
Economic Outlook and Why Public Policy Matters

January 2024

ROUNDS CONSULTING GROUP



What we will cover:

- The national economy and how it impacts the state.
- The state's economy and how it impacts budgeting.
- Budgeting and how policy analysis plays a role.
- How to calculate the benefits of policy proposals.

The National Economy



Question: Are we going to have a recession?

- Why the uncertainty?
- Why do economists keep changing their minds?
- What will happen in AZ and the U.S.?
- Do economists just make up stuff?

Outdated Definition of a Recession

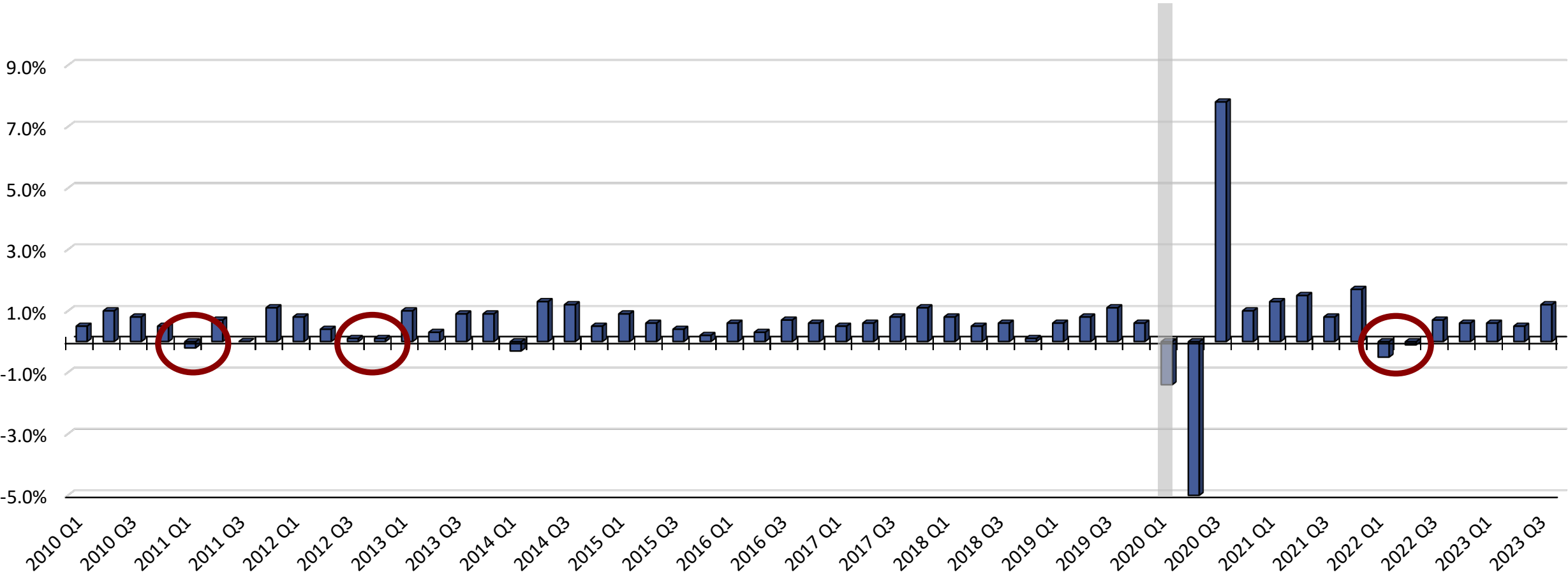
Most known definition:

Two consecutive quarters of decline in GDP.

U.S. Real GDP

Annualized Percent Change; Quarterly, 2010 - 2023*

Source: U.S. Bureau of Economic Analysis



*Data through Q3 2023

Defining a Recession

The fine print:

Q: What indicators does the committee use to determine peak and trough dates?

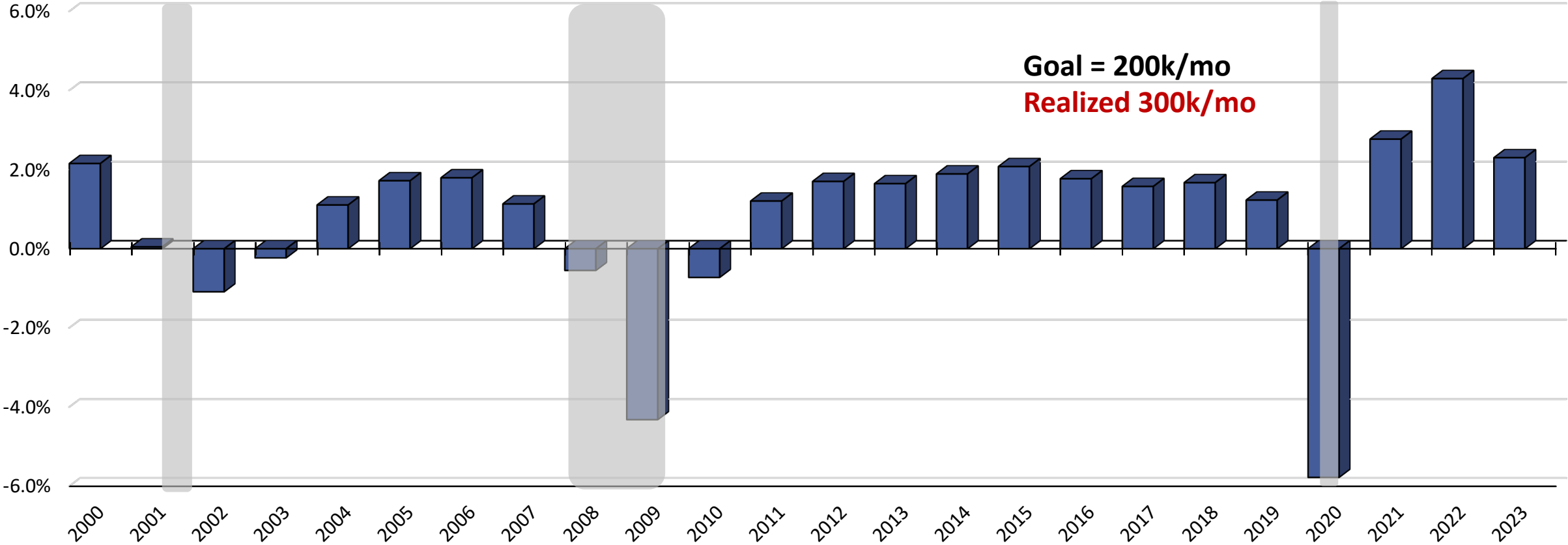
A: The determination of the months of peaks and troughs is based on a range of monthly measures of aggregate real economic activity published by the federal statistical agencies. These include real personal income less transfers (PILT), nonfarm payroll employment, real personal consumption expenditures, wholesale-retail sales adjusted for price changes, employment as measured by the household survey, and industrial production. There is no fixed rule about what measures contribute information to the process or how they are weighted in our decisions.

