$ Investing Basics $

Evergreen Consulting Group Inc. - Richard A. Green, DDS, MBA

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Dear Reader: I would enjoy hearing from you. Spread the word about these articles. I think you and your friends will find them helpful.

– *Richard A Green DDS, MBA*

Know Enough about Money and Markets to Make Them Work for You

In this issue, I would like to encourage you to read "outside" your industry. While everybody seems to be focused on being in or out of the market (Market Timing), as a way to make up for the catastrophic losses of the past three to five years, I would suggest a little historical reading and reflection may lead to less "hysterical" responses and nervousness about the markets

I am including an article that appeared on the *Wall Street Journal's (WSJ)* editorial page of Wednesday June 11, 2003. It was written by Mr. Regan, who was President Reagan's Treasury secretary in the 1980's. Mr. Regan's article reflects his active mind up until his death, which was Monday night, June 9, 2003, and just prior to this appearing on the editorial page. I encourage you to reflect on his thought process, analysis, and future focus as he looks at the impact on "Money, Markets, and Investing" – Investing Basics!

A Reaganomic "GPS"
By Donald T. Regan

The recent debate over President Bush's tax proposal had so many echoes of the Reagan era that I could almost recite the parts of the various players from memory. Amid all the clamor, few have stepped back, as President Reagan did in 1981, and asked three basic questions: Where are we, where do we need to go, and how are we going to get there? Unfortunately, we have no GPS that could pinpoint where we are and how to navigate from here to there.

The 1981 tax debate occurred when the economy had serious ills. It was entangled in a strange phenomenon known as stagflation, a combination of slow growth and inflation that could not he accounted for by the dominant Keynesian economic theory of the time. Keynesian economists believed that slow growth. or no growth, was the cure for inflation, but somehow both were happening at the same time. Tax cuts, it was feared, would only create more deficits, stimulate more inflation and raise interest rates, already in the high

teens, further into the stratosphere.
Ronald Reagan, however, was not troubled by this state of affairs. To answer the question of where we were, he recognized that growth was held back by high tax rates and excessive regulation. As for where we needed to go, his answer was that the first priority was economic growth; other problems would take care of themselves as long as the Federal Reserve maintained a steady and moderate rate of monetary expansion. And his policy for how we were going to get there was breath-takingly simple, the government was going to get off the back of the American people by taxing and regulating less.

The opponents of Mr. Reagan's program were saying many of the same things they said in response to the Bush tax cut proposal: We can't cut taxes, it will increase inflation and raise interest rates; deficits are already too high; tax cuts will only deprive the government of the revenues it requires to meet the many needs of the American people.

Thanks to President Reagan, we know a lot more today, although it seems that many in Congress didn't get the memo. We know that tax cuts spur economic growth by improving incentives to work and invest and by making more money available for new ventures and small business, where the real job growth occurs in our economy. There are many examples of this in recent history, from the Kennedy tax cuts of 1962, through the Reagan cuts of 1981 and 1986. We also know that deficits do not cause inflation or cause interest rates to rise. Although the deficits during the Reagan period were higher (as a percentage of gross domestic product) than the deficits projected today, interest rates declined after the Reagan tax plan was adopted.

As I interpret Mr. Bush's tax program, I think I see that he has tried to answer the same three questions that President Reagan always kept in mind, even though the economic problems he faces are different. We are not in a period of inflation. Quite the opposite, inflation and interest rates are at historic lows. We are, however, in the midst of a slow economic recovery, in which jobs are not coming back as quickly as we might have hoped. In fact, the whole economy is changing right before our eyes, and will continue to change. Unskilled or semiskilled jobs are going overseas, and jobs involving knowledge and skill-technology, specialized services, finance, health care, energy, entertainment and communications, are the growth areas here at home.

The Bush tax program is ideally suited to address this new economy. Whereas Mr. Reagan saw generalized economic growth as essential, the Bush plan has both a simulative component to start the engine and a long-term component to advance the process of moving our economy into the new areas of future growth. That's what the dividend tax cut and the cut in the capital gains rate are all about. As companies increasingly pay out dividends, and pay less of a penalty for making profits, investors will have funds to invest in new ventures. Our economy, already the most dynamic in the world, will continue to change and grow in response to the growing skills of the American people, particularly in the service sector.

President Bush should also aim to extend his tax-relief vision beyond financial transactions such as dividends and capital gains. In a knowledge economy, education and learning are real factors of production. Americans who add to their knowledge and skills are, then, adding to the stock of the nation's productive assets. The president's next tax bill should recognize this with tax credits for individuals that match the investment tax credits that have been available to business. That's a program that assesses where we are, where we need to go, and how we are going to get there.

Dow 9300

Despite signals from equity markets that the worst might be behind us, concerns about the economy in general and the troubling unemployment situation weigh heavily on the minds of Americans. There are some encouraging signs, yet the present skittishness seems strange, in some respects, to this observer; after 13 rate cuts, through the end of July, the Federal Reverse Board still maintains an accommodative position. There seems to be good news from corporate America as well: reported corporate earnings have exceeded expectations and productivity growth is strong. Estimated second quarter S&P 500 earnings will be higher than the previous year with two-thirds of the S&P 500 companies that have reported earnings so far, have beaten their estimates.

So, you ask, why is it that the public is not feeling more jubilant about the recovery, especially my patients? The most obvious answer continues to be the national unemployment rate, 6.4% in June and 6.3% in July, especially if you are living and practicing in a town that has felt the direct effect of recent massive layoffs. How does the unemployment rate impact overall perceptions of the economy? Even in periods of unemployment, the vast majority of workers keep their jobs. Thus the effect of high unemployment on consumer confidence comes from an uncertainty about one's own job security, and/or consumer sympathy pain for friends, family and acquaintances that are out of work.

The changes in the unemployment rate filter through to the public and your patient base. In many ways, as the "Market Rotates" and industries perform better or worse than others on a relative scale, so to does your patient-base connected to those industries. Be sensitive to these rotations as you generate "appropriate" treatment plans with your patients. Because there is a high correlation between the actual unemployment rate and the percentage of Americans (patients) saying they know someone who has recently been laid off or fired. News of improved corporate earnings will ring hollow with your patients until they start to see, and feel, employment figures catching up.

Unemployment will continue to move in a positive direction as industries and individual companies gain confidence in consumers' intentions and inventories become smaller. Looking at the last twelve months, the Dow and S&P 500 are up over 30%, and NASDAQ is up over 40% with semi-conductors leading the way, up well over 70%. The underlying fundamentals seem to be supporting these moves and point to continued movement for 2004, unless there is a major devaluation of the dollar.

Oh, don't misunderstand me, there will be plenty of ups and downs but the trend should be basically up. As a "long-term" investor – stay with your discipline: Regularly keep putting money away, thereby accumulating your wealth, over time.