**Economic Outlook:**
**Third Quarter 2010**

**Alabama**

**Employment.** The state added 13,700 new jobs in May, slightly fewer than the 14,200 created in April. With job losses subsiding in recent months, nonfarm employment of 1,883,800 in May 2010 was just 16,700 below May 2009, a drop of 0.9 percent. Looking back to before the recession, annual Alabama nonfarm employment fell from a decade high of 2,005,700 in 2007 to 1,885,700 in 2009, with the loss of 120,000 jobs amounting to a 6.0 percent decline. Alabama’s nonseasonally adjusted unemployment rate dropped from 10.3 percent in April 2010 to 10.0 percent in May; still, however, above the 9.5 percent rate of May 2009. The 209,278 residents counted as unemployed in May 2010 represent a 3.3 percent increase from a year ago. Forty-three of the state’s 67 counties reported unemployment rates of 10.0 percent or above in May. Wilcox County’s 24.0 percent was the highest, while Shelby County had the lowest rate at 7.3 percent. Despite gradual improvement in Alabama’s economy, the job market remains tight, there are still a number of discouraged workers who have dropped out of the labor force, and a significant number of workers who would like a full-time job but can only find part-time employment.

Employment in goods producing industries was down by 15,600, or 2.6 percent, during the year ending in May 2010. Construction firms shed 5,900 jobs (2,800 in construction of buildings and 2,600 among specialty trade contractors), while manufacturing lost 9,300 workers. It should be noted, however, that these are some of the smallest job losses we have seen since the beginning of the recession, indicating that the economy continues to improve gradually albeit without any major gain in payrolls. Job losses in manufacturing industries slowed considerably in May—firms producing durable goods lost 6,000 jobs from a year ago, while nondurable goods producing firms shed 3,300 workers. Job losses over the last year among durable goods firms were concentrated in wood products manufacturing (2,000); primary and fabricated metals (1,400); machinery manufacturing (800); computer and electronic products (1,100); transportation equipment manufacturing (800), primarily in motor vehicle manufacturing; and furniture and related products (1,000). Payroll losses in nondurable goods producing firms were primarily associated with textiles and apparel industries (1,800), paper manufacturing (900), and food manufacturing (400).
Although results over the past year were mixed, Birmingham-
All of the state’s 11 metro areas added jobs in May 2010, workers, largely due to temporary census-related jobs. Federal government employment grew by almost 11,000 (1,400). While state governments shed 1,400 jobs and local and utilities (500); information (1,900); and other services that have experienced a net loss of payrolls over the past year, dropping 5,600 jobs for a decline of 5.6 percent. Financial industry employment losses have been spread across the board, with credit intermediation and related activities down 1,200; real estate and rental and leasing losing 1,000; and insurance carriers shedding 1,500 workers. Retailers laid off 1,600 employees during the 12-month period ending in May 2010, with most cuts at food and beverage stores (1,800). Despite relatively weak consumer spending, general merchandise stores added 1,500 workers. Other service providing sectors that have experienced a net loss of payrolls over the past year include: wholesale trade (2,600); transportation, warehousing, and utilities (500); information (1,900); and other services (1,400). While state governments shed 1,400 jobs and local governments lost 1,600 between May 2009 and May 2010, federal government employment grew by almost 11,000 workers, largely due to temporary census-related jobs.

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Service providing businesses have shown significant improvement in recent months, albeit at a very slow pace. During the 12-month period ending in May 2010, these firms lost just 1,100 jobs, a drop of less than 0.1 percent. Some segments actually added to payrolls and, for those that shed workers, the loss of jobs was much smaller than the layoffs seen just a few months ago. Between May 2009 and May 2010, educational services gained 3,800 employees, while leisure and hospitality added 1,600, all in accommodation and food services. Professional and business services, usually one of the fastest growing segments of the state’s economy, added 900 new workers in May, putting employment above year-ago levels for the first time since the start of the recession. Sector job gains were only in administrative support and remediation services, which added 2,600 positions in May 2010 and 4,600 since May 2009.

The financial activities sector saw the largest losses over the past year, dropping 5,600 jobs for a decline of 5.6 percent. Financial industry employment losses have been spread across the board, with credit intermediation and related activities down 1,200; real estate and rental and leasing losing 1,000; and insurance carriers shedding 1,500 workers. Retailers laid off 1,600 employees during the 12-month period ending in May 2010, with most cuts at food and beverage stores (1,800). Despite relatively weak consumer spending, general merchandise stores added 1,500 workers. Other service providing sectors that have experienced a net loss of payrolls over the past year include: wholesale trade (2,600); transportation, warehousing, and utilities (500); information (1,900); and other services (1,400). While state governments shed 1,400 jobs and local governments lost 1,600 between May 2009 and May 2010, federal government employment grew by almost 11,000 workers, largely due to temporary census-related jobs.

