

Western New York ECONOMIC NEWS

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The national economy is well on its way to moving onto the growth path that it was on prior to the onset of the COVID recession in the first quarter of 2020. Real GDP was 0.84% below its 2019:Q4 peak in the first quarter of 2021. Both the fiscal and monetary policy measures that have been implemented were extremely aggressive. These policies are in part responsible for the recovery, as well as the acceleration of inflation that took place during the first quarter of 2021. The region has recovered more than half of the jobs lost during the recession, and the average wages of those working are higher in 2020 than they were in 2019. State government finances seem remarkably stable, and the feared reduction in intergovernmental transfers did not materialize.

The National Economic Outlook

Quarterly annualized growth in real GDP was 33.4% in 2020:Q3, 4.3% in 2020:Q4 and 6.4% in 2021:Q1, recovering from the COVID-induced recession that began in 2020:Q1 [www.bea.gov]. In the first quarter of 2021, the economy remains \$166.4 billion or 0.84% below the peak in real GDP that occurred during the fourth quarter of 2019 (see Figure 1). The recovery from the decline in real GDP during the first two quarters of 2020 has been robust. Contributions to the recovery were largely driven by increases in personal consumption expenditures as the economy re-opened after the unprecedented COVID shutdown.

The main concern at present is whether the increase in the rate of inflation that was experienced during March and April will influence the inflation expectations of consumers and firms. Inflation rates since 2007 based on the Consumer Price Index [www.bls.gov] and the Personal Consumption Expenditure inflation index [www.bea.gov], the Federal Reserve's preferred measure of inflation, are shown in Figure 2. From February to April 2021, the annual rate of inflation based on the CPI increased from 1.68% to 4.16% while PCE inflation increased from 1.57% to 3.58%. A variety of forces are responsible for the acceleration of inflation. Among these are the overly generous fiscal stimulus packages passed by Congress, the aggressive expansion of the money supply by the Federal Reserve, supply chain problems affecting production of goods and the pent-up demand for goods and services by consumers who have been unable to spend during the pandemic. The 4.16% increase in the CPI and the 3.58% increase in the PCE index from April 2020 – April 2021 were the largest 12-month increases since September 2008.

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Figure 1. Real GDP 2007:Q1 - 2021:Q1

