THE WALL STREET JOURNAL ONLINE

September 17, 2002

ECONOMY

Household Net Worth Falls 3.4%; Economists Fear Spending Decline

By ANDREW CAFFREY
Staff Reporter of THE WALL STREET JOURNAL

The stock market continues to hammer away at Americans' net worth.

The Federal Reserve Monday reported that household net worth in the second quarter this year plunged $1.425 trillion, or 3.4%, to just under $40.077 trillion from first-quarter figures that were revised upward. The drop reverses a moderate 1% gain reported in the prior quarter.

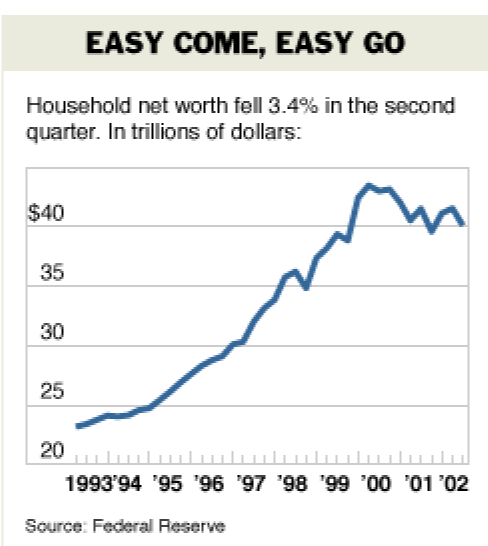
Economists worry that a sustained decline in household net worth could cause consumers to cut back on spending. Household net worth -- a measure of total assets such as homes and retirement funds, minus liabilities such as mortgages and credit-card debt -- had fallen in 2001 and 2000 after hitting a $42.382 trillion peak in 1999 due to the bull market.

• Read the full text[1] of Wednesday's report from the Commerce Department, and analysis[2] from Briefing.com.

Dean Maki, an economist at Putnam Investments in Boston, notes that since the beginning of 2000, declines in the value of stock-market holdings have far outstripped gains in housing values. Moreover, he adds, current consumer spending, while healthy for a soft economy, still is growing at only about half the rate it did it during the late 1990s.

"What that's telling us is the negative wealth effect" from stock-market losses "has been a weight on consumer spending, and will be going forward," Mr. Maki says.

The Fed publication, the quarterly "flow of funds" report, showed that stock-market losses accounted for much of the second-quarter decline in household net worth. The value of corporate equities fell $877 billion, or 15%, from the prior quarter; mutual-fund assets were down nearly $200 billion, or 6.6%; and pension holdings fell $469 billion, or 5.3%. Those losses swamped the $291 billion, or 2.3% gain, in the value of household real estate for the period. The drop in net worth includes a small amount attributable to nonprofit organizations.



Moreover, the Fed said that growth in household debt, driven by mortgages, "remained rapid" in the second quarter at 9%, on a seasonally adjusted annualized basis. Home mortgages increased by $157 billion to $5.663 trillion, while consumer-credit debt, such as credit cards, increased almost $30 billion to $1.706 trillion. Federal government borrowings surged 13% -- the largest such gain in more than a decade -- compared with a 1.2% increase in the first quarter. Debt of state and local governments increased 12% for the second quarter, compared with a 4.5% increase in the first quarter. The burst of debt reflects lower tax collections, among other reasons.

One positive measure in the Fed report is that disposable personal income grew about $119 billion, or 1.55% on an annualized rate, following a sharp drop in the measure in the fourth quarter of 2001. The increase in disposable income "means the household sector can get out of debt, which it's got to," says Jane D'Arista, program director for the Financial Markets Center, which studies monetary and financial policy. Still, Ms. D'Arista says the "big picture isn't good" because households are more dependent on home value staying high to hold up net worth.

Meantime, a separate government report showed consumer spending is nonetheless driving a robust increase

DATA AND RESOURCES

- Economic Indicators
- U.S. Calendar
- International Calendar
- Economic Chartbook
- Reports from Briefing.com

INVENTORIES ON THE RISE

• Businesses Add to Stockpiles, Anticipating Higher Spending[4]
08/15/02

• Businesses Boost Inventories, Ending Long Streak of Cuts[5]
07/15/02

in inventories among retailers and wholesalers, raising hopes that liquidation of stocks that marked much of the recession is over, and a pattern of expanding production at factories may soon follow.

The Commerce Department said stockpiles of goods rose to a seasonally adjusted $1.124 trillion in July, a 0.4% increase from the prior month, marking the third straight month of such inventory rebuilding.

"Businesses have really pared back; they can't afford to run any leaner," says James Glassman, senior U.S. economist for J.P. Morgan Securities. He adds the economy may be "on the edge of a further acceleration of inventory rebuilding which will carry us through the winter." Mr. Glassman says the inventory report is causing him to think that overall economic growth will be higher in both the third and fourth quarters. His current forecast for third-quarter gross domestic product annualized growth is 3.5%, but he believes it now could grow as much as 4%.

But Fred Breimyer, chief economist at State Street Corp., in Boston, says business capital spending remains vulnerable to cutbacks as profits decrease and lenders remain tightfisted about such investments. He predicts economic growth in the fourth quarter and subsequent quarters will be in the 2% to 2.5% range, "nothing impressive."

Write to Andrew Caffrey at andrew.caffrey@wsj.com[3]

URL for this article:
http://online.wsj.com/article/0,,SB1032229127346610315.djm,00.html

Hyperlinks in this Article:
(1) http://online.wsj.com/documents/bbinv-20020916.pdf
(2) http://online.wsj.com/documents/bcom-fuecbusinv.htm
(3) mailto:andrew.caffrey@wsj.com
(4) http://online.wsj.com/article/0,,SB1029327578735109475,00.html
(5) http://online.wsj.com/article/0,,SB1026735727393566080,00.html

Updated September 17, 2002