Recovery: One Year After

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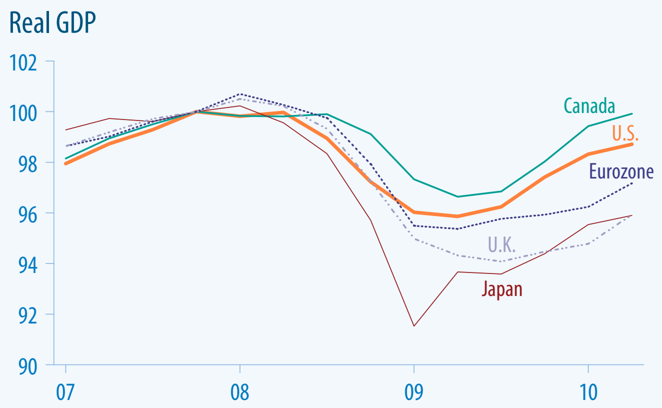
CHART 1
AS THE CYCLE TURNS
(2007Q4 = 100)



Having just passed the two-year anniversary of the Lehman Brothers bankruptcy and the third anniversary of the start of the credit crisis, some more positive developments deserve at least a bit of air time—the North American recovery has passed its first anniversary. The NBER officially declared an end to the devastating U.S. recession, stating that the downturn bottomed out June 2009. The U.S. economy has expanded in each of the past four quarters by a total of 3.0%, which is above its average growth rate over the past 40 years. While that may be disappointing in light of the deep downturn, and joblessness remains unacceptably high, most of the contours of the recovery are actually well within the historical norm. Clearly, the genesis of this recession was highly unusual, as was its synchronized nature (*Chart 1*), but we would caution against assuming that *"it's completely different this time"*, because so far in this recovery "*it*" isn't.

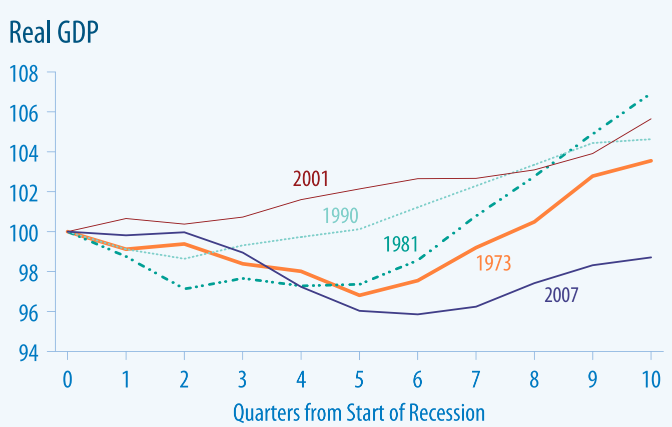
TABLE 1
U.S. RECOVERY HISTORY
(percent)

Economic Trough **	GDP Growth Year 1	GDP Growth Year 2	Employment Growth Year 1	Employment Growth Year 2	Jobless Rate At Trough	Jobless Rate Year 1 *	Jobless Rate Year 2 *
Nov. 1970	4.5	6.9	1.9	4.5	5.9	+0.1	-0.6
Mar. 1975	6.2	3.2	3.5	3.6	8.6	-1.0	-0.2
Nov. 1982	7.7	5.6	4.2	5.0	10.8	-2.3	-1.3
Mar. 1991	2.6	3.4	-0.5	1.6	6.8	+0.6	-0.4
Nov. 2001	1.9	3.8	-0.8	-0.2	5.5	+0.4	-0.1
Average Recovery	4.6	4.6	1.7	2.9	7.5	-0.4	-0.5
Current Recovery	3.0	2.0(f)	0.3	1.2(f)	9.7	-0.1	-0.5(f)

(f) = forecast * (ppt chng) ** short 1980 cycle not included

Comparing the current recovery one year in to the prior five U.S. recoveries shows that GDP and job growth have been slower than the typical episode (*Table 1*). However, the upturn has by no means been extreme on either front—each of the latest two recoveries was even weaker in the first year. Note that employment actually continued to fall in the first year of the two prior recoveries, and the unemployment rate rose in the first year of recovery in three of the past five cycles. All three of those slow-poke cycles saw growth pick-up markedly in the second year, and—perhaps most optimistically—all five U.S. recoveries saw stronger job gains in the second year of recovery than in the first year. Even the level of unemployment is not at an extreme, as it was higher in the early 1980s cycle.

