

Breakfast with the Economists: Mid-Year Economic Update

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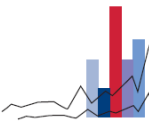


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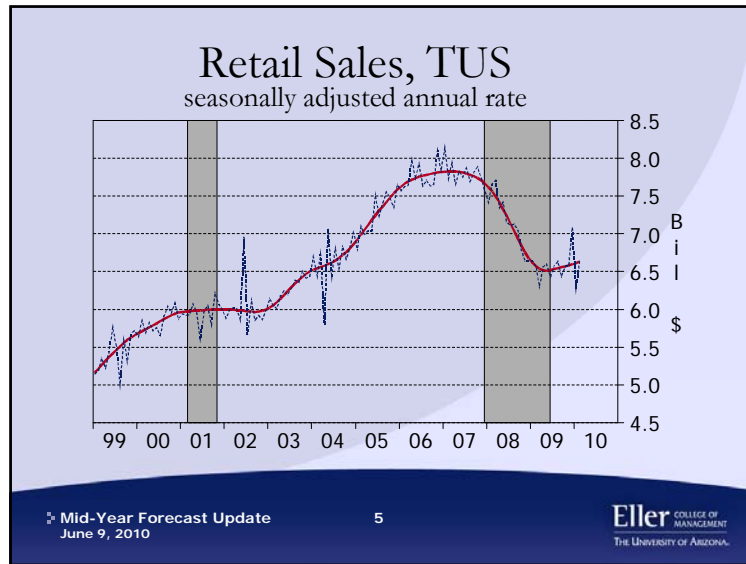


Consumer Spending

- Retail sales bottomed in June 2009 (nominal terms) and is growing at 8.8% AR
 - Spread across categories
- Restaurant & bar sales bottomed in October

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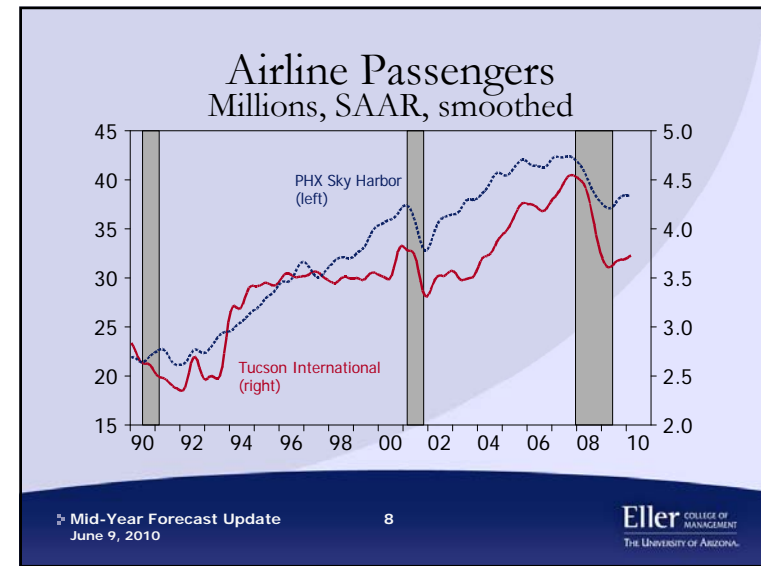
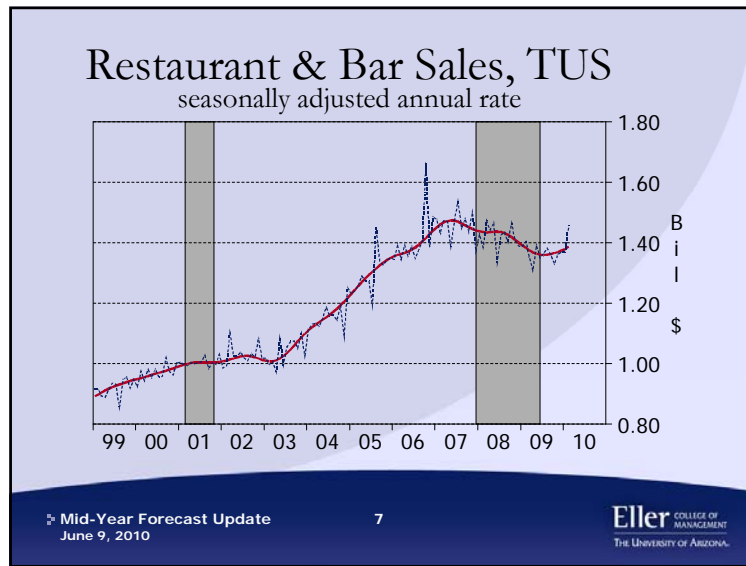


