

Growth to Continue

Economic cross-currents evident

by Ransom Gustafson

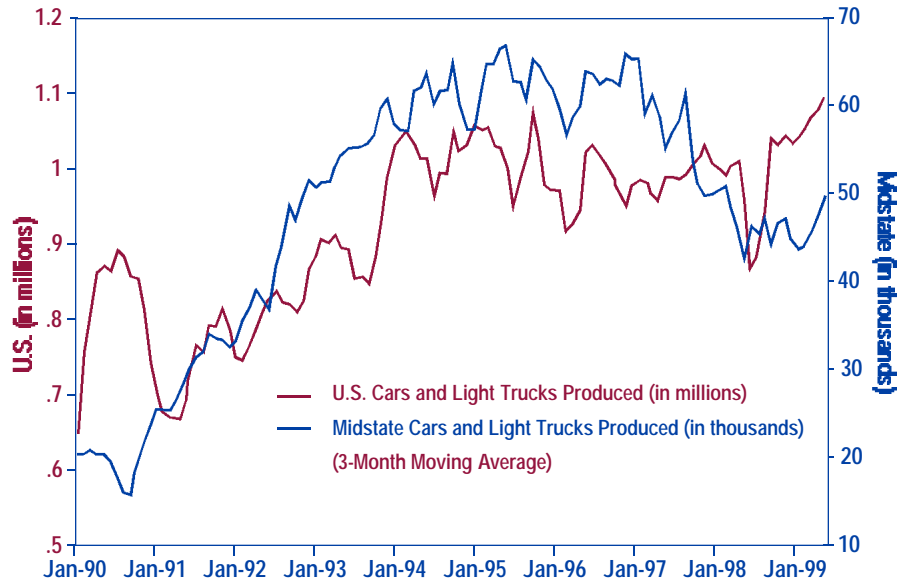
Will it ever rain on the midstate economy's parade? Right now, it looks like sunny skies and clear sailing ahead. The midstate leading index continued its four-quarter steady climb, thanks to increases in employment and hourly pay in manufacturing, a decrease in bankruptcy filings, and a dramatic increase in automobile production—all good news for economic conditions for the remainder of 1999 and the beginning of the new millennium.

Much of the good news was focused in motor vehicle production, which displayed four months of solid growth—a feat it has not accomplished since the summer of 1995. Nissan has finally aligned its product mix to meet insatiable consumer demand for sport-utility vehicles with its Xterra and four-door Frontier models, which hit showrooms in June. However, a few sprinkles appear in the forecast in the shape of lower hotel revenues and a drop in building permits issued.

Effects of the region's persistent growth are reflected in labor market conditions, which remain very tight. Low unemployment is a double-edged sword when it comes to economic forecasting. On the one hand, the more people work, the more money cycles through the economy. On the other hand, tight labor markets tend to push up costs of production as employers are forced to raise wages to attract workers. Higher wages could raise product prices, and the very vision of that eventuality has led the Federal Reserve to raise interest rates twice during the summer months.

Admittedly, there is some debate among economists over whether today's unemployment rate is consistent with stable inflation in the short run. By any standard, however, today's national rate of 4.5 percent or less represents comparatively tight conditions. As the midstate area has been beneath that rate for six quarters, wage pressure will remain a threat in the local area.

Figure 1. U.S. and Midstate Auto Production



While the midstate area is experiencing low unemployment rates, political leaders remain active in promoting job growth in their respective jurisdictions. It remains to be seen how tight local labor markets can become before we begin to see adverse effects (e.g., employers relocating to areas where they can more easily fulfill their labor needs).

On the positive side, the surge in midstate automobile and light truck production is a welcome development. In addition to the revamped product line, the surge is driven by the strong nationwide pace of vehicle sales, which posted a near-record (annualized) rate of 16.9 million units in June and July and a new record sales rate of 17.2 million units in August. Unfortunately, while midstate vehicle production is very much improved, it is still considerably below the peak production of early 1995 (Figure 1). Reflecting the local-area boost in vehicle production, employment in the transportation manufacturing sector showed healthy growth for the quarter.

In contrast, building permits dropped, which may reflect a cooling-off of what has been a white-hot sector in the local economy for quite some time. Rising mortgage interest rates

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The surge in midstate automobile and light truck production is a welcome development.

