



The US Economy & Tax Rebates

Following last week's fall against the euro the dollar will be vulnerable to more bad news from the US. Crucial this week will be July's retail sales report, which is due for release on Tuesday. Last week's Beige Book and chain stores sales reports raised concerns about the consumers' ability to keep the overall US economy out of recession. The numbers will be important in determining how worried we should be about consumer spending slipping back too much before business spending starts to recover and if the tax rebates which started to come through in the last week of July will have a discernable impact on retail activity. Retail sales increased 0.2%, or 4.1 in year-on-year terms in June. However, this was boosted by the fact that motor vehicle sales stayed reasonably high. Underlying sales (ex-autos) fell 0.2%, with the year-on-year rate coming in at a weaker 3.6%. This month headline sales are forecast to fall 0.3% with underlying sales up 0.1%. Due to their timing, if the tax rebates do make a difference it will more be more noticeable in the August retail sales report. Nevertheless, July's numbers will give a good indication of how the land lies.

The Bush tax plans says that it will give \$38 billion back to the economy. This equates to an average \$600 additional income for each married couple (based on joint tax return). The big question is, in the face of economic downturn and rising unemployment, will people spend or save their rebates. Falling energy prices and significantly lower interest rates should make consumers more comfortable about spending the extra cash. Crude oil prices are now 13% lower than they were this time last year. Official interest rates, which primarily affect consumers through their impact on mortgage repayments, have been reduced by 2.75% since the beginning of the year. Even the IRS is encouraging consumer to get out and shop. At the Internal Revenue website (www.irs.gov) an article on the rebates reads *"let's see – new barbecue, early holiday shopping. You get the idea "* or *"Alabama couple revels in receiving advance payment check"*. Large retail outlets are also heavily advertising enticing concessions and offers to ensure that the money is spent in their stores.

People will spend the money if they are feeling good about the future. Recent confidence surveys may provide some clues as to what consumers will do. After improving for two months, consumer confidence slipped down by several points in July to a reading of 116.5. Both the expectations and the assessment of current conditions eroded. The perception of the labour market is eroding rapidly.



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Only 36% of consumers believe that jobs are plentiful, down from 56% one year ago. To put this in perspective, however, this measure fell to 5% during the last recession. Despite being gloomier about the economic outlook consumer still seem ready to spend, with the only positive aspect of the report coming from resilient consumer spending plans.

After the spending spree of the past couple of years it is estimated that each family has run up credit card debt of around \$8,000. Therefore, many may choose to use the extra money to make some in roads into reducing this. Recent polls have suggested that the economic impact may not be as big as originally anticipated. One poll showed almost half of the respondents saying that they would use the money to play bills. According to the latest Gallup poll, only 17% of the respondents plan to spend the cheques, with 30% saying that they intend to save it. The results of that survey however, do leave over 50% undecided.

The last time that consumer received such as rebate was in 1975. Only one third of the \$200 rebate was spent back then. However, economic conditions are very different 26 years ago. Inflation averaged 9.2% that year while unemployment, at 8.5%, was almost double what it is today. 3-month interest rates averaged 6.8%. Currently, the headline inflation rate in the US is 3.2%. Also, while over half a million jobs have been shed in the manufacturing sector since the beginning of the year, the unemployment rate has only edged up by 0.3%, from 4.2% to 4.5%. Robust economic conditions for the last ten years means that the US consumer has changed significantly since 1975 and is now a better spender than saver. The personal savings ratio is currently in negative territory. In 1975 it was 7.0%. It's all down to Al and Arlene Able from Alabama.

