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## **News and Commentary**

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## **The Maine Economy: Facing the Challenge**

*Laurie Lachance*

### **Introduction**

Over the past decade and a half, the Maine economy has been through a period of extreme turbulence, first soaring to new heights then plummeting to what has felt like new lows. The primary factors that had propelled our growth in the eighties--a consumer spending spree, an influx of defense spending dollars, and an unprecedented real estate boom--vanished in 1990, causing the largest job losses in our history. Although the recovery path has been painfully slow and we have not emerged from this recession unscathed, there are indicators that suggest that the new Maine economy is better positioned for long-term viability. We face many challenges going forward, not the least of which is strengthening the balance sheet at every level--personal, business, and state government. But we are making progress, picking up the pieces, developing a plan for the future, and laying a sound foundation for long-term economic prosperity.

### **The Employment Picture**

National employment growth has averaged a slow but respectable two percent annual rate since 1991, growing a full eight percent over trough levels. Unfortunately, U.S. economic growth has been of little solace to the New England region. Nowhere has the term "jobless-recovery" seemed so fitting than in recession-battered New England. After four years of recovery, this region remains at 95 percent of peak employment levels. Only the northern tier states of Maine, New Hampshire, and Vermont have actually recovered the jobs that had been lost in the downturn.

Following an economic slide that lasted through much of 1990 and 1991 and eliminated six percent of the employment base, Maine has been on a fairly slow growth path (see Figure 1). While typical recoveries are marked by a resurgence in economic activity over the 4-6 quarters following the downturn, it has taken Maine four full years to recoup the jobs that had been lost earlier this decade. Although there is growing concern over the relative quality of the jobs that were lost as compared to the new jobs, at least Maine has been made somewhat whole which is much more than can be said for southern New England.

As Figure 2 illustrates, the bulk of all jobs created through the eighties came from the nonmanufacturing sector, led by medical and business services, retail trade, and construction. Manufacturing employment continued to dwindle through the decade with the exception of a work-force build-up at Bath Iron Works in 1988 that bolstered the industrial job figures. The recession took its toll on both sectors as the cyclical downturn combined with defense cutbacks

and industry restructuring to eliminate over 34,000 jobs spread fairly evenly over the services and goods-producing sectors. Maine's job growth going forward is expected to average 1.5 percent, a slightly faster pace than that being seen region-wide. Consistent with the trends experienced over the past several decades, virtually all job growth will be in the nonmanufacturing sector, primarily in business and health services, retail trade, and construction. Ongoing restructuring of Maine's three investor-owned electric utilities and state government will dampen the service sector growth. In the manufacturing sector, only the fabricated metals, food, and instrument industries are projected to see any job gains while the other goods-producing industries will experience stable employment or minor declines.

### **Job Quality and Income Growth**

Despite the fact that Maine employment figures have recovered to their pre-recession level, there remains a good deal of concern over the relative quality of the jobs that have been created. Even a cursory review of the average wage data suggests there is some validity to those concerns. Although wages are not the only measure of job quality, they certainly are a critical component of overall quality and job desirability.

From 1989 to 1994, Maine Department of Labor figures show that there were 10 industries which suffered a combined loss of 27,800 jobs over the five year period. The industries experiencing the largest losses included construction, shipbuilding, paper manufacturing, electrical equipment, lumber and wood products, and leather. These industries paid Maine workers an average annual wage of \$29,227 (1994 dollars) and offered a minimum work week of 38.4 hours. In other words, considering that Maine's average annual wages in 1994 were below \$22,000, the jobs lost in this downturn were predominantly high-paying, full-time jobs.

By comparison, the 10 industries that added the largest number of jobs to Maine's economy from 1989 to 1994 included health, business, social and amusement services, local government, miscellaneous retail, and general merchandise stores. These 10 industries combined to offer Maine workers 22,800 new jobs with an average annual wage of \$19,777 and an average work week of 27-33 hours. The difference in the "quality" of the new job offerings as compared to the jobs that were lost is both striking and disturbing.

Another fact that surfaces from this analysis is that the majority of the jobs lost were in manufacturing and virtually all of the new jobs are in the nonmanufacturing sector. And while it would not be fair to characterize all manufacturing jobs as "good" and all service sector jobs as "less desirable," an analysis prepared for the Economic Growth Council does suggest there is a distinct difference in the average wage rates of the two sectors. The Growth Council's analysis basically assigns a rank to each of the state's 65 industries based on the ability of each industry's weighted average wage to surpass the state and federal poverty threshold for families of two, three, or four people.

If you were to assign ranks of A, B, C, and D to each industry based on average industry wages compared to the six poverty hurdles, you would find that manufacturing jobs, in general, pay higher wages. In fact, 50 percent of all manufacturing categories would earn an A while only 38 percent of the nonmanufacturing categories would rank that high. In addition, not one of the

manufacturing industries would receive a D but a full 15 percent of the nonmanufacturing industries would. Finally, the seven industry groups that receive the less-than-desirable "D" ranking include, restaurants, general merchandise, clothing and food stores, hotels, movie theaters, and amusements, which happen to be some of the industries that are forecast to grow the fastest over the next few years.

