FEDERAL RESERVE BANK of ATLANTA

Economic Research

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DEPARTMENTS

On the Bubble: When Real Estate's Long Haul Took a Shortcut

While home prices kept appreciating handsomely, homeowners thought they were on a surefire path to personal wealth. The market swoon brought a sobering realization: What goes up can come down.

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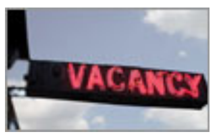

Vacancy Signs Dot Lodging Landscape

Hoteliers are leaving the lights on for travelers, but they're not showing up. The recession has had a big impact on the lodging industry in the Southeast especially, leading to price cuts and other efforts geared toward attracting corporate and individual guests.

Sports Still Draw Fans Despite Recession

Shaking off the effects of the recession like a rusher shaking off tacklers, many teams at the professional and collegiate levels are weathering the economic downturn well. Smaller teams, though, are finding the challenge daunting.

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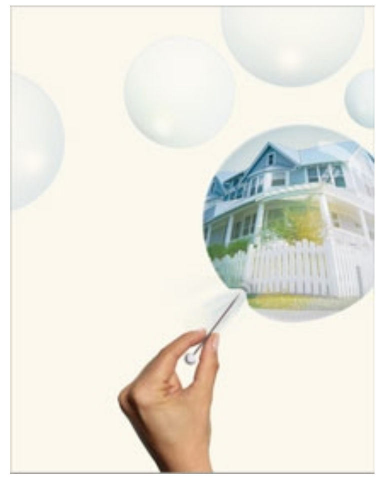
On the Bubble: When Real Estate's Long Haul Took a Shortcut

A home is often a person's biggest investment. But as home prices began their dramatic appreciation, the stage was set for the once-solid investment strategy to show cracks in the foundation.



When housing prices began to fall after the housing bubble burst in 2006, the drop represented more than a loss of wealth to a wide swath of Americans. It was a contradiction of what homeowners assumed was a universal truth: that home ownership was always a good investment. That assumption seemingly had been in place since the passage of the Home Owners Loan Act of 1933, which paved the way for long-term amortized mortgages.

But beginning in 2006, home values began to take an epic fall in many markets. The S&P;/Case-Shiller Home Price Index, which reflects home pricing trends by comparing repeat sales of single-family homes in 20 U.S. markets, offers one compelling illustration. In the first 78 quarters tracked by the index created in 1987 by economists Karl Case, Robert Shiller, and Allan Weiss, only 13 quarters (16.6 percent) showed negative growth.

Beginning in the third quarter of 2006, the next 13 quarters all ranked among the lowest 15 quarters in the history of the index. Prior to this span, the index's biggest quarter-to-quarter decrease had been a modest 1.6 percent. That decline was dwarfed by the post-bubble stretch from the fourth quarter of 2007 to the first quarter of 2009, which featured decreases ranging between 5.5 percent and 11.2 percent quarter over quarter. Price declines continued without interruption until the second quarter of 2009, when the Case-Shiller index posted a 3.7 percent increase.

Long-held assumptions rocked

While the stock market and other investments have had highs and lows in the past eight decades, investment in single-family homes generally grew along with their price appreciation. Although some housing bubbles have occurred in the past, none has had the same adverse impact on average home values nationwide as the bursting of this one. Further, the severity of price declines has varied regionally, making it challenging for homeowners to assess the investment performance of their own homes and leaving them searching for an explanation of this investment's sudden fluctuation.

Related Links

On this site:

Indexing the Housing Market podcast
(MP3 14:57)
Karl Case, an economics professor at Wellesley College and codeveloper of the S&P;/Case-Shiller Home Price Index, discusses house prices and the state of the housing market.

On the Web:

Case-Shiller Home Price Indexes

U.S. Census Bureau's housing information

Federal Housing Finance Agency

"It's a complicated story," said John S. Adams, author and professor emeritus of geography at the University of Minnesota. "It doesn't make for very good headlines to say that we've got over 300 metro areas in this country, and each one is a separate housing market. When you say that, the audience's eyes start to glaze over because what they really want you to tell them is where to invest money to make a quick buck."

That sort of analysis, filled with nuances and exceptions, runs counter to the common wisdom that Americans could count on their homes for making a buck, even if it wasn't always a quick one.

"People have viewed their house as investments for a very long time. That's part of the mantra of why people own houses," said Kelley Pace, professor of finance and director of Louisiana State University's Real

Estate Research Institute. "The difference between now and then is that then houses were long-term investments. They were illiquid. There was really not much people could do with that investment. That was going to be something that was going to help them out later in life, typically."

When renters became owners

In 1920, according to the U.S. Census Bureau, 46 percent of American households were renters. However, a number of factors, both political and economic, eventually transformed the landscape of home ownership in America.

In 1922, future president Herbert Hoover, then serving as President Harding's secretary of commerce, implemented the "Own Your Own Home" program, which encouraged builders to increase residential construction and called for new banking rules allowing nationally chartered banks to increase lending for residential properties.

Although some housing bubbles have occurred in the past, none has had the same adverse impact on average home values nationwide as the bursting of this one.

In addition to passing the Home Owners Loan Act in 1933, Congress created additional institutions during the 1930s to promote home ownership: the Federal Home Loan Bank system to provide a stable source of funds for banks; the Federal Housing Administration (FHA) to insure mortgages; the Federal National Mortgage Association (Fannie Mae) to buy the insured mortgages; and the Federal Savings and Loan Insurance Corp.

Meanwhile, a surplus of savings Americans accumulated during World War II, and assistance from the GI Bill for soldiers returning home, launched a housing boom in the late 1940s that saw the homeownership rate in America rise to 55 percent by 1950, according to the U.S. Census Bureau. That percentage has steadily inched upward, reaching 69 percent in 2005 before receding slightly.

A place to call home—and invest

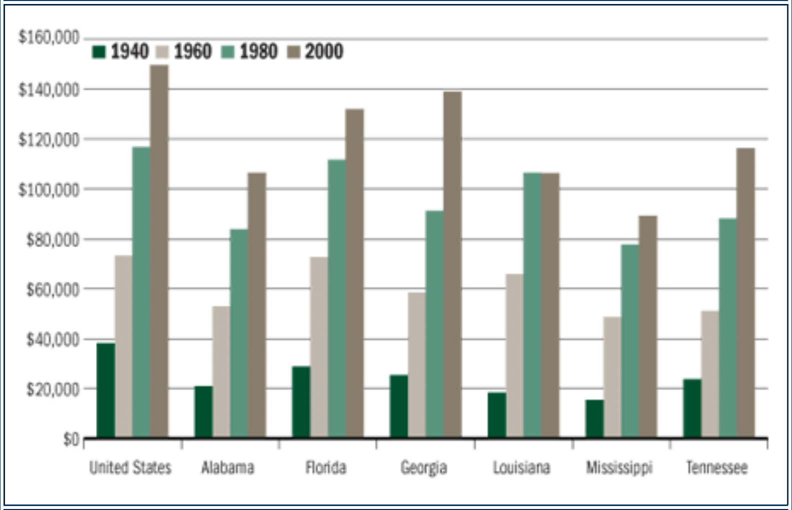
During that period of expanding home ownership, the appreciation of home values along with tax incentives made housing an attractive investment for many Americans. In some cases, it wasn't just the best option; it was one of few options because investment opportunities were not as plentiful as today.

"Nowadays, mutual funds are easy to get into," said James Kau, chair of the University of Georgia's Department of Real Estate and cofounder and coeditor of the *Journal of Real Estate Finance and Economics*. "When I was young, they didn't even exist. It was difficult to get into alternative investments. You had to do things like find a stockbroker. Now there are retirement plans, and a lot of people have both stocks and housing. Housing has been the consumer durable that most people take advantage of. In many cases, it's because of taxes."

While many homeowners may not be aware of the annual appreciation of their homes in dollar terms, filling out an Internal Revenue Service 1040 long form is an annual reminder of a home's tax benefits. Through the years, Americans have been able to take advantage of a variety of tax benefits from home ownership, including mortgage interest deductions, property tax deductions, and an exemption for homeowners over 55.

In addition, when homeowners have examined the change in home value, they liked what they saw. According to U.S. Census Bureau data converted into 2009 dollars, the inflation-adjusted median U.S. home price grew from $30,600 in 1940 to $58,600 in 1960, $93,400 in 1980, and $119,600 in 2000. The median home values in the Southeast are generally below the national average, but all states have seen increases, with Florida and Georgia having the region's highest median prices (see the chart). For decades, Florida's median home price led the region, starting at $28,889 in 1940 and rising to $131,937 by 2000. Georgia, which had a median home price of $25,512 in 1940, surpassed Florida in 2000 with a median value of $139,065. At the other end of the spectrum, Mississippi's median value of $15,507 in 1940 had jumped to $89,292 by 2000.

Chart 1
Median Home Values in the Southeast, 1940–2000



Note: Figures represent 2009 dollars.
Source: U.S. Census Bureau

While these increases in value hold obvious appeal to homeowners, Adams said hidden costs offset some of the asset's appreciation and disguise a home's true value as an investment.

"All the analysis I've seen shows that housing as an investment, if you hang on to it long enough, is not much different from other kinds of investments of a reasonable sort," said Adams, who did extensive research in the field for his book *Housing America in the 1980s*. "I bought a house in 1973 that I paid $53,000 for. It's now assessed at something like $600,000. I've done the math and know how much I've put into the house in remodeling. You might say 'Wow, isn't that great?' But you need to look at what it's worth today minus the present value of the money that was put into the house. If you compare that in compound interest rates from 1973 to the present, it's appreciated about 4 to 4.5 percent." He added that if a homeowner is not investing 2 percent of the value of a home annually into its maintenance, it's losing value to deterioration. (See the interview with Adams.)

