

ALTERNATIVE FORECASTS

DRI has assigned a 60% probability of occurrence to its November 1999 baseline forecast of the U.S. economy. The major features of this forecast include:

- Real GDP grows 3.9% in 1999, 3.4% in 2000, 3.5% in 2001, 3.0% in 2002, and 3.2% in 2003;
- U.S. nonfarm employment advances 2.2% this year, 1.6% next year, 1.4% in 2001, then averages about 1.1% thereafter;
- the U.S. civilian unemployment rate remains at least one percentage point below the full employment rate of 5.5%;
- consumer confidence peaks in 1999, then slowly tapers off over the forecast period;
- consumer inflation remains well below 3.0%;
- the federal budget surplus increases in each year of the forecast;
- and the U.S. merchandise trade deficit widens.

While the baseline scenario represents the most likely path for the national economy over the next few years, uncertainties surrounding several key variables mean other outcomes are also possible. To account for this, DRI prepares alternative forecasts based on different assumptions regarding these key variables. Two of these alternative forecasts, along with their impacts on the Idaho economy, are discussed below.

While it is believed the economy will not suffer a recession over the forecast period, it should be noted the risk of a recession is high. A review of the probabilities of occurrence for each forecast scenario shows this. The baseline does not include a recession and its probability of occurrence is 60%. However, both of the alternative scenarios do contain recessions and their combined probability of occurrence is 40%. This implies the chances of the economy not suffering a recession over the next few years are better than even.

STOCK-MARKET-CORRECTION SCENARIO

The *Stock-Market-Correction Scenario* has been assigned a 10% probability of occurrence. An early recession might be triggered by a collapse of the U.S. stock market. One estimate suggests the stock market is overvalued by 30%. A correction of this magnitude would send shock waves through the U.S. economy. A stock market crash would destroy consumer wealth and confidence. Consumers would react to this by curbing spending and increasing savings. However, the impacts of the crash would not end at our shores. It could derail the Asian recoveries, which would exacerbate the U.S. downturn. It is assumed that this correction comes early next year and a recession results shortly thereafter.

This recession is relatively short lived. The Federal Reserve has been very responsive to threats to the U.S. economy's health. While it may not be able to prevent a recession, the central bank can contain the damage by moving quickly to lower interest rates after a stock market correction. Thankfully, the current low-inflation environment should provide enough maneuverability to make this possible. This downturn would be unique. In the postwar era, every recession has been preceded by a jump in core inflation rate. This recession would commence without such a jump.

As the table on the facing page shows, Idaho's economy takes its biggest hits in 2000 and 2001. Total nonfarm employment, which was expected to grow 2.1% in both 2000 and 2001 in the baseline case, averages about 1.35% growth in both years in the *Stock-Market-Correction Scenario*.

