Twitter Thread by Clay Finck



Clay Finck
@Clay_Finck

Ray Dalio understands the macro environment as well as anyone.

While most investment managers were down big during the Great Financial Crisis, Dalio's fund was up 8.7% in 2008.

Here is how Dalio views our global economy today:



In order to prepare for the future, it's important to study history and see how things have played out in the past.

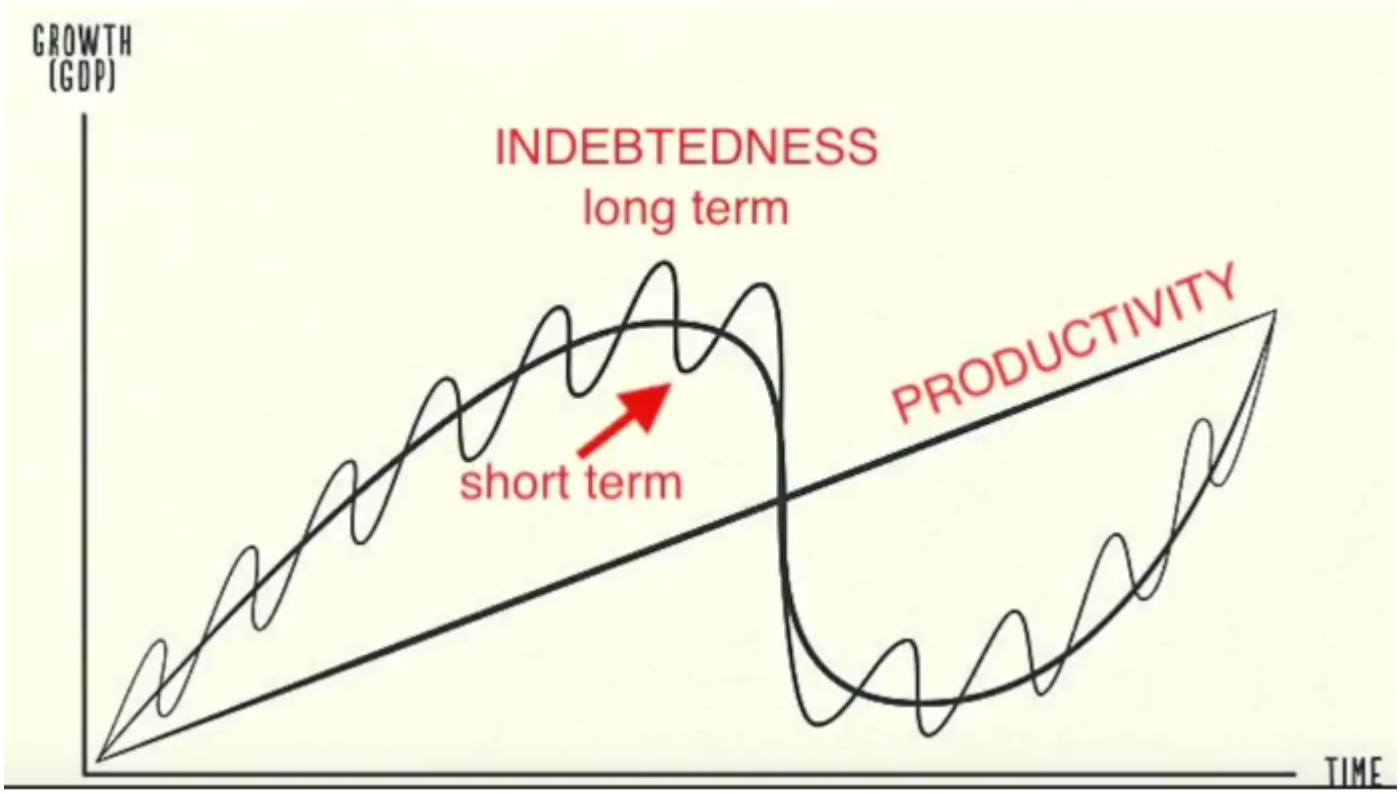
In his book, Big Debt Crises, Dalio studied more than 48 debt crises that have occurred throughout history.

