# Western New York ECONOMIC NEWS
## Canisius College
## Richard J. Wehle School of Business

**Volume 8, Number 1** **January 2005**

On the national level growth seems to be the byword. Over the last year and a half, GDP growth rates were twice what they were over the period 2001-2003. The rise in real oil prices have abated while nominal crude prices have dropped $10 per barrel from their October highs. Inflation is not a substantial problem and the national economy is in full recovery. Locally, the story is quite different. The region continues to lose high earning goods producing jobs and replace them with service providing jobs that pay substantially less per worker. Once again the region has followed the pattern of leading the nation into recession, falling deeper, staying longer and recovering less fully. It is time for a change in the methods that we have followed to get to this position.

The full text and supporting documents of this newsletter appear on the following internet address: http://www.canisius.edu/wnyeconomicnews.

### The National Economic Outlook

Growth rates of real GDP over the past three years are shown in Figure 1. GDP grew at a 4% rate during the third quarter of 2004 (2004:Q3), after growing at annual rates of 7.4%, 4.2%, 4.5%, and 3.3% during the period 2003:Q3 - 2004:Q2 www.bea.gov. Over the past six quarters, real GDP growth has averaged almost 4.6%. This rate is more than double the anemic 2.1% real growth rate in the six quarters from the end of the 2001 recession through the first quarter of 2003 (2001:Q4 – 2003:Q1). Personal consumption expenditures, residential fixed investment, and business spending on equipment and software have been the main contributors to the acceleration in economic growth over the past year and a half.

Crude oil prices have declined almost $10 off their October high of $55 per barrel. The importance of energy market developments to the US economy were pointed out in the October 2004 issue of this newsletter. The moderation in crude oil prices removes one of the main risks to the continued growth of the economy and significantly reduces the likelihood of recession in the near future.

The Conference Board's www.conference-board.org index of leading economic indicators increased in November after declining for five consecutive months. The decline in the index has not been of sufficient duration or magnitude (1.2% decline) to signal an end to the current recovery. However, recent weakness in the index may signal lower rates of growth for real GDP in the future.

---

The Wehle School of Business at Canisius College publishes the *Western New York Economic News* as a public service to the Western New York community with research and analysis performed by faculty members:
**George Palumbo, Ph.D. - Professor of Economics & Finance** email: palumbo@canisius.edu
**Mark P. Zaporowski, Ph.D. - Professor of Economics & Finance** email: zaporowm@canisius.edu

