

# Economic Forecast

**MAUI EDITION 2010 - 2011**

## Maui County's Economic Picture Is Marked By Its Impressive Tourism Industry Rebound

**W**hat distinguishes the Maui economy in 2010 is the impressive rebound in tourism. It leads all other counties in that regard. Maui residential real estate sales are another area of impressive growth. In other sectors, such as construction, Maui lags both Honolulu and the Big Island.

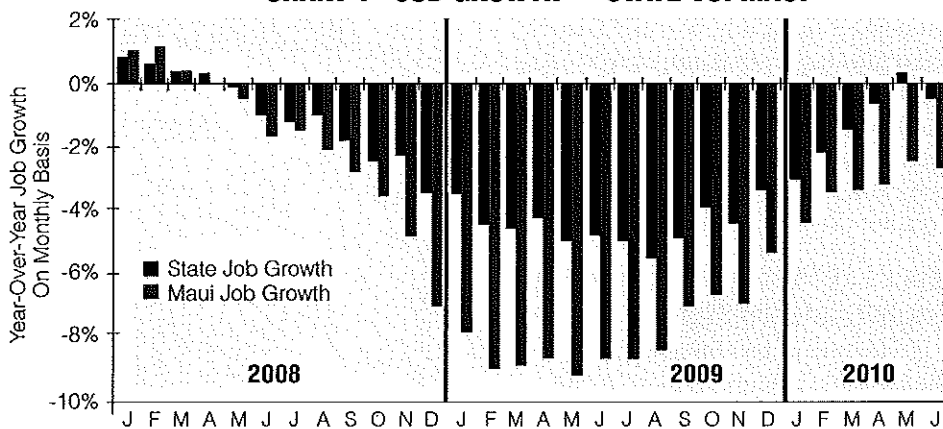
Barring any unforeseen misfortunes, an economic recovery is now underway or at least imminent for the Maui economy, but don't expect a rapid return to normal. Remember, an economic recovery begins when positive growth resumes after a recession, but it doesn't end until the previous peak is reached. The 2006-2007 peaks for a number of important economic variables won't be reached for some time, but at least the direction is right.

*“Neighbor Islands have felt the recession more than Oahu.”*

Led by its economic mainstay of tourism, Maui can look forward to better times in the future. Much greater uncertainty would have been attached to a statement like that a year ago.

I have characterized our current recession as an “L-shaped” one — that is, a sharp decline followed by a more gradual recovery. There is no reason to change that basic scenario now. The good news is that the free-fall on the *back* of that L is over. We seem to have entered the bottom of the L, with a slow recovery underway or soon to occur. Some of the important numbers are now showing increases, and those that are still declining are doing so at decreasing rates as time moves on.

**CHART 1 • JOB GROWTH — STATE VS. MAUI**



Source: State Labor Department

### Island Job Growth Totals Are At Last Turning Around

The Hawaii state economy started to fall off the cliff in the second quarter of 2008 when the exit of Aloha Airlines, ATA charter service and two NCL cruise ships began to be felt. A number of other negative blows — in construction, agriculture, a bad summer for tourism with higher fuel prices, and so forth — soon followed. And the culmination, for Hawaii as well as the rest of the world, was the collapse of financial markets in the fall of 2008. The result was a very grim year for almost all of 2009.

But as 2010 has progressed, a bottom has emerged. Chart 1 shows a marked reduction in monthly year-over-year job losses. A few job categories are already growing, and without further negative developments, it won't be long before overall job gains become consistent. The year 2010 as a whole could still show very mild overall job loss, but by 2011 aggregate state jobs

will likely show sustained (if slow) growth.

Maui job growth shows a similar pattern — still losing overall jobs, but at a slower rate. The chart shows that Maui has further to go in returning to positive job growth than the overall state, a reflection of the reality that all of the Neighbor Islands have felt the recession more acutely than Oahu's relatively diversified economy.

### Island Unemployment Rate Has Topped Out

Before the recession, Hawaii had one of the lowest jobless rates in the nation, but like everywhere else unemployment

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**Maui County** (continued from page 1)

here has shot up dramatically. Clearly, as Chart 2 shows, the rate has now peaked. The unemployment rate is always a lagging indicator, and it will probably come down slowly, but the statewide rate won't break 7% again. And all during the recent recession, it has remained about 2 percentage points below the national rate.

