

Perna's Perspective

by Nicholas S. Perna, PhD

"Mr. Corleone is a man who insists on hearing bad news immediately."

I couldn't resist quoting Tom Hagen (Robert Duval) in that great scene from *Godfather I* where the movie producer has just refused Don Corleone's request to give singer Johnny Fontaine the starring role in a movie. The next morning the movie mogul wakes up with the horse head in his bed. I am going to report some good news, but have to get November jobs data out of the way first.

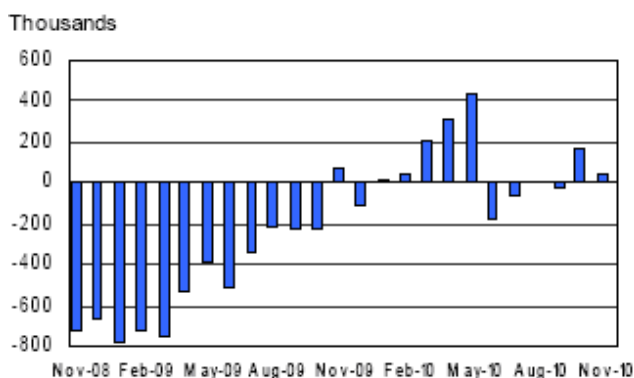
Jobs: Going Nowhere Slowly

Based on a variety of clues, the experts were betting that nonfarm payroll jobs rose about 140,000 in November. The actual gain was a mere 39,000. And with workweek hours and hourly earnings also flat, there was very little improvement in weekly paychecks. Unemployment rose to 9.8 percent from October's 9.6 percent – just a bit below the recession peak of 10.1 percent reached in October 2009.

The labor market data are the most important of all the economic indicators. They tell what is happening to real people on a timely basis just a few days after the month has ended. Not only is the real GDP more of an abstraction to most people, but it comes out quarterly with a one month lag. The jobs and related data give important information about trends in incomes and household purchasing power since employee compensation is almost 65 percent of total personal income. The data affects consumer confidence and can have a major impact on financial markets.

Ben Bernanke has expressed concern over whether the kind of slow recovery we have been experiencing is sustainable. If you've ever flown a plane, the analogy is whether the economy is close to the "stall speed" where the forward momentum is not sufficient to keep the craft aloft. This is a major reason for the controversial Quantitative Easing program that was recently expanded by the Fed. It is also justification for some additional short-term stimulus such as the newly proposed payroll tax holiday.

Nonfarm payroll employment over-the-month change, seasonally adjusted, November 2008 – November 2010



Vehicle Sales: Picking Up Speed

The automotive sector has been a bright spot. Sales of new cars and light trucks climbed 17 percent in November from levels a year ago. Since the bottom of the recession, the improvement has been even more dramatic. Economists like to look at the monthly SAAR, or seasonally adjusted annual rate of sales. Simply stated, the SAAR tells what sales would be if the monthly pace continued for an entire year. At the worst of the recession, sales averaged about 9.7 million units during the early months of 2009, compared with 12.4 million during October

and November of 2010. Although the most recent sales are well below the 17-18 million vehicles sold during the boom years just before the financial meltdown that started in 2007, this is a very decent recovery of about 30 percent. We should easily get another 10 percent rise in 2011 – provided that the economy doesn't stall.

Why so good? There's a huge replacement demand for vehicles since millions of cars have worn out since the boom years. Prices of new cars are rising, so there's little incentive to postpone buying. The industry is doing well as evidenced by the warm reception given to General Motors IPO in its bid to recapitalize following bankruptcy. GM and most other U.S. firms have dramatically lowered their breakeven points through cost reductions. This means they can be profitable at much lower volumes of sales than in the past. It also helps to have shed debt and other costly obligations through bankruptcy.

Washington: Potentially Good News

As of this writing (12/7/10), things have taken a turn for the better in Washington with the announcement of an agreement between the White House and Congressional leaders to extend the Bush tax cuts and jobless benefits for the long term unemployed. There's also an extra kicker from the inclusion of a temporary reduction in payroll taxes. Of course, all this still has to pass the House and the Senate.

Implications

The Fed won't start raising short-term rates until there is tangible progress in generating jobs and reducing unemployment. Best bet is that this won't start for another year or so. The bond market is a different story. Yields have been rising in recent weeks, reversing the decline in response to QE2. Nobody's quite sure why. I think the yield on the 10-year will move unevenly upwards by a hundred basis point or so to the vicinity of 4 percent a year from now as the Fed scales back on Quantitative Easing. Mortgages will move more or less in lockstep.

Car sales are on an upward trajectory – provided we get a bit better jobs picture. As I mentioned at the Economic Forums in Illinois and New York, auto loans are a growth opportunity for credit unions during the coming year.

Seasonally Adjusted Greetings!



Nick Perna is Resident Economist, Members United Corporate. He specializes in economic analysis, forecasting and strategy. Dr. Perna has served as an economist for the Federal Reserve Bank of New York, General Electric and a number of major banking institutions. The *Wall Street Journal* and *BusinessWeek* have each twice cited Dr. Perna as one of the top economic forecasters in the United States. He has served as an economics professor at Williams College and New York University, and currently teaches an economics course at Yale University. In addition, he has also appeared on *The NewsHour with Jim Lehrer*, CNN, CNBC, the *NBC Nightly News*, ABC Radio and NPR's *All Things Considered*.