



What's blocking the recovery

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The economy's expansion last quarter, for the first time in more than a year, has prompted much speculation that the recession is over. This turning point, however, simply marks an end to the decline in activity. The unemployment rate is at the highest level since the early 1980s, and full employment remains a long way off. Early this year a team of scholars at the Brookings Institution began tracking data to assess where the nation stands regarding the Constitution's mandates that the government "provide for the common defense, promote the general welfare, and secure the blessings of liberty." In this second "How We're Doing" index, we examine the forces that stand in the way of a strong rebound.

About 8 million jobs have been lost to this recession -- the largest decline in percent terms since the Great Depression. While the pace of job loss has recently moderated, the weak business outlook and still-tight financial conditions point to continued slack in labor demand. A weak labor market augurs weak income growth, which means we are unlikely to see sustained robust gains in consumer spending anytime soon.

Strong growth in consumer spending is possible if households are willing to spend more and save less out of the income they have. But with home prices and stock prices both down about 30 percent from their pre-recession peaks, personal saving has risen as people attempt to rebuild household assets. Greater saving will eventually put households in a more sustainable position, but will also slow the pace of recovery.

Housing prices have turned up in recent months, but it is unlikely that a rebound in home construction will lead the recovery. The inventory of unsold homes has fallen with the collapse in construction, but remains high by historical standards. The millions of homes in the foreclosure process raise the risk that distressed properties will flood the market in coming quarters.

Regional diversity reflects the different forces at play with regard to a broad recovery. While this recession represented a massive blow to the national economy, the Washington area was only mildly hit. Its job losses and unemployment rate are well below national averages, and its gross domestic product has already recovered to pre-recession levels. Home prices fell substantially, but recent increases may signal that a turning point has been reached. Washington has benefited from strong concentrations in industries whose declines were minimal, such as professional services, information, education and government.

By contrast, Cleveland began to suffer well before the national economy. While employment there is down almost 6 percent from a year ago, the metro area has shed nearly 40 percent of its manufacturing jobs since 2000. The mortgage credit boom drove serious foreclosure problems in both the city and its suburbs. Now the region's economic crisis may be further destabilizing housing

prices, which, after showing signs of recovery earlier this year, flatlined in the past quarter. Like other manufacturing-dependent metro areas in Great Lakes states of Ohio, Michigan and Indiana, it is unclear when, if ever, Cleveland may recover fully to its pre-recession state.

Out West, the recession came a bit later to Las Vegas, but its recent job losses have been even more severe than those in Cleveland. That region's overreliance on home building and rising home prices during the housing bubble ultimately battered its economy amid the subprime lending fallout and ensuing credit crisis. A plunge in consumer spending further damaged the metro area's tourism and hospitality industries, which are critical to the local economy. While national home prices are showing signs of recovery, home prices in this area continue to fall. Las Vegas and similarly structured housing and economic markets in inland California and throughout Florida will have to rethink their future growth path.

The nation's largest metro area, around New York, has performed relatively well. Despite Wall Street layoffs, job losses overall have been relatively modest, and home prices have begun to recover from declines early this year. The diversity of that region's economy, together with the high education levels of its workers, leave New York and similar structured metro areas such as Boston and San Francisco better poised for recovery than those that had relied heavily on housing or manufacturing for growth.

Beyond the economy, the surge of public satisfaction with the president, with Congress and with "the way things are" recorded in the first half of the year has retreated. These indicators remain twice as high as a year ago, at the height of the crisis, but the noticeable decline in the president's approval among independents, and the growing gap between how Republicans and Democrats view the presidency, are signs to watch.

The conflicts in Iraq and Afghanistan, with climbing fatalities, contribute to national unease. Though troop levels have begun to decline in Iraq, they have nearly doubled in Afghanistan. As the country looks to the final quarter of the president's first year in office, Americans seem to be asking not only "how are we doing" but also "where are we going?"

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