

The Economy in Perspective

Close calls ... The Federal Reserve's Open Market Committee will meet on September 24 to review the state of the economy and to consider making changes in its chief monetary policy instrument, the federal funds rate. Financial market participants have been poised for a September rate increase for nearly six months, but their expectations continue to rise and fall with the tide of information about near-term economic activity. In August, for example, an upward revision of second-quarter real GDP, coupled with stronger-than-expected data about housing starts and durable-goods orders, persuaded investors to retract their prediction of an imminent economic slowdown.

Despite last month's vibrant economic news, financial market participants did not react similarly to August's labor market situation. The Bureau of Labor Statistics reported on Friday, September 6, that net new jobs increased by 250,000, hourly earnings jumped sharply, and the unemployment rate fell to 5.1 percent—its lowest point (on a comparable basis) since early 1973. What prevented a sharp sell-off in the nation's financial markets?

For one thing, the markets had already declined the previous day on expectations of a strong report. Just as important, perhaps, was analysts' recognition that the unemployment rate fell primarily because of a steep decline in the labor force, not because employment surged. Since many observers are convinced that the economy is operating at, or beyond, its ability to generate output without boosting inflation, such distinctions are regarded as highly relevant to the outlook.

Preoccupation with the ebb and flow of daily economic news tends to obscure policymakers' longer-term objectives and downplays the problems they face along the way. Some people expect the Federal Reserve to carefully control short-term movements in economic activity and, at the same time, to employ these fluctuations to regulate the pace of inflation. Although monetary policy may affect real economic activity in the short run, it has no ability to move real output systematically along a predetermined growth path. Over time, the average rate of real economic growth stems from productivity gains and from the amount and quality of labor and capital employed in production.

Similarly, monetary policy probably has little influence over short-run price-level fluctuations, but it plays the determinative role in establishing the inflation trend through control of the

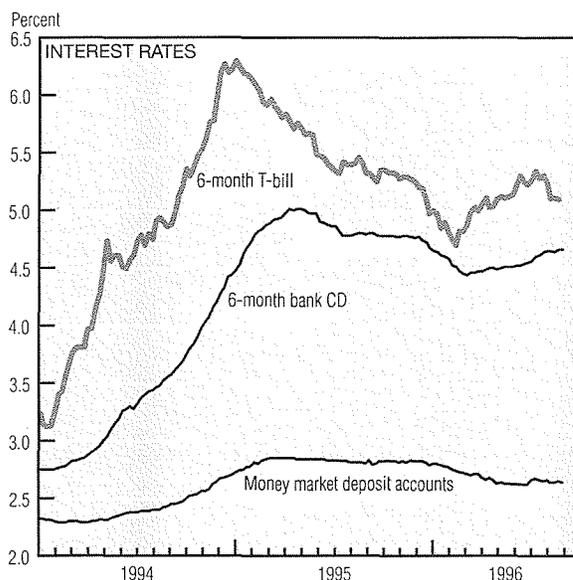
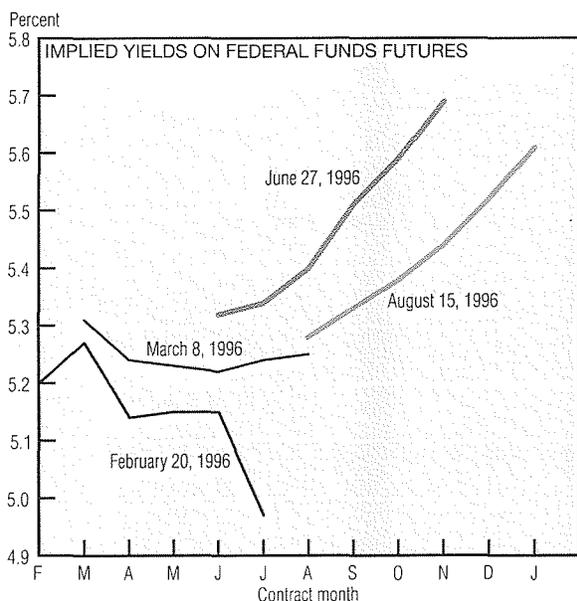
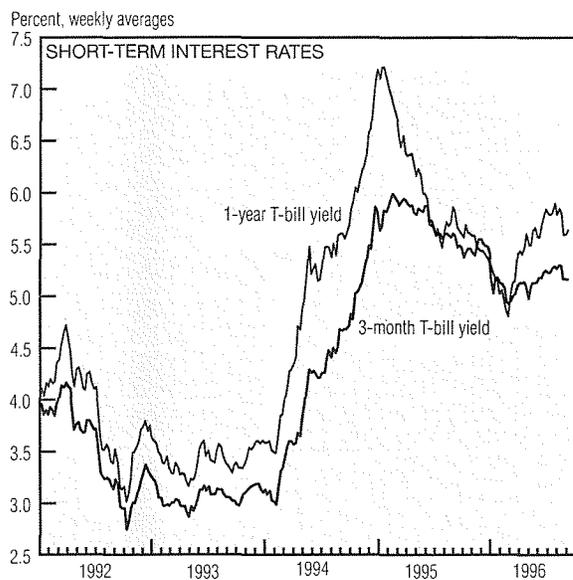
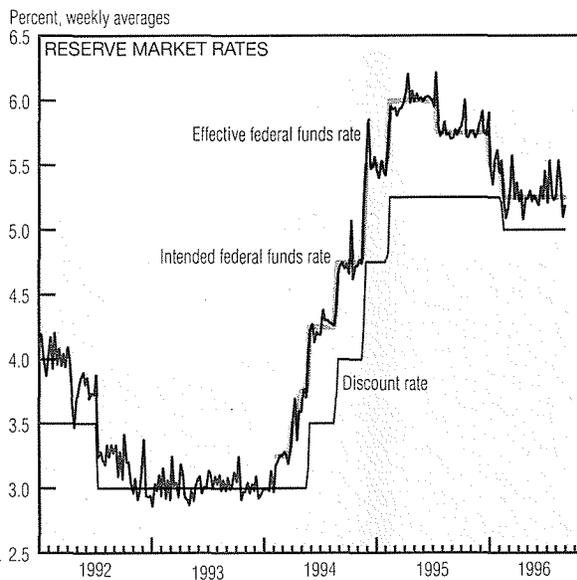
money supply. The Federal Reserve did not establish a numerical objective or time path when it took strong actions in 1979 and 1980 to halt the prevailing inflation spiral. It was sufficient then to recognize that double-digit inflation was too high and had to be stemmed.

As it happened, the inflation rate fell more quickly and remained lower than the public initially expected. By the mid-1980s, the Consumer Price Index (CPI) was fluctuating around a trend rate of 4.5 percent. Once it became clear that inflation had stabilized, the Fed undertook a program of further disinflation. Again, there were no numerical goals or time frames, but there was a public commitment to achieve price stability (commonly defined as inflation so low that it does not affect economic decisions).

During the approximately 10 years that the Federal Reserve has been committed to this course, it has both tightened and eased its policy stance. It is not likely that every policy action has been perfect: At times steps may have been taken too quickly or too late, and some may have been either too large or too small. Nevertheless, both inflation and inflation expectations have moved onto a lower track. Since 1991, the CPI has been hovering around 3 percent, and real output has expanded in every year but one. Capital formation rates have strengthened notably, raising hopes of faster productivity growth.

Some economists consider a 3 percent inflation rate to be close enough for government work, while others think that 0 or 1 percent is more appropriate. Operating within the narrow range of 0 to 3 percent, and recognizing that some measurement biases are present in all inflation indexes, policymakers must proceed carefully. However, the experience of the last 10 years should leave little doubt about the Federal Reserve's ability to achieve a new, lower inflation trend over time. Perhaps more explicit inflation targets will prove useful in narrowing the price-stability range.

For the moment, financial markets do not appear to be focused on price stability per se. Instead, they seem more concerned about the prospect of inflation breaking out above its 3 percent trend. The federal funds futures markets and the degree of upward slope built into the U.S. Treasury yield curve clearly reflect the market's view that the Federal Reserve will tighten monetary policy at its September meeting. The truth is close at hand.



SOURCES: Board of Governors of the Federal Reserve System; the Chicago Board of Trade; and *Bank Rate Monitor*, various issues.

Since its February meeting, the Federal Open Market Committee (FOMC) has chosen to maintain the federal funds rate near an intended level of 5¼%. The funds rate (the interest rate banks pay on overnight loans to each other) is an anchor for other short-term rates. Between June 1995 and February 1996, the FOMC voted to lower the intended funds rate in three increments of 25 basis points each. The yield on one-year Treasuries fell about two percentage

points from its January 1995 peak, while the yield on the three-month Treasury bill dropped to below 5%. That these yields had fallen below the overnight rate suggested an expectation of further funds-rate cuts.

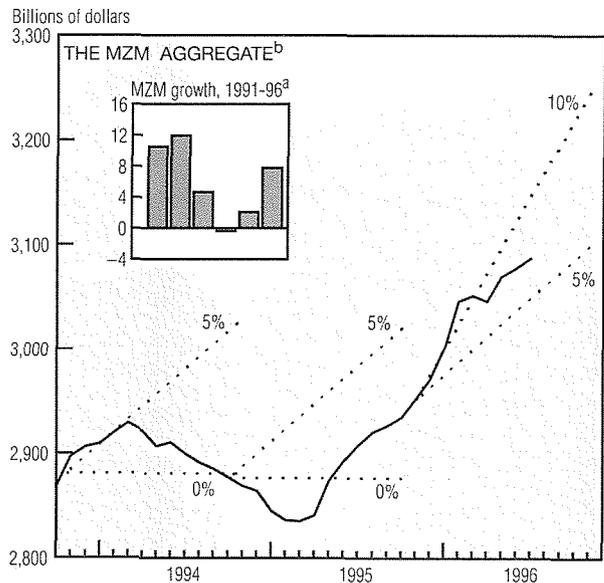
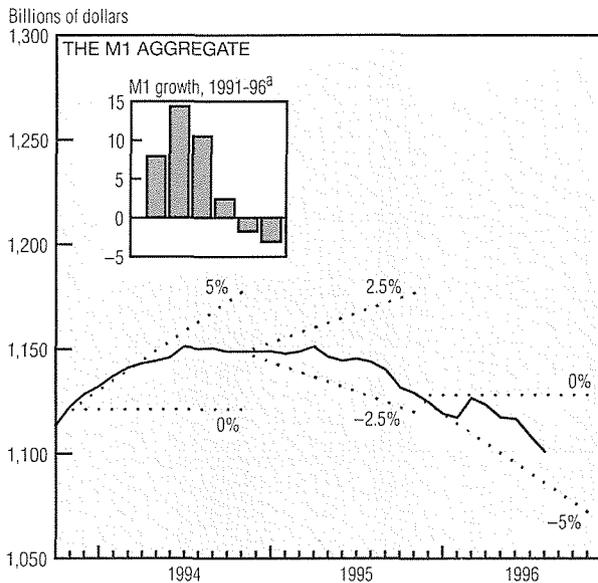
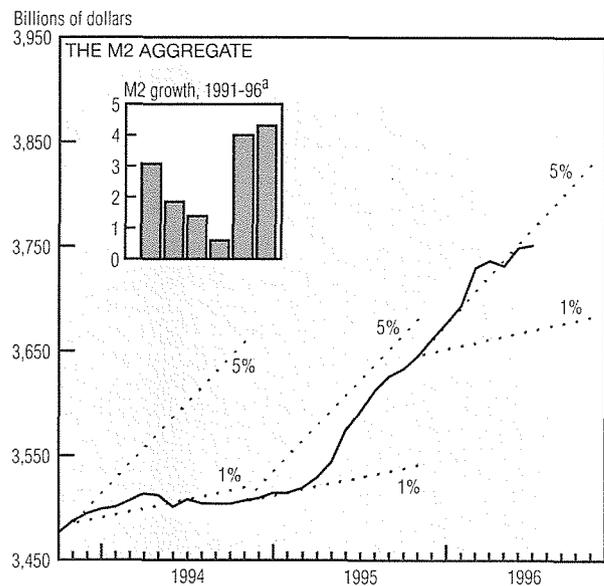
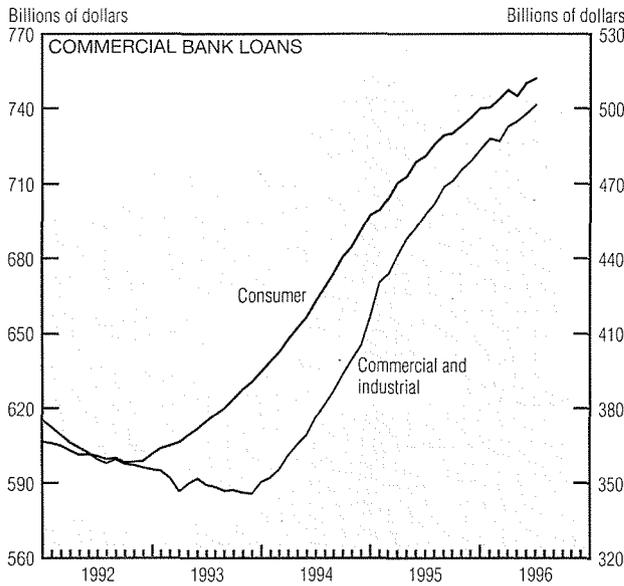
Early this year, however, the one-year yield changed direction quickly as market sentiment reversed. By midyear, money market yields imparted an expectation that the next deliberate policy action would result in a funds-rate increase. Such an expectation was also evident in the fed

funds futures market. The implicit yields on these instruments in late June indicated an expectation that the funds rate would increase at least 25 basis points by early fall. As the summer progressed, however, the expected trajectory shifted out by more than two months.

