

DISTRICT ECONOMIC OVERVIEW

BY ROBERT LACY

Economic growth was relatively strong in most sectors of the Fifth District economy in the fourth quarter of 2004. The broad services sector expanded at a solid pace as ongoing gains in employment and income drove demand for services higher.

Housing markets were particularly strong; new home construction was well above the pace of a year earlier and home prices rose sharply in a number of District states. Manufacturing was a soft spot, however, as growth in shipments and new orders slowed and factory employment edged lower. Job growth was somewhat stronger in other sectors of the economy, though, pushing the District's unemployment rate down to 4.6 percent.

Services Sector Expands but Retail Soft

The Fifth District's services sector expanded at a brisk pace during the fourth quarter. Services firms generally reported solid revenue growth throughout the period. Retailers said merchandise sales growth was spotty early in the quarter, but improved in late December. Sales of automobiles and other big-ticket retail items, though, were soft throughout the quarter.

“The Fifth District economy continued to expand at a solid pace as 2004 came to a close.”

One of the District's largest retailers, Richmond, Va.-based Circuit City, continued to struggle in a difficult retail environment. In February, it announced the closing of 19 stores, mainly in the Midwest, in an effort to cut costs. A distribution center in Doswell, Va., will also be closed.

Manufacturing Growth Slows

In order to gauge developments in the manufacturing sector, the Richmond Fed now releases a composite manufacturing index. This index more broadly reflects activity in the sector by combining what manufacturers tell us about shipments, new orders, and employment. The composite index suggests that growth in manufacturing activity slowed substantially in the fourth quarter of 2004. The weaker readings were the result of lower index values for shipments, new orders, and employment during the quarter.

Reports of higher prices for raw materials were more in evidence among respondents in October and November. Steel, plastic, and natural gas were among those commodities most frequently mentioned as rising rapidly in price. But raw material price hikes eased toward the end of the year, and prices for finished goods rose only modestly.

District Job Performance Bests Nation's

We track monthly payroll employment numbers closely because these data are among the timeliest measures of economic performance available at the state level.

Fifth District payroll employment in the fourth quarter was 1.9 percent higher than a year earlier, a somewhat stronger growth rate than the 1.6 percent rate of the United States as a whole. Growth was above 2 percent in Maryland and Virginia, the two fastest-growing states in the District. By sector, employment growth continued to be centered in services.

House Prices Soar

House prices in the District of Columbia and in parts of Maryland and Virginia have skyrocketed over the last year. HUD's Office of Federal Housing Enterprise Oversight tracks state-level house prices on a quarterly basis. According to their statistics, prices in the District of Columbia in the third quarter of 2004 were 23 percent higher than a year earlier.

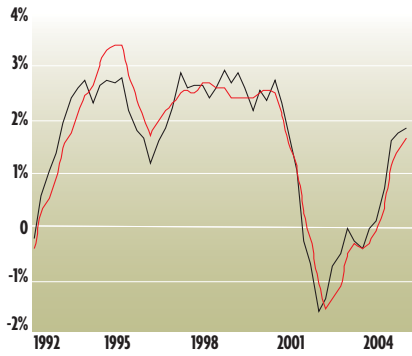
Increases in Maryland and Virginia were 19 percent and 16 percent, respectively. Prices in other Fifth District states rose at a more modest 5 percent to 8 percent pace during the period.

Economic Indicators

	4th Qtr. 2004	4th Qtr. 2003	Percent Change (Year Ago)
Nonfarm Employment (000)			
Fifth District	13,254	13,011	1.9
U.S.	132,294	130,168	1.6
Real Personal Income (\$bil)			
Fifth District	870.5	838.2	3.9
U.S.	9,152.4	8,794.2	4.1
Building Permits (000)			
Fifth District	53.4	49.8	7.1
U.S.	471.7	451.8	4.4
Unemployment Rate (%)			
Fifth District	4.6%	5.3%	
U.S.	5.4%	5.9%	

