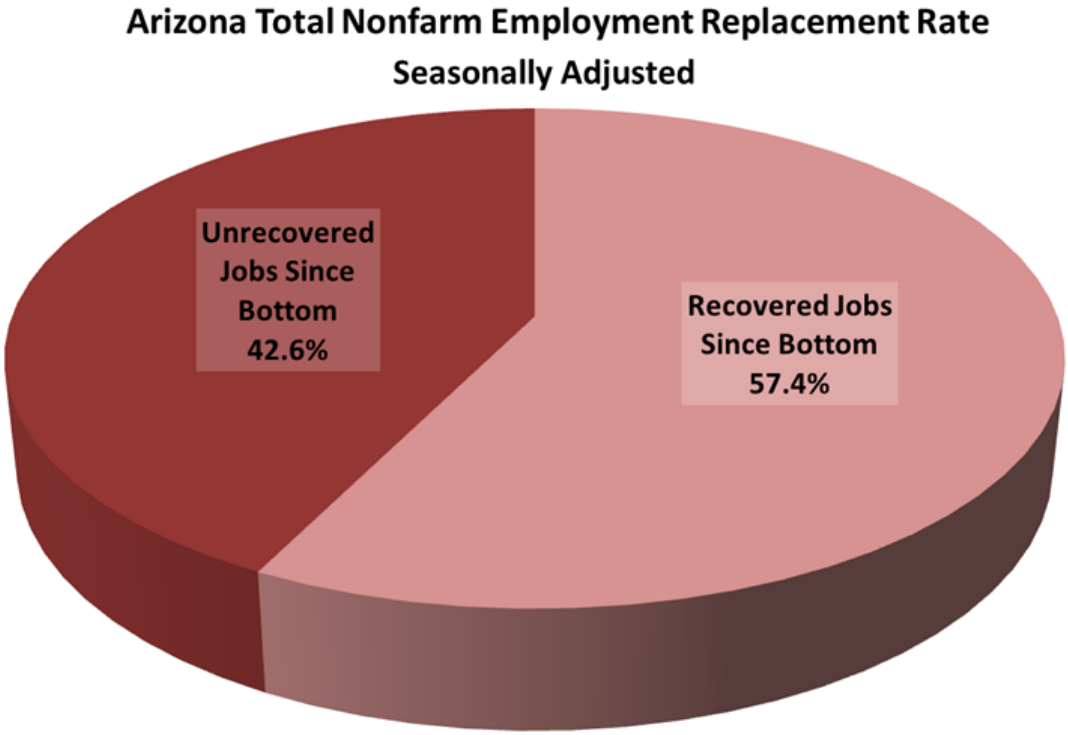
ARIZONA ECONOMIC ENVIRONMENT

The Arizona Department of Administration (ADOA), Office of Employment and Population Statistics (EPS) produces demographic, labor force, and economic information for Arizona. As described by EPS, the following are the economic highlights for PY 2013:

Arizona's overall economic environment has continued to gradually improve since the end of the recession (July 2009). Arizona experienced one of the deepest and longest recession of any state. The recession period has been followed by a slow and gradual recovery. As of June 2014, Arizona has recovered 57.4% of Nonfarm jobs lost as measured from peak employment level (October 2007) to trough employment level (September 2010). In contrast U.S. has recovered 104.8% of Nonfarm jobs lost from peak employment level (January 2008) to trough employment level (February 2010). The employment peak and trough occurred at different time frames in the U.S. and Arizona.



