How To Weather The Coming Financial Storm

PART II

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Are we adequately prepared to survive the next financial storm? This is the question all prudent financial managers everywhere are asking themselves. Quite frankly, this concern has no simple answers. The reason for this is because the reality of the world in which we live varies considerably from one person to the next and covers one end of the thinking spectrum to the other. For example some would ask, *"What storm?"*—while others intuitively know a huge financial tsunami is on its way and fear the worst for our country and the world. This is the difficulty we face in laying out steps to a sound financial survival strategy. And this is the subject of this article—part two and conclusion to last month's ***LMR*** commentary on, *How To Weather the Coming Financial Storm.*

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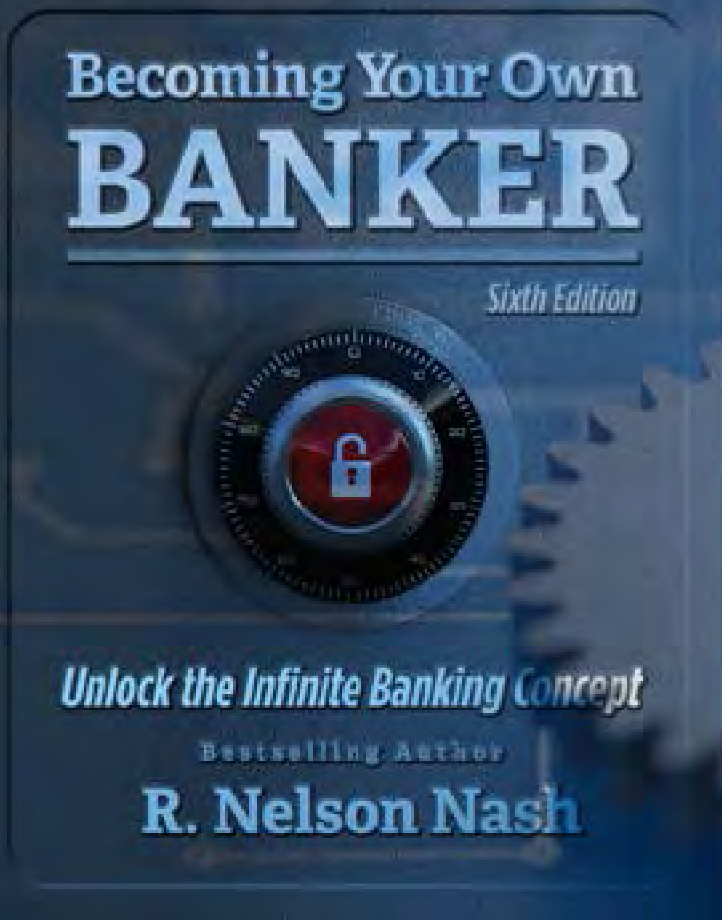
Recapping Part I of Our Narrative

In the previous outline we made clear that ultimately there will not be much we can do to appeal to those who do not even see some kind of financial crisis at hand. There are always individuals among us who for one reason or another remain unaware and fail to take the necessary precautionary measures to protect themselves. Caught up in the euphoria of the economic boom they are



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blinded to what lies ahead. Once the storm arrives and they are devastated by it, they are shocked and can't believe they never saw it coming. Unfortunately, this is the sad truth. Every historical boom and bust of the past has evidence of substantial collateral damage from the naïve public. But for the sensible financial manager of a business or household who is paying close attention to the ominous economic clouds that are forming, we offer a sound financial strategy that may well prove to be exactly what is needed.

The ideal blueprint to survive the next financial storm is Nelson Nash's *Infinite Banking Concept.* Since liquidity and control are fast becoming preeminent in this kind of economic environment, Nash's approach, when anchored with several months' worth of basic expenses denominated in gold, provides the best-balanced means of passage through the worst kind of storm, including a temporary re-set of our currency, if it should come to that.

