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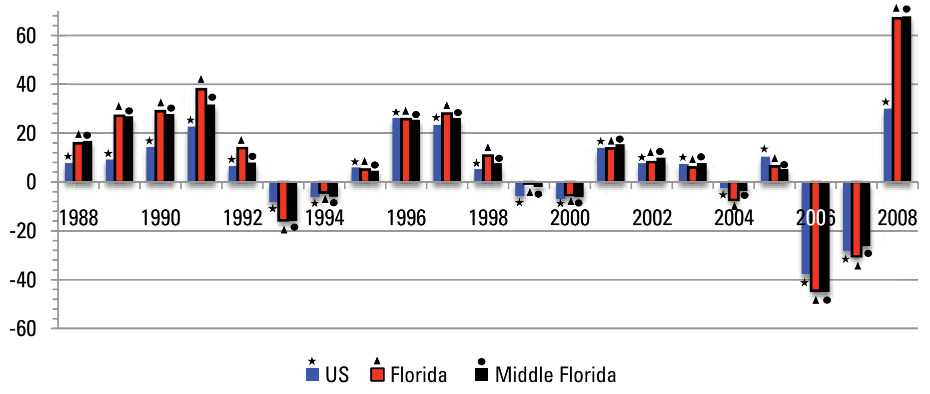
the tampa bay economy

THE DARK SIDE OF THE GREAT RECESSION

by Brian T. Kench, Ph.D. and Jeffery R. Donaldson, Ph.D., CFA

Annual Percentage Change in Chapter 7 & Chapter 13 Bankruptcy Filings
Source: www.uscourts.gov



Bad things happen to otherwise good people during recessionary periods. As the current downturn drags on, two economic indicators are tell-tales of the devastating human tragedy occurring on the dark side of the Great Recession. The first is the unemployment rate and the second is the residential bankruptcy rate.

Changes in the unemployment rate offer one of the most important indicators of the improving, or declining, health of the economy. The national unemployment rate has increased from a low of 4.4 percent in March of 2007 to 10 percent last November. In the state of Florida, it has increased from its low of 3.3 percent in March of 2006 to 11.5 percent last November. And in the Tampa-St. Petersburg-Clearwater MSA, it has increased from its low of 3.1 percent in April of 2006 to 12.3 percent last November. These elevated rates of unemployment signal the continued fragile state of the national and local economies.

In the Tampa-St. Petersburg-Clearwater MSA, for example, 105,100 jobs have been lost since the beginning of the recession in December of 2007, and many more lives have been turned upside-down because of the turmoil that comes with the devastation of unemployment. After the 1990-91 and 2001-03 recessions, the year over year percentage change in nonfarm payroll jobs in the Tampa Bay area continued to decline for 1 and 2.5 years, respectively. This time around, the duration of the decline and its aftermath are likely to be worse.

One consequence of the lengthy downturn in the job market is the constraint it imposes on consumer spending, which accounts for around 70 percent of gross domestic product or GDP each year. The problem is that each job loss decreases consumer income. Each $1 lost in consumer income decreases consumer spending by 70 cents, which in turn increases the likelihood of another job loss. It is this self-reinforcing process, which occurs in all recessionary periods, that generates continued negative pressure on GDP.

The newly unemployed typically tap into federal and state assistance programs. Nearly 5.5 million Americans have received unemployment insurance during the Great Recession and one in eight Americans was on food stamps as of early December 2009. The unemployed and underemployed also tap into their savings, borrow funds from family and friends, and use credit cards and home equity lines of credit, all in an effort to survive their spell of unemployment. As the recession drags on, typical federal and state sources of survival can and do expire. As we pass the second anniversary of the beginning of the Great Recession, one in eight mortgages is in default or foreclosure. Many unemployed

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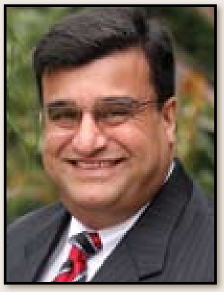

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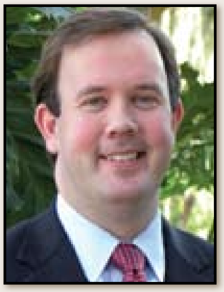

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TAMPA BAY ECONOMIC ANALYSIS

by Brian T. Kench, Ph.D.