Interest rates paid on certificates of deposit (CDs) and money market deposit accounts (MMDAs) respond sluggishly to market conditions. As a

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Monetary Policy (cont.)



a. Growth rates are calculated on a fourth-quarter over fourth-quarter basis. Annualized growth rate for 1996 is calculated on an estimated August over 1995: IVQ basis.
 b. MZM is an alternative measure of money that includes M2 plus institutional money market mutual funds less small time deposits.
 NOTE: All data are seasonally adjusted. Last plot is estimated for August 1996. Dotted lines represent growth ranges and are for reference only.
 SOURCE: Board of Governors of the Federal Reserve System.

consequence, the opportunity cost of a given deposit (typically measured as the spread between the interest rate paid on a Treasury bill and that paid on the deposit) tends to rise and fall with market rates.

Commercial bank loan growth has slowed in recent months. Nevertheless, both consumer and commercial and industrial credit continue to expand at a moderate pace. With lessened credit demands, banks are unlikely to raise deposit rates quickly in response to a firming in

market conditions. Any rise in opportunity cost would probably induce a further slowdown in the monetary aggregates.

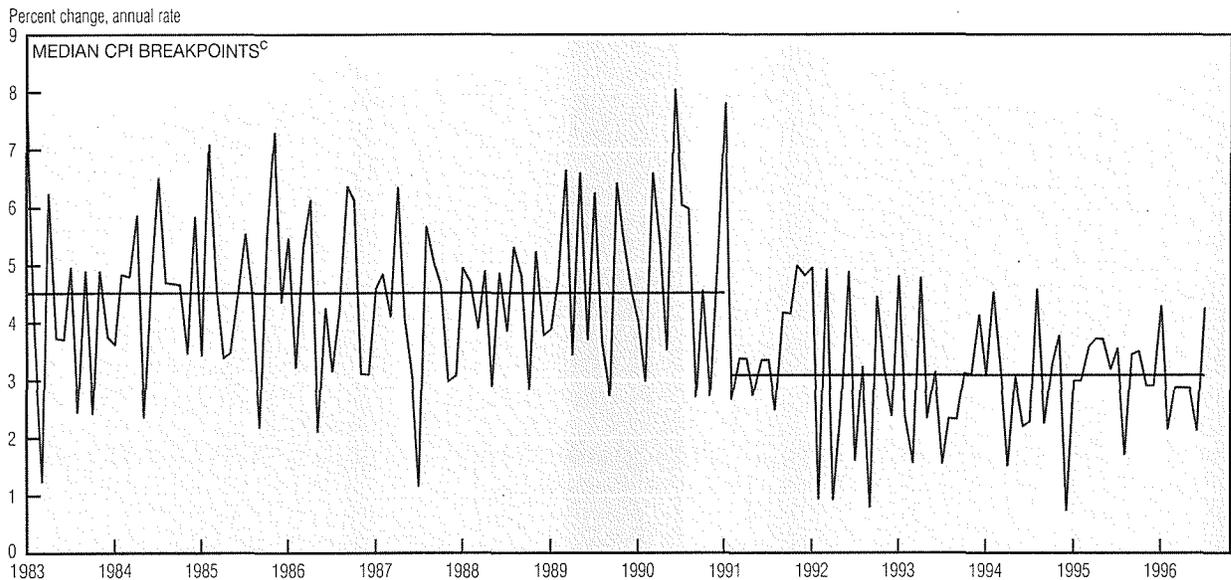
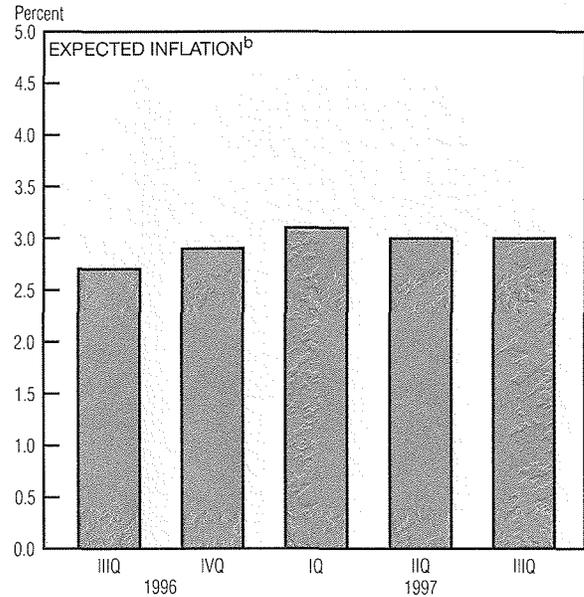
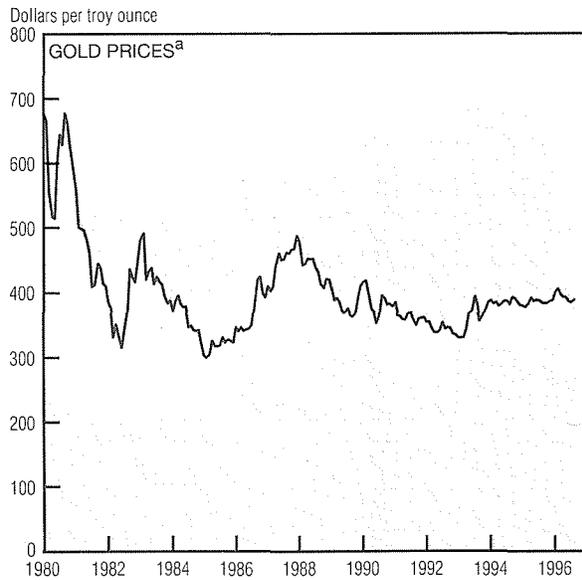
The response of money growth to interest-rate changes typically occurs with a lag. Indeed, M2 growth slowed in the second quarter only after the effects of the previous rate reductions wore off. The aggregate appears to be responding more consistently with its historical pattern, after behaving atypically in the early 1990s. Federal Reserve Chairman

Alan Greenspan noted in his recent Congressional testimony that the relationship linking M2 to its opportunity cost has "reasserted itself."

M1 continues to fall. It is widely understood that weakness in this aggregate is largely related to the implementation of sweep accounts, which automatically transfer funds from other checkable deposits (OCDs) to MMDAs, when balances allow. It is believed that M1 would be increasing were it not for the proliferation of sweep accounts.

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Monetary Policy (cont.)



a. Handy and Harman base price, New York.

b. Survey of Professional Forecasters, Federal Reserve Bank of Philadelphia.

c. Horizontal lines represent trends.

SOURCES: DRI/McGraw-Hill; the Federal Reserve Bank of Philadelphia; and the Federal Reserve Bank of Cleveland.

The MZM measure of money comprises instruments that have zero maturity and hence are redeemable at par on demand. Because this aggregate includes both OCDs and MMDAs, it is immune to the effects of sweep accounts. MZM growth has moderated from its rapid pace earlier this year. The recent modest increase in market interest rates is expected to slow MZM's pace even further.

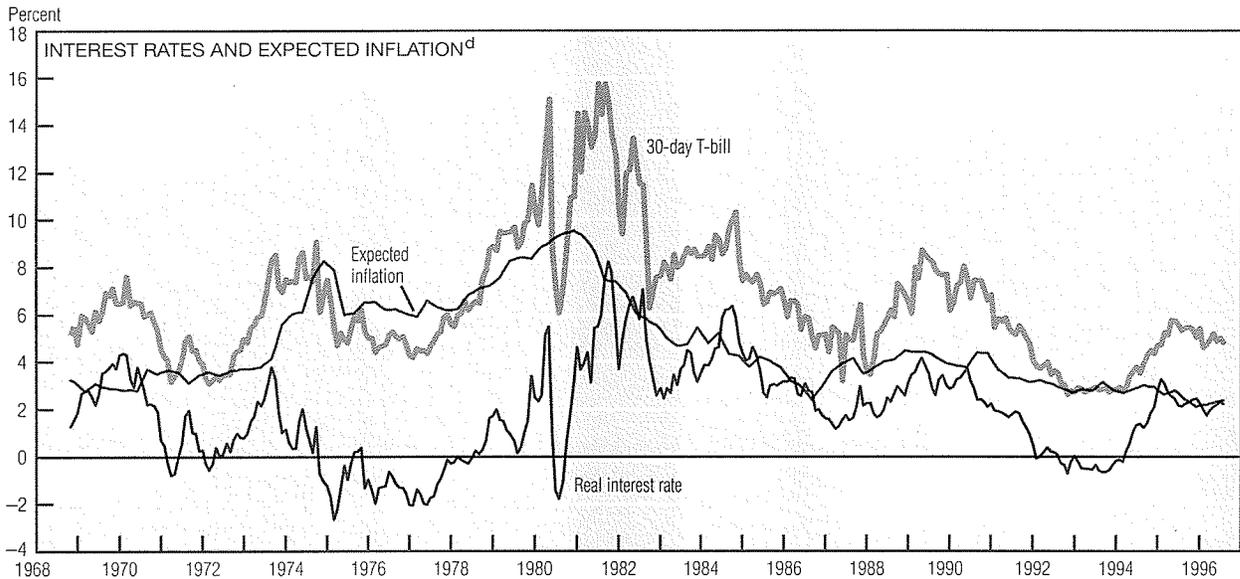
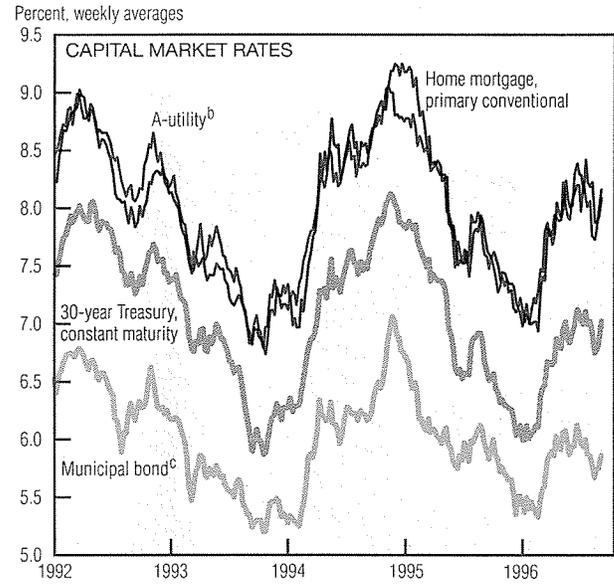
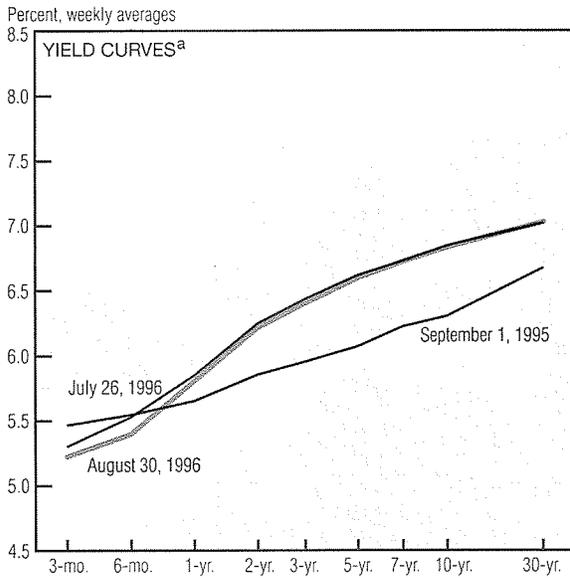
Since early 1991, core inflation (as measured by the median CPI) has

been in the neighborhood of 3%. Facing signs of inflationary pressures in early 1994, the FOMC headed off the threat with a series of actions that initially led to a period of rising interest rates and slowing money growth.

As inflationary pressures subsided in 1995, the FOMC took actions that led to falling interest rates. The series of funds-rate reductions, although inducing an acceleration in money growth, were modest. Consequently, neither M2 nor MZM growth has persisted at excessive rates.

The price of gold has historically been one of the most sensitive indicators of inflation. Although gold exceeded \$400 per ounce in February, its price has receded substantially since then, suggesting that inflation fears are contained. Moreover, survey data on inflation expectations corroborate a stable outlook for the price level. This stability, however, hinges on the belief that the FOMC will act swiftly to head off any potential for accelerating inflation.

