with hedge fund manager Erik Townsend

Lyn Alden: What Will Stop This Train?

Erik: Joining me now is Lyn Alden, our number one macro voices all time listener favorite, as measured by listener downloads. Lyn, congratulations on taking the number one slot.

Lyn: Thank you. I'm humbled. Happy to be here.

Erik: The thing is I actually feel bad about this. The whole idea was to flatter you and honor you. And what did we do? We set you up to follow Jim Bianco, Alhaji, Louis Gav and Luke Groman.

How are we gonna top Luke Groman?

Lyn: I'm happy to have been part of the journey. It's always interesting when you start as a listener. So I listen to Macro Voices before I came on the show.

And so it was of course fascinating to join it and participate along the way. So I certainly thank you for having me on all these times. And hopefully I can continue to provide value. And as far as following all those people, that is certainly, challenging. I guess the best that I can do is try to add to it, try to build on top of it. Certainly not really trying to top anyone in particular. And those are all people that I've certainly learned from over the years.

Erik: Let's dive right in. You told me that you agreed and disagreed with various different parts of Luke's interview last last week.

Tell me more. What did you agree with, disagree with, and why? What did you see differently?

Lyn: I mentioned I pretty much mostly agreed with it there. There's rarely anything that I outright disagree with Luke on. We generally get, I think, correctly lumped together in, in kind of the same macro camp in some ways.

Main where area where I disagree I differ, I guess I would say from Luke is just areas of emphasis or areas that he has built up more expertise than I have on and other areas that I focus more on. But I thought that entire interview was directionally correct. One way that I maybe sometimes differ a little bit is that I'm of, in some ways Luke Gromen light, uh, which is that my timeframes tend to be a little bit longer than his sometimes correctly, sometimes incorrectly.

And so I tend to maybe be a somewhat more muted version of Luke. But otherwise quite similar. So there, if there's areas that you wanna touch on, I'm happy to go in multiple directions.

Erik: You just alluded to it. What's really interesting in my mind is this question of what is it that causes or enables that change from slowly at first to then all at once. And of course, that was a major thrust of Luke's interview. I was actually affected more by reactions. When we called the pandemic in January of 2020 on Macrovoices. It was weeks weeks and weeks of hate mail and angry people saying, you're alarmists you're fear mongers, you're crazy.

Luke's interview was pretty darn grim, frankly, with respect to its outlook. Lots and lots of attention, almost all of it positive, and were not getting all of the accusations of fear mongering, so forth. It says to me that people's attitude has changed and this Luke Gromen moment idea of a really significant breakdown in the international monetary system because the US dollar is at the center of it and the US dollar is not quite as strong as everybody hoped it would be.

That was really controversial stuff a few years ago. It seems like everybody's maybe ready to accept it and that scares the hell outta me. 'cause it, I think it means we're. Accelerating is, am I right to interpret it that way? And what do you think causes that state transition to all at once?

Lyn: Yeah, I think that's a reasonable interpretation.

And I'll start by saying that I actually remember you, you talking about the pandemic early on your podcast. I was a listener back then , it was helpful for me hearing you and Jim Bianco and others cover it. And so for example, I was able to have notes about it in my research service and also provide warnings.

And that was in large part because of I was listening to the right people at the right time. And I was able to dig into myself and help confirm it. So I certainly appreciate the work you did there at the time. Going back to where this goes, or are we hitting a gradually then that suddenly moment.

Part of why I got into macro in the first place was to answer that very question or more specifically, the question was, where is the public debt going? When will it matter? And so I, I, prior to that, I, listeners probably know I worked as an engineer for a long time. I had a long history of investing primarily in equities.

I consider myself more of an equity analyst. And I started, realized that we were entering and to some extent I had already entered a very macro heavy. Decade. And so more so than just getting individual stocks, right? It was really important to get the macro right. Big questions like, are stocks gonna outperform bonds or vice versa?

Are things to run hot and inflationary or are things gonna have more disinflationary and contractionary type of things. Getting those really big pieces, right? What sectors to own. There kind of major trends and my kind of starting question was basically, so we have rising public debt to GDP at, throughout the 2010s decade there obviously, there's lots of polarization. There was the Paul Ryan versus Obama. Era that whole kind of, the republican more fiscal hawks back then, and then and Obama on the other side of that and that great debate around deficits and public spending.

And what we started to see at the end of the 2010s decade. And I, Luke covered this early, I started covering it early, was that we started to get rising deficits as a share of GDP even as we had unemployment continue to fall. So there's a multi-decade history of those being highly correlated.

