WILLIAM S. Spears School OF BUSINESS

Center for Applied Economic Research

2010 Economic Outlook: Owasso

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307 Spears School of Business, Stillwater, OK 74078 | *economy.okstate.edu*

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National Economic Conditions

Recovery in 2010?

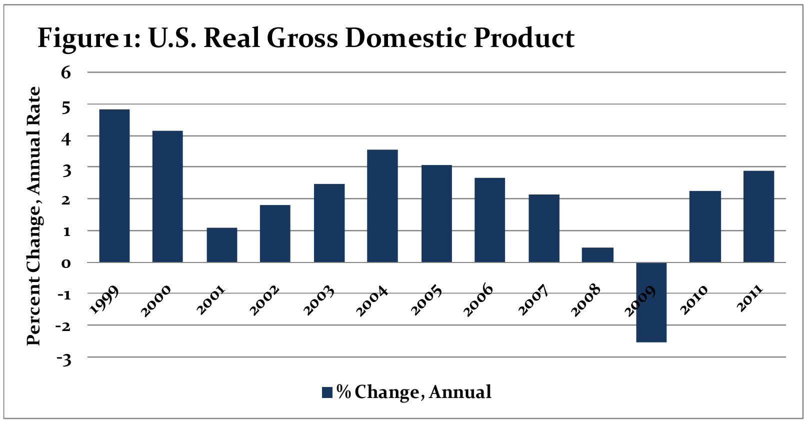


Figure 1: U.S. Real Gross Domestic Product

While economic data reveal a current recessionary experience not unlike previous ones, the abruptness with which the economy faltered and the fears of a global credit catastrophe set it apart as the most significant economic event since the Great Depression. The effects of eroded household wealth and the loss of over 8 million payroll jobs will linger through much of the coming decade. Meanwhile, the effects of unprecedented monetary and fiscal policy as well as the erosion of confidence in the U.S dollar as a reserve currency will linger for generations.

Economic recovery is underway but is likely to proceed slowly and only then with continued support from monetary authorities. Our current forecast calls for 2.2% growth in U.S. Real GDP, well below historical trend growth. Real questions remain about the ability of the economy to generate activity of its own accord at levels consistent with significant job creation through 2010 and into 2011. This question is likely to remain unanswered until well into the new-year.

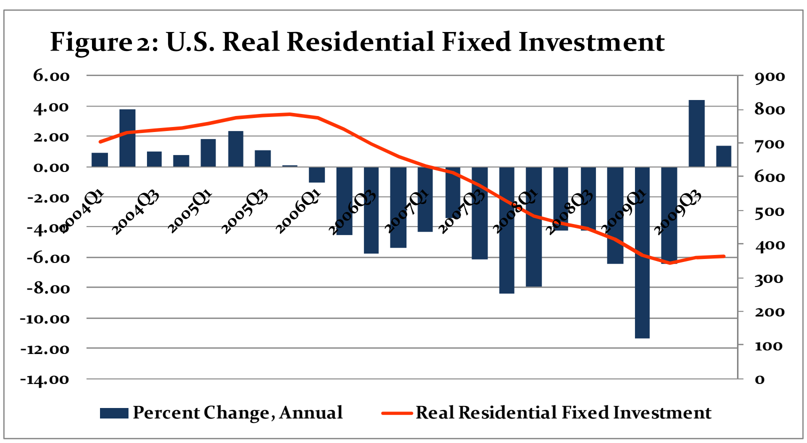
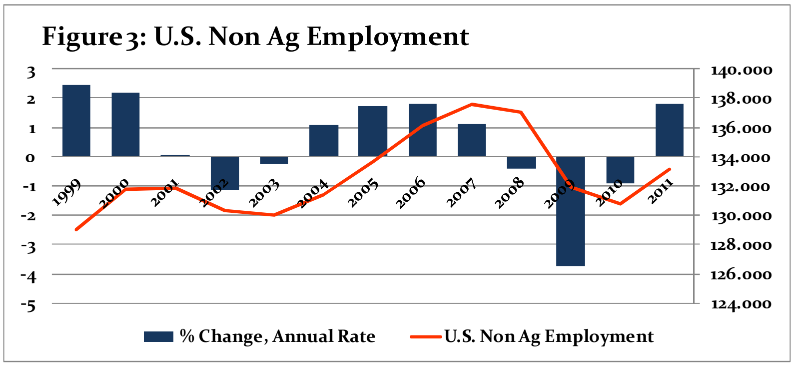


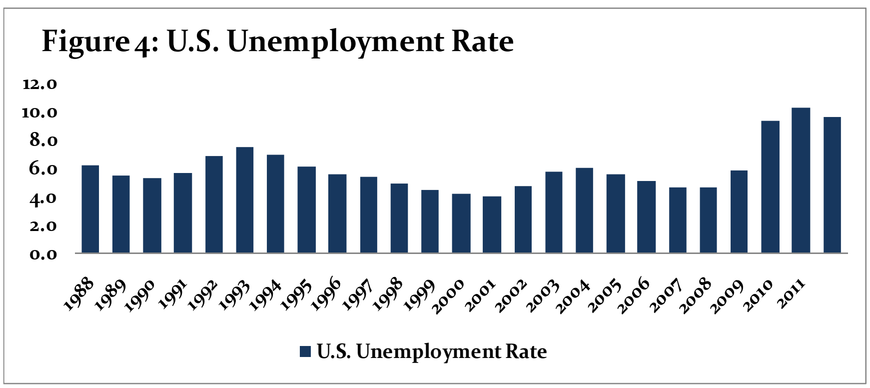
Figure 2: U.S. Real Residential Fixed Investment