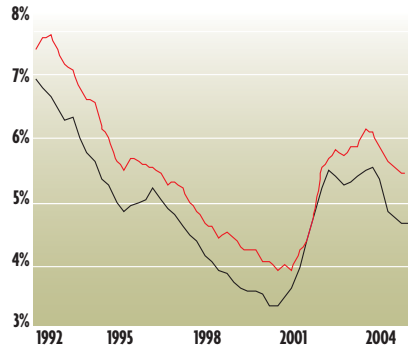
Nonfarm Employment

Change From Prior Year
First Quarter 1992 - Fourth Quarter 2004



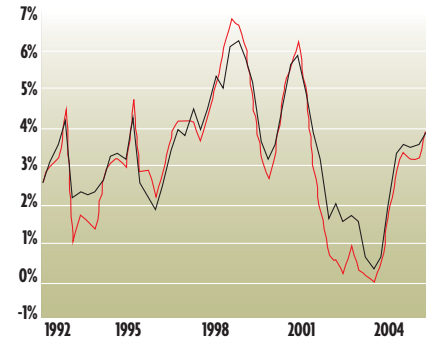
Unemployment Rate

First Quarter 1992 - Fourth Quarter 2004



Real Personal Income

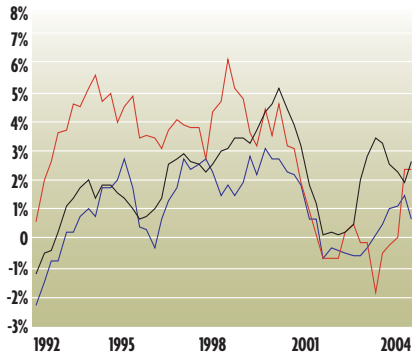
Change From Prior Year
First Quarter 1992 - Fourth Quarter 2004



— Fifth District — United States

Nonfarm Employment Metropolitan Areas

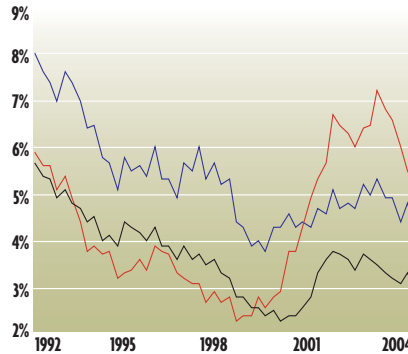
Change From Prior Year
First Quarter 1992 - Fourth Quarter 2004



— Baltimore — Charlotte — Washington

Unemployment Rate Metropolitan Areas

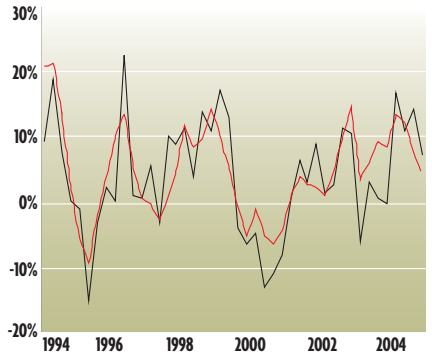
First Quarter 1992 - Fourth Quarter 2004



— Baltimore — Charlotte — Washington

Building Permits

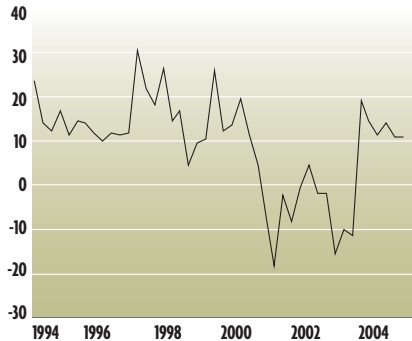
Change From Prior Year
First Quarter 1992 - Fourth Quarter 2004



