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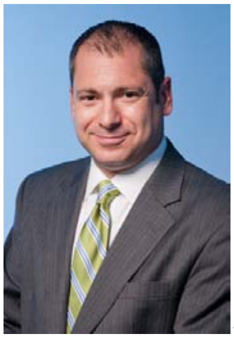

Written by Mitchell O. Goldberg, July 9, 2008.
ClientFirst Strategy, Inc.
For immediate release.

Are we in a recession or not?

This is the BIG question that everyone is asking. The answer is critical because that's what will in large part determine the next move for businesses, consumers, the Federal Reserve, foreign central banks, Congress, and the two Presidential Candidates.

Some pundits say we've been in a recession for some time, some say we're heading into one, and some say we'll avoid one even if just barely.

First, it depends on how one **defines** a recession. ***The conventional definition is 2 quarters in a row of negative GDP***. Based on this definition, we're not there yet. Why aren't we there yet? Because the economy is so much more diversified than it was 20 years ago. Of the 10 major industrial subsets (GICS) of the S&P 500, only financial services are in a major contraction.* It's just that it will take a lot more than that to knock us down for 2 quarters in a row.

However, I am one who believes that as the U.S. economy has undergone such deep structural changes since the last comparable period of **1989-1991**, the definition of a recession needs to be adapted to today's global economy. Back then and like today, the economy underwent a severe banking crisis, horrific red ink from the domestic auto sector, a flat lined home building sector, rising unemployment, and a hard to get credit environment (amongst other negatives). Yet, today we're not net-negative for two quarters in a row. The 2nd quarter GDP figures come out later this month, by the way. I can hardly wait!

So, let me craft a more current and flexible definition of recession with a few more questions and then I'll tie it all together:

1. Is recession a state of mind? This means that if we believe we're in a recession, we'll act like it.
2. Are we so diversified as an economy that we need to say that slower growth is all it takes to be in a recession?
3. Should a recession be defined as an arbitrary term like "unemployment rate of 6% or higher means we're in a recession"?

4. Should the economies of our trading partners be taken into account since our economy is global? About 40% of the S&P 500's profits come from overseas.
5. Should we just use the ISM (Institute for Supply Management) figures for the manufacturing and service sectors as our proxy for the economy?

Tie it all together:

1. Definition of recession: Recessions may now need to be taken on an industry by industry basis. If the majority of industries are in their own recession, then one could postulate that indeed the U.S. economy is in a recession.
2. The "medicines" prescribed in terms of monetary (Fed changes in its target of Fed Funds and Discount Window) and fiscal (tax rebates, tax brackets and codes) policies need to be targeted at the "ill" industries. This is much like an ill patient being prescribed a targeted medication for the specific ailment as opposed to something that targets the entire body.
3. Last, we need to acknowledge that not everyone will be in a recession at the same time.

So, it is clear where the recessions are in the U.S. and now the corrective measures can be aimed squarely where they could do the most good and the least harm, and cost the least.

Now, to the weak Dollar, inflation, eventual recovery in housing, and alternative energy:

1. **<u>The Dollar</u>**, in my opinion, will strengthen when the Fed's backbone strengthens. The Fed moved too slowly at the start of the sub prime crisis and it is now trying to jawbone the Dollar higher. For crying out loud, take a stand! If the Fed wants a stronger Dollar, then it should do what it can – raise the Fed Funds rate. Of course, I don't want the Fed to do anything to hurt the economy! But the market (equities, fixed income and global currencies) is clearly telegraphing that a strong Fed is what it will take to instill confidence back into all global economic participants. A credible Fed is key. Yes, that is my opinion too.
2. **<u>Inflation</u>** is expected to come down when commodities come down. It is believed that since oil is priced in Dollars, a stronger Dollar will push oil prices lower. Hey, there's only one way to find out, Mr. Bernanke. The conventional definition of inflation is too much currency chasing too few goods. The Fed has printed a lot of money to prop up the U.S. Banking industry's balance sheet. Are there too few goods? Is the 100% price increase in a barrel of oil in the last year solely attributable to speculators? Folks, as a student of economics for over two decades, I want to assure you it is rarely just one factor. The fact is; a slower rate of growth both here and abroad should do most of the heavy lifting in bringing down inflation **<u>expectations</u>**. That's right, the inflation "bark" is often worse than the inflation "bite". That's what Fed Governors and the ECB keep telling us; that worsening inflation **<u>expectations</u>** need to be checked.
3. **<u>Eventual recovery in housing</u>**? It'll be here! When? The way I see it, it may take about another year for the U.S. banking sector to shore up its balance sheet. That's why people are so perplexed as to why the banks aren't lending money despite very low interest rates. The banks need to help themselves before they can be in a position to help borrowers. So, I'm looking at mid 2009 for the banks to start lending again. Expect more turbulence in that sector while you wait.
4. **<u>Alternative energy</u>**? Big myth! To me, alternative means that you have a substitute choice. For anyone reading this, you will be utilizing fossil fuels for the rest of your life. As a nation, we simply don't have enough renewable energy sources at this time. I will give

you this much; there are “additional” sources of energy. I expect nuclear energy to play a huge role in this on the global level. I also expect hybrid automobiles to play an ever increasing role. Of course, buying a used car is greener than buying a new fuel efficient car. It is called “recycling”! If we could just get our fossil fuel energy dependence down by, perhaps 5%, we could pay substantially less for all forms of energy. The upside for all of us would be to send less money to unfriendly oil rich states. Hey, maybe we could even get rid of our country’s detrimental ethanol policy. Food prices are rising and hurting the 98% of the people in this country who don’t grow corn. Food inflation is most directly hurting poverty stricken areas of the world; a foreign policy disaster in the making, to be sure. Wherever you see violence in the world, you’ll usually see hungry people too. Remember what Marie Antoinette once said about cake? That basket must’ve had her name on it.

Thanks for reading this. I’m skipping the usual newsletter this month. Please forward this to anyone you know who may find it interesting (or amusing). Please reply me if you would like to comment on this.

(Disclosure: This is solely MY opinion. Of course, you are welcome to share my opinions. If you act on any of this information without speaking to me first and lose money, don’t blame me. I may be wrong. I reserve the right to change my mind about any of this whenever I want and without warning. Have a great freaking day.)

*Standard & Poor’s.