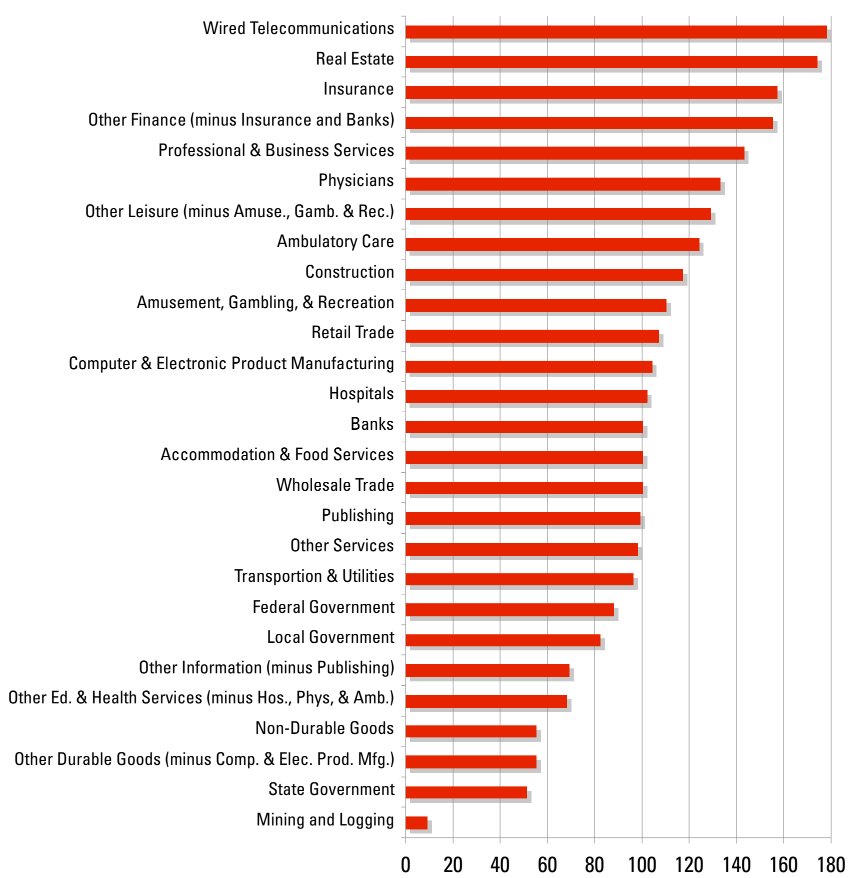
The Tampa–St. Petersburg–Clearwater Metropolitan Statistical Area (hereafter, TSC-MSA) is comprised of Hernando, Hillsborough, Pasco and Pinellas counties. The area has shown continued weakness as it adjusts to declining home values, increasing unemployment rate and the anemic national output.

Our analysis of the TSC-MSA employment share by sector relative to the United States highlights the sectors in which we specialized in 2008. The analysis has neutralized common macroeconomic events in the dataset by comparing local sector shares to national sector shares. The analysis reveals that the top sectors in the TSC-MSA are wired telecommunications, real estate, insurance, other finance, professional and business services, physicians, other leisure, ambulatory care, construction, and amusement, gambling, and recreation.

Annual Percentage Change in Nonfarm Payroll Jobs: TSC-MSA
Source: US Department of Labor

Industry	10/03-10/04	10/04-10/05	10/05-10/06	10/06-10/07	10/07-10/08	10/08-10/09
All Nonfarm Payroll Jobs	4.8	2.3	1.4	-1.1	-2.7	-4.8
Wired Telecommunications Carriers	-0.8	-7.1	-1.7	-4.3	-8.2	-4
Real Estate	5.1	7.5	-1.2	0	-4.6	-3.1
Insurance	2.8	6.7	0.09	0.9	0.6	-0.6
Finance	1.8	3.9	2.4	-2.2	-2.5	-3.1
Professional and Business Services	12.5	1.6	1.8	-2.3	-3.5	-7.2
Education and Health Services	2.7	1.3	3.2	4.9	1.5	1.9
Leisure and Hospitality	3.7	2.6	1.8	-1	-3.2	-2.2
Construction	13.5	9.4	3.6	-11.4	-11.4	-15.3
Retail Trade	1.8	3.9	0.1	-0.3	-2.3	-6
Computer and Electronic Product Mfg	0.8	-4	0.8	3.3	-4.2	0
Banks	-0.6	2.2	4.6	-5.5	-7.2	-5.7
Wholesale Trade	2.4	3.5	2.5	-0.2	-3.3	-12.1
Publishing	-2.4	2.5	3.6	0	-17.4	-4.2
Federal Government	4.6	2.9	0	1.9	1.9	2.3
State Government	-3	4.9	4.3	0	-0.4	2.5
Local Government	1.2	-0.8	1.6	1.1	0.7	-4.4

