Rathbones
Look forward

Review of the week

6 April 2021

# Resurrection

**The US economy is rocketing towards recovery, with jobs, confidence and output soaring amid a strong vaccination drive and stimulus. Next on the list, investment in clean energy.**

As spring blooms, the US is bounding back from the pandemic.

American business surveys have soared to record highs and many more jobs have been created than economists had expected. The widely watched ISM Manufacturing PMI, a mixture of business optimism and order figures, hit 64.7 in March as production and hiring soared. It's not just factories that are doing well either. The ISM Services PMI unexpectedly rocketed to 63.7, the highest level since the measure was created in the late 1990s. Again, new business and hiring drove much of the rise. Unemployment continued falling, to 6.0% from 6.2% the previous month, as the number of jobs created in March ballooned to almost a million.

With $1.9 trillion of stimulus being injected into the nation, vaccinations continuing apace and warmer weather inbound, America is teed up for a strong summer of spending. Consumer confidence backs this up, with measures rising strongly over past months. This helped push the S&P 500 through 4,000 for the first time.

But while some investors are focused on the coming summer, others are pondering what the world may look like in the following years. President Joe Biden unveiled his infrastructure bill last week, a huge spending plan aimed at improving US infrastructure that has been neglected for many years. The $2.25 trillion plan is focused on roads, utility grids, green energy, water infrastructure and supporting the electrification of vehicles over the next eight years. It also includes measures to address the country's digital divide by rolling out high speed broadband. The bill is light on the detail, but the investment would be accompanied by tax hikes that are forecast to raise the ticket price for the investment in 15 years. Much of the extra tax comes from increasing the corporate tax rate to 28% from 21% and making it harder for American companies to funnel profits through offshore tax havens.

That tax hike would mean lower profits for owners of US stocks, as taxes come right off the bottom line. However, it's worth noting that the US tax rate was 35% as recently as 2017, and few American companies actually pay taxes at the headline rate because of the byzantine deductions, loopholes and minimums written into the code. According to the Tax Foundation, the average effective US corporate tax rate was 25% in 2019. The Biden administration also appears to be starting to use its diplomatic muscle to set a standard global minimum company tax rate. A global tax floor would help reduce the amount of time and resources spent by companies 'structuring' themselves into more profitable (i.e. lower tax paying) companies, which may mean more thought put into better businesses and products. But it would be fiendishly difficult to pull off. It would take a lot of overbearing American economic menace to make it happen, which could burn a lot of political capital with overseas allies, and it takes just one holdout to make the plan crumble anyway.

For now, though, Mr Biden will have to focus on getting his infrastructure and taxation bill through Congress intact.

### Energy is key

Globalisation and a brisk pace of technological progress has meant the world has lived through decades of abundance.

The rapid industrialisation and modernisation of China and other developing nations led to a surge in the productive capacity of the world – more stuff could be made quicker and cheaper than ever before. Fewer trade barriers allowed these cheaper toys, tools and appliances to be sold all over the world, boosting the buying power of hundreds of millions of people. New techniques of oil extraction meant the black stuff could be sucked up from deeper, further out to sea, or from rock formations that were once a no-go. That put paid to urgent warnings of 'peak oil' and a destabilising rise in the price of our world's most vital energy source. Digital advances meant smarter, quicker and more versatile computers. It soon led to cloud-computing - you don't even need the computer to get the computing power anymore - and along the way it has spread productivity-enhancing tools to virtually everyone, giving them hours back in their days. There are countless other examples: more efficient cars and machines and new business models, like ride-sharing and home-renting, which allow better use of resources or assets that would otherwise sit dormant.

At the same time, we've managed to harness different, more sustainable technologies and use them to reduce our reliance on the finite resources. But technology cannot completely eliminate this reliance. And it has only reduced the per head usage of materials, not the total. The most stark manifestation of this is the oil industry. The world is using 50% more oil now than we were in 1980 and 25% more than at the turn of the 21st century.

It is as much a shame as it is a truth: crude oil is the bedrock of our modern society. Without it, our economies and our societies would disintegrate. Oil is in virtually everything manmade that we touch. It is used to grease the machines that make our goods, if not in the goods themselves (plastics). It runs the tractors and harvesters that allow so few farmers to create so much food for the rest of us. It is ubiquitous in packaging and transportation. For a great many people, it fuels the generators that keep them warm at night too.

It is a foregone conclusion that this reliance is unsustainable, that we must move quickly to a cleaner future. But this will cost money. Big money. Mr Biden's infrastructure bill would no doubt have to have several sequels if America is to rebalance its energy situation from more than a century of reliance on one, cheap substance, to a proliferation of other, renewable options. It may also require punchy changes in attitudes and lifestyles. The same goes for every other nation in the world.

Whether this global energy transition can be done smoothly and what it will do to the cost of energy - which flows into the cost of everything - won't become apparent for years. It's just too complex to know how it will play out. Sustainable energy may turn out to be cheaper still, or it could push prices higher. Future energy dynamics are something we should be very mindful of. Because we have all been lucky enough to live in times of relative plenty. Cheap energy leads to cheap goods, cheap travel, cheap computing and more for everyone to share. But if energy becomes more expensive, that works in reverse too.

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