Western New York ECONOMIC NEWS
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Western New York has historically lagged the rest of the nation in recovery from recession, though it is difficult to separate the secular decline of the region from the cyclic variations around the long-term downward trend. Since the appearance of the last issue of this newsletter, the BEA earnings report for the year 2001, Census information, and a revised New York State Department of Labor report have been released. These data give every indication that the past is indeed a precursor to the economic future of Western New York. Employment declines in the region preceded those for the nation. Especially hard hit has been durable goods employment, which has had some of the highest levels of earnings per worker in the region. Hopes of escaping the past patterns of cyclical decline seem to have been misplaced. The region may indeed fall deeper into recession and recover less fully than the rest of the nation. The challenge to the economic development community is to help change the future, by focusing on an expansion of the economic base with new high earning jobs. An increase in productivity that would result from investment in the region for new plant and equipment could reduce local production costs and help avoid the continued pattern of long-term decline following the end of the current recession. The full text and supporting documents of this newsletter appear on the Internet under the address http://www.canisius.edu/wnyeconomicnews.

The National Economic Outlook

Although the national economic contraction of 2001 may now be history, the U.S. economy has been mired in a slow growth recovery. Real GDP growth rates since 2000:Q1 appear in Figure 1. Advance estimates of 2003:Q1 real GDP shows the growing at an annual rate of only 1.6%, after annual rates of 5.0%, 1.3%, 4.0%, and 1.4% during the four quarters of 2002. Reductions in expenditures on consumer durables over the past two quarters and weak business investment, have contributed to the slow growth recovery. This represents a significantly change in consumer behavior as consumers were largely responsible for preventing the 2001 recession from becoming more severe. The level of uncertainty concerning the present condition of the national economy is so high that the National Bureau of Economic Research (NBER) has yet to determine the date of the end of the last recession and will only do so when it concludes that a hypothetical subsequent downturn would be a separate recession, not a continuation of the past one. The NBER's main concern has been that the U.S. economy continues to experience growth in output and income without any significant growth in employment.

Although a double dip recession may yet be avoided, economic growth has not been substantial enough to increase employment and reduce the unemployment rate (see Figure 2). Since the peak in payroll employment in March 2001, the economy has shed more than 2.1 million jobs. The unemployment rate has risen steadily from 4% in January 2000 to its present 6% level. We do not project significant new jobs to be added or the unemployment rate to fall unless the GDP growth rate increases substantially from its current anemic rate.

