Burgundy Book

A report on economic conditions in the Little Rock zone

Fourth Quarter 2013

The Little Rock zone of the Federal Reserve comprises the majority of Arkansas, except northeast Arkansas. The total population is approximately 2.5 million people, including the 710,000 who live in the Little Rock MSA.

Business Contacts Express Optimistic Outlook for 2014

By Kevin L. Kliesen, *Business Economist and Research Officer*

A November survey of business contacts in the Little Rock zone revealed modest optimism about the strength of the economy in 2014. Two-thirds of those surveyed expected economic conditions to be better or somewhat better next year.

Bolstered by healthy growth of private-sector employment, labor market conditions in the third quarter improved in three of four MSAs in the Little Rock zone. The zone's unemployment rate in the third quarter averaged 7.1 percent, about unchanged from the previous quarter. Arkansas's economy has benefited from a burst of manufacturing exports that has outpaced that seen nationally.

Residential housing market conditions were mixed in the third quarter, as single-family building permits fell in most areas, but home sales rose sharply in Little Rock. House prices remain on an upward trajectory in most areas, though continuing at a slower rate than that seen nationally.

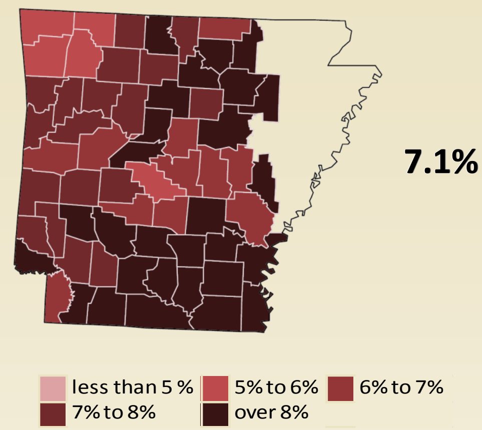
Similar to the nation, households in the Little Rock zone continued to reduce their outstanding debt—both mortgage debt and credit card balances. Delinquency rates on credit card debts are now below pre-recession levels.

Boosted by rising net interest margins and improving loan quality, Arkansas banks continue to be, on average, significantly more profitable than their U.S. peers.

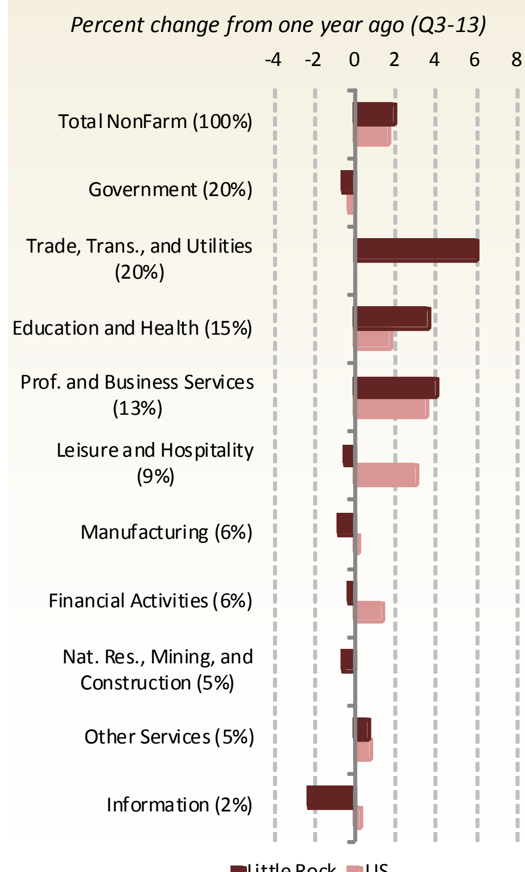
Arkansas's corn and soybean production was expected to be sharply higher in 2013, while cotton and rice production was expected to decline markedly compared with 2012.

Data Snapshot

County unemployment rates (SA, Q3-13)



Nonfarm payroll employment by industry



This report is published by the Federal Reserve Bank of St. Louis

How to read this report

Unless otherwise noted, **city names** refer to the metropolitan statistical areas (MSAs), which are geographic areas that include cities and their surrounding suburbs, as defined by the Census Bureau.

