Four Corners Economic Quarterly

2009 Q1

Office of Business and Economic Research, School of Business
Fort Lewis College, Durango Colorado

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A Comparison to the National Economy

By: Dr. Deborah Walker

A popular question for local economists these days is, "How will the economic situation now occurring on the national (and even international) level effect our local economy?" Of course, no one knows exactly how all of this will play out. Economists are in vast disagreement on why the economy has taken a turn for the worse and, therefore also do not agree on "the right solution." But one thing is clear; we have seen some significant changes in national labor markets over the last year.

So I thought it might be interesting to compare these changes to the changes in the Colorado labor market and in the local county labor markets. The data used here are the most recent available (and therefore are preliminary figures) from the Colorado Department of Labor and Employment and the Bureau of Economic Analysis.

> … it appears that the State of Colorado is not holding its own during this economic downturn when compared to the national labor market.

Probably the most well known economic indicator in labor markets is the unemployment rate. This rate is determined as a percent of the civilian adult (16 and over) population who wants to work (known as the labor force) but can't find a job. The national unemployment rate in October 2007 was 4.8%, and in October 2008 it was 6.5% – an increase of 1.7 percentage points. In October of 2003 the unemployment rate was 6.0% and steadily declined each year until 2007. Colorado's unemployment rate in October 2007 was 3.6%, and in October 2008 it was 5.3% – an increase of 1.7 percentage points. So the state seems to be mirroring the nation in terms of the unemployment rate (at least over the last year).

So what is happening locally? Let's look at what is happening in the labor markets of five neighboring counties: Archuleta, Dolores, La Plata, Montezuma and San Juan.

Starting with Archuleta County, its unemployment rate was 5.0% in the month of October 2008. One year ago during the same month, the rate was 3.5% - an increase of 1.5 percentage points. Dolores County has seen the largest increase (with respect to the five local counties compared) in the unemployment rate over the last year (absolutely and relative to the nation). Its unemployment rate went from 4.4% in October 2007 to 6.7% in October 2008 – an increase of 2.3 percentage points.

La Plata County's unemployment rate increased by 0.9 of a percentage point during the same time frame (from 2.6% to 3.5%). Montezuma County saw an increase from 3.6% to 5.3% (1.7 percentage points). San Juan County seems to be weathering the economic storm pretty well. It saw a *decrease* in unemployment from October 2007 to October 2008 of 0.8 of a percentage point (from 3.8% to 3.0%).

A second labor market statistic that economists like to keep track of is the number of employed people in an economy. This gives us an indication of job growth even with a changing unemployment rate. If the labor force stays the same and employment increases, unemployment will decrease. But if the labor force is increasing, both the number of people employed and the unemployment rate could increase at the same time. The worse-case scenario would happen if the labor force and the unemployment rate increase, but employment did not. That would mean that all of the people entering the labor force looking for a job can't find one.

Again, looking at the time from between October 2007 and October 2008, the national labor force increased by about 1.1%. At the same time, the number of employed decreased by 0.7% and the number of unemployed increased by 38.6%. So not only did those who entered the labor force not find jobs (at least that number of people), but people already working lost their jobs.

The State of Colorado increased their labor force by 0.9% from October 2007 to October 2008. At the same time employment decreased by 0.8% and unemployment increased by 47.7% (by 47,620 people). Colorado seems to be fairing slightly worse than the nation as a whole.

Archuleta County saw a drop in the number of people who want a job (the labor force) by 3.5%. At the same time employment dropped by 5.2% and unemployment increased by 39.9% (by 97 people). Dolores County increased their labor force by 1.7%, decreased the number employed by 0.8% and increased the number unemployed by 54.2% (by 26 people).

La Plata County's labor force increased by 2.8% (by 915 people), the number of employed *increased* 1.9% (by 595 people), and the number of unemployed increased by 37.6% (by 320 people). Similar to Archuleta County, Montezuma County's labor force decreased 380 people (by 2.8%), while the number of employed decreased by 590 people (by 4.5%) and the number of unemployed increased by 210 people (by 42.7%). San Juan County stands alone compared to the other four counties. It is the only county that saw an increase in the labor force (by 103 people or 17.6%), an *increase* in employment of 104 people (or by 18.4%) *and a drop in the number of unemployed* by 1 person (by 4.6%).

In conclusion, it appears that the State of Colorado is not holding its own during this economic downturn when compared to the national labor market. However, San Juan County seems to be keeping its head above water with increasing employment and decreasing unemployment (even if by only one person). La Plata County also seems to be doing pretty well (at least when compared to the nation). Although it saw an increase in the number unemployed, it managed to employ a majority of its labor force increase from October 2007 to October 2008.