Figure 1: Real GDP Growth Rates

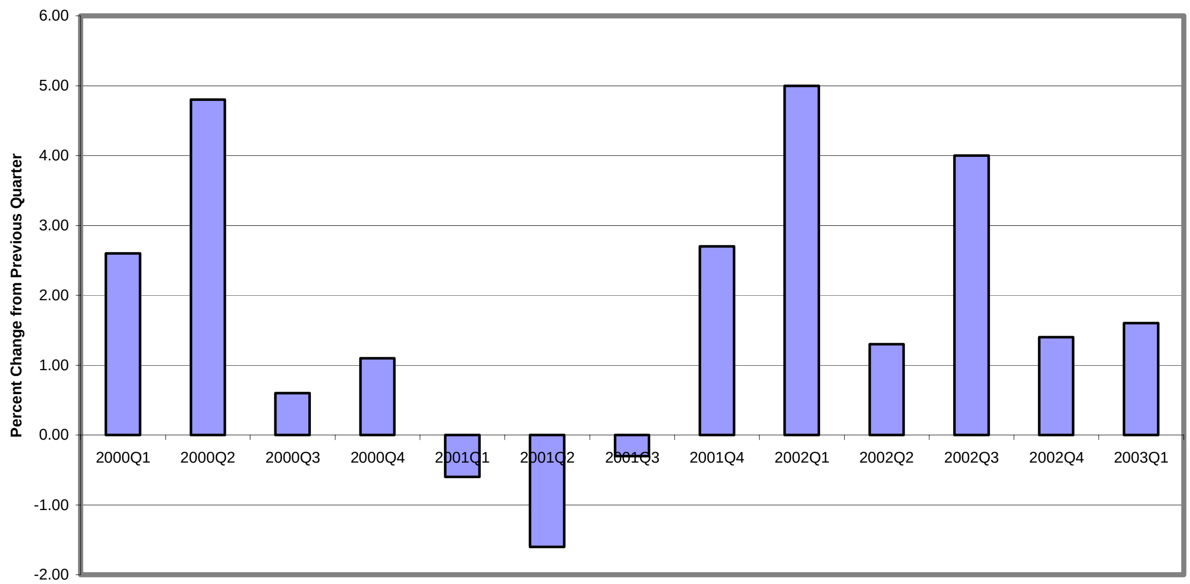
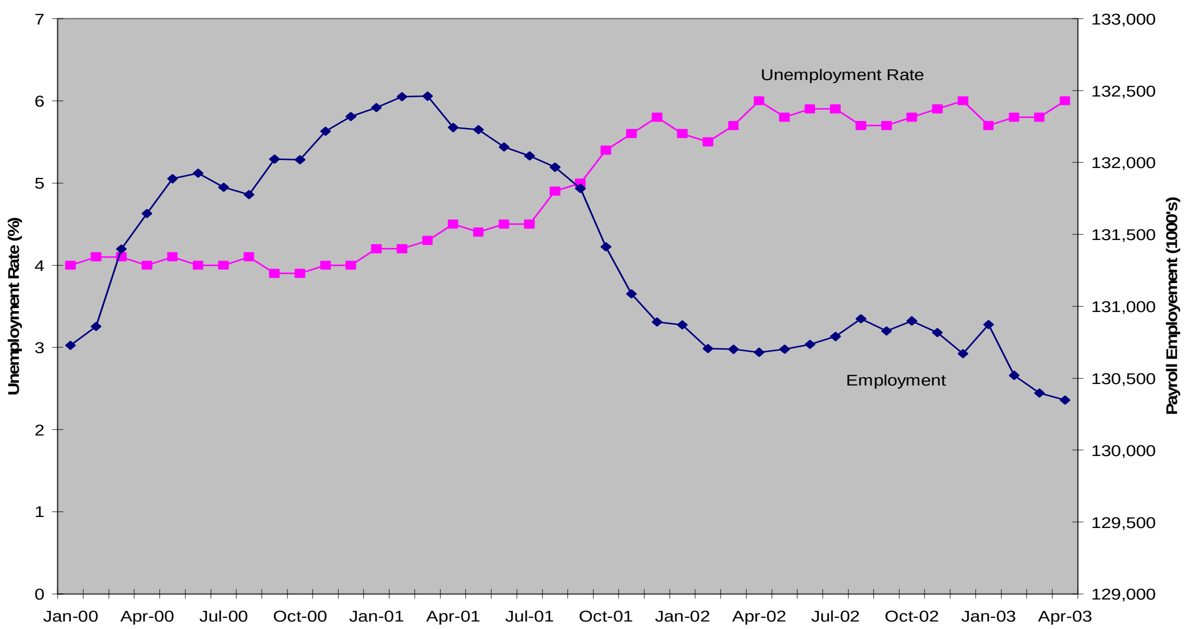


