

Arizona Economic Review and Outlook

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ARIZONA[®]
TUCSON ARIZONA

Overview

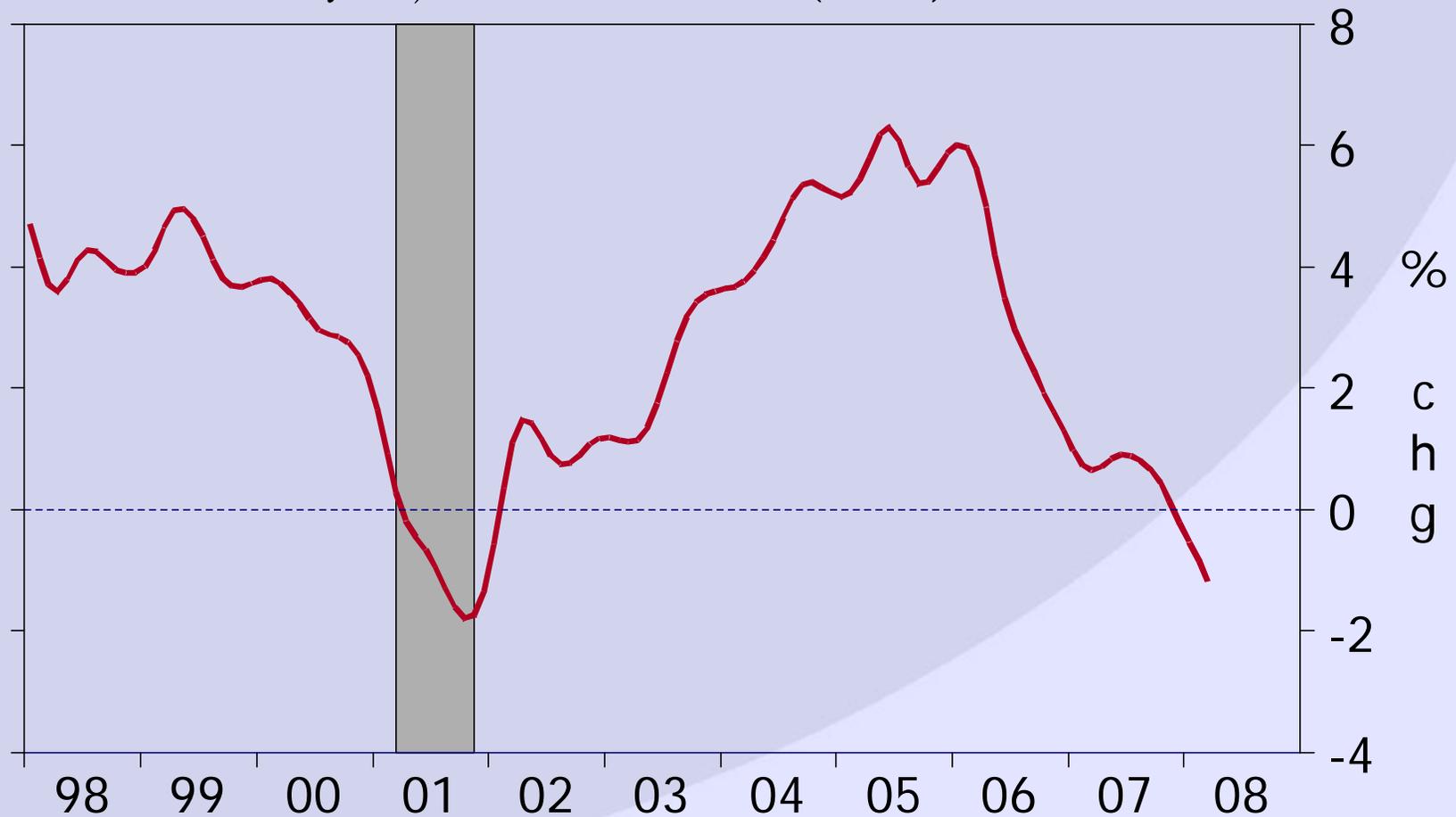
- AZ is one of nine states in recession
- Most indicators are plunging
 - Labor market is deteriorating
 - Housing is in the most severe downturn since WW-II
 - Wages and incomes are stagnant
 - The consumer spending spree is over
- Look for recovery in second half '09

Labor Markets

- Revisions reduced 2007 employment by 53,600, the largest ever (25 years history)
 - Y/Y growth now 1.2% versus 2.9%
- Employment is declining modestly but overstated
 - Birth/death model is providing growth
 - Large jump in state education in PHX

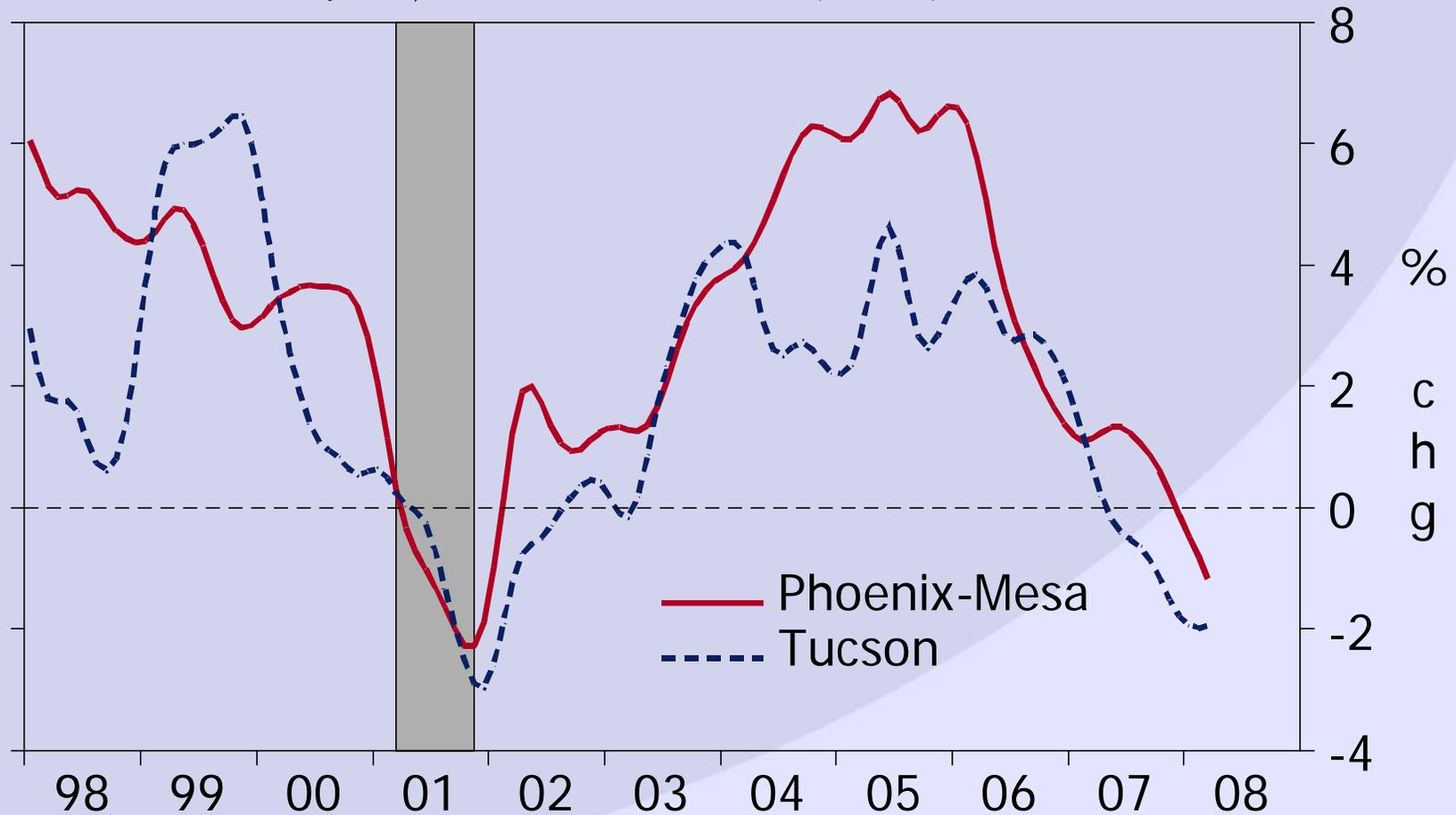
Nonfarm Job Growth, AZ

seasonally adjusted annual rate (m/m), smoothed



Nonfarm Job Growth

seasonally adjusted annual rate (m/m), smoothed



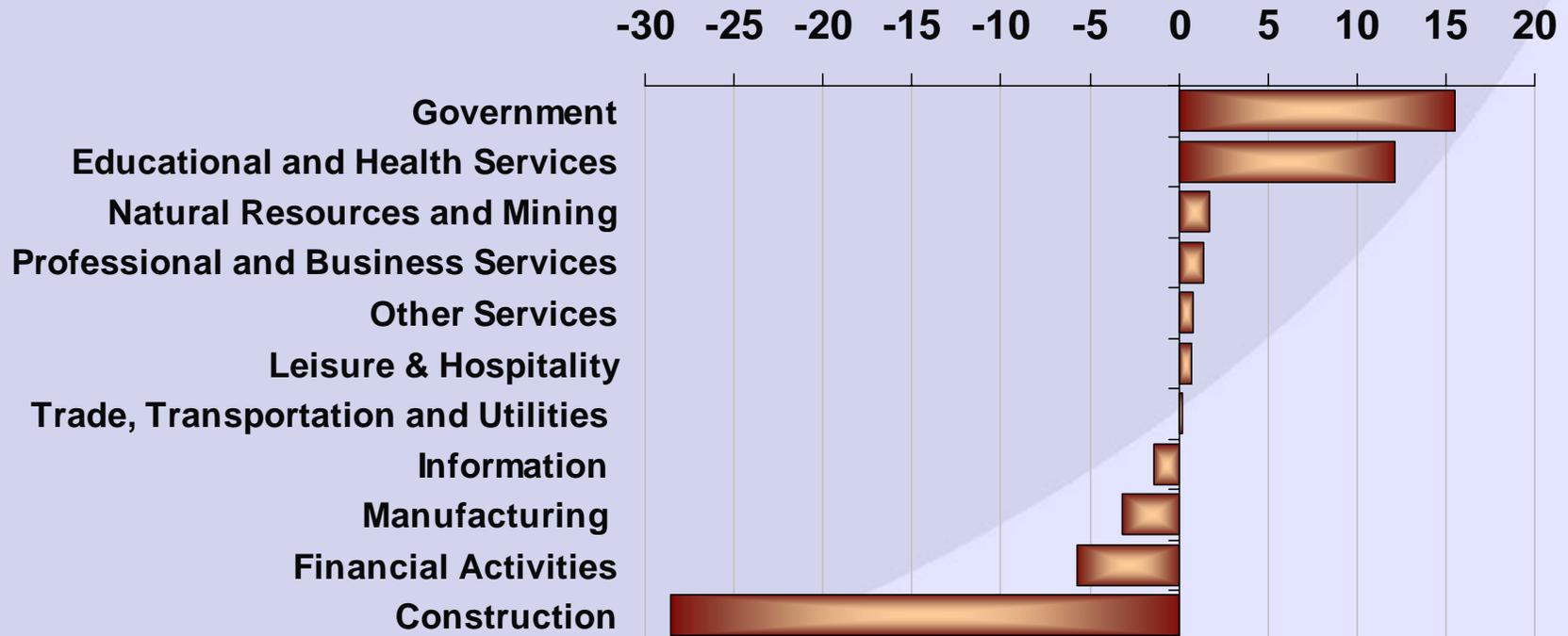
Employment Trends Over Past Year

- Declining
 - Construction
 - Financial activities
 - Manufacturing
 - Information
- Increasing
 - Government
 - Educational & health services
- Flat
 - All other sectors