At the heart of the financial crisis of 2008 lie years of overleveraged investments in U.S. residential real estate and the systemic mispricing of risk. Encouraged by federal programs and monetary policy, households and financial institutions expanded balance sheets to finance and refinance real estate purchases. These mortgages then became the foundation for ever more complex financial products coveted by financial institutions, brokerage houses, and fund managers. By late 2005 the residential real estate construction sector began to contract and would continue doing so through the second quarter of 2009. In the meantime, home prices collapsed setting in motion a chain reaction that would lead previously perceived safe investments to cease trading, leaving an entire asset class, and the balance sheets replete with them, nearly impossible to value; a global credit crisis promptly ensued. While rebounding off their lows, residential fixed investment will grow only modestly in the near term as inventory excess and the erosion of wealth combine to dampen residential construction.

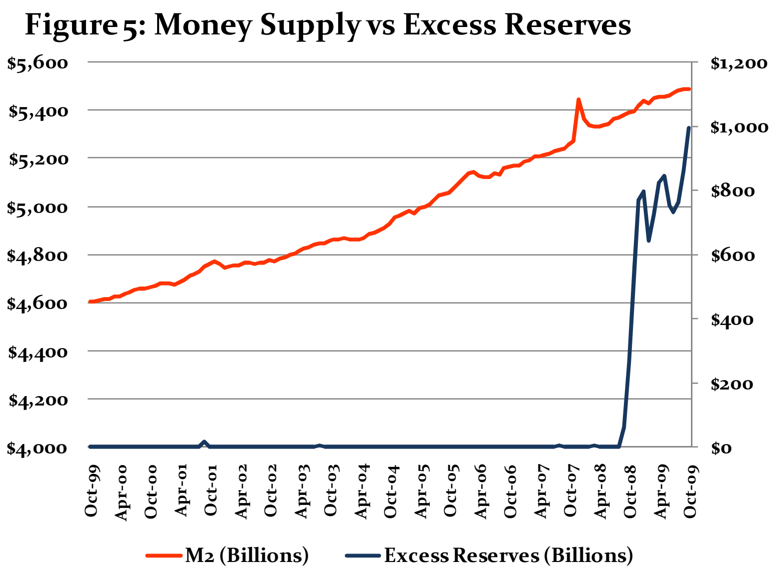


Among the most pressing concerns at the national level are a jobless recovery, inflation, and a weak dollar. We address each briefly in turn to present the backdrop against which the state and local forecasts are derived.

As economies emerge from recession, the initial surge in economic activity is nearly always jobless as demand is met through productivity gains rather than new employment. It is only as recovery persists and productivity increases are exhausted that hiring on a significant scale occurs. While measuring productivity is admittedly complicated in production processes increasingly characterized by imported inputs, we nonetheless expect productivity gains to accommodate much of the expected growth in economic activity in 2010. Indeed, given the scale of employment losses in this recession, the economy would need at least 3-5 years of robust monthly job creation to return to pre-recessionary levels. We project modest job losses to continue throughout the first half of 2010 offset by gains in the latter half of the year.

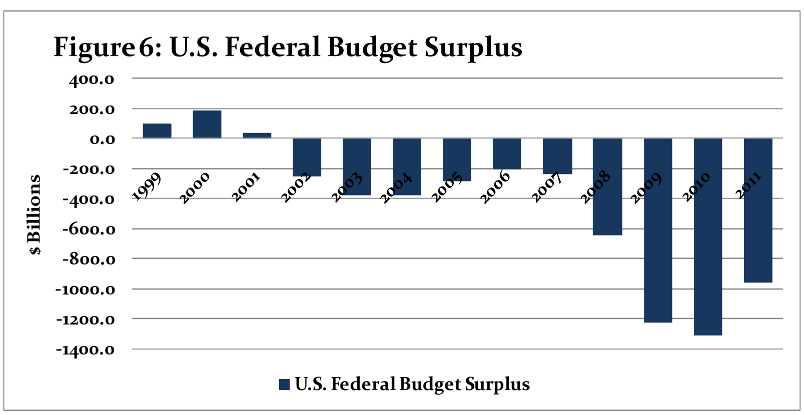


Recessionary exits are often accompanied by upticks in the unemployment rate; the reason offered by simple mathematics. The Bureau of Labor Statistics includes in its count of the unemployed only those who are willing to work, available for work should an opportunity present itself, and actively seeking employment. Workers who lose their job, grow discouraged, and abandon an active job search fall from the ranks of the unemployed despite wanting, and not having, a job. As the labor market improves and prospects for employment return, these discouraged workers return to the labor process by way of the unemployed classification. In doing so, the unemployment rate often increases. We project job losses and discouraged workers abandoning a search will keep the unemployment rate at or above 10% for much of the year, with a labor market recovery driving the rate higher before it falls in late 2010. Our current forecast calls for an average yearly unemployment rate of 10.2%.



