

Executive Summary

Kenai Peninsula Borough (KPB) industry diversity proved to be an asset during first quarter 2005 as some sectors experienced double digit growth, others double-digit decline. As the most diverse economy in Alaska, the KPB economic system gained strength from its diversity as industry sectors expanded or contracted. The KPB tourism outlook for 2005 indicates continued growth. The commercial fishing industry anticipates another strong year with the sockeye return forecast to increase 200,000 over the 2004 strong run. Demand for the Kenai Wild sockeye is increasing, further improving the outlook. Oil & gas industry participants continue to explore and develop within the KPB. Support industries will benefit from projects in the KPB as well as from projects such as the Pebble Mine located in the Lake and Peninsula Borough west of the Kenai Peninsula Borough.

First quarter sales expanded as gross sales increased 2.3% from \$360,872,443 during first quarter 2004 to \$369,092,946 during 2005, an \$8,220,503 increase. Taxable sales increased 0.7% to \$140,836,157 from \$139,896,835, a \$939,322 increase.

Construction activity appears strong, even in the face of a substantial decrease in values. First quarter values during 2004 set a new record high, easily exceeding the 1995 high, so the decline is not unexpected. Values for the period decreased 61.6% to \$6,475,255 but produced the fifth highest value on record. The quarterly permit value was \$16,851,943 during 2004 while the 2003 value was \$5,255,313. While total value decreased, volume increased 56.8% from 37 permits a year ago to 58 for first quarter 2005. Forty-six permits were issued during first quarter 2003.

Each of the four employment indicators showed improvement, month for month, when compared to January, February and March of 2004. The labor force increased by 290, 157 and 182 persons over the same months. Unemployment was down 266, 206, and 448 persons over the three-month period. The resultant unemployment rates were down 1.4, 1.0 and 2.2 points during January, February and March 2005, respectively. Finally, employment increased by 556, 363 and 630 persons for the three respective months. The four factors combine to indicate increasing strength during March.

Issues in the oil & gas industry are many and varied as known natural gas reserves decrease. At the end of 2004, the reserves estimate in the Cook Inlet Basin marked the first increase in several years as exploration resulted in improved reserves, more than matching product used during 2004. Experts feel the Outer Continental

Shelf region in the Cook Inlet is unexplored, resulting in Alaska offering exploration incentives for the area. The increased use of natural gas during the winter months has raised the issue of gas storage from summer production, which could be used if needed during the winter months, when demand is greatest. There have been some discussions regarding development of the Kenai National Wildlife Refuge. Other issues include extension of oil platform lives in the Cook Inlet Basin, making them economically viable while recovering the more difficult oil reserves. Two gas exploration wells have been successful, located on the west side of Cook Inlet.

Presently, the largest concern in the oil & gas industry is the announced closure of Agrium's fertilizer plant in Nikiski unless economically viable supplies of gas are found. Although the company does not plan to sell the plant, they project closure near the end of 2005. As a result, the Regulatory Commission of Alaska is investigating the Cook Inlet Gas Gathering System, to determine if it should be a regulated part of the infrastructure. Agrium recently requested proposals for gas supplies, indicating they were willing to increase the price they would pay for gas to remain operational. The governor appointed a task force to study the situation.

Population data for 2004 indicates a 0.8% decrease across the KPB for 2004, and each of the incorporated cities experienced a decline. The Homer population declined 9.1%, Kachemak City was down 0.6%, Kenai declined 4.4%, Seldovia dropped 5.7%, Seward decreased 7.5%, and finally, Soldotna's population dropped 5.6%. Perhaps this trend has reversed because the labor force increased each of the first three months of 2005 over 2004, and employment has done the same.

SALES

Initial data for first quarter 2005 indicate gross sales of \$369,092,946, 2.3% more than the \$360,872,443 in sales during 2004, a gain of \$8,220,503. Taxable sales increased 0.7% from \$139,896,835 during 2004 to \$140,836,157 during the most recent quarter, with five of ten sectors with increasing sales. The increase in taxable sales for the quarter was \$939,322.

It must be noted that, effective April 2004, a change in sales reporting options became effective. Businesses that have less than \$6,000 in taxable sales annually, and meeting other reporting requirements, may opt to report all sales annually during fourth quarter, rather than quarterly. This skews quarterly sales data, with fewer sales reported during first, second and third quarter, but increased sales

reported during fourth quarter when sales for the year will be reported. The effect of this action is particularly strong in the manufacturing sector, where sale of value-added products in both commercial fishing and oil & gas are generally classified as non-taxable as they enter the distribution system. Sale of wholesale goods are also skewed by the action. Our sales tax system is intended to tax only the final sale, which generally occurs in retail sales to the consumer.

