THE GLOOM, BOOM & DOOM REPORT

ISSN 1017-1371 A PUBLICATION OF MARC FABER OVERSEAS LIMITED OCTOBER 3, 2017

OCTOBER 2017 REPORT

Buying Votes with Public Money and Dismantling a Legal System that Favours Private Property

> "It is futile to try to talk facts and analysis to people who're enjoying a sense of moral superiority in their ignorance."

Thomas Sowell

> "When a managed economy begins to fail, the only direction is to manage it more and more. It's how 'democratic socialism' leads to repression."

Garry Kasparov

> "The most effective way to destroy people is to deny and obliterate their own understanding of their history."

George Orwell

> "A people living under the perpetual menace of war and invasion is very easy to govern. It demands no social reforms. It does not haggle over expenditures for armaments and military equipment. It pays without discussion, it ruins itself, and that is an excellent thing for the syndicates of financiers and manufacturers for whom patriotic terrors are an abundant source of gain."

Anatole France, pseudonym for Jacques Anatole Thibault (1844–1924)

> "In politics, nothing happens by accident. If it happens, you can bet it was planned that way."

Franklin Delano Roosevelt

INTRODUCTION

My readers know by now the deep respect and admiration I have for Big Governments and their ill-conceived economic and social policies. Mihir Sharma, a *Bloomberg View* columnist who previously worked for *The Indian Express* and *The Business Standard* and is the author of *Restart: The Last Chance for the Indian Economy*, recently hit the nail on the head in a piece about India's "demonetization" ("Modi's Biggest Move is a Total Bust — Eliminating 86 percent of the country's currency has had zero benefits", *Bloomberg*, September 1, 2017). In general, I give India's Modi relatively high marks for the reform agenda he is trying to implement (unfortunately, he is also an interventionist — just like most of today's leaders), but I fully agree with Sharma, who wrote:

> When India's prime minister announced last November that 86 percent of India's currency would be worthless in hours, he presented the decree as a well-thought-out measure to attack cash "hoarded by anti-national and anti-social elements." We were led to believe that honest taxpayers would line up to return their high-value currency notes, but these "anti-national and anti-social elements" [Read "tax evaders" and "corrupt" individuals — *ed. note*.] would be unable to do so without raising suspicion. In the words of Finance Minister Arun Jaitley: "Obviously people who have used cash for crime purposes are not foolhardy enough to try and risk and bring the cash back into the system because there will be questions asked."
>
> **Well, if that's true, then apparently nobody in India is dishonest — because, according to the Reserve Bank of India's long-delayed accounting, more than 99 percent of the cash in circulation has been returned.** This isn't surprising. Indians are not the idiots their government seemed to imagine. **Within days of the "demonetization," a dozen methods to launder piles of cash had been pioneered. Instead of the world's best-planned attack on black money, India's government had launched the world's biggest legal money laundering scheme.**
>
> Eight months on, no argument advanced by the government or its backers in favor of demonetization has been validated. Some officials argued that the piles of cash the prime minister spoke of would be "extinguished," representing a transfer from black money hoarders to the Reserve Bank's balance sheet which the government could use, say, to recapitalize India's struggling banks. That hasn't materialized, and in fact the RBI has given far less than usual to the government this year.
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> **Some said that counterfeit currency would be exposed; in fact, it's less than 0.0007 percent of the cash taken in.** The prime minister himself argued that demonetization would "break the back of terrorism" by cutting off sources of funding. Instead, this has been among the bloodiest summers for Indian security forces in Kashmir. This week, Jaitley argued that the move would change Indians' behavior, encouraging them to use digital payments instead of cash; but as I've pointed out in the past, demonetization is the exact opposite of what Cass Sunstein would call a "nudge."
>
> The government has been reduced to boasting that the fact that almost all the cash was returned shows how efficiently the government can collect money. That's like throwing yourself off a building while praising how hard the ground is.
>
> The only real, if weak, defense left is that demonetization pushed the Indian economy toward more formal ways of operating and saving and expanded the tax base. But neither of these requires a policy as incredibly destructive as demonetization. Nor is it clear that the government's claims are valid. Officials, including Modi and Jaitley, keep on arguing that the direct tax base has vastly increased. But the numbers they've released have been contradictory and deceptive. And even if the figures are correct, we've seen increases of comparable proportions several times in the past, without the trauma of demonetization. India's new goods-and-services tax is going to expand the formal economy and the tax base anyway. There was simply no need for an additional, untested and hugely disruptive policy to achieve the same end.
>
> **Exactly how disruptive was demonetization?** Well, it may have eliminated over 5 million jobs; it's certainly ensured that growth slowed. For weeks, hundreds of thousands of small businesses struggled to find working capital; many of them may have gone out of business permanently. There was so little cash that agricultural prices crashed ~ and, as a result, protesting farmers began to demand that their debts be written off. The government may give in, with dreadful consequences for India's fiscal position.
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> Most of this could have been foreseen by any half-decent economist. But the demonetization decision was taken in secret by less than half a dozen people, none of them an economist. Few governments in history have introduced something as disruptive as this with as little thought, preparation or study. [Former Governor of the Reserve Bank of India Raghuram Rajan had repeatedly opposed demonetization — *ed. note*.]
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> Unfortunately, the paucity of benefits from its sole big policy innovation may lead the government to do more harm. Both Modi and Jaitley have turned to arguing that "excess" deposits in the months after demonetization will have to be investigated. In essence, this means that India's notoriously corrupt tax administration — already being used by the government as a tool to attack the political opposition — will be given a free hand. A "raid raj" isn't just illiberal, it will further depress already weak business sentiment.
>
> India's government has learned no lessons from this fiasco. Why should it? It hasn't suffered at the ballot box. Enough voters bought the idea that demonetization may not have worked "perfectly," but at least Modi tried. As long as that remains true, the government will surely be tempted to launch some other scheme soon that is equally unusual, unnecessary and counterproductive [emphasis added in each instance].

My readers may not agree with everything Sharma writes, but he's got this 100% right: "Within days of the 'demonetization,' a dozen methods to launder piles of cash had been pioneered. Instead of the world's best-planned attack on black money, India's government had launched the world's biggest legal money laundering scheme." Furthermore, as he points out, demonetisation hurt small business owners and less privileged people the most, as "for weeks, hundreds of thousands of small businesses struggled to find working capital; many of them may have gone out of business permanently."

I should add that, in February 2016, Raghuram Rajan, Governor of the Reserve Bank of India, had warned that demonetisation was undesirable. He later explained: "Although there may be long-term benefits, I felt the likely short-term economic costs would outweigh them, and felt there were potentially better alternatives to achieve the main goals.... I made these views known in no uncertain terms." Apparently, and not surprisingly, the United States Agency for International Development, which is the US government agency that is primarily responsible for administering civilian foreign aid, was highly supportive of demonetisation (as were other foreign Keynesian academics, such as Kenneth Rogoff, who are all clueless about how corruption really works and crime families operate).

