A 'Bigger Boat' Is Needed to Endure Current Economic Crisis

Policymakers may be unprepared for 'echo crisis' says SCM Advisors Strategist

HARTFORD, Conn., July 20 /PRNewswire-FirstCall/ -- In his latest quarterly commentary, Max Bublitz, chief strategist and portfolio manager at SCM Advisors LLC, an affiliated investment manager of Virtus Investment Partners (Nasdaq: VRTS), likens the recent financial tumult to a critical moment in the 1975 thriller "Jaws" when Police Chief Martin Brody first realizes the enormity of the great white shark terrorizing the beaches of Amity. "You're gonna need a bigger boat," a wide-eyed Brody tells the captain of the ship that's hunting the shark.

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"We get the distinct impression that many policymakers today are staggering around with their Chief Brody face on, realizing that a bigger boat may indeed be needed," Bublitz writes.

He notes that while there has been both an economic and market bounce from government efforts to respond to the 2008-2009 recession, the recovery has been extremely fragile and significantly weaker than what many expect. Money and credit growth is nonexistent, the labor markets have been slow to respond, and most important, debt – the root cause of the crisis – has not been meaningfully reduced," says Bublitz.

Now, we must hope for a successful handoff from the government to the private sector. That will be the point when the economic recovery is sustained enough for private sector earnings to help offset the effects of deleveraging, leaving the government to go about the business of putting its fiscal house in order.

Bublitz doesn't expect any Fed rate hikes until well into 2011, and is actually expecting to see another round of easing from the Fed. "(Fed Chairman Ben) Bernanke can't and won't tolerate a double-dip recession out of fear of creating a cut and paste version of the 1930s. Like Amity's mayor, he knows full well the impact of closing the economic beaches."

Economic growth for this cycle has likely peaked, both in the U.S. and abroad, and Bublitz forecasts slower growth in the second half of 2010 with domestic GDP falling below 2 percent. He also believes that neither the housing nor labor market has hit the bottom of their cycles. On the positive side, while inflation is nearing its trough, the timeframe for it to become a concern for the economy can now be measured in years, not months.

The financial system now finds itself in the next phase of the crisis, an "echo crisis," which, Bublitz says, has led to an echo in volatility. "We continue to view the rally off the March 2009 lows as a cyclical bounce within the secular bear market that began in 2000. The major indexes are retesting their lows for the year for the fourth time, and we're left with many more questions than we have answers."

Policymakers will need to keep their eye on a number of trends – such as consumer and business confidence, money and credit trends, the jobs picture, and the direction of the dollar – to help them decide on a course of action. "But however they respond, we're definitely in the middle of one hell of a lab experiment," Bublitz says. "No doubt, these are highly uncertain and likely very volatile times."

About SCM Advisors LLC

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