

January 31, 2003

Slim Growth for Economy in 4th Quarter

By DANIEL ALTMAN

The economy eked out a meager growth rate of 0.7 percent in the fourth quarter of last year, the Commerce Department reported yesterday, as the first positive gain for business investment in two years was not enough to compensate for consumers' dwindling appetite for new cars and trucks.

Emerging from recession last year, the economy posted decent overall growth of 2.8 percent from the end of 2001 through the end of 2002, but it was a year of jagged quarterly performance, capped by a sharp slowdown from the 4 percent rate during the third quarter.

"In the areas where you had a recession, you can't get a recovery given the levels of overcapacity and risk aversion," said Paul A. McCulley, a managing director at the Pacific Investment Management Company who is known for his economic forecasting.

Most economists had predicted a weak figure for the fourth quarter, and none interviewed yesterday said they planned to change their forecasts. Though they expect growth to improve slightly this year, it might not be enough to create jobs until the spring or summer.

Many companies hesitate even to bet on a midyear recovery, said Carl T. Camden, president and chief operating officer of [Kelly Services](#), a leading provider of temporary workers. His clients "talk about things turning around in the third quarter," he said, "and then they realize that's the same speech they gave last year."

The confirmation of dreary suspicions about the fourth quarter could give both political parties ammunition in the coming debate on another fiscal stimulus package. Yet consumers have been less than impressed with the president's proposal, said Richard T. Curtin, director of consumer surveys at the Institute for Social Research at the University of Michigan. "They don't think it will help improve the job outlook."

In the fourth quarter, the resilience of the American consumer suffered a small lapse. The increase in consumer spending, in the midst of heightened uncertainty about a war in Iraq and stubbornly high unemployment, was just 1 percent, adjusted for inflation and seasonal changes, the smallest gain since 1993.

A drop of \$25 billion in auto sales accounted for virtually all of the lull. William T. Wilson, a senior economist at Ernst & Young, said that he expected the slackness in vehicle sales to continue. Special incentives have kept sales above their trend for four years, he said, but the enthusiasm of consumers was bound to wane.

"You have been borrowing from the future for a year or two," Mr. Wilson said. "Even with aggressive discounting, you're still looking at another down year for auto sales."

Mr. McCulley added that consumers had come to expect no-interest financing for cars and trucks regardless of changes in the economy. "The consumer has been trained to pull back until zero is restored," he said. "There's no pricing power in that sector."

The other sector that bolstered the economy last year, housing, stayed strong through the fourth quarter. Investments in residential housing swelled by 6.8 percent. On Tuesday, the Commerce Department reported that sales of new homes rose by 37,000 in December, capping a record year of 976,000 sold.

In addition to spending on new homes, consumers kept buying more goods from abroad. Oil prices also rose in the fourth quarter, and exports from American manufacturers dropped by 1.7 percent. The nation's trade gap ballooned by \$18.9 billion, further dragging down the economy's growth rate.

"The trade picture is certainly a reminder that we're working in a very weak global economic setting," said Robert V. DiClemente, chief United States economist at Salomon Smith Barney. "When the world steps back, it hurts us regardless of whether the dollar is moving up or down, or sideways."

A steep increase in spending by the federal government, which rose 10.1 percent, salvaged the quarter. Most of the surge came from military spending as the nation mobilized for a possible war. Without that spending, the economy would have shrunk by 0.2 percent.

The economy's average growth rate was 2.4 percent in 2002. That pace easily bested the glacial progress of 0.3 percent in 2001 but still fell short of the long-term growth rate, which the government projects at 3 percent.

In yesterday's report, a small sign of strengthening came in the area of corporate investment, excluding changes in inventories. After declining steadily since the fourth quarter of 2000, before the beginning of the recession, investment edged up 1.5 percent. Spending on computers and software jumped for the second consecutive quarter, this time by \$12.1 billion.

Mr. DiClemente has been tracking a jagged upward trend in that category for several months. "That's the one area where we have probably undershot in terms of long-run needs," he said, "and it's not surprising that we're getting this kind of slow, grinding recovery." The retrenchment of corporate investment, in his view, may be nearing its end.

Yet Mr. McCulley, who insisted that the economy still suffered from too much capacity for production, was not impressed by the latest figures. "The dog that won't bark in this recovery has been business investment," he said. "The fourth-quarter data says he still ain't barking."

Inventories rose \$3.3 billion in the fourth quarter, compared with \$18.8 billion last summer, as wholesalers and retailers anticipated a subdued holiday shopping season.

The dip in the growth of consumers' spending echoed a steady decline in measures of their confidence in the economy. That decline continued this month, according to figures that were released Tuesday by the Conference Board, a business research group. Its index of confidence fell from a revised value of 80.7 in December to 79.

The government also released mixed reports on the labor market yesterday. First-time claims for unemployment benefits inched upward last week, the Labor Department reported, to 397,000. The four-week moving average slipped to 384,000, however, its lowest level since November.

Employment costs rose 3.4 percent in 2002, the smallest gain since 1999. Much of the modest inflation came from benefits rather than wages and salaries.