**RSG WORLD Economic Brief**

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## Key US Statistics

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<tbody>
<tr>
<td>Dow Jones Indus. Avg.</td>
<td>9,180.69</td>
<td>9,712.28</td>
<td>9,972.18</td>
<td>9,712.73</td>
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<tr>
<td>NASDAQ</td>
<td>1,698.52</td>
<td>2,122.42</td>
<td>2,154.47</td>
<td>2,045.11</td>
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<td>S&amp;P</td>
<td>954.09</td>
<td>1,057.08</td>
<td>1,079.60</td>
<td>1,036.19</td>
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### Other Rates

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<tbody>
<tr>
<td>Consumer Price Index</td>
<td>202.9</td>
<td>218.8</td>
<td>215.8</td>
<td>216.0</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>4.5%</td>
<td>6.2%</td>
<td>9.7%</td>
<td>9.8%</td>
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## Recent News and Analysis on the United States Economy

**Ford** has finally begun making a profit again, Reuters reports. Reuters reports that Ford, the only American car manufacturer to avoid bankruptcy and bailout money, now projects that it will be “solidly profitable” by 2011, though its debts remain sizable. Ford hadn’t seen a quarterly profit in North America since the first quarter of 2005. GM and Chrysler, meanwhile, are still trying to recover.

The Federal Reserve’s Beige Book reported this month that there have been some improvements in the manufacturing and housing sectors. However, the market for loans and commercial real estate has worsened, indicating a continued reluctance to increase investment. Employment, wages, and prices are also unchanged, as is consumer spending.

The Federal Reserve further reported that its Fifth District (which contains the state of Virginia) has seen an increase in tourism and in the service sector. While the report attributes the increase in tourism in part to the weather, the increase in services was not similarly attributable to any flu outbreaks (though demand for healthcare did increase slightly). Within the service sector itself, employment only increased at some financial services or technical companies, while other firms saw little change. Meanwhile in the housing sector, one real estate agent was quoted as saying that “pristine credit is practically required to get financing[,]” indicating that banks are still quite cautious after last year’s disaster.

Meanwhile, the International Monetary Fund (IMF) reports that while the United States and other first-world countries are starting to recover, their economies are now dependent on the large amounts of stimulus money to keep them going. The IMF further reports that growth is likely to be quite slow for a while, and unemployment has yet to reach its worst. The IMF notes that the slow growth in employment and consumer spending in the United States will adversely affect those nearby nations that are dependent on tourism from the United States (e.g., many of the...
Caribbean nations). Even after the United States recovers, however, the IMF expects that it will be saddled with a **great amount of debt**, which will continue to plague the country far into the foreseeable future.

### Controversies in the US Economy: Executive Pay Caps

The **Federal Reserve** recently announced that it wants to **limit the pay offered by banks** and other lenders, the Wall Street Journal reports. The Federal Reserve said that it was introducing new regulatory procedures that will routinely **investigate the pay packages** offered by U.S. banks. The new regulations will **apply to all lenders** in the U.S., including small banks and U.S. subsidiaries of foreign corporations. The Fed further announced that it will **review the pay offered by “28 large, complex banking organizations,”** to determine whether any of these is overpaying its executives **relative to the others**, and to encourage policies that **base compensation on risk-aversion** rather than profits alone.

#### Arguments in Favor

Jeannine Aversa of the Huffington Post argues that the Fed’s regulations are necessary to **prevent risky investments**, implying that similar regulations might **have prevented the current financial crisis**. Aversa echoes the Fed’s worries that banks **frequently reward current gains**, regardless of any long-term hazards. Aversa also notes that the Fed is seeking **public input** about **possibly banning certain practices**.

#### Arguments Opposed

Dave Mason of the Heritage Foundation argues that such restrictions have historically had a **tendency to produce unintended side effects**. Specifically, he argues that capping executive pay will make it **difficult** for companies to hire **qualified executives**. He further argues that these caps are **overbroad** and will **hurt small banks** that were not responsible for the crisis, as well as managers at local banks.

#### Questions to consider:

1. What effect will capping executive salary have on the market for highly talented executives? For untalented executives (a substitute for highly talented executives)? What if the supply and demand for talented executives is very elastic? Very inelastic? What if the supply of these executives is very elastic and the demand is very inelastic? Vice-versa? Which of these elasticity scenarios do you think is most likely (taking into account the likelihood or unlikelihood of these executives working in other industries or other countries)? What might the effects of this scenario be? How might your calculations be different if companies were unable to distinguish talented from untalented executives? Which of these scenarios do you think is more likely?

2. The Fed also said it would try to reward risk aversion. From a macroeconomic perspective, at what point in the business cycle do businesses tend to be overly risk-taking? At what point do they tend to be overly risk-averse?