THE SUNDAY TIMES

November 29, 2009

Give thanks for the confidence of US consumers

Irwin Stelzer: American Account

On Friday, an estimated 134m bargain-hunting Americans descended on malls and shops on the second-biggest shopping day of the year (the Saturday before Christmas ranks first). Given the increase in the number of stores that for the first time opened for business on Thursday, Thanksgiving Day, the rise of internet shopping, and the increased use of gift cards that are not included in sales figures until actually used, it will be a while before we know whether consumers — 90% of whom do have jobs — have decided to loosen the purse strings.

The early signs are promising. The crowds are clearly larger than they were last year. As Terry Lundgren, chief executive of Macy's, put it: "Last year we were falling off a cliff, grabbing for branches on the way down." No longer. My guess is that traditionally pessimistic retailers will find reason to cheer when the final results of the shopping season are tallied. Consumers are showing signs of starting to spend, and lower inventories will limit profit-busting discounting, despite the extension of the price war between Amazon and Wal-Mart from DVDs and books to appliances.

Brian Dunn, chief executive of the appliance seller Best Buy, said he is offering great prices but has avoided "irrational pricing". Millard Drexler, boss of fashion retailer J Crew, told the press: "Our mission, and our dream, is no promotions." He can dream, but for now he will have to settle for doubling his profits in the third quarter. **Dana Telsey of the eponymous consulting group concluded: "This year will be a profitable Christmas rather than a markdown Christmas."**

Tomorrow it is back to work and to contemplation of the future. Americans are increasingly aware that it is going to be a long road to prosperity and full employment. The Federal Reserve Board is guessing that we will not recover lost ground for five or six years. And Americans are acutely aware that the policies adopted to prevent a more serious downturn have left a mountain of public debt, mortgaging the future of our children and grandchildren.

There are other reasons to worry:

-One in four American households (10.7m) owe more on their mortgages than their houses are now worth.

-Credit remains tight — lending by American banks to homebuyers and businesses dropped 2.8% in the last quarter, the fifth consecutive quarter in which the banks have tightened up, and the largest drop since records were first kept in 1984. Big banks that have been bailed out by the taxpayer led the tightening.

-Unemployment is in double digits, and the Fed is expecting it will decline only to somewhere between 9.3% and 9.7% next year. Worse still, 20% of those out of work have been unemployed for a year or more, compared with only 10% when the downturn started in 2007.

-552 financial institutions, roughly 7% of all US banks, are likely to fail. These are mostly small regional banks, over-exposed to the commercial property market.

-The fiscal deficit is ballooning to between 12.5% and 15% of GDP, and the Fed is printing money with which to buy all the IOUs the government is issuing. As a result, the dollar seems to be in free-fall, or at least was until the financial difficulties of Dubai World caused a flight to safety — the dollar. Worse still, the president and Congress want to spend even more on healthcare, energy and a second stimulus.

Still, Americans are natural optimists: where foreign businessmen talk of "problems", their American counterparts, surveying the same economic landscape, speak of "challenges". And we know we have much to be thankful for. Not only the traditional blessings of the rule of law and freedom. Or the mixed blessing of families united by the return to the nest of unemployed sons and daughters, no longer able to pay their own way (the teen unemployment rate is approaching 28%). Or steady increases in longevity as more diseases are conquered by the healthcare system our president is convinced is in need of radical reform.

In three unrelated events this week my wife and I met a 90-year-old publisher, a 90-year-old social scientist and a 90-year-old historian — all active, all sharp. Ninety is the new 60.

Share prices are up and — more important to more people — the housing market seems to be stabilising. Most indexes of home prices have either turned up modestly or stabilised this year, and inventories of unsold houses are down. Sales of new and existing homes rose in October, the former by 5.1% over last year, the latter by 23.5% to a level not seen since before the housing market collapsed.

We are in a world in which some see a glass half-full, others one that is half-empty. Economists expect growth of 3.2% in 2010, a big improvement over this year's miserable performance. But it is only about half the rate at which the economy grew when past recessions ended. The Fed and private-sector economists expect the unemployment rate to decline — good news — but remain above 9% — the bad news. Profits are up, and economists predict a further gain of 12.4% next year, but much of the gain comes from cost cutting, which cannot continue for ever, rather than rising sales.

The housing sector is recovering — good news — but here is the inevitable bad news: the rise is due in large part to subsidies to new homebuyers, recently extended but due to expire in May, and low mortgage rates, a function of the fact that the Fed is printing money and the government is buying up some 80% of all mortgages.

Confusing, certainly. Americans are thankful that the financial system has not collapsed, as we feared at this time last year, but remain worried. Warren Buffett puts it this way: "The financial panic is behind us, the economic spill-off is still with us." Now, attention is turning to longer-term reform of the economic system (the good news) by hysterical populist politicians (the bad news) who just might destroy the system in their effort to save it.