WAR ON WEALTH

BY ROBERT A. WIEDEMER
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About Robert A. Wiedemer
What’s one of the biggest themes of this year’s presidential campaign? Anger. Lots of anger. Anger toward politicians; anger toward the system; and a lot of anger toward wealthy people, especially those on Wall Street.

The asset booms over the last few decades in stocks and real estate haven’t necessarily benefited a lot of middle and lower class people—not directly, anyway. Incomes have been basically flat over the last 20 years. Unemployment is down, but that’s mostly a reflection of low-paying and part-time work going to college-aged and retirement-aged folks.

The jobs market is still pretty lousy for people between 25 and 55, the years when most people want to be growing careers, starting families and buying homes. There are still 45 million people on food stamps in this country—compared to about 27 million before the financial crisis of 2008—and more than 100 million receiving welfare. That’s 35 percent of all Americans. Add in pensions, unemployment, Social Security and Medicare and we have half of the country receiving some kind of federal payments.

Naturally, the effect of this is more government outlays. Medicaid benefits are up almost 90 percent in the last decade, up to $553 billion in 2016 from $291 billion in 2006.

If that’s how the problem has grown after the 2008 crisis, imagine if we had an even worse economic crisis on the horizon. As I wrote in my book AFTERSHOCK, that’s just what I believe is going to happen. And the number of people receiving government federal payments will only go up.

That may be hard to believe: more than half of the country receiving federal payments? But remember: the stock market is still high, real estate prices are still high, and even though the jobs market isn’t as great as the White House and the media would have you believe, it’s still not catastrophically bad.
Assuming the Aftershock hits, the stock market, real estate market and jobs market pretty much collapse. We’ll have more people on welfare, more people unemployed, and of course we’ll still have an aging population in need of more assistance—and plenty of political support for the government to provide assistance.

Right now the government can meet people's needs through borrowing and money printing. Following the Aftershock, though, credit markets are destroyed and money printing is ineffective. So the only way to pay for these programs would be taxation, which means taxes would be very high for anyone with a steady income or assets.

You can also be sure that taxes would be especially high on the wealthy. We’ve already heard some calls in this presidential campaign for higher taxes on the highest bracket. Those calls will only get louder, and when the government—both in the U.S. and abroad—needs to find more money, the highest earners will be the logical place to turn. We can already see some of the early stages of this in Greece. It’s what some are calling the “War on Wealth.”

America’s Political Climate

Both candidates for President appear to support expensive social welfare programs. Even Trump, a multibillionaire, has broken from traditional conservatism in that he’s expressed support for these programs even when the federal budget is as strained as it is. He may not want to raise taxes to pay for them, but he indicates he can just borrow the money instead.

So we’re seeing support from two popular candidates from both parties, who potentially have the combined support of 89 percent of the country, both running on a populist platform and embracing government assistance programs. Maybe they’re not everybody’s first choice for president, but they have more support than anyone would have predicted a year ago.

Is this a reflection of the country’s growing welfare needs, as shown in those earlier charts? Probably. But more importantly, if this is where the country’s politics are now, when the economy is growing and the stock market is high, what does it say about our future if and when the economy and stock market tank?
Political cycles come and go. But given the economic realities ahead, it’s fair to say that the political climate today is a microcosm of what it will be after the Aftershock. If unemployment figures rise back to 2009 levels and far beyond, support for populist, anti-wealth candidates is only going to grow even stronger than it is today.

**Taxation in the Aftershock**

If upwards of 60 percent of the country were unemployed or underemployed and in need of assistance, you can be sure taxes will be sky-high for the remaining 40 percent. Income tax rates from 30 percent up to 60 percent for the highest earners would be likely. We’d also probably see limits on deductions for real estate and interest. Those deductions would look more like medical deductions today: they’d need to be over a certain percentage of income to be deducted. On top of that, one can expect a cap on those deductions—a cap that probably wouldn’t be adjusted for very high inflation rates, meaning it would drop every year in real terms.