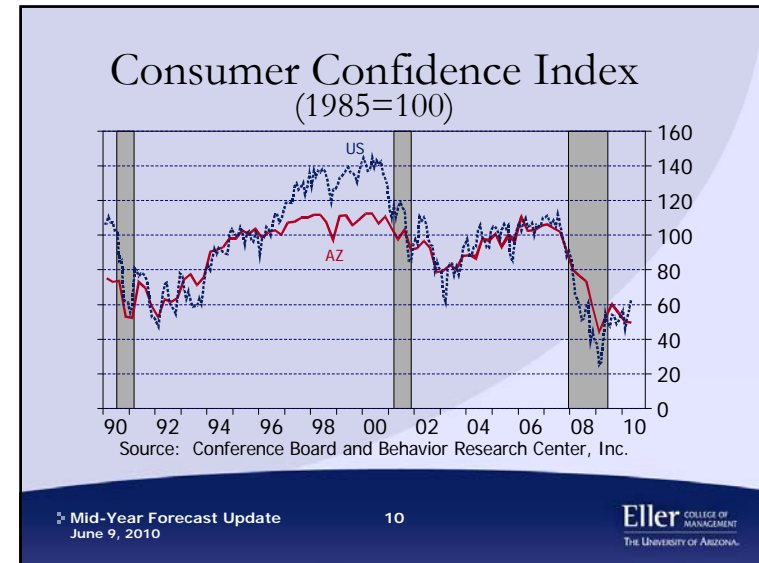
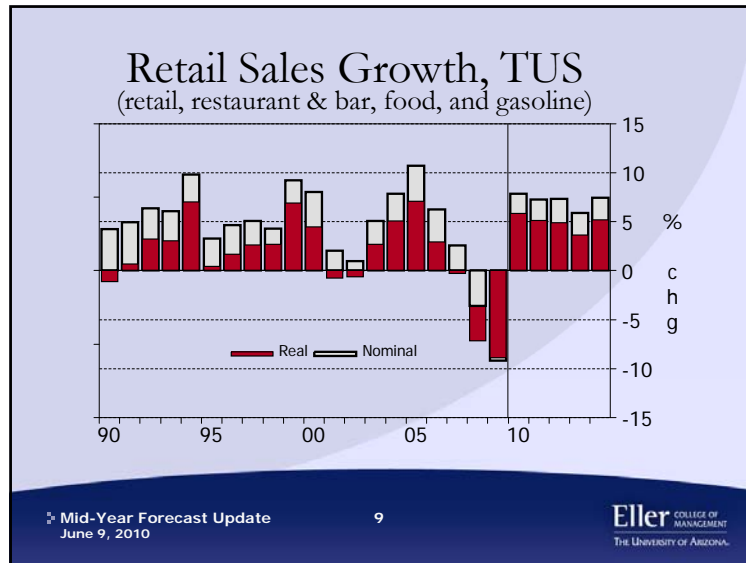
Spending Growth, Past 6 Months (AR), Arizona

| | % change | % of total |
|----------------------------------|----------|------------|
| Retail sales, total | 8.8 | - |
| Motor vehicle dealers | 2.6 | 10.3 |
| Miscellaneous automotive | 11.2 | 4.3 |
| Furniture, home furnishings | 20.7 | 6.4 |
| Building material, lawn & garden | 5.9 | 7.0 |
| Food & liquor stores | 0.0 | 8.2 |
| Miscellaneous retail | 19.5 | 15.8 |
| Clothing & accessories | 11.3 | 5.8 |
| General merchandise | -3.1 | 18.8 |
| Restaurant & bar sales | 0.0 | - |