And they separated on a sustained multi-year basis. In the late 2010s. And that was like a handful of reasons. There were some tactical ones, like for example in Trump's first term he did unfunded tax cuts. Which, which, around the margins contributed to the deficits. But the really big piece was simply demographics that the baby boomer generation started entering retirement in pretty significant numbers. And therefore we started to draw down on some of these really big entitlement things. Things that, like Stanley Druckenmiller and others have been warning about for a long time started to really actually happen. So that whole top heavy entitlement system started to really matter.

Then of course. COVID kicked everything into high gear. And that distracted people a lot, I think, from the secular trend. But then after that, all eventually subsided, we're still back on this more secular trend of structurally high deficits in large part because of the entitlement system, because of multiple other factors contributing.

And what I became known for over the past five, six years is my emphasis on the importance of fiscal. Which is that, so many people are focused on what the Fed's gonna do and of course that is relevant. But my view was. The really hot fiscal deficits that were running matter.

So back in, in 2020, 2021 and all that, it was me kind of warning about inflation. And after that kind of hit and eventually, somewhat cooled off from that really explosive period, it was more about this nothing stops this train thesis, which is sure it's not running quite as hot as the, the hyper stimulus of 2020 and 2021 and the lagged after effect.

But it's more of the sustained. Run it hot large deficit environment that mutes economic cycles keeps inflation generally above target offsetting, a lot of various kind of technology driven disinflation we would otherwise have. And keeps going. So then the question is, it goes back to my original thing is where is this all headed?

When does the public debt truly matter? So my first answer to that is that it has mattered for at least the past six or seven years, ever since we've entered this more sustained fiscally dominant environment. The economic cycles have changed. Things like the yield curve have become less predictive than they historically have been.

I think it's fueled some of the political polarization because those on the receiving side of the deficits. Are experiencing on average, a very different economy than those not on the receiving side of the deficits, and they're instead more on the tight side of monetary policy. So all of this has been mattering, but it's not mattered in any sort of grand, moment of crisis.

It's more like a bunch of mini crises that string together. I think where I differ from Luke is that I think it won't matter in the true. Mega crisis sense, probably for many years with certain caveats that we could go over. So I'll stop there for a second. Before we get into that, in case you had any comment.

Erik: Yeah, I definitely want to go a lot of different directions with this. So one of my favorite Luke Gromen lines he very frequently says, deficits don't matter until they do, and then they matter a lot. That's a lot of wisdom built into that. But of course, the question is the timing. When do they start to matter?

Because all the grownups have really been talking since the 1970s about the fact that the us government was starting to move in a direction. Didn't seem to be sustainable by the 1990s. And you had Ross Perot in the 92' presidential election talking about it. Clearly those people were right about unsustainable aspects of US fiscal policy, even though they're not sustainable long term, they were able to sustain them for several decades and it's getting dangerous to say it's a, it's gonna start to matter really soon, so you better be watch out. So many people have been conditioned to just say, oh, come on. It's, everybody knows someday that's gonna be an issue, but as you just said, probably not for several years.

Why don't we just ignore it and not worry about it? Needless to say, that's what's got us here, but how do we know when we're getting close and how do we assess how close we are to that moment where all of the sudden deficits do matter and matter a lot?

Lyn: Yeah, good set of questions. Yeah.

So the late eighties, early nineties were the peak zeitgeist for the public debt being relevant. So the national debt clock went up in the late eighties. As you point out, Ross Perot really emphasized that ran the most successful independent presidential campaign in modern history largely on that topic.

And if you look at the chart of interest expense, so public interest expense. As a share of GDP. It was peaking right around that time. Prior to that for, decades after World War II into the seventies, we had falling public debt to GDP. And what was different is that in the eighties we went back to a period of rising debt to GDP.

So after, five, 10 years of that, people I think were rightfully freaking out about that trend. We're also hitting giant numbers a trillion dollars in public debt for the first time. So that combination was pretty significant. I think, a significant reason for why they were early is throughout the eighties China started to open to the rest of the world. That really kicked into the high gear in the decades that followed. And then of course, the Soviet Union fell by the early nineties. And so what we had was, this massive supply of Eastern labor and resources was able to connect to Western Capital.

And so we went into this period of renewed globalization, which is, which was disinflationary and productive. Now it came at the cost of fragility. When you globalize supply chains, you make them more efficient but fragile. And so, that gave us a wave of disinflation, a raise, sustained wave which allowed interest rates to keep falling for longer than people expected and lower than people expected.

