

### First Quarter 2017 Report

The Bureau of Economic Analysis (BEA) Advance Estimate recently reported that **national GDP growth slowed to 0.7% in the first quarter of 2017, the weakest pace in three years.**<sup>1</sup> While most analysts expected the figure to be revised upward, the Commerce Department's just-released Second Estimate was only modestly higher, measuring first quarter growth at a still-disappointing 1.2%.<sup>2</sup>

It's worth noting that downbeat first quarter GDP reports have become the norm throughout the recovery. From 2011 to present, growth has only averaged 0.97% in the first quarter compared with 2.27% in the second, 2.48% in the third, and 2.33% in the fourth.<sup>3</sup> Despite tweaking its measurements in recent years to account for "residual seasonality," many economists believe that the Commerce Department still tends to understate growth in the first quarter, only to overstate it later in the year.<sup>4</sup>

Regardless of its methodology, the first quarter GDP data was undeniably rife with mixed economic indicators, once again sparking debate over the economy's stamina.

**On the bright side, there were roughly 527,000 new jobs added in the U.S. during the first three months and wages continued to rise, albeit moderately.**<sup>5</sup> Likewise, both new residential and overall construction increased in the first quarter.<sup>6</sup> **On the downside, however, the nation's auto sales have now posted year-over-year declines from last year's figures for four consecutive months.**<sup>7</sup> And, despite relatively high consumer confidence, consumer spending nearly stalled in the first quarter.<sup>8</sup>

The Federal Reserve Board at its May Open Market Committee meeting acknowledged the lackluster GDP data but noted that the slowdown was "likely to be transitory," meaning that it expects a second quarter rebound. **While the Fed left its benchmark rate unchanged, most analysts still anticipate another rate hike in June (which would be the third since December 2016).** Meeting minutes and the committee's subsequent statement stated "The labor market has continued to strengthen even as growth in economic activity slowed," and that "Household spending rose only modestly, but the fundamentals underpinning the continued growth of consumption remained solid."<sup>9</sup> As one analyst paraphrased, "The economy's engine was still looking good, even if the car was moving a little slowly."<sup>10</sup>

At the local level, our economic indicator data was also considerably mixed in first quarter 2017. Most notably, **Lucas County auto sales were lower than last year's record markers, and appear to be poised for a good, but not great year.** In another unwelcome development, **both Toledo and Lucas County saw their unemployment rates rise significantly during the first quarter, although recent**

### What is the Wade Wire?

As a public information service, *The Wade Wire* is a regularly published/released quarterly report in which we identify, measure, and analyze key local economic indicators within Lucas County.

Rather than formulating a complex Index of Leading Economic Indicators aimed at predicting trends yet to occur, we want to determine how well our local economy is *currently* performing (compared to the prior year) based on three essential questions:

1. Are people working?
2. Are people spending?
3. Are people building?

The data sources we use generally fall under the category of "concurrent" economic indicators (reflective of present conditions). However, some of them have had historically leading or predictive qualities. Thus, each report will also include a quarterly assessment, aimed at summarizing significant developments within and among our indicators and evaluating their potential impact on our county's economy.

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wage growth would suggest that the labor market is still likely tightening, despite the recent slowdown in job growth.

Similarly, local construction sector data posted mixed results, with permit activity gains in the New Residential and Residential Additions/Alterations categories, but a slight decline in the New Commercial segment and sizable dip in Commercial Additions/Alterations. As I've mentioned in previous reports, building permit activity is among the most vital of our local economic indicators due to the "multiplier effect" that home building and the construction industry has in spurring growth in numerous other economic sectors (manufacturing, transportation, retail, etc.).

In all, the first quarter 2017 national economic indicators were all too typical of many previous reporting periods. Once again, the job market seems to be at its healthiest point in nearly two decades, yet economic growth remains stubbornly sluggish. For now, however, let's take a look at our Key Local Economic Indicators.



## Are People Working?

Starting the year on a mostly positive note, the U.S. Department of Labor announced revised first quarter job gains of 216,000 jobs in January, 232,000 in February, but only 79,000 in March.<sup>11</sup> Although it is worth noting that job gains rebounded in April (211,000), the first quarter 2017 totals (527,000) were still markedly lower than those posted during the same period last year (609,000). Also, in a potentially troubling development, our local job market data showed both Toledo and Lucas County posting higher year-over-year jobless rates in January and February, but finishing March roughly unchanged from last year.

