



Newsletter Vol. 12 Issue 6

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MACROECONOMIC MOVES AND MORTGAGE MARKET ANALYSIS

European Yields Rise
(Week ending May 1, 2015)



The Fed statement released on Wednesday contained no surprises. Going forward, Fed officials will decide at each meeting whether to raise the federal funds rate or not. In the statement, Fed officials said that

economic growth slowed during the winter, "in part reflecting transitory factors."

The timing of the first rate hike likely will depend on how quickly the economy rebounds. In a week packed with big

BEST BUYS THIS MONTH

- Conforming 5/1 ARM @ 2.375%
- High Balance Conforming 15 Yr. Fixed @ 2.875%
- Jumbo 5/1 ARM @ 2.750%
- Jumbo 30 Yr. Fixed @ 3.8750%
- FHA & VA Conforming 15 Yr. Fixed @ 2.625%
- DU Refi Plus/Open Access 30 Yr. Fixed @ 3.625%
- ALL-IN-ONE LOAN @ 3.680%



Conforming to \$417,000 < High Balance Conforming \$417,001 to \$562,350 < Jumbo

I ALSO DO:

- **COMMERCIAL LOANS** (more than 4 units)
- **"HARD MONEY" LOANS**
- **REVERSE MORTGAGES**
- **FOREIGN NATIONALS**
- **DELAYED FINANCING**
- **STATED INCOME LOANS**
- **MANUFACTURED HOMES**
- **ASSET DEPLETION LOANS**





economic events in the US, a shift in sentiment in Europe had the greatest influence on US mortgage rates. With bond yields in much of the euro zone at record low levels, the move higher accelerated swiftly. The increase in yields was due to an improving growth outlook and to rising optimism that Greece and euro zone officials will reach an aid agreement allowing Greece to remain in the European Union. In typical fashion, bond yields around the world were dragged higher as well.

Gross Domestic Product (GDP), the broadest measure of economic activity, increased at an annualized rate of just 0.2% during the first quarter, down from 2.2% during the fourth quarter. Unusually bad winter weather, port disruptions, lower energy prices, and the stronger dollar were the major factors behind the weak first quarter figures.

Job Gains on Target (Week ending May 8, 2015)

Against a consensus forecast of 220K, the economy added 223K jobs in April. The figures for March were revised lower from 126K to 85K. Despite the weakness seen in much of the other recent data, the economy has added an average of roughly 200K jobs per month so far this year. The Unemployment Rate has declined from 5.6% in December to 5.4% in April. This was the lowest level since May 2008.



Perhaps more influential for mortgage rates, Average Hourly Earnings were just 2.2% higher than one year ago, which was lower than expected. Wage growth has remained close to this level for over a year. It generally takes wage growth of 3.0% to 4.0% before it exerts upward pressure on the overall inflation level. Since mortgage rates are determined based on expected future inflation, this wage data was positive news for mortgage rates.

Solid job growth with low wage gains is a nice combination for both stocks and bonds. It adds little pressure for the Fed to bring forward the timing of the first federal funds rate hike. The stock market rallied on the news as well.

Volatility Continues (Week ending May 15, 2015)

To understand this week's market action, it was helpful to look at long-term trends. In recent months, bond yields in Europe generally dictated the direction of yields around the world. A sluggish economic growth outlook and a new sovereign bond purchase program from the European Central Bank caused investors to view European bonds as promising assets. Yields declined to record low levels in Germany and many other European countries.

Eventually, however, investor sentiment shifted, sparked by signs of improving economic conditions and reduced concerns about a default on Greek debt. The resulting increase in European yields seen this month has dragged global bond yields, including those of US mortgage-backed securities, higher at a rapid pace. It has overwhelmed this month's weaker than expected US economic data, which normally would result in an improvement in mortgage rates.

While retail sales activity in March showed signs of rebounding from a winter slump, the April Retail Sales report released this week revealed that the momentum did not continue. Retail sales in April, excluding the volatile auto component, increased slightly from March, but fell far short of the expected level. Lower gas prices and pent up demand from the winter did not have the anticipated impact on consumer spending in April.

Housing Starts Jump (Week ending May 22, 2015)

The minutes from the April 29 Fed meeting released on Wednesday contained no major surprises. According to the minutes, Fed officials do not expect that economic conditions will justify a federal funds rate hike in June. They attributed weak economic growth during the first quarter to "transitory" factors including bad weather and the West Coast port shutdown. Most investors now are looking for the first rate hike to take place in September or December.



The housing data released this week was mixed. Single-family housing starts in April jumped 16% from March to the highest level since January 2008. By contrast, April existing-home sales fell 3% from March, but they still were 6% higher than a

year ago. The median existing-home price was 9% higher than a year ago. According to the NAR, a lack of supply is holding back sales activity and pushing home prices higher. Based on this month's strong data on housing starts, builders, fueled by low rates, may help to alleviate the shortage of available homes.

Attention on Greece (Week ending May 29, 2015)

The next Greek debt repayment is scheduled for June 5. Without a bailout, there is a risk that Greece will default on its debt. If this were to occur, the effects on the rest of the eurozone are difficult to predict. In typical fashion, investors have responded to the uncertainty by shifting to relatively safer assets, including U.S. mortgage-backed securities (MBS). Added demand for MBS helps mortgage rates move lower. Since investors reverse their positions when the uncertainty decreases, news reports about Greece have created volatility in U.S. mortgage rates. Over the past week, the net impact was slightly favorable for mortgage rates.

The housing data released over the past week was encouraging. April's pending home sales rose 3% from March to the highest level since May 2006. They were 14% higher than one year ago. April's new-home sales increased 7% from March, and they were 26% higher than a year ago. While the existing-home sales data for April showed a small monthly decline, pending and new-home sales reflect the more current housing market activity.