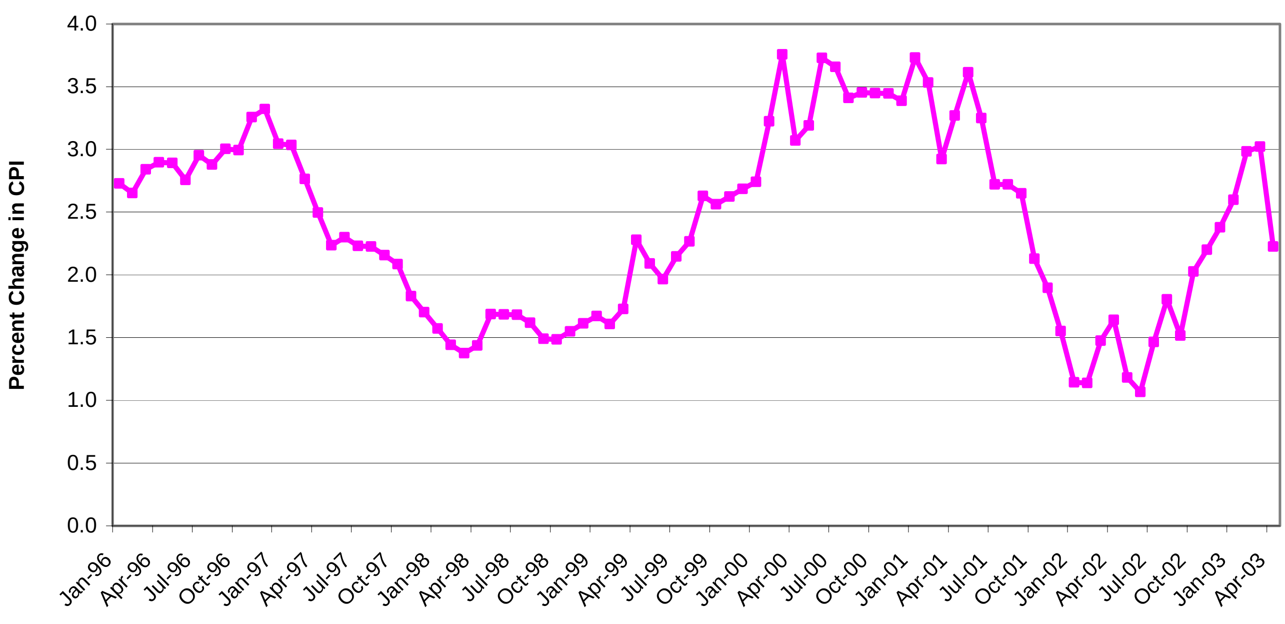
Figure 2: U.S Payroll Employment and Unemployment Rate



There has been a great deal of recent concern expressed over the prospect of deflation and its consequences. The specter of the Japanese economic malaise has weighed heavily on the thinking of U. S. policymakers, particularly at the FED. The Japanese inflation rate has been negative over the past four years while their real GDP has fallen or grown at very low levels over the past decade. Typically, deflation occurs when an economy experiences severe and prolonged recessions. The last episode of deflation in the U.S. occurred during the Great Depression of the 1930's. The April 2003 CPI decline of .3% will likely reinforce concern over the prospect of deflation. Given the volatility in the CPI, it's important to view US inflation in a larger context. Figure 3 shows the inflation rate based on 12 month changes in the CPI. The 2001 recession caused a significant drop in the rate of inflation from 3.5% to approximately 1% in early 2002. The rapid rise in energy prices that occurred prior to the Iraqi war caused the inflation rate to trend upward to 3%. The end of hostilities in Iraq has led energy prices to fall and this in turn has caused the reduction in the April 2003 CPI. Barring entry into another recession, we do not expect the inflation rate to turn negative.

Since the Fed announced a decrease in the federal funds rate target in late 2002, they have left the federal funds rate target unchanged with a bias toward reducing rates should economic conditions sour. Low inflation expectations and an ample supply of bank reserves have caused interest rates to be at their lowest levels in 45 years. Three month US Treasury security yields are at 1.05%, 71 basis points below their level of a year ago. Ten year US Treasury note yields are at 3.53%, 128 basis points below their April 2002 levels. These low rates have helped keep the residential housing market healthy. Equity markets have recovered nicely coming off their February lows. The Dow-Jones industrial average has added 10% while the S&P 500 index is up almost 12% over this time frame. Since the stock market is often taken as a predictor of future economic activity, it seems to be predicting an upswing in economic growth.

Figure 3: US CPI Inflation Rate (12 Month Percent Change)



The Economic Outlook for the Buffalo Region

The Bureau of Economic Analysis of the US Department of Commerce http://www.bea.gov released revised personal income data for the Buffalo region in May 2003. The data and growth rates for the Buffalo area, the U.S., and New York State, appear in Table 1.

Real personal income growth in the Buffalo area dropped by 1.06% in 2001, as the national economy entered recession. Real personal income growth in New York State was nil in 2001 and -.72% in 2002. Even though the US economy was in recession during 2001, real U.S personal income grew by .46% and followed with a 1.30% growth rate in 2002.

