John Dessauer Investments, Inc.

John Dessauer's Outlook

May 2013

Stocks and the Annual Spring Economic Slump

Quarterly earnings reports are dominating the financial headlines. They cover a lot of this issue as well. There are 18 company reviews in this issue. Five are outright buys. A few are rated hold and most are rated buy below a specific price target. There is exciting news for shareholders of **GlaxoSmithKline**. The company is shedding non-core businesses. We may get a windfall in the form of a special dividend or shares in a spinoff. Take a look at the report and the others.

The broad stock market averages have been quite calm. So far we have not seen the expected 5%-10% correction. However, there has been a good deal more volatility in individual stocks. The selling has not been sustained, just enough to push some stock prices down sharply for a day or two. This looks like the old, familiar "sell on good news" investing strategy. Profits generally have been in line or better than expected. Profit growth has slowed. It is running at a 4%-6% rate, down from the strong double digit growth rates during the earlier stages of the recovery. The current profit growth rate looks to be sustainable and is enough to keep stock prices in an upward trend. Stocks remain the best asset class for investors.

Pessimists sounded the alarm when the IMF slashed its growth forecast for the U.S. economy.

Last month economists at the IMF (International Monetary Fund) revised their forecasts for economic growth in 2013. For the global economy they now expect growth of 3.3%, down from their 3.5% estimate in January. The estimate for the U.S. economy was revised down from 2% to a scant 1.9%. The disappointing 0.4% growth in the final quarter of 2012 surely influenced that revision. The combination of anemic fourth quarter growth

and the IMF's downward revision provided fuel for the pessimists. They have been warning of a new U.S. recession or worse. According to their thinking the U.S. economy is headed either for a new nastier recession or the Federal Reserve will throw so much more money at the problem that destructive inflation will be inevitable. The sub-par recovery, they say, has drained resources to the tipping point. One more political fiscal misstep and the economy will spiral down, out of control. This current pessimism has produced best-selling books, and popular newsletters full of radical investment advice. Doomsday predictions seldom come anywhere near reality. Optimism almost always triumphs in the end. Never-the-less, for as long as I have been writing, I started in 1980, doomsday scenarios have been the most popular. Pessimism sells more books and newsletters. This time is not likely to be different. Next year we will look back and realize that the popular pessimism was just plain wrong.

The recovery has been considerably slower than recoveries from past deep recessions. In addition it has been uneven. Some sectors, housing and manufacturing, for example, have been doing much better than others. Suffering at the individual level has also been wider spread and more intense than in past recoveries. The persistent high unemployment numbers don't tell the whole story. New jobs are too often at wages far below pre-recession levels. There are millions who have been out of work more than six months and still cannot find a job. The slow recovery means that job creation is not running at a pace fast enough to keep up with labor force growth. There is plenty to complain about and plenty to worry about. But, as dismal as the situation may seem, it does not support the doomsday claims of the pessimists. On the contrary, there are sound reasons to be reasonably optimistic about the outlook for growth at home and abroad.

China

For the first quarter, China reported growth of 7.7%, down from 8% last year. That report was enough to scare investors. Stocks dropped on fear that the Chinese growth engine might be slowing too much. The official Chinese government growth target for this year is 7.5%. The IMF kept its 8% estimate in the April review. It should be obvious that export driven annual double digit growth is not sustainable, not even in China. Slower growth is inevitable.

