

The Economy of Western North Carolina: Charting a Course for Transylvania County



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Fortunately...

**“The economy depends about
as much on economists
as the weather does on weather
forecasters.”**

Discussion Topics

- **Key Takeaways for Transylvania County...**
- **The Global Economic Crisis: In Search of the Bottom ...**
- **The WNC Economy: Near-term Indicators ...**
- **The WNC Housing Market: A Preliminary View ...**
- **WNC Outlook: Demographic Trends**
- **Charting a Course Ahead: Strategic Implications for WNC...**

Daniel J. Ostergaard Bio

- **Director, Institute for the Economy and the Future @ WCU**
 - Associate Professor of Management and International Business
 - Adjunct Professor of Applied Criminology (Homeland Security)
- **WNC Native** - Grew up in Jackson County (near Cherokee)
- **U.S. Coast Guard Seagoing Officer**
 - Ship Captain; Law Enforcement; Homeland Security; Environmental Protection; Federal Budget
- **Senior Administration Official at DHS**
 - Executive Director, U.S. Homeland Security Advisory Council & a senior policy advisor to Secretary of Homeland Security Tom Ridge and then Michael Chertoff
 - Executive Office of Governor Jeb Bush (Liaison in Washington to Congress and Executive Branch)
- **Founded Pelorus Enterprises** (International Biz Dev Consulting)
- **Elected as a Commissioner for Neighborhood Commission 6B while in D.C.**
- **Commercial Farmer** (<http://www.smokymountainfarm.com>)
- **Education:** **US Coast Guard Academy**, B.S. Gov't ('94); **US Naval War College**, M.A. Nat'l Security and Strategic Studies ('03); **Harvard Kennedy School**, M.P.A. ('04)
- ***And Most Importantly:***
Husband and Dad (aka, ABYSA U7 Co-Ed Soccer Coach and upcoming Cub Scout Den Leader!)

Definitions

- **Recession.** Reduction of a country's GDP for at least 2 quarters; period of reduced economic activity.
- **Stagnation.** Prolonged period of slow economic growth (depending on who you ask: <1% or maybe <2-3%)
- **Depression.** Sustained, long downturn. A rare but extreme form of recession characterized by abnormal increases in unemployment, restriction of credit, shrinking output and investment, numerous bankruptcies, reduced amounts of trade and commerce and highly volatile currency value fluctuations.
- **Stagflation:** A condition of slow economic growth and relatively high unemployment - a time of stagnation - accompanied by a rise in prices, or inflation.

Shape of a Recession

- **V-shaped.** Usually short and fairly shallow.
- **U-shaped.** Longer and deeper. Slow road to bottom and slow road to recovery. Early decisions to close/delay/cancel high-cost assets and/or unnecessary new capacities may be required.
- **W-shaped.** Severe destocking leads to an apparent early recovery new orders allow the value chain to restock... However, demand is not sustainable and begins to slip back again before achieving a sustainable recovery.
- **L-shaped.** Protracted period of economic stagnation (See Japan in the 1990s)

Key Takeaways

- **The Economic Crisis is Global, National, and Regional.**
- **The Economy Is Likely to Follow the 1980-1984 “L” Pattern of Behavior Toward Recovery with Growth Returning in 2009 Q 3. Some indications pork barrel stimulus will spur slight “W” pattern with emerging markets need for extractives (e.g., oil) pushing economies back down...**
- **Stagflation Appears on the Horizon for 2011.**
- **Recovery Will Occur with Stabilization of Asset Prices, Especially Housing and with the Unlocking of the Bond Market.**
- **Housing Starts May Go Below 200,000 Units (90+% under peak).**
- **Current House Prices in WNC Have Registered Slightly More than One Half the Likely Decline (6-7% from peak so far).**
- **A Key Factor in Setting Strategy ~ Interest Rates Are Very Near a Bottom; Long and Short Rates Will Rise Soon After Recovery Begins.**



**The Global Economic Crisis: In Search of the
Bottom ...**

In Search of the Bottom ...

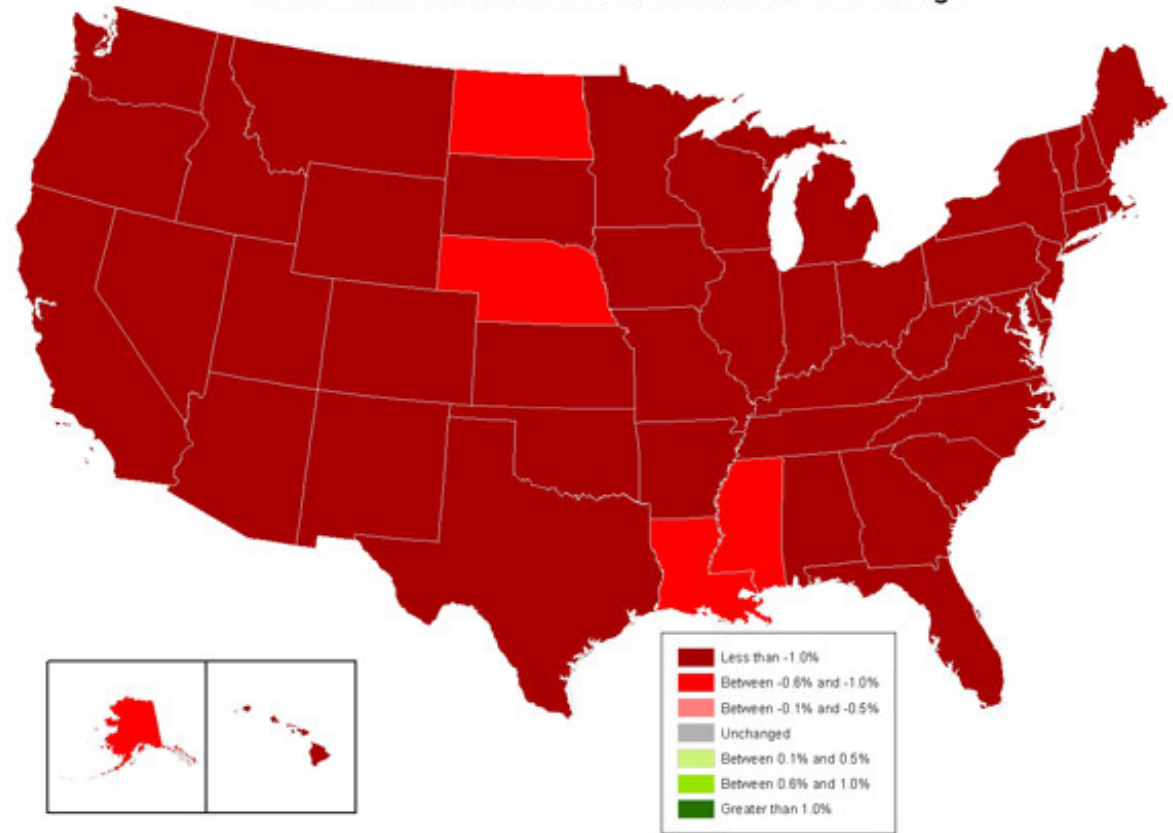
1980-1984	<ul style="list-style-type: none">• Two step decline completing a W shaped recession• Globally synchronized• Fed has ammo
1988-1991	<ul style="list-style-type: none">• First “credit crumble” recession• Not globally synchronized (V shape)• Fed has ammo• Regional in U.S.• Resolution Trust Corp help (Liquidating S&L assets)
2001-2004	<ul style="list-style-type: none">• 9/11 shock• Globally synchronized (V shape)<ul style="list-style-type: none">• China and India• Fed nearly runs out of ammo
2007-?	<ul style="list-style-type: none">• Second “credit crumble”• Huge and global• Widespread U.S.• Fed is broke and the financial system is broken-down

This Time, Unlike the 1988-1991 “Credit Crumble,” the Entire Country Is Affected ...

The Federal Reserve Bank of Philadelphia in March released the coincident indexes for all 50 states.

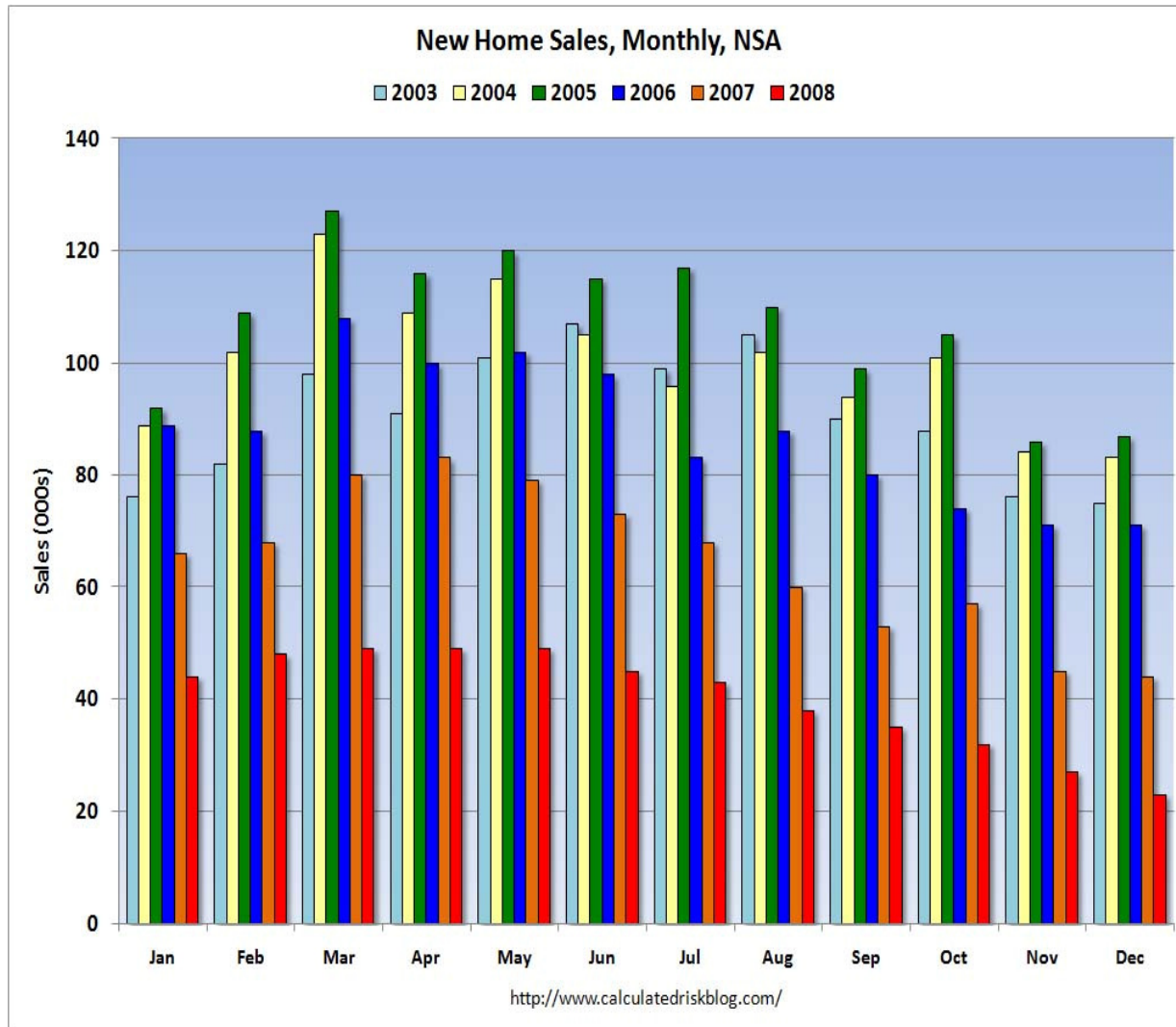
The coincident indexes combine four state-level indicators to summarize current economic conditions in a single statistic: non-farm payroll employment, average hours worked in manufacturing, the unemployment rate, and wage and salary disbursements deflated by the consumer price index (U.S. city average).

