

Economic Forecast

2009 - 2010 EDITION

A Year of Stabilization Expected in 2010, Followed by Sustained Recovery in 2011

Next year — 2010 — may be a year of stabilization in the Hawaii economy, but it will likely be 2011 before sustained economic recovery sets in, in spite of an improving picture at the U.S. national level and tenuous recovery in Japan.

Patience may be the keyword in the short run. Recovery in the Islands will likely be a good bit slower than the descent into recession.

Forecasts for 2010:

- **Job Growth: Minus 0.5%** — The labor market is usually a lagging indicator, so don't expect that to be where our recovery starts. Other things like tourism have to show signs of sustained improvement before employers start to hire again. Plus, fiscal pressures will restrain job creation in the public sector. And the construction sector, the major source of job creation in the recent boom, has to bottom out. I expect continued job declines for 2010 as a whole, though at a much lower rate of about 0.5%.
- **Unemployment Rate: 7.5%** — As with jobs, the unemployment rate lags the cycle. All the pressures I mentioned above for job growth apply here also. Unemployment could remain at the same level as 2009, or it could actually rise some, at least remaining near the 7.5% range.
- **Inflation: +1.0%** — We were all surprised by 2009's first half inflation rate of 0.3% for the state. The price rise for the remainder of 2009 will remain muted as well. Given a

continued fragile local economy in 2010, any price pressures will have to originate at the external level — such as a surge in oil prices driven by national and global recovery. Still, it's a pretty safe bet that local inflation won't be among the bigger problems in 2010. Stable prices are a good thing, and lower inflation makes inflation-adjusted growth numbers like real personal income or real state GDP look better.

- **Visitor Arrivals: + 1.7%** — Even as the national recession ends, long distance, relatively expensive leisure travel will likely remain weak. Price discounting here helps, but revenues are hit harder. And remember that the rest of the world is in this price war also. But arrivals have fallen so far in 2008 and 2009 that at least some growth won't be that difficult to achieve. As 2010 progresses, without unforeseen shocks the visitor industry could look increasingly better. But if wealth losses continue to be a drag on U.S. consumption growth, those who do make the trip to Hawaii may continue to be in the mood to spend less than usual when they get here.
- **Real Personal Income Growth: +0.5%** — Inflation-adjusted personal income growth is the broadest measure we forecast. I've characterized 2010 as a year of transition to better and more sustained growth. We may see year over year growth in some of the numbers about mid-year. That growth will likely be sub-par even

THE FORECAST

	2009 (Estimate)	2010 (Forecast)
Job growth	-3.0%	-0.5%
Unemployment rate	7.2%	7.5%
Inflation (CPI)	+0.5%	+1.0%
Visitor arrivals	-5.5%	+1.7%
Real personal income	-2.0%	+0.5%

for the second half of 2010, but could break into positive territory for the year as a whole. And remember, as long as inflation remains muted, inflation-adjusted numbers like this one will look better.

At times like this we all look for silver linings. One silver lining to a slow recovery is that it gives us all time to consider priorities and plan for future growth when it does eventually come. If that is done thoughtfully, there is less chance of making hasty, poorly thought out decisions on the spur of the moment.

I said a year ago that — by 2011 — it's possible for the Hawaii economy to be firing on all cylinders once again.

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A Year of Stabilization Expected

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I'll stick by that forecast. The lag with which the Hawaii economy trails the national one varies from cycle to cycle, but we can draw optimism from the picture that's now emerging at the national level — an end to the longest recession since the 1930s.

Shape of Local Recovery: An L With a Slow Rise from the Bottom

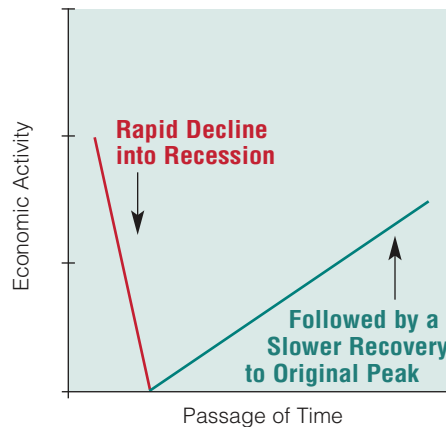
The year 2009 has brought Hawaii more of what began in 2008. The question on everyone's mind nowadays is when we will see better times. Many have tried to describe the national economy recently by reference to various letters: Will our current local recession be V-shaped, U-shaped, L-shaped, or even a double-dip, W-shaped?

It may not exactly be any of the letters in this alphabet soup, but may be closer to an "L" than any of the other possibilities (See Chart 1.) That is, an L with a steep drop-off — which we've already seen — and a bottom that more slowly trends upward. The slope of that upward trend on the bottom of the L depends on several things, but chief among them for Hawaii is the recovery of our main industry, tourism. And that, in turn, depends on how the Mainland economy recovers, especially the west coast.

We have to recognize that, with respect to tourism, Hawaii is in the business of selling a luxury product to the rest of the world. Even a budget vacation to Hawaii is among the first of things eliminated by a typical household in hard times, and it may be among the last of things restored as the economy recovers.

The recent national recession has been characterized by low consumer confidence and spending. For that, we can thank the reductions in financial portfolio wealth in 2008. So the question in Hawaii is: How will long-distance leisure travel fare in this more frugal world? Will the shift to frugality be transient, or longer in nature?

CHART 1 • WHAT AN L-SHAPED RECOVERY LOOKS LIKE



Maybe a reference to some economic cycle terminology is useful here. Recessions are measured from the peak of the cycle to the trough — the trough being when positive growth starts again. But the "recovery" period lasts until we achieve a level that puts us even with the previous peak. Now, if we're talking about a recovery that has a much shallower slope than the previous decline — as with the stylized "L" that I mentioned above — the recovery could be a good bit longer than the earlier decline.

Let's do a little arithmetic. Taking visitor arrivals as an example, if they peaked at about 7.6 million in 2007, then fell as they did in 2008 and 2009, it would take average growth in the 5-6% range for the next three years to get back to that previous peak. And that's far above any forecast in the state over that time frame now.

The Drop-off: 2009 Compared to 2008

Chart 2 shows some numbers that illustrate the first part of that L. The Hawaii state economy slid precipitously into recession in the second quarter of 2008. The U.S. national recession that began a few months earlier had something to do with that, but there were a number of local developments that made the decline more severe than it would have otherwise been.

CHART 2 • CHANGE IN MAJOR HAWAII ECONOMIC INDICATORS (2009: Q1 VS. 2008: Q1)

	Percent Change
Jobs	-3%
Unemployment rate rise	+4%
Visitor arrivals	-14%
Visitor spending	-18%
Private building permit values	-27%
General Excise Tax revenues	-13%
Matson container volume	-14%

Sources: State Department of Business, Economic Development and Tourism; Department of Labor; Alexander & Baldwin Inc. 10Q filing

Some of the major 2008 blows were: Loss of airlift with the exit of Aloha Airlines and ATA; two fewer cruise ships, followed by a disappointing summer for tourism with higher fuel costs and airfares; and finally the financial meltdown in the fall of 2008 which dampened everyone's wealth and expectations.

Since the first quarter of 2008 was the last decent quarter the Hawaii economy had, the dramatic nature of the drop can be seen by comparing the change in major economic indicators from that quarter to the first quarter of 2009, just a year later.

