

Tea Leaf

...weekly since 1976

Your guide to understanding
today's economy and
financial markets

August 3, 2010

[view previous issues](#)



THREDGOLD
ECONOMIC
ASSOCIATES

The TEA Company
A Professional Speaking and
Economic Consulting Company
1366 S Legend Hills Drive, Suite 150
Clearfield, Utah 84015
801-614-0403

www.thredgold.com

Copyright © 2010 Thredgold
Economic Associates, LLC.

Please call 1-888-847-3346
for reprint permission.

An Economic Chat

Written by Jeff Thredgold, CSP, President, Thredgold Economic Associates

During the past 35 years of writing a weekly economic, financial, and (sometimes) political newsletter, I have periodically tried to present information in an unusual format so as to make “the dismal science” less intimidating and more interesting. Over the years, we have occasionally run a discussion between two old friends—Mrs. Smith and Mr. Jones—regarding a variety of issues. Their topic of discussion today is the latest data regarding U.S. economic growth, and important revisions to the data of the past three years...

While sitting on a park bench...

“I am really confused by all these numbers and statistics about the economy that have been in the news in recent days,” stated Mr. Jones. “What the heck is GDP, and what does it have to do with me?”

“GDP, or Gross Domestic Product, is an estimate of the value of all goods produced and services provided inside U.S. borders, measured as an annual growth rate or annual rate of decline, with the impact of inflation removed. It is provided by the U.S. Commerce Department,” noted Mrs. Smith.

“For example,” continued Mrs. Smith, “the U.S. economy grew at a 2.4% real (after inflation) annual rate during 2010’s second quarter, just slightly less than expected. In addition, all of the U.S. economic data of the past three years was revised, in some cases for the fifth time, to more accurately reflect what is happening in the American economy.”

“That could really be confusing,” noted Mr. Jones. “Why all of the revisions?”

“More accurate estimates are being gathered all the time for employment, consumer income and spending, business investment, new home construction, new commercial buildings, and all forms of government spending,” offered Mrs. Smith. “It is important to have the most accurate information possible as to where the economy ‘has been’ in order to determine the best mix of fiscal and monetary policy going forward.”

“Whoa! You lost me!” stated Mr. Jones with a puzzled expression on his face.

“Sorry,” stated Mrs. Smith. “Fiscal policy is a fancy term for what the

Congress and the Administration do as far as taxing and spending and managing the national debt. Monetary policy is what the Federal Reserve does with money creation

and the control of the most important short-term interest rate—the federal funds rate—to stimulate or slow the economy, while always keeping a sharp eye on inflation.”

“That sounds like a discussion for another time,” noted Mr. Jones, with a glaze over his eyes.

“Agreed,” proffered Mrs. Smith.

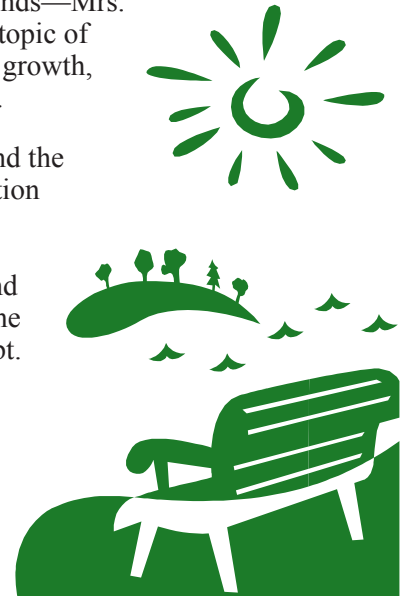
Revised Data

“So, what do we know now about the economy we didn’t know before all of the new numbers?” asked Mr. Jones dejectedly.

“We know that the recession was actually worse than we had previously thought,” observed Mrs. Smith. “We also know that the U.S. economic recovery of roughly the past year has been a little weaker than we originally understood.”