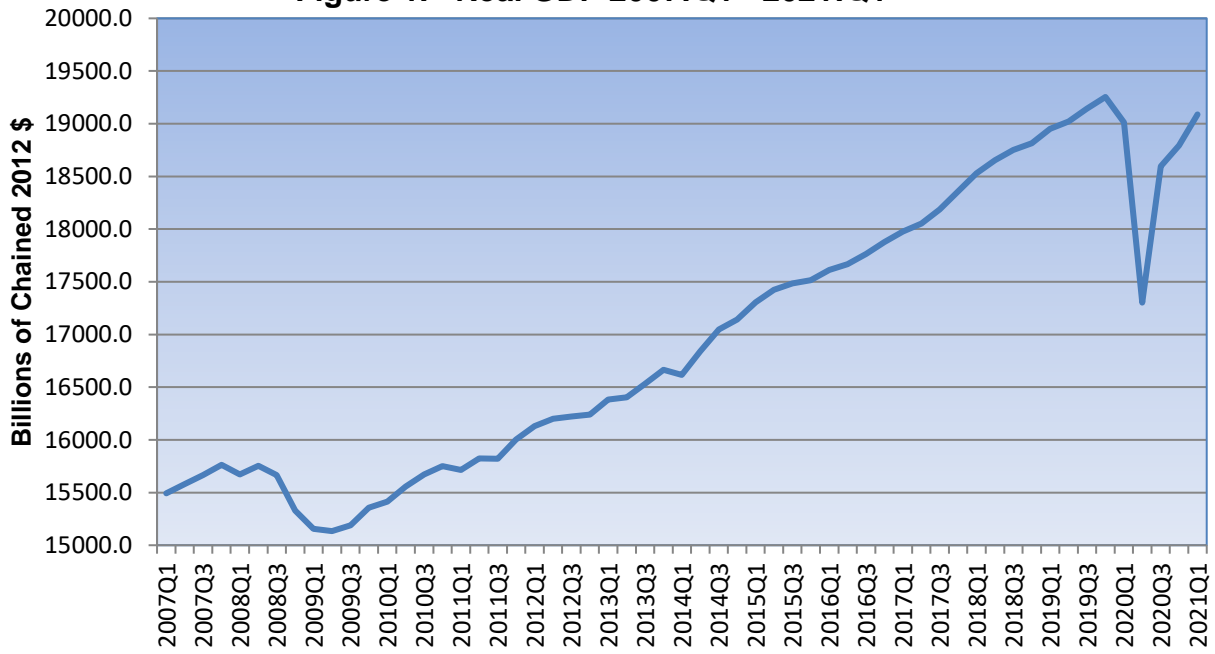
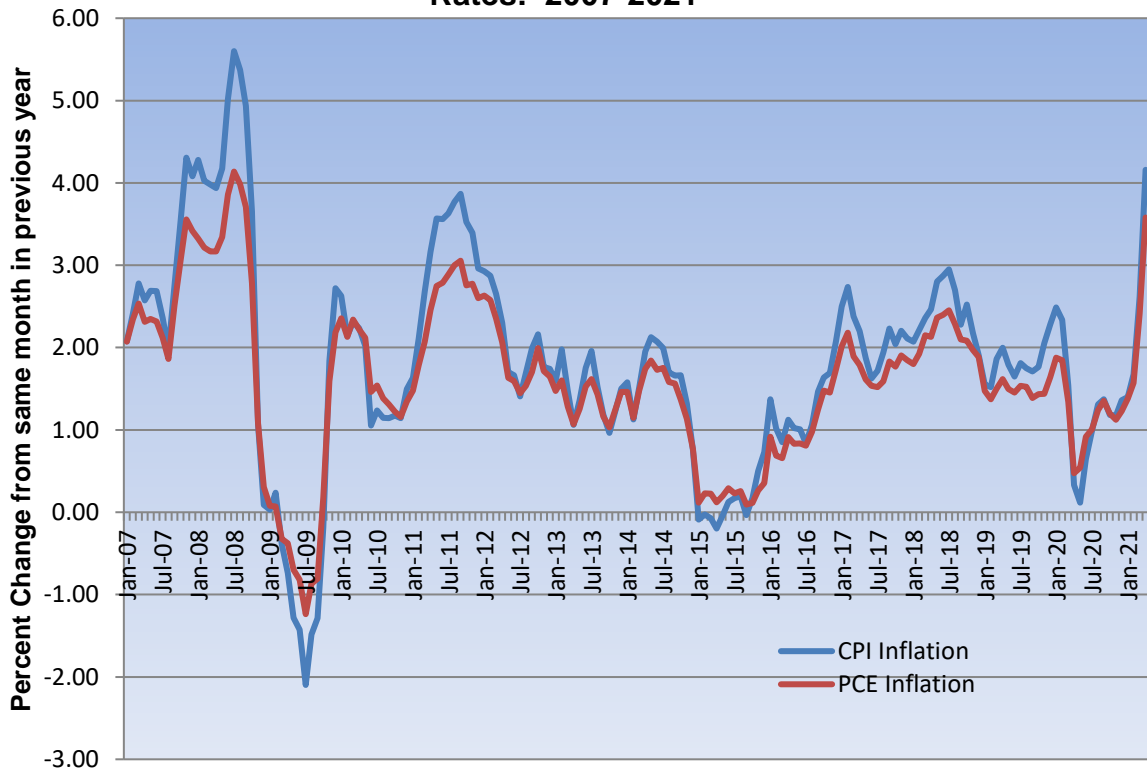


