GEORGIA BUSINESS AND ECONOMIC CONDITIONS

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Georgia's economic outlook for 2008

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Georgia's inflation-adjusted GSP is forecast to rise by 2.4 percent, which is only slightly lower than the 2.6 percent advance in GSP estimated for 2007. Although the percentage gain will be lower than last year, it will be higher than the 2 percent growth expected for the nation. The state's nonagricultural employment will follow a similar path, expanding by 1.1 percent in 2008, down from the 1.3 percent gain posted in 2007, but higher than the 0.8 percent gain expected in nationwide employment. Georgia's leading sectors include life sciences, health care, the defense industry, transportation, professional and business services, and hospitality. Commercial construction may thrive for one more year, but the number of new projects announced will drop sharply. The main weak spots will be housing and manufacturing, but the financial services and information industries also are expected to lose jobs.

On an annual average basis, the state's nonagricultural employment will increase by 43,700 jobs, from 4,141,300 in 2007 to 4,185,100 jobs in 2008. All of the new jobs will be in services-producing industries. Heavy job losses in residential construction and manufacturing will be the main counter forces to overall employment growth. As a consequence, the unemployment rate will rise from 4.7 percent in 2007 to 5 percent in 2008. Despite job losses in several important sectors and a higher unemployment rate, Georgia's nominal personal income will expand by 5.3 percent, thanks to the 1.1 percent increase in total employment and the expectation that the proportion of jobs in relatively high paying occupations will be steady. Finally, increases in hourly compensation will help to support personal income growth. A negative factor, however, will be declining contribution to income growth from capital gains.

Many of the positive forces underlying the forecast for Georgia and the U.S. are the same. Businesses will continue to hire and make capital investments. The global economy will expand, and its growth will outpace domestic economic growth. The dollar will weaken, boosting prospects for Georgia's export-oriented businesses. Consumer price inflation will retreat to less than 2 percent. The federal fiscal stimulus will be significantly larger, and will be tilted towards defense, which should benefit Georgia's military bases and defense contractors. Nonresidential construction will reach its cyclical peak. There also are some very powerful negative forces. The housing and manufacturing recessions will deepen. Tight credit standards and considerable uncertainty in the financial markets will restrain lending and dampen sales of consumer items typically bought on credit.

In general, the economic implications of these trends are the same for Georgia as they are for the nation, but this is not uniformly the case. For example, existing home prices nationwide are expected to decline by 6 percent in 2008 and by 2 percent in 2009, but because home price bubbles did not

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develop in any of Georgia's MSAs, existing home prices here will be relatively steady. Nonetheless, Georgia's economic growth is very dependent on new home construction, so the sharp housing recession will damage the state's economy, but the downturn's impact will more be tightly focused on the housing industry itself than in places where home prices are dropping.

The economic repercussions of oil and fuel price movements also demonstrate how national trends can play out differently in Georgia. The extreme climb in oil and fuel prices over the last several years hurt deeply because the state is a major regional transportation, distribution, and logistics center, and these activities are fuel intensive. Georgians also are more dependent on their cars than are people in many other states. In addition, since Georgia's per capita personal income is only 90 percent of the national average, high fuel prices probably hit consumer spending a little harder here.

Strengths

As the U.S. business cycle becomes less conducive to economic growth, Georgia's substantially above-average population growth will become a more important driver of the state's overall economy. In-migration from other states will boost Georgia's population by 1.9 percent in 2008, which is more than double the 0.9 percent gain expected for the nation. The newcomers will span the age spectrum from well-heeled retirees to young, single, college-educated people--a mix that ensures both an adequate supply of talented young workers as well as a consumer base that is less exposed to the ups and downs of the business cycle.

Fortunately, the cost of doing business in Georgia is relatively low. A recent KPMG study found that Atlanta was the least costly large U.S. city in which to do business. In 2008, as businesses' priorities shift towards lowering costs, Georgia will be well positioned to compete nationally for corporate headquarters, high tech industries, expansions, and relocations. In addition to low costs, recent tort reform, deep pools of talent, and expansive transportation and logistics infrastructure make Atlanta an ideal place to establish a headquarters. Traffic congestion, however, is the main negative.

Chinese companies' growing desire to make direct investments in the U.S. is already proving to be a good fit for Georgia. Since mid-2006, three Chinese companies have announced major plans for operations in the state: Sany Heavy Industry Company plans to build a manufacturing facility in Fayette County that will employ up to 600 workers; a joint venture between Atlanta-based Heritage Capital Advisors and China-based General Protecht Group will bring 240 jobs to Lamar County over the next two years; and Kingwasong will build a food processing plant in Newnan, creating 200 jobs.