A tale of two spikes

The housing bubble earlier this decade was not the first. Industry watchers remember well the biggest home price spike of the last half of the 20th century.

"One of the big parties in real estate was in the late '70s," Pace said. "Now we've had another big party lately. But these parties occurred for very different reasons. The '70s bubble was financially induced partly by the combination of inflation and taxes. The latest one was induced largely on the finance end by relatively easy money with no standards, comparatively."

Although spurred by different forces, the run-up in prices across the two bubbles was historically significant. According to data from the National Association of Realtors, the median price for existing housing jumped from $35,300 in 1975 to $62,200 in 1980, a 76 percent increase. The latest bubble saw median prices for existing homes jump from $139,000 in 2000 to $185,000 in 2004, a 33 percent increase.

"Back in those days, real estate was the best choice," Pace said. "In the '70s, there was no other place to go the way the taxes worked. Any gains you had were taxed at 50 percent. If I made 17 percent on a money market, I got 8.5 percent back after I paid my taxes. If you factor inflation at 10 percent, now I'm 1.5 percent worse off after tax and inflation."

Other than historic price appreciation, Pace said the most recent housing bubble had its own character.

"Until relatively recently, the transaction costs for flipping a house were very high," Pace said. "In other words, it wasn't that long ago that the closing costs were very expensive. Title insurance was more expensive. All sorts of things were more expensive, and that was a big drag to making a short-term investment.

"Another aspect was that you historically could not borrow easily as much money on a house," he added. "The lowering of transaction costs allowed you to use your home as an ATM."

The relaxation of standards and decreased transaction costs swelled the number of potential buyers in the housing market, driving demand and prices upward. But while home values rose, many owners didn't want to defer the rewards from their appreciating asset. Data from the Federal Housing Finance Agency (FHFA) dramatize a shift in the philosophy of home buyers. Beginning in 1991, when the FHFA began tracking the nature of refinanced mortgages, the percentage of home owners withdrawing equity was 10 percent or less in half of the first 18 quarters. Since the first quarter of 2001, between 30 and 49 percent of homeowners have pulled out equity each quarter. Eleven of those quarters show withdrawal rates higher than 40 percent.

Homeownership had become more than merely a long-term investment for many Americans.

Homeownership in the future

Certainly, homeowners were encouraged when the Case-Shiller index showed a net increase in home values for the second quarter of 2009. It was the first such increase since the second quarter of 2006.

The big question going forward is whether the housing market's first "green shoot" in some time will take root. At least one industry observer thinks Americans' relationship with homeownership will undergo change.

"Backing up from all of this, I expect fully that we're going to be hunkering down and building fewer houses," Adams observed. "We're going to be occupying housing more intensely, and the value of housing is going to take a hit all across the country, especially in what were the nation's fast-growing areas, simply because of the costs for maintenance and borrowing money."

Pace foresees change as well but is somewhat hopeful of what change might bring. "We'll be in a reactionary, conservative phase for a little while," he said. "But we'll be back in equilibrium before too long as the population increases. I'm not expecting a reversion back to smaller houses up next to each other as some are forecasting. It may go another direction for a while, but it will probably settle down to something that's appropriate relative to our income, which would be a new house in the 2,000 square foot range. I don't anticipate the death of the suburbs or any of these other kinds of things that some people throw out."

Whatever changes homeownership undergoes, it seems probable that more Americans will regard their home primarily as their domicile rather than an investment that comes with a roof over their heads.

This article was written by Ed English, a staff writer for EconSouth.

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Vacancy Signs Dot Lodging Landscape

The effects of the recession have finally caught up with the U.S. lodging industry. Leisure and business travel have fallen off as consumers and businesses tighten their purse strings. Hoteliers are trying to find creative ways to draw in customers and are waiting for a turn in the economic tide to bring travelers flooding back.

Without a doubt, the lodging industry has seen better days. The unfortunate mix of weak demand and strong supply growth has resulted in what Atlanta-based PKF Hospitality Research describes as one of the worst years on record for the industry. According to Smith Travel Research, a lodging industry research firm, three key industry performance measures declined sharply: from July 2008 through July 2009, occupancy rates fell 10.3 percent, average daily rates fell 8.8 percent (to $98.41), and average room revenue (referred to in the industry as revenue per available room, or RevPAR) fell 18.2 percent (from $67.40 to $55.12).

Troubling signs for the industry first appeared last summer, when occupancy rates sank to 68 percent, a 4 percent dip from 2007, according to Standard & Poor's. For much of 2008, an influx of international travelers, drawn by a weak dollar and the relative strength of other economies, helped offset the lull in domestic travel. According to the U.S. Commerce Department's Office of Travel and Tourism Industries, overseas arrivals to the United States (including those from Mexico and Canada) topped 25 million in 2008, up 6 percent from 2007. But the flood of international visitors to the United States slowed to a trickle after the financial crisis in the fall of 2008, and the number of foreign visitors is expected to drop 9 percent for 2009, according to the U.S. Travel Association.

Consumers curtail travel plans

Job losses and job insecurity, declining household wealth, and tight credit have curbed consumer spending. Not surprisingly, people are taking fewer and shorter vacations. Data from the U.S. Bureau of Economic Analysis indicates real spending on travel and tourism fell at a 5.9 percent annual rate in the first quarter of this year following a 6.9 percent drop in the previous quarter. A survey conducted for CareerBuilder.com highlights Americans' travel apprehensions: 35 percent of those surveyed were not planning to take a vacation in 2009; 71 percent cited finances as the reason, while roughly one in five were worried about losing their jobs or felt guilty for being away from the office.

Related Links

On the Web:

American Hotel and Lodging Association

Hotel News Now

Article on forecast for lodging industry

Lodging magazine

But leisure demand may be starting to rebound, according to Peter Yesawich, CEO of Ypartnership. In a July 2009 survey by the market research firm, 63 percent of respondents planned to take an overnight trip in the next six months, up from 61 percent a year ago. But even though people are keeping their vacation plans, the hitch is that travelers are downgrading their accommodations and shortening their stays.

Business travel—the sweet spot goes sour

Like leisure travel, corporate travel has fallen off, causing even more pain for the lodging industry. Isaac Collazo, a vice president at InterContinental Hotels Group (IHG), based in Atlanta, calls business travel "the sweet spot in the hotel industry." Individual business travelers and corporate groups are traditionally a reliable source of revenue for hoteliers because they tend to pay premium room rates. But the tough economy has forced many companies to cut their travel budgets. Collazo says that the absence of business travelers has been especially noticeable for conventions and meetings. In fact, a survey conducted by

Ypartnership found that meeting planners expected their budgets for 2009 to shrink by an average of 23 percent, with the economy being the primary reason for the decline.

Corporate cost cutting for group business travel has been aggravated by what is being called the "AIG effect." Following the public backlash against some companies receiving taxpayer funds, many businesses are wary of attracting negative media attention for hosting corporate events that might be perceived as overly lavish. Group meetings, if not entirely forgone, are being scaled back. A recent survey of Association of Corporate Travel Executives members found that 60 percent were avoiding leisure or resort destinations, even if the less luxurious accommodations were more expensive. As a result, these resort properties have experienced sharp declines in revenue.

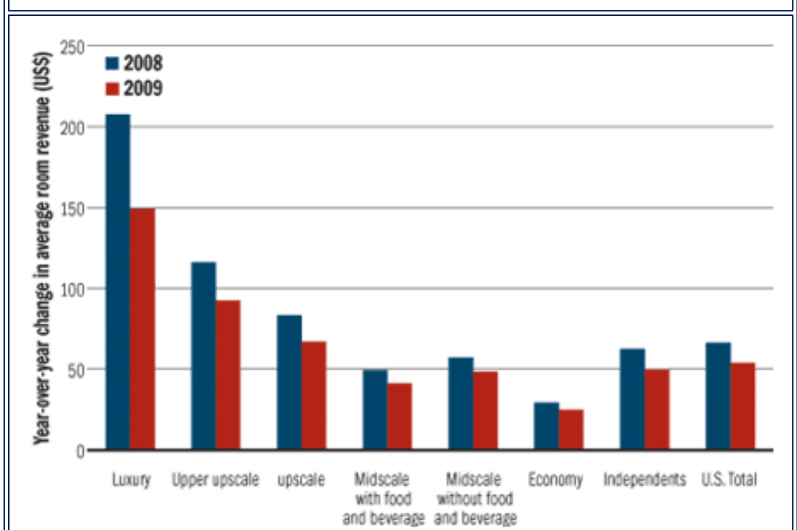
Growing pains

Further complicating matters for the battered lodging industry is the influx of new hotels coming online in 2009, the fruits of a three-year building boom. Charlotte Kang, vice president at PKF Consulting, notes that the current lodging slump differs from previous ones, especially in terms of the balance between supply and demand. In the past, she explains, "supply growth typically decreased when demand growth started to decline." Conversely, "demand growth began to contract in the first quarter of 2008, but supply growth was accelerating."

This increase in supply, combined with feeble demand, erodes hoteliers' pricing power. Smith Travel Research forecasts a 3 percent increase in supply this year and a 1.4 percent rise in 2010. Meanwhile, quarterly demand is expected to decline 5.5 percent in 2009.

Hoteliers are doing what they can to motivate consumers, including aggressively reducing room rates. Luxury chains are making the biggest cuts; Smith Travel Research's June report showed a 28.6 percent drop in these chains' average room revenue from a year earlier compared with a nearly 10 percent decline industrywide (see chart 1). In addition to cheaper rates, to help stimulate demand several hotel chains are offering incentives such as free additional nights and complimentary spa services.