Geraldine Concagh

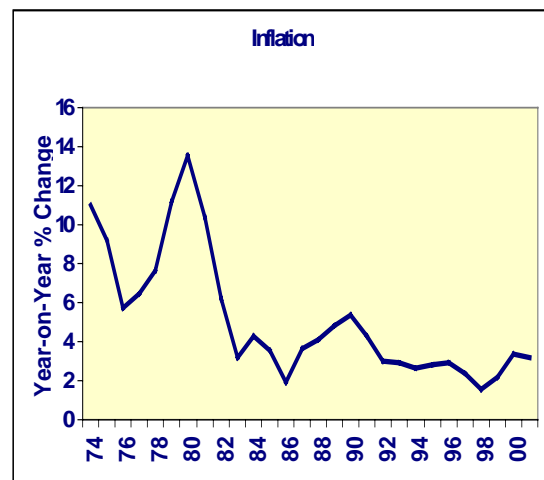
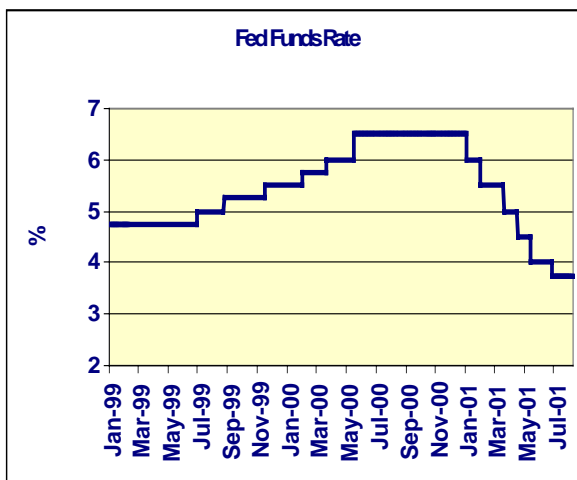
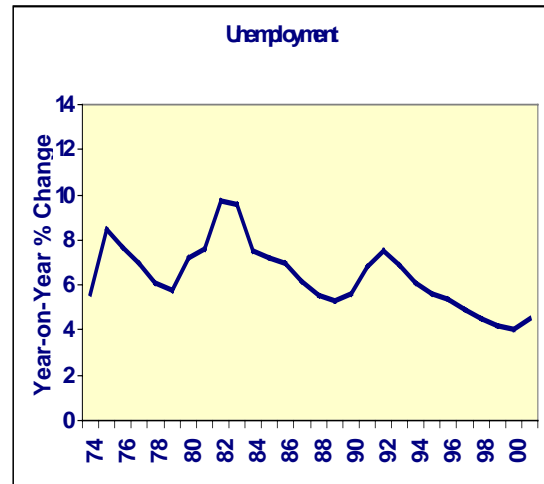
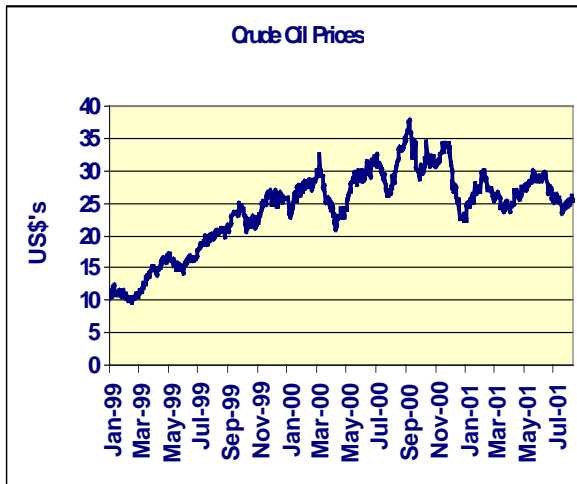
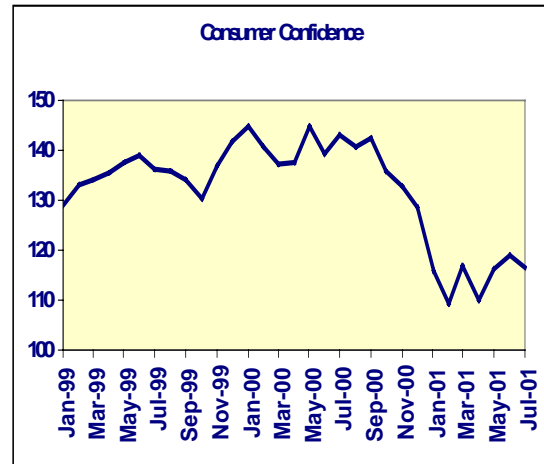
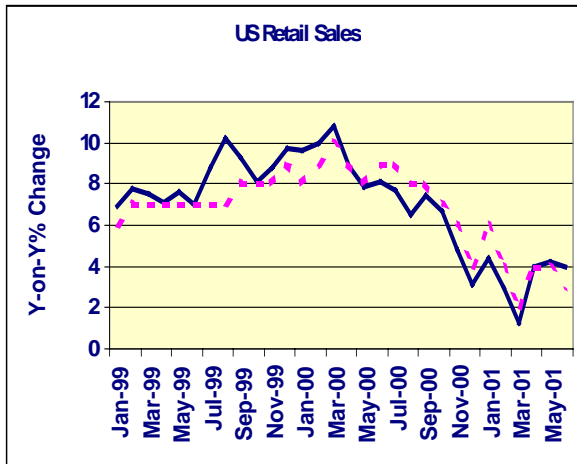
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US Chart Book



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