

The Kiplinger Letter

FORECASTS FOR MANAGEMENT DECISIONMAKING

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Dear Client:

Washington, April 16, 2004

A slew of business tax cuts are coming, riding the coattails of must-pass legislation to repeal an export subsidy deemed in violation of world trade rules. European Union tariffs imposed in retaliation for the U.S. subsidy aren't having a substantial effect yet. But...

Later on this year or sometime next... Congress will give legislation the nod.

TAXES

Certain to be included in the package: A corporate tax rate cut, from 35% now to 32%. Maybe not for all corporations, though. Some lawmakers want to restrict the lower rate to manufacturers...multinational and domestic. And an extension of the R&D tax credit.

But there's a full sleigh of other goodies being mulled as well. Extending tax breaks for employers that hire welfare recipients. Continuing an expensing tax break for small businesses till 2007.

It permits companies to expense up to \$102,000 of new assets each year. Exempting more small businesses from the alternative minimum tax. Simplifying S corporation taxes and expanding eligibility rules. Allowing unprofitable firms to carry back losses for three years.

Plus energy-saving incentives, new or expanded: Tax credits for improving the energy efficiency of homes and commercial buildings. For using solar power or buying a gasoline-electric hybrid vehicle. Also for makers of energy-efficient appliances. And the reinstatement of breaks for nonconventional energy sources...wind, biomass, shale, etc.

Also breaks for businesses starting up in depressed rural areas. And for specific industries and occupations...farmers, teachers, shipbuilders and employers of military reservists. Even car dealers that closed their Oldsmobile franchises when that make was discontinued.

The bottom line: Many lawmakers want to load up the tax bill knowing full well that Congress must repeal the export subsidy. But not all the goodies will survive. Deficit hawks will dig in to limit any loss of revenue, forcing lawmakers to make tough choices.

Given all that, there are more reasons to delay than to hurry. Business interests are divided. Some want broader tax relief, others want to tailor the breaks to address their specific problems. Some Republicans are wary of passing any bill before November, lest Democrats claim it'll prove the GOP's only aim is to aid business. And President Bush is staying on the sidelines. He's content to let Congress thrash out the details of this particular tax bill.

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TRADE
AND
POLITICS

Trade agreements are low on Congress' agenda this year.

The prevailing view among most lawmakers is to avoid anything that could be seen as encouraging imports and reducing U.S. jobs. Only two bilateral trade deals have a chance in Congress this year: One just negotiated with Australia and another concluded with Morocco.

But that's not deterring Bush from pursuing deals far and wide. He's about to open free-trade negotiations with Panama, Colombia and Thailand and is eyeing agreements with other countries as well.

The president believes that more-open trade motivates nations to enact economic and democratic reforms. Improving trade relations often also helps bolster political, diplomatic and military ties.

And he hopes that bilateral talks will spur multilateral pacts, such as the Free Trade Area of the Americas plan. The broader talks have stalled for now, but their revival is important to U.S. firms.

Bush is taking a political gamble by pushing free trade while many Americans fret about sending more jobs and profits abroad. He figures more folks will see trade pacts in a more favorable light as the economy improves, making it easier for Congress to OK deals.

SHIPPING

Are warehouses becoming obsolete? For more and more firms, yes.

They're turning to new distribution strategies that allow them to ship products to customers directly from factories or port terminals.

Soon, about half of all products will sidestep warehouses.

Nearly 40% already do. Low-cost satellite and Internet tracking systems are helping to make it possible for companies to cut their delivery times and hold down costs. Firms that receive goods directly include Wal-Mart, Benetton, Ann Taylor, Barnes & Noble and many small specialty retailers.

"Bypass" experts can help. Such firms include GeoLogistics, FedEx Trade Network, UPS Supply Chain Solutions and Argix Direct.

The trend is not good news for warehouse operators, of course. Or for commercial real estate in general. Declining demand for storage will be felt the most in cities such as L.A., Chicago, Atlanta and NYC. Also in Albany, N.Y., Winchester, Va., and other distribution centers.

A new transportation technology promises to reduce freight costs. It's a hybrid rail-truck system from RailRunner NA, of East Point, Ga., that enables railroad wheels to be slipped under truck cargo containers. Shippers using the device won't need large cranes to load containers onto railcars, potentially a significant savings of time and money.

Grain shippers are likely to find it particularly useful as quality control concerns drive up demand for containerized shipments.

SOFTWARE

Renting business software instead of buying it can save big.

And it offers more flexibility to pick and choose among products, getting exactly what you need for only as long as you actually need it. In today's buyer's market, most software vendors will work with you.

By the end of the decade, flexible terms will be the norm, with firms renting software on a month-to-month or per-use basis.

More-attractive standard licensing plans are also helping firms. For example, Microsoft is offering contracts that allow businesses to spread out the cost of software purchases over three to five years.