Here, too, Maui mirrors performance at the state level — the Maui jobless rate has peaked and is now coming down. It often runs higher than the state average, and here you see more evidence of how a tourism-dependent Neighbor Island economy is more vulnerable in the kind of recession we've just been through. Look for slow future declines here also.

**Maui's 2010 Tourism Recovery Easily Leads the State**

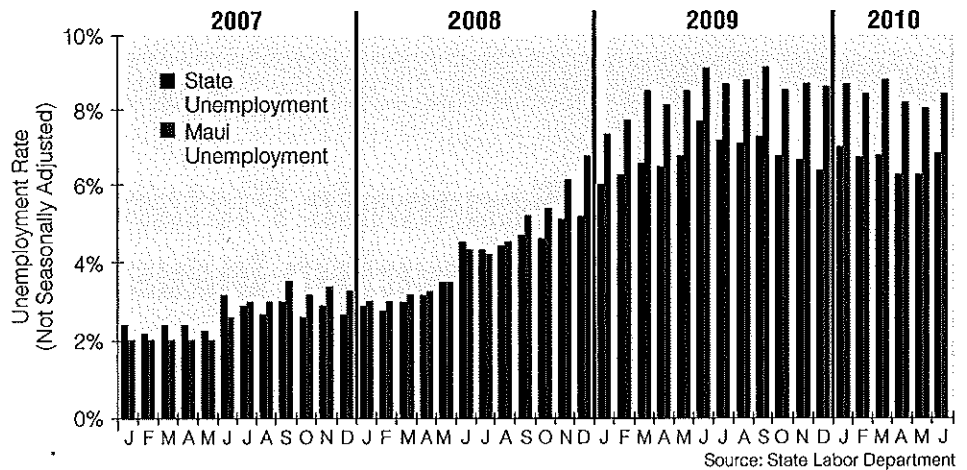
Two important components of the Hawaii economy — tourism and construction — have to return to health before a sustained recovery emerges.

As for tourism, we're already seeing signs of recovery. Chart 3 shows that, in recent months of 2010, statewide visitor arrivals and spending have both shown encouraging year-over-year monthly gains. After disastrous performance in 2009, those gains are not hard to achieve. But we are coming up from that bottom.

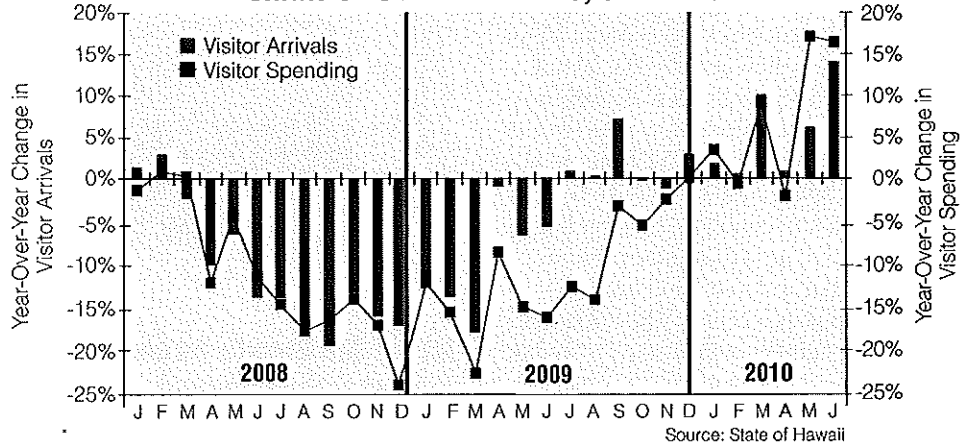
Maui's tourism recovery in 2010 easily leads the state, as Chart 4 illustrates. Both visitor arrivals and spending are well ahead of other islands. Both March and May of 2010 have shown particularly impressive gains. Added flights — from Hawaiian and Alaska Airlines, as well as Canadian carriers WestJet and Air Canada — are helping.