Our global economy from a high level is driven by three things:

- Productivity Growth
- The Short-Term Debt Cycle
- The Long-Term Debt Cycle

In the long run, the economy is primarily driven by productivity

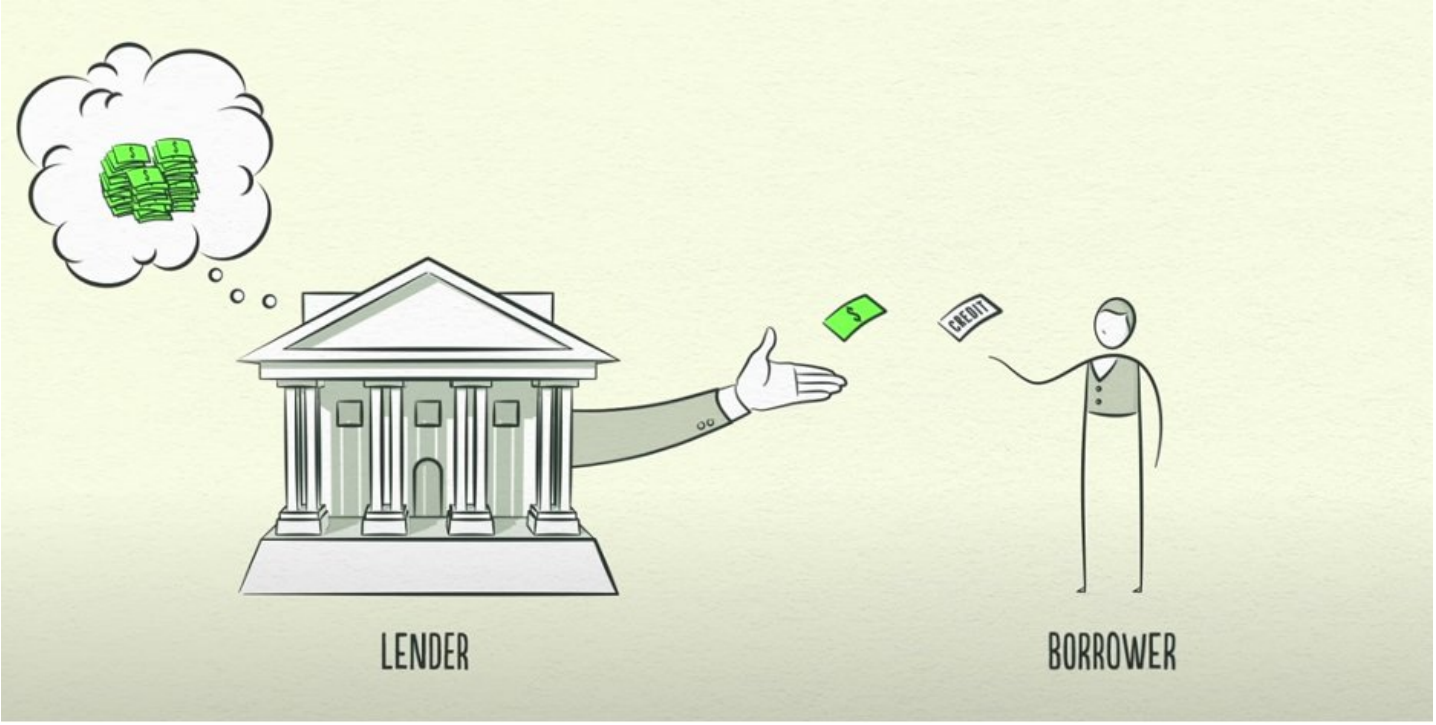
In the short run, the economy is primarily driven by credit and debt



According to Dalio, credit is the most important part of the economy and the least understood.

Dalio defines credit as the giving of buying power.

The buying power is given to the borrower in exchange for a promise to pay it back, which is debt.



Credit can be a good thing because we can purchase something today that we otherwise wouldn't be able to.

It's especially good when credit is used by individuals and businesses to expand the production of the overall economy.

Credit and debt eventually become a problem if the debt levels reach a point where the debt can't be paid back.

