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PART I

THE U.S. ECONOMY: WHERE IT IS HEADED
Keep Your Eye On The Ball

The first thing that a tennis coach teaches his pupil is: Keep your eye on the ball!

While this is an excellent axiom for a student of the sport of tennis, it is, also, an appropriate maxim for students of economics, observers of a country's economy, or even investors, looking for an appropriate place to park some money.

The September 11, 2001, attacks by Arab madmen on the US, and the subsequent threats by the US President, Mr George W. Bush, to root out terrorism, where-ever it may be, and, more recently, to attack Iraq, pre-emptively, and to rid that Regime of its President, Mr Saddam Hussein, as well as disarming the country of its weapons of mass destruction, have tended to cause many people to take their eyes off the very poor state of the US economy.

Prior to September 11, 2001, the state of the US economy was, just about, the only subject that one heard on Wall Street and, with the slightest suggestion of seemingly good, or seemingly poor, results of this company or that enterprise, key indices on The New York Stock Exchange or on the NASDAQ would move, sometimes most violently, one way or the other.

Of late, however, the war news has tended to overshadow all else.

And, rightly so, too, because, when the US – or the United Nations Coalition Forces, led by the US military might – does launch an attack on Iraq, and it appears that it must come in the fullness of time, the drain on the US economy will be enormous, regardless of platitudes to the contrary.

The cascading effects of such an international event will be widely felt in just about every economy of the world.

Over the past few weeks, statistics have been spewing out of various US Government agencies, statistics, which, to a very great extent, have been largely overlooked except, perhaps, by a few of the more perspicacious individuals, banks and research establishments, private and governmental.

Chain-store sales in the US for the month of September were dismal.

Retail sales, generally, slumped in the US, during the month of September.

Motor-vehicle sales collapsed in the US, during the month of September.

The Index of the Mortgage Bankers Association of America set new records for the week, ended October 4.

Chain-Store Sales

Mitsubishi Bank-Schroder Wertheim tracks spending at major chain stores in the US in the category of general merchandise, apparel and furniture.

It produces, what is known as, the Mitsubishi Index of Chain Stores.

This Index is one of the oldest of its kind to plot the course of consumer spending in such stores, the stores, having had a history of at least one year.

For the month of September, the Mitsubishi Index registered a plus value of 1.50 percent.

That means, after factoring in seasonal adjustments, consumer spending at major US chain stores rose by 1.50 percent in the month of September, Year-on-Year.

However, this 1.50-percent-plus value was the lowest increase in the previous 12 months, going back to September 2001.

The following table illustrates the obvious weakness in chain-store sales, running back to February, this year:

	September	August	July	June	May	April	March	February
Mitsubishi Index of Chain Store Sales	1.50%	1.80%	2.60%	5.10%	3.50%	1.60%	6.40%	6.20%

While one could say that the 1.50-percent increase was, still, an improvement, compared with the figures for September 2001, one could, also, argue, quite successfully, too, that it indicates waning consumer confidence, with household purse strings, drawn rather tightly.

In September 2001, one must remember, it was just after the attacks on Manhattan and Washington, D.C. by the Arab gunmen, attacks, organised by Osama bin Laden, the most-wanted man on the planet (if he is still alive).

In respect of the September 2001 figures for chain-store sales in the US, therefore, one must take into account the September 11 incident.

In fact, one may not be incorrect to discount those statistics, perhaps, even disregard them, completely, in view of what transpired on that fateful day in September 2001.

The decline in stock and share prices on equity markets in the US, during the months of July and August, must have played a part in the decline in consumer spending in the month of September, the wealth effect of lower stock and share prices and the prospects for even lower levels, having knocked the wind out of many an investor's sails (or sales).

In very simple terms, Mr and Mrs US Consumer were not, and still are not, motivated to go to the shops in order to buy, unless there is an urgent requirement for something.

Less disposable income in US households translates into the forced reining in of spending habits.

Further, job security – and the lack of it, of course – must be playing a large part in the equation with regard to the purchasing power of Mr and Mrs US Consumer because, from day to day, many a US family is not certain that there will be a pay cheque in the coming months.