- State jobs were 3% lower than in the same quarter a year earlier.
- The state unemployment rate rose dramatically by over 4 percentage points, to 7%, in just one year.
- Visitor arrivals fell by 14%.
- Total visitor spending had fallen by almost 18%.
- The value of private building permits was almost 27% lower.
- General excise tax receipts were 13% less.
- And Matson container volume was 14% lower.

Seldom does any economy experience such enormous declines in so short a period, and the fallout can't help but be substantial.

Real Personal Income Growth

Inflation-adjusted personal income growth illustrates well the local economic cycle, and you see that in Chart 3. It's one of the broadest and most often quoted measures of our state economy. It includes not just wages and salaries but also investment income, transfer payments, and other income sources.

That nine-year expansion that ended in the early 1990s was bracketed by recession years in 1981 and 1991 that corresponded to U.S. national downturns. Then the prolonged slump of the mid-1990s ensued, lasting longer than many first thought. After that, the longer 11-year expansion followed. The 1981 recession that you see in the slide was the V-shaped variety; that of the mid-1990s was more L-shaped like the present one is likely to be.

For 2009, we project a contracting economy. That contraction would be worse for inflation-adjusted numbers like real personal income and state real GDP if inflation were not coming in sharply lower than originally projected.

Hawaii Job Market

Another broad measure of the state's overall economy is job growth (Chart 4). Over the long haul, it shows about the same cycle as real personal income growth. This is not a dollar figure, so it requires no adjustment for inflation. Jobs will also show a significant contraction for 2009. So far, job losses have been pervasive across almost all private sector categories.

The unemployment rate (Chart 5), another broad labor market indicator, mirrors the negative job growth, and will likely rise over 3 percentage points for this year over 2008, to over 7%. You have to go back to the 1970s in Hawaii to find a jobless rate over 7%. That's still easily at least 2 percentage points below what the national rate will be for the year.

Hawaii Inflation Rate

The weak economy has driven the local inflation rate rapidly toward zero (Chart 6). Honolulu gets a CPI figure only twice a year, but in the first half of

CHART 3 • STATE REAL PERSONAL INCOME

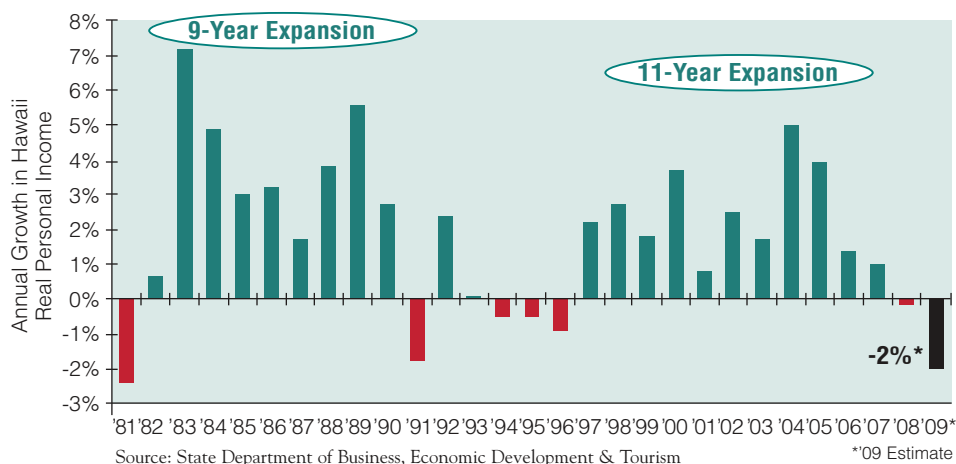


CHART 4 • STATE NON-FARM JOB GROWTH

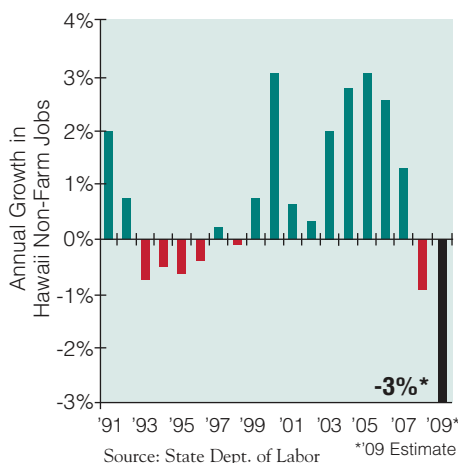
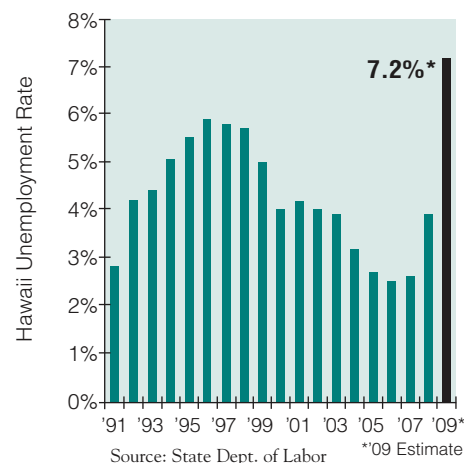


CHART 5 • HAWAII STATE UNEMPLOYMENT



2009 it was only 0.3% over a year earlier — a good bit lower than all local forecasts. (The comparable national figure was actually deflation — at -0.6%.)

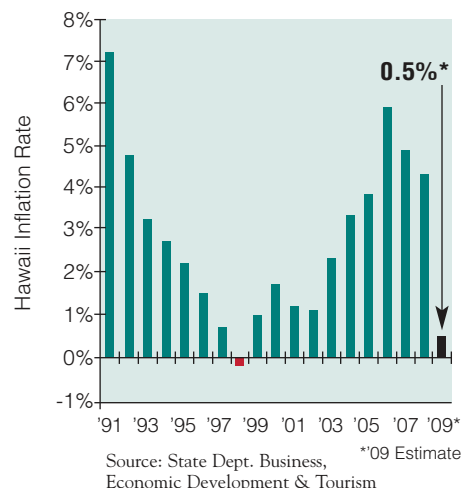
Lower inflation makes real growth numbers look better, because less is taken out of current dollar figures for increases in the price level. Inflation for the whole year, which we won't get until February 2010, will fall in a similar range.

General Excise Tax Revenue

Growth in the state's General Excise Tax revenue (Chart 7, next page) is often inspected as a gauge of economic activity, because all transactions are subject to it. And since that's the largest component of the total State General Fund, it also reflects the government

(continued on page 4)

CHART 6 • HAWAII INFLATION RATE



A Year of Stabilization Expected

(continued from page 3)

fiscal situation. Both GET revenue and the General Fund will be off well into double digits in 2009, and forecasts of the Council on Revenues have been revised down repeatedly recently.

Not only does this reflect the economy, it also throws light on what government must do to balance its budget. Unlike the federal government, which can borrow virtually without limit to finance its deficits, state and local governments don't have the luxury of endless deficit spending and countercyclical fiscal policy.

Ironically, the legal requirement to balance the budget can force state government to do undesirable things at just the wrong time. That's happening now. Regardless of whether these budget balancing attempts involve worker furloughs, layoffs, other spending cuts, or tax increases, the effect is the same — less money in circulation and a further drag on the economy. And state government is large enough that this drag can be significant, triggering even further reductions in revenue forecasts. A significant part of a projected weak economy involves these unpleasant, if necessary, government actions.