Dalio warns that throughout history, most countries eventually run into debt crises because policymakers generally err on the side of being too loose with credit.

Credit and debt naturally create cycles in an economy because when credit is issued, the person taking on the debt is spending more than they make today.

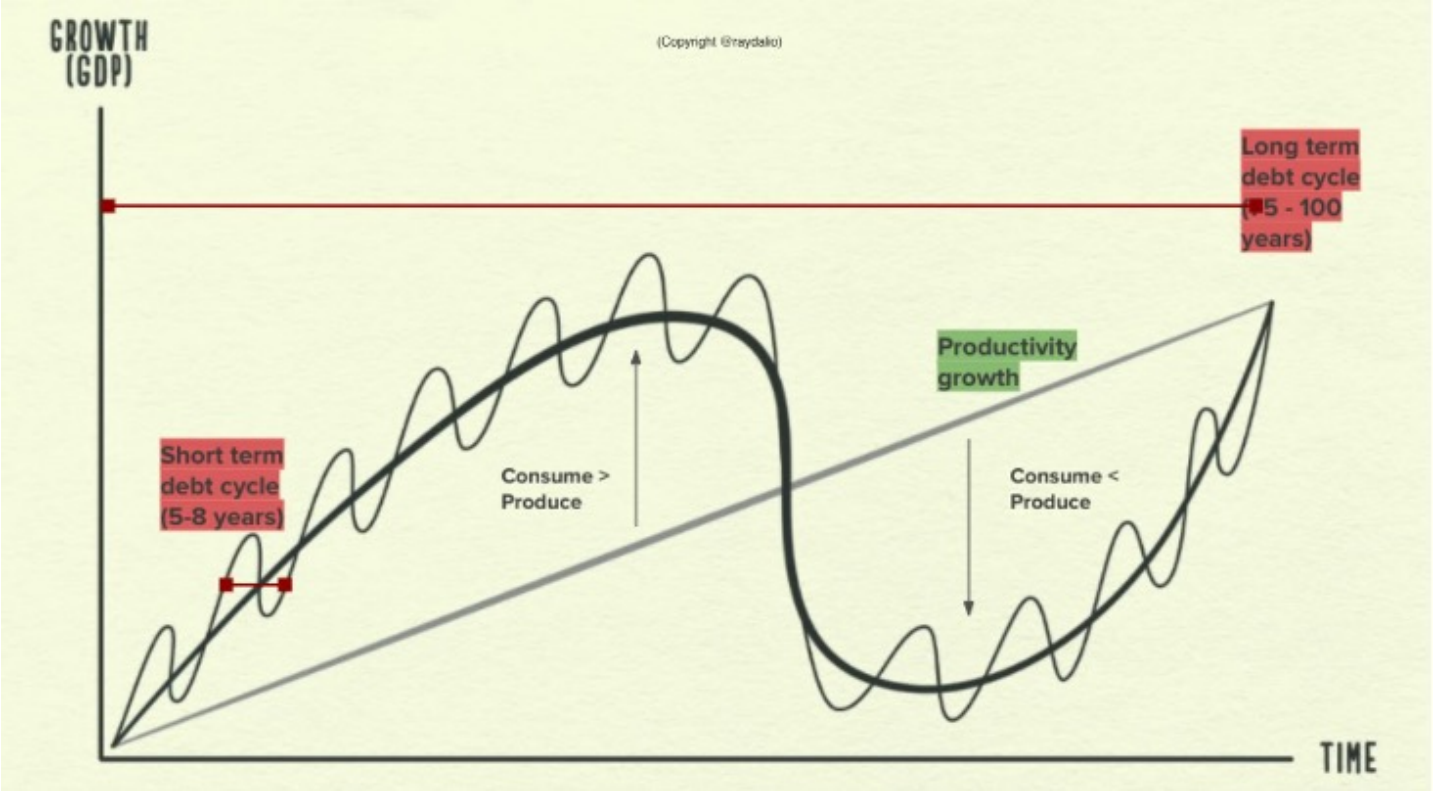
In order to pay that back, that person will need to spend less than they make at some point in the future.

