

How We Get Through This Mess

How We Get Through “Where Is My V-Shaped Recovery?” We Have Met the Enemy, and He Is Us

So Where’s the Good News?

LA and Europe

By John Mauldin

This week I spoke to a small group of businessmen/entrepreneurs about the current economic environment, and after my presentation one asked me whether I didn’t have any good news for them, with a kind of gallows humor laugh. And I tried. But upon reflection there is more I could have said, so this week’s letter will be what I should have said to be a little more encouraging.

The group was a Vistage group in which my daughter Tiffani participates. This is an organization of 12 businesspeople (in this case all CEOs of small businesses) who meet once a month to share and learn about better business practices, accountability, planning, and all the aspects of running a business. Every person I have ever met who has been involved in Vistage has had good things to say about it. I have watched it help Tiffani a lot. She truly runs our business now, allowing me to read and write and travel and speak. I am a very lucky man and proud Dad.

I have particularly watched my partners at Altegris really truly transform their business model through their involvement with Vistage. First the CEO, Jon Sundt, joined, and now the partners have all joined Vistage groups focusing on their roles in the business. Sundt was always a good businessman, but the level of professionalism of his whole company has gone up a notch. It is a pleasure to watch them grow, and they give Vistage a large measure of the credit for their success. In fact, when I went to the Vistage web site to get the link, I saw a brief video of Sundt talking about his experience. (<http://www.vistage.com/>) I am proud to be their partner.

If you have a business and could use some help and professional mentoring, you should look into finding a Vistage group that works for you. They match businesspeople in different industries but with roughly same size businesses. In tough times you need all the help you can get.

I talked to them about the current economic environment and what I saw coming down the road. Long-time readers know that I think we are in for an extended period of slow growth, high and sticky unemployment, and volatile markets punctuated by more frequent recessions. That is what you get when you have a deleveraging environment resulting from a credit crisis. It is what happens when the Debt Supercycle ends. We start the journey to the New Normal and it just takes time.

“Where Is My V-Shaped Recovery?”

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Remember all the bulls and cheerleaders late last year and into this one talking about a V-shaped recovery? They were making their projections based on what had happened in past recessions. I (and others) argued that that data was meaningless, as it did not reflect the fact that a balance-sheet recession requires years of deleveraging, is inherently deflationary, and all the factors that produce the normal “V” are no longer in play. Bank lending is still dropping. Savings rates go up. Debt gets paid down. Governments run into limits as to how much they can stimulate the economy without creating large and destabilizing debt. Central banks push rates to zero, and then what? This is a far different environment than we have had for the last 70 years. Using past performance to predict future results when the future environment is significantly different than the period in which the data was collected is misleading at best and worthless at worst, leading to bad decisions. Much better to deal with reality.

And just to show that I am really the optimist in the room, let's turn to my good friend David Rosenberg, writing this morning under the following headline:

