THE "YOU MAY NOT KNOW REPORT"

A PUBLICATION OF RETIREMENT LIFESTYLE ADVOCATES

Unintended Consequences and the Emergence of New Markets

Our lives have changed dramatically this year. But more change is coming.

As a result of the response to COVID-19 in many states and rioting in many cities, massive, permanent change is occurring. Ironically, as existing markets falter or fail, new markets emerge. Historically speaking, this has always been the case as policies pursued by politicians typically have unintended consequences.

From where we live, to how we educate our children, to how we get healthcare, current trends suggest that our lifestyles will continue to evolve as these new markets emerge and look much different in just a few, short years.

Sadly, it seems that these trending changes will only accelerate the already wide wealth gap and likely lead to even more social unrest, an unintended consequence of current policies.

In the book "Economic Consequences" that I wrote back in 2011, I discussed unintended consequences in detail. The Endangered Species Act did not end up protecting habitat as intended. Instead, landowners harvested or changed habitat before an endangered species could call the area home. The Americans with Disabilities Act actually resulted in fewer jobs for the disabled. There are many more examples, but it's easy to demonstrate that new regulations almost always have unintended consequences.

I believe we are on the verge of massive change and the emergence of more unintended consequences due to current policies. Once the massive federal spending funded by new money creation dries up, these unintended consequences will become more apparent, but the trends are developing quickly.

In this short piece, I'll look at three policies that I believe will create permanent change: the defund the police movement, the lockdown response to COVID 19 and the suspension of healthcare for many patients whose medical conditions don't meet the essential definition as defined by the politician du jour.

Each of these policies is motivating many citizens who are more affluent to take action. These well-off citizens have choices that less affluent citizens do not.

The defund the police movement and rioting in many of America's big cities are finding these cities are quickly dying, probably never to be revived. As my past RLA Radio guest Jim Rickards recently noted[1] there is a lot of hard evidence to support the fact that those who have the ability are leaving big cities in droves.

He notes that the cost to rent a U-Haul trailer to move from Los Angeles to Sedona, Arizona is four times the cost to rent the same trailer to move from Sedona to LA. The same is true when renting the same U-Haul to move from New York City to the Catskill Mountains.

As noted previously in this report, past RLA Radio guest and economic commentator, Mish Shedlock recently moved from Illinois to Utah and found that he couldn't rent a moving trailer for 3 weeks. However, if you're moving from Utah to Chicago, U-Haul will practically pay you to tow the trailer.

Rickards states that there are three reasons for this migration and compares it to the Dust Bowl migration of the 1930's when desperate people moved west to seek jobs in the California agricultural industry. Now, ironically, the move is in the opposite direction.

The first reason is that the millennials are getting older. In just a couple of years, the oldest of the millennial generation will turn 40 (feel old yet?). While city life is appealing to many, if not most twenty-somethings, it's not as appealing to many who are approaching 40.

The second reason is the pandemic. It's no secret that rural areas have not been hit as hard as densely populated areas like New York City.

The third and primary reason is the riots. In my view, mainstream media has been extremely lax in covering the true damage caused by rioting. But many alternative news sources and videos show the damage has been extensive and, as a result, many of the city dwellers who are able to are leaving. (Note: Peaceful protests for change to address social injustices are constitutionally protected and should be supported. But, destruction of property and looting are not peaceful protests.)

Rickards points out that those who are leaving the city are the people you don't want to leave – those with assets, talent and energy are those who have the option to exit. Rickards notes that this will have a devastating economic impact.

Something similar is happening in education.

While many of those who have the financial ability to leave the cities are leaving, many parents who have the ability to pay to educate their children are also doing so, bypassing the traditional education system.

With many states mandating that classes be held remotely this fall, many parents are stepping up and taking responsibility for the education of their children. Learning pods are gaining in popularity. A learning pod has a few families who combine resources to hire a private teacher to educate their children.

One of my friends with school-age children has teamed up with three other families and hired a full-time teacher to educate six children. Each family pays a share of the teacher's salary.

This is a good option for affluent single-parent families or two-parent families where both spouses work. But, again, it is only available to those who can afford it.

