

*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>*

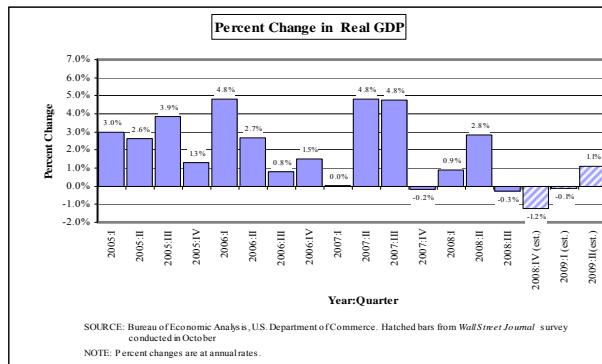
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### NATIONAL ECONOMY

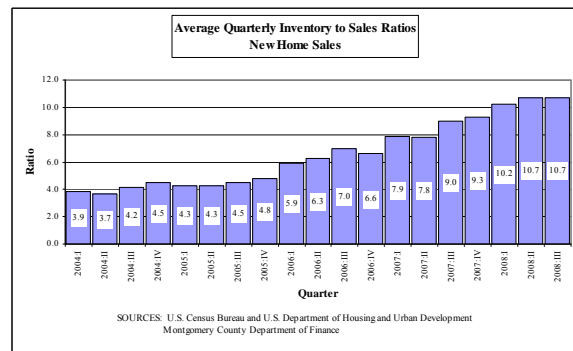
According to the advance estimate from the Bureau of Economic Analysis (BEA), U.S. Department of Commerce, gross domestic product (GDP) decreased at a 0.3 percent seasonally adjusted annual rate during the third quarter – the first such decrease since the fourth quarter of 2007. That decrease followed a 0.9 percent increase during the first quarter and a 2.8 percent increase during the second quarter. Based on the recent *Wall Street Journal* survey of fifty economists conducted in early October, economic growth during the fourth quarter of this year and the first quarter of next year are expected to decrease 1.2 percent and 0.1 percent, respectively. However, the survey was conducted prior to the dramatic decline in the stock market.



The decrease in real GDP was attributed to declines in consumer spending (↓3.1%), which was led by a decrease in purchases of durable goods (↓14.1%); a decline in residential construction (↓19.1%); and business purchases of equipment and software (↓5.5%). Purchases of durable goods declined for the third quarter in a row, purchases of equipment and software also declined for the third quarter in a row, and residential construction declined for the eleventh quarter in a row.

According to a recent forecast by the National Home Builders Association, residential construction will continue to decline in the fourth quarter and into the first quarter of next year. Residential construction is expected to increase 2.0 percent by the second quarter of next year according to NAHB’s forecast.

The justification for the continuing decline is that the inventory-to-sales ratio for new homes remains at an historic high level. Based on data from the Bureau of the Census and the U.S. Department of Housing and Urban Development, that ratio has increased steadily from a low of 3.7 during the second quarter of 2004 to 10.7 during the third quarter of this year.



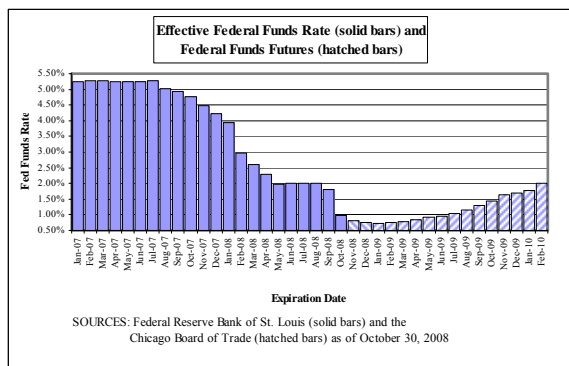
Inventories of existing homes for sale also remain at historically high levels. Since July 2007, the inventory-to-sales ratio has averaged 10.3. That ratio translates into at least a 10-month supply of homes on the market. To put that value in perspective, the average inventory-to-sales ratio between 2000 and 2005 was 4.5 – less than one half the current inventory level.

