Keys To The Kingdom

One of the great privileges of being a financial planner is the opportunity to work with God's children from all walks of life, at a variety of stages in their lives, as each strives for financial freedom and a sense of security. From struggling to figure out student loans to dealing with health care costs in retirement, we have the chance to advise people all along on life's journey.

While each person has a different set of personal goals and circumstances, we all share the same economy, tax rates, interest rates, real estate returns, stock returns and cost of government. Each person is impacted a bit differently depending upon their circumstances, however when we do something like deposit money in a saving account we all receive a similar rate.

"How Can the Bank Do This to Me?!"

Years ago I heard this from a woman who retired and put all of her retirement funds into a deposit at the bank that in the mid 80's earned her around 10% interest. Looking to renew the deposit in the early 90's she expected to renew at the same rate, but instead was quoted a rate closer to 4% on her deposit and was now facing a roughly 60% reduction in her retirement income. Anyone in the same situation would feel betrayed and impoverished.

Rates Go Up and Rates Go Down

Our private banking authority, the Federal Reserve Bank (the Fed) has a very profound impact on interest rates by controlling the rate at which its member banks can borrow money and by buying or selling securities for the asset side of its balance sheet. Think of it like heating up or cooling off the economy.

If the Fed lowers interest rates, buys government bonds and mortgage bonds, they are trying to heat up the economy. Raise interest rates and sell some of the bonds the Fed owns and they cool off the economy. However not just the economy and business are affected, citizens, some of whom live off of interest payments in retirement, are also significantly impacted.

Hard to Earn a Buck

People who have been good throughout their lives and have saved money "in the bank" are feeling a little punished these days. While they are often earning less than 1% on deposits, the cost of things like healthcare, education, food and energy by many measures are increasing at 5% or more. At a point where they were expecting to "live off the interest", many feel they are losing ground. After taxes and inflation they probably are, even more than they know.

"Financial Repression"

A little over a year ago this phrase first appeared in some communications in the financial services industry. One Webster comment about the meaning of repression included "to put down by force". Many who watched their retirement income from their bank deposits go down might agree with this characterization.

One observer described this as a stealthy tax on savers and investors. If banks and the government pay very low interest, advertise low inflation when actual inflation is much higher, then they are able to maintain their debt at a much lower cost. In essence this is done on the backs of citizens who have been good savers, imposing a stealthy tax by not paying a higher and perhaps more appropriate interest rate when inflation may be closer to 5% or higher on key goods and services. This is the essence of "financial repression".

Encouraging Risk

When smart savers recognize this pattern it causes them to consider other ways to put dollars to work, recognizing that increasing prices (inflation) eats continually at the value of every dollar they own. While there are benefits to risk taking there is also, well…….risk! In the end, some investments just do better when the dollar goes down in value and then it takes more of them to feed ourselves, pay our utilities, pay for homeowner's insurance and to put the car in the shop.

Don't Fight the Fed

One piece of wisdom many market observers agree upon is, if the Fed is moving in a particular direction, in general go in the same direction. The direction for now is to keep rates very low and to make lots of money available to the government and banks. This environment suggests future inflation.

Investing in things that stand a chance of going up with inflation would make sense in such an environment. While investments like deposits in banks may not do so well, until the situation of financial repression gives way to a more normalized and perhaps balanced set of economic circumstances.

Bottom Line

Abnormally low interest rates favor those who have built up big debts, like our federal government. Individual savers can accept the circumstances (and what could be a stealthy additional tax on their savings) or they can seek opportunities to do better. Risk has to be very carefully weighed by each investor in each investment they make. Still, at the end of the day there is also the risk that Fed policies may not be working in their individual best interests. A different course of action than they are used to may prove prudent. It is certainly worth a few minutes of conversation and we'd love to hear from you.

Your Feedback

I would love feedback on this newsletter. Future issues may include a host of good ideas, insights, specific steps to take financially, life insights and of course "Wit and Wisdom". Most importantly, I'd like it to be of value to you and to encourage an exchange of great ideas and insights. Please send your feedback to:

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