MIDLAND DAILY NEWS

Northwood Economic Outlook: Tax reform needs to be addressed

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The U.S. economy showed stronger than expected results as the first half of 2017 came to a close.

The job market showed robust results with an impressive 220,000 new jobs created in the month of June. The June numbers were strong considering economists expected only 185,000 jobs to be created for the month.

One statistic clearly worth noting is that the U.S. economy has created an impressive 863,000 new jobs since President Dondal Trump took office, according to the Bureau of Labor Statistics.

The unemployment rate increased slightly to 4.4 percent in June and was accompanied by an improving labor force participation rate of 62.8 percent, which was an improvement over the May rate of 62.7 percent. The labor force participation rate is at one of its lowest levels since the late 1970s giving economists pause for concern, while the current unemployment rate gives pause for optimism as it stands at its lowest level in 16 years.

Average hourly earnings increased slightly in June by 1.8 percent on an annual basis. The U.S. national debt is almost 20 trillion dollars or 105 percent of U. S. GDP, with the specter of higher interest rates posing an additional drag on the U.S. economy in the future.

Real wages remain sluggish, with consumer spending making up 70 percent of U.S. GDP, while real average hourly earnings growth of 3 percent or greater is imperative if average U.S. GDP growth is to return to 3.5 percent or higher. Over the last 12 months, U.S. real wages have increased less than 1.65 percent resulting in U.S. GDP growing at just under 2 percent on an annualized basis since 2009.

Preliminary second quarter U.S. GDP came in at a respectable 2.6 percent, up from a disappointing revised first quarter GDP of 1.2 percent. U.S. GDP has averaged 3.2 percent annually since the end of U.S. Great Depression.

The U.S. continues to receive little help from China and much of the global economy as they are not growing as predicted in 2017 and are providing little catalyst for additional GDP growth in the U.S.

Through six months, consumer spending continues to be the brightest spot of the U.S. economy and could pick up steam in the future given the state of U.S. wage growth and the tax cuts promised by the 2016 election of Donald Trump.

Investment in business infrastructure, equipment and intellectual property declined in 2016 and is lagging so far in 2017, especially given the state of current oil prices and associated tax revenue from gasoline sales.

One of the most important indicators for the economy in general and the robustness of the automotive sector are monthly actual total miles driven on U.S. highways, which according to most recent data, increased from February 2017 to March 2017. Gasoline and oil prices have slowly moved downward in June from May and remain more than a dollar below the levels they were at during the same time in 2015.

U.S. oil prices started the year at roughly $46 a barrel and we continue to believe they could very well end the year averaging less than $50 a barrel based on current global trends and their price at $46 a barrel in late June.

U.S. gasoline prices averaged $3.36 a gallon in 2014; averaged $2.50 a gallon in 2015, averaged $2.23 for 2016 and is currently priced at $2.47. With gasoline prices averaging less than $2.48 a gallon the last few months, we expect stable to slightly lower gasoline prices by year end based on the projected growth in the worldwide supply of oil relative to demand and the slower than expected growth in the European and Chinese economies.

Current Issues

We have been calling for U.S. tax reform and a considerable tax cut at the federal level for more than a decade. The U.S. has the second highest marginal corporate income tax rate in the industrialized world at 38.98 percent and trails only Saudi Arabia among developed economies.

The U.S. taxes corporations at a higher marginal rate than any of its fellow G-20 or OECD member countries as it places American businesses at a severe competitive disadvantage on a domestic and international basis.

The cornerstone of the U.S. and all other productive economies is a free and competitive marketplace which produces profits, products and services and jobs! They have economies that encourages risk-taking and entrepreneurial job creation and generate the revenue which allows for just and productive government.

Like the Heritage Foundation and the Cato Institute, we like much of what Trump is proposing. Here is what we would like to see in the final tax bill:

1. A cut in the federal corporate tax rate from 35 percent to 15 percent as we believe it would jump-start the U.S. economy and provide great incentive for capital investment and hiring. It would also provide great incentive for U.S. corporations to bring home nearly $3 trillion dollars in profits currently being held overseas due to high U.S. corporate tax rates.

2. Adopting a "territorial tax system" rather than our current "worldwide tax system" would encourage multinationals to move their headquarters to the United States, as well as reverse the trend for U.S. corporations to incorporate abroad.

3. Reduce the number of individual income tax brackets from the current level of 7 to 3 with the rates being 10 percent, 25 percent and 35 percent. Certainly, we expect that many current deductions will be reduced or eliminated in order to meet revenue and economic growth needs.

Conclusion

We expect that the tax cuts noted above, coupled with continuing regulatory reform, will produce the kind of economic and revenue growth realized from tax cuts during the Reagan Administration. We believe that U.S. GDP growth can return to levels exceeding 3.5 percent annual growth with said changes. However, it is important to remember that tax cuts must be coupled with long-term spending reforms or the deficits that plagued the end of the Reagan administration and haunt the U.S. economy to this day will spell disaster over the long run. We also encourage a spirited discussion of a national "fair tax" in the near future.