Inaugural Economics

By: Dr. Robert Sonora

Given yesterday's inauguration of a new president I am going to summarize current hurdles to economic well-being.

Current Situation

The challenges in the near term are quite transparent. As many have already discussed, we are possibly on the verge of what could be the worst economic downturn in over 75 years. So let's dive right in.

Currently, the unemployment rate is about 7.2% or approximately 2 percentage points above its long run "natural rate". Cyclical unemployment is rising sharply as is the natural rate. Most economists believe unemployment will reach somewhere between 9-10% before the economy begins to recover.

Closely associated with the natural rate of unemployment is potential real gross domestic product (GDP). This what the economy produces in when working at "full capacity" without over- or under-utilizing resources. When actual real GDP deviates from this level of output the economy goes through expansionary or recessionary "output gaps".

> Most economists believe unemployment will reach somewhere between 9-10% before the economy begins to recover … temporary tax cuts are useless.

In July 2008, the most recent data available, the output gap hit –2%, and is heading the wrong direction. The size of the gap is getting close to the size of the ".com" recession – though still quite a distance from the Reagan-Volcker recession of the early 1980s. However, a quick "back of the envelope" calculation reveals the December gap has fallen to about minus 5%.

If you had asked me a year ago about the other worry, inflation, I was concerned about a spiraling supply side inflationary spiral – stagflation. If, on the other hand, you had asked me about inflation four months ago, I wouldn't have worried about it all. Now I am worried about the possibility of deflation, "negative" inflation. Annualized inflation rates are falling dangerously close to zero, about 0.1% in December. In the last quarter of 2008 monthly inflation rates were *negative*.

Deflation is associated with declines in aggregate demand for goods and services, and while falling prices are good for purchasing power, they are bad for firm costs-revenue calculations. As output prices fall firms pull back on their payroll to trim costs which raises unemployment, further dampening demand, and the economy enters into a vicious downward spiral.

Fixes?

Economic policy makers have two tools they can use to combat: monetary and fiscal policy. To date, monetary policy has failed despite the Fed's new zero policy interest rate target. This should encourage lending, but uncertainty and lack of confidence have gummed up credit markets. Despite the Fed's best intentions the money supply is *shrinking* – theory suggests that with zero interest rates money should become infinite.

With monetary policy effectively sidelined we must rely on fiscal policy to pull out of the hole. The current price tag of the Obama fiscal stimulus is $825 billion over two years. And while that may seem to be a lot of money, well it is, it is a lot less than the Federal government would have to spend if nothing was done. Without it we could look forward to potentially a decade of economic doldrums.

Support for this fiscal stimulus has almost universal support from both sides of the congressional aisle with the debate over the money will be spent. Tax cuts? Road construction? Education? Energy?

My two cents are the following: temporary tax cuts are useless. On aggregate, US households have amassed $13.9 trillions of debt while after tax income is $10.7 trillion; the percentage of disposable income-to-debt ratio in percentage terms is currently about –20%. Thus, temporary tax breaks will be used to pay down debt and/or increase savings – which is also close to zero. Any tax relief should be of the permanent variety not like the Bush "permanent" tax cuts which are set to expire in 2011.

Nor should the fiscal stimulus package be used for long term investments in human capital, new energy technologies, or other long term programs. These are ideal long term investments for the future of the US economy, but will have relatively little impact over the next 6 – 18 months when we need it.

Rather, we should concentrate on projects which pump cash into the economy yesterday not five years from now. Infrastructure repairs is a sensible start, with a couple of caveats. First, it is no substitute for investment in new infrastructure investment along the lines of the telecommunications or interstate highway system. And second, it remains to be seen how far reaching road and bridge repairs will be.

Another interesting idea is mortgage rate "reform". Now that the Federal Government owns Fannie Mae and Freddie Mac, they should allow nationwide refinancing of mortgages. This will allow household considering foreclosure to get in at a safer low interest rate mortgages. And current home owners can free up income for expenditures, or pay down existing debt.

Also, congress must decide to take a "pork" vacation. Well, perhaps, pork should be retired permanently, or limited to projects which require less than, say, $1 million.

We are in for a long haul. 2008 Nobel winning economist Paul Krugman is quoted as being “frightened” about the near future, and economists are accustomed to pessimism. I believe that whoever was elected last November would arrive at the same conclusion − the economy needs a kick start – And a substantial one at that.

Last Quarter Comparisons for La Plata County

By: Dr. Deborah Walker

Although there are signs that La Plata County’s economy is feeling some of the negative effects of the national downturn; when compared to the nation, we aren’t faring too bad. When looking at the local data available for the last quarter of 2007 in comparison to the last quarter of 2008, the local economy is holding its own in many areas.

