



Economic Indicators

Prepared by the Department of Finance • April 2006

The purpose of this report is to keep policy makers apprised of changes in the national and local economies that the Montgomery County Department of Finance believes may impact current and/or future revenues and expenditures.



*This report is also available through the Internet on the Montgomery County Web Page:
<http://www.montgomerycountymd.gov>*

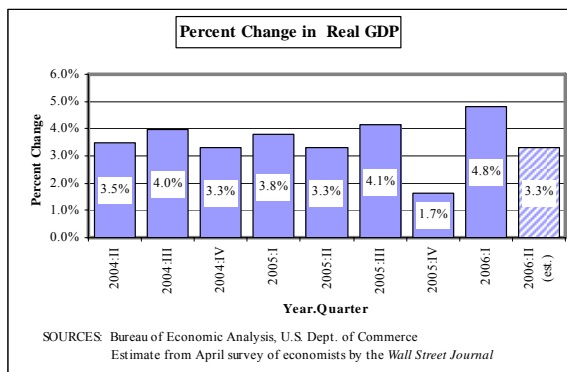
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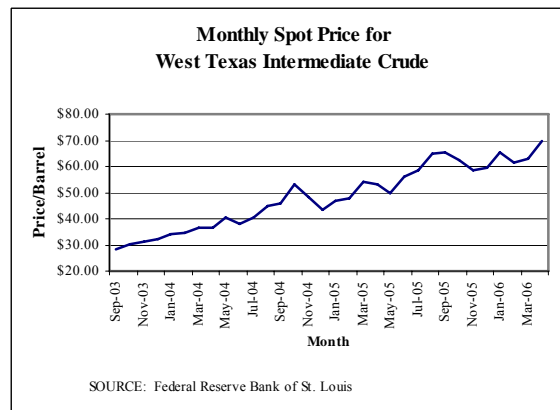
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ECONOMIC OVERVIEW

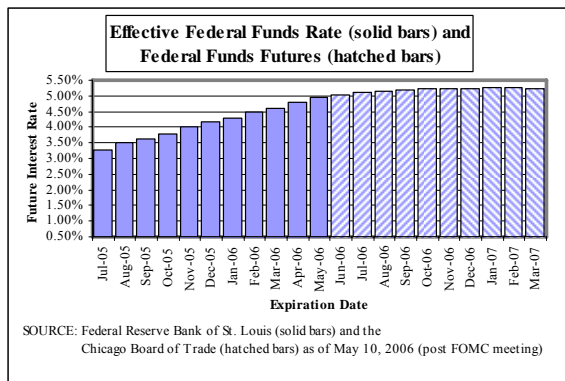
According to the latest economic data, the U.S. economy grew at a 4.8 percent seasonally adjusted annual rate during the first quarter of 2006 which was well above the 1.7 percent experienced during the fourth quarter of 2005 and slightly above the average forecast of 4.6 percent from the *Wall Street Journal* (WSJ) economic survey conducted in April. Although the rate is based on either incomplete data or data subject to revisions, the major contributors to the very strong increase were consumer purchases of durable goods (↑20.6%), a significant increase in business purchases of equipment and software (↑16.4%), and exports of goods (↑17.8%). Residential construction was up only 2.6 percent, which follows a similar increase of 2.8 percent during the fourth quarter of 2005 and the lowest increase since the fourth quarter of 2004. GDP is expected to grow 3.3 percent during the second quarter of this year according to the economists surveyed by the *WSJ*.



The price for West Texas Intermediate (WTI) crude increased to \$69.69 per barrel in April and surpasses the monthly price since September (Katrina level). The April price is \$16.65 above the price in April 2005 and \$33.00 above April 2004, or an increase of nearly 90 percent.



