The Alaska economy has been through three consecutive years of a mild recession. There is hope that 2019 will be the year where we begin to grow again and add jobs. A positive indicator occurred when the State Department of Labor reported growth of 500 jobs in January compared to January of 2018. This is the first month of year-over-year increase in employment since September of 2015. The Department of Labor forecasted an increase of 1,400 jobs, or 0.4% growth for the entire year. They expect the major drivers of job growth to be military, oil & gas activity and tourism.

The wildcard in this forecast is the outcome of the state government budget debate in Juneau. The Governor has proposed large cuts to government spending in the operating budget and large increases to the Permanent Fund dividend to compensate for reductions made by the prior administration. An apparent majority of legislators are opposed to the Governor’s budget and prefer a more measured pace to cuts. Conversation has begun again about broad based sales or income taxes to help fill the budget gap. Each of these options will undoubtedly affect the economy in different ways across regions of the state, industry sectors and income classes.

Responsible natural resource development has been, and continues to be, the foundation of the Alaska economy. Royalties and taxes from past projects are the primary reason we have been able to adequately fund government, pay $23 billion in dividends to residents and still have over $60 billion in savings accounts. We need to take the necessary steps to balance the government budget, but we cannot lose focus on helping a number of world-class resource projects advance. This will stimulate new jobs, private sector investment, personal wealth creation, and tax revenue to help fund government.

**Oil Prices and Production**

Alaska North Slope (ANS) crude oil prices have trended higher over the last two years. The recent low monthly average was $30.22 in January of 2016. Oil prices moved higher throughout 2017 and reached a monthly average high of $80.03 in October of 2018. ANS prices have moderated since then and averaged $65.02 for the month of February 2019. The State Department of Revenue has forecasted an annual average ANS oil price of $68.90 per barrel in fiscal year (FY) 2019 and $66 per barrel in FY 2020. Alaska’s crude oil production averaged 540,500 barrels per day (bpd) in FY 2017. This was an increase of 9,300 bpd over the previous year and the second year of production growth. This two-year positive trend reversed slightly last year when total output declined 1.2% to 534,000 bpd in FY 2018. The State Department of Revenue forecasts production to decline in FY 2019 by 1.3% and then rise by 3.5% in FY 2020 on the North Slope.

The low price environment experienced between 2015 and 2017 caused companies to cut back on spending as certain projects were no longer economically viable. This led to a reduction in State revenues and a loss of thousands of high paying oil and gas related jobs.

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**Federal Support for Resource Development**

The recent comprehensive change to the U.S. tax code includes a provision opening the coastal plain of the Arctic National Wildlife Refuge (ANWR) for oil and gas exploration and development. There will be at least two large lease sales in ANWR prior to 2028 and 50% of the federal royalties will be provided to Alaska.

There is also renewed optimism for future natural resource development in Alaska due to executive orders supporting domestic energy independence and reducing regulatory burdens. Specifically, there have been reversals of federal positions pertaining to off-shore Arctic oil exploration and regulation in the Beaufort and Chukchi outer continental shelf and climate change policy.

**New Oil Prospects**

ConocoPhillips has advanced four large-scale developments in the National Petroleum Reserve – Alaska (NPR-A), which is west of Prudhoe Bay and the Trans Alaska Pipeline System (TAPS). Greater Mooses Tooth (GMT) 1 and 2, CD-5, and Willow are all planned to connect through pipelines via Alpine to move the oil east back to TAPS. GMT-2 is under construction this winter and could produce up to 40,000 bpd starting in 2021. GMT-1 has just begun production at about 3,000 bpd and is projected to reach peak production at 30,000 bpd. CD-5 is producing approximately 37,000 bpd, far beyond the 16,000 bpd that was originally forecasted. Willow is the largest find in the area. Discovered in 2017, it is expected to produce up to 100,000 bpd starting in 2024 or 2025. It will require the investment of $2 to $3 billion, including the construction of a new fluid processing facility. Together, these projects are creating thousands of construction jobs, hundreds of permanent positions, and $5 to $6 billion in direct investment. Royalties and taxes also provide significant revenues for Alaska Native Corporations, and local, state and federal government.
The expansion of infrastructure further west improves the economics of other exploration targets in NPR-A.

