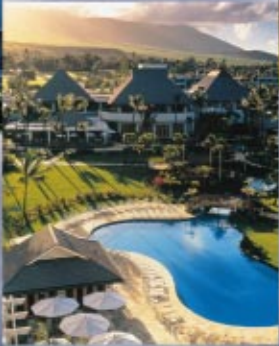


HAWAII 1999

Annual Economic Report, Vol. 48



 Bank of Hawaii

Because we came from numbers,
we tend to have a preference
for tangible **results**.

1, 2, 3,

Actions speak louder than words. And with a
global network of people who know how to
turn insight into results, you can always
expect something concrete. Together,
we can make ideas real. Count us in.

www.ey.com

 **ERNST & YOUNG**

FROM THOUGHT TO FINISH.™

CONTENTS

EXECUTIVE SUMMARY 3

Fifty Years of Economic Research
on the Fiftieth State: A retrospective 4

HAWAII'S ECONOMY: Major Indicators

Gross State Product 6

Personal Income 8

Inflation 10

Employment 12

Tourism 15

Investment 19



To Our Clients and Friends:

We are pleased to present this year's edition of our Hawaii Annual Economic Report. This publication marks the 50th anniversary of economic research at Bank of Hawaii and our family of financial services companies.

Economic expansion continues to be increasingly evident in Hawaii, and we are optimistic about the economic future of our state. Since 1998, Hawaii real personal income and gross state product growth have been consistently rising faster than consensus forecasts. Current forecasts for real gross state product growth for 2000 range between 3.0 and 3.5 percent, and we expect economic growth in Hawaii to continue to accelerate during 2001.

For 2000, we expect to see continued job growth and decreasing unemployment statewide; solid growth in visitor arrivals, contributing to record-setting tourism performance; a modest rise in inflation; and a rebound in construction activity. We are encouraged by the improving economic conditions in Asia and the emerging recovery in international travel to Hawaii.

We are confident that our state will continue to play a vital role in the regional and global economy of the 21st century. We are committed to building a strong economic future for Hawaii. Through research, analysis and published reports such as this, we want to facilitate greater understanding of the factors that shape Hawaii's economy.

For additional analysis and updates on economic and business trends in the state of Hawaii and the Pacific region, please visit the economics section of our website at www.boh.com.

Aloha,



Lawrence M. Johnson
Chairman of the Board and
Chief Executive Officer



Richard J. Dahl
President and
Chief Operating Officer



Executive Summary

- Hawaii real economic growth for 2000 is forecast at 3.0 percent, following release of official figures for 1999 real personal income, confirming Bank of Hawaii's 2.5 percent 1999 forecast after a mid-year revision. The 3 percent forecast is for both real personal income and real gross state product growth during 2000. A recent revision by the State of Hawaii Department of Business, Economic Development and Tourism (DBEDT) now calls for 3.5 percent growth in 2000. Bank of Hawaii expects economic growth in Hawaii to accelerate to 3.5 percent, after inflation, during 2001.
- A consistent pattern of upward revisions has characterized consensus forecasts since 1998. Bank of Hawaii's forecasts for 1999 growth started at 1.5 percent and were revised at mid-year to the 2.5 percent actual outcome. DBEDT's 2000 real GSP growth forecast was 2.2 percent in December 1999, and was revised to 2.6 percent in March 2000 and to 3.5 percent in June 2000. These revisions reflect consistently stronger than anticipated performance across all economic indicators.
- Other Bank of Hawaii 2000 forecasts include: (1) job growth of 1.5 percent, statewide unemployment below the national average by year-end; (2) growth in total visitor arrivals of 3.5 percent to an all-time high for Hawaii tourism; (3) Honolulu inflation trending from 1.5 percent in 2000 to 2.5 percent in 2001; (4) construction growth of 10 percent in 2000 and higher double-digit growth rates thereafter. Record-setting tourism performance will be complemented by the cyclical rebound in construction for more rapid growth than at any time since the late-1980s.
- Total visitor arrivals surged 4 percent from January through May 2000, and 9-10 percent in April-May 2000, shrugging off the impact of Y2K. Asia's economic hangover held eastbound visitor arrivals to a 8 percent decline in 1999, but this was swamped by a 6 percent increase in the dominant, westbound market segment. International arrivals were still down 2.4 percent in first quarter 2000, but the turning point for international travel to Hawaii was marked by a 6 percent increase in April-May 2000. This rebound is expected to accelerate through the remainder of the year.
- Strong performance of "one island only" travel reflects domestic airlines' increasing non-stop capacity to all islands. Scheduled domestic seats were up more than 14 percent through May 2000, continuing a two-year trend. The 7 percent increase in domestic travel to Hawaii from January through May 2000 includes a 20 percent increase in Oahu-only travel from the mainland, and a 4 percent increase in neighbor island-only travel (at the expense of multiple-island travel, down 4 percent).
- The investment explosion in high-end residential and resort real estate has spread to proximate neighborhoods such as East Honolulu and Windward Oahu, West and South Maui, the Kona-Kohala coast on the Big Island, and Kauai's North and South shores. The West Coast US capital inflow is fueled by technology-sector wealth and valuation differentials between Hawaii and California.
- Precommitments for new private construction continue to surge from the cyclical trough established in 1998. Residential building permits rose 24 percent and nonresidential permits rose 33 percent in 1999. First quarter 2000 building permit totals rose 14 percent. Plans for additional hotel inventory are forming across all major destination resort areas statewide with available developable lands.
- Government construction commitments are in decline as state and local governments retrench from the countercyclical public investments postures adopted in the 1990s. However, federal military projects to upgrade military command and control facilities promise to sustain government construction through the emerging upswing.
- Even with individual income tax and general excise tax "de-pyramiding" reductions, state general fund revenues increased more than 4 percent in the fiscal year ending in June 2000.

Fifty years of economic research on the fiftieth state: A retrospective

As Hawaii's economy advances into the new century, perhaps its most striking characteristic is the widening gap between perceptions of its performance and the economic reality. The slow-moving economic recovery of the mid-1990s has been pushed aside by an economic expansion now approaching two years in age. That expansion raised total Hawaii personal income and the number of persons employed in Hawaii to the second straight year of record, all-time highs during 1999. Both measures of economic activity will set new records in 2000. Even while burdened by the legacy of Asia's sharp, if brief, economic crisis of 1997-98, Hawaii tourism also is poised to establish record volumes in 2000. Were it not for the fact that Hawaii's official visitor counts have never been formally revised downward because of overestimates in the early 1990s, tourism in Hawaii might already be recognized as having reached record levels by decade's end.

Thus, two themes characterize this annual economic report. First, this report will serve to chart the pace and composition of the unfolding economic expansion and to provide a forecast for its sustainability. The second underlying theme, however, is the mismatch between performance and perception and the consequences of misperception. With economic expansion increasingly evident, the challenge will be to commit to building the productive capacity necessary to sustain growth. Such commitments to the economic future—whether in physical capital investments, adoption of new technologies, investments in human capital or expansion of public infrastructure—require an expectation of returns on investment. As Hawaii's economy proceeds into the 21st century, it seems as if remarkably few people in Hawaii share such expectations even as increasing numbers of offshore investors are recognizing Hawaii's upside potential.