— Fifth District — United States

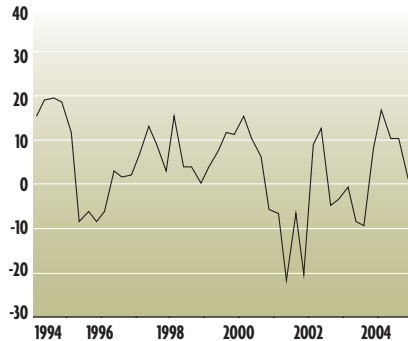
FRB—Richmond Services Revenues Index

First Quarter 1994 - Fourth Quarter 2004



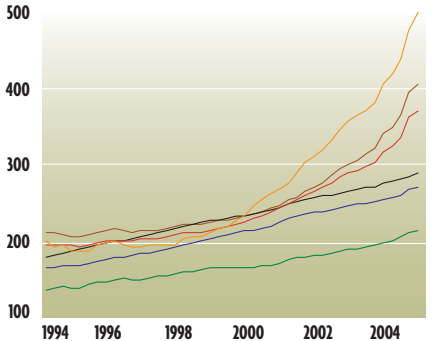
FRB—Richmond Manufacturing Composite Index

First Quarter 1994 - Fourth Quarter 2004



House Price Index

(1980 Q1 = 100)
First Quarter 1994 - Fourth Quarter 2004



— MD — VA
— NC — WV
— SC — DC

NOTES:

1) FRB-Richmond survey indexes are diffusion indexes representing the percentage of responding firms reporting increase minus the percentage reporting decrease. The manufacturing composite index is a weighted average of the shipments, new orders, and employment indexes.
2) Metropolitan area data and building permits are not seasonally adjusted (nsa); all other series are seasonally adjusted.

SOURCES:

Income: Bureau of Economic Analysis, U.S. Department of Commerce, <http://www.bea.doc.gov>.
Unemployment rate: LAUS Program, Bureau of Labor Statistics, U.S. Department of Labor, <http://stats.bls.gov>.
Employment: CES Survey, Bureau of Labor Statistics, U.S. Department of Labor, <http://stats.bls.gov>.
Building permits: U.S. Census Bureau, <http://www.census.gov>.
House prices: Office of Federal Housing Enterprise Oversight, <http://www.ofheo.gov>.

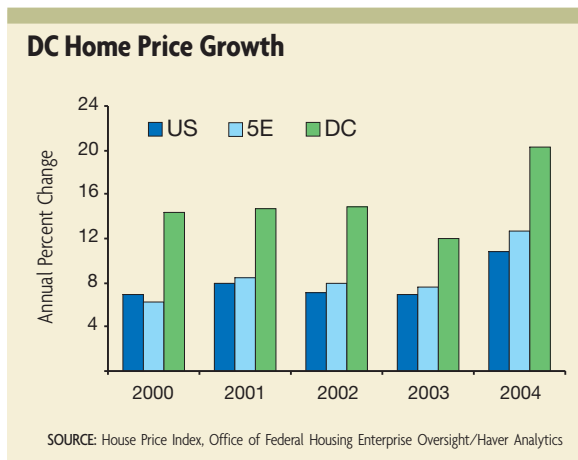
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STATE ECONOMIC CONDITIONS

BY ANDREA HOLLAND

District of Columbia

As 2004 drew to a close, business conditions in the District of Columbia continued to show improvement, but conditions of households softened. Businesses in the District of Columbia continued to tack on jobs in the fourth quarter. Payroll employment expanded 0.1 percent, marking five consecutive quarters of job growth. Among sectors, education and health services establishments led the gains, adding 4,300 jobs. By comparison,



construction posted the weakest performance, trimming 733 jobs. Looking ahead, the refurbishment of the RFK stadium and construction of a new major league baseball stadium are expected to create 900 new jobs later this year.

Other recent economic indicators also pointed to an upturn at businesses. Venture capital inflows into District of Columbia firms totaled \$38 million in the fourth quarter, the largest quarterly increase in three years.

Moving on, the financial conditions of households were mixed. The District of Columbia's unemployment rate edged up to 8.8 percent in the fourth quarter — the highest rate since the third quarter of 1998. On a more positive note, the number of unemployment benefits claimants decreased in the fourth quarter, following a slight uptick the quarter before.

Turning to the District of Columbia's real estate market, home prices reached an all-time high in the fourth quarter, standing 23.0 percent higher over the year. But sharply steeper prices didn't deter buyers — in excess of 18,000 homes were sold during the period, a new record. Underlying strength was apparent in readings on future construction as well. Fourth-quarter building permit authorizations were 3.6 percent above third-quarter levels.

