

A man in a suit is sitting on a large banknote, possibly a \$100 bill, which is part of a larger image of a stack of money. In the foreground, there is a blue sign with the word 'Recovery' and a white arrow pointing to the right. The background is a close-up of the banknote, showing the number '100000' and some text.

# Economic Outlook Montana's Recovery is Closer

by Patrick M. Barkey

**T**he forecasting business is by its very nature future-oriented. So even though evidence of the recession remains depressingly easy to find, the signs of recovery in the coming months are becoming clearer as well. The question for the Montana economy is, what will the recovery look like?

That was the question we addressed during our Economic Outlook Update program delivered in six Montana cities this summer. Just as every recession has been different, the recoveries that have followed have each been distinct. And with so much heavy lifting ahead as businesses and households attempt to repair their balance sheets by accumulating assets and retiring debt, this recovery promises to be a very slow one indeed.

## Montana's Recession Experience

As the recession has played out and the signs of recovery begin to appear, two basic conclusions have emerged concerning the state's economic performance.

The first is that the recession has been milder in Montana than in most parts of the country. As shown in Figure 1, the employment decline has been much shallower in Montana than the U.S. average. Indeed, the 1.8 percent decline in payroll employment we expect to see over the entire recession in Montana is smaller than all but three other states plus the District of Columbia.

But it is equally apparent that the state did not escape the recession. Indeed, for some parts of the economy, such as the construction industry, the downturn has been just as severe in Montana as in the national economy. Both Montana and the nation have seen construction payrolls shrink by more than 20 percent

since the beginning of 2007. The recession has put significant stress on state and local governments and has produced double-digit unemployment rates in some parts of the state, particularly in northwest Montana where the permanent closures of wood products facilities have idled thousands of workers.

We have made no major revisions to our forecast of the state economy that we delivered in February of this year. We correctly anticipated much of what has unfolded since then, but we have been surprised by some things.

Our February forecast factored in the passage of significant stimulus legislation, which did occur. We also expected that construction would continue to decline. Unfortunately, that forecast came true as well – housing starts statewide have now fallen to just 25 percent of their pre-recession peak levels experienced in 2005. We also guessed, with a bit less confidence, that commodity prices would end their free fall and stabilize at levels at or near those experienced just before the 2007-08 boom. In fact, those prices have remained a moving target, but the direction of change has been up for oil, copper, lead, and zinc.

On the other hand, we were surprised by the weakness in the retail economy in Montana at the close of 2008. Based on retail employment and other indicators, Montana experienced the same sharp decline in retail sales during the last quarter of 2008 that occurred in the national economy, which impacted the state's retail centers. Wages paid to retail trade workers in the fourth quarter of 2008 were down by 2.3 percent, 6.9 percent, and 9.3 percent in Missoula, Flathead, and Gallatin counties, respectively, compared to the same quarter one year earlier. But we were pleasantly surprised to find that some announced or anticipated layoffs in the state's mining industry did not take place.

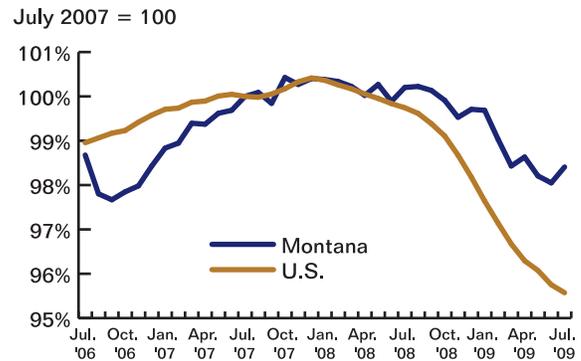
## An Assessment of Montana's Economic Base

The U.S. recession will end this fall. There are several signs that it may have ended already. Housing and manufacturing have begun to rebound from their recession lows, retail sales have begun to tentatively recover, and although job losses continue in the U.S. economy, they have become significantly smaller with each passing month. The economy remains quite fragile, but a respectable rebound in stock prices and the easing of the financial panic has helped consumer confidence recover, and with it an end to the worst recession in a generation will finally arrive.

Those events will impact Montana as they affect the key industries that are the basic drivers of the state economy. In building our updated forecast, we consider the outlook for each of these industries in turn:

- **Nonresident travel.** Tourism and recreation spending were sharply down in Montana in 2008, after four years of strong growth. The industry has been impacted by cutbacks in consumer spending overall, with shorter trips and less spending the unfortunate result. The forecast is for another 2 percent decline in spending in 2009.
- **Mining.** Natural resources employers have neither grown nor shrunk their workforce, although hours and overtime have been curtailed. With the early resumption of growth in Asian markets, the outlook is cautiously optimistic.

