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Economic recovery falters dramatically in first half of year

Government figures show the economy grew at a weak pace of 1.3% in the second quarter and a revised 0.4% pace in the first quarter.

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Reporting from Washington

The economic recovery faltered dramatically in the first half of the year, and that means more trouble ahead.

The latest Commerce Department figures show that the nation's economic output was gasping for breath long before the debilitating debt-ceiling debate took center stage, further dimming prospects for 14 million unemployed Americans.

The nation's total economic output grew at an anemic annual rate of 1.3% from April through June, below already weak expectations. And the government sharply scaled back its estimate of first-quarter growth to a feeble 0.4%, the lowest figure since the recession technically ended two years ago.

"These are disastrous numbers for the economy," said **Bernard Baumohl**, chief global economist at the Economic Outlook Group. "We're seeing some clear, concrete signs that the economy is teetering on the edge of recession."

Those fears and the continuing debt-ceiling standoff ripped through the financial markets Friday, pushing the Dow Jones industrial average down 96 points to its sixth straight loss. It was the worst weekly performance for the index in more than a year.

Economists are now talking more freely of prospects for a "double-dip" recession. Nariman Behravesh, chief economist at IHS Global Insight, pegs the odds at 30%.

"When growth is so weak, it's not going to take much of a shock to push us over the edge," he said, noting that a surge in oil prices, now less than $100 a barrel, to $110 a barrel could do it. "Add on top of it all this stupidity in Washington and this is a very risky situation."

On a practical level, the new data show the economy is not generating nearly enough horsepower to spur employers to hire. That means consumers will continue to keep a tight lid on the kind of spending needed to boost demand and get more people working.

Consumer spending increased just 0.1% in the second quarter, a key reason for the slow growth. And weighed down by the political stalemate over the debt ceiling, consumer attitudes only worsened in July.

Consumer confidence plunged this month to its lowest level since early 2009, according to the Thompson Reuters/University of Michigan Survey of Consumers released Friday. The outlook by consumers for their finances was "quite bleak" and their spending will be "barely higher" in the second half of the year, predicted Richard Curtin, the survey's chief economist.

The U.S. economy has been buffeted this year by harsh winter weather, soaring gasoline prices because of Middle East unrest, and supply chain disruptions in the automotive and electronics industries caused by the Japanese earthquake and tsunami.

Adding to the economic woes is the looming threat of a U.S. default or credit rating downgrade because Congress and the White House have been unable to raise the nation's $14.3-trillion debt ceiling.

"It's creating a big issue for consumers and businesses," Behravesh said of the uncertainty over what a debt ceiling deal would include.

President Obama used Friday's economic data to push lawmakers to strike a deal before Tuesday's deadline for raising the debt ceiling. And one of his top economic advisors, Austan Goolsbee, warned that U.S. officials must "end the uncertainty surrounding the risk of default."

"We are at a fragile moment in the world economy and cannot afford to do anything to undermine our recovery at a moment such as this," said Goolsbee, chairman of the Council of Economic Advisors.

The steep cuts in federal spending that would be triggered if the government could no longer borrow to pay all its bills probably would force the economy to contract in the third quarter, **Baumohl** said. The odds that such a contraction would last for two quarters — the technical definition of a recession — are increasing given the weak growth, he said.

"It clearly shows that people continue to be gripped by uncertainty, and that has increasingly crippled consumer spending and business investments," he said. "All of these things together are really making it very difficult for the economy to move forward."

That move is even tougher because it turns out that the severe recession was deeper than originally thought. From late 2007 to mid-2009, the economy shrank at an annual rate of 3.5%, much worse than the previous estimates of 2.8%, the Commerce Department said Friday.

Given that data, and the worldwide problems during the first half of this year, the poor growth numbers were expected, said Sal Catrini, managing director for equities at Cantor Fitzgerald & Co.

"If that didn't cause a short-term blip … I'd question all economic models," he said, noting that second-quarter growth was much better than in the first quarter. "You can argue given how bad things were … things are on the margin getting better."

The poor second-quarter growth numbers would have been even worse without federal spending, which increased 2.2% after dropping 9.4% in the first three months of the year.

But huge federal spending cuts included in proposals to raise the debt ceiling pose another problem for the recovery, Behravesh said.

"Given how fragile things are … the hope is the cuts would not kick in right away," he said, "because now would be a terrible time to cut spending."