The Federal Reserve, through a number of new credit facilities, has successfully provided support to the financial sector while staving off deflationary concerns. However, there remains an unprecedented amount of liquidity on bank balance sheets that must be absorbed by the Fed as they unwind the policies of the previous year. The situation is underscored by a Fed balance sheet that has swelled to over $2 trillion while excess reserves of financial institutions have increased similarly to roughly $1 trillion – over 50 times greater than the peak excess reserves during the post 9-11 recession! The problems facing the Federal Reserve are now matters of logistics and timing; specifically, when and how to back away from an unprecedented expansion of the central bank's balance sheet. At present, we expect inflation to remain well controlled in the short term, but remain concerned about inflationary pressures and/or destabilizing restrictive policy as the Fed tries to manage the recovery.

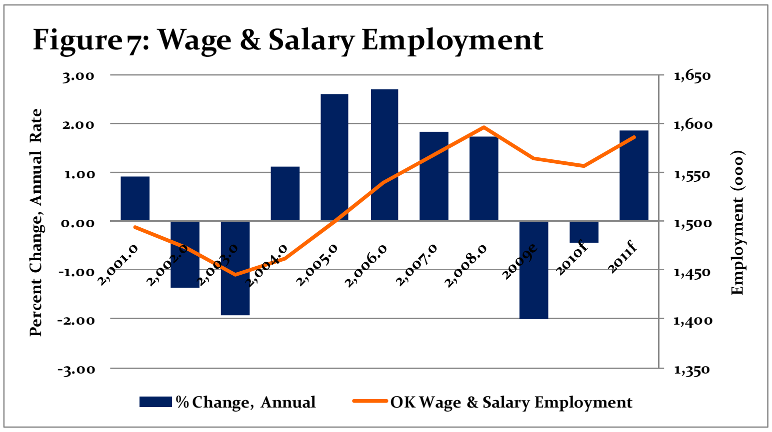
Finally, a weak U.S. dollar that has contributed to commodity price increases and dollar carry trades abroad is likely to remain weak by historical standards, but strengthen modestly throughout the course of the year, driven by a combination of recovery and higher interest rates.



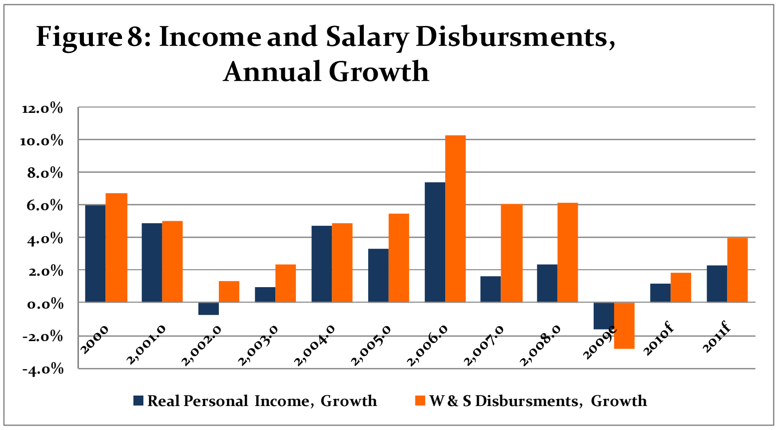
The combination of falling tax revenues and fiscal stimulus financing have driven Federal budget deficits to heights not seen in many decades. Current estimates put 2009 deficits at roughly 13% of GDP with projected deficits in 2010 and 2011 just above and just below 10% of GDP respectively. While large deficits are indeed potentially damaging, some perspective is required. First, in contrast to the asset collapse kicking off Japan's "lost decade," this collapse is a (nearly) global phenomenon leaving the world's developed economies with the largest deficits of recent years. Dealing with deficits will be a challenge for the next several decades, and dealing successfully would leave the U.S. economy in a continued position of relative strength. Second, outlays as a percent of GDP are up only moderately from where they have been in recent administrations, suggesting a transition to more manageable levels of debt may not be far off. Finally, and most importantly, budget deficit figures continue to be among the most widely reported yet least understood releases of economic data. Only tomorrow will tell how significant are today's deficits.

Oklahoma Economic Conditions

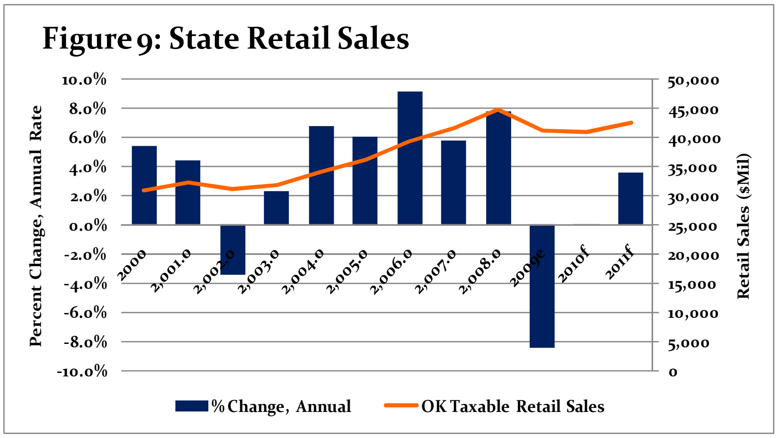
Where do we stand relative to the nation?