Changes in Employment, AZ

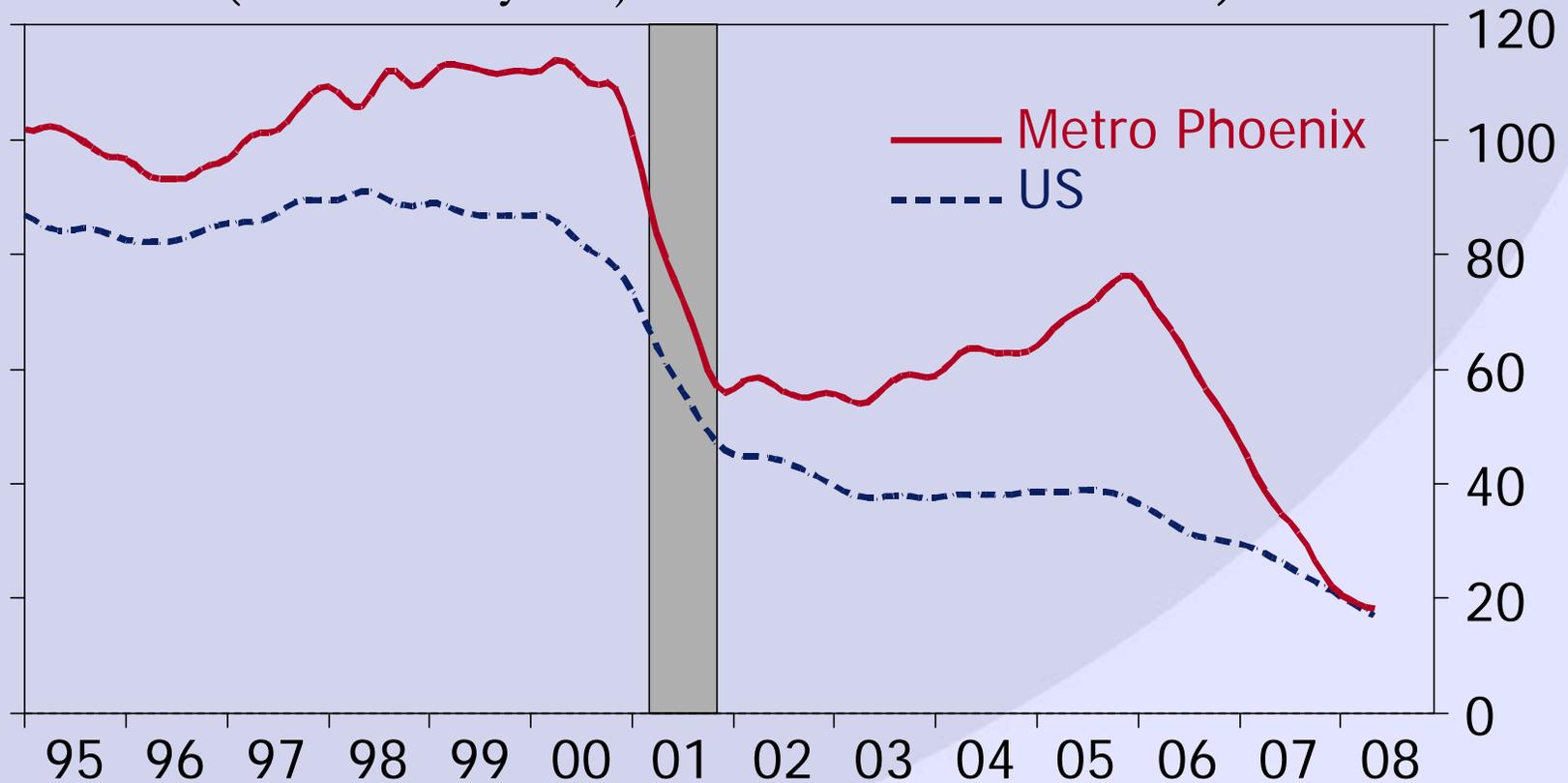
May '08 vs. May '07

000s



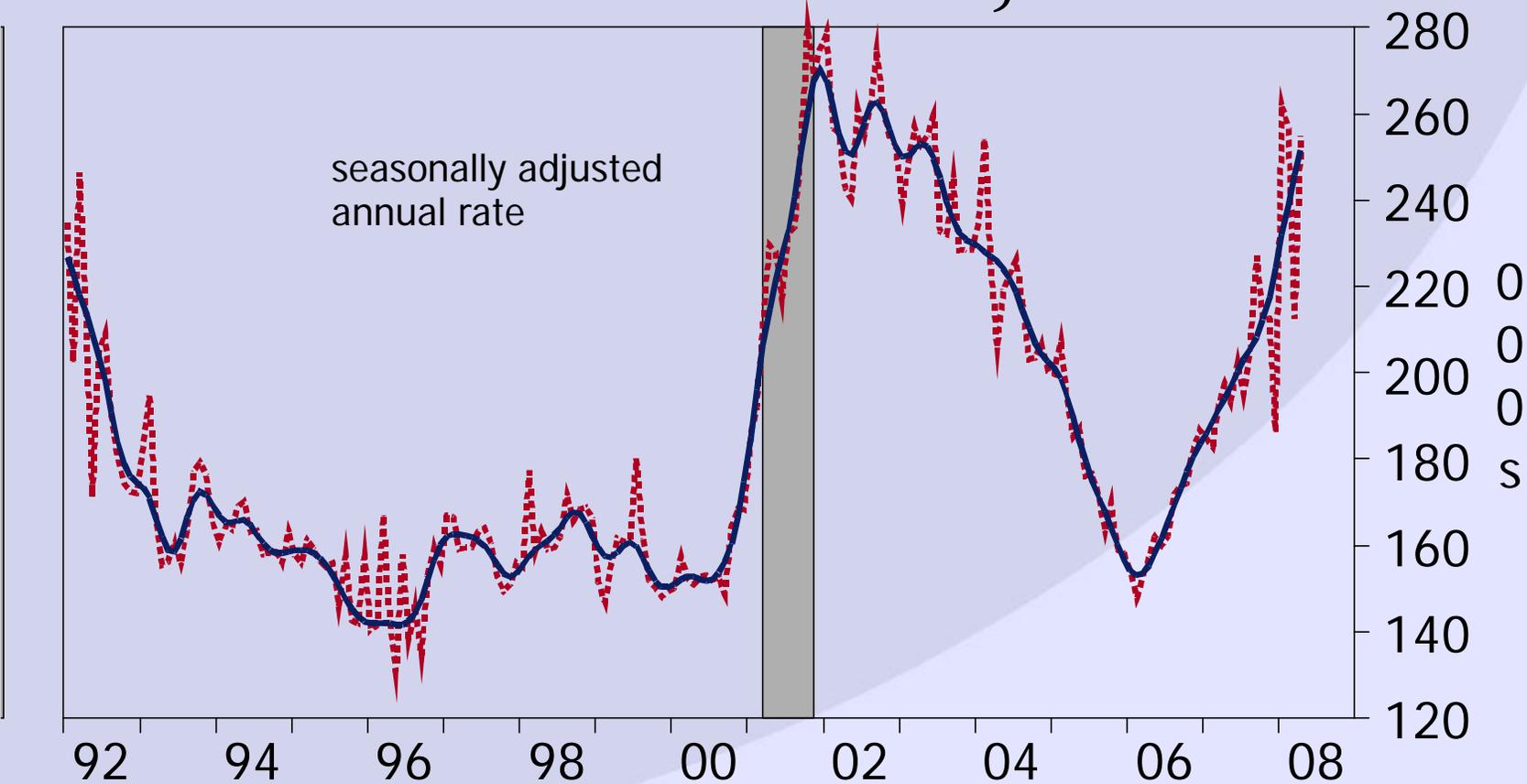
Help Wanted Index

(seasonally adjusted and smoothed)

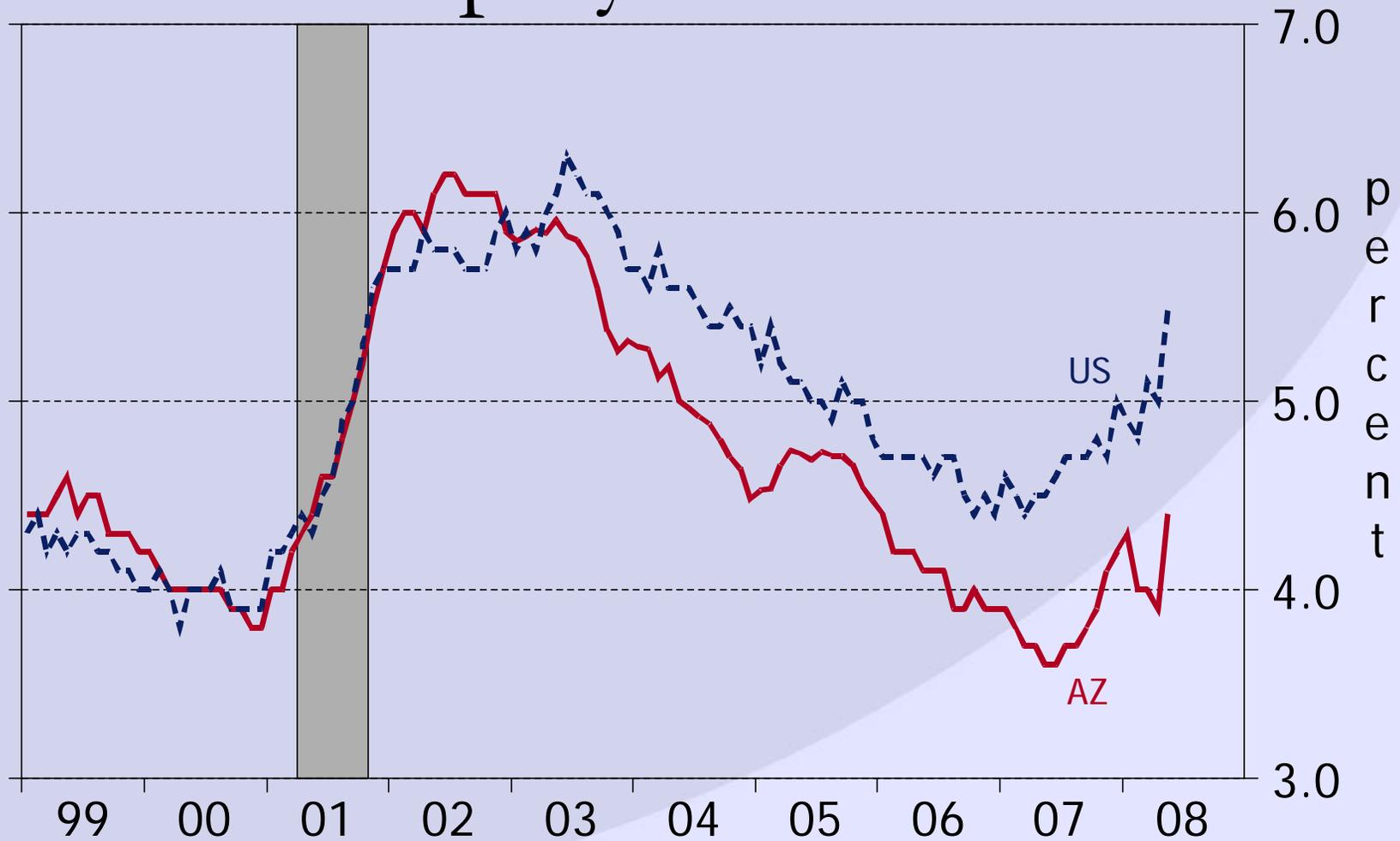


Source: Conference Board

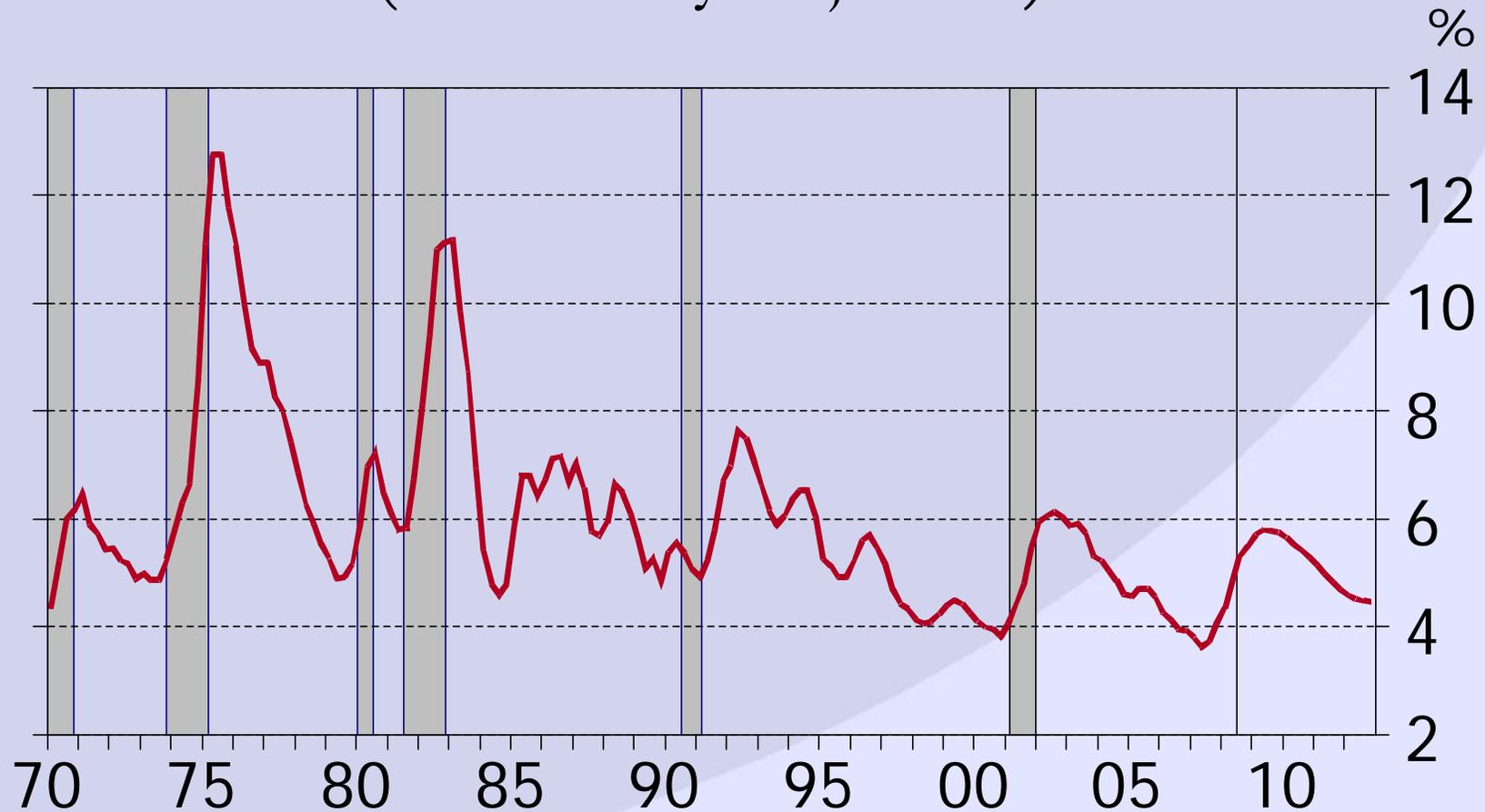
Initial Unemployment Insurance Claims, AZ



