



# *Indiana* **Business Review**



## **Outlook 2006**

**Winter 2005**

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# Outlook for 2006

**Jerry Conover**

Director, Indiana Business Research Center, Kelley School of Business, Indiana University

Following a tradition established more than a third of a century ago, a group of faculty gathered at the Kelley School of Business in October 2005 to discuss the economic outlook for the year ahead. Their goal was to forecast the prospects for 2006 in terms of global, national, state, and metropolitan perspectives, as well as to assess the outlooks for the financial and housing markets.

This discussion began with a review of the latest forecast based on the econometric model of the U.S. developed by Indiana University's Center for Econometric Model Research (CEMR). The professors then made adjustments to the model's predictions to accommodate expectations about key underlying variables. The CEMR model of Indiana's economy similarly provided a basis for projecting the outlook for the state.

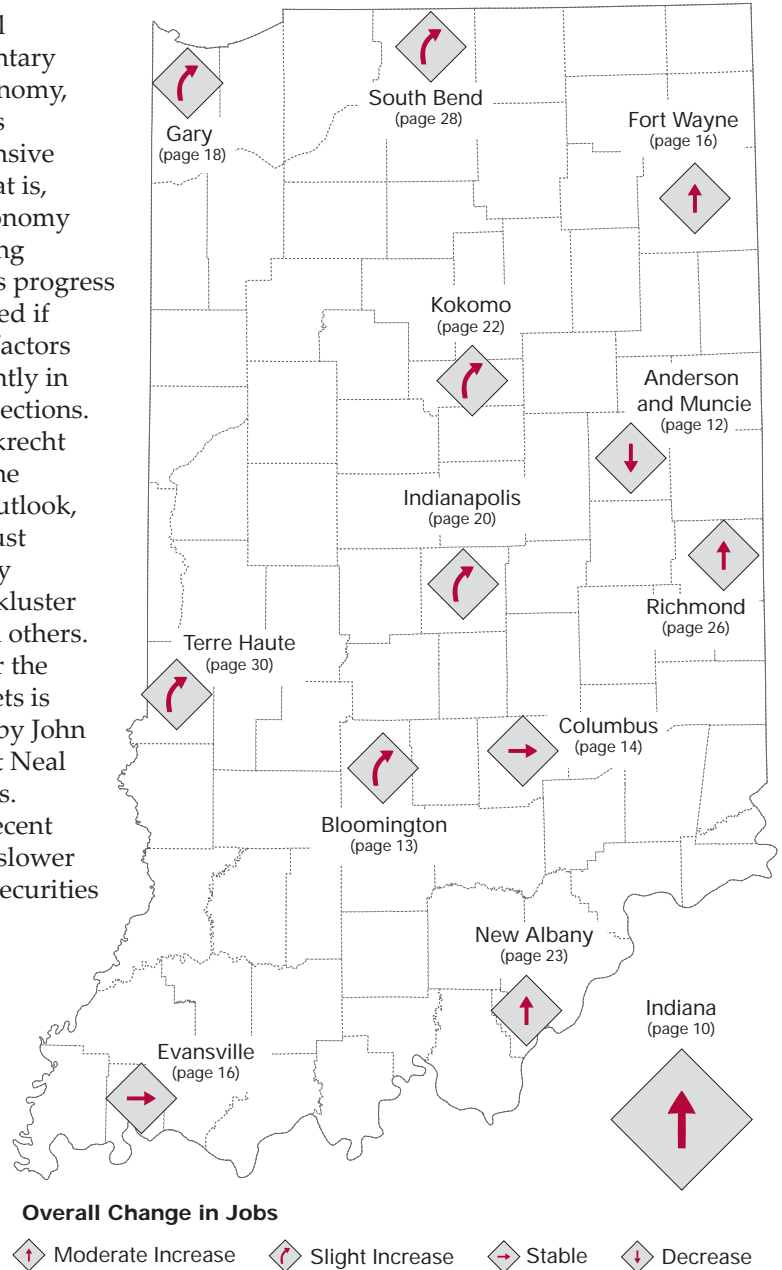
These economists and selected colleagues traveled to cities throughout Indiana to share their views through the Kelley School's Business Outlook Panel program. In each city, the panel was joined by an expert on the local economy who discussed the outlook for the metro area. The predictions of all the Business Outlook panelists are contained in the pages that follow, along with additional supporting detail.

The 2005 economy turned out to be somewhat more robust than the panel forecasted a year ago, despite the sustained high energy prices that we predicted. Overall, however, our prognostications were fairly close to the mark. This year's outlook shows increased uncertainty compared to last year, reflecting several forces that could throw a wrench into an economy that is growing at a moderate pace.

The 2006 outlook issue of the *Indiana Business Review* begins with Bill Witte's commentary on the U.S. economy, which he views with "apprehensive optimism." That is, the nation's economy shows surprising strength, but its progress could be derailed if any of several factors move significantly in detrimental directions. Andreas Hauskrecht then assesses the international outlook, predicting robust growth in many regions but lackluster performance in others. The outlook for the financial markets is next reviewed by John Boquist, Robert Neal and Bill Sartoris. They project decent but somewhat slower growth in the securities markets, with uncertainties about interest rates and energy prices complicating the picture.

Jeffrey Fisher weighs the outlook for housing, a sector that impacts much of the rest of the economy. Corinne Alexander looks at what is expected for the Hoosier agriculture sector. The prospects for continued growth in Indiana, reviewed by Jerry Conover, remain reasonably good, though some

**Figure 1**  
Projected Directional Change in Jobs, 2006



sectors will outperform others. Finally, a group of economists and business leaders from around the state share their insights into what 2006 holds in store for Indiana's metropolitan areas (see **Figure 1**). ■

# The U.S. Economy

**Willard E. Witte**

Associate Professor of Economics, Indiana University, Bloomington

Prior to the left-right combination of Katrina and Rita (Katrita for short), the economy was headed toward a very satisfactory 2005. Growth in the first half of the year was at 3.6 percent and seemed to be accelerating. This extended the solid recovery that began in earnest during 2003 (see **Figure 1**). Employment growth was averaging over 190,000 per month, implying about 2.3 million new jobs for the year. Unemployment in August was below 5 percent, down one-half percent from the end of 2004 (see **Figure 2**). Inflation (measured by core consumer prices—that is, excluding the volatile food and energy sectors) was stable at about 2 percent. It was reasonable to expect that 2006 would bring a continuation of these trends.

Of course, even in ordinary circumstances, forecasting the economy is something of a fool's errand for several reasons: First, much of what happens (especially for short-term horizons) results from inherently nonforecastable events. Second, economic data include a lot of noise and arrive after the fact. Third, our conceptual understanding of the forces that drive an economy as complex as the United States, while arguably improving, is very far from perfect.

The current situation is a textbook example of these difficulties. Five months ago, Katrita was in no one's forecast. Looking ahead now, there is very little concrete basis for predicting a wide range of important variables in the aftermath of the storms: How long will energy prices remain high? How much government aid will flow into the region (and how quickly)? How much will transportation infrastructure damage disrupt economic activity outside the region?

The storms will also seriously distort virtually all economic data

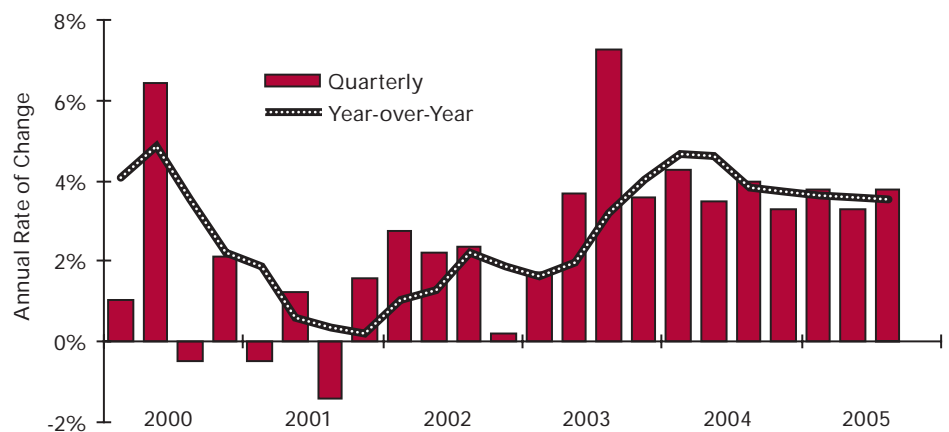
for at least the next few months. To a considerable extent, the numbers will be the result of guesses made by government statisticians as to how to incorporate the storms' effects. But even if we could confidently predict answers to questions like those in the previous paragraph, and even if we had reasonably good data, sorting out the quantitative effects of all the opposing forces in the current situation goes beyond the capability of available economic models.

So be forewarned—what follows comes with a higher degree of uncertainty than usual.

That said, we expect 2006 to be a reasonably good year for the national economy. We think the economy will continue to expand, probably close to its performance during the past year. Employment will also continue to rise, but a little short of 2005. Some details:

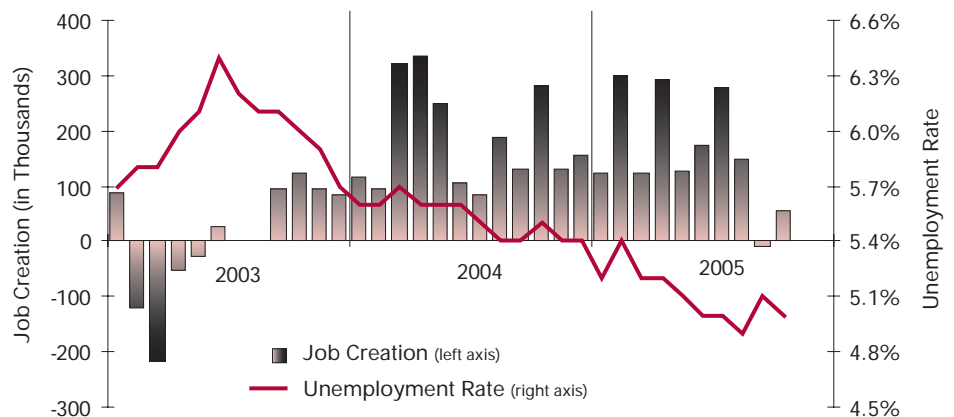
- We expect output to grow about 3.6 percent in 2006, similar to 2005 and somewhat above the long-run potential of the economy.

**Figure 1**  
U.S. Real Output



Source: Bureau of Economic Analysis

**Figure 2**  
U.S. Job Creation and Unemployment



Note: Data are seasonally adjusted  
Source: Bureau of Labor Statistics

- Employment will expand by about two million. This will be enough to bring unemployment back down to its levels just prior to Katrina, but not much more.
- Inflation overall will be similar to 2005, possibly somewhat lower with energy prices stable rather than rising. The consumer price index will increase about 3 percent.
- The Federal Reserve will push short-term interest rates to at least 4.5 percent—a level we expect to be reached early in the year.

Basically, our outlook is that the direct damage to the economy from the storms, as well as the indirect damage due to elevated energy prices, will be mostly offset by the stimulative effects arising from the rebuilding effort.

### Sources of Uncertainty

Our relatively sanguine outlook could be knocked off course by potential shocks coming from many directions. At least three of these merit more extensive comment: energy prices, the housing sector, and the level of national saving.

Our outlook assumes that energy prices will remain high, but will not escalate further from the levels reached post-Katrina (that is, crude oil prices around \$65 per barrel, gasoline a little under \$3 per gallon, and natural gas about \$13 per million Btu). These levels will clearly put pressure on the economy, especially on energy intensive sectors (airlines, for example). But we think such pressure will prove bearable. However, if energy prices were to rise beyond our assumed levels, the resilience of the economy would be severely tested. Moreover, given the current tightness in the supply situation (particularly for natural gas and refined products), it would not take much to drive prices higher.

Another danger related to the rise in energy prices is that inflation and inflation expectations could move higher. If this were to happen, the Federal Reserve would probably react by pushing interest rates higher than our forecasted levels.

Rising interest rates are particularly significant for the housing sector. The rate increases we expect—roughly another 1 percent across the yield curve—will raise mortgage rates to about 7 percent. Given rebuilding in Louisiana and Mississippi, this is probably not enough to prevent another good year for the sector. However, if rates were to go higher than our forecast, new construction could slow significantly.

For some homeowners (particularly those with adjustable rate mortgages) a combination of higher rates, significantly higher bills for heating, and perhaps higher insurance costs could create a serious budget bind.

A third cloud hanging over the economy is the low and decreasing level of national saving. In another dimension of the consumer budget dilemma, personal saving has fallen to virtually zero over the past two years. The net worth of the household sector has been insulated from this lack of new saving by increases in the value of existing assets (equity values during 2004 and housing values for several years). Looking ahead, we do not expect these gains to continue at their recent levels. The second component of national saving (from the government sector) has also deteriorated. Since the beginning of 2000, the combined budget of federal, state, and local governments has

swung from a one-quarter trillion dollar surplus to a one-quarter trillion dollar deficit. The only piece of the saving puzzle that has been favorable recently is that of the corporate sector. But even with this factored in, the picture is not good. The total level of national saving is now only about one-third its level during the late 1990s. Over the past four years, total national saving has been less than 20 percent of its amount during the previous four years.

This saving shortfall is made up by borrowing from abroad, which necessitates a large and growing international trade deficit. The resulting accumulation of foreign-held U.S. debt could easily put downward pressure on the value of the dollar in the foreign exchange market.

The above litany of problems is especially ominous in two regards. First, the problems are interrelated. For example, higher energy prices carry a risk of inflation, as does depreciation of the dollar. Inflation, especially if it leads to higher interest rates, could further squeeze household and government budgets. Second, all of them involve pressure on the household sector. If this pressure were to cause any significant pullback in consumer spending (which comprises two-thirds of the total economy), the economic outlook would worsen dramatically.

We think, however, that the more likely outcome is that both households and the economy as a whole will muddle through. The year 2006 will be a reasonably good year with adequate growth in output, continued improvement in the labor market, and only slightly elevated inflation. ■

“The year 2006 will be a reasonably good year with adequate growth in output, continued improvement in the labor market, and only slightly elevated inflation.”

# The International Economy

**Andreas Hauskrecht**

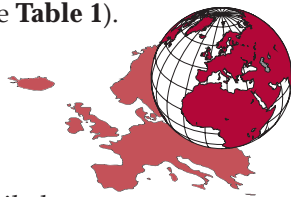
Clinical Assistant Professor of Business Economics and Public Policy, Kelley School of Business, Indiana University, Bloomington

**W**orld economic growth for 2005 is projected at 4.3 percent, measured in terms of real gross domestic product (GDP). The years 2003 and 2004 had growth rates of 4.0 percent and 5.1 percent, respectively. The International Monetary Fund in Washington forecasts world economic growth for 2006 at 4.3 percent;<sup>1</sup> this is a constant growth rate compared with 2005, still significantly above the historical trend of 3 percent.

The forecast predicts continuously robust economic growth for the United States, China, and India. Middle and Eastern European countries, emerging Asian, African, Latin American, and oil-exporting countries will dynamically expand economic output. Similar to previous years, the economic outlook for Europe and Japan is lackluster (see **Table 1**).

## Europe

The expected recovery in Europe has failed to appear; quite to the contrary, economic expansion faltered and the GDP growth forecast for 2005 was 1.2 percent. For 2006, an economic expansion of 1.8 percent is projected; for Germany and Italy forecasted output growth is even more modest at 1.2 and 1.4 percent, respectively. Economic performance across Europe remains mixed. For countries like Spain and France, domestic consumer demand was rather robust, while net export growth was sputtering. The opposite holds true for Germany, where export growth was very dynamic but domestic demand remained dull. Evidence suggests deeper structural problems for Europe that go well beyond a shortfall in economic demand. Long-term growth of an



economy is determined by three main factors: employment, productivity growth, and capital formation. The aging European population is a big hurdle for more healthy growth rates; and rising social security spending is a burden for fiscal policy. France, Germany, Greece, Italy, and Portugal are all expected to exceed the 3 percent GDP cap stipulated by the Stability and Growth Pact. While unemployment is still high at almost 9 percent for the euro area,<sup>2</sup> labor utilization has to rise over the long run: Europeans will have to work longer, not retire earlier. Also alarming is the relatively low capital spending that partly explains the low productivity growth. The process of reforms has to accelerate, labor market

restrictions have to be removed, and social security reforms need to continue.

The United Kingdom will do slightly better than continental Europe with an expected economic expansion of 2.2 percent.

