

### 3. *ECONOMIC CONTEXT*

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Anchorage's regional economy is distinctive relative to more traditional economies in the Lower 48 states. Because Alaska relies heavily on the use of its vast holdings of natural resources, it is vulnerable to market fluctuations related to changes in supply/demand conditions and related effects on pricing of its key products. Today, Alaska's key economic sectors are oil and gas, air cargo/logistics, government, seafood, tourism, and timber.

The oil and gas industry has had by far the most significant influence on economic development in Alaska over the last half-century. The meager and inconsistent extraction and processing of oil beginning in the Cook Inlet in 1958 began to accelerate through the 1960s. After discovering massive quantities of oil at Prudhoe Bay, Alaskan oil companies generated \$1 billion in revenue for the state by 1970.<sup>2</sup> Construction of the Trans-Alaskan Pipeline, beginning in 1974, legitimized Alaska as a global player in the oil production industry and caused a 30-percent year-over-year increase in overall employment in the state in its first year of construction. This extreme expansion in economic activity persisted throughout the pipeline construction period through the late 1970s, finally tapering off at the end of the decade.

The first half of the 1980s saw a sizeable economic expansion of its own, this time related to high oil prices worldwide, and a healthy market for Alaska's oil. This period was associated with rapid rates of increase in population, employment, income, and many other indicators. However, when oil prices dropped drastically in the middle of the decade, a severe economic slump was observed, whereby population, employment, and overall economic activity in Alaska shrunk markedly almost until the end of the decade.

After the "boom-bust" cycles of the 1970s and 1980s, Alaska has enjoyed a prolonged period of sustained growth and economic expansion. Since 1988, Alaska has enjoyed uninterrupted annual positive growth in employment and Gross Domestic Product, although the rate of growth has slowed considerably during the current economic downturn and may see the first year of negative growth since the 20-year streak began.

## **Prospects for Growth**

### **Mining**

It is estimated that today, approximately 33 percent of Alaska's economy is directly tied to the oil and gas industry, another 33 percent is directly tied to spending by the federal government, and the remaining 33 percent is spread across various industry sectors.<sup>3</sup> Today, Alaska is primed for another increase in oil and gas-related activity because the market for oil has become

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<sup>2</sup> Alaska Department of Labor and Workforce Development, "Alaska Economic Trends," December 1999.

<sup>3</sup> University of Alaska, Anchorage, Institute of Social and Economic Research.

constrained in recent years. Several development proposals, including most notably the construction of the new ANS natural gas line, present opportunities for a new era of resource extraction activity and economic expansion well into the future.

## **Tourism**

In addition to the oil sector, several industries have potential to become emerging sectors contributing to increased economic growth. Tourism, for example, is an industry that has seen significant growth in recent years as outdoor enthusiasts and world travelers have been increasingly drawn to the natural beauty of Alaska. The cruise ship industry is expanding its Alaskan presence, with cruise ship passenger volume increasing from approximately 600,000 in 2000 to more than 1 million in 2007.<sup>4</sup>

## **Alternative Energy**

Alternative natural energy has also been identified as an industry that could receive increased attention in coming years. With Alaska's windy coasts and tidal/wave resources, it is a viable candidate to be a leader in alternative energy production in future years. In fact, Alaska's first major wind farm at Fire Island is nearing the end of the planning process. It is expected that construction will begin on this project in the summer of 2009, and the first phase of the facility will be fully operational in late 2010. Other similar projects throughout Alaska are being studied, and it is expected that this industry could be a major asset for Alaska for many years to come.

## **Shipping/Logistics**

Although already firmly entrenched in Alaska—and in Anchorage in particular—the shipping/logistics industries could still see significant future expansion. Alaska's location positions it well relative to key world markets. It is closer to Asia than any other major North American city and is opportunely located between the Pacific Rim and Europe by way of the Northwest Passage. Global warming and the expected ice melt will further open a direct passage to Europe.

The Anchorage business community and public officials are working to capitalize on its transportation networks—including rail, airport, port, and highway systems—to best serve key markets. Anchorage is already home to the busiest air cargo airport in the U.S., with a major presence among firms such as FedEx and UPS.<sup>5</sup> In response to the need to accommodate Panamax tankers, increased military operations, barge shipments, and the projected opening of the Northwest Passage, the Port of Anchorage has several planned enhancements in progress.

