

BLUE CHIP ECONOMIC FORECAST

PHOENIX



ASU W. P. CAREY
SCHOOL of BUSINESS
ARIZONA STATE UNIVERSITY

The Greater Phoenix Area

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Phoenix housing market: The worst is yet to come

The worst is yet to come for the Greater Phoenix housing market, according to the *Greater Phoenix Blue Chip* panel. Although 2007's estimate for single-family permits of 32,000 units is just about half of the total of only two years ago, another decline – to just above 30,000 units – is expected in 2008. The panelists anticipate a rebound in 2009 to around 36,600 units, about a 20 percent gain. This still would, however, be well below 2005 and 2006 levels. The diversity of the panel's opinion regarding 2009 single-family permits is substantial, with a range of permit estimates from 29,000 to 48,000 units.

The outlook for multifamily activity is more sanguine. Apartment permits should remain relatively stable with more than 5,500 permits this year, 5,600 permits in 2008 and 6,100 permits in 2009. Vacancy rates are also expected to stay relatively level at about 7.0 to 7.5 percent over that period. Interestingly enough, absorptions – which were actually negative last year –

are expected to be only slightly positive, at about 2,400 units this year, and more than 4,000 units in both 2008 and 2009.

The area's commercial markets have remained strong. However, weakness is expected past this year. After office construction of about 2.2 million square feet in 2006, the construction forecast jumps to 3.6 million square feet in 2007, and is anticipated to be roughly 3.3 million square feet in 2008. Office construction is then forecasted to fall off to about 2.2 million square feet in 2009. Absorption is expected to slow from 2.2 million square feet in 2006 to an estimated 1.9 million in 2007 and 1.6 million next year. Vacancy rates, which were 12 percent at the end of 2006, are expected to be closer to 14 percent by the end of 2007 and over 15 percent in the fourth quarters of 2008 and 2009.

The old adage of retail following rooftops continues to hold true, as a record amount of construction will take place in 2007 according to the panel's forecast. After 4.5

million square feet of retail construction in 2006, the panelists expect more than 8.6 million square feet to be built by the end of 2007. Retail construction is expected to slow to 7.4 million square feet for 2008 and 6.3 million square feet in 2009. Vacancy rates should stay in the 7 percent range for the forecast period.

The outlook for the industrial market, according to the panel, remains surprisingly strong. A record level of construction is expected in 2007, and most of the participants expect construction to remain strong in 2008 with only a modest drop in 2009. Vacancy rates are expected to increase over that period as absorption in each year is less than new construction.

Overall, the outlook remains less than favorable for the single-family residential markets throughout the forecast period. Although the outlook is positive for the commercial markets, 2007 will clearly be the peak of this cycle.

— Elliott D. Pollack

Weak housing market continues to weigh on economy

It is clear that the national, state and local economies have hit strong headwinds and that 2008 will continue the slowing trend we have already seen. It is not certain that the economic slowdown will officially be labeled a recession, but the practical difference between a recession and a significant slowdown is small.

We know that the slowdown in the housing market is finally making itself felt. Construction employment is falling and there has been a substantial drop in activity in the real estate market. Interestingly, the biggest impact of the housing slowdown that has showed up in the num-

bers so far is the drop in auto sales. Auto sales for Arizona started slowing in the latter part of 2006 and have been negative or flat since December of 2006. We don't have directly comparable data for the U.S. as a whole, but the survey-based data that is available suggests that while the growth of auto sales has slowed significantly, it has yet to go negative. Home owners are no longer able to extract equity from their houses – an activity that was potentially more widespread in markets like ours where price appreciation was rapid. The very high level of activity in the housing market also provided extra income to part-time real estate agents and some workers

in the mortgage industry, and income from rental housing. Dropping auto sales and slowing growth of other retail result in significant revenue shortfalls for state and local government.

The news is not all bad, with international exports likely to rise and some good prospects that oil prices will stabilize and eventually start to decline somewhat. The dollar has declined enough recently to encourage exports to trading partners in Europe, Canada and some other non-Asian countries. The dollar decline against Asian currencies has been much less pronounced.