TSC-MSA 2008 Employment Share By Sector Relative to the United States
Note: United States = 100



The nearby table reports that several of the sectors in which the TSC-MSA specializes have seen the harshest annual percentage declines. The October 2008-over-October 2009 percentage change in jobs were worst in construction (-15.3 percent), wholesale trade (-12.1 percent), professional and business services (-7.2 percent), and wired telecommunication carriers (-4 percent). Job gains were greatest in state government (2.5 percent), federal government (2.3 percent), and the education and health services sector (1.9 percent). Each of these growth sectors benefited from federal stimulus funds.

In the third quarter of 2009, seasonally adjusted nonfarm payroll jobs in the TSC-MSA decreased by 11,900 or 1 percent. The TSC-MSA's percentage decrease is 2.4 times the decrease the state of Florida experienced and twice the decrease the nation experienced in the third quarter.

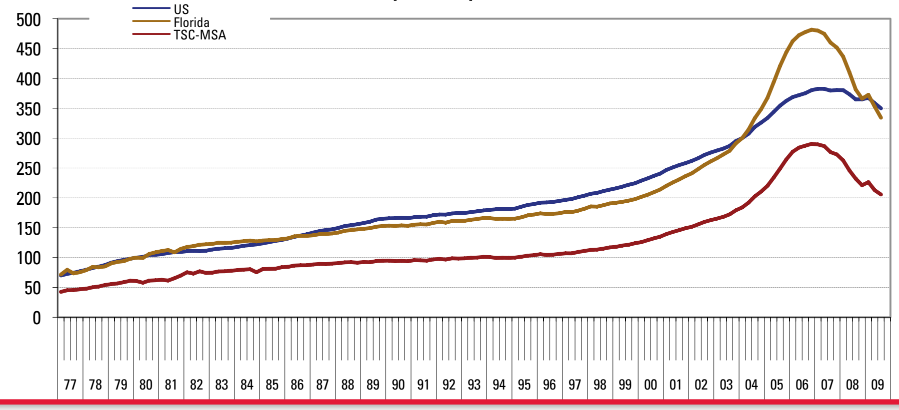
The annual percentage change in nonfarm payroll jobs continued to decrease, in the TSC-MSA, for one year after the 1990-91 recession and 2.5 years after the 2001-03 recession. We forecast that it will take several years for annual percentage change in nonfarm payroll jobs in the TSC-MSA to return to the level observed prior to the Great Recession.

The unemployment rate in the TSC-MSA was 12.3 percent in November of 2009, which is higher than the national unemployment rate by 2.3 percent. The unemployment rate in Hillsborough County was 12.1 percent, which is 0.2 percent below the unemployment rate for the entire MSA. Historically, the unemployment rate is a lagging economic indicator. Thus, we forecast that it will continue to increase as the national and local economies exit the current recessionary period.

