

State of the Sitka Economy 2009 Update

Summary Report

Prepared For:



Sitka Economic Development Association

April 2009

Table of Contents

Introduction	1
State of the Sitka Economy: Selected Indicators	2
Population	2
School Enrollment.....	2
Employment and Earnings.....	2
Housing Construction	3
Business Sales	3
The Southeast Regional Economy: Selected Indicators	4
Population	4
Employment and Earnings.....	4
The Alaska Visitor Industry and Sitka’s Role	5
Extended Section: The Regional Seafood Industry and Sitka’s Role	5
Local Perceptions of Sitka’s Economy	8
Economics 101	10
Basic and Support Industries.....	10
Economic Multipliers.....	10
Sitka’s Economic Strategies	11

Introduction

The Sitka Economic Development Association (SEDA) sponsors an annual community business planning event entitled *State of the Sitka Economy*, for which it retains the McDowell Group to prepare a presentation summarizing the economic status of the community. McDowell Group is an Alaska research-based consulting firm with expertise in Alaska's economy and industries. The purpose of this summary report is to clarify and expand on the information presented at the April 16, 2009 event.

In addition to an overview of the Sitka economy, three special sections were added to this year's report and companion PowerPoint presentation, which is available from SEDA. The first section is an expanded discussion of *The Regional Seafood Industry and Sitka's Role*; the second, an overview of local perceptions of Sitka's economy; and third, an explanation of the fundamental principles underlying economic impacts and multiplier effects. The latter section, *Economics 101*, was added at the request of SEDA and is intended to offer the reader a stronger context in which to understand the local industries and their effect on Sitka's economy. Specific focus was also given to the role Sitka plays in the regional tourism industry, as has been done in past reports.

State of the Sitka Economy: Selected Indicators

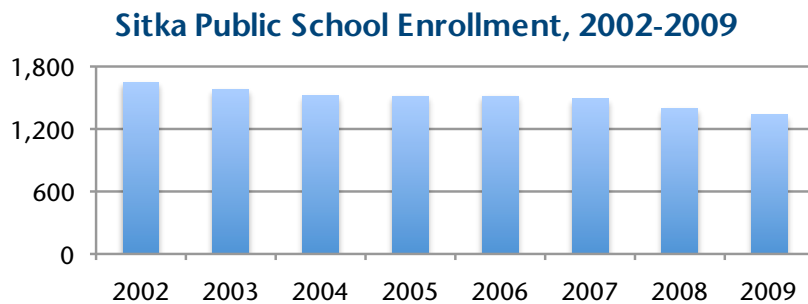
Population

According to the Alaska Department of Labor and Workforce Development (ADOLWD), Sitka's population has been fairly consistent since 2000. Over the past nine years, the community's population has fluctuated by fewer than 400 residents. In 2008, Sitka was home to an estimated 8,615, an increase of 13 residents (0.2 percent) from 2007.

School Enrollment

Unlike Sitka's general population, public school enrollment has declined steadily over the past eight years. Local public school enrollment declined from 1,646 in 2002 to 1,335 in 2009, a 19 percent decrease. Between 2008 and 2009, Sitka's public schools lost 65 students, or 4.6 percent of total 2008 enrollment.

Shifting demographics are contributing to changes in school enrollment. As with many communities in Southeast Alaska, fewer young families are making Sitka their home. Recent job losses associated with the closure of Sheldon Jackson College and other employment cutbacks have likely added to the challenge of attracting and retaining younger workers.



Source: Alaska Department of Education and Early Development.

Employment and Earnings

Sitka's economy is well balanced, with several sectors contributing to the local economy. Five sectors, seafood, health care, government, retail and wholesale trade, and leisure and hospitality, each accounted for over 10 percent of Sitka's total employment in 2007 (the most recent available data). Education, professional services, finance, transportation, construction and other smaller sectors are also important contributors to the community's economy. With this diverse economy, Sitka can more easily withstand employment losses in one or two specific sectors.

Total government employment, including those jobs that would normally be classified in the education or health care sectors, made up 27 percent of all 2007 employment. The majority of these jobs are within local government, followed by state and federal government jobs.

