

The Good, the Bad and the Ugly

April 2010

Who can forget Ennio Morricone's score to this classic spaghetti Western made in 1966? You barely have to nudge your memory to hear that haunting title tune. Clint Eastwood was the Good ("Hey Blondie!"), Lee Van Cleef the Bad and Eli Wallach, the Ugly, each in search of Civil War gold. Few films have been as reviewed or revered. Twists and turns took us through brutality, swindle and betrayal. In the end Clint Eastwood, the Good, stands tall...with his gold.

The quest of these three characters seems to mirror our current quest for economic prosperity. For the sake of trying to grasp some sliver of a silver lining, let's consider them in reverse order, the Ugly, then the Bad, and finally the Good.

At minimum, the Ugly represents our massive unfunded entitlement liabilities. Not long ago as a guest on David Letterman, former and probable future Presidential candidate Mitt Romney, suggested these entitlements represented a "significant liability to America's future that desperately needed attention". Funny how politicians interested in the new fiscally conservative voter movement feel inclined to talk about reigning in "entitlements" but they don't want to mention their real names... Social Security, Medicare and Medicaid.

The unfunded tab for these entitlements has been calculated at anywhere between \$25 and \$100 trillion dollars...\$46 trillion by current CBO projections. You read that right; trillions in unfunded promises are on our books...on the national balance sheet...part of our future monthly bills. The calculations for these deficits include meaningful to robust GDP growth as well as tax collections. These are not unfunded because we have yet to collect the Social Security or Medicare taxes. They are unfunded balances **after reasonable estimates of ALL future tax collections.**

A decent portion still needs to be paid to the Greatest Generation, the Korean and Vietnam War generations and finally the Baby Boomers. Who gets to make the sacrifice here? Are any of these voters willing? Not hardly. Gradually over the last few decades the notion of sacrifice has been replaced with entitlement. It is no wonder this can keeps getting kicked down the road.

To add to the Ugly we might throw in "guaranteed" government pensions and retirement health care benefits. These folks have defined benefit plans, meaning they have "guaranteed" retirements, or as one might suggest, "more" guaranteed than the private sector...you know...the one that supposedly creates real GDP. As of now U.S. state government employee pensions are underfunded between \$450B and \$3T. The difference? Aggressive investment rate of return projections get you to the \$450B figure...remember that's still \$450B underfunded.

It is far easier to change the rules for disparate voters in the private sector than it is to alienate a large block of voters like unions and government workers, which in many cases are the same. According to the BLS there are more union members working today in the public than the private sector. Now why do we need unions in government? Does government have a history of oppressing its workers?

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The Ugly is...well, just quite ugly. We have trillions in promises we can't afford even with a return to a 1999 or 2007 style robust economy. We have Boomer's with expectations that include \$250 Tom Petty concert tickets, \$40 steak dinners and Robert Parker anointed wine selections. Heck, it costs \$80 for a day ticket to Disneyland. How can Boomer's afford to entertain their grandkids?

If future entitlements are the Ugly, then the Bad must be Washington's inability to deal with them, as well as its current effort to increase them. Damn the torpedoes, full steam ahead! Guaranteed health care for everyone! Unemployment compensation in perpetuity! Everyone deserves to own a home and get a college education! It's in the Declaration of Independence, "Life, liberty and the pursuit of happiness." See...happiness is Washington's responsibility! Pass out the free loaves of bread! Just hire more "bakers" in Washington.

The Ugly may be ugly, but the Bad seems dead set on making things even more ugly! We've had 50 years or so of "entitlement creep" that we can no longer afford and now we're ready to add more entitlements. Hmm...what's that definition of "insanity"...continuing to make the same bad decisions in hope of getting a better outcome?

Anyone who thinks Washington's control over an industry as large as health care...any industry for that matter...is going to decrease costs surely deserves to be sent to Disney's ToonTown. Governments don't decrease costs. They always increase them.

The best path to promotion in government is to find a problem that needs a bigger budget for you to manage. And the bigger your budget the more you make in personal compensation. So for a government employee the route to higher personal compensation is to find ways to increase the size of your budget, to find more "problems" government must "fix". This kind of pursuit leads to increased taxes and fees and increased costs to companies under the "surveillance" of government, which increases costs to consumers. Grow government and you grow taxes and costs.

I guess we could also throw unemployment into the Bad pile. It's hovering around 10% and there's good analytics out there suggesting high unemployment is here to stay for years to come. This only increases the need for more government give away programs, meaning more government employees to manage these give away programs, all of which needs to be supported by more taxes.

Man oh man oh man oh man oh man...it's time to get some Good. Where's that Good stuff, Doug? Get me out of this Alice in Blunderland. We're tired of being stuck in the Hurt Locker. Where's the Yellow Brick Road...you know...the one paved with gold...like in 1999 and 2007? Where's Clint Eastwood's booty? Get on with the Good stuff. There's some Good out there, right? Sure there is.

The U.S. owes its economic and political success to various unique attributes that form our core competitive advantage over most every country in the world.

We seem to have the best breadth of abundant natural resources of any country. We are home to the best agriculture in the world. We possess an excellent supply of traditional fuel in coal, oil and gas,

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even in renewable energy potential. We have excellent Pacific, Atlantic and internal transportation capabilities. And not normally counted or considered, the U.S. has the best human resource talent pool on the planet.

No country has inspired so many. We are an immigrant melting pot of dreamers, aspirers and desirers. Most all of us are here because an ancestor took action to materially improve their lot in life. Supported by great natural resources our collective desire for a better life allowed the U.S. to rise to the top of world influence. There was no assurance of great success but there was assurance of opportunity and ample tools (resources) to capture that opportunity.

No country has freed so many from the bonds of institutional slavery. The collective of our immigrant value systems plus our daily interaction with people of different race and creed inspires our compassion. Few countries in the world possess a fraction of our compassion. Critics of U.S. “imperialism” surely have not considered that all our former enemies are free, and their citizens are now in possession of more individual liberty and economic opportunity than generations before them.

No country has innovated so much. From housing to food to transportation to energy to communications to health care to art, innovation explodes in the U.S. And that innovation can continue as its fertility exists within the melting pot of our population. When you put different cultures and thinking together new ideas spring forth. Why is it people keep bashing our educational system when we still lead the world in patents and innovation? The U.S. has a culture, almost a “genetic disposition”, for innovation. Book smarts is not the only attribute needed for innovation.

No country is as adaptable. We are burdened with massive entitlements and intrusion into our daily lives by government. We possess sovereign debt that would choke a whale and fiscal deficits as far as the eye can see. Our current leadership seems intent on making things worse rather than better. Even still, the U.S. is by far the most adaptable country and culture in the world. Our labor force has no problem moving from California to Texas while you’ll find few Greeks moving to Germany for a job. Our Democratic process is much more nimble than Europe, where entitlements and managed economies are more deeply seated. Americans are more flexible than any culture. Want to get us to sacrifice for the future of our children? Then just let Washington lead by example.

As in The Good, the Bad and the Ugly, the path to prosperity holds its twists and turns. It can take us through brutality, swindles and betrayals before landing us in the Promised Land. Will we end up like Clint Eastwood, with a bag of gold for all our effort? Odds are Good but timing and leadership are the challenges at this current point in the path of Adam Smith’s invisible hand. Before again finding that Good, we likely must first defeat the Bad and the Ugly.



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