ECON SOUTH

Volume 10, Number 3
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FEATURES

DEPARTMENTS

Foreclosures Chill Once-Hot Southeast Housing Market

The housing market once added considerable sizzle to the Southeastern economy. But the foreclosure crisis has roiled the region and spread its tentacles into many industries and residents' lives. Foreclosures' eventual cost to the region's economy remains to be seen.

Podcast on Home Foreclosures and Resources in South Florida (MP3 9:12)

Remittances Ebb and Flow With the Immigration Tide

Many people in developing countries rely on the remittance payments sent back home by family members working abroad. An economic slowdown in the United States has dampened the growth of this payment method. Changing migration patterns, economic developments, and new technologies and policies are affecting how—and how many—remittances are sent abroad.

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Plumbing the Gulf's Depths for Oil and Gas

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Podcast on Gulf of Mexico Energy Exploration and Production (MP3 8:14)

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Foreclosures Chill Once-Hot Southeast Housing Market

Photo by Brad Newton

Housing markets in the Southeast once sizzled like an August afternoon, helping to heat up the region's economy. But a cold wave of foreclosures has crashed through many of the region's housing markets, and its ripples have spread through most corners of the region. The eventual toll this foreclosure wave will take on the region's economy remains to be seen.

During the housing boom of 2004–06, Atlanta's Pittsburgh neighborhood briefly emerged as a magnet for new home construction. Builders saw opportunity in a previously neglected area across Interstate 75-85 from Turner Field (the Atlanta Braves stadium), an area that provides easy access to Atlanta-area jobs.

For a while, prices of newer homes with top amenities in the gentrifying Pittsburgh neighborhood approached $400,000. But in 2007 these prices began tumbling, and within months foreclosures began to spread quickly from house to house.

Today, boarded-up windows and overgrown landscaping characterize this once up-and-coming community. For sale, for lease, and foreclosure signs proliferate like the dandelions in the lawns. LaShawn Hoffman, chief executive officer of the Pittsburgh Community Improvement Association Inc., which promotes economic and community development in the Atlanta neighborhood, said new working families began moving into the area a few years ago. Many of them were renters who have now been forced out as banks repossess properties from absentee speculators who failed to pay their risky mortgages. The dwindling number of remaining residents find themselves constantly on guard against squatters trying to move into abandoned properties.

Foreclosure spreads its tentacles

While the Pittsburgh neighborhood of Atlanta—also known as Adams Park—offers an unusually concentrated microcosm of foreclosure issues, it is by no means an isolated case. A sudden and widespread increase in bank-owned real estate has broad economic and social consequences. While many areas in the Southeast have not been directly touched by foreclosures, the problem has exacerbated an overall decline in house prices and economic weakness throughout much of the region.

Since 2005, foreclosure rates in Southeastern states have risen. The hardest-hit state is Florida, followed by Georgia, where the chief problems are in parts of the Atlanta metropolitan area.

Related Links

Home Foreclosures and Resources in South Florida (MP3 9:12)

Atlanta Fed Foreclosure Resource Center

Federal Reserve mortgage foreclosure resources OFF-SITE

The Federal Reserve's Homeownership and Mortgage Initiative OFF-SITE

NeighborWorks America OFF-SITE

Hope Now OFF-SITE

Maps of subprime mortgage activity OFF-SITE

Foreclosures have swept through communities with surprising speed. Just three years ago, Florida was below the national average in foreclosures. But the state now has the highest foreclosure rate in the Southeast, with almost 4 percent of mortgages in foreclosure in 2007, according to the Mortgage Bankers Association (MBA). Florida's foreclosure rate in 2008 has continued to climb.

In Georgia, 3.23 percent of all mortgages were in foreclosure in 2007—up from 2.56 percent in 2006. As in Florida, Georgia's foreclosure rate surged in the first half of 2008 (see the maps).

But the rate is not as high throughout the region. For example, according to data from the MBA, the foreclosure rate for Alabama at the end of 2007 was 2.37 percent—the lowest rate in the Southeast and below the national average of 2.84 percent. Foreclosures in Tennessee and Louisiana are also below the national average but are up from a few years ago. Mississippi's foreclosure rate has increased sharply, to about 3.5 percent at the end of 2007.

Housing price depreciation is a key culprit

The increase in foreclosures can be attributed to many factors, such as mortgage fraud and predatory lending. While acknowledging these issues, Atlanta Fed financial economist and policy adviser Scott Frame said one economic dynamic underlies almost all foreclosures: the decline in house prices.

Frame traces today's foreclosure problems to the rapid increase in house prices that took place a few years ago. U.S. house prices appreciated more than 55 percent between 2001 and 2006, driven primarily by income growth, low interest rates, and, in certain markets, supply constraints.

As housing affordability declined, subprime lending increased significantly with the availability of new and untested mortgage products. By 2006, about 20 percent of new residential mortgages were subprime; in other words, one in five mortgage borrowers had either low credit scores, high levels of debt compared with income, high mortgages compared with their homes' value, or unverified income. Many of these high-risk borrowers were buying houses with minimal or no down payments just as prices were peaking.

Photo by Brad Newton

Foreclosures began ravaging the gentrifying Pittsburgh neighborhood in downtown Atlanta in 2007. House prices there continue to decline as developers, lenders, and homeowners await the market stability that must precede the area's rebound.

"The path of house prices appears to be very important—in both theory and in practice," Frame said. "Negative equity [owing more than the house is worth] is a necessary, but not sufficient, condition for foreclosure."

In principle, if they have positive equity, homeowners can either borrow to cover temporary shortfalls or sell the house. But owner-occupiers do not default simply because they have negative equity. Typically foreclosure involves a significant trigger event related to household budgets such as job loss, divorce, or large medical expenses.

When such events lead to numbers of foreclosures in a subdivision or community, the consequences can be severe—not just for those who lose their homes but also for builders, lenders, and others in the community with good credit. Examining how these various stakeholders are adjusting to the impact of foreclosures in the Southeast provides a window into the housing crisis in the region.

Homeowners work out the workout process

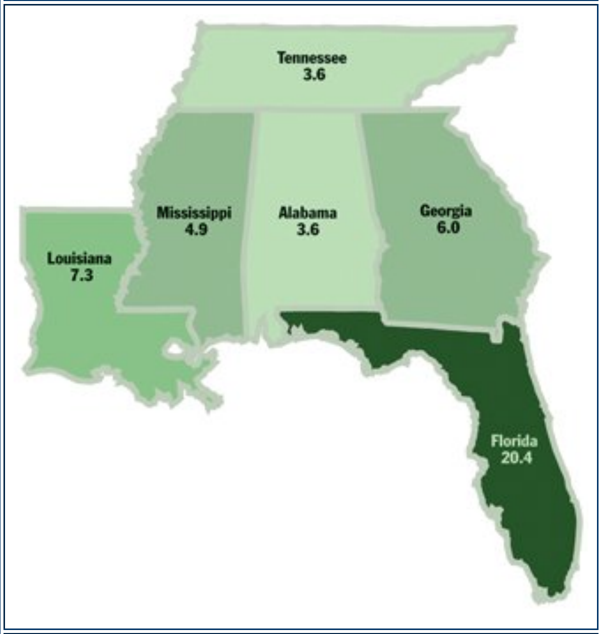
During the first half of 2008, the Consumer Credit Counseling Service (CCCS) of Greater Atlanta experienced a surge of calls from homeowners delinquent on mortgage payments, said Suzanne Boas, the agency's president. Nearly as many people—some 30,000—turned to CCCS for housing counseling sessions in the first six months of 2008 as in all of 2007.

The increased housing counseling at CCCS this year reflects a deepening foreclosure crisis that began with low-income borrowers and spread to families with more substantial means. For the first time in 2008, the average household income of CCCS clients seeking housing counseling exceeded $40,000.

Along with additional foreclosure-related activity, CCCS has continued to receive calls from people struggling with credit card bills, medical expenses, and other types of unsecured debt.

"Demand for our counseling services is rising significantly as people try to avoid foreclosure and bankruptcy, as well as cope with rising gasoline and food costs," Boas said.

Map 1
Percent of Subprime Loans in Foreclosure by State



Note: Data are current as of August 2008.
Source: FirstAmerican CoreLogic, LoanPerformance Data

Map 2
Percent of Homes in Foreclosure per 1,000 Housing Units by State

Note: Data are current as of August 2008.
Source: FirstAmerican CoreLogic, LoanPerformance Data

In response, CCCS is hiring about 80 more counselors using the proceeds of a $2 million grant from the Ford Foundation. Counselors help borrowers negotiate with loss mitigation departments of mortgage servicers and often help provide information that can lead to a loan modification, or workout. Typically, workouts involve investigation and time-consuming back-and-forth negotiations that vary depending on the situation. Such delays can be costly for borrowers and lenders alike. Recently, however, CCCS began testing a new software program to standardize and speed the workout process, Boas said.

A window on Florida's housing woes

With their patience and knowledge of the financial landscape, credit counselors and other nonprofits have played a crucial role in helping address the foreclosure crisis in south Florida, said Ana Cruz-Taura, regional community development director in the Atlanta Fed's Miami Branch.

In the climate of rapid house price appreciation between 2002 and 2006 in south Florida, many potential homebuyers abandoned the traditional go-slow approach of saving for a down payment to buy a house. Rather than paying more later by delaying their purchase, they instead chose to take a chance on a subprime loan in the hopes of getting into a home before property values increased further. Speculators fueled house price increases and worsened the affordability problem that drove ordinary borrowers into risky mortgages.

But when the housing market cooled and prices began to decline, overextended borrowers began to have credit problems. Between May 2007 and May 2008, Miami-area house prices fell by more than 28 percent, according to the S&P; Case Shiller 20 City Composite Index, which tracks home values in 20 markets around the country. Still, even with this recent drop, house prices in Miami now are still much higher than in 2000.

Now, many homeowners who bought at the peak of the market a few years ago have negative equity. Others lost equity by borrowing against the price appreciation that had already occurred. Homeowners drained the equity gained with price appreciation and found themselves in trouble when their homes depreciated. Faced with the possibility of further price declines, many potential buyers have stepped aside, leaving distressed sellers with few options. Many borrowers who fell behind on payments have responded to this adversity not by reaching out to their lenders but instead by simply walking away from their homes.

"It's human nature that people tend to be afraid to confront bad news," said Janet Hamer, community development manager at the Atlanta Fed's Jacksonville Branch, who has worked on mitigating foreclosure problems in northeastern and central Florida. "There's an embarrassment factor that prevents people from asking for help."