“U.S. RECESSION NEVER ENDED; GDP TO CONTRACT IN Q3

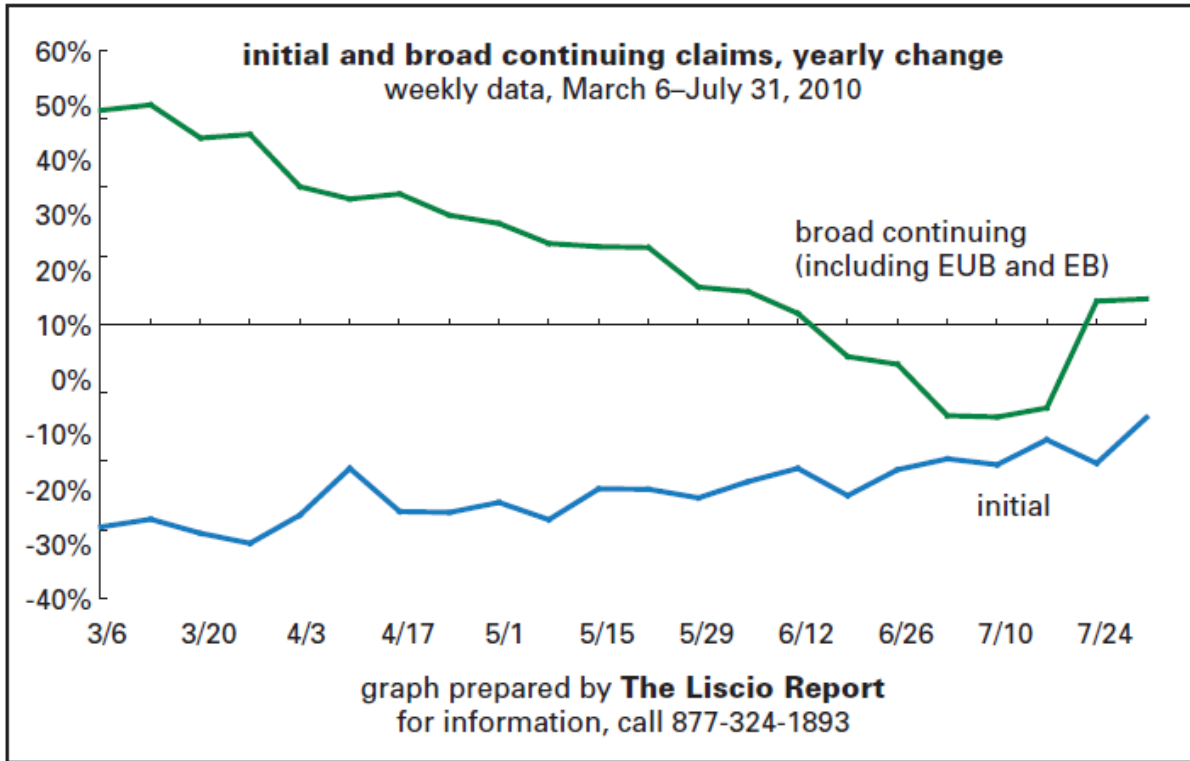
“Our suspicions have been confirmed — the recession never ended. Macroeconomic Advisers produces a monthly U.S. real GDP series and it shows that the peak was in April, as we expected, with both May and June down 0.4% in the worst back-to-back performance since the economy was crying Uncle! back in the depths of despair in September-October 2008. The quarterly data show that Q2 stands at a +1.1% annual rate (so look for a steep downward revision for last quarter) and the ‘build in’ for Q3 is -1.5% at an annual rate. Depending on the data flow through the July-September period, it looks like we could see a -0.5% to -1% annualized pace for the current quarter. Most economists have cut their forecasts but are still in a +2.5% to +3.5% range. What is truly amazing is that despite all the fiscal, monetary, and bailout stimulus, the level of real economy activity, as per the M.A. monthly data, is still 2.5% below the prior peak. To put this fact into context, the entire peak-to-trough contraction in the 2001 recession was 1.3%! That is incredible.

“Interestingly, and dovetailing nicely with our deflation theme, nominal GDP fell 0.3% in May and by 0.4% in June. This is a key reason why Treasury yields are melting.”

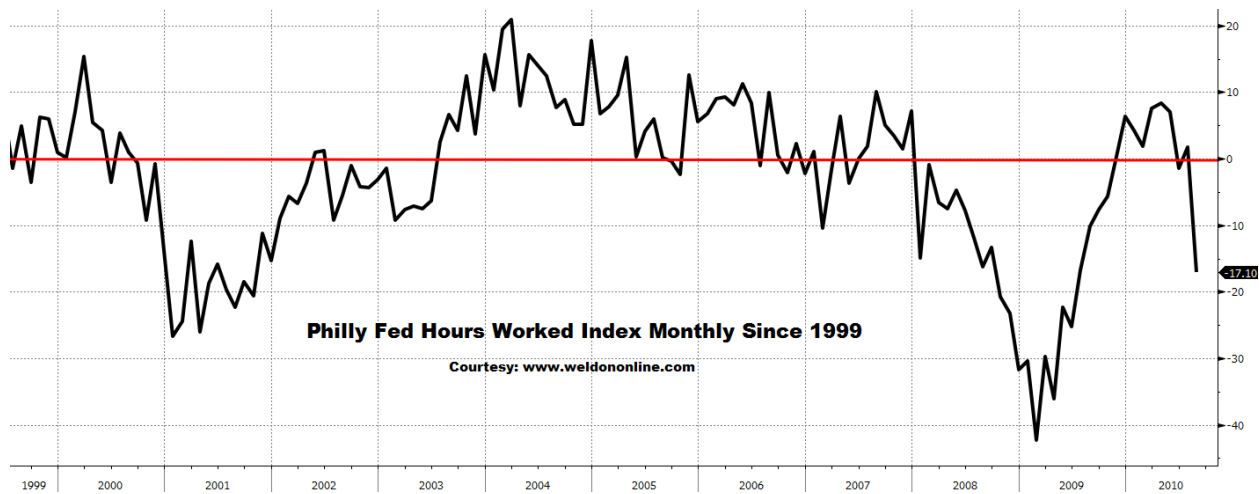
Politicians are going to be greeted with a GDP number for the third quarter, right before the elections. Will it be negative like Rosie thinks? I am not sure, but in any event it will not be good. Structural unemployment will still be over 10% and deficits will be high.

