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### DECEMBER 2004

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### Analysis

The Oregon economy continued to edge upward in December. The University of Oregon Index of Economic Indicators rose 0.1 percent in December to a level of 105.5 (1996=100), compared to 105.4 in November. Four of the eight indicators that comprise the index—Oregon residential building permits, Oregon nonfarm payrolls, U.S. consumer confidence, and real new orders for manufactured goods—improved in December. Improving indicators outweighed those that deteriorated or held steady, creating a gain in the index.

Indicators of the Oregon labor market remain mixed, although December saw improvement in a key variable. Nonfarm payrolls grew to 1.6 million employees, a gain of 1,700 over November. While the improvement is welcome, note that in the last six months of 2004, payrolls increased by a mere 4,900 workers. In contrast, firms added 29,200 employees in the first six months

of 2004. The weakness in payrolls is not consistent with the improvement of initial jobless claims, which have dropped to pre-recession levels. While the pace of firings has slowed to a more normal rate, firms appear hesitant to step up the pace of hiring.

The spread between the ten-year Treasury interest rate and the Federal Funds interest rate continues to narrow, a negative influence on the index. The narrowing is attributable to interest rate hikes as the Federal Reserve continues its efforts toward normalization of monetary policy. Rates on ten-year Treasury bonds, in contrast, have remained relatively stable. One interpretation of this dynamic is that financial market participants expect that the Federal Reserve will slow national

economic activity sufficiently to maintain stable inflation, but not enough to trigger a recession.

Due to month-to-month volatility of components, a more reliable indicator of economic health is obtained from six-month changes in the index. On that basis, the UO Index stands 0.5 percent (annualized) higher. The six-month diffusion index, a measure of the proportion of components that are rising, fell to 56.3.

The behavior of the index suggests continued economic growth in Oregon. Activity, however, slowed in the second half of 2004, implying that growth in early 2005 will be soft to moderate.

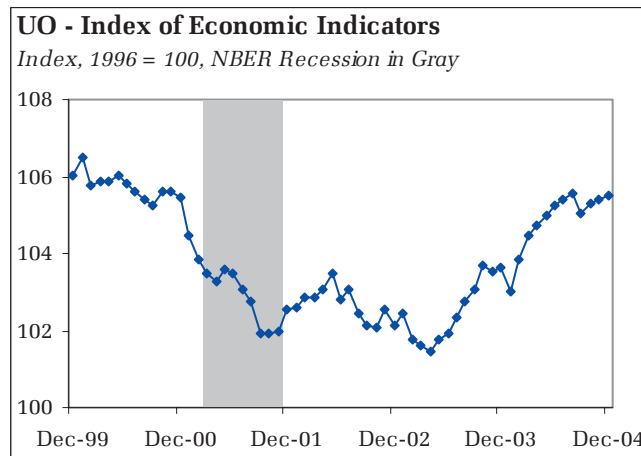


Table 1: Summary Measures

	2004					
	July	August	Sept.	Oct.	Nov.	Dec.
University of Oregon Index of Economic Indicators, 1996=100	105.4	105.5	105.1	105.3	105.4	105.5
Percentage Change	0.1	0.1	-0.5	0.2	0.1	0.1
Diffusion Index	62.5	43.8	31.3	43.8	56.3	50.0
6-month Percentage Change, Annualized	4.7	3.3	1.1	1.1	0.9	0.5
6-Month Diffusion Index	87.5	75.0	43.8	68.8	62.5	56.3



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### Methodology and Notes

The methodology employed in creating the University of Oregon Index of Economic Indicators is identical to that used by The Conference Board, an independent, not-for-profit research organization, in the computation of the U.S. Leading Index. For information, see [www.globalindicators.org](http://www.globalindicators.org).

The UO Index is constructed to have the properties of a leading indicator. As a general rule, a decline in the index of greater than 2 percent over six months, coupled with a decline in more than half of its components, signals that a recession is likely imminent. The 2 percent rule—which has since changed to 3.5 percent due to index revisions—was originally employed by The Conference Board for the U.S. Leading Indicators, and it appears appropriate for the UO Index.

