

OBAMA'S
ECONOMY

For a parallel to the challenges Obama faces as he assumes office...

You don't have to look as far back as FDR and the Great Depression.

Most presidents of the past 60 years have taken the oath amid varying degrees of economic stress. Though the present situation may turn out to be more dire than what other rookie presidents faced, their crises were very real at the time.

Truman had to guide the nation from a wartime to a peacetime economy, shifting from strict controls to a free market. The transition didn't go smoothly.

Ford and Carter were dogged by problems mostly not of their own making but spurred by a 600% hike in the global price of petroleum from 1973 to 1980.

The presidents Bush, father and son, took office at the end of expansions that eventually collapsed of their own weight in late-stage speculative excesses. Both suffered the hangovers. What's more, both had the misfortune of presiding over recessions when international crises further weakened the U.S. economy.

Reagan faced an economic crisis most similar in magnitude to today's. Unemployment was a nasty 7% and climbing fast; inflation had been running at 12.5%. Interest rates in the high teens crippled residential real estate and business investment. The stock market had been in a rut since 1966.

The cost of the cure was high. The Fed tightened the screws on credit, pushing the economy into the worst recession since the 1930s. Despite stimulus from deep cuts in tax rates and a military buildup, output still took a nosedive... down 5%-6% in back-to-back quarters. Joblessness hit almost 11% in late 1982. Tax receipts fell but not spending, producing a modern record deficit... 6% of GDP.

In short, Reagan inherited a sick economy that worsened before recovering. But recovery did come...in the middle of his first term...and voters credited Reagan with playing a key role in bringing it about, gratefully reelecting him in 1984.

Obama will likely experience something similar with this difficult economy, which will probably worsen before growth resumes. Today's unemployment rate of about 7% will hit at least 9% and may approach the double-digit peak of 1982. The contraction will probably bottom out by midyear, but the ensuing growth will be weak for another year or so. As tax receipts again plunge and costs zoom, Reagan's record federal deficit will be eclipsed, topping \$1 trillion...7% of GDP.

Like Reagan, Obama has tax cuts in his quiver, and he will use them.

But most of his faith is in the stimulus of infrastructure spending on transportation, alternative energy and public school renovations... projects he views not as New Deal-style make-work, but as investments in the future.

Obama will be judged on how well the economy is nursed back to health by the White House, Congress, the Fed and American business leadership.

This will take time, but all recessions eventually end. What's more, since they've never run their course without a variety of remedies being tried, no one can be sure which treatments work and which might prolong the slump.

On Inauguration Day, the new president and all Americans can take heart:

The challenges ahead are not unprecedented in recent U.S. history.

The nation has met and matched equally daunting crises before, finding a way to get back on track. There is no reason to believe America can't do it again.

Yours very truly,

Knight/Kiplinger
THE KIPLINGER WASHINGTON EDITORS

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