U.S. EconomyWon't Avoid Global Slowdown



Lawrence S. Davidson

Professor of Business Economics

& Public Policy and Director,

Global Business Information

Business, Indiana University,

Network, Kelley School of

Bloomington

he economic recovery that began in 1991 will continue into 1999, though at a slower pace. The U.S. economy behaved oddly in the last five years, befuddling economists enough to be

called the "new economy" because of its ability to grow rapidly sans rising interest rates and inflation (see **Figure 1**). Strong foreign and domestic demand propelled growth, while a strong dollar, fierce global competition, and rising manufacturing productivity kept inflation at bay.

A world financial and economic crisis ended all that in mid-1998, and will continue to affect the U.S. economy in 1999. U.S exports have contracted while imports continued to grow, leaving the country with what will be its largest trade deficit ever. Consumers dug deep into savings this year and can dig no deeper. Heightened risk in equity markets reduced consumer confidence and spending. The upshot is that spending in 1999 will grow more slowly, despite falling interest rates and a depreciating dollar. Expect GDP to grow by 2% and the unemployment rate to rise to 5%.

Other highlights of the 1999 outlook include:

payroll employment increases by 1 million;

short-term interest rates average less than
4.5%, while long-term rates average 25 basis points lower than the average for 1998;

 lower corporate profits and declining interest rates have offsetting influences on equity markets;

 housing starts average 1.5 million units, while existing home sales reach 4.4 million;

•consumer and business spending will gr ow, but at less than half the growth rates of 1998;

• exports will increase by 2%, but imports will grow by at least twice that rate;

•employment growth in Indiana compared to 1998's increase of approximately 35,000 will be re-

duced noticeably, although the picture will become brighter as the year progresses;

• Hoosier exports will grow by about 3%, largely because of trade to Canada, Mexico, and Europe.

The National Real Outlook

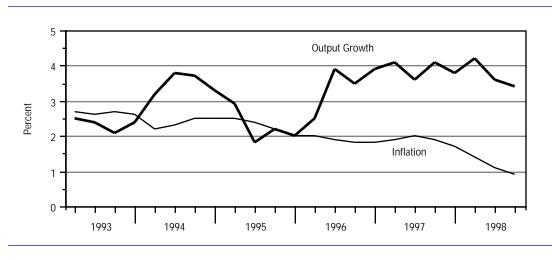
Willard E. Witte

Associate Professor of Economics, Indiana University, Bloomington

During the past year, the U.S. economy has continued its remarkable performance, extending the current expansion into an eighth year. The outlook for the coming year, however, includes some significant potential risks, and we think that a year of sluggish output and employment growth is a prospect.

Figure 1 presents the core of the current situation. The heavy line shows the year-over-year growth rate of real GDP on a quarterly basis; the light line is the year-over-year change in the GDP deflator. Despite a few minor fluctuations, for the most part the U.S. economy has grown at a rate well in excess of 2.5% for the past six years. Since the end of the last recession in 1991 (now over 90 months ago), output growth has averaged 3% per year. For the three-year period ending with third quarter 1998, growth has

Figure 1



U.S. Economy: Year-Over-Year Growth Rate of Real GDP and Change in GDP Deflator