With the oversupply of housing in Florida amid a worsening foreclosure problem, construction employment in the state has pulled back sharply, and the state's labor market has suffered. From January 2006 to July 2008, Florida lost more than 115,000 jobs, including 49,000 construction jobs, according to the U.S. Bureau of Labor Statistics. The combination of job losses and foreclosures has provided a painful double whammy in certain markets such as Palm Bay, along the Atlantic Coast, which has also suffered from cutbacks in funding to NASA's space shuttle program.

In community after community, foreclosures set off a domino effect. Foreclosures led to an oversupply of housing on the market, and the oversupply deepened price depreciation and intensified foreclosure, which led to even more oversupply of housing and a resulting sharp construction pullback and laid-off workers.

The decline of house prices throughout Florida has created one bright spot: the opportunity for value investment. This time, many investors, including those from overseas, plan to wait for the right time to buy—at the bottom of the market, ahead of the next cycle of appreciation.

The shifting lending landscape

For Southeastern lenders that have targeted residential markets, the recent spike in foreclosures has been costly. A number of the region's mortgage providers have gone out of business, and many Southeastern banks have struggled with the loans they made to small builders. Also, many of the home loans ending up on bank balance sheets are not primary mortgages but instead are nonperforming second mortgages or home equity lines of credit, including many loans backed by vacation homes.

Repossessing, maintaining, and selling foreclosed properties in a declining housing market have been major challenges for lenders, who have been looking for alternatives to adding to their real estate inventories. For example, lenders have devised new outreach programs such as enhanced Web sites targeting at-risk borrowers (see the interview with Barb Godin).

Lenders also have strengthened ties with credit counseling organizations, which have provided a vital link between lenders and distressed borrowers who are interested in making an informed and good faith effort to renegotiate their mortgages in the hope of obtaining more favorable loan terms.

But following an extended period of easy credit, lenders face their own constraints. Underwriting standards and regulatory oversight are changing the way mortgages are made and, concurrently, subprime lending has ceased because lenders have lost their appetite for these loans. Regulated financial institutions are bound by underwriting guidelines that require more careful scrutiny of loan documentation and more substantial down payments among other steps to ensure credit quality, said Pamela Cross, vice president and senior community development officer in the Atlanta office of North Carolina–based Wachovia Corp.

Cross noted that the concentration of foreclosures has become a factor in residential appraisals, especially in harder-hit areas of Atlanta. "Values now are lower than they were a year ago, and our lending ability is based on appraisal," she said.

Lower appraisals and other restrictions make it harder for owners to refinance and possibly avoid foreclosures—a scenario that might not have occurred with more stable real estate conditions. "In some cases we are seeing a huge difference between the present value of the mortgage and the newly appraised value of the home," said Arthur Fleming, first vice president and director of community investment for the Federal Home Loan Bank of Atlanta. In such cases, he added, "refinancing is a big issue."

Lenders can take solace in the relatively uneven distribution of foreclosures. Subprime loans account for less than 10 percent of homeowner mortgages, but they make up more than half of all foreclosures, according to the National Association of Realtors. In more affordable markets where subprime mortgage lending was not widespread, foreclosures have been much less problematic.

State by state, the landscape changes

Even in the overbuilt Atlanta area, population growth has helped to support housing demand in the more stable communities, especially those with convenient access to intown jobs. And some areas have been relatively unaffected by the foreclosure crisis. "Outside of Atlanta, the foreclosure issue in the rest of Georgia is not as severe," said Connie Bryant, community development officer with Wachovia Corp.

Bryant said isolated foreclosures have been problematic in Macon and Dalton, where subprime borrowing was prevalent and the carpet manufacturing and chicken processing industries were laying people off. But the scale of the problem in these areas is moderate, as it is in much of Savannah and Augusta.

During the peak period of subprime lending, Louisiana experienced only modest growth in both population and house price appreciation. As a result, the state did not attract much of the type of lending activity that set the stage for foreclosure problems in other states, said Nancy Montoya, the Atlanta Fed's senior regional community affairs manager for the Gulf Coast. In the New Orleans area and along the Mississippi coast, many of the outstanding loans were on a voluntary foreclosure moratorium because of heavy losses from Hurricane Katrina in 2005. Once vulnerable homeowners received their insurance proceeds, many chose to pay off their loans.

Photo by Brad Newton

When an area is hit with numerous foreclosures, it's not only the foreclosed homeowners who are affected. The pain is shared by other residents, whose home values can also decline.

Greg Gonzalez, Tennessee's banking commissioner, said declining asset quality was a concern in his state. But he noted that his office has not received a large number of complaints about foreclosure and that the incidence of foreclosure statewide has not been severe. "The problem is evolving, and we're trying to get information and respond appropriately," Gonzalez said.

Builders offer discounts, concessions

During the housing boom, residential developers had plenty of options for borrowing money. Lenders competed to finance construction projects in fast-growing markets across the Southeast, and regional banks were also heavily concentrated in real estate lending. Their activity is now clearly evident with the boom of condominium construction on Florida beachfronts and along Atlanta's Peachtree Street.

These properties, some of which have taken years to build, are now being marketed in a real estate environment much more difficult than developers anticipated when they received financing and broke ground on their projects. In recent months, demand for new construction in major Southeastern markets has been weakened substantially by declining consumer confidence, less credit availability for purchasers, and increased competition from resales, including market sales, short sales, and foreclosures, said developers in the Atlanta area. In response, developers have offered concessions, including price discounts.

With the decrease in qualified demand and more supply coming into major markets from the large influx of condominiums that were started from 2002 to 2006, house prices have stagnated and in some cases declined. These developments, in turn, have boosted the foreclosure rate and a greater concentration of foreclosures, particularly for condominiums and homes delivered and purchased in the past three years, developers said.

In the close confines of a condo building, a few foreclosures can have a ripple effect on sales. Residents who stay in buildings with rising vacancies or foreclosures often end up paying more for shared expenses such as maintenance and insurance under the broad umbrella of association fees, said the Atlanta Fed's Cruz-Taura. Also, because of the uncertain value of the collateral, lenders have become increasingly wary of originating mortgages to buy condominiums in buildings that have been tainted by foreclosure. In many cases, prospective buyers have simply walked away from their deposits—because they either couldn't get a loan to close the purchase or were deterred by the declining market.

With less financing available for purchases, demand for rental properties has increased. Also, developers have begun to convert some condominium properties into rental units. "People who can't get mortgage financing are back in rental," said Egbert Perry, president of Integral Group, a real estate development and management business in Atlanta. "We're starting to build in rent increases after a period when rental rates were artificially held down because of demand and credit for buying houses for sale."

An upside of the foreclosure problem is improved affordability of housing, especially in the most expensive markets in the region. In this environment, however, most of the improvement in affordability has been offset by higher taxes and other costs, said John O'Callahan, president of Atlanta Neighborhood Development Partnership. The need for more affordable housing is as pressing as ever, he noted.

But first-time buyers with good credit and ample savings for a down payment are well positioned to become homeowners. Whether or not they face more house price declines is uncertain. The abundance of foreclosed properties provides opportunities for bargains but also tends to drag down the rest of the market. Given the severity of the problem in neighborhoods such as Atlanta's Pittsburgh and the additional supply coming into already glutted markets in parts of the Southeast, projecting the bottom of the housing market is difficult.

Signs of progress are appearing, though. Distressed mortgage borrowers have become more aware of their options, and lenders seeking to avoid additional and perhaps preventable foreclosures have devised creative ways to keep families in their homes.

Fed Chairman Ben Bernanke stressed the importance of such efforts in a May speech: "Most Americans are paying their mortgages on time and are not at risk of foreclosure. But high rates of delinquency and foreclosure can have substantial spillover effects on the housing market, the financial markets, and the broader economy. Therefore, doing what we can to avoid preventable foreclosures is not just in the interest of lenders and borrowers. It's in everybody's interest."

This article was written by William Smith, a staff writer for EconSouth.

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Remittances Ebb and Flow with the Immigration Tide

For families in many developing countries, remittance payments sent back home by family members working abroad are the difference between subsistence and privation. After years of rapid growth, remittances have leveled off amid an economic slowdown in the United States. How are changing migration patterns, economic developments, and new technologies and policies affecting this important payment method?

For the citizens of many developing countries, remittances are a vital source of personal income and, in some cases, survival. Remittances—literally, transmittals of money to a distant place—are generally understood to mean transfers of income from workers who have migrated from a poor to a rich country back to family members who remain in the home country.

The World Bank estimates that recorded remittances reached $318 billion worldwide in 2007. (Unrecorded flows through formal and informal channels likely mean that actual numbers are significantly larger than the reported numbers.) Of this amount, remittances sent home by migrants to developing countries represented $240 billion, more than double the amount sent in 2002 (see chart 1). In 2007, remittances totaled more than the amount of official government aid and more than half the amount of foreign direct investment in emerging economies.

Latin America has some of the highest levels of remittances, both in aggregate and per capita, according to the World Bank report. Mexico, for example, received $25 billion, or approximately 2.5 percent of gross domestic product (GDP), in remittances during 2007. These financial flows are particularly large in Central America and the Caribbean. In 2007, remittances made up 25.6 percent of total gross domestic product in Honduras, 24.3 percent in Guyana, and 21.6 percent in Haiti.

These high levels of remittances to Latin America are clearly related to the rate of immigration from the region. The World Bank's 2007 report, titled *Close to Home: The Development*

Related Links

World Bank *Close to Home* remittances report OFF-SITE

Impact of Remittances in Latin America, estimates that Latin American migrants (both documented and undocumented) in the United States increased from 8.6 million in 1990 to about 16 million in 2000, nearly 10 million of whom were Mexican. About one-third of El Salvador's natives live abroad, mostly in the United States, and almost 50 percent of Grenada's population has migrated to a foreign country.

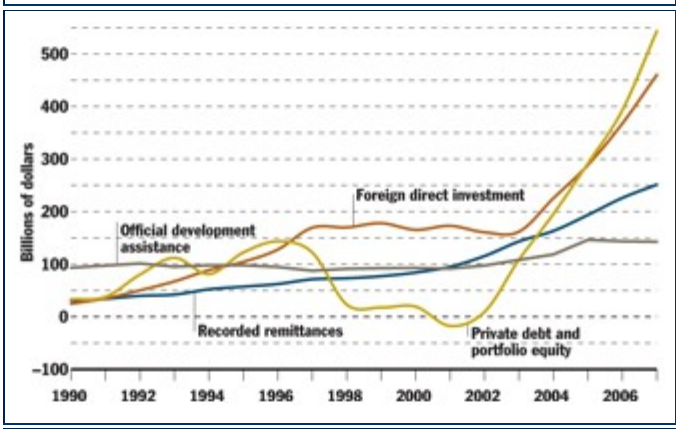
Multilateral Investment Fund remittances information OFF-SITE

FRBA's "Remittances and the Macroeconomy" conference

Boosting welfare and the economy back home

People who migrate from their home countries are typically seeking a higher standard of living for their families. The remittances they send back home can have a remarkably positive impact. (Migration and remittances can also bring their share of problems; see the sidebar.) Because remittances are mainly directed to relatively poor households, they play an important role in reducing absolute poverty and income inequality in recipient economies.