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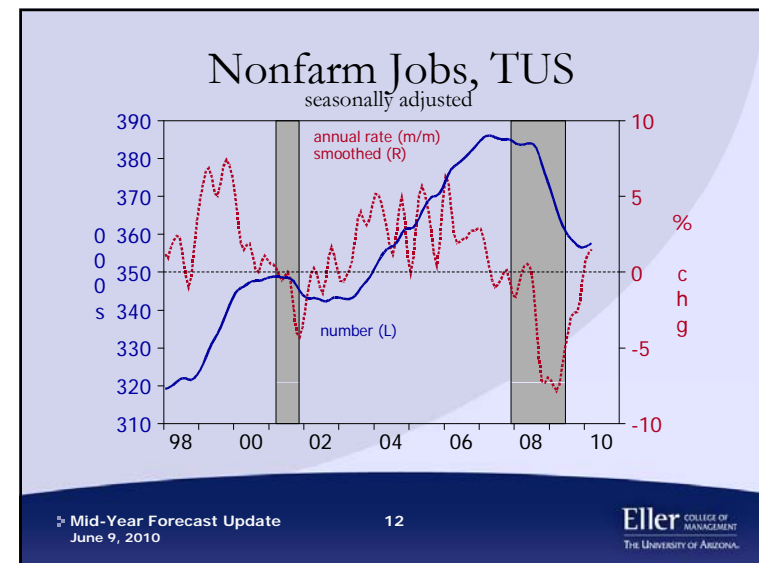


