Albemarle County, Virginia

July 31, 2010

# QUARTERLY ECONOMIC INDICATORS

INSIDE THIS ISSUE:



**Special points of interest:**

- Unemployment rate rises slightly; remains below U.S. and Virginia levels.
- Total employment drops, but the finance & insurance and real estate sectors gain.
- Prices in Albemarle's housing market remain under downward pressure.
- New residential and commercial building permits drop; the decline reflects excess existing inventory.
- Sales tax, meals tax, and hotel/motel tax revenues rise modestly.
- U.S. consumer confidence jumps sharply; U.S. leading economic indicators grow at steady pace.

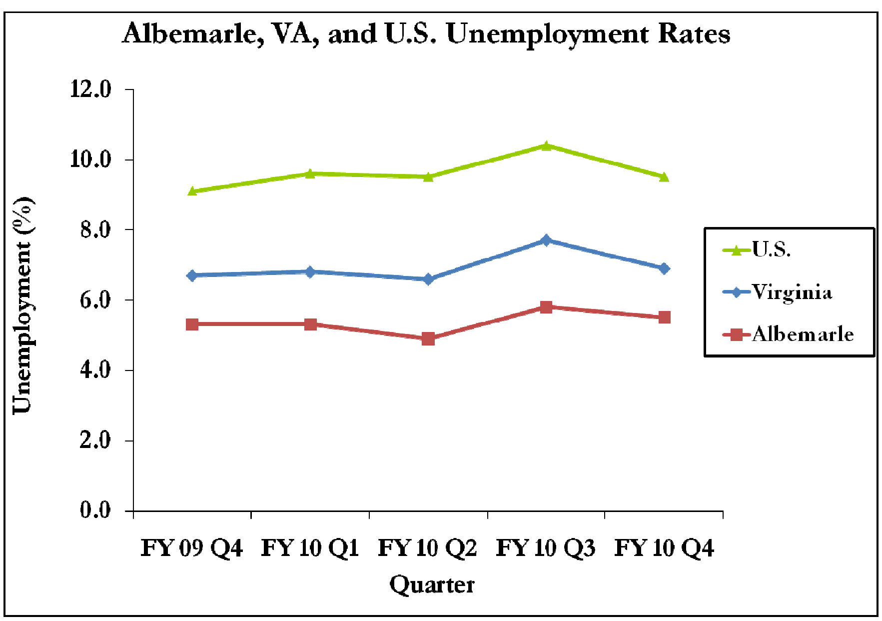
## UNEMPLOYMENT RATE RISES SLIGHTLY

Albemarle County's non seasonally-adjusted unemployment rate rose slightly from 5.3% in FY 2009 Q4 to 5.5% in FY 2010 Q4, the latest complete quarter for which Virginia Employment Commission data exists. This increase was in tandem with the rise in Virginia's rate, which went from 6.7% to 6.9%, and the U.S. rate, which rose from 9.1% to 9.5%, during the same period. Please see the graph below.

The increase in the County's rate of unemployment, although unfortunate, does contain at least one piece of good news: Albemarle's rate remains lower than the state and U.S. rates, a testament to the resilience of the County's economy. This situation parallels the relative rankings of the local, state, and national unemployment rates during the 1990-91 and 2001 recessions. The 3.8% increase in the County's unemployment rate was slightly higher than the 3% rise in the state rate, but below the U.S. rate increase of 4.4%.

Contrary to a commonly-held belief, the County does not always lag the state and the U.S. going into recession, and does not always lead the state and the U.S. coming out of recession, at least not with regard to changes in the rate of unemployment. In the case of the past several quarters, as shown on the graph below, the change in Albemarle's rate generally has been in the same direction as the change in the state and U.S. rates. The County's quarterly rate, in fact, has moved in the same direction as the state and/or U.S. quarterly rate roughly 75% of the time in every quarter since FY 1990 Q3.

Another important point to know about the unemployment rate is that this figure tends to be a *lagging* indicator of the health of the economy; firms frequently lay off workers *after* business conditions have deteriorated, rather than *in anticipation of* difficult conditions. Similarly, it should be pointed out that the unemployment rate historically has tended to peak *after* the officially-designated end of recessions. One theory with regard to this latter phenomenon is that people who have dropped out of the workforce during the recession (and, therefore, are not counted among the official unemployment numbers) tend to re-enter the workforce when business conditions begin to improve, thereby driving up the official rate of unemployment.