Statistics for the Little Rock zone are based on data availability and are calculated as weighted averages of either the 62 counties in the zone or the six MSAs. As of 2012, approximately 74 percent of the zone's labor force was located in an MSA. Specifically: 29 percent in Little Rock, 20 percent in Fayetteville, 11 percent in Fort Smith, 6 percent in Texarkana, 4 percent in Pine Bluff, and 4 percent in Hot Springs; 26 percent of the zone's labor force was located in non-metropolitan areas.

Arrows in the tables are used to identify significant trends in the data. The direction of the arrow indicates the sign (up/down) and the color indicates the economic significance (green = good, red = poor). Arrows appear only when the change from the previous quarter is greater than 1 standard deviation. For example, the standard deviation of the change in the U.S. unemployment rate is 0.4 percent. If the U.S. unemployment rate declined from 8.4 percent to 8.2 percent, no arrow would appear; but if it declined from 8.4 percent to 7.9 percent, a green down arrow would appear in the table.

Selected **variable definitions** are located in the appendix.

Selected quotes from business contacts are generally verbatim, but some are lightly edited to improve readability.

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Join our Panel of Business Contacts

The anecdotal information in this report was provided by our panel of business contacts, who were surveyed between November 1 and November 15.

If you're interested in becoming a member of our panel, follow this link to complete a trial survey:

http://research.stlouisfed.org/beigebooksurvey/

Or email us at beigebook@stls.frb.org.

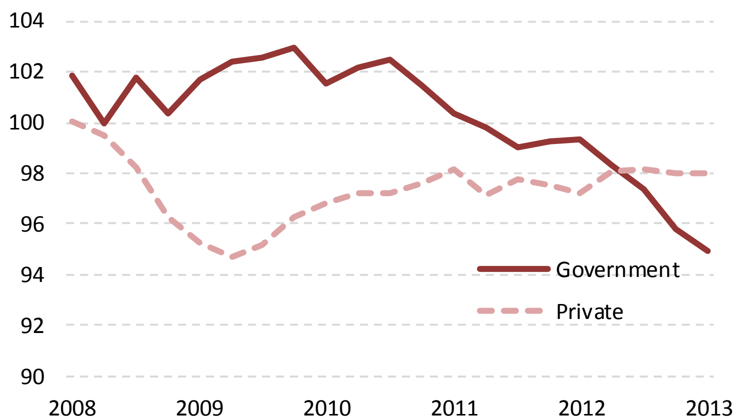
Private Sector Drives Employment Growth in Little Rock Zone

By Maria A. Arias, *Research Analyst*

> *"There has not been as much new or large construction projects to go after so we have not needed all of our staff. We had our first layoffs in several years this year and at this point do not look to hire anyone for the next year."*
>
> —Little Rock architect
>
> *"Health care industry unknowns are definitely making the public concerned and afraid to spend too much money."*
>
> —Conway area auto dealer

Government employment decreases steadily in Texarkana since 2012

Nonfarm payroll employment, SA (Index 2008=100)



Source: BLS.

- Anecdotal evidence from the survey of business contacts suggests the local labor market conditions will remain about the same or improve slightly through 2014: 50 percent of contacts expect employment and average weekly hours to increase slightly, the remaining contacts expect employment and hours to remain unchanged.
- Though employee wage growth has slowed during the second half of 2013, about 60 percent of contacts expect labor costs and wages to continue increasing through next year.
- Labor market conditions have improved in all but one of the four MSAs in the Little Rock zone. Unemployment rates have decreased slightly and employment growth has increased moderately since the second quarter in Little Rock, Fayetteville, and Fort Smith (see table).
- Private-sector employment continued to drive employment growth in the zone's MSAs. Specifically, Fayetteville's service sector grew three times as fast as the national average (see table).
- Government-sector employment continued to decline in Texarkana, despite increasing slightly in July, offsetting the modest employment gains in the private sector (see figure and table).

	Little Rock	Fayetteville	Fort Smith	Texarkana	US
Unemployment rate (Q3-13) (%)	6.4	5.4	7.5	7.0	7.3
Nonfarm employment (Q3-13)	2.0	5.3 ▲	2.2	-0.4	1.7
Goods-producing sector	-0.7 ▲	1.9	-2.0	3.2	1.2
Private service-providing sector	3.1	6.9 ▲	4.2	0.4	2.2
Government sector	-0.6	1.3	0.7	-4.5	-0.3

Note: Unless otherwise noted, values are percent change from one year ago. Arrows indicate a significant (± 1 standard deviation) change from the previous quarter. See appendix for notes and sources.

