

Western New York ECONOMIC NEWS

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The national economic outlook has improved over the year. Even with the end of the housing boom and the uncertainty surrounding the sub-prime mortgage mess, second quarter growth of GDP was 4 percent in real terms. On the local scene, with the possible exception of one local bank merger, it appears that the local economy will not be dramatically affected by the credit crunch that has focused on the housing market. Without the rapid growth in housing values that fueled the speculative housing boom of the last decade, there has been little need or desire for imaginative financing packages to get unqualified buyers into homes they can not afford in the hope that they could sell these properties before interest and principal payments adjusted to the level needed to fully service and retire the debt. While the direct effects appear to be modest, it is less clear how distressed debt markets could affect the consumption of durable goods, and even less clear what effect it would have on this important, though declining, sector of the Western New York economy. A more troublesome development has been the GM strike. Given the importance of the automobile sector in WNY, a quick settlement is in the best interests of the region.

The National Economic Outlook

Advance estimates of 2007:Q2 real GDP shows the national economy growing at a 4.0% rate after posting an anemic 0.6% gain during the first quarter of 2007 www.bea.gov. Real GDP growth rates since 2002 are shown in Figure 1 below. Factors responsible for the acceleration of growth during the second quarter included increases in: federal government spending, inventory and nonresidential structure components of gross private domestic investments and a decrease in imports. The growth rate of consumer expenditures, the most important component of GDP, was positive during the quarter but exhibited a deceleration to a 1.4% rate. Consumer expenditures on durable goods decreased by 0.3% during the quarter. This is an important development for the WNY economy given our dependence on the automobile sector. Expenditures on new residential housing units declined by 11.6%, the fifth consecutive quarterly double digit drop.

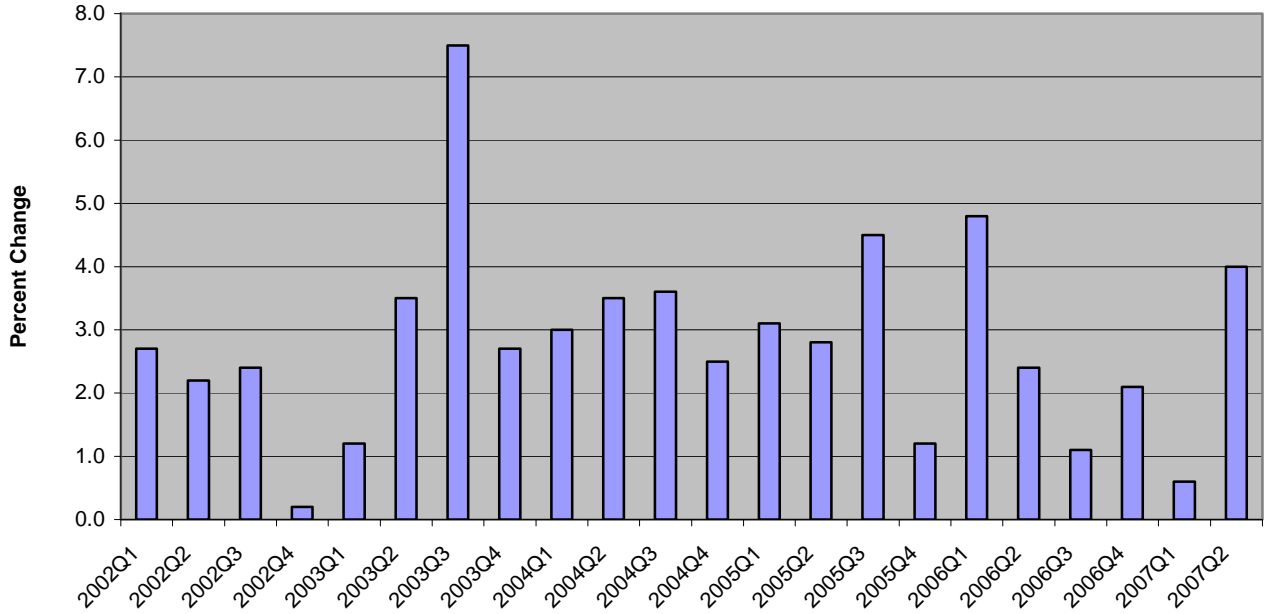
Ominous developments in the sub-prime mortgage market brought about by the dissipation of the housing bubble have led to an international credit crunch requiring central bank intervention. A severe drop in the demand for commercial paper caused the Federal Reserve and other central banks to intervene in the credit markets by offering additional liquidity. In mid-August, the Fed reduced the primary credit discount rate from 6.25% to 5.75% in response to the building international credit crisis. The discount rate, the rate charged by the Fed on loans to the banking system, has been set