Chart 1
Capital Flows to Developing Economies



Source: World Bank, *Global Economic Prospects 2006*; International Monetary Fund, *Balance of Payments Statistics Yearbook 2008*, World Development Indicators 2008, and Global Development Finance 2008

The World Bank's analysis of household surveys shows that for most recipient countries, remittance income may help alleviate some inequality in income levels among households. In Mexico, El Salvador, and the Dominican Republic, the report estimates that extreme poverty would be 35 percent higher and moderate poverty would be 19 percent higher in the absence of remittances among recipient households.

Several studies, including *Close to Home*, indicate that remittances ease constraints on recipient households' budgets and allow families to spend a smaller share of total income on food and more on housing and related expenses (for example, durable goods), health, and education.

Households with migrants abroad have significantly better knowledge of basic health care and a higher probability of a doctor delivering a baby, according to the *Close to Home* report. "Children from households that report receiving remittances tend to exhibit higher health outcomes than those from non-recipients households with similar demographic and socioeconomic characteristics," the report said.

The World Bank report also points to evidence that "for some specific groups ... remittances increase children's educational attainment. However, the impact is often restricted to children with low levels of parental schooling."

A 2006 World Bank working paper by Pablo Acosta shows that remittances also reduce the incidence of child labor, allowing children to focus on schooling. For example, school enrollment is between 12 percent and 17 percent higher in families receiving remittances in Nicaragua, Guatemala, and Honduras.

Dealing With the Downside

While remittances may bring many benefits to recipient households and economies, they also come at a price. Migration imposes important, immeasurable costs on the family members left behind, particularly on children who grow up with one or both parents absent. In addition, some studies, such as the World Bank 2007 *Close to Home* report, associate remittances with a perceptible decline in employment participation of recipients who become accustomed to the steady flows of remittances without any work effort in exchange.

A potential economic problem related to these financial inflows is the so-called Dutch disease. This phenomenon, named for the Netherlands' economic condition in the 1970s, involves a sizable appreciation in the real exchange rate and a resulting loss in international competitiveness as a result of massive inflows of foreign currency to relatively small and underdeveloped economies. This rise in the exchange rate leads to a decline in manufacturing and the export of other goods that are internationally traded and is accompanied by a decline in employment. Dutch disease can undermine the potential performance of business undertakings and, for motivated individuals and would-be entrepreneurs, reinforce incentives to migrate.

Fortunately, recipient economies have several policy options to remedy some of these problems, including fiscal policies that encourage employment participation and monetary policies that reduce exchange rate misalignments.

Beyond their effects on households, remittances can enhance financial development in migrants' home countries. When remittance payments are made through financial institutions, the receiving banks can reach out to recipients without bank accounts to offer them financial products and services. According to a 2006 World Bank working paper by Reena Aggarwal, Asli Demirgüç-Kunt, and Maria Soledad Martinez Peria, total credit in the economy can significantly increase as banks direct deposited remittances to funds that can then be loaned. This increased availability of credit funding in turn boosts investment expenditures and spurs economic growth. Banked remittances also provide a means for households to finance the opening and expansion of small business and entrepreneurial activities.

From a macroeconomic perspective, remittances tend to be countercyclical in relation to the recipient economy. Immigrants tend to send additional funds back home when their relatives face severe socioeconomic hardship; these contributions reduce disposable income volatility and smooth households' consumption paths in economies historically characterized by economic and institutional instability. Thus, the inflow of remittances can dampen the current account reversal and the decline in most macroeconomic variables (such as output, consumption, and investment) in the aftermath of a financial crisis.

The inexact science of tracking immigration and remittances

Given that remittance payments are originated mainly by immigrants, it is clear that remittances and immigration are strongly linked. Thus, remittances are often used to track immigration trends. But this method has its shortcomings because immigration and remittances are both difficult to measure precisely.

Accurately tracking immigration levels in the United States is virtually impossible because the number of undocumented immigrants is unknown. A 2008 study from the Multilateral Investment Fund (MIF), which is administered by the Inter-American Development Bank, estimates that 47 percent of Latin American and Caribbean immigrants living in the United States are undocumented.

Money can be transferred among countries without any formal record, which makes remittances hard to track, but most remittance transfers are made through formal channels. According to the MIF, in 2006 the percentage of the immigrants who sent remittances through established institutions ranged from 57 percent to 88 percent, depending on the state.

Changing patterns

Growth in remittances from Southeastern states has varied in recent years. Data from the MIF show that in 2004 Florida had the fourth-highest total remittances in the United States at $2.45 billion, and Georgia had the seventh-highest total at $947 million. By 2006 remittances from Florida had increased 26 percent, and Georgia's had increased 83 percent.

This rapid growth in remittances from Florida and Georgia is largely the result of the swift influx of Latin American and Caribbean immigrants. Today about 83 percent of all Latin American immigrants in the United States live in just 10 states. In 2006 Florida ranked fifth and Georgia sixth nationally in the highest concentration of recorded immigrants from Latin America and the Caribbean, according to the MIF.

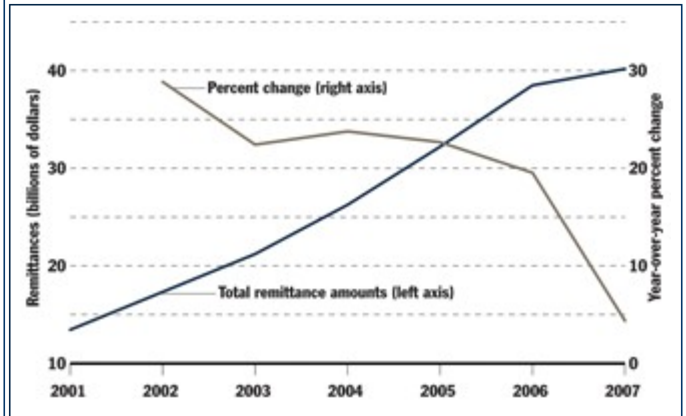
Recent developments in the United States seem to be affecting the flow of remittances abroad. A 2006 National Bureau of Economic Research working paper by Gordon Hanson argues that a declining number of apprehensions of people attempting illegal entry along the U.S.-Mexican border—despite more stringent border patrols—indicates a decline in the number of people attempting to enter the United States.

The flow of remittances seems to mirror this drop-off; remittances sent to Mexico grew only 1.4 percent year-over-year during the first nine months of 2007 compared with more than 20 percent annual growth during 2002–06, according to the MIF. The recent slowdown in remittances can also be seen on a wider scale. According to the World Bank, total recorded remittances from the United States to Latin America and the Caribbean grew from $17.3 billion in 2002 to $26.25 billion in 2004—a 52 percent increase—and to $38.5 billion in 2006, a 47 percent increase (see chart 2). An April 2008 MIF report, *Survey of Latin American Immigrants in the United States*, estimates that total remittances from the United States to Latin American countries will increase barely over 1 percent from 2006 to 2008.

The slowing growth in remittance flows was accompanied by a significant decrease in the percentage of immigrants in the United States from Latin America and the Caribbean sending remittances home. According to MIF estimates, from 2006 to 2008 the percentage of immigrants who sent money home fell from 73 percent to 50 percent in Florida, from 85 percent to 53 percent in Georgia, from 57 percent to 31 percent in Utah and New Mexico, and from 88 percent to 59 percent in North Carolina and Virginia.

Some of this decline in the number of remitting immigrants is likely tied to the current weakness in the housing market, which has slowed employment in the construction industry (see chart 3). A 2008 MIF survey found that approximately 14 percent of Latin American and Caribbean immigrants who come to the United States work in construction. When the construction market declines, undocumented workers are often the first to lose their jobs because they are typically just day laborers rather than company employees. Florida and Georgia, which were hit especially hard by the housing slump that began in 2006, also had some of the largest declines in the number of remitting immigrants.

Chart 2
Remittances to Latin America and the Caribbean



Source: World Bank

Finding the best policies

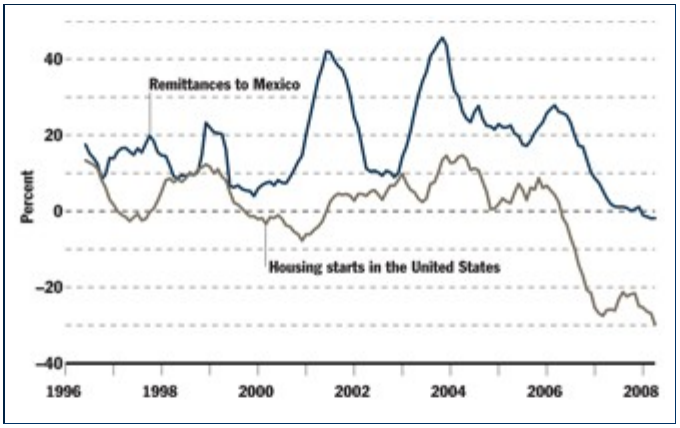
Policy can play an important role in promoting an institutional environment that facilitates remittance flows. Remittance services are currently extremely expensive, with fees that can represent 15 percent to 20 percent of the principal transmitted. The World Bank *Close to Home* study recommends policies that encourage competition among money transfer providers and enhance transparency and consumer protection. Such policies would result in more efficient and effective tracking of remittances and prevent criminal abuse of remittance channels.

Policymaking could also promote technological advances. Mobile banking and partnerships with cell phone companies may constitute an important channel to extend remittance services to unbanked individuals in rural areas. The mobile phone company Vodafone has launched a joint venture pilot program with Citigroup to explore the possibility of promoting such services in the United Kingdom.

In an effort to promote efficient remittances, the Federal Reserve has signed an agreement with the central bank of Mexico to provide low-cost automated clearinghouse (ACH) payments from the United States to Mexico. This service, Directo a México, allows U.S. commercial banks to transfer money from their customers to bank customers in Mexico using the Federal Reserve System ACH network.

Chart 3
Growth Rates of Remittances and Housing Starts

"The number of financial institutions offering account-to-account transfer services, including Directo a México, is



Source: Banco de México and U.S. Bureau of Labor Statistics

growing steadily, and their customers are responding positively," said Elizabeth McQuerry, assistant vice president in the Atlanta-based Federal Reserve's Retail Payments Office, which administers the program. "Additionally, banked transfers bring remittances into the formal financial system, where individuals can not only have access to credit, but the transfers take place between regulated financial institutions in both countries."