And so we basically entered, we had a 40 year period of falling interest rates which was able to offset the rising debt to GDP. And so what's different now is a couple things. One is we are entering the more draw down heavy period of our entitlement system. So with baby boomers entering their retirement years, that's new.

That's all in the past, you know, like I said and the other big factor is we no longer have structurally declining interest rates. We basically bounced off zero other parts. The developed world went negative. At that peak, we had something like $18 trillion worth of negative yielding, Yen and euro bonds outstanding. And so now we're in this period where we no longer have some of the offsets and we have troubling demographics and we're no longer globalizing.

Even if we don't rapidly deglobalize just the sheer fact that we no longer have that tailwind of evermore productivity, evermore international connections and evermore fragility, where instead we're reintroducing local. Into the equation. We're reintroducing the concept of robustness rather than just efficiency.

It's not how efficiently can we make things with near zero inventory? It's how can we prepare for shocks along the way? And you mentioned before some of the things you warned about. Before the pandemic, people weren't yet really accustomed to really big things happening.

It was the idea that nothing ever happens. And, if anything that these past five years told us is that some really big things happened whether it's of course the pandemic, whether it's Russia, invading Ukraine, and all the, geopolitical stuff that followed there.

Of course the. Massive ongoing conflict in Gaza and the world reorienting and, emphasizing that whole situation. So we've entered a new kind of geopolitical situation where things do happen. I think there's so there's two separate answers to the question.

If we look at it from a purely quantitative mindset and this is probably where I channel my Brent Johnson for a minute. The, milkshake theory. With most currencies, as soon as investors and the public lose confidence in it. So confidence is one of those things.

It's hard to predict ahead of time at what stage it will be lost. But once you lose it, it can happen very rapidly with most currencies if they lose confidence. They can quickly spiral into disaster because there's no, or there's very little required demand for that currency outside of the country.

What makes the dollar different of course, and what gives us a longer runway both to benefit from and to hang ourself with in some ways is that there is a lot of entrenched demand for the dollar that has nothing to do with people's opinion of the dollar. It's just a bunch of contractual obligations for the dollar which mostly takes the form of debt, so depending on what source you use.

The bank for international settlements is one of the better sources out there. They show something like $18 trillion worth of offshore dollar do debt. And that's mostly not owed to the us It's mostly owed, between all entities in all these different countries. Some entity in Brazil were owe were owed to some entity in China and so forth.

And that's this big entrenched network effect of demand for the dollar. And so that's the part that, that historically, will likely move very slowly even as public sentiment around the dollar and kind of the optional side of demand. Can change very quickly just like it does for any other currency.

And so when we quantify that, when you have all that offshore debt that, that's a bigger amount of debt than there is a monetary base of US dollars. And it's smaller than, but comparable to the entire US onshore broad money supply. So that's a lot of entrenched demand. So I, going purely from a quantitative standpoint.

I think the US still has a long runway ahead, which is not to say that it won't matter. It's that the magnitude with which it'll matter will be manageable. So for example, in the seventies, the, the oil crisis very much mattered. The high inflation very much mattered but for a variety of reasons, the US and its financial system was able to get through it and then even get stronger on the other side of it.

And so at the current time, we, when we had that kind of quantitative basis that's where I get my kind of, nothing stops this train view, which is from now into the 2030s. Based on, how rapidly our money supply is growing and is likely to continue to grow with a couple of these other, physical limitations along our way, which, for example, Luke Gromen covered in your prior interview.

Things like Rare Earth things like our de-industrialized manufacturing base, all these things. So we're running these big deficits. We're growing money supply. But it's offset by this entrenched global demand for it. So I, if I were to say, okay, what could shorten it, what can make this not last very long?

It's actually less so the macro side and more the political side. We're in the era of the big headlines we're in the era of increased political polarization. We're in the era of realizing that significant percentage of our kind of structure for how governance work is less so on based on laws, is more based on norms.

And norms can be changed easier than laws. And so you could have non-linear. Dislocations where, you know, contracts that were thought to be, immutable are defaulted on or changed or major geopolitical alignments shift in a very rapid period of time. And that's the kind of hard to predict ahead of time variables that could move forward.

Kind of the estimate date for when it, it truly becomes a crisis rather than a series of mini crises. For example, in 2022. UK guilt had a crisis. Three years later it's not as though. The UK's currency is trash. Now that was a mini crisis that they handled and, they end up switching their government over it partially.