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Figure 1: Real GDP Growth Rates (2002:Q1 - 2007:Q1)



100 basis points above the fed funds target in a formulaic fashion since January 2003. At their September 18 meeting, the FOMC lowered their Fed Funds target by 50 basis points to 4.75%. Obviously the Fed was attempting to combat the spillover of problems in the credit market to the overall economy. Since the last recession, the Fed's policy decisions have focused on achieving "reasonably" low rates of inflation. Since 2004, the Fed has steadily increased their fed funds target in 25 basis point increments. The 50 basis point increase in rates is clearly meant to send a message that the Fed is now bent on diminishing the probability of recession.

News from the inflation front has been relatively benign of late. Inflation rates based on the consumer price index have recently been in the 2% range while the GDP price deflator for personal consumption expenditures has been hovering around 2.3%. These inflation rates are shown below in Figure 3. The August payroll employment statistics showed a 4,000 job decline, the first drop in employment since August 2003 www.bls.gov. This development is indicative of a weakening economy and clearly played a role in the Fed's decision to lower short term interest rates. The payroll employment figures and the economy-wide unemployment rate are shown in Figure 2 below.

Figure 2. US Payroll Employment and the Unemployment Rate: 2002-2007

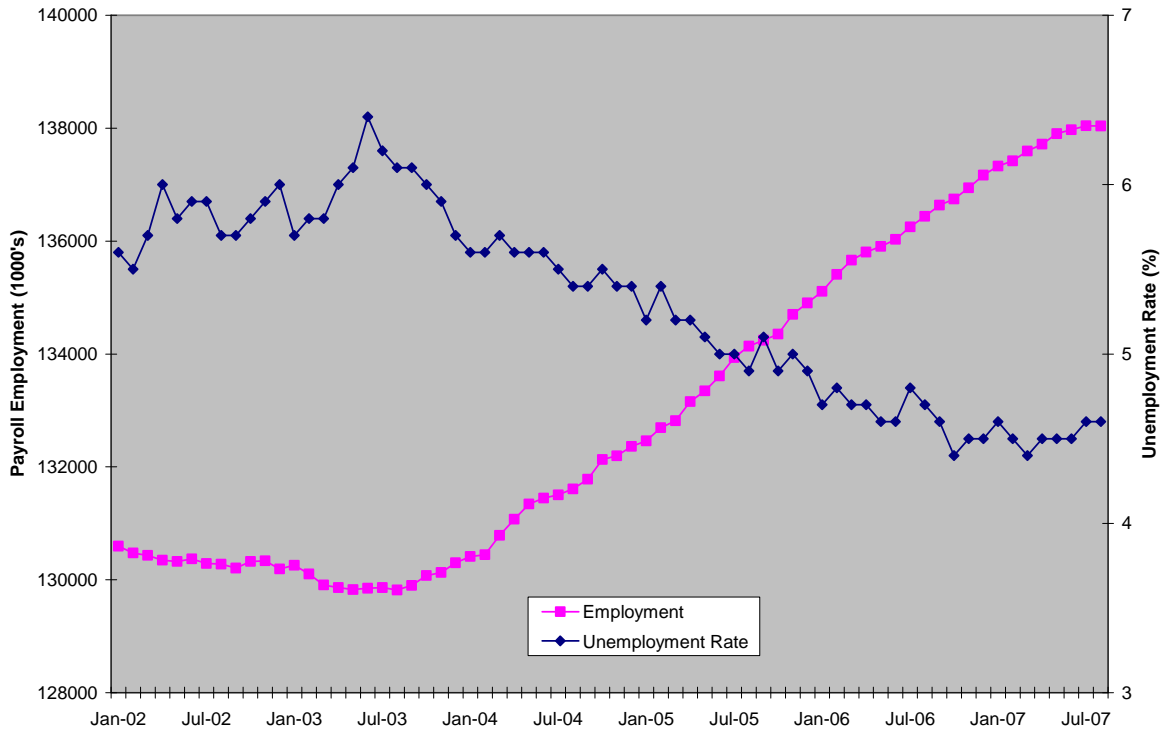
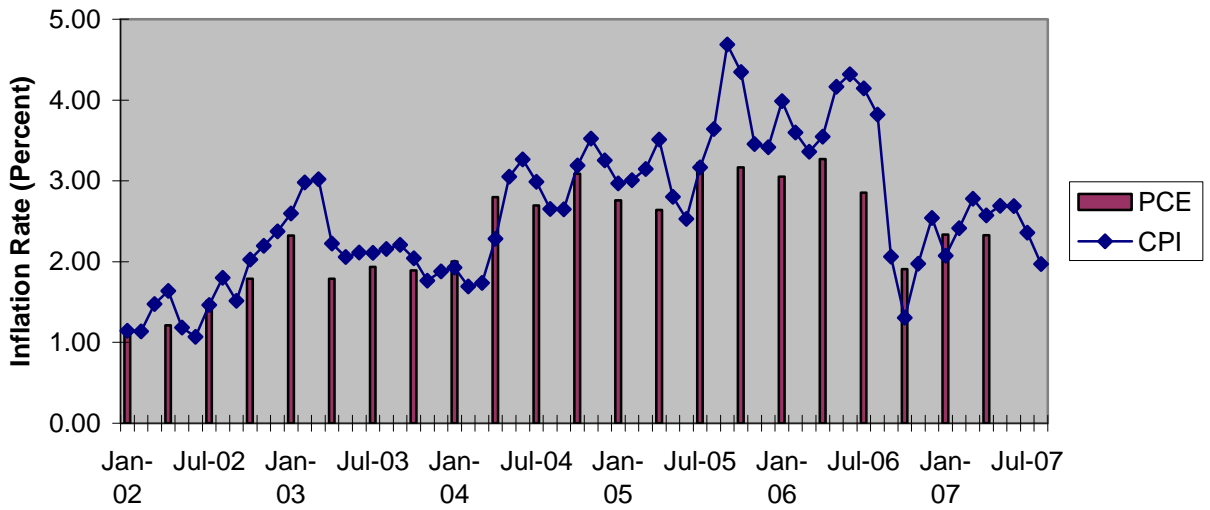