Economics and politics cloud remittances' outlook

Like other money transactions, remittances tend to rise and fall with the economy: The economy drives labor market trends, which drive immigration trends, which drive remittance flows. Current virtually stagnant remittance growth has several possible culprits—a slowing U.S. economy, a number of Latin American and Caribbean countries experiencing relatively robust economic growth, and a lack of jobs in industries such as construction and manufacturing, which typically employ high concentrations of immigrants from these countries.

These conditions are directly affecting remittance growth because they make it more difficult for immigrants to send money home and provide little or no incentive for individuals in poorer countries to immigrate to the United States. Although this slowdown may be cyclical, the growing anti-immigration sentiment in the United States and other advanced economies may pose long-term difficulties for potential remitters. How these factors play out will influence the outlook for a vital source of income for impoverished residents of other countries.

This article was written by Federico S. Mandelman, a research economist and assistant policy adviser at the Atlanta Fed, and Courtney Nosal, an economic analyst at the Atlanta Fed.

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Plumbing the Gulf's Depths for Oil and Gas

Historically high oil prices and gradually dwindling supplies of easily accessible oil and gas deposits worldwide have inspired energy firms to renew and expand exploration and drilling in the Gulf of Mexico. Advances in technology and engineering have not only increased the chances of finding oil deposits but also made it physically possible—and more economically feasible—to plumb depths never before reached in the search for liquid gold.

Photo courtesy of Global Santa Fe

Increased interest in extracting oil and gas from deepwater sites has proved a boon for drillships like the *Jack Ryan* (pictured here). These ships are designed both to carry drilling platforms to deepwater locations and to perform drilling operations on their own.

As oil prices soared during 2007 and 2008, Allen Verret pondered whether the high prices would spark a new boom for Gulf of Mexico oil and gas production.

"You would assume that with a price at an all-time high there would be an all-time high in permits secured to do drilling, in work orders and other activity," said Verret, executive director of the Offshore Operators Committee, a trade group of petroleum firms that work in the Gulf.

Without question, plenty is happening in the Gulf's murky depths, some of it driven by rising fuel prices. Yet, for many reasons, high crude oil prices have not set off a mad rush to extract the Gulf's long-buried hydrocarbons, as oil and gas deposits are called in industry parlance.

"I don't think because oil hits $130 a barrel that you're going to see, all of a sudden, a surge in activity," said Jeffrey Goetz of Poten & Partners in New York, a consultancy that works with shipping and energy services firms.

The business of oil and gas production simply does not lend itself to sudden surges. Finding and pumping oil and gas from miles under the Gulf seabed takes too long—generally five years to a decade from discovery to production—and costs too much, often more than $1 billion in capital investment to develop a field.

Signs of resurgence

A slow expansion of exploration and production work is afoot, though, especially in the Gulf's deeper water 100 miles and more from shore. After leaving in recent years, a few mobile drilling rigs are returning to the Gulf from other parts of the world, still more are under construction, and major petroleum companies recently paid record prices to explore in depths where it has historically been cost prohibitive to produce oil or gas.

"Gulf of Mexico activity today is greater than most observers anticipated even six months ago," said Dean Taylor, chairman, president, and chief executive officer of New Orleans–based energy services company Tidewater Inc., in a July 31 conference call with analysts and investors.

Related Links

[MMS's Gulf of Mexico oil and gas production forecasts](#) OFF-SITE

[MMS report on Gulf of Mexico energy exploration](#) OFF-SITE

[Entergy-Tulane Energy Institute Web site](#) OFF-SITE

[Rigzone.com: Information about the oil and gas industry](#) OFF-SITE

[Gulf of Mexico Energy Exploration and Production](#) (MP3 8:14)

After falling for four straight years, Gulf of Mexico oil production climbed 7 percent in 2007, to 1.34 million barrels a day (see the [chart](#)), and will likely rise in each of the next five years, according to projections from the U.S. Department of the Interior's Minerals Management Service (MMS), which regulates and serves as landlord for the Gulf's offshore drilling.

The production of natural gas—which comes from the earth in gaseous form from many of the same rigs that pump oil—also appears to be on the upswing in the Gulf, although not as sharply as oil production. The MMS estimates that the Gulf's gas production was roughly 8 billion cubic feet per day (cfpd) in 2006–07, down from a plateau of about 14 billion cfpd from 1996 through 2001. But, based on new discoveries and producers' announced plans, the MMS projects that gas production will rise slowly over the next few years to 9.8 billion cfpd in 2014.

Drilling deeper

In recent years, the Gulf of Mexico offshore energy industry has evolved into two distinct segments—shallow water and deepwater. Easy-to-reach gas and oil in shallower waters have been largely depleted, so the major companies have moved farther offshore. At the same time, advances in discovery and drilling technology—along with higher market prices that fuel greater investment—are making it more economical to find and extract oil and gas in deep waters, defined as more than 1,000 feet, and even in ultradeep seas of 7,500 feet and more.

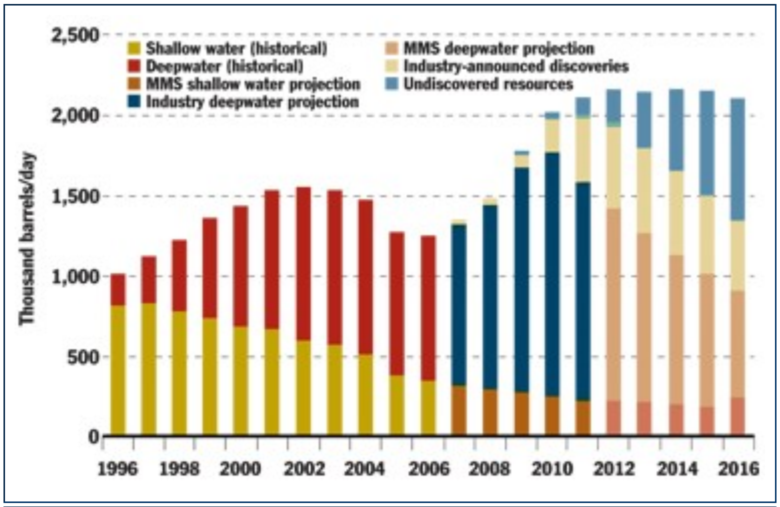
At the end of 2007, the MMS reported that 130 projects were producing oil and gas in the deepwater Gulf of Mexico, double the number from five years earlier. Firms are plunging their diamond-tipped drill bits through ever deeper water: In 2007, a record 15 rigs were drilling for oil and gas in water depths of 5,000 feet or more.

Experts believe far more deepwater work will likely occur. At least 13 drilling rigs are currently being built and should be in use in the ultradeepwater Gulf in the next two to three years, the MMS reports. These rigs can work in water 12,000 feet and drill to seven-and-a-half miles, or 40,000 feet, under the sea floor.

These ultradeepwater rigs don't come cheap. Thunder Horse, the world's largest moored semi-submersible platform, located 150 miles southeast of New Orleans, cost $1 billion just to build the production rig alone. The total development costs, though—including not only construction but also seismic surveys, preliminary drilling, towing it to sea, and repairs of mechanical problems and hurricane damage during construction—are around $5 billion, according to several news reports.

Despite such hefty price tags to develop these massive platforms, recent sales of drilling rights indicate a long-term interest in deepwater expansion. Exploration companies in March 2008 paid $3.7 billion in winning bids for leasing rights in the deepwater Gulf, the most money raised in a single auction since the federal government began offshore leasing in 1954. Two 2007 lease sales attracted a combined $3.2 billion in winning bids.

Historical and Projected Oil Production in the Gulf of Mexico



Source: Minerals Management Service (MMS), *Gulf of Mexico Oil and Gas Production Forecast: 2007-2016*, figure 2 (May 2007)

The areas in ultradeep water are attracting the most interest and dollars. In 2007, exploration companies bid on 152 "blocks," or sections of the Gulf, in waters greater than 7,500 feet deep, according to the MMS, up from just six blocks bid on in 2006. In the 2008 auction, more than 93 percent of the total of the winning bids was spent on deepwater blocks.

Motivated to produce

Tidewater Inc. CEO Taylor said exploration in the Gulf of Mexico is spurred in part by the rise in natural gas prices in late 2007 and the first half of 2008. He noted that the industry expects three to five of the rigs that had left in recent years to return to the Gulf later in 2008.

In another sign that energy producers are busier in the Gulf, Tidewater reported that the day rate it charges customers to use its boats in the Gulf increased 9 percent in the second quarter of 2008 from the previous three months. Tidewater operates the world's largest fleet of boats, more than 450, serving the offshore energy industry.

Much of the demand for services like Tidewater's appears to be coming from major oil companies plumbing the Gulf's deep waters. Giants such as British Petroleum (BP), BHP Billiton, Royal Dutch Shell, Chevron, and Devon Energy began producing oil and natural gas from several new fields in the Gulf in 2007, and more projects are due to come online in 2008 and 2009.

For example, BP announced that in late 2008, after a series of delays, it will begin extracting oil and gas at Thunder Horse, which can produce up to 250,000 barrels of oil a day, nearly a fifth of the Gulf's total production in 2007.

Meanwhile, in late 2007 and the first half of 2008, Australia-based BHP Billiton began pumping oil from three deepwater fields, boosting its Gulf production more than eightfold—to 100,000-plus barrels of oil a day from an average of 12,000 a day in its 2007 fiscal year. Another major field, Tahiti, in which Chevron owns a 58 percent interest, is expected to produce its first oil in 2009. Chevron predicts that the $4.7 billion project will generate as much as 125,000 barrels of oil and 70 million cubic feet of natural gas a day.

Oil and gas prices that most experts expect to remain elevated over the longer term are motivating exploration in the Gulf and worldwide, said Eric Smith, associate director of the Entergy-Tulane Energy Institute at Tulane University in New Orleans. Global oil and gas exploration and production spending will rise 20 percent in 2008 versus 2007, according to a midyear survey of 398 energy companies by the former investment bank Lehman Bros. And the world's largest oil company, ExxonMobil, reported that capital and exploration spending was up 35 percent, to $12.5 billion, in the first half of this year.

Energy still golden in Louisiana

Louisiana, more than any other state in the Southeast, benefits from a strong energy industry, even though energy does not dominate the state's payrolls as it once did. Less oil is being produced in state waters and on land than in the past, and that production has become less labor intensive. Also, some large energy companies have moved their corporate offices out of the state. Still, on most days, Smith figures, 10,000 to 15,000 people are working off Louisiana's shore and another 25,000 to 35,000 on land in the industry. Louisiana's oil and gas production employment, although currently almost 40 percent lower than in 1985, has climbed each year since 2004. The monthly average in 2007 through September was 46,759, up about 6,500 jobs from 2004, according to the Louisiana Department of Natural Resources.