Looking at our fifteen month rolling track of non-seasonally adjusted local unemployment data, the area's jobless rates were uncharacteristically disappointing in first quarter 2017.

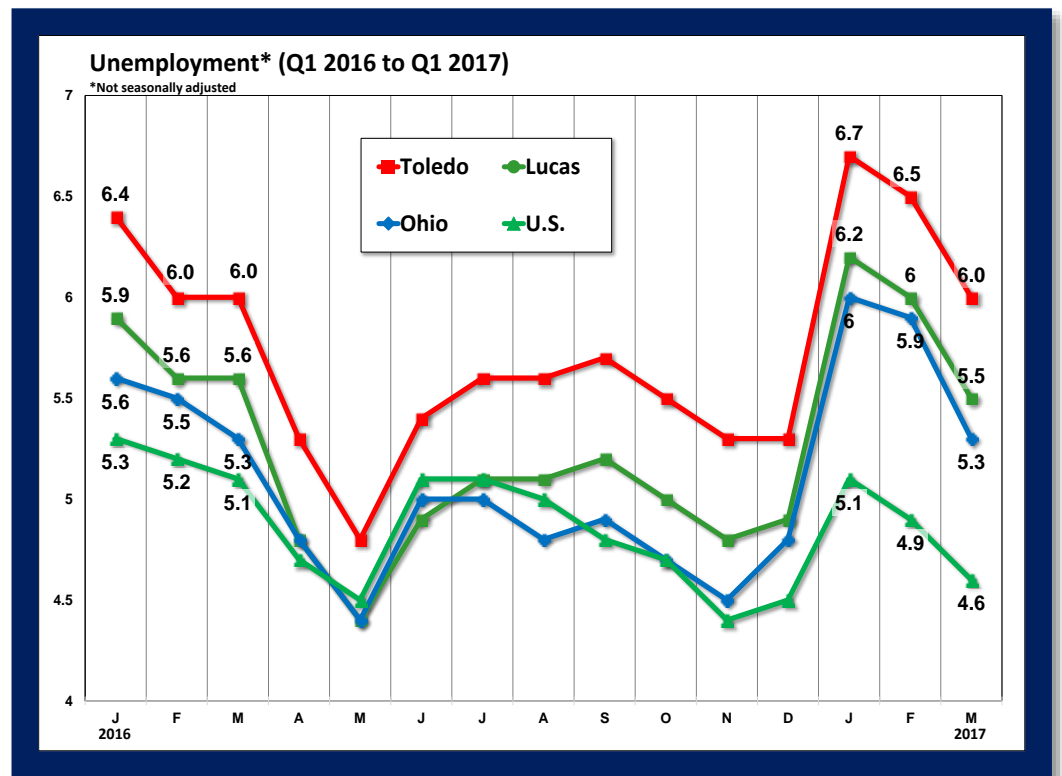
As Table 1 shows, Lucas County's January 2016 jobless rate rose to 6.2%, up from the 5.9% of the prior year. The February rate of 6.0% was an even greater increase from the 5.6% posted a year earlier.

**However, Lucas County ended the quarter in March with a jobless rate of 5.5%, a slim 0.1% lower than the previous year (5.6%).**

The City of Toledo also saw its unemployment rate rise in the first quarter. Its January 2017 rate increased to 6.7% from 6.4%. In February, it rose more sharply, this time to 6.5%

Table 1

(Source: Ohio Dept. of Job and Family Services)<sup>12</sup>



from 6.0% in 2016. **Toledo finished the quarter by posting a March jobless rate of 6.0%, exactly matching the previous year's mark.**

*Table 1* also illustrates an interesting and potentially troubling trend. There is little doubt that our area and the industrial Midwest struggled with the decline of manufacturing in recent decades, and that the region was among the hardest hit during the Great Recession. Likewise, the jobless rates of both Toledo and Lucas County remained somewhat higher than those of the state and nation throughout much of the recovery. However, from April 2014 through July of 2016, the monthly unemployment rates for both Lucas County and Ohio were usually equal to or below those of the nation, with Toledo's only lagging by roughly one half of one percent.<sup>13</sup> **But the region's job market data has lost ground versus the national data since last summer, and the gap seems to be widening.**