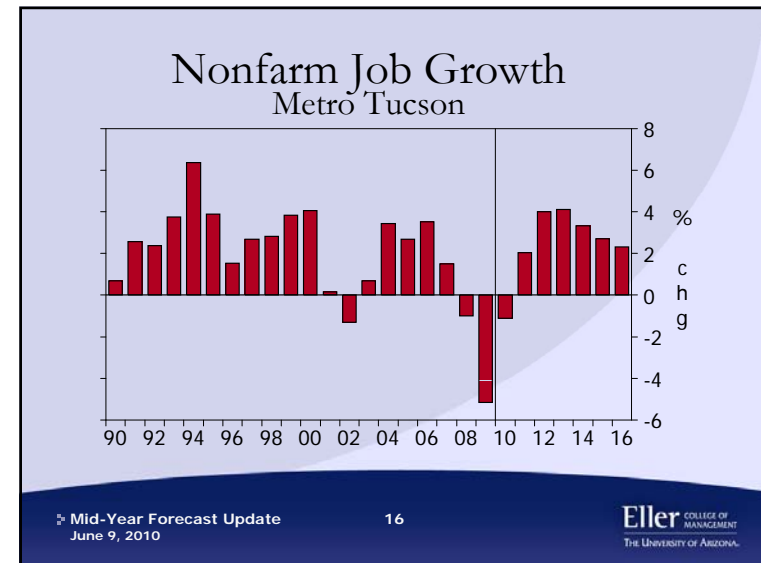
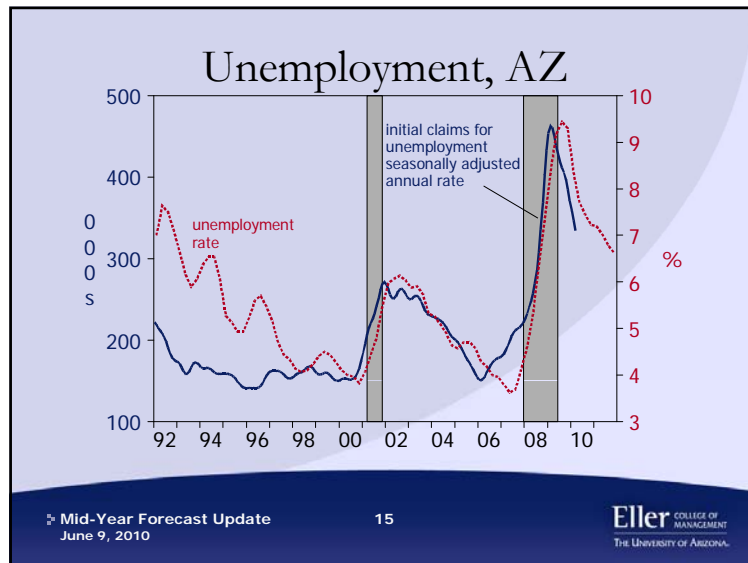
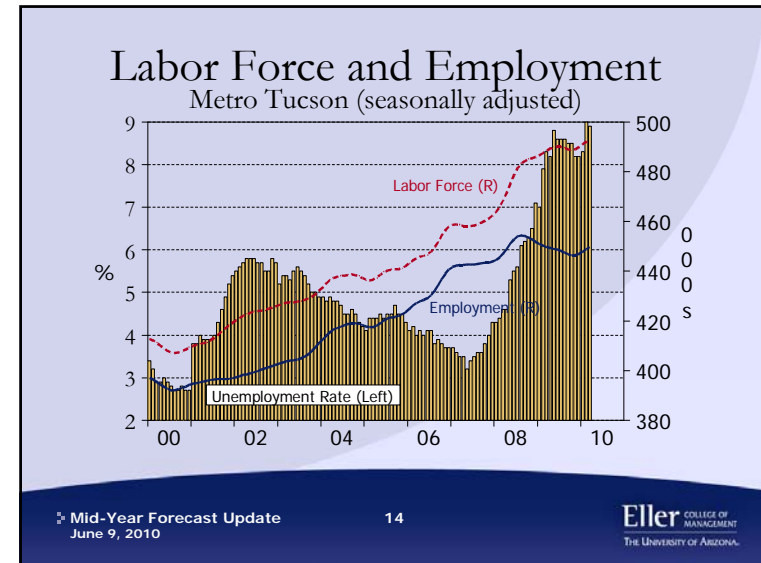
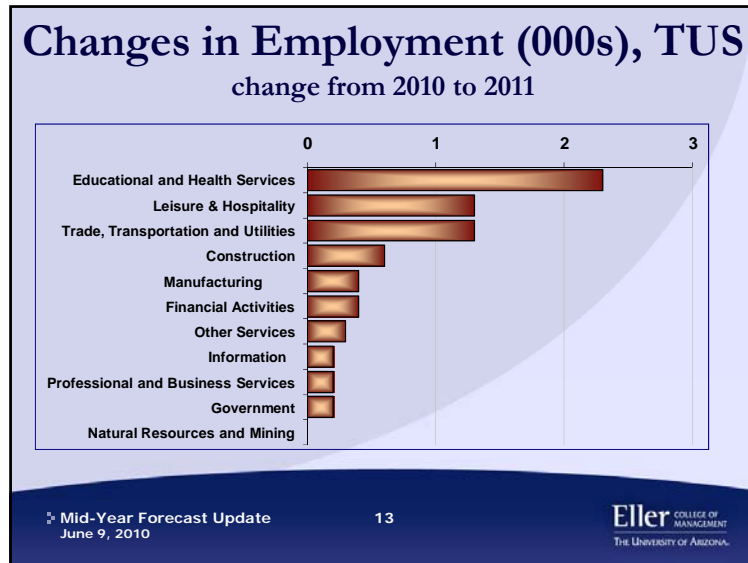
What's Fueling Spending?

