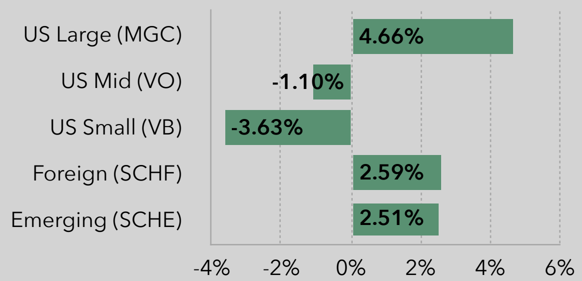
March 2023

Economic Data

- Only 236,000 jobs were added in March, but the unemployment rate edged down to 3.5%
- Retail sales were were down 0.4% in February dragged down by a 4.0% decline from department stores
- Y/y inflation (CPI) slowed a half-point in March to 6.0%—the 21st month in a row at or above 5%
- Existing home sales snapped a 12-month slide by jumping 14.5% in February; median prices were $363,000, down 12.3% from its $413,800 August peak

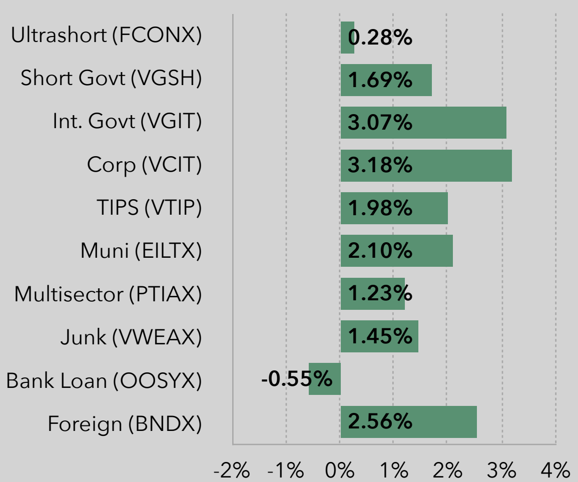
Stocks

March Returns



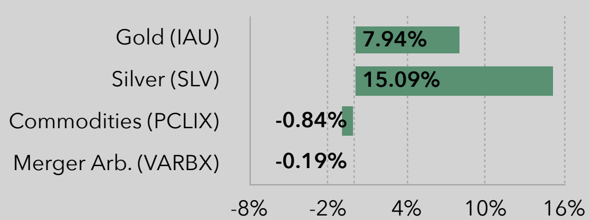
Bonds

March Returns



Alternatives

March Returns



Performance data provided by Morningstar

The brain uses two systems to process information. The first type is intuitive but lazy, rapidly forming judgements with no conscious input. The second system is slow, reflective, and not guided by emotions. It is that second system — type 2 — that we want in control of our investment portfolios.

Are the Dollar's Days Numbered?

I have had a couple different clients ask me about the safety of the US dollar in the past few weeks, both with specific reference to other countries transacting oil trade in their own currencies and moving away from the petrodollar. I have also seen a lot of headlines about this recently, so let's address it. First, what exactly is the petrodollar? If you're imagining some Disney Dollar-like scrip, with a cartoonish image of the Iron Sheik on the front and a gushing oil derrick on the back… I mean, that would be really cool, but no.

The petrodollar is just a term used to reference the fact that oil is priced and traded in US dollars, even between non-dollar countries. How did that come to be and why does it matter? Prepare to be wowed with a fun and riveting history lesson on global reserve currencies.

Before we talk about the petrodollar, we need to set the table. During World War II, many countries turned to the US for weapons and supplies and they paid in gold. With depleted gold reserves, a return to the gold standard was not possible for many countries after the war. Instead, 44 countries met at Bretton Woods, New Hampshire in 1944 and an agreement was made in which countries would now peg their currencies to the US dollar, which was still backed by gold. Instead of gold reserves, these counties started holding dollar reserves and buying US Treasury bonds. This, along with economic dominance, set the US on a quick path to becoming the world's global reserve currency.

In 1971, President Nixon abandoned the gold standard and the Bretton Woods Agreement collapsed. This set the stage for a decade of high inflation, but there were other factors contributing to that as well. On October 6, 1973, an Arab coalition of armed forces led by Egypt and Syria launched a surprise attack on Israeli forces occupying the Sinai Peninsula in what would become known as the Yom Kippur War. We supported Israel in the conflict, and in retaliation the Arab nations of OPEC placed a trade embargo on the US. Being cut off from this oil supply caused a massive energy crisis here. There were shortages, long lines at the pump, strict rationing, and the price of oil quadrupled. It was a disaster.