WEALTH AND INCOME INEQUALITY 2.0



This is the eleventh and final installment of my multi-part series on the macroeconomics of political and social issues that weigh heavily on our "State of the Union". As Theodore Parker, an early American Transcendentalist observed: *The arc of the moral universe is long, but it bends toward justice.* Because economics relies heavily on numbers and statistics it is an invaluable indicator of the costs and benefits associated with "being on the right side of history". Over the past 18 months, I have tried to illustrate that the nation's social progress, economic development and our quality of life are inextricably linked.

In the March 2014 newsletter (Volume 11 Issue 3) I raised the issue of income inequality and mentioned Professor Thomas Piketty and his book, Capital in the Twenty-First Century, but, in retrospect, I did not emphasize his main thesis: The growth of income inequality has been responsible for even greater wealth inequality, which in turn, has fostered the growth of asset bubbles, financial instability and diminished economic growth. His book has since become the magnum opus of economics books in the past decade. As a consequence, I felt the need to revisit this topic.

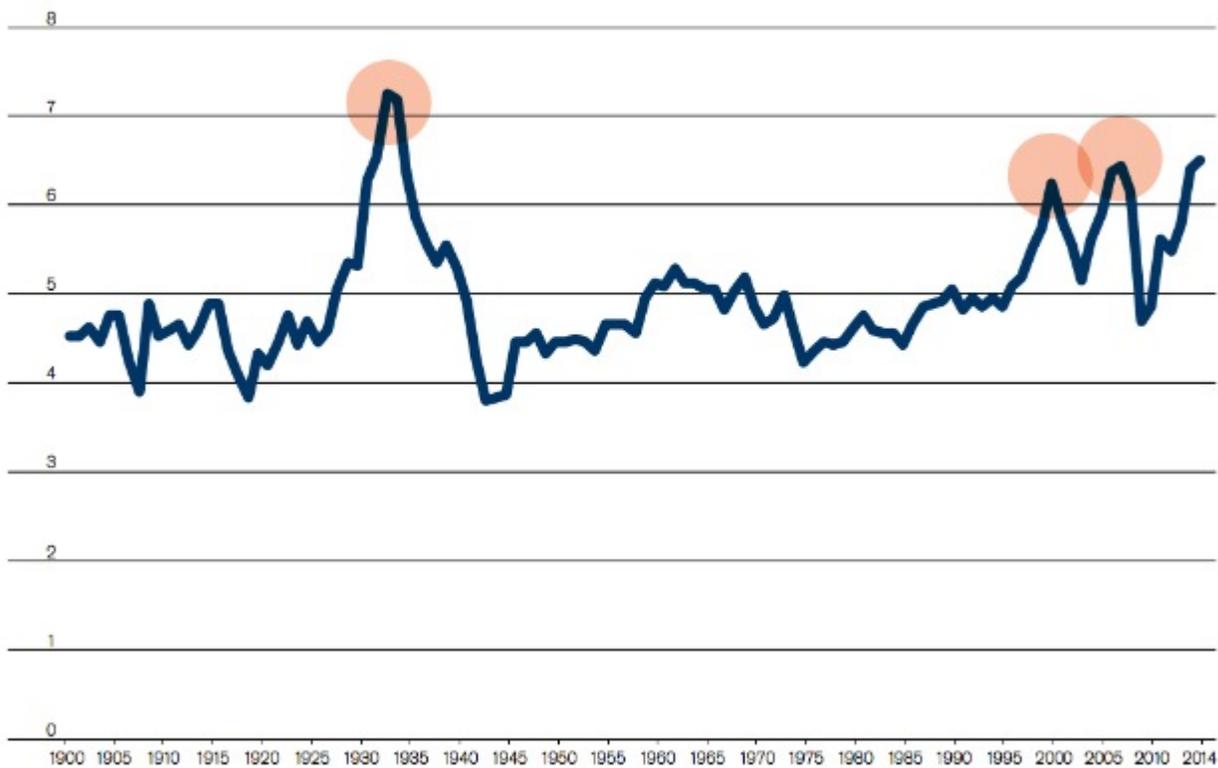


Simply stated, wealth is outpacing income. More household wealth in American sounds like good news, but it often presages economic trouble in the form of asset bubbles. But Piketty is not alone in this observation. The ratio of wealth to income has hit a recent high, according to Credit Suisse. The last time it was this high was during the Great depression. And it came close two other times: 1999, the year before the dotcom bubble burst and leading up to 2007, before the housing market crash. Credit Suisse analysts found that the ratio of wealth to income is 6.5. For more than 100 years it has typically fallen between 4 and 5. "This is a worrying signal given that abnormally high wealth income ratios have always signaled recession the past," the Credit Suisse report said.



The current ratio of wealth to household income is at a level not seen since the Great Depression

Source: US Federal Reserve Board (1900 – 2013); James Davies, Rodrigo Lluberas and Anthony Shorrocks, Credit Suisse Global Wealth Databook 2014



COURTESY: CREDIT SUISSE

The graph above shows that there have been three periods of high wealth to income ratios in the past 15 years. Not only that, but as these asset bubbles are becoming more frequent and they're adding to further financial instability.