Today's economic forecasters are not being shy in telling us that the next bust will be much more punishing to our financial well being than in times past. And so it is for this reason that our very first suggestion for determining the potential impact of these

storms on our own personal economy was to catalogue them as A, B or C in terms of their severity. For example, a type A Storm, we explained, was a stock and real estate market crash similar to what we experienced in 2008.

Most of us can recall what the 2008 financial storm was like and more or less know what to expect when it happens again this next time around. We also know that many of us survived that particular type A storm by either having adequate cash flow or by not being invested in either of those two markets. Others of us were not so lucky. Since we all remember that there were bank runs in this last debacle, we should all be acting promptly to remove our cash or other dollar denominated assets from inside institutions vulnerable to systemic risk, such as commercial banks and Wall-Street entities. This is especially more urgent now with the "bail-in" ramifications of the Dodd-Frank Act[1] when a designated "systemically important financial institution" (SIFI)[2] experiences a severe bank run.

A type B or C storm we pointed out were much more grievous. And if based on our worldview we envision these types of storms on the horizon, more the reason to start moving toward safety and liquidity now. Naturally, our choice should be a non-bank mutual or mutual holding life insurance company, as

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Nelson Nash explains in his work.

Finally, in Part I of this paper we stressed that the best cash flow guide for an unstable economic environment such as this is John Exter's Inverted Pyramid.[3] In this picture model we get a visual organization of asset classes in terms of risk and size, making it ideal for planning our money moves much more carefully and expeditiously. In a collapsing economy the direction of our money moves should be toward the base of the pyramid. It's easy to see why. There is where we see cash and gold.

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Of course this article and the protection steps outlined only make sense if you feel our economic environment is indeed extremely turbulent and uncertain. These are bold money moves we are discussing, not your typical estate or investment plans offered by your average financial advisor. We must remember this as we keep reading. At the same time, these money moves are quite simple, straightforward, and conservative. With that in mind I will now turn our attention to the insurance sector and explain some of the newer developments of the Dodd-Frank Act relative to insurance companies and why it is still prudent to move our money there.

There Is No Such Thing As A Fail-Safe Financial Bunker

Before going any further it makes sense to be clear on this one point. Nearly everyone agrees that gold has historically represented sound money. It is readily acknowledged that when all financial institutions and all fiat currency fail, gold still represents the bedrock money. This is exactly why it appears at the base of Exter's Inverted Pyramid. Of course world economic events have to get pretty bad for that sort of thing to actually happen. But ironically many financial experts actually think that this is exactly where we are all heading, and there is plenty of proof that makes it difficult to repudiate their be-

liefs. Consequently we need a strategy that focuses not only on the severity of that kind of impact, but also on its duration. We must be able to weather the storm no matter how bad it gets. It is for this reason that we include in our financial survival strategy several months of basic household expenses in gold or silver. Robert Murphy's article in this month's ***LMR*** issue is excellent reading on this subject and lays out the exact *emergency* money strategy step by step.

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And yet gold is not totally insulated from government tyranny and confiscation. "Executive Order 6102"[4] on April 5, 1933 criminalized the possession of monetary gold by any individual, partnership, association, or corporation. In other words, gold is not completely bulletproof. When we say owning it today as a form of *emergency money,* not as an investment, we mean for you to take physical possession of it so that you have access to it in the event of an "emergency" declared from the White House. For the remainder of your fiat money, the best place to warehouse it is inside a mutual life insurance company where the policyholders are also the owners of the mutual, and then practice *privatized banking* with it.

