Geithner: No Double Dip

When he appeared on ABC News's This Week on February 7, U.S. Treasury Secretary Timothy Geithner was quizzed about the risk of the United States losing its triple-A credit rating, the chances that foreign investors might start shunning US debt, and whether the economy would suffer a double dip recession.

Last week the credit rating agency Moody's warned that weak economic growth and increasing debt burdens could "put pressure on the country's triple-A status." When asked to respond, Geithner said, "Absolutely not. That will never happen to this country." One remembers the speaker's rule to be very careful about using absolutes, such as "absolutely", and "never happen". History books are filled with examples of events that could "absolutely never happen."

Then Geithner was asked about concerns he might have about finding investors to continue to purchase debt securities issued by the government to fund its huge and increasing deficits. He answered that "there was no sign that investor interest was waning in U.S. debt," and in fact such debt was being sought by investors "because of trust in the U.S. ability to repay [it]."

> If you step back and look at what has happened throughout this crisis, when people were most worried about the stability of the world, they still found safety in Treasuries. You're still seeing that every time.

This neatly sidesteps concerns voiced by Chinese officials recently about the size of the US deficits, and their reluctance since the summer to add significantly to their already enormous holdings of US debt securities.

But it was Geithner's response to the third question that caught people's attention: what are the chances of the economy slipping back into a recession? He said, "I think we have [a] much, much lower risk of that today than at any time over the last 12 months or so." So much has been written in *The New American* online (click here, here, and here) and elsewhere about the increasing chances of such a double-dip occurring that a closer look is deserved.

A Double Dip Recession is defined "when GDP [Gross Domestic Product] growth slides back to negative after a quarter or two of positive growth. A double-dip recession refers to a recession followed by a short-lived recovery followed by another recession." Causes of such a double-dip recession, according to Investopedia, vary but "often include a slowdown in the demand for goods and services because of layoffs and spending cutbacks from the previous downturn."

Wells Capital Management's Chief Investment Strategist Jim Paulsen pointed to the "debate surrounding the strength of the…economic recovery," and concluded that the current recovery is closely tracking the "strong recoveries of 1975 and 1982." These were the two deepest recessions over the past 50 years and, when compared to the numbers coming from the economy at present, "the 2009 recovery is thus far tracking quite closely with these historically 'strong' recoveries!" After reviewing carefully the numbers on GDP growth and inventory numbers, Paulsen concludes the "real GDP growth [currently] is thus far matching two of the strongest expansions in the last 50 years.

Forbes magazine agrees: no double dip here. "The ISM (Institute of Supply Management) Manufacturing Index hit 58.4 in January, higher than any time during the late-1990's boom. New orders for 'core' capital goods…are up at a 15% annual rate in the past three months." And January auto sales were 11 percent ahead of last June's rate, just before the Cash for Clunkers program began. Forbes continued: "Real consumer spending grew at a 2.4% annual rate in the second half of 2009 [and] in the past three months civilian employment has gone up an average of 110,000 per month." And the work week is getting longer, too, as employers are finding it more efficient to add hours to their present workforce than to bring on new workers. "[This] increase in total hours worked amounts to the equivalent of adding 200,000 jobs per month. In other words, the demand for labor is [increasing], it's just that firms are temporarily meeting it by increasing hours. Either way, more labor demand will turn into more consumer buying power and more growth."

Forbes goes on to point out that "consumer debt, rent, and mortgage payments are falling. Our calculations show that the financial obligations ratio is now the lowest in ten years. Add it all up and our forecast for 4.5% real GDP growth in 2010 doesn't look so far-fetched anymore. In other words, this is a very normal, self-sustaining, V-shaped economic recovery."

The Vanguard Group of mutual funds weekly newsletter is much less certain. It points out that the drop in the unemployment rate from 10 percent to 9.7 percent "can be explained by a technicality concerning the collection of employment data. The numbers are derived from two different surveys and do not always match perfectly." Vanguard economist Roger Aliaga-Diaz indicated that it is too early to tell whether the unemployment rate has already peaked despite positive trends in the labor market. "There is still a considerably large pool of discouraged workers that may decide to start searching for jobs later this year," he said. "Depending on how fast this process takes place relative to the rate of job creation in the economy, we could see the unemployment rate inch higher."

The Vanguard report said that although personal income rose slightly in December, construction spending "fell much faster than economists projected [and] suggest continued weakness in the housing and commercial real estate markets and do not bode well for a quick turnaround."

Vanguard also referred to the ISM purchasing manager's index increase in January, but then pointed out that the ISM's Non-Manufacturing (a measure of the service sector's activity) barely moved, signaling "that the economic recovery is not broad-based." Finally, the report concluded that factory orders continue to grow strongly, and consumer credit balances are declining much more slowly, indicating perhaps a willingness by the consumer to increase spending modestly.

The U.S. Chamber of Commerce is much less tentative, warning of a double-dip recession "because of the taxes and regulations under consideration by the Democratic Congress and President Barack Obama." Last month Chamber President Tom Donohue said "lawmakers should not let former President George W. Bush's tax cuts expire at the end of the year." If they are allowed to expire, "We will likely end up with even bigger deficits and greater economic misery. We're talking about a massive tax increase in a very weak economy — a tax increase whose clearly intended purpose is not to reduce the deficit, but to pay for more spending."

In Great Britain in January there was a "sudden and unexpected collapse in retail sales," according to the British Retail Consortium. Its sales monitor decline for January was the "steepest…since the survey began in 1995," and was "an awful start to the year and a stark contrast to an upbeat December." Stephen Robertson, the Director General, expressed concern: "This is the worst January sales growth in the 15 years we've been running the survey. The VAT change brought some sales forward to December, but customers are becoming cautious again in the face of economic and political uncertainty. Retailers will be hoping these results are mainly a [weather]-induced blip, rather than an indication of further difficulties."

In summary, economists in Great Britain are putting up a significant probability that their economy will drop back into a recession "early this year."

Perhaps the most telling and persuasive argument for a possible double-dip recession in the U.S. comes from Morningstar's analysis of the housing market for 2010. Although the surface numbers appear to be strong, with existing home sales in December increasing 15 percent over the previous year, and the inventory of existing homes for sale dropping significantly, there is a "shadow inventory of homes that may soon be for sale due to delinquency and foreclosure." This "shadow inventory" could double the present inventory of existing homes for sale, which would take a year to a year and a half to clear. "Thus, [this] market data, which is improved bur still depressed, warrant a cautious approach to the housing market…over the coming year."

In the short run, then, Geithner could be right that the economy will move slowly higher without falling into another recession. In the long run, as John Maynard Keynes is famous for saying, "we are all dead." But what about for the foreseeable future? With huge deficits "as far as the eye can see", with welfare state transfer payments greatly exceeding revenues, with foreign military interventions and adventures pursuing political ends, even for a healthy economy these are enormous burdens. For a sick economy, such burdens could be fatal.

Photo of Treasury Secretary Timothy Geithner: AP Images