

# The Washington Times

## Home-price dip casts pall on economy

By Patrice Hill December 28, 2010

The slumping housing market struck a sour note Tuesday, somewhat dampening optimism that the economy is getting a big sugar rush from the best Christmas selling season in three years.

Splurging consumers bent on celebrating the holidays in style so far have been largely undeterred by continuing doubts about the state of the housing and jobs markets, retailers report. Consumer spending is the biggest engine of growth, accounting for about 70 percent of economic activity.

But a report from Standard & Poor's Corp. on Tuesday showed the housing market continues to cast a shadow over the consumer parade. A renewed drop of 1.3 percent in home prices in 20 major U.S. cities in October showed clearly that housing fell into a double-dip recession last fall.

"Consumers are making a comeback, despite a poor housing market and high gasoline prices," said Chris G. Christopher Jr., economist at IHS Global Insight. He said consumers are being motivated by such things as heavy discounting by retailers, a rising stock market, easing of credit conditions, and higher disposable incomes, thanks to the tax cuts and extended unemployment benefits just passed by Congress.

As a result, "the holiday season is looking very bright," he said. IHS estimates that Christmas sales — which continued into this week as consumers flocked to the shopping malls armed with gift cards, plenty of free time and Christmas spirit — will rise a robust 5 percent over last year's depressed levels.

Retailers are reporting the best demand since before the recession began in December 2007. Notably, luxury retailers such as Neiman Marcus, Saks and Nordstrom have seen a surge in traffic and sales as high-income consumers regained confidence and another two years of Bush-era tax cuts.

The party mood is likely to continue into the new year, with sales of bubbly wines and luxury champagnes soaring by 12 percent after being flat during the recession. Purchases by the richest 20 percent of consumers account for nearly 40 percent of total consumer spending, according to the International Council of Shopping Centers.

"People are sick of saving; it's not fun," said Cindy Novotny, a Los Angeles business consultant who bought her daughter a \$630 pair of black leather pumps for Christmas. "In 2009, I shopped in my closet, and I said, 'I'm over that.'"

Mr. Christopher said the consumer revival is a godsend for the many retailers who earn most of their profits and revenues during the Christmas season, and should be good news for other businesses as well because of the important role consumers play in the economy.

"Hopefully, if businesses start seeing consumer spending gaining some momentum, they will start hiring at a faster pace, thus motivating even more consumer spending," he said.

A reminder came out Tuesday, however, that consumers remain well aware and glum about still-gloomy job prospects, rising gas prices and the declining housing market. The Conference Board reported an unexpected dip in its consumer confidence index for December.

Sung Won Sohn, economics professor at California State University at Channel Islands, said the resilience of consumers has surprised everyone recently.

A report on Thursday showed inflation-adjusted growth of 2.4 percent in consumer spending during the summer quarter — the highest annualized rate since before the recession in 2006. And so far in October and November, the first two months of the fall quarter, spending is growing at a torrid 4.2 percent annualized rate, IHS estimates.

But Mr. Sohn is not sure the good times will last, given the big problems still dogging consumers.

"After the holiday shopping season, consumers could retrench again," he said. "After all, the deleveraging process for the consumer has not run its course. American consumers want to save more, pay down the debt and put their financial house in better shape."

Richard Berner, chief U.S. economist at Morgan Stanley, expects consumers to continue to spend more freely, particularly as they will be bolstered next year by the extension of President Bush's tax cuts, extended unemployment benefits, and a powerful new \$114 billion cut in Social Security payroll taxes that will benefit people with more modest incomes.

"Despite stubbornly high levels of unemployment and the still ongoing household deleveraging process, personal consumption has essentially returned to growing at pre-recession rates," and will continue to "play an essential role in driving the unfolding recovery," he said.

Mr. Berner views the renewed decline in housing prices as a potent threat that could disrupt the consumer revival and economic recovery, however. Morgan Stanley and IHS both expect an additional 10 percent drop in home prices before they turn up again.

"Housing imbalances remain the most significant downside risk," Mr. Berner said. "A decline in home prices larger than the 10 percent we expect would disrupt further the supply of credit, menace consumer balance sheets, and thus threaten consumer spending."

**Bernard Baumohl**, chief economist at the Economic Outlook Group, is optimistic that consumers will overcome their debt and housing troubles.

"The economy is ending the year on a very strong note, and I believe this momentum will carry through well into 2011," he said.

"Consumer spending is expected to become a major contributor to growth next year," he said. Despite what people say in response to consumer confidence surveys, the strong uptick in spending recently is betraying increasing confidence about the economic future, he said.

"Americans have become so confident about the economy and their finances, they are setting aside fewer savings," in the most telling sign of the brightening outlook, he said. The personal savings rate has fallen from a high of 8.2 percent in May 2009 to 5.3 percent last month.