

# QE Didn't Quite Cut It, So Now What?

Looking to the past may not help Yellen on rates.

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Oil Painting: Braulio Amado; Images: Bloomberg mages (4)

Members of the Federal Reserve Board of Governors don't usually share their differences in public. On Oct. 11 the board's vice chairman, Stanley Fischer, said in Lima that he expects a hike in the Fed's main rate "later this year," confirming what Chair Janet Yellen had said in September. Within two days, Lael Brainard and Daniel Tarullo, both on the board, said the Fed should wait because there wasn't yet any sign of inflation. That disagreement shows the dilemma Yellen faces: Raise rates soon and risk smothering a tepid recovery, or wait until next year and risk igniting inflation.

Congress gave the Fed two jobs: Keep inflation predictable and unemployment low. In the past, as unemployment went down, inflation went up. Fed hawks argue that, with unemployment at 5.2 percent, inflation is on its way. Doves say that relationship isn't what it used to be. There's a third argument: We don't really know how well the last seven years of Fed policy have worked. And if the central bank can't be sure of what happened in the past, it will find it hard to decide on the future.

The Fed can't tell banks how to lend. Instead, it relies on something measurable that it can control: the rate of interest. Since 2008, the Fed has kept short-term rates near zero and brought long-term rates down

through “quantitative easing.” That required the central bank to buy a lot of long-term U.S. government debt. By lowering long-term rates, QE would encourage people to buy houses, and businesses to borrow for expansion.

While QE succeeded in bringing down long-term rates, lending didn't increase as much as anticipated. The Fed hit its interest rate target square on. It's hard to measure how much easing has benefited Main Street. Some economists are skeptical. “We no longer believe that QE can fix everything,” says Michala Marcussen, global head of economics at Société Générale.

“We have very good estimates of how quantitative easing affected interest rates,” says Amir Sufi, a professor at the University of Chicago Booth School of Business. “We don't know how to translate that into how it affected the real economy.” Sufi's lecture in June at the Bank for International Settlements in Basel, Switzerland, asked whether monetary policy was as effective as economists had believed. Central banks, he concluded, failed to take into account that people behave differently under the same policy. Economists call those differences in behavior “heterogeneity.”

Sufi cited two recent papers that show that when rates fell in the U.S., households with higher debt burdens—generally the poor—were more likely to spend. His own research shows that for every dollar rise in a home's value, the poorest households borrowed and spent 25¢. The richest 10 percent took out no new loans. And while Yellen's low interest rates made mortgages cheaper to refinance, that didn't necessarily mean more spending.

The same is true for credit card loans. In theory, low rates make it cheaper for banks to borrow and encourage them to increase credit limits. In a working paper for the National Bureau of Economic Research, a group of researchers looked at 8.5 million credit card accounts. They found that for every 1 percentage point reduction in what it costs banks to borrow, banks extended \$127 in credit to families with credit scores below 660. Those families spent 58¢ for every new dollar in credit.

Under the same conditions, families with credit scores above 740 got \$2,203 in extra credit. But they didn't spend a penny of it. Says Johannes Stroebel of the NYU Stern School of Business, one of the authors: “The targeting of these credit expansions is potentially to the wrong people, to the people that don't want to borrow more.”

A report prepared for the Lima meeting by the Group of Thirty, a body of central bankers, regulators, and economists, reached similar conclusions. Among developed economies, according to the report, the rich have gotten richer, their homes and investments have increased in value, and they're the least likely to spend more. “How far down do you have to get interest rates,” Sufi asks, “before you get someone like Bill Gates saying, ‘Well, now I'm going to spend my money’?”

At his Basel speech, Sufi urged central banks to change their models to account for heterogeneity. The Fed has already started. A 2015 paper by its research division looks at how the unconventional monetary policy of the past seven years has affected U.S. unemployment. The paper assumes that households differ in the way they respond to lower rates and in their view of the future, with most households planning no more than five years ahead. For those with such a short-term perspective, the Fed's success in bringing down rates on loans that mature in 10 years is irrelevant. The paper concluded, however, that loose monetary policy at its peak in early 2015 subtracted an extra 1.25 percentage points from the unemployment rate.