On May 10th, the Federal Open Market Committee (Committee) raised the target rate on federal funds to 5 percent, its sixteenth consecutive increase. The press release announcing the rate increase stated that “the Committee judges that some further policy firming may be needed to address inflation risks but emphasizes that the extent and timing of any such firming will depend importantly on the evolution of the economic outlook as implied by incoming information. In any event, the Committee will respond to changes in economic prospects as needed to support the attainment of its objectives.” Fed Chairman Bernanke stated before Joint Economic Committee, U.S. Congress, on April 27th that “future policy actions will be increasingly dependent on the evaluation of the economic outlook, as reflected in the incoming data.” Hence the press release essentially reiterates the Chairman’s remarks before Congress. The federal funds futures market forecasts no further increases until October at the earliest. However, the futures market may alter its predictions based on the performance of inflation. At present, the inflation indicator monitored by the Fed, the personal consumption expenditures index excluding energy and food, is at 2 percent which is at the high end of the Fed’s target range.



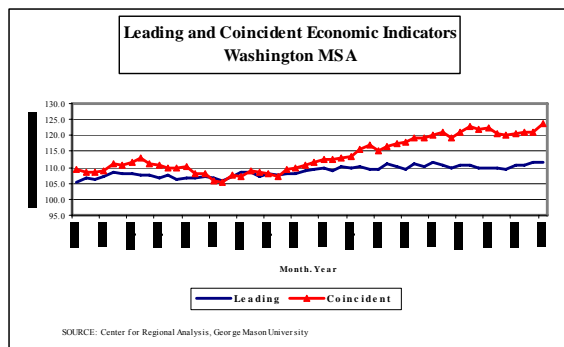
At the end of April, the stock market was up significantly for the year. Led by strong earnings reports and a healthy economy, the Dow Jones Industrial Average was up 2.3 percent for the month and 6.1 percent for the year. The S&P 500 was up 1.2 percent for the month and nearly 5.0 percent for the year. While the NASDAQ and Russell 2000 fared poorly for the month, down 0.7 percent and 0.1 percent, respectively, they both experienced strong yearly growth rates of 5.3 percent and 13.6 percent, respectively.

Recent economic releases showed mixed results in March and April. The Conference Board’s consumer confidence index increased in April (↑2.0%) for the third month in a row. However, the leading indicator of economic activity was down 0.1 percent in March for the second month in a row. The national economy added 138,000 jobs in April which followed increases of 200,000 in February and March. During the first four months of this year, the economy added nearly 700,000 payroll jobs and the unemployment rate stood 4.7 percent at a seasonally adjusted rate in April. Sales of existing homes were up in March to 6.9 million units at an annual rate, which was 0.3 percent above February sales but 0.7 percent below the March 2005 level. Sales of new single-family homes were up 13.8 percent compared to February’s sales but 7.2 percent below March 2005. Median home

prices are beginning to show signs of easing with the price of a new home decreasing from a high of \$243,900 in October to \$224,200 in March. The National Association of Realtors’ Pending Home Sales Index declined 1.2 percent in March for the second consecutive month. Since reaching a high in August of 128.2, the index has dropped 9.4 percent which confirms what many real estate analysts have claimed for some time, that the slowdown in home sales began during the late summer of 2005.

While the national economy grew 4.8 percent in the first quarter, the region’s economy grew only 2.3 percent during the first two months of this year according to the latest report from the Center for Regional Analysis (CRA), George Mason University. The Washington Leading Index, which is developed to forecast the performance of the regional economy six to eight months ahead, increased 0.2 percent in February for the fourth consecutive month.

According to CRA, the region’s economy “accelerated its expansion following a slow January with the Coincident Index up sharply driven by job growth and increased consumer spending.” The expansion is attributed to the addition of 71,600 net new jobs, an increase of 2.5 percent over the year, and consumer spending which increased 4.3 percent adjusted for inflation. CRA also points out that the February increase in its Leading Index, though small, suggests further expansion in the regional economy through the rest of this year. However, CRA is not so sanguine about the expansion continuing into 2007. Labor costs and inflationary expectations due to energy costs could forestall the expansion.



