Current Economic Conditions in the Eighth Federal Reserve District

Little Rock Zone

September 17, 2008

Prepared by the
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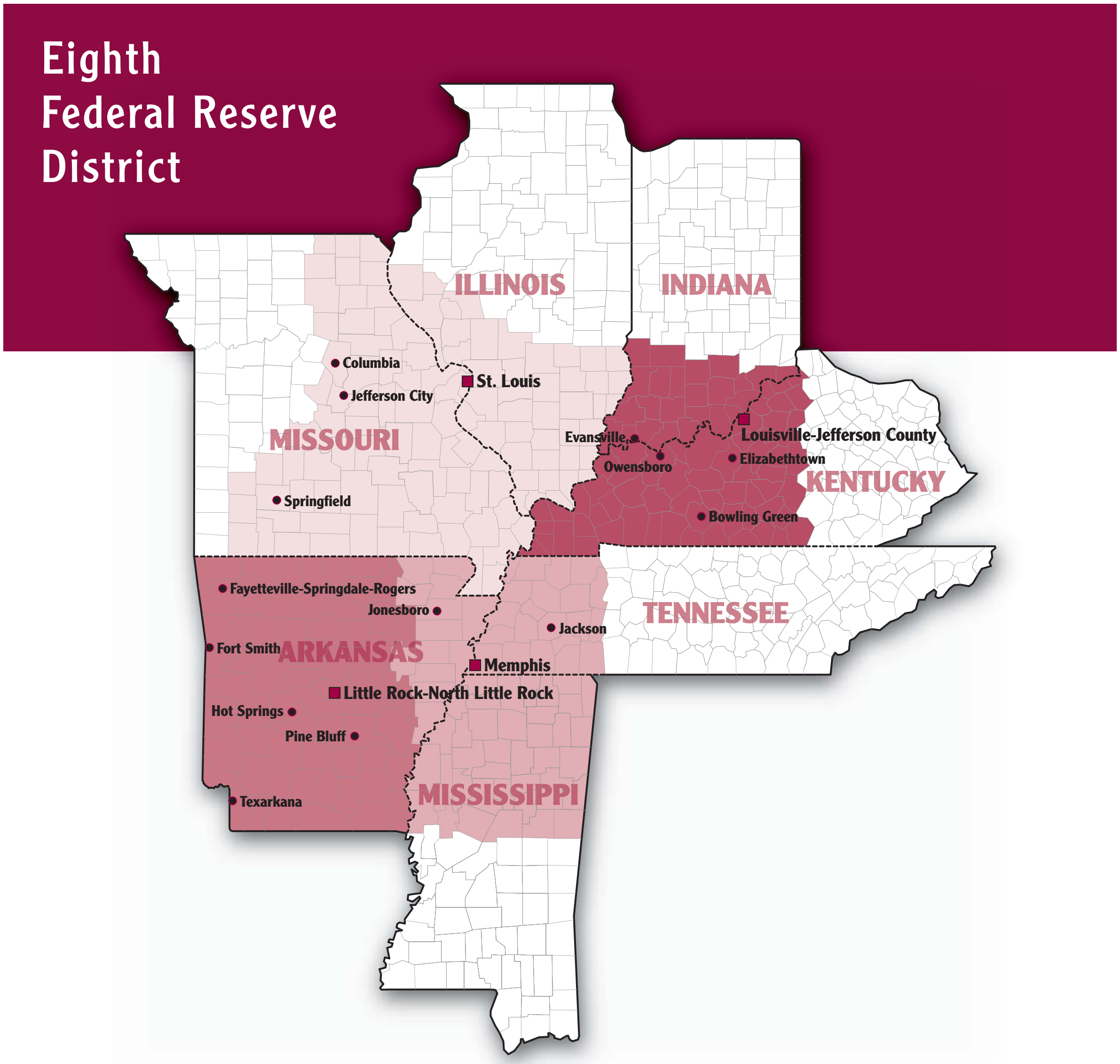

This report (known as the *Burgundy Book*) summarizes information on economic conditions in the Little Rock zone of the Eighth Federal Reserve District (see map above), headquartered in St. Louis. Separate reports have also been prepared for the Louisville, Memphis, and St. Louis zones and can be downloaded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

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

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Little Rock Zone Report—September 17, 2008

Incoming information about economic activity in the Little Rock zone was mixed in the third quarter. Some contacts, including those in general retail, agriculture, and the service sector, indicated signs of positive or improving conditions. Other sectors, including auto sales, construction, and manufacturing, reported weakened conditions.

