# THE ECONOMIC SITUATION

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After the short war, now what?
Jobs and money. There are some new life signs.
South Carolina: A new forecast.
Mr. Ford and the Model T. Looking for heroes.

**The short war. Now what?**

It was a mercifully short war, measured in weeks instead of months. And while short, and still devastating to many people, places, and precious relics of past civilizations, the conflict was not as disruptive to the U.S. economy as some expected.

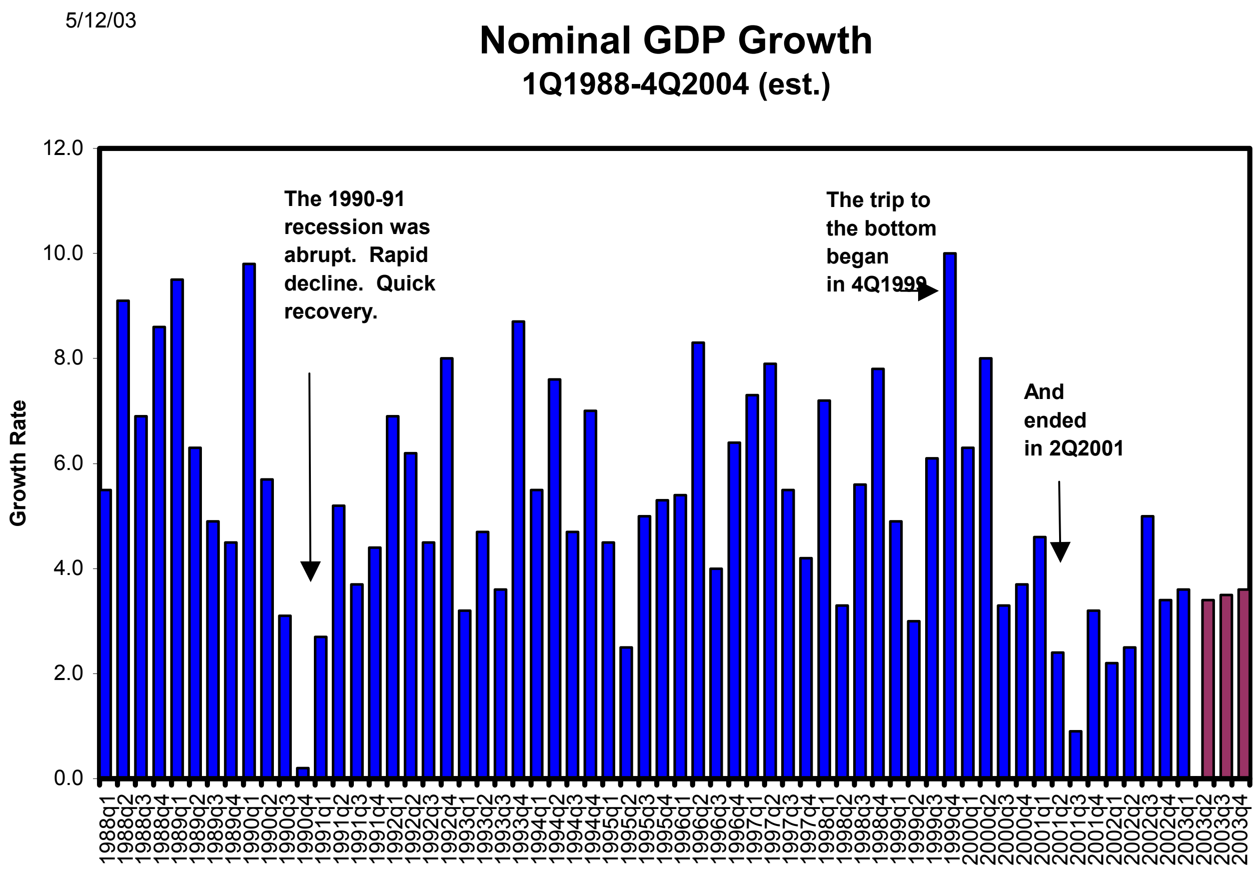
Writing on March 12, just days before the war was launched, I described two possible war scenarios, one based on a short war and the other long. The short war scenario predicted oil prices—the critical variable for the economy—would spike immediately to $50 a barrel and then quickly fall in the direction of $29 a barrel, with the happier low price arriving by January 2004. Fortunately, due to coalition forces gaining quick control of Iraqi oil fields and with Venezuela coming back on stream, crude oil barely nudged $40 and is now trading in the $26 range.