Interest Rates



a. All instruments are constant-maturity series.

b. Estimate of the yield on a recently offered, A-rated utility bond with a maturity of 30 years and call protection of five years.

c. Bond Buyer Index, general obligation, 20 years to maturity, mixed quality.

d. The real interest rate and expected inflation rate are from the Survey of Professional Forecasters and are calculated using the 30-day T-bill rate.

SOURCES: Board of Governors of the Federal Reserve System; the Federal Reserve Bank of Philadelphia, Survey of Professional Forecasters; and *The Wall Street Journal*, various issues.

After having spent most of August at lower levels, the yield curve has recently shifted up to where it stood at the end of July. The 3-year, 3-month spread and the 10-year, 3-month spread have both widened slightly, moving to 118 and 161 basis points, still well above their 30-year averages of 80 and 120.

Capital market rates have also followed this pattern, but while 30-year Treasuries and municipal bonds have moved within one basis point of their July values, mortgage rates have not kept pace. Utility rates have moved above mortgage rates

for the first time since the week ending July 5.

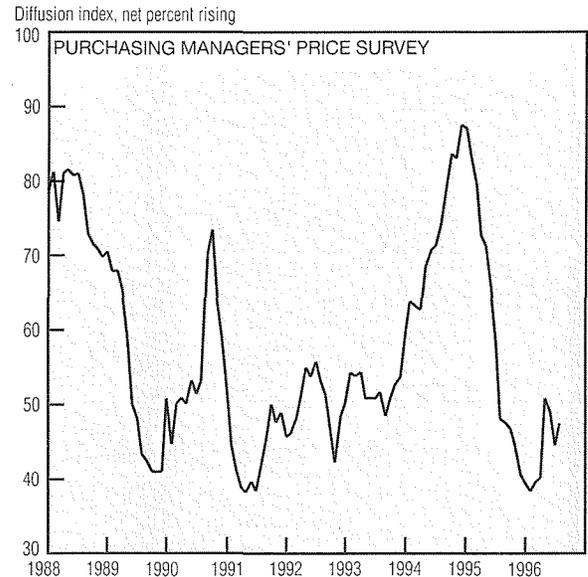
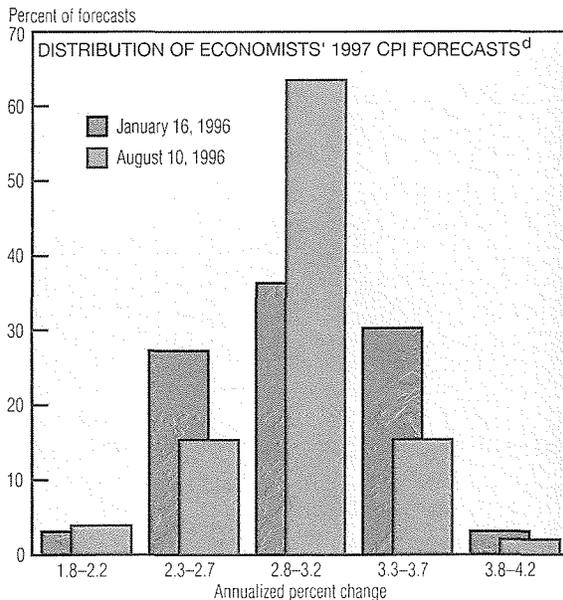
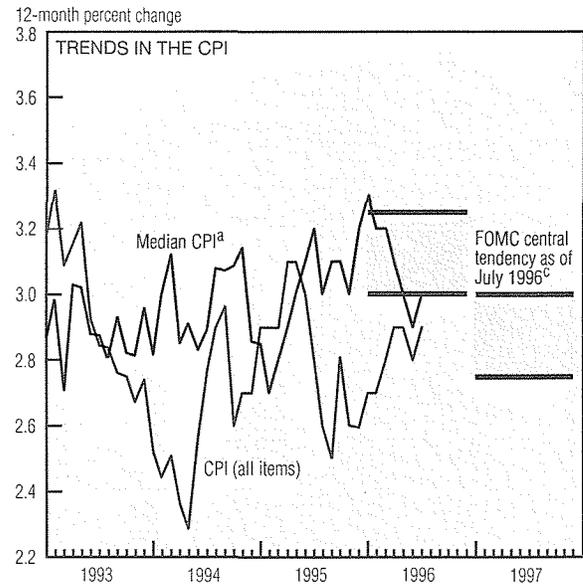
Interest rates are usually quoted in nominal terms, but it is sometimes better to look at them from a real, or inflation-adjusted, perspective. Inflation adjustments come in two shapes. After a bond has matured, its return can be adjusted ex post for the inflation that actually occurred. Prior to maturity, a bond's yield can be adjusted ex ante for expected inflation. The bottom chart shows one such ex ante adjustment that accounts for the risk of inflation and the correlation between inflation

and real interest rates.

Since the beginning of last year, real rates have averaged around 2%, rising from negative levels in early 1994 to more than 3% in the first few months of 1995. Expected inflation rates have shown a similar uneven decline, edging down from 2.7% in February 1995 to just below 2.4% last month. These movements seem relatively minor compared to the large shifts of the early 1980s, when the 30-day T-bill went above 15% and real rates dropped by more than 7% in less than a year.

Inflation and Prices

	Annualized percent change, last:				1995 avg.
	1 mo.	7 mo.	12 mo.	5 yr.	
July Price Statistics					
Consumer Prices					
All items	3.1	3.5	2.9	2.9	2.6
Less food and energy	3.7	3.0	2.7	3.1	3.0
Median ^a	4.2	3.1	3.0	3.1	3.2
Producer Prices					
Finished goods	-0.2	2.0	2.6	1.6	2.1
Less food and energy	0.4	0.7	1.5	1.6	2.6
Commodity futures prices^b					
	-16.7	1.1	5.8	3.3	5.4



a. Calculated by the Federal Reserve Bank of Cleveland.

b. As measured by the KR-CRB composite futures index, all commodities. Data reprinted with permission of the Commodity Research Bureau, a Knight-Ridder Business Information Service.

c. Upper and lower bounds for CPI inflation path as implied by the central tendency growth ranges issued by the FOMC and nonvoting Reserve Bank presidents.

d. Forecast of the Blue Chip panel of economists.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; the Federal Reserve Bank of Cleveland; National Association of Purchasing Management; the Commodity Research Bureau; and *Blue Chip Economic Indicators*, January 16 and August 10, 1996.

After dropping sharply in June, retail prices resumed the strong upward trend that began last December. The Consumer Price Index (CPI) increased at an annualized rate of 3.1% in July, and has risen 3.5% since the beginning of the year, almost a percentage point higher than 1995's average increase. The core inflation indicators moved up even more in July: The median CPI, and the CPI excluding food and energy, rose an annualized 4.2% and 3.7%, respectively.

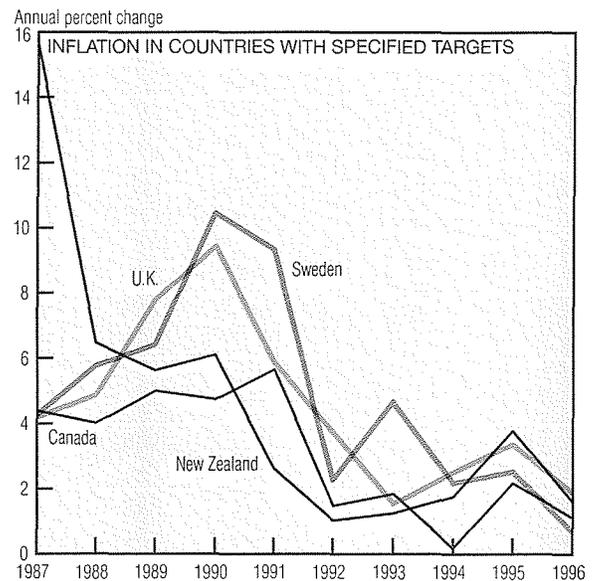
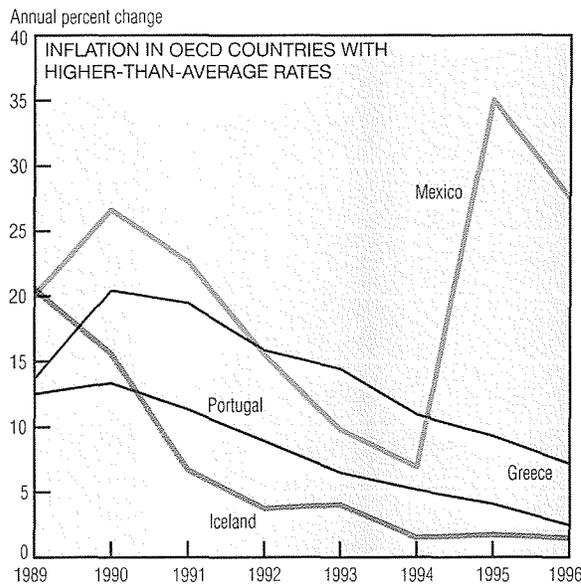
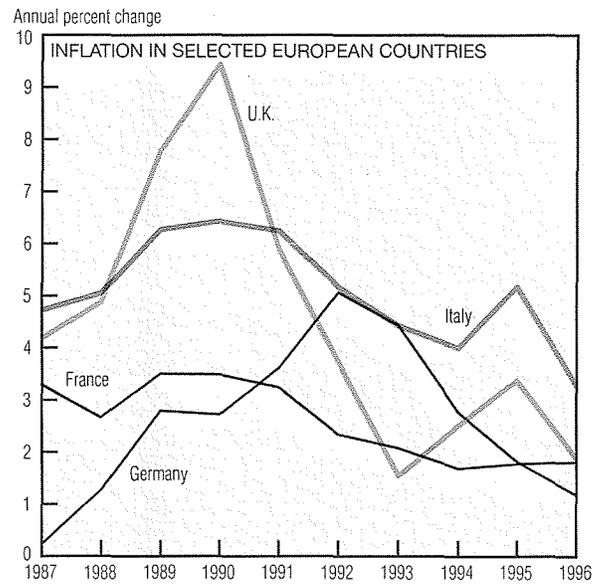
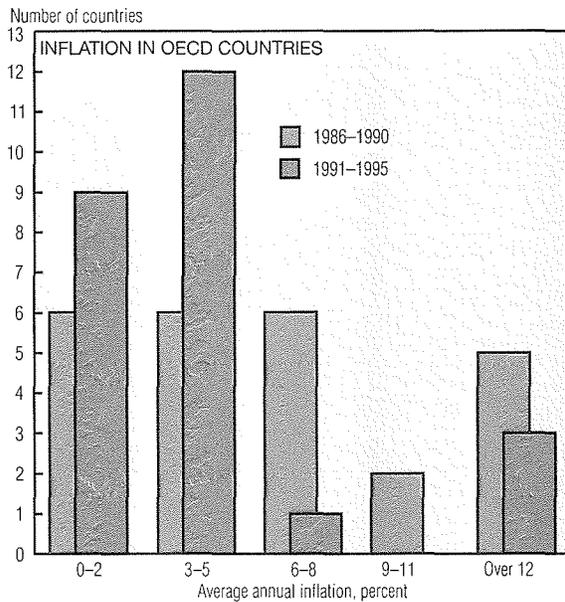
While the current 12-month trend in the CPI is a bit below the central tendency range projected by the Federal Open Market Committee (FOMC) for 1996, year-to-date estimates suggest that CPI growth for the remainder of the year must average slightly less than 3% if the index is to stay within the *upper* bound of that projection. For 1997, the FOMC sees retail price increases slowing to less than 3%. The Blue Chip projections for the CPI are not materially different. For 1997, roughly two-

thirds of the economists surveyed see the index increasing around 3%. The respondents who anticipate much higher, or lower, inflation rates appear to be evenly balanced and few in number.

Reports from industry continue to show much less inflationary pressure than was noted at the retail level. Year to date, the Producer Price Index (PPI) has risen at an annualized rate of only 2.0%, and much of that upward climb has

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Inflation and Prices (cont.)



SOURCE: Organisation for Economic Co-operation and Development (OECD), *Main Economic Indicators*, January 1986 through May 1996.

come from energy commodities. Excluding food and energy, the PPI is up less than 1% this year. Industrial purchasing managers are about evenly divided between those observing price increases and those noting price declines.

Compared with other nations, the U.S. inflation performance has been about average in recent years. In the past five years, the average U.S. inflation rate has been just below the 3% mark. Of 25 countries belonging to the Organisation for Economic Co-operation and Development (OECD), nine had better inflation

records over the 1991-95 period, 12 were similar or slightly higher, and only four were substantially worse. This is a marked difference from the late 1980s and reflects a strong disinflationary sentiment among a growing number of nations.