Credit Card Spending

From First Hawaiian Bank's own internal data, a number always worth watching is credit card spending growth at the bank's 300 largest merchant customers. This figure reflects both tourism and local spending, so it's an excellent gauge of the overall picture. Chart 8 shows yet another indication of a deteriorating economy, after earlier boom years. Following flat growth last year, it's down in 2009.

Car and Truck Sales

New car and truck sales are always a good indicator of consumer confidence in buying big-ticket items other than homes. This number (Chart 9) is another one that traces Hawaii's business cycle well over the long haul.

CHART 7 • GENERAL EXCISE TAX GROWTH

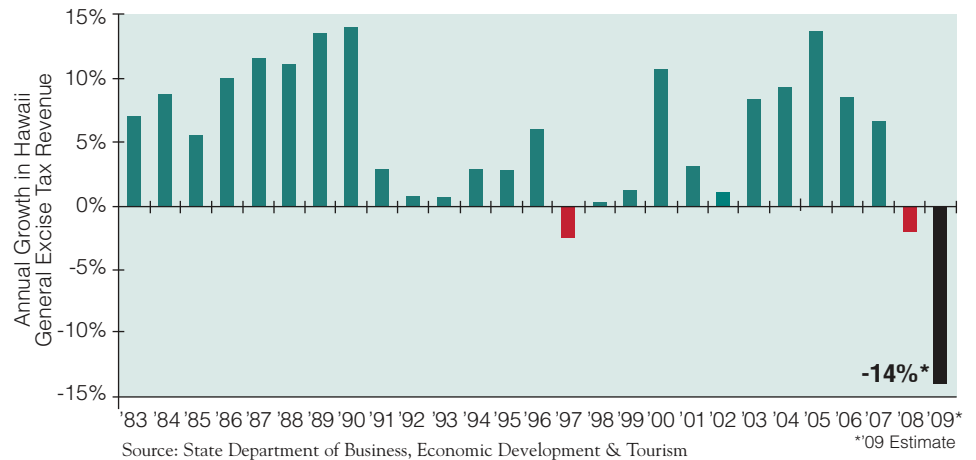
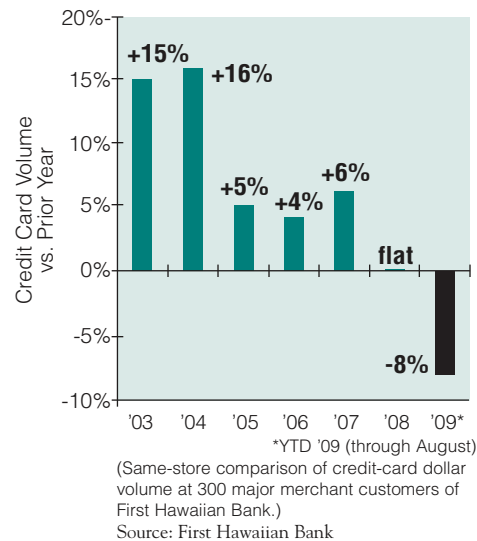


CHART 8 • CREDIT CARD SPENDING GROWTH



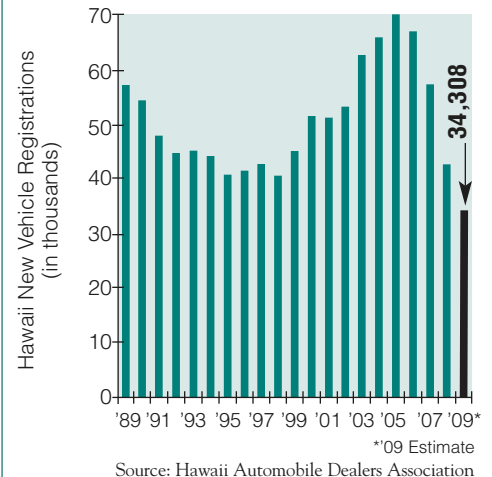
The boom after the 1990s' slump is apparent in the chart, but you can see the recent dramatic slowdown. For 2009, the Hawaii Auto Dealers Association projects just over 34,000 new car sales, less than half of the peak year of 2005, which saw 70,000 registrations.

Hawaii Visitor Industry

The sector of the Hawaii economy hardest hit in 2009 continues to be the visitor industry, as Charts 10 and 11 show all too vividly. That's a genuine blow when we consider all the other things that feed off that sector.

Visitor spending is what really counts, no matter how many come,

CHART 9 • HAWAII NEW VEHICLE REGISTRATIONS

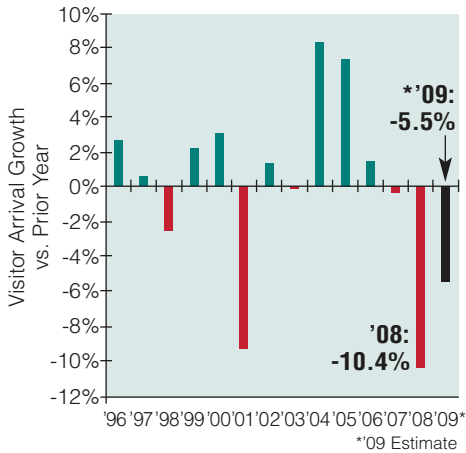


where or how long they stay, or where they come from. And spending declines have been far outstripping the drop in arrivals. The declines have diminished some as 2009 has progressed, because the first quarter was compared to the stronger 2008 first quarter.

The Neighbor Islands have been particularly impacted this year. (See Page 6 for more detail on Neighbor Island tourism.)

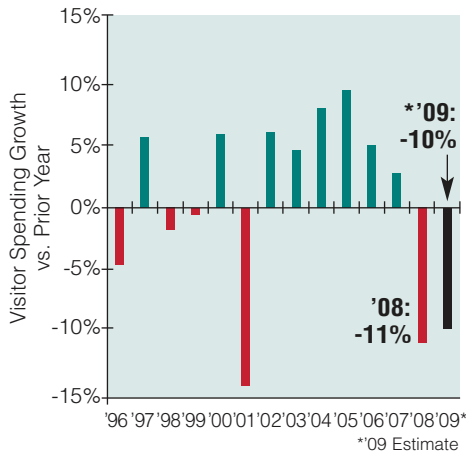
Broken down by source in 2009, the Japan market has been down especially, with H1N1 (swine) flu and other scares making Japanese travelers particularly skittish. But airlift generally has been holding up, and the numbers would be worse if time-share had not shown relatively greater resilience

CHART 10 • HAWAII VISITOR ARRIVAL GROWTH



Source: State Department of Business, Economic Development & Tourism

CHART 11 • HAWAII VISITOR SPENDING GROWTH



Source: State Department of Business, Economic Development & Tourism

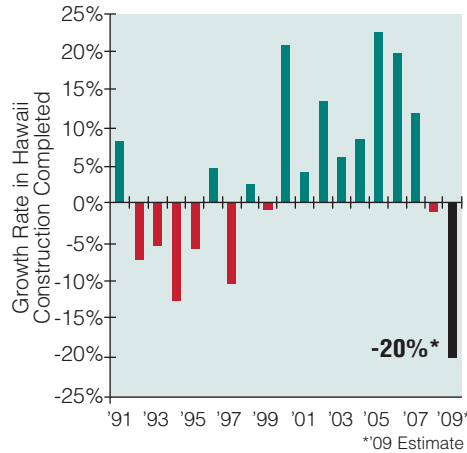
because owners have already paid for much of their vacation.