Chart 1
A Measure of Hotel Chains' Performance, June 2008 versus June 2009



Source: Smith Travel Research

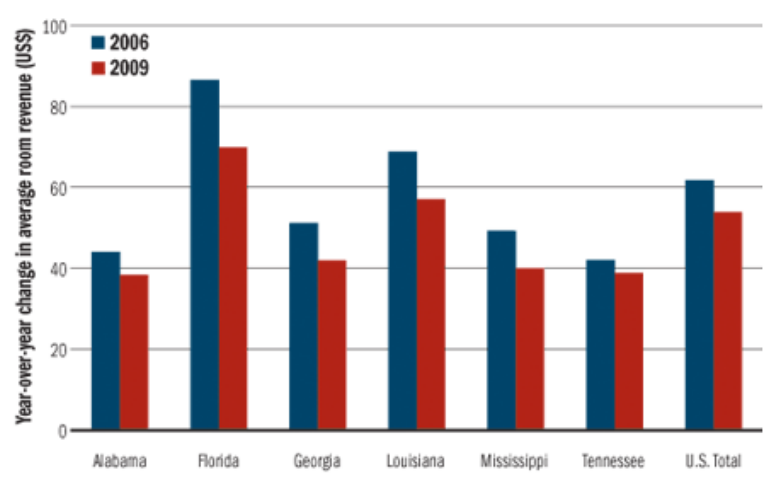
Most industry experts agree, though, that rate cuts do more harm than good. Walter Banks, owner and president of Lago Mar Resort and Club and a director of the Atlanta Fed's Miami Branch, explains that lowering rates "creates a downward spiral, reducing dramatically the net profit for hotels." Jan Freitag, vice president at Smith Travel Research, agrees and considers rate cuts "a little bit suicidal." He reasons that certain groups of people will always travel regardless of the price. So hotel rate cuts are, in effect, "subsidizing inelastic demand."

Freitag says the double-digit declines in room rates are hurting hotels on two fronts. First, lower rates squeeze profit margins in the short term. And in the longer term, once the economy rebounds, it becomes difficult to raise rates. This difficulty stems in part from the fact that group meeting planners have a longer booking window. Thus, today's lower prices are being used as a starting point for negotiating future rates.

Problems paying the piper

The negative trends afflicting the industry are also miring more hotels in loan defaults, foreclosures, and bankruptcies. A number of the distressed properties are located in the Southeast, including the Sheraton Downtown Orlando and the Coconut Grove Hotel in Miami. Declines in occupancy and revenues mean owners have less money to meet their debt service. PKF Hospitality Research predicts that in 2009 about 36 percent of full-service U.S. hotels will not have enough cash flow to pay their monthly mortgages compared with 21 percent last year. The credit crunch has kept potential buyers on the sidelines, leaving many troubled hotel owners with no other option but to default. University of California economist Kenneth Rosen predicts that as many as one in five U.S. hotel loans may go into default through 2010.

Chart 2
A Measure of Southeastern Hotels' Performance, June 2006 versus June 2009



Source: Smith Travel Research

Moreover, the fact that many commercial mortgages were securitized has complicated hoteliers' efforts to renegotiate the terms of their loans, and, until recently, laws governing commercial mortgage-backed securities prevented owners from restructuring their loan until they became delinquent. The IRS has since issued new rules giving servicers more flexibility to negotiate with borrowers on loans that are still current. But some hotel owners are using defaults as a tactic to force lenders to renegotiate their terms, according to CNNMoney.com.

One upside is that many distressed properties will be sold at prices low enough for the new owners to operate profitably. Kang of PKF Consulting observes that "investors who have the financial ability to take advantage of the market conditions can expect very attractive prices and realize spectacular returns when the market turns around."

Lodging's doldrums are a drag on local economies

Data from the U.S. Bureau of Labor Statistics indicate that hotels and other accommodations employed 1.7 million people in the United States as of June 2009. But because a large portion of hotels' expenses are fixed, reduced revenues have forced hotel operators to cut jobs in order to reduce costs. From the onset of the recession through July 2009, the lodging industry has lost a net total of 170,800 jobs nationally. Unemployment in the industry, at 10.9 percent in June 2009, is higher than the 9.4 percent national unemployment rate.

Predictably, lodging's weakness has adversely affected the economy in the Southeast, where hotels and other accommodations have a strong presence. For example, Atlanta is the regional headquarters for Intercontinental Hotels Group, which includes brands such as Crowne Plaza and Holiday Inn. The lodging industry makes significant contributions to the local economy in terms of jobs, tax revenues, and sales for other businesses, such as transportation, entertainment, restaurants, and retailers. In 2008, hotels, resorts, and other lodging properties were projected to generate $13.8 billion in tax revenues for the Southeast's state and local governments, according to the American Hotel and Lodging Educational Foundation.

Ypartnership's Yesawich also points to the region's draw as a resort destination, especially Florida and the coastal areas of Georgia. Properties there are among the hardest hit. Chart 2 shows the impact of declining travel on the region's lodging industry. Florida, which relies heavily on tourism, has seen a 19 percent drop in average room revenues in the past three years compared to a 13 percent decline nationwide.

A light at the end of the tunnel?

According to research by PKF, as much as 70 to 80 percent of hotel performance is linked to the local economy, so conditions in the industry are unlikely to improve until there are clear signs that a sustainable economic recovery is under way. Kang notes that "the lodging industry will recover when the economy improves to the extent that companies start hiring, unemployment rates begin falling, and people have jobs, can keep their homes and start spending." In the meantime, hoteliers like Banks are pinning their hopes on pent-up demand.

As the economy begins to recover, the industry can expect to see a new balance that is more favorable toward hotel operators, Freitag observes. The Atlanta Fed's outlook for the U.S. economy is for a recovery to begin in the second half of 2009. PKF Hospitality Research forecasts that the lodging industry will resume sustained growth starting in 2011. But the pace and timing of the recovery will vary from market to market, so some locations could begin to improve as early as 2010.

Despite the down times being visited upon the lodging industry, analysts see some silver linings. IHG's Collazo asserts that, despite the current challenges, lodging is still a vibrant industry. For the remainder of 2009, the industry's decline should abate, and supply growth should slow down during the rest of 2009 and 2010. PKF Consulting's Kang stresses that although she does not envision the industry's performance turning positive until 2011, the industry appears to be on the road to recovery.

This article was written by Lela Pratte, a strategic information research analyst in the Atlanta Fed's Public Affairs Department.

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FEATURES

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Sports Still Draw Fans Despite Recession

In sports, nothing succeeds like success. Buoyed by fan loyalty, teams at larger colleges and pro levels have mostly thrived despite the challenging economic climate. Smaller teams, though, are feeling the brunt of the down economy.

College football in the South has often been compared to a religion, even by scholars. Like an icon, your favorite team's logo can be stamped on everything from a cap to a casket.

Not surprisingly, Southerners put their money where their passion is. Five of the top 10 revenue producers in college football in the 2007–08 academic year were Southeastern schools: Georgia, Florida, Auburn, Alabama, and LSU, which brought in a combined $303 million, according to Street & Smith's *SportsBusiness Journal*. In spite of the recession, all indications are that these teams and their rivals will continue to rake in dollars from ticket sales and lucrative television contracts.

Sports as an industry, especially the most high-profile leagues and franchises, is weathering the downturn comparatively well. Even as unemployment has risen dramatically—more than tripling in Florida, for instance, from July 2006 to July 2009—many people are still spending at least some money on sports.

"Certainly they've felt an impact, but fans are addicted to sports, if you want to think about it that way," said J.C. Bradbury, an economist and associate professor of health, physical education, and sports sciences at Kennesaw State University near Atlanta. "Once you gain a taste for it, you want to see an event, and it's a relatively cheap thing to do." Eric Bain-Selbo, head of the Department of Philosophy and Religion at Western Kentucky University wrote in a 2008 paper: "As sport around the country continues to become a communal and emotional fixture in people's lives—as it has with so many college football fans in the South—it increasingly is becoming the new opiate of the masses."

Related Links

On the Web:

Street & Smith's *SportsBusiness Journal*

Forbes report on the business of baseball

Article on sports-related subsidies

International Speedway Corp. filings with the U.S. Securities and Exchange Commission

While some might consider that view extreme, the rabid devotion of fans surely helps explain why the television networks ESPN and CBS, amid a severe recession, earlier this year agreed to pay the Southeastern Conference (SEC)—home to the five schools listed above and seven others—$3 billion to broadcast mainly football games over the next 15 years.

But the recession has brought some signs of economic strain to the world of sports. In a February poll of 1,100 sports industry executives by Turnkey Sports & Entertainment and Street & Smith's *SportsBusiness Journal*, a third said their companies had laid off staff, while 2 percent said they had closed offices. Several minor league professional teams in the Southeast have folded.

Attendance at NASCAR races and Major League Baseball (MLB) games, including those of the Atlanta Braves, is down. Even football ticket sales are down a small amount for a few pro teams and some major colleges in the region. The Jacksonville, Fla.-based PGA Tour's overall prize money could decline this year for the first time since 1975, according to news reports.

Gap widens between college haves and have-nots

Economic tremors have been felt on college campuses as well. Traditional Southeastern powerhouse programs, including Tennessee, Auburn, and Florida State, have experienced small declines in 2009 season ticket sales, according to various news reports. Georgia Tech's athletic program laid off a few employees.

The defending national collegiate football champion Florida Gators sold out of 2009 season tickets. Yet even that organization's bottom line has been affected. Athletic director Jeremy Foley told the Miami Herald in June that the expected windfall from national championship–related licensed products —shirts, hats, jackets, etc.—has not equaled sales of similar items after Florida's 2006 championship. Also, the school, according to the *Orlando Sentinel*, did not increase 2009 football ticket prices "to reward fans during these economic times."

Small schools have been much harder hit. In Louisiana, several smaller college athletic departments have made severe budget cuts and eliminated sports such as tennis. The University of New Orleans even warned that it might drop athletics altogether before local donors came to the rescue.

Pain for the little guys

More or less the same phenomenon is playing out in the sports landscape at large. Even though organizations such as the SEC, MLB, and the National Football League (NFL) have taken their share of economic blows, their survival is hardly threatened. But the situation is different for less-established leagues and teams.

