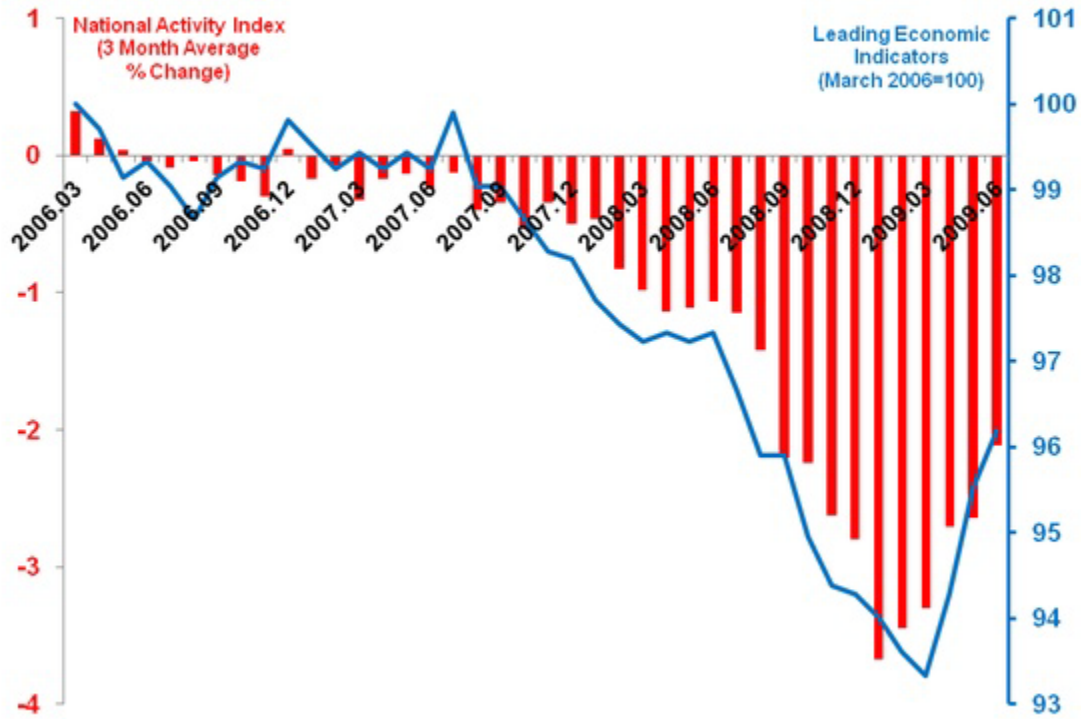




The Condition of the U.S. Economy



Source: Chicago Federal Reserve and The Conference Board

July 27, 2009

While reports on the state of the economy were sparse last week, the news was generally positive (see *Latest Economic Reports* section below). Sales of existing homes rose for a third consecutive month in June, signaling that the housing market is starting to turn around, and the latest initial unemployment claims (while on the upturn) are still lower than they were a month or so ago.

However, it is important to remember that new claims for unemployment insurance have been artificially low over the past few weeks due to seasonal adjustment factors involving the auto sector. Going forward, these factors should subside, and we should get a better look at the actual state of the labor market as the economy makes its way through the first month of the third quarter.

The most significant positive news that came out last week involved two reports on present and current economic conditions (see chart above). After deteriorating for seven consecutive months and bottoming out in January, the Chicago Fed's National Activity Index (CFNAI) improved for a fifth consecutive month in June. The three-month moving average (see red bars in chart) shows that the economy ended the second quarter in a better position than when it began the first quarter.

In June, 15 of the 85 components that make up the CFNAI were positive (the same number as May.) However, 52 of the components actually improved while only 33 deteriorated. Recent improvements should be put into context. The three-month average of the CFNAI is still consistent with an economy in recession. While the economy is clearly contracting at a slower rate than at the beginning of the year, it is still contracting.

The other significant piece of good news is that the Conference Board's leading indicators improved for a third consecutive month in June (for the first time in five years) and increased by 3.1 percent in the second quarter (the biggest three-month gain since early 2002, see blue line in chart).

With June's increase, the leading index has reversed almost half of its peak-to-trough fall over a three-year period ending in March of this year. The lead times between the trough in the leading index and the official trough in economic activity, as determined by the NBER Business Cycle Dating Committee, have averaged about six months in all the recessions since 1960. If this relationship holds, the end of the current recession could come either late in the third quarter or early in the fourth quarter of this year.

Dave Huether
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Latest Economic Reports

Last Week's Economic Indicators:

Color Code

Positive (improving)

Positive (slowing)

Unchanged

Negative (improving)

Negative (declining)

This Week's Indicators:

Monday

New Home Sales (June)

Texas Manufacturing Survey (July)

Tuesday

S&P Home Prices (May)

Consumer Confidence (July)

Richmond Manufacturing Survey (July)

Wednesday

Durable goods orders (June)

Leading Economic Indicators (June)

The Conference Board's leading economic indicators posted a third consecutive monthly gain in June, rising by 0.7 percent last month and capping an impressive second quarter that suggests the recession could end sometime in the second half of the year.

Chicago Fed National Activity Index (June)

The Federal Reserve Bank of Chicago's national activity index rose to -1.8 in June from an unrevised -2.3 in May. The three-month average increased to -2.1 from an upwardly revised -2.7 in May. The index has improved considerably since January but is still consistent with recession.

Although a majority of the 52 components that make up the index are still in decline, their rate of decline is slowing.

Existing Home Sales (June)

Existing home sales are turning up, and the overall housing market is nearing a bottom. Sales of existing homes increased by 3.6 percent in June, marking the third consecutive monthly increase and the longest string of gains since 2004.

The months of inventory fell to 9.4 months, the second consecutive monthly decline.

Initial Jobless Claims (Weekly)

Following three consecutive weekly declines, the Labor Department reported that initial jobless claims rebounded during the week ending July 18, rising to a level of 554,000 from 524,000 for the week ending July 11.

Even with that increase, initial claims were down 12 percent compared to a month earlier. Is this a sign that the labor market is starting to stabilize? Unfortunately, no.

Initial claims have been depressed over the last few weeks due to seasonal adjustments that expected temporary layoffs in the motor vehicle sector this time of year. However, because shutdowns in auto production already occurred earlier in the year, this expected component in initial claims did not take place, resulting in a lower number of initial claims reported by the Labor Department over the past few weeks.

Thursday

Weekly Jobless Claims
Kansas City Manufacturing Survey (July)

Friday

GDP (2Q Advanced)
Employment Cost Index (Q2)

Questions or Comments?
Please contact Dave Huether at
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This week's report will be the first since late June where the motor vehicle adjustment will not be a significant issue, so it should be a good gauge of the direction of the labor market. While an increase in initial claims is expected, the extent of the gain will be an important barometer of the state of the economy.

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