March State Coincident Indexes: Three-Month Change



The trend for each state’s index is set to the trend of its gross domestic product (GDP), so long-term growth in the state’s index matches long-term growth in its GDP.

It Has Been More Than a Year Since the Recession Began and the Housing Bottom Remains Elusive ...



Sales of new one-family houses in March 2009 were at a seasonally adjusted annual rate of 356,000.

This is 0.6 percent below the revised February rate of 358,000 and is 30.6 percent below the March 2008 estimate of 513,000.

The median sales price of new houses sold in March 2009 was \$201,400; the average sales price was \$258,000. The seasonally adjusted estimate of new houses for sale at the end of March was 311,000. This represents a supply of 10.7 months at the current sales rate.

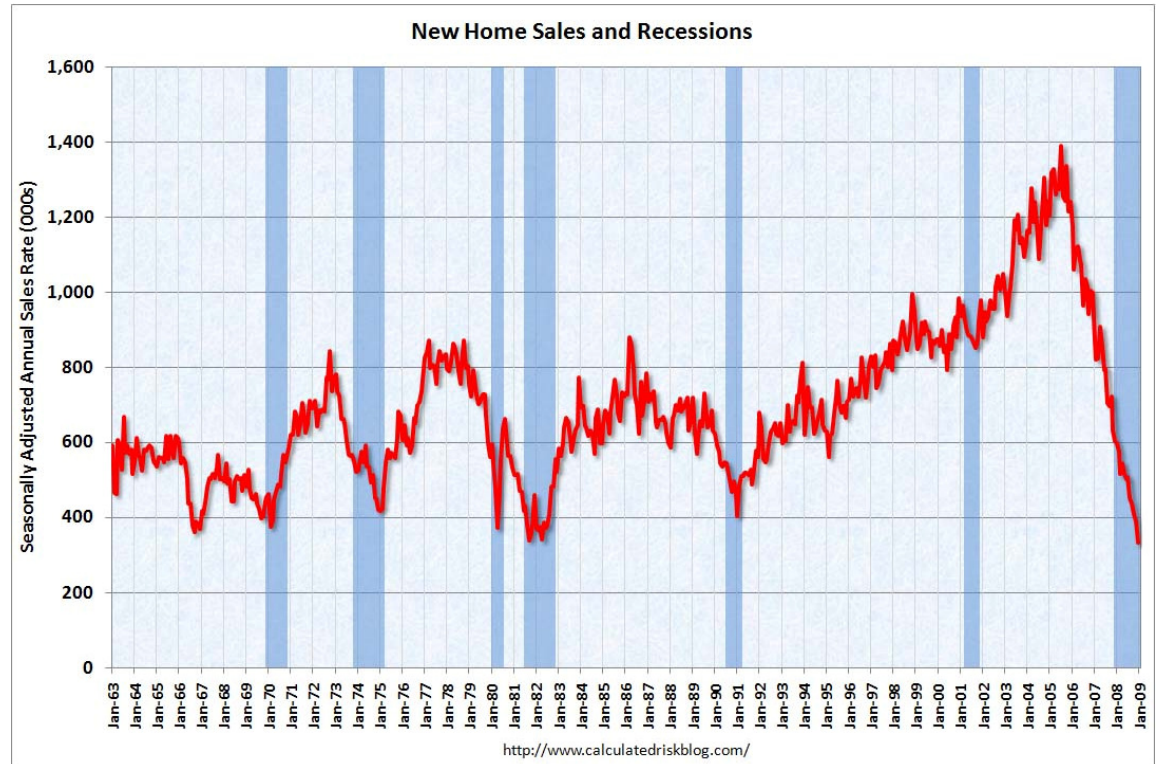
February's Read on the U.S. Housing Situation Suggests More Weakness Ahead ...

February 2009 Inventory of Homes for Sale:

	<u>2-09</u>	<u>2-08</u>
All	25.2	28.0
Previously Owned	22.0	23.8
New Construction	3.2	4.2

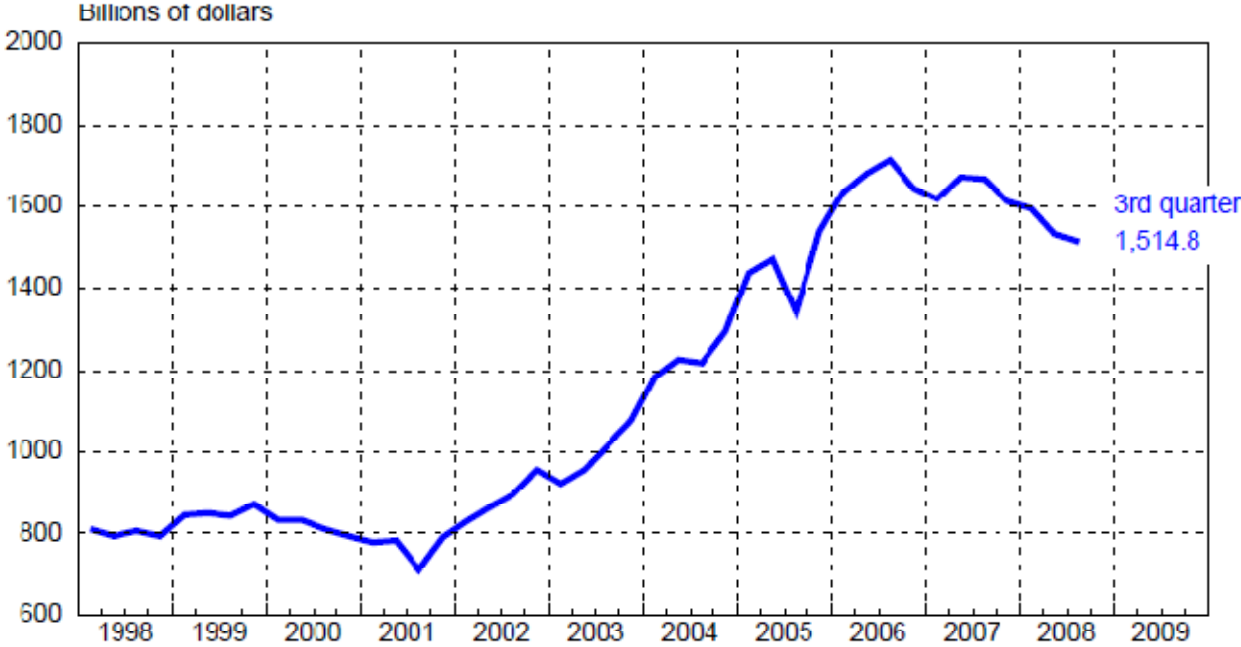
More residential construction projects will be cancelled or postponed in this environment. Expect continued downward pressure on home prices and to a continued decline in residential construction.

A potential plan to contain illiquid mortgage-related assets in a "bad" or "aggregator" bank may help and hasten the end of the painful housing recession. But it may still take several quarters to work through the excess supply in the housing market.



The Good News Is that Corporate Profitability Held on Through 2008 Q3 ...

CORPORATE PROFITS WITH IVA AND CCADJ Seasonally Adjusted Annual Rate



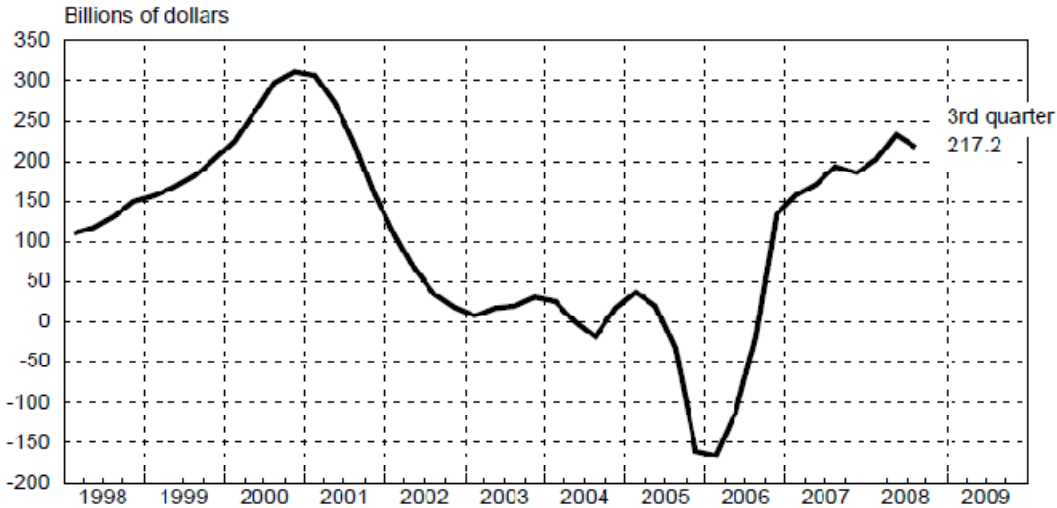
Source: Bureau of Economic Analysis.

