Retirement Lifestyle Advocates

RADIO PROGRAM

Expert Interview Series

Guest Expert: Michael Pento
Pento Portfolio Strategies

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Dennis Tubbergen:

Welcome back to RLA Radio. I'm your host, Tubbergen. Joining me once again on today's program is returning guest Mr. Michael Pento. Michael is the founder and chairman of Pento Portfolio Strategies. You can learn more about his work at PentoPort.com. He is also the host of the popular podcast, The Midweek Reality Check, and I always appreciate catching up with Michael and getting his perspective. And Michael, welcome back to the program.

Michael Pento:

Thanks for having me back on.

Dennis Tubbergen:

So Michael, let's just start. We were chatting just a minute before we started actually recording this interview, about the health of the US economy. Give us your assessment.

Michael Pento:

Well, the economy isn't falling off of a cliff yet. Certainly on the precipice. We had a GDP report came out recently for Q-2 that showed growth was around 3%, but don't forget it wasn't growing at all in Q-1, so we have to average those two out.

But when you look at the extension of the TCJA, the Tax Cut and Jobs Act, that's a little bit of a boost to the American economy. But those tax cuts or the extension of those tax cuts is just, basically the persistence of the same rate that was already in place. So you have to add to that, the fact that we have pretty significant tax hikes coming from tariffs. That's about $600 billion a year in tariffs. As a matter of fact, we just recently learned that India is facing a 25% tariff on its goods. So there's a lot of regulations and taxes going on as well.

So taxes, and tariffs are taxes, and someone's going to pay them, and it's either going to be margin compression from US corporations or it's going to be consumers that are going to pay those increases. And when you add it all up, you get the idea that earnings are not going to grow very fast, the GDP is not going to grow very fast.

And what does that mean when it comes to supporting the three massive bubbles that still are in existence, which is an unprecedented credit bubble, an unprecedented real estate bubble, and an absolutely gargantuan, humongous stock bubble, all existing concurrently. And if you believe in the reversions to the mean, you have to believe there's going to be a great reconciliation of asset prices. It's still in our cards.

And to be honest with you, if you look at where the level of asset prices are today in the stock market, if you look at things like the CAPE ratio, if you look at the total market cap of equities due to GDP, the negative risk premiums that exist, price to sales, that is three times the price of the S&P 500, is trading at three times sales.

The ensuing decade shows that in nominal terms, stock prices fall. And in real they fall even more. The risk-reward ratio to go way over your skis long, the typical 60/40 portfolios, 60% stocks and 40% bonds, is probably going to delay your retirement by decades.

Dennis Tubbergen:

Michael, there was a lot there. You mentioned the cyclically adjusted price earnings index as well as the Buffett indicator, which I'm not sure you use that by name, but you certainly described it. I think the last I looked, the Buffett indicator was at a second all-time high and like the CAPE was at over 36. So given those huge nosebleed numbers, what's your forecast for stocks?

Michael Pento:

The CAPE ratio is now very close to 38, and the total market cap of equities as a percentage of GDP, as you mentioned, the Buffett indicator, is at over 210%. So it has never been that high before in history. And as a matter of fact, if you want to look back to where it was in 2000, it was 140% of GDP. That was the massive Nasdaq bubble.

And at the start of, at the global financial crisis, before stocks fell by 50%, it was 104%. So we're in the thermosphere of asset prices. Never before in history have we seen this. In fact, the mean ratio here, we're talking about total market capital of equities of GDP, should be sub 100, something around 85, 90%. We've never seen this before.

So if you ask me where I am, I manage money for a living. I am still net long the market, but not way over my skis. We have about a 20% net long position, but we're in the right sectors, Dennis. So we're in the precious metals complex. We're in inflation hedges, we are in aerospace and defense, and we have some tech.

And because I manage money for, I have almost 1100 client accounts here, I am here every day, managing the second derivative of inflation in the context of growth. So I can best ensure me and my clients can avoid the next recession/credit crisis, which is surely coming. We have not abrogated the business cycle here. And when that happens, you're going to see debt and deficits soar. My projection is for annual deficits to reach between four and $6 trillion. They're already at $2 trillion.

