

Current Economic Conditions in the Eighth Federal Reserve District

Memphis Zone

September 17, 2008

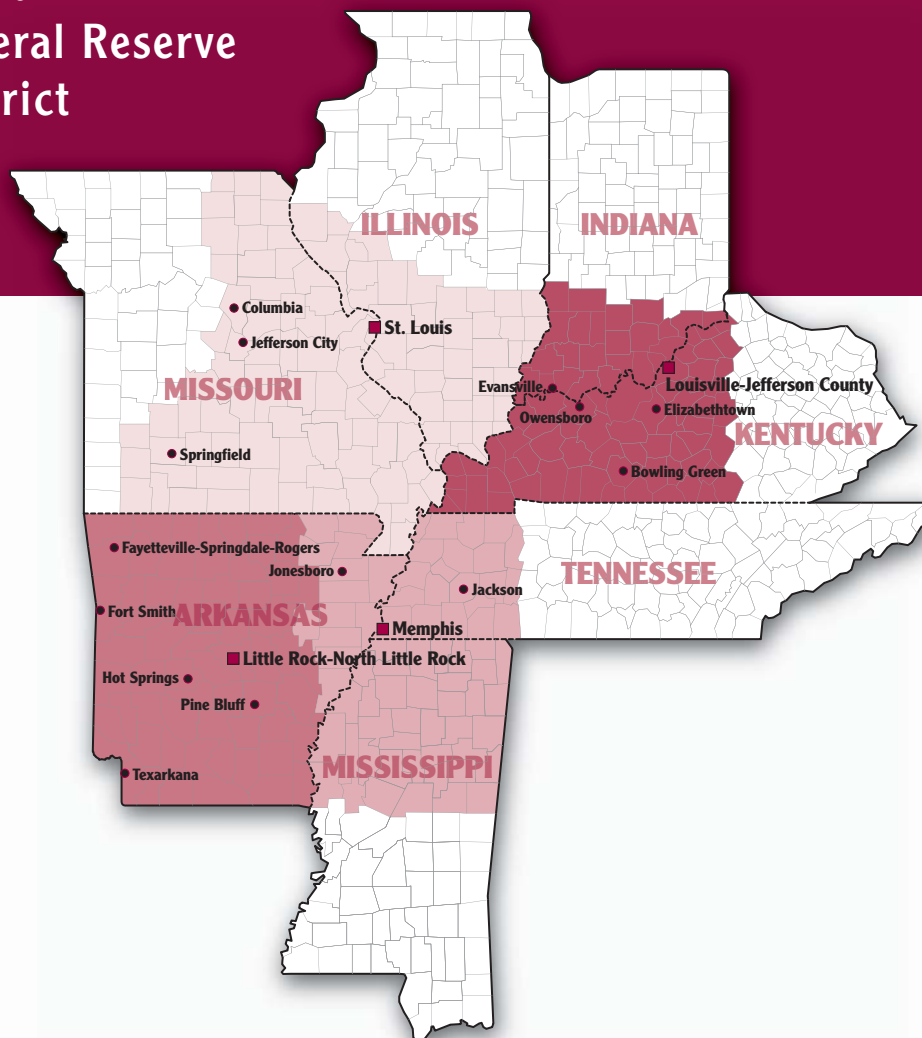
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CRE8

Center for Regional Economics—8th District



Eighth Federal Reserve District



This report (known as the *Burgundy Book*) summarizes information on economic conditions in the Memphis zone of the Eighth Federal Reserve District (see map above), headquartered in St. Louis. Separate reports have also been prepared for the Little Rock, Louisville, and St. Louis zones and can be downloaded from the CRE8 web site (research.stlouisfed.org/regecon/).

The first section of this report summarizes information provided by various contacts within the District and is similar to the type of information found in the Fed's *Beige Book* (federalreserve.gov/fomc/beigebook/2008/). The period covered by this section coincides roughly with the two *Beige Book* periods immediately preceding this report. The second section includes government-provided data for the metro areas and states of the Memphis zone. These data are the most recent available at the time this report was assembled.

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Memphis Zone Report—September 17, 2008

Economic conditions in the Memphis zone continued to soften during the third quarter of 2008. Manufacturing activity decreased across a broad range of industries, and the service sector showed signs of weakness in some areas. Reports from retailers and car dealers indicated reduced sales for July and the first half of August, compared with sales a year ago. Residential real estate market conditions have continued to deteriorate since our previous report, but commercial real estate market conditions showed no signs of weakening. Reports from banking contacts were mixed.

