

Western New York ECONOMIC NEWS

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The national unemployment rate stood at 3.7% in August 2019 and the economy continues to add jobs. In spite of healthy labor markets and positive GDP growth led by consumer spending suggesting a strong economy, the FOMC lowered the federal funds target rate by 25 basis points. The Fed's easing along with the trade war with China, the inverted yield curve and low growth or recession in the rest of the world are causes for caution concerning the national economy. Local employment continued its steady post-recession growth, though at a place slower than the rest of the nation. Average annual pay remains about 14% lower than the national average.

The National Economic Outlook

Real GDP during the second quarter of 2019 showed the economy growing by 2.0%, slowing from the 3.1% rate during 2019:Q1. Growth was fueled by consumption expenditures, as well as federal, state and local government expenditures. Private inventories, exports, residential and non-residential fixed investment declined from the previous quarter and were a drag on GDP growth. Figure 1 shows real GDP growth rates over the past ten years.

The national unemployment rate has been below 4% since February 2019 and stood at 3.7% in August 2019. Monthly additions to non-farm payrolls have averaged a little over 158,000 during 2019. Both the U.S. unemployment rate and the payroll employment series over the period 2007-2019 are shown in Figure 2.

Healthy labor markets and positive GDP growth led by consumer spending indicate a strong economy. This is at odds with slowing global economic growth, the trade war with China, and the recent inversion of the yield curve, which point towards recession or at least a significant slowdown in economic growth in the near future. In September 2018, we pointed out that the economic expansion was aging (It's more than 10 years old in July 2019) and that a full blown trade war or other exogenous shock, like the recent destruction of Saudi oil installations, could bring the expansion to an end.

The Fed's angst over the state of the economy showed with its lowering of the federal funds target rate by 25 basis points on July 31 (2% - 2.25%). Some analysts are predicting another 25 basis point cut during the upcoming September meeting of the

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Figure 1. Real GDP Growth Rates: 2009:Q3 - 2019:Q2

