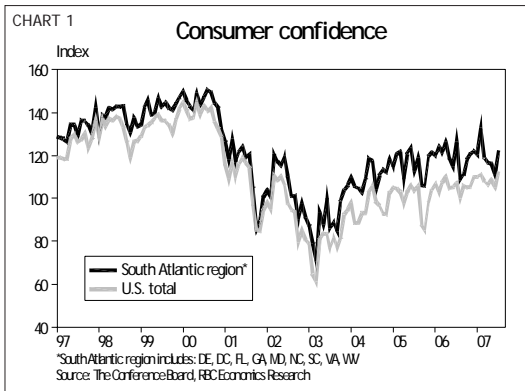


## States in focus



**Southeast region: North Carolina, South Carolina, Virginia, Georgia, Florida, Alabama**



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## U.S. STATE MONITOR

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## Despite housing weakness, consumer resilience in the southeast keeps the retail sector afloat

Last month we looked at the state of housing markets across the southeast region to assess the extent of the current correction. While significant state-by-state variation is playing out, the underlying theme is characterised by housing markets that appear to be stabilizing near the bottom after a major housing market correction. While we expect the pace of consumer spending to continue to slow in reaction to softer real estate markets, we do not expect a significant spillover from housing market weakness to bleed into consumer demand. Tight labour markets, healthy wages, and strong equity markets have served as powerful offsets to softer real estate markets. Infact, the resiliency of consumers has been a substantial support to the economy and will be a significant contributor to economic growth in the coming year as the residential market remains soft.

The evidence that demonstrates the strength of the consumer across the southeast region is showing up in several different measures. Consumer confidence levels are healthy, retail sales - though volatile - are still growing at a decent clip, and the expectations for sales going forward are fairly optimistic. While most of these measures which gauge consumer activity are below their late 1990s peaks, they are still tracking at elevated levels and are sitting comfortably above the lows hit at the start of the decade when the economy witnessed a mild recession.

### Consumer expenditures cool, but supports in place...

Consumer expenditures at the national level slowed in the second quarter from the robust 4.2% pace averaged over the prior two quarters as rising gasoline prices took a bite out of consumer's wallets. Still, employment growth continues to progress at a good pace and wage growth remains healthy. Combine this with the fact that gasoline prices are off their recent peaks and supports are in place to ensure that consumer spending continues at a decent clip going forward. The second quarter dip in expenditures is expected to be temporary, with the pace to gradually pick up momentum through this year and into next.

### ...and latest consumer confidence reading soars

Consumer confidence trends in the South Atlantic region are tracking closely to the national average, though historically the South Atlantic index remains a touch higher (chart 1). Though confidence levels in the South Atlantic appeared to be tapering off through the early part of 2007 after peaking in February, the latest reading showed a surge in confidence in both the South Atlantic region as well as right across the nation. The nationwide confidence reading in July climbed to its highest level since 2001. While the level in the South Atlantic region did not shoot above its February peak, it made significant headway to recover from the decline in confidence that set in during the early part of 2007.

Taken together with other improving confidence measures, the recent report suggests that spending will accelerate from its tepid second quarter pace, as consumers are buoyed by continued labour market strength and healthy income gains. The latest surge in confidence provides one more piece of evidence that a pick-up in activity in the economy will gradually take hold.

### Retail sales in the southeast still running at a healthy clip

After a surge in May, U.S. retail sales dipped in June. However, the year-over-year rate remained at a still solid 3.8% pace and sales are still up an annualized 5% in the second quarter. To get a sense of retail activity in the southeast, the Federal Bank of Richmond provides a monthly retail sales index, which covers a variety of retail characteristics for states in the Richmond district. The region includes the District of Columbia, Maryland, North Carolina, South Carolina, Virginia, and most of West Virginia. For states in the southeast not included in the Richmond district, an update on retail conditions can be found in the Federal Reserve Board's Beige Book, which provides qualitative descriptions for each of the different Federal Reserve districts. The overall index for the Richmond district has shown improvements for the last three months after a fairly strong pull-off through 2006 signalling sustained resilience in the retail sector (chart 2). The Beige Book report for the Atlanta region (Alabama, Florida, Georgia, Tennessee, and parts of Louisiana and Mississippi) indicated that sales in June were mixed, but on balance similar to a year earlier.

