Transcript: Quantum Economics and Financially Transmitted Diseases

Featuring: Marin Katusa

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Synopsis: Marin Katusa, founder of Katusa Research, explains why he calls negative interest rates a "financially transmitted disease." He reveals how negative interest rate policy (NIRP) affects savings rates and the rest of the global economy. He talks about the potential for further negative rates around the world, as well as the prospects for NIRP in the United States. In the face of a dismal global macro picture, Katusa argues that exposure to U.S. dollars, precious metals (especially miners), and bitcoin will bolster portfolios through turbulent times. Filmed on October 10, 2019 in Vancouver, Canada.

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MARIN KATUSA: Negative interest rate policy that the bankers are using as the new stimulus, I call it an FTD, a financially transmitted disease.

It goes back to my days-- I used to teach calculus quantum mechanics essentially was you can't take the square root of a negative number then they said, we'll introduce an imaginary variable and voila, long story short, you get quantum mechanics. That's essentially what we're doing in this new quantum economics with negative interest rates. If we're at negative three quarters, why can't we get to negative one and a quarter, negative one and a half? That's what happens in an FTD. This is going to spread virally.

My name's Marin Katusa. I'm the chief investment strategist at my own firm, Katusa Research, and we run one of the largest funds in the resource sector.

What macroeconomic policy will have the greatest impact on the global economy going forward?

I think without a doubt, it's a negative interest rate policy that the bankers are using as the new stimulus. I call it an FTD, a financially transmitted disease. I don't think investors or the media or even the central bankers truly understand the implications that this FTD will have for portfolios co-stemming from pension funds to retirees to even sovereign wealth funds down to regular portfolio managers. We're in like I call the Keynes's quantum economics where when they originally modeled this, there were no negative interest rates. Everything's in this new uncharted territory and I think it's going to have drastic effects across the board.

There's this misconception that your mortgage is going to be cheaper, people will be able to get access to cheaper money. That's not how it's going to work. The velocity of capital is going to really, really slow down and it's going to be a select few that get access to this cheaper negative interest rate policy money. It's going to have drastic negative effects such that almost like in China where you have the government rate and then the shadow market rate, I see that happening in the rest of the world now, and it's going to have serious implications.

What impact will negative interest rates have on, inflation or deflation?

Without a doubt, my opinion is it's deflationary. If you look at what the impacts are, and I wrote 40 pages on this in my publication, the amount of capital chasing the fixed number of goods is going to be less hence that's deflationary. You look at the velocity of the capital is also going to slow it down, so it's going to have this double impact and again, a lot of people think this is a short term fix like what QE was. I'm taking the other side of that bet, I think it's going to last a lot longer and negative interest rates are going to go a lot lower.

For example, if you look at how these bonds are trading, so you got the negative interest rates, so first thing and you ask yourself is who the hell wants to take a negative interest rate bond? That's not these bond managers are looking at and going, "Holy crap, it's trading at like a 30%, 40% 50% premium." That's what they're looking at. They're willing to cut that in so they get their bonuses, and they get all the numbers that work for them. It's this self-fulfilling prophecy and rather than returning 35%, maybe they'll return 20%.

They'll go a little bit deeper on the negative interest rate. This is the spreads going to keep getting bigger and bigger. That's what I see happening here.

How much further negative can interest rates go?

10 years ago, no one would have ever thought that this would even be where we are. It could go a hell of a lot lower. Could it go negative two and a half? Sure. Why not? It all comes out. It's all relative basis. It goes back to my days, I used to teach Calculus. Quantum mechanics essentially was you can't take the square root of a negative number then they said, we'll introduce an imaginary variable and voila, long story short, you get quantum mechanics. That's essentially what we're doing in this new quantum economics with negative interest rates. If we're at negative three quarters, why can't we get to negative one and a quarter, negative one and a half? That's what happens in an FTD. This is going to spread virally.

What impact will negative interest rates have on real people?

