

## THIRD QUARTER

### MIXED BUT IMPROVED

by David A. Penn

Third quarter indicators are mixed but improved from the second quarter. Housing construction rebounded strongly after a lackluster second quarter, and the Midstate Leading Index rose by a full percentage point, now standing 5.0 percent higher than in the third quarter of 2003. However, midstate total employment and labor force show little change from the second quarter, and tourism indicators are down slightly after adjusting for typical seasonal variation.

Housing construction rebounded in the third quarter with single-family permits rising by 4.8 percent and total permits up 12.4 percent from the second quarter, seasonally adjusted. At 4,637 units, third-quarter single-family permits reached the second-highest level since the second quarter of 1996. The dollar value of single-family units experienced a more impressive gain, rising by \$53.9 million, a 9.1 percent increase from the second quarter and up 20.6 percent from the same quarter of 2003. The value of

**HOUSING CONSTRUCTION REBOUNDED STRONGLY ... AND THE MIDSTATE LEADING INDEX ROSE BY A FULL PERCENTAGE POINT, NOW STANDING 5.0 PERCENT HIGHER THAN IN THE THIRD QUARTER OF 2003.**

the average single-family unit in middle Tennessee increased 3.4 percent from last year.

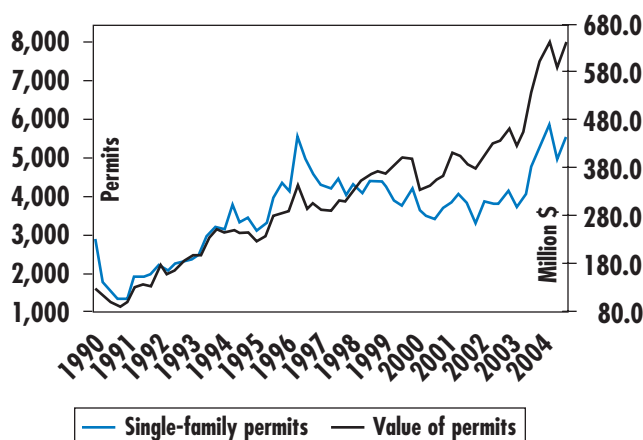
The fourth quarter will likely experience considerable cooling of housing market growth. Preliminary figures for October show single-family permits down 12.9 percent from the same month of 2003 and the value of single-family permits down 9.7 percent. According to Market-Graphics, builders are beginning to experience a significant shortage of lots to build on; not enough land has been purchased, developed, and platted to meet the demand for new housing units. Even though demand continues to be strong and mortgage rates are historically low, the supply of land ready for housing construction may act to limit the number of housing starts during the coming year.

The midstate labor market showed little forward momentum during the third quarter, continuing a trend starting with the first quarter. Both labor force and total employment increased just 0.1 percent from the second quarter while the unemployment rate held steady at 4.3 percent. Although total employment is up 2.3 percent from last year, nearly all the increase occurred during the first quarter. On a more positive note, initial claims for unemployment insurance fell by 7.9 percent from the second quarter and are now at their lowest level since the fourth quarter of 1999.

Employment gains by county are not very widespread geographically with only 23 of the 41 counties in our midstate area experiencing increased employment from the second quarter. Unemployment rates increased in more counties than in the last quarter: 19 midstate counties experienced higher unemployment rates compared with 12 counties during the second quarter.

*continued inside*

**Figure 1  
Number and Value of Single-Family Construction Permits,  
Midstate Counties**



**... THE SUPPLY OF LAND READY FOR HOUSING CONSTRUCTION MAY ACT TO LIMIT THE NUMBER OF HOUSING STARTS DURING THE COMING YEAR.**

# THIRD QUARTER

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Total nonfarm employment for the Nashville Metropolitan Statistical Area (MSA) rose by just 1,400 jobs during the third quarter, a very modest 0.2 percent quarter-to-quarter gain. Excluding the government sector, private sector nonfarm employment actually declined slightly from the second quarter, slipping by -0.1 percent.

A review of employment by industry for the Nashville MSA shows a mix of job increases and job losses. Of the 12 major sectors, seven gained jobs, three lost jobs, and two were unchanged (Table 1). Manufacturing gained more than one thousand jobs with all the net gain in durables manufacturing. Wholesale trade and retail trade produced very small employment gains while employment increased moderately in educational and health services, leisure and hospitality, and transportation and utilities.

