

Boot in the Face

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In Orwell's best seller, "1984," O'Brien says to Winston, "If you want a picture of the future, imagine a boot stamping on a human face – forever." Just like Orwell warned against, the United States government has grown exponentially the past 200 years. Amity Shlaes highlights the guns vs. butter phenomenon in her book, "Great Society: A New History," contrasting government spending on national defense and social programs. While social spending is now nearly seven times¹ that of defense spending, both categories added together should be a warning sign to Democrats and Republicans alike.

Government spending is currently 27% of GDP compared with sub-8% in the 1930's². This rapid expansion in size and scope of the federal government has made nearly every aspect of American life political. Education, religion, healthcare, finance, and even groceries have become politically contentious. As government has expanded, so have corporations. Big government works hand in glove with big companies to write laws that protect monopolistic interests, thereby stamping on the face of small business. In nearly every industry, large corporations write regulation that is self-interested and anti-competitive.

The result is higher prices, less choice, and worse products for consumers. Look to the CCP, USSR, Cuba, or nearly every other place communism and socialism have been tried. Centralized power always leads to scarcity, while capitalism and free markets always lead to abundance. We experienced a small taste of failed centralized planning during the pandemic. While COVID was a tough disease and we all know someone affected by it, in our opinion, the global government response was an overreaction. Supply chains which are incredibly complex and sophisticated were shut down overnight sending a shock wave through the system. Worse yet, we paid millions of people more to stay home than to work, a trend that hasn't yet been corrected. Recent employment data show nearly 4 million people still out of the workforce that should have re-entered by now. This a core contributor to wage inflation and won't be fixed by interest rate hikes.

In short, government policy needs to change, and soon. We currently spend \$1.64 trillion on the Department of Health and Human Services, \$1.28 trillion on Social Security, \$1.16 trillion on the Department of the Treasury, \$727 billion on military defense, \$639 billion on the Department of Education, and the list goes on³. While we still have an extraordinary economic engine, we are quickly burdening our children, grandchildren, and great-grandchildren with excessive amounts of debt, now financed at 5% or higher interest rates. Servicing the U.S. federal debt costs more than ever before with interest payments skyrocketing to \$928 billion in the first quarter of 2023, up 83% since 2018⁴.

So, who's to blame? A great deal of the blame belongs with politicians. Both Democrats and Republicans have spent sickening amounts of money without raising taxes or selling bonds. George W. Bush, on the right of the political aisle, presided over an 80% increase in federal spending compared with President Clinton. Similarly, President Obama added nearly \$5 trillion to the federal deficit, nearly double initial economic projections. President Trump was no different, adding nearly \$8 trillion to the federal deficit. President Biden, another continuation of the boot stomp, has already spent \$4.8 trillion in money we don't have⁵.

While all this spending is bad news, the true culprit who allowed it to happen is the Federal Reserve, and in our view, not by accident. For hundreds of years, famous banking families have pushed for centralized monetary control not backed by gold. More dollars in the economy means less buying power for us, but more interest-bearing deposits for them. While smaller banks are struggling right now, large banks are literally printing cash essentially risk free thanks to the Federal Reserve. Rather than acting as a check against terrible fiscal policy, the Fed has walked lockstep with Republican and Democrat regimes to print money, avoiding raising taxes or cutting social and military spending. As investors, our mandate is clear – equities provide the only true and lasting hedge against inflation in the long run. Companies raise prices ultimately protecting their margins. If we pay the right price for their stocks, we'll see our wealth, at a minimum, keep pace with boot stamping over time.

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Sources

¹Guns and Butter 2.0, BlackRock Investment Management, January 25, 2023

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²Federal government current expenditures, St. Louis Fed data, April 27, 2023

³U.S. government spending, Treasury.gov, March, 2023

<https://fiscaldata.treasury.gov/americas-finance-guide/federal-spending/>

⁴Federal government current expenditures-interest payments, St. Louis Fed data, April 27, 2023

⁵Biden Admin Has Approved \$4.8 Trillion of New Borrowing, Committee for a Responsible Federal Budget, September 13, 2023

<https://www.crfb.org/blogs/biden-administration-has-approved-48-trillion-new-borrowing>

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