US recession now official: "new economy" expansion one of weakest on record

Nick Beams
28 November 2001

The announcement by the National Bureau of Economic Research (NBER) that the US economy has entered a recession has not just confirmed what was widely felt to be the case. The official ending of the longest period of expansion on record has raised a number of questions as to the nature of economic growth in the decade of the 1990s, particularly the “new economy” of its latter years.

Announcing its decision, the NBER panel, made up of six leading economists, said it was not guided by the commonly used definition of recession—two consecutive quarters of negative economic growth—but looked to employment as the broadest monthly indicator of the state of the economy. The rise in unemployment in October to 5.4 percent from 4.9 percent in September had provided evidence that economic activity turned down. The decline began in the March quarter of this year, making it exactly 10 years since the end of the previous recession at the start of the 1990s.

The NBER statement noted that the cumulative decline in employment was now about 0.7 percent, equivalent to two-thirds of the total decline in an average recession. The fall in industrial production was more marked. This showed a peak in September 2000, followed by a total decline over the next 12 months of close to 6 percent, surpassing the average decline in earlier recessions of 4.6 percent.

While the expansion of the 1990s was the longest recorded—the previous record was the 1961-69 expansion which lasted for eight years and 10 months—it does not compare favourably with other expansionary phases in the post-war business cycle.

In an editorial published on November 1, following the earlier announcement that US growth had declined by 0.4 percent in the third quarter, the *Financial Times* explained that while the expansionary cycle had been hailed as a “miracle” and a “new economy,” the truth was “more mundane.”

The growth rate of 3.1 percent in gross domestic product over the whole cycle “only just exceeded the lacklustre late 1970s”. Compared to the 4.4 percent average growth rate of the 1960s, “recent US growth performance has been paltry.”

The editorial recalled that the early 1990s were frequently characterised as the “jobless expansion”. While there was an element of truth in the claim that greater productivity in the latter part of the decade had allowed the US economy to grow faster, this assumption had yet to be tested in a downturn.

“Just as plausible,” it continued, “is the suggestion that an unsustainable private spending and investment binge created the productivity improvement. As the painful unraveling process gets under way, a productivity growth could be shown to be more mirage than miracle. And a long period of stagnation, or even a deep recession, would then follow.”

An analysis by economist Dean Baker, published by the Center for Economic and Policy Research, explained that even a cursory review of the data showed that the “new economy” was mostly hype.

“For the business cycle as a whole, the average GDP growth rate of 3.1 percent was much lower than in the fifties and sixties, and even slightly below the pace of the seventies ... The nineties cycle only slightly edges out the eighties cycle, which takes last place in the growth category. Annual productivity growth in the nineties cycle was approximately the same as in the seventies, and nearly a full percentage point below the growth rate in the quarter century following World War II.”

Baker noted that the reason the second half of the cycle looked good was because the first half was so bad. “GDP and employment growth in the first half of the cycle were even worse than in the eighties and productivity growth was only slightly better.”

In the nineties cycle, the average real wage of production workers and the median wage both grew by around 0.5 percent annually. This was slower than the 0.8 percent growth rate in the eighties and well below the 1.9 percent growth rate of the sixties.

But there is one area in which the growth cycle of the nineties has exceeded all others. This is the increase in social inequality. By 1999 the top 1 percent of the US population received as much after-tax income as the bottom 38 percent combined. From the mid-1970s the top 1 percent has doubled its share of national wealth from under 20 percent to 38.9 percent. It has been calculated that if wages in the 1990s had risen as fast as the salaries, bonuses and stock options enjoyed by CEOs the average worker would have received annual earnings of $114,000 per year and the minimum wage would be $24 per hour.

In a report on income issued in September, the Economic Policy Institute noted that while household income showed an increase in the years 1997-99, there was no growth in the year 2000. In fact, the earnings of full-time, year-round male workers fell by 1 percent while those of females increased by only 0.5 percent.

Far from laying the foundations for a new era of prosperity as a result of increased productivity, as claimed by the “new economy” proponents, the growth cycle of the 1990s was to a great extent financed by the rapid expansion of debt.

This is indicated by two statistics—the savings ratio and the level of international indebtedness. The private sector deficit, measuring the excess of expenditure over income by both corporations and households, has widened to about 6 percent. This gap has been largely financed by the inflow of foreign capital into the US.

According to figures produced by the Financial Markets Center, measured as a share of GDP “US indebtedness to foreign creditors crossed the 20 percent mark that has traditionally signalled a serious imbalance in the country’s international accounts.”

“The deterioration in the US international accounts,” it noted, “represents the rapid acceleration of a decade-long trend. The US became a debtor nation in 1989 and the level of debt has grown in every subsequent year ... At year-end 2000, the net stock of external debt reached 22 percent, up from 16.4 percent in 1999 and nine percentage points higher than the 12.9 percent recorded in 1997.”

If these figures are anything to go by, it seems that the 1990s growth cycle will go down in history not as the era of the “new economy” but rather as the decade which set in place major structural imbalances in the US economy—imbalances which will have far-reaching implications both for the US and global economy in the coming period.