Montana Outlook
The Transition to Growth

by Patrick M. Barkey

It certainly has been a trying time for the Montana economy. The state remains in the grip of its worst recession since the 1980s, and news of closures and layoffs is depressingly easy to find. Yet it is also apparent that a long-awaited recovery in the economy has begun to take hold. We know that the U.S. economy has already swung to growth, beginning as early as late last summer. We believe that the Montana economy has also swung to growth as well – although the data to prove it won't be available for several months.

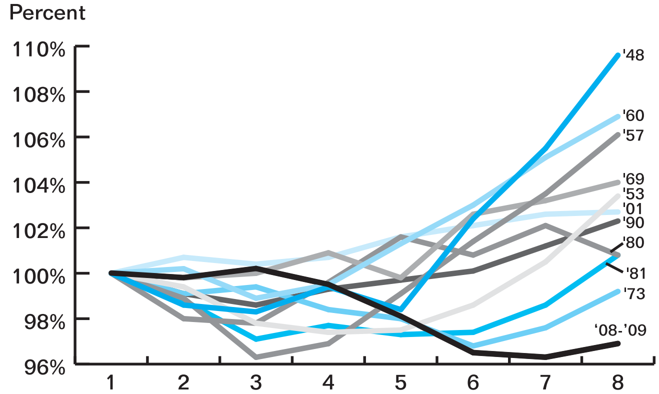
But it will not be a robust recovery, either for Montana or for the U.S. economy. To understand why that is so, we need to first understand why this recession – dubbed the Great Recession by some – has been so different from other downturns in recent experience.

The Recession of 2008-2009

The 2008-2009 recession has been the longest and deepest contraction in the U.S. economy since World War II. In the eight quarters since the recession was declared, total economic output fell by almost 4 percent. As shown in Figure 1, the depth and the duration of this recession exceed any of the 10 officially declared national recessions that preceded it. But this most recent recession experience is still on the same page as others the economy has suffered and not the full-scale panic and depression that many had feared.

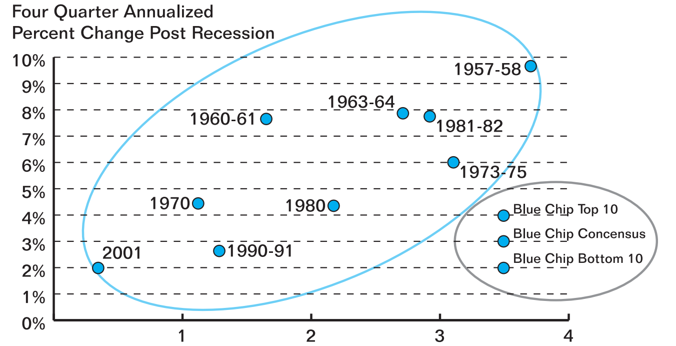
But beneath this superficial similarity, there are important differences between the recent recession and those of the past. This is evident from the kind of recovery that most economists are projecting. If you were to plot out all of the post-World War II recessions according to the depth of the downturn (measured in percentage change in Gross Domestic Product (GDP) from pre-recession peak to recession trough on the horizontal axis) and growth in the recovery (as measured by the four-quarter average of the percent change in GDP immediately following), a clear relationship can be seen, as depicted in Figure 2. Broadly stated, deep recessions are usually followed by robust recoveries, and vice versa, at least in the immediate wake of the downturn.

Figure 1
Real GDP as a Percent of Pre-Recession Peak
Post-World War II Recessions



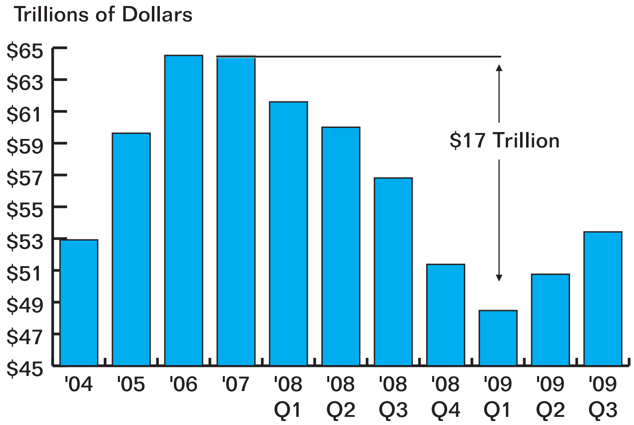
Source: U.S. Bureau of Economic Analysis.

