U.S. STORM CLOUDS HAVE GATHERED: THEY WILL NOT GO AWAY IN A HURRY

Storm clouds are definitely gathering and heavy rain is almost a certainty.

The question is, of course, whether or not these economic storm clouds, forming over the entire United States of America, will graduate to become a storm with hurricane-force winds that could blow away part of the existing economy.

The risk of a recession in The Land of The Free and The Home of The Brave is about one chance in 5, today.

That risk is growing, monthly, however.

That being said, it seems unlikely that The Federal Reserve will increase interest rates at its Open Market Committee Meeting, scheduled for this Tuesday and Wednesday.

Higher interest rates in the US would put an added burden on home-owners, mortgage lenders and retail banks, and the domino effect could just tip the balance so that one may see the first quarter of negative growth in the US economy before the end of September.

With 2 consecutive quarters of negative growth and, Bob's yer Uncle: Economic recession is upon us, by definition.

TARGET () does not want to be taken to task and realises that various economists define a recession in an economy somewhat differently. Generally, recession, which is a fall-off in activity in an economy, is said to have occurred when there has been a significant decline in output and employment. The definition of what constitutes a *'significant decline'*, in this context, is essentially arbitrary. Some economists define it in terms of duration – 2 consecutive quarters in the fall of the **G**ross **N**ational **P**roduct (GNP) while others define it as being 3 consecutive quarters in the fall in the GNP. There is, also, the belief that an economic recession takes into account the depth of the decline of an economy, i.e. by how much output (or employment) has fallen.

The US housing bubble is about to go Pop! and, with it, certain companies, undoubtedly, will fail, especially those companies in the US, which agreed to lend money to people or corporate entities, who/which were then, and must be considered, definitely, today, high-risk borrowers.

The buzz-word, today, for this kind of aggressive lending organisation is subprime mortgage lenders.

It is estimated that subprime delinquency levels are running at about 25 percent, these days.

At least, 5 percent of all subprime borrowers are in default, according to the latest statistics.

The chances are high that a large proportion of this 5 percent of subprime borrowers will lose their homes, their savings … and who knows what else.

The amount of money that has been lent by subprime mortgage lenders is estimated to be at least $US1,500 million.

One does not have to be a mental giant to realise that, in the event that a large segment of this money cannot be repaid, then, it will have a dramatic effect on many areas of the US economy.

Retailers will feel the pinch – in fact, they are, already, feeling the pinch – motor-vehicle producers will see motor-car lots, full of vehicles, with very few takers, building companies will have to close down, as will a variety of lending organisations, and suppliers of goods to the US building industry will be stuck with large stocks of inventory, from plywood to tools of the trade to toilet bowls.

This will lead to higher unemployment.

All this, and more, does not bode well for the largest and most-important economy of the world.

Chain-Store Sales

One can always generalise about nearly anything – the bottle is not half empty, it is half full – but the facts tend, in the final analysis, to speak for themselves.

In the case of chain-store sales for the month of February, The International Council of Shopping Centres (of the US), a well-respected organisation, used widely as a gauge of spending in major, US chain stores, reported some rather dramatic falls of late.

The following table tells the tale:

Chain-Store Sales (Year-On-Year Percentage Change)

Category	February 2007	January 2007
Apparel Stores	-0.80 percent	3.40 percent
Departmental Stores	2.10 percent	6.70 percent
Drug Stores	6.60 percent	8.80 percent
Discount Stores	1.50 percent	2.60 percent
Furniture Stores	-10.20 percent	-10.20 percent
Wholesale Clubs	2.90 percent	2.60 percent

What is clear is that the February growth of sales at chain stores in the US was the slowest since November of 2006.

Further, last November's sales' growth was the slowest growth since March 2006.

For furniture stores – which are suffering, badly, from the US housing slump – logged in the fifth consecutive, double-digit decline in sales' growth.

For apparel stores, declines in sales' growth were dramatic and, compared with October 2006, there has only been positive growth in 2 months – November 2006 and January 2007.

The following graph pictorially depicts the situation in the US with regard to chain-store sales over the past 12-month period:

The disappointing performances of US retailers for the month of February 2007 has been ascribed to inclement weather, across the US, the high price of petrol, slower growth in employment, and, of course, the doldrums in the US housing market.

To the above list of alleged reasons, **TARGET** wonders whether or not a tightening of credit in the US had a telling effect, also.

It is a given that many, if not most, banks in the US, today, are not keen to issue new credit cards to prospective customers, let alone approve new credit cards for existing customers.

Home-owners, those whose credit must, now, be totally shot due to an inability to service debt and/or repay capital, must have been forced to rein in spending, quite considerably, and the use of plastic money is no longer an option, open to them.

TARGET strongly suspects that, in the months to come, there will be more retrenchment in sales at the retail level in the US.

This will, in time, rebound around the world, and Asia, which has come to be known as the world's tailor shop, will feel the pinch, too.

Motor-Vehicle Sales

DaimlerChrysler A.G. wants, desperately, to find a buyer for its US Chrysler marque.

The fact is that Chrysler can't make a profit and its losses are a drain on its German owners.

Aside from the well-known fact that the US cannot compete with its European and Asian counterparts, by and large, when it comes to producing functional and long-lasting motor vehicles – Detroit, having lost its international dominance for all times – consumers in the US are not inclined to maintain past habits of trading in their motor vehicles, annually, or even every couple of years.

For the most part, US consumers are trying to keep the family car, running as long as it is possible in order to economise.