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Hoover’s net loss of 13,900 jobs between May 2009 and May 2010 was the largest, followed by Mobile (3,400), Montgomery (2,800), Dothan (1,200), Huntsville (300), and Anniston-Oxford (100). Four metros actually added to employment over the past year, mostly in recent months. Tuscaloosa saw 900 new jobs, Auburn-Opelika and Florence-Muscle Shoals each gained 400, while Decatur added 300. Payroll employment in Gadsden was flat. Metro area job gains were in service providing businesses, particularly in the generally low-wage leisure and hospitality industry, and with the federal government. Every metro area saw flat or declining employment in manufacturing, where wages are among the highest. As of May 2010, Huntsville reported the lowest unemployment rate at 7.7 percent; unemployment was worst in Mobile at 11.0 percent. Several other metros also saw double-digit unemployment, including Decatur (10.5 percent) and Anniston-Oxford and Gadsden, both with 10.0 percent rates.

Exports. Alabama exports climbed from $2.8 billion in first quarter 2009 to almost $3.5 billion in the first quarter of 2010, an increase of approximately 25 percent. During the same period, exports to Canada, one of Alabama’s largest trade partners, rose from $463 million to almost $817 million, a 77.0 percent increase. While exports to China soared from $194 million to $444 million, exports to Germany, another major trading partner, dropped from $382 million to $342 million. Transportation equipment was still the state’s top export in the first quarter of 2010, with shipments totaling nearly $1.1 billion, up from $829 million during first quarter 2009. Other major exports during the first three months of 2010 included: chemicals ($484 million), mining ($328 million), paper products ($208 million), machinery manufacturing ($236 million), and primary metals ($149 million).

Tax Revenues. Even though state tax receipts continue to show a decline over the previous fiscal year, the rate of decline is gradually slowing as the economy shows modest signs of improvement. For the first nine months of the current fiscal year (FY2009-2010) through June 2010, state tax revenues were down 3.0 percent (or $196 million) from the same period a year earlier and totaled around $6.3 billion. Sales tax revenues were up 0.4 percent (about $6 million) to approximately $1.4 billion. At $344 million, corporate income tax receipts were $47 million lower compared to the first nine months of FY2008-2009. Individual income tax revenues fell by 4.4 percent for the first three quarters of the current fiscal year, down $115 million to about $2.5 billion. Slowing job losses and a gradually improving Alabama economy should help stabilize tax receipts in the coming months.

For the first nine months of FY2009-2010, appropriations to the Alabama Education Trust Fund, which are primarily from income and sales taxes, dropped approximately $243 million, or about 6.0 percent, to just over $3.8 billion. At the same time, appropriations to the state’s General Fund, directed to noneducation-related spending, declined about $237 million to approximately $879 million, a drop of 21.2 percent.
Outlook. Alabama’s GDP is expected to show positive growth this year. For all of 2010, real GDP is forecasted to increase 2.5 to 3.0 percent, with payrolls rising by 0.7 percent. The unemployment rate will fall, although at a very slow pace as improving economic conditions and labor markets lead more people to enter or re-enter the workforce. Most job growth in the coming months and going forward into 2011 is expected to be in service providing businesses.

Business sentiment, measured quarterly by the Center for Business and Economic Research’s Alabama Business Confidence Index™ (ABCI), has steadily improved since a low of 31.5 in the first quarter of 2009. The third quarter 2010 ABCI of 51.6 is up 2.1 points from a consensus of 49.5 in the second quarter, indicating that an economic recovery in terms of GDP is most likely underway and will strengthen in the coming months. An index value above 50 indicates that businesses are generally more optimistic about the economic environment and their prospects going forward. All of the industry indexes—sales, profits, hiring, and capital expenditures—moved above 50 for the third quarter of 2010, signaling a broad-based recovery.

While Alabama’s economy is now rebounding, the course of recovery will not be smooth. Economic development prospects are picking up and projects, including the ThyssenKrupp steel plant, that were set in motion before the recession are beginning to come online. Improved consumer demand is reviving the state’s automotive manufacturing industry. And BRAC-related developments are bringing new jobs to Huntsville’s Redstone Arsenal and related contractors as well as population gains in both North Alabama and the Southeastern part of the state (in conjunction with the expansion of Fort Benning). But challenges to state funding for services and public education as stimulus money is used up are looming. The recent oil spill in the Gulf and its effects on the state will have both short- and long-term impacts on the state’s economy. The biggest risk to a sustainable economic recovery in the state is payroll employment. But recent job gains suggest that chances for the state’s economy to revert into another recession are slight.