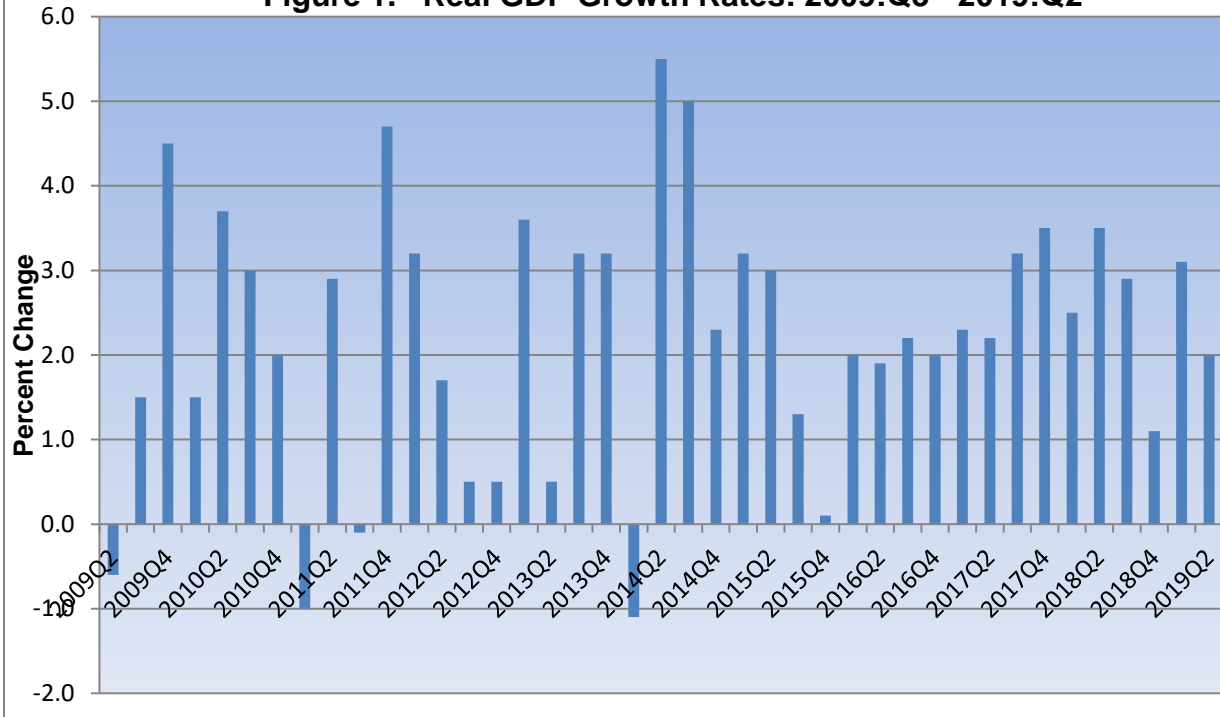
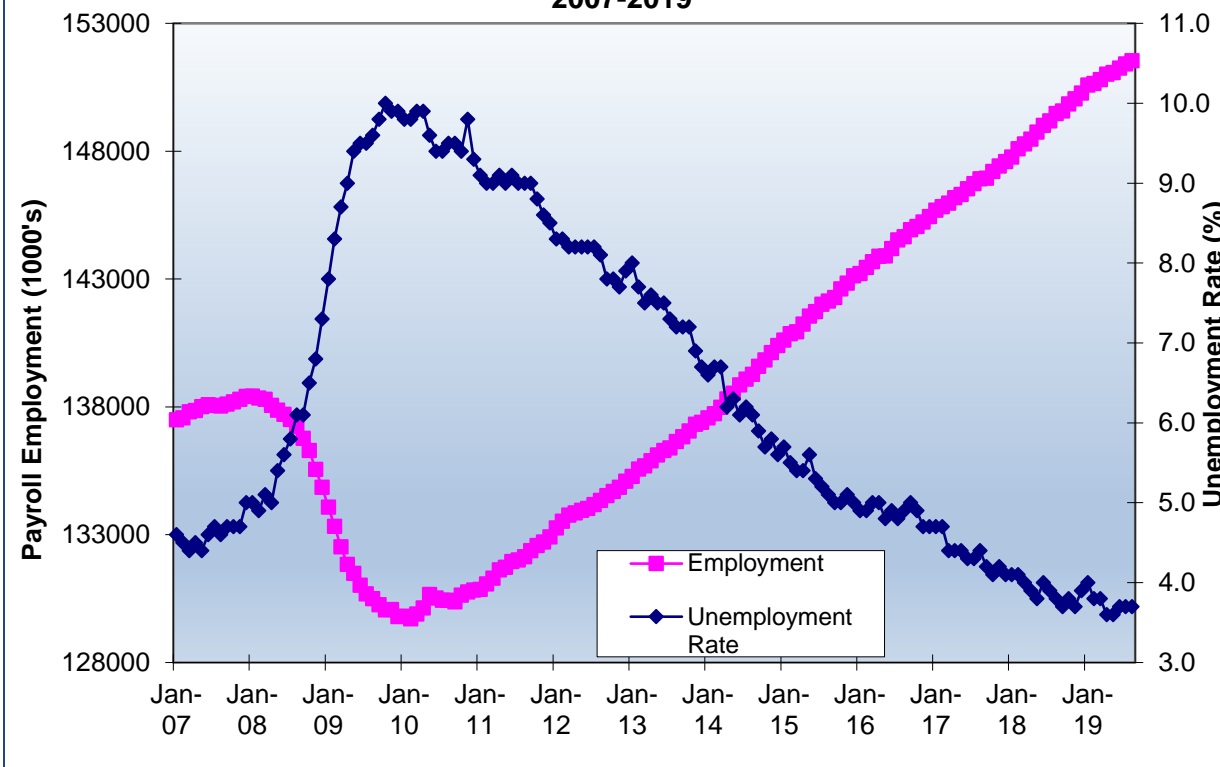