News from the broadly defined Washington, D.C. MSA was more upbeat than in the District of Columbia

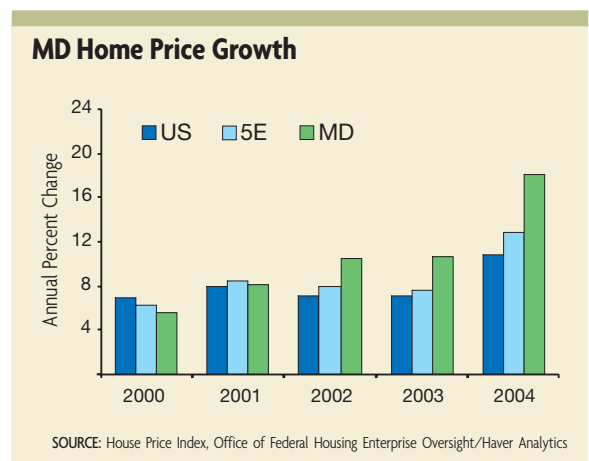
proper. Boosted by a surge in defense and homeland security spending and an improved outlook at high-tech related businesses, fourth-quarter payrolls expanded 4.1 percent and the unemployment rate dropped 0.3 percentage points to 3.0 percent.

Maryland

Barometers of Maryland's economic health were generally bright at the end of 2004. Businesses in the state continued to add jobs in the fourth quarter, marking two straight years of positive payroll growth. Gains came almost entirely from service-providing establishments — goods producers in the state trimmed jobs during the period.

Adding to the upbeat tone, venture capitalists infused \$236 million into Maryland businesses in the fourth quarter, almost tripling the third-quarter inflow and registering the largest gain in exactly three years. The most exciting news was that 38.5 percent of the funding went toward seed stage businesses, leading some analysts to suggest the beginning of a long-awaited pickup in investor confidence.

Financial conditions at Maryland households also brightened. Keeping with stronger payroll growth, the jobless rate fell 0.3 percentage points to 3.9 percent, remaining well below the national rate. In contrast, another indicator of labor force activity — initial jobless claims — inched higher in the fourth quarter, following three quarters of improvement.



Looking at real estate conditions in Maryland, residential activity remained on target, despite a blip in home sales. Sales of existing homes contracted 0.5 percent in the fourth quarter, making Maryland the only District state to record a slowdown during the period. Despite softer sales, home prices continued to increase with the

median-priced home now 18.6 percent more expensive than a year ago. Tracking sales activity, building permits also dwindled in late-2004, but remained 4.8 percent above a year earlier.

The Baltimore metro area economy continued to outperform the state as a whole. Payrolls rose by a solid 5.1 percent in the fourth quarter, and the jobless rate plummeted 0.5 percentage points to 4.3 percent. New construction activity in Baltimore outperformed other areas of the state — building permits jumped 73.5 percent from the third quarter. In other news, Baltimore's commercial real estate market continued to warm, albeit slowly. Fourth-quarter office and industrial vacancy rates came in below levels posted a year ago.



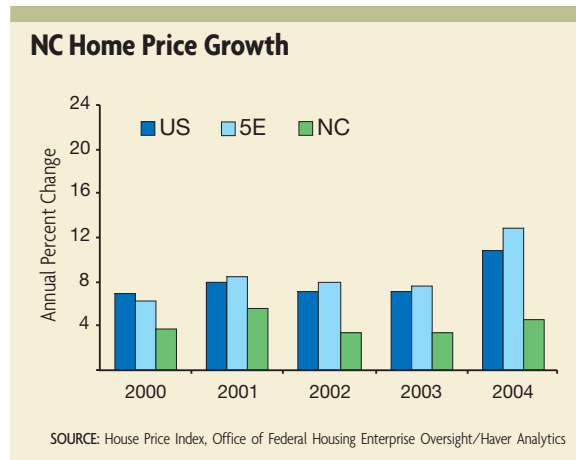
North Carolina

North Carolina's economy advanced steadily in the fourth quarter of 2004. Businesses in the state continued to expand hiring, causing payroll employment to expand by 1.3 percent in the fourth quarter — the third straight quarterly increase. By sector, job numbers picked up most at government and leisure and hospitality establishments. By comparison, job losses were greatest in the manufacturing sector, where the broader economic recovery has yet to fully establish itself.