U.S. Employment Percent Change

Annually, 2000 – 2023*

Source: Arizona Office of Economic Opportunity

Recession Period



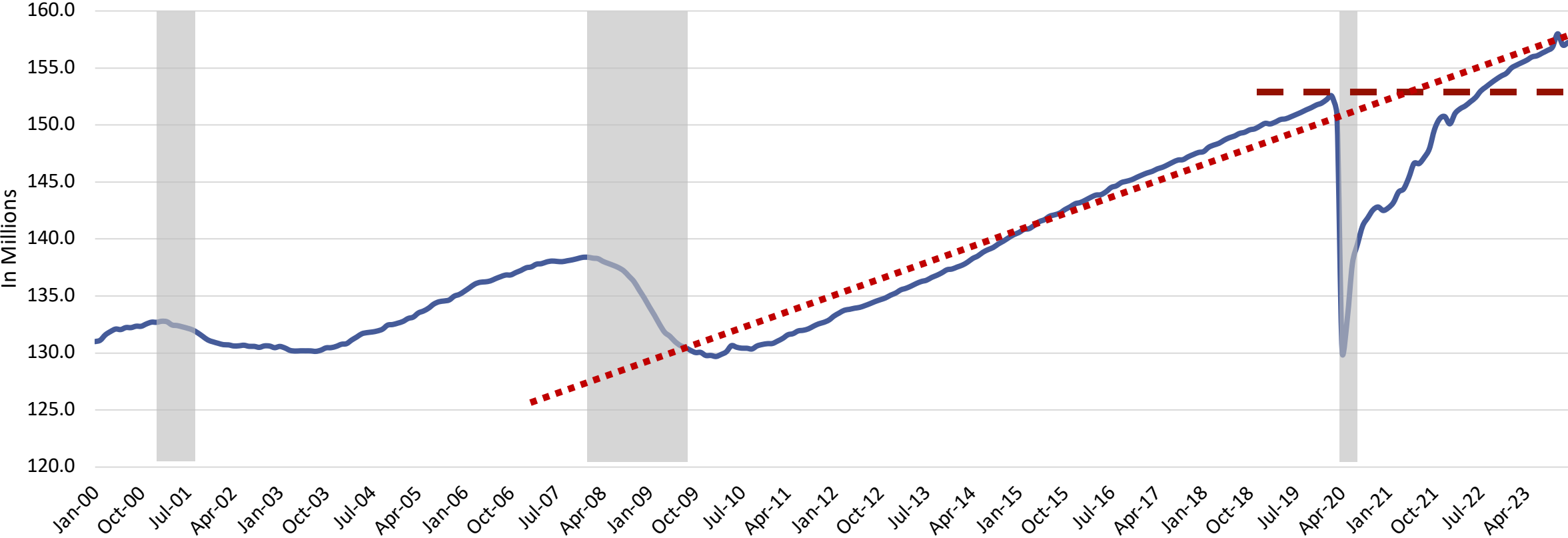
*Year-to-Date through December 2023

U.S. Employment

Seasonally Adjusted; Monthly, 2000 - 2023*

Source: U.S. Bureau of Labor Statistics

Recession Period



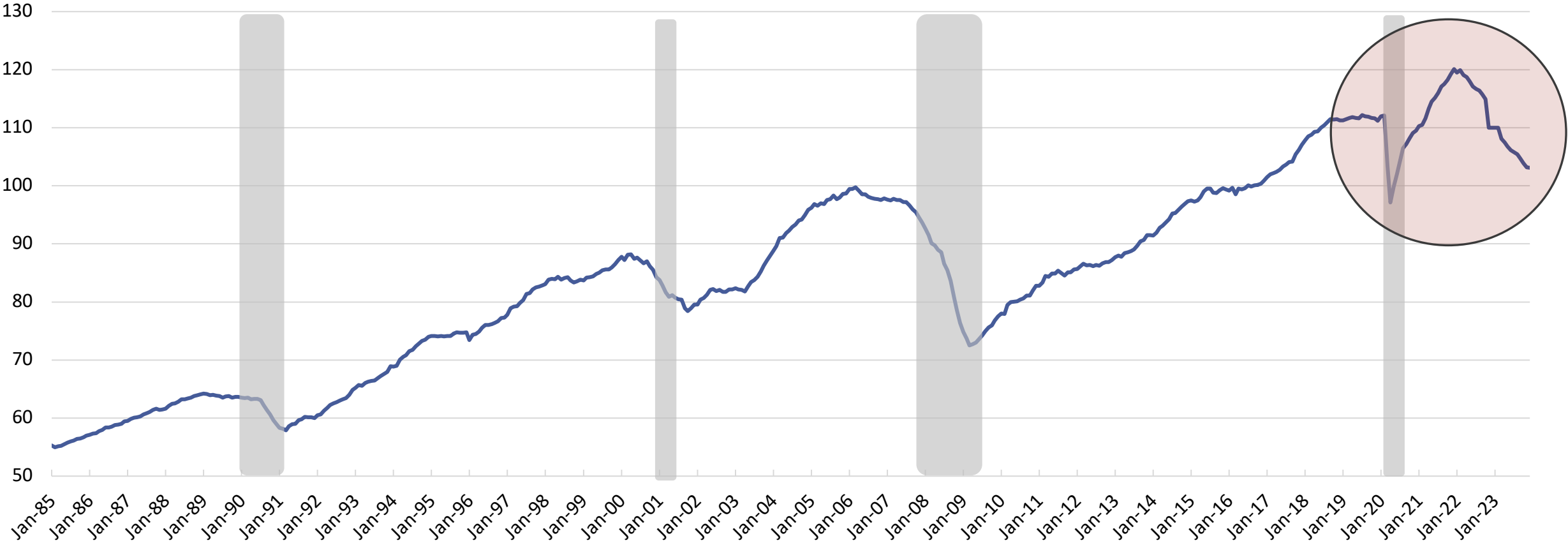
*Through December 2023

U.S. Leading Economic Index

Monthly, 1985 - 2023*

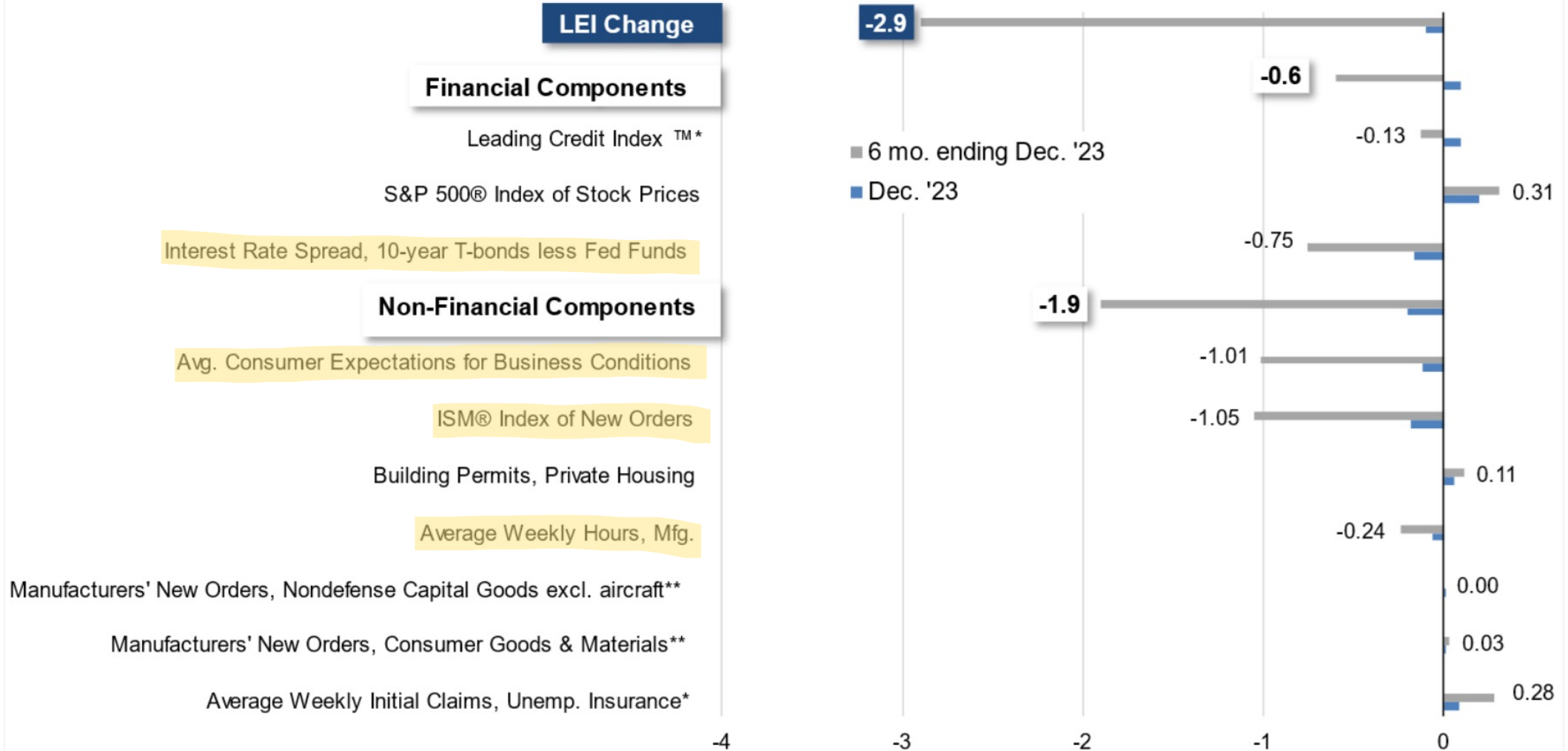
Source: The Conference Board

Recession Period



*Through October 2023

The Conference Board Leading Economic Index® and Component Contributions (Percent)



Source: The Conference Board

* Inverted series; a negative change in this component makes a positive contribution.

