

AZB ARIZONA BUSINESS

ARIZONA STATE UNIVERSITY'S MONTHLY NEWSLETTER ON THE ARIZONA ECONOMY

Employment density highest in populous cities

Employment density in Arizona in 2001 was highest in the most populous cities of the Phoenix and Tucson urbanized areas and in the largest cities elsewhere in Arizona. In particular, the populous cities of Phoenix, Scottsdale and Tempe had large numbers of jobs given their numbers of residents.

A recently completed study of the economy of each incorporated city in Arizona, along with unincorporated areas and regions, was introduced in the July 2004 issue of *AZB/Arizona Business*. This study was performed by the Center for Business Research under contract to the Arizona Department of Commerce. The 125 reports produced for this project, along with the datasets, are available from the Department of Commerce's Web site: www.commerce.state.az.us (click on "Economic Info & Research" then on "Arizona Community Economic Base Studies").

INCORPORATED AND UNINCORPORATED AREAS

Because of the unavailability of economic data by city, zip code data were used in this study. Thus, the geographical boundaries of the incorporated places as defined for this study are considerably different from the actual boundaries. In particular, the zip code area of some cities includes considerable unincorporated area. Arizona has 88 incorporated cities, but in six cases two adjacent incorporated cities had to be combined because the zip code boundaries were considerably different from city boundaries. Thus, an economic base study was completed for 82 incorporated areas.

In order to compare areas of unequal size, employment per 1,000 residents was calculated. In general, employment per 1,000 residents was highest in the most populous cities (population of more than 100,000) of the Phoenix and Tucson urbanized areas and in the largest cities (population of more than 20,000) outside these two major urbanized areas. The lowest employment per 1,000 residents was in the smallest cities (less than 5,000 residents) and in unincorporated areas. Employment per 1,000 residents also was below average in cities of less than 100,000 residents in the two major urbanized areas, which tend to be at some distance from the urban center and largely are "bedroom communities." In each category, however, employment density ranged widely by city.

Only 17 of the 82 incorporated places had a figure greater than the state average of 457 jobs per 1,000 residents. However, three highly populous cities had

per capita employment far above the Arizona average — Phoenix (625 jobs per 1,000 residents), Scottsdale (690), and Tempe-Guadalupe (1,081) — and Tucson-South Tucson also had an above-average figure (487).

The state's employment per 1,000 residents was 8 percent less than the national average. The figure was greater than the national average of 505 in only 11 incorporated places: Clifton (626), Flagstaff (540), Hayden (1,344), Jerome (708), Paradise Valley (895), Phoenix (625), Prescott (557), Scottsdale (690), Sierra Vista (517), Tempe-Guadalupe (1,081), and Tolleson (1,167).

In contrast, employment per 1,000 residents in several cities was only 40 percent or less of the state average (a figure of 183 or lower). Apache Junction, El Mirage and Surprise in the Phoenix area and Oro Valley in the Tucson area had such low figures. Elsewhere in the state, six of the nine cities with such low figures are located in the mining region and all nine had a population of less than 5,000.

Average payroll per nonfarm private-sector employee generally was greatest in the two major urbanized areas and lowest in the least-populous places. However, unincorporated areas generally had somewhat higher averages than most of the smaller cities.

In only nine of the 82 incorporated places was average payroll per nonfarm private-sector employee greater than the state average. Seven of the nine cities are in the Phoenix urbanized area, including the highly populous cities of Chandler, Phoenix, Scottsdale and Tempe-Guadalupe. Average payroll per private-sector employee was greater than the national average in only three incorporated places: Chandler, Scottsdale, and Tolleson. The state's average was 13 percent less than the national average.

The state's unincorporated territory (other than that included in zip codes assigned to incorporated cities) was divided into 32 areas for this project. Just two of the 32 unincorporated

Economies of Arizona's Communities

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areas had an employment-per-1,000-residents figure greater than the state and national averages: the Salt River-Fort McDowell Indian Reservations near Scottsdale and Fountain Hills and part of unincorporated Coconino County (which includes the Grand Canyon). Average payroll per nonfarm private-sector employee was greater than the state average in only three: the nonreservation unincorporated area of the mining region, the southwestern portion of unincorporated Yavapai County (which includes the copper mine in Bagdad), and the Kayenta area (which includes coal mines). Only the latter's average was greater than the national average.

ECONOMIC REGIONS

As part of the Arizona Statewide Economic Study produced by the Arizona Department of Commerce in 2002-03, Arizona was geographically split into 11 economic regions:

- **Canyon:** the portions of Coconino and Mohave counties north of the Colorado River, including Page.

- **Central:** Maricopa and western Pinal counties.

- **Mining:** Southern Gila, Graham, Greenlee, and eastern Pinal counties.

