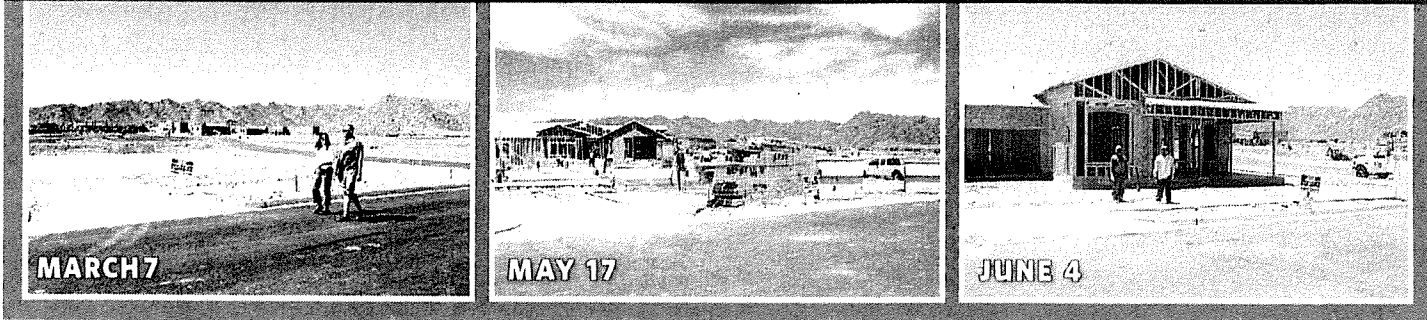


LOT 1311 | This series told the story of the Phoenix housing economy through a new home built for Kevin and Holly Johnson.



PHOTOS BY TOM TINGLE/THE ARIZONA REPUBLIC



How long Will it

last?

Panel discusses Phoenix's future

At the beginning of the year, *The Arizona Republic* formed a panel of experts to help quantify the scale and economic impact of the Phoenix housing industry. Month to month as the project progressed, members of the panel provided information and analysis. Members were added through the year as the project findings evolved. For this fifth and final installment of the series, the panelists have been asked to respond to some of the key questions raised by the story of Lot 1311 and how the Phoenix housing industry and regional economy operate.

THE PANEL (below, from left to right) ¶ **DREW BROWN**, president of DMB Associates, board member of Greater Phoenix Leadership. DMB is the developer building Verrado. ¶ **R.L. BROWN**, publishes an influential monthly report, the *Phoenix Housing Market Letter*, chairman of the Governor's Advisory Real Estate Board. ¶ **JAY BUTLER**, a professor at Arizona State University and director of ASU's Arizona Real Estate Center. ¶ **STANLEY PAUL COOK**, an analyst with Landiscor Aerial Information and a California developer. ¶ **GRADY GAMMAGE**, partner in the law firm Gammage & Burnham, board member of the Central Arizona Project (CAP), author of *Phoenix in Perspective*. ¶ **ANNE MARIUCCI**, a trustee of the international Urban Land Institute, co-owner of the WNBA's Phoenix Mercury, former president of home builder Del Webb Corp. ¶ **IOANNA MORFESSIS**, founding president and former chief executive of the Greater Phoenix Economic Council, founder of the consulting firm IO.INC. ¶ **ELLIOTT POLLACK**, president of the consulting firm Elliott D. Pollack and Co., a consulting economist for the annual "Arizona Blue Chip Economic Forecast." ¶ **SUNG WON SOHN**, executive vice president and chief economic officer of Wells Fargo Co., member of *Time* magazine's Board of Economists.



DREW BROWN • R.L. BROWN • JAY BUTLER • STANLEY PAUL COOK • GRADY GAMMAGE



ANNE MARIUCCI • IOANNA MORFESSIS • ELLIOTT POLLACK • SUNG WON SOHN

ONLINE
For more from the *Arizona Republic* panel, plus slideshows and previous installments of the Next West series, go to nextwest.azcentral.com.

What's the relationship of Phoenix's housing industry to the overall economy?

Ioanna Morfessis: Growth is the lifeblood of the Greater Phoenix economy, and the housing industry and its value and supply chains represent the primary economic output of our region. Fueled by historically inexorable population growth, housing and its myriad direct and indirect support services and products have been and continue to be the single most important driver of Greater Phoenix's economy.

R.L. Brown: The current Phoenix housing market, when combined with the known trickle-down effects, is clearly a huge part of the overall regional and state economy.

Grady Gammage: The basic industry of our town is real estate development and the delivery of houses to as many new people moving here as possible. Most cities go through a period of growth in which new-home building is a critical industry. But more typically a boom is a period passed through on the way to satisfying the immediate demands caused by immigration because of some other industrial building: railroads coming to Chicago, defense industries to Los Angeles. In Phoenix's case it seems like massive construction of new houses is not designed to close a gap but is, rather, a permanent state of being.

As other cities grow, there is often a debate about what comes first: jobs or houses. But in Phoenix's case, the answer is relatively settled. It is new houses that drive population inflow.

