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# Something to Think About

OAKWORTH CAPITAL BANK

COMMON CENTS

This morning, the Bureau of Economic Analysis (BEA) released its first stab at 4Q 2016 Gross Domestic Product (GDP). Since the BEA estimated the economy grew at a 3.5% annual rate for 3Q 2016, no one was expecting a huge number (or shouldn't have). However, the 1.9% figure the BEA gave us was less than the so-called 'consensus' estimate of 2.2%, but it wasn't surprising.

In fact, it was the somewhat gaudy 3Q estimate I found a little, well, head-scratching. Sure, the headline looked great, but how in the world did our trade deficit improve so much in one quarter as to add 0.85% to the 3.5% estimate? Sure, the US dollar fell a smidgeon, a smidgeon, during 3Q, but enough to engender a 14.4% annualized surge in exports (goods) and essentially no change in imports (goods)? That seemed a bit much to me, even if the various governmental agencies could support it in some form or fashion.

Historically, there tends to be some volatility with the trade data in the GDP report, if volatility is the right word. As a result, a large surge in either exports or imports in one quarter ordinarily results in a swing the opposite direction the next. Such was the case this morning. To that end, exports (goods) reportedly fell at a 6.9% clip and imports (goods) surged 10.9%. As a result, the worsening in our trade deficit during 4Q shaved a full 1.70% off the GDP equation.

In so many ways and words, the 3Q number (headline) probably overstated domestic economic growth, just as the 4Q number understated it. For the year as a whole, the BEA currently estimates GDP grew 1.6% when adjusted for inflation. This means the US economy has not grow at a 3.0% or greater clip for 11 years, as 2005 was the last turn of the calendar when we had such 'august' economic activity.

Further, the trailing 10-year real GDP number (annualized) for the US economy is currently 1.32%. I use the word currently because the BEA will take a few more stabs at its 4Q estimate before declaring it official. To put that 1.32% number into perspective, consider it is the worst trailing 10-year number (using annual/calendar year observations) since, get this, 1939. The observation at the end of 1954 was close at 1.34%, but that included a massive economic downturn in 1946 after the end of WWII.

To be completely fair, there is issue of the 'law of large numbers' at play here, at least the financial context of said law. It is hard to maintain the same level of relative growth as the absolute value of the denominator increases. Put another way, it is easier to grow 10% when your sales are $100,000 than when they are $100 million.

Even so, 1.32% annualized growth over the last decade, and 2.10% over the last 5 years, isn't terribly robust. After all, those numbers reflect the inflation-adjusted economic output of every man, woman, and child in the United States. IF the US economy has only grown a little over 1.3% per year over the last decade while our population has increased on average 0.7% per year, well, you can intuit per capita income has barely budged….and some people have undoubtedly slipped or fallen behind.

For some years, I have maintained to anyone who will listen our bigger problems in the US are societal and not economic. We can grow 2% until the end of time, if only the Top 25% grows 8%

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per annum. With that in mind, let me give you what I recently submitted to the Montgomery Advertiser (and from which I have received considerable positive feedback). *Admittedly, the first paragraph of this snippet is kind of a repeat of what I just wrote.*

> For the last five years or so, when pressed during the Q&A, I have maintained the country's bigger problems are societal, not economic. We can chug along at 2% until Doomsday, if only the Top 25% grow 8% per year and everyone else stays flat on their back. It is just math.
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> The data suggests this has basically been the case for the better part of two decades, as median household income is currently less than it was in 1999, when adjusted for inflation. The numbers are even more discouraging the lower you go on the income spectrum. Just staring at the data, and not the actual households that comprise it, you can argue many Americans haven't gotten ahead of the game in quite literally decades.
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> If so, there is no way this won't eventually foster some sort of societal discontent.
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> Therein lies the quandary for economists and politicians. The headline data says things are decent and perhaps sustainable. However, when you start peeling back the layers of the proverbial onion, the numbers start to break down. Do you really need a calculator to understand this? Or will a good set of eyeballs suffice?
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> Certainly, from purely a numbers standpoint, we don't need to physically produce a single thing in this country, and the economy will still grow. Of course, we need to convince investors the US is still a good bet, and we have been doing so for a long period of time. In so many ways, as long as the money keeps flowing into and around the US, the spreadsheets and tables will say one thing, while many of our neighborhoods and small towns may say something else altogether.
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> I would argue this why a strong blue collar middle class is important. It is a powerful glue that helps make our society strong. We will always have the rich and the poor, by definition since wealth is relative. It is that vast middle segment which determines long-term success. When it is enfranchised in the system, good things tend to happen, and not all of them economic. Historically, it seems producing items of meaningful value is an effective way of doing this.

