Outlook for the Hawai'i Economy

December 31, 1999

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Hawaii’s economic picture began to improve in 1999. Driven by a strengthening external environment, the visitor industry started to recover from a very weak 1998, helping to sustain moderate income growth for the state as a whole. While labor markets remain weak, payroll job losses came to an end, and the unemployment rate edged downward. Even construction, which has suffered a severe slump in recent years, showed signs of life. This performance bodes well for the year 2000, with virtually all sectors of the Hawaii economy finally beginning to move in the right direction!

The visitor industry has been stuck between two divergent business cycles. The U.S. mainland economy continues its torrid expansion, growing for the third year in a row at nearly 4%. (See Global Recovery Gathers Steam.) As a result, westbound visitor arrivals expanded by 6.5% for the year to October. Eastbound arrivals continued to contract, falling 6% through October, as Japan’s economy struggled to recover from its worst annual performance in recent decades. Overall, visitors arrivals are expected to slightly exceed our April forecast of 1.9% in 1999, with average daily census up slightly more because of increases in the length of stay.

Visitor expenditures appear to have strengthened in 1999, driven in part by a continually rising yen. For the first 11 months of the year, the yen’s value was 11% higher than its average value in 1998, raising Japanese purchasing power here. Retail sales grew by nearly 4% in the year through August, compared with 1998. Since much of the yen’s surge has come since mid-year, we can expect this to show up more clearly in sales activity in the New Year.

There is finally convincing evidence that the construction cycle in Hawaii has bottomed out. Construction put in place continued to be rather weak in 1999, falling about 1% for the year through August. But other indicators are much more upbeat. Home re-sales continue to rise strongly, aided by ongoing price declines. The issuing of private building permits is up 30%, hinting at measurable growth in coming months.

Labor markets tend to lag general economic conditions. In Hawaii, there has been considerable payroll job destruction during the slow growth period of the 1990s. To some extent, payroll numbers have overestimated the extent of the problem, as self-employment has grown in importance. Nevertheless, nonagricultural payroll jobs continued to decline through the first half of 1999, with some recovery later in the year. Other labor market indicators have improved. The unemployment rate has fallen by nearly one percentage point since last year, to 5.2% in November.

Consumer prices have also fallen as Hawaii’s long-running slowdown has drawn on. While lower prices are undoubtedly a silver lining for local residents and the competitiveness of the tourism industry, the decline in prices we saw in 1998 is a symptom of exceptionally weak demand. Consumer prices have started to firm, rising 1% from the second half of 1998 to the first half of 1999. A combination of the higher than expected first half inflation rate, and rising rents, oil prices, and medical costs have caused us to revise our 1999 inflation forecast upward by more than 1% from our April forecast. We now expect inflation for 1999 to be just slightly less than 1%.

For the overall state economy, economic activity expanded moderately in 1999. Real income growth is
estimated to have grown by about 2% for the year as a whole. Gross State Product (GSP), the broadest measure of Hawaii’s economic activity should expand by a similar amount.

**2000 FORECAST SUMMARY**

Hawaii’s economy is expected to strengthen in the year 2000. External conditions for growth have improved in recent months. The decline in Eastbound arrivals bottomed out in October. November Eastbound arrivals were up 1% over November of 1998. Barring a serious setback, we should see at worst flat, and more likely a modest increase in, Eastbound travel in 2000. Combined with continued strength on the U.S. mainland, we predict overall visitor arrivals to grow by 4% over 1999 levels. If the yen stays near its current high value, length of stay and expenditures by visitors will strengthen further.

Private sector construction activity should finally contribute positively to state economic growth. As the recent surge in permitting begins to show up at job sites, real construction put in place is expected to rise 4.5% above 1999 levels. This will improve the job picture, but we are unlikely to see significant job gains for the state as a whole because of existing excess capacity.

Inflation will continue to edge upward, heading ultimately toward convergence with a US trend inflation rate of perhaps 2.5 percent. An important source of price pressure is likely to be shelter costs, as apartment rental rates continue their recent increases. We expect a 1.5% rate of consumer price inflation for 2000 as a whole.

Strength in Hawaii’s flagship tourism industry and the end of job losses will help to maintain the moderate rates of growth in income that we have seen in recent years. We anticipate growth in real personal income of 2.4% for 2000, slightly higher than in 1999. Real gross state product is likely to roughly match that performance. While not dramatic, this is certainly good news for the state’s fiscal situation.

The portrait we have drawn is of a gradually improving economy, not of a sleeping giant rebounding to 1980s-vintage growth rates. And this recovery is fragile. For better or ill, Hawaii’s fortunes continue to be entwined with those of its two principle tourism markets, California and Japan. California growth may well slow, retreating somewhat from the unsustainably robust expansion of recent years. But barring a mainland recession, westbound tourism growth seems fairly certain. The near doubling of convention visitors expected next year will also boost visitor numbers.

We are much less sanguine about Japan. The early 1999 surge in Japanese growth proved to be short-lived, and it remains to be seen whether the private sector can sustain even the assumed moderate growth without additional strong fiscal stimulus. A retreat of the yen to its 1998 average level would also reduce visitor spending here.

Hawaii’s recovery is a clearly a work in progress. If the rest of world will cooperate, that progress should continue in 2000.
## Hawai‘i Economic Indicators (Annual Growth Rates)*

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<tbody>
<tr>
<td>Real Personal Income</td>
<td>1.8</td>
<td>2.8</td>
<td>2.1</td>
<td>2.4</td>
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<tr>
<td>Visitor Arrivals</td>
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<td>-2.0</td>
<td>1.9</td>
<td>4.0</td>
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<tr>
<td>Nonagricultural Jobs</td>
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<td>-0.3</td>
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<td>0.5</td>
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<tr>
<td>Real Construction Put in Place</td>
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<td>0.5</td>
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<tr>
<td>Real Gross State Product</td>
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<td>2.2</td>
<td>1.8</td>
<td>2.2</td>
</tr>
<tr>
<td>Consumer Price Inflation</td>
<td>0.7</td>
<td>-0.3</td>
<td>0.9</td>
<td>1.5</td>
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*1999 figures are estimates. All 2000 figures are forecast. Real values adjusted for inflation.