The American economy faces steep and continuing difficulty in its path to recovery. Employment as a share of total population has been static or declining throughout 2012. With unemployment rates continuing to hover around 8 percent, there is mounting evidence that structural unemployment (a skills mismatch) plays a larger role in soft labor markets than previously believed. Moreover, Europe remains in recession, with unemployment rates at 50-year highs, while slow growth in BRIC nations suggest that much of the world shares our economic virus. These difficulties are magnified by the deepest policy uncertainty in decades. Lack of reasonable insight on such basic factors as tax rates in the coming days can only act to disincentive domestic investment and employment. This is a difficult landscape for the national economy.

For these reasons, our models suggest that unemployment rates will remain roughly where they are now throughout the coming year, with any relief in rates coming primarily from a dwindling labor force, not job creation. Real GDP growth will average 2 percent, roughly the rate of productivity growth. Inflation will not be an issue this year, nor will there be significant changes to borrowing costs.

A national recession remains highly likely this year. Though economic models have performed poorly in capturing economic turning points, either the composition of the ‘fiscal cliff’ or a sustained European recession alone are significant enough to push our economy into recession.

Over the long run (through 2025), we expect more of the same. We anticipate GDP growth will remain at roughly 2.5 percent and employment growth at less than 1 percent over this horizon.

GOING OVER THE FISCAL CLIFF

A tax increase and spending cut similar to the current fiscal cliff debate will lead us into a recession. Nominal GDP will drop to the negative range in 2013, and remain a full point behind the long-term level through 2017 (or fiscal cliff model horizon). Employment will decline, and then rebound, remaining sluggish under either scenario through the forecast horizon.

...Either the composition of the ‘fiscal cliff’ or a sustained European recession alone are significant enough to push our economy into recession.
THE HOOSIER ECONOMY

Indiana’s economy has outperformed the nation as a whole in GDP growth and employment growth over this recession. However, our model suggests a mixed future. Overall economic activity in Indiana will continue to exceed the national average through much of this decade, slowing somewhat between 2018 and 2025. During this time period, employment growth will lag the nation as a whole. The explanations for this are fairly straightforward. First, labor force constraints will limit labor-intensive business expansion. Slower population growth is the most visible sign of this problem, but it is a nuanced concern, involving both the attractiveness of many of the state’s regions to workers and the overall human capital levels in the state. Second, the state’s most intensive industries are those that continue to experience high levels of productivity growth, thus dampening demand for workers.

THE SHORT-TERM OUTLOOK

In the short run, we expect a decline in personal income in durable goods manufacturing, retail, transportation, information and finance, insurance, and real estate sectors. We expect growth in mining and utilities, construction, health care, and non-durable goods manufacturing. Overall we expect personal income growth of 2.4 percent next year, followed by growth of 2.1 percent in 2014. Unemployment in the state will remain sticky, with an average annual rate of 7.8 percent and a lower rate of 7.2 percent in 2014. However, the same cautionary tales regarding Europe, BRIC nations, and the fiscal cliff apply.

Indiana is a significant exporter of goods to the European Union, with more than 2 percent of GDP destined for Europe. Their recession will reduce demand for these goods and demand for employment in these firms. The slow growth in China and India add to lower demand for our goods.

Indiana is susceptible to major shocks with both spending cuts and tax increases. Domestic and defense spending cuts will likely affect services for the poor and public infrastructure grant programs. Likewise, defense spending may well impact the state, with the potential for significant cutbacks at U.S. Navy and joint training centers in southern and southwestern Indiana. Also, cessation of planned acquisition of aircraft, ground weapons systems, and electronics may also impact civilian employment in many businesses within the state.

The Indiana economy in 2013 will, at best, look much like it does today, with roughly 8 percent of Hoosiers unemployed and little or no prospects for rapid economic growth.

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EAST CENTRAL INDIANA

The forecast for east central Indiana (see map) through 2025 reflects a continuation of the trend of slow population and personal income growth. While the region as a whole will grow through 2025, virtually all the economic activity will occur in the county most proximal to the Indianapolis metropolitan area (Madison). The remaining east central Indiana counties will continue to experience population declines throughout the forecast horizon, with nearly uniformly accelerating population declines in the latter half of the forecast horizon.