This year's annual economic report also commemorates the half-century anniversary of economic research at Bank of Hawaii and its family of financial services companies. Then, as now, undertaking research to reveal the structure of and challenges facing Hawaii's economy was intended to be shared with the business community and general public as a public good. Today, the Internet provides broader and more efficient path-

ways through which to share this knowledge capital, and economic research on Hawaii and the Pacific Islands economies is widely available on Bank of Hawaii's web site at www.boh.com as well as from many peer research organizations. Some of those resources are provided in references throughout this report.

Bank of Hawaii's first report on the economy of Hawaii was released on May 1, 1950 following the October 1949 establishment of Bank of Hawaii's research department. Writing in that report's introduction, E.W. Carden, president of Bank of Hawaii, reiterated a promise "to make available to the people of Hawaii the results of the studies of this new department." The first economic report was published in the belief that "it is only on the basis of facts that constructive programs can be developed to improve the basic conditions that affect all of us."

That first report, prepared by James H. Shoemaker, vice president and director of the Department of Business Research at Bank of Hawaii, was entitled *The economy of Hawaii today: a preliminary study of our present economic position with estimates of income and expenditure and a brief review of measures necessary to achieve post-war readjustment*. The report advocated coordinated public policies for employment creation and a long-range program of natural resource development, tourism development, production for export as well as for import substitution and the expansion of onshore value-added in local production. Its principal recommendation was that growth of trade and services and higher living standards required an expansion of Hawaii's exports.

While the parallels between Hawaii's economy in 1950 and in 2000 are notable, equally instructive are the distinctions. In 1950, the territory was struggling to revive its economic health after the wartime boom had given way to a postwar bust, aggravated by a long waterfront strike in 1949. In 2000, the state's economic recovery has finally come into focus, but only after a long hangover following the 1980s boom, punctuated by the Asian economic crisis of 1997-98.

In 1950, mechanization was transforming the sugar and pineapple industries, as well as transportation and distribution of these plantation-based exports. In

HAWAII 1999: ANNUAL ECONOMIC REPORT

2000, another technological revolution has transformed the now dominant services-oriented sectors, generating turbulence in many industries while at the same time creating opportunities for new ones.

In the five years up through 1950, the combined impact of post-World War II demilitarization and the ensuing economic stagnation produced a net population outflow from the territory. In the five years through 2000, post-Cold War military downsizing and the unrelated economic stagnation produced yet another historically notable net population out-migration from the state.

Of all the parallels between the mid-century and turn of the century, the most significant—Hawaii’s ongoing need to emphasize exports as the path to greater economic prosperity—now differs in two important aspects. First, the dominance of tourism as Hawaii’s principal export sector distinguishes today’s island economy from its former character as a plantation agricultural commodity exporter. Second, and more significantly, Hawaii’s export market is today a global market and no longer merely a national market. Advances in transportation and information technologies have radically expanded the geographic scope of Hawaii’s potential exports, and opened trade to a wider range of services and merchandise than ever before possible.

In 1950, Bank of Hawaii’s economic report concluded that “the ultimate objective ... is an expansion of the productive capacity of Hawaii designed to bring into a balance (1) manpower and jobs and (2) income from, and payments to, the mainland.” Today, invigorating employment growth and expanding trade with the global economy—not just the mainland—would top the list of Hawaii’s economic development objectives.

Selected Economic Indicators

	1996	1997	1998	1999	% Change
Macroeconomic indicators					
Honolulu CPI-U (82-84)	170.7	171.9	171.5	173.3	1.0
Inflation rate (%)	1.5	0.7	-0.2	1.0	—
Personal income (bil. \$)	30.393	31.279	31.856	33.006	3.6
Wages and salaries (bil. \$)	16.856	17.362	17.743	18.450	4.0
Other labor income (bil. \$)	3.132	3.090	3.090	3.179	2.9
Proprietors' income (bil. \$)	2.316	2.421	2.477	2.610	5.4
Div, int, rent (bil. \$)	5.584	5.889	6.019	6.162	2.4
Transfer payments (bil. \$)	3.723	3.766	3.764	3.914	4.0
FICA (bil. \$)	1.216	1.250	1.266	1.308	3.3
Real personal income (bil. 99\$)	30.856	31.534	32.190	33.006	2.5
Real income growth (%)	-0.9	2.2	2.1	2.5	—
Employment (thousand)					
Labor force	593.6	594.7	595.0	594.8	0.0
Persons employed	555.7	556.7	557.8	561.5	0.7
Unemployment	37.9	38.1	37.2	33.3	-10.3
Unemployment (%)	6.4	6.4	6.2	5.6	-9.7
Payroll Jobs (thousand)					
Nonagricultural jobs	530.8	531.5	531.3	533.7	0.5
Construction	23.7	22.3	21.7	21.6	-0.5
Manufacturing	16.7	16.6	16.5	16.5	0.0
Transportation	31.0	31.2	31.0	30.9	-0.3
Communications	6.4	6.6	6.8	6.8	0.0
Utilities	3.7	3.6	3.4	3.3	-2.9
Wholesale trade	21.4	21.0	21.0	21.1	0.2
Retail trade	113.9	113.4	111.2	111.7	0.4
Finance, ins., real estate	36.9	36.2	35.5	35.0	-1.5
Hotel services	38.4	38.4	37.8	37.1	-1.7
Health services	34.1	34.7	35.3	35.7	1.0
Other services	94.2	96.2	99.2	101.5	2.4
Federal	31.1	30.7	30.4	30.4	-0.2
Nondefense	14.3	14.4	14.4	14.6	1.7
Defense (civilian)	16.8	16.3	16.1	15.8	-1.9
State	62.8	64.3	65.0	65.8	1.3
County	16.6	16.8	16.9	16.7	-1.2
Agricultural jobs	7.4	7.2	7.6	7.7	1.3
Total jobs	537.8	537.8	538.4	541.3	0.5
Oahu	406.8	405.0	402.6	401.8	-0.2
Hawaii	50.7	51.7	52.5	53.8	2.6
Maui	52.8	53.7	54.9	56.6	3.1
Molokai	1.9	1.9	2.1	2.1	0.0
Lanai	1.5	1.5	1.6	1.6	0.0
Kauai	24.2	24.1	24.8	25.5	2.8
Real Estate Indicators					
Single-family prices (thou. \$)	343.6	321.7	332.4	336.7	1.3
Condominium prices (thou. \$)	201.8	184.4	179.6	180.7	0.6
Single-family sales (units)	3,249	3,759	4,646	5,198	11.9
Condominium sales (units)	3,126	3,556	4,472	5,332	19.2
Total sales (units)	6,375	7,315	9,118	10,530	15.5
Gross receipts (bil. \$)					
Retail	16.396	16.200	16.771	17.946	7.0
Wholesale	12.527	12.284	11.736	12.939	10.2
Services	5.590	5.342	5.520	5.818	5.4
Contracting (construction)	3.240	2.894	2.956	3.092	4.6
Hotel rentals	2.048	2.130	2.060	2.263	9.9
Other rentals	3.779	3.786	3.774	3.737	-1.0
Insurance	0.696	0.754	0.598	0.680	13.7
Commissions	0.678	0.640	0.654	0.738	12.8
Producing	0.466	0.497	0.461	0.509	10.2
Manufacturing	0.608	0.573	0.530	0.605	14.2
All Other	1.995	1.883	1.469	1.385	-5.7
Total	48.023	46.983	46.529	49.712	6.8