It is not my intention to pick on India, an economy with first-class companies and which I still like from a long-term investment perspective. However, bad economic policies don't come as a one-off, but usually in endless repetition. On January 20 of this year, *Bloomberg* carried a report by Ian Marlow and Anirban Nag, "India's New Tax Squeezes the Little Guys", which stated:

> Before Prime Minister Narendra Modi introduced the country's new goods and services tax on July 1, Ansari said he was earning 6,000 rupees ($93) a day selling leather jackets, wallets, bags and belts. But India's new tax classified leather products as luxury items and raised the rate to 28 percent – more than double the 13.5 percent tax levied until June 30. Since then, his business has collapsed. "My business is down nearly 75 percent," Ansari said....
>
> India's vast informal economy – which accounts for more than 90 percent of the workforce – is struggling under India's new tax rates ... [with] broader pain being felt by many small-and-medium-sized businesses in India's informal sector, said K.E. Raghunathan, president of the All India Manufacturers Organisation.

It should be obvious to anyone (except to the interventionist Keynesians) that a GST tax of 28% is an open invitation for black markets to develop and to flourish, as well as for *more* – and not less – corruption.

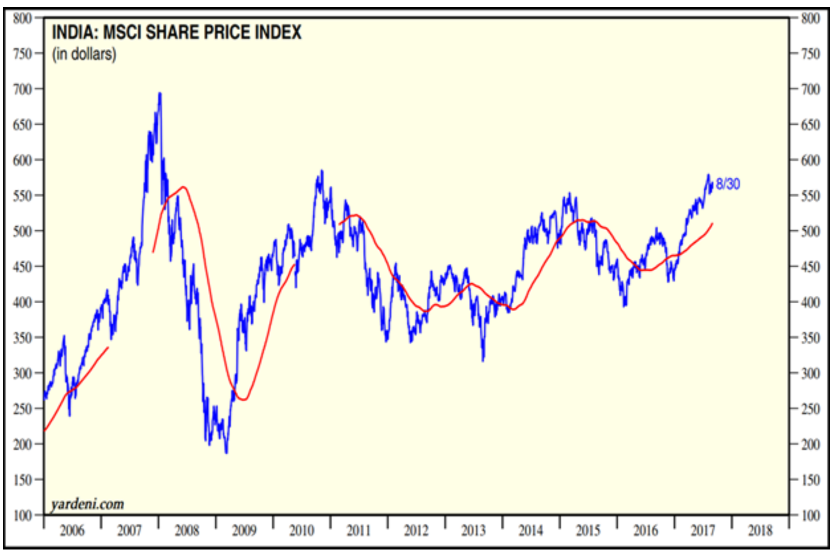
Regular readers of this report will recall that, over the past 12 months, I have repeatedly highlighted the attractiveness of Indian assets (equities, bonds, and real estate). However, in view of Indian stocks' strong performance since 2013 and in the spring of 2016, some caution is now in order. I am still a holder of the India Capital Fund, and I intend to increase my position in future, but for now I regard the stock market as being fully priced. The BSE Sensex is up by 80% from its September 2013 low, and up 40% from its March 2016 low (see Figure 1). John Thorn, who runs the India Capital Fund (www.indiacapital.com), is still enthusiastic about India, and I am a firm believer that investors should have an allocation to Indian equities even if they are likely to tread water over the next six to 12 months. (As can be seen from the excellent chart by Ed Yardeni, Indian stocks in US dollar terms are no higher now than in 2007.)

FREE MARKETS AND CAPITALISM VERSUS SOCIALISM

Above, K.E. Raghunathan explained that India's vast informal economy, which accounts for more than 90% of the workforce, "is struggling under India's new tax rates ... [with] broader pain being felt by many small-and-medium-sized businesses in India's informal sector". Unfortunately, most government interventions have the unintended (although in some instances it may be intended) consequence of "squeezing the little guys", as the *Bloomberg* article referred to above explained, and as the Peruvian economist Hernando de Soto, author of *The Mystery of Capital* and *The Other Path*, has highlighted on many occasions.

In an article entitled "The Free Market Secret of the Arab Revolutions" (see *Financial Times* of November 9, 2011), de Soto wrote that he met with Salem, the younger brother of the brave Tunisian fruit

Figure 1 **India: MSCI Share Price Index (USD), 2006–2017**



Source: Ed Yardeni, www.yardeni.com

vendor whose self-immolation triggered the Arab uprising. (I urge my readers to peruse the following story, which — in addition to being very touching — explains why low economic growth has descended upon the Western world.)

When de Soto asked Salem

> ...what his brother in heaven would say if we asked what he hoped his sacrifice would bring to the Arab World, Salem did not hesitate: "That the poor also have the right to buy and sell." It is worth remembering these words as experts busily debate the challenges for the future of the Arab revolution as countries balance the quest for democracy, fidelity to Islam, with secularism and tribal power. In the wake of the overthrow of three autocrats, not enough credit has been given to the mighty consensus that triggered the uprising — the desire of a vast, underclass of people to work in a legal market economy. In the culturally diverse Middle East and North Africa, **the one common thread is its informal economy**. [This also applies to most other emerging economies — *ed. note*.] **This is the key to future growth and indeed stability.** This huge shift began after all when the 26-year-old Tarek Mohamed Bouazizi immolated himself in front of the governor's offices in the town of SidiBouzid last December, after his merchandise was confiscated. One day after he set himself alight, thousands of people in his town and neighbouring villages took to the streets. Before a few weeks passed, many of the 180 million Arabs who work in and around the informal markets in the Middle East and North Africa were identifying with his disempowerment and sending their shouts to heaven. Millions marched under banners for reform. According to research by colleagues of mine, at least 35 businessmen followed his desperate example and set themselves on fire (13 more in Tunisia, 17 in Algeria, four in Egypt, three in Morocco and so on). People identified with his dire situation: like 50 per cent of all working Arabs, **he was an entrepreneur, albeit on the margins of the law, who died trying to gain the right to hold property and do business without being hassled by corrupt authorities**.... If Marx taught us anything, it is that the powerless can crystallise into a revolutionary class when they become conscious that they share a common suffering — and especially when a martyr embodies that suffering. There is no doubt that millions of Arabs see Bouazizi as their icon.... To understand this you have to appreciate the details: Bouazizi flicked his lighter on at 11.30am, one hour after a policewoman, backed by two municipal officers, had expropriated his two crates of pears ($15), a crate of bananas ($9), three crates of apples ($22) and an electronic weight scale ($179, second hand). While a total of $225 might not appear to justify suicide, the fact is that, as a businessman, Bouazizi had been summarily wiped out. **Without those goods, Bouazizi would not be able to feed his family for more than the next month. Since his merchandise had been bought on credit and he couldn't sell it to pay his creditors back, he was now bankrupt.** Because his working tools were confiscated, he had lost his capital. **Because the customary arrangement to pay authorities three dinars daily for the property right to park his vendor's cart on two square yards of public space had been terminated, he lost his informal access to the market.** Without property and trade, his reputation as a reliable administrator of goods was now undermined in the only market he knew. He was not on a salary. He was a budding entrepreneur. **According to his mother and his sister, his goal was to accumulate capital to grow his business. But this was impossible as we discovered when we investigated the records and the laws he had to comply with.** To get credit to buy the truck he so needed, he needed to demonstrate he had some kind of legally recognised collateral. The only legal collateral he had access to was the family house in SidiBouzid. However, he had never been able to record a deed in the property registry, an indispensable requirement for using the house as a guarantee. **Compliance requires 499 days of red tape at a cost of $2,976. To create a legal enterprise he would have had to establish a small sole proprietorship. This would require taking 55 administrative steps during 142 days and spending some $3,233 (12 times Bouazizi's monthly net income, not including maintenance and exit costs).** Even if he had found the money and the time to create a sole proprietorship firm the law did not enable him to pool resources by bringing in new partners, limit liability to protect his family's assets, and eventually, issue shares and stocks to capture new investment. The forces of the market have come to the Arab world — even if governments didn't invite them in. Political leaders must realise that, since Bouazizi went up in flames and his peers rose in protest, poor Arabs are no longer outside but inside, in the market, right next to them. The Arab consensus ahead is undoubtedly about more than just emancipating the entrepreneurial poor. But Middle Eastern and African leaders cannot afford to forget what the industrial revolution was about: if their agenda does not include tackling the nitty-gritty institutional deficiencies that make most Arabs poor, they will eventually open the doors to the anti-democrats and enemies of modernity who fight democracy and modernity in their name [emphasis added in each case].

