

ALASKA ECONOMIC UPDATE

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EMPLOYMENT & INCOME

Alaska unemployment remains lower than the national average, but gap is closing – Alaska’s seasonally adjusted unemployment rate finished the year at 6.4%. The comparable national rate in December was 6.7%. This was an improvement of 0.2% and 1.1% respectively for Alaska and the U.S. versus the December of 2012 rates.

As seen in the graph below by the Alaska Department of Labor, for over five years Alaska has been doing better than the U.S. in terms of unemployment. The rate in Alaska in green has been relatively stable, despite the national recession and the U.S. rate spiked much higher. Now the U.S. rate is improving relatively faster than Alaska. This appears to already be affecting population migration trends as jobs are more easily found in the lower 48.

UNEMPLOYMENT RATES, ALASKA AND U.S.
JANUARY 2003 TO DECEMBER 2013



Source: Alaska Department of Labor and Workforce Development, Research and Analysis Section

The unemployment rate is even better in Alaska’s largest communities. The preliminary, not seasonally adjusted, rate for Anchorage was 4.6%, Juneau 4.6%, and Fairbanks at 5.4%. The Mat-Su rate improved from 8% in 2012 to 7.3% in December of 2013, but is still higher than the national unemployment levels.

Anchorage and Juneau’s rate is in the range of what economists call “full employment.” At these low levels a

majority of those unemployed are due to seasonal, frictional, structural or cyclical reasons. For example, some seasonal workers only plan to work part of the year and collect unemployment benefits for the remainder of the year. The frictional part is the natural short-term movement of workers between jobs and first-time job seekers. The most important issue for employers is these low rates inevitably lead to a scarcity of qualified workers and upward pressure on wages.

High levels of unemployment still persist in several rural areas of Alaska. The worst situations are the Hoonah-Angoon Census Area at 21.3%, Wade Hampton Census Area 20.8%, Municipality of Skagway at 20.4% and the Aleutians East Borough at 19.6%. However, the North Slope Borough has the lowest unemployment levels in the state at 3.9%.

Payroll jobs increase only 0.5% in 2013 – Alaska’s payroll job count increased by 1,800 jobs or 0.5% last year. This slight increase is much lower compared to 5,300 jobs added in 2012 and 4,900 in 2011. The total number of payroll jobs, not including uniformed military and the self-employed, is about 336,000 on average throughout the year. It is important to note this is a preliminary estimate by the Alaska Department of Labor using nine months of actual data from employer tax returns and three months of estimates. The final numbers will be revised in March of 2014.

The Alaska Department of Labor’s forecast for 2014 is a modest growth of 0.4% or 1,500 jobs. The largest drag they foresee will result from declining government spending. This will come from a smaller state capital budget and federal sequestration efforts in Washington D.C. These job losses will be more than made up for by continued gains in health care and the energy industry.

Health care is benefiting from a demographic situation where Alaska has both an aging baby boomer population and a young, under 20 generation. People require the most health care at the beginning and end of their lives.

Oil and gas is seeing a large amount of independent energy exploration in response to the tax rate adjustments and continued high oil prices. Other forecasted contributors to positive labor growth include seafood processing, tourism, retail trade and professional services.

Personal income rises 2.3% – Total personal income for Alaska was \$37 billion in the third quarter of 2013, according to data released by the U.S. Department of Commerce Bureau of Economic Analysis. This is an increase of \$800 million compared to one year ago, or a growth rate of 2.3%. That equates to per capita income of roughly \$50,000 in Alaska.

POPULATION

Population increases only 0.6% – The most recent Department of Labor estimate for Alaska’s population is 736,399. That is a 0.6% increase in 2013 resulting from an additional 4,572 people. This is the smallest increase in the last 17 years. The period between 1994 and 1996 saw similarly low levels. In historical perspective, this is the seventh lowest rate of population change in the 68 years since the end of World War II in 1945.

A majority of the growth is due to natural increase. There were 11,263 births reported and 3,843 deaths recorded for a natural increase of 7,420 people. This is very consistent with the last ten years. Where the variability comes from is the net of in and out migration of people internationally and from other parts of the U.S. Migration resulted in a net loss of -2,848 people. This again was the largest decrease since the 1994-1996 period. The driving factor is likely to be the relative improvement of the U.S. and world economy compared to Alaska.