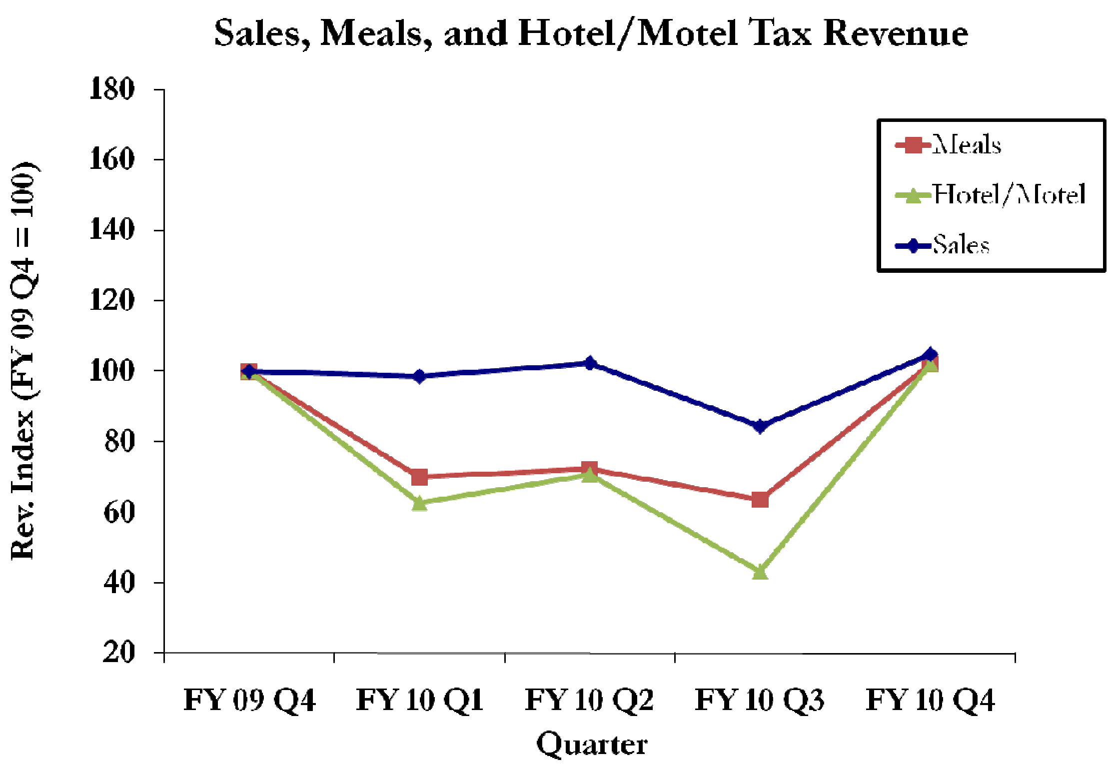
# Sales, meals, hotel/motel tax revenues Rise

Tax revenues offer a good indication of the state of the County's economy. Changes in sales, meals, and hotel/motel tax revenues in particular offer a reasonable approximation of strength or weakness in local economic conditions, since these revenue streams reflect the underlying consumption of many goods and services. At the national level, private consumption represents roughly 70% of all economic activity; the exact local percentage is not known but is thought to be a major component of Albemarle's economy. There exists reasonably good news with regard to the performance of hotel/motel, meals, and sales tax revenues between FY 09 Q4 and FY 10 Q4, the last quarter for which complete data exists.

Hotel/motel tax revenue increased by about 2% between these quarters. (Note that the large increase between FY 10 Q3 and FY 10 Q4, shown on the graph below, reflects the seasonal impact of the University of Virginia graduation ceremonies, which take place in May of each year). The modest Q4-to-Q4 performance of hotel/motel tax revenue would seem to suggest that the County's tourism industry has bottomed out. If tourism did bottom out, then we would expect to see meals tax revenue perform roughly in line with hotel/motel tax revenue. Not surprisingly, between FY 09 Q4 and FY 10 Q4 meals tax revenue grew also by about 2%. It should be pointed out that the U.S. economic recovery probably began sometime around the start of FY 10 (see U.S. GDP story, page 5), might have encouraged residents of the Charlottesville MSA to eat in restaurants again, thereby contributing to the modest increase in meals tax revenue. Meals tax revenue, in other words, depends on both tourism and the spending patterns of local residents.

As for sales tax revenue, this item performed better than did the other two revenue streams. Between FY 09 Q4 and FY 10 Q4 the County's sales tax revenue grew by 4.85%. The strength of this number offers further evidence that the recession ended some time during the course of the past year and that a recovery, however weak, has begun. Note that the increase in sales tax revenue coincided with a fairly strong increase in U.S. consumer confidence between the two quarters (see Consumer Confidence & Leading Economic Indicators story, page 5). This situation highlights the relationship that is thought to exist between consumer expectations about the future, on the one hand, and current consumption, on the other hand. If consumers expect that the economy will improve tomorrow, they will tend to increase consumption today.

