Published by the W. P. Carey School of Business at Arizona State University

NOVEMBER 2004 Volume 16, Number 4

BLUE CHIP ECONOMIC FORECAST

PHOENIX

W. P. CAREY SCHOOL of BUSINESS

The Greater Phoenix Area

ARIZONA STATE UNIVERSITY

Single-family setting records; commercial market improving

The single-family housing market will set new records this year. The unanticipated strength seems to be a function of a strong economy and low interest rates. Indeed, the 2004 forecast is for about 52,000 permits, or more than a 25 percent increase over 2003. Only minor declines are anticipated in 2005 and 2006. While the forecast for 2005 calls for an 8.5 percent decline, followed by another relatively small decline in 2006, those years would be strong by any historic standard.

The apartment market seems to be improving. The forecast for 2004, 2005 and 2006 shows more absorption than new units permitted, and vacancy rates dropping from 9.6 percent in 2004 to the mid-8 percent range by 2006. This would be a significant recovery for a market that has been troubled. As interest rates and median home prices move up, affordability for single-family housing could become more of an issue. Such a trend would help return the multi-family market to normal.

The same absorption dynamics are true for the office market. Absorption in 2003 exceeded construction for the first time since 1997. Absorption should exceed construction by nearly 500,000 square feet in 2004 and 2005, and by more than 600,000 in 2006. This would help take downward pressure off rents as vacancy rates decline from an anticipated 18 percent in 2004 to the mid-15 percent range by the end of 2006. Construction, which has been modest since 2003, is likely to remain relatively modest over the next couple of years.

The consensus is that the retail market will be relatively healthy, with construction and absorption balancing out over the next three years. Vacancy rates are likely to remain in the mid-8 percent range and new construction in the 3.5-to-4 million square-foot range.

According to the consensus, the industrial market will be the first to get back to normal levels of vacancy. Vacancy rates have dropped from 10.3 percent at the end of 2002 to a projected 9 percent at the end of 2004. Vacancies are expected to continue to decline to under 8 percent by the end of 2006. Once again, in that market, absorption would exceed construction in 2004, 2005 and 2006.

Overall, the commercial markets are improving as absorptions exceed new supply, thus allowing vacancy rates to decline. Single-family housing is expected to remain strong, albeit not as strong as this year.

— Elliott D. Pollack

" While the forecast for 2005 calls for an 8.5 percent decline [in single-family permits], followed by another relatively small decline in 2006, those years would still be strong by any historical standard. "

National economic slowdown is drag on metro area's growth

In the face of uncertain economic performance at the national level, the local economy continues to hold its own. However, those nationwide uncertainties mean the Greater Phoenix area is not faring as well as it normally would at this point in the economic cycle.

The Phoenix Metropolitan Statistical Area, which includes both Maricopa and Pinal counties, had the third fastest job growth among large MSAs in August, with its growth rate of 2.5 percent. Typically it would be reasonable to expect job growth somewhere in the 3 percent range at this point in the recovery.

Manufacturing job growth remains negative, primarily due primarily to continued weakness in semiconductors. It seems likely that the panel will have to further lower its manufacturing employment projections. The region also is experiencing weakness in information employment because of the continuing weakness in telecommunications. Manufacturing and information are the only two negative sectors, but many other sectors are growing more slowly than expected. Construction is the only sector growing faster than expected, and upward revisions to construction employment forecasts were the biggest change to the fourth quarter forecast.

The panel does not see inflation as a major problem despite the recent surges in energy prices. First, energy is a lower percentage of overall spending than it was during the energy crises of the ’70s and ’80s. Second the inflation-adjusted price of gasoline would have to be close to $3 a gallon to equal the constant dollar price for gas in the early eighties. Thus, the potential for oil price hikes to impact the local economy is lower than it used to be. The Phoenix metro area is lucky too in that the summer driving season is over and most Valley residents don’t spend much to hear their houses in winter — at least compared to most U.S. homeowners.

