Trying to Snatch Defeat from The Jaws of Victory (But it won’t work...)

Lambda Alpha

January 18th, 2013

Presented By:
Elliott D. Pollack
CEO, Elliott D. Pollack & Company
Economic Conditions
The economy we wanted...
What we got…
It is only because conditions have been so poor for so long that we feel this mediocre recovery is OK.
NATIONAL ECONOMY –

Continued subpar growth. But, recovery should continue.
(unless the Federal Gov’t does something stupid….)
Speaking of stupid...
FISCAL CLIFF
(still unresolved)

Causes great uncertainty.
Keep your eye on the ball.

(The ball is deficit reduction).
Best case scenario, The American Taxpayer Relief Act will reduce the deficit by $737 billion over 10 years.

Total Reduction Needed: $4-6 Trillion

*Source: Office of Management and Budget
What we’ve got so far resolves only 12-15% of the problem.
ObamaCare

- Uncertainty over costs
- Uncertainty over implementation
ObamaCare

Summed up in one sentence by:
Barbara Bellar
(Candidate for Illinois State Senate)
Obamacare
Summed up in One Sentence

“We are going to be gifted with a health care plan we are forced to purchase, and fined if we don’t…”
ObamaCare

Summed up in One Sentence

…which reportedly covers at least 10 million more people, without adding a single new doctor, but provides for 16,000 new IRS agents…
ObamaCare
Summed up in One Sentence

…written by a committee whose chairman says he doesn’t understand it…
ObamaCare
Summed up in One Sentence

…passed by a congress that didn’t read it, but exempted themselves from it…
ObamaCare
Summed up in One Sentence

...signed by a president (who smokes)
ObamaCare
Summed up in One Sentence

…with funding administered by a treasury chief (who didn’t pay his taxes)…
ObamaCare
Summed up in One Sentence

...for which we will be taxed for four years before any benefits take affect...
ObamaCare
Summed up in One Sentence

...by the government which has already bankrupted social security and Medicare...
Obamacare
Summed up in One Sentence

...all to be overseen by a surgeon general (who is obese), and financed by a country that’s broke.”
ObamaCare
Summed up in One Sentence

What could possibly go wrong?
United States Real Gross Domestic Product*
Annual Growth 1970 - 2013**
Source: U.S. Bureau of Economic Analysis & Blue Chip Economic Indicators

* Based on chained 2005 dollars.
** 2012 - 2013 are forecasts from the Blue Chip Economic Indicators, November 2012

Recession Periods
At least we’re growing!

And growth should continue,

BUT...
...growth will remain weak because of the following:

- Consumer spending modest, but up (Additional jobs and hours worked).
- Business spending up
- Excess industrial capacity.
- Continued housing recovery in 2013. Large percent gain. Small numerical gain.
- Limited commercial construction.
- Continued pressure on state and local government.
- Limited policy options on part of Federal government.
Consumers
Consumer debt has declined by $1.7 trillion over the last 4 years.
Financial Obligation Ratio**
1980 – 2012*
Source: Federal Reserve

*Data through second quarter 2012
**Ratio of mortgage and consumer debt (including auto, rent and tax payments) to disposable income.
Non-Mortgage Consumer Credit Outstanding
Percent Change Year Ago
1970 – 2012*
Source: The Federal Reserve Bank of St. Louis

*Data through November 2012
US New Job Data
Change from Prior Month (S/A)
June 2010 – December 2012
Source: Bureau Labor of Statistics
Hours Worked
Percent Change from Year Ago
1976 – 2012*
Source: Bureau of Labor Statistics

-10%
-8%
-6%
-4%
-2%
0%
2%
4%
6%
8%
10%

1976 Q1
1977 Q1
1978 Q1
1979 Q1
1980 Q1
1981 Q1
1982 Q1
1983 Q1
1984 Q1
1985 Q1
1986 Q1
1987 Q1
1988 Q1
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2001 Q1
2002 Q1
2003 Q1
2004 Q1
2005 Q1
2006 Q1
2007 Q1
2008 Q1
2009 Q1
2010 Q1
2011 Q1
2012 Q1

Recession Periods

*Data through third quarter 2012
Consumer Confidence
1978 – 2012*
Source: The Dismal Scientist

Recession Periods

Approval of medical marijuana...

*Data through December 2012
Refinancing will free up money...
WEALTH EFFECT

Housing prices are up.

