Stagflation Investment Strategies

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Investors old enough to remember the inflation of the 1970s will remember the term stagflation. Stagflation is the term invented to describe when the economy is growing slowly, unemployment is high, and inflation is rampant. A formal definition is when the gross domestic product declines while there is inflation. The market is already starting to see "stagflation trades!" In this article we look at what stagflation investment strategies might be useful if this next decade is back to the 70s.

Origins of 1970s Stagflation

As the 1970s were ushered in, the USA had been at war in Southeast Asia six years since the Tonkin Gulf Resolution and for more like twenty years supporting France's efforts to retain its colony, French Indochina. The costs of that war were coming to bear on the economy and on society. And, during the Johnson Administration from the death of President Kennedy in the fall of 1963 until he left office in early 1969, the former Texas Senator, Vice President and then President ushered in a host of social programs such as Medicare. The economy had been heating up and inflation was rearing its head to the degree that President Nixon instituted wage and price controls which were a disaster. Then the Saudis embargoed oil after the US supported Israel in the 1973 war after which they confiscated US oil assets in their country and raised the price of oil.

Government Stimulus Policy

What was "gospel" at that time for many in government was the idea that the government could stimulate the economy and create jobs by pumping money into the system. This came from the British economist, John Maynard Keynes. Every time the economy lagged a bit, Congress dropped taxes or spent money on something. This approach tended to win votes for the party in power but the national debt started going up to the point that Senator Dirksen of Illinois commented, "a billion here, a billion there, and pretty soon you are talking about real money"! His irony seems to have been lost on Congress then and now as today he would say a trillion here and a trillion there. The bottom line was that along with other factors, this was a huge reason for the stagflation of the 1970s.

Will We See Stagflation Today?

This is not 1970 although we just got out of Afghanistan and we were ready to leave Vietnam back then. We are no longer dependent on Saudi oil after fracking has taken hold and the US is pivoting to solar energy and other sustainable sources. Today the interstate highway system is in dire need of repair as are ports, airports, bridges, internet infrastructure, and dams across the country. Biden's infrastructure pack in its original form was to cost $3.5 Trillion which many have said would be a budget buster and lead to more inflation. However, economists are generally not worried about long term spending that tends to increase productivity and economic efficiency. A concern of many is the list of “social program” expenses that include child care. But, even that expense holds the promise of getting more working age women into the workforce instead at home watching the kids which would tend to remedy some of the current labor shortages. As such, we think it is a tossup as to whether we see a repeat of the 70s.

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We recently wrote about whether or not [investing in commodities]() was a good idea for [balancing your portfolio](). Although commodities are more a matter of trading futures (unless you hoard gold), this could be a good idea if you want to guard against inflation. During the terrible stagflation of the 1970s gold rose ten-fold in price while commodities like corn and wheat went up by three and four-fold respectively. Likewise real estate went up in price, especially in areas that were already highly priced. Farm land multiplied in value as their crops increased in value as well. If you don’t buy to buy and hold gold, consider a gold ETF.

Although the Dow went up by less than 5% during the 1970s some stocks did well. You are not going to buy and hold commodities like cattle and corn but companies with commodities in the ground like mining stocks for gold or in this era, [strategic minerals]() are likely to be good bets if inflation gets out of hand.

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