John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday February 1, 2023

The U.S. economy is still growing but the rate of growth is slowing. The fourth quarter GDP report showed the economy grew at a 2.9% rate. That is good news. But layoffs by tech giants including Amazon and Microsoft plus a major slump in chip demand indicates a loss of momentum. Likewise, news that restocking inventories accounted for 1.46% of the growth points to slower growth ahead. Businesses will not keep adding to inventories unless consumer spending increases. The sharp decline in the savings rate - 2.9% in the fourth quarter compared with 7.3% a year ago - suggests that consumers are running out of savings. That may mean a coming decline in consumer spending.

As the economy slows the rate of inflation is declining. The Fed's favorite inflation measure, the personal consumption expenditure price index fell to 3.2% in the fourth quarter, down from 4.3% in the third quarter and 7.5% in the first quarter. That is remarkable progress in the inflation battle and indicates that the Fed may not have to keep raising interest rates much longer.

There was a 6.7% fall in fixed private investment, most of which was in housing. High prices plus rising mortgage interest rates have significantly slowed the pace of housing sales and stopped the prior sharp rise in prices. Housing isn't alone. Motor vehicle prices and sales have also slowed.

“Believe it or not, a central bank that wants to control inflation can do so with the right monetary policy. That was clear Thursday in the Labor Department’s report that inflation fell in December for the sixth consecutive month at an annual rate. If the Federal Reserve keeps it up, we might escape the worst inflation in 40 years with less economic damage than it looked three months ago. The biggest risks to the U.S. economy other than higher interest rates this year are probably the tax increases in the Inflation Reduction Act and a regulatory onslaught that are compounding business uncertainty. President Biden has a growing economy, and let’s hope he can keep it.” (The Wall Street Journal, Jan 27 2023)

Millionaires and billionaires have been fleeing high tax states like California and New York. Recent proposals to increase wealth taxes have been an incentive even for entrepreneurs to look for business friendly states. One entrepreneur is looking at North Dakota as a state where business is welcome and supported. Democrats are the political leaders in the high tax states. They are upset at the loss of wealthy taxpayers. The mayor of New York City has been outspoken about the problem. He wants an end to the wealth taxes saying that the city needs all the billionaires it can find. The top income tax payers provide more than 40% of the city’s tax revenue. Losing the wealthy means that others will have to pay more. But that sensible attitude is rare among blue state legislatures.

“Democrats finally have a strategy to stop billionaires from fleeing high tax states: Block the escape routes. That’s the logic behind coordinated moves in progressive states to tax wealth. The reforms aren’t likely to pass immediately, but they illustrate the increasingly open socialist goals of progressives and their public-union backers." (The Wall Street Journal Jan. 27, 2023)

California's tax would take 1% a year from households worth more than $50 million and 1.5% from those worth more than $1 billion. The California bill would also require taxpayers with illiquid assets to file yearly reports on their holdings and eventually pay the tax, even if they move out of state. Other blue states have the same idea but with their own twists to tax the wealthy even if they move. Washington state Senator Noel Frame on a zoom call said: "They will pay what they owe."

To me this is astounding. These successful, wealthy tax payers have been paying and driving state tax revenues to new highs. Why attack successful people? Why drive them out of your state?

If blue states persist in attacking success and wealth, they will create a new long-term trend. Other states with lower tax rates and a business-friendly atmosphere will benefit. They will attract the future successful people and all that goes with that. Successful businesses are where they are today because the atmosphere once was business-friendly. Successful businesses are followed by universities, hospitals, and a long list of other infrastructure components. Blue states with high taxes risk losing these benefits over the long run.

As for the stock market investors like the news of lower inflation but worry what the slowing economy will mean for corporate profits. There is a wide range of opinions among analysts on what corporate profits will be like over the coming twelve months.

Some see lower profits this quarter but much better results later in the year. In my view, managements will do what they can to cut costs and keep profit margins healthy. That will minimize the damage as the economy slows. And that will position profits to grow nicely once the economy turns the corner and resumes faster growth.

I will have the next market review and update for you one week from today on Wednesday, February 8, 2022.

All the best,

John Dessauer