NEW ENGLAND ECONOMIC OUTLOOK, FALL 2012

After the Election the New England Economic Outlook Remains Much the Same – Challenges and Uncertainties Continue and Weak Economic Conditions Persist

New England Economic Outlook: Overview

The New England states continue to experience slow growth and slow recovery of the jobs lost in the recent recession. The main reason for this is the continued weakness in global and U.S. economic conditions. The U.S. and New England economies are affected by concerns about the fiscal cliff in the U.S. (see discussion below of conference theme) and the weak European economy and sovereign debt crisis and all of these have strong influence over the regional economic outlook.

The New England Economic Partnership Fall 2012 forecast is based on the Moody's Analytics United States baseline forecast. NEEP forecast managers and the NEEP Forecast Quality Review Committee believed that the most recent data and events suggested that the Moody's Analytics October baseline forecast was reflective of the prospects for the national economy.

The forecast for the New England region is for the economy to continue to grow slowly with employment growth averaging 1.5% per year and overall economic (regional gross product) growth averaging 3.3% per year over the forecast period out to 2016. This is below the growth of 2% in employment required to significantly reduce unemployment in New England. With the expected slow growth the region will not return to its pre-recession employment level until 2015.

After a relatively strong first quarter of 2012 with 2% annualized growth in employment, employment growth is not expected to be at 2% again until the middle of 2014 and then is not expected to rise much higher during the forecast period. The regional unemployment rate is expected to remain below the U.S. average, but above 6% until 2015.

Recent data suggests that the housing market might emerge as a relative bright spot in the economy, with rising home prices bolstering the construction industry and related industries including retailers selling home supplies, landscapers and cable providers. Regional median housing prices are expected to increase. However, the increases are expected to be only modest, with annual increases only reaching 3 to 4% starting in 2013.

All the states in the region are expected to have employment growth below the national average over the forecast period. Demographic factors including lower labor force growth than the U.S. average contribute to slower employment growth than the national average. There will continue to be significant variation in economic performance across the region. Massachusetts, New Hampshire and Vermont are expected to have the strongest economies in the region over the forecast period. Rhode Island is expected to continue to have the highest unemployment rate in the region throughout the forecast period as the state continues its slow recovery from the most significant percentage employment decline in the region during the last recession.

Gross Regional Product

The region's overall economic growth is expected to remain low, especially for a recovery from a recession. The gross regional product annualized growth is expected to remain below 3% until mid-2013. After peaking at 4.1% in mid-2014, overall growth is expected to decline, with annualized growth in 2016 expected to be 3.3%.

Employment

Annualized growth in employment in the region is expected to remain below 1% through the first quarter of 2013, and then increase gradually to 2.3% in the fourth quarter of 2014. The region's employment growth is expected to be 0.5 to 1% below national employment growth throughout the forecast period.

On a percent change from employment troughs to the middle of 2016 basis, the strongest sector of the regional economy is expected to be professional and business services increasing by 17.5%, followed by construction (16.2%), high tech (15.9%), leisure and hospitality (12.4%), and health and education services (10.7%). Manufacturing, trade and finance are expected to have lower growth. Government employment is expected to continue to be adversely affected by fiscal pressures at the federal, state and local levels with below 1% annualized growth until late 2013.

Unemployment

With the extended period of low employment growth, the unemployment rate in the region is expected to decline only gradually -- from 7.4% in the last quarter of 2011 to 6.8% in late 2013 and then to just below 6% (5.8%) by mid-2016. The region's unemployment rate is expected to remain below the national average throughout the forecast period mainly due to the slow growing labor force and the relatively high level of educational attainment of the workforce in the region.

Across the Region

Vermont is expected to continue on its trajectory with the fastest growth in employment coming out of the recession in the region. Total employment growth in Vermont from its recession trough to the end of forecast period is expected to be 9.2%, followed by Massachusetts (8.8%), and New Hampshire (8.2%). All of the New England states are expected to continue to have below the U.S. average employment growth, with Maine having the lowest forecasted growth rate from trough to the end of the forecast period at 5.8% about one-half the US growth rate (11.2%).

