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The U.S. economy continues to be mired in the worst recession since the Great Depression of the 1930's. The rate of decline of real GDP has moderated significantly from its 6.4% rate during the first quarter of 2009. It seems likely that if current trends continue that the economy will begin growing again at some point during the next three quarters. Home prices in the 20 largest metropolitan areas in the U.S. halted their decline during the summer and show some signs of stabilization. There are mixed feelings about the risks associated with deflation and the long term inflationary consequences of the fiscal and monetary stimulus used in an attempt to avert a more serious and dangerous recession. Since the Buffalo area economy has not fully recovered from the 2001 recession, it will in all likelihood fall more deeply into recession, stay longer and recover less fully than the nation as a whole, as it has consistently since 1975. The full text and internet links for this newsletter are available at http://www.canisius.edu/wnyeconomicnews.

The National Economic Outlook

The recession that began in December 2007 has been the most severe downturn since the Great Depression of the 1930's in terms of duration and magnitude. Since final estimates for real GDP during 2009:Q2 show the economy contracting at .7 percent, the duration of this recession presently stands at 18 months. In terms of magnitude, real GDP has contracted by 3.83% from its peak in 2007:Q4. Real GDP growth rates since the first quarter of 2006 are shown in Figure 1 (www.bea.gov). It is important to note that the rate of decline has moderated significantly from its 6.4% decline during the first quarter of 2009. It seems likely that if current trends continue, the economy will begin growing again at some point during the next three quarters.

Since the present recession had its origins in the housing market, it is encouraging to see this market stabilizing. The closely watched Case-Shiller index of home prices in the 20 largest metropolitan areas in the U.S. halted its decline during the summer quarter, rising by 1.1% in June 2009 and by 1.6% in July 2009. The index peaked in May 2006 and exhibited constant declines each month through May 2009. This turn-around plays an important part in halting the huge decline in household wealth brought about by the financial crisis and the burst housing bubble, since wealth is an important

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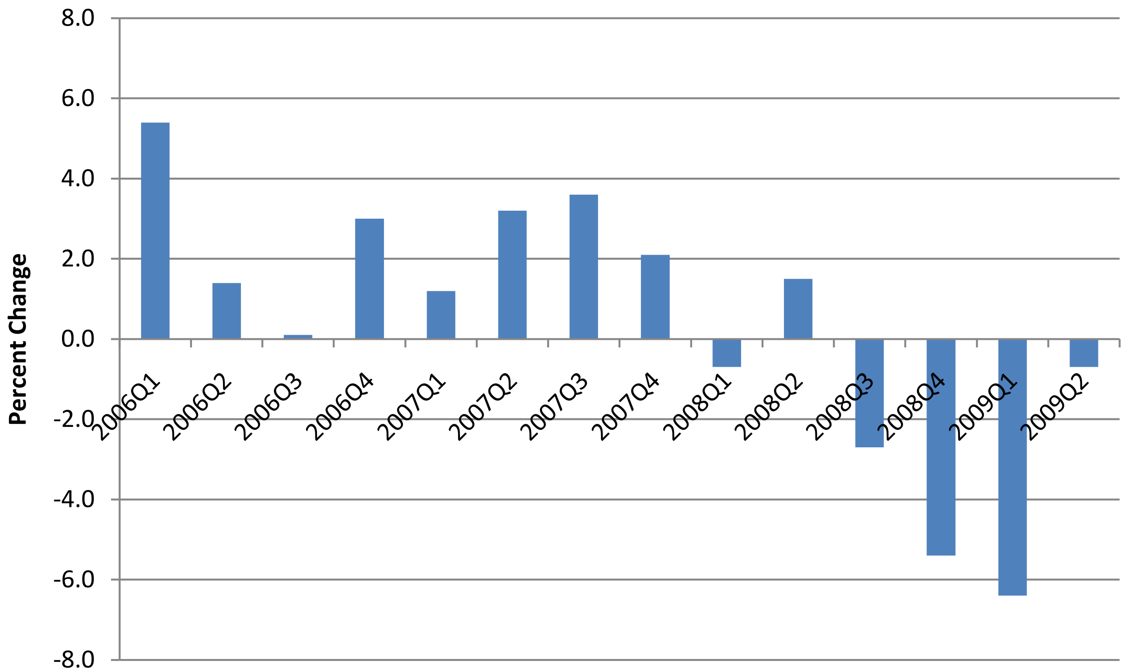
Figure 1. Real GDP Growth Rates: 2006:Q1 - 2009:Q2



determinant of personal consumption expenditures, which account for approximately 70% of GDP.