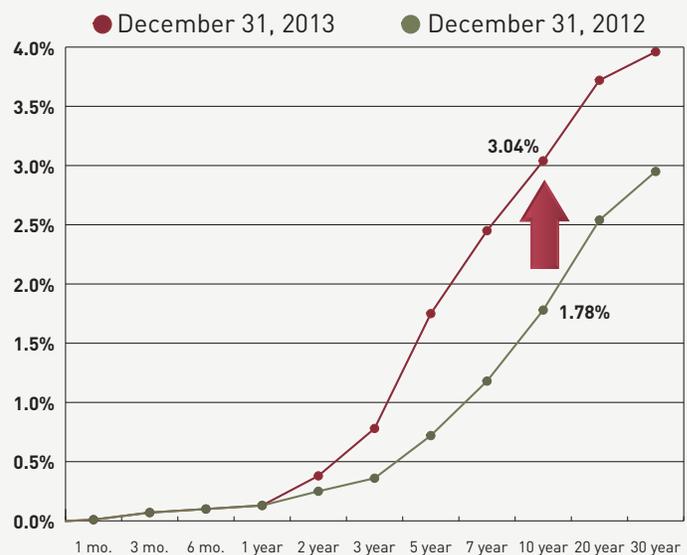
The median age is 34, but that is one of the least common ages in the state. The distribution is heavily weighted on the young and older end. Of ages under 65, the fewest people are age 35 to 44. The male and female gap has also been narrowing over time with women now accounting for 48.3% of the population.

INTEREST RATES

Interest rates are rising – You can see in the graph to the right that since the end of 2012 interest rates for all maturities longer than one year have risen. The 10 year bond is highlighted. It rose 1.26% in 2013. Expectations are for rates to continue to rise as the Fed tapers its purchasing of longer maturity bonds and mortgage backed securities

now that the unemployment rate has hit their target goal of 7%. At 6.5% they have signaled that they would start pushing the overnight Fed funds rate up, which would create separation on the left side of the graph. It has remained at the historically low 0% - 0.25% target rate since December of 2008. This is unprecedented accommodative monetary policy for an extended period of time. It is likely that any Fed funds rate increase would come at a slow and measured pace.

U.S. TREASURY YIELD CURVE



HOUSING

Home lending activity growing slightly – The Alaska Housing Finance Corporation (AHFC) released its third quarter report on Alaska housing indicators. It tracks new loan activity for single family homes and condominiums in Alaska. The data is based on a survey representing approximately 95% of mortgage lenders in Alaska and also includes AHFC loans. The survey covered mortgage lending activity in the first nine months of 2013.

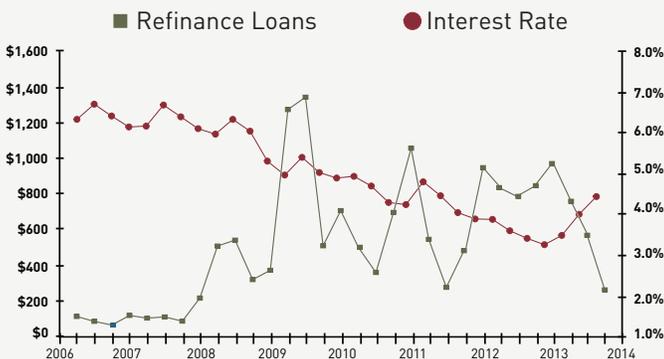
It reported 6,856 loans were originated statewide for single family homes and condominiums for a total amount of \$1.8 billion. This is an increase compared to 6,014 loans for \$1.5 billion in the first 9 months of 2012. Loans were done with an average down payment of 10% over the last five years. Single family homes accounted for 90% of statewide mortgage lending activity with 56% of those loans occurring in Anchorage. The Mat-Su contributed 15% of the volume, 10% in Fairbanks, 7% in Kenai, 6% in Juneau, 2% in Kodiak, and 1% in Ketchikan.