For years western economies have complained bitterly about China's fast, export dependent growth. Economists warned that sustained double digit growth would end badly, in a burst of destructive inflation. Business competitors and politicians argued that China's currency manipulation was unacceptable and threatened retaliation. Fortunately, China understood that fast, export-driven growth was unsustainable and began a policy of currency appreciation some time ago. The recession of 2008 forced China to accelerate the pace of economic change. Over the past few decades China has done what was thought to be impossible, gone from a nation riddled with abject poverty to a job creating wonder. Hundreds of millions of real jobs have been created. However, China needs hundreds of millions more real jobs and cannot tolerate rising unemployment. The 2008 recession caused a slump in China's export industries, threatening a rise in unemployment. In response the Chinese government has orchestrated a dramatic shift in its economy. In the past three quarters services have been a greater contributor to GDP than industry. Consumption, while still a much smaller part of GDP than in the U.S., made a bigger contribution to first quarter GDP growth than did investment. These two trends reinforce each other. Services are more labor intense than industry, which puts upward pressure on wages. In turn higher wages mean more consumption. China may be growing at a slower pace, but the emerging Chinese economy is on track to be a long term sustainable growth engine for the global economy. A Chinese economy growing at a 7.5% rate based on a balance between exports and domestic consumption is a far better growth engine than the old export driven double digit growth engine.

Europe

Richard Hoey, chief economist for BNY Mellon has this to say about Europe: "We do expect that overall economic activity should stop declining in Europe overall about midyear 2013, marking the technical end of the European recession. However, we expect a gradual saucer-shaped bottom to European economic activity over the course of this year, rather than the V-shaped pattern usually seen at the end of cyclical recessions."

Richard Hoey has an excellent command of economics around the world. He pays close attention to details in faraway places. He is far more likely to be right about Europe than the pessimists.

The United States

Some economists were disappointed with the 2.5% growth rate in the opening quarter. They were looking for growth of 3% or more. However, a growth rate of 2.5% under the circumstances looks pretty darn good. Remember that on January first the payroll tax rate went up, tax hikes on the "rich" took effect and sequester fear was being encouraged by the President and many economists. The fact that consumers did not buckle and stay home is very encouraging. Likewise, the political response to the air traffic delays is encouraging. If continued, long delays in air traffic would hurt the economy.

There is an antidote to the sequester, one that will likely keep consumers spending. The economic impact, overall, from the sequester is estimated at $85 billion. While that is tiny compared with overall federal spending and the U.S. multi-trillion dollar economy, it could, as we saw with the air traffic delays, hurt the private sector. The antidote is falling prices for gasoline. Gas prices are down and likely to fall further. If the gas price falls below $3.40 a gallon, the savings for consumers over the course of this year would be more than $80 billion.

Researchers at Capital Economics recently wrote about falling gas prices: "As a result, economic growth might not be as bad as we initially feared."

This does not mean the U.S. economic recovery will suddenly advance at a much faster pace. It means the government spending cuts are not going to push the economy back into no-growth or recession.

Richard Hoey has this to say about the U.S. economy: "We expect a "Labor Day inflection point" from the 2% growth rate of recent years to a new cyclical growth rate of 3% or more. This would be an important "Two Percent to Three Percent Transition" in the growth rate of the U.S. economy. However, it is unlikely to occur until late 2013."

My conclusion, be patient. Odds are the U.S. will muddle through the sequester and new higher tax rates. If Richard Hoey is anywhere near right, stocks will end this year higher than they are now.

NEWS AND VIEWS ON OUR COMPANIES

AT&T, NYSE, T, $37.30, reported first quarter profits that were exactly what most analysts expected. AT&T earned $0.64 a share in the opening quarter. The stock fell on the news because Revenue dropped 1.5% and AT&T added far fewer new Customers than rival Verizon. In the first quarter Verizon added 677,000 new customers, while AT&T added 296,000. The main reason for the difference is network technology. In an effort to catch up AT&T has been upgrading its network to a technology called long-term evolution or LTE. Chief Financial Officer, John Stephens said that by year end AT&T will have nearly 90% of the LTE build-out completed. Wall Street analysts are looking for 2013 earnings of $2.50 a share. The $1.80 per share annual dividend provides a yield of 4.9%. There is little risk in the stock. There also is little room for capital gains until the LTE technology has been completed and proven as a competitor. I rate AT&T a buy below $35.