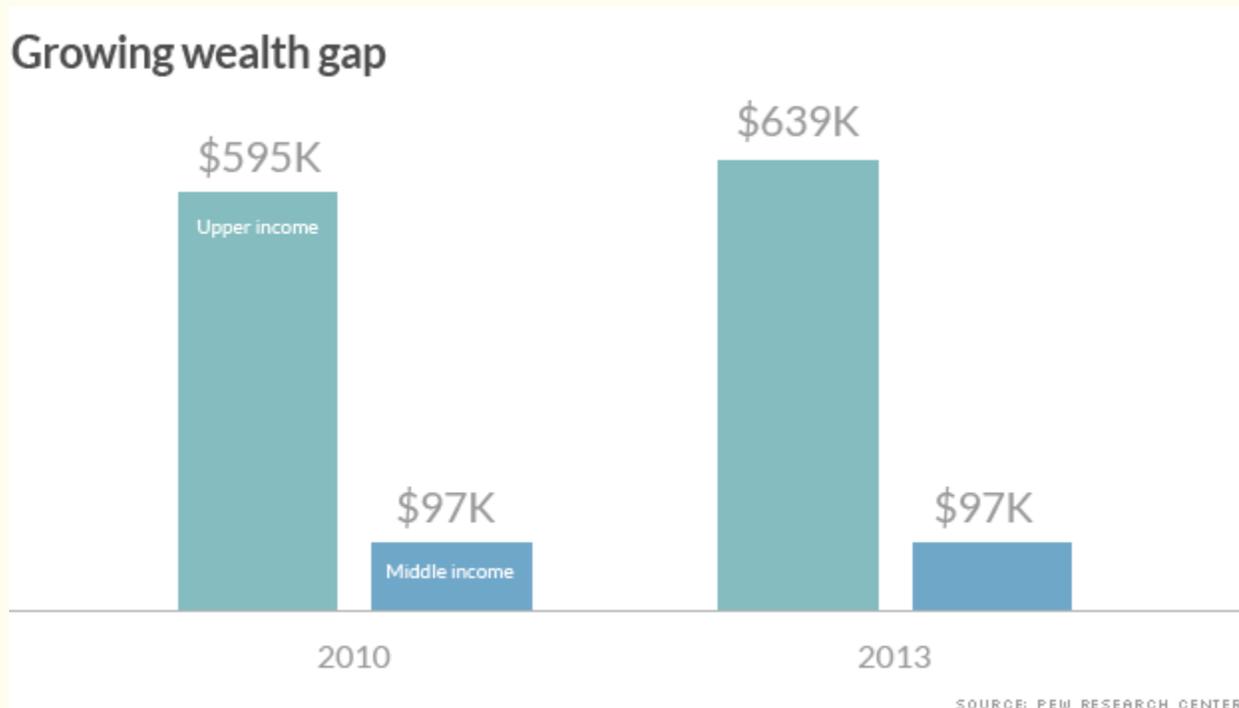
Wealth per adult in the U.S. has risen every year since 2008. In fact, average wealth is now 19% above the pre-crisis peak hit in 2006, the report stated. And \$31.5 trillion household wealth has been added to the U.S. since 2008. While experts said it's normal for wealth to outpace income, especially after a recession, it becomes a problem when it rises so fast that people feel overly optimistic about their wealth. When wealth inequality increases, the likelihood of asset bubbles also rises because the stock market and financial industry are always moving around looking for the highest returns and when the stock market gets hot, more people pour in, and that amplifies the creation of a pending bubble."

The bar chart below also shows that wealth gap between the middle class and those at the very top is diverging while the living standards for the majority are stagnating. Not only are middle class suffering from stagnant incomes, their wealth hasn't grown at all either. That's led to the widest wealth gap on record between the middle class and the rich. The median household net worth of middle-income Americans remained at \$96,500 between 2010 and 2013, according to a new report from the Pew Research Center, which looked at Federal Reserve Bank data. Some 46% of American



household fall into middle income under its methodology, which adjusts for family size. Pew defines middle income as family of four with a household income between \$44,000 and \$132,000. Upper-income Americans are those who earn more than \$132,000 for a family of four. Upper-income households, however, saw their wealth grow to \$639,400 last year, up from \$595,300. That means the rich have 6.6 times more wealth than the middle class, a figure that's grown from 4.1 in 1998 and 3.4 in 1983. It's also a record 69 times the wealth of lower-income Americans, who had accumulated only \$9,300 as of last year.

WEALTH GAP BETWEEN MIDDLE CLASS AND RICH WIDEST EVER



Part of the reason for the gap stems from how the rich and the middle class build wealth. The former are more likely to invest in the stock market, which has been on a tear in recent years. The latter have more of their net worth tied up in the housing market, which hasn't recovered as much. That's also why the Great Recession had a bigger impact on the net worth of the middle class. Back in 2007, before the housing crash, the middle class saw its median wealth soar to \$158,400. The rich also haven't recovered fully from the downturn, but they are a lot closer to their 2007 peak of \$718,000. Looking longer term, the rich have more than doubled the size of their nest eggs over the past three decades, while the middle class have inched up 2.3%.



Piketty posits that wealth concentration is a natural tendency in market economies. The Fed's report also said the widening income gap represented a reversion to a long-term trend that was only disrupted by the recession. It stated that the top 3 percent of families collected 30.5 percent of ALL income in 2013, up from 27.7 percent in 2010, but still slightly below their 31.4 percent share in 2007. This concentration of wealth continued without interruption, albeit at a slower pace during the recession. The Fed said that the top 3 percent of families held 44.8 percent of wealth in 1989, then 51.8 percent in 2007 and 54.4 percent in 2013.

Piketty's asserts that economic inequality has worsened significantly in the United States and some other countries, that we have re-entered the gilded Age of the Robber Barons and the current situation is tipping evermore in favor a relatively small percentage of "haves" versus an overwhelming percentage of "have-nots". He observes that our extant capitalism is an ersatz capitalism whereby we socialize losses, even as we privatize gains. CEOs enjoy incomes that are on average 295 times that of the typical worker, a much higher ratio than in the laissez-faire capitalism of the past. To wit: The income of a typical American family has barely risen since the 1970s while the share of national income captured by the richest 1 percent of Americans is even higher than it was at the dawn of the 20th century. In 2012 the top 1 percent of American households collected 22.5 percent of the nation's income, the highest total since 1928. The great bulk of that rise has taken place among the top 0.1percent, the richest one-thousandth of Americans.