Stock market is up from a year ago.
Net Worth – Owners' Equity in Household Real Estate
Source: Board of Governors of the Federal Reserve System

Recession Periods
Total Net Worth

Source: Board of Governors of the Federal Reserve System

Recession Periods
Consumer Summary:

- Jobs are being created at a slow rate.
- Those that have jobs are spending a little more but will remain cautious.
- Unemployment to remain high, but should trend lower.
- Wealth levels are improving.
- Will the additional uncertainty translate into reduced consumer spending?
Business
Business debt has declined by $2.9 trillion over the last 4 years.
Corporate Profit
(Billions of Dollars, SA)
1975-2012*
Source: BEA

*Data through third quarter 2012
Business Spending on Equipment
Percent Change from Prior Quarter
2005 – 2012*

Source: Bureau of Economic Analysis

Recession Periods

*Data through third quarter 2012
Business Spending on Plant
Percent Change from Prior Quarter
2005 – 2012*

Source: Bureau of Economic Analysis

Recession Periods

*Data through third quarter 2012
Capacity Utilization Rate
1970 – 2012*

Source: The Federal Reserve Bank of St. Louis

*Data through November 2012
Business Summary:

- Businesses are in better shape.
- Spending on equipment to continue to grow.
- Spending on plant will lag until capacity utilization goes higher...getting close.
- Employment to continue to grow.
Government
Speaking of stupid...
Gross Government debt has INCREASED by $5.8 trillion over the last 4 years.
Balanced Budget

We are borrowing $0.34 of every dollar we spend and can’t collect enough in taxes to make it up.
## Balanced Budget

<table>
<thead>
<tr>
<th>RECEIPTS</th>
<th>$ tril</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual income taxes</td>
<td>1.165</td>
</tr>
<tr>
<td>Corporate income taxes</td>
<td>0.237</td>
</tr>
<tr>
<td>Social insurance &amp; medicare taxes</td>
<td>0.775</td>
</tr>
<tr>
<td>Unemployment insurance</td>
<td>0.066</td>
</tr>
<tr>
<td>Other</td>
<td>0.226</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$2.469</strong></td>
</tr>
</tbody>
</table>

Source: U.S. Treasury; FY 2013 U.S. Budget
## Balanced Budget

<table>
<thead>
<tr>
<th>EXPENDITURES</th>
<th>$ tril</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discretionary (security – military, defense, homeland security, FBI, CIA and non-security – departments of education, energy, etc.)</td>
<td>1.319</td>
</tr>
<tr>
<td>Mandatory (Programs such as Medicare, Medicaid, SS, TARP)</td>
<td>2.252</td>
</tr>
<tr>
<td>Interest on debt</td>
<td>0.225</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$3.796</strong></td>
</tr>
</tbody>
</table>
Balanced Budget?

EXPENDITURES = $3.796 trillion
RECEIPTS = $2.469 trillion

= DEFICIT = $1.327 trillion

Discretionary Expenditures = $1.319 trillion

Source: U.S. Treasury; FY 2013 U.S. Budget
Balanced Budget

So, even if we completely shut down government, including the military, we still wouldn’t have a balanced budget.
Balanced Budget

The federal debt scheduled to be:

$16.2 trillion in 2013
$25.9 trillion in 2022

Source: U.S. Treasury; FY 2013 U.S. Budget
U.S. Gross National Debt ($tril)

Source: U.S. Treasury; FY 2013 U.S. Budget

--- Obama Administration proposed budget, Aug. 2012
Federal Surplus (+) or Deficit(-)
1905-2012
Source: Office of Management and Budget
What is the tipping point?
It WILL happen but no one can tell when.
You won’t know what you’re getting until it’s TOO LATE.
What does the government need to do?

First, admit there is a problem

Second, deal with the problem.

It will be painful and there is no easy way out.
What does the government need to do?

- Need significant cuts in the rate of increase for long term fiscal health.
- Modest tax increases designed not to hurt incentives.
- But, significant cuts or tax increases will hurt the economy next year.
- Therefore, they need to phase it in!!!
Individual Income Taxes as Percent of GDP
Source: Office of Management and Budget
In 1930, the average life expectancy of someone entering the workforce was 66 years old.
Today, the average life expectancy of someone entering the workforce is 79 years old.
In 1934, the retirement age was 65.
Today, the retirement age is 67.
Social Security Beneficiaries per 100 Covered Workers
1950-2090*
Source: Social Security Administration

*2012-2090 Intermediate Forecast by Social Security Administration
Today, persons 65 years and older represent 13% of the U.S. population.

*Source: U.S. Census Bureau*
In 2020, persons 65 years and older will represent nearly 17% of the U.S. population.

*Source: U.S. Census Bureau*
In 2030, persons 65 years and older will represent nearly 23% of the U.S. population.

