Government report shows sharp fall in US economic growth

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The US economy grew at a less-than-expected rate of 1.9 percent in the second quarter of this year, according to figures released Thursday by the Commerce Department. The department also announced revisions to its previous growth estimates, concluding that the US economy contracted for the first time since 2001 in the fourth quarter of 2007.

"We're in a recession," Allen Sinai, chief economist at Decision Economics Inc., told Bloomberg News. "It's going to widen, it's going to deepen." The second-quarter growth figures were lower than the 2.3 percent predicted by a Bloomberg survey of economists.

The anemic second-quarter growth estimate is particularly ominous since it covers the period when US taxpayers received hundreds of dollars in rebate checks as a result of a $170 billion stimulus package submitted by the Bush administration and passed by Congress last February. The bounce in consumer spending turned out to be far less than expected, and the impetus to the growth rate for April through June resulting from the rebates will likely be followed by an even deeper slump in the coming months, as consumer spending retreats even further.

Personal consumption, which accounts for two-thirds of total spending, increased by 1.5 percent, slightly higher than the 0.9 percent increase in the first quarter. "The increase in real consumer spending was quite minimal, despite the massive fiscal stimulus," John Lonski, chief economist at Moody's Investor Service, told the *New York Times*. The economy would have contracted by 0.5 percent were it not for a surge in exports, largely the result of the slumping US dollar, which makes US exports relatively cheaper. Exports increased by 9.2 percent, even faster than the 5.1 increase in the first quarter. Imports dropped by 6.6 percent, compared with a 0.8 percent fall in the second quarter. This narrowed the trade deficit to its smallest level in seven years. The growth in exports added some 2.4 percentage points to the growth rate.

The housing sector continued to contract rapidly, with revenues falling by 15.6 percent after a drop of 25 percent in the first quarter.

While the Commerce Department initially estimated the growth rate for the fourth quarter of 2007 at 0.6 percent, in its latest report it revised the estimate downward to minus 0.2 percent, marking the first quarterly contraction of the US economy since 2001. The Commerce Department also announced a small reduction in first quarter 2008 growth estimate, from 1.0 percent to 0.9 percent.

Meanwhile, the financial crisis has only intensified. Merrill Lynch announced Tuesday that it plans to sell $30 billion in mortgage-backed securities at 22 percent of their original value, resulting in a $5.7 billion write-down. The deep discount at which Merrill Lynch was obliged to sell off these assets will place further pressure on the balance sheets of other financial institutions, resulting in tens of billions in additional debt writ-downs and losses.

The sale came only ten days after Merrill reported $9.4 billion in second quarter write-downs and a $4.6 billion loss for the quarter. To compensate for the latest bout of write-offs, the firm has announced an $8.5 billion share offering, bringing the total capital it has been forced to raise to $26 billion.

Deutsche Bank announced a $2.3 billion dollar write-down on Thursday, bringing its total write-downs for this year to over $5 billion. Moody's, the investment rating agency, warned Thursday that the coming months will bring an intensification of write-downs as housing prices continue to fall and the economy deteriorates. Home prices are down by over 15 percent in the past year, according to the S&P/Case-Schiller index. Former Federal Reserve chairman Alan Greenspan said yesterday that the fall in home values was "nowhere near the bottom."

In the same speech, Greenspan noted the precarious position of Fannie Mae and Freddie Mac, the giant mortgage finance companies, saying, "I think the ultimate solution is a nationalization of both Fannie and Freddie."

The Labor Department said Thursday that claims for unemployment insurance jumped by 44,000 to 448,000 this week, the highest level in five years. The department is expected to announce a payroll decline of some 75,000 jobs for July, according to Bloomberg. This would bring total net payroll losses this year to over 500,000.

The number of US workers classified by the government as involuntarily employed part-time has reached 5.3 million, up by one million from a year ago. This figure includes both those who are looking for full-time work but cannot find it and those who have had their hours cut from full-time to part-time. The number of people who have had their hours reduced from full- to part-time at their current job has reached over 3.7 million, the highest figure on record.

"The change in working hours is the canary in the coal mine," Susan J. Lambert, a professor at the University of Chicago, told the *New York Times*. "First you see hours get short, and eventually more people will get laid off." If current layoff rates continue, 2008 will see a net jobs loss of over one million.