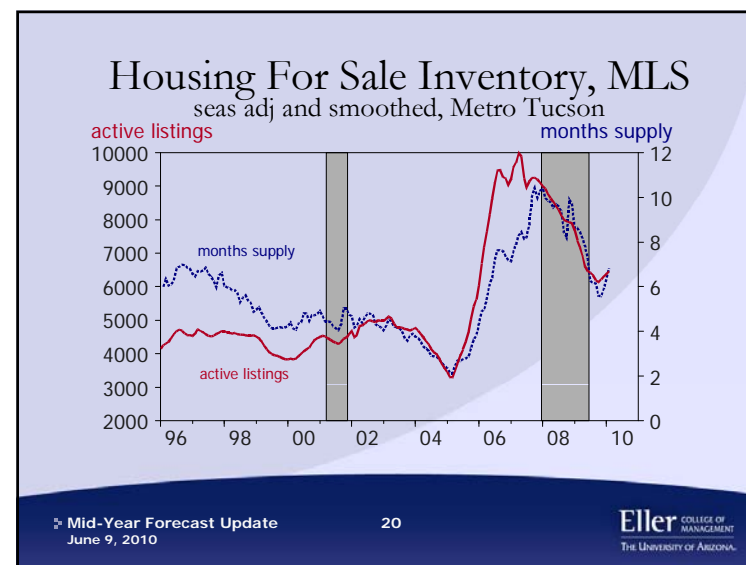
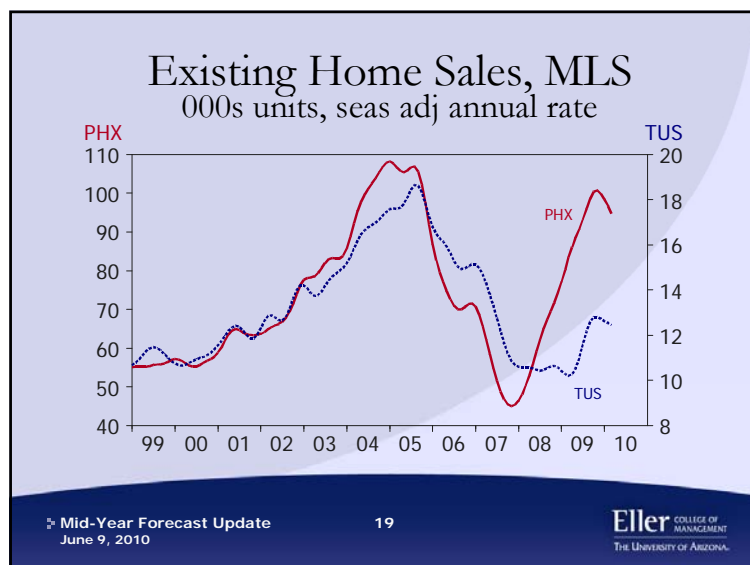
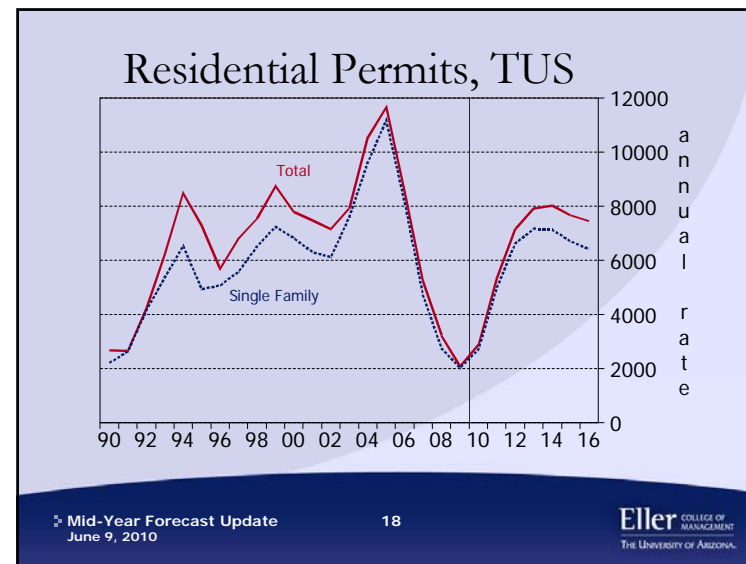
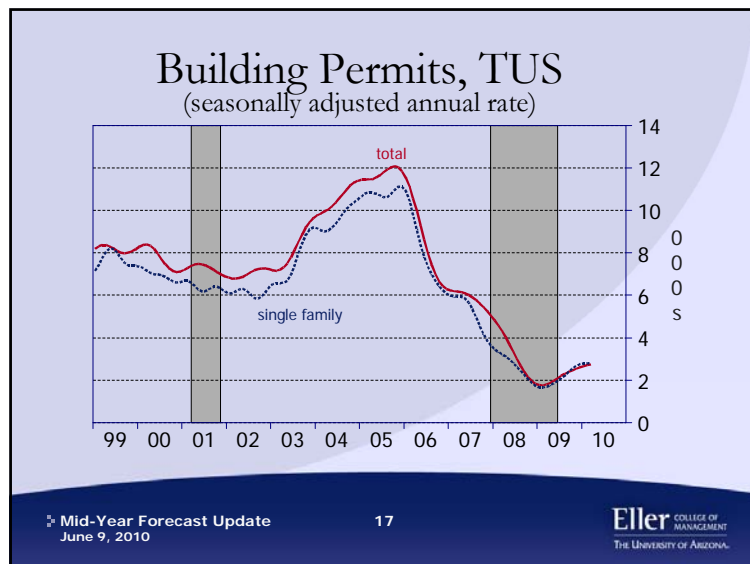
- Releasing "pent-up demand"
 - Upper income households
- Savings rate is moving lower
- Federal rebate programs
 - Cash for clunkers, homebuyer credits
 - Rebates for energy efficient appliances, windows
- No longer making mortgage payments
 - Delinquencies, strategic defaults, etc.
- Personal income growing again

