

Allen Sinai: Jobless Recovery and the Failure of Current Economic Policies

By Robert Huebscher
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As the Democratic leadership in Congress has looked for ways to simultaneously create jobs and reduce the deficit, a key person they have turned to and continue to rely on is Allen Sinai.

Sinai, however, has not been able to offer any creative solutions to this potentially unsolvable dilemma. Moreover, he believes a solution is now more difficult because America's role in the global economy has become increasingly marginalized. That trend something "Americans don't yet fully grasp," Sinai said in a recent talk. "It has been and is still

happening."

"Longer-run, it's looking like America could be in relative decline," Sinai said, pointing to the recent rise in gold prices as a reflection of that outlook.

Sinai delivered a talk titled "After the Crises: Recovery and Reality," last week in Lexington, MA. He is the president of Decision Economics, the economic research firm he founded in 1996, and has advised both Democratic and Republican administrations.

The US economy is in recovery, albeit a jobless one, and its shape will be an "L" with an up-tilt at the bottom, he said – in other words, the recovery will be slow and uneven. "It may look like a recovery to some, but not to those looking for jobs," he said.

Anemic growth but powerful earnings performance

Sinai discounted the possibility of a v-shaped recovery because of a lack of consumer spending. "Consumers will spend far less for far longer than ever before, and they will save far more for far longer than ever before," he said – as many as four or five decades.

GDP growth will soften in Q4 and the first quarter of next year, Sanai said, and will be 2.5% to 3% in 2010 and a little less in 2011. He is worried, as things stand, about another recession in 2012 once the \$787 billion stimulus package runs dry.

Global economic growth will go from its current rate of -2.1% to 3.5% in 2010, led by the rest of the world, he predicted. Brazil, China, South Korea, Taiwan, the Philippines, and much of Asia are all having a v-shaped recovery, he said.



The UK will grow slowly, although most of Europe will grow faster, he said. Growth in Russia and the Middle East will depend on oil prices.

The cyclical processes within the US economy that were in a state of collapse have now stabilized, he said: housing, consumer spending, and spending by corporations on inventory and capital goods.

Earnings performance by American companies was “absolutely incredible” in the third quarter, according to Sinai. Those earnings were down only 0.2% in Q3 year-over-year, versus Sinai’s projection of a decline of 8%. Only 43 companies in the S&P 500 lost money.

“Under the mantra of maximizing shareholder value, companies did what they are very good at – slashing expenses,” he said, specifically slashing jobs. He is not sure if they will hire those people back, though.

Earnings will grow year-over-year because results in Q4 of 2008 and Q1 of 2009 were so poor, Sinai said, and this is the first time in four years that has happened. Earnings growth on the S&P 500 will be five to six times his projected GDP growth of 2.5% to 3%, he said.

He noted that the performance of the US stock market over the last year – it’s up 16% – has been dwarfed by the performance of virtually all foreign markets, with the exception of the UK and Japan.

The jobless recovery and its political implications

The disconnect between rising earnings and strong market performance on the one hand, and rising unemployment on the other, could go on for a “long time” according to Sinai, creating a major political and social issue. “Those who created the problems [the financial institutions] are benefiting,” he said, “and the average worker is not.”

Unemployment will peak between 10.5% and 11% and will stay high for a long time, Sinai said.

He called this the “mother of all jobless recoveries.” (When he gave a similar presentation to Nancy Pelosi, however, he called it the “father of all jobless recoveries,” he said.)

For the first time since World War II, Sinai said, compensation, which makes up 40% of real disposable income, has declined for six consecutive quarters.



Add to that the huge loss of wealth in the housing and stock markets, the lack of optimism among American consumers reflected in sentiment indices, and the lack of consumer credit availability, and the message is clear: Consumer spending can no longer grow at its historical rate of 3.5%.

“The new reality for how the US economy will grow over the next few years will be set by the consumer, and it’s going to be a slow, on average, pace of growth,” he said.

Obama’s approval ratings will go down, Sinai said, “as Americans look at what has happened and wonder what will happen next.”

“One of the realities is that the rest of the world is moving ahead very quickly and our future is very much uncertain.” The relative decline of the US has accelerated as a result of the crisis, he said.

General complacency is partly to blame. Sinai cited an attitudinal shift among Americans, who are now more content with slower growth, even if it puts us on the trajectory followed by the Japanese and European economies.

The failure of current economic policies

Although Sinai said he voted for Obama, he had virtually no positive things to say about the administration’s economic policies.

The first stimulus plan – George Bush’s \$170 billion tax rebates – “did nothing except put us another \$170 billion into debt,” and he is not sure whether Obama’s \$787 billion stimulus will do much better. “It may be doing the same thing.”

Monetary and fiscal policies have not been directed at the consumer, Sinai said. “We don’t think the medicine that’s being applied is really going to rev up the consumer,” he said, although over the long run it “may allow us to get our house in order.”

Sinai said government policies that recapitalized banks with the goal of forcing them to lend were based on “false assumptions.” Similarly, policies cannot force companies to hire through measures such as job credits.

“We could tax corporate profits away – and we may well do that – but I’m not sure that solves the problem of getting people back to work.”

He said George W. Bush’s tax reductions after taking office and again in 2003 revived growth and employment following the 2001 recession, although they are widely discredited because of Bush’s unpopularity.



Since monetary policy options have been exhausted, help will need to come from the fiscal policy realm, he said. Fiscal measures thus far have been “politically disappointing” but, given the time lag in the processes, he said we won’t know for a while whether they will work.

“My guess,” he said, “is that they are not working.”

Two-thirds of the \$787 billion stimulus was for outlays and social spending, much of it for “things we need to get done,” Sinai said. But those things did not have the “economic leverage” in terms of growth and job creation that other policies might have had, he added.

Sinai said Congressman Dave Obey (D-WI), “a sincere and very good legislator,” wrote the stimulus bill and was able to incorporate virtually everything that had been on the Democrats’ wish list for years and, in some cases, decades.

That stimulus was advertised as something that would create jobs, which Sinai said constituted “fallacious economic reasoning.”

“We have a spend-and-tax thrust going on in policy,” he said, adding that he expects the \$787 billion stimulus package to be followed by tax increases.

He also expects legislation to spur job creation, but doubts it will be “curative.”

Healthcare legislation will pass, Sinai predicted, something he said was long overdue and desirable, but he cautioned that it could be bad for the economy.

The decline of the US and the rise of gold

Global investors, perhaps cynically, Sinai said, are asking whether the US is repeating failed policies previously tried in the UK, Europe, and Japan, where governments bailed out institutions and, once they got involved, could not get out.

“Investors have not seen good results with this approach in other countries,” Sinai said.

Decoupling is the new reality, and perceived risk in Chinese, Asian, and other emerging markets is decreasing, making them more attractive candidates for investment.

A self-confessed gold bug, Sinai is bullish on the metal at \$350/ounce. He views it as a “buyable” alternative asset that has special significance now because of the declining role of the US economy.

Gold, though, is exhibiting some bubble-like characteristics, including increasing demand from individuals and a rapidly rising price.



The recent rise in the price of gold, Sinai said, stems in part from expectations the US will debase its currency, through monetary and fiscal policy measures.

“Fundamentally, beneath that is a question about the credibility and viability of the United States,” he said.

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