# Perryman Financial Advisory, Inc.

Three Forest Plaza
12221 Merit Drive, Ste. 1725
Dallas, Texas 75251
Phone: (972)770-4800
Fax: (972)770-4888

## The Economy Has Hit Bottom

*by Alan S. Blinder*

How's the economy, you ask? I have the proverbial good news and bad news, but in this case, they're exactly the same: The U.S. economy appears to be hitting bottom.

First, the good news. Right now, it looks like second-quarter GDP growth will come in only slightly negative, and third-quarter growth will finally turn positive. Compared to the catastrophic decline we recently experienced -- with GDP dropping at roughly a 6% annual rate in the fourth quarter of last year and the first quarter of this year -- that would be a gigantic improvement.

Furthermore, there is a reasonable chance -- not a certainty, mind you, but a reasonable chance -- that the second half of 2009 will surprise us on the upside. (Can anyone remember what an upside surprise feels like?) Three-percent growth is eminently doable. Four percent is even possible. Surprised? How, with all our economic travails, could we possibly mount such a boom? The answer is that this seemingly high growth scenario isn't a boom at all. Rather, it follows directly from the arithmetic of hitting bottom.

Bear with me for two paragraphs while I do some numbers. In recent quarters, several critical components of GDP have declined at truly astounding annual rates -- like minus 30% and minus 40%. You know the culprits: housing, automobiles and business investment. (Also inventories, about which more later.) Eventually, those huge negative numbers must turn into (at least) zeroes. Notice that the move to zero doesn't constitute a boom, not even a dead cat bounce, but merely the cessation of catastrophic decline. In fact, hitting zero growth and staying there would be a disaster scenario. We'll almost certainly do better.

But watch what happens when -- and remember, it's when not if -- the arithmetic of bottoming out takes hold. Housing, which is down to 2.6% of GDP, will serve as an example. In the first quarter, spending on new homes declined at a stunning 39% annual rate. If that minus 39% number turned into a zero in a single quarter, that change alone would add a full percentage point to that quarter's GDP growth (because 2.6% of 39% is about 1%). If the move to zero were to happen over two quarters, it would add about a half point to each. Many people think housing may in fact bottom out in the third or fourth quarter. Autos may already have passed their low point. And business investment will follow suit.

Now back to inventories. Recent quarters have seen an almost unprecedented liquidation of inventory stocks, which means that American businesses were producing even less than the paltry amounts they were selling. That, too, must come to an end. As inventory change turns from a large negative number into just zero, GDP will get another a big boost.

Now the key point: None of these events are probabilities; they are all certainties. The only issue is timing, about which we can only guess. But if several of these GDP components happen to bottom out at roughly the same time, we could be in for a big quarter or two.

Feeling a little better? There's more.

Remember the fiscal stimulus that everyone seems to be complaining about? One of the critics' complaints is that little of the stimulus money has been spent to date. OK. But that means that most of the spending is in our future.

And remember all those interest-rate cuts the Federal Reserve engineered in 2008, in a futile effort to stem the slide? The Fed's efforts were futile largely because widening risk and liquidity spreads negated any impacts on the interest rates real people and real businesses pay to borrow. Now those spreads are narrowing, which allows the Fed's rate cuts to start showing through to consumer loan rates, business loan rates, corporate bond rates, and the like. In short, monetary stimulus is in the pipeline -- a pipeline that was formerly blocked.

Continued...

***July 2009***

- About Us
- Meet the PFA Team
- PFA in the News
- Contact Us
- Calculators
- Web Links

### Market Watch

| | 7/28/2009 | YTD |
|---|---|---|
| **DJIA** | 9,096 | +3.65% |
| **S&P 500** | 979 | +8.42% |
| **NASDAQ** | 1,975 | +25.24% |

### Special Tax Break for 2009

If you're in the market for a new car, Uncle Sam is providing a powerful tax incentive. You may be able to claim a new above-the-line deduction on your federal tax return. But this tax break comes with a catch: It's phased out for high-income taxpayers.

For purchases made between February 16, 2009 and the end of the year, you can deduct sales and excise taxes attributable to the first $49,500 of a new vehicle's price. The deduction isn't limited to just cars. It also applies to light trucks and SUVs that don't weigh more than 8,500 gross pounds, as well as motorcycles and motor homes. Under these rules, if you buy a new car costing $40,000 in a state with a 6% sales tax, for example, you can deduct $2,400.

However, this new write-off begins to be phased out if your adjusted gross income (AGI) in 2009 exceeds $125,000 for single filers and $250,000 for joint filers. Make more than $135,000 or $260,000, respectively, and you're not eligible for this deduction. (IRS link)