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<sup>4</sup> Alaska Department of Labor and Workforce Development, "Alaska Economic Trends," April 2008.

<sup>5</sup> Ted Stevens International Airport is ranked number one in the United States for having the most landed weight of cargo aircraft, according to the AEDC.

## Prospects for Anchorage

Anchorage is the economic and government center of a region consisting of the Anchorage Bowl, northern communities of Chugiak-Eagle River and Eklutna, as well as Palmer, Wasilla, and the rest of the Mat-Su Borough. Anchorage is also the key finance and business center of the State and has by far the largest population and employment of any developed area statewide.

The Alaskan “Boom-Bust” dynamic described above has been observed several times, and Anchorage has not been shielded from these effects. These booms and busts have had significant impacts on the base of employment and makeup of industry throughout Alaska and has influenced the size, shape, and character of industrial land development throughout the State and in Anchorage in particular. Moving forward, the MOA needs to ensure that it is able to capture its share of economic activity that occurs in Alaska, and the provision of viable industrial land is a key component of that effort.

### Workforce Issues

Like the entire state of Alaska, Anchorage has long been beset by a significant “brain drain,” in which students and young educated workers leave the state for other areas.<sup>6</sup> This has historically been a major issue in Anchorage, and although some improvements have been made in recent years, a common sentiment among the business community remains the absence of available labor. The costs and uncertainty associated with a lack of labor has contributed to the area’s relatively modest rates of industrial land development, as compared to those typically seen in metropolitan areas throughout the U.S. The lack of large, well developed industrial clusters, combined with the boom-bust dynamic, presents a risk to employees who would otherwise consider permanent relocation to the State. If steps can be taken to improve the feasibility of industrial development, a larger and more diverse local economy will continue to emerge over time, potentially mitigating some of these concerns.

### Existing Industrial Market Conditions

The industrial real estate market has been shaped by many of the economic and demographic factors that are specific to Alaska—and Anchorage in particular—as described above. This section describes the nuances of the industrial real estate market in Anchorage.

#### *For-Sale Industrial*

Historically, the industrial land market has developed at a relatively slow rate in Anchorage, although it is intermittently punctuated by flurries of activity associated with major construction projects. In 2008, only 9 industrial land parcels were sold in Anchorage, at prices between \$9.00 and \$12.50 per land square foot.<sup>7</sup> Interviews of persons involved in local development suggest prices could be reduced by 15 to 20 percent if retail and other uses of this land are prohibited. Because cost is a major factor precluding feasible expansion of the industrial base, such

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<sup>6</sup> See Chabin Concepts’ “Vision Anchorage” study, 2002.

<sup>7</sup> See BOMA 2009 Industrial Forecast.

restrictions may improve the local industrial development climate. The 9 industrial parcels referenced above amounted to a total of only 15 acres, which implies an average lot size of approximately 1.5 acres per parcel, which is too small to accommodate many industrial uses.

As shown in **Table 2**, the asking sales price of industrial buildings currently for sale in the MOA range anywhere from \$57 to \$240 per square foot. The largest industrial building currently for sale in Anchorage is a 150,000-square-foot warehouse facility, which is offered at an asking price of \$18.6 million. Although this building would be suitable for a large industrial user, smaller buildings characterize the majority of for-sale industrial product. As shown, the median size for-sale industrial building in Anchorage is 12,700 square feet.

In 2008, 19 existing industrial buildings were sold at an average price of \$132.67 per building square foot. In contrast, development costs are similar if not higher than this amount, implying that developers cannot achieve significant return on investment in this context. The acreage, which comprises these 19 industrial buildings, totaled approximately 6 acres, implying an even smaller average parcel size than the vacant industrial land, at 0.25 acres per parcel.

### ***For-Lease Industrial***

Currently, average lease rates for industrial buildings in Anchorage range between \$1.00 and \$1.10 per square foot per month. These rates have slowly trended upwards in recent years, increasing from \$0.91 to \$0.96 per square foot in 2006. Again, capitalized lease rates (assuming an average capitalization rate of 7.8 percent) yields an imputed value of about \$150/square foot, which may not be sufficient to cover predevelopment, vertical costs, and developer profit.