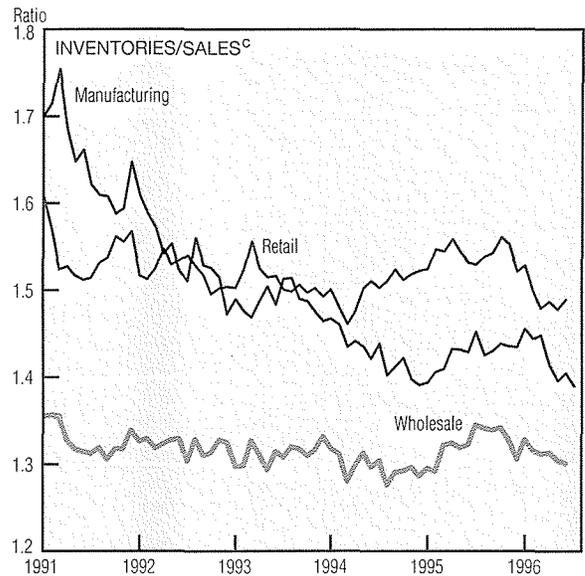
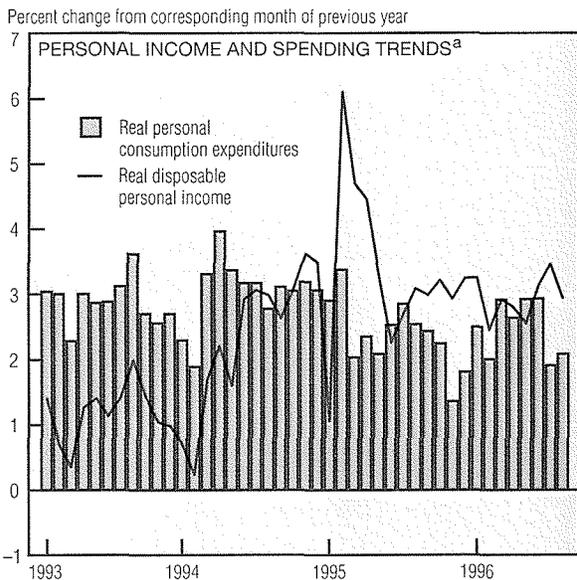
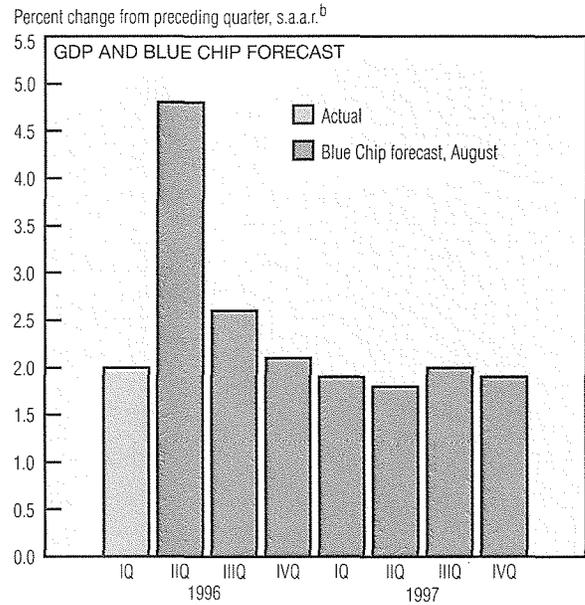
In Europe, many major countries have lowered their inflation rates to 3% or less—for some, nearly a 50% reduction over the last decade. Part of this improvement can probably be tied to the “convergence criteria” imposed by the European Monetary Union. Even nations that tended to suffer from persistent double-digit

inflation in the 1980s, such as Portugal, Greece, and Iceland, have been able to engineer dramatic improvements in their inflation rates this decade. Mexico appeared to be following such a path, although a sharp devaluation of the peso in December 1994 reversed this trend.

The disinflationary trend around much of the world has, in some cases, been supported by legislated commitments for central banks to achieve specified inflation targets. Four such nations—New Zealand, Sweden, the U.K., and Canada—have recently brought their inflation rates down to 2% or less per year.

Economic Activity

	Change, billions of 1992 \$	Percent change, last:	
		Quarter	Four quarters
Real GDP	80.2	4.8	2.7
Consumer spending	39.0	3.4	2.6
Durables	16.9	11.8	6.9
Nondurables	5.9	1.7	1.3
Services	16.5	2.5	2.3
Business fixed investment	7.4	4.0	5.7
Equipment	8.2	6.0	6.5
Structures	-0.5	-1.1	3.4
Residential investment	10.2	15.9	9.7
Government spending	25.1	8.2	1.2
National defense	8.6	11.5	-1.5
Net exports	-11.2	—	—
Exports	9.5	4.8	6.9
Imports	20.7	9.4	5.3
Change in business inventories	10.2	—	—



a. Chain-weighted data in 1992 dollars, seasonally adjusted.
 b. Seasonally adjusted annual rate.
 c. Seasonally adjusted.

SOURCES: U.S. Department of Commerce, Bureau of the Census and Bureau of Economic Analysis; and *Blue Chip Economic Indicators*, August 10, 1996.

The Commerce Department increased its second-quarter GDP estimate by \$9.4 billion, lifting the quarterly growth rate from 4.2% to 4.8%. Upward adjustments to business fixed investment and government spending, and a downward reappraisal of imports, dominated the revisions. The Department also lowered its estimates of consumer spending and the rate at which businesses added to their inventories.

The second-quarter growth rate

was markedly better than the 2.0% posted in the first three months of the year. Much of the improvement resulted from a rebuilding of automobile inventories, government spending at all levels, consumer spending on durables, and investment in residential structures.

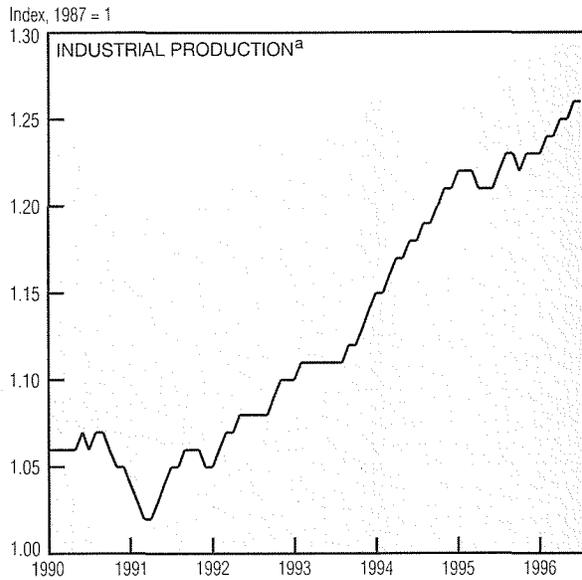
Most economists do not see the second-quarter growth spurt continuing. Those responding to the Blue Chip survey, for example, expect the economy to expand approximately 2.6% in the third quarter,

2.1% in the final quarter, and 1.9% in 1997. According to many economists, a long-term growth rate of 2% (or slightly faster) is consistent with trends in U.S. investment, work hours, and productivity over the last decade or so.

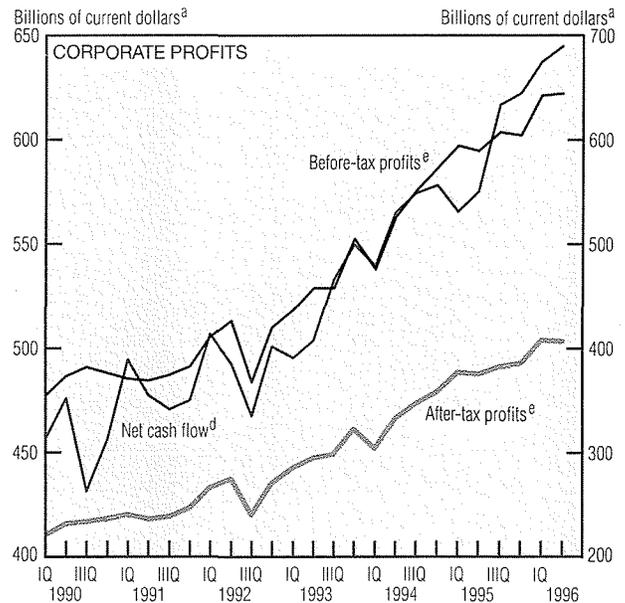
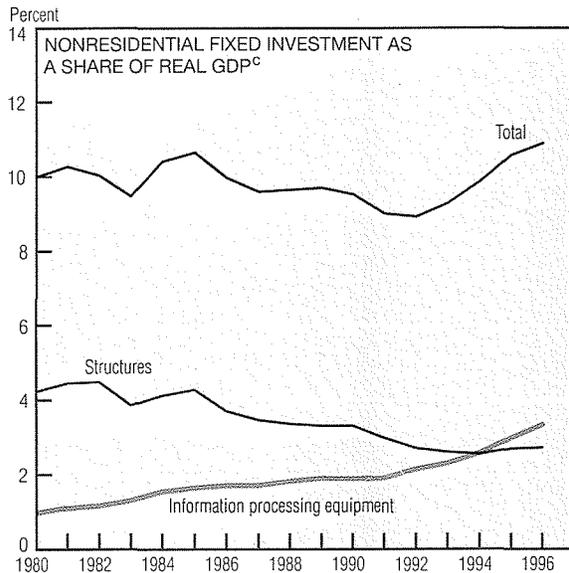
Real personal consumption spending increased approximately 2% in June and July on a year-over-year basis, slowing from a 2.6% average clip over the first five months of the

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Economic Activity (cont.)



	July 1996 level, thousands	Percent change since	
		June 1996 ^b	July 1995
Housing starts, total	1,455	-1.3	0.3
Housing starts, single unit	1,133	-5.7	0.7
Permits, total	1,457	3.0	7.3
Permits, single unit	1,073	-1.1	5.5
New homes sold, single unit	783	7.9	0.1
Existing homes sold, single unit	4,140	-0.5	4.3



a. Seasonally adjusted.
 b. Not annualized.
 c. Chain-weighted data in 1992 dollars, seasonally adjusted.
 d. Includes inventory valuation and capital consumption adjustment.
 e. Excludes inventory valuation and capital consumption adjustment.
 SOURCES: U.S. Department of Commerce, Bureau of the Census and Bureau of Economic Analysis; Board of Governors of the Federal Reserve System; and the National Association of Realtors.

year. Real disposable income growth continues to hold steady near 3%. The difference between consumption and income growth suggests that consumers may be attempting to adjust their debt positions.

Inventories were also weaker than expected in June, but inventory-to-sales ratios looked favorable at all levels. Retailers were holding only 1.49 months' worth of stock in June, and manufacturers' inventory-to-shipping ratio reached a low of 1.39 in July. Further inventory trimming is

unlikely; in fact, many economists are expecting some rebuilding.

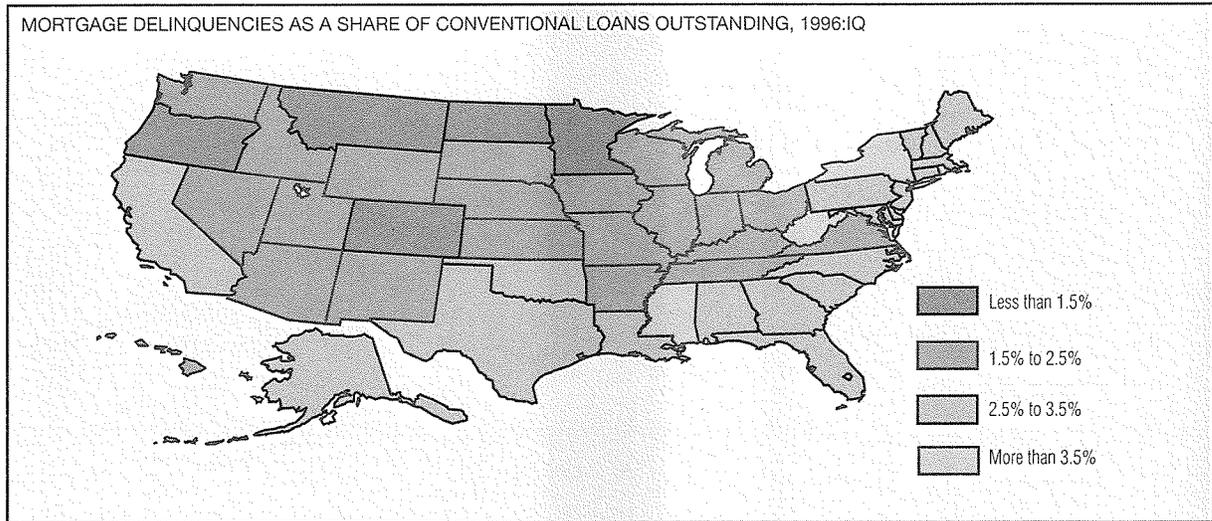
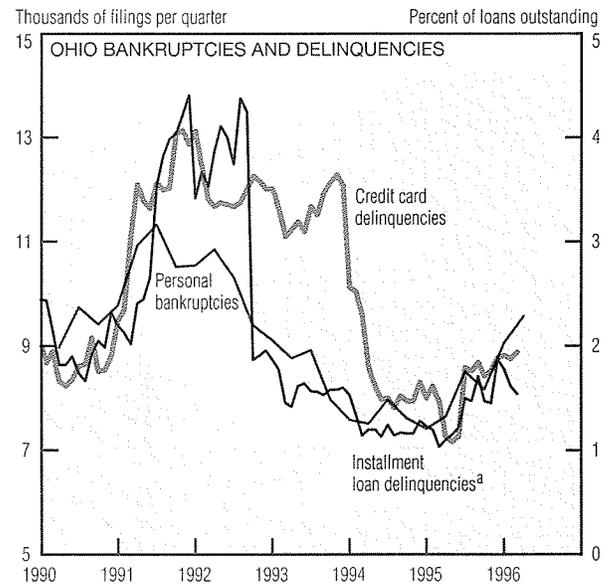
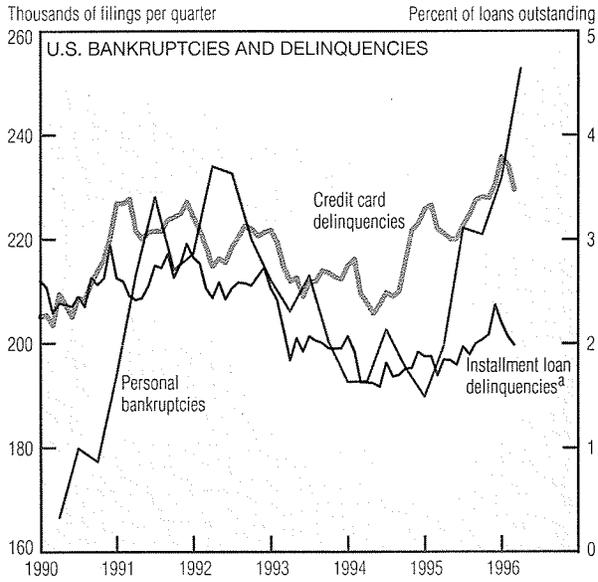
Although housing starts fell 1.3% in July, total starts remained at a respectable 1.46 million units and permits increased. Sales of new and existing homes in recent months suggest some moderate slackening in demand, but consumer attitudes about home buying are holding steady.

