Cautious Optimism: Massachusetts Economic Recovery and Expansion

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MODERATE ECONOMIC EXPANSION IN MASSACHUSETTS REFLECTS A STRONGER HOUSING MARKET, RENEWED CONSUMER SPENDING, AND THE FASTEST POPULATION GROWTH IN THE NORTHEAST. THE STATE ADDED OVER 50,000 JOBS LAST YEAR, BUT THE UNEMPLOYMENT RATE REMAINS STUBBORNLY HIGH, ESPECIALLY IN AREAS OUTSIDE OF GREATER BOSTON.

INTRODUCTION

The Massachusetts economy overcame a sluggish first half of 2013, finishing the year with more steady and moderate economic expansion and job growth. The state’s housing market has strengthened, especially in the Greater Boston area, giving homeowners more confidence in the value of their generally largest asset and bolstering the construction industry. Consumer spending is up as confidence in the private sector-led economic recovery continues. The long arc of population change in the state has transitioned from stagnation to modest growth as Massachusetts now has the fastest growing population in the Northeast and has roughly equaled U.S. population growth in recent years.

While the Commonwealth and broader U.S. economies continue to strengthen, strong headwinds have been impeding growth. The major forces holding back more robust economic growth include: 1) policy-induced austerity at the federal government level, including sequestration spending cuts and the October 2013 government shutdown (the sequestration cuts for this year and next have been modified and reduced in a recent congressional budget deal, somewhat lessening this impact and 2) continuing sluggishness from many of the state’s major international trading partners, particularly Europe, though recent data suggest an uptick in exports from the state. These negative forces seem to be holding back, or even stalling, improvement in the labor market. While the state added over 50,000 jobs in 2013, the unemployment rate, which had been falling since its peak during the recession, increased noticeably.
during the middle of 2013. The state’s rate has tracked the pattern of the national rate, falling below the national rate for the first time since November of 2013. The state’s rate now stands at 6.5% compared to the national rate of 6.7%. As the national fiscal policy continues to provide uncertainty with little progress towards a “grand bargain” (despite the December budget agreement, which did not address long-term sequestration spending cuts), the growth of the Commonwealth’s economy continues to hinge on the strength of the state’s innovative private sector with overall growth dragged down by the broader forces.

**Output, Employment, and Unemployment**

As measured by the MassBenchmarks Current Economic Index, a proxy for gross state product (GSP), the state has bounced back from a weak fourth quarter in 2012. Throughout 2013, GSP exhibited modest to healthy growth. In three of the four quarters last year, the state outperformed the nation in overall growth. Growing state product has not necessarily been passed through to employment growth in the state. Having added over 50,000 jobs over the past year, total state employment now exceeds its pre-recession level, though it still lags behind its peak a decade ago. The unemployment rate exhibits a more discouraging pattern. Having fallen steadily since November of 2009, the jobless rate climbed, albeit slowly, from 6.4 percent in April 2013 to 7.2 percent in July, remaining at that level through October before a modest reduction to finish the year at a seasonally adjusted rate of 7.1 percent. Over this same time period, the U.S. rate fell from 7.5 percent in May to 6.7 percent in December of 2013. And, as has been documented in previous issues of this journal, the jobless rate does not reflect the serious issues of underemployment and the discouraged worker effect. Complicating this picture is the fact that the unemployment rate data and the employment data are generated by two different independent surveys, and do not always paint a consistent picture of the state labor market. (See sidebar on next page for further discussion.)

