THERE IS A CHINK IN THE U.S. ECONOMIC DOOR,
BUT ONLY A CHINK, MIND YOU

It is faint, to be sure, but there is a hint of an indication that things in the US may be turning for the better.

As TARGET pointed out on May 21, 2002, there is a definite correlation between capital expenditure, the capital value of equity markets and consumer spending patterns.

Equities are an alternate source of funding for business, as TARGET pointed out at the time of the May article, but capital spending is reliant on consumer spending, present and prospective.

In the US, as in most Western countries, capital spending by industry is predicated by the demands of consumers who, in turn, make demands upon healthy and vibrant equity markets.

Equity markets, in turn, have to be able to demonstrate to investors that there will be a reasonable return on investments, or give promises of future, acceptable returns on capital expended by investors.

US household net worth, as at today's date, has declined by about $US2.50 trillion from its peak in 2000, first quarter, according to US Government statistics.

Prior to 2001, household net worth had never declined, Year-on-Year, for 2 consecutive quarters, going back to 1953, the US Government points out.

Falling US stock market prices eroded household net worth for a period of 15 months, until, that is, the first quarter of 2002.

As at September 2001, household wealth was put at about $US4.30 trillion, which represented a drop of about 9 percent, Year-on-Year.

In the first quarter of 2002, household wealth gained about 2 percent, compared with the like 2001 quarter.

Rising prices for homes in the US contributed to the gains, of course, as the value of real-estate holdings increased by about 8 percent between January and March, this year.

The erosion in household wealth, during the recession, was centred, to a great extent, in the decline in the values of equities.

It is estimated that one family in 3 families in the US hold – or held – shares in publicly listed companies in the US, but these holdings were centred in what the US Government terms, high-income households whose spending ethic is one that applauds frugality, at least to some extent.

By contrast, it is noted that about 2 families out of every 3 families, on average, own their own homes in the US.

As home prices appreciate, as they have of late, this creates, or has the appearance of creating, wealth.

The appreciation of prices of homes was precipitated by low interest rates by mortgage lenders, spurred by lending institutions, many of which were, and still are, sitting on mountains of cash.

Low interest rates facilitated refinancing and home-equity lending.

Their combined effect was to put cash into many a household's pocket.

In turn, some of this cash started to dribble into stores, throughout the US, as was evidenced by retail sales figures.

The resultant effect of all this is to suggest that things could be on the mend in the US.

The question is, of course: Is it sustainable?

Should the US real-estate *'bubble'* start to deflate, many households in the US could be back to square one.

The US Federal Reserve Board, thus far this year, has not seen fit to increase interest rates because there has been no call for such action.

Later in the year, one does not know, however, whether or not the US Government statistics may indicate a fractional adjustment to the current low interest rates is justified.

Even a quarter of one percent in US Federal Funds – short-term borrowings between banks in the US – could be enough to worry the US real-estate market and could start the ball, rolling down the slippery slope.

Retail Sales

In May, there was an unexpected fall of about 0.90 percent in retail sales in the US, the US Bureau of Census has reported.

The fall was led by sharp declines in sales of motor cars, apparel and departmental stores.

The May figures were in stark contrast to the April figures – and they were quite worrying to a number of statisticians.

The seeming weakness in sales in departmental stores was, probably, consumers, responding to the uncertainty of their salary packages, if, indeed, there is to be the security of work in the future.

US tax cuts boosted disposable income, to some extent, but one-off tax rebates will not last forever.

It is highly unlikely that the Bush Administration will release more money into the economy via tax rebates.

Against the US Government's figures, The Bank of Tokyo-Mitsubishi's Chain Store Index rose by about 0.10 percent in the final week of May.

Autodata Corporation, which plots the sales of motor vehicles in the US, among other things, reported sales of about 15.70 million units for the month of May, a fall of about 10 percent, with the 17.40 million units, sold in the month of April.

Comparing sales of April to May, sales of motor cars declined by about 9.30 percent, sales of lorries fell by about 10.42 percent, while General Motors's motor-car sales fell by about 18 percent.

By and large, Japanese-manufactured motor cars appeared to hold their own, during the 2 months.

Floundering equity markets were, most likely, behind the poor sales of motor vehicles in the US during the month of May.

The US labour market is still moribund so that consumers are not too anxious to take on new financial commitments even with zero-percent financing arrangements, offered by many motor-car manufacturers/dealers.

In the month of May, employers in the US were reluctant to add more workers on the payrolls in spite of what appeared to be an easing of economic activity.

Mass layoffs (defined as the sacking of 50 or more workers) were not as widespread in the month of May as had been expected.

In the month of June, however, mass sackings of staff have picked up, considerably, as more and more companies have to downsize, or suffer the consequences.

It is clear from the reports of Apple Computer and other manufacturers of personal computers and chips, such as Advanced Micro Devices (AMD), to name but one such company, that consumer spending on electronics continues to fall.

AMD announced, just last Tuesday in New York, that it expected a dramatic cut in earnings and a *'substantial loss'* for its latest quarter. (Please see the second story of today's TARGET: Wednesday's stock market report)

AMD, also, said that second quarter revenues would be about 26 percent below previous estimates.

Apple Computer cut its sales forecast for the April-June quarter to between $US1.40 billion and $US1.45 billion, down from earlier estimates of about $US1.60 billion.

Management of Apple said that sales had been disappointing and that sales efforts in Europe and Japan had seen *'particularly weak'* results.

There is a great deal of evidence to suggest that those workers, who were laid off, some months ago, are having trouble, securing alternative employment.

The median duration of unemployment of workers in the US has, now, been extended from 8.90 weeks to 9.80 weeks.

Unemployment may well rise again in the near future, by all accounts.

Conclusion: The picture is becoming less foggy in the US, now, but it is only the merest hint of an improvement in confidence in the world's largest single economy.

The *'wild card'* still remains the Middle East and terrorism, both of which the world will have to learn to grin and bear.

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