Hawaii's Economy: Major Indicators

Gross state product

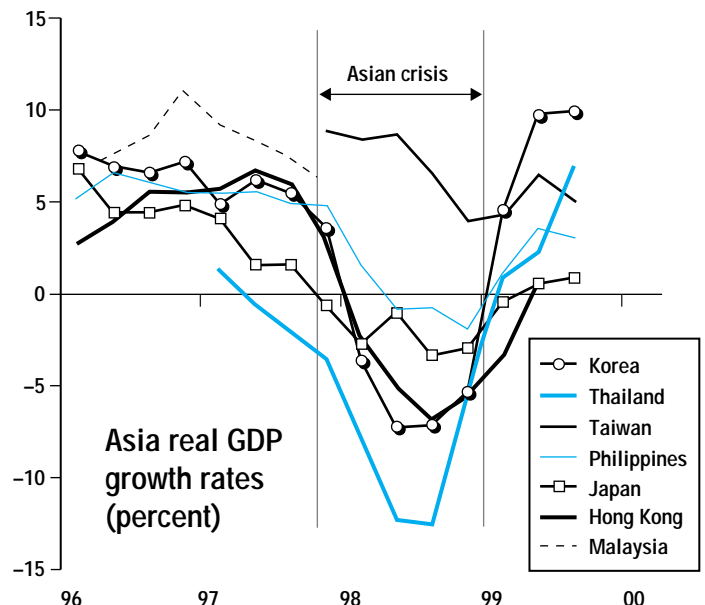
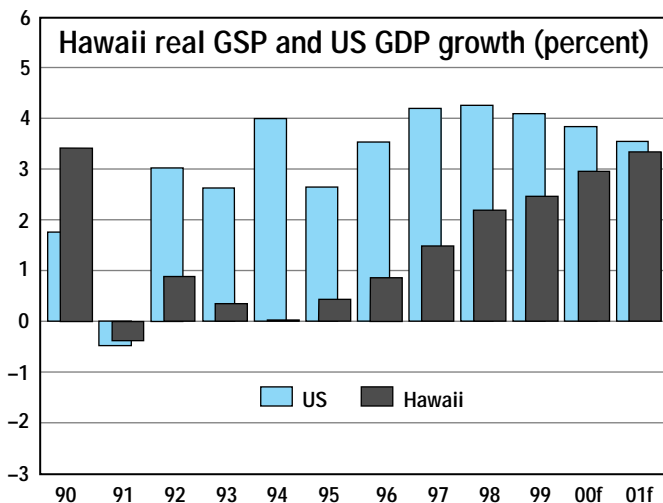
Hawaii real or inflation-adjusted gross state product (GSP) has grown considerably less rapidly than US real GDP during the late-1990s. Moreover, during the transition from recovery to expansion beginning in 1995, Hawaii real GSP has only experienced annual rates of increase that are half as rapid as mainland growth. Real GSP should rise 3 percent in 2000, but Hawaii's 2.1 percent growth rate for 1999 was not at all impressive. Still, this estimate for 1999 by the Hawaii Department of Business, Economic Development and Tourism (DBEDT) is only preliminary. Growth was 2.2 percent during 1998. Before considering the forecast, some context for these growth rates is warranted.

Economic growth in Hawaii was virtually nil from 1990-1995. During the first five years of the decade, Hawaii real GSP grew at a mere 0.3 percent compound annual rate. Recovery began with a slight acceleration to 0.5 percent real growth in 1995, and on to 0.9 percent and 1.5 percent annual growth in 1996 and 1997. More important than these actual growth estimates is the fact that final figures for both 1997 and 1998, when 2.2 percent growth was first registered, were significantly higher than consensus expectations at the time. The pace of economic recovery was not corroborated by anecdotal evidence at the time. Expectations for economic performance, as revealed in Bank of Hawaii's semiannual business confidence surveys, were even more dismal for much of the late-1990s than

earlier in the decade. The sense that Hawaii's economy had missed the boat was underscored by the comparative good health of the US economy and the rapid—if late—economic recovery and technology sector-led expansion in California during the mid-1990s.

Still, in both 1997 and 1998 actual real GSP growth rates proved perhaps one-third faster than originally anticipated in the consensus forecast. This fact was more notable for having been obtained during the worst years of Asia's financial and economic turbulence. Modest growth occurred in spite of the anticipated but nonetheless sharp adverse response of Hawaii tourism to the Asian recession. Still, 2 percent growth, when the national norm was 4 percent, was not even enough to help Hawaii catch up.

Preliminary official estimates for 1999 suggest that real Hawaii GSP increased 2.1 percent in 1999 and 2.2 percent in 1998. Bank of Hawaii's estimate is that growth in 1999 was at least 2.5 percent, and the bank's forecast is that 3.0 percent growth is more than likely in 2000. Both the bank's 1999 estimate and the bank's 2000 forecast represent higher growth rates than was expected one year ago. The bank's view is that growth in 1999 certainly could not have been slower than in 1998, and is almost certainly to have been faster. Hawaii's two main external macroeconomic



drivers, the US mainland and Asian economies, were in better shape in 1999 than in 1998. That fact is seen in much of the economic and statistical detail discussed later in this report.

Upward revisions of both preliminary growth estimates and of growth forecasts have become the rule rather than the exception since 1997. This is true for both the bank's estimates and for official estimates, and it is also true for the consensus estimates. A comparison of initial forecasts, forecast revisions, and actual data for a representative sampling of Hawaii economic forecasters is included in the table at the bottom of page 19.

