

October 21, 2009

The Second Act

President Obama got a big lift from the Nobel Prize Committee. By celebrating the President, the award underscored and added gravitas to his vision of peace. It's a pity there is not a parallel award to bless and focus the President's domestic agenda.

The curtain has risen on the President's second act. In the theatre, the second act deepens the understanding of the characters and their motivations. Conflicts intensify. Players take center stage. Relationships change. The audience warms to some characters and distances itself from others.

From the opening curtain, President Obama has been able to articulate the issues and propose an agenda but he has left the details to Congress. White House leadership on the stimulus bill, for example, seemed so distant that the result was legislation inadequate to jolt the economy out of its stupor. In the ensuing months, whether healthcare or regulatory reform, the President's team has not been able to back up the boss's words with legislation. A question arises from this pattern of whether "Yes We Can" will become "Well, We Tried!"

We have some suggestions for a successful second act. Let's start with director's notes, which might be viewed as style over substance but in government, as the theatre, presentation creates illusion.

Stay in the Oval Office more. Stop popping up in Copenhagen acting like a barnstorming mayor or being ubiquitous on Sunday talk shows. Why give a pedestrian speech on Wall Street after a Presidential address to Congress. The constant drum of exposure doesn't seem to be translating into effective government.

Expand the mix of your advisors; fill the vacancies in Treasury's senior staff. Get some business folks in more prominent places. Now, most of the private sector members of the Administration are former Wall Streeters camouflaged as Counselors in the Treasury. Not even the Secretaries of Commerce or Treasury are from business.

Lack of business participation in the Administration, coupled with broad attacks on business sectors – beyond the requisite Wall Street philippics – hinder efforts to build the business confidence required for a sustained recovery.

Vary your tone. Jerry Seinfeld has a wonderful comedy routine on "tone" – a quality he didn't know his voice had until he was married. President Obama's tone is cool but sometimes "cool" masks intensity. It's hard for the audience to distinguish priorities from secondary goals.

From a policy perspective, the Administration needs an effective economic second act. Skillfully, its actions avoided the abyss. It and the Fed created a series of effective programs – TARP, TALF, P-PIP, guarantees of bank deposits, commercial paper and other instruments – and restructured the auto industry which unfroze the capital markets. By and large, however, the initiatives bailed out big banks, big unions, big pension funds and big companies.

The blowout earnings reported by Goldman Sachs and JPMorgan are a tribute as much to the success of public policy as they are to the trading skills of those firms' employees.

The Administration's dilemma is that Main Street business has not benefited to the same extent. As recently as October 14th, Bridgewater Associates, the largest hedge fund, noted for its research, wrote that "a significant portion of the US economy represented by small business is still contracting" and is in a "dismal" condition.

There are two problems for most businesses but particularly for smaller ones – demand and credit!

The demand issue is obviously a result of the slow growing economy. To an extent, it also reflects the lower exposure of smaller companies to the export market, propelled by the collapse of the dollar.

The credit issue is more serious because even in the absence of demand, credit has become scarce.

In the recent JPMorgan earnings statement, outstanding loans to businesses in every size category decreased. Credit companies like GE and American Express are also reducing their exposure. CIT, a major lender, is in reorganization. Illustratively, last month, our corporate card issuer notified our firm of a reduction in PJSC's credit line. Simultaneously, we had requested an increase because of our growing business. The issuer immediately saw the error of its ways, but the challenge it presented is being repeated nation-wide.

The same phenomenon is affecting consumer credit. In the consumer's case, the reduced borrowings result partially from the loss of home equity and lower incomes. Pressure by Government on credit companies to reduce fees, lower late charges and generally decrease profitability, coupled with the imminent Consumer Protection Act, has also led to issuers reducing exposure dramatically. With consumption representing an historically high 71% of the GNP, a robust consumer remains the springboard to economic growth.

What are the actions the Fed and Treasury need to mitigate the credit scarcity for smaller companies? First, obviously, keep money as "easy" as possible. To most businesses, short-term price deflation is a greater risk than inflation. Raising rates would be devastating to Main Street.

Second, use the bully pulpit of the Oval Office to encourage lenders to provide more loans. Banks are re-building their capital through cheap borrowings and Government programs. It may be unusual to suggest that an American President emulate the French. But President Sarkozy is employing the prestige of the Elysee Palace to persuade French banks to increase lending.

Use TARP and TALF to support lending through the Small Business Administration. The Treasury has allocated \$636 billion to TARP financings but \$270 billion is unspent. Additionally, TALF –

successful insofar as it thawed the secondary capital markets for asset-backed securities – seems to have had less impact on new loans. The Treasury planned to allocate \$70 billion to this effort but has, according to its own records, used \$100 million.

We are in the middle of the second act. The plot line is unclear. The economy could continue its recovery and justify the stock and debt market rallies. Or, it could follow the course of little growth and unacceptable levels of unemployment. Without a narrowed focus on the economy and direction to support the broader range of businesses, the Obama second act may well disappoint.

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