

# ARIZONA

## EMPLOYMENT GROWTH

2000-02

12

2000-05

2

Best=1 Worst=54

## RISK-ADJUSTED RETURN, '00-05

1.70%

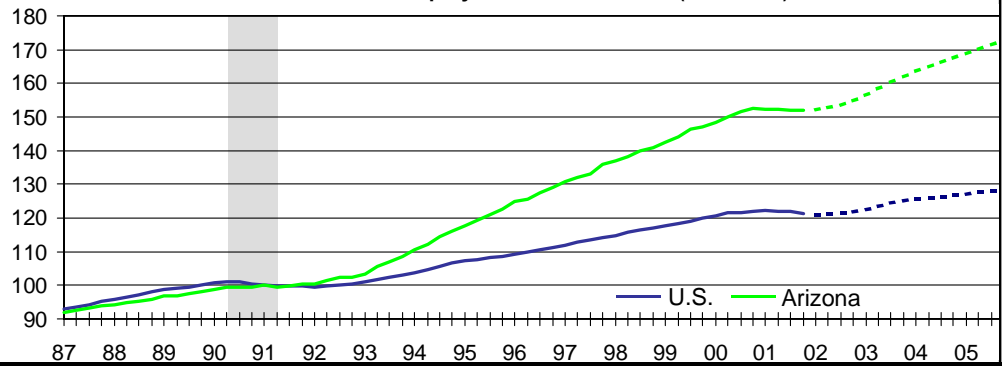
## COST OF DOING BUSINESS

U.S.= 100% 100%

## MOODY'S RATING

N/A

## Relative Employment Performance (1991=100)



1994	1995	1996	1997	1998	1999	2000	Indicators	2001	2002	2003	2004	2005
98.3	105.4	112.9	120.8	131.3	140.1	149.4	Gross State Product, C\$B	152.7	154.6	163.4	171.5	179.6
1,691	1,795	1,891	1,984	2,075	2,164	2,250	Total Employment (000)	2,271	2,290	2,379	2,472	2,550
6.7	6.1	5.4	4.9	4.6	4.3	4.0	% Change	1.0	0.8	3.9	3.9	3.2
6.4	5.1	5.5	4.6	4.1	4.4	3.9	Unemployment Rate	4.4	5.5	5.1	4.7	4.7
9.5	8.4	7.8	8.3	8.9	5.7	8.2	Personal Income Growth	5.1	4.3	6.9	7.3	6.7
4,243	4,427	4,577	4,721	4,860	4,994	5,131	Population (000)	5,265	5,395	5,535	5,694	5,847
141.7	146.5	110.9	102.8	98.8	94.1	95.0	Net Migration (000)	92.9	86.4	97.0	114.1	107.4
42,124	39,879	41,311	44,373	50,540	53,240	48,844	Single-Family Permits	49,181	45,039	47,342	46,055	46,238
9,708	12,835	12,404	13,389	13,390	11,869	12,641	Multifamily Permits	12,043	10,959	14,763	14,745	15,413
150.4	159.0	166.8	173.7	183.3	193.4	206.7	House Price Index (1987 = 100)	220.6	224.5	231.3	237.7	243.3
18,854	17,165	20,672	22,322	38,882	33,032	28,511	Mortgage Originations (\$M)	48,728	35,071	33,474	32,622	31,694
232.3	246.9	261.1	253.0	256.0	292.3	319.9	New Vehicle Registrations (000)	339.6	272.2	283.3	281.4	289.5
14,398	14,958	19,375	24,195	23,422	21,798	20,202	Personal Bankruptcies	23,931	25,959	23,889	22,151	22,272

## STRENGTHS & WEAKNESSES

### STRENGTHS

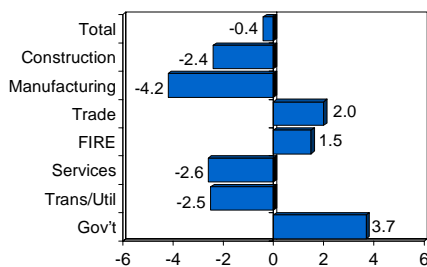
- Proximity to southern California markets attracts relocating businesses.
- The state benefits from NAFTA.
- Housing is affordable.
- Major center for low-cost high-tech manufacturing and back-office operations.