AutoData Corporation, which tracks sales of motor vehicles in the US, brought out the following data which is self-explanatory:

Vehicle Sales (Millions, Seasonally Adjusted Annualised Rate)

Category	**February 2007**	**January 2007**	**December 2006**	**November 2006**	**October 2006**
Total Vehicle Sales	16.60	16.70	16.70	16.00	16.20
Automobiles	7.40	7.70	8.10	7.40	7.30
Light Trucks	9.20	9.00	8.60	8.70	8.80

General Motors Vehicle Sales	4.00	3.80	3.90	3.90	3.90
Ford Vehicle Sales	2.70	2.50	2.60	2.30	2.70
DaimlerChrysler Vehicle Sales	2.30	2.40	2.20	2.20	2.10
Honda Vehicle Sales	1.50	1.50	1.50	1.40	1.50
Toyota Vehicle Sales	2.50	2.70	2.70	2.60	2.50
Nissan Vehicle Sales	1.10	1.30	1.10	1.00	1.00

While sales of motor vehicles for the first 2 months of 2007 may be considered surprisingly strong, at first glance, all things considered, it is known from industry sources, who talk quite openly, that things will get tough from hereon in.

Once again, tighter credit in the US will take its toll at the consumer level and, with the prospects for the remainder of the year, not being exactly bullish, except in cases of dire need, a new family motor car is a very low priority purchase for the average family in the scheme of things.

One important factor that many people may not fully appreciate is that AutoData’s statistics are based on the number of motor vehicles that are known to have been sold; and, sales of motor vehicles may have little correlation to the dollar value of those sales.

In other words, if motor-vehicle producers/retailers in the US offer sizeable discounts to prospective customers, those companies may be able to move stocks, but those sales could well be consummated at cost – or even below cost.

Construction Spending

According to the US Government’s Bureau of The Census, construction spending in the US, during the month of January 2007, fell by about 0.80 percent, Month-On-Month.

Year-On-Year, construction spending was off by about 1.20 percent.

The following is lifted from the archives of The Bureau of The Census:

Construction Spending

(In Billions of US Dollars, Seasonally Adjusted Annualised Rate)

	January 2007	December 2006	November 2006	October 2006	September 2006
Total	1,180.20	1,189.30	1,181.60	1,181.40	1,190.70
Percentage Change, Month-On-Month	-0.80	0.60	0.00	-0.80	-0.80
Total Private	894.30	905.10	904.00	908.30	920.10

Percentage Change, Month-On-Month	-1.20	0.10	-0.50	-1.30	-1.00
Private Residential (Percentage Change, Month-On-Month)	-1.80	-1.00	-1.40	-1.50	-1.30
Private Non-Residential (Percentage Change, Month-On-Month)	0.00	2.30	1.40	-1.00	-0.50
Total Public	286.00	284.20	277.60	273.10	270.60
Percentage Change, Month-On-Month	0.60	2.40	1.60	0.90	0.10

The private residential construction market represents about 66 percent of the entire private construction market.

It is indicative of, among other things, business confidence.

The declines in the price of homes, over the past few months (January's fall in sales was about 17 percent, Month-On-Month, in respect of new, single-family homes) suggests that it is highly unlikely that the US economy will recover from this blot this year ... or even for the best part of next year.

The US economy, without question, is faltering and, with State budgets, suggesting deficits, it is highly probable that purse strings will be tightened, very considerably.

In other words, any and all material public spending is quite likely to be curtailed.

Conclusion

TARGET could have dug up a great deal more statistics in order to bolster its suggestion that the US economy could well be headed for a recession before the year is out if things continue along the present path.

Statistics can prove everything or nothing, as any economist will state, because statistics may be used to support or refute any argument, but, disregarding statistics – which are only useful guides, at best – one is told, almost weekly, that this head of this construction/housing company is forecasting a rum 2007-Year and sees little hope for the best part of the 2008-Year.

For home-owners, having trouble, meeting interest payments, they will have to put their homes on the market and, as more second-hand homes are put up for sale, so prices will ease, appreciably.

It is fact that house prices are falling, in some areas of the US, by something in the neighbourhood of 5 percent per month!

Whereas, a few years ago, it was a sellers' market, today, it is a buyer's market.

The wealth effect will be eroded in a hurry and this is quite likely to be felt in the equity markets, at the High Street, and so on down the line.

At the end of the day, the entire US economy will be affected by the current situation in the housing market ... unless there is a sudden turnaround (which is quite unlikely).

As soon as it is declared that a main-stream mortgage lender is facing insolvency – or has been in that unhappy position for some time – it will result in actions, being taken by various private (and, perhaps, US Government) agencies to try to plug the gap.

While this will, undoubtedly, be a situation of locking the gate after the horse has bolted, nevertheless, it will result in prospective home-owners, finding it increasingly more difficult to raise money to fund the purchase of a new home, while existing home owners, who are having trouble in keeping the creditor wolves away from their doors, will face compound problems, leading, in many cases, to their losing their homes due to foreclosures by mortgage lenders.

Eroded mortgage credit is leading, also, to problems in other parts of the US economy as companies, such as New Century Financial Corporation, which announced last week that it was struggling with extreme, cash-flow problems, tell their tales of woe.

With each announcement, suggesting that this company or that company faces the prospects of insolvency, so the equity markets will be hit, hard.

As share prices retreat, it exacerbates the wealth-effect erosion.

If holders of equities try to put financial fingers in their leaking mortgage dykes by selling publicly listed shares, so key indices of US stock markets will fall to even lower levels.

The situation with regard to the housing problems in the US will not go away in a hurry and one must be prepared for more trouble in the coming months.

The US Commerce Department will be announcing on Tuesday, Washington time, the housing starts and building permits for February.

These statistics will be telling, to be sure.

Whatever they indicate, one must not lose sight of the fact that, since January 2006, housing starts have declined not less than 38 percent.

To state that the situation appears ominous is not worthy of being repeated.

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