Life Insurance Companies Are Not Banks Or Wall Street

In the same way that gold is not completely impenetrable by severe outside economic forces, including severe government interventions, commercial banks and investment Wall Street firms are by far the weakest link to the interconnectedness of our financial system. But now central bankers speculate that the life insurance sector also has its own Achilles heel. After all, life insurance companies are financial institutions and like most financial institutions, they play a major role in sustaining our economy thereby making it interconnected to many other financial sectors. Just to give you an idea of how important a foundation it is to our overall financial system, consider that life insurers make up a large segment of the institutional investor space and play an important role in fixed income markets, especially as major providers of long-term funding to banks and other sectors. The industry as a whole with over one thousand carriers channels a huge volume of savings into a wide range of financial markets, with asset holdings on the same order of magnitude as those of mutual funds,

which are larger than those of hedge funds and sovereign wealth funds. Consequently the current low interest rate environment has cast a spotlight on life insurance companies to reveal the possible consequences of their investment strategies and portfolio allocations that may have negative financial market implications.

However, if there is only one important take away point from this entire message it would be this: Life insurance carriers are vastly different from other money intermediaries, especially commercial banks and investment firms. These differences include structure, investment allocation, management, accounting, and statutory oversight to name just a few. Unlike most financial institutions, which are generally regulated by the federal government, state commissioners regulate the insurance sector. What makes this difference so critically important is that the federal government specifically watches over and extends protection to systemic risk issues so endemic to the commercial banking sector while state commissioners, who oversee companies with virtually no systemic risk concern, are primarily preoccupied with protecting the individual policy owner. Now that's the kind of difference we all like.

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Peter J. Wallison, past general council to the U.S. Treasury Department and White House council to President Ronald Regan makes this important distinction between banks and life insurance companies. "While there have in fact been liquidity runs on life insurance companies, no historical quantitative or qualitative evidence exists in the record which supports a run of the scale and speed posited [by federal authorities], or to support a rapidly spreading sector-wide run. The 2008 financial crisis was driven by the losses suffered by commercial banks and investment banks that were reliant on short term funding to carry long-term assets. When those assets—mostly mortgages and mortgage-backed securities—declined in value, the firms suffered substantial losses in paying off their short-term liabilities as these came due."[5]

On the other hand life insurance carriers do just the opposite. They are a liability driven business that relies on long-term funding which it matches with its long-term assets. If those assets should decline in value there is no particular financial pressure on the company because the assets are supported by long-term debt. Although it's true that a policyholder's fast exit strategy in a crisis is the policy surrender, without this financial pressure on the company, there are likely to be few, if any, policyholder surrenders (runs).

The ***LMR*** archives have numerous articles written specifically to address this one point and it is highly recommended that ***LMR*** readers review these reports. And since over 70% of a life carrier's portfolio of assets is made up of bonds, the very next rung on the Exter Pyramid, Robert's article in this ***LMR*** issue is the ideal reading companion to this particular section of this article.

Should We Fear The Dodd-Frank Act?

If you hold substantial amounts of money inside commercial banks, especially if that bank is large, there are legitimate reasons to be concerned about the Dodd-Frank Act. For a comprehensive review of this law please read my May 2014 ***LMR*** article, "Bank Deposits Are Risky—Now, More Than Ever!"

According to a recent study by the Inter-

national Monetary Fund, May 2014, entitled *Bank Size and Systemic Risk,* several important factors are highlighted pertaining to large banks. "Large banks tend to have lower capital, less-stable funding, more market-based activities (those outside traditional bank lending) and be more organizationally complex than small banks. This suggests that large banks may have a distinct, possibly more fragile, business model. Failures of large banks tend to be more disruptive to the financial system than failures of small banks. Banks may operate at a size too large from a social welfare perspective due to 'too-big-to-fail' subsidies and corporate governance shortcomings. However, the potential for economies of scale in large banks cannot be dismissed. As a result, 'optimal' bank size is uncertain."[6]

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On the other hand, the larger an insurer becomes the less likely it is to encounter financial distress or failure. "The business model of insurance is based upon the assumption of a large number of ideally uncorrelated risks from policyholders to build up and maintain a well-diversified portfolio. In practice, this means that with an increasing portfolio there is less opportunity for unexpected results and a lower probability of very large losses in relation to the entire portfolio."[7]