## Asia

Japan's economy expanded by 2 percent in 2005 and will continue to grow around that range in 2006. However, while the economy is growing, price levels keep declining; deflation has not come to an end yet. Domestic consumption and modest export growth have contributed to



**Table 1**  
**World Output and Unemployment**

Geography	GDP		Inflation*		Current Account Percent of GDP		Unemployment	
	2005	2006	2005	2006	2005	2006	2005	2006
World Output	4.3	4.3	n/a	n/a	n/a	n/a	n/a	n/a
Advanced Economies <sup>a</sup>	2.5	2.7	2.2	2.0	-1.3	-1.4	6.1	5.9
Emerging Asia <sup>b</sup>	7.3	6.9	3.9	4.4	3.7	3.4	n/a	n/a
Western Hemisphere	4.1	3.8	6.3	5.4	0.9	0.6	n/a	n/a
Africa	4.5	5.9	8.2	7.0	1.6	3.5	n/a	n/a
United States	3.5	3.3	3.1	2.8	-6.1	-6.1	5.2	5.2
Japan	2.0	2.0	-0.4	-0.1	3.3	3.0	4.3	4.1
Euro Area	1.2	1.8	2.1	1.8	0.2	0.2	8.7	8.4
Germany	0.8	1.2	1.7	1.7	4.3	4.4	9.5	9.3
France	1.5	1.8	1.9	1.8	-1.3	-1.5	9.8	9.6
Italy	-	1.4	2.1	2.0	-1.7	-1.4	8.1	7.8
United Kingdom	1.9	2.2	2.0	1.9	-1.9	-1.8	4.7	4.8
Canada	2.9	3.2	2.2	2.5	1.5	1.7	6.8	6.7
Mexico	3.0	3.5	4.3	3.6	-1.1	-0.8	3.6	3.9
Brazil <sup>c</sup>	3.3	3.5	6.8	4.6	1.7	1.7	9.5	n/a
China	9.0	8.2	3.0	3.8	6.1	5.6	9.0	9.3
India	7.1	6.3	3.9	5.1	-1.8	-2.0	10.0	9.3
South Korea	3.8	5.0	2.8	2.9	2.0	1.5	3.6	3.3
Taiwan	3.4	4.3	2.0	1.8	4.3	4.6	4.3	4.2
Russia	5.5	5.3	12.8	10.7	13.2	13.0	7.7	7.4

\*Consumer Price Index

<sup>a</sup>Advanced economies include the United States, the euro area, Japan, United Kingdom, Canada, Korea, Australia, Taiwan Province of China, Sweden, Switzerland, Hong Kong, Denmark, Norway, Israel, Singapore, New Zealand, Cyprus, and Iceland.

<sup>b</sup>Emerging Asia includes developing Asia, the newly industrialized Asian economies, and Mongolia.

<sup>c</sup>Brazil's unemployment data is for July 2005.

Sources: Center for Econometric Model Research, Indiana University; IMF World Economic Outlook, Fall 2005; The Economist Intelligence Unit, Country Reports

this slightly brighter outlook. The financial sector looks healthier, although profitability is still low. Hopefully, the planned reforms of the Postal Saving System will succeed.<sup>3</sup> More than any other country, Japan faces a rapid aging of its population. This implies a heavy burden for the government budget and for future economic growth, since future employment will probably shrink, not increase. Japan has the highest budget deficit and the highest government debt of all industrialized nations. Fiscal consolidation, including social security systems, is a must. Exports to the United States and China are a very crucial demand component. Possible exchange rate changes make this component fragile.

Over the last two years, China and India have accounted for 28 percent and 10 percent of world economic growth, respectively. Average regional growth for emerging Asian countries reached 7.3 percent for 2005 and a comparable robust economic expansion is expected for 2006. Several Asian economies, among them China, Japan, South Korea, and Taiwan, continued to buy dollars in the foreign exchange market in order to avoid an appreciation of their currencies and jeopardizing export-led growth. However, regional current account surplus is projected to decline modestly to around 3.7 percent in 2005. Mostly caused by rising energy costs, inflation will gain momentum and is expected to increase above 4 percent in 2006.

### North America

The economies of the NAFTA members are increasingly integrated. Strong demand from the United States caused a further increase of Mexican and Canadian exports to the United States and contributed to robust economic development in both



countries. While the Canadian dollar strongly appreciated against the U.S. dollar, the Mexican peso depreciated against the dollar. Both economies are expected to grow in real terms slightly above 3 percent in 2006.

### Russia and East Europe

Russia and most middle and East European countries continue to do well and the outlook is optimistic into 2006. The common explanation is, of course, the booming crude oil price. Yet, the Russian economy shows signs of imbalance, including double-digit inflation and a federal budget with an unhealthy reliance on oil export revenues, while significant structural problems are not accordingly addressed. GDP growth for 2006 should be slightly lower, decreasing from 5.5 percent in 2005 to 5.3 percent in 2006.



### Latin America

Latin America continued to grow robustly in 2005 and is expected to do so again in 2006, with an estimated output increase for the region of 3.8 percent. The accelerated world market integration continues; the regional current account is expected to remain in modest surplus, although the Brazilian currency, the real, has significantly appreciated against the U.S. dollar and the euro. This is caused by huge capital inflows that make it easier to finance and restructure the still significant government debt.



### The Risks

High oil prices are the biggest risk for world economic activity in 2006. The forecasts presented in **Table 1** assume

a yearly average crude oil price of slightly above \$60 (U.S.) per barrel.

High crude oil prices cause a redistribution of wealth from oil importing to oil exporting countries. Note, however, that the engines of world growth, the United States, China, and India are all crude oil net importers. A further rise in oil prices would have negative effects on consumption expenditures and feed fears of accelerated inflation. Several countries, particularly in Asia, try to cushion the effects of rising oil pricing on domestic demand by heavily subsidizing energy. This immense burden on national budgets is not sustainable; so in 2006, high energy costs will gradually pass through to domestic consumption in these countries and shall slow down economic expansion.

A second risk for the world economy is possible repercussions from exchange rate changes. China allowed a modest (2.1 percent) appreciation of the yuan against the U.S. dollar in July 2005. Since then, Chinese monetary authorities have continuously intervened in foreign exchange markets to avoid any further appreciation. During the third quarter of 2005, the dollar gained strength against most currencies; given market expectations of further interest rate increases by the Fed, a rather robust dollar value in 2006 is most likely. Given the more and more attractive yields for U.S. nominal assets, we expect country risk premiums to rise during the coming year. ■

### Notes

1. International Monetary Fund, *World Economic Outlook: Building Institutions*, September 2005. Available at [www.imf.org/external/pubs/ft/weo/2005/02/index.htm](http://www.imf.org/external/pubs/ft/weo/2005/02/index.htm).
2. The euro area includes Germany, France, Italy, Spain, the Netherlands, Belgium, Austria, Finland, Greece, Portugal, Ireland, and Luxembourg.
3. The Japanese Postal Savings System is the largest financial institution in the world, with about \$2.4 trillion (250 trillion yen) on deposit, or one-third of the country's total bank deposits. It is a government-run banking system based on 24,000 post offices, each having a bank inside.

# Financial Forecast

## John Boquist

Edward E. Edwards Professor of Finance, Kelley School of Business, Indiana University, Bloomington

## Robert Neal

Associate Professor of Finance, Kelley School of Business, Indiana University, Indianapolis

## William Sartoris

Professor of Finance, Kelley School of Business, Indiana University, Bloomington

How times have changed. The new mantra from Wall Street is that sex, drugs, and rock and roll have now been replaced by the three P's: pensions, Porsches, and a place on the beach. As college professors, our dean ensures that we don't get paid enough to buy a Porsche—much less a place on the beach. But everyone is concerned about pensions and investment performance, so let's turn our attention to the financial outlook.

The year 2005 has been interesting. We've had everything from the White Sox to oil shocks. We've had bankruptcies in airlines and auto parts and huge losses from hurricanes. We've had creeping inflation and soon we'll have a new Fed chairman.

Despite all of this, the economy is like the Energizer Bunny®: it keeps going and going. Since our forecast a year ago, gross domestic product (GDP) has increased at an annual rate of about 3.6 percent. This was on the high end of our forecast range and has translated into strong earnings growth. From the third quarter of 2004 to the third quarter of 2005, earnings for the S&P 500 were up 15 percent.

The equity markets have followed suit, albeit a bit more cautiously. Over the past twelve months, the S&P 500 is up about 7.5 percent and the NASDAQ Composite is up about 6 percent. On a year-to-date basis, however, the stock market has been essentially flat, so all the gains over the past twelve months came from November and December 2004.

Two factors have contributed to this lackluster performance. Over the past year, the federal funds rate has risen from 1.75 percent to 4 percent (see **Figure 1**), and the prime rate has

increased from 4.75 percent to 6.75 percent. Higher interest rates make it more costly for firms to finance their expansions, and higher discount rates reduce the value of future earnings. The long-term rates have also risen, but at a slower rate. The yield on the benchmark ten-year Treasury bond rose from 4.1 percent to 4.6 percent and the average rate on thirty-year mortgages increased from 5.7 percent to 6.3 percent.

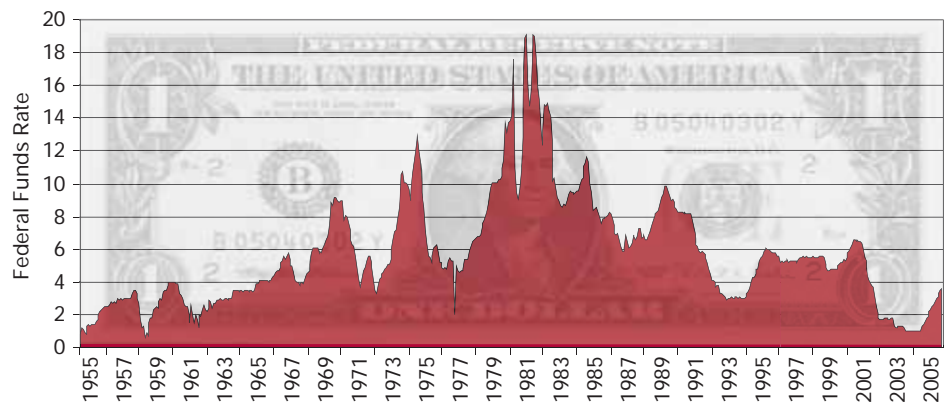
Another factor is compression of the price-earnings (P/E) ratio, which measures the price an investor needs to pay to acquire \$1 of company earnings. Firms with high P/E ratios have strong growth prospects. A decrease in the P/E ratio means that investors are less optimistic about future growth or have become more risk averse about the stock market in general. From the third quarter of 2004 to the third quarter of 2005, the P/E for the S&P 500 declined from 19.3 to 17.8. This is above the long-term historical average of about 16, but below 24, the average over the last fifteen years.

## Outlook for 2006

Our projection is that the stock market will provide a decent return this year, although less than the historical average of about 12 percent. Several factors lead us to this projection for 2006.

We expect that short-term and long-term interest rates will rise in 2006. The Fed increased short-term rates by 25 basis points at the December 2005 Federal Open Market Committee meeting. We expect at least one additional increase in 2006, bringing short term rates to 4.5 percent and the prime rate to 7.5 percent. Increases beyond this will depend on rate of inflation. The Fed seems to have a comfort zone of 1 percent to 2 percent for inflation. We are currently close to the 2 percent boundary, and if our inflation forecast of 3 percent is realized, then we will see additional increases in the federal funds rate. An important factor for inflation is the price of energy. In the past two years, oil has risen from about \$28 per barrel to about \$65 per barrel. If this trend

**Figure 1**  
Monthly Federal Funds Rate over Time, July 1954 to September 2005



Source: Federal Reserve



continues, inflationary pressures are unlikely to abate.

The long-term Treasury bonds have shown strong resilience to the rise in short-term rates. Over the past year, the federal funds rate has risen by 225 basis points, while the yield on the benchmark ten-year Treasury only increased by 50 basis points. This has caused the yield curve to become flatter, which may depress economic growth in 2006. Historically, steeper yield curves have been associated with higher growth rates of GDP.

While the muted reaction of the ten-year bond to the rise in inflationary pressures suggests the market believes that inflation is not a long-term problem, there is uncertainty about the new Fed chairman. Lost in the discussion of the positive reaction to the Bernanke announcement was that long-term bonds sold off and the yields rose by about 20 basis points.

On the earnings front, we anticipate a decent year for corporate earnings. Earnings projections from Wall Street firms suggest a 10 percent to 12 percent growth in earnings in 2006. This is down from the 15 percent growth over the past year, but greater than the 10 percent annual earnings growth over the past fifteen years. One of the unusual characteristics of corporate earnings is that firms have a tendency to lower expectations about their earnings so their announced earnings will exceed the diminished target. While this process is well known on Wall Street, the earnings announcements do provide some good news. In recent months, there has been a greater than average tendency to exceed their targets, which bodes well for 2006 earnings. Firm revenues are expected to grow 8 percent to 10 percent in 2006 and productivity is expected to increase 2 percent to 3 percent, which remains strong by historical standards.

Much of the earnings strength in 2005 came from the energy sector, where earnings increased 45 percent.

Excluding this sector, overall earnings fall to a more modest 11 percent. At this date, it is still unknown how consumers will react to higher energy prices. Since consumer spending generates about 60 percent of corporate profits, an energy-related slowdown in consumption could have a large adverse impact on 2006 earnings. Another source of strength in 2005 was the housing sector, as home sales and housing starts continued strong through the third quarter. Recently, however, signs of weakness have developed. Thirty-year mortgage rates are up to 6.3 percent and mortgage applications have declined. The ability to use home equity to pay for consumption items has also diminished as fewer households are using refinancing as a means to realize the price appreciation of their home. A third source of earnings uncertainty comes from hurricanes Katrina and Rita. Many economists believe the impact of the storms will shift GDP from the last half of 2005 into the first half of 2006. While 400,000 jobs disappeared and the property damage may exceed \$100 billion, there is likely to be a massive government-led rebuilding effort. In turn, this will trigger hiring, increased spending, and ultimately corporate profits.

Prudent investors should always diversify their investments. For 2006, many analysts are recommending an asset mix that contains slightly less stock and slightly more bonds than the average recommendation. We expect the stock market performance in 2006 to be similar to 2005: choppy, with total returns in the 6 percent to 10 percent range. One important step investors can take to improve investment performance is to monitor the total fees paid to mutual funds and investment advisors. Fund expenses, management fees, and inefficient trading for taxable accounts can reduce total returns by 4 percent per year. ■

# Housing

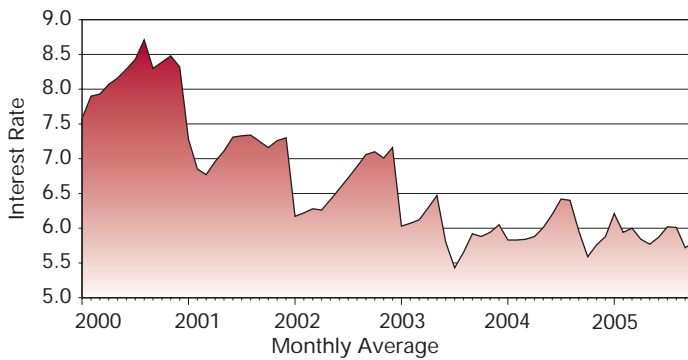
**Jeffrey D. Fisher**

Director, Center for Real Estate Studies and Charles H. and Barbara F. Dunn Professor of Finance and Real Estate, Kelley School of Business, Indiana University, Bloomington

The national housing sector has benefited significantly from low long-term interest rates in recent years. The Fed's hikes in short-term rates after mid-2004 did little to dampen housing demand. There has been talk of a housing bubble in many areas of the country as home prices have risen considerably compared to historical levels. Prices have also risen much faster than rental rates, analogous to having a high price-earnings ratio for houses. Average national home prices have not dropped since the Great Depression but the recent frenzy in the real estate market has investors wondering if the market can maintain this pace. Housing prices have risen and popped in past years. Texas collapsed in 1986, Southern California in 1989, and Massachusetts and Connecticut in 1991. But the debate continues over whether a nationwide bubble has materialized.

Some compare today's coastal housing market, where prices increased the most, to the investment craze that led to the technology stock crash a few years ago. Home prices in some regions have more than doubled in the past five years, leading to concerns that the speculative bubble might burst. There have also been record levels of conversion of apartments into condominiums in many areas of the country as demand for homeownership has also led to increased demand for condominiums. Investors can earn a greater profit by selling apartments as condos rather than renting apartments. In markets like Miami, where the condo market has been particularly hot, some units have even changed hands the same day as speculators have been buying many of the condos.

**Figure 1**  
Thirty-Year Fixed Rate Mortgages



Source: HSH Associates

The bad news for homeowners in Indiana is that they have not seen their home values rise like many other areas of the country. The Indianapolis area's home prices grew at nearly the slowest pace of the top fifty markets, or 19 percent during the past five years. Homeowners in the Boston and San Diego areas saw their homes appreciate more than 75 percent during the same period.

The good news is what has not gone up will probably not go down. That is, home prices in Indiana are not likely to fall with a possible drop in prices in those areas of the country that may be experiencing a bubble. So there is less risk associated with purchasing a home in Indiana compared to many other areas of the country. This also makes homes in Indiana relatively affordable compared to many other areas.

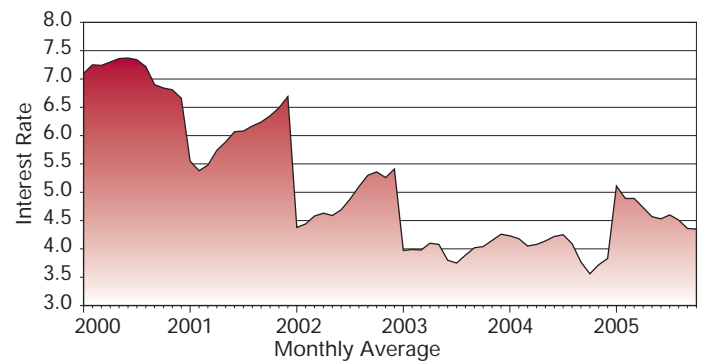
Of course, it can be painful for someone who plans to sell a home in the Midwest where the median home

price is \$174,100 and move to another area like the Northeast where the median is \$252,900 or the West where the median is \$327,300. Whether such an extreme difference in median home prices is sustainable is questionable.