Table 2: Forecast Unemployment and Job Growth

	Actual				Forecast	
	'98Q3	'98Q4	'99Q1	'99Q2	'99Q3	'99Q4
Unemployment Rate						
Middle Tennessee	3.8%	3.7%	3.8%	3.6%	3.1%	3.5%
East Tennessee	4.2%	4.3%	4.3%	4.2%	3.7%	4.3%
West Tennessee	4.6%	4.5%	4.4%	4.4%	3.6%	4.3%
Tennessee	4.2%	4.1%	4.1%	4.0%	3.4%	4.0%
Job Growth: One Quarter SAAR						
Nashville MSA	2.2%	1.2%	2.6%	0.1%	2.1%	1.9%
Chattanooga MSA	0.7%	-0.5%	0.1%	-0.7%	1.2%	2.0%
Tennessee	3.4%	-0.2%	1.7%	0.2%	2.1%	1.9%
Job Growth: Four Quarter SAAR						
Nashville MSA	3.2%	2.5%	2.0%	1.5%	1.5%	1.7%
Chattanooga MSA	0.3%	-0.1%	0.3%	-0.1%	0.0%	0.6%
Tennessee	2.4%	1.9%	1.7%	1.3%	1.0%	1.5%

Sources: Bureau of Labor Statistics; MTSU
SAAR=Seasonally Adjusted Annual Rate

Hospitality businesses may experience a cure for their no-theme-park flu in the spring of 2000 when the Opry Mills shopping complex opens.

Growth

continued from front

(see related story) are probably the culprit. However, the tight national job market may also have a bearing on midstate housing construction as it limits in-migration to the region. Because of the rise in mortgage rates, local-area developments have mirrored and will likely continue to mirror national conditions. Nationally, projections for housing starts show that most areas of the country should moderate over the remainder of 1999. A notable exception is California, which, because of tax law changes, is experiencing a building boom that almost makes up for shortfalls in the rest of the country.

Hotel revenues, another midstate weak spot, are still suffering from the no-theme-park flu, but hospitality businesses may experience a cure in the spring of 2000 when the Opry Mills shopping complex opens. The Tennessee Titans are playing in a new stadium, which should also push up employment numbers in the hospitality sector.

Employment in the finance, insurance, and real estate (FIRE) sector has fallen slightly for two quarters in a row as consolidation in banking has adversely affected the midstate area. Nationally, employment in FIRE has been robust, suggesting that jobs are moving away from the area when mergers with outside firms take place. ■

Table 1. Data Bank for Middle Tennessee

Series (adjusted for seasonality and inflation)	Geographical Area	'98Q2	'99Q1	'99Q2	'99Q1-'99Q2
COMPOSITE INDICES					
Midstate Leading Index	Midstate (41 Counties)	101.45	103.13	104.00	0.8%
U.S. Leading Index	U.S.	102.81	110.82	111.85	0.9%
EMPLOYMENT					
Midstate Number of Employed Persons	Midstate (41 Counties)	998,815	1,023,400	1,032,943	0.9%
Midstate Unemployment Rate	Midstate (41 Counties)	3.9%	3.8%	3.6%	-3.2%
Percent of Sectors with Employment Increase for Month	Nashville MSA(8 Counties)	56%	22%	59%	168.2%
Percent of Counties with Employment Increase for Month	Midstate (41 Counties)	73%	59%	76%	28.8%
Average Hours Worked per Week in Manufacturing	Nashville MSA(8 Counties)	41.29	38.86	39.72	2.2%
Average Pay per Hour in Manufacturing	Nashville MSA(8 Counties)	12.92	13.06	13.14	0.6%
INITIAL CLAIMS AND BANKRUPTCY					
Initial Claims for Unemployment Compensation	Midstate (41 Counties)	33,758	32,510	32,740	0.7%
Bankruptcy Case Filings	Midstate (41 Counties)	3,051	2,797	2,729	-2.4%
REALESTATE					
Occupancy Index	Davidson County	98.12%	98.17%	97.99%	-0.2%
New Residential Units (permits)	Midstate (41 Counties)	4,190	4,388	4,097	-6.6%
Value of New Residential Units (million \$)	Midstate (41 Counties)	417.3	440.7	426.4	-3.3%
AUTOMOBILE PRODUCTION					
Autos Assembled in U.S.	U.S.	2,870,936	3,164,462	3,285,658	3.8%
Autos Assembled in Midstate	Midstate (41 Counties)	129,597	131,768	151,567	15.0%
Units Sold: Autos Assembled in Midstate	U.S.	145,430	134,873	139,405	3.4%
TOURISM					
Hotel Revenue	Davidson County	93,298,774	99,703,840	94,002,543	-5.7%
Air Passengers	Davidson County	1,994,283	2,089,564	2,111,328	1.0%
INCOME, EARNINGS, AND RETAIL SALES					
Retail Sales (million \$ per quarter)	Midstate (41 Counties)	5,262	5,372	5,408 (est.)	0.7%
Total Personal Income (annual billion \$)	Midstate (41 Counties)	49.1	50.0	50.2 (est.)	0.4%
Earnings per Resident Worker (annual)	Midstate (41 Counties)	35,089	34,578	34,376 (est.)	-0.6%