Source: Produced by the Arizona Office of Employment and Population Statistics in cooperation with the U.S. Dept. Of Labor, Bureau of Labor Statistics

- Indicators that contributed to this gradual economic recovery are:
  - Gross Domestic Product, real personal income at the state and national levels, employment, and retail sales show continued improvement.[1]

[1] See FRED graphs and data for the variables: real gross domestic product, 1 decimal (GDPC1); real personal income (RPI); real disposable personal income (DSPIC96); total personal income in Arizona (AZOTOT); per capital personal income in Arizona (AZPCPI); and real retail and food services sales (RRSFS) at the website http://research.stlouisfed.org/fred2/

- Continued employment gains in the private sector, increasing private domestic investment, gradual increase in the index of industrial production and rate of capacity utilization, high levels of corporate profit, and a gradual resurgence in private residential construction permits.[2]
- Continued gradual climb in household net worth resulting from paying down of debts and accumulation of assets either through cash savings or through their homes. U.S. exports are also increasing.[3]
- Residential real estate markets in Arizona and Phoenix metropolitan area are showing an improvement as measured by various indicators. Home prices in Arizona are improving but are still way off pea k[4]. In private residential real estate, a majority of the growth recently has been in the construction of multi-family structures, or apartments. Construction and sales of single family, private residences, though gradually increasing, are well below their most recent peaks of the housing bubble.[5] Commercial real estate is gradually improving with lower vacancy rates, higher rental rates and lower rates of default and delinquency in mortgage loans.[6] Industrial real estate sectors are also improving with increasing levels of construction activity across the nation for the building of warehouses and distribution centers to support online commerce.[7].
- Revolving consumer credit levels have remained flat. However, an expansion of non-revolving consumer credit since 2011 has served as an impetus to expanding economic activity. Consumer sentiment and consumer spending have shown signs of improvement, but the rate of growth has been slowing down.[8]

---

[2] See FRED graphs and data for the variables: real gross private domestic investment, 3 decimal (GPDIC96); industrial production index (INDPRO); capacity utilization (TCU); capacity utilization – manufacturing (MCUMFN); corporate profits after tax (CP); new private housing units authorized by building permits-in structures with 1 unit (PERMIT1); privately owned housing starts authorized by building permits, 1-unit structures for Arizona (AZBP1FH); and new private housing units authorized by building permit for Arizona (AZBPPRIV). at the website http://research.stlouisfed.org/fred2/

[3] See FRED graphs and data for the variables: total net worth-balance sheet of households and nonprofit organizations (TNWBSHNO); total assets-balance sheet of households and nonprofit organizations (TABSHNO); owners' equity in household real estate-net worth-balance sheet of households and nonprofit organizations (OEHRENWBSHNO); total liabilities-balance sheet of households and nonprofit organizations (TLBSHNO); home mortgages-liabilities-balance sheet of households and nonprofit organizations (HMLBSHNO); debt outstanding domestic nonfinancial sectors-household, consumer credit sector (HCCSDODNS); debt outstanding domestic nonfinancial sectors-household, home mortgage sector (HHMSDODNS); household debt service payments as a percent of disposable personal income (TDSP); and real exports of goods & services, 1 decimal (EXPGSC1) at the website http://research.stlouisfed.org/fred2/

[4]See FRED graphs and data for the variables: all-transactions house price index for the United States (USSTHPI); all-transactions house price index for Arizona (AZSTHPI); home price index for Phoenix, Arizona (PHXRNSA); new private housing units authorized by building permit for Phoenix-Mesa-Scottsdale, AZ (MSA) (PHOE004BPPRIV); privately owned housing starts authorized by building permits: 1-unit structures for Phoenix-Mesa-Scottsdale, AZ (MSA) (PHOE004BP1FHSA); privately owned housing starts, authorized by building permits, 1-unit structures for Tucson, AZ, MSA, (TUCS004BP1FHSA); new private housing units authorized by building permits for Tucson, AZ, MSA, (TUCS004BPPRIV) ;privately owned housing starts authorized by building permits, 1-unit structures for Arizona (AZBP1FH); and new private housing units authorized by building permit for Arizona (AZBPPRIV); total private construction spending: residential (PRRESCONS); private residential fixed investment (PRFI); and real private residential fixed investment, 3 decimal (PRFIC96). At the website: http://research.stlouisfed.org/fred2/.