And, it could get worse. Extreme popular opposition to wealth means a whole host of tax laws that eat away at wealth. For starters, capital gains could be taxed the same as ordinary income. We’d probably also have a value-added tax of around 20 percent. VAT taxes already exist in Europe—that’s how Europeans pay for their welfare system. But unlike in Europe the new VAT tax in the U.S. would likely have few exclusions, as the government at this point would be desperate to raise money.

With a 30 percent baseline income tax rate, and a 20 percent VAT tax, that means the U.S. government would be taking half of GDP. Somewhere between a quarter and half of that would be used for welfare programs, and the rest used for government services—such as healthcare and education, which due to the economic realities would need to be provided by the government for 80% or more of the population in the country. In short, it would be a horrendous mess.

But it won’t stop there. Estate taxes could rise to as high as 70 percent in some cases—levels we haven’t seen since the 1960s, but at least then there were significant loopholes. More importantly, high inflation means that the exclusion rate for estate taxes becomes lower and lower even without any rule changes.

Though less likely, it’s possible we could even see a wealth tax—which is exactly what it sounds like. People above a certain net worth would have to pay annual taxes on their net worth. A 2 percent wealth tax on a $10 million estate would mean a $200,000 payment to the federal government on wealth that was already taxed as income earlier. Again, that’s relatively unlikely, but a somewhat softer version would be more likely: perhaps a tax on any wealth that was accumulated before the Aftershock and not after, or a tax on properties that are deemed to have been undertaxed in earlier years (before the “War on Wealth” really took off).
The Stock Market Shutdown

In 1933, at the height of the Great Depression, newly inaugurated President Franklin D. Roosevelt declared a four-day bank holiday across the United States in order to take steps to allow banks to meet customer demands. In the decades since, the U.S. financial system has been relatively stable. But make no mistake: the government can and will take similar steps when our financial stability is seriously threatened.

If money printing by the Federal Reserve fails to keep the stock market from plunging, the Fed will have no choice but to shut the whole market down temporarily. A similar situation happened in China in early 2016, when predetermined “circuit breakers” were tripped by plunging stock prices. The idea is to give investors time to compose themselves, assuage their panic, and behave more rationally once the market reopens.

Of course, if the market shuts down, preventing investors from selling when prices are plunging, that doesn’t necessarily make investors want to stay in stocks when it opens back up. More importantly, when the U.S. stock market falls, it will be because a massive bubble is bursting. In other words, any panic among investors would be rational panic. When a bubble is bursting, it’s critical to get out as quickly as possible, because it’s only going to keep deflating.

So after a brief shutdown—maybe only a couple hours—the market would open back up again only to see the plunge continue in short order. Then the Fed would need to shut it down again, now promising reforms, such as banning short-selling and other negative bets against the market. Congress might take the additional step of passing new tax laws to reward buying stocks and punish selling. Then they could open the stock market back up with more confidence.

Unfortunately, short-selling and taxes aren’t the issue. The new incentives might push prices up briefly, but soon the market could start plunging again. Instead of taking the trading holiday to renew their confidence in the market, investors will be starting to smarten up.

They will then realize that a market supported by massive government borrowing and massive money printing is not a sound market. They will want out of the market. Even those that are unsure aren’t going to want to buy stocks. By then, the stock market would be down anywhere from 20 to 60 percent, while the safe haven of gold could be skyrocketing. Even the most mainstream investors would be looking to reduce their stock exposure and increase their gold exposure, just out of prudence.

When a stock market holiday of a few days doesn’t work, the time frames of subsequent holidays grow longer. Days become weeks, weeks become months. Eventually the Fed might have to declare that the market will be shut down indefinitely until the investment community returns to normal.

But that’s not going to happen. This would be the new normal. After enough time has passed—and it could be months—the Fed would have little choice but to accept it and reopen the stock market. Government officials and what’s left of Wall Street would condemn selling stocks—saying that investors are acting irrationally, that they don’t understand value—but they would let it take its course.
By then the real damage would have been done. By that time, the Dow could be as low as 1,000, and investors may have seen markets closed for months, unable to get out. It would be worse than a collapse in asset prices; it would be a collapse in public trust in the financial system. It would be more than the loss of some wealth in the stock market; it would be an all-out massacre of wealth.

