

Western New York ECONOMIC NEWS

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Wehle School of Business

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The mission of *Western New York Economic News* is to provide analysis and forecasts of trends in the Buffalo-Niagara Falls Metropolitan Statistical Area and contrast these trends with those in New York State and the nation. Topics of discussion include the national economic outlook, analysis of the labor market in the Buffalo MSA, and a forecast of area economic conditions. We use the term Buffalo MSA to refer to the Buffalo-Niagara Falls MSA. We will also publish analysis of other topics relevant to the Western New York business community.

Three issues of *Western New York Economic News* will be published each year. The full text and supporting documents of the newsletter will appear on the internet under the address <http://www.canisius.edu/wnyeconomicnews>. We will also publish a condensed version of this newsletter on paper to interested parties. If you are interested in receiving hard copy of this newsletter please notify the authors through e-mail.

The National Economic Outlook

Real GDP growth slowed to a 1.4% annual rate in the second quarter of 1998 after expanding at a robust 5.4% annual rate in the previous quarter www.bea.doc.gov. This was the 29th consecutive quarterly increase in real GDP since the trough of the 1990-91 recession. The slowdown in economic activity was due to a downturn in inventory investment and deterioration in the flow of net exports. Prior to the release of the 1998:II GDP data, many economists had predicted a negative real GDP growth rate in the second quarter and had reported on the increased likelihood of the economy falling into recession in 1998. The resiliency of the economy in its ability to overcome the drags of the Asian economic crisis and the General Motors strike has been somewhat of a surprise to analysts. The Conference Board's index of leading economic indicators www.conference-board.org, designed to forecast economic conditions six to nine months ahead, have declined the past two months, pointing towards slower economic growth. An accelerated decline in the indicators in July may point towards the onset of recession nine months ahead. We place a small probability of recession in 1998, but expect real GDP growth to average only 1.75% over the remainder of 1998.

US financial markets continued to surge in July 1998 as a result of the low inflation rate (1.7% growth in the CPI), and the continuing economic expansion. In early August 1998, the blue chip stock indexes declined by 10% from their highs of the previous month signaling the possible end to the bull

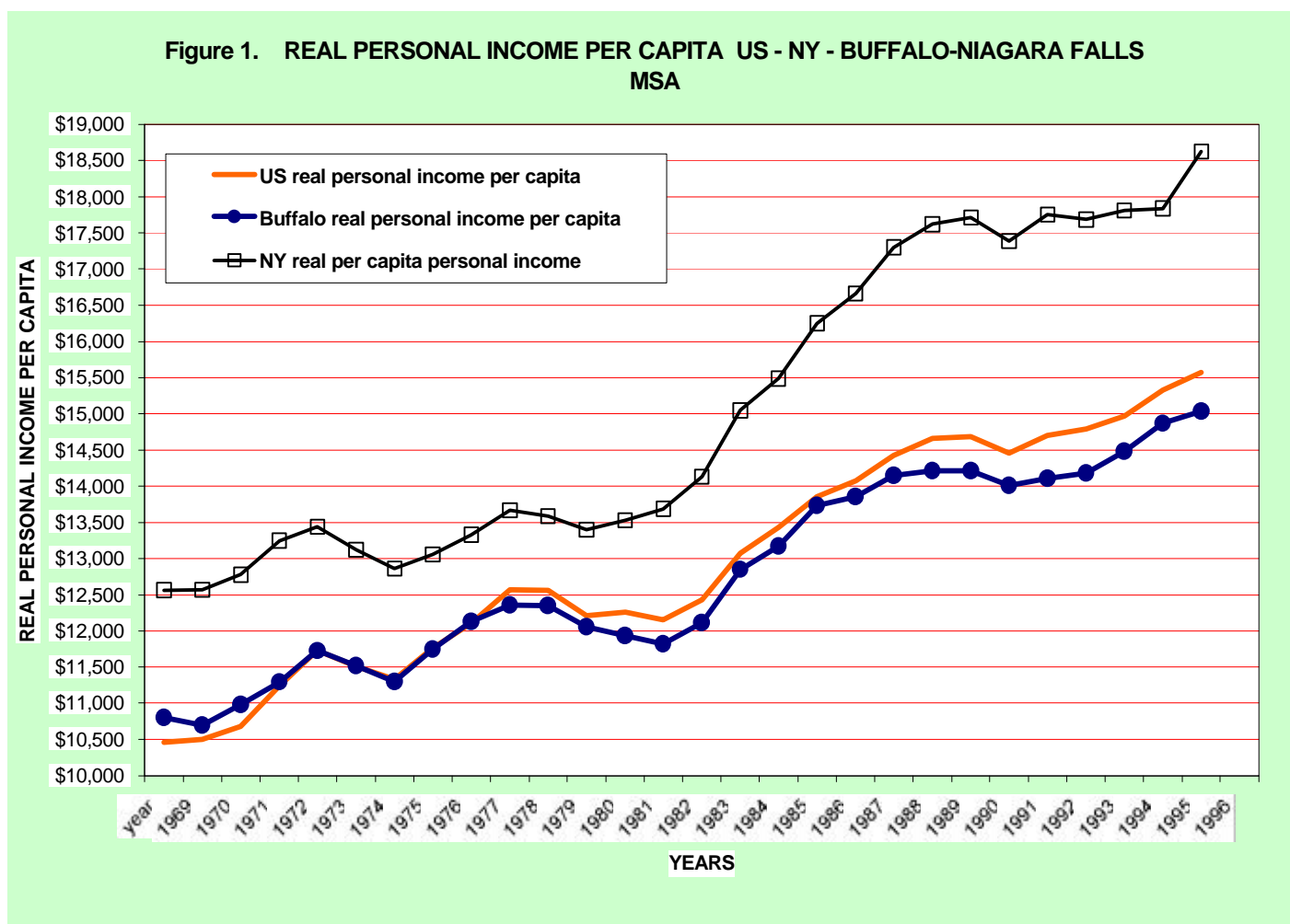
The Wehle School of Business at Canisius College publishes New Western New York Economic News as a public service to the Western New York business community with research and analysis performed by the following faculty from the Department of Economics & Finance:

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market of the last decade. A continuation of this stock market correction would increase significantly the chances of recession. In the bond markets, 30-year Treasury security yields have declined by approximately 100 basis points while 3-month Treasury bill yields have declined by approximately 20 basis points over the period June 1997 - July 1998, resulting in a substantial flattening in the yield curve. Short-term real interest rates continue to be in excess of 3%.

The Economic Outlook for the Buffalo Region

US personal income has continued to grow at a 5% rate in nominal dollars, exceeding the rate of inflation by approximately 3.3% www.bea.doc.gov. Since 1982, each 1% growth in US real personal income has resulted in a 1.04% increase in Buffalo real personal income. It is interesting to note that the percent change in Buffalo real personal income is more weakly correlated with the percent change in New York State real personal income than it is with the US. Since 1982, each 1% growth in New York State real personal income has resulted in a .67% increase in Buffalo real personal income. The distinction between Buffalo and New York State real personal income per capita and the connection to the US is shown in Figure 1. This result is due to the fact that the structure of the Buffalo economy is considerably different from that of New York City, which dominates the New York State personal income data.



The changing structure of the Buffalo economy is shown in Figure 2 where earnings in basic industrial sectors in the Buffalo area are compared to those of the nation in the years 1969, 1980, 1990 and 1996. The share of total earnings accounted for by each industry in Buffalo is compared to the US share for each industry. A 100% value for an industry implies that Buffalo's share is identical to the US share of total earnings for that industry. While declining as a share of total earnings, primary metals, motor vehicles and chemicals are still more heavily concentrated in Buffalo than in the rest of the nation. Fabricated metals are becoming more heavily concentrated in Buffalo. Business services, educational services, and finance, insurance and real estate (FIRE) are less heavily concentrated in Buffalo than the nation as a whole. The drastic drop in the importance of primary metals and the substantial increase in the importance of the cyclically dependent motor vehicle sector may explain Buffalo's recent past and immediate future. This traditional dependence on cyclically sensitive industries may well explain the close linkage between changes in Buffalo and US real personal income. It is interesting to note that fabricated metals are twice as important to Buffalo as to the national economy, and though declining, the motor vehicle sector is four times as important to Buffalo as it is nationally. Earnings in the service sector are less important in Buffalo than in the nation. Only in health care services has the relative share increased more rapidly locally than it has nationally.