CHART 2
U.S.: COMPARING CYCLES
(start of recession = 100)



What *is* different in this U.S. economic cycle is the combination of a high jobless rate and a relatively modest growth rebound. Even with the moderate growth of the past four quarters, the level of GDP is still 1.3% below the pre-recession peak, reflecting the deep output losses during the downturn (*Chart 2*). In all five prior cycles, recession losses were long since recouped by this stage of the cycle. And, based on our forecast, it will take another three quarters to bring GDP back to its prior peak. And, yet,

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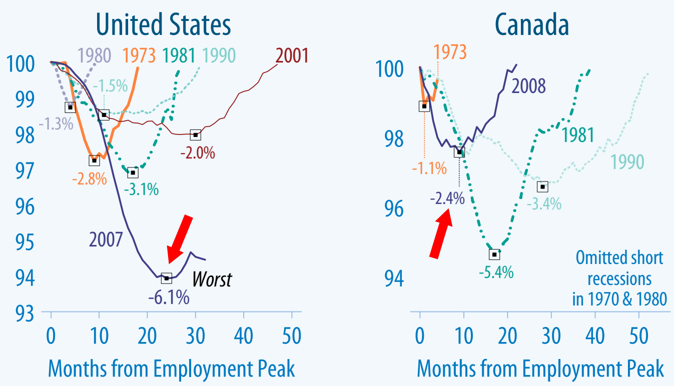
TABLE 2
CANADIAN RECOVERY HISTORY
(percent)

Economic Trough	GDP Growth Year 1	GDP Growth Year 2	Employment Growth Year 1	Employment Growth Year 2	Jobless Rate At Trough	Jobless Rate Year 1 *	Jobless Rate Year 2 *
June 1970	3.6	6.5	1.8	3.1	6.1	0.0	+0.2
Mar. 1975	6.3	2.6	5.9	1.7	6.6	+1.1	+1.1
Oct. 1982	6.2	5.7	3.5	2.0	12.9	-1.6	0.0
Apr. 1992	2.2	4.6	0.1	1.5	10.7	+0.9	-0.7
Nov. 2001 **	3.5	1.5	3.5	1.8	7.6	-0.2	0.0
Average Recovery	4.4	4.2	3.0	2.0	8.8	0.0	+0.1
Current Recovery	3.4	2.3(f)	2.4	1.0(f)	8.7	-0.6	-0.4(f)

(f) = forecast * (ppt chng) ** technically not a recession in Canada; U.S. date used

CHART 3
CHANGE IN EMPLOYMENT DURING RECESSION
(peak = 100)



Dates refer to start of recession

recall from *Chart 1* that the U.S. is further down the road to recovery than Europe or Japan.

Of course, the country at the front of the G7 recovery pack is Canada, where quarterly GDP is now just 0.1% below its pre-recession peak. By almost every measure, Canada has experienced a healthier recovery than the U.S., most notably on the jobs front. The 3.4% y/y rise in GDP is not substantially different from the U.S. growth rate, but it compares well to the recent first-year recovery pattern in Canada (*Table 2*). In contrast, Canadian employment has rebounded forcefully, rising 2.4% from the lows of a year ago. That's actually slow by Canadian recovery standards, but it has outstripped the U.S. pace by a whopping 2 percentage points. Notably, job gains seem to be front-end loaded for Canadian recoveries—in direct contrast to the U.S. history—with job growth often slowing in year two; an outcome we expect to be repeated this cycle. One notable feature of this recovery is the relatively quick retreat in the unemployment rate (the second biggest drop on record in the first year of recovery), in spite of only a moderate GDP rebound. While that's clearly not good news for productivity, the stronger job market has supported consumer confidence and spending this year.

There is little doubt that, along with the housing market, the defining distinction between the Canadian and U.S. cycles has been the labour market performance. *Chart 3* vividly captures how extraordinary this cycle is for U.S. employment, while the Canadian outcome has been positively pedestrian on that front. The August Labour Force Survey revealed that employment has now fully recouped all the recession losses, in less than two years. The early-1980s cycle needed nearly four years to accomplish that feat, and the early 1990s cycle required nearly five years. Meanwhile, U.S. payrolls were still 5.5% below pre-recession peaks in August, a hole that could easily take three to four years to dig out of, even under relatively upbeat assumptions.

Bottom Line: The sluggish U.S. recovery is not especially unusual, either in terms of GDP or jobs growth—what is unusual is the extremely weak starting point combined with so-so growth. However, we believe that rather than fretting about a double dip, the greater concern is that we are facing a long single slog in the U.S. economy. And while Canada has outperformed in the first year of recovery, a swift housing snap-back was a big factor in the relatively strong growth—a factor that won't be sustained.