In other business news, the latest numbers on venture capital investment were very encouraging. Fourth-quarter inflows totaled \$114 million — the largest quarterly injection in two years. The majority of the capital was slotted for expansion-stage and later-stage companies.

Household financial conditions remained steady. Despite the solid gain in payroll employment in late-2004, the unemployment rate remained fixed at 5.0 percent as nearly 10,000 new persons entered North Carolina's labor force over the period. On a less positive note, the number of state residents newly applying for unemployment benefits rose by 11.8 percent in the fourth quarter, the second straight increase.

Switching gears, North Carolina's housing market continued to gain strength in the fourth quarter. According to the latest data, home prices rose 6.1 percent in the fourth quarter. Residential realtors were kept on their toes — existing home sales stood 25.4 percent higher in the fourth quarter compared to a year earlier, marking the strongest annual growth rate districtwide. Indicators of future construction were not as robust. New building permits edged 3.0 percent lower in the fourth quarter, following a similar decline in the third quarter.



North Carolina's metro areas saw steady job growth in late 2004. In the fourth quarter, Charlotte and Raleigh-Durham posted payroll employment gains of 11.9 percent and 3.8 percent, respectively. Likewise, both metros saw a decline in their jobless rates. In real estate, new construction activity in Charlotte and Raleigh-Durham mirrored that of the state. Both posted a significant drop in new building permit authorizations.



South Carolina

Going into 2005, economic momentum was more evident in South Carolina than a year earlier. Business conditions in the state continued to improve. South Carolina added 4,176 jobs in the fourth quarter, reversing a modest third-quarter loss. By category, the leisure and hospitality sector displayed the most strength — payrolls increased by 15,267. By comparison, the largest loss was recorded in the professional and business services sector, where employment fell by 3,833.

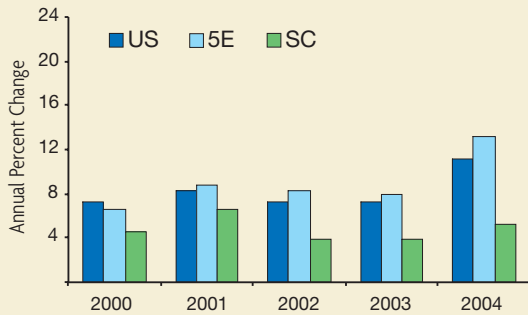
Adding to the positive tone on the business front, venture capitalists injected \$12.3 million dollars into South Carolina firms, the largest quarterly inflow since late

“Economic momentum was more evident in South Carolina than a year earlier.”

2002. Of this total, more than one-third of the venture funding went toward a business still in the start-up stage, possibly suggesting a pickup in investor confidence.

The latest data suggested that households in the state may also be experiencing a pickup in confidence — the number of job seekers increased by nearly 10,000 in the fourth quarter. Despite strong job gains, the sizable increase in the labor force pushed the unemployment rate up 0.2 percentage points to 6.6 percent. Initial claims for unemployment insurance in the fourth

SC Home Price Growth



SOURCE: House Price Index, Office of Federal Housing Enterprise Oversight/Haver Analytics

quarter rose by 16.2 percent but were attributed mainly to seasonal factors.

As in other Fifth District states, the median price for a South Carolina home continued to move higher last year, rising by 5.8 percent. And the evidence suggests that demand pulled prices higher. Fourth-quarter existing home sales were 15.4 percent higher over the year, marking the second strongest growth rate districtwide. Prospects for new construction remained on track — new building permits filed in the fourth quarter were significantly higher over the year.