Over the next three to four years, Georgia stands to realize a major economic boost from the round of base closing and realignments that were recently finalized. The net gain to the state will be approximately 4,300 military and civilian jobs. In addition to these direct jobs, there is the induced impact that will add another 2,000 to 4,000 jobs to the off-base economies of the communities that host Georgia's bases. Fort Benning in Columbus can expect a proposed gain of 9,800 civilian and military jobs at the base itself and $1.1 billion in annual payroll. Moody Air Force Base in Valdosta will see a net gain of about 1,100 jobs. Robins Air Force Base in Warner Robins will see a net gain of about 700 jobs. Although Georgia was a net overall beneficiary of the latest BRAC, the closing of the Naval Air Station, Fort McPherson, Fort Gillem, and the Navy Supply Corps School will cost the Atlanta-Athens region over 7,000 military and civilian jobs. Of course, it will take years to fully implement these decisions.

Georgia's deepwater ports are another big plus, tapping directly into the fast-paced economic growth overseas and taking market shares from other U.S. ports. The prospects for growth are enhanced by the recent announcement of several new shipping services at the Port of Savannah, including a 20-year agreement with Maersk Line and a 15-year agreement with CMA CGM. Meanwhile, the Port of Brunswick has carved a lucrative niche for itself in agricultural cargo and car shipments.

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Services-Producing Industries

This sector's broadly based gains will gravitate towards higher wage industries. Education and health services will see one the highest rates of employment growth—2.7 percent, while the government sector will see the second highest rate of job growth—2.6 percent. Many of the new government jobs will be created at the military bases that benefited from the 2005 BRAC. Thus far, very few of the BRAC-related defense jobs have been created, but the big push will begin in 2008 when the military's Armor School moves to Columbus. Professional and business services will see the third highest (2 percent) rate of employment growth.

In Georgia, above-average population growth will greatly increase demand for educational services. Long-term trends are favorable, too, since current and future jobs will require significant investment in higher education. Widespread dissatisfaction with publicly funded K-12 education will encourage the growth of private schools. In addition, Georgia's extremely low SAT scores will spur demand for supplemental educational services.

The outlook for Georgia's health care providers is good. Job growth and an increasing number of retirees with Medicare will reduce the proportion of customers who self-pay or do not have insurance. Georgia's rapid population growth, stable funding for Medicare, Medicare's new prescription drug insurance plan, more use of health services, better management of operating expenses, and the increasing market power of health care providers will help the industry's bottom line.

Law firms will benefit from a cyclical increase in demand for legal services. Firms that provide legal services to private clients will benefit from growth in personal income and employment; and firms that handle corporate clients will benefit from advances in Georgia's gross state product, but there will be fewer business startups, and fewer mergers and acquisitions. The slower growth of corporate profits implies slower growth in spending for litigation in 2008, however. Also, the deepening housing recession, the peaking of nonresidential construction activity, and new caps on medical malpractice awards will reduce the amount of money spent on legal fees.

Georgia's booming hospitality industry will be the fourth largest contributor to employment growth in 2008. The rising number of out-of-state visitors at major attractions and major convention centers will be a primary driver, but higher prices also will buttress revenues and profits. Although the percentage of hotel rooms that are rented is forecast to decrease slightly, the Selig Center expects room rates to rise by about 4 percent, which will be more than double the overall rate of consumer price inflation. Room rates in many areas therefore will reach all-time record highs.

The outlook for Georgia's transportation, distribution, and logistics cluster is very solid. Foreign GDP growth, increasingly complex supply chains, gains in domestic industrial production, and positive—but slower—growth in consumer spending will push up cargo volumes in 2008. Fast-paced growth of containerized cargo coming into and shipped from Georgia's ports is the primary factor behind the transportation sector's growth. As activity in these industries expands, so will hiring. Also, Delta's successful emergence from bankruptcy eliminates one of the major restraints to net job creation.

The biggest challenge will be the continuing pattern of slow U.S. GDP growth, particularly because the slowdown is likely to be focused on transportation-intensive sectors of the economy. Nonetheless, bigger shipments of many manufactured goods, capital equipment, coal, and processed foods are expected to more than offset smaller shipments of home building materials and home-related consumer durables.

The Final Print Issue of *GBEC*

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GBEC **is sixty years old this year, so a change of pace is good. We think you'll agree. Thanks for your continued support; and we'll see you online.**

Unlike most services industries, employment in the state's information industry will decline in 2008. Many of the lost jobs will stem from the acquisition of BellSouth by AT&T and the deep job cuts announced by EarthLink. The recent re-pricing of risk also will curb job growth in this debt-heavy industry.