**Figure1: Real GDP Growth Rates (2001:Q3 - 2004:Q3)**

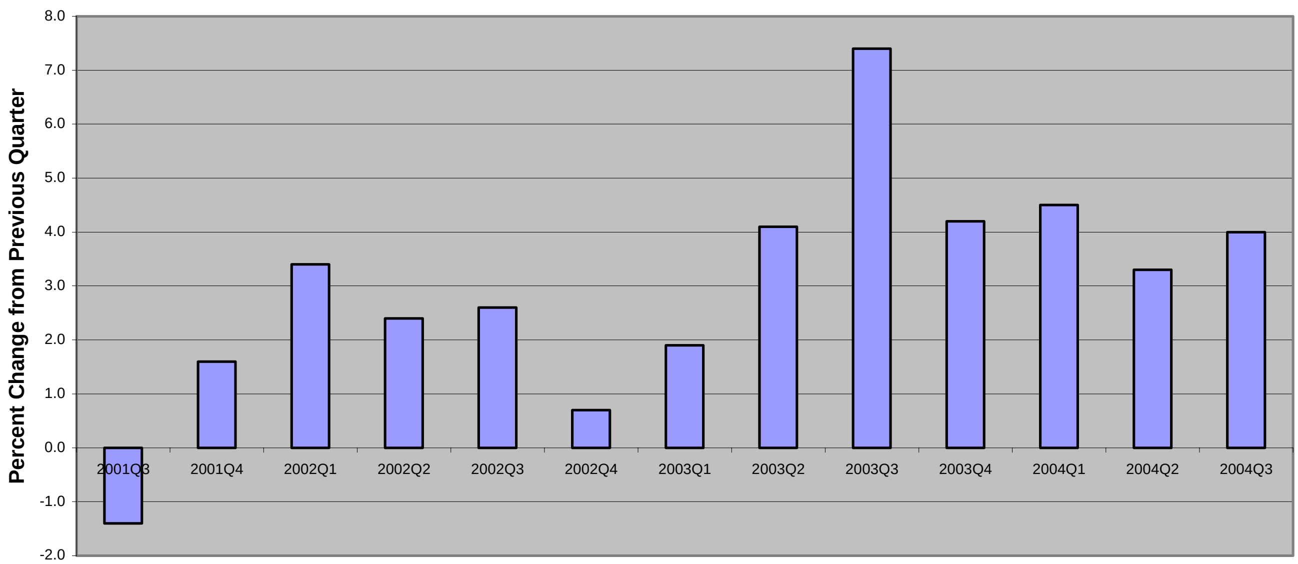



Figure 2 shows the economy-wide inflation rate based on 12-month changes in the Consumer Price Index www.bls.gov (CPI) from January 2000 to the present. Inflation has accelerated from a 1.7% rate in February 2004 to a 3.5% rate in November 2004. An aging recovery and energy prices are primarily responsible for this increase.

The labor market has continued to improve both in terms of a lower unemployment rate and in the number of new jobs added to payrolls, albeit at a slower pace than has occurred in past recoveries. U.S. payroll employment and the national unemployment rate since January 2001 are shown in Figure 3. The slow labor market recovery since the end of the 2001 recession has left the economy with 386,000 fewer jobs in November 2004 compared to the March 2001 employment peak. Normally, at this point in the recovery, we would have surpassed the previous peak in employment. The national unemployment rate stands at 5.4%.

The Federal Reserve has continued to raise its federal funds target rate by 25 basis points. These increments have occurred at each FOMC meeting since May 2004. The most recent increase occurred at the November 10 meeting. This policy has been consistent with FOMC press releases and has been widely anticipated by financial markets. The yield curve has continued to flatten with ten-year U.S. Treasury yields at 4.20% and three-month Treasury bill yields at 2.18% on December 22, 2004. Using a 3% expected inflation rate, short term real interest are negative. If the economy continues to grow, it is expected that interest rates will continue to increase.

Another development that has caught the attention of the financial press has been the rapid depreciation of the dollar. The trade weighted exchange rate with respect to other major currencies has depreciated more than 25% since February 2002. This should result in a growth of U.S. exports.