Another interesting factor that aptly characterizes the industrial real estate sector in Anchorage is the vacancy rate for industrial building space. Whereas the average rate for industrial buildings throughout the U.S. is approximately 12 percent, vacancy rates in Anchorage are extremely low for industrial land and buildings, at 2 to 3 percent.<sup>8</sup> The fact that speculative development is nearly non-existent in Anchorage despite low vacancies and relatively high lease rates reflects the significant risk inherent in developing these structures, primarily stemming from unknown or onerous front-end costs. Industrial development is carried out by owner operators responding to direct need for local services who construct facilities as part of a larger business operation strategy, not as a real estate venture. With progress in reducing risks and costs, it is likely additional operators, who currently manufacture in Sea-Tac or other lower-48 locations, may view operating a facility in Anchorage more favorably.

One of the major factors that cause the industrial real estate market in Anchorage to exist the way it does has to do with the high cost of land development in Anchorage. Site development costs are extremely expensive in Anchorage because many of the parcels require removal of peat soil and backfilling with soil that is more adequate for development. This can cost up to \$0.45 per cubic foot.<sup>9</sup>

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<sup>8</sup> CB Richard Ellis, 4<sup>th</sup> Quarter 2008.

<sup>9</sup> BOMA 2009 Industrial Forecast, Robert D. Martin, CCIM. January 9, 2009.

**Table 2**  
**Anchorage Bowl Industrial Land Assessment**  
**Summary of Actively-Selling Industrial Zoned Land within City of Anchorage**

Location	Property Type	Building Size (SF)	Price (\$)	Price/SF
401 E. 100th Avenue	Industrial Warehouse	150,000	\$18,600,000	\$124.00
401 E. 100th Avenue	Industrial Warehouse	60,000	\$7,440,000	\$124.00
401 E. 100th Avenue	Industrial Warehouse	40,000	\$4,960,000	\$124.00
2216-2340 N. Post Road	Industrial Warehouse	85,770	\$8,000,000	\$93.27
3521 E. Tudor Road	Industrial Self/Mini-Storage Facility	79,483	\$11,250,000	\$141.54
814 W. Northern Lights Boulevard	Industrial Warehouse	49,792	\$3,750,000	\$75.31
2225 E. 5th Avenue	Industrial Office Showroom	18,730	\$4,500,000	\$240.26
125 W. International Airport Road	Industrial Warehouse	12,747	\$1,475,000	\$115.71
4041 Old International Airport Road	Industrial Warehouse	12,735	\$1,250,000	\$98.15
200 E. 26th Street	Industrial Warehouse	11,800	\$750,000	\$63.56
1000 W. 66th Avenue	Industrial Warehouse	9,867	\$1,300,000	\$131.75
6407 Greenwood Street	Industrial Office Showroom	8,000	\$1,400,000	\$175.00
5713 Arctic Boulevard	Industrial Flex Space	6,240	\$650,000	\$104.17
Alaska Place	Industrial Warehouse	NA	\$11,000,000	NA
200 E 26th Street	Industrial, Office, Retail, Warehouse	8,154	\$750,000	\$91.98
5617 E Dowling	Industrial Warehouse	13,440	\$1,700,000	\$126.49
126 W International Airport Road	Industrial, Office, Retail, Warehouse	12,747	\$1,578,000	\$123.79
1155 E 70th	Industrial	4,145	\$545,000	\$131.48
6727 Greenwood Street	Industrial Warehouse	5,250	\$650,000	\$123.81
2225 E 5th Avenue	Industrial, Land, Retail, Office, Warehouse	18,730	\$4,500,000	\$240.26
5202 A Street	Industrial, Office, Retail, Warehouse	17,640	\$999,500	\$56.66
651 E 100th Building B	Industrial, Office, Retail, Warehouse	6,000	\$898,000	\$149.67
651 E 100th Building A	Industrial, Office, Warehouse	4,800	\$950,000	\$197.92
651 E 100th Building C	Industrial Warehouse	8,400	\$1,000,000	\$119.05
651 E 100th Building D	Industrial Warehouse	4,800	\$900,000	\$187.50
345 Boniface Parkway	Industrial Warehouse	13,276	\$1,400,000	\$105.45
9210 Vanguard	Industrial, Office, Retail, Warehouse	7,200	\$1,149,000	\$159.58
	Maximum	150,000	18,600,000	\$240.26
	Average	25,759	3,457,204	\$131.71
	Median	12,741	1,400,000	\$124.00
	Minimum	4,145	545,000	\$56.66

