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Economic Commentary

Claims Not Signaling Recession

When it comes to measuring the strength of the economy, no data tell us as much and as often as the Labor Department's weekly figures on new claims for unemployment insurance.

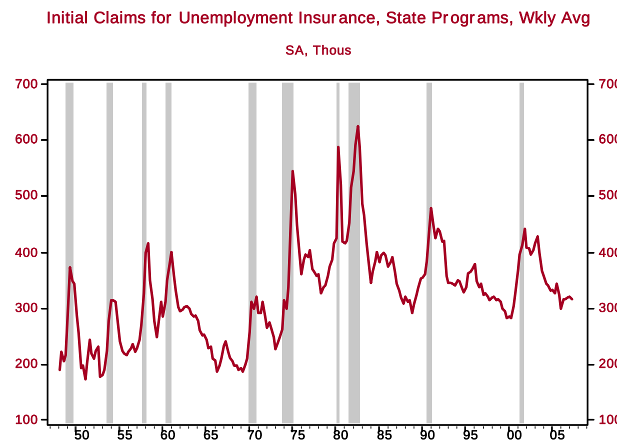
Many indicators give us more specific information about the economy – retail sales, industrial production, the monthly employment report and, of course, GDP itself. But all of these reports come out less frequently than the claims data and well *after* the month or quarter they describe. In contrast, the claims data offer a "real time" glimpse – and perhaps leading forecast – of the growth rate of the economy.

Last week, new claims for unemployment insurance increased 4,000 to a seasonally-adjusted level of 319,000. The four-week average of initial claims fell 1,000 to 324,000. If claims come in at this 324,000 level for the next three weeks they will average 318,000 for Q3 as a whole, versus an average of 317,000 in Q2.

A simple statistical test suggests that when the level of claims remains stable the economy is growing at an annual rate of roughly 3%. Stable claims data indicate that the economy is running smoothly and that normal friction in the labor markets is generating a steady number of layoffs and job losses.

Interestingly, this signal from claims is exactly in line with our "add-em-up" forecast of 3% real GDP growth in the third quarter (see First Trust's _Monday Morning Outlook: Solid Growth Continues in Third Quarter_, September 4, 2007).

Claims are the "canary in the coal mine" of economic indicators. With one understandable exception, the first full month of every recession since 1957 has had new unemployment claims at least 16.2% higher than the same month the previous year. The lone exception was 1981, when claims were already high from the recession of 1980.



Source: Department of Labor /Haver Analytics

This does not mean that a 16.2% rise in initial claims automatically signals a recession is underway. However, it does create a mark for comparison, and in August 2007 initial claims were only 2.2% above the level in August 2006.

For claims to get to the 16.2% trigger, they would have to rise to about 370,000 and stay there for at least several weeks. Nonetheless, this 16.2% trigger has issued a couple of false alarms in the past, where claims rose but the economy did not lapse into recession. So, in the unlikely event that we reach the 370,000 level, a recession is still not a certainty.

Initial claims are a volatile series as the chart above shows. But, the behavior of initial claims during the recent period of market turmoil suggests nothing other than the continued resilience of the U.S. economy.

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