Consumer Spending

Retail sales reports for July and the first half of August were mostly positive among general retailers but mostly negative among car dealers in the Little Rock zone. About 88 percent of the general retailers indicated that sales were up compared with 2007, and 86 percent reported that sales were higher than anticipated. In contrast, 72 percent of car dealers reported decreased sales. Forty-three percent of car dealers reported increased sales of low-end cars relative to high-end cars and 57 percent of car dealers reported more rejections of finance applications.

The sales outlook for September and October was mostly optimistic among the general retailers, with 75 percent expecting sales to increase over 2007 levels. Among car dealers, 71 percent expect sales to remain below last year's pace.

Manufacturing and Other Business Activity

Manufacturing in the Little Rock zone continued to decline slightly in the third quarter of 2008. Firms in the sporting and athletic goods manufacturing industry and plastic manufacturing industry both reported plans to open a new facility in the zone. Other contacts in the machinery manufacturing industries reported plans to expand existing operations, and a firm in the furniture manufacturing industry announced plans to move their corporate headquarters into the Little Rock zone. In contrast, contacts in the animal slaughtering and processing industry and ship/boat manufacturing industry reported plans to lay off workers and decrease operations, citing weak demand. A firm in the iron and steel pipe manufacturing industry announced that it will close a plant in the zone due to rising costs.

The service sector continued to expand. Contacts in the business support services, customer/technical support services, and transportation/warehousing industries reported plans to expand operations and hire additional workers. A major computer manufacturer announced plans to locate a new service center in the Little Rock zone. In contrast, the merger of wireless cell phone providers will reportedly result in a net decrease of workers.

Real Estate and Construction

In Little Rock, year-to-date home sales in July were down by 21 percent from the same period a year earlier. For the same period, year-to-date single-family housing permits were down by 35 percent. The industrial vacancy rate in Little Rock decreased in the second quarter of 2008 relative to the first quarter. Meanwhile, the suburban office vacancy rate decreased while the downtown office vacancy rate increased. A contact in northeast Arkansas reported that commercial building was slow. A contact in northwest Arkansas expects that tightened financing requirements will lead to a softening of commercial real estate development. A commercial construction contact in central Arkansas reported that their backlog has decreased from 12 months to 6 months as projects have begun to dry up.

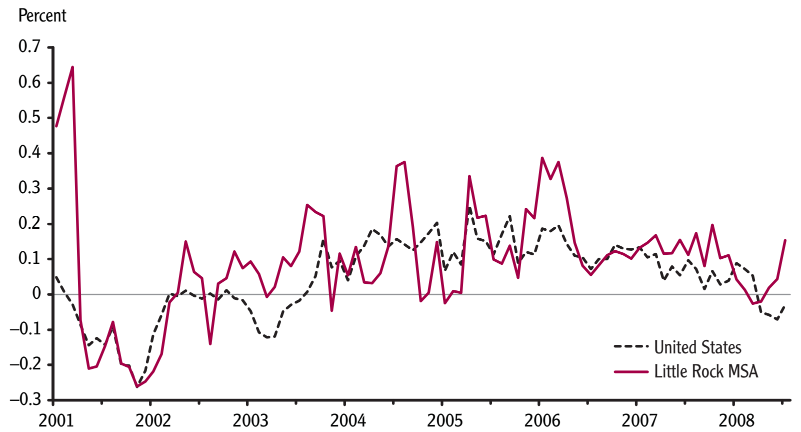
Banking and Finance

Contacts provided mixed reports on local banking conditions. On net, loan demand across all categories was flat. Contacts reported continued declines in commercial and industrial loans, and modest declines in residential mortgage lending activity. One contact noted that residential mortgage lending for small homes picked up over the summer, but the decline in lending activity for large homes has outweighed this increase. Reports indicated a slight increase in consumer lending activity. However, some contacts noted that tightened credit standards have limited the increase in consumer loan volume. Contacts indicated little to modest growth in deposits.

