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Sharp Drop in Jobs Adds to Grim Economic Picture

Kevin P. Casey for The New York Times

The Labor Department estimated that the nation lost 63,000 jobs in February, sending many to job fairs like this one in Seattle.

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By EDMUND L. ANDREWS
Published: March 8, 2008

WASHINGTON — The worst fears of consumers, investors and Washington officials were confirmed on Friday, as deepening paralysis on Wall Street collided with stark new evidence of falling employment and a likely recession.

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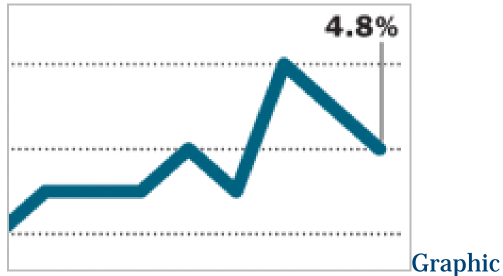

Graphic

Labor Picture in February

In a report that was far worse than most analysts had expected, the Labor Department estimated that the nation lost 63,000 jobs in February. It was the second consecutive monthly decline, and the third straight drop for private-sector jobs.

Even before the bad news on jobs emerged, the Federal Reserve was already racing to ease the latest crisis in the credit markets, where seemingly rock-solid companies have been caught short because the markets are devaluing the collateral they had posted to back billions of dollars in loans. Much of that collateral consists of mortgages.

In a surprise announcement early Friday, the Federal Reserve said it would inject about $200 billion into the nation's banking system this month — with more to come after that — by offering banks one-month loans at low rates and in return letting them pledge mortgage-backed bonds and even riskier assets as collateral.

Though monthly payroll data are notoriously volatile and subject to revision, the jobs report was so bleak that many of the few remaining optimists on Wall Street threw in the towel and conceded that the United States was already in a recession.

"Godot has arrived," wrote Edward Yardeni, who had been one of Wall Street's most relentlessly upbeat forecasters. "I've been rooting for the muddling through scenario. However, the credit crisis continues to worsen and has become a full-blown credit crunch, which is depressing the real economy."

The convulsions in the credit markets were spurred in part when Thornburg Mortgage, one of the nation's biggest independent mortgage lenders, and Carlyle Capital, the offspring of one of the country's largest private equity firms, failed to meet demands by lenders to post more cash or pledge other assets, also known as margin calls, on debts that had been backed by packages of mortgages.

Fed officials said Friday that they were not pumping money into the system in response to the poor jobs data but rather to the growing unwillingness or inability of investors to finance even routine business deals. Fed officials have long feared that anxiety about credit losses would create a "negative feedback loop," or self-perpetuating spiral of rising unemployment, more home foreclosures and yet more credit losses.

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"There is no denying that when you get negative job numbers, realistically the economy is less strong than we had hoped it would be," Mr. Lazear said. "The question is how quickly will it pick up. We think it will pick up — as I mentioned, we think it will pick up by the summer."

Skip to next paragraph

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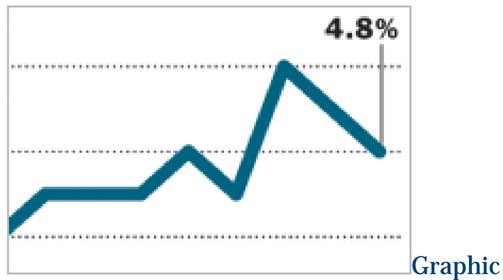

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Labor Picture in February

Few private forecasters were so buoyant. Many firms had already concluded that a recession was under way. Within minutes of the new report on employment, many in the dwindling pool of optimists changed their positions.

Mr. Yardeni was hardly alone. Just one minute after the Labor Department published its report at 8:30 a.m., JPMorgan Chase reversed its stance, declaring that a recession appeared to have begun. Lehman Brothers switched its position as well.

Unemployment typically starts to rise only after a recession has started, and it keeps climbing for many months after the economy has hit bottom and begun to recover.

Paul Ashworth, an economist at Capital Economics, noted that private-sector payroll employment has now declined by an average of 47,000 a month — a decline that has been followed by a recession every time it has happened in the last 50 years. In each of those recessions, Mr. Ashworth added, the job market recovered only after monthly job losses peaked at 200,000 jobs.

Ben S. Bernanke, chairman of the Federal Reserve, had already sent clear signals in recent weeks that the central bank was ready to reduce the overnight federal funds rate when policy makers meet on March 18.

Since August, the Fed has sharply cut overnight rates five times, to 3 percent from 5.25 percent, and investors have been all but assuming that the central bank would reduce them by at least another half a percentage point, and perhaps three-quarters of a point, at the next meeting.

But by Thursday, Fed officials had become increasingly alarmed that rates for many kinds of lending were skyrocketing as investors demanded steep risk premiums that are normally associated with a serious economic recession.

What particularly alarmed Fed officials was that the margin calls on Carlyle Capital and Thornburg Mortgage had stemmed from plunging confidence about the value of highly conservative mortgages that were guaranteed by Fannie Mae and Freddie Mac, the giant government-sponsored mortgage companies.

If investors lose confidence in Fannie Mae and Freddie Mac, which have become the only major remaining source of mortgage financing in recent months, Fed officials fear that home sales and housing prices could plunge further and foreclosures could climb even higher than they already have.

On Thursday, the Mortgage Bankers Association reported that about 7.9 percent of all loans — a record high — were past due or in foreclosure. Until the third quarter of last year, the rate had not climbed above 7 percent since 1979.

Home prices are falling in almost every part of the country, a phenomenon that Fed officials and many other experts until recently thought was all but impossible, and some analysts now predict that average home prices will ultimately fall 20 percent from their peak in 2006.

The effect is reducing household wealth. According to data this week from the Fed, net household wealth declined by $900 billion in the fourth quarter of last year.

Indeed, the ratio of homeowners' equity to the value of their homes fell below 50 percent for the first time in history last year, according to the Fed. Far more alarming, however, is that about 30 percent of all homes bought in 2005 and 2006 are "under water," meaning they have mortgages that are higher than their resale value.

"We're at the beginning of the bursting of the housing bubble," said Dean Baker, co-director of the Center for Economic and Policy Research, a liberal research organization in Washington. "The rate of foreclosures is just going to increase as time goes on."

Eric S. Rosengren, president of the Federal Reserve Bank of Boston, noted that the housing calamity thus far has occurred even though unemployment is still low, at just 4.8 percent. But a surge in joblessness would almost certainly lead to more foreclosures and more downward pressure on home prices.

"A downside risk that we do need to consider is whether a rising unemployment rate generated by slow growth will force some people to sell their houses, creating further downward pressure on housing prices," Mr. Rosengren said in an interview.

In opening up its monetary spigots on Friday, the central bank left little doubt that it wanted to increase the money for mortgage lending.

Its first move was to offer up to $100 billion through the Term Auction Facility, a program created in December that allows any bank or savings and loan to bid for loans at what amounts to wholesale rates and allows them to pledge a wide variety of securities — including mortgage-backed securities that are not tradable at the moment — as collateral.

The central bank's other new initiative is to lend an additional $100 billion in March through its open-market operations. That money is available only to primary dealers, a few dozen major investment banks, but the loans can be secured by certain mortgage-backed securities, like those issued by Fannie Mae or Freddie Mac.

Fed officials said they were prepared to infuse even bigger sums of money into the financial system if they see a need, and the central bank said it was in "close consultation with foreign central bank counterparts" — a hint that it might seek support from other central banks if the credit problems persist.

« Previous Page

- 1
- 2

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