These Buffalo area growth rates are below both those of the nation as a whole and New York State. In fact, while the national economy soared during the decade of the 1990's, the Buffalo region failed to share in this growth. Furthermore, there appears to be no local economic developments on the horizon that suggest a reversal in the region's fortunes over the next decade. The economic performance of the region during 2003 depends largely upon the robustness of the national recovery.

Historic growth rates of real personal income in the US and Buffalo are used to generate the forecast of the change in personal income for Buffalo in 2002 and 2003 (**bold face**). This forecast assumes that US real personal income will grow by 3.5% in 2003. The growth rate of real personal income in the Buffalo area has been strongly correlated with the growth of US real personal income over the period 1980-2001 (Pearson correlation coefficient = .92). Each 1%

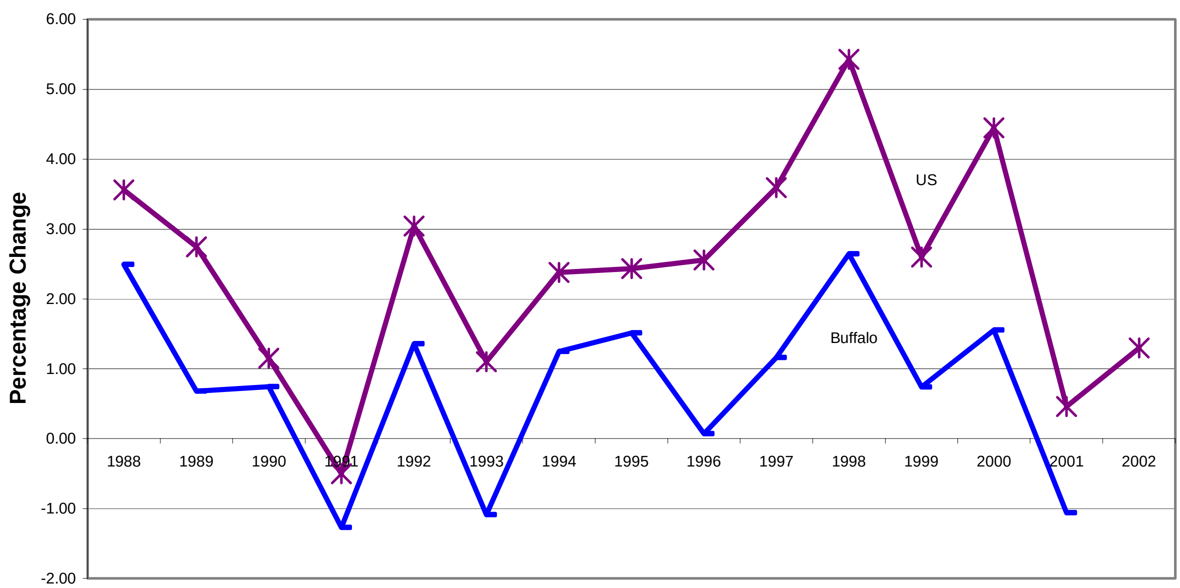
TABLE 1

Real Personal Income Growth Rates: Buffalo, US, New York State

YEAR	BUFFALO PERSONAL INCOME (MILLIONS OF 2001$)	BUFFALO PERCENT CHANGE	US PERCENT CHANGE	NEW YORK STATE PERCENT CHANGE
1993	30,027.5	-1.09	1.10	-1.09
1994	30,401.3	1.25	2.38	0.53
1995	30,860.5	1.51	2.44	2.24
1996	30,881.6	0.07	2.56	2.50
1997	31,239.7	1.16	3.59	1.91
1998	32,065.7	2.64	5.43	5.02
1999	32,301.3	0.73	2.60	2.13
2000	32,802.1	1.55	4.45	4.51
2001	32,454.3	-1.06	0.46	0.00
2002		**-0.44**	1.30	-0.72
2003		**1.20**		

growth in US real personal income has been met by a .95% growth in Buffalo area real personal income. The historic relationship between these growth rates is shown in Figure 4. The cyclical slowdown in the growth of personal income has historically been felt more intensely in the local economy. If past patterns hold then the Western New York economy will take longer to recover, and recover less fully than the nation as a whole.