Business fixed investment has accounted for 10.9% of GDP this year, the highest share since at least 1980.

Much of this investment reflects acquisition of information equipment, mainly computers. Investment in business structures has slowed since the early 1980s.

Despite slackening in the second quarter, after-tax corporate profits have demonstrated relatively strong growth over the last year. Corporate cash flow, which exerts a stronger influence on near-term investment decisions, has shown even higher growth.

Consumer Bankruptcies



a. Based on the "summary of accounts (closed-end only)" data reported in the American Bankers Association's *Consumer Credit Delinquency Bulletin*.
 SOURCES: American Bankruptcy Institute; American Bankers Association, *Consumer Credit Delinquency Bulletin*; and Mortgage Bankers Association of America, National Delinquency Survey.

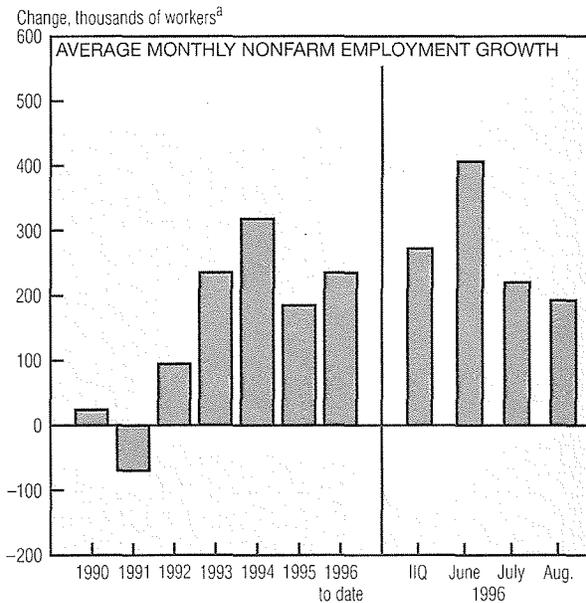
Much attention has been given to the recent rise in bankruptcies. Indeed, in the first quarter of this year there were 252,761 personal bankruptcy filings in the U.S., the highest quarterly posting in history and an increase of 27% since 1995:1Q. Personal bankruptcies in Ohio have mirrored national trends, although Ohio's current levels are still substantially below the high of 11,326 filed during the second quarter of 1991.

Despite these recent concerns, consumer delinquencies on both installment loans and credit card debt have been falling since the beginning of the year. While such easing might foreshadow a reduction in the number of consumer bankruptcies through the end of the year, many financial institutions are reporting an increase in the number of "surprise bankruptcies," or bankruptcy filings with no prior delinquencies. Thus,

many analysts remain cautious about the outlook for the future.

Mortgage delinquencies have also risen in the U.S. over the last year, from 2.31% of all conventional mortgages outstanding in June 1995 to 2.67% in June 1996. The highest delinquency rates appear to be in the South and East, while those in the Midwest, the Great Plains, and the Mountain states generally remain below 2.5%.

Labor Markets

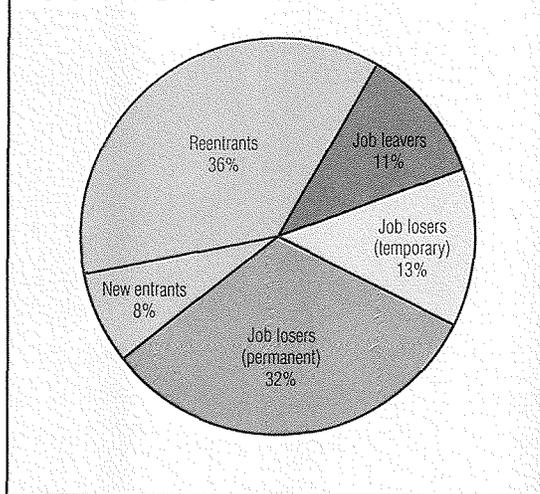


Labor Market Conditions^a

	Average monthly change (thousands of employees)				
	1995	1996			
	Year	IIQ	June	July	August
Payroll employment	185	272	219	228	250
Goods-producing	-5	26	13	-9	29
Manufacturing	-12	5	-5	-27	25
Construction	9	21	19	23	6
Service-producing	190	246	206	237	221
Services	110	116	109	74	81
Retail trade	36	77	76	88	21
Government	9	19	-7	39	77
Local	11	22	14	31	75
Household employment	34	153	148	274	171
Average for period					
Civilian unemployment rate (%)	5.6	5.4	5.3	5.4	5.1



SOURCE OF UNEMPLOYMENT^a



a. Seasonally adjusted.

b. Vertical line indicates break in data series due to survey redesign.

SOURCE: U.S. Department of Labor, Bureau of Labor Statistics.

Continuing this year's string of strong labor market reports, August brought 250,000 net new jobs and a drop in unemployment to a seven-year low of 5.1%. This unemployment rate reflects adjustments to the household survey methods, started in January 1994, that were expected to raise the measured unemployment rate as much as 0.5%. If these adjustments are taken into account, we have to look back to early 1973 to find an

equally low (4.6%) jobless rate.

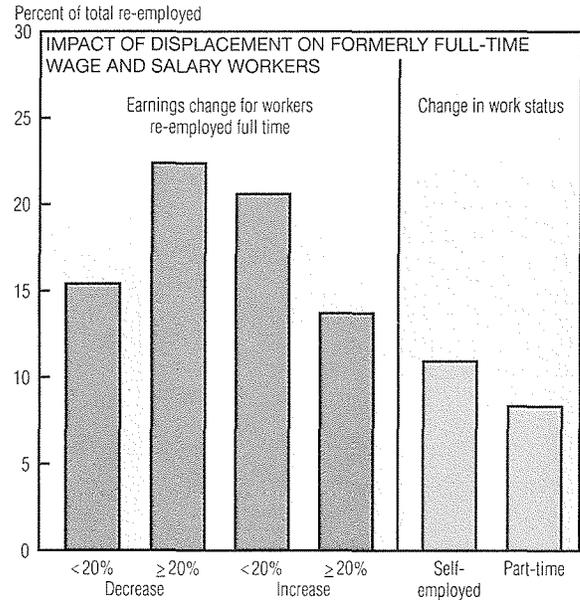
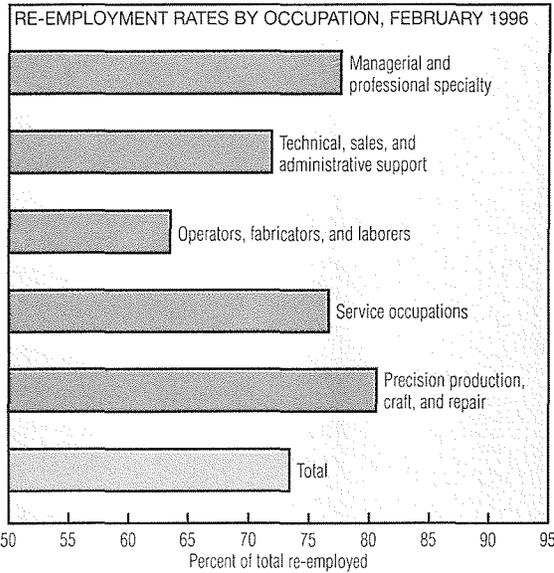
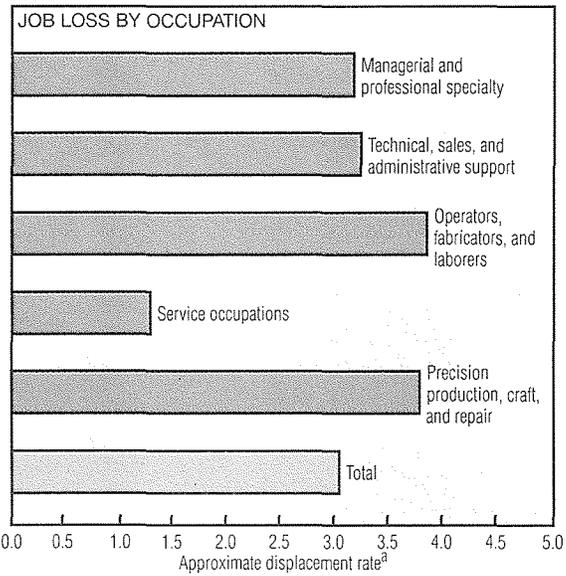
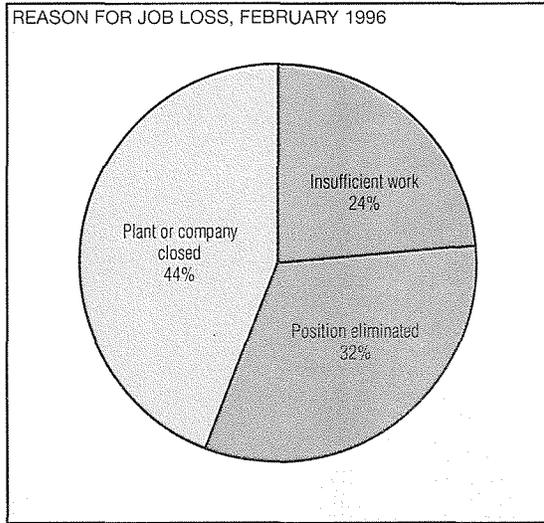
Employment growth was widespread, with most narrowly defined industries reporting increases. Strong gains in both manufacturing and local government employment were partly due to unaccustomed seasonal patterns: the return of manufacturing workers from unusually long vacation downtimes, along with earlier starting dates for schools. Neither of these factors can explain away August's strong employment

showing, but they may dampen jobs growth in the coming months.

Although the unemployment rate is one of the most carefully compiled labor statistics, it does not allow us to draw inferences about the effects of unemployment on workers' well-being. It turns out that many "unemployed" workers were not fired or laid off: 55% are new entrants, reentrants, and workers who voluntarily left their jobs.

(continued on next page)

Labor Markets (cont.)



a. Total workers displaced between January 1993 and December 1995 as a percentage of total workers employed in July 1994.
 NOTE: All data refer to workers with three or more years of tenure who were displaced between January 1993 and December 1995. Data are not seasonally adjusted.
 SOURCE: U.S. Department of Labor, Bureau of Labor Statistics.