Output from the state’s manufacturing sector is expected to increase by 4.0 percent in 2010. However, manufacturing employment will continue to lag any growth in GDP, with payrolls expected to decline 2.0 percent in 2010. Motor vehicle manufacturing should continue to rebound, with production forecasted to increase by 6.0 percent in 2010 as demand for both cars and light trucks rises in both domestic and overseas markets. Most service-related businesses will see some growth, albeit at a more sluggish pace and without adding any substantial number of new workers to their payrolls, at least during the next few months. Both residential and commercial construction will remain a drag on the economy as developers still face tight lending conditions, frozen securitization markets for loans for major projects, and rising vacancy rates in an already-overbuilt commercial market. Commercial construction is not expected to begin to recover until 2011.

In terms of payroll employment, most sectors of the state’s economy will experience a gradual recovery for the remainder of 2010. Among durable goods manufacturers, transportation equipment and related industry should see modest growth in payrolls. Service providing businesses will generally add new workers, although employment gains are expected to be tepid. Professional and business services firms are forecasted to increase employment by about 1,000 during the year due to pent-up demand; however, the change in payrolls is expected to be significantly below the rate of growth these businesses experienced before the start of the recession. For 2010 as a whole, the leisure and hospitality sector could create approximately 2,000 new jobs, while educational and health services
will add 3,000 workers. However, many nondurable goods producers will continue to shed workers and Alabama’s construction industry, particularly commercial construction, could lose another 6,400 jobs this year. Despite the fact that job growth is resuming in 2010, employment is not expected to reach its prerecession level until at least 2014.

State tax receipts are forecasted to decline slightly in FY2009-2010, albeit at a much slower pace than was experienced during the previous fiscal year. Under our most optimistic scenario, if the Alabama economy gets back on solid footing, overall receipts will decline by around 0.5 to 1.0 percent. However, in our baseline scenario, where economic growth continues on its current path and there is no significant improvement in payrolls, total tax revenues will decline by 2.0 to 2.5 percent. Our most pessimistic scenario, where the recession continues to drag on or the economy reverts into another recession, forecasts a 3.0 to 4.0 percent drop in overall tax revenues. However, in our estimation, the chances for this last scenario are slim.

**United States**

**Gross Domestic Product (GDP).** Following a 5.6 percent rate of growth in fourth quarter 2009, real GDP (the value of goods and services produced in the United States adjusted for inflation) increased by only 2.7 percent in the first quarter of 2010. Positive contributions from consumer spending, inventory investment, exports, and nonresidential fixed investment in the first quarter were offset by negative effects of cutbacks in state and local government spending and residential fixed investment, as well as an increase in imports, which is subtracted from GDP. Stronger growth in the fourth quarter of 2009 mainly reflected the inventory cycle, as production rose to replenish inventories depleted during the recession. With inventories largely rebuilt, the pace of manufacturing sector output growth slowed in the first quarter of 2010. Real GDP is expected to grow by 3.8 percent in the second quarter, followed by a 2.3 percent rate of increase in the third. We are looking for growth only in the 2.0 to 2.5 percent range during the second half of the year. For all of 2010, GDP is now expected to increase by approximately 3.0 to 3.5 percent. The increase in GDP in 2010 will mainly reflect positive contributions from consumer spending (2.7 percent); nonresidential business spending (3.3 percent); residential investment (3.0 percent); exports (12.0 percent); and federal government expenditures (3.6 percent). State and local government spending will be flat or see at most a 0.5 percent increase. Imports, which are a subtraction from GDP, are expected to increase about 12 percent in 2010.

**Consumer Spending.** Consumer spending accounts for approximately 70 percent of the U.S. economy. After increasing by 1.6 percent in the fourth quarter of 2009, expenditures rose 3.0 percent in first quarter 2010. Expected consumer expenditure gains of 2.3 percent in the second quarter and 2.8 percent in the third will contribute to around a 2.7 percent increase for 2010 as a whole. This is a significant rebound from the 0.6 percent decline in consumer spending during 2009. From its bottom in early 2009, consumer wealth has increased by approximately $6.0 trillion, although it remains about $12 trillion (18 percent) below the mid-2007 peak. While many consumers still face debt, credit, and employment concerns, a gradually improving job market over the remainder of this year is expected to boost household income to support a sustained recovery in consumer spending.

Following a decline of 3.9 percent in 2009, spending on durable goods increased by 12.0 percent in the first quarter of 2010 and is forecasted to grow around 14 percent in the second and 12 percent in the third quarter. For all of 2010, spending on durable goods will increase by almost 10 percent. The fastest growing segments are expected to be new motor vehicles (14.0 percent), new light trucks (approximately 20 percent), information processing equipment (almost 20 percent), computers and peripheral equipment (about 21 percent), and software and accessories (14.5 percent). Spending on nondurable goods,
which rose 3.9 percent during first quarter 2010, should increase 3.2 percent in the second quarter and 2.7 percent in the third. Expenditures for nondurable goods could improve 3.0 percent during the year. Sales of off-premises food and beverages will increase by 3.3 percent, while sales of clothing and footwear are forecasted to post about a 7 percent gain during 2010.

