



ERIE

**Economic Research
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ELI Erie
Leading
Index

2ND QUARTER 2017 REPORT



ELI Refuses to Give Up Its Sparkle as It Basks in the Summer Sunshine.

**ELI Shows Resilience by
Increasing for the Fourth
Consecutive Quarter,
But Employment Growth
in the Local Economy
Remains Lethargic**

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ELI Continues Slowly On Upward Path, But Job Growth Remains a Major Challenge for the Local Economy

For the fourth consecutive quarter, the Erie Leading Index (ELI) has shown gradual improvement, rising by a modest 0.7% through the first three months of the year. ELI has not decreased since the 1st quarter of 2016 and is currently basking gently in the warm summer sunshine. That's good news, since changes in ELI's direction of movement can signal upcoming turning points in the local economy. Let's hope that the rising summer temperatures will provide ELI with a sustained and perhaps more robust upward lift.

Unfortunately, as in the past three quarters, ELI's restrained growth is a reflection of the continued weakness in the local labor market. The latest statistics from the Pennsylvania Department of Labor and Industry indicate that, on a seasonally adjusted (SA) basis, Erie's total nonfarm employment fell by 0.1% (100 jobs) to 128,600 in May compared to a year ago. Although the total (SA) number of nonfarm jobs in Erie increased by 0.3% (400 jobs) between April and

May, many industries in the local economy experienced job cuts during the past year, with the largest percentage job losses year-over-year in May occurring in the following sectors: Information (-8.3% or 100 jobs); Professional and Business Services (-3.9% or 400 jobs); and Manufacturing (-3.5% or 700 jobs).

Erie's manufacturing sector continues to experience employment setbacks, even after the relatively large number of job losses in 2016. Between March and May of this year, employment in the manufacturing sector shrank by 1.0% (200 jobs).

All of these statistics confirm that job growth is among the foremost challenges for the region's economy. This remains a daunting challenge, especially as the region must also continue to adapt to rapidly changing global, technological, and demographic trends.

There is some good news, however. A few sectors of the local economy did manage to add jobs during the

past twelve months. Year-over-year in May, employment grew by 3.5% (1,000 jobs) in the education and health services sector, by 2.0% (200 jobs) in the local government sector, and by 1.6% (100 jobs) in the financial activities sector. And since March of this year, employment has expanded by 14.2% (1,900 jobs) in the leisure and hospitality sector, by 13.9% (500 jobs) in the mining, logging, and construction sector, and by 3.0% (100 jobs) in the transportation, warehousing, and utilities sector. With the summer weather and tourist season approaching, the positive job trend is likely to continue for leisure and hospitality as well as for construction.

But these job gains were not sufficient to prevent Erie's seasonally adjusted unemployment rate from rising to 6.1% in May from 6.0% in April. In contrast, the May seasonally adjusted unemployment rate continued to be lower in Pennsylvania (5.0%) and in the nation as a whole (4.3%).



*Data through March 2017

Components of ELI

Variable	Dec.	Jan.	Feb.	March	Dec.-Mar.	% Change*	Weights
ERIE Leading Index	100.98	101.06	102.06	101.65	0.67	0.67	1.000
U.S. Interest Rate Spread (%)	2.0	1.8	1.8	1.7	-0.26	-13.33	0.333
U.S. Index of Coincident Indicators (2004=100)	114.5	114.5	114.7	114.9	0.40	0.35	0.263
U.S. Real Money Supply (M2) (bill of chained 2009 \$)	11,811.2	11,832.8	11,857.1	11,955.4	144.20	1.22	0.143
PA Avg Weekly Hours in Manufacturing (hours)	41.6	42.1	41.7	40.6	-1.01	-2.44	0.087
Erie Manufacturing Employment (thou of jobs)	19.4	19.5	19.6	19.6	0.23	1.18	0.074
U.S. TS Freight Index (2000=100)	124.6	124.0	125.9	124.0	-0.60	-0.48	0.058
S&P 500 Stock Index (1941-43=10)	2,246.6	2,275.1	2,329.9	2,366.8	120.19	5.35	0.025
U.S. Building Permits (thou of units)	1,228	1,293	1,216	1,260	32.00	2.61	0.017

*Symmetric % change, using the average value of the series in the last quarter as the base. *Changes may differ from hand calculations due to rounding.

Despite the weakness in the local labor market, ELI still rose modestly by 0.7% between December and March as five of the eight components that make up the composite index grew.

This quarter, the component that registered the largest increase was the S&P 500 Stock Index, which rose by 5.4%. Despite some volatility amid the debate and resulting uncertainty over fiscal, trade, regulatory, and other federal government policies, U.S. stock markets have remained fairly buoyant this year. Both the Dow Jones industrial average and the S&P 500 reached record highs. If the markets can sustain this momentum, ELI will be in for a nice boost.

A second reason for ELI's rise this quarter was the growth in the number of U.S. Building Permits. After falling by 1.2% last quarter, building permits rebounded with 2.6% growth. With nicer weather conditions ahead, and assuming the national economy maintains a healthy growth trajectory, this component is likely to remain strong.

Further contributing to ELI's rise this quarter was U.S. monetary policy, which continued to be slightly expansionary. The U.S. Real Money Supply, another component of ELI, increased by 1.2% in the first quarter. However, this was lower than the 2.0% increase during this time a year ago, reflecting a gradual monetary tightening by the Fed as it strives to meet its "dual mandate" of promoting maximum sustainable employment and price stability in the national economy. With U.S. unemployment close to the Fed's estimated long-run "normal" rate of 4.6% and with core inflation in 2017 expected to be below the Fed's target of 2%, the Fed is gradually raising its benchmark federal funds interest rate (most recently in mid-June) to help achieve both of its overarching goals.