Two of my readers recently sent me articles that showed how ridiculous our regulatory system has become in the West. In one instance, a six-year-old girl who was selling orange juice on a London street corner was fined \$50. In another, a county in California decreed that schoolchildren who were cutting the grass of their neighbours' lawns needed a licence. I find it very commendable when young children try to be entrepreneurs instead of relying on handouts from the government, begging on the streets, taking illicit drugs, or attending courses on political correctness.

Naturally, most politicians have a different view of laws and regulations: the more, the better. In their view, regulation enables a more efficient allocation of resources. I visited several planned and socialist economies in the 1970s and early 1980s and I saw first-hand just how well "The Plan" worked in practice. It was a complete economic catastrophe that led eventually to the collapse of those countries' economic systems (for the reasons that de Soto explained above). The only surprise was that it took such a long time for these failed systems to collapse. They all bred unimaginable corruption from which the ruling class, as well as some smart operators, benefited enormously. I suspect that well-functioning and efficient, though informal and illegal, black markets kept these systems alive for longer than would otherwise have been the case. But that fact seems to escape righteous socialists such as New York City mayor Bill de Blasio, who, unlike de Soto, believes that (according to an interview that appeared in *New York* magazine on September 4, 2017) "the biggest obstacle to progress is the idea of private property. He spoke of a 'socialistic impulse,' and seemed to favor the idea of turning the Big Apple into Venezuela." The magazine's Chris Smith asked de Blasio: **"In 2013, you ran on reducing income inequality. Where has it been hardest to make progress? Wages, housing, schools?"**

De Blasio: **"What's been hardest is the way our legal system is structured to favor private property. I think people all over this city, of every background, would like to have the city government be able to determine which building goes where, how high it will be, who gets to live in it, what the rent will be.** I think there's a socialistic impulse, which I hear every day, in every kind of community, that they would like things to be planned in accordance to their needs. And I would, too. Unfortunately, what stands in the way of that is hundreds of years of history that have elevated property rights and wealth to the point that that's the reality that calls the tune on a lot of development.... Look, if I had my druthers, the city government would determine every single plot of land, how development would proceed. And there would be very stringent requirements around income levels and rents. That's a world I'd love to see, and I think what we have, in this city at least, are people who would love to have the New Deal back, on one level. They'd love to have a very, very powerful government, including a federal government, involved in directly addressing their day-to-day reality."

Smith: **"Unemployment is at record lows, yet the income gains have largely gone to upper-income brackets. So the income-inequality you ran against has worsened."**

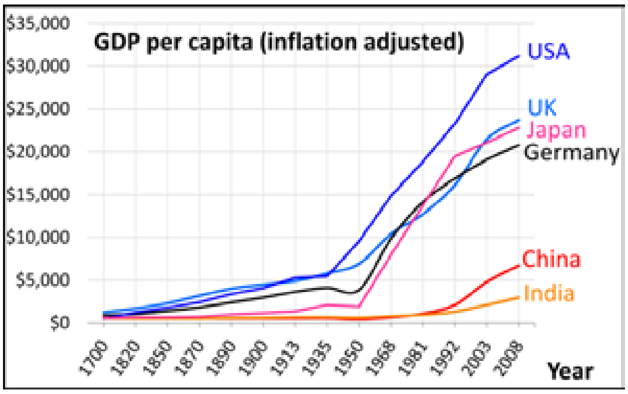
De Blasio: **"There's two ways to address it: Ask more from the wealthy in terms of their obligation to society, first and foremost from taxes.** Or raise wages and benefits for everyday people.... We helped to lead the charge to increase the minimum wage, and people are starting to feel that.

The problem is the top end. In very few ways can we address the rampant growth of wealth among the one percent. The state and the federal government have the power to do that. I called for a tax on the wealthy to fund pre-K. We didn't achieve that, but we did get the money for pre-K from the state. Now I'm calling for a millionaires tax to fix the subways and to provide the half-cost fare for low-income New Yorkers. If we're going to have a strong social fabric, if people are going to have faith it's a fair and open society, they need to see the wealthy paying their fair share. **It frustrates me greatly that we don't have the power here to tax the wealthy in this city** [emphasis added in each instance]." (Winston Churchill: "I contend that for a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle.")

Above, we heard from de Soto how the poor Bouazizi "was an entrepreneur, albeit on the margins of the law, **who died trying to gain the right to hold property** and do business without being hassled by corrupt authorities"; and just now we heard from de Blasio that the biggest obstacle to progress is the idea of private property and that most people "would like to have the city government be able to determine which building goes where, how high it will be, who gets to live in it, what the rent will be." I am sure that most of my readers would side with de Soto's view that well-established property rights (and a "tolerable administration of justice" — Adam Smith) are a precondition for creating prosperity. (Well-established property rights and impartial courts are the most important factors that have kept London property prices elevated over time.) Equally, most of my readers will find de Blasio's views to be outrageous, anti-business, anti-personal freedom, and inconsistent with free markets and the capitalistic system, which — despite their shortcomings — have lifted standards of living for most people across the world over the last 200 years or so (see Figure 2). (De Blasio's statement about the city government determining who gets to live in which buildings is particularly objectionable.) However, it would be wrong to dismiss de Blasio as a complete fool (as we well know some politicians to be), because he gets at least one point right when he says: **"I think there's a socialistic impulse, which I hear every day, in every kind of community, that they would like things to be planned in accordance to their needs."** (People with socialistic impulses would probably love "things to be planned in accordance to their needs" by someone like Stalin, Mao Zedong, Hitler, or Kim Jong-un.)

My point (and I have written about this before) is that most people want *more*, not less, government. Naively, people believe that governments can solve their problems when, in fact, most of their problems have been caused by government interventions.

Figure 2 **Free Markets and the Capitalistic System Lifted Global Economic Growth Rates over the Last 200 Years**



Source: www.nextbigfuture.com

(The liberal media has successfully brainwashed the public into accepting Keynesian and political interventions as desirable.) Therefore, de Blasio has a point when he says that he hears about socialistic impulses every day, in every kind of community. Today's politically correct society prefers to waste its time with tearing down important historical monuments that are a reminder of our history, even if it was not always glorious. (George Orwell: "The most effective way to destroy people is to deny and obliterate their own understanding of their history.") Important issues, such as how we are going to resolve the problem of excessive debts and enormous unfunded pension fund liabilities, etc., are ignored or neglected. Westeners prefer nowadays "not to give to society but for society to give to them", and they ardently wish for freedom from any responsibility (Edward Gibbon). I don't want to enter into a serious discussion about the tearing down of monuments of historical personalities, but I cannot omit mentioning how the liberal hypocrites condemned the Taliban when they blew up the world's two largest standing Buddhas (one of them 165 feet high), situated at the foot of the Hindu Kush mountains of central Afghanistan, in 2001. **But the very same people are now disturbed by statues of honourable people whose only crime was to defend what all societies had done for more than 5,000 years: keep a part of the population enslaved. And thank God white people populated America, and not the blacks. Otherwise, the US would look like Zimbabwe, which it might look like one day anyway, but at least America enjoyed 200 years in the economic and political sun under a white majority.** I am not a racist, but the reality – no matter how politically incorrect – needs to be spelled out as well. (And let's not forget that the African tribal heads were more than happy to sell their own slaves to white, black, and Arab slave dealers.)

