The Recession Is Over, the Economic Depression Just Beginning

Economics / Great Depression II Jan 12, 2010 - 07:30 AM

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In late 2009, former Merrill Lynch economist, now with the Canadian firm, Gluskin Sheff, said the following:

"The credit collapse and the accompanying deflation and overcapacity are going to drive the economy and financial markets in 2010. We have said this repeatedly that this recession is really a depression because the (post-WW II) recessions were merely small backward steps in an inventory cycle but in the context of expanding credit. Whereas now, we are in a prolonged period of credit contraction, especially as it relates to households and small businesses."

Summarizing his 2010 outlook, Rosenberg highlighted asset deflation and credit contraction imploding "the largest balance sheet in the world - the US household sector" in the amount of "an epic $12 trillion of lost net worth, a degree of trauma we have never seen before," even after the equity bear market rally and "tenuous" housing recovery likely to be short-lived and illusory with a true bottom many months away.

As a result, consumer spending will be severely impacted. "Frugality is the new fashion and likely to stay that way for years," highlighting a secular shift toward prudence and conservatism because households are traumatized, tapped out, and mindful of a bleak outlook. It shows in new consumer credit data, contracting $17.5 billion in November, the largest monthly amount since 1943 record keeping began.

Surprisingly, only people over age 55 have experienced job growth. All others have lost jobs, can't get them, and for youths the "unemployment crisis (is) of epic proportions." In addition, there's a record number of Americans out of work for longer than six months, in part because the "aging but not aged" aren't retiring, and those who did are coming back, of necessity, to make up for wealth lost.

Rosenberg stresses that for a sustainable recovery to begin, the ratio of household credit to personal disposable income must revert to the mean and reach an excess in the opposite direction. In the 1950s, it was 30%. Today its 125%, down from the late 2007 139% peak, with a long way to go taking years, and when it's over, another $7 trillion in household credit will have to be extinguished.

Until he retired in 1992, Robert Farrell was a highly respected Merrill Lynch market strategist and theorist, best remembered for his "10 Market Rules to Remember." Number one was that "markets tend to return to the mean over time." Number two was that "excesses in one direction will lead to an opposite excess in the other direction," and number nine was that "when all the experts and forecasts agree -- something else is going to happen."

According to a November National Association of Business Economics (NABE) survey, 48 top economists expect the US economy to grow 3.2% in 2010 even though the job outlook is bleak. Overall, they're so optimistic that only 15% want more stimulus, 40% said leave the present package in place, and the other 45% want the amount approved but not spent cut because it's not needed. At the same time, according to Investors Intelligence, market sentiment is at the highest level since December 2007, shortly after equities peaked, headed down, and world economies began to crator.

In his January 5 commentary, David Rosenberg notes that "Sentiment is wildly bullish....almost every survey is overwhelmingly constructive," yet reviewing 2009's market performance in the face of economic fundamentals "almost wants to make you believe in the tooth fairy." He explained that "small business (still faces) a credit quagmire," there's no housing recovery, and household spending is retrenching and hunkering down for the long haul.

The latest US nonfarm payroll report provides more confirmation. Although the headline number was a modestly anemic -85,000, Rosenberg called it "horrible" because its details showed consistent weakness. As a result, he estimates a more accurate "465,000" December decline, based on what's occurring at the small company level "where the trend in orders, output, sales and employment" has been dismal.

Importantly, economic sectors sensitive to the business cycle actually "cratered" in December, "which flies in the face of the overwhelming view that this recession has fully run its course." Also disturbing was that while "temp help" gained 47,000 jobs, its fifth straight increase, full-time employment "plunged" 647,000 last month, a clear sign that no one is hiring, especially small businesses that do most of it.

The reason headline U-3 unemployment held steady at 10% was because the labor force plunged by 661,000, the sharpest (discouraged worker) decline in nearly 15 years. The broader U-6 unemployment is 17.3%, and economist John Williams (shadowstats.com) calculates it more accurately at 21.9% by excluding manipulated changes for more valid figures. He estimates about 500,000 December job losses, not the sanitized U-3 number. He also says that a "major double-dip downturn should be obvious by mid-year."

Economist Jack Rasmus' Outlook

Z Magazine's January issue features a bleak outlook from economist Jack Rasmus in his article titled, "Economic Crisis in 2010 and Beyond." In reviewing 2009, he argued that no recovery is possible as long as job losses and home foreclosures continue.