It should be pointed out, however, that a number of factors might be influencing consumer expectations in such a way that growth in private consumption will be limited in the next several quarters. One factor almost certainly is the state of the labor market. Even if the U.S. economy has bottomed out and begun a modest recovery, the rate of growth in the economy has not been sufficient to bring down the unemployment rate (see Unemployment Rate, page 1). This uncertain employment environment clearly would not encourage consumers in Albemarle County to increase their purchases goods and services. A second factor that could be working against growth in consumption in the County involves ongoing weakness in the local real estate market (see Housing Prices story, page 3). As housing values have declined, Albemarle consumers likely feel less wealthy than they did during the "boom" years and, consequently, probably are spending less than they would if their housing-related wealth had not fallen with the housing market.



# HOUSING PRICES REMAIN UNDER DOWNWARD PRESSURE

Prices in Albemarle's housing market continue to face downward pressure as the result of an ongoing surplus in the supply of unsold homes. As a general rule of thumb, a residential real estate market is in equilibrium when a five or six month supply of unsold homes exists in that market. The term "equilibrium" means that prices are stable, with no tendency to rise or fall.

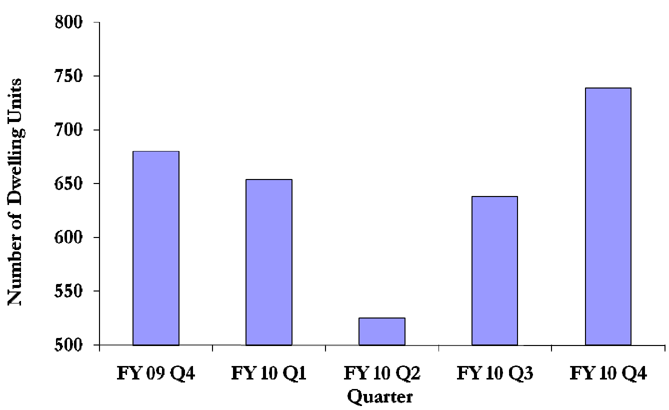
In the case of Albemarle County, as of the end of FY 10 Q4, there existed a 9.05 month supply of unsold single family detached dwelling units, compared with a 12.91 month supply in FY 09 Q4. Note that Q4 of FY 10 marked the end of the federal government's homebuyer tax credit; the decline in inventory from FY 09 Q4 to FY 10 Q4 might reflect buyers' "scrambling" to take advantage of the credit before the expiration date. The surplus of single family units for sale in FY 10 Q4 indicates that downward pressure on prices continues to exist in this segment of the housing market. Single family detached homes account for roughly two-thirds of the County's total housing stock, so this situation has broad implications for Albemarle.

In order to understand how this 9.05 month number is calculated, consider the information contained in Graphs I through III below. As shown on Graph I, in FY 10 Q4, there were 739 single family homes for sale in Albemarle. During this quarter, as shown on Graph II, an average of about 82 homes sold each month. These numbers mean that, at the rate at which homes sold during the quarter, it would have taken about nine months to sell all of the homes that were on the market, i.e., there was about a nine month supply of unsold inventory, as shown on Graph III.

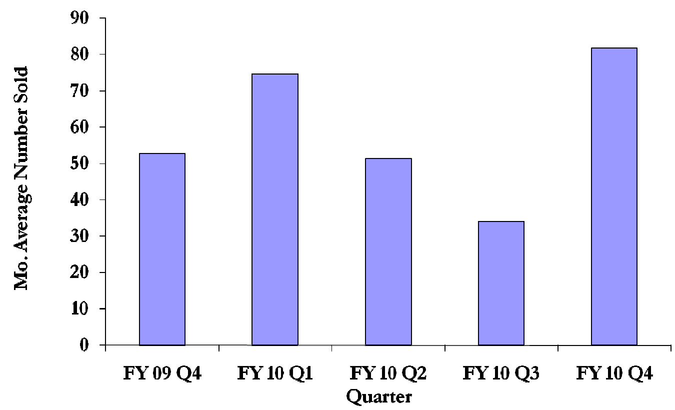
The downward pressure on home prices that persisted during the course of the past year is reflected in the Charlottesville MSA home price data shown in Graph IV, below. The U.S. Federal Home Finance Administration's Home Price Index (HPI) for the *region* declined by about 5% between FY 09 Q4 and FY 10 Q4. It is worth emphasizing, however, that this FHFA data includes outlying counties, not just Albemarle, and covers only purchases or re-financings in which conforming mortgages were involved.