These credit cycles are self-reinforcing on the way up, and the way down.

More credit ➡■ more spending ➡■ higher incomes ➡■ higher asset prices ■

Less credit ➡■ less spending ➡■ lower incomes ➡■ lower asset prices ■

Credit exacerbates the natural boom/bust cycle.

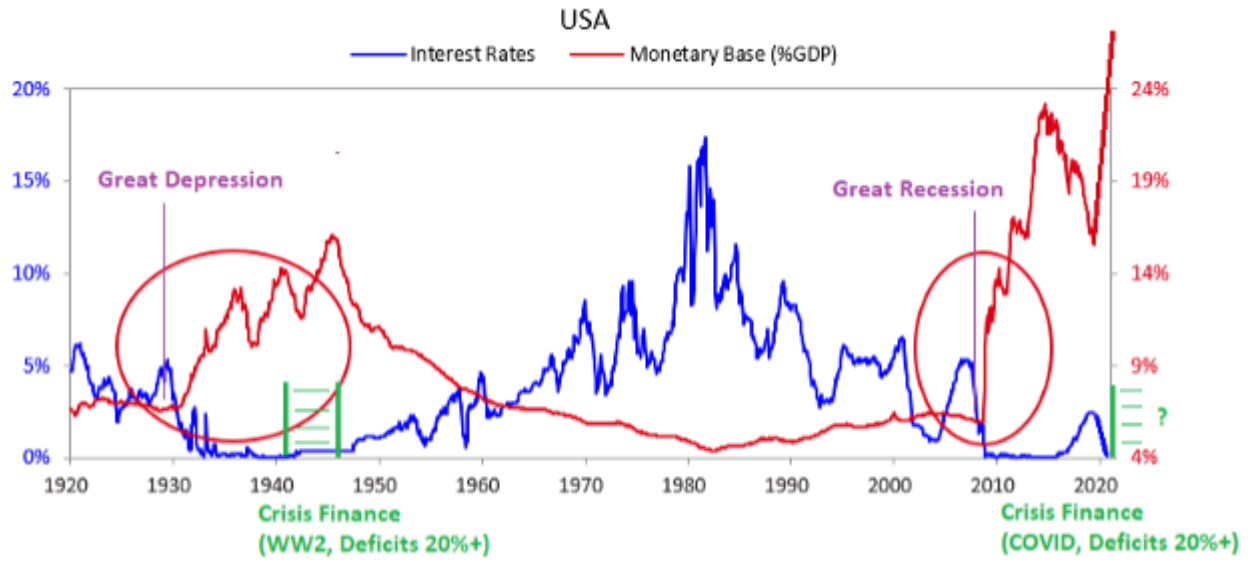


Historically debt levels become unsustainable every 75-100 years, creating the long-term debt cycle.