Look at the following graph from my friends at *The Liscio Report*. Unemployment and continuing claims have started to rise again. This is not what happens in V-shaped recoveries, gentle reader. The ONLY reason the headline unemployment number has dropped a little is that the Labor Department has dropped so many people from the labor force. Again, if you have not looked for a job for four weeks, they do not count you as unemployed. If you use the labor-force number from just last April, unemployment is 10.5%. Brutal. Who doesn't know too many people without jobs?

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But it is not just rising unemployment claims. Yesterday’s Phillie Fed report was just awful. Buried in the details was the fact that the hours-worked index is collapsing, consistent with previews to past recessions. Very worrisome. (From my favorite slicer and dicer of data, Greg Weldon: www.weldononline.com)



Bottom line? It is going to be a tough environment for the next 6-8 years. That is just what happens when you have a deleveraging / balance sheet / deflationary / end of the Debt

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Supercycle recession. It is what it is, and no amount of wishing or finger pointing can change the facts.

Let me take a moment and offer some sympathy to President Obama. This recession/slow period is not his fault. Obamacare? A now-trillion-dollar stimulus? Those he owns. But the recession/credit crisis would have happened if McCain had been elected.

And it is not Bush's fault. Did he make some mistakes? Oh yes. Squandering those surpluses is huge in my book. Not vetoing all that excess spending is at his feet. And there are other issues, but that is not my point.

We Have Met the Enemy, and He Is Us

There is a great line from the old cartoon strip Pogo: "We have met the enemy, and he is us." (Ah, I miss Walt Kelly and Pogo. But I show my age!)



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Neither Clinton nor Bush forced people to borrow money against their homes. Yes, some of the laws made it easier. Yes, Greenspan pushed rates lower than they should have been. Allowing banks to go to 30:1 leverage was stupid (courtesy of the Bush administration). Repealing Glass-Steagall in hindsight was not wise (Clinton era).

But we the people borrowed and spent. Congress taxed and spent and we voted for the SOBs and collectively asked for more goodies. Maybe not you, gentle reader, because all my readers too smart to have engaged in such reckless activity, but those other guys sure did. Probably the readers of Paul Krugman. (Did I say that?!?)

So, the current problems are not Obama's fault. But how he deals with them is. Raising taxes in what can only be called a soft environment gives him ownership of the consequences. And it is more than just the Bush tax cuts going away. Obamacare gives us a host of new taxes. (If you want to see more, read <http://www.atr.org/six-months-until-br-largest-tax-hikes-a5171>)

So Where's the Good News?

Ok, I could go on for hours, sorting through the problems. Where is the good news I promised?

Here's what I should have said to Tiffani's group: Let's face it. Running a small business is never easy. I am a serial entrepreneur. I have started and run a lot of very different businesses. Some have been very, very good and some went down in spectacular flames. I can remember some near-death experiences when the economy was booming. I have watched a million-dollar income stream dwindle to zero and there was not a damn thing I could do about it, except enjoy the money while it was there and use it to buy the next income stream. I have had to rebuild several times from scratch as markets shifted drastically underneath my feet. And I've changed directions as new opportunities revealed themselves.

In all this I'm like every other small-business entrepreneur out there. It is never easy. But that is what we do. We get up in the morning and figure it out. Some 80% of startups die within ten years. But we pick ourselves up and start over.

I know unemployment is 10%. But that means almost 90% are employed. Consumers are saving more. So adjust. Figure out what your New Normal looks like.

The '70s were a bitch. I woke up many times in the middle of the night with real pains in my stomach wondering whether to pay the rent or make payroll. So did a lot of people. But look at all the new companies that came out of that era and changed everything: Microsoft, Apple, Intel, etc. Cell phones. The internet. The list is long.

Yes, we have to make our way in this Muddle Through World. It will be challenging, but I can almost guarantee you that when we do get through there will be other challenges. If it was easy everybody could do it and there would be no money in it. Embrace the challenge!

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I asked one of my really close (36 years) friends and business associates last year how his business was doing. “We are doing great!” he said. That was not the answer I was expecting. “Why? How?” I asked.

“Well, most of our competitors have folded. We survived and got the business.”

Ultimately, that is how we get out of this. A hundred million families and millions of businesses figuring it out, learning how to adapt to the New Normal. Sadly, some of them won't make it. But most of us will!