Maui sources report travelers are still a little cautious despite gains in the numbers, but if potential travelers do a little research on packages they can get good deals. Visitors are still searching for value. Regarding trends in visitors, honeymoons are up even if weddings on island are falling, and family business has been strong.

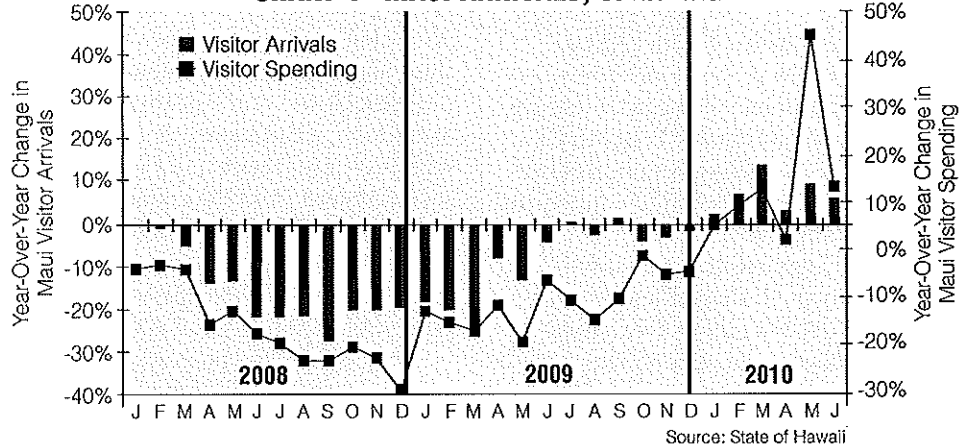
**CHART 2 • UNEMPLOYMENT — STATE VS. MAUI**



**CHART 3 • STATE ARRIVALS, SPENDING**



**CHART 4 • MAUI ARRIVALS, SPENDING**



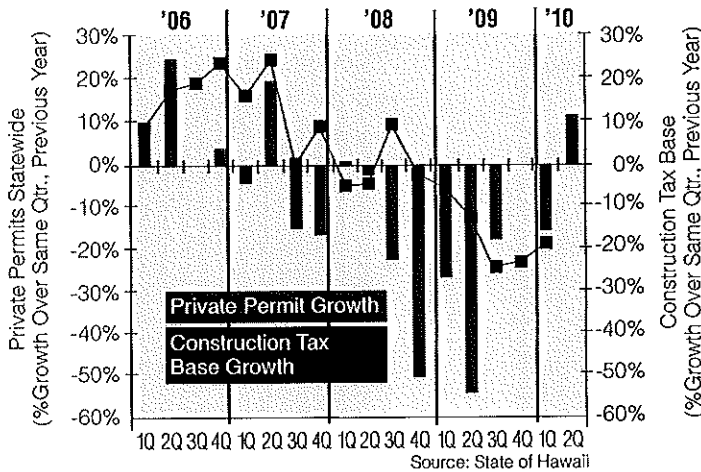
**Maui's Construction Industry Lags Honolulu, Big Island**

Construction is an important component of the economic cycle just because of its volatility. The statewide construction picture still has a way to go, as shown in Chart 5. Construction completed in the tax base (the line on the chart) was still falling through the

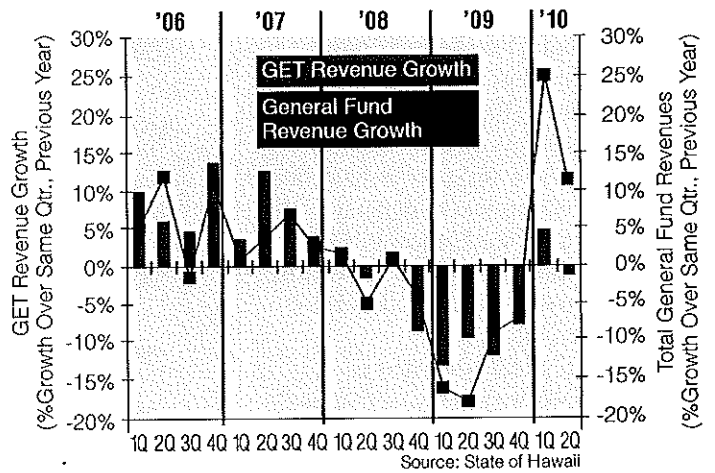
first quarter of 2010, the most recent observation. And total private permits (the bars on the chart) actually rose, by almost 11%, in the second quarter.