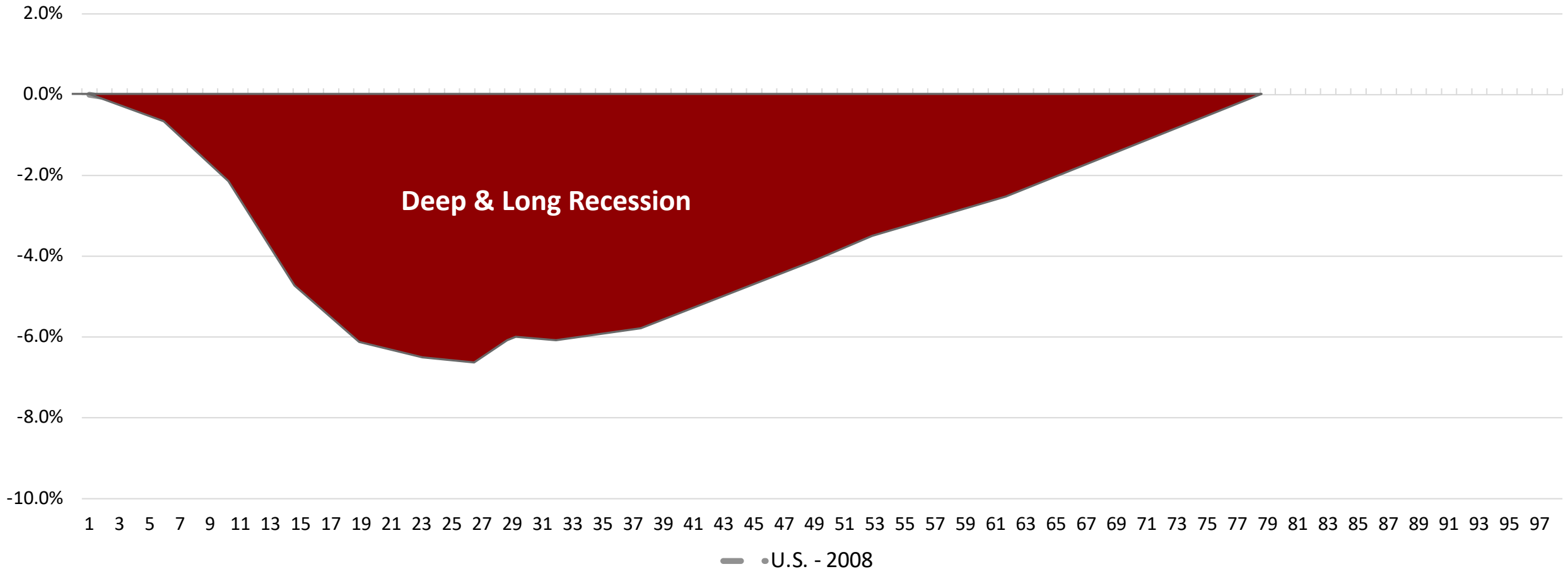
** Statistical Imputation

LEI change might not equal sum of its contributions due to application of trend adjustment factor

Reminder of how we got here...

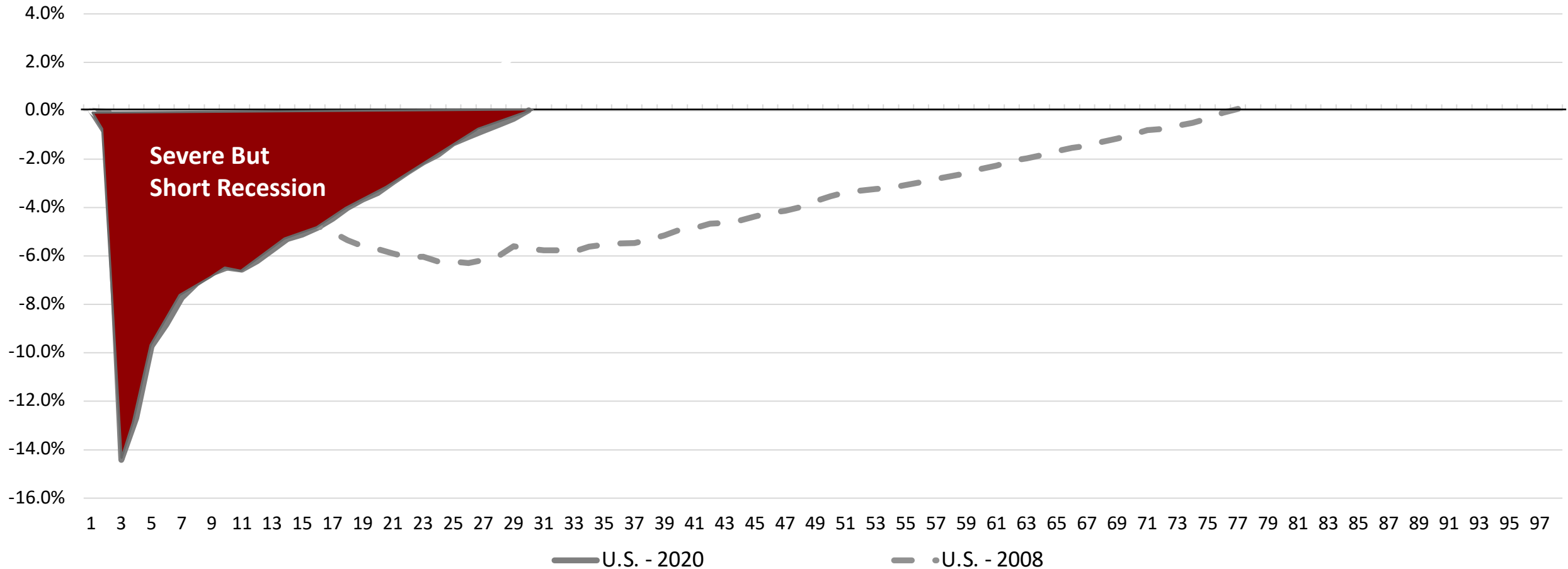
Covid Recession – What the Feds thought would happen...

Employment - Seasonally Adjusted; Monthly Employment Percent Change Since Peak Levels (Jan 08'/Feb 20') Source: Bureau of Labor Statistics



Covid Recession – What actually happened...

Employment - Seasonally Adjusted; Monthly Employment Percent Change Since Peak Levels (Jan 08'/Feb 20') Source: Bureau of Labor Statistics