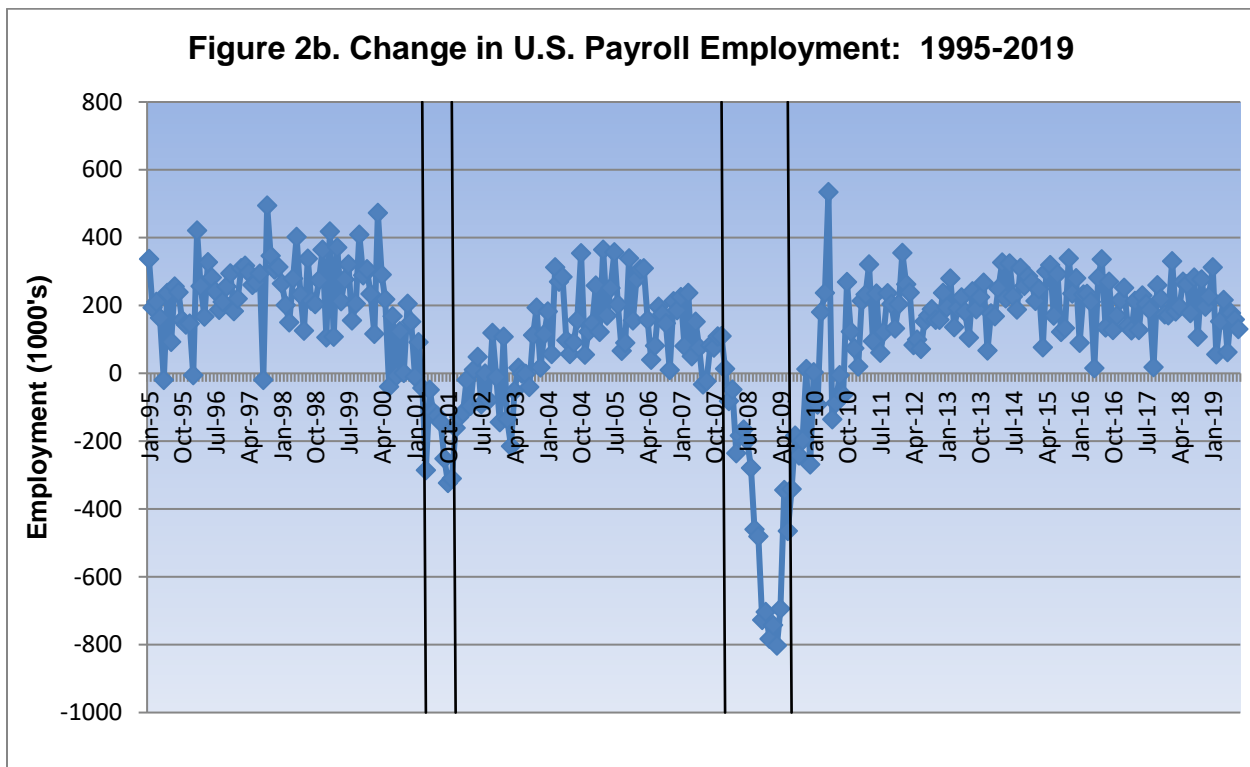
Figure 2a. US Payroll Employment & the Unemployment Rate: 2007-2019



FOMC (www.federalreserve.gov). The July decrease was the first reduction in the fed funds target since 2008 and signals worry about future economic growth and an inflation rate that has been below target. The rationale provided for this rate cut was that although economic activity had been growing moderately and labor markets were strong, business investment was soft and the core inflation rate (excluding food and energy prices) has remained below the 2% target. With its dual mandate of economic growth and inflation control in mind, the Fed wishes to keep the economy from entering a recession accompanied by deflation.

A comparison of employment levels and patterns of change tell a somewhat different story. Figure 2a presents the trends in payroll employment and the unemployment rate from the bottom of the last recession. The figure displays steady, uninterrupted growth in employment and a consistent reduction in the unemployment rate.

Monthly changes in payroll employment since 1995 are shown in Figure 2b. The pattern that preceded the 2008-2009 recession indicates a reduction in the growth of employment that began in mid-2005 and continued until 2008 when the level of employment declined and continued declining until 2010. A similar pattern of employment growth was observed prior to the 2001 recession.