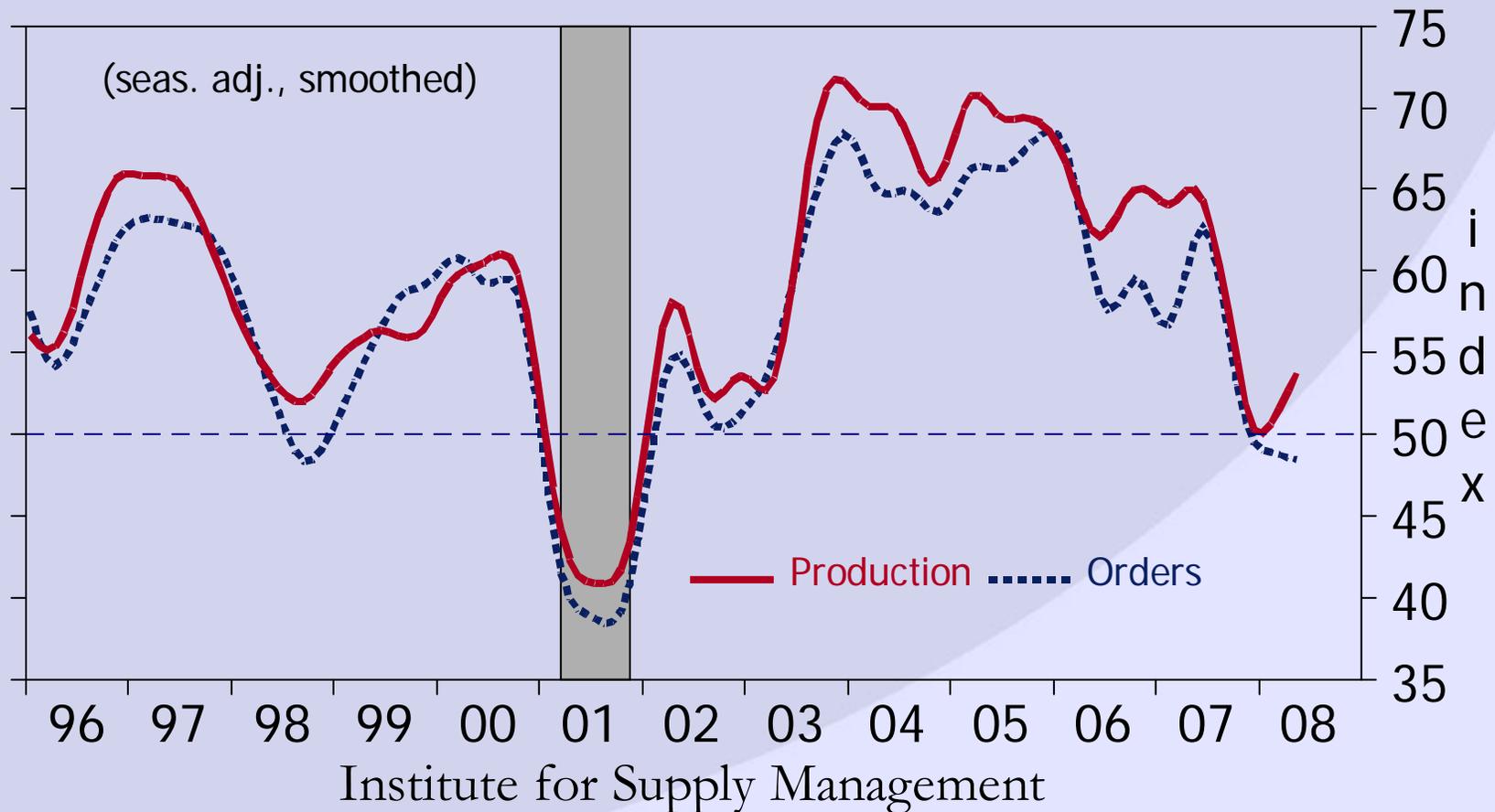
Unemployment Rate



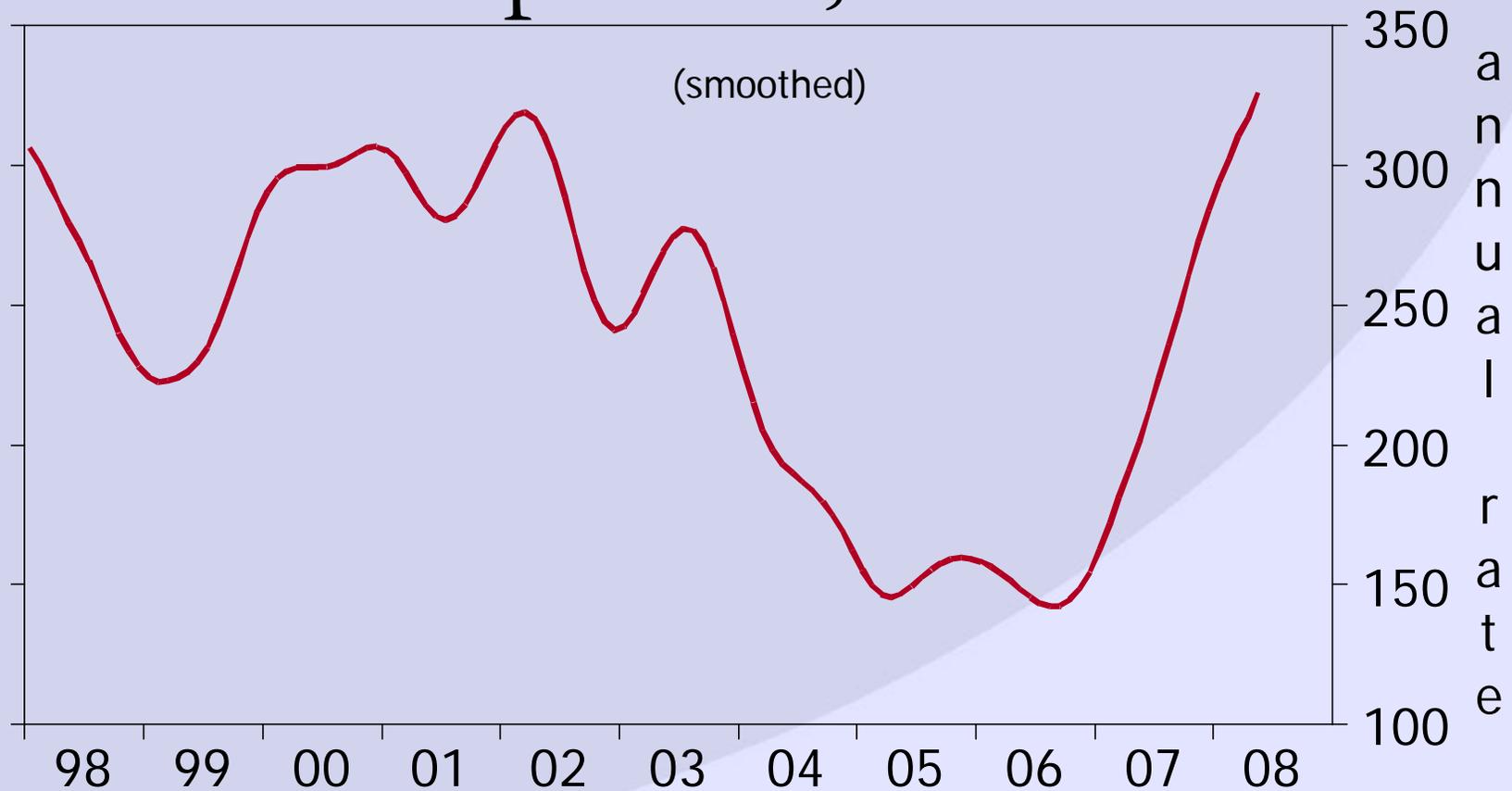
Unemployment Rate, AZ (seasonally adjusted)



Purchasing Management Survey Arizona



Business Reorganizations Chapter 11, AZ





Us

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See what your peers think.

Q2 2008 results are available

[See the latest survey](#)

Welcome to the Business Leaders Confidence Index® (BLCI) for Arizona. The BLCI is a snapshot of what your colleagues and your competition are expecting in the next quarter.

Q2 2008 Arizona BLCI **36.9**

Index above 50 indicates expansion. **Red** - Decrease from previous quarter. **Green** - Increase from previous quarter.

Arizona's BLCI Falls to New Low

The Arizona Business Leaders Confidence Index® (BLCI) declined by 3.5 points, to a reading of 36.9. That's the lowest reading yet for our survey that began in mid-2002. A number

JOIN THE SURVEY

The next survey opens on **June 1**. If you are an Arizona business owner or manager and would like to serve as a BLCI panelist, please **register as a new panelist**.

According to business leaders in Arizona, the top issues facing the state in 2007 are:

- Immigration/border
- Water supply, management, conservation
- Growth management
- Education
- Real estate/housing slowdown/glut
- Infrastructure/roads/traffic

Business Leader Confidence Index Arizona

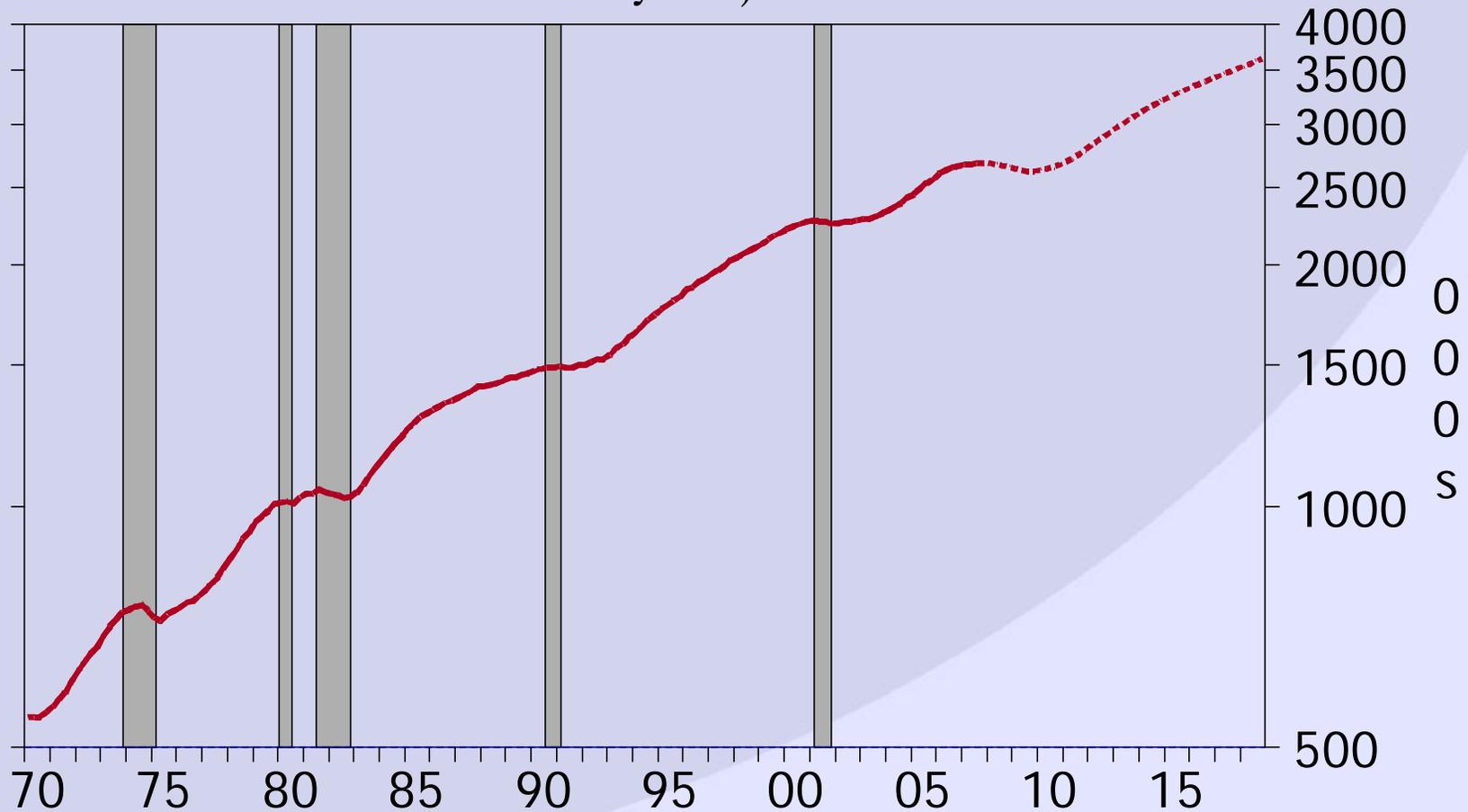


Outlook for Employment

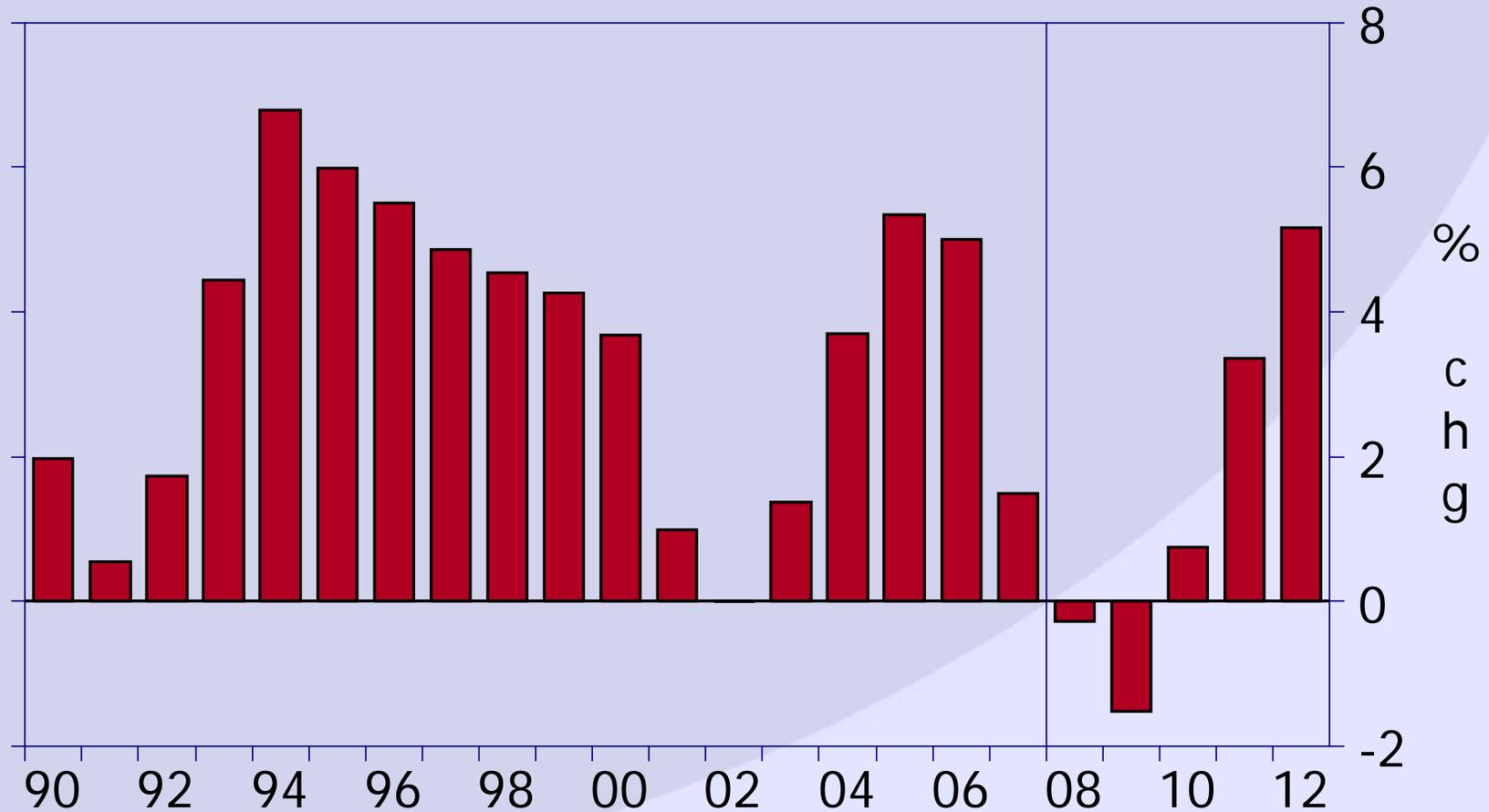
- Nonfarm employment peaked in August 2007
- Bottom in 3Q 2009
 - 65,000 job loss, 2.4% peak-to-trough
 - 4.7% decline in 1974-75
 - 2.4% 1981-82
 - 0.6% 1990-91
 - 1.4% 2001

