The 25-year bull market

by Jack_Kemp

The great "existentialist philosopher" Yogi Berra once famously said, "history is just one damn thing after another." Of course the antithesis of Yogi was George Santayana, an equally famous philosopher who said wisely, "those who neglect the mistakes of the past, are doomed to repeat them."

As I write these words in the dog days of August, with all the bad news of the subprime mortgage market, liquidity crunch and a fluctuating stock market, it's important to keep things in perspective and heed the words of Santayana, not Berra.

In other words, we should turn to history and its empirical evidence, and not give in to irrational decisions based on fatalism and the neglect of real history.

One such historical fact to remember is that the past 25 years have been the best stock market for investors in U.S. history. As the widely respected New York Times financial journalist Floyd Norris wrote, (and blogged) recently, the Dow Jones industrial average hit bottom on Aug. 12, 1982, at 776.9, while interest rates were at 15 percent.

Since that date, the compounded rate of return from the last quarter of 1982 until this summer, circa 2007, has been 11.8 percent. Taking into account inflation, the rate of return has been 8.5 percent. Norris pointed out this quarter of a century is the best ever in U.S. history.

This remarkable achievement didn't just happen, it was the result of policy decisions in the 1980s, 90s and more recently - confirming the fact that lower tax rates on capital and labor, sound monetary policies, with open market initiatives and liberalized trade leads to stronger economic growth and rising values in equities.

We neglect these lessons at our peril.

As economist Art Laffer pointed out recently, "if these pro-growth policies that have led to our 25-year bull market are reversed, don't be surprised if our financial gains and competitive edge quickly disappear."

Make no mistake dear readers, listening and watching the presidential candidates in the Democratic Party debate over the economy, I believe they are all headed in the direction of higher tax rates, and protectionist trade policies. Have they all forgotten John F. Kennedy in the early 1960s and indeed Bill Clinton in the 1990s? Where, oh where is the pro-growth, pro-trade, pro-internationalist wing of the Democratic Party?

Except for Joe Lieberman, they apparently no longer exist.

Some history for all of us, 25 years ago, there was a mighty revival of classical economics led by two young economists named Robert Mundell of Columbia University and the aforementioned Art Laffer then a professor at USC.

They posited that the only answer to the Keynesian dilemma of simultaneous inflation coupled with recession was to restore sound money and sharply reduced marginal tax rates on both capital and labor. In other words, a hardened dollar, combined with lower taxes, reduced regulation and liberal trade policies would spur economic growth and jobs while combating inflation.

Theses two economists, took me, a GOP Congressional backbencher from Buffalo, N.Y., and turned me from a rather orthodox conservative in the Eisenhower wing of the Party, into a radical tax rate cutter and classical liberal on trade and globalization.

Candidate for President Ronald Reagan in 1980 turned out to be the one (and only) candidate among Republicans who fully (and firmly) bought into this neo-classical school of supply side economics because he'd been educated at Eureka College in the late 1920s at the height of the teachings of the 18th century Adam Smith and David Ricardo.

Most people forget that when Ronald Reagan took office the top tax rate was 70 percent and the capital gains rate was near 50 percent. The soft money policies of the Carter administration had left us with rising unemployment and inflation rate of 16 percent, (i.e. stagflation.) Trade was virtually shut down because of the mercantilist trade policies of "the left" in the U.S. and those of "the right" in Japan and "old Europe".

Despite several exogenous events from Y2K to 9/11, from Hurricane Katrina and the rising defense spending in the war on terror, the U.S. economy is the model for the world as more and more nations from Brazil and India to Russia, China, and Eastern Europe begin to emulate our entrepreneurial pro-growth economic ideas.

As I've said, August 1982 was the real beginning of the lower tax rate, lower interest rate and lower tariff policies that turned out 25 years later to have been the policy prescriptions that brought us this remarkable record. As I write this on Monday, the Dow is at 13,335 - not bad!

So to summarize Santayana, yes, we must learn from our mistakes, but equally important we must remember those decisions that from Reagan to Clinton to Bush have given the world a road map to prosperity.

We've come a long way and we've still got a long way to go in lifting more people out of poverty, creating more minority business owners and to further democratize our capitalistic system. So to both Democratic and Republican candidates for the presidency: let's hear a real debate about growth and prosperity and not redistribution of wealth and soaking the rich.

Jack Kemp is founder and chairman of Kemp Partners.