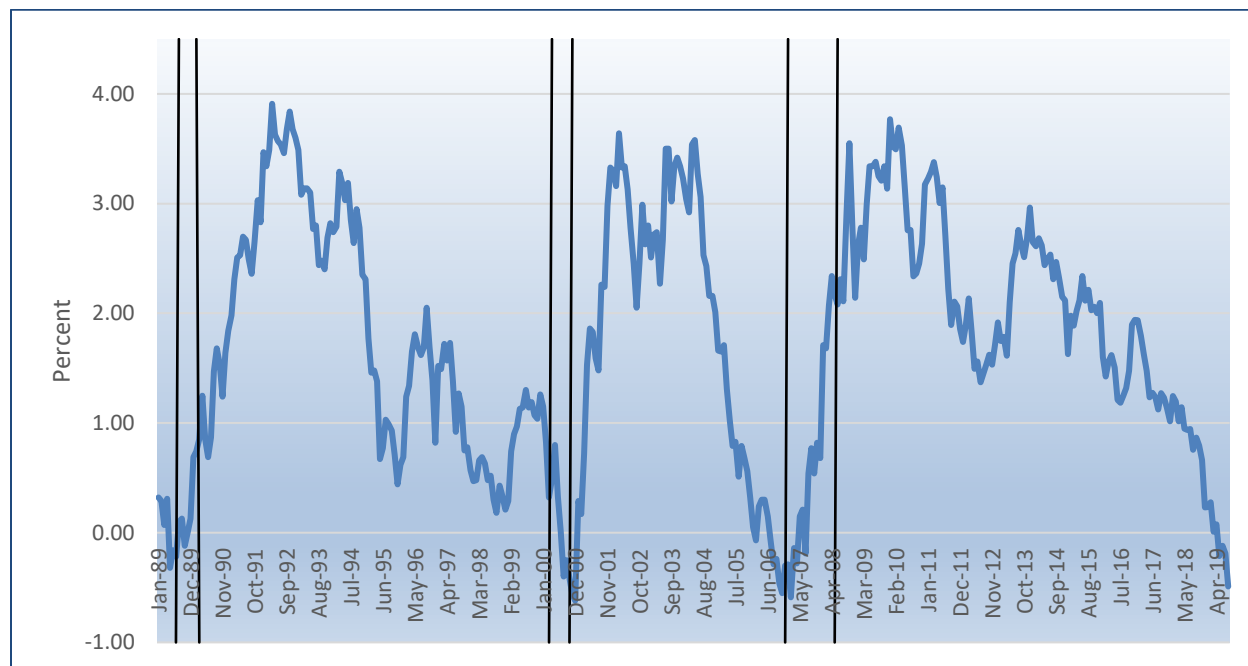
Since the end of the 2008-2009 recession, there has been no long term reduction in the growth in employment. The current economic expansion has been marked with fairly consistent employment growth. A slowing of employment growth like that observed prior to the last two recessions might signify that an economic downturn is on the horizon.

While the inverted yield curve, the trade war and the worldwide slowdown in economic growth is worrisome, one should watch employment levels, and changes in those levels to ascertain whether the recessionary pattern has re-emerged.

It is interesting to note that approximately 30 percent of the world's bonds have negative nominal yields. Most of the large European governments' bonds (except for the U.K. and Italy) have negative yields at present. The same is true for Japanese bonds. The safe haven that U.S. Treasuries provide the rest of the world is one reason why there has been downward pressure on U.S. nominal yields.

The Treasury yield curve from the 3-month bill to the 10-year note maturity exhibited a sustained inversion beginning on May 23, 2019. Historical daily yield differences between the 10-year Treasury note and the 3-month Treasury bill since 1982 appear in Figure 3. The yield curve is typically upward sloping since investors require a risk premium for holding long term bonds causing long term yields to exceed short term yields. Because interest rates are pro-cyclical, an expectation of recession will cause the demand for long term bonds to increase, lowering yields on these bonds and increasing their price. Since long maturity bonds exhibit a greater price increase than short maturity bonds for a given change in yield, long term yields will rise relative to short term yields.