"The marginal leagues just get decimated in these times," Bradbury said.

The 22-year-old Arena Football League, which had teams playing indoor football on a shrunken field in New Orleans, Atlanta, Tampa Bay, and Orlando, among other cities, folded in August 2009. A couple of minor league hockey teams in the Southeast—the Augusta, Ga., Lynx and the Pensacola, Fla., Ice Pilots—shut down in late 2008. The Lynx were the first team to close during a season in the 21-year history of the East Coast Hockey League, according to news coverage. Also, in November 2008 the Atlanta Silverbacks men's United Soccer League team became the city's second professional soccer team to shut down since the Beat, a Women's Professional Soccer (WPS) team, folded in 2003 (although the WPS expects the Beat to be playing again in 2010). The Silverbacks cited the economic downturn as a major reason for canceling the 2009 season. (The Silverbacks women's team was still active for its 2009 season, which ended in July.)

Signs of strain for the big guys

NASCAR is, of course, vastly more prominent than minor league hockey and professional soccer. Nevertheless, the stock car racing league—whose popularity soared in the few years before the recession when the economy was generally strong—is facing tough economic times. High gas prices, rising unemployment, and economic uncertainty have caused racing fans and the automotive-industry sponsors, which are central to the sport, to cut spending.

Daytona Beach, Fla.-based International Speedway Corp. (ISC) reflects NASCAR's troubles. The publicly traded company, which runs Daytona International Speedway and 12 other motorsports tracks, including the Talladega Superspeedway in Alabama and Homestead-Miami Speedway, reported in its Securities and Exchange Commission filings that its food, beverage, and merchandise revenue slid 34 percent, to $26.8 million, in the first half of 2009 from the same period in 2008. In the same period, the company's ticket sales revenue declined 16 percent, to $91.5 million. ISC posted a net loss of $31.7 million for the second quarter of 2009 compared with a net profit of $26 million a year earlier.

"We are sensitive to the economic challenges that many of our fans face, and to address this, beginning in 2009, we lowered prices on over 150,000 seats, or 15 percent of our grandstand capacity, for NASCAR Sprint Cup events across the Company," ISC said in its 2009 second quarterly report. Those challenges, the company noted, include credit availability, the decline in consumer confidence, the rise in unemployment, and increased fuel and food costs.

ISC also noted that securing corporate sponsorship arrangements is taking longer because companies have become cautious with their marketing dollars.

Stadiums full for kickoff

Pro football does not have as many worries as stock car racing. For some years, it has been the nation's most popular sport in terms of television viewership and opinion surveys, and that strength appears to be serving the NFL well during these lean times. Even though the league laid off employees at its New York headquarters, the teams in the Southeast are generally warding off glancing blows from the economic downturn.

As the September season openers got under way, among the six pro football clubs in the Southeast, only the Jacksonville Jaguars appeared to be having significant problems selling tickets, according to news reports. Jaguars owner Wayne Weaver told the *Florida Times-Union* that all eight home games would likely be blacked out on local television because of insufficient ticket sales. "I'm concerned," Weaver told the Jacksonville newspaper in August. "But you have to realize we're in an unusual economy that most of us have never gone through."

Weaver's Jaguars are not the only NFL team whose business has been at least trimmed by recession. The Tampa Bay Buccaneers, for the first time in nearly a decade, had no waiting list for 2009 season tickets. In response, the team designed several new ticket packages, such as half-season plans.

The Atlanta Falcons have not traditionally drawn as well as the Buccaneers, but season ticket sales increased 5 percent for the 2009 season, in part because of a much-improved team in 2008 and a popular new quarterback. The Falcons' and Buccaneers' division rival, the New Orleans Saints, sold out all their season tickets for the fourth straight season.

Farther north, Nashville's Tennessee Titans maintain a waiting list for season tickets. And the team will extend its streak of consecutive sellouts to 114 after this season's eight regular season and two exhibition games, said Marty Collins, the team's senior director of ticketing. The entire season sold out before the middle of August, according to the team's Web site. As of Aug. 13 on the Titans' NFL Ticket Exchange, an online after-market sales operation run by the teams, single tickets for the Oct. 11 Indianapolis Colts game ranged up to $910.

Even some clubs doing brisk business have, like the Buccaneers, created flexible payment plans and instituted other measures to accommodate customers. The Falcons, for example, introduced a six-month payment plan, and the Saints for the first time offered season ticket holders a layaway option.

Fewer fans at the old ball game

So far, the MLB appears to be weathering the recession comparatively well. Leaguewide revenue increased 5.5 percent to $5.8 billion in the 2008 season, which was less than the 9 percent growth the season before, according to Forbes magazine's annual special report, "The Business of Baseball." Revenue figures are expected to grow even less in 2009. MLB attendance through Aug. 10 was down by approximately 5.6 percent compared with the same time last year. Moreover, IEG, a sponsorship consulting and research firm, predicted at the start of the baseball season that sponsorship spending on MLB deals—including the league, teams, and stadiums—would decline 4.8 percent this year from $540 million in 2008 to $514 million.

In the Southeast, the Atlanta Braves' crowds were down through Aug. 10, but only by 3.4 percent. The region's other two big league teams, the Florida Marlins of Miami and Tampa Bay Rays, were drawing more fans through August than they did in 2008, though the Marlins' attendance was second-worst in the majors, and both clubs trailed the Braves' attendance substantially.

One reason MLB has been able to hold its own so far is baseball's embrace of technology to generate revenue, said Bradbury, who has written books on the economics of the sport. In particular, mlb.com has been highly successful—so successful, in fact, that in 2005 a proposed (but ultimately shelved) initial public offering of the online property could have fetched up to $3 billion, according to numerous media reports.

Build it and they will come—or will they?

How much do we love our sports? Even during a recession, a few Southeastern cities and states are channeling significant public funds into professional sports venues.

Public funding of sports facilities is hardly new. Such projects date back to the early 20th century. The 77-year-old Los Angeles Coliseum is an example. Back then, cities typically built horseshoe-shaped municipal arenas for multiple uses—parades, track meets, football and baseball games, rodeos, and festivals—according to Dennis Coates, an economist at the University of Maryland, Baltimore County, and Brad Humphreys, an economist at the University of Alberta.

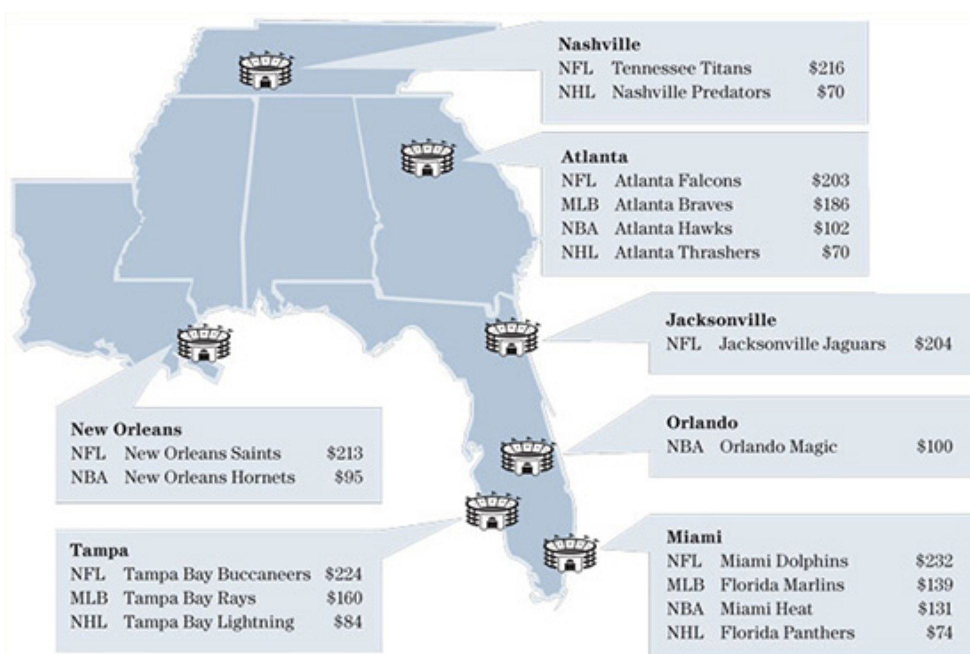
More recently, states and municipalities have built arenas for the exclusive use of one professional team. Often, governments pony up after a team threatens to leave the city or in order to lure either a team from another town or a brand-new team.

While the difficult economy and credit markets have postponed some projects, Bradbury said, public subsidies have flowed freely for sports arenas in the Southeast over the past dozen years. Louisiana's state government; Tampa; Miami; Montgomery and Mobile, Ala.; Floyd County, Ga.; Jacksonville; and Chattanooga and Sevierville, Tenn., have collectively dedicated billions of dollars to build stadiums and practice facilities in the past dozen years.

Even amid dire financial times for governments, some places in the Southeast, hoping to stimulate economic activity, continue to channel tax dollars into sports facilities. Gwinnett County in suburban Atlanta is financing a $64 million baseball park, which opened in April and helped bring the Atlanta Braves Triple-A farm team from Richmond, Va. County leaders expected to sell naming rights to help offset costs but have as yet been unable to do so.

Meanwhile, Miami-Dade County and the city of Miami this summer agreed to use hotel room taxes to finance the majority of a stadium for baseball's Marlins that will cost—after paying off bonds over 40 years—about $2.4 billion. Officials broke ground on the new ballpark in July.

Pro Sports Revenue in the South



Notes: Figures represent millions of dollars. Revenues for the NBA, NFL, and NHL are for the 2007–08 seasons; MLB, for the 2008 season.
Source: Forbes.com

That same month, Louisiana's state government finalized a deal to help keep the Saints in New Orleans through 2025. That arrangement includes spending $85 million in state funds to renovate the team's stadium, the Louisiana Superdome, and leasing space for state agencies in a New Orleans office building owned by Saints owner Tom Benson.