As stated by CRA's recent report on the regional economy, the hallmark of the region's economy is its ability to create jobs. For the twelve-month period ending in March, the regional economy generated nearly 76,300 jobs and has led the nation in job creation. The Bethesda-Gaithersburg-Frederick (B-G-F) metropolitan division added 15,700 jobs during the same twelve-month period and experienced the lowest unemployment rate, 2.6 percent, among the 34 most populous metropolitan divisions throughout the nation.

Concern about the vitality of the housing market in the Washington area is reflected in the latest report from PMI Mortgage, Inc. The likelihood that home prices in the Washington Metropolitan area, excluding B-G-F division, will decrease in the next two years increased from 15 percent in the winter of 2004 to nearly 40 percent in PMI's spring 2006 report. The probability that home prices will decline in the B-G-F corridor is an even more troubling 43 percent. Both metropolitan divisions have a significantly greater probability compared to the Baltimore-Towson area which has a probability of 28 percent. *Note that PMI's percentage indicates the probability of a decline, not that regional prices are projected to decline 40 or 43 percent.*

According to an article in the February's issue of *Regional Financial Review*, Mark Zandi of Moody's Economy.com states that

“a housing market correction, and not a collapse, is the most likely outlook, but the risks are decidedly on the downside. For example, he estimates that the housing market in the Bethesda-Gaithersburg-Frederick and Washington-Arlington-Alexandria metropolitan divisions is overvalued by nearly 32 percent. At the National Association of Home Builders Forecast Conference on April 27, Mr. Zandi stated that the Bethesda housing market may expect a 5 to 10 percent price decline while the remainder of the Washington region could experience a decline of 10 percent or more. Mr. Zandi also noted that such declines are contractions rather than collapses and suggests those declines would occur over an unspecified period of time rather than one year.

MONTGOMERY COUNTY ECONOMIC INDICATORS

Montgomery County experienced mixed economic activity during the first quarter of this year. The primary reasons for the County's mixed performance were a contraction in the growth of residential construction, a decline in housing sales particularly, and rising energy costs attributed to high oil prices.

However, a number of economic indicators for the County experienced significant improvement during this period. Foremost among the indicators that exhibited strong performance was the labor market. The County's businesses added an estimated 12,000 jobs to total payroll employment during the first quarter. The County's unemployment rate of 2.5 percent is one of the lowest in the State and suggests that the County is at or near full employment.

Residential construction in the County experienced a significant slowdown in 2006. Both the number of units and value added were down significantly during the first quarter compared to the same period in 2005. However, vacancy rates for office space in the County continued their downward trend in March improving to 7.2 percent in March.

It is against this backdrop of a strong labor market, high-energy costs, a decline in home sales, modest consumer spending, and weak construction activity that the Department of Finance estimates a slightly slower pace of growth in employment, a slight deceleration in the growth of personal income and wages and salaries, and somewhat higher yields on investment attributed to the policy of the Federal Reserve Board for 2006.

Employment Situation

In terms of the County's total payroll employment, over 14,000 jobs were added to the County's employment in 2004 and 2005. Based on preliminary data derived by the Department of Finance, the County's business establishments hired an additional 12,000 employees during the first quarter of this year compared to the same period in 2005.

While payroll employment made significant gains during the first quarter, preliminary data from the labor force series reported that employment based on place of residence grew 3.6 percent, or 17,400, compared to the January-March period of 2005. With significant improvement in resident employment, the unemployment rate for the County remained well below the State's average. As of March, the County's rate at 2.5 percent was a full percentage

point below the State's average and slightly below the region's 2.9 percent.

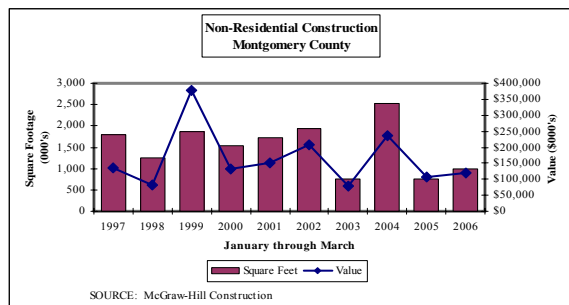
The County's payroll employment grew at a faster rate during the first quarter (↑ 2.8%) compared to the 2.7 percent for the entire Washington Metropolitan Area. The low unemployment rate also suggests that both the public and private sectors are providing a stable foundation against significant labor market volatility and that the County is close to full employment.