Healthcare is also changing since many "non-essential" medical services were suspended as part of the lockdown response to COVID-19. There is a growing movement of doctors who don't take health insurance and charge patients a monthly fee for access to health care. These doctors are unaffiliated with a hospital or healthcare group and work independently. These practices are known as direct primary care practices and they're growing in popularity.

Yahoo News reports[2] that monthly membership fees to join a direct primary care practice range from $50 to $150. That fee covers office visits and the member patient typically gets drugs from the physician at much lower prices.

A direct primary care membership makes a lot of sense for many people, but once again, it is only available to those with discretionary income.

Here's the reality of these trends. Once an affluent person leaves a city, they're not returning. Many families who decide to take control of the education of their children will find that they prefer the individualized instruction their children receive, and they won't return to the traditional education system. And, those who become members of a direct primary care practice may find it difficult to return to waiting a month or more for an appointment when choosing to get their medical care more traditionally.

The unintended consequence of these government policies is citizens taking action to avoid the regulations that negatively affect them. Arguably, it has been these policies and the Fed enabling these policies via money creation that has been the primary cause of the wealth gap and social unrest.

And, this is not new. As I noted above, I wrote about this nearly 10 years ago in the book "Economic Consequences". Here is an excerpt of just one example of unintended consequences from that book:

> *The City of Detroit is a perfect example of failed regulation, failed bureaucracy and unintended consequences. The Model City program, initiated by President Lyndon Johnson in 1966 as part of his Great Society programs poured a total, of about $1 billion into the City of Detroit to attempt to revitalize the inner-city slums.*
>
> *The result?*
>
> *By the mid 1990's, the Model City area lost 63% of its population and 45% of its housing units. In 2009, an auction was held to sell over 9,000 seized homes and lots many located in the Model City area. Only 20% of the properties sold despite the fact that bidding began at just $500 on many properties.*

If you're not familiar with the Model City program, here is some background as it relates to the City of Detroit. In Detroit, the Model City program attempted to turn a nine square mile area into the government's idea of a model city. Government bureaucrats were telling people where to live, what to build and which businesses should be opened and closed. In return, people received cash, training, education and healthcare.

Immediately after the Model City program was initiated, 22,000 middle- and upper-class citizens moved out of the city. These folks simply didn't like paying higher taxes and being told what to do. In July of 1967, police attempted to break up a party in the middle of the new Model City; their efforts resulted in a race riot that was one of the worst of the 1960's. The Mayor of Detroit feared that additional police presence might only make matters worse, so he did nothing to stop the riots. Five days later, President Lyndon Johnson sent in 2 divisions of paratroopers in order to settle things down. Over the next 18 months, another 140,000 people exited the city, almost all of them middle and upper class.

Instead of coming to the realization that this type of central planning didn't work, in 1974 the program was expanded under the Community Development Block Grant Program. Under this program politicians and bureaucrats would decide which groups and individuals would receive funds for various renewal programs and efforts. Despite these efforts, the exodus from the city continued.

Today, with the population of Detroit down to just over 700,000 from about 2 million in the 1950's, the unintended effects of the Model City program are clear.

If we update those population numbers for 2020, the population of the City of Detroit now stands at about 667,000. That's about 1/3rd of the city's population in 1950.

Pretty much the only folks left in Detroit are the ones who don't have an option to leave.

Today's policies are likely to have an even more devastating impact on the less affluent. Not only will many big American cities meet the same fate as Detroit, education and healthcare will also be negatively affected.

The Above Opinion Piece By:
Dennis Tubbergen

Digital Money Update

As fiat currencies continue to see their purchasing power decline, many central banks around the world are working to introduce digital currencies to their populations.

The Bahamas launched a digital currency at the beginning of the year. This[3] from "Coindesk" (emphasis added):

> *The Bahamas' digital currency pilot project went live in Exuma on Friday.*
>
> *Residents of the island can now enroll in the Central Bank of The Bahamas' "Project Sand Dollar," which began Dec. 27.* ***They will receive mobile wallets the Bahamian govern-***

> ***ment sees as facilitating the future of payments on the island chain. Central bankers announced the debut on Tuesday.***
>
> *Bankers said "Sand Dollar" is a "digital fiat currency" – not a cryptocurrency, stablecoin or competitor to the Bahamian dollar. Instead, it is simply a digital version "equivalent in every respect to the paper currency," they said in the project outline.*
>
> ***But it is also a step toward the Bahamas' long-term goal of launching a fully-fledged central bank digital currency (CBDC).*** *Also called the sand dollar, that larger project would link domestic residents and businesses across a seamless digital payment infrastructure.*

