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Return of the old ways of thinking threatens recovery & maximum confusion

Tom Gallagher | Sep. 29, 2009 NCR Today

Democratic political strategist and pundit, James Carville, came up with the effective and stinging slogan, "It's the economy, stupid," as a way for presidential candidate, Bill Clinton, to attack President George H.W. Bush, during the 1992 campaign. The slogan is as relevant now as it was then. Yet, for most people it seems impossible to understand economic theory and policy. The most important economic issue for families is jobs. After that it's wages, benefits and retirement.

I suggest that the economy can be understood, albeit over time and with some amount of sustanied reading. One person worth keeping an eye out for is Mohamed El-Erian, the chief executive and co-chief investment officer of Pimco, a premier investment manager of bonds with $842 billion in assets under management as of June 30, 2009. See www.pimco.com

El-Erian writes an opinion piece [1]in today's Financial Times, which is worth reading.

His opening paragraph quickly frames his view:

"We are at the point of maximum confusion in the multi-year transition of the global economy, markets and policymaking. We have left the global growth regime that was driven primarily by debt-financed consumption in the US (translation: mortgages and credit card debt), but we have not as yet reached a position of more balanced, albeit anaemic, growth. Those who lack a robust anchoring framework, be they investors or policymakers, risk being misled and backtracking to outdated ways of thinking."

He points out four key ingredients to this maximum confusion: (1) consumer indebtedness is still too high relative to income expectations and credit availability (translation: more saving, less consumer spending), (2) banks? balance sheets are still too geared for the comfort of regulators or their own managers (translation: no bank loans available as little lending in commerical real estate and for homeowners), (3) high unemployment that will be difficult to lower (translation: less buying of goods by consumers, less political support for necessary reforms), and (4) public debt has risen too fast (translation: necessary, future reforms become "iffy" - uncertain).

El-Erian concludes:

"The longer it takes for investors and the policy consensus to shift to the appropriate analytical framework ? one that factors in levels rather than just rates of change ? the greater the risk of disappointment in 2010."

(See, that wasn't too bad, was it?)

Links:
[1] http://www.ft.com/cms/s/0/1551b95e-ac59-11de-a754-00144feabdc0.html?nclick_check=1