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Micro-Management Economics

Always running for something, while seldom lacking a bad idea, the ever-populist Hillary Clinton has another plan to micro-manage the US economy. As is typical, her political narrative is chock full of victims and villains, yet falls short on substance. In this version, the culprit is a tax code promoting short-sighted corporate behavior, starving our economy of capital expenditures. Never mind that this is the same behavior producing all-time record corporate profits, which after all is the point of free enterprise.

As the story goes, corporate America is under-investing in long-term projects, as businesses opt to return profits to shareholders via rising dividends and stock buybacks. But, we are told, this is not managements' preference; corporate chieftains are being held hostage by Wall Street. Current management mindset is to keep corporate raiders at bay, and nothing works so well as record stock prices. So more money is going to shareholders, and less money is going to costly and uncertain spending projects. According to Mrs. Clinton, the trick is to devise a more complex capital gains tax structure, which will surely deter activist investors from asserting their shareholder rights.

Some owners can be so demanding.

It makes for a nice story, so far as political poppycock goes. Yes, capital spending is lagging, but perhaps globalization, technology, and a robust service economy explain the shortfall. Or maybe the problem is the sluggish economic recovery itself, leaving excess capacity in our industrial base. Defense spending cuts cannot help, nor can the targeting of the coal and oil industries. And there is the miniscule funding for basic infrastructure, such as roads and bridges. What ever happened to 'shovel-ready'? Then again, there is always something.

If Washington wants to target higher capital spending, it has the means at its disposal. Spend more money on public works projects, or provide direct tax incentives for corporations to increase spending. Accelerated depreciation offers a simpler and more effective use of the tax code to raise capital expenditures. It is certainly more plausible than a scheme to complicate investor taxes, expecting this annoyance to trickle down to corporate spending decisions. Who comes up with these ideas?

And if Mrs. Clinton's goals are met, then what? Here's one possibility:
A decline in employment and real wages, as capital spending supplants labor. The knee-jerk reaction will be restrictions on overseas outsourcing, trying to force jobs and investment back to the US. This will be followed by retaliatory trade wars, restraining global growth, and with it, capital spending. Did we just find a path back to low capital spending? So we are back where we started, all in the name of a meddling government. A dog chasing its tail has a better chance of success.

Ever consistent, Mrs. Clinton has once again hit the liberal double-play: a damaging solution to a problem that doesn't exist.

Next up is the White House, with its own ill-conceived ideas. Among its most recent is a plan to change overtime rules for salaried workers. Under long-standing labor laws, exempt 'white collar' workers are not paid for overtime work if they receive a minimum salary of 23,660 dollars.
The administration's revision more than doubles this salary threshold, to just over 50,000 dollars.

"We've got to keep making sure hard work is rewarded. Right now, too many Americans are working long days for less pay than they deserve," wrote President Obama in announcing this change. He added, "In this country, a hard day's work deserves a fair day's pay. That's at the heart of what it means to be middle class in America."

Picture this scenario: You begin your career working for a mid-sized business, successful if not thriving. Every day you show up by 8 am, well-groomed, neatly dressed, ready and eager to work. You settle into your own office, attend business lunches; and, when not neck-deep in research, participate in mid-level meetings. You receive full health care coverage, sick days, and paid vacation. You also earn a salary of 40,000 dollars per year. This is a pretty good start for a recent college graduate.

Now here is the catch... you leave work at 6 pm. That's ten hours per day, five days per week, totaling well beyond the standard 40-hour workweek. The White House believes you should bill your employer for working too much. Do you really expect to be paid ten hours of overtime each week? Are you a professional, or a hired hand?

Let's put it another way. If overtime pay is mandatory, you will either receive a lower salary, or your job will be outsourced. Say goodbye to the start of your career.

Not to be outdone are the cities of New York, Los Angeles, San Francisco and Seattle. All have enacted, or are moving toward, a minimum wage set at 15 dollars per hour. As so often occurs, new policy initiatives start on the west coast and work their way east, in this case skipping over most of the nation. New York City's belated move targets the fast food industry with a wage hike proposal to be phased in over several years.

For big city activists, fast food is an inviting target. It employs a low-skill, low-wage business model. It is also captive to a local market; outsourcing to China is not an option. We immediately think of the golden arches and the billions of dollars the business takes in every year. Surely there is room for higher pay.

