The Real Financial Crisis That Is Looming

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There is a financial crisis on the horizon. It is a crisis that all the Central Bank interventions in the world cannot cure. It is a financial crisis that will continue to change the economic landscape of America for decades to come.

No, I am not talking about the next Lehman event or the next financial market meltdown. Although something akin to both will happen in the not-so-distant future. It is the lack of financial stability of the current, and next, generation that will shape the American landscape in the future.

The nonprofit National Institute on Retirement Security released a study in March stating that nearly 40 million working-age households (about 45 percent of the U.S. total) have no retirement savings at all. And those that do have retirement savings don't have enough. As I discussed recently, the Federal Reserve's 2013 Survey of consumer finances found that the mean holdings for families with retirement accounts was only $201,000.

Fed-Survey-2013-NetWorthbyAge-091014

Such levels of financial “savings” are hardly sufficient to support individuals through retirement. This is particularly the case as life expectancy has grown, and healthcare costs skyrocket in the latter stages of life due historically high levels of obesity and poor physical health. The lack of financial stability will ultimately shift almost entirely onto the already grossly underfunded welfare system.

A recent article by Kelley Holland via CNBC addresses this issue:

"Part of the problem with the 4 percent rule is that it was developed in the 1990s, when interest rates were significantly higher. Retirees with their savings in safe instruments such as bonds and annuities were getting more income than retirees today do with similar assets.

Another problem, though one with a positive side as well, is that life expectancies have increased. Americans are living longer after they stop working, which means their savings have to last longer. A man reaching age 65 in 1970 could expect to live 13 more years, but by 2011 that figure was 18 years. A woman's life expectancy at age 65 rose from 17
years in 1970 to 20 years in 2011 (the most recent year for which such data is available from the Centers for Disease Control).

Research published in 2013 by Michael Finke of Texas Tech University, Wade Pfau of The American College, and David Blanchett of Morningstar Investment Management found that using historical interest rate averages, a retiree drawing down savings for a 30-year retirement using the 4 percent rule had only a 6 percent chance of running out. But using interest rate levels from January 2013, when their research was published, the authors found that retirees' savings would grow so slowly that the chance of failure rose to 57 percent."

However, that is for those with financial assets heading into retirement. After two major bear markets since the turn of the century, weak employment and wage growth, and an inability to expand debt levels, the majority of American families are financially barren. Here are some recent statistics:

**47% of US households save NOTHING from current incomes.**

American families in the middle 20% of the income scale earn less money and have a lower net worth than in 2007.

**More than 50% of the children in US public schools come from low-income households.**

**65% of children** live in households on Federal aid programs.

**62% of Americans** currently live paycheck to paycheck.

**53% of wage earners** make less than $30,000 per year.

**The wealthiest 5% of Americans have 24 times the wealth** of the average household in 2013, up significantly from 16.5 times in 2007.

**Over 100 million Americans are enrolled** in at least one welfare program run by the federal government. This figure **does NOT include** the 64 million in Social Security or 54 million in Medicare.

It is important to remember that the total population in the US is currently around 320 million. In other words, more than 1:3 individuals in the United States is currently being supported by some form of government assistance. This is at a time when roughly 70 cents of every tax dollar is absorbed by government welfare programs and interest service on $18 Trillion in debt.

Here is the problem with all of this. Despite Central Bank's best efforts globally to stoke economic growth by pushing asset prices higher, the effect is nearly entirely mitigated when only a very small percentage of the population actually benefit from rising asset prices. The problem for the Federal Reserve is in an economy that is roughly 70% based on consumption, when the vast majority of American's are living paycheck-to-paycheck, the aggregate end demand is not sufficient to push
While monetary policies increased the wealth of those that already have wealth, the Fed has been misguided in believing that the "trickle down" effect would be enough to stimulate the entire economy. It hasn't. The sad reality is that these policies have only acted as a transfer of wealth from the middle class to the wealthy and created one of the largest "wealth gaps" in human history.

The real problem for the economy, wage growth and the future of the economy is clearly seen in the employment-to-population ratio of 16-54-year-olds. This is the group that SHOULD be working and saving for their retirement years.

With 54% of this prime working age-group sitting outside of the labor force, it is not surprising that in a recent poll 78% of women in the U.S. want a "man with a J.O.B."

The current economic expansion is already pushing one of the longest post-WWII expansions on record which has been supported by repeated artificial interventions rather than stable organic economic growth. While the financial markets have soared higher in recent years, it has bypassed a large portion of Americans NOT because they were afraid to invest, but because they have NO CAPITAL to invest with.

The real crisis that is to come will be during the next economic recession. While the decline in asset prices, which are normally associated with recessions, will have the majority of its impact at the upper end of the income scale, it will be the job losses through the economy that will further damage and already ill-equipped population in their prime saving and retirement years.

With consumers again heavily leveraged with sub-prime auto loans, mortgages, and student debt, the reduction in employment will further damage what remains of personal savings and consumption ability. That downturn will increase the strain on an already burdened government welfare system as an insufficient number of individuals paying into the scheme is being absorbed by a swelling pool of aging baby-boomers.

At some point, the realization of the real American crisis will be realized. It isn't a crash in the financial markets that is the real problem, but the ongoing structural shift in the economy that is depressing the living standards of the average American family. There has indeed been a redistribution of wealth in America since the turn of the century. Unfortunately, it has been in the wrong direction as the U.S. has created its own class of royalty and serfdom.

For many, retirement years will not be golden. They will simply be more years of working to make ends meet as the commercials of "old people on sailboats," promoted by Wall Street, will become a point of outrage. While the media continues to focus on surging asset prices as a sign of economic health, the reality is far different.

The real financial crisis in the future won't be the "breadlines" of the 30's, but rather the number of
individuals collecting benefit checks and the dilemma of how to pay for it all.

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