That permit growth picture is mixed throughout the state, with Maui lagging Honolulu and the Big Island. Private permits on Maui (Chart 6) were down almost 50% in the first quarter of

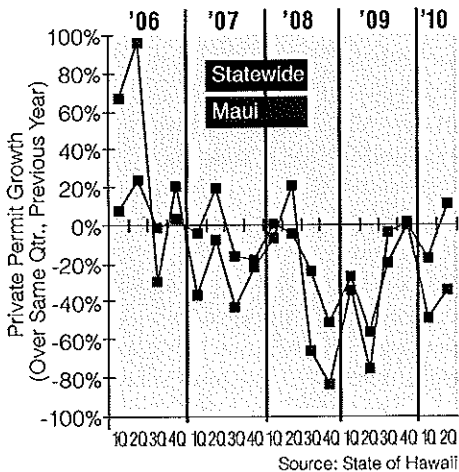
**CHART 5 • STATE CONSTRUCTION INDUSTRY**



**CHART 7 • STATE TAX REVENUE GROWTH**



**CHART 6 • CONSTRUCTION — STATE VS. MAUI**



**State Tax Revenue Trend Lines Finally Showing Improvement**

Even state tax revenues, a big source of concern over the past year, have shown some improvement recently (Chart 7). The state General Fund was up by double-digit percentages in 2010's first half. Most of that came from an increase on withholding taxes on wages and delayed income tax refunds. But even General Excise taxes, a good monitor of ongoing economic activity, came in higher than the first half of 2009. This encouraged the state to release income tax refunds sooner than planned earlier.

**Alexander & Baldwin Has More Big Plans for Maui**

Alexander & Baldwin, which always plays an important development role in the Maui economy, anticipates several projects in the coming years:

- Maui Business Park Phase II, its light industrial area in Kahului along the Hana Highway, anticipates a start of construction activity in early 2011, with completion in late 2012.
- Kahului Town Center is a mixed-use project designed to reinvigorate the site of the old Kahului Shopping Center, which was destroyed by fire several years ago. It will call for 125,000 square feet of retail space, 70,000 square feet of new office space, and about 400 residences.
- Also included in this redevelopment is Kane Street Condominiums, another mixed-use component now in the permit process.

**CHART 8 • MAUI REAL ESTATE**

**Change in Number of Sales**

	2009	'10 YTD*
Single-family homes	-24%	+43%
Condominiums	+4%	+64%

**Change in Median Price**

	2009	'10 YTD*
Single-family homes	-14%	-7%
Condominiums	-18%	-32%

\*Data through June 2010

Source: Realtors Association of Maui

■ In Wailea, A&B's two most imminent projects are 75 fee-simple luxury condo units and a mixed-use project with commercial space, condo units, and single-family residential lots.

**Residential Real Estate Sales Bounce Back Strongly in 2010**

Like elsewhere, Maui residential real estate sales are up big time, fueled by greater affordability with declining prices and record low mortgage rates. And tax incentives plus some short sales also have played a role.

Chart 8 shows that median prices are still falling, but at a lower rate than in 2009. (We can ignore the big 2010 decline in condo prices, which can be traced to the higher-end Honua Kai development coming on in early 2009, which makes this year's prices look far lower.)

As with other counties, lower real property valuations have serious implications for Maui County tax

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2010 over a year earlier, and showed a second quarter decline of over 30%.

Some in the industry still cite two causes for the trend: Maui's 50% affordable housing requirement for new residential development, as well as the "show me the water" ordinance requiring a water meter permit before building can begin.

Nonetheless, there is some construction activity worth mentioning. At Maui Lani, some commercial as well as residential activity is ongoing. Site work for a 100,000-square-foot building for Paradise Beverage has started, and at Professional Row another 61,000 square feet of commercial space in seven different buildings is for sale. As well, a 24,000-square-foot Latter Day Saints church will be coming soon. And three completed water wells there will help with the permitting process.