July was busy. That's also when the city of Birmingham began design work on a publicly funded domed stadium with no fixed tenant that, according to the city and news reports, will cost more than $550 million to build. The city council authorized spending $8 million a year to plan and design the building and at the same time voted to spend $7.5 million to restore Rickwood Field, a century-old baseball park, and to build a museum devoted to the city's baseball history.

Proponents of those projects cite potential economic benefits such as new jobs, spending, and neighborhood revitalization, along with the ability to host major events and the prestige that comes with a new venue and a big-league team. At the Birmingham groundbreaking, Mayor Larry Lankford said the city needs a "yes, we can" attitude.

Economists are not so sure. Studies by professional economists overwhelmingly suggest that such projects do not generate broad economic benefits, according to a 2008 paper by Coates and Humphreys. In a 2005 survey of American Economic Association members, 86 percent either said they strongly agree (58 percent) or agree (28 percent) that local and state governments should eliminate subsidies to professional sports franchises, Coates and Humphreys note.

They find that the results of nearly 20 years of research are "strikingly consistent. No matter what cities or geographical areas are examined, no matter what estimators are used, no matter what model specifications are used, and no matter what variables are used, articles published in peer reviewed economics journals contain almost no evidence that professional sports franchises and facilities have a measurable economic impact on the economy." Research shows that the impact is lessened because money spent in and around a stadium would otherwise have been spent elsewhere and on other activities.

Whatever the case, we still love our sports, and based on recent experience it appears we'll continue spending money on them even during tough economic times.

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

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FEDERAL RESERVE BANK of ATLANTA

Economic Research

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On Point

Housing inspection

This quarter, as we assess the slow progress the economy is making to rebuild itself, we wanted to look at what's happened to a couple of specific sectors and industries. With the exception of health care, it seems that one topic has been in the news in recent months: home values and home price appreciation, or the lack thereof. The value—or perceived value—of homes and the concept of home ownership itself have changed during the past 80 years or so. For our podcast, we talked to Karl Case who, with Robert Shiller and Alen Weiss, designed the respected S&P;/Case-Shiller Home Price Index, which tracks changes in the value of the residential real estate market in 20 U.S. metropolitan areas. Case discussed home values and how perceptions and expectations have changed. (You can hear our podcast with Case on our Web site, frbatlanta.org.)

As staff writer Ed English researched home value issues for our cover story, he noted, "As a baby boomer, I have many friends and contemporaries who were much more open to taking on a large mortgage than their Depression-era parents were. While my generation isn't big on delayed gratification, it also witnessed a period in which home buyers were almost universally rewarded for 'going big.' It will be interesting to see if the next generation sees a large mortgage as a risk or a reward."

Perhaps a more sanguine segment of the economy, sports tend to play a big role in the culture of the South, particularly this time of year. Staff writer Charles Davidson says that what struck him as he talked to sports experts was that despite the economic blows to the industry, such as fewer corporate sponsors and—depending on the sport—dwindling numbers of spectators, sports still reign on television and in Southeastern stadiums, which are packed with 50,000, 80,000, or even 100,000 fans on game day. But Davidson says the other issue that reared its head as he looked at college sports was the apparent disconnect between high-level, high-revenue college sports and higher education. "As virtually every state in the Southeast is cutting spending on public universities, including laying off faculty and staff, some major college teams and conferences continue to pay huge salaries to coaches and garner multibillion-dollar television contracts."

The Southeast has been a mecca for tourists for a long time. When staff writer Lela Pratte went looking for a story that would focus on the lodging industry in the Southeast, she expected to center her story on the effects of consumer retrenchment. What she found, however, was the deep impact that significantly declining corporate travel has made on the lodging industry. According to the sources Pratte spoke with, larger hotels and resorts won't see a rebound in business travel for quite some time to come.

We hope you will find some new insights in this issue. Please let us know if you have comments or questions.

Lynne Anservitz
Editorial Director

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Fed @ Issue

The Exercise of Economic Forecasting

Photo by Brad Newton

Mike Bryan is a vice president and senior economist in the Atlanta Fed's research department.

Whenever I give an economic outlook speech, I like to begin by pointing out how notoriously inaccurate economic forecasts are. I usually show the year-ahead predictions of top economists and then report what actually happened. Ordinarily, the predictions aren't very close. In fact, the standard error for the year-ahead growth forecast is about 1.5 percentage points, meaning that the typical one-year-ahead growth forecast encompasses a range of reasonable possibilities so large that it usually includes the likelihood of both strong growth and considerable weakness.

I can usually count on getting a big laugh at this point, which is partly why I do it. But showing how poorly economic forecasts predict the future makes me feel more honest about whatever economic prediction I'm about to lay on the audience.

And here's another humbling observation: Economic forecasts are especially inaccurate when you need them most—around turning points in the business cycle. Forecasting models have a hard time seeing a recession in the making, and—as in the current environment—they have a hard time spotting when recovery will begin.

It's not a number, it's a conversation

So why even bother with economic forecasts? The value of an economic forecast isn't justly measured by the accuracy of a specific prediction over a specific horizon. The forecast guides a discussion on issues that are crucial to making decisions: What are the key assumptions on which the forecast is based? What is the strength of these assumptions? How does this forecast compare with forecasts based on alternative beliefs? And how do we weigh one forecast path relative to another one? In the case of the Federal Reserve Bank of Atlanta, I think the underlying value of an economic forecast is that it represents the foundation of an important dialogue between the research department and Atlanta Fed President Dennis Lockhart.

So our forecast exercise doesn't rely on just one economic model for our forecast; we run a collection of them. Some of the models we use are purely statistical, some are stripped-down economies, and some are large empirical models. None of these models is likely to be "accurate" in that it consistently produces the best prediction. However, taken as a whole, these models provide guidance about a range of possibilities that influence how a Reserve Bank president weighs policy options.

The current conversation

In recent months, the Atlanta Fed has judged that the incoming data indicate greater economic stability. We've seen signs that financial markets are improving and key markets such as residential real estate are no longer deteriorating. But we remain very cautious in our assessment of the immediate future.

While our forecast shows the recession ending sometime in the third quarter, we see impediments to growth that could cause the economy to bump along the bottom for some time. So while we might soon begin the process of recovery, it might not be a very strong recovery. The key assumptions in this outlook are that financial markets will recover only gradually, consumer spending will remain unusually subdued as households rebuild their savings, and lingering uncertainty about the economy's health will keep a lid on business investment.

Forecasting in the current environment has been made all the more difficult because monetary policy has drifted into uncharted, or maybe imperfectly charted, waters.

There are also a few key issues that are still unfolding and require close monitoring. Perhaps at the top of this list is the state of the real estate market. Has the bottom in home prices been found? How far do home and commercial property prices have yet to fall before they reach a bottom? Another issue is the global economic environment. How sustainable is the recent upturn in the European and Asian economies?

Closely related to these issues is the still fragile state of the financial sector and how financial market dysfunction is likely to prolong the economic recession or weaken a recovery. Atlanta Fed research economists have been working to incorporate financial market dysfunction into a simple dynamic model of the economy.

Clouds amid the clouds

Forecasting in the current environment has been made all the more difficult because monetary policy has drifted into uncharted, or maybe imperfectly charted, waters. With our traditional policy lever—the fed funds rate—now resting at essentially zero, our policies have shifted to include a new set of instruments, many of which are designed to operate beyond the usual channels of monetary policy (see "Snapping Rope and Breaking Bricks," EconSouth, first quarter 2009). The innovative actions taken by the Federal Reserve during this financial crisis are historically unprecedented. From a forecasting perspective, we don't have much experience gauging the impact of these actions on the business cycle.

Difficult or not, the process is about to begin again. I can't say at this time how the new forecast will turn out. But there is one thing I can say with perfect certainty: It's going to be an interesting conversation.

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Grassroots

Daytona, Florida
Daytona Area Engines Sputtering

Photo courtesy of the Daytona Beach Area Convention and Visitors Bureau

Cassandra Reynolds saw more than flying steel as 57 cars roared at 180 mph around an asphalt oval in Daytona, Fla., in February. She saw the future of her community's economy.

Reynolds, a Daytona Beach city commissioner, is founder and chair of the Motorsports Daytona Beach Executive Committee, a group that aims to maximize the economic potential of the motorsports industry. She formed the committee out of the belief that the city needed a more diverse economic foundation than beach-related tourism. "And motorsports was the best thing I could think of that we could use as a catalyst," Reynolds said.

Economy needs a jump start

Like most of Florida, Daytona could use a catalyst. Housing market problems and reliance on struggling tourism, leisure, and retail industries have pummeled the Daytona-Deltona-Ormond Beach economy. The recession and job losses have reduced business at events like the Daytona 500 and the 10-day Bike Week, the latter of which brings about 500,000 motorcycle enthusiasts to the area every year. According to a study commissioned by local officials, motorsports generate $1.9 billion in annual local economic activity and account directly or indirectly for more than 30,000 jobs.

Daytona, Fla.