IDAHO ECONOMIC FORECAST
BASELINE AND ALTERNATIVE FORECASTS
JANUARY 2000

	BASELINE				STOCK MARKET CORRECTION				LATE RECESSION			
	1999	2000	2001	2002	1999	2000	2001	2002	1999	2000	2001	2002
GDP (BILLIONS)												
Current \$	9,228	9,671	10,159	10,649	9,228	9,414	9,712	10,239	9,228	9,705	10,208	10,243
% Ch	5.3%	4.8%	5.0%	4.8%	5.3%	2.0%	3.2%	5.4%	5.3%	5.2%	5.2%	0.3%
1992 Chain-Weighted	8,113	8,386	8,676	8,939	8,113	8,170	8,373	8,751	8,113	8,400	8,625	8,454
% Ch	3.9%	3.4%	3.5%	3.0%	3.9%	0.7%	2.5%	4.5%	3.9%	3.5%	2.7%	-2.0%
PERSONAL INCOME - CURR \$												
Idaho (Millions)	27,524	29,056	30,615	32,329	27,524	28,737	29,879	31,481	27,524	29,069	30,744	31,996
% Ch	6.3%	5.6%	5.4%	5.6%	6.3%	4.4%	4.0%	5.4%	6.3%	5.6%	5.8%	4.1%
U.S. (Billions)	7,783	8,188	8,592	8,992	7,783	8,067	8,274	8,651	7,783	8,187	8,617	8,792
% Ch	5.8%	5.2%	4.9%	4.6%	5.8%	3.6%	2.6%	4.5%	5.8%	5.2%	5.2%	2.0%
PERSONAL INCOME - 1992 \$												
Idaho (Millions)	24,147	25,059	25,954	26,808	24,147	24,844	25,581	26,539	24,146	24,992	25,753	26,030
% Ch	4.6%	3.8%	3.6%	3.3%	4.6%	2.9%	3.0%	3.7%	4.6%	3.5%	3.0%	1.1%
U.S. (Billions)	6,827	7,061	7,284	7,456	6,827	6,973	7,084	7,292	6,827	7,039	7,218	7,153
% Ch	4.1%	3.4%	3.2%	2.4%	4.1%	2.1%	1.6%	2.9%	4.1%	3.1%	2.5%	-0.9%
TOTAL NONFARM EMPLOYMENT												
Idaho (Thousands)	535.7	547.1	558.8	572.2	535.7	543.3	550.2	566.6	535.7	547.1	556.9	559.5
% Ch	2.7%	2.1%	2.1%	2.4%	2.7%	1.4%	1.3%	3.0%	2.7%	2.1%	1.8%	0.5%
U.S. (Millions)	128.6	130.6	132.5	133.9	128.6	129.1	128.5	130.8	128.6	130.6	132.1	129.1
% Ch	2.2%	1.6%	1.4%	1.0%	2.2%	0.4%	-0.4%	1.8%	2.2%	1.6%	1.1%	-2.3%
GOODS PRODUCING SECTOR												
Idaho (Thousands)	112.8	113.6	115.7	118.6	112.8	110.9	111.7	116.6	112.8	114.0	115.9	112.9
% Ch	1.4%	0.7%	1.9%	2.5%	1.4%	-1.7%	0.7%	4.4%	1.4%	1.1%	1.6%	-2.6%
U.S. (Millions)	25.2	24.8	24.7	24.6	25.2	24.3	23.4	23.8	25.2	24.8	24.5	23.1
% Ch	-0.5%	-1.6%	-0.6%	-0.1%	-0.5%	-3.5%	-3.7%	1.7%	-0.5%	-1.6%	-1.1%	-5.6%
SERVICE PRODUCING SECTOR												
Idaho (Thousands)	422.9	433.5	443.0	453.6	422.9	432.3	438.5	450.0	422.9	433.1	441.0	446.6
% Ch	3.1%	2.5%	2.2%	2.4%	3.1%	2.2%	1.4%	2.6%	3.1%	2.4%	1.8%	1.3%
U.S. (Millions)	103.4	105.9	107.9	109.3	103.4	104.7	105.1	107.0	103.4	105.8	107.5	105.9
% Ch	2.9%	2.4%	1.9%	1.3%	2.9%	1.3%	0.3%	1.8%	2.9%	2.4%	1.6%	-1.5%
FINANCIAL MARKETS												
Federal Funds Rate	5.0%	5.5%	5.5%	5.5%	5.0%	4.7%	4.2%	4.3%	5.0%	5.3%	6.3%	6.1%
Bank Prime Rate	8.0%	8.5%	8.5%	8.5%	8.0%	7.7%	7.2%	7.3%	8.0%	8.3%	9.3%	9.1%
Mort Rate, New Homes	7.2%	7.7%	7.2%	7.0%	7.2%	7.6%	6.9%	6.9%	7.2%	7.6%	7.5%	8.0%
INFLATION												
GDP Price Deflator	1.3%	1.4%	1.6%	1.8%	1.3%	1.3%	0.7%	0.9%	1.3%	1.6%	2.5%	2.4%
Personal Cons Deflator	1.6%	1.7%	1.7%	2.2%	1.6%	1.5%	1.0%	1.6%	1.6%	2.0%	2.6%	3.0%
Consumer Price Index	2.2%	2.3%	2.1%	2.6%	2.2%	2.1%	1.3%	1.8%	2.2%	2.7%	3.1%	3.3%

Forecast Begins the THIRD Quarter of 1999

Goods-producing employment actually declines nearly 2.0% this year and rises less than 1.0% in 2001. Services-producing employment growth tapers down to 2.2% in 2000 and 1.4% in 2001. Total nonfarm employment does post a strong recovery in 2002, but it is not enough to overcome the weaknesses of the previous two years. In 2002, Idaho total nonfarm employment is about 5,600 lower than its baseline counterpart. Idaho real personal income also grows slower in 2000 and 2001. Like employment, it too fails to make up ground lost during 2000 and 2001 despite a relatively strong showing in 2002.

LATE-RECESSION SCENARIO

The *Late-Recession Scenario* has been assigned a 30% probability of occurrence. This scenario is a more typical end-of-expansion recession than the *Stock-Market-Correction Scenario* discussed above. In the *Late-Recession Scenario* the U.S. economy grows stronger in 1999-2000 than in the baseline. The unemployment rate stays low and the U.S. stock market keeps climbing. Both of these factors keep consumer confidence buoyant. As a result, consumer spending continues to boom. In addition to the strong domestic economy, the recovery in Asia causes worldwide demand to strengthen. But this stronger growth comes at the price of higher inflation. Commodity prices recover along with foreign demand. Wage pressures grow as the U.S. labor market is stretched to its limit. Despite the signs of increasing inflation, the Federal Reserve is slow to tighten. This policy mistake proves costly.

The nation's central bank attempts to make up for delayed tightening by raising interest rates sharply. In the fall of 2001 the federal funds rate is at 6.75%. Because of the delayed response to inflation, the recession spirals downward, resulting in a peak-to-trough decline of 2.7%. While this recession would be about average by historical standards, it would be deeper and longer than the recession experienced in the *Stock-Market-Correction Scenario*.

In this scenario, Idaho's economy departs significantly from its baseline counterpart beginning in 2001. Idaho nonfarm employment increases just 1.8% in 2001 and 0.5% in 2002. In the *Baseline Scenario* it advances 2.1% in 2001 and 2.4% in 2002. The goods-producing sector is hit harder than the services-producing sector. The former rises 1.6% in 2001 then declines 2.6% in 2002. The latter grows 1.8% next year and 1.3% in 2002. Idaho real personal income advances 3.5% this year, 3.0% next year, and 1.1% in 2002. In the baseline case, this measure rises 3.8% in 2000, 3.6% in 2001, and 3.3% in 2002.