Manufacturing Data Point to Increased Uncertainty

By Yang Liu, *Senior Research Associate*

"Until the economy becomes more clear, there will be cash sitting on the balance sheet, not fully invested to capacity."

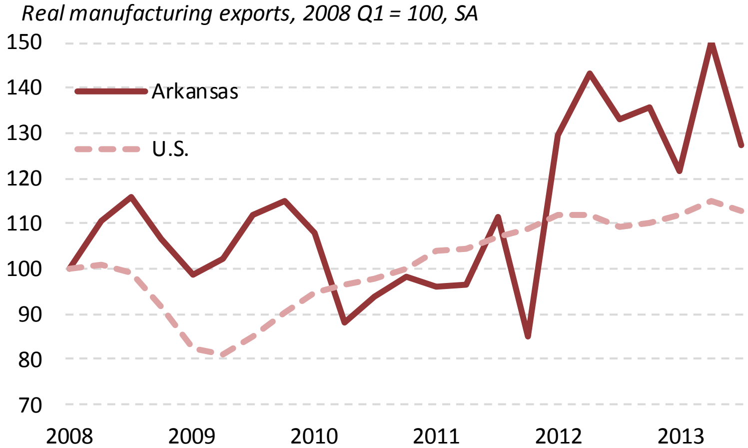
– Northwest Arkansas transportation executive

"We expect lumber production in the U.S. South to increase by 50 percent during the next three to five years from present levels."

— Southern Arkansas manufacturer

Manufacturing exports in Arkansas are up 30% since the recession ended

Real manufacturing exports, 2008 Q1 = 100, SA



Source: World Institute for Strategic Economic Research.

- Manufacturing employment in Little Rock dropped slightly in the third quarter of 2013; Fayetteville reported no growth in manufacturing employment. On a year-over-year basis, such developments translates into a modest decline in Little Rock and modest uptick in Fayetteville (see table).
- Arkansas's nondurable goods manufacturing shed 500 jobs in the third quarter of 2013, while its durable goods manufacturing added 500 jobs. As a result, Arkansas experienced no manufacturing employment change in the third quarter. However, its year-over-year manufacturing employment decreased 0.6 percent, due to losses in the previous quarters (see table).
- Arkansas's real manufacturing exports have been quite volatile since 2012. Arkansas' exports reached a peak in the second quarter and then dropped significantly in the third quarter. Currently, Arkansas' manufacturing exports are 27 percent higher than its precession level and 14 percent higher than the national pace (see figure).
- Arkansas's manufacturing earnings grew in the second quarter. However, its pace was below the national average (see table).

	Little Rock	Fayetteville	Arkansas	US
Manufacturing employment (Q3-13)	-0.8	0.4	-0.6	0.1
Durable goods	--	--	1.4	0.4
Nondurable goods	--	--	-2.6	-0.5
Manufacturing earnings (Q2-13)	--	--	0.8	1.7
Durable goods	--	--	0.3	1.6
Nondurable goods	--	--	1.4	2.0

Note: Values are percent change from one year ago. Arrows indicate a significant (± 1 standard deviation) change from the previous quarter; see appendix for notes and sources.

The Real Estate and Construction Markets Remain Stable

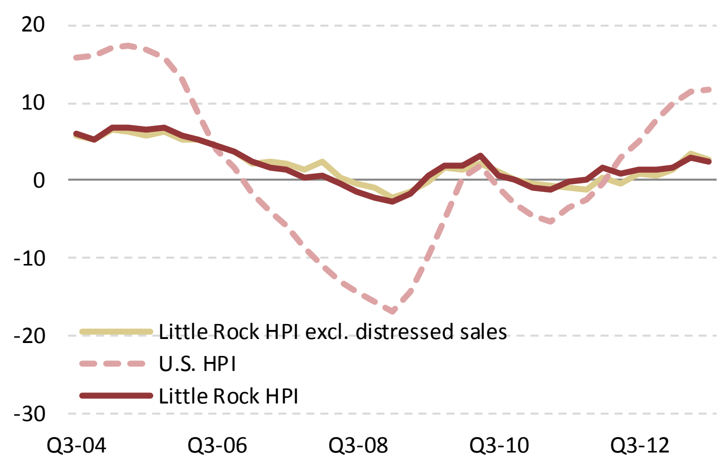
By Li Li, *Senior Research Associate*

> *"As financing becomes more available there will be a shift out of rental properties to owner occupied. However, this can only occur with affordable available housing. "*
>
> — Fayetteville area realtor
>
> *"Little Rock industrial market is a sleepy sector."*
>
> — Little Rock area realtor