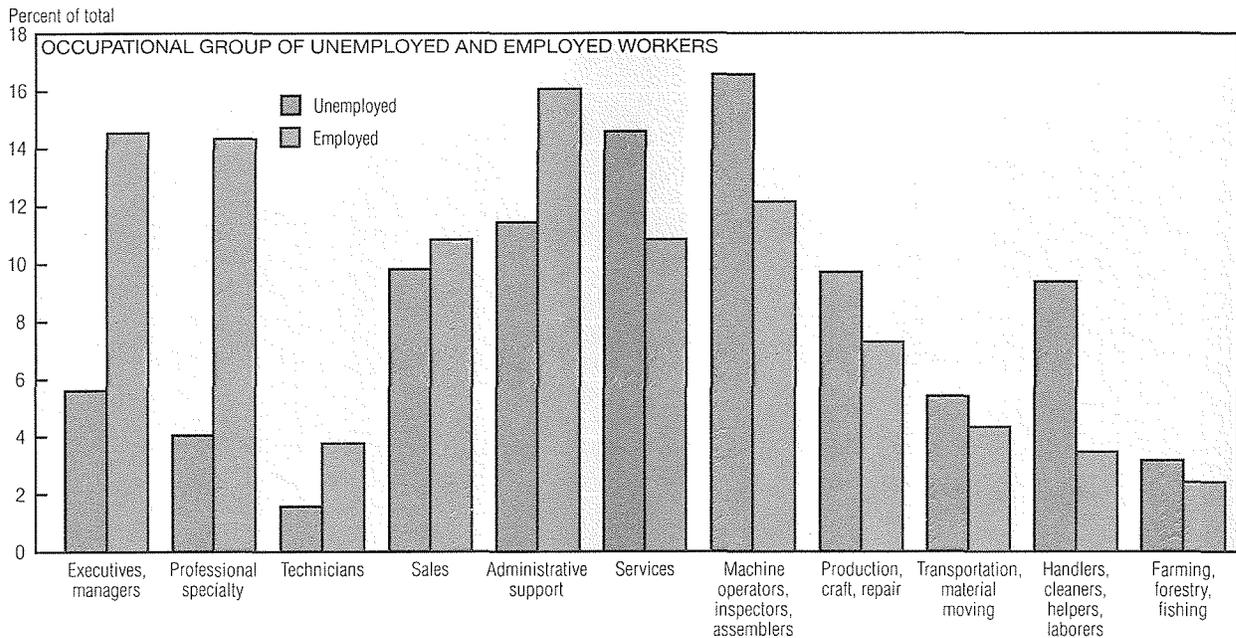
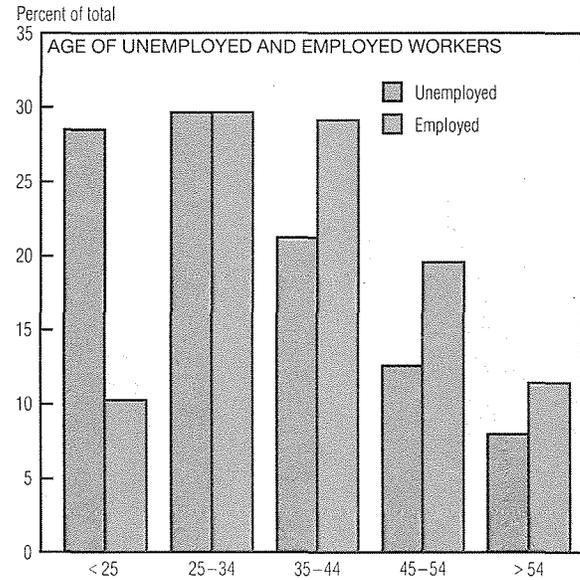
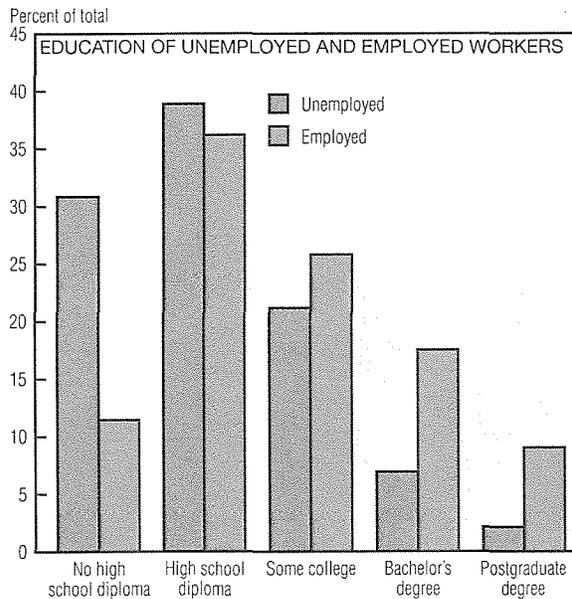
Laid-off workers are further studied in the BLS's Displaced Workers Survey, which asks about any job loss in the previous three years, focusing on the effects of joblessness and clarifying the unemployment patterns that have led to growing reports of job insecurity. About half of displaced workers were let go while their plant or site continued to function, indicating that targeted layoffs are an important source of displacement.

Over time, white-collar occupations have come to account for a significant chunk of layoffs. In the survey's early years (1979-93), recessions pushed the overall displacement rate up to 8.5%, but left managers and professional specialties relatively unscathed (4.4%), while blue-collar specialties' rates were well into double digits.

Re-employment rates are as important as displacement rates, and the

1996 survey shows a vital economy. It reports the highest re-employment rates since the survey began and should comfort laid-off workers, particularly those in the more skilled blue- and white-collar occupations. On average, re-employed workers continue to lose wages, but the latest data show that their chances of a wage increase nearly equal those of a wage reduction.

Skills and Unemployment



NOTE: Employed refers to full-time workers as defined by the Bureau of Labor Statistics.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Department of Commerce, Bureau of the Census; and the Federal Reserve Bank of Cleveland.

When thinking about labor market policies for reducing unemployment, it is important to consider what skills the pool of jobless people possess. More specifically, how do their skills compare with those of the employed?

March 1992 was a period of high unemployment, when roughly 9.7 million Americans were out of work and about 93 million had full-time jobs. The charts above use three broad measures to compare the

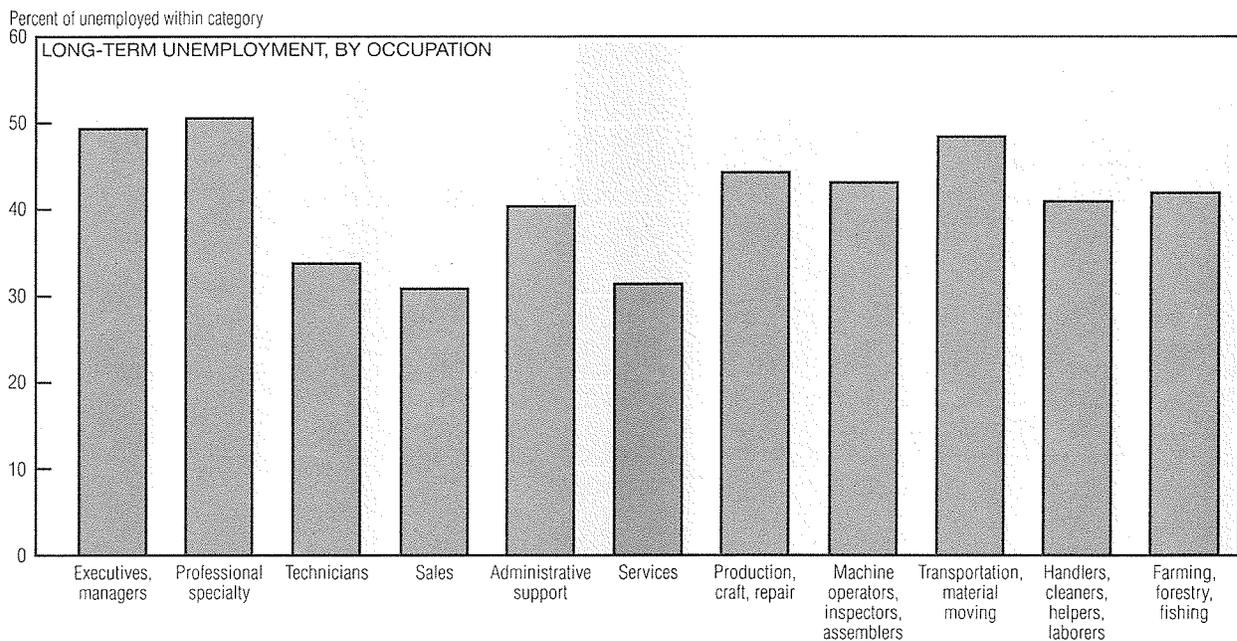
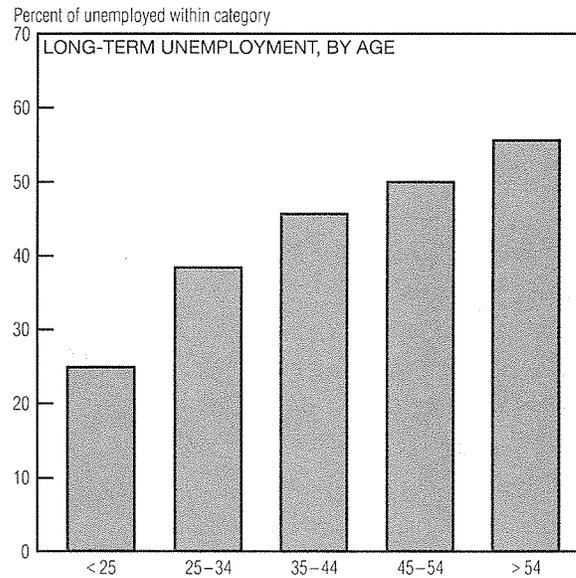
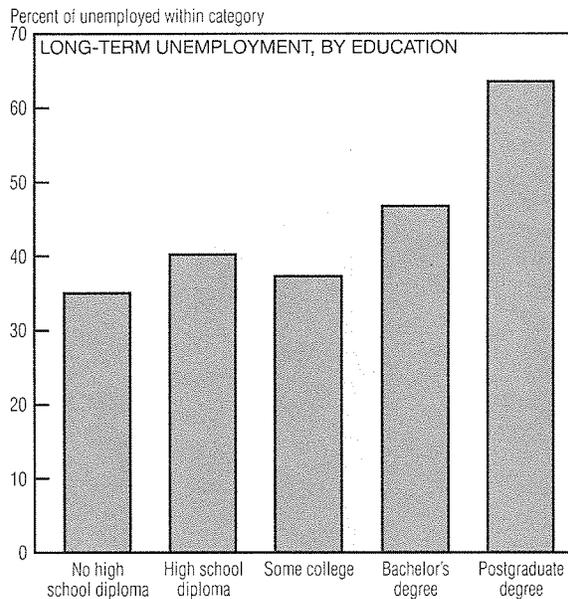
skills of people who were unemployed that month with the skills of full-time workers: education, age (which is strongly correlated with work experience), and occupation.

Although people without a high-school diploma made up only 11.5% of full-time workers, they accounted for over 30% of the unemployed. In contrast, college graduates formed 26.5% of the employed, but only 9% of the jobless.

Noticeable differences were also found in the ages of the two groups. Those younger than 25 made up about 10% of the employed, but 28.5% of the unemployed. In comparison, people in their prime working years (35 through 54) formed about 49% of the fully employed, but only around 34% of the unemployed. Not surprisingly, jobless people tended to be younger and less educated than those working full time.

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Skills and Unemployment (cont.)



NOTE: Long-term unemployment is defined as 13 weeks or more of continuous unemployment. All data are for March 1992.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Department of Commerce, Bureau of the Census; and the Federal Reserve Bank of Cleveland.

Looking at occupations, we find several that comprise a much larger share of the unemployed than of the employed. For example, handlers, equipment cleaners, helpers, and laborers accounted for only 3.5% of employed workers, but 9.4% of the unemployed. This is consistent with the relatively high jobless rates experienced by people in many low-skilled occupations. In contrast, executives, managers, and professionals accounted for 29% of full-time workers, but less than 10% of the unemployed.

Many observers consider unemployment to be especially problematic for those who go for long spells without a job, so it is interesting to see what share of the unemployed have been out of work for an extended period and how this percentage differs across groups with divergent skills.