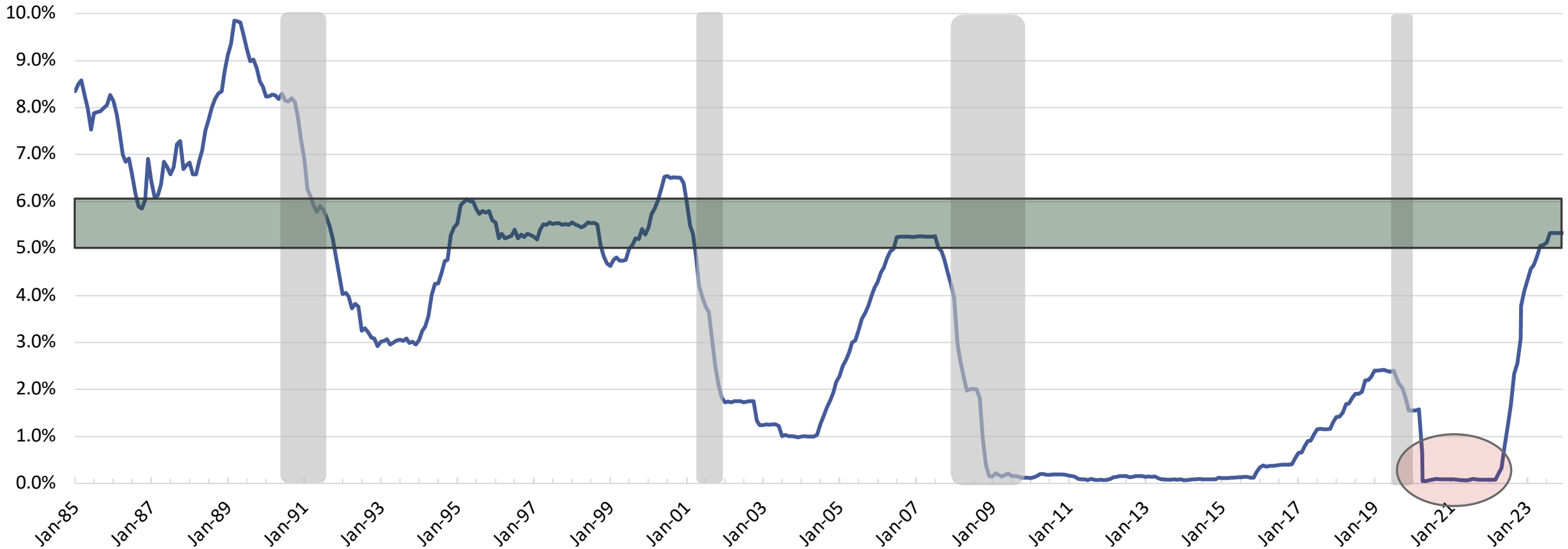


Federal Funds Effective Rate

Not-Seasonally Adjusted; Average Monthly, 1985 - 2023*

Source: Board of Governors of the Federal Reserve System

Recession Period



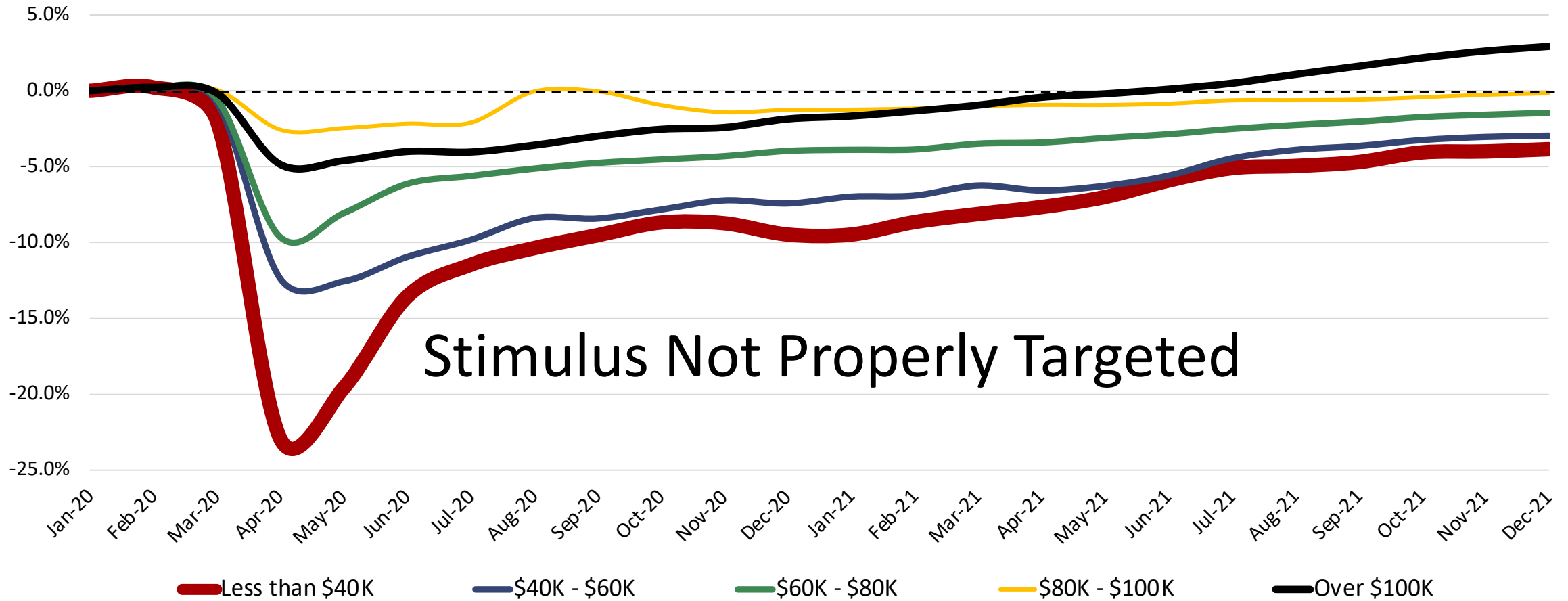
*Through December 2023

The result -
Lots of spending; Lots of easy money...



Covid Recession – Impact by income group...

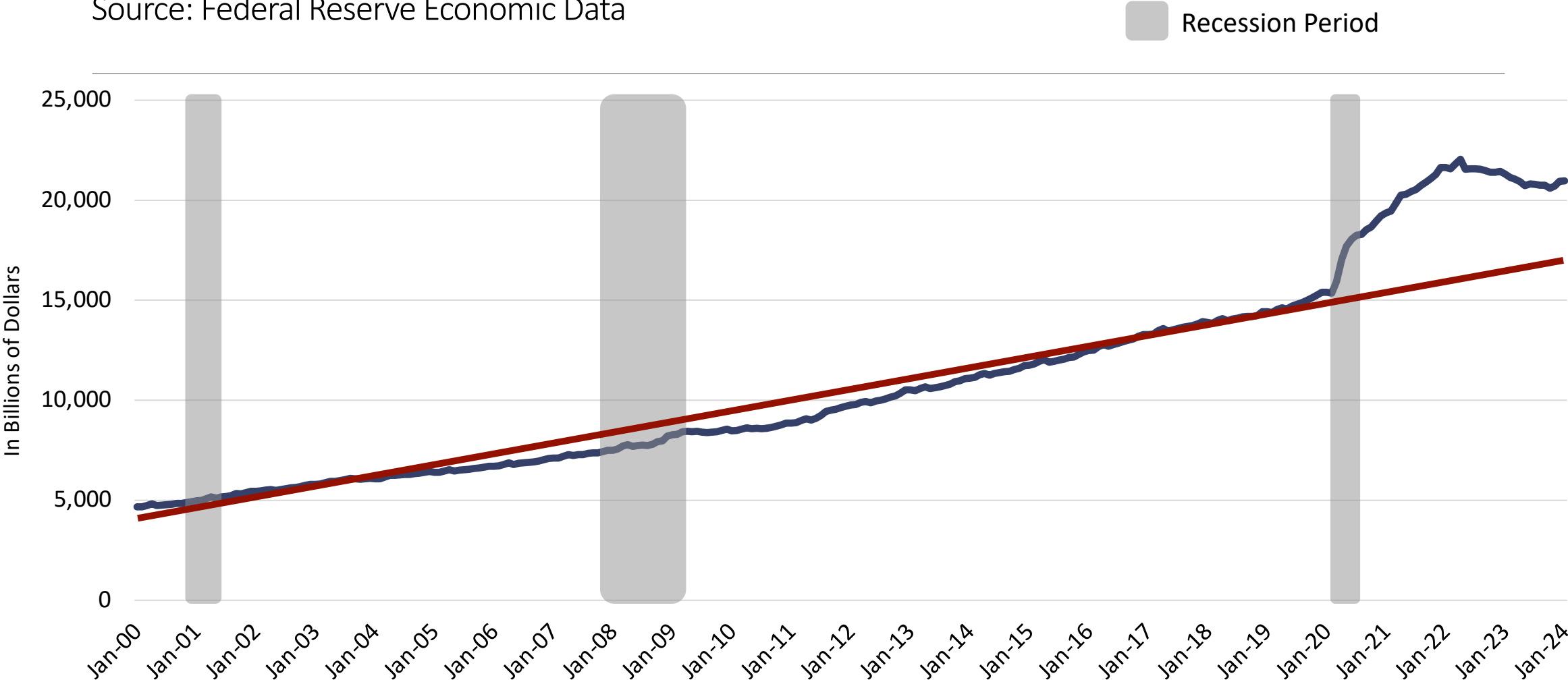
Seasonally Adjusted; Percent Change from January 2020 Source: Bureau of Labor Statistics



