The Real Key to Economic Stimulation

Eliminating costly legislation empowers businesses—and more crucially, catalyzes job creation

Robert Knakal

I was pleasantly surprised by the tremendous feedback that I received from last week's column about the condition of our employment market and methods of stimulating job creation. I received dozens of emails from readers, most of which concurred with the perspectives presented, seeking additional clarity on these positions and further explanation of the benefits of each of the initiatives discussed. Given this unusual volume of response, I will delve deeper into each and provide additional color.

The first thing that really struck me was how aware the industry is, and how much participants in the industry really care, about the importance of job creation as a driver of both our economy and our commercial real estate market. Passion for this issue, and ideas for creating jobs, should be conveyed to elected officials whenever we have an opportunity to grab their ears. Regardless of your political tendencies, thoughtful conversation with legislators about this topic is extraordinarily important at this time.

With economic indicators mostly trending downward and job growth stalling, we are beginning to feel a tangible slowdown in commercial real estate investment sales volume. All indications, at this point, lead us to believe that both the dollar volume of sales and the number of properties sold in 3Q11 will be lower than the totals achieved in 2Q11. Friends on the office space leasing side of the business have expressed similar concerns that space absorption in 3Q11 has also started to slide as companies are growing increasingly concerned about the uncertainties that market conditions are presenting.

One of the more controversial suggestions in last week's column was the endorsement of repealing the new national health care law, commonly referred to as Obamacare. I think most people agree that it would be a tremendous social benefit if health care were available to all U.S. citizens. However, the delivery of this service, and how to pay for it, has been a political hot potato for decades. Clearly, health care costs are escalating at ever increasing rates, to the point where they have become one of the major expenses companies face today. The new legislation attempts to cover an additional 35 million Americans. It was simply disingenuous to present such a plan as something that would actually lower total costs and reduce the budget deficit.

Within months of its passage, double counting, miscalculations and gimmicks like using 10 years of revenue and seven years of expenses (imagine if we could run our companies this way) were disclosed and revealed that completely wiped out the purported deficit-reduction benefits of the plan. Furthermore, most government initiatives like this result in total costs that are many multiples of original estimates. Once the government gets its hands on something, waste, fraud and abuse is normally so rampant that costs get out of control very quickly. For an illustration, just think about New York's Off Track Betting operation. It was probably the only bookie joint in the history of the world that actually lost money.

The debate over the effect Obamacare would have on job creation and its economic impact was intense from the get-go. The president indicated that it would be stimulative to both and Nancy Pelosi went so far as to say that the law would create more than 400,000 jobs almost immediately. Business leaders, on the other hand, argued that the additional economic burden imposed by the law would slow down hiring. After all, had any one person actually read the entire 2,000-page law and could anyone actually project what the true economic impact of this legislation would be on companies? Most rational business leaders were left with no choice but to believe that costs would rise, and rise significantly. Could tax increases to pay for this legislation be far behind?

An analysis of net job growth before and after the passage of Obamacare shows that job creation slowed dramatically after the adoption of the new law. According to a U.S. Chamber of Commerce study, about one-third of business owners indicated that the new law was either the primary or second-most important reason why they were not creating more jobs. Adding unknown new costs to the total expense of creating a new job is a significant deterrent to the employment market. These new burdens are created by forcing employers to provide costly government-approved insurance or pay a fine.

The new legislation also discourages small businesses from becoming midsize businesses by requiring companies to comply once they grow to 50 or more employees.

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The evidence could not be more clear that the new law is discouraging job creation. Unfortunately, few people on either side of the aisle, believe that this president will in any way alter his signature legislation simply to bolster the economy. It is interesting to note that approximately 1,400 exemptions to the law have been granted, mostly to unions and other supporters of this administration. What this means is that the costs associated with this program will be shared by an even smaller group of unlucky companies that could not secure an exemption.

Entitlement reform was another key issue mentioned in last week's column. What I meant by that is that programs like Social Security and Medicare must be fundamentally changed for them to be sustainable. It was interesting how, in the rhetoric leading up to last week's special elections, we heard over and over again that some candidates wanted to "protect Social Security and Medicare." This is akin to standing back and admiring the parts of a sinking ship that remain above water. Last year, Social Security paid out more than it took in for the first time in history. It is projected that, by 2032, the program will be bankrupt and even that extrapolation assumes the $2.67 trillion raided from the Social Security trust fund by the government to pay other expenses will be paid back.

Moreover, entitlement spending now makes up about 40 percent of all government outlays. If programs stay on their present course, by 2049 entitlement spending will reach 100 percent. Clearly, this course is not sustainable and very difficult decisions have to be made in terms of reforming these programs so that they will still be around years from now. Long-term economic prosperity is simply impossible without these fundamental reforms.

Repealing or significantly altering the Dodd-Frank financial regulation law was also suggested. The Sarbanes-Oxley accounting rules have added billions of dollars to the cost of doing business for companies across the nation. The 16 Sarbanes-Oxley regulations that businesses must comply with have forced companies to alter their business practices with little positive effect. Dodd-Frank is Sarbanes-Oxley on steroids, containing over 200 debilitating new regulations and essentially perpetuating "too big to fail" by reinforcing a prevailing system that creates incentives to become too big to fail. This is a classic example of an over-swinging pendulum.

With regard to job-creation strategies, I suggested that signing free trade agreements would be beneficial. We should be doing what we can to incentivize trade and investment with foreign countries and to reject protectionism. Drafts of the free-trade agreements with South Korea, Colombia and Panama have been around since President Bush was in office and have been collecting dust since. Signing these and exploring additional opportunities for such agreements would be stimulative as more options are made available for domestic entities.