- **Mountain:** Part of Coconino County (excluding the portion north of the Colorado River, the Hopi and Navajo reservations, and the Sedona area) and the Winslow area of Navajo County.

- **Navajo/Hopi:** The Hopi and Navajo reservations in northern Apache County, northeastern Coconino County, and northern Navajo County.

- **North River:** Part of Mohave County (excluding the portion north of the Colorado River) and the Parker area of La Paz County.

- **Plateau:** Southern Apache, northern Gila, and southern Navajo counties.

- **South River:** Part of La Paz County (excluding the Parker area) and Yuma County.

- **Southeast:** Cochise and Santa Cruz counties.

- **Southern:** Pima County.

- **Yavapai:** Yavapai County and the Sedona area of Coconino County.

The land area shown in Table 1 is less than the actual amount (the 94,730-square-mile land area of the 11 regions combined is 17 percent less than the state total of 113,635 square miles). Unsettled and very sparsely settled areas are not associated with any mail delivery route and therefore were not tabulated by the Census Bureau in numbered zip code tabulation areas in the 2000 census, which is

the source of the population and land area data. (The combined population of the 11 regions is nearly identical to the state's 2000 census count.) The population in the central and southern regions — the Phoenix and Tucson areas — was much more than the number of residents of the other regions, all but one of which had a 2000 population between 85,000 and 170,000. Similarly, employment varies between 21,000 and 62,000 in most regions, far less than the numbers in the two highly populous regions. The employment in the 11 regions combined is nearly equal to the wage and salary employment for the state reported by the U.S. Department of Commerce, Bureau

of Economic Analysis.

Employment per 1,000 residents was less than the national average of 505 in all regions, though the shortfalls in the central and mountain regions were minimal. Each of the other nine regions had a figure less than the state average.

Similarly, in each region average nonfarm private-sector payroll per employee was less than the national average [see Figure I]. The central region was the only region with a figure greater than the state's average.

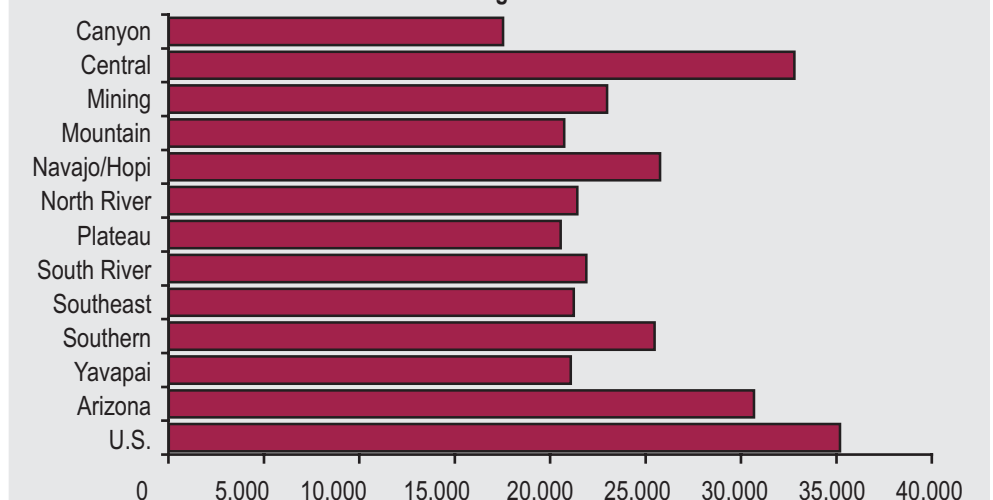
— **Tom R. Rex**
Research Manager

TABLE 1
ARIZONA'S ECONOMIC REGIONS

Region	2000 Population	Land Area (Square Miles)	2001 Employment	Employment per 1,000 Residents
Canyon	17,442	3,939	6,226	357
Central	3,227,416	9,606	1,616,546	501
Mining	85,351	8,558	24,858	291
Mountain	94,896	8,518	46,137	486
Navajo/Hopi	105,488	17,691	21,048	200
North River	159,389	5,870	48,439	304
Plateau	95,264	9,756	31,119	327
South River	168,547	5,096	61,884	367
Southeast	160,245	8,835	60,603	378
Southern	846,103	9,052	368,645	436
Yavapai	170,324	7,809	58,853	346
Sum of Regions	5,130,632	94,730	2,344,358	457

Source: Population and land area from U.S. Department of Commerce, Census Bureau, 2000 census. The land area shown in this table understates the actual total (113,635 square miles in Arizona). Employment estimated from U.S. Department of Commerce, Census Bureau, *Zip Business Patterns 2001* and estimates of agriculture and government employment.