## Maui County (continued from page 3)

revenues, about 41% of which come from property taxes. There were some great years during the last real estate boom, but that's over for a while.

Maui won't be hit quite as hard here as some other counties. Its dependence on property tax is less because of a higher exemption from property tax on the first several hundred thousand dollars in valuation of homes.

Values are lagged one year in determining property taxes — that is, the 2011 tax base will be taken from valuations on January 1, 2010.

The biggest increase this year in leased commercial properties on Maui has come on the retail side, which has actually doubled. That may seem surprising in a still recovering economy, but not as much office space is available and office tenants are going into retail space more. They are getting better space at lower prices, and landlords are offering more concessions. Demand for office space itself is up only slightly, and industrial space is about level.

### Retailing: Tourism Sector Stronger Than Locally-Oriented Malls

There is always a dichotomy in Maui retailing between tourism retail and the local market. Tourism retail is strong in 2010, reflecting the revival in visitors and their spending. Occupancies in nearby hotels and proximity to more fully occupied time-share units are, as always, important in determining foot traffic.

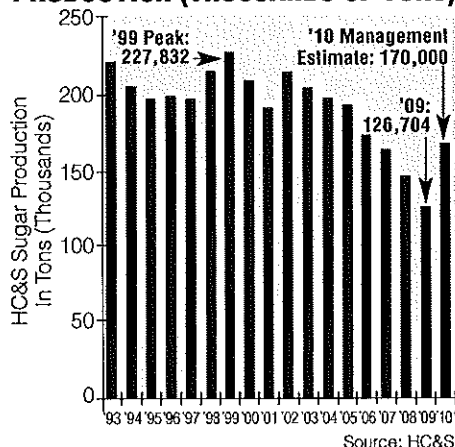
Some regional malls more oriented toward Maui residents are still seeing mild declines in sales, but nothing compared to the weakness experienced in 2009. Discounters are doing better, and local restaurants are showing more signs of life.

### Maui Economic Development Board Active in Educational Programs

Maui Economic Development Board in Kihei reports a lot of activity in the area of education development. For example, there is an ongoing professional development program for teachers in the areas of science, technology, and math.

MEDB has also ramped up its

**CHART 9 • HC&S SUGAR PRODUCTION (THOUSANDS OF TONS)**



renewable energy curriculum in the last year and has already trained 100 teachers statewide in this area. And the board continues to sponsor the AMOS (Advanced Maui Optical and Space Surveillance Technologies) Conference.

### Maui Community College Leads State in Enrollment Growth

Maui Community College had the highest enrollment increase in the University of Hawaii system in 2009 at 25%. The 2010 enrollment increase should at least break well into the double digits. Enrollment there now exceeds 4,000 students, and the college reports an estimated \$7.8 million in external grants this fiscal year.

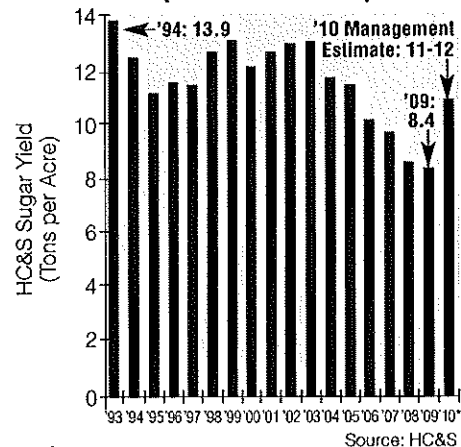
Among the developments this year at the college:

- Groundbreaking for a \$25-million Science Building.
- A new \$1.2-million Hawaiian Studies Center should be complete in the fall of 2010.
- A \$5-million electrical replacement system should soon be complete.
- And a \$500,000 redesign of the old science building is planned to house the nursing and dental programs.