The government of Ukraine is also getting in on the act. This[4] from "Coin Geek" (emphasis added):

> *The Ukraine Ministry and Committee of Digital Transformation has signed a deal with Crystal Blockchain that allows them to track digital currency transactions.*
>
> *Ukraine says its primary goal is to use the blockchain analytics software to assist the country in* ***"the rapid formation and legalization of the market of virtual assets in Ukraine." At the moment, the Ukraine Finance ministry says they will be tracing any digital currency transaction in which more than $1,200 is sent.***

Then there is Ecuador. This[5] from CNBC (emphasis added):

> *In 2000, Ecuador moved to ditch its stumbling currency for the U.S. dollar. Now more than 15 years later, the South American country is revamping its monetary system again—**using digital currencies.***
>
> *Ecuador's Sistema de Dinero Electrónico (electronic money system) kicked off in December by allowing qualifying users to set up accounts, and it will begin acting as a real means of transaction this month.*
>
> *Once the government flips the switch, the South American nation of 16 million will host the first-ever state-run electronic payment system. (Other countries, such as Sweden, use digital currencies widely, but they're not state-sponsored.) But the Ecuadorean government says the scheme is designed to support its dollar-based monetary system, not replace it.*

Uruguay and China are also using or testing digital currencies. This is a growing global trend that is picking up steam.

In his recent piece[6] titled "Doubling Down on Failed Policies with Central Bank Digital Currencies", past RLA Radio program guest, Alasdair Macleod noted that central banks want digital currencies for many reasons. Among them are reducing costs associated with managing physical cash, making it easier for the 'unbanked' in the population to manage their finances, make it easier for the central bank to impose negative interest rates and get newly created money directly to the public while bypassing commercial banks.

A recent Bloomberg article[7] featured an interview with two former Federal Reserve officials who propose using "Recession Insurance Bonds" (a form of digital money) to get money directly to members of the public. This from the article (emphasis added):

> *Former central bank officials Simon Potter, who led the Federal Reserve Bank of New York's markets group, and Julia Coronado, who spent eight years as an economist for the Fed's Board of Governors, are among the innovators brainstorming solutions. They propose creating a monetary tool that they call recession insurance bonds, which draw on some of the advances in digital payments. Coronado, president and founder of MacroPolicy Perspectives LLC, and Potter, nonresident senior fellow at the Peterson Institute for International Economics, spoke with* Bloomberg Markets *to explain their idea.*
>
> *Congress would grant the Federal Reserve an additional tool for providing support—say, a percent of GDP [in a lump sum that would be divided equally and distributed] to households in a recession.* ***Recession insurance bonds would be zero-coupon securities, a contingent asset of households that would basically lie in wait. The trigger could be reaching the zero lower bound on interest rates or, as economist Claudia Sahm has proposed, a 0.5 percentage point increase in the unemployment rate. The Fed would then activate the securities and deposit the funds digitally in households' apps.***

There is some question as to the timing of the development of a digital currency. Mr. Macleod concludes his excellent article with this:

> *Central banks researching CBDCs (Central Bank Digital Currencies) are motivated by finding an additional means of monetary inflation to the existing means of issuing increasing quantities of fiat currencies. By issuing CBDCs directly to the public, commercial banks are by-passed, and central bankers hope to forensically target where the inflation is applied. A successful introduction of a CBDC could eliminate the impediment of contracting bank credit which occurs at the end of every credit cycle.*
>
> *The further benefit for central banks is it will increase their power as an organ of the state at the expense of commercial banks, potentially becoming more important than the state itself. However, the current economic situation is deteriorating more quickly than a working CBDC can be introduced, so the whole exercise is likely to be too late to have any relevance to monetary policy in the foreseeable future.*

California Considers an Excessive Wealth Tax

The State of California is now mulling the idea of a wealth tax. The "California Wealth Tax Bill (AB2088) would tax the net worth of Californians who accumulated excessive wealth. And, if you're a wealthy Californian who might be affected by the new law should it pass, you won't even be able to move to avoid the tax according to the bill's sponsor. This[8] from "California Globe" (emphasis added):

> *Assemblyman Rob Bonta (D-Oakland) made an appearance on "Cavuto: Coast to Coast" Friday to discuss his Wealth Tax proposal. Bonta told Cavuto the tax "affects about 0.15% of the California population — not the top 10%, not the top 1%, the top .15%, about 30,000 people."*

California Globe reported Bonta held a Zoom press conference Thursday announcing his legislation to tax the state's wealthiest job creators and innovators – he claimed the "30,400 billionaires" living and working in California. (According to CNBC, there are only 630 billionaires in the entire United States.)