Fourth-quarter activity in South Carolina's metro areas was mixed. Payroll employment expanded at a robust 6.4 percent rate in Columbia, but Charleston experienced a decline in job numbers — employment contracted 1.0 percent. New construction slowed in both metropolises in the fourth quarter, but as seen statewide, remained well above year-ago levels.

Virginia

Virginia's economic prospects continued to brighten as 2004 drew to a close. The state posted the District's strongest rate of job growth in the fourth quarter as well as the fifth strongest nationwide for all of 2004.

Fourth-quarter payrolls increased by 0.5 percent, or 4,500 jobs, marking the seventh straight quarter of positive job growth. Among major industries, government establishments created the most new jobs, while education and health services businesses cut the most positions.

Mirroring national activity, venture capital invest-

ment into Virginia businesses picked up in the fourth quarter. Capital inflows totaled \$73.8 million, nearly double the amount recorded in the third quarter. By stage of investment, nearly one-fifth of the funds were infused into seed and startup businesses.

Household conditions also remained on track in the fourth quarter. The jobless rate dropped 0.2 percentage points to 3.3 percent, despite an inflow of 11,300 job seekers into the labor market. And although the number of first-time claimants for unemployment insurance increased by 20 percent, the level remained below that of a year ago.

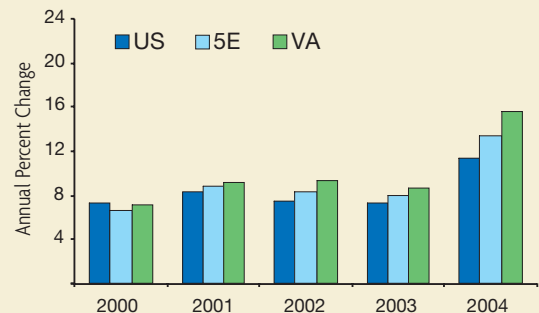
On the real estate front, the latest readings on home prices suggest that appreciation has continued to heat up. The state recorded a 10.5 percent jump in the fourth quarter alone. As in other states, the increases appear to result from strong demand growth, as illustrated by the 3.4 percent increase in fourth-quarter home sales. New construction, however, advanced at a more moderate pace. The number of building permits issued in the fourth quarter was somewhat below those recorded in the third quarter.

Economic activity in Virginia's metro areas also continued to look up, with businesses in the Norfolk and Richmond metro areas boosting payrolls by 4.3 percent and 3.0 percent, respectively. Much of Richmond's job growth was centered in education and health services — not a surprise since the city is home to several universities and research hospitals. According to a break-

down of the data, Norfolk's labor market was boosted by increased defense and homeland security spending. In line with strengthening labor markets, the jobless rate posted healthy declines in both areas.

“In Virginia, government establishments created the most new jobs.”

VA Home Price Growth



SOURCE: House Price Index, Office of Federal Housing Enterprise Oversight/Haver Analytics



West Virginia

West Virginia businesses trimmed jobs in the final quarter of 2004 — the only Fifth District state to do so — suggesting that the economic expansion may not have been firmly entrenched in 2004.

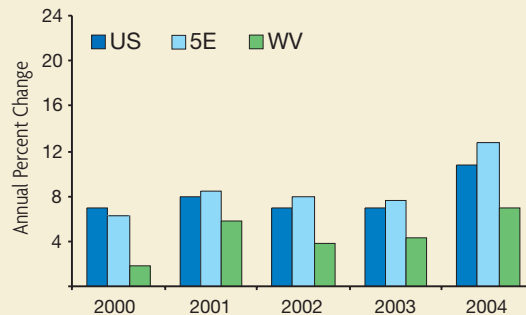
Compared to states across the nation, West Virginia ranked 41st in terms of job growth in 2004. Fourth-quarter payroll numbers slipped 1.7 percent, with reductions sprinkled across establishments on the services side of the economy. In contrast, West Virginia goods producers added jobs during the quarter.

Other business news was more upbeat — venture capital investment into West Virginia businesses totaled \$5.3 million in the fourth quarter, following flat inflows in the third quarter. Also positive, nearly 60 percent of the inflows were targeted toward firms in the startup stage.