Figure 3. Inflation Rates based on the CPI & the Implicit Price Deflator for Personal Consumption Expenditures



The State of the Upstate Economies

Total employment on an NAICS basis for the Buffalo, Rochester and Syracuse metropolitan areas over the period 1990-2006 are presented in Figures 4a-4c. By the end of 2006, total employment in the Buffalo, Rochester and Syracuse metropolitan areas had not yet returned to their pre-2001 recession levels. Total employment figures from the summer of 2007 demonstrate there has been only modest growth over the 12 month period from the preceding summer in the Buffalo and Rochester metropolitan areas. The Syracuse metropolitan area, in contrast, has nearly returned to its pre-recession employment levels.

Figure 4a: Total Non-Farm Employment Buffalo MSA: 1990 - 2006

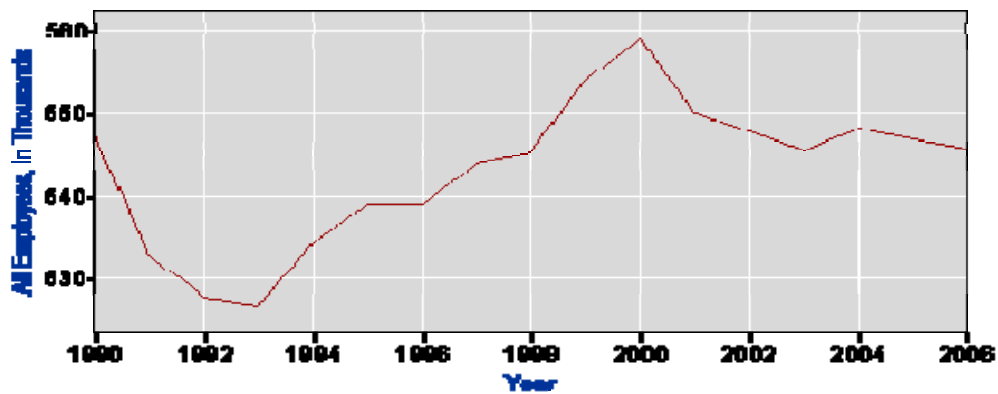


Figure 4b: Total Non-Farm Employment in Rochester MSA: 1990 - 2006

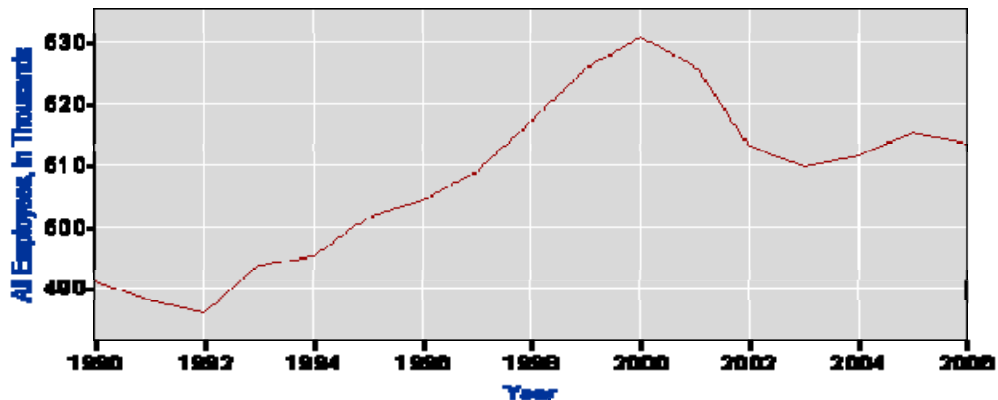
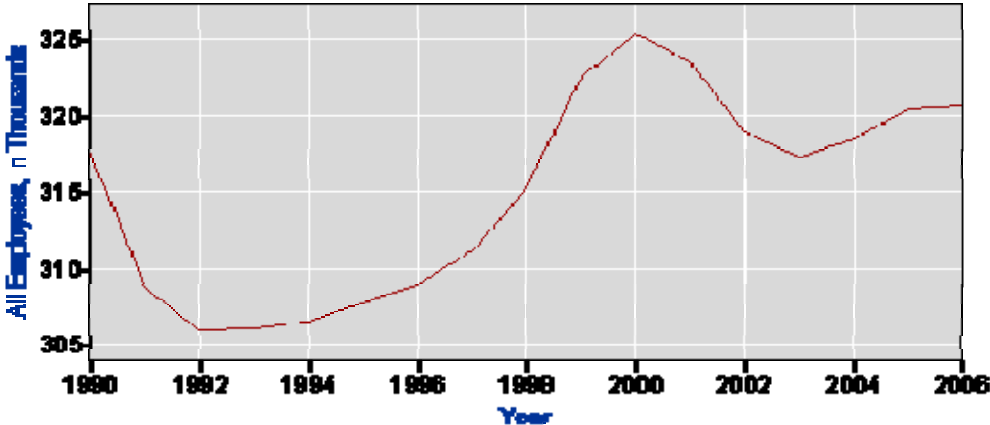
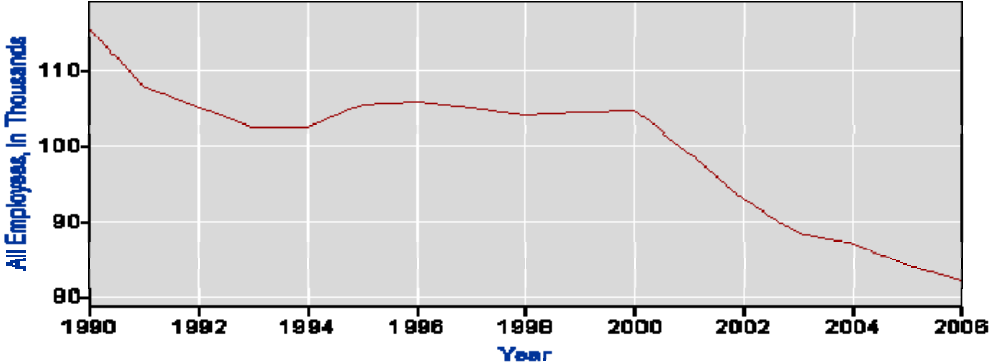


