JOINT ECONOMIC COMMITTEE

Senator Sam Brownback
Ranking Republican

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RECENT ECONOMIC DEVELOPMENTS

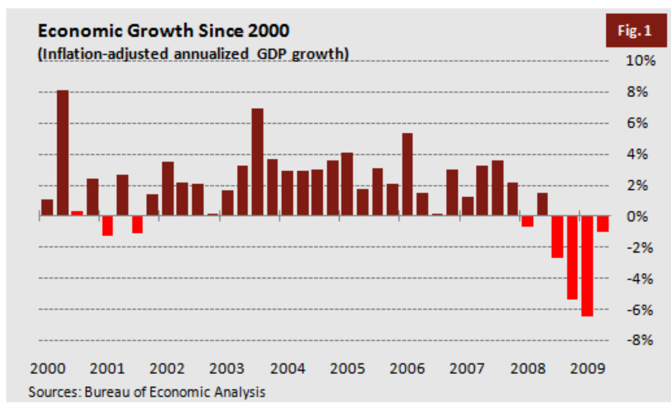
AUGUST 4, 2009

Freefall Ends, Significant Risks Remain

Output in the economy, measured by the inflation-adjusted (real) gross domestic product (GDP) fell at a 1.0% annualized rate in the 2nd quarter, an improvement from -6.4% in the 1st quarter, -5.4% in the 4th quarter of 2008, and -2.7% the 3rd quarter of 2008. The four consecutive quarterly declines in GDP is a post World War II record string of declines. The unemployment rate rose to 9.5% in June and is up by 4.6 percentage points since the start of the recession. Non-farm payroll employment fell by 467,000 jobs in June, above May's losses of 322,000 jobs but more moderate than the average decline of almost 700,000 in the first three months of this year. The economy remains sluggish, but incoming data show signs of repair; the paces of decline in output is diminishing; the housing market is showing signs of stabilization; and home price declines have subsided (by some measures, prices have shown some recent increases). Arresting the declines in home prices and resulting declines in household wealth is important for an economic recovery. However, with more and more households experiencing unemployment, home foreclosures continue to grow.

Highlights

- *GDP* fell at a 1.0% annualized rate in the 2nd quarter, the fourth consecutive quarterly decline (Fig. 1).
- The *unemployment rate* rose to 9.5% in June, the highest in over 26 years (Fig. 2, next page).
- *Payroll employment* fell by 467,000 in June and close to 6.5 million in the past 18 months (Fig. 3, next page).
- Declines in *home prices* are abating; some price measures show recent increases (Fig. 4 next page).
- *Mortgage delinquencies and foreclosures* continue to rise (Fig. 5, next page).



GDP Declined at a 1.0% Annualized Rate in the 1st Quarter

Real GDP fell at a 1.0% annualized rate in the 2nd quarter following a 6.4% decline in the 1st quarter, 5.4% decline in the 4th quarter of 2008, and 2.7% decline in the 3rd quarter of 2008 (Fig. 1). The drop in 2nd-quarter GDP reflected declines in business investment (-8.9% in the 2nd quarter vs. -39.2% in the 1st), consumer spending (-1.2% vs. +0.6%), residential investment (-29.3% vs. -38.2%), exports (-7% vs. -29.2%), and inventory investment (the change in inventories subtracted 0.83 percentage point from the 2nd quarter change in GDP vs. a subtraction of 2.36 percentage points in the 1st quarter). Those declines were partly offset by positive contributions from federal government spending (+10.9% vs. +4.3%) and state and local government spending (+2.4% vs. +1.5%). Federal government spending in the 2nd quarter was boosted by 10.9% annualized growth in national defense spending; non-defense spending grew 5.9% in the quarter.

Unemployment Rate Rises to 9.5%; Close to 6.5 Million Jobs Lost in Past 18 Months

The *unemployment rate* rose to 9.5% in June (Fig. 2, next page). *Payroll employment* fell by 467,000 jobs in June and by nearly 6.5 million jobs in the past 18 consecutive months with job losses (Fig. 3, next page). Expectations are for further job losses in this Friday's report on July's labor market conditions (many forecasts are for losses of around -350,000) and an increase in the unemployment rate (many forecasts are for the unemployment rate to increase to around 9.6%).

Household Wealth, Consumption, and Saving

Net worth of households and nonprofit organizations fell by $1.3 trillion in the 1st quarter, following a $4.9 trillion decline in the 4th quarter of 2008. Since its peak in the 2nd quarter of 2007, net worth has fallen by $13.9 trillion, a 21.6% decline. In the face of declining wealth, households have trimmed *consumption spending* and increased *savings* to shore up their balance sheets; personal saving as a percentage of disposable (after-tax) income has climbed from a near-term low of 0.8% in April 2008 to 6.2% in May and 4.6% in June 2009.

