Early Signs of the Coming Economic Ice Age Are Evident

By Robert McHugh, Ph.D.
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One of the most significant and typical causes of economic collapse is starting. Just before almost every financial crisis, we see Bank regulators put the halt on lending under the guise of "protecting the taxpayer and economy from catastrophic bank credit losses." The unfounded bank regulator fear of such losses coerces banks to slow or stop lending, which is the first shot fired across the bow of a coming economic collapse. In essence, bank regulators cause the coming economic collapse by shutting down lending, which destroys business and consumer spending, which causes economic collapse and ergo increases bank losses as quality borrowers experience the fallout of economic slowdown which inhibits their ability to repay, or their ability to obtain capital financing for business expansion and normal growth opportunities. Bank regulator overzealous actions in effect become a self-fulfilling prophecy.

Recently the Comptroller of the Currency put out this warning to banks it regulates: "credit risk is now building after a period of improving credit quality and problem loan cleanup." My comment: If this is their view, then our economy is in deep trouble.

According to the Russell Sage Foundation, as reported this week on June 24th in an article by Rick Newman at The Daily Ticker on Yahoo.com, bank Risk Officers are getting pay increases, more authority in lending, with staffs being beefed up substantially. My comment: This is precisely how to destroy our economy. When risk officers are running our most fundamental intermediation economic function, the process of moving (lending) money from those who have it (banks) to those who need it (consumers and small businesses), then our economy is headed for the crapper and fast. This shift in power from line function to back room function at banks across the country is a direct result of overzealous pressure from bank regulators and a direct result of that disastrous Dodd-Frank law that was passed a few years back. In essence, bank lending is being forced to shut down. An economy cannot grow when bank lending is being shut down, where loans are only approved if a borrower can prove he does not need the money and those that do need the money cannot obtain loans due to stringent requirements from risk officers who are essentially pencil pushing numbers crunchers (a.k.a. computer analytics) with little sense for revenue generation, nor respect for creative use of capital.

Banking is a risk business by definition and it has become far too conservative. If they do not lend, then they serve little purpose. This same nonsense occurred back in the early 1990's and threw the U.S. into a severe recession, which led to Clinton's victory in 1992 overthrowing George the 1st. I know. I was running a bank back then and witnessed bank regulators imposing intimidation upon bank officers and directors to shut down the lending function. How? They march a team of senior steely-eyed regulators armed with stone-faced in-house lawyers from Washington D.C., outnumbering senior management and directors of the bank in a large room, and threaten to fire bank officers, to remove directors, to sue board members if their directives, their memorandums of understanding, and if necessary due to resistance, their cease and desist orders to shut down lending are not obeyed. I watched bank regulators twice in the 1990s, just before the 1991-1992 recession and just before the 2000-2002 recession classify good loans as bad loans, forcing writeoffs and loan loss provisions that were completely unjustified, which wiped out earnings, reduced bank capital, and in effect forced bank managements to operate under duress all across the country. Now, here in 2014, we see it happening again, only this time they have insider Risk Officers doing their dirty work for them.

The same thing happened in the late 1990s, just before the recession of 2000 through 2002. Bank regulators shut down lending, which assured a coming recession at the start of the new millennium. That time, they also slowed economic growth by limiting bank investment portfolio choices (which is another form of intermediating capital from those who have it to those who need it). A perfect example is the efforts by the Federal Reserve to shut down the FHLB, the Federal Housing Loan Board, which was lending a lot of long-term money to financial institutions at very reasonable rates in order to fund long-term mortgage loans for consumers. The FHLB served a very important purpose, but because the egos at the Federal Reserve felt they were losing control over the money supply if another government agency is lending money to banks without their permission, they pressed banks that made use of the FHLB. In the 1990s the Federal Reserve was working hard to get Congress to shut down the FHLB to stop this important intermediation. I personally testified before Congress in favor of the FHLB against this effort by the Federal Reserve. But it was a battle in the late 1990s, and I can remember Fed examiners beating the crap out of banks who borrowed long term money from the FHLB. This overzealous bank regulatory action led to the economic recession of the early 2000s.