(Lucent Technology Incorporated, just last week, made a shock announcement that it would be sacking another 10,000 of its workers)

The growth of wages for those people with steady jobs is no great shakes; debt levels must be climbing at households of Mr and Mrs US Consumer; and, prospects are far from being colourful for most people in the US, today.

It would appear, considering all the factors at hand, consumer spending will continue to wane – even though the Christmas season is approaching.

Retail Sales

The Bureau of Census – a department of the US Government – produces, what is known as, The Monthly Advance Retail Sales Survey.

This is a survey, which takes into account merchandise that is sold by establishments, primarily engaged in the retail trade, either for cash or credit, retail or wholesale.

For the month of September, retail sales and food services, on a national basis, fell by about 1.20 percent, compared with the month of August.

If one subtracts sales of motor vehicles – which were dramatically down in the month of September and will be covered, later on in this analysis – then, the figure for sales in the month of September was 0.10 percent, which is down from the month of August, which registered a plus 0.30 percent.

The following table tells the tale:

	National Retail Sales, Month-on-Month, Seasonally Adjusted							
	September	August	July	June	May	April	March	February
Retail Sales and Food Services	(1.20%)*	0.60%	1.20%	1.40%	(1.0%)	1.20%	(0.10%)	0.50%

*( ) negative values

While one could look at the annual statistics and state that the September statistics for retail sales and food services were plus 5.80 percent, which was a record increase for the year, one must bear in mind that this statistic is inflated, due to the events that took place on September 11, 2001.

The following table shows the growth of retail sales and food services, on an annual basis:

	National Retail Sales, Year-on-Year, Seasonally Adjusted							
	September	August	July	June	May	April	March	February
Retail Sales and Food Services	5.80%	5.20%	4.90%	3.80%	2.10%	3.90%	3.70%	3.20%

Again, what the above statistics must indicate is that Mr and Mrs US Consumer are not motivated to drive down to the local shop and to spend some money.

For families, who put their retirement funds into equities, they must be staring at a very dismal and painful situation, especially if they were caught in some of the hanky-panky companies, presently under investigation by the US Authorities, or in those companies that have gone belly up, for one reason or another.

Business activity in the US is constrained, due to a number of factors, and Mr and Mrs US Consumer are well aware of this situation.

The outlook for consumer spending, as with the outlook for sales at chain stores, would appear to be dismal in the coming months, in spite of the Christmas season, fast approaching.

Motor Vehicle Sales

Total vehicle sales in the US for the month of September were about 16.30 million units, according to statistics, gathered from the Big Three motor-car manufacturers – General Motors, Ford, and Daimler-Chrysler.

The sales for the month of September were off by about 2.40 million units, compared with the month of August.

And the lower sales were in spite of the Big Three, offering zero-percent financing packages, while Japanese motor-car dealers were offering historically (in many cases) low financing packages with cash-back payments (in many cases).

Even the mighty Japanese imported vehicles are taking it on the nose, now.

The following table tells the tale, very clearly:

	Vehicle Sales in the US in Millions of Units, Seasonally Adjusted							
	September	August	July	June	May	April	March	February
Total Vehicle Sales	16.30	18.70	18.10	16.40	15.70	17.30	16.70	16.60
Motor Cars	7.90	8.70	8.80	7.90	7.80	8.50	8.20	7.90
Light Lorries	8.40	10.00	9.40	8.40	7.90	8.90	8.50	8.70
General Motors Vehicle Sales	4.10	5.50	5.60	4.80	4.10	5.00	4.60	5.10
Ford Vehicle Sales	3.70	4.00	3.70	3.50	3.40	3.60	3.50	3.30
Daimler-Chrysler Vehicle Sales	2.20	2.40	2.20	2.10	2.30	2.40	2.40	2.20
Honda Vehicle Sales	1.30	1.50	1.30	1.20	1.10	1.20	1.20	1.10
Toyota Vehicle Sales	1.60	2.00	1.80	1.70	1.80	1.80	1.70	1.60
Nissan Vehicle Sales	0.70	0.80	0.70	0.70	0.70	0.70	0.80	0.70

It is obvious that the motor-vehicle sales of the summer months were unsustainable.

Many US consumers, seeing the advertisements, put out by the Big Three in respect of the seemingly enticing financing packages, could not pass up the deals.

