How Deep the Hole: Holding Job Losses to 100,000?

The Connecticut Economic Outlook: May 2009

Peter E Gunther, Senior Research Fellow

Connecticut Center of Economic Analysis

University of Connecticut

SUMMARY

If the Federal and international stimulus initiatives do not take hold by the end of 2009, Connecticut may see a deepening recession with job losses hitting 110,000 or more by 2011, with no end in sight. The result of the capital market crisis and serious losses in exports, the hole would be deep indeed. But if domestic and international stimulus packages take hold, generating a stronger national recovery, Connecticut employment losses would reach only 100,000 in mid-2010, then begin to recover. This will still be a painful contraction, with nearly twice the job losses of the last recession, but with less than two-thirds the losses of the early 1990s. Yet even the optimistic stimulus-driven Outlook suggests only a weak recovery for Connecticut in 2011 and 2012. Unless Connecticut develops a coherent, effective economic development strategy, supported with significant strategic investments, it faces an increasingly difficult economic future.
Introduction

The Bureau of Economic Analysis’ (BEA) most recent release of national accounts clarifies the underlying drivers of the US recession and with them some of the difficulties of returning to robust growth. Preliminary rates of change in national output (RGDP) and its components for 2009Q1 reveal that RGDP fell at an annual rate of 6.1% on the heels of the previous quarter’s decline of 6.3%; exports collapsed at an annual rate of 38.7%, and private investment imploded, contracting 51.8%. Because exports of goods accounts for 7.8% of RGDP, the worldwide nature of the recession hits the United States more strongly than in the past, the contraction in exports accounting for nearly half the contraction in 2009Q1 RGDP. The downturn in investment reflects both the difficulty in securing credit for those needing funds and the unwillingness of those with funds to make new investments in the face of uncertainties.

Internationally, continuing tensions in the Mideast, the H1N1 virus, and massive adjustments in the economies of America’s trading partners point to, at best, a slow recovery. The restoration of financial markets continues to be sluggish, but there is a small silver lining: inventories declined sharply, a process that will lead to expanding production in the future, and one that disguised a smaller contraction in the more important area of private fixed investment.

Our Recent Past

Massive downward revisions in national economic performance, together with leading indicators for 2008Q4 and preliminary data for 2009Q1 shape this Outlook. New permits for residential housing declined sharply, to 1,195 in 2008Q4 and 686 in 2009Q1, down from their peak in 2005, when they averaged 2,861 per quarter. (These data are seasonally adjusted.) Chart 1 reveals the downward trend of unit housing permits in the tri-state area since 2006 and Chart 2 their falling value. The only exception to the generally falling trend was the slight percentage increase in the value of CT housing permits in 2008Q1, offset by a steeper dive in 2009Q1.

Chart 1: First Quarter Change in Housing Permits 2006 to 2009 (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>Connecticut</th>
<th>New York</th>
<th>New Jersey</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td></td>
<td></td>
<td>-51.8%</td>
</tr>
<tr>
<td>2007</td>
<td></td>
<td></td>
<td>-19.7%</td>
</tr>
<tr>
<td>2008</td>
<td>-38.7%</td>
<td>-51.8%</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>-38.7%</td>
<td></td>
<td>-19.7%</td>
</tr>
</tbody>
</table>
This trend has cut nearly 15,000 jobs from the Connecticut construction industry, falling from 68,600 to 53,900 in the past year.

**Outlook**

Given both the national and local patterns, the Outlook is the bleakest since its inception. The challenge in projecting the pattern of economic activity over the next eight quarters is what to expect of the massive Federal stimulus and—this is critical—the rate of recovery in exports. This Outlook first explores the impact of a continuing weak national economy on Connecticut’s economic output and employment. This is an economy that continues to stall despite attempts to jump start it. The Outlook then looks at the contrasting case where the Federal stimulus (and those of its trading partners) takes hold, with the national economy accelerating from the fourth quarter of 2009. This offers a more optimistic projection.

**I: Weak National Recovery**

In the Outlook based on weak national growth, at annual growth rates of 0.79% in the next quarter, 1.5% for each of the next there quarters, and then 1.1%, 0.86%, 0.67%, and 0.05% in the last four quarters, Connecticut’s total output falls at annual rates of about 2.5% a quarter, as Chart 3 shows. This sustained decline in total Connecticut output (CtRGDP) undermines employment in the state, resulting in a deepening recession. Employment would fall to levels last seen 22 years ago, about 1,615,000—and would continue to fall beyond the ten quarters this Outlook evaluates.
II: The Stimuli Take Hold
The first Outlook may be unduly pessimistic, by fully discounting the benefits of global stimulus packages. CCEA developed an alternative scenario based on stimulus-driven recovery in RGDP, which Chart 4 shows. National economic growth, at annual rates, improves gently in 2009Q4, reaching 3.5% growth by the end of 2010.

Chart 4: Comparative National Growth at Annual Rates
The implications for Connecticut’s economic performance are profound. It flattens out in the middle of 2010 and begins to recover in 2010Q4 and into 2011, as Chart 5 reveals. CT employment would flatten out between 1,625,000 and 1,630,000, then begin to recover. This is but the beginning of a recovery, not a full fledged one. Employment would be about 100,000 below its previous peak. Even this bottom is 10,000 below the one in the previous Outlook due to the downward revisions in the BEA’s National Accounts data over its last three reporting quarters.

**Chart 5: Outlook for CtRGDP as RGDP Stimuli Take Hold**

Among the sectors particularly hard hit are construction, the result of the collapse in residential housing, durables, nondurables, retail and finance insurance, and real estate. As noted in the previous Outlook, there is also a significant risk that in their zeal to balance operating budgets and to make dramatic reductions in capital budgets—both of which Connecticut is doing—state governments will themselves generate economic contraction, undermining the international stimulus packages.

**Conclusions**

The sharp contraction in international trade, and thus in U.S. exports, and the melt down in credit markets are the root causes of the current recession. We now wait to see whether Federal and international economic stimuli are sufficient in scale, in design, and in length of commitment. But even if they clear each of those hurdles, Connecticut may see job loses for another year and then achieve only anemic recovery. If Connecticut reverses its steep cuts in capital expenditures, adopts a balanced approach to address its massive budget deficits, and—critically—develops and implements a coherent, focused economic development strategy, it would assuredly both accelerate its own recovery and begin to build the foundation for a healthy economic future.