

April 15, 2011

Today Washington is arguing for less than 1% of federal spending. It's like arguing the bar tab on the titanic.

David M. Walker, president and CEO of the Comeback American Initiative

Chronologically, there are three big images that stand out in my mind so far in 2011: the first is the people of Egypt packed into Cairo's Tahrir Square struggling and succeeding to end the oppression of the Mubarak regime; the second is the tsunami overtaking towns on the coast of Japan and literally wiping out lives and families and friends; and the third is our elected leaders in Washington performing absurdist political theater about a looming government shut down.

When I first wrote these images down, my immediate reaction was that sometimes, in light of the real struggles of humanity, it is just embarrassing to watch the machinations of our federal government. (Sometimes it is not even fun to be cynical!) But as I pulled back and viewed the images together, I could see that the characteristics displayed by our government were as valid, in their time and place, as the images from Egypt and Japan as illustrations of the broader human condition. When viewed as a group, I see many of the pieces that make us who we are: the desperation and hope in risking your life to change your world, the determination and faith supported in a common purpose with others, the jubilation and disbelief in overcoming seemingly insurmountable obstacles, the fragility and tragedy in having lives swiftly and senselessly taken, the shock of tragedy and of surviving in a world so suddenly changed, the lust and glee in wielding power, the arrogance of obfuscation and manipulation of truth, and the wisdom in the design of institutions to help protect individuals from the volatile nature of humanity. It's been a busy year – already!

When I focus on the debt situation that our federal government was supposedly fighting over, I want to say, "Stop screwing up a good thing!" We are a wealthy country that has been over-committed by our government in terms of current financial debt and future unfunded financial commitments. We have the resources to solve all of our big issues: spending/debt/taxation, a social safety net (including medical care), energy/defense, education, environmental protection, infrastructure, etc. What will jeopardize our future is continuing to spend and cut taxes without regard to debt (and that is a non-partisan comment!). To our politicians, I would emphasize that having a difference in opinion on the role of the federal government, on how to prioritize spending or on how to extract taxation does not preclude finding a balanced path. And to those special interests who have been feeding at the trough of our government's over-commitment, I would recommend that promoting true equality of opportunity for all (in its many forms) is a worthy policy goal.¹

Turning more specifically to our economy, our federal government's debt issues could have a number of real world effects before the end of 2011. First, we remain a country enmeshed in deleveraging from a consumer/housing debt binge. While the US economy is indeed in a business cycle recovery, the lackluster growth in Gross Domestic Product (GDP) and the lackluster recovery in employment are indicative of the secular hangover from the housing/debt bubble (both GDP and employment recoveries have been the worst since after the Great Depression). From where I sit, our federal government's deficit spending and accompanying tax cuts (along with the Federal Reserve's accommodative monetary policy of low interest rates and "quantitative easing"ⁱⁱ) have definitely helped support the recovery to date. Particularly, the early fiscal aid to the states helped them to delay or reduce their necessary budget cuts.ⁱⁱⁱ Now, with the federal government's previously enacted stimulus spending coming to an end, and with the federal deficit and debt levels creating a heightened political debate and polarization around stimulus spending and tax cuts, it is unlikely that there will be any further acceleration in federal spending or any further reductions in federal taxes. In the 3rd and 4th quarters of this year, we will find out (all else being equal) whether our economic recovery has reached a self-sustaining momentum. Second, depending on the nature of the debate and of actual spending and taxing outcomes around our short-term and long-term federal debt trajectories there could be either positive or negative economic effects. Given the fragile nature of the recovery, consumer, business and investor reactions to those developments will all play a critical role in our economy's overall direction.

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Finally, as the world continues on its voracious path through 2011, and we move through the many events in our lives, large and small, we at Peak will continue to do our best to support you in defining and meeting your financial needs and aspirations. We appreciate your business.

John McCorvie, CFA

ⁱ Last week I went to the Conference of World affairs at CU here in Boulder to hear Gigi Ibrahim speak about what real political will is (Gigi is a 24 year old Egyptian/American, political activist who helped plan the protest in Tahrir Square and ended up participating in an 18 day revolution – see [Time](#) magazine cover, 02/28/11). She downplayed political oppression as the catalyst in the Egyptian uprising and emphasized the rampant corruption, crony capitalism and the general lack of economic opportunity for the majority of Egyptians to provide for themselves and their families (with a recent "how to" revolution example from Tunisia). In response to questions about the hard work ahead, she presented an optimistic long-term view, saying she believed the key was to give the people a real voice in their government and to keep a separation between government and religion as well as a separation between government and business, and to foster equality of opportunity. (Indeed!)

ⁱⁱ In an effort to support monetary growth, the Federal Reserve has had two official stages of "quantitative easing" so far (the 2nd is currently known as "QE2"). In the first round, started in November 2008, the Fed purchased approximately \$2.1 trillion in mortgage backed securities, and in the second round, slated to end this coming June, the Fed has been working on purchasing \$600 billion of Treasury Notes/Bonds.

ⁱⁱⁱ As the federal government stimulus dollars come to an end, state budget cuts have accelerated and have become a material economic drag – including adding to the unemployment numbers.