THE CONNECTICUT
ECONOMIC DIGEST

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IN THIS ISSUE...

In April...

Nonfarm Employment

Connecticut 1,617,000
Change over month .... +0.19%
Change over year .... -0.9%

United States 130,161,000
Change over month .... +0.22%
Change over year .... -1.0%

Unemployment Rate

Connecticut 9.0%
United States 9.9%

Consumer Price Index

United States 218.0
Change over year 2.3%

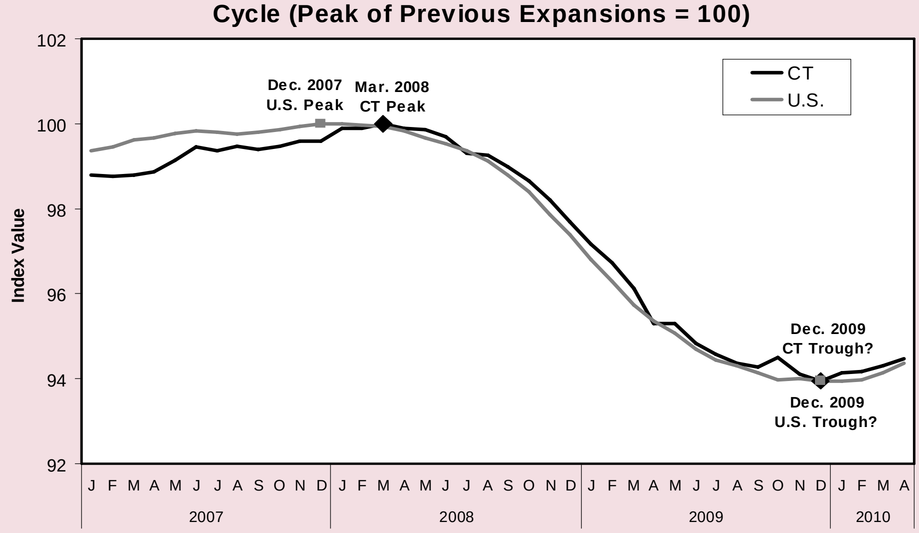
Forecast to 2011: Navigating the Crosscurrents

By Daniel W. Kennedy, Ph.D., Senior Economist, DOL

On May 6, 2010, the Dow plunged nearly 1,000 points before "recovering" to close down 347.80 (-3.20%)[1] points—an unpleasant reminder of 2008. Despite the infamous "fat finger" glitch and model-driven threshold selling, the underlying driver of the market's gyrations was the sovereign debt crisis centered on Greece. It is a stark reminder that the world's financial system is still very fragile. On the other hand, the U.S. jobs report for April 2010, which came out the next day, showed that the national economy had added 290,000 jobs in April[2]—the best monthly performance in four years. These two events highlight the strong crosscurrents that are pulling the economy, as this apparent turning point proceeds.

Interestingly, Connecticut seems to have done something over this cycle that it has not done before in the post-Cold War era. Nonfarm employment turned down going into the last recession after it did in the U.S. Graph 1 presents an index of U.S. and Connecticut nonfarm employment, with both index values equal to 100 at their respective peaks in the last recovery/expansion. The U.S. officially went into recession in December 2007, and employment turned down that same month. Connecticut's nonfarm employment did not turn down until March 2008. Further, it appears that the U.S. and Connecticut's employment cycles bottomed in December 2009. If these turning points hold up in next year's benchmark, it would mean that Connecticut recovered with the U.S.—again, a first in the post-Cold War era. On the other hand, while the U.S. had job declines of 3.0% per year on an annualized basis over 24 months, Connecticut's employment con-

GRAPH 1: CT and U.S. Nonfarm Jobs Trajectory-Current Cycle (Peak of Previous Expansions = 100)



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tracted at 3.5% per year annualized over 21 months.

RECESSION AND PANIC: Assessing the Damage to Labor Markets

Table 1 shows historical fourth-quarter employment for 19 industry sectors and a 2011 forecast. Like the U.S., the steepest decline occurred in Connecticut's construction employment. Jobs declined by 24% in both the U.S. and Connecticut construction sectors between 2007Q4 and 2009Q4. This, of course, is the consequence of the collapse of the sub-prime mortgage/housing asset bubble.

The second largest decline for the U.S. was in manufacturing jobs (-16%). For Connecticut, manufacturing job losses were the third steepest sectoral decline, but they accounted for 59% of all jobs lost in the goods producing sector. Fifty-four percent of Connecticut's manufacturing job losses were in the durable goods subsector. However, it was Connecticut's non-durable goods subsector that declined the most steeply, contracting by 22.4% compared to 9.2% for durable goods.