Overall, local employment during the first two quarters of 2008 was down 2.1 percent compared to the first two quarters of 2007. These numbers reflect the loss of Sheldon Jackson College, as well as SEARHC and US Forest Service cutbacks seen over the course of 2007.

Considering inflation, Sitka's total payroll in the first two quarters of 2008 was slightly lower than that during the same period in 2007, \$72.3 million compared to \$73.0 million, paralleling employment shifts. Additional payroll losses can be expected in the annual 2008 data (which is not published until summer 2009), again, reflecting the job losses at some of Sitka's top employers. Sitka's total payroll for 2007 (\$153 million) was the highest annual figure within the past decade.

Readers should note that official ADOLWD nonagricultural employment and payroll data, as presented above, excludes all self-employment, including earnings from commercial fishing and by uniformed Coast Guard, which are substantial in Sitka.

Housing Construction

According to the City and Borough of Sitka, 32 dwelling units were constructed in 2008, a small decline from 2007's total of 34 new units. Peak building activity took place in 2005 when a number of multiple unit buildings were built, for a total of 71 new units. Housing occupancy reportedly remains high with demand for affordable housing still a major issue in the community, as it is in other major Southeast communities.

The City and Borough of Sitka also tracks lot absorption. Lot absorption is measured by the number of existing residential lots experiencing construction for the first time, and a means to measure changes in residential land availability. Figures for 2008 indicate the Sitka housing market absorbed 28 new lots, compared to 16 in 2007. This is similar to 2006 figures, when 31 new lots were absorbed.

Business Sales

Sitka gross business sales, as reported to the City and Borough (and not adjusted for inflation), continued their 11-year upward trend, increasing 3 percent, from \$371 million in 2007 to \$382 million in 2008. Some of the community's steady increase in business sales may be attributed to more thorough reporting measures, but the overall trend is positive in any event.

The Southeast Regional Economy: Selected Indicators

Population

The regional population for Southeast Alaska totaled 69,200 in 2008, a 0.3 percent increase from 2007, but still down from earlier years. Among boroughs and census areas in Southeast, Haines, Juneau, Prince of Wales and Sitka all experienced some amount of population growth, while Yakutat, Skagway-Hoonah-Angoon, Ketchikan Gateway and Wrangell-Petersburg all witnessed declines. In recent years, a number of smaller regional communities have experienced the greatest proportional decline, as residents have typically moved from rural communities to urban areas, reflecting a statewide trend.

Southeast Alaska Population Trends, 2003-2008

	2003	2004	2005	2006	2007	2008
Southeast Region	71,730	70,831	70,786	70,271	68,971	69,202
Haines	2,316	2,250	2,205	2,234	2,246	2,310
Juneau	31,266	31,087	31,179	30,753	30,134	30,427
Ketchikan	13,512	13,067	13,111	13,176	13,089	12,993
Prince of Wales	5,586	5,562	5,502	5,469	5,299	5,360
Sitka	8,882	8,814	8,931	8,972	8,602	8,615
Skagway-Hoonah-Angoon	3,162	3,114	3,059	3,010	2,986	2,946
Wrangell-Petersburg	6,317	6,262	6,157	6,022	5,997	5,959
Yakutat	689	675	642	635	618	592

Source: Alaska Department of Labor and Workforce Development

Employment and Earnings

According to the State Department of Labor's *Current Employment Statistics Program* (CES), preliminary estimates indicate Southeast employment was up slightly (0.3 percent) in 2008. This small net increase is attributed to growth in the service, retail trade, and leisure/hospitality sectors, among others. Sectors that experienced employment losses from 2007 to 2008, included education, health care services, natural resources and mining, construction, professional and business services, goods producing, seafood processing and federal government. Early 2009 estimates indicate a slight decrease in overall regional employment.

Recent employment losses in Southeast have been specifically focused within the education, health care and government sectors. Jobs in these sectors are typically well-paying, stable, year-around positions, providing individuals with a livable wage. Unfortunately, most employment growth in Southeast has been concentrated in sectors that do not provide employees with wage levels and seasonal stability comparable to those of the jobs being lost. This exchange of family-wage jobs for lower-paying employment in trade and service industries is part of a longer-term statewide and national trend.