*Inventory Valuation Adjustment (IVA) and Capital Consumption Adjustment (CCAdj)



Helping to Support Capital Spending in 2008 Q3 ...

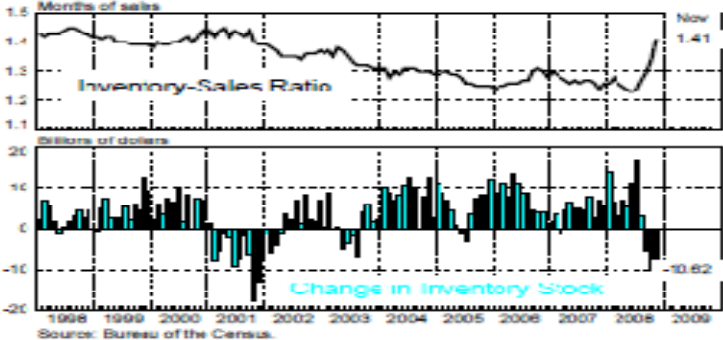
FINANCING GAP -- CAPITAL SPENDING LESS CASH FLOW
NONFINANCIAL CORPORATE BUSINESS
4 quarter Moving Average of Seasonally Adjusted Flows



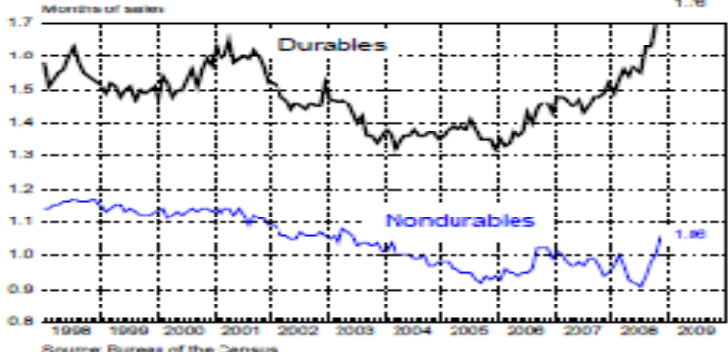
Source: Federal Reserve Board of Governors.

However, the Surge in Unplanned Inventories in 2008 Q4 ...

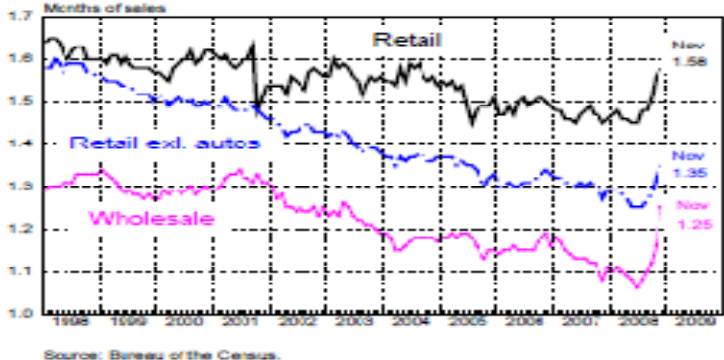
MANUFACTURING AND TRADE INVENTORIES
Seasonally Adjusted



MANUFACTURING INVENTORY-SALES RATIOS
Seasonally Adjusted



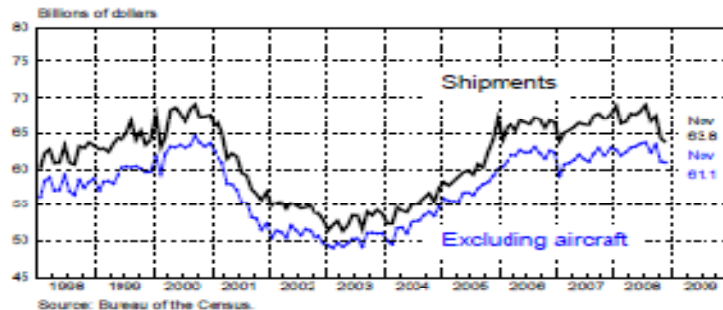
TRADE INVENTORY-SALES RATIOS
Seasonally Adjusted



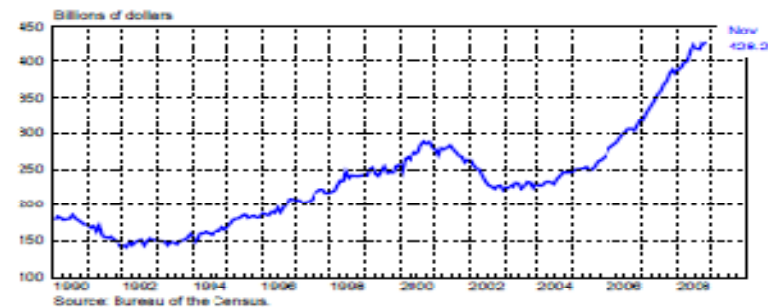
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And the Drop in Capital Goods Orders in 2008 Q4 ...

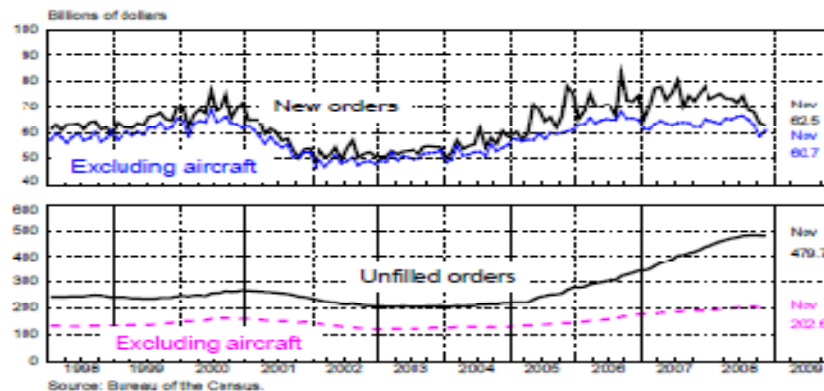
NONDEFENSE CAPITAL GOODS SHIPMENTS
Seasonally Adjusted



PRIVATE NONRESIDENTIAL CONSTRUCTION
Seasonally Adjusted Annual Rate



NONDEFENSE CAPITAL GOODS ORDERS AND BACKLOGS
Seasonally Adjusted



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U.S. Industrial Production and Capacity



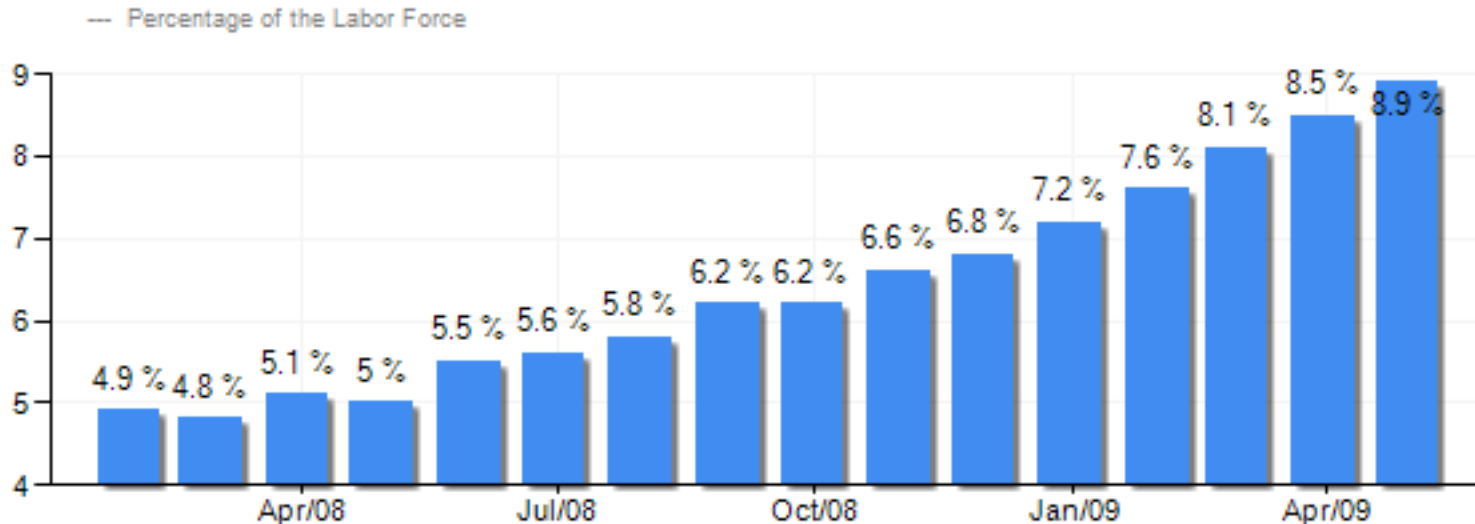
Point to Further Weakening of the Economy through 2009 H1 and Bottoming in 2009 Q3.

Period	US GDP Growth Outlook With Fiscal Stimulus (%q/q)	US GDP Growth Outlook Without Fiscal Stimulus (%q/q)	Difference
2009 Q1	- 6.0	- 6.0	+0.0
2009 Q2	- 1.5	- 5.0	+3.5
2009 Q3	+0.5	- 3.0	+3.5
2009 Q4	+2.5	+2.0	+0.5
2010 Q1	+3.0	+3.0	0.0
2010 Q2	+2.5	+3.0	- 0.5
2010 Q3	+3.5	+3.5	0.0
2010 Q4	+3.5	+3.5	0.0
2011	Stagflation ???		

Challenges or Opportunities for Transylvania County?