Consumer Spending

Reports of retail sales for July and the first half of August were mostly negative among general retailers and car dealers in the Memphis zone. About 83 percent of the general retailers and all car dealers surveyed indicated that sales were down compared with the same months in 2007; the remaining 17 percent of general retailers reported flat sales. Among the general retailers, 25 percent noted that sales levels met their expectations, but the other 75 percent reported that sales were below what they had anticipated. About 83 percent of car dealers reported more rejections of finance applications. Half of the general retailers and two-thirds of the car dealers reported that their inventories were too high; most of the remaining contacts reported that their inventories were at desired levels. The sales outlook for September and October was mostly pessimistic among both general retailers and car dealers.

Manufacturing and Other Business Activity

Manufacturing in the Memphis zone declined during the third quarter of 2008, with job losses in a broad array of industries and a large number of plant closures. A firm in the aerospace product manufacturing industry reported plans to hire additional workers due to increased demand. In contrast, a contact in the auto parts manufacturing industry reported plans to lay off workers and decrease operations. Firms in the appliance, structural metals, apparel manufacturing, plastics products, animal slaughtering/processing, auto parts, and building supplies manufacturing industries announced plans to close plants in the zone and lay off workers.

The service sector showed signs of weakness in some areas. Contacts in the transportation and warehousing industry, financial services, and business support services reported plans to expand operations and hire additional workers. However, firms in the health care assistance, education, architectural, and technical consulting services industries announced plans to cut jobs.

Real Estate and Construction

Compared with the same period in 2007, year-to-date home sales in Memphis declined by 20 percent in July 2008 while year-to-date single-family housing permits declined by about 56 percent. The second-quarter 2008 industrial vacancy rate in Memphis decreased over the first quarter of 2008. During the same period, the suburban office vacancy rate increased while the downtown office vacancy rate decreased. A large commercial contractor reported that 2009 contracts are on track to beat record-breaking 2008 revenues. A contact reported that commercial construction in Jackson and Madison counties in Tennessee remains strong compared with 2007, but believes that tornado damage from February 2008 is a primary driver.

Banking and Finance

Banking conditions in the Memphis zone were mixed during the third quarter of 2008. Contacts reported varying levels of demand for consumer loans, ranging from unchanged to a modest decrease. All contacts reported decreases in the demand for business loans. A number of contacts also expressed concern over tightened lending standards. Most contacts indicated little to no change in the demand for residential mortgage loans. One contact noted that residential mortgage lending activity was surprisingly brisk because of increases in refinancing activity. All contacts reported a steady increase in deposits.

Agriculture and Natural Resources

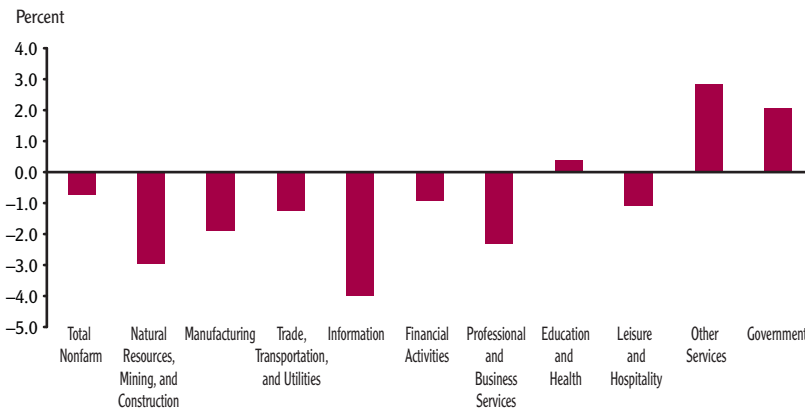
The development of soybeans and cotton is behind the normal pace in Mississippi and Tennessee, as is the development of corn in Tennessee and of sorghum and rice in Mississippi. Corn development in Mississippi is on par with its normal pace. Crop conditions have deteriorated since mid-July for all of the aforementioned crops except sorghum. As of August 1, yields for corn, soybeans, rice, and cotton in Mississippi were expected to be lower than last year's yields. Yields for corn, tobacco, cotton, and soybeans in Tennessee were expected to be higher than last year's yields.