Looking ahead in 2010, he says "The fundamental problems of financial and consumption fragility have not been resolved." Both are deteriorating, and banks are in trouble, large and small, with 500 or more of the latter ones to fail this year. In addition, credit contraction will continue. Banks aren't lending to business or consumers. "Commercial property markets' deflation will deepen," so more Fed rescues will be needed in the face of defaults.

Business bankruptcies will increase, and so will the numbers of unemployed and those losing their homes. And if interest rates rise, the junk and Treasury bond markets will crater.

As for consumers, consumption will continue weak. Disposable income will decline, so recovery in 2010 isn't likely. In addition, without more stimulus (he believes won't come), unemployment will rise to 27 million from the current 24 million level, U-6 unemployment will reach 19% by year end, (the true number will be close to 25%), and hiring that does occur will be mostly low-wage temporary and part time.

Home foreclosures will also exceed seven million, "on their way to a possible 10 million." After stabilizing, home prices will again fall, and by year end "Between 33 percent to 50 percent of homes will be under water," a grave situation with many owners walking away from them and glutting the market more with unsold properties.

Rasmus also sees no interest rate hike until after the November mid-term elections, no meaningful financial reform, a lower dollar, more defaults like Dubai-World, perhaps in troubled economies in Latvia, Ukraine, Greece and Italy, and US states in greater trouble than today because of falling revenues, rising deficits, little in the way of relief, and forced budget cuts and layoffs exacerbating a dire situation. In other words, Rasmus, like Rosenberg, sees hard times ahead, in contrast to the consensus rosy outlook.

He discusses his views monthly on The Lendman News Hour, easily accessed through the archives link at the end of this article or listened to live.

Reality Check in California, Michigan and Other States - Except One

In December 2009, the National Governors Association (NGA) and National Association of State Budget Officers (NASBO) issued their latest biannual Fiscal Survey of States, assessing their economies and presenting their outlook for the year ahead, a very glum one in their opening statement saying:

"States are currently facing one of the worst, if not the worst, fiscal periods since the Great Depression. Fiscal conditions significantly deteriorated for states during fiscal 2009, with the trend expected to continue through fiscal 2010 and even into 2011 and 2012."

They say tax revenues are drastically lower from all revenue sources, and collections are expected to fall further in the current year. Citing a $256 billion budget gap between FY 2009 and 2011, they've had to enact sharp spending cuts and find new revenue sources. The federal American Recovery and Reinvestment Act of 2009 (ARRA) made up $135 billion of the shortfall. Another $87 billion in Medicaid funding facilitated critical health and human services spending.

Even so, programs across the board were cut with more coming in 2010 as governors and budget officers prepare for the worst. According to NASBO Executive Director Scott Pattison:

"We expect a continued deterioration in all financial indicators including revenues, balances and expenditures."

As a result, the fiscal health of America's states is dire with little in the way of expected relief. Across the country, governors say federal stimulus money is running out, yet conditions are worsening so more spending cuts and revenue increases are planned at a time opposite measures are needed.

However, unlike the federal government, states must balance their budgets, making up shortfalls by borrowing, taxes, and/or cuts in vital services. While constitutional, statutory, or traditional practices vary, three general kinds of balanced budget requirements exist, differing only in detail:

-- the governors' proposed budget must be balanced;

-- the enacted one must be as well; and

-- the fiscal or biennium fiscal year one must be also, with no deficits carried forward.

Given today's conditions, that makes for cantankerous debates producing compromises and delicate juggling, satisfying no one, especially households hit hardest by the results.

One state alone stands out in the current environment, North Dakota, with its governor, John Hoeven calling a December 15 news conference to explain that the state has so much money (a $1.3 billion FY 2009 surplus, its largest ever) that individuals and businesses will average $650 in 2009 tax savings from income and property tax cuts enacted by its legislature. In addition, seniors and disabled people who own property or rent will get additional savings from an expanded Homestead Property Tax program.

According to Tax Commissioner Cory Fong:

North Dakota has been able to weather the economic crisis. "While other state governors and legislatures are looking for ways to raise revenue through raising taxes and cutting services, we just came through a historic session of funding both our important priorities and substantial tax relief....The winners are families, businesses and the State of North Dakota," because it's unique in one important respect.

It's the only one with a state-owned bank (The Bank of North Dakota - BND) that sustains its distinctiveness and strength. As a result, it had the nation's lowest unemployment rate of 4.1 at year end 2009 and created jobs throughout the crisis.

Established in 1919, it's been a "credit machine" ever since, according to financial writer Ellen Brown, delivering "sound financial services that promote agriculture, commerce and industry," something no other state can match because they don't have state-owned banks.