— Tracy Clark

GREATER PHOENIX ECONOMIC FORECAST FOR 2007

SOURCE	ANNUAL PERCENT CHANGE 2007 FROM 2006							AVERAGE RATE FOR 2007	
	Popu- lation	Personal Income	Retail Sales	Wage & Salary Empl.	Manu- facturing Empl.	Construc- tion Empl.	Services Empl.	National CPI	Unem- ployment Rate
Arizona Department of Commerce	3.0	6.9	6.1	3.5	0.1	-10.0 L	4.1	3.1	4.3
Arizona Public Service	3.4 H	7.5	9.0 H	4.1 H	0.5	6.0 H	4.5	2.8	4.2
ASU - Economic Outlook Center	3.0	7.2	1.5 L	2.7 L	-0.1	-7.0	3.6	2.6	4.0
Department of Economic Security	3.4 H	7.1	6.2	2.7 L	-0.8	-0.9	3.5 L	3.1	3.1 L
ECON-LINC	3.0	7.0	6.0	3.2	-1.5 L	-5.0	3.5 L	2.6	3.5
EconLit LLC	3.0	7.2	6.8	3.7	1.2	-5.0	4.8	2.8	4.2
Elliott D. Pollack and Co.	3.2	7.0	2.5	3.5	-1.0	0.0	4.5	2.8	3.5
H.C. Reardon Economics	3.0	7.0	6.5	3.6	0.5	0.0	4.6	2.2	4.6 H
Joint Legislative Budget Committee	3.1	7.2	5.5	3.5	1.0	-5.0	4.5	2.7	4.0
The Maguire Company	3.1	7.6	7.4	4.0	2.5 H	0.0	5.0	3.2 H	4.1
Southwest Growth Partners	3.0	6.4 L	5.2	3.2	0.2	-6.0	4.2	3.0	4.2
Salt River Project	3.0	7.7	7.0	3.1	1.0	-3.0	4.2	2.1 L	4.0
U of A - Eller College	3.3	8.2 H	4.6	3.4	1.5	-5.7	5.4 H	2.7	
VisionEcon	2.9 L	6.7	6.3	3.1	1.6	4.0	4.5	2.7	4.5
Consensus	3.1	7.2	5.8	3.4	0.5	-2.7	4.4	2.7	4.0

GREATER PHOENIX ECONOMIC FORECAST FOR 2008

SOURCE	ANNUAL PERCENT CHANGE 2008 FROM 2007							AVERAGE RATE FOR 2008	
	Popu- lation	Personal Income	Retail Sales	Wage & Salary Empl.	Manu- facturing Empl.	Construc- tion Empl.	Services Empl.	National CPI	Unem- ployment Rate
Arizona Department of Commerce	3.0	6.8	6.4	3.3	-0.5	-5.0	4.0	2.9	4.4
Arizona Public Service	3.2	7.5 H	8.5 H	4.4 H	0.0	5.0 H	5.0 H	2.4	3.7
ASU - Economic Outlook Center	2.8	6.5	0.8 L	3.3	-0.5	-5.0	3.0	2.4	4.2
Department of Economic Security	3.3 H	6.7	6.5	1.8	-0.1	-4.9	2.9 L	3.0	3.3 L
ECON-LINC	2.8	6.8	5.8	3.0	1.0	-7.0	4.0	2.6	4.0
EconLit LLC	3.0	7.2	6.5	3.5	0.7	0.0	4.6	2.7	4.3
Elliott D. Pollack and Co.	2.7 L	6.0	1.5	2.0	0.0	-10.0	3.0	3.0	4.0
H.C. Reardon Economics	3.0	7.0	6.5	3.7	0.5	0.5	4.9	2.0	4.6 H
Joint Legislative Budget Committee	3.0	6.9	5.5	3.2	1.0	0.0	4.0	2.4	4.2
The Maguire Company	3.2	7.5 H	7.5	4.0	2.0 H	0.0	5.0 H	3.3 H	4.2
Southwest Growth Partners	2.9	5.8	4.6	2.8	0.0	-8.0	3.8	3.2	4.6 H
Salt River Project	3.0	7.3	6.8	3.0	1.0	-1.0	4.2	2.1	4.0
U of A - Eller College	2.8	5.0 L	2.5	0.7 L	-0.6 L	-15.4 L	3.3	1.8 L	
VisionEcon	2.7 L	6.3	6.7	2.2	1.0	0.0	4.0	2.7	4.6 H
Consensus	3.0	6.7	5.4	2.9	0.4	-3.6	4.0	2.6	4.2