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Source: AnchorageProspector.com, Cityfeet.com, Loopnet.com, and EPS

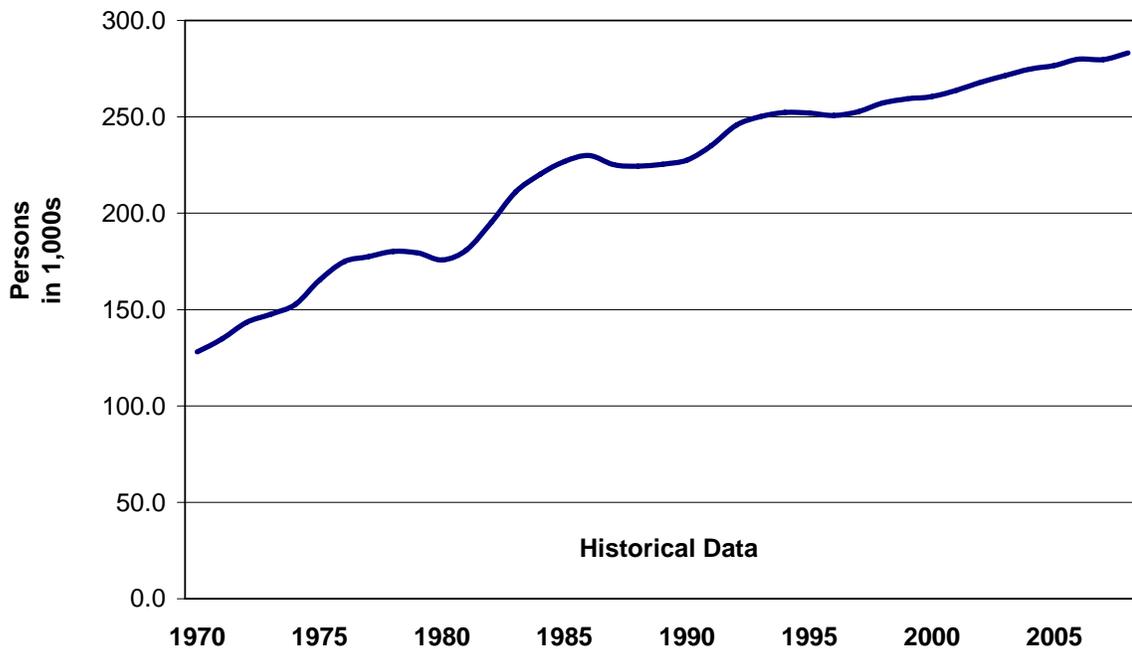
## Demographics and Socio-Economics

EPS has evaluated several sources of demographic and socio-economic data to have a more robust understanding of historical growth fundamentals, and how these factors may relate to future expansion in the MOA.

### Population

**Figure 3** shows population growth in the MOA from 1970 through 2008. This figure aptly illustrates the cyclical nature of growth in Alaska, in which growth in population occurred much more quickly during the “boom” periods related to oil and gas markets in the mid-1970’s and early-1980’s. The 1980’s oil boom was particularly acute, and was followed by a prolonged contraction of population in the MOA from 1986 through 1990. In the period from 1990 to the present, Anchorage has seen a healthy and steady rate of population growth, and has not been prone to the volatility of previous decades.