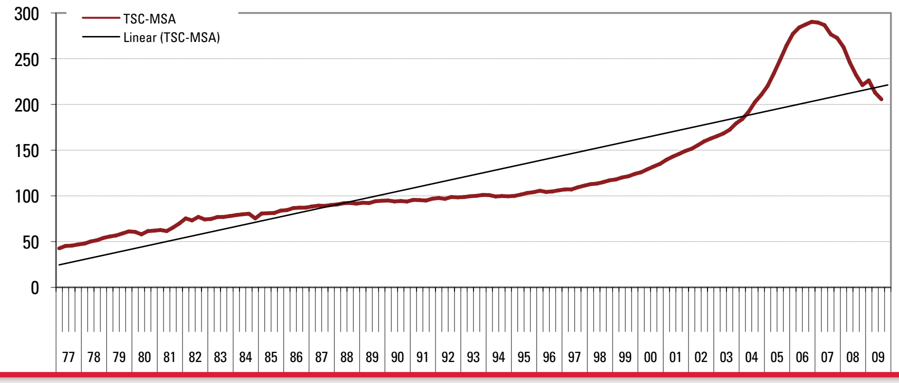
The FHFA housing price index (HPI) for the TSC-MSA has decreased 3.5 percent in the third quarter of 2009. The TSC-MSA HPI has now declined 29.2 percent from its peak in the fourth quarter of 2006; the HPI for the state of Florida has declined 30.6 percent from its peak in the fourth quarter of 2006; and the national HPI has decreased 8.5 percent from its peak in the first quarter of 2007. We continue to expect a stabilization of these indexes over the coming quarters.

Overall, the TSC-MSA economy continued to slow in the third quarter of 2009. Our 2010 forecast for the TSC-MSA shows that the area should reach the trough of the current business cycle, with unemployment rates to rebound subsequently.

FHFA Housing Price Index: US, FL & TSC-MSA*
1/1977-9/2009



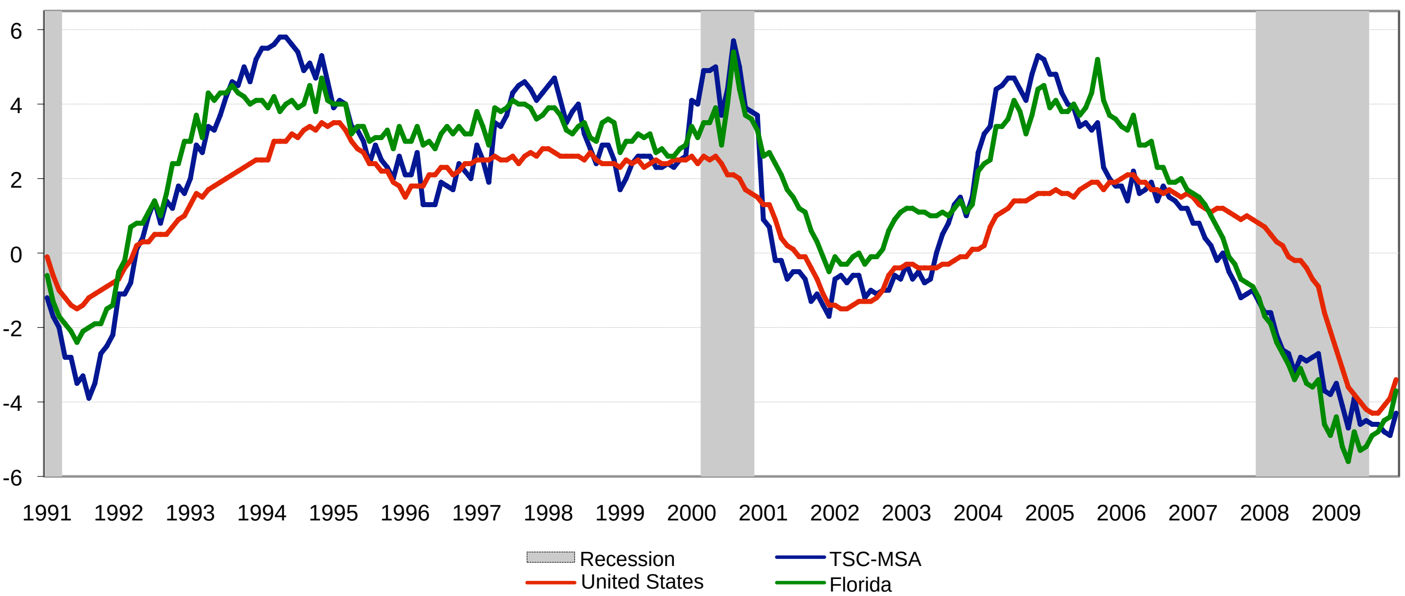
FHFA Housing Price Index: TSC-MSA*
1/1977-9/2009



* The Federal Housing Finance Agency's Housing Price Index (HPI) is a broad measure of the movement of single-family house prices. The HPI is a weighted, repeat-sales index, meaning that it measures average price changes in repeat sales or re-financings on the same properties. The index is based on transactions involving conforming, conventional mortgages purchased or securitized by Fannie Mae or Freddie Mac.

