



## Third Quarter – 2015

An independent economic analysis of Arkansas' three largest metro areas:

- Central Arkansas
- Northwest Arkansas
- The Fort Smith region

### About The Compass

The Compass Report is managed by Talk Business & Politics. The Fort Smith analysis is sponsored by Arvest Bank. Economist Jeff Collins compiles the data and provides analysis.

## REGIONAL SUMMARIES

### Fort Smith region

The Compass Report for the Fort Smith area posted a C- grade for the second quarter, down from the B in the first quarter of 2015 and down from the C in the second quarter of 2014.

Fort Smith's metro economy was not able to build on gains seen in the first quarter. Although the region's jobless number declined (5.9% in June 2015, compared to 6.3% in June 2014), the number of jobs fell. Non-farm employment in the metro area peaked at 113,500 in the first quarter, but ended June at 112,600. That is down from a second quarter 2014 peak of 113,600 and June 2014 at 113,300 jobs.

### Northwest Arkansas

The pace of job growth, tax revenue gains and building activity produced a not surprising grade of B+ for the Northwest Arkansas economy during the second quarter. The grade was up from a B grade in the first quarter of 2015 and better than the B in the second quarter of 2014.

Nonfarm employment grew rapidly June-on-June. The metro economy added roughly 5,600 job, up 2.5%. Also, improved construction activity has translated into improved employment in the sector. Since the height of the recession when sector employment fell to a little more than 7,000 jobs, the sector has grown by approximately 20%.

### Central Arkansas

Economic conditions in central Arkansas, the state's largest metro area, received a grade of C+ in the second quarter, unchanged from the first quarter of 2015 and better than the C in the second quarter of 2014.

Overall job gains, especially in the construction and tourism sectors, and stability in sales tax revenue helped the region to continue gains from the first quarter. There were 352,800 non-farm jobs in the region in June, ahead of the 346,700 in June 2014.

There were an estimated 18,600 construction jobs in the region during June, well ahead of the 16,100 in June 2014. The tourism sector posted 34,500 jobs in June, better than the 33,300 in June 2014.

# Regional "Takeaways"



## FORT SMITH REGION

(July-September 2015 conditions)

Nonfarm employment was down 0.6% September-on-September (700 new jobs), with total nonfarm employment an estimated 112,900 jobs in September compared to 113,600 in September 2014.

Comparing quarter-on-quarter data, nonfarm employment in the metro was essentially unchanged. Since the first quarter of the year non-farm employment growth has been relatively weak. The September total number of employed in the MSA was an estimated 114,553. By contrast, total employment in September 2006, prior to the recession, was 125,426.

Examining labor force data, there were 120,946 people either employed or looking for work in September 2015. By comparison, in September 2014, 119,267 people fit that description. This is an increase of roughly 1.4%.

September-to-September the manufacturing sector lost 200 jobs or roughly 1.1%. In September 2015 an estimated 17,800 people worked in the sector. Despite stabilizing earlier in the year, manufacturing appears to be shedding employment one again.

While overall nonfarm employment declined, three service sectors had increased employment September-to-September. Professional and business services (600), education and healthcare services (300), as well as other services (300) increased September-on-September. Service sectors losing employment include trade, transportation, and utilities (-300) and leisure and hospitality services (-600).

In addition to the service sectors mentioned, natural resources, mining, and construction employment also declined (-800). Financial services, government services, and information services were unchanged according to the data.

Residential construction as measured by number of permits was down but as measured by value up significantly quarter-on-quarter (-35% and 22% respectively).

Sales and use tax revenues, reported by the Arkansas Department of Finance and Administration, were off slightly quarter-on-quarter 0.26 percent after adjusting for the increased rate in Crawford County. Collections were particularly strong in July.

Despite weak jobs data, the unemployment rate in the Fort Smith area September-on-September was down 0.3%. The reason for the decrease was a significant increase in the number of employed (2,023) relative to the increase in the labor force (1,679).

Data for the Fort Smith regional economy had been mixed for some time. The obvious conclusion is that the region has been significantly impacted by structural changes in

the U.S. economy. Specifically, despite rebounding output in the manufacturing sector employment has not returned to previous levels.