[5] See (a) FRED graphs and data for the variable: new private housing units authorized by building permits for Arizona(AZBPPRIV); privately owned housing starts authorized by building permits: 1-unit structures for arizona(AZBP1FH); housing starts: total: new privately owned housing units started(HOUST); privately owned housing starts: 1-unit structures(HOUST1F); new privately-owned housing units authorized by building permits: total(PERMITNSA); and new private housing units authorized by building permits - in structures with 1 unit(PERMIT1) . At the website: http://research.stlouisfed.org/fred2/.

(b) Wells Fargo Economics Group. Special Commentary. Housing Data Wrap-Up: February 2014. Mark Vitner. Anika R. Kahn. February 28, 2014 . At the website: www.wellsfargo.com/com/research/economics.

(c) Wells Fargo Economics Group. Special Commentary. Housing Chartbook: March 2014. Mark Vitner. Anika R. Kahn. April 9, 2014 . At the website: www.wellsfargo.com/com/research/economics.

(d) IHS Global Insight U.S. Forecast for April 2014. At the website: www.ihs.com/products/global-insight/index.aspx.

[6] See (a) Wells Fargo Economics Group. Special Commentary. Commercial Real Estate Chartbook:Q4. Mark Vitner. Anika R. Kahn. March 13, 2014 . At the website: www.wellsfargo.com/com/research/economics.

(b) IHS Global Insight U.S. Forecast for April 2014. At the website: www.ihs.com/products/global-insight/index.aspx.

[7] See (a) Wells Fargo Economics Group. Special Commentary. Industrial Fundamentals Move Ahead. Anika R. Kahn. March 28, 2014 . At the website: www.wellsfargo.com/com/research/economics.

(b) IHS Global Insight U.S. Forecast for April 2014. At the website: www.ihs.com/products/global-insight/index.aspx.

[8] See FRED graphs and data for the variables: total revolving credit owned and securitized, outstanding (REVOLSL); total nonrevolving credit owned and securitized, outstanding (NONREVSL); University of Michigan: consumer sentiment (UMCSENT); and real personal consumption expenditures (PCEC96) at the website http://research.stlouisfed.org/fred2/

Some factors that could further dampen the growth of the local economy are given below. However, the positive factors listed above outweigh the uncertainties in the sections described below.

- Constrained budgets persist for a large majority of households. Despite some job growth and lowering in the unemployment rate, many consumers in Arizona continue to face employment insecurity, lower wages and benefits, debt, and rising prices for essentials that limits the amount of funds available for discretionary spending.[9]
- Despite the improvement in residential real estate market, stringent Dodd-Frank rules and increased government scrutiny may limit the entry of new firms into the mortgage market. Rising interest rates could serve as a deterrent to some prospective buyers.[10]
- Although real business investment continues to grow, the rate of growth has slowed as a consequence of demand uncertainty.
- In the public sector, the policies of the federal government have turned from fiscal stimulus during and immediately after the most recent economic downturn to austerity in the form of reduced expenditures and higher taxes as a means of reducing the federal budget deficit. The cost of austerity policy measures that include spending cuts, tax increases, or a mixture of the two have slowed the aggregate demand in the US economy, thereby slowing the rate of economic and employment growth.[11]

- Arizona is one of the states in the nation most vulnerable to federal government expenditure changes because of the large proportion of military spending in the state's economy. Operating at a lower level of federal government expenditures is projected to have the greatest impact in the following major industry sectors: Manufacturing; Retail Trade; Professional and Business Services; and Government. [12]
- Despite the factors listed above there are some grounds for limited optimism as Arizona exports could have a slight stimulating effect with a gradual improvement in the overall world economy, especially in the major US trading partners such as Canada and Mexico.