Figure 2. CPI & Personal Consumption Expenditure Inflation Rates: 2007-2021



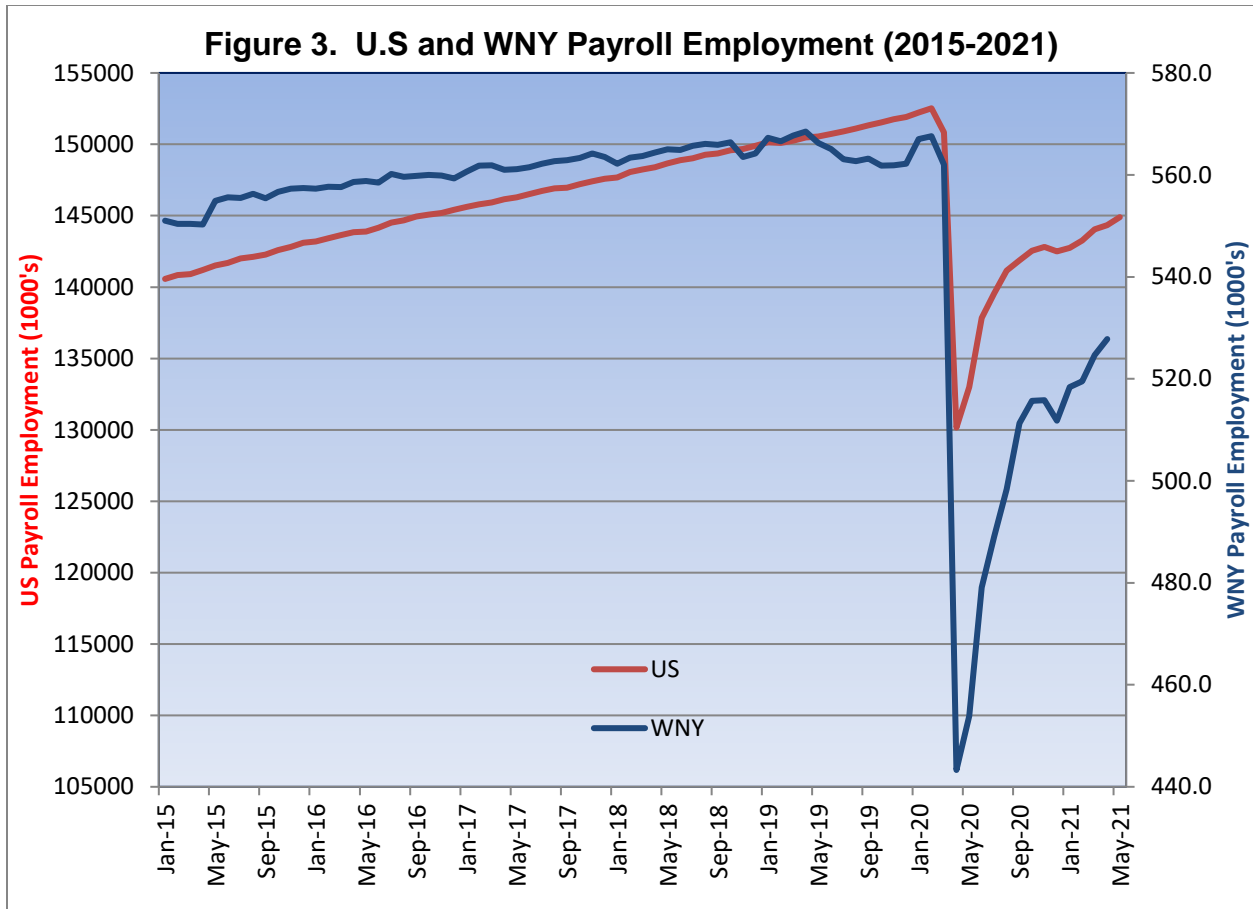
Federal Reserve policy has been more aggressive in response to the COVID recession than it was during the 2008-2009 recession. Assets on the Fed's balance sheet have doubled since March 2020 and now stand at approximately \$8 trillion. The M2 money supply has increased by more than \$4 trillion since March 2020. In its meeting at the end of April, the FOMC decided to continue its policy of increasing its holdings of Treasury securities and mortgage-backed securities by \$80 billion and \$40 billion per month, respectively. If inflation continues to accelerate at its current pace, this policy will likely be altered.

Short-term Treasury bill yields are essentially zero as a result of Fed policy. At the end of May 2021, the 3-month Treasury bill yield stood at 0.013% while the 10-year T-note was yielding 1.584%. Equity market indexes are at or near their all-time highs as investors continue to chase yield that cannot be found in investment grade debt instruments. Inflation expectations from the Treasury market can be estimated by subtracting the yield on Treasury Inflation Protected securities of a given maturity from the yield on Treasury securities with the same maturity. This metric predicts inflation of 2.864% over the next two years and inflation of 2.472% over the next 10 years.