Data sources for Maricopa County (Greater Phoenix area): population, U.S. Census Bureau; 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

	Popu- lation (thousands)	Personal Income (millions)	Retail Sales (millions)	Wage & Salary Empl. (thousands)	Manu- facturing Empl. (thousands)	Construc- tion Empl. (thousands)	Services Empl. (thousands)	National CPI	Unem- ployment Rate
2006	3,764	131,729*	43,821*	1,827.0*	134.0*	174.2*	744.8*	201.6	4.0*
	3.5%	8.4%	8.2%	4.8%	1.4%	6.8%	5.5%	3.2%	
2005	3,636	121,521*	40,500	1,743.1	132.2	163.1	706.0	195.3	4.1
	3.9%	9.4%	14.2%	6.2%	2.5%	15.8%	6.7%	3.4%	
2004	3,499	111,104	35,466	1,641.2	129.0	140.9	661.6	188.9	4.4
	3.2%	8.6%	9.6%	4.2%	0.5%	9.3%	5.6%	2.7%	

* Estimate

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST RESIDENTIAL

	2007				2008				2009			
	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
ASU, Realty Studies	33,400	5,000	7.0%	5,000	37,500	6,000	6.0%	6,000	43,600	7,000	7.0%	5,000
CB Richard Ellis	32,000	7,000	6.0%	4,000	26,000	8,500	6.3%	6,000	30,000	9,200	6.5%	6,000
Commerce Realty Advisors	31,000	6,000	7.0%	(1,000)	28,000	5,400	7.5%	500	30,000	5,800	8.0%	1,000
Elliott D. Pollack & Co.	32,000	6,000	8.0%	3,000	24,000	6,000	8.0%	6,000	29,000	5,000	8.0%	5,000
Griffin Consulting	34,500	4,700	7.5%	3,300	37,000	4,650	8.0%	3,500	48,000	5,300	6.5%	5,200
Grubb & Ellis/BRE Comm.	34,000	5,000	9.0%	(1,000)	37,500	4,500	8.5%	3,000	40,000	4,000	8.0%	5,000
Southwest Growth Partners	31,400	4,200	6.6%	3,800	27,000	3,800	6.8%	3,200	38,000	5,200	6.4%	4,400
U of A, Eller College	28,700	6,700	NA	NA	25,000	6,000	NA	NA	34,500	7,400	NA	NA
CONSENSUS	32,125	5,575	7.3%	2,443	30,250	5,606	7.3%	4,029	36,638	6,113	7.2%	4,514
<i>Actuals from Phoenix Housing Market Letter and ASU:</i>				2006 year-end inventory: Single-family: 1,027,634 Multifamily: 321,294								
2006 Actuals	42,423	3,922	5.3%									

