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In April...

Nonfarm Employment

Connecticut..... 1,625,100
 Change over month +0.49%
 Change over year +1.2%

United States 131,028,000
 Change over month +0.19%
 Change over year +1.0%

Unemployment Rate

Connecticut..... 9.1%
 United States 9.0%

Consumer Price Index

United States 224.9
 Change over year 3.2%

The Ups and Downs of Recovering from a Balance Sheet Recession: The Outlook to 2012

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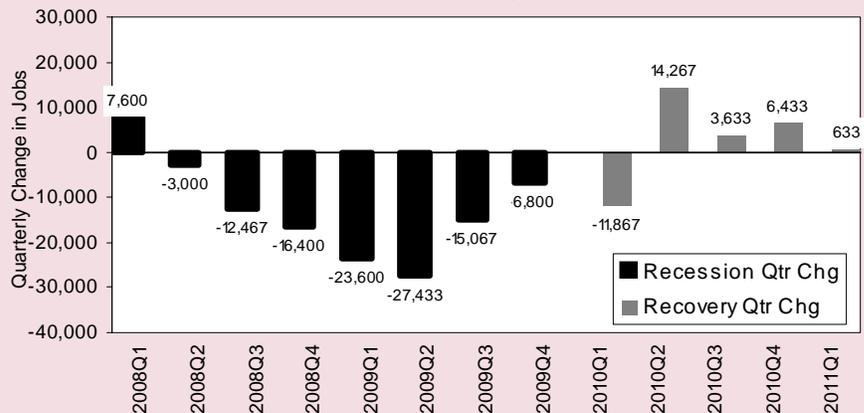
The ups and downs of this recovery continue as U.S. GDP growth decelerated from 3.1% (on an annualized basis) in 2010Q4 to 1.8% in 2011Q1.¹ But then, U.S. nonfarm payroll employment grew by 244,000 in April.² After the killing of Osama bin Laden, commodity prices, including oil, plummeted the first week of May. However, this may have also been driven by the retreat of speculators and a bearish outlook for the world economy.

The recent downturn was no “ordinary” recession, and we are currently in anything but a “normal” recovery. This recovery has followed the first U.S. systemic banking panic since the 1930s, the first collapse of a shadow banking system since 1907,³ and the first succession of collapses in asset bubbles in housing and the stock market, in conjunction with unsustainable levels of household debt

since the 1920s.⁴ This resulted in what has been called a *Balance Sheet Recession*.⁵ The Great Depression was a balance sheet recession, as was the recession that followed the collapse of Japan’s real estate bubble in 1989. Balance sheet recessions are steeper and last longer than non-balance sheet recessions, and they are followed by weaker recoveries.

Despite the severity of the recession and the weakness of the recovery, Connecticut seemed to bounce back better than the nation. The state’s nonfarm employment recovered in January 2010, one month before the U.S., and Connecticut’s job recovery was relatively stronger than the nation’s. But as the U.S.’s recovery in jobs, particularly in private sector jobs, began gathering momentum, Connecticut’s job recovery seemed to sputter. As depicted in Graph 1, even at the lower quarterly fre-

GRAPH 1: CT's Quarterly Job Change, 2008Q1-2011Q1



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quency, Connecticut's job changes are fairly volatile. Nevertheless, there does appear to be a significant downshift in the state's job creation rate going into 2011.

ONE YEAR INTO CONNECTICUT'S JOB RECOVERY

The base period of the current forecast round is 2008Q4 to 2010Q4. The following focuses on the last segment (2009Q4-2010Q4) of the base period, which includes the first four quarters of the current recovery.

Sectors That Drove the State's Job Recovery

Between 2009Q4 and 2010Q4, nine of Connecticut's major industry sectors added nearly 16,000 net new jobs, while 10 sectors eliminated 8,000 jobs. The result: 8,000 net new jobs were added to Connecticut's economy. Twenty-seven percent (4,164) of the jobs added to the state's economy were in health care and social assistance. Growth was about evenly split between the health care services and social services sub sectors, with modest growth in the hospital sub sector.

