

February 2012

Introduction

The U.S. and global economy continues to send mixed messages as the month of February draws to a close. Fourth quarter U.S. GDP for 2011 has been revised upward to 3.0 percent growth with the Dow Jones Industrial Average closing above 13,000 for the first time since 2008. Yet unemployment remains above 8% and factory orders were at a four year low in January.

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 January Conference Board Global Leading Economic Indicators Report shows the United States increased .4 percent while Europe increased .1 percent and China increased 1.6 percent. The U.S. savings rate settled at 4.0 percent in January, compared to 4.0 percent in December. Despite the maintenance of savings in January 2012, the savings rate is still well below the January 2011 rate of 5.1 percent. Automobile, SUV and light truck sales were solid in January relative to the same month in 2011. Vehicle sales remain high in the winter months. The unemployment rate settled at 8.3 percent in January, falling below 9 percent for the third time since March 2009. Finally, consumer confidence declined in January to 61.1 which is a 3.7 point drop from a strong December.

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 54.1 in January from 52.6 in December, but is still very close to falling below 50 which signals a recession for the manufacturing sector. Construction spending in January was down relative to both the previous month and January 2011. Durable goods orders and shipments were both down in January relative to both the previous month and January 2011. 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 of 3 percent in 2012, this shows a general decrease in real income.

Current Issues

As we end the month of February there is much to be optimistic about in the United States. Four quarter 2011 GDP was revised upward from 2.8 to 3.0 percent growth, the index of intent to purchase a new home shot up 8.2 percent in the last week of February, the Dow Jones Industrial Average closed above 13,000 for the first time since 2008 while the S & P 500 finished above 1,370 on the same day. However, there continues to be signs that our desire to be optimistic is misplaced. Factory orders for long-standing manufactured goods plunged 4 percent in January which was the highest decline in three years. Much of the decline came from the expiration of a key tax break for purchasing machinery and equipment that ended in December of 2011. The Standard and Poor's/Case-

Schillar Home Price Index fell in December in 18 of 20 markets. In fact, the latest quarterly gauge of national home prices fell to its lowest inflation adjust price since the index began in 1987. And perhaps most troubling, the once prosperous city of Stockton, California may well declare bankruptcy by summer.

Why can't we be more optimistic? Why has our economy not recovered in a more robust fashion as it has in every recession since The Great Depression? We believe that Europe and the U.S. are facing the "New Stagflation" which could end in a severe economic downturn.

The European Central Bank just injected 530 billion Euros or \$707 billion into the European banking system on February 29th which is the second offering of cheap three-year funds since December of 2011, taking the total north of 1 trillion Euros. Simultaneously, the U.S. Federal Reserve Bank (FED) has argued that it plans to keep interest rates near zero until late 2014. In addition, the FED has not ruled out buying additional government debt and already has a record \$2.94 trillion of U.S. debt (bonds) on its balance sheet since 2008. So what does this mean? It means that we are creating money in an attempt to stimulate the economy both here and in Europe which will simply lead to inflation (higher prices) and little, if any, real economic growth. Why? Because we have stifling regulations and the second highest corporate income tax rate in the industrialized world aka business has little incentive to take risks and create new jobs. The threat of higher taxes and more burdensome regulations only exacerbates this problem.

The U.S. National Debt is approaching \$15.5 trillion dollars or almost 100% of GDP with the EU Composite at greater than 100%. The U.S. and EU do not have a lack of tax revenue; both have excessive tax rates and over-spending problems. If taxes are not cut and government spending reduced, the EU and the U.S. will continue to be burdened by: a) no to slow economic growth, b) increasing debt, c) a continued lack of economic

competitiveness and d) ever-higher inflation in the not-to-distant future!

Conclusions

Perhaps U.S. and EU should study the New Zealand economy over the last 15 years...more next month!

Contact Us

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