Looking at education, we find that the fraction who had experienced long-term unemployment generally increased with the level of education. Similarly, older groups had a larger percentage of long-term un-

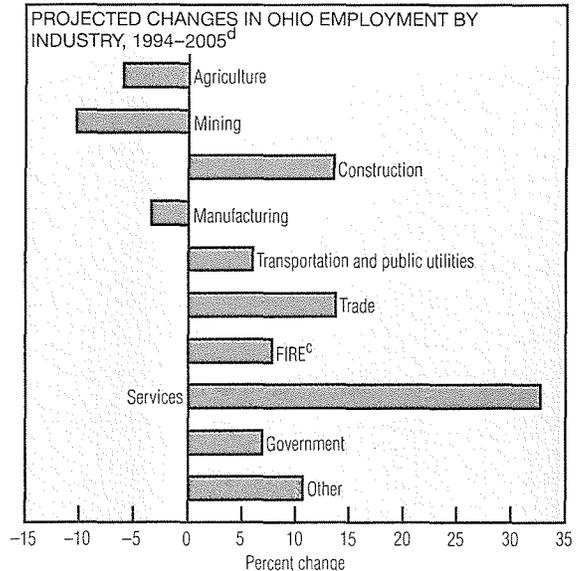
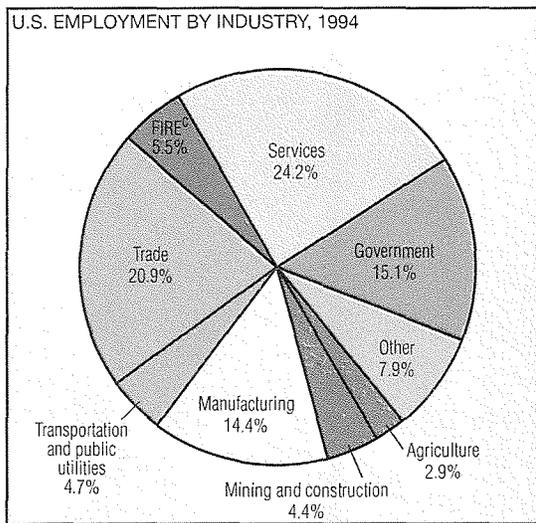
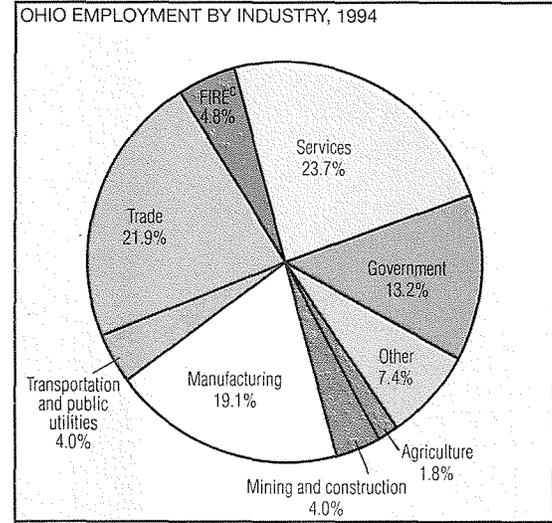
employed than did younger ones. Turning to occupations, we see that executives, managers, and professionals had relatively high rates of long-term unemployment compared to those in the service occupations and sales.

In sum, jobless people tended to be younger and have less schooling than full-time workers. However, the younger, less-educated unemployed also tended to be out of work for a shorter time than their older, more educated counterparts.

Regional Conditions

Metropolitan Area Employment Growth Estimates, 1993-2005^a

	Percent change
Cincinnati	19
Cleveland-Lorain-Elyria	9
Columbus	23
Mansfield	9
Pittsburgh	13
Steubenville-Weirton	4
Wheeling	5
Ohio ^b	13
U.S. average	19



a. Estimates for 2005 are from the Commerce Department's Survey of Current Business, June 1996.
 b. Data are for 1994-2005. Estimate for 2005 is from the Ohio Bureau of Employment Services.
 c. Finance, insurance, and real estate.
 d. Estimates are from the Ohio Bureau of Employment Services.
 SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; U.S. Department of Labor, Bureau of Labor Statistics; and Ohio Bureau of Employment Services, Labor Market Information Division.

Over time, an economy not only grows, but also experiences sectoral reallocations. These reallocations affect both employment in specific industries and the national and regional mix of occupations.

Commerce Department projections show that by the year 2005, the U.S. will have 19% more jobs than it did in 1993, which translates into an average annual growth rate of about 1.5%. In contrast, the anticipated increase for Ohio between 1994 and 2005 is only 13%, a growth

rate of 1.1% per year. Furthermore, of the 10 U.S. metropolitan areas expected to have the weakest employment growth, four are in Ohio. Only Cincinnati and Columbus are at or above the anticipated U.S. growth rate.

Although it is difficult to understand the causes of the difference between Ohio's and the nation's expected performance, some insight can be gained by examining which industries and occupations are changing, and what role these

changes will play in determining whether Ohio will look more or less like the U.S. in the year 2005.

Currently, industry employment patterns in Ohio are similar to those of the U.S. as a whole, with a few noteworthy differences. In 1994, the manufacturing sector accounted for 19.1% of Ohio's total employment, compared with 14.4% nationally. Service's share of employment, however, was only slightly lower in Ohio, 23.7% versus 24.2%. Furthermore,

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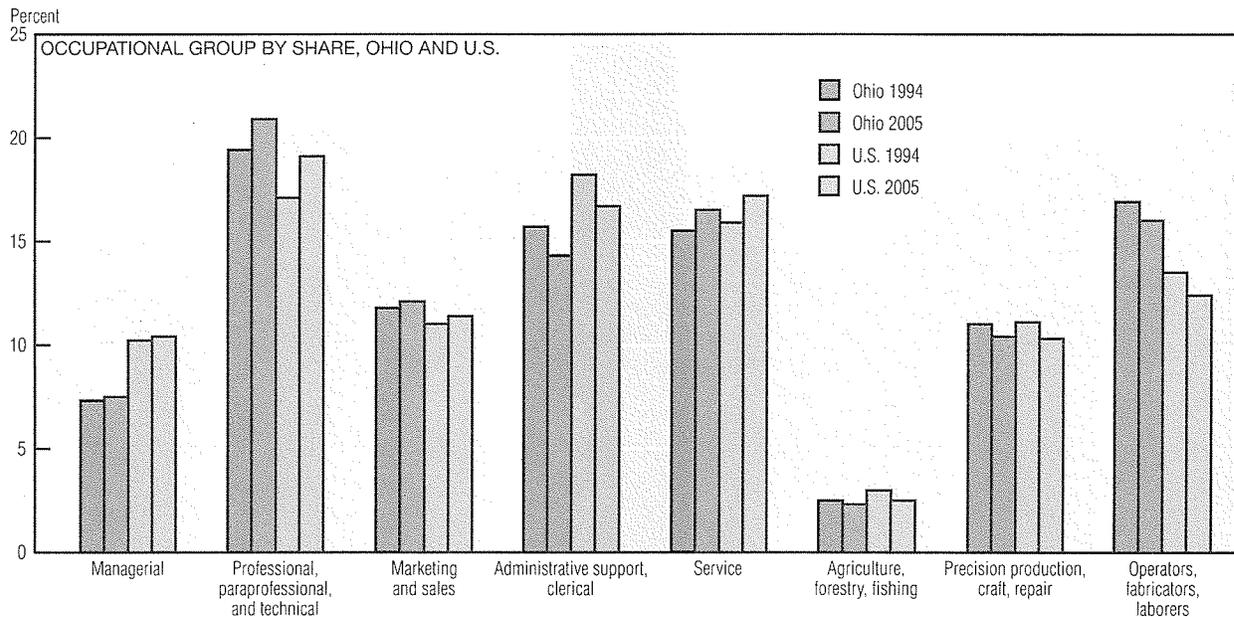
Regional Conditions (cont.)

Fastest-Growing Occupations in Ohio and U.S., 1994–2005

	Percent change	
	Ohio	U.S.
Systems analysts	91	92
Personal care aides	85	119
Computer engineers	84	90
Physical therapy assistants	76	83
Home health aides	74	102
Physical therapists	70	80
Occupational therapists	67	72
Residential counselors	62	77
Human services workers	58	75
Medical assistants	54	59

Occupations with Largest Projected Job Declines, 1994–2005

	Percent change
Central office operators	-70
Telephone installers/repairers	-70
Directory assistance operators	-70
Billing, posting, and calculating machine operators	-67
Central office/PBX installers and repairers	-39
Computer operators, except peripheral equipment	-38
Typists/word processors	-33
Lathe and turning machine tool setters and setup operators, metals and plastics	-31



only 1.8% of Ohio's workforce is employed in agriculture, while the national rate is about 2.9%.

Over the next decade, Ohio is expected to see employment declines in agriculture, mining, and manufacturing. The largest gain (32.7%) is expected in the service sector. No other expanding industry will grow nearly as fast.

The expected change in occupations tells a similar story—that the U.S. and Ohio share some similarities but also have some glaring differences. Some of the largest differences again reflect the importance of manufacturing in Ohio. More

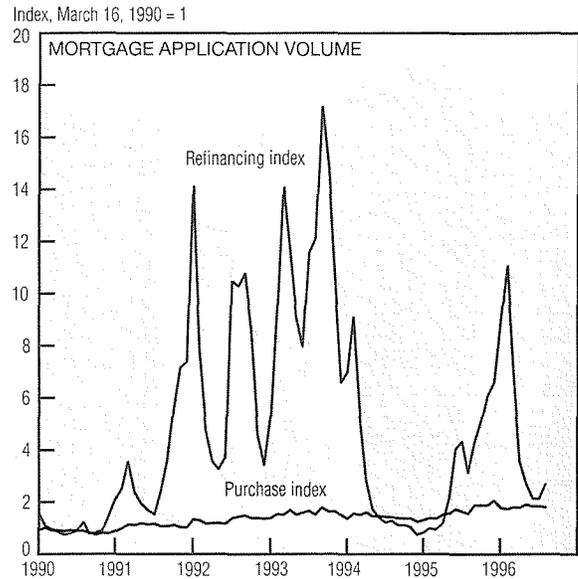
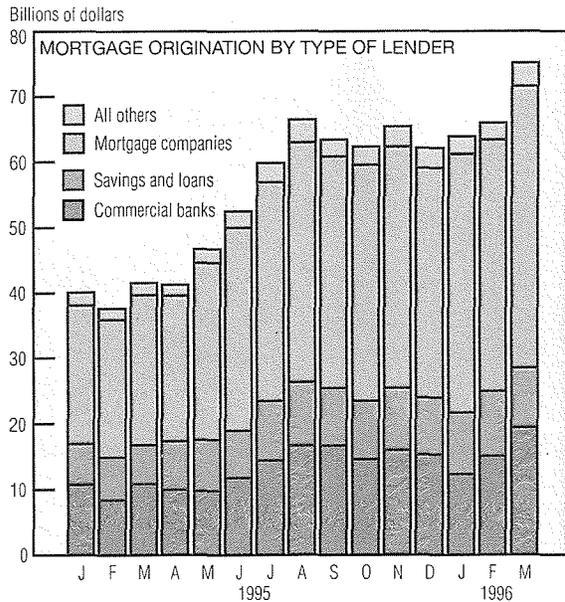
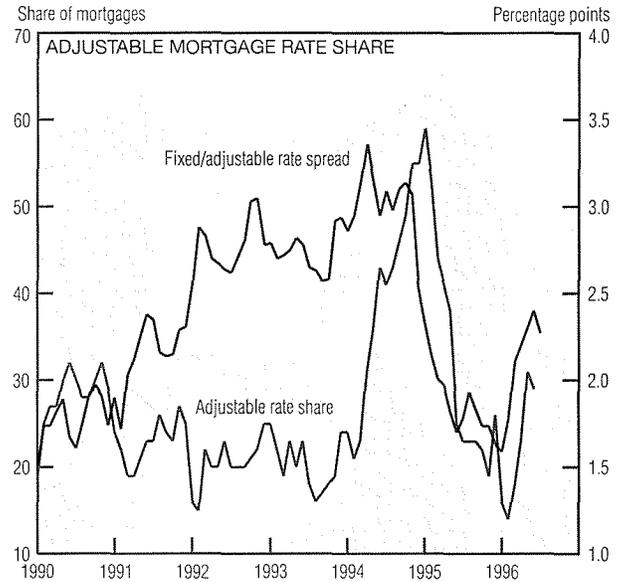
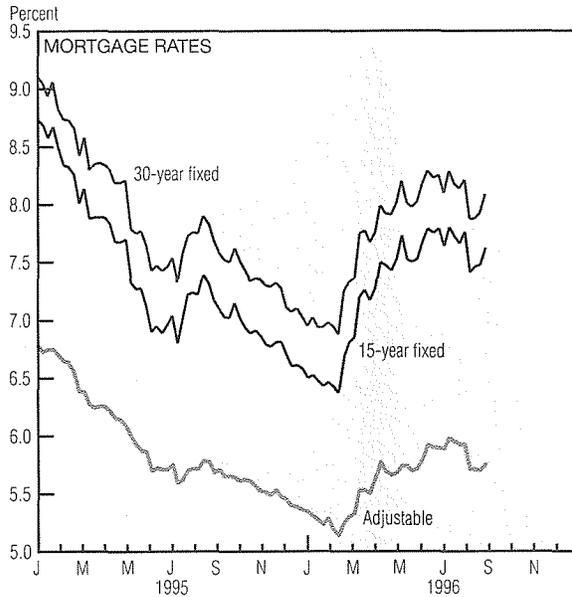
than 10% of U.S. employment is in the managerial professions, versus only about 7% in Ohio, with both expecting slight gains over the next decade. By contrast, about 17% of Ohio workers fall into the operators, fabricators, and laborers category, compared to less than 14% nationwide, with both expecting declines in the next 10 years.

In the U.S., the fastest-growing occupations are personal care aides and home health aides. Ohio's fastest-growing job category is systems analysts, followed closely by personal care aides and computer engineers.

On the national scene, analysts foresee drastic reductions in several areas. The largest expected declines—roughly 70%—will affect telephone operators and installers, and billing, posting, and calculating machine operators. Manufacturing machine operators will also face substantial cutbacks, as will typists and word processors.