**Figure 2: CPI Inflation Rates (Twelve Month Percent Change)**

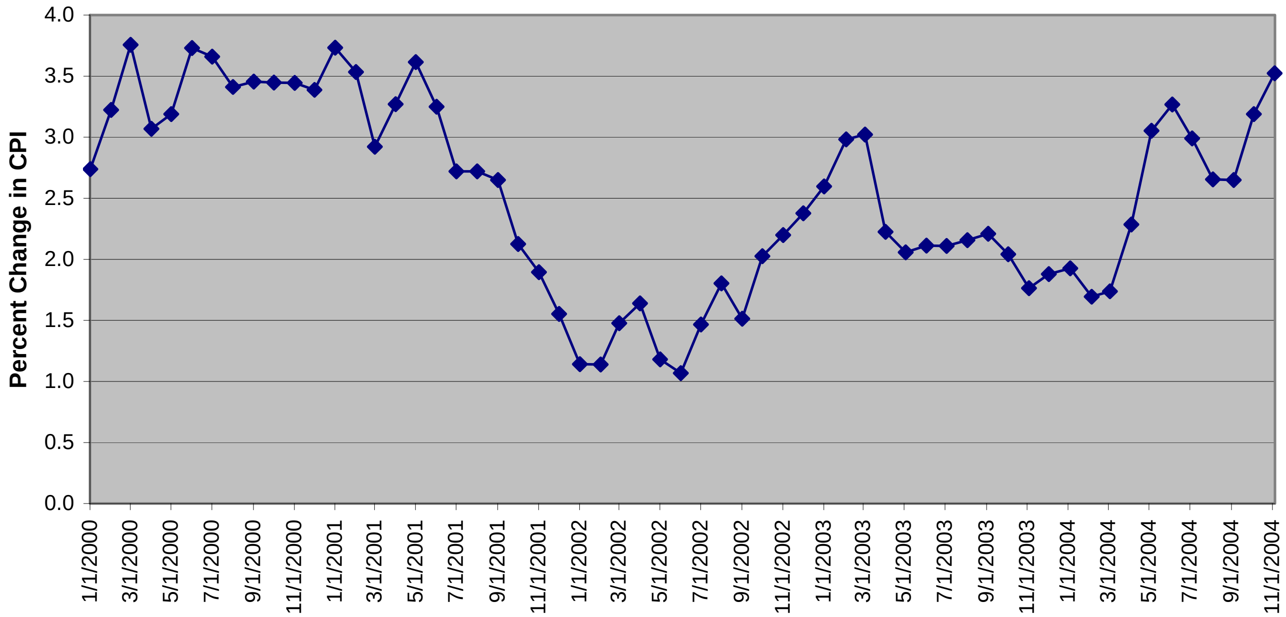
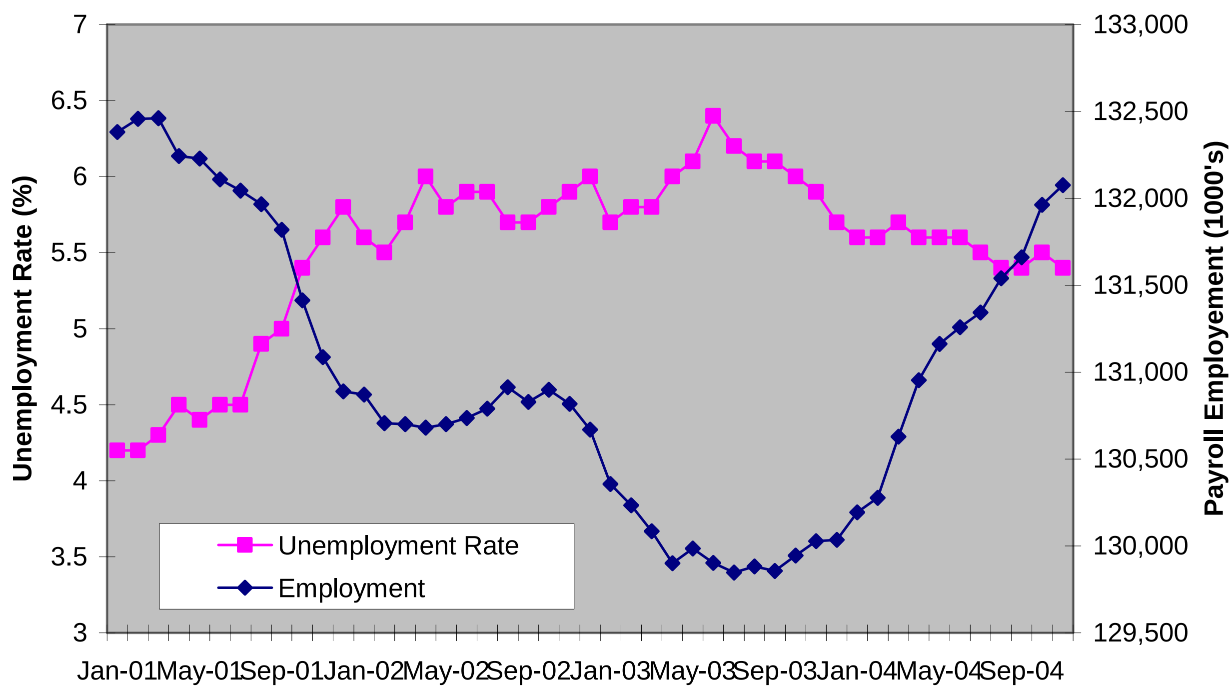