Agriculture and Natural Resources

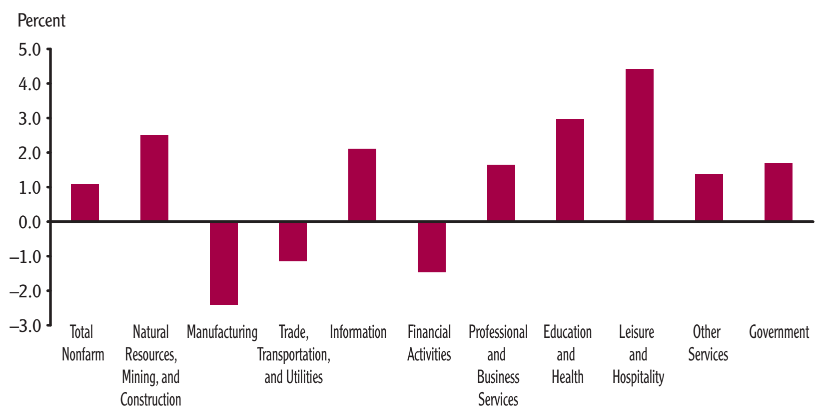
Partly due to late planting this year, development of corn, soybeans, sorghum, cotton, and rice is behind the normal pace in Arkansas. Since mid-July, corn, soybeans, sorghum, and cotton conditions have deteriorated slightly, but conditions for rice have improved somewhat. Currently, 18 percent of the soybean crop is rated in poor condition, and less than 10 percent of the other crops have that rating. As of August 1, yields for corn, soybeans, sorghum, rice, and cotton in Arkansas were expected to range from 2 percent lower to 4 percent higher than last year's yields. As of mid-August, 88 percent of the pastures in Arkansas were in fair condition or better, 29 percentage points more than in 2007. Winter wheat yields were expected to be 41 percent higher.

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



During 2007, payroll employment growth in the Little Rock MSA was stronger than for the nation as a whole. Employment growth slowed during the first part of 2008, but has since rebounded. Over the three-month period ending in July 2008, Little Rock monthly employment growth averaged 0.15 percent, while U.S. employment growth averaged –0.03 percent. Over the past 12 months, employment in the Little Rock MSA has increased by 3,700 jobs, approximately 1.1 percent.

Little Rock Employment Growth by Sector
Year/Year Percent Change, July 2007–July 2008



Between July 2007 and July 2008, employment growth has been strong in several service-related sectors. Employment growth in the leisure and hospitality sector exceeded 4 percent and employment in education and health increased by 3 percent. Other sectors with net job gains included information services, professional and business services, other services, and government. In contrast, manufacturing employment contracted by 2.4 percent. Led by strong job growth associated with the Fayetteville shale play, employment growth in the natural resources, mining, and construction category amounted to 2.5 percent.

Little Rock Zone—MSA Employment and Unemployment

	Nonfarm payroll employment percent change, July 2007–July 2008			Unemployment rate
	Total	Goods producing	Service providing	June 2008
Little Rock	**1.08**	**–0.22**	**1.27**	**4.2**
Fayetteville-Springdale-Rogers, Ark.	1.18	–1.59	1.94	3.8
Fort Smith, Ark.	0.24	–4.47	2.17	4.8
Texarkana, Ark.-Tex.	2.70	–1.33	3.33	4.6
United States	0.19	–2.64	0.74	6.0

SOURCE: Bureau of Labor Statistics.