“But I thought we were...we are... in a terrible recession,” said Mr. Jones. “Is it over?”

“What many refer to as the Great Recession has been over for about a year, according to forecasting economists,” offered Mrs. Smith. “The actual



scorekeeper for the U.S. economy, the National Bureau of Economic Research, has a Business Cycle Dating Committee that is likely to make that call later this year or early in 2011. The NBER previously announced that the recession officially began in December 2007.”

“That’s confusing,” argued Mr. Jones. “I still hear most people talk about the recession as if it is still underway.”

“Unfortunately,” continued Mrs. Smith, “the recovery from the recession has been weak. Never since the Great Depression of the 1930s have we had a sharp decline in the economy without having a sharp rebound. As most economists had forecast earlier, this time seems to be different.”

“But why?” asked Mr. Jones.

“Consumers have been hurt by more than eight million lost jobs and high unemployment,” stated Mrs. Smith. “Overall consumer spending, which represents 70% of the economy, has been barely growing.”

She continued, “Large businesses cut employment to the bone during 2008 and 2009. Some of these businesses have begun to hire more people, but business managers are very leery of all the new regulations and rules and higher taxes coming from Washington DC. As a result, they use more part-time people and remain tentative in adding new permanent workers.”

“Will all of these lost jobs ever return?” asked Mr. Jones.

“It’s highly unlikely,” added Mrs. Smith. “Hundreds of thousands of jobs in manufacturing and construction are unlikely to return. Tens of thousands of other jobs in state & local government and the finance sector are also unlikely to return. The nation’s unemployment rate, which averaged 9.7% during 2010’s first half, could still be above 9.0% by the end of next year.”

She continued, “And don’t forget, we need to add about 130,000 net additional jobs each month just to keep the unemployment rate steady; just to meet the needs of a rising population.”

More Stimulus?

“The President and the Democratic leaders in Congress talk about how effective the more than \$850 billion ‘stimulus’ program has been during the past year or so,” noted Mr. Jones. “Can’t they just do another ‘stimulus’ program?”

“There is real debate as to how effective the massive stimulus bill has been. They could try another one, but getting the votes in the Congress to get it done would be very difficult,” stated Mrs. Smith. “Keep in mind, an additional stimulus program would be ‘paid for’ with even more borrowed money.”

“Don’t forget,” she continued. “The budget deficit for this year will be more than \$1,400,000,000,000, close to last year’s \$1.4 trillion, and largely matching the proposed budget deficit for next year. In fact, proposed annual budget deficits during the Obama years will exceed the budget deficits of all previous U.S. presidents.”

“Now that’s scary,” cautioned Mr. Jones. “Are we going to fall back into recession? I hear that on the radio, you know.”

“It is a possibility,” Mrs. Smith stated. “But most forecasting economists think we will stumble forward with about a 2.0%-2.6% real growth rate during the next 12 months. There is still a massive amount of stimulus in the economy, from both the Congress and the Fed.”

“Was there any good news in the big GDP revisions?” asked Mr. Jones.

“Yes,” noted Mrs. Smith. “American consumers have been saving more than originally thought. They also seem to be further along in getting debt levels under control than we thought. Each of these factors could be good news down the road.”

“I’m still confused,” moaned Mr. Jones.



“TEA”ser

Golf Caddy Comments

Golfer: “Do you think I can get there with a 5 iron?”

Caddy: “Eventually.”

Golfer: “I’d move heaven and earth to break 100 on this course.”

Caddy: “Try heaven, you’ve already moved most of the earth.”

From Bill Losey



THREDGOLD
ECONOMIC
ASSOCIATES

To receive the *Tea Leaf* free via email,
sign up at
www.thredgold.com

Thredgold Economic Associates
1366 S Legend Hills Drive, Suite 150
Clearfield, Utah 84015
www.thredgold.com

Graphics and layout by Kendall Oliphant
Research assistance by Shawn Thredgold