Figure 4c: Total Non-Farm Employment in Syracuse MSA: 1990-2006

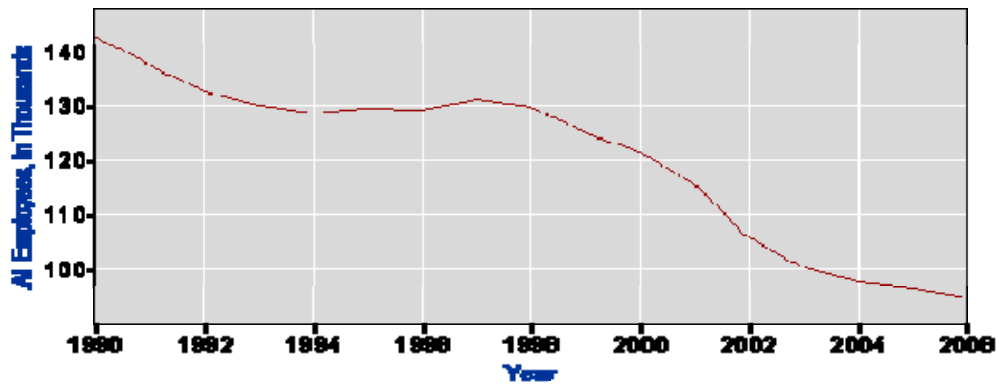


An analysis of the composition of the employment recovery may lead one to predict further decline for the major upstate areas. Following the recession of 2001, there has been a continuous reduction in high paying goods producing jobs and a movement toward lower paying service providing jobs in each of the upstate metropolitan areas. The annual levels of goods producing employment are presented in Figures 5a-c, for the Buffalo, Rochester and Syracuse metropolitan areas.

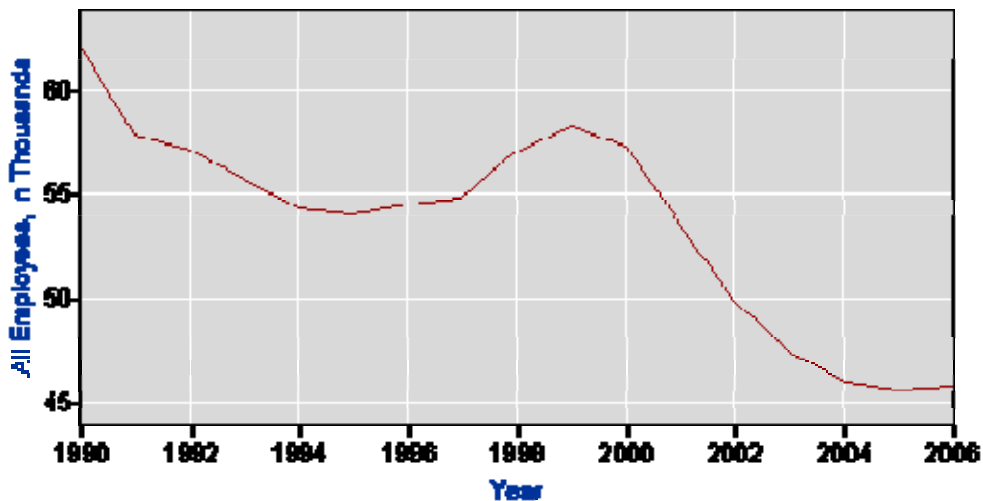
Figure 5a: Total Employment in the Goods Producing Sector Buffalo MSA: 1990 - 2006



**Figure 5b: Total Employment in the Goods Producing Sector
Rochester MSA: 1990 - 2006**



**Figure 5c: Total Employment in the Goods Producing Sector
Syracuse MSA: 1990 - 2006**



For the metropolitan areas of upstate New York, the decline of goods producing employment since the mid-1990s has continued. Every region has lost a substantial number of goods producing jobs, though Syracuse has seemingly found a bottom at around 47,000 goods producing jobs. For the other upstate areas, there is no indication that this trend has been reversed in 2007. From July 2006 to July 2007 there was a 2.6% decline in goods producing employment in the Buffalo metropolitan area, which was exceeded by the 3.1% decline in the Rochester area.

In the Buffalo metropolitan area, some of the uncertainty surrounding the automobile industry discussed last year has been resolved with the dramatic employment and

earnings reductions surrounding the decision by American Axle to leave Buffalo. Current labor negotiations may leave those remaining employees in the local automobile industry with lower hourly earnings than they have traditionally had. We may actually see a decline in nominal earnings per worker in the near future, rather than the declines in real earnings per worker that have occurred a number of times over the last 25 years. One should also expect a continuation of the decline in nominal earnings per worker relative to the nation as a whole that began over a decade ago in the upstate regions. It is unlikely that the jobs lost in the goods producing sector will ever be replaced by jobs that pay comparable wages and fringe benefits.