Sales of existing homes dropped 15.8 percent during the first three quarters of this year compared to the same period last year. That decrease followed a 10.6 percent decline during the first three quarters of 2007. Median prices decreased 7.7 percent between January and September compared

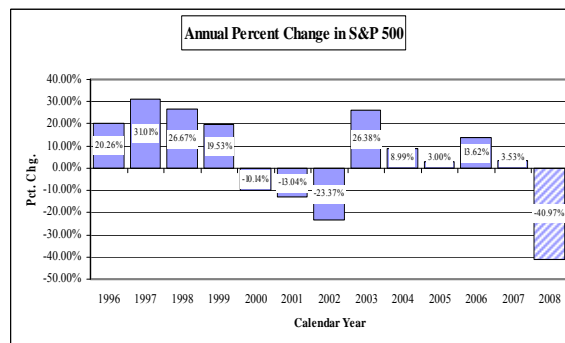
to the same period last year. Average prices decreased 7.3 percent.

Business capital spending as measured by new orders for non-defense capital goods excluding aircraft decreased 0.7 percent during the third quarter compared to increases of 1.1 and 2.5 percent for the first and second quarters, respectively. That decrease coupled with three consecutive declines in investment in equipment and software (GDP component) suggests that businesses are less than sanguine about an economic recovery in the near term. Case in point, during the last recession, new orders declined nearly 17 percent between April and November 2001 (dates of the last recession as determined by NBER) compared to April and November 2000.

Because of the continuing turmoil in the housing market, as a result of the subprime mortgage crisis creating a credit crisis that started in the summer of 2007, the Federal Open Market Committee (FOMC) of the Federal Reserve (Fed) began aggressive rate cuts starting in September 2007. Since that time, the FOMC has cut the target rate on federal funds from 5.25 percent to 1.00 percent. The futures market for 30-day federal funds anticipates that the FOMC will cut the rate an additional 25 basis points at its next meeting in December.



Since the start of the year, the S&P 500 index has decreased 36.6 percent (for the week ending November 7). At that rate, the index could decrease by nearly 41 percent by year end – that decline would match the three year decline in the index between 2000 and 2002. That estimated year-end decline is also reflected in the Dow Jones Industrial Average (↓36.6%), the NASDAQ (↓42.4 %) and the Russell 2000 (↓38.1%).



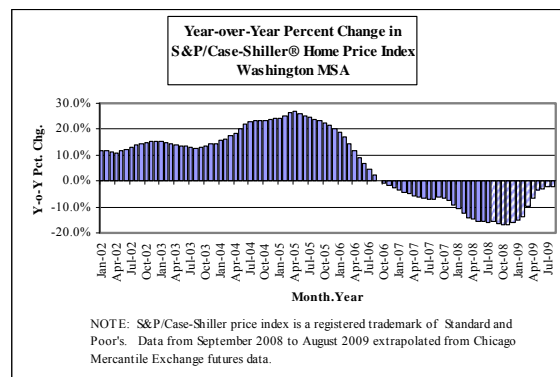
## REGIONAL ECONOMY

According to the latest report from the Center for Regional Analysis (CRA), George Mason University, “the Washington area economy has been spared the full impact of the negative forces at work on the economy.” However, the Washington region’s economy “continues to struggle in response to growing weakness at the national level – weakness in home building industry, turmoil in the financial markets, inflation pressures, and slower consumer spending.” However, while national payroll employment has declined by 1.2 million since the start of the year (data through October), payroll employment in the Washington region has increased on average by 31,300 (data through September). While the unemployment rate at the national level reached 6.0 percent (not seasonally adjusted) in September, the region’s unemployment rate was two full percentage points lower (4.0%). However, there are indications that