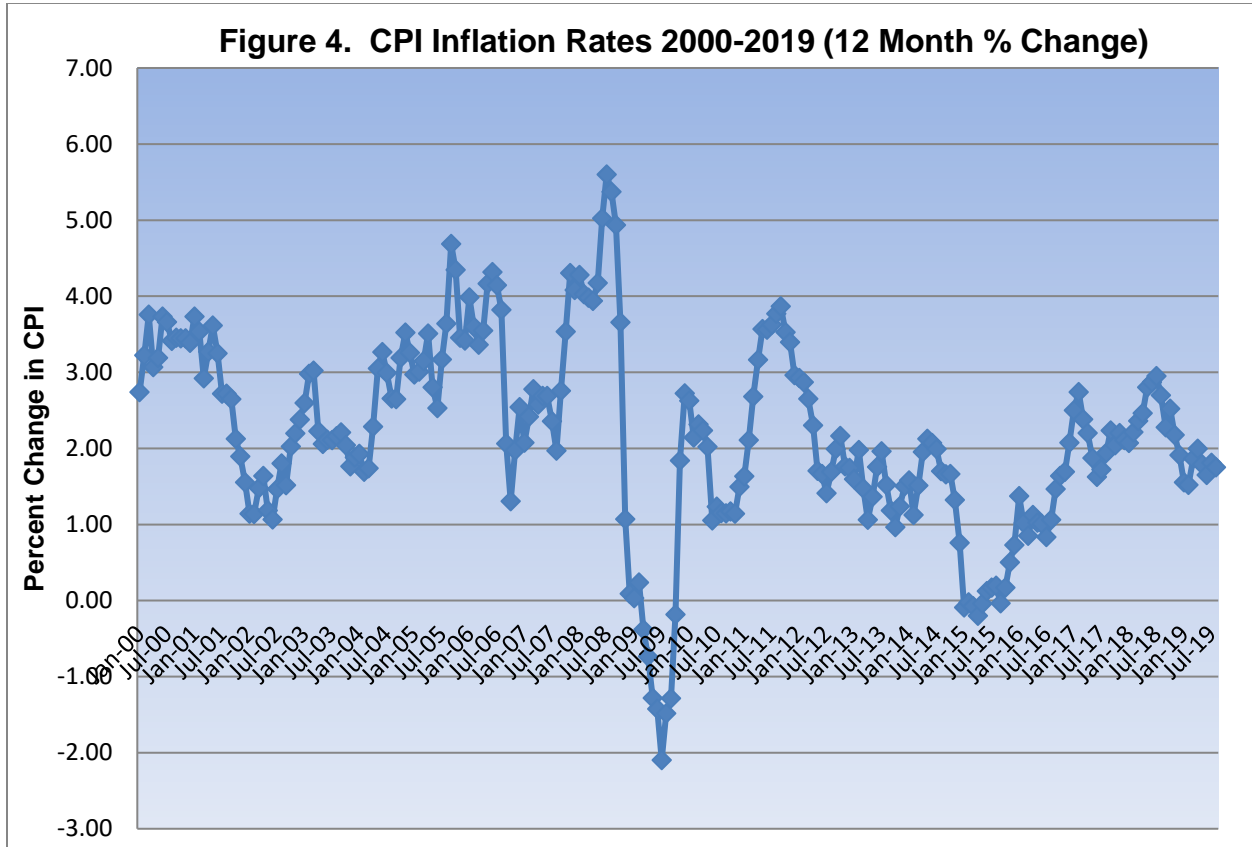
Figure 3. 10-Year Treasury Yields minus 3-Month Treasury Yields



The yield curve inverted 14 months prior to the recession that began in August 1990, 9 months prior to the recession that began in April 2001, and 19 months prior to the recession that began in January 2008. The present inversion began in May 2019.

The CPI inflation rate (including food and energy prices) has hovered around the 2% level since January 2017 (see Figure 4). According to the June 2019 Livingston inflation

expectations survey published by the Philadelphia Federal Reserve Bank, survey participants project CPI inflation to be 1.9% over the period 2018-2019 and 2.0% over the period 2019-2020.



The Economic Outlook for the Buffalo Region

We continue to find it informative to compare the monthly *Current Employment Statistics* (CES) data series to the broader based and larger *Quarterly Census of Employment and Wages* (QCEW) data series when attempting to draw conclusions about trends in the regional economy.

Figure 5 shows the seasonally adjusted monthly employment series for the Buffalo MSA from 1990 through July 2019. The Buffalo MSA data is based on the payrolls of establishments drawn from the CES survey <http://www.bls.gov/sae/>. The data provided by this survey shows that there has been sustained, though relatively modest employment growth in the Buffalo MSA since 2010. These numbers reflect a revision of the CES regional employment estimates and account for the differences from the figures reported in 2018.