Construction Industry

Another aspect of Hawaii's recession is the construction sector, which would be on the downside of its natural cycle now anyway even without other developments. Nonetheless, the financial turmoil of the past year has made this sector worse because of general uncertainty and financing problems.

The local construction cycle peaked in 2007 at the statewide level, measured by construction completed in the tax base shown in Chart 12. There were deep drops in both residential and

CHART 12 • HAWAII CONSTRUCTION GROWTH



Source: State Department of Business, Economic Development & Tourism

commercial permit values during 2008, at rates that have been continuing into 2009. This indicates that it will probably be a while before a gradual recovery ensues in the construction sector.

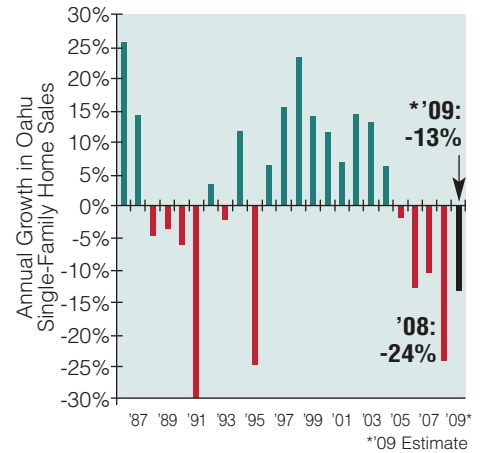
Commercial and resort development will continue to be impacted for some time, and residential construction won't pick up until home prices find a bottom. A good bit of the outlook for the construction sector depends on whether federal fiscal stimulus money will move forward more rapidly, and if a major project like Honolulu mass transit can ramp up.

Oahu Real Estate Market

Residential real estate is always an important sector of any local economy — not just because of activity there but also because of its effect on building activity and expectations.

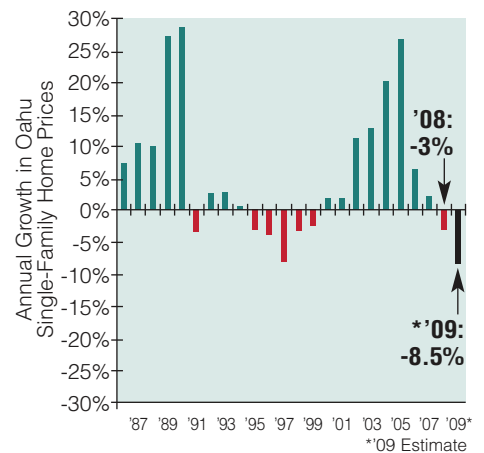
Charts 13 and 14 show real estate numbers for Oahu. With a few minor exceptions, the Neighbor Island picture has generally fared worse than Oahu (see pages 7-10) in sales and median prices, with numbers there weighted down by shrinking second-home activity. There have actually been some encouraging signs of a bottom in single-family residential sales activity on Oahu in 2009 — at least declines in activity haven't been as great as the previous year.

CHART 13 • OAHU SINGLE-FAMILY HOME SALES



Source: Honolulu Board of Realtors

CHART 14 • OAHU SINGLE-FAMILY HOME PRICES



Source: Honolulu Board of Realtors

However, the decline in median prices probably has a while to go. That decline will likely be in high single digits for 2009, followed by a smaller drop in 2010 before prices stabilize in 2011. The total decline this time won't be as great as the average nationally, and it will likely be less than that of the mid-1990s here if inventory levels and days on market remain more favorable than they were then.

At least affordability will be improving in this high-cost market, even if mortgage rates rise some.

Hawaii's Neighbor Islands Have Been Feeling Impact of Economic Downturn More than Oahu

Hawaii's Neighbor Islands have been affected by the current downturn to a significantly greater extent than Oahu. Less diversification and the greater role of tourism are major reasons.

The question everyone's asking is: How long before better times return?

For the Neighbor Islands, recovery will be gradual and will depend critically on the return of healthy tourism. And that in turn will depend on the return of better times to the Mainland economy, especially the West Coast.

Chart 1 shows how the Neighbor Islands have taken the brunt of the recession, especially since tourism is much more important to them than it is for Oahu. Declines for all islands will look a bit less draconian by year's end, because the first quarter showed the largest contraction relative to 2008.

KAUAI COUNTY

- Tourism continues to suffer on Kauai as much as — or more than — the other islands. The construction slump has slowed or halted work on several projects at Poipu and elsewhere. The real estate market has seen significant declines in both sales and prices.
- But all is not gloom and doom. Time-share visitor numbers are holding up well. A \$1 million Kauai tourism marketing effort has begun. The missile range continues to supply high-salary jobs. Federal stimulus money could help provide government construction projects. A new St. Regis Hotel has opened and Safeway will anchor a planned new shopping center to open in 2010.

Kauai Jobs Shrinking

Payroll jobs on Kauai have been shrinking at about the same rate as the other Neighbor Islands. In 2009, the island will likely see a larger contraction than in any year since Hurricane Iniki in 1992.

The Kauai unemployment rate broke into double digits early in 2009 — highest rate since the aftermath of Iniki and an astounding 7 percentage points higher than early 2008.

CHART 1 • TOURISM DECLINES, BY ISLAND

	2008	1st Half of '09
Arrivals (% Growth in Visitor Arrivals)		
Kauai	-20%	-16%
Big Island	-18%	-13%
Maui	-15%	-15%
Oahu	-11%	-10%
Spending (% Growth in Visitor Spending)		
Kauai	-15%	-16%
Big Island	-15%	-17%
Maui	-13%	-13%
Oahu	-6%	-15%

Source: State Department of Business, Economic Development & Tourism

Kauai Tourism: Time-share Helps

Kauai's tourism numbers would look a good bit worse were it not for the time-share component, which — as always — has held up better. Though time-share rentals are down, owners are still coming. Other good news is that "Dr. Beach" this year chose Kauai's Hanalei Bay as the #1 beach in the United States.

Kauai has shown initiative in devoting \$1 million of public funds to marketing the island. About half of this money will be aimed at wholesalers and on-line travel agents; other targets are the kama'aina market, military and West Coast and Canadian markets.

There are these developments in Kauai's visitor plant:

- Princeville Hotel has re-opened as a St. Regis property, Hawaii's first. A 50th anniversary celebration of the movie "South Pacific" is planned. Also at Princeville, the renovated Makai Golf Course is scheduled to re-open near year's end and Princeville Shopping Center has been refreshed, with a new tenant mix. Occupancy at Princeville Ocean Villas, the new Westin time-share development, has been running full.
- Koa Kea Hotel, formerly the Poipu Beach Hotel, opened as an upscale boutique property.