Financial institutions also will not hire new staff. Banks will be challenged by high and rising mortgage default rates, the deepening housing recession, less vigorous spending for big-ticket consumer durable goods, and fewer opportunities to boost earnings derived from mergers and acquisitions, IPOs, or trading stocks. Banks that cater to business customers are likely to fare better than those that cater to individual clients, however. Healthy foreign economies and expanding export markets will be two areas of economic opportunity, which favor banks that operate globally. In contrast, worsening conditions in the state's and nation's housing markets, less mortgage origination and refinancing, and restraint in consumer spending for durables will have the greatest impact on community banks.

Goods-Producing Industries

Georgia has lost over 97,000 jobs in goods-producing industries since mid-1999, and the downward spiral will intensify in 2008. The 5.6 percent job loss in construction will stem primarily from the deepening of Georgia's housing recession. Manufacturing employment will decline by 2 percent, with heavy job losses in automobile assembly, textiles, and building materials. In contrast, the outlook for food, beverage, biomedical, pharmaceutical, and equipment manufacturers is good.

The job losses stemming from the closure of both the Ford plant in Hapeville and the General Motors facility in Doraville will probably have their greatest impact on manufacturing employment in 2007-08. Before the closings were announced, the Ford and GM plants employed 2,100 and 3,100, respectively. In addition to these direct job losses, additional jobs will be lost at supplier firms that depend on contracts with one or both plants. About 2,500 workers will be needed when the new Kia Motors plant opens, however.

The downturn in U.S. auto sales will hurt manufacturers of original equipment, but manufacturers of replacement parts should enjoy stronger markets in 2008. Tire manufacturers will benefit from increases in the number of miles driven as well as consumers' increased desire to purchase high-performance and other specialty tires. Rising transportation costs and political pressures will encourage foreign manufacturers to invest more in U.S. production facilities and to buy automotive parts from U.S. manufacturers. More foreign companies now have assembly plants in neighboring states in the Southeast, fostering growth of auto parts manufacturers in Georgia.

TABLE 1

GEORGIA'S GROSS STATE PRODUCT, 1999-2008
(billions of dollars)

Year	Current $	Constant (2000) $	Percent Change from Previous Year in Current $	Percent Change from Previous Year in Constant (2000) $
1999	277.1	282.8	8.4	6.3
2000	290.9	290.9	5.0	2.8
2001	299.4	292.8	2.9	0.7
2002	306.7	294.1	2.4	0.4
2003	317.9	299.6	3.7	1.9
2004	337.6	310.0	6.2	3.5
2005	358.3	320.3	6.1	3.3
2006	379.5	331.1	5.9	3.4
2007	339.1	339.7	5.2	2.6
2008	416.1	347.9	4.2	2.4

Source: Data for 1999 through 2006 were obtained from the U.S. Department of Commerce. Data for 2007-2008 were obtained from the Selig Center for Economic Growth, Terry College of Business, University of Georgia (September 11, 2007).

Accounting for about one fourth of Georgia's manufacturing gross state product, food product manufacturing is the state's largest manufacturing industry. The demand for food products will continue to grow at a relatively steady, but moderate pace. Food processing is highly competitive and faces very demanding consumers, however. Consequently, firms have limited flexibility in pricing and the industry's already thin profit margins probably will not widen much in 2008.

Georgia's apparel manufacturing industry will continue to shrink as open world trade and cheaper foreign labor give a tremendous price advantage to many imported apparel items. The domestic industry's profit margins will remain under severe pressure. Meanwhile, Georgia's carpet and textile industry will be coping with both the housing recession and slumping automobile sales.

Prospects for Selected MSAs

Atlanta On an annual average basis, the 28-county Atlanta MSA will add 26,800 jobs, a year-over-year increase of 1.1 percent, which matches the percentage gain predicted for the state as a whole. Atlanta's high concentration of services-producing industries, distribution companies, and universities, as well as a very low concentration of manufacturing jobs ensures a bright employment forecast. Factors that will retard Atlanta's growth include the housing recession, the ongoing restructuring of the large information industry, limited prospects for employment gains at financial institutions, the closing of two major automobile assembly plants, and the early effects of the announced closing of three military bases.

Albany The 2008 forecast indicates that the Albany area will see its fourth-straight year of modest job growth. Nonagricultural employment will rise by 0.7 percent. Because Albany is a small MSA, the actions for the better or for the worse by one major company probably will determine the area's actual economic performance. The area will continue to capitalize on its many assets, including a low cost of doing business, an excellent telecommunications infrastructure, a reputation as a good place to raise a family, and a low crime rate. Albany will benefit from its role as a regional distribution center and from spillover from Florida. Redevelopment efforts along the Flint River should add to the area's charm, and add to the area's potential to benefit from tourism and retiree-based development. Its increasing role as a regional center for health care also weighs strongly in its favor.