Nonfarm Employment, AZ

seasonally adjusted

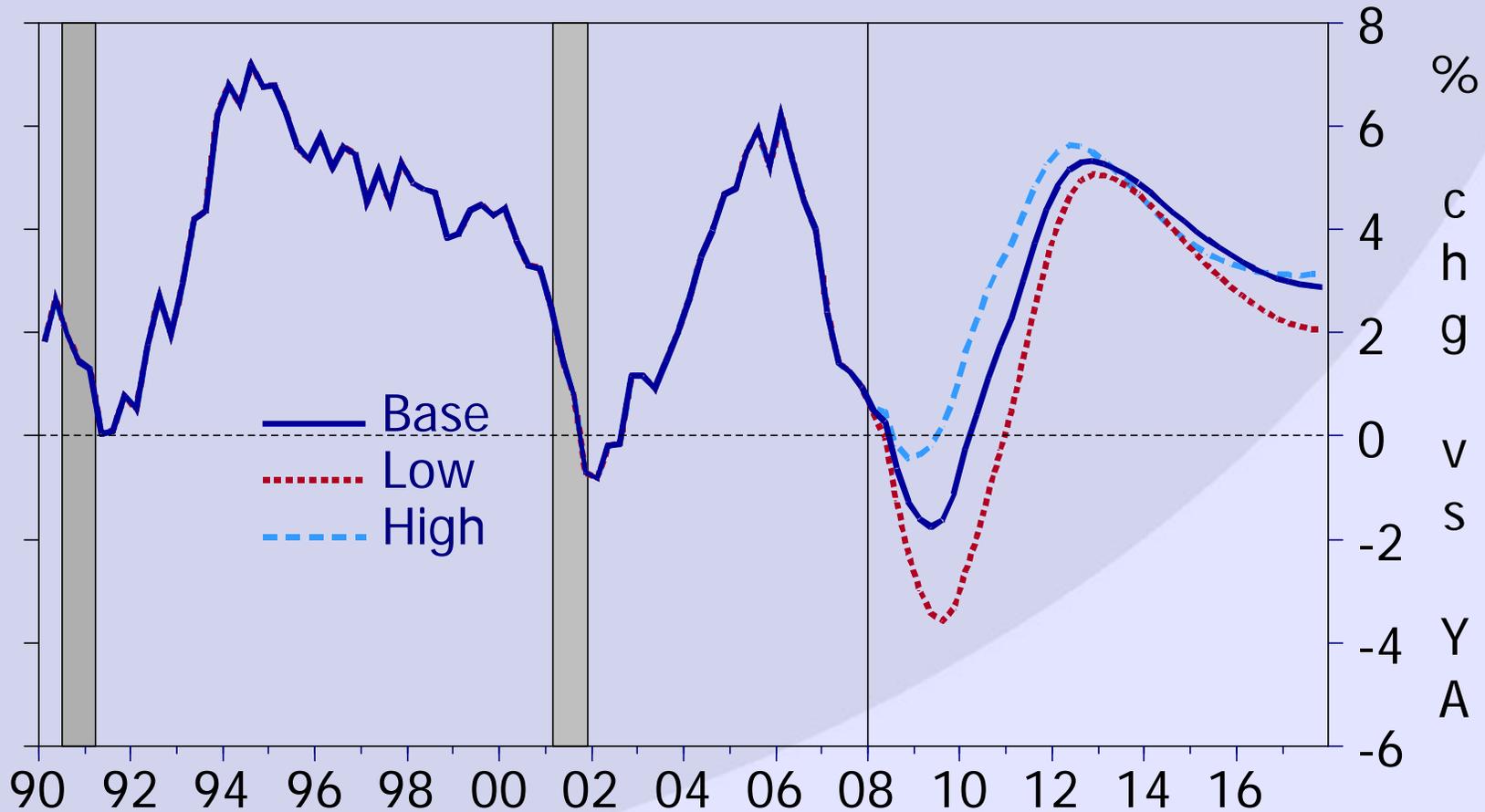


Nonfarm Job Growth Arizona



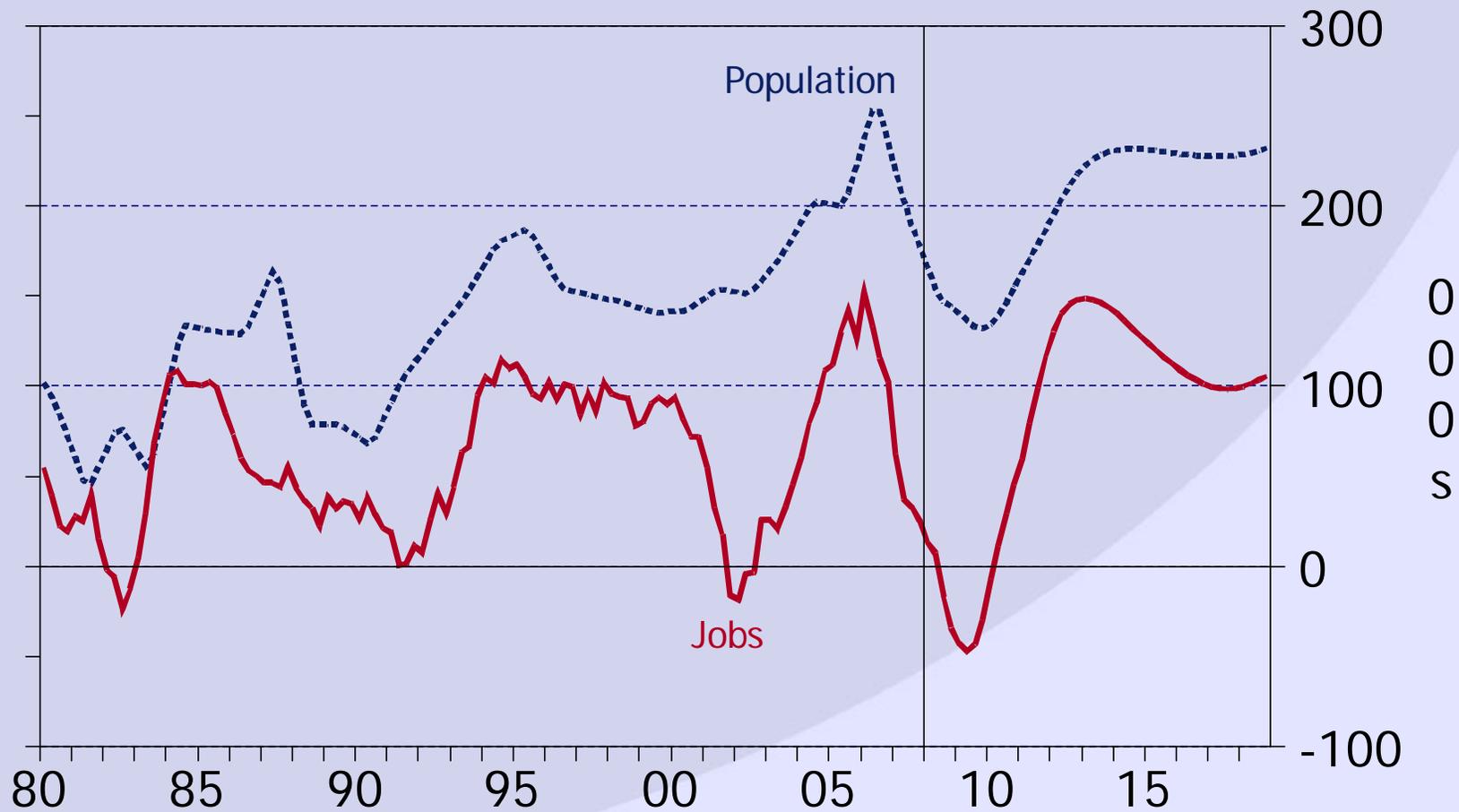
Nonfarm Employment, AZ

Alternative Scenarios



Annual Change in Pop & Jobs

Arizona



Residential Electric Customers

TEP, SRP, and APS Metro Service Areas

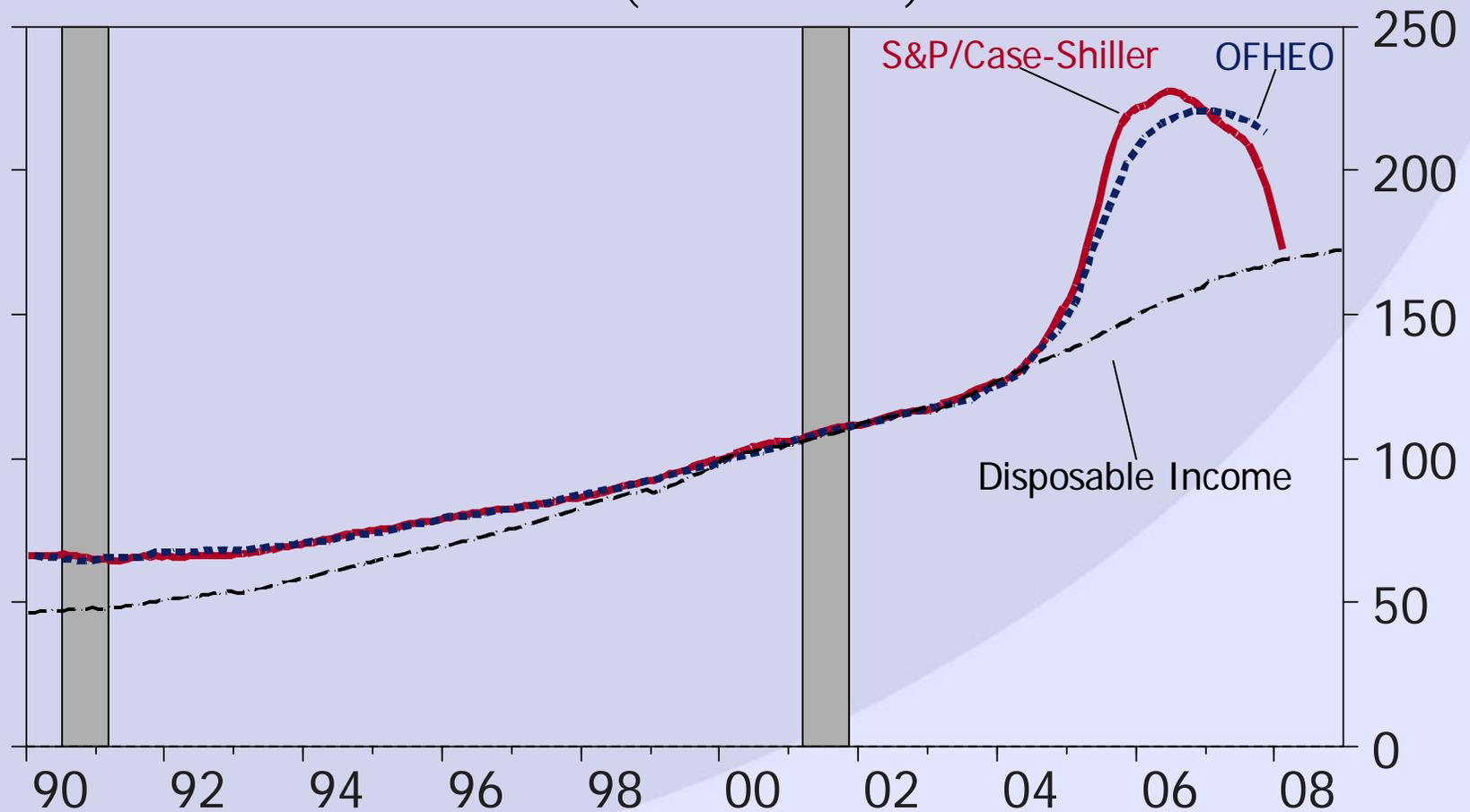


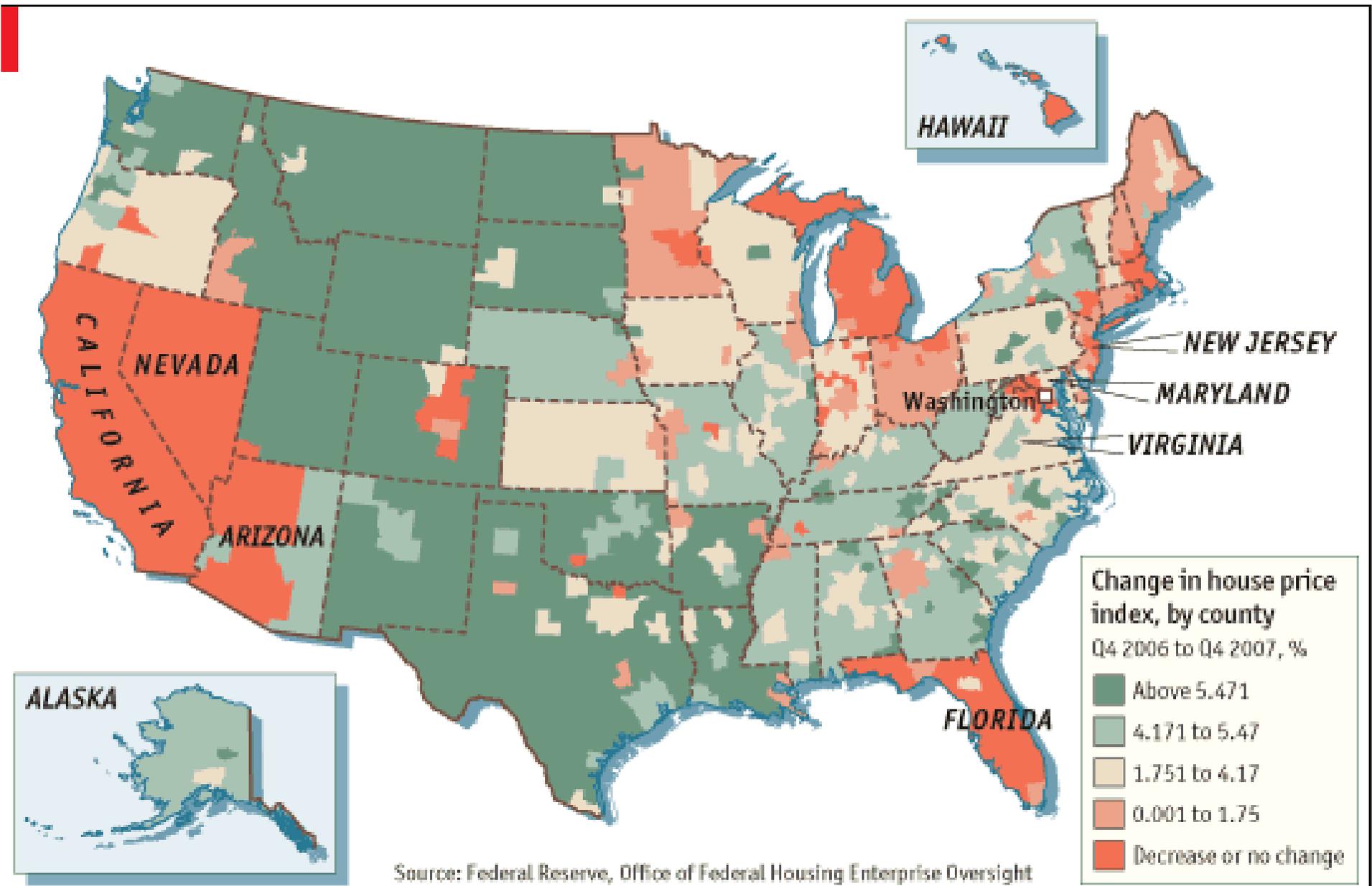
Housing

- In the most severe downturn since WW-II
- AZ one of the hardest hit states
- How much have housing prices declined?
 - MLS – down 19.2% since Sept '05 (thru March)
 - OFHEO – down 6.7% since 4Q '06 (1Q '08)
 - SPCS – down 29.1%, June '06 thru Apr. '08
- Good news: affordability is improving!
- Bad news: inventories still high