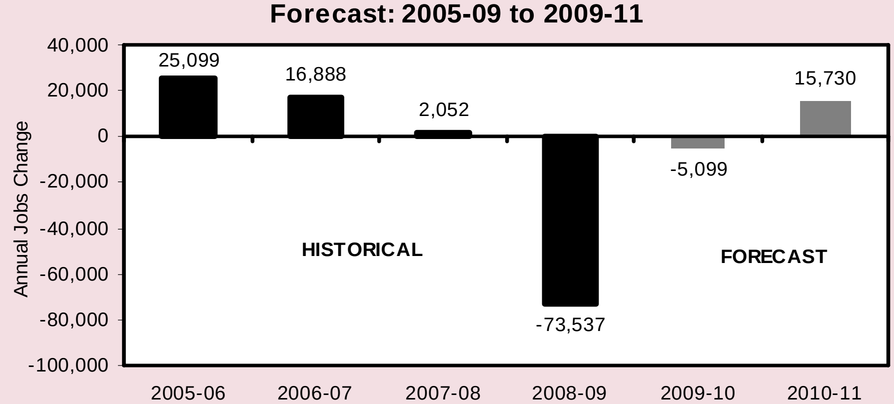
Again in line with the U.S., a significant share of Connecticut job losses in the private service providing industries were concentrated in retail trade and administrative, support and waste management services (hereafter, admin and support). These two sectors accounted for 54% of U.S. job losses in services, and for 53% of Connecticut's employment losses. U.S. admin and support jobs fell by 14%, while Connecticut lost 16% of jobs in this sector. In addition, 70% of Connecticut's admin and support job losses were in employment services, reflecting increased use of contingent and temporary workers. The decline in retail trade jobs was similar for both the U.S. and Connecticut: 7.3% for Connecticut and 7.6% for the U.S.

Even during the most severe financial and economic crisis since the Great Depression, a few industry sectors actually added jobs. For both Connecticut and the U.S., educational services and health care and social assistance (HCSA) added jobs between 2007Q4 and 2009Q4. In addition, the U.S. utilities sector added jobs over the eight-quarter period. Educational services jobs grew at a weaker pace in Connecticut (+0.1%) than in the U.S. (+4.2%). On the other hand, HCSA jobs in Connecticut grew at 4.4% over the 2007Q4-2009Q4 period compared to 4.3% for the U.S.

WHAT'S AHEAD: The Outlook for 2011Q4

Graph 2 summarizes the annualized job changes from 2005 to 2009 and the expected annual job changes over the two forecast years: 2010 and 2011. On an annual average basis, it is expected that Connecticut's economy will recover from the steep losses of 2009, but still register a decline of 5,100 jobs in 2010. It is expected that annual job growth will turn positive again in 2011, and that the State's economy will recover 15,700 jobs. This would represent a net gain of 10,600 jobs over the two-

GRAPH 2: CT Annual Job Changes - History and Forecast: 2005-09 to 2009-11



year forecast period, on an annual basis.

Turning to individual sector forecasts, the goods producing sector is expected to continue losing jobs over the forecast period. However, losses will decelerate from 40,800 between 2007Q4 and 2009Q4, to 4,500 jobs over 2009Q4-2011Q4. Though losses are expected to diminish in the construction sector, the continued drag of the housing market on the economy will limit growth. Manufacturing, after hemorrhaging 24,100 jobs between 2007Q4 and 2009Q4, is expected to return to trend losses. This implies the elimination of about 4,200 more jobs over the 2009Q4-2011Q4 forecast period. Manufacturing will continue to restructure, including downsizing and outsourcing.

After losing 25,200 jobs over the 2007Q4-2009Q4 period, the service providing sector is expected to return to job growth over the forecast period, adding 24,600 jobs. Though a turnaround from recession lows, the projected job growth in services is quite modest compared to the 51,100 jobs created over the 2005Q4-2007Q4 period as the last expansion was coming to a close. Once again, health care and social assistance (HCSA) is projected to account for a significant portion of net job gains over the forecast horizon as it has over the historical periods depicted in Table 1. HCSA is expected to add 9,400 jobs between 2009Q4 and 2011Q4, and account for 38% of all the net job gains in the service providing sector. However, the growth rate is expected to slow from the 4.4% pace between 2007Q4 and 2009Q4 to 3.7% over 2009Q4-2011Q4. The chief culprit affecting the slowdown in growth is the hospital subsector. Year-to-year, job growth at Connecticut's hospitals began slowing after the middle of 2008, and by the end of 2009 it was actually negative. It is expected that this drag on HCSA job growth will persist over the forecast horizon.