Quarterly Sales

Gross by Industry. In spite of the 65.1% decline in reported gross manufacturing sales, total gross sales increased 2.3%, increasing from \$360,872,443 to \$369,092,946 from first quarter 2004 to first quarter 2005. Two other industries marked declines in gross sales: Finance, Insurance and Real Estate (FIRE) sales declined 15.3% from \$13,304,735 to \$11,269,988 and sale of wholesale goods decreased 12.2% from \$41,782,771 to \$36,667,868.

Mining sales increased 0.1% to \$39,831,609 while service sector sales increased 1.3% or \$549,399 to \$43,629,834. The 1.8% expansion in retail sales provided \$129,130,943 in sales, a \$2,299,039 gain. Agriculture, Forestry and Fishing (AFF) sales of \$2,951,383 were 26.1% greater than one year ago, increasing \$610,457. Construction sales reached \$38,194,463, gaining 33.3%. Finally, Transportation, Communication and Public Utilities (TCPU) sales grew by 49.6% to \$58,281,566. Government sales increased 11.4% but the \$15,214 in sales is not of consequence in the \$370 million total picture. (See page 15 for detail.)

Taxable by Industry. Taxable sales increased 0.7% for the quarter, a gain of \$939,322 to reach \$140,836,157. The 1.1% gain in retail sales, equivalent to \$875,760, coupled with gains in other sectors, was strong enough to overcome a 13.4% decline in reported manufacturing sales – down \$202,180, a 13.0% decrease in reported wholesale goods sales – down \$766,000, and an 8.1% drop in FIRE sales – down \$394,737. The reporting deadline may be a reflection of sales that were not reported during first quarter but will be reported during fourth quarter as a result of the change in taxable sales reporting options.

In addition to retail sales, TCPU sales increased 9.7% to \$23,066,441; AFF sales increased 4.6% to \$930,189 and mining sales rose 3.8% to \$1,087,830. Construction sales decreased from \$2,217,009 to \$2,016,842, sales in wholesale goods dropped 13% to \$5,126,430 and manufacturing sales totaled \$1,309,950, down from \$1,512,130 during 2004. Government sales increased 11.9% to \$15,214, an inconsequential amount. (See page 16 for detail.)

Gross by Area. The six reporting areas were evenly split with three areas experiencing gains, three reporting sales declines. Overall, gross sales increased 2.3%. Kenai led the charge with sales increasing 22.1% to \$74,587,278 with strong TCPU sales. Seward sales gained 13.8% to reach \$24,087,155 due to construction sales. Lastly, Homer gross sales of \$49,752,632 marked a 3.3% gain.

Seldovia businesses reported declining sales, down 12.1%, to \$1,235,684, largely as a result of a decrease in construction sales, which were exceptionally strong a year ago. Soldotna sales contracted 7.9%, to \$64,359,653, with strength in construction but weakness in wholesale goods. Lastly, sales in the unincorporated area of the KPB decreased 2.6% to \$155,070,544. (See detail on page 17.)

Taxable by Area. Taxable sales are not impacted so heavily by the change in reporting options and increased 0.7% for the quarter. Seward sales increased 4.7% to \$9,943,549; Soldotna sales gained 1.8% to reach \$38,071,634; and, with sales of \$39,575,966, the KPB unincorporated area gained 1.3%.

Homer taxable sales decreased 1.6% to \$23,444,569 while Kenai sales dropped 1.0% to \$29,236,679. Finally, sales in Seldovia decreased 0.5% to total \$563,760. (See detail on page 18.)

Annual Sales

KPB 2004 annual gross sales of \$2,222,004,286 were 15.7% above those of 2003 as seven sectors reported improved sales and three had declining sales. Total 2003 sales of \$1,920,035,537 were 2.2% greater than 2002 sales of \$1,877,961,633. These, in turn, were 4.6% less than 2001 sales of \$1,967,506,986. Each area had increased gross sales from 2003 to 2004.

Taxable sales increased 6.4% from 2003 to 2004 with sales reaching \$780,093,713, following a 1.2% increase from 2002 to the 2003 level of \$732,852,339. The 2.6% gain from 2001 to 2002 resulted in sales of \$724,232,961. All areas had increased taxable sales from 2003 to 2004.