Trouble in the Banking System

Unlike during the Great Depression, there would be no need for a bank holiday during the Aftershock. The Federal Reserve could simply guarantee demand deposit (i.e. checking) accounts in the U.S.—something it couldn’t and wouldn’t do in the Depression. The Fed’s guarantee would even go beyond typical FDIC insurance on deposits up to $250,000. The cost of printing money to insure demand deposits is well worth it, even in the worst of times.

Then again, it’s not as if cash in the bank is great protection against losses. First of all, inflation could be eating away at cash accounts at an unprecedented rate. On top of that, any interest on demand deposits would be heavily taxed, even though they won’t nearly offset the effect of inflation in the first place.

That’s demand deposits. As for savings accounts and CDs, forget it. Banks won’t have the money to make good on these guarantees—the loans that back them are basically worthless at this point—and the government can’t afford to pay for them either.

Investors with significant losses from savings accounts and CDs might be able to apply for hardship payments from the government. But those are exactly what they sound like: hardship payments, for those who can’t meet basic life expenses without that money. There is little interest at this point on the part of the government in loss of wealth. The demands on the system would simply be too great. Someone could lose $500,000, or $2 million, or $10 million, by no fault of their own, and never see it replaced.

There’s more bad news, and it has to do with another war going on, and tied into the “War on wealth:” the war on privacy.

The War on Privacy

Increasingly, governments want to know what people are doing: how they’re spending their money and where. And because of this amazing electronic age we live in, it’s easier than ever to keep tabs on people’s financial habits. So much information is held electronically now that if the government really wants to track its citizens, there’s little standing in its way. With the war on terror still ongoing, there is both more motivation for government surveillance to increase and more legal or bureaucratic cover for such surveillance.

In line with the war on wealth and the war on privacy, we can see that governments around the world are moving increasingly toward a cashless society. You may not remember this, but there was a time in this country when we had $10,000 bills. As startling as that sounds today, think about how much more valuable that amount was in the 1930s. And it wasn’t too long before that when many commercial transactions were carried out in gold.
Today we’re moving in the opposite direction. Even small purchases at Starbucks or McDonald’s are often made with credit cards and debit cards instead of cash. Checks, too, are becoming increasingly rare. Social Security payments used to come by checks in the mail. Now most people have the money deposited electronically into their bank accounts.

It’s convenient that this move away from cash—often hailed as a wonderful advance in technology—also allows governments to monitor financial transactions more easily. It may make our day-to-day lives a little easier—fewer trips to the bank, more room in our pockets and purses—but it’s a Pandora’s box of opportunity when we have governments that don’t necessarily have a lot of respect for their citizens’ privacy.

All this, combined with the coming Aftershock I see, could make for a very difficult time ahead for wealthy people. And we’d find that, especially as traditional investments in the stock, bond and real estate markets lose a great deal of their value, gold (and silver) will be a preferred option for holding wealth.

Not only could gold be a great place for investors due to its performance, but it also affords investors much greater privacy than traditional investments. We’ve already seen this happen in tough economic times in the past. It could be even more important now that the “War on Wealth” can be waged at a much higher level.

The Aftershock—and the hardship it would put on government budgets—ramps up the government’s incentive for surveillance just as technology provides greater means. Every digital financial transaction can be tracked as the government determines it needs to.

That’s why gold won’t just be important in the Aftershock. It’s important before the Aftershock. Move too late, and your options become limited. Throughout human history, gold has been a safe haven in times of trouble. Whether it’s a financial “Wild West” or a confiscatory government, gold has always been a store of value. In both the “War on Wealth” and the “War on Privacy,” gold could once again be the gold standard in defense.

For more information on gold, and on specific gold, silver, platinum and palladium investment products, please contact:

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