Summerwood

New thinking for alternative investments

Investing Through Inflation

A Series of Papers to Inform Investors the Program is Changing

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Investing Through Inflation

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A Series of Papers to Inform Investors the Program is Changing

***Summary**: It has been more than forty years since investors have had to concern themselves with inflation. This series of papers has been written to highlight that change is afoot and how best to prepare portfolios to protect against the effects of inflation.*

Maestro – an honorific title of the highest respect. Most often applied to a symphonic orchestra's leader, the Maestro's role is to unify the group, to keep the music moving at a steady pace, to fight the group's influence. Think of the central banker as the Maestro of the economy[1] - to keep the economy moving along steadily, at just the right tempo.

The natural flow of an economy is to cycle through expansions and contractions. The central banker attempts to control the tempo, to ensure the crescendos are allowed to build, the decrescendos allowed to fall, all within a range pleasing to the audience – society, businesses and politicians. A beautiful economic symphony – when it works.

The economic equivalents of the crescendos/decrescendos are inflation and deflation. Central bankers are ever vigilant to keep the push/pull of inflation/deflation in check. One might presume central bankers' concerns would be evenly balanced between inflation and deflation. I posit this is not the case. The next statement will attract counter arguments; I postulate that all Fed Chairs since the end of Paul Volker's era (circa 1987) have shown an over exuberance to avoid deflation versus a concern of invoking future inflation. Central bankers fear their inability to counteract deflation more than they fear their ability to control inflation. Simply put.

It's important for investors to recognize the policy imbalance. Inflation isn't a virus that can be eradicated. Investors will, in due course, need to be in a position to defend against inflation's effect. Central bankers, politicians, the fourth estate, none of these will "ring the bell" alerting investors ahead of inflation. Investors have to take it upon themselves to restructure their portfolios ahead of an inflationary environment or align themselves with investment professionals with a focus and understanding of inflation.

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[1] At the height of his central banking career Alan Greenspan was referred to as Maestro. Bob Woodward's 2000 biography of Greenspan was titled Maestro: Greenspan's Fed and the American Boom.

In the paper **What's An Inflation Protected Portfolio?** I wrote that classic investment theory recognizes that inflation protection is notoriously difficult to manage. In the pursuit of brevity what I omitted was that the assets and strategies used for inflation protection are scarce. Investors need to be positioned ahead of inflation just as home owners need to have home insurance in place prior to making a claim. The cost of inflation protection will rise as inflation becomes recognized. It will rise to the point where the cost of the protective assets and strategies will mitigate the benefits.

Throughout this series of papers, I have tried to not overtly plug Summerwood's services or capabilities. That being said I hereby countermand that directive. Summerwood has long held the view that inflation is inevitable and that the investment industry is ill prepared to manage through inflation. The argument that such a viewpoint has been early, or worse, wrong, needs to be addressed, briefly. My counterpoint to this critique is that by design the portfolio outlined in **What's An Inflation Protected Portfolio?** will protect assets through inflation while also providing risk adjusted returns in non-inflationary periods. To point, the bond portfolio is not eliminated but rather transformed from fixed rate interest payments to floating rate interest. Equities are not eliminated but are reduced and refocused on companies with real earnings. By design the highs and lows that accompany traditional portfolios due to the heavy equity weight are muted. All the while being in a position to protect assets when inflation begins its deleterious effect on the markets.

Summerwood has been singularly focused on the effect of inflation. Managing assets through inflation requires a breadth of knowledge and skills and exposure to a full suite of products and strategies. Summerwood has experience managing traditional assets and alternative assets. Bonds, equities, commodities, real assets and alternative strategies are all within its repertoire and experience. These are the tools that investors will need to avail themselves of in the days ahead.

A Maestro will have chosen the musical program before the audience arrives, before stepping up to the podium and before the baton is lifted. **Investing Through Inflation – A Series of Papers** was written to inform investors that the program will be changing from what they've been enjoying. The **Overview** papers alert investors to the inevitability of inflation. The **Asset Building Blocks** warns against relying on the illusion that gold and bitcoin can magically provide inflation protection. Finally, the **Inflation Protected Portfolio Management** papers provide investors with the basis for establishing an inflation protected portfolio.

To those who have read all or a portion of the series I want to thank you for your time and attention. They were written to help investors. If you would like to learn more about how Summerwood can help, please feel free to use the contact details below.

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