- The residential market is improving. Single-family home sales were as strong as last quarter in Little Rock. Home prices grew modestly throughout the majority of the MSAs, while Fayetteville had a significant increase (see table). Anecdotes indicated that most of the new homes are being sold before the house is 75 percent completed.
- On the residential construction side, the growth rate of single-family building permits dipped in the third quarter, except in Fayetteville (see table), partly due to the fact that mortgage rates increased in the summer.
- Overall, realtors expected that the Little Rock housing market will remain on its steady course of modest growth.
- The retail market is considered healthy. Vacancy rates dropped by 30 basis points from last quarter to 12.7 percent, while the national rate is 10.5 percent. Asking rents increased by 1.7 percent from a year ago.
- There is very little construction in the commercial market. Speculative office building construction is not expected to happen in 2014. Contacts noted that there are no significant developments in retail and industrial real estate markets.

Home prices increase modestly in Little Rock

CoreLogic Home Price Index (HPI), percent change from a year ago



Source: CoreLogic.

Non-residential market (Little Rock, Q3-13)	Apartment	Office	Retail	Industrial
Vacancy rate (%)	6.6	12.2	12.7	8.1
Asking rent *Percent change from one year ago*	2.9	0.8	1.7	5.1

Note: Apartment, office, and retail values are from Reis.com. Industrial values are estimates from Cassidy Turley.

Residential market (Q3-13)	Little Rock	Fayetteville	Fort Smith	Hot Springs	Pine Bluff	Texarkana	US
CoreLogic Home Price Index	2.3	5.1 ▲	0.5	2.2	-0.8	-11.6 ▼	11.8
Single-family building permits	-5.8	39.8	-17.0	-7.9	382.4 ▼	-13.2	23.3
New and existing home sales	20.2	--	--	--	--	--	11.4

Note: Values are percent change from one year ago. Arrows indicate a signficant (±1 standard deviation) change from previous quarter. See appendix for notes and sources.

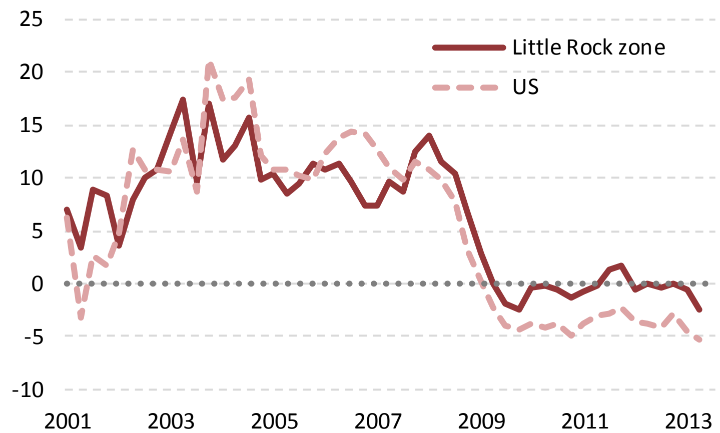
Debt Accumulation Has Slowed Across the Zone

By Bryan Noeth, *Policy Analyst*

> *"Consumer confidence is still low due to the sluggish local economy and employment."*
>
> – Little Rock area auto dealer
>
> *"Consumers continue to be challenged by ongoing uncertainty around healthcare costs, the payroll tax increase and recent reductions in SNAP benefits"*
>
> – Little Rock area retailer

Households still paying down mortgage debt

Average mortage debt, percent change from one year ago



Source: FRBNY Consumer Credit Panel, Equifax, and Haver Analytics.