So what does all of this mean for Maine? Well, it means we now have a much clearer picture of where to focus our economic development efforts. With these data, informed decisions can and are being made as to which industries should be targeted in the state's long-term development strategy. Through the work of the Economic Growth Council, the King administration, and such groups as the Maine Chamber and Business Alliance, strategies are being developed to enhance Maine's long-term growth potential in industries that offer a brighter future for Maine workers.

In addition, there are some encouraging signs in Maine's recent income statistics. Historically, Maine has been characterized as being a relatively poor state. As Figure 3 shows, through the fifties, sixties, seventies, and early eighties Maine's per capita income as a percent of the national average hovered in the vicinity of 81 percent to 85 percent. During that same time frame, Maine consistently ranked 37th, 38th, or 39th of the 50 states in terms of overall per capita income levels, adding some justification to our "poor state" label. But the unprecedented income growth in New England during the mid-eighties carried Maine to a new income plateau. By the end of the decade, Maine's per capita income had grown to 93 percent of the national average and the state's rank had risen to 25th in the nation. Even with the deep regional recession of the early nineties, Maine has lost some ground but has not returned to the pre-boom income levels.

Looking forward, real per capita income growth in Maine is projected to continue along a slow growth path, averaging one percent to two percent annual increases through the next few years. Analysts hypothesize that the pool of educated, unemployed, or underemployed workers is currently large enough to diminish the bargaining power of the employees, thus keeping wage gains to a minimum.

## **Unemployment**

Relatively high unemployment rates have long been an issue in Maine. The seasonal nature of our natural resource based industries along with our high dependence on tourism cause the state's jobless rate to vary widely through the course of the year, driving up the annual average. With the exception of the mid-eighties when labor markets in the northeast tightened dramatically, Maine's rate of unemployment is usually above that of the nation's and Maine frequently vies with Vermont for the distinction of having the highest jobless rate in the region.

Within our state borders, the variation in the rates of unemployment can also be significant, with the highest county rate being as much as 7.7 percentage points above the lowest county rate. As Figure 4 shows, even in the best of times the relative disparity among counties only closes to 5.2 percentage points. Throughout the past decade and a half, Cumberland County has consistently achieved the lowest jobless rate while Washington and Waldo Counties have shared the distinction of having the highest rates. The good news that can be drawn from Figure 4 is that all counties benefit in times of economic growth. The discouraging news is that there has been no

sustained narrowing of the gap between counties with relatively low unemployment rates and counties with relatively high rates. Exceptionally high unemployment rates persist in certain regions of the state.

As Figure 4 illustrates, Maine's statewide unemployment rate peaked at nine percent in 1983, fell dramatically through the eighties reaching a low of 3.8 percent in 1988, then climbed rapidly through the recessionary period towards a high of 7.9 percent in 1993. Although the jobless rate has drifted slowly downward through 1994 and 1995, no significant improvement is expected in the near-term. Maine's unemployment rate is forecast to continue its slow descent but will remain above national rates for the foreseeable future.

### **Construction and Finance**

Throughout the nineties, the Federal Reserve Board has been very active in "fine-tuning" interest rates to achieve a slow, steady recovery and to keep inflation under control. When the national economy heated up during 1994 and surged towards six percent real gross domestic product growth at the end of the year, the Fed very effectively cooled things down. The Fed's activities also had a chilling effect on states like Maine who have been struggling through this half-paced recovery, and the impact could be seen in several Maine indicators. In 1995, auto sales plummeted and housing permits started to slide. The number of net new businesses fell and the percentage of nonperforming loans ticked upwards. State government revenue collections stalled and consumer confidence started to wane. With the memories of 1990's downturn still vivid, these very indicators have left Maine residents wondering if the economy was headed for another fall.

Fortunately, even with the temporary weakness seen in some of the indicators, the Maine economy of today is much less vulnerable than the Maine economy of 1989. The primary difference lies in the relative health of the region's financial institutions. During the eighties, the New England region experienced a construction boom of incredible proportions. Real estate values appreciated as much as 100 percent in some areas and speculative building flooded the market. When the bottom fell out in 1989, many of the region's financial institutions were left "holding the bag." In fact, the real estate bust had such a devastating effect on the financial sector, that by 1990, only 25 percent of the region's commercial banks and 37 percent of New England's savings banks were profitable (see Figure 5). In addition, from 1990 to 1994, the number of financial institutions serving the region fell from 595 to 454, a drop of 24 percent.

Currently, the shake-out in the region's financial sector is mostly behind us. Maine banks are quite healthy and appear ready, willing, and able to finance economic expansion in this state. A strong financial sector is absolutely critical to our ability to grow and prosper, so this development makes us much less vulnerable and bodes well for future growth.

