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Stagflation and a portfolio answer

COVID-19 has shifted the global deflationary course into stagflation – an environment where real assets should perform, according to Centurion Asset Management's **Greg Romundt**

ONE INVESTMENT manager sees danger on the horizon after a decade-long trend in interest rates staying 'lower for longer.' Greg Romundt, president of Centurion Asset Management, says that COVID-19 and "reckless money printing" on the part of governments are sending major economies hurtling toward stagflation.

Romundt says he predicted the past 10 years of downward interest rate pressure, resulting in a decade of disinflation. Rate cuts in North America in the wake of the COVID-19 pandemic brought a trend that started in Japan full circle, with rates in almost every developed economy near or even below zero. Romundt's view is that this trend would go on until a 'Minsky moment' hit and everything snapped, shifting disinflation to rapid inflation. He says that now, that moment is coming fast.

"The trend toward disinflation is over," he says. "COVID-19 – and, more importantly, the poor government response to it – has accelerated what may have taken another decade or two to play out otherwise. Stagflation, at best, is what lies ahead. Now is the time to reposition portfolios if you haven't already done so [because] time is running out to move into real assets."

The sustained deflationary pressure witnessed over the past decade was, in Romundt's view, driven by four distinct forces. "Robotization and softwarization," he says, have made workforces redundant, reduced demand and will drive down corporate profits in the long term. Increasing debt and declining debt productivity will weaken the outlook for small and medium-sized businesses in Canada. An aging society has flipped the relationship between interest rates and savings rates because people approaching retirement cannot rely on low-yielding fixed income and pensions to survive. The long-promised arrival of higher-quality jobs with globalization hasn't materialized either, further compounding damage to the purchasing power of the working class.

The big picture, Romundt says, has been deflation. But now, COVID-19 has reversed that order and set us on a course to stagflation. Romundt says this due to a range of governmental, social and economic factors that have been shaped by the pandemic.

He says the pandemic response in the developed world has resulted in economies crashed by lockdowns while governments printed untold amounts of money to ameliorate an even worse crisis. In the course of this, he says, central banks have ceded control of the money supply to politicians. In an era of populist policies, Romundt sees politicians abusing this power and printing yet more money to pay for "giveaways." Government debts and deficits are already exploding, he says, and nobody seems to care. He predicts, too, that the central banks will allow inflation to "run hot" for longer than they normally would, given the huge amounts of debt incurred.

A second lockdown, too, could prove even more disastrous for the economy, and the promise of a vaccine may never be fully realized, with uncertainties around efficacy, reinfection and the logistics of a rollout still ahead.

In addition, Romundt says, the deglobalization trend initiated by the nativist policies of leaders in the Anglosphere has been accelerated by the pandemic as global trade

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> Greg Romundt, Centurion Asset Management

cratered in 2020. The pandemic has raised fears of global supply chain breakdowns and made autarky more attractive. Global tensions are accelerating, too.

Romundt believes "robotization and softwarization" are set to continue at an accelerated pace, destroying yet more jobs as robots become the 'safe' option. He sees working from home as a Trojan horse for workers who still have their jobs. He expects that while it seems like a boon now, companies will more quickly begin to move jobs offshore and cut compensation for at-home workers. This will, in turn, require further income support from governments.

Main Street, too, is cratering while Wall Street booms, Romundt says, thanks to a few major tech stocks. This is accelerating a concentration of economic power in a few large companies and weakening the outlook for small and medium-sized businesses. The wealth gap, too, is exploding even faster than it did pre-pandemic. This is resulting, Romundt says, in a breakdown in social cohesion as younger and more marginalized people feel the worst economic impacts. More radical politics are moving into the mainstream, and he believes governments will need to implement universal basic income to buy social peace.

On top of all these pressures, investors and advisors are witnessing the breakdown of the 60/40 portfolio. That model is highly vulnerable in the current environment, Romundt says, as equities are overpriced, and bonds provide negative return with a heavy downside risk. He believes that in this environment, gold and silver are the new bonds, capable of hedging against inflation and deflation at the same time.

In the face of all these pressures, Romundt says governments will have to engineer stagflation. In that environment, real assets tend to perform best. Relative to stocks, he says, commodities are extremely cheap. Apartments should also do very well, with access to artificially engineered low interest rates. As of now, Centurion can borrow below the rate of inflation – meaning, in real terms, that it is getting paid to borrow money.

As advisors look at the plays they can make to win for their clients in a stagflationary world, Romundt says they should look more closely at apartments and some of the ways Centurion is uniquely set up to benefit.

"In normal times, we would buy apartments as income-generating assets and then pay part of this income as interest on mortgages we used to finance part of the purchase," he says. "I believe, if I am correct that inflation will continue to exceed the rate of interest, the Centurion Apartment REIT would be in the position of earning income on its assets, which would increase with inflation, and earning income on its liabilities. Let that sink in for a moment, too – getting paid on both sides of the balance sheet. That is why I believe apartments are a strong play for the times ahead." WP

Greg Romundt's white paper is available on **centurion.ca**.