Obviously, the emphasis placed for systemic risk issues with regards to banks is size, market based activities, and complexity of organization. What we are mostly concerned with here, however, is not so much the banks,

but more importantly the relationship of the life insurance companies to the Dodd-Frank Act. The Financial Stability Oversight Council (FSOC), established by the Dodd-Frank Act has extraordinary authority to designate financial firms as systemically important financial institutions (SIFIs). "The Dodd-Frank Act itself has determined that a bank holding company with more than $50 billion in assets should automatically be considered and regulated as a SIFI."[8] Firms so designated are then turned over to the Federal Reserve for stringent regulation. However, neither such size dollar threshold had been assigned, nor such action taken on insurance companies by the FSOC until the

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Financial Stability Board (FSB), an agency empowered by the G20 leaders to reform the international financial system, designated three U.S. insurers—*AIG, Prudential,* and *Met-Life* as SIFIs. Apparently, without a comprehensive analysis of these insurance companies to qualify them as SIFIs other than size, the FSOC just followed the FSB's lead. Not surprisingly, Met-Life has sued (June 16, 2015), seeking to overturn its "too-big-fail" designation. "The filing comes on the heels of a federal judge's ruling that the government went beyond its authority in demanding an equity stake while bailing out American International Group (AIG)."[9] A federal judge will hear Met-Life's case this fall. We will need to watch this case closely as it develops.

At the heart of the Prudential and Met-Life cases is the "Collin Amendment," a requirement of Congress for the Fed to establish minimum risk-based capital requirements for commercial banks, investment banks, and non-bank financial institutions that have been designated as SIFIs. "Although the Fed officials have said that they intend to 'tailor' these requirements somehow for insurers, they haven't indicated how this would be done. This is a serious conceptual problem. The fed is apparently having a very difficult time trying to figure out how to

pervisors."[10]

Prudential, AIG, and Met-Life were designated as SIFIs based solely on size. To put this in perspective, Prudential, a stock company and the second largest U.S. insurer, has $900 billion in assets so it is very large and is an international player. Met-Life, also a stock company, has $919 billion. By comparison, the largest mutual life insurance company in the U.S. is New York Life with $514 billion in assets, North Western Mutual has $229B, and Mass Mutual has $195B. Only 26 out of 1,000 life insurance companies in operation have assets over $50 billion. Most mutual and mutual holding companies are smaller than $50B and do not fall under the Dodd-Frank Act at all or have the potential to be regulated by the federal government in the future.

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comply with what seems a clear congressional directive. There is no assurance that the Fed has, or can develop, with any reasonable period of time, sufficient competence in insurance accounting and regulation to carry out the role of an insurance regulator that are more stringent than the regulations normally imposed on insurers by their state su-

Conclusion

While there may be many who seem to think that the economy really is improving, the well advised are thinking otherwise. In fact many now strongly believe that a financial tempest of massive proportions is heading our way. The steps for surviving such a storm have been laid out and explained in these two brief articles. Now you have the critical steps at hand.

One other thing. Please forget the impractical idea of trying to set up some type of foreign bank account to safeguard your fiat money. That no longer works. The Foreign Account Tax Compliance Act became law in March 2010 and closed off that option. What we're recommending here is quite harmless and traditional. There is nothing complex or illegal about it— hey, we're simply buying life insurance!

If you are ready to make your move I would recommend that you contact an Authorized IBC Practitioner in your area for individualized assistance. These men and women are financial professionals who have graduated from our IBC Practitioner Program. They understand these important matters and can assist you in implementing a specially designed dividend paying whole life policy with an appropriate highly rated mutual or mutual holding company life carrier. The most current list of them can be found at

www.InfiniteBanking.org/Finder.

Gold and silver purchases can be made easily and conveniently online from many reputable sources. Remember—physically possess your coins!

So there you have it. It's time to move away from uncertainty and to move toward safety, liquidity, and control. The sooner you do it the better.

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