Flat incomes raise doubts about economic recovery

By MARTIN CRUTSINGER (AP) – August 29 2009

WASHINGTON — Household income in the U.S. is essentially stagnant, raising doubts about whether consumers already hurt by job losses can sustain an economic recovery.

The now-ended Cash for Clunkers program helped lift consumer spending last month and is expected to provide an even bigger boost in August. But any rebound could falter if shoppers don't boost their buying, which makes up about 70 percent of U.S. economic activity.

"Consumers just don't have the financial firepower to go out and spend more," said Mark Zandi, chief economist at Moody's Economy.com. "Unless businesses curtail their job cuts, the recovery could very well peter out."

Stronger consumer spending is the key to a sustained recovery. For spending to rise, analysts said, income growth has to resume.

The Commerce Department reported Friday that personal incomes were flat July, the eighth month out of 10 in which incomes have either fallen or failed to grow. Americans have been hammered by massive layoffs and efforts by some companies to restrain costs by forcing workers to take unpaid days off.

With incomes flat in July as spending rose, the personal savings rate dipped slightly to 4.2 percent from 4.5 percent in June. The savings rate was 2.6 percent a year ago.

Economists expect the savings rate to rise in coming months to around 6 percent as workers try to rebuild depleted nest eggs. The process of rebuilding savings is one of the factors expected to depress consumer spending and weaken the broader recovery.

The 0.2 percent rise in spending last month followed a 0.6 percent jump in June, a gain driven by a surge in gasoline prices. Adjusting for inflation, spending also rose 0.2 percent in July, and 0.1 percent in June.

The slight rise in spending reflected a 1.3 percent jump in purchases of durable goods such as cars, a gain propelled by the clunkers program that started at the end of July. Purchases of nondurable goods such as clothing actually fell 0.3 percent last month.

The unchanged reading for personal incomes followed large swings in the previous two months that reflected payments to individuals from the government's $787 billion economic stimulus program. Those payments pushed incomes up 1.4 percent in May and their absence in June caused incomes to fall 1.1 percent.

Even households with sufficient income to hit the shopping malls have trimmed their purchases and boosted savings to cope with a severe financial crisis which sent the stock market into a nosedive last year.

The Federal Reserve has pushed a key interest rate to a record low near zero in an effort to boost the economy and is pledging to keep rates low for a considerable period even as the economy begins to grow again.

The Fed is able to make that pledge because inflation is not a problem. A price gauge tied to consumer spending was unchanged in July after a 0.5 percent jump in June that had reflected a big rise in energy prices. Excluding food and energy, the price gauge showed a 0.1 percent rise, and over the past year increased 1.4 percent, well within the Fed's comfort zone for inflation.

The government reported Thursday that the overall economy, as measured by the gross domestic product, fell at an annual rate of 1 percent in the April-June quarter. It marked the fourth consecutive decline in GDP, the longest stretch on records that go back more than six decades.

Many economists believe GDP in the current July-September quarter will rebound to growth above 3 percent and remain at that level in the fourth quarter. The economic growth likely will reflect a boost from the highly successful clunkers program to boost car sales and other government stimulus efforts.

But the fear is that economic growth will slip back in the early part of 2010 as the impact of the government programs fade and unemployment rises. The 9.4 percent jobless rate in July is expected to edge up to 9.5 percent in August and keep rising until it tops 10 percent. That will be a tough environment to see strong gains in consumer spending.

Some analysts worry that the country could be headed for a double-dip recession in which the economy resumes growing for a brief period only to fall back into a downturn.

The troubles consumers face have meant tough times for the nation's retailers. A survey of big retail chains showed that shoppers remained tightfisted in July, a development that raised worries about back-to-school sales and the holiday shopping season later this year.

In July, mall-based apparel stores fared the worst with Macy's Inc. and teen retailers Abercrombie & Fitch Co. and Wet Seal Inc. reporting disappointing results.

However, apparel discounters like Ross Stores Inc. and TJX Cos. both reported sales gains that exceeded Wall Street estimates. TJX operates the T.J. Maxx and Marshalls chains.