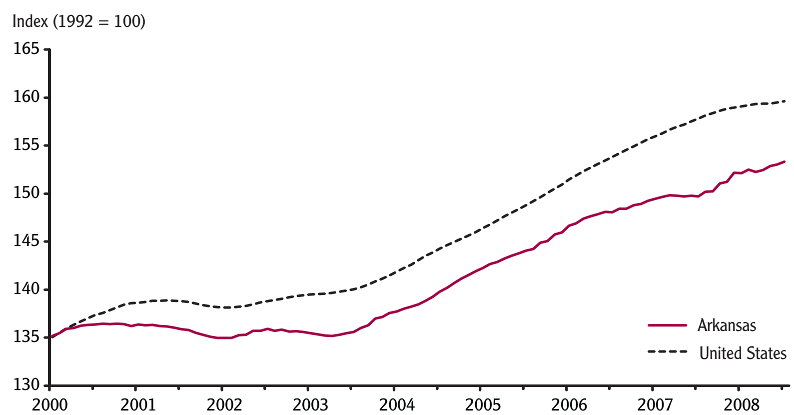
Little Rock Zone—MSA Housing Activity

	Total building permits, units year-to-date		
	July 2008	**Percent change**	**House price index, percent change, 2008:Q2/2007:Q2**
Little Rock	**1,876**	**–1.8**	**1.09**
Fayetteville-Springdale-Rogers, Ark.	1,747	–18.0	–2.09
Fort Smith, Ark.	403	–34.3	1.80
Hot Springs, Ark.	39	–38.1	4.93
Pine Bluff, Ark.	61	69.4	0.21
Texarkana, Ark.-Tex.	95	–67.2	3.36
United States	604,303	–32.0	–1.71

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

Total residential building permits through July were lower than a year earlier in five of the six MSAs in the Little Rock zone. In Little Rock, permits fell by 1.8 percent. In Pine Bluff, however, permits were up by over 69 percent from the previous year. In the second quarter of 2008, house prices were up in five of the six MSAs. In the Fayetteville-Springdale-Rogers MSA, prices fell by 2.1 percent. In contrast, house price increases in the other MSAs ranged from 0.2 percent (Pine Bluff) to 4.9 percent (Hot Springs).

Arkansas Coincident Economic Activity Index

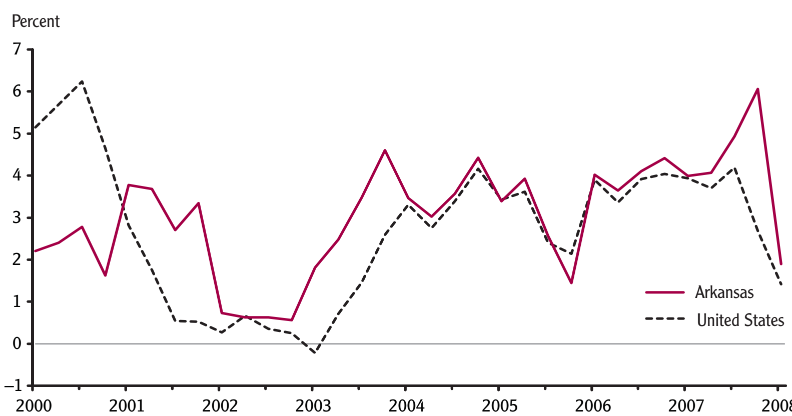


SOURCE: Federal Reserve Bank of Philadelphia.

The Philadelphia Fed's coincident index combines payroll employment, wages and salaries, the unemployment rate, and hours worked into a single index. According to this index, Arkansas has underperformed the country as a whole since 2000. However, recent data show an increase in economic activity relative to the rest of the nation. In the 12 months ending July 2008, the Arkansas index rose 2.4 percent, compared with an increase of only 1.1 percent for the nationwide index.

Arkansas Real Personal Income Growth

Percent Change, Year/Year



SOURCE: Bureau of Economic Analysis.

Personal income growth in Arkansas has kept slightly ahead of national income growth since 2006. In 2007, however, the difference in growth rates increased. Year-over-year growth in the third and fourth quarters of 2007 was 4.9 and 6.0 percent in Arkansas, while the U.S. personal income growth in those quarters was 4.2 and 2.7 percent. In the first quarter of 2008, the most recent quarter for which there are data, year-over-year income growth in Arkansas was 1.9 percent, compared with a 1.4 percent growth in the nation as a whole.

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

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

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

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

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

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

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