CHART 2 • KAUAI JOB GROWTH

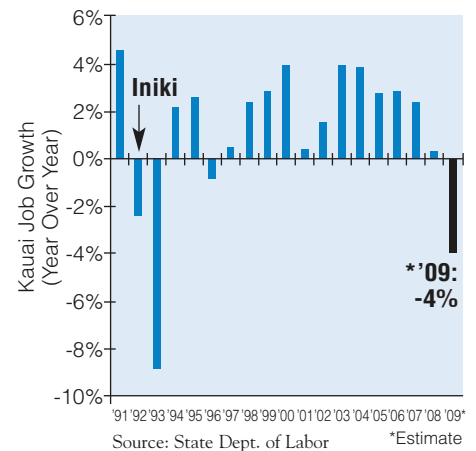
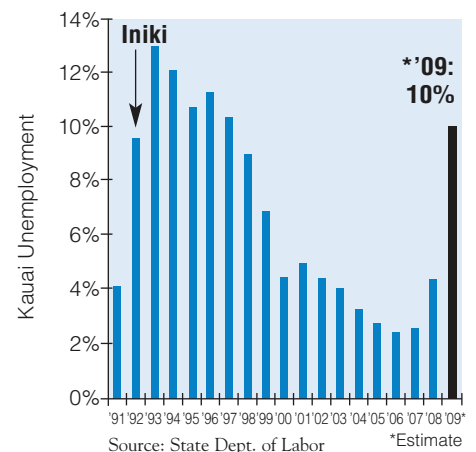


CHART 3 • KAUAI UNEMPLOYMENT



- The Kauai Marriott started a \$50 million renovation.
- Work at Kauai Lagoons and Ritz Carlton Residences ceased, another fallout of the financial turmoil.

Kauai Construction Slumping

Much of the construction in the Poipu area has either halted or slowed:

- Lots have been on the market since mid-2008 at Poipu Beach Estates, a 106-lot sub-division across from the Sheraton Kauai Resort. Seven out of 25 lots offered have been sold so far, but no construction has started.
- The construction pace has slowed and prices are down at nearby Koloa Landing, a 323-unit luxury condo project.
- Pre-leasing has begun at Koloa Marketplace, a 70,000-square-foot shopping complex, with construction slated to extend over two years.

- A soft opening has taken place at the new Kukui'ula Shopping Village, which includes a Merriman's restaurant and other well known shops. Hard leases are around 40-50%. Construction also continues on the golf course and the main clubhouse at Kukui'ula. Alexander & Baldwin has become the main investor in the project. Residential construction there in the near future will be sales-driven.
- Other projects in the Poipu area are either not proceeding or are moving forward on a very limited scale.

On the plus side for the future, Grove Farm's Lihue-Hanamaulu Master Plan Community envisions 2,500 single- and multi-family residential units combined with mixed-use commercial components.

Grove Farm also sold 11 acres across from Kilohana Plantation to Safeway in May 2009. Safeway intends to eventually buy a total of 22.8 acres there, and the Hokulei Village complex will have a 56,000-square-foot Safeway store plus a range of local and national retail tenants, and professional offices. The center could create more than 1,000 new jobs, and is now planned for completion by end of 2010.

With resort and residential construction drying up, construction firms are diversifying into other types of work including government projects.

Kauai Real Estate

Looking at the Kauai real estate market, it's easy to see why residential builders are not moving forward with projects. Through June, sales were off 30% for single-family homes and 40% for condos. Median prices also have shown weakness since last year — down 27% for single-family and 47% for condos. The number of transactions has declined so much, however, that these price data mean less than ever.

Compared to other islands, Kauai has been more affected. On balance, declines are slightly less for Maui and the Big Island, and much less for Oahu.

CHART 4 • KAUAI HOUSING MARKET

Kauai Single-Family Home Sales - Number of Sales		
2008	2009	Change
148	103	-30%
Kauai Condominium Sales - Number of Sales		
2008	2009	Change
114	60	-40%
Kauai Single-Family Home Median Price		
2008	2009	Change
\$657,500	\$479,000	-27%
Kauai Condominium Median Price		
2008	2009	Change
\$599,500	\$320,000	-47%

YTD Data through June 2009
Source: Hawaii Information Service

Missile Range a Key Force

When the economy struggles, activities not related to the economic cycle such as the Pacific Missile Range Facility are appreciated more than ever. Counting contractors as well as uniformed military and government civilians, jobs there total about 875 and are much higher paying than elsewhere on Kauai. Government and contractor payroll is about \$130 million annually.

Another value of PMRF to the economy lies in the seed it provides for high-tech on the island, which would be virtually nonexistent otherwise.

Kauai Agriculture

The agricultural sector also marches to its own drum rather than following the fluctuations in tourism and construction. Developments this year:

- Gay & Robinson decided to harvest its last sugar crop this year instead of next, to take advantage of currently high sugar prices.
- An informal blessing for the long dormant Tropical Fruit Disinfestation Facility was held in June.
- The County-funded cattle handling facility at Kalepa has shipped 4,500 head. Most cattle shippers using this facility are smaller ones.
- The Kilauea Agricultural Park Master Plan, for a 75-acre County owned property, has been completed and is under review.

The seed corn research industry has become a major stabilizing influence on the West side. Four major research entities have been present on Kauai for some time: Pioneer Hybrid (a DuPont subsidiary), Syngenta Seeds, BASF Plant Science, and Monsanto. Over the past year, Monsanto moved its nursery operation to Maui, but a fifth one is now relocating to Kauai from Molokai — Mycogen Seeds.

MAUI COUNTY

- Maui has shown declines in visitor arrivals and spending in 2009. Retailing is seeing lower spending from both residents and value-oriented tourists. The real estate market has had declines in sales and prices. And the long drought threatens the viability of sugar.
- On the plus side: Maui Land and Pineapple Co. has completed work at the Ritz Carlton Club and Residences at Kapalua. An 1,100-home project was just announced for Ma'alaea. Some hotel renovations planned at Ka'anapali may help the construction industry if they get through the approval process. Community college enrollment is soaring as the recession motivates more people to get more education.

In 2008, Maui fared a little better than other Neighbor Islands in both arrivals and spending, but 2009 has brought bigger declines.

Perhaps the biggest hurdle for Maui in the current environment is the image it has tried hard to cultivate — an upscale destination for affluent travelers, not a reputation you want in this new world of frugality. Visitors attracted to Maui by lower airfares and hotel room rates are not likely to be big spenders when they get here. And after all, spending is the bottom line.

Maui's Job Market Struggling

As Chart 5 shows, payroll jobs on Maui have been shrinking at about the same rate as the other Neighbor Islands; 2009 will likely see a 4% contraction.

(continued on page 8)

Maui County (continued from page 7)

The county's unemployment rate (Chart 6) could end 2009 at about 10% — double the 2008 rate.

Maui Retailing Trends

Maui retailing has felt the downturn on both the local and tourist fronts. At Maui's biggest mall, Queen Ka'ahumanu Center, only 10-15% of sales are related to tourism, but sales are off well into the double digits. Some categories — like food, shoes, and some accessories — have fared better than others, such as jewelry and certain categories of services.

Visitors are shopping for value. Foot traffic is higher if time-share units are nearby, because occupancies are higher there than in hotels. But one shopping bag instead of several is more the norm, and often that bag is from an ABC Store, not a higher-end retailer.

Maui Construction Industry

The ongoing slowdown in resort and residential construction has made “diversification” the key word for Maui builders. Public works projects, hotel remodeling, and subcontracting for others are among the targets of that effort.

The slowdown would have occurred anyway, but a further drag on residential construction comes from Maui County's “show me the water” ordinance, which requires developers to identify sources of water for new houses before the County will grant them a meter. Another drag is the workforce housing ordinance passed in 2006, which raised the affordable housing component for development.

Recently in Maui construction:

- Maui Land & Pineapple Co. completed its Ritz Carlton Club and Residences at Kapalua, a mix of fractional and whole ownership condos.
- Financing problems caused Dowling Co. to scale down plans to build luxury condos in Makena. Instead, single-family lots are being offered.
- Spencer Homes proposes to build 1,100 single-family homes, mostly in the affordable category. The project, in the Ma'alaea area, is called Ohana Kai Village.