In so many ways, academic economics is arguably the business of trying to explain the past and predict the future with math. We can debate the effectiveness of these efforts until the cows come home, but I would always add: even if economics can predict future behavior within some reasonable variance, it can't predict the individual human psyche….whether it be pleasure or discontent.

With this in mind, I would imagine there are any number of workers at shuttered textile mills who would rather have their old jobs back, as opposed to working at, say, Wendy's for not a completely dissimilar amount of money. In fact, I would bet you a beer it would be a significant percent, if not an outright or even overwhelming majority. I could be dead wrong, and very well might be, but I can't imagine I would/should be as different as everyone else.

A week or two after the election, I picked up a copy of The Economist at the airport, and wrote about it, again, for The Advertiser. Let me give you the pertinent point *(lots of cutting & pasting here today)*:

> In the letters to the editor, an economics professor from Greece, seriously, made a prescient observation about the US electorate, and I paraphrase mightily: "while it might be economically efficient for the US worker to flip burgers in order to afford a 50" Chinese made television set, perhaps they would settle for a 30" variety if only they could make it themselves."
>
> Sometimes the wisest observations are the most obvious. Someone just has to say them, and this one got me to thinking. The more I thought about it, the more I concluded the writer was spot on accurate. While there is no shame in flipping burgers, and my first job was making sandwiches, there is no great honor in it either. Let alone having that be your life's work.

## Something to Think About Cont.

> But how to stem the tide of offshoring production? That is a great question. I would first have to say we will never return to the days when 27% of the workforce was actively engaged in manufacturing activities, as it was 50 years ago. However, there is room for improvement from the 8-9% today. This is primarily due to technological efficiencies and increased automation, but we still import a lot of stuff we used to make ourselves.
>
> As the writer of the letter implied, it might be economically efficient to do this, but the societal impact in doing so might not be worth the money. Catch my drift?

It is an interesting topic for discussion or a college level thesis.

Hey, it is all well and good for people, like myself, who have graduate degrees and have the luxury of waxing poetic about how free trade is good for the economy and how we don't need to produce a single thing in this country in order to prosper. I could pull out plenty of numbers to support these contentions, and I believe them to be absolutely accurate in pure dollars & cents.

However, lost in the noise/data are hordes of people, because not everyone can design, engineer, and market the goods & services the brightest of the bunch concoct….for whatever reason. Our politicians, policy makers, economists, and CEOs should always remember this, and also remember what George Bailey said:

> "Just a minute, just a minute. Now, hold on, Mr. Potter. You're right when you say my father was no business man. I know that. Why he ever started this cheap, penny-ante Building and Loan, I'll never know. But neither you nor anybody else can say anything against his character, because his whole life was...Why, in the twenty-five years since he and Uncle Billy started this thing, he never once thought of himself. Isn't that right, Uncle Billy? He didn't save enough money to send Harry to school, let alone me. But he did help a few people get out of your slums, Mr. Potter. And what's wrong with that? Why...Here, you're all businessmen here. Doesn't it make them better citizens? Doesn't it make them better customers? You...you said...What'd you say just a minute ago?...They had to wait and save their money before they even ought to think of a decent home. Wait! Wait for what? Until their children grow up and leave them? Until they're so old and broken-down that they...Do you know how long it takes a working man to save five thousand dollars? Just remember this, Mr. Potter, that this rabble you're talking about...they do most of the working and paying and living and dying in this community. Well, is it too much to have them work and pay and live and die in a couple of decent rooms and a bath? Anyway, my father didn't think so. People were human beings to him, but to you, a warped frustrated old man, they're cattle. Well, in my book he died a much richer man than you'll ever be!"

Now, perhaps this doesn't make for scintillating reading today, and it probably doesn't have much to do with reality. However, this topic has been creeping into my thoughts with each passing set of economic data. Something is going to give, in our society, at some point if we don't grow this economy at a far more rapid rate than 1.6%.

As such, every policy out of Washington needs to reflect this….that needs to be job #1. Thus far into the new Administration, I am not necessarily overjoyed, but still optimistic.

## Disclosure