### HC&S Expecting Sugar Production, Yield to Climb in 2010

Charts 9 and 10 concerning Hawaiian Commercial & Sugar Company, Hawaii's sole remaining sugar plantation, paint a grim picture, but better news is on the way. HC&S estimates that 2010 total production

**CHART 10 • HC&S SUGAR YIELD (TONS PER ACRE)**



should exceed 170,000 tons, less than they would like, but far better than 2009's total of less than 127,000 tons. The 2010 yield should be around 11 to 12 tons of sugar per acre, well above 2009's figure of 8.4. A big reason for higher production and yield is getting more age on the crop with a delay in harvesting.

In June, HC&S got a reprieve — if no victory — when the state Commission on Water Resource Management ordered 12.5 million gallons of water per day to discontinue being diverted from West Maui streams for HC&S use. Any reduction in water use for sugar hurts, especially in these days of drought, but it could have been worse.

Shutdown of HC&S would put about 800 direct employees out of work and have other negative impacts on the Maui economy — among them a serious blow to the physical appearance of the Valley Isle.

### Maui Land & Pineapple Undergoes Major Reorganization

Another venerable Maui agricultural operation, Maui Land & Pine, has undergone a major reorganization over the last year, leasing out seven product lines and selling an eighth. That makes the operation a landlord; it has gone from about 680 employees down to around 200, most of those in golf and retail.

Pineapple took the biggest hit. A new operator there is Halimaile Pineapple, which will concentrate on a niche product aimed mostly at the local market.

# U.S. & Global Economic Outlook, 2010-11: Short-Run Expediency vs. Long-Run Needs

By Dr. Jack P. Snyderhoud, Professor of Business Economics, Shidler College of Business, University of Hawaii at Manoa

As we enter the second half of 2010, fear of a "double dip" recession has returned. At issue is the ability of the U.S. and some other major economies to reconcile the conflicting needs of short-term stimulus with long-term rebalancing. The short term requires stimulus to offset a lack of consumer and business spending. However, the resulting government deficits and monetary expansion run counter to the long-term needs of reducing excessive government debts.

Some countries, most notably the UK, have already introduced painful austerity measures to come to grips with the long-term rebalancing. In the U.S., these tough choices are being deferred as policymakers continue to focus on the more immediate concerns of the wobbling recovery.

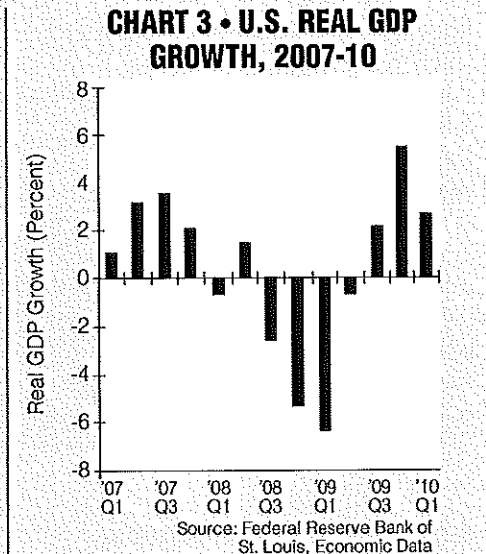
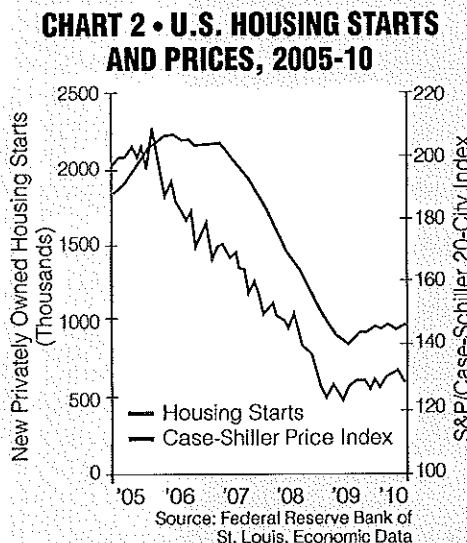
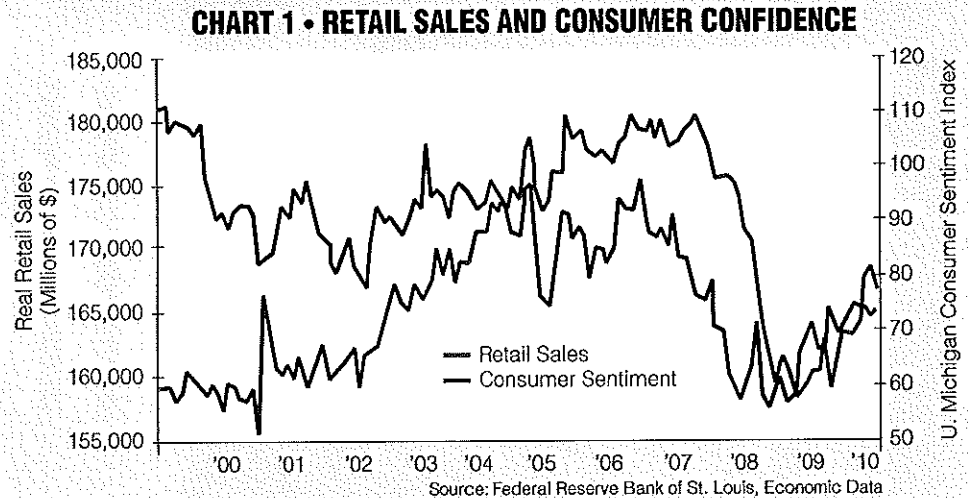
## A Wobbling U.S. Recovery:

Most economists agree that the recession started in late 2007 and ended in the summer of 2009. Consumer confidence and spending (Chart 1) began to improve in late summer 2009 but have not returned to pre-recession levels. Likewise, housing prices and construction (Chart 2) troughed in that same period. All of these were buoyed to some extent by federal stimulus programs. As a result, GDP growth (Chart 3) was positive starting with the 3rd quarter of 2009.

However, the recovery has been tepid, and employment (Chart 4) looks unlikely to return to pre-recession levels anytime soon. In fact, even if we add 100,000 jobs per month it will take more than six years to return to the previous peak. While that is bad news, lackluster growth means that inflation has yet to rear its ugly head.

## Mixed Global Picture:

The prospects for Europe remain poor as many of these countries deal with uncomfortably high public debt levels. These issues have tested the monetary union that has been so important to European economic



integration, but the weakened euro will help these countries' exports.

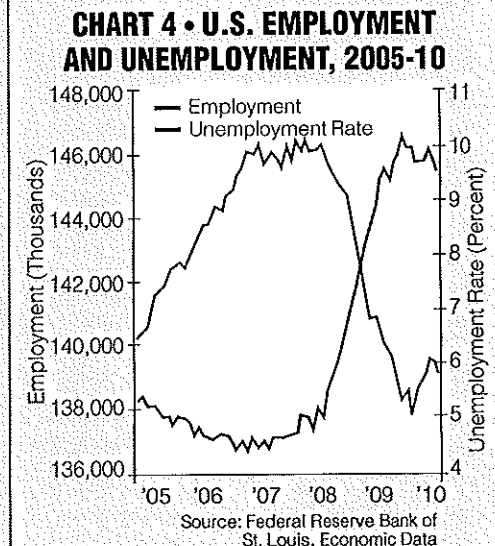
Likewise, Japan's growth is expected to be slow. But the strengthening yen will not help their export sector.

In contrast, China, Korea, India and Australia all have growth rates that exceed global averages, since these countries are becoming more reliant on domestic-led growth and more reliant on each other, rather than European and U.S. markets. Already central banks in China, Australia, and Korea have started to raise interest rates.

## U.S. Stimulus Policies:

Aggressive U.S. monetary and fiscal policies have been somewhat successful in cushioning the impact of recession.

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## U.S. & Global Economic Outlook

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The Federal Reserve has used all of its monetary policy tools and invented new ones, purchasing vast amounts of financial assets that others did not want — first, commercial paper and asset-backed securities, then Fannie Mae and Freddie Mac securities.

All this quantitative easing stabilized the financial system but has done little to expand economic growth. A decline in the so-called “credit multiplier” due to a lack of consumer and business borrowing has led Fed Chairman Ben Bernanke to call on banks to lend more.

Meanwhile, fiscal stimulus has resulted in troubling deficits and debt levels not seen since World War II, as the U.S. and other countries followed Keynesian prescriptions and used government spending to soften the effects of the recession.