In last quarter's newsletter, I predicted the price of unleaded gasoline, based on higher oil prices, would hit $1.60 and then head toward $1.25. The $1.25 forecast was on target, but this pleasant number arrived earlier than expected. Meanwhile, the Dow-Jones industrials have added 1,000 points since March 12 when the index stood at 7552. We still have a way to go to hit 10,000 by yearend, but I am still betting on it. Keep your fingers crossed.

The war's quick end removed a key element of uncertainty from the economy and brought a renewed focus on just how poorly the non-war economy was performing. Less than happy news came in the form of data on real GDP growth for 4Q2002 and 1Q2003. The 4Q2002 early estimate had indicated growth of 0.7%. That number was revised upward to 1.4%. But the initial estimate for 1Q2003 came in at a meek 1.6%, with little promise that things would get brighter in the second quarter. Oil, war, bad weather, and a manufacturing recession that would not seem to give up all combined to keep the economy in low gear. With three of those factors removed, it is time to shift into second. But don't hold your breath.

**A quick look at GDP data tells the tale**

The GDP data and forecast for the next few quarters, stated in nominal terms, are shown in the next chart. The data for the next few quarters, which include an expected inflation rate of around 1.5% are virtually flat.

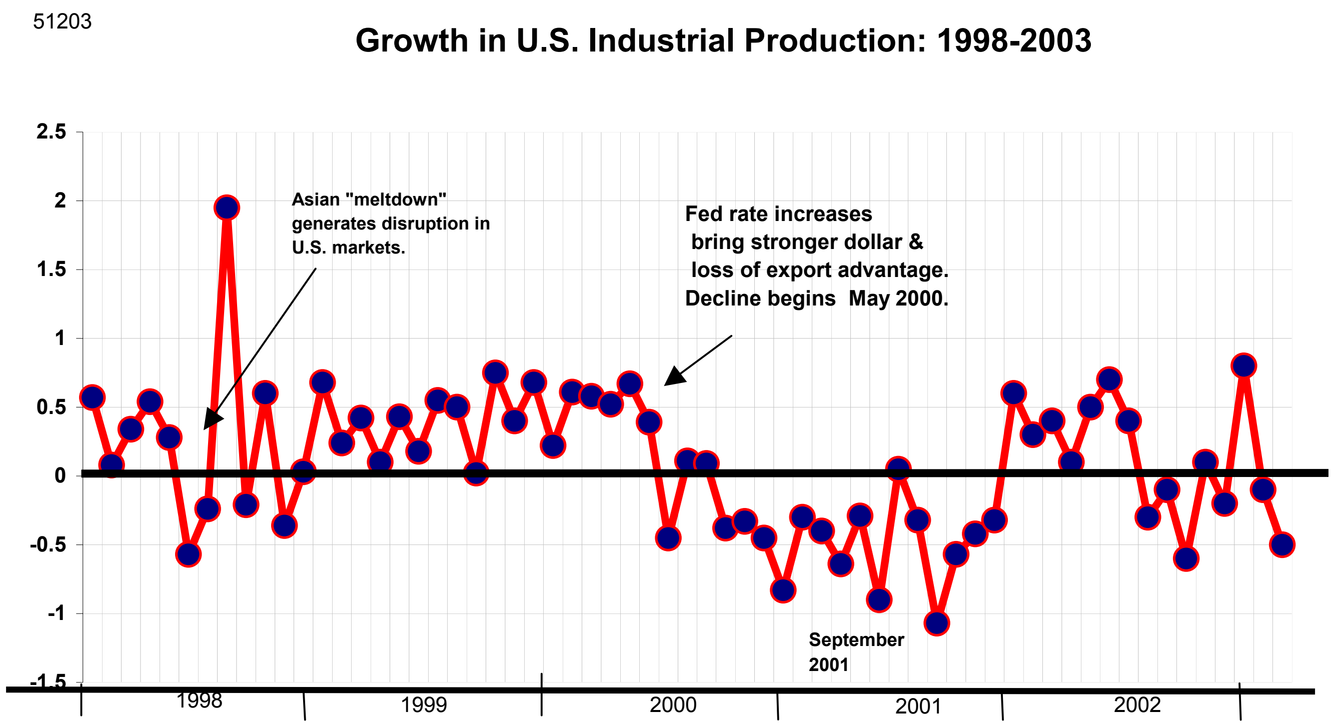



