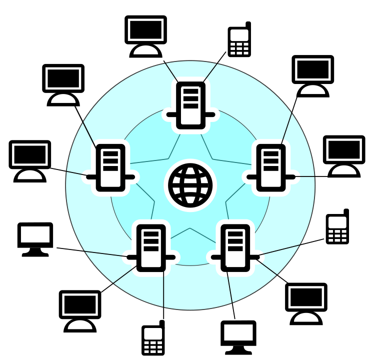
Now let us look at a real example from history. To finance the Revolutionary War in 1776, the American government authorized $4 million Continental Dollars and backed each one with one dollar of gold or silver. By November 1779, $226 million had been printed and it took $40.00 in paper to buy what one dollar would have bought in 1776. The value of the Continental Dollar fell 97.5% in three years.

Now that you understand inflation, how can you prepare to flourish during it? Is there a form of money that withstands inflation? Yes, there is and it is only possible because of the Internet!



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Internet money?

What would Internet money be?

1. It would have to be digital because the Internet is composed of digital computers. This is no different than credit cards or online banking.

From our earlier definition of money, it would also have to be:

2. Something we broadly agreed to accept as payment and
3. Something that holds its value over time and doesn't spoil or depreciate.

What is cryptocurrency?

The prefix *crypto*- means hidden or secret and comes from the Greek word Kryptos meaning hidden. *Cryptography*, for example, is secret writing, or secret codes. Governments use cryptography during war so the enemy can't read where and when attacks will come.

Cryptocurrency is digital currency that uses cryptography to ensure that can't be faked or counterfeited. This is because each cryptocurrency "coin" contains a unique mathematical code guaranteeing that it is genuine and not counterfeit.

You may have heard the word *blockchain*. A blockchain is built of blocks of digital information. Each cryptocurrency adds blocks at its own speed, for example Bitcoin adds a new block every ten minutes. Each block records specific information of the previous 10 minutes: new coins added, who owns them, and any coin transfers. The next block records the same information for the next 10 minutes and so on.

Each block also contains a unique cryptographic code identifying that block. The next block uses the code from the previous block to create its identifying block and so on. This is like Lego blocks where the original identifying code is the hollow base and the new code is the set of raised circles they interlock with. The reason they are chained like this is to prevent someone trying to insert a false, counterfeit block.

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The blockchain was one world-changing idea incorporated into Bitcoin. There was another. There are thousands of computers connected to each other in the Bitcoin network, each one contains the entire record of the whole blockchain and a number of them have to agree on the data before the block is added to the chain.

So to counterfeit a Bitcoin would require recreating the entire the entire blockchain (669,879 blocks as of February 9, 2021) on thousands of computers within 10 minutes! As more blocks get added and more computers join the network, this task becomes more and more impossible. And this is why people trust Bitcoin.

How well accepted is Cryptocurrency?

Bitcoin is the oldest and largest cryptocurrency and is the most accepted of all. As of February 9, 2021, the cryptocurrency market (more than 8,000 different coins and 33,000 markets) is worth more than 1.3 trillion dollars. Bitcoin alone trades more than 210 billion dollars traded each day. With a total value (market cap) of more than 850 billion dollars, it is worth more than the largest US companies, such as Tesla, Facebook, Visa, Wal-Mart, or JPMorgan Chase.

In August 2013, the German Federal Ministry of Finance recognized Bitcoin for commercial and private payments. In November of that same year, Bitcoin transferred more money than Western Union. In April 2017, Japan legalized Bitcoin for payment of debts and investment.

In December 2020, Massachusetts Mutual Life Insurance Company, a 168 year-old insurance company, purchased $100 million in cryptocurrency for its general investment account.

In January 2021, Tesla purchased 1.5 billion dollars of Bitcoin to replace US dollars in its treasury. Harvard and Yale have been buying cryptocurrencies in their endowment funds for at least a year.