Australian company OIl Search is moving closer to developing the Pikka field into what could potentially produce as much as 120,000 bpd. Flord West is a series of new wells northwest of Alpine expected to come online in 2021 and produce an estimated 20,000 bpd. It will use improved technology of an extended reach drill rig to reduce the surface impact of the project.

**U.S. Economy**

Real GDP growth in the United States increased at a rate of 2.9% in 2018, compared to 2.2% in 2017 and 1.5% in 2016, according to the Federal Bureau of Economic Analysis.

The 2018 improvement is attributed to increased consumer spending, exports, inventory investment, and government spending. Gains were partially offset by lower residential fixed investment and a higher level of international imports.

The Bureau of Labor Statistics reported a national unemployment rate of 3.9% at the end of 2018 compared to 6.3% for Alaska.

**Tourism**

The improvements in the national economy have directly benefited the tourism industry in Alaska. More people are able to travel as consumer disposable income improves. Age demographics of the prosperous baby boomer generation are also helping the cruise industry reach record numbers.

According to a State Department of Commerce report released in November of 2018, the Alaska tourism industry generated $4.5 billion in economic output in 2017. The sector earned $1.5 billion in labor income from 43,300 annual jobs. A record 2.2 million visitors spent $2.8 billion. $126 million was earned in state government revenues from the Alaska railroad, fish & game, vehicle rental taxes and other programs. Another $89 million in revenues flowed to local governments from sales taxes, lodging taxes and dockage fees. Roughly half the visitors come by cruise ship, 47% by air and 4% by the highway or ferry system. The number of visitors has grown for five consecutive years and 2019 is forecasted to be another record year. The cruise industry is predicting 175,000 more passengers in 2019 for a growth rate of 16% from larger ships and more ports of call.

**Military**

Alaska is expected to benefit from increased levels of federal military and infrastructure spending. Fairbanks has been positively impacted by the announced transfer of two F-35 squadron to the local Eielson base between 2020 and 2022. They expect an increase of approximately 50% in base population, adding 3,300 people to the current 6,800 (including families). This is projected to require over $550 million in base construction and significant residential construction, both on and off base, according to presentations by officials at Eielson Air Force Base. 974 new housing units are projected to be needed in the next three years to support this growth.

**Interest Rates**

The Federal Reserve raised the fed funds target rate 0.25% to a range of 2.25% to 2.5% on December 20, 2018. This follows a quarter rate hike in September, June and March of 2018. The Fed raised rates 0.25% three times in 2017 and once each in December of 2015 and 2016. These nine 0.25% rate increases total 2.25% in the last three years. Prior to that, the Fed had not raised interest rates for nine years since they reached 5.25% in June of 2006.

Although dependent upon a variety of economic indicators and forecasts, expectations for gradual increases were anticipated in 2019. However, the Fed did not adjust rates in their first meeting of 2019 and signaled through policy statements the possibility of no change in rates for the coming months. While rates are volatile, current levels are still below long-term historical averages and could still trend upward if the national economy continues to improve. Rising interest rates will most impact sectors that require more fixed asset investments and higher levels of financial leverage and customers with variable rate loans, such as lines of credit.

Though overnight rates have increased by 1% in the last year due to Fed monetary policy, medium and long term U.S. Treasuries have actually decreased slightly compared to a year ago. The yield curve for one month to five years in duration has been flat to even slightly inverted for most of 2019. This has been positive by providing relief to home buyers who need 30 year loans. However, inverted yield curves often foreshadow future recessions. 10 to 30 year maturities are not yet inverted, but this is an important development to pay close attention to.