**Figure 1**  
Payroll Employment, Montana vs. U.S. Index, July 2007=100



Source: U.S. Bureau of Labor Statistics.

- **Manufacturing, including forest products.** Montana's forest products industry has been dealt a severe blow, as the housing slump promises to drag on. Sawmill capacity is down 30 percent, and the industry's survival in many areas is in doubt. The performance of manufacturing outside of forest products has been much better, especially in comparison to other states.
- **Agriculture.** Grain prices are down significantly from their pre-recession peaks, with only mild relief

## Chronology of a Recession

What some now call the "great recession" had humble beginnings in early 2008. A correction in housing markets, primarily in the United States and a handful of other countries, was putting the brakes on consumer spending growth and stressing financial institutions. The Bush administration steered a tax stimulus through Congress. And at the Bureau of Business and Economic Research we were projecting that Montana was likely to miss the national recession altogether.

That forecast was not without precedent. In each of the previous two recessions, in 1991 and 2001, the state economy emerged relatively unscathed. And with the important exceptions of construction and forest products, Montana was on course to weather this storm as well. High commodity prices and good years for agriculture helped offset the housing-related weakness in the state economy, and the state economy managed good growth through the first half of 2008.



But the mild national recession turned much more severe in the fall of 2008. In a short space of time, the financial sector collapsed, commodity prices plummeted, and the recession became global. Consumer spending went into sharp retreat as a sense of panic gripped Wall Street, sending stock prices sharply downward and ultimately wiping out \$15 trillion of households' net worth. That is when the downturn in Montana began in earnest. As depicted in Figure 1, stagnation in payroll employment turned into a significant decline beginning in August. The most recent (preliminary) data now show that Montana's seasonally adjusted payroll employment total was down by 9,000 jobs in July 2009, or about 1.8 percent, from its pre-recession peak. That decline was milder than all but three other states plus the District of Columbia. But it is still the most severe downturn the state has suffered since the 1980s.

## Recession in Montana: It Depends On Where You Live

This recession has proven to be the biggest setback for the state economy since the 1980s. Yet its impacts across the state have been remarkably varied. Western Montana has faced the full brunt of the downturn, especially the previously faster growing communities where the housing bubble's impact was especially pronounced. But some areas of the state have hardly felt the recession's impact at all.

The tiny 0.4 percent growth in inflation-corrected non-farm labor income posted by the Montana economy last year was lower than anything the state has experienced in 20 years. And it was a jarring change from the 3.6 percent average annual growth posted by the state in the seven years prior to 2008.

But as shown in Figure 2, there was quite a gap between the high and low performing areas within Montana over the last year. From the fourth quarter of 2007 (when the recession officially began) to the fourth quarter of 2008, income growth was sharply negative for Flathead and Gallatin counties, thanks in part to their heavy dependence on real estate and construction plus the wood products layoffs and shutdowns near Kalispell. On the other hand, the government-dominated economies of Cascade and Lewis and Clark counties enjoyed positive growth, particularly in Helena. Strong agricultural prices, continued oil and gas exploration, plus additional border patrol resources gave a boost to the Hill County economy. The Missoula and Yellowstone county

economies, the state's largest, both hovered close to zero.

The recoveries in these separate areas can be expected to be varied as well.

- Flathead County has been the epicenter of the recession. The real estate and construction bust has been accompanied by wood products layoffs and permanent closures. Our forecasts show two years of decline (2008 and 2009) followed by a return to slow growth in 2010.
- The recession has been relatively mild in Yellowstone

County. The Billings-area economy has slowed dramatically, but growth is not projected to turn negative. Billings' retailers continue to lose market share to competitors in Miles City and Bozeman.

- The deceleration in Gallatin County has been caused (so far) mostly by the real estate and construction bust. The big worry is whether or not the high-tech sector will be hit as hard as it was during the 2001 recession. The recovery in Gallatin County is likely to be lethargic because of the state government wage freeze impacting Montana State University.
- State and federal governments dominate the Lewis and Clark County economy, so the recession impacts were relatively small in the Helena area. But the state government wage freeze will mean relatively slow growth during the next two years.
- The Missoula economy has been hit by the construction and real estate bust, a slowdown in transportation, plus the permanent closure of a wood products plant. Our forecasts show two years of decline (2008 and 2009). The recovery will be slowed by the state government wage freeze impacting The University of Montana. In the long run, Missoula retailers are also facing competition from firms in Hamilton and Kalispell.
- The presence of Malmstrom Air Force Base has made the recession hardly visible in Cascade County. There has been a slight slowdown in construction, and this will lead to slightly slower growth in the future.
- Economic growth in Hill County will slow as agricultural prices have moderated and the recent increases in federal employment and oil and gas will probably not be repeated.