Notes: Seasonal adjustment with X11-ARIMA; not annualized; dollars converted to '99Q2 prices with GDP implicit consumption deflator
Sources: U.S. Department of Labor, Bureau of Labor Statistics; Tennessee Department of Employment Security; Nashville Electrical Service; U.S. Bureau of the Census; *Automotive Weekly*; Metropolitan Nashville Government; Nashville Airport Authority; Tennessee Department of Revenue; U.S. Bureau of Economic Analysis

Table 3: Change in Employment 1999Q1 to 1999Q2 (Eight-County Nashville MSA)

Sector	Nashville MSA 1999Q2	Nashville MSA Change	Nashville MSA % Change*	USA % Change*
Total	656,385	4,241	2.6%	2.6%
Construction and Mining	33,379	477	5.9%	8.3%
Manufacturing: Transportation Equipment	15,472	771	22.7%	-0.8%
Manufacturing: Other Durable	41,407	-302	-0.7%	-0.8%
Manufacturing: Printing and Publishing	13,806	-144	-4.1%	-1.2%
Manufacturing: Other Nondurable	24,496	-390	-1.6%	-0.5%
Finance, Insurance, and Real Estate	42,306	-6	-0.1%	4.2%
Transportation, Communications, and Utilities	32,395	140	1.7%	3.0%
Wholesale: Total	39,297	347	3.6%	2.2%
Retail: Eating and Drinking	44,364	197	1.8%	3.5%
Retail: Food	13,680	25	0.7%	-0.4%
Retail: General	18,290	-47	-1.0%	3.0%
Retail: Other	44,914	593	5.5%	3.2%
Services: Education	14,975	136	3.7%	3.9%
Services: Health	53,526	120	0.9%	0.9%
Services: Hotel	10,413	60	2.3%	-0.2%
Services: Other	129,280	1,690	5.4%	6.2%
Government: Total	84,113	-8	0.0%	1.6%

Sources: U.S. Bureau of Labor Statistics; MTSU
*Seasonally adjusted annual rate

Table 4: Single-Family Permits Jan-Jun '98 vs. '99

County	1998	1999	% Change '98-'99
Bedford	0	2	NA
Cheatham	134	158	18%
Coffee	66	45	-32%
Cumberland	35	51	46%
Davidson	1,228	1,389	13%
Dickson	147	175	19%
Franklin	122	131	7%
Hickman	6	6	0%
Marshall	132	117	-11%
Maury	391	436	12%
Montgomery	591	632	7%
Moore	22	28	27%
Putnam	24	29	21%
Robertson	415	407	-2%
Rutherford	1,212	1,293	7%
Smith	5	0	NA
Sumner	600	661	10%
Warren	15	69	360%
Williamson	1,048	976	-7%
Wilson	580	592	2%
Total	6,773	7,197	6%

Sources: U.S. Bureau of Census; MTSU

Interest Rate Developments and Prospects for Housing Activity

The monthly average rate on 30-year, fixed-rate mortgages reached a thirty-two year low last October. In response, midstate building permit issuance moved upward (Figure 2). Is this coincidence or causation? Since then, mortgage rates have spiraled upward (also Figure 2) along with other long-term rates, with barely any effect on permit issuance.

In fact, the buoying effect of the late 1998 fall in mortgage rates was evident throughout the first half of 1999, when the number of single-family building permits issued was 6.3 percent higher than in the first half of 1998 across the midstate. Table 4 presents data (not seasonally adjusted) for each county with a reporting station. A notable reversal of fortunes is that Davidson County's permits rose while Williamson's fell. Cheatham County may have experienced a flurry of activity in advance of the development tax increase in April. (Yet another increase, far larger, went into effect August 18.)

In the face of the current advanced state of expansion and strength of construction in the midstate area, we thought it useful to study the relationship between mortgage rates and midstate single-family building permits issued since January 1990 to assess future prospects.

Building permits rost sharply between 1991 and late 1993, in response to the prolonged decline in mortgage rates. Since early 1994, building permit issuance averaged roughly 1,030. During this same period, the 30-year mortgage rate averaged 7.66 percent.