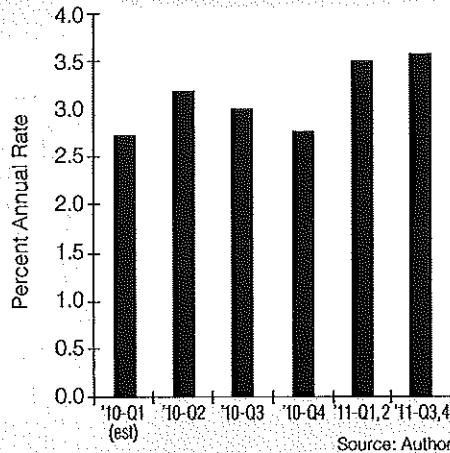
Credit markets have responded by demanding higher risk premiums on the debt of riskier countries. There is even talk of a credit downgrade for Japanese government bonds. But this has yet to affect U.S. Treasuries since the dollar is still an international reserve currency and there has been a flight to safety into U.S. securities.

### Graceful Exit or Painted Into a Corner?

But the question remains: How much stimulus can we afford and for how long? We need an exit strategy to unwind both the monetary and fiscal stimuli. Given the recent slowing of the U.S. economy, it seems policymakers are putting off that day of reckoning and considering still more stimulus. But stimulus is like an antibiotic. You need to use the right amount for the right time in order for it to work. If you use it too often, it will lose its efficacy. And undoing the stimulus will require more austerity and longer recovery. It is thus reasonable to ask: Have we painted ourselves into a long-term corner in order to avoid short-term pain?

We need organic domestic growth that is both vigorous and self-sustaining,

### CHART 5 • U.S. REAL GDP GROWTH FORECAST



and this can only come from the private sector. And it will come only if tax and regulatory systems reward investment and risk taking and reduce uncertainties. In addition, government stimulus needs to be aimed at creating long-term capacity rather than short-term benefits.

### U.S. Forecast and Risks:

Given the discussion above, U.S. GDP growth (Chart 5) is expected to be positive but slow for the rest of 2010 and into 2011 due to several factors:

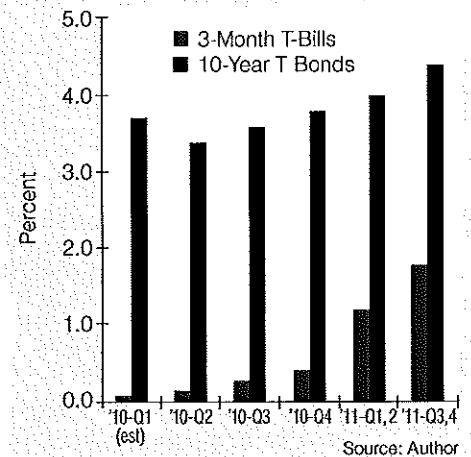
- Consumer spending growth will be moderated by the need for consumers to reduce debts and by a lack of job growth and confidence.
- Export demand for U.S. products will be hampered as the dollar will remain strong relative to major trading partners' currencies.
- U.S. fiscal boosts from the 2008-09 stimulus packages will become smaller as these programs unwind. It is doubtful that there is political will to roll out even more.
- Uncertainties in regulations related to health care, the financial system, and environmental policies will create a drag on growth.

Employment (Chart 6) will grow only slowly and unemployment will remain near 9% through 2011. On the plus side, the tepid growth will keep inflation in check through 2011. As a result, the Fed is not expected to increase the Fed Funds rate until 2011 and then only by small amounts.

### CHART 6 • FORECAST U.S. UNEMPLOYMENT AND INFLATION



### CHART 7 • FORECAST U.S. INTEREST RATES



Treasury yields (Chart 7) will increase somewhat through 2011 but will remain very low by historical standards.

The risks to even this modestly positive short-term forecast are on the downside. The need to come to grips with long-term imbalances (deficits and debt) may force more austerity sooner as financial markets may balk at the levels of public debt. If that is so, interest rates will rise and further reduce consumer spending and business investment. I hope by then our policymakers will have put in place policies that will encourage economic growth, because we will need them.