Home Prices, Metro Phoenix

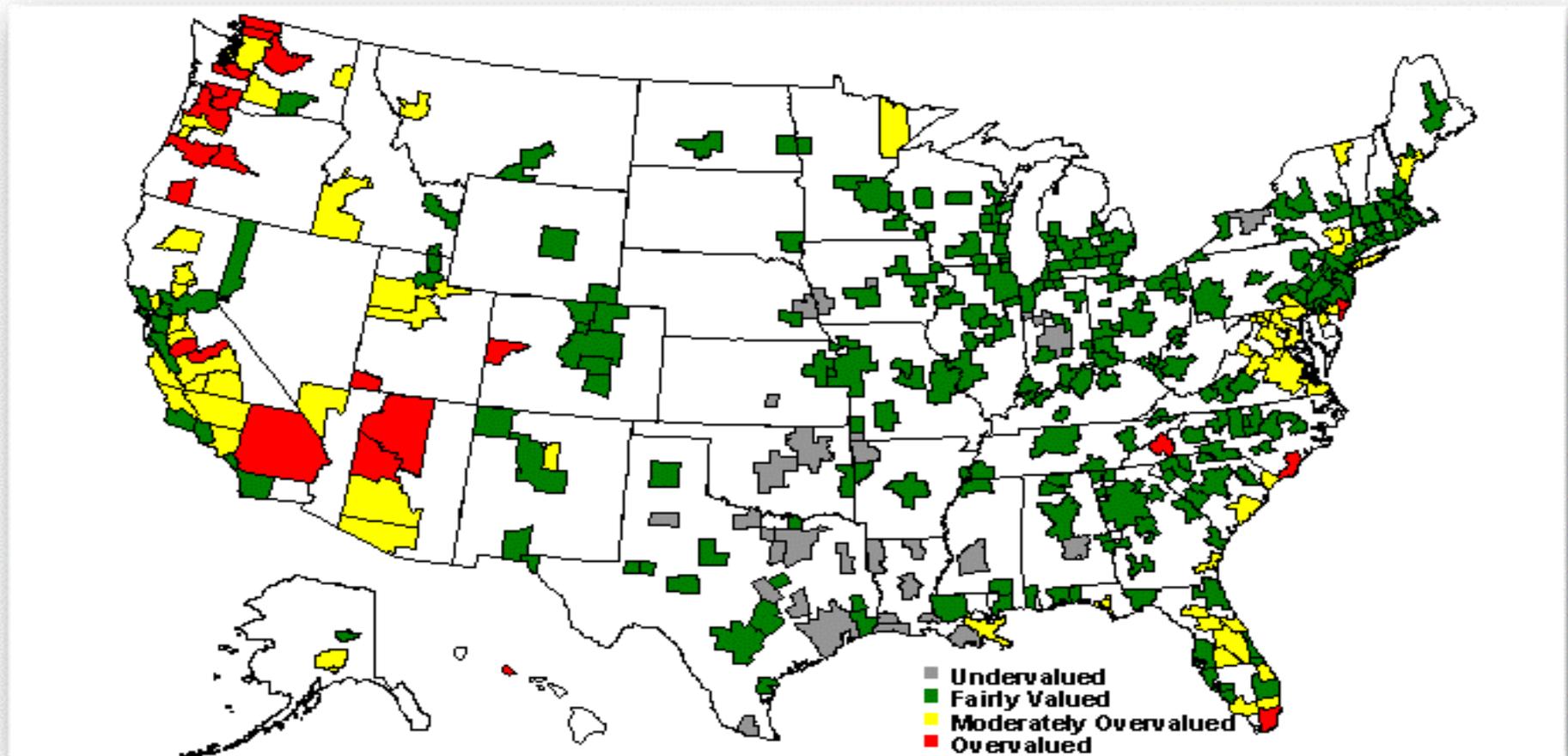
Index (2000=100)





House Prices: Overvaluations Becoming Less Extreme

Global Insight estimates, 2007 Q4

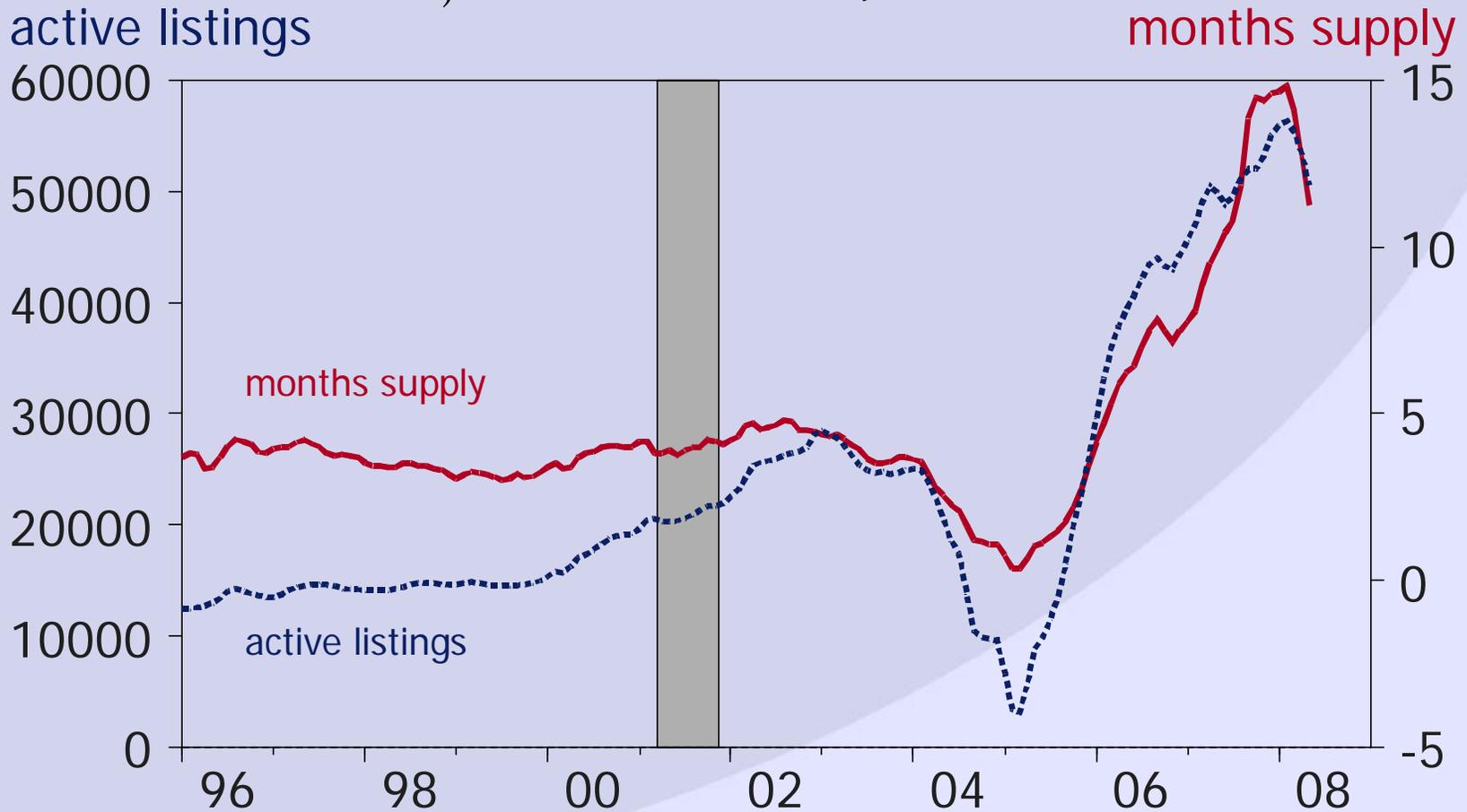


Housing

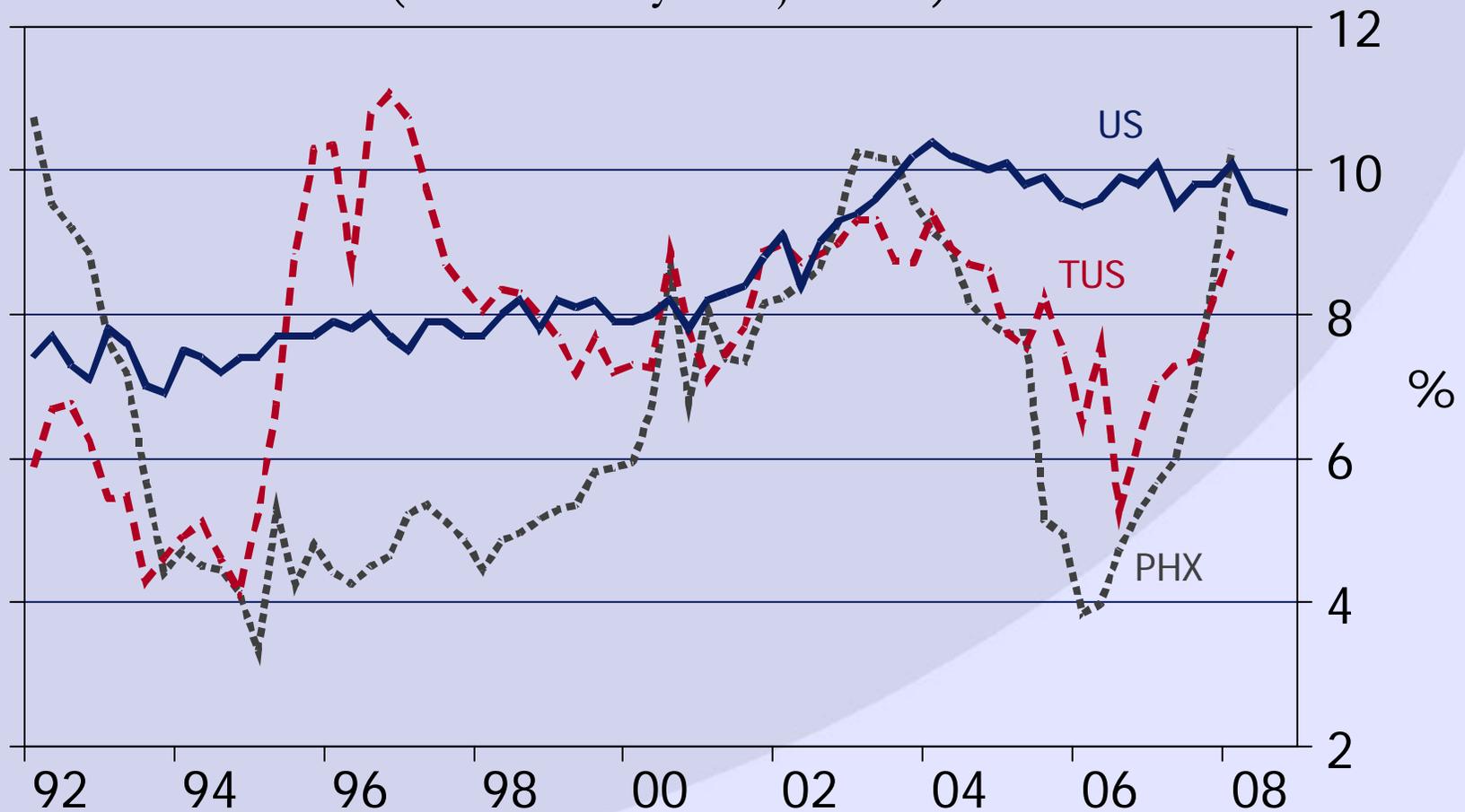
- Inventories very high but declining
- Foreclosure rate in Apr. '08
 - AZ ranks 3th, 11,557 properties, up 119%
 - CA ranks 2nd, 71,930 properties, up 81%
 - Source: RealtyTrac
- Apartment vacancy rates moving up
- Home sales and permits beginning to stabilize?

Housing For Sale Inventory, MLS

seas adj and smoothed, Metro Phoenix

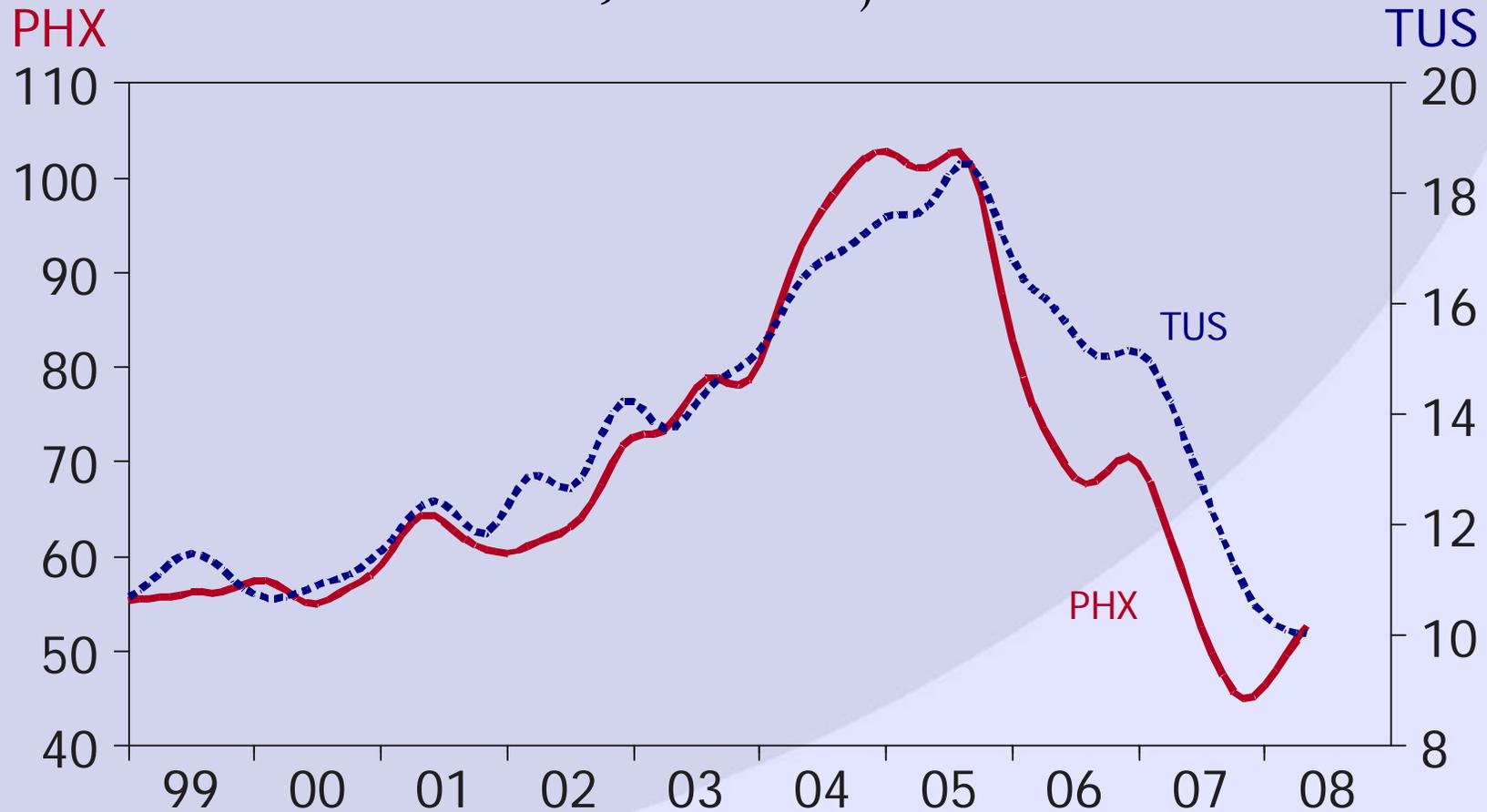


Apartment Vacancy Rates (Seasonally Adjusted)