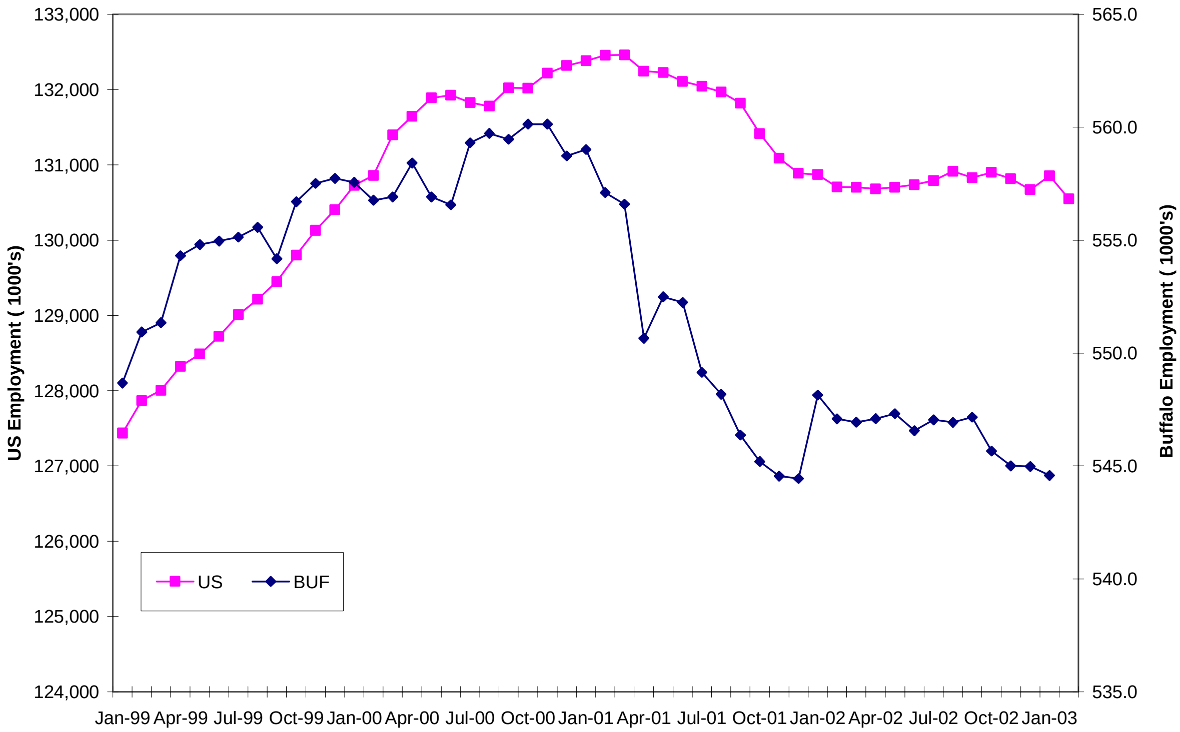
Figure 4: Real Personal Income Growth Rates: US v. Buffalo



Much was made at the turn of the century about the changing nature of the Buffalo economy and the possibility that the new industrial composition of the region would insulate it from the wild cyclical swings that accompanied past national recessions. Indeed, Buffalo has lost significant amounts of its manufacturing employment base over the last two decades, but it appears even though these employment opportunities have been replaced with lower wage non-manufacturing jobs, the local economy is still susceptible to the changes in the cyclically sensitive durable goods sector. It is clear from Figure 4 and the data presented in Table 1, that changes in local income are still tightly linked to changes on the national scene.

