Economic Outlook: First Quarter 2009

United States

Review. The U.S. economy, as measured by gross domestic product (GDP), declined at an annual rate of 3.8 percent for the fourth quarter of 2008, the largest drop since the first quarter of 1982 when the economy shrank by 6.4 percent. This follows a 0.5 percent decrease in the third quarter. The decline was positively offset by an increase in federal government spending, a decrease in imports, and a build-up in inventories as production outpaced demand. Without the positive impact of government spending and inventories, GDP would have declined by 5.3 percent during the fourth quarter.

Reductions in consumer and business spending subtracted 2.5 percent and 2.2 percent, respectively, from overall economic growth. Cutbacks in motor vehicle output shaved almost 2.1 percent from GDP in the fourth quarter. A sharp decline in exports subtracted another 2.8 percent from overall growth, while weakness in the housing sector and construction activity deducted 0.9 percent. On the positive side, the increase in inventories contributed 1.3 percent and the sharp decline in imports added 2.9 percent to overall GDP growth in the fourth quarter.

For all of 2008, the U.S. economy grew by 1.3 percent. While consumer expenditures increased 0.3 percent, business spending fell 5.9 percent. GDP is now forecast to decline by approximately 5.5 percent in the first quarter of 2009 and by around 2 percent during the second. For all of 2009, GDP is expected to contract by 2.5 percent.

Consumer spending fell 3.5 percent during the fourth quarter, following a 3.8 percent decline in the previous quarter. Business spending, which held up fairly well during the first half of 2008, dropped 12.3 percent in the fourth quarter, with spending on equipment and software declining by approximately 20 percent, the largest drop seen in decades. Residential fixed investment, including both residential construction and home sales, fell by almost 28 percent, while new home sales slipped to the lowest level on record.

Commercial construction activity, which had been growing for most of 2008, is beginning to sputter as projects in the pipeline are completed and financing for new projects gets harder to obtain.

With both consumers and businesses curtailling their spending, imports from other countries declined by 15 percent during the fourth quarter. As the recession spread across the globe in the second half of 2008, however, the demand for U.S.-made products also fell sharply, causing exports to drop by almost 20 percent in the fourth quarter. Exports had kept the economy from sinking into a deeper recession during the first half of the year. While federal government spending rose, state and local government spending fell in fourth quarter 2008, indicating that shortfalls in tax revenues are forcing state and local governments to cut back on expenditures.

The Institute for Supply Management’s manufacturing index rose to 35.6 in January from an upwardly revised 32.9 in December; an index below 50 indicates contraction. The index had fallen steadily since August as the economy deteriorated, hitting a 28-year low in December. While the reading for January showed some improvement, it still indicates continued weakness in the industrial sector. For all of 2008, orders for durable goods fell 5.7 percent, a decline second only to the 10.7 percent drop seen in 2001. Orders for computers and electronic goods dropped by 7.2 percent in December, and factory orders for metals, machinery, transportation equipment, and communications equipment also slumped as businesses cut their production and their outlook on the economy. Orders for durable goods, particularly automobiles and other big ticket items, will have to revive in order for the manufacturing sector to come out of recession.

As of January 2009, a total of 3.6 million jobs had been lost since the beginning of the recession in December 2007, the largest drop since 1945. Employers shed about 2.5 million jobs during just the five months from September 2008 through January 2009. Unemployment jumped to 7.6 percent in January, the highest rate since 1974.

During the first seven months of 2008, crude oil and commodity prices rose to record highs, causing inflation to run at about a 6.25 to 6.5 percent annual rate. This had a significant impact on consumers by reducing their purchasing power and on businesses by increasing their costs, with the result that both consumer and business spending fell at a rapid rate. However, prices began to drop in August 2008 and the inflation rate declined sharply between August and December. This spawned concerns...
about the risk of deflation—as aggregate price levels continue to fall, both consumers and businesses curtail their purchases thinking they will be able to get a lower price sometime in the future.

