SFGate.com | Print This Article | Back to Article
SFGate.com

Odds Are Growing for Economic Recession

By JEANNINE AVERSA, AP Economics Writer
Sunday, January 13, 2008

(01-13) 08:19 PST WASHINGTON, (AP) --

The unemployment rate leaps to a two-year high, record numbers of people are forced from their homes and Wall Street nose-dives again. Such is the fallout from a housing meltdown that threatens to slingshot the country into a recession.

The big economic question these days is whether the weakening economy will survive the strains or collapse under them.

The odds have grown that the economy will slip into a recession. At the beginning of last year, many economists put that chance at less than 1-in-3; now an increasing number says it has climbed to around 50-50. Goldman Sachs, the biggest investment bank on Wall Street even thinks a recession is inevitable this year.

Hopeful it can be avoided, President Bush and the Democrat-controlled Congress are exploring economic rescue measures, including possible tax rebates. Federal Reserve Chairman Ben Bernanke pledged to lower interest rates as needed.

The idea is to induce people to boost spending, especially on big-ticket items such as homes and cars, and revitalize economic activity.

"The recession gorilla is there. The question is can the Federal Reserve do enough to avert a recession?" asked Brian Bethune, economist at Global Insight. "We think the odds are close to 50 percent that there will be a recession. It is high — no question about it."

Much hope rides on the Fed. By dropping rates, it can act quickly — faster than Congress or the White House could agree on and deliver an economic boost.

"The Federal Reserve is not currently forecasting a recession," Bernanke said last week. "We are forecasting slow growth."

Bernanke signaled that a rate cut would come this month. Many economists believe a key rate, now at 4.25 percent, could fall by as much as one-half of a percentage point. Such a cut would lower the rates that are charged to millions of consumers and businesses for many different types of loans.

Analysts predict the Fed will keep doing that in the months ahead as part of a campaign that started in September, when the central bank cut rates for the first time in four years.

Trying to put the fragile economy back on firm footing is the biggest challenge for Bernanke since taking over the Fed nearly two years ago. His job requires a deft reading of the economy's vital signs and keen insights into what makes people and businesses tick. It is their behavior that shapes the economy. And it is in turbulent times that the Fed chief needs to bolster public and investor confidence.

Still, Wall Street is on edge. The Dow Jones industrials plunged nearly 250 points on Friday. Also, consumer confidence tumbled in early January.

Bill Cheney, chief economist at John Hancock Financial Services, puts the odds of a recession as high as 40 percent. "There are a lot of headwinds and the economy probably has enough momentum to get through, but when things get rough, there are a lot of ways things could go wrong," Cheney said.

The fear is that people will clamp down on the spending and businesses will put a lid on hiring and capital investment, sending the economy into a tailspin.

By one rough rule of thumb, a recession occurs when there are two consecutive quarters — six straight months — when the economy shrinks.

The National Bureau of Economic Research, the recognized arbiters for dating recessions, uses a more complicated formula. It takes into account such things as employment and income growth. By that measure, the last recession was in 2001, starting in March and ending in November.

Tax rebates aimed at stimulating the economy were part of Bush's $1.35 trillion in tax cuts in 2001. They were credited with helping to make the recession short and mild.

The current housing slump, made worse by a credit crunch, is weighing heavily on economic activity.

Upcoming reports are expected to show the economy grew at a feeble pace of just 1.5 percent or less in the final three months of last year and will be weak in the first part of 2008. Consumers, whose spending is indispensable to a healthy economy, are expected to have tightened their belts.

High energy prices, weaker home values that make people feel less wealthy, and a deteriorating jobs market all figure into more caution on the part of consumers.

The unemployment rate jumped to 5 percent in December from 4.7 percent, fanning recession fears. It was the biggest one-month gain since October 2001, during a time of massive layoffs in the travel industry after the Sept. 11 attacks.

Lawrence Summers, one of President Clinton's treasury secretaries, said the odds of a recession this year went up after the dismal employment report. He advocates temporary tax cuts and emergency spending. "It is now conventional opinion and many fear that there will be a serious recession," Summers wrote recently in the Financial Times.

Martin Feldstein, who was President Reagan's top economic adviser, and former Federal Reserve Chairman Alan Greenspan have urged greater government intervention. Greenspan recently said the economy is "getting close to stall speed," and Feldstein has said his best guess is that the economy "has not turned down and it is still expanding, but very weakly."

http://sfgate.com/cgi-bin/article.cgi?f=/n/a/2008/01/13/national/w063050S88.DTL