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Notes from the Board

1 message

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September 6, 2023

Contrary to expectations of a slowdown, the Massachusetts' economy sped up during the first half of 2023 and a soft landing looks more probable, observes the MassBenchmarks Editorial Board

Today's economy is solid, but Massachusetts needs policies to grow its labor force for greater economic opportunity and competitiveness in coming years



The most recent MassBenchmarks Board meeting began with a review of economic data demonstrating better than expected performance in the economy, notably in terms of payroll jobs and gross domestic product. The growth comes in the face of what are now historically high interest rates designed to dampen inflation. The better-than-expected economy is also pushing the Massachusetts unemployment rate down to record low levels. Growth in real gross domestic product (GDP) in Massachusetts is now outpacing the nation and Massachusetts has become a leading state for net jobs growth. Most major industry sectors are experiencing payroll jobs growth through the first half of 2023, showing that the economic improvements in the state are broadly based.

Somewhat of a surprise is that Massachusetts tax revenues have been coming in below Department of Revenue projections in early 2023. However, this may be due to bonuses and capital gains being negatively affected by relatively poor equity and stock market performance in 2022. The still-elevated U.S. inflation rate is another concern, as progress in lowering inflation has been steady but slow. All told, it is now looking possible that a long-expected recession may be further delayed.

GDP

After declining in the first two quarters of 2022, Massachusetts' real GDP has swung back and has grown faster than U.S. averages in both the fourth quarter of 2022 and the first two quarters of 2023. The unexpectedly strong rebound in state and U.S. economic growth has come despite inflation, slowing economic growth in China, the war in Ukraine, and the lingering effects of the pandemic on production and supply chains. Heading into the latter half of 2023, GDP growth is expected to slow, and may be on course towards a soft landing, rather than an economic downturn. The anticipated slowdown in GDP growth is due, at least in part, from a downward trend in consumer spending as government supports gradually come to an end and pandemic-related savings are drawn down. Indeed, lower motor vehicle sales in Massachusetts in June may be a leading indicator showing a further decline in consumer spending. Current MassBenchmarks estimates see GDP growth hitting a high of 4.0 percent in the second quarter of 2023 and projections show growth moderating to 0.7 percent and 2.0 percent, respectively, in the third and fourth quarters of the year. The U.S. GDP growth is also projected to slow in the second half of 2023 and may even go slightly negative by the fourth quarter.

Employment

Payroll jobs growth continues to be a strong point for the Massachusetts economy. Massachusetts outpaced the U.S. in jobs growth during the second quarter of 2023 with the state growing at an annualized rate of 2.2 percent compared to the U.S. rate of 1.9 percent. Looking at the year-over-year data, Massachusetts and the nation posted payroll employment increases of 2.8 and 2.6 percent, respectively. With the steady growth in employment, Massachusetts finally surpassed its February 2020 pre-pandemic record in March 2023, and as of June the state had 3.77 million jobs, 25,000 more than the previous pre-pandemic peak. Preliminary figures for July from the U.S. Bureau of Labor Statistics show payroll employment growth continuing to be quite robust in the state.

Labor market

Since cresting during the early stages of the pandemic in 2020, the Massachusetts unemployment rate is continuing a downward trend. The June unemployment rate stood at 2.6 percent, down from 3.7 percent in June 2022 and is now significantly below the U.S. rate of 3.6 percent. The declining unemployment rate, while a positive indicator, is due in part to declining labor force size. A modest uptick in the labor force at the start of the year proved to be short-lived. The seasonally adjusted Massachusetts labor force declined by 30,000 between June 2022 to June 2023. More significantly, this represents part of a longer trend that began prior to the pandemic. Since reaching a peak of about 3.846 million in June 2019, the state's labor force has fallen to 3.721 million in June 2023, a net decline of 125,000. The combination of employment growth and labor force decline is contributing to the state's record low unemployment rate and overall tight labor market conditions. Further complicating workforce decline is the aging of the resident population, as more and more baby boomers start reaching retirement ages in the coming years.

Risks

The potential downsides of the Massachusetts economy remain in place, some structural and others more temporal. Housing costs are stubbornly high and likely contributing to out-migration to other states. Although the economy has steadied and grown after the pandemic, there are still some things that have not worked their way through the tumult, such as commercial real estate. There is uncertainty about what a series of defaults would do to the banking sector and financial markets and how this would work its way through the economy. Other risk factors that could have potentially adverse effects on Massachusetts are China's slowdown, Russia's war with Ukraine, and the possibility of a looming federal shutdown in October if a budget is not passed.

Policy considerations

Given the largely positive data for Massachusetts and the diminished likelihood of a full-blown recession, the Board focused on policies that can make the Massachusetts economy more resilient, better able to respond to new growth opportunities, and help to address its chronic pockets of inequality. A unifying theme among Board members is investing in growing the labor force, a rallying point that could guide state policy. For example, providing more affordable housing and childcare, free community colleges, and improving our antiquated transportation infrastructure would help make Massachusetts a more attractive place to live and work. Because immigrants are a primary source of the state's population growth, the Board also favors policies for helping them get plugged into the labor force by providing in-state tuition regardless of their present documentation status, making sure that underrepresented workers have access to apprenticeships and other work-based training needed to work in emerging sectors like clean energy, and by reviewing occupational licensure requirements to ensure that immigrants (as well as professionals in other states) are not facing unnecessary obstacles to employment.

In conclusion, the condition of the Massachusetts economy looks good heading into the latter part of 2023. Current indicators are solid and have defied expectations on the upside for several quarters running. On the downside, the effects of higher interest rates are still playing out while uncertainties in the international economy as well as political polarization in the U.S. continue to be concerns. Even with slower economic growth expected on the horizon, Massachusetts has the assets to better position itself for the future and should not delay in acting now on measures to grow its labor force.

This summary reflects the discussion of the members of the Editorial Board of MassBenchmarks at its meeting on July 31, 2023 and it reflects the economic data available up to that date. It was prepared by Branner Stewart, Senior Research Manager at the UMass Donahue Institute, and was reviewed and edited by the members of the Editorial Board. While discussion among the Board members was spirited and individual Board members hold a wide variety of views on current economic conditions, this summary reflects the broad consensus of the Board regarding the current state of the Massachusetts economy.

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