But let us not digress, and return our focus to de Blasio's "socialistic impulses", which are not only evident in people's abdication of personal responsibility but also in an increasing number of academics advocating a universal basic income.

UNIVERSAL BASIC INCOME (UBI)

> "Capitalists … would welcome any commercial reorganization which would bring them a calmer life. It is, we believe, not as a remedy for the miseries of the poor, but rather as an alleviation of the cares of the rich, that Socialism is coming upon us."
>
> *Reverend William Cunningham*

Writing for CNBC, Catherine Clifford explains that, according to a study by the left-leaning Roosevelt Institute, "Giving every adult in the United States a $1,000 cash handout per month would grow the economy by $2.5 trillion by 2025" (see CNBC of August 31, 2017). According to Clifford:

> The study made economic forecasts for three proposals: a full universal basic income in which every adult gets $1,000 a month ($12,000 a year), a partial basic income in which every adult gets $500 a month ($6,000 a year), and a child allowance in which parents get $250 a month ($3,000 a year). **The larger the universal basic income, the greater the benefit to the economy, according to the report**.... Some, like Tesla and SpaceX CEO Elon Musk, see cash handouts as a solution to the imminent threat of automation to the labor force. **Musk has said that universal basic income will be a virtual necessity because robots will put so many low-skilled workers out of a job. Others, like Facebook CEO Mark Zuckerberg, think handouts could give everyone the safety net necessary to think like an entrepreneur. Zuckerberg touts UBI as a way to ensure people are not afraid to take risks to pursue the projects and business ventures they are passionate about.**
>
> Robert Greenstein, the founder and president of the D.C.-based think tank Center on Budget and Policy Priorities, called the notion too idealistic. "An effort to secure UBI would prove quixotic," he wrote in 2016. Greenstein says universal basic income is both too expensive and impossible to get through Washington, D.C. [emphasis added in each instance].

According to the CNBC article, Greenstein offered one innovative alternative. He suggested the introduction of a "carbon tax that returns its proceeds to the public via a universal payment". Greenstein added: **"If a carbon tax could pass, we might**

need to focus the proceeds available for these payments on low- and moderate-income families — so the payments would be adequate to offset the higher energy costs these families would face as a result of the tax — rather than extending the payments all the way up the income scale in universal fashion [emphasis added]"

Before rejecting the idea of a universal basic income as a measure that would bring us closer to socialism and to a planned economy, I should mention that Milton Friedman supported the idea in his book *Capitalism and Freedom*. He referred to the plan mostly as a negative income tax. He also referred to UBI as a guaranteed income, **because that's exactly what it is**. Now, it may be surprising that such an outspoken free-market capitalist as Mr. Friedman would support giving people money for nothing. However, according to Matt Orfalea (www.patreon.com), the following are Friedman's reasons in Friedman's words:

> **1. To reduce government bureaucracy**
> A single guaranteed income program could replace the current government maze and mess of 126 separate anti-poverty programs. We should replace the ragbag of specific welfare programs with a single comprehensive program of income supplements in cash — a negative income tax. It would provide an assured minimum to all persons in need, regardless of the reasons for their need.... A negative income tax provides comprehensive reform which would do more efficiently and humanely what our present welfare system does so inefficiently and inhumanely.
> **2. The efficiency of free markets**
> Markets allow people to vote with their dollars. Businesses must compete for these dollars/votes by offering a better price or higher quality product. That goes for food, housing, nearly anything. But in order for this voting power to work, people must have at least a minimum amount of money to vote with, and **they must have the freedom to choose how to spend it.**

In theory, Friedman is right. People should have choice in how to spend their money. However, since close to 50% of Americans have no savings at all, they have so far not proven that they are very responsible in how they spend their money. But, let us provide a basic income of, say, $2,000 per month and *require* each adult person who gets the basic income to purchase private health insurance. How does Friedman guarantee that people will be responsible enough actually to do so? Don't forget that Friedman proposed getting rid of the current welfare system, which naturally would also include the entire healthcare system. It is far more likely that at least 30% of the basic income recipients will spend their income on i-phones, drugs, booze, imported electronics, holidays, etc., than on health insurance. **Therefore, it wouldn't take long before the socialists — and the Republicans, I might add — introduced Obamacare-like programs to ensure that everyone has government-sponsored healthcare coverage, which would lead to people receiving a basic income and all kinds of welfare and health benefits.** Also, how does Friedman propose to deal with illegals? Should they also get the basic income? The point is simply that I fully support the idea that people should have the freedom to choose how to spend their money; equally, however, I believe they should assume responsibility for providing for themselves in the event of emergencies, either by having substantial savings or through taking out private health insurance.

To return to Matt Orfalea on Friedman:

> The proposal for a negative income tax is a proposal to help poor people by giving them money, which is what they need, rather than as now, by requiring them to come before a government official to tally all their assets and liabilities and be told that you may spend X dollars on rent, Y dollars on food, etc.
> **3. To end the welfare trap**
> With a guaranteed income it pays to work. You can always work to earn more. **However, the current welfare system punishes you for working. If you take a job and increase your income, you lose your benefits.** A guaranteed income removes that disincentive to work, and allows everyone to earn more without being penalized.
>
> **The number of people on welfare has been skyrocketing. Why? Because once they get on welfare, we make it almost impossible for them to get off.** In order for somebody who gets on to get off, he or she has to be able to have a really good job, because to get off gradually, to earn a little bit, now doesn't pay....
> **4. To enable work**
> Removing the burden of needing to earn an income, even partially, will help enable people to do work that is otherwise not compensated in a free market economy, such as charity or volunteer work.
>
> One of the great virtues of the negative income tax, in my opinion, is that by taking off the mass burden of income maintenance it would make it possible for private charitable organizations to do [charity work].
> **5. Justice and equality**
> Civil rights leader Martin Luther King proposed a guaranteed income to promote justice and equality. Milton Friedman (although more concerned with reducing government) agreed: "The virtue of [a negative income tax] is precisely that it treats everyone the same way ... there's none of this unfortunate discrimination among people."

BUT, IS A UNIVERSAL BASIC INCOME SUCH A WONDERFUL IDEA?

> "I predict future happiness for Americans if they can prevent the government from wasting the labors of the people under the pretense of taking care of them."

Thomas Jefferson

I agree that a universal basic income has some appeal (as do wealth taxes, negative interest rates, rent controls and subsidies, etc.). However, let me point out some of the problems associated with the idea of a UBI. If the Roosevelt Institute believes that "the larger the universal basic income, the greater the benefit to the economy", then why not give every adult in the United States a $10,000 — or $100,000 — cash handout every month, which would grow the economy not by $2.5 trillion by 2025, but by 25.5 — or $255 — trillion?

Above, Robert Greenstein of the Center on Budget and Policy Priorities called the notion "too idealistic", and I call it complete economic sophism. To argue that the larger the universal basic income, the greater will be the benefit to the economy is like saying the more money we print, the greater the economic benefits will be. (It has been tried before repeatedly, with catastrophic consequences — just look at Zimbabwe.)

