Fortunato Asset Management

Q2 2021 Market Update and Newsletter

The Declining Purchasing Power of Money

This quarter's title is borrowed from chapter 6 of a book I published last year called Joe's Dynamic Investments. In that chapter I make the following comments about inflation:

"No, it hasn't always been that way. Let's examine a little history on the subject. Counter to what most people believe, consistent inflation is a relatively recent phenomenon. Persistent inflation, without countering deflation, didn't really occur until after World War II in this country.

"From 1650 to the early 1900s, there was little inflation, although there was a lot of volatility in price. Prices went up one year, down the next. Up for two, down the next three. One dollar in 1650 had the purchasing power of $1.12 in 1750, a total of 12% inflation (currency devaluation) over 100 years. By 1850, it took $1.37 to buy the equivalent of that 1650 dollar, or 37% inflation over 200 years – hardly anything. Prices were relatively stable over the longer term, rising only slightly. In 1913, the year the Federal Reserve was created, it would have taken $1.74 to equate in purchasing power to that 1650 dollar. Over this period, currency exchange rates were very stable as well, changing little."…

"Over time, inflation tears away at wealth, especially if that inflation number tics up for an extended period. Just as compound returns work to multiply our savings, inflation compounds to deflate our purchasing power."…

"Anyway," I resume, "one of the key differences in the twentieth century was that there were fewer and fewer down years in price deflation as the century went on. After 1950, there were almost no years of deflation in the government's Consumer Price Index (CPI) save for a minuscule .3% in 1955 and a .4% decline in 2009."

With that historical context on inflation in mind, I endeavor to follow up on our Q2 2020 market update, in which I focused on the unprecedented amounts of peace time increases in the money supply via monetary and fiscal stimulus measures.

Let's take a look at the massive total of fiscal (Federal Govt legislative) and monetary (Federal Reserve) stimulus since the covid lockdowns:

March 2020 Cares Act: $2.3T

April 2020 Supplementary to Cares: $484B

December 2020 Relief Bill: $900b

March 2021 American Rescue Plan Act: $1.9T

Total Approximate Fiscal Stimulus: $5.58 Trillion

+

Total Assets Federal Reserve Balance Sheet: Increase $3.94T, from $4.15T to $8.09T or 95% since January 2020.

= **Total U.S. Covid Lockdown Related Fiscal and Monetary Stimulus: $9.52 Trillion**

To put that amount in perspective, that's nearly 2 times the entire Japanese GDP for 2019. Monetary stimulus has proven to have a muted impact on inflation since the 2008 financial crisis. However, this go round, we have over $5T fiscal stimulus to go with it, and the fiscal stimulus is **definitely** having an impact on inflation. Year over year CPI for Q2 2021 is listed by the BLM at 4.8%. The CPI is muted, perhaps drastically so.

Consumers are paying up for autos, trucks, rental cars, plane tickets, hotel rooms, food, restaurant prices, and housing. There is a major push on price through the supply chain. There are more dollars floating around in the economy and $2.5T in extra household savings since the pandemic began. You can see it and you can feel it. Jerome Powell and the extraordinary bankers at the Fed make the case that the spike in inflation is temporary. This is likely true for some of it. We have temporarily robust demand and temporarily obstructed supply which makes for short term inflation. A lot of the inflation generated will be permanent.

At some point in the (near) future I think there will be a hangover from all this binge spending. There will be a letdown in the economy likely in 2022, but prices will continue to stay high, just like they have done since 1950. After a brief hangover, prices may accelerate further when the economy picks up steam. Our federal government has thrown discipline out with the chamber pot water. Why not? Here's a riddle. What's good for the government, but bad for its citizens, the poor, middle class, rich, and most companies? If you guessed inflation you're spot on. Inflating away government debt has been a popular pastime of profligate governments since fiat money began. With inflationary tactics the govt pays back bond holders with ever declining currency. It's a hidden and very expensive tax.

With the market and assets exorbitantly priced, we still want to be optimistic. I've found throughout my investing career that it simply pays better. The declining purchasing power of currency forces us to play aggressively with our investments.

Optimism without hope. Discipline without speculation. Patience without impulse. Show us the money and how you are going to make more in the future. We like companies that make money and trade at reasonable multiples. That's our investment attitude in this and every market.

What is the S&P 500 Index?

What does average mean for an S&P 500 stock?

The average market value for an S&P 500 company is $60 billion dollars. The median is $23b.

On average 21 analysts cover each S&P stock. The average “Buy” rating ratio, buys divided by total, is 53%. The avg. “Sell” ratio is 7%. That leaves an average neutral (“Hold”) rating ratio of 40%. Obviously rosy. We never look at analyst ratings.

The average analyst price target for an S&P 500 stock implies a gain of about 6%.

The total market capitalization for the S&P 500 index (the sum of market caps for all included companies) is $31.6T.

Apple is around 7% of the index total.

The current dividend yield of the S&P 500 index is 1.27% vs. a long term average of 1.86%.

Each stock in Dow Jones Industrial Average (the Dow) company has an avg. market cap of $280b, and 30 analysts cover each stock. The average analyst price target for the Dow works out to a 7% gain.

Our Strategies, Fees, Costs and Alignment

Below is a recap of each strategy and fee structure for Qualified Clients:

Fortunato 1 Growth and Value Strategy. Invests in a combination of reasonably priced growth stocks and value stocks. No Management Fee. The Performance Fee is 25% over a 6% per annum return with price breaks at $1M and $2M. On the first 6% return, no fee. Goal is a 14% average annual return over time.

(Note: Due to overlapping similarities in holdings and performance we have closed Fortunato 2 Concentrated Value Strategy for now).

Fortunato 3 Dividend and Income Strategy. Invests in a conservative mix of government short term bonds, mortgage-backed securities, dividend paying stocks, and preferred stocks. Fee is .55% of assets under management. The goal is a 6% average annual return over time.

I maintain a substantial portion of our family's savings in the Fortunato strategies, aligning my interests perfectly with investors. Many thanks to Brittany Rowland and Heath Martin for their valuable ongoing contributions to research, administration, and technology and thanks for reading!

=S Dee