Obama’s Coming Taxes On The Poor

Throughout the 2008 campaign and during the first two years of his putative presidency Barack Hussein Obama Soetoro Obama has often and steadfastly repeated that he will not raise taxes on American families that earn less than $250,000 per year. This promise continues the routine class warfare strategy of modern Democrats, pitting one group of voters against another in order to win elections without regard for the general welfare. Coming from someone whose training was in community activism, Obama’s tactic was certainly not surprising. You do not excite crowds or gain votes by saying, *“Look within yourselves to see where you may have gone wrong in your life, overcome your obstacles and work harder to achieve success.”* You rally the crowds to action by telling them, *“Your problems are all the fault of someone else, and I will help you go after those bastards!”* (While the “have-nots” marched off to demonstrate against the “haves” and were arrested for disorderly conduct, Obama remained behind drinking his café parfait or imported beer and having a salad with arugula he bought from Whole Foods, followed by a Marlboro Extra Light.)

Helping the poor is best achieved by removing the obstacles blocking their success. Lowering taxes and reducing regulations to create jobs and holding teachers accountable to improve education immediately come to mind. The poor are not helped by punishing the wealthy. Regrettably, the community organizer’s goal is not to help the poor; it is to boost his political popularity. The class warfare candidate’s goal is to get elected and maintain power, not reduce poverty—because a reduction in poverty is a reduction in the number of voters to whom the “us against them” appeal succeeds.

January 1, 2011 is almost upon us and, depending on the actions of Congress and Obama, the American people may be facing the largest tax increase in U.S. history—if all of the Bush tax cuts are allowed to expire. What is more likely is that those earning less than $250,000 will be spared direct increases in their income taxes, while all of the other tax cuts will be allowed to expire. That means tax increases not only on the income of some people—the people who already pay the largest share of taxes—it also means increases in capital gains taxes, dividends taxes, and estate taxes. More than a few small businesses and family farms will have to be sold when their owners die, in order that their heirs can pay the government’s death taxes. That alone will cost tens of thousands of jobs. And tens of thousands of retirees will see their incomes reduced because they will have to pay increased capital gains and dividends taxes.

These tax increases are of no concern to the legions of Obama fans. *They will have been spared, thanks to him!* Before they get too complacent, however, they should realize that they are about to be hit with the worst form of all the government’s taxes: the hidden tax of inflation.

All Americans have had to pay the inflation tax throughout their lives. That hidden tax has reduced the value of the U.S. dollar by more than 95 percent since the Federal Reserve was created by President Woodrow Wilson on December 23, 1913. That hidden tax is the main reason why a house that used to cost $25,000 now costs $250,000, and

why an automobile now costs not $2,500 but $25,000. It was not the greed of automakers that has driven up the cost of a new car to astounding levels over the last few decades; it was primarily inflation (with a good amount of unjustifiable labor union demands and management incompetence thrown in for good measure).

Contrary to popular belief, inflation does *not* mean rising prices. Rising prices are *caused by* inflation. The word "inflation" refers to the practice of "inflating." Just as one inflates a balloon, the government (via the Federal Reserve) inflates the supply of money in the economy. That introduction of additional money into the private economy ultimately causes prices to rise, because the amount of goods and services has remained essentially the same. *There is more money chasing the same amount of goods and services*.

To use a simple example, if a farmer has 100 apples to sell and each of 100 customers has $1.00 which he is willing to spend on an apple, the apples would sell for $1.00 each. If each person was given another dollar, the price of apples will go up. The first few customers might decide to buy two apples with their $2. But the farmer, seeing the long line of customers with $2—and a supply of apples that is declining because customers are now buying two rather than one—decides to raise the price of an apple to $1.50. As the line of customers continues unabated, the farmer again raises the price, little by little, and it eventually may approach (or even reach or exceed) $2.00. The customers at the end of the line will, however, find themselves out of luck—because the farmer will run out of apples as a result of some customers having bought two.