With one, BND "create(s) 'credit' with accounting entries on (its) books" through fractional reserve banking that multiplies each deposited amount magically about tenfold in the form of loans or computer-generated funds. As a result, the bank can re-lend many times over, and the more deposits, the greater amount of it for sustained, productive growth. If all states owned public banks, they'd be as prosperous as North Dakota and be able to rebate taxes and expand public services, not extract more or cut them.

Brown explains that the BND:

"chiefly acts as a central bank, with functions similar to those of a branch of the Federal Reserve," that's neither federal or has reserves as is owned by major private banks in each of the 12 Fed districts, New York by far the most dominant with Wall Street's majority control and a Fed chairman doing its bidding.

In contrast, BND is a public bank, 100% owned by the state, operating in the public interest and those of the state. It "avoids rivalry with private banks by partnering with them." Local banks do most lending. "The BND then comes in to participate in the loan, share risk, buy down the interest rate and buy up loans, thereby freeing up banks to lend more. (One of its functions) is to provide a secondary market for real estate loans, which it buys from local banks. Its residential loan portfolio is now $500 to $600 billion" in a state with around 700,000 people and thriving.

Its function in the property market helped it "avoid the credit crisis that afflicted Wall Street when the secondary market for loans collapsed in late 2007 and helped it reduce its foreclosure rate....(Its other services) include guarantees for entrepreneurial startups and student loans, the purchase of municipal bonds from public institutions, and a well-funded disaster loan program." When the state didn't meet its budget "a few years ago, the BND met the shortfall."

In sum, state-owned banks have "enormous advantages over smaller private institutions....Their asset bases are not marred by oversized salaries and bonuses, they have no shareholders" demanding high returns, and they don't speculate in derivatives or other high-risk investments. As a result, BND is healthy with a 25% return on equity, paying "a hefty dividend to the state projected at over $60 million in 2009" and well over five times that amount in the last decade, so it begs the question why other states don't operate the same way. If enough of their residents demanded it, they might and not suffer the way nearly all of them are today, two notably - California and Michigan.

California - A State in Crisis

Conditions are so bad that rumors suggest a future bankruptcy that would be unprecedented if it happens, but a more likely worst case scenario would be default. Either way is the same if on all state obligations, and in 1975, New York city was on the brink with its lawyers at the State Supreme Court filing a bankruptcy petition on October 17 and police cars standing by to serve papers on the city's chief creditors, the banks.

At the last moment, it was withdrawn after the United Federation of Teachers used union retirement funds to back city loans and saved the day. At the time, few knew the danger or what it meant. Today many states face the same bind with California most significant because of its size. As a nation, it would rank 8th economically in the world, so a default would affect the entire country, and perhaps other states would follow.

On November 18, 2009, the Legislative Analyst's Office (LAO), California's Nonpartisan Fiscal and Policy Advisor issued its "2010-11 Budget: California's Fiscal Outlook," showing the following:

-- a $20.7 billion "budget problem" from late November to when the Legislature enacts its 2010-11 state budget; addressing it will require painful choices besides ones already adopted;

-- LAO cites "failed budget solutions responsible for" the current crisis; as a result, a huge deficit hole must be plugged and an even bigger one coming in 2012-13 when local government loans must be repayed pursuant to Proposition 1A (2004); federal ones as well in 2011;

-- "In the coming years, (additional) major state spending programs will have to be significantly reduced," and new revenues added as little help from Washington is expected; and

-- LAO sees a continuing budget problem of around $20 billion "for years to come," saying "as the nation goes, so goes California."

In US politics, an old saying in presidential races (no longer true) was that "As Maine goes, so goes the nation." Economically, perhaps as California goes, the nation follows, given the state's importance and deep distress. It's real unemployment rate way exceeds 20%, by some measures third worst in the nation behind Michigan and Oregon.

According to Marilyn Cohen, president of the Los Angeles-based Envision Capital Management, "This is much worse than anyone thinks. I have no confidence in the state legislature."

The data are stunning. "We are looking at numbers that are going to be incredibly staggering to resolve," says state Controller John Chiang in a recent interview. The Legislative Analyst's Office explained that, in 2009, California relied on $20 billion of one time fixes, including accelerating income tax collections and borrowing from local governments. They're no longer available, and with a November election ahead, lawmakers fear raising taxes.

In late December, Governor Schwarzenegger asked Washington for over $8 billion in aid, announced suggested transportation program cuts, and earlier proposed offshore oil drilling near Santa Barbara. Regardless, more cuts are coming, how soon and severe will depend on aid amounts gotten, but will it matter given no letup in California's eroding fiscal health, and House Speaker Nancy Pelosi (D. CA) saying don't bank on federal help because other states will demand the same.

