

Date - February 23, 2013

NOW TO THE QUESTION OF SEQUESTER - Only because you asked.....

Sequestration is the employment of automatic, across-the-board spending cuts in the face of annual budget deficits.

This uniform percentage reduction is applied to all programs, projects, and activities within a budget account.

Sequestration causes a spending reduction in FY13. Afterwards the defense budget starts growing at a rate of 10% per year per the [Cato Institute](#). The problem is the sudden cuts made in January to meet the sequestration law would be across the board and without much thought to the long-term consequences. If cuts are made to everything, critical programs will be delayed throughout the Federal government. **The primary impact of sequestration is not real cuts but is lower spending growth.** However, in January many programs will be reduced or delayed.

There has been [little to no guidance from Federal agencies](#) as to where the sequestration cuts will be made.

Sequestration can also occur under the Pay As You Go Act of 2010, with some exceptions. Under that law the federal government must continue to pay out **for Social Security, unemployment and veterans benefits, and the low-income entitlements such as Medicaid, food stamps and Supplemental Security Income.**

Medicare is subject to automatic cuts under sequestration. Its spending cannot be reduced by more than 2 percent, however.

Under the assumptions required by the STA (The Sequestration Transparency Act), the sequestration would result in a 9.4 percent reduction in non-exempt defense discretionary funding and an 8.2 percent reduction in non-exempt nondefense discretionary funding. The sequestration would also impose cuts of 2.0 percent to Medicare, 7.6 percent to other non-exempt nondefense mandatory programs, and 10.0 percent to non-exempt defense mandatory programs.

That just about covers the “Trauma” being generated by our politicians!

#### Answer and Comment:

My sense is that the best way to describe this entire fiasco is to call it a “Tempest in a Teapot”, which is about what it is about . . . lots of noise, and little final impact on the overall system.

From the way the market has reacted to all the turmoil, it seems pretty clear that there are few “believers” in the “coming chaos” theory.

I follow a lot of monetary aggregate numbers to try to understand what is really happening to the underlying economy. These numbers are saying that there is a momentum building in the US economy, in the private sector, and that there is going to be increasing private sector economic growth.

This is a time when you place your confidence in the private sector, and say goodbye to federal spending. Government spending can no longer impact our economy positively. On the other hand, an across-the-board cut in government spending may well have an inverse impact to what economists are forecasting. The reasoning is somewhat convoluted, and has not been dealt with from an academic

standpoint - that I know of. That being said, the reasoning seems pretty sound to me - the concept of an inverse multiplier attached to government spending (a negative multiplier).

Anyway, whatever happens when the sequester takes place - which surely it will - life will go on; government spending will be reduced near term, and our private economy will know that it can begin to spend again, planning for the future.

I am in hopes that the Sequester will provide an opportunity for investors to buy into the stock market at lower prices, to allow us to move money out of fixed income assets and into equities.

Over the coming 5-10 years, we should see a long term economic growth curve that will see stock prices increase in value, companies growing their revenues, and profits improving throughout the US economy.