90% of condominiums were financed in Anchorage. Juneau accounted for 5%, the Mat-Su 2% and Fairbanks 1%. Additionally, there were 199 units of multi-family housing financed by 63 loans in the first nine months of 2013.

Refinance activity slowing rapidly as rates rise – 30 year conventional fixed interest rate mortgage loans have been getting less expensive for three decades. In 1981 they peaked at 16.6% and have undergone a slow and steady decline ever since. In early 2009 rates dipped under 5% on average for the first time and a surge in refinance activity began.

According to AHFC statistics, there was less than \$200 million in refinance loans completed per quarter in Alaska in 2006 and 2007. In 2008, the average rose to \$400 million. Then in the first quarter of 2009 the activity spiked to \$1.4 billion, followed by \$1.2 billion in the second quarter. During this time, the average 30 year interest rate declined nearly 1.5% in six months.

**REFINANCE LOANS VS. U.S. AVERAGE
30 YEAR MORTGAGE RATES**



The refinance pace slowed somewhat in the last half of 2009, but still finished the year with \$3.7 billion in refinanced mortgage loans according to AHFC statistics. In 2010, the refinance volume declined to \$2.4 billion, followed by \$2.1 billion in 2011. 2012 saw an unexpected decrease in interest rates again to an all-time historic low of 3.3% by the end of the year. This led to an increase to \$3.1 billion in refinance activity. Rates increased throughout 2013 and you can see on the far right of the graph, the result has been a steep drop off in refinance activity. Rates finished last year at 4.5% on average. Total refinance activity was \$1.5 billion through September of 2013.

Housing statistics good relative to the U.S. – The recently released survey by the Mortgage Bankers Association shows that Alaska continues to have some of the lowest levels of foreclosures and delinquencies on residential mortgage loans in the United States. Through the third quarter of

2013, Alaska ranked fourth and fifth best in the nation out of 50 states in foreclosures and delinquencies of all loan types.

The total inventory of foreclosures in process is 1.1% in Alaska, while the country has a much larger lingering foreclosure inventory at 3.1% due to higher rates during the recession and longer resolution times. These rates are an improvement from three years ago when Alaska’s rate was 1.4% and the U.S. foreclosure rate was 4.6%.

Delinquent loans are more than 30 days past due, but not yet in foreclosure. Alaska is fifth best behind North Dakota, South Dakota, Montana and Hawaii in the overall level of delinquent loans. Alaska’s delinquency rate is 3.8%, while the U.S. average is 6.7% for all loan types. This is an improvement for Alaska from 4.8% three years ago. The U.S. delinquency rate has also come down more dramatically from 9.4% at this time three years ago.

	NATIONAL RANK	ALASKA	U.S.
Delinquencies, total 3Q 2013	5th Best	3.8%	6.7%
Foreclosures, total in progress	4th Best	1.1%	3.1%
Subprime delinquencies	Best in Nation	9.8%	20.8%
Subprime foreclosures	Best in Nation	2.6%	11.2%

Subprime lending to traditionally non-qualified borrowers was a large contributing factor to the national mortgage problems. The survey covers 93,519 mortgages in Alaska. 6,215 or 7% were considered subprime, compared to 9% nationally. The rate of delinquencies and foreclosures on subprime loans is significantly higher. However, Alaska is in a far better position and again leads the nation as having the lowest level of foreclosures and delinquencies in this important category. Subprime foreclosures in Alaska are at 2.6% while the national average is 11.2%. Alaska’s subprime delinquency rate is 9.8% compared to the national average of 20.8%.

Building permits up 9%, but still historically low –

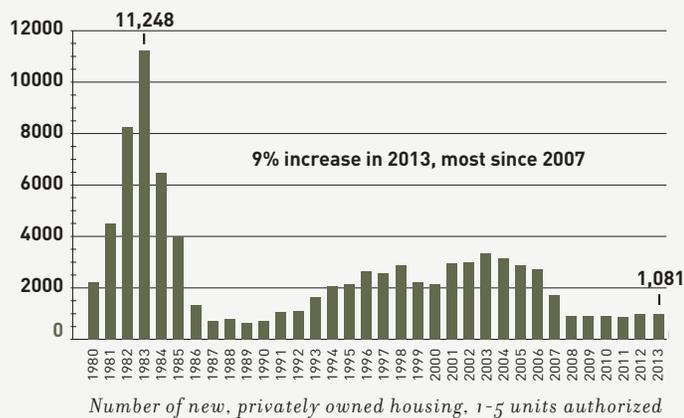
According to the U.S. Census Bureau, the number of building permits for new, privately owned housing of one- to five-unit buildings remained low for the sixth straight year. It had been under 1,000 units since 2007, but in 2013 it grew 9% to 1,081.

