

A tale of two economies

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Robert Smith

“It was the best of times, it was the worst of times, it was the age of wisdom, it was foolishness ... we had everything before us, we had nothing before us.”

No, that isn't from Barack Obama's second inaugural or even his speech in Cairo. It's Charles Dickens' novel "A Tale of Two Cities." However, it does sound enough like the current situation to give one pause for thought. This is particularly true with regard to the economy.

Ironically, in the age of Obama ("The Great Equalizer"), two very different economies emerged - and they share very little in common. First, there is the Wall Street economy. This is populated by rapacious financial types who spend most of their time gulling unsuspecting folks into predatory mortgages and the like. You know the type - greedy and reckless. Then there's Main Street, beer and pizza, or barbecue case may be, the busted knuckle garage and old Harley parts. The former has benefited enormously from easy money amid tight credit while the latter continues to suffer.

Wall Street houses and equity fund operators are the insiders, while you are the essential grist for their mill. They move back and forth between the highest levels of business and government with consummate skill, profiting enormously thereby. All the while, hours worked and wages earned by the middle class shrink and their savings disappears.

Most ordinary Americans have benefited very little from the run-up in equity prices driven by the Fed's growth of the money supply. Only recently have they seen any recovery in the value of their primary asset - housing. Finally, they have less to spend from their savings because the Fed's near-zero interest rate policy has slashed these anticipated income streams to near zero.

This schism is exacerbated by the siren call of the stock market. With returns on traditional safe-haven investments next to nothing, more and more money is being lured into a stock market that is essentially played out. The higher stock prices go with an economy that is essentially flat and likely to remain so for many more years.

In this environment, the stock market essentially becomes a zero-sum game: someone must lose for another to win. In this case, it's Wall Street and aforementioned fund operators who are the winners, having driven asset prices up over the past four years with the Fed's funny money.

It should be obvious to all by now that monetary illusion (more, cheaper money) is no substitute for real economic growth. All it does is grossly distort the allocation of capital and further enrich a fraction of the population that has access to it.

My advice is to begin raising some cash by selling off some better capital gains positions in equities. A large position will allow one to take advantage of the fluctuation in asset pricing that is sure to come.

The game is about played out. How can an economy that is so weak as to forestall the Fed's much ballyhooed tapering possibly provide more support for further short-term capital gains?

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