North Carolina
Cooperative Extension Service
NORTH CAROLINA STATE UNIVERSITY
COLLEGE OF AGRICULTURE & LIFE SCIENCES

NC STATE
ECONOMIST

Agricultural and Resource Economics January/February 1999

1999 ECONOMIC OUTLOOK

General Trends - National and North Carolina

National Economy

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Economic Fundamentals

The "economic good times" rolled on in 1998. Growth, little inflation, and rising wages and incomes mark the "good times." It doesn't get much better than this!

Specifically, the data show the national economy as measured by real (inflation-adjusted) Gross Domestic Product (GDP) grew 3.8% in 1998, almost as strong as in 1997 (Table 1). There was a 2.6% increase in jobs, and the national unemployment rate fell to an exceptionally low 4.5%.

Perhaps the biggest surprise in the economy was the continuing low inflation rate. Retail level inflation (the Consumer Price Index) rose only 1.5% in 1998, significantly lower than the 2.3% rise in 1997.

Partially responsible for the slower increase in average prices was the fall in the prices of imports, especially imported oil.

Lower interest rates also contributed to the good economy of 1998. Both short- and long-term interest rates fell during the year. Lower interest rates lowered the cost of borrowing and created more spending and economic activity.

Several measures of worker production and compensation showed that workers benefited from the good economy in 1998. Labor productivity (output-per-hour) increased a strong 2.3% in 1998, faster than the 1.4% improvement in 1997. Real (inflation-adjusted) compensation-per-hour jumped 2.7% in 1998, almost twice 1997's rate. Last, and probably the best measure of income change, real disposable personal income-per-capita, which looks at income change after subtracting taxes and the effect of inflation, increased a strong 2.5% in 1998, much better than 1997's increase.

Business inventories show no indication of being out of line with sales, with the business inventory/sales ratio holding steady at 1.4. The consumer debt situation actually improved in 1998, as the ratio of consumer installment debt to consumer income fell slightly from 1997 to 1998.

Much news has been made about the improved federal fiscal situation; indeed, the numbers reflect this. Federal tax revenues increased more than twice as fast as federal spending in 1998, and the federal budget, including the balance on the Social Security Trust Fund, recorded a surplus of $63 billion in the year.

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Table 1. Key U.S. Economic Statistics

	1997	1998	1999 Forecasts
Real U.S. GDP, % Chg.	3.9%	3.8%[a]	3.0%
Unemployment Rate	5.0%	4.5%[b]	4.9%
Labor Force, % Chg.	2.6%	2.6%[b]	1.8%
Inflation, Rate, CPI	2.3%	1.5%[b]	2.0%
90-day T-bill Rate	5.2%	4.8%[b]	4.9%
30-year T-bond Rate	6.6%	5.6%[b]	5.7%
Real Compensation Per Hour, % Chg.	1.4%	2.7%[a]	2.4%
Output Per Hour, % Chg.	1.4%	2.3%[a]	2.0%
Real Disposable Personal Income Per Capita	1.9%	2.5%[a]	2.0%
Business Inventory/Sales Ratio	1.4	1.4[b]	1.4
Consumer Installment Debt/Income	17.9%	17.7%[b]	17.8%
% Change in Fed. Tax Revenues	8.5%	8.7%[a]	4.9%
% Change in Fed. Spending	2.7%	3.3%[a]	4.0%
Federal Budget Balance	-$21 billion	+$63 billion[a]	+$80 billion
M2 Growth Rate	5.0%	2.0%[a]	3.5%
Net Exports/GDP	-1.7%	-2.6%[a]	-2.3%

a Annualized rate based on January - July.
b.Annualized rate based on January - September.
Sources: U.S. Dept. of Commerce, Federal Reserve Bank, Congressional Budget Office, forecasts by Mike Walden

The Federal Reserve reduced some key interest rates in 1998. However, the Fed maintained its tight reins on the money supply during the year, with the “M2” measure of the money supply rising only 2% in 1998.

On a negative note, the country's trade balance fell further into negative territory in 1998. Net exports, as a percentage of Gross Domestic Product was -2.6% in 1998, compared to -1.7% in 1997. This means the trade deficit grew relative to the economy in 1998. A probable reason is a reduction in exports to financially troubled East Asian countries.

Outlook

The “economic good times” should continue in 1999, although at a slightly slower pace. Table 1 gives the 1999 forecasts. Real Gross Domestic Product (GDP) is expected to increase 3%, down from 1998’s rate of 3.8%. Slower economic growth will cause job growth to slow and the unemployment rate to move slightly higher. Without big drops in import prices, the inflation rate will edge up to 2%, but interest rates will only be marginally higher.