Moving on, the bounceback at West Virginia households has also been slow to take hold. Mirroring payroll activity, West Virginia was the only District jurisdiction to record a contraction in the labor force in the fourth quarter. The downsizing of the labor market helped facilitate the 0.3 percentage point decline in the jobless rate, despite falling payroll numbers. Also less encouraging, initial claims for unemployment insurance rose in the fourth quarter, reversing three consecutive periods of improvement.

One bright spot of West Virginia's economy in recent years has been real estate, driven in part by historically

WV Home Price Growth



SOURCE: House Price Index, Office of Federal Housing Enterprise Oversight/Haver Analytics

low mortgage rates and relatively affordable housing. Fourth-quarter home prices expanded at a healthy rate, by 7.6 percent. Some of the price increase likely stemmed from playing catch up with surrounding states, as West Virginia home prices remain the lowest districtwide. Affordable prices have apparently attracted homebuyers, though — sales of existing housing units rose by 4.0 percent in the fourth quarter.

Economic activity was a bit more upbeat in the Charleston metro area than in other areas of the state. Payrolls in that area continued to move higher, rising 0.6 percent in the fourth quarter. In line with the improvement in hiring activity, Charleston's jobless rate fell 0.1 percentage points to 4.1 percent.

Behind the Numbers

Maryland added 52,300 to the ranks of the employed in 2004, according to the Labor Department. No wait — make that 63,800, according to the, er, Labor Department.

What gives? The problem is a simple discrepancy between two sets of government-generated numbers: the so-called “payroll” and “household” surveys, from which monthly U.S. job statistics are derived. The payroll survey produced the 52,300 employment growth figure mentioned above, while the household survey came up with the 63,800 number. Sometimes, the differences between the two studies can be even more significant.

In general, economists consider the payroll survey more reliable. Here's why.

The payroll survey, also called the “Establishment Series,” is based on reports from a sample of about 400,000 businesses, covering about a third of nonfarm employment.

By comparison, the household survey uses a sample of 60,000 homes.

One other key difference is that the payroll survey asks firms how many employees they have, while the household survey asks people whether they have jobs. For that reason, some economists say the household survey may be more effective in capturing the number of self-employed people in the economy as well as in predicting job growth.

Still, “it's clear the payroll survey is the preferred survey for judging changes in business conditions in the near term,” says Roy Webb, an economist at the Federal Reserve Bank of Richmond. He adds that, shortcomings notwithstanding, the household survey enjoys broad support from economists as another tool in their analysis kit. “As an economic analyst, I always think more data is better,” Webb says.

— DOUG CAMPBELL

State Data, Q4:04

	DC	MD	NC	SC	VA	WV
Nonfarm Employment (000)	672.3	2,538.7	3,874.9	1,839.0	3,595.5	733.4
Q/Q Percent Change	0.1	0.5	1.3	0.9	0.5	-1.7
Y/Y Percent Change	1.2	2.1	1.8	1.4	2.2	1.5
Manufacturing Employment (000)	2.5	144.2	576.5	269.8	295.0	63.4
Q/Q Percent Change	0.0	-0.5	-3.9	-0.9	-0.5	0.0
Y/Y Percent Change	-2.6	-0.5	-2.2	-1.5	-0.7	-0.9
Professional/Business Services Employment (000)	146.9	370.9	447.5	188.7	581.5	56.5
Q/Q Percent Change	3.0	-3.3	3.3	-7.7	0.3	-3.7
Y/Y Percent Change	3.4	3.0	5.4	0.3	4.7	0.3
Government Employment (000)	231.9	462.7	664.2	336.0	660.3	142.3
Q/Q Percent Change	-0.4	-2.8	6.0	1.7	3.9	-4.9
Y/Y Percent Change	0.5	0.7	1.6	1.2	2.9	1.0
Civilian Labor Force (000)	307.8	2,956.9	4,187.6	2,082.0	3,853.5	801.0
Q/Q Percent Change	9.2	0.6	0.9	1.8	1.2	-0.8
Y/Y Percent Change	2.3	1.7	-1.6	3.3	1.8	2.7
Unemployment Rate (%)	8.8	3.9	5.0	6.6	3.3	5.0
Q3:04	7.8	4.2	5.0	6.4	3.5	5.3
Q4:03	7.0	4.5	6.3	6.9	3.9	5.7
Personal Income (\$bil)	27.0	205.4	236.0	107.5	250.2	44.3
Q/Q Percent Change	1.6	1.6	1.5	1.3	1.7	1.7
Y/Y Percent Change	3.9	3.6	3.5	3.1	4.6	4.1
Building Permits	347	7,211	20,382	10,677	13,669	1,082
Q/Q Percent Change	15.1	-11.5	-49.2	-5.2	-48.4	-70.3
Y/Y Percent Change	298.9	4.8	4.8	30.0	-2.8	-3.9
House Price Index (1980=100)	496.2	403.4	289.3	270.7	369.3	215.2
Q/Q Percent Change	19.9	9.8	6.1	5.1	10.5	7.6
Y/Y Percent Change	23.0	18.6	5.2	5.8	16.4	8.0
Sales of Existing Housing Units (000)	18.1	153.4	375.1	176.4	210.1	39.3
Q/Q Percent Change	19.1	-0.5	4.4	4.7	3.4	4.0
Y/Y Percent Change	8.4	10.1	25.4	15.4	13.1	14.2