Nonfarm Payroll Employment Growth 3-Month Average, SA, January 2001–July 2008



Recent estimates indicate that Memphis employment has contracted more sharply than the national average throughout 2008. Over the three-month period ending in July 2008, Memphis monthly employment contracted at a 0.18 percent monthly rate, while U.S. employment fell at a monthly pace of only 0.03 percent.

Memphis MSA Employment Growth by Sector Year/Year Percent Change, July 2007–July 2008



Between July 2007 and July 2008, employment growth in the Memphis MSA was negative in all goods-producing sectors and in most service-providing sectors. Expansion remains ongoing, however, in the education and health services sector as well as in the “other services” category, which saw employment increases of 0.4 and 2.8 percent, respectively. Employment in natural resources, mining, and construction; manufacturing; information; and professional and business services were all down by 1.9 percent or more.

Memphis Zone—MSA Employment and Unemployment

Nonfarm payroll employment percent change,
July 2007–July 2008

| | Total | Goods producing | Service providing | Unemployment rate June 2008 |
|----------------|--------------|-----------------|-------------------|--------------------------------|
| Memphis | -0.72 | -2.24 | -0.50 | 7.3 |
| Jackson, Tenn. | 1.13 | -2.07 | 2.11 | 6.9 |
| United States | 0.19 | -2.64 | 0.74 | 6.0 |

SOURCE: Bureau of Labor Statistics.

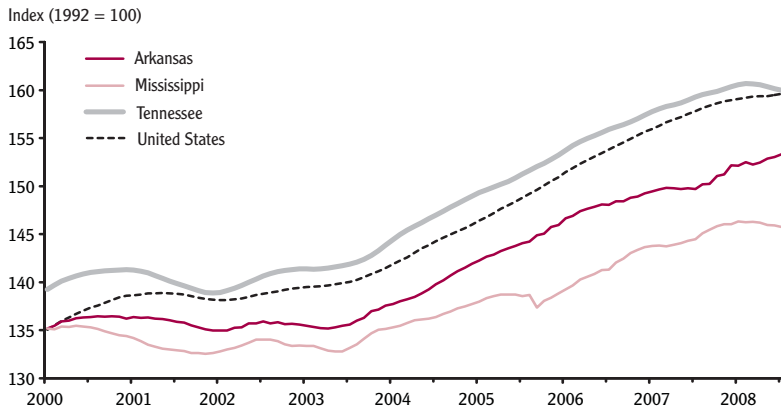
Memphis Zone—MSA Housing Activity

| | Total building permits, units year-to-date | | House price index, percent change, 2008:Q2/2007:Q2 |
|-----------------|---|----------------|--|
| | July 2008 | Percent change | |
| Memphis | 2,237 | -57.9 | 0.98 |
| Jackson, Tenn. | 210 | -44.0 | -1.68 |
| Jonesboro, Ark. | 368 | 37.8 | 1.03 |
| United States | 604,303 | -32.1 | -1.71 |

SOURCE: Bureau of the Census, Office of Federal Housing Enterprise Oversight.

Total residential building permits in July 2008 were lower than a year earlier in two of the three MSAs in the Memphis zone. In Memphis and Jackson, Tennessee, permits fell by 58 and 44 percent, respectively, while permits fell by 32 percent nationally. House price indices increased from year-earlier levels in two of the zone cities in the second quarter of 2008: Prices were up by about 1 percent in Memphis and Jonesboro, while prices declined by 1.7 percent in Jackson. Nationwide, house prices declined by 1.7 percent over the same period.

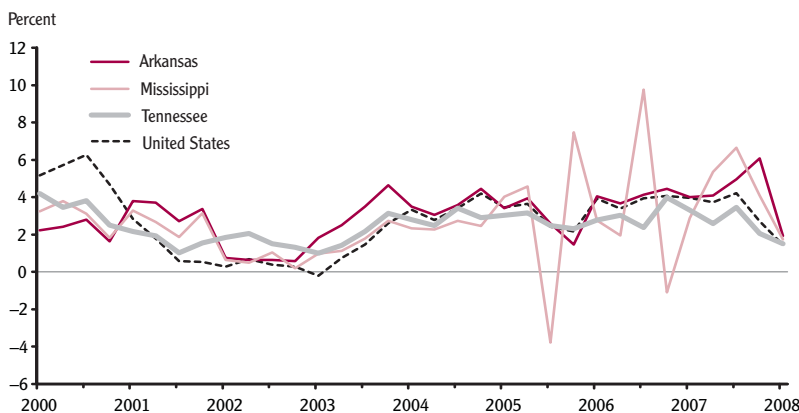
Memphis Area Coincident Economic Activity Index



SOURCE: Federal Reserve Bank of Philadelphia.