Modern monetary theorists seem to have rejected Milton Friedman's premise that inflation is always and everywhere a monetary phenomenon. Many are not disturbed by the Fed's monetization of the huge federal deficits that have been incurred over the past several years. We do not agree with this and assign a non-zero probability of an acceleration of the inflation rate, resulting from the fiscal and monetary policies that have been put in place. The degree to which current inflation is linked to price levels that actually fell during the first half of 2020, versus increased liquidity in the banking system and higher expectations of future inflation, will in large part determine the length and severity of future price level increases.

The labor market has historically been slow to re-attain its previous peaks as a result of recessions. U.S. and WNY payroll employment since 2015 is shown in Figure 3. The national economy has recovered 14.773 million jobs since its April 2020 trough but remains approximately 7.629 million workers below its February 2020 peak. In WNY, we have recovered 82,700 jobs since April 2020, but remain 39,200 jobs below the previous April.

The national unemployment rate stood at 5.8% in May 2021, down from 13.3% in May 2020. The national labor force participation rate was up in April 2021 to 61.6% from 60.2% in April 2020 but remains below its 63.4% peak in January 2020. Significant increases in unemployment benefits, perhaps combined with increased child-care costs and perceptions of health-related risk at work, have reduced workers willingness to work at pre-pandemic wages.



The Economic Outlook for the Buffalo Region

Much has changed since the spring of 2020. The local economy has recovered at a relatively robust pace as businesses have reopened, Covid-19 positivity rates have declined, vaccination rates have climbed and consumers' confidence has increased. As summer approaches, the pent-up demand is surfacing, and we expect the job gains we have seen thus far to continue. Table 1 shows the stage of the local economic recovery as measured by payroll employment. The Buffalo MSA lost 120 thousand jobs, more than 20 percent, from April 2019 to April 2020. Since April 2020, 67.84% of those jobs have been recovered.

Accommodation and Food Services and Arts, Entertainment and Recreation each lost more than 60 percent of the jobs in the industry as the economy shut down. Through April 2021, 65.46 percent of the jobs lost in Accommodation and Food Services and 83.02 percent of the jobs lost in Arts, Entertainment and Recreation have been recovered. More than 80 percent of the jobs lost in Manufacturing and in Retail Trade, and more than 95 percent of the jobs lost in Construction have been recovered. We have seen significant improvements in the WNY job market. Though, there are still a substantial number of jobs yet to be recovered – 39,200 in all, with 10,500 in Accommodation and Food Services and 6,500 in Health Care and Social Assistance.

Table 1. Buffalo MSA Payroll Employment

	Jobs Lost from April 2019 thru April 2020	Percent Lost	Jobs Recovered thru April 2021	Percent Recovered	Jobs Yet to be Recovered
Total	121,900	21.85%	82,700	67.84%	39,200
Total Private	115,600	24.77%	80,500	69.64%	35,100
Mining, Logging and Construction	8,100	44.75%	7,700	95.06%	400
Manufacturing	8,800	16.83%	7,800	88.64%	1,000
Retail Trade	15,600	26.94%	13,100	83.97%	2,500
Information	900	13.85%	-200	-22.22%	1,100
Financial Activities	1,800	4.90%	1,100	61.11%	700
Professional, Scientific and Technical Services	3,600	12.46%	2,200	61.11%	1,400
Administrative, Support and Waste Services	7,500	27.99%	6,300	84.00%	1,200
Education	2,900	13.88%	0	0.00%	2,900
Health and Social Assistance	12,600	15.67%	6,100	48.41%	6,500
Arts, Entertainment and Recreation	5,300	67.95%	4,400	83.02%	900
Accommodation and Food Services	30,400	61.91%	19,900	65.46%	10,500
Other Services	10,000	39.22%	6,900	69.00%	3,100
Local Government	6,600	11.13%	3,500	53.03%	3,100

With over 39,000 jobs yet to be recovered, the April 2021 unemployment rate of 6.2 percent may seem surprising. Figure 4 shows the unemployment rate and the size of the labor force in the Buffalo MSA from the labor department’s household survey. Over the past year, the unemployment rate has been difficult to interpret because of the way that unemployment is defined and because of dramatic changes in the size of the labor force. In 2021 however, the size of the labor force has been relatively consistent, and we expect that the official unemployment rate understates a truer measure of unemployment by only 0.3 percentage points – that 6.5 percent is only 30 percent higher than the 5.0 percent unemployment rate in February 2020 and is down from 20.9 percent in April 2020. So, it seems that the local economy, as measured with statistics from the household survey, is recovering faster than the payroll survey may indicate.