Figure 2. BUFFALO - NIAGARA FALLS MSA EARNINGS SHARES AS PERCENT OF US EARNINGS SHARES

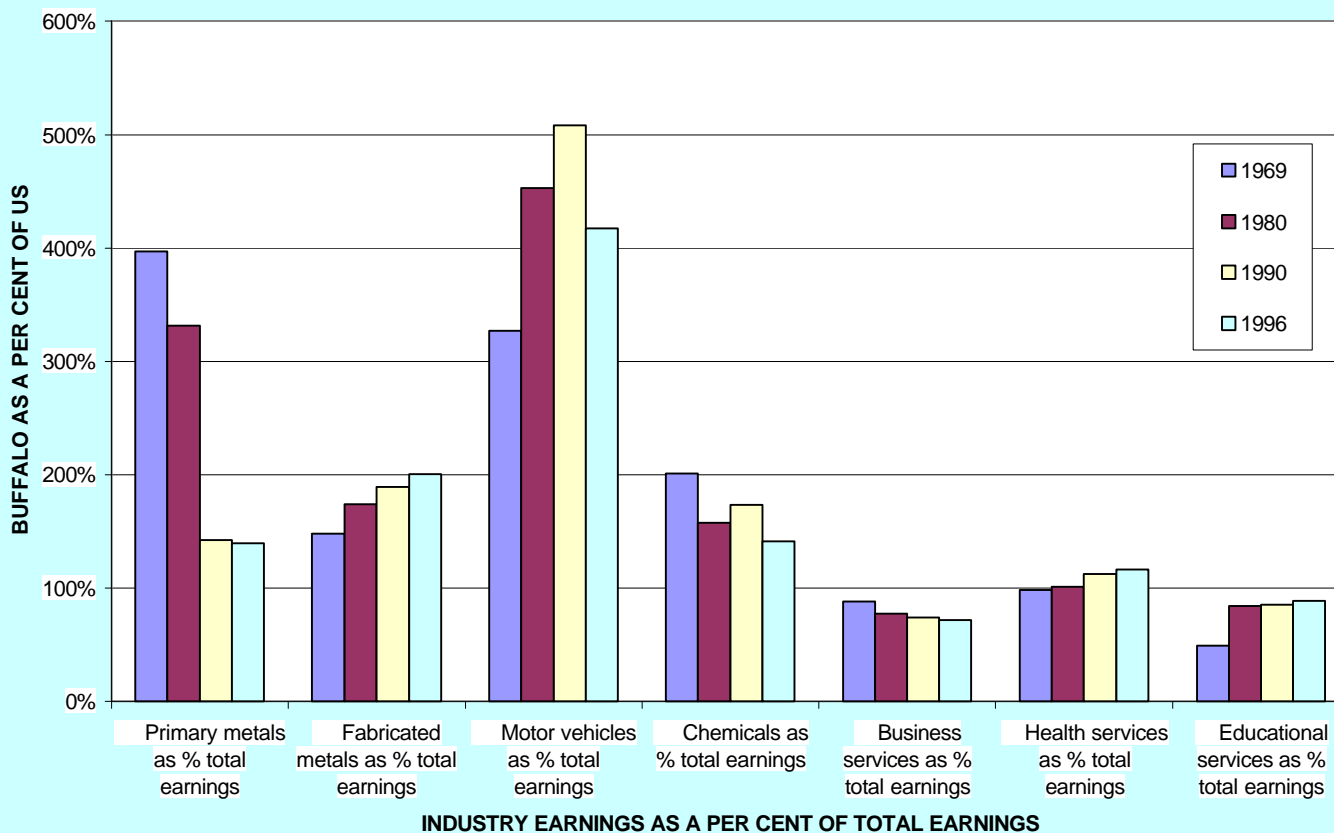


Figure 3 shows the implications of the changing structure of the Buffalo economy on earnings per worker. In 1969, earnings per worker in Buffalo were 9.7% higher than earnings per worker in the US. By 1990, it was 1.2% lower and in 1996 it was 4.5% lower than the national rate.