These two quirks in the HPI numbers mean that (a) the data from the outlying counties, where the region's housing prices, according to local Realtors, have declined the most, might be influencing the regional index number disproportionately; and (b) the HPI numbers likely do not include a significant portion of sales or re-financings that took place in Albemarle County, since Albemarle tends to have a larger percentage of higher-end homes than do the outlying jurisdictions, and the sale or re-financing of higher-end properties in many cases involves the use of "jumbo" mortgages, rather than conforming mortgages.

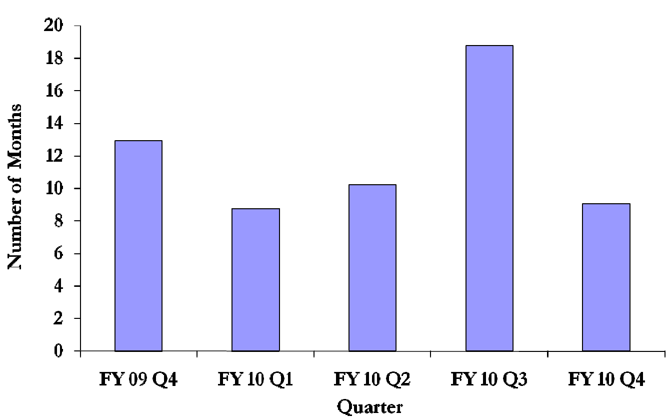
**Graph I -- Single Family Homes for Sale**



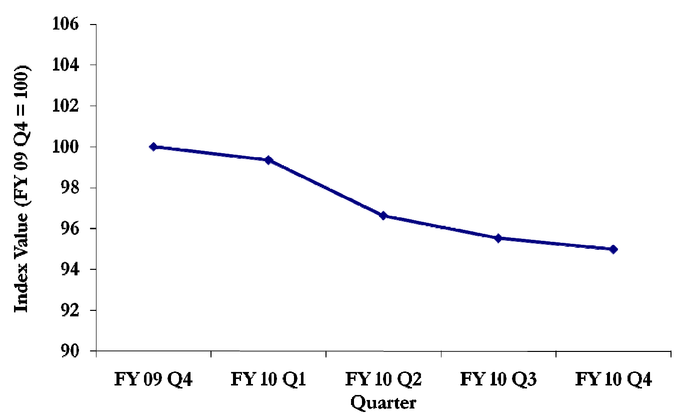

**Graph II -- Mo. Avg. No. of S. Family Homes Sold**




**Graph III -- Mos. Supply Unsold S. Fam. Homes**



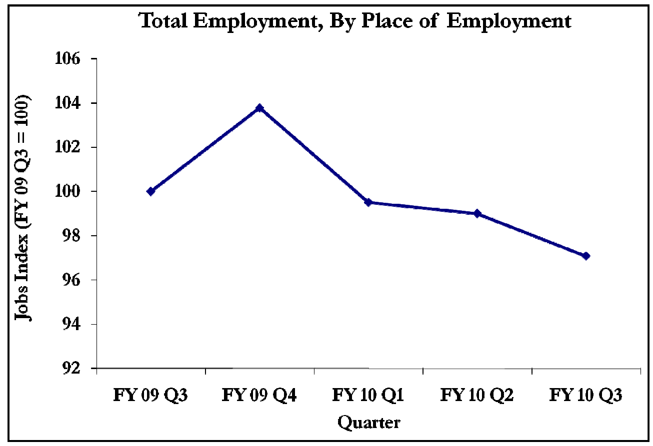

**Graph IV -- FHFA Price Index for the C-Ville MSA**



# TOTAL EMPLOYMENT FALLS, BUT FINANCE, REAL ESTATE GAIN

The Virginia Employment Commission produces data showing the total number of full- and part-time jobs in Albemarle County, by place of employment, but this data, unfortunately, is usually several quarters behind the most recent quarter and, consequently, does not provide as much timely information as does the VEC unemployment rate data, which is fairly current. According to the most recently available total employment numbers, between FY 09 Q3 and FY 10 Q3, the total number of jobs in Albemarle fell from 48,446 to 47,033 for a net loss 1,413 jobs, or about 3% of the employment base. An examination of the various employment sectors reveals that the retail trade and manufacturing categories experienced the largest drops in the *absolute number* of jobs. The net loss in the retail trade sector came to 440 jobs (8%), while the net loss in the manufacturing sector equaled 399 jobs (14.3%). The drop in retail trade employment is not surprising given that, during the time period in question, sales tax revenue in the County declined. (Note: Sales tax revenue has grown in subsequent quarters. Please see Tax Revenue story, page 2).