U.S. Money Supply (M2)

2000 – 2024*

Source: Federal Reserve Economic Data

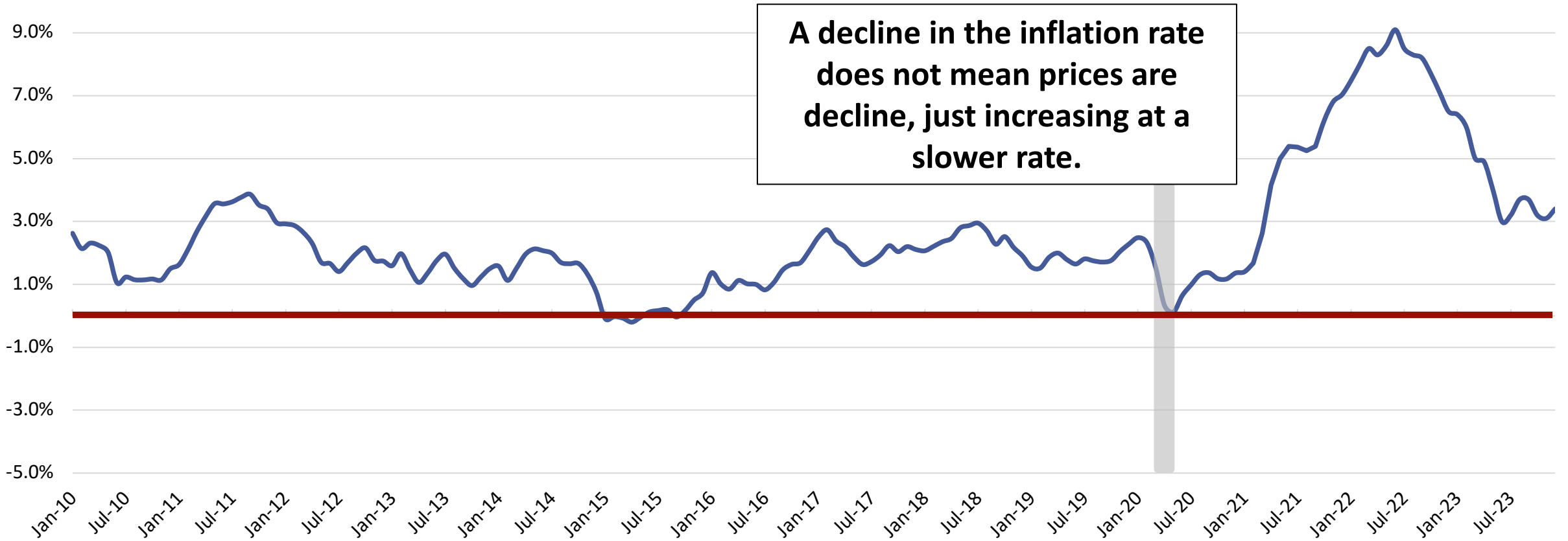


*Through January 2024

Consumer Price Index

All Items CPI, Non-Seasonally Adjusted; YoY Percent Growth, 2010 - 2023*
Source: U.S. Bureau of Labor Statistics

Recession Period



*Through December 2023

Money Supply Concerns?

4.3% Decline in M2

For the first time in 9 decades, M2 money supply is meaningfully declining. M2 has now declined by 4.3%, **representing the biggest drop since 1933**. The reason the decline in M2 is concerning is that if the money supply is shrinking, it means people and businesses will forgo certain purchases. **This is typically a recipe for a recession but very good news for inflation.**

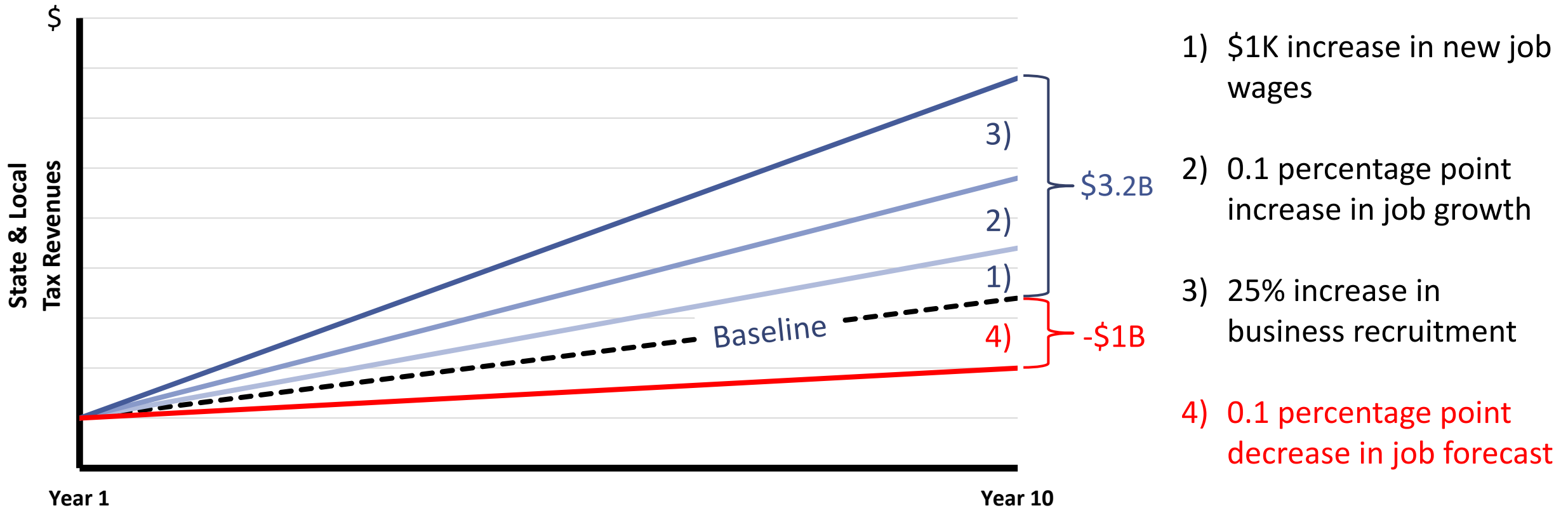
Why does this matter?

- The story **explains** why incomes/spending have been so high and resulted in very large **temporary statewide tax revenue surpluses**.
- It also explains why a recession is (at some point) around the corner and that a large **portion of the current revenue surplus is still temporary**.
- **To get through a recession, AZ will need an extra \$1.5B to \$2.5B in reserves** if services are to be maintained, borrowing is to be limited, and tax increases are to be avoided.

Why does this matter?

- There is money in your **current revenue base** that **won't be there next year.**
- **We borrowed significantly from the future**, so thank your kids (and later their kids) for paying off our debt.
- **Will Arizona be different? Most likely...**

Fiscal Benefits from Economic Enhancements (or losses)



- 1) \$1K increase in new job wages
- 2) 0.1 percentage point increase in job growth
- 3) 25% increase in business recruitment
- 4) 0.1 percentage point decrease in job forecast

The Local Economy





Job Growth by State 2023

State Ranking

Source: U.S. Bureau of Labor Statistics

Arizona is usually top 5, so what happened?