Home Price Declines Abating

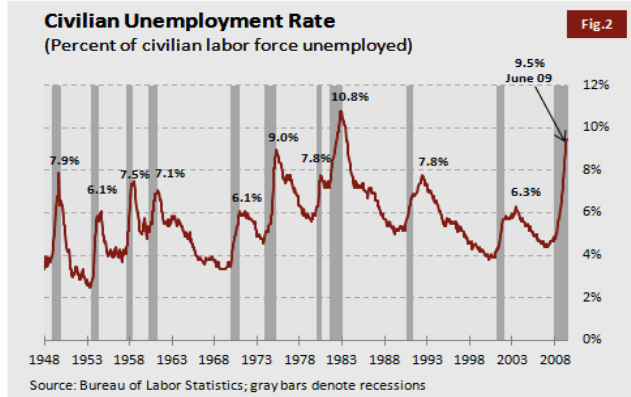
Home prices, which have been declining following the bursting of the housing bubble around the end of 2006, have shown signs of stabilization. By some measures there have even been price increases in recent periods (Fig. 4). Stabilization or increases in home prices would help prevent homeowners from falling underwater on mortgages, which has been contributing to home foreclosures.

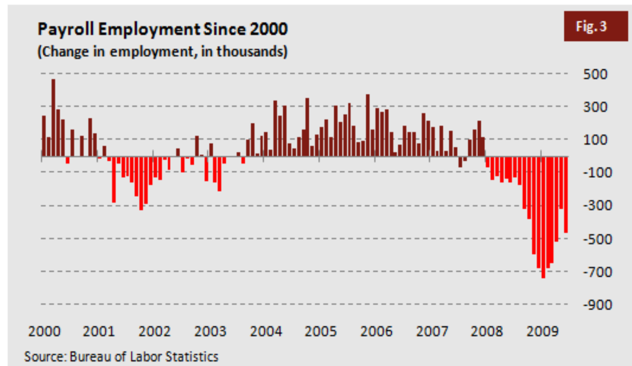
Delinquencies and Foreclosures Continue to Rise

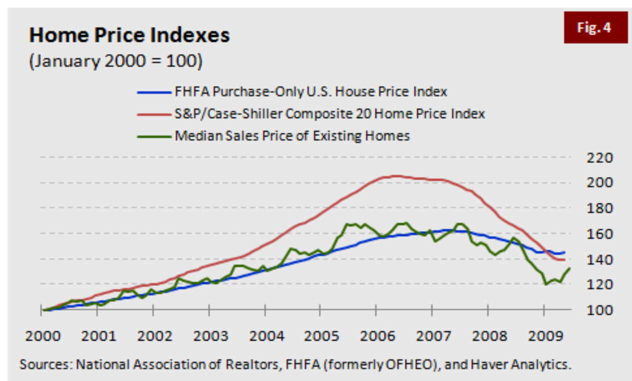
Despite abating home price declines, rising unemployment has likely been a growing contributor to recent increases in *mortgage delinquencies and foreclosure* (Fig. 5). Last year, most of the growth in foreclosures was in Arizona, California, Florida, and Nevada—states that saw precipitous run-ups in home prices during the housing bubble and subsequent large price declines. Foreclosures in those four states rose 16% in the 2nd half of 2008 relative to the 1st half of that year. For the remainder of the U.S., the number of foreclosures actually declined in the 2nd half of 2008 relative to the 1st by 5%. This year, while foreclosures in the four states listed above continue to climb, foreclosures in remaining states are climbing as well, as the ranks of unemployed workers grow.

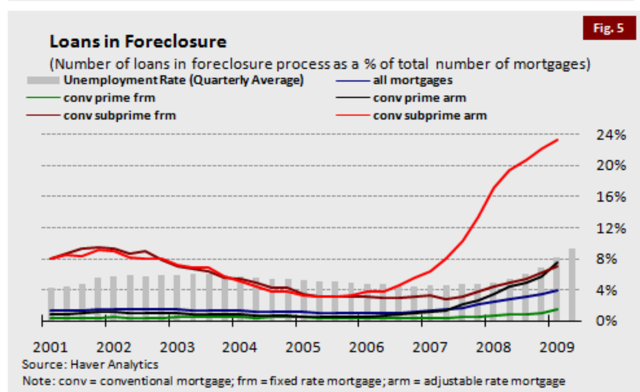
Suggestions of Future Growth in Manufacturing

The *Institute for Supply Management (ISM) manufacturing index* rose to 48.9 in July from 44.8 in June—a value below 50 indicates contraction in the manufacturing sector; above 50 signals expansion. The ISM manufacturing index has been below 50 since January 2008 and hit a low of 32.9 in December of that year. The ISM report for July indicated that "…the more leading components of the PMI—the New Orders and Production Indexes—rose significantly above 50 percent, thus setting an expectation for future growth in the sector." A separate ISM services-sector index has been below 50 since September 2008 but has risen from an all-time low (since the data began in 1997) of 37.4 in November 2008 to 47.0 in June of this year.









Upcoming Indicators

Employment – The Bureau of Labor Statistics reports on the July employment situation on *August 7.*

Federal Reserve – The Fed's next policy meeting is scheduled for *August 11 and 12.*

Inflation – The Consumer Price Index for July is scheduled for release on *August 14*.

GDP – The second estimate of the 2nd quarter GDP is scheduled for release on *August 27.*