A countrywide meltdown in housing prices could have a profound effect on the economy, as more Americans are invested in real estate than in stocks. A decline in housing prices would have a very serious effect on the economy because housing has been supporting the economy ever since the recession. Roughly 5 percent of the gross domestic product is associated with homebuilding and construction. Furthermore, there has been a consumption boom based on people taking out second mortgages and refinancing their homes.

However, most economists do not expect a national decrease in home prices. Housing is very dependent on the local economy and the markets that have experienced the rapid

**Figure 2**  
One-Year Adjustable Rate Mortgages



Source: HSH Associates

increase in prices have also had rising household income.

Sales of existing homes held at the second highest pace on record in September 2005, with sales surging in some areas following Hurricane Katrina. Rebuilding in Louisiana and Mississippi will likely keep the housing market strong through 2006, as long as mortgage interest rates do not rise too much. The recent trends in fixed and adjustable interest rates are shown in **Figures 1** and **2**.

Mortgage rates could increase from their current level if the Fed continues to increase interest rates. The National Association of Homebuilders projects rates for fixed rate mortgages to rise from their current levels of less than 6 percent to about 6.5 percent in 2006, whereas the Indiana University econometric model forecasts a slightly higher 7 percent rate. In either case, these rates are still at historically low levels and are not likely to have much of an adverse effect on housing demand. Housing starts could drop slightly during 2006, although as mentioned above, rebuilding due to Katrina will add to the demand.

**Table 1** shows the recent historical levels and forecast for housing and interest rates from the National Association of Home Builders ([www.NAHB.org](http://www.NAHB.org)). Housing starts and new home sales are forecast to drop slightly in 2006 and 2007 as mortgage interest rates rise. The underlying fundamentals remain relatively strong and the decline is mainly due to a drop off from the boom we have been experiencing. ■

**Table 1**  
Indiana's Housing and Interest Rate Forecast

	2003	2004	2005	2006	2007	
(in Thousands)	Total Starts	1,854	1,950	2,032	1,930	1,850
	Single-family	1,505	1,604	1,683	1,580	1,510
	Multi-family	349	345	349	350	340
	New Single-Family Home Sales	1,091	1,200	1,275	1,208	1,155
	Existing Home Sales	5,441	5,913	6,167	5,857	5,625
Interest Rates (Freddie Mac Commitment)						
	5.8%	5.8%	5.8%	6.5%	6.6%	
	3.8%	3.9%	4.5%	5.4%	5.5%	
	4.1%	4.3%	6.2%	7.5%	7.5%	

Source: National Association of Homebuilders

# Indiana Agriculture

**Corinne Alexander**

Assistant Professor, Department of Agricultural Economics, Purdue University, West Lafayette

Where is the Indiana agricultural economy headed in 2006? The answer is toward weakening income and increasing (though at a slower pace) farmland values.

Let's start with net farm incomes. Part of the reason farm incomes seem low is the extraordinary income levels of nearly \$2.4 billion in 2004. The previous record incomes were near \$1.4 billion in 1996 and 1997. Thus, Indiana's net farm income in 2004 was 70 percent higher than the previous record. To put \$2.4 billion of income in perspective, the average yearly income for the previous ten years, 1994–2003, had been around \$1 billion (see **Figure 1**).

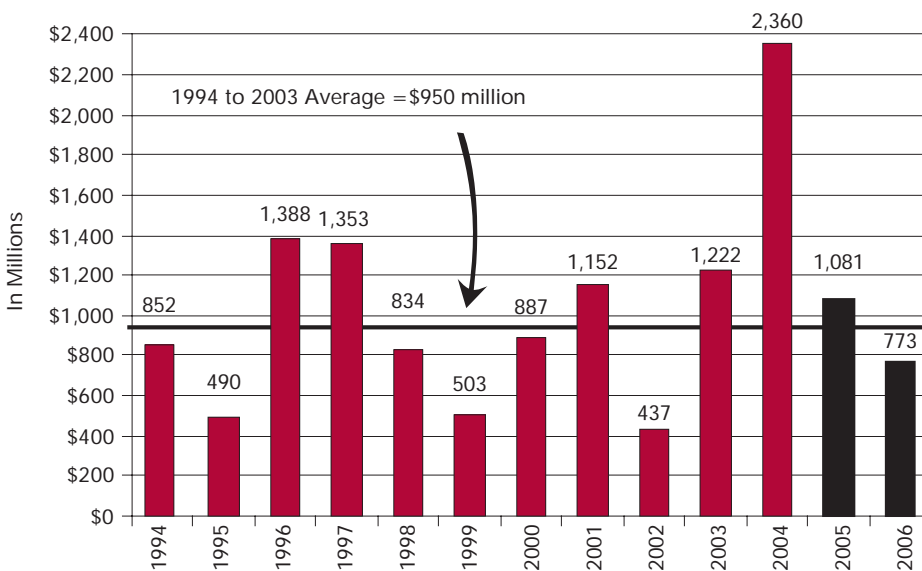
Since 2005 data are not currently available, Purdue estimates much more modest incomes between \$1 billion and \$1.1 billion. While down sharply from 2004's record, many Indiana crop farmers feel fortunate to have seen their income prospects recover with good yields after a hot,

dry summer. Crop yields in 2005 are expected to be slightly below normal for corn and slightly above normal for soybeans. Costs of crop production were up sharply in 2005, cutting into farmer margins.

Livestock, milk, and poultry prices are somewhat lower than 2004 as well. Large variations in individual farm incomes can also be anticipated given wide ranges in yields from farm to farm across Indiana this fall.

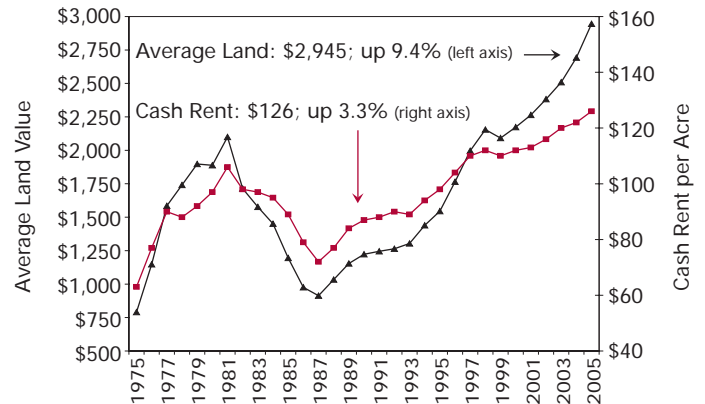
Finally, what about 2006? At this early point, we see continued sharp increases in costs of crop production led by fuel and fertilizer costs, plus interest rate increases. Unfortunately, crop prices are not expected to rise by enough to cover these surging costs.

**Figure 1**  
Indiana Net Farm Income in Actual Dollars, 1994 to 2006



Source: 1994–2004, U.S. Department of Agriculture; 2005–2006 estimates, Purdue University

**Figure 2**  
Indiana Agricultural Land Values and Cash Rents per Acre



Source: Purdue University

The outlook for the animals sector turns down as well, with 2006 prices dropping for beef cattle, hogs, milk, and turkey. The only good news for livestock producers is that feed costs will be lower. Purdue's estimates of Indiana's 2006 net farm income suggest further declines to a below average income between \$700 million and \$800 million. With record-high land values and cash rents, surging input costs, and struggling grain prices, 2006 looks to bring a severe cost/price squeeze for crop farmers and narrowing returns for animal producers.

Where are agricultural land prices and cash rents headed in 2006? Let's start by reviewing what happened in 2005. According to the Purdue Land Value Survey, Indiana farmland values reached record highs again in 2005 at an average value of \$2,945 per acre (see **Figure 2**). This 9 percent increase was the latest in a series of increases that started in 1987. Cash rents also edged upward to \$126 per acre, an increase of 3 percent.

Looking toward 2006, we expect farmland values to continue to increase until long-term interest rates increase. Because long-term interest rates are projected to increase in 2006, farmland values are expected to increase at a slower pace, only 4 to 6 percent. There are three other factors

# Indiana

that would derail a continued increase in farmland values.

1. If the 2007 farm bill reduces government price support payments.
2. If rental income is reduced because of continued pressure on margins from either production cost increases or price declines.
3. If real estate taxes increase.

The demand for land to rent remains strong as farmers seek to increase the size of their operations. However, crop margins for 2006 are projected to be very tight, which will limit the ability of tenants to pay higher rent. Therefore, we expect cash rents to only increase 0.5 percent to 1 percent in 2006.

The financial condition of the Indiana farm sector is the strongest since the 1960s due to strong income performance in 2003, 2004, and 2005, and record-high land values that keep asset values high. However, changes appear to be coming for some in the agricultural community in 2006. Landowner wealth is high, but tenants have not shared as strongly in the good fortunes.

In 2006, tenants will be caught in a struggle to cover the escalated input costs, higher rents, and higher interest costs with little ability to improve revenues. Margins may be negative and will provide incentives for tenants to reduce input use somewhat, cut back on capital purchases, seek concessions on cash rent, and cut their family living expenses as they struggle through the year and hope for a change in prospects in 2007.

One trend that may improve future prospects comes from the energy sector. The energy bill requires that 7.5 billion gallons of renewable fuels be used by 2012, with the most likely candidates being ethanol made from corn and biodiesel made from soybean oil. Demand from the energy sector for corn and soybeans has the potential to improve prices and incomes, positively influencing farmland values and cash rents. ■

## Jerry Conover

Director, Indiana Business Research Center, Kelley School of Business, Indiana University

Taking stock in the final quarter of 2005, Indiana's economy has continued to grow during the past year, though its rate of growth is slowing down as the year draws to a close. As shown in **Figure 1**, the state's total nonfarm employment has recouped much of its losses from the first few years of this decade. In fact, in September 2005, total employment was only 45,000 below its all-time high of 3,013,800 reached in May 2000. This represents a gain of 83,700 jobs since the state's employment bottomed out in July 2003.

Since the start of 2005, Indiana employment has averaged about 40,000 more jobs than a year earlier. However, much of that growth occurred in the early months of this year—since April, year-over-year growth has averaged a little over 34,000 jobs; and for the third quarter, employment was up only about 29,000 more jobs than a year earlier.

Indiana's employment gains have come more from some sectors than others, and the pattern of sectoral growth seems to be shifting. Education and health services continues to lead the charge with a gain of 9,100 jobs in the past twelve

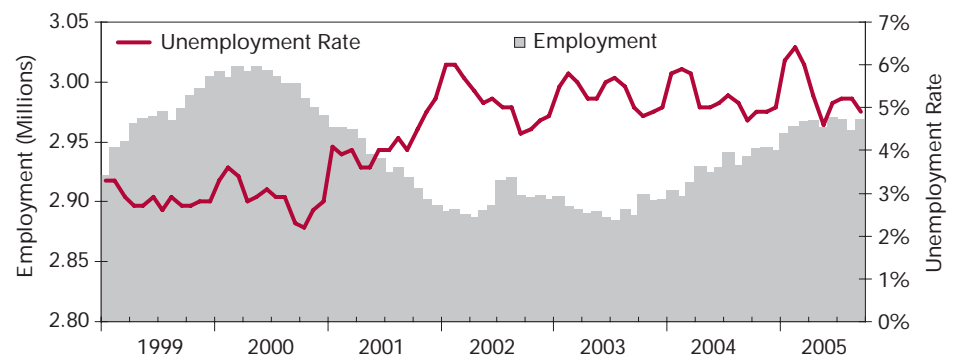
months. Leisure and hospitality has maintained a steady second position this year, up by 6,000 jobs. The fluctuating professional and business services sector has experienced weakening growth this year, slowing considerably in the last several months to around 4,000 jobs more than a year earlier, compared to gains of around 11,000 jobs earlier in the year.

Construction has remained strong throughout 2005, averaging about 5,000 more jobs than a year earlier. Trade, transportation, and utilities, which has employed slightly more Hoosiers than manufacturing for the past few years, also showed solid growth in 2005, with an increasing pace evident the last half of the year.

Manufacturing, the sector in which Indiana still leads the nation as a percentage of total employment (19.2 percent), continues to struggle. Manufacturing employment was down in September by 2,200 jobs compared to a year earlier, and down by 5,100 jobs compared to its post-recession peak in March.

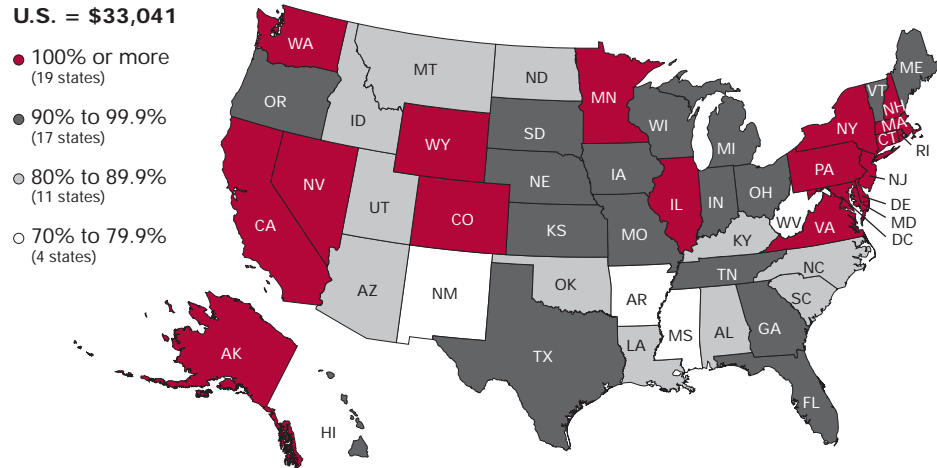
Indiana's unemployment rate has meandered around 5 to 6 percent for nearly four years. For most of 2005, the rate has been slightly above 2004

**Figure 1**  
Indiana's Monthly Nonfarm Employment and Unemployment Rate



Note: Employment is seasonally adjusted; unemployment rates are not.  
Source: Bureau of Labor Statistics

**Figure 2**  
Per Capita Personal Income as a Percent of the U.S. Total, 2004



Source: Bureau of Economic Analysis

levels, but the year is closing in on a level close to the end of last year.

### Other Indicators

The pulse of a state's economy is measured by more than just employment statistics. Indiana's gross state product (GSP) ranks fifteenth nationally, as it has for many years, and is the broadest measure of total output of a state's economy. However, the rate of growth in GSP since 2000 (a 7.1 percent gain) ranks Indiana forty-fourth among the states. Indiana's per capita personal income, which reflects individual earnings from all sources, has slipped to only 91 percent of the national average, below two-thirds of the states (see **Figure 2**).

### Indiana's Outlook for 2006

Several factors combine to complicate prediction of Indiana's economic outlook. The American auto industry is struggling, weakening demand for the products of many Indiana firms, especially manufacturers. This could take a toll on the state's steel industry, too, although mills supplying foreign customers or the construction industry may do well. Moreover, even if housing demand begins to level off, demand for Indiana appliances and other goods used in residential construction should hold its own.

Indiana farmers are expected to face a challenging year ahead as costs of production rise faster than farm prices, but some anticipate increasing demand as they target the biofuels industry. Hoosier consumers are entering the winter heating season with the prospect of record-high fuel bills, especially for those heating with natural gas. Coupled with persistent high gasoline costs, consumers may be less inclined to spend money in Indiana stores and restaurants.

The overall outlook suggests that Indiana's economy will experience moderate growth in 2006, but that the growth will be unevenly distributed across the economy. Especially in light of recent announcements of plant closures and layoffs, Indiana manufacturing jobs are not likely to grow, though they may hold their own as more competitive firms expand in selected industries. Job growth in Indiana is expected in health and education services, construction, trade and transportation, and leisure and hospitality. Overall employment should expand in 2006 by around 30,000, possibly even clearing the 3 million mark. The state unemployment rate should finish the year down slightly from its current level to around 4.8 percent. ■

### Patrick M. Barkey

Director of Economic and Policy Studies,  
Ball State University

**A**s former Nixon economic advisor Herbert Stein once said, things that can't go on forever usually don't. That is the spirit in which we turn again to the task of projecting the economic future of the Anderson and Muncie metro for the coming year. Logic and reason say that the long, painful decline in these medium-sized cities, which began in earnest in the mid-1990s and continues to this day, cannot continue indefinitely. Yet the forecast of another down year in 2006 for each of these economies, in the light of current developments, continues to be the most reasonable forecast.

In the midst of an improving economic climate, particularly in the manufacturing sector, both the Anderson (Madison County) and Muncie (Delaware County) metropolitan areas continue to struggle just to tread water. Employment totals in 2005 thus far show no break in the pattern of decline that predated the recession, and the likelihood of more bad news for manufacturing facilities in Anderson (Delphi) and Muncie (New Venture Gear) digs the hole a little deeper for 2006.

Yet, there are success stories to be told in both communities. Considerable efforts are underway in both metro areas to attract and grow new business, as evidenced by the active small business incubators, innovative zoning initiatives, and other development efforts in each county. However, aggregate economic indicators continue to be dominated by the predominantly negative developments unfolding in the existing economic base.

### Economic Performance to Date

**Figure 1** shows the magnitude of the decline in Anderson and Muncie—similar to the declines in the nearby cities of Marion and Richmond. There

were almost 8 percent fewer business establishments in the Muncie metro in 2004 than existed ten years earlier, with the number of employees on payrolls for the period declining by almost 13 percent. The Anderson metro suffered nearly an identical employment decline, although the number of businesses operating in the county remained nearly unchanged.