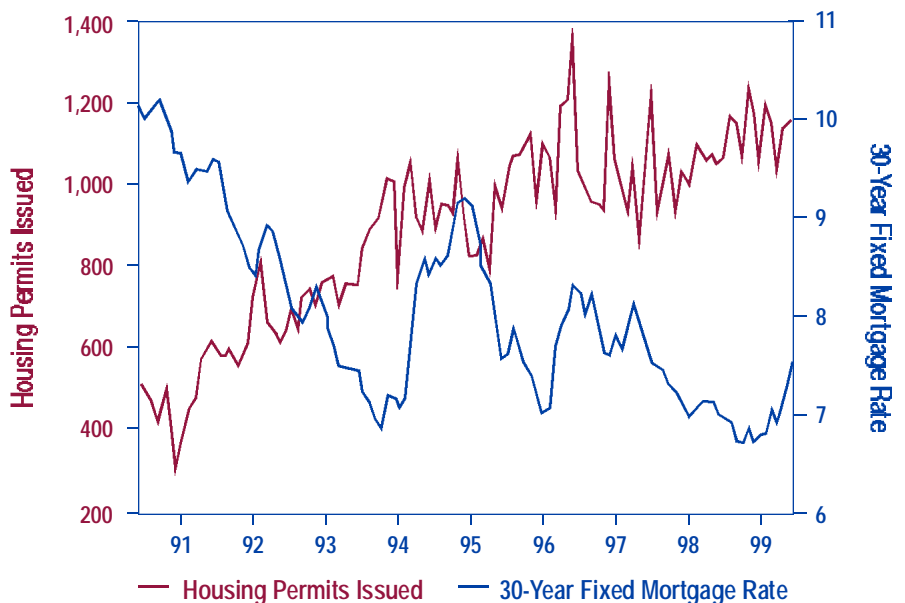
The large differences (noted above) among the various counties demonstrate that many

other considerations come into play, not the least of which is the strong job growth in the midstate area. Consumer attitudes also figure into the mix (e.g., Fannie Mae research shows two-thirds of Americans think this is a good time to buy a home).

Our analysis revealed a relatively strong relation between mortgage rates and building permit issuance. The effect was spread over a nine-month period, with most of the effect

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Figure 2. Housing Permits Issued and 30-Year Fixed Mortgage Rate



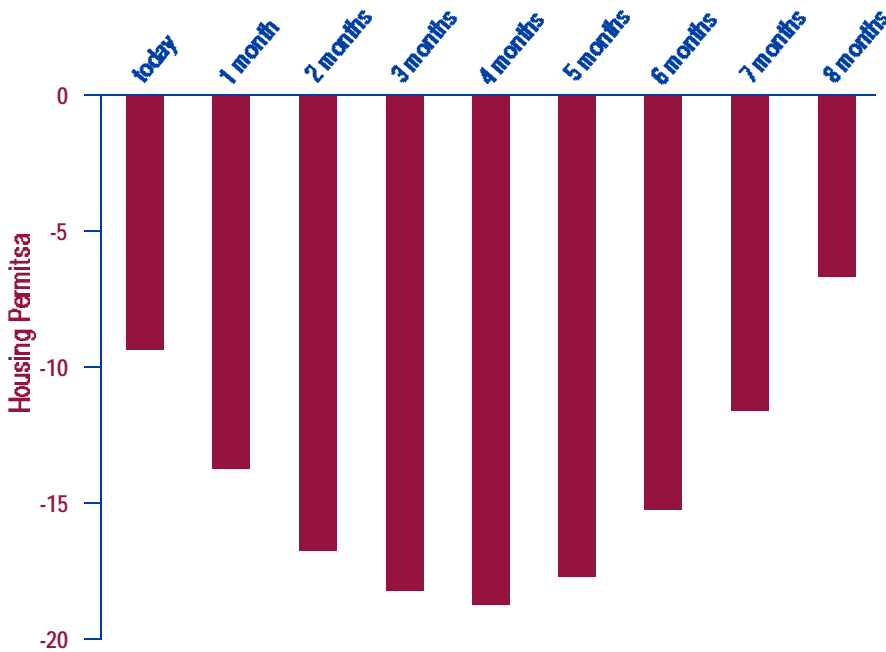


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Figure 3. Change in Number of Single-Family Permits due to a 1 Percent Rise in Mortgage Rates



Interest

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concentrated about three to five months after a mortgage-rate change. Figure 3 shows the diffusion of these effects over time.

Ignoring employment changes and shifts in consumer confidence, the model suggests that a one-percentage-point change in the 30-year mortgage rates would lead to a cumulative decline of 127 units spread over the subsequent eight months.

Notwithstanding the presumed model, permit issuance is uneven after seasonal adjustment (Figure 2). Building permits reached an all-time high in June 1996 of 1,360 units in the midstate counties that issue permits. However, levels were extremely volatile throughout that year. The industry maintained that this period was characterized by market instability as agents could not predict future movements in rates. Near year-end 1996, Federal Reserve Chairman Alan Greenspan made his famous “irrational exuberance” statement regarding stock prices. Since that time, midstate building permits have been a bit less erratic. Also, mortgage rates tended downward from early 1997 until late 1998, which may have lessened the monthly gyrations in permit issuance.

If the 30-year fixed mortgage rate stays at around 8 percent over the remainder of 1999 and throughout 2000, it will probably be associated with a gradual slowing of single-family permit issuance, from around 1,150 units in mid-1999 to around 975 units during the first half of 2000. ■

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