Job losses continued in professional and business services and, to a smaller extent, information and non-durable goods manufacturing. The professional and business services sector has lost nearly 2,800 jobs from a year ago, a 3.4 percent decline. Virtually all the job decline occurred in administrative and support and waste management services.

Seasonally adjusted taxable sales again showed little change from the previous quarter for the 41 midstate counties (Figure 2). After impressive gains in 2003, sales have averaged \$8.4 billion per quarter with little variation since the first quarter of 2004. Much of the slack in taxable sales can be attributed to a slower pace of auto sales from the beginning of the year. Another important factor explaining slower sales growth is the slower growth of mortgage refinancings as a consequence of rising mortgage rates and the winding down of the impact of federal income tax cuts. Households generated substantial new funds for spending as the result of refinancing; these opportunities will diminish substantially as mortgage rates increase.

Taxable sales grew 5 percent or more over the past 12 months in 25 Tennessee counties; of these, more than seven in 10 are located in the midstate (Figure 3 on back). Just-released sales tax collection figures from the Tennessee Department of Revenue show midstate taxable sales up 3.7 percent year to year for October compared with a 4.4 percent rise in September.

Growth improved somewhat in the national economy during the third quarter with gross domestic product (GDP) rising 3.9 percent, an improvement from 3.3 percent growth during the previous quarter. Household spending rebounded in a big way, rising by 5.1 percent with most of the gain in durable goods. Exports rose faster than

**TAXABLE SALES GREW 5 PERCENT OR MORE OVER THE PAST 12 MONTHS IN 25 TENNESSEE COUNTIES; OF THESE, MORE THAN SEVEN IN 10 ARE LOCATED IN THE MIDSTATE.**

**Table 1  
Nashville Nonfarm Employment Gains and Losses**

Second quarter employment gains	Fourth quarter losses
Educational and Health Services	Construction and Mining
Government	Information
Leisure and Hospitality	Professional and Business Services
Manufacturing	
Retail Trade	No change
Transportation and Utilities	Financial Activities
Wholesale Trade	Other Services

imports, buoyed by a falling dollar. Spending for plant, equipment, and software gained a substantial 12.9 percent, but some analysts believe this is not good enough; capital equipment spending should be much more robust given the large amounts of cash businesses have on hand and investment incentives created by capital investment tax breaks that are scheduled to expire at the end of the year.

National nonfarm payrolls increased just 112,000 in November following an impressive gain of 303,000 for October. Job gains in October and September were revised lower in subsequent reports, leaving the three-month average job increase at a subpar 178,000. The professional and business services sector generated at least one-fourth of

Series (seasonally adjusted)	Geographical Area
Midstate Leading Index	Midstate*
<b>EMPLOYMENT</b>	
Midstate Total Employment	Midstate
Midstate Labor Force	Midstate
Midstate Unemployed	Midstate
Midstate Unemployment Rate	Midstate
Average Hours Worked per Week in Manufacturing	Nashville MSA**
Counties with Increased Employment (percent)	Midstate
Counties with Increased Unemployment (percent)	Midstate
Initial Claims for Unemployment Compensation	Midstate
<b>HOUSING CONSTRUCTION</b>	
New Residential Permits	Midstate
Single Family	
Total	
Value of New Residential Units (million \$)	Midstate
Single Family	
Total	
MarketGraphics: Single-Family Construction	6 NMSA Counties***
<b>TOURISM</b>	
Hotel Tax Revenue (million \$)	Davidson County
Total Air Passengers, Nashville International Airport	Davidson County
<b>TAXABLE SALES (estimates)</b>	
Nashville MSA (million \$)	Nashville MSA
Midstate (million \$)	Midstate

Notes: Seasonal adjustment with X11. \*Midstate is a 41-county area. \*\*Nashville MSA includes 8 counties. \*\*\* Sources: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Bureau of the Census; Davidson County

recent monthly job growth in stark contrast with job losses for this sector in the Nashville MSA.

