



# ANALYSIS | Seeking a bottom for an entire economic cycle: Don Pittis

Must we suffer the painful changes of capitulation for recovery?

By Don Pittis, [CBC News](#) Posted: Jan 18, 2016 5:00 AM ET | Last Updated: Jan 18, 2016 5:00 AM ET



Terra Green, who was seeking a job last week in the previously booming Bakken oilfield on the Saskatchewan-North Dakota border, found that she was too late. (Andrew Cullen/Reuters)

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**Don Pittis**  
The Business Unit

As oil concluded a bad week with a **plunge of nearly \$2 a barrel** on Friday, it seems pretty clear that something's got to give.

"Everyone was assuming that Russia and/or the North Sea or somewhere — some of these mature basins — would have seen dramatic declines [in production] because of those low oil prices," said Citigroup's top energy analyst **Seth Kleinman** in a recent interview. But it hasn't happened yet.

Stock traders sometimes talk about **capitulation**, a moment when markets give up all hope of recovery and finally collapse. As oil, stock markets, the loonie and perhaps the entire world economy, tumble from low to new low, it may be that we need to see real signs of surrender before the world can bounce back again.

- [Canadian dollar dips below 69 cents US as oil resumes slide](#)
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In his book *The Upside of Down* Canadian author Thomas Homer-Dixon describes something he calls **catagenesis**, where "catastrophe is followed by creativity and eventual renewal."

## Cleansing fire

Seen in the grand sweep of history, a devastating war or a fire in a great city that allows its citizens to rebuild an even better city may seem worth the sacrifice. Such events are hell to live through.

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Don Pittis has been a Fuller Brush man, a forest fire fighter and an Arctic ranger before discovering journalism. He was principal business reporter for Radio Television Hong Kong before the handover to China and has produced and reported for CBC and BBC News. He is currently senior producer at CBC's business unit.

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- [The Upside of Down by Thomas Homer-Dixon](#)
- [Seth Kleinman interview on oil \(Bloomberg\)](#)

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Good things can come out of a crisis, but few people willingly accept the consequences. (Reuters)

In his book *Homer-Dixon* must have captured a mood. He published it in 2007 as if anticipating the great market meltdown from which the world is still struggling to recover.

But at the time it appeared *Homer-Dixon* was wrong. Rather than a crumbling followed by renewal, the world's governments merely flooded the market with more money, keeping the old system running. There was no catagenesis because there was no catastrophe.

With so many opinions in this wide world, inevitably there are those who are impatient for the Marxist crisis of capitalism that will bring us into a new world order. Those who read history and understand the destructive power of previous economic and social breakdowns are less likely to wish for a new one.

The current market for oil is a less portentous example that helps to illustrate the economic pressures that come to bear.

## Blinking last

There is so much at stake for oil-producing countries that none wants to be the first to cut production. Even at current prices below \$30 a barrel, countries such as Venezuela and Russia, to name just two prime examples, are so dependent on foreign exchange from oil exports that they are under pressure keep selling despite the falling price.



People line up to buy basic products outside a supermarket in Caracas, Venezuela last week. The plunging price of oil is hurting, but production remains high. (Reuters)

In developed countries, including Canada, private companies also continue to produce even after the price they earn is **less than the cost of production**.

As Kleinman points out, Russian oil production finished the year at an all-time high. All we have seen so far is a slight cutback in U.S. shale drilling. At the same time, Kleinman says, emerging markets such as Brazil that drove the oil and commodities boom as they consumed more and more are now shrinking, meaning that demand has declined even as production has grown.

Each oil producer is betting that one of the others will crack first. As in a war, every country and every company hangs on until they reach a crisis



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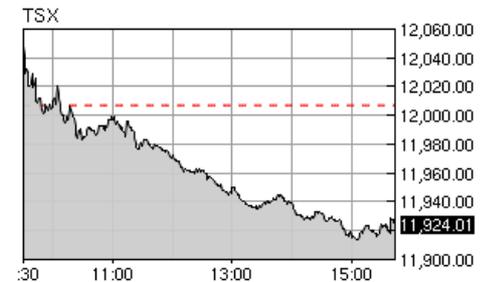


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point. In a country, perhaps it will be a moment of social collapse. In the case of companies, it will be the final moment when company managers and their bankers just cannot justify continuing.

## Hitting bottom

Unlike economies ended by war or cities destroyed by fire, market capitulation is not so extreme.

New York's Dow Jones index and the TSX were down hundreds of points on Friday. No one seems quite sure when it will stop. The **price of houses in Calgary** is looking for a bottom. So is the loonie, which is dependent, at least partially, on the value of oil and copper, which depend on when China hits bottom.

In market lore, capitulation is a good thing. Companies have been forced by necessity to cut costs. Some have gone broke. Capitulation, if you can recognize it, is when all the bad news has been priced in and markets can begin to rise again.

In the wider global economy, there may be problems that have not yet been solved that still require the pressure of necessity to force governments into unpalatable action.

No one wants to sell their house for less than they think it's worth. No one voluntarily asks for their buying power to shrink. No one wants to pay higher taxes. Sometimes it is only the cruelty of recessions and capitulation that forces us to make painful change.

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