*Source: U.S. Census Bureau*
Per Capita Health Care Costs by Age
Source: “US-Europe Comparisons of Health Risk for Specific Gender Age Groups”

U.S. is spending much more for older ages
Government Summary:

- State & local under pressure.
- But, more revenues available in FY2013.
- Federal spending up but more slowly.
- Fiscal problem not resolved.
Question:
Can Europe cause a recession in the U.S.?
Conclusion:

Europe unlikely to cause any significant problems for U.S.
NATIONAL SUMMARY

- Consumers still restructuring
- Confidence low, but spending will continue to grow
- Business in good shape but not confident because of:
  - Low capacity utilization
  - Cost of Obama Care
  - Fiscal Cliff?
- Federal government, no leadership whatsoever.
ARIZONA

Happy Birthday!!
Arizona & US Move Together
(Non-farm Emp. Percent Change 1980 – November 2012)
Job Growth 2006

Source: US BLS

Alaska

Hawaii

Jobs growing
Top 10
Jobs declining
Job Growth 2009

Source: US BLS

Jobs growing: Hawaii (49)

Jobs declining:
- Alaska (2)
- 34
- 46
- 44
- 20
- 1
- 3
- 5
- 10
- 7
- 9

Hawaii

Jobs growing
Top 10
Jobs declining

Elliott D. Pollack & Company
Jobs growing

Jobs declining

Top 10

Source: US BLS
Job Growth 2012
YTD November 2012 vs YTD November 2011
Source: US BLS

Alaska
43

Hawaii
14

Jobs growing
Top 10
Jobs declining

Source: US BLS
There is little that isn’t transitory…

...It is mostly cyclical
How did AZ go from 2nd to 49th?

- Financial meltdown.
- Credit crunch/freeze.
- Overextended consumer.
- Excess single family inventory.
- Housing prices decline.

- Loss of wealth including home equity.
- Can’t sell homes or retire.
- Homebuilding and home prices crash.
- *Population inflows weaken in AZ.*
- Household size increases.
- Household formations decline.

- Excess commercial construction

- “Growth” job losses.
- All sector job loses.
How does AZ go from 49th to 2nd?

- Overall US economic recovery improves.
- Stock market improves.
- Credit frees up.
- Consumers more confident.
- **People start to move to AZ again, slowly.**
- Investors help absorb excess housing.

- Excess housing absorbed
- Housing prices rise.
- Construction kicks in.
- **Construction job gains.**

- **All sector job gains.**
- More people move to AZ.
But the local recovery will be slow because...

- Slow national recovery
- Consumers still restructuring
- Low levels of confidence
- Winding down of defense sector
- Population flows slow:
  - 40% of U.S. households are not mortgage creditworthy.
  - More than 39% in Arizona and 22% nationally have no equity in their homes.
# Arizona Employment Growth

*Source: Arizona State University, U.S. Bureau of Labor Statistics*

<table>
<thead>
<tr>
<th>Year</th>
<th>Rank</th>
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<td>2009</td>
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<td>2010</td>
<td>49</td>
</tr>
<tr>
<td>2011</td>
<td>23</td>
</tr>
<tr>
<td>2012*</td>
<td>6</td>
</tr>
</tbody>
</table>

*YTD November 2012 vs YTD November 2011*
Arizona Employment*
Annual Percent Change 1975–2013**
Source: Department of Commerce, Research Administration

*Non-agricultural wage & salary employment. Changed from SIC to NAICS reporting in 1990.

** 2012 & 2013 forecast is from Elliott D. Pollack & Co.
Speaking of stupid...
FISCAL CLIFF IN ARIZONA?

Projected Net Job Growth:
2012 = 48,000
2013 = 73,600
2014 = 88,500
FISCAL CLIFF IN ARIZONA?

If the mandated spending cuts take place, total loss to Arizona is projected at:

45,000 to 50,000 jobs.

(This does not take into account any slowdown caused by tax increases.)

We will still grow, but very slowly.
### Greater Phoenix Employment*
#### Annual Percent Change 1975–2013**

*Non-agricultural wage & salary employment. Changed from SIC to NAICS reporting in 1990.

