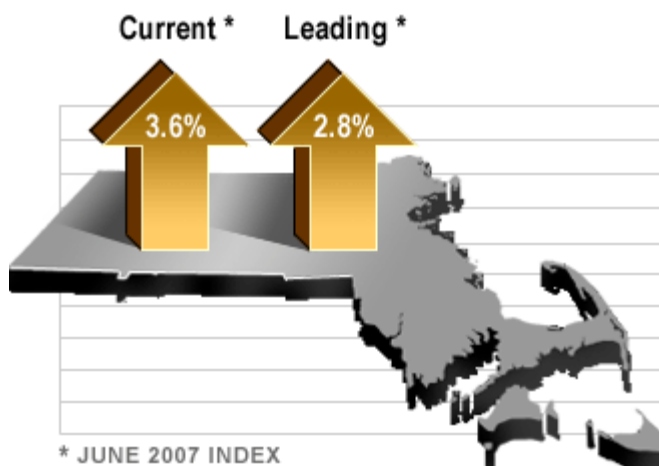




 The Current and Leading Indices - June 2007

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Housing slump restrains state economic growth in the second quarter.


The Massachusetts economy grew at a 3.6 percent annual rate in the second quarter of this year, according to the *MassBenchmarks* Current Economic Index. This is down from a strong 4.1 percent rate in the first quarter. According to the Bureau of Economic Analysis, U.S. real gross domestic product (GDP) grew at an estimated annual rate of 3.4 percent in the second quarter, following a growth rate of 0.6 percent in the first quarter of 2007.

The Massachusetts Current Economic Index for the month of June was 168.1, up 3.6 percent from May (at annual rates), and up 3.7 percent from June 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 domestic product over the 1978–2003 period.

The Massachusetts Leading Economic Index for June was 2.8 percent, and the three-month average for April through June was 3.1 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 2.8 percent over the next six months (through December).

For the rest of the year, the state's economy is expected to continue to expand at a more moderate annualized pace of about 3 percent. Strength in the state's technology, science, knowledge, and health sectors will be partially offset by weakness in residential real estate. Despite improvements in some recent housing market indicators, such as rises in (seasonally adjusted) median prices and declines in inventory of unsold homes (both from the Massachusetts Association of Realtors), the market has not hit bottom yet. Prices are expected to fall further and mortgage delinquencies and defaults are likely to rise as the peak of the subprime lending crisis approaches.

"The Massachusetts economy is being pulled in two

Recent Index Values

	CURRENT	LEADING
JUN - 06	162.1	2.4
JUL - 06	162.5	2.8
AUG - 06	162.9	3.3
SEP - 06	163.4	3.8
OCT - 06	163.9	3.8
NOV - 06	164.5	3.9
DEC - 06	165.0	4.3
JAN - 07	165.6	4.0
FEB - 07	166.1	3.5
MAR - 07	166.6	2.4
APR - 07	167.1	3.0
MAY - 07	167.6	3.5
JUN - 07	168.1	2.8

directions," noted Alan Clayton-Matthews, UMass Boston Professor and co-editor of *MassBenchmarks*.

"On the upside, strong demand for the state's technology-, science-, knowledge-, and health-based goods and services is creating good job and income growth. On the downside, the housing market slump is restraining employment growth and consumer spending in related sectors," Clayton-Matthews added.

These two opposing forces are reflected in differences in recent employment trends by sector in Massachusetts. Employment in computer systems design; management, scientific, and technology consulting; scientific research and development; software; securities, commodity, and investment finance; and health care has been expanding at more than twice the overall payroll employment growth of 1.1 percent over the past year. Employment in sectors related to housing, such as construction, and retail sales of furniture and building materials, have declined over the past year.

Consumer spending tied to the wealth and credit that rising home prices provided has also weakened. This is reflected in June '06 to '07 declines in retail employment in general merchandise stores and motor vehicle and parts dealers, declines in motor vehicle sales taxes, and weak growth in other sales taxes.

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.

In June, one indicator, total nonagricultural employment, contributed to a forecast of above-trend growth. Six indicators contributed to below-trend growth: sales taxes, consumer confidence, the interest rate spread between 10-year and 3-month U.S. Treasury securities, initial unemployment claims, construction employment, and motor vehicle sales taxes. Three indicators contributed to average-

Contributions of Indicators to the Leading Index

	JUN	APR - JUN AVERAGE
Trend	3.4	3.4
Total Nonagricultural Employment	0.2	0.3
Withholding Taxes	0.0	- 0.1
Sales Taxes	- 0.1	- 0.1
Unemployment Rate	0.0	0.1
Consumer Confidence (New England)	- 0.1	- 0.1
Interest Rate Spread (10-year less 3-month)	- 0.1	- 0.1
Bloomberg MA Stock Index	0.0	0.0
Initial Unemployment Claims	- 0.1	0.0
Construction Employment	- 0.1	- 0.1
Motor Vehicle Sales Taxes	- 0.4	- 0.3
TOTAL	2.8	3.1

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

rate, and the Bloomberg stock index for Massachusetts.

trend growth: withholding taxes, the unemployment

For the three-month period, April through June, two indicators contributed to a forecast of above-trend growth: total nonagricultural employment, and the unemployment rate. Six indicators contributed to below-trend growth: withholding taxes, sales taxes, 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: the Bloomberg stock index for Massachusetts, 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 June except the interest rate spread and the Bloomberg stock index, which are through July 18. 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 May and June were extrapolated from the MassInsight release for April using the April to May and May to June 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

July 19, 2007

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