



Your Global Investment Authority

School Daze, School Daze Good Old Golden Rule Days

A mind is a precious thing to waste, so why are millions of America's students wasting theirs by going to college? All of us who have been there know an undergraduate education is primarily a four year vacation interrupted by periodic bouts of cramming or Google plagiarizing, but at least it used to serve a purpose. It weeded out underachievers and proved at a minimum that you could pass an SAT test. For those who made it to the good schools, it proved that your parents had enough money to either bribe administrators or hire SAT tutors to increase your score by 500 points. And a degree represented that the graduate could "party hearty" for long stretches of time and establish social networking skills that would prove invaluable later on at office cocktail parties or interactively via Facebook.

College was great as long as the jobs were there.

Now, however, a growing number of skeptics wonder whether it's worth the time or the cost. Peter Thiel, an early investor in Facebook and head of Clarium Capital, a long-standing hedge fund, has actually established a foundation to give 20 \$100,000 grants to teenagers who would drop out of school and become not just tech entrepreneurs but world-changing visionaries. College, in his and the minds of many others, is stultifying and outdated – overpriced and mismanaged – with very little value created despite the bump in earnings power that universities use as their *raison d'être* in our modern world of money.

Fact: College tuition has increased at a rate 6% higher than the general rate of inflation for the past 25 years, making it four times as expensive relative to other goods and services as it was in 1985. Subjective explanation: University administrators have a talent for increasing top line revenues via tuition, but lack the spine necessary to upgrade academic productivity. Professorial tenure and outdated curricula focusing on liberal arts instead of a more practical global agenda focusing on math and science are primary culprits.

Fact: The average college graduate now leaves school with \$24,000 of debt and total student loans now exceed this nation's credit card debt at \$1.0 trillion and counting (7% of our national debt). Subjective explanation: Universities are run for the benefit of the adult establishment, both politically and financially, not students. To radically change the system and to question the sanctity of a college education would be to jeopardize trillions of misdirected investment dollars and financial obligations.

Conclusion to ponder: American citizens and its universities have experienced an ivy-laden ivory tower for the past half century. Students, however, can no longer assume that a four year degree will be the golden ticket to a good job in a global economy that cares little for their social networking skills and more about what their labor is worth on the global marketplace.

Fareed Zakaria, as usual, has a well-thought-out solution. "We need," he writes, "a program as ambitious as the GI Bill," but one that focuses on retraining existing unemployed workers and redirecting our future students. Instead of liberal arts, he suggests focusing on technical education, technical institutes and polytechnics as well as apprenticeship programs. Our penchant for focusing on high tech value-added jobs should be modified and redirected, he claims, to mimic the German path, which allows people with good technical skills but limited college education to earn a decent living.

One thing college does do is to keep 25 million students off the unemployment rolls, much like it did for me when I went on my own four year vacation. The world was a different oyster in 1966, however, and it behooves America to recognize the reversal and the necessity for significant changes if it is to compete in the global marketplace of the 21st century.

It is becoming obvious that the 2012 election will be fought on a battlefield of job creation. A 9.1% official unemployment rate, and a number nearly double that when discouraged and part-time workers are included in the rolls, portend an angry and disillusioned electorate, which will include millions of jobless college graduates ill-trained to

compete in the global marketplace. Over the past 10 years under both Democratic and Republican administrations, only 1.8 million jobs have been created while the available labor force has grown by over 15 million. It is clear, however, that neither party has an awareness of the why or the wherefores of how to put America back to work again. Few economic advisors from either party ever mention structural long-term disconnects in employment – a recognition that cyclical influences will no longer dominate the U.S. labor market. Manufacturing and goods exports have ceded enormous ground to China and other developing labor markets, as America's reliance on services and high tech innovation has exposed gaping holes in an historically successful model. Almost any industry dominated or significantly connected to finance and financial leverage has hit the canvas and stayed down in the aftermath of Lehman 2008. Housing construction, real estate brokerage, banking and consumer retail employment will likely never come back to levels dominated by our prior decade's excessive leverage and its abuse leading to overconsumption. Because of that focus, a "shovel-ready," vigorous manufacturing sector is not there to pick up the slack.

Similarly, the high tech paragons of the 21st century – Apple, Microsoft, Google, Facebook et al. – never were employers of high school or B.A. college graduates in significant numbers. Production of hardware, to the extent that any was needed, quickly gravitated to foreign ports of call where workers were willing to produce an excellent product for 1/10th of the U.S. wage. The past several decades have witnessed an erosion of our manufacturing base in exchange for a reliance on wealth creation via financial assets. Now, as that road approaches a dead-end cul-de-sac via interest rates that can go no lower, we are left untrained, underinvested and overindebted relative to our global competitors. The precipitating cause of our structural employment break is both internal neglect and external competition. Blame us. Blame them. There's plenty of blame to go around.

Solutions from policymakers on the right or left, however, seem focused almost exclusively on rectifying or reducing our budget deficit as a panacea. While Democrats favor tax increases and mild adjustments to entitlements, Republicans

pound the table for trillions of dollars of spending cuts and an axing of Obamacare. **Both, however, somewhat mystifyingly, believe that balancing the budget will magically produce 20 million jobs over the next 10 years.** President Obama's long-term budget makes just such a claim and Republican alternatives go many steps further. Former Governor Pawlenty of Minnesota might be the Republicans' extreme example, but his claim of 5% real growth based on tax cuts and entitlement reductions comes out of left field or perhaps the field of dreams. The United States has not had a sustained period of 5% real growth for nearly 60 years.