Construction Activity

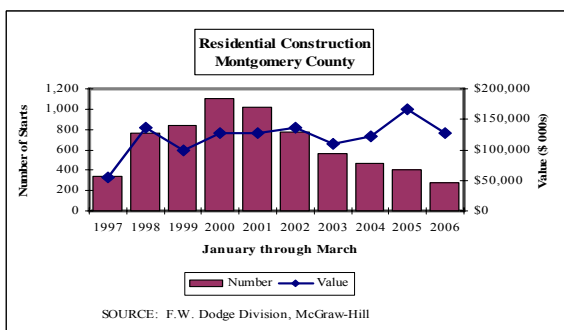
Construction activity in the County during the first quarter was mixed. While non-residential construction improved, construction of new homes declined dramatically compared to January-March 2005. With home sales and homebuilding declining in the County, the residential real estate market experienced a contraction during the first quarter.

The amount of square footage added to non-residential property through new construction increased 29.3 percent during the first quarter from 7.7 million square feet to 9.1 million square feet, while the value of new construction in the County increased nearly 13.0 percent. Additions of square footage by commercial property were up 81.0 percent and represented nearly all of the added non-residential capacity (9.0 million square feet). Vacancy rates in the County improved. After reaching a high of 10.3 percent in March 2005, the rate declined to 7.2 percent in March of this year and below the region's rate of 7.8 percent. That vacancy rate reflects an inventory of 1.9 million square feet of vacant office space (Class A properties). Fairfax County had a vacancy rate of 8.8 percent with 5.5 million square feet of vacant office space, the City of Alexandria and Arlington County had a

combined vacancy rate of 9.2 percent with 2.5 million square feet of vacant office space, and the District of Columbia had a vacancy rate of 6.5 percent with 4.3 million square feet of vacant office space.

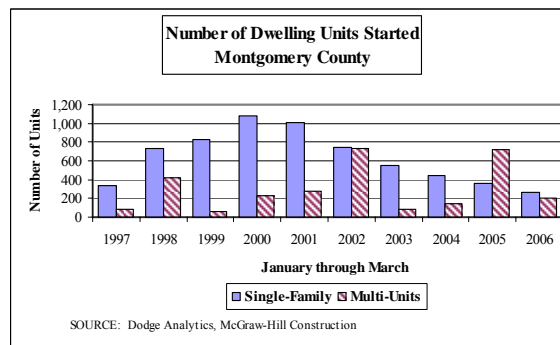


Residential construction experienced a dismal performance during the first quarter. Even with the mild winter weather, the number of new residential projects declined (↓32.3%) and the total value of new construction decreased nearly 24 percent. While it may be premature to draw any conclusions on homebuilding for the remainder of 2006 based on three months of data, declines during the first quarter in each of the five previous years signaled a decline for the entire year.



Based on data provided by McGraw-Hill Construction, the number of new single-family houses built in Montgomery County fell sharply from a little over 360 units during the first quarter of 2005 to less than 270 during January-March 2006 (↓25.8%) and the number of multi-family units declined from approximately 716 units in

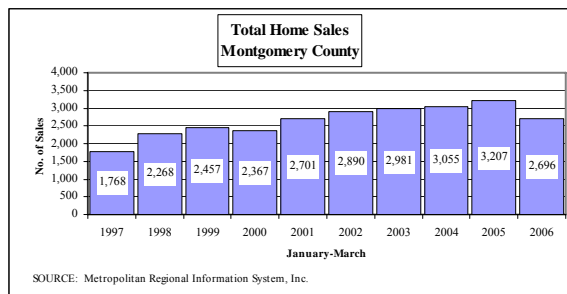
2005 to slightly above 200 units during the first quarter of this year (↓70.8%).



