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STEVEN F. CARTER
CERTIFIED FINANCIAL PLANNER™ Practitioner

CARTER FINANCIAL, LLC

4225 Executive Square, Suite 1030
La Jolla, California 92037-1486
Phone: (858) 678-0579 • Fax (858) 546-0792
www.SteveCarterFinancial.com

CLIENT BULLETIN

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- ***Trouble Ahead?***

There are not any easily identifiable bubbles in the U.S. economic/financial atmosphere right now that need to be corrected, but if there were one, it would be student loans. While defaults have fallen for most forms of consumer debt like mortgages, credit cards and auto loans, severely delinquent student loans have soared since 2012. A record $89.2 billion of student loans was in default at the end of June and approximately 11% of the $1.5 trillion federal student loan portfolio is 90 days or more past due. The true rate is likely double that because only half of the loans are currently in the repayment phase. And let's be clear - the federal government desperately needs this debt to be paid off – student loans represent the largest **financial** asset of the U.S. government (sources: Congressional Budget Office; New York Federal Reserve Quarterly Household Debt Survey).

- ***How Did We Get Here?***

The short answer appears to be excessive availability of government loans for higher education. Of course, every young person should have the opportunity to get a higher education if they want one, but too much easy money has warped the higher education system. Without it, our universities could never have gotten away with the egregious price increases of recent decades. But what has enriched our institutions of higher learning may have crippled a generation of students with debt that will sharply curtail their career choices and their retirement security.

- ***Tale of Two Cities***

Consumer spending, as measured by retail sales, accounts for approximately 70% of the U.S. economy and it has been strong recently. The broad term "retail sales", however, is antiquated. It really is a tale of two economies. On the **retail outlet** side out of the ledger, the picture is not bright. 7,037 retail stores in the U.S. closed through 6/30/19, already exceeding the 5,864 closures that occurred during all of calendar year 2018. 2019 store closures are on pace to exceed the all-time record of 8,139 from 2017. **Online sales**, meanwhile, led by Amazon's Prime Day sale on July 15th have soared 16 percent in the past 12 months (sources: Commerce Department; Coresight Research).

- ***Currency Games***

The US Treasury labeled China as a "currency manipulator" last month. Since 1988 the U.S. has accused three countries of weakening their domestic currency to gain a trading advantage – Japan (1988), Taiwan (1988 and 1992) and China previously (1992-1994) (source: Treasury Department).

- ***Danger Will Robinson***

Beware of robocalls, especially ones purportedly from Social Security telling you that your account had been suspended. The first hint that such phone calls are bogus is that the recording refers to the "Department of Social Security." There is no such thing. The Social Security *Administration* doesn't call individuals to tell them their accounts have been suspended due to "suspicious activity." Crooks are just trying to scare people into giving them their Social Security numbers that leads to identity theft. Just hang up. Also be on the lookout for spoofing, which is when a caller deliberately falsifies the information transmitted to your caller ID display so it appears that an incoming call is coming from a local number or a government agency. We know how scary such phone calls can be to elderly, more isolated individuals so please pass this along to a parent or grandparent who may be more vulnerable to these types of scams.

- ***You Think We're Unstable?***

Earlier this month Argentina's presidential primary elections caused shock waves in that country when current President Mauricio Macri suffered an unexpected defeat. After the election, the Argentine stock market dropped 48%, the interest rate on their central bank benchmark interest rate rose 74.8% and the Argentine peso depreciated by 20% - all in one day!

- ***Less Than No Interest***

When you lend money you expect to be paid by the borrower for the use of your money and to compensate you for the risk of not being repaid, right? Not so much anymore. There are currently $15 trillion worth of government bonds around the world with negative yields. That means, essentially, that savers buying these bonds are **paying** the government to store their money rather than receiving interest. Like pink hair, negative interest rates don't occur naturally and are wholly synthetic (source: Bloomberg Barclays Global Negative Yield Debt Index).

- ***Why are there Negative Interest Rates?***

Most of the negative rates are in countries in the Eurozone (along with Japan) that have sputtering economies. It is a last-ditch attempt by governments to coerce banks into lending in hopes of reviving their moribund economies. Unfortunately, the cure is often worse than the disease. Negative interest rates act as a tax on the financial system of a country and are incredibly damaging to the banking sector. Critically, subzero yields have not worked in reviving the economies of the countries where they have been applied.

- ***Could It Happen Here?***

While the possibility of negative rates in the US cannot be entirely ruled out, the need to experiment with them here is not as high as in other countries. Inflation in the U.S. is still in the ballpark of 2% and the US economy is still expanding, albeit modestly. But what would happen if interest rates did turn negative here? It would severely discourage savings – would you be willing to **pay** interest to your bank for the privilege of depositing money with them? Even more importantly, negative interest rates are a dangerous game because they take away the Federal Reserve's main tool to contend with deteriorating economic conditions in the future – the ability to lower interest rates to stimulate the economy.