To use a more complicated example, assume that the Obama administration—in an effort to "eradicate poverty forever"—decides to print money and send every American citizen a check for $1 million. Voila! Everyone is a millionaire! No one is poor!

Most Americans would see the stupidity of such a plan, of course. The luckiest Americans will be those who receive their checks first, because they will spend some of their new wealth quickly—before prices have a chance to rise. And prices will indeed rise. The Cadillac dealer, seeing the throng of people eager to buy a new Escalade SUV, will raise the vehicle's price. *Why would he not?* After all, he may have only 50 SUVs on the lot and 500 customers who want them. Before the day is over, the vehicle price will have doubled, or tripled—or more. His lot will have been emptied, and the dealer will telephone the General Motors factory to order a new supply of Escalades. Yet no one will pick up the phone to answer his call. Why? Because the employees are now all millionaires and have not bothered to show up for work.

Eventually, prices on products and services across the country will rise dramatically to absorb the cash of all the new millionaires. Eventually, people will reluctantly return to work—as soon as they realize that their $1 million in the bank will not last long, with the price of a loaf of bread having risen to $500.

Who will be the winners in such a scenario? Those who receive the million dollars and spend the money first, before prices have had a chance to rise. Who will the losers be? Those who are last in line to buy goods and services, because they will face the highest

prices. Other losers will be those who are prohibited by law from raising prices. For example, landlords in rent-control cities like New York will not be able to raise rents, yet they will see their operating expenses jump sky high. After everything returns to "normal," things will be pretty much the same as they were before—except that all prices will be higher. People will return to their jobs, where they will be given wage increases. But those higher wages will be offset by the higher cost of goods and services. A few people will have become better off through the money-printing scheme, but most will be worse off.

It should be obvious that someone who used to earn $25,000 per year and who today earns $50,000 per year is *not necessarily twice as well off*. If prices have more than doubled during the same period, his salary doubled he is actually *worse off*. If a new car cost $2,500 when he earned $10,000 per year, that car's "price" was actually one-fourth of his annual income. If a new car today costs $25,000, his income would have to be $100,000 for the ratio of car to income to be the same.

Of course, the incomes of some people rise faster than those of others. Someone who is unemployed obviously does not receive a wage increase—but the prices have gone up for him just as they have for everyone else. The employee covered by a union contract that provides a cost-of-living wage increase is most certainly better off than an employee whose employer is not able to raise prices enough to provide for those wage increases. The person with a "regular" job will likely suffer more than a government employee, who is more likely to see greater wage increases—because his employer is able to "print money."

All of the above is nothing more than common sense, but some people simply "don't get it." They are too easily swayed by the belief that having more money necessarily makes one wealthier under all circumstances. They may benefit from this author's book, *What You Don't Know About Economics Can Hurt You*. You can order it at:

http://www.amazon.com/exec/obidos/search-handle-url?_encoding=UTF8&search-type=ss&index=books&field-author=Don%20Fredrick)

Regardless of whether one "gets it," *all* Americans are about to be hit by the largest "hidden" tax increase in the nation's history: the coming inflation caused by the Obama administration and the Federal Reserve. In the last two years the federal government has incurred deficits of about $2.8 trillion. Although some of the nation's debt is being financed by borrowing from China (or anyone else who contributes to the scheme by purchasing Treasury Bills or Savings Bonds), much is being financed by the Federal Reserve. However, the Federal Reserve does not actually "have" the money to buy the debt. It simply prints it. More accurately, it does nothing more than make bookkeeping entries. The Federal Government gets the cash to cover its spending by selling Treasury Bills to the Federal Reserve, which "creates" the money out of thin air. The Federal Reserve has also bought hundreds of billions of dollars of "toxic assets"—mostly mortgages—from banks. It "paid" for them with mere bookkeeping entries, and in the process introduced enormous amounts of new cash into the banking system. None of this

is meant to excuse the administrations of any prior presidents or Federal Reserve Board chairmen. Bush, Clinton, and their predecessors deserve blame as well, and Alan Greenspan should be tarred and feathered. But Obama and current chairman Ben Bernanke have broken all records for incompetence and money-printing, and they will easily warrant all the scorn and invectives directed at them after the voters understand what the dynamic duo has done to destroy their economic lives.