FIGURE I
AVERAGE NONFARM PRIVATE-SECTOR PAYROLL PER EMPLOYEE IN 2001
Economic Regions of Arizona



Note: The average is estimated due to the payroll for some zip codes being withheld by the Census Bureau to meet disclosure restrictions. The payroll was not disclosed in a high proportion of the zip codes in the mining region.

Source: Estimated from U.S. Department of Commerce, Census Bureau, *Zip Business Patterns 2001*.

Housing affordability declines in second quarter

In the midst of a lackluster economic environment, the single-family market continues at a torrid pace. With 44,760 recorded sales in second quarter 2004, the local housing market shattered the 33,425 second-quarter record in 2003. Two fundamental factors appear to be the driving forces. The first is the threat of ever-higher interest rates. The second is the fact that homes are an increasingly popular form of investment.

While the current level of activity indicates a market of continued potential, there is mounting concern that the housing market will begin to slow later this year — when potential homeowners with stagnant incomes are faced with higher home prices and mortgage rates. Basically, the housing market could be limited by the inability of potential buyers to afford any changes in their current housing situations.

RESALE SINGLE-FAMILY HOMES

With 28,760 recorded sales, the Greater Phoenix resale home market was well above the previous record of 20,560 sales set in second quarter 2003 and the 19,460 sales for the initial quarter of 2004. The second quarter brought increasingly stronger months, from 7,250 sales in April to 9,845 in May to a record 11,665 in June.

Median resale home prices ranged from \$97,500 (160 sales) in the Sky Harbor area \$919,000 (215 sales) in Paradise Valley. Active areas were: Mesa with 3,240 sales

(\$153,450 median price), Deer Valley with 2,600 (\$202,000), Glendale with 2,220 (\$155,000), and North Scottsdale with 2,120 (\$420,000). The median square footage for a resale home increased from last year's 1,670 to 1,700.

NEW SINGLE-FAMILY HOMES

Based on a strong June (3,720 sales), the new home market set another quarterly record at 9,845 sales, breaking the previous record of 9,270 sales for fourth quarter 2003. (In the resale market, strong activity typically is expected in the second quarter, while the fourth quarter tends to be strongest for the new home market.)

The West Valley communities represented 26 percent of the Greater Phoenix new home market. A big reason for this growth is the greater affordability of new homes in the West Valley. The following examples illustrate the disparity: In the East Valley, the median price in Gilbert is \$210,210 for a 2,980-square foot home and in Mesa, \$207,990 for 2,290 square feet. In the West Valley, the median price is \$157,450 for a 1,720 square foot home in Avondale and \$130,835 for 1,505 square feet in El Mirage.

With 80 percent of the 180 new home sales priced in excess of \$300,000, North Scottsdale had a median sales price of \$537,949; the lowest was \$130,835 in El Mirage, based on 75 sales. Other active

markets were: Deer Valley with 1,000 sales (\$262,305 median price), South Phoenix with 975 (\$146,425) and Superstition Springs with 325 (\$203,560).

The median square footage for a new single-family home recorded sold in second quarter 2004 was 2,130, slightly smaller than the 2,275 square feet reported a year ago.

TOWNHOUSE/CONDOMINIUMS

Both investors and occupying owners recognize the advantages of the low maintenance, recreational facilities and security offered by the townhouse/condominium housing style. The median sale price for resale units increased from \$85,000 in first quarter 2000 to \$113,000 in second quarter 2004. However, even with the rapid increase, the median price represents only 66 percent of that for single-family homes. Despite higher prices, sales activity in the second quarter set a record at 5,515 sales, breaking the previous one set a year ago (4,165 sales).

Many of the newer developments are at the high end of the market; the median price of \$177,250 for new units represents 93 percent of the \$190,745 for new single-family homes. The primary reason is that 34 percent of the 640 sales were in North Scottsdale, at a median price of \$250,900. Other active areas were Superstition Springs (90 sales, \$129,415), Union Hills (70 sales, \$219,380) and East Mesa (50 sales, \$125,380).

TABLE 1

HOUSING AFFORDABILITY INDEXES Greater Phoenix, Single-family Only

Quarter	Resale Homes					New Homes		
	Median Gross Monthly Income	Effective Interest Rate	Median Sales Price	Monthly Housing Payment	Affordability Index	Median Sales Price	Monthly Housing Payment	Affordability Index
First Quarter 2002	\$4,000	6.9	\$139,700	\$920	122	\$158,015	\$1,040	108
Second Quarter 2002	4,020	6.6	144,000	920	122	155,250	995	114
Third Quarter 2002	4,030	6.2	146,000	895	126	159,535	975	115
Fourth Quarter 2002	4,040	6.0	147,000	880	128	164,540	990	115
First Quarter 2003	4,050	5.7	148,750	865	131	163,545	950	119
Second Quarter 2003	4,060	5.4	155,000	870	131	176,085	995	115
Third Quarter 2003	4,060	5.9	159,500	945	120	173,895	1,030	110
Fourth Quarter 2003	4,075	5.7	155,800	905	126	177,820	1,030	111
First Quarter 2004	4,075	5.4	159,705	900	127	180,510	1,015	113
Second Quarter 2004	4,095	6.0	170,000	1,020	112	190,745	1,145	100

Source: Arizona Real Estate Center, L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University.