### WEAKNESSES

- The state has traditionally been a boom-bust economy.
- Low per capita income and high poverty rate.

## CURRENT EMPLOYMENT TRENDS

### October 2001 Employment Growth % Change Year Ago



## FORECAST RISKS

SHORT TERM ↑ LONG TERM ↑

### UPSIDE

- Defense contracts boost manufacturing activity in AZ.
- Stronger-than-expected snowbird traffic boosts winter tourism.

### DOWNSIDE

- One of AZ's embattled major employers, like America West, shuts down.
- Prolonged tech recovery forces more cutbacks in AZ's high-tech manufacturers.

## ANALYSIS

**Recent Performance.** Arizona's economy has run the entire course from being one of the fastest growing economies last year to one of the fastest declining ones now. Nearly all industries are contracting, with manufacturing and services both shrinking at a rapid pace. Retail trade and government growth are providing some support to the economy, but not enough to keep the state out of a recession. The jobless rate has shot up over the past few months, reflecting the still rising tide of layoffs.

**Technology.** AZ's important high-tech manufacturing industry continues to contract, even as the terrorist attacks and global economic slowdown have put off any chance of a quick recovery. All of AZ's high-tech manufacturers, including Motorola, Intel, and Qwest, have announced significant layoffs over the past few months, and the outlook for an imminent recovery in demand for chips remains poor.

Intel's performance in the state is indicative of the environment for AZ's tech manufacturers. On the one hand, Intel recently closed down its consumer gadgets division, with offices in Phoenix, due to slowing demand. On the positive side, Intel just opened its brand new \$2-billion Fab 22 chip manufacturing plant in Chandler, despite the slowing demand for chips. The new plant, which is expected to employ over 1,800 eventually, will give Intel a leg up on chip production when demand eventually rebounds.

**Tourism.** The state's tourism industry is expected to have lost \$200 million since the September 11 attacks, at a time when the state's tourism department is facing an almost \$400,000 cut in its budget due to fiscal constraints. In December, occupancy rates in Phoenix area hotels are down over 10%, while Tucson occupancy rates are almost 20% off last year's levels. Attendance in the Grand Canyon was down 21% in October. A proliferation of fears regarding further terrorist attacks will likely discourage many snowbirders from trav-

eling to AZ this winter. Since September 11, Tucson's hotels and conference centers have lost significant business through cancellations and rescheduling, not to mention lost revenues through unrealized retail and tourist spending in the area. An estimated 1,700 hotel workers in Tucson are facing job losses. December hotel bookings are weak, and overall winter bookings could be 15% below last year's levels.

**Defense.** The only redeeming factor for AZ is its strong military-industrial complex. The state is home to five major military bases, including the Army proving ground in Yuma, and the Davis-Monthan Air Force Base in Tucson. Together, the military is responsible for over 50,000 jobs in AZ, and has an estimated \$6 billion economic impact on the state.

The state's major defense players are hoping to capitalize on increased defense spending that might be coming down the pipeline, especially from the recently awarded Joint Strike Fighter contract. Phoenix-based Honeywell Avionics is expected to receive contracts worth \$5 billion in connection to the JSF contract and a \$1 billion contract recently from Airbus, a significant windfall that will benefit the company's plants in Phoenix and Tucson. Both Raytheon and Boeing also have defense units based in Arizona.

**While the near-term outlook calls for a mild recession in Arizona, the state is expected to remain an above-average performer over the long-term forecast horizon. Long term, the economy is well positioned to take advantage of the information economy. Arizona has a large and diverse base of high-tech industries, mostly in high value-added manufacturing. Further global economic integration will only improve AZ's outlook. AZ is attracting financial services jobs at the expense of high cost metro areas. This trend is expected to continue as financial services continues to consolidate.**

Rakesh Shankar  
December 2001

## EMPLOYMENT

### TOP EMPLOYERS

Honeywell International, Inc.	16,994
Motorola, Inc.	15,000
Banner Health System	12,850
Wal-Mart Stores, Inc.	11,730
Raytheon Missile Systems	10,300
The Kroger Company	10,135
Intel Corporation	10,000
America West Holdings Corporation	9,702
American Express Company	9,284
Safeway, Inc.	8,870
Wells Fargo Bank	8,722
Bank One Arizona Corporation	8,500
Qwest	7,500
Pinnacle West Capital Corporation	6,624
American Stores Company, Inc.	6,245
Albertson's, Inc.	6,104
Bank of America Arizona	5,994
Tosco Marketing Company	5,945
Bashas', Inc.	5,799
Walgreen Company	5,333