Administrative and support and waste management (admin. and support) sector was the next largest contributor to job gains. This sector accounted for 24% (3,756) of Connecticut's new jobs between 2009Q4 and 2010Q4. In addition, its growth of 4.9% was the strongest of any sector. Ninety-four percent of the jobs created were in employment services subsector, which is largely temporary help, reflecting

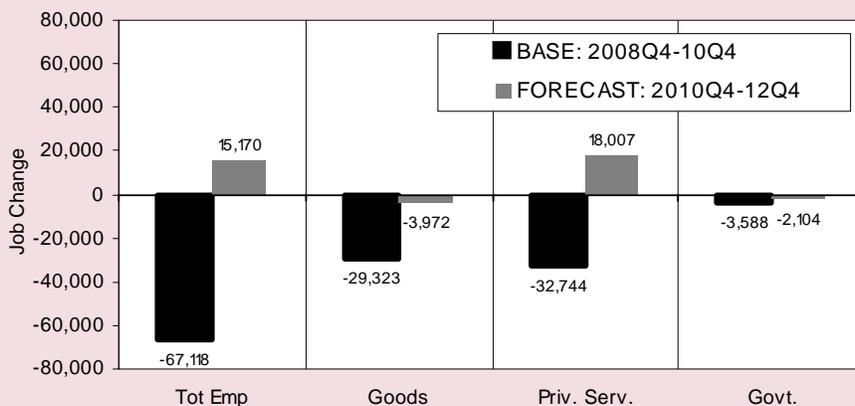
the changing structure of the economy where using contingent workers has grown significantly over the last two decades.

Accommodation and food services accounted for 12.8%, or 1,991 net new jobs. Virtually all of the growth was concentrated in food services and drinking places. Retail trade (+1,555), education (+1,445), and professional, scientific, and technical services (+1,302) each added more than 1,000 jobs to Connecticut's economy. Eighty-seven percent of the job growth in the retail trade sector was in food and beverage stores. Ninety-one percent of the job growth in education was in colleges and universities, with the remainder in junior colleges (+547) and other schools and instruction (+384). Virtually all of the jobs created in the professional, scientific, and technical services sector were in computer systems design and related services, its share of jobs increasing from 13% in 1990 to nearly 24% in 2010.

Sectors That Continued to Shed Jobs

Ten major industry sectors continued to eliminate jobs between 2009Q4 and 2010Q4. Twenty-eight percent, or 2,247, of the jobs lost in Connecticut's economy were in the information sector. Further, this sector also had the steepest decline at 6.6%. Telecommunications accounted for 92% of all the job losses in the information sector. However, two industries in this sector added jobs: motion picture and sound recording industries

GRAPH 2: CT Job Growth and Forecast for Major Sectors



(+129) and broadcasting (except Internet) (+258).

Construction, hit hard by the housing bust, shed another 1,606 jobs between 2009Q4 and 2010Q4, which accounted for 20% of all jobs lost. Construction also had the second steepest decline in jobs (-4.7%). Two other sectors each accounted for more than 10% of job losses: finance and insurance shed 1,474 jobs, and accounted for 18.5% of job losses, and government lost 799 jobs, and accounted for 10% of job losses. Virtually all job losses in the finance and insurance sector were in insurance, offset partially by gains in securities, commodity contracts (+750) and funds and trusts (+555). Government job losses, reflecting the state and local fiscal crises, were all in state and local government (which includes the tribal casinos).

THE EMPLOYMENT OUTLOOK TO 2012

Graph 2 shows Connecticut's job growth by major sector for the base period, 2008Q4-2010Q4, and the forecast period, 2010Q4-2012Q4. As depicted in Graph 2, the impact of the recent crisis is

reflected in the job losses over the base period 2008Q4-2010Q4, when Connecticut employment declined by 67,118. The goods producing sector lost 29,323 jobs, and even the private service providing sector had a net loss of 36,332 jobs. The government sector lost 3,588 jobs.

The forecast is predicated on a slowing of the economic recovery's momentum, resulting from the winding down of federal fiscal stimulus. This includes the sun-setting of the temporary payroll tax reduction and UI benefits extension at the end of 2011, the state's fiscal crises, and continued stress in the housing market. It is projected that Connecticut's economy will add 15,170 jobs between 2010Q4 and 2012Q4 (see table). The forecast expects the growth in private service providing jobs over the 2009Q4-2010Q4 period to continue into the 2010Q4-2012Q4 forecast period, resulting in 15,900 new jobs. Though its losses should abate considerably, the goods producing sector is expected to shed another 4,000 jobs. Though the Governor and State's unions have an agreement, it still must be voted on by the membership. If approved, there will still be job

reductions through consolidations and attrition. If in fact Plan B has been avoided, it is expected that government will still eliminate another 2,000 jobs at the state and local levels over the forecast period.

Six industry sectors are expected to add 1,000 or more jobs over the forecast period. The health care and social assistance sector is expected to continue to dominate job creation in both the state and national economies. The health care services and facilities subsector is projected to add 5,000 jobs between 2010Q4 and 2012Q4, and the social assistance sub sector is expected to add 4,743 new jobs. Nearly 1,000 jobs were lost in elementary and secondary education between 2009Q4 and 2010Q4. Nevertheless, over the same period the education sector added 1,445 jobs, driven by growth in junior colleges, colleges and universities. Though tempered by the new budget realities, especially at public institutions, the trend is expected to continue, resulting in 4,459 new jobs created in education by 2012Q4.