**The industrial economy is still the weak link in the chain.**

Lack of growth in the goods producing sector continues to be the vulnerable part of the national economy. Chastened partly by a strong dollar that made foreign goods relatively more attractive to U.S. consumers and then hit by a generally weaker world economy, U.S. producers have yet to begin adding production and workers. But the declining value of the dollar, due mostly to rock-bottom U.S. interest rates, and the continued recovery of the national economy will improve things for the goods sector as we turn the calendar page for 2004.

The next chart gives this picture in terms of monthly industrial production data. The weaker months of the first quarter leave little to celebrate. But it may be better to take a longer view of the data. If we focus on the observations from September 2001 forward, we can see a positive trend that doesn't want to go away.

As they say, the trend can be your friend.




**Total employment in the economy also shows a bit of promise.**

The positive trend observed in the industrial economy is seen in employment data. The next chart shows total U.S. employment and a trend line fit to the series. The gap between trend and recent employment levels gives a crude indication of the severity of the national slowdown. But as can be seen, the gap is closing.

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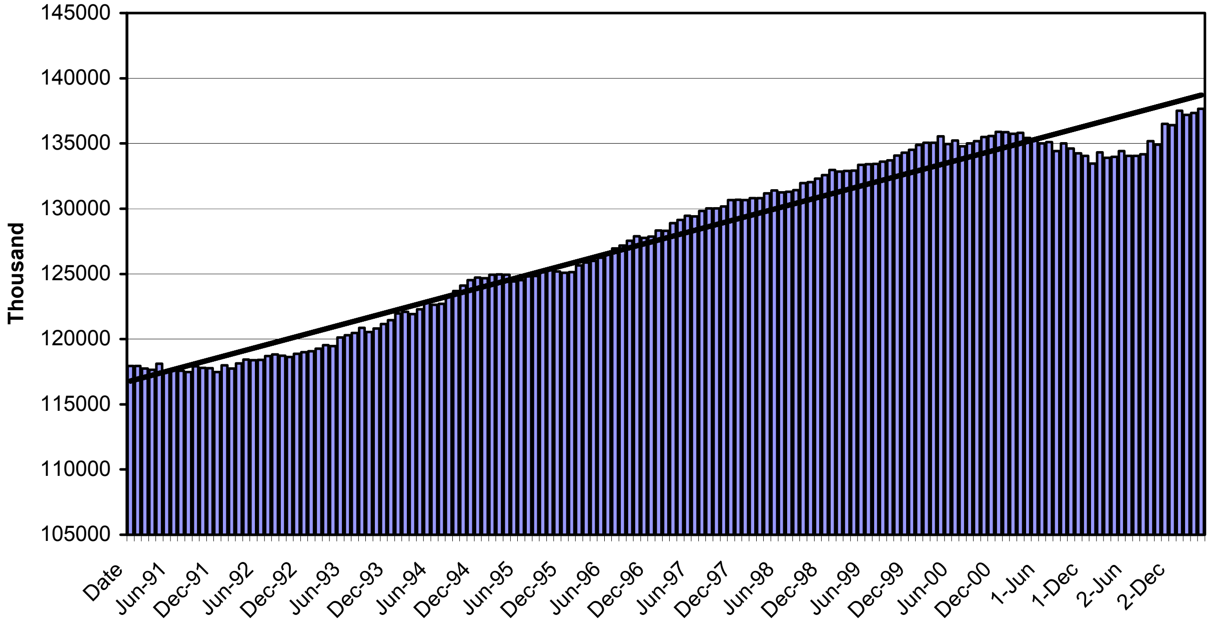
**Total Employed, 16 and Over, Seasonally Adjusted**
**1/1991 - 4/2003**