Over the same period, 1994 to 2004, the national and the state economies posted respectable growth on both measures. Even though the state's 8 percent growth in payrolls since 1994 is less than half the national average, it stands in stark contrast to the double-digit declines in the east-central part of the state.

These job declines have had a dramatic effect on wages, particularly

in Anderson. Over a ten-year period that saw wage and employment propel total wages to a growth of nearly 70 percent nationally, wage earnings in Anderson actually registered a slight decline. That outcome reflects the high average pay of the jobs lost during these years. The loss of this base has been keenly felt by area merchants and other local businesses.

For both Anderson and Muncie, the employment base today has substantially fewer manufacturing jobs, as shown in **Figure 2**. Given the impacts of global trade and improving technology on manufacturing employment nationally, this is neither surprising nor new. What is of more concern is the relatively slow growth of the nonmanufacturing sector. Of

the five industries with the largest payroll employment, only health care services has managed any significant growth since 1994. In the Muncie metro, more people work in health care than any other major industry.

### The Outlook for 2006

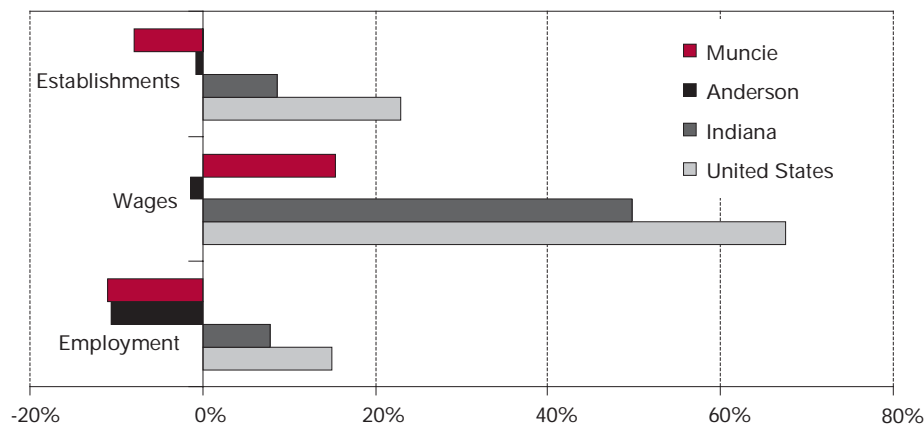
The recent trends in the external economic environment, particularly in the industrial economy, present both opportunities and threats to Anderson and Muncie in 2006. Certainly, the strength in business spending nationwide and the durability of the industrial expansion, which has propelled manufacturing output nationally beyond its pre-recession levels, present opportunities for many area companies. Yet special events in the automobile industry (in particular, the auto parts business) do not auger well, for Anderson especially.

The 500 jobs still at Delphi in Anderson are at considerable risk, given the GM spin-off's bankruptcy filing and recent tough rhetoric on upcoming negotiations on wage and benefit reductions. Since 2000, the motor vehicle parts industry has shed almost a third of its workforce, and given the major losses at both Delphi and its biggest customer, General Motors, the survivability of the Anderson jobs is doubtful.

In Muncie, the announced closing of the former New Venture Gear transmission facility may be offset somewhat by the arrival of Magna Drive Train's operations in the city's southside industrial park. The rapidly changing nature of the parts industry, however, makes any sort of concrete projections for individual facilities very difficult.

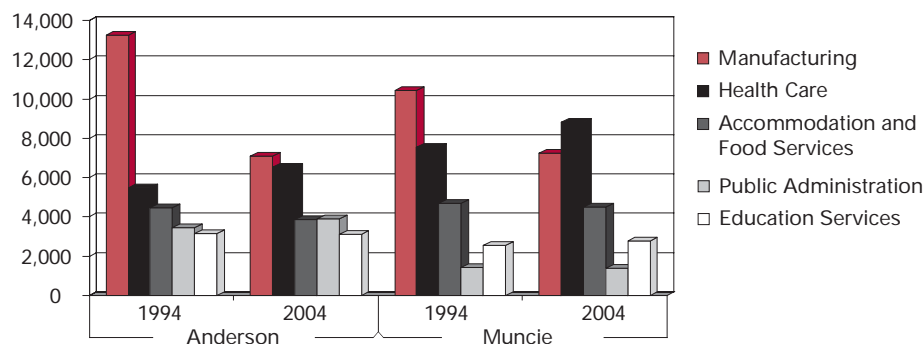
Those impending events and recent trends in the data noted above suggest that the decline in the Anderson-Muncie employment base will continue into 2006. We project a job decline of 1 percent, or about 800 to 1,000 jobs, will be trimmed from the aggregate payrolls of the two cities in the next twelve months. ■

**Figure 1**  
Business Growth, 1994 to 2004



Source: Bureau of Labor Statistics

**Figure 2**  
Employment by Industry, 1994 and 2004



Source: Bureau of Labor Statistics

# Bloomington

**Linda Williamson**

President, Bloomington Economic Development Corporation

One need only look to Bloomington and Monroe County to find where the new economy is taking root. Recent announcements, ribbon-cuttings, and construction projects indicate the life sciences and advanced manufacturing sectors are alive and well. Local information technology firms are expanding, and jobs in the professional and technical services are growing.

Buoyed by the recent investments of Cook Group Incorporated and fueled through strong support and assistance from both Indiana University and Ivy Tech Community College, area companies are creating jobs. Cook Group Inc.'s investments include over \$70 million in the new Cook Pharmica LLC and \$12 million in an expansion of Cook Inc. These projects will create over 450 jobs, which when added to those being created by the new BioConvergence LLC and the recent expansions at Baxter Pharmaceutical Solutions total about 1,300 new jobs (see **Figure 1**).

While the job news has been mostly positive, there have been layoffs and business closings in the past year. General Electric cut nearly 500 jobs and Otis Elevator ceased manufacturing operations earlier this

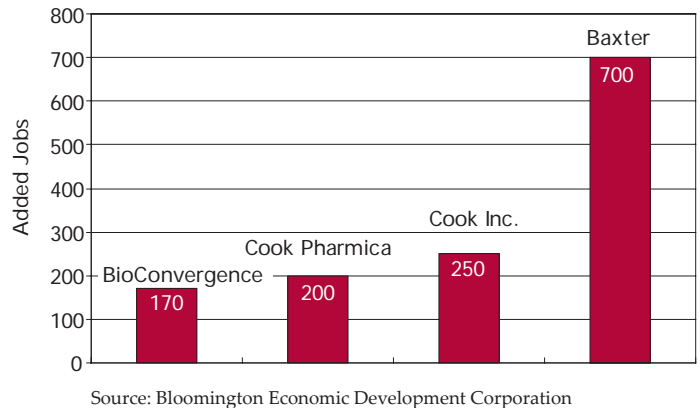
year, eliminating nearly 200 jobs. The most closely watched employer in the community may be Indiana University. With declining state funding and changing demographics, both enrollment and employment at Indiana University are monitored closely.

The continued decline in traditional jobs mixed with the new job growth leads to predictions of modest net job growth for the coming year. Job growth will be spread over most business sectors including hospitality, health care, and other service industries.

With the changing business mix, it remains to be seen if the local per capita income will begin to rise. The most recent per capita income data (2003) shows that Bloomington is well below the state and national income levels (see **Figure 2**). However, the lower per capita income can be partially attributed to college students working part time.

Population estimates continue to predict slow to moderate growth

**Figure 1**  
Recent and Anticipated Life Science Jobs in Bloomington

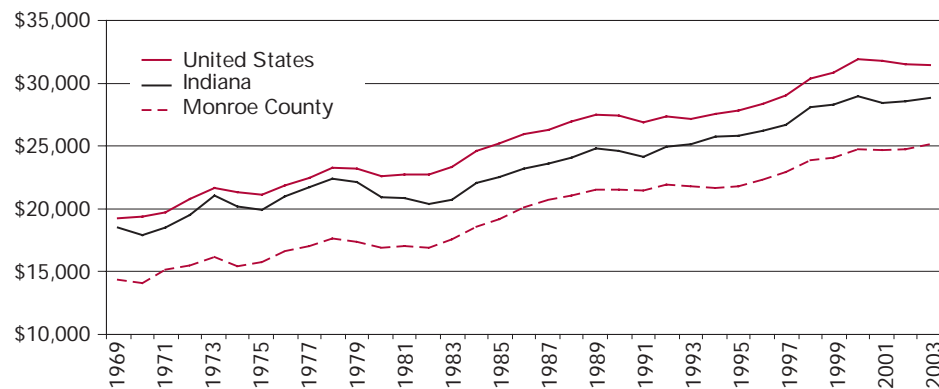


for the Bloomington area of just less than 1 percent per year for the next ten years. Meanwhile, the number of people commuting into Monroe County for employment continues to grow with nearly 16,000 workers driving into the county daily (see **Figure 3**).

Construction activity has been strong in Monroe County since the late 1990s. Building permit activity for single-family homes has been very consistent and looks to stay that way into the future. Permits for 2005 are on track to match the annual average of five hundred new units. The major change will be in the construction of multi-family housing. With nearly five hundred new bedrooms constructed in the downtown area and large apartment complexes completed on both the east and west sides of town in recent years, there is currently only one project under consideration.

Local planners report that 2005 has been a strong year for office, commercial, and industrial construction. Work continued on a new Hilton Garden hotel, Monroe Hospital (the community's second hospital), the first office building in North Park, Cook Pharmica, Cook Inc., and BioConvergence. Lighter caseloads currently in local planning departments may indicate a decline in the area's construction industry for 2006.

**Figure 2**  
Per Capita Personal Income, 1969 to 2003



Note: Data are adjusted for inflation.  
Source: STATS Indiana, using Bureau of Economic Analysis data

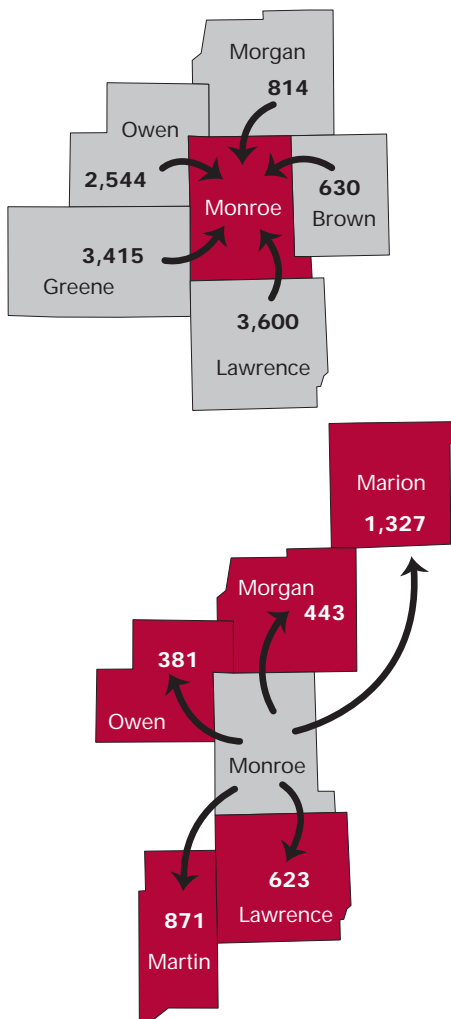
# Columbus

**James C. Smith**

Senior Lecturer in Finance and Co-director, Center for Econometric Model Research, Kelley School of Business, Indiana University

Bloomington's economy continues to transition. The presence of a large research university and a regional community college continues to provide stability for the current economy and a workforce for the new economy. Successful entrepreneurs who start and grow their businesses in the community, continued emphasis on development in the life science and information technology sectors, and strategic public investments should allow for continued, though modest, growth and improvement in the local economy. ■

**Figure 3**  
Top Five Counties Commuting Into and Out of Monroe County



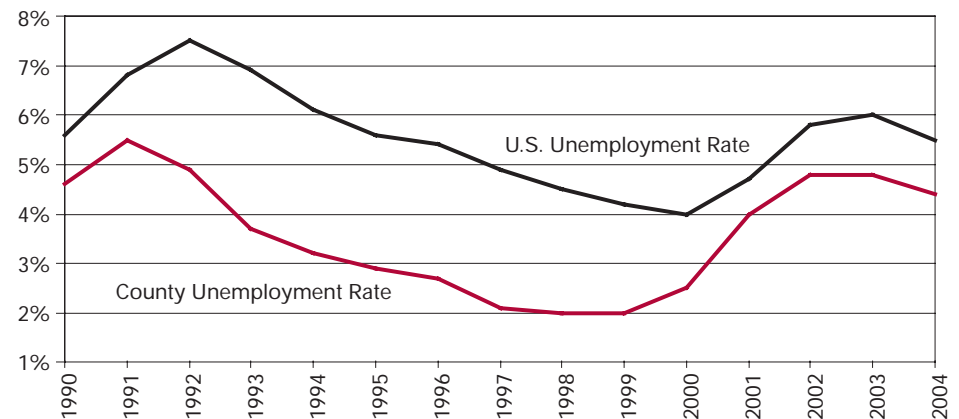
Source: STATS Indiana 2003 Commuting Profiles

Columbus and Bartholomew County are sensitive places. When the U.S. economy is happy, the local area is very happy. When the U.S. economy is a little sad, Columbus and Bartholomew County feel terrible.

Figure 1 shows the historical patterns of unemployment, illustrating this special sensitivity. Coming out of the recession of the early 1990s, the U.S. unemployment rate improved by about 1.5 percentage points in the first two years of the recovery. Bartholomew County's rate dropped faster, falling 2 full points. Unemployment in this area improved to a low point by 1998 and remained there in 1999, a decline of 3.5 points from its recent peak. The U.S. rate also shrank by 3.5 percentage points but took longer to get there.

This area tends to react quickly to changes in the national economy — sometimes even getting a head start. The recession of 2000 pushed the national unemployment rate up by 2 percentage points, starting in 2000. Sensitive Bartholomew County reacted more strongly. Its rate went up 3 points, and the problems started almost a year earlier.

**Figure 1**  
Bartholomew County vs. United States Unemployment Rate, 1990 to 2004



Source: Bureau of Labor Statistics

This pattern shows up in many sectors of the Bartholomew County economy. Take the construction industry: Figure 2 shows how that sector in Columbus and Bartholomew County has reacted to the general level of economic activity in the nation. The bars show the rate of growth or decline in construction employment in this county. The line tracks the annual percent change in U.S. gross domestic product (GDP). (There is no data point for Bartholomew County in 2001 because the definition of construction has changed between SIC and NAICS.)

The dip in GDP in 1991 caused a big drop in the number of jobs. Afterwards the strong national recovery during the early 1990s led to even stronger growth rates in Columbus-area construction employment: the bars are higher than the GDP line. The relatively mild national slowdown in 2000, however, caused real whiplash locally. The last two years of available data show significant declines in jobs.

Bartholomew County's manufacturing sector is big (more than 35 percent of all jobs in the county) but it reacts to national



# Evansville

**M. Gale Blalock**

Professor of Economics and Chair,  
Department of Accounting and Business  
Administration, University of Evansville,  
Evansville

trends, too. One big influence is the level of vehicle sales. **Figure 3** shows this relationship, once again showing percent changes. Sales of cars and light trucks in the United States exhibit wide swings in the annual percent change. But Bartholomew County's manufacturing employment tracks these changes pretty closely. And the bad news is that vehicle sales are not likely to be as strong in 2006 as in some recent years. So local manufacturing employment probably will not rise much, either.

This historical sensitivity provides a way to think about Bartholomew County's economic future. The forecast from Indiana

University for the U.S. economy is cautiously optimistic. Assuming that interest rates and oil prices don't climb more than expected, the U.S. GDP should expand at about the same rate as in 2005, or about 3.6 percent. That means the local construction industry should have a reasonably good year.

U.S. unemployment rates, however, are not forecast to improve

much. So the unemployment rate in Bartholomew County probably will not get below 4 percent. The impressive numbers from the 1990s, when we saw unemployment rates here around 2 percent, just are not in the cards for next year.

Vehicle sales are a good indicator for the local manufacturing sector. And vehicle sales are not likely to improve much in the face of high fuel prices and rising interest rates in 2006.

Moves in the U.S. economy often translate into even bigger moves in the local economy. So watch the numbers for U.S. GDP, the national unemployment rate, and vehicle sales. If those numbers start to

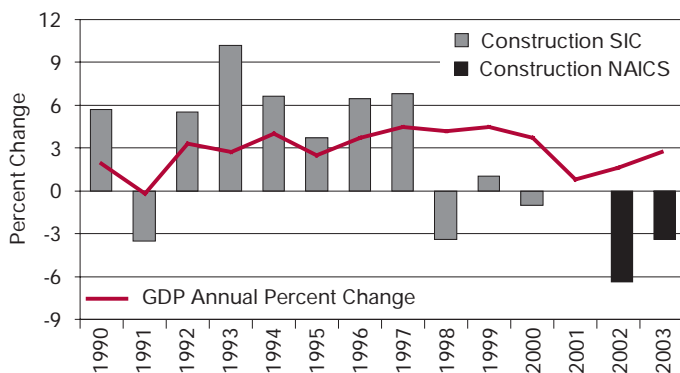
look better than expected next year, Bartholomew County could be very happy. But if the national situation turns out as forecasted, we'll see little or no improvement in U.S. unemployment and vehicle sales. And that means 2006 is probably not going to show much new business or many new jobs in Columbus and Bartholomew County. ■

“The Columbus area tends to react quickly to changes in the national economy—sometimes even getting a head start.”