Nixon sent a small team over to the Middle East to negotiate. On June 8, 1974 Secretary of State Henry Kissinger signed an agreement with Saudi Arabia. We would give Saudi Arabia technology, support with economic and educational development, and access to military training and weapons. In exchange the US would buy oil from Saudi Arabia in dollars. The US was already the biggest economy in the world and the largest consumer of oil, so pricing in dollars made sense. The Saudis would in-turn *secretly* plow that money back into US Treasurys for safekeeping. That secret was kept until 2016, when the Freedom of Information Act was utilized to reveal that the kingdom owned $117 billion in Treasury bonds, but the real figure is likely a multiple of that.

The real beauty of the plan was that it would allow the US to fund its deficit spending…well, forever. Or at least as long as the world went along with it. I can't overemphasize how huge of an advantage this is to us. We get real things from other countries, and in return give them an entry on a ledger that we can essentially erase by hitting the print button. This has funded untold amounts of infrastructure spending, economic growth, social benefits, military dominance, and the US's influence over the rest of the globe. It's certainly an advantage we would be very foolish to put in jeopardy of losing.

Anyway, last year the Biden administration overplayed their hand when they went after Russia. It's one thing to sanction a small county like Cuba, or a hermit kingdom like North Korea, it's another thing entirely to go hunting a grizzly bear like Russia that feeds and fuels a lot of the world. China, India, Turkey, and a host of other countries didn't go along with it, and why should they? By freezing Russian assets, we also let the world know that their money wasn't safe with us. We cut them out of our financial system, and by doing so forced them to create a new one. One that by its nature will compete for market share. Now Brazil, Russia, India, Chinas, and South Africa (BRICS) are in talks of creating their own currency to break free of the dollar. Other countries, like Malaysia (where I currently am, incidentally), are also getting serious about reducing their dependence on the US dollar.

Does this mean that the dollar's demise is imminent? No, these things don't move that fast. The political missteps will certainly accelerate dedollarization, but it's not happening overnight and we won't be dethroned in the next couple of decades. The US dollar will continue to be the dominant reserve currency of the world, but will just have to get used to sharing increasingly more reserve currency shelf space. This is nothing new. The Euro made big inroads in the early 2000's, and the Japanese yen, British pound, Canadian loonie, and Australian dollarydoo, along the Chinese renminbi, each have a small slice of the pie, too.

Binge Box

1883 (Paramount+)

1883 isn't explicitly a screen adaptation of the classic video game *Oregon Trail*, but it sure does feel like it. It's got it all: fording the river, hunting for game, selling oxen, and dying of dysentery. And with a cast made for westerns that includes Sam Elliot, with his husky voice and bushy mustache, Faith Hill, Tim McGraw, and even a little Billy Bob Thornton for good measure, this show is a must-watch. It's actually a prequel to *Yellowstone* with Kevin Costner, which I haven't got around to watching yet but might have to.

Tactical Asset Allocation					
Asset Class	Heavy Under-weight	Under-weight	Neutral	Over-weight	Heavy Over-weight
Fixed Income			●		
Duration	●				
Inflation				●	
Credit	●				
Foreign			●		
Equities		●			
Large Cap	●				
Mid Cap		●			
Small Cap			●		
Developed Intl.	●				
Emerging		●			
Alternatives					●
Commodities					●
Hedging					●

The US dollar will eventually lose its status as the world's global reserve currency. That's the nature of the ebb and flow of empires. A look at the last six centuries of reserve currencies tells that story:

- 1450–1530: Portuguese real 🇵🇹
- 1530–1640: Spanish silver dollar (piece of eight) 🇪🇸
- 1640–1720: Dutch guilder 🇳🇱
- 1720–1815: French Franc 🇫🇷
- 1815–1921: British pound 🇬🇧
- 1921–1930 : US dollar briefly becomes the dominant reserve currency following WWI before yielding to the pound again during the Great Depression 🇺🇸
- 1930–1954: British pound 🇬🇧
- 1954–present: US dollar 🇺🇸

The previous five global reserve currencies have held the mantle for an average of 99 years each, while the US has held the honor for a combined eight decades. There will continue to be massive amounts of trade done in the US dollar, and it will still be viewed as a stable currency that is easy to access and trade for the foreseeable future.

So how do we trade on this? Well, we don't, really. It's hard to trade on things that might take decades to materialize. We do, however, build robust investment portfolios with an eye towards secular trends like these. We hold international and emerging market stocks that are not dollar-hedged and so will, all else equal, go up in value if the dollar falls. We hold treasury inflation protected securities (TIPS) to hedge the loss of purchasing power that comes with a currency in decline. Lastly, we hold commodities, particularly silver and gold which have been viewed as sound money for millennia.

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About EmeraldSpark

EmeraldSpark Investments, LLC is a Registered Investment Adviser based in Chicago, IL. We were founded by Ryan P. Layton, CFA in 2015 to provide personalized financial planning and fiduciary investment management services to select clients. Our investment process blends the foundations of Modern Portfolio Theory with the latest research in the field of behavioral finance. We specialize in asset allocation and investment due diligence to help provide our clients with investment strategies personalized to match their specific goals and risk comfort zone.