And this is happening, Dennis, in a time where we have relatively full employment, and we have a relatively healthy economy. Again, according to the government, we grew the economy by a 3% seasonally adjusted annualized rate in Q-2.

But why do we have deficits that are over $2 trillion and we're paying over a trillion dollars in interest payments, now the second-largest item in the budget? So deficits are going to go between four and 6 trillion. That's what they historically do. During recessions, they increase by 300%, and that's because the automatic stabilizers that kick in. And the problem is there's just not any buyers left for our treasury debt. So interest rates could spike, rather than fall as they usually do in previous recessions. And that could be a very existential crisis for the... First, certainly for the three bubbles and of course for the U.S. economy.

Dennis Tubbergen:

Michael, again, a lot there. If you're just joining us, I'm chatting to Mr. Michael Pento. He is the founder of Pento Portfolio Strategies. You can learn more about his work at PentoPort.com. I'd also encourage you to check out his popular podcast, The Midweek Reality Check, information on that at PentoPort.com as well.

So Michael, you mentioned that interest rates could spike, and earlier you referred to the 60/40 portfolio. So if we see interest rates spiking here, that pretty much destroys the 60/40 portfolio. And when you look at government deficit spending, as you mentioned, we're at 2 trillion, despite the whole Doge thing, which seemed to now be more political theater than anything substance. Seems there's like zero political will to cut spending. And of course the next question is, where do you cut it? So doesn't that mean the Fed's going to have to stop in and... Step in, rather, and become the buyer of last resort and we're going to see more inflation?

Michael Pento:

Yes, unfortunately, that is my prediction. My prediction is that the Fed is going to turn to the only playbook they have ever used since 1987 in particular. They're going to cut interest rates towards 0% and they are going to print massive amounts of money, grow the balance sheet back to... The balance sheet, by the way, just for reference was about 700, $800 billion prior to the global financial crisis in 2007.

And then it grew all the way to $9 trillion. I mean, who in this nation ever voted for a money supply, someone who could manipulate the money supply, to grow by over $8 trillion in a relatively very short period of time? And there's a reason for that. There's a reason why the Fed has done that. Because if the money supply was kept relatively constant, as it would be fettered under the gold standard, then interest rates would go to the moon.

The CBO projects that the debt is going to rise to around 50... I think $58 trillion by 2035. But if you look at reality, I think it's going to go to $67 trillion by 2035, because the CBO doesn't think we're going to have a recession. I mean, I'm not trying to use hyperbole here. I'm trying to give you an accurate estimate as to what the deficit is going to be, and debt and deficits are going.

So the CBO doesn't think we're going to have another recession in the next decade. The CBO doesn't think inflation or interest rates are going to rise in the next decade. So to put this in perspective, the country now has 37 trillion in debt. We're going to add 30 trillion more in the next decade because we're going to have another recession in the next 10 years. The U.S. averages this recession every 6.4 years since the end of World War II.

So why does the CBO not think we're going to have one? We're going to have another recession. Debt and deficits are going to absolutely skyrocket. And that means we're going to add, it took from 1776 all the way to today, that rate to accumulate $37 trillion in debt. We're going to add $30 trillion more in just one decade. That's the fastest accumulation of debt in modern history.

And the Federal Reserve has to expand the money supply, not that they should. I'm not saying that that's a good thing. I wish they would not. I wish we didn't have a Federal Reserve, because that would actually be the governor to the massive fiscal madness that's going on in D.C. We just expanded, we just passed the extension of the TCJA, the Tax Cut and Jobs Act, and part of that Big beautiful Bill was the raising of the debt ceiling by $5 trillion.

This has to stop. And the only way it would stop is if the Fed stopped ameliorating the crisis by just printing trillions of dollars. Because if they stopped interest rates would spike out of control, and that would be the fettering mechanism. That would be the reality check that would prove we can't continue doing this.

But I'm afraid, Dennis, at this point, interest rates are destined to spike either way, because even if the Fed started going down that same road and printing trillions of dollars, once again, and expanding its balance sheet and lowering interest rates to zero, back to 0%, inflation will cause interest rates to spike regardless.