In the resale townhouse/condominium sector, the median square footage is 1,160, which is slightly smaller than the 1,175 reported a year ago. The most active resale areas were North Scottsdale with 785 sales (\$198,000 median price), South Scottsdale with 600 (\$128,700), Sun City/Peoria with 390 (\$85,000) and South Mesa with 360 (\$94,000).

AFFORDABILITY

In light of an improving economy and heightened inflationary concerns, a common concern throughout the quarter was that the Federal Reserve would begin to raise interest rates. In response to these expectations, 30-year mortgage interest rates rose from 5.1 percent in March to 5.9 percent in June. Since low or declining interest rates were the most commonly prescribed stimulant for the housing market, increasing rates were perceived as a suppressant. Before interest rates could rise higher, people moved quickly to satisfy their housing expectations of investment wealth, larger size or better location.

As demand heightened, the supply of homes began to lessen as the number of listings declined from nearly 25,000 at the beginning of the year to under 20,000. This classical struggle of demand and supply resulted in a record median price of \$170,000 for a resale home. This price greatly exceeded the previous record set in first quarter 2004 (\$159,705) and last year's \$155,000. In new homes, the median price also set a record at \$190,745, up from

\$180,510 in first quarter 2004 and \$176,085 a year ago.

While home prices have been soaring, anemic job growth and low inflation have combined to limit growth in the median household income. Thus, affordability took a big tumble during the quarter.

The resale affordability index fell from 127 in the first quarter to 112, which was last seen in second quarter 2000 (based on an effective interest rate of 8.2 percent, median price of \$130,000 and a monthly median household income of \$3,880). The new home affordability index value followed a similar pattern, dropping from 113 to 100, which was last seen in third quarter 2000 with an effective interest rate of 7.8 percent, a median new home price of \$151,525 and a monthly median household income of \$3,910.

The concept of affordability is wide-ranging, affecting potential homeowners of all income levels. The affordability index is based on the ability of a median-income family to afford a median-priced home. An index value of 100 means the typical home buyer would be able to afford a median-priced resale home at an effective interest rate of 7.1 percent, based on the current median resale price and household income. Although a lower index value indicates less affordable homes, it does not take into account alternative housing forms such as townhouse/condominiums or manufactured housing.

Since home prices and incomes vary throughout the Valley, so does the affordability index. For example, in the resale sector, the second-quarter 2004 index was 64 in Scottsdale, 118 in the Surprise area, 118 in the Mesa area and 132 in the Avondale area.

In order to buy a home, the household has to have both the needed income and wealth. The monthly income from jobs and investment is needed to pay the monthly mortgage payment and associated costs such as utilities and maintenance. The wealth from savings, equity in current home, gifts or investments is needed to provide the required down payment. While income can be a major issue, the wealth creation is frequently the biggest problem for home buyers, especially for young or minority households. This is especially true for first-time home buyers, because current homeowners can use their built-up equity to purchase their next home.

Based on the median-income household headed by a person under 25 years and with a 5 percent down payment, the affordable home is priced at \$102,000. This and lower-priced homes represented only 10 percent of the resale single-family homes recorded sold, but 39 percent of the recorded townhouse/condominium transactions. If this same household could put down 20 percent, then the affordable home price is \$122,000, which represents about 10 percent of the market in the second quarter.

TABLE 2
GREATER PHOENIX HOME SALES

Median Sales Price	Single-family			Townhouse/Condominium			Grand Total
	Resale	New	Total	Resale	New	Total	
First Quarter 2003	\$148,750	\$163,545	\$153,610	\$101,000	\$180,000	\$107,000	\$148,380
Second Quarter 2003	155,000	176,805	160,000	103,375	181,835	109,000	154,000
Third Quarter 2003	159,000	173,895	163,785	103,000	188,690	108,620	158,000
Fourth Quarter 2003	155,800	177,820	163,995	105,000	187,775	110,500	158,240
First Quarter 2004	159,705	180,510	165,585	110,000	161,910	115,000	160,000
Second Quarter 2004	170,000	190,745	175,500	113,000	177,250	117,500	168,200
<i>Number of Sales</i>							
First Quarter 2003	15,030	7,125	22,155	3,215	355	3,570	25,725
Second Quarter 2003	19,845	7,680	27,525	4,165	470	4,635	32,160
Third Quarter 2003	20,560	8,630	29,190	3,745	500	4,245	33,435
Fourth Quarter 2003	18,350	9,270	27,620	3,565	500	4,065	31,685
First Quarter 2004	19,460	8,135	27,595	3,765	575	4,340	31,935
Second Quarter 2004	28,760	9,845	38,605	5,515	640	6,155	44,760

Source: Arizona Real Estate Center, L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University.