Source: The Arizona Republic - Arizona Inc., May 2001

### Public

Federal	48,333
State	87,711
Local	231,264

2000

### INDUSTRY EMPLOYMENT

Sector	AZ	U.S.
Mining	0.4%	0.4%
Construction	7.2%	5.1%
Manufacturing	9.6%	14.0%
Durable	77.2%	60.1%
Nondurable	22.8%	39.9%
Transport/Utilities	4.8%	5.3%
Wholesale Trade	5.0%	5.4%
Retail Trade	18.4%	17.6%
Finance, Ins, Real Estate	6.4%	5.8%
Services	31.9%	30.7%
Memo: Health Services	6.6%	7.7%
Government	16.3%	15.6%

Percent of total employment, 2000

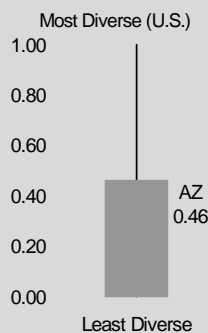
### LOCATION QUOTIENTS 5 Highest at 2-digit SIC Level

SIC	Industry	Location Quotient
10	Metal mining	10.11
07	Agricultural services	2.65
36	Electronic & other electric equip.	1.70
17	Special trade contractors	1.63
70	Hotels and other lodging places	1.44

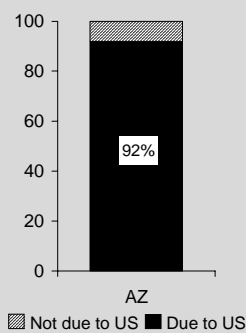
Economy.com Industry Services, 2000

## EMPLOYMENT AND INDUSTRY STRUCTURE

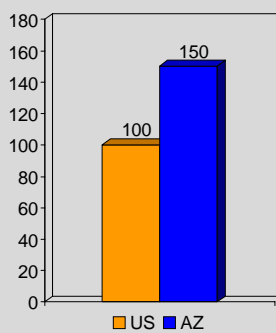
### INDUSTRIAL DIVERSITY



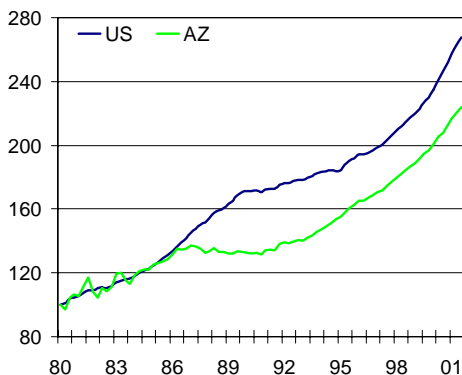
### EMPLOYMENT VOLATILITY DUE TO U.S. FLUCTUATIONS



### EMPLOYMENT VOLATILITY U.S. = 100



## HOUSE PRICES



Source: OFHEO, 1980Q1 = 100, NSA

## MERCHANDISE TRADE

### Exports by Destination

Country	Exports (Millions \$)	Share Total Exports %
World	15,712.1	100.0
Mexico	5,031.9	32.0
Canada	1,568.5	10.0
United Kingdom	971.8	6.2
Malaysia	952.7	6.1
Taiwan	677.4	4.3

### Exports by Commodity

Commodity	Exports (Millions \$)	Share Total Exports %
Total	15,712.1	100.0
Elec equip	6,724.1	42.8
Trans equip	2,580.6	16.4
Ind'l machines	1,578.2	10.0
Fabricated metal	869.1	5.5
Instruments	823.4	5.2

Source: MISER, 2000

## MIGRATION FLOWS

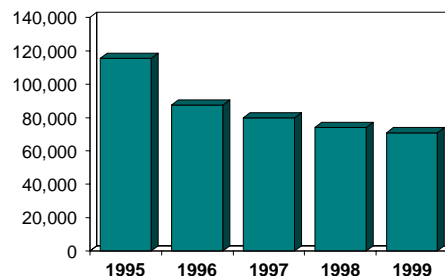
Into Arizona	Number of Migrants	Median Income
California	38,203	22,761
Texas	14,055	26,304
New Mexico	10,576	18,852
Illinois	9,715	27,506
Washington	9,491	24,949
Colorado	8,155	25,402
Nevada	6,392	23,435
Utah	5,675	22,837
Florida	5,462	23,062
New York	5,265	23,883
Immigration	191,560	22,884