As an energy state, Oklahoma often lags the nation entering recessions, particularly recessions induced in part by high energy costs. Such was the case with the current recession. Falling home prices eroded the solvency of household and bank balance sheets in pockets of the country, generating secondary effects of credit tightening, declining activity, and a fall in demand for energy. It was only as oil and natural gas prices fell precipitously last fall that Oklahoma began to feel the full effects of the recession. While a robust energy sector provides some insulation from recessions, Oklahoma is clearly not immune to the effects of a global credit crisis. Indeed, it is likely that only as revisions to state and local data are made that we will appreciate the full extent of the recession within our state. That said, it is important to remember that Oklahoma has fared much better than many parts of the nation and Oklahomans have received significant praise for their economic prudence and resiliency. Jobs contracted at an annual rate of 2% in 2009 and are expected to be flat in 2010. While our current forecast calls for a slight contraction (0.4%), a slight expansion is possible if the labor market turns a few months earlier than we project.



After nearly a decade of strong growth that brought Oklahoma per capita income to approximately 90% of U.S. per capita income, both income and wage disbursements contracted in 2009 (-1.6% and -2.8% respectively). Relative to previous recessionary experiences in the state, income contraction appears disproportionate to job losses. This likely signals revisions to the jobs data, as well as explains much of the disappearing state and local tax revenue through fiscal year 2009 and continuing in FY 2010. We forecast only modest income growth ahead as a slow recovery, regulatory uncertainty, and tepid borrowers combine to keep commodity prices stable at levels much below their 2008 peak. While much could change in the interim, a full recovery may be as far away as 2012.



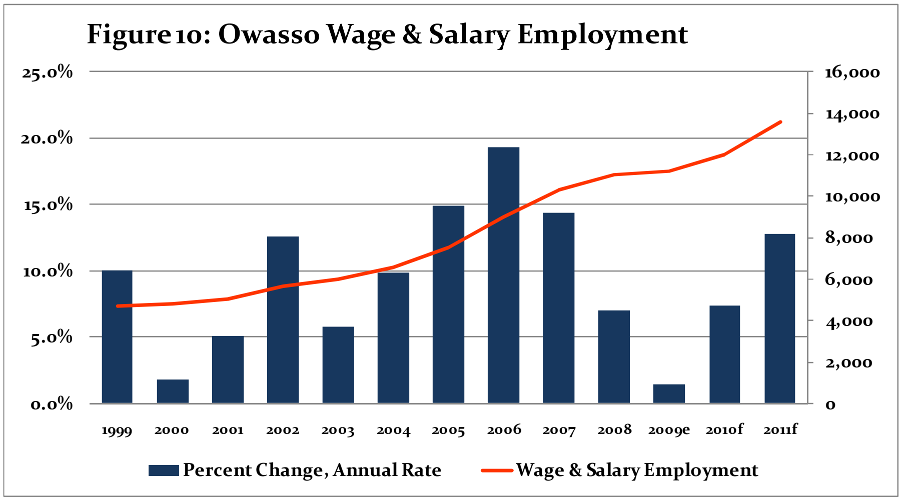
With the expansion of income through much of the decade came an expansion of retail sales. While the precipitous fall in energy prices directly impacts severance tax collections and indirectly income tax collections at the state level, it was only as the recession progressed that retail sales fell dramatically impacting the budgets of so many local governments. Retail sales contracted at an 8.5% rate in 2009 and are forecasted to be flat in 2010 as Oklahomans increase savings rates to restore household balance sheets and prepare for uncertainty ahead. We project that while slow, the current recovery will hold with no significant secondary event in the near term. Retail sales are thus expected to show growth towards the end of 2010 and into 2011, suggesting continued tough times for municipal budgets around the state.

Oklahoma Economic Conditions: Summary

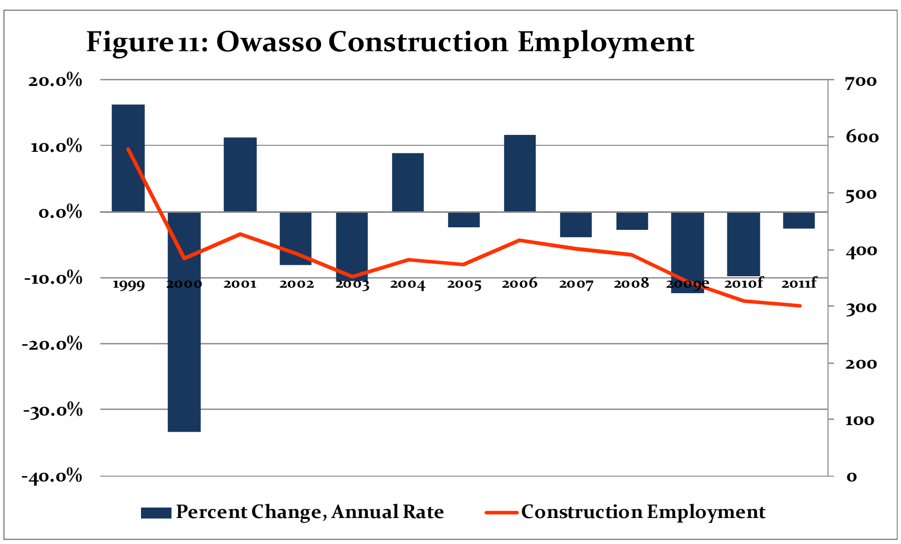
The biggest obstacles facing recovery in the state are energy and fiscal budget related. The energy sector has enjoyed a recovery in commodity prices, but the drivers of this price increase remain unclear. To the extent that they represent protection against a weak dollar or bullish sentiments of recovery, current prices may prove unsustainable and yield to unwanted price volatility. Also volatile is the prospect for energy policy reform at the national level. While energy reform has taken a backseat to stimulus and health care reform, we expect the discussion to be revived at a later date. The regulatory uncertainty is particularly concerning to Oklahoma's many small and medium sized independent producers. We expect production activity to remain relatively subdued until prices not only recover, but are reasonably stable as well. Finally, fiscal challenges at the Capitol and around the state pose challenges not just to policymakers, but also to the individuals employed in state and local service and the firms with whom they deal. A removal of state and local discretionary spending from the economy, while likely required to restore fiscal balance, will serve to partially offset the federal stimulus spending within the state. We currently anticipate a tight 2010 fiscal year before seeing some modest growth in revenues in FY 2011.