**Consumer Spending.** Consumer spending, which generally accounts for two-thirds of economic growth, dropped 3.5 percent in the fourth quarter of 2008, following a 3.8 percent decline in the third quarter. Since WWII, consumer spending has seen two consecutive quarterly declines only four times. The recent pullback was the first time expenditures in the two quarters have fallen by over 3.0 percent. According to a Federal Reserve report, consumer borrowing through credit cards and other consumer loans dropped to $7.94 billion in November, the biggest decline in 65 years of record-keeping, leaving total consumer credit outstanding at $2.57 trillion. The Conference Board’s Consumer Confidence Index fell from 38.6 in December to 37.7 in January 2009, a historic low for the series that began in 1967. Overall, consumer spending is now forecasted to decline by 3.3 percent in first quarter 2009 and by almost 2 percent during the second quarter. For the year, consumer spending will drop 1.0 percent, providing the economy begins its path to recovery during the third quarter. Even if the economy starts to recover by mid-year, this will still be the longest recession since the 1930s.

Spending on durable goods—big ticket items such as automobiles, home furnishings, etc.—dropped 22.4 percent in the fourth quarter, following a 14.8 percent decline in third quarter 2008. Rapidly increasing job losses, economic uncertainty, tight lending standards, falling home prices, and a loss of wealth all contributed to the decline in purchases of durable goods. Consumer expenditures on durable goods are forecasted to decline by over 11 percent during the first quarter of 2009 on an annualized basis. For the year as a whole, spending on durable goods will fall 6.0 percent, the sharpest drop since 1942 and the first decline since 1980. Spending on motor vehicles and parts will decrease about 9 to 10 percent, while spending on household furnishings and equipment will drop by 2.5 to 3 percent.

Consumer expenditures for nondurable goods, such as food, gasoline, and apparel, fell 7.1 percent in both the third and fourth quarters of 2008. Spending on nondurable goods is expected to drop by approximately 5 percent in the first quarter and by 2.0 percent for all of 2009. Expenditures for clothing and shoes will decline by 2.5 percent in 2009; spending on food and beverages will also drop 2.5 percent, largely due to a 3.5 percent decrease in spending at restaurants during the year.

**Nonresidential and Residential Business Spending.** Nonresidential business investment, which includes spending on structures and on equipment and software, dropped 19.1 percent in fourth quarter 2008, with expenditures on structures declining by 1.8 percent. Business investment in equipment and software fell 27.8 percent during the fourth quarter. Overall, however, nonresidential business spending actually increased by 1.8 percent in 2008, primarily due to an almost 12 percent increase in investment in structures during the year. These were primarily commercial projects already in the pipeline and financed before financial institutions tightened up on lending. However, as ongoing projects are completed, it will be more difficult to obtain financing for new commercial construction.

Investment in structures is forecasted to fall by almost 20 percent during the first quarter of 2009 and by around 30 percent in the second quarter. For the year, these capital expenditures are expected to drop by 15.0 percent. Business spending on equipment and software will decline by 20.0 percent in the first quarter and by about 15 percent during the second quarter, mainly due to a decrease in spending on industrial and other capital equipment and on transportation equipment. Total nonresidential investment is forecasted to decline by about 18 percent in first quarter 2009 and by over 20 percent during the second quarter.

Residential investment, including both home construction and sales, dropped 27.8 percent during fourth quarter 2008; for all of 2008, the decline was 20.8 percent. Residential construction spending alone decreased 22.3 percent during the year. Problems in the housing markets just continue to multiply—according to the Commerce Department, sales of new single-family homes in December were down 14.7 percent to a record-low annual rate of 331,000, despite prices being at their lowest levels since February 2004. Furthermore, the year over year drop in prices seen in December was the largest on record. New home sales in December were 44.8 percent below their December 2007 level.

In 2008, 482,000 new homes were sold as housing prices continued to drop and credit conditions worsened. That figure was 37.8 percent lower than the 776,000 homes sold in 2007. New-home construction fell 15.5 percent from November to December 2008 to an annual pace of 550,000, the slowest on record and 45.0 percent below 2007. According to the U.S. Department of Commerce, approximately 904,300 housing units were started in 2008, a drop of 33 percent from 2007, making the year the worst for housing starts since records were first kept in 1959. Housing starts, which peaked at 1.7 million in 2005, are expected to fall below the 500,000 level in 2009. The Standard & Poor’s/Case-Shiller Home Price Index found prices in November 18.2 percent below a year ago. Total residential investment is forecasted to decline by over 30 percent during the first quarter of 2009 and by about 20 percent in the second quarter. For the year as a whole, the decrease is forecasted to be around 20 percent. Housing starts will continue to drop through the first half of 2009.