Another previously strong-growing sector, education, may also be facing some severe headwinds going into the forecast period. Its pace has already slowed from a 7.7% rate (+12,700) between 2005Q4-2007Q4 to flat over 2007Q4-2009Q4. However, the growth rate is expected to be slight at 4.0% (+7,100) over the 2009Q4-2011Q4 forecast period. Student demand remains high, especially at the community college level. Many take advantage of the downturn to change careers or improve their skills. However, budget cuts at the state level are restraining the response to the increase in demand. Further, given the state's budget deficit and consequent cuts to local government aid, education budgets are being slashed. Thus, even this modest job growth forecast may be overly optimistic.

After losing 15,100 jobs over the 2007Q4-2009Q4 period, admin and support services is expected to add 4,100 jobs over the forecast period. Driving the change in this sector is employment services. It is expected that employers will rely very heavily on temporary and contingent workers over the coming recovery and beyond. In addition, changes in job growth in this industry seem to telegraph impending turning points in the business cycle.

Another sector that experiences large swings over the business cycle is professional, technical, and scientific services. Computer systems and design is particularly sensitive to the recession, accounting for three-quarters of the sector's job growth between 2005Q4 and 2007Q4, and one-quarter of the

--Continued on page 5--

TABLE 1: Connecticut Nonfarm Employment: History and Forecast

INDUSTRY	HISTORICAL			FORECAST	NUMERICAL CHANGES			PERCENT CHANGES		
	2005:Q4	2007:Q4	2009:Q4	2011:Q4	2005-07	2007-09	2009-11	2005-07	2007-09	2009-11
TOTAL	1,649,936	1,692,218	1,624,730	1,646,119	42,283	-67,489	21,390	2.56	-3.99	1.32
GOODS PRODUCING	261,598	261,853	221,022	216,554	255	-40,831	-4,467	0.10	-15.59	-2.02
Mining	749	749	609	685	0	-139	75	-0.04	-18.61	12.38
Construction	66,446	70,464	53,854	53,553	4,018	-16,609	-302	6.05	-23.57	-0.56
Manufacturing	194,403	190,641	166,558	162,317	-3,763	-24,083	-4,241	-1.94	-12.63	-2.55
SERVICE PROVIDING	1,363,869	1,414,946	1,389,752	1,414,369	51,077	-25,194	24,617	3.74	-1.78	1.77
Wholesale Trade	66,951	68,279	63,853	65,087	1,328	-4,425	1,234	1.98	-6.48	1.93
Retail Trade	197,475	197,521	183,095	183,041	46	-14,426	-54	0.02	-7.30	-0.03
Transportation and Warehousing	53,347	53,951	49,464	51,500	604	-4,487	2,036	1.13	-8.32	4.12
Utilities	8,478	6,685	6,590	6,697	-1,793	-95	107	-21.15	-1.42	1.63
Information	37,629	38,153	34,009	33,158	524	-4,144	-851	1.39	-10.86	-2.50
Finance and Insurance	118,479	123,339	116,694	114,933	4,860	-6,645	-1,761	4.10	-5.39	-1.51
Real Estate and Rental and Leasing	20,946	20,937	18,977	18,498	-9	-1,960	-479	-0.04	-9.36	-2.52
Professional, Scientific, and Technical Services	89,442	93,827	85,392	88,961	4,385	-8,435	3,570	4.90	-8.99	4.18
Management of Companies and Enterprises	24,923	27,076	27,160	27,838	2,153	84	678	8.64	0.31	2.50
Admin and Support/Waste Manage/Remediation	89,456	91,785	76,656	80,716	2,330	-15,129	4,060	2.60	-16.48	5.30
Educational Services	164,730	177,404	177,556	184,632	12,675	151	7,076	7.69	0.09	3.99
Health Care and Social Assistance	229,756	241,328	251,895	261,282	11,572	10,567	9,387	5.04	4.38	3.73
Arts, Entertainment, and Recreation	43,437	42,540	40,638	41,637	-896	-1,902	999	-2.06	-4.47	2.46
Accommodation and Food Services	105,336	113,137	110,158	111,366	7,801	-2,979	1,208	7.41	-2.63	1.10
Other Services	56,494	58,747	56,523	58,284	2,254	-2,225	1,762	3.99	-3.79	3.12
Government**	56,991	60,235	91,093	86,738	3,244	30,858	-4,355	5.69	51.23	-4.78

SOURCE: Connecticut Department of Labor, Office of Research NOTE: Data not seasonally adjusted

**State and local government employment did not actually increase by 30,858 between 2007Q4 and 2009Q4. Reporting requirements changed, which caused a jump in jobs reported by the State and local governments.