CHART 5 • MAUI JOB GROWTH

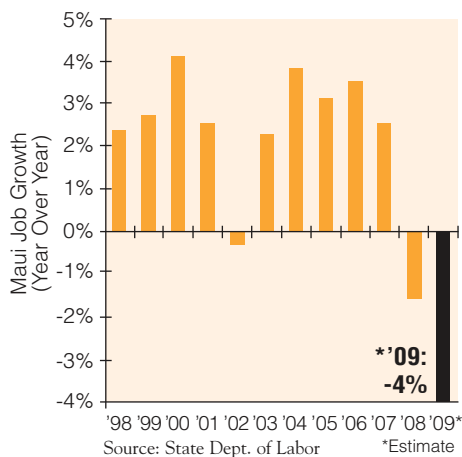
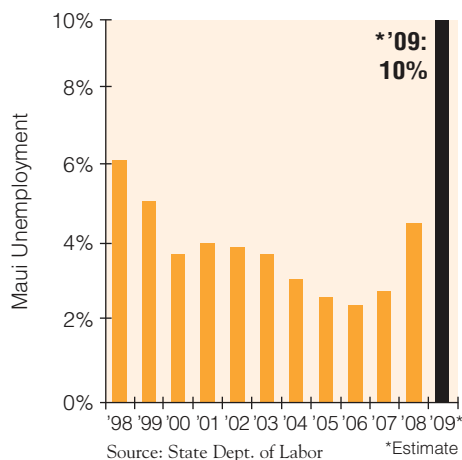


CHART 6 • MAUI UNEMPLOYMENT



- A number of hotel extension and improvement projects are reportedly ready to start in Ka'anapali, but are now tied up in the approval process.
- Ongoing commercial developments include a professional row at Maui Lani Village Center and A&B's planned 179-acre Business Park II in the Dairy Road area. Currently planned commercial development on Maui should satisfy the demand for commercial space for a number of years.
- Alexander & Baldwin's Kahului Town Center will proceed in four quadrants, the first commercial and the others more mixed use. Construction may begin before year's end at Aina o Kane condos in the same area. Other A&B residential projects include the Bluffs at Wailea, a 12-lot subdivision, the nine-lot Ridge at Wailea, and the 170-lot Halimaile subdivision.

CHART 7 • MAUI BUILDING PERMITS

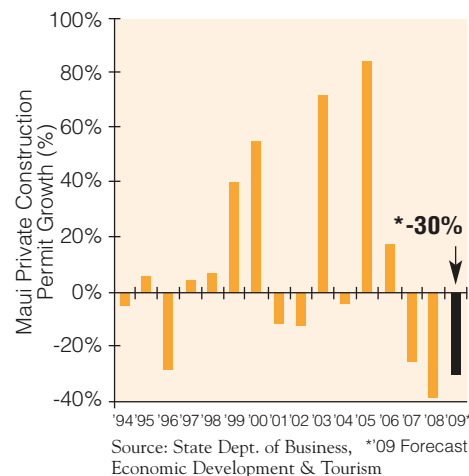


CHART 8 • MAUI HOUSING MARKET

Maui Single-Family Home Sales - Number of Sales			
2008	2009	Change	
479	285	-41%	
Maui Condominium Sales - Number of Sales			
2008	2009	Change	
510	275	-46%	
Maui Single-Family Home Median Price			
2008	2009	Change	
\$592,696	\$510,000	-14%	
Maui Condominium Median Price			
2008	2009	Change	
\$575,000	\$420,000	-27%	

YTD Data through June 2009
Source: Realtors Association of Maui

Maui Real Estate Picture

Trends in Maui real estate (Chart 8) continue to follow the rest of the state, with declines in both sales and median prices. So far in 2009, there have been big drops in the number of sales, but price declines have not been as great as for other Neighbor Islands.

Because real estate is an important sector, fewer sales mean less economic activity in general. Real estate activity is closely related to construction and consumer confidence.

Higher Education on Maui

Recession can do strange things in the education industry. More unemployed or underemployed individuals can translate into higher enrollments if they decide to use the extra time to go back to school.

Enrollments are up throughout the UH Community College system, but nowhere more than at Maui Community College. Spring 2009 enrollment was up 21% over the previous spring, and fall 2009 enrollment will be up over 25% from the previous fall, bringing the student body to over 4,000.

The college's new science building is expected to start construction by the end of 2009, and grants have been strong with \$9.8 million in the last fiscal year. MCC has had the strongest record in grants throughout the community college system over the years.

Maui Sugar Troubles Grow

When Gay & Robinson on Kauai harvests its last crop of commodity sugar in 2010, HC&S on Maui will be the state's lone remaining sugar operation. Increasingly, however, threats to its survival are becoming more real.

Chart 9 shows total sugar production over the years. Total tons of sugar harvested fell to just over 145,000 in 2008. Chart 10 shows yield in tons of sugar per acre, which fell to 8.6 in 2008. Even though specialty sugar products have been a success for HC&S, the plantation cannot make money at these levels; the company estimates that yields of at least 12 tons of sugar per acre are necessary for it to remain viable.

The reason for falling production is the long-running drought. HC&S use of surface water from East and West Maui also has been challenged by lawsuits from environmental groups. HC&S, one of the island's largest employers, has been able to survive as other plantations closed mainly because of its size. As its size shrinks, economies of scale evaporate.

If its 35,000 acres — virtually all of the "valley" in the Valley Isle — were to go fallow, the land would likely remain so because no tropical or temperate climate crop, or combination of them, can possibly use that much acreage.

The green fields of Central Maui's plain would revert to a dry state, bringing pressure to urbanize the former sugar land. Maui depends upon an attractive environment to nurture tourism. Those who remember the green hillsides of

CHART 9 • HC&S SUGAR PRODUCTION

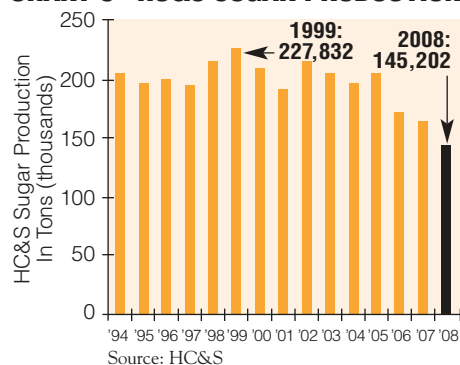
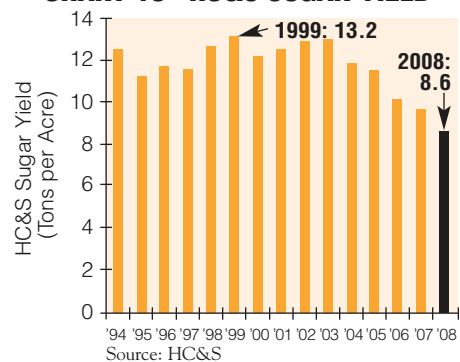


CHART 10 • HC&S SUGAR YIELD



West Maui before sugar's exit, compared with the wind-swept red dirt of today, realize that sugar made the scene much more attractive to the visitor.

HAWAII COUNTY

If tourism, construction, and real estate are all struggling simultaneously — as they are now — the recessionary picture is similar across all of Hawaii's Neighbor Islands. However, the Big Island is somewhat different than Maui and Kauai now. It's a little more diversified than they are, and — as always — there are big differences in the East and West sides of Hawaii County.