"Our goal is to ensure that all states are treated fairly," she said, meaning little relief is coming, a stated 2009 administration policy. In denying a June 2009 aid request, US Treasury Secretary Tim Geithner said:

"A lot of the burden is going to be on (California) to lay out a path that gets their deficits down to the point where they're going to be able to fund themselves comfortably."

It applies to all states, forcing them to freeze hiring, cut jobs, lower wages, impose sweeping austerity, and erode social services when they're most needed.

In California, the impact on vital ones is stunning. In 2009, public education was decimated by $1.6 billion in the 2008-09 budget, another $4.2 billion for 2009-10, and earlier $11.6 billion in approved cuts. As a result, California ranks last in per-pupil funding with more cuts still coming.

They show up in increased class sizes, fewer textbooks and other materials, teacher layoffs, vital courses eliminated, and fewer school year days. Higher education was also hit hard after the University of California regents hiked tuition by 32%, forcing students to pay over $10,000 annually for what was once free. In addition, faculty member 10% pay cuts were ordered, the result of the number of imposed furloughed days, and students needing aid found most of it cut and not available. Others with awarded grants didn't get them, and 2010 looks worse.

Other social service cuts impacted healthcare, abused and neglected children, those with disabilities, the elderly, the poor, and benefits to the unemployed, California ranking 37th in the nation in the percentage of them getting benefits. In January 2009, its unemployment fund became insolvent because of increased demand. As a result, it borrowed from Washington, and current projections are for another $17.8 billion in 2010, all requiring repayment in 2011 without funds to do it.

As a result, on January 8, Governor Schwarzenegger declared a fiscal emergency in unveiling the $82.9 billion state budget calling for no tax hikes, more pay and social service cuts for the most needy, and a plea to Washington for help, likely to go unheeded.

Hard Times in Michigan

A December 2009 Michigan League for Human Services report titled, "Michigan by the Numbers: Hard Times Continue" says the state continues to suffer.

"Families....are still losing ground as personal incomes continue to fall or stagnate, unemployment remains the highest in the nation (as high as one in four or greater), and the poverty rate continues to climb."

In addition, fewer households have employer-covered heath insurance, and they're spending a higher percentage of their income on housing. As always, the poor and disadvantaged are hardest hit with key indicators pointing lower.

Instead of more aid for the needy, Governor Jennifer Granholm approved a 2009-10 budget that drastically cuts education and social spending making a bad situation worse. Included are more public education cuts averaging $292 per student for most parts of the state.

According to the Michigan Parent Teacher Student Association's (MPTSA) Kevin McLogan, the cuts are "devastating. A lot of terrible things are going to happen. There are a lot of districts that are already in tough shape. They will be pushed to the edge of receivership. For other schools, there will be a lot of cutting around the edges. They will curtail busing, after-school programs, community education and alternative education. Some districts will increase the amount of kids in the classroom, institute shorter school years, and force teachers to buy more of their own supplies."

Healthcare will also be impacted by new 8% cuts in Medicaid allocations to hospitals, clinics, nursing homes, and doctors treating 1.7 million poor and disabled residents. The Detroit News reports that "Some nursing homes with a heavy Medicaid caseload may close," further hit by the loss of hundreds of millions in federal matching funds. Other budget cuts include the following:

-- 11% less to cities and towns, a loss of $100 million impacting services across the board;

-- the Michigan Promise college scholarship program, providing $1,000 - $4,000 grants for 100,000 students; in addition, tuitions are being increased and financial aid reduced; also lost are nursing scholarships, the Michigan Work-Study Program, and the Part-Time Independent Student Program;

-- a 0.4% cut to state colleges and universities;

-- a loss of $62 million in mental health services, and many other cuts from dozens of gubernatorial line-item vetoes affecting education, healthcare for the indigent and uninsured, senior food aid in two counties, a volunteer Bay City health clinic, the traditional Michigan State Fair since the 19th century, much more; according to political leaders in both parties, they're only the beginning as hard times are forecast for many more months or years.

In addition, shortfalls keep exceeding cuts, and according to the Detroit Free Press:

"Michigan's budget problems will almost certainly worsen before they improve. Tax revenues are expected to remain flat or decline. Program needs - from welfare to the cost of public employee salaries and benefits - will continue to grow. (Most of the state's unionized employees are scheduled to get a 3% pay increase next spring.) And about $1.4 billion in onetime federal stimulus money to balance the 2009-10 books will be gone," and not likely replaced.

