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## **Dow 20K, 2% GDP Rut; Border Taxes become of Threat**

**Friday, 11:10 a.m. EST**

In contrast to Dow 10k, which was breached almost 18 years ago, when the Dow broke through the 20,000 barrier on Wednesday, it stayed above that level – at least for now. But threats are ever present. The news media had reported that Trump has warmed up to the idea of a border tax, after appearing to have rejected the concept several weeks ago.

Let's first talk about today's Q4 GDP announcement. It came in modestly below expectations at 1.9%. In fact growth in 2016, measured from fourth quarter 2015 to fourth quarter 2016 is precisely 1.9%. And estimates for this quarter are also around 2%. The economy has been stuck in this 2% "growth rut" for a long time. Although certainly not at a recession level, given the increase in jobs over the past 5 years, the US economy should have been growing at 4% or more. The reasons for the poor performance: the collapse in productivity growth and there are no signs that that problem is going away.

Earnings have been good, but not spectacular. Almost 150 S&P 500 firms have reported since Delta Airlines launched the Q4 earnings season on January 12<sup>th</sup>. Just over three-fourths of the firms have "beat the street." Guidance has run hot and cold, with the border tax threat cited as a major source of uncertainty.

Is a "border tax", specifically exempting exports and taxing imports good for the economy and the stock market? The answer is mixed. A border tax will raise the value of the dollar, but nearly enough to offset the tax itself. Those who rely on imports, such as retailers, will be hurt. Those who produce in the US and compete against importers will be helped (such as Tesla). It may be a net plus for US firms, particularly exporters. But it will be a net minus for consumers, who will see the price of imports rise. Since the US is virtually at full employment, I would say that the net effect on the economy would be negative since exporters will be accessing a tight labor market to increase output. A border tax will also give a bump to inflation, which could cause the Fed to tighten more rapidly. However, the Fed's action may be tempered by the one-shot nature of the price increase. Overall the effect on business could be mildly positive, but the impact on the equity market uncertain. If border taxes spark a trade war, the economy and the risk markets will go south.

Next week the Fed meets and there is no question that they will be on hold. But I would rate it an even-money bet on a March hike. At present, the market expects 2 to 3 one-quarter percent increases this year.