Athens The Athens MSA will see moderate economic expansion in 2007, but the pace of growth will slow down. Employment should increase by about 1.5 percent, or about 1,200 jobs in 2008--the fourth-straight year on which the pace

TABLE 2

GEORGIA'S ECONOMIC FORECAST, 2007-2008

Georgia	2003	2004	2005	2006	2007	2008
Real Gross State Product, Bil of 2000$	299.7	310.0	320.4	331.1	339.7	347.9
Percent change	1.9	3.5	3.3	3.4	2.6	2.4
Nonfarm Employment (thousands)	3844.9	3900.5	4003.2	4086.4	4141.3	4185.1
Percent change	-0.6	1.4	2.6	2.1	1.3	1.1
Personal Income, Bil of $	250.8	264.7	282.3	298.6	318.6	335.5
Percent change	2.4	5.6	6.6	5.8	6.7	5.3
Housing Permits, Total	96704	108356	109336	104200	71900	60901
Percent change	-0.8	12.0	0.9	-4.7	-31.0	-15.3
Unemployment Rate (percent)	4.8	4.7	5.2	4.6	4.7	5.0

Source: Selig Center for Economic Growth, Terry College of Business, The University of Georgia, September 11, 2007.

TABLE 3

GEORGIA'S EMPLOYMENT FORECAST, 2007-2008

Georgia	2003	2004	2005	2006	2007	2008
Nonfarm Employment[1]	3884.9	3900.5	4003.2	4086.4	4141.3	4185.1
Goods Producing	659.3	660.3	670.7	680.1	674.8	656.2
Natural Resources and Mining	12.3	12.2	12.1	12.2	12.2	12.0
Construction	195.0	199.8	208.8	219.1	224.6	211.9
Manufacturing	452.0	448.3	449.8	448.8	438.0	429.3
Services Providing	3185.7	3240.2	3332.5	3406.3	3466.5	3528.9
Trade, Trans., Utilities	824.6	830.2	852.9	867.6	880.6	897.3
Information	123.4	118.2	116.5	115.6	114.2	113.6
Financial Activities	216.4	218.8	225.4	230.7	233.0	232.3
Professional and Business Services	490.3	510.4	533.8	550.0	561.0	572.2
Education and Health Services	395.0	409.3	424.0	437.8	449.6	461.8
Leisure and Hospitality	348.1	360.1	372.0	382.6	391.0	398.8
Other Services	155.5	156.2	158.3	159.3	159.8	160.6
Government	632.4	637.2	649.6	662.7	677.3	695.2
Percent Change						
Nonfarm Employment	-0.6	1.4	2.6	2.1	1.3	1.1
Goods Producing	-3.2	0.2	1.6	1.4	-0.8	-2.8
Natural Resources and Mining	-0.8	-0.8	-0.8	0.8	0.0	-1.6
Construction	-1.4	2.5	4.5	4.9	2.5	-5.6
Manufacturing	-4.1	-0.8	0.3	-0.2	-2.4	-2.0
Services Providing	-0.1	1.7	2.8	2.2	1.8	1.8
Trade, Trans., Utilities	-1.9	0.7	2.7	1.7	1.5	1.9
Information	-7.3	-4.2	-1.4	-0.8	-1.2	-0.5
Financial Activities	0.7	1.1	3.0	2.4	1.0	-0.3
Professional and Business Services	-1.9	4.1	4.6	3.0	2.0	2.0
Education and Health Services	5.2	3.6	3.6	3.3	2.7	2.7
Leisure and Hospitality	2.2	3.4	3.3	2.8	2.2	2.0
Other Services	-2.1	0.5	1.3	0.6	0.3	0.5
Government	1.2	0.8	1.9	2.0	2.2	2.6.

[1] Indicates thousands of workers.

Source: Selig Center for Economic Growth, Terry College of Business, The University of Georgia, September 11, 2007.