Drew Brown: We have experienced a particularly strong burst of housing, but my guess is its impact on the economy will decline over time. The best-case scenario is the housing market won't grow by much more. Jobs will follow the people moving here if we focus on our quality of life issues like education, the arts and culture. I tend to view housing as one of the elements that allows us to attract quality people and jobs

What are the benefits and perils of having an economy that depends on one large sector, especially housing?

Ioanna Morfessis: There are some benefits to having such a boom in the housing sector. First, construction jobs generally are higher-paying jobs than those in the hospitality and retail sectors. While the boom lasts, employment in this sector will remain abundant and will provide opportunities for skilled construction workers.

Economic downturns and upswings occur as a result of many factors, most of which are completely beyond the control of government, business and all other institutions of our society. Having a diverse economy with multiple, well-developed sectors will greatly strengthen our region's ability to be competitive, sustainable and more resilient.

Anne Mariucci: It is always dangerous to have a local economy overdependent on a single, specialized industry, a la Seattle with aerospace in the '80s and '90s. But given that the housing industry is a shadow sector vs. a driving sector, I don't believe its concentration in Phoenix presents any serious problem.

Most of the new housing in Phoenix today is built to order, and there is very limited speculative building. If economic forces worked against Phoenix, the housing industry could contract quickly. From an employment perspective, subcontractor trades that dominate the housing industry are more transient than most industries. They're mobile and will quickly move to where the work is.

R.L. Brown: The benefits of this housing engine begin with the relative affordability of housing itself and its social and economic impact on the availability of homeownership to the citizens of the region. In communities where the housing industry has been stifled by regulation or economic downturn, rising prices have killed the opportunity for ownership amongst all but the most affluent.

Overall, the benefits fuel a wide-ranging economic "factory" that allows widely diverse entrepreneurial growth and development of a region. A collapse of such a key economic driver could be ruinous for the region's economy.

Elliott Pollack: If affordability becomes an issue again, a cyclical downturn could occur. This would negatively affect the economy. Also, in the long run if population growth slowed, the transition from where we are today to where we would be, would be painful.

Stanley Paul Cook: The obvious peril is having too many eggs in the basket and the possibility of an overall collapse of a very large segment of the economy. However, remember that real estate is cyclical, and when disaster strikes at some point the event turns into opportunity. The benefit of this powerful engine is that the money circulating in the local economy spreads

far, wide and deeply and influences decisions by big business to locate in the vicinity, which further fuels the fire.

Sung Wohn Sohn: Diverse economies tend to be less volatile. They are less susceptible to dramatic booms and busts. An economy that tends to have high concentrations of specific industries often reflects the health of those industries; if the industries are growing, the overall economy is expanding. The converse is also true. Historical examples include the steel industry in Pittsburgh, the oil industry in Houston, and the technology sector in Silicon Valley. All of these economies experienced rapid growth when the corresponding industries boomed, but they also experienced sharp declines when the industries contracted.

What factors can affect our economy in a positive or negative way?

Anne Mariucci: Positives include: (1) Right-to-work state, limited influence of unions. (2) Can-do attitude regarding major economic development opportunities. (3) Unanimous desire of all stakeholders to diversify our economic base with a heightened emphasis on knowledge-economy sectors and a lesser emphasis on low-paying service jobs. (4) Relatively low state tax rates.

Negatives: (1) Lack of large corporate headquarters that give Phoenix a "national presence" and a "hometown commitment." (2) Historical emphasis on quantity of job growth vs. quality of job growth. (3) Education, education, education. Our national reputation and reality are abysmal and a handicap.

Jay Butler: Because we are basically a developing economy, it could be impacted by higher energy and water costs. Given that we have reasonably low incomes, people could be severely impacted by higher costs. Further, companies came here to take advantage of lower costs and could have difficulties if costs accelerate.

What should a Phoenix homeowner worry about in coming years?

R.L. Brown: I would be ensuring that I maintained and improved my home and that I was proactive in my neighborhood to ensure that my neighborhood remained an attractive place to live. I would become involved in local politics to ensure that local government was adequately funded and directed toward neighborhood preservation and zoning enforcement. Good local government and strong neighborhoods are critical.

Ioanna Morfessis: My concerns lie in the continued deterioration of our environment. Much attention has been given re-

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cently to the scarcity of water and the absolute imperative to do something about our water supply. Although houses use far less water than do agricultural users, still, I am worried about having sufficient quality water supplies for the future.

The worsening air quality of our region is extremely worrisome. Greater Phoenix continues to rank as one of the worst air-quality communities in the nation. Maricopa County's Board of Supervisors just created a new Air Quality Department, again a step in the right direction, and yet we still have a long way to go. Finally, I am concerned about the ability of our region to keep, develop and attract young people, typically first-time home buyers, because of the rapid acceleration in housing values.

Anne Mariucci: Homeowners should worry if they have financed their home in a way that requires it to increase in value over 5 percent per year in order to make ends meet. When people start banking on their home increasing over 10 percent per year, and there are lenders that will provide home equity loans up to 100 percent of their houses value, there's absolutely no room for error.