--Continued from page 3--

sectoral losses over 2007Q4-2009Q4. Also contributing 1,000 jobs each to the 8,400 jobs lost in professional, technical, and scientific services were architectural and engineering services, driven by the housing bust, which accounted for 26% of the job losses; advertising, which accounted for 16% of the losses; and legal services, which contributed to 14% of the sector's job losses. A good portion of the 3,600 expected new jobs in the professional, technical, and scientific services sector between 2009Q4 and 2011Q4 will be in computer systems and design. Jobs in this industry are tied to other sectors, including financial services.

Though the finance and insurance sector's share of the state's employment at first declined and then recovered, its share of output and earnings have steadily grown over the last two decades. By 2009, in spite of the financial crisis, finance and insurance accounted for a larger share of Connecticut's economy than manufacturing, which has steadily declined.

The finance subsector contributed 55% of the sector's job losses, even though it represents only 42% of the sector's total jobs. The principal activity under this heading is credit intermediation, which includes banks and other depository and non-depository institutions. Though they accounted for only 26% of credit intermediation jobs in 2007Q4, non-depository institutions accounted for two-thirds of the industry's job losses between 2007Q4 and 2009Q4. Reflecting the reach of the housing bust, the non-depository employment declines were concentrated in real estate credit and sales financing. Job losses in depository institutions, which include commercial banks and savings institutions, began to accelerate in 2009 on a YTY basis. Again, driven by the continued weakness in the housing market and the persistence of foreclosures, it is expected that employment losses in depository institutions, real estate credit, and sales financing will continue, though the pace will slow from a 6.4% decline between 2007Q4 and 2009Q4 to a 1.5% decline over the forecast period. Insurance, though recovering from the 2,700 job decline between 2007Q4 and 2009Q4, is still expected to shed another 650 jobs over the forecast period.

RISKS TO THE FORECAST

A major risk on the downside is posed by the currently unfolding sovereign debt crisis in Europe, centered around Greece, but possibly other countries as well. After Canada and Mexico, Europe is the most important U.S. export market. This is particularly true for Connecticut, as two of the state's three largest export destinations, France and Germany, are members of the Eurozone. The end of the first-time homebuyer's tax credit and the Fed's exiting the secondary mortgage market may cut short what appeared to be possible life-signs in the housing market. In addition, $1 trillion in ARMs are scheduled to re-set in 2010 and 2011[3]. This could set off a new wave of foreclosures. Thus, the housing sector, with its consequent multiplier effects, will continue to act as a drag on economic growth throughout the forecast period. ■

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[1] YAHOO FINANCE, http://finance.yahoo.com/q?s=^DJI Accessed on May 6, 2010.
[2] THE EMPLOYMENT SITUATION – APRIL 2010, U.S. BLS (May 7, 2010)
[3] See CSMonitor.Com, $1 trillion mortgage bomb still ticking away (March 5, 2010) < http://www.csmonitor.com/Money/The-Daily-Reckoning/2010/0305/1-trillion-mortgage-bomb-still-ticking-away> Accessed on May 12, 2010.

GENERAL ECONOMIC INDICATORS

(Seasonally adjusted)	1Q 2010	1Q 2009	CHANGE NO.	CHANGE %	4Q 2009
Employment Indexes (1992=100)*					
Leading	115.1	111.6	3.5	3.1	114.3
Coincident	102.0	105.6	-3.6	-3.4	102.0
General Drift Indicator (1986=100)*					
Leading	NA	NA	NA	NA	NA
Coincident	NA	NA	NA	NA	NA
Farmington Bank Business Barometer (1992=100)**	117.9	120.8	-2.9	-2.4	119.0
Philadelphia Fed's Coincident Index (July 1992=100)***	**APR**	**APR**			**MAR**
(Not seasonally adjusted)	**2010**	**2009**			**2010**
Connecticut	154.2	154.5	-0.3	-0.2	153.5
United States	157.8	158.3	-0.5	-0.3	157.2

*Sources: *The Connecticut Economy, University of Connecticut **Farmington Bank ***Federal Reserve Bank of Philadelphia*

The Connecticut Economy's **General Drift Indicators** are composite measures of the four-quarter change in three coincident (Connecticut Manufacturing Production Index, nonfarm employment, and real personal income) and four leading (housing permits, manufacturing average weekly hours, Hartford help-wanted advertising, and initial unemployment claims) economic variables, and are indexed so 1986 = 100.

The **Farmington Bank Business Barometer** is a measure of overall economic growth in the state of Connecticut that is derived from non-manufacturing employment, real disposable personal income, and manufacturing production.

The **Philadelphia Fed's Coincident Index** summarizes current economic condition by using four coincident variables: nonfarm payroll employment, average hours worked in manufacturing, the unemployment rate, and wage and salary disbursements deflated by the consumer price index (U.S. city average).