It's going to be awful. Yet they think it's a good thing. Really, they're injecting themselves with this FTD thinking that it's going to help them. They think it's a steroid for themselves, when in opposite, it's a virus for their portfolio. For example, say you're a 55-year-old guy, you're going, "Wow. I got this mortgage, I can refinance it. My kid's a useless millennial, he's probably going to move in in the basement with his girlfriend and they're not really doing anything. They're trying to find themselves in their art career, whatever the situation may be." They're going, "Well, I'll refinance my house. I'm all for negative Interest rates," but what they've realized is you're not going to get a negative interest rate mortgage, okay. That stops there.

Secondly, their portfolio, their pension funds are going to be significantly impacted because these pension fund managers to base when they started this 30, 40 years ago, when they started in their careers, they expected it between 5% and 7% earnings year over year and the thing but you're not getting that in the bond market. It's turning everything upside down. Their investment returns are going to shrink significantly, but pro rata, their cost of living and access to capital for the average working person, the average person who needs that capital to sustain their mortgage or cart, they're not going to get negative interest rate, they're not going to get any of the relief.

No one truly understands what's going on here, and hence why the central bankers are kicking the can down the road and the politicians are totally okay with it, because everyone lives on this four-year cycle and they're not understanding the long term implications. This is why I said in this case, believe it or not, the US dollar actually wins and gold wins. Those are the two places that I think people should have some exposure and a lot of people go, "Well what about Bitcoin?"

I go, "Sure, why not?" Have a little bit in it. I'm no Bitcoin expert. What I did was I put a significant amount of money on one of the largest shareholders and who I think is a super smart guy who's really focusing on Bitcoin and industries that I'm not paying attention to. Yeah, have yourself exposed to areas that should benefit from this FTD that is happening virally.

How widespread could negative rate mortgages become?

You got to look at who's getting it, how they qualify and you can argue that here in Vancouver, there's so much subsidized housing that in downtown, some poor bastard's spending three and a half million dollars on a two bedroom apartment and then next door to him is a subsidized housing at 80% subsidized so technically, that person has a negative cost of living versus his peers. You first has to ask yourself, who got that, but more importantly, what the size of that mortgage is. I just don't see the bank getting to that point because they we're in a basically socialist state, then at that point, you're going to get taxed on your cash and your portfolio and all sorts of things.

Interestingly enough, a lot of people don't know that in Canada, pre-World War II, you used to get dinged a tax 3% on your assets that were deemed in your portfolio. Back then, they take your cash and your assets, whether you own stock in a railway or whatever, in the bank, and they charge you 3%. You'd have to pay that in hard cold cash. Now, they changed things with property taxes, and they took that tax away. Eventually, I do see that also coming back because the pendulum sure is swinging into-- I don't see people getting negative interest rates for houses because then, it just how do you control things. Just then we truly are in a quantum realm of economics, which doesn't make sense at all.

What happens to savings rates with negative interest rate policy?

In a negative interest rate policy world, people are recognizing-- they'd eventually realized that, "Oh crap, I'm going to retire and I'm not getting the returns I expected to have. I'm somewhat fiscally normal, maybe not conservative, but fiscally, I got to figure out how to pay ends meet." It's going to affect the economy because you're not going to do those spontaneous purchases that you regularly did, you're not going to do the vacations or the big dinners. Instead of buying a $200 bottle of wine on your anniversary, you might buy a $50 bottle of wine or $40 bottle of wine.

That's just the natural evolution of these things. As people start to retire, they start planning and becoming more conservative, and that's going to have its ripple effects across the board. It's going to force people to save, then the irony will be then the government will probably bring in some tax on the savers. The government's going to screw you whichever way you think and that's just how it is.

What about bonds?

I actually see that the trend will continue. As negative interest rates decrease and they'll continue, there's going to be a new junk bond era where it's not based off of the old valuations we've seen. For example, the Austrian bond was up over 55% at a negative point six, and the bond managers were all over it. Maybe the next savvy banker will say, "Hey, we'll do point negative seven, and we're happy with yielding 35% or 40% on the trading of the bond."