Elon Musk might just as well have said that universal basic income had become a virtual necessity at the end of the 19th century because technological progress in agriculture would put so many low-skilled farm workers out of a job. Sure, robots will put many workers out of a job. But my readers might consider *why* more and more companies are replacing humans with robots. Workers have become too expensive (not their salaries, but the contributions companies have to pay to the government for each worker); their work ethics and dependability have diminished; and they are not only low-skilled, but have become unskilled (as in possessing no skills whatsoever) workers. I live in Thailand, which has close to 70 million inhabitants and low wages. However, it is practically impossible to find a qualified carpenter, plumber, electrician, or computer repairman. In my opinion, the problem is not a surplus of labour because of robots, but a shortage of skills because of ill-conceived educational and economic policies (especially monetary policies, which encourage playing the asset market appreciation instead of acquiring skills). Also, Mark Zuckerberg's notion that "handouts could give everyone the safety net necessary to think like an entrepreneur" is complete nonsense, but is not surprising coming from someone who makes his money from Facebook. Does Zuckerberg really think that all the great inventions of the last 5,000 years or so, and especially during the 19th century's Industrial Revolution, were the result of people enjoying "the safety net necessary to think like an entrepreneur"? My view would be precisely the opposite. The more of a "safety net" people have, the less they will be motivated to think and *act* like an entrepreneur. My personal observation (of course, there are exceptions) is that the less people work, the less they will think *productively*.

Greenstein's idea that a carbon tax could finance payments to low- and moderate-income families is no different than the notion of introducing an additional tax on high-income earners, estate taxes, a GST, or a value-added tax.

I have far more sympathy for Milton Friedman's view that "a single guaranteed income program could replace the current government maze and mess of 126 separate anti-poverty programs". **However, Friedman should know better. It is completely unrealistic that "a single guaranteed income program" would replace the current maze of anti-poverty programs.** Why? For the same reason Western countries don't have a flat tax: too many interest groups benefit from the current maze of tax laws and anti-poverty and immigration programs. (Tacitus: "The more corrupt the state, the more numerous the laws.") Therefore, a guaranteed income program is unlikely to replace the maze of anti-poverty programs; it would be more likely to increase the abuse that comes with such redistribution, and with any other government-sponsored program. (As an aside, who would decide on the amount of "handouts" the government should "give everyone" to enable them "to think like an entrepreneur" and "to do work that is otherwise not compensated in a free market economy, such as charity or volunteer work"? Hopefully, Friedman wasn't thinking of de Blasio, who would plan everything in accordance with people's needs.)

There is, however, one point raised by Friedman with which I fully agree. He opines:

> **With a guaranteed income it pays to work. You can always work to earn more.** However, the current welfare system punishes you for working. If you take a job and increase your income, you lose your benefits. A guaranteed income removes that disincentive to work, and allows everyone to earn more without being penalized.
>
> The number of people on welfare has been skyrocketing. Why? Because once they get on welfare, we make it almost impossible for them to get off. **In order for somebody who gets on to get off, he or she has to be able to have a really good job, because to get off gradually, to earn a little bit, now doesn't pay....**

I once attended a presentation by Larry Lindsay, who made precisely the same point, offering several examples of how the current welfare system was a disincentive to work. But, as I said, I doubt that a basic income would *replace* existing welfare programs. Furthermore, whereas the de Blasios of this world would likely be in favour of a universal basic income, they would argue that it wouldn't make sense to provide wealthy people and high-income earners with a basic income. (I tend to agree with this view.) However, who would decide what the threshold is to qualify as a "high-income" recipient? (De Blasio believes that he should take these decisions.) What about the 18-years-plus children of the super-wealthy? Should they receive a basic income if they don't work? I can assure my readers that once the socialists go over the basic income issues, the UBI laws and regulations will be little better than the existing welfare system.

I wish to make two final points about the universal basic income. In the 1970s and early 1980s, I visited several Eastern European socialist republics, as well as Russia, Vietnam, and China. All these countries had some sort of universal basic income program in place. (Nowadays, several Middle Eastern countries have such programs, but only for their own citizens – not for the guest workers, who do most of the work.) I can assure my readers that these basic income systems neither acted as an incentive for people to work, even less so to work productively, nor did they "give everyone the safety net necessary to think like an entrepreneur", as Zuckerberg maintains. In fact, quite the contrary: they made people lazy, lethargic, unhappy, poor, and completely uninterested in working.

Also, having spent a lifetime reading economic works and observing carefully how economic systems work in practice, I have come to the conclusion that some beautiful theories simply don't work in the real world. The Keynesian tenet that governments should create deficits in recessionary times and surpluses in economic expansions is wonderful, but it was seldom applied in democracies, and never in recent times. Socialism and communism are very enticing ideas – that is, until you see the results, which I have seen; in every case, they were not heartening.

I am not arguing that capitalism doesn't have shortcomings and weaknesses (it is a very cruel system), but as the economist Joan Robinson opined, "Any government which had both the power and the will to remedy the major defects of the capitalistic system would have the will and the power to abolish it altogether."

The de Blasios of this world will be more than happy to provide a basic income for everybody, and to ensure that "the city government [is] able to determine which building goes where, how high it will be, who gets to live in it, what the rent will be". When self-driving cars are introduced, they will also have you picked up in the morning and taken to your workplace, where you will be led to a workstation (factory, office, etc.). At the end of the workday, you will be picked up again and taken straight home (no pit-stops at pubs, nightclubs, etc.), where you will be fed meals planned by de Blasio and his associates. In the event that you break any of the rules introduced by the city government, a self-driving car will pick you up and deliver you safely to a wonderful facility adorned with bars on the windows and cages, where you will be locked up because you violated the city government's plans.

I want my readers to clearly understand this: a universal basic income is a very appealing idea, as is socialism, colonialism, democracy, the welfare state, charities, and international organisations for the protection of human rights, wildlife, the environment, people's health, the climate, etc. Unfortunately, sooner or later, all of these ideas are highjacked either by the wrong people or by very evil people, who use them to advance their own self-interest and abuse their power.

Furthermore, the universal basic income is probably the most dangerous such idea. When the government controls the money that it allocates to people, it will also have full control over them. (Thomas Jefferson: "A government big enough to give you everything you want, is strong enough to take everything you have.") Maybe people prefer, as de Blasio mentioned above, that the government should plan everything because they are prepared to abandon freedom from responsibility for the security they believe the state will give them (Edward Gibbon); however, they should also be aware that, sooner or later, they will lose all their freedom and will be enslaved by an evil leader.

I am aware that my affluent readers may not be particularly interested in the universal basic income issue because it won't impact the performance of assets over the next three days, one month, or possibly even over the next few years. However, as I said above, once the government has full power over how it allocates money to people, it will also use its power to take money away. The question is: from whom? Obviously, not from people who have no money to start with. The government will go after the asset holders, who have been fattened by central banks' expansionary monetary policies over the past few years. (De Blasio: "It frustrates me greatly that we don't have the power here to tax the wealthy in this city.") I concede that the government has a few options for "financing" the UBI. It could just use helicopter money — that is, issue cheques to every adult person, and either have the Fed pay for it (by increasing its balance sheet) or just increase the federal deficit. (Don't believe for a minute that the UBI wouldn't boost the deficit.) Or, as I indicated, the government could raise taxes on the super-wealthy (income taxes, wealth and estate taxes, etc.), which would be politically very popular among 90% of the population. (President Trump, despite his universal ignorance, will probably know this and propose large tax increases on the super-wealthy in order to swing the 2020 election in his favour.) Since, I don't expect the UBI to boost economic growth at all (except possibly, but not with certainty, in the very short term), it is likely that the government will implement a cocktail of all the policies I have mentioned above – not necessarily simultaneously, but likely at different times.