Driven by weak exports, increasing automation, and relatively cheap production costs off-shore the near-term and long-term trend for employment in the sector is negative. Barring some unforeseen factor, the metro area economy is likely to struggle for some time.

## **NORTHWEST ARKANSAS**

(July-September 2015 conditions)

Nonfarm employment grew at a solid rate September-on-September. The metro economy added roughly 3,800 jobs. This was an increase of 1.7%.

Looking at construction related data for the metro, the number of building permits in the third quarter for Northwest Arkansas were roughly 187% of the total for Q3 2014. However, the valuation of permits was 164% of Q3 2015.

Improved construction activity has translated into improved employment in the sector. Since the height of the recession when sector employment fell to just over 7,000 jobs, the sector has grown by approximately 21%. September-on-September the sector was unchanged despite strong permit activity and trend growth. Based on permit data the sector employment is likely to grow in the coming quarters.

Sectors that added jobs September-on-September were: trade, transportation, and utilities (2,000), education and health services (1,000), government (600), leisure and hospitality services (500), and financial services (200). Professional and business services (-200) lost employment September-on-September. Sectors unchanged during the period were manufacturing and natural resources, mining, and construction.

Growth in leisure and hospitality services was exceptionally strong growing at 5.8% September-on-September.

The unemployment rate in Northwest Arkansas was the lowest in the state amongst all MSAs in September (3.5%). It was almost a percentage point lower than that for the Little Rock/North Little Rock/Conway MSA (4.4%). The highest rate in the state was the Pine Bluff MSA at 7%. To add perspective, of the 387 MSAs in the country, only 2 posted rates above 10% while 19 had rates below 3%.

The labor force grew September-on-September in Northwest Arkansas by roughly 2.7%. By comparison, the labor force grew in Central Arkansas 3.1%. In the Fort Smith area the labor force grew a more modest 1.4%.

Sales and use tax collection data indicate that Bentonville, Fayetteville, Springdale, and Rogers have experienced solid growth quarter-on-quarter. In percentage terms, Bentonville experienced the strongest growth in collections (24%) while Fayetteville collected the most tax dollars of any of the four major municipalities (\$10.5 million in the third quarter).

Strong growth is expected to be the norm in Northwest Arkansas for the foreseeable future.

## **CENTRAL ARKANSAS**

(July-September 2015 conditions)

The unemployment rate for Central Arkansas peaked in January 2011 at 8% but has improved since, estimated at 4.4% in September. Comparing to September of last year, the metro area unemployment rate has fallen 0.8%.

Nonfarm employment added 6,400 jobs, or 1.8% since, September 2014. By comparison, the Northwest Arkansas regional economy grew at a slower rate (1.7%) but added fewer new jobs (3,800). The Fort Smith regional economy lost roughly 700 jobs or down 0.6% during the same period.

Government services and trade, transportation, and utilities comprise the two largest sectors of the Central Arkansas economy. September-on-September government services was up slightly (200 jobs) while trade, transportation, and utilities lost 1,100 jobs or 1.6%.

Other sectors gaining employment were leisure and hospitality services (2,500), natural resources, mining, and construction (2,100), education and health care services (1,500 jobs), professional and business services (400), financial services (300 jobs), other services (300), and manufacturing (200). Information services employment was unchanged September-on-September. The sector with the greatest percentage increase was natural resources, mining, and construction (12.5%).

Looking at the construction sector, building permit data revealed solid activity for the quarter. Expectations are the sector should add employment in the coming months but at a slower rate for the next several quarters.

Interestingly, despite the relatively larger size of the Central metro area, there were 118 more building permits issued in the Northwest Arkansas metro (1,082 vs. 1,220). The discrepancy was even more pronounced looking at permit valuation. The value of permits in the Central Arkansas metro was roughly \$98.4 million for the quarter versus \$242.8 million for Northwest Arkansas.

Comparing the most recent three month period to the same period for the previous year, sales and use tax data indicates that retail activity grew for the metro area by approximately 3.3%. Perry County had the fastest growth rate (20.8%). Collections were up quarter-on-quarter in all three major metros.

Weak growth in the government sector aside, the Central Arkansas metro has performed reasonably well coming out of the recession. The declining unemployment rate and growth in non-farm employment are positive signs the region has returned to trend. Given the size and over-all importance of the metro to state economy, a return to trend growth is very positive news.