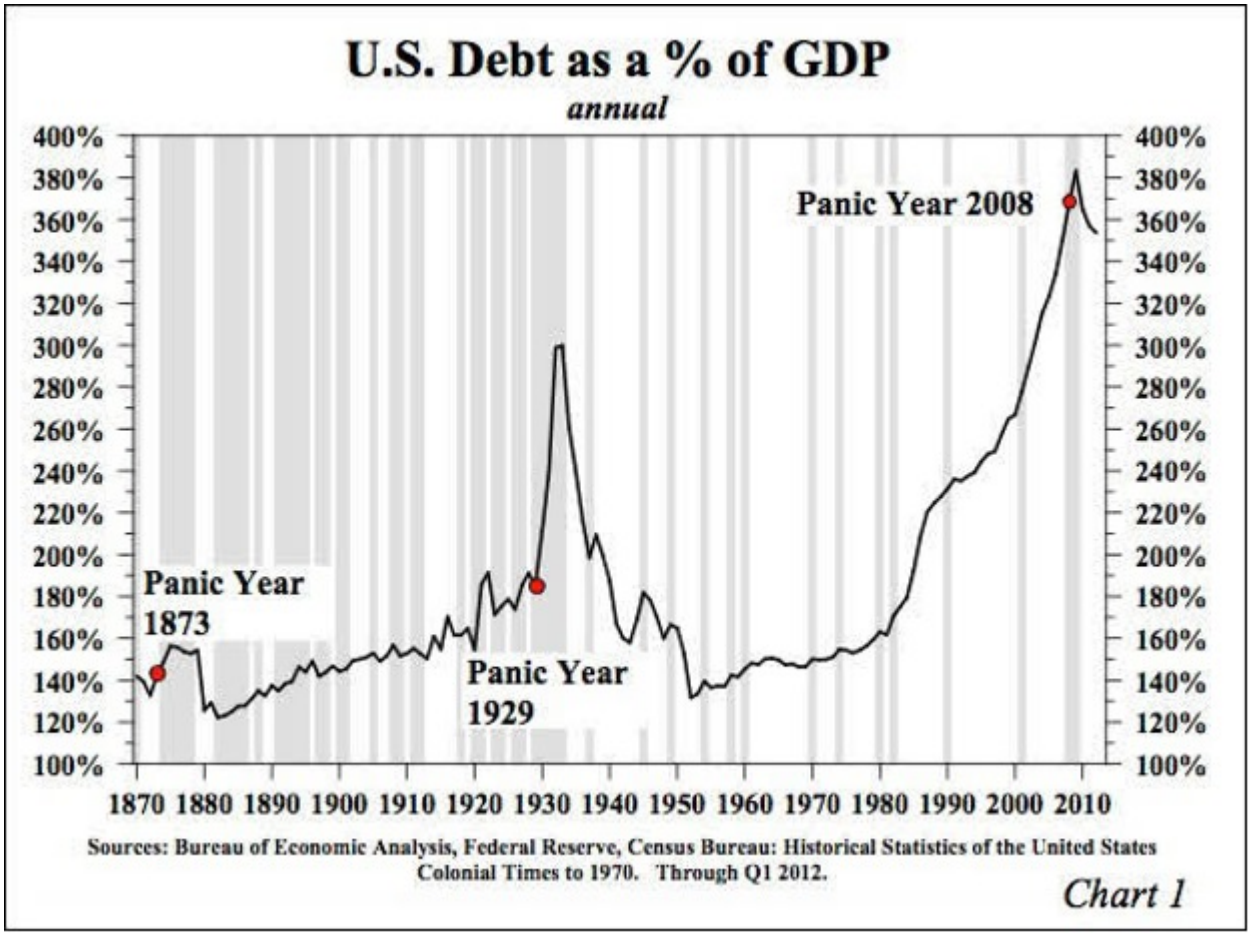
The short-term debt cycle, widely known as the business cycle, occurs roughly every 5-8 years.

The telltale sign of the conclusion of the LT debt cycle is when interest rates hit 0%.

Interest rates are a key driver in debt accumulation, as cheap money incentivizes individuals, companies, and countries to take on debt at artificially low-interest rates.



The US hit the end of a long-term debt cycle in the 1930s, and in 2008 during the great financial crisis.



