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Your Kiplinger Connection

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The economy

Some of the pep in the economy this past quarter will fade as interest rates continue to climb and cold weather takes hold. Costly heating and electricity bills will deflect some consumer spending in the winter months. Auto production will also hit the brakes.

We continue to expect economic growth of 3% next year.

Home remodelers will be even busier next year than this year, with spending on remodeling expected to increase to about \$163 billion, up from \$155 billion in 2005. Spending on home improvements will come in contrast to a dip in construction of new housing by about 5% in 2006.

Fueling the trend: Decent price appreciation on most homes, which gives homeowners more home equity to tap for remodeling work. And a penchant of baby boomers, particularly those over 50, to spend more on fixing up their homes than previous generations did at the same age.

Red tape will slow new-home construction on the Gulf Coast.


There'll be only 45,000 or so housing starts in 2006, about half of what builders were planning on in the weeks after Hurricane Katrina.

Workers are in short supply, which will drive up wages. Plus a Gulf Coast-area exemption to a federal law that requires workers on federal projects to be paid prevailing wages will end in November.

Sales of construction equipment will slow next year, rising 9% after a 15% jump this year. The smaller-than-expected highway bill plus a cooler economy will cause demand to slacken for cement trucks, paving equipment, cranes, large compressors, and related equipment.

Business costs

Budget for big hikes in 2006 electricity rates ... 10% on average,

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much more in some parts of the country. In New England, Florida, Texas, California, and the Upper Midwest, greater reliance on natural gas for power generation will push rates up by at least 15%. In fact ...

Some commercial customers will pay up to one-third more for power next year. Electricity rates have lagged the surge in other energy costs in the past year, in part because of states' regulatory requirements. But no longer. Electricity buyers will soon feel the heat as utilities pass along the soaring prices they pay for natural gas and coal.

Have an underfunded pension plan? Consider freezing benefits.

It buys time for employers that are up against the wall, especially now that Congress is eyeing a bill to tighten funding rules. When a company opts to terminate its pension plan altogether, it must buy annuities for plan participants ... an expensive proposition.

Freezing offers two advantages: It halts the accrual of additional benefit liabilities and allows the company to wait until interest rates rise and annuity prices fall before termination.

Converting to a cash-balance plan isn't an option for now. A bill to clarify the status of such plans is bottled up in Congress.

Money

Fed Chairman-designate Ben Bernanke will be an inflation hawk ...

Even more of one than current Chairman Alan Greenspan. Bernanke believes that stifling inflation should be the Fed's main task. Bernanke's advocacy of an inflation target is a strong sign of his desire to emphasize the central bank's inflation-fighting mandate. Its other mission to keep employment at a high level will come second.

Adoption of a target isn't a sure thing, given skepticism among several Fed officials who think one would be too constraining. Even so, Bernanke's views on the issue will influence his approach.

A focus on inflation will make him slow to cut interest rates when economic shocks occur. Don't expect much help from the Fed if housing slows more than expected. The same goes for energy spikes.

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