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Nicholas S. Perna, **Economic Advisor**

THE NATIONAL RECOVERY

In a couple of months, we'll be celebrating the second anniversary of the end of the "Great Recession." The downturn that started in December 2007 finally "ended" in June 2009 – according to the official recession scorekeepers, the National Bureau of Economic Research. However, I don't think we'll hear too many champagne corks popping because the long and deep recession has been followed by a highly uneven and, in many cases, incomplete recovery.

In the final quarter of last year, real gross domestic product (GDP) returned to the level reached just before the recession started. The recovery started when GDP began growing again in the middle of 2009. And after falling more than 50 percent, the Dow Jones average passed though 12,000, putting it only about 15 percent below the all-time high of 14,165 hit in October 2007.

On the other hand, we've only recovered slightly more than 1 million of the nearly 9 million jobs lost during the recession. And despite a decline from 10 to 9 percent, the unemployment rate is more than double the 4 percent low achieved four years ago.

If we look beneath the top line GDP number, the picture is very mixed. Consumer spending has more than recovered its recession losses, but motor vehicles sales are well below previous peaks. Car sales hit record levels in 2005, slipped for the next couple of years and then really slid during the recession. Business spending on equipment and software is also more than fully recovered. During 2010, imports grew a bit faster than exports but exports looked considerably stronger towards year-end.

Construction has been hit very hard. Commercial buildings (offices, hotels, factories) continue to slide. These types of buildings usually lag the rest of the economy during the recovery phase of the cycle. This time, however, the lag could be even longer than usual given the slow growth of the economy and jobs.

One of the hardest hit areas is residential real estate. Housing starts plunged more than 75 percent during the cycle and have yet to begin rising. Normally, housing leads the economy out of recession. But falling prices, tight mortgage lending criteria and millions of foreclosures are preventing this from happening. State and local government spending has been declining for the past three years as budget problems take a heavy toll.

Stock prices have done well for a couple of reasons. The decline into early 2009 was probably overdone since the financial world did not come to an end! Today's very low interest rates make equities attractive relative to bonds and money market instruments. Plus, profits have been climbing thanks to increased business volume (real GDP), small employee compensation increases and large productivity gains. No wonder the Dow Jones average has soared about 85 percent from its March 2009 low.

In sharp contrast, only a small fraction of the huge number jobs lost have been regained. Close to 14 million people are unemployed, with about 6 million of them out of work for 6 months or more. The modest growth of real GDP by comparison with past recoveries is one reason for the labor market slack. Furthermore, employers have been able to minimize hiring by increasing the average workweek in addition to getting large productivity gains.

What's next? The consensus forecast is for roughly 3.5 percent rate real GDP growth this year with faster job growth than last year as productivity gains become harder to achieve. The CPI is expected to rise a modest 2 percent, a bit faster than last year's 1.5%. The majority of economists are not expecting a substantial pickup of inflation anytime soon. One key reason is that it will take some years for the unemployment rate to get down to levels where wage pressures are apt to intensify.

Musings & Amusings: Late Night

"Happy Presidents Day. This is a day when we celebrate history by getting great deals on mattresses."
- Craig Ferguson

"The problem in Egypt is that so many government officials are rich and the people are poor. I think it's a pyramid scheme." - Jay Leno

"The Senate has sent President Obama a spending bill that gives the government enough money to keep going for two weeks. Our Congress has the financial planning skills of a college sophomore." -Conan O'Brien

The problem with this forecast is an abundance (excess supply?) of uncertainty over factors that could undermine the outlook. This is beginning to be captured by the consumer confidence surveys. The better known confidence gauge, which is compiled by the Conference Board, was still well below pre-recession levels in February. However, this was entirely due to their pessimism about current economic conditions. Their optimism about the future had rebounded to levels last seen in 2007.

A more recent survey conducted by the University of Michigan showed a sharp deterioration in early March as people have become more worried about the future. Much has been happening lately: soaring oil prices and dramatically increased turmoil in the Middle East to cite just two. Not only do higher oil prices endanger the inflation forecast but they undermine consumer purchasing power as well. The Conference Board survey is soon likely to register the same concerns.

There's also concern among some economists that the potential for large cuts in federal spending and budget tightening at the state and local level could put the recovery at risk. In the short-run, spending cuts and tax increases are a drag on the economy – especially an economy in the early stages of recovery from a deep recession.

Given the pervasiveness of budget deficits, there's no easy solution. At the federal level, the Congress might focus its efforts on passing credible legislation now that starts reducing those deficits in a couple of years. This could be done by passing very explicit measures to reduce deficits that could be over-ridden only in the event of a national emergency.

THE REGIONAL RECOVERY

The pace of economic growth is very uneven in the northeast. Recent major revisions to the establishment survey of employment have altered the picture significantly. Furthermore, bad weather probably depressed the January 2011 employment data. No wonder Mark Twain complained about "lies, damned lies and statistics!"

As summarized in the table, Connecticut is now shown to have lost 119,000 jobs which is 7 percent of total employment and a deeper decline than previously reported. The state has since regained a sizeable 23,000 jobs which amounts 19% of the amount lost. This is a much better recovery than indicated by the older data. During the past 12 months, jobs have grown by a decent 1.4 percent. In January, the state unemployment rate was the same as for the nation.

On the other hand, the revised data still show Rhode Island as having endured one of the worse recessions of all the states. And in terms of jobs, the recovery had yet to begin as of January 2011. At 11.1 percent, Rhode Island's unemployment rate is one of the highest in the nation. At the top of the list are Nevada (14.2), California (12.4) and Florida (11.9).

The new data show a smaller decline for Massachusetts and a milder recovery than previously thought. Initially, jobs were reported to have grown by 1.5 percent in the Bay State last year. This has been cut almost in half by the revisions.

Like Massachusetts, New York's recession was considerably less severe than the rest of the nation and recovery is unfolding. As with all the other states in the region, government jobs continue to decline. Employment in financial services has started to rise again in New York and Connecticut but not yet in Massachusetts and Rhode Island.

What's next? The forecasting services had been predicting jobs growth in all our states during the coming two years. They will be crunching these new numbers to see whether recovery momentum (or the lack thereof) will continue in the face of federal and state budget cuts and much higher than expected energy costs. We'll let you know when they become available.

Regional Economic Conditions

	Unemployment		Jobs				Latest Change
	Peak	Latest	Lost		Regained		
			%	thous.	%	thous.	%
Connecticut	9.2	9.0	7.0	119	19.0	23	1.4
Massachusetts	8.8	8.3	4.3	143	26.9	38	0.6
New York	8.9	8.3	3.8	337	21.1	71	0.6
Rhode Island	11.8	11.3	7.9	39	0	0	0
United States	10.1	9.0	6.3	8,750	12.3	1,077	0.8

Labor market data are through January 2011. Latest change is from January '10 to January '11. All data are seasonally adjusted.

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