Embedded with the state unemployment rate is considerable variation at the sub-state level. The New

**Figure 1. Growth in Real Product, Massachusetts and U.S.**

![Figure 1. Growth in Real Product, Massachusetts and U.S.](image)

Source: U.S. Bureau of Economic Analysis, Real GDP (U.S.); MassBenchmarks Index (MA)

**Figure 2. Unemployment Rates, Massachusetts and U.S., 2007 to 2013**

(Seasonally adjusted)

![Figure 2. Unemployment Rates, Massachusetts and U.S., 2007 to 2013](image)

Employment and Unemployment Surveys: Where the Numbers Come From

National labor market data in the United States are tracked monthly using two different types of surveys. The first of these, the monthly Current Population Survey (CPS), is a survey of approximately 60,000 households conducted by the U.S. Bureau of the Census for the U.S. Department of Labor’s Bureau of Labor Statistics (BLS). The CPS collects monthly labor force data from all household members 16 and older. The findings of the CPS are used to produce monthly estimates of the numbers of working-age individuals who are employed and unemployed and the nation’s unemployment rate, which typically receives the most attention.

The second survey is the monthly survey of the number of workers on the payrolls of nonfarm private firms and government agencies. Also known as “the establishment or payroll survey,” it is based on a national sample of approximately 145,000 business establishments and government agencies. The statistical survey governing this data collection effort by the BLS is formally known as the Current Employment Statistics (CES) program. A complementary effort at the state level allows for monthly wage and salary employment estimates for states and large-to-medium-sized metropolitan areas.

Every month, the “jobs report” utilizes data from both surveys. The change in employment is devised from the CES survey, and the unemployment rate is derived from the CPS survey. This can and does lead to inconsistencies between the reported data on job growth and trends in the unemployment rate. Here is a summary of the differences between these two surveys:


<table>
<thead>
<tr>
<th>CES SURVEY</th>
<th>CPS SURVEY</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Monthly sample survey of 145,000 U.S. businesses and government agencies.</td>
<td>• Monthly sample survey of approximately 60,000 U.S. households.</td>
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<tr>
<td>Firms of all sizes are included.</td>
<td></td>
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<tr>
<td>• Measures employment, hours, and earnings with significant industrial and geographic detail.</td>
<td>• Measures employment and unemployment with significant demographic detail.</td>
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<tr>
<td>• Reference period is the pay period (could be weekly, biweekly, monthly, and so forth) that includes the 12th of the month.</td>
<td>• Reference period is the week that includes the 12th of the month.</td>
</tr>
<tr>
<td>• Employees of all ages are included.</td>
<td>• Only workers aged 16 and older are included.</td>
</tr>
<tr>
<td>• Employment measure reflects the number of nonfarm payroll jobs.</td>
<td>• Employment measure reflects the number of employed persons.</td>
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<tr>
<td>• Multiple jobholders are counted for each payroll job.</td>
<td>• Multiple jobholders are counted once.</td>
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<tr>
<td>• Groups excluded from this survey include self-employed persons; the agriculture sector; private household workers (nannies, housekeepers, and the like);* unpaid family workers (persons working without formal pay in their family’s business); and workers on leave without pay throughout the reference period.</td>
<td>• Groups included in this survey are self-employed persons; the agriculture sector; private household workers; unpaid family workers; workers on leave without pay throughout the reference period.</td>
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*Note: Interested readers are encouraged to see the latest BLS definition of how private household workers are classified at http://www.bls.gov/ces/cesbmk.htm.
Bedford metropolitan area has the highest unemployment rate in the state at 11.7 percent as of January 2014. Following New Bedford are the Fall River, Leominster-Fitchburg-Gardner, Barnstable, and Springfield metro areas, all with unemployment rates above or near eight percent. The Boston-Cambridge-Quincy metro area has the lowest unemployment rate in the state, with all other areas above the state level. Unemployment rates for many of the Commonwealth’s Gateway Cities remain stubbornly high, with the cities of Fall River, Lawrence, New Bedford, Springfield, Fitchburg, and Holyoke all experiencing rates at or above 10 percent. This is another indication that despite the renewed focus on regions of the Commonwealth beyond Boston, economic growth in these areas remains a serious challenge.