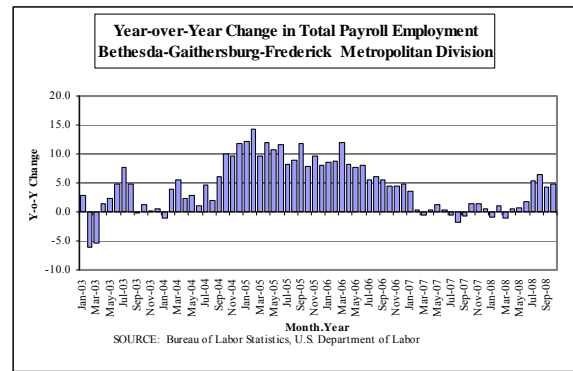
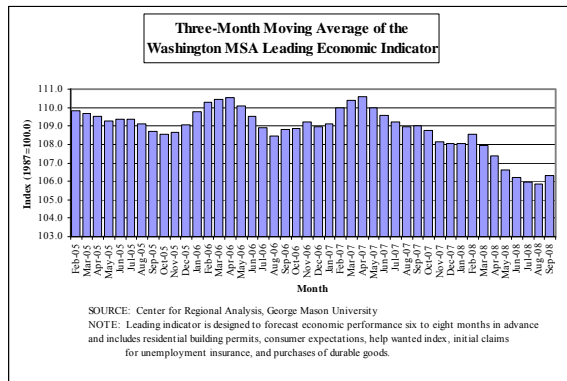
the local economy remains weak. Among those indicators are consumer confidence and home prices.

Consumer confidence decreased 44.6 percent in October, the January-October average stood at 45.8 percent below the same period last year. If consumer confidence does not improve, consumers will be reluctant to spend and invest, particularly on purchases of durable goods. While purchases of non-durable goods increased 7.1 percent during the first five months of this year compared to the same period last year, purchases of durable goods increased a meager 2.1 percent over the same comparative period. While the effects of the 2008 tax rebate may have increased sales of durable goods according to a study by Christian Broda (University of Chicago) and Jonathan Parker (Northwestern University), their findings underscore the limited effects of the economic stimulus package in stabilizing consumer spending. However, further declines in consumer confidence post fiscal stimulus could have an effect on consumer spending particularly deterioration in purchases of durable goods.

The second indicator reflecting a weakness in the region's economy is home prices. Prices continued to weaken since May 2006. Based on the S&P/Case-Shiller® Home Price Index for the Washington region, monthly prices have steadily declined such that the August index, the latest data available to date, was 15.4 percent below August 2007 and 22.4 percent below the May 2006 peak. According to futures traded on the Chicago Mercantile Exchange, regional home prices may decline an additional 8.1 percent by February of next year bringing the total decline in home prices to 29.7 percent since the May 2006.



The Washington Leading Index, which forecasts the performance of the regional economy six to eight months ahead, increased 0.3 percent in August, the latest date for which data are available. However, on a year-over-year basis, the index decreased 2.7 percent since August 2007. The performance of three of the index's five components contributed to its decline: (1) purchases of durable goods (on a seasonally adjusted basis), (2) the Help Wanted Index, and (3) residential housing permits. According to CRA, this performance of the index suggests that "the Leading Index continues to point to slower growth, falling 2.7 percent lower than its August 2007 level." Although the index registered positive gains in July and August, further increases will vary with economic trends. Given that the index is through August, the effects of the dramatic decline in the stock market during October have not been reflected in the index, particularly consumer expectations.



## MONTGOMERY COUNTY ECONOMIC INDICATORS

The coincident index, which measures the current state of the region’s economy, decreased 0.6 percent in August and is down 5.1 percent from August 2007. The August decrease was attributed to a decrease in purchases of nondurable goods (on a seasonally adjusted basis) and consumer confidence.