So, how is it that people are unaware of this development, or at least of its scale? The most likely answer is that the truly rich are so removed form ordinary people's lives that we never see what they have. The exceptions are celebrities, who live their lives in public. But celebrities make up only a tiny fraction of the wealthy, and even the biggest stars earn far less than the financial barons who really dominate the upper strata. For example according to Forbes, Robert Downey Jr. was the highest paid actor in America, making \$75 million in 2013. According to the same publication, for the same period, the top 25 hedge fund managers took home, on average, almost a billion dollars each or over 13 times as much as he did.

Defenders of the superrich take advantage of the average citizen's ignorance of enormity of the inequality when entities like the American Heritage Foundation tell us that the top 10 percent pay 68 percent of income taxes, it's obfuscating the fact the top 10 percent receive almost half of all income and own 75 percent of the nation's wealth, which makes their burden seem a lot less disproportionate.

INHERITANCE VS. INCOME INEQUALITY

WEALTH OVER WORK. A major tenet of Piketty's 700 page tome is that increasingly, the return on capital exceeds the return on labor. He asserts that we have arrived at a point where the return on capital is vastly rewarded over work. Piketty makes a powerful case that we're on the way back to "patrimonial capitalism," by documenting the growing concentration of income in the hands of a small economic elite. In looking at the Forbes list of the wealthiest Americans he reports that about a third of the top 50 inherited large fortunes from their forebears. Another third are 65 or older, so they will probably be leaving large fortunes to their heirs. We are on the road to establishing a hereditary aristocracy of wealth in which birth matters more than effort and talent. Although he concedes that the rise of America's 1 percent has mainly been driven by executive salaries and bonuses rather than income from investments, let alone inherited wealth, there is an inexorable trend. Six of the 10 wealthiest Americans are heirs rather than self-made entrepreneurs, and the children of today's economic elite start from a position of immense privilege. As Mr. Piketty notes, "the risk of a drift toward oligarchy is real and gives little reason for optimism."



Though America's nascent oligarchy may not yet be fully formed, one of our two main political parties already seems committed to defending the oligarchy's interests. Despite the efforts of some Republicans to pretend otherwise, it is patently obvious today's G.O.P. favors the interests of the rich over those of ordinary families. Few people realize the extent to which the party favors returns on wealth over wages and salaries. But, a good starting point is an examination of actual policies and policy proposals. While it's generally understood that George W. Bush did all he could to cut taxes on the very affluent (and that the middle-class cuts he included were essentially political loss leaders) what is less well understood is that the biggest breaks went not to people paid high salaries but to coupon-clippers and heirs to large estates. True, the top tax bracket on earned income fell from 39.6 to 35

percent. But the top rate on dividends fell from 39.6 percent (because they were taxed as ordinary income) to 15 percent—and the estate tax was completely eliminated.

Some of these cuts were reversed under President Obama, but the point is that the great tax-cut push of the Bush years was mainly about reducing taxes on unearned income. And when Republicans retook one house of Congress, they promptly came up with a plan—Representative Paul Ryan’s “road map”—calling for the elimination of taxes on interest, dividends, capital gains and estates. Under this plan, someone living solely off inherited wealth would have owed no federal taxes at all.



This tilt of policy toward the interests of wealth has been mirrored by a tilt in rhetoric; Republicans often seem so intent on exalting “job creators” that they forget to mention American workers. In fact, not only don’t most Americans own businesses, but business income, and income from capital in general, is increasingly concentrated in the hands of a few people. In 1979 the top 1 percent of households accounted for 17 percent of business income; by 2007 the same group was getting 43 percent of business income, and 75 percent of capital gains. Nevertheless, this small economic elite commands all of the G.O.P.’s love, and most of its policy attention.

Why is this happening? Well, bear in mind that both Koch brothers are numbered among the 10 wealthiest Americans, and so are four Walmart heirs. Great wealth buys great political influence—and not just through campaign contributions. Many conservatives live inside an intellectual bubble of think tanks and captive media that is ultimately financed by a handful of mega-donors. Not surprisingly, those inside the bubble tend to assume, instinctively, that what is good for oligarchs is good for America. And so the drift toward oligarchy continues.

A BRIEF HISTORY INCOME INEQUALITY IN AMERICA

Someone once said, “Perspective is everything.” So, it is relevant to view recent economic trends from a historical perspective and recall the aptness of a former president’s observations:

“The absence of effective State, and, especially, national, restraint upon unfair money-getting has tended to create a small class of enormously wealthy and economically powerful men, whose chief object is to hold and increase their power,” and follow that statement with a call for “a graduated inheritance tax on big fortunes...increasing rapidly in amount with the size of the estate.”



Who was this left-winger? It was Republican Theodore Roosevelt, in his famous 1910 New Nationalism speech.

The years from the late 19th and early 20th centuries were not the most egalitarian in American history. Robber barons roamed the economy, living off lavish rents generated by powerful cartels and industrial monopolies. The richest 1 percent of Americans reaped nearly one in five dollars generated by the economy and amassed almost half its wealth; at the other end of the scale, wage earners lost ground to inflation. Not that much different from today.



While federal income tax has generally played a progressive role in mitigating income inequality, but it has varied widely since it was introduced a century ago. By itself, it has not proven powerful enough to overcome the widening gap of recent decades. In 1917, the top federal income tax rate was raised to 67 percent. Though it fell in the 1920s, it would rise again during the Great Depression and,

especially, World War II. In 1940, before the United States entered the war, the federal income tax raised \$1.5 billion (\$25 billion in today's money). By 1945, it collected \$17 billion (\$223 billion). The top income tax rate would not fall below 70 percent again until 1980. But, justifying hefty taxation of the wealthy required a more compelling argument than inequality. The immiseration caused by the Great Depression, no doubt, helped. But winning the argument also required two wars. With idea of military conscription came the notion of conscription of wealth and income. Only the prospect of many thousands of poor young men contributing their lives to the national project could justify taking more of the elite's money in the service of the national good.