Gross by Industry. Dynamics within the various industry sectors are notable as comparisons are made between 2003 and 2004 sales. Only two sectors had single digit changes. All the rest, gains or losses, were double-digit percentage changes, the largest being 88.5% in the construction industry where sales grew from

\$194,212,922 to \$366,072,552. Next, with a 55.2% increase, mining sales increased from \$106,561,739 to \$165,354,111. The AFF sector gained 25.5%, with sales of \$27,631,235, up from \$22,009,310 during 2003. TCPU sales of \$181,051,679 marked a 14.3% gain, up from \$158,372,166. FIRE sales increased 11.8% to reach \$64,843,380. The second largest sector, services, gained 11.1%, or \$30,756,093, to total \$308,996,885, while the largest sector, retail sales, increased sales by 8.6% to \$699,834,751, a gain of \$55,139,289.

Manufacturing sales of \$170,708,311 decreased 14.4% while construction sales decreased 8.1% to \$237,476,277, perhaps a factor of the change in reporting options. The inconsequential \$35,105 in government sales marked a 16.4% decrease. (See detail on page 19.)

Taxable by Industry. All sectors except government marked growth for the 2004 calendar year, resulting in a 6.4% borough-wide taxable sales increase. Mining sales grew 12.6% to \$5,502,300 joined by AFF sales in double-digit gains, rising 10.3% to \$5,525,243. Retail sales increased 7.5% while services increased 7.0% with sales of \$461,616,411 and \$154,902,802, respectively. Retail and service sales accounted for 79.1% of all taxable sales for the year. Manufacturing sales grew 6.7% to reach \$9,859,796 and sale of wholesale goods increased 6.1%, for \$25,769,380 in sales. The 1.6% gain in TCPU sales brought sector sales to \$82,707,524. Percentagewise, FIRE and construction sales rose the least, 0.6% and 0.1%, with \$22,880,826 and \$11,294,391 in sales, respectively.

Government's 16.5% sales drop to \$35,040 is inconsequential. (Detail on page 20)

Gross by Area. The Kenai 65.6% sales expansion was a result of TCPU sales, which increased 212.9%, helping Kenai sales total \$469,300,234 for the year. Seldovia sales of \$8,325,201 were 14.7% above one year ago. Sales in the unincorporated area grew 8.5%, to \$933,477,858 while Soldotna sales of \$361,104,164 were 6.9% greater than one year ago. Seward, with \$166,135,648 in sales, marked a 5.8% gain while Homer sales increased 3.5% to reach \$283,661,181. (See detail on page 21.)

Taxable by Area. Kenai taxable sales increased 14.3%. leading the way to a borough-wide 6.4% increase during 2004. Total KPB sales reached \$780,093,713 as Kenai sales totaled \$138,627,446 for the year. Homer sales increased 6.4% to \$140,057,562. Soldotna sales gained 4.9% to total \$200,050,269 while Seward saw a 4.7% increase with sales of \$79,929,511. Seldovia sales marked a 0.1% increase to total \$3,381,682. (See detail on page 22.)

CONSTRUCTION PERMITTING

Quarterly Permitting

Fifty-eight construction permits were issued in KPB cities during first quarter 2005, a 56.8% increase over first quarter 2004 when 37 permits were issued. Total permit value declined 61.6% to \$6,475,255. The decline is not of concern because total value is fifth highest since 1986 and 2004 permit values were exceptionally high. The record year, 1995, was a result of the Seward SeaLife Center permit. Data in this section does not include construction activity outside incorporated cities of Homer, Kenai, Seldovia, Seward and Soldotna because the KPB does not require building permits.

By Area, Value. Homer permit values decreased 16.4% but provided 48% of KPB first quarter total permit values, \$6,475,255. Homer permits totaled \$3,105,900. Seward permitting provided 23.3% of quarterly value, issuing permits totaling \$1,507,300. Soldotna's total permit value, \$1,421,555, was 22% of the borough-wide total. Kenai issued permits valued at \$425,500 and added 6.6% to the total. Seldovia issued a \$15,000 permit during first quarter of 2004. (See detail on page 28.)

By Area, Volume. All reporting areas experienced a first quarter increase in permitting activity as 58 permits were issued. Homer increased from 16 to 18 permits; Soldotna gained 77.8%, moving from nine to 16 permits; Seward increased from seven permits to 13, an 85.7% increase while Kenai reported a 150% increase, from four permits during 2004 to ten permits this year. Seldovia issued one permit, as it did first quarter 2004. (See detail on page 29.)