Management of companies and enterprises is expected to resume growth and add 1,447 jobs. Admin-

--Continued on page 5--

Connecticut Nonfarm Employment: History and Forecast

| INDUSTRY | HISTORICAL | | | FORECAST | NUMERICAL CHANGES | | | PERCENT CHANGES | | |
|--|------------------|------------------|------------------|------------------|-------------------|----------------|---------------|-----------------|---------------|--------------|
| | 2006:Q4 | 2008:Q4 | 2010:Q4 | 2012:Q4 | CH06-08 | CH08-10 | CH10-12 | %CH06-08 | %CH08-10 | %CH10-12 |
| TOTAL | 1,717,038 | 1,701,407 | 1,634,289 | 1,649,459 | -15,631 | -67,118 | 15,170 | -0.91 | -3.94 | 0.93 |
| GOODS PRODUCING | 262,995 | 248,551 | 219,228 | 215,256 | -14,444 | -29,323 | -3,972 | -5.49 | -11.80 | -1.81 |
| Mining..... | 749 | 747 | 581 | 600 | -1 | -166 | 19 | -0.18 | -22.26 | 3.27 |
| Construction..... | 68,964 | 63,300 | 52,246 | 50,816 | -5,664 | -11,055 | -1,430 | -8.21 | -17.46 | -2.74 |
| Manufacturing..... | 193,282 | 184,503 | 166,401 | 163,840 | -8,779 | -18,102 | -2,561 | -4.54 | -9.81 | -1.54 |
| SERVICE PROVIDING | 1,429,575 | 1,437,437 | 1,401,105 | 1,417,008 | 7,862 | -36,332 | 15,903 | 0.55 | -2.53 | 1.13 |
| Wholesale Trade..... | 68,237 | 68,531 | 63,337 | 63,917 | 295 | -5,195 | 580 | 0.43 | -7.58 | 0.92 |
| Retail Trade..... | 196,985 | 190,245 | 184,656 | 185,721 | -6,741 | -5,589 | 1,065 | -3.42 | -2.94 | 0.58 |
| Transportation and Warehousing..... | 53,853 | 53,054 | 49,286 | 48,950 | -799 | -3,769 | -335 | -1.48 | -7.10 | -0.68 |
| Utilities..... | 6,616 | 6,875 | 6,341 | 5,934 | 260 | -535 | -407 | 3.93 | -7.78 | -6.41 |
| Information..... | 37,009 | 36,643 | 31,773 | 31,194 | -366 | -4,870 | -578 | -0.99 | -13.29 | -1.82 |
| Finance and Insurance..... | 124,191 | 121,969 | 115,244 | 113,300 | -2,222 | -6,724 | -1,944 | -1.79 | -5.51 | -1.69 |
| Real Estate and Rental and Leasing..... | 21,141 | 20,210 | 19,084 | 18,263 | -931 | -1,126 | -821 | -4.40 | -5.57 | -4.30 |
| Professional, Scientific, and Technical Services.... | 93,369 | 91,574 | 86,759 | 87,506 | -1,795 | -4,815 | 748 | -1.92 | -5.26 | 0.86 |
| Management of Companies and Enterprises..... | 26,129 | 28,455 | 27,690 | 29,137 | 2,327 | -766 | 1,447 | 8.90 | -2.69 | 5.23 |
| Admin and Support/Waste Manage/Remediation.. | 89,413 | 82,974 | 80,476 | 81,915 | -6,439 | -2,498 | 1,439 | -7.20 | -3.01 | 1.79 |
| Educational Services..... | 172,622 | 180,370 | 180,769 | 185,228 | 7,748 | 399 | 4,459 | 4.49 | 0.22 | 2.47 |
| Health Care and Social Assistance..... | 248,342 | 263,215 | 269,809 | 280,287 | 14,873 | 6,594 | 10,478 | 5.99 | 2.51 | 3.88 |
| Arts, Entertainment, and Recreation..... | 42,841 | 43,097 | 39,943 | 39,709 | 256 | -3,154 | -233 | 0.60 | -7.32 | -0.58 |
| Accommodation and Food Services..... | 112,241 | 112,158 | 112,074 | 113,579 | -84 | -84 | 1,506 | -0.07 | -0.07 | 1.34 |
| Other Services..... | 58,240 | 57,899 | 57,287 | 57,890 | -341 | -613 | 603 | -0.59 | -1.06 | 1.05 |
| Government..... | 78,346 | 80,169 | 76,581 | 74,477 | 1,823 | -3,588 | -2,104 | 2.33 | -4.48 | -2.75 |

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

NOTE: The sum of the major industry sectors will not add to the total because total employment (the top line) also includes jobs that are not covered by unemployment insurance laws, most of which are student workers at colleges and universities.