So, what are the consequences of these rather disturbing facts for Western democracies? I doubt that democracies will survive in their present form. As de Blasio said, it is probable that people will give up their freedom voluntarily for (perceived) security. Freedom of expression and of the press will be a thing of the past. Economic growth rates will decline further. Social unrest will increase, and the self-driving limousines that will take people to the special facilities with the nice iron bars on the windows and cages (which, of course, are operated by robots) will work overtime. In order to hold their grip on power, Western governments will become more belligerent and invent one villain after another: every Ayatollah, Saddam Hussein, Muammar Gaddafi, Bashar Hafez al-Assad, Recep Tayyip Erdogan, Xi Jinping, and the current favourites who occupy the top two places on the "hit" parade: Vladimir Vladimirovich Putin and Kim Jong-un. (Didn't you know? Only China, Russia, and North Korea have hackers.) The guiding principle will be: Show me the country and I'll find you the crime. (Lavrentiy Beria, "Show me the man and I'll find you the crime.")

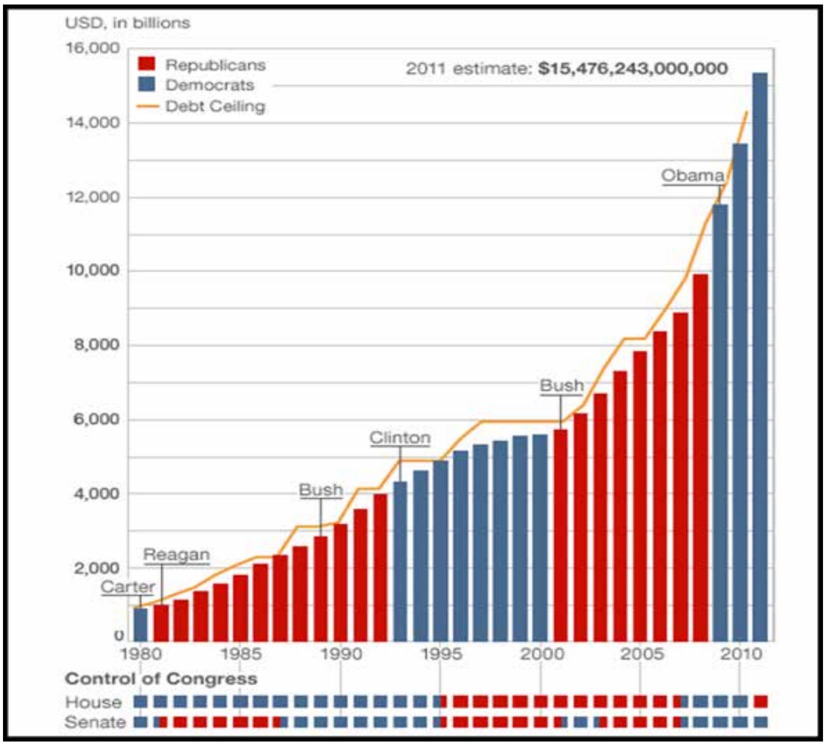
None of the people listed above are particularly pleasant, but they all have one trait in common: they didn't pay tribute to the Great Empire and the other Western imperialists and colonialists (The Latin word *tributum* is a payment in kind that a party gives to another as a sign of respect or, as was usually the case in historical contexts, of submission or allegiance. Various ancient states exacted tribute from the rulers of land which the state conquered or otherwise threatened to conquer. To be called *tribute*, recognition by the payer of political submission to the payee was normally required. Tribute also served as protection money.)

And what are the investment implications of these encouraging and uplifting developments that will bring us even closer to socialism?

INVESTMENT OBSERVATIONS

As my readers can imagine, I am dead opposed to the universal basic income proposal because it will unlikely replace existing welfare programs and, therefore, will vastly increase the federal government's deficits. Deficits will rise even without the UBI, independent of whether the Democrats or the Republicans are governing (see Figure 3). This will be particularly true under President

Figure 3 **The US Government Debt Will Continue to Increase and Lead to Widening Fiscal Deficits (US Government Debt, 1980–2011)**



Source: www.whitehouse.gov

Figure 4 **US Dollar Index, 2010–2017**

Source: www.stockcharts.com

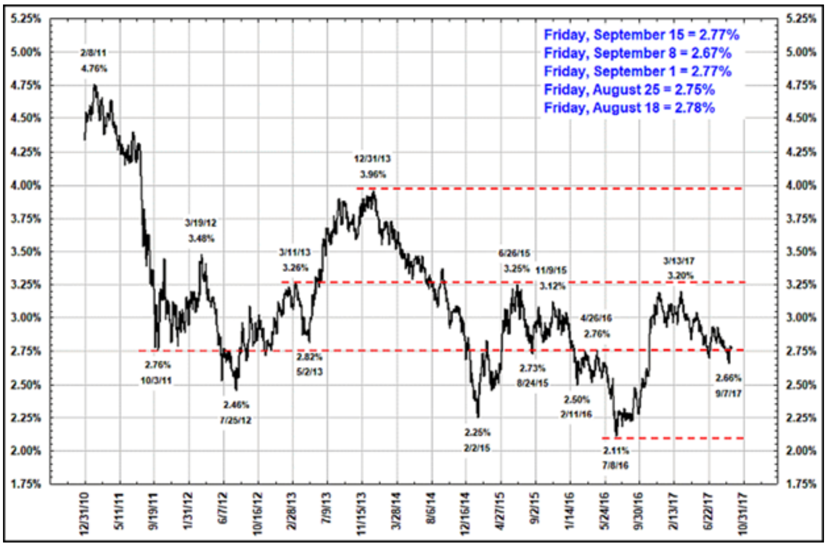
Trump, who will increase welfare benefits — or even introduce the UBI — to please the Democrats and obtain their support in the 2020 election while at the same time massively increasing US military spending in order to please the military, which has already taken over the White House. (It's worth noting that the US debt doubled under President Obama, to currently over US$20 trillion.) But what is really remarkable is that, despite the doubling of the federal debt under the previous administration, and the Federal Reserve simultaneously pursuing an extremely expansionary monetary policy, the US dollar remained strong until this year (see Figure 4). As an international investor who always has a large US dollar exposure, and as a US dollar income recipient, I was certainly happy about the currency's strength, but I certainly didn't expect the magnitude of that strength. (From the May 2011 low, the US dollar index rose by 42% to the early January high.) Equally surprising for many investors (not for me) was this year's dollar weakness given the Fed's tapering, the lifting of the Fed fund rate, and the talk about reducing the Fed's balance sheet — all at a time when the European Central Bank (ECB) and the Bank of Japan (BoJ) were still expanding their balance sheets. Some people will argue that, in the current markets, "nothing makes sense". But this is not my view. Between 2011 and early 2017, the US economy performed somewhat better than other major industrialised nations, and the US also had far higher interest rates than Europe or Japan (see Figures 5 and 6). As an example, ten-year US Treasuries are currently yielding 2.24%, whereas French sovereign bonds (same maturity) are yielding 0.72%.

