Employment gains in construction, services, and government in February and the loss of only a couple hundred manufacturing jobs helped put Alabama’s job picture back in the black after three straight years of losses. New and expanding auto manufacturers and suppliers will be a source of job creation throughout the remainder of 2004. Growth in the state’s economy should be helped by accommodative financial conditions; the continuing effects of the fiscal stimulus, particularly on consumer spending; rising business confidence; and productivity gains and profit growth, supporting business capital investment. Risks to growth in the state and national economies in the second quarter include the possible effects of higher energy prices and of surging commodity prices. These pressures could force companies to push productivity gains and outsourcing to cut costs.

Energy prices are expected to be a continuing concern in 2004. Two-thirds of Alabama business leaders predict that energy prices will increase substantially during the remainder of the year. Higher gas prices are effectively a transportation tax on businesses and consumers. Global Insight estimates that every dime increase in gasoline prices costs U.S. consumers around $1 billion per month, so the 25 cent average increase from December to March takes $2.5 billion out of consumers’ pockets each month. The recent sharp fall in U.S. crude inventories and gasoline stocks in the face of strong demand growth and the approaching summer driving season does not bode well for prices in the short run.

The confidence of Alabama business leaders in an improving economy for the second quarter of 2004 matches the record 67 of the first quarter index. Most panelists expect growth in the national and state economies to accelerate. However, on the heels of strong expectations for first quarter economic performance, more panelists are in the position this quarter than last of expecting overall economic growth in both the United States and Alabama to continue at its current pace. All four industry indicators registered their highest positive readings in the two and a half years of BLCI survey results. Over 80 percent of panelists forecast improved sales in their industry during the second quarter, while more than 69 percent think profits will increase, and almost 60 percent foresee increased capital spending. Most importantly for a sustained economic rebound, the share of business leaders expecting their industry to add jobs rose slightly to 49.2 percent, while the percent anticipating job cuts fell to a new low of 4.9 percent. Manufacturing seems to be getting back on track, with increases on all four indicators compared to the previous quarter.
The National Economy

U.S. economic growth accelerated in the first quarter of 2004, in line with the predictions of an overwhelming 89.1 percent of BLCI panelists. Continued consumer spending, low interest rates, rising productivity, and record profits were finally supported by the beginnings of job creation. Alabama business leaders feel confident that the pace of growth will pick up further in the second quarter, with 78.3 percent predicting increased economic activity at the national level. Given first quarter gains, however, some respondents think growth will continue at the first quarter pace (15.2 percent) or will slow (6.5 percent). Still, the second quarter outlook represents the second highest consensus for growth since the survey’s inception and contrasts with a year ago when the survey, completed as the United States prepared to go to war in Iraq, found just over half of panelists forecasting economic gains.

The Alabama Economy

Business leaders are optimistic about prospects for growth in the Alabama economy. About 65 percent expect economic activity to increase in the second quarter of 2004, a sharp contrast to a year ago when just 43 percent forecast gains. A number of new and expanding automotive manufacturers and suppliers should be hiring during the quarter, adding to modest job gains from other sectors including construction, services, and government that could reverse Alabama’s three-year job decline. And, although lawmakers are grappling with anticipated budget shortfalls for FY2005, the current fiscal year crunch has been eased by cost-cutting measures and improved revenues. The 65 percent of panelists forecasting increased growth in the state’s economy in the second quarter is off from 71 percent last quarter as some moved into the position of expecting economic activity to continue at the first quarter pace. However, just 5.1 percent think the state’s economy could slow—the lowest negative reading since the BLCI survey began in first quarter 2002.