The Alaska Visitor Industry and Sitka's Role

In 2008, Alaska's summer visitor industry saw an estimated 1.7 million out-of-state visitors between May and September, a slight decrease (0.4 percent) from summer 2007. Most visitors exited the state via cruise ship (49 percent) or air (47 percent), while a small percentage exited via highway or ferry (4 percent). Among visitor transportation modes, only the cruise industry experienced growth in 2008, with a 1.1 percent increase in passenger exits. The small decline in 2008 overall visitor traffic reflects the 1.3 percent decrease in air passenger exits, as well as larger decreases in highway and ferry exit figures.

Sitka's visitor industry was a bright spot in the local economy in 2008. That year, the community's visitor volume totaled 374,600, an increase of 16 percent from 2007. Cruise traffic to Sitka, which tends to fluctuate from year to year depending on ship itinerary changes and competitive port factors, increased by 19.3 percent in 2008. Ferry traffic grew by 17.5 percent, a result of increased AMHS service to Sitka. Air passenger traffic fell 8.2 percent compared to 2007. Both air and ferry traffic includes local residents and business travelers.

Sitka Visitor Traffic Indicators 2002-2008

	2002	2003	2004	2005	2006	2007	2008
Cruise passengers	250,200	256,800	232,400	229,800	267,000	234,000	289,800
Air passengers	68,200	68,300	73,000	71,800	69,800	72,700	66,800
Ferry Passengers	14,000	13,500	15,000	13,300	13,400	14,900	18,000
Total	332,400	338,600	320,400	314,900	350,200	321,600	374,600

Source: Bureau of Transportation Statistics, Alaska Marine Highway System and McDowell Group estimates.

This 8.2 percent decline in air passenger traffic, coupled with an 8.5 decrease in 2008 Sitka bed tax receipts, reflect the small downturn seen in the local charter fishing industry, plus likely declines in business travel. Measured in terms of gross business sales, Sitka's charter industry declined by approximately 4 percent between 2007 and 2008.

Extended Section:

The Regional Seafood Industry and Sitka's Role

This report includes an expanded discussion of the status of Southeast's regional seafood industry because of its importance to Sitka's economy and the recent growth in the local processing sector.

Seafood harvesting and processing is one of Sitka's top industries in terms of employment and earnings, and 2008 was a strong year for this sector. During this year, 445 active Sitka resident fishermen, plus their crew, fished 734 commercial permits and landed 23 million pounds of fish with an ex-vessel value of \$36 million. Sitka's shore-based seafood processors produced an estimated 39 million pounds of finished product, worth approximately \$89 million in first wholesale value and accounting for nearly one-quarter of Southeast regional land-based processing activity.

This Sitka and regional land-based processing totals do not account for floating processors, direct marketers, or seafood harvested in the immediate area that is tendered to other communities for processing. All processing considered, Sitka area production likely easily exceeds \$100 million annually. With the 2007 opening of Silver Bay Seafoods' new salmon processing plant, Sitka's 2007 peak processing season employment totaled approximately 500 jobs.

In 2007, the regional seafood industry produced \$401 million in first wholesale value from fish with an ex-vessel value of \$205 million. Pounds harvested in the region totaled 280 million, which were processed into 203 million pounds of product.

Halibut and Sablefish

Halibut harvested in the area 2C IFQ fishery comprised 12 percent of Southeast region ex-vessel value in 2008, at \$25 million. This is a substantial decline from \$37 and \$38 million in the two previous years, and the economic loss is due to allowable commercial harvest cutbacks by the International Halibut Commission to compensate for charter industry overharvests and declining halibut biomass.

Halibut prices declined slightly from the peak levels of 2007, but the more significant factor reducing 2C halibut value has been the 40-percent cut in the quota. The 2C halibut quota has declined from 10.3 million pounds in 2006 to 6.1 million in 2008, with a further cut to 5 million pounds for the 2009 season.

Halibut ex-vessel price is expected to see a substantial correction in 2009. Statewide halibut prices were at all-time highs in 2007 and dropped only slightly in 2008. There has been some end-user dropout in the marketplace over the last 2-4 years due to high price but this was masked by steady quota reductions since 2004 and the price continued to climb. However, recessionary spending patterns of 2009 are expected to substantially reduce demand for products that are at or near their historic price peaks, like halibut.

