L. R. Levin Consulting, L.L.C.

Newsletter

September 2008

What Can We Expect in 2009?

Our **Newsletter** this month discusses the key driving forces in the current business cycle. The indicators give some real insight into what the next 18 months look like. Several things have happened in the last few days not yet reflected in the economic data that have a material negative impact. The Fed has intervened in AIG as well as Fannie Mae and Freddie Mac. This was followed by "bailout" or "rescue" legislation, depending on who is discussing it. It is estimated this legislation will cost the taxpayers approximately $3,000 for every person in the United States.

Like so many things in Washington this legislation has become embroiled in politics. As we will discuss in our future **Newsletters**, there are noted economist who believe that these actions not only will makes the coming recession much worse, but materially delay the recovery process. Others think the alternative of permitting failures or not passing the legislation would be worse.

What is certain is that the banking system had begun to freeze up restricting credit and there are no easy solutions. Each action outside normal market forces has its own consequences. The questions are simple, the solutions are complex.

Over the past decade we have experienced an economic cycle that looks a lot like 1919 to 1929.

Rapid technological change, great zeal for greed, and excesses leading to bursting bubbles. These kinds of excesses often take more than a decade to digest.

We are just now beginning to see some of the overcapacity left over from the 90s tech boom fade away through growth and obsolescence. ***How long will it take to absorb all of the new homes, office buildings, and commercial construction?***

The past decade has been characterized by the Fed and monetary policy easing us through the various economic cycles. ***But now we may face the perfect storm where both the Fed and the government have no really effective tools left to guide the ship.*** We face inflation, potential substantial increases in interest rates, a growing trade imbalance and a host of other eco

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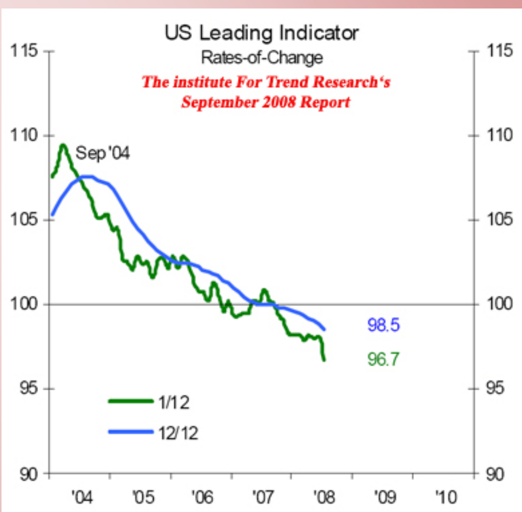
nomic problems that the traditional tools currently available cannot adroitly avoid.

To maintain growth and profits companies need scenario based strategic planning and implementation based on a real understanding of what the coming economic cycle means for them. **What can we expect during the period 2008-2010?**



The Institute For Trend Research (ITR), a premiere economic forecasting organization and our strategic partner, has forecast a continuing decline in economic activity in the last quarter of 2008 continuing through 2009, and

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culminating in a more severe business cycle crunch in 2010.

In short, says ITR, "What the trend says to us is that company growth is going to have to come from within because you shouldn't rely on the overall economy to provide ascent."

What are some of the key drivers that can track whether the economy will follow this path?

- **Petroleum Prices**
- **Natural Gas Prices**
- **Exports**
- **Retail Sales**
- **Strength of the Dollar**
- **M2 Money Supply**
- **Industrial Production**
- **Raw Material Prices**

What is keeping the economic decline moderate?

Several factors are helping keep the economic decline on a moderate rather than a precipitous slope. The decline in Petroleum and Natural Gas Prices, especially as winter approaches, should help stabilize Retail Sales. Similarly, the recent reduction in commodity costs and moderate interest rates should help manufacturing. **ITR, prior to the Fed's most recent actions, sees trends like these permitting conditions to "get marginally better before a broader-based contraction takes hold in 2009."**

Should we expect a severe cycle crunch by 2010?

Why the expectation that a more severe business cycle crunch lies ahead in 2010? The export side of the economy has been crucial for our ability to limp along through most of 2008. **However, with the dollar getting stronger, while foreign economies are decelerating, the export opportunities are waning.**

A big post-election question is how the growing need to fund the cost of government and social programs will impact taxes and interest rates. Higher taxes and interest rates would drain purchasing power from the economy and may well be treated as increasing the cost of goods sold and causing further inflation. **While keeping rates low, the Fed has quietly reduced the real money supply (M2) to fight inflation which means its ability at this stage to come to the aid of hard pressed consumers is severely limited.**

What else over the next 18 Months?

During the next 18 months with domestic consumer sales dropping, exports likely to decline, the value of the dollar rising relatively, corporate profits and margins are projected to decline and with them the stock market. If all this comes to pass, we will experience ***a continuing decline in economic activity in the last quarter of 2008 continuing through 2009, and culminating in a more severe business cycle crunch in 2010.*** This crunch may last awhile. It is possible that we will not see moderate growth again before 2012.

The projected picture is one of rising interest rates, rising inflation, slowing home, commercial, and office construction, lagging ability to maintain transportation infrastructure, and reduced employment opportunities amid a shrinking economy. The real question is one of severity. **The "wild card" is how the government behaves after the election.**

What does this mean for you?

What does this mean for business? Strategic Planning and implementation are key. As ITR put it, "A plan that has its basis in rising with the tide and going with the flow is going to lead to diminished opportunities and poor financial performance. Seek solutions from internal changes and decisions that you can control."