Another positive sign for a return to growth is the recovery in the equity markets. Over the present cycle, the S&P 500 index of common stocks declined by almost 57% from its peak October 2007 to its trough in March 2009. The index has recovered nicely since reaching its nadir but still remains 34% below its October 2007 peak. Since equity prices are thought to be a leading indicator of economic activity, this development supports our view that the economy will soon return to economic growth.

Labor markets (see Figure 2) have continued to deteriorate. The unemployment rate stands at 9.8% in September 2009, its highest level in 26 years. The payroll employment data shows that more than 7.2 million jobs have been lost since the employment peak in December 2007 (www.bls.gov). It is likely that the unemployment rate will continue to rise and payrolls will continue to shrink over the remainder of 2009.

The recession has had a dramatic impact on the Consumer Price Index (see Figure 3). The economy began to experience deflation, a negative rate of change in the CPI, in March of this year. The rate of deflation, which accelerated through July, moderated its pace in August and September. Inflation will likely return when economic growth returns. Conversation has already begun among analysts about how and when the Federal Reserve will begin to drain reserves out of the financial system. The unprecedented expansion of the Fed’s balance sheet through purchases of non-traditional assets such as mortgage backed securities and commercial paper will surely have to be reversed to prevent the inflation rate from accelerating.

Figure 2: US Payroll Employment & the Unemployment Rate

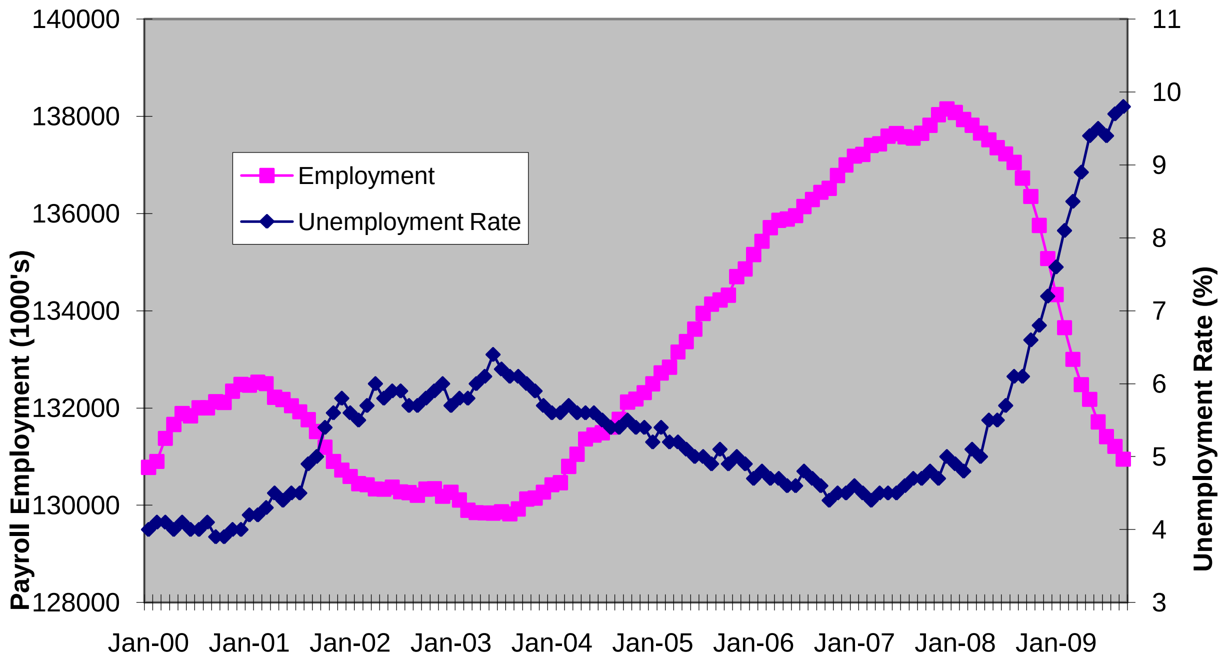
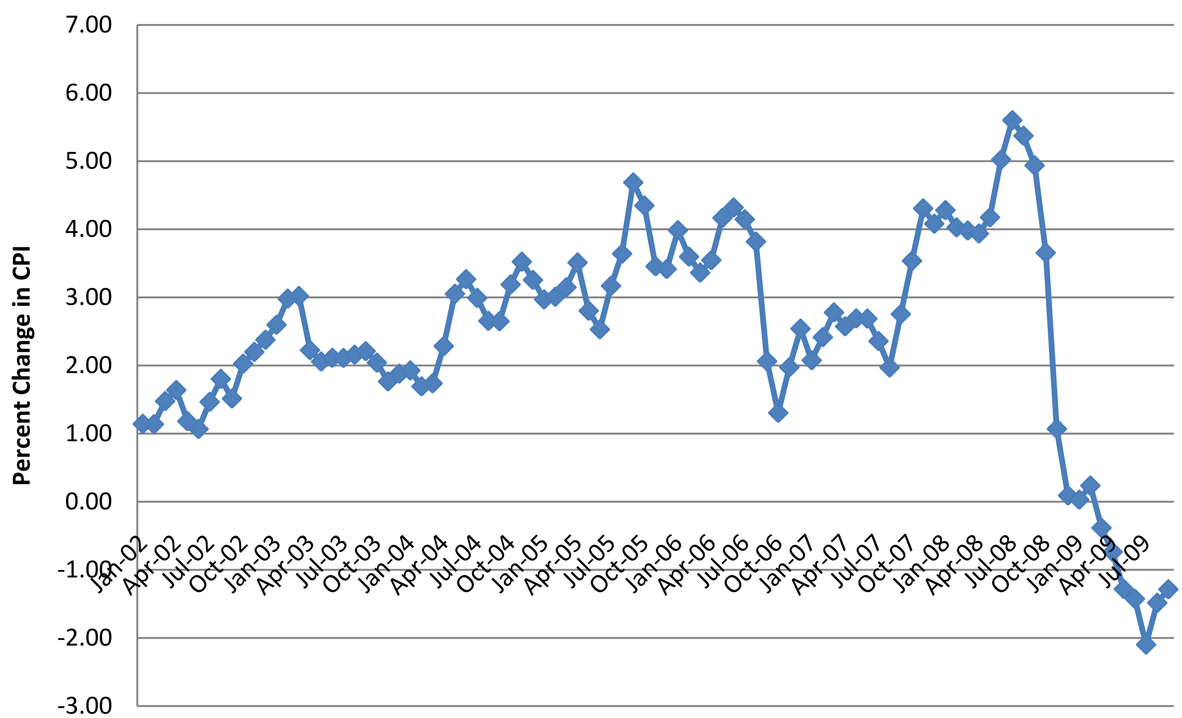