- Oil/Energy Prices
- Decoupling of the Dollar
- Increasing Competition in the Global Marketplace
- Out-of-Control Federal Debt/Deficit
- Continued Decline in U.S. Manufacturing
- Increasing competition for Extractives
- Relative Size of Burgeoning Middle- and Upper-Classes Globally
- Continued Instability with Nuclear Proliferation

United States Unemployment Rate



source: Bureau of Labor Statistics

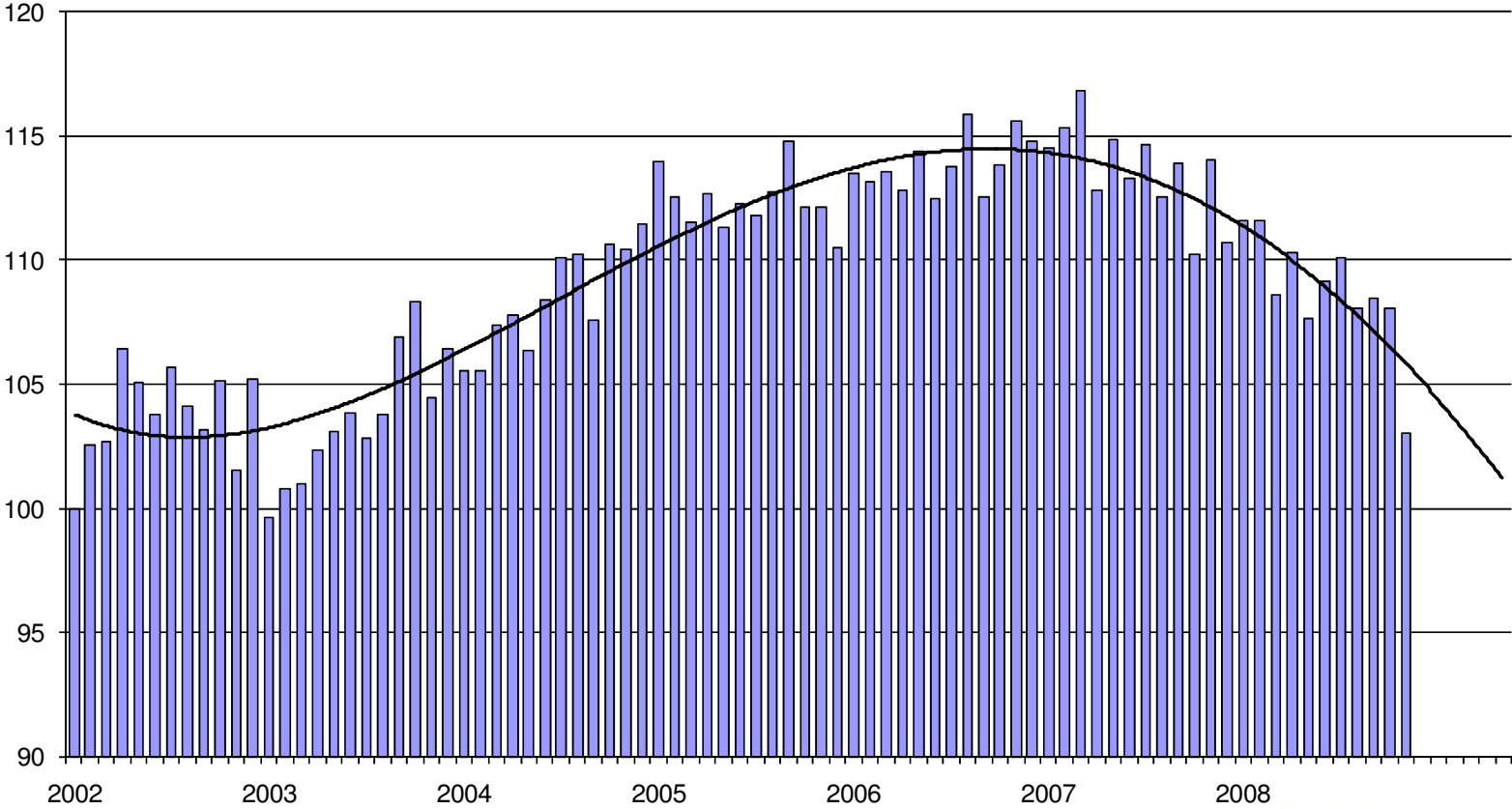


The WNC Economy: Near-term Indicators

...

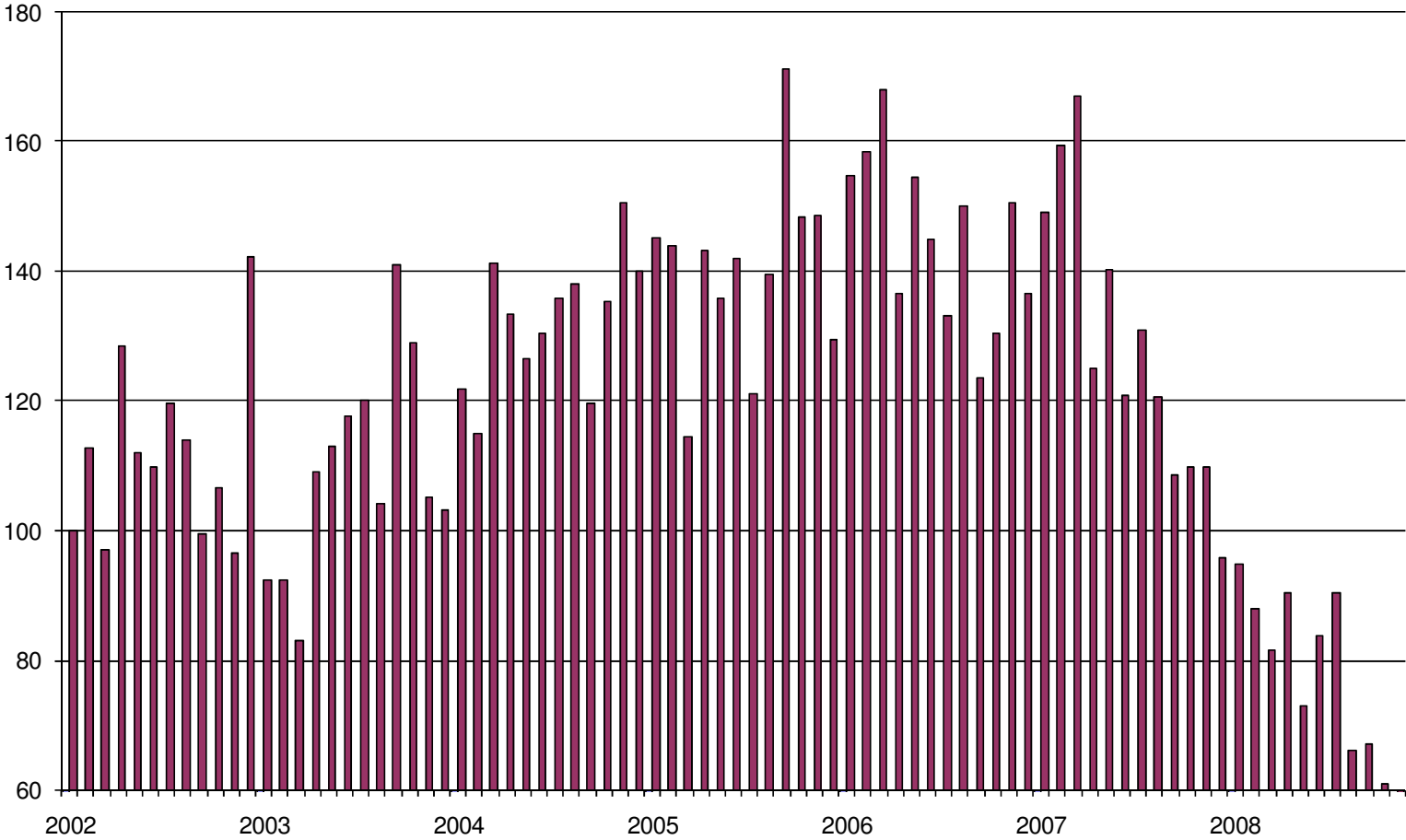
The Current Weakness in the Regional Economy of WNC Largely Reflects ...

