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John Dessauer's market review and update as of Wednesday December 2, 2015

When it comes to competition in the private sector, U.S. politicians are all for it. But, when it comes to competition between governments, U.S. politicians do everything in their power to stop it. The flap over corporate inversions is the latest in our government's war on competition from other governments.

Pfizer, NYSE, PFE, $32.80 has agreed to merge with Allergan, NYSE, AGN, $319.76. The merger has a $160 billion value and will create the world's largest pharmaceuticals company. What has American politicians upset is that the new company will be headquartered in Ireland, where the corporate income tax rate is 12.5%. The U.S. top federal corporate income tax rate is 35%. When state corporate taxes are included, the top U.S. corporate income tax rate rises to 39.3%. The United States has the highest top corporate income tax rate of any of the world's developed economies. Mergers like the Pfizer-Allergan deal are called "tax inversions." They are not new. In fact they have been going on for years. The solution for the United States is obvious: reduce the corporate tax rate and make the United States a more attractive place to do business. If our politicians got it right, the "tax inversions" might go the other way and bring businesses *into* the United States. After all, there is more to running a successful business than tax rates. In the case of Ireland, the low corporate tax rate comes along with a well-educated workforce and well-developed infrastructure, including airports, seaports, trains, roads and excellent communications facilities from telephone to Internet. The United States would not have to match the low Irish corporate income tax rate to become competitive in the global corporate market place. But instead of talking about making the United States more competitive, our politicians and political candidates are aggressively attacking American companies including Pfizer. Obviously they don't like the competition from other countries.

Donald Trump: "The fact that Pfizer is leaving our country with a tremendous loss of jobs is disgusting."

Bernie Sanders: "The Pfizer-Allergan merger would be a disaster for American consumers. It would also allow another major American corporation to hide its profits overseas."

Hillary Clinton: "This proposed merger, and so-called inversions by other companies, will leave US taxpayers holding the bag."

Pfizer responded by defending the deal. Pfizer's CEO explained that the merger would allow the combined companies to continue investing approximately $9 billion a year, mainly in the United States. He also pointed out that the combined companies have 40,000 employees in the United States and they are staying, not moving to Ireland as Trump indicated.

Mrs. Clinton should acknowledge that the combined company will continue to pay U.S. corporate income taxes on its American profits. She, along with other politicians should also stop fooling American voters by linking income tax rates with revenue collected. Sometimes lower tax rates produce more tax revenue. That is the case in Ireland right now. Corporate tax revenues are much higher in Ireland than economists expected.

The bigger picture is that by being friendly to business, Ireland fared better during the 2008-2009 financial crisis and is now rebounding so well that *The Economist* titled a recent article about the Irish Economy: “Celtic phoenix.” Here is what *The Economist* has to say about Ireland:

“Even in the depths of the slump the Irish economy nonetheless retained some formidable strengths. It continues to appeal to American multinationals as a European production base, thanks to a well-educated labor force and a low corporate tax rate of just 12.5%. Ireland is favored by pharmaceutical giants such as Pfizer and has also become a magnet for tech and so-called media firms. Apple continues to build up its activities in Cork: Dublin hosts the likes of Facebook and Google.” (*The Economist,* November 21st, 2015)

Business friendly Ireland is an example, showing that corporations - including major corporations that American politicians love to bash - help moderate the economic pain during a slump and provide the basis for a speedy recovery. The Irish economy grew at a 5.2% rate in 2014. During the first half of this year it grew at a 7.0% rate. The United States needs corporate tax reform. It is discouraging to see a leading Republican presidential candidate on the wrong side of such an important economic issue. Hopefully others will support American corporations and be able to accomplish meaningful tax reform.

On a brighter note, American consumers continue to improve their financial condition. In spite of record low interest rates, the personal savings rate rose again in October.

The bad news, at least in the short run, is that U.S. consumer spending barely rose in October. The Commerce Department said consumer spending edged up 0.1% in October, the same pace as in September. Consumer spending was running at a 3.0% rate in the third quarter. Since consumer spending accounts for two-thirds of the American economy, any slowdown is bad news for the immediate future. However, the good news is that the personal savings rate rose to 5.3% in September and 5.6% in October. That is well above the 2.5% in August of 2005. Back in the days before the 2008 economic meltdown, pessimists were fond of condemning American consumers as spendthrifts who threatened the long term health of the economy. That gloom and doom notion no longer has any merit. American consumers are behaving sensibly, balancing savings and spending.

The current healthy savings rate is all the more impressive because interest rates on savings are so low. In the late 1970s and early 1980s the personal savings rate reached 12%. But, in those days savings earned double digit interest rates. It is one thing to pileup cash at 10%+ interest and quite another to add to savings when interest rates are near zero.

Financially healthy consumers are a major plus for the U.S. economy over the long term.

The major stock market indices have been treading water, waiting for a December interest rate increase.

Stock markets around the world have been trading in a narrow range. The vicious terrorist attacks in Paris shocked investors for a day or two. But markets quickly recovered. Investors at home and abroad are waiting to see if the U.S. Federal Reserve will raise interest rates this month. Odds now favor a mid-December interest rate increase of 0.25%. The question is: how will markets, especially currency markets, react to an interest rate increase? Stock markets will likely take a modest interest rate increase in stride. Currency traders most likely have anticipated an interest rate increase. The bottom line is that the long anticipated interest rate increase will likely be a nonevent for financial markets.

I will have the next market review and update for you one week from today on Wednesday December 9, 2015.

All the best,

John Dessauer