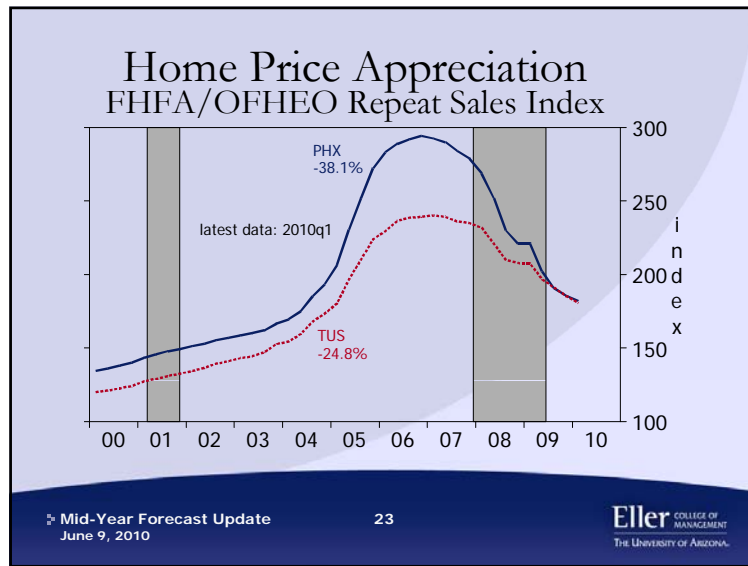
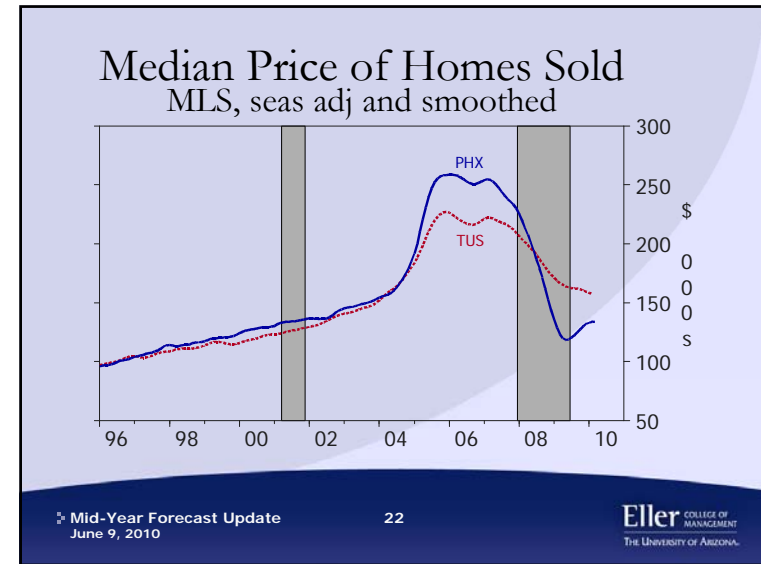
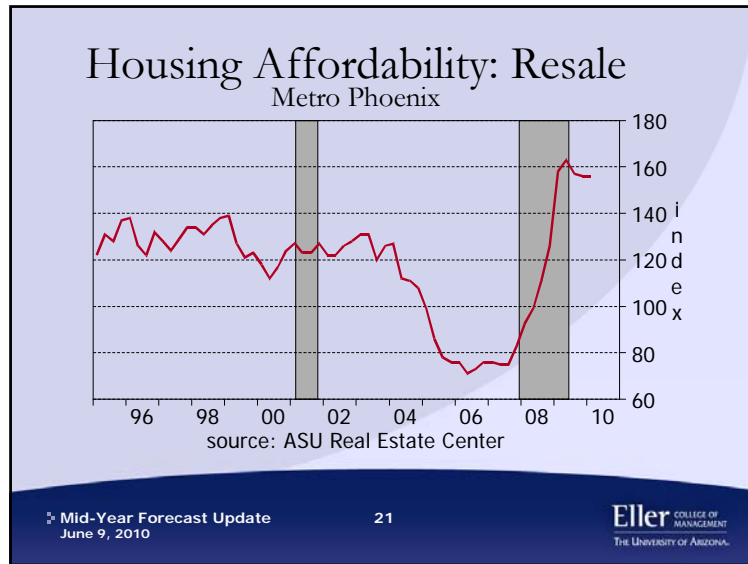
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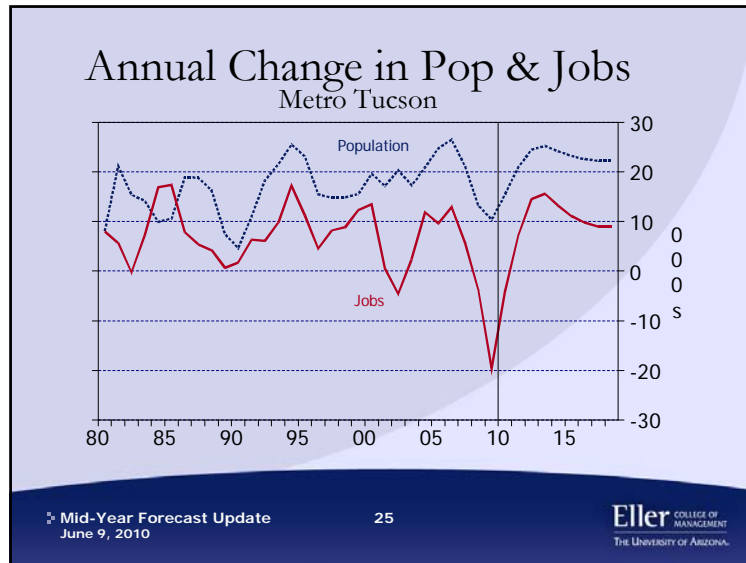
Foreclosures, April 2010

