

Economic Views for Investors

by Roger Nightingale

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In economics, the wish is often father to the forecast

In late spring and early summer, the world economy was still deteriorating, but at a markedly slower pace than previously. Put in quasi-mathematical terminology, the *first* differential of GDP was awful, but the *second* was excellent. Forecasters, lacking arithmetical competence, made light of fine distinctions of this sort. Things were getting better, they said. A full scale recovery was imminent.

Drowning men clutch at straws; economists at second differentials

Was their euphoria justified? Probably not. The improvement in the data had been largely a function of the turnaround in inventories. The steep decline in production at the end of 2008 and the beginning of 2009 was a consequence of industry's urgent need to raise liquidity at a time when pusillanimous bankers were cutting their loan books. The shallower decline more recently had been the result of spent-out consumers tightening their belts.

In reality, though one constraint has gone, a second remains

One negative had possibly run its course, but the other probably hadn't: inventories were no longer being savaged, but the outlook for retailing remained bleak. It wasn't the greedy lender who was inhibiting activity, but the penurious spender. Credit was available to those who could afford it, but pay settlements were falling and unemployment was rising. In much of the world, supply and demand had been brought close to equilibrium: stability was restored, but it was stability at a very depressed level.

The performance of emergers is, as usual, high beta and lagged!

And what was to be made of the apparent collapse in activity in much of the developing world. It had been fashionable last year to suppose that *Emerging* countries would consistently fare better than *Emerged* ones. Nonsense, of course; and they haven't. But the extent of their recent debility has nevertheless taken analysts by surprise.

Will China and India buck the trend?

Estonia and Latvia make the point in Eastern Europe; Brazil and Mexico in Latin America; Hong Kong, Singapore and Korea in Asia. The numbers in each have been devastating. And the chances are that China and India will shortly repeat the message.

Extremely unlikely. The numbers are going to surprise on the downside

For the moment, official sources in Beijing and Delhi stick to the fiction that activity is strong, but nobody pays much attention. Data relating to imports and tax collections tell a different story—and one that's not pretty. Growth at the end of last year seems to have been negligible and, early this year, modestly negative. What worries the establishment, of course, is the risk of social dissent. Reform is popular when it yields rising living standards. When it doesn't, there is a threat of Reaction, possibly of Revolution!

There'll be political implications; some of them profound

Governments have to ask themselves whether they are facing recession or depression. Whether their economies' debility will last for a couple of years or a couple of decades. Whether there will be psephological repercussions for just one election, or for many. In public, understandably, they presume recession. But in private? Do they agonise about the alternative? Do they regret their earlier insouciance? Almost certainly!

And the corporate landscape will change

How different might the world be after a generation of disappointing progress? How many major corporations would have gone to the wall in the meantime? Lots! General Motors was the largest automobile manufacturer in the world for a hundred years, but seems now to be on its last legs. It's possible that an unrecognisable rump of the old behemoth will survive for a while longer, but it's more likely that the whole thing will disappear.

The only fixed star: hateful lawyers

It'll not be alone. Whole swathes of manufacturers and banks, media companies and software houses will accompany it. Untroubled by a sequence of recessions, they'll be extinguished in a flash by a single depression. It's those that can most easily organise cartels that'll find life most comfortable. Sadly, therefore, lawyers (who turn protectionism into an art form) look set to be with us for a few more millennia.

Which countries will be promoted to the Premier League?

And will the "Who's Who?" of nation states be much changed? It wasn't by the thirties. The commodity producers took a sizeable hit—Argentina ruined and Australia disadvantaged—but most of the rest survived with their rankings little altered. Was that because of the war? If there'd been no conflict, or if its outcome had been different, would things have been as recognisable?

Which demoted to the Championship?

The curse of living in interesting times! Happily, securities markets are appreciating. Progress may be erratic, but it's likely to be sustained. A surge in the second half of 2009; more modest advances thereafter. The pensioner deserves a break!

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