Financial Reckoning Day *– Surviving the Soft Depression of the 21st Century*
By William Bonner

Bill Bonner wrote and published this book in 2003. Reading this book in 2009 (reread 2012) you would think, this guy must be a soothsayer, since his foresight is especially accurate in a number of key financial areas. His main premise is that the U.S. economy is in for a prolonged 'bear market' over the next 17 years (starting in the year 2000). He provides his arguments based mostly on history but also reminds us of many other factors that support his hypothesis. He reminds us that from 1929 to 1946 (17 yrs) it was a bear market, from 1946 to 1965 (19 yrs) we had a bull market, from 1965 to 1982 (17 yrs) it was a bear market and from 1982 to 2000 (18 yrs) it again was a bull market. If this trend continues we can expect to have a bear market for the next 17 years, from 2000 to 2017 (?).

He believes that our economy and market is mirroring the Japanese market, only lagging 10 years behind. If we continue to monitor what happened in Japan we could predict what will happen in the U.S. So far it has happened and if it continues, stocks could be expected to return to late 1990's trend line, with the DOW below 4,000 in the year 2017, at almost the very moment that America's baby boomers will most need the money.

He suggests that the value of the dollar will drop dramatically. We continue to print dollars at an alarming rate (recent increase of 2,000% in 2003). Obviously, the more dollars that are available the less valuable they become. Foreign holdings now (2003) equal $9 trillion and should these holdings be reduced by as small a percentage as 1% it could be devastating. Against gold and the Euro the dollar has fallen since 2002 (by end of 2003) and as we know it continued to fall through 2011.

He suggests that this might be a good time (2003) to buy gold. He reminds us that in January 1980 (after the highly inflationary 70's) gold hit an all time high of $850 an ounce and many investors were convinced that was the only true money and that it would go up for ever. So they bought gold . . . and regretted it for the next 20 years. Gold was $342 at the end of 2003 and if history tells us anything it is that we should be buying gold starting in 2004 (gold as of 6/2012 is just over $1,500 an ounce). It seems he was right, but he also suggests that this be carefully reviewed around 2015 since things could be quite different at that time.

He is very concerned about the fact that US companies profits have been declining for the past 5 years, yet the stock market continues to move up. He didn't believe this trend could continue. In the 1990's people 'were not investing', they were having a lark. Laughing. Playing. Getting rich. They had no idea of the rules. No concept of history. No clue about the risks. Investing was a game to them and thanks to their ignorance, they were winning. He suggests that they got not what they expected from their investments, but what they deserved. Interesting enough 2001 & 2002 was just a blip compared to what they were about to experience in 2008 (March 2008 to March 2009 the market declined 52%).

He is particularly critical of what he calls 'mob rules'. He believes that following the mob makes people stupid. Because of modern communications, information gets to the crowd much quicker enabling them to do stupid things quicker. Public thinking seems to have replaced individual thinking. People continue to react to stuff reported in the papers, discussed on editorial pages and on cable news programs. We no longer use 'private

personal knowledge', things we know from our own experience and observation. Thanks to the information age people seem to grow more ignorant every day. He suggests that we be suspicious of headlines in the news and opinions of the editorial pages (public knowledge). The secret to enjoying all mass movement, he says, is to be a spectator, not a participant.

He had some very interesting thoughts regarding Alan Greenspan and the Federal Reserve System

- The Federal Reserve System is merely a cartel of member banks (not a part of government) that make their money by controlling money and credit to their own advantage. They do not have much interest in rigidly protecting the value of the dollar, but neither do they benefit from its quick destruction.
- Greenspan has added $4.5 trillion to the money supply (as measured by M3) – doubling the total amount printed by all of the Fed chairmen before him.
- Investors were convinced that Greenspan wouldn't allow a serious bear market or recession. Americans would allow the bankers profits, their limousines, and boardrooms . . . they would permit a gradual ruin of the nation's currency, too. But in exchange, the Fed would manage the economy so that people did not have to worry about a serious decline. That was why savings rates were low in America. People did not have to save for a rainy day – because it never rained.
- Lowering rates, so nearly everyone thought (including central bankers), was the way to stimulate demand for money, which, in turn, would increase consumer spending and business investment, and practically force investors to buy stocks. "In Greenspan We Trust" proclaimed *Fortune* in late 2000.
- By knocking 475 basis points off short-term rates, he enticed millions of innocent consumers deeper into debt – urging them to buy new SUV's and refinance their homes as if the fate of the nation depended on it. Consumers did themselves no favor by taking on bigger mortgages and auto loans, and a few were beginning to realize it.
- By the close of 2002, foreclosures rates were at 30-year highs, bankruptcies were at a new record, and business profits were falling. (We know that these statistics have dramatically increased through 2011).