### Cautious optimism characterises the outlook for retail prospects in the southeast

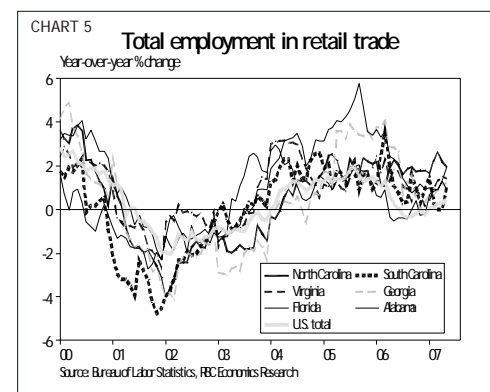
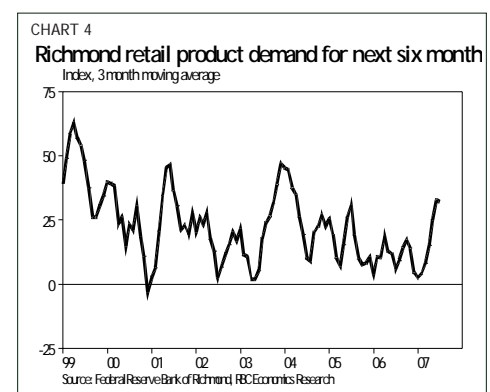
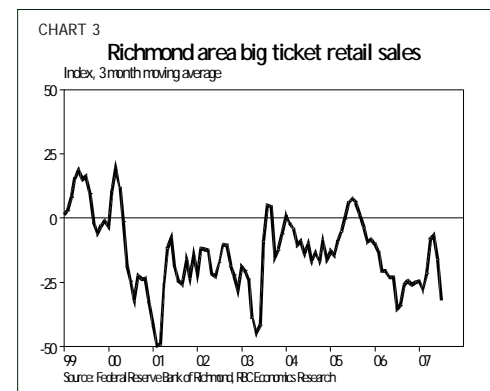
While the overall positive reading in the Richmond district still points to stable sales growth ahead, there does appear to be some weakness in big-ticket item sales, which have been trending down over the last two years (chart 3). Looking forward, the index for expected demand in the Richmond region over the next six months has been on an upswing so far in 2007 (chart 4). In the Atlanta region, many retailers reported being cautiously optimistic about their outlook going forward and most anticipate modest sales growth over the next few months. Similar to the Richmond district, big-ticket sales such as vehicles have been soft relative to overall sales.

### Employment in retail trade softer, but still positive

Retail employment growth across the southeast has been more robust than the nationwide average rate over the last few months (chart 5). Employment growth in the retail sector in North Carolina and Alabama has witnessed the fastest growth on a year-over-year basis over the last couple months. The slowest pace of growth in the sector was reported in Florida with July coming in at an annual 0.8% pace. But even the relatively soft pace of job gains in the retail sector in Florida still trumps the weak national pace. Nationwide, retail employment growth is churning out an average annual pace of 0.3% so far this year. It is clear that the drag on national retail employment growth is coming from regions outside the southeast area.

### Overall employment conditions still healthy

Even though jobs in the retail sector are hanging on well throughout most of the southeast region, what is more important is conditions in the overall job market. Job growth across the southeast is tracking at a healthy average annual pace of 1.5%. Growing incomes, tight labour market conditions and slower, but still positive, changes to net wealth will prevent the consumer from pulling back aggressively. Overall we remain cautiously optimistic about the outlook for the consumer, but we are looking for slower growth rates ahead compared to the strong rates booked in 2006