Bank of America, NYSE, BAC, $12.38, reported a much improved opening quarter, but missed analysts' expectations. Earnings per share in the first quarter were $0.20, a significant improvement over last year's $0.03 a share. However, analysts were looking for $0.22 a share. Net revenue rose 5.5%, but adjusted revenue fell 8.4%. Bank of America is still struggling with mortgage related issues. They are overwhelming improvement in the wealth management business. The U.S. economy, housing in particular, is improving. Over the coming year or so Bank of America will resolve the mortgage related issues. Meanwhile, I rate the stock a hold.

Cheesecake Factory, NASDAQ, CAKE, $39.60, had an excellent opening quarter that comfortably beat analysts' expectations. CAKE earned $0.478 per share in the quarter. That was up 27% from last year and $0.05 better than the average analyst's estimate. Excluding super storm Sandy, comparable store sales were up 2%. Expansion plans call for 8-10 new stores in the United States this year. CAKE is also expanding internationally through licensing agreements that cost CAKE nothing in the way of investment. Management has raised 2013 earnings guidance to $2.12-$2.18 a share. Argus Research has a 2013 estimate of $2.20 and a 2014 estimate of $2.48. The long term average P/E is 17, but the average for the restaurant group is 19. Based on the midpoint of management's 2013 guidance, the stock is now trading at almost a P/E of 19. Applying a 19 P/E to the Argus 2014 estimate of $2.48 indicates a stock price of $47. The annual dividend of $0.48 (yield 1.2%) is likely to be raised. CAKE is clearly doing very well and has a clear growth strategy. Buy CAKE below $40.

Citigroup, NYSE, C, $46.82, reported a better than expected first quarter. Earnings per share, excluding a special accounting item, were $1.29, 30% better than a year ago. That is also considerably better than the $1.17 analysts were expecting. Trading and investment banking accounted for virtually all the increase. Revenue rose a more modest 5.7%. Argus Research has a $4.45 per share full year 2013 earnings estimate. In light of the better than expected first quarter, that probably will be raised. Standard & Poor's research has a $4.70 per share estimate for this year. Citigroup is clearly making progress, but is still struggling with distressed and unwanted assets and is a long way from sustained growth and predictable profits. I am keeping a hold rating on Citigroup.

General Electric, NYSE, GE, $22.27, reported a better than expected opening quarter of 2013. Earnings per share, excluding special items, were $0.39, up 15% from last year's $0.34 a share. Analysts were looking for earnings of $0.35 a share. The stock fell sharply, not because of the first quarter, but because management warned that Europe remains a challenge for GE. While that introduces some uncertainty, the consensus earnings estimate for all of 2013, at $1.67, looks to be achievable even with difficult market conditions in Europe. The dividend at $0.76 a share is secure and provides a current yield of 3.5%. The stock at 13 times 2013 earnings estimates is an attractive long term investment. However, given the uncertainties my advice is to buy GE on any dips below $20.

GlaxoSmithKline, NYSE, GSK, $52.42. There is exciting news from Glaxo. No, it's not about the first quarter results. They were as expected. Sales were down 3% and per share profits were down 6%. The first quarter sales and earnings were actually quite good, but last year was even better making the comparison difficult. Profits this year will likely be $3.60 a share, about the same as in 2012. The dividend has been increased 6%. That will increase the dividend yield to 5.7%. Without the news, Glaxo is a low risk, attractive, long term investment with an above average dividend yield. There are two parts to the exciting news. First, Glaxo will sell its two drink brands, Lucozade (a series of energy and sports drinks) and Ribena (British market fruit drinks). The proceeds are expected to be 2-2.5 billion British pounds ($3-$3.8 billion). While management has not said what will be done with the proceeds, the expectation is that they will be used to benefit shareholders, probably through a special dividend. Second, Glaxo plans to create Global Established Products portfolio. The portfolio will include over 50 brands, with annual sales of 3 billion pounds. While there are no more

specifics at this point, analysts speculate that this portfolio could be sold or spun off to shareholders. Glaxo shareholders may be in for a windfall in the coming twelve months. Glaxo is a buy.