**Money always helps. If only we had more.**

Recent statements by newly reappointed Fed Chairman Greenspan imply that the central bank is prepared to open the money valves if things do not pick up soon. On two recent occasions, in February and again in May, the Open Market Committee has chosen to leave interest rates at their current bargain basement levels. But the Fed holds one other face card. Open market operations, the purchase and sale of government securities, enables the Fed to increase or decrease the money supply.

But what have they been doing? Is the money supply rising or falling? What do the data tell us?

The next chart provides data on a broad measure of the money supply, M3, which includes currency, demand deposits, savings, and money market accounts, and several categories of large denomination deposits. The chart shows monthly data for M3 growth as well as a 4-month running average.

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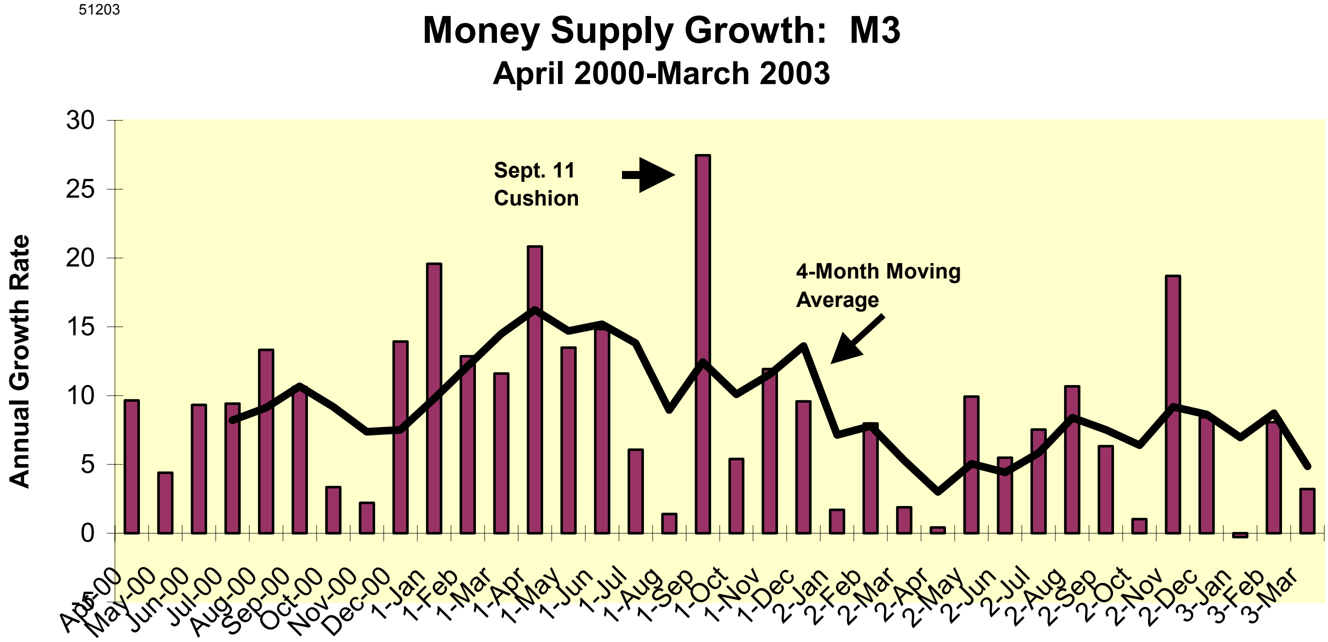