- Income growth in Arkansas, like the US, was sluggish in the first half of the year. Income grew by 1.8 percent in Arkansas over the past year.
- Households continued to repair balance sheets. Credit card debt was down across the zone (see table), continuing a lengthy trend of consumer debt deleveraging. Households may take on more debt in the fourth quarter, contacts expect relatively strong holiday sales. Delinquency rates on credit card debt continued to fall and are now below pre-recession levels.
- The rapid growth in auto loans seems to have tempered in the middle portion of the year. While annual growth was still positive across the zone, dealers have cited economic uncertainty as a potential reason for the slow down.
- Households in Arkansas on average lowered their mortgage debt in the third quarter of the year. This continued a trend of low or negative growth in total mortgage borrowing that Arkansas has witnessed since the housing downturn (see chart). Low demand for mortgages and homeowners paying down existing mortgages were potential reasons for the decrease.

	Little Rock Zone	Arkansas	Little Rock MSA	US
Per capita personal income (Q2-13)	--	1.8	--	1.9
Per capita debt balances (Q3-13)				
Mortgage	-4.2	-4.3	-1.9	-6.8
Credit card	-4.3 ▼	-4.7 ▼	-3.6 ▼	-5.4 ▼
Auto loan	4.7	4.7	5.3	4.3
90+ day delinquency rates (%) (Q3-13)				
Mortgage	2.2	2.2	2.2	3.8 ▼
Credit card	7.9	7.9	7.2	9.1
Auto loan	2.2	2.2	2.4	3.2

Note: Unless otherwise noted, values are percent change from one year ago. Arrows indicate a significant (±1 standard deviation) change from the previous quarter. See appendix for notes and sources.

Banking Conditions Steady in Arkansas

By Michelle Neely, *Economist*

"The management of household finances seems to be under more focus than in years past. Consumers and businesses alike have taken a more proactive stance in understanding the metrics involved in obtaining and using credit."

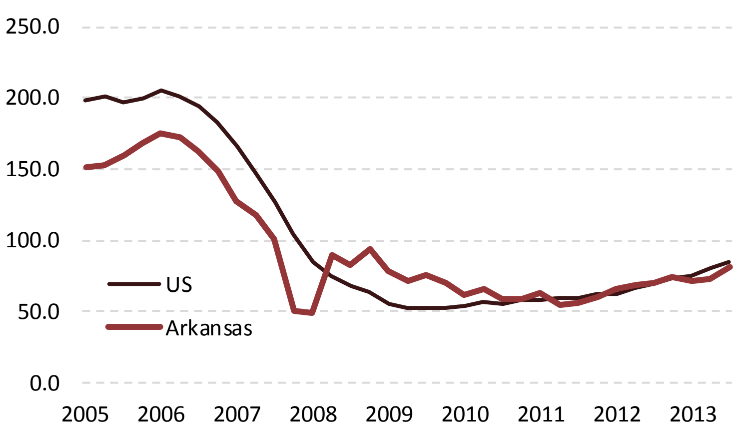
– Northeastern Arkansas banker

"Our income is up, but the gain is due to volume; we're making more loans, not more profitable loans."

—Northwest Arkansas banker

Arkansas coverage ratios track national average

Loan loss reserve coverage ratio, percent



Source: FRED.

- Return on average assets (ROA) at Arkansas banks increased 2 basis points to 1.25 percent in the third quarter, nearly erasing the dip that had occurred between the first and second quarters. ROA also increased by 2 basis points at U.S. peers, but declined 7 basis points in the District. Arkansas banks continue to be, on average, significantly more profitable than their U.S. peers.
- Rising net interest margins (NIMs) are largely responsible for the earnings increases at the state, District and national levels. Arkansas banks led the District, in average NIM at 4.11 percent and also outperformed the national peer average of 3.85 percent. NIMs at all three sets of banks had been declining for several quarters as tough competition made it difficult for banks to maintain profit margins on loans. Loan loss provisions—the earnings added to reserves to cover delinquent loans—basically held steady in the third quarter.
- Nonperforming loans declined again in the third quarter in Arkansas, the District, and the nation. Although it has fallen quite a bit, the ratio of nonperforming loans to total loans remains higher in Arkansas than in surrounding states because of mergers and acquisitions by Arkansas institutions of failing banks.