As I said, I am a serial entrepreneur. I have a friend who designs and oversees large teams of programmers of really robust analytic software, very cutting-edge stuff. She is a winner, and I am backing her (I know nothing about software but the rule is, invest in people!). We'll see how it goes, but my bet is that in a few years there will be a lot of people getting jobs because we take on some risk now.

We are adapting our own business here. We will soon have new websites. I will be doing (at first) an audio podcast called the Mauldin Minute and then (hopefully) by the end of the year morphing into video. That's the wave of the future and I need to keep up.

I am addicted to information and reading . We are going to try and make some money from my addiction. What would you pay to look over my shoulder and read the 5-10 most important things I find in a week? I will become your personal reader. Will that be a life-style changer? No, but it will provide some income diversification.

When Tiffani made her presentation to her Vistage group about our business, she had a lot of charts and graphs. I was surprised how our sources of income have varied over time. Some previously large (at least on my scale) sources literally dried up within a few years, completely askew from our original optimistic expectations. It was very apparent that we cannot sit and assume things will be the same year to year. So we adapt.

I have been presented with a very different opportunity in a non-finance field that is right in my wheelhouse, as they say. Tiffani and Ryan and I are going to pursue it. Will it thrive? Be a real business in five years? We will see, but I have the ability to take that risk and I am going to do so.

And so will hundreds of thousands of other visionaries and dreamers. That is how we get through this. We work through the ugly and then we get to the 2020s, and I think we will once again be talking about the Roaring 20s! Whole new industries will come into existence. Pay attention to the advancements in robotics. Biotech will be HUGE this decade, but we need to change the rules so we don't lose the intellectual property and the jobs. Electric cars will boom as we replace our fleet all over the world. Nanotech later in the '20s. Green energy and nuclear. Artificial intelligence (finally!). Really cheap (I mean *really* cheap!) wireless high-speed

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broadband all over the world will open the door to all kinds of possibilities. I met last night with very credible scientists who have developed a way to filter water very cheaply. A desalinization module that fits in a cargo container. Yes, they need a lot of money to finish, but they will figure it out. And on and on. The opportunities are going to be huge. Trillions will be made.

So, we get through this. We Muddle Through. We figure it out, one business and family at a time. And as a culture, a world, we get to a better place. My bet is that in 2020 no one is going to want to go back to the good old days of 2010. We will be excited about the future and all the cool stuff that is happening.

Recessions and tough times are God's way of telling you that you need to adjust a few things, both on a personal and business level – also nationally and globally. I am an optimist. I believe we will adjust and grow, not just in the US but as an emerging world. There are just so many opportunities.

So, don't let the problems I write about in this letter make you crawl into a cave. Just be realistic and figure out where your opportunities are. And then go make them happen! You are responsible for creating your own future. And I hope it is a good one. I plan on making mine one.

LA and Europe

I am in San Francisco at the MoneyShow. There is a good crowd and I have dropped in on a few presentations. There seems to be some talk about a bond bubble, whatever that is. I just see Boomers realizing they need to be more conservative, and a deflationary environment.

The bubble is in sovereign debt. That is not going to end easily. For many countries it will end in tears.

It looks like I am going to have to shoot to LA week after next for some meetings and a check-in with the design/imaging/branding group that is developing our new web presence strategies. Within a few months you will be able to comment on my writing, communicate with fellow readers (civilly, of course!), and ask questions which Ryan will try to corral me into answering. Lots of new and cool things coming.

Oh yes, the book. Sigh. A personal situation has delayed me a week, but I swear I'll get the final chapter written next week and then out to some friends for comments and off to the publisher.

My schedule for Europe is shaping up. I will be in Amsterdam September 11-14, then Malta, Zurich, Mallorca for some fun with my London partner Niels Jensen and team for the weekend, then to Copenhagen for a day (at least one session will be open to the public), and then on to London and back home. Drop me a note if you want to meet, and I will get it to the keeper of the schedule.

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And thanks to Charles Githler for being such a great host at the MoneyShow! Amazing, this is their 32nd year of doing the show here. Where does the time go? He was a 21-year-old kid when he started this, and he has created a really significant business, with conferences all over the world. And he started in 1978 and lived through two recessions. It can be done!

It is time to hit the send button. I have yet another presentation in 37 minutes and need a few minutes to prepare. Have a great week and enjoy the moment! I am, although sitting in a hotel room in San Francisco is not my preferred environment. I do love this city. But that, gentle reader, is the small price of the privilege of writing to you each week.

Your ready to get out of this room analyst,

John Mauldin