Arizona's employment was one of the fastest growing in the nation prior to the recession starting at the end of 2007. During Calendar Year (CY) 2010, the state's national ranking had fallen to

---

[9]See (a) Global Insight U.S. Forecast for October 2013. At the website: www.ihs.com/products/global-insight/index.aspx.
(b) Wells Fargo Economics Group. Special Commentary. The U.S. labor Market Is Not Working For Many. Jay H. Bryson and Sarah Watt. August 29, 2013. At the website: www.wellsfargo.com/com/research/economics.
(c) Wells Fargo Economics Group. Special Commentary. Economic Western Round Up: Western States Leading the Nation's Recovery. Mark Vitner, Michael T. Wolf and Sara Silverman. July 24, 2013. Page 4. At the website: www.wellsfargo.com/com/research/economics.
[10] See Finance Advisory Committee. Revenue and Budget Update. Joint Legislative Budget Committee. State of Arizona Legislature. April 10, 2014. At the web site: http://www.azleg.gov/jlbc/revenuebudgetupdate041014.pdf.
[11]See (a) Global Insight U.S. Forecast for April 2013. at the website www.ihs.com/products/global-insight/index.aspx.
(b) Wells Fargo Economics Group. Special Commentary. Economic Impact of Sequestration. February 25, 2013. At the website: www.wellsfargo.com/com/research/economic.
(c) Wells Fargo Economics Group. Special Commentary. Sequestering Economic Growth?. John E. Silvia and Michael A. Brown. September 27, 2013. At the website: www.wellsfargo.com/com/research/economic.
[12]See: (a) Wells Fargo Economics Group. Special Commentary. Sequestration: Which States Are Most Vulnerable?. February 18, 2013. At the website: www.wellsfargo.com/com/research/economic.
(b) Wells Fargo Economics Group. Special Commentary. Economic Impact of Sequestration. February 25, 2013. At the website: www.wellsfargo.com/com/research/economic.
(c) Wells Fargo Economics Group. Special Commentary. Arizona Economic Outlook: November 2013. Mark Vitner and Michael T. Wolf November 4, 2013. At the website: www.wellsfargo.com/com/research/economic.
(d) Wells Fargo Economics Group. Joint Economics and Municipal Commentary. FY 2014 State Budgets and Beyond. John E. Silvia, Natalie Cohen, Michael A. Brown and Roy Eappen. July 9, 2013. At the website: www.wellsfargo.com/com/research/economics.
(e) IHS Global Insight. US Markets State Economies. Arizona. Jim Diffley. Winter2013-14. At the website: http://www.ihs.com/products/global-insight.

49th, improving to 36th by May, 2011. As of the writing of this report, Arizona's ranking had improved to twenty first in the nation.

There was modest growth of 1.9 percent in Nonfarm employment in 2013. Nonfarm employment was flat in 2010 and increased by 1.7 percent in 2011 and 2.3 percent in 2012, after posting losses of 5.3 percent in 2009 and 5.3 percent in 2008 (**Table 1**). For PY 2013, all the major industrial sectors posted employment gains with the exception of Manufacturing and Government. Manufacturing recorded an employment contraction of 0.3 percent, while Government lost 0.7 percent of employment. When over-the-year rate of growth across various sectors are compared in 2013, Financial Activities leads the gains at 5.1 percent followed by Leisure and Hospitality, and Construction, each at 3 percent. Other gaining sectors were: Education and Health Services (2.9 percent); Natural Resources and Mining (2.6 percent); Professional and Business Services (2.2 percent); Information (2.0 percent); Trade, Transportation and Utilities (1.9 percent); and Other Services (0.3 percent).

Table 1: Percentage Change in Program Year (PY) Average Employment in Arizona

Industry	PY 2008	PY 2009	PY 2010	PY 2011	PY 2012	PY 2013
Total Nonfarm	-5.3%	-5.3%	0.0%	1.7%	2.3%	1.9%
Manufacturing	-8.3%	-8.6%	-0.3%	2.7%	1.7%	-0.3%
Natural Resources and Mining	1.1%	-15.1%	3.1%	8.2%	8.1%	2.6%
Construction	-25.3%	-25.9%	-4.5%	1.9%	6.6%	3.0%
Trade, Transportation and Utilities	-5.7%	-5.4%	-0.3%	1.3%	0.4%	1.9%
Leisure and Hospitality	-3.8%	-3.8%	1.4%	2.7%	2.7%	3.0%
Education and Health Services	4.2%	3.0%	3.2%	3.3%	2.2%	2.9%
Professional and Business Services	-8.6%	-7.0%	0.9%	2.3%	4.4%	2.2%
Financial Activities	-4.6%	-3.4%	0.7%	2.8%	3.7%	5.1%
Other Services	-3.0%	-7.4%	-1.9%	-2.2%	0.2%	0.3%
Government	0.1%	-2.3%	-2.1%	-0.7%	0.6%	-0.7%
Information	-4.4%	-6.7%	-1.7%	5.7%	6.2%	2.0%