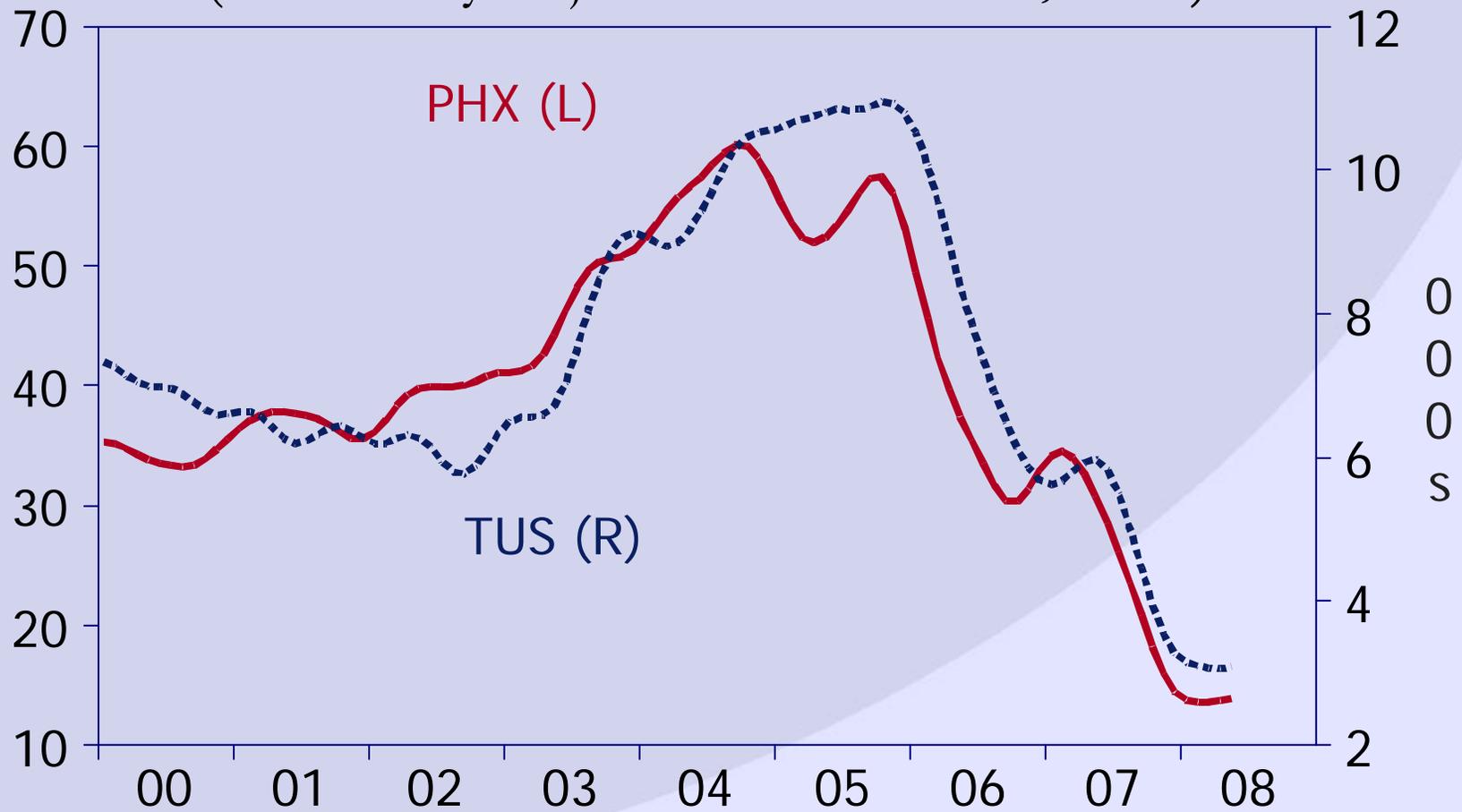
Existing Home Sales, MLS

000s units, seas adj annual rate



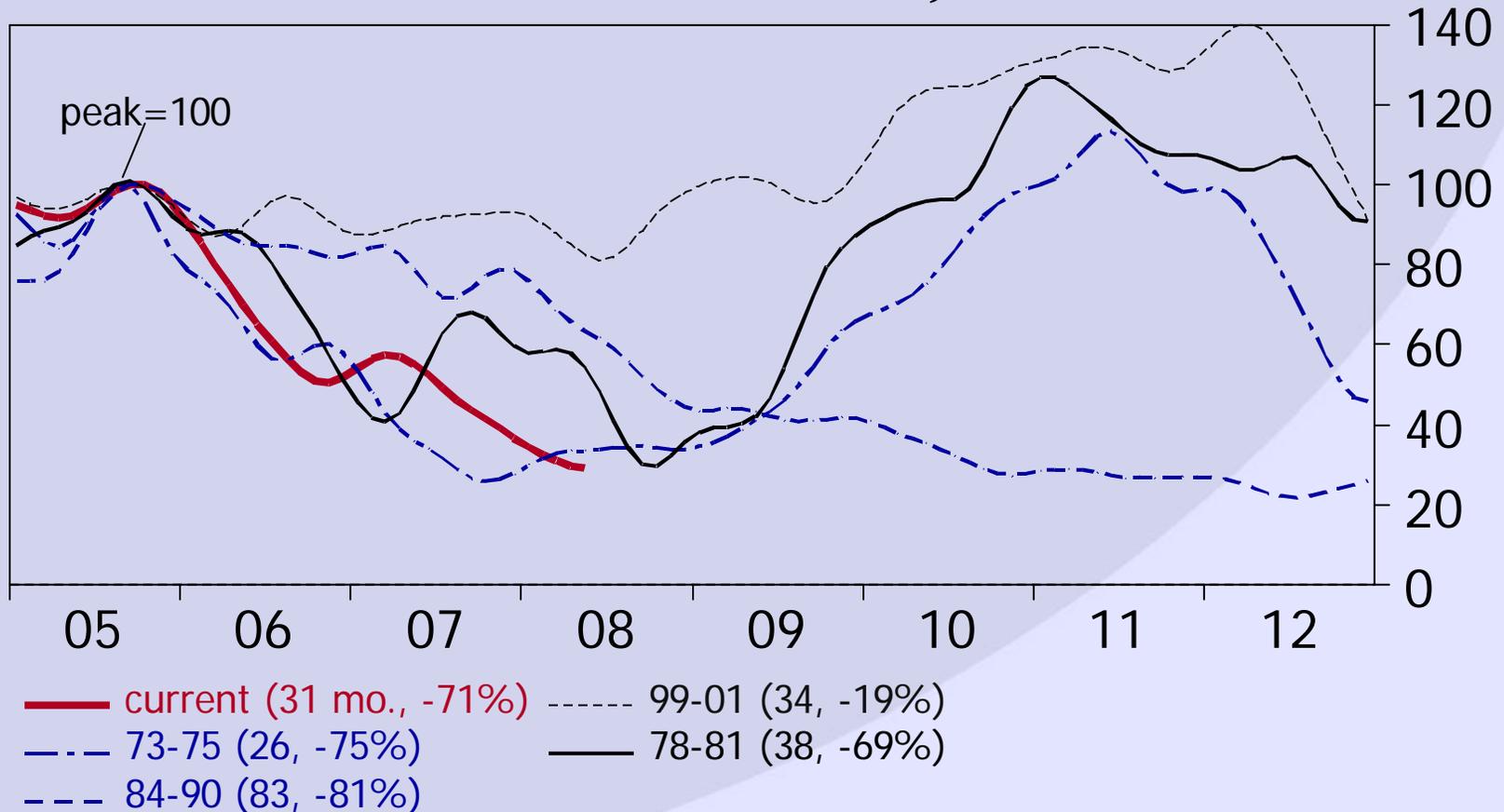
Single Family Building Permits

(seasonally adjusted annual rate, 000s)



Housing Recessions Compared

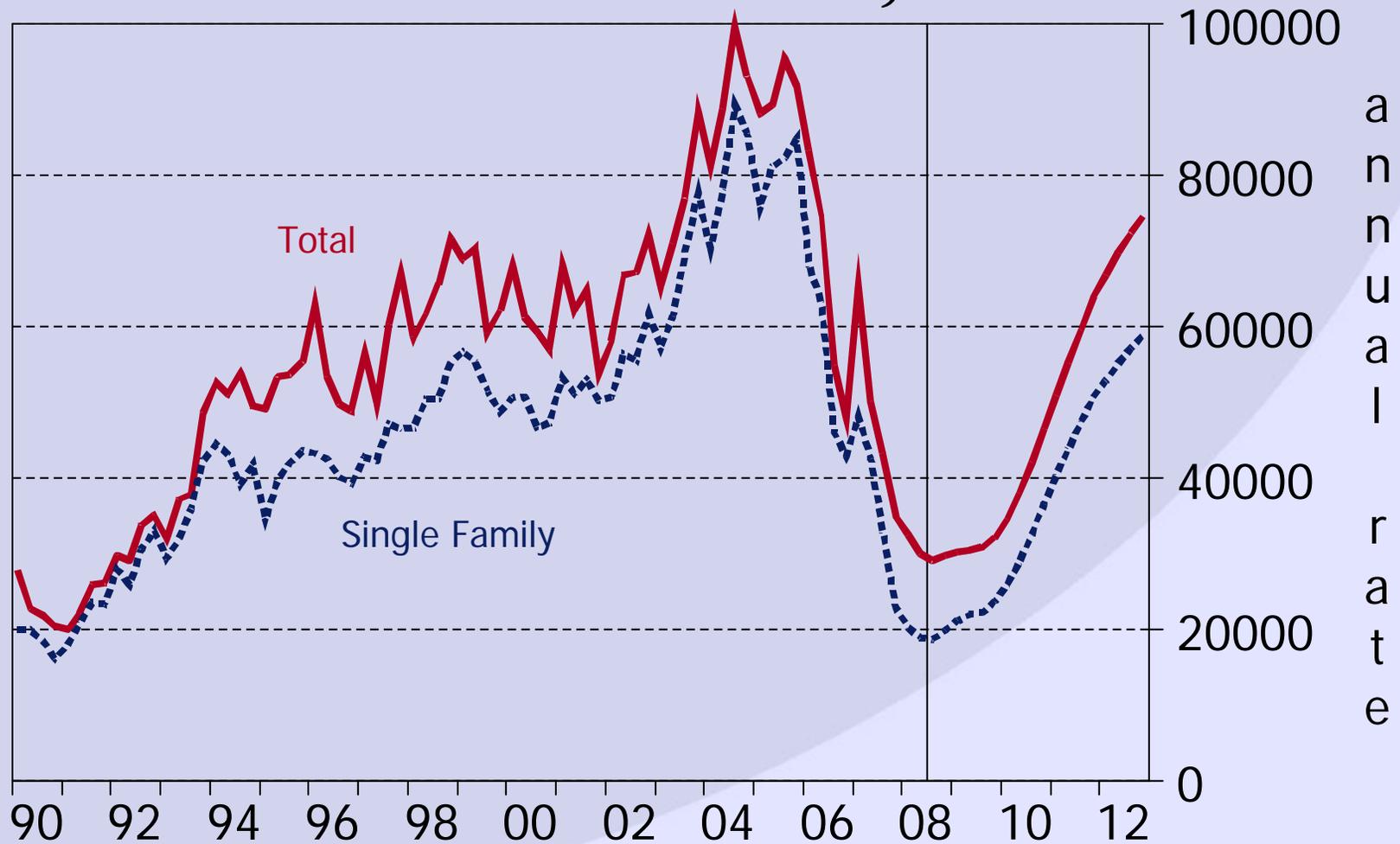
Residential Permits, AZ



Housing Outlook

- Continued weakness
 - Sales stabilize in late 2008 and move up modestly in 2009
 - Starts move up in early 2009
 - Housing prices stabilize in 2010