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

	2007			2008			2009		
	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption
CB Richard Ellis	3.6	13.9%	1.3	3.0	16.6%	0.7	1.8	17.1%	1.1
Colliers International	4.9	12.9%	2.5	4.5	13.6%	2.3	2.5	13.2%	2.4
Cushman and Wakefield	4.0	14.2%	1.5	2.0	15.2%	1.0	2.0	15.4%	1.5
Elliott D. Pollack & Co.	3.5	13.0%	1.5	3.0	16.0%	1.0	1.5	17.0%	1.0
Grubb & Ellis/BRE Comm.	3.8	15.5%	1.8	3.5	15.0%	2.0	3.0	14.5%	2.3
Lee & Associates	2.3	15.0%	1.7	4.0	18.0%	1.5	1.5	17.0%	2.0
Southwest Growth Partners	3.4	12.2%	3.0	2.8	12.4%	2.6	3.0	12.0%	3.2
CONSENSUS	3.6	13.8%	1.9	3.3	15.3%	1.6	2.2	15.2%	1.9
<i>Actuals from Lee & Associates:</i>				2006 year-end inventory: 57.7 million square feet					
2006 Actuals	2.2	12.0%	2.2						
2005 Actuals	1.5	12.9%	4.2						

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

	2007			2008			2009		
	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption	Construction	Leaseable Year-end Vacancy	Absorption
CB Richard Ellis	10.6	6.6%	8.1	9.5	7.6%	7.4	7.4	7.5%	7.0
Elliott D. Pollack & Co.	10.0	6.5%	8.0	7.5	7.5%	7.0	6.0	8.0%	5.0
Grubb & Ellis/BRE Comm.	7.2	6.5%	6.0	6.8	6.0%	6.5	6.5	5.8%	6.3
Southwest Growth Partners	6.8	6.6%	6.2	5.8	6.8%	5.4	5.4	6.8%	5.4
CONSENSUS	8.7	6.6%	7.1	7.4	7.0%	6.6	6.3	7.0%	5.9
<i>Actuals from CB Richard Ellis:</i>				2006 year-end inventory: 126.3 million square feet					
2006 Actuals	4.5	5.1%	5.2						
2005 Actuals	6.5	5.3%	6.7						

METROPOLITAN PHOENIX REAL ESTATE CONSENSUS FORECAST INDUSTRIAL (Millions of Square Feet)									
	2007			2008			2009		
	Leaseable			Leaseable			Leaseable		
	Con- struction	Year-end Vacancy	Absorp- tion	Con- struction	Year-end Vacancy	Absorp- tion	Con- struction	Year-end Vacancy	Absorp- tion
CB Richard Ellis*	10.4	6.9%	8.2	12.4	8.2%	9.0	10.5	8.7%	8.1
Cushman and Wakefield**	10.3	7.3%	4.5	7.5	8.0%	5.0	7.5	8.7%	5.0
Colliers International**	6.4	7.9%	6.2	5.5	8.2%	5.4	4.9	7.9%	5.3
Grubb & Ellis/BRE Comm.**	9.0	8.5%	6.0	8.5	8.9%	6.3	6.5	8.6%	6.0
Lee & Associates*	8.5	7.8%	7.0	7.0	8.3%	6.0	6.8	8.0%	8.0
CONSENSUS - Total Space	8.9	7.7%	6.4	8.2	8.3%	6.3	7.2	8.4%	6.5
<i>Actuals from CB Richard Ellis:</i>				2006 year-end inventory: 237.5 million sq. ft. (CB Richard Ellis)* 248.2 million sq. ft. (Cushman and Wakefield)** 236.0 million sq. ft. (Colliers International) 240.0 million sq. ft. (Lee & Associates)* 249.0 million sq. ft. (Grubb & Ellis)**					
2006 Actuals Total Space	7.0	6.7%	6.0						
2005 Actuals Total Space	6.3	5.6%	12.3						
* All space over 5,000 sq. ft. **Total market (space over 10,000 sq. ft.)									

REAL ESTATE FORECAST PANEL		
Arizona State University Realty Studies Jay Q. Butler	Cushman and Wakefield Mark Urbanowicz	Lee & Associates Arizona Kyle Mecker Chris Seale
CB Richard Ellis Jeff Cooledge	Elliott D. Pollack and Co. Elliott Pollack	Southwest Growth Partners LLC Steve Pritulsky
Colliers International Stewart Park	Griffin Consulting Brian J. Smargiassi	University of Arizona Eller College Marshall Vest
CRA Ltd. Todd Vesledahl	Grubb & Ellis / BRE Commercial Mike Coover	

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