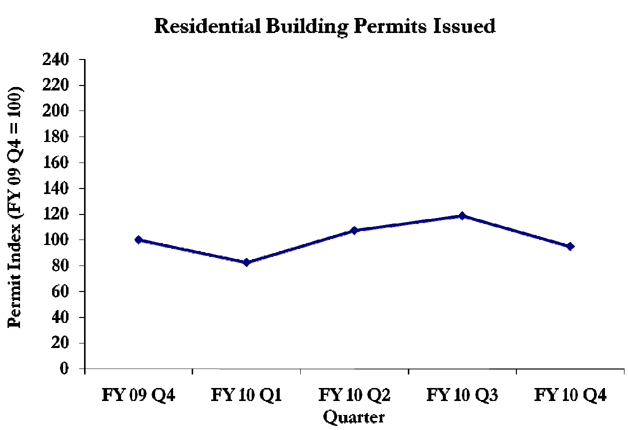
Other sizable employment categories that had large *percentage* losses included administrative & waste services (296 jobs, or 16.4%), agriculture (a loss of 46 positions, or 11.2%), and the construction sector (289 jobs, or 10.7%). Interestingly, two sectors that were at the root of the cause of the recession that began in FY 08 Q2 actually managed to *grow* between FY 09 Q3 and FY 10 Q3; the finance & insurance sector experienced a net gain of 55 positions (6.2%) while the real estate category had a net addition of 38 jobs (5.7%). These modest net gains between FY 09 Q3 and FY 10 Q3 suggests that the *worst* of the recession in the two sectors has passed, although real estate generally is not out of the woods yet (see New Construction story, below, and Housing Price story, page 3).

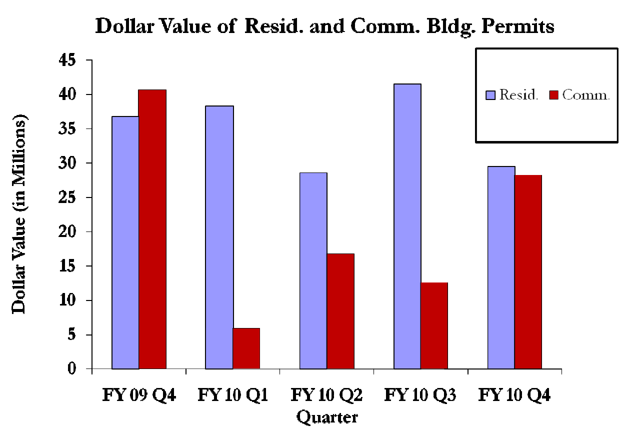



***"The fact that the finance & insurance and real estate categories were able to eke out modest net gains in employment between FY 09 Q3 and FY 10 Q3 suggests that the worst of the recession in these sectors has passed."***

# NEW CONSTRUCTION DROPS

The number of building permits issued, and the total dollar value of these permits, offers a decent, but not *perfect*, forward indication of the quantity and nature of new construction in the County. On the residential side of the market, the number of building permits issued between FY 09 Q4 and FY 10 Q4 dropped by 5%. According to the County's Department of Community Development, many of the building permits issued were for lower-end multifamily construction. The relative scarcity of new *single family home* building permits reflects a market response to the surplus of unsold single family detached inventory in the County's housing market (see story on Page 3). The total dollar value of residential permits issued also fell, by roughly 20% between FY 09 Q4 and FY 10 Q4. On the non-residential side, the dollar value of permits issued plummeted by about 30% between FY 09 Q4 and FY 10 Q4, which is not surprising, given that the commercial real estate sector in the U.S. remains distressed. According to the County Assessor's office, capitalization rates on commercial properties have been rising in recent quarters; this situation reflects declines in the underlying value of commercial properties. In this environment, other than some soon-to-be-completed hospital projects at UVA and Martha Jefferson, the County should not expect to see much new commercial building activity until existing inventory is absorbed.



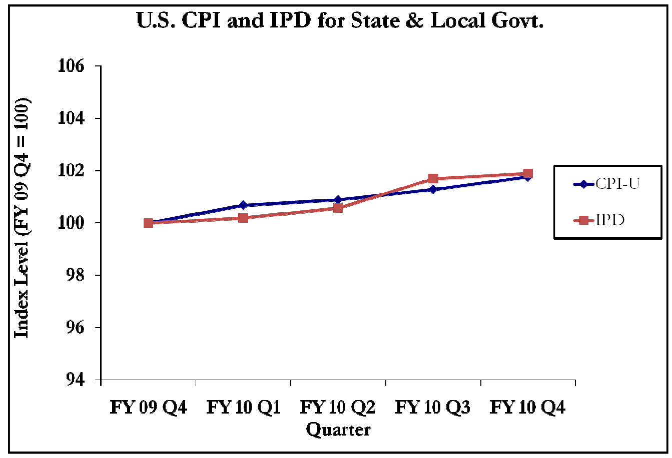



## U.S. PRICE INDICES POST MODERATE INCREASES

The U.S. Consumer Price Index (CPI) and the Implicit Price Deflator (IPD) for state and local governments rose slightly between FY 09 Q4 and FY 10 Q4. The increase in CPI came to 1.77%, while the rise in the IPD equaled 1.89%. The year-over-year increases in these indices seem to reflect a diminished prospect of price deflation. Potential price deflation has motivated the U.S. Federal Reserve to keep short-term interest rates at historically low levels, in order to stimulate demand for goods and services.