Population	66,941
Volusia County population	494,198
Median household income	$30,532
Median owner-occupied home value	$167,000

Source: U.S. Census Bureau, 2007 American Community Survey

Most notably, stock car racing's signature event, the Daytona 500—dubbed "the Great

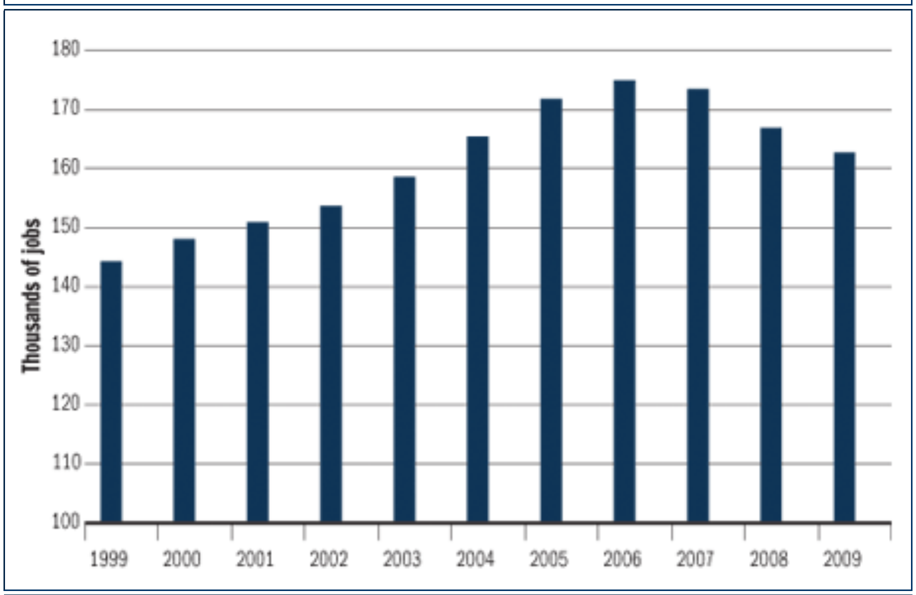
American Race" by promoters—comes to Daytona International Speedway every February. The race caps several days of parades, festivals, concerts, and preliminary races. The 2009 race drew 180,000 fans and paid prize money totaling more than $16 million. The track also hosts another major NASCAR race along with numerous smaller events throughout the year.

Weakened demand led Daytona race officials to cut ticket prices for the 2009 Daytona 500, and it sold out just hours before the starting flag waved. They have also taken the unusual step of closing sections of grandstands for other races. During March, when Bike Week rolled into town, Volusia County's tax revenues from short-term hotel and condo rentals slipped 16 percent, to $918,488, from $1.09 million in March 2008, according to the *Daytona Beach News-Journal*, which cited figures from the county revenue department.

Other motors are also stalling

Daytona's struggles are hardly unusual, especially in Florida. But because the area relies heavily on tourism and a few major events, its economy has suffered even more than other parts of the Sunshine State.

Chart 1
Daytona Area Jobs, 1999–2009



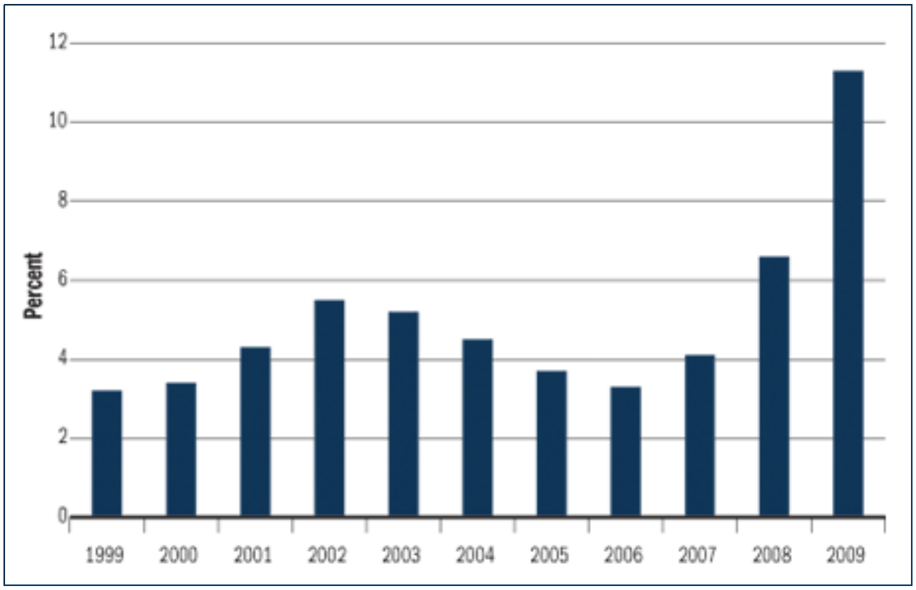
Note: Data are through June 2009.
Source: U.S. Bureau of Labor Statistics

Total nonfarm employment in the Daytona metropolitan area during the first half of 2009 averaged 165,800, the lowest level since 2004, according to the U.S. Bureau of Labor Statistics (BLS) (see chart 1). A preliminary June unemployment rate of 11.3 percent was worse than the state rate of 10.6 percent and the U.S. level of 9.5 percent. The local downturn has been steep: Daytona's unemployment rate has more than tripled since it averaged a scant 3.3 percent in 2006 (see chart 2), according to the BLS.

This employment picture is in part a result of lower attendance at races, despite aggressive pricing at the events. Lower attendance also means fewer merchandise sales, hotel room stays, restaurant meals, and so forth, according to Sean Snaith, director of the University of Central Florida Institute for Economic Competitiveness (IEC) in Orlando.

International Speedway Corp., which runs Daytona International Speedway and 12 other motorsports tracks, including the Talladega Superspeedway in Alabama, reported in Securities and Exchange Commission filings that its food, beverage, and merchandise revenue slid 34 percent in the first half of 2009 from a year earlier, to $26.8 million. In the same period, the company's ticket sales revenue declined 16 percent, to $91.5 million.

Chart 2
Daytona Area Unemployment, 1999–2009



Note: Data are through June 2009.
Source: U.S. Bureau of Labor Statistics

"That all adds up to slower and lower activity in that region," Snaith said. "When you're tightening belts, it's easier to give up going to Daytona than to give up a house payment."

As high-profile as they are, auto racing and motorcycle rallies are hardly the entire economy in the Daytona area. In fact, the housing market bust has hurt the area at least as much as the downturn in tourism, according to Andrew Gledhill, a Moody's Economy.com analyst. From its 2006 peak, the area's median house price has fallen 32 percent, with a 60 percent drop likely by the end of 2010, Gledhill wrote in a March 2009 report. However, the speed of that decline will slow as home sales improve. And those house price figures are not as bad as those for Florida as a whole.

Is improvement around the bend?

As Florida strives for recovery, Daytona-Deltona hopes to rebound gradually as well. The area isn't projected to reach its 2006 peak employment level of 174,900 jobs again until 2015, according to the IEC.

On a brighter note, the Daytona area's stable retiree population makes for a strong health care industry. The education and health care sectors added 1,200 jobs in 2008, while other industries lost jobs and leisure and hospitality employment was

Photo courtesy of the Daytona Beach Area Convention and Visitors Bureau

unchanged, according to the BLS. Through May 2009 employment in education and health care along with leisure and hospitality was flat in Daytona compared with the same period a year earlier. These sectors were comparativelystrong, however, as total employment through May 2009 was down 10,421 jobs from January to May 2008. Indeed, the metro area's 10 largest employers include two hospitals (Halifax Health, the second-largest employer, and Florida Hospital, the fourth); Volusia County Schools, which is the biggest employer, with 8,350 workers; Daytona State College; and Embry Riddle Aeronautical University.

Reynolds, of the Motorsports Daytona Beach Executive Committee, hopes to blend the area's economic strengths and help citizens use education as a doorway to the motorsports industry, broadly defined. "These careers go far beyond the jobs on the race teams for these events," she said. "They can include careers in engineering, marketing, finance, information technology, health care, and hospitality, to name a few."

Any expansion in those sectors will no doubt be welcomed.

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

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Q & A

"The Average Is Almost Meaningless"

An Interview With John Adams, Housing Policy Expert

Behind the headlines about falling house prices and homeownership rates are stories that are more challenging to summarize but tell us more about changes in national housing consumption. John Adams, professor emeritus of geography at the University of Minnesota, has spent a good deal of his career telling those stories. Adams is an expert in housing policy, housing finance and markets, regional economic development policy, urban planning and land use, and urban sprawl. He foresees significant changes in U.S. homeownership as the nation's demographics evolve.


Photo courtesy of the University of Minnesota

JOHN S. ADAMS

Title	Professor
Organization	University of Minnesota
Web site	www.hhh.umn.edu/people/jadams/
Other	Adams is a faculty member in the Hubert H. Humphrey Institute of Public Affairs at the University of Minnesota. He has been a National Science Foundation Research Fellow at the Institute of Urban and Regional Development at the University of California at Berkeley and an economic geographer in residence at the Bank of America. Among his books are *Housing America in the 1980s* and *Minneapolis-St. Paul: People, Place, and Public Life*.

EconSouth: *What are some of the factors that cause the overall rate of homeownership to fluctuate?*

John Adams: One of the things that needs to be pointed out is [that] the way in which people buy and use housing at any given time is the consequence of several things going on at the same time. One, of course, is the inflation rate, which then is reflected in interest rates. Another is the general economic prosperity of the moment. Sometimes prosperity and inflation go together, but sometimes they don't; they'll push in different directions. The third thing that is overlooked is the revision of the Internal Revenue Service code in 1986, which had as one of its consequences the removal of some of the profitability of owning, operating, and investing in rental housing. As a result [of the code changes], many people who owned rental units decided that owning and operating rental housing was no longer as profitable as other investment opportunities, so they converted rentals to condos. One of the results of converting to condos in the middle and late '80s and into the '90s was an increase in home ownership rates. Renters became owners because they didn't want to move, and at least in part of the '80s the terms for which one could make those kinds of purchases had interesting effects.

ES: *How meaningful an indicator is the rate of homeownership in a given metropolitan area?*
Adams: As a geographer, I try to draw people's attention to national averages that, when you start looking at them closely, start to dissolve into regional variations that in some ways are far more complicated and interesting than the national average. For example, you look at Atlanta, Sandy Springs, and Marietta, Ga., in the 2000 census, and you see the population of that metro area increased almost 40 percent in a 10-year period.