General comments and observations (from the book):

- Instead of coming up with innovative new ways to make people rich, American's financial intermediaries – notably Wall Street and Fannie Mae – came up with ways to make them poor.
- Excessive monetary stimulation and use of credit fuels the flames of irrational speculation and public participation, which involves a larger and larger group of people seeking to become rich without any understanding of the object of speculation.
- Unrestricted, people thought they were doing the reasonable thing when they bought stock at preposterous prices – because they believed prices would be even more preposterous in the months ahead. Likewise, they saw no reason to curtail borrowing and spending – not when things could only get better.
- No one seemed to notice that America had long ago shifted from high investment, high growth economy – where people were free to get rich or go bust on their own merits – to a high spending, highly regulated economy, where people expected something for nothing . . . and were willing to vote to get it.

- During the period from 1982 to 1999, the S&P 500 gained 19% a year, dividends included. From 1994 to 1999 stocks did even better and the S&P 500 rose 20% per year. Boomers were euphoric. But it was only a dream. Encouraged by TV, books, magazines, cocktail chatter and the internet, they became convinced they need not worry about stock prices going down. The more seriously they believed that buy and hold really worked, the more certain they were to lose money.
- Sales of stocks by boomers as they enter retirement should continue to outweigh the purchases being made by the next generation as they approach middle age. The study (based on demographics alone) predicts that while the market may rally periodically, its overall direction will be downward until around 2018. Demographics are the most critical factor in determining long-term market trends.
- A half-century of economic progress and a 25-year bull market had led Americans to believe things that were not true and to expect things that they were not likely to get. Never in the history of man had any people been able to get rich by spending money . . . nor had investment markets ever made the average buy-and- hold investor rich . . . nor had paper money, not backed by gold, ever retained its value for very long.
- People do not give up their general belief easily, especially one as attractive as something for nothing. Why should they have to accept a decline in their standards of living, when everybody knows that they were getting richer and richer? The author believes people must carry on with a trend until they are ruined by it.
- The monetarists say a slump can be corrected by printing more money. The Keynesians say spending it can solve the problem. Investors do not know one from the other, but they are sure something can be done.
- Wouldn't it be nice if people really could cure their financial troubles by spending more money? Who wouldn't jump at the chance to fix an overdrawn account by going out and buying a new car? Our intuition tells us it does not work. Nothing comes from nothing; adding zeros produces no positive number. Forbearance and thrift, not profligacy, lead to prosperity.
- Americans did not make nearly as much from the bull market as they thought, either. John Bogle, founder of the Vanguard group, interviewed in *Fortune* magazine at the end of 2002, explained that frequent trading by fund managers and high fees had reduced the average rate of return during the biggest bull market in history – 1984 to 2000 – to just 4.2% a year. This was a period in which the S&P rose 13% per year.
- We might try to do the smart thing, but we are not that smart. All we can do is try to protect ourselves from madness by following the most ancient and venerable traditions: the distilled wisdom of previous generations. We guess that stocks are a bad investment, for very simple reasons: "the place to find a safe and remunerative investment is usually where others aren't looking for it," writes James Grant. Everybody is looking on Wall Street. So we will look elsewhere.
- It is obvious that two elements are essential to material progress – saving and applying the savings to some useful enterprise.

I found this book quite enlightening seeing that most of what he predicted has come true. It should lead to an important question for everyone who reads the book, or this summary: ***'what should I be doing'?*** I have found that when making financial decisions it is just as important to know 'what not to do' as it is to know

‘what to do’. You need to start thinking for yourself, not with the mob. So let me give you my thoughts on this.

