THE ECONOMIC OUTLOOK GROUP

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ECONOMIC TALKING POINTS

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Brace Yourself for Some Awful Job Numbers on Friday

Every economic indicator with ties to the job market is flashing a warning sign about December: Brace yourself!

We expect the upcoming employment report will alarm investors and terrify households. Indeed, we would be somewhat relieved if payroll losses came close to November's 500,000 level. A more likely scenario, we fear, is that jobs plummeted by nearly three-quarters of a million in the final month of the year. Such a huge figure will only perpetuate the vicious downward cycle propelling this economy. As the number of people without jobs accelerates, so will the retrenchment in households spending. And if consumers cut back more, business sales and earnings will shrink further. As profit margins collapse, employers will be under pressure to carry out yet another round of lay offs --- which adds more momentum to the destructive cycle. Unfortunately, that's the scenario we see ahead.

Let's review four recent reports on December job activity.

1. The ADP National Employment Report released today said an unprecedented 693,000 jobs were shed in the private sector last month. It's an ominous number. While the ADP has not had a sterling track record for predicting the government's monthly employment report, the folks at ADP and Macroeconomic Advisers have announced changes in their methodology to bring it closer in line with the Bureau of Labor Statistics survey. We'll soon see if that's true. (In any event, remember the ADP report focuses only on private

sector jobs. On top of their large job cuts, we believe state and local governments were also under pressure to lay off workers last month given the ballooning deficits these municipalities face.)

2. Challenger, Gray & Christmas, a firm that monitors layoffs announcements by companies, reported that employers declared plans to eliminate 166,348 jobs in December. That is the largest job cut ever recorded for that month, and nearly four times more than a year ago.

3. The Institute for Supply Management (ISM) issued its report on December manufacturing activity last week and a key component of that survey is the employment index. It fell to 29.9 last month, which turned out to be the lowest since November 1982 (also a recession year) when the figure stood at a not much lower 28.2. Not a single one of the 18 manufacturing industries reported an increase in employment.

4. Earlier this week, the Institute for Supply Management (ISM) released a similar survey for the service industry, which makes up nearly 90% of the economy. There was more bad news on the labor front. Their service employment index contracted in December for the 11th time in the last 12 months. All 18 industries the ISM surveys reported a decrease in service-related employment!

With the economy now caught up in a destructive spiral (rising joblessness → less consumer spending → fewer business sales → more layoffs), there is really only one solution left to break this impasse and that is massive government intervention. We're not talking about lower interest rates here. The Fed has been dropping rates for 17 months, yet the economy has failed to gain any traction. The future of the economy now rests with the economic stimulus package President-elect Obama and the new Congress are crafting. Parts of the program have already leaked out. It will cost about $800 to $1 trillion and spread out over two years. It's aim is to create 3 million new jobs by 2011, initially by financing major infrastructure projects across the country and by encouraging consumers and businesses to increase spending with the aid of $300 billion in tax cuts and credits.

Even if Washington enacts and then implements the program fairly quickly, don't expect any sharp rebound in job creation anytime soon. At best, we expect the economy to emerge from recession in the second half of the year, but the recovery in employment will take longer. Our forecast is for the unemployment rate to climb all year and peak at 9% in the first quarter of 2010. Thus, while the economy will begin to recover later this year, growth will be much too sluggish for employers to consider hiring back workers in large numbers in 2009.