Photo courtesy of British Petroleum

Thunder Horse, jointly operated by BP and ExxonMobil, is the world's largest semi-submersible drilling platform. It has the capacity to process and export a quarter million barrels of oil a day.

Many of those jobs are high paying. For instance, operators of small unmanned submarines and heavy, sophisticated cranes aboard offshore rigs typically earn more than $100,000 a year, Smith said.

Back on land, the energy services industry in Louisiana is growing. Port Fourchon in Galliano, about an hour southwest of New Orleans, serves much of the offshore oil and gas business in the Gulf. The port is in the midst of doubling its size to more than 1,500 acres.

Although most of Tidewater's revenue and profits are generated outside the United States, the New Orleans–based company also enjoys strong domestic operations. Tidewater's two shipyards in Houma, La., have produced four 220-foot platform supply vessels in the past three years and are now building two 250-foot supply ships. In the past eight years, Tidewater has purchased or built 140 vessels for about $1.6 billion, according to company reports.

McMoRan Exploration Co., also headquartered in New Orleans, has been able to reduce debt and invest in potentially rich natural gas fields in the Gulf of late, according to James Moffett and Richard Adkerson, the company's co-chairmen. McMoRan's specialty is returning to depleted fields in the shallower Gulf and drilling deeper into the seafloor for untapped reservoirs of gas.

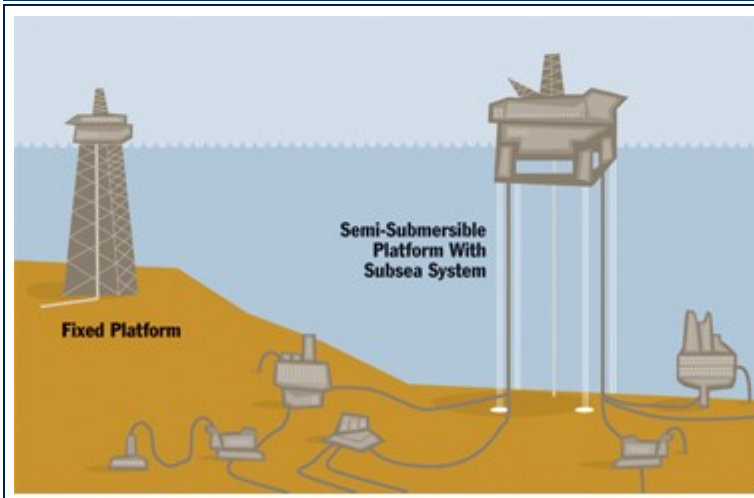
This year, in fact, the company drilled what is billed as the deepest well ever at a field called Blackbeard, in just 70 feet of water in the Gulf. (Like most major offshore oil and gas projects, Blackbeard is a partnering venture among McMoRan and other firms, though McMoRan is the operator.) ExxonMobil gave up on Blackbeard after drilling to 30,000 feet, or 5.7 miles, under the seabed. McMoRan reported in July that it had reached 35,000 feet at Blackbeard and was going deeper in search of natural gas.

Technology gives and takes

Another Louisiana firm that is prospering along with the energy industry is C&C; Technologies of Lafayette, a privately held company with 400-plus employees. The company designs highly sophisticated autonomous underwater vehicles, or AUVs. The machines, which look like capsules with fins at the stern, are programmable submarines that are dropped from a ship or platform and cruise the sea floor for up to 50 hours at a time, helping to locate the best routes for pipelines and performing other work in depths divers cannot safely reach.

Only a handful of AUVs are operating around the world, Smith said. The machines advance the more common technology of remotely operated vehicles (ROVs). Unlike an AUV, ROVs are generally tethered to a ship or platform and guided by an onboard operator. They maintain drilling and pumping equipment and do other submarine chores. An AUV needs no driver because internal computers store its instructions.

Two Oil Rigs, One Objective



While economics and technology are stimulating more exploration in the Gulf, other forces are working against it. Among those are shortages of expert labor and equipment and a resulting rise in prices for equipment and materials, Smith and other experts said.

Indeed, in August the BP Web site included a help-wanted notice for offshore technicians in its Gulf of Mexico operations. In the past 20 years, the United States has not produced enough petroleum engineers to satisfy the current demand, not to mention other workers such as technicians and operators of ROVs, Smith said, noting that during sluggish times in the industry fewer people enter the field.

"The industry is so cyclical that we have a missing generation, if you will," Smith said. "We just don't have the people to do the work."

What's more, he said, most of the companies that produce the more sophisticated offshore equipment are European. Norwegian firms, particularly, took the lead in offshore technology while working in the North Sea through the 1970s, '80s, and '90s, said Smith, who held strategic planning positions at major energy companies before joining Tulane's faculty.

Marvels of engineering

Today's oil platforms are considerable engineering feats. The biggest, like Thunder Horse, are as long and wide as three football fields, with tons of pipes, pumps, storage tanks, compressors, and drilling equipment, along with living quarters, kitchens, lounges, and small medical facilities. The design of the structures has evolved from rigid legs that extended to the sea bottom in shallower water to the latest semi-submersible platforms.

Those platforms are typically built on land and towed to the drilling location, where ballast tanks filled with water hang about 80 feet underwater to stabilize the structure. Enormous chains anchor the platform to the sea bottom. Some of the newest rigs are not anchored to the bottom but include systems of pontoons and ballasts designed to keep them stationary.

These designs are critical because the most difficult engineering problem involved in the offshore drilling process is keeping a rig in place amid powerful currents and waves, according to BP. Hurricanes Katrina and Rita proved that even giant rigs can be tossed about by nature.

There is plenty more infrastructure underwater too. Modern production platforms do not simply drill and pump oil from directly below. Gas and oil wells spread over miles of sea floor are often tied back to a single platform.

For example, the Independence gas hub in the Gulf, which began production in 2007, is at the center of 10 undersea fields spread over an area as large as metropolitan Atlanta or Houston. Its longest subsea tieback, linking a well to the platform, stretches 45 miles. Most subsea wells are within 10 miles of the host platform, but the longest tieback in the world currently is 62 miles, part of the Mensa platform in the Gulf, according to a 2008 MMS report.

Drilling ships are also sometimes used in ultradeep water. Networks of propellers are programmed to keep these vessels still while they bore into the seabed.

Photo courtesy of British Petroleum

The science of sighting

Of course, energy companies do not invest huge sums to drill blindly. The search for oil and gas has advanced as much as the methods of extracting it. In the late 1940s and '50s, offshore seismic surveys involved throwing dynamite from a boat and reading the sound waves that bounced back to the surface. Nowadays, air guns fire acoustic pulses to the ocean bottom and through the rock below. Sound waves bounce off surfaces within underwater rock to microphones nearer the water's surface. Using supercomputers, geologists analyze the data collected by the microphones and map the rock formations, projecting 3-D images that look like tie-dyed patches onto large screens and looking for patterns that suggest reservoirs of oil or gas might be present.

The Mars platform, a joint venture between Shell Oil and BP, operates in the Gulf of Mexico and produces 220,000 barrels of oil and 220 million cubic feet of natural gas a day.

Advances in seismic techniques have increased the hit rate from 10 percent or less in early offshore days to about 50 percent for wells drilled in areas with no existing oil or gas production, according to Smith and to BP's Web site.

All this design and technology are aimed at finding big reservoirs of hydrocarbons and then tapping them in a way that will allow enough oil or gas to be extracted to make the venture profitable. Until recently, production rates (the volume at which oil can be pumped out) from the deepwater fields were not sufficient for commercial success, Smith said.

Aside from finding the oil or gas and then accessing it, bringing it out has been a huge challenge. Extraordinarily high temperatures of rock and liquids, along with crushing pressure that collapses the pipe that sucks out the oil, are among the difficulties. Reservoirs of oil or natural gas are often trapped within the pores of rocks, like a fossilized sponge, and not in large underground pockets that would be easier to drain.

Once they get oil or gas out of those rocks, producers must then tie into the Gulf's existing pipeline network, which now totals about 33,000 miles. As drilling goes farther and farther from shore, and thus from the pipelines, some companies are experimenting with sending their oil and gas to shore via tanker ships, Goetz said.

It appears that oil and gas exploration and production in the Gulf of Mexico will continue to move farther offshore and deeper under the sea floor. But there might not be a boom coming. Compared to some other oil-rich regions of the world, the Gulf's petroleum is expensive to find and produce. And while high prices make producing that petroleum more economical, they also have shown signs of reducing U.S. demand for oil and gas. It seems certain, though, that if oil and gas remain expensive, efforts will only intensify to find it and pull it from the nethermost crannies of the earth under the Gulf of Mexico.

This article was written by Charles Davidson, a staff writer for EconSouth.

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Economic Research

ECON SOUTH

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FED @ ISSUE

John C. Robertson is a vice president and senior economist in charge of the macropolicy and applied microeconomic research group in the Atlanta Fed's research department.

Figuring Out the Oil Price Puzzle

A quiz: Gasoline prices during the first half of 2008 were higher than a year ago because of

a. strong growth in global demand,
b. the weak U.S. dollar,
c. weak supply growth, or
d. excessive speculation in oil futures markets.

"All of the above" would be a reasonable choice. But I would argue that (a) and (c) are the key factors in the current story of high energy prices.

At present, underlying global demand for oil is strong but is being tempered by high prices. Global oil demand is now more resilient than in the past in part because of subsidies protecting consumers in some countries and because of robust economic growth in very populous countries outside the Organisation for Economic Co-operation and Development (OECD). The weaker dollar has also contributed to higher oil prices, but it's important to note that oil prices in other currencies also hit record levels.

Prices up, consumption down

As oil prices reached record highs recently, oil consumption responded by falling in developed OECD countries, where consumers usually face market-based prices. An interesting question is what would have happened if prices had not risen. Here are some simple economic calculations. In the second quarter of 2008, U.S. gross domestic product grew by 2.2 percent year over year. Assuming a growth response of 0.5, oil demand would be 1.1 percent higher if the price remained unchanged. In the second quarter of 2007, U.S. oil consumption was around 20.6 million barrels per day (mbd), so, with constant prices, consumption would have been predicted to rise to above 20.8 mbd by the sescond quarter of 2008. But during that quarter consumption was only 20.4 mbd. That drop was surely related to the fact that oil prices averaged $124 per barrel in the second quarter—up almost 70 percent from the average 2007 price.

The supply-demand seesaw

All told, supply has not kept pace with demand growth, and this development is another important factor behind today's high prices. Cuts in OPEC production in 2006 and 2007 initially spurred the run-up in oil prices. And even though more recently OPEC has increased output, spare capacity remains very low. Moreover, non-OPEC oil-producing nations have failed to increase output despite favorable prices.