**U.S. TREASURY RATES**

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<thead>
<tr>
<th>Time</th>
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<th>March 2019</th>
</tr>
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<tbody>
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<tr>
<td>6 mo.</td>
<td>2.41%</td>
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<td>1 year</td>
<td>2.31%</td>
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</tr>
<tr>
<td>30 year</td>
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**Residential Foreclosure and Delinquency**

According to the Mortgage Bankers Association, Alaska’s foreclosure rate was 0.66% at the end of 2018, virtually identical to 0.64% at the end of 2017. This ranked Alaska 20th best of 50 states in the country and better than the national average rate of 0.95%. The national rate showed continued improvement from a rate of 1.19% at the end of 2017.

The national survey reported that the percentage of delinquent mortgage loans in Alaska at the end of 2018 was 2.92%, compared to 3.37% for the same period in 2017. This ranked Alaska 10th best in the nation. The 2018 average delinquency rate across the country was 1.4% higher than Alaska at 4.32%.

Alaska’s delinquency and foreclosure levels continue to be better than most of the nation. Alaskans showed resiliency and kept their home payments current despite the local recession. The current levels of problem mortgage loans are even lower than they were pre-recession in 2014. Nationally, the overall delinquency rate and the percentage of loans in foreclosure are improving relatively faster than in Alaska. The majority of the country suffered more during the larger U.S. recession and now economic improvements are being enjoyed more broadly across the country.

**MORTGAGE FORECLOSURE & DELINQUENCY RATES**

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<th>Year End Data</th>
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<td>3.37%</td>
<td>2.92%</td>
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<td>U.S. Delinquencies</td>
<td>5.99%</td>
<td>5.45%</td>
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<tr>
<td>Alaska Foreclosures</td>
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<td>0.66%</td>
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<tr>
<td>U.S. Foreclosures</td>
<td>2.27%</td>
<td>1.19%</td>
<td>0.95%</td>
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</tbody>
</table>
Residential Average Sales Price and Inventory

Despite a three year recession, the average home price in Alaska has been stable. Anchorage Multiple Listing Service (MLS) statistics show the average sales prices for single-family homes in Anchorage in 2018 were up 2.3% to $373,180. The 2017 average sales price declined slightly by 0.35% following a 0.2% reduction in 2016. The 2,774 single family homes sold in Anchorage in 2018 was virtually the same as the 2,800 sold in 2017.

As of March 7, 2019, there were 594 single family homes listed in Anchorage with 220 sales occurring per month over the last year. That results in an average of 2.7 months of supply on the market. All home price ranges under $400,000 have less than a three month supply. Homes priced between $300,000 and $499,000 have the most listings and sales. The average days on market was 55 days for homes that sold in the last year for all price ranges and 64 days for sales in the last six months.

Most of the softening in the residential market has come in the higher priced homes. The highest paying jobs in the State were the areas most impacted; namely oil & gas, construction and professional services. Homes priced $500,000 to $750,000 show 3.6 months supply in inventory. The $750,000 to $999,999 segment shows 5.1 months supply and homes over $1 million have 6.2 months of inventory.

In the Wasilla Core Commute area, the statistics include condominium sales with single-family homes. Average sales prices in Wasilla have grown steadily over the last five years. The average sales price in 2018 was $278,553, which was 2.7% higher than 2017. The preceding year growth rates were 3% in 2017, 2.2% in 2016 and 5.9% in 2015. The number of homes sold in Wasilla increased 2.8% to 1,143 in 2018.

Residential Building Permits

The U.S. Census Bureau reports a total of 1,698 residential building permits for 1 to 5 unit houses were issued statewide in 2018. This compares to 1,539 in 2017, an increase of 10.3%. The growth primarily came from 120 more single family units and 18 more duplexes than in 2017. It is important to note there are many smaller communities in Alaska that do not require the permits and therefore are not tracked in this data. Though this data is not comprehensive, it is a consistent report of activity in larger communities like Anchorage and Fairbanks. Permitted building activity has grown from 868 units at the recent low in 2011 to the current level of 1,698.

