Boenning Morning Comment

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Stocks continued to recover on Friday. Given the uniformity of the rally, it appeared to be a day of index buying in an economic world void of much real news. What economic data we could peruse over the weekend suggests that the U.S. economy is seeing some slight growth acceleration from the soft first quarter pace but year-over-year we remain locked in a 2% growth world just as we have been for many years.

With the President now on a 9-day overseas trip and the front page dominated more by pageantry than revelations, everyone can take a breather and reassess. Politically, not much has changed. The White House continues to be playing more defense than offense and Congressional Republicans are still in the relatively early stages of trying to cobble together healthcare and tax reform packages. Both the White House and Republican leaders express optimism that they will be able to get both healthcare reform and tax reform done this year but both paths are rutted with potholes and maybe sinkholes. Both investors and corporate leaders are moving forward expected little or nothing but hoping, still, for the best.

As I have been noting, the second quarter, at least in my view, is a crucial time for Congressional Republican leadership to start to shape economic packages that have a real chance of achieving the proper compromise to insure passage. While the Constitution requires fiscal bills to originate in the House, the real focus will be on the Senate where the Republican majority is fragile. Clearly, Democrats want no part in repealing and replacing Obamacare. That will have to be done without a single Democratic vote. In theory, tax reform could attract some Democrats if done in a manner than favors lower and middle class Americans. But so far, Republican leadership has appeared to be going the same route with tax reform as with healthcare, namely relying on just the Republicans to get the necessary 50 votes. That probably means that while some deficit increases can be tolerated in the early years, to get to a majority, whatever tax bill is put to a vote needs to be very close to revenue neutral over the 10-year period that the Congressional Budget Office (CBO) scores.

The key will be willingness to compromise, even within the Republican Party itself. To date, the so-called Tea Party or Freedom Caucus members have shown very little willingness to accept any changes to their agenda. They want the maximum possible tax cut, probably to 15% offset by broad cuts in both spending and entitlements. That even goes beyond Mr. Trump's agenda and clearly is a non-starter. The House gave in to the Freedom Caucus to get healthcare reform moved over to the House. Republican leaders know the Senate will start from scratch and try to cobble together a more centrist bill. Given than they can only afford to lose two votes, the only way that will happen is with both sides willing to accept half a loaf in order to achieve their goals. There have been few signs of willing compromise within Congress for the past eight years but clearly the message of the last election was for change, for help for the working class and for less gridlock.

Whatever the outcome of the healthcare debate, incumbents in Congress will now own whatever is achieved or not achieved. If a new law is passed, Republicans will own the consequences, good or bad. But even if nothing is passed, and the exchanges that now sell insurance to otherwise uncovered individuals fall apart, incumbents, both Republicans and Democrats will own the consequences. Democrats will own it because of the faults embedded within Obamacare. Republican incumbents will also own it because they allowed the exchanges to fall apart on their watch.

After all, with ownership of the White House and majorities in both chambers of Congress, Republican incumbents will have a tough time pointing fingers elsewhere for any economic failings between now and the mid-term elections. Thus, while no Democrats are going to vote to repeal and replace Obamacare, everyone who will run in 2018 will have an invested interest in making sure that health care works as well as it can.

Moving away from politics, we are in that mid-quarter vacuum where there is limited economic data and few earnings reports. Last week, we heard from retailers and while the severe problems of department stores took the headlines, the numbers weren't universally bad. Walmart had an OK quarter that met or exceeded expectations. Traffic was better than expected. Sales growth continued to be hindered by deflationary pressures. The home improvement stores had very strong results. Most of the weakness was apparel related. While the problems have been well chronicled, they will take a long time to solve. The biggest problem is that there are simply too many stores selling to too few people. Millennials are not extravagant spenders, at least not on goods, and baby boomers, beginning to retire are going to shop their closets more than stores going forward.

It isn't that no one is spending. Restaurants are doing fine and travel is strong. Even the art market showed signs of reinvigoration at last week's major auction, at least at the very high end. A combination of technology and changing tastes has transformed the consumer landscape tremendously over the past few years. Older companies are having a hard time adapting. New entrants are labeled disruptors but only a few truly are. New conceptual restaurant chains come and go quickly. Few achieve staying power. The Internet offers low cost ease of entry but that also means many imposters get to play the game for a while. The metamorphous of consumer behavior is only in the early innings. Before it is over, it will change the ways we buy everything. In the end, few of the old line stores will end up flourishing but most of the new entrants will fail as well. What we eat and how we eat will change. But as you see with the problems. Don't be surprised if one or two old line grocery chains don't stay near the top. Don't give up on all the old vets yet.

Today, Novak Djokovic is 30. Naomi Campbell turns 47.

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