TABLE 4

EMPLOYMENT FORECAST FOR GEORGIA'S METROPOLITAN AREAS, 2007-2008

Metro Area	2003	2004	2005	2006	2007	2008
Nonfarm Employment[1]						
Albany	63.8	63.7	64.3	64.8	65.4	65.8
Athens	76.6	76.9	79.1	81.3	83.1	84.3
Atlanta	2,236.9	2,268.5	2,338.2	2,398.3	2,434.3	2,461.1
Augusta	208.8	213.6	214.7	214.0	216.3	220.4
Brunswick	41.4	42.8	44.3	45.5	46.1	46.7
Columbus	120.2	120.1	121.8	122.3	123.6	128.5
Dalton	76.1	76.8	77.9	79.6	70.1	80.1
Gainesville	68.0	68.5	70.6	72.9	75.2	76.3
Hinesville	15.8	16.8	17.6	18.2	18.6	18.9
Macon	100.3	101.3	101.3	100.8	101.0	101.2
Rome	42.8	42.7	43.3	44.3	45.3	45.8
Savannah	138.4	145.8	151.3	157.0	160.3	163.8
Valdosta	51.7	52.8	54.5	55.5	56.5	57.6
Warner Robins	50.2	51.4	53.3	56.3	57.9	59.1
Percent Change						
Albany	2.1	-0.2	0.9	0.8	0.9	0.7
Athens	1.6	0.4	2.9	2.8	2.2	1.5
Atlanta	-1.0	1.4	3.1	2.6	1.5	1.1
Augusta	0.9	2.3	0.5	-0.3	1.1	1.9
Brunswick	0.5	3.4	3.5	2.7	1.3	1.4
Columbus	0.3	-0.1	1.4	0.4	1.1	4.0
Dalton	-1.6	0.9	1.4	2.2	0.6	0.0
Gainesville	4.3	0.7	3.1	3.3	3.1	1.5
Hinesville	1.9	6.3	4.8	3.4	2.2	1.7
Macon	1.2	1.0	0.0	-0.5	0.2	0.2
Rome	4.1	-0.2	1.4	2.3	2.3	1.0
Savannah	0.0	5.3	3.8	3.8	2.1	2.2
Valdosta	2.6	2.1	3.2	1.8	1.8	2.0
Warner Robins	2.2	2.4	3.7	5.6	2.9	2.1

[1]Indicates thousands of workers.

Source: Selig Center for Economic Growth, Terry College of Business, The University of Georgia, September 11, 2007.

of job growth exceeds that of the state. Although Athens is poised to benefit from a surge in life sciences jobs, it also risks losing additional jobs in manufacturing.

Augusta This MSA will enjoy faster economic expansion in 2008, with employment climbing by 1.9 percent (4,100 jobs). Strong performance of the area's services- producing industries--notably in health care and private education--will help, too. Moreover, the Georgia Medical Authority will use the expertise available at the Medical College of Georgia to establish Augusta as a center for the rapidly growing life sciences industry.

Columbus The excellent outlook for this MSA is courtesy of zooming growth, which is just the opposite of the forecast for both the state and the national economies. In 2008, employment will rise by 4 percent, or 4,900 jobs--nearly quadruple the 1.1 percent gain expected for the state as a whole. The bullish forecast reflects several developments. Columbus will benefit from major announced expansions at Aflac and Fort Benning. Aflac plans to expand its employment in Columbus by 2,000 jobs between 2007 and 2012. The number of military personnel, contractors, and civilian employees associated with Fort Benning is expected to grow by at least 11,000 over the next five years.

Also, there is considerable excitement regarding the Kia Motors plant that is under construction on the north side of the MSA. When the plant opens in 2009 or 2010 it will employ about 2,500 workers, many of who live in the local area. The assembly plant also will lead to the creation of about 2,000 jobs at suppliers in both western Georgia and Alabama.

Macon Although total employment will rise by 0.2 percent in 2008, Macon's extensive surface transportation system and its proximity to Atlanta are pluses, as is its strategic location at the intersection of I-75 and I-16. Also, as Atlanta becomes more congested, sites in Macon will become very attractive to both private businesses and state government operations. The city's expansive historic district, places of special interest, and revitalization efforts are turning downtown into an even more attractive hub for business.

Savannah Employment in this coastal MSA will rise by 2.2 percent, or by 3,500 jobs, which is slightly higher than the 3,300 jobs estimated for 2007. Its dual personality--that of a major tourist attraction and a thriving deepwater port—gives Savannah a vibrancy that few other places can match. The metro area's short-term and long-term growth prospects are among the best in the nation, and its unique ambiance makes it an attractive place in which to live and do business. ■

The National Outlook 2008

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Due to the deepening of the housing recession and a series of financial shocks, the pace of inflation-adjusted GDP growth will remain subdued in 2008. Turbulent financial markets turned what initially appeared to be a nearly perfect soft landing for the U.S. economy into a protracted one, and thus U.S. GDP will rise by only 2 percent in 2008, which is about the same as the 1.9 percent growth estimated for 2007. Although this will be far below the long-term trend rate of growth of approximately 3 percent, the prolonged cool down will not be harsh enough to qualify as a hard landing. Still, the Selig Center expects the pace of U.S. GDP growth in 2008 to be similar to the pace estimated for 2007, a regularity that masks an increased risk of recession.