Source: Bureau of Labor Statistics (BLS) Current Employment Statistics
1. Calculated from seasonally unadjusted data; and
2. PY 2013 estimates are preliminary.

Although the Financial Activities sector had the most over-the-year percentage gains, this sector has a smaller, but steadily growing, employment base as shown in **Table 2**. As shown in **Table 2**, Arizona's large industrial sectors in descending order as of PY 2013 are Trade, Transportation and Utilities, Government, Education and Health Services, Professional and Business Services, Leisure and Hospitality, Financial Activities, Manufacturing, Construction, Other Services, Information, and Natural Resources and Mining.

Table 2: Program Year (PY) Employment by Industry in Arizona (in thousands)

Industry	PY 2008	PY 2009	PY 2010	PY 2011	PY 2012	PY 2013
Total Nonfarm	2528.3	2393.7	2394.0	2435.6	2490.5	2537.3
Manufacturing	163.6	149.5	149.0	153.0	155.5	155.0
Natural Resources and Mining	12.8	10.8	11.2	12.1	13.1	13.4
Construction	156.2	115.8	110.6	112.6	120.1	123.7
Trade, Transportation and Utilities	497.3	470.4	468.9	475.1	477.2	486.0
Leisure and Hospitality	263.1	253.0	256.4	263.3	270.5	278.7
Education and Health Services	329.1	339.1	350.0	361.6	369.5	380.4
Professional and Business Services	365.8	340.3	343.3	351.1	366.5	374.5
Financial Activities	173.9	168.0	169.1	174.0	180.4	189.6
Other Services	97.3	90.1	88.4	86.5	86.7	87.0
Government	429.7	419.9	410.9	408.0	410.3	407.5
Information	39.6	36.9	36.3	38.4	40.8	41.6

In May 2014, EPS forecasted a gain of 114,000 Nonfarm jobs over the two projected years of 2014 and 2015 for Arizona. An over-the-year gain of 53,500 Nonfarm jobs were projected for 2014 and a gain of 60,400 jobs for 2015. The rate of growth projected for Nonfarm employment in Arizona is 2.1 percent in 2014 and 2.4 percent in 2015. This would suggest flat growth in the rate of Nonfarm employment gains in 2014 compared to 2013. A slight increase in the rate is projected for 2015. The average annual growth rates in Total Nonfarm employment for Arizona, Phoenix MSA, Tucson MSA, and Balance of State are depicted in **Table 3** below.

Table 3: Forecasted Growth Rate in Arizona Nonfarm Employment

	2012[a]	2013[a]	2014[b]	2015[b]
Arizona	2.1%	2.1%	2.1%	2.4%
Phoenix MSA[1]	2.6%	2.8%	2.5%	2.6%
Tucson MSA[2]	1.5%	0.7%	1.2%	1.8%
Balance of State[3]	0.6%	0.2%	1.3%	1.7%

Notes:
1. Maricopa and Pinal counties
2. Pima County
3. Arizona less Maricopa, Pinal, and Pima counties
   a. Historical
   b. Forecast

In 2014, all regions are forecasted to have positive annual over-the-year growth rates in Nonfarm employment. Arizona is forecasted to grow at 2.1 percent in 2014. Phoenix is expected to grow faster than the state at 2.5 percent. However, the projected growth rates for Tucson (1.2 percent) and the Balance of State (1.3 percent) are slower than the statewide and Phoenix Metropolitan Statistical Area (MSA) rates. The expected Nonfarm job gains in 2014 for the Phoenix MSA are 44,600 jobs, for Tucson MSA are 4,400 jobs, and for Balance of State job gains are projected at 4,500 jobs.

