

US. ECONOMY CLOSE TO EDGE

By John J. Duffy

PARIS — The U.S. economy in 1990 will tip closer toward recession than at any point in the last seven years but should, with the help of easier credit policies from the Federal Reserve, manage to right itself before it falls off the edge.

That is the message from most U.S. economists as 1989 draws to a close. Despite government forecasts that the economy will grow at a steady 2.6 percent pace next year, many private analysts say growth at about half the level is a more likely bet.

"The economy will grow at a good bit less than its potential, but with any luck it should keep growing," said David H. Resler, chief economist at Nomura Securities International Inc, in New York.

Analysts say the seven-year old U.S. economic expansion is entering the 1990s with several of its major growth cylinders either misfiring or not working at all.

U.S. corporations, for example, are locked in a severe profits squeeze. Because of slack demand, many are unable to raise the prices of their products enough to keep pace with rising wages and costs. As a result, U.S. corporate profits are expected to fall by between 5 percent and 10 percent in 1990.

"The profit squeeze is in place now and the fallout will show up

clearly in 1990," said Allen Sinai, chief economist at Boston Co. Economic Advisers.

Economists say lower corporate profits translate directly into lower spending for new plant and equipment, which hits at an important source of strength for the U.S. manufacturing economy.

The Commerce Department estimates that U.S. capital spending will rise by only 4.9 percent next year, half the estimated 1989 pace and the lowest since 1987.

In addition to suffering lower corporate profits and capital spending, the U.S. economy in 1990 is unlikely to get the big boost from exports that it has received in recent years.

The dollar, despite its recent decline, remains higher than a year ago and that erosion in U.S. competitiveness in world markets is expected to show up in higher monthly trade deficits next year.

As a result, the decline in the U.S. merchandise trade deficit from over £ 150 billion in 1987 to an estimated £ 103 billion in 1989 - a decline which meant boom times for U.S. exporters - is likely to come to at least a temporary halt in 1990, economists said.

"The improvement in trade will stall next year with the monthly trade deficit hanging at about £9 billion," said Neal Soss, chief economist at First

Boston Co. in New York.

Despite the black marks against the economy as the new year begins, economists said several positive factors will prevent the slowdown in growth from becoming an outright contraction.

Internationally, the United States will shift from its traditional role as a locomotive of world economic growth to more of a free rider, with its economy dragged upward by the more buoyant growth of its trading partners.

"Major economies abroad are on a much faster growth track than the American economy," said Walter Joelson, chief economist at General Electric Co. Growth abroad will help U.S. exports resist the pressure from a stronger dollar, Mr. Joelson said.

But perhaps more importantly, economists said, restrained U.S. inflation in 1990 will allow the Federal Reserve Board to lower interest rates progressively in early 1990, which should feed through to faster growth in the second half of the year.

Mr. Joelson said an easier Fed policy will revive interest-sensitive sectors of the economy such as housing stimulate the export sector by dragging the dollar lower, and help restore capital spending.

"Interest rates are clearly too high in real terms," Mr. Joelson

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said, "A decline is critical to stimulate investment."

Analysts said that the Fed is acutely aware of the dangers the U.S. economy faces in 1990 and that it has already embarked on a policy to lower rates.

The Key federal funds rate, which has hovered at about 8.5 percent recently, is expected to ease to about 8 percent by mid-year and to 7.5 percent or lower by the end of 1990.

Economists are generally confident in the Fed's ability to ward off a recession in 1990, because the central bank showed such confidence in 1989. The Fed tightened policy sharply in the first half of the year to counter a surge in inflation, but shifted gears during the summer as signs of economic sluggishness became evident.

But the 1990s will also bring changes in the U.S. economic outlook that even that Fed will be powerless to influence, making economists hesitant about making forecasts beyond next year.

U.S. demand for new cars, which weakened considerably in 1989, will weaken further in the 1990s because fewer new drivers will be entering the market, Resler said, while a slower rate of family formation will mean less of a demand for housing.

On the positive side, he said, less U.S. resources are likely to be devoted to defense in the 1990s because the perceived threat from the Soviet Union and Eastern bloc countries is expected to recede further in the wake of the dramatic changes of 1989.