
Funny Money and the Super-Rich

By Martin Hutchinson *Thu, Apr 11, 2013*

The publisher of The Prudent Bear website blames U.S. monetary policy for empowering tasteless parvenus to leverage their way to the top—or at least onto the Forbes 400.

Increasing inequality is bemoaned by the left worldwide, with the *Financial Times*' Edward Luce doubtless making President Obama choke on his cornflakes by claiming that "U.S. inequality will define the Obama era."

Yet contrary to the left's fond belief, the increasing inequality and the crass behavior of the super-rich are responses, not to inadequate levels of taxation, but to two decades of monetary policy that has imposed negative real interest rates on the world economy.

Ben Bernanke, his predecessor Alan Greenspan, and their imitators abroad are responsible for the rise of a global nouveau riche class that is not only uniquely privileged, but in many (though not all) cases uniquely unpleasant in its ethics and behavior.

Self-made, through leverage

If you compare the first "Forbes 400" list of the richest Americans in 1982 with the 2012 list, you will notice a startling change. Whereas a clear majority of the 1982 list—32 of the top 50—had inherited their money, in 2012 a larger majority of the list—34 of the top 50—were self-made, coming from families that were poor or middle class, and in most cases without a significant business presence. Over such a short period (many of the top names of 2012 were already on the 1982 list) that's a remarkable change.

Another change since 1982 is that the rich have got richer; the combined net worth of the Forbes 400 was 2.8% of U.S. GDP in 1982, and 11.5% of GDP in 2012—in other words, the average wealth of a Forbes 400 member had increased by over 4 times as a share of the U.S. economy, thus by 8 times in real terms, or by over 20 times in money terms.

Naturally, you'd expect the proportion of self-made billionaires to have increased between 1982 and 1997, because of the huge bull market in U.S. stocks, and indeed it had, but only from 18 out the top 50 to 23, a proportion close to that of 1918.

Only since 1997 has the great switch to self-made ultra-rich taken place, with a corresponding further increase in fortune size that's not explained by the relatively modest growth in stock values (less than doubling in nominal terms, up only 10-20% in real terms) during the period.

The enablers

The explosion in self-made super-rich from 1997 to 2012 and the increase in their net worth were due to the same cause: the highly expansionary monetary policy instituted by Greenspan in February 1995 and exacerbated by Bernanke since 2006.

The mechanism is quite simple. Interest rates close to or below the rate of inflation favor borrowers over lenders, since borrowers are able to attract borrowed capital at close to no cost in real terms.

Hence highly leveraged strategies, which rely on borrowing large amounts of money and investing in relatively low-yielding assets, create wealth very rapidly, enabling the nouveaux riches to overtake established wealth holders.

The key to getting rich in the modern economy is thus no longer the ability to build a good long-term business, but access to cheap leverage. Technology has also had an effect; businesses that are largely virtual and essentially ephemeral, such as Google and Facebook, can be built up much more quickly than old-fashioned businesses requiring massive investments in bricks and mortar or worldwide sales forces.

Return of old money

There are three conclusions to be drawn. First, the prevalence of nouveaux riches is a temporary phenomenon produced by pathological monetary policies worldwide; once those monetary policies are changed, most of the fortunes built largely on leverage will vanish.

Second, adopting leftist policies of high tax rates will only cement the current wealth structure in place. It will make it impossible instead of over-easy to create new fortunes, and will thus increase the dominance of the current nouveaux riches in the world economy.

Third, the unspeakable vulgarity of modern plutocrat culture is also a passing phase. By 2030, London house prices will have crashed, and the majority of nice homes will again be owned by those with long-established money, once again able to compete in the housing market.

The ultra-rich will no longer have to perpetuate their tottering overleveraged empires through pointless international “deals” but will settle to building family dynasties, while deploying their long-term fortunes in ways that are truly enjoyable.

Resentment of the super-rich is generally an unpleasant emotion, detracting from life’s fulfillment and leading to immoral and economically counterproductive government meddling. Currently, however unpleasant are the current plutocrats, resentment should be turned squarely towards the source of their ill-gotten wealth: Ben Bernanke and his funny money colleagues worldwide.

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