US economy stalls in fourth quarter

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Figures released by the Commerce Department last week show that US economic growth slowed sharply in the fourth quarter of 2002, putting the world's largest economy on the brink of recession.

The increase in gross domestic product for the three months to December was just 0.7 percent on an annualised basis compared to an annual expansion rate of 4 percent for the third quarter. Overall for the whole of 2002, the US economy grew by 2.4 percent. While this was significantly greater than the growth of just 0.3 percent in 2001, it was well below the level expected during an economic "recovery".

The *Economist* magazine described the figures as a "dismal performance" saying they confirmed the impression from recent surveys and anecdotal evidence that the American economy is "faltering" with rising unemployment, falling consumer confidence and growing economic uncertainty.

According to the Commerce Department: "The major contributors to the slowdown ... were a deceleration in consumer spending and downturns in inventory investment and exports."

The slowdown in consumer spending was particularly significant given that the relatively high levels of domestic consumption have so far staved off a major recession. But that may well be on its way. Consumer spending for the fourth quarter grew by only 1 percent on an annualised basis, compared to 4.2 percent in the previous three months, making it the lowest rate in almost 10 years and the worst fourth quarter result since 1991.

The fall-off in demand was concentrated in the durable goods sector. Spending on these so-called big ticket items, such as cars and appliances, which jumped by 22.8 percent on an annualised basis in the third quarter, fell at an annual rate of 7.3 percent in the fourth—a clear indication that the process by which consumption has been boosted by low-interest rate financing is coming to an end.

Another significant result was on the balance of trade. For the first time the US trade deficit rose above an annualised rate of $500 billion in real terms, equivalent to a record 4.3 percent of GDP. This means that the US is becoming even more dependent on capital inflows from the rest of the world to finance its widening balance of payments deficit and growing external debt.

While the early reports for this year point to increases in spending, there is no suggestion that the economy will grow by anything like the 4 percent rate needed to stop unemployment from rising.

The worsening employment situation is not just a result of the latest downturn but reflects long-term trends within the US economy. As an article by David Friedman in the January-February issue of the *Atlantic Monthly* pointed out, while the latter years of the 1990s were hailed as a "boom", the US economy in the period 1993-2002 "created barely more jobs than in the previous 10 years, when the working-age population was smaller." Furthermore since 1998, the manufacturing sector has cut 11 percent of its jobs, "the second worst rate of job loss in the past 50 years."

With little or no growth in Japan and the European economy being held back by near-recession conditions in Germany, the low US growth figures have underscored the recessionary trends in the world economy as a whole. These trends are reflected in both the financial markets and the broader economy.

Last week, for example, the UK stock market passed a significant milestone. The FTSE 100 index fell to 3,460.3, less than 50 percent of its closing peak recorded on December 31, 1999. If the share market slide continues it could set off a major financial crisis, as insurance companies write off billions of dollars in share investments. The *Guardian* reported last Tuesday that "reports were rife that insurance companies were selling shares to shore up their shaky financial position” as the FTSE went below the 3,500 mark previously identified as a possible flashpoint.

A vicious circle is in the process of formation. As share prices decline, the position of insurance companies worsens, sending down their shares and further contributing to the overall market decline. The problems are not confined to London but extend across Europe with the CAC in Paris down almost 60 percent from its peak and the Frankfurt DAX down by more than 65 percent. In Tokyo, the Nikkei index is hovering near 20-year lows.

It seems that the similarities with Japan are not confined to the state of financial markets. Like Japan, Germany, which is the powerhouse of the continental European economy, appears to have entered a period of protracted stagnation.

The latest estimate from the government, contained in its annual economic report, is that growth will only reach 1 percent this year, down from a previous estimate of 1.5 percent. This prediction comes on top of figures which show that the economy grew by just 0.2 percent in 2002, following growth of only 0.6 percent in 2001.

Even the estimate of 1 percent growth for this year could be too optimistic, with domestic demand falling sharply. Figures for the retail trade show that turnover in 2002 fell by 3.5 percent on the previous year, the largest decline in post-war history.