And, but they got their wheels back on the track. So my kind of base case from a purely quantitative standpoint is that over the next. Five, 10 years, we'll continue to have a number of many crises in the US and elsewhere. Those fires will be put out. There will be ongoing political polarization because the large deficit will remain in effect, people will continue arguing about them. Those in the receiving side will continue to have that higher side of the K-shaped economy, whereas those not on the receiving side will be in the lower part of this K-shaped economy. We're in this kind of sustained, run it hot, slowly meltdown type of environment with the risk of more political driven disruptions along the way.

Erik: Wow. A huge amount to unpack there. Lyn, I wanna go back to one of the first things you said, which is the secular driver of a lot of this is retiring baby boomers going from paying into our entitlement systems to drawing down from them. We're only seeing the beginning of that, Lyn. There's still a lot more baby boomer drawdowns to come.

We've only just gotten to the point where most of the baby boomers have retired. We're not even through that cycle yet, so this is going to stay. With us for a long time. There's gonna be a lot of money that has to be spent to service the obligations that we have through our entitlement system to baby boomers.

Hang on a second. We've got huge political division in the United States already, and one of the big themes is a lot of Generation Z and to some extent also the millennials who came before them, are down on baby boomers. They tend to blame baby boomers for a lot of problems in society.

Now it really doesn't matter whether those beliefs. Are justified or not justified, they hold those beliefs and we're coming into a period of extreme political division. It seems to me like you can get into a generational war out of that, where just as the baby boomers are realizing, wow, all of our benefits could be subject to a complete reversal if we get into a fiscal crisis, we've gotta really stand up for our rights and make sure that nobody messes with our social security. If that happens, just as the Zoomers are getting to the age where they're really voting actively and paying attention and feeling like, no, actually we don't.

I think the baby boomers deserve all of those overpriced entitlements. Yeah. They supposedly paid into that system, but it was publicly discussed that social security was guaranteed to be bankrupt. We're not footing the bill for this. We're gonna cut those benefits that could set up, further civil war risk, frankly, and I think we've already got some of that.

If that caused the rest of the world to get concerned about the United States, as you said, it could play out a couple of different ways. It could be. A mini crisis, although the one I just described is awfully persistent in terms of its duration. But if that causes the rest of the world to start to doubt the US dollars, reserve currency status, and especially if we have a digital currency alternative that seems better than the US dollar.

All of a sudden you could see an unwind where all of those mechanical factors that cause the artificial demand for the US dollar could start to get unwound. So it seems to me like there could be this massive, vicious cycle that just causes horrible outcomes, or it could be broken into mini crises. And as long as there's some time in between, maybe it's okay.

It's really hard to figure out what's gonna happen, isn't it?

Lyn: Oh yeah, absolutely. And, as someone who spends part of each year in Egypt I've been there during 38% official inflation, let alone whatever the kind of the real in inflation number was. And I'm sure other listeners have been in that environment as well.

So one thing I think is that, it, it takes. A pretty as bad as that was in Egypt, for example because their political situation held together it didn't spiral into something worse than it could have. And then they, at least for now, partially stabilized the issue. And so you're absolutely right that there is this extra artificial demand for dollars and that can over time evaporate and it's the analogy I've used before is that, like a more balanced economy is like someone standing straight up, whereas the US economy is more like someone leaning against a wall and pushing on it. Which is basically we have all this extra demand for our currency, for our reserve currency status.

And we run these structural trade deficits with the rest of the world to supply them. With that currency and if that wall were to give out for one reason or another we're unbalanced, we're leaning against it so we can stumble harder than we can compared to economy that's more balanced.

That, that's basically the key risk there. Now, when we analyze what, what could rug pull that wall away from us, or what could break that wall? We can analyze the four major parts of what the reserve currency status is. One is that, with. Over a hundred currencies.

Some of them are pegged, but, dozens and dozens of large free floating currencies. Most of them are not very liquid relative to each other. For example, if you wanna convert Egyptian currency into South Korean currency there's not exactly the super liquid deep market there.

Because the number of combinations between all those dozens of large currencies would, be a huge number. And so the way it usually works is that, something like 90% of currency trades dollars on one side of it. So you trade whatever currency you're starting with into the dollar, and then you trade the dollar for whatever currency you want to get to.