Helena, Missoula, and Bozeman will all be negatively impacted by the state government pay and hiring freeze. The BBER forecast calls for growth during the recovery to be slower than what was experienced during the pre-recession boom in all of these communities.



in input prices. Beef prices are also challenged by declines in global demand that only recently seemed to be permanently rising.

- **Federal government.** The federal presence in the Montana economy has been an important source of stability. In addition to a continuation of growth in forest and land management, as well as staffing of border facilities, the passage of the stimulus legislation has significantly expanded federally funded activities of all kinds. It is estimated that the state will receive \$900 million in earmarked and unrestricted stimulus money.

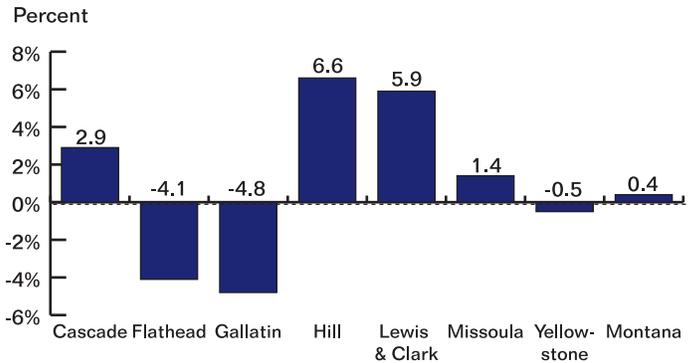
These industries have always been key to the state's overall economic performance because they all draw dollars and resources from outside our borders into the state. There is also a very close relationship between variations in the industries on this short list and changes in the overall state economy.

## The Forecast for the Montana Economy

The tepid U.S. recovery and the mixed outlook for Montana's key industries translate into a recovery for the state economy that is markedly milder than the growth experienced in the pre-recession boom. Indeed, if our forecast is on the mark, the state will see income growth in each of the next two years that is no better than half of the growth averaged during the 2001-2007 period.

The recent history and our forecast for inflation-adjusted nonfarm personal income for the years 2009-2012 shown in Figure 3 reflect both revisions to recent historical data as well as our new forecast. The weakness in retail, construction, and real estate led to a significant downward revision in

**Figure 2**  
Annual Percent Change in Nonfarm Labor Income in Constant Dollars, 2007Q4 - 2008Q4



Source: U.S. Bureau of Labor Statistics.



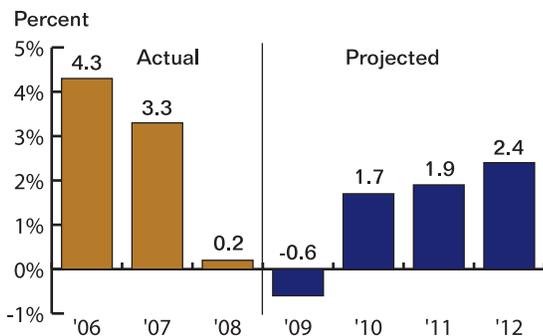
the growth estimate for 2008. We now estimate that the state economy saw only 0.2 percent growth in that year. As can be seen from the figure, 2009 is the trough year for the state economy, with modest growth resuming in 2010.

Given the slow pace of growth as the recovery gets started, we cannot expect to see meaningful improvement in the labor market in the months ahead. Indeed, it won't be until the end of next year before we see strong enough growth in the Montana economy to produce significant job growth and a fall in the state's unemployment rate. □

*Patrick M. Barkey is the director of The University of Montana Bureau of Business and Economic Research.*

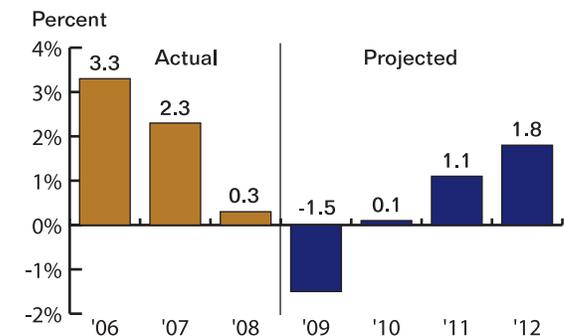


**Figure 3**  
Actual and Projected Change in Nonfarm Labor Income, Montana, 2006-2012



Source: U.S. Bureau of Economic Analysis and The University of Montana Bureau of Business and Economic Research.

**Figure 4**  
Montana Employment Forecast, 2006-2012



Source: IHS Global Insight, Inc.