Part of this strategy should include avoiding a trade war with China. We have heard talk about implementing such a strategy from both sides of the aisle. While this position may be intended to win over working-class districts in Pennsylvania, Ohio and Michigan, giving Americans the impression that a trade war will bring back jobs that have been shipped overseas is offering false hope.

A component of the free-trade strategy should include reducing or eliminating the duties U.S.

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producers pay on imported raw materials and components they need for manufacturing. This step would instantly increase the competitiveness of U.S. goods domestically and internationally. In 2010, U.S. Customs and the Border Patrol collected about $30 billion in duties on $2 trillion of imports. More than half of these imports were ingredients for manufacturers such as chemicals, minerals and machine parts. Rather than negotiating a reduction in foreign tariffs on behalf of U.S. exporters, simply reduce the import tax on essential raw material. This would not only have the same impact as improving foreign market access but has the added benefit of improving competitiveness at home. These measures would be beneficial to continued U.S. economic growth.

Encouraging multinational companies to repatriate profits made overseas would add significantly to job creation. Our tax code, which imposes higher taxes than just about any other country, liscourages such actions and makes operating overseas extremely attractive or our largest companies. It is estimated that companies operating abroad have about $1.2 trillion sitting in overseas accounts. Supporting the Freedom to Invest Act of 2011 would allow these companies to take advantage of reduced tax rates, encouraging them to inject these dollars into the U.S. economy by investing in jobs, plants and equipment here at home. The time frame within which this capital could be advantageously repatriated could be controlled to incentivize job creation immediately.

The woes within the U.S. housing market have created a tremendous drag on our economy. For most Americans, their home is their major asset and the amount of equity within that home creates a significant wealth effect that impacts consumer spending greatly. Government intervention in the housing market has been unprecedented, including the first-time home buyers tax credit, which simply perpetuated getting people into houses they couldn't afford, and the foreclosure moratorium. Both of these initiatives have impeded the clearing of the market that is necessary before any traction can be attained in a housing recovery. With a significant oversupply of housing nationally, there is a need for increasing demand, but this demand must be solid demand from buyers with real equity. IRA, Keogh and 401(k)s are presently locking up about $15 trillion. Access to these funds prior to retirement comes with a stiff 10 percent penalty in addition to regular taxes. Allowing individuals to access this capital to purchase homes (with stiff restrictions) could be just what the housing market needs to get jump started. With significant equity invested in these homes, the risk of default drops substantially. For evidence of this, simply look at the strength of the Canadian housing market, which requires at least 20 percent down payments n most cases.

Relaxing restrictions on the oil and gas ndustry would also be very stimulative to ob creation. The drilling moratorium imposed after the BP oil spill dealt a harsh low to the industry. The discovery of a eep reservoir estimated to contain at east one billion barrels of oil in the Julia eld in the Gulf of Mexico has tremendous otential. This was the largest oil discovry in over 10 years. ExxonMobil needs o have permits renewed to develop this eld. Thousands of jobs would be creatd immediately if the Department of the terior were to cut through the red tape nd renew these permits. Increased approvals for natural gas exploration would ot only decrease our dependence on forgn oil but would similarly create tens of ousands of jobs very quickly.

There has been much talk about the enefits of addressing the country's inastructure as a way to stimulate the onomy. While there are some good arments for this approach, the key to e magnitude of the benefits will be in the nature of the implementation. The infrastructure bank, referenced in the president's jobs speech a couple of weeks ago, calls for about $30 billion that can seed hundreds of billions of "grants and loans" to rebuild roads, bridges, ports, broadband lines and smart grids. These would get done via public/private partnerships and is, oddly enough, supported by both the Chamber of Commerce and the AFL-CIO. This fact alone should raise a red flag. Unfortunately, this bank would carry an implicit subsidy for its debt based upon an implicit government guarantee. This appears to be the Fannie Mae/Freddie Mac model of a government sponsored enterprise applied to public works projects. Any entity like this would inevitably become politicized, devolving into a vehicle for the political allocation of credit. Taxpayers would get less for their money as these federal projects would have to follow Davis-Bacon Act rules that inflate costs by 10 percent to 30 percent depending on the project and location. A better idea would be to have more control of these funds at the state and local levels so that users can decide exactly what they want. Projects that pay for themselves in the form of tolls or usage fees would be most preferable.

Lastly, entrepreneurs and small businesses need to be empowered. New start-ups should be encouraged and incentives need to be created to catalyze small business growth. Relaxing immigration rules for foreign entrepreneurs who will be hiring American workers could jump-start job creation. To encourage investment in these, as well as domestic, start-ups, capital gains tax relief for early-stage investments would reduce the cost of capital for these firms and allow them to hire more workers. As these companies grow, barriers to I.P.O.'s can be reduced if shareholders had the ability to opt out of Sarbanes-Oxley regulations. If investors are willing to live without the "protections" this regulation provides, they should be allowed to do so.

When it comes to the underlying fundamentals of commercial real estate, nothing comes close to the importance of job creation. Whether these ideas or others are implemented, something needs to be done to stimulate employment. These new jobs will fill our office buildings and those who receive them will buy our condos and fill up our rental apartment buildings. These employed workers will shop in our retail stores and this new demand will drive industrial production, stimulating our manufacturing facilities. It was always said that real estate is all about three things: location, location, location. Today, it appears more to be about jobs, jobs, jobs. Let's hope we get some.

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