From Figure 5 it can be seen the Buffalo metropolitan area has again led the nation into recession just as it has in every recession since 1974. U.S. employment peaked in March of 2001 signaling the onset of the nations latest recession while the Buffalo employment peak occurred in November of 2000. The ultimate length and severity of this recession on the Buffalo economy will not be know until a bottom has been reached. There is no definitive reason as yet to believe that a bottom has been reached. Unfortunately, a secondary factor may affect this regions economy. Local firms that have not re-invested in new plant and equipment in the Buffalo region may choose to invest in other regions. When the current national economic downturn ends, investment decisions will be implemented. This may well lead to a continuation of the long term investment trend away from Western New York. Without the commitment that comes from substantial investment in new plant and equipment, the long term presence of existing firms in the area is in doubt. Demands of local firms for substantial tax relief on an

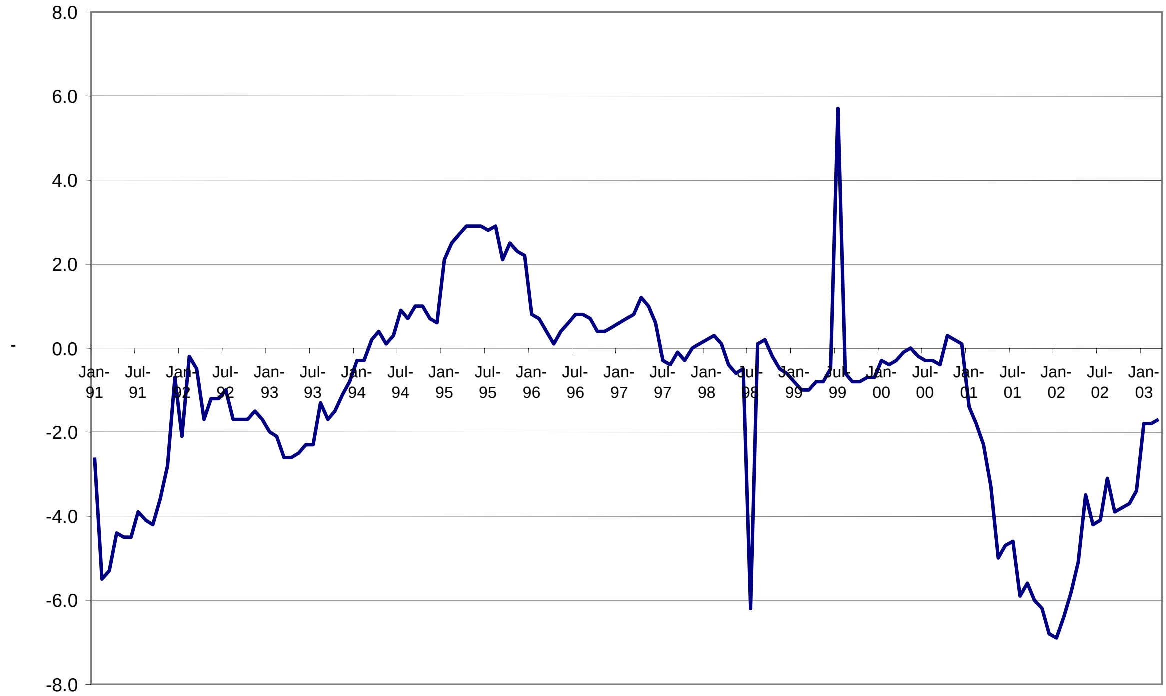
Figure 5 US - Buffalo Nonfarm Employment: January 1999 - February 2003



individual basis should be considered in terms of a correspondingly high commitment of investment in new plant and equipment that will make Western New York workers more productive, while lowering the cost of producing goods and services in the region. Without such investment commitments, it is difficult to conclude that this region's economic development policy is successful. The failure of the Western New York economy to recover from each recession since 1974 as fully as the rest of the nation is a reflection of plant and firm re-location. To date, there has been nothing to indicate that this pattern will be broken.

The durable goods employment information from the New York State Department of Labor helps complete the picture of the depths of the current recession in the Western New York economy. The decline in durable goods manufacturing employment from its level twelve months previous seems to be easing, but one must keep in mind that the March 2003 decline of nearly 2% is being compared to employment in March of 2002. By that time, the region had already been in recession for nearly 18 months. The effect of the decline in durable goods employment is intensified by the fact that employees in this sector have historically enjoyed some of the regions highest earnings per worker. As durable goods employment declines, its economic impact on the region is more adverse than would be the case when workers at lower wage levels lose their jobs. As has been stated in previous issues of this newsletter, it is not the number of jobs gained or lost that is of paramount importance, it is the change in the total earnings that results from these employment changes. Economic development policy should be judged solely on the basis of how it affects the level of earnings per worker in the community.