Inflation

Inflation picked up in Alaska in 2018. The consumer price index (CPI-U) in “Urban Alaska” rose 3% in 2018. The Federal Bureau of Labor Statistics (BLS) measures the rate of change in prices for a basket of goods and services from year to year in Anchorage and the Mat-Su. Inflation had been very low the last three years, averaging only 0.5% per year. The ten year average for Alaska was 1.75%. Alaska’s 3% inflation rate in 2018 compares to a national average of 1.9%.

The BLS just released a comprehensive report on the spending from typical households in all 50 states in 2016 and 2017. Alaskan households spent significantly more on average of $71,606 a year, compared to the national average of $58,681. The largest expense was housing, which accounted for one third of all spending across the country and 32% in Alaska. Transportation expenses for primarily buying and maintaining vehicles were second and consumed 15.9% of spending in the U.S. and 17.4% in Alaska. Insurance and pension payments were 11.6% of average American spending and a much higher 14.2% in Alaska. Food was the fourth major category, accounting for 12.7% of U.S. spending and 11.6% for Alaskans. Interestingly, health care spending was 8.1% of the national spending budget and only required 6.4% of the average Alaskan’s total for the year. It was also confirmed that Alaskans spent more on entertainment and less on clothes than the rest of the country.

State Budget

Low oil prices for three years left the state government with a multi-billion dollar budget deficit due to the heavy reliance on oil taxes to fund government. A short-term drag on the economy has been occurring as the legislature made difficult decisions to move towards a sustainable balanced budget by cutting government spending and limiting dividends. In fiscal year 2018 (ended June 30, 2018) that impact was reduced from higher than expected returns on the State’s sizable investment portfolio and improvement in oil prices.

The use of the Permanent Fund earnings through the percentage of market value calculation (POMV) was a critical step towards a balanced budget. In the coming fiscal year this will provide a visible stream of $2.9 billion to ensure dividends and help balance the state government budget. According to the new law, the government cannot use more than 5.25% of the Permanent Fund’s market value per year for the next three years and then reduce the draw to 5% thereafter. The formula is based on a five year rolling average, so the current year draw will be closer to 4.35% of the fund’s current value. This equates to roughly $2.7 billion being available for spending in fiscal year (FY) 2018 and 2019 and $2.9 billion in FY 2020. Last year, about $1.1 billion was paid to residents in the form of a $1,600 dividend per person in October. The remaining $1.6 billion was available to help balance the State budget.

The Permanent Fund will still grow, just at a slower pace. Average investment returns over the last five years of nearly 9% on the $60 plus billion fund would return approximately $5.4 billion a year. Additionally, current resource development royalties add approximately $300 million in new deposits to the fund each year. The State Legislative Finance Division forecasts the Permanent Fund principal will grow by $2.8 billion in FY 20 after $2.9 billion is spent on dividends and balancing the budget.

Total State appropriations, including the dividend, were $11.2 and $11.4 billion in FY 2017 and 2018 according to the Legislative Finance Division. The current management plan for FY 2019 (ending June 30, 2019) is to spend just under $11.4 billion. Total revenues from all sources are projected to be $11.1 billion, leaving a projected deficit of $268 million to be funded from a draw on the Constitution Budget Reserve (CBR). The fund is projected to earn $176 million during FY 19 and nearly cover the deficit needs.

Revenues have been increasing primarily due to above average investment returns. The Alaska Permanent Fund returned 10.7% in FY 2018 and over 12% in FY 2017. The five-year average return was 8.9%. FY 2018 oil prices were above the State’s budget forecast, which resulted in several hundred million dollars in additional petroleum revenue for the State.
The Alaska Division of Legislative Finance reported the CBR had $2.4 billion and the Earnings Reserves of the Permanent Fund (ER) had $18.9 billion at the beginning of FY 2019. In addition, the Permanent Fund principal, excluding the ER, had another $44.2 billion. There is $1.5 billion more in accounts designated for specific purposes, such as the Power Cost Equalization Endowment, the Community Assistance Fund and the Alaska Higher Education Investment Fund. Another $172 million is available in the Statutory Budget Reserve Fund.

