EW | ECONOCAST™ WEEKLY

ECONOCAST™ UPDATE – December 18, 2017

U.S. Economy – Tax Cuts and a Strengthening Economy

The House-Senate Conference Committee approved and published the Tax Cut and Jobs Act on Friday, and it is scheduled for passage this week. For corporations the Act cuts the tax rate to 21%, provides for full expensing of new investments for five years, and shifts taxation to a territorial basis among other things. Individuals get lower rates, a doubling of the standard deduction, and an increase in the child tax credit. But, the deduction for mortgage interest is reduced, and state and local property and income taxes are capped at $10,000. On average, households will get cuts of $1,500-to-$3,000 per year until the cuts expire in 2025.

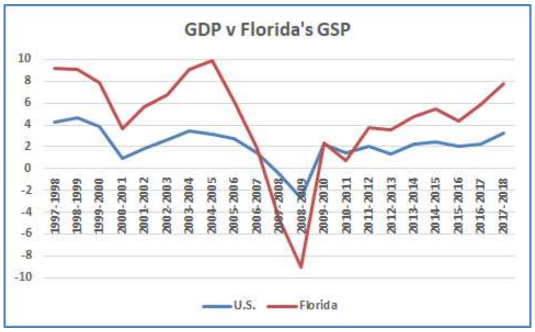
The Act will boost GDP by ¼% in 2018 and 2019 by pushing up consumption and investment. However, the timing is bad, because the economy is fast approaching full employment and has high capacity utilization. Employers already cannot fill all their job openings, so increasing demand cannot create much additional employment. Instead, most of the stimulus will push prices and wages higher. This comes when the Fed is increasing the rates, with 6 more increases planned for 2018 and 2019. Ultimately, this will result in a recession in 2020-21.

But, the near-term outlook is bright. Retail sales rose 0.8% in November with core sales up 0.8% as well. Growth was strong in a broad set of segments, with no major segments except auto dealers having monthly declines. In November, sales were 5.8% above their year-ago level with core sales up 5% for the fastest growth since 2012.

As expected, the Fed increased the funds rate for the 3rd time this year to 1.5%. The Fed confirmed its plan to raise rates at least 3 times in 2018 and again in 2019. The Fed also raised its forecast for GDP growth to 2.5% from 2.1% in part because of the tax cuts. All of this despite the fact that inflation continues running below the Fed's 2% target rate.

Florida Economy: Tax Cuts and Growth in 2018

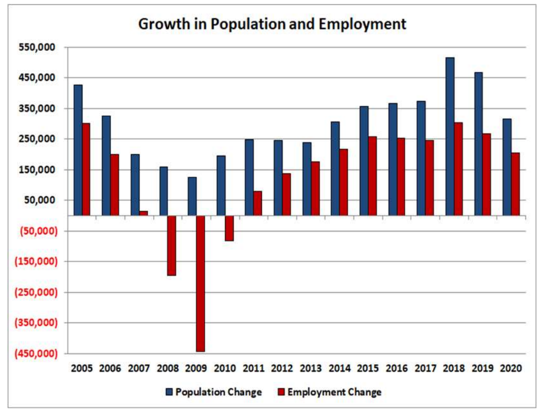
Florida's economy was already very strong this year and will boom in 2018 with the added stimulus of the tax cuts and strong migration from Puerto Rico. Consider first the close relationship between Florida's gross state product ("GSP") and GDP.



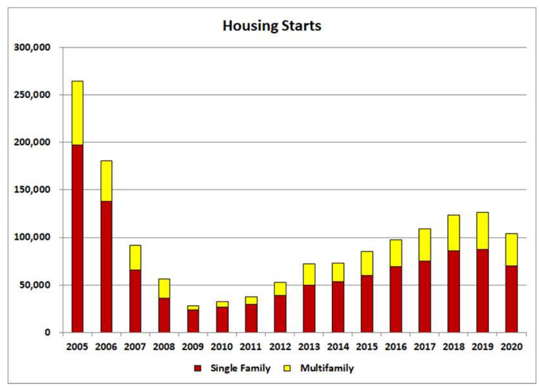
More than 88% of the trajectory of growth in GSP can be explained by growth in GDP. With GDP set to accelerate to 3.5% in 2018, GSP would receive a boost to 4.5% growth.

On top of this, 247,000 Puerto Ricans have come to Florida since October 3rd according to data from Florida's Department of Emergency Management. The influx is running at nearly 4,000 per day, and over 50,000 Puerto Ricans have already booked flights into Orlando over the upcoming two weeks. However, the counts are based only on travel through Florida airports from Puerto Rico. They do not include those who fly into other parts of the U.S. and move to Florida

This combination of stimuli will drive population growth to 515,000 in 2018 and support more than 200,000 jobs, eclipsing levels reached in 2005 and approaching all time high levels of population growth.



Housing starts will move higher, but they remain far below the past peak. Household size has increased, and it will be very high for the new migrants from Puerto Rico, so housing demand is far lower than in the past.



The upswing in GDP will foster faster growth in domestic visitors, pushing the 2018 total to 121 million. Orlando's share will increase to 65%. These gains will offset weakness in foreign arrivals that have relatively larger impacts on South Florida.