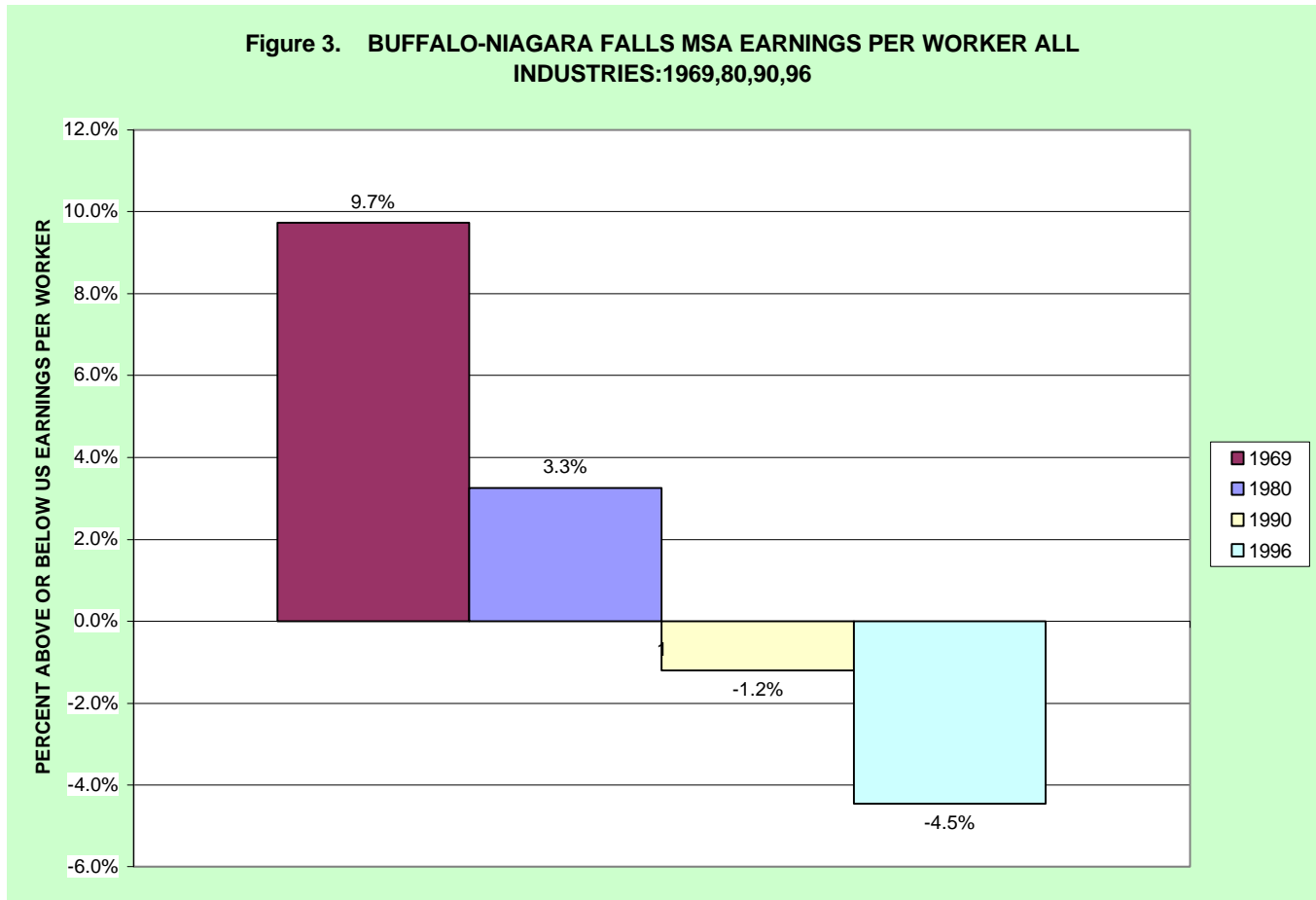