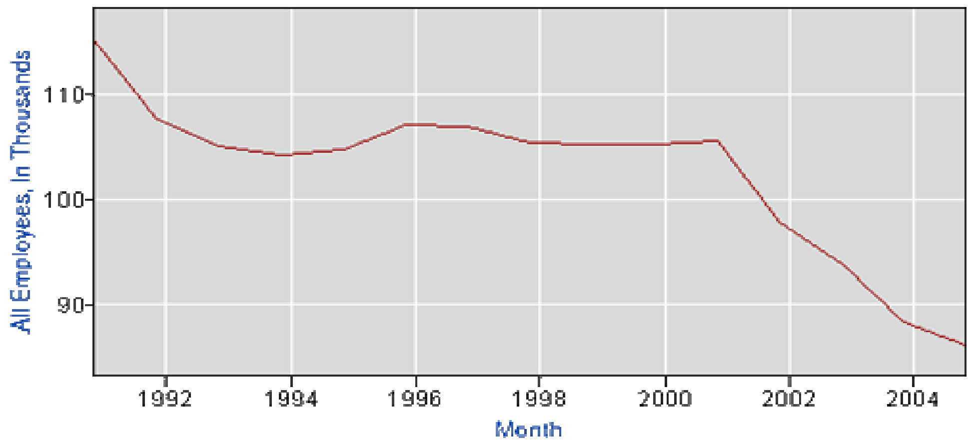

**Figure 3: U.S Payroll Employment and Unemployment Rate**



## The State of the Region's Economy

The data in Figures 4a and 4b, www.bls.gov, presents 1990 to 2003 annual data for total goods producing and service providing employment on an NAICS basis for the Buffalo metropolitan area. Even in an era of long term decline, the dramatic decreases in goods producing and durable goods employment that accompanied the recession of 2001 have been of increasing concern to local analysts.

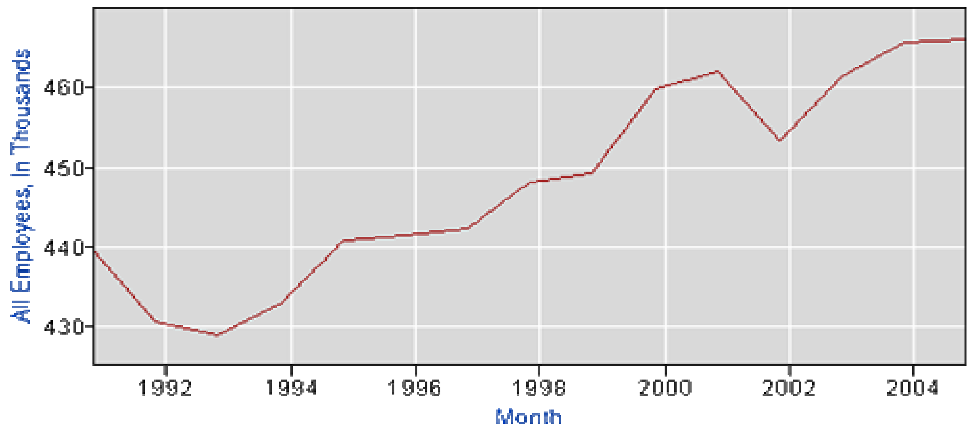
**Figure 4a: Total Employment in Goods Producing Sector**
**Buffalo MSA: November 1990 - November 2004**




Since November of 2001, over 11,500 local jobs in the goods producing sector have been lost. Approximately two-thirds of this loss was accounted for by the decline in durable goods employment. This durable goods sector lost over 9,200 jobs between 1990 and 2001, and an additional 7,000 between 2001 and 2004. Overall, the manufacturing jobs that were lost over this period paid an average annual wage of $49,000 in 2002, www.labor.state.ny.us . The manufacturing jobs that remain in Western New York generate about 50% more earnings per worker than the national average.

Over the period 1990-2004, the region gained about 26,600 service providing jobs. These jobs generated average annual earnings of approximately $28,200. According to BLS earnings estimates, service sector employment in Western New York has earnings per worker that are about equal to the national average for service sector employment. Thus, the region continues to have growth in relatively low wage sectors while it has lost substantial amounts of employment in relatively high wage sectors. This transition has accelerated within the region since the beginning of the last recession, and the region continues to fall relative to the national average in earnings per worker.