That's the realm I was talking about earlier. I see that continuing longer than people expect, because people are going to have to put their money somewhere. They're not actually now the bond market, a way to think of it is it's no longer paying the bond for the yield. It's actually paying the bonds for the return on the bond, if that makes sense.

What is your outlook on the U.S. dollar and gold?

Let's talk about how the US dollar plays its role in the resource sector. Over 90% of all capital infrastructure in debt globally is financed in the US dollar. Pick any commodity you want. Let's take uranium for example. The world's largest producer of uranium is called Kazatomprom. The Soviets drilled out this time stuff back in between World War II all the way to the fall of the Soviet Union. Kazakhstan has these incredible uranium fields that produce-- it what's called unconventional but really the majority of the world's uranium is produced via IRS, used to be called ISL but now, it's called ISR. I call it the conventional way of doing it now because it's the majority.

How they funded this was really clever by the Kazakhs and the Russians. If you ever go to Kazakhstan, the languages, Russian Cyrillic, the Russians are still there. For people to think that the Russians aren't involved is a fool. Half of the production goes to Russia. The Russians and Kazakhs are completely aligned, but what they did brilliantly here was they brought the foreigners so like the company Orano, used to be called Areva, that's a French national company. They brought their money to fund the development of these fields.

Cameco, Canada's largest producer of uranium, they brought their funds and I'll use them specifically as an example. They used to be the world's largest producer of uranium, they're third now. Back about 12 years ago when Cameco struck a deal with Kazatomprom on the Inkai project, it was 60% Cameco, 40% Kazatomprom. World class deposit, nothing against it, makes money at $12, $13 uranium. Cameco put up 100% of the money for it.

Then as time happened, Cameco started getting their returns, they get back. The Kazakhs, so let's call them the Soviets, the former Soviets, said, "Hey, Cameco, we're doing all the work. This is our land, our costs are going up a little bit. Let's renegotiate." Today, it's 40% Cameco, 60% Kazatomprom. I say that this trend is emotion. That's part one of this.

Part two, the CapEx is built, you have sustaining CapEx or OpEx we call it in mining, but generally the big costs are the frontend upfront costs. Now, yes, you got production zones and there's costs going on, but you're producing in a devaluing currency, the tenge, which is the Kazakh currency, and you're bringing in US dollars. Today, the spot price of uranium is about 25 bucks a pound. The Kazakhs are doing better today at $25 uranium than they were at $40 because their tenge is devalued at that ratio. We're there.

That's what's happening across the board. The Kazakhs, the last two decades, went from a million pounds of domestic production, when I first went there in '03 to about 40% and change of the global primary production without really using much of their own money. It was using foreigner's. They're fixed and they're going to be horse trading to get more of that asset. What is the foreigner going to do?

You're in the former FSU, at the Kazakhs, you're not going to screw around there, you're going to pretty much, I see Cameco ending up with maybe 25% or 30% of the asset. The Kazakhs are so smart at this. Don't ever underestimate them. That's just uranium. That's my whole thesis, the cut to kill strategy.

Take copper for example, if you just add Chile and Peru, that's about half of the world's copper right there. Well, what's going on with their currencies? The big mines, the CapExes are in place. Now, they're getting in. Yes, you still have OpEx, but they're still making great money at $2.50 copper, because their currency is devaluing. Is there a reason why the price of copper has to go ballistic? No. That's a deflationary effect on these commodities that I've been talking about here.

Then all these guys go, "Hey, well, Marin, come on, we're running out of copper." The problem with most of the people in the resource sector, they use linear mathematics. They think, "Okay, 3% year over year." That's not how the world works. Fortunately, my skill set is in math. I say, "Well, here's my model. Here's where I think and I think this whole shortage of copper by the end of 2021, I don't really buy it. I've been involved in building and actually I'm the director of one of Canada's largest copper mines."

When the tough gets going, the one thing you can say about miners, they know how to survive. They're very resourceful and they'll start figuring these things out. You see so many examples that guys are reducing costs, producing more with less. That's a trend that we see going on. Now, if you look at, for example, gold, if you take, we're over $2,000 Canadian ounce of gold, and I wrote about this a year and a half ago saying, "Hey, we're going to have $2,000 gold in Australia and Canada," and your costs are in a devalued currency, like what's happened to the Australian currency and the Canadian currency.