Sablefish is currently the second-largest contributor to ex-vessel value in the region, with 15 percent of the Southeast region total. Harvest in the Southeast-area IFQ fishery and in the state-waters fisheries of Chatham Strait and Clarence Strait produced a total of \$31 million in ex-vessel value in 2008, up from \$25 million in 2007.

The value increase is primarily the result of steady growth in Alaska sablefish prices, which has offset reduced landings volume. Harvest quotas in the region's sablefish fisheries have sustained modest but steady reductions in recent years.

The allowable catch for the Southeast sablefish IFQ fishery decreased by 15 percent in 2009, to 6 million pounds. While the volume decrease will likely reduce total ex-vessel value for the region, sablefish markets are sensitive to supply and the price is likely to remain relatively strong.

Alaska produces approximately two-thirds of the world sablefish supply, and with the statewide sablefish quota reduced by 11 percent, recessionary pressures on the price are likely to be offset by the reduced market supply.

Salmon

Salmon remains the value leader in the region's major fisheries, by a wide margin. Preliminary salmon value in 2008 was nearly \$117 million (57 percent of the total) and is expected to increase as 2008-season value data are finalized. The 2008 season represents a sixth consecutive year of salmon value growth in the region, having more than doubled from the decade's low point of \$50 million in 2002.

The value growth in salmon is driven by a combination of strong harvest volumes for pink and chum salmon and steady growth in the price per pound of all five salmon species caught in the region. Salmon harvest volume in the strong years of the pink salmon abundance cycle has declined recently, but this has been offset by substantial price increases for all five salmon species, particularly for pink and chum salmon in 2008.

Recent price growth in pink and chum salmon is driven by a combination of steady growth in the average wholesale price of meat products (frozen, canned, etc) and by a major price increase for roe products in 2008.

The outlook for salmon value in 2009 is uncertain. Prices for the traditional high-value salmon species of the region (particularly Chinook and coho) will likely see substantial downward pressure with recessionary spending patterns. Chum salmon prices are also likely to be lower, as the unusually strong roe market (primary driver for chum price) has cooled substantially from 2008.

Pink salmon may offset the anticipated salmon value decline for the Southeast region in 2009. The 2009 season is projected to be a strong harvest for pinks in the region and value for pink salmon meat and roe products has grown steadily in recent years. The recent first-wholesale price of canned pinks suggests strongly that the canned segment of the market has made a full recovery from the depressed prices associated with the chronic product surplus during the early part of this decade.

This presents an interesting situation for the product-form balance in 2009. The shift from canned to frozen production in the middle years of the decade has slowed and the product-form balance now stands at approximately 50/50. However, with canned pink prices at their highest point in nearly two decades, there is significant incentive to shift back from frozen to canned production.

However, the fact that frozen pink salmon is capable of achieving a very modest price point in a price-sensitive (recessionary) marketplace serves as a moderating factor in the incentive to divert raw pink salmon from frozen to canned production.

Herring

Southeast region herring value increased substantially, up from \$2.4 million in 2006 to \$9.4 million in 2008. Value growth is a result of substantial increases in both harvest tonnage and price. The 2006 fishery produced 11,000 tons at an average per-ton price in the \$200 - \$360 range. Region-wide harvest volume increased to over 16,000 tons for the 2008 season, with per-ton prices in the \$400 - \$600 range.

The market situation for herring is uncertain, considering the world economy and the potential impact on Japan, the primary market. However, the Sitka herring sac roe quota increased to 14,500 tons and may offset a modest price decline, if there is one.

Local Perceptions of Sitka's Economy

As part of this year's *State of the Sitka Economy* research effort, interviews were conducted with eight community residents who are particularly knowledgeable about the local economy or a specific sector of the economy. The purpose of these interviews was to gain insight into some of the local perceptions of the health of Sitka's economy, as well as the expected local effects of the national economic downturn.

Listed below are key points, organized by industry, discussed by the interviewees. Industries include seafood, tourism, health care, retail business and local government.