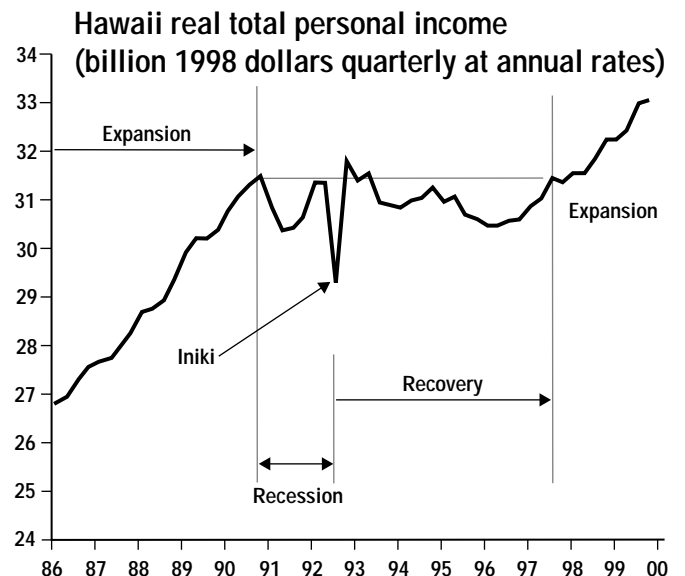
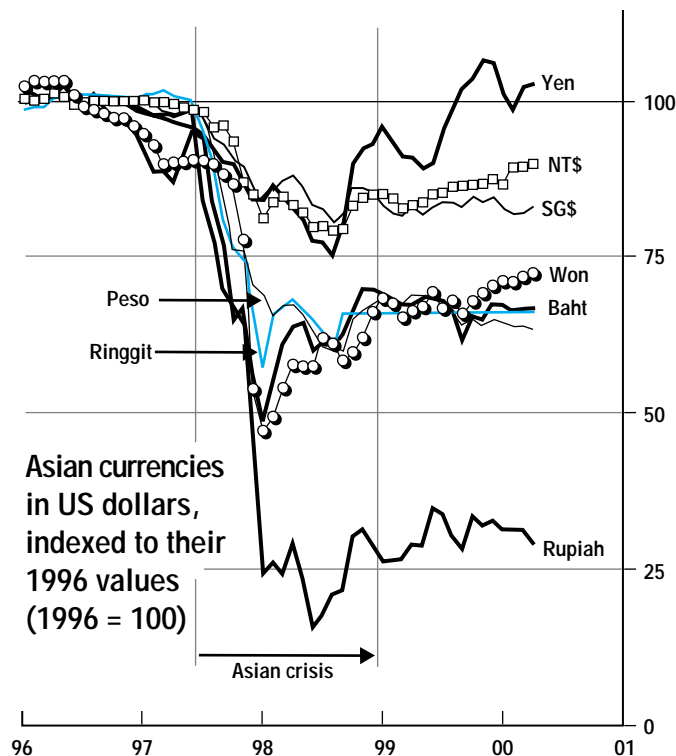
Even 3 percent growth does not seem like much when paired against growth rates elsewhere in the Pacific Rim. US real GDP growth was at a cruising speed of 4.2 percent in both 1997 and 1999, and 4.3 percent in 1998. Quarterly US real GDP growth of as much as 7.3 percent has been clocked as recently as fourth quarter 1999, although it is expected that tighter monetary policies in the US will produce the requisite deceleration to contain price inflation. The Federal Reserve Board—the nation's monetary policy-making authority—in the past has enunciated a target real GDP growth rate closer to 2.5 percent. Whether that will be achieved remains an open question, but economic growth in Hawaii seems likely to

converge to the national norm in 2000 or 2001.

Because of the contribution of modern information technologies to productivity, a debate has been ongoing about how fast US real GDP growth can be sustained without accelerating inflation. Adherents to the view that the “New Economy” has emerged would argue that more rapid productivity growth enables the US to grow at 4 percent without fear of higher inflation. A more traditional view is that US real GDP growth in excess of 3 percent is unsustainable without the risk of higher domestic inflation. For an advanced economy like the US, 3-4 percent annual real GDP growth is thought by most economists to be relatively good.

Matters are complicated by the fact that much of the activity in the new economy is ill-suited to measurement using statistical tools developed back when agricultural and manufactured goods dominated aggregate economic output. Goods-producing industries now comprise smaller shares of gross domestic product than information and services. These newer kinds of output are less easily rendered discrete and countable, while goods generally can be measured in unit values at market prices. It is increasingly challenging to use measuring sticks intended for merchandise to gauge growth in outputs of information and services. Though measurement techniques are evolving rapidly, old rules of thumb about which GDP growth rates are consistent with price stability may no longer apply.

Moreover, US economic growth in recent years has been dominated by nonresidential fixed investment in equipment and software, and by personal consumption



expenditures on durable goods. The latter are increasingly weighted toward personal computing equipment and other high technology-laden items. As twin engines of growth, consumer durables outlays and private investment spending reflect the public's commitment to the economic future. Consumption and investment devoted to information technologies embody rapid advances in processing speeds and bandwidth that are central to the productivity boost provided by high technology. Understanding the quality change embodied in hardware and software has been a major research objective of government agencies charged with measuring gross product.

For this reason alone, Bank of Hawaii's forecasts for Hawaii real GSP in recent years have tended to be higher than others' forecasts. Since the mid-1990s, Bank of Hawaii's forecasts have been consistently revised upward after having been released in comparatively conservative, preliminary form. Taken together, these features—the anticipated productivity boost provided by the adoption of modern information technologies, and the unanticipated economic growth that reflects an excessively conservative outlook—suggest that our characterization of economic activity in Hawaii has been insufficiently vigorous. Ironically, more often than not, recent forecasts have been received with skepticism. As a result, to many it would seem almost provocative to assert that Hawaii's economic recovery is not only over, it has been superseded by an economic expansion now moving into its third year.

However received, our view is that a real

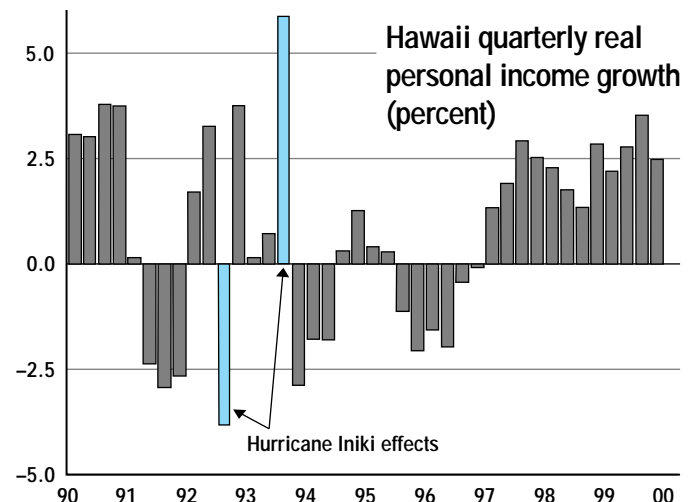
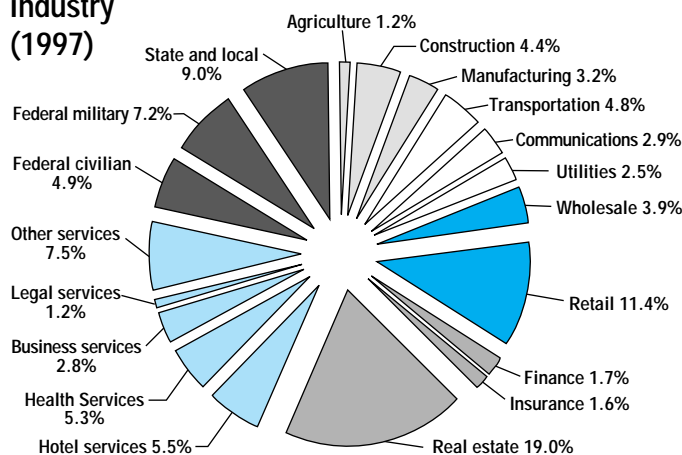
economic growth rate in the neighborhood of 3 percent is not only likely, it is likely to be surpassed during the next year or two. The positive impact of the technology shock alone is sufficient to generate real GSP growth at this rate in coming years. The negative—and transitory—impact of rising crude petroleum prices during the winter of 1999-2000 is insufficient to derail that economic acceleration. The rebound in Asia-Pacific travel and tourism anticipated in 2000 will complement the persistent strength of westbound travel from North America associated with a healthy national economy. Even during the depths of the Asian crisis, Hawaii experienced net growth in the number of visitor days.