** 2012 & 2013 forecast is from Elliott D. Pollack & Co.

<table>
<thead>
<tr>
<th>Year</th>
<th>Percent Change</th>
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<tbody>
<tr>
<td>1975</td>
<td>-3.7%</td>
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<tr>
<td>1977</td>
<td>4.9%</td>
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<tr>
<td>1979</td>
<td>13.3%</td>
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<tr>
<td>1981</td>
<td>10.4%</td>
</tr>
<tr>
<td>1983</td>
<td>5.8%</td>
</tr>
<tr>
<td>1985</td>
<td>11.2%</td>
</tr>
<tr>
<td>1987</td>
<td>9.3%</td>
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<tr>
<td>1989</td>
<td>4.8%</td>
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<td>1991</td>
<td>3.5%</td>
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<td>1993</td>
<td>2.5%</td>
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<td>1995</td>
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<td>1997</td>
<td>6.6%</td>
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<td>7.2%</td>
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<td>2001</td>
<td>7.3%</td>
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<tr>
<td>2003</td>
<td>5.4%</td>
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<td>2005</td>
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<td>1.6%</td>
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<tr>
<td>2011</td>
<td>2.0%</td>
</tr>
<tr>
<td>2013</td>
<td>3.0%</td>
</tr>
</tbody>
</table>

Recession Periods

*Department of Commerce, Research Administration*
# Greater Phoenix Employment*

*Source: Bureau of Labor Statistics*

<table>
<thead>
<tr>
<th>Sectors in Decline</th>
<th>Net Change</th>
<th>Sectors Improving</th>
<th>Net Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other Services</td>
<td>-800</td>
<td>Professional &amp; Bus Services</td>
<td>12,900</td>
</tr>
<tr>
<td>Information</td>
<td>-400</td>
<td>Trade, Transp, Utilities</td>
<td>11,100</td>
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<tr>
<td></td>
<td></td>
<td>Education &amp; Health Services</td>
<td>9,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Construction</td>
<td>5,400</td>
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<td></td>
<td></td>
<td>Leisure &amp; Hospitality</td>
<td>5,000</td>
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<tr>
<td></td>
<td></td>
<td>Financial Activities</td>
<td>4,500</td>
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<td>Government</td>
<td>2,500</td>
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<tr>
<td></td>
<td></td>
<td>Manufacturing</td>
<td>1,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Mining</td>
<td>0</td>
</tr>
</tbody>
</table>

*Nov. 2012/ Nov. 2011*
Greater Phoenix-Jobs Finally in the Black

Over last 12 months:       50,700
12 months before that:     26,200
12 months before that:     5,900
12 months before that:     (134,300)
12 months before that:     (97,500)

* As of November 2012
Greater Phoenix Jobs
Source: BLS

Jobs lost Peak to Trough: 234,000
(Dec-07) (Jul-10)

Jobs gained Trough to Current: 92,400
(Jul-10) (Nov-12)

***We are 40% of the way back***

*Based on seasonally adjusted monthly data*
Employment Levels: Greater Phoenix back to Peak in 2015?

Source: ADOA

Recession Periods

Peak
Greater Phoenix Non-Farm Employment Gains
41 Months After Recession End
Source: BLS Seasonally Adjusted Data
## Phoenix-Mesa Employment Growth

(Ranking among all metro areas greater than 1,000,000)

*Source: Arizona State University, U.S. Bureau of Labor Statistics*

<table>
<thead>
<tr>
<th>Year</th>
<th>Rank</th>
<th># MSA’s</th>
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<tbody>
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<th>Year</th>
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<td>2011</td>
<td>12</td>
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<tr>
<td>2012*</td>
<td>3</td>
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*Year-to-date, November 2012*
# Greater Phoenix Employment

Source: U.S. Bureau of Census; Arizona Department of Administration; University of Arizona Forecasting Project

<table>
<thead>
<tr>
<th>YEAR</th>
<th>EMPLOYMENT</th>
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<tbody>
<tr>
<td>1950</td>
<td>74,400</td>
</tr>
<tr>
<td>1960</td>
<td>181,700</td>
</tr>
<tr>
<td>1970</td>
<td>327,200</td>
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<td>1980</td>
<td>636,200</td>
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<td>1,013,300</td>
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<tr>
<td>2000</td>
<td>1,578,400</td>
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<tr>
<td>2010</td>
<td>1,686,800</td>
</tr>
<tr>
<td>2020</td>
<td>2,312,700</td>
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</table>
## Maricopa County Population

Source: U.S. Bureau of Census; Arizona Department of Economic Security; University of Arizona Forecasting Project