Employment and Income are projected to be relatively flat with early setbacks offset by second half gains. The unemployment rate in the state is expected to increase modestly early in 2010 before dropping below 7% by late spring/early summer. Oklahoma should hold the income gains made on the nation during the last decade. Across the state, we see little in the way of further deterioration of conditions. Rather, 2010 is likely to be a year of slow recovery, with much new information revealed about the strength of the recovery globally offering a clearer insight into 2011.

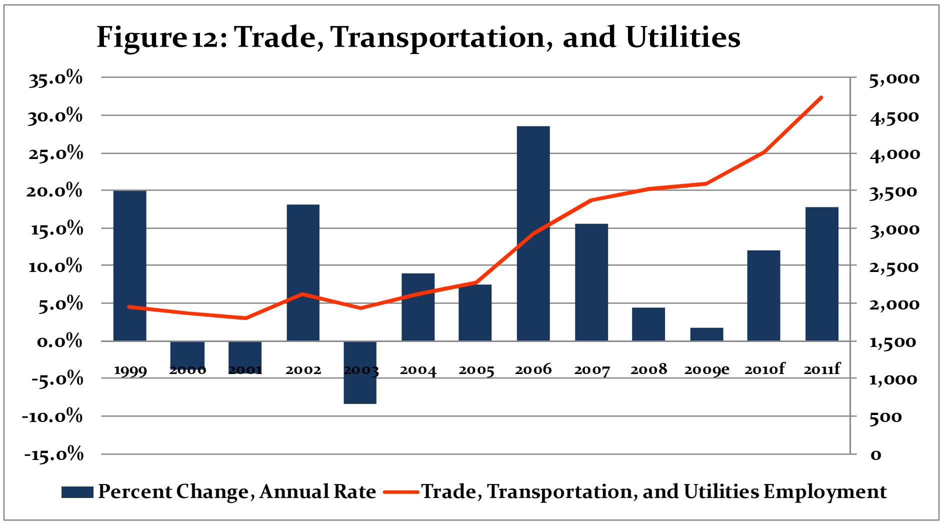
Owasso: 2010 Economic Outlook



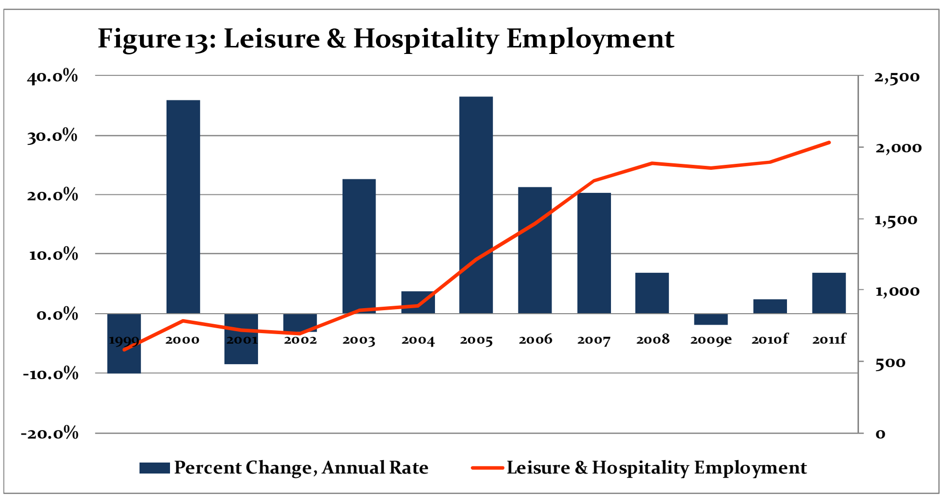
While much of the state enjoyed broad employment growth throughout the past decade, few areas witnessed growth to the extent enjoyed in Owasso. The aggressive expansion of Owasso as a residential Tulsa suburb has been accompanied by the location of industries to support a residential community. Owasso now appears to moving towards a new phase of economic development characterized by the location of wealth generating industries that will, in turn, attract and enhance the local labor force. The current forecast estimates a significant slowing of job growth in 2009, consistent with the national economy and structural makeup of the community. We foresee a return to modest job growth in 2010 with aggressive growth returning in 2011. However, significant economic headwinds are forming that may yet cast into question the prospect for a broad recovery carrying into 2011.