The largest publicly traded business intelligence company, MicroStrategy, bought $250 million worth of Bitcoin in August, followed by $175 million in September. Then on February 3 and 4, 2021 the CEO, Michael Saylor, held a Bitcoin for Corporations program with 8,000 attendees many of whom were fellow CEOs. His theme was that Bitcoin was the best safe haven from raging inflation. He actually called it "digital gold." Remember the graph of the value of the dollar?

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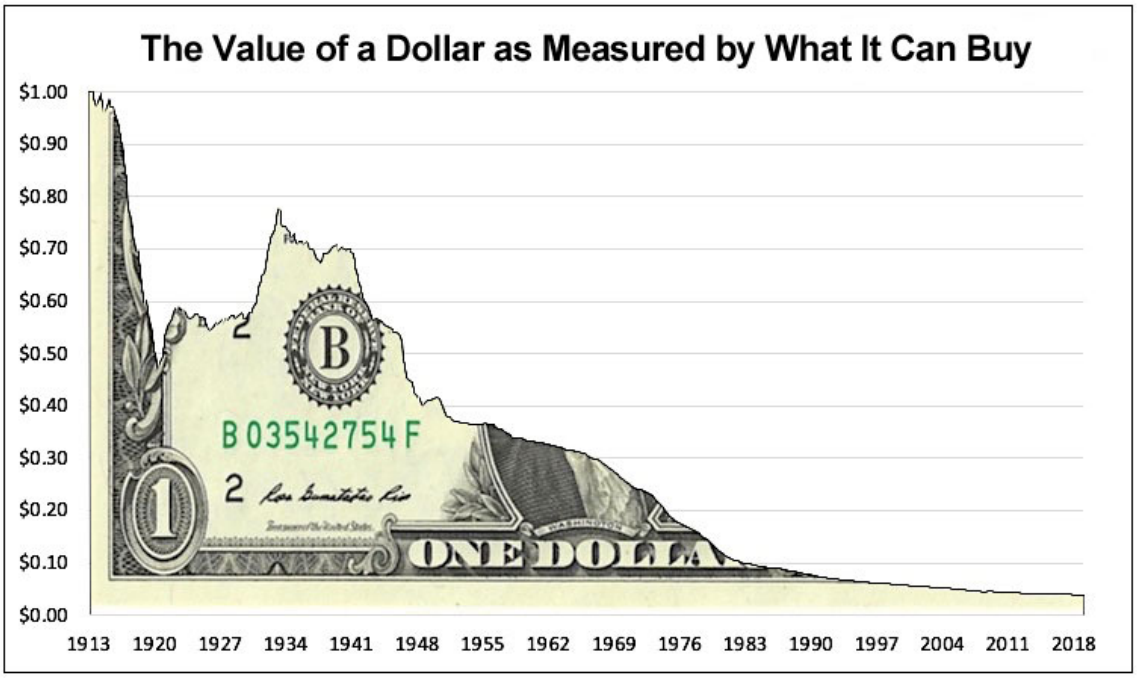

Data Courtesy: St. Louis Federal Reserve

Contrast that with this graph of the historical value of Bitcoin.