Figure 2
Peak to Trough Decline in GDP vs. Post-Recession Growth
Post-World War II Recessions



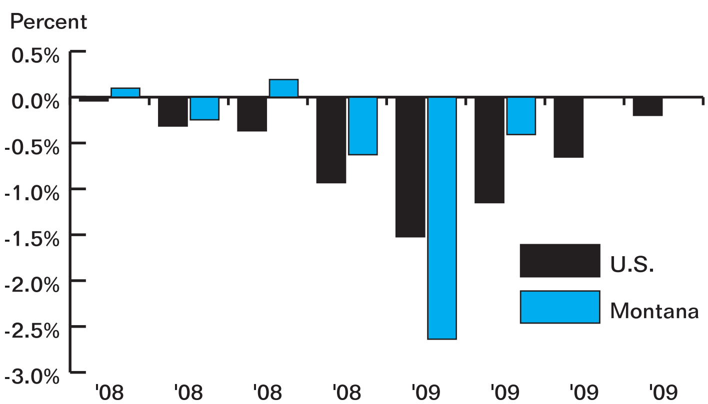
Source: U.S. Bureau of Economic Analysis, Blue Chip.

Figure 3
U.S. Household Net Worth
Trillions of Dollars



Source: Federal Reserve.

Figure 4
Payroll Employment, Percent Change
U.S. and Montana, 2008 Q1 - 2009 Q4



Source: U.S. Bureau of Labor Statistics.

The difference emerges when you plot the recent recession. We obviously don't have data yet for the post-recession recovery, but if we were to use instead the growth forecast by a survey of economic forecasters – the Blue Chip Consensus forecast – a striking contrast can be noted. Despite the fact that this recession has been the most severe, all three of the forecasts – the most optimistic, the consensus, and the most pessimistic from the Blue Chip survey – are quite pessimistic. No burst of "make-up" growth is anticipated by forecasters in the wake of this recession.

The reasons for this pessimism have to do with the nature of this recession. Whereas previous recessions have disrupted income flows in different pieces of the economy – energy, high tech, defense, or real estate – this has clearly been what might be called a "net worth" recession. It has produced an enormous decline in asset values, effectively wiping out $17 trillion of U.S. household net worth in the span of eighteen months. Those declines occurred as home prices, equity prices, and commodity prices all fell significantly.

As shown in Figure 3, there has been some recovery in net worth since the trough reached in the first quarter of last year, thanks to a rebound in stock markets and progress toward stability in home prices. Yet consumers still find themselves in a significantly worse position than before the recession, which why they have been saving more and spending less. Every economic recovery has been characterized by an increase in credit that fuels fast growth in consumer spending. But in the wake of the crash in asset prices, this spending surge is going to take much longer to arrive.

Recession in Montana

The most recent data on the 2008-2009 recession in Montana make it clear that:

- the recession has impacted every part of the state, with once faster-growing western counties most severely affected;
- downturns in private sector employment have occurred in every industry except health care;
- the Montana economy has been much more in sync with the U.S. economic downturn than has occurred in previous recessions.

The recession has produced declines in inflation-adjusted nonfarm income in the state economy in two consecutive years, 2008-2009, for the first time since 1986. What began as a contraction in construction and wood products industries in 2008 spread out into almost every other sector of the state economy as the recession worsened, with retail trade, trucking, and warehousing industries especially affected. Job declines across Montana peaked in the first quarter of 2009.

The pattern of job declines in Montana over time closely resembles what has occurred in the national economy, as shown in Figure 4. For both Montana and the United States., job declines were most severe in the first three months of 2009, with declines tapering off significantly since that point. Almost all sectors of the Montana economy experienced job losses, as shown in Figure 5.

The data make it clear that wealth-destroying declines in asset prices affected Montana consumers and businesses in much the same way as those across the country, producing weakness in both business and consumer spending that was felt in all segments of the economy. In the national economy, recovery in consumer spending is expected to be slow, as households increase savings and shed debt. Will the recovery in Montana over- or undershoot that performance?