Nonfarm Payroll Jobs Annual Percentage Change (not seasonally adjusted) 1/2001-11/2009

Source: US Department of Labor



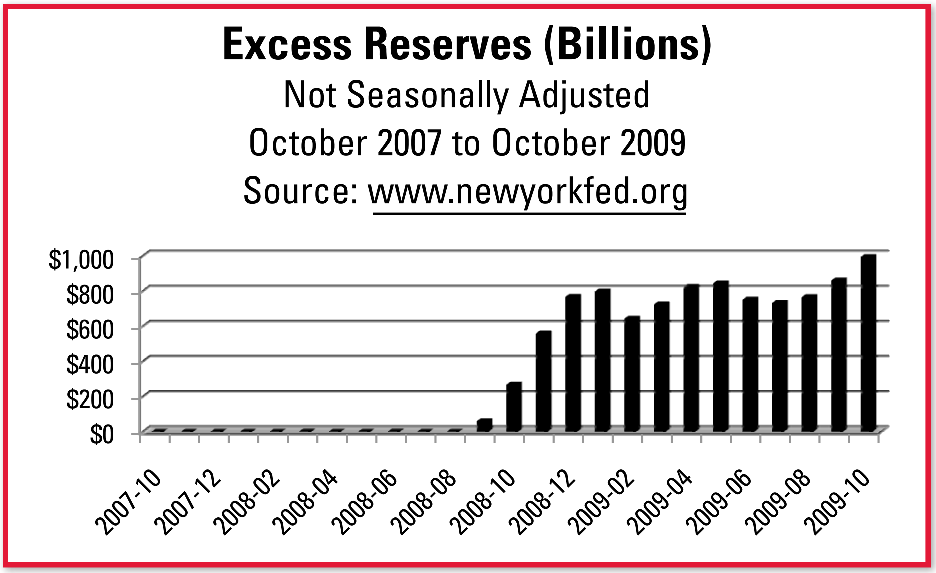
MONETARY AND FISCAL POLICY DURING THE GREAT RECESSION

by Brian T. Kench, Ph.D.

I will begin with a story first told in a 1970s academic journal in economics. Once upon a time, there was a babysitting cooperative in Washington, D.C. The Co-op issued coupons for its members to use as currency as they traded babysitting services with each other. As the story goes, a funny thing started to happen to the co-op. Members started to save their coupons for a special night out. The problem was that when one couple saved their coupons, another couple was denied the opportunity to earn coupons. Which, of course, caused others to save their coupons. In short, the babysitting co-op economy went into a recession. Sometimes, bad things do happen to otherwise good economies.

The co-op had a few economists in its membership. They eventually had their voices heard and more coupons were printed and randomly distributed. As the number of coupons in each member's pocket increased, they were more willing to actually use them to go out. As the demand for babysitting services increased, more coupons cycled throughout the co-op. The gross babysitting product or GBP began to increase, and the recession ended. The take away point of this story is that this recession had everything to do with a lack of coupons.

What does this babysitting co-op have to do with our Great Recession? Economists have discovered that during recessionary periods the psychology of economic actors can be boiled down to a lack of confidence — a fear that you don't have enough coupons. However, fear is a self-reinforcing process. As people hoard coupons, because they fear that they'll run out, fewer coupons actually circulate, which in turn causes people to hoard more coupons. In this environment, stimulative monetary policy can limit the extent of a recessionary period by increasing liquidity. Rather than issuing babysitting coupons to increase liquidity, the U.S. Federal Reserve Bank, or the Fed, typically increases liquidity by lowering key interest rate targets.



The Fed's actions make the average consumer feel as if they have more money and it enhances their desire to increase economic activity, which begins to pull the economy out of the recessionary period.