However, since the beginning of 2017, investors' sentiment has changed. From Figure 4, we can see that the US dollar index spiked up with the election of Mr. Trump, who had been critical of artificially low interest rates and the Fed. However, investors soon realised that there is a difference between what Mr. Trump says today and what he will say a day later, when he suddenly found low interest rates to be very convenient.

Furthermore, investors began to have doubts about the Fed repeatedly hiking interest rates in 2017 when they woke up to the fact that once an incorrigible dove, the Fed would always be a dove, and that the US economy, if properly measured, was not as strong as the Fed had expected. In the meantime, European and emerging economies (especially China) surprised economically on the upside and attracted foreign capital flows, which lifted their currencies versus the US dollar and their capital markets versus the S&P 500.

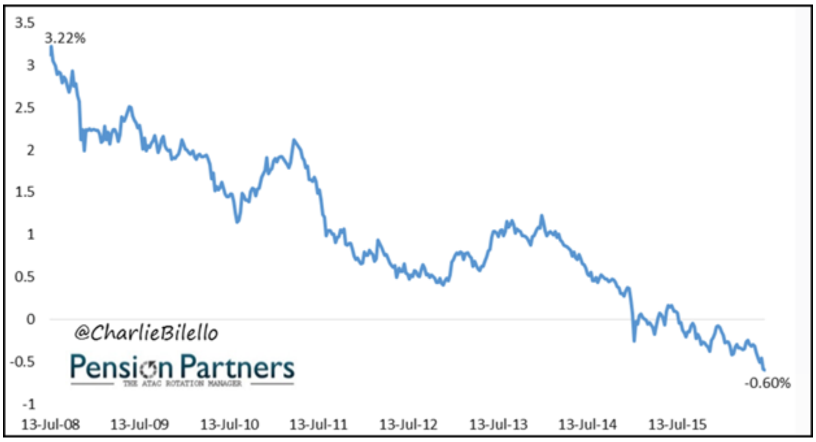
Where do we go from here? **The US dollar is near-term oversold and investors' sentiment is extremely bearish.** This is exactly the opposite of the dollar's position at the beginning of the year. At the time, the US dollar was overbought and investors' sentiment was extremely bullish (see Figure 7). Therefore, I believe that the US dollar could rebound against the Euro, and especially against the

Figure 5 **US Treasury Bond Yield (30-year constant maturity), 2010–2017**



Source: Ron Griess, www.thechartstore.com

Figure 6 **Switzerland 10-Year Sovereign Bond Yield (10-year yield), 2008–2016**



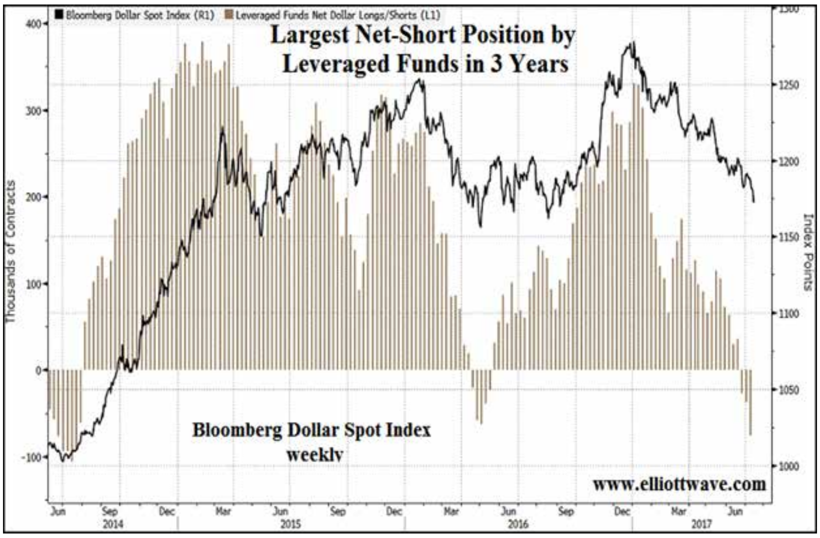
Source: Charlie Bilello, Pension Partners

Japanese Yen. (The US dollar index could recover to between 95 and 97 – see Figure 4.) However, my readers should note that this is not a high-confidence view, because the risk is extremely high that the US dollar will weaken far more in future. (I explained the reasons for this bearish view above.)

Other reasons to be concerned about the US dollar are the following. Mr. Trump has the rare talent of alienating both friends and allies of the US, as well as countries the US perceives to be "enemies" (China, Russia, Iran, Venezuela, Cuba, North Korea, etc.). Given that the US still runs large trade and current account deficits, and that the US dollar is still the world's most important reserve currency, unfriendly or even hostile relations with large US dollar holders is a senseless strategy that can only lead to a weaker currency over time. However, it is likely that Mr. Trump doesn't care at all about a weaker dollar. On the contrary, in order to make "America great again", a very weak dollar might help temporarily and could be useful ahead of the 2020 election. (I should add that a strong dollar has never been a priority of the US.)

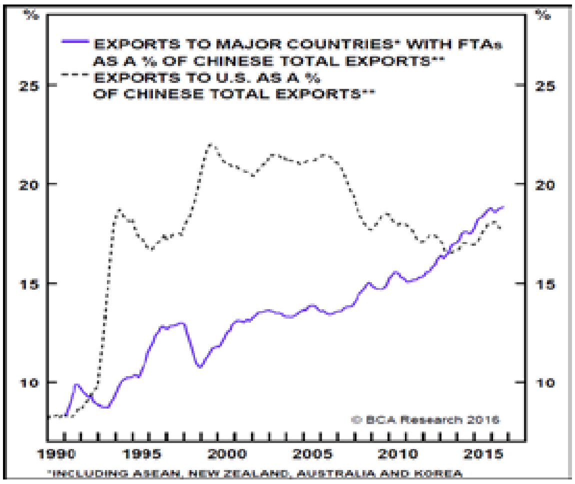
Another point investors should consider when deliberating about the US dollar is the fact that more and more international trade is being transacted outside of the United States. Currently, China exports more to countries with which it has a free trade agreement (FTA) than to the US (see Figure 8). (China's exports to commodity producers are almost twice as large as to the US. Ditto for South Korea, I might add.) In the case of Russia, its top export destinations (2015) were the Netherlands (US$32.2bn), China (US$31.1bn), Germany (US$18.5bn), Italy (US$15.5bn), and Belarus (US$15.5bn); its top import origins were China (US$34.5bn), Germany (US$22.4bn), the United States (US$10.2bn), Belarus (US$10.1bn), and Italy (US$7.71bn). Therefore, it seems to me that it is only a question of time before less and less trade will be settled in US dollars, which is unlikely to be supportive of the dollar.