When that happens in a place, the growth starts to feed on itself. When a place is growing fast, money flows into the place from outside to invest in the opportunities that the growth creates. And then people getting out of college look for where the jobs are; it becomes kind of a positive, expanding cycle. But at the same time that Atlanta's growth is going through the roof in the '90s, some other metro areas are losing population. So the average [growth rate] turns out to be something like 13 or 14 percent, but the average is almost meaningless when you look at how much variation there is around that average.

ES: *You've written that a house is an investment that requires an investment.*
Adams: If you just bought [a house] and lived in it and didn't do anything to it, it'd be falling down around your ears in 36 years. You have to take care of these things. The scuttlebutt in the literature says if you're not investing 2 percent a year in the house, it's deteriorating in the absolute quality and in the absolute value. We'll see. Of course, it also depends a bit on what's going on around it in the neighborhood and the community in which it's located. And then there's a cachet associated with this neighborhood versus that neighborhood and this suburb versus that suburb. For the press to talk about this in very gross terms can mislead people, who then think,"Well, look, this was going on in Las Vegas in 2003, 2004, 2005. Therefore, it's going to happen to me in Altoona, Pa." It doesn't work that way, especially in this huge country, where what's going on in Miami and what's going on in Portland, Ore., are two completely different worlds.

This interview was conducted by Ed English, a staff writer for EconSouth.

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Regional Update

Regional Economy Stabilizes

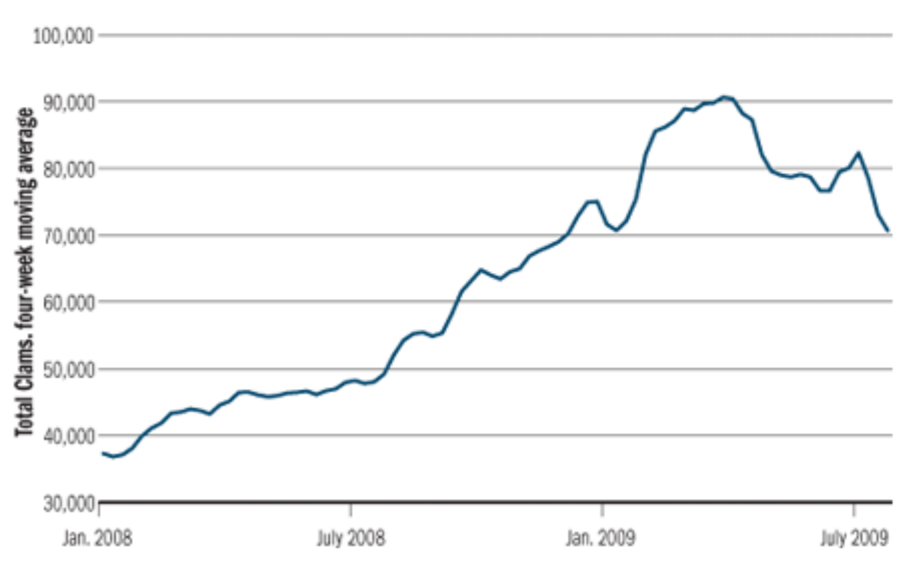
The first half of the summer has witnessed further signs of economic stabilization in the Southeast. Data reports and information the Atlanta Fed research department gathers from business contacts show steady, albeit weak, economic activity in most sectors. While the regional economy is expected to improve throughout the rest of the year, the rate of improvement will likely be very modest.

The main reason for the sober outlook is the numerous headwinds businesses and consumers continue to face. In particular, consumers are not expected to embrace additional spending as they strive to pare back expenses. This cautious consumption is likely to continue for some time, especially in light of the weak employment outlook. Sales tax revenue for the Southeastern states declined, on a year-over-year basis, for seven consecutive quarters through June 2009, with second-quarter revenue more than 5 percent below year-earlier levels. Households are expected to increase their savings and limit spending as long as the economic environment remains uncertain.

Tourism-related spending, an important and typically buoyant component of retail activity in several parts of the Southeast, is also suffering. For example, the Florida Department of Revenue estimated that sales tax revenue for tourism and recreation activities was down more than 10 percent in June 2009 from a year earlier. In addition, estimates from Visit Florida, the state's official tourism marketing corporation, show a 9.4 percent drop in the total number of travelers to the state in the second quarter compared with the same period in 2008. Information from hospitality industry contacts supports these data. Some areas noted a significant decline in business-related travel and convention attendance.

One area that has seen modest improvement is single-family residential sales and construction. Permits for new single-family residential construction remain well below year-earlier levels in all Southeastern states, but all six states have posted monthly gains since January 2009. Existing home sales also are improving. Data from the Florida Association of Realtors show a 28 percent year-over-year increase in single-family sales in June. The outlook among builders and Realtors, which had improved in the spring, moderated over the summer. The condo market remains in distress. Vacancy rates remain high, and since many condo sales are second or vacation homes, the outlook for future sales continues to be bleak.

Initial Claims for Unemployment Insurance in the Six Southeastern States



Source: Source: U.S. Department of Labor, Federal Reserve Bank of Atlanta

Another construction-related sector that remains under stress is commercial development. Office and industrial vacancy rates have been trending upward, with some areas reporting greater availability of sublease space. Developers continued to report fewer backlogs, and more projects were delayed. Recent data support the view that commercial construction activity will continue to soften.

Regional factory activity continued to climb from very low levels over the summer. Overall production continues to contract, albeit at a much slower pace than earlier in the year. Kennesaw State University's Southeast Purchasing Managers Index (see this issue's "Data Corner") rose to 50 in July, indicating that manufacturing activity was neither expanding nor contacting. The report also showed that new orders were rising, a sign that future production will likely tick up.

Business hiring plans remain very conservative, according to most of the Atlanta Fed's business contacts. Although layoffs continue, businesses are implementing layoffs at a more modest pace than earlier in the year. The chart shows that initial claims for unemployment insurance for the combined states of the Southeast, although still elevated, have declined steadily since April. While the worst may be over regarding job losses, the unemployment rate appears set to remain high as hiring plans continue to be cautious.

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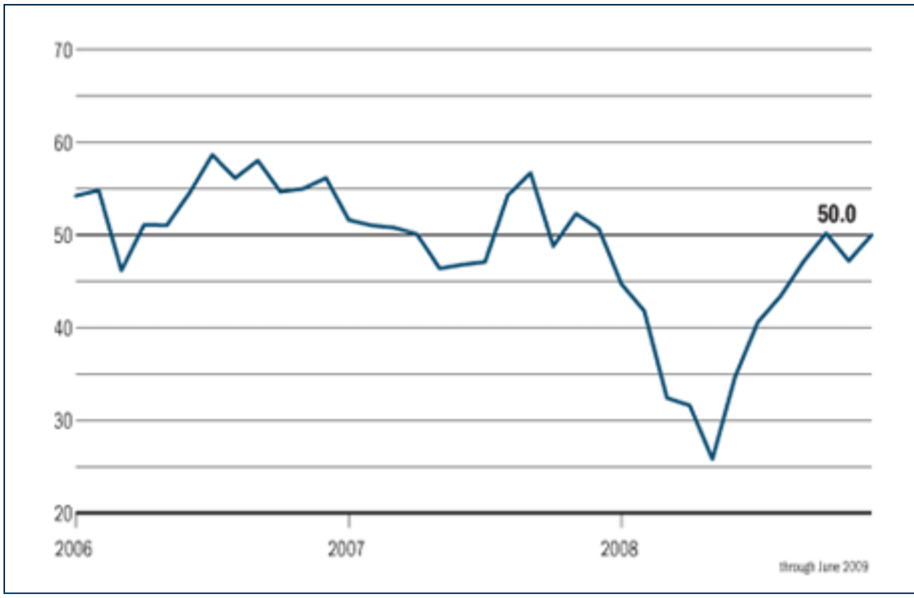
Data Corner

Southeast Purchasing Managers Index

Southeast Purchasing Managers Index



Source: Kennesaw State University Econometric Center

The Econometric Center at Kennesaw State University's Coles College of Business prepares a monthly Purchasing Managers Index (PMI) Report. This report provides an analysis of the most current market conditions for the manufacturing sector in Alabama, Florida, Georgia, Louisiana, Mississippi, and Tennessee.

The report, which is based on a survey of major manufacturing companies in those states, analyzes trends and activities for new orders, production, employment, deliveries, purchased materials, finished goods, and commodity prices.

An index reading above 50 indicates that more participants are reporting a higher level of activity than the prior month. The higher the index is above 50, the stronger the indication of wider-spread growth. The lower the reading is below 50, the more activity is contracting.

The Southeast PMI rose to 50 in July from 47.2 in June. A reading of 50 suggests that the manufacturing sector's performance is neither increasing nor decreasing, but stable. The chart shows that the path of the Southeast PMI has been trending upward since December 2008, when it hit 25.8, its lowest point since the series began.

The increase in July's Southeast PMI was based on increases in advances in new orders, production, and employment. The new orders component rose for the third consecutive month, increasing 11.2 points during that period and 4.5 points in July alone. Production rose 13.4 points in July to 62.2. Employment's 4.8 point increase was related to the strong movement for new orders and production. Supplier delivery time fell 4.1 points, suggesting that orders are increasing faster than suppliers can deliver. The commodity price measure rose 5 points to 55.1 points, its highest reading since September 2008. A 4.7 point decline in finished inventory components was likely tied to the three-month pickup in new orders.

The Southeast PMI is calculated using the same methodology as the Institute for Supply Management's (ISM) national survey, making comparisons of national and regional trends possible. The ISM index for July was 48.9, which suggests that manufacturing activity in the Southeast is rebounding a bit faster than it is nationally.

