

John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday October 20, 2021

How many times have you heard President Biden and other Democrats say that the rich and corporations aren't paying their fair share of U.S. taxes? Guess what, that is not the case at all. Rich Americans pay more taxes than the rich in any other country. Data from the OECD show that the top 10% of American households earn about 33.5% of all earned income but pay 45.1% of all income taxes, including Social Security and Medicare payroll taxes. That progressivity ratio of 1.35 is far higher than in any other country. The ratio in France is 1.10. In Germany it's 1.07, and in Sweden an even 1.0%. Conversely, the bottom 90% of earners in the U.S. paid 55% of the taxes. The bottom 90% of earners in France paid 72%. In Germany it was 69% and in Sweden 73%.

What's more the U.S. Joint Committee on Taxation and the Congressional Budget Office found that the 2017 tax cuts made the American tax system more progressive, and according to the CBO, the "highest quintile's share of federal taxes was 0.5 percentage points higher in 2018 than in 2017". How is that possible? For the most part the answer is that people don't understand that corporations don't ultimately pay taxes. Taxes imposed on corporations are partly paid by consumers through higher prices and partly by workers who earn less. Workers pay between 50% and 70% of the corporate tax that isn't passed on to consumers in higher prices. After the 2017 corporate tax cuts there was record growth in real wages, especially among low-income, minority and disadvantaged workers. So, the tax cuts especially the corporate tax cuts favored workers in the bottom

quintile far more than those in the top quintile. Overall, that resulted in the top earners paying a bigger share of the taxes.

The next question is, do we need a tax increase? In the fiscal year that just ended, federal revenue hit a record \$4 trillion. Taxes from corporations rose 75% year over year from \$158 billion to \$370 billion. Individual income taxes rose \$443 billion, or 27.5% to reach \$2.05 trillion. That's about 9% of the entire U.S. economy. The CBO in its monthly budget summary said: "that increase most likely reflects higher total wages and salaries, particularly among the relatively high-income workers who are subject to higher tax rates on earnings."

In other words, the rich had a good year, but they also paid a huge fiscal dividend in taxes. President Biden: Does \$2.05 trillion qualify as a "fair share"?

The problem of course is the spending side of the federal budget. Federal spending rose 4% in the fiscal year to \$6.82 trillion. That is 30% of GDP. Left alone, some of that will decline as emergency spending due to the pandemic eases unless Democrats succeed in pushing through the massive expansion of government.

"All of this raises the question: With tax revenues coming in like a gusher, and the economy slowing from supply-side shortages, why raise taxes at all? In particular, why raise tax rates when current rates seem to be capturing the profits of companies and income of individuals well enough? There's no fiscal or economic logic to it, so the likely answer is simply to punish Americans who make more than what Mr. Biden thinks is fair." (*The Wall Street Journal*, Oct. 13)

The Biden agenda is running into a major political hurdle. The Democrats hold a slim majority in the House, and are tied 50-50 in the Senate. In addition, President Biden won by a narrow margin. This is hardly a call for a mandate. But the President and many Democrats have been acting as if they really had a mandate to massively expand government and raise taxes. But they are now running into trouble. A new poll by Gallup asked whether government should do more or less to solve the country's problems: 52% of Americans said the government is doing too much. A year ago, when Gallup asked that question 54% said they wanted government to do more to solve the country's problems. This year's results show that last year was a blip. The only other time over Gallup's 29 years asking that question that at least half of Americans wanted more active government was after the 9/11 terror attacks.

The biggest shift over last year is among independents. Last year 56% of independents favored more government; that has dropped to 38% today. Democrats are divided, 37% favor more taxes and services, 40% want to keep them where they are and 19% want lower taxes and fewer services. No wonder the \$3.5 trillion budget proposal has stalled in Congress. Every member of the House faces reelection a year from now. The last thing they want is to face a crowd of voters upset about higher taxes and more regulation.

Meanwhile third quarter earnings season has begun. The early results from banks and other financial institutions are looking good. Analysts now expect a 29.6% year-over-year increase in S&P 500 earnings for the third quarter. That will be down from the 96.3% increase in second quarter earnings. But the second quarter comparison benefited

from the pandemic depressed second quarter 2020 earnings. And a gain of 29.6% is outstanding. Companies have done very well controlling costs and dealing with the myriad pandemic related issues. In coming quarters, the comparisons will become more difficult and corporations still face shortages and inflation. As usual, the future course for corporate profits is uncertain. For now, we can enjoy the profit boom for at least one more quarter.

I will have the next market review and update for you one week from today on
Wednesday October 27, 2021

All the best,

John Dessauer

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