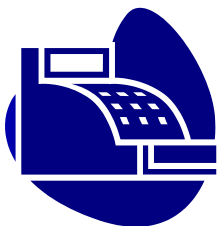
*As I've detailed in previous reports, fluctuations in unemployment rates can mean many things. Ticks downward can be skewed by demographic trends (i.e., baby boomers retiring) or discouraged job-seekers giving up their search for work, while upward movement can often be an encouraging sign that the long-term unemployed are rejoining the labor market. With that in mind, let's look closer at the year-over-year Civilian Labor Force (CLF, those actively seeking work) and employment statistics from February 2017, when the year-over-year unemployment rate rose sharply in both Toledo and Lucas County.*

The city's non-seasonally adjusted data showed that **there were 900 more Toledoans working in February 2017 (122,000) than in February 2016 (121,100).**<sup>14</sup> But unlike some previous quarters, in which a dramatic improvement in the unemployment rate could be attributed to a drop in the CLF, the opposite seems to have occurred – *the number of people seeking work grew substantially in February* (130,500 in 2017, compared to 128,900 the year before).<sup>15</sup> That same month **there were 1,400 more Lucas County residents working (199,600) than there were a year earlier (198,200)**, while the number of county job-seekers had also grown substantially (212,400 in 2017, compared to 209,900 in 2016).<sup>16</sup>

A closer look at the statistics shows that Toledo's March 2017 CLF grew by 1.24% from the prior year, while its employment level increased by only 0.74%. At the same time, Lucas County's CLF went up by 1.19%, while its employment level only grew by 0.71%. While increases in both the CLF and number of people working are positive trends, ***the increase in local jobless rates was driven by a growth in the CLF, rather than people losing jobs, but it is also apparent that job growth is failing to keep pace with the number of people seeking work.***

**Turning to wages, our local payroll withholding survey data showed a sturdy year-over-year first quarter gain of 4.07%.**<sup>17</sup> Taken together, the employment and payroll data suggest that our local job market is tightening, with job growth slowing somewhat, but with wages still moving upward in 2017.

The employment-cost index, a broad measure of U.S. workers' wages and benefits, rose by a seasonally adjusted 0.8% in the first quarter.<sup>18</sup> **And in the twelve months ending in March, the index showed total wages were ahead by 2.6%, keeping paycheck growth well ahead of inflation.**<sup>19</sup>



## Are People Spending?

As I mention in every report, it's the flow of currency (from employer to employee, from consumer to merchant/vendor) that is the lifeblood of a thriving local economy. For the purpose of this report, I focus on two key concurrent indicators of consumer spending – the sales tax generated by purchases made in Lucas County and the motor vehicle sales sector of our local economy.

Like the national data, local consumer spending was nearly flat in first quarter 2017, as **taxes collected on sales in Lucas County by 0.66% from a year ago (a gain of \$185,559.18).**<sup>20</sup> Meanwhile, there are few better indicators of consumer confidence than the purchase of durable goods, and it's hard to find an example more fitting and relevant to our region than auto sales.

As *Table 2* indicates, **Lucas County auto dealers saw first quarter new car sales drop by 6.25% from last year's record figures.** Area dealers also saw used car sales dip by 0.98% during the same period.

*End of the streak?: The first quarter of 2017 marks only the third time that local sales data failed to top the prior year's figures in the nearly eight years since the end of the Great Recession. However, it was the second down quarter in less than a year.*

Slumping auto sales were a major contributor to the dismal first quarter GDP data, as **the nation's dealers posted a first quarter decline of 1.5% from last year's markers.**<sup>22</sup>