The unemployment rates for October, November and December 2007 were 2.6, 2.9 and 3.1 percent respectively. That’s an average of 2.86. The unemployment rates for October, November and December 2008 were 3.5, 4.0, and 3.8 respectively. That’s an average of 3.76 (a quarterly increase of almost one percent point). During the same time frame (the fourth quarter of 2007 as compared to the fourth quarter of 2008), the average unemployment rate for the United States went from 4.8% to 6.8% (a quarterly increase of two percentage points).

Interestingly, employment numbers for La Plata County show job growth for the fourth quarter of 2008 (compared to the same quarter in 2007). The average number employed in the fourth quarter of 2007 was 30, 841. The same average in 2008 was 31,429 (an increase of 1.9%). This means more people are entering the labor force and at least some are finding jobs. Comparing the same time frame, employment numbers for the United States declined by about 1.6% from quarter to quarter.

Major employers in La Plata County include firms in the service, retail, government and construction industries. These industries, which include tourist activity, continue to drive the local economy (along with oil and gas extraction). Passengers using the Durango–La Plata County Airport increased in the fourth quarter by around 18%, while people riding the Durango-Silverton Railroad decreased by about 14% (this is an estimate). Visitors to Mesa Verde declined by about 3.7%. According to the National Park Service, recreation visits to all national parks during the fourth quarter increased by about 0.87% from 2007 to 2008.

Agriculture still remains an important contributor to the local economy. Unadjusted average alfalfa hay prices increased from the fourth quarter of 2007 to the fourth quarter of 2008 by 20%. Adjusted prices increased around 17.8%. Calf prices, on the other hand, fell by 12.8% (unadjusted) or by 14.4% when adjusted for inflation. Industrial kilowatt hours used in the County during the fourth quarter increased by 9.2% (estimate). This is an indicator of industrial activity, including compression of natural gas through pipelines. Natural gas extraction remains an important part of the local economy.

Whither the Euro?

By Dr. Robert Sonora

With all the brouhaha surrounding the billions of dollars being used to “rescue” American financial institutions and business – The projected Federal Government budget deficit set to reach $1.9 trillion this year – It’s hard to remember there is an global economy that lies beyond our borders.

The International Monetary Fund (IMF) predicts the global economy will shrink between minus one percent and –0.5% this year, the first global contraction in over sixty years. The largest economies of the US, the Euro area, and Japan are forecast to shrink by about −2.6%, −3.2%, and −5.8% respectively.

Though the US may fare less poorly then the rest of the world, this is hardly good news.

Now, we should shift our attention to the European Union, our single largest trading partner. It could be said that while the seeds of the financial crisis were sown in the US, they first sprouted in Europe.

It began in Iceland. To attract foreign currencies Icelandic banks began offering high interest rates. People in the UK were particularly happy with this arrangement. Unfortunately, the Icelanders weren’t as adept at finance as many thought. The bubble popped and the UK was forced to rescue its citizens who sent their savings abroad. The British bank Northern Rock was nationalized.

In France BNP Paribas admitted it didn’t know the true value of its (US) mortgage backed asset holdings. And the flood gates opened into what is now the subprime mess.

But there’s another potential European bank crisis around the corner: Eastern Europe. And like all financial crises we don’t have to look back too far to find an antecedent − the 1980s Latin American debt crisis.

A similar situation exists in Eastern Europe. Market liberalization has led to an explosion of foreign investment in these countries, which could now default on foreign loans.

In the seventies and early eighties many Latin American countries relaxed trade restrictions and liberalized capital markets. At the same time there was a euphoric attitude about these countries in the US and large banks leant billions of dollars to these countries.

A similar situation exists in Eastern Europe. Market liberalization has led to an explosion of foreign investment in these countries, which could now default on foreign loans.

These countries borrowed primarily in euro and these debts must be paid. Currently, the foreign debt to GDP ratio is about 40%. While the absolute numbers are that large (trillion is the new billion), the threat of loan default may destructive to larger European commercial banks in Austria, Sweden and Italy.

Austrian banks have 80% of their assets in Eastern Europe and if these collapse it could bring the Austrian banking system with it. Austria, however, is a small country with little means to rescue a bank system. Maybe the IMF will have to ride to the rescue, again, as there are few alternatives.

There are cries from several corners that the current crisis may lead to the dismantling of the European economic experiment (including World Bank president Robert Zoellick) and, worse, maybe civil war in the Balkans.

I, for one, would not be surprised if the euro ceases to exist when all is said and done.

The *Four Corners Economic Quarterly* is a newsletter on economic indicators of Southwest Colorado published by the Office of Economic Analysis and Business Research in the Fort Lewis College School of Business Administration and Region 9 Development District of Southwest Colorado, Inc.

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