So you have that really big liquid network effect there that is less so about the stability of the dollar. 'cause you're potentially only gonna be in there for a short period of time. But it's more about the sheer scale and liquidity of it. The other big factor, and this one I would, I think it's already been changing, is the reserve holding of it, which is that central banks and other large pools of semi-public capital, like large pension funds and sovereign wealth funds and things like that that they will store a disproportionate share of their holdings in the dollar.

For lack of anything better as kinda the principle ledger for where to store their, accumulated current account surpluses, for example. And that's, around the margins already changing. There's not a lot of foreign demand official demand for treasuries anymore. There's a combination of increased tonnage of gold buying as well as the appreciation of gold.

We're rough at the point. Gold is flipping treasuries in terms of how much central banks hold compared to treasuries. For the first time in many decades. And, around the margins, there's a very slow diversification even to, into other fiat currencies. So I think that the kind of the more optional thing, that's the more optional type of demand for the dollar that can evaporate.

On a fairly rapid basis because that's a voluntary human decision rather than a contract in most cases. And of course the other, the two other big pillars of the reserve currency status. One is international contract pricing. So if you're buying commodities from one country, from another country, or you're selling goods and services often it'll be priced in dollars again, is the biggest, most liquid trusted ledger to do things in.

And then the other one, which I mentioned before, is cross-border lending. So all of this. Dollars denominated debt that's outstanding. Which is contractually owed. And the thing there is when we analyze how could that Gordian not be untied? The, the main way is that it can slowly stop growing the total debt as the US money supply keeps growing until it gets de Delevered or more rapidly, some of that debt could be paid back and then switched over to, for example Chinese currency. There, there are various mechanisms that can enable that. But generally speaking, there's a little bit of a chicken and the egg problem because there are entities that have dollars that owe dollars and that are owed dollars by others.

And so it's, the creditor countries are the ones that have a little bit more flexibility. In terms of saying, okay, instead of paying me back in dollars you can pay me back in this other currency, for example. But, if they still have significant dollar obligations of their own then, how do they pay dollars to, downstream who they owe.

So it, that's the complex network effect that usually takes longer to untangle than clean sheet of paper. We might expect it to. That's kinda one of those real world standoffs that's really hard to unwind. And so basically these network effects are very strong.

And the most optional one is that voluntary holding of excess currency. The other ones are. Varying degrees of involuntary. And there's tens of trillions of dollars of the US' negative net international investment position. So all this foreign capital stuffed into US equities, US bonds, to a lesser extent, US real estate and private equity.

Around the margins that can be pulled out and that, that can give us a pretty significant currency drop when it happens. We saw a kind of a very tiny taste of it around Liberation Day earlier this year. But that can of course happen on a much larger scale. So those are the entrenched things that even if we do have a significant, political feud that's intergenerational or widening ble between the the political polls that we have, a lot of that is still there. It's still contractually demanded for. I think the bigger factors from the US standpoint is, at what point do we risk just outright defaulting on certain foreign obligations, or we put up capital controls and say that capital that you stuffed into US markets that you thought you could get out, actually you can't.

Now, those types of more non-linear things is what can break things more rapidly. And so that's again, back to the political realm more than the numbers only realm. And at that point you can get these kind of big things that you know, much like the pandemic or much like a war things that you know could happen. They might go a decade or two without happening, and then they can happen all at once in a weekend. Where you wake up to like very nonlinear reactions in markets. And the defense against that is to, own assets that are not necessarily securities, things like gold or Bitcoin, things that can be self custody.

Things that are kind of outside of the "system" for those types of extreme events. And going back to the one point and then I'll stop is. I do think that the ongoing generational crisis will get worse. That's my expectation. We've already generally seen that baby boomers do vote in pretty large numbers.

The younger generation, of course, has a more spotty record with voting. And while there is a deteriorating social contract there, people generally feel that. Compared to decades ago, they don't feel necessarily that the government has their back. The way that it had prior generations and the way that prior generations generally felt about it.

They don't really feel part of a cohesive whole. They feel that, that, that say prior generations were bailed out. For example, the global financial crisis and that all the stimulus that happened in response to the pandemic, which, most analysis showed, was actually pretty top heavy in the way that it was distributed.

Despite the fact that headlines folks lot on the, the Stimy checks a lot of it was actually funneled to big corporations, to wealthy small business owners. A after a series of those types of things I do think that the younger duration is fed up. And they do take it out in terms of, more political voting selections sometimes unfortunately violence.

And I, sadly, I think a lot of that's going to get worse. And that's where you enter these more non-linear effects compared to what otherwise clean sheet of paper is what I would argue is a pretty long process.