Growth in single occupancy units increased from 821 to 888 last year. The number of duplexes permitted went from

44 to 62. The number of structures with three or more living units rose from 30 to 58.

The biggest challenge has been making new construction affordable enough to meet buyer's income levels. There is a shortage of low cost housing in Anchorage. Vacancy factors are very low and the number of existing homes under \$350,000 is in short supply. However, the major constraint is how much the property will be able to rent or sell for once it is completed. The cost of land and rising interest rate environment will also put pressure on the affordability of homes. Anchorage will likely follow other growing cities by becoming denser, building vertical and redeveloping older properties.

ALASKA BUILDING PERMITS



OIL INDUSTRY

Alaska oil production declines another 8% in 2013 – Alaska's oil production peaked at two million barrels per day in 1988, but has since declined to 543,800 barrels a day at the end of the State's fiscal year ending June 30, 2013. This was an 8% decrease from the prior year and continues two and a half decades of decline. High oil prices and production taxes have masked the decline by helping keep state government revenues healthy despite the loss in output. On February 4, 2014 the price of Alaska North Slope crude closed at \$103.16.

State revenues declining while operating costs are increasing. Cuts to capital spending are occurring in response. The state earned \$15.8 billion in revenue from all sources in FY 2013. That includes \$5 billion from investment returns and \$2.4 billion from the Federal government. Taxes and fees from non-petroleum sources such as corporate taxes, fishing, mining, tourism, alcohol and tobacco taxes accounted for \$1 billion. Petroleum

accounted for a total of \$7.4 billion. When looking only at the portion the Legislature can spend out of the General Fund, petroleum accounted for 92% of the state's unrestricted revenue in FY 2013.

Costs keep rising on the operating side of the budget. The FY 2013 budget was \$8.97 billion and the current FY 2014 plan is \$9.72 billion. The Governor has requested increasing that to \$11.48 billion in FY 2015. The largest source of the increase would be a \$2.3 billion additional contribution for the unfunded pension fund obligations for state employees. This issue has not yet been decided by the Legislature.

If we exclude Permanent Fund earnings from the revenue side then the State expects to earn \$9.5 billion in revenues in FY 2014. The operating budget is higher at \$9.7 billion and another \$2 billion is slated for the capital budget. This results in a \$2.2 billion budget shortfall. In response, the state is making dramatic cuts to the capital budget. The 2013 budget included \$3.15 billion in capital expenditures, while the FY 2014 plan is for \$1.97 billion. This is a 37% reduction. The FY 2015 Governor's proposal for the year starting in July of 2014 is to further reduce it by another 16% to \$1.67 billion. In the recent past about \$900 million of the capital budget comes from federal sources.

TOURISM

Visitors to Alaska reached nearly 2 million between October 2012 and September 2013. This is a 7% increase over 2011-2012. Cruise ship passengers account for over half of the annual visitors in Alaska. Visitor spending was over \$1.8 billion in 2012-2013. This does not include transportation to enter/exit Alaska. Employment did not increase at the same rate as visitor volume, but still had an increase of 3% to 39,000 jobs. Nearly half of the jobs were in Southcentral, with just over a quarter in Southeast. Labor income and total spending for the period both jumped 6% to \$1.32 billion and \$3.93 billion, respectively.

Written by Mark Edwards, VP Commercial Loan Unit Manager and Bank Economist with Northrim Bank. He was an adjunct professor of economics at Alaska Pacific University. Mark served the State of Alaska as its state economist in the Department of Commerce and the Department of Revenue, and as the Director of the Office of Economic Development. He has a B.A. in Economics from the University of Virginia and a Master's Degree in International Business from the Thunderbird School of Global Management.