It is time for a change. Faithful readers of this space will recall that the Evansville economy did not show substantial growth after the turn of the century, according to the index of economic activity maintained at the University of Evansville. That index used fixed 1998 value-added components from that year's gross domestic product (GDP) as its fixed weights. This fixed weight index methodology is similar to the way the Consumer Price Index is calculated. This year, the weights have been updated and the hospital sector has been added.

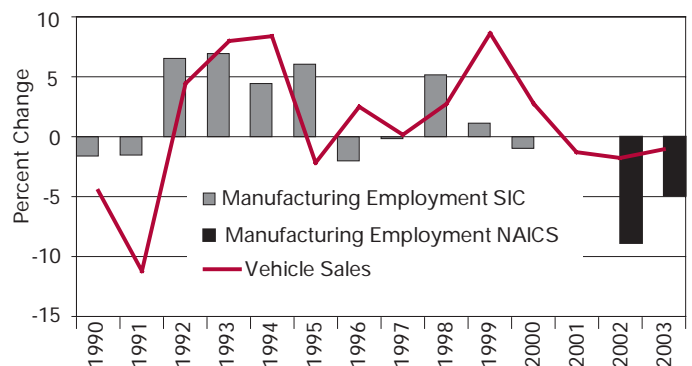
The new categories capture about 60 percent of value-added for the nation. The old index indicates a small contraction from 2002 to 2003 while the new index indicates a substantial increase from 2002 to 2003. The new index posts a decline of 2.5 percent from 2003 to 2004 (see **Table 1**). This decline was centered in construction and finance. Even the strong and continued growth in health and the other sectors was not sufficiently strong to counteract the negatives reported in construction and finance.

**Figure 2**  
Bartholomew County Construction Employment and U.S. GDP, 1990 to 2003



Note: Data for 2001 not available due to change in reporting.  
Source: Bureau of Economic Analysis

**Figure 3**  
Bartholomew County Manufacturing Employment and U.S. Auto and Light Truck Sales, 1990 to 2003



Note: Data for 2001 not available due to change in reporting.  
Source: Bureau of Economic Analysis

# Fort Wayne

**John Stafford**

Director, Community Research Institute, Indiana University Purdue University, Fort Wayne

Interest rates will continue to move away from historic lows to levels near their historic averages. These increased interest rates are not likely to make doing business in the durable goods or construction sectors any easier. The effects of higher interest rates on the finance sector remain uncertain. We can thank the employers of our area for substantial job growth in the past and hope for stability in the future. Again, barring any unexpected local, national, or international developments, 2006 will be much like 2005 for the Evansville area. ■

## Notes

The index is defined as follows:

**Health** = total gross patient revenue in acute care hospitals. **Industrial**

**Production** = electricity sold to industrial users. **Construction** =

total value of new construction permits in Vanderburgh County.

**Transportation** = annual boardings at the Evansville Regional Airport. **Trade**

= metropolitan area employment in wholesale and retail trade. **Finance** =

finance sector employment.

The Fort Wayne area economy is steadily but gradually rebounding from the recession of the early portion of this decade. From an employment perspective, it appears that northeast Indiana hit the low point of the downturn in the last three quarters of 2003 and the first quarter of 2004. The past year has witnessed a substantial upturn in the number of new project announcements for both facility/equipment investment and job creation. While Fort Wayne has a significant distance to travel to get back to the employment highs reached in 1999 and 2000, it is at least now moving in the right direction.

A formal geographic definition of northeast Indiana is a constantly moving target. This analysis will use the newly established Fort Wayne–Huntington–Auburn Consolidated Statistical Area (CSA), which includes Adams, Allen, DeKalb, Huntington, Noble, Wells, and Whitley counties. Larger than the newly-delineated Fort Wayne Metropolitan Statistical Area

(metro), it is a better indicator of the true Fort Wayne area economy.

Based on employer-reported data (the Quarterly Census of Employment and Wages, or QCEW), total employment in the area began to increase in the second quarter of 2004 and has increased each of the last four quarters of reported data when compared with the same quarter of the previous year. Between the first quarter of 2004 and the first quarter of 2005, the area gained 1,955 total jobs for an annualized growth rate of 0.7 percent. During the same time period, Indiana's total employment grew by 1.2 percent and the United States' by approximately 1.8 percent. Compared to the first quarter of 2000, a time of peak employment for our region, we are still down over 17,000 jobs. At the current job growth rate, it will take several years to fully recover the employment so quickly lost in the early part of the decade.

Of the nearly 2,000 job increase in over the past year, noticeable growth occurred in the health care, wholesale trade, and manufacturing sectors. Declines occurred in the retail trade and the finance and insurance sectors. Of particular note is the creation or re-establishment of 760 manufacturing jobs. Given the ongoing productivity improvements and the pressures facing the automotive supplier network—a significant component of northeast Indiana's industrial base—this increase is welcomed news.

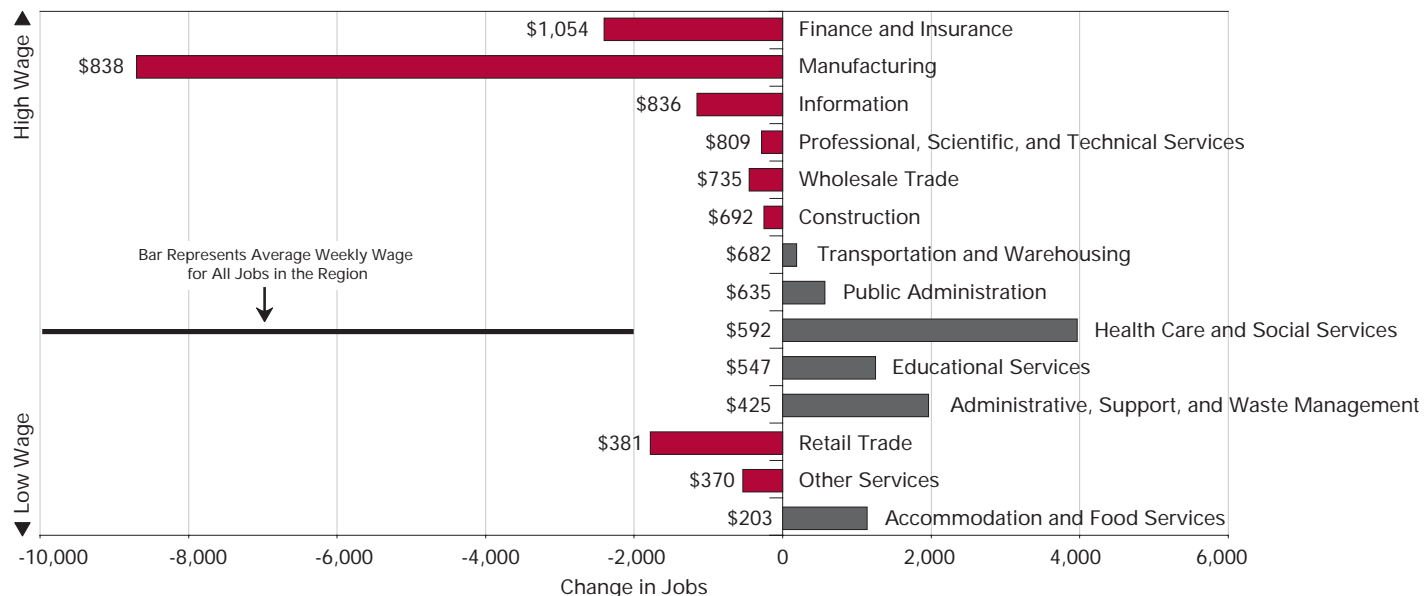
The other primary source of employment data, the monthly household survey (Local Area Unemployment Statistics), provides even more positive news. This source, perhaps less reliable but more current than the QCEW data, also indicates that by the third quarter of 2004, our region began experiencing consistent monthly employment growth. Comparing each month to the corresponding month from the

**Table 1**  
Evansville's Old and New Indices

The Old Index								
Year	Industrial Production	Construction	Trade	Transportation	Finance	Index	Index Growth	
1999	0.385	0.090	0.282	0.062	0.247	1.066	6.6%	
2000	0.397	0.072	0.285	0.060	0.254	1.068	0.2%	
2001	0.387	0.045	0.288	0.052	0.280	1.053	-1.4%	
2002	0.401	0.064	0.284	0.052	0.254	1.054	0.1%	
2003	0.385	0.071	0.283	0.050	0.260	1.049	-0.5%	
Percent Change from 2002								
	-4.0%	10.9%	-0.4%	-3.8%	2.4%	-0.5%	n/a	
The New Index								
Year	Health	Industrial Production	Construction	Trade	Transportation	Finance	Index	Percent Change
1999	0.055	0.200	0.112	0.194	0.056	0.378	99.4	n/a
2000	0.072	0.207	0.089	0.196	0.054	0.388	100.6	1.2%
2001	0.080	0.201	0.056	0.198	0.047	0.429	101.1	0.5%
2002	0.087	0.209	0.079	0.195	0.046	0.388	100.4	-0.7%
2003	0.101	0.200	0.088	0.194	0.045	0.398	102.6	2.2%
2004	0.113	0.211	0.076	0.210	0.048	0.342	100.0	-2.5%
Percent Change From 2003								
	11.9%	5.5%	-13.6%	8.2%	6.7%	-14.1%	-2.5%	n/a

Source: University of Evansville

**Figure 1**  
**Fort Wayne CSA Change in Jobs by Major Industry, 2001:1 to 2005:1**



Source: Bureau of Labor Statistics

prior year (necessary when using non-seasonally adjusted data), employment totals for the second and third quarters of 2005 indicate that the region is now experiencing employment growth at a rate that would annually support job creation of approximately 3,200 in the CSA.

While the sustained upswing in employment for the first time this decade (based on the QCEW data) has been anticipated and tracks with what is being experienced statewide and nationally, it does not portray the total picture of regional economic dynamics. Of lingering concern to our area is the continuing lag in relative wage growth. The Indiana Department of Workforce Development has recently divided the state into eleven economic growth regions (EGRs). The northeast Indiana area—EGR 3—has experienced the slowest rate of wage growth of any of the eleven regions between 2001 and 2004. EGR 3 includes the Fort Wayne–Huntington–Auburn CSA plus Grant, LaGrange, Steuben, and Wabash counties. We experienced a 7.2 percent growth in average annual wages over

the four-year period, compared with a statewide growth rate of 9.2 percent.

Stepping back from the details for a minute to look where job growth and loss has occurred in the CSA since the beginning of 2001 (when the Bureau of Labor Statistics began reporting employment data utilizing the NAICS industry classifications), a revealing picture emerges. **Figure 1** illustrates the job growth or loss for each of the two-digit NAICS classifications which have a significant employment presence in the CSA. These industry sectors have been placed on the chart from top to bottom in descending order based upon their respective average weekly wage. Each bar represents the job gain or loss over the four-year time frame in a respective business sector. As can be seen, northeast Indiana has generally been losing jobs in the higher paying sectors while gaining jobs in those at the lower wage end of the continuum. The first quarter 2005 average weekly wage for all jobs covered by unemployment insurance was \$632, as illustrated by the black line on the chart.

In 2006, northeast Indiana should expect to see continued job growth, likely at a pace reflective of that for Indiana statewide. On the conservative end, adding an additional 2,000 to 2,500 jobs to the Fort Wayne–Huntington–Auburn CSA should be very achievable. If the ongoing churn of job creation, company expansion, and business attraction mixed with the inevitable job losses through downsizings, mergers, and company failures breaks on the positive side, it may be possible to continue the very recent rate of growth and add between 3,000 and 3,500 jobs. There is, however, one very important cloud on the horizon. My predecessor and frequent contributor to the *Indiana Business Review*, Dr. Thomas Guthrie, used to say that “when the automobile industry catches a cold, northeast Indiana gets pneumonia.” If the domestic automobile supply network unravels to the extent that recent announcements portend that it could, the fallout will undoubtedly hit this region very hard. In that event, all net job growth bets are off. ■

# Gary

**Donald A. Coffin, Ph.D.**

Associate Professor of Economics,  
Indiana University Northwest, Gary

**N**orthwest Indiana<sup>1</sup> continues to struggle to recover from the recession that began in the spring of 2001 and ended in the fall of the same year. While the recession was brief and relatively mild nationally, total employment in northwest Indiana fell by about 2 percent immediately, and, in 2005, is about 3 percent below its 2001 level.<sup>2</sup> Average annual earnings per worker should remain relatively unchanged in 2006 (compared with 2005). Meanwhile, a shrinking labor force (down by 2.5 percent between 2001 and 2004, and projected to decline by another 0.7 percent by 2006) has accompanied a slowly falling unemployment rate.

Between 2005 and 2006, employment should rise very modestly—by about 0.2 percent, or 700 new jobs. This increase in total employment masks declines in almost every industry sector—only service employment will grow significantly (3,000 additional jobs, a 2.2 percent increase over the 2005 level), with employment outside of services declining by about 2,300 jobs. The unemployment rate is likely to fall, from 5.9 percent in 2004 to 5.8 percent in 2005 to 5.7 percent or 5.6 percent

**Table 1**  
**Employment and Employment Growth by Industry**

Industry	Estimated 2005 Employment	Projected 2006 Employment	One-Year Growth	Five-Year Growth
Total	387,100	387,800	+0.2	-3.1
Construction	24,800	24,400	-1.9	-7.8
Manufacturing	46,200	44,600	-3.4	-23.2
Transportation and Utilities	19,700	19,500	-0.7	-5.3
Wholesale Trade	15,500	15,600	+0.4	+0.1
Retail Trade	74,000	73,900	-0.2	-2.2
Finance, Insurance, and Real Estate	22,200	22,100	-0.2	-6.2
Services	134,600	137,600	+2.2	+9.6
Government	50,000	49,900	-0.2	-2.7

Note: Employment data are rounded to the nearest hundred; percent changes are calculated from unrounded data. Source: Historical data from STATS Indiana. Forecast calculated by author.

in 2006. However, this decline is a result of a declining labor force, not of employment growth.

## Employment

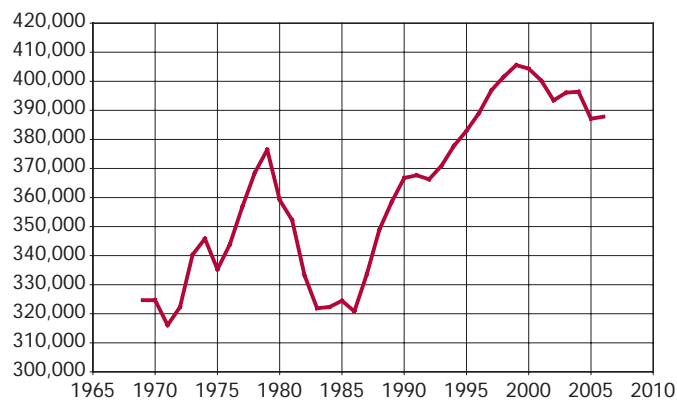
**Figure 1** charts the changes in total employment in northwest Indiana from 1969. Most recently, total employment peaked in the late 1990s and began a slow descent, which has not yet decisively been halted. Although employment should rise slightly in 2006, that increase will leave total employment at about the level it reached in 1996. **Table 1** presents expected 2005 and projected 2006 employment levels by major industry classifications and 2005–2006 and 2001–2006 employment growth rates.

**Manufacturing:** The decline in total employment also shows up in manufacturing employment, which

continues its steady decline. About 22,000 manufacturing jobs have been lost since 1996, and employment should decline by about another 1,600 jobs between 2005 and 2006. Much of this decline has occurred in the steel industry, with about 9,000 jobs lost in the 1996–2005 period. Employment in steel appears, however, to have stabilized at about 20,000 jobs and should maintain that level in 2006.

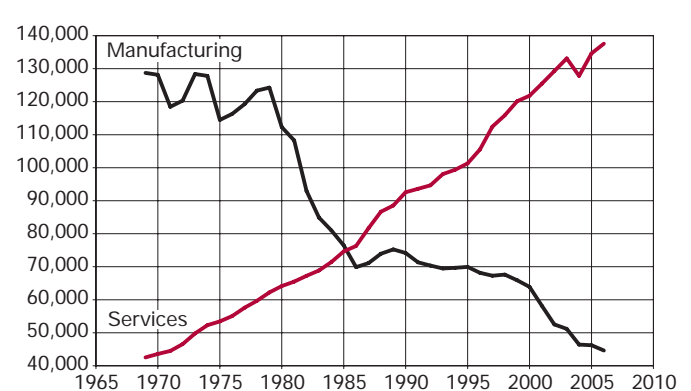
**Services:** Only service employment has shown any strength in recent years, and, indeed, service employment has become the dominant sector of the local economy, at least in terms of employment (see **Figure 2**, which shows the reversal in importance of manufacturing and service employment). Within the service sector, the most rapid growth between 2001 and 2005 occurred in health care (+11.7 percent, with even

**Figure 1**  
**Total Employment**



Source: Historical data from STATS Indiana. Forecast for 2006 calculated by author.

**Figure 2**  
**Manufacturing and Services Employment**



Source: Historical data from STATS Indiana. Forecast for 2006 calculated by author.

more rapid growth in ambulatory health care and in nursing and residential care facilities). This rapid growth can be expected to continue, with perhaps 1,000 of the 3,000 new service jobs in health care. Employment in hospitals was essentially unchanged. Employment in professional, scientific, and technical services<sup>3</sup> rose by 8 percent between 2001 and 2005, with 700 new jobs being created. Although the growth here is likely to continue to be strong, only about 150 new jobs are likely to be added between 2005 and 2006.