Detroit - A Dying City

On December 16, Detroit News writer Mike Wilkinson's article headlined, "Nearly half of Detroit's workers are unemployed." They don't have jobs and those with them work fewer hours.

"Using a broader definition of unemployment, as much as 45 percent of the labor force has been affected by the downturn. And that doesn't include those who gave up the job search more than a year ago, a number that could exceed 100,000 potential workers alone."

Yet for over 100 years, auto companies provided high-paying, good benefits jobs for Detroit workers, drawing many from around the country there for them. No longer with the city and industry in decline. Especially in the last decade, half its population left, and if the present trend continues, Detroit may be in its death throes, and what's happening there may hit other cities.

Already, factories and entire neighborhoods are empty. In 2005, US Census Bureau figures showed the city to be the poorest in America with one-third of its residents (and one-half of its children) below the official poverty line. Now it's much worse, and it's highlighted on August 13, 2009 by CNN Money.com's Steve Hargreaves article headlined, "Hunger hits Detroit's middle class."

He calls a lack of food in this recession-racked city a serious problem with not "a single major non-discount chain supermarket (there), forcing residents to buy food from corner stores or discount chains. Often (it's) less healthy, less varied, or more expensive food" for those able afford it or enough. Many can't and rely on food stamps and charity services.

The "food crunch is intensifying, and spreading to people not used to dealing with hunger. As middle class workers lose their jobs," people who used to donate to food banks now need them as recipients in growing numbers - "about a third more people than before," according to Jean Hagopian, a New Life food pantry volunteer in a suburb 20 miles northeast of the city.

Throughout metro Detroit, social service agencies report a huge increase in demand, far in excess of what they can provide and rising. It's no longer just for the homeless and poor. It's for households whose breadwinners lost auto and other good-paying jobs, also homes and savings, and are now desperate for help.

Detroit is a microcosm of Michigan, and its hard times are getting harder. So are California's, and conditions throughout the country. In its 2009 report "Hunger and Homelessness in US Cities," the US Conference of Mayors state:

"Hunger and homelessness (are) at record levels in US cities." They cite:

-- a 26% increase in demand for help over the past year;

-- more middle class families needing it;

-- more people relying on food pantries and emergency kitchens, but the demand is so great that about 25% of it goes unmet;

-- rising family homelessness; and

-- growing numbers of tent cities and other homeless encampments that "account for a very small percentage of people who are homeless."

"At a time of historic economic crisis, the issues of hunger and homelessness in America are more prevalent than ever," cities are hard-pressed to deal with them, and budget cuts and revenue shortfalls will impose an even greater burden in the new year and beyond.

Some other disquieting facts are as follows:

-- US households are burdened with the most severe poverty, joblessness, hunger, homelessness, and level of foreclosures and threatened personal bankruptcies since the Great Depression - with no planned relief measures to help;

-- the National Academy of Science calculates 47.4 million Americans, 15% of the population, impoverished in 2008; the true number is much higher since the government's income threshold is $22,000 for a family of four, an amount way inadequate throughout urban America where even half again as much is too little;

-- the US Department of Agriculture reported that a record 49.1 million people lacked dependable access to food in 2008;

-- a new Brookings Institution-First Focus study reported seven million more food stamp recipients in August 2009 than a year earlier, the number reaching 36.5 million under the Supplemental Nutrition Assistance Program (SNAP);

-- a January 2, 2010 New York Times article reported a surge in food stamp demand with six million Americans receiving them saying they have no other income - no welfare, no unemployment insurance, no pensions, no child support, no disability pay, and no other form of help;

-- an Archives of Pediatrics and Adolescent Medicine reported study said about half of US children will rely on food stamps during some portion of their childhood; for black children, the figure is a shocking 90%; and

-- another study showed less than half of college students graduate on schedule, and most who quit or temporarily drop out, do so for economic reasons; in addition, graduates face bleak employment prospects in the worst job market in decades.

Nonetheless, in his upcoming State of the Union address, Obama is expected to repeat his post-China trip message that fiscal austerity (meaning sharp social spending cuts) is necessary to cut the public debt. In other words, bankrolling Wall Street, health insurers, the drug cartel, other corporate favorites, and war profiteers will continue while working Americans won't be helped during the greatest economic crisis in their lifetimes, a protracted one that will last years.

Looking ahead in 2010, the state of the nation for most people is dire and worsening, and 2011 looks no better. City mayors are on the front lines dealing with it. So are governors at their state levels, but increasingly they're getting less help from Washington from an administration with priorities leaving them out and the millions they serve, on their own and out of luck.

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