### From Arizona

California	26,146	21,260
Texas	11,109	24,965
New Mexico	10,204	17,281
Colorado	8,073	23,281
Nevada	6,333	23,598
Washington	5,377	21,199
Florida	4,879	22,221
Illinois	4,369	22,567
Utah	4,081	18,405
Oregon	3,902	20,697
Outmigration	141,670	21,606

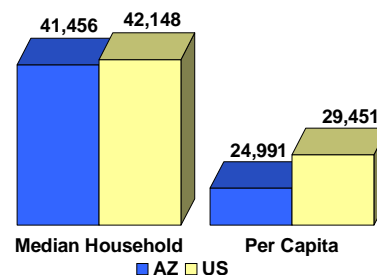
<b>Net Migration</b>	<b>49,890</b>	<b>1,278</b>
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### Net Migration, AZ



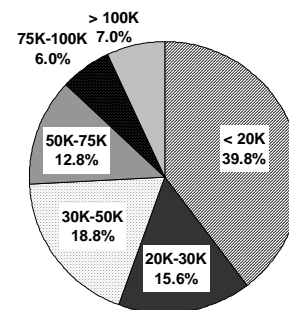
Source: IRS (top), 2000; Census Bureau, 1999

## INCOME



Source: Census, 2000 (household), BEA, 2000 (per capita)