Figure 3. CPI Inflation Rates 2002-2009 (Twelve Month Percent Change)



The Economic Outlook for the Buffalo Region

As presented in Table 1, the Buffalo metropolitan area has consistently lost population since 1980. Although per capita income in the area has risen since 1980, it has become a smaller fraction of the national average over the period. Wage and salary employment has yet to return to its level prior to the 1991 recession or even the 2001 recession (see Figure 4a). If past history is an indicator of the future, the long term impact of the 2008-2009 recession on total employment in the region is likely to be severe. The average wage per worker as a fraction of the U.S. average has declined significantly over the past three decades, falling from 101% of the US average in 1980 to 87.3% in 2007. The causes of the relative decline in wages and income are

Table 1. U.S & the Buffalo Metropolitan Area: 1980 - 2007

	1980	1990	2005	2006	2007
Population					
U.S.	227,224,719	249,622,814	295,560,549	298,362,973	301,290,332
Buffalo MSA	1,241,275	1,190,943	1,140,309	1,131,989	1,126,513
Per capita personal income as a % of US	98%	97%	92%	91%	91%
Wage & salary employment					
U.S.	97,894,000	117,594,000	140,973,000	143,321,000	144,815,000
Buffalo MSA	521,797	561,444	558,105	556,744	557,126
Average wage per job					
U.S.	$13,999	$23,326	$40,188	$42,009	$43,889
Buffalo MSA	$14,138	$22,463	$35,319	$36,961	$38,294
Buffalo wage per worker as % of US average	101.0%	96.3%	87.9%	88.0%	87.3%

generally rooted in the unabated decline in the high wage goods producing sector (see Figure 4b). Few respectable economists would expect a reversal of this trend.

The region has become increasingly dependent on its financial services industries to make up for declines in the goods producing sector. While continuing problems in the national financial markets could have had a direct impact on the local economy, employment in financial activities remained virtually constant between August 2008 and August 2009. This did not hold for total employment in the region. Since August 2008, total employment has declined by 13,800 jobs while goods producing employment has declined by 7,400 jobs. While not apparent in Figure 4c, the service sector also declined over the last year with employment falling by 6,400 jobs.

