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Fed Economist Predicts Slow Recovery

By Dana Herra dherra@daily-chronicle.com

SYCAMORE – The U.S. economy will continue its recovery over the next two years, but progress will be painfully slow, according to an economist with the Federal Reserve Bank of Chicago.

William Strauss spoke Tuesday at the annual economic outlook luncheon of the DeKalb County Economic Development Corp. Strauss estimated the recession may have technically ended last June.

“We’ll have to wait until next year for the government to tell us that the recession ended sometime last year,” he said. “The economy appears to be growing, although the growth rate is still not all that strong.”

Steep recessions in the 1970’s and 1980’s had recoveries that were almost as dramatic, Strauss said, but recovery from this recession is expected to be more subdued due to factors including lost jobs that are unlikely to come back and tightened lending restrictions. The gross domestic product is estimated to grow by 2.9 percent this year and 3.2 percent next year, about half of what economists would expect to see in such a severe recession.

The economy expanded by 5.7 percent in the fourth quarter of 2009 – about twice the growth rate of an average economy, Strauss said, but still not fast enough to make much more than a dent in the worst recession since World War II.

The country is seeing what Strauss called “the paradox of thrift,” he said as consumers have seen income from investments and capital gains vanish, they have been saving their income at a much higher rate. In the long term, this will be good for the economy, because more money will be available to be spent and interest rates will remain low. But in

the short term, it means consumer spending, which is two-thirds of the U.S. economy, is markedly down.

The way people look at real estate may also be changing, Strauss said. Homes are being viewed less as investments and more as a place to live, so Strauss expects to see families living in smaller homes and owning less property. For about 50 years before the recession, residential investment made up about 4.6 percent of the gross domestic product, he said. In the last decade, it ballooned to more than 6 percent before the housing bubble burst.

“By the end of the 90s, we had pretty much put everyone into a home who should have been in a home,” he said. Then we had this Ponzi-like scheme of putting more and more people into housing who couldn’t afford to be there.”

A sharp drop in new housing starts has reduced the inventory of unsold new homes to about a seven or eight month supply, down from more than a year’s supply, Strauss said. Despite low interest rates and stable home prices, tight lending standards and uncertainty in the labor market have kept many potential buyers out of the market, he said.

Unemployment will continue to be a significant problem for the foreseeable future, Strauss said. Since the recession started the county has shed 8.4 million jobs. Unemployment recovery always lags economic recovery; after the 2001 recession ended, for example, it took a year and a half to replace the lost jobs. Strauss estimated this recession might set new records in the length of time it takes the job market to recover.