

Healing Light Cast on 2011

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EXPECTATIONS for economic growth were modest at best heading

into 2010, and that's what the year has delivered. The only good news, really, has seemed to be that the worst hasn't happened. No double-dip recession. No collapse of the banking system.

With the dawning of 2011 on the horizon, the outlook had already turned brighter, even before the outcome of the November elections buoyed the spirits of the business community. "The bias of the U.S. economy is that it wants to grow," observes Ron Davis, Ph.D., and Printing Industries of America's (PIA) chief economist and vice president.

Then came the decision by Ben Bernanke, chairman of the U.S. Federal Reserve (the Fed), to purchase \$600 billion worth of long-term Treasury securities to provide an economic stimulus. While it did elicit concerns about inflation and complaints from foreign governments, the move has largely garnered a wait-and-see response domestically.

Because of such unknowns, Davis frames his outlook in terms of The Good, The Bad and The Ugly scenarios. Heading into the fall, he was betting on The Bad—sluggish recovery, with a GDP growth rate of 2.7 percent in 2011 and 2.7 percent in 2012.

However, the outcome of the November elections and other factors now have PIA's economist somewhat more optimistic about the outlook for 2011 and 2012. Davis sees the most likely trajectory of the economy over the next two years bringing inflation-adjusted growth of 3.3 percent in 2011 and 3.5 percent in 2012. He puts the likelihood of that scenario at 50 percent vs. 30 percent for a continued sluggish recovery, and 20 percent for a double-dip recession (The Ugly).

Davis explains that the Republican gains were stronger than he thought they might be, which hopefully will lead to a more positive, settled political climate rather than "bickering over not very important things. That would erode confidence."

Haunted by Excess

Keeping tax rates at their current levels is factored into his now more optimistic "likely" scenario, but not any additional cuts. Davis would also like to see some moratoriums on new regulations and maybe the Environmental Protection Agency backing off enactment of cap-and-trade regulations on carbon emissions.

There's no question that the economy is healing, agrees Andrew Paparozzi, NAPL's chief economist and vice president. "Any indicator you look at—whether it is employment or GDP, consumer spending or industrial production—is noticeably and meaningfully stronger than it was a year ago. But it is a painfully slow and maddeningly inconsistent process because we created such severe excesses. There's simply no easy way to purge those excesses. It is happening, but it's going to take time."

Rather than the election results, Paparozzi believes the response of the new Congress and President Barack Obama to the Bowles-Simpson Deficit Reduction Plan will be the real indicator of any positive impact on the economic outlook.

"Right now, the election is a non-factor because it didn't prove anything," he asserts. "Everyone knows what has to be done. The question is: will they work together to craft a credible plan for getting it done? The response to the deficit reduction commission will be our first indication of whether anything has, in fact, changed, rather than simply shuffling a bunch of seats around."

The latest Blue Chip Economic Indicators forecast is for 2.7 percent growth this year and 2.5 percent in 2011, notes NAPL's economist. "Those numbers are very, very weak for the first year of recovery from a very deep recession. Normally, the deeper the recession, the stronger the first year or two of recovery simply because of the pent-up demand that is created and then released early in the recovery."

NAPL is projecting printing industry sales to come in somewhere

between down 1 percent or flat to maybe up fractionally in 2011. "We had originally thought sales were going to grow 2 percent to 3 percent this year," Paparozzi reports.

"We are projecting 1 to 3 percent growth in 2011. If you're counting on the economy making everything right, you're going to be very disappointed. Whereas our recoveries had been inclusive, they are now increasingly exclusive. They are reserved for companies that are prepared for what our industry is becoming."

During the downturn, market leaders—as NAPL defines them—have been able to stay focused on getting more efficient, more productive and more valuable to their clients, according to Paparozzi. They are now in a position to dramatically widen their lead over the rest of the industry. "Even now, while everyone still has this kind of wait-and-see mentality, the leaders are getting prepared to grow and gain market share at the expense of their competitors. It happened after the last recession, and it will happen after this one."