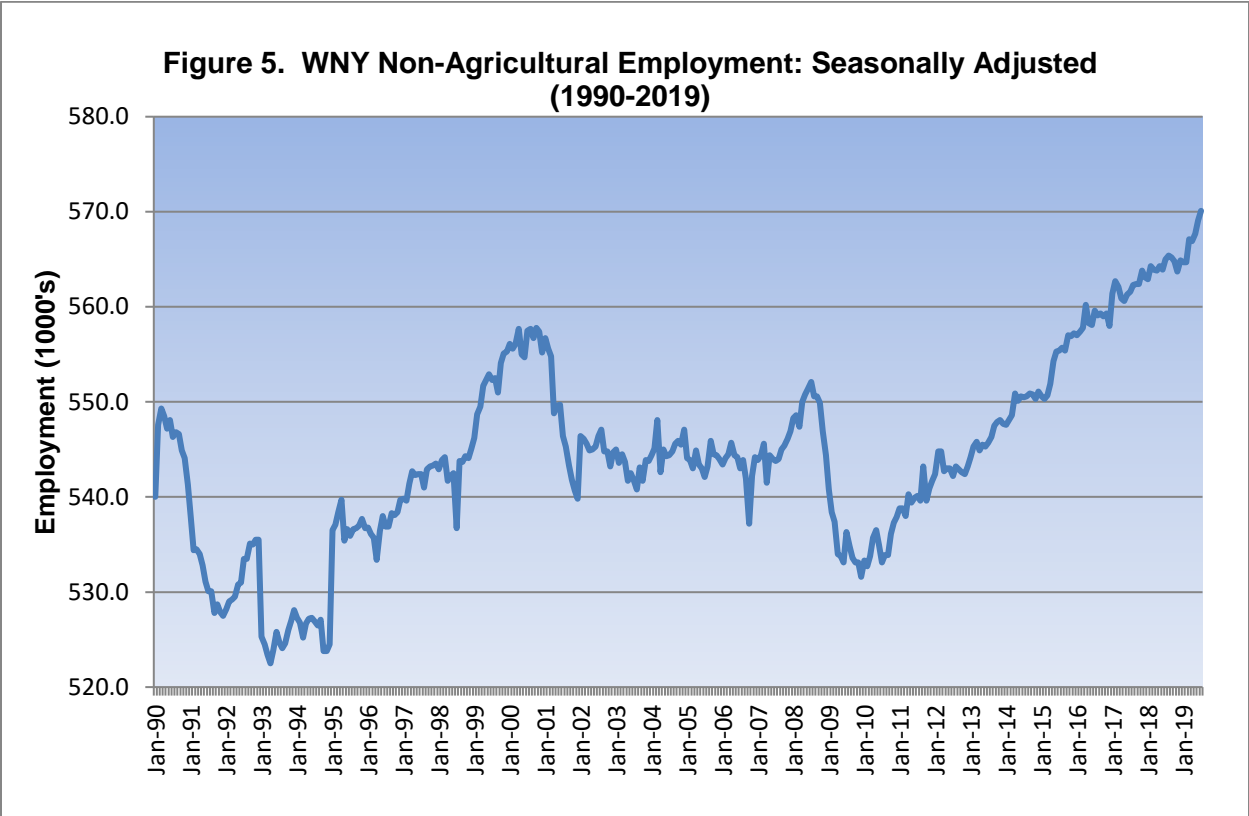


Figure 6 compares CES employment growth rates since 1990 for the Buffalo, Rochester and Syracuse metropolitan areas and compares them to the U.S. The ratio of annual employment in each area to its level in 1990 results in the construction of an employment index. These metropolitan area indices can then be compared to the national employment index to determine the relative growth of the metro areas to the nation. Employment levels in the United States were 37.8% higher in 2019 than in 1990. To keep the context of change clear, the Rochester metropolitan area had 8.8% more employment in 2019 than it had in 1990, Buffalo was 3.3% higher and Syracuse was 2.4% above the level in the base year. It is clear that these upstate New York metro areas have experienced far less employment growth since 1990 than has the rest of the U.S.