The highest median household income is associated with those in the 45-54 age bracket, which is also the group that is looking for move-up homes. Based on the median household income (\$64,140) and a 20 percent down payment, the affordable home for this group is \$265,000, which represents about 5 percent of the resale market in second quarter 2004. But if this household was to make only a 10 percent down payment, then the affordable home becomes \$235,000.

For a household earning 80 percent of the area's median income and placing a 5 percent down payment, the affordable home becomes \$137,000. For those households at 120 percent of median income and using a 25 percent down payment, the affordable home is at \$260,000. Thus, the affordable home is influenced not only by household income, but also wealth base.

LOOKING AHEAD

Although the home-buying appetite seems insatiable, there are mounting concerns about the continuing strength of this market. In the last year, the housing market has performed well above its historical norms. Since 1982, the resale home market in the second quarter averaged 5 sales per 1,000 population; currently it is at 7. While the increase is due in part to the transition of more people from renters to owners, some may be attributed to home buying for investment purposes.

In the late 1980s, a similar surge was driven by declining interest rates and a fairly strong economy, but it could not be sustained. The appreciable decline that was so evident in the early 1990s probably will not occur this time around because monthly payments are relatively low, and the economy is recovering rather than entering a decline as it was then.

As with any increase in demand, the strong increase in prices — while attractive for homeowners — makes it increasingly difficult for people to afford their first home or even to improve significantly on their current housing. In a time of potentially higher mortgage rates, the ability to support higher home prices is reliant on the household income. While job growth is becoming increasingly evident, the fundamental issue is whether the new jobs will provide the careers and opportunities for advancement that will translate into greater and sustainable income to support the housing market. Even with existing jobs, pension and health-care costs are increasingly being

shifted onto the employee, which affects a household's ability to purchase and maintain a home.

Over the last few years, low interest rates have enabled people to fulfill their respective housing dreams, whether for ownership or for a specific type, size or location. Higher interest rates combined with higher home prices provide little incentive for people to move out of their current homes, thus providing additional stimulus to the market and the economy. Since some of the current purchases are being financed by adjustable-rate mortgages, higher interest rates could impact the ability of some to retain their homes.

If the effective interest rate was the same as in 1990 (10.5 percent), the current median-income household could afford a home priced at only \$125,000 or less. This price-income ratio is the fairly typical 2.5, while the current ratio is 3.5. The low mortgage rates have allowed households to significantly upgrade their housing and support the ever appreciating home prices.

With housing representing a greater pressure on the household income, it is important that either or (preferably) both forces continue: increasing income and home prices. Higher income allows the household to support its purchase, while higher home prices allow the household to make a profit at sale, or to refinance.

Although events of the early 1990s are not expected to repeat themselves, the high interest rates that were the remnants of the 1980s showed what can happen to a housing market when a depressed economy significantly lowers a household's income. Even with low interest, the high rates of foreclosure and bankruptcy show that some households are struggling to maintain their homes.

The investor market also could become subject to economic pressure. If investors

are struggling to maintain their rental properties or if they do not foresee the needed appreciation, they would become more likely to sell their investments. Thus, there is the possibility that the housing market will find itself under significant pressure as people, whether owner-occupants or investors, work to reduce the pressure on their incomes.

The Greater Phoenix area has grown by providing jobs and affordable housing to a diverse population. The growth is especially evident in the residential development of the West Valley communities and Pinal County. Since many of the communities are a distance from employment centers, the increasing pressure on the freeway system and higher energy costs make it even more important for the "newer" areas to advance beyond bedroom communities to more economically diverse ones.

All of these factors lead to the conclusion that there are no certainties regarding the future of the Greater Phoenix housing market. In fact, the market is tied directly to the area's ability to create and sustain jobs that pay well and offer advancement potential.

— Jay Q. Butler
Director

Arizona Real Estate Center

TABLE 3
GREATER PHOENIX AREA AFFORDABLE HOME PRICE
By Level of Income (\$4,095*) and Down Payment**

	5 Percent Down Payment	15 Percent Down Payment	25 Percent Down Payment
Household Median Income (HMI).....	\$171,000	\$192,000	\$215,000
80 Percent of HMI.....	137,000	153,000	174,000
120 percent of HMI.....	205,000	230,000	260,000

* Median gross monthly income as shown in Table 1.

** Effective Interest Rate of 6.0 percent.

Source: Arizona Real Estate Center, L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University.