**Figure 1. Regional Economic Activity Index
Western North Carolina (23 Counties)
(Jan 2002 = 100)**



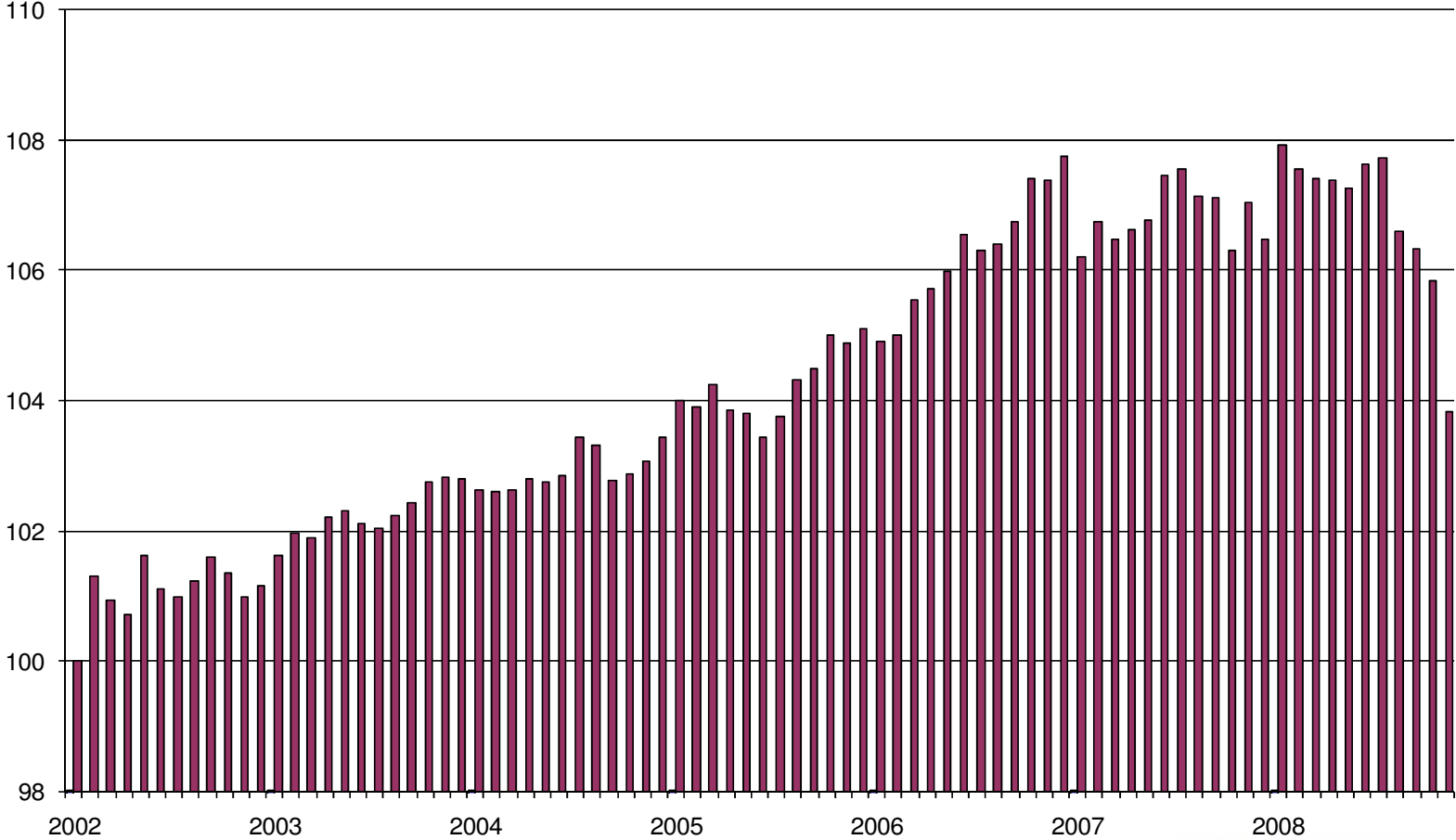
The Sharp Slowing of Real Estate Activity ...

Figure A-4: Real Estate Index



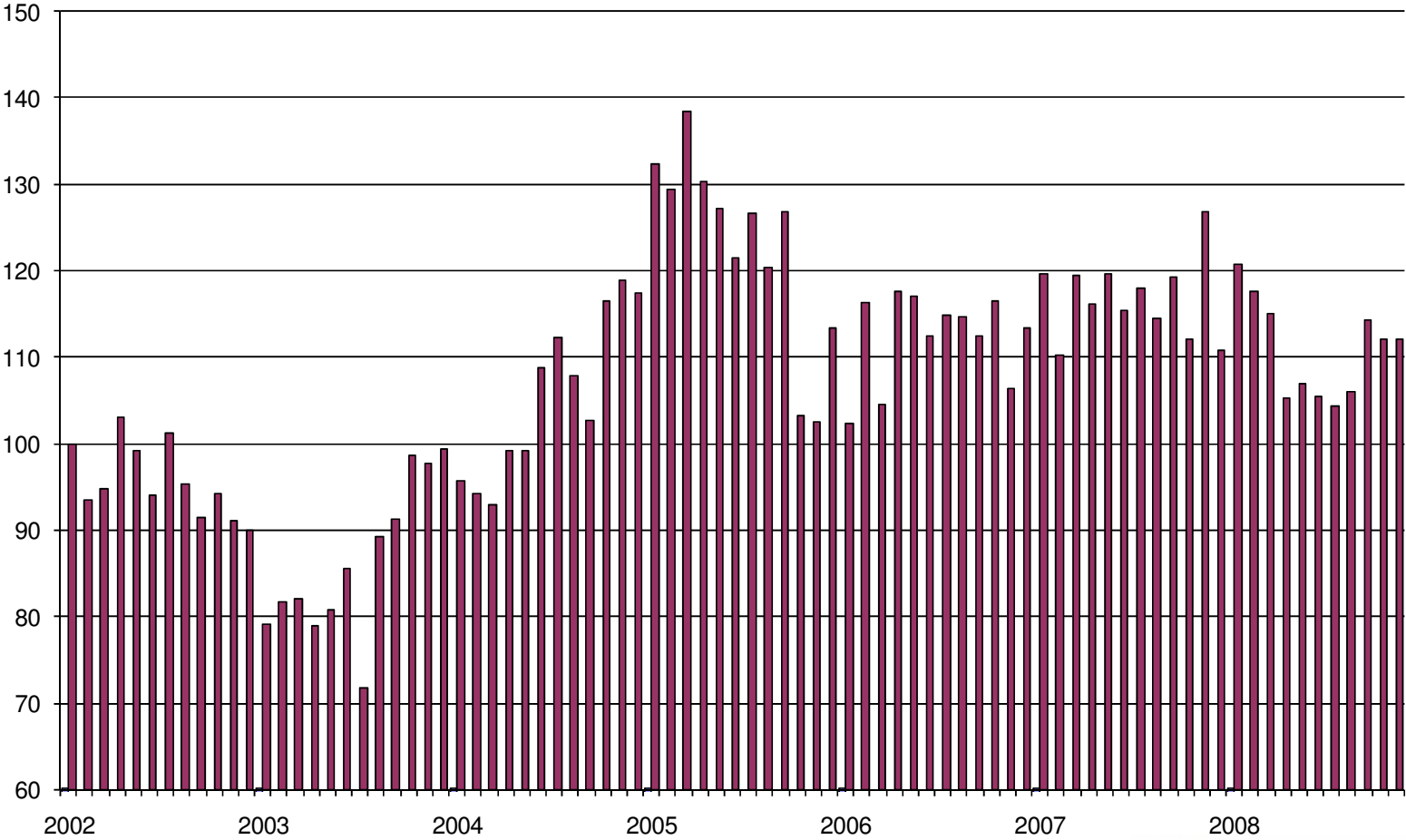
There Has Been Slippage in Regional Employment ...

Figure A-1: Employment Index



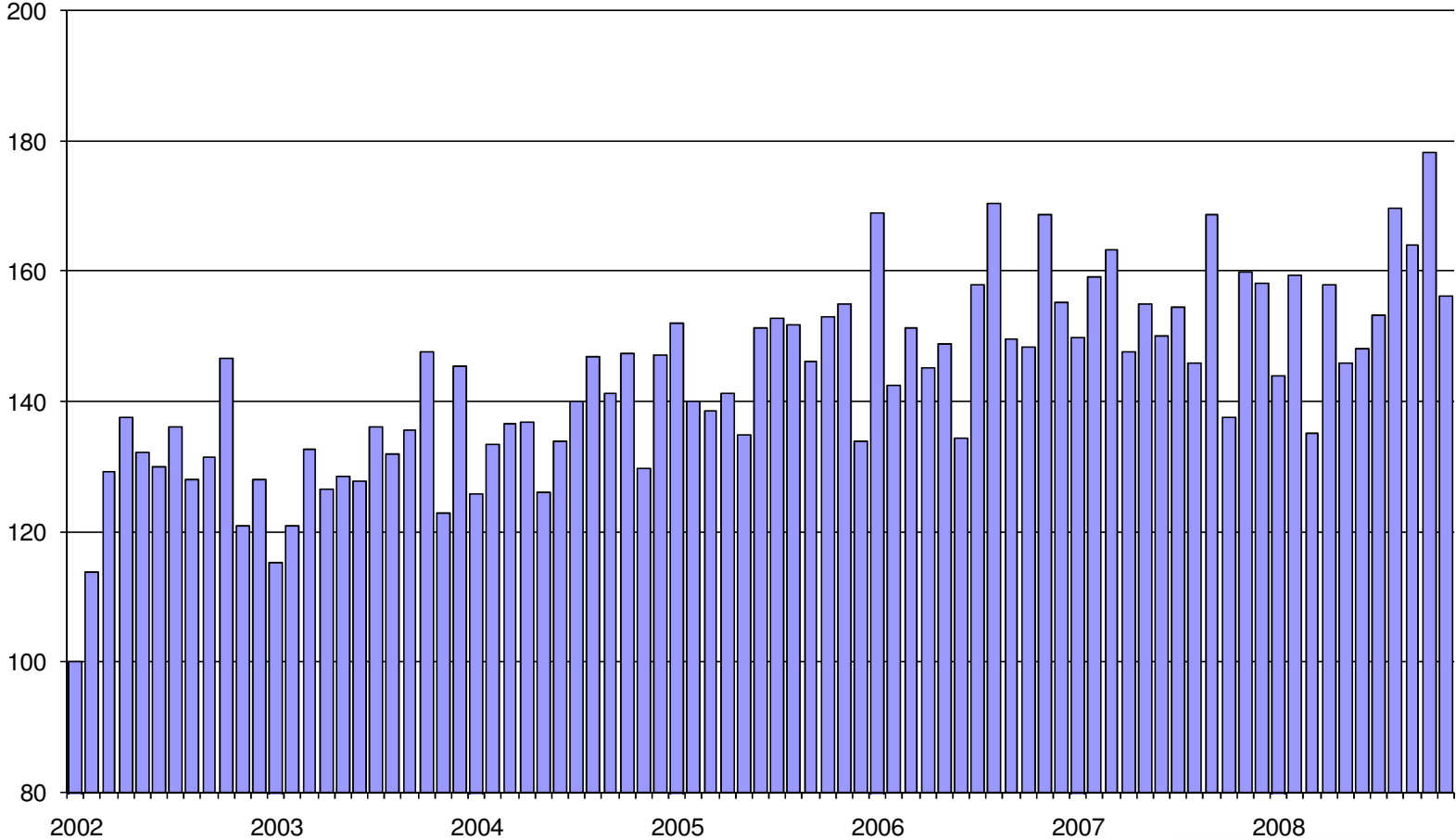
Tourism ...

Figure A-3. Tourism Index



And to Some Extent Retail Sales.