Figure 6. Upstate MSAs v. U.S. Employment: 1990 = 1

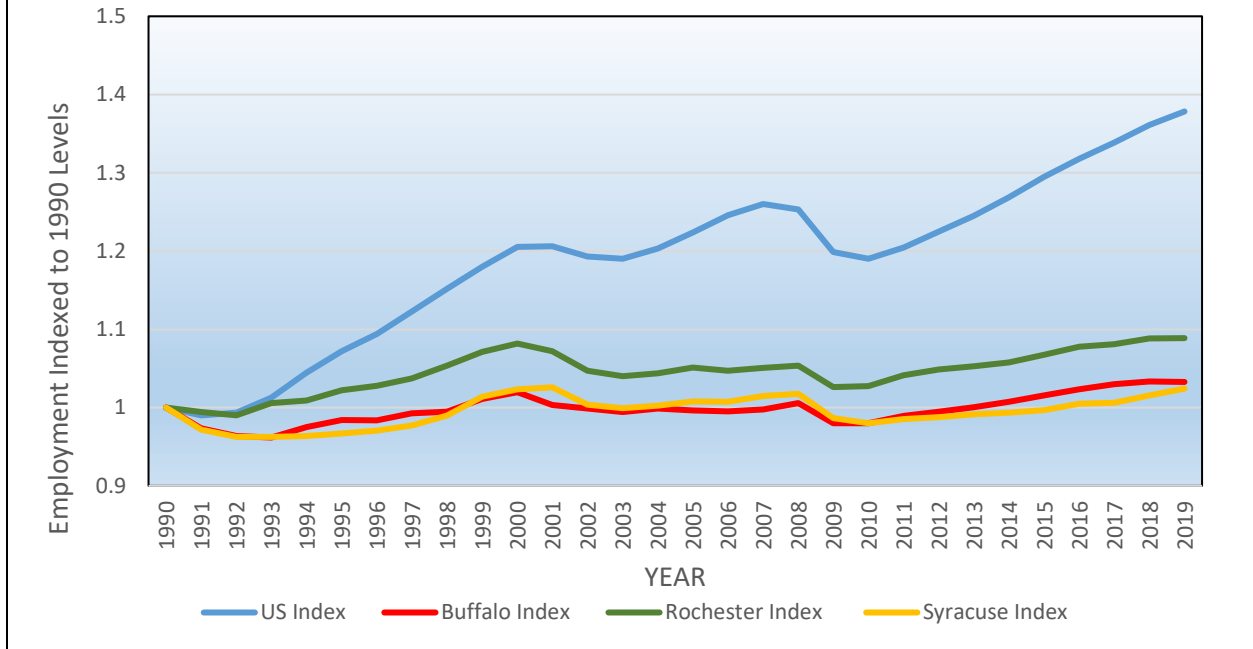


Table 1 presents annual employment and annual pay data for the Buffalo MSA and for the U.S. in 2018. It also presents average earnings per worker for each industry sector and the concentrations of employment per industrial sector relative to the national average in the form of local location quotients. Additionally, the table presents the ratio of local to national earnings per worker. The data allows a comparison of Buffalo versus the nation for total employment in the public and private sectors, as well as for specific industries in the private sector.

The location quotients (LQs) are calculated by dividing the ratio of industry employment in the Buffalo MSA to total employment in the MSA divided by the ratio of industry employment in the U.S. to total employment in the U.S. Thus, the .75 value of Buffalo's LQ for construction means that the proportion of total employment made up by construction employment in Buffalo is 75% of the average for the entire United States.

Table 1. Buffalo MSA Employment and Earnings by Industry: 2018

Industry	Average Annual Employment 2018	% Change in Employment 2017-2018	Average Annual Pay (\$)	Location Quotient Relative to U.S. 2018	Local % of U.S. Average Pay 2017	Local % of U.S. Average Pay 2018
Total, all industries	542,038	0%	49,273	1.00	86%	86%
Total, Federal Government	9,360	0%	79,270	0.90	94%	95%
Total, State Government	20,160	-5%	71,232	1.17	102%	117%
Total, Local Government	55,402	0%	54,675	1.05	107%	106%
Total Private all industries	457,116	1%	47,036	0.99	82%	82%
Goods-producing	73,555	0%	63,078	0.91	96%	96%
Natural resources & mining	1,774	3%	38,775	0.25	65%	65%
Construction	20,112	0%	57,640	0.75	93%	92%
Manufacturing	51,669	0%	66,029	1.10	96%	96%
Service-providing	383,561	1%	43,959	1.01	79%	79%
Trade, transportation & utilities	97,219	0%	38,697	0.96	81%	81%
Information	7,197	6%	63,879	0.69	60%	56%
Financial activities	35,473	-1%	65,858	1.17	68%	69%
Professional & business services	67,360	0%	59,583	0.88	78%	79%
Education & health services	94,808	3%	44,663	1.11	88%	89%
Leisure & hospitality	60,548	0%	24,255	1.02	105%	101%
Other services	20,410	1%	27,887	1.21	71%	72%
Unclassified	547	-44%	32,045	0.98	52%	54%

Source: <http://www.bls.gov/cew/datatoc.htm>

The LQ's shown here are employment based, but the same calculation could be made using industry earnings compared to total earnings. An LQ greater than 1 implies some degree of specialization in that industry for the region.

In addition to the LQ's, Table 1 also shows average earnings per worker by industrial sector in the Buffalo MSA as a percent of the national average for that sector. This

combination reveals the areas of specialization within the Buffalo MSA and the relative earnings generated per worker in each sector. Buffalo has a larger concentration of state workers than is the norm for the country (17% higher). The same is true for employment in the financial sector.

State workers are paid 17% more than the national average for state employees. This might reflect the occupational mix of state employment in the Buffalo MSA that has higher paying jobs than the average of state workers in the nation (for example professional employment at the SUNY campuses). It might, however, reflect a higher pay scale regardless of occupation for New York State government employees. The slightly higher level of local government employment may reflect the requirement that county level governments deliver social services in New York State, a function that is provided at the state level in most states. Whether this explains the higher earnings per worker in the Buffalo MSA for employees of local governments is not clear.