With this as a backdrop, the outlook for construction activity in Maine is fairly positive. The forecast suggests that residential housing activity will expand at a very slow pace and will be almost entirely single-family units. Our expectation is that the speculative building of the eighties is behind us and a resurgence in the construction of luxurious condominium units is unlikely. Maine non-residential construction contract awards surged through 1995 which is a

good sign for the years ahead. The state's non-building construction contract awards stabilized at a fairly high level in 1995, also a positive indicator.

### **The Challenge...**

Maine has been expanding, albeit slowly, for a full four years. The challenge we now face is how to improve the balance sheets of households, Maine businesses, and state government in a time of slow growth. The bill for our excesses of the eighties just came due and there is no magic mega-bucks drawing that is going to pay it off overnight. That said, we are making progress towards putting our financial houses in order and if we continue to doggedly focus on the ultimate goal of financial viability at every level, we will undoubtedly survive and likely prosper.

### **...for Maine Consumers**

Over the past 10 to 15 years, the American consumer appears to have thrown caution to the wind. Consumer spending increased at phenomenal rates through the prosperous eighties. The savings rate, which had averaged eight percent through the seventies and early eighties, declined to four percent and has shown little or no improvement since. The consumer's willingness to take on debt has risen sharply from 12 percent of personal income during the sixties, seventies, and early eighties to 16 percent in 1989 and towards a new high of 17 percent in 1995. The result? When the recession hit in late 1990, the consumer was totally unprepared.

While we have little Maine-specific data on savings rates and installment credit outstanding, we have no reason to believe that Maine residents have behaved much differently. In addition, bankruptcy filings in Maine grew by 130 percent through the early part of the decade, showed significant improvement through 1993 and 1994, then rose dramatically through much of 1995. While it is impossible to separate personal bankruptcy from business filings, current bankruptcy levels in the Pine Tree State remain at nearly double the pre-recession levels which suggests we still have some issues to work out. In addition, the Maine Omnibus Survey, published by Market Decisions, reports that consumer confidence in Maine fell by 3.6 percentage points during the fourth quarter of 1995 to a level that had not been seen since 1993. With relatively high personal debt levels, slow income growth, and waning confidence levels, the Maine consumer should not be counted on for a major spending surge in the near future.

On a more positive note, the longer-term demographic trends suggest that, once we have worked through the current financial issues at the household level, the Maine consumer will be much better positioned. By the year 2000, the baby boom will be fully in its peak spending years.

### **...for Maine Businesses**

Perhaps the most encouraging news comes from Maine businesses. While few would report record breaking growth, many Maine businesses have seen dramatic improvement in their business balance sheets. Estimated corporate income tax payments have been very strong in recent months which suggests a level of performance that Maine businesses have not seen in some time. Although we continue to see restructuring activities in several of the state's largest employers, the downsizing appears to be more in an effort to prepare for longer-term viability

than in response to financial losses. For example, the reports on the recent downsizing activities at L.L.Bean and the Portland Newspapers both cited sales growth and reasonable profits, however, neither sales growth nor profit levels were as high as had been expected. Many businesses feel that if they are going to truly compete, rather than just survive, in this new global economy, they have to trim management layers and increase productivity wherever possible.

There are other encouraging signs as well. There are a number of paper industry expansions being planned in the near future. Over the last few months, there have been six new applications filed for State Tax Increment Financing. If all are approved, approximately 1,800 new jobs will be created in Maine. About 800 of those jobs will offer average annual wages at the \$18,000 level. The remaining 1,000 opportunities are expected to pay closer to \$44,000 per job. This will be a tremendous boost for Maine workers. In addition, the King administration's "Plus 1" development program for small businesses includes proposals for a job creation tax credit and a small enterprise growth loan fund, providing the thousands of Maine's smaller businesses with an incentive to expand. The best news here is that if Maine business is able to grow and prosper, the problems of Maine State Government and Maine households will be mitigated.

### **...for Maine State Government**

The primary challenge for Maine State Government is to continue along this extremely difficult path of fiscal responsibility. Given that a full 80 percent of Maine State General Fund Revenues are derived from either the sales tax or the personal income tax, and given that both income growth and consumer spending increases are expected to be minimal, state government will likely be facing very slow revenue growth in the foreseeable future. Efforts to cut costs, such as the work of the Productivity Realization Task Force, will be absolutely essential in preparing state government for long-term viability.

### **Summary**

The challenges facing the Maine economy are formidable, but not insurmountable. Although the recession of the early nineties was devastating and the after shocks continue to reverberate, Maine emerges with a stronger foundation for growth. Our real estate sector is no longer poised for disaster. Our financial institutions are very healthy and are capable of financing economic expansion. Our state government has followed the lead of the business sector and is trimming costs and putting its financial house in order. Several large businesses are expanding, offering a number of new job opportunities. The Economic Growth Council and the Maine Chamber and Business Alliance have developed a long-term plan and the King administration has developed the shorter-term strategies to focus our economic development efforts and to better utilize our scarce economic development resources.

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