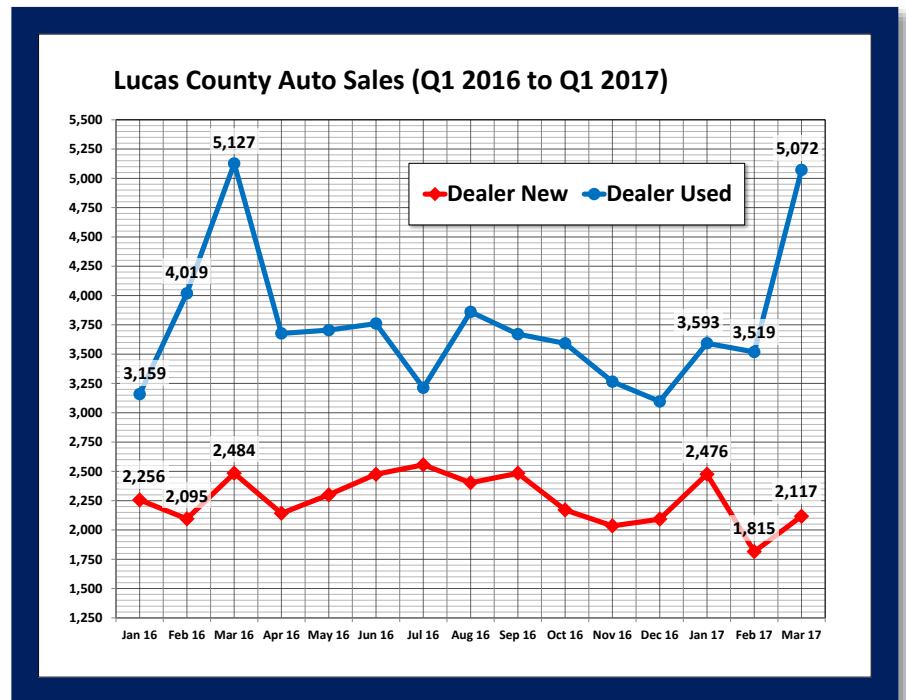
With April sales plunging another 4.7%, U.S. vehicle sales have now fallen for four consecutive months.<sup>23</sup> As I suggested several times last year, it appears that the nation's new vehicle sales likely reached a plateau in 2016.

Using March 2017 sales as an example, it appears that the biggest problem continues to be sagging sedan sales. For example, **GM saw a March year-over-year sales increase of 1.5%**, driven by a 12% increase in GMC truck and SUV sales, while the company's gains were tempered by a precipitous drop in its Impala (-23%) and Malibu (-36%) sales.<sup>24</sup> **Ford Motor Company sold 234,895 vehicles, a drop of 7.2% from March 2016.**<sup>25</sup> But the company's F-Series pickup sales were up 10% from last year, while its car sales plummeted by 24.2%.<sup>26</sup> **Likewise, Fiat Chrysler reported a 4.6% drop in March.**<sup>27</sup> FCA's data showed that the Dodge brand rose 9.7%, including a 6% increase for Ram trucks.<sup>28</sup> But not all trucks and SUVs advanced, as Jeep sales fell by 11%.<sup>29</sup> Last, Chrysler sales dropped by 33.1%.<sup>30</sup>

We are likely witnessing the end of the auto sector's seven-year winning streak, which began in 2010 as the U.S. was recovering from the Great Recession. Low fuel prices, favorable credit conditions and a strengthening economy helped drive the record run – which, in turn, helped fuel much of the recovery.

Table 2

(Source: Lucas County Clerk of Courts)<sup>21</sup>



## Are People Building?

Building permit activity has always been considered the gold standard of economic indicators. Because the industry relies on a combination of confidence and optimism, access to credit, and several time-intensive stages of planning and development, economists have long relied on building permit activity as a tried and true “leading” or predictive indicator for an economy's future direction. In addition, it bears repeating that the construction industry is also well known for its “multiplier effect,” generating spin-off manufacturing, retail, and transportation jobs and profit.



As Table 3 shows, **new residential construction activity increased in first quarter 2017**. Permits were drawn for a combined estimated value of \$29,564,043. **The gain (\$2,013,963) marked a 7.31% improvement over 2016 figures.**

**Residential additions and alterations activity also grew in the first quarter.** Permits were drawn for a combined estimated value of \$7,131,031. **The increase (\$220,817) was 3.20% better than the 2016 totals.**

**New commercial construction activity, though strong, dipped during first quarter 2017.** Permits were drawn for a combined estimated value of \$123,983,644. **The decline (-\$8,272,156) marked a 6.25% drop from 2016 numbers.**

Last, **commercial adds/alterations activity dropped significantly in first quarter 2017.** Permits were drawn for a combined estimated value of \$25,338,787. **The downturn (-\$16,541,011) was a 39.37% decrease from the 2016 markers.**

While our local construction sector numbers were mixed, the national data saw year-over-year gains in every category.