Halliburton, NYSE, HAL, $41.57, is attempting to negotiate a settlement of claims arising from the Macando Gulf oil spill. While insisting Halliburton did nothing wrong, CEO David Lesar says a settlement on a reasonable basis is in the best interests of shareholders and the company. The company set aside a $1 billion pretax charge in the first quarter to cover settlement costs. Halliburton's most recent settlement offer includes both cash and stock. As a result of the reserve, Halliburton reported a loss for the first quarter. Operating results were quite strong. International sales were up 21% compared with the first quarter of 2012. That was better than Schlumberger and Baker Hughes. Halliburton's profit margin in the quarter also was better than Schlumberger or Bake Hughes. Excluding the special charge, Halliburton earned $0.62 a share. That was $0.05 better than analysts expected. The average earnings estimate for all of 2013 is $3.00 a share. In light of the strong performance in the first quarter, that will likely be raised. Argus Research has a stock price target of $48. Morningstar's target is $50. Both are in line with the stock's long term average P/E. Halliburton is a buy.

Intel, NASDAQ, INTC, $23.76, reported first quarter revenue slightly better than expected, and earnings per share in-line with analysts' expectations. Intel earned $0.40 per share (down 17% from a year ago) on revenue of $12.6 billion. Cash generation in the quarter was $4.3 billion. Intel spent $1.1 billion on dividends and used $533 million to buy back 25 million shares. Share buy backs are helping earnings per share during this time of a PC sales slump and the transition to new 14nm technology. Wall Street has the stock rated as a hold with 2013 earnings estimates around $1.90 a share. I expect the share buy backs to continue in this quarter, and for the rest of this year. That makes the $1.90 earnings estimate look achievable even if there is no rebound in PC sales. Intel is the world leader in providing chips for a wide range of technology products and systems. The company generates huge amounts of cash. The dividend is safe and the yield at just over 4% is very attractive. The next earnings growth cycle is likely to begin later this year. I rate Intel as a buy.

Johnson & Johnson, NYSE, JNJ, $85.58, reported first quarter profits of $4.1 billion, or $1.44 a share, excluding litigation and acquisition related expenses. That was $0.04 better than analysts expected. Revenue also

was better than expected at $17.5 billion, up 8.5% from the year ago quarter. Johnson & Johnson has not fully recovered from problems at some of its plants. The company has recovered from product recalls and is nearing the end of manufacturing challenges. Johnson & Johnson is very profitable and generates huge amounts of cash, more than 20% of sales. That has funded fifty consecutive years of dividend increases, which are very likely to continue. Both Argus and Standard & Poor's estimate 2013 earnings at $5.45 a share. The stock at just over 15 times earnings with a dividend yield of 2.95% is attractive as a long term investment. However, I would be patient and buy more JNJ on any dip below $80.

Microsoft, NASDAQ, MSFT, $32.61. Much maligned Microsoft delivered respectable results for its third fiscal 2103 quarter. Earnings per share were $0.72, up 20% from last year's third fiscal quarter. Adjusting for promotional sales, revenues from Windows were flat. That is remarkable given the steep decline in PC sales. Earnings estimates for this year, which ends June 30, have been $2.75 a share. They will likely be raised to at least $2.85, thanks to the better than expected third quarter. From a stock valuation point of view, the estimates for fiscal 2014 are coming into sharp focus. The consensus for the new fiscal year that begins July first was $3.10. That was before the recent third quarter earnings report. I expect fiscal 2014 estimates to be raised to $3.15 a share. Microsoft, in my opinion, deserves more than a 10 P/E. I rate the stock a buy. The 3% dividend is attractive. I see a stock price of $35 in the coming twelve months.

Nokia, NYSE, NOK, $3.32, reported good news and bad for the opening quarter of 2013. The good news was a quarter over quarter, 27% jump in sales of Nokia's new Lumia smart phones. Nokia had some supply issues in January. Sales were stronger than expected leaving some dealers' with empty shelves. That has since been fixed. Lumia sales this quarter may deliver an even better showing. The bad news is that sales of inexpensive cell phones in emerging markets fell sharply. Nokia blames competition and seasonal patterns and says there will be a range of new cheaper cell phones available soon. From the final quarter of 2012 to the first quarter of 2013 Nokia's cash increased by 100 million euros. The bottom line is that Nokia is still in the game, and has a chance at a full recovery. My rating on Nokia is hold.