Figure A-2: Retail Sales Index



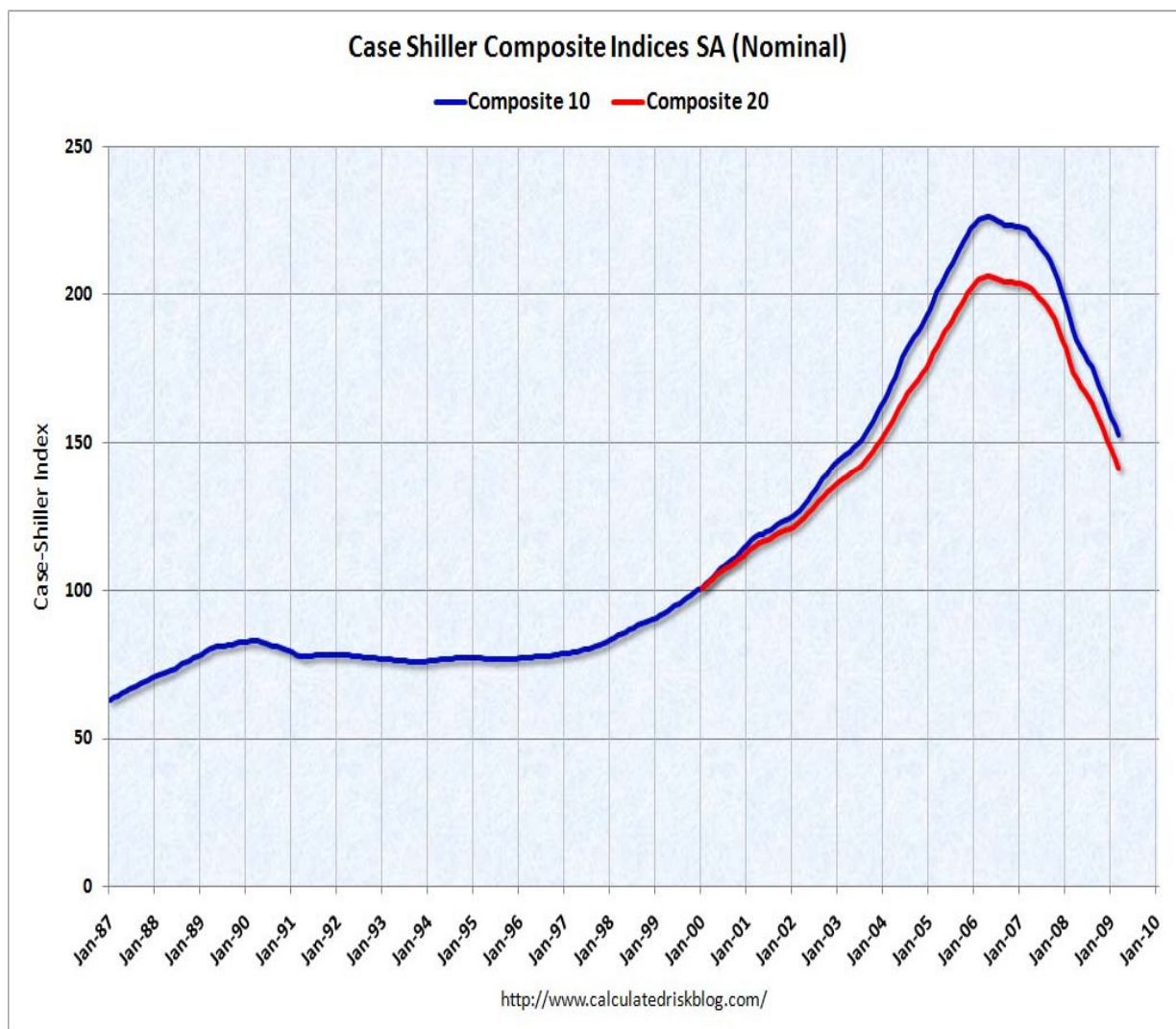


**The WNC Housing Market:
A Lagging Indicator**

Key Takeaways, WNC Housing Market ...

- **NC and WNC Prices correlate well with Case-Shiller***
*(quarterly nominal house price indices for the U.S.)
- **0% to 5% further decline in WNC prices based on historical trends**
 - Seasonal fluctuation is 5% to 10% on top of base trends
- **Housing markets take 3+ years to clear after major recessions**
- **Expect foreclosures in areas where mean housing values are out of line with mean personal income**

National Home Sale Prices ...



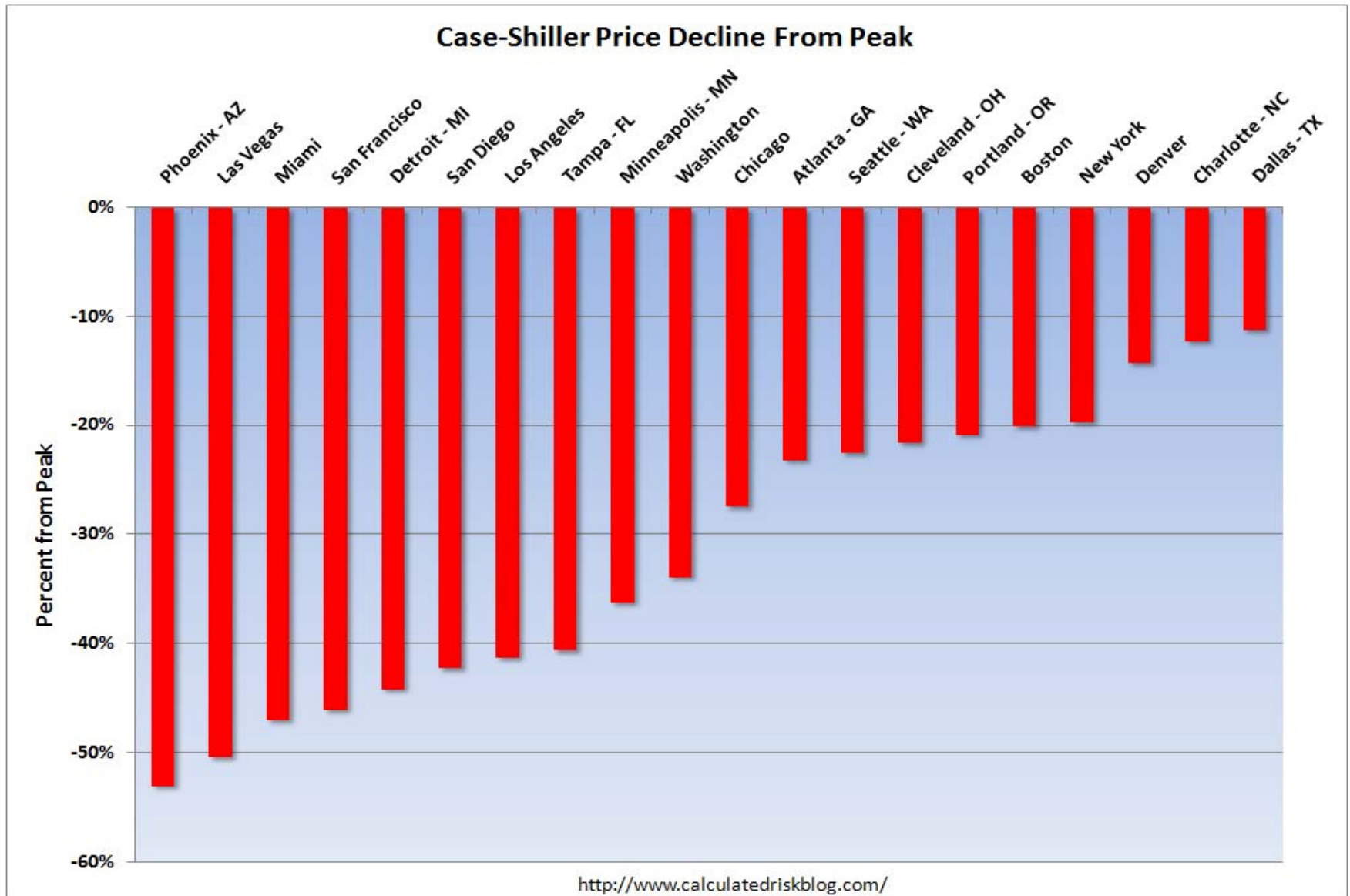
- Lower index = more affordable housing
- Prices dropped most during Q1 coinciding with foreclosure moratorium period (during quick sales and cheap prices)
- Lower prices may now be driving slight up-tick in demand...

...but demand seems to be new homebuyers and investors...