**Transportation, Distribution, and Logistics:** This sector has been identified as having the potential to provide major stimulus to the northwest Indiana economy.<sup>4</sup> Certainly, northwest Indiana is well positioned to take advantage of a nationwide transportation network, including rail, truck, and air transportation. Data sources do not provide data on the number of establishments or on employment in air and rail transportation, as the number of firms is too small to permit such publication. Trucking has grown locally from 2001 to 2005, with about 900 additional jobs (nearly 15 percent growth), although the number of firms has declined slightly. The past five years in wholesale trade shows a mixed picture, with fluctuating employment, but a 7 percent increase in the number of firms. Overall, employment in these two industries looks to be about the same in 2006 as in 2005.

**Other Sectors:** No other sectors are likely to experience either rapid growth or decline. Of some interest are the employment developments in construction. Construction employment has grown very slowly in Lake and Porter counties (growing about 5 percent between 2001 and 2005) and has been about unchanged in La Porte County. This suggests that construction employment has been declining in the less urban counties

**Table 2**  
Average Annual Real Earnings per Worker and Earnings Growth by Industry

Industry	Estimated 2005 Earnings	Projected 2006 Earnings	One-Year Growth	Five-Year Growth
Total	\$37,800	\$37,900	+0.1	+4.7
Construction	\$48,900	\$48,800	-0.2	+4.9
Manufacturing	\$69,000	\$68,500	-0.6	+11.2
Transportation and Utilities	\$53,300	\$53,500	+0.3	+1.9
Wholesale Trade	\$48,200	\$48,100	-0.3	-1.6
Retail Trade	\$17,700	\$17,600	-0.6	-3.1
Finance, Insurance, and Real Estate	\$26,400	\$26,200	-0.6	+5.4
Services	\$29,400	\$29,300	-0.3	-1.6
Government	\$41,100	\$41,300	+0.4	+2.6

Notes: Earnings data are adjusted for inflation and rounded to the nearest hundred dollars. Percent changes were calculated from unrounded data.

Source: Historical data from STATS Indiana. Forecast calculated by author.

of northwest Indiana, and that the expected decline in 2006 is also likely to be concentrated in Jasper, Newton, Pulaski, and Starke counties. In addition, it is difficult to reconcile the slow growth in construction employment with the anecdotal perception of construction as a thriving sector. Housing construction appears to have been quite strong, and highway construction appears to be everywhere. In fact, employment in heavy and civil engineering construction has grown by about 10 percent since 2001.

**Unemployment:** The unemployment rate in northwest Indiana has generally tracked the changes in the national economy, declining in the late 1990s, rising through the 2001 recession, and declining slowly since 2002. The unemployment rate, averaging about 5.8 percent in 2005, should continue to decline to 5.6 percent or 5.7 percent in 2006. However, this does not necessarily represent any noticeable strengthening of the labor market. As noted above, employment will grow very modestly. The driving force in lowering the unemployment rate is, it turns out, a continuing decline in the labor force of northwest Indiana.

The labor force—residents of northwest Indiana who are either employed or seeking work—peaked in the late 1990s and has declined since. The decline between 2001 and 2004 was about 2.5 percent, with

about 10,000 fewer people in the labor force. By 2006, the total decline in the labor force projects to a little over 12,000 workers, with the decline between 2005 and 2006 coming in at about 1,000. With fewer people participating in the labor force, firms will experience difficulty in expanding employment rapidly. It seems likely that the decline in the labor force has been one of the factors leading to slow employment growth. The slow growth in the labor force reflects the slow growth in, and aging of, the population. Total population has grown by only 3 percent in the last thirty years, and about 13 percent of the population was age 65 or older in 2003 (a share that continues to rise over time).<sup>5</sup>

## Earnings

**Table 2** shows average annual (real) earnings per worker, for all workers and by industry; data for the 1969–2006 period for all workers compared to manufacturing workers is shown in **Figure 3**. Total average annual earnings peaked in northwest Indiana in 1978, at about \$47,200, and have subsequently declined to about \$37,800 in 2005. Predicted annual earnings for all workers in 2006 are \$37,900, an increase of about 0.3 percent. Much of the decline in average earnings can be attributed to a change in the industrial composition of employment, particularly the decline in manufacturing employment

# Indianapolis

**Philip T. Powell, Ph.D.**

Associate Clinical Professor of Business Economics, Kelley School of Business, Indiana University, Indianapolis

The data and forecasts in this article refer to the entire Indianapolis metro, including Boone, Hamilton, Hancock, Hendricks, Johnson, Madison, Marion, Morgan, and Shelby counties. Unless otherwise stated, all data is from the U.S. Census Bureau ([www.census.gov](http://www.census.gov)) or STATS Indiana ([www.stats.indiana.edu](http://www.stats.indiana.edu)). STATS Indiana is maintained by the Indiana Business Research Center at the Indiana University Kelley School of Business.

(where annual earnings were about \$70,000 in 1978, projected to be about \$68,500 in 2006) and the rise in service employment (with earnings of about \$30,500 in 1978 and \$29,200 in 2006).

Real earnings growth from 2001 to 2006 has been adequate, if not spectacular, averaging 4.7 percent, with even more rapid growth in construction, manufacturing, and in the financial sector. The earnings growth in manufacturing has been led by very strong earnings growth in the steel industry, where average annual earnings rose by about 30 percent, largely as a result of increased overtime pay. Outside of steel, earnings in manufacturing have declined from 2005 to 2006.

Earnings growth over the next year will be very weak across industries in all likelihood, a consequence of the slow growth in employment. In addition, the slow growth in earnings will contribute to slow growth in retail trade and in services.

## Conclusions

Northwest Indiana will continue its slow growth. Employment and earnings will grow more slowly than in the state, even as Indiana grows more slowly than the nation. Employment growth of about 0.2

percent with an earnings increase of about 0.3 percent will lead to roughly constant total labor income in the region in 2006 compared with 2005. Slow growth in employment will place downward pressure on earnings growth, and reduced earnings growth will place downward pressure on employment growth in the retail sector and in services. The unemployment rate will decline fractionally, largely as a result of a continued decline in the labor force. The short-term outlook for the northwest Indiana economy continues to be discouraging. ■

## Notes

1. Beginning with the 2006 outlook, the northwest Indiana region will consist of seven counties: Jasper, Lake, La Porte, Newton, Porter, Pulaski, and Starke. Slightly more than 90 percent of the region's employment is located in Lake, La Porte, and Porter counties.
2. All data on employment, unemployment, and earnings in this report come from STATS Indiana ([www.stats.indiana.edu](http://www.stats.indiana.edu)), or are estimates and forecasts prepared by the author.
3. This includes lawyers offices, accounting firms, architectural and engineering firms, etc. See <http://www.census.gov/epcd/naics02/naicod02.htm> for complete details on the NAICS industrial classification.
4. *Northwest Indiana Times*, 30 October 2005, p. 1.
5. About 26 percent of the population was under 18 in 2003, a percentage that has also increased in recent years.

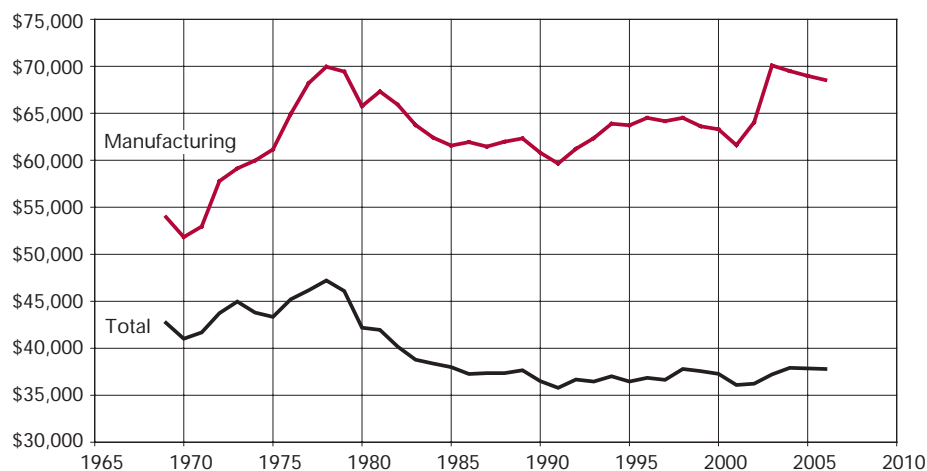
## Income

Income for households in the Indianapolis metro is shrinking. According to the U.S. Census Bureau's American Community Survey, real median family income in Indianapolis fell \$2,240 and only \$491 nationally between 2002 and 2003. Between the first quarters of 2004 and 2005, real weekly wages fell 2.7 percent. Income shrinkage is caused by two things. First, there is no dynamic growth in the local economy. Second, high-paying professional jobs are disappearing as Indianapolis-based corporate headquarters are closed through merger and bankruptcy (such as Great Lakes Chemical Company, Galyans, and American Trans Air).

## Employment

Between August 2004 and August 2005, the local unemployment rate increased from 4.6 percent to 4.7 percent, while the national unemployment rate fell from 5.4 percent to 4.9 percent. More individuals have entered the labor force in Indianapolis, but their wait for a new job has not shortened like it has in the rest of the United States. Between 2004 and 2005, the highest rates of local job growth were 9.7 percent in administrative services, 6.0 percent in transportation and warehousing, and 4.1 percent in

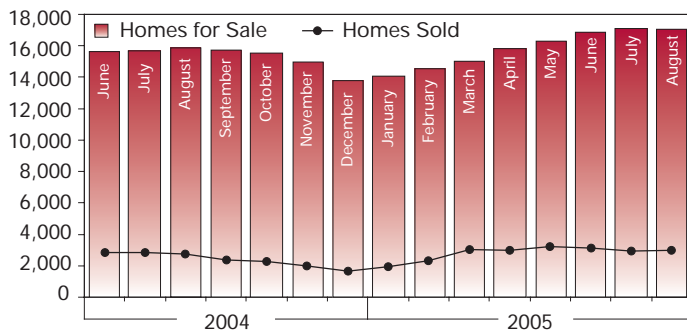
**Figure 3**  
Average Annual Earnings for All Workers and Manufacturing Workers



Note: Data are adjusted for inflation.

Source: Historical data from STATS Indiana. Forecast calculated by author.

**Figure 1**  
**Metro Homes Sold Compared to Homes for Sale, 2004 to 2005**



Source: [www.ftucker.com/news/index.html](http://www.ftucker.com/news/index.html)

professional and scientific services. Finance and insurance jobs shrank by 2.8 percent and growth in government jobs was flat. All other sectors of the local economy saw job growth of 3 percent or less.

### Real Estate

Between April 1, 2000, and July 1, 2003, the U.S. Census Bureau estimates that the population of the Indianapolis metropolitan area increased by 70,273 individuals (4.6 percent). From the beginning of 2001 to the end of 2003, enough building permits were approved to house an estimated 211,507 individuals in new structures.<sup>1</sup> This trend suggests that housing capacity is expanding at three times the rate of population growth. Employment in construction remained steady at 45,000 jobs between the first quarters of 2004 and 2005, but the average wage fell from \$788 to \$770 per week.

**Figure 1** shows home sales in the past year. A situation of excess supply explains why the real value of residential real estate in the metro has fallen 1.5 percent over the last four years.<sup>2</sup> Only 40 percent of the new housing being constructed is in Marion County. Between April 1, 2000, and July 1, 2003, the U.S. Census Bureau estimates that the population of Marion County grew by 3,407 while the populations of Hendricks and Hamilton counties grew by 14,787 and 38,124, respectively. These numbers underscore massive migration out of Marion County townships and into suburban communities. In an environment of excess housing

supply, this type of population movement negatively impacts the real wealth of both urban and suburban residents. Real estate values in Marion County fall because there is no increase in population. Real estate values in suburban communities do not appreciate because the construction of new homes floods local markets and keeps prices low.

### Forecast

The current Indianapolis economy is anemic and will continue to fall behind the nation in 2006. Permanently higher energy prices, cheaper labor in foreign countries, and a possible General Motors bankruptcy place worrisome pressure on a local economy that remains too dependent on non-vibrant industries. Job growth will occur, but at an unimpressive rate and not in high-paying occupations. Real household income is expected to shrink locally by 1 percent in 2006. Real estate wealth will also shrink as developers continue to build in over-supplied communities and deflate the price of homes in neighborhoods that are already established. Growth among local life science and technology enterprises will be notable, but their small presence in the Indianapolis economy will not reverse a more general malaise. If the current trend continues, Indianapolis risks becoming an economic satellite of cities that demonstrate a more energetic and pioneering approach to economic development. ■

### Notes

1. This calculation assumes 2.6 individuals per household, as estimated by the U.S. Census Bureau.
2. Calculation based on data from "Bringing Down the House," *Indianapolis Star* 16 October 2005.

# Kokomo

## Brian Harris

First Vice President, First National Bank and Trust

with input from

## Walter Wolff,

Regional President, STAR Financial Bank

and **John O'Donnell**

President, First National Bank and Trust

**T**he short-term economic forecast for Kokomo can be summed up with one word: uncertainty. The local Kokomo economy will suffer in 2006 more from the apprehension and fear of impending local manufacturing changes rather than from the changes themselves, which will not occur for some time.

It is difficult to focus on the local economy when it is so heavily dependent on global markets, since our largest local employers have locations and vendors scattered across the world. As our largest employers go, so goes the city. With that said, a large amount of apprehension exists in the local economy while the second largest employer, Delphi, works through a reorganization plan that will most likely drag out to the end of 2006. Meanwhile, the largest employer, DaimlerChrysler, is financially sound and continues to benefit from its large capital investments in Kokomo. Kokomo was at one time number one in the nation for European investment, almost entirely due to DaimlerChrysler. However, DaimlerChrysler will be closely monitoring the wage negotiations with Delphi as their next contract negotiations near in 2007. Workers are one of the most important and expensive commodities to the majority of large corporations, and the most efficient productivity for the lowest price will prevail in their strategic planning in nearly all instances. Compensation restructuring and/or job reductions at Delphi will negatively affect Kokomo.

Kokomo's economy remains heavily tied to the manufacturing

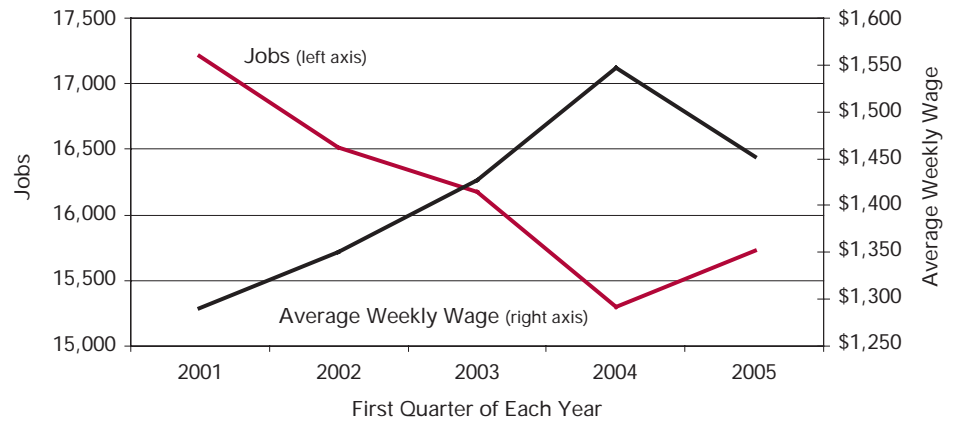
industry, specifically the automotive industry. Manufacturing jobs in the area and the state as a whole continue to be lost permanently to competition, mainly from overseas facilities as their productivity and operations in general continue to improve (see **Figure 1**). The auto industry is volatile, but has been very strong in the past twelve months, as loan rates remained low and incentive pricing, including offering employee discounts to everyone, kept sales strong. This kept demand high for a second year in a row with a different marketing approach to the 0 percent financing that was offered in 2004. This has helped protect jobs in the area, but the automakers may not be able to maintain this sales pace and the demand may fall back to normal levels as interest rates increase and they prepare a new marketing approach in 2006. The automakers have been showing signs of a shift in strategies to being more focused on productivity and cost of production to remain competitive for some time. Changes have been slow because of strong sales and long-term union contracts. Changes are inevitable and will have large consequences on the local manufacturing job market.

Our local charities will also feel the brunt of the community's apprehension and most are already searching for additional funds. A slump in the local economy will only increase the need for their services and decrease the amounts of money that they will have to operate.

Job creation will continue to lag well behind the state averages and will remain difficult due to the strong union influences and higher than average wages. The city would like to attract more high-paying jobs but

**“The Delphi bankruptcy reorganization will be the major cause of uncertainty and fear in the local economy for most of the year, causing a decrease in local customer spending and outside business investments.”**

**Figure 1**  
**Howard County Manufacturing Jobs and Average Weekly Wages, 2001:1 to 2005:1**



Source: STATS Indiana

as the economy changes, those types of jobs will require a higher level of skills and education than we may be able to offer at this point in time. The focus shifts to education, the quality of our schools and teachers and attracting the businesses that will hire the college graduates before they leave the area. Our local middle-class workers are being slowly reduced to just the working class, as wages and benefits are squeezed downward. The current Delphi situation will speed up this occurrence, which will

have severe consequences in the short-run, but may make Kokomo much more attractive to outside investment in the long-run depending on the outcomes.