Interestingly, while manufacturing is still somewhat concentrated in the Buffalo MSA (10% above the national average employment in the sector), average pay is 4% lower than the national average. In 1998, BEA estimates showed earnings per manufacturing worker in the Buffalo metropolitan area were about 9% higher than the national average. Manufacturing employment in the Buffalo MSA in 1998 was approximately 90,000, while at present there are about 51,442 manufacturing employees. Thus, the region has lost manufacturing jobs and more importantly, the jobs it has retained generate earnings that are lower than the national average for the sector.

Table 1 shows that financial service employment continues to be concentrated in the Buffalo MSA. While average annual pay in this sector is well above the regional mean, it is only 69% of the national average. It is not surprising that there is employment growth and strength in an industrial sector where the average pay is lower than the national norm, for this behavior is consistent with properly functioning markets.

The 1.17 LQ for the financial services sector in Buffalo supports the statement made many times in this space that the region is attractive to those firms that need skilled workers who are willing to work here for less than the national average salary. When this salary is higher than that which can be earned by workers in almost any other local industry, both the firms that relocate to WNY, as well as newly employed residents working for them, are made better off by the move.

Last year we expected new employment growth to appear in the information services sector since wages are substantially lower in Western New York compared to the rest of the nation. While employment growth in information services of 6% was larger than in any other industrial sector, average annual earnings per worker fell from 60% to 56% of the national average from 2017 to 2018. Perhaps this sector will see continued growth in the future.

NATIONAL, STATE & LOCAL BUSINESS INDICATORS

					% change
NATIONAL INDICATORS					2018:II -
	2018:II	2018:IV	2019:I	2019:II	2019:II
Real GDP (billions of chained 2012\$) (1)(a)	18,598.1	18,783.5	18,927.3	19,023.0	2.3
US Personal Income (billions of \$) (1)(a)	17,725.0	18,082.8	18,355.4	18,600.8	4.9
					% change
					Aug-18 -
	Aug-18	Jun-19	Jul-19	Aug-19	Aug-19
CPI Inflation Rate (%) (2)**	2.70	1.65	1.81	1.75	
Exchange Rate Canadian cents/US \$ (3)(b)	130.41	130.930	132.130	133.120	2.08
10 Year Treasury Note Yield (%) (3)(b)	2.86	2.006	1.895	1.500	-1.36
3 Month Treasury Bill Yield (%) (3)(b)	2.10	2.125	2.085	1.989	-0.12
S&P 500 Stock Index (3)(b)	2,901.52	2,941.76	2,953.56	2,926.46	0.86
Dow-Jones Industrial Average (3)(b)	25,964.82	26,599.96	26,864.27	26,403.28	1.69
LABOR MARKET TRENDS (2)					
Nonag Civilian Employment					
US (1000's)(a)	149,467	151,252	151,411	151,541	1.39
Change from previous month	282	178	159	130	
NY State (1000's)(a)*	9,691.7	9,778.7	9,780.1		0.99
WNY (1000's)(a)*	565.4	569.1	570.1		0.81
Unemployment Rate (%)					
US (a)	3.8	3.7	3.7	3.7	-0.1
NY State (a)*	4.2	4.0	4.0		-0.3
WNY*	4.3	3.7	4.3		-0.2
Ave. Weekly Hours in Mfg. US (a)	42.2	41.7	41.5	41.6	-1.42
Ave. Weekly. Earnings in Mfg. US \$(a)	909.41	922.82	920.89	924.77	1.69
US Private Employment (1000's)(a)	126,973	128,723	128,854	128,950	1.56
WNY EMPLOYMENT BY SECTOR (1000's)(2)					
Mining, Logging & Construction	23.2	22.6	22.7		-1.73
Manufacturing	52.6	52.3	51.4		-2.10
Trade, Transportation & Utilities	99.6	101.0	100.1		0.30
Durable Goods	32.5	32.6	32.0		-1.23
Finance Activities	36.5	37.5	38.1		3.81
Government	86.2	90.4	86.8		0.35
(1) US Dept. of Commerce	(a) Seasonally Adjusted				
(2) US Dept. of Labor	(b) End of month data				
(3) Wall Street Journal	* Jul-18 - Jul-19 % change				
	**% change from same month in previous year				