Erik: You've used this metaphor of an unstoppable train. Nothing can stop this train.

Please be very precise at exactly what you mean by that. What is the train that can't be stopped? But then look, then every train has to stop eventually. 'cause you run out of tracks. What could stop this train eventually, even if that's away down the road.

Lyn: Good question. So I refer to the train as it's US fiscal deficits specifically.

Which is to say that I think there's very low probability in any sort of investible time horizons, let's call it five, 10 years that US deficits are going to meaningfully shrink. Now around the margins, you can add tariff revenue you can trim Medicaid, you can, there's little things around the margins, but right now we're running six to 7% of GDP deficits.

And, we're running hot in terms of nominal GDP. We're, continuing to grow the nominal size of the debt pretty significantly. And the nothing stops this train thesis is the idea that is not going to stop very, with very high level of confidence in an investible time horizon.

Now what eventually stops it I would say death by fire, not by ice, which is that they don't get the deficit under control anytime soon. But that instead it. It debases so rapidly or so significantly that the obligations are devalued enough. Things have become chaotic enough likely politically.

And then the question is in those depths. Does the United States manage to stick the landing? So for example, after World War II we devalued a lot of the debt through inflation. But then we pivoted more toward austerity after those debts were sharply devalued. We had a very, we were in the opposite situation we had now.

We had very strong demographics. We, we had a lot of the cards globally had the. Basically the only intact manufacturing base we had all the gold. We had 40, over 40% of global GDP. And so we were able to grow our way out of it after a significant devaluation. The big question here is after we have a big devaluation and a big kind of it could take the form of a significantly weaker currency, therefore defaulting on bond holders. And to your prior point, it could take the form of eventually defaulting on some portion of Social security or Medicare. And basically saying that those are just gonna nominally be lessened to some extent.

Whether it's mean testing whether it's, cost of living increases for a period of time. There, there's kind of various mechanisms that could be some type of default on basically purchasing power in that capacity. So after some degree of default, then the question is can we stop the bleeding? Can we pivot toward a period of predictive growth again that's the part that I think that remains to be seen.

That's more of a political question than a macro question. The numbers themselves are certainly fixable. After a period of sharp devaluation, the question is, can we as a country have enough of a shared vision? I think basically to, to rebuild from there. And one thing I've kinda emphasized in the past, I I've borrowed this from Ray Dalio is that you concept of the long-term debt cycle, which I think has significant, aspects to it, and both you and I have discussed the importance of the fourth turning. And, some of the pushback against the idea of the fourth turning is that it's like astrology for investors or demo demographers. Like it's this woo cycle theory and, there's, I think there's some truth to that criticism, but the reason that I give it so much credence is because behind that cyclical aspect to it, that kind of roughly 80 year cycle approach. There are a handful of specific things that grow and die or strengthening and weaken along the way. And some of those are quite measurable. And so the three that I would highlight, one of them is the long-term debt cycle.

So basically, we go through a period of recessions over decades. Every time we have a recession the central bank gets more dovish. They cut interest rates, they do quantitative easing, whatever the tool of the day happens to be. They reinflate the growth of debt. In addition whenever we have private sector contraction in lending during those recessions, we generally blow out the public deficit.

And that, keeps building and building over time as we get lower interest rates. And, we've really hit the apex of that in, in 2008. So we basically got interest rates all the way to zero. We got private debt very high. So then we started rotating it onto the public ledger.

As as bank debt and housing debt blew up we ran very large deficits. We bailed out large swaths of the system. Then we did it again basically during COVID, during the pandemic. That was another kind of shift from private sector debt, more to public sector debt. And so you pile that debt up and up.

And then once it's on the public ledger you eventually basically inflate it away. They did that in the Civil War. They did that during and after the 1940s. And, we've really done it over the past five or six years as well. It's been one of the worst environments for bond holders compared to every other asset out there.

I don't think it's fully done yet. But basically that's one cycle that happens along that fourth turning, which is basically once you get the, when it's all around the sovereign level and you enter that more. Sovereign level purchasing power default phase. That's the fourth turning. So that's one of the three big pillars that's measurable and watchable.

The second one. Is legal accumulation. So during a normal course of operation every year lawmakers create new laws they generally create more laws than they repeal. And so we get this layered bureaucracy that kind of builds up over time. It's kind if your paint scratches and you just paint over it.