During the year 2000, more businesses will awaken to the economic opportunities foregone by their complacency; more consumers will awaken to the dark side of rising property values; and more politicians will awaken to the positive income elasticity of tax revenues than in any year in the prior decade. The few die-hards still obsessed with recession can take heart that as Hawaii real economic growth steps up from 3 percent to 4 percent during 2000-2001, the economic expansion will bring them two years closer to the next recession than the last. Meanwhile, we will just have to be content with Hawaii gross state product rising from one record high to the next.

Personal income

Because personal income is published quarterly by the Bureau of Economic Analysis (BEA), US Department of Commerce, it tends to be a more readily available measure of aggregate income than gross state product, which is available only on an annual basis. Personal

Hawaii gross state product originating by industry (1997)



HAWAII 1999: ANNUAL ECONOMIC REPORT

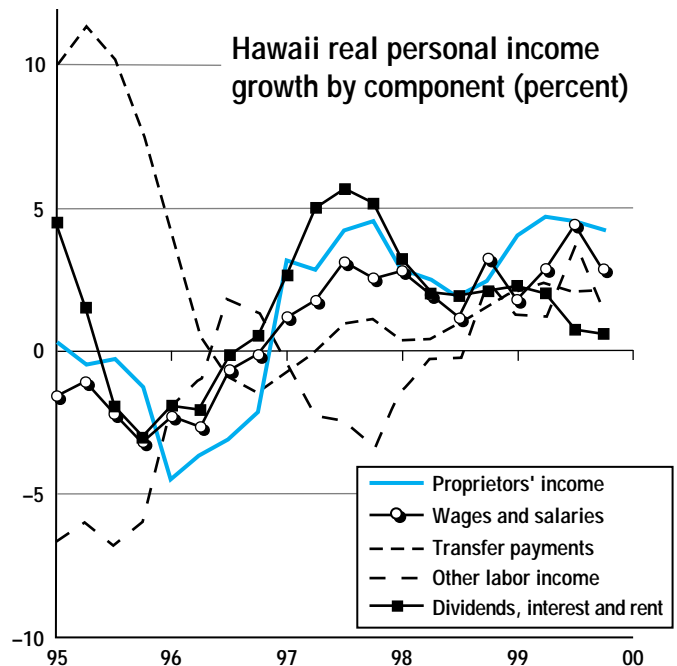
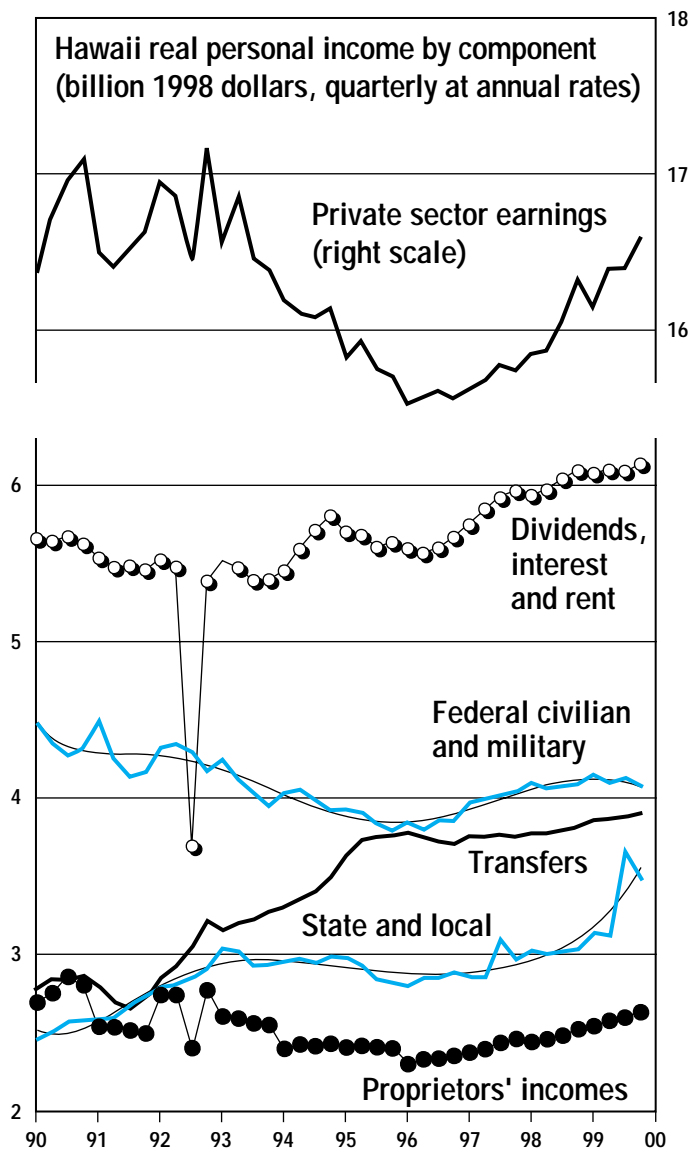
income reveals more about the pattern of income growth across income components than does GSP, although gross product can usefully be decomposed into aggregate expenditures and value-added by industry. Quarterly personal income data published through fourth quarter 1999 confirm much of what has been argued in the preceding section.

As with Hawaii gross product, Hawaii personal income has been rising faster than forecast. Bank of Hawaii forecasts 3.0 percent growth in Hawaii real personal income in 2000. Contingent on a rebound in construction and investment activity in Hawaii, prospects for 2001 are even better, and 3-4 percent real personal

income growth is a possibility. (Quarterly real personal income estimates are derived from the nominal BEA personal income time series, adjusted for inflation using a quarterly Honolulu CPI-U series interpolated from the official semi-annual data. The quarterly interpolations are weighted toward the most recent semiannual estimate to take into account inflation momentum.)

Between fourth quarter 1997 and fourth quarter 1999 total personal income grew at a 2.6 percent compound annualized rate after adjustment for inflation. Fourth quarter 1999 Hawaii real personal income was 2.5 percent higher than the year-earlier total. Hawaii's nominal personal income total (not adjusted for inflation) for fourth quarter 1999 was fully 4.1 percent higher than the year-earlier figure. These growth rates matched the 2.5 percent Bank of Hawaii forecast for 1999 and slightly exceeded other Hawaii forecasters' assessments, which ranged from 2.0 to 2.2 percent. Even under the clear evidence of faster-than-expected growth during the last two years, forecasters remained cautiously optimistic about prospects for 2000. This makes it more than likely that in 2000, once again, actual data are likely to surprise forecasters by coming in higher than expected.

For example, after June 2000 revisions, the State's official forecast from economists at the Hawaii Department of Business, Economic Development and Tourism (DBEDT) calls for personal income growth of 3.5 percent in 2000, after inflation. DBEDT's prelimi-



nary estimate for 1999 real Hawaii personal income growth was 2.1 percent, even after three quarters of real growth at an annualized rate in excess of 2.2 percent. This forecast was revised upward from a 1.7 percent forecast published in September 1999, and 1.6 percent published in March 1999.