The fundamental supply problem is not one of global resource constraints. Most estimates suggest the life span of global proved oil reserves has not declined. In fact, proved reserves should be sufficient to sustain current levels of world consumption for several decades. The problem is more about accessibility (such as environmental and location issues and technological and labor constraints) and deliverability (refinery bottlenecks). These difficulties have caused the short-term cost of producing more oil to skyrocket.

Is speculation skewing the balance?

The usual counterargument to the supply-and-demand explanation outlined earlier is that oil prices were driven higher by speculation in oil futures markets by noncommercial interests (those unrelated to the physical oil market and without an economic need to hedge against oil price changes), with hedge funds and index funds identified as the primary culprits.

However, recent studies by the International Energy Agency and the Commodity Futures Trading Commission (CFTC), among others, have investigated this concern but have failed to find compelling support for the argument that excessive speculation in futures markets is behind the oil price run-up. For one thing, prices have also risen for most primary commodities, including those traded in futures markets as well as those traded in physical markets where little or no speculative involvement takes place: liquefied natural gas, coal, iron ore, minor metals, silicone, rice, bananas, and fish meal, among others. In addition, price increases across the commodity spectrum have not been particularly synchronized.

Perhaps even more importantly, if speculators are persistently driving spot prices higher than the equilibrium of the underlying supply by producers and demand by refiners and consumers, then an imbalance in the form of higher stocks should be apparent. In prior historical episodes of speculative bubbles (such as with tulip bulbs and silver), higher stocks were evident. In the recent run-up in oil prices, however, OECD oil inventories have remained well within historical norms during the past two years.

What specific role have noncommercial traders (such as hedge funds) played in price setting? The CFTC study shows that changes in commodity prices tend to be positively correlated with net long positions of noncommercial traders. But this correlation doesn't appear to have behaved differently in the recent period. In fact, the study suggests that noncommercial positions do not predict prices. If anything, the relationship is one of trend chasing—that is, price changes leading to changes in noncommercial positions.

Some people have also argued that increased investments in commodity index funds have pushed commodity prices above levels consistent with supply and demand. The amount of money invested in commodity futures contracts through index funds has indeed increased sharply in recent years, consistent with the marketing of commodities as an asset class and a tool for portfolio diversification. Most of these increases, however, appear to reflect valuation changes associated with higher prices. In fact, during the past year the number of futures contracts held by index traders has been relatively stable for the few commodities for which such data are available. In addition, these traders do not take delivery of the physical product. Thus, every long position held by a speculative trader unwinds before expiration of the futures contract. Averaged over time, the net demand from speculators tends to balance out.

Waiting for relief

In summary, the crude outlook remains relatively tight with little supply relief in the very short term, although more supplies appear to be on the horizon. Inventories are not unusually high, and demand is slowing, especially in developed countries. Finally, the available evidence does not support the argument that speculators have driven prices above the levels consistent with supply and demand.

So while price increases are still possible, demand and supply factors that will dampen the upward pressure on prices appear to be evolving.

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Grassroots

Tourism, Manufacturing Revive Chattanooga

If there were an award for the city that has won the most awards, it might well go to Chattanooga, Tenn.

Photo courtesy of the Chattanooga Area Chamber of Commerce

The renovation of the Walnut Street Bridge, the world's longest pedestrian bridge, has contributed to the revival of downtown Chattanooga.

A host of media outlets have hailed Chattanooga, located on the Tennessee River in the Ridge-and-Valley Appalachians, as an eco-friendly ideal of urban transformation. *Southern Living* readers named the city their third-favorite place in the South to take children, behind only the tourist meccas of Walt Disney World and Orlando, Fla.

Since 1990, local and state government, private businesses, and local charitable foundations have invested more than $2 billion in downtown Chattanooga—in an aquarium, parks, a river walk, historic theaters, bike paths, small inns, museums, residences, and one of the world's longest pedestrian bridges. The city even runs free electric buses downtown.

And the city is about to receive an economic boost. The German automaker Volkswagen announced in July that it will build a $1 billion plant—its first in North America since it closed a Pennsylvania plant in 1988—just outside Chattanooga. The plant will employ between 2,000 and 2,500 people when it begins production in 2011.

"Chattanooga is a model of what a mid-sized downtown can achieve when its community unites in a common cause," said RevitalizationOnline.com, a Web site about restoring communities. And *Utne Reader* magazine noted several years ago, "Chattanooga's progress, past and present, demonstrates that problems, however onerous, needn't defeat people who care."

Clearing the air

Chattanooga has had its problems. A former iron smelting hub, the city enjoyed prosperity through the 19th and 20th centuries that had its downside: dirty air. The city began cleaning up after the federal government in 1969 dubbed Chattanooga's air quality the nation's worst. A local newspaper editor once told National Public Radio that pollution used to make his white windowsill look like it had pepper sprinkled on it.

In the

Chattanooga, Tenn.

Population	151,944
Hamilton County population	312,905
Households (city)	65,518
Median household income	$36,981

Source: U.S. Census Bureau's 2006 American Community Survey

1970s, local factories agreed to install pollution-control devices. In addition, iron and steel foundries declined through the 1970s and '80s. Although improving the air quality, the industrial decline also hammered the city's employment base. "We've been on a climb back ever since all of that happened," said Tom Edd Wilson, a retired banker and president of the Chattanooga Area Chamber of Commerce. "It's been an interesting climb."

The climb took a big step in the early 1990s. City leaders launched a downtown revitalization campaign lauded for its inclusion of citizens from various neighborhoods, socioeconomic strata, and ethnic groups. The aquarium opening in 1992 and the christening of the Walnut Street Bridge the following year were two of the most visible early components of the downtown resurrection. The bridge, a 100-year-old span over the Tennessee River, was slated for demolition but instead was renovated as a walkway. Downtown Chattanooga also now boasts 140 acres of parkland, up from virtually none before the revitalization.

By most accounts, the downtown makeover has succeeded wildly. The city of about 152,000—and metro area population of 514,000—attracts some three million visitors a year. Many of them are drawn to the riverfront, whose $120 million rejuvenation was completed in 2005.

That renewal project included a $30 million expansion of the Tennessee Aquarium, the linchpin of the downtown resurgence; a $19.5 million expansion of the Hunter Museum of American Art; and $61 million spent on a pier and bridge, boat slips, green space, and the rerouting of a four-lane highway to improve pedestrian access to the river.

Tourism can't go it alone

The resurgence of the city's downtown has been a boon for tourism. But tourism alone is not a solid base for the local economy, said Bruce Hutchinson, an economist at the University of Tennessee-Chattanooga. He points out that tourist attractions, hotels, and restaurants offer mostly lower-paying service jobs with little chance for advancement.

After expansion through the 1990s, job growth in the Chattanooga area has slowed. Through May, total nonfarm employment in 2008 averaged 246,800. This figure is up from 238,400 in 2000 but is down from 2007, according to the U.S. Bureau of Labor Statistics. Some of the city's larger employers—the Tennessee Valley Authority, DuPont, and Wheland Foundry Co., to name a few—have shed jobs over the past several years.

Along with Tennessee and the nation, Chattanooga has shown other symptoms of slowing: The value of permitted residential and commercial construction projects fell 30 percent in 2007 compared to 2006, and retail sales growth in Chattanooga's Hamilton County slowed to 2.6 percent from 7.9 percent during the same period, according to the Chattanooga Area Chamber of Commerce.

Facts About Chattanooga

- In 1899 Chattanooga became the first city to bottle Coca-Cola.
- The Moon Pie was created in Chattanooga in 1917 and has been produced continuously since then.
- The country's first miniature golf course was built in Chattanooga in 1929.

Nevertheless, in spite of weakening in some old-line industries, the local economy overall has been performing better than it should have, Hutchinson said.

One reason for that performance is a handful of large construction projects in the metro area. Blue Cross and Blue Shield of Tennessee is building a $300 million, five-building campus headquarters scheduled for completion in June 2009. Alstom, a French manufacturer of power generation equipment, is constructing a factory to make generators for nuclear power plants, a $280 million investment expected to add 300 jobs when it begins production in 2010. Memorial Health Care System is spending a similar amount on an expansion.

The insurance industry has become a local stalwart. Blue Cross and Blue Shield of Tennessee is the area's largest employer, with 4,800 workers, while Unum Group and Cigna HealthCare are also among the top 10.

Meanwhile, downtown development has not stopped. More than 400 condos were completed in late summer and early fall. Despite the nationwide housing slump, two big projects in Chattanooga appear healthy, said Jeff Pfitzer, director of special projects for the River City Co., a private nonprofit and a leader in downtown development. As of Aug. 1, a 200-unit building was 75 percent presold, and a 100-unit building had 65 percent of its residences sold, though those sales have not all closed, Pfitzer said.

Rolling out the welcome wagon

But of all the boosts to the modern Chattanooga economy, the biggest one in recent history is Volkswagen's plant. Auto plants typically attract a fleet of suppliers, so Chattanooga business boosters are aglow. To prepare for challenges along with an anticipated bonanza, Wilson and several other Chattanooga officials have visited Greenville and Spartanburg, S.C., to study that area's experience with the BMW factory that opened there in 1994.

State and local governments and community colleges will help provide job training as part of an incentive package awarded to Volkswagen that is expected to total at least $400 million, according to the *Chattanooga Times-Free Press*. Training will be "a huge undertaking," Wilson said. Local schools also must prepare for an influx of students.

No one yet knows how many Volkswagen jobs will be filled by Chattanoogans or how many people the company might move from elsewhere. Soon after Volkswagen's news conference in July, though, it was already clear that luring the automaker polished Chattanooga's image as a city for commerce and not just a nice place to live and play. "The psychology is playing out very positively for Chattanooga," Hutchinson said. "We shouldn't underestimate that in terms of businesses seeing it as a viable place to grow."

This article was written by Charles Davidson, a staff writer for EconSouth.

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ECON SOUTH

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Q & A

"We Know These Are Difficult Times"

An Interview With Barb Godin of Regions Bank

As pressures in the housing market mount, increasing numbers of homeowners are facing the threat of foreclosure. Some banks have instituted programs to assist customers who find themselves in this situation. Barb Godin, executive vice president and consumer credit executive for Regions Bank in Birmingham, Ala., discussed steps her bank is taking in this area.

BARB GODIN

Title	Executive vice president
Organization	Regions Bank
Web Site	http://www.regions.com/
Other	Before joining Regions in 2003, Godin was executive vice president and chief consumer credit officer for KeyBank. Previously, she held various positions at Scotiabank, including senior vice president of retail lending, vice president of credit risk management, director of collections, and director of consumer underwriting. She received an MBA from the University of Western Ontario and is a graduate of the International School of Banking.