**Figure 3 - Total Population  
(1970-2008)**

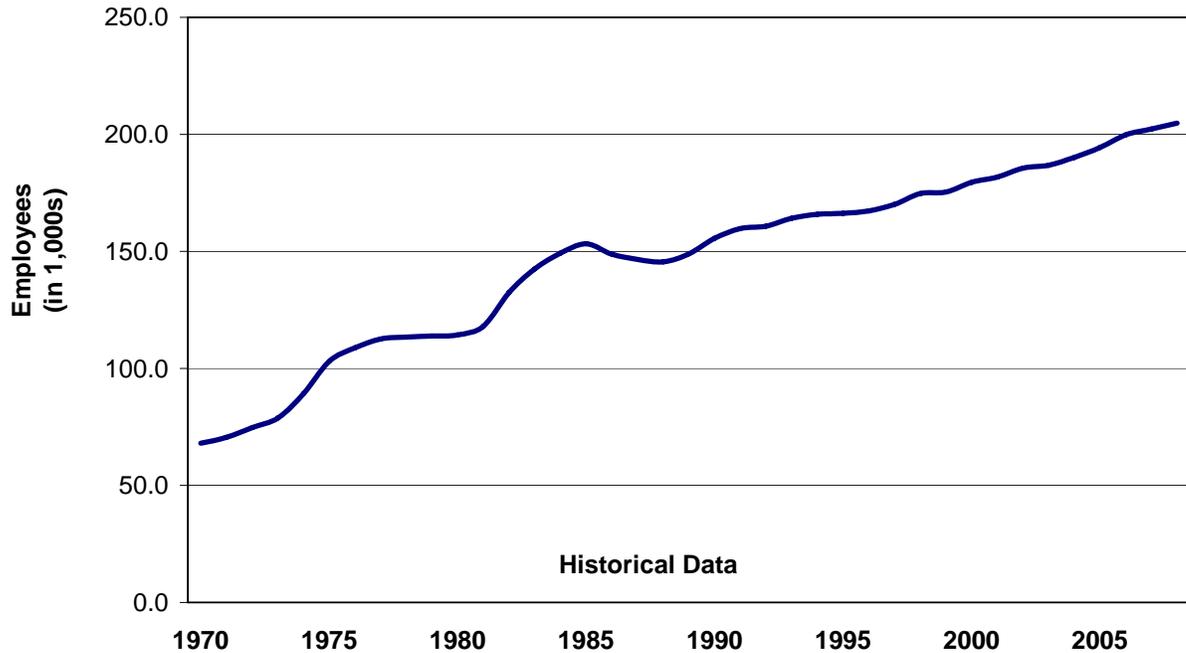


Source: Woods and Poole Economics, Inc. and EPS.

## Employment

**Figure 4** shows employment growth in the MOA from 1970 through 2008.<sup>10</sup> This figure shows a similar cyclical pattern of economic and related employment activity in Alaska, in which employment growth occurred rapidly in the mid-1970's and tapered off in the later portion of the decade, and an even more pronounced boom in the early 1980's, followed by a more severe "bust" in the late 1980's. After these two significant "boom-bust" cycles, Anchorage has seen positive, uninterrupted growth in employment.

**Figure 4 - Total Employment  
(1970-2008)**



Source: Woods and Poole Economics, Inc. and EPS.

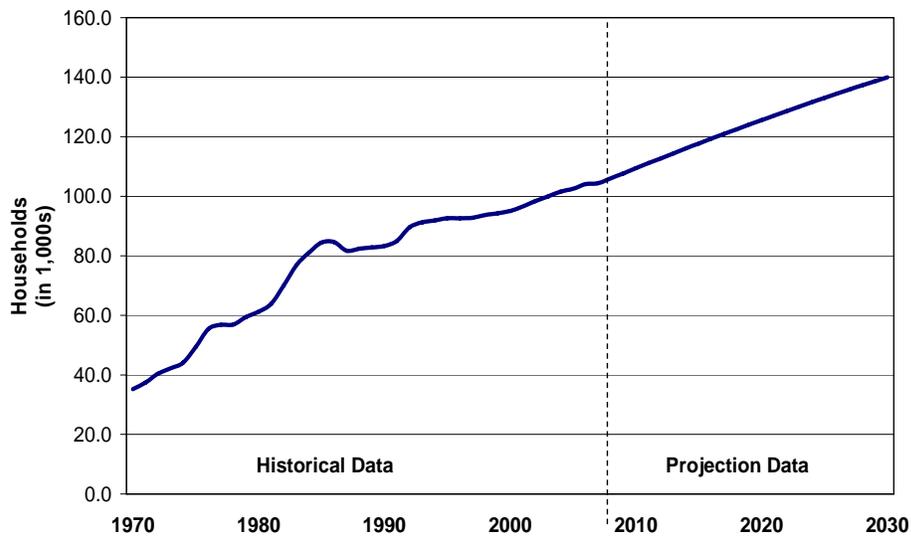
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<sup>10</sup> Please note that the employment figures used in this analysis are for employment by place of *work* (as opposed to place of *residence*) and include all part-time and full-time jobs in the MOA. Furthermore, these figures may be higher than those seen elsewhere because they include proprietors, private household employment, and both full- and part-time workers. Because employment projections are a key component of the land demand analysis, these figures will be discussed in greater detail in the following chapter.