Figure 7 **Bloomberg Dollar Spot Index and Leveraged Funds Net Dollar Longs/Shorts, 2014–2017**



Source: www.elliottwave.com, *Bloomberg*

Figure 8 **Exports to Major Countries with FTAs and to the US as a Percentage of Chinese Total Exports, 1990–2016**



Source: Yan Wang, *The Bank Credit Analyst*

I am aware that many US investors will shrug their shoulders when hearing about the US dollar. They will argue that they are paid in US dollars, measure their performance in dollars, and pay for their expenses in dollars. Therefore, why would they care whether the US dollar goes up or down? Well, this is a typical US-centric view, which from an investment perspective makes no sense. If an investor can boost his performance by holding foreign assets (cash, bonds, equities, etc.), why would he not allocate some money overseas? Let us assume that the treasurers of multinationals, fund managers, and foreign investors became convinced that the dollar index would tumble within the next 12 months to around 80 (see Figure 4). Undoubtedly, they would shift funds out of US dollars. Such a move could be favourable for foreign assets, and especially for foreign equities and properties. **More importantly, a major shift away from US assets could have an impact on US inflation and US interest**

rates. Usually, a weak currency leads to higher long-term interest rates. But this isn't always the case in a financially manipulated world. From Figure 4, we can see that since 2011, the Euro has been very weak against the US dollar. Yet, European interest rates continued to decline because of Mr. Draghi's massive interest rate suppression scheme through the purchase of European bonds. So, let us assume that inflation picks up in the US because the combination of a weakening dollar and the introduction of a universal basic income would almost certainly boost the velocity of money (see Figure 9).

Under these conditions, interest rates would *normally* rise through market forces. But that is no longer the overriding consideration, as further massive asset purchases by the Fed could suppress any upward pressure on long-term rates. (The Fed could buy all the outstanding US long-term Treasuries and mortgage bonds as well.) In my opinion, monetisation on such a massive scale could keep interest rates down, but at the cost of the US dollar collapsing. But, even this scenario isn't written in stone. The Bank of Japan's massive asset purchases (stocks and bonds) suppressed interest rates, but have not yet brought about significant weakness in the Yen. I suppose the reason for the Yen's resilience is Japan's large foreign exchange reserves and the low exposure of foreign investors to the Japanese bond market. In the case of the US, we should expect foreign holders of US Treasuries to dump them if US dollar weakness is accompanied by another round of interest rate suppression and additional massive monetisation (QE4). I concede that if foreign central banks were also to increase their asset purchase, the dollar may not weaken against other currencies. **Still, given the fact that the US dollar has already weakened at a time when the ECB and the BoJ are still increasing their balance sheets, and amid talk of quantitative tightening (QT), further dollar weakness over the next few years (aside from a short-term rebound — see above) is likely.**

Figure 9 **Velocity of M2 Money Stock, 1958–2017**

Source: Federal Reserve Bank of St. Louis, Gijsbert Groenewegen, www.silverarrowpartners.com

Figure 10 **MSCI Eurozone ETF (EZU) versus S&P 500 Index, 2007–2017**

Source: www.stockcharts.com

Despite what I said above about further US interest rate suppression and the Fed's additional asset purchases (as soon as the economy weakens), I doubt that US long-term rates will decline much further. Long-term Treasuries made lows in July 2012 and July 2016, and I doubt that we shall see much lower rates in future (see Figure 5). **I still hold them, but I am no longer a buyer of Treasuries (and other European and Japanese sovereign bonds) at the current level of interest rates.** It is likely that the future economic stimulus policies of democratic governments will include more fiscal measures than just asset purchases by central banks. **Helicopter money or universal basic income (which is nothing other than *permanent* helicopter money) will certainly be on the table in the next recession.** As explained above, expansionary fiscal policies would probably increase the rate of inflation.

Figure 11 **Apple, 2016–2017**

Source: www.stockcharts.com

Figure 12 **Bitcoins, June–September 2017**

Source: www.investing.com

Concerning **equity markets**, I should reiterate the view I have held since last year: **emerging market and European stocks are more attractive than US equities and are likely to continue their 2017 outperformance** (see Figure 10, and Figure 12 of the August GBD report).

I still like European utility and infrastructure plays such as Engie (ENGI FP), Electricite de France (EDF), Veolia Environment (VIE FP), E.On (EOAN GR), RWE (RWE GR), ENEL (ENEL IM), Iberdrola (IBE SM), SSE plc (SSE LN), and Abertis (ABE SM). I concede that after strong upward moves, some of these stocks will need to correct on the downside. Furthermore, as explained in earlier reports, I have increased my exposure to Swiss equities, most of which have a far higher dividend yield than Swiss government bonds, which offer over 10 years a negative yield of 0.2%. **Along with US pharmaceuticals, Swiss pharma stocks such as Roche (ROG VX) and Novartis (NOVN VX) should strengthen.** (Please note the recent strength of PFE, MRK, BMY, etc.) As a reminder, the Swiss Market Index (SMI) is hardly higher than in 1998 (see also Figure 13 of the July 2017 report).

In the August 2017 report, I also discussed under the heading "Change in Leadership" that FANG and related stocks would begin to sell off – punishing the overweight tech investors. I suggested that very old and boring economy stocks (institutions no longer own them) would perform well and offset the weakness in high-tech stocks. These sectors would include, among others, fertiliser stocks (MOS, AGU, POT, etc.), energy and energy-related stocks (drillers, oil, and oil service companies such as DO, HAL, TOT, etc.), and mining companies. What is interesting is that despite the US stock market making daily new highs in mid- September, many FANG and related stocks are no longer making new highs. The NASDAQ Index made a new high on September 18, but Apple peaked out on September 1 at almost US$165 (see Figure 11). As at September 21, Apple was at US$155, down 6% from the high and it was no higher than in May 2017, while the NASDAQ is no higher than on July 26, 2017.

Clearly, the FANG and related stock have begun to underperform the US stock market.

Although I am not increasing my overall equity exposure, I recently increased my position in China Mengniu Dairy (2319 HK). I also own Bank of China (3988 HK), China Life Insurance (2628 HK), Shanghai International Airport (600009 CH), and China Yangtze Power (600900 CH). **I think that investors should**

accumulate, over time, a meaningful position in Chinese stocks. Global investors should aim at having at least 50% of their assets in emerging economies, of which at least 50% should be in China and India.

Currently, Malaysia also appears to be coming back on to the radar screen of international investors. I have increased my position in Malayan Banking Berhad (MAY MK) and CIMB Group (CIMB MK).

I recently attended a large international investment conference in Hong Kong whose participants are mostly from some of the world's largest financial institutions. The main subjects of discussion: Chinese technology stocks and crypto-currencies. I have been attending this conference for the last 20 years or so. Never before have I seen such a unanimous consensus among investors that they had to have a heavy exposure to high-tech stocks…. Furthermore, this is the first time I have known institutional investors to discuss crypto-currencies, and so passionately, with the bears and the bulls having heated arguments about their future. Contrarians, take notice. I am a believer that blockchain technology is here to stay and that crypto-currencies will replace paper money over time. However, I doubt that Bitcoins will be as valuable as some investors seem to believe (see Figure 12).

The recent announcement by the Fed about quantitative tightening depressed precious metals and mining stocks. **I shall use the current weakness to increase my position in physical precious metals.**

THE GLOOM, BOOM & DOOM REPORT

Author & Publisher
DR MARC FABER

Research Editor & Subscription
LUCIE WANG

Copyeditor
ROBYN FLEMMING
E-mail: robynfle@gmail.com
Website: www.robynflemming.com.au

Subscriptions and enquiries
MARC FABER OVERSEAS LTD
Unit 801, The Workstation, 43 Lyndhurst Terrace, Central, Hong Kong
Tel: (852) 2801 5410 / 2801 5411 Fax: (852) 2845 9192
E-mail: luciew@biznetvigator.com; Website: www.gloomboomdoom.com

Design/Layout/Production
POLLY YU PRODUCTION LTD
E-mail: pollyu1962@gmail.com