OCT 12, 2017 @ 12:00 PM

The Economic Impacts Of Recent Hurricanes And Tax Reform

Mark Avallone, CONTRIBUTOR
I help people on their path to Financial Freedom. FULL BIO
Opinions expressed by Forbes Contributors are their own.

The release of the September jobs report, which showed a net decline of 33,000 jobs, has caused some concern that the U.S. economy might be slowing. However, a closer look at the data shows otherwise.

In the same report, we saw the nascent trend of wage growth continuing. For the past twelve months, average hourly earnings have increased 2.9%. We've also witnessed a decline in the unemployment rate to 4.2% and a labor-force participation rate holding steady at 63.1%. These are signs of a strong economy. The weak jobs number, however, is more reflective of the short-term economic impact of hurricanes Harvey and Irma. Major hurricanes can have a significant short-term impact on monthly economic data, and that is one reason why looking at long-term trends can yield a more accurate analysis. This is especially true of Irma and Harvey, which have shut down large portions of Texas and Florida, two of our country's largest economic engines.

Boats are pushed up along the shore line after hurricane Irma passed through the area on September 19, 2017 in Marathon, Florida. The process of rebuilding has begun as the Federal Emergency Management Agency has reported that 25% of all homes in the Florida Keys were destroyed and 65% sustained major damage when they took a direct hit from Hurricane Irma. (Photo by Joe Raedle/Getty Images)

Many service industry jobs have been impacted, especially those in hospitality, fast food, casual dining, and retail. Meanwhile, locals are focusing on rebuilding and repairing. These latter activities will eventually bring in jobs and economic activity, possibly making these natural disasters a net booster of economic activity in 2018.

In Puerto Rico, Hurricane Maria has left complete devastation. The entire island will need a massive infrastructure rebuilding program. Who will fund this effort has been the cause of debate, but the situation is so dire that politics will have to take a back seat. The images of destruction and personal suffering will compel our legislators to finance the rebuilding. However, don't look for Congress to bail out Puerto Rico's existing $73 billion worth of debt. If Congress were to show that kind of generosity to Puerto Rico, a lot of mismanaged U.S. cities and states would likely march on Washington asking for the same largess, so bailouts are untenable.

As noted earlier, despite these massive natural disasters, the U.S. economy is growing and shows few signs of weakening. This raises the question of why we need tax cuts now. To be sure, tax reform is needed to help American corporations compete with lower-taxed foreign competitors, and there are some loopholes that many agree are better off closed. On the individual side, the benefits of cutting taxes and putting more money in the pockets of workers is also appealing. However, tax cuts are usually a very powerful tool that Congress can use to help boost a slow economy, and historically we've seen tax cuts when the economy slows, not when it is expanding. Even so, Republicans, perhaps wary of the potential end of their one-party rule and desirous of 3%-plus GDP growth, are intent to deliver at least one major legislative victory. If tax reform isn't possible, a simpler bill that just cuts taxes could result; this may stimulate the economy but could also exacerbate the budget deficit.

One wild card that legislators may be overlooking is the Federal Reserve Bank (the Fed). Cutting taxes now, during a period of economic expansion, may simply embolden the Fed to accelerate its monetary tightening. And while our current economic recovery isn't roaring like the 1980s and 90s, it has been gradually expanding for almost 9 years. In fact, the economy has been strong enough to encourage the Fed to slow down its bond purchase programs and raise the Federal Funds rate. These Fed actions should have the net effect of raising interest rates, which can slow economic growth. If the Fed more aggressively tightens monetary policy while Congress tries to stimulate the economy with tax cuts, these two massive forces could collide and potentially negate each other. Then we will be left with our current scenario: strong corporate earnings, reasonable global economic growth, relatively low energy prices, low inflation, low unemployment, and rising wages. The confluence of these favorable market conditions may explain why the stock market continues to look beyond the headlines and news noise in its record-setting upward climb.

Contributor's Bio

Mark Avallone is the author of Countdown To Financial Freedom, and founder and President of Potomac Wealth Advisors, LLC a financial advisory firm serving clients through holistic financial planning and wealth management. Avallone writes on a variety of financial topics, and his contributions have appeared in the Wall Street Journal as well as in Forbes where he is a regular contributor. He has appeared on CNBC and has been a repeat guest on the Fox Business Network. His insights have also appeared in USA Today, U.S. News & World Report, The Washington Post, and other leading publications.