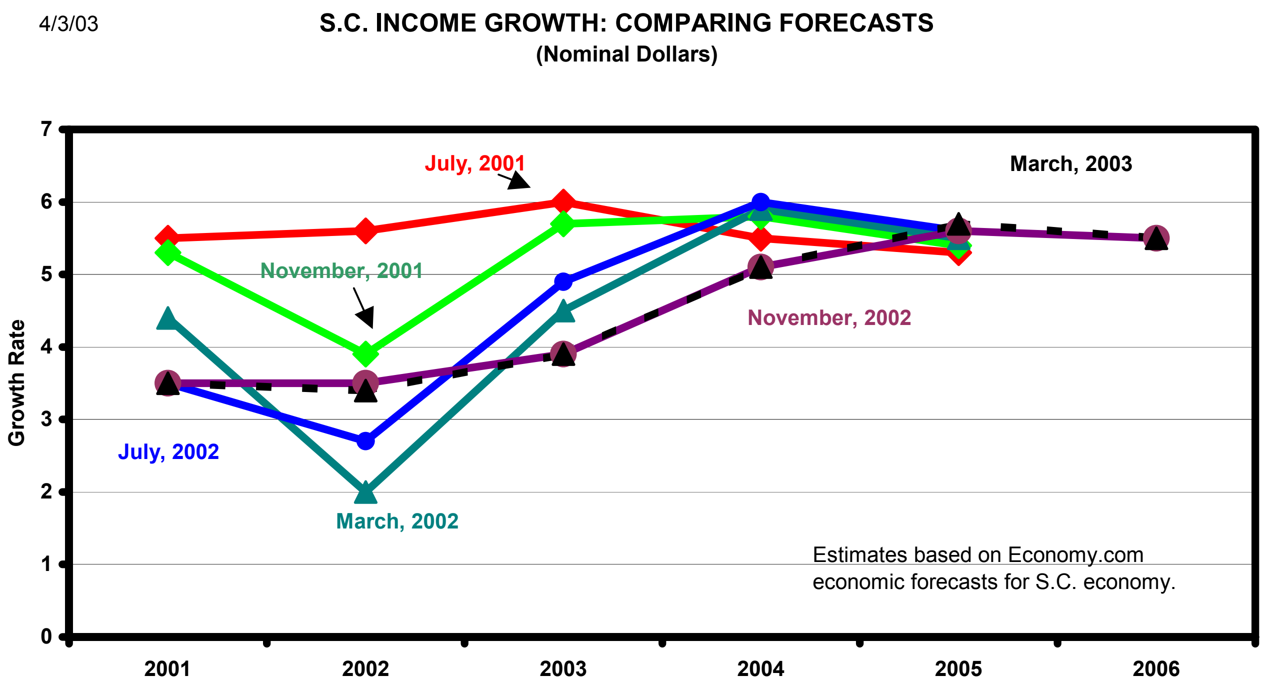

Close inspection of the chart does not support the notion that the Fed has rushed to inject more money into the economy. Since mid-2002, the 4-month moving average has risen somewhat, but growth is still well below that of 2000 and 2001 when the Fed was attempting to resuscitate a very weak economy. The data, which reveal facts not rhetoric, suggest the Fed is still concerned that sudden acceleration of the economy will ignite inflation. On the other hand, it could be that the Fed is attempting to offset what they believe are the effects of a growing federal deficit.