In addition to the housing recession, consumer caution is another major factor behind below-average GDP growth. The Selig Center is convinced that slower growth in consumer spending is imminent. Households' inflation-adjusted spending will advance by only 2.1 percent, compared to 2.7 percent in 2007 and 3.1 percent in 2006. The slowdown reflects the worsening of the housing recession, tighter credit standards, turmoil in the financial markets, substantial home price declines, the expectation of limited appreciation in the stock market, and high levels of consumer debt coupled with the need to save more out of current income.

The Selig Center's expectation of a sub-par growth rather than an outright recession hinges on several factors. First, banks are well capitalized and corporate balance sheets are in excellent shape, which reduces the likelihood that serial financial shocks—stemming primarily from the housing recession—will develop into a broad-based credit crunch that is severe enough to kill the expansion. Second, U.S. export growth will accelerate but import growth will not. Net exports therefore are expected to make a major contribution to GDP growth. Third, businesses' spending for new equipment will continue to grow. Fourth, spending on nonresidential construction will expand slightly to reach its cyclical peak in 2008. Next, federal fiscal policy will be more stimulative in 2008 than in 2007, reflecting increased defense spending. Also, crude oil and gasoline prices should remain at roughly the same levels as in 2007. Finally, decelerating inflation should reassure the bond markets and the Federal Reserve. So, if most of these expectations are realized, then the U.S. economy will continue to grow slowly, but with a relatively high--40 percent--risk of recession.

Obviously, the bad risks to the baseline forecast outweigh the good ones. The major downside risk is that a succession of financial shocks between mid-2007 and mid-2008 dry up liquidity, deny credit to the creditworthy, and produce steep drops in asset values. Consumers and businesses will pull back sharply. Since the shocks themselves would be deflationary, the Federal Reserve would have the leeway to quickly lower interest rates, so the recession originating from the "panic" would be mild. It helps that overstaffing and overinvestment is not widespread among U.S. businesses, which greatly reduces the potential for job losses. Layoffs therefore would be mostly related to temporary declines in demand rather than widespread restructuring.

The slow pace of U.S. GDP growth makes the economic expansion more vulnerable to an oil price shock in 2008 than at any time over the last several years. Due to tight market conditions, a significant interruption in the supply of crude oil and/or refinery products could make prices climb dramatically. A second energy crunch—stemming from major supply interruptions rather than robust demand growth—could prompt a hard and fast economic plunge.

On the positive side, productivity gains could be stronger than expected, which would spur U.S. GDP growth while containing both inflation and interest rates. Bearish bond investors might push down long-term interest rates, which could shorten the housing recession. Other potential positive developments include lower than expected oil prices, more business spending for investment, and stronger than expected growth in foreign GDP. Given these circumstances, the 2008 economic outlook assumes that the baseline forecast prevails, and that the optimistic and pessimistic extremes are avoided.

Housing Recession

Substantial declines in affordability stemming from several years of fast-paced home price appreciation, higher mortgage rates, tighter lending standards, investor pullbacks, and rising mortgage delinquencies continues to chill the nation's overheated housing market. Conditions will worsen in 2008, as sales of existing homes will plummet by 15 percent, sales of new homes will decline by 12 percent, and housing starts will drop by 11 percent. Given the setbacks already reported for 2007, these may seem like dramatic percentage declines, but that's only because the market was so extremely overheated in 2002-2005.

Affordability is the most serious issue facing the housing industry. Recent home prices gains have far outpaced income growth. According to the Office of Federal Housing Enterprise Oversight (OFHEO), over the last five years, home prices are up 55 percent, which is more than double the 27 percent rise in total personal income. Modest income growth in a rapidly appreciating housing market means that the heady rates of home price appreciation reported from late 2003 through late 2005 were simply not sustainable. Thus, it was not too surprising that price appreciation reported by OFHEO was absent in the second quarter of 2007. Meanwhile, other indices of home prices were reporting price declines. For example, the Standard&Poor's/Case Shiller U.S. Home Price Index reported a year-over-year decline of 3.2 percent, with no signs that the pullback in the residential real estate market was slowing down. The home price declines were widespread, with 15 of the 20 major markets that are tracked reporting negative annual returns. Atlanta, Charlotte, Dallas, Portland, and Seattle were the only markets where home prices were higher on a year-over-year basis.