Banking performance (Q3-13)	Arkansas	8th District	US Peer Banks
Return on average assets	1.25	0.94	1.01
Net interest margin	4.11	3.74	3.85
Nonperforming loans / total loans	2.31 ▼	1.95 ▼	2.01 ▼
Loan loss reserve coverage ratio	80.95	79.89	85.07

Note: All values are percentage points. Arrows indicate a significant (± 1 standard deviation) change from the previous quarter. See appendix for notes and sources.

2013 Harvest Brings Exceptional Corn, Weak Rice production

By Lowell R. Ricketts, *Senior Research Associate*

"We have had three fabulous years, but there's no guaranty next year will be the same. We had unusually cooler weather that is more characteristic of the Midwest than Arkansas."

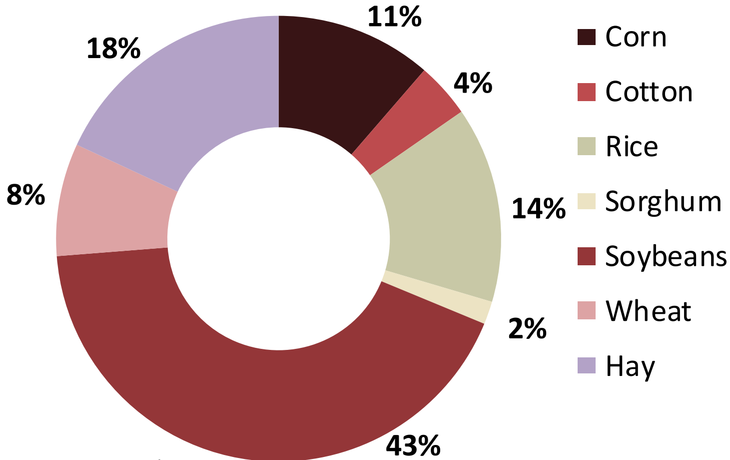
— Northern Arkansas farmer

"The southern part of Arkansas had tremendous soybean yields, with many soybean growers having field averages from the mid-60 to mid-70 bushels per acre."

— Arkansas agronomist

Soybeans composed much of the 2013 harvest

Percentage share of total acres harvested



Source: USDA/NASS

	Arkansas	US
Natural resources (Q3-13)		
Mining and logging employment	-0.6 ▲	3.3
Coal production	-32.6	1.8
Production (2013)		
Corn	25.8	29.8 ▲
Cotton	-46.0	-24.3
Rice	-15.8 ▼	-5.4
Sorghum	-3.0	68.3
Soybean	6.0	7.4

Note: Values are percent change from one year ago. Arrows indicate a significant (± 1 standard deviation) change from the previous quarter or year. See appendix for notes and sources.

- Within the Little Rock zone, agricultural bankers surveyed expect loan demand to decrease in the fourth quarter relative to the same time last year (see right table). In contrast, respondents expect more funds will be available for borrowers seeking a loan.
- 2013 corn production in Arkansas was around 26 percent greater than last year. This was slightly less than the increase for the nation as a whole (see left table). Cotton production dropped significantly, largely due to 49 percent fewer acres planted in spring. Farmers switched from cotton in pursuit of higher corn and soybean prices. Rice production had a significant decline this year due to cooler growing conditions and flooding in northeast Arkansas.
- The bulk of the Arkansas harvest consisted of soybeans this year (see figure). Hay, wheat, and corn rounded out a combined 43 percent of the harvest. Cotton and sorghum had a small share of the overall harvest.
- Coal production in Arkansas (see left table) declined in the third quarter relative to the same time last year. Production appeared to fall precipitously. However, overall coal production in Arkansas is quite small and subject to extremely large swings, percentage-wise.

Little Rock zone Ag. Banker's expectations Q4-13 vs. Q4-12

	Lower	Higher	Net
Loan demand	29	0	-29
Available funds	0	14	14
Loan repayments	14	14	0
Farm income	14	14	0
Capital expenditure	29	29	0

Note: Percentage of responses. See appendix for notes and sources.

Cover Page

Sources

Bureau of Labor Statistics

Unemployment rate, nonfarm payroll employment.

Labor Markets

Table Sources

Bureau of Labor Statistics

Unemployment rate. Nonfarm employment and contributions by sector.

Notes

Goods-producing sector comprises the manufacturing and natural resources, mining, and construction sectors.

