

The Economy: What Now?

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Article:

The roller coaster that is the recession of 2008-09 keeps careening along. April marks the recession's 17th month, which makes it the longest one since the Great Depression. I don't suppose anyone will be popping corks to celebrate this milestone.

By this point in a typical recession, economists start to notice glimmers of light at the end of the tunnel, as handfuls of economic indicators turn positive. One of the strongest indications is when the number of initial claims for unemployment insurance declines significantly from its mid-recession highs. The index of consumer confidence shows signs of life, manufacturing perks up, and housing starts begin to rise.

But as of this writing, very little is glimmering. Unemployment claims are the highest they've been since 1982. Consumer confidence hit another all-time low in February and manufacturing is still in the doldrums. And housing? I don't think anyone expects that industry to lead us out of this recession.

Overall, the news continues to be quite bad. Since the start of the year, we've seen the unemployment rate continue its upward trend. We've seen declines in payrolls, factory orders, service-sector activity, housing starts, and home sales. And furniture retail sales are continuing their two-year slide. They fell again in January and have declined over 20 percent (in inflation-adjusted terms) since they peaked in early 2007.

The only good news so far this year has been either sporadic or misleading. There were upward blips in consumer spending and personal income, but it's too soon to place much weight on those numbers. Gasoline prices have risen on increasing demand, which is actually good news in the middle of a deep recession, when any hint of increasing demand is encouraging. But this is likely the market's anticipation of the coming spring driving season rather than a sign of the recession's imminent end.

The index of leading economic indicators rose for the second straight month in January, but it was largely artificial (a "head fake" in the words of one economist), driven by the government's large increases in the supply of money, as it struggles to keep the entire system from freezing up.

Finally, the dollar is stronger than expected, a result of the global flight to financial stability. It might be surprising at a time when our financial system is at risk of collapsing, but U.S. government securities are highly valued by foreign investors whose own economies are in bad shape. To be sure, a stronger dollar is bad news for exporters, but it's good news on the whole given the extent of government borrowing ahead of us.

So if none of the good news carries with it much hope of an imminent economic recovery, the question remains: "Why are we seeing such bad news so far into the recession?"

In part, this is because the official dating of this recession is problematic. What we're experiencing is really a "recession within a recession." From December 2007 until last fall, we had a mild downturn, as employment declined but most other economic indicators held steady. Then, the financial crisis slammed the economy with a vengeance, and that's when the roller-coaster phase began.

The financial crisis began in earnest after the investment bank Lehman Brothers failed in mid-September. Using that date, we're only about seven months into the deep recession that built on and exacerbated the mild recession then under way. Therefore, perhaps we shouldn't expect to be over the hump yet in this "recession within a recession."

Sure enough, few economists are predicting either a quick end to the recession or a vibrant recovery. The most optimistic forecasts see the recovery happening about mid-year. And many of those forecasts are predicated on the federal government's anti-recession initiatives working.

This is why the Obama administration has been communicating a sense of urgency about the recession. The fiscal stimulus package it pushed through Congress will inject nearly \$800 billion into the economy. Some of the spending in the bill will be highly stimulative, some less so.

From the home-furnishings perspective, the stimulus bill will lack an important provision that was supported by a number of trade associations, including National Home Furnishings Association. These groups lobbied hard but unsuccessfully to include a tax credit for buying home furnishings.

Of the remaining furniture-friendly elements of the bill, the best known are provisions that encourage home purchases (not home construction!). For example, the temporary tax credit for first-time home buyers was increased slightly to \$8,000 for a married couple. And unlike the credit enacted for last year, the new one doesn't have to be repaid to the government. But given the rule of thumb that only about a fifth of retail furniture sales are attributable to a home purchase, the furniture-specific stimulus is less than the industry had hoped for.

Perhaps that's okay. For the most part, the interests of furniture retailers coincide with everyone else's. We need consumers to regain confidence and start spending. That will only happen when job losses level off and new jobs are created, whether by government projects or private businesses.

But fiscal stimulus is just part of the puzzle. It's hard to see how the stimulus bill can succeed unless credit markets thaw. So far both the Bush and Obama administrations have taken only tentative steps to solve the problem of widespread insolvency. Neither the Obama administration nor Congress appears to have the stomach for the dramatic actions needed in the banking and financial sector (possibly including temporary nationalizations) to get capital flowing again.

We haven't seen this combination of deep recession and financial crisis since the 1930s. Even though the economic pain of this recession won't approach that of the Great Depression, our situation is still quite serious. But with luck, the combination of fiscal stimulus and financial stabilization will make it possible for more glimmers of light to start shining our way.

Writer's note: After my deadline for this column, the federal government released advance estimates for February's retail sales, and the numbers weren't bad at all. Total retail sales fell only 0.1 percent from January, which was a smaller decline than expected. And furniture sales rose 0.7 percent, the first monthly increase since last May. The increase could prove to be only a blip, and furniture sales are still well below their peak of two years ago. But until we see next month's data, perhaps we can afford a teeny bit of optimism for a change.