DBEDT was not alone. Bank of Hawaii's real personal income forecasts for 1999 were 1.5 percent in January 1999, revised upward to 2.0 percent in August 1999, and again revised upward to 2.5 percent by the end of 1999. The University of Hawaii Economic Research Organization (UHERO) forecasted 1999 real personal income growth of 1.2 percent at the beginning of the year, but revised its assessment to 1.7 percent in the spring and to 2.1 percent by year's end. Bank of Hawaii, DBEDT and UHERO have generally been regarded as excessively optimistic. Media treatments of the Hawaii economy's performance continued to refer openly to Hawaii's "recession" throughout 1999.

To many, even more surprising than the relatively high rates of real personal income growth Hawaii recorded since 1997 is the composition of income growth. In a state where the business community has struggled, it will seem almost contradictory that since the mid-1990s the clear pattern emerging from the personal income data is that business income has led Hawaii's economic recovery. In 1998 and 1999 that pattern was reaffirmed: of the major Hawaii personal income components, proprietors' income has risen—at a 3.5 percent rate, adjusted for inflation—faster than any other component. Over a three-year period, since the end of 1996, proprietors' income has grown at a 3.8 percent compound annual rate, after inflation. Since the end of 1997 that growth rate has been 3.5 percent. Fourth quarter 1999 Hawaii proprietors' income was 4.3 percent higher than one year earlier, after adjustment for inflation. Hawaii's economic expansion currently is led by small business income.

The largest component of Hawaii personal income, wages and salaries, has experienced about 2.5 percent annual growth for the last several years. Since 1996, real quarterly wages and salaries in Hawaii have increased at a 3.0 percent compound annual rate, and since 1997 at a 3.2 percent annualized rate. Fourth quarter 1999 real wages and salaries were 3.0 percent higher than the year-earlier amount. Real growth in dividends, interest and rent has been decelerating for the last several years, as has growth in transfer payments.

Other labor income has growth slightly slower than wages and salaries.

By industry, real earnings growth has varied widely. Not surprisingly, state and local government experienced the most rapid growth in earnings during the late-1990s. Earnings growth in state and local government was 6.6 percent, after inflation, on a compound annual basis, between the end of 1996 and fourth quarter 1999. State and local government earnings surged at a 10.9 percent annual rate during 1999, and recorded a 14.8 percent increase between fourth quarter 1998 and fourth quarter 1999. The data provide clear evidence of public sector unions' success in recent years at squeezing income growth out of a state economy with an underlying growth rate only one-half to one-sixth as fast.

Inflation

As a further indication of the quickening pace of economic recovery, inflation in Hawaii began to work its way back into positive territory during 1999. For the year 2000 inflation in the Honolulu consumer price index is forecast to continue converging to the national norm of 2.5 to 3.0 percent. However, even taking into account the faster-than-expected rebound in Hawaii inflation that occurred during 1999, national inflation is still expected to be somewhat higher than local measures during 2000.

Where regional economic activity is strongest, such as in the San Francisco Bay Area, inflation has averaged around 4.5 percent. In those regions, living costs will probably continue to rise faster than the national norm. Conversely, where regional economic activity is comparatively weak, such as Hawaii, inflation will remain below the national average. Lower than average inflation will mean that Hawaii living costs will not rise as fast as nationwide. Consequently, the cost of living premium associated with Hawaii in recent years—relative to the national average—is likely to continue narrowing during 2000. By one measure, Hawaii's cost of living premium has fallen from around 35 percent above the national average to 25 percent above the national norm. As Hawaii's economic expansion proceeds into 2001, however, the trend toward declining relative living costs in Hawaii may begin to reverse.

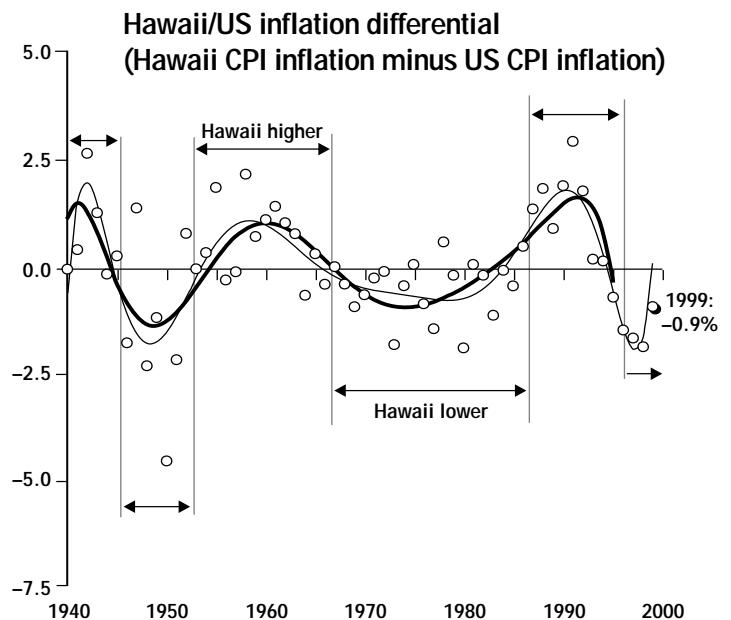
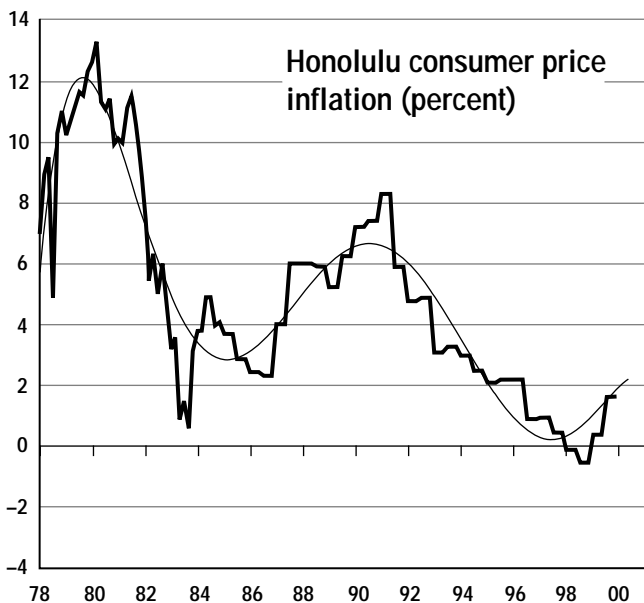
For calendar year 1999 the Honolulu consumer price index for all urban consumers (CPI-U) was 173.3 on the 1982-84 = 100 base period. That index number yielded a 1.0 percent Honolulu inflation rate for the year as a whole, following the -0.2 percent inflation rate

(outright deflation) registered during 1998. Inflation in 1997 was only 0.7 percent. Steady disinflation occurred in Hawaii during the mid-1990s, following a peak annualized inflation rate of 8.9 percent in first half 1991 at the end of the last cyclical upswing. The transition in Hawaii inflation through the trough of 1997-99 was consistent with other evidence of a reacceleration in economic growth at that time. (Although neighbor island inflation rates may differ slightly, as a measure of urban inflation the CPI-U is available only for Oahu. It is probably representative for the state as a whole.)