Figure 4a: Total Employment Buffalo MSA: 1990 – 2008

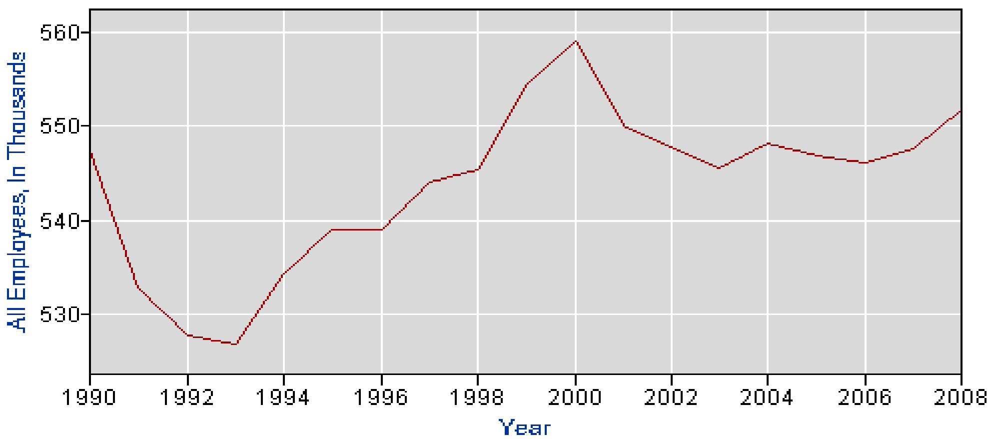


Figure 4b: Total Employment in the Goods Producing Sector Buffalo MSA: 1990 - 2008

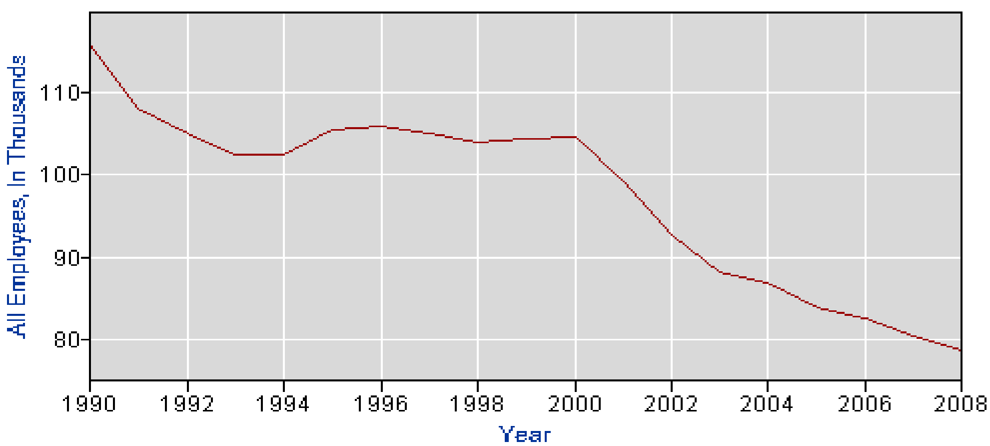
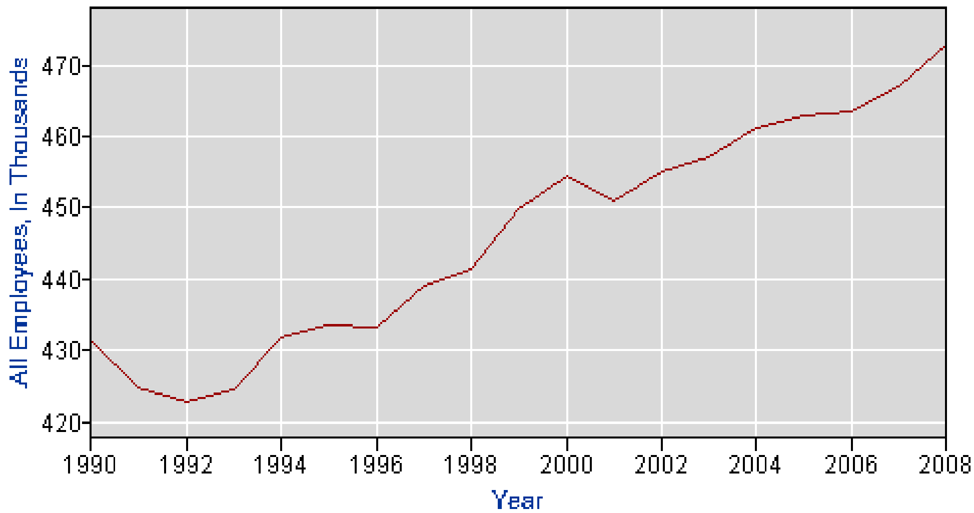