The Montana Outlook

Only modest growth is projected for the national economy in 2010, with tepid new hiring expected to produce little change in uncomfortably high national unemployment rates. There are several reasons why Montana's economic performance in the coming year can be expected to exceed these modest expectations:

- the significant recovery in prices of important commodities, including copper, zinc, lead, and oil improves the prospects for Montana's natural resource industries;
- Montana's exposure to the housing market adjustments that have produced high rates of foreclosures and large numbers of unsold homes elsewhere is limited, so the negative impacts of the housing bust will be less severe;
- the state economy has a stronger reliance on industries like agriculture and activities of the federal government which have fared relatively better during the downturn.

On the other side of the equation, there are some special challenges to growth in the state economy in 2010 that the national economy does not face. Perhaps the most significant obstacle to growth in Montana is the decline in the state's forest products industry. The permanent closures of facilities in western Montana are still reverberating through the rest of the economy, and can be expected to act as a drag on growth in the coming years. There is also no prospect of a quick return to fast growth for residential construction. We project that housing construction, as measured by residential housing starts, will only reach 65 percent of its pre-recession peak levels by the end of year 2013.

We expect to see some recovery overall in the state economy in 2010, as consumer spending in the national economy stabilizes and markets for Montana's products begin to improve. Modest improvement in residential construction and natural resources industries will combine with increases in health care and government spending to produce slow growth in the state economy. Job growth will be slow, and the unemployment rate is expected to remain high through the end of the year. The recovery will be slow, and rapid growth is not foreseen until 2011.

The BBER forecast for the state economy calls for significantly slower growth than prevailed prior to the recession, as shown in Figure 6. In the period since the end of the 2001 recession and the beginning of the current recession, Montana enjoyed an average rate of growth in nonfarm labor income of 3.3 percent. Over this time period the state experienced an energy boom, a significant increase in construction activity, and a steady rise in spending by nonresident visitors.

During the eight quarters of recession beginning in 2008, growth turned negative, hitting an average decline of 1.2 percent. Beginning in 2010, the BBER forecast calls for average growth of only 2.4 percent, with growth not even hitting that mark for most of 2010. We are more optimistic that the recovery will show more strength beginning in 2011, as the imbalances in the economy work themselves out and consumer spending resumes faster growth.❑

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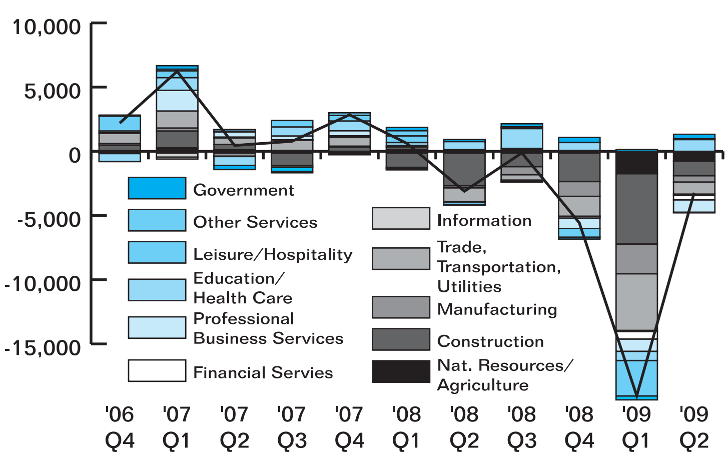
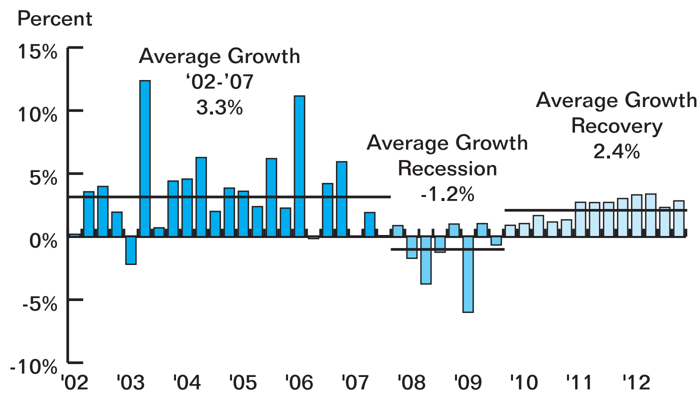
Figure 5
Montana Payroll Employment Growth by Sector



Source: U.S. Bureau of Labor Statistics.

Figure 6
Montana Nonfarm Labor Income, Percent Growth, Actual and Predicted, 2002Q1 - 2013 Q4



Source: Bureau of Economic Analysis and BBER forecast.