EconSouth: *What kind of consumer hardship problems has Regions Bank been encountering?*

Barb Godin: Generally, the first mortgages we originated were sold to Freddie [Mac] and Fannie [Mae]. So we've been dealing mostly with home equity loans. A lot of these are second mortgage loans in Florida, cases where the customer is less invested in staying as opposed to primary residences. Along with the problems in Florida, there have been problems in the inner cities, and we've also seen an increase [in foreclosures] along the coast in Alabama.

ES: *What are some steps you've taken to address the foreclosure problem?*

Godin: We want to identify problems before they get out of hand. We will call people who are close to their limit on home equity lines of credit. If we notice a repayment pattern change or a credit score decline, we'll give them a call. Most people are glad to hear from us. They know we're not fair weather bankers. For those who need more help, we'll put them through a customer assistance plan. We're open to rewriting the loan and extending the repayment period. If we need to, we'll go from 10 to 20 years or 15 to 30 years—whatever works to keep people in their homes.

Depending on the problem, we can suspend foreclosure actions or do what's called a short sale. Basically, that's an agreement to accept a lesser amount than is owed to release a lien against the property so that it can be sold. Also, we have a program for certain borrowers to avoid foreclosure known as Keys for Cash. We will pay them to vacate their home. We make an offer, and we give them a check if they leave the house in good working order.

We know these are difficult times. We recognize foreclosure is a very emotional process. But as long as they're willing to talk, we'll listen. It's not just an ability to pay that we're looking for but also a willingness.

ES: *What are some of the things that Regions Bank has done to mitigate your customers' foreclosure problems?*

Godin: One of the most important steps we've taken is our enhanced Web site. We have launched portals called Home Equity Payment Hardship and Mortgage Payment Hardship. These provide a way for customers who have payment hardship to reach out and start a conversation with us on their options. I would describe it as a kinder, gentler approach.

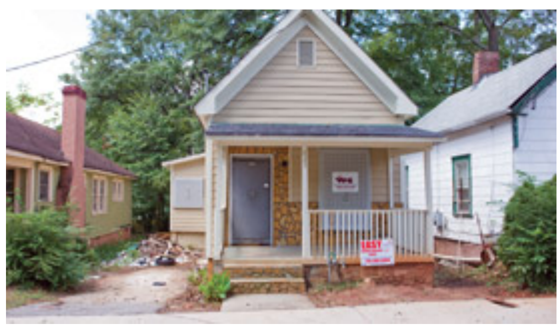

Photo by Brad Newton

To help borrowers avoid foreclosure, Regions has set up programs to help homeowners, including a Web site and a toll-free phone number, that permit them to discuss their options.

ES: *How do these programs work?*

Godin: To begin with, there's an 800 number to call us toll-free. There's also a link to a financial assistance form that borrowers can send in to explain their financial hardship. So they have a choice to send in the form or call.

ES: *What other information do you provide on the Web?*

Godin: We've found that it helps to explain some of the jargon that comes with the mortgage process, and that information is on our Web site. We try to answer questions such as, What is a repayment? What's modification? We explain the meanings of these kinds of terms in both English and Spanish. Also, there's a free DVD available with some examples of customers we've helped.

ES: *What kind of reaction have you gotten?*

Godin: We've received a good response and a lot of nice feedback. People have said, "Thanks for doing this." With a telephone call, people are afraid they will be judged for their problems—or worse. But if they go to the Web they're not threatened. They start to recognize that there might be a payment plan that could work for them. The Web helps to do away with the fear of being rejected.

ES: *What have been the results of this effort?*

Godin: We started this customer assistance program in October 2007. Since that time through our Web site we've helped 1,070 customers and worked with loans amounting to $270 million. These loans have involved some form of modification or forbearance.

ES: *What are the origins of this program?*

Godin: This project is an extension of best practices we learned after Hurricane Katrina when many of our customers experienced a different kind of hardship. We dedicated a group to customer assistance, and we've expanded staff to cope with foreclosures. The difference with the subprime meltdown is that we're not dealing with a natural disaster like a hurricane. It's a manmade disaster.

This interview was conducted by William Smith, a staff writer for EconSouth.

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ECON SOUTH

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The State of the States

Recent events and trends from the six states of the Sixth Federal Reserve District

- For the third quarter of 2008, the Compass Bank Business Leaders Confidence Index for Alabama was 42.7, only 0.2 points below its second quarter reading. (A reading above 50 indicates expansion, below 50, contraction.) The bank's economic outlook index declined by 0.9 points to 45.2, almost 19 points below its level from a year earlier. However, declining expectations in both indexes have leveled off during the past few months.

- In early May, Atlanta-based Home Depot broke ground on a new distribution center in McCalla. The $33 million center, targeted for completion by the end of 2008, will initially employ 214 people. The 657,000 square foot facility is being built on a 70-acre site in Jefferson Metropolitan Park. Home Depot expects that the facility will help improve service and efficiency at its Southeastern U.S. stores.

- The Florida consumer confidence index rose to 60 in July from its all-time low of 59 in June, signaling that Floridians may be looking ahead to when the housing market picks up. "Consumers are quite gloomy about their current finances, but expect some change over the next

Related Links

[REIN (Regional Economic Information Network) Data and Analysis]

[Compass Bank Business Leaders Confidence Index for Alabama] OFF-SITE

[Florida Consumer Confidence Index (University of Florida)] OFF-SITE

["Examination of the Development of Liquefied Natural Gas on the Gulf of Mexico"] OFF-SITE

[University of Southern Mississippi July 2008 economic outlook conference] OFF-SITE

[Middle Tennessee Consumer Confidence Reports] OFF-SITE

year," said Chris McCarty, survey research director for the University of Florida's Bureau of Economic and Business Research. "Floridians may be looking ahead to a bottoming out of home prices, which may come sooner than expected, and a pickup in sales, which will probably not occur until next year."

- In May, Gov. Charlie Crist announced that Piper Aircraft plans to keep its headquarters in Vero Beach and further expand manufacturing operations there. By 2012, Piper plans to add more than 450 jobs to the 960 already on the payrolls.

- Manufacturing activity in Georgia remained unchanged in July, according to the Econometric Center at Kennesaw State University. The center's Georgia Purchasing Managers Index (PMI)—a snapshot of the state's manufacturing sector—was 49.6, the same level as in June. (A reading above 50 indicates expanding manufacturing activity, below 50, contracting activity.) The reading indicates some stability but also reflects a weakness in manufacturing that began in December 2007. "The manufacturing sector doesn't see a long-term sustainable trend," said Don Sabbarese, the center's director.

- In May, Korea-based Kumho Tire Co., one of the world's top 10 tire manufacturers, broke ground near Macon on its sixth overseas plant. The $225 million, 5.7 million square foot facility, slated for completion by the end of 2009, is expected to provide more than 450 jobs and initially manufacture more than 2 million tires per year for original and replacement equipment markets in the United States.

- David Dismukes, associate executive director of Louisiana State University's Center for Energy Studies, recently published a study examining the role, importance, and development of liquefied natural gas (LNG) regasification facilities along the Gulf of Mexico. The study finds that the Gulf is probably the best location in the United States for the development of LNG regasification facilities because the region has a large energy infrastructure that can support and serve as a market for LNG.

- In June, Zagis USA broke ground on the first of two textile mills in Jefferson Davis Parish. The company will invest $75 million in a two-phase cotton spinning project that will bring 160 new jobs to the area. The average annual wage will be $31,000 plus benefits. The first phase is estimated to be completed by late fall of 2008, and the second is projected to begin in early 2009.

- At an economic outlook conference in July sponsored by the Bureau of Business and Economic Research of the University of Southern Mississippi, William Gunther, the bureau's director, reported that Mississippi's economy tends to parallel the U.S. economy and that weak job growth will likely continue for the rest of 2008. He expects job losses in manufacturing, retail trade, and nonresidential construction and only marginal gains in health care and in business and professional services in the second half of the year. For 2008 as a whole, he believes total employment growth will likely be negative.

- PK USA Inc., an automotive parts supplier, announced earlier this year that it will open a new stamping and welding assembly plant in Senatobia. The 200,000 square foot facility will employ 150 people when it begins production in 2010. The plant will supply the Toyota plant now under construction in Blue Springs as well as other Japanese manufacturers and suppliers in the state.

- A recent Middle Tennessee State University survey of local consumers showed that confidence has fallen to its lowest level since the beginning of 2003, when the previous year's news reports featured corporate accounting scandals and uncertainty about the war in Iraq. Timothy Graeff, director of the university's Office of Consumer Research, noted in the report that high gasoline prices are affecting local consumers' mindset. "Even though the local economy is healthy, consumers . . . have become increasingly pessimistic about the current [and] future economy."

- In July, Volkswagen AG picked Chattanooga as the site for its new U.S. auto plant. The plant is expected to employ 2,000 workers and have the capacity to produce 150,000 cars a year when it begins production in 2011. University of Tennessee economist Bill Fox said spinoff jobs in Tennessee and neighboring corners of Georgia and Alabama could total more than 10,000.

This information was compiled by Shalini Patel, an economic analyst at the Atlanta Fed.

Illustrations by Jay Rogers

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Research Notes and News

Research Notes and News highlights recently published research as well as other news from the Federal Reserve Bank of Atlanta.

Fed chief discusses reducing systemic risk

Federal Reserve Chairman Ben Bernanke recently laid out two broad strategies for reducing risk in the nation's financial system: strengthening the financial infrastructure and adopting a broader approach to financial supervision and regulation.

Although the financial market turmoil that began in 2007 is not over, the nation must explore how to bolster the system to make such bouts of instability rarer and less severe, Bernanke said during an August speech at the Federal Reserve Bank of Kansas City's Annual Economic Symposium in Jackson Hole, Wyo.

The Federal Reserve is collaborating with the private sector and other regulators to strengthen the financial infrastructure, he said. For example, the New York Fed is leading a public-private initiative to improve arrangements for clearing and settling trades in credit default swaps and other over-the-counter derivatives.

Bernanke also discussed the notion of a broader approach to supervising and regulating financial institutions. But he cautioned that such reforms must be carried out carefully. "The adoption of a regulatory and supervisory approach with a heavier macroprudential focus has a strong rationale, but we should be careful about overpromising, as we are still rather far from having the capacity to implement such an approach in a thoroughgoing way," he said.

Atlanta Fed research director introduces economics blog

Research staff at the Federal Reserve Bank of Atlanta are now producing macroblog, an economics blog that appears on the Atlanta Fed's Web site.

The blog offers commentary and observations on economic topics of the day, including monetary policy, macroeconomic developments, financial issues, and Southeastern economic trends. Posts so far, for example, have addressed what employment statistics say about the economy's health, the gross domestic product deflator, the complexities of measuring inflation, and the results of the federal government's economic stimulus package.

David Altig, senior vice president and director of research at the Atlanta Fed, originally launched macroblog in 2004 while he was an adjunct professor of economics in the graduate business school at the University of Chicago. He suspended the blog in August 2007, when he began his responsibilities at the Atlanta Fed.