Bonta blames coronavirus for creating "inequality" in California, and not previous legislation and policies. "Families are hurting right now. COVID-19 has only made matters worse," Bonta said. "In times of crisis, all Californians must step up and contribute their fair share. Asking these well-resourced Californians to give a little more to keep our people working and support our most vulnerable is the right thing to do."

This first-in-the-nation net worth tax is estimated to generate $7.5 billion per year in new "revenues" to the state coffers.

California has the highest tax rates in the nation. Bonta and Democrats want to force successful Californians to pay additional taxes on wealth and income that's already been taxed.

***In the new bill is an introduction statement that the wealth tax is "for the benefit of accumulating excessive wealth in this state,"** Globe contributor Chris Micheli reported.*

*Knowing about the huge outbound migration from California, Cavuto asked what would happen to wealthy people who move out of state. Bonta said **tax "avoidance" would not be allowed as California would tax them for the next ten years, despite what state they live in. Bonta said that because they accrued the wealth in California, the state can continue to legally tax it.***

*"Tax avoidance," with the primary purpose of reducing the valuation of a taxpayer's worldwide net worth is required to be disregarded. "The bill authorizes the Franchise Tax Board to **adopt regulations necessary to carry out these new statutory provisions including the valuation of certain assets that are not publicly traded," Micheli said.***

That last line should be particularly alarming to business owners who might be affected by the tax. If the business is not publicly traded, a bureaucrat from the State of California will value it for you to determine the level of tax you'll be required to pay.

How many wealthy Californians are moving now to avoid this outcome?

Many.

Golfer Phil Mickelson for one. He told[10] the "Golf Channel" several years ago that one of the reasons he was considering a move from his native California was taxes.

> *"Although Mickelson didn't offer a reason for his potential move, in 2013 he suggested he might move out of California because of his federal and state tax bill, **which he estimated had pushed his tax rate above 60 percent.***
>
> ***"There are going to be some drastic changes for me because I happen to be in that zone that has been targeted both federally and by the state and, you know, it doesn't work for me right now," he said in 2013. "So, I'm going to have to make some changes."***

Construction on the golfer's home in Jupiter, Florida began in January of this year.

Time Deposit Rates

As this issue went to print, these rates were valid:

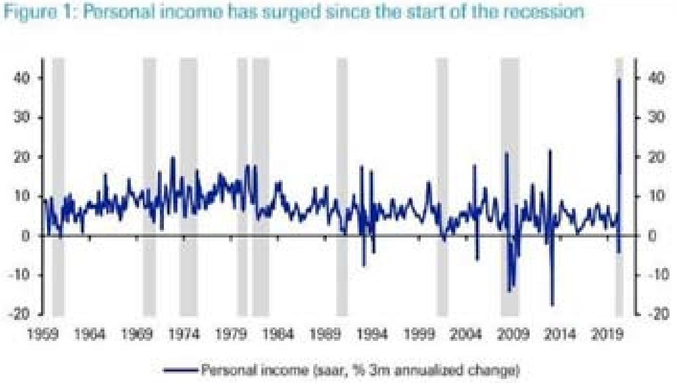
1-Year	1.75%
2-Year	1.75%
3-Year	2.50%
5-Year	3.10%
10-Year	3.25%

Call the office for details at **1-866-921-3613.**

Current Recession Realities

Deutsche Bank's Jim Reid recently observed that recessions don't typically find personal incomes increasing but this one has as noted by the chart.

Figure 1: Personal income has surged since the start of the recession



Source: BEA, Haver Analytics, Deutsche Bank Asset Allocation

Notice that going all the way back to 1959, in recessions and in periods of economic expansion, personal incomes have never increased like they did during this recession.