What we don't initially consider is that the store with the iconic logo may be a franchise unit. The owner takes in millions, not billions, while he pays exorbitant rent for his prime location. He also pays high taxes, the usual food costs, and a franchise fee on every dollar of sales. He employs low-skill, low-wage labor because that is what the business demands. In the purest test of supply and demand, if the owner were paying below market wages, his workforce would leave. No one is flipping burgers for the high job satisfaction.

As recently reported by the Patriot Post:

> "Democrats are bickering over how high to raise the minimum wage, even though doing so would hurt constituencies the party claims to represent. Democrats all agree the minimum wage must be raised. The party's establishment politicians -- Harry Reid and Nancy Pelosi -- propose a minimum wage hike to $12. Democrat presidential candidate Bernie Sanders is calling for a $15 minimum wage, even though the socialist only pays his interns $12 an hour. Is that all he can afford to pay them?
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> A study published by the American Action Forum and the Manhattan Institute for Policy found both proposed minimum wage policies would decimate the jobs held by low-skilled workers who often vote Democrat. If the minimum wage rose to $12 an hour, the economy would lose 3.8 million jobs. If the minimum wage rose to $15 an hour, 6.6 million jobs would disappear. Besides putting the jobs of fast-food workers at risk, the Democrats' plan would hurt their supposed darling constituency: illegal immigrants. Of the 11.3 million illegals in this country, 8.1 million hold jobs. At the same time, there are 9.6 million unemployed Americans -- a number that would very well rise if Democrats take a top down, emotional approach to the economy."

In a recent interview with The Wall Street Journal, Buffalo Wild Wings Chief Executive Sally Smith was asked how minimum-wage increases are affecting the company's business decisions. According to Ms Smith:

> "You look at where you can afford to open restaurants. We have one restaurant in Seattle, and we probably won't be expanding there. That's true of San Francisco and Los Angeles, too. One of the unintended consequences of rising minimum wages is youth unemployment. Almost 40% of our team members are under age 21. When you start paying $15 an hour, are you going to take a chance on a 17-year-old who's never had a job before when you can find someone with more experience?"

The minimum wage ruse is a populist ploy that misses the point on two key issues. First, most Americans at one time in their lives earned, or will earn, a minimum wage. But they are not supporting a family on this wage. More likely the income will serve as spending money for America's youth, and offers a reminder that low skills generate low wages. If ever there was an incentive for youngsters to focus on their education, this is it. For those few Americans trying to support a family on low income, the political solution is found in Medicaid, Welfare, and the Earned Income Tax Credit. Where these programs are lacking, they should be improved at the expense of state and federal governments, not on the back of targeted businesses.

In addition, a higher minimum wage ignores the reality of today's economy -- it is increasingly global and highly competitive. Raising costs on American business will drive jobs out of the US and into foreign nations. Perhaps those nations will thank us for our generous gesture.

Vultures and Other Dangers

In a recent op-ed piece in The Wall Street Journal, titled "What the United States Owes Puerto Rico", authors Joseph Stiglitz and Mark Medish describe Puerto Rico and Greece as "cases of fiscal mismanagement and unsustainable external debt in the context of fixed exchange rates through a common currency, the U.S. dollar for Puerto Rico and the euro for Greece."

That is to say, both are broke, with no easy way out. Fair enough.

The authors then assert that, "Excluding unfunded pensions, Puerto Rico has a debt burden of more than $70 billion, which it cannot service. Most of Puerto Rico's private creditors -- such as Oppenheimer Funds and Franklin Templeton Investments, the latter also a large creditor of Ukraine -- insist that Puerto Rico merely has a serious short-term liquidity problem but is not insolvent. Yet absent a comprehensive long-term growth strategy, this is a distinction without a difference. The territory can't pay its debts today, and with short-term debt financing at the high interest rates demanded by creditors, it will be even less able to pay its debts tomorrow."

While arguing for a reasonable change of law -- allowing Puerto Rico to enter bankruptcy in order to restructure its debts -- the authors hit on a tangential, yet critical, issue with their use of the inflammatory phrase 'vulture creditors'. This is no accidental slip of the tongue.

The emerging narrative is that lenders are to be blamed and punished for the profligate spending of debtors. Argentina defaulted on its debt simply because it thought it could. Any recovery by holdout creditors will be costly, time consuming and likely of little benefit to the majority of Argentine creditors. Meanwhile, Argentina has popularized 'vulture' as a pejorative term for any lender who expects his money paid back in full.