Economic expansion continues

National economic growth accelerated in mid-2003. Gains in national employment accelerated further in 2004 following an unusually long and slow recovery period. Growth rates in most national economic indicators in 2004 are typical of the expansionary phase of the economic cycle, even with the somewhat slower growth registered in early summer.

Economic growth also accelerated in mid-2003 in Arizona. In mid-2004, however, advances in measures such as employment and personal income remained below the rate of earlier economic expansions. While aggregate growth rates in Arizona exceeded the national average, the differential was less than is typical during an expansionary period.

The latest income and earnings data from the U.S. Bureau of Economic Analysis are for first quarter 2004. This was the fourth consecutive quarter of inflation-adjusted per-person gains in personal income and earnings following a more than two-year period of mild decreases [see Figure I]. Nationally, growth over these four quarters totaled about 2.5 percent — similar to annual gains in the early years of the prior economic expansion, but considerably less than the advances during the second half of the expansion. Real per capita growth rates in Arizona were nearly identical to the national average over the last four quarters. As ratios to the national averages, per capita personal income and earnings in Arizona remained at cyclical lows, 16 percent below average on personal income and 18 percent less than average on earnings.

In the first 21 months after the official end of the recession in November 2001, the nation's employment decreased in most months [see Figure II], falling by more than a quarter million over this "recovery" period. Modest increases averaging 81,000 per month followed from September 2003 through February 2004 before employment gains reached a more typical expansionary rate of 256,000 per month from March through June 2004. Even at this accelerated pace, it would be mid-2005 — more than 3.5 years after the end of the recession — before the nation's employment regained the early 2001 level that preceded the recession. In comparison, in the early 1980s, employment regained its prerecessionary high just 12 months after the end of the recession; it took 23 months in the early 1990s.

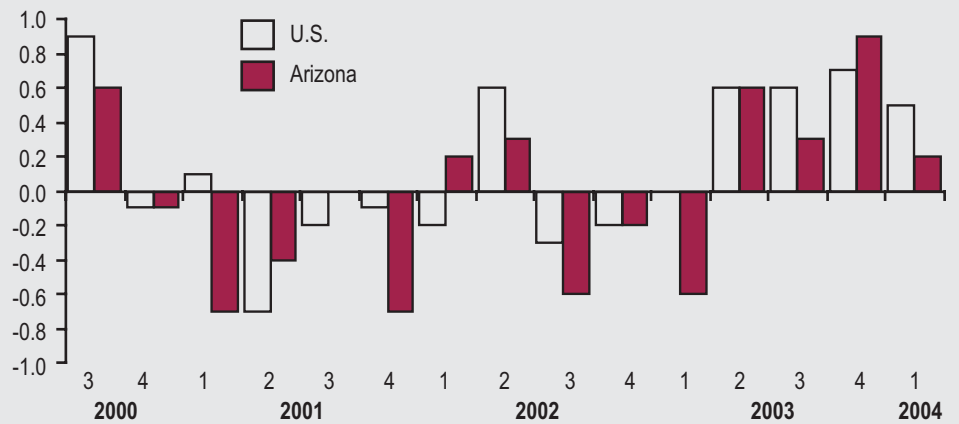
Instead of the employment losses registered nationally, Arizona experienced a period of weak employment growth after the end of the 2001 recession [see Figure II — the Arizona

figures are a three-month moving average]. In July 2003, growth accelerated to a moderate rate, two months earlier than the national improvement. However, a further acceleration in employment growth did not occur in 2004, leaving Arizona's employment gains during the first half of 2004 well below those of ear-

lier expansionary periods. As of June 2004, the year-over-year rise was 54,000 (2.4 percent). Annual employment gains were more than this from spring 1993 through 2000.