Seafood

- 2008 saw record prices
- Current sales are slower than last summer – wholesalers and retailers are pulling back on orders
- Tight credit markets prevent buyers from financing larger purchases – shallower margins for local processors
- More inventory being held locally
- Salmon harvest will likely be up in 2009

Tourism

- Cruise ship capacity decreased for 2009
- May/June bookings holding, but July-September bookings are slow
- Concern about visitor per-capita spending
- Recent change in ferry schedule will further reduce number of independent visitors to Sitka

Health care

- Sizable federal funding increases expected for Native health care providers
- SEARHC recently made significant investment in electronic administrative overhaul – which will increase efficiency
- Sitka Community Hospital has recently contracted with Quorum – which will likely improve financial status

Retail business

- Feels some decline in the local market already
- Grocery customers trading down among food choices, but stores' employment stable
- Concern that some small businesses will not be able to withstand market downturn
- Closure of Sheldon Jackson College and SEARHC cutbacks felt somewhat in the retail sector

Local government

- Less sales tax revenue as a result of decreased cruise visitor spending and charter bookings
- 2009 Permanent Fund Dividend likely to be significantly less than 2008 PFD – resulting in less local spending
- Potential 8% to 9% decline in 2009 sales tax revenue
- Unsure of trickle-down effect of federal stimulus funds, but likely positive

Consistent with this year's *State of the Sitka Economy* presentation, a brief overview of fundamental principles that drive a local economy, such as Sitka's, is offered in this report. This discussion includes defining both basic and support industries and explains the economic multiplier effect. An economic multiplier takes into account direct, indirect and induced spending and provides a way to estimate total economic impacts associated with a particular business, organization or industry.

Basic and Support Industries

One way to describe an economy is with an "export base model." According to the export base model, there are two primary segments of an economy – basic industry and support industry.

Basic industry:

- brings new money into the economy from outside the local area, stimulating growth.
- produces goods and services for consumers located outside the local area.
- is the reason for the existence of the local economy and community.

By these definitions, many of Sitka's industries are considered basic, including seafood, tourism, education, health care, Alaska Native interests and national interests (such as the US Coast Guard). All of these industries attract money from outside sources, thus meeting the fundamental criteria of a basic industry.

Support industry:

- receives income from local sources, recirculating existing income.
- sells goods and services to residents, businesses, and government and nonprofit entities located in the local area.
- is not the reason for existence of the local economy, but contributes to the economy.

Sitka's support industries include local government services, retail trade and services serving local markets, local transportation and housing, for example.

Economic Multipliers

Economic multipliers are figures used to estimate the sum total of direct, indirect and induced spending within a particular economy.

- Direct economic impacts are the initial spending by businesses and organizations on wages, benefits, goods and services.
- Indirect and induced impacts are the impacts following this initial direct spending as the money circulates through the local economy.

- Indirect Impacts result from local spending on goods and services by businesses and organizations.
- Induced impacts result when employees of these businesses and organizations spend their payroll dollars locally.

A typical Alaska economic multiplier is about 1.5, meaning that every \$1.00 of direct spending generates an additional \$0.50 in indirect and induced impacts, for a total economic impact of \$1.50. Alaska multipliers are generally low (1.2 to 1.8) because much of what Alaskans purchase comes from outside the state and much of what Alaska produces is sold outside the state. This importing and exporting, called leakage, means there is much less interaction among local industries compared to more developed economies.

Multipliers tend to be higher when basic industries:

- Have high wages.
- Have high resident employment in year-round jobs.
- Generally involve a significant amount of local activity.

Multipliers are also higher when support industries are well developed, so that more goods and services are purchased locally, minimizing leakage.

Sitka's Economic Strategies

This analysis of basic and support industries, the multiplier effect and economic leakage could lead Sitka to some fundamental economic strategies, such as the following:

Economic growth strategies:

- Support existing basic industries – including government and nonprofits – that have high wages, lots of local activity, high resident employment, and year-around jobs.
- Encourage new basic industries with the same characteristics.

Leakage capture strategies:

- Support and encourage retention and expansion of existing support industries – including government and nonprofits, as well as for-profit businesses.
- Encourage new support industries in areas currently not served well by local businesses.