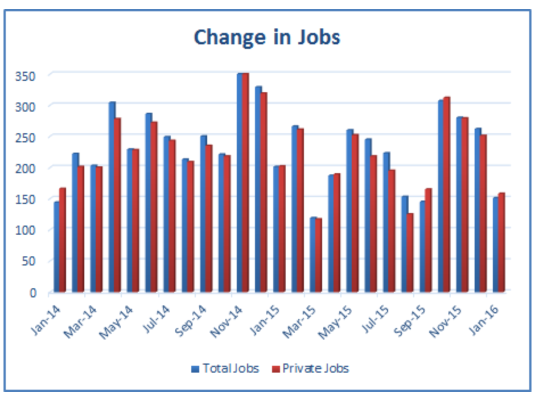
ECONOCAST™ UPDATE – February 8, 2016

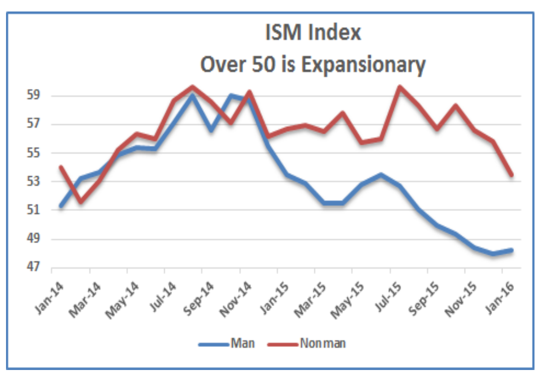
U.S. Economy – Losing Speed

The January employment report reflects the slower pace of growth last quarter. Job growth slowed to 151,000 in January down from the revised gain of 262,000 in December. Most of the weakness came in sectors that were artificially boosted by the warm December weather and by holiday hiring, including construction, couriers and temp help. If I adjust for the slowdown to these three industries in January, underlying payroll gains are about the same 200,000/month they have averaged in recent years.



Furthermore, the January jobs data are notoriously flakey due to weather and seasonal adjustment frailties. The composition of job growth was puzzling in January. For example, retail employment jumped nearly 57,000, the largest gain and its highest since November 2014. Manufacturing jobs jumped 29,000 — suspicious given the struggles in the industry. Education services employment fell roughly 39,000 in January for no obvious reason.

The ISM indices are more reliable near term indicators. The manufacturing index was about flat in January, but below the 50 mark indicating contraction. The strong dollar, weak trade demand, and low energy prices will offset gains from domestic demand. The nonmanufacturing index continues cooling. Since it accounts for 88% of GDP, this is concerning if it continues. Some of the recent weakness reflects the volatility in financial markets. However, when financial markets settle down, I expect nonmanufacturing to improve.



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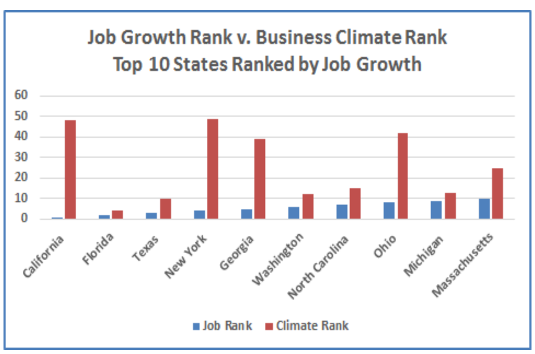
Florida Economy: Job Growth and Taxes

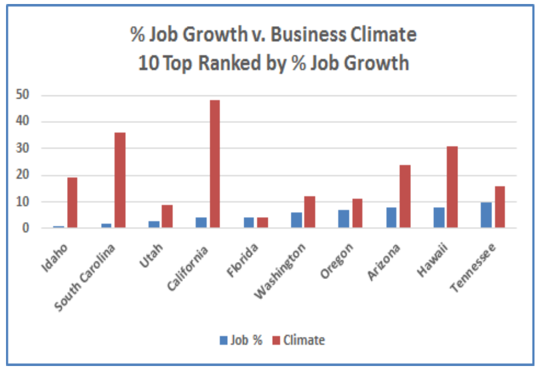
Florida's 2016 Legislative session ends March 1st. The only requirement is to pass a budget, but this is proving problematic again. In his continuing efforts to promote economic development in Florida, the Governor is insisting on a $1 billion tax cut, mostly for businesses to stimulate jobs. However, there are no data to support the contention that low business taxes promote job growth.

I compared the latest business climate rankings, published by the Tax Foundation, to the latest data for job growth in 2015. The correlation between job growth and business climate was -0.09, which is essentially zero meaning there is no relationship.

Consider the fact that California ranked 1st for job growth and 48th for climate, or that New York ranked 49th for climate and 4th for job growth. There simply is no relationship between job growth and taxation.



The same result is obtained using data for the percentage rate of job growth, instead of the volume of new jobs. The correlation coefficient is 0.06 - which again is essentially zero. On a percentage basis Idaho ranked 1st for job growth but 19th for climate. South Carolina ranked 2nd for job growth but 36th for climate, and California came in 4th in job growth with a rank of 48th for climate.



This may sound a bit counter intuitive since businesses routinely complain about taxes and often demand tax breaks. Businesses are very good at bargaining. By pitting one location against another, they can achieve lower costs than would otherwise be the case, even if a tax savings was not their original justification for moving. So, in some circumstances cutting taxes in a tactical response for recruiting purposes can be effective. But this is not at all the same thing as cutting all taxes for a whole sector of the economy as Governor Scott has proposed.

Florida is already a very low tax state. The State ranked 4th for business climate in 2016 and has routinely ranked among the top 5 best in the U.S. Clearly, Florida's challenge is not that its taxes are too high. Just as obvious is the fact that high tax states such as California and New York can have high taxes and strong job growth only if they are providing high levels of services, such as education, infrastructure, and healthcare, which businesses find attractive. Instead of cutting taxes by $1 billion, Florida would be better served by investing those funds in education, training, healthcare and infrastructure to make Florida more competitive.

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