



Pioneer Bank & Trust

Trust & Investments

The Best For The West!

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Head fake?

A number of economic indicators turned upward as the last quarter of 2011 came to a close. For example, U.S. housing starts jumped 9.3% in November, to the highest level in 19 months. Permits for future building also rose to more than a one-year high. Unemployment declined, as did new jobless claims. Business profitability was strong.

The good news is easily tempered, unfortunately. Much of new residential construction was for multifamily units, suggesting a continuing decline in home ownership rates. That sentiment was buttressed by a study by Zillow, Inc., forecasting further erosion in home prices. [From the peak in July 2006, home prices already have fallen 31%, according to the Case-Shiller index of values in 20 U.S. cities. About 29% of homeowners have negative equity, that is, they owe more than their homes are worth, according to Zillow's data. Some experts in the Zillow survey see an upturn by 2013, although the most pessimistic expect values to be flat or slightly down for five more years.

The Commerce Department had estimated growth in the July-September quarter at 2.0%, but this had to be revised downward to a 1.8% annual rate. Although that was the best quarter for 2011 to that point, such anemic growth numbers won't feel like "recovery" to most Americans. The key issue in the third quarter was a shortfall in personal consumption expenditures, which rose only 1.7% in the quarter.

Unemployment

Even the welcome unemployment numbers had a darker explanation. Much of the decline in the unemployment rate in November was attributable to the discouraged workers dropping out of the hunt for jobs. The labor force participation rate fell from an already low 64.2% to 64.0%. During better economic times, the country has had 67% participation rates. If the participation rate were the same as in January 2009, unemployment would stand at 11.0%.

The broader measure of unemployment, one which counts part-timers who would rather be working full time, stood at 15.6% in November.

In general, periods of such slow growth lead to recession about 70% of the time.

Interest rates

The Federal Reserve Board announced earlier in the year that short-term rates would be held close to zero until well after the next election. In December the Fed reaffirmed that position. It's unusual for the Fed to announce such a long time frame for its policies. Low interest rates will make it especially difficult for retirees to live off their portfolio income, without tapping into principal. Perhaps that helps to explain the preference for bonds over stocks among investors in 2011. Just \$4 billion flowed into equity mutual funds and exchange-traded funds in the U.S., compared to \$86 billion in fixed-income funds, according to data from EPFR Global.

Tax headwinds

One reason so many experts expect growth to slow in 2012 is that much of the stimulus coming from Washington, D.C., will be ending. Spending programs are not likely to be renewed, and new spending appears unlikely. The controversy over extending or expanding the payroll tax cut took all the headlines in December, but a variety of additional tax breaks for business expired on the first of the year as well. A measure intended as temporary pump priming, such as expanded depreciation allowances, still feels like a tax increase when it is taken away. Overall, the expiring tax provisions and spending declines could shave a full point off economic growth in 2012.

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