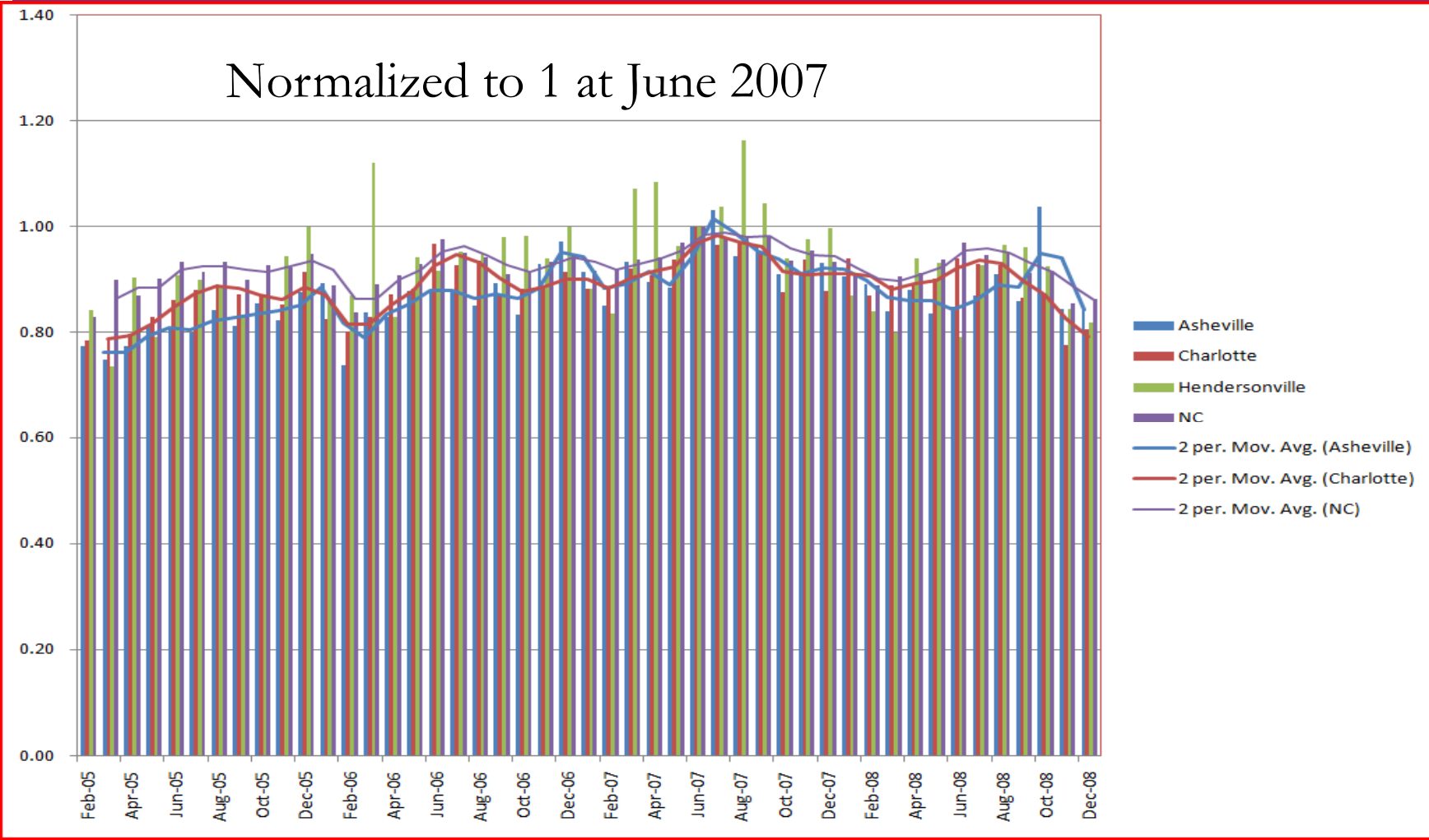
...leaving normal “up-graders” stranded...

The indices are normalized to have a value of 100 in the first quarter of 2000.

Regional Housing Markets ... (March 09)



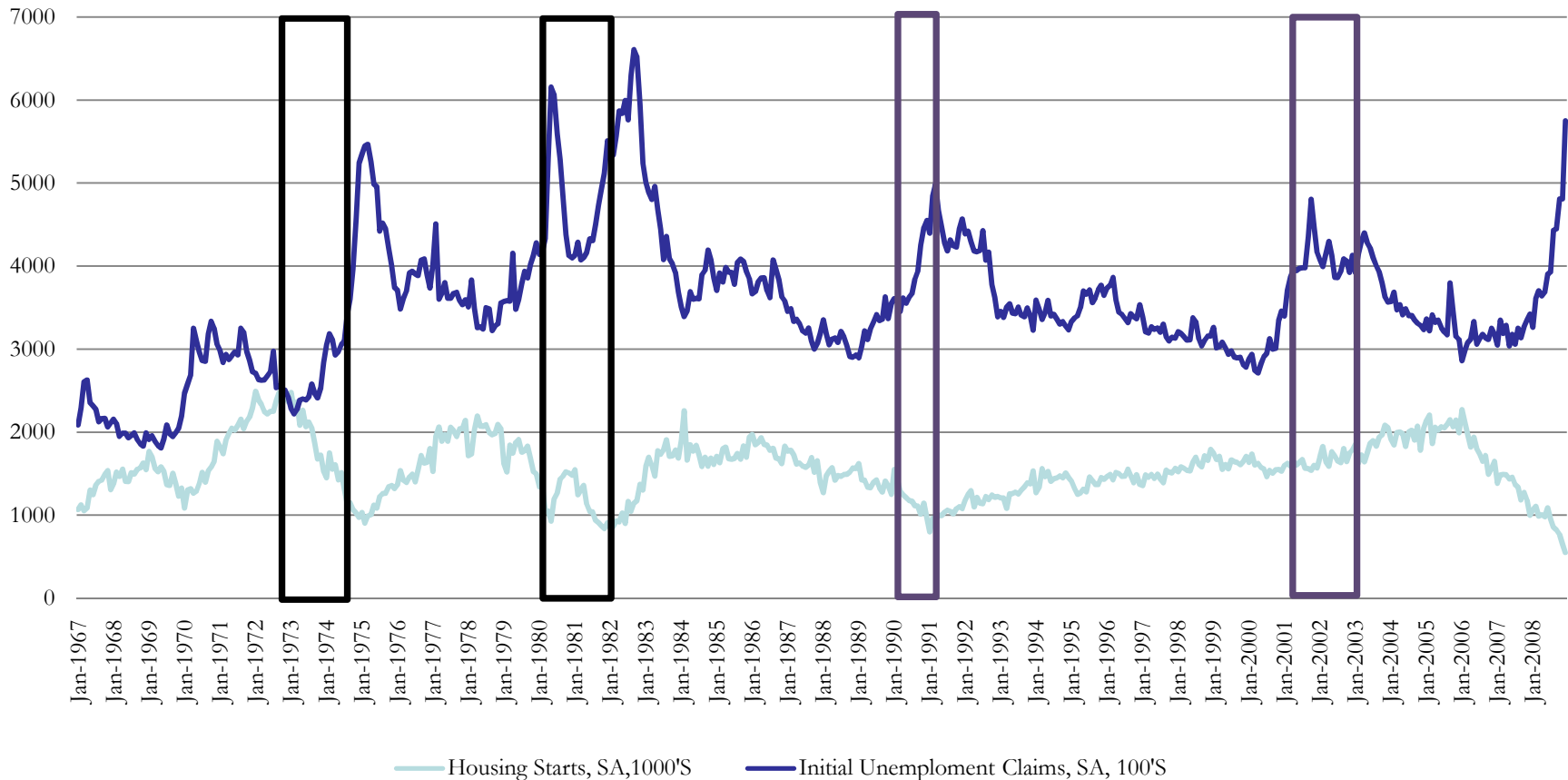
NC Average Home Sale Price History ...