Novartis, NYSE, NVS, $73.74, reported a 6.7% increase in first quarter profits. New products and emerging markets were major contributors

to the growth. Earnings per share were $1.32, $0.04 better than expected. Novartis is a unique pharmaceutical company. Novartis is diversified providing generic drugs, eye care, branded drugs, consumer health, vaccines, and has a leading position in developing cancer fighting drugs. Over the last several years Novartis has been a steady contributor to the performance of our portfolios. That is likely to continue this year and next. Standard & Poor's estimates full year 2012 earnings of $5.36 a share rising to $5.80 in 2014. Standard & Poor's rates the stock as a hold at this price. The long term average P/E is 14.5. Over the past twelve months the P/E has been above 15. The stock is up roughly 30% over the last year. After that sterling performance, Standard & Poor's conservative rating is understandable. However, the strong first quarter indicates that earnings estimates may have to be revised upwards. Twelve months from now Novartis could be $85-$90. I rate the stock a buy below $70.

Pepsico, NYSE, PEP, $82.65, delivered better than expected first quarter results, and is on track to achieve its 2013 goals. This year Pepsico management sees a 7% gain in earnings and will deliver $6.4 billion to shareholders through dividends and stock buy backs. Pepsico earned $4.10 a share in 2012. Applying the management's 7% guidance, points to earnings of $4.39 a share this year. Morningstar estimates $4.40. Argus Research has a $4.45 estimate. Analysts agree that Pepsico's global snack foods business is a crown jewel, capable of sustained long term growth. They disagree on a current stock price target. The reason for that is the swing in P/E for Pepsico over the last several years. Before the 2008 crisis, Pepsico was consistently valued at a P/E of 20, or slightly higher. In the stock market plunge of 2008-2209, the P/E fell below 15. The past two years the P/E has been around 16.5. Based on that recent history, Morningstar has a $75 stock price target. Argus is more optimistic with an $82 stock price target. My view is that over the next year or two Pepsico will head back to the old, long standing 20 P/E. Two years from now the stock should be well above $90. My advice is to buy Pepsico on dips below $80.

Philips Electronics, NYSE, PHG, $27.79, reported first quarter earnings of EUR 0.18 ($0.23). That was down 10% from a year ago. Organic year-over-year sales growth was plus 1%. Profit margins in the quarter rose to 5.8%, a significant improvement from the 3.4% in last year's first quarter. Management says weakness in Europe and slow growth in the United States are significant challenges. As a result management is cautious on the outlook for sales and profits in the first half. The dividend at EUR 0.75 ($0.95) is

payable in June and provides a yield of 3.5%. Philips is making progress with its restructuring program. The EUR 2 billion stock buyback program is 86% complete. Morningstar has a $34 stock price target. I rate Philips a buy below $30.

Rite Aid, NYSE, RAD, $2.60, has turned one corner, but still faces challenges. For the fourth quarter of fiscal 2013, Rite Aid surprised analysts and investors with a per share profit of $0.13. A year ago Rite Aid reported a fourth quarter loss of $0.48 a share. That is a remarkable turnaround. For the full 2013 fiscal year, Rite Aid had a profit of $0.12 a share. Management says that this year, fiscal 2014, the results will be a profit of $0.04 to $0.20 a share. Rite Aid has turned the profit quarter. This is very good news. It gives us confidence to hold on to our Rite Aid shares. I am reluctant to start buying, because the balance sheet still has too much debt. Net long term debt fell from $6.1 billion at the end of fiscal 2012 to $5.9 billion at the end of fiscal 2013. With the company now profitable and positive cash flows growing, the pace of debt reduction should be somewhat faster this year. However, it will take several more good years to bring the debt down to a comfortable level. I rate Rite Aid a hold.