In times like these, the disparity between the two sides can be good news. Hawaii County's economic cycle is determined by what happens on the West side because that's where the visitor industry is centered, and most construction also. The West Hawaii economy is thus more volatile, while East Hawaii acts as an economic stabilizer. That may not seem so good in boom times, but it looks a lot better in times like the present.

CHART 11 • HAWAII COUNTY JOB GROWTH

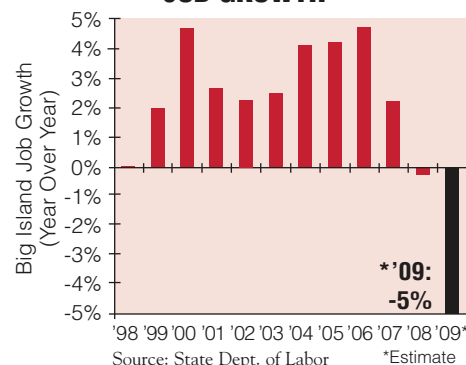
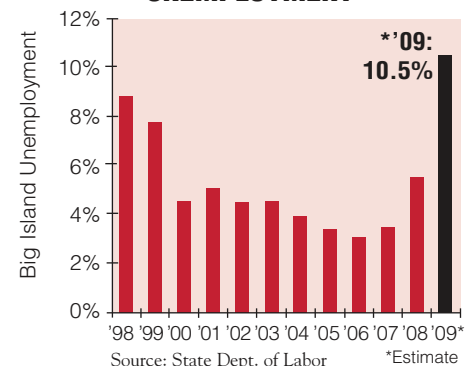


CHART 12 • HAWAII COUNTY UNEMPLOYMENT



One brighter side for the Big Island is that airlift has been holding up. Alaska Airlines has been coming since 2008, and another Oakland to Kona Alaska flight will begin soon.

The East side benefits less from tourism, but in times of contraction in the visitor industry, it also feels less pain than the West side. Hilo could eventually grow its tourism industry. After all, an increasingly active volcano is quite an attraction, among other things. But to do so it needs two missing assets: a first-rate hotel and dedicated airline commitment.

Hawaii County Job Picture

Hawaii County payroll jobs (Chart 11) have been shrinking at about the same rate as the other Neighbor Islands, and 2009 as a whole will likely see about a 5% contraction. The unemployment rate (Chart 12) for 2009 as a whole could finish above 10%, almost double 2008.

(continued on page 10)

Hawaii County (continued from page 9)

Hawaii County Construction

Big Island construction peaked in mid-2006, about a year before the rest of the state, and is entering its fourth year of contraction. Industry sources see a bottoming out about mid-2010, with a very gradual recovery.

There is only one housing project underway on the Big Island now, an affordable project in Kona. Observers foresee the resort condo market to be last to show a recovery.

Hawaii County is on the list for a \$35 million highway project in Kona, to be funded by Federal stimulus money, and hopes are high that project will be awarded.

Oversupply in commercial development is a bigger factor in the Hawaii County market than on other islands. The East side is not nearly as overbuilt as the West side, however.

Hawaii County Real Estate

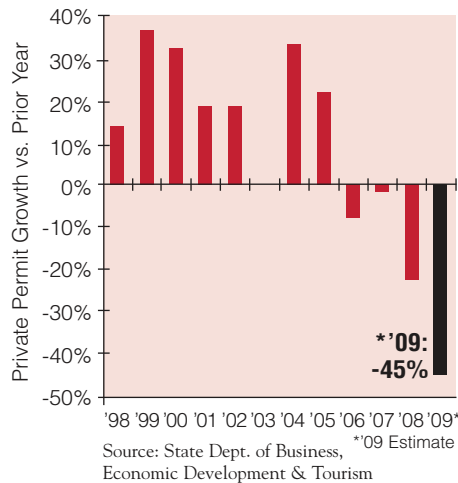
The soft Big Island real estate market (Chart 14) has been following trends elsewhere in the state. Both sales and prices have been falling in 2009; sales figures are more telling, because median prices mean much less as the sample size shrinks. These declines are a function of low buyer confidence, tighter financing, and expectations that prices may fall further.

Appraisers report price declines of about 1% a month, and the market is back to 2004 levels. Even though it is hard to quantify, increased vog on the Kona side is also said to be influencing sales. Nonetheless, Realtors do report that there are a substantial number of people at least looking.

East Hawaii, where there has been less vacation home building, is more stable than the West side. Even though price declines have been about the same on both sides, the East side is expected to bottom out quicker.

Falling property values will have an impact on County property tax income.

CHART 13 • HAWAII COUNTY CONSTRUCTION PERMIT GROWTH



Astronomy: Good TMT News

The Big Island got welcome news with the announcement that Mauna Kea was chosen over Chile as the site for the Thirty Meter Telescope (TMT). This will be the world's largest scope — about three times larger than current telescopes, also atop Mauna Kea. Ideal atmospheric conditions, low temperatures and humidity make Mauna Kea the best site for astronomical observation.

TMT will pump an estimated \$1.2 billion into the economy over nine years, providing 300 construction jobs and 140 full-time permanent jobs. Astronomy is a clean industry that provides higher income jobs and diversification, so it's one to be nurtured.

As usual, there have been cultural and environmental objections, but local support for TMT has been more united than for previous observatory proposals.

University of Hawaii at Hilo

The Hilo campus is a big contributor to East Side economic stability and several things are going on now there that are especially welcome.

- Widening of the Kawili Street entry to UHH, a \$4.6 million project that includes student access to the planned U.S. – China Center.
- Sites have been selected for a Hawaiian Language College building and a consolidated Student Services Building.

CHART 14 • HAWAII COUNTY HOUSING MARKET

Big Isle Single-Family Home Sales - Number of Sales		
2008	2009	Change
628	528	-16%
Big Isle Condominium Sales - Number of Sales		
2008	2009	Change
213	135	-37%
Big Isle Single-Family Home Median Price		
2008	2009	Change
\$379,053	\$281,050	-26%
Big Isle Condominium Median Price		
2008	2009	Change
\$450,000	\$295,000	-34%

YTD Data through June 2009
Source: Hawaii Information Service

- College of Pharmacy modules are now being constructed in the University Park of Science and Technology. A \$5.5 million permanent College of Pharmacy Building is planned to start soon also.
- A \$25 million Science and Technology Building is also under construction.

Big Island Agriculture

The economic slowdown and rising costs of fuel, fertilizer, and transportation have taken their toll on many crops. But there are some bright spots.

- Rainfall this winter kept the coffee belt green. Prices remained constant for a while, but then fell toward the end of the season. If good weather continues, a fairly large crop is expected in the 2009-2010 season. Prices next season may start lower, but could rise as the season continues.
- Favorable weather also provided a good macadamia nut crop, but several processors took limited amounts from independent suppliers. Some farmers phased out of the crop.
- Weaker beef demand and higher shipping costs have squeezed rancher profits. More Big Island cattle are being finished locally.
- The weak economy and slower construction have dampened exported foliage sales.

Global Economy Should Improve in 2010 and 2011

By James F. Smith, Ph.D.