Owasso construction employment shows signs of modest contraction through the decade even as Owasso experienced significant job growth accompanied by commercial and residential development. The data series serves to highlight some of the challenges in forecasting for small communities for whom timely and thorough data collections are unavailable. The employment data should reflect construction jobs (not projects) located in Owasso. It is certainly possible that the release of Census 2010 data will reflect a different pattern entirely.

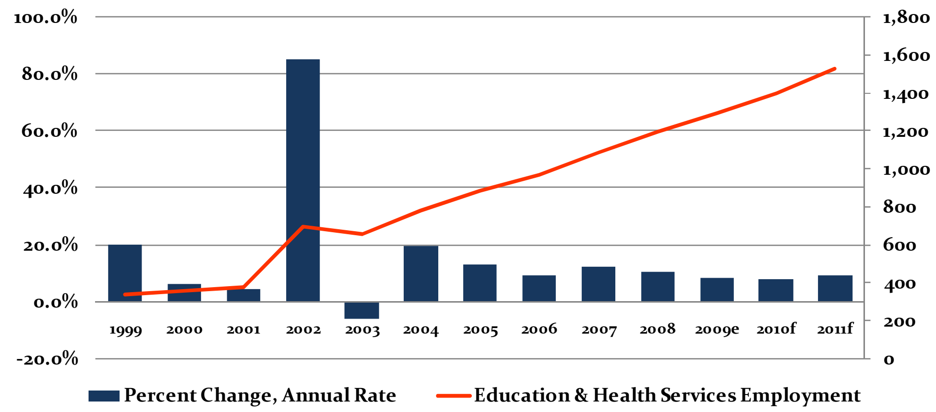


Because Owasso serves as a largely residential suburb, its employment patterns mimic somewhat that of a university community. The largest sector in terms of employment is Trade, Transportation, and Utilities accounting for almost one-third of all jobs in Owasso. The majority of these jobs likely fall in the Retail Trade subsector, providing support to residents who live in Owasso and work in Tulsa. This reliance on Retail Trade also provides a broad a retail sales tax base for the municipality. However, further development almost certainly requires a transition to new, moderate income jobs located in Owasso to serve as a local base of economic activity.



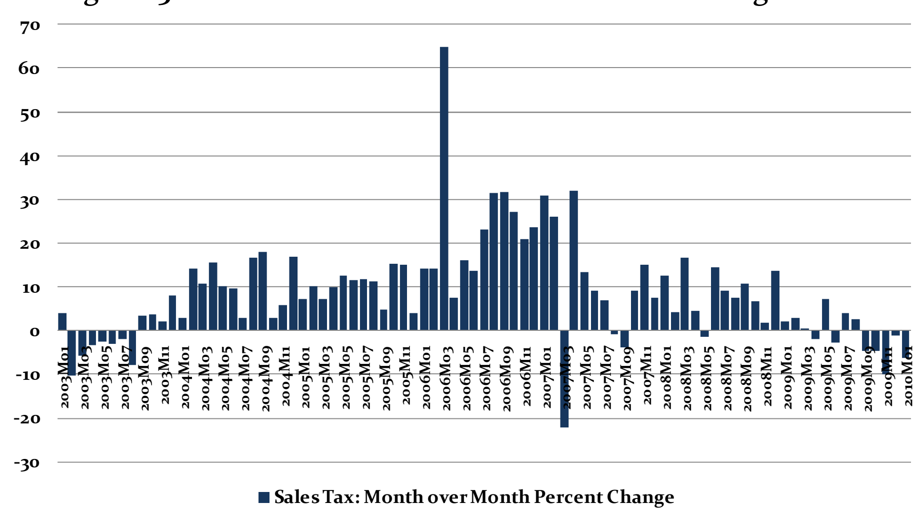
Again, similar to a college town, Owasso enjoys broad employment in the Leisure and Hospitality sector, accounting for nearly 20% of all employment, with the majority of these jobs likely in the Accommodation and Food Services subsector. Like employment in Trade, Transportation, and Utilities, employment in Hospitality will stagnate in 2009 and grow only modestly in 2010 as consumer discretionary spending remains soft. Our current forecast looks for 2010 growth only to return the industry to its 2008 employment levels.

Figure 14: Education and Health Services Employment

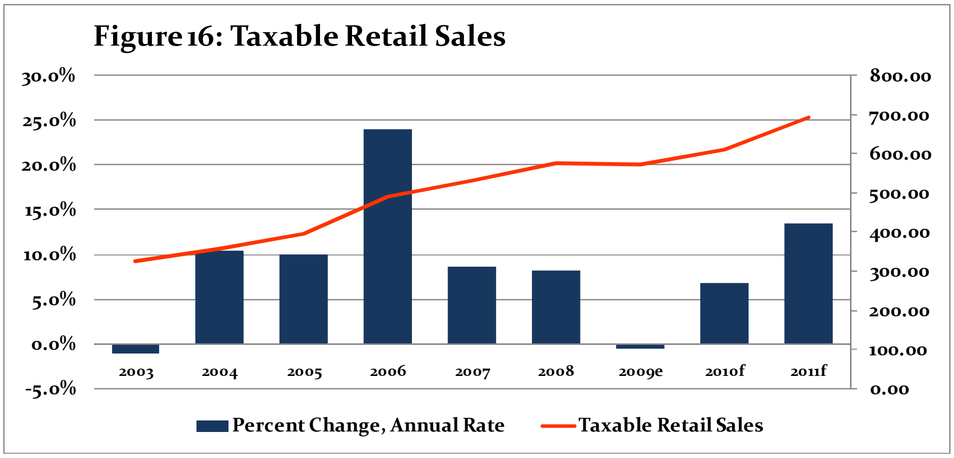


Where Owasso differs from a typical college town is in its robust and growing Education and Health Services sector. Demographic differences create a demand for accessible and reliable personal and family health care. The sector is projected to grow steadily throughout the forecast period as population growth maintains a base of demand. The announced TCC/Tulsa Tech facility is expected to contribute to growth in this sector as well as reinforce Health Services growth by providing local opportunities for education and training.