By Type, Value. New residential permit values increased 0.4% to total \$3,470,356 during first quarter 2005 and provided 53.6% of the total. Commercial alterations followed with 32.1% of the total, \$2,076,969. New commercial permit values decreased from \$12,880,026 to \$509,000, adding 7.9% of the total. Residential alteration/addition permit values of \$418,930, increased 60.2% over 2004. (See detail on page 30)

By Type, Volume. Distribution of permitting during first quarter 2005 was fairly well divided as 19 permits were issued for commercial alteration projects, 18 for new residential projects, and fifteen for residential alteration. Each of these

marked an increase over 2004. Only new commercial permitting decreased, as six permits were issued. (See detail on page 31.)

Annual Construction

Construction permit values during 2004 set a new record high, easily surpassing the previous high, 1995, when the Seward SeaLife Center was permitted. Year 2004 will now set the standard, as permitted values totaled \$84,041,457, overcoming the previous annual high, \$61,670,382. Projects included expansion of Central Peninsula General Hospital, expansion of the Fred Meyer store and the new Trustworthy Hardware store, all located in Soldotna.

There were 312 permits issued during 2004, 7.1% fewer than the 336 issued during 2003 and the 351 issued during 2002, but third highest on record. Homer issued the greatest number of permits, and 34.6% of the KPB total.

By Area, Value. Soldotna's issuance accounted for 44.4% of the total, with values reaching \$37,296,926. Homer followed closely with \$24,070,631 in permit value and 28.6% of the total. Seward issued \$17,711,150 in construction permits for the year, 21.1% of the KPB total. Kenai added another \$4,786,550 in permits and 5.7% of the total while Seldovia provided the last \$176,200. (See detail on page 32.)

By Area, Volume. During 2004 Homer issued 108 of the 312 permits, providing 34.6% of the KPB total. Kenai issued 79 permits while Soldotna issued 67, for 25.3% and 21.5% of the total, respectively. Seward issued 54 permits, 17.3% of the total and Seldovia's four permits completed the count. Homer issued 25.6% more permits than during 2003 and Seward's count increased by 8.0%. Areas with declining permit activity include Kenai, down 30.7%, Seldovia was down 66.7% and Soldotna issued 9.5% fewer than one year ago. (See detail on page 33.)

By Type, Value. New commercial projects provided 66.7% of permit activity, \$56,079,343 as new residential permits provided 19% of the total, \$15,935,344. Commercial alteration/addition permit values totaled \$9,146,486 or 10.9% of the total. Finally, residential alteration/addition permits added \$2,880,284 for 3.4% of the KPB total. New residential permit values were 1.3% above 2003 while residential alteration total values increased 26.3%. New commercial values increased 254.5% while the residential alteration/addition total value was down 6.4%. (See detail on page 34.)

By Type, Volume. With 312 permits issued, residential alteration permitting increased from 94 permits during 2003 to 96 during 2004. New commercial permitting was stable at 42 permits each year. New residential permit activity for 2003 decreased 9.6% from 104 to 94 permits. Eighty commercial alteration/addition permits were issued, down from 96 during 2003, down 16.8%. There were 336 permits issued during 2003. (See detail on page 35.)

EMPLOYMENT

KPB's January 2005 labor force had 21,856 persons, decreasing to 21,841 potential employees during February but rebounding to 21,980 during March. The March 2005 labor force was 182 persons greater than one year ago.

The KPB had 2,690 persons listed as unemployed during January 2005. That number increased to 2,763 during February but reversed to 2,449 during March. The March 2005 unemployed total was 448 less than March 2004.

KPB's January 2005 employment rate of 12.3% was down from 13.7% during January 2004. The rate increased to 12.7% during February, but improved during March to 11.1%. The March 2004 rate was 13.5%.

Employment during January 2005 rose to 19,166 from 18,610 a year earlier, climbed to 19,078 during February and on up to 19,531 during March. This compares with 18,715 during February 2004 and 18,901 during March 2004. (See detail on pages 40-44.)

POPULATION

Population estimates for 2004 show the Kenai Peninsula population at 50,980 persons, a 0.8% decrease for the year. Each of the incorporated cities also marked decreases. Homer dropped 9.1% to 5,332 while Kachemak City lost 0.6% to a total of 475 persons. Kenai also decreased, losing 4.4% to 6,809 residents. Seldovia decreased 5.7% to 263 and Seward lost 7.5%, down to 2,540 persons. Soldotna's population is down 5.6% to 3,767. Alaska's population, estimated at 655,435 for 2004, marked a 1.1% increase for the year. (See page 46 for detail.)