



The Current and Leading Indices - September 2006

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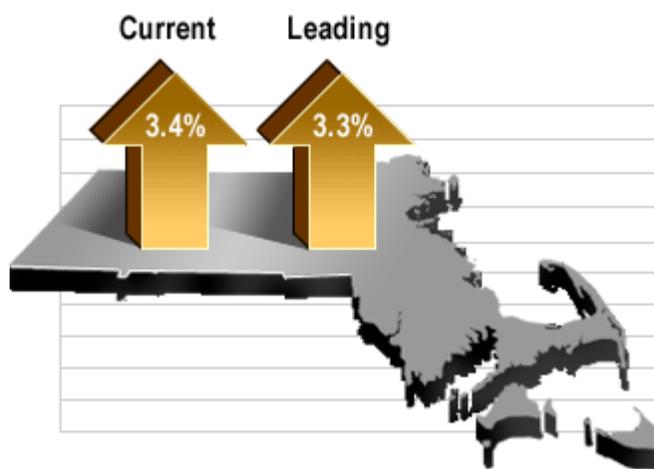
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Bay State Grows at Over Twice the Rate of U.S. in 3rd Quarter

Steady Growth expected through 1st quarter of 2007



The *MassBenchmarks* Current Economic Index for September was 163.3, up 3.4 percent from August (at annual rates), and up 3.4 percent from September of last year. The current index is normalized to 100 in July 1987 and is calibrated to grow at the same rate as Massachusetts real gross state product over the 1978–2003 period.

The *MassBenchmarks* Leading Economic Index for

September was 3.3 percent, and the three-month average for July through September was 2.9 percent. The leading index is a forecast of the growth in the current index over the next six months, expressed at an annual rate. Thus, it indicates that the economy is expected to grow at an annualized rate of 3.3 percent over the next six months (through March). Because of monthly fluctuations in the data on which the index is based, the three-month average of 2.9 percent may be a more reliable indicator of near-term growth.

The state's economy expanded solidly in the third quarter, at an annual rate of 3.4 percent, significantly surpassing the growth of the U.S. economy of 1.6 percent during the same period. This was the third straight quarter of good growth. In the first quarter, Massachusetts gross state product is estimated to have expanded at a 3.4 percent annual rate as compared to 5.6 percent for the nation. In the second, Massachusetts grew at a 3.6 percent annual rate outpacing the U.S. rate of 2.6 percent.

"In the past four quarters, the state has experienced its strongest growth since the recession, lifted by worldwide demand for its technology and science-based products", noted *MassBenchmarks* co-editor and UMass Boston professor, Alan Clayton-Matthews. Payroll employment grew by 1.0 percent in Massachusetts in the last twelve months, twice the annual average rate of 0.5 percent since the employment trough in December 2003 to last September. Massachusetts wage growth has also been strong. Withholding tax-based estimates indicate that per-worker wages grew by 4.7 percent in the past twelve

Recent Index Values

	CURRENT	LEADING
SEP - 05	158.0	2.9
OCT - 05	158.4	2.8
NOV - 05	158.8	2.8
DEC - 05	159.2	2.8
JAN - 06	159.6	3.2
FEB - 06	160.1	3.3
MAR - 06	160.6	3.7
APR - 06	161.0	2.6
MAY - 06	161.5	2.6
JUN - 06	162.0	2.4
JUL - 06	162.4	2.5
AUG - 06	162.9	2.9
SEP - 06	163.3	3.3

months, 1.8 percent faster than consumer prices. This income growth has helped buffer the impacts of high energy prices and a weakening housing market.

The leading index suggests that growth will cool slightly over the next six months, principally due to the effects of a decline in housing prices and its related effects on construction and consumer spending. "The sharp fall in energy prices should help keep the economy from slowing less in the near future than economists previously thought, although this respite may turn out to be short-lived", Clayton-Matthews added.

The 10 indicators that comprise the leading index usually do not all move in tandem. Typically, some may indicate an expectation of faster than average growth, while at the same time others may indicate an expectation of slower than average growth. The following table accounts for the contributions of each towards faster or slower growth than the long-term trend of 3.4%. The index value is their sum.

Contributions of Indicators to the Leading Index

	SEP	JULY - SEP AVERAGE
Trend	3.4	3.4
Total Nonagricultural Employment	- 0.1	- 0.1
Withholding Taxes	0.3	0.2
Sales Taxes	0.0	0.0
Unemployment Rate	- 0.1	- 0.2
Consumer Confidence (New England)	0.0	- 0.1
Interest Rate Spread (10-year less 3-month)	- 0.3	- 0.2
Bloomberg MA Stock Index	0.3	0.1
Initial Unemployment Claims	- 0.1	0.0
Construction Employment	- 0.1	- 0.1
Motor Vehicle Sales Taxes	- 0.1	- 0.2
TOTAL	3.3	2.9

NOTE: Numbers may not add exactly, due to rounding.

In September, two indicators contributed to a forecast of above-trend growth: withholding taxes, and the Bloomberg stock index for Massachusetts. Six indicators contributed to below-trend growth: total nonagricultural employment, the unemployment rate, the interest rate spread between 10-year and 3-month U.S. Treasury securities, initial unemployment claims, construction employment, and motor vehicle sales taxes. Two indicators contributed to average-

trend growth: sales taxes, and consumer confidence.

For the three-month period July through September, two indicators contributed to a forecast of above-trend growth: withholding taxes, and the Bloomberg stock index for Massachusetts. Six indicators contributed to below-trend growth: total nonagricultural employment, the unemployment rate, consumer confidence, the interest rate spread between 10-year and 3-month U.S. Treasury securities, construction employment, and motor vehicle sales taxes. Two indicators contributed to average-trend growth: sales taxes, and initial unemployment claims.

Several recent months of the indices are revised each release. These revisions are a result of the statistical method used to create the index, as well as revisions in the underlying indicators.

All of the indicators except interest rates refer to Massachusetts. The current index is composed of four indicators: nonagricultural employment, withholding taxes, sales taxes, and the unemployment rate. The leading index includes these four current indicators plus the other six (leading) indicators in the contributions table. All of the indicators are as of September except the interest rate spread and the Bloomberg stock index, which are through October 24. The MassInsight Consumer Confidence Index for Massachusetts has replaced the Conference Board's Consumer Confidence Index for New England as a leading indicator. The MassInsight index is released every third month. Intervening months are interpolated. The values for August and September are extrapolated from the MassInsight release for July using changes in the U.S. Consumer Confidence Index from the Conference Board.

For a description of the methodology used to construct these indices, see: Alan Clayton-Matthews and James H. Stock, "An application of the Stock/Watson index methodology to the Massachusetts economy", *Journal of Economic and Social Measurement*, vol. 25 (1998/1999), pp. 183-233.

Alan Clayton-Matthews

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