Interest Rates

Most BLCI panelists (62.6 percent) expect interest rates to hold steady during the second quarter of 2004. The Federal Open Market Committee left the federal funds target rate at 1.0 percent at its March 16 meeting, citing the importance of an accommodative stance in helping drive economic activity in the face of continued weak job creation. With the economy picking up, however, about 35 percent of Alabama business leaders think interest rates could rise by the end of June. If the more robust March job gains can continue for several months, some forecasters expect a modest hike of 0.25 percent to come as early as June, particularly since there are now clear signs that inflation has bottomed out.
Industry Sales

Sales should be the strongest contributor to accelerated economic activity in the second quarter of 2004. Eighty percent of panelists expect sales in their industry to be above first quarter levels, up slightly from last quarter for the most optimistic prediction in survey history. And the 5.6 percent of business leaders forecasting a decline in sales is the lowest negative. Consumer spending should be supported in the second quarter by an anticipated $25 billion one-time boost from extra tax refunds that more than offsets the negative effect of higher gasoline prices in the short term. Almost 91 percent of respondents in wholesale trade anticipate higher second quarter sales, while over 85 percent of retail trade and finance, insurance, and real estate (FIRE) panelists expect sales gains. Transportation, information, and public utilities (TIPU) could see the largest increase in sales, with 86.7 percent predicting higher second quarter sales compared to 66.7 percent last quarter. Manufacturers are slightly more optimistic about sales growth this quarter, with 77.4 percent expecting gains.

Industry Profits

Alabama business leaders generally anticipate increased profitability in the second quarter, with 69.3 percent forecasting gains in their industry—the highest positive expectation since the BLCI survey began in first quarter 2002. Weak wage gains continue to allow sales growth to be passed on to profits. Profit expectations are most robust in TIPU, where over 83 percent of panelists feel profits will rise in the second quarter—a jump of 25 percentage points from last quarter’s 58 percent. Profit growth is also expected to be above average in wholesale and retail trade, FIRE, and leisure, hospitality, and other services. In manufacturing, the negative effects of the rapid rise in commodity prices should be offset by increasing demand and a continued upside to productivity gains. Over 65 percent of Alabama manufacturers expect profits to strengthen during the second quarter of 2004, up from about 57 percent last quarter.

Industry Hiring

While the first quarter of 2004 brought a glimmer of job creation in Alabama, the second quarter offers promise that the state will begin to recover from three years of job losses. Alabama business leaders are the most confident since the survey’s inception in first quarter 2002 that the state will add jobs—49.2 percent forecast job gains in their industry, while 46 percent expect employment to be unchanged. Most importantly, only 4.9 percent of panelists think their industry will shed jobs this quarter—a new low. Over half of respondents in construction, services, and FIRE expect job gains in their industry during the second quarter. The hiring outlook is most

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improved for construction, with spring weather and continued strong housing sales in view. And while half of manufacturers expect employment to be flat, the 45.4 percent expecting to see jobs added is up from 41.1 percent in the first quarter.

### Industry Capital Expenditures

Capital spending should be a significant component of economic growth in the second quarter of 2004. Strong profits have given companies money to invest and the bonus depreciation tax deduction set to expire at the end of 2004 gives them a reason to purchase equipment and software this year. Close to 60 percent of Alabama business leaders anticipate an increase in capital expenditures in their industry in the second quarter, up about one percentage point from last quarter. And the share expecting capital spending to decrease dropped to a survey low of 4.8 percent. Retailers are most likely to make second quarter capital investments, according to the forecast of 70 percent of industry panelists. Capital spending should also be particularly strong in health care services and FIRE, with around 65 percent of respondents predicting increases. Manufacturers are more likely to make capital investments this quarter than last—the 60.6 percent of industry panelists forecasting an increase is up from 51.8 percent in the first quarter.

### BLCI Panelists

More than 400 Alabama panelists completed the second quarter 2004 BLCI survey online during March. Respondents registered their views on the probable course of the national and Alabama economies and of sales, profits, hiring, and capital expenditures in their industry. Alabama business leaders responding to the survey represent small, midsize, and large companies across Alabama’s 11 metropolitan areas and over 40 nonmetro communities. On the second quarter survey, 35.3 percent of participating firms reported annual sales under $5 million, while 36.2 percent had sales in the $5 to $50 million range, and 23.8 percent tallied sales of more than $50 million. In terms of employment size, one third of second quarter panelists were from firms with fewer than 20 employees, while 29.8 percent employed 20 to 99, and 37 percent had at least 100 employees.