Expanding state economic activity at a rate more consistent with past recoveries that also generates stronger employment growth likely awaits stronger national and global economies. While it is possible for Massachusetts to outpace the national economy, many of the state’s businesses, especially in the high-technology and health care sectors, sell to national and international markets. Absent a strong national economy, these businesses face stagnant demand for their products and services. In fact, the national economic recovery remains frustratingly slow, impeded by skittish consumers and fiscal austerity by the federal government. While housing seems to have turned the corner nationally, there remain pockets of large unsold inventories and underwater homeowners whose mortgages exceed their home values. Virtually every national economic recovery is either led or aided by a recovering housing market. With that said, the fall 2013 New England Economic Partnership macroeconomic outlook highlighted the housing sector, with evidence of housing demand exceeding supply, as a possible growth catalyst for 2014. A strong housing market bolsters the construction industry, with its important web of input/output relations with many other sectors. Homeowners’ balance sheets are growing stronger as housing improves, prompting increased consumer spending. While the housing market has been aided by historically low interest rates there is still a long way to go.

At the same time, policies of fiscal austerity by the federal government are well documented, and are ill-timed in a period of a weak economic recovery with relatively high unemployment rates. A wide range of expenditure cuts and earlier tax changes that reinstituted the payroll tax and increased rates on the highest earners have significantly lowered the current-year budget deficit. For example, the Congressional Budget Office estimates that the fiscal year 2013 budget deficit will be $680 billion (4.1% of U.S. GDP), down significantly from a high of $1.4 trillion (9.8% of U.S. GDP) in 2009. But, the near-term fiscal tightening also poses a cost to the economy as it siphons aggregate demand from the national economy when a demand shortfall continues to be a major problem. Ultimately, state economic growth cannot gain full strength during a tepid national economic recovery that still has not recovered all jobs lost during the Great Recession.

State economic growth is always dependent to some extent on the economic performance of surrounding regions. The broader New England economy that Massachusetts operates in is characterized by slow economic and demographic growth. For example, Connecticut and Rhode Island are still struggling to recover from the recession, with persistently high unemployment rates, and the Canadian economy, the state’s most important single trading partner, is now growing more slowly than the U.S. Growth opportunities are driven by a number of factors, including your nearby trade partners, and thus for Massachusetts, the surrounding region is generally not a source of economic growth, leaving our economic destiny often

![Figure 3. Unemployment Rate by NECTA, January 2014](image-url)
more connected with New York City (financial services, trade) and beyond.

**Performance by Sector**

Employment growth by sector has been mixed over the past 12-15 months, reflecting the conflicting forces playing out in the state economy. Most sectors experienced some positive job growth from January 2013 to January 2014, with the exception of Manufacturing and Public Administration. By percentage, the fastest growth was exhibited by the Information industry (e.g., software companies) with a 4.8 percent increase in jobs. The second fastest industry growth was in Construction, led by strong improvement in the construction of buildings (houses, multi-unit housing, offices, etc.). Education and Health Services, generally a stalwart of growth in good and bad times, grew by 1.5 percent over the same period, but this represented the second largest source of job gains with a net increase of 10,900 jobs. Professional and Business Services was another strong industry sector, expanding by 2.7 percent and adding 13,500 jobs along with high average pay and was an important contributor to the state’s knowledge-based economy.

The decline in manufacturing jobs in Massachussets is not a new trend but tends to mask more complex dynamics as that industry continues to be one of the top contributors to GSP, exports, and productivity growth as over 7,000 manufacturing companies in the state find ways to compete in domestic and global markets. The minimal job growth in Financial Activities is somewhat surprising but may relate to the continuing reorganization of the financial system since the recession, including a trend towards banking consolidation. The lack of growth in Public Administration is largely related to a reduction in federal government workers (including postal workers) and a small decrease in local government jobs.