Industrial production growth has been choppy but positive: industrial production rose nicely in July, flattened in August and September, and rebounded in October. The utilization rate of industrial capacity continues to inch upward, rising to 77.7 percent in October. Pressures for businesses to spend on expanding capacity will build as the economy approaches 80 percent capacity utilization, the rate typically associated with full capacity.

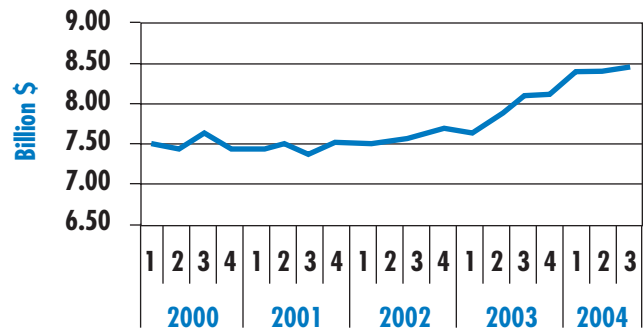
The ISM index of manufacturing activity indicates expansion but at a slower rate than that which prevailed last summer. The Conference Board's consumer confidence index produced its fourth consecutive decline in November, suggesting that uncertainty created by the war on terrorism, war in Iraq, and high gasoline prices are taking a toll on confidence.

The coming months will most likely produce more choppy growth both for the U.S. and midstate economies. Smooth growth trends are not likely to return until both consumer and business confidence get back on track. ■

*continued on back*

**INDUSTRIAL PRODUCTION GROWTH HAS BEEN CHOPPY BUT POSITIVE: INDUSTRIAL PRODUCTION ROSE NICELY IN JULY, FLATTENED IN AUGUST AND SEPTEMBER, AND REBOUNDED IN OCTOBER.**

**Figure 2**  
**Seasonally Adjusted Taxable Sales, Midstate Counties**



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**Table 2**  
**Economic Indicators for Middle Tennessee**

2003Q1	2003Q2	2003Q3	2003Q4	2004Q1	2004Q2	2004Q3	% Change 2004Q2 - 2004Q3	% Change 2003Q3 - 2004Q3
106.1	106.3	107.8	108.6	112.2	112.1	113.1	1.0%	5.0%
1,058,849	1,055,183	1,054,358	1,057,691	1,075,510	1,076,587	1,078,148	0.1%	2.3%
1,115,825	1,116,195	1,116,129	1,119,720	1,126,956	1,125,599	1,126,328	0.1%	0.9%
56,976	61,012	61,771	62,029	51,446	49,012	48,180	-1.7%	-22.0%
5.1%	5.5%	5.5%	5.5%	4.6%	4.4%	4.3%	-1.8%	-22.7%
38.3	38.8	39.1	39.7	39.7	39.7	39.6	-0.3%	1.2%
41.5%	29.3%	65.9%	75.6%	80.5%	63.4%	56.1%	-11.5%	-14.8%
75.6%	82.9%	61.0%	43.9%	2.4%	29.3%	46.3%	58.3%	-24.0%
37,393	38,055	33,084	28,065	28,460	28,300	26,071	-7.9%	-21.2%
3,298	3,668	4,100	4,268	4,429	4,424	4,637	4.8%	13.1%
3,739	4,066	4,755	5,320	5,878	4,933	5,542	12.4%	16.5%
422.6	457.1	533.8	599.9	638.2	589.7	643.5	9.1%	20.6%
445.1	482.5	579.6	645.9	668.8	629.1	708.4	12.6%	22.2%
2,719	2,949	3,259	3,297	3,460	3,293	3,238	-1.7%	-0.6%
5.08	4.63	4.76	4.76	4.75	5.11	5.04	-1.3%	5.8%
2,000,092	1,943,393	2,028,912	2,002,015	2,058,339	2,194,178	2,173,667	-0.9%	7.1%
5,477	5,610	5,807	5,844	5,992	6,017	6,022	0.1%	3.7%
7,630	7,819	8,076	8,128	8,379	8,390	8,426	0.4%	4.3%

A is Nashville MSA. s office; Metropolitan Nashville Airport Authority; U.S. Bankruptcy Court, Middle Tennessee District; MarketGraphics, Brentwood, Tennessee

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**Figure 3**  
**Percent Change Taxable Sales Third Quarter 2003 – Third Quarter 2004 by County**