Dennis Tubbergen:

Well, my guest today is Mr. Michael Pento. You can learn more about his work at pentoport.com. Also check out his podcast, The Midweek Reality Check. I'll be continuing my conversation with Mr. Michael Pento, when RLA Radio returns, stay with us.

Welcome back to RLA Radio. I'm your host, Dennis Tubbergen. I have the pleasure of chatting today with Mr. Michael Pento. He is the founder and chairman of Pento Portfolio Strategies. You can learn more about his work at pentoport.com. Also, he hosts The Midweek Reality Check podcast.

And Michael, as you were talking, I've got a number of follow-up questions for you, but before we jump back in, maybe give the listeners a bit of an explanation, a little bit of a preview as to your podcast, The Midweek Reality Check.

Michael Pento:

So it is simply a five-week free trial. If you go to the website, it's called, as you say, The Midweek Reality Check. And in it, I just go over the most salient data, the economic data and the happenings of the previous week. And I give you an honest and objective read on the data. So sometimes, I'll give you an example, like we have CPI prints that come out and you'll hear on the mainstream financial media, hey look, the month-over-month rate was unchanged. That means we no longer have an inflation problem. But wait a second, here's the truth. The year-over-year change in CPI actually accelerated from 2.4% to the 2.7%. And by the way, it's not just the fact that inflation is rising much faster than the Fed's asinine 2% target, it's been above the Fed's target for 50 months in a row. The past 50 months in a row, it's been above 2%.

It's rising further away from 2%, and everybody's talking about slashing interest rates. In fact, the administration wants interest rates slashed to 1%. Now, I am independent. I'm actually a libertarian. I voted for Trump. So this is not a political diatribe, but why would you want to slash interest rates aggressively when inflation has been above the Fed's target for 50 months in a row, and the level of inflation has wiped out the middle class?

There was a recent survey done and the study done that shows that 60% of Americans, six zero, have less than a thousand dollars in net worth. And think about that. So most of Americans have no net worth or negative net worth. That's sad, but that's laid right at the feet of our Federal Reserve, which enabled that to happen by destroying the dollar, eviscerating the middle class. And they did that primarily because the people that inhabit DC can't help but spend money. And you can't live in reality when that's the case. Because if you lived in reality, as I said, if you try to finance the rollovers and the debt when you have 37 trillion national debt, if you kept that in reality without the Federal Reserve owning trillions of dollars of US treasuries and holding them out of the public's domain, interest rates would go much, much higher. And the housing market would crash and the stock bubble would burst and the credit bubble would burst.

Dennis Tubbergen:

So Michael, big picture, you talk about debt. Now, I just read a statistic that worldwide debt now is an excess of $325 trillion, which is just an unfathomable number. Seems like that's deflationary. And then over on the other side of the coin, you've got the Fed that, if they become the buyer of last resort, that could lead to an inflationary or a hyperinflationary outcome. So how do you see this playing out? What's the end game here in your view?

Michael Pento:

That's a great question, Dennis. So you're correct. The natural state of things to occur, the gravitational, I call it the gravitational forces of deflation, if they were allowed to work, would actually reconcile all these deformations in the economy. It would be very painful. It would be a depression, it would be very deflationary. But in the end, that's reality. That's what needs to happen.

I mean, it's not tenable. It's an untenable situation to have home prices so high, home ownership costs so high, that first time home buyers have been priced out of home ownership. That's not reality. You can't have an economy function that way. You can't have a real estate market function that way when the transaction market has been pretty much frozen.

So you mentioned debt, total non-financial US debt is now 257% of GDP. Now, that surpasses the global financial crisis peak of 234%. Remember that crisis occurred because of an over-leveraged financial system that was just 234% of GDP. Now we're 257% of GDP.

So why is this occurring? We have had for the past 20 years, negative real interest rates. That is also unprecedented. In other words, you go to the bank and borrow money from 2002 to 2022, you went to the bank and borrowed money and could have invested in anything, stocks, bonds, real estate, anything, precious metals, and you would make money because your returns were much higher than your borrowing costs. That's called negative real interest rates. You're borrowing from much less than the rate of inflation.