Overall economic conditions continue to stagnate, following steep employment declines in the early 2000s. However, a secular trend towards smaller populations, smaller businesses, and reduced levels of high value-added production has gripped the region for more than a generation. Economic transition throughout most of the region has been elusive. While some areas (e.g. Jay County) have continued to see relatively stable levels of manufacturing employment, and others (e.g. Delaware County) have seen important new job announcements in manufacturing, the region as a whole has not adapted to the structural changes facing it. Even communities that are expected to see population growth through the forecast period face infrastructure constraints on new residential development.

Despite relatively robust state level economic performance through this business cycle, the region’s level of unemployment remains a drag on local conditions, and overall supply concerns regarding available human capital remain among the greatest impediments to economic growth in east central Indiana.

Please see the next page for figures 2 and 3.

While some areas have continued to see relatively stable levels of manufacturing employment, and others have seen important new job announcements in manufacturing, the region as a whole has not adapted to the structural changes facing it.

FIGURE 1. MAP OF INDIANA’S EAST CENTRAL REGION

Source: U.S. Geological Survey and CBER Publications

TABLE 4. PERSONAL INCOME AVERAGE ANNUAL GROWTH RATE

<table>
<thead>
<tr>
<th>County</th>
<th>2013–2018</th>
<th>2019–2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>Blackford</td>
<td>0.27%</td>
<td>1.24%</td>
</tr>
<tr>
<td>Delaware</td>
<td>0.65%</td>
<td>1.63%</td>
</tr>
<tr>
<td>Grant</td>
<td>0.05%</td>
<td>0.01%</td>
</tr>
<tr>
<td>Henry</td>
<td>1.10%</td>
<td>1.30%</td>
</tr>
<tr>
<td>Jay</td>
<td>3.40%</td>
<td>4.73%</td>
</tr>
<tr>
<td>Madison</td>
<td>1.00%</td>
<td>2.01%</td>
</tr>
<tr>
<td>Randolph</td>
<td>0.66%</td>
<td>1.67%</td>
</tr>
<tr>
<td>Wayne</td>
<td>-2.05%</td>
<td>-1.31%</td>
</tr>
<tr>
<td>East Central Region</td>
<td>1.08%</td>
<td>1.74%</td>
</tr>
</tbody>
</table>

Source: Bureau of Economic Analysis and author’s calculations

TABLE 5. POPULATION AVERAGE ANNUAL GROWTH RATE

<table>
<thead>
<tr>
<th>County</th>
<th>2013–2018</th>
<th>2019–2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>Blackford</td>
<td>-0.59%</td>
<td>-0.61%</td>
</tr>
<tr>
<td>Delaware</td>
<td>-0.30%</td>
<td>-0.31%</td>
</tr>
<tr>
<td>Grant</td>
<td>-0.44%</td>
<td>-0.45%</td>
</tr>
<tr>
<td>Henry</td>
<td>-0.23%</td>
<td>-0.23%</td>
</tr>
<tr>
<td>Jay</td>
<td>-0.29%</td>
<td>-0.30%</td>
</tr>
<tr>
<td>Madison</td>
<td>0.54%</td>
<td>0.67%</td>
</tr>
<tr>
<td>Randolph</td>
<td>-0.37%</td>
<td>-0.39%</td>
</tr>
<tr>
<td>Wayne</td>
<td>-0.33%</td>
<td>-0.35%</td>
</tr>
<tr>
<td>East Central Region</td>
<td>-0.10%</td>
<td>-0.07%</td>
</tr>
</tbody>
</table>

Source: Bureau of Economic Analysis and author’s calculations
FIGURE 2. COUNTY PERSONAL INCOME, 1969–2025, IN 2011-CONSTANT DOLLARS

FIGURE 3. COUNTY POPULATION, 1969–2025

Source: Bureau of Economic Analysis and author's calculations