This reality is occurring again now, and the timing is perfect as we see the multi-decade Jaws of Death stock market pattern complete, warning that the economy is soon going into a deep recession again. You see, Risk Management Officers (employees of banks mandated by bank regulators to not only be in existence, but to have high salaries and ultimate credit granting authority in banks) have no clue as to how to gauge a borrower's creativity or management skill or earnings potential from a good idea, or a willingness to pay; Risk Management Officers have no interest in boosting the economy, and are not interested one bit in generating revenue or profits for a bank. They just want to say "no" and avoid any potential losses whether such feared losses will come to fruition or not. This is a very dangerous development for our economy here in 2014 and 2015. If banks do not lend, the economy cannot grow. It is that simple. You want to know what made Clinton's presidency possible and his economic policies successful? One of his first acts as president was to get bank regulators off the backs of bankers. It worked. I know. I was there. The economy recovered.

Housing is at a freeze, construction is at a standstill. Down payment requirements are ridiculously high. Many banks are requiring 40 percent down payments for a construction loan no matter how strong the borrower's financial position is, regardless of income or net worth. Cash is what banks have, is what consumers and small businesses need, and yet banks are requiring consumers to self-fund a ton of cash required in real estate transactions. This is a bad situation. It will act like a black hole, eventually sucking/contracting our economy so fast and deep that the Fed can print all the cash it wants to and hand it to Wall Street and it will not have a meaningful effect on reversing the economy. Five trillion dollars was just printed since 2008 and handed to Wall Street and most of it did not get into the hands of the general public. Only a few benefited. It caused a ton of inflation which is not reported in the CPI numbers. Food, medical, and housing inflation. Automobile price inflation.

Want the proof? We learned last week that the net worth of the median household in the U.S. was 43 percent lower in 2013 than it was in 2008. This is remarkable but not surprising. Think about that. Net worth has declined by almost half, yet the Fed printed $5.0 trillion of new money over that same time period and gave it to Wall Street. If we listen to pundits and Central Planner economic reports, including those from the Fed, they would have us believe everything is chugging along nicely. Bullbleep. 1st quarter 2014 U.S. GDP was negative. It could be revised lower soon. If we see the second quarter also negative, then by the Central Planners' own admission, the U.S. would officially be in a recession. Weather related? That dog don't hunt.

In my book, The Coming Economic Ice Age (available at amazon.com) I warned that bank regulators would start this coming economic mess by shutting down lending. I showed that in spite of this $5.0 trillion of Fed monetization, the printing of money out of thin air and handing it to Wall Street, that it would not end up in the hands of Main Street and small businesses, but it would be wasted, and that there was a better way to improve economic prosperity and wealth. I warned that the Fed's QE programs would not work. Well, they have not worked, not when you see net worth down almost 50 percent.

You want to know why housing and construction are down the johnny? Because down payment requirements are too onerous. Households have no source of cash for current higher-than-what-was required-in-the-past down payment requirements. With household net worth down 43 percent in five years, just where are households supposed to get the cash to put 25 or 30 percent down payments on a home residence purchase? The value of their current homes is down 25 percent or more over the past five years. Necessities inflation is through the roof and completely unreported by phony Central Planner economic reports. It costs a lot more to live. So, where is the cash going to come from? Instead of helping households purchase housing by reducing down payment requirements, bank regulators have forced banks to increase down payment requirements at precisely the wrong time. This affects housing related businesses and jobs, retarding U.S. economic growth.

About every mistake that can be made by the Central Planners is now underway. This economy is headed for a tanking. These fundamental economic policy mistakes are the fulfillment of the Jaws of Death pattern's warning.

There will be a time lag here, but the steps are in motion. Build up your cash folks. Get out of debt folks. Reread my book. A crash is coming. Maybe later this year, maybe next, but it is coming.

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"Jesus said to them, "I am the bread of life; he who comes to Me shall not hunger, and he who believes in Me shall never thirst. For I have come down from heaven,

For this is the will of My Father, that everyone who beholds the Son and believes in Him, may have eternal life; and I Myself will raise him up on the last day."

John 6: 35, 38, 40