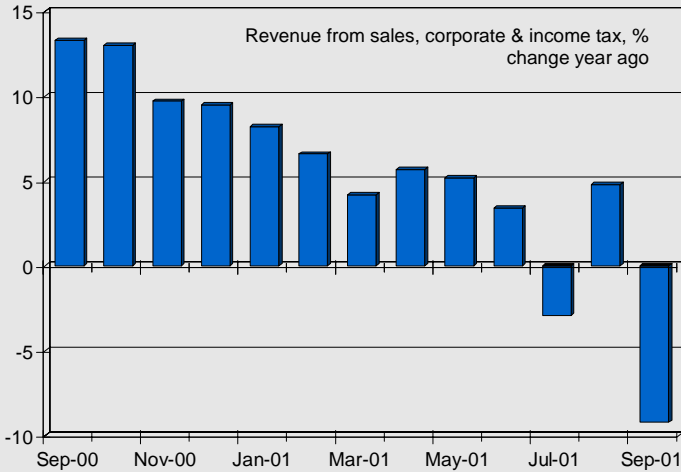
## INCOME TAX DISTRIBUTION



Source: Internal Revenue Service, 2000

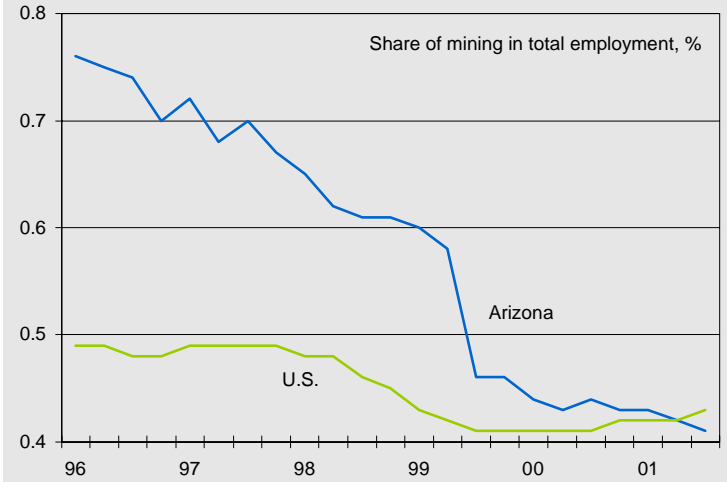
# Arizona

## Arizona's Fiscal Health Rapidly Deteriorating



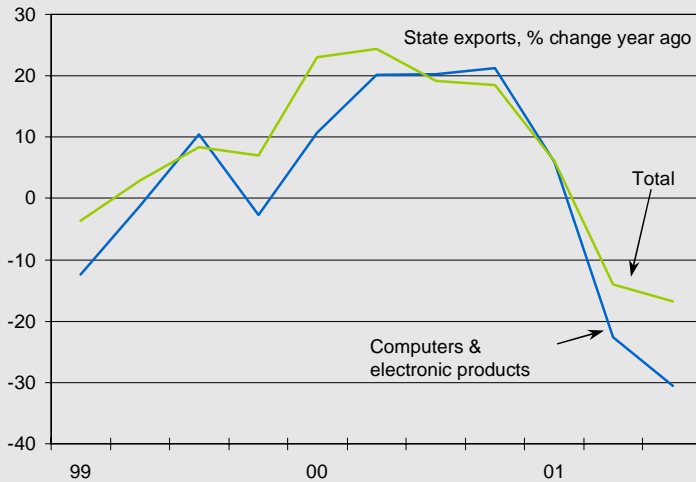
The rapid reversal of the state's fortunes is most evident in its deteriorating fiscal situation. Sales tax revenues were down \$31 million by the end of August, income tax revenues came in \$22 million below expectations. Currently, Arizona Governor Jane Hull expects the budget to be \$1.6 billion over the budget. State lawmakers are already discussing program cutbacks for the fiscal year totaling \$1.5 billion, with education and tourism facing the biggest cuts. Overall, most state government departments are expecting a 4% cut in funding.

## Mining Woes Worsen in Arizona



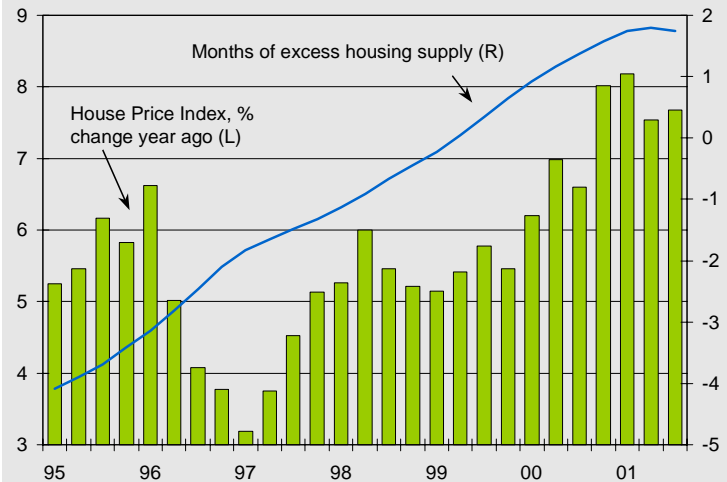
Citing slowing demand for copper and a weak pricing environment, the Phelps Dodge Company, the second largest employer in the Phoenix metro area and one of the largest in the state, announced plans to shut down mines in Miami AZ and cut back production at the Serrita and Bagdad mines in the state, cutting nearly 800 jobs. Although this is merely one further step in an industry that has long been a shrinking player in the state economy, the shutdown of the mines will hurt the regional economies in the southern and north-western parts of the state where the mine was the major employer.

## Exports Take a Dive



The worsening global economic downturn has taken its toll on AZ's exports. Dominated by high-tech products, AZ's manufacturers have had to contend both with declining domestic demand and with slumping foreign demand. Exports comprised nearly 10% of the AZ GDP in 2000, as opposed to little over 7% for the country as a whole, underscoring the importance of export for the local economy. AZ's exports are slanted inordinately towards Mexico and East Asia, particularly Malaysia, Hong Kong and Singapore. With both Mexico and East Asian mired in a recession, the outlook for AZ's exports remains weak.

## Housing Market Slowing But Healthy in Arizona



House price appreciation in AZ is moderating in the face of the slowing regional economy, even as housing supply begins to ease. This points to a healthy, imbalance-free housing market in the state. Demand for homes remains strong, with home sales in the state up a dramatic 15% for the third quarter. Speculative building is still being undertaken in Phoenix and Tucson, based on the healthy expectation that the metro area economies will rebound rapidly when the economic recovery enters full swing in 2002. Healthy demographic trends will ensure stable housing demand in AZ across the forecast horizon.