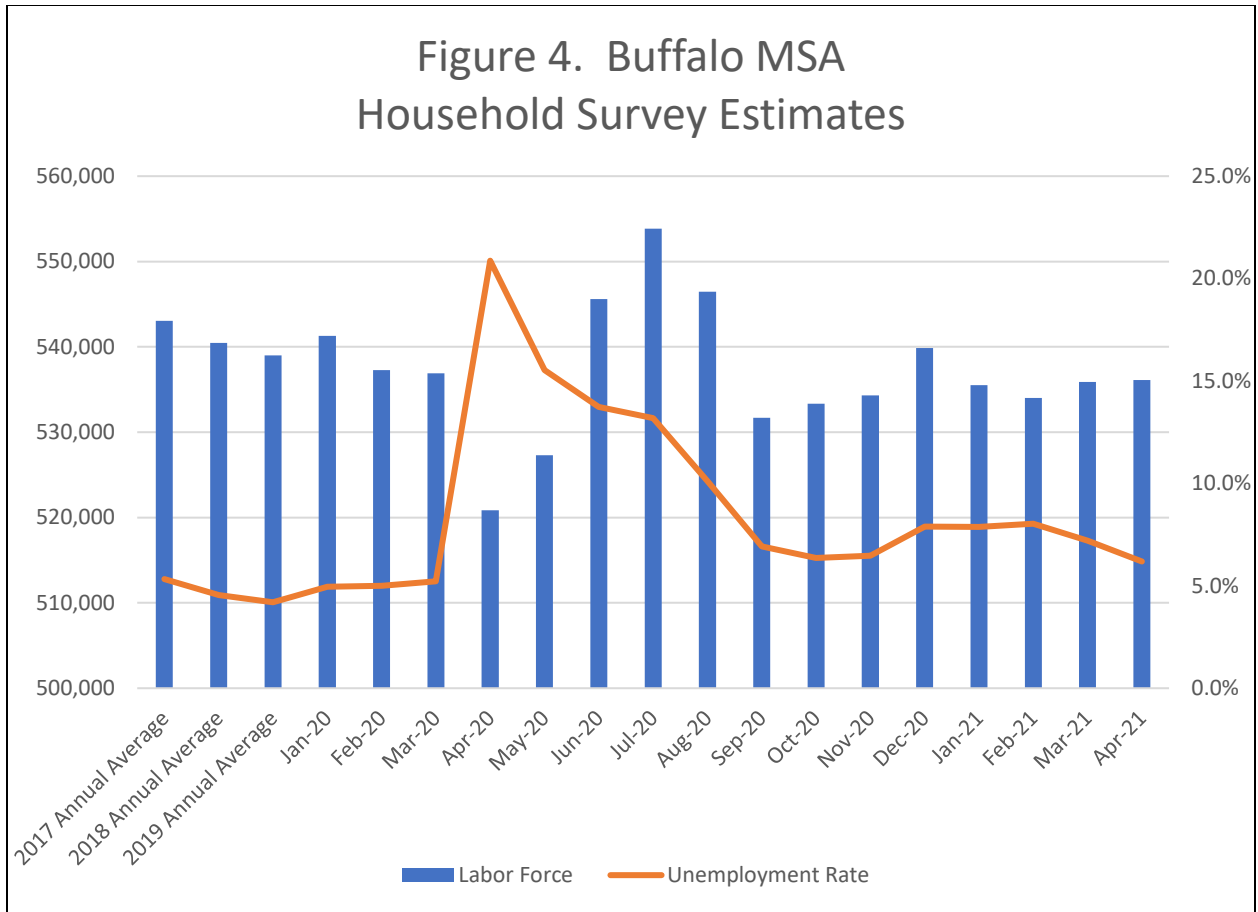