In 2012, Ben Bernanke, Yellen's predecessor, told economists at the annual gathering of central bankers in Jackson Hole, Wyo., that the Fed's actions had lowered long-term interest rates and improved financial conditions. "Obtaining precise estimates of the effects of these operations on the broader economy is difficult," he said. As Yellen considers her next move, that's true for her, too.

***The bottom line:** Researchers on Fed policy are discovering that rate cuts affect rich and poor consumers differently.*

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## A Wal-Mart Heir Is \$27 Billion Poorer Than Everyone Thought

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DamscoDave    tommetcalf123

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Christy Walton. Photographer: Alberto E. Rodriguez/Getty Images

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- ▶ Son Lukas Walton, now 29, inherited twice as much as Christy
- ▶ John Walton's widow was long pegged as America's richest woman

Ever since Wal-Mart heir John T. Walton died 10 years ago in a plane crash, it's been widely assumed that he passed the bulk of his vast estate to his widow, Christy.

Turns out that was very wrong.

In what's been a closely guarded family secret, Walton gave half of his then-\$17 billion estimated fortune to charitable trusts and a third to their only child, Lukas Walton, now 29, an analysis of court documents reveals. Christy got the rest.

The filings, unsealed by a Wyoming court at Bloomberg News's request, mean that Christy's fortune as previously calculated has taken a big hit -- from \$32 billion before the court records were unsealed to about \$5 billion now. She's unlikely to ever again reach her former designation as America's richest woman, which she held until last month.

But her loss is Lukas's gain. Though little-known outside of a few scattered social media posts, he becomes the 103rd-richest person in the world, with about \$11 billion -- and as much as \$25 billion if certain trusts are included, according to the Bloomberg Billionaires Index.

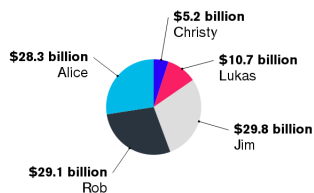
That makes the grandson of Wal-Mart founder Sam Walton \$5.5 billion richer than his 66-year-old mother. and the fourth-wealthiest member of the Walton family. His net worth is higher than the likes of

Google executive Eric Schmidt and money manager John Paulson.

The Waltons declined to comment for this article. "Lukas Walton is an entrepreneur involved in a variety of investment and philanthropic activities," Kiki McLean, a spokeswoman for the Walton family, said in an e-mail.

#### Sam Walton's \$100 Billion Wal-Mart Legacy

With a fortune of more than \$100 billion, the heirs of Wal-Mart founder Sam Walton -- siblings Jim, Rob and Alice, grandson Lukas and daughter-in-law Christy -- have one of the world's largest family fortunes.



Source: Bloomberg Billionaires Index

Bloomberg

John Walton, the second of four children of Sam and Helen Walton, left an estate that included gold bars, a catamaran and \$100 million in cash, according to the documents. Most valuable was his 20 percent interest in Walton Enterprises LLC, the family's main investment entity.

## Key Vote

As a result of that holding, Lukas may wield a key vote in the closely held entity, which together with another family trust controls a 50.2 percent stake in Wal-Mart Stores Inc. At more than \$100 billion, the Waltons -- siblings Jim, Rob and Alice, as well as Lukas and Christy -- can claim one of the world's largest family fortunes, according to the index.

"There's no other public company of this size that I am aware of where a family has such a big stake," said Brian Yarbrough, a consumer research analyst at Edward Jones in St. Louis.

Lukas has proved adept at keeping a low profile. He grew up in National City in San Diego County and Jackson, Wyoming.

"They were just one of the neighbors, just one of the very rich neighbors," said Ron Morrison, mayor of National City, who was a regular visitor to the area where the family lived from 1986 to 2005.

As a young child, Lukas was diagnosed with cancer. His mother attributes his survival to an organic food diet, according to an interview she gave to the San Diego Union-Tribune in 2008.

## Colorado College

Lukas graduated with a bachelor's degree in environmentally sustainable business from Colorado College, according to a letter from his high school. His college directory lists his graduation year as 2010 and his work history as an unspecified position at the Walton Family Foundation. He has worked for True North Venture Partners, a firm that traces its roots to his father's venture capital activities, according to local press coverage of the commencement speech he gave at his high school in 2011.