Rank	%	State	Rank	%	State
1	4.29%	Nevada	11	2.55%	Pennsylvania
2	3.64%	Texas	12	2.54%	Massachusetts
3	3.46%	Florida	13	2.53%	Delaware
4	3.17%	Idaho	14	2.49%	North Carolina
5	2.83%	Washington	15	2.38%	Georgia
6	2.73%	Wyoming	16	2.38%	Oregon
7	2.66%	Kentucky	17	2.34%	South Dakota
8	2.60%	New Mexico	18	2.28%	Hawaii
9	2.57%	Utah	19	2.21%	North Dakota
10	2.57%	South Carolina	20	2.17%	New Hampshire
			29	2.09%	Arizona

*Through December 2023

Percent Growth by State from Pre-COVID Peak

State Ranking

Source: U.S. Bureau of Labor Statistics

Rank	%	State	Rank	%	State
1	11.5%	Idaho	11	5.6%	South Carolina
2	9.8%	Utah	12	5.3%	Arkansas
3	9.7%	Nevada	13	5.0%	Tennessee
4	8.7%	Florida	14	4.0%	Washington
5	8.7%	Texas	15	3.9%	Alabama
6	7.2%	Montana	16	3.8%	Delaware
7	7.0%	North Carolina	17	3.7%	Indiana
8	6.5%	Arizona	18	3.4%	Kentucky
9	6.3%	South Dakota	19	3.3%	Colorado
10	5.9%	Georgia	20	3.2%	New Jersey

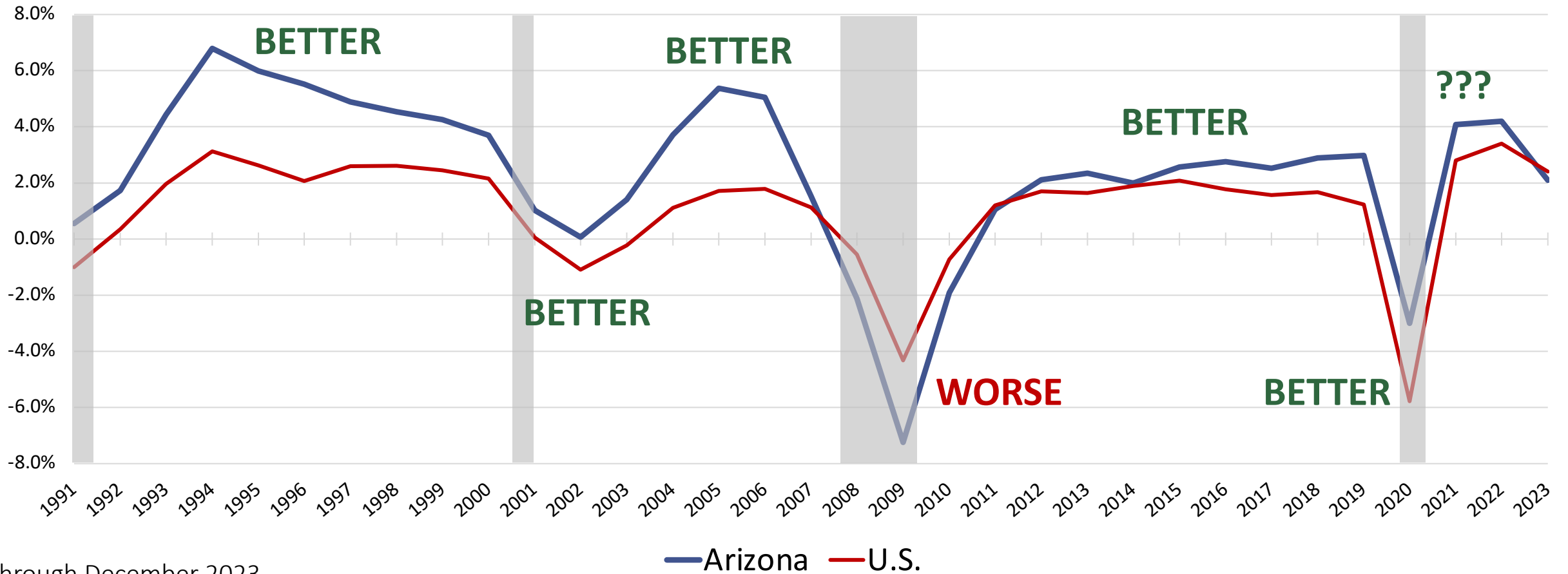
*Through December 2023

Arizona and U.S. Job Growth

Annual Percent Growth 1985 - 2023*

Source: U.S. Bureau of Labor Statistics; AZ Office of Economic Opportunity

Recession Period



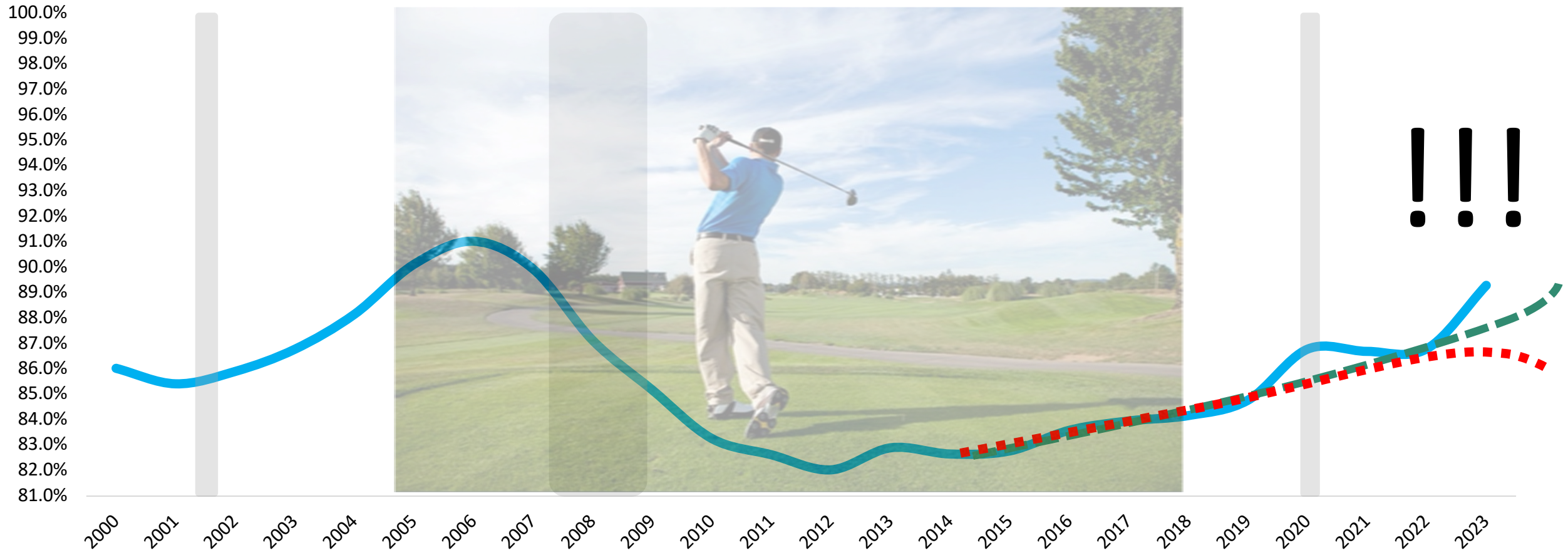
*Through December 2023

— Arizona — U.S.

Quality Measure – PCPI as a Percent of the U.S.

Arizona as a Percent of U.S.; Annual 2000 - 2023
Source: U.S. Bureau of Economic Analysis

Recession Period



What is Arizona's story?

- AZ has a fairly resilient economy.
- This occurred not by accident, but **was deliberate**.
- Resilient economies **perform better during recessions**.
- Therefore, **volatility in tax revenues is modest** compared to other states.
- **Need to keep diversifying, need to build on our strengths.**

Policy Choices: What Matters in Growing the Economy?

- Tax Rates
- Econ Development Programs
- Workforce (quality/avail/cost)
- Transportation Infrastructure
- Marketing
- Responsible Regulations
- Balanced Budget
- Reliable/Cost Effective Energy
- Water
- Housing Affordability
- Economic Diversity



Short term forecast for AZ?

- Nationally, the recession could be dampened by continued govt spending and the Fed keeping the economy flooded with money.
- AZ will not be hit nearly as hard and we will realize fewer job losses.
- Instead, the next AZ recession will be the **“Jobs Posting Recession.”**



Rest of the decade?

- AZ will still be a top 5 state for growth.
- **But, can we also be top 5 for quality growth?**
- AZ can potentially post a very strong expansion, from 2025-2035, with the right investments and policy focus.
- But, will we do this?

State and Local Budgeting

A nighttime photograph of a city street scene. In the foreground, a multi-lane road shows long, horizontal light trails from moving vehicles. To the left, a modern building with large glass windows is illuminated from within. A prominent sign for 'Verve' is visible, along with a poster for 'Young People Revolution #YPR'. The background features several tall, modern skyscrapers with lit windows against a dark, twilight sky. The overall atmosphere is urban and vibrant.

Getting through a recession?