Although CPI and the IPD both measure changes in prices, the two indices track price changes in two different market baskets of goods and services. The Consumer Price Index pertains to goods and services that *households* are likely to purchase, while the Implicit Price Deflator pertains to goods and services that *state and local governments* are likely to purchase. Households, for example, might buy items such as diapers, and barber services, while state and local governments are more likely to buy things such as police radios and traffic lights. Clearly, there exists some overlap between the two market baskets; households, as well as state and local governments, buy products such as personal computers, pens, and motor vehicles.

The differences that exist in the two sets of market baskets, however, typically generate numbers that do not coincide with each other, especially in the long run. As shown on the graph, IPD increased by only slightly more than did the CPI between FY 09 Q4 and FY 10 Q4. At first glance this situation would seem to suggest that the two price indices move pretty much in tandem over time, but the cumulative impact of differences in annual rates of change can render large long-term gaps between CPI and IPD price levels. Between FY 05 Q4 and FY 10 Q4, for example, CPI increased by 12.1% while IPD for state and local government rose by 20.2%, or at a rate that was more than 66% higher than Consumer Price Index's rate of growth.



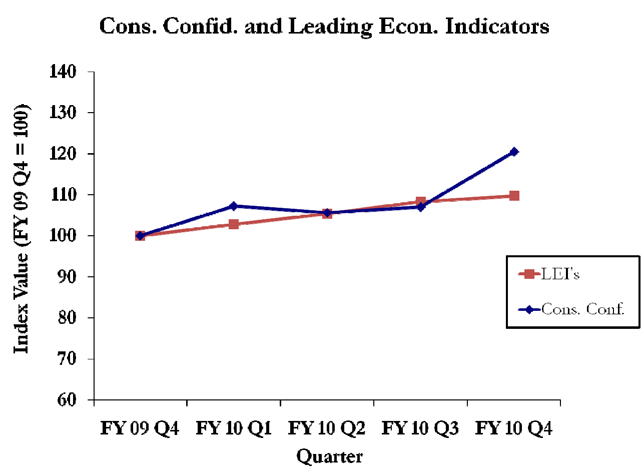

***"The Consumer Price Index (CPI) pertains to goods and services that households are likely to purchase, while the Implicit Price Deflator (IPD) pertains to goods and services that state and local governments are likely to purchase."***

## CONSUMER CONFIDENCE REBOUNDS; LEI'S GROW STEADILY

The Conference Board, a nonprofit organization that tracks business and economic trends, publishes a U.S. Consumer Confidence Index, as well as a set of U.S. Leading Economics Indicators (LEI's). The numbers in these data sets offer a general idea about the direction of U.S. macroeconomic trends and, by extension, Albemarle County's economic prospects.

Changes in consumer confidence should shadow changes in consumption. As shown in the graph, consumer confidence jumped by about 20% between FY 09 Q4 and FY 10 Q4. This dramatic increase coincided with growth in U.S. GDP between FY 09 Q4 and FY 10 Q4 (see story on page 6), and a rise in local consumption, as measure by the County's sales, meals, and hotel/motel tax revenues (see story on page 2).

The U.S. Leading Economic Indicators rose by about 10% between FY 09 Q4 and FY 10 Q4. The LEI's include items such as weekly manufacturing hours, interest rates, and orders for capital goods. Interestingly, the improvement in the LEI figures largely *outpaced* the growth in U.S. GDP that took place between FY 09 Q4 and FY 10 Q4. The 10% increase in the LEI's, along with the fact that the LEI's consistently rose between each of the quarters during this time period, suggests that the recovery might be somewhat stronger than has been anticipated.