## **THE NATIONAL ECONOMY**

(July-September 2015 conditions)

Low oil prices are like a tax holiday for the consumer. Most industry analysts expect low prices to continue into the foreseeable future, particularly given slowing growth in China and weakness in the EU.

Unrest in the Middle East poses the greatest risk to low petroleum prices.

The strong dollar has made imports relatively cheaper and exports more expensive, negatively impacting U.S. GDP growth.

Improvement in the national unemployment rate has finally reached a point which corresponds to upward pressure on wages. The unemployment rate stood at 5.3% at the end of the third quarter. Of the 387 MSAs in the country, only 2 posted rates above 10% in September and 2 had rates below 3%. No Arkansas MSA had a rate above 8%.

The Fed has finally begun to inch the short-term interest up from essentially zero. The current target range is  $\frac{1}{4}$  to  $\frac{1}{2}$  percent. The justification for the increase seems to be the move is pre-emptive and that the economy was strong enough to absorb the modest increase.

Business investment had been one of the bright spots for the national economy. Although recent data indicate investment spending slowed recently, the outlook is for spending to accelerate through 2016.

Non-farm employment has grown for the last 20 quarters. The economy created roughly 576,000 non-farm jobs in the third quarter after creating 692,000 in the second quarter. Consumer demand continues to expand. Real personal consumption expenditures grew by 3% in the third quarter compared to an increase of 3.6 percent in the second quarter.

Federal government expenditures, which had been steadily declining, grew in the second and third quarters.

Employment growth at both the national and state level has been and will continue to be relatively strong in the services. Manufacturing continues to be weak throughout the state.

Demand for housing has also rebounded due to latent demand, low mortgage interest rates, and renewed lending. With the memory of the recession still fresh in the minds of many, the Northwest Arkansas market appears over-heated to some observers. Absorption of new inventory needs to be closely monitored for signs the market is over-built.

According to the Bureau of Labor Statistics, the Consumer Price Index decreased at a seasonally annualized rate of 0.2% in September. The decrease was driven by lower energy prices. This was partially offset by rising food, shelter, and medical care prices. Automobile prices also declined. The lack of inflationary pressure has allowed short and long-term interest rates to remain at or near historic lows. Short-term rates are expected to remain low for the foreseeable future as long as inflation remains below 2%.

Long-term interest rates remain low and have actually declined relative to rates at the end of 2013. For example, the 10-year Treasury Constant Maturity rate was below 2% throughout 2012 but had subsequently risen over time reaching 2.9% in December 2013. In September 2015 the rate stood at 2.09%. Further propelling the housing recovery the 30-year Conventional Mortgage rate was below 4% percent for the same period until rising to a peak of roughly 4.4% in January. The rate has since retreated, standing at 3.86% in September.

Incomes and employment are expected to grow modestly in the near-term. Housing, however, is expected to continue to accelerate given positive market conditions.

#### RISKS TO THE ECONOMY

The U.S. economy is being driven by the consumer. Consumer confidence has improved significantly but international crisis could induce consumers to pull back. This is particularly true to the extent that international events impact the equity markets.

Globally, growth has softened as regional economies in Asia and Europe struggle. This has impacted demand for U.S. goods abroad and stimulated demand in the U.S. for imports as the dollar strengthens against other currencies.

There are significant structural challenges to the Chinese economy which must be addressed to create stability and a sound basis for a return to growth. Unfortunately short-term imperatives make those changes extremely difficult.

While the unemployment rate has improved, it does not adequately tell the entire story. Reduced labor force participation, high unemployment rates for young and minority workers remain persistent problems.

Income growth is perhaps a truer signal that labor markets are finally returning to normal.

The Federal Reserve has significantly reduced monetary stimulus in response to stabilized growth. However many economists continue to be concerned about the impact on inflation of prolonged easy money.

The Fed took pre-emptive action, raising the Fed Funds target rate from 0% to 0.25% percent to 0.25% to 0.5%. While negligible, this does signal a change in Fed outlook.

Low oil prices are like a tax break, and are unlikely to increase anytime soon barring significant unrest in oil producing countries.