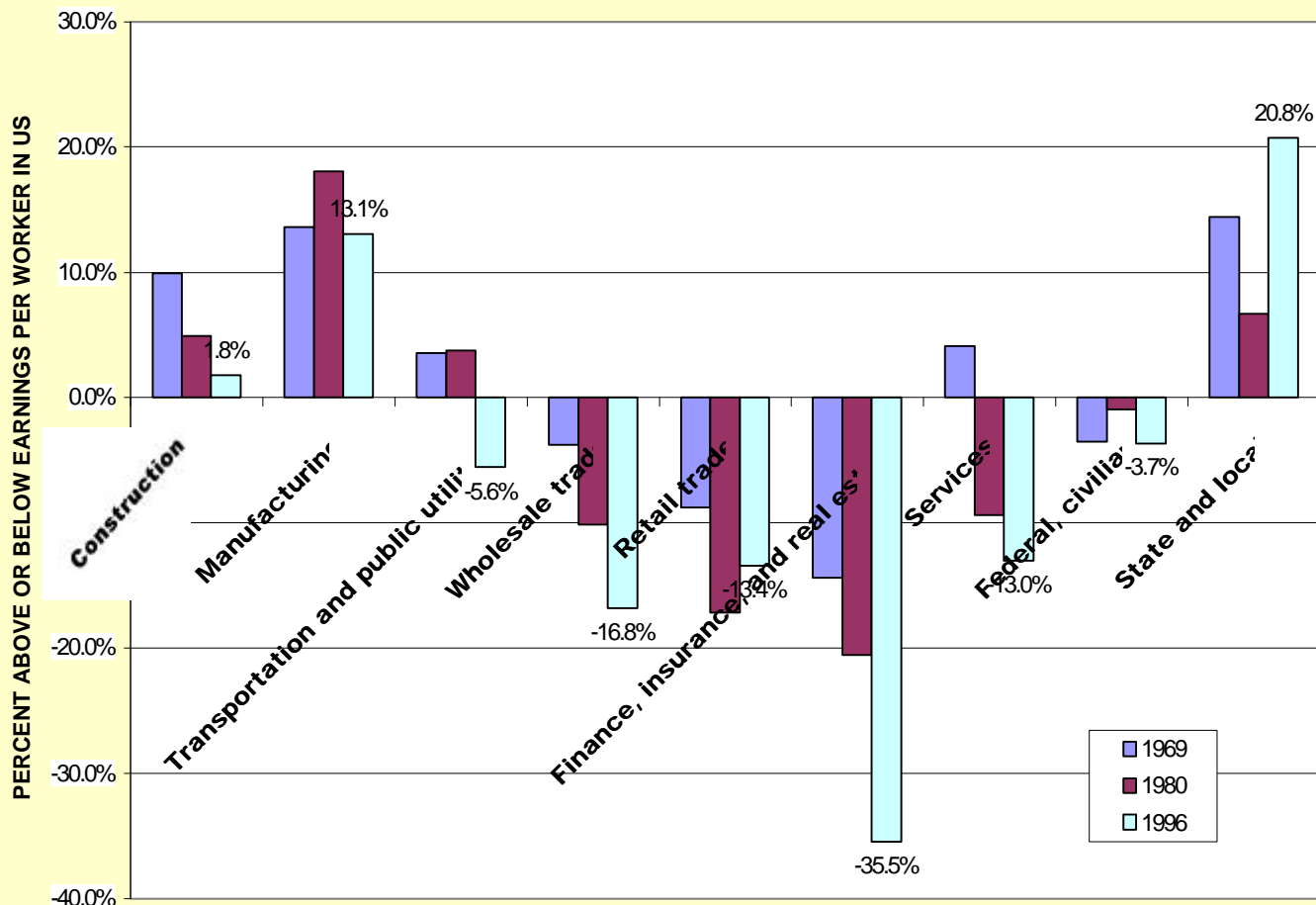