**Employment.** In January 2009, the United States experienced the biggest monthly decline in payroll employment in 34 years. Employers shed 598,000 jobs during the month, following a loss of 577,000 jobs in December, bringing
January 2009, the economy has lost over 2.5 million jobs. If the people who are looking for a full-time job but can only find part-time work are included, the unemployment rate would swell to around 14 percent at year-end 2008, compared to 8.7 percent at the start of the recession.

Employers in nearly every industry have cut payrolls; healthcare and education are the exceptions, with a combined total of 64,000 new jobs during the last five months. Manufacturers, construction companies, and retailers have shed the most jobs during this recession—over a million manufacturing jobs and 740,000 construction jobs have been lost. Jobs have also dried up in the financial sector, the printing and publishing industry, retailing, and in the leisure and hospitality industry, primarily at hotels and restaurants. Retail trade employment, which fell by 45,000 in January, is down a total of 592,000 since its peak in November 2007.

The U.S. unemployment rate is forecasted to rise to 8.0 percent in the first quarter of 2009 and to 8.5 percent in the second; unemployment is expected to be over 9 percent by year-end. Payroll employment will decline by over 4 percent in first quarter 2009, followed by an approximately 3 percent decline during the second quarter. For all of 2009, payrolls are expected to shrink around 2.9 percent, a loss of almost 3 million more jobs. Overall, employment is expected to fall by 5.0 to 6.0 million during the current recession. Most of the job losses will be in construction, retailing, and manufacturing, where payrolls are forecasted to decline by around 9 percent.

Alabama

Employment. Alabama’s unemployment rate jumped from 3.7 percent in December 2007 to 6.7 percent in December 2008. As of December 2008, there were 138,855 people unemployed statewide, a 67 percent increase from December 2007 when the total number of unemployed was 83,516. Twelve of the state’s 67 counties had unemployment rates above 10 percent. In December 2008, Wilcox County registered the highest rate at 15.1 percent, up from 9.6 percent a year earlier. Shelby County’s unemployment rate was the lowest at 4.4 percent, albeit up from 2.3 percent in December 2007.

During the 12-month period ending in December 2008, Alabama lost a total of 41,900 jobs, with the pace of payroll losses accelerating toward the end of the year. The state’s 11 metropolitan areas, comprised of 28 counties, lost 20,100 jobs, while the remaining 39 counties experienced a loss of 21,800. The largest metro area, Birmingham-Hoover, shed 10,300 jobs during the year, followed by Dothan (-1,700); Decatur (-1,600); Montgomery (-1,400); Tuscaloosa (-1,300); and Mobile and Gadsden (-1,200). The Florence-Muscle Shoals metro area lost 600 jobs, while Anniston-Oxford dropped 400. Huntsville, which saw payroll employment reduced by 300, and Auburn-Opelika, with a drop of 100 jobs, fared the best among the metros. Job losses in Birmingham-Hoover were concentrated in retailing (-3,100), manufacturing (-1,700), educational and health services (-1,600), construction (-1,300) and leisure and hospitality (-1,000). Across the metros, a total of 7,200 manufacturing jobs were lost, including 1,400 in the Huntsville area. The sharp decline in both consumer and business spending had a significant impact on the state’s major retailing centers, with the resulting loss of 6,300 retail jobs and 2,300 leisure and hospitality (mostly restaurant) jobs across the metro areas.

Statewide, manufacturing firms shed 17,100 jobs for the 12-month period ending in December 2008. The only industries adding to payrolls were manufacturers of motor vehicles with 100 jobs and of aerospace products and parts, with an additional 400 workers during the year. Overall, however, transportation equipment manufacturing, which also includes motor vehicle parts, posted a net decrease of 1,200 jobs. Every other industry lost jobs during the year, with the decline in textiles and apparel alone totaling 3,600. Slipping consumer spending and the weak housing market negatively impacted wood products and primary and fabricated metals manufacturing, which lost 1,700 and 1,100 jobs, respectively, during the 12-month period ending in December 2008. Overall, durable goods industries shed 9,200 workers during the year and nondurable goods manufacturers dropped 7,900.

Service providing firms, which until recently were the main drivers behind new job creation, lost 20,200 jobs from December 2007 to December 2008, with most of the losses concentrated in retailing. A rapid slowdown
in consumer spending on both durable and nondurable goods toward the end of the year caused retailers to shed 7,300 workers—motor vehicle and parts businesses laid off 1,000 workers and department stores reduced employment by 1,300. Payroll employment in financial activities fell, with finance and insurance companies losing 400 jobs and real estate leasing and rental firms dropping 800 during the 12 months ending in December 2008.

