iSectors® Newsletter

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"Inflation Threats Loom Amid Loosening Financial Conditions and Increasing Money Supply"

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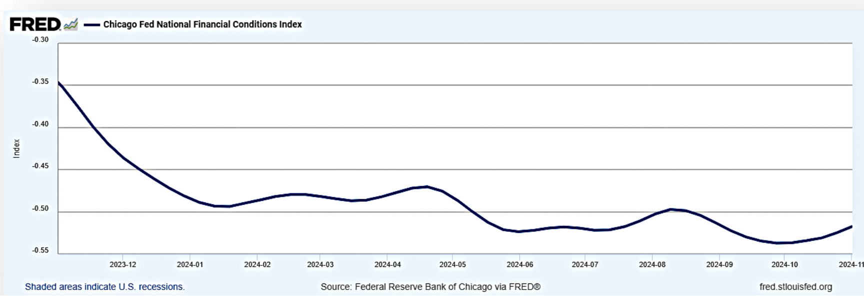
iSectors® continues to see an ongoing threat of resurging inflation in the face of increasing money supply and liquidity, decreasing interest rates, continued fiscal spending, and loosening financial conditions. With Donald Trump primed to re-take office in January, potential tariffs and reduced taxes could certainly fan the flames of the inflation fire that has been building for years. Jerome Powell even admitted that the Federal Reserve "expects there to be bumps on inflation" in his most recent comments made after the FOMC meeting in early November.
Our quantitative models tend to agree, with high allocations to gold and an increased weighting to energy stocks in the most recent month. Here are a couple of specific indicators we have been focused on that lead us to believe inflation will be an ongoing issue as we head toward a new presidential term and into 2025.

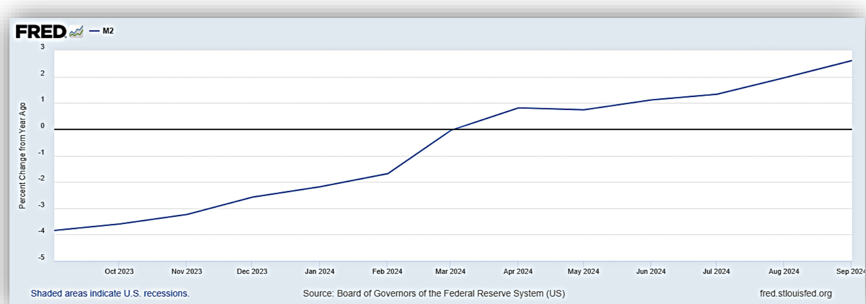
Loosening of Financial Conditions

Over the last 12 months, financial conditions have only become looser, despite the Federal Reserve holding short-term interest rates at a twenty-year high above 5% for most of this period. This can be seen by the Chicago Fed National Financial Conditions Index (NFCI) dropping even more negative over the last year. The more negative the NFCI is, the looser the financial conditions are.



Increasing Money Supply

Going hand-in-hand with loose financial conditions comes increasing growth in money supply. Over the last year, the M2 money supply has grown by over $1T, and the year-over-year percentage change was the largest since 2022. A growing amount of supply of money in the system increases liquidity and often leads to a proportional increase in inflation within the 18 months to follow.



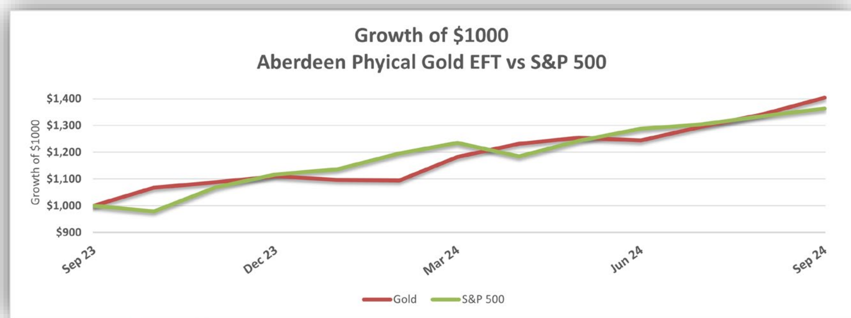
iSectors® Solutions

Various iSectors® models are positioned for potential increasing inflation, and there is a common theme amongst them: gold.

The **iSectors® Post-MPT Allocations** have held heavy allocations to gold for almost two years. These models are dynamic and will change over time as the economic factors in their quantitative algorithm change. They are still holding steady with high gold allocations and have even added an allocation to energy stocks, which is another sector that tends to perform well when inflationary pressures rise, as evidenced by the 63% return of the Vanguard Energy ETF (VDE) in 2022 when almost every other asset class posted an outsized negative return. Since the iSectors® Post-MPT Allocations are dynamic and can change every month, there is no guarantee that they will hold a high allocation to gold in the future. Other iSectors models hold strategic weightings to gold to help preserve purchasing power. These models are the **iSectors® Inflation Protection Allocation**, which will always hold a 10-20% position in gold or silver, and the **iSectors® Precious Metals Allocation**, which offers focused exposure to various precious metals and has historically held about 50% of the model in gold.

Back to Gold

The Aberdeen Physical Gold ETF (SGOL) posted a positive return in 2022 and has also performed exceptionally well over the last 12 months, seemingly hitting a new all-time high every month. In fact, over the previous year, the price return of gold has kept up with the performance of the broad stock market.



2024 Election Aftershock: Republican win is also Crypto's

The tailwinds for crypto, Bitcoin, and blockchain companies are only greater now that Donald Trump has won the election. He has made mention of creating a strategic reserve of Bitcoin along with many other proposed crypto friendly policies which we won't know the full extent of until 2025. Many of the other investments mentioned previously also stand to benefit if certain policies are passed such as tariffs and potentially lower taxes. If those policies are passed, inflation becomes even more of a concern, on top of the already increasing money supply and loose financial conditions. Either a strategic allocation to inflation sensitive assets like gold, or a model that can dynamically allocate to those type of investments is crucial as a part of a diversified client portfolio that can withstand many different market environments both on the upside and the downside.

One Last Idea

Suppose you are more interested in a model that can potentially protect against the extreme asset price inflation we have experienced since the COVID pandemic that has seen the S&P 500 return more than 20% in three of the last four years (something that hasn't happened since the 90s). In that case, it might be worth considering one of the iSectors models that allocate heavily to an investment with greater than 50% returns in five of the last six years. That model is the iSectors® CryptoBlock® Allocation, and that investment is Bitcoin. The model has a 60% allocation to spot Bitcoin ETFs and a 40% allocation to blockchain equities and technology ETFs, which includes things like Ethereum, crypto exchanges, and other traditional companies utilizing the blockchain such as PayPal, Visa, and MasterCard.

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