**Total housing starts in March grew to an annual rate of 1.22 million, an increase of 9.2% from 2016.**<sup>32</sup> The country's total construction spending (including nonresidential projects) in March posted a year-over-year gain of 3.6%, pushing first quarter 2017 figures to a 4.9% increase over the previous year.<sup>33</sup> Continuing to benefit from the improving economy, **March 2016 sales of newly built single-family homes rose to an annual rate of 621,000 units, an increase of 15.6% from the March 2016 estimate of 537,000.**<sup>34</sup>

Locally, **The Toledo Board of Realtors reported that total home sales were up 7.8% compared to the first quarter of 2016.**<sup>35</sup> The average sale price rose to \$125,024 (an increase of 10.4%).<sup>36</sup> New listings dropped by 16.1%, and the average days on the market shortened by 6.2%.<sup>37</sup>

As I mentioned in the introduction, the country's economy had clearly lost steam in first quarter 2017. For the most part, however, the underlying dynamics appear strong enough to fuel a historically typical second quarter rebound, followed by more moderate growth for the remainder of 2017. Yet there are some potential trouble spots looming as we move further into the year. With that in mind, let's turn to my assessment of first quarter 2017.

Table 3 Q1/17 Permits (vs. Q1/16)<sup>31</sup>

Residential New	
Permits: 168	Est: \$29,564,043
34 (25.37%)	\$2,013,963 (7.31%)
Residential Add/Alt	
Permits: 368	Est: \$7,131,031
-195 (-34.64%)	\$220,817 (3.20%)
Commercial New	
Permits: 398	Est: \$123,983,644
355 (825.58%)	-\$8,272,156 (-6.25%)
Commercial Add/Alt	
Permits: 289	Est: \$25,338,787
74 (34.42%)	-\$16,451,011 (-39.37%)



## Summary: An Assessment of First Quarter 2017

As I mentioned earlier, the year began on a slightly gloomy note, with our key local economic indicators showing mostly mixed data in the first quarter of 2017. **Local unemployment rates rose in the first two months, only to reach par with last year's rates in the third.** Yet more people were working than in the previous year, and wages continued to edge upward. **However, consumers bought fewer cars, and area builders posted gains in the two residential categories but saw declines in the two commercial segments.**

Likewise, the national data was also decidedly mixed. **The nation's employers continued to add more jobs, though at a slower pace than in recent years, and wages continued to make moderate gains.** In another positive development, the nation's builders picked up the pace of both new residential and overall construction. **On the other hand, consumer spending was flat, and the nation's auto sector has seen year-over-year sales figures drop for four consecutive months.**

Despite the Commerce Department's disappointing first two reads of the nation's GDP, there is a general sense that the overall trajectory of job and wage growth will bring a reasonable rebound in the second quarter data, with moderate growth (~ 2%) to follow for the foreseeable future. That said, **I am concerned about two looming trouble spots – declining productivity and weakening auto sales.**

Essentially a measure of how much product comes from labor and investment, it's fair to say that productivity has remained weak throughout most of the recovery. Most recently, **U.S. productivity fell by 0.4% in first quarter 2017, bringing the twelve-month average to a sluggish 1.1%.**<sup>38</sup> Historically, productivity increases usually stem from advances in technology and/or through job growth. As I have mentioned in previous reports, much of the decline in manufacturing jobs during the last two decades was due more to automation rather than lopsided trade deals. In addition, **the dual factors of an aging population and a labor market nearing full employment will likely hamper future output growth.**

**At minimum, these factors will make it much more difficult to achieve the 3% growth rate upon which the White House is basing so many of its tax and budgetary assumptions.**

**While all national economic indicators are important to our area, there are likely none more critical to our region than the auto manufacturing sector.** Without question, the decline in sedan sales in favor of trucks and SUVs is leading to major changes in production and inventory strategies. In this context, our local manufacturers may be better positioned than others to weather the storm. But **Detroit's Big Three has already begun instituting production cuts and temporary plant closures, mostly at those plants producing sedans, coupes, and other slow-selling passenger car models.**<sup>39</sup>

**As I have mentioned in previous reports, auto dealers have relied on increasingly generous incentives and low interest/long duration financing in order to lift sales to recent record totals.** Industry analysts report that such incentives now average \$3,900 per vehicle, or roughly 10% of the typical sticker price.<sup>40</sup> And a full one-third of first quarter retail sales were backed by loans of at least 72 months.<sup>41</sup> **Worse, the increasing reliance on sub-prime auto loans has resulted in the highest levels of delinquencies since 2008, just before the Great Recession and the auto sector's near-collapse.**<sup>42</sup>

All told, I remain cautiously optimistic the economy will rebound in the second quarter, and then return to a typical post-recession growth rate of around 2%, but we're not out of the woods yet, and there are more than a few things to worry about as we move further into 2017.

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