Of course, the reason personal incomes have expanded is that the government has supported the newly unemployed through increased unemployment benefits funded by newly created currency. Now, however, those benefits are beginning to be scaled back despite the fact that the unemployment rate remains high.

Interestingly, the government's response to the recession that came about as a result of the COVID-10 lockdowns created a temporary illusion of prosperity that may now be coming to an end. As Bank of America noted, "Absent government support, disposable income would have fallen the most in history; with that support it has risen the most in history."

So, where do we go from here economically speaking?

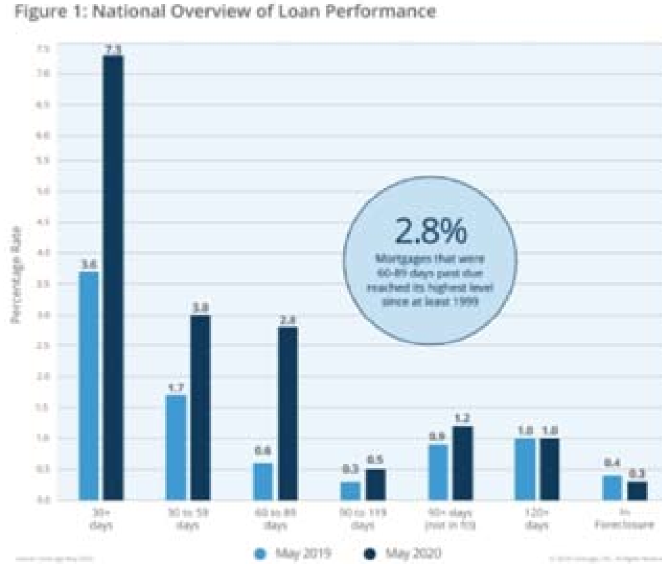
The Peterson Institute did a study10 which assumed there were 20 million people who were unemployed at the end of July. They also assumed that the now-expired $600 federal unemployment benefit has a fiscal multiplier of 1.5. Based on that assumption, about $50 billion in monthly income would be removed from the economy each month. That translates to a 2.5% decline in Gross Domestic Product and 2 million fewer jobs over the next year and a 1.2% increase in the unemployment rate.

Bank of America commented that these numbers are probably conservative, and the reality will be more severe.

Fallout is already being seen with mortgage delinquencies. According to "Forbes"[11], the mortgage delinquency rate is now over 15% on FHA loans (typically used by first-time homebuyers).

"Business Wire" published a chart[12] that illustrates how more than 13% of all loans are from 30 to 90 days past due:

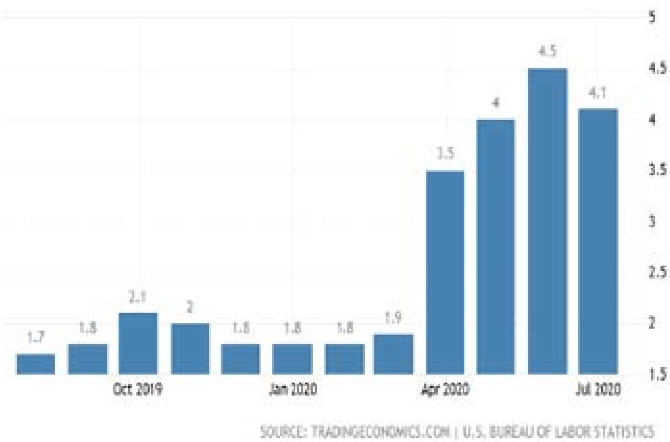
Figure 1: National Overview of Loan Performance



As we have noted in a past issue of this publication, we expect those numbers to continue to increase. In another 60 to 90 days, barring more direct-to-the consumer stimulus, we expect our minimum delinquency rate forecast of 20% of all mortgages delinquent to be reached.

As extra government benefits to the unemployed are being pared back, food price inflation is accelerating. While some of this food price inflation could be attributed to supply chain interruptions, we are of the opinion that much of the blame for higher food prices can be attributed to Fed policies.

Note from this chart[13] from "Trading Economics" that food price inflation year-over-year increased by 3.5% in April year-over-year, 4% in May, 4.5% in June and 4.1% in July.



Clearly, should these trends continue, it will be another huge drag on the economy (and cause of even more social unrest).