Source: RealtyTrac

| | Foreclosure rate | Properties in foreclosure | |
|--------------|------------------|---------------------------|------------------|
| | | 1 in every X Houses | Notices in April |
| Arizona | 169 | 16,088 | 124,611 |
| Maricopa Co. | 138 | 11,323 | 89,443 |
| Pima Co. | 242 | 1761 | 11,458 |
| Pinal Co. | 109 | 1331 | 10,964 |

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Near Term Outlook

- Recession in AZ is over, recovery will be slow
 - Drag from real estate and public sector
- Risks
 - Oil spills, euro-zone turmoil, volatility in stock markets
 - Policy mistakes
 - AZ's new immigration law
- Voters deserve credit
 - But Arizona still facing a structural deficit

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America's Most Innovative Cities Forbes.com

| | | | |
|----|---------------|----|------------------|
| 1 | San Jose | 11 | Palm Beach |
| 2 | Austin | 12 | Minneapolis |
| 3 | Raleigh, NC | 13 | Washington, D.C. |
| 4 | San Francisco | 14 | Rochester, NY |
| 5 | Seattle | 15 | Albany, NY |
| 6 | San Diego | 16 | Boise, ID |
| 7 | Madison, WI | 17 | Oxnard, CA |
| 8 | Boston | 18 | Denver |
| 9 | Provo | 19 | Tucson |
| 10 | Portland, OR | 20 | Bridgeport, CN |

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ANGST!

THE WORD *DU JOUR*

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Unemployment

| | |
|---------------|-------|
| December 2007 | 5.0% |
| December 2009 | 10.0% |
| APRIL 2010 | 9.9% |

GOOD NEWS?

MAY 2010 9.7%

Currently 15 million unemployed

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Unemployment

MAY UNEMPLOYMENT 9.7%

46% have been unemployed for over 6 months

32% have been unemployed for over 1 year

Worst long-term unemployment since 1930s

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Inflation - Deflation

May 2010 = -.01%

Core Price Index Slide in April
to its Lowest Level in 44 Years

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Growth in GDP

GOOD NEWS!

