Prospects for US recession increase as jobs report shows first decline in four years

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A report released Friday estimates that US employers cut 4,000 jobs in August—the first monthly decline since 2003. The report is the latest indication of an economic slowdown in the US, extending beyond the housing market into the broader economy.

Stock markets fell sharply on Friday, amidst talk of a possible recession in the US and extreme nervousness on Wall Street. The Dow Jones Industrial Average fell 250 points, down 1.87 percent. All but one of the 30 stocks that make up the Dow fell, showing the broad character of the market reaction. At the same time, investor buying pushed up the price of US treasury bonds, considered a safe investment, driving yields down sharply.

European markets also reacted to the US jobs report. Most major European stock indices were down at least 2 percent. European investors and banks have been very nervous in recent weeks about the potential impact of the US housing market problems on European banks and the possibility of a broader economic downturn.

Late in the day, the California-based Countrywide Financial, the biggest US mortgage lender, announced that it would eliminate 12,000 jobs, 20 percent of its total work force, because of the housing market slowdown. The company estimated a 25 percent fall in the number of new mortgages to be issued in 2008.

This huge cutback comes on top of earlier layoffs at Countrywide totaling 1400 workers. The company was forced last month to withdraw its entire $11.5 billion line of credit, and then sold a sizeable stake in the business to BankAmerica to gain an additional $2 billion in cash. The financial markets have been repeatedly swept by rumors that the mortgage lender would file for Chapter 11 bankruptcy.

The national jobs figures were released Friday morning by the Bureau of Labor Statistics, part of the US Labor Department. The decline of 4,000 jobs in total seasonally adjusted nonfarm payroll employment masked a much steeper fall in certain sectors, including manufacturing and construction.

Manufacturing jobs fell for the fourteenth month in a row, and the 46,000 manufacturing jobs lost in August was the largest fall in over four years. The biggest decline was in motor vehicles and parts, in which 11,000 net jobs were cut, reflecting the continued attack on workers in the auto industry.

Construction employment also fell by 22,000, particularly in residential housing. Employment in local government education fell a seasonally adjusted 32,000 in August as a result of budget cuts. Employment rose in health care, leisure and hospitality services, and food services. Financial activities jobs remained flat, although there was a 6,000 net job loss in credit intermediation and related activities.

Friday’s figure was sharply lower than the 112,000 increase expected by economists. The Labor Department also revised downward previous jobs reports from June and July. According to the updated figures, only 69,000 jobs were added in June and 68,000 in July, down from previous estimates of 126,000 and 92,000, respectively. Given the fluctuations in the economy, it is possible that the August estimates will also be revised downward.

The figures give a sense of the increasingly precarious economic situation faced by millions of Americans. US workers are facing the combination of rising mortgage payment and higher prices for consumer goods, stagnating wages, and job cuts. Workers have not benefited from the supposed economic recovery of the past several years, and they will be hit hard by any slowdown or recession.

One of the main causes of nervousness on Wall Street is the concern that consumer spending will begin to fall sharply as a consequence of these developments, increasing the likelihood of a recession.

The unemployment rate reported in a separate survey remained statistically unchanged at 4.6 percent, but this was mainly due to a large drop in the number of people considered to be part of the labor force, particularly among teenage workers. Individuals who have stopped looking for work—including those who have given up on finding a job—are not counted as part of the labor force and therefore are not included in the unemployment rate.

HSBC economist Ian Morris told the *Wall Street Journal* that if the labor force participation rate had not dropped, unemployment would have risen to about 5 percent.

The jobs figures reflect a number of interrelated factors. They show a continued attack on manufacturing jobs in the United States. At the same time, they indicate that problems in the US housing market are beginning to have a broader effect, extending into other sectors. Banks are becoming much more leery of lending money to individuals and businesses, forcing cuts in business investment and hiring.

The *Wall Street Journal* quoted ING Bank economist Rob Carnell, who noted, "For those wishing to see some evidence of the impact of sub-prime [housing mortgages] on the broader macro economy—look no further!" Carnell called the jobs numbers "awful." Comments from financial analysts were generally gloomy to dire on Friday, with most predicting a further deterioration in the economic situation over the coming weeks and months.

Other figures released this week show that pending sales of already-owned US homes fell 12 percent in July, hitting their lowest level since September 2001. The Mortgage Bankers Association reported on Thursday that foreclosures on home mortgages rose to a record of 0.65 percent of loans in the second quarter (April-June), up from 0.58 percent in the first quarter. This figure does not take into account the most recent deterioration of the housing market in July and August.

In other signs of the a continued housing market slump, Beazer Homes USA, the sixth-largest home builder in the country, announced Friday morning that it had received notices that it was in default on its loans because it had not filed its financial reports on time. There has been speculation that Beazer might declare bankruptcy. Meanwhile, Hovnanian Enterprises, which builds luxury homes, reported its fourth consecutive quarterly loss on Thursday.

Developments in the US economy prompted the Organization for Economic Cooperation and Development (OECD)—the Paris-based organization of leading capitalist countries—to issue a warning of a possible recession in the US earlier this week. "Our diagnosis is a slowdown. We cannot rule out a recession," OECD chief economist Jean-Philippe Cotis wrote in a statement released on Wednesday.

In somewhat understated language, Cotis said, "[P]rospects going forward are now clearly less buoyant and more uncertain. Downside risks have become more ominous, in a context where overall financial market conditions are likely to remain durably tighter." Cotis went on to warn, "Recent developments have revealed serious imperfections in the functioning of US housing markets and, more broadly, in credit markets worldwide." He called for the US Federal Reserve Bank to cut interests rates in response.

On Friday, Rodrigo Rato, the managing director of the International Monetary Fund, said the organization would likely revise downward its estimates for global economic growth for 2007 and 2008, mainly because of an expected slowdown in the United States. Rato said that effects might also be felt in Japan and Europe.

William Poole, president of the St. Louis Federal Reserve added on Thursday: "I think the probability of recession is higher than it used to be."

Friday's jobs report, combined with the danger of a recession, has increased pressure on the US Federal Reserve Bank to cut interest rates at its September 18 meeting, if not earlier, in an attempt to boost economic activity. In statements over the past two weeks, Fed Chairman Ben Bernanke has refrained from giving a clear signal that an interest rate cut is imminent.

The jobs figures and the reaction by Wall Street investors could force the Fed's hand. Parallel developments Friday showed the dilemma facing the American ruling elite in working out an economic policy, however. The US dollar fell sharply against European and Asian currencies, on the expectation of an interest rate cut. An interest rate cut would make borrowing easier, but it would also make dollar-denominated assets, including US treasury securities, less valuable.