Although it is probable that Ohio's share of manufacturing employment will still be above the U.S. average in 2005, the state is slowly reducing its reliance on this sector as jobs in the service industries and technical occupations expand.

Housing Finance



SOURCES: U.S. Department of Housing and Urban Development; Mortgage Bankers Association of America; and *Bank Rate Monitor*.

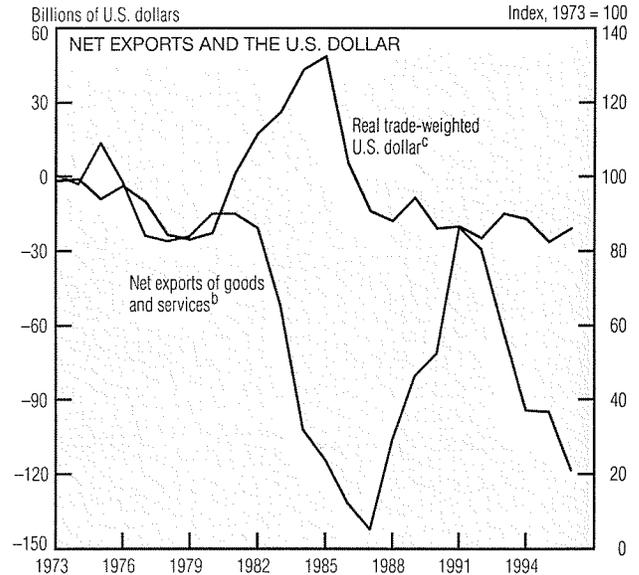
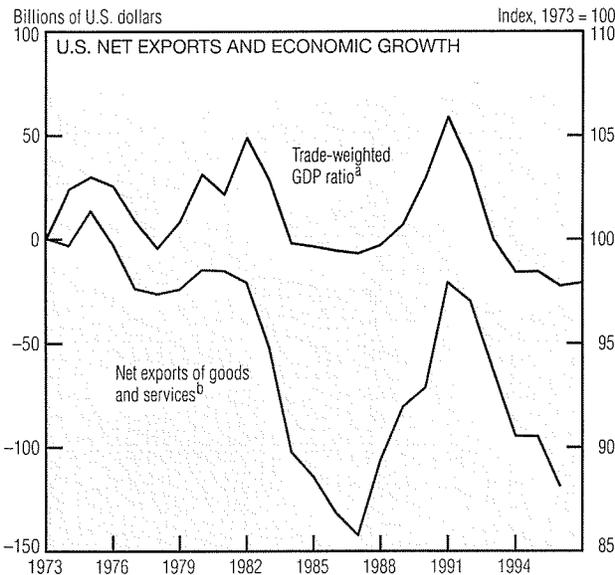
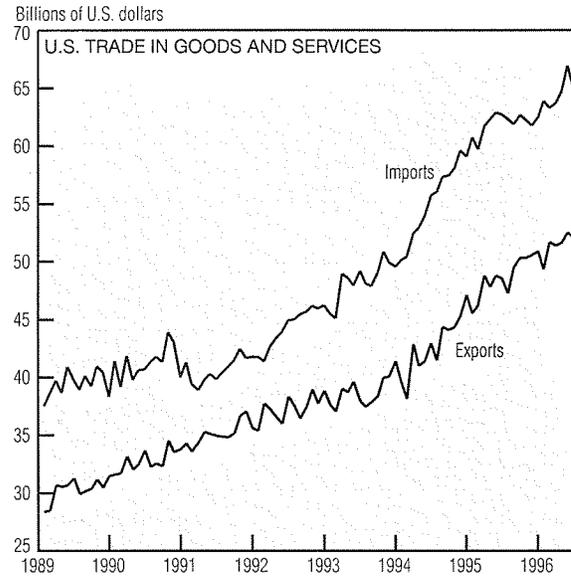
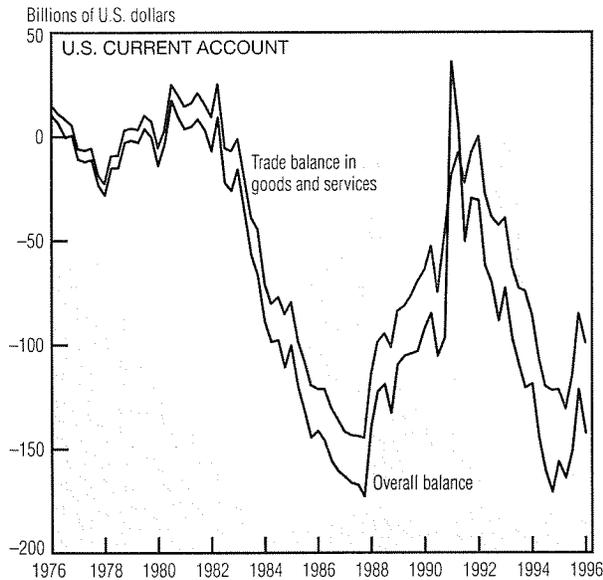
Although one might expect the general rise in long-term mortgage rates (up over 100 basis points since the beginning of the year) to have dampened the demand for new home loans, mortgage originations have exhibited steady, if unspectacular, growth over the last several months. By contrast, mortgage refinancing activity has responded dramatically to the rate increase, dropping 70% since the beginning of the year.

Much of this may be explained by the fact that adjustable mortgage rates have risen more slowly than fixed rates (adjustable rates now stand at less than 6%) and thus are still fairly attractive to new home buyers. Although mortgage rates are not expected to drop significantly over the next several months, there is a general feeling in the market that rates will be somewhat lower in 1997. This expectation may make the risk of adjustable-rate mortgages

seem more palatable and, if correct, could lead many recent borrowers to refinance and switch to fixed-rate mortgages next year.

Surprisingly, the increased attractiveness of adjustable-rate mortgages has had little effect on the composition of mortgage originations. Commercial banks have picked up only a slightly larger market share over the last few months, while savings and loans are holding steady.

International Trade



a. Ratio of foreign real GDP or GNP to U.S. real GDP. Foreign countries and trade weights are those used to construct the Board of Governors' trade-weighted dollar index. 1996 and 1997 projections are from *The Economist*, August 10-16, 1996.

b. 1996 plot is an average of the first two quarters of the year.

c. 1996 plot is an average of the first seven months of the year.

SOURCES: U.S. Department of Commerce, Bureau of Economic Analysis; Board of Governors of the Federal Reserve System; International Monetary Fund, *Financial Statistics*; and *The Economist*, August 10-16, 1996.

The U.S. current account deficit grew by \$20.6 billion (annual rate) in the first quarter, reaching \$142.4 billion. A wider trade deficit and larger unilateral transfers offset a slight decline in net U.S. interest payments to foreigners. Monthly data on trade in goods and services suggest that the trade deficit, the largest component of the current account balance, will widen further in the second quarter.

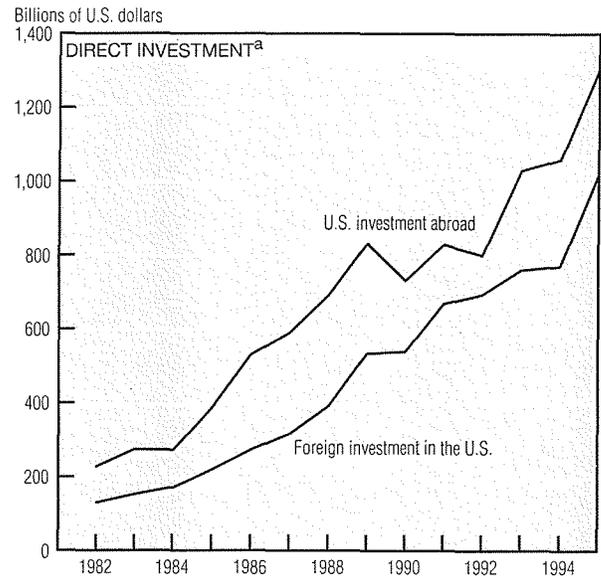
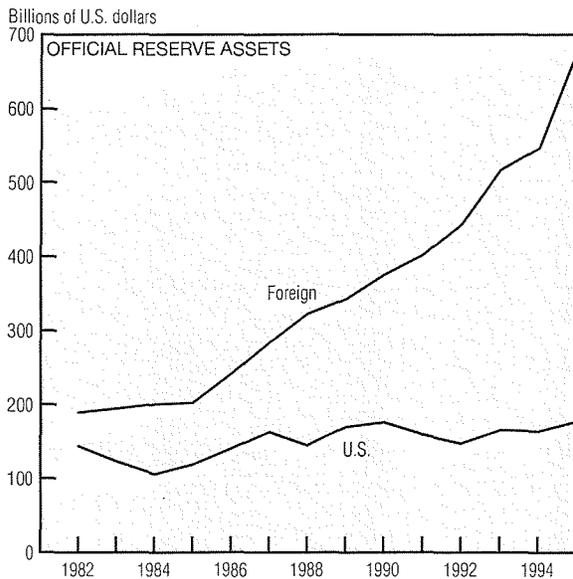
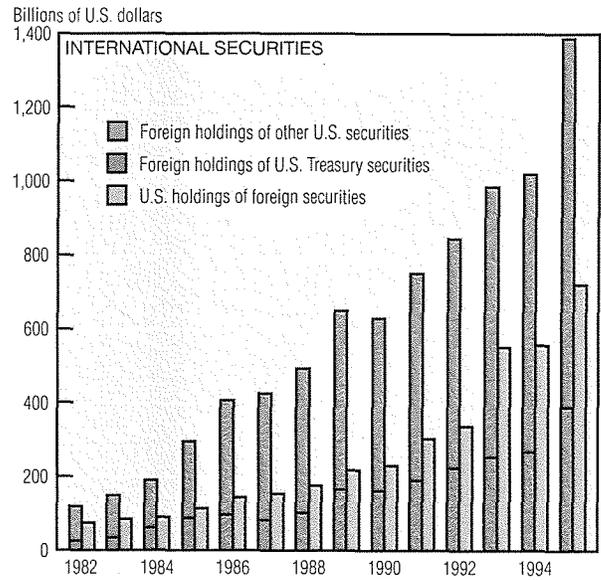
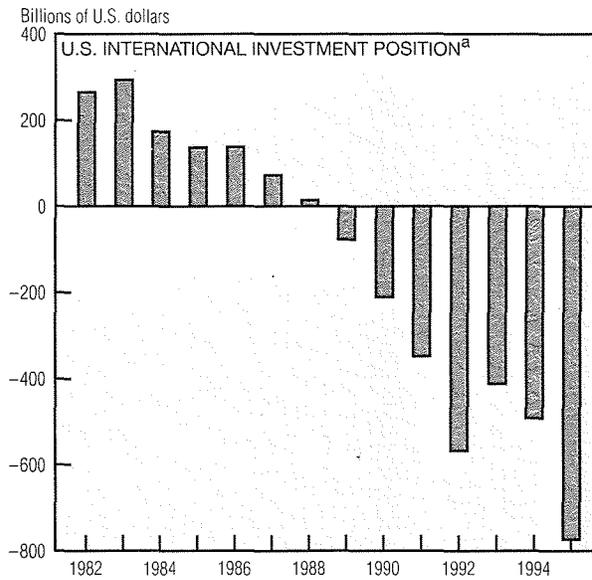
The deterioration in U.S. net ex-

ports since the 1991-92 recession can be traced to substantially higher economic growth here than abroad. Foreign economies have been picking up, however, and with trade-weighted growth projected at 1.7% this year and 2.5% in 1997, the prospects for a further sharp decline in U.S. net exports seem remote.

The connection between relative growth and the trade deficit is indirect and therefore somewhat tenuous. The relationship ultimately de-

pends on how growth influences decisions to save and invest. A deficit country, by definition, consumes and invests more than it produces and hence must borrow savings from abroad. The connection between movements in the real dollar exchange rate and net exports also runs through savings and investment decisions and seems even weaker than that between relative growth rates and net exports.

U.S. International Debt



a. Direct investment recorded at market value.
 SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis.

As a result of persistent current account deficits, the U.S. international investment position has shifted from a net credit of \$265 billion in 1982 to a net debt of \$775 billion in 1995. The biggest shift has taken place in portfolio investments. Since 1982, foreigners have acquired \$906 billion in private U.S. securities and \$360 billion in U.S. Treasury obligations. Over this same period, U.S. holdings of foreign securities have increased by about \$650 billion.

The U.S. owes a substantial portion of its international debt to foreign governments, which have added dollar assets to their foreign exchange reserves. These governments often buy dollars to forestall a dollar depreciation against their own currencies, then hold them to thwart any unwanted future appreciation. Official U.S. holdings of foreign currencies have not grown since 1982.

In contrast to our overall investment position, Americans' direct in-

vestments abroad continue to exceed foreigners' direct investments here. Direct foreign investments imply a controlling interest in the management of a foreign business.

Our international indebtedness represents a foreign claim on future U.S. output. This claim need not have implications for our future standard of living, provided that the underlying foreign capital inflows enhance our productive capacity.