And then that layer starts to scratch. So you paint over that and, a after 30 years, you've got 30 coats of paint. And that's what happens to a country's legal system. So it becomes very bureaucratic hard to operate in. People wonder why, we could build the Empire State Building in a year and a half, but California can't build, high speed rail even given seemingly infinite amounts of time and money.

It. That's one of the factors that goes into it. And so generally speaking, when you have a fourth turning, you've entered such a complex phase of the law that there are calls for, basically breaking of the norms of some of those laws outright disregarding some of those laws or big political movements to, to, reorganize and reset some of those laws.

And that's, we can think of that as like a shields down moment for the economy and for governance, which is. When you're undergoing major change allows for on one hand much better situations. You can clean out a lot of that. It's kinda if you leave your computer on and it gathers memory leaks and eventually you have to reset it.

It allows that kind of opportunity. We can streamline laws you can reorganize things. You can make sure that they're, that the laws are geared to the present day. But of course it also means that you can go off the tracks and wind up in. Either fascism or communism, you go off on one of the two sides where you're not shielded in the same way that you are in a more normal operating environment.

Basically we're entering that kind of era of, some degree of legal resets going on in addition to that long-term debt cycle. And we have those kind of playing together. And then the third one would be institutions. So institutions are generally created to solve a set of problems or social needs in one era.

And we know when you look at the fourth turning analogy is basically, after four human lifetimes or four generations, which is like one long birth to death human lifetime, the people that built those institutions are no longer around. A lot of times those institutions have become corrupted over, over generations.

Entropy, basically social entropy has taken hold. And those institutions for a variety of reasons, no longer serve the way that they once did, or at least they're no longer perceived to serve the way that they once did. And and currently when you look at, say, polls.

Whether it's organizations, whether it's whole sectors like the media or Congress there's been a major loss of confidence and trust in most types of institutions. There's been a gradual kind of building of new institutions. So in addition to the long-term debt cycle rolling over and the whole legal complexity cycle rolling over, you get that institutional birth and death. And so all those things are culminating in this environment. And again, it's not just one year. It's not like what year is the fourth turning? It's this whole era. It's basically the, as they would, the authors of that book would define it.

It basically started with the global financial crisis. It continues through this day with this kind of rising series of crises until we hit rock bottom and there's some sort of massive realignment in a particular direction and that could be a better direction. Or it could be a worse direction.

But I think that's going to continue to play out over the next five or 10 years, and that it's somewhat quantifiable and observable rather than merely, woo cycle theory. And that, that really actually does play a role in macro analysis because you do have to take into account these things that are outside of the normal Overton window.

And that can really shake up various investment outcomes.

Erik: Lyn, I think you've done an absolutely brilliant job in this interview of laying out this entire fiscal train that can't be stopped and what eventually stops it and so forth. Feels like a logical time to wrap up the interview. Oh, wait a minute.

I can't do that because I think there's something. Equally important. Another major secular trend that I see probably playing out in about the same timeframe that you're talking about over the next, quite a few years, be probably beyond the investible timeframe or well beyond the investible timeframe.

And I'm gonna call that broken money, meets broken energy. What I mean by that is we've got a serious problem with energy. And some people will say to me on Twitter, oh, whatcha you talking about? We're back down to, just above 60. Bucks on oil here. It's nothing compared to what it was a few years ago.

Forget that. Look, big picture big picture. Energy from fossil fuels already costs more than double what it cost. When I was a kid, even after adjusting for inflation over all of those years, and it's been a lot of years since I was a kid. Lyn. We're gonna solve that problem. I'm convinced that the fossil fuel source is only going to get more and more expensive compared to what it was when I was a kid.

The solution is nuclear energy, except that takes a long time and a huge amount of CapEx. You gotta be in a really good borrowing position in order to fund all of that CapEx investment in building out nuclear energy. I think you just explained all of the reasons why our borrowing ability is about to start shrinking and maybe eventually collapse.

How are we gonna solve the energy problem? That's really essential to the continuation of humanity and the restoration I think of human prosperity.

Lyn: Yeah, good question. That partially touches on the legal cycle that I mentioned, which is, for the length of time it takes to build a nuclear facility is much longer and therefore much more expensive than it used to be, in part because the legal situation just became so onerous to do that.

And, I agree with you that right now fossil fuels hydrocarbons are well under control in terms of price. I don't expect any kind of near term catalysts to pop them higher. If you asked me three years ago, what I thought they'd be a little bit higher than they are now, I would say yes.