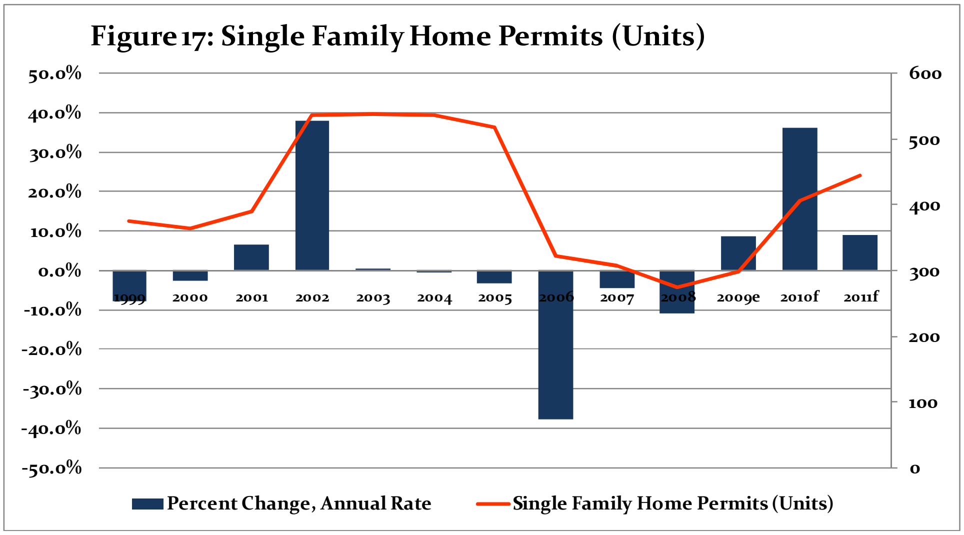
Figure 15: Sales Tax: Month over Month Percent Change



In spite of challenging conditions nationally and across the state, retail sales tax collections remained relatively stable in Owasso through 2008 and into 2009. Monthly collections are now down relative to the same month in the previous year, a pattern that is likely to continue intermittently through the spring. The bulk of the fiscal discomfort should be concentrated in FY 2010, as collections stabilize in late 2010 and carry into 2011, assuming a self-sustaining recovery can hold that long.



With a significant allocation of Owasso labor dedicated to retail trade and food services to cater to a growing residential community, retail sales continue to grow with the population. Discretionary spending contracted in 2009 as consumers faced a tight job market, declining incomes, and investment losses, contributing to a modest contraction in taxable retail sales. Retail sales are projected to recover in 2010, although the current forecast of 6.7% growth likely overstates the strength of the recovery. We look for more modest gains in 2010 with a mid-year return to consumer activity.



Single family housing permits rose to more than 500 per year from 2002 through 2005 before falling to slightly more than 300 per year in 2006 and 2007. Activity slowed considerably in 2008 and 2009, but is forecast to revert to growth in 2010. However, the stimulus driven nature of the 2010 recovery is likely overstating the impact on residential development. While we anticipate growth in single family construction in 2010, we have reservations about the extent currently projected in the model.

Owasso Employment and Economic Indicators Forecast Summary

(Thousands, percent change at annual rate)