Based on the OFHEO index of existing home prices, the Selig Center expects the average sales price of existing homes to drop by about 6 percent in 2008. It should be noted that the OFHEO index is constructed from Fannie Mae's and Freddie Mac's records of repeat sales or refinancing of the same single-family properties. Since that database only includes conventional, conforming mortgage transactions, it may understate price drops for homes that are typically purchased using other types of mortgages.

Although the U.S. housing market's immediate prospects are rather grim, several fundamental determinants of demand for homes—growth in employment, personal income, and population—are still positive, and should prevent the housing recession from extending into 2009. Also, from a long-term perspective, mortgage rates will not be very high in 2008 and 2009.

Consumer Spending

Consumer spending will grow more slowly than in 2007, but assuming the credit crunch in the mortgage markets does not spread to consumer credit, corporate credit, or small business lending, there should be enough credit and jobs around to ensure that consumers will spend more. The biggest drag on spending, however, will be the protracted housing recession as well as its side effects on the financial markets. A drop in U.S. home prices, less housing turnover, resets on variable-rate loans, and high numbers of mortgage defaults will restrain growth in consumer spending, especially for highly leveraged homeowners.

A related strain on household spending is that U.S. consumers now realize that they are heavily indebted and very short on savings. By almost any measure, households are overextended. The depressed household savings rate also reflects consumers' recent willingness to boost current spending by extracting more and more wealth from their appreciated homes. Not surprisingly, the household savings

UNITED STATES ECONOMIC FORECAST 2007-2008

United States	2003	2004	2005	2006	2007	2008
Gross Domestic Product, Bil. of 2000$	10,301.0	10,675.8	11,003.4	11,319.4	11,534.5	11,765.2
Percent change	2.5	3.6	3.1	2.9	1.9	2.0
Nonfarm Employment (millions)	130.0	131.4	133.7	136.2	137.6	138.8
Percent change	-0.3	1.1	1.7	1.8	1.1	0.8
Personal Income, Bil. of 2000$	8,677.9	8,974.1	9,231.4	9,577.9	9,952.4	10,245.6
Percent change	1.2	3.4	2.9	3.8	3.9	2.9
Personal Income, Bil. of $	9,163.6	9,727.2	10,301.1	10,983.4	11,675.4	12,235.8
Percent change	3.2	6.2	5.9	6.6	6.3	4.8
Civilian Unemployment Rate (percent)	6.0	5.5	5.1	4.6	4.8	5.2
CPI-U, Annual Percent Change	2.3	2.7	3.4	3.2	2.6	1.9

Source: Selig Center for Economic Growth, Terry College of Business, University of Georgia, September 11, 2007.

rate in mid-2007 was a meager 0.6 percent. Now, however, households will exercise noticeably more restraint in their spending in 2008. One major concern is that a sharp rise in the savings rate probably would cause a mild recession.

At this juncture, job creation--and the income growth that accompanies it--is absolutely vital to the outlook for both consumer spending and the overall economy. The 2008 forecast anticipates that job growth should be adequate to ensure continued economic expansion, but grossly inadequate to boost its current rate of growth. With asset appreciation on hold and a greater focus on savings, increases in inflation-adjusted disposable personal income must account for virtually the entire projected rise in consumers' spending. The number of jobs, which is forecast to expand by 0.8 percent, will underpin this income growth.

In 2008, consumers' spending for services will increase much faster than their spending for goods. Among services, spending on vehicle leasing, medical care, and personal business services will increase the fastest. Among goods, spending for durables will decline, but spending on non-durables will increase. Outlays for drugs, pharmaceuticals, purchased meals, and computers and software will increase briskly. In contrast, spending on cars and household appliances will decline sharply.

Labor Markets

The overall outlook for jobs is still okay. As noted previously, total nonfarm employment will expand by 0.8 percent, which is slightly lower than the 1.1 percent gain estimated for 2007. But things could change if the second-straight year of slow GDP growth restrains hiring; GDP growth lags the rise in productivity; and if the outsourcing of U.S. jobs to developing countries continues to spread from blue-collar manufacturing jobs to white-collar high-tech occupations. Even devaluation of China's currency relative to the dollar will not help to preserve U.S. jobs to any great extent.

In the coming year, the nation's transportation and warehousing industries will see the fastest rate of employment growth. Professional and business services companies will post the second fastest rate of employment growth. Education and health services as well as leisure and hospitality will see above-average employment gains. Average growth is expected in wholesale trade, retail trade, and government. Due to the housing recession, construction jobs and jobs in several closely related services industries will be lost. Meanwhile, U.S. manufacturing will continue to bleed jobs in apparel, textiles, furniture and wood products, electrical equipment and appliances, automobile manufacturing, chemicals, plastics, and construction materials. But some job stability will occur in the aircraft, oilfield equipment, food products, machinery, and fabricated metal products sub-sectors.