## Other Economic/Demographic Information

Figures 5 through 7 show various other economic and demographic time series data from 1970 through 2008, and projected to 2030.<sup>11</sup> As shown, most economic indicators follow the same pattern described above, in which significant fluctuations as the results of the “boom” periods of economic expansion in the mid- and late- 1970’s and early 1980’s, which are generally immediately preceded by a tapering or decline during the “bust” periods. Since 1990, the Anchorage economy has been relatively stable, as compared to the turbulence of the 1970’s and 1980’s.

Figure 5 - Total Number of Households

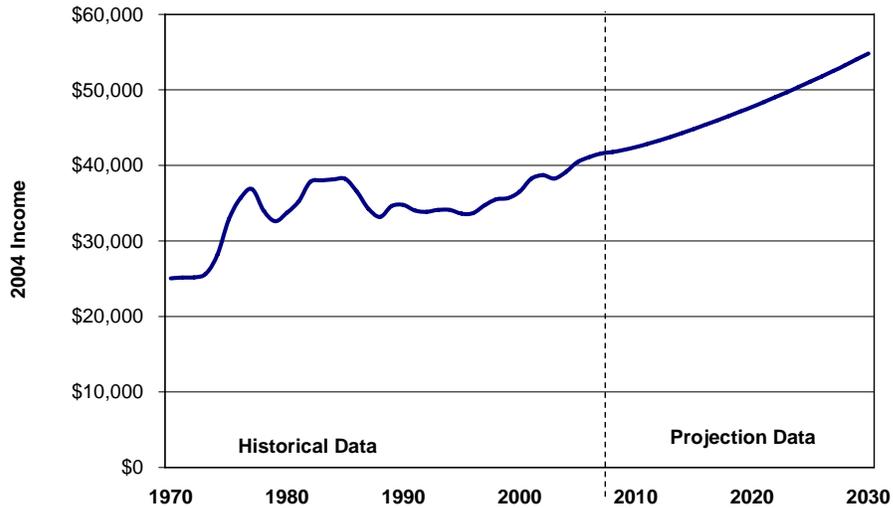


Source: Woods and Poole Economics, Inc. and EPS.

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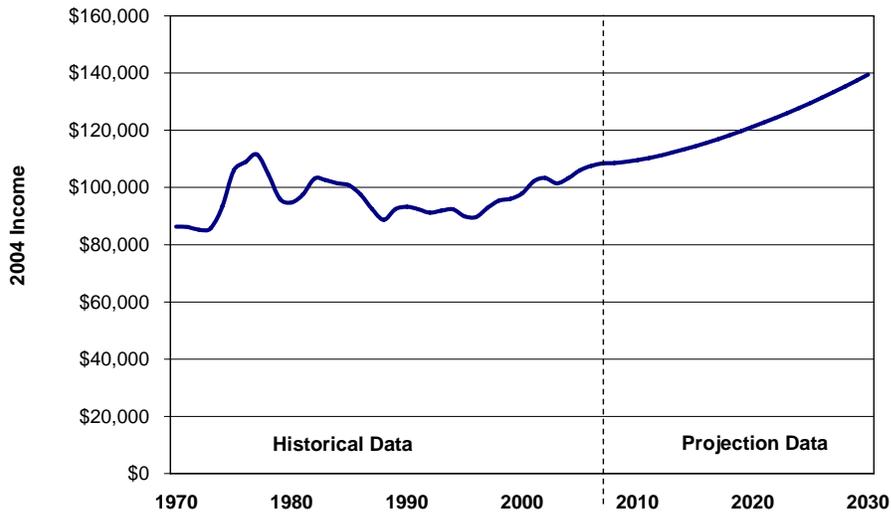
<sup>11</sup> These figures are based on data provided by Woods & Poole Economics, Inc., 2008. The Woods and Poole projections use a complex statistical algorithm, which is based on historical observations and projected growth in output for a range of industries. This methodology is based on long-term forecasts of total United States personal income, earnings by industry, employment by industry, population, inflation, and other variables, which are allocated to economic subregions based on the region’s expected capture of each industry. For more information on the methodology used to derive these projections, please see **Appendix C**. Also, please note that these projections were derived in mid-2008, based on 2007 data, and do not account for many of the severe economic events that occurred in these years. Although the short-term projections may be inexact, it is reasonable to believe that the long-term projections are valid.