Let’s start with what we know is going to happen in the next 3,000 days. Not that we get a peak at tomorrow’s newspapers. We know no more about what will happen than the forecasters at the Federal Reserve or a Dial-A- Psychic Hotline. But common sense tells us that certain things will take place and knowing them will certainly make it easier to make key financial decisions.

- There will be less taxpaying workers (10,000 baby boomers retiring every DAY)
- More retirees – more on government programs – more living longer
- More money flowing OUT of 401(K) programs (more retirees) than money going IN – more sellers than buyers usually means downward pressure
- Increase in government social programs
- Increasing government debt (not deficit)
- Seniors selling off stock for more conservative (less risk) returns
- More seniors downsizing their homes (condos)
- Effects of record amounts of personal debt (affects everyone)
- Increasing taxation – decreasing benefits
- Uncertainty (market risks, future taxation, terror)

Based on the above facts we are lead to believe that traditional financial planning is just not going to cut it. The government, because of its own actions, is now conceding that taxes must go **UP** in the future. Fact: Money will never be worth more than it is today. Fact: This may be the lowest tax bracket you will ever be in. If these two facts are true, and we believe they are, then the idea of saving/investing more now, so that you can pay higher taxes on money with less value in the future may not be the best idea. Traditional thinking tells you to take as much of today’s money as you can and throw it as far as you can into the future – where it will have less buying power and be taxed the most. This is a game you may not want to play, but that is what you are doing when you put money into one of today’s government qualified plans (IRA, 401k, 403b, etc.), and, of course, that is what Wall Street wants you to do.

You will discover that the rate of return on your money and where it is stored/invested may not be as important as how to use your money. Learning how money works could be the best lesson of the day. This is why we believe you should put some of your savings in a place where the taxman can never get to it. Where you have access to it, and where it is guaranteed to be worth more tomorrow than it is today (saved not invested). We are not against buying stocks, bonds and mutual funds, but we do think that you should have some safe liquid money out of the government’s reach. Also realize that your investment could go down.

Think about it. They (government and Wall Street) want you to put money in these qualified plans so that the money is tied up for over 10 to 37 years. You can’t utilize money you can’t get to, and the only way to grow your wealth effectively is to have access to your cash so that it can be utilized. You don’t think banks or companies that raise cash for their business let the money sit in the vault? NO, they put it to work to create profits. The bank knows that they need to loan (increase the velocity of money –not to be confused with

investing money) that money (loan $5 to $9 for every $1 on deposit) over and over as quickly as possible to generate profits. The banks accomplish this feat without using any of their money but rather by using the money we deposited with them. Yet we are told to put our money where we can't get to it for many years and hope it grows enough to enable us to live off the interest it might generate. Why is the financial community telling us to do something they wouldn't do themselves, because it doesn't benefit **them** if you don't do it their way?

Traditional thinking is mired in the thought that accumulation and rates of return are two factors that will determine your future success. We believe it is far more important to understand how money works and the buying power of your dollar, and then you can more effectively and efficiently use your money.

Remember, ***"If something you thought to be true turned out not to be true, when would you want to know about it?"*** If it affected your financial future I would say as soon as possible. Also, how can you say yes or no to ideas that you don't even know exist? How can you be aware of something you're not aware of?

In traditional financial planning they are so busy selling you the products; they forget to give you the knowledge. Will the products you are asked to purchase reduce your risk, help to beat inflation, avoid taxes or eliminate penalties? If they don't, then they may continue to feed the problem rather than address and solve the problem. Attempting to solve a problem will be difficult if all of the factors surrounding that problem are not considered. Ignoring the demographic shifts and current economic trends will simply compound the unintended consequences.

You goals should be to: 1) increase your money supply today and in the future, 2) create more and better benefits, and 3) reduce the element of risk and future taxes. 4) all without spending one more dime than you are spending today.

Understanding how your money works for you, not others, is the center point in changing your thinking. We are asking you to start thinking for yourself and to prepare for these events.

You may need support and assistance when it comes to planning and fully understanding a sound financial thought process. Many professionals have the misfortune of not knowing what they should know. We have the knowledge and experience and we are willing to take the time to educate and teach you how money works. We look forward to helping you through the next 3,000 days, and beyond.

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