University Studies

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Universities Delve Into Regional Economies

To gauge where the economy is and to see where it may head, researchers examine data that measure consumer sentiment. Two widely used sources of such data are the Conference Board's Consumer Confidence Index and the Reuters/University of Michigan Index of Consumer Sentiment. While these two indexes can provide insight into consumers' opinions on a national level, gauging how consumers feel at a more local level is also useful. Fortunately, some members of the Atlanta Fed's Local Economic Analysis and Research Network (LEARN) have constructed their own versions of these indexes.

Businesses' outlook improving in Alabama
The Alabama Business Confidence Index (ABCI) is a quarterly gauge of the state's business sentiment conducted by the Center for Business and Economic Research at the University of Alabama. The ABCI equally weights six survey variables—expectations for the national and Alabama economies and four key industry indicators: sales, profits, hiring, and capital expenditures.

During the third quarter, the ABCI climbed 14 points, posting the largest quarterly gain in the survey's almost eight-year history. Still, the economy is not expected to turn the corner in the third quarter, as indicated by an ABCI reading of 46. (An index reading above 50 indicates expansion; less than 50 indicates contraction.) Sales, with a reading of 50.3, was the only component higher than 50. However, all six components of the index rose by double digits, led by a 20.4 point improvement in the national economy variable.

Wariness in the Sunshine State
The University of Florida publishes a monthly Florida Consumer Confidence Index. The index is constructed using current perceptions and expectations of personal finance and national economic conditions and perceptions about buying big-ticket items.

In July, Floridians' consumer confidence declined 2 points, to 67, from a revised June index of 69. (An index reading above 100 indicates strong growth.) The only component that rose is whether now is a good time to buy big-ticket consumer items. "This decline comes as a bit of a surprise," Chris McCarty, the survey director, said. "Most of the decline can be attributed to a big drop in consumers' perceptions of long-term economic conditions and, second, to perceptions of personal finances. Given that the stock market is now up for the year and housing is showing strong signs of stabilizing, I would attribute much of this decline to the news about employment. Moving forward we predict consumer confidence may gain a little in the next month or two given this big a drop."

Mississippi businesses optimistic
The Gulf Coast Business Council Research Foundation releases a quarterly report based on local chief executive officers' and business owners' perceptions of the economy compared with six months prior and their outlook for the next six months.

For the second quarter of 2009, Mississippi Gulf Coast business owners and CEOs reported significant improvements in perceptions of the current economy compared with the previous six months and in their six-month projections. Their overall measure of business confidence for the Mississippi Gulf Coast improved by 13 points from the previous quarter, to 57. More than 55 percent of respondents predict that the performance within their own industries will improve in six months, compared with 46 percent in March. The number of respondents who believe the economy would worsen in six months declined to 19 percent from 26 percent the previous quarter.

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Personal Consumption Expenditure

Personal consumption expenditure (PCE) is the consumer spending component of gross domestic product (GDP). PCE measures the value of goods and services purchased by U.S. households. It is the largest portion of GDP, accounting for more than 70 percent of the measure.

As a result, significant changes in PCE—what we might also refer to as consumer spending habits—will affect the economy. Marked drops in consumer spending can lead to a recession. Conversely, an increase in PCE during a recession generally indicates that a recovery is at hand.

PCE and personal savings are inversely related; as consumers save more, they spend less, a phenomenon also linked to consumer attitudes and expectations. For instance, if consumers are uncertain about their current and future finances, they will rein in spending and save more. As of July 2009, the savings rate (savings as a percentage of GDP), sits at 4.2 percent, well above the 10-year average of 2.8 percent. However, the savings rate has noticeably decreased recently, which may mean that people are feeling a bit more confident and thus spending more.

The goods component of PCE accounts for almost one-third of total consumer spending. The goods component is very broad and is broken down into two subcategories: durable and nondurable goods.

Durable goods make up about 11 percent of PCE and are defined as items that last for more than three years (such as cars, refrigerators, and televisions) and are generally more expensive than nondurable goods. Because the timing of many durable goods purchases is discretionary, they are a key indicator for economists.

Nondurable goods are generally less expensive than durables. Nondurables, which account for about 22 percent of PCE, usually display less volatility than durables because many nondurables are necessities, such as food and clothing, that people must buy even when times are tough.

Services account for more than two-thirds of PCE. Today the United States is a service-based economy. Services, like nondurable goods, tend to have more stable spending patterns during volatile economic times because some services, such as going to the doctor and getting haircuts, are hard to cut back on.

Because of the role that personal spending plays in the economy, PCE is a key indicator that yields important insight into the economy's direction. During times of economic uncertainty, such as today, economists track PCE closely.

By Courtney Nosal, an economic analyst at the Atlanta Fed

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On the Ground

An Interview With Julius Weyman, Regional Executive at the Atlanta Fed's Birmingham Branch

When you became regional executive at the Birmingham Branch, you didn't have many contacts to help gauge the Alabama economy. What steps have you taken to gather economic information effectively? I have found the public is pretty excited to engage when they learn that the Federal Reserve is not only interested in what they have to say but is also eager to maintain a flow of information and consider it in the context of informing, guiding, and ultimately constructing monetary policy. The best insights into Alabama came from the people around me. When I landed in this assignment, the office staff had already outlined places to go and people to meet. Careful thought had been given to connections that would likely be helpful, and the groundwork had been laid. Not only were the right people selected for me to meet, but they were expecting me to learn from them, and they were energized about the Atlanta Fed's focus and the REIN (Regional Economic Information Network) initiative. To a person, they were prepared to suggest ideas, provide information, and contribute. I'd say they were hungry to be involved and quite excited about the Atlanta Fed's increasing its attention to this area beyond what the bank had done previously.

What relationships have you formed that will help you gather solid regional intelligence? Once we got the right contacts helping us, our relationships have been easy to build. Manufacturing and agriculture, education, health, the financial sector, construction, real estate, and the rest—there is nothing Alabama doesn't do, and there is someone we know or can talk to as necessary.

Have your information-gathering efforts reached outside the Birmingham area? Through the formation of advisory councils—the Atlanta Fed has several now—we have selected key players in targeted areas for seats on the councils. We search the entire region to choose folks, and the regional executives in our five branches share our best people with one another depending on who needs what and who knows whom. For example, Birmingham's advisory council is agriculture, and I have citrus representatives from Florida based on references I received from our Jacksonville and Miami regional executives. Our Nashville regional executive helped identify a sugar industry representative. We have crawfish and rice farming representatives from Louisiana, and I went to Georgia to find a biofuels contact. Of course, Alabama is well represented with row-crop farming and cattle ranching advisers.

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D6 Factor

The D6 Factor fell to a record low of –6.3 in April from a revised –6.0 at the end of the first quarter. From its April low, the index rose slightly to –6.2 in May, reflecting a slight improvement in Southeastern economic activity. The index has been in negative territory since October 2006 and, until the May upturn, had been setting new historical monthly lows since the start of the current recession. (A negative value indicates that economic conditions are weak.)

Note to readers: This issue's D6 Factor summary and chart are updated only through May because we are in the process of updating the methodology and construction of the D6 Factor index.

The D6 Factor

Note: The growth rate is normalized to zero.
Source: Federal Reserve Bank of Atlanta

About the D6 Factor
The D6 Factor is an estimate of the trend common to 25 distinct monthly series of economic data for the six states of the Sixth Federal Reserve District. It provides a broad measure of Southeastern economic conditions that is available more frequently than estimates of gross domestic product (GDP) for the six states. Also, unlike an average of state-level GDPs or other factors, the D6 Factor can filter out idiosyncratic shocks that disproportionately affect individual states. For detailed information on the D6 Factor's construction, see "When More Is Better: Assessing the Southeastern Economy with Lots of Data," by Pedro Silos and Diego Vilán (*Economic Review*, Third Quarter 2007).

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Economic Research

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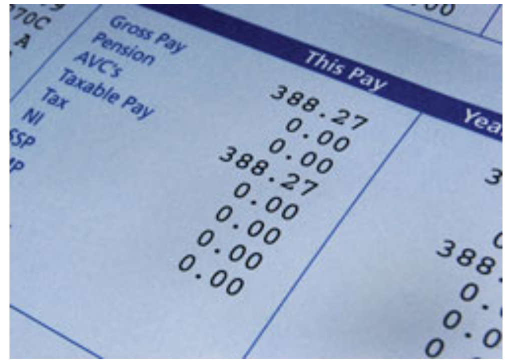
Closing Numbers

$857

Median amount earned weekly by U.S. workers 25 years and older

Source: U.S. Bureau of Labor Statistics



4,338

Number of U.S. facilities offering spectator sports

Source: U.S. Census Bureau

62.2

Percent of U.S. individual tax returns e-filed in tax year 2007

Source: Internal Revenue Service

$13.8

Tax revenue, in billions, that the hotel, motel, and lodging industry generated in the Southeast in 2008

Source: The American Hotel and Lodging Educational Foundation, as cited in EconSouth's article, "Vacancy Signs Dot Lodging Landscape"

$6

Revenue, in billions, that the National Football League generated during the 2008–09 season

Source: NFL.com

69

Percentage of Americans who owned their home in 2005

Source: U.S. Census Bureau, as cited in *EconSouth*'s article, "On the Bubble: When Real Estate's Long Haul Took a Shortcut"

$975

Salaries, in millions, paid by the plastics industry in Georgia in 2008

Source: Society of the Plastics Industry

19,670

Number of retail establishments in Alabama

Source: U.S. Census Bureau

$2.569

Amount, in trillions, of assets controlled in the United States by nonprofit organizations

Source: Internal Revenue Service

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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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Now and Then

The archetype of the modern suburban community, Levittown, N.Y. (right), helped provide affordable housing to post–World War II Americans and satisfy the country's appetite for homes. More recently, house price appreciation led to the overbuilding that contributed to the swoon the economy has experienced.

Photos by Brad Newton (left), and courtesy of Library of Congress photographic archives (right)