Figure 6 Durable goods employment 1990 – 2003:
% change in previous 12 months



Conclusions

The region is following its traditional path during the current recession. It has led the nation into recession, it continues to shed jobs in the important durable goods sector, and it may well fail to recover as fully as the rest of the nation. A reversal of the pattern can only be expected after we see a commitment to the region in the form of substantial investment in new plant and equipment. Only then will the outlook for the economic vitality of the region improve. Failing that, one should expect more of the same patterns of economic decline and population contraction. The claims of the economic development community that the region has undergone a transformation that will insulate it from the volatility of the business cycle seem unfounded. The region is in long term economic decline. When this national recession concludes, we can only wonder how much longer the Western New York economy will continue to decline. This region missed much of the expansion of the 1990's. Without a significant restructuring of its economic base, it may miss out on the recovery that will occur once the current recession ends. Without significant levels of investment in new plant and equipment in the region, there is little reason to believe there will be a reversal of the long-term trend of falling behind the rest of the nation in earnings per worker and income per capita.

NATIONAL, STATE & LOCAL BUSINESS INDICATORS

NATIONAL INDICATORS	2002:I	2002:III	2002:IV	2003:I	% change 2002:I-2003:I
Real GDP (billions of chained 1996$) (1)(a)	9,363.2	9,485.6	9,518.2	9,556.0	2.1
US Personal Income (billions of $)	8,803.4	8,958.9	9,039.9	9,127.8	3.7
	Mar-02	**Jan-03**	**Feb-03**	**Mar-03**	**Mar-02 - Mar-03**
Leading Indicators Index (1996=100) (1)(a)*	112.1	111.3	110.8	110.6	-1.34
Consumer Price Index (1982-84=100) (2)	178.8	181.7	183.1	184.2	3.02
Exchange Rate Canadian/US $ (3) (b)	62.8	65.7	67.4	68.0	8.31
10 Year Treasury Bond Yield (%) (3) (b)	5.39	3.97	3.70	3.81	-1.58
3 Month Treasury Bill Yield (%) (3) (b)	1.75	1.17	1.19	1.09	-0.66
S&P 500 Stock Index (3) (b)	1,147.4	855.7	841.2	848.2	-26.08
Dow-Jones Industrial Average (3) (b)	10,403.9	8,053.8	7,891.1	7,992.1	-23.18
LABOR MARKET TRENDS (2)					
Nonag Civilian Employment					
US (1000's) (a)	130,701	130,873	130,520	130,396	-0.23
NY State (1000's) (a)	8,457.3	8,417.5	8,400.5	8,390.2	-0.79
WNY (1000's)	541.5	534.7	538.3	540.5	-0.18
Unemployment Rate (%)					
US (a)	5.7	5.7	5.8	5.8	0.10
NY State (a)	6.0	6.3	6.1	6.0	0.00
WNY	6.5	6.8	6.4	5.8	-0.70
Ave. Wkly. Hours in Mfg. WNY	42.4				
Ave. Wkly. Earnings in Mfg. WNY ($)	800.50				
Ave. Wkly Hours in Mfg. US	41.0	40.9	40.8	40.8	-0.49
Ave. Wkly. Earnings in Mfg. US ($)	620.00	631.30	627.80	633.30	2.14
WNY EMPLOYMENT BY SECTOR (1000's) (2)					
Natural Resources, Mining & Construction	17.4	17.2	16.7	17.4	0.00
Manufacturing	72.5	70.2	70.3	70.7	-2.48
Trade, Transportation & Utilities	103.2	102.5	101.8	101.8	-1.36
Durable Goods	44.9	42.9	43.0	43.2	-3.79
Finance Activities	32.9	34.0	33.9	34.0	3.34
Service Providing	451.6	447.3	451.3	452.4	0.18
Government	94.8	91.8	93.6	94.0	-0.84

(1) US Dept. of Commerce

(2) US Dept. of Labor

(3) Wall Street Journal

(a) Seasonally Adjusted

(b) End of month data