Residential Real Estate

The housing market in Montgomery County experienced a contraction during the first quarter. Since November of last year, home sales have declined dramatically. During the first three months of this year, home sales declined 15.9 percent compared to the same period in 2005. This dramatic drop, however, did not translate into a collapse in home prices. On the contrary, home prices were up 11.7 percent for the quarter compared to the January-March 2005 period. On a fiscal year basis, home sales were down 13.0 percent during the July 2005 to March 2006 period compared to the same period for fiscal year 2005. Home prices, on the other hand, have not contracted. They were up 17.4 percent for this fiscal year to date. The contraction in sales is reflected in the dramatic increase in inventory-to-sales ratio. Since August, the ratio increased from 1.37 to 4.16 in March. This means that in August for every home listed on the market, there was one buyer. By March, for every four homes listed, there was only one buyer. Such a dramatic increase in the ratio suggests that buyers are not in a rush to purchase a home compared to 2004 and 2005. Such action may be attributed to an affordability issue or the potential buyer is anticipating a significant deceleration in prices. As a result, because

of the modest increase in mortgage rates and the anticipation of a decline in home prices, potential home buyers are sitting on the sidelines and as such the market has shifted from a seller's market to a buyer's.



Retail Sales

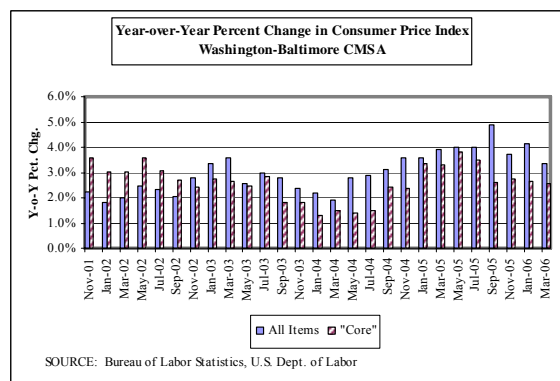
Using sales tax receipts as a measure of the level of retail sales for the County, retail sales were up 8.9 percent in March compared to March 2005 and up 6.0 percent during the first quarter of this year compared to the same period in 2005. The sale of nondurable goods, which includes food and beverage, apparel, general merchandise, and utilities and transportation, increased 5.9 percent during the quarter while purchases of durable goods were down 2.4 percent.

For the three-month period, purchases of energy products (↑13.4%), food (↑6.1%), and apparel (↑5.0%) led sales of nondurable goods. Purchases of building and industrial supplies (↑19.9%) led sales of durable goods followed by hardware, machinery and equipment (↑9.2%). However, consumer

purchases of the “big ticket” items were down compared to the first three months of last year. Purchases of furniture and appliances were off 23.4 percent and automotive products were up only 1.4 percent. The dramatic decline in furniture and appliance expenditures could be attributed to the decline in home sales.

Consumer Prices and Inflation

As measured by the Consumer Price Index for All Urban Consumers (CPI-U), inflation in the Washington-Baltimore consolidated statistical metropolitan area increased 3.3 percent over the twelve-month period ending in March. That rate was slightly below the national average of 3.4 percent. Consumer prices excluding food and energy purchases were up 2.5 percent in the region, based on the latest data available compared to 2.1 percent for the nation.



