

Who Will be the Buyers Next Year?

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Bloomberg recently reported that Wall Street firms are experiencing their best profit year since 2000. The numbers at this time appear to be \$24B before taxes. This is twice the number they paid out in fines and settlements over the last 4 years prior to 2005. It is pretty darn easy to pay an average of \$3B per year when one makes that kind of money. At any rate it seems that way to us. Financial institutions as a whole account for 30% of total corporate profits as well as 40% of the profits of those that make up the S & P 500. As you probably remember we keep coming back to the proposition that Wall Street continues to do well while Main Street is having a hard time making ends meet. For example, real wages have not advanced at all over this time period and based upon prior recoveries, we are 10 ½ million people behind in total employment. This dichotomy is sure to sow the seeds of future economic weakness. What we have here is overcapacity in finance and undercapacity in demand.

On a larger scale the world economy is much the same in that the US does all the consuming while China and India do most of the producing. China does goods and India does services. It is interesting to note that both are thinking about moving into the each others area. China into servicing and India into manufacturing. What we have here is overcapacity manufacturing and service bureaus and undercapacity in domestic demand. The demand they do have comes mostly from the US, but as stressed again and again we see this topping out due to weak income and high debt. Those things that in the long run make for a prosperous future, globalization, spell economic problems in the short run.

Is there anything in the next year that might allow for increased demand for the huge worldwide overcapacity we presently have? Much of the increase in spending recently has come from borrowing on one's home since 2000. In 2004 it was \$600B. For the period 2001-2004 it averaged \$425B per year. We, of course, also had tax cuts and Federal deficits, which also made for more spending. It is difficult for us to see from where any new stimulus might come.

Wall Street economists keep calling for the corporate sector to kick in with capital spending. But why would this occur when we have too much capacity worldwide now? Most all the spending that is taking place has to do with cutting costs, mostly employees. What is not spent thusly seems to be going for the purchase of their own common stock. In fact, most all the volume in the market place these days seem to be coming from hedge funds trading with one another and cash rich corporations doing stock buybacks. Let's face it, we are in a sense contracting while Asia and the Middle East are expanding.

We expect the question this time next year to be; where has all the demand gone? We believe we must all know by now that large supply and weak demand can lead to only one thing - lower economic activity and deflation.