**Housing**

A strong and sustained recovery in housing is usually a necessary condition for a more comprehensive economic recovery. The state’s housing market continues to show signs of strong growth. According to the Warren Group, a total of 3,902 single-family homes sold in November, down from 3,983 in November 2012. This is the first time that home sales posted a decrease and the fewest number of sales recorded for a single month since April. Even so, year-to-date sales are up more than 6 percent. A total of 45,979 sales have been recorded, up from 43,222 during the same period last year. The median price of single-family homes rose 4 percent to $307,000 in November, up from $295,000 a year earlier. This is the 14th consecutive month of year-over-year increases in the median price of a single-family home. The median price for homes sold January through November was $322,000, up 11 percent from $290,000 in the prior year.5

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**Figure 4. Employment Change by Industry, Massachusetts**

January 2013 to January 2014

(Seasonally adjusted)

![Graph showing employment change by industry](image)

Source: Massachusetts Labor and Workforce Development, Labor Market Information, Current Employment Statistics (CES - 790)

Note: Natural Resources & Mining is excluded due to its small employment.
A more accurate indicator of house price change, one that controls for the quality of houses being sold, is only available for the Boston metropolitan area via the Case-Shiller Index. It shows a 7.5 percent increase in the value of residential housing in Boston in the 12 months ending in November of 2013. Regions outside of the Boston metropolitan area are not necessarily experiencing the same healthy growth as is Boston, but even so, there are pockets around the state where the housing market is buoyant. And the recent rapid pace of growth in construction employment reflects and is driven by the recovery in house sales and prices.

**Federal Fiscal Impact: The Sequestration**

Commonly referred to as the sequestration, the Budget Control Act of 2011 mandated federal spending cuts as part of a negotiated compromise to raise the federal debt ceiling in 2011. Its intent was to push lawmakers to pass a compromise that would result in significant deficit reduction over the next 10 years. Because that compromise was not reached, the result was the sequester spending cuts of $1.2 trillion nationally over the next decade (evenly split between defense and non-defense), including $85 billion in the federal fiscal year 2013 between March 1 and September 30. While there have been relatively few announced major layoffs due to sequestration and some existing Federal grants and contracts will not be directly impacted until future years, there is mounting evidence that the sequestration has acted as a significant drag on the Massachusetts and national economies, with an estimated job impact of about 14,000 in 2013, reflecting both job losses and economic growth not added. Based on research by the UMass Donahue Institute, the magnitude of the sequestration spending reductions to Massachusetts was estimated to total at least $1 billion in 2013, possibly higher, providing a negative shock across a wide range of activities from hospital care reimbursements to furloughs of civilian workers to reduced Head Start early childhood workers and more. Furthermore, the Massachusetts economy is particularly dependent on federal grants and contracts, with $11.3 billion in defense sector contracts in 2012 (50% higher than the U.S. average on a per capita basis) and $2.5 billion in National Institute of Health (NIH) grants annually (2nd in the country), among others. Finally, because the sequestration spending caps were kept in the deal to end the government shutdown and were only temporarily lowered for 2014 (and minimally in 2015) in the December 2013 budget agreement, lower federal funding is likely a new long-term reality that impacts the core basic research at universities, hospitals, and other institutions throughout the Commonwealth, and thus threatens the broader economy in life sciences and other key technology areas.

**State Product Exports**

The state’s high-technology sector depends on global demand for its products, led by export commodities such as medical and surgical instruments, and computer and electronic machinery. After experiencing strong export growth coming out of the recession through 2010, the dollar value of exports declined in the year ending in November of 2012. In the most recent year, ending in November of 2013, export growth has rebounded, even if only modestly at about three percent, but is still trailing the peak reached two years earlier. In the recent past, up to the start of 2010, state merchandise exports closely tracked the nation. Starting that year, however, while the nation’s exports continued to grow, the state diverged from the national trend, driven in large part by oil and gas exploration and exports in other parts of the country. As exports have continued to grow nationally, state exports have followed a more variable, flat growth trend.
with current export volumes approximately at the same level as they were in the latter part of 2010. Massachusetts exports have gained ground over the past 15 months, an encouraging recent trend.

