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Boenning Morning Comment

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Today is the last trading day in May and tomorrow starts the stream of monthly economic data that will give investors a clearer picture of what has been happening this month. It promises to be more of the same, i.e. slow and steady growth with few signs of acceleration or deceleration. In simple terms, our economy is on autopilot as it seemingly has been since the end of the Great Recession.

That wasn't the way it was supposed to be, at least if you looked at the market action right after the election or listened to President Trump's campaign rhetoric and took it literally. Given Republican majorities in both chambers of Congress, one might have suspected that both healthcare and tax reform would be nearing completion. Instead, even though the House has passed its version of healthcare reform, both packages are, at best, incomplete works in progress. At worst, each is in disarray with no clear path toward a majority consensus that would lead to passage. For some time, some have argued that getting a grand plan accomplished might be too difficult but at least some modest step forward would be likely. While it is too early to disregard such prospects, time is working against the likelihood that anything gets done this calendar year.

Simply put, Congress is scheduled to be in recess for most of August. There are interruptions between now and then for various reasons including the 4th of July holiday period. While work doesn't cease completely while Congress is in recess, the pace of progress slows markedly.

Congress has a September 30 fiscal year. It has a two-year spending plan in place that currently runs through September 30. Many non-essential parts of the government cannot operate passed September 30 without further spending authorizations. One thing we can all be sure of is that this issue won't be resolved until late September but it will consume much of Congress's time in September. If that isn't enough, action will also be required to raise the debt ceiling once again right around the same time. Both raising the debt ceiling and passing the required spending authorizations to keep government running will require 60 votes in the Senate. That means Republicans and Democrats will actually have to work together. It also means that August and September are going to be consumed with matters other than tax and healthcare reform. That leaves about eight weeks to pull some sort of framework together that allows leadership to build coalitions that will lead to passage. Republicans are trying to work through reconciliation that requires only 50 votes in the Senate. With a majority of 52, there isn't much wiggle room. So far, it appears the conservatives who want major cuts in Medicaid aren't backing down while moderates who don't want 20+ million dropped from insurance rolls won't accept such cuts. If there is a way to bring both sides together, it isn't apparent at the moment meaning healthcare reform is stuck in place.

Tax reform offers similar dilemmas. Leadership wants to cut the corporate tax rate to 15%. The border adjustment proposal that could provide offsetting revenue seems dead on arrival. About the only revenue raising provision that has Republican consensus is the elimination of the deduction for state and local taxes. But that won't allow a cut in rates anywhere near what leadership wants to see. While some will accept large initial deficits hoping subsequent acceleration in growth can pick up the slack, most are unwilling to accept the idea that tax reform alone can accelerate growth even as much as a full percentage point. Thus, tax reform today is much closer to square one than the finish line.

All this, of course, can change quickly in Washington and it is likely that as time passes, Republicans will feel an urgency to get something done. But one thing legislators can change is the pace of time. In the best of times, the legislative process is slow. Republicans are finding out quickly that having 52 Senators doesn't create a majority if they can't find common ground. At some point, they will need to agree collectively that half a loaf is better than none. Clearly, they aren't there yet. In fact, it is safe to say they aren't close. Normally, this is where White House leadership often comes into play. So far, however, the White House hasn't offered more than campaign-style single page blue prints. It celebrated, some will say to excess, the healthcare reform victory in the House. But everyone knew that would never serve as a blueprint for what the Senate might someday approve. As for tax reform, the outline offered so far is nothing more than a repeat of campaign slogans. If Republicans are going to have a chance to pass anything substantive this year or early next year, the White House is going to have to take a leadership role. At the moment, its attention appears to be elsewhere.

Markets seem to accept all this. Healthcare and tax reform would be icing on the cake. In the meantime, markets are feeding off of synchronous worldwide growth, expanding earnings and low interest rates. It's an environment that appears to be working very well. Thus, it isn't the market that needs legislative wins; it's the Republican Party who won in 2016 as the great disruptor who could forge the changes necessary to make America great again. If, instead, it turns out that all it can accomplish is two more years of legislative gridlock, its prospects for the 2018 mid-term elections will be cloudy at best.

As noted, starting tomorrow we will get a flurry of data that should give a clear picture of May activity. The biggest report, as always, will be Friday's employment report. We will be watching the unemployment rate and the wage price inflation data in particular. Unless, the data deviates from recent numbers in a major way, you can expect the Federal Reserve to raise interest rates 25 basis points later in June.

Today Brooke Shields is 52. Joe Namath turns 74. Clint Eastwood is 87.

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