Vermont and New Hampshire are expected to continue to have the lowest unemployment rates in the region and Rhode Island the highest over the forecast period. By the end of 2015 Vermont's unemployment is expected to be down to 4.1% and New Hampshire's to 4.5%. In mid-2016 Rhode Island (7.0%), Connecticut (6.4%), and Maine (6.1%) are expected to have the highest unemployment rates. Massachusetts is expected to have 5.7% unemployment at the end of the forecast period.

Housing

Housing prices have been starting to stabilize and slowly rise nationally and in the region. The increases in median price are expected to be highest out to mid-2016 in Vermont (25.6%) and Massachusetts (25.2%). Rhode Island (14.6%) and New Hampshire (12.9%) are expected to have the slowest recovery in housing prices in the region.

Conference Theme: **The Next Four Years: Economic Outlook in New England Post Election**

Of significant concern looking forward is how the nation's financial difficulties and the so called fiscal cliff will be addressed. This issue has become front and center after the 2012 election and this is the focus of the conference luncheon panel**.**

In addition to the baseline forecast, Moody's Analytics has provided NEEP with an alternative forecast scenario of "U.S. Fiscal Cliff." This scenario describes the impact if federal law makers do nothing before the end of the year and the federal government goes over the fiscal cliff. Doing nothing would mean tax increases and spending cuts totaling just under $730 billion nationally in calendar year 2013. This would be the fiscal result of the expiring of the Bush-era tax cuts, the alternative minimum tax patch, this year's payroll tax holiday and the emergency unemployment insurance program -- all expiring on schedule just as government spending drops according to the terms of last summer's deal to raise the Treasury debt ceiling.

The economic implications of going over the fiscal cliff would be significant in the region. The region, according to Moody's, would be expected to experience above average employment decline. This is mainly because of the region's relatively high average income and the impact on high tax payers of increasing taxes on their spending in the region. It is also influenced, but less so, by the region's relatively high dependence on federal healthcare expenditures and research support.

In terms of employment loss, all the states in the region would be expected to be adversely affected above the U.S. average. Four of the New England states – Connecticut, Vermont, Rhode Island and Massachusetts – are forecasted by Moody's to be among the seven most negatively impacted states. This is in terms of expected percentage decline in employment in 2014 from the baseline due to going over the fiscal cliff. Maine (18^{th}) and New Hampshire (20^{th}) would also be affected more than the median state, see Table 1. All the states in the region would be expected to suffer percentage decline in employment above the U.S. average of 2.03%.

Table 1: Fiscal Cliff Percent Decline in Employment from the Baseline in 2014

	% chg	Rank
Connecticut	2.5	3
Maine	2.1	18
Mass	2.2	7
NH	2.0	20
Rhode Island	2.3	6
Vermont	2.3	5
US	**2.0**	
Top	2.6	Michigan
Bottom	1.4	Delaware

The indirect effects of the fiscal cliff particularly represented by the expiration of the Bush tax cuts and the alternative minimum tax patch represent more than 75% of the total employment changes due to the fiscal cliff. These would hit the New England states particularly hard.

According to Moody's the New England states would not be as impacted relative to other states by the direct federal spending cuts with the fiscal cliff as they would be impacted by rising taxes. This is due to the relatively limited presence of military operations in a majority of the region's states. Direct federal government expenditure declines with the fiscal cliff would account for more than the national average in three of the New England states – Maine, Connecticut, and Vermont, with New Hampshire the least impacted (see Table 2).

Table 2: Fiscal Cliff Federal Defense and non-Defense Expenditure Decline as % of GDP

	% of GDP	Rank
Connecticut	0.40	13
Maine	0.40	12
Mass	0.31	31
NH	0.29	42
Rhode Island	0.31	30
Vermont	0.40	14
US	**0.31**	
Top	0.81	Hawaii
Bottom	0.15	Delaware

While the likelihood of going completely over the fiscal cliff is low, the projected state employment percentage declines highlight how significantly federal policy and slow action on addressing longer term fiscal concerns could impact the New England state economies. The hope is that after the election there will be some progress made to address the immediate fiscal cliff and over time with more rational economic policy making in Washington.

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