<table>
<thead>
<tr>
<th>Year</th>
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<th>Rate</th>
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<tbody>
<tr>
<td>1950</td>
<td>331,770</td>
<td></td>
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<tr>
<td>1960</td>
<td>663,510</td>
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<td>1970</td>
<td>971,228</td>
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</tr>
<tr>
<td>1980</td>
<td>1,509,175</td>
<td>4.5%</td>
</tr>
<tr>
<td>1990</td>
<td>2,122,101</td>
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</tr>
<tr>
<td>2000</td>
<td>3,072,149</td>
<td>3.8%</td>
</tr>
<tr>
<td>2010</td>
<td>3,817,117</td>
<td>2.2%</td>
</tr>
<tr>
<td>2020(forecast)</td>
<td>4,569,572</td>
<td>1.8%</td>
</tr>
</tbody>
</table>
Greater Phoenix Population
Annual Percent Change 1976–2013*
Source: Arizona State University & Department of Commerce, Research Administration

* 2012 & 2013 forecast is from Elliott D. Pollack & Co.
Five Year Distribution of Movers in U.S. by Type*
1980-2010
Source: U.S. Census Bureau

*Excludes movers in the same county

Movers (in millions)

- 1965–1970
  - Different county, same state: 6.9
  - Different county, different state: 7.1
  - From Abroad: 1.2

- 1970–1975
  - Different county, same state: 7.4
  - Different county, different state: 7.6
  - From Abroad: 1.7

- 1975–1980
  - Different county, same state: 9.6
  - Different county, different state: 9.5
  - From Abroad: 1.9

- 1980–1985
  - Different county, same state: 8.2
  - Different county, different state: 7.8
  - From Abroad: 1.6

- 1985–1990
  - Different county, same state: 10.4
  - Different county, different state: 10.1
  - From Abroad: 2.4

- 1990–1995
  - Different county, same state: 9.4
  - Different county, different state: 8.6
  - From Abroad: 2.3

- 1995–2000
  - Different county, same state: 11.7
  - Different county, different state: 10.1
  - From Abroad: 3.5

- 2000–2005
  - Different county, same state: 9.7
  - Different county, different state: 8.3
  - From Abroad: 2.5

- 2005–2010
  - Different county, same state: 6.7
  - Different county, different state: 5.6
  - From Abroad: 1.5

*Excludes movers in the same county
School Enrollment Growth
2001-2012
Source: Arizona Department of Education

The real estate market we wanted...
The real estate market we got...
It’s hard not to be optimistic about HOUSING
US Total Vacant Housing Units
1965-2012*
Source: US Census Bureau

*Data through 2012 Q3
Housing

Not a light switch...

A dimmer switch...
• Think of what the housing market is going through as the same as any manufacturer that finds themselves with excess inventory…

• Prices are cut until the excess is sold.

• Then prices rise.
Price gains are largely in distressed properties.
Also, about 40% of Households are not credit worthy.

Source: CoreLogic
Until this gets resolved locally and nationally, the rate of population growth will be anemic.
This will limit the rate of growth in jobs.
As housing prices go up, more and more people will be able to sell their homes because they aren’t underwater.
Household Formations

Lower during recessions (doubling up, living at home with mom & dad, etc)
In a weak economy, population growth fails to translate into household growth, but when the economy begins to strengthen, there is pent-up demand for housing.

Source: Linneman Letter
As new housing and housing prices recover, the entire economy is helped.
There are still issues…

• Population flows
So, we are on the right track.
But, we are recovering, we are not recovered.
OFFICE

More lights on?
As of third quarter 2012, there are 300,975 square feet of office space under construction.

Source: CBRE
Under any reasonable employment growth scenario, we believe it will be 2016 before any significant office construction occurs (although some sub-markets will be sooner).
INDUSTRIAL

Slowly filling up?
As of third quarter 2012, there are 5.4 million square feet of industrial space under construction.

Source: CBRE
RETAIL

WEDDING DRESS
$50
WORN ONCE
BY MISTAKE
As of third quarter 2012, there are 0.9 million square feet of retail space under construction.

Source: CBRE
CONCLUSIONS:
How will it all turn out?
The Result....

9 Months Ago...
My Mommy Read
50 Shades of Grey
The economy is improving in both absolute and relative terms.
Is the Glass Still Half Full?
Growth is slow by historic standards because the U.S. economy is slow and incentives are perverse.
The economy should gain some momentum (unless the Federal government does something stupid)
Speaking of Stupid…
There is a BOOM for Arizona out there somewhere.
But not in 2013.
ARIZONA—
Slow but mildly accelerating recovery.

2013 will be better than 2012
2014 will be better than 2013
2015 should be a good year.
• Economic and Fiscal Impact Analysis/Modeling
• Real Estate Market and Feasibility Studies
• Litigation Support
• Revenue Forecasting
• Keynote Speaking
• Public Finance and Policy Development
• Land Use Economics
• Economic Development

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