SEI Investments, NASDAQ, SEIC, $28.07, reported first quarter operating earnings of $0.33 a share, in line with analysts' expectations. Profits were up 18% over the first quarter of last year. Revenues were up 14%. Assets under management grew 17%. And, during the quarter SEI bought back 1.3 million shares at a cost of $36.2 million. For all of 2013 analysts expect earnings of $1.46 a share. The long term average P/E is 20, indicating a stock price of $29.20. SEI is an attractive long term investment with a takeover possibility. Buy SEI below $25.

Texas Instruments, NYSE, TXN, $35.97, is off to a good start in 2013. First quarter earnings, excluding items, were $0.35 a share, $0.04 better than most analysts expected. Revenue at $2.89 billion was at the high end of guidance, and also better than analysts expected. Management gave an up-beat outlook for the quarters ahead, saying that demand is improving. The details indicate the transition to a pure analog based business is on schedule. By next year, loss making businesses should have been wound down and profit margins should expand. The average earnings estimate for this year is $1.62 a share. For next year Standard & Poor's estimates a jump to $2.21 a share. The dividend has been increased to $1.12 a year for a 3.1% yield. The long term average P/E is 19. Last year's P/E was 17. As the

transition progresses and profit margins improve I expect the P/E to return to the 19 level or slightly higher. Standard & Poor's has a stock price target of $42. I agree. Texas Instruments is a buy.

Wyndham Worldwide, NYSE, WYN, $60.48, reported first quarter profits of $0.71 a share. That was 18% better than last year's first quarter and $0.04 better than analysts expected. Revenue increased 9% from the opening quarter of 2012. The company bought back 2.4 million shares during the quarter. All in all it was a very good quarter for Wyndham. The stock pulled back following the report. The stock had run up prior. The selling was classic "sell on good news," nothing more. For all of 2012 management says earnings per share will be between $3.60 and $3.70 a share. Looking ahead, Wyndham's business mix and strategy should produce double digit growth in earnings for at least the next several years. Standard & Poor's rates Wyndham a buy with a stock price target of $66. My twelve month stock price target is $70. Wyndham is a buy.

CLOSING THOUGHTS

At long last, after years neglecting their basic fiscal duty, the members of the U.S. Senate began serious debate on formulating a budget. This will come as a shock to all who have given up on the Senate's budget credibility. During the debate there was a vote on a non-binding resolution that would require the Congressional Budget Office (CBO) to produce a dynamic score, in addition to their usual static score, on all changes in the U.S. tax code. All the Republicans in the Senate voted for the resolution. The shock was that six Democrats also voted for the resolution. It passed 51-48. It is too bad that this debate did not get media attention, because this goes to the heart of the current fiscal divide in Washington. The 48 Democrats who voted "No" do not want more information on how effective tax changes are in raising revenue or reducing economic growth even though they know the current static accounting done by the CBO is more often wrong than right.

On January 1, 2013 the tax rate on dividends, capital gains and personal income went up for taxpayers earning more than $400,000. The result; from the third to the fourth quarter of 2012 there was one of the largest shifts in timing of income in American history. In the fourth quarter of last year personal income soared by $262 billion. Businesses and individuals did everything they could to take advantage of the lower rates in

2012. For example, SEI, like many companies, paid an extra dividend in the final months of 2012 and accelerated the 2013 dividend as well. In the opening quarter of this year personal income fell $109 billion. Obviously people do change their behavior in response to changes in the tax code.

In May 2003 the Congress cut the capital gains tax rate from 20% to 15%. Using its usual static accounting methods, the CBO confidently predicted the tax cut would reduce 2006 capital gains tax revenue from $68 billion to $65 billion. For 2007, the CBO said tax revenue from capital gains would fall from $73 billion to $69 billion. Static accounting assumes taxpayers pay no attention to changes in tax rates. The CBO's capital gains tax predictions were not just wrong, they were totally out of touch with reality. Investors reacted positively to the new lower capital gains tax rate. Tax revenue from capital gains was $109 billion in 2006 and $126 billion in 2007. Reducing the tax rate on capital gains resulted in a huge **increase** in tax revenue.

