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## THE U.S. ECONOMY:
## <u>THERE'S MUCH MORE BAD NEWS COMING</u>

As the Americans are wont to say: *'You ain't seen nothin yet, folks!'*

The problems, lying deep in the core of the US economy, have yet to be fully appreciated, but they will materialise in the months ahead.

Just on Monday, the fourth-largest, US investment bank, Lehman Brothers Holdings Incorporated, announced a $US2.80-billion loss for its second quarter, a large proportion of that loss, being the result of the bank's exposure to residential and commercial mortgage-lending activities.

As everybody is well aware, Lehman Brothers Holdings Incorporated is not the only well-heeled banking entity in the world to get caught with its trousers, around its ankles.

The US, subprime mortgage crisis is but one of the knock-on effects, due to a number of factors that has plunged the US economy into its present crisis mode.

The housing market of the US lies at the root, however: It is the hobgoblin, to be sure.

And, there is no end in sight for a recovery in this sector of the largest and most-important economy of the world, today.

According to the latest statistics, the amount of negative equity in the US housing market, across the entire country, is still being calculated.

Nobody has yet to come up with a figure that could be considered close to the mark.

It is that large.

House prices are continuing to fall across the US and, in the fourth quarter of 2007, it is now history that house prices fell at the sharpest pace of the previous 32 years.

The depth of the falls in the prices of homes is considered frightening by most banks and finance companies, the managements of which know fully well that more provisions for bad and doubtful debts are going to be required before this year is out – at least.

There is, as yet, no hint of a bottoming out in the US housing market and, if anything, it looks as though the situation is being exacerbated as tens of thousands of US home-owners are just walking away from their commitments.

Because they are unable to find the wherewithal to meet the demands of banks and finance houses in order to service debt let alone whittle down the original loans, used to purchase their homes.

Further, because of the negative equity in their homes, they cannot refinance them.

It is being estimated that at least one percent of all homes in the US are about to be forced into the foreclosure process.

Foreclosures and late payments are running at record-breaking levels, according to The (US) Mortgage Bankers Association.

Ergo: Home-owners are walking away from their homes, leaving them to the entities that arranged the finances in the first instance.

The credit market, as a result of this and an assortment of other problems, continues to be in turmoil.

US consumer confidence is in tatters.

Demand for new residential dwellings is soft and will continue to be soft for some time to come.

The actions of the US Federal Reserve to try to put a financial finger in the leaking dyke in an attempt to stabilise the financial markets is just not working.

Further, such actions are not helping to give a boost to the weak housing market in the country.

At the same time, more and more inventories are being dumped onto the housing market as banks and finance houses try to salvage something from the mess.

But, as the banks and finance houses put their inventories on the market, it depresses house prices even further, thus exacerbating the already difficult situation.

The prices of homes, therefore, are highly unlikely to recover before the middle of 2009, at the earliest, according to the latest statistics.

**The Construction Industry**

In the US construction industry, the situation is, also, dangerously close to crisis proportions.

Year-On-Year, construction spending in April was off about 3.90 percent.

In private residential construction, spending decreased by about 2.30 percent in April, a figure which equates to a fall, Year-On-Year, of about 21 percent.

As for private, non-residential construction spending, it was down in April by about 1.60 percent, which was about 15.40 percent higher than April of 2007.

Clearly, the residential side of the equation is responsible for the continued slide in construction spending in the US.

In this industry, also, there is no light at the end of the tunnel, to be trite.

As the inventory of homes remains high, and continues to go higher, prospective home buyers sit on the sidelines, waiting for the dust to settle.

In short, falling home prices are undercutting any incentive to commission new construction.

In such a scenario, it is hardly surprising to learn that motor-vehicle manufacturers in the US are in trouble as a direct result.

As petrol prices continue to rise, US consumers think twice before considering the purchase of a new motor vehicle.

According to AutoData, there has been a steady decline in the number of motor-vehicles, purchased in the US over the past 10 months.

In October 2007, total vehicle sales numbered about 16.10 million units on a seasonally adjusted, annualised basis.

As at May 2008, vehicle sales were down to about 14.30 million units.

These sales are not limited to motor vehicles, produced in the US by Detroit, but even the might of the Japanese motor vehicles are feeling the heat.

Japanese motor-vehicle sales – Toyota, Honda and Nissan – totalled about 5.30 million units, as at May 2008.

As at October 2007, the number of Japanese motor vehicles, sold in the US, numbered about 5.20 million units.

General Motors appears to have been the hardest hit, during this period, with a fall of about 30 percent for the 8 months, ended May 2008.

The (US) Bureau of Economic Analysis has determined that the situation in the US motor-vehicle industry is the worst of the past decade.

The Bureau has determined a number of factors, which include:

1. Motor-vehicle purchases cannot be financed, in part or in whole, using equity in homes as collateral, for the most part;

2. Motor-vehicle dealers, in any event, are no longer accepting homes are partial collateral for the purchase of new motor vehicles;

3. Banks and finance companies are loathe to enter into subprime mortgage loans;

4. Because the US labour market is very shaky and because US consumers are uncertain as to the direction of the economy and, hence, their ability to retain their present employment positions, there is an abject loss of consumer confidence. Thus, new motor-vehicle purchases are very low on the totem pole for households;

5. With the weak labour market in the US, it is putting pressure on any increases in wages and salaries and, due in part to the high cost of fossil fuels and foodstuffs, it is eroding real incomes; and,

6. More and more consumers, in dire need of transportation, are turning to the second-hand market because of price differentials.

Production at US, motor-vehicle factories is being cut back, resulting in labour being given the old heave-ho.

And so the unemployment rate rises, rapidly.

The unemployment figure of 5.50 percent may well just be the baseline, rather than the zenith.

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