Yet, that's a great place to be fundamentally where-- another thing I say, if you're a non-US citizen who doesn't have US dollars, gold is a must. For the American citizen, you're not going to have that big bang on the gold compared to a Canadian or a Russian or a Turk or Argentinian because of the devaluation factor. The best way to play that would be through the equities, which will get that big-- I remember when Grant videoed me a while-- a few years ago, look at what we experienced with new market that became Kirkland Lake, these things went up 60 times and we're not even really in a big gold market yet. We'll be there, but for the Americans, the best way to play it, and the gold guys who buy and sell gold-- they hate when I say this, for an American, the best way to play is through the equities.

What about natural gas?

The natural gas, we don't really need to talk about it. There's so much of it. You look what's going on in Europe, it's a byproduct with the shale. You can't give this stuff away. Like natural gas, be very careful where you invest in natural gas.

Do you see natural resources equities as better investments than the underlying commodities?

First of all, that would be the only reason to invest in the equities is because you're taking way more risks so you want much bigger return. The easiest way to play this is just buy gold and sit on it, take no risk. The only risk is somebody steals it from you. If you're going to play the equity, you got to ask yourself, what's your timeframe and what's your risk tolerance. I think it's going to be very different than what Rick's experienced through his generation and Rick's a really good friend of mine. We're partners. We've worked together for years.

In the old days, it used to be that-- today, the boomers, they would speculate and you get these newsletter writers and the market was a lot smaller back then. These juniors would fly and everyone all-- the rising tide raised all boats. The big difference now is never compared to today in the past, has so much money been managed passively. What I see happening here as a part of my article that I wrote was this passive management, they don't have guys like me and Rick sitting around going, "Well, here's our inflows, what should we buy?"

These are algos, and they're charging things. They're looking at minimum market caps, minimum volumes, minimum-- they have this very complicated thing. They're throwing money in the market. They're not going to go downstream into the juniors so they're going to play in these bigger caps. We're seeing that today where historically, it used to be that the juniors used to be so overvalued relative to the majors and mid-tiers. Now, we're seeing that the majors are trading much closer and even above NAV, so some of these streamers like Franco, they're treating above NAV which is your basic future value into it today.

That's because of this passive management just coming in. In a way, you can argue that that money's the dumb money, like in the past, retail money was seen that way. Yet, there's very little retail money today. You get these juniors that are trading at a huge discount to NAV and what's going to happen I think differently were the big gains aren't going to be made from necessarily discoveries which they happen but they're so rare. One in 3000 ever work and become a mine, where I think it's going to be about buyout. That's where I've been focusing out on and you've seen so many happen where these larger companies who are trading at a much higher valuation or premium to NAV buy out something that's trading at point seven NAV or point eight.

That's where you want to look at. You want to be able to find quality that's low risk, that's developed trading at low NAV that someone else is going to buy out and that's how you get your-- what I call the easy doubles and triples and we've seen them happen, like time and again, and we've been writing about it. That's where I think this first phase of moneys coming in. Then when the market starts seeing many of these happen in another year or so as gold gets going, then you're going to see people go downstream and then all will go up with the rising tide.

I don't think we're there yet. I think step one is playing that NAV ARB is where we are right now in the market. The timeframe of this NAV ARB, we're seeing it right now. When you look at-- when I bought just under 10% of new market, which Kirkland Lake merged, that was just an ARB play. Then you've seen it have a 50 bagger return.

Same thing happened. You look at what's going on Atlantic Gold, my friend Steven Dean just got bought out by St. Barbara, an Australian company that traded at a much higher NAV came and gobbled them up for cash because it was cheaper for them to raise cash because they're trading at a premium to NAV and Biota Jr., well, I call it a junior because they're producing less than 200,000 ounces a year-- bought out

Steven Dean's Atlantic, and as because he was trading at a discount to NAV so it was cheaper for the bigger company to issue cash and play that. We're seeing that happen in real time and you're going to continue to see it happening.