The state’s most important export recipients are the countries that comprise the European Union. These countries continue to experience austerity-induced recession or stagnation, leading to a reduction in their purchase of Massachusetts-made goods. While recent growth in the EU has prompted hope of a strong recovery, this is still more prospect than reality. Asia, where growth is still strong though lower than in recent years, is another trading bloc where demand for state products has been reduced.

DEMOGRAPHICS AS DESTINY

The two feature articles elsewhere in this issue both focus on demographic issues in the Commonwealth. Without stealing their thunder, it is worth reviewing the remarkable recent turnaround in the state’s population trend. For years, the state has not only lost population to out-migration, it has lost representation in the U.S. House of Representatives. The loss of a House seat in 2010 actually obscured a reversal of fortune in the Commonwealth’s population. Since 2005, state growth in population has outpaced the New England states, as well as the northeastern states, while converging with the national rate in recent years. More than ever, the state is a population growth center in the middle of a demographic desert. Over the past year, Massachusetts ranked 12th nationally for net population growth, and 24th for percentage increase (excluding Washington, D.C.). So, while Massachusetts does not have a fast-growing population, the long-held perception of flat or declining growth is simply not the case over the past five plus years.

CONCLUSION: SO WHAT LIES AHEAD FOR THE STATE ECONOMY?

As is described in this issue’s featured article on migration, the biggest change in the state’s population dynamics in recent years is due to a much stronger trade balance of domestic migrants. The number of net migrants has consistently been negative since 2000, falling below negative 55,000 in 2004 and 2005, meaning that more than 55,000 more people left the state for other parts of the U.S. than moved to Massachusetts. That number rapidly improved in the latter part of the last decade, peaking at a net positive of about 6,800 in 2009. While that number has dropped in more recent years, it is estimated to now be less than 10,000, largely offset by natural increases (births minus deaths) and a continued positive flow of international migrants. This growth is highlighted by the city of Boston, which grew by 3.1 percent from 2010 to 2012, with anecdotal evidence based on the recent residential building recovery that the city is continuing to expand. As with most indicators in Massachusetts, the trends and opportunities in Boston are often quite independent from the rest of the state.

This past year has seen reasonable job growth but an unemployment rate that inched up this year and is now ever so slightly higher than the U.S. These data trends make it hard to assess the state’s job markets. Will 2014 see even more job growth and an unemployment rate that falls along with it? Will the strong labor and housing market conditions in Greater Boston extend to other regions of the state? While challenges remain, we believe there are a number of factors that will lead to a stronger economy, a lower unemployment rate, and continuing job growth into 2014.
The state housing market continues to improve. House prices have firmed up, improving household balance sheets and encouraging construction activity. The prospect of higher mortgage interest rates could reign in some of this progress, but housing prospects remain positive in Massachusetts and nationally. The European Union trading bloc, the most important destination for state exports, is stabilizing and may see modest growth, an important avenue for expansion in the state’s key innovative sectors (e.g., high technology, life sciences). The December 2013 federal budget agreement eliminates the fear of another government shutdown in the near term, and lessens the severity of sequester cuts with promising signs of improved national economic growth. There is also the prospect of substantial private investment associated with the state’s casino projects, adding over $3 billion in construction over the next two to three years. While there remain risks to continuing growth, there is a distinct upside to prospects for the Commonwealth’s economy.

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The authors wish to thank Lindsay Kosigian of the UMass Donahue Institute for her research assistance and contributions to this article.

Endnotes
2.) http://www.ncepecon.org/fall2013.htm, U.S. economic forecast by Moody’s Analytics
3.) http://www.cbo.gov/publication/44716
6.) http://us.spindices.com/index-family/real-estate/sp-case-shiller
7.) http://www.donahue.umassp.edu/docs/Economic_Impacts_of_Sequestration_on_Mass_economy
8.) http://quickfacts.census.gov/qfd/states/25/2507000.html