In the case of the mortgage GSEs, Fannie Mae and Freddie Mac, conservatorship was understood to mean one thing, until the federal government imposed its third-amendment profit sweep, at the considerable expense of preferred and common shareholders. This was seen as retribution for the lax credit standards of the two mortgage giants -- whose easy-lending policies of course were developed at the behest of the same federal government.

The bankruptcy restructuring of General Motors elevated the status of employee pensions, to the detriment of previously-senior bond holders. California is moving piecemeal in the same direction, chipping away at creditor rights, again to the benefit of pension claims. In a pinch, other states will likely follow. Apparently pensioners vote in greater numbers than bond holders.

The recurring theme is that creditors are under siege, with governments leading the attack.

Given today's low yields, if bond holders believe they are fully-compensated and well-protected for these risks, they best beware of dangers far worse than vultures.

Poverty and Prosperity

Excerpted from “The Left Has Its Pope” by Thomas Sowell; TSowell.com
September 22, 2015

Any serious look at the history of human beings over the millennia shows that the species began in poverty. It is not poverty, but prosperity, that needs explaining. Poverty is automatic, but prosperity requires many things -- none of which is equally distributed around the world or even within a given society.

Geographic settings are radically different, both among nations and within nations. So are demographic differences, with some nations and groups having a median age over 40 and others having a median age under 20. This means that some groups have several times as much adult work experience as others. Cultures are also radically different in many ways.

As distinguished economic historian David S. Landes put it, “The world has never been a level playing field.” But which has a better track record of helping the less fortunate -- fighting for a bigger slice of the economic pie, or producing a bigger pie?

In 1900, only 3 percent of American homes had electric lights but more than 99 percent had them before the end of the century. Infant mortality rates were 165 per thousand in 1900 and 7 per thousand by 1997. By 2001, most Americans living below the official poverty line had central air conditioning, a motor vehicle, cable television with multiple TV sets, and other amenities.

A scholar specializing in the study of Latin America said that the official poverty level in the United States is the upper middle class in Mexico. The much criticized market economy of the United States has done far more for the poor than the ideology of the left.

source:
Bloomberg
Patriot Post
Tax Foundation
TSowell.com
The Wall Street Journal

Tidbits..

Federal Reserve retains zero interest rate policy, marking nine years since last rate hike.
US Treasury finds free money, issues three-month bills at zero percent yield, first time in history.
International Monetary Fund cuts global growth forecast for 2015 and 2016, with emerging market economies particularly weak.
European Central Bank says it is willing to expand its version of Quantitative Easing.

Because it is working so well, or so poorly?

United Continental Chairman & CEO is ousted amid corruption probe, set to receive separation payments of 28 million dollars.

Who says crime doesn't pay?

AB InBev reaches tentative 106 billion dollar merger pact with SABMiller, combining world's two largest brewers.
Privately owned Dell to acquire EMC for 67 billion dollars, in record-size technology deal.
Europe's Altice to buy Cablevision Systems for 18 billion dollars, creating fourth largest US cable-TV company.
Global merger and acquisition activity exceeds three trillion dollars year to date, near record pace.

General Motors settles Justice Department probe of faulty ignition switches, agrees to 900 million dollar penalty; no individuals expected to be charged.
Apple reportedly developing electric car with self-driving features, target date 2019.
Volkswagen caught cheating on clean-diesel emissions, 11 million cars tainted, CEO resigns.
US auto sales running at highest rate in 10 years.

Securities and Exchange Commission regularly over-counts its enforcement cases to win public support and Congressional funding, study shows.

Tax Foundation ranking of international tax competitiveness places US tax code as third worst among 34 industrial nations.

Thank goodness for Italy and France.

Royal Dutch Shell abandons Alaskan Arctic oil exploration project after spending seven billion dollars looking for new reserves.

Big oil includes big, costly risks.

World food prices fall 19 percent in past year, according to United Nations' organization.
Gasoline prices drop to six year low.
Health care spending accelerates to 5.5 percent growth rate in 2014, after five years of sub-four percent growth.

A triumph of Obamacare, or a failure?

US federal budget deficit falls to 439 billion dollars in fiscal year 2015, lowest level since 2007.

Someone in Washington will claim this as an accomplishment.