When measured on the semiannual basis that is the reporting frequency for Honolulu consumer price index, the switch from declining to rising inflation in 1999 was even more stark. During 1998, Hawaii inflation benefited from the deflationary impulse of depreciating Asian currencies (and therefore import costs) and falling commodity prices (especially petroleum) associated with the Asian economic crisis. Deflation in consumer prices was recorded at -0.5 percent in second half 1998. However, the subsequent stabilization and recovery of Asian economies, partial rebound in Asian currency values, and the acceleration of westbound tourism growth in 1999, combined to turn first half 1999 inflation from negative to a positive 0.4 percent. Inflation accelerated during second half 1999 to 1.6 percent, on a year-over-year basis, as rising energy costs, a tightening labor market, and residential real estate rebound came together. Annual inflation in 1999 not only was higher than the -0.5 percent originally forecast by Bank of

Hawaii, but also exceeded the +0.5 percent inflation rate anticipated in a mid-1999 forecast revision. Like other Hawaii indicators, Honolulu's 1.0 percent 1999 inflation rate exceeded even the most bullish forecasts for the year.

Recent improvements in the measurement of price change have improved the ability of the consumer price index to account for product quality improvements and consumers' substitution responses to changing relative prices. However, those enhancements have not completely erased the upward bias inherent in the construction of the CPI. Thus, even though measured inflation in Honolulu was 1.0 percent during 1999, for the last several years inflation has been virtually nonexistent. This is partly a reflection of the unimpressive pace of economic recovery as it emerged in Hawaii during the late-1990s. Still, without the deflationary contribution of Asia's economic crisis, and with a statewide unemployment rate likely to fall from 5 percent to 4 percent during the course of 2000, Honolulu's CPI-U seems certain to record an acceleration in inflation. Whether 2-3 percent inflation is the outcome partly depends on how quickly the inflationary impact of higher energy costs passes through the inflation statistics, and partly depends on how much inflationary pressure comes from rising housing costs during the year. With US inflation expected to remain in the 2-3 percent range during 2000, a case can be made that returning to the national norm may be the outcome by the end of 2000.



Employment

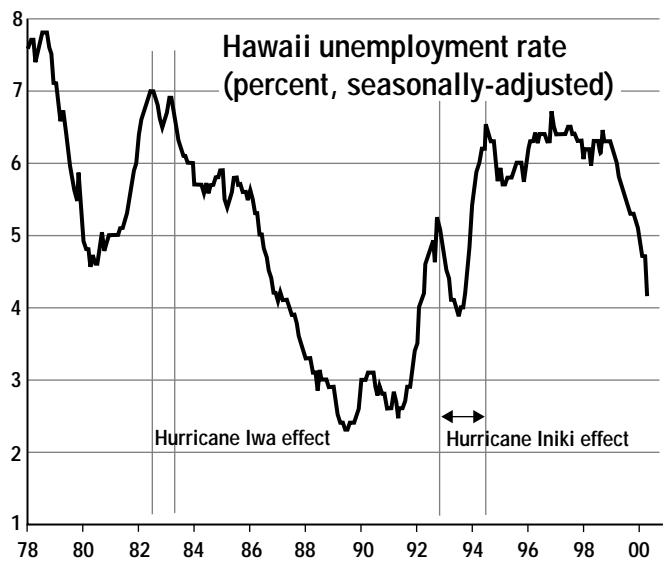
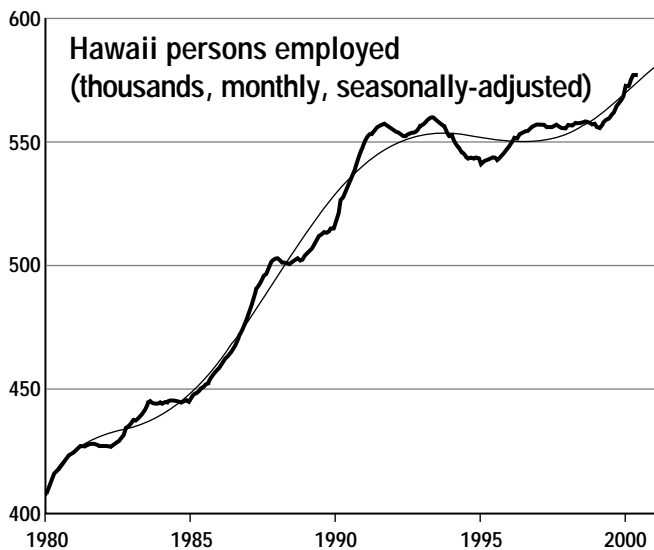
A significant, missing aspect of Hawaii’s emerging economic expansion has been growth in employment. Similar to total Hawaii personal income, the number of persons employed statewide did rise enough to break into record territory during 1999, even with a relatively small calendar-year increase of 0.7 percent. Still, after revisions to earlier data, Hawaii employment growth was virtually nil for most of the 1990s, right through the end of 1998. Moreover, payroll employment growth—the number of occupied jobs in Hawaii—also was practically nonexistent in 1998 and 1999. Technological progress can sustain rising income even without employment growth, as long as productivity growth is sufficient. But most people look to employment growth as a confirmation of an economy’s recovery.

Labor market indicators are lagging indicators. Thus, given the late arrival of Hawaii’s recovery it is not surprising that confirmation is only just appearing in employment data during 1999 and 2000. As forecast, the nonagricultural job count in Hawaii rose 0.5 percent during 1999. Nonagricultural payrolls declined 10 percent between 1991, the last peak, and 1996, the low point for the cycle. The nonagricultural job count languished at around 531,000 for the next two years, rising less than 0.1 percent through 1998. Now that economic activity has been rising for a couple years, job growth is certain to follow. Job data have been notably slow to respond, although other employment measures have rebounded.

Unlike other macroeconomic indicators for

Hawaii, actual job growth did not exceed the forecast for job growth. Moreover, seasonally-adjusted payrolls only began to show serious signs of revival during fourth quarter 1999, when year-over-year growth reached 1.0 percent. The 1999 averages were 533,700 nonagricultural jobs and 7,650 agricultural jobs. Both totals were substantially lower than in the early 1990s, when agricultural employment peaked at 9,550 (1991), and nonagricultural employment peaked at 542,800 (1992). Still, the 0.5 percent increase in nonagricultural jobs during 1999 was accompanied by a 6.3 percent increase in agricultural jobs. Following an uneven transition period after plantation closures in the mid-1990s, the growth of diversified agriculture on former plantation lands gathered speed.