It's a hard cruel world out there with much economic turmoil and concern. Problems associated with valuing mortgage-backed securities based on U.S. subprime mortgages cascaded across financial institutions and markets around the world in 2007 and resulted in an ongoing panic that began on August 9. A month later the panic led to a run on the fifth largest mortgage lending institution in the United Kingdom, Northern Rock, the first bank run in the U.K. since 1866.

This freezing of financial markets has recurred many times throughout history. A comprehensive documentation that is also a most delightful and interesting book to read is *Manias, Panics, and Crashes: A History of Financial Crises (5th Edition)* by Charles P. Kindleberger and Robert Aliber (ISBN 978-0-471-46714-4). *The Wall Street Journal* had a lead editorial on September 16, 2008 ("Surviving the Panic") referring to the usefulness of this book in understanding the current situation. You'll feel better if you get a copy of the book and peruse it carefully.

“Freezing of financial markets has recurred many times throughout history.”

The International Monetary Fund (IMF) in its October World Economic Outlook expects world output to shrink by 1.1 percent in 2009 after having grown 3.0 percent in 2008. That makes 2009 the worst year for the global economy since the end of World War II. They expect global growth of 3.1 percent in 2010 and for growth to average 4.4 percent a year in the 2011-2014 period.

ECONOMIC FORECASTS

Real GDP growth rate in:	2010	2011
United States	+3.2%	+4.0%
European Union	+0.5%	+2.0%

Sources: U.S. forecast by James F. Smith, Ph.D.; European Union forecast by International Monetary Fund

What no one seems to remember is that the five years 2003 through 2007 were quite good for the U.S. economy. They were even better for the world as those were the best five consecutive years for global economic growth ever recorded.

Not coincidentally, the number of people lifted out of poverty (defined globally as having a cash income of less than \$1.00 per day) was in the hundreds of millions around the world. That's also a five-year record.

The U.S. officially entered recession in December 2007 according to the National Bureau of Economic Research. Not coincidentally, that was also the peak month for nonfarm payroll jobs at 138,152,000 such jobs. According to the Bureau of Labor Statistics (BLS) report of October 2, that number was 130,947,000 on a seasonally adjusted basis in September. That's a loss of 7,205,000 such jobs since the recession began.

Total employment peaked in November 2007 at 146,665,000 people. That had fallen to 138,864,000 people in September. That's a decline of 7,701,000 in the number of people employed. There were 15,142,000 unemployed people looking for work in September. That produced an unemployment rate of 9.8 percent, double the rate at the start of the recession. It's the highest since the 10.1 percent rate in June 1983.

Real GDP in the U.S. rose on a year-over-year basis by only 0.4

percent in 2008. That was the worst performance since the 1.1 percent of 2001, a year with eight months of recession in it.

For 2009, the U.S. economy should shrink by 2.3 percent, despite having good growth in the last half of the year. That's worse than the 1.9 percent drop in 1982 and is only exceeded in the post-World War II era by the 10.9 percent collapse in 1946 as we were making the transition to a peacetime economy.

“For 2009, the U.S. economy should shrink by 2.3%, despite good growth in the last half of the year.”

My forecast is for 3.2 percent real GDP growth for the U.S. in 2010 and 4.0 percent in 2011 on a year-over-year basis. These are both above consensus, but quite consistent with past experience after recessions end.

Both the European Union¹ (EU) and the Euro Zone² are hurting worse than the U.S. The IMF projects that real GDP in the EU will fall 4.2 percent this year after 1.0 percent growth in 2008. They expect only a slight rebound to 0.5 percent for 2010 and only around 2.0 percent in 2011.

For the Euro Zone, they have a projected drop in real GDP of 4.2 percent this year and only 0.3 percent growth in 2010. They don't even get up to 2.0 percent for 2011.

Japan is the world's second largest economy. It is in a deep recession and indeed has posted little economic growth since the collapse of its “bubble economy” in 1990. It has very little room for any fiscal stimulus

(continued on page 12)

¹ Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Spain, Sweden, and the United Kingdom

² Austria, Belgium, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain

Global Economy (continued from page 11)

because its federal debt-to-GDP ratio is about 200 percent. Thus its debt service, even at its low interest rates (1.26 percent on 10-year government bonds on October 2) means that the government must spend about 3.2 percent of nominal GDP on paying interest to bond holders. As the Japanese economy has not grown by more than 3.2 percent in nominal terms in 20 years, that means the debt ratio will just keep growing forever until their economy collapses unless they start paying down debt soon.

“Japan has very little room for any fiscal stimulus because its federal debt-to-GDP ratio is about 200%.”

Sufficient Stimulus Always Works

Reading *Manias, Panics, and Crashes* will convince you that whenever massive resources are thrown at ending financial panics, three things have always happened in every country that has done that:

1. **The panic stops.** Since this one has been going on since August 9, 2007—which makes it the longest panic since the Great Depression of August 1929 to March 1933—that will be really good news when it happens. We’ll know that day has arrived when the spread between the 3-month U.S. dollar LIBOR (London Inter-bank Offered Rate) returns to its normal range within 3 to 7 basis points of the 3-month U.S. Treasury bill yield.

On October 2, 2009, LIBOR was 0.28 percent while the 3-month Treasury yield was 0.10 percent, a gap of 18 basis points. That’s a big improvement over the 110-basis point spread of March 9 or the 43-basis point gap in June, but we still have a small distance to go to be sure the panic has ended.

2. **Stock markets boom.** All that liquidity has to go some place and the best returns on investments are in stocks over the long run. This should occur in 2009, although that seemed far off when the equity markets hit 12-year lows on March 9. Since then, however, we have seen rallies strong enough to put most market indices above year-end 2008 levels.
3. **With a lag of only a few months, the real economy (the parts that produce goods and services) soars.** The huge growth in real GDP from the end of 1982 through the second quarter of 1984 shows this (real GDP grew at seasonally adjusted annual rates of 5.1, 9.3, 8.1, 8.5, 8.0 and 7.1 percent, respectively, over those six quarters). Real GDP grew by 7.2 percent in 1984 (after a 4.5 percent increase in 1983), the best year since the 7.7 percent of 1951 and still the third fastest growth rate since the 16.4 percent of 1943. The 8.7 percent real GDP growth rate in 1950 is the post-1943 high.

“Whenever massive resources are thrown at ending financial panics, the panic stops, stock markets boom and with a lag of only a few months, the real economy soars.”

After That, the FOMC’s Actions Are Crucial

The late William McChesney Martin, the longest serving Chairman of the Federal Reserve, once famously said that the main job of the central bank was “to remove the punch bowl just when the party is going good.” That is a most apt description of the challenge.

“If the Fed moves quickly to remove the excess liquidity it has created, a long growth period with low inflation is likely to follow.”

If the Federal Open Market Committee (FOMC) moves quickly to remove the excess liquidity it has created since 2007, then a long growth period with low inflation is likely to follow. The FOMC did this very successfully after the July 1981 to November 1982, the July 1990 to March 1991 and the March to November 2001 recessions. That’s why the period since the 1981-1982 recession is known as the “Great Moderation.” It’s been a period of relatively stable growth with low inflation. Real GDP growth was positive in 97 of the 104 quarters (26 years) through 2008. That’s a ratio of growing-to-shrinking quarters that is unprecedented in U.S. history.

When the FOMC has been too slow to sop up the excess liquidity, then inflation becomes a problem and another recession is needed to bring it under control. This is what happened after the December 1969 to November 1970, the November 1973 to March 1975 and the January to July 1980 recessions.