There is so much financial leverage in a home-purchase transaction that many people forget that a modest decrease in housing prices of, say, 10 percent could totally wipe out homeowners that have overleveraged themselves.

Just like the late '90s, when cocktail party talk was dominated by everyone's dot.com day-trading experience, when everyone starts talking about "flipping houses" and buying houses as a pure investment, we should start to worry.

In rapidly growing areas like Phoenix, new homes are built out on the fringes before there are schools, stores, parks, businesses, essentially all the things that will dictate the quality of life. Home buyers should do their homework to evaluate when these things will come to their area.

On another topic, there is general consensus that interest rates will rise over the next several years. Savvy homeowners should lock into a fixed-rate loan.

When the market inevitably cools, there will be a flight to quality. And in the case of housing, quality will be dictated by quality of life as dictated by curb appeal, access to quality schools, access to key transit links.

Grady Gammage: I have people ask me every once in awhile if they should be worried about some sudden crash in the value of single-family homes in the Phoenix metropolitan area. Frankly, I am not able to construct any scenario under which I think there is a big risk. In this regard, we have a long way to go before houses here are as overvalued as they are in much of California. Some people are unrealistically concerned that we will suffer some kind of

complete collapse in our water supply and a precipitous decline in housing values will follow. To the extent our water supply operates to regulate growth, this will be a relatively slow-moving phenomenon that develops over a multidecade time period.

Jay Butler: What homeowners are always worrying about? Who will buy my home and for how much. This is of increasing concern if people paid at the height of the market or are counting on higher values for retirement.

Sung Wohn Sohn: If the homeowner purchased the home for speculative reasons, there is considerable risk.

But, in general, most homeowners in Phoenix should not be worried if they have reasonable expectations. Just as the equity markets have shown that returns realized during the late 1990s were unsustainable, the home price appreciation realized over the past few years may also be unsustainable. This doesn't mean prices will collapse. It only means the market will adjust as interest rates rise and demand slows.

What land or growth policy changes make sense for Phoenix?

Drew Brown: I would like to see the public debate focused more on quality than quantity. That's very hard to do. It's not so important whether a site calls for four, seven or 12 units per acre. What's important is how those homes are configured. We need to create places and communities where people want to be.

Jay Butler: Most of our land is farm land that tends to lack any aesthetic value such as sea coast or view. Unless something begins to severely restrict supply, then land prices should remain supportable, especially as builders work with densities and plans to keep cost low.

Because of the low interest rates and housing boom, builders have been able to pass the increase costs on to the buyer. If the rates go up and income stays stable, the ability to pass on costs becomes limited and the newer designs and densities become even more important, especially for first-time buyers.

The real land policy issue is how to sustain or revive our aging housing stock. If we continually focus on the outer reaches, we will lose our core.

Grady Gammage: We are in the process right now of shifting most of our future urban growth away from the larger, more sophisticated Valley cities, which have learned how to manage it, and toward the smaller communities with lots of empty land.

Unfortunately, the natural evolution of this growth pattern is that the most active and dynamic growth areas are often the ones playing catch-up and least able to handle the long-term implications of that growth. We do not need to adopt the kind of

growth-management systems designed for the Pacific Northwest, but we ought to start thinking through more Arizona-generic solutions.

What is your prediction for Greater Phoenix's economy and the housing industry in the next 20 years?

R.L. Brown: This city will continue to grow into a regional megalopolis of probably 10 million people, not unlike Southern California. It will be economically and culturally diverse and, hopefully, we will be wiser and timelier in our planning for the inevitable growth than others have been or we have been to date. If we plan to ensure that job-base centers are located within 30 minutes or so of housing centroids and traffic flows from those housing centers to those job centers are managed by transportation design, we can achieve this growth without the freeway snarls that afflict California. Rapid transit will be a vital part of the mix but should be "rapid" and be built from housing center to employment center, not to some downtown core from the far outlands of housing.

We must revisit the "village" concept and implement it through a regional transportation plan that consumers will find more attractive and affordable than one-passenger auto commutes.

Elliott Pollack: The Greater Phoenix economy will continue to grow more rapidly than the U.S. as a whole. It will continue to be cyclical, and we will need to continue to diversify the export sector (base jobs) of the economy. The dominant industry will be business and medical services with a mix of biotech and high-tech manufacturing.

Drew Brown: We have a real chance to make a difference. There are substantial leaders committed to making Phoenix a top economy by 2020. Housing will continue to be important to the Valley, but it will be of less importance than it is now.

Housing is an important leg in the stool, but it's just a leg. To keep growing, we must have a sensible business environment, decent housing costs, a good education system and a vibrant arts-and-culture scene.

Jay Butler: Most forecasts are based on the idea that the past will repeat itself into the future. Thus, it is easy to see all of the great forecasts for local population growth. This area has grown basically on a somewhat circular process of jobs attracting people and jobs coming here because of the population growth. If this area is to grow, it must still attract jobs.

Grady Gammage: In that future economy, Phoenix will continue to be well-positioned if it continues to be a place where people want to live and where they can pursue their personal ambitions. If we can keep it from getting any hotter here, I think we will be fine.