The Economic Recovery in The U.S. and
Prospects for New Orleans
Remarks by Robert P. Forrestal
New Orleans Rotary Club

May 27, 1992

I. **Outlook for the Nation**

A. Overall Outlook

1. GDP - 2% - a bit higher than earlier expected

2. Jobless rate - 7.0% on average, though by quarter 4 should be back down to level at end of 1991 -- ca. 6.8%

3. CPI -- around 3%

B. Recent data suggest a genuine recovery is under way

1. Progress in alleviating imbalances has been made over past 12 months

a. Fed has pursued accommodative monetary policy stance since September 1990 that has reduced fed funds rate from slightly more than 8% to 3.75% and discount rate from 7% to 3.5%.

b. Monetary policy always works with a lag, but this time the lags were, if anything, more extended because of the substantial debt accumulation by households and corporations during the 1980s.

c. Over the last year or so, households and businesses have used lower interest rates, largely to de-leverage.

(1) Mortgage refinancings have surged

(2) Corporations have called in debt and issued new debt at lower rates or equity

d. Now I believe these are in better position to translate the Fed's monetary stimulus into higher demand

2. Consumer and business attitudes have improved

3. Pent-up demand has developed over time

C. Strengths in the economy's outlook

1. Exports

a. Manufacturing is being boosted by export demand

b. Real export growth will continue to outpace overall GDP growth

c. Latin America and Middle East are strong sources of demand, taking up slack in sluggish European economies

2. Consumer spending

a. Spending on services continue to grow

b. Pick up in durables purchases stronger than anticipated

3. Housing -- This is behind some of improvement in demand for durable goods

a. Improving conditions in resale markets for single-family housing

b. In turn, people are buying more household items like carpets and furniture

D. Weaknesses in the economy's outlook

1. Commercial and Multifamily Real Estate construction

a. Problems with past overbuilding

b. Single-family on an upswing, but not apartments and condos

c. Office building and commercial will still decline for another year

2. Durable Goods

a. Slow prospects for other capital spending by businesses

b. Capacity utilization low and modest growth unlikely to put pressure on this during 1992

II. **Prospects for New Orleans**

While this outlook for the nation is considerably brighter than it has been for some time, the situation in Louisiana, and particularly New Orleans, is a bit different. As the nation and the region move into recovery, Louisiana is maintaining its traditional contrarian economic role by threatening to slip back into recession. The main reason is the important role of energy in the local economy.

A. Energy's Countercyclical Role

The reversal is especially painful because Louisiana did not enjoy much of the highly touted prosperity and growth of the 1980s. At the beginning of the decade, when oil prices were booming, some 250,000 people moved into the state, fueling construction of houses, apartments, offices, and industrial facilities. Then oil prices began a long and substantial decline, and New Orleans languished. By 1986 the unemployment rate had soared to 11%. While the jobless rate gradually declined, much of the improvement was the result of people moving elsewhere to look for jobs. In fact, the state lost most of the 250,000 people who had moved in at the beginning of the decade. In turn, this outflow of people meant that the houses, apartments, offices and industrial facilities built during New Orleans' early 1980s boom were simply no longer needed. In turn, some local financial institutions have felt the pinch. Although much of the real estate boom was not financed locally, area banks and thrifts have been closely involved with the energy industry and some came to reflect its troubled state.

Nonetheless, by 1990, the local economy was looking up. The New Orleans unemployment rate had fallen to the national average. Payroll employment expanded faster than it had in ten years. Single-family housing hit bottom in early 1991, and commercial construction showed signs of improvement. Through mid-1991, New Orleans employment continued to expand slowly, even as other Sunbelt cities, such as Atlanta and Orlando, suffered employment losses in the national recession.

Then energy prices fell, particularly for natural gas. This drop accelerated a longer term structural shift of major oil companies out of domestic production. U.S. producers have been shifting drilling resources and capital for exploration overseas because oil and gas abroad tend to be closer to the surface and thus cheaper to find. Additionally, tax incentives for drilling have been eliminated and environmental restrictions, tightened. Perhaps most importantly, technological advances have been taking place that allow companies to explore more efficiently, that is, to drill less with greater success. As a result of these short and longer term developments, local wells have been capped and Gulf platforms, shut down. In fact, the number of Gulf platforms being disassembled and plugged last year nearly equalled the number of new wells drilled. Nationally, rig counts are at a post World War II low. Little more than a third of the mobile rigs available for drilling in the Gulf are under contract.

Aside from shifts to overseas production, several major oil companies have announced or implemented cutbacks and consolidation to Lafayette and Houston. As a result of these and other layoffs, energy-related employment in the New Orleans area has fallen by nearly 2,000 since last spring, and these were high-wage jobs. Their loss disproportionately dampens the region's purchasing power. Clearly, these developments bode ill for New Orleans outlook in the next year or so.

B. Port Activity and Tourism--Future Strengths

Fortunately, New Orleans has the advantage of having substantial port and tourism activity, which will help mitigate some of the economic distress arising from these fundamental changes in the energy sector. In these areas, the dynamics underlying business activity are more "in sync" with the rest of the United States. As I mentioned, international trade is a key source of strength in the recovery nationally, largely because the dollar's value relative to other foreign currency has helped make many U.S. products competitive. Looking ahead, I see little significant currency realignment on the horizon. The dollar could appreciate slightly as the U.S. economy strengthens and interest rate differentials narrow, assuming other industrial economies remain sluggish. Thus, the dollar should continue to support port activity and international tourism.

Statistics on port activity indicate that it has been a source of strength. In the first quarter of 1992, New Orleans' port activity (imports plus exports) increased 13 percent over the same period in 1991. However, the 1991 numbers were somewhat depressed because of the diversion of many ships for the Gulf War. Steel shipments have been particularly strong after the port won back a USX shipment contract from the Port of Mobile. As you know, New Orleans is currently in the midst of a major capital improvement project which began in 1991, adding berths and improving truck and rail access. The improvements, which should be completed in mid-1993, will enhance the port's intermodal shipment capability.

In the coming years, New Orleans could benefit greatly from increased trade with Central and South America. Latin America, with Puerto Rico at the lead, is already the port's numberone "trading partner." (Imports from the Far East are second in importance.) Latin America's rapidly developing economies and the implementation of the North American Free Trade Agreement (NAFTA), should result in tremendous growth in trade with Latin America. New Orleans, along with other southern ports, are uniquely positioned to take advantage of these opportunities.

The tourism industry in New Orleans has begun to recover and is likely to continue expanding through 1992. Convention attendance and hotel occupancy rates are improving; advance bookings for 1992 are exceeding 1991 levels to date, and some new construction has been initiated. Tourist expenditures have been boosted by a marked increase in cruise passengers. Although New Orleans' tourism market is primarily domestic, it also attracts more international visitors than any other southeastern destination than Florida. Over time this segment of the industry holds great promise for growth.

III. Policy Implications and Conclusion

A. Modest recovery under way

1. Restructuring in corporate and consumer finance takes time but positive momentum has been set
2. I wish I could see similar progress with federal budget deficit
3. New Orleans is facing some tough times; nonetheless, but it has the resources to make the kind of changes that will position it for growth and prosperity in the 21st century

B. Lessons

1. I hope that locally and nationally we will learn from our recent

experiences of debt-propelled growth and its aftermath of recession.

2. I hope this painful experience has made us more willing to support policies that foster sustainable, long-term growth.