In recent years, much of the job growth in the state has been in professional and business services, educational and health services, and leisure and hospitality. These industries have not been immune to the recession, however—from December 2007 to December 2008 professional and business services lost a total of 4,500 workers, of which 3,700 were in administrative support, waste management, and remediation services. Educational and health services dropped 3,500 from their payrolls, with 1,500 in educational services and 2,000 in health care and social assistance services, including 1,300 jobs lost in hospitals. Leisure and hospitality services was hit particularly hard by the retrenchment in consumer spending. Overall, the industry lost a total of 5,000 workers, including 4,500 at accommodation and food service establishments. The only sectors of the Alabama economy cushioning the shock of the rapid fall in payrolls were state and local governments. State government added 1,700 workers, while local governments added 1,900. However, most of these gains were during the first half of the year, and, with budget shortfalls now plaguing government entities, we are beginning to see declines in state and local government payrolls.

Exports. The relatively lower value of the U.S. dollar and growing economies abroad helped state exports for most of 2008, but with the recession now global in scope, we are seeing a slowdown in exports. During the first three quarters of 2008, Alabama exports totaled $12.2 billion, 1.2 percent higher than for the same period in 2007, despite a significant slowdown in the third quarter. Although exports to Germany dropped slightly during the first nine months of the year, it remains the state’s largest trading partner with exports totaling over $2.5 billion. Other major export destinations in 2008 included: Canada ($2.1 billion in exports), Mexico ($7.25 million), China ($606 million), and the United Kingdom ($521 million). On an annualized basis, China has actually surpassed Mexico as the state’s third largest trading partner. Exports to these five countries alone totaled almost $6.5 billion during the first nine months of 2008, or 54 percent of total state exports. During the nine months ending in September 2008, transportation equipment, the state’s largest export category, declined by 3.0 percent compared to the same period in 2007 and totaled approximately $4.4 billion. Other major state export industries during the first three quarters of 2008 included: chemicals ($1.8 billion); mining ($790 million); paper products ($785 million); primary metals ($764 million); machinery manufacturing ($668 million); and computer and electronic products ($484 million).

However, the continuing global slowdown, together with the gradually strengthening U.S. dollar, is likely to have a negative impact on the state’s exports going forward into 2009.

Tax Receipts. After experiencing remarkable growth in tax revenues in recent years, the state is seeing tax receipts slow significantly in the current fiscal year. During the first four months of the fiscal year ending in September 2009 (FY2009), state tax revenues totaled around $2.8 billion, down 4.4 percent, or approximately $129 million, compared to the same period a year ago. The slowdown in consumer and business spending has had a significant impact on sales tax revenues, which declined by 9.1 percent to about $632 million, almost $63 million below the same period last fiscal year. Corporate income tax receipts during the first four months of FY2009 totaled about $143 million, $30 million (17.5 percent) below the same period in FY2008. Individual income tax revenues were down 5.4 percent to approximately $958 million, about $54 million lower than the first four months of the previous fiscal year. Appropriations made to the Alabama Education Trust Fund were down about $170 million to approximately $1.7 billion, a decline of 9.1 percent from the first four months of FY2008. At the same time, appropriations to the state’s General Fund decreased by approximately $96 million, a drop of 14.9 percent, to total about $546 million.

Outlook. Alabama’s economy is forecasted to grow by 0.3 percent in 2009, assuming passage of the fiscal stimulus package currently under consideration in both houses. However, if the stimulus package is not large enough or is not implemented in a timely manner, we could see the state’s economy contract by 1.0 to 1.5 percent. Nonagricultural employment is currently forecasted to decrease by 1.0 to 1.9 percent, raising the unemployment rate to between 7.5 and 8.0 percent by the end of 2009. The biggest risk is in the length and depth of the recession.

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Given the sharp retrenchment in both consumer and business spending, any respite from oil prices or prices generally is likely to go into savings or paying down debt rather than into consumption.

While slowing demand will negatively impact almost every sector of the economy, manufacturing and retailing will continue to be hit particularly hard. The state’s construction sector is also forecasted to shed more workers as commercial projects dry up. Service providing firms could begin to add workers back to their payrolls during the second half of 2009, but most likely not in any significant numbers.

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