The local real estate market will remain soft in the coming year as apprehension and speculation on salaries and job security remain the main topic of discussion. That, along with the anticipation of higher mortgage interest rates, will have the biggest impact on an individual's decisions to buy or build a home in the area. The housing market has been averaging over eight hundred listings per month

with only an average of just over one hundred sold per month through the third quarter of this year. There are also more than four hundred completed building lots available in the county at the present time with more being developed. These figures along with very low appreciation rates of homes and slowly declining population trends, make it difficult for homeowners to move within the county as well as elsewhere.

The trend for the upper middle-class wage earners in recent years has been to buy or build in counties south of Kokomo and commute. Nearly 5,000 people commute to Kokomo from Tipton and Hamilton counties alone. Compare this to the 1,400 workers commuting out of Howard County to Tipton, Hamilton and Marion counties.

Building permits have also declined in the past three years, from 448 in 2002, to 353 in 2003 to 268 in 2004. As of the third quarter of 2005, less than 125 residential building permits have been issued. Home values can also be directly related to the average family incomes of the area, especially since we don't have a major tourist attraction or any major natural draws such as lakes, mountains or an ocean to inflate demand and pricing. It is also unfortunate that the number one individual seller of homes in Howard County at the present time has been



# New Albany

the sheriff and his numbers could increase in 2006.

Overall, the Delphi proceedings may benefit Kokomo in the long run as pieces of the company are consolidated and Kokomo has the opportunity benefit from some of those contractions. Unfortunately, in the short run, local consumer confidence levels are low while the community waits on the outcome. This will affect small business owners the most as they compete for fewer disposable dollars from consumers. The consumers will most likely be a little more conservative for now and the total manufacturing salaries and wages in the county will inevitably see a reduction of some amount. Factor in increasing short-term interest rates, health care costs, and fuel and energy costs (compared to the twelve-month period just ended) and the most likely outcome will be a net loss of businesses in Kokomo during 2006. This is a domino effect as the small business owners do what they must to survive, cutting expenses themselves, which could be a reduction of hours or workforce as well. The key to their success will be the number of businesses that draw the transient or destination consumer from the north, east and west and those simply traveling through town.

Kokomo has always been resilient. Examples of past struggles would include the Continental Steel closing, the Chrysler bankruptcy in the 1980s and more recently the Haynes bankruptcy filing. The current troubles within the U.S. auto industry have been compared to the U.S. steel industry. The year 2006 will be another that tests the resiliency of Kokomo, as the second-largest employer makes drastic changes in its corporation. However, Delphi has a well-trained and skilled workforce with one of the best divisions of the company located in Kokomo. Kokomo should be able to rise to the occasion, reinvent itself, and actually come out of this better than it was going in. ■

## Dagney Faulk, PhD.

Associate Professor of Economics, School of Business, Indiana University Southeast

Economic indicators for southern Indiana show mixed results for 2005. Average employment in the Louisville Metropolitan Statistical Area (metro), and in southern Indiana in particular, increased for the second year in a row. Yet, indicators of consumer activity suggest that consumers may be starting to reign in spending. In this analysis, various measures of economic activity are examined for counties in the Louisville metro. Particular attention is paid to Clark, Floyd, Harrison, and Washington counties in southern Indiana and Bullitt, Jefferson, and Oldham counties in northern Kentucky.<sup>1</sup> Four additional Indiana counties—Crawford, Jefferson, Orange, and Scott—in the southern Indiana labor market area are included when available.

### Labor Markets

September unemployment rates in many of the Indiana counties of the Louisville area increased from September 2004 to 2005. From month to month, unemployment rates in many of these counties have actually decreased from earlier this year but continue to be quite volatile. Over the past year, unemployment rates in these counties grew to exceed that of the United States and the Indiana state average. **Table 1** suggests that part of the increase in unemployment rates in these counties can be attributed to increasing labor force participation; as job opportunities have increased, people who had dropped out of the labor force have begun looking for jobs. Clark, Floyd, and Scott counties, in particular, have shown substantial increases in labor force participation.

Recent data for the Louisville metro indicates that the average level of nonagricultural employment was 603,600 for the January–September 2005 period, an increase

of approximately 6,600 jobs from the same period last year and approximately 16,000 jobs below the 2000 peak of 620,000. Manufacturing jobs decreased by approximately 200 jobs in the metro area, while average weekly earnings in that sector declined an additional \$30 to \$766 for the January–September period. Metro area employment in retail sales continued its decline to 64,200 from a high of 70,500 in 1999.

Total employment has steadily increased in the southern Indiana counties, gaining over 1,000 jobs in the first quarter of 2005 from the same quarter in 2004 (see **Figure 1**). Job growth in the southern Indiana counties was led by transportation and warehousing (367 jobs) and health care and social services (261 jobs). Positive growth continued in several other sectors, including construction, retail trade, finance and insurance, administrative and support services, and educational services.

Manufacturing employment in the southern Indiana metro counties continues to decline (although at a slower rate), averaging just over 18,000 jobs for the first quarter 2005, a decline of just over 70 jobs over the same period in 2004. Manufacturing employment has steadily decreased from the 2001 peak of approximately 21,000 jobs. Despite significant job losses over the past several years, manufacturing remains the largest employment sector in southern Indiana with over 20 percent of total employment. The average weekly wage for manufacturing workers in southern Indiana has continued to increase, but remains consistently lower than that of the Louisville metro as a whole and the state of Indiana. While there is no standard measure of labor productivity for metropolitan areas, national averages suggest that labor productivity in manufacturing

has increased substantially, which would boost wages.

### Consumer Activity

*Sales and Marketing Management* magazine's 2005 Survey of Buying power shows continued increases in retail sales. Total retail sales in the Louisville metro increased by 5.7 percent from \$13.9 billion in 2004 to \$14.7 billion in 2005. This is significantly lower than the 11.6 percent increase in metro retail sales from 2004 to 2005, suggesting a dampening in consumer spending.

Jefferson County, Ky. had the largest change with over a \$449,000 increase between 2004 and 2005. Oldham County, Ky., Floyd County, and Harrison County had substantial positive growth in retail sales, at 18.0 percent, 14.8 percent and 9.7 percent, respectively, while the growth in Clark County was quite modest (3.6 percent) by comparison. The increased retail spending in Floyd and Harrison counties may indicate a redistribution of spending patterns due to new retail development. Retail sales growth outpaced inflation,

which was approximately 2.8 percent for the Midwest region between 2004 and 2005.

Activity in the residential housing market continued to increase over the past year, but at a slower pace than the previous year. Housing sales through October 2005 in the southern Indiana area<sup>2</sup> totaled 2,959 units—an 8.1 percent increase, compared with 12.1 and 13.9 percent increases for the same time period in 2004 and 2003, respectively. The average sales price was \$137,539 for January–October 2005 sales, up 4.2 percent from the

**Table 1**  
**Labor Force and Unemployment Rates, September of Each Year, 1999 to 2005**

Geography	1999	2000	2001	2002	2003	2004	2005
<b>Clark*</b>							
Labor Force	53,484	51,836	51,779	51,796	52,444	51,967	53,319
Unemployment Rate	2.6	2.7	4.4	4.7	4.7	4.7	4.9
<b>Crawford</b>							
Labor Force	5,463	5,101	5,273	5,298	5,225	5,373	5,462
Unemployment Rate	3.7	3	4.4	5	5.6	5.8	6.4
<b>Floyd*</b>							
Labor Force	39,339	37,549	37,458	37,220	37,091	36,738	37,743
Unemployment Rate	2.2	2.5	3.8	4.2	4.4	4.4	4.7
<b>Harrison*</b>							
Labor Force	19,083	18,435	18,458	18,522	18,885	18,719	19,421
Unemployment Rate	2.1	2.2	3.8	3.8	4.7	4.8	6
<b>Jefferson</b>							
Labor Force	13,554	16,138	16,389	16,499	16,809	16,978	17,381
Unemployment Rate	2.4	2.6	4	4.2	4.5	4.2	4.8
<b>Orange</b>							
Labor Force	8,784	9,573	9,396	9,185	9,033	8,997	9,026
Unemployment Rate	5.3	2.7	6.4	6.4	6.9	5.8	6.2
<b>Scott</b>							
Labor Force	11,240	11,249	11,051	10,972	10,901	11,140	11,501
Unemployment Rate	2.7	2.5	4.9	5.3	5.7	4.9	5.5
<b>Washington*</b>							
Labor Force	11,668	13,838	13,964	13,914	13,875	13,770	14,093
Unemployment Rate	3.5	2.8	5.3	5.1	5.3	5.4	5.4
<b>Louisville Metro</b>							
Labor Force	622,050	606,664	593,805	598,299	602,249	598,878	615,994
Unemployment Rate	3.5	3.2	4.3	4.7	5.6	4.4	5.3
<b>Indiana</b>							
Labor Force	3,131,258	3,117,405	3,145,090	3,156,404	3,158,344	3,161,637	3,222,728
Unemployment Rate	2.7	2.3	4	4.4	5	4.7	4.9
<b>Kentucky</b>							
Labor Force	1,939,975	1,947,164	1,934,449	1,950,155	1,978,396	1,964,754	2,012,844
Unemployment Rate	4.3	3.8	4.9	5	5.8	4.4	5.3
<b>United States</b>							
Labor Force	139,217,000	142,149,000	143,601,000	145,167,000	146,166,000	147,186,000	149,838,000
Unemployment Rate	4.1	3.8	4.7	5.4	5.8	5.1	4.8

\*Indiana counties in the Louisville metro, as defined June 2003.  
Source: Bureau of Labor Statistics

year before. The average amount of time for a house to sell was 108 days; the 2004 average was 98 days.

Residential construction as measured by residential building permits for new single-family units in the metro counties continued to slow and actually decreased in most metro counties (see **Table 2**). Permits for single-family units decreased by 9.7 percent for the January–September 2005 period. This is in sharp contrast to the 3.5 percent increase for the 2004 period and the 9.1 percent increase for the 2003 period. In addition, there was a substantial decrease of 38.8 percent in the number of permits issued for multi-family units. Only Clark and Washington counties experienced increases in single-family permits. Mortgage rates have been creeping up, contributing to the dampening of residential building permits and home sales.

Gaming at Caesars Casino experienced a decline in attendance in 2005. January through September 2005 admissions was 896,319, a 1.6 percent

**Table 2**  
**Building Permits, January through September\***

Single-Family Units						
Area	2000	2001	2002	2003	2004	2005
Clark	547	561	689	621	611	766
Floyd	282	282	254	331	268	264
Harrison	173	144	162	146	179	142
Scott	n/a	94	90	123	78	n/a
Washington	n/a	n/a	n/a	n/a	24	80
Bullitt	534	498	493	588	624	597
Jefferson	2036	2382	2,242	2476	2,570	2,036
Oldham	446	469	449	491	590	581
Multi-family Units						
Clark	18	189	76	122	94	12
Floyd	72	6	10	8	23	4
Harrison	26	0	4	6	0	0
Scott	n/a	73	72	15	4	n/a
Washington	n/a	n/a	n/a	n/a	10	0
Bullitt	56	37	76	92	125	65
Jefferson	531	321	540	673	510	359
Oldham	46	90	61	92	0	29

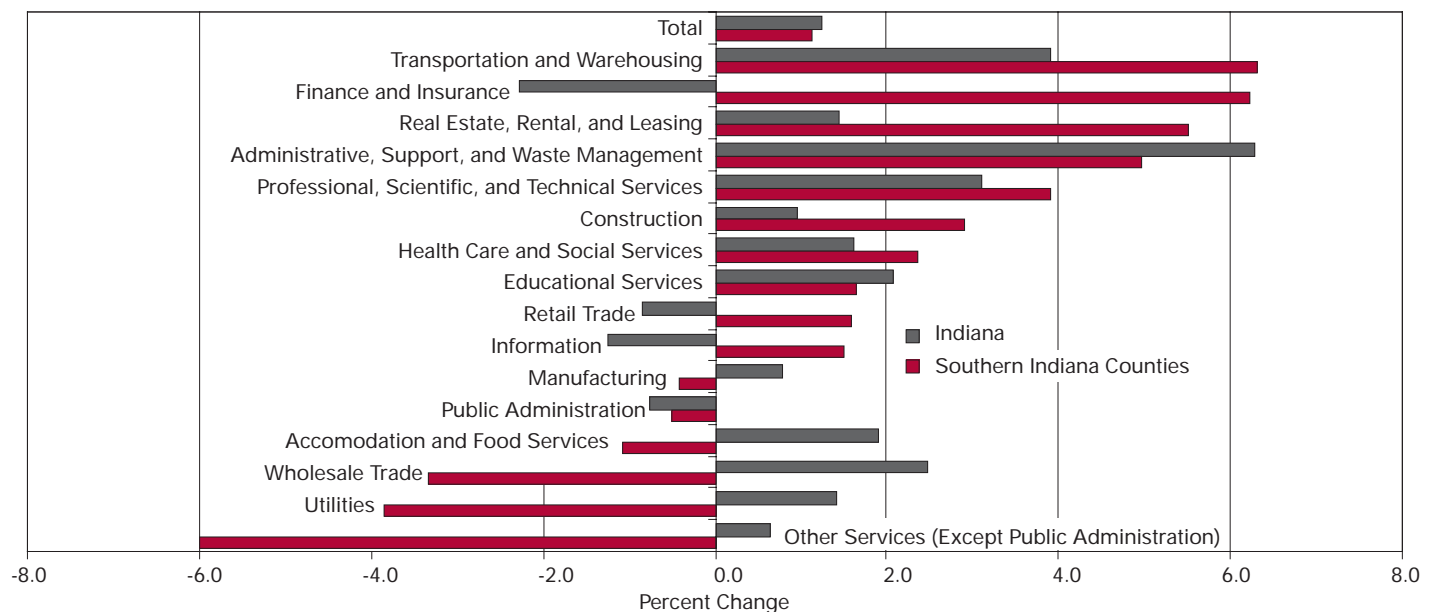
\*Estimates with imputation.  
Source: STATS Indiana, using U.S. Census Bureau data

**Table 3**  
**Caesars Indiana, Admissions and Total Taxes, January through September**

	2003	2004	2005	Change 2004–2005	Percent Change 2004–2005
Admissions	891,274	910,754	896,319	-14,435	-1.6%
Total Tax*	\$16,830,631	\$18,197,891	\$18,940,290	\$742,399	4.1%

\*Total tax includes admissions taxes and wagering taxes.  
Source: Indiana Gaming Commission Monthly Reports

**Figure 1**  
**Percent Change in Employment, 2004:1 to 2005:1**



Notes: Indiana counties in the Louisville metro (2003 classification): Clark, Floyd, Harrison, and Washington counties. Totals exclude county data that are not available due to nondisclosure requirements.  
Source: Indiana Business Research Center, using ES202 data

# Richmond

## Ashton I. Veramallay

Professor Emeritus and Director Emeritus, Center for Economic Education, Indiana University East, Richmond

decrease from the same period in 2004 (see **Table 3**). Tax payments totaled over \$18.9 million for the January–September 2005 period, a 4 percent increase over the same period in 2004.

In 2005, the available labor market data for Louisville and southern Indiana is fairly positive. While unemployment rates have increased and remain quite volatile, labor force participation has increased, suggesting that people are optimistic about finding jobs. Average employment increased by 6,600 jobs in the metro area, which includes an increase of over 1,000 jobs in the southern Indiana counties of the metro area. Consumer activity has dampened a bit. Retail spending in the Louisville metro continues to increase but at a slower rate and housing sales have increased relative to the previous year. The number of single-family residential building permits actually decreased in all counties except Clark and Washington, suggesting that the housing market is cooling. Cautious optimism is in order. Over the coming year, employment in the health care and transportation sectors are expected to remain strong. The dark cloud on the horizon is manufacturing employment, which continues to decrease. With the closing of the Colgate plant by January 2008, manufacturing will undoubtedly continue its decline. Retail spending will likely grow but at a slower rate, while activity in the housing market will continue to slow. ■

### Notes

1. In 2003, the Office of Management and Budget redefined the counties in the Louisville metropolitan area. They are Clark, Floyd, Harrison, and Washington counties in southern Indiana and Bullitt, Henry, Jefferson, Meade, Nelson, Oldham, Shelby, Spencer, and Trimble counties in Kentucky.
2. Data on home sales from the Southern Indiana Realtors Association Multiple Listing Service, which covers Clark, Crawford, Floyd, Harrison, Jefferson, Scott, and Washington counties.

There is mixed news coming from the Richmond–Connersville–New Castle (RCNC) area economy. The manufacturing sector, especially in Richmond, suffered a few plant closings in 2004 and 2005. A significant number of good-paying jobs were lost. Firms producing durable goods such as automobile parts, wire, and machine tools, are affected in varying degrees by current economic conditions. International competition from low-wage and low-cost producing nations, along with soaring commodity and energy prices, is affecting the bottom line of local firms.

Against this background, there is a silver lining. A few firms, such as Johns Manville, Osborn International, Berry Plastics, Contract Industrial Tooling, and JMC Restaurant Distribution, plan to expand in 2006. This internal expansion, plus the location of new firms (including both the strip mall adjacent to Hayes Arboretum by private investors and business prospects by the Economic Development Corporation of Wayne County) will brighten the employment picture. Taconic Farms and Kelsie's Food and Dairy, for instance, will add 250 new jobs, followed by the strip mall with another 200 jobs. Between January and August 2005, there was a net job gain of 268.