Private service-providing sector includes the following sectors: Trade, Transportation, and Utilities; Information; Financial Activities; Professional and Business Services; Education and Health Services; Leisure and Hospitality; and Other Services.

Unemployment rate data are seasonally adjusted.

Manufacturing

Table Sources

Bureau of Labor Statistics

Manufacturing employment: total, durable, and nondurable goods.

Bureau of Economic Analysis

Manufacturing earnings: total, durable, and nondurable goods.

Notes

Real manufacturing exports are defined as total dollar amount of exports by the manufacturing industries, deflated by the chained price index for exports of goods and services.

Durable goods manufacturing sector is defined by the Bureau of Labor Statistics as industries with a NAICS classification code of 321 (Wood Product Manufacturing); 327 (Nonmetallic Mineral Product Manufacturing); 331 (Primary Metal Manufacturing); 332 (Fabricated Metal Product Manufacturing); 333 (Machinery Manufacturing); 334 (Computer and Electronic Product Manufacturing); 335 (Electrical Equipment, Appliance, and Component Manufacturing); 336 (Transportation Equipment Manufacturing); 337 (Furniture and Related Product Manufacturing); and 339 (Misc. Manufacturing).

Nondurable goods manufacturing sector is defined by the Bureau of Labor Statistics as industries with a NAICS classification code of 311 (Food Manufacturing); 312 (Beverage and Tobacco Product Manufacturing); 313 (Textile Mills); 314 (Textile Product Mills); 315 (Apparel Manufacturing); 316 (Leather and Allied Product Manufacturing); 322 (Paper Manufacturing); 323 (Printing and Related Support Activities); 324 (Petroleum and Coal Products Manufacturing); 325 (Chemical Manufacturing); and 326 (Plastics and Rubber Products Manufacturing).

Manufacturing earnings is the sum of wage and salary disbursements, supplements to wages and salaries, and proprietors' income less contributions for government social insurance.

Real Estate and Construction

Table Sources

CoreLogic

Home price index, including distressed sales.

Census Bureau

Year-to-date single-family building permits.

National Association of Realtors

Year-to-date new and existing home sales.

Notes

Asking rent is the publicized asking rent price. Data are in current dollars.

Vacancy rate is the percentage of total inventory physically vacant as of the survey date, including direct vacant and sublease space.

New and existing home sales consists of single-family home sales.

Household Sector

Table Sources

Equifax based on authors' calculations

All figures are based on a 5 percent sample of individual credit reports. Balances are geographical averages of various debt categories. The mortgage category includes first mortgages and home equity installment loans, but home equity lines of credit are omitted. Auto loans include those financed by finance company or bank loans. Credit cards are revolving accounts at banks, bankcard companies, national credit card companies, credit unions, and savings and loan associations.

Haver Analytics

Per capita income.

Census Bureau

Homeownership rates.

Notes

Delinquency rates are calculated as the percentage of payments past due by more than 90 days, weighted by the dollar value of the loan.

Homeownership rates are the proportion of households in each area that are owners. It is calculated by dividing the number of households that are owners by the total number of occupied households.

Banking and Finance

Table Sources

Federal Financial Institutions Examination Council

Return on average assets: USL15ROA. Net interest margin: USL15NIM. Nonperforming loans: USL15NPTL. Loan loss reserve/Total loans: USL15LLRTL. Net loan losses/Average total loans: USL15LSTL.

Note: The data available in the table can be found in FRED.

Notes

Loan loss provisions are expenses banks set aside as an allowance for bad loans.

Nonperforming loans are those loans managers classify as 90 days or more past due or nonaccrual, which means they are more likely to default.

Loan loss coverage ratio is loan loss reserves divided by non performing loans.

US peer banks are those commercial banks with assets of less than $15 billion.

Due to the seasonal nature of bank return on average assets and net interest margin, the **arrows** in the table denote significant changes from one year ago.

Agriculture and Natural Resources

Table Sources

Federal Reserve Bank of St. Louis Survey of Agricultural Credit Conditions

Agriculture Bankers' expectations of loan demand, available funds, loan repayment rates, farm income, and capital expenditures are relative to one year ago. Respondents can answer "increase," "decrease," or "no change."

Energy Information Administration (EIA)

Coal production.

Bureau of Labor Statistics (BLS)

Mining and logging employment.

USDA

Crop production.