**Figure 6 - Total Personal Income Per Capita**



Source: Woods and Poole Economics, Inc. and EPS.

**Figure 7 - Mean Household Total Personal Income**



Source: Woods and Poole Economics, Inc. and EPS.

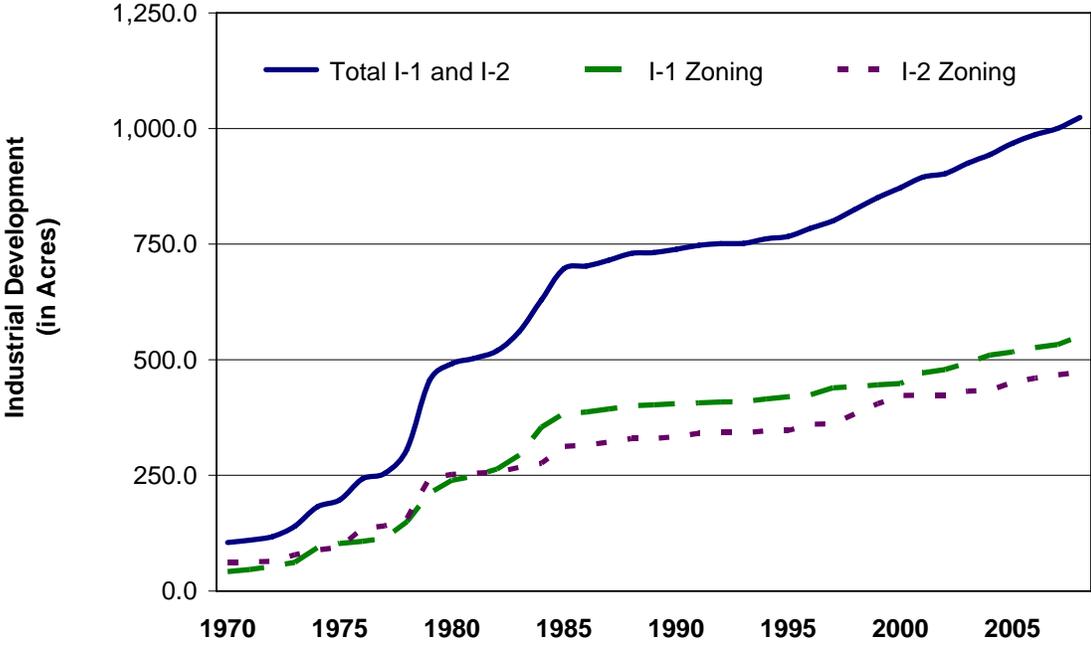
### Industrial Land Development

**Figure 8** shows the rate of industrial land development from 1970 through 2008. This figure similarly mirrors the cyclical nature of the Anchorage economy, and demonstrates that industrial development tends to occur during periods of economic expansion and employment growth, while tapering off during periods of slow or depressed economic activity.

It is of interest to note that during the period of intense employment growth associated with the pipeline construction period in the mid- to late 1970's, a noticeable increase in I-2 land can be

observed. During periods of more moderate growth, or the gas price boom of the 1980's, industrial land is characterized by more I-1 development than I-2.

**Figure 8 - Cumulative I-1 and I-2 Industrial Development (1970-2008)**



Source: Woods and Poole Economics, Inc. and EPS.