— Tracy Clark

GREATER PHOENIX ECONOMIC FORECAST FOR 2004

	ANNUAL PERCENT CHANGE 2004 FROM 2003							AVERAGE RATE FOR 2004	
SOURCE	Population	Personal Income	Retail Sales	Wage & Salary Empl.	Manufacturing Empl.	Construction Empl.	Services Empl.	National CPI	Unemployment Rate
Arizona Public Service	3.1 H	7.4	6.7	3.9	2.0	5.5	4.7	2.1	4.7
ASU – Bank One Economic Outlook Center	2.7 L	6.6	6.0 L	3.3	1.5	(3.5) L	5.8	1.8 L	4.8 H
CH2M HILL	2.8	6.6	6.2	3.3	2.4	1.5	4.4	2.4	4.6
Department of Economic Security	2.7 L	6.3	6.4	2.5 L	(2.0) L	3.5	3.7	2.4	4.6
ECON-LINC	2.9	6.2 L	6.5	2.6	0.0	10.0 H	3.3	2.4	3.8 L
EconLit LLC	2.7 L	6.5	6.2	3.2	2.0	0.0	4.2	2.5	4.0
Elliott D. Pollack and Co.	3.0	6.5	8.5	3.0	0.0	10.0 H	4.0	2.5	4.4
H.C. Reardon Economics	2.9	7.1	6.5	2.8	0.0	9.0	5.0	2.6	4.0
Joint Legislative Budget Committee	2.9	6.5	6.5	3.5	1.5	3.0	4.5	2.5	4.4
The Maguire Company	2.9	6.6	6.8	3.3	2.6	3.0	4.8	2.4	4.6
Protitlement	2.9	6.8	6.5	3.8	3.1	2.8	5.5	2.5	4.4
Salt River Project	3.0	6.8	9.0 H	3.0	0.0	8.0	3.0 L	2.7	4.2
U of A – Eller College	3.1 H	7.1	8.5	3.9	2.2	6.4	5.1	2.7	
VisionEcon	2.8	6.7	6.1	4.0	2.8	3.0	6.0 H	3.6 H	4.8 H
Consensus	**2.9**	**6.8**	**6.9**	**3.4**	**1.4**	**4.3**	**4.6**	**2.5**	**4.4**

GREATER PHOENIX ECONOMIC FORECAST FOR 2005

	ANNUAL PERCENT CHANGE 2005 FROM 2004							AVERAGE RATE FOR 2005	
SOURCE	Population	Personal Income	Retail Sales	Wage & Salary Empl.	Manufacturing Empl.	Construction Empl.	Services Empl.	National CPI	Unemployment Rate
ASU – Bank One Economic Outlook Center	2.8	7.0	6.6	4.2	2.6	(9.0) L	7.5 H	2.2	4.5 H
CH2M HILL	2.8	6.7	6.5	3.7	3.1	1.8	4.4	2.5	4.5 H
Department of Economic Security	2.6 L	7.1	6.5	3.2 L	1.1 L	3.4	4.5	2.5	4.4
ECON-LINC	2.9	6.5 L	6.6	3.8	3.0	(2.0)	4.3 L	2.5	3.8 L
EconLit LLC	2.8	7.0	6.6	4.0	2.4	2.5	4.6	2.6	3.8 L
Elliott D. Pollack and Co.	3.1	7.7	7.0	4.5	3.5	2.5	5.5	2.7 H	4.0
H.C. Reardon Economics	3.0	7.4	6.7	4.2	3.0	0.0	5.0	2.3	3.8 L
Joint Legislative Budget Committee	2.8	7.0	6.8	4.0	3.0	2.0	5.0	2.2	4.1
The Maguire Company	2.9	6.9	7.0	4.2	3.7	2.0	4.9	2.4	4.2
Protitlement	3.0	7.2	6.8	4.5	3.7	(1.0)	5.8	2.5	3.9
Salt River Project	2.9	7.5	8.0 H	4.5	4.0	1.0	5.0	1.8 L	3.8 L
U of A – Eller College	3.4 H	8.2 H	5.6 L	4.8 H	4.8 H	6.3 H	5.2	1.8 L	
VisionEcon									
Consensus	**2.9**	**7.2**	**6.7**	**4.1**	**3.2**	**0.8**	**5.1**	**2.3**	**4.1**

Data sources for Maricopa County (Greater Phoenix area): population, Arizona Department of Economic Security (DES); personal income, Bureau of Economic Analysis; retail sales, Arizona Department of Revenue; wage and salary employment, manufacturing employment, construction employment, service employment and unemployment rate, DES.

GREATER PHOENIX HISTORICAL DATA

SOURCE	Population (thousands)	Personal Income (millions)	Retail Sales (millions)	Wage & Salary Empl. (thousands)	Manufacturing Empl. (thousands)	Construction Empl. (thousands)	Services Empl. (thousands)	National CPI	Unemployment Rate
2003	3,382.0	$103,762.0	$32,132.0	1,576.6	126.9	128.6	627.4	184.0	4.9%
	2.8%	5.3%	4.7%	1.3%	(6.0)%	3.3%	2.7%	2.3%	
2002	3,289.0	$98,540.0	$30,690.0	1,556.9	135.0	124.5	610.8	179.9	5.6%
	3.0%	4.4%	0.3%	(0.2)%	(10.2)%	(1.7)%	1.0%	1.6%	
2001	3,194.0	$93,317.0	$30,605.0	1,559.5	150.3	126.7	604.5	177.1	3.9%
	3.1%	4.7%	1.5%	1.2%	7.5%	8.3%	19.2%	2.8%	

