

# The New York Times

## U.S. Economy Grew at 2% Rate in Third Quarter

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The United States economy is a bit like a jetliner short on fuel these days, waiting for something to give it the oomph needed for takeoff.

The latest report offers not much by way of immediate relief, as the Commerce Department estimated on Friday that the nation's economy grew at an annual rate of 2 percent in the third quarter. That growth rate, matching the forecast, is the barest tick up from the second quarter.

The weak report comes at a parlous time for President Obama and the Democrats, who are only days away from crucial midterm elections that are widely expected to turn out well for Republican challengers. High unemployment and soaring foreclosure numbers in the Midwest and West already made this a particularly difficult election for Democrats. The nation's tens of millions of unemployed — many now jobless for close to two years — present a political and social challenge. Two percent growth, almost all economists agree, cannot produce nearly the demand needed to reduce the nation's 9.6 percent unemployment rate.

The trade gap remained wide in the latest quarter, as imports again surged and outpaced exports, and that too could portend ill for job creation.

“It's the expected G.D.P. number, which is mostly bad news for the economy,” Josh Bivens, an economist with the Economic Policy Institute, said of the gross domestic product. “The growth rate is just nowhere near enough to put downward pressure on unemployment.”

In the fourth quarter of last year, the picture was far brighter, when growth rose 5 percent as the country emerged from recession. But conditions have weakened considerably. Demand is crucial to re-igniting the economy, and demand remained flaccid in the third quarter, although there were hints of increased consumer spending. Income growth, adjusted for inflation and taxes, slowed, rising at an annualized rate of 0.5 percent in the

third quarter after increasing at a 4.4 percent rate in the second. And at the other end, prices excluding food and energy increased at a rate of 0.6 percent compared with 0.8 percent in the second quarter.

In recent weeks, the economy has presented two faces, which is reflected in the latest G.D.P. numbers. There have been fledgling signs of growth: home sales and chain store sales are up a bit; a swelling equities market has raised consumer confidence a few notches; and jobless claims fell noticeably last week, albeit they are still quite high. At the same time, the steroidal effect of the federal stimulus spending is fading (although more than a trace of that spending is in the growth in large highway and bridge projects found in this quarter's output numbers). City and state governments have shed tens of thousands of employees, and states face a sea of red ink as they look at next year's budgets.

"Two percent growth is not great, but it beats zero," said Steve Blitz, chief economist with ITG investment research. "But the picture of the economy remains troubling. There is certainly no sign that a normal cyclical upturn is taking hold. The consumer is still underemployed and overindebted, so the normal push won't be there."

Economic bulls are more difficult to locate now than in the spring, when the economy appeared to gain traction. But **Bernard Baumohl**, chief economist for the Economic Outlook Group, has lost none of his élan, saying that he spots signs of strength.

"The main message from this report is that the economic recovery is gathering fresh momentum from the sector that matters most to this recovery: consumer spending," he said in an e-mail. "Slowly but surely, worries over job security and future income growth have subsided and households appear to be more at ease about shopping."

Consumer spending, which accounts for roughly 70 percent of economic activity, remains the great unknown. Americans have shed some debt, which is good, but in an unsightly fashion, which is not so good. They have defaulted on credit card debt or have lost their homes to foreclosure in record numbers. Their spending rose this quarter and personal savings was estimated at 5.5 percent of income, compared with 5.9 percent in the second quarter.

But price and income growth remains too weak to banish entirely the fear that deflation might yet take hold.

The Federal Reserve Bank of San Francisco touched on this prospect two weeks ago in a gloomy forecast, noting that no sector of the private economy stands ready to drive a robust recovery. "The economic recovery is proceeding at a very slow pace and has lost momentum since the spring," said Mary C. Daly, vice president of the Federal Reserve Bank of San Francisco. "Japan's experience beginning in the early 1990s underscores the risk of getting into a long period of sustained disinflation."

The midterm elections on Tuesday further complicate the economic picture. After the votes are counted, and certainty edges aside uncertainty, American business may start spending a bit more and banks may start lending to small businesses. But few economists

are willing to turn that wish into a forecast, not the least because political deadlock looms as a possibility.

David Rosenberg, economist for the Canadian investment firm Gluskin Sheff and Associates, does not put a lot of faith in consumers pulling the economy out of its ditch. “Barring divine intervention, it’s not clear how the economy keeps expanding in the coming year,” he said. “You’ll have federal spending declining and more and more folks falling out of emergency unemployment benefits.”

The eyes of some economists and political leaders have turned to overseas economies, in hopes that sturdier boats might come to America’s aid. The Chinese economy has cooled a touch, but its engine remains impressive. And the European economies have shown signs of stabilizing of late, with Germany as a potential driver of growth (its unemployment recently reached an 18-year low). All of this could bode well for America’s export sector.

But the facts in Friday’s report offered little immediate help. Imports in the third quarter once again grew faster than exports, leaving a significant trade gap. Imports grew at an annual rate of 17.4 percent, compared with a 5.0 percent gain for exports.

Government spending began to slow, as the effects of the stimulus spending wear off. That was reflected in the unemployment numbers for September. Companies added 64,000 jobs last month, but over all, the economy lost 95,000 nonfarm jobs, the result of a 159,000 decline in government jobs. Local governments were particularly hard hit. “The problematic factor is that consumers remain fundamentally insolvent or worried about becoming so, and too many of the major banks are zombies uninterested in commercial or industrial lending,” said James K. Galbraith, an economics professor at the University of Texas.

Still, each quarter that the economy does not lapse back into recession adds incrementally to consumer and business confidence, and perhaps eventually to growth. The great immediate test, economists say, is the fourth quarter. The hope is that small signs of market strength in recent weeks may coalesce into something that looks more like an actual recovery, and that by next spring unemployment may stabilize and the gloom may lift.

“As with money, there is a power of compounding the economy,” Mr. Blitz said. “The longer you go with 2 percent growth, you begin to push up against constraints, and the more the fear of unemployment ebbs, the more chance there is that people will begin to feel confident. It’s a very slow burn.”