THE SUNDAY TIMES

American Account: Companies act while others stand and stare

Irwin Stelzer Published: 2 December 2012

Politicians seeking sources of revenue with which to reduce the deficit will find that some of the sheep did not wait for the shearing

Markets move even when politicians don’t. Investors and consumers aren’t waiting for America’s politicians to decide whether and, if so, how to put our fiscal house in order. They are acting, now.

Many corporations, especially those in which founders hold large positions, have decided to declare special dividends, or to bring forward dividend distributions to avoid swingeing tax increases next year.

If the Bush tax cuts are allowed to expire, tax rates on dividend income will rise from 15% to 43.4% when the 3.8% Obamacare tax on the investment income of higher earners is included. Such hefty increases might be avoided, but some non-trivial increases there will be.

Markit, the data-gatherer, reckons that by year-end, some 120 companies will have taken steps to avoid next year’s higher taxes — four times the average. Wal-Mart, 48% owned by the Walton family, moved its dividend-payment date from January 2, 2013, to December 27 this year, and Las Vegas Sands, in which Sheldon Adelson and his wife own roughly half the shares, declared a special dividend in excess of $2bn (£1.25bn).

The effects of these moves are not confined to the recipients of the payouts. For one thing, companies declaring special dividends will enter 2013 with less cash with which to make acquisitions. For another, there will be more share buy-backs next year as companies seek to find a way to get cash to shareholders without paying dividends. “Dividends were the big thing . . . the new focus will be on stock buyback programmes,” portfolio manager Peter Andersen told the press.

Finally, politicians seeking sources of revenue with which to reduce the deficit will find that some of the sheep did not wait for the shearing — hundreds of millions of dollars will have escaped the increase in tax rates on dividends, the cash pocketed by shareholders by the time singing of Auld Lang Syne begins. Negotiators will have to look elsewhere to make up for this lost revenue.

Taxes on capital gains are also scheduled to soar if we jump off the cliff. There is some disagreement as to the effect of replacing the Bush-era rate of 15% with the 23.8% (20%+3.8% to fund Obamacare) rate that is now scheduled to replace it. There is some evidence that entrepreneurs who have built decent-size businesses, and private equity firms owning companies that have prospered, are trying to sell off these assets before the New Year, but the extent of such activity and the ability to complete complicated deals in the remaining days of the year are difficult to judge.

Investors holding shares that have chalked up gains may also be taking steps to beat the tax increases by selling now. Jeremy Siegel, the Wharton School finance professor, reckons that selling by investors eager to beat what the politicians have in store for them in 2013 is having a dampening effect on share prices. Nonsense, says Warren Buffett, perhaps the world's most famous investor, and a man who has won the heart of Obama by demanding to pay higher taxes.

Buffett says an increase in capital gains taxes won't depress share prices because, with interest rates at record lows, investors have no alternative to holding shares. "Where are they [investors] going to go?" Buffett asked Stephen Gandel, senior editor of CNNMoney, at a chance meeting.

In this disagreement between academic economists and the Sage of Omaha, so far the facts seem to be coming down on the practical man of affairs.

One group seems too browbeaten by the demonisation of their colleague Mitt Romney during the recent election to do more than watch the political show: private equity firms.

Much of the income of these investors, known as carried interest, now taxed at 15%, will be taxed at roughly 35% if the Bush cuts expire, and, I think, even if they don't. Although the industry has not fashioned a robust intellectual defence of its special treatment, its lobbyists still believe they can salvage some of their clients' advantages. But many leaders of the industry believe that this is a fight they can't win: these sheep are for shearing, and feel that bleating will do them little good.

All of this concentration on whether a dive off the cliff is in store, and on who will pay higher taxes, either to avoid that plunge, or next year when some more comprehensive deficit-cutting bargain is reached, seems oddly unrelated to what is going on in the economy. Consumers don't seem to be concerned about the fiscal cliff, and are more confident than they have been in almost five years.

They are less fearful of losing their jobs, have reduced their mortgage debt to the lowest level in six years, and are comforted by the continued recovery in the housing market. House prices rose for a sixth consecutive month in September (the latest month for which data is available), and are 3% higher than last year. Supplies of unsold houses are down and sales of new and existing homes are up.

Because consumers are local while businesses are international, bad news from recession-hit Europe, accompanied with pictures of mob scenes in Athens, affect businessmen more than consumers, who are enjoying America's economic recovery, tepid though its pace may be. But businesses, which have been cutting spending to and into the bone, might, only might, be coming out of their funk.

Orders for non-defence capital goods, excluding the volatile aircraft component, rose 1.7% in October. If business spending does increase significantly, a big "if", and if consumers continue to spend on cars and houses, we just might be in for an upside surprise early in 2013, something far better than the 1% growth rate or worse, recession, that many economists believe will make 2013 an unhappy new year. Were the economy to grow at something like 3%, the deficit would become far more manageable.

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