***The sharp rise in consumer confidence between FY 09 Q4 and FY 10 Q4, along with consistently increasing Leading Economic Indicators during this time period, suggests that the U.S. economic recovery could be more robust than has been anticipated.***

## U.S. GDP expands by 3.85% during Q4-to-Q4 Period

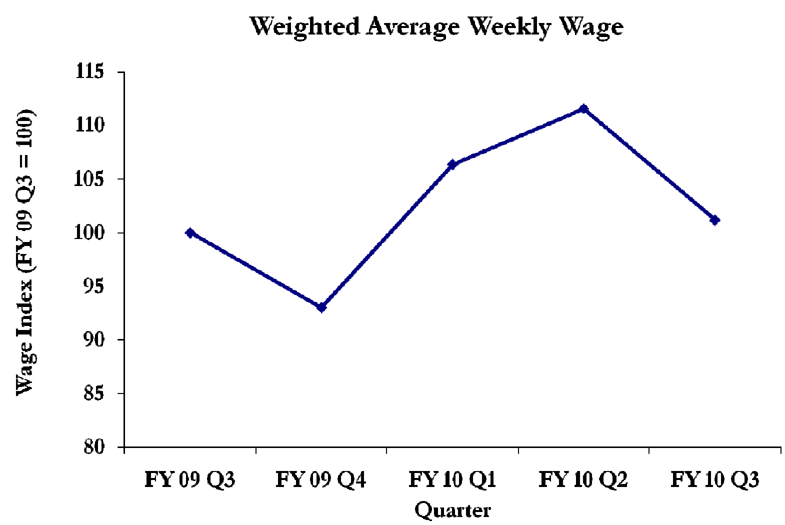
U.S. Gross Domestic Product (GDP) represents the total dollar value of all the goods and services produced within the United States. Between FY 09 Q4 and FY 10 Q4, U.S. GDP rose from $14.035 trillion to $14.575 trillion, or by 3.85%, apparently signaling the continuation of a recovery from the severe national recession that began in December of 2007. It is worth noting that U.S. GDP grew in each of the three quarters after FY 09 Q4. Many economists now think that the recovery has reached a self-sustaining phase, such that the phasing out of federal government stimulus efforts will not result in a "double dip" recession.

Despite this seemingly good news, two scenarios, either separately or together, could derail the recovery: (1) a sovereign default in one or more of the Euro Zone countries; and (2) an inflation-fighting, government-induced slowdown of China's economy. Even without these two scenarios, the question remains as to whether or not the current U.S. economic recovery will be sufficiently strong to bring down the country's unemployment rate in coming quarters.

Note that the U.S. Bureau of Economic Analysis (BEA), the entity that calculates U.S. GDP, also calculates a GDP figure for Virginia, as well as regional GDP data for the Charlottesville MSA, but this information is done only on an annual basis and is not completed until well after the end of the calendar year. This regional GDP data will be tracked annually by the County.

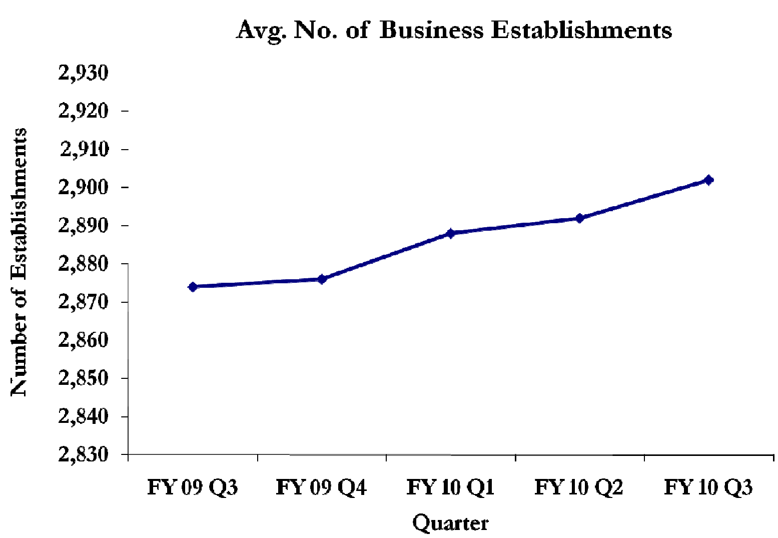
## Weighted average weekly wage rises slightly

The weighted average weekly wage gives a *rough* idea about changes in the earnings of the "typical" worker in Albemarle. The most relevant comparison involves the same quarter between years, since the weighted average weekly wage can be influenced by changes in seasonal employment. Between FY 09 Q3 and FY 10 Q3, the weighted average weekly wage rose by 1.18% in nominal terms, but this growth could have resulted from job losses in low-paying sectors, such as construction, rather than an improvement in wages. Given the fact that the County's unemployment rate remains elevated (see story, page 1), Albemarle should not expect to see strong growth in the weighted average weekly wage in quarters to come.