Sector	2001	2002	2003	2004	2005	2006	2007	2008	2009e	2010f	2011f
Wage & Salary Employment	**5,020**	**5,652**	**5,979**	**6,568**	**7,547**	**9,008**	**10,300**	**11,026**	**11,188**	**12,017**	**13,554**
	5.1%	12.6%	5.8%	9.9%	14.9%	19.4%	14.3%	7.0%	1.5%	7.4%	12.8%
Ag, Forestry, Fishing, and Hunting	**0**	**3**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
	0.0%	0.0%	-100.0%	0.0%	0.0%	0.0%	0.0%	70.1%	16.8%	8.4%	0.4%
Mining	**79**	**35**	**77**	**80**	**74**	**80**	**102**	**141**	**142**	**169**	**243**
	-7.9%	-55.9%	120.2%	4.3%	-7.8%	8.0%	27.7%	38.2%	0.9%	18.8%	43.8%
Construction	**428**	**393**	**352**	**383**	**374**	**418**	**402**	**391**	**343**	**309**	**301**
	11.2%	-8.1%	-10.5%	8.9%	-2.4%	11.7%	-3.8%	-2.6%	-12.4%	-9.8%	-2.6%
Manufacturing	**448**	**423**	**703**	**695**	**750**	**1,021**	**1,142**	**1,183**	**1,188**	**1,328**	**1,503**
	31.0%	-5.6%	66.2%	-1.2%	7.9%	36.1%	11.9%	3.5%	0.5%	11.7%	13.2%
Trade, Transportation, and Utilities	**1,794**	**2,117**	**1,940**	**2,113**	**2,273**	**2,921**	**3,375**	**3,524**	**3,586**	**4,016**	**4,731**
	-4.3%	18.0%	-8.4%	8.9%	7.5%	28.6%	15.5%	4.4%	1.8%	12.0%	17.8%
Information	**45**	**48**	**63**	**41**	**61**	**65**	**67**	**60**	**64**	**76**	**91**
	60.8%	6.5%	31.3%	-34.9%	48.9%	6.5%	2.6%	-10.3%	6.8%	19.1%	19.7%
Financial Activities	**299**	**364**	**399**	**482**	**487**	**508**	**535**	**531**	**492**	**452**	**432**
	4.9%	21.8%	9.5%	20.8%	1.0%	4.3%	5.4%	-0.7%	-7.3%	-8.1%	-4.5%
Professional and Business Services	**325**	**446**	**466**	**574**	**903**	**971**	**1,171**	**1,383**	**1,292**	**1,299**	**1,525**
	25.5%	37.0%	4.6%	23.1%	57.4%	7.6%	20.5%	18.2%	-6.6%	0.5%	17.5%
Educational & Health Services	**375**	**694**	**653**	**782**	**885**	**965**	**1,084**	**1,195**	**1,296**	**1,399**	**1,525**
	4.3%	85.2%	-5.8%	19.7%	13.2%	9.1%	12.3%	10.3%	8.4%	7.9%	9.1%
Leisure & Hospitality	**720**	**698**	**855**	**887**	**1,211**	**1,468**	**1,766**	**1,887**	**1,850**	**1,896**	**2,028**
	-8.5%	-3.1%	22.6%	3.8%	36.5%	21.2%	20.3%	6.8%	-2.0%	2.5%	7.0%
Other Services	**490**	**421**	**458**	**527**	**531**	**589**	**651**	**724**	**927**	**1,066**	**1,165**
	42.7%	-14.0%	8.8%	15.0%	0.7%	10.9%	10.7%	11.1%	28.1%	15.0%	9.3%
Unclassified Industries	**17**	**13**	**14**	**8**	**2**	**5**	**6**	**7**	**7**	**8**	**8**
	-48.5%	-23.0%	8.2%	-42.6%	-74.9%	150.2%	14.6%	13.7%	10.4%	7.8%	5.9%
Taxable Retail Sales ($Mil)	**0.00**	**328.17**	**324.40**	**358.31**	**394.03**	**488.74**	**530.69**	**574.48**	**571.16**	**609.70**	**691.82**
	0.0%	0.0%	-1.2%	10.5%	10.0%	24.0%	8.6%	8.3%	-0.6%	6.7%	13.5%
Sales Tax Revenue ($Mil)	**0.00**	**9.85**	**9.73**	**10.75**	**11.82**	**14.66**	**15.92**	**17.23**	**17.13**	**18.29**	**20.75**
	0.0%	0.0%	-1.2%	10.5%	10.0%	24.0%	8.6%	8.3%	-0.6%	6.7%	13.5%
Wage & Salary Earnings ($Mil)	**118.9**	**126.4**	**133.2**	**152.0**	**177.7**	**209.6**	**243.6**	**274.0**	**284.1**	**293.1**	**330.5**
	14.3%	6.3%	5.3%	14.2%	16.9%	17.9%	16.2%	12.5%	3.7%	3.2%	12.8%
Population	**19,831**	**20,749**	**21,833**	**22,736**	**23,894**	**25,115**	**26,352**	**27,580**	**28,760**	**29,977**	**31,241**
	4.5%	4.6%	5.2%	4.1%	5.1%	5.1%	4.9%	4.7%	4.3%	4.2%	4.2%
School Enrollments	**6,783**	**7,037**	**7,282**	**7,510**	**7,900**	**8,196**	**8,507**	**8,568**	**8,731**	**9,042**	**9,359**
	3.0%	3.7%	3.5%	3.1%	5.2%	3.7%	3.8%	0.7%	1.9%	3.6%	3.5%
Business Establishments	**529**	**556**	**569**	**615**	**674**	**689**	**710**	**748**	**785**	**823**	**861**
	5.2%	5.1%	2.3%	8.1%	9.6%	2.2%	3.1%	5.3%	5.0%	4.8%	4.6%
Single Family Home Permits (Units)	**389**	**537**	**538**	**536**	**518**	**322**	**308**	**275**	**299**	**407**	**444**
	6.7%	38.0%	0.2%	-0.4%	-3.4%	-37.8%	-4.4%	-10.8%	8.7%	36.3%	9.1%
Single Family Home Permits Value ($Mil)	**40.1**	**53.9**	**52.5**	**53.1**	**54.5**	**34.8**	**33.2**	**28.1**	**31.3**	**43.5**	**47.0**
	5.0%	34.5%	-2.7%	1.2%	2.6%	-36.1%	-4.7%	-15.3%	11.4%	39.0%	8.2%
[e]Estimate [f]Forecast	2001	2002	2003	2004	2005	2006	2007	2008	2009e	2010f	2011f

Source: Bureau of Labor Statistics, OSU Center for Applied Economics Research. [e]Estimate [f]Forecast