# Trade deficit up, as US economy turns down

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A series of statistics released last week show a worsening in the international financial position of the US economy and underscore growing fears that it may be entering a new economic downturn.

Government figures showed that the US trade deficit in November surged by 13.9 percent to reach a record $40.1 billion. This was well above the level of around $36 billion which had been predicted by most economists. While some of the increase was due to a rapid rise in imports following the ending of the Los Angeles port shutdown in October, there is no mistaking the underlying trend. At $390.5 billion, the trade deficit for the first 11 months of 2002 has already surpassed the previous annual record of $378.7 billion set in 2000.

Commenting on the widening trade and balance of payments deficit, the Economic Policy Institute pointed out that it was leading to growing levels of foreign debt. It predicted that the US net foreign debt would reach an all-time high of $2.8 trillion in 2002, equivalent to 27 percent of US gross domestic product.

"The rapid growth of US foreign debt," it noted, "threatens the stability of the US economy: if foreign investors grow wary about the US inability to borrow enough money to finance this debt, it could result in a financial panic that would lead to soaring interest rates, a collapse in the dollar and a deep recession or depression."

While a major outflow has yet to take place, signs of pressure on the dollar can be seen in the fact that it has lost 16 percent of its value, on a trade-weighted basis, since hitting its peak in February 2002.

Despite the rapid growth in the balance of payments deficit in the latter half of the 1990s, the value of the US dollar was boosted by the inflow of capital from the rest of the world seeking higher profits in the US economy. But those days have gone and there are clear signs that the US has entered a period of stagnation if not a downturn.

Figures from the Federal Reserve Board show that production in factories, mines and utilities fell 0.2 percent last month, with automobile and parts production dropping by 4.7 percent. Industrial production has fallen by 0.6 percent for 2002, after a 3.5 percent decline in 2001. This is the first time since the major recession of 1974-75 that industrial production has fallen in back-to-back years. Over the last three years production has increased by less than 1 percent, the worst result for a comparable period since 1983, when the US was in the midst of its worst recession since the Depression.

The Fed's Beige Book survey reported "subdued growth in economic activity from mid-November through early January, with little change in overall conditions." Some of the 12 regional banks, whose reports comprise the survey, used words such as "sluggish", "soft", "subdued" and even "anaemic" to describe economic conditions in their area.

There is considerable confusion over how the US economy should be characterised. Economic growth rates remain positive but there has been a two-year fall in industrial output as well as a sharp increase in job losses over the past two months. Employment fell by 101,000 in December and 88,000 in November.

The National Bureau of Economic Research (NBER), which determines the duration of business cycles, has refused to declare the recession, which it says began nearly two years ago, has finished. In its monthly economic statement released last week the NBER said it would "determine the date of a trough in activity when it concludes that a hypothetical subsequent downturn would be a separate recession, not a continuation."

In other words, the NBER, which places considerable emphasis on employment numbers in determining the turning points in the business cycle, is not sure whether the US economy is still in the recession that began in March 2001, or whether it has recovered from that recession only to enter a “double dip”.

Whatever the official terminology, there is no mistaking the direction in which the US economy is heading. Over the past two years, consumer spending, fuelled by low interest rates and increases in personal debt, has been the main factor in sustaining economic growth. But there are signs this process is coming to an end.

The widely followed University of Michigan index on consumer sentiment fell to 83.7 in January from 86.7 in December, instead of rising to 87 as forecast. The fall in the index, which was bigger than the most pessimistic prediction of any economist, has been attributed to fears over the direction of the economy, the impact of a war against Iraq and concerns over rising unemployment.

Those concerns are certain to increase in the coming weeks. A survey published last week by the National Association for Business Economics reported that US firms were reluctant to increase hiring and capital spending in the face of uncertainties over a war against Iraq and weak corporate profits. Responding to the survey, economists predicted that the US economy would grow at an annual rate of between 2 and 3 percent in the first six months of the year—below the level of around 4 percent considered necessary to prevent the jobless level rising.