Keep in mind that food and fuel prices are not included in the calculation to determine the officially reported inflation rate. This was not the case in the 1970's when annual inflation was in double digits.

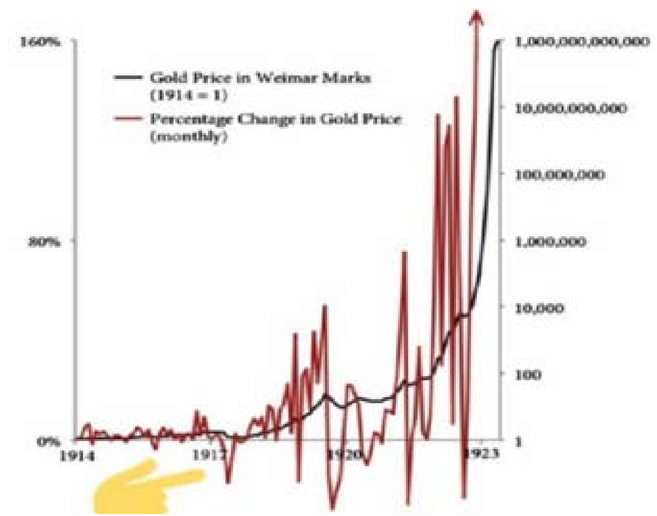
When looking at food prices, it seems we may be back to 1970's levels of inflation despite what the official number might be.

Still Bullish on Metals

Precious metals prices have been volatile of late. We expect this volatility trend will continue.

The reason is simple. Money printing will have to continue. History teaches us that the Fed is now in a position where the bank will have to print money faster and faster in order to meet growing needs for more bailouts and likely to bail out member banks at some future date.

Jay Taylor, a past RLA Radio guest, published this chart recently that demonstrated the volatility in gold prices in Weimar Germany as the German Mark failed.



Notice that from 1914 to 1923, gold prices in German Marks increased by a factor of 1 trillion. That's remarkable, almost unfathomable when you consider it. But the chart also illustrates how volatile the gold market was as nominal gold prices soared.

The point?

We are still of a mind that accumulating metals up to 15% to 20% of one's portfolio may be advisable for many investors.

Be patient though. Both gold and silver have already made big moves this year. As we often state, markets usually don't go straight up or straight down. The gold chart from the Weimar Republic proves that.

Debt Levels Weigh on Economy

For a long time, we have been talking about debt levels in the private sector that will weigh on the economy moving ahead. Corporate America ,along with American citizens, is weighed down in debt to the point that economic recovery will probably not be possible until debt is purged from the system.

This[14] from "Bloomberg" (emphasis added):

> *After tapping the bond market at a record-shattering pace in recent months, Corporate America is more indebted today than ever before.*
>
> *And while much of that fresh cash -- more than $1.6 trillion in total -- helped scores of companies stay afloat during the pandemic lockdown, it now threatens to curb an economic recovery that was already showing signs of sputtering.* ***<u>Many companies will have to divert even more cash to repaying these obligations at the same time that their profits sink, leaving them with less to spend on expanding payrolls or upgrading facilities in months ahead.</u>***
>
> *The over-leveraging of America's corporate sector is not a brand-new development, of course. It's been building for more than a decade, ever since the last crisis -- the housing-market meltdown -- prompted the Federal Reserve to pump unprecedented amounts of cash into the economy, a policy tool that it has taken to new heights during the pandemic as it has supported corporate credit markets.*
>
> ***But in a sign of just how pronounced the borrowing overhang has become, the average junk-rated company had debt levels relative to earnings that were so high in the middle of the year, according to a new analysis by Bloomberg Intelligence, <u>that they almost would have tripped do-not-touch alerts from banking regulators a few years ago</u>.*** *Those warnings back then only applied to a handful of borrowers. Had regulators not opted to drop these warnings, they could today apply to far more.*
>
> *"An overburdened corporate sector is likely to grow less rapidly and that could slow the whole recovery down," said Kathy Jones, chief fixed-income strategist for Charles Schwab Corp.*

The eternal truth is that debt consumes future production. Since future production is finite, debt accumulation also needs to be finite. Once debt levels in the economy reach levels that are unsustainable, economic growth has to stop.

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Best wishes to you and yours

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