January 6, 2017

Even though the American public is already pretty well acquainted with Donald Trump, the first year of his presidency will reveal how he interacts with the new Congress to introduce favored policies. They are too numerous to examine closely here, such as those in the societal category: college debt, gang violence and care of military veterans, or in the area of international relations: modernizing the military, building a Mexican border wall, suppressing ISIS and managing immigration from terror prone areas. But even at this early date it is evident that some of the president-elect's attitudes are significant to the economic outlook and it is timely to discuss how they may influence our personal financial objectives.

Simplest of the batch is the reduction of personal and corporate income taxes. Even assuming that actual outcomes probably will fall short of the proposals mentioned during speeches and interviews, it is easy to like a tax reduction. (For example, a company paying taxes at the full 35% corporate rate would enjoy an increase in net income of 30.7% if the rate dropped to 15%.)

In a similar vein, the encouragement of energy development such as solar projects and increased fracking in oil and gas fields, plus a widespread overhaul of the nation's roads, schools, tunnels, and bridges would be strong stimulants.

A background subject but one with great potential importance is the Supreme Court, which became evenly balanced between left and right viewpoints since the recent death of Antonin Scalia. The new president is likely to appoint as many as four justices, as three of the remaining eight are around age 77 and the average age of retirement over the past 50 years is 78. (An example of a contentious issue that would be settled is the legality of requiring photo ID at voting booths.)

More problematic would be the complex subject of tariffs. The concept is simple, in that America could levy taxes on imported goods, thereby relieving domestic manufacturers of foreign competition and enabling an increased share of market and higher prices. The obvious problems are possible tariff retaliation against US exports and the presumed diminishment of prosperity of our customers abroad. Basically, we are net exporters to Europe and big net importers from Asia. Europe is heavily laden with the cost of social support programs while Asia, having been influenced historically by more authoritative societal structures, has lower production costs and selling prices. With respect to quality of production, Japan progressed from crude, simple items to high quality manufactures over the past 80 years, while China is perhaps halfway there. Asia and India is where the growth potential is greater. Down the road, as measured by decades, are Latin America and Africa.

With respect to the American economy, taking note of its modest growth in public income and consumption, with unemployment moderate but improvable, it seems we have fertile ground for the range of stimulants being proposed. Political opposition within the Republican Party remains to be measured when the new Congress convenes but we suspect the power of electoral success will tend to solidify the majority while the Democrats regroup. Accordingly, passage of the first batch of legislative proposals ought to stimulate the economic-political mood in noticeable ways. Actually, the upbeat mood became palpable before the election and has stayed that way since.

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The black cloud remaining on the horizon is $20 trillion of government debt, for which the only solution is a combination of economic growth, future budget surpluses instead of deficits, and a dash of inflation to cheapen the value of the burden. We shall see.

Meanwhile, the best resting places for wealth continue to be stocks, inflation protected short term debt and gold. Long term bonds are to be avoided.

All in all, this ought to be a decent year.

Sincerely,

John May