They're chugging along as they are. I do think that as we look out, to the end of this decade. And into next decade. Kinda along this kind of time horizon we talked about, I do think we will have another bull cycle of hydrocarbon. It's basically another cycle of shortages, high prices trying to get more supply to come online.

As you mentioned, nuclear. Is a major solution. We had an, we had a whole episode together, of course called Broken Energy that I would suggest listeners check out. And, nuclear is a very powerful solution to that, but it does take a long period of time, and especially in an economy that is burdened itself with weaker human capital.

Like basically know how to build them. The legal situation that makes it hard and costly to build them. So I do think that we'll have another energy crisis along the way, which is solvable. But basically the longer that is delayed, basically the more that we have energy supply flowing well without disruption, that adds runway to the political situation.

Whereas, you can imagine right now if we had the current political situation where we had oil at, 150 or 200 a barrel. Imagine what do to politic climate as it now, and both domestically in the US as well as globally between nations. What would that look like? I think in the years ahead we could certainly find out, I mean if you look at US shale oil, so if we back up the various reasons, and maybe you have something to add, but if you back up the reasons of why Energy's cheap, there's a bunch of reasons.

One is of course the 2010s. We had a lot of unprofitable drilling combination with low interest rates and, the application of technologies to get, shale oil outta the ground. So even though we had peak conventional oil. According to estimated timelines, we had all that unconventional oil come to market.

And, the war in Eastern Europe hasn't taken barrels totally off the market the way that, that some feared that it would partially, that's a political choice. Europe found themselves not really in a position to, to really get Russian oil off the market.

So it's still find its way to market just through various frictions along the way. And right now at the current time with current prices, US shale production is rolling sideways to over. The price was not significant enough to incentivize enough drilling to both offset the depletion rates as well as substantially add more.

So far secretary Bessent. Goal to, I believe it was increase production by 3 million barrels is not really playing out. We're not really directly going in the way that he expected in large part because the prices don't support it. And in fact, some of the some of the kind of the goals conflict because they wanted cheaper oil, but they also wanted more oil production coming to market.

And really the only way that could work is if you just outright. Subsidize them which they've not done. And basically I think that in the years ahead that kind of weaker supply from shale will impact things as well as, any other geopolitical disruptions that could happen.

And while there are more unconventional sources that can come to market. That generally requires both high prices and sustained prices. Basically some of the deeper water stuff, some of the Arctic stuff these, the underwriters of those projects, especially in a geopolitically complex world where there's more kinetic risk in various parts of the world and sanction risk and geopolitical feuds over places. The willingness to finance those longer term operations has to come with pretty high confidence that the energy prices are gonna support it profitably. And so I do think that we'll have another cycle of energy shortages, higher energy prices which, again is solvable.

But then when you have that hot political mix. Already happening and you're already in fiscal dominance. That's where it's a powder keg. That's where you get things like, financial repression, like you get another inflation spike. But instead of raising interest rates, central banks are captured and they're just keeping interest rates low and debasing the currency anyway.

And that's the, I think, an example of a mini crisis that can happen along the way. And of course, in many crisis, poorly handled can become a mega crisis. And so it's hard to predict ahead of time how that would be handled. But I do expect more of those issues along the way. And the, the earlier that, that people can get ahead of it, the better.

If we have a kind of a general global realignment that nuclear energy is good then that can alleviate the eventual problem, by starting earlier rather than responding to it as it happens or after it happens.

Erik: Listeners, you'll find a link in your research roundup email to the broken energy interview, which Lyn described as she was speaking.

Lyn, you know the drill here. Before we we close. Tell us about what you do at [Lyn Alden Investment Strategy](), what services are on offer, and how people can follow your work.

Lyn: Sure. So I have a low cost research service, that people can follow. I'm also a general partner at [Ego Death Capital](), where we do venture related investments.

And so thank you for having me on and congrats again on having 500 episodes under your belt. What does it feel like?

Erik: Lyn, as I said earlier, for me almost 10 years of Macrovoices, it's mostly been about the people that I've met and the way that people have challenged my thinking, and particularly the reward for me is in, touching a few people's lives.

And I, I really feel proud of you. I hope that doesn't sound condescending, but I'd like to think that we played a role in your success and it's just fantastic to see you doing all the things that you're doing.

Lyn: I appreciate that and I'm hope hopefully to be back one day and I wish you continued success with everything you're doing.

Thank you,

Erik: Patrick Ceresna and I will be back as Macrovoices continues right here at [Macrovoices.com.]()