- Severe Recession – Need about \$2.5B
- Mid Level Recession – Drops to \$2.0B
- **Mild Recession – Requires about \$1.5B**

Getting through a recession?

- Current Rainy Day Fund Monies = About \$1.5B
- \$400M+ was added in 2021 to hedge against possible income tax cut problems.
- Conclusion – If managed properly, we will not require massive budget cuts or tax increases.

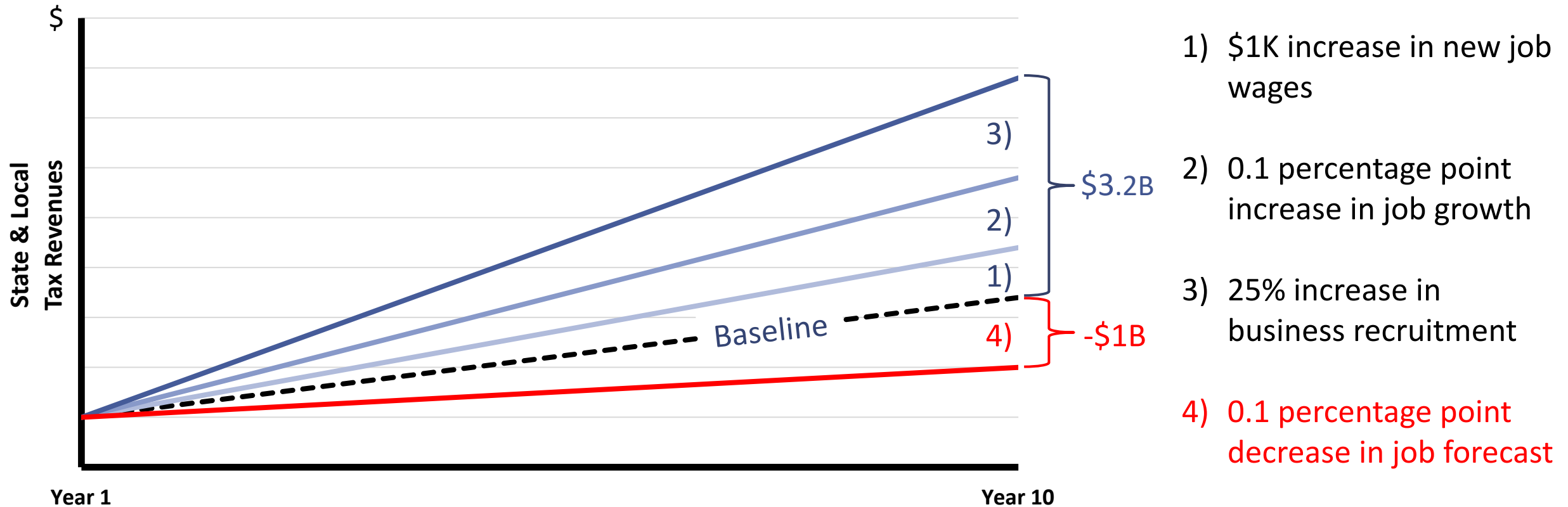
Getting through a recession?

- Risks – We can't stop investing.
- What do we do?
- Bring money to the table...High ROI projects.
- **Will the state come after local distributions?**

A man with a shaved head and sunglasses, wearing a dark jacket, is shown from the chest up. He is holding two glowing spheres in his hands, one red and one blue. The background is dark. The text "Long Term Consequences:" is overlaid in large, bold, blue letters.

Long Term Consequences:

STILL TRUE: Fiscal Benefits from Economic Enhancements (or losses)



Arizona Public Policy



ROUND

Housing Affordability?

Why so much debate?

What data to review?

New solutions?

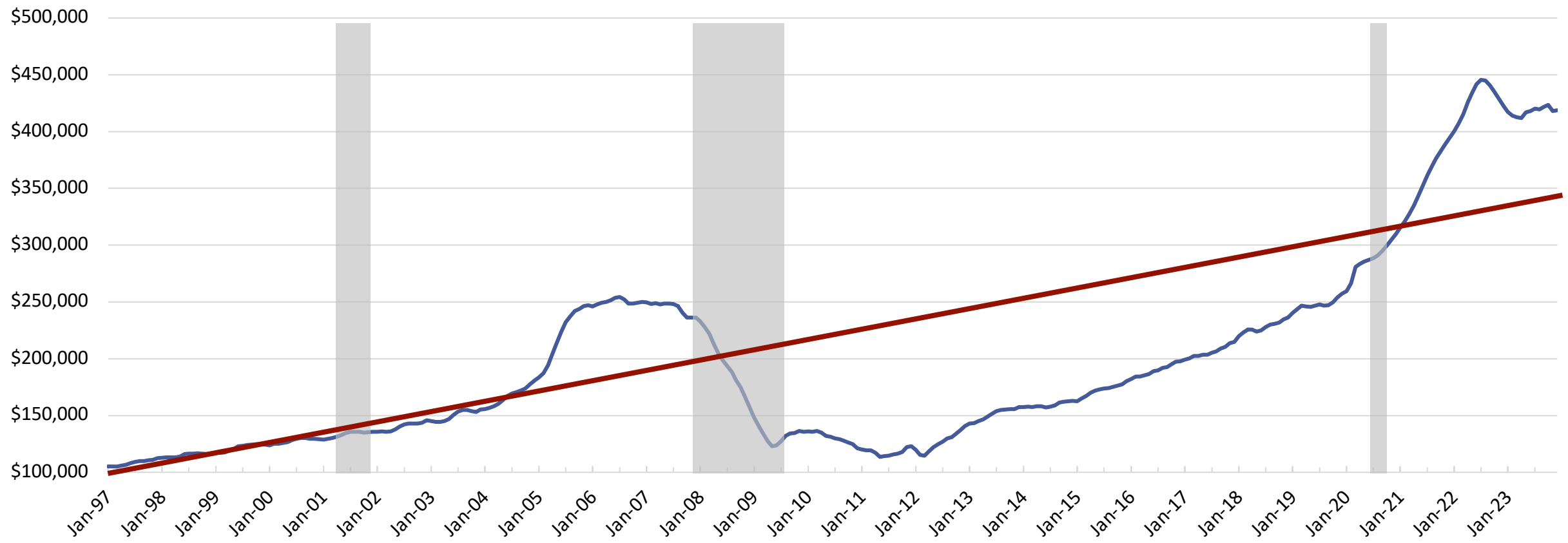
General Housing Affordability

Arizona Median Price of Homes Sold

1997-2023*

Source: Zillow Research

Recession Period



*Through December 2023

Annual Household Expenditures

Arizona Average

Source: U.S. Bureau of Labor Statistics

Category	2005 % of Annual Expenditures	2010 % of Annual Expenditures	2022 % of Annual Expenditures
Housing	30.0%	33.6%	34.3%
Transportation	21.5%	16.3%	23.0%
Food	13.1%	13.4%	10.5%
Healthcare	5.9%	6.1%	7.7%
Entertainment	4.8%	6.3%	3.8%
Apparel	3.8%	4.9%	2.4%
Education	1.5%	0.6%	1.4%
Other	19.4%	18.8%	16.9%

Arizona (**Workforce**) Housing Shortage Estimates?

