MACRO PULSE™

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The "Gulliver" Economy

Gulliver was a character in a Jonathan Swift novel who, when washed ashore after being shipwrecked, awoke on the beach only to discover that the island's diminutive inhabitants, the Lilliputians, had tethered him to the ground. Gulliver is a fitting metaphor for the U.S. economy: it survived a "shipwreck" of a recession but numerous risk factors now constrain it from achieving full recovery and could tip it back into recession. Like the Lilliputians' ropes that kept Gulliver prostrate in the sand, any one of those risk factors could hardly prevent the economy from rising to its feet; collectively, however, they prove a formidable restraint. Some of those risk factors include:

• Oil prices – The monthly average U.S.-dollar price of West Texas Intermediate crude oil shot higher in March, to $102.94 per barrel – the highest price since September 2008. If oil prices average $100 a barrel for the year, growth could be 0.3 percentage point lower than if prices had stayed at last year's average of less than $80 a barrel. A few months of $125-per-barrel oil would slash economic growth by a full percentage point, while several months at or above $150 per barrel could push the economy back into recession.

• Employment – Although non-farm payrolls increased by 216,000 jobs in March, many of those new jobs were concentrated in service industries that typically do not pay "economy-sustaining" wages. Not surprisingly, wages grew at their slowest pace in seven years. Moreover, the civilian labor force participation rate remained stuck at its 25-year low for a third consecutive month. Without a substantial infusion of high-paying jobs the economy will remain vulnerable to anemic consumer spending.

• Construction – Residential construction activity was abysmal in February. Total housing starts plummeted to their second-lowest level of activity since the Census Bureau began collecting housing data. In addition, sales of new and existing homes dropped off significantly (to a record slow pace for new homes), causing inventories to rise and prices to fall. About the only good news involved a rise in pending sales of existing homes, but that rise did not offset January's decline. Given the large and expanding disparity between new and existing home prices, a substantial near-term rebound in construction activity is unlikely.

• Manufacturing – Factory output has been one of the bright spots in this recovery, and the expansion appears to be continuing. The sector grew at a slightly slower pace in March, but that rate was near the top of the range of the past seven years. Rising input costs, especially the oil prices discussed above, threaten to put a damper on activity, however. Also, disruptions caused by Japan's devastating earthquake and tsunami are rippling into the United States and could worsen if Japanese suppliers are unable to quickly return affected plants to production.

This report is a compilation of articles posted on our website (http://delphiadvisorsmacropulse.blogspot.com/); those articles relate recent economic developments to the U.S. forest products sector in much greater detail. They also provide context for our complete, 24-month forecast, which is contained in the *Economic Outlook* newsletter available through Forest2Market (http://www.forest2market.com/f2m/us/products/outlook). ■

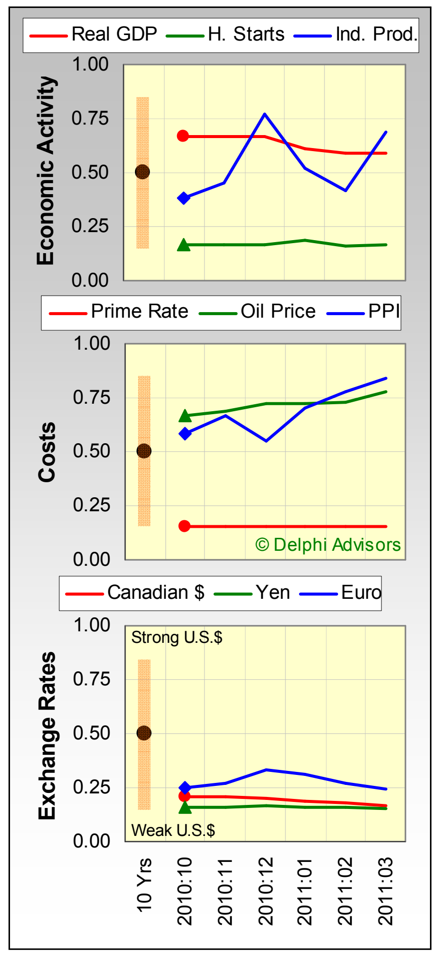

Figure 1. **Previous six month's behavior of macroeconomic variables indexed relative to their historical 10-year min, max and average (lower and upper ends of the orange bars, and black dots, respectively)**