Residential Permits, AZ

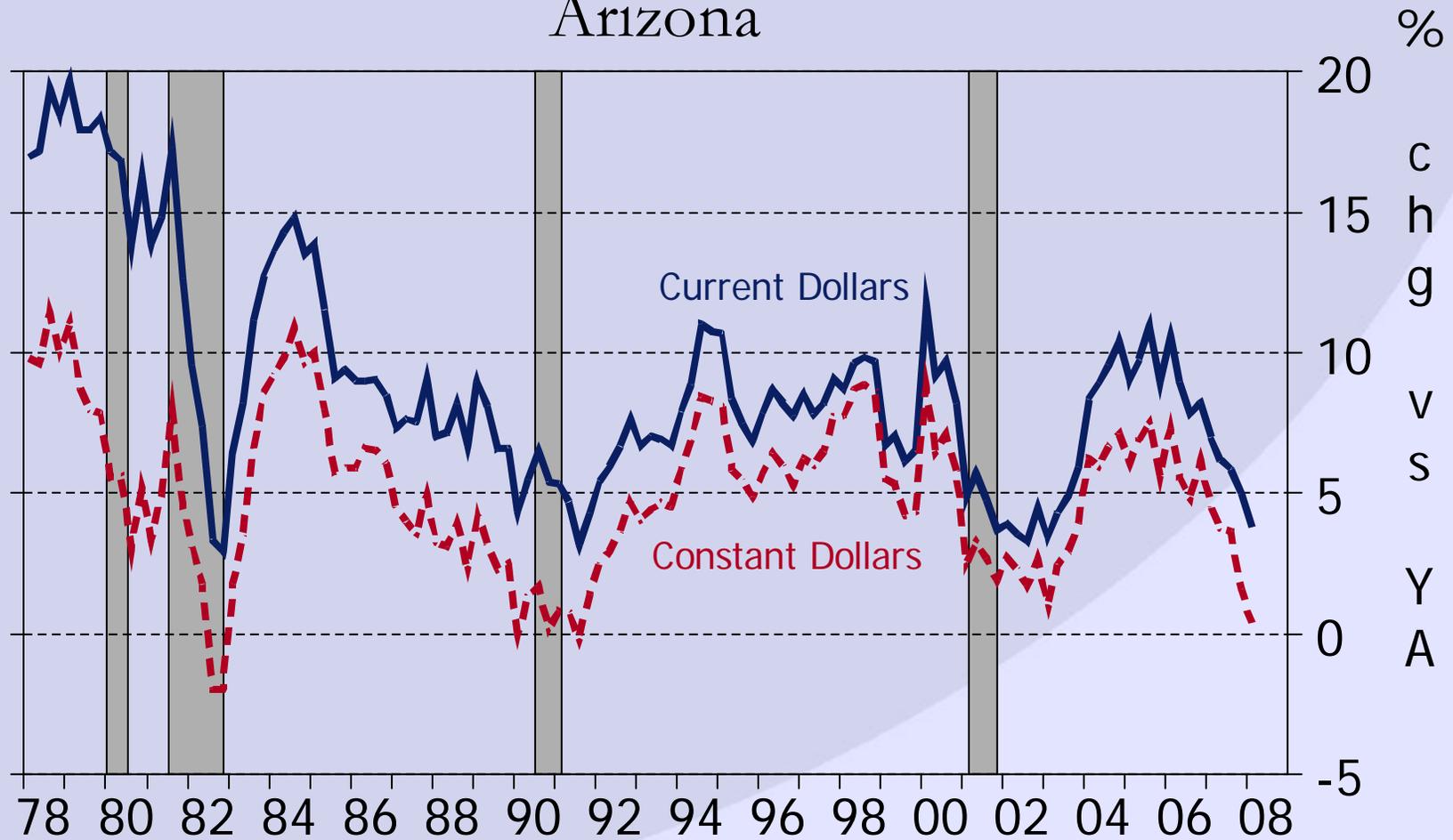


Income and Wages

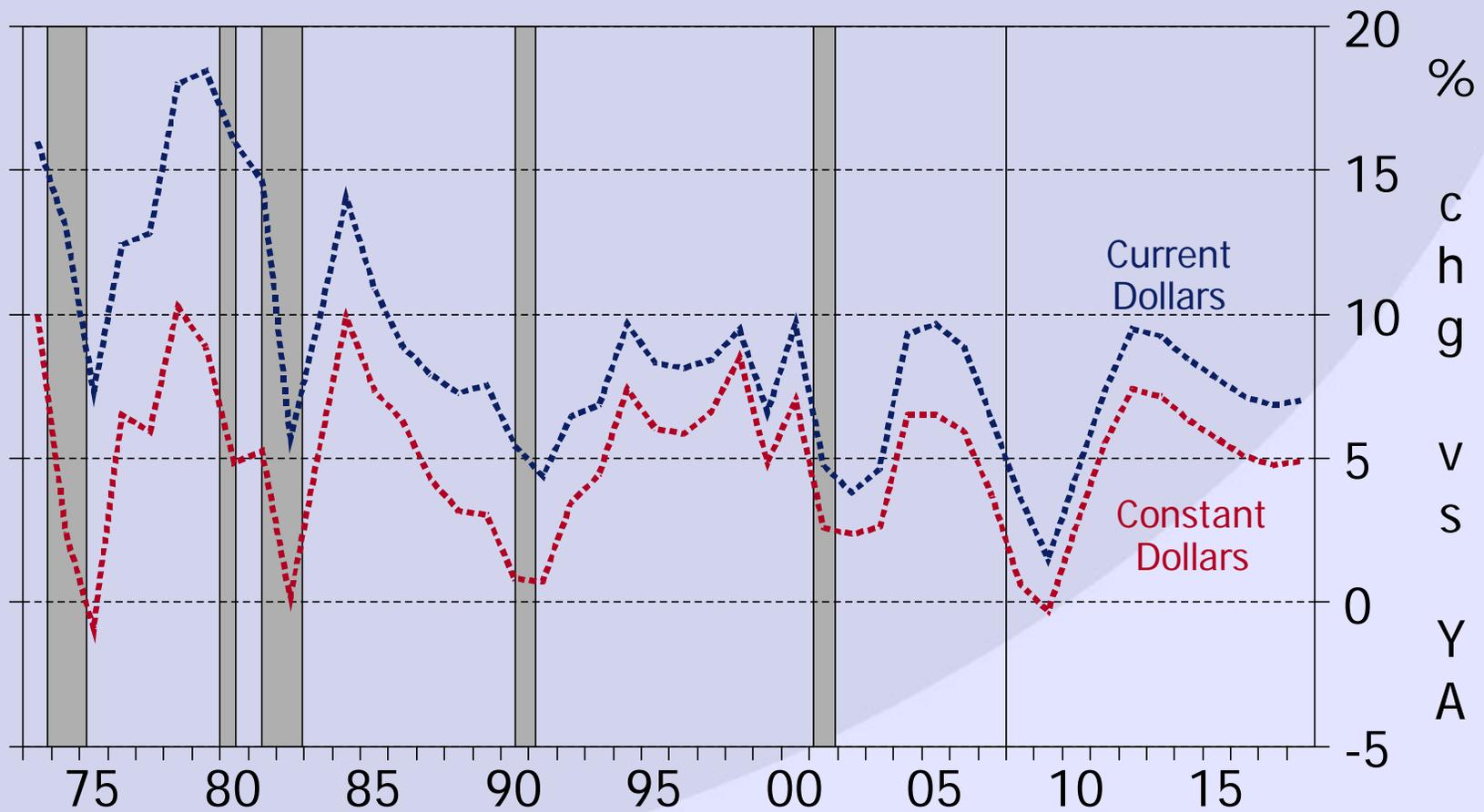
- Personal income grew 3.8% Y/Y in '08Q1
 - forecast to grow by 3.6% this year, 1.5% next
- Spending will grow more slowly than income
- Wage growth will slow to 2.5 – 3.0%

Personal Income Growth

Arizona

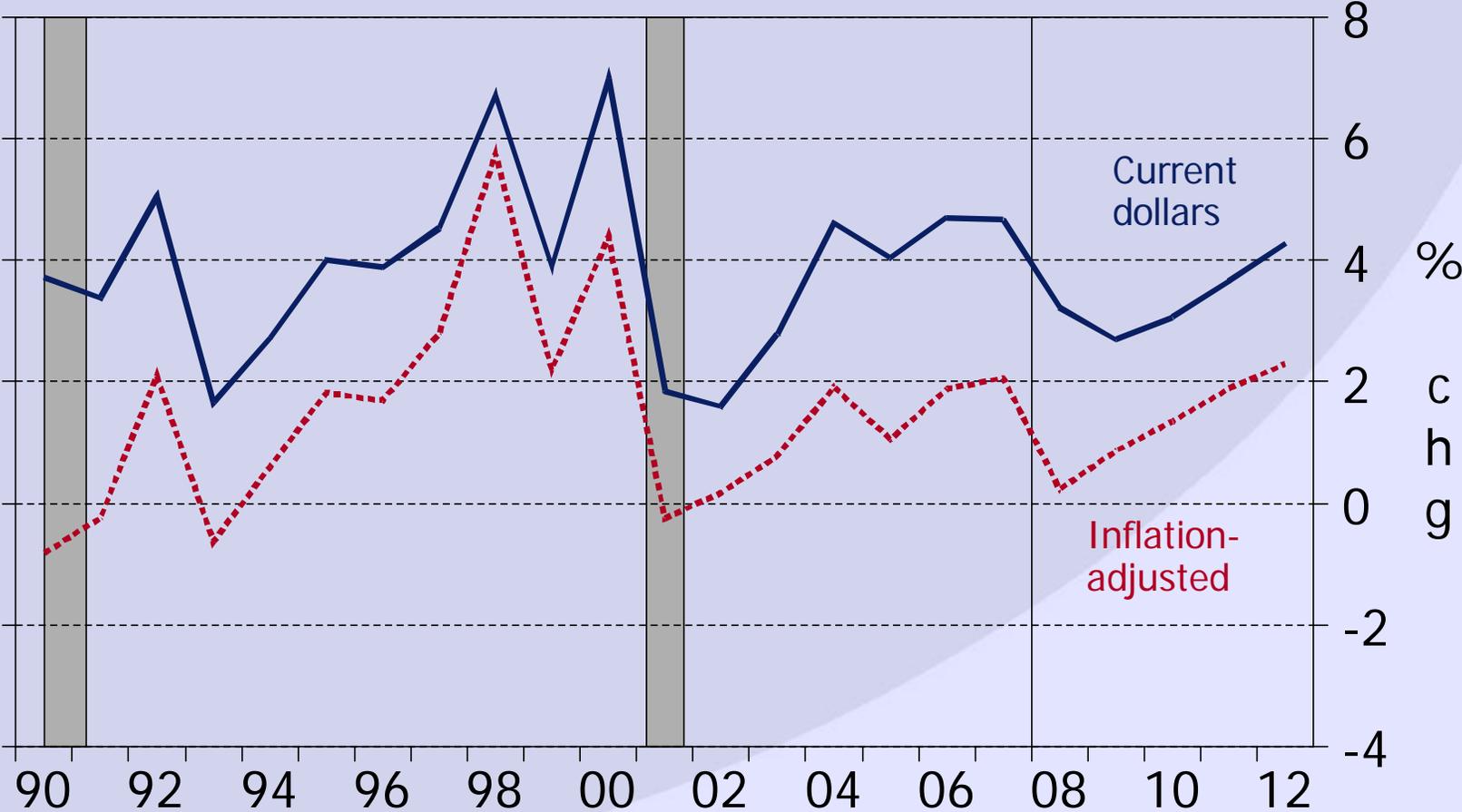


Personal Income Growth Arizona



Average Wages Per Employee

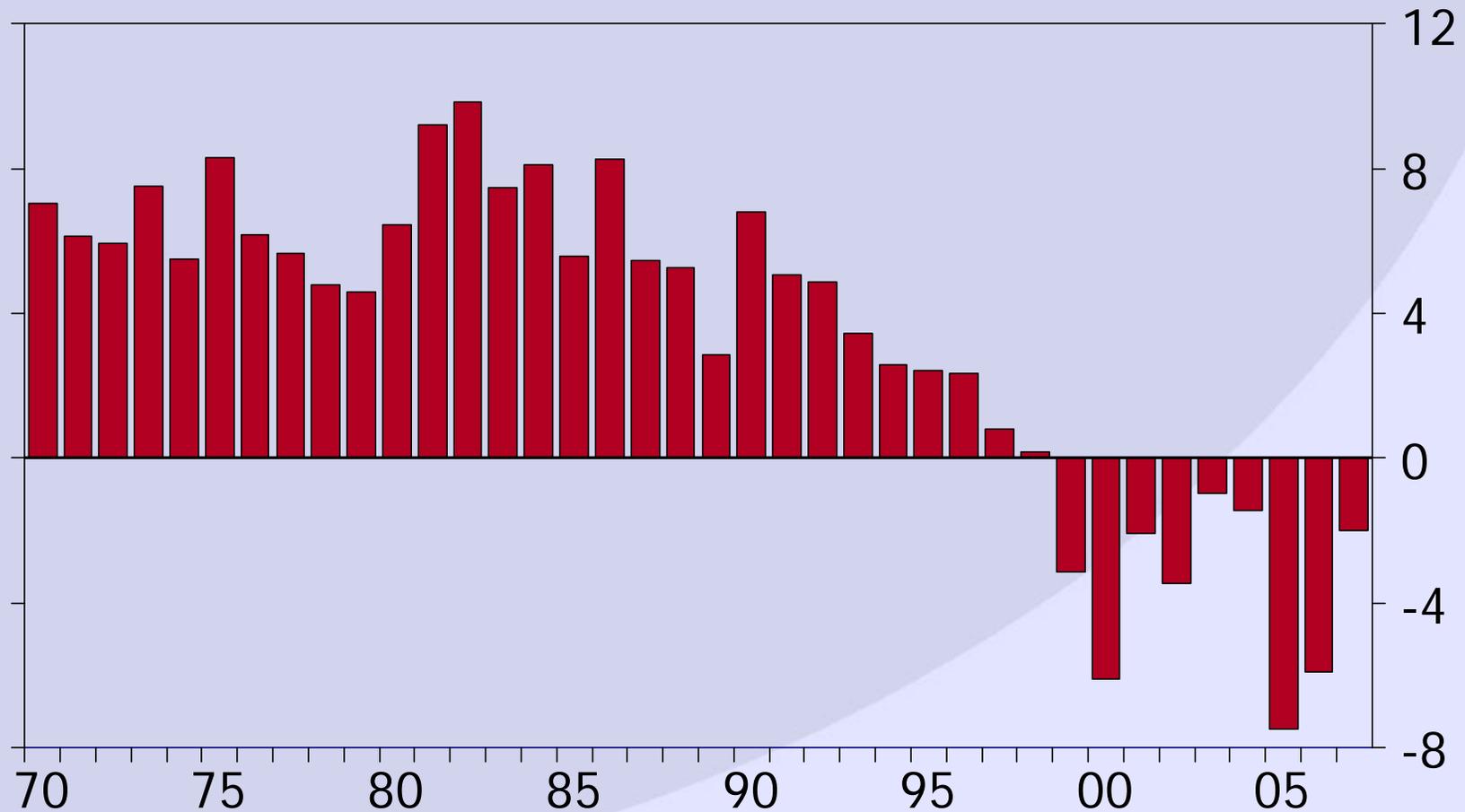
Private Sectors, Arizona



Consumer Update

- Consumers now in full retreat
- Money to support spending
 - Mortgage equity withdrawals
 - Have sold huge amounts of corporate equities
 - Borrowed heavily
- Since 1999 households have been running a deficit
 - Net financial investment has been negative
 - Liabilities grow faster than assets

Households: Net Financial Investment as % of Personal Income

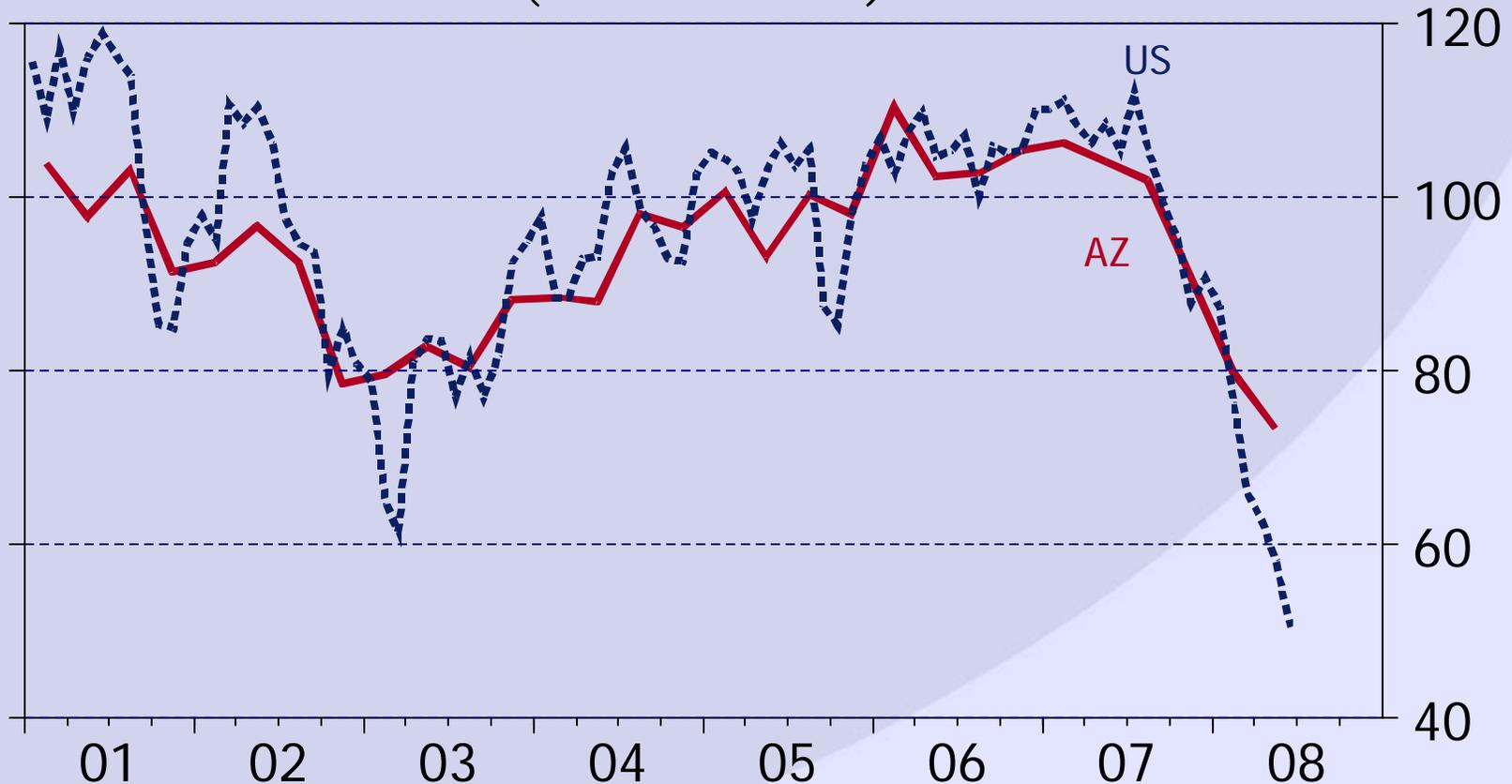


Consumer Update

Confidence plunging (lowest since early '80s)