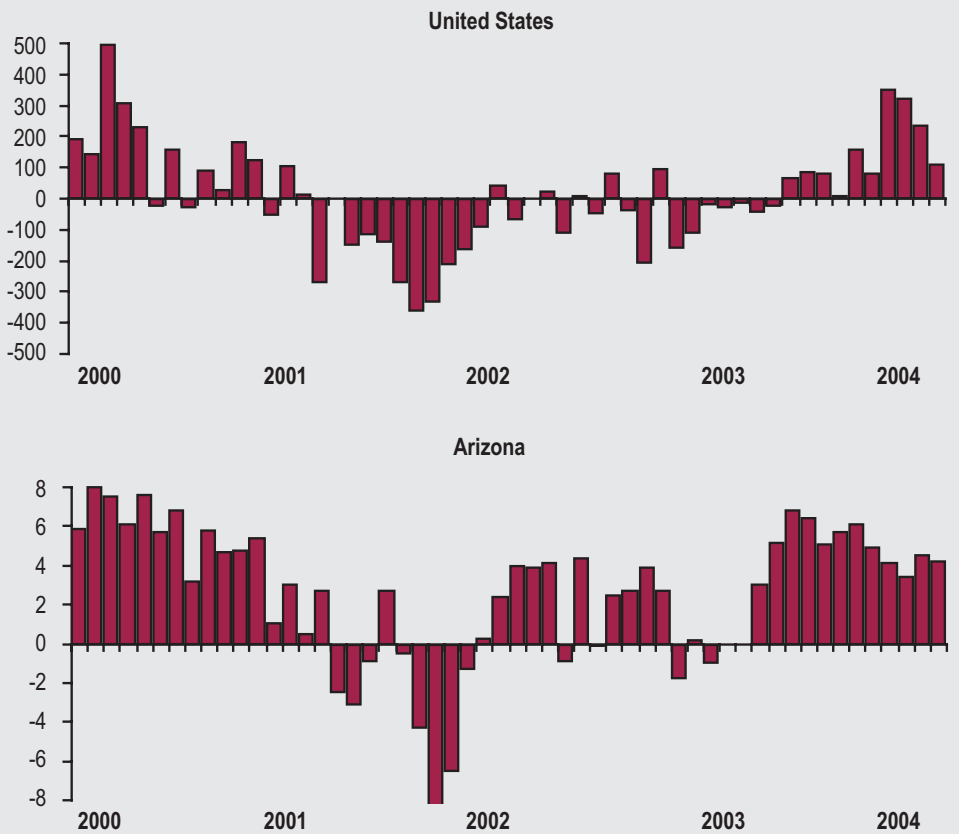
— Tom R. Rex
Research Manager

FIGURE I
QUARTERLY PERCENT CHANGE IN REAL PER CAPITA PERSONAL INCOME



Source: Center for Business Research, L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University, from data of the U.S. Department of Commerce, Bureau of Economic Analysis..

FIGURE II
SEASONALLY ADJUSTED MONTHLY CHANGE IN EMPLOYMENT



Source: U.S. Department of Labor, Bureau of Labor Statistics..

Arizona Business Conditions Index moves up in July

The seasonally adjusted Arizona Business Conditions Index rose to 67.2 in July from 65.9 the previous month, a 2 percent increase. An index reading over 50 indicates that the local economy is growing; below 50 suggests a slowdown in the overall level of economic activity in the near term.

ANALYSIS

The index continues to oscillate in the mid-60s for the 11th consecutive month. This is well within the range of steady economic growth. The manufacturing sectors did not fare as well as the non-manufacturing sectors in July, but there are no signs of deteriorating conditions.

The purchases subindex jumped by 4.8 points in July, the greatest change in any of the components. This was followed by the production subindex, which rose by 3.9 points. Both of these components are good indicators that the output side of the economy is showing strong growth. The employment component rose only slightly, but is still well within growth territory. Employment was the last component to recover from the recession, but a spurt of growth in January brought

it within range of the other components.

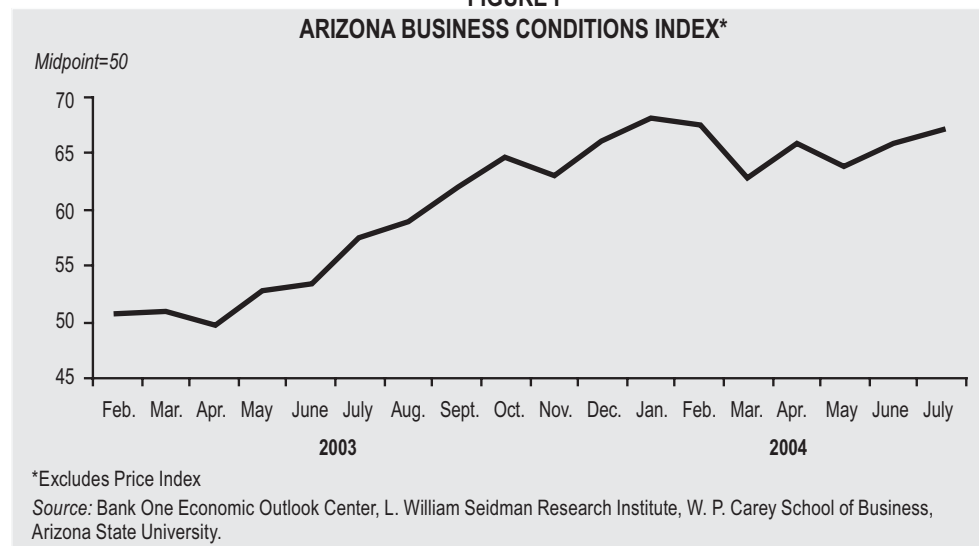
The Prices Index remains in the 70s, falling slightly to 74.0 in July. While this is an improvement over the level of 76.9 seen in May, it still indicates upward pressure on prices in the local area. Prices of steel and other metals, fuel and lumber all have been drivers of this increase. More recently, other

commodities such as plastics have been rising. At this point, the increase in the price of inputs does not appear to be deterring growth in output.

