

Economic Views for Investors

by Roger Nightingale

The economist's idea of forecasting is to wait until something has happened . . .

. . . and then say it's going to

His lack of foresight recently makes him risible

Those in the B-of-E were bad; those in the Treasury and FSA shocking

Why waste money subsidising malefactors?

Why let incompetents steer the boat?

By not objecting, the rest of us were complicit

We approved the punishment of the innocent

How long before equilibrium is re-established?

Will it be months or decades?

Charlatans say the one . . .

. . . realists the other

Economists have many fine qualities, but the ability to anticipate events is not one of them. A year ago, the overwhelming majority had foreseen nothing untoward on the horizon. Six months earlier, they'd thought inflation a greater threat to stability than recession. Non-economists are no better, of course. But there is a difference: the one group recognizes its incompetence; the other doesn't.

The demonstration is that, in the aftermath of the calamity that has recently afflicted global activity, very few professional economists have fallen on their swords. Arguably, almost all should have. Central Bankers, for instance. Did those who'd raised interest rates in 2006 and 2007, in the face of mounting indications of cyclical and secular slowdown, think they'd done a good job? Did they account themselves insightful? Did they sleep well at night?

And what about their opposite numbers in Treasury Departments and Regulatory Authorities? Why hadn't they been more alive to the possibility of financial impropriety? For more than a decade prior to the crisis, money supply had been growing much more quickly than current price GDP. How so? What was happening to the extra liquidity? Was it disappearing into an economics black hole? Or being used improperly? Why had there been no intellectual curiosity?

If an investigation had been launched, the misbehaviour of the mortgage lenders might have been discovered and remedial action taken. In the event, nothing was done. Even after the sub-prime crisis had broken in the US in January 2007, the complacency of the rest of the world was largely unshattered. Officials in London and Frankfurt, Tokyo and Canberra, couldn't conceive of comparable misbehaviour at home. They had to wait until their own crises struck before, in panic-mode, they acted. And what did they do? Mindlessly, because they could think of nothing else, they bailed-out the banks!

Why? What made them think banks important? Why were industrialists and retailers, consumers and pensioners, sacrificed to preserve the scallywags who'd been instrumental in causing the problem? And why did the rest of us let those who'd demonstrated nothing but ineptitude for years beforehand take the helm?

We knew, for instance, that Mervyn King lacked judgment. He'd been one of the 350 infamous economists who'd criticized Margaret Thatcher's policies shortly after she'd become Prime Minister. We knew that Gordon Brown was similarly incapacitated. He'd disposed of the country's gold at the lowest possible price and, worse, unthinkingly financed two disastrous Middle Eastern wars!

Did we suppose that these underperformers would suddenly become saviours? And what was their plan? To take resources from A, and give them to B, in order that B could lend back to A! What genius! Why did anybody take it seriously?

Its implementation helped the banks, of course, but only by harming the rest of the economy. How long would it be before both recovered? A matter of months, or quarters; years or decades? Economists and politicians, a little self-servingly, said the cure would be quick; realists feared that it might be slow.

In effect, the question was trivial: was it recession we were facing, or depression? Was the current debility the weak phase of a *single* business cycle, or would it straddle *several* of them? Nobody knew, least of all those who did most of the talking.

As it happened, we were quite familiar with recessions, much less so with depressions. The one was the *common cold* of the economics world; the other, the *plague*. The first was annoying, but rarely fatal to those affected. The second was devastating, often terminal, blighting the lives even of those who survived it.

The majority of economists assess the current debility as recession. So it's probably not. They reckon the slower rate of decline seen in recent data items will soon turn into unambiguous growth, and that, by early next year, activity will be back to normal. They fear that inflation, a corollary of the still rapid growth in liquidity, will become a problem shortly thereafter.

The sceptical minority says the parallels with previous depressions are alarmingly close. They say it'll take a decade at least, possibly a generation, to re-establish equilibrium. In the meantime, the chances of inflation are negligible.

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