Something to Cheer This New Year: the Economy

U.S. ECONOMIC DATA FROM THE third and fourth quarters of 2003 showed the economy gaining momentum to speed past the last three years of persistently weak growth and an eight-month recession.

Robust economic fundamentals were due largely to income gains accruing to businesses and money going to households. Previously, income generated by the ongoing surge in productivity was helping companies more than consumers. Moreover, businesses generally sat on their cash instead of using it to finance new capital equipment or hire new workers. That helped explain why the economy fluctuated and consumers felt uncertain about their future in the jobless recovery. But with a solid pickup in demand, businesses were increasingly willing and able to invest in new equipment and expand their payrolls.

The Federal Reserve reported in late November 2003 that economic conditions were improving across the country and appeared to be "reasonably broadly based," with most of the regional Fed districts noting growth in a number of industries.

Also in late November, the Department of Commerce reported revised third-quarter real gross domestic product at an annual rate of 8.2%, while corporate operating profits soared. Profits at U.S. companies rose 30% in the third quarter to more than $1 trillion from $771 billion a year earlier. That was the largest year-over-year growth in profits in 19 years, and it was the first time in history that profits topped $1 trillion.

Among 87 industries tracked by Dow Jones & Co., 66 saw profits improving. Energy and financial companies posed the highest profits collectively. Technology companies more than doubled earnings to $8.9 billion compared with a collective loss of $7 billion in the third quarter of 2002. Soft drink makers saw a 14% increase in reported net income. Industrial companies collectively realized 70% improvement. Cyclical consumer-goods companies reported an 87% improvement. But sectors such as steel, tobacco, and pharmaceuticals deteriorated.

Companies posting rising profits used some of that money to lift their equipment outlays to 18.4%, a pace not seen since the middle of the capital-spending boom in late 1998. Productivity at U.S. companies hit a 20-year high in the third quarter. Nonfarm business productivity grew at a seasonally adjusted annual rate of 9.4%, the Department of Labor said, the strongest showing since the second quarter of 1983, which followed the recession of 1981 to 1982.

Productivity gains weren't entirely due to fewer employees. Workers' hours expanded at the fastest pace in three years. Net employment increased by 57,000 in November, 137,000 in October, and 99,000 in September. That followed seven prior months of job losses totaling 510,000, according to Economy.com. But only when the economy is consistently generating 300,000 jobs per month is strong economic growth sustainable. If that level is reached and maintained for the next year, that would be enough to absorb the nearly three million people out of work who want a job, the Economic Policy Institute reported.

Meanwhile, fewer people filed initial unemployment claims late last year, suggesting a declining trend in unemployment. In late November, new claims for jobless benefits reached a 34-month low. For example, the four-week average of claims in mid-November dropped 9,000 to 367,250, its lowest level since before the recession. Claims are down nearly 100,000 from a 2003 peak of 459,000 set in April. A sustained drop below 400,000 is generally considered to be a benchmark for rising national employment.

But nothing props up the economy more than consumer spending, which accounts for roughly two-thirds of the nation's economic activity. "Personal consumption expenditures," as the Commerce Department calls them, held up well in the last three years. Still, the Conference Board's index of consumer attitudes rose 10 points in November, to 91.7, the highest level in more than a year. Households expressed increased optimism in both their present situation and in the future. In October 2003, U.S. manufacturers saw orders for durable goods—items meant to last three years or more, such as cars—jump 3.3% to $184.5 billion, the largest amount since July 2002.

Finally, business confidence was improving as well, with increased optimism from both businesses and their suppliers, according to Economy.com's regional purchasing manager surveys. In addition, fourth quarter 2003 levels of investment were typically financed internally, standard procedure in the early stages of recovery. Next, debt and equity would likely supplement cash flow, further facilitating investment spending. ■