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST RESIDENTIAL

	2004				2005				2006			
	Single-family Permits	Multi-family Permits	Year-end Apt. Vacancy	Apt. Absorption	Single-family Permits	Multi-family Permits	Year-end Apt. Vacancy	Apt. Absorption	Single-family Permits	Multi-family Permits	Year-end Apt. Vacancy	Apt. Absorption
Arizona Public Service	49,500	4,300	9.0%	5,900	42,500	4,800	8.9%	4,700	43,400	4,900	8.5%	5,900
ASU Real Estate Center	45,000	4,200	9.0	4,000	38,500	4,500	9.0	4,000	35,000	6,000	8.5	6,000
CB Richard Ellis	55,000	5,500	9.4	4,900	59,000	5,500	8.6	6,200	58,000	6,000	8.2	6,500
Elliott D. Pollack & Co.	57,000	4,300	9.0	6,500	49,000	4,500	8.5	6,500	48,500	5,500	8.1	6,500
Griffin Consulting	47,400	4,800	9.5	5,250	44,000	5,300	9.0	6,550	41,000	5,600	8.8	7,250
Grubb & Ellis/BRE Comm.	52,000	2,000	9.5	3,500	50,000	2,000	9.0	3,800	45,000	2,500	8.5	4,500
Marcus & Millichap	N/A	N/A	9.2	4,537	N/A	N/A	9.0	4,990	N/A	N/A	N/A	N/A
Meyers Group	55,750	5,500	N/A	N/A	50,175	4,800	N/A	N/A	47,750	4,500	N/A	N/A
Protitlement	56,000	4,200	12.5	4,800	49,000	5,000	11.8	5,400	46,000	6,000	11.2	6,500
U of A, Eller College	53,500	6,122	N/A	N/A	49,190	5,669	N/A	N/A	49,113	5,816	N/A	N/A
Consensus	**52,350**	**4,547**	**9.6**	**4,923**	**47,929**	**4,674**	**9.2**	**5,268**	**45,974**	**5,202**	**8.8**	**6,164**
Actuals from ASU:					2002 year-end inventory: 899,077 (single-family) 325,311 (multi-family)							
2003 ACTUALS	39,652	4,836	9.6	3,702								
2002 ACTUALS	34,312	5,607	9.4	3,355								

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST OFFICE (Millions of Square Feet)

	2004			2005			2006		
	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption
Arizona Public Service	0.90	21.0%	1.20	1.10	19.5%	1.70	2.20	19.2%	2.00
CB Richard Ellis	0.80	16.2	1.80	1.30	15.8	2.20	2.30	14.1	3.00
Cushman and Wakefield	0.66	17.0	1.50	1.59	16.3	2.00	1.81	14.5	2.80
Elliott D. Pollack & Co.	1.00	17.0	1.70	1.50	16.0	2.00	1.50	15.2	2.00
Grubb & Ellis/BRE Commercial	0.95	19.0	1.00	0.80	18.5	1.40	1.20	17.2	2.00
Lee & Associates	1.11	17.1	1.10	1.01	15.5	1.75	0.93	13.8	1.75
Marcus & Millichap	0.92	18.3	1.64	1.08	17.8	1.21	N/A	N/A	N/A
PricewaterhouseCoopers LLP	1.00	17.0	1.20	1.50	15.2	1.70	1.20	15.2	1.20
Protitlement	0.80	19.5	1.40	1.00	17.6	1.80	1.40	16.5	2.20
Consensus	**0.91**	**18.0**	**1.39**	**1.21**	**16.9**	**1.75**	**1.57**	**15.7**	**2.12**
Actuals from Lee & Associates:				2003 year-end inventory: 54.8 million square feet					
2003 Actuals	1.08	18.7	1.32						
2002 Actuals	2.89	19.3	1.19						

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST RETAIL (Millions of Square Feet)

