

October 8, 2010

Introduction

The United States economy continues to try to shake off one of the most challenging economies in its history. By many standards, 2009 was the worst year since the Great Depression. Annual U.S. Gross Domestic Product (GDP) declined 2.4 percent, while Global GDP declined by 2 percent. Currently, the U.S. economy is showing mixed signs of improvement and still faces daunting financial issues, indecisive consumers and investors, unpredictable and unprecedented government fiscal and regulatory policy, record levels of government spending, and a mounting record national debt of \$13.56 trillion or roughly 95% of GDP. Real GDP increased at an alarmingly slow pace for the first half of 2010, decreasing from a finalized real growth rate of 5.6% in the fourth quarter of 2009 to 2.4% in the second quarter of 2010. This left second quarter GDP at a level not seen in almost a year. Unfortunately, the second revision of second quarter GDP released in September came in at a growth rate of just 1.7%, additional fuel for uncertainty and concern.

Key August/September Data

Positive Signs

According to the latest Manufacturing ISM Report on Business, the manufacturing sector of the U.S. economy continued to grow in September as evidenced by the Purchasing Managers Index remaining at a healthy level of 54.4%. U.S. productivity remains near record levels while cash balances for corporations are at an all-time high with non-financial based U.S. corporations holding more than \$1.95 trillion for investment. Private sector employment remained positive edging up by

64,000 jobs in September according to the Bureau of Labor Statistics. Pending home sales showed improvement in September reaching a five month high with fixed mortgage interest rates at a record low of 4.25% while the survey of consumers intending to purchase an automobile over the next 6 months remained positive in September. Finally, the Conference Board's Leading Economic Indicators for the U.S., Europe and China were positive in September growing at .3%, .4% and .5% respectively. The U.S. savings rate continues to grow realizing a rate of 6.0% in September. Finally, the Dow Jones Industrial Average climbed 773 points last month which was the strongest September rally since 1939.

Negative Signs

The Conference Board Report on Consumer Confidence turned negative in September dropping to 48.5 from 53.2 in August. Less than impressive job growth and slower automobile sales ended the month of September with concern for U.S. investors and the economy as a whole. The U.S. dollar index dropped 5.4% in September, the largest monthly decline since May, 2009, while gold rose above \$1,300 an ounce and silver surpassed \$22 an ounce respectively, giving us an additional reason to be concerned regarding future inflation. The U.S. unemployment rate remained static at 9.6% in September with nearly 15 million Americans unemployed and 159,000 temporary census taker and other government jobs eliminated in September. Total nonfarm payroll employment dropped by 95,000 while unemployment benefits remain at the record high extension of 99 weeks. August new private sector jobs created was revised

down to just 15,000 from 67,000 based on the September revision.

Current Issues

Assume General Motors (GM) and Toyota (Japan) operate plants in Ireland and each earn profits of \$1,000,000 there. Under current tax law, Toyota pays the 12.5% Irish corporate income tax rate, but avoids the 39.54% Japanese corporate income tax rate because Japan operates under a territorial system. Therefore, they only pay \$125,000 in taxes and net \$875,000 which they can repatriate back to Japan at no further cost.

GM, however, pays the 12.5% Irish corporate income tax rate (\$125,000). If they repatriate their income, they must pay the U.S. tax rate of 39.27% (on average) on the \$875,000 earnings after taxes. This comes to \$343,612.50. At this point, they take their credit of \$125,000 for foreign taxes already paid, bringing their U.S. taxes owed down to \$218,612.50 (\$343,612.50 - \$125,000). GM will net \$656,387.50 or pay an effective tax rate of 34.36% by repatriating profits back to the U.S. versus their Japanese competitor at 12.5%.

Today over 80% of OECD nations have adopted a territorial tax system. The United States is just one of five OECD countries to operate with a worldwide system, and of these five nations the U.S. is the only country to have a corporate income tax rate over 30%. In fact, the U.S. combined average (state and federal) corporate income tax rate is the second highest in the OECD and the third highest in the developed world. With a combined corporate income tax rate of 39.27% the U.S. dwarfs the tax rates of some of our largest global competitors such as China (25%), India (33.99%), Russia (16%), and Germany (29.44%). This disparity

between rates is largely due to a global tax reform trend centered around cutting corporate income tax rates. According to KPMG, an international tax and auditing firm, the global average tax rate on corporations fell from 32.69% in 1999 to 25.51% in 2009. All the while the U.S. rate has remained relatively untouched producing the incentive for companies to move production abroad in order to escape the higher U.S. tax rate.

Tax rates are becoming increasingly important in investment decisions as capital becomes ever more mobile in the global market place. Whether the U.S. moves to a territorial system (home country tax does not apply) or keeps our current system, a cut in the corporate income tax rate must be included in any tax reform if we are to make real progress in enhancing U.S. global competitiveness.

Conclusions

Our concern regarding a double dip recession in 2011 or 2012 is still present, but is being tempered by the hope that the 2010 fall elections will bring more bipartisan cooperation to Washington and a decidedly more pro-business policy focus.

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