The continuous decline in the goods producing sector is an important contributing factor in the decline in earnings per worker relative to the rest of the nation. Based on BEA data, workers in the Buffalo metropolitan area earned 14.3% less than the national average in 2005. Per capita income was 7.7% lower than the rest of the nation and transfer payments as a percent of total income in the region were 35% higher than the national average. This high dependence on government transfer payments is probably linked to the aging population within the region. For years this newsletter has discussed the flight of the many of our best and brightest young people from the upstate metropolitan areas to the rest of the country. The ever increasing gap in earnings per worker here, compared to the remainder of the country, explains the economic opportunities that have been an attractive force. The result of these trends is an aging population that brings Social Security and other transfer payments into the region. The latest issue of the *Upstate New York Regional Review* written by Richard Deitz and Ramon Garcia of the Federal Reserve Bank of New York indicates that 15.8% of the population in the Buffalo metropolitan area is aged 65 or older. That compares to 11.4% for the U.S. population. While not as old as Buffalo, both Rochester and Syracuse have elderly percentages that are higher than the U.S. average. In relative terms we are getting older and poorer.

Additionally, it has been shown in this newsletter as well as in other publications that the Buffalo metropolitan area ranks near the bottom as a destination for immigrants. While one might understand the reluctance of people who have enjoyed the growth that has occurred along the coasts and in the southern region of the United States to move to Buffalo, it is hard to understand why the poor from the rest of the world have ignored Buffalo as a final destination. While we have been declining in relative terms compared to the rest of the country, we remain a region with per capita income and earnings per worker that exceed most of the rest of the world.

In addition to high income potential for immigrants from the rest of the world, the ratio of median housing value to median household income is very low, one of the reasons why the sub-prime mortgage has not had many direct effects on the region. Perhaps our economic development efforts should be directed towards individuals from Africa, Asia and Europe who want to bring their capital, both human and financial, to a place that combines high earnings potential and relatively low land and structural costs.

The full text and internet links for this newsletter are available at <http://www.canisius.edu/wnyeconomicnews>.

NATIONAL, STATE & LOCAL BUSINESS INDICATORS

NATIONAL INDICATORS	% change				
	2006:II - 2007:II				
	2006:II	2006:IV	2007:I	2007:II	2007:II
Real GDP (billions of chained 2000\$) (1)(a)	11,306.7	11,395.5	11,412.6	11,523.8	1.9
US Personal Income (billions of \$)	10,915.5	11,200.2	11,469.2	11,604.9	6.3

	% change				
	Aug-06 - Aug-07				
	Aug-06	Jun-07	Jul-07	Aug-07	Aug-07
Leading Indicators Index (1996=100) (4)(a)	137.0	137.7	138.7	137.8	0.58
Consumer Price Index (1982-84=100) (2)	203.900	208.352	208.299	207.917	1.97
Exchange Rate Canadian/US \$ (3) (b)	90.5	93.9	93.7	94.7	4.67
10 Year Treasury Note Yield (%) (3) (b)	4.74	5.03	4.77	4.55	-0.19
3 Month Treasury Bill Yield (%) (3) (b)	5.03	4.82	4.96	4.01	-1.02
S&P 500 Stock Index (3) (b)	1,303.8	1,503.4	1,455.3	1,474.0	13.05
Dow-Jones Industrial Average (3) (b)	11,381.2	13,408.6	13,212.0	13,357.7	17.37

LABOR MARKET TRENDS (2)

Nonag Civilian Employment					
US (1000's)(a)	136,438	137,973	138,041	138,037	1.17
NY State (1000's)(a)	8,615.8	8,695.3	8,708.8	8,702.4	1.01
WNY (1000's)	544.9	555.4	548.5	547.2	0.42
Unemployment Rate (%)					
US (a)	4.7	4.5	4.6	4.6	-0.1
NY State (a)	4.4	4.7	4.9	4.9	0.5
WNY	4.9	4.6	4.9	4.5	-0.4
Ave. Weekly Hours in Mfg. US (a)	41.3	41.4	41.3	41.3	0.00
Ave. Weekly. Earnings in Mfg. US \$(a)	695.08	714.56	713.66	714.08	2.73
Ave. Weekly Earnings (1982\$(a)	276.31	281.16	280.78	282.13	2.11

WNY EMPLOYMENT BY SECTOR (1000's) (2)

Natural Resources, Mining & Construction	22.3	21.2	21.6	21.8	-2.24
Manufacturing	62.5	60.6	59.6	59.5	-4.80
Trade, Transportation & Utilities	102.5	102.9	101.9	101.9	-0.59
Durable Goods	38.0	36.8	35.7	35.5	-6.58
Finance Activities	35.5	36.3	36.6	36.8	3.66
Service Providing	460.1	473.6	467.3	465.9	1.26
Government	88.6	96.4	91.4	89.3	0.79

(1) US Dept. of Commerce

(2) US Dept. of Labor

(3) Wall Street Journal

(4) The Conference Board

(a) Seasonally Adjusted

(b) End of month data