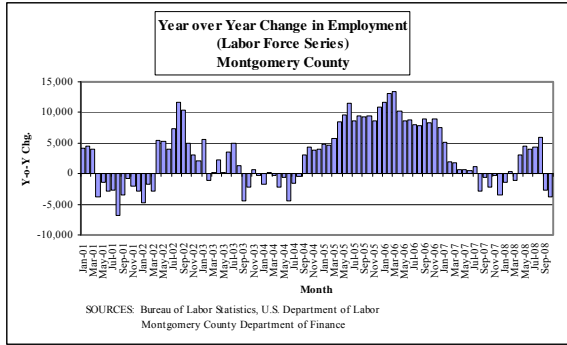
Montgomery County has experienced weak economic performance during calendar year 2008. The primary reasons for the County’s weak performance were modest growth in employment based on the labor force (resident employment) series and little growth based on the establishment (payroll) series, a continuation in the decline of home sales and the high level of inventory-to-sales ratio, and weak construction in residential properties.

As stated previously, the Washington metropolitan area continues to have one of the lowest unemployment rates in the country. Of the 49 metropolitan areas with a population of more than one million in 2000, the Washington region had the second lowest unemployment rate (4.0%) in September and the third largest employment increase among the 310 metropolitan areas (↑40,700). The Bethesda-Gaithersburg-Frederick metropolitan division continued to report the lowest jobless rate (3.4%) among the 34 metropolitan divisions. However, that low unemployment rate did not translate into job growth. In fact, during the January-September period, average monthly payroll employment stood at 577,300 compared to an average of 575,100 during the same period in 2007 – an increase of slightly more than 2,200 (↑0.4%). Essentially, there was little job growth over the past year in Montgomery and Frederick counties.

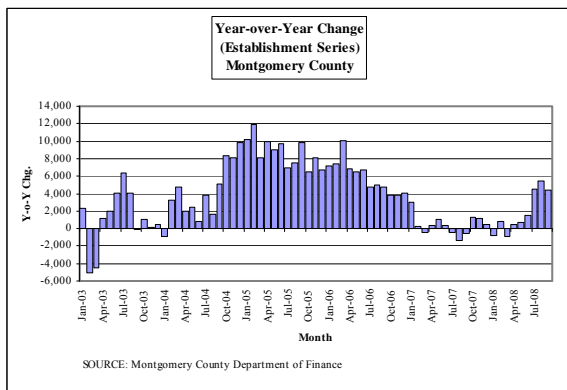
### *Employment Situation*

Based on data from the Maryland Department of Labor, Licensing and Regulation (DLLR) and the Bureau of Labor Statistics, (BLS) U.S. Department of Labor, resident employment (labor force series and not seasonally adjusted) in Montgomery County decreased by 2,300 in September compared to September 2007. Over the ninth month period ending in September, total resident employment averaged approximately 500,000 per month – an increase of only 1,900 over the same nine-month period in 2007.





Payroll employment is derived by the Department of Finance (Treasury Division) using BLS and DLLR data. The County’s total payroll employment increased by 1,800 (↑0.3%) during the nine-month period ending in September. Throughout 2008, the monthly average of payroll employment experienced very little growth in the County. Employment stood at a monthly average of 484,100 jobs compared to 482,300 jobs during the same period in 2007. With both resident and payroll employment indicating little growth, any increase in income tax revenues during this fiscal year and into next fiscal year will be based on growth in wages and salaries rather than employment or no “real” or inflation adjusted growth.

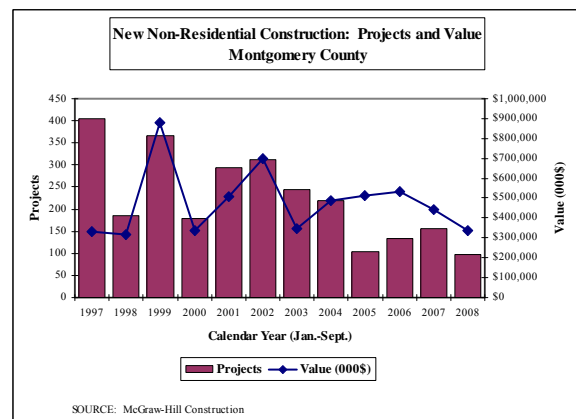


While the employment situation remains meager in terms of growth, the unemployment rate of 3.3 percent in September remains one of the lowest in the State (4.5% not seasonally adjusted).

Howard County had the same unemployment rate.