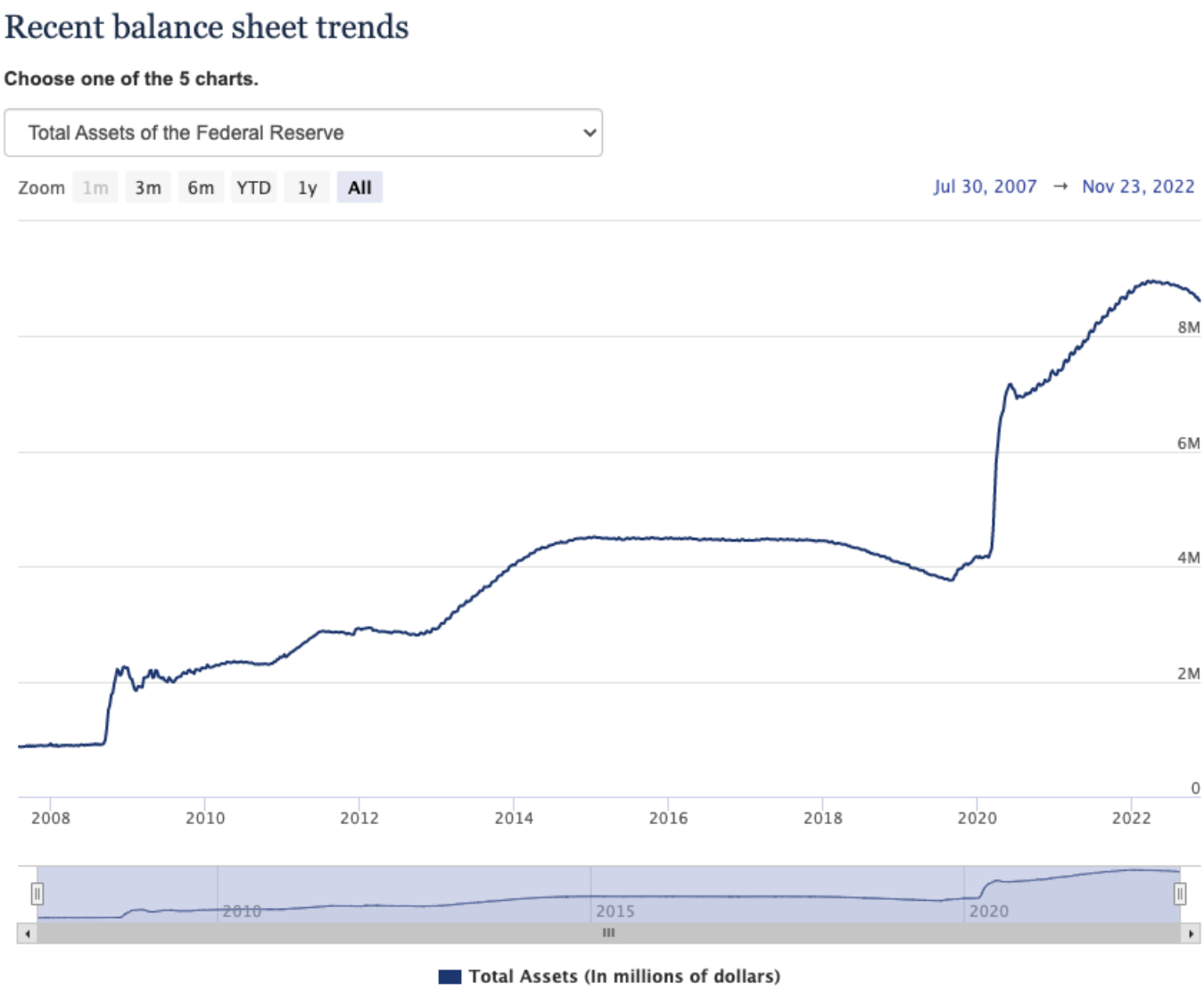
There are four levers policymakers can use to deal with the underlying debt issues

- Austerity (spending less)
- Debt defaults/restructurings
- The central bank printing money
- Wealth redistribution

Time after time, policymakers choose money printing as the primary tool to handle these debt issues, which results in major currency devaluations.

It’s the easiest way out and the most effective tool relative to the other options.

This has been the Fed’s playbook since the GFC.



So, where do we go from here?

Going forward, I expect:

• The Federal Reserve funds US government deficits, leading to continued currency devaluation relative to real goods and services.

• Artificially low-interest rates with negative real rates.

Here's Dalio explaining why:



Tough economic conditions are likely ahead, so good rules of thumb include:

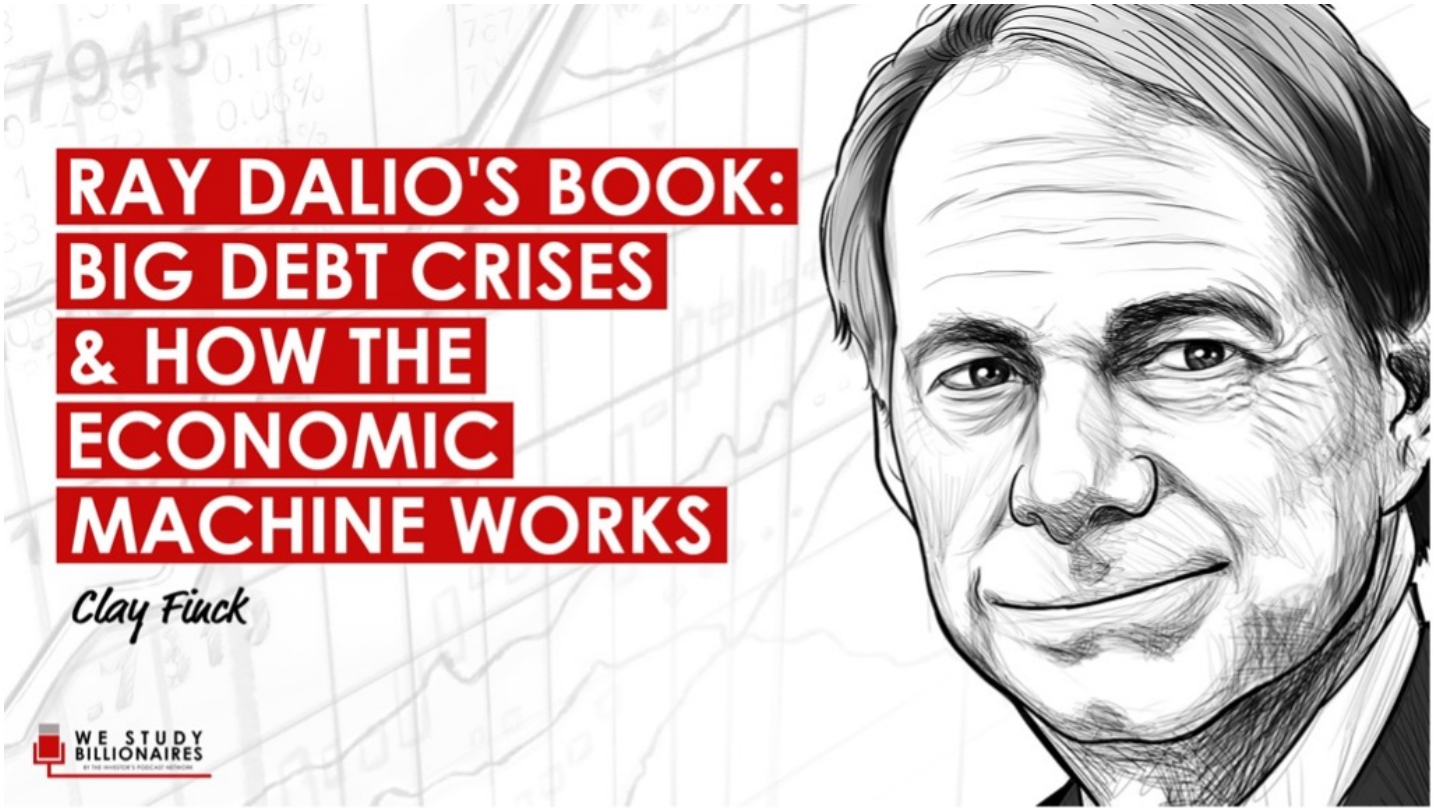
• Have a solid emergency fund
• Live within your means
• Eliminate unnecessary debts
• Own a diversified portfolio
• Own quality, cash flow positive companies

Focus on what you can control.

Special shoutout to @LynAldenContact as well for her great work on the subject:

https://t.co/8zDSOeubbi

If you'd like to learn more about Dalio's work, be sure to check out my recent podcast episode here: https://t.co/dGc141Jtzf



If you found value in this thread, be sure to like & retweet the first tweet so others can discover Dalio's brilliant work: https://t.co/RdgGyGgW6r

> Ray Dalio understands the macro environment as well as anyone.
>
> While most investment managers were down big during the Great Financial Crisis, Dalio\u2019s fund was up 8.7% in 2008.
>
> Here is how Dalio views our global economy today: pic.twitter.com/rXFusmWVrk
>
> — Clay Finck (@Clay_Finck) November 29, 2022