Even if the voters woke up today, however, it is too late. The hyperinflation has already been "baked into the pie" because the money has already been created. The only reason prices have not yet risen dramatically is that the banks are not yet lending that money to businesses or consumers—because they consider the current economy too risky an environment. Instead, the banks are sitting on some of that money and lending it to the federal government through the purchase of Treasury Bills. The banks would rather earn low interest from the government than risk the money on higher-interest loans to businesses and consumers that may turn sour. Further, many corporations have considerable cash on hand that they are temporarily holding back. They are reluctant to spend it on business expansion and hiring until the economy shows some signs of reliable improvement. The administration has been begging the banks to lend and the corporations to spend their money, essentially pleading with them to take substantial risks. But Obama can hardly force them to lend and spend, as much as he would like to—and when they finally do he may wish he had not asked.

At some point the U.S. economy will improve. When that happens, the banks will start to lend those enormous amounts of money to businesses and individuals, and corporations will start to spend their cash reserves. When that happens, a *flood* of currency will enter the private economy. The result will be price increases that *cannot be avoided*.

Making matters worse is the standard manner in which banks operate. They generally carry reserves of only about 10 percent of their deposits. That is, for every dollar deposited in the bank, the bank has loaned $10.00. Therefore, each dollar in a "fractional reserve banking" system has a "multiplier effect," thus greatly expanding the supply of money in the economy. (If you have trouble understanding the concept, recall the scene in the James Stewart movie, *It's a Wonderful Life*, in which he tells his bank customers they cannot all withdraw their deposits at the same time because their money has been loaned to their neighbors for their homes and businesses.) Because banks have been reluctant to lend, their reserves are greater than is typical. When they start to lend that money, the multiplier effect will further increase the amount of money in the economy.

How bad will the coming price increases be? No one can possibly know. Granted, the situation will not be as bad as the government sending every American a check for $1 million because the amounts are certainly not that great. *Nevertheless, the amounts are enormous.* There is probably upwards of $2–$3 trillion (or perhaps even more) waiting to be released into the economy. That amount will then be expanded by the multiplier effect at the banks.

Assume that the money supply will be expanded by $3 trillion. (Feel free to pick your own number if you like; the difference is only in degree, not effect.) The Gross Domestic Product of the United States is approximately $14.5 trillion. That is, the economy creates $14.5 trillion in goods and services each year. Now, add $3 trillion to the money supply. That means $17.5 trillion will be chasing $14.5 trillion in goods and services. That translates into an inflation rate of 20 percent, but that $3 trillion is also *expanded* through the bank-lending multiplier effect. What happens if $20 trillion chases $14.5 trillion in goods and services? Or $25 trillion? Or $30 trillion? The price increases will be greater than most Americans have ever *imagined*, let alone *experienced*.

Will everyone be losers? No, there will be some winners. The winners will be those who see the hyperinflation coming. That includes some Wall Street investors and many people in government. It includes anyone who buys gold, silver, and other commodities which are likely to increase dramatically in price. Even if you can afford to invest only $25 per week, you can buy an American Eagle silver dollar every week. If the price of silver skyrockets as a result of inflation, you will be ahead of the game. No, you will not be a millionaire, but you will have more than the person who placed more trust in the paper currency in his wallet than in silver.

The average American will suffer tremendously under a hyperinflation scenario. Others will suffer slightly less, such as union workers with contracts that include cost-of-living increases. Most employees do not have such protections, however, and will see prices rising much faster than their incomes.

Who will suffer the most? The unemployed, the minimum wage workers, the poor. That includes the people who voted for Obama in the belief that he would never raise their taxes.

Yet Obama only promised not to raise income taxes on those who earn less than $250,000 per year. *He never promised not to raise the hidden tax of inflation.*

Obama only promised not to raise your taxes. He did not promise not to raise the price of apples…

Don’t say I didn’t warn anyone.

Don Fredrick
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