— Dawn McLaren
Research Economist

Bank One Economic Outlook Center

FIGURE I
ARIZONA BUSINESS CONDITIONS INDEX*



Arizona Leading Index up slightly in July

The Bank One Arizona Index of Leading Economic Indicators rose in July to 124.9, an incremental 0.08 percent higher than the previous month's 124.8 and 2.9 percent above the July 2003 level of 121.4 (1987 = 100).

Positive influences in the July index included the inflation-adjusted value of Maricopa County residential building permits, production, new orders, and employment from the Business Conditions Survey. Hours worked in manufacturing, the inflation-adjusted value of the M2 money supply, materials inventories and delivery times were negative. Sensitive materials prices were neutral.

Residential building permits (positive) and hours worked in manufacturing (negative) were the only indicators with substantial changes in July. The former continues to surprise, with some contractors reporting that labor shortages are significant enough to limit the number of homes going up. The evidence is mounting that suggests the sector has to slow down soon. Building materials, which are already in shorter than usual supply because of demand from China, will be further squeezed

by the need to rebuild in Florida and other places hit by hurricanes this season.

Hours worked in manufacturing was a weak component at the beginning of the year. Unfortunately, the earnings forecasts by major semiconductor manufacturers like Intel, Motorola and ON suggest that the manufacturing sector in Arizona still has a

way to go before recovery really sets in.

Arizona remains stuck in limbo, with an economy that will remain sluggish unless and until the national economy improves.

— Tracy Clark
Associate Director

Bank One Economic Outlook Center

FIGURE I
ARIZONA INDEX OF LEADING ECONOMIC INDICATORS





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ARIZONA ECONOMIC INDICATORS

	Month or Quarter	Current Value	Previous Value	Percent Change Previous Period	Percent Change from Year Ago	Year-to-Date	
						Value	Percent Change from Year Ago
LEADING ECONOMIC INDEX (1987 = 100)							
Arizona	July	124.9	124.8	0.1	2.9	NA	NA
BUSINESS CONDITIONS INDEX							
Arizona	July	67.2	65.9	2.0	16.7	NA	NA
BUILDING PERMITS (Thousands of \$)							
Maricopa County	June	1,194,509	1,177,379	1.5	24.6	6,303,750	32.5
Pima County	June	193,311	131,610	46.9	41.4	951,910	13.4
Balance of State	June	364,964	312,300 r	16.9	17.7	1,860,129	26.5
Arizona	June	1,752,784	1,621,289 r	8.1	24.7	9,115,789	28.9
TOTAL HOUSING UNITS AUTHORIZED							
Maricopa County	June	5,257	4,928	6.7	0.8	28,700	26.8
Pima County	June	1,202	738	62.9	44.5	5,484	13.2
Balance of State	June	2,531	2,274 r	11.3	6.5	13,764	22.5
Arizona	June	8,990	7,940 r	13.2	6.7	47,948	23.8
HOME SALES							
Maricopa County – Number.....	June	17,730	15,290	16.0	40.3	76,710	32.5
Maricopa County – Median Price(\$).....	June	173,000	166,475	3.9	10.8	165,000	9.1
HOUSING AFFORDABILITY INDEXES							
Metropolitan Phoenix – New Homes	2nd Quarter	100	113	-11.5	-13.0	NA	NA
Metropolitan Phoenix – Resale Homes	2nd Quarter.	112	127	-11.8	-14.5	NA	NA
MORTGAGE RATES (30-year Fixed)							
Maricopa County	July	5.7	5.9	-3.4	5.6	NA	NA
POPULATION ESTIMATES (Thousands)							
Maricopa County	1st Quarter	3,476	3,444	0.9	3.4	NA	NA
Pima County	1st Quarter	918	913	0.6	2.3	NA	NA
Balance of State	1st Quarter	1,365	1,353	0.9	3.2	NA	NA
Arizona	1st Quarter	5,759	5,710	0.9	3.2	NA	NA
RETAIL SALES (Millions of \$)							
Maricopa County	June	2,922	2,850	2.5	6.9	17,296	9.4
Arizona	June	4,307	4,300	0.2	7.1	25,366	8.9

Note: The above figures reflect the latest data available as of date of publication and are subject to revision.

NA = Not Applicable r = Revised

Source: Center for Business Research, Arizona Real Estate Center, and Bank One Economic Outlook Center, affiliates of the L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University. Retail sales data are from the Arizona Department of Revenue.