--Continued from page 3--

istrative and support, driven by employment services, is projected to add 1,439 jobs over the forecast horizon. Food and beverage stores will continue to drive growth in retail jobs, propelling that sector to tack on 1,065 new jobs.

Four industry sectors are expected to eliminate 1,000 or more jobs over the forecast horizon. As noted above, government is expected to lose more jobs than any other sector. Between 2010Q4 and 2012Q4, government at all levels will shed 2,100 jobs. Manufacturing will continue to shed jobs but at a much slower pace, declining by 2,561. Continued job losses in credit intermediation and the trends in the insurance industry will result in the elimination of 1,944 jobs in the finance and insurance sector by 2012Q4. With the continued depressed state of the housing market, construction will decline by another 1,430 jobs.

RISKS TO THE FORECAST

There are significant downside risks to the forecast. After the collapse of housing and the accumulation of unsustainable debt loads, households and non-incorpo-

rated businesses, in an effort to rebuild their net worth, have reduced their borrowing and increased their debt service. This raised the savings rate and reduced spending in the economy. Though consumers have been paying down debt to address the liabilities side of their balance sheets, with housing prices still declining nationally, the asset side is still down, especially for households at or below the median income. This has and will continue to inhibit spending, and act as a drag on the recovery. Withdrawing more spending from the economy through aggressive cuts in federal spending, in conjunction with the spending reductions by the states to balance their budgets, could short-circuit the recovery. Hopefully, the most remote downside risk would be playing political brinksmanship with the U.S. debt ceiling. A U.S. default, technical or otherwise, or even an 11th hour deal, would be nothing short of a disaster for the U.S. and world economies.

On the positive side, strong export growth could make the forecast overly pessimistic. Further, if the decline in the price of oil proves to be sustainable, it would

act like a progressive tax cut lifting that drag on the economy. Finally, if the union agreement is ratified, and if tax revenues continue to exceed projections, then the forecast's expected job losses in local government would be overly pessimistic, which, given multiplier effects, could raise the overall forecast upward toward 20,000 over the 2010Q4-12Q4 forecast horizon. ■

¹ U.S. BEA, GROSS DOMESTIC PRODUCT: FIRST QUARTER 2011 (ADVANCE ESTIMATE) (April 28, 2011) U.S. Department of Commerce: Washington

² U.S. BLS, THE EMPLOYMENT SITUATION – APRIL 2011 (May 6, 2011) U.S. Department of Labor: Washington

³ Bruner, ROBERT F. and Sean D. Carr, THE PANIC OF 1907: Lessons Learned from the Market's Perfect Storm (2007) John Wiley & Sons: New York

⁴ White, Eugene N., The Great American Real Estate Bubble of the 1920s: Causes and Consequences (October 2008) National Bureau of Economic Research: Cambridge, MA.

⁵ Koo, Richard C., THE HOLY GRAIL OF MACROECONOMICS: Lessons from Japan's Great Recession (2009) John Wiley & Sons: New York

GENERAL ECONOMIC INDICATORS

| | 1Q | 1Q | CHANGE | | 4Q |
|---|-------------|-------------|--------|-----|-------------|
| <i>(Seasonally adjusted)</i> | 2011 | 2010 | NO. | % | 2010 |
| Employment Indexes (1992=100)* | | | | | |
| Leading | 116.0 | 114.9 | 1.1 | 0.9 | 116.4 |
| Coincident | 102.6 | 101.1 | 1.4 | 1.4 | 102.4 |
| General Drift Indicator (1986=100)* | | | | | |
| Leading | NA | NA | NA | NA | NA |
| Coincident | NA | NA | NA | NA | NA |
| Farmington Bank Business Barometer (1992=100)** | 124.5 | 122.0 | 2.5 | 2.0 | 124.8 |
| Philadelphia Fed's Coincident Index (July 1992=100)*** | APR | APR | | | MAR |
| <i>(Not seasonally adjusted)</i> | 2011 | 2010 | | | 2011 |
| Connecticut | 156.3 | 150.8 | 5.5 | 3.6 | 155.9 |
| United States | 153.5 | 149.4 | 4.1 | 2.7 | 153.0 |

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).