### Construction Activity

Construction activity experienced mixed results during the first nine months of 2008. While the total number of projects decreased (↓8.9%), the total value added was also lower compared to the same period last year (↓17.1%). The decrease in additional value was attributed to both a significant decline in the value of residential construction (↓24.3%) and, to a lesser extent, non-residential construction (↓9.4%).



The number of non-residential construction projects has been down 37.6 percent during the first nine months of 2008 compared to the same period last year. While the number of non-residential construction projects decreased during this period, the total amount of additional value also decreased (↓9.4%). The major contributor to that decrease was manufacturing (↓100.0%), education and science (↓80.4%), and amusement (↓80.4%) facilities. Construction of stores and food service facilities (↓17.1%) and hotels and motels (↓53.2%) also led to the decline in non-residential construction.

The office vacancy rate for Class A property in the County was 9.5 percent

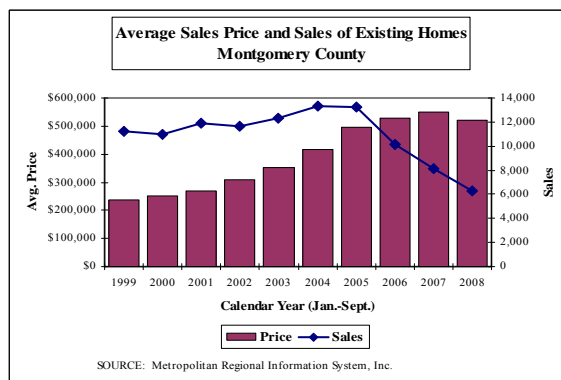
during the third quarter of this year, up from the 8.9 percent during the second quarter, and represents the highest rate since the first quarter of 2005. The vacancy rate for Montgomery County is below the regional average of 11.0 percent and is the fourth lowest among the seven jurisdictions.

**Residential Real Estate**

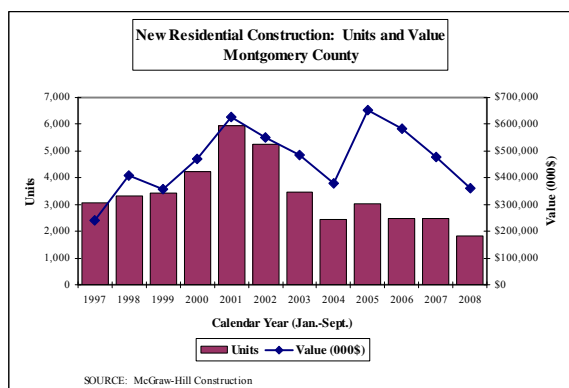
Led by the decline in the building of new multi-family units (↓39.5%), overall residential construction continued to decrease during the first nine months of 2008 in response to the correction in the real estate market that began in the summer of 2005. Construction of new residential units declined 27.6 percent. The overall added value of new residential construction declined 24.3 percent. While the County continues to add residential property to its property tax base, it has been doing so at a decreasing rate since 2005, the peak of the housing boom.

At the same time that the number of total residential construction starts declined during 2008, the number of units authorized, i.e., permitted, has decreased 54.0 percent during this period based on data from the Census Bureau. The number of permitted units decreased from nearly 2,900 during the January-September 2008 period to over 1,330 units during the same period this year.

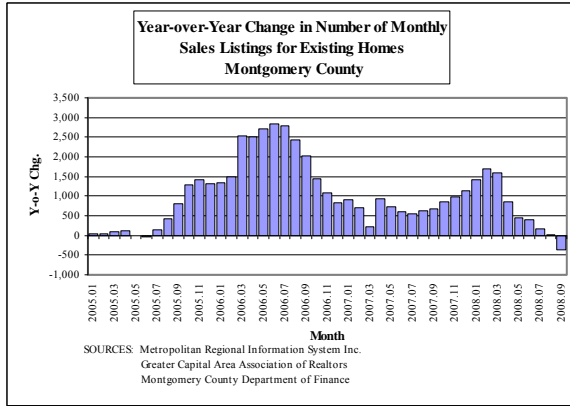
During 2008, home sales declined 22.9 percent, which followed a 19.6 percent decline during the same nine month period last year. Average home prices have also declined 5.4 percent which followed increases of 6.1 percent and 4.4 percent during the same periods in 2006 and 2007, respectively.