PIKETTY'S "CAPITAL IN THE TWENTY-FIRST CENTURY"

Piketty's First Law of Inequality maintains that so-called "free markets," by their nature, tend to enrich the owners of capital at the expense of people who own less of it. The fact that the rich earn enough money to save money allows them to make investments that other people simply cannot afford. And investments—



whether they are land, corporate stock or education—tend to bring a positive return. Piketty describes the relationship formally as $r > g$: the rate of return on capital usually exceeds economic growth. He notes that certain things can disrupt this relationship. When a war destroys farms, the big farmers are no longer much richer than anyone else. A depression can play the same role. When income or wealth is taxed at high rates, the rich are not able to save and accumulate as much. It's no accident that in the decades after World War II, when middle-class incomes were rising even more rapidly than the incomes of the rich, the top marginal income-tax rates were exceptionally high. In the 1950s, the top rate exceeded 90 percent and we were a more egalitarian society. Today, it is 39.6 percent, and only because President Obama finally won a year long battle with Republicans in early 2013 to increase it from 35 percent.

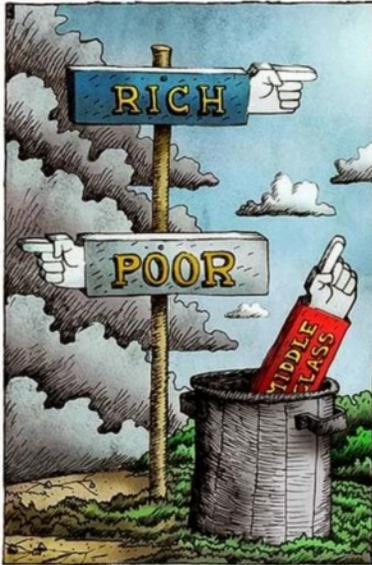
Piketty's work charges that economic inequality leads to economic destabilization, market distortions and a waste of human resources. It is also a challenge both to Marxism and laissez-faire economics, which both count on pure economic forces for harmony or justice to prevail. While Marx presumed that the rate of return on capital, because of the system's contradictions, would fall close to zero, bringing collapse and revolution, Mr. Piketty is saying the opposite. "The rate of return to capital can be bigger than the growth rate forever—this is actually what we've had for most of human history, and there are good reasons to believe we will have it in the future." The political assumption of the 1950s and 1960s was that inequality would stabilize and diminish on its own and has proved to be illusory. Basic models of political economy hold that inequality self-corrects. As income concentrates among a smaller group of voters, majorities will vote for more redistribution. But that isn't quite how the world works. For starters, the poor vote less than the rich. And they don't vote exclusively based on their economic self-interest.



The concentration of income at the top has become even more pronounced than it was during the Clinton administration. At the same time, Supreme Court Rulings allowing a rush of private money into political campaigns have underscored how plutocracy could purchase the policies it wants to maintain as privilege, locking in inequity forever. So, the growing concentration of income can, in fact, make inequality more difficult to correct, as the wealthy bring their wealth to bear on the political process to maintain their privilege. What's more, disparities in income seem to produce political polarization and gridlock, which tend to favor those who receive a better deal from the prevailing rules.

This poses one of the most important socio-economic questions: Can democracy stop inequality from rising? Despite the gains of the Progressive Era, the answer echoing down the halls of history is not encouraging. While the gains in recent years have not been as impressive as during the post-World War II years, they do

exist, for now. Even as the rich have gotten much, much richer, the 99 percent have shared in growing prosperity in real, measurable ways. Higher income tax rates, subsidies to buy health insurance under the Affordable Care Act and expanded tax breaks for poor families with children—have produced “the most significant policy-induced reduction in inequality in at least 40 years.” Yet even these measures only offset about half a decade’s worth of increasing inequality.



Piketty argues that rising inequality isn’t merely a feature of our times; it has been the historical norm. It has risen throughout much of modern history, he writes, with the notable exceptions of wars, depressions and their aftermath, when everyone was forced to rebuild from a more equal place. He adds inequality is likely to continue increasing for decades, ultimately resulting in a plutocracy in which the rich separate themselves from everyone else, perpetuating their wealth from one generation to the next, as nobility of past centuries did. While that scenario sounds dystopian to most, he says it doesn’t necessarily have to turn out that way. To say that something is likely, or even natural, is not to say that it is inevitable.

Not so long ago, the rich owned a much smaller share of this country’s resources and made a smaller share of its income than many of their predecessors. Perhaps more important, even though inequality has risen abroad, it has done so far less rapidly. Instead, their middle class and poor have enjoyed more aggressively rising incomes, all while their economies have grown as rapidly as ours in recent years. In short, a more equal society does not mean a less dynamic one.

The United States has come a long way over the last century. Still, it remains a strikingly similar place in a couple of important respects. We are now back to a traditional pattern of returns on capital of 4 percent to 5 percent a year and rates of economic growth of around 2 percent a year. So inequality has been quickly gathering pace, aided to some degree by the Reagan and Thatcher doctrines of tax cuts for the wealthy. “Trickle-down economics might have been true,” Mr. Piketty said simply, “but it just happened to be wrong.” So while a rising economic tides may float all boats, the current situation, instead is mostly lifting the yachts in 2014 and beyond, with the majority of the working class left stranded in the shallows. Increasingly, the American Dream is slipping away because the return on capital is ever so much greater than the return on labor.