NOTES:

Nonfarm Employment, thousands of jobs, seasonally adjusted (SA); Bureau of Labor Statistics (BLS)/Haver Analytics, Manufacturing, thousands of jobs, SA; BLS/Haver Analytics, Professional/Business Services, thousands of jobs, SA; BLS/Haver Analytics Government, thousands of jobs, SA; BLS/Haver Analytics, Civilian Labor Force, thousands of persons, SA; BLS/Haver Analytics, Unemployment Rate, percent, SA; BLS/Haver Analytics, Personal Income, billions of chained 2000\$, Bureau of Economic Analysis/Haver Analytics, Building Permits, number of permits, NSA; U.S. Census Bureau/Haver Analytics, House Price Index, Office of Federal Housing Enterprise Oversight/Haver Analytics, Sales of Existing Housing Units, thousands of units, SA; National Association of Realtors®

Metropolitan Area Data, Q4:04

	Washington, DC MSA	Baltimore, MD MSA	Charlotte, NC MSA
Nonfarm Employment (000)	2,937.2	1,282.3	856.6
Q/Q Percent Change	4.1	5.1	11.9
Y/Y Percent Change	2.7	2.0	2.8
Unemployment Rate (%)	3.0	4.3	5.2
Q3:04	3.3	4.8	5.5
Q4:03	3.3	4.9	6.8
Building Permits	7,866	2,884	4,642
Q/Q Percent Change	-57.9	73.5	-61.2
Y/Y Percent Change	2.1	-5.8	3.2

	Raleigh, NC MSA	Charleston, SC MSA	Columbia, SC MSA
Nonfarm Employment (000)	703.3	266.7	307.5
Q/Q Percent Change	3.8	-1.0	6.4
Y/Y Percent Change	2.3	2.4	2.3
Unemployment Rate (%)	3.2	4.3	4.1
Q3:04	3.3	4.6	4.3
Q4:03	4.2	4.5	4.0
Building Permits	3,099	2,059	1,649
Q/Q Percent Change	-45.3	-29.5	-23.6
Y/Y Percent Change	-5.8	22.3	44.3

	Norfolk, VA MSA	Richmond, VA MSA	Charleston, WV MSA
Nonfarm Employment (000)	750.4	575.1	134.5
Q/Q Percent Change	4.3	3.0	0.6
Y/Y Percent Change	1.2	1.5	0.5
Unemployment Rate (%)	4.0	3.7	4.1
Q3:04	4.4	4.2	4.2
Q4:03	4.1	4.0	4.2
Building Permits	2,621	2,127	68
Q/Q Percent Change	44.4	-40.3	-76.8
Y/Y Percent Change	-16.8	-1.1	4.6

For more information, contact Andrea Holland at 804-697-8273 or e-mail Andrea.Holland@rich.frb.org.