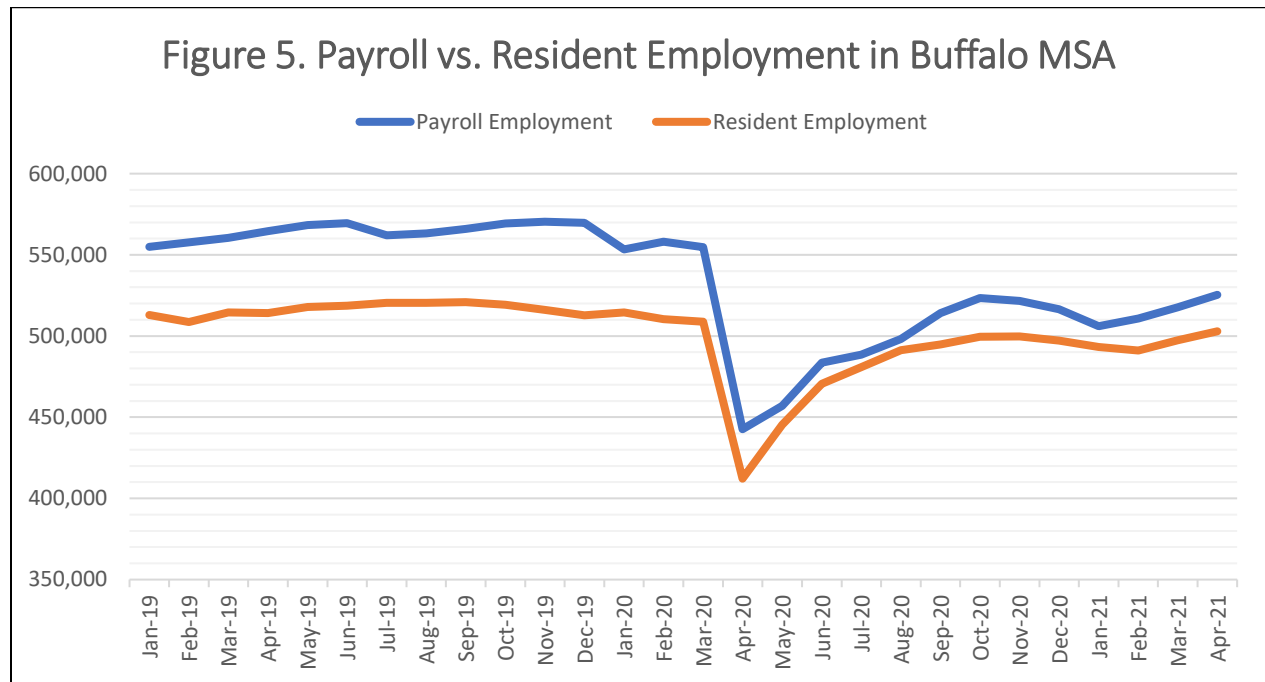