Third Quarter 2009 + 2.2%
Fourth Quarter 2009 + 5.6%
First Quarter 2010 + 3.0%

**STILL TOO SLOW TO SIGNIFICANTLY
CHANGE UNEMPLOYMENT RATE**

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Growth

Technically the recession is over!
However--

**The recession dating committee
has yet to go out on a date**

National Bureau of Economic Research

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GROWTH

RISK = ANGST

Is this a hollow recovery?
Like a piñata without candy?
Euro crisis = double dip recession?

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Consumption

Consumers are decreasing their debt at lightening fast pace.

Mortgage Defaults
Strategic Mortgage Defaults

THINK--
Debt Destruction – Not Repayment
More money to spend on consumption!

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Investment Spending

- Business confidence low but improving
- **Inventories are a bright spot**
- New home building showing signs of life
- Loans are still difficult to get

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Investment Spending

Manufacturing Capacity Utilization
GOOD NEWS!

April 2010 73.7%
Up 4.5 % From April 2009

Slowly Improving!
80%+ = Normal

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Fiscal Policy

Deficit

Fiscal 2009-\$1.4 TRILLION
Projected 2010
-\$1.5 TRILLION

Projected 2011
-\$1.3 TRILLION

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Fiscal Policy

February 2010 \$220 Billion Deficit

All Time Monthly World Record
for Deficit Spending!

20 Consecutive Months of Budget Deficits
First Time Ever

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Fiscal Policy

ANGST

44% of federal government
spending is currently being
financed by borrowing

NOT SUSTAINABLE!

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Fiscal Policy

ANGST

Recent Gallop Poll

81% people said that they trust
government to do what is right some
of the time or never

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Deficits and Unfunded Liabilities

"Everyone wants to go to heaven,
but nobody wants to die!"
- Songwriters Dorsey & Thomas

SOLUTION =

National Commission on Fiscal Responsibility and Reform

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Government Spending

Deficit for fiscal 2009 = **10.0%** of GDP

3% of GDP is normally considered safe

ANGST
Our we on the verge of a sovereign debt crisis?

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Euro Zone Risk Sovereign Debt Crisis

Once there were three little pigs
Now – there are five little PIIGS
Portugal
Ireland
Italy
Greece
Spain

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Fiscal Policy

MANDATORY SPENDING
1965 29% OF BUDGET
2010 66% OF BUDGET

ADD DEFENSE in fiscal 2010
83% OF BUDGET

17% DISCRETIONARY

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Fiscal Policy

We can not grow ourselves out of this deficit

IT IS A STRUCTURAL DEFICIT

TO SOLVE THE DEFICIT PROBLEM:
TAXES MUST BE INCREASED
AND/OR
SPENDING MUST BE CUT

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FISCAL POLICY

MY PREDICTION--

THERE IS A VALUE ADDED TAX

COMING TO A STORE NEAR YOU IN THE
NOT-TOO-DISTANT FUTURE

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Monetary Policy

Brilliant Ben and the
Fantastic Federal Reserve

Our New Superhero!

SO FAR SO GOOD

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Monetary Policy

Federal Funds Rate Still Zero

ANGST

129 banks failed in 2009
73 banks have failed in 2010

772 BANKS ON FDIC WATCH LIST

- ONE OUT OF EVERY TEN BANKS -

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Monetary Policy

HYPEREXPANSIONARY MONETARY POLICY

The Federal Reserve's Balance Sheet has Exploded

| | |
|-------------|----------------|
| August 2007 | \$800 billion |
| APRIL 2010 | \$2.3 trillion |

Think Printing Lots of Money

ANGST = INFLATION

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Conclusion

We Are Facing Lots of Uncertainties

We are Worried

We Have Lots of Angst

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Conclusion

The Recession Will Not Be Viewed as Over Until -

“The Unemployed Fat Lady Sings”

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CONCLUSION

REMEMBER –

**PRIVATE SECTOR
PRODUCTION AND INCOME
PAYS FOR PUBLIC SECTOR
GOODS AND SERVICES**

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Conclusion

For the rest of the year let's be:

Patient
Productive
And YES
Avoid Angst!

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Conclusion

HAVE A SAFE AND ENJOYABLE SUMMER

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