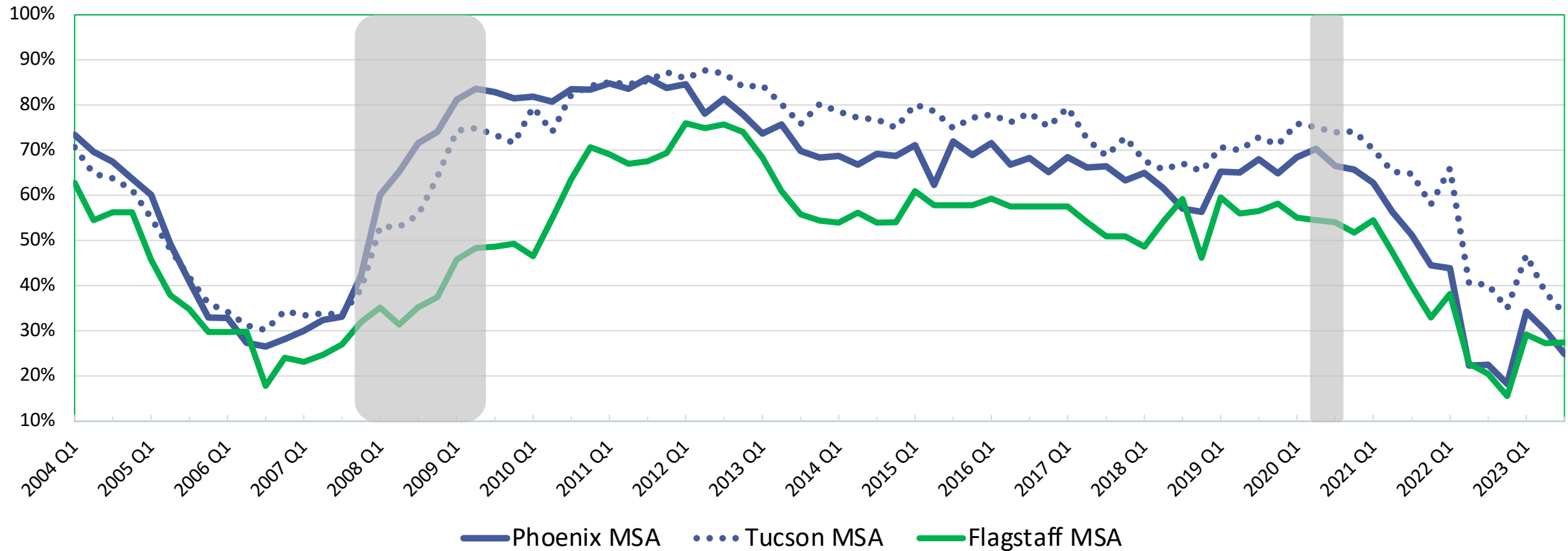
Up For Growth Study	Common Sense Institute Study	Rounds Consulting Group Estimate
122,700 Units	95,800 Units	40,000 – 80,000 Units

Housing Affordability – Phoenix, Tucson & Flagstaff

Share of Homes Sold Affordable to Families Earning the Median Income; Quarterly, 2004 - 2022*

Source: NAHB Housing Opportunity Index

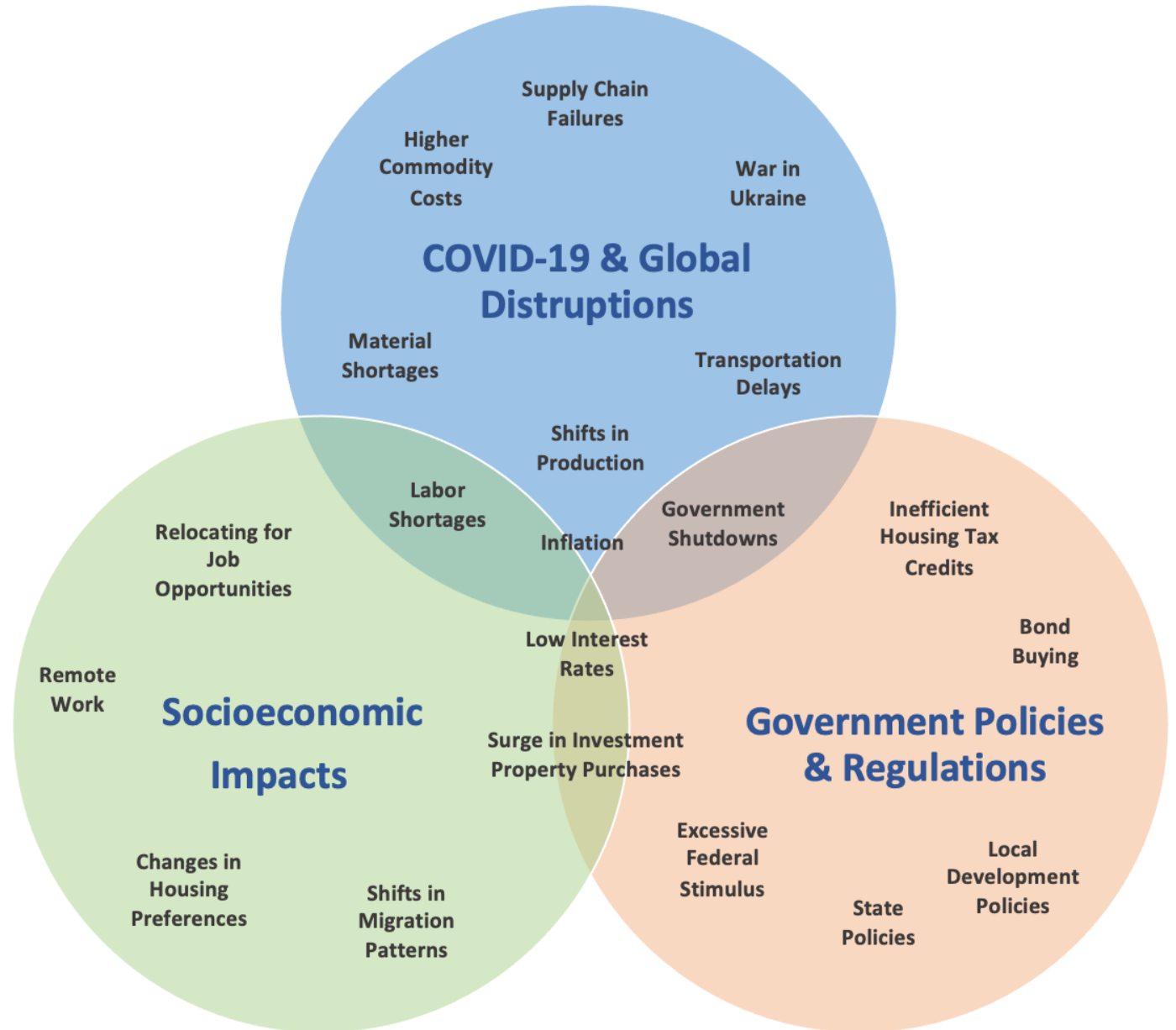
Recession Period



*Through Q3 2023

High Prices?

Some local issues, most national...



Homelessness v. Housing Affordability

Arizona has one of the worst homelessness crises in the nation, according to data from the U.S. Department of Housing and Urban Development (HUD) that showed homelessness across the country increased by 1% but increased by over 20% in Arizona from 2020 to 2022.

- Need to focus on a solution to end homelessness, instead of just providing shelter.
- It is true that some of the homeless population is homeless because they cannot afford housing due to unemployment or other constraints; however, the root cause of homelessness is mental illness, substance abuse, or individuals who were orphaned.

Solutions to ending homelessness and housing affordability are two very different things.

Bumper Sticker Case Studies:



Case Study: Higher Ed

Annual gains by becoming average in attainment...

9,500
Additional High
School Graduates



19,500
Additional College
Enrollees



14,800
Additional College
Graduates



\$1.4B
Additional Annual
Earnings



\$497.6M
New Statewide Tax
Revenues



Case Study: Environmental Tech

GROWING ARIZONA'S NEW ECONOMY AND SUSTAINABILITY JOBS FROM 2.0% TO 2.6%

**\$7.0 BILLION
ECONOMIC
OUTPUT**



**Total direct,
indirect, and induced
economic activity**

**40,400
JOBS**



**Total direct,
indirect, and
induced jobs**

**\$2.4 BILLION
WAGES**



**Total direct,
indirect, and
induced wages**

**\$243.6 MILLION
TAX REVENUES**

**Total state and local
(city and county)
tax revenues**

x2

We just found \$1B in annual
net-new tax revenues.

(with just 2 policy initiatives)

Govt. - Change the Narrative

- Are you an inefficient user of taxpayer dollars?
- Or, are you an economic development entity?
- **Show your ROI.**

How to get people to listen?

- Think bigger picture, but implement individual and innovative projects.
- Each region will have a different story and a different list in projects.
- Again, do the math.

Things to Consider - Costs or Savings:

- GPLET?
- Lack of TIF?
- Better Affordable Housing Programs?



Costs or Savings:

- Foster Kid Programs?
- Criminal Justice Reform?
- Apprenticeships?
- Tourism Funding?
- Homelessness Programs?



Prove it! Do the Math!



Thank You!



Questions...