

National and District Overview

It's a Wait and See Economy Out There

by Adam M. Zaretsky

Oh, what a difference a year makes! Nine months ago, this column asked if the economy had really achieved a soft landing or if, perhaps, it had not even touched down yet. The question was posed on the heels of six hikes in the federal funds target rate from mid-1999. The answer was mixed: Although real GDP data indicated that the economy was still strong, the employment picture was weakening and inflation appeared to be creeping up. "Time will tell," the article concluded, "if the ... corrections already put in place will work to keep the economy on course and inflation at bay."

Three months ago, this column asked if the economy would gain a second wind. By then, GDP growth in the latter half of 2000 had slowed to less than a third of what it had been in the prior six months. However, employment numbers were coming in stronger than expected, sales of homes and vehicles were rebounding, and inflation appeared tamer.

Output's Ups and Downs

Today, the picture is still confusing, as surprises have occurred on both the upside and downside. As stated three months ago, output grew in the second half of 2000 at a 1.6 percent annual rate, and expectations were that growth would slow further in the first quarter of 2001. Then, the advance data caught the market by surprise. In April, the Bureau of Economic Analysis (BEA) announced that GDP had grown at a 2 percent annual rate in the first quarter—about double what most analysts had expected. Perhaps the economy hadn't slowed as much as was believed. Perhaps the bottom had already been hit in late 2000,

and the economy was starting a slow rebound. Perhaps more data were needed.

In May, the BEA released a revised figure for first-quarter GDP growth: 1.3 percent at an annual rate. What happened? The later, more-comprehensive data revealed that decreases in inventories were much greater than had been originally reported—almost three times April's initial data. This change alone knocked about one-half of a percentage point off April's advance growth rate. Revisions to other categories were minor in comparison.

Jobs' Downs

At the same time that GDP numbers were coming in first high and then low, job growth actually turned negative—that is, the number of workers on payrolls was *declining*—and the unemployment rate was rising. By April 2001, the unemployment rate had inched up to 4.5 percent after spending more than a year at or below 4.3 percent, although the rate fell to 4.4 percent in May. Keep in mind, though, that by historical standards, this rate is still low: Unemployment did not fall below this even once between early 1970 and 1998.

The striking slowdown in payroll employment is more worrisome than the small rise in the unemployment rate. In May, payroll employment was down by about 19,000 jobs from April, a month that had itself seen a decline of about 182,000 jobs. In the first half of 2001, payroll employment grew by about 17,200 jobs per month. By comparison, it grew by about 66,000 jobs per month in the second

half of 2000, after increasing by about 267,000 jobs a month in the first half of the year.

The bulk of the employment slowdown has occurred in the manufacturing sector. In fact, this sector has not seen its total payrolls increase since July 2000. Since then, the sector has lost approximately 675,000 jobs. The service-producing sector, on the other hand, has fared better. Between September 2000 and May 2001, it gained employment every month, adding somewhat more than 1 million jobs.

Time Will Tell

All told, in the first half of this year, the economy continued to slow, with the bulk of the job losses occurring in the manufacturing sector. During the same period, the Federal Open Market Committee cut the federal funds target, not once, not twice, but six times—for a total of 2.75 percentage points—in an attempt to stimulate the economy. Because the effects of these rate cuts have yet to be fully felt, once again, time will tell if the policy changes in place will work to keep the U.S. economy on course.

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