Growth rates in 2015 are expected to be higher than 2014 across all regions. Phoenix is forecasted to continue growing at a faster pace (2.6 percent) than Tucson (1.8 percent), Balance of State (1.7 percent), and the state overall (2.4 percent). For 2015, the job gains forecasted for Phoenix MSA are 48,000 jobs, Tucson MSA 6,400 jobs, and Balance of State 6,000 jobs.

In Arizona, employment losses continued late into 2010 past the official end of the national recession in June 2009 as declared by the National Bureau of Economic Research (NBER). Net positive over-the-year gain started only since January 2011. The overall employment situation in Arizona is improving and expected to be better over the coming years. However, the forecasted rate of growth in Nonfarm employment in 2014 and 2015 is lower than what was observed prior to the recession (1997-2006 average of 3.4 percent).

The state's seasonally adjusted unemployment rate was 9.5 percent in May 2011 and has continually dropped through May 2014 as shown in **Table 4** below. The decline in the unemployment rate is an indication of an improving Arizona employment outlook. The U.S. unemployment rate has continued to decline from 9.0 percent in May 2011 to 6.3 percent in May 2014. The state has a higher unemployment rate compared to the nation as of May 2014.

Table 4: Unemployment Rate (Seasonally Adjusted) - End of Program Years

	May-11	May-12	May-13	May-14[(1)]
United States	9.0%	8.2%	7.5%	6.3%
Arizona	9.5%	8.4%	8.0%	6.8%
Phoenix - Mesa - Glendale	8.7%	7.4%	7.0%	6.0%
Tucson Metro	8.5%	7.4%	7.1%	6.3%
Flagstaff Metro	9.3%	8.2%	8.1%	7.0%
Lake Havasu City - Kingman - Metro	11.1%	10.0%	9.8%	8.2%
Prescott Metro	9.9%	8.7%	8.3%	6.50%
Yuma Metro	26.8%	27.0%	27.3%	25.9%

Note:
1. Preliminary data provided and is subject to change

Table 5 shows that the number of claimants receiving unemployment benefits in Arizona steadily increased in 2008 and 2009 in tandem with the negative trajectory of the employment environment, but has started a declining trend since 2010. From PY 2007 to PY 2008, the number of claimants increased by 99.6 percent, and from PY 2008 to PY 2009, the number of claimants increased by 33.2 percent. From PY 2009 to PY 2010, the number of claimants declined by 28 percent. From PY 2010 to PY 2011, the number of claimants declined further by 15.4 percent and continued this decline to 26.6 percent from PY 2011 to PY 2012. From PY 2012 to PY 2013, the number of claimants again declined, by 12.2 percent. Nonetheless, the average duration jumped from its level of 15.3 weeks in PY 2008 to its highest level of 19.2 weeks in PY 2010. Compared to the high level in 2010, the average duration has been on the decline, dropping to 17.6 weeks in PY 2011, 17.0 weeks in PY 2012, and 16.1 weeks in PY

2013. The number of persons receiving unemployment claims began declining as the economy starting recovering from the recession and went from a peak of 98,990 in PY 2009 to 38,832 in PY 2013.

Table 5: Claimants Receiving Unemployment Benefits in Arizona

	PY 2008	PY 2009	PY 2010	PY 2011	PY 2012	PY 2013
Average Number of Claimants per Month	74,292	98,990	71,313	60,300	44,236	38,832
Average Number of Weeks (Duration)	15.3	18.6	19.2	17.6	17.0	16.1
Percentage Over-the-Year Change	99.6%	33.2%	-28.0%	-15.4%	-26.6%	-12.2%

Note: Program years begin on July 1 of the given year and end on June 30 of the following year.
Source: Arizona Department of Economic Security