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First Trust

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Monday Morning Outlook

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Things to Be Thankful For

Some people say recessions are inevitable; others say they are healthy (necessary) to clean out the system and clear the way for the next expansion. Finally, while many blame greedy capitalists for pushing things too far, there are some who believe that the current recession is something we deserved (or earned) because so many lived beyond their means.

No matter what you believe, recessions are never fun. Beneath all the statistics and data are real people facing real challenges. The unemployment rate, now 6.7%, is headed to about 8% by late 2009. In the fourth quarter, real GDP will drop the most since the brutal recession of 1981-82 when, over the course of only two years, Paul Volcker reversed 20 years of inflationary monetary policy.

But it is not just the speed of the collapse that is so scary; it is that our current generation has little experience with economic pain. Between 1965 and 1982, the US economy was in recession one out of every three years, inflation hit double digits and the unemployment rate peaked at 10.8%.

Since 1982, the US has been in recession just one out of 16 years, the unemployment rate bottomed at 3.8% in early 2000 and then at 4.4% in early 2007. In other words, a wobbly economy today *feels* much worse to the average American and politician than it did 30 years ago.

So we have a real schizophrenia today. People are going to the mall for holiday shopping, parking hundreds of yards away and waiting in long lines to check out. But then, these same people go to parties and argue about whether the Obama economic stimulus plan should be $500 billion or $1 trillion. It feels so bad that President Bush is justifying his economic intervention by saying that “I’ve abandoned free market principles to save the free market system.”

What’s important to recognize is that even at the bottom of the current recession, sometime in mid-2009, the living standards of the typical American will still be amazingly high. In fact, even an aggressive contraction in real GDP will leave per-capita real GDP above 2005 levels.

Now, we did not have 8% unemployment back in 2005, but that kind of jobless rate is not unusual for recessions. The unemployment rate peaked at only 6.3% in the recession early this decade but peaked at 7.8%, 10.8%, 7.8%, and 9.0% in each of the previous four recessions, respectively, dating all the way back to the 1973-75 recession.

Meanwhile, most of the lessons of the Great Depression and stagflationary 1970s have been learned. Rather than shrinking as in the Depression, the money supply is growing, which will prevent persistent deflation. And the Fed promises to reverse course before inflation sets in. Protectionist policies are highly unlikely to be adopted. Tax rates may eventually go up, but are unlikely to skyrocket as they did under Presidents Hoover, Roosevelt, Nixon or Carter.

Unfortunately, one policy of the Great Depression – mark-to-market accounting – has yet to be suspended. But, given the savvy with which President-elect Obama has shown in picking economic policy-makers, we hold out hope that mark-to-market will be suspended (or significantly changed) early in 2009.

Even the original manifestation of the economic problem – the massive overbuying and overbuilding of residential real estate – will eventually generate benefits once the economy starts to recover. Think about the young worker or family just starting out in 2005. Now think about a similar worker in 2010. The future worker/family will pay less for housing, and not because they get “teaser” interest rates on loans for houses they end up unable to afford. In addition, these very same investors have a chance to buy equities at extremely attractive valuations.

Most importantly, for the long run, we still live in a country blessed with a Constitution that limits the power of would-be tyrants and a culture that attracts and encourages entrepreneurs like no other place on earth.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
12-23 / 7:30 am	Q3 GDP Final	-0.5%	**-0.6%**		-0.5%
7:30 am	Q3 GDP Chain Price Index	+4.2%	**+4.2%**		+4.2%
9:00 am	New Home Sales - Nov	0.415 Mil	**0.390 Mil**		0.430 Mil
9:00 am	Existing Home Sales - Nov	4.920 Mil	4.940 Mil		4.980 Mil
12-24 / 7:30 am	Durable Goods - Nov	-2.5%	**+1.0%**		-6.9%
7:30 am	Durable Goods (Ex-Trans) - Nov	-0.1%	**+2.8%**		-5.4%
7:30 am	Personal Income - Nov	-0.1%	**-0.2%**		+0.3%
7:30 am	Personal Spending - Nov	-0.7%	**-0.6%**		-1.0%
7:30 am	Initial Claims - Dec 20	558K	**552K**		554K