There was a similar result from the reduction in tax rates on dividends. Following the cut in dividend tax rates to 15% more companies began paying dividends. The amount of dividend income quickly tripled. Uncle Sam has collected far more tax revenue from dividends at a 15% rate than he did when rates were much higher.

Members of the House and Senate have known for a long time that the CBO's current static tax modeling routinely gets the outcome wrong. In 2005 two Harvard economists, Greg Mankiw and Matthew Weinziel studied the revenue results from tax changes and concluded that: "the dynamic response of the economy to tax changes is too large to be ignored." Why then, are so many members of Congress, mainly Democrats, so reluctant to at least look at dynamic accounting by the CBO?

Senate Budget chairman Patty Murray claims dynamic scoring is "very difficult" because it "relies on judgment calls." Mrs. Murray is right that predicting the consequences from tax changes is an inexact science. Some tax cuts promote growth and produce more revenue than others. But, uncertainty about future consequences is no excuse for holding firm on static scoring that everyone knows is more often wrong than right. Refusing to consider dynamic scoring is stacking the beltway deck against sound tax policy. That may have been tolerable political ideology decades ago, but no longer. This country faces unprecedented fiscal challenges as a result of the

globalization and the 2008 financial crisis. We desperately need to get the policy mix right. Faster economic growth is the only practical way to bring the nation's fiscal house back in order. Yes, we need more revenue, but not at the cost of economic contraction. The Senate and House members need all the information they can get and should do more than add dynamic scoring. They should pay attention to the past consequences of changes in tax rates and adopt practices that regularly monitor the consequences of future changes in tax rates.

Thank goodness for economists like Arthur Laffer. Some Senators may choose tax ideology over practical results, but they do so in full view of competent critics. Arthur Laffer is chairman of Laffer Associates and was an economic advisor to President Reagan. He is perhaps best known for the "Laffer Curve", a diagram showing how tax rates and tax revenue interact. For decades Arthur Laffer has challenged the ideology of political leaders like Patty Murray. She holds firm to the idea that cutting tax rates on business and individuals reduces tax revenue and hurts economic growth. Laffer lectures, writes articles and constantly introduces facts about what is actually happening in our economy.

In a recent article Laffer (and Co author Stephen Moore from the editorial board of the *Wall Street Journal)* wrote: "You can tell a lot about prosperity in America by observing the places people are moving to and where they are packing up and moving from. New Census Bureau data on metropolitan areas indicate that the South and the Sunbelt regions continue to grow, while the Northeast and Midwest continue to shrink."

"Among the 10 fastest-growing metro areas last year were Raleigh, Austin, Las Vegas, Orlando, Charlotte, Phoenix, Houston, San Antonio and Dallas. All of these are in low-tax, business-friendly red states. Blue–state areas such as Cleveland, Detroit, Buffalo, Providence and Rochester were among the biggest losers."

I was born in Rochester New York and now live in Naples Florida. I am positive that weather is a factor in the population shift from Rochester to the South. However, I won't dispute Arthur Laffer when he says taxes and business conditions are also very significant. He concludes: "The contrast (between red and blue states) sets up a wonderful natural laboratory to test rival economic ideas."

The Senate may be slow to change how it looks at taxes and economic growth, but outside the Beltway other political leaders are vigorously engaged in pursuit of policies that work. Long burdened with tops-down economic policies imposed by Washington, the U.S. is now shifting more and more towards a bottoms-up approach, where state and local governments have significant influence on economic policy. Economic necessity, perhaps desperation is forcing real change. The outcome is likely to be positive for the economy, voters and taxpayers.

Next issue: The June issue of John Dessauer's Outlook will be ready on Wednesday May 5, 2013.

Next weekly hotline: Wednesday May 8, 2013

All the best,

John Dessauer
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