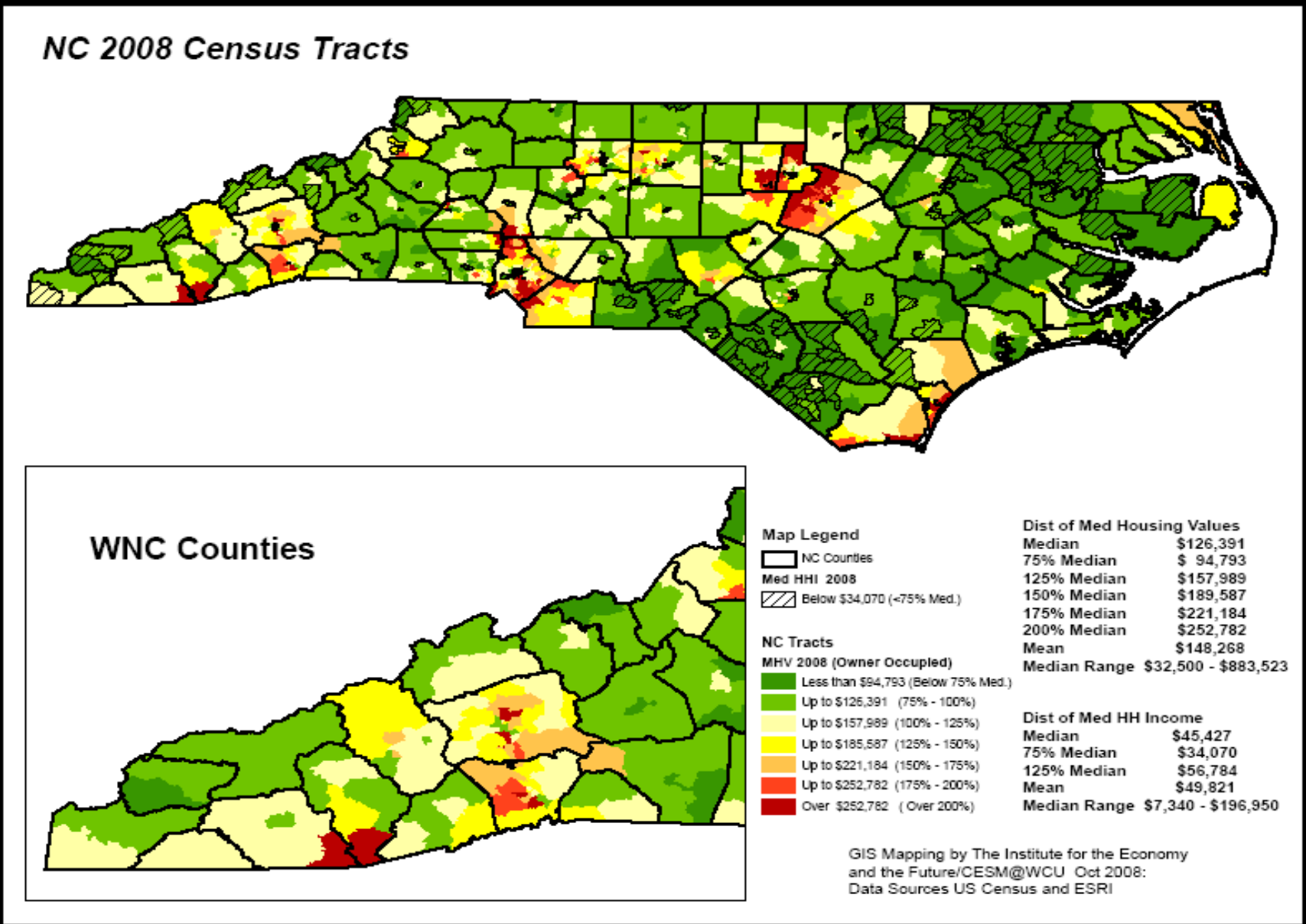
Source: NC Association of Realtors



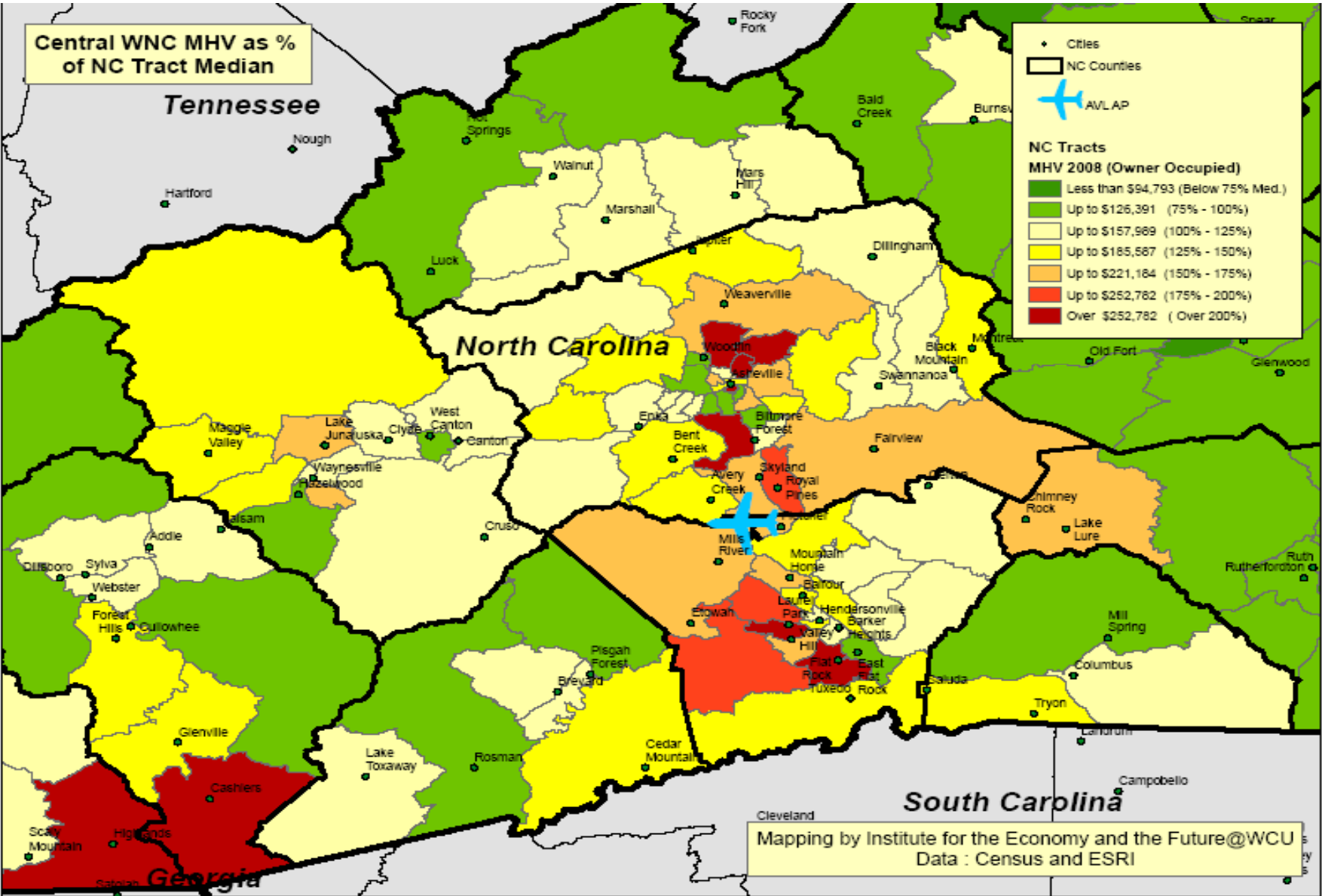
Housing Starts, New Unemployment Claims and US Recessions ...



Housing Values in NC: A Basis for Foreclosure Projections ...



Housing Values in WNC: A Basis for Foreclosure Projections ...





WNC Outlook: Strategic Implications

WNC Is a Prime Location

- **Centrally located within the megapolitan area**
- **Central to major transportation arteries**
- **Land/area to expand**
- **Workforce that had been seeking opportunities elsewhere but lived here due to quality of life**

WNC Cluster Development?

- **Clusters affect competition:**
 - Increasing productivity
 - Driving direction and pace of innovation
 - Stimulating the growth of new businesses
- **Once Cluster begins to form, self-reinforcing cycle...quality of workforce, innovation, shared marketers, suppliers, etc...**

Strategic Implications

- **Financial Considerations in this recession**
 - View Credit Quality as Paramount for Years to Come
 - Focus Heavily on Spread Management As Rates Rise and the Yield Curve “Ratchets” Upward
 - Avoid Locking in Long Maturities of Assets
 - Continue Lowering “Production Costs”
 - Seek More “Non Rate-Driven” Income
 - Build Capital and Economies of Scale, as they are Vital for Survival

Advice from the “Experts” Part 1

“4 Actions to Survive the Recession and Emerge Triumphant”

Passivity will only make things worse...

1. Move while others are distracted.
2. Announce and own a grand concept.
3. Get rid of things that have outlived their usefulness.
4. Concentrate on helping your users, clients, or customers succeed.

Professor Rosabeth Moss Kanter, Harvard Business School, Jan 9, 2009

(<http://discussionleader.hbsp.com/kanter/2009/01/four-actions-to-survive-the-re.html>)

Advice from the “Professionals” Part 2

1. **You must avoid taking on bad business under the mistaken impression that any business is better than no business.** Projects that cannot pay their way guarantee a trip to bankruptcy. You cannot pursue new business that can't begin to cover costs. If a new client can't produce a positive cash flow, don't accept that client.
2. **Staying in business is more important than the size of today's staff.**
3. **Aggressively pursue monies due you.** Today's accounts receivable have no reality until they're collected. Receivables require a vigorous effort - you must be aggressive in collections.
4. **Today, much of the best talent is out on the street looking for a new home.**
5. **Marketing is everything in a recession.** Smart firms continue with a strong marketing effort even in difficult times. But don't expect instant gratification. Marketing in tough times paves the way for future profits.
6. **Consider solidifying future business through mergers and acquisitions.**

Barry B. LePatner, Real Estate Weekly, Jan 29, 1992

(http://findarticles.com/p/articles/mi_m3601/is_n25_v38/ai_11853888)



Marketing Advice from the “Professionals” - Part 3a

Companies should bear eight factors in mind when making their marketing plans during a recession:

1. **Research the customer.** Instead of cutting the market research budget, you need to know more than ever how consumers are redefining value and responding to the recession. Price elasticity curves are changing. Consumers take more time searching for durable goods and negotiate harder at the point of sale. They are more willing to postpone purchases, trade down, or buy less.
2. **Focus on family values.** When economic hard times loom, we tend to retreat to our village. Look for cozy hearth-and-home family scenes in advertising to replace images of extreme sports, adventure, and rugged individualism. Zany humor and appeals on the basis of fear are out.
3. **Maintain marketing spending.** This is not the time to cut advertising. It is well documented that brands that increase advertising during a recession, when competitors are cutting back, can improve market share and return on investment at lower cost than during good economic times.
4. **Adjust product portfolios.** Marketers must reforecast demand for each item in their product lines as consumers trade down to models that stress good value, such as cars with fewer options. Tough times favor multi-purpose goods over specialized products, and weaker items in product lines should be pruned.

Marketing Advice from the “Professionals” - Part 3b

(Continued)

5. **Support distributors.** In uncertain times, no one wants to tie up working capital in excess inventories. Early-buy allowances, extended financing, and generous return policies motivate distributors to stock your full product line. This is particularly true with unproven new products. Be careful about expanding distribution to lower-priced channels; doing so can jeopardize existing relationships and your brand image. However, now may be the time to drop your weaker distributors and upgrade your sales force by recruiting those sacked by other companies.
6. **Adjust pricing tactics.** Customers will be shopping around for the best deals. You do not necessarily have to cut list prices, but you may need to offer more temporary price promotions, reduce thresholds for quantity discounts, extend credit to long-standing customers, and price smaller pack sizes more aggressively.
7. **Stress market share.** In all but a few technology categories where growth prospects are strong, companies are in a battle for market share and, in some cases, survival. Knowing your cost structure can ensure that any cuts or consolidation initiatives will save the most money with minimum customer impact. Other companies with healthy balance sheets can do so by acquiring weak competitors.
8. **Emphasize core values.** CEOs must spend more time with customers and remaining employees reassuring and helping shape their vision for tomorrow.

Successful companies do not abandon their marketing strategies in a recession; they adapt them.

John Quelch, Harvard Business School, March 3, 2008

(<http://hbswk.hbs.edu/item/5878.html>)



Transylvania County's Stated Comprehensive Goals



The following comprehensive goals are presented as a guide for Transylvania County's future development and growth.

- Preserve Transylvania County's distinctive rural character, mountain heritage, natural environment and ambiance, while promoting proactive planning and economic growth.
- Conserve the valuable land, water and air resources within the county, for present and future generations.
- Collaborate with the NC Department of Transportation to provide the best possible roads for Transylvania County and promote alternative transportation.
- Collaborate with the City of Brevard and Town of Rosman to supply reliable and safe drinking water, wastewater treatment and solid waste collection and disposal.
- Promote affordable, safe and adequate housing for all residents.
- Plan and provide appropriate public facilities and services for county residents and businesses. Promote the best use of land while protecting citizens' property rights.

And some final advice from Professor Ostergaard...

- **Survive... Be here for the recovery. Emerge stronger.**
- **What is your new business model? New strategy?**
- **Focus on existing customers to solidify existing relationships... Help them help you.**
- **What are you doing within the global marketplace? 1.2 billion Indian customers, 1.3 billion Chinese customers, .3 billion U.S. customers...**
- **Prepare for the unknown by studying how others in the past have coped with the unforeseeable and the unpredictable.**
- **Workforce Retention in WNC? How do you get the talent back during recovery?**
- **Weight resource allocation decisions. Not everything is a priority.**
- **Participatory Democracy... Beware politicians bearing gifts... As an old cattle farmer in Weaverville once told me about Washington...**

Poly-Ticks!

Contact Info

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