Both parties, in fact, are moving to anti-Keynesian policy orientations, which deny additional stimulus and make rather awkward and unsubstantiated claims that if you balance the budget, "they will come." It is envisioned that corporations or investors will somehow overnight be attracted to the revived competitiveness of the U.S. labor market: **Politicians feel that fiscal conservatism equates to job growth.** It's difficult to believe, however, that an American-based corporation, with profits as its primary focus, can somehow be wooed back to American soil with a feeble and historically unjustified assurance that Social Security will be now secure or that medical care inflation will disinflation. **Admittedly, those are long-term requirements for a stable and healthy economy, but fiscal balance alone will not likely produce 20 million jobs over the next decade. The move towards it, in fact, if implemented too quickly, could stultify economic growth.** Fed Chairman Bernanke has said as much, suggesting the urgency of a congressional medium-term plan to reduce the deficit but that immediate cuts are self-defeating if they were to undercut the still-fragile economy.

Academics also point to a theory known as Ricardian equivalence, a notion named after David Ricardo from the early 19th century. His ivory tower theorem was that consumers would become more and more confident of their financial future if in fact they believed that their own government's exuberance would be held in check. Balance the U.S. or any government budget, he prophesied, and the private sector would extend and lever theirs. Well,

commonsensically and anecdotally, I know of no family who, after watching the Republican candidates' debate in New Hampshire, went out the next day and bought themselves a flat screen under the assumption that their Medicare entitlements would be cut in future years and the U.S. budget balanced. Ricardo and his "equivalence" belong in the trash bin of theses and research aimed more towards academics than a practical remedy to America's job crisis.

What then, shall we do? My preferred solution has long-term elements, which includes the opening language in this *Investment Outlook*, concerning the value of a college education as currently structured. Peter Thiel may be on to something, but all of our kids just can't up and quit college à la Bill Gates. Still, if we are to compete globally while maintaining a higher wage base, we must train for "middle" in addition to "high" tech. Philosophy, sociology and liberal arts agendas will no longer suffice. Skill-based education is a must, as is science and math.

Additionally and immediately, however, government must take a leading role in job creation. Conservative or even liberal agendas that cede responsibility for job creation to the private sector over the next few years are simply dazed or perhaps crazed. The private sector is the source of long-term job creation but in the short term, no rational observer can believe that global or even small businesses will invest here when the labor over there is so much cheaper. That is why trillions of dollars of corporate cash rest impotently on balance sheets awaiting global – non-U.S. – investment opportunities. Our labor force is too expensive and poorly educated for today's marketplace.

In the near term, then, we should not rely solely on job or corporate-directed payroll tax credits because corporations may not take enough of that bait, and they're sitting pretty as it is. Government must step up to the plate, as it should have in early 2009. An infrastructure bank to fund badly needed reconstruction projects is a commonly accepted idea, despite the limitations of the original "shovel-ready" stimulus program in 2009. Disparate experts such as GE's Jeff Immelt, Fareed Zakaria, Jeffrey Sachs and Paul Krugman believe an infrastructure bank to be an excellent use of deficit

funds: a true investment in our future. While the current administration admits that the \$25 billion in Recovery Act spending on infrastructure only created 150,000 jobs, it also stabilized and improved this nation's productivity for years to come. Clean/green energy investments also come to mind, most of which require government funding and a government thrust in order to create millions of jobs. China knows this and is off and running. The U.S. needs to learn from their state-oriented model. In times of extremis, pushing on the private sector string is ineffective, especially within the context of a global marketplace that offers alternative investment locations. Government must temporarily assume a bigger, not a smaller, role in this economy, if only because other countries are dominating job creation with kick-start policies that eventually dominate global markets.

And how about at least an intelligent discussion on "trade policy" which incorporates more than just a symbolic bashing of Chinese currency relative to the dollar. Who, from either side of the aisle is willing to discuss the use of trade measures in order to help balance our \$500 billion trade deficit? This is delicate territory, reawakening fears of Smoot-Hawley in the 1930s, but we are in delicate territory regarding our unemployment rate as well. Warren Buffett in 2003 advocated an idea he called "Import Credits" which he claimed would increase exports in the hundreds of billions and jobs in the hundreds of thousands. Republicans? Democrats? Discussion please.

In the end, I hearken back to revered economist Hyman Minsky – a modern-day economic godfather who predicted the subprime crisis. "Big Government," he wrote, should become the "employer of last resort" in a crisis, offering a job to anyone who wants one – for health care, street cleaning, or slum renovation. FDR had a program for it – the CCC, Civilian Conservation Corps, and Barack Obama can do the same. Economist David Rosenberg of Gluskin Sheff sums up my feelings rather well. "I'd have a shovel in the hands of the long-term unemployed from 8am to noon, and from 1pm to 5pm I'd have them studying algebra, physics, and geometry." Deficits are important, but their immediate reduction can wait for a stronger economy and lower unemployment. Jobs are today's and tomorrow's immediate problem.

Those who advocate that job creation rests on corporate tax reform (lower taxes) or a return to deregulation of the private economy always fail to address dominant structural headwinds which cannot be dismissed: 1) Labor is much more attractively priced over there than here, and 2) U.S. employment based on asset price appreciation/finance as opposed to manufacturing can no longer be sustained. The "golden" days are over, and it's time our school and jobs "daze" comes to an end to be replaced by programs that do more than mimic failed establishment policies favoring Wall as opposed to Main Street.

William H. Gross
Managing Director

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840 Newport Center Drive
Newport Beach, CA 92660
+1 949.720.6000

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