Now, that has ended. For the past two years, that has ended, and that has usually engendered the correction process to begin. Now, I have a model. I'm working here every day. I don't know, I can't pick a date for when this is going to end, but this fantasy will end. And perhaps you can look at May of 2026 when President Trump replaces the current Fed share with what I call an obsequious sycophant, a presidential puppet who will just slash interest rates. That could be the catalyst for long-term rates to start spiking higher, and that would bring the end of this whole fantasy.

Dennis Tubbergen:

So Michael, you mentioned real estate. I read a statistic recently that at the time of the financial crisis, the subprime housing market collapsed, if you will. At that peak there were 550,000 single family homes listed. I think we're now back up over 500,000. So are we about to see this real estate market turn over?

Michael Pento:

Yeah. Well, 20% of listings have, home listings have seen price reductions. It's the highest in a decade. You're like, you're right. They're 500,000 more sellers than buyers. Active listings are up 28% year over year, and pending home sales are being canceled at a record pace. So that's the bubble bursting. We're seeing it now. In fact, I think in the top one... The biggest 100 markets in the United States are now seeing price reductions. One third of those are seeing price reductions. So one third of the biggest markets in the nation are now seeing price reductions. So it's happening. The process has started.

Dennis Tubbergen:

So do you see real estate doing what it did at the time of the housing crisis? I think we had, depending on the part of the country, you want to look at, maybe declines of around 40%. Are we going to see something on par with that again?

Michael Pento:

I think nationwide home prices dropped 33%. I would not be surprised if that happened again, Dennis, and again, this is the big key here. The salient issue is, when the Fed cut interest rates in December of 2007, it took them to 0% in a year's time, took them to zero, and then printed trillions of dollars, took banks bad assets off of their balance sheets, and we had a recovery. It took a few years. We had a recovery in home prices and in the economy.

But if they did the same thing again, here's the question. If the same playbook is deployed, do we get the long end of the yield curve, the ten-year note, which by the way, that's where the mortgages are priced. That's where student loans are priced. That's where corporate debt is financed. Auto loans are made. So if that end of the yield curve spikes, you might not get any salve from the Fed cutting the money market down, the Fed funds interbank lending rate.

So that's the question. So could they drop 30 40% again? Yes, that would just put it in line to historical metrics, home to home price to income ratio now, today, is higher than it was at the start of the global financial crisis. And then when you add things like mortgages, the maintenance, the insurance, the taxes, the most unaffordable by far in history.

Dennis Tubbergen:

Michael, you mentioned earlier that 60% of Americans have a net worth of less than a thousand dollars, which is an eye-popping statistic. But taking that stat with what you just mentioned, it seems that the consumer is very much on their last legs. And this economy, which is really consumer spending dependent, has been kind of moved along, if you will, by the top 10% spending money. But you're seeing credit card default rates that are up, auto loan default rates that are up. Is this bubble starting to unravel as well? You mentioned a credit bubble at the beginning of the first segment.

Michael Pento:

Well, yeah. I mean, that's what I see happening. Yes, you're correct. Not only that, but you see FHA loans starting to default too. So the consumer, I call it the bottom four quintiles. So the bottom 80% have been struggling for a few years now, and it's only the top 20%, but that top 20%, their expenditures are derived from real estate and equity holdings that have appreciated. And if that's starting to roll over, at least on the real estate side, and then if we get at least at the start of a bear market, I think you could see the top 20% give up the ghost and then it's all over.

Dennis Tubbergen:

Well, I'm chatting to Mr. Michael Pento. His website is PentoPort.com. He is the host of the podcast, The Midweek Reality Check. He offers a five-week free trial for that. You can visit PentoPort.com to get more information. Michael, always a pleasure to catch up with you. Thank you for joining us on today's program, and I'd love to have you back down the road for an update.

Michael Pento:

I'm looking forward to it, Dennis.

Dennis Tubbergen:

We will return after these words.