Is there a big difference between precious metals markets and other natural resources markets?

Historically, gold is always traded at a higher premium on both cash flow and NAV. For example, 10 years ago, I wrote about how stupid it is that these analysts and fund managers use 5% NAV when the mine's not even built because the cost of capital is higher than five. The gold guys get away with it, the copper guys would never get away with that. The base metal guys never get away with it. For some reason, the gold guys get away with little differences like that so they get away with 5% discount.

Well, good luck trying to find five. The only guy who can find 5% money was Ross Beaty on Equinox. He got it from Mubadala. He got it at 5.50% and that's because it's Ross Beaty, and he's put almost $200 million himself into the deal. Other than that, there's no other gold guy that can get 5% money. Using a 5% discount to your NPV is ludicrous, except to gold, which they get away with it. The base metals, uranium, you're looking at 12% discounts, 15% because there's so much risk priced in. That's the biggest difference.

What is the most interesting investment in the natural resources space over the next 6 to 18 months?

You got to be in gold and just know where you are, know your political risk. The other one that I love is-- I'm probably the most hated guy in uranium, because I've been saying, "Hey, you got to understand what the Kazakhs are doing. There's a cut to kill strategy here that I've been talking about for a couple years." The world's largest producer of it has used my data in their PowerPoint, I don't work for them. I got no fees from it, but it's saying that, "Okay, I've been right on this. I was the keynote at the world nuclear futures market."

I'm one of the largest financiers in the uranium market saying, "Guys, the spot price is going north for a while. The best way to play that is through royalties." You want to pick up streams and royalties when nobody wants it. The game for uranium is not over, but you got to be realistic and people are using $50 uranium in their evaluations. That's just not realistic. Your cost of capital, the best way to play that in my opinion and the way I'm playing it is through a royalty and streaming company in that sector. I take no production risk and no permanent risk, you're just playing the strict ARB and some of the best returns, Franco-Nevada, Silver, Wheaton, Royal Gold-- you look at these guys who've done these great deals and that's how you play it.

What are the most promising names in the natural resources industry?

The last time Real Vision asked me that, I picked out Tara which I was the second largest shareholder of that, I was with Ross Beaty. That got bought out at a big premium for my cost base and my subscribers cost base because of the whole thesis that I'm playing, chasing developed assets that pay a yield that actually reward the investor. In the gold sector, I'm going to bet-- I bet big with Ross on Equinox Gold. I think that is a no brainer at current prices.

I think if you want another one on gold that no one's talking about, I think Liberty Gold is a no brainer. I'm one of the largest shareholder so I'm talking my book, but I don't give a crap. If it wasn't good, I wouldn't buy it. I think they made a world class discovery and the guys on that are world class with Moira and Cal Everett. Moira Smith is I think one of the best geos that-- here's an interesting thing. I actually think that our industry is so upside down. If she was a man, she would get the recognition and I think everyone would recognize that but because she's a woman, for whatever reason, I think that's how stupid the resource industry is.

I think she's one of the best geologists, period, I've ever met in my life. Liberty is really lucky to have her and I think it's a world class discovery that nobody's talking about and then again I talked about I think Uranium Royalty Corp is something that I've bet big. Your previous get Rick Rule, him and I are going to-- I'm the largest investor, the chairman is the second largest, then Rick's the third. I think that's the way to play it. What you have to have? Three-year timeframes on both from today.

Gold vs Bitcoin.

It's almost like saying gold versus silver. Why not have a little bit of both? Have all of the above. The point of having money is to make money and I think that discrediting Bitcoin-- I'm by no means any Bitcoin expert. I put my money with Mark Hart. I'm a pretty significant shareholder in his fund. He's a good buddy of mine and with Ray that run that and I just don't have the time to understand it, but I think he's really smart and he's going to make me a lot of money in it. Why not have US dollars? My portfolio if I was to have my All Star team, go US dollars, gold, some silver, some Bitcoin. Why not?