Figure 5 compares employment in the Buffalo MSA measured by the payroll survey (CES) to employment measured by the household survey (CPS). The payroll survey is sent to businesses and reflects the number of individuals on the payroll during that month. The household survey is sent to households and asks residents about their employment status. The payroll survey in the Buffalo MSA generally indicates more jobs because individuals can work for more than one company, and there are a greater number of people outside the Buffalo MSA who come into the local area to work than vice-versa. Beginning in April 2020, the gap between payroll and resident employment has narrowed, and in April 2021, resident employment is down only 11,200 from April 2019, compared to the 39,200 loss of payroll jobs.

Potential explanations for this disparity include the closing of the U.S. - Canada border, which has made it difficult for Canadian residents to travel into the Buffalo MSA for work; the shift from payroll jobs to self-employment opportunities like contract work; the availability of remote work options, which would allow local residents to take jobs that were based in other geographic locations; and the shift from part-time to full-time opportunities and/or an increase in wages, which would decrease the need to work multiple jobs. No matter the cause(s), this will have implications for the jobs recovery going forward.

Recently, anecdotes of difficulties faced by businesses in hiring workers are often followed by discussions of the unemployment insurance benefits offered to workers who lost their jobs during the pandemic. While the benefits certainly affect individuals' decisions, especially as they raise reservation wages (potentially above the pre-pandemic wage levels in Food Service and in Social Assistance), a look at local resident employment indicates that it is not the only explanation, and since some local schools have only recently transitioned to full-time, in-person learning, a discussion of the necessity and affordability of child care in decisions regarding a return to the workforce is warranted.



The most accurate measure available of the overall impact of the coronavirus recession on the local economy is the 2020 QCEW data released on June 2 (see Table 2). While these charts have been a part of our reports for several years, never before has a year over year comparison show such stark and dramatic changes. While establishment based annual employment levels fell 10% from 2019 to 2020, average pay per worker increased approximately 10%. This is not the stuff of normal recessions. The only industrial sector to gain employment over the year was the federal government, a modest 500 jobs during a Census year.

The industry sectors that lost the largest proportion of 2019 employment were leisure & hospitality (-30%), other services (-19%) and information services (-13%). Interestingly, the average wage of those who continued to work in those industries in 2020 was higher than the average wage had been in 2019. Likely causes of this change are that lower wage earners made up a larger fraction of those who lost employment during 2020, or there individuals were working longer hours in these sectors.

Table 2. Buffalo MSA QCEW Employment and Earnings by Industry: 2019 - 2020

Industry	Average Annual Employment 2019	Average Annual Employment 2020	Change in Employment 2019 to 2020	2019 Average Annual Pay (\$)	2020 Average Annual Pay (\$)	2020 Pay % of U.S. Average
Total, all industries	544,123	490,461	-10%	50,912	55,745	87%
Total, Federal Government	9,391	9,843	5%	79,265	80,305	94%
Total, State Government	20,285	19,970	-2%	74,375	75,573	115%
Total, Local Government	55,877	51,607	-8%	56,165	60,544	106%
Total Private all industries	458,570	409,041	-11%	48,653	53,580	83%
Goods-producing	74,259	69,251	-7%	64,985	67,377	96%
Natural resources & mining	1,745	1,720	-1%	40,622	42,618	70%
Construction	20,489	18,733	-9%	59,800	64,484	96%
Manufacturing	52,025	48,798	-6%	67,844	69,360	94%
Service-providing	384,312	339,790	-12%	45,497	50,769	81%
Trade, transportation & utilities	96,943	89,748	-7%	40,331	45,110	86%
Information	6,651	5,769	-13%	67,014	73,900	54%
Financial activities	35,555	34,315	-3%	67,313	72,481	68%
Professional & business services	68,357	62,013	-9%	61,021	64,772	77%
Education & health services	95,273	88,188	-7%	45,918	50,017	90%
Leisure & hospitality	59,967	42,055	-30%	25,882	30,329	117%
Other services	20,952	17,057	-19%	29,367	32,610	74%
Unclassified	614	645	5%	37,331	45,373	68%

<https://www.bls.gov/cew/overview.htm#coverage>

Table 3. Tax Revenue U.S. and New York State

	United States Total		New York	
	State Government Tax as % of Total	% Change Tax Collections 2019 to 2020	State government tax as % of total taxes	% Change Tax Collections 2019 to 2020
Property Tax	2%	3%	0%	NA
Individual Income	37%	-7%	56%	12%
Sales & Gross Receipts	48%	1%	32%	4%
Other taxes	5%	-8%	5%	2%
Total Taxes	100%	-2%	100%	9%

State and local governments seem to have fared better than feared last spring. The most important single revenue source for the New York State government is the individual income tax. NYS individual income tax collections increased by 12%, compared to a 7% decline for the nation as a whole. Sales taxes increased 4% compared to 1% for the rest of the states and other taxes increased 2% compared to a decline of 8% nationwide. The dependence of other states on extractive industry taxes may be the explanation for some of this difference.

Since total tax collections for the New York State government increased by 9%, the feared reduction in state aid to local has not yet materialized. Combined with direct federal transfers to states, the fear of state and local government debt defaults and bankruptcies has diminished from the near panic levels of March 2020. The long-term impact of the pandemic on commercial and residential property values is yet to unfold, but the dramatic increase in housing prices is contrary to what some feared last spring.