Figure 4 shows earnings per worker in selected industries compared to earnings per worker in the US in the years 1969, 1980 and 1996. Construction, manufacturing, and state and local government workers in the Buffalo area earn more than their US counterparts, while workers in wholesale trade, retail trade, services and FIRE earn substantially less.

Nonagricultural civilian employment in the Buffalo SMA increased by 1.16% from June 1997 to June 1998. This compares with growth of 1.61% in New York State and 2.62% growth in the nation. The local unemployment rate stood at 5.3% in June 1998 compared with 5.1% in June 1997. The New York State unemployment rate declined by 1% (5.5% versus 6.5%) over the same period while the national rate has declined by .5% (4.5% versus 5.0%). Labor market improvement in the area has lagged that of the state and the nation.

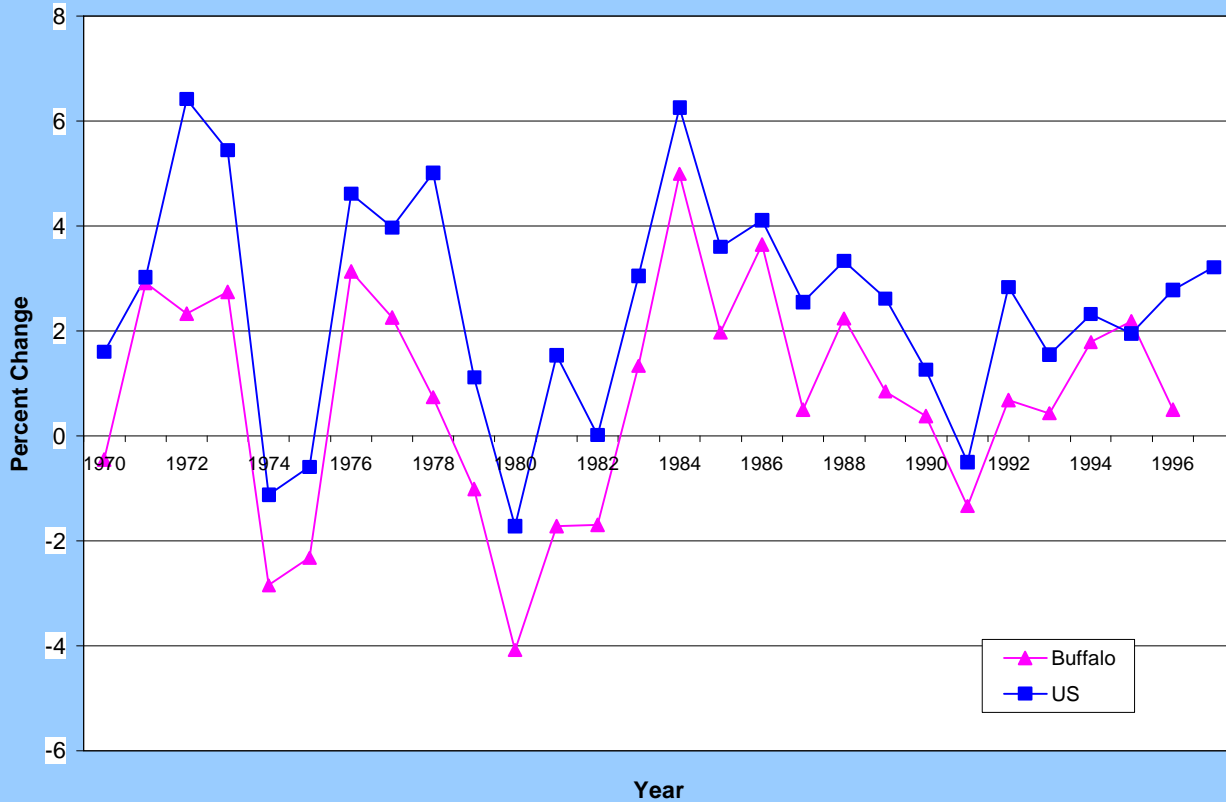
**Figure 4. BUFALO-NIAGARA FALLS EARNINGS PER WORKER SELECTED INDUSTRIES:
1969, 80, 96**



Revised data on personal income for the Buffalo MSA over the period 1969 - 1996 was published in May 1998 by the US Department of Commerce, Bureau of Economic Analysis. Personal income is made up of wages, proprietor's income, dividends, interest, rent and transfer payments. Adjustments are made for place of residence and personal contributions to social security are removed in generating an income series received by residents of Erie and Niagara counties. We feel that the level and growth rates of real personal income are the best single measures of the health of the Buffalo economy.

Figure 5 illustrates annual growth rates of real personal income in the Buffalo MSA versus the US. The close correlation between these series is obvious.

Figure 5. Annual Growth Rates of Real Personal Income: Buffalo v. US



Data from 1989 through 1996 are presented below along with our forecast for the period 1997 and 1998. The 1997 forecast uses the actual growth rate of real US personal income from 1996 to 1997 of 3.18%. Over the first half of 1998, real US personal income has grown by 3.45% over the first half of 1997. We expect this growth rate to slow to 2.5% for the entire year 1998. This translates to a 1.24% growth rate in real Buffalo MSA personal income in 1998.

Buffalo Area Real Personal Income

YEAR	PERSONAL INCOME (MILLIONS OF 1982\$)	ANNUAL PERCENT CHANGE
1991	16689.7	-1.34
1992	16803.6	0.68
1993	16876.2	0.43
1994	17177.2	1.78
1995	17552.3	2.18
1996	17639.7	0.50
1997	*17983.4	*1.95
1998	*18207.0	*1.24

An important component of the personal income picture for residents of the Buffalo MSA is the fraction of their incomes derived from such transfer payments as Social Security, Welfare, and other federal programs. Figure 6 shows the dramatic increase in the dependency of Buffalo MSA residents on transfer payments. In 1969, Buffalo residents received slightly more than 9% of their personal income from transfers, approximately the same rate as the remainder of the US. By 1996, Buffalo residents received almost 21.5% of their personal income in the form of transfer payments, while it accounts for less than 16.5% of personal income for most Americans. Potential Social Security and Welfare reform can have a far more profound impact upon Buffalo than the remainder of the US.

**Figure 6. TRANSFER PAYMENTS AS % OF PERSONAL INCOME: US & BUFFALO
NAGARA FALLS MSA**