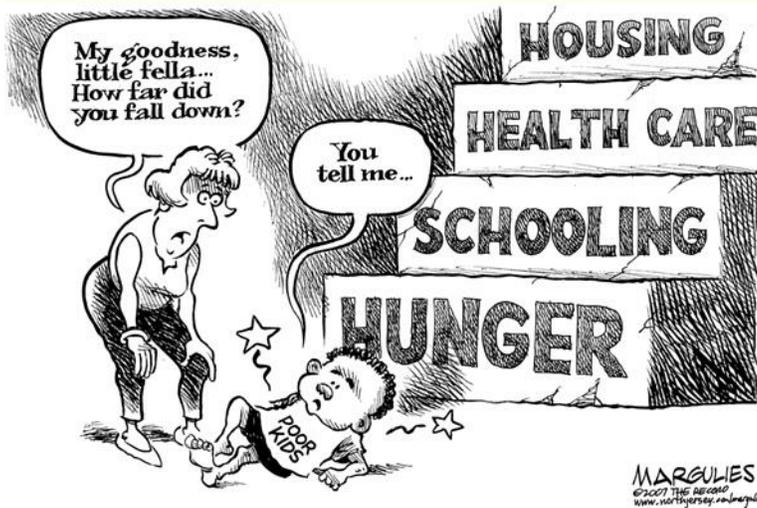
ECONOMIC DESTABILIZATION. While some inequality is acceptable to the extent it spurs individual initiative and the generation of wealth; extreme economic inequality has a deep and deleterious impact on democratic values. We seem to have reached the point where inequality actually has become an impediment to economic growth. The nation grew more quickly in periods when we were more equal, including in the golden decades after World War II when growth was strong and inequality actually diminished. Likewise, a major research paper from the International Monetary Fund last April found that more equitable societies tend to enjoy more rapid economic growth. Indeed, even Lloyd Blankfein, the chief executive of Goldman Sachs, warns that “too much... has gone to too few” and that inequality in America is now “very destabilizing.” Inequality causes problems by creating fissures in societies, leaving those at the bottom feeling marginalized or disenfranchised. That has been a classic problem in “banana republic” countries in Latin America, and the United States now has a Gini coefficient (a standard measure of inequality) approaching some traditionally poor and dysfunctional Latin countries.



MARKET DISTORTIONS. Disparities reflect not just the invisible hand of the market but also manipulation of markets. Joseph Stiglitz, the Nobel Prize-winning economist, wrote “The Price of Inequality” in which he observes: “Much of America’s inequality is the result of market distortions, with incentives directed not at creating new wealth but at taking it from others.” Wealth-holders manage to keep their after-tax rate of return high relative to economic growth by rigging the game through politics to ensure a certain outcome. For example, financiers

may be wealthy partly because they’re highly educated and hardworking but also because they’ve successfully lobbied for the carried interest tax loophole that lets their pay be taxed at much lower rates than other people. Likewise, if you’re a pharmaceutical executive, one way to create profits is to generate new products. Another is to lobby Congress to bar the government’s Medicare program from bargaining for drug prices. That amounts to a \$50 billion annual gift to pharmaceutical companies.

WASTE OF HUMAN RESOURCES. But doesn't taxing the rich and helping the poor reduce the incentive to make money? Well, yes, but incentives aren't the only thing that matters for economic growth. Opportunity is also crucial. And extreme inequality deprives many people of the opportunity to fulfill their potential. Think about it. Do talented children in low-income American families have the same chance to make use of their



talent—to get the right education, to pursue the right career path—as those born higher up the ladder? Of course not. Moreover, this isn't just unfair, it's expensive. Extreme inequality means a waste of human resources. And government programs that reduce inequality can make the nation as a whole richer, by reducing that waste. We know that some of the tools, including job incentives and better schools, can reduce this opportunity gap. Education is a force that can disrupt inequality. When a society becomes more educated, many of its less-wealthy citizens quickly acquire a crucial form of capital—knowledge—which can bring enormous returns. The great income gains for the American middle class and poor in the mid-to-late 20th century came after this country made high school universal and turned itself into the most educated nation in the world.

As the economists Claudia Goldin and Lawrence Katz have written, "The 20th century was the American century because it was the human-capital century." Education continues to pay today, despite the scare stories to the contrary. The pay gap between college graduates and everyone else in this country is near its all-time high. The countries that have done a better job increasing their educational attainment, like Canada and Sweden, have also seen bigger broad-based income gains than the United States. But the United States is one of the few advanced countries that spends less educating the average poor child than the average rich one. And so, our once-large international lead in educational attainment has vanished, and our lead in inequality has grown. Indeed, researchers find that there is less economic mobility in America than in class-conscious Europe. But the fact of the matter is that if you look systematically at the international evidence on inequality, redistribution, and growth—which is what researchers at the IMF did—you find that the lower levels of inequality are associated with faster, not slower, growth. Specifically, Sweden, Finland and Norway have all succeeded in having about as much or faster growth in per capita incomes than the United States and with far greater equality.



There is, at this point, no reason to believe that comforting the comfortable and afflicting the afflicted is good for growth, and good reason to believe the opposite. Furthermore, income redistribution at the levels typical of advanced countries (with the United States doing much less than average) is robustly associated with higher and more durable growth. There is no evidence that making the rich richer enriches the nation as a whole, but there's strong evidence of benefits from making the poor less poor.

SOLUTIONS As previously mentioned, the growing concentration of wealth in the hands of a relative few can make income inequality more difficult to correct, as those with financial clout use their resources via the political process to maintain their privilege. The American political system is overrun by money. Simply put, economic inequality translates into political inequality and political inequality yields increasing economic inequality.