**Business Spending.** Overall nonresidential fixed investment rose 2.2 percent in the first quarter of 2010, rebounding from the 17.8 percent drop seen in 2009. For the second and third quarters, business spending will increase by around 11 percent and 5 percent, respectively. Across the year as a whole, business expenditures are forecasted to increase approximately 3 percent. Spending by firms on equipment and software, which rose 11.4 percent during first quarter 2010, is expected to climb 12.4 percent in the second quarter and a stronger 16.8 percent in the third. Spending on equipment and software will be a bright spot across the year, increasing by almost 12 percent. Pent-up demand from expenditure cutbacks in 2009 will propel exceptionally strong investment in computers and peripherals (up almost 27 percent) and communications equipment (10.6 percent increase). After falling by 48.7 percent in 2009, expenditures by firms on transportation equipment will rise 38.5 percent in 2010. However, purchases of industrial equipment are forecasted to increase only about 3 percent this year. Sluggish commercial real estate markets will continue to depress investment in structures—after a decline of 19.8 percent in 2009, spending on structures will fall 13.0 percent in 2010. Approximately $1.5 trillion of commercial loans will have to be refinanced over next four to five years, and almost 45 percent of the already restructured loans are now delinquent. Commercial construction will remain a drag on the overall economy in 2010.

Residential fixed investment, which includes both home construction and sales, fell by 20.5 percent in 2009 and dropped another 10.3 percent in the first quarter of 2010. It is expected to increase 3.0 percent in 2010, primarily as a result of the temporary jump in sales due to the homebuyer’s mortgage tax credits, which expired this spring. Sales of new homes are forecasted to be approximately 420,000 units, compared to 374,000 in 2009, up about 3 percent, while sales of existing homes will increase from 5.1 million units in 2009 to 5.3 million units in 2010. Home prices continue to fall though, and, with the tax credits expired, home sales will also weaken. Sales of new homes dropped 33.0 percent from April to May 2010, the largest decline since the government started compiling the data in 1963. The May sales rate of 300,000 units was 18.3 percent below that of May 2009, when sales totaled 367,000. Almost 25 percent of homeowners with mortgages have loans larger than the value of their homes and 65 percent of homeowners that have mortgage debt have lost their equity—from 2007 to 2009 almost $6 trillion in home equity was wiped out by falling home prices. The number of homes repossessed, the final stage of the foreclosure process, reached 257,944 during the first quarter. That is up 9 percent from the previous quarter and 35 percent from the first quarter of 2009.

**Employment.** The U.S. unemployment rate improved from 9.7 percent in May to 9.5 percent in June. The decline in unemployment came because almost 652,000 people dropped out of the labor force. Nonfarm payroll employment declined by 125,000. Termination of 225,000 temporary census workers was responsible for the decline in employment—the private sector actually added 83,000 jobs in June. A 39,000 increase in employment in professional and business services was largely associated with temporary help services (21,000); these services have added 379,000 jobs since September 2009. Manufacturing employment increased by 9,000 over May and factories have added 136,000 jobs during the past six months. Payrolls in healthcare also rose by 9,000 in June. Over the past 12 months, the healthcare sector has added almost 217,000 jobs, while educational services has gained 13,000. Construction lost another 22,000 jobs, mostly associated with commercial or nonresidential construction. Financial activities-related businesses shed 15,000 workers, while state and local governments cut 8,000 jobs. Most other sectors of the economy showed little or no change in June.

Close to 8.5 million jobs have been lost since the recession began in December 2007. Just to keep up with population and labor force growth and hold the unemployment rate at its current level, the economy will have to add 100,000 jobs a month. Approximately 15 million Americans were unemployed in June, and almost 46 percent (6.8 million) have been unemployed for over six months. The underemployment rate, which counts people whose hours have been cut along with those working part-time for lack of a full-time position, stood at 16.5 percent in June. As the economy begins to improve, more workers who are currently not actively looking for work—the discouraged workers—will begin to look for work and be added to the labor force, which could keep the unemployment rate at a relatively high level at least through 2010. The U.S. economy is expected to add approximately 1.5 million jobs in 2010, only enough to absorb a fraction of the currently unemployed. A sustained economic recovery will require the addition of at least 200,000 to 250,000 jobs every month. We do not believe that the U.S. economy is heading for a double-dip recession, but we do not expect to see a rapid recovery either. Stimulus programs for housing and consumer spending have expired, while the inventory-cycle boost provided by the manufacturing sector is fading.

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