The significant contraction in sales is reflected in the dramatic high level in the inventory-to-sales ratio. From June 2005 to January of this year, the ratio steadily increased from 0.98 to 11.4. However, that ratio has steadily declined from its peak to a ratio of 7.0 in September. This means that for every seven homes listed on the market in September, there was one buyer. In January, for every eleven to twelve homes listed, there was only one buyer. While there has been a decline in the ratio since January, it remains well above the June 2007 inventory-to-sales ratio of 4.8 and suggests that monthly home sales and listings will continue to decline compared to the same month the previous year. Although a lower ratio can be an indicator of an improving market, the recent decline is more likely due to residents withdrawing their homes for sale from the market as opposed to an up tick in demand.







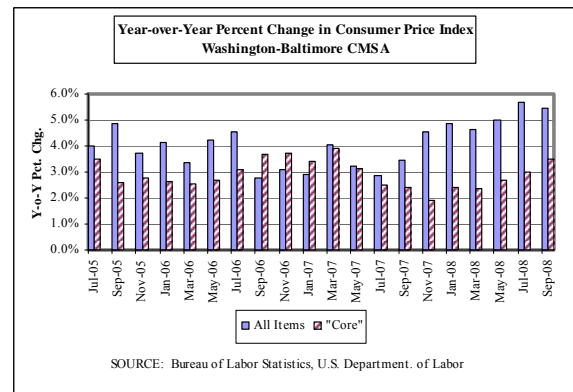
**Retail Sales**

Using sales tax receipts as a measure of retail sales activity in the County, the growth in sales of durable and nondurable goods, excluding miscellaneous and assessment collection, were down 1.8 percent (adjusted for the rate increase) during the first eight months of this calendar year compared to the same period in 2007. Purchases of nondurable goods, which include food and beverage, apparel, general merchandise, and utilities and transportation, increased 2.8 percent during this period while sales of durable goods were down 11.1 percent.

Purchases of utilities and transportation (↑8.1%), food and beverages (↑2.7%), and general merchandise (↑1.9%) led sales of nondurable goods. Purchases of building and industrial supplies (↓11.1%), furniture and appliances (↓15.9%) and automotive (↓6.6%) also declined.

**Consumer Prices and Inflation**

As measured by the Consumer Price Index for All Urban Consumers (CPI-U), inflation in the Washington-Baltimore region increased 5.5 percent on a year-over-year basis in September, i.e., September 2008 over September 2007, and above the year-over-year national average of 4.9 percent. That increase in the region’s index was the second largest since the data index has been tabulated by the Bureau of Labor Statistics, U.S. Department of Labor. A major factor in the difference between the regional and national index was the increase in the gasoline component of the index. That component increased 33.8 percent from September 2007 to September 2008 for the region compared to 31.7 percent nationwide. Consumer prices excluding food and energy purchases were up 3.5 percent in the region (on a year-over-year basis), which was significantly higher than the increase for the nation (↑2.5%) over the same September 2007-to-September 2008 period.



### METROPOLITAN AREA OFFICE MARKET

#### Direct Office Vacancy Rate by Jurisdiction and Class, 2008:3Q

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	21.41%	11.77%	9.91%	16.90%
Fairfax	13.25%	12.49%	5.17%	12.68%
Frederick	5.51%	11.72%	6.36%	9.02%
Alexandria/Arlington	8.41%	6.35%	5.31%	7.36%
<b>Montgomery</b>	<b>9.49%</b>	<b>8.68%</b>	<b>7.82%</b>	<b>8.99%</b>
District of Columbia	8.27%	4.47%	5.20%	6.75%
Prince George's	23.27%	13.73%	6.93%	16.16%
<i>Metropolitan Area</i>	10.98%	8.70%	6.07%	9.74%