## U.S. southeast current economic indicators

### REAL ESTATE PROFILE

		<u>North Carolina</u>	<u>South Carolina</u>	<u>Virginia</u>	<u>Georgia</u>	<u>Alabama</u>	<u>Florida</u>	<u>United States</u>
At seasonally adjusted annual rates, unless otherwise indicated								
Housing starts	June-07	88,071	42,803	36,703	80,641	24,183	121,682	1,470,000
Annual % change (3-month moving ave.)		-8.7%	-13.2%	-24.8%	-21.3%	-8.7%	-43.9%	-21.2%
Housing permits	July-07	83,052	35,952	41,052	61,080	23,136	103,092	1,423,200
Annual % change (3-month moving ave.)		-10.9%	-15.8%	-11.6%	-31.0%	-26.7%	-45.9%	-23.3%
Home prices (median)								
Existing homes	Q1 2007	\$137,156	\$121,839	\$229,565	\$142,462	\$109,348	\$208,608	\$223,800
Annual % change		7.9%	7.5%	5.3%	4.9%	6.9%	4.2%	-1.5%
New homes	Q1 2007	\$174,907	\$162,853	\$301,545	\$186,986	\$144,291	\$287,805	\$257,400
Annual % change		11.5%	10.5%	12.8%	9.3%	8.8%	11.5%	3.9%
Home price index (weighted repeat sales)								
Annual % change	Q2 2007	7.1%	6.3%	3.7%	4.7%	6.6%	1.3%	3.2%
Existing single family home sales <sup>1</sup>	Q2 2007	231,200	113,600	124,000	226,400	124,800	247,200	5,913,000
Annual % change		-4.5%	-9.3%	-15.3%	-13.1%	-3.1%	-41.3%	-10.8%
Vacancy rates <sup>2</sup>								
Industrial	Q2 2007	13.2%	n/a	14.4%	20.1%	n/a	8.5%	9.8%
Office	Q2 2007	12.4%	n/a	10.1%	19.7%	n/a	10.1%	12.6%

1. Including apartments, condominiums, and cooperatives

2. Charlotte-Gastonia-Rock Hill, NC; Washington, DC-MD-VA-WV; Atlanta, GA; Ave of major MSA's, FL for office and Jacksonville for industrial.

### ECONOMIC PROFILE

		<u>North Carolina</u>	<u>South Carolina</u>	<u>Virginia</u>	<u>Georgia</u>	<u>Alabama</u>	<u>Florida</u>	<u>United States</u>
Employment	July-07	4,089,200	1,934,900	3,796,700	4,154,500	2,011,600	8,134,700	138,041,000
Annual % change (3-month moving ave.)		2.2%	2.4%	1.8%	1.7%	1.5%	1.8%	1.4%
Unemployment rate		5.0%	5.9%	3.1%	4.6%	3.7%	3.9%	4.6%
Labor force		4,522,704	2,148,831	4,051,204	4,844,865	2,189,034	9,230,273	153,231,000
Annual % change (3-month moving ave.)		1.4%	1.2%	1.4%	2.1%	0.0%	2.4%	1.1%
Personal income growth (annual % cl)	Q1 2007	6.1%	5.6%	4.5%	5.3%	6.3%	6.1%	5.8%

### EMPLOYMENT PROFILE

		<u>North Carolina</u>	<u>South Carolina</u>	<u>Virginia</u>	<u>Georgia</u>	<u>Alabama</u>	<u>Florida</u>	<u>United States</u>
July-07								
Employment (non-agricultural)								
Annual % change [share of employment]								
Total		2.7	2.7	0.9	1.4	1.3	0.4	1.1
Government		2.3 15%	2.5 16%	1.4 18%	2.1 16%	1.6 18%	2.6 13%	0.8 15%
Manufacturing		-3.3 13%	-1.1 13%	-3.4 7%	-3.9 10%	-2.5 15%	-4.1 5%	-2.0 10%
Professional & business services		4.7 12%	4.4 12%	2.6 17%	1.7 14%	2.4 11%	1.0 17%	1.9 13%
Education & health services		5.0 13%	5.6 10%	3.5 11%	3.7 11%	2.5 10%	2.9 13%	3.1 13%
Retail trade		2.8 11%	2.5 12%	1.2 11%	2.6 12%	3.5 12%	0.3 13%	1.0 11%
Wholesale trade		3.3 4%	5.1 4%	1.4 3%	1.9 5%	0.7 4%	1.2 5%	2.2 4%
Leisure & hospitality		3.5 10%	5.6 12%	1.8 10%	3.4 10%	2.2 9%	2.1 12%	2.6 10%
Transportation & utilities		-0.8 3%	4.2 3%	1.1 3%	2.3 5%	1.6 4%	0.5 3%	1.2 3%
Construction		2.6 6%	3.3 7%	-3.9 7%	0.0 5%	1.9 6%	-10.0 8%	-0.9 6%
Financial services		1.7 5%	3.8 6%	-0.5 5%	0.6 6%	1.6 5%	-0.9 7%	0.0 6%
Unemployment rate (%)								
July-07		4.7	5.8	3.0	4.4	3.6	4.1	4.7
July-06		4.7	6.2	3.0	4.5	3.5	3.4	4.7
Labor force								
y/y % change		1.0	1.3	1.5	1.8	0.9	2.3	1.1

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