Based on his likely scenario, Davis is forecasting print markets to "grow by around 3 percent or so" (on a nominal, non price-adjusted basis) in 2011 and 2012. He, too, notes that this economic recovery is lagging significantly compared to the historical trend. That will contribute to "printing shipments remaining below pre-recession levels."

Confidence Not High

Despite the improvement in the economy, PIA's economist doesn't expect any significant increases in printers' costs other than the ongoing upward trend in healthcare costs and possibly paper prices because that industry has been rationalizing its capacity. "I don't think there's going to be any pressure on wages, at least within the next year and half or two years," he adds.

Beyond 2011, Davis cautions that there is potential for risk to the economy in the Fed's latest mon-

etary move, and he doesn't believe the credit market is what's holding back growth. "The big problem is consumer and business confidence. They're both not buying. I think the wheels are in motion with what the Fed had previously done to bring economic growth."

The Fed is now gambling that down the road it can take money back out quickly enough to avoid having things get out of hand and cause inflation, the industry economist surmises.

There's also the risk that the current verbal backlash from for-

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eign governments could turn into trade wars. "If we come out on the right side of those two issues, we could still see six or seven years of growth after this recession before we go into the next one," he adds.

As for the printing industry specifically, Davis has laid out his vision of its future in a new book, titled "Competing for Print's Thriving Future." His thesis is that print markets will reach equilibrium where they stop declining and then, conceivably, the total dollar volume of print could start growing again from that level.

"Somewhere around five or 10 years out, we'll start to see this decline in real, inflation-adjusted print shipments stabilize and then start to grow as GDP grows. This is a little different from what I have been saying. Print has value, and you can only do so much electronically. There will be a significant portion of printers—the survivors who have their act together—that do very well," Davis concludes.

Not Out of the Woods

NAPL's Paparozzi has a different take on the Fed's announcement. "It's not a panic move, but it is a clear statement to me that they (its

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board of governors) are still incredibly concerned about the state of the economy. They're still very concerned about the banking system, residential real estate, commercial real estate and mortgages. To their credit, in my opinion, they are erring on the side of doing too much rather than too little."

The obvious, longer term concerns are the potential inflationary aspects of the move and the impact on the American dollar, Paparozzi adds. "Bernanke knows the kinds of problems that this type of credit creation can produce, but right now he has a choice to make. 'Do I hope that everything works out or do I do what I believe is necessary to reduce the chances that the

economy slips back into recession, and then worry about the negative consequences of this huge liquidity creation later on?'"

Deflation is a bigger concern than inflation, the NAPL economist says, because "we know how to correct inflation. The last thing Bernanke wants to do is see deflation because we really don't know how to correct that. He has access to a whole lot of indicators the rest of us don't that clearly are telling him very important parts of the economy are not on firm footing just yet. The patient hasn't reached the point of a sustainable recovery."

Unemployment has replaced consumer spending as the economic indicator to watch, since the recovery won't be sustainable until the level of unemployment is much lower than what it is now, Paparozzi con-

tends. It's a Catch 22 situation, though, since employers have to be convinced that the recovery is, in fact, sustainable before they will add staff.

"Once they are convinced, then you'll see a surge in hiring because staffs are stretched so thin. I can't imagine that's going to happen until sometime late in the second half of 2011," he predicts. "Uncertainty paralyzes people. It's not a matter of Washington coming up with policies that are universally endorsed because whether you agree with the policies are not, knowing what they are is a big step forward. Once businesses know what to expect, they can then deal with it."

Printing businesses face an additional challenge because the industry continues to be redefined, NAPL's economist says. "Compa-

nies have to make themselves more competitive (re: more efficient and productive), and more valuable to their clients. There are big opportunities for growth, but not in the same places or by doing the same old things.

"Look for industries that give you the best opportunity to really make yourself more important to those clients and thereby insulate yourself from the vagaries of a commodity business," Paparozzi concludes. "Certain industries, like gaming and healthcare, are much more advanced in terms of knowing about their clients and collecting the kind of data on their customers that support personalized, data-driven marketing." **PI**