Corporate Profits

Skyrocketing corporate profits make year-over-year comparisons very difficult. In mid-2007, corporate profits were 90 percent higher than they were five years ago, which dwarfs the 33 percent increase in nominal GDP during that same period. Indeed, the share of national income devoted to profits is unusually high, and probably cannot be sustained. Profit growth is very sensitive to movements in GDP, and GDP growth will be sub-par in 2008. Also, the damage the sub-prime credit crisis inflicts on the profits of banks and others will weigh heavily on the overall profits earned by U.S. companies. After-tax corporate profits therefore are not expected to rise significantly in 2008, and may decline slightly. Another challenge to the bottom line will be margin compression due to higher costs, but slower growth in demand is probably the more important factor because it curtails top- and bottom-line growth.

On the positive side, unit-labor costs and commodity prices are expected to rise more slowly in 2008, and productivity growth is expected to quicken somewhat. Even slight moderation of oil prices in 2008 could provide an additional tailwind to the profits earned by many domestic companies. Finally, strong foreign economies coupled with the declining value of the dollar will help bolster sales of many export-oriented companies and will help companies producing for the domestic market to compete with foreign rivals.

Business Spending

Despite tighter credit and higher borrowing costs for all but the most creditworthy, the Selig Center is slightly optimistic about capital spending. Spending for computers, aircraft, other transportation equipment, and software will increase the fastest. Spending for communications equipment will increase modestly, and spending for light vehicles, home-related equipment, and industrial equipment will decline.

Corporate discipline with respect to recent capital outlays for equipment and software also suggests that pent-up demand has the potential to power capital spending in 2008. Yet another factor boosting outlays for labor-saving equipment and software will be the recent and scheduled increases in the minimum wage.

The second-straight year of slow-paced GDP growth and the expectation of flat or declining corporate profits will be two headwinds, however. The uncertain economic outlook also will keep businesses cautious in their approach to capital expenditures. Another deterrent is that the after-tax cost of corporate debt will rise in 2008, however the slight increase will not hurt investments very much.

The Selig Center expects businesses' inflation-adjusted spending on buildings to rise by less than 1 percent in 2008. Nonresidential construction activity will reach its cyclical peak in 2008, and will decline in 2009. Demand for new office space will be very modest, but new industrial space near transportation hubs will be prized.

International Trade

In 2008, real exports will increase more than twice as fast as imports, so net exports will be a prime contributor to GDP growth. A substantially weaker U.S. dollar also will help exports and deter imports. The narrowing of interest rate differentials between the U.S. and our trading partners also will hurt the dollar. Export growth will be especially fast-paced for aircraft, consumer goods, and capital goods. Exports of food, feeds, and beverages will increase more slowly.

Inflation

If oil prices steady, consumer price inflation will increase by 1.9 percent in 2008, compared to 2.6 percent in 2007. The overall trend suggests that consumer price inflation peaked in 2005 and is headed lower. Moreover, the

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usual drivers of inflation will be less intense. For example, the pace of GDP growth is well below average and it will not accelerate. Consumer spending and employment will both grow more slowly. The Federal Reserve's short-term interest rates will not be overly accommodative. There is still some excess capacity in a number of economic sectors. Heightened competition for jobs from foreign workers will help to keep the lid on U.S. wages and benefits. Finally, plummeting housing prices suggest that one of the biggest risks to higher inflation is much diminished.

Crude Oil Markets

If there are no additional significant supply interruptions, it is unlikely that oil prices will go higher. Prices will range between $70 and $80 per barrel, but it would not be too surprising if oil were to trade outside of this boundary. Also, this forecast is predicated upon a moderate slowdown in the pace of global economic growth, no major disruptions in the supply of crude, and bringing new energy infrastructure online.

Nonetheless, further oil price shocks remain as one of the major threats to economic growth. Energy markets are likely to remain tight for the foreseeable future, because OPEC production is already at or near full capacity, while the growing global economy wants more. Meanwhile, it is obvious that OPEC is not too eager to increase production. The bottom line is that any unanticipated supply interruption is likely to produce sizable spikes in oil prices, and could establish a new, higher, floor for oil prices. A major disruption—such as the withdrawal of Iranian crude from the global market—could spiral crude oil prices to over $100 per barrel, which, if sustained, would precipitate an oil-shock recession. ■

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