Figure 4c: Total Employment in the Service Providing Sector
Buffalo MSA: 1990 – 2008



While much has been made of the lag of employment growth in the early stages of economic recoveries, durable goods production has historically been very sensitive to the business cycle. Perhaps the best that the region can hope for is a reduction in the long term rate of decline that has occurred in the goods producing sector as the current national recession comes to an end.

It is highly unlikely that this region will lead the nation into recovery. Specific areas of concern beyond the long term decline of the region include the end of the federal stimulus packages that were designed to support state and local government activity as their tax and fee based revenues declined during the contraction. The impact may be seen in general purpose and school district budgets which have been negatively impacted by a decline in sales taxes and a stagnant property tax base. When this is combined with reductions in state aid and the end of the federal transfers to the states, one could expect higher tax rates, reduced budgets and a reduction in the compensation of public sector employees. Of special note will be the desire of the state to recover lost pension funds by shifting more of the revenue raising responsibility to local governments. Additionally, county responsibility for Medicaid and other social services may increase if state revenue raising capacity does not increase.

NATIONAL, STATE & LOCAL BUSINESS INDICATORS

NATIONAL INDICATORS	2008:II	2008:IV	2009:I	2009:II	% change 2008:II - 2009:II
Real GDP (billions of chained 2005$) (1)(a)	13,415.3	13,141.9	12,925.4	12,901.5	-3.8
US Personal Income (billions of $)	12,292.9	12,233.5	11,952.7	11,971.8	-2.6

	Sep-08	Jul-09	Aug-09	Sep-09	% change Sep-08 - Sep-09
Consumer Price Index (1982-84=100) (2,c)	218.783	215.351	215.834	215.969	-1.29
Exchange Rate Canadian cents/US $ (3) (b)	106.410	107.750	109.510	107.070	0.62
10 Year Treasury Note Yield (%) (3) (b)	3.83	3.56	3.40	3.31	-0.52
3 Month Treasury Bill Yield (%) (3) (b)	0.92	0.18	0.15	0.10	-0.82
S&P 500 Stock Index (3) (b)	1,164.74	987.48	1,020.62	1,057.08	-9.24
Dow-Jones Industrial Average (3) (b)	10,850.66	9,171.61	9,496.28	9,712.28	-10.49
LABOR MARKET TRENDS (2)					
Nonag Civilian Employment					
US (1000's)(a)	136,732	131,411	131,210	130,947	-4.23
NY State (1000's)(a)	8,818.8	8,649.2	8,645.4		-0.021
WNY (1000's)	557.0	538.2	539.0	540.2	-0.025
Unemployment Rate (%)					
US (a)	6.1	9.4	9.7	9.8	3.7
NY State (a,c)	5.8	8.6	9.0		3.3
WNY	5.9	8.6	8.3	8.4	2.5
Ave. Weekly Hours in Mfg. US (a)	40.50	39.9	39.9	39.8	-0.7
Ave. Weekly. Earnings in Mfg. US ($)(a)	721.31	728.97	728.18	728.74	1.03
Ave. Weekly Earnings (1982$)(a,c)	275.99	284.48	283.98	282.76	2.45
WNY EMPLOYMENT BY SECTOR (1000's) (2)					
Natural Resources, Mining & Construction	23.4	21.0	21.6	21.0	-0.103
Manufacturing	58.2	53.3	53.5	53.5	-0.081
Trade, Transportation & Utilities	103.9	99.0	98.7	99.3	-0.044
Durable Goods	35.4	31.6	31.8	31.7	-0.105
Finance Activities	32.8	32.8	32.8	32.4	-0.012
Service Providing	475.4	463.9	463.9	465.7	-0.020
Government	93.9	91.0	90.4	91.1	-0.030

(1) US Dept. of Commerce — (a) Seasonally Adjusted
(2) US Dept. of Labor — (b) End of month data
(3) Wall Street Journal — (c) rate of change is Aug-08 - Aug-09