Northwood University's
Monthly Economic Outlook

January 2012

Introduction

The U.S. economy shows signs of hope in early 2012 with 4th quarter 2011 GDP coming in at an impressive percentage growth rate. Current economic data points to confusing economic activity and is becoming difficult to predict which direction the economy will tilt in the coming months. The Bureau of Economic Analysis' most recent release announced its first estimate of U.S. GDP for the 4th quarter of 2011 to be 2.8 percent growth. The BEA's estimation for Q4 GDP was strong given that the final estimate the 3rd quarter GDP showed only 1.8 percent growth. This follows a weak 2nd Quarter GDP which settled at a lowly growth rate of just 1.3 percent. While inflation slid slightly in December, it still remains above 3 percent as it has since April.

Key December/January Data

Positive Signs

U.S. productivity remains among the highest in the world while U.S. non-financial corporations' cash reserves remain at nearly $2 trillion. The December Conference Board Global Leading Economic Indicators Report shows the United States increased .4 percent while Europe increased .1 percent and China increased .7 percent. The U.S. savings rate settled at 4.0 percent in December, compared to 3.5 percent in November. Despite this month-to-month increase the December 2011 rate is still well below the December 2010 rate of 5.2 percent. Automobile, SUV and light truck sales were up 8.1 percent in December relative to the same month in 2010. Vehicle sales finished high in the winter months. Housing starts have slid from the high summer months, but the December 2011 level was up 2.2% from November and 7.3% higher than the December 2010 level. The unemployment rate settled at 8.5 percent in December, falling below 9 percent for the second time since March 2009. Finally, consumer confidence surged in December reaching 64.5, which is a 9 point increase from November.

Negative Signs

The U.S. remains one of the highest corporate tax rate countries in the world at an average rate of 39.3 percent with U.S. companies holding more than $1.2 trillion overseas as a result. Oil, gold, and silver prices continue to remain relatively high, signaling the potential for a future inflationary period. According to the latest manufacturing sector of the ISM Report on Business, the manufacturing sector of the U.S. economy increased to 52.6 in December from 52.3 in November, but is still very close to falling below 50 which signals a recession for the manufacturing sector. The Dow Jones Industrial Average increased roughly 500 points in January, up 3% so far in 2012. Construction spending in December was down relative to both the previous month and December 2010. Durable goods orders and shipments were both down in December relative to both the previous month and December 2010. Durable goods orders and shipments were both down in November relative to October. Personal disposable income continues to trend upward and is now up 2.0 percent from the beginning of the year. However, when compared to an inflation rate which has remained north of 3 percent since April, this shows a general decrease in overall wealth.

Current Issues

The Associated Press announced January 30, 2012 "25 EU nations to sign treaty to stop over spending" while Rueters reported on the same day that 25 of the 27 EU member countries had agreed in principle to a fiscal constraint that would hopefully bring a halt to the out of control deficit spending being practiced in most countries within the EU. Only Great Britain and the Czech Republic failed to endorse the measure. An unnamed British official summarized Great Britain's opposition by stating, "To write into Law a Germatic view of how one should run an economy and that essentially makes Keynesism illegal is not something we want to do."

It has been the application and/or misapplication of Keynesian economics by politicians across the globe that has created much of the economic mess Europe and the United States finds itself in today. In 1900, U.S. government at all levels consumed just over 7% of GDP with state and local government consuming the majority of the total (5 of the 7%). Today, government at all levels consumes roughly five and a half times as much of U.S. GDP versus 1900 with the federal government consuming almost 25% of U.S. GDP in 2012. It is also important to note that in 1900 the total U.S. national debt was $2.13 billion and less than 11 percent of total U.S. GDP. Today, the national debt of the United States is greater than $15.4 trillion and is just about 100 percent of U.S. GDP.

Many in Washington today believe that the solution to America's problems is to simply raise taxes on the top 2% of personal income earners in the United States as well as increasing corporate tax rates. With the 2012 presidential elections less than ten months away, it is important that we bring fiscal sanity and objective policy to the forefront of the presidential debates. It is important that whoever occupies The White House and the hallowed halls of the U.S. Congress in 2013 understand that the United States has a spending problem as well as a global competitiveness problem. The solution to America's problems rest in not over-taxing productive individuals and corporations, rather it can be found in reducing the size and scope of government programs and government waste in general. The U.S. has the highest federal corporate income tax rate (35%) in the industrialized world and the second highest combined federal and average state corporate income tax rate (39.3%), trailing only Japan at 39.54 %. The above, coupled with the fact that the top one percent of income earners paid 40 percent of the federal personal income taxes last year, should be further validation that there is no room to raise taxes rather our focus should be clearly on spending cuts.

Conclusions

It was sound fiscal policy and monetary policy in Germany after World War II which brought Germany out of economic and political ruin. Perhaps sound fiscal policy led by Germany can save the EU today and inspire national reform here in the U.S. as well.

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