



Moral Hazards

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“The consequences of an act affect the probability of its occurring again.” – B.F. Skinner

Seriously?! Everyone gets a trophy? Even if they didn't win, much less try?! Ok, before I get up on my high-horse again, let's discuss the definition of “moral hazard”. Simply put, it's a situation where someone takes on risk knowing that his/her potential loss will be accepted by another. Thus, that person (or company) may take an otherwise unacceptable risk knowing there will be slim to no consequences. Why, in the midst of high inflation and looming recession, do I bring up the topic of moral hazard? Because I am a simple numbers guy that strongly believes there are consequences to *everything*, and recession is a painful yet healthy and natural part of every business cycle – and some well-intended actions can create moral hazard.

For instance, remember the great economic experiment called modern monetary theory (“MMT”), where a government could print as much money as it likes to stimulate growth without concern for deficit spending and potential ballooning inflation? Well, I think we can put this one to bed as we are in the midst of massive inflationary times (persistent or not will be answered only in hindsight in a year or two). To be fair, MMT proponents suggest that supply issues are the real culprit to MMT's apparent failure, but I'd be suspect if anyone said, “hey, give it another chance, let's dispense even more money!” The moral hazard with MMT was that every bit of historical evidence and intuition said that inflation would be a natural consequence of too much money supply, and now we are paying the price (no pun intended) for taking that risk.

I thought we had learned this lesson, especially after the government threw a massive lifeline to the financial industry during the Great Recession. Does anyone even remember the billions of dollars the federal government gave to institutions who played games with other people's money? Sure, we were in the midst of a financial meltdown, and Lehman Brothers was not spared, but, in my humble opinion, we are only kidding ourselves when we think the so-called titans of wall street actually learned anything from that debacle, other than to get out of a bad trade before everyone else does. I believe the moral hazard from that fiasco was that all types of institutions foresaw that they could re-engage in overly risky behavior without consequential loss.

The next debacle was the covid crisis that started in early 2020. Look, I am not here to say that it wasn't an unusual and deadly situation, but we may have over-applied the financial medication. Not only did we give just about everyone and every company a handout financially, but then we kept on giving possibly beyond the point of true need – where companies big and small were, and still are, struggling to entice people to simply work! Seriously, I understand how some vulnerable people need to stay at home, due to either a health or family situation, but it seems crazy when plenty of healthy adults simply choose not to work for no other reason than they don't have to since the government is paying their bills (or telling them they don't need to)! So, by trying to prevent a recession in 2020 and 2021, the moral hazard is that the populace may be looking for a handout every time things get tough, like during a normal recession.

Maybe this explains why we now have a much greater number of cars being repossessed. One car dealer said he believes repossessions have doubled over the last two years, for both prime and subprime lenders, and most of them from cars that were bought in 2020 and 2021 rather than spread over many years. One very valid explanation may be that some consumers' incomes and cash balances were temporarily high as the pandemic response included not only cash and tax stimulus but also debt forbearance. The moral hazard of giving too much for too long may have created a situation where the banks or taxpayers get stuck with the bill for the buy-what-you-want-while-you-can mentality (which always goes against my mantra of "just because you can doesn't mean you should").

And I know this isn't going to be popular with some, but how can I not mention the moral hazard, much less massive cost to taxpayers, of cancelling student debt. Please understand I am not advocating for or against forgiveness, as each side of the debate has merit. However, I would be insincere if I did not mention the multiple moral hazards forgiveness could create (speaking of insincere – there is *never* "debt forgiveness", just someone else paying the bill). Think about the people who learn that if they simply do not pay their debts (student or otherwise) long enough that it may be paid for by someone else. Current and future students may be encouraged to take out more loans thinking they may not have to ever pay them back. Universities and colleges may be encouraged to increase fees and tuition even further knowing someone somewhere will ultimately pay them back (I'd love to see the government go after these institutions that took advantage of the situation and raised fees and tuition by much more than any normal inflationary trend in the last twenty years). And don't forget the anger of the people who have paid their bills previously!

Last but not least, let's talk about the trophy winners. Look, I get it, we all want to be inclusive and encourage others to participate. But sacrificing competition in the name of inclusiveness means you must be willing to sacrifice hard work and endurance in the face of loss as well. In my mind, you create moral hazard by not challenging people to be the best they can be regardless of the outcome, win or lose. If there is no true winner, you discourage those who might win, and demean those who might lose but try hard anyways; paraphrasing Teddy Roosevelt, the true credit goes to the person who, win or lose, tries again and again.

I hope this all doesn't come off as too preachy, but as the country song says, the road to hell is paved with good intentions. And as well intended as some actions may be in good times and bad, we always need to be cognizant of potential moral hazard that is created when we try to avoid consequences.

Thanks for your friendship and trust, thanks for your referrals, and have a great rest of the Summer!

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