One major problem in the Great Recession, however, was that the Fed had already decreased the federal funds rate, one of its key interest rate targets, as much as they could and economic activity was not responding. Because of this constraint, non-traditional methods were used by the Fed to increase liquidity. For example, the Fed began buying mortgage backed securities guaranteed by Fannie Mae, Freddie Mac, and Ginnie Mae and debt issued by Fannie, Freddie, and the Federal Home Loan Banks. Current plans call for the Fed to buy $1.25 trillion in mortgage-backed securities and $200 billion in debt. In March through October of 2009, the Fed bought nearly $300 billion in long-term Treasury securities. And these are just a few of the non-traditional actions adopted by the Fed. Nevertheless, each of these actions increases liquidity because when the Fed buys an asset, it pays for it with money that was not previously in circulation. More important, the Fed has a longer time horizon than the private market. For example, the Fed is willing to hold onto a mortgage-backed security for 30 years if such action is needed.

Despite these aggressive actions, the nearby figure of average monthly excess reserves highlights the Fed's problem. Excess reserves equal the amount banks reserve over and above the amount required by the Fed. As the Fed injected liquidity into the financial system, financial institutions did very little with the money because they remained fearful. Excess reserves increased from a non-seasonally adjusted monthly average of $1.7 billion between October of 2001 and September of 2007 to a monthly average of over $994 billion in October of 2009. Thus, despite the massive amount of liquidity pumped into the financial system, institutions remain fearful and are reluctant to use excess reserves.

The Fed's movement towards alternative monetary policy and the subsequent build up of excess reserves have led some to argue that monetary policy is ineffective. However, Larry Ball, a professor at Johns Hopkins University and visiting scholar at the Fed, reminds us that even in normal times monetary policy has a lag. Typically, the maximum impact is felt between 22 and 27 months after the Fed acts. When we think about the injections of liquidity last fall and the ones that are ongoing, let us not forget that it takes at least two years for monetary

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The Dark Side of the Great Recession

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and underemployed are looking at filing for bankruptcy as the next rational step.

If events do force a bankruptcy filing, individuals must make the painstaking decision to file under Chapter 7 or Chapter 13. The benefit of filing under Chapter 13 is that the law allows you to hold onto certain valuable assets, such as your home. If assets are saved, the court develops a plan that enables the filer to catch up with past due debt payments over a three to five year period. However, if your economic hardship continues, and you fail to make payments under the plan, your home would be placed into the foreclosure process.

The majority of bankruptcy cases are filed under Chapter 7 because both secure and unsecure debts may be discharged. A home is an example of a secure debt and your credit card balance is an example of an unsecure debt. Once debts are discharged, you are no longer legally responsible to make payments. As the Supreme Court wrote, this bankruptcy option "gives to the honest but unfortunate debtor…a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt." Local Loan Co. v Hunt, 292 U.S. 234, 244 (1934).

Conventional wisdom was that the opportunity to discharge all of one's debts was a vehicle for abuse. Thus, the Bankruptcy Abuse Prevention & Consumer Protection Act of 2005 (BAPCPA) imposed additional monetary restrictions on bankruptcy filings to prevent potentially abusive Chapter 7 filings. However, a 2008 study, "Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors," published by the *American Bankruptcy Law Journal* analyzed bankruptcy filings from before BAPCPA, in 2001, and from after BAPCPA, in 2007, and found no income differences in the pool of filers. Rather, families that filed in 2007 owed more debt, particularly more credit card debt, than their counterparts from 2001, and families had a much harder time paying down their debts. Because of the changes made to the bankruptcy law, "Americans are struggling harder than ever before they collapse into bankruptcy…This is a result Congress neither intended nor promised."

While we now know that debt to income ratios are higher for the most recent filers, do we know who is collapsing into bankruptcy and why they find themselves in this situation? A study, "Medical Bankruptcy in the Unites States, 2007: Results of a National Study," published by *The American Journal of*

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Monetary and Fiscal Policy...

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policy to alter behavior in the real economy.

Because of rising unemployment rates in communities around the country and because of the slow nature of stimulative monetary policy, Congress decided to join the fray and use fiscal policy to stimulate the economy. In terms of our co-op story analogy, the government has decided to not only be the issuer of coupons, but to also become a member in good standing of the co-op. As a member, it changes the co-op in two ways: first, it offers new babysitting opportunities, which is the co-op's version of government spending; and second, it mandates a decrease in the price of babysitting services, which is the co-op's version of decreasing taxes.