Using the rule, the index signaled an impending recession in January 2001; the National Bureau of Economic Research (NBER) dates the national recession from March to November 2001. The index did signal the so-called “jobless recovery” that followed the 2001 recession, but did not falsely predict a double-dip recession. No other recessions were signaled during the period for which data are available (beginning February 1995).

The general rule, however, should be used judiciously. The available data encompasses only one recession, a very small sample from which to draw generalities. Moreover, no single variable is capable of decisively determining the state of the business cycle. Consequently, the UO Index of Economic Indicators is best considered as another tool in assessing the economy.

Sources: The Conference Board, Oregon Department of Transportation, Oregon Employment Department, Federal Reserve Bank of St. Louis, Bureau of Labor Statistics, Census Bureau, and the author’s calculations.

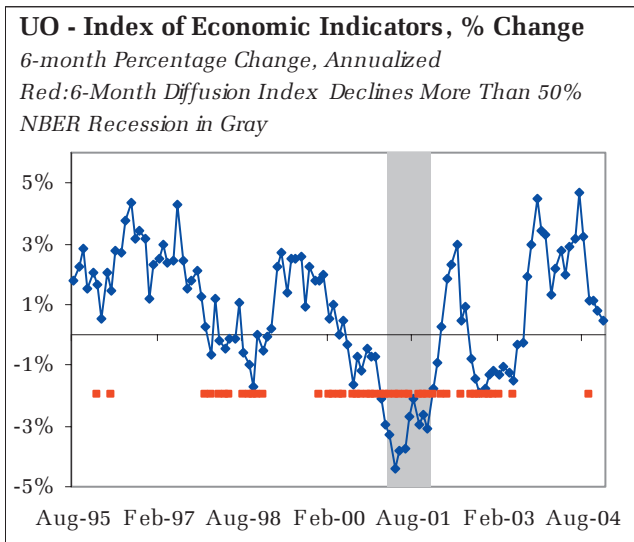
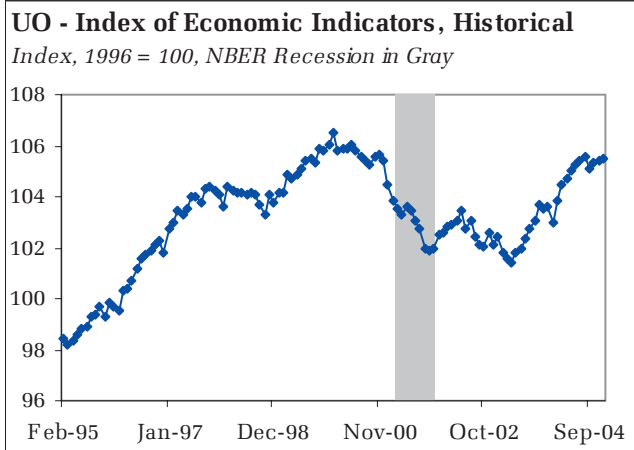


Table 2: Index Components

	2004					
	July	August	Sept.	Oct.	Nov.	Dec.
Oregon Initial Unemployment Claims, SA*	7,265	7,329	6,961	7,092	6,125	6,129
Oregon Residential Building Permits, SA	3,053	2,904	1,977	2,291	2,028	2,600
The Oregonian Help Wanted Ads, SA	18,702	20,988	18,872	23,745	21,017	20,249
Oregon Weight-Distance Tax, \$ Thousands, SA	19,033	22,751	19,496	22,531	24,558	18,996
Oregon Total Nonfarm Payrolls, Thousands, SA	1,599.6	1,599.8	1,602.3	1,601.2	1,600.8	1,602.5
Univ. of Michigan US Consumer Confidence	96.7	95.9	94.2	91.7	92.8	97.1
Real Manufacturer's New Orders for Non-Defense, Non-Aircraft Capital Goods, \$ Thousands, SA	43,276	43,564	45,791	43,787	44,094	44,830
Interest Rate Spread, 10-year Treasury Bonds less Federal Funds Rate	3.24	2.85	2.52	2.34	2.26	2.07

\* SA—seasonally adjusted

The goal of the UO Index of Economic Indicators is to create a summary measure of various data that pertains to the Oregon Economy.