U.S. economists warn possible danger ahead amid signs of economic recovery

by Matthew Rusling

WASHINGTON, Aug. 17 (Xinhua) -- A rash of economic indicators show early signs of recovery from the worst U.S. recession in decades, but the economy could still take another nose dive, economists said.

Gross domestic product for the second quarter of this year shrank by only 1 percent in the U.S., with auto sales rising 15 percent in July and manufacturers reporting rapid growth in new orders.

Moreover, the S&P/Case-Shiller 20-city index of home prices rose 0.5 percent for the three-month period that ended in May. A more stable housing market would boost the flow of credit and reduce loan defaults, experts said.

Based on those and other positive figures, economists believe the recession will soon reach -- or has already hit -- its bottom. But despite the welcome news, some fret the rebound will be short lived.

Tad DeHaven, budget analyst at the Washington, D.C.-based CATO Institute, said that while the economy might rebound, gains could be lackluster and temporary.

"We'll either get a shallow recovery and meander along or have a recovery followed by another recession," he said.

The problem, he said, is that government spending has triggered much of the recent growth, and that is no panacea for long-term growth.

Programs such as "cash for clunkers" -- a government-funded program encouraging people to purchase new cars while trading in old ones -- may boost auto sales in the short term but could run out of gas once funds dry up.

"Car sales are up because of 'cash for clunkers'," he said. "Soyou get the jump in auto sales but it's just short term."

Moreover, the economy faces a number of issues that could bode ill for the country's long-term fiscal health, such as skyrocketing deficits and too much borrowing, he said. "The government can not continue to issue the debt that it is issuing," he warned.

And if government spending is a cure-all for sick economies, "then shouldn't we have been in an economic boom now?" Former President George W. Bush oversaw eight years of heavy government spending that yielded few economic benefits, he said.

Desmond Lachman, resident fellow at the Washington, D.C.-based American Enterprise Institute, said the numbers indicated that the pace of economic decline had moderated substantially. "So we are going to get a bounce in the third quarter," he said.

Companies' inventories are depleting -- which means production must ramp up -- "cash for clunkers" is boosting auto sales and the stimulus package is kicking in, all of which will stabilize the economy in the short run, he said.

"But the issue is whether it will continue," he said, adding that there are a number of reasons to be cautious.

Those include retail sales, which declined in July, compressed wages and the possibility that unemployment could linger around the 10 percent mark until 2010, he said. And with consumption fueling 70 percent of demand, such conditions bode ill for the long term.

Moreover, the unemployed may feel the sting of joblessness for some time, as companies will increase hours for part-timers before hiring new employees, he said.

And while GDP is projected to rise by 2 or 3 percent this quarter, it will take time to climb to pre-recession levels, Lachman said.

Dean Baker, co-director at the Washington, D.C.- based Center for Economic and Policy Research, said, "I really haven't been that impressed with any (numbers) we've seen."

Investment and net exports will be the drivers that lift the economy out of recession, but there is no evidence that those indicators are picking up, he said. Unemployment will continue to weaken the market, given that the jobless tend to spend less, he said.

Indeed, Chad Stone, chief economist at the Washington, D.C.-based Center on Budget and Policy Priorities, said July's employment report showed that labor market conditions remained "extremely harsh for job-seekers, generating a record level of long-term unemployment".

But the good news is that the labor market has improved from earlier this year, signaling that a rebound may be in sight, although "that news must be tempered by the ongoing plight of the long-term unemployed," he said.

Other experts, however, voiced a more positive outlook and pointed to indicators that could signal a turnaround. Most important are the higher-than-usual industrial productivity figures that could bode well for the short term and provide the spark that re-ignites the economy.

"I'm optimistic that we are on the road to recovery," said Robert Johnson, associate director of economic analysis at Morning star, an independent research provider. He added the economy had hit bottom in June or July and that growing manufacturing orders could spark a ripple effect to other sectors.

Since many company inventories are low, firms will need to ramp up orders from factories. That will put more people to work and spark an uptick in spending, he said.

"Exact predictions are difficult, and any unwise decisions in Washington could thwart a rebound, but based on numbers I've seen so far we'll have a shot at 3 percent long-term growth," Johnson said.

France and Germany's recent GDP increases could also be good for U.S. exports, he said. "If you put all those things together it's a roadmap to recovery."