

their profit productivity substantially. Banks have offered wider varieties of financial services. These additional services or higher service quality may have increased costs but also increased revenues by more than the cost increases. Although the evidence is still being generated, it appears that those banks involved in merger activity had greater profit productivity improvements than other banks. Merging banks may have been able to shift their portfolios into higher risk and therefore higher expected return investments to exploit the advantage of diversification gains from the merger.

What will integration of financial services between banks, brokerages, and insurance companies mean? A review of the empirical evidence of the risk-return tradeoffs in increasing banking services to include other financial activities is summarized in **Table 6**. It is important to note that the evidence is based on nonbank financial institutions not affiliated with banks. It appears that by broadening banking firms' revenue base, earnings can be improved. On the other hand, we must be careful to not compromise bank safety and soundness.

As we move into the 21st century, public and private organizations in other cities and states are being as aggressive as Indianapolis in the promotion of new technologies and product development. As economist Hal Varian writes, "The great fortunes of the information age lie in the hands of companies that have successfully established proprietary architectures that are used by a large installed base of locked-in customers."

Fort Wayne

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Last year's *Outlook* article noted, "It is difficult to identify a likely source of significant growth for the area economy in 1999.... The twin problems from the Asian flu—lackluster demand for our exports and increased competition from imports—will be quite troublesome to the manufacturing sector...."

According to preliminary employment data, the six-county Fort Wayne area economy experienced no growth in 1999. Specifically, the preliminary estimate of employment in September 1999 was 274,900 versus 275,000 a year ago.¹

As forecast, the trouble spot has been manufacturing employment. It decreased 1,000 during the period. The preliminary estimate of manufacturing employment in September was 75,100. Wholesale and retail trade employment also declined 600 to 63,800 as of September.

According to the preliminary data, those losses were largely offset by an increase of 1,300 in the catchall services category. It includes both business and personal services employment.

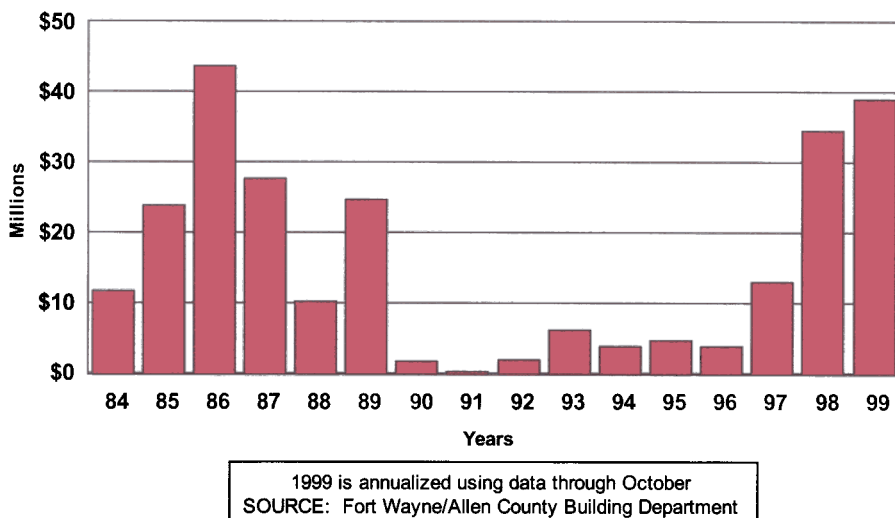
Is the preliminary judgment of no growth in employment accurate? Housing construction data cast some doubt. Construction of new housing is at a record pace in 1999. Permits for new, single-family housing in Allen County in 1998 almost beat the record of 1,984 set 20-years earlier, and 1999 permits are currently on a pace to beat the record nominally.

Additionally, the previously moribund condominium and apartment construction has been resuscitated. Two years ago, there was essentially no new construction and now the record spending of approximately \$44 million set back in 1986 is being challenged (see **Figure 1**). Certainly, \$44 million in 1986 dollars produced more housing than \$44 million in 1999 dollars; however, the recovery is still impressive.

Factors favoring a robust new housing market abounded in 1999: favorable mortgage rates, appreciation in housing prices (causing equity to increase), and outsized gains in the stock market.