The Philadelphia Fed's coincident index combines payroll employment, wages and salaries, the unemployment rate, and hours worked into a single index. According to this index, Mississippi and Arkansas have underperformed the country as a whole since 2001, while Tennessee had tended to keep pace with the nation until recently. Through most of the first half of 2008, growth rates have slowed in Mississippi and Tennessee. For July, the index grew by -0.08, -0.10, and 0.20 percent in Tennessee, Mississippi, and Arkansas, respectively.

Memphis Area Real Personal Income Growth Percent Change, Year/Year



SOURCE: Bureau of Economic Analysis.

Personal income growth in Arkansas has tended to keep pace with national income growth since 2004, while Tennessee has tended to be just below the national pace. Since Hurricane Katrina in the third quarter of 2005, Mississippi has experienced relatively erratic income growth. As of the first quarter of 2008, all three states were showing year-over-year growth in excess of the national average. Arkansas was up 1.9 percent, Mississippi was up 1.7 percent, and Tennessee was up 1.5 percent. For the United States as a whole, personal income growth was 1.4 percent over the same period.

Residential Mortgage Delinquency Rates for Eighth District States
Percent 90+ Days Delinquent or in Foreclosure, 2008:Q2
FRM (fixed rate mortgages) ARM (adjustable rate mortgages)

| State | All mortgages | Prime | | | Subprime* | | |
|-------------------|---------------|------------|------------|------------|-------------|------------|-------------|
| | | Total | FRM | ARM | Total | FRM | ARM |
| Missouri | 3.1 | 1.5 | 1.1 | 4.7 | 13.2 | 7.2 | 20.8 |
| Illinois | 4.7 | 2.3 | 1.4 | 6.3 | 20.1 | 11.3 | 27.9 |
| Indiana | 5.7 | 2.9 | 2.2 | 9.2 | 18.5 | 12.3 | 27.8 |
| Kentucky | 4.0 | 1.9 | 1.4 | 6.4 | 15.8 | 9.9 | 26.1 |
| Tennessee | 3.7 | 1.7 | 1.3 | 6.4 | 12.6 | 7.8 | 20.4 |
| Mississippi | 5.0 | 2.5 | 1.9 | 10.1 | 16.1 | 11.6 | 25.1 |
| Arkansas | 2.7 | 1.5 | 1.0 | 6.1 | 11.4 | 7.8 | 18.1 |
| U.S. total | 4.5 | 2.4 | 1.3 | 6.8 | 17.9 | 9.6 | 26.8 |

NOTE: *The Mortgage Bankers Association divides the sample of conventional mortgages into prime and subprime categories based on whether the servicer handles primarily prime or subprime loans. Therefore, there are some prime loans in the subprime sample and some subprime loans in the prime sample.

SOURCE: Mortgage Bankers Association, National Delinquency Survey/Haver Analytics.

One of the symptoms of the ongoing problems in the nation's housing markets is a sharp rise in mortgage delinquencies and home foreclosures. From the second quarter of 2007 through the second quarter of 2008, the percentage of mortgages with more than three consecutive missed monthly payments or in foreclosure rose from 2.5 percent to 4.5 percent.

The table above summarizes the data for Eighth District states as of the second quarter of 2008. The data show that our region has suffered along with the nation. In fact, three Eighth District states have had higher proportions of delinquencies than the national average—Illinois, Indiana, and Mississippi. But the other states in the region—Arkansas, Kentucky, Missouri, and Tennessee—have fared better than the national average. Arkansas, in particular, has experienced a much lower rate of delinquencies and foreclosures than the rest of the country has.

For both the nation and the District, there are distinct differences in the pattern of delinquencies across various types of mortgages. Fixed-rate mortgages (FRM) have lower delinquency and foreclosure rates than do adjustable-rate mortgages (ARM). Moreover, the rate of delinquencies and foreclosure is much higher for subprime loans than for prime loans, and the rates for subprime ARMs are much higher than the rates for subprime FRMs. These patterns are clear in each of the Eighth District states. In fact, those states that have delinquency and foreclosure rates above the national average for all mortgages taken together tend to have rates above the national averages for each category of mortgage loans as well.