Altig made the first post to the Atlanta Fed's macroblog on Aug. 12, 2008. New posts appear on Tuesdays and Thursdays. Postings made during the week before and the week of Federal Open Market Committee meetings do not comment on monetary policy.

Users may subscribe to macroblog via RSS feeds and e-mail.

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FEDERAL RESERVE BANK of ATLANTA
Economic Research

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Southeastern Economic Indicators

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		Alabama	Florida	Georgia	Louisiana	Mississippi	Tennessee	6th District	U.S.
Total payroll employment (thousands)[a]	**2008Q2**	**2,011.9**	**7,967.2**	**4,159.7**	**1,944.5**	**1,156.6**	**2,784.7**	**20,024.7**	**137,715.7**
Percent change from	2008Q1	–0.2	–0.8	–0.5	0.3	0.1	–0.4	–0.5	–0.1
Percent change from	2007Q2	0.4	–1.0	0.4	1.7	0.5	–0.3	–0.1	0.2
Manufacturing payroll employment (thousands)[b]	**2008Q2**	**290.8**	**368.9**	**417.9**	**157.6**	**165.0**	**371.7**	**1,771.9**	**13,580.0**
Percent change from	2008Q1	–0.5	–1.6	–1.3	–0.1	–0.8	–0.3	–0.9	–0.1
Percent change from	2007Q2	–2.1	–6.2	–3.6	–0.2	–3.6	–2.4	–3.4	–2.5
Civilian unemployment rate[a]	**2008Q2**	**4.5**	**5.4**	**5.5**	**4.0**	**6.6**	**6.1**	**5.4**	**5.3**
Rate as of	2008Q1	3.9	4.7	5.1	4.1	6.0	5.2	4.8	4.9
Rate as of	2007Q2	3.5	3.9	4.4	3.9	6.3	4.6	4.2	4.5
Existing single-family home sales (thousands of units)[c]	**2008Q2**	**90.0**	**270.8**	**175.2**	**65.6**	**53.2**	**126.8**	**781.6**	**4,913.0**
Percent change from	2008Q1	–8.5	10.1	–7.0	–1.2	–3.6	–5.4	–0.9	–0.8
Percent change from	2007Q2	–27.2	–13.2	–21.4	–17.6	–13.6	–12.7	–17.3	–16.3
Single-family building permits YTD (units)[b]	**2008Q2**	**6,949**	**22,974**	**15,579**	**6,947**	**4,280**	**9,423**	**66,152**	**332,296**

Percent change from	2007Q2	–35.4	–47.6	–52.2	–20.5	–33.6	–43.6	–44.5	–41.0
Personal income ($ billions)[c]	**2008Q1**	**154.2**	**716.7**	**325.2**	**152.1**	**85.4**	**212.0**	**1,645.6**	**12,002.1**
Percent change from	2007Q4	0.8	1.1	1.2	–0.6	–0.3	0.6	0.8	1.1
Percent change from	2007Q1	4.7	4.0	3.8	7.0	5.1	4.9	4.5	4.8

		Atlanta	Birmingham	Jacksonville	Miami	Nashville	New Orleans	Orlando	Tampa
Total payroll employment (thousands)[b]	**2008Q2**	**2,473.3**	**533.4**	**631.3**	**2,419.7**	**766.1**	**527.2**	**1,104.2**	**1,289.1**
Percent change from	2007Q2	1.0	0.0	–0.5	–0.7	1.1	1.9	0.2	–1.5
Civilian unemployment rate[b]	**2008Q2**	**5.4**	**3.8**	**5.1**	**5.0**	**5.1**	**3.6**	**4.9**	**5.5**
Rate as of	2007Q2	4.1	2.9	3.7	3.6	3.6	3.6	3.6	3.8
Office vacancy rate[b]	**2008Q2**	**18.7**	**—**	**16.0**	**9.2**	**11.0**	**—**	**12.0**	**15.0**
Rate as of	2007Q2	18.3	—	14.3	7.2	10.8	—	9.0	12.3
Median existing home sale price (thousands of $U.S.)[b]	**2008Q2**	**158.3**	**163.5**	**186.8**	**310.1**	**—**	**162.9**	**223.5**	**180.8**
Median price as of	2007Q2	175.5	164.9	198.7	384.4	—	166.0	265.1	222.7

[a]Seasonally adjusted data

[b] Not seasonally adjusted

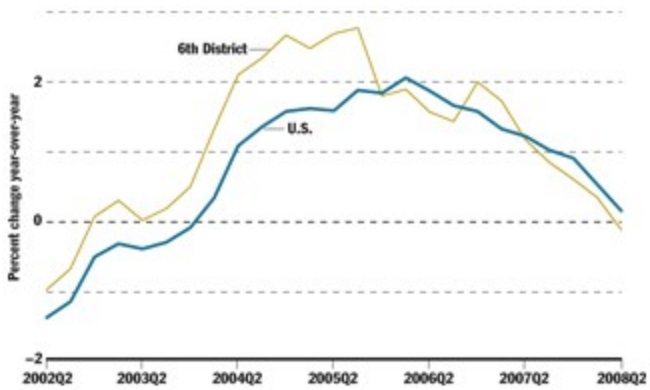
[c] Seasonally adjusted annual rate

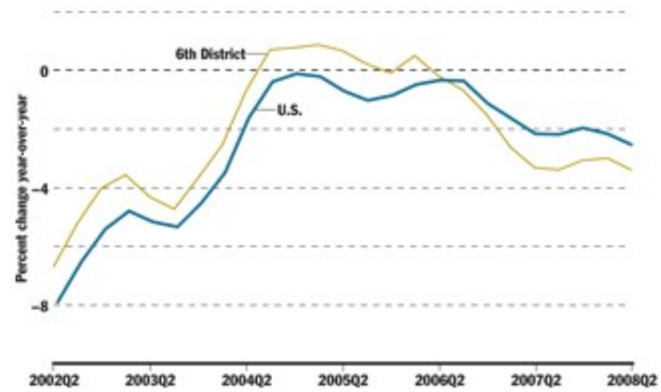
Sources: Payroll employment and civilian unemployment rate: U.S. Department of Labor, Bureau of Labor Statistics. Existing home sales and median existing home sale price: National Association of Realtors. Single-family building permits: U.S. Bureau of the Census, Construction Statistics Division. Personal income: Bureau of Economic Analysis. Quarterly estimates of all construction data reflect annual benchmark revisions. Office vacancy rate: CB Richard Ellis. Most data were obtained from Economy.com and are subject to revision by the data-gathering agencies.

For more extensive information on the data series shown here, see historical data.

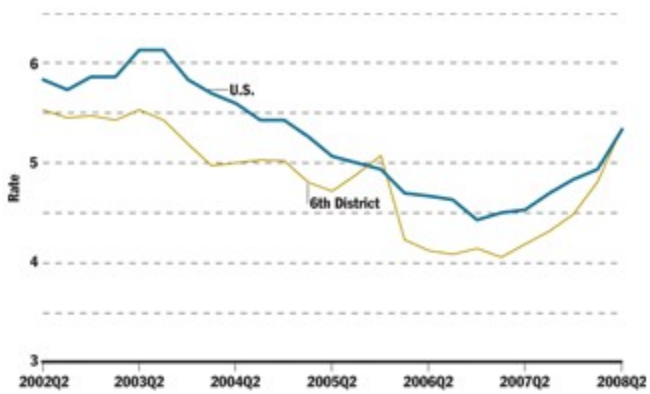
Total Payroll Employment

Manufacturing Payroll Employment

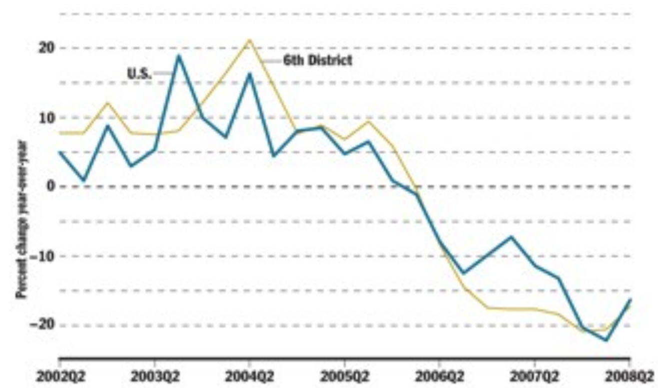




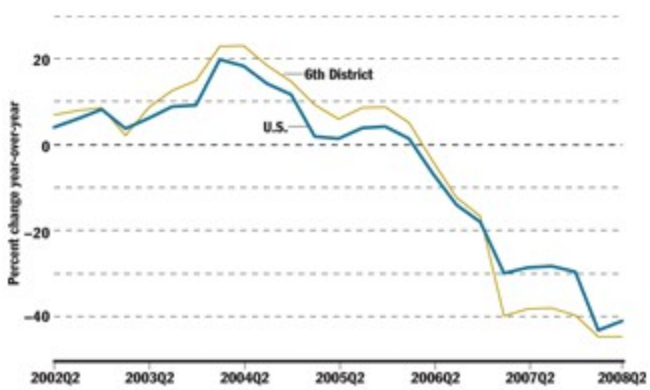
Civilian Unemployment Rate



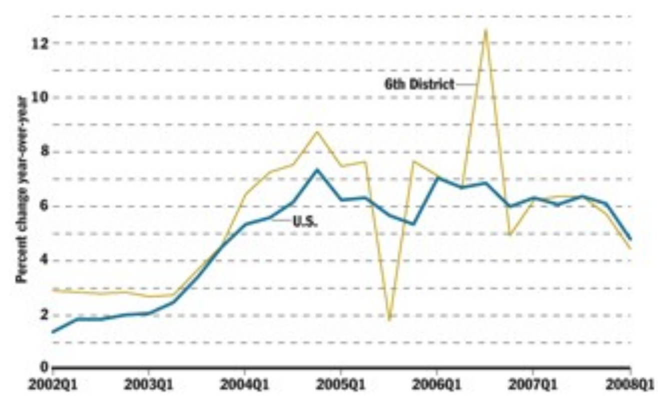
Existing Home Sales



Single-Family Building Permits YTD



Personal Income



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Editor's note: Throughout this issue, *Southeast* refers to the six states that, in whole or in part, make up the Sixth Federal Reserve District: Alabama, Florida, Georgia, Louisiana, Mississippi, and Tennessee.

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Back Ground

Photo courtesy of the Library of Congress photo archives

This Louisiana petroleum refinery, shown in 1944, used a chemical process called "cracking" to produce fuel for military equipment during World War II. Developed in the late nineteenth century, cracking became widely used in wartime to increase Allied gasoline production.