In the past, ideology and interests have combined nefariously. Some drew the wrong lesson from the collapse of the Soviet system. The pendulum swung from much too much government there to much too little here. Corporate interests argued for getting rid of regulations, even when those regulations had done so much to protect and improve our environment, our safety, our health and the economy itself. But this ideology was hypocritical. The bankers, among the strongest advocates of laissez-faire economics, were only too willing to accept hundreds of billions of dollars from the government in the bailouts that have been a recurring feature of the global economy



since the beginning of the Thatcher-Reagan era of “free” markets and deregulation. So, corporate welfare increases as we curtail welfare for the poor. Congress maintains subsidies for rich farmers as we cut back on nutritional support for the needy. Drug companies have been given hundreds of billions of dollars as we limit Medicaid benefits. The banks that brought on the global financial crisis got billions while a pittance went to the homeowners and victims of the same banks’ predatory lending practices. Our economy, our democracy and our society have paid for these gross inequities. Justice has become a commodity, affordable to only a few. While Wall Street executives used their high-retainer lawyers to ensure that their ranks were not held accountable for the misdeeds that the crisis in 2008 so graphically revealed and the banks abused our legal system to foreclose on mortgages and evict people, some of whom did not even owe money. The true test of an economy is not how much wealth oligarchs can accumulate in tax havens, but how well off the typical citizen is—even more so in America where our self-image is rooted in our claim to be the great middle-class society. Yet, median incomes are lower than they were a quarter-century ago. Growth has gone to the very, very top, whose share has almost quadrupled since 1980.

What our society gravely lacks is empathy when confronting today’s issues such as inequality or poverty. If one were to simply use that supposedly most Christian of doctrines, the Golden Rule of “Do unto others as you would have them do unto you” it would readily answer why we should create safety nets to support the poor and good schools to help their kids achieve a better life. Imagine that were we all to agree on a social contract, from a “position of not knowing” that is, if we didn’t know, if we would be rich or poor, smart or dumb, diligent or lazy, American or Bangladeshi. If we didn’t know whether we’d be born to a wealthy suburban family or to a single mom in an inner city, we’d be more inclined to favor measures that protect those at the bottom. Such a social contract benefits all of us in society.



A true attack on inequality would require that the country move the issue to the center of every political debate: how we tax wealth, how we tax the income of the middle class and poor (often stealthily through the payroll tax), how we finance schools and measure their results, how we tolerate income-sapping waste in health care, how we build roads, transit systems and broadband networks. These are precisely the sort of policies pursued by countries with better recent middle-class income growth than the United States.

Mr. Piketty goes so far as to say that “confiscatory taxation of excessive incomes”—that is, taxation whose goal was to reduce income and wealth disparities, rather than to raise money— was an “American invention.” And this invention had deep historical roots in the Jeffersonian vision of an egalitarian society of small farmers. Back when Teddy Roosevelt gave his speech, many thoughtful Americans realized not just that



extreme inequality was making nonsense of that vision, but that America was in danger of turning into a society dominated by hereditary wealth—that the New World was at risk of turning into Old Europe. And they were forthright in arguing that public policy should seek to limit inequality for political as well as economic reasons, that great wealth posed a danger to democracy. Thus, he proposed that inequality could be tempered by returning to the tax rates of the past. “If we could raise top tax rates to nearly 80 percent once, why couldn’t we do it again?” He advocates a progressive global tax on real wealth (minus debt), aimed more directly at capital inequality than income taxes currently are. “Net wealth is a better indicator of

ability to pay than income alone. All I'm proposing is to reduce the property tax on half or three-quarters of the population who have very little wealth." It would apply to anyone with more than about \$1.4 million in net worth and become steeper on higher fortunes than moderate ones. It's an interesting idea, but it has little, if any, chance of passing the current legislative environment. So is there any hope of stopping America's income chasm from growing? There hasn't been the immiseration you would associate with a revolution, but people are more concerned about fairness that they have in a long time and the perception that like Elizabeth Warren claims, "the game has been rigged".



CONCLUSIONS

Americans, in the main, don't realize how extreme income inequality is or of the extent to which it is re-shaping society. The French economist, Thomas Piketty posits that we're on our way toward a society dominated by wealth, much of it inherited, rather than by work. While many of the members on the list of richest Americans are self-made men, by and large, they did their self-making a long time ago. The inevitable development is that over time, extreme inequality in income leads to extreme inequality of wealth; with high incomes increasingly coming from investment income, not salaries, it's only a matter of time before inheritance becomes the biggest source of great wealth.

We can alter the course of inequality by insuring that those at the top pay their fair share of taxes—ending the special privileges of speculators, corporations and the rich—is both pragmatic and fair. We are not embracing a politics of envy if we reverse the politics of greed. Inequality is not just about the top marginal tax rate but also about our children's access to food and the right to justice for all. If we spent more on education, health and infrastructure, we would strengthen our economy, now and in the future. Being nice to the wealthy and cruel to the poor is not; it turns out, the key to economic growth. On the contrary, making our economy fairer would also make it richer. The problem of inequality is not so much a matter of technical economics. It's really a problem of practical politics. Inequality, then, is less an inevitability than a choice.

U.S. ECONOMY SHRANK IN THE FIRST QUARTER, AGAIN

America's economic growth was actually negative in the first three months of 2015. Gross domestic product, the widest measure of growth, fell -0.7%, according to revised government statistics. The cold weather, the strong U.S. dollar and West Coast port strike all contributed to the weak start to the year. The strong dollar is making American exports look very expensive to people in other countries.



The same winter blip happened last year. The U.S. economy actually contracted by -2.1% in the first quarter of 2014, but the economy came surging back as the weather improved. It is likely to be a recurring pattern in the years to come as weather becomes more extreme, not only in the winter months, but also in the spring with their torrential rains and flooding and severe droughts in the summers.

Fortunately, the U.S. economy is showing signs of life. Housing starts—the pulse of American real estate—had its best monthly gain since 1991 in April. Consumer confidence ticked up a bit recently and orders for durable goods—refrigerators, for example—jumped up too. People tend not to buy big ticket items unless they are optimistic about where their finances are headed.

Hiring is also strong. The economy added a healthy 223,000 jobs in April, a reassuring sign after March saw few job gains.