#### Direct Vacant Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	1,724,549	740,410	57,444	2,522,403
Fairfax	9,007,429	4,861,064	211,143	14,079,636
Frederick	115,761	478,839	86,453	681,053
Alexandria/Arlington	2,567,288	1,336,105	281,057	4,184,450
<b>Montgomery</b>	<b>2,958,993</b>	<b>2,333,436</b>	<b>512,802</b>	<b>5,805,231</b>
District of Columbia	6,442,877	1,994,662	564,069	9,001,608
Prince George's	2,051,909	1,607,539	256,416	3,915,864
<i>Region</i>	24,868,806	13,352,055	1,969,384	40,190,245

#### Office Space Inventory by Jurisdiction and Class (sq.ft.)

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	8,055,919	6,291,225	579,617	14,926,761
Fairfax	67,991,873	38,921,811	4,082,529	110,996,213
Frederick	2,101,534	4,086,539	1,359,709	7,547,782
Alexandria/Arlington	30,524,095	21,050,601	5,296,925	56,871,621
<b>Montgomery</b>	<b>31,164,647</b>	<b>26,885,183</b>	<b>6,559,682</b>	<b>64,609,512</b>
District of Columbia	77,880,581	44,576,585	10,843,859	133,301,025
Prince George's	8,817,191	11,704,901	3,702,638	24,224,730
<i>Region</i>	226,535,840	153,516,845	32,424,959	412,477,644

#### Share of Office Space Inventory by Jurisdiction and Class

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	54.0%	42.1%	3.9%	100.0%
Fairfax	61.3%	35.1%	3.7%	100.0%
Frederick	27.8%	54.1%	18.0%	100.0%
Alexandria/Arlington	53.7%	37.0%	9.3%	100.0%
<b>Montgomery</b>	<b>48.2%</b>	<b>41.6%</b>	<b>10.2%</b>	<b>100.0%</b>
District of Columbia	58.4%	33.4%	8.1%	100.0%
Prince George's	36.4%	48.3%	15.3%	100.0%
<i>Metropolitan Area</i>	54.9%	37.2%	7.9%	100.0%

#### Share of Total Regional Vacant Office Space by Jurisdiction and Class

<i>Jurisdiction</i>	Class A	Class B	Class C	Total
Loudoun	6.9%	5.5%	2.9%	6.3%
Fairfax	36.2%	36.4%	10.7%	35.0%
Frederick	0.5%	3.6%	4.4%	1.7%
Alexandria/Arlington	10.3%	10.0%	14.3%	10.4%
<b>Montgomery</b>	<b>11.9%</b>	<b>17.5%</b>	<b>26.0%</b>	<b>14.4%</b>
District of Columbia	25.9%	14.9%	28.6%	22.4%
Prince George's	8.3%	12.0%	13.0%	9.7%
<i>Total</i>	<i>100.0%</i>	<i>100.0%</i>	<i>100.0%</i>	<i>100.0%</i>