While it has been very gradual so far, future monetary tightening by the Fed will be an important factor to watch since the restraining effect it is likely to have on the U.S. economy may also possibly generate adverse spillover effects on the local economy.

Another factor that helped boost ELI in the first quarter was a slight (1.2%) increase in Erie Manufacturing Employment, based on seasonally adjusted statistics through March.

The component with the biggest negative effect on ELI this quarter was the U.S. Interest Rate Spread, which shrank by 13.3%. This narrowing of the spread, which measures the difference between the 10-year Treasury bond yield and the short-term federal funds rate, partly reflects the Fed's monetary tightening. It is also something to watch because a negative interest rate spread may signal the possibility for an economic downturn. Other components that had a negative effect on ELI this quarter were Pennsylvania Average Weekly Hours in Manufacturing, which fell by 2.4%, and the U.S. Transportation Services Freight Index, which fell by 0.5%.

Let's hope ELI won't fizzle when the summer starts to sizzle!

Trends and Implications for Different Sectors of the Erie Economy

Goods-Producing Sectors

Mining, Logging, and Construction:

Employment in this sector increased by 13.9% (500 jobs) between January and May, and currently stands at 4,100. Although this is the same number of jobs recorded in the sector a year ago, the warmer summer and fall seasons are likely to bring about more job growth. This sector may also be affected by future shifts in U.S. fiscal, regulatory, and environmental policy.

Manufacturing:

This sector continues to struggle in terms of job growth. After rising slightly between January and March, the number of jobs fell by 1.0% (200 jobs) in April and currently stands at 19,200, which is 3.5% lower compared to a year ago. Ongoing changes in technology as well as possible shifts in government policy are likely to have major effects on this sector.

Plastics & Rubber Products Mfg:

Employment in this sector remains stable, with no growth during the past year. After rising slightly between January and February, the number of jobs has held steady at 4,400 from February to May. Just as for the manufacturing sector overall, changes in technology and government policy can affect this sector.

Private Service-Providing Sectors

Wholesale Trade:

The number of jobs in this sector has been fairly steady, fluctuating between 3,700 and 3,800 in the first five months of the year. As of May, however, employment is down by 2.6% (100 jobs) compared to a year ago. Employment in this sector is likely to be influenced by seasonal variation in economic activity, as well as by changes in government fiscal and trade policies that affect global supply chains.

Information:

This broad sector includes these industries: publishing (including software, traditional, and Internet publishing), motion picture and sound recording, broadcasting (including traditional and Internet broadcasting), data processing, and information services. The number of jobs has remained steady at 1,100 over the last five months, but this is down by 8.3% (100 jobs) compared to last year. The sector will continue to be influenced by changes in technology.

Education and Health Services:

Employment in this sector has continued to expand, growing by 2.4% (700 jobs) between January and May. Moreover, the current employment level of 29,400 represents an increase of 3.5% (1,000 jobs) compared to May 2016. Locally, this is again the largest sector (by employment). Changes in U.S. education policy and in educational and biomedical technology, as well as shifting demographics in the local region, are likely to affect this sector.

Retail Trade:

After declining by 5.7% (900 jobs) in January due to seasonal variations in consumer expenditures, employment in this sector has held steady at 14,800 to 14,900 jobs since then. However, employment fell by 2.6% (400 jobs) year-over-year in May. E-commerce, job losses in manufacturing, and government policies that affect household disposable incomes can all influence this sector.

Financial Activities:

Employment in this sector has expanded slightly compared to a year ago, growing by 1.6% (100 jobs) year-over-year in May and remaining unchanged at its current level of 6,300 since January. In addition to technological innovations in data and information processing, this sector is also likely to be affected by changes in government fiscal and regulatory policies that influence financial decisions on the part of individuals, households, and corporations.

Transportation, Warehousing, Utilities:

Similar to Retail Trade, this sector experienced an employment decline of 5.7% (200 jobs) in January due to seasonal variations in economic activity. Since then, jobs held steady at 3,300, then rose to 3,400 in May, the same number compared to a year ago. Changes in U.S. fiscal, trade, regulatory, and environmental policy can affect this sector.

Professional and Business Services:

After dipping by 2.0% (200 jobs) between December and January, this sector bounced back and regained some of those jobs between January and May. However, the current employment level of 9,900 is still 3.9% (400 jobs) below where it was a year ago. As in other sectors such as Financial Activities, this sector can also be affected by changes in government fiscal and regulatory policies.

Leisure and Hospitality:

Seasonal factors continue to play a key role in this sector. Employment fell by 3.7% (500 jobs) between December and February. However, jobs have come roaring back, increasing by 16.8% (2,200 jobs) since February to its current level of 15,300. This represents an increase of 1.3% (200 jobs) compared to May 2016. Jobs are likely to increase with the summer tourist season as well as with the continued development of the Bayfront.

Other Services:

Employment in the Other Services sector has been expanding, rising by 3.5% (200 jobs) in the first five months of the year to its current level of 5,900. However, this represents a year-over-year decrease of 1.7% (100 jobs) compared to May 2016. As with many other parts of the local economy, government policies and other events affecting household disposable income are likely to have an impact on this sector.

Government Sector

State government employment fell by 2.2% (100 jobs) year-over-year in May and stood at 4,400 jobs, while local government employment increased by 2.0% (200 jobs) during the same period and stood at 10,300 jobs. Federal government employment remained unchanged at 1,500 compared to a year ago. Changes in U.S. fiscal, education, and regulatory policy may affect the government sector at all three levels. Employment changes related to the normal course of the school year may also occur, especially at the state and local government levels.



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