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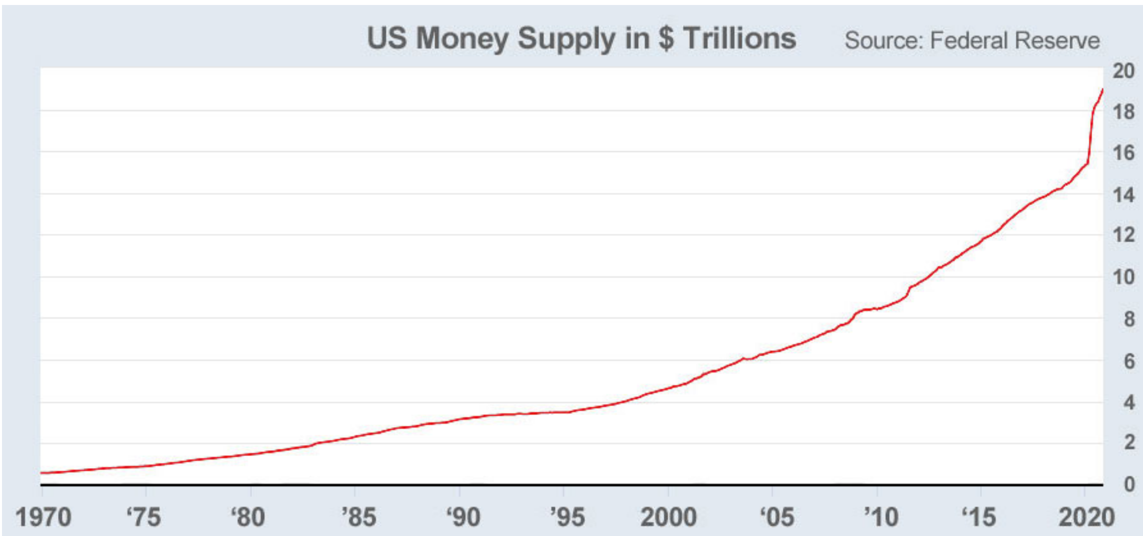
Why are those two graphs so different? The answer is that there is no limit to the number of dollars that a government can print and when too many are printed, the dollar loses value. There is a limit to the number of Bitcoin that can be created. The program that creates Bitcoin will never create more than 21 million. As more people adopt Bitcoin the limited supply causes its value to increase. Remember this graph?



Things to think about

If you look at Bitcoin's graph on the previous page, you will be struck by the dramatic, vertical rises and the later, dramatic drops. Bitcoin's price has occasionally multiplied by two or more times within a month or two. It has also dropped significantly after such rises. Although the trend is up, the journey is not smooth. So, I offer you these suggestions if you decide to invest in Bitcoin.

1. Start by buying a little Bitcoin and don't put more money into it than you can afford to lose. Do NOT take out a loan or empty your 401k.
2. After you have some Bitcoin, learn about other cryptocurrencies, starting with Ethereum.
3. Be prepared for major ups and downs along the way. This point is related to the first point, don't buy more than you can afford to lose. If you can't sleep at night because you are worrying about your investment, you've bought too much.

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I was once a stockbroker at A. G. Edwards & Sons. One of the things I learned was that Individual investors without years of experience tend to buy with their emotions. Everyone else is making lots of money and they don't want to miss out. So they buy at the tops. Then when their investment goes down they panic and sell. As a result, they buy high and sell low. Don't let this happen to you with Bitcoin. Only buy what you can afford to lose and you'll be able to hold through the dips and sell high…very high.

4. Plan to hold Bitcoin for two or more years to account for the skyscraper highs and kamikaze lows.

A look to the future

Online shopping is taking over. I remember the thrill I felt when I went to my local Borders bookstore to see my first published book on the shelf. I even have a picture coming out of the store holding up the book with a huge smile on my face. Enter Amazon. Borders is no more. Amazon and ecommerce (online shopping) are changing the retail landscape (literally) by connecting manufacturers directly to buyers through the Internet.

The same will occur in finance (loans, savings and investments). Currently, you deposit money into your savings account at the bank for 1% (or less) interest per year. Your bank then loans that money at 5 to 36% to someone else and keeps the difference. This is the cost of a financial middleman.

Just as the Internet has removed the middleman from shopping, this will also happen in banking. We *will* pay less for money transfers and loans, and receive higher interest on our savings accounts. In fact, there are already cryptocurrencies that paying 8% or more for deposits

Conclusion

We've covered the evolution of money and the inevitable inflation crisis. It will only get worse. We've also covered using cryptocurrency to prepare and even prosper from this crisis. I am no longer a licensed investment advisor. I am now an author. My hope for you is that you will do your own research and use it to improve your life.

I am happy to help you, if you have any questions or need further information. Please email me at peter55glick@gmail.com.

I get a lot of email, so please be patient.

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