Not so understandable is who is occupying either the new houses and/or the older houses being traded in if the preliminary employment data are correct. The data suggest no increased demand from new hires. Are the preliminary employment data low, or is their some unusual phenomenon occurring

Figure 1
Annual Dollar Value of Condominium and Apartment Construction in Allen County, 1984 to 1999



within the housing sector? Maybe older housing is being destroyed at an atypical rate or maybe builder speculation is driving the sector.

Having an answer would certainly be helpful in developing a forecast for 2000, but that's not possible at this time. My bias is that 1999 employment ultimately will be revised upward, and that probably speculation has crept into the new housing market. Ten years of uninterrupted success will do that.

Even if 1999 employment ultimately is revised upward it won't be large, and therein also lies the logic for what is likely to happen to the area economy in 2000. That the cupboard of excess labor in the Fort Wayne area is bare is obvious. The unemployment rate in the Fort Wayne area has been running approximately two percentage points below the U.S. unemployment rate since 1993. In September it was 2.5 percent, not seasonally adjusted.

Yearly population estimates since the 1990 census suggest that the Fort Wayne area population is growing between 0.5 and 0.7 percent annually. This is about half the growth rate for the U.S., and it is consistent with the fact that the Fort Wayne area has not been a mecca for in-migration. Thus, the principal source of population growth is the excess of births over deaths.

If everyone wanting a job is already employed, then the labor force is likely to grow at approximately the same rate as the population, ignoring age discrepancies. This means an increase of between 875 ($.005 \times 175,000$) and 1,225 ($.007 \times 175,000$) per year.

Now the only question relative to the 2000 forecast for the Fort Wayne area economy is whether the U.S. economy will grow sufficiently to create demand for increased employment between 875 and 1,225. Probably, any balanced growth in U.S. GDP of at least three percent will do that. The logic also suggests that whether U.S. GDP growth is three percent or five percent won't make that much difference to area economic performance.

Balanced growth requires that the manufacturing sector participate fully, and that appears likely in 2000. The twin problems noted in the opening paragraph are reversing. Foreign demand—especially Asian and European—for U.S. manufactured goods is growing again and a falling dollar is making U.S. manufactured goods more competitive.

Trying to analyze the manufacturing sector can be confusing. For the U.S., manufacturing employment decreased 19,000 monthly in 1998 and it has decreased 29,000 monthly in 1999. One might assume then that production of manufactured goods has been decreasing, but that isn't the case. Actually, production has been increasing at approximately a five percent annualized rate. How can this be? The answer is that productivity in the manufacturing sec-

tor has also been increasing at approximately a five percent annualized rate, so the increased production can be obtained with the same or fewer employees.

Obviously, these trends have a tremendous impact on the potential for employment growth in the Fort Wayne area because it has an outsized dependence on manufacturing.

Can Fort Wayne employment grow faster than 1,250 annually? It's possible, but not probable. Possibilities include a company moving to the area and bringing its employees or \$100,000 jobs to be filled locally. The latter would cause a one-time increase in the labor force as additional people chose work over leisure, but the interesting question is whether the Fort Wayne area has a sufficiently skilled labor force to fill the \$100,000 jobs.

What's the downside risk to the forecast? Accelerating inflation and the rising interest rates that will result! Wage growth is accelerating. For example, the UAW just signed an agreement that gives three percent annual increases plus a cost of living adjustment. Crude oil prices have doubled and OPEC's share of the market (and resulting pricing power) has increased. As the managed part of managed care is reigned in, it appears likely that the health care industry may start adding to inflation again rather than subtracting from it. Finally, commodity prices are starting to increase.

Note

1. Not seasonally adjusted

Columbus

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State of the National Economy

After successfully avoiding last year's global financial crisis, the U.S. economy continued to steam along at a remarkable rate. While the Asian, Russian, and (to a lesser degree) Latin American economies were trying to climb out of their financial debacle, the U.S. economy posted an astonishing 6.01% annual growth rate in the fourth quarter of 1998, followed by a strong 4.3% in the first quarter of this year. While growth in the second quarter of 1999 leveled off to a modest but positive annual rate of 1.9%, growth in the third quarter beat expectations as it rebounded to a robust 4.8%.