**Getting closer to home. What about South Carolina?**

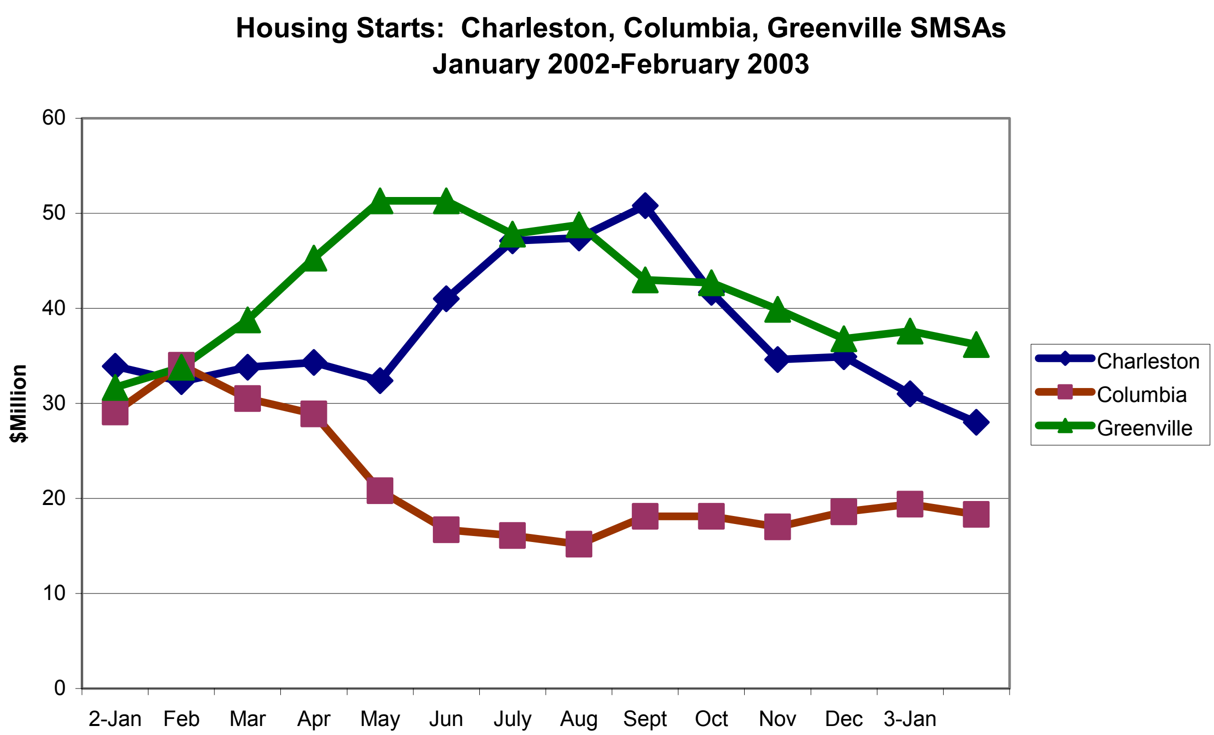
With heavy dependence on manufacturing, and in spite of a strong auto sector, the state economy continues to follow a weak growth path. Total employment is rising, but at a weak pace. At the same time, there is some good news to consider. This is found in the forecasts for state total personal income growth provided by economy.com.

The next chart, based on economy.com data, tells the tale. Please be patient, now. It takes a few minutes to absorb what is shown here. The chart contains growth rates for six individual forecasts dating by to July 2001 and ending with March 2003. There are six forecasts shown in the chart. But the last one is very hard to see. That is the good news. It lies almost on top of the previous forecast. It appears the bottom has formed. Reasonable growth lies ahead. But notice. It will be 2005 when the state economy begins to grow at the pre-911 rate.

4/3/03




The slower pace of economic activity is seen in data on housing permits for the state's three largest metro areas. As seen the next chart, the slowdown in public sector hiring has taken a toll a Columbia. The Charleston and Greenville metro areas are running neck-and-neck, but at a slightly slower pace.



**Still looking for heroes.**

In my search for heroes, I have become fascinated with Henry Ford, best known for producing millions of "Tin Lizzies." His development of assembly-line production set the pace for the industrial world. Ford set the world on its ear in 1914 when he doubled the rate of pay at his plants from $2.50 a day to $5.00, and cut the work day to 8 hours. At the time, the rate of pay in England was $5.00 a week. Ford immediately cut the price of his Model T. Commentators at the time thought he had lost his marbles. Higher wages, lower prices! How could that be?

The higher pay cut worker turnover, increased loyalty, and increased production. Costs fell. Profits rose. It must of felt so good that Ford raised pay to $6.00 an hour, and he cut the price of a new Model T, which had started with a price above $900, to $265. With no withholding taxes, a worker could earn enough to buy a brand spanking new Ford in 44 days.

Mr. Ford democratized personal transportation . His marvelous car machine made it possible for ordinary workers to own new automobiles and see this wonderful country. His is a powerful story that is still being repeated.

America is great. Pass the word.