- Job security, deterioration in labor markets
- Deteriorating financial conditions
- Inflation, esp. gasoline and food
- Postponing purchases of autos, appliances
- Cancelling vacations (lowest since Oct. 1978)
- AZ Retail sales down 9.5% in real terms
- Restaurant & bar sales also declining

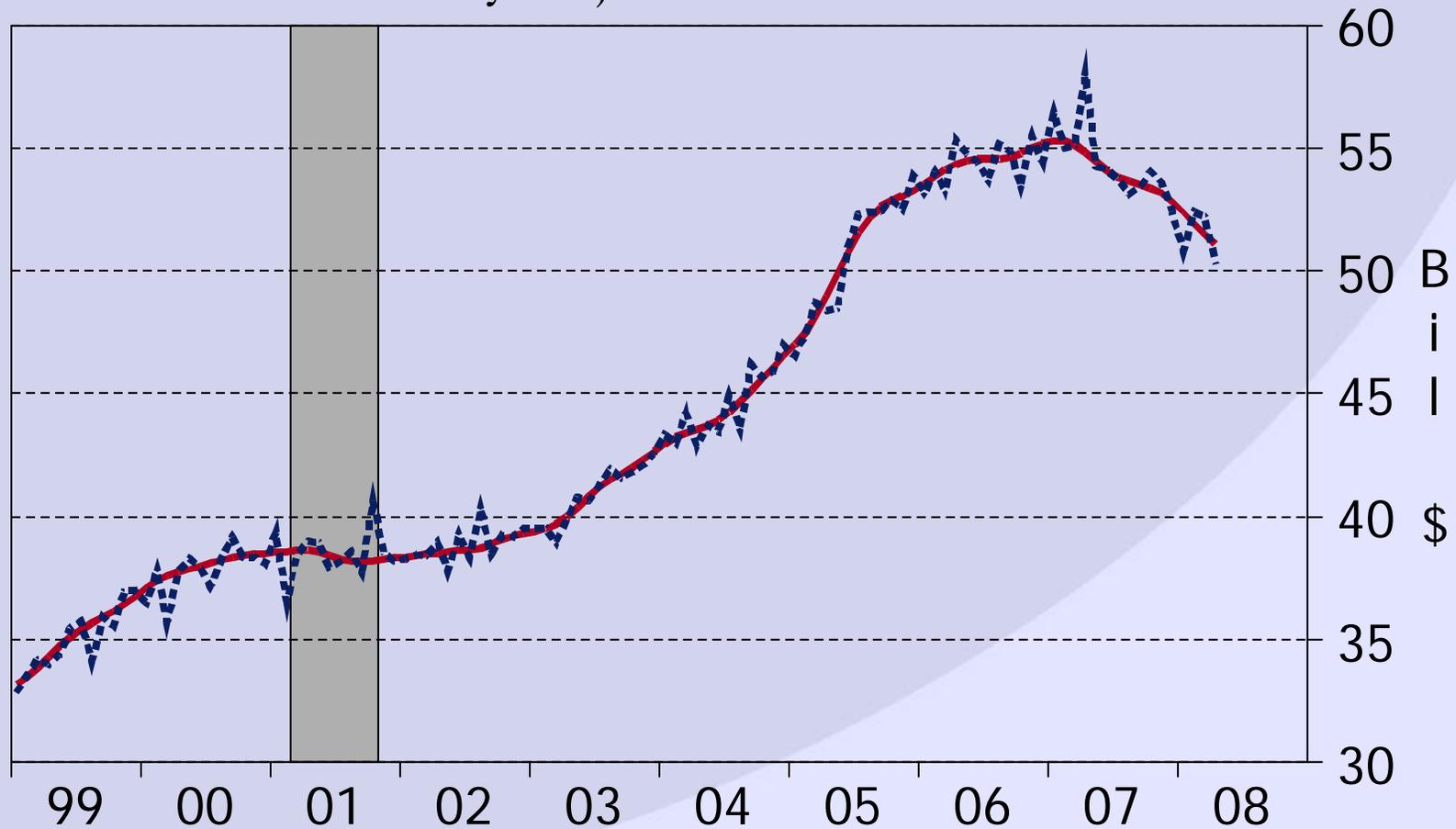
Consumer Confidence Index (1985=100)



Source: Conference Board and Behavior Research Center, Inc.

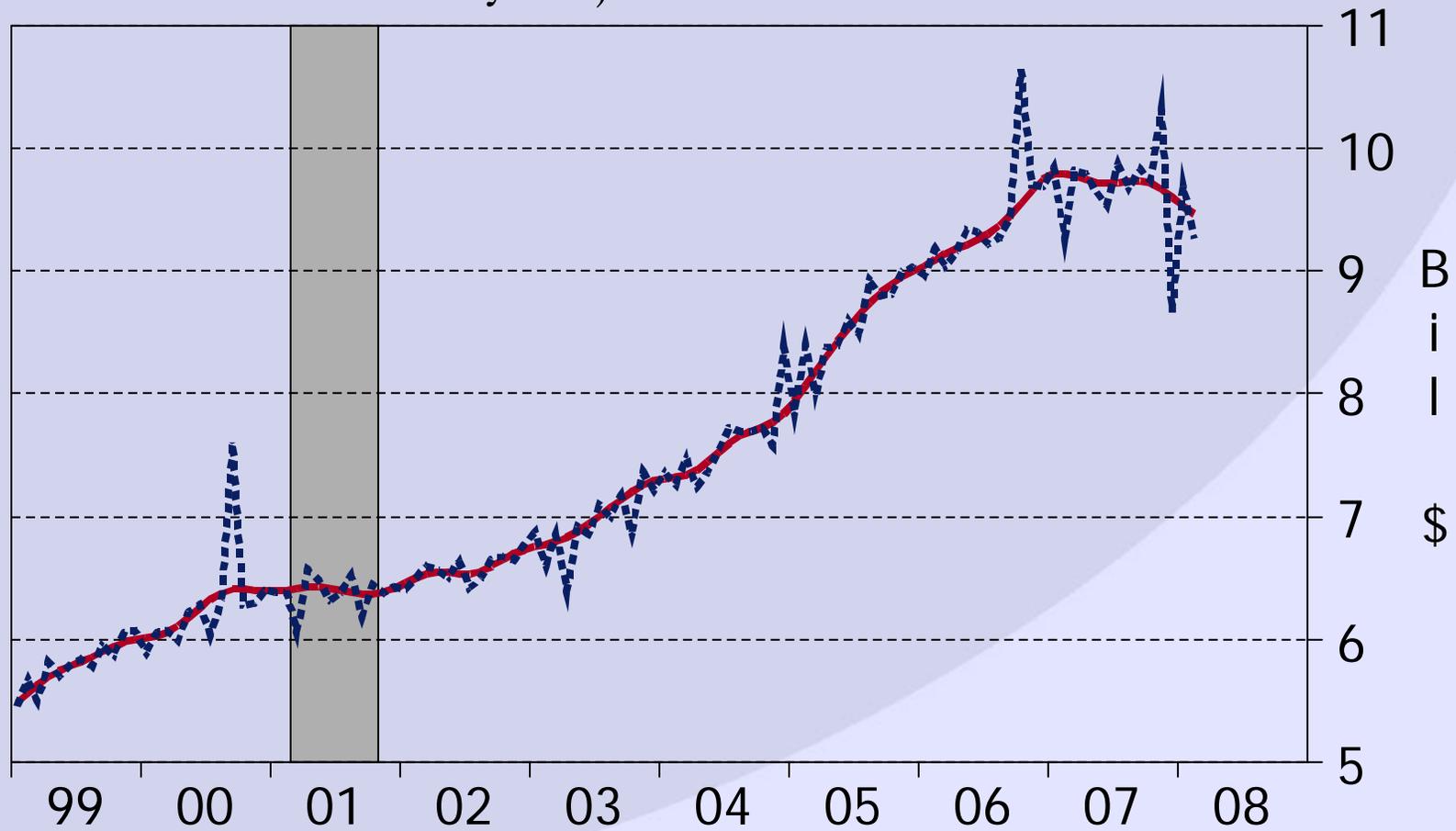
Retail Sales, AZ

seasonally adjusted annual rate

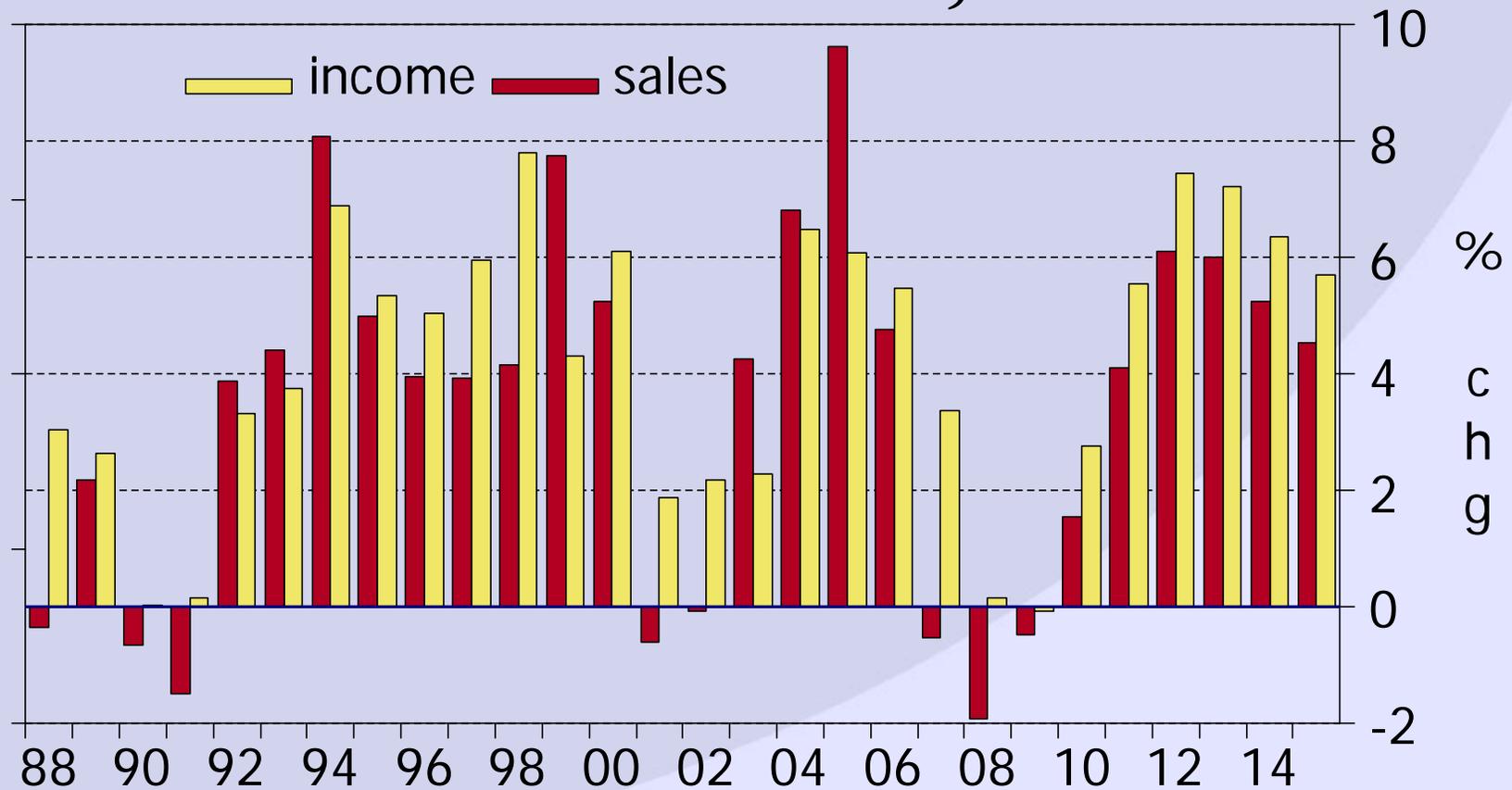


Restaurant & Bar Sales, AZ

seasonally adjusted annual rate



Real Consumer Spending and Income Growth, AZ



Factors Affecting Recovery

- Credit crunch worst since '90-91
 - Credit quality continues to sink, lending standards are tightening
- Massive policy response
 - Fed cut interest rates, sale of Bear Sterns, opened credit windows to banks, Fannie & Freddie
 - Rebate checks are 4.3% of quarterly spending

A W-Shaped Recession?

- Stimulus will lift economy this summer, but when stimulus ends, economy could contract in 4Q and 1Q '09
- With lingering credit problems, growth will be slow
- AZ will not pick up until construction cycle turns up – second half '09

Forecast Highlights: PHX

2007 – 2009

	<u>2007</u>	<u>2008</u>	<u>2009</u>
Nonag Jobs	1.7%	-1.2%	-0.9%
Population	3.5%	2.2%	2.2%
Retail Sales	-0.1%	-1.3%	0.1%
R&B Sales	2.2%	1.6%	3.9%
Personal Income	6.5%	2.9%	2.5%
Housing Permits	-15.8%	-42.5%	2.0%
Wage per Worker	4.2%	3.6%	3.5%

Conclusions

- Housing is in a sharp correction
- Consumers are in full retreat
- No sign of the bottom as yet
- Recession in AZ
 - Job losses 2.4% peak-trough (deeper)
 - Bottom in 3rd quarter 2009 (longer)

**You can't put enough
lipstick on this pig...**



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