## Number of businesses is Relatively flat

Changes in the average number of businesses that exist in Albemarle in each quarter renders an approximate estimate of business formation in the County. The Virginia Employment Commission does not generate this data in a timely manner but, between FY 09 Q3 and FY 10 Q3, the number of businesses in Albemarle was essentially flat (going from 2,874 to 2,902 or an increase of just under 1%). This percentage change, although small, at least was in the right direction. Previously, between FY 08 Q3 and FY 09 Q3, Albemarle experienced *declines* in the number of businesses.



*Albemarle County is a community of 94,000 people, located 116 miles southwest of Washington, DC, and 72 miles northwest of Richmond. Founded in 1744, Albemarle surrounds the City of Charlottesville, and is the home of the University of Virginia, the University of Virginia Medical Center, and Thomas Jefferson's Monticello. The County's resident labor force of 52,000 is well-educated; 53% of the population aged 25 or older has at least a bachelor's degree. Industries that have expanded in Albemarle in recent years include biotechnology and national defense intelligence. The County's location at the intersection of Interstate 64 and U.S. Highway 29, the availability of air service to several major hubs from the Charlottesville/Albemarle Airport, and AMTRAK passenger rail service to the northeast corridor help support Albemarle's role as a transportation hub in Central Virginia. The County's natural beauty and historical importance, additionally, continue to attract visitors from around the world.*

**Please visit us on the web at www. albemarle.org**

*The Albemarle* Quarterly Economic Indicators *is published in the middle of February, May, August, and November by the Albemarle County Office of the County Executive, 401 McIntire Road, 4th Floor, Charlottesville, VA 22902. For additional information about this newsletter, please contact Steven A. Allshouse, Coordinator of Research and Analysis at (434) 296-5841 or at sallshouse@albemarle.org.*

## Summary & Analysis

The U.S. economy apparently has begun to recover from the severe recession that started officially in FY 08 Q2, and the incipient recovery bodes well for Albemarle. The National Bureau of Economic Research (NBER), the organization that designates the official beginning and end of business cycles, has not yet declared an end to the "Great Recession" but, from FY 09 Q4 onward, U.S. GDP has expanded each quarter [see story, page 6]. Note that the term "recovery" means that economic conditions are improving, while "full recovery" means that the economic activity has returned to the level that existed prior to the beginning of the recession.

The rise in GDP over the course of the past four quarters, although encouraging, might not be sufficient, by itself, for NBER to declare the recession officially over, although, as discussed below, the official designation likely will be made in the near future. (Note: Official designations typically take place well after the fact so, even if NBER decides that the recession did in fact end in FY 10 Q1, this pronouncement might not take place until, say, FY 11 Q1 or even later). The reason for this lag involves the fact that the NBER looks at many variables in order to reach a decision about changes in the business cycle. It is worth noting that total GDP already has *more* than recovered from recession. In FY 08 Q2, at the official beginning of the recession, total U.S. GDP stood at $14.291 trillion. By FY 09 Q4, GDP had contracted to $14.035 trillion but, by FY 10 Q4, the U.S. economy had grown to $14.579 trillion, a gain of $288 billion over the level that existed at the start of the recession.

In order to understand why an official designation of the end to the recession looks increasingly likely, realize that U.S. GDP is composed of four main pieces, and all of these pieces have begun to behave in ways consistent with an economic recovery. Between FY 09 Q4 and FY 10 Q4, personal consumption rose $365.3 billion, and government spending increased by $71.5 billion. Growth in these two segments of the U.S. economy had taken place in earlier quarters but, interestingly, government spending previously made up a much larger share of the combined increase than was the case several recent $Q_x$-$Q_x$ time periods. Another hopeful change involves private investment; this category jumped by $311.6 billion Q4-to-Q4, a dramatic increase from previous $Q_x$-$Q_x$ time periods. Net exports, which dropped $204.1 billion from FY 09 Q4 to FY 10 Q4 represented one dark spot in the GDP numbers, but the fact that *both* exports and imports *rose* during this time period (imports increased more than did exports, hence a drop in *net* exports) suggests that economic activity in the U.S. picked up.

Locally, Albemarle's quarterly indicators offer some glimmers of hope that the County's economy is recovering, albeit slowly. Meals tax revenues, hotel/motel tax revenues, and sales tax revenues all have risen form their year-ago levels, and this fact offers evidence that consumption, which is thought to be a major portion of the County's economy, is making a rebound [see story, page 2]. The unemployment rate remains elevated, however, and total employment has fallen [see stories, pages 1 and 4]. Net business establishment remains essentially flat [see story, page 6], and the weighted average weekly wage in Albemarle, although up, might have risen due to losses in lower-paying employment sectors [see "wage" story, page 6 and "total employment" story, page 4]. The County's housing market, meanwhile, remains problematic [see story, page 3], and nonresidential construction activity indicates continuing downward pressure on the County's commercial real estate sector [see story, page 4].