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Deep trouble seen for U.S.

ECONOMIST'S VIEW: Woes are very unlikely to pass Canada by

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CANWEST NEWS SERVICE

Ignore the fact that equities are flourishing and stock markets have been hitting new highs. Pay no heed to the annual-earnings front where companies are reporting gains in their earnings-per-share that exceed 11 per cent.

Don't look to consumers to continue their free-spending ways. It's not going to last.

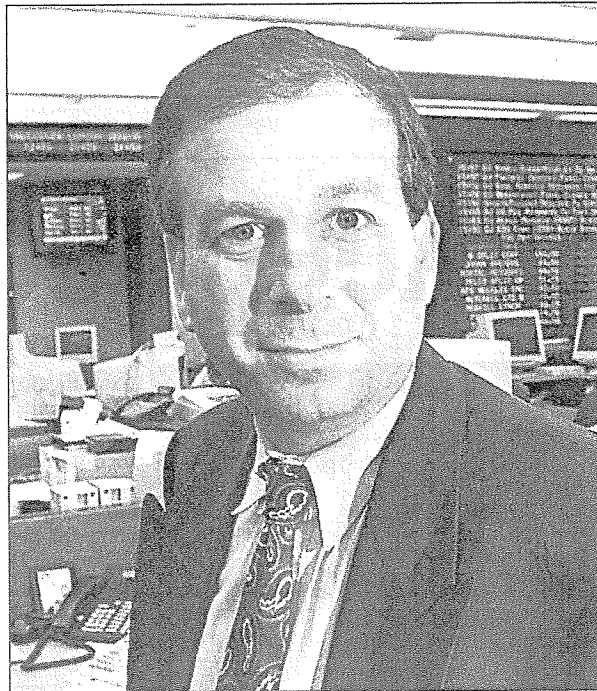
This is an economy in deep trouble. Productivity is on the skids and the odds of a recession are growing. It could, perhaps, require three interest-rate cuts to stave it off.

In Canada, you say? Not at all. We're talking about the U.S., and the views are those of one of Wall Street's leading economists, David Rosenberg of Merrill Lynch.

Rosenberg is glum about the U.S. outlook and, if he's correct in his assessment, don't expect it to bypass Canada's economy.

Rosenberg believes the Federal Reserve may have to lower its key interest rate, now at 5.25 per cent, by 75 basis points to 4.5 per cent to revitalize employment. The impact that would have on the Canadian economy and the dollar could be painful.

The Bank of Canada would be compelled to follow suit or risk seeing the dollar



David Rosenberg sees economic trouble ahead for the U.S. — and Canada. — CANWEST FILE PHOTO

surge even higher with devastating consequences for Canadian manufacturers and exporters, who are already fighting a currency headwind.

Lowering Canada's overnight lending rate by 75 basis points to 3.5 per cent would boost stocks, lift the housing market, boost consumer spending and could increase inflationary pressures.

That last one presents a problem. The Bank of Canada is on an anti-inflation

bent, even if it means raising rates. For Bank of Canada governor David Dodge, standing pat on the interest-rate front, even while the Fed lowers, risks driving the dollar through the roof.

From Rosenberg's perspective, the U.S. economy is sickly. For those wondering how consumer spending can persist in face of a slowdown, Rosenberg says it's homeowners using cash withdrawn from equity in their homes who are the spenders.

The decline in housing wealth, tightening in mortgage lending, rising gasoline prices, brutal debts and a looming soft labour market will put a stop to that in coming quarters, he says.

"The bottom line is that we have just come off the fourth consecutive quarter of sub-three-per-cent sequential real GDP growth . . . and over the past 60 years that's always heralded a recession. This multi-quarter trend of below potential growth is not sustainable — something is going to break in one direction, of that much we are sure. All we have to say is that it had better be different this time." But will it be? He thinks not.

This all suggests that the U.S. economic ship may be becalmed in the next 12 months and equities, too.

Wall Street celebrated when the Dow Jones Industrial Average surpassed 13,000 points. But one-third of the 1,000-point surge in the Dow over the past six months has been due to just four stocks — Altria, Boeing, Honeywell and ExxonMobil — Rosenberg says.

"What the move in these companies really tells you about anything in the U.S. economy or global economy is actually very little."

Of course, there is the possibility that Rosenberg's assessment of the U.S. economy is wrong. But if he isn't . . . well, we've been warned.