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“Checks” and “Balances”

Our government was designed with great care by the Founding Fathers to protect “We the people” from the tyranny of majorities or loud and powerful minorities. Our system of “checks and balances” is not perfect, but it has served an ethnically diverse nation well these 230 plus years. However, one glaring omission threatens to ruin it all. Fundamentally understood and respected by the Fathers, but nearly lost on today’s leaders is the idea of fiscal discipline, or spending no more than is received. Indeed today’s Senators and Congressmen are richly rewarded by “we the people” through longevity of office and growth of power, to take from one class and give it to another. Our leaders write larger ‘checks’ against ever-decreasing asset and ever-increasing liability ‘balances’ with no end in sight. Perhaps “we the people” are finally rising up to say enough is enough?

The protests at town hall meetings across the country are getting much media attention, but less analysis. Yes, that the arrogance of the majority party angers those in the minority. But wasn’t that true when the tables were turned during the former administration? Remember the town halls Mr. Bush conducted around privatizing Social Security? Sadly today, the media conveniently dismisses much of the rancor as mere politics, which is revealing in and of itself. But clearly, there are deeper and more fundamental issues driving this movement.

Americans, Republican and Democrat alike, are sick of seeing their hard-earned taxes so easily and absent-mindedly spent by today’s politicians. As Dr. Ed. Yardeni points out, “mobs of taxpayers are riled up by the open-ended spending spree in DC. After years of excessive borrowing, Americans are scrambling to live within their means and they think our nation should do the same, particularly in light of the mess in which we find ourselves.” A recent Gallop poll shows that heated protests at sessions held by members of Congress have made independents more sympathetic to the protesters’ views than to the administration. Independents by 2-1, say they are more sympathetic to the protesters now. People don’t need the media to tell them that their taxes will soon be rising if the free-spending continues.

Perhaps the stock market rise is due in large part to investors taking heart in the possibility of gridlock returning to Washington to end or slow the spending spree. Yesterday afternoon, House Speaker Nancy Pelosi said “there’s no way I can pass a bill in the House of Representatives without a public option.” As Bloomberg puts it, Ms. Pelosi drew a line in the sand on one of the most contentious issues surrounding the health-care overhaul after Obama administration officials earlier suggested the White House might be willing to back away from the public option to win broader support. Republicans and even some Democrats have said the idea is a nonstarter in the Senate. It also looks like the House’s version of cap and trade legislation which curbs greenhouse-gas emissions will not pass the Senate due to its potential harm to the economy. Investors like gridlock.

So what about the economy? Fed Chair Ben Bernanke just moments ago told bankers in Jackson Hole, Wyoming to expect the economy to grow soon saying “fears of financial collapse have

receded substantially” adding that “the prospects for a return to growth in the near term appear good.” He acknowledged the continued difficulty that many households and businesses had in gaining access to credit. Regarding timing, he said that “the economic recovery is likely to be slow at first,” and unemployment will decline “only gradually from high levels.”

The week’s economic data were mostly supportive of Mr. Bernanke’s upbeat forecast. The week started with a report from the NY Fed showing strong industrial production. The Empire State Manufacturing index jumped to 12.08 from July’s -.055, the best reading in the recession.

The index of leading economic indicators is pointing toward recovery. The LEI rose 0.6% in July boosted by rising long rates, a dip in initial jobless claims, and the rise in the factory work-week. Claims would seem to be in question for next month's August reading. Dragging on the index are the continuing negative consumer expectations readings, driven by continuing high unemployment, tight credit, rising gasoline prices, and the looming threat of higher taxes.

During July, motor vehicle assemblies in the US rose 45% to 5.74 million units from 3.97 million units in June. A year ago, the industry assembled 9.33mn units. In other words, there is plenty of room for a V-shaped recovery in the auto industry. Yardeni says a V-shaped recovery in auto production could produce a V-shaped recovery in real GDP, at least for a couple of quarters. But it is doubtful the consumer will soon pick up the slack.

Housing made several bold steps forward this week. Housing starts in June increased 3.6%, following a huge 17.3% spike in May. Sales of existing US homes jumped more than forecast in July to the highest level in almost two years. Purchases climbed 7.2% to a 5.24 million annual rate, the most since August 2007, according to the National Association of Realtors. The gain was the biggest since records began in 1999, a period which included the housing bubble.

While impossible to name all of the reasons the American economy works so well, perhaps it’s useful to remind ourselves of a few of the obvious ones. This country is among the most innovative in the history of the world. Distinctly American are the combination of the profit motive with model patent and copyright laws which protect one’s intellectual property enabling him to reap the rewards of his ideas and hard work. Add our rich cultural diversity to fuel those ideas, an excellent university system to train and direct them, a national Internet to link every thought and ideas can become reality at unprecedented speed. Near limitless capital from private and government sources stands ready to fund the idea’s development. Place this innovation machine amidst the world’s richest natural resources, temperate growing climate, and near-limitless space to nurture them. Connect even the remotest regions by an unequalled natural river and waterway system, interstate highway system, rail, and air systems and one begins to see just how unstoppable this innovation machine can be.

To reach its potential, this big beautiful innovation machine must be governed by those who understand how she works. Drain too much lubrication there, or ‘adjust’ too much here and she grinds and screams to beat the band. Her complaints, her “checks and balances” are exactly what keep our elected ‘mechanics’ in line. Either they learn on the job how to get the best out of her, or she rolls on by them.