<u>SELECTED ECONOMIC INDICATORS</u>	Reporting Period	Current Period	Prior Year's Period	Year To-Date		Annual 2007
				2008	2007	
<b>Leading Indicators</b>						
National	Sept. '08	0.3%		-2.3%		-1.7%
Washington MSA	Aug. '08	0.3%		-2.7%		-0.4%
<b>Coincident Indicators</b>						
National	Sept. '08	-0.5%		0.1%		1.1%
Washington MSA	Aug. '08	-0.6%		-5.1%		-4.8%
<b>Consumer Confidence Index</b>						
National	Oct. '08	-38.1%		-42.4%		-17.6%
South Atlantic Region	Oct. '08	-44.6%		-45.8%		-29.9%
Consumer Sentiment (University of Michigan)	Oct. '08	-18.1%		-25.8%		-17.7%
<b>Consumer Price Index</b>						
<u>All Items (nsa)</u>						
National	Sept. '08	4.9%		4.6%		2.8%
Washington - Baltimore CMSA	Sept. '08	5.5%		5.1%		3.6%
<u>Core CPI (nsa)</u>						
National	Sept. '08	2.5%		2.4%		2.3%
Washington - Baltimore CMSA	Sept. '08	3.5%		2.8%		2.8%
<b>Retail Trade</b>						
National (sales - nsa)	Sept. '08	0.0%		2.5%		4.1%
Washington MSA (sales - nsa)	Aug. '08	4.3%		5.0%		3.9%
Maryland (sales tax)(1)	Aug. '08	-3.0%		-3.1%		1.6%
Montgomery County (sales tax)(1)	Aug. '08	-4.3%		-2.8%		0.1%
<b>Employment</b>						
National (labor force data - nsa)	Sept. '08	145,310,000	146,448,000	145,650,000	145,818,000	146,047,000
- Percent Change		-0.8%		-0.1%		1.1%
Bethesda-Federick-Gaithersburg (establish.)	Sept. '08	582,700	577,400	577,300	575,100	576,700
- Percent Change		0.9%		0.4%		0.1%
Montgomery County (labor force data)	Sept. '08	495,496	497,800	500,002	498,093	498,279
- Percent Change		-0.5%		0.4%		0.0%
Montgomery County (QCEW)(p)	Mar. '08	455,683	457,331	454,635	455,155	459,346
- Percent Change		-0.4%		-0.1%		-1.2%
<b>Unemployment</b>						
National (nsa)	Sept. '08	6.0%	4.5%	5.5%	4.7%	4.6%
Maryland (nsa)	Sept. '08	4.5%	3.4%	4.0%	3.6%	3.6%
Montgomery County (nsa)	Sept. '08	3.3%	2.7%	3.0%	2.8%	2.7%
<b>Construction</b>						
<u>Construction Starts - Montgomery County</u>						
Total (\$ thousands)	Sept. '08	\$55,952	\$56,349	\$760,299	\$917,426	\$1,343,352
- Percent Change		-0.7%		-17.1%		-6.2%
Residential (\$ thousands)	Sept. '08	\$15,640	\$28,809	\$361,141	\$476,923	\$668,329
- Percent Change		-45.7%		-24.3%		-6.8%
Non-Residential (\$ thousands)	Sept. '08	\$40,312	\$27,540	\$399,158	\$440,503	\$675,023
- Percent Change		46.4%		-9.4%		-5.5%
<u>Building Permits (Residential)</u>						
National	Sept. '08	68,790	97,722	749,924	1,113,484	1,380,470
- Percent Change		-29.6%		-32.7%		-24.9%
Maryland	Sept. '08	1,063	948	11,915	16,543	19,940
- Percent Change		12.1%		-28.0%		-14.3%
Montgomery County	Sept. '08	249	80	1,329	2,888	3,459
- Percent Change		211.3%		-54.0%		14.1%
<u>Building Permits (Non-Residential)</u>						
Montgomery County	Sept. '08	146	130	1,431	1,286	1,661
- Percent Change		12.3%		11.3%		-6.4%
<b>Real Estate</b>						
<u>National</u>						
Sales (saar)	Sept. '08	5,180,000	5,110,000	4,966,700	5,896,700	5,652,000
- Percent Change		1.4%		-15.8%		-12.8%
Median Price	Sept. '08	\$191,600	\$210,500	\$202,700	\$219,700	\$219,000
- Percent Change		-9.0%		-7.7%		-1.3%
<u>Montgomery County</u>						
Sales	Sept. '08	768	583	6,263	8,128	10,360
- Percent Change		31.7%		-22.9%		-23.4%
Average Price	Sept. '08	\$458,036	\$511,437	\$520,293	\$549,994	\$550,210
- Percent Change		-10.4%		-5.4%		3.9%
Median Price	Sept. '08	\$350,000	\$415,000	\$407,444	\$447,389	\$444,000
- Percent Change		-15.7%		-8.9%		1.1%
Average Days on the Market	Sept. '08	101	82	105	82	84

**NOTES:**

(nsa): not seasonally adjusted

(p): annual data are preliminary

(1): Data adjusted for rate increase