The fate of his father John's stake was unknown ever since a judge in Teton County, Wyoming, sealed the estate in September 2005 at the request of the family. Walton had died three months before, at age 58, when the ultra-light aircraft he was piloting crashed shortly after taking off from Jackson Hole Airport.

The documents reveal the painstaking seven-year-long legal undertaking to distribute the estate and underline the family's extensive use of trust structures to minimize the amount of tax they pay.

## Voting Right

His father's will directed that Lukas be given the right to vote the estate's general and limited partner units in Walton Enterprises. That could make him one of the first of the family's third generation to be a voting shareholder in the controlling entity, if he decides to exercise his voting power.

That structure is in keeping with Sam Walton's vision to minimize estate taxes while keeping the family's control of the company unified. In 1953, he put his stock in a trust that gave each of his children a 20 percent stake in the business, leaving the remainder for himself and his wife.

"The principle behind this is simple: the best way to reduce paying estate taxes is to give your assets away before they appreciate," Sam Walton explained in his autobiography.

When John married Christy Tallant, he had a net worth of about \$195 million, according to a 1982 premarital agreement that was unsealed this month by the Wyoming court.

## Tax Avoidance

John Walton's own bequest appeared to take advantage of several tools to reduce taxes on the estate. The estate was appraised at \$6.6 billion, according to the documents.

Yet, the Wal-Mart shares controlled by John Walton's estate would have had a market value of \$17 billion at the time of his death if he hadn't given any of his holdings away during his lifetime, according to data compiled by Bloomberg. That discount in part reflects the holding structure the family has established for

their shares, according to John Anzivino, head of the estates and trust division at Miami-based accountants Kaufman Rossin.

“The LLC may have all kinds of restrictions, such as profit allocations and lack of control, which reduce its value from the market value of the stock itself,” he said. In Bloomberg’s analysis, the net worth of Christy and Lukas is calculated using the retailer’s stock price.

## Appraised Value

This structure saw the estate estimate its tax liability to be about \$1.4 billion, only 21 percent of the appraised value. The top federal estate tax rate was 47 percent in 2005, according to Anzivino. This is the rate on the portion passing to the child subject to estate tax in excess of the exemption of \$1.5 million. Christy, as the surviving spouse, gets her share estate tax-free and the gift to the charitable trusts are estate tax-free.

John Walton’s will split the estate into two parts.

Half of the estate was placed into tax-friendly vehicles known as charitable lead annuity trusts, or CLATs, of which Lukas is the only beneficiary.

For the other half, Walton directed that two-thirds was to be held in trust for Lukas. The remainder went to his widow.

The charitable trusts make annual non-taxable payments under IRS guidelines to the Walton Family Foundation charitable arm until 2036. If its investments outperform certain benchmarks, whatever is left at the end goes to Lukas without any tax bill.

## Future Performance

In Bloomberg’s calculation, Lukas isn’t credited with the portion of the estate held by the charitable trusts. If he were, his net worth would be as high as \$25 billion, according to the [Bloomberg Billionaires Index](#).

Depending on future performance, Lukas may not receive anything from these CLATs, according to an adviser for the family who asked not to be named as the details are private. It was John Walton’s intent to leave half his estate to charity, the adviser said.

Currently the trusts are accumulating assets faster than they’re giving them away, according to an analysis by Bloomberg based on the fair market value of these trusts as reported in annual IRS filings. That suggests the underlying assets could ultimately pass to Lukas in 21 years.

## Christy's Share

Christy's share of her husband's estate -- about 17 percent, according to the unsealed will -- includes 500,000 Wal-Mart shares, personal effects, interest in various ranches and other sundries. A philanthropist, she donated the Victorian house in National City, California, where she had lived with John and Lukas, to charity in 2006.

"The Waltons were always very good at being very philanthropic to youth programs, but they always did it anonymously," National City's Morrison said.

The documents unsealed by the court reinforce how close the family remains in business, more than two decades after Sam Walton's death. They show loans to the estate from Sam's three surviving children that enabled it to meet its obligations and prevent any loss of control at the family retailer.

It's a setup not likely to be lost upon the youngest Wal-Mart billionaire. If Lukas is ever tempted to break the tradition of family rule, his grandfather left some stern advice for his offspring.

"If you start any of that foolishness, I'll come back and haunt you," Sam Walton warned in his book. "So don't even think about it."

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