Fiscal Update: May 1996

Trends in the Labor Market

Revised estimates of employment figures provided by the Michigan Employment Security Commission (MESC) indicate that Michigan unemployment rates have remained below that of the national average for the last two years. The gap was 0.8 percentage points in April. Following an eight-month decline, the Michigan unemployment rate remained steady in April, while the U.S. rate decreased. Growth in wage and salary employment is expected to decline in 1996.

- Michigan unemployment rates decreased from 4.8% in February to 4.6% in March and April. The annual unemployment rate for Michigan for calendar year 1995 averaged 5.3%. The U.S. unemployment rate increased in March, but fell to a 14-month low of 5.4% in April.

- Wage and salary employment in Michigan grew by 2.6 percent in 1995, with a 3.3% growth in private nonmanufacturing out pacing a 2.2% growth in manufacturing employment. 1996 growth is projected at 1.8%, with nonmanufacturing again providing the stimulus, rising by 3.0%, compared to a decrease of 0.6% in manufacturing.

The National Economy

Composite Indices

In predicting the future path of the economy, economists traditionally look at three types of indices: the composite index of leading economic indicators, the composite index of coincident economic indicators, and the composite index of lagging economic indicators. The value of each index is derived from several economic indicators and is now calculated by The Conference Board, Inc., New York, N.Y.

- The composite index of leading economic indicators had been declining steadily for the past 13 months, but rebounded in February to 101.5, an increase of 1.3 percent over January (100.2). This is somewhat of a surprise, suggesting the economy may grow more quickly in 1996 than previously thought, but most economists still believe it will grow at a slower rate than in 1995.

- The composite index of coincident economic indicators, except for a slight downturn in January 1996, has been climbing steadily. It increased by 0.8% in February 1996 to 119.4, the largest increase in over a year. This suggests the economy may be experiencing a surge in growth.

- The composite index of lagging economic indicators declined in February by 0.5% to 102.5, confirming the slowdown in economic growth at the close of 1995.

Components of Gross Domestic Product

Gross domestic product (GDP) measures the total value of all final goods, services, and structures produced in the United States. GDP growth is the standard measure of the performance of the economy.

- GDP increased 0.5% in the fourth quarter of 1995, and at an unexpectedly solid revised rate of 2.3% in the first quarter of 1996. Much of the increase can be attributed to a somewhat surprising surge in personal consumption.

- Movements in personal consumption expenditures, which compose the bulk of GDP at two-thirds of the total, tend to be stable and yield very small variations; thus, this variable is useful in gauging the long-term health of the economy. Consumption climbed by a healthy 2.4% percent (revised) in the first quarter of 1996. This is somewhat surprising considering the harsh winter in the Northeast and the GM brake plant strike (both of which were expected to restrain spending), and suggests a stronger than anticipated economy.

Productivity and Long Run Growth

Labor Productivity is an indicator of the underlying efficiency of the workforce, and is measured as output per hour worked. Economists believe that productivity growth is the fundamental driving force behind long-term economic growth and increases in wealth and the standard of living.

- The rate of productivity growth determines long run per capita wage and personal income growth. As the productivity (efficiency) of the workforce changes, so do their wages and personal income. In the long run, if productivity grows at a slower rate, wages and personal income will also grow at slower rates. This in turn will adversely affect the ability of workers to save, invest, and consume; hence GDP growth will be retarded. Although growth in real personal income and labor productivity is somewhat erratic, for the post World War II era, the trends in both are downward sloping, and the 1990's has seen this trend continue.

- Labor productivity estimates may be biased downward. The increasing role of the service sector, where output measurements are difficult to quantify, and difficulties in measuring the effect of technological change on output suggest that measurements may not accurately capture all aspects of output growth and hence productivity measurements may not reflect true increases in productivity. Thus, the marked downward trend in productivity may be somewhat overstated.

- Lower incomes will inhibit growth in state and federal tax revenue. As income growth slows, tax revenue growth will slow as well. Decreases in economic growth arising from lower labor productivity growth will also curb tax revenue collections from other sources.

The Michigan Page

Personal Income and the Auto Industry

Growth in state tax revenue is largely determined by growth in state personal income. The rate of personal income growth in Michigan decreased markedly at the close of 1995.

- The U.S. Department of Commerce reported that Michigan's personal income totaled $227.1 billion in the fourth quarter of 1995, an increase of 1.4% (the U.S. increased 1.2%), but well below the 2.6% increase of the previous quarter.

- Real disposable income is an indicator of future strength in the durable goods sector. This sector, comprised of light vehicles and other goods, is an important contributor to the Michigan economy. Real disposable income for the U.S. increased by 3.2% in the first quarter of 1996, compared to a 3.6% increase at this time last year, and 0.4 percentage points below that of the fourth quarter of 1995. Real disposable income increased 3.3% in 1995.

- Year-to-date 1996 U.S. car and light truck sales totaled over 4.9 million. Light trucks were once again the primary engines of growth, increasing 14.3% in April (cars gained 10.9%). 1996 year-to-date sales of cars and light trucks are up 6.2% over 1995 levels. The proportion of imports to domestic autos remained relatively stable so far this year. 1996 year-to-date U.S. production is down 11.5% below 1995 levels, largely because of the GM brake plant strike.

- The capacity utilization rate is an indicator of future price levels; as maximum capacity is approached, upward pressure on prices is exerted. The capacity utilization rate in the auto and light truck industry fell from 81.8% to 67.7% in March as a result of the GM strike. Although this one-month drop is excessively steep, it is a continuation of a 12-month downward trend. This trend is also reflected in the manufacturing sector as a whole, suggesting inflation may not be a serious problem in the foreseeable future.

For a copy of this report (with accompanying tables, graphics, and footnotes) prepared by Stephen Marasco under the direction of the HFA economist, please contact Mitch Bean or call the HFA office at 517.373.8080.

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