The government's initial estimate of first quarter economic growth, published a month ago, was a disappointing 0.2%. But even that projection was too optimistic. The government typically revises the data as it gets more accurate information.

Although the first quarter is long gone, it is a big deal to the Federal Reserve, which is trying to decide if the economy is strong enough to raise interest rates soon. The negative economic growth means a June rate hike is almost certainly not going to happen. Many experts believe the Fed is prepping for a September rate hike.

GOOD NEWS: U.S. ECONOMY ADDS 223,000 JOBS

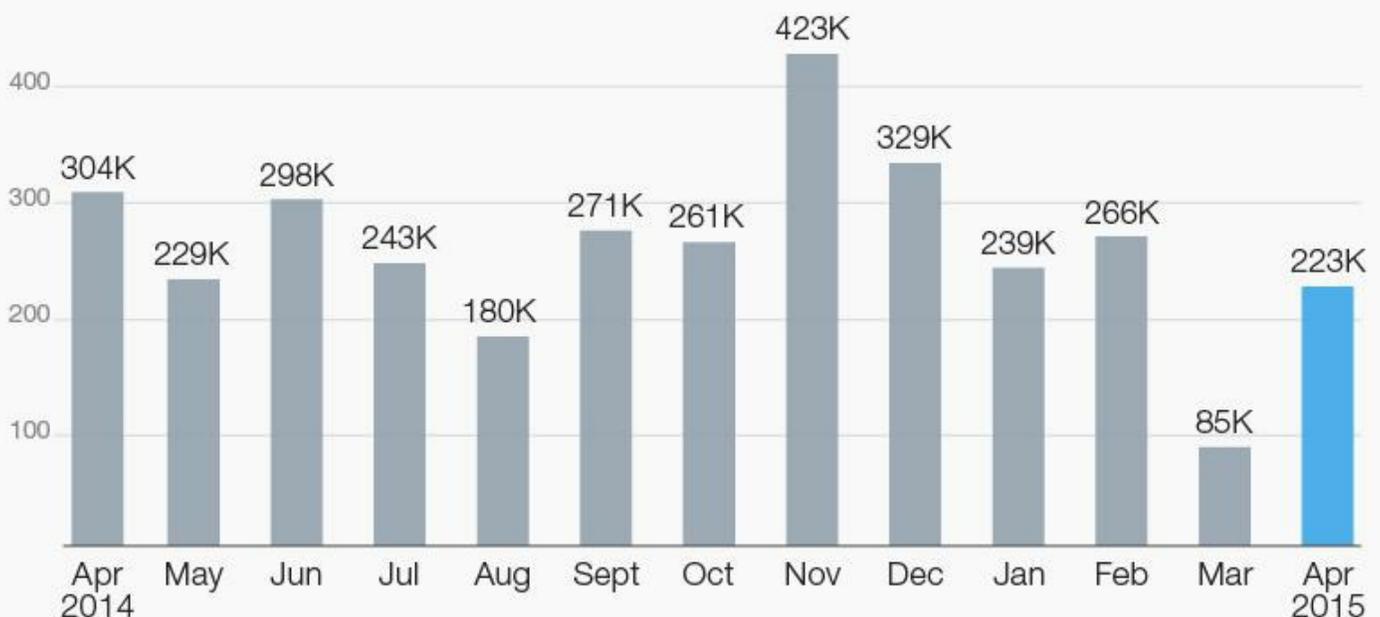
The economy gained 223,000 jobs in April, a healthy pick up after a disappointing March. April's strong job gains reflect a trend the country saw last year: job growth cooling in the winter months, then, gaining momentum in the spring.

The good news doesn't stop there. The unemployment rate dropped to 5.4%, its lowest mark since May 2008. The one thing regular Americans still want is better pay. There are finally signs it's picking up. Wages are now growing at 2.2%. Experts say pay should continue to bump up if unemployment remains low.

Where the jobs are: Hiring has been strong in many industries with one big exception: Energy. About 15,000 energy jobs—oil drillers, coal miners and others—were lost in April, the worst month for the sector since May 2009. Low gas prices are great for Americans at the pump, but they're causing energy companies to cut jobs. Despite the bad energy news, other industries picked up the slack. Construction and health care each added 45,000 jobs. Business services—marketing, accountants, and consultant—was the best performer in April, adding 62,000 jobs.

Monthly job gains

500 thousand



SOURCE: BUREAU OF LABOR STATISTICS

What's ahead: The April jobs report gives more fuel to the optimists who believe the U.S. economy will continue to expand. Last year was the best year for job gains since 1999. Then the winter of 2015 came. The economy barely grew in the first quarter this year. Many experts thought low gas prices would encourage Americans to spend during the winter months. Shoppers stayed home though as retail sales -- computers, clothes and cars -- were negative or near flat. The cold weather, strong U.S. dollar and West Coast port strike were the culprits for weak economic growth.



Although April's job gains were good, they probably aren't enough to convince the Federal Reserve to raise its key interest rate in June, experts say. The Fed hasn't raised rates in almost a decade, and a rate hike would be the bank's two thumbs up for the economy's health. Most economists believe the Fed will raise rates in September or later now. Still, April's good job news suggests the tide could be turning in the right direction for the U.S. economy.

RATE SUMMARY

Overall, in the past 30 days, rates worsened by an eighth.

*Conforming programs—an 1/8th higher ↑

*Jumbos—an 1/8th worse ↑

*Governments—an 1/8th higher ↑



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MORTY'S MAILBAG



There were no letters in the mailbag, this month.

Recipients of the newsletter are invited to Ask Morty any real estate or financing questions. The answer to the question will be answered either by phone or email and posted in the next issue for the benefit of all. Questions may be forwarded via mail phone or fax. Due to the high incidence of spam, if you email me a question it needs to be identified as a "real estate question" on the subject line of the email. (See front of issue for phone and fax numbers).

Morty's email address is....

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