Employment

Alaska’s seasonally adjusted unemployment rate was 6.3% at the end of December 2018. The comparable U.S. rate was 3.9%. The Alaska Department of Labor’s preliminary estimates show Alaska’s payroll job count decreased by 900 jobs, or 0.3% compared to the prior year. 500 of the lost jobs were in the government sector, which declined 0.6% in 2018. The largest employment declines in the private sector were in Retail, Manufacturing (primarily seafood processing), and Professional & Business Services, with these sectors declining by about 400 jobs each.

Health Care continues to be the bright spot, adding 400 jobs in 2018. Tourism helped boost Leisure & Hospitality employment by 200 jobs. Construction added 200 jobs, which is a positive trend compared to the decline experienced in the prior two years. Also significant was a positive increase of 100 jobs in the Oil and Gas sector. This sector suffered the most during the recent recession and it consists of the highest paying jobs in the economy.

Over the course of 2018, the Anchorage/Mat-Su region lost 400 jobs and the Northern region declined by 600 jobs. The Gulf Coast region has 200 fewer jobs. The Southeast region increased by 100 jobs. The Interior region is the only area to show a significant improvement with 500 more positions than last year.

Gross State Product

Alaska’s seasonally adjusted gross state product (GSP) in real terms was $54.6 billion in the third quarter of 2018, according to the U.S. Bureau of Economic Analysis (BEA) in a report released on February 26, 2019. Alaska’s real GSP declined 5% annualized in the first quarter of 2018, but then grew by 3.7% and 1% in the second and third quarters. The third quarter growth rate ranked Alaska 49th in the 50 United States.

Per Capita Income

Alaska’s per capita income in the third quarter of 2018 was $59,647. Total income in Alaska was $44 billion, up 3.3% annualized, according to the BEA’s third quarter 2018 report, released December 20, 2018. Total income in Alaska climbed $357 million in the third quarter of last year. $123 million of the improvement came from wage earnings, $60 million from investments and rents, and $174 million from increased government transfer payments.

Population

The State Labor Department’s 2018 Alaska population estimate is 736,239. This is a decrease of 1,608 people or 0.2%. Alaska’s population declined in 2017 by 1,829, or 0.2%. These were only the fourth and fifth year on record since 1945 that Alaska lost residents. Between 1986 and 1988 Alaska lost 15,700 residents, which at the time accounted for about 3% of the state population. In 1978 the population decreased by 6,400 or 1.5%.

Alaska has had a net out-migration of 35,346 people cumulative over the last six years, likely in response to a limited local job market and the relative improvement of the national economy compared to Alaska. However, the total population continued to grow through 2016 because the natural increase of net births minus deaths was over 7,000 a year. This changed in 2017 as the net out migration increased to 8,165 people and the natural increase slowed to 6,336. In 2018, the net out-migration was 7,577 residents and the natural increase slowed again to 5,969. This is attributed to both the birth rate declining and the mortality rate increasing, likely due to an aging population.

Over 40% of the State’s population resides in Anchorage where the population declined by 0.8% in 2018, resulting in a loss of 2,386 people. Meanwhile the Mat-Su Borough continues to grow, adding 1,355 people, up 1.3% in 2018. The Mat-Su surpassed the Fairbanks North Star Borough population of 97,121, which declined 0.8% and lost 734 people last year. The Southeast Region combined has a population of 72,876. It declined 0.1% last year for a loss of only 80 people. Juneau was down 0.2%, Sitka lost 1.1% and Ketchikan’s population grew by 0.4%.

Written by Mark Edwards, EVP Chief Credit Officer and Bank Economist with Northrim Bank. Mark served the State of Alaska as an Economist in the Department of Commerce and the Department of Revenue, and as the Director of the Office of Economic Development. He was an adjunct professor of economics at Alaska Pacific University. 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.