Some of those deals, being offered, included no down payments and no payments for the succeeding 90 days.

But, it has all become rather stale bread, now, due to a deteriorating situation with regard to the overall economy of the US and the uncertainty of the next pay cheque.

Mr and Mrs US Consumer, faced with their meagre assets, being depleted by bearish equity markets, and with debts, continuing to climb, about the last thing that they want is to incur further debt by purchasing a new motor vehicle.

They will, in most cases, make do with the old family jalopy, until the economic dust settles, at least.

Alternatively, if the family jalopy has to be scrapped, Mr and Mrs US Consumer will, most likely, opt for a second-hand vehicle, which is much more affordable in the present economic climate.

Mortgage Application Survey

The Mortgage Bankers Association of America (MBA) produces a survey, known as the MBA Index.

The latest update of this Index would appear to indicate that the refinancing market is booming.

It is obvious as to the reasons for these phenomena.

Record-low mortgage rates – and they continued to plumb for new lows – have spurred refinancing by Mr and Mrs US Consumer to new record levels.

The following are the findings of the MBA, which are said to cover about 40 percent of the residential market of the US:

	MBA Mortgage Applications Survey							
	4/10	27/9	20/9	13/9	6/9	30/8	23/8	16/8
Composite Index	1,317.00	1,285.40	1,183.80	1,130.10	1,238.20	1,059.50	1,079.70	1,127.40
Weekly Change	2.50%	8.60%	4.80%	(8.70%)	16.90%	(1.90%)	(4.20%)	11.40%
Refinancing Index	6,926.90	6,671.40	5,977.20	5,625.00	6,104.30	5,129.60	5,355.40	5,523.60
Weekly Change	3.80%	11.60%	6.30%	(7.90%)	19.00%	(4.20%)	(3.00%)	14.00%

A very positive aspect of the above is that it could, well, translate into Mr and Mrs US Consumer, having a little more disposable income at hand due to the lower recurring costs of keeping the family home.

Whether or not they choose to spend this money, however, remains to be seen.

It is more likely that the savings on the annual cost of keeping the family home – debt service and repayment of part of the principal – thanks to lower financing costs, will be used to pay the butcher, the baker, the candlestick maker.

Conclusion: When the US/UN launches an invasion into Iraq, all bets are off.

Then, who knows what is likely to happen since one has no idea how the Arab world will react to an armed incursion into this rogue, Middle-Eastern state.

Which Muslim country, if any, will side with Iraq?

Will another Jihad be demanded by some, or all, fanatic Muslims?

Will there be another attack on the US homeland by Muslim terrorists?

Further, who can say what action, if any, President Saddam Hussein will take against the US/UN troops on Iraqi soil, and, of course, against Israel: The deployment of chemical weapons; the deployment of biological weapons; the deployment of nuclear weapon?

Further, Iraq has been selling between 500,000 barrels of oil and one million barrels of oil to the US, on a daily basis.

That amount of oil represents between 2 percent and 3 percent of the daily oil consumption in the US.

There can be no doubt that, when Iraq is invaded, this supply of oil will be stopped and, while, in the short term, it is unlikely to mean very much at the pumps on Main Street, USA, long term, it will have a very telling effect.

Of course, who knows just how long the war will last.

More to the point, however, it is likely that some of the oil-producing countries in the Middle East will be persuaded to stop selling oil to the US in the belief that the US invasion was based on that powerhouse country's perceived requirements to dominate Iraq, whose known oil reserves represent about 10 percent of the known reserves of oil in the world, today.

Securing a foothold in Iraq would be securing a stable supply of oil for the US, it could be argued by those, who are opposed to the invasion of Iraq.

This argument has, in fact, already been mooted.

Uncertainty is the one single factor that has the ability to cause stagnation in the minds of consumers: They are unable to make a determination and, as a direct consequence, they do nothing.

Consumer confidence in the US is, now, said to be at a decade low.

There would appear to be good reason for this: It may well be justified, too.

The war is likely to cause the focus of attention to be shifted to patriotic considerations, as was the case, following the attacks of September 11, 2001, but TARGET would, humbly, suggest that one should keep one's eye on the ball and its direction.

Part II of this series will be published next Wednesday

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