Residents of the Tampa Bay area have been affected by both of these fiscal stimulus levers. First, let's take a peek at the increases in federal government spending. All Tampa Bay city governments have received monies for direct fiscal relief. In addition, local non-profits, such as the Boys & Girls Club of Tampa Bay ($42,500), All Children's Hospital ($633,749), and The University of Tampa ($87,321), and local for-profits, such as TECO ($97,850) and Kinder Morgan Liquids Terminals ($170,142), have received funds for qualifying projects. Second, consider a few of the 2009 tax law changes. Working individuals each received a maximum tax credit of $400, first time home buyers are eligible for a tax credit of up to $8,000, buyers of certain 2009 vehicles received cash for the clunker that they traded-in, and buyers of new energy efficient products will receive a maximum tax credit of $1,500.

I think it is fair to say that most economists agree with the direct effect of government spending or the reduction of taxes when the economy has a lot of slack and is operating below its potential output level: it increases economic activity. Indeed, in an environment where 1) productive activities are needed, say a new road, 2) there's an excess supply of building labor, and 3) input prices are relatively low, then the government might be able to play matchmaker. It is simply good economics to build a road today for a lower total cost than it would cost to build the road tomorrow, when input costs are higher.

Moreover, if the government were to transfer tax revenue back to individuals and businesses, these economic actors do have the incentive to engage in productive activities, which would generate an increase in aggregate demand. The positive feedback loop is similar: as the demand for goods and services increases, jobs are created; as jobs reappear, the demand for additional goods and services increases, and so on.

In both cases, if the economy grows because of stimulative fiscal policy, the tax base also expands. All else equal, a larger tax base will decrease the individual burden of paying back the government's debts.

Disagreement among economists exists, however, over the magnitude of the increase in economic activity that occurs because of stimulative fiscal policy. Economists use the term "multiplier-effect" to help discuss the effectiveness of fiscal policy. A recent study by Christina Romer, head of the Council of Economic Advisors to the President, and UC Berkeley economist David Romer found that each $1 decrease in taxes increases economic growth by $3. Additional research by UC San Diego economist Valerie A. Ramey estimates each $1 increase in government spending increases economic activity by $1.40. Given this evidence on the effectiveness of the two fiscal policy levers, then the country might place a bit more weight on the tax-reduction lever than on the spending-increasing lever — if we are going to use fiscal policy as a supplement to monetary policy.

The Dark Side of the Great Recession

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Medicine tells us that in 2007 those who file for bankruptcy are middle aged, with a mean age of 44.4 years, they consider themselves middle class, 61.9 percent of filers have gone to college, two-thirds of them are homeowners, and two-thirds had health insurance. When asked about specific reasons for filing for bankruptcy, 62.1 percent of those who claimed bankruptcy cited a medical cause.

Indeed, between 2001 and 2007, the share of bankruptcies attributable to medical problems increased by 50 percent. This phenomenon is exacerbated when companies go out of business, which occurs a lot during recessionary periods. Current federal law denies former employees access to COBRA benefits when there is no longer an underlying firm to support the plan. Worse, individual private insurance plans can be difficult and expensive to obtain, especially if you have a pre-existing medical condition.

The nearby figure shows that there is a new and disturbing spike in bankruptcy filings in the U.S., Florida, and the middle district of Florida, which includes 57 percent of the state's population, with 35 of the state's 67 counties included. In 2008, Chapter 7 and Chapter 13 filings increased 30 percent nationally, 67 percent in Florida, and 68 percent in the middle district of Florida. By June of 2009 the annual rate of filings was 35 percent nationally, 58 percent in Florida, and 52 percent in the middle district of Florida.

A different bankruptcy lever is being pushed in the Great Recession. This increase in bankruptcy filings appears to be driven more by real estate related issues and unemployment than by medical issues and changes in governmental bankruptcy legislation.

The good news is that the stock market has increased 50 percent from its bottom in March 2009, perhaps an indication that the worst of the global recession is behind us. The question now becomes how long will the economic recovery take? Leading economic indicators are improving along with recent corporate profits. However, corporate profits have increased more from a reduction in labor costs, because of layoffs, rather than a top-line increase in sales. In the end, high unemployment and bankruptcy rates mixed with a labor force that finds it difficult to relocate because their homes are underwater, are ingredients for a recovery that is slower and longer in duration then we all would prefer.

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