SELECTED ECONOMIC INDICATORS	Reporting Period	Current Period	Prior Year's Period	Year To-Date		2005
				2006	2005	
Leading Indicators						
National	Mar	-0.1%		2.1%		1.8%
Washington MSA	Feb	0.2%		0.6%		-0.1%
Coincident Indicators						
National	Mar	0.2%		2.3%		1.5%
Washington MSA	Feb	2.1%		2.3%		1.7%
Consumer Confidence Index						
National	Apr	2.0%		4.0%		1.1%
South Atlantic Region	Apr	8.2%		6.7%		2.7%
Consumer Sentiment (University of Michigan)	Mar	2.5%		-5.5%		-5.8%
Consumer Price Index						
<u>All Items (nsa)</u>						
National	Mar	3.4%		3.6%		3.4%
Washington - Baltimore CMSA	Mar	3.3%		3.7%		4.0%
<u>Core CPI (nsa)</u>						
National	Mar	2.1%		2.1%		2.2%
Washington - Baltimore CMSA	Mar	2.5%		2.6%		3.2%
Retail Trade						
National (sales - nsa)	Mar	7.6%		8.2%		6.9%
Washington MSA (sales - nsa)	Feb	6.3%		7.1%		6.8%
Maryland (sales tax)	Mar	9.7%		8.1%		6.4%
Montgomery County (sales tax)	Mar	8.9%		6.0%		5.0%
Employment						
National (labor force data - nsa)	Apr	143,405,000	140,939,000	142,413,000	139,620,000	141,730,000
- Percent Change		1.7%		2.0%		1.8%
Bethesda-Federick-Gaithersburg (establish.)	Mar	576,500	560,800	572,600	558,500	570,900
- Percent Change		2.8%		2.5%		0.9%
Montgomery County (labor force data)	Mar	502,425	484,189	500,156	482,765	491,801
- Percent Change		3.8%		3.6%		2.1%
Montgomery County (ES-202)	Sept '05(a)	462,450	450,550	456,460	447,183	449,397
- Percent Change		2.6%		2.1%		2.0%
Unemployment						
National (nsa)	Apr	4.5%	4.9%	4.9%	5.5%	5.1%
Maryland (nsa)	Mar	3.5%	4.5%	3.8%	4.6%	4.1%
Bethesda-Federick-Gaithersburg (nsa)	Mar	2.6%	3.4%	2.8%	3.4%	3.1%
Montgomery County (nsa)	Mar	2.5%	3.4%	2.7%	3.5%	3.1%
Construction						
<u>Construction Starts - Montgomery County</u>						
Total (\$ thousand)	Mar	\$38,545	\$71,024	\$247,420	\$273,614	\$1,286,612
- Percent Change		-45.7%		-9.6%		0.1%
Residential (\$ thousand)	Mar	\$31,960	\$48,851	\$126,860	\$166,730	\$742,279
- Percent Change		-34.6%		-23.9%		9.6%
Non-Residential (\$ thousand)	Mar	\$6,585	\$22,173	\$120,561	\$106,884	\$544,333
- Percent Change		-70.3%		12.8%		-10.4%
<u>Building Permits (Residential)</u>						
National	Mar	191,266	185,587	496,025	475,150	2,147,617
- Percent Change		3.1%		4.4%		6.1%
Maryland	Mar	2,448	3,594	6,135	7,999	32,276
- Percent Change		-31.9%		-23.3%		13.7%
Montgomery County	Mar	102	833	283	1,332	3,564
- Percent Change		-87.8%		-78.8%		-6.2%
<u>Building Permits (Non-Residential)</u>						
Montgomery County	Mar	125	339	455	639	2,154
- Percent Change		-63.1%		-28.8%		9.6%
Real Estate						
<u>National</u>						
Sales (saar)	Mar	6,920,000	6,970,000	6,800,000	6,940,000	7,075,000
- Percent Change		-0.7%		-2.0%		4.4%
Median Price	Mar	\$218,000	\$203,000	\$220,000	\$193,667	\$219,600
- Percent Change		7.4%		13.6%		12.4%
<u>Montgomery County</u>						
Sales	Mar	1,105	1,218	2,696	3,207	17,011
- Percent Change		-9.3%		-15.9%		-4.2%
Average Price	Mar	\$507,297	\$468,348	\$505,592	\$454,744	\$507,340
- Percent Change		8.3%		11.2%		18.1%
Median Price	Mar	\$427,500	\$393,450	\$419,917	\$379,458	\$425,000
- Percent Change		8.7%		10.7%		19.7%
Average Days on the Market	Mar	50	26	53	33	25

NOTES:

(nsa): not seasonally adjusted

(saar): seasonally adjusted at annual rates

(a): Year-to-date data are for 2005 and 2004 respectively. Annual data are for 2004.