**Figure 4b: Total Employment in Service Providing Sector Buffalo MSA: November 1990 - November 2004**




The consequences of the transition are beginning to be seen by the general population. As the region falls in relative terms compared to the rest of the nation, the declining standard of living is manifested in a number of ways. The most obvious, of late, have been the strains on the fiscal stability of the local governments within the region. Much has been made about the fiscal stress the City of Buffalo has felt over the last 25 years. The city has been on the verge of bankruptcy a number of times and is unlikely in the future to have access to debt markets without enhancements like insurance, letters of credit, or state guarantees.

The city is just one of many local governments that have felt the budgetary stress that is the result of a declining population and declines in the earning capacity of the remaining residents. As incomes fall relative to the rest of the nation, levels of consumption and the value of property fall in relative terms as well. Income, consumption and property values are the drivers of own-source revenues for local governments in New York State. The property tax accounts for 41% of own-source revenue, while sales taxes and fees make up 14.6% and 29%, respectively. Whether these revenue drivers fall due to cyclical patterns or secular transformations, there is a fiscal stress placed on local governments.

From 1990 BEA data, www.bea.gov , approximately 16% of local income was generated by pensions, welfare, Social Security or other types of income maintenance programs. Over the last 14 years this number has increased to 20%. Although not all of the people receiving these government transfers are eligible for the social services that generate costs to local government, enough are to affect the level of local expenditure.

From the Governments Division of the Bureau of the Census www.census.gov/gov, it can be shown that for the year 2002, health, hospitals and social services account for 56% of Erie County government total expenditures. That is the highest proportion of any large county in New York State (New York City operates like a city, a county, and the state's largest school district, so health, hospitals and social services account for only 22% of New York City's total expenditures.) Much has been said lately about the need for New York State to relieve county governments of their share of the burden of the social service expenditures. Generally, less than 20% of the revenues for these services come from local sources. There has been relatively little discussion about the increased burden placed on Erie County government due to the reduced regional earnings and out migration of the best and brightest of our young. The region is getting older and less affluent, and this is causing fiscal burdens to the region's residents. The same holds for other large upstate New York counties such as Monroe and Onondaga.

The 2000 Census of Population, www.census.gov , identified the percent of the population that moved from another state to the metropolitan area of residence in 2000, for everyone living in a metropolitan area at the time of the last census. Only 4 out of the 323 metropolitan areas in existence at the time, had in-migration rates lower than the 4.6% in the Buffalo metropolitan area. In other words, only 4.6% of the local residents in 2000 moved into the Buffalo metropolitan area from another state between 1995 and 2000. This compares to 14.3% in Gainesville, Florida, 27% in Kileen, Texas, 9.6% in Columbus, Ohio; 17.2% in Grand Forks, North Dakota; and 17.8% in Charlotte, North Carolina.

New York City continues to be a common destination for in-migrants. In the year 2000, 10.6% of the residents of the New York PMSA had moved from another state into the metropolitan area in the previous five years. Before one leaps to the old saw that jobs and people have left upstate New York because of high local taxes, the downstate area is a common destination for our young migrants and taxes are substantially higher there than they are here.

## Conclusions

The Western new York region continues to decline. It appears that the last recession has followed the pattern of the other recessions since 1969 where the region led the nation into recession, has fallen more deeply and will recover more slowly and less fully than the nation as a whole. What can we do about this? We must be prepared to deal with the consequences of decline. Local government must be pared down to more closely resemble the relative earning power of the local tax base. Calls for help from the state government should be for the placement of state departments and agencies in the region that will generate local income, rather than for auditoriums, stadiums, arenas, or other play toys that do next to nothing for the regional economy.

The region sits astride one of the lowest cost sources of electric power in the nation, yet regional electric costs are amongst the highest in the nation. The property tax base has been whittled away with preferential treatment to a select few, while the remaining full payers have had to make up the difference generated by abatements and special allowances.

