

Government, the Anti-Stimulus

After a strong ADP jobs report last Wednesday (297,000 new private jobs in Dec), we raised our jobs forecast. Going into Friday, we expected the official report to show a net gain of 220,000 new jobs in December. When added to the weak November report (+39,000 jobs), the December rebound would bring the two month average back to about 130,000 per month.

When it came out, the headline said just 103,000 new jobs. However, revisions to prior months added 70,000 and the three-month average is now 128,000 jobs per month. Cut to the chase and the job market looks much like we expected.

Yes, civilian employment – an alternative measure of jobs that catches small businesses and start-ups – jumped a robust 297,000 in December. And, the unemployment rate dropped to 9.4% from 9.8%. But, the job machine has remained relatively weak for the past year. We do expect acceleration to 220,000 new jobs per month in 2011, but even this would be less than historical recoveries have produced.

Some argue this is a new and weaker “normal,” and that it signals a fragile underlying recovery that will be permanently at risk of a double dip. Some say debt, housing and shattered consumer confidence are the cause. But, in reality, this is what we should expect when government has become so large.

Contrary to popular belief, government spending is not stimulus – it’s anti-stimulus. Look back at the US in the 1970s, or Europe (and Canada) over the past 30 years. Whenever government spending rises as a share of GDP, unemployment rises too. Government must tax and borrow from the private sector to fund itself. The larger the government, the smaller the private sector, and the fewer jobs there are.

Between 1975 and 1983, federal spending in the US averaged 21.6% of GDP and never once fell below 20%, the unemployment rate averaged 7.7%. Between 1995 and 2005, government spending in the US fell to an average of 19% of GDP and the unemployment rate averaged 5%. Lately, government spending has gone back to above 23% of GDP. As a result, the unemployment rate will remain elevated as compared to the recoveries of the past 30 years.

Unless spending is cut, the US will look more like the Euro-zone, where unemployment is now 10.1% and has been persistently higher than in the US for the past 30 years.

One difference between the US and Europe is that the Fed and the European Central Bank have different missions. The Fed is expected to help bring unemployment down *and* keep inflation low, while the ECB has one job – keep inflation down. At least the Europeans are honest. Central banks cannot offset the negative impact of government spending. Central banks can only do one thing – print money. And printing money cannot create jobs or wealth in the long run – if printing money could create wealth, counterfeiting would be made legal.

Nonetheless, the Fed remains committed to this goal and there seems to be a consensus among monetary policymakers that they should remain accommodative until the unemployment rate falls to about 5.5%.

This means rate hikes are not likely any time soon. This makes us even more confident about our bullish call on the economy and equity markets in 2011. Easy money will continue to fuel growth for many quarters into the future. Inflation will rise, but growth will come first.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
1-12 / 7:30 am	Export Prices - Dec	+0.8%	+0.7%		+1.5%
7:30 am	Import Prices - Dec	+1.2%	+1.2%		+1.3%
1-13 / 7:30 am	PPI - Dec	+0.8%	+1.1%		+0.8%
7:30 am	"Core" PPI - Dec	+0.2%	+0.2%		+0.3%
7:30 am	Int'l Trade Balance - Nov	-\$40.8 Bil	-\$39.0 Bil		-\$38.7 Bil
7:30 am	Initial Claims - Jan 8	408K	406K		409K
1-14 / 7:30 am	CPI - Dec	+0.4%	+0.4%		+0.1%
7:30 am	"Core" CPI - Dec	+0.1%	+0.1%		+0.1%
7:30 am	Retail Sales - Dec	+0.8%	+0.7%		+0.8%
7:30 am	Retail Sales Ex-Autos - Dec	+0.7%	+0.4%		+1.2%
8:15 am	Industrial Production - Dec	+0.5%	+0.5%		+0.4%
8:15 am	Capacity Utilization - Dec	75.6%	75.6%		75.2%
8:55 am	U. Mich. Consumer Sentiment	75.5	75.0		74.5
9:00 am	Business Inventories - Nov	+0.7%	+0.7%		+0.9%