Job growth was strongest in agriculture, but was closely followed by growth in the business services sector. Business services registered a 5.4 percent increase in payrolls during 1999, rising to 27,200 jobs. Since 1991, when the business services job count was first published (19,900), payrolls have grown at a 4.0 percent annual rate. The business services sector is a catch-all of sorts, comprising three major new industry definitions that have been adopted for use in future industrial classifications. These industries are: (1) information, (2) computer software and services, and (3) professional, technical and managerial services. The fact that business services (under the old industrial classification system) is one of the fastest growing employment sectors in Hawaii is a confirmation of rapidly changing technology and its impact on the structure of Hawaii’s economy. This is mirrored in the declining employment of industries like

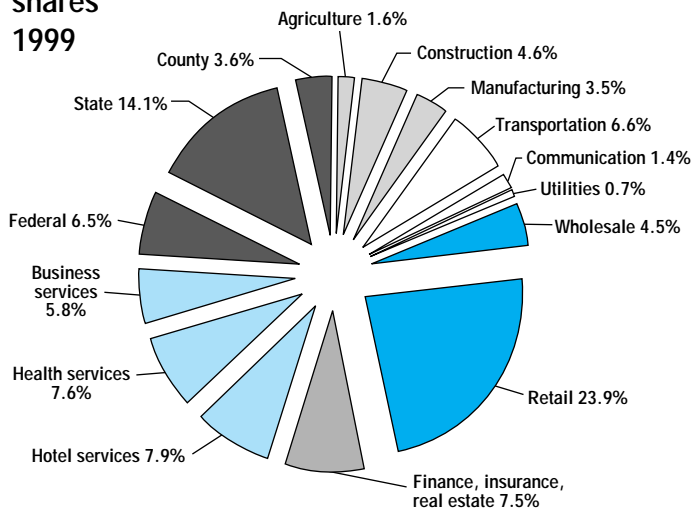


HAWAII 1999: ANNUAL ECONOMIC REPORT

financial services and hotels in Hawaii, where technological progress and globalization are driving structural change. During 1999, performance of both financial services and hotels in Hawaii were improving, yet both industries were downsizing and outsourcing many functions.

While jobs have been slow to respond to Hawaii's economic expansion, the number of persons employed has been rising somewhat faster since the mid-1990s. The small, 0.7 percent increase in persons employed during 1999 followed four years during which annualized employment growth was also 0.7 percent (after recent downward revisions). Although these increases have been small, they have taken place against a backdrop in which the labor force has remained unchanged. In 1996 Hawaii's labor force totaled 593,600 while in 1999 the labor force was 594,800. Labor force growth is limited by a combination of very little net in-migration to Hawaii and shrinkage of the population of persons aged 20-30. That age cohort represents the bulk of first time labor force entrants; between migration, demographic shifts and the "discouraged-worker" phenomenon, growth in the number of persons employed has tightened up the labor market since mid-1998. Over an 18-month period ending in early 2000, Hawaii's unemployment rate has fallen 1.9 percentage points to 4.3 percent, on a seasonally-adjusted basis. By mid-2000, at this rate, unemployment in Hawaii will be under 4 percent, approximately the same as the national average. Thus, even with slow employment growth, labor markets have been tightening because of labor supply constraints.

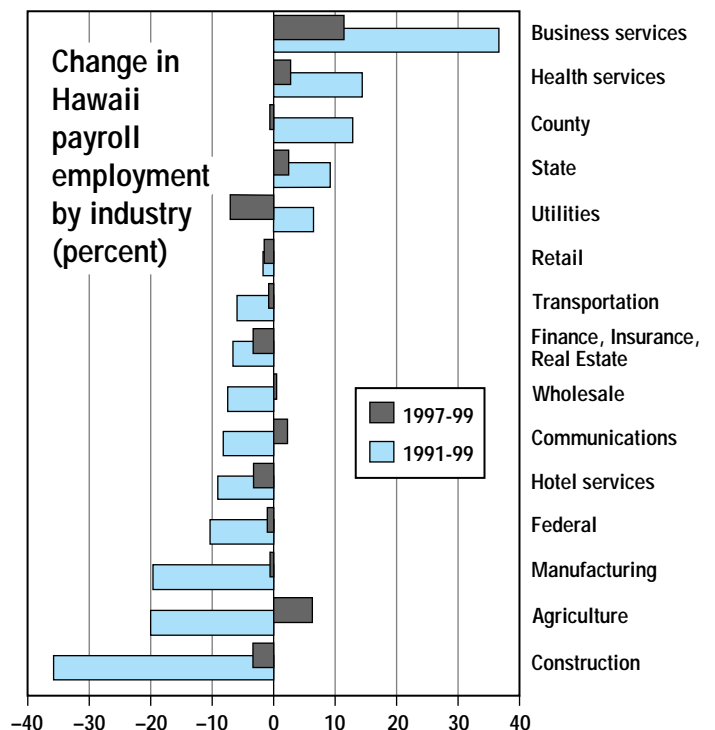
Hawaii employment shares 1999



The pattern of employment growth varied across the islands during 1999. Payroll employment declined 0.3 percent on Oahu during 1999 to just under 400,000 jobs, the lowest since the late-1980s. Employment on the neighbor islands was up modestly, rising 2.6 percent on the Big Island, 2.7 percent on Kauai and 2.9 percent on Maui, to a combined total of just under 135,000 jobs. That growth rate for payroll employment is consistent with other indicators pointing to overall neighbor island economic growth in excess of the 2.5 percent real GSP growth rate estimated for the state as a whole.

Job growth was most rapid in the construction industry on Maui (up 17.1 percent) and the Big Island (up 14.3 percent). Although construction jobs on Kauai were largely unchanged in first half 2000 from one year earlier, the construction recovery statewide is expected to generate a continuing resurgence in construction employment during 2000.

Throughout the 1990s payroll employment growth has been dominated by one sector: business services. With its strong information technology foundation, it may seem surprising that the fastest growth in business services employment occurred in neighbor island labor markets during 1999. Job growth was strong in the business services sector on Kauai (up 22.2 percent), Maui



(13.9 percent), the Big Island (9.7 percent) and was respectable in Oahu business services (up 4.3 percent).

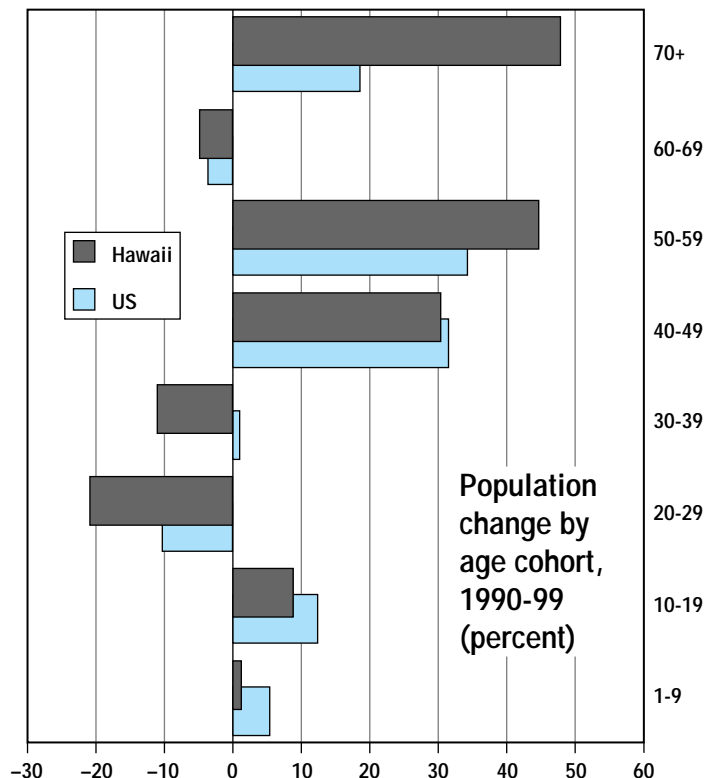
