

# Small “d” Depression: The Financial System is stabilized, the Real Economy Continues to Fall

By [Mike Whitney](#)

Global Research, November 12, 2009

12 November 2009

Region: [USA](#)

Theme: [Global Economy](#)

The Fed’s extraordinary intervention into the financial markets, makes another Lehman-type meltdown extremely unlikely. But while the financial system has been stabilized with a government blank check and rivers of liquidity, the real economy continues to languish. On its current trajectory, GDP will fluctuate erratically for a decade or more while the economy seesaws between positive and negative growth. That means persistent high unemployment, flagging demand, and falling living standards. Where the economy finally lands, will depend more on government policies than on market dynamics. Political changes, like the upcoming midterm elections and Blue-dog resistance to additional stimulus, only add to the uncertainty. That’s bad news for anyone who’s looking for job security or who wants to see speedy end to the two year-long crisis.

There’s little chance that the financial system will suddenly implode or that the country will be overtaken by Zimbabwe-type hyperinflation. But the economy will undergo a low-grade depression, a period of sluggishness and retrenchment that drags on for, what seems like, an eternity. This is what typically happens when crises are extended by keeping terminally-ill banks on life-support instead of putting them out of their misery. Capital that could have been used for jobs and productive activity, ends up vanishing down a rathole.

Regrettably, the post-Lehman economy can’t be explained simply in terms of the extremes. Neither “robust recovery” nor “economic Armageddon” accurately describe present conditions. The truth lies somewhere in between, in that vast gray-area where economic indicators conflict with each other and where the best compass is an analyst who knows how to interpret the data. Edward Harrison is a banking and finance specialist who runs the Credit Writedowns website. He posts articles daily and has a solid grip on some very difficult topics. Here’s a recent entry on consumer credit which, paradoxically, appears to be expanding and shrinking at the same time. Here’s how Edward Harrison sums it up:

“Nonrevolving credit is now increasing along with GDP.... On the other hand, revolving credit is getting crushed....Bottom line: “In Q3, banks are lending again (think cash for clunkers) because nonrevolving debt is up. That’s also why GDP is up. But, revolving credit lines (credit card lines) are being cut..” ( Edward Harrison, “Consumer Credit Down, but does it show deleveraging?”  
Credit Writedowns)  
<http://www.creditwritedowns.com/2009/10/the-recession-is-over-but-the-depression-has-just-begun.html>

See how subtle distinctions can make a big difference? In this case, it looks like government programs (cash for clunkers) have actually helped to keep credit flowing into the economy

through even though the banks are still cutting back in other areas. That means that Obama's stimulus has helped to slow the pace of household deleveraging making a crash in personal consumption is less likely. Although some will argue that this merely kicks the can down the road—since households will eventually have to reduce their red ink by either paying off their debts or defaulting—it does make a short-term recovery more probable, which is the objective. Whether that's enough to keep the economy from tipping back into recession, is left to be seen.

In another article, "The Recession is over, but the Depression has just begun", Harrison demonstrates his talent as a capable and insightful analyst. He focuses on the root of our economic problem (debt) and presents a likely scenario of how things will play out. Here's an excerpt:

"The issue was and still is overconsumption i.e. levels of consumption supported only by increase in debt levels and not by future earnings. This is the core of our problem—debt....specifically an overly indebted private sector...."

"When debt is the real issue underlying an economic downturn, the result is a period of stagnation and short business cycles as we have seen in Japan over the last two decades. This is what a modern-day depression looks like – a series of W's where uneven economic growth is punctuated by fits of recession. A recession is merely a period of recalibration after businesses get ahead of themselves by overestimating consumption demand and are then forced to cut back by making staff redundant, paring back inventories and cutting capacity. Recessions can be overcome with the help of automatic stabilizers like unemployment insurance to cushion the blow. Depression is another event entirely." (Edward Harrison, "The Recession is over, but the Depression has just begun", Credit Writedowns)

Harrison describes an economy that is set to bounce along the bottom for years to come. He cites Gluskin Sheff's David Rosenberg, who adds that "Depressions are marked by balance sheet compression" whereas "Recessions are typically characterized by inventory cycles." And, since, "Depressions often are marked by...debt elimination, asset liquidation and rising savings rates" stimulus is not as effective.

This is razor-sharp analysis. By explaining exactly what's going on, it's possible to anticipate what will happen in the future. As Harrison points out, the Fed has already revealed how it plans to fight deflation, by opening up the liquidity faucet and pumping up asset prices. This is the rationale behind Bernanke's zero-percent interest rates, multi-trillion dollar lending facilities, and quantitative easing (QE) programs. Increase asset prices; that's the whole ball-o-wax.

Edward Harrison again:

"As for the recent asset-based economic reflation, be under no illusion that these measures 'solve' the problem. The toxic assets are still impaired and banks are still under-capitalized. But the increased asset value and the end of huge writedowns has underpinned the banks and led to a rise in the broader market in a feedback loop that has been far greater than I could have imagined at this stage in the economic cycle."

Okay, so what's next?

This is where Harrison separates himself from the pack and shows his ability to grasp the complexity of the economy/policy dynamic. His prediction is less-satisfying, but more realistic than many others:

Edward Harrison: "A lot of the economic cycle is self-reinforcing .... So it is not completely out of the question that we see a multi-year economic boom. Higher asset prices, lower inventories, fewer writedowns all lead to higher lending capacity, higher cyclical output, more employment opportunities and greater business and consumer confidence. If employment turns up appreciably before these cyclical agents lose steam, you have the makings of a multi-year recovery. This is how every economic cycle develops. This one is no different in this regard."

So, could a momentum-shift and boatloads of liquidity produce a "multi-year recovery" in spite of nagging structural problems and the massive build-up of personal debt?

Yes. But even though a rebound is economically feasible, Harrison does not think it is probable. He believes that "the government prop for the economy" is going to be removed. In other words, the Congress will not approve a second round of stimulus; the opposition to deficit-spending is just too great. Without more stimulus to maintain the current level of activity, the economy will slide back into recession.

So, get ready for the next leg down; rising unemployment, soaring foreclosures, tumbling stock markets, and growing political unrest. Liquidate, liquidate, liquidate. The Bluedogs and Republican obstructionists are determined to drag the economy back into depression. Onward!

The original source of this article is Global Research  
Copyright © [Mike Whitney](#), Global Research, 2009

---

[Comment on Global Research Articles on our Facebook page](#)

[Become a Member of Global Research](#)

Articles by: [Mike Whitney](#)

**Disclaimer:** The contents of this article are of sole responsibility of the author(s). The Centre for Research on Globalization will not be responsible for any inaccurate or incorrect statement in this article. The Centre of Research on Globalization grants permission to cross-post Global Research articles on community internet sites as long the source and copyright are acknowledged together with a hyperlink to the original Global Research article. For publication of Global Research articles in print or other forms including commercial internet sites, contact: [publications@globalresearch.ca](mailto:publications@globalresearch.ca)

[www.globalresearch.ca](http://www.globalresearch.ca) contains copyrighted material the use of which has not always been specifically authorized by the copyright owner. We are making such material available to our readers under the provisions of "fair use" in an effort to advance a better understanding of political, economic and social issues. The material on this site is distributed without profit to those who have expressed a prior interest in receiving it for research and educational purposes. If you wish to use copyrighted material for purposes other than "fair use" you must request permission from the copyright owner.

For media inquiries: [publications@globalresearch.ca](mailto:publications@globalresearch.ca)