	2004			2005			2006		
	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption
Arizona Public Service	3.10	10.9%	2.50	4.20	11.6%	3.00	3.60	11.7%	3.10
CB Richard Ellis	5.00	6.5	5.70	6.50	7.0	5.50	5.00	6.1	5.80
Grubb & Ellis/BRE Commmercial	3.60	6.0	3.40	3.60	5.5	3.50	3.70	5.0	3.60
Marcus & Millichap	1.94	8.8	1.80	2.24	8.5	2.09	N/A	N/A	N/A
PricewaterhouseCoopers LLP	3.80	10.2	3.80	3.80	9.8	4.00	3.60	10.6	3.40
Protitlement	3.50	9.2	3.10	4.30	9.6	3.80	4.00	9.2	4.40
Consensus	**3.49**	**8.6**	**3.38**	**4.11**	**8.7**	**3.65**	**3.98**	**8.5**	**4.06**
Actuals from CB Richard Ellis:				2003 year-end inventory: 110.0 million square feet					
2003 Actuals	5.00	7.4	4.12						
2002 Actuals	3.89	7.3	3.04						

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST
INDUSTRIAL (Millions of Square Feet)

	2004			2005			2006		
	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption
CB Richard Ellis*	4.5	0.1	6.7	6.0	0.1	7.0	7.0	0.1	6.0
Cushman and Wakefield**	1.3	0.1	3.4	2.1	0.1	4.6	3.2	0.1	5.6
Grubb & Ellis/BRE Commercial**	3.2	0.1	6.0	4.5	0.1	7.1	5.6	0.1	7.8
Lee & Associates*	4.9	0.1	2.6	4.7	0.1	3.9	4.0	0.1	3.5
Consensus — Total Space	**3.5**	**0.1**	**4.7**	**4.3**	**0.1**	**5.6**	**5.0**	**0.1**	**5.7**

Actuals from CB Richard Ellis:	Construction	Leaseable Year-end Vacancy	Absorption
2003 Actuals Total Space	3.44	9.7	4.40
2002 Actuals Total Space	5.65	10.3	3.36
2001 Actuals Total Space	8.47	9.8	2.77
2000 Actuals Total Space	6.51	7.4	10.71

*All space over 5,000 sq. ft. **Total market (space over 10,000 sq. ft.)

2003 year-end inventory: 215.2 million sq. ft. (CB Richard Ellis)*
234.3 million sq. ft. (Cushman and Wakefield)**
222.8 million sq. ft. (Lee & Associates)*
233.0 million sq. ft. (Grubb & Ellis)**

REAL ESTATE FORECAST PANEL

Arizona Public Service
Pete Ewen

Arizona Real Estate Center
Arizona State University
Jay Q. Butler

CB Richard Ellis
Jeff Cooledge

Cushman and Wakefield
Stewart Park

Elliott D. Pollack and Co.
Elliott Pollack

Griffin Consulting
Brian J. Smargiassi

Grubb & Ellis / BRE Commercial
Jaime Weideman

Lee & Associates Arizona
Curt Czarsty and Josh Kohlhase

Marcus & Millichap
Jason Wong

The Meyers Group
Stu Burton

PricewaterhouseCoopers LLP
Tom Kabat

Protitlement
Steven Pritulsky

University of Arizona, Eller College
Marshall Vest

ECONOMIC FORECAST PANEL

Arizona Department of Economic Security
Donald Wehbey

Arizona Public Service Co.
Pete Ewen

Arizona State University
Bank One Economic Outlook Center
Tracy Clark

CH2M Hill
Kent Ennis

ECON-LINC
John Lucking

EconLit LLC
Dwight Duncan

H. C. Reardon Economics
Hank Reardon

Joint Legislative Budget Committee
Staff

The Maguire Co.
Alan Maguire

Elliott D. Pollack and Co.
Elliott Pollack

Protitlement
Steve Pritulsky

Salt River Project
Arlyn Herrera, Rebecca Holmes and Karen Wolfe

University of Arizona, Eller College
Marshall Vest

Vision Econ
Debra J. Roubik

W. P. CAREY
SCHOOL of BUSINESS

ASU

Bank One Economic Outlook Center

Tracy L. Clark, Economics Editor
Elliott Pollack, Topics Editor
Nancy A. Maneely, Editorial Coordinator

GREATER PHOENIX BLUE CHIP (ISSN 1042-6825) is published four times a year by the Bank One Economic Outlook Center, an affiliate of the L. William Seidman Research Institute in the W. P. Carey School of Business at Arizona State University. Rates: Print copy – one year (4 issues), $45.00; PDF (e-mail delivery) – one year, $39.00. For information, call the Bank One Economic Outlook Center at (480) 965–5543.

©2004 Arizona Board of Regents for Arizona State University. Reprint permission required from the Bank One Economic Outlook Center.

Arizona State University vigorously pursues affirmative action and equal opportunity in its employment, activities and programs.

• Not Printed or Mailed at State Expense •

Greater Phoenix Chamber of Commerce

www.phoenixchamber.com

Rich Boals, *Chairman*
Valerie Manning, *President/CEO*