There are two reasons behind this forecasted economic slowdown. One is the current problem in several East Asian economies. These countries, including Japan, will purchase fewer products from American companies, which, in turn, will cause these companies to slow their operations. The second reason is the tight labor market, which will inhibit the ability of firms to expand and increase their output.

The measures of worker production and compensation will also improve more slowly in 1999. Real compensation-per-hour, output-per-hour, and real disposable income-per-capita are all projected to improve at healthy rates in 1999, yet the rates will not be as high as in 1998.

The business inventory and consumer debt measures will change little in 1999, and the federal fiscal position will continue to improve. In response to the slow economy, the Federal Reserve will boost money growth.

What are the biggest threats to continued economic growth? There are two. One is the ever-present threat from the unknown. A foreign financial collapse, the outbreak of armed conflict in the Middle East, or political instability in a major country could cause a major drop in the stock market and spending curtailment by consumers. These threats are virtually impossible to predict, and there is no reason to expect their probability to be greater in 1999 than in previous years. Yet, they cannot be dismissed.

The second threat comes from the major private sector contribution to the economic expansion, the significant improvement in labor productivity. The threat is the negative impact on the economy if the productivity improvements stop or slow considerably. In this event, business costs and general inflation would rise and economic performance would deteriorate.

Altogether, the economic outlook is bright for 1999. Although economic growth will slow, no recession, which means shrinkage in the economy, is on the horizon. Most people and businesses should continue to see their economic situation improve in the new year.

North Carolina Economy

Table 2 summarizes the performance and forecasts for the North Carolina economy. Overall, in 1998, the North Carolina economy grew faster and the unemployment rate fell to a lower rate than for the nation. Real Gross State Product increased a very robust 4.5%, and the unemployment rate fell to 3.3%, more than a full percentage point lower than the national jobless rate.

Table 2. Key North Carolina Economic Statistics

	1997	1998[a]	1999 Forecasts
Real N.C. GSP, % Chg.	**5.3%**	**4.5%**	**4.0%**
Unemployment Rate	**3.6%**	**3.3%**	**3.3%**
Total Employment, % Chg.	**3.4%**	**2.3%**	**1.5%**
% Chg., Employment, by Sector:			
Durable Goods Manuf.	**3.1%**	**-2.0%**	**-2.0%**
Nondurable Goods Manuf.	**-1.8%**	**-4.0%**	**-3.0%**
Transportation and Utilities	**7.5%**	**-3.3%**	**4.0%**
Wholesale Trade	**-1.0%**	**8.0%**	**4.0%**
Retail Trade	**2.0%**	**4.0%**	**2.0%**
Financial Services	**6.3%**	**11.1%**	**5.0%**
Services	**13.2%**	**3.0%**	**3.0%**
Government	**1.0%**	**3.2%**	**2.0%**

[a] Analyzed rate based on January-September.
Sources: Employment Security Commission of North Carolina, North Carolina Economic Forecast, forecasts by Mike Walden

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Looking at sectoral employment performance in the state in 1998, there are some noticeable differences. Employment increased in the trade, services, and government sectors, but jobs fell in both durable and non-durable manufacturing and in transportation and utilities.

The fall in non-durable manufacturing jobs resulted from the downsizing in the textile, apparel, and tobacco industries. Losses in durable manufacturing jobs likely occurred from the loss in exports to East Asian countries and strong productivity improvements in this sector. The drop in jobs in transportation and utilities was surprising, but probably occurred from restructuring in these firms.

In 1999, the North Carolina economy, like the national economy, will again grow, but at a slower pace (see Table 2). Both overall growth and employment growth will be slower. Most regions of the state, including the metropolitan counties, will experience the slowdown. Within sectors, manufacturing will again lose jobs but other sectors will add jobs.

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N.C. State Economist
Published bi-monthly by the Dept. of Ag. and Resource Economics and the Coop. Ext. Serv. Address correspondence to:
The Editor, N.C. State Economist
Box 8109, N.C .State University
Raleigh, NC 27695-8109

Published by
North Carolina Cooperative Extension Service

NORTH CAROLINA
COOPERATIVE EXTENSION SERVICE
NORTH CAROLINA STATE UNIVERSITY
AGRICULTURAL AND RESOURCE ECONOMICS
BOX 8109
RALEIGH, NORTH CAROLINA 27695-8109

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