### Employment

The August 2005 figures, released by the Indiana Department of

Workforce Development, showed that the unemployment rates in Wayne, Fayette, and Henry counties were 7.0 percent, 8.1 percent, and 6.2 percent, respectively. These rates were higher than both the state rate of 5.2 percent and the national rate of 4.9 percent (see **Figure 1**). In terms of county rankings, they were second (Fayette), seventh (Wayne), and twenty-first (Henry). With the exception of Henry county, the unemployment rates inched upward from August 2004. In short, total employment was 63,120

from a labor force of 67,780, giving an employment-to-labor-force ratio of 93.1 percent while the employment-to-population ratio of 45.3 percent remained unchanged. The employment-to-labor-force ratio is expected to

improve with increased economic activity.

### Income

Slow job and productivity growth translates into slow income growth. Personal income is the income received by all persons from all sources or the total income for all households. It also reflects the quality of life in a community. The per capita personal income (PCPI) in 2003 for Wayne, Fayette, and Henry counties was \$25,316, \$27,172, and \$27,428, respectively. Indiana's 2003 PCPI was \$28,838, while the nation's was \$31,472. Analogously, the poverty rate in the tri-county area was 11.7 percent (Wayne), 10.4 percent (Fayette), and 9.5 percent (Henry).

The service sector continues to lead the local economy on the employment

“The housing sector is doing reasonably well after a slowdown in the first half of the year. There is an uptick in home sales partly due to the influx of professional and management people.”

# South Bend and Elkhart-Goshen

front. Growth in health care and education services, professional and business services, and personal services adds jobs and helps offset job losses in other sectors of the economy. It is important to note that Reid Hospital and Health Care Services, apart from its \$250 million complex on Chester Boulevard, is Wayne County's largest employer with 1,517 employees, followed by Richmond Community Schools with 853 employees.

## Housing

The housing sector is doing reasonably well after a slowdown in the first half of the year. There is an uptick in home sales partly due to the influx of professional and management people in RCNC. There is also upscale movement among existing homeowners. Interest rates are still relatively attractive. Local financial institutions reported on October 31, 2005, rates of 5.95 percent for fifteen-year mortgages, 6.32 percent for thirty-year mortgages, and 5.35 percent for one-year adjustable mortgages. Long-term rates on conventional mortgages are slightly lower than they were when the Fed began tightening policy in June 2004.

The City of Richmond issued 1,083 building permits with an investment value of \$17.2 million between January and September 2005. The local median price of a home is \$93,000, well below the national median of \$204,600. Home price increases are expected to slow with the market cycle, and if the Fed continues tightening policy, it will affect mortgage origination and equity extraction which, in turn, will affect personal consumption expenditures and gross local product.

Related to housing is banking. Banking activity is picking up. It is much better than a year ago. Profit margins are somewhat compressed because of low interest rates. There is also disintermediation of funds to brokerage houses. Disintermediation follows as depositors take their funds out of intermediaries and invest in open market instruments such as Treasury bills, commercial paper, and corporate bonds.

Barring external shocks to the U.S. economy, the RCNC economy is expected to perform better in 2006. There is, however, some degree of skepticism regarding consumer confidence and the future course of the national economy. ■

## Grant C. Black

Director of Bureau of Business and Economic Research and Assistant Professor of Economics, School of Business and Economics, Indiana University, South Bend

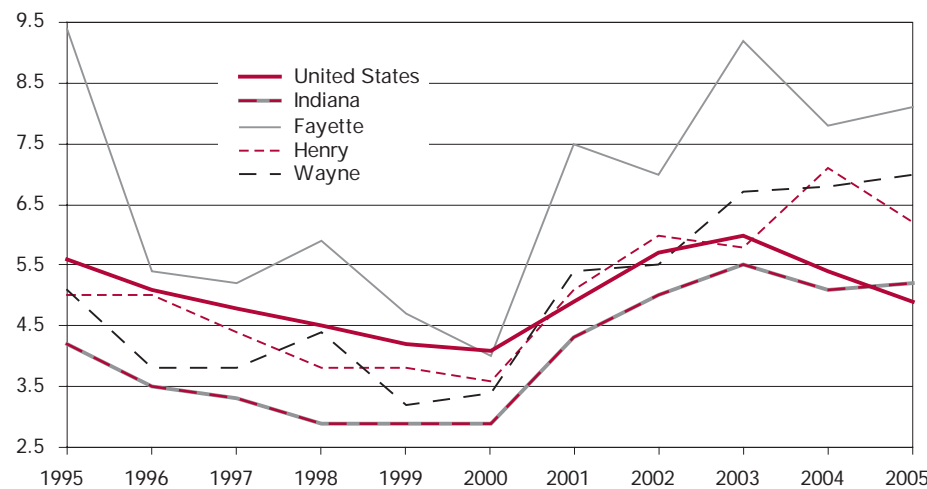
The Michiana region's economy sent mixed signals in 2005, but the outlook for 2006 is encouraging. This analysis examines the major metropolitan areas in the Michiana region, South Bend and Elkhart-Goshen, to provide an overview of the region's economic conditions and an indication of its future.

## Employment

Table 1 reports monthly employment data for the region's metropolitan areas. From January 2004 to August 2005, total nonfarm employment (measured by a seasonally adjusted index with 1986 as the base year) has decreased slightly. Total employment fell 1.5 percent in South Bend and 0.7 percent in Elkhart-Goshen. Unemployment rates across the region have remained below the national and state averages. The drop in unemployment rates in August 2005 indicates that labor demand has picked up again after a slight decline earlier in the year.

The overall employment decline was largely driven by a gradual drop in manufacturing employment through most of 2005. Manufacturing employment fell 2.5 percent in South Bend and 3.3 percent in Elkhart-Goshen from January 2005 to August 2005. While the recreational vehicle (RV) industry, which dominates Elkhart County employment, has experienced record growth in the past couple years, it faced declines in the first half of 2005, particularly for luxury motor homes. This was possibly caused by rising interest rates and escalating fuel prices. Rising fuel costs have dampened large-sized SUV sales nationwide, which likely impacted AM General's local production. The introduction of the

Figure 1  
Unemployment Rate, 1995 to 2005



Source: STATS Indiana

smaller-sized H3 Hummer produced outside the metro may reduce sales on the larger, locally produced models.

The second half of 2005 looked more promising for the transportation equipment industry. Demand for towable RVs continued to expand, and the manufactured housing industry rebounded from its slump due to increased demand for temporary housing caused by recent hurricanes. Soon after Hurricane Katrina hit, FEMA initially ordered 125,000 mobile homes and travel trailers, including many from local producers.<sup>1</sup> This increased production will continue well into 2006. In addition, new manufacturing developments in the region will require more workers. For example, Bennington Marine is constructing a new pontoon boat manufacturing plant in Elkhart that will employ 300 to 400 people.

Nonmanufacturing employment has also shown mixed results, falling 1.7 percent in South Bend but expanding 1.9 percent in Elkhart–Goshen from January 2005 to August 2005. This is partly due to a decline in the retail sector in South

Bend in terms of the number of establishments and employment from the first quarter of 2004 to the first quarter of 2005.<sup>2</sup> Retail employment, however, should rise in 2006 as new major retail spaces open, particularly in South Bend.

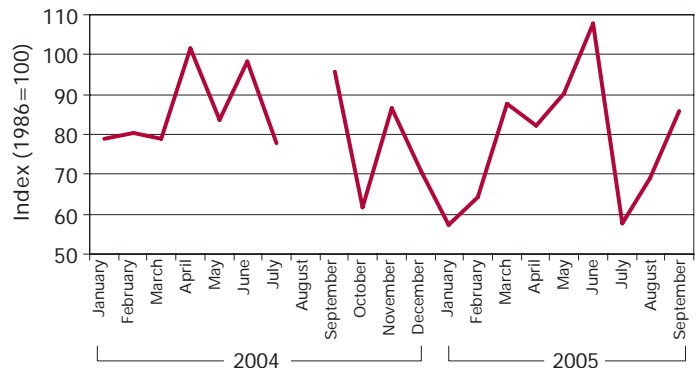
Moreover, continued growth in health care and social services contributed to positive expansion in nonmanufacturing. Health care and social services employment grew 5.5 percent from the first quarter of 2004 to the first quarter of 2005 in Elkhart County.

### Wages

The average weekly wage rose 2 percent from the first quarter of 2004 to the first quarter of 2005 in St. Joseph County but jumped 4.3 percent in Elkhart County. Manufacturing

wages grew 5.2 percent in St. Joseph County and 2 percent in Elkhart. Wages in retail moved slightly, falling 0.3 percent in St. Joseph County and rising 0.7 percent in Elkhart. Wages in the health care and social services industry moved in opposite directions across the region, likely due to differing demand for workers. Wages in this sector fell 1.4 percent in St. Joseph County but increased 6.3 percent in Elkhart County. Given expected regional growth in

**Figure 1**  
New Housing Index for St. Joseph County



Notes: All housing figures are a seasonally adjusted index with 1986 as the base year. August 2004 is not available.

Source: St. Joseph County Building Department

**Table 1**  
Employment Indices with Unemployment Rates, 2005

	January	February	March	April	May	June	July	August	September	October	November	December
<b>2004</b>												
<b>South Bend</b>												
Total Nonfarm	126.3	126.2	125.6	125.4	125.3	125.5	127.1	126.1	126.4	126.2	126.3	126.8
Manufacturing	76.8	77.3	76.6	76.7	76.7	76.2	76.7	75.8	75.3	75.1	75.4	75.4
Nonmanufacturing	141.2	140.9	140.2	139.6	139.4	139.8	141.4	140.8	141.3	140.9	141.0	141.6
Unemployment Rate	5.0	5.0	4.7	6.7	4.4	4.2	4.9	5.1	4.4	4.4	4.2	4.3
<b>Elkhart-Goshen</b>												
Total Nonfarm	133.7	133.2	132.3	133.3	133.5	133.1	132.9	132.1	133.2	132.8	132.8	132.3
Manufacturing	120.8	121.0	119.7	120.1	119.5	119.6	118.7	117.5	117.3	116.4	117.2	117.6
Nonmanufacturing	148.1	147.3	147.1	148.7	149.6	148.9	149.6	148.6	152.2	151.6	151.6	150.1
Unemployment Rate	4.6	4.7	4.4	5.8	4.4	5.5	4.5	4.5	4.2	4.2	4.1	4.0
<b>2005</b>												
<b>South Bend</b>												
Total Nonfarm	138.9	138.9	138.9	139.4	138.5	138.0	138.6	136.8				
Manufacturing	93.8	93.9	94.5	94.5	92.6	92.8	92.2	91.5				
Nonmanufacturing	152.5	152.5	152.2	152.4	151.8	151.2	151.7	149.9				
Unemployment Rate	5.6	5.9	5.6	5.0	4.5	4.9	5.4	4.9				
<b>Elkhart-Goshen</b>												
Total Nonfarm	144.7	144.9	143.5	143.9	143.1	142.0	143.7	143.7				
Manufacturing	134.2	134.0	132.2	132.0	130.6	128.9	131.1	129.8				
Nonmanufacturing	156.3	157.4	156.9	157.7	157.6	157.3	158.5	159.3				
Unemployment Rate	4.9	5.0	4.7	4.2	3.8	4.4	5.0	4.5				

Notes: All employment figures except for unemployment rates are seasonally adjusted indices with 1986 as the base year. All underlying employment data are derived from a monthly survey of establishments.  
Source: Indiana Department of Workforce Development

“The overall employment decline was largely driven by a gradual drop in manufacturing employment through most of 2005.”

# Terre Haute

manufacturing and nonmanufacturing in 2006, average wages will likely continue to rise over the next year—even more so if national expectations of inflation cause upward pressure on wages.

## Commercial Real Estate

Regional real estate markets have remained strong despite rising interest rates over the past year.<sup>3</sup> Occupancy rates rose for many commercial developments in the region. Significant commercial development will continue in 2006 with new retail and industrial developments throughout the region.

## Housing

Residential construction, measured by a seasonally adjusted index of new single-dwelling housing permits issued in St. Joseph County, remains active (see **Figure 1**). From January 2004 to September 2005, new housing permits increased 8.2 percent. More dramatic is the substantial growth of 49.2 percent in the first nine months of 2005. It remains to be seen if demand for homes will be dampened by expected interest rate hikes in the near future.

In 2005, the Michiana region has experienced mixed economic signals: fairly flat employment, relatively low but fluctuating unemployment rates, rising wages, increased production in certain sectors, and active real estate markets. The outlook for the coming year is optimistic, with the region expanding production in some manufacturing and nonmanufacturing sectors, growth in retail, higher employment, continued growth in wages, and considerable real estate activity. ■

## Notes

1. Linda Lipp, "Indiana's RV, housing manufacturers prepare to aid Katrina's victims," *Indiana Economic Digest* 5 September 2005.
2. [www.stats.indiana.edu/cew/simple\\_cew\\_naics.asp](http://www.stats.indiana.edu/cew/simple_cew_naics.asp).
3. CB Richard Ellis, *2004 Real Estate Market Study: Northcentral Indiana and Southwestern Michigan* Summer 2005.

## Robert Guell

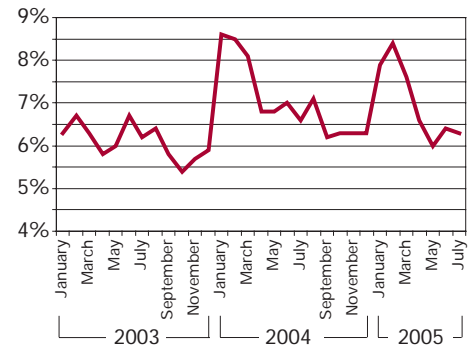
Associate Professor of Economics and Coordinator of First-Year Programs, Indiana State University, Terre Haute

**A**fter decades of steady decline, the Terre Haute economic horizon has noticeable signs of economic progress but a few lingering clouds. The demolition of the city's iconic Terre Haute House, a retail construction boom, and a significant expansion at Aisin Brake suggest a new economic vitality to the city. Still, the uncertain future of Sony's Blu-ray technology for the high definition home movie market, the uncertain future of Pfizer's yet-to-be approved inhaled insulin, and the almost certain total closure of Columbia House prevent unbridled enthusiasm.

As 2005 opened, Mayor Kevin Burke announced the city had secured an option on the Terre Haute House. The hotel, closed since the early 1970s, was an icon for many. Those who loved its Mayflower Room considered it a potential cornerstone to a revitalized downtown, while others viewed it as a symbol of the city's inability to move forward. By April, several plans had been submitted but none were judged by the city to have sufficient financial backing to succeed. By fall, the Hulman family sold the building to Terre Haute's Greg Gibson for \$1 and demolition began shortly thereafter. Amid demolition came the November announcement of plans for a new "Hilton Garden Inn—Terre Haute House" to open in the summer of 2007.

Also in 2005, retail construction began a boom not seen in the city for decades. South of the existing Wal-Mart Supercenter, construction began on a retail complex that will ultimately include a Kohl's, a TJ Maxx, and several small stores and restaurants. Meanwhile, construction of a new Wal-Mart Supercenter on the east side of the city (near the I-70–Indiana 46 interchange) promises to bring a significant

**Figure 1**  
Terre Haute Unemployment Rate



Note: Data are not seasonally adjusted.  
Source: Bureau of Labor Statistics

expansion of retail activity. Several other smaller construction endeavors also significantly upgraded the retail options in the city.

It is not entirely clear that there will be good-paying jobs to support these new retail ventures. Though Aisin Brake announced a significant planned expansion of its workforce during the year, the BMG purchase of Columbia House makes it all but certain that one of the city's former employment mainstays will ultimately abandon its Terre Haute northeast location. As shown in **Figure 1**, the city's unemployment rate jumped markedly in early 2004 and 2005 with Columbia House job-cut announcements. Each time it has returned near its previous levels.

In 2006, two decisions—one made by the Food and Drug Administration (FDA) and one made by movie studios and consumers worldwide—will provide significant clarity for Terre Haute's economic future. The FDA stands ready to approve Pfizer's inhaled insulin. Terre Haute's southside Pfizer plant would likely manufacture much of these delivery systems, adding significant jobs in the process. On the other end of the city, Terre Haute's northside Sony plant stands ready to produce a significant portion of the high definition movies that will be sold throughout the world. The uncertainty here is that Sony's Blu-ray technology is incompatible with Toshiba's HD DVD and a BetaMax vs. VHS type war is likely in the offing. If Blu-ray wins, so will Terre Haute. ■

## Mark Your Calendar

### **The Health Care Conundrum: A Call for Leadership**

*Registration: February 21, 2006*

*Date: March 8, 2006*

The Kelley School of Business at Indiana University will host its 60th annual business conference to begin the development of a coalition between health care industries. Participants will hear keynote speakers from Eli Lilly, Wellpoint, Deloitte Center for Health Solutions, Humana, Clarian, and Maytag give insight into what their companies could do to aid in solving the problem.

[www.kelley.iu.edu/alumni/60thAnnual/index.html](http://www.kelley.iu.edu/alumni/60thAnnual/index.html)

### **Women in Leadership**

*Registration: March 26, 2006*

*Date: April 23-28, 2006*

The Kelley Executive Partners at the Indiana University Kelley School of Business have developed a program that provides an opportunity for high-performing women to learn tangible and intangible skills to further their careers. Participants will learn in an environment that allows them to practice communication and leadership techniques to enhance their supervisory performance while networking with similarly minded women from across the country, and much more. For more information, visit

[www.kelley.iu.edu/kep/pdf/womensbro.pdf](http://www.kelley.iu.edu/kep/pdf/womensbro.pdf)

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