Local agencies have for years proclaimed long and loud about the number of new jobs that have been brought to the region, by special development projects and tax abatements, yet the earnings per worker of those new jobs have often escaped discussion. The region continues to convert high paying jobs into those that pay less. Local government officials continue to ask what's in it for the city when discussing the reorganization of local government, or argue about ways to protect patronage jobs when looking for items to cut in the county budget or analyzing how much to raise local taxes. The real unanswered questions are how can this region stop the bleeding, and how can it attract employers that will offer wages that are higher, not lower than those that have disappeared from the area?

# NATIONAL, STATE & LOCAL BUSINESS INDICATORS

| NATIONAL INDICATORS | 2003:III | 2004:I | 2004:II | 2004:III | % change 2003:III-2004:III |
|---|---|---|---|---|---|
| Real GDP (billions of chained 2000$) (1)(a) | 10,472.84 | 10,697.5 | 10,784.7 | 10,891.0 | 4.0 |
| US Personal Income (billions of $) | 9,209.3 | 9,445.0 | 9,592.7 | 9,674.3 | 5.0 |
| | **Nov-03** | **Sep-04** | **Oct-04** | **Nov-04** | **Nov-03 - Nov-04** |
| Leading Indicators Index (1996=100) (1)(a) | 114.2 | 115.4 | 115.0 | 115.2 | 0.88 |
| Consumer Price Index (1982-84=100) (2) | 184.5 | 189.9 | 190.9 | 191.0 | 3.52 |
| Exchange Rate Canadian/US $ (3) (b) | 76.99 | 79.28 | 82.10 | 84.32 | 9.52 |
| 10 Year Treasury Bond Yield (%) (3) (b) | 4.34 | 4.13 | 4.03 | 4.36 | 0.02 |
| 3 Month Treasury Bill Yield (%) (3) (b) | 0.92 | 1.70 | 1.87 | 2.20 | 1.28 |
| S&P 500 Stock Index (3) (b) | 1,058.2 | 1,114.6 | 1,130.2 | 1,173.8 | 10.93 |
| Dow-Jones Industrial Average (3) (b) | 9,782.5 | 10,080.3 | 10,027.5 | 10,428.0 | 6.60 |
| **LABOR MARKET TRENDS (2)** | | | | | |
| Nonag Civilian Employment | | | | | |
| US (1000's) (a) | 132,027 | 131,660 | 131,963 | 132,075 | 1.58 |
| NY State (1000's) (a) | 8,417.1 | 8,452.1 | 8,462.7 | 8,469.5 | 0.62 |
| WNY (1000's) | 554.0 | 547.6 | 550.9 | 552.3 | -0.31 |
| Unemployment Rate (%) | | | | | |
| US (a) | 5.9 | 5.4 | 5.5 | 5.4 | -0.5 |
| NY State (a) | 6.3 | 5.5 | 5.2 | 4.9 | -1.4 |
| WNY | 6.4 | 5.6 | 5.5 | 5.7 | -0.9 |
| Ave. Wkly Hours in Mfg. US | 40.8 | 40.8 | 40.6 | 40.5 | -0.74 |
| Ave. Wkly. Earnings in Mfg. US ($) | 655.92 | 664.22 | 662.19 | 665.86 | 1.52 |
| **WNY EMPLOYMENT BY SECTOR (1000's) (2)** | | | | | |
| Natural Resources, Mining & Construction | 20.5 | 21.3 | 20.9 | 20.2 | -1.46 |
| Manufacturing | 67.8 | 66.4 | 65.9 | 65.9 | -2.80 |
| Trade, Transportation & Utilities | 106.1 | 102.4 | 103.1 | 105.5 | -0.57 |
| Durable Goods | 41.0 | 39.6 | 39.4 | 39.4 | -3.90 |
| Finance Activities | 34.1 | 33.9 | 34.1 | 34.3 | 0.59 |
| Service Providing | 465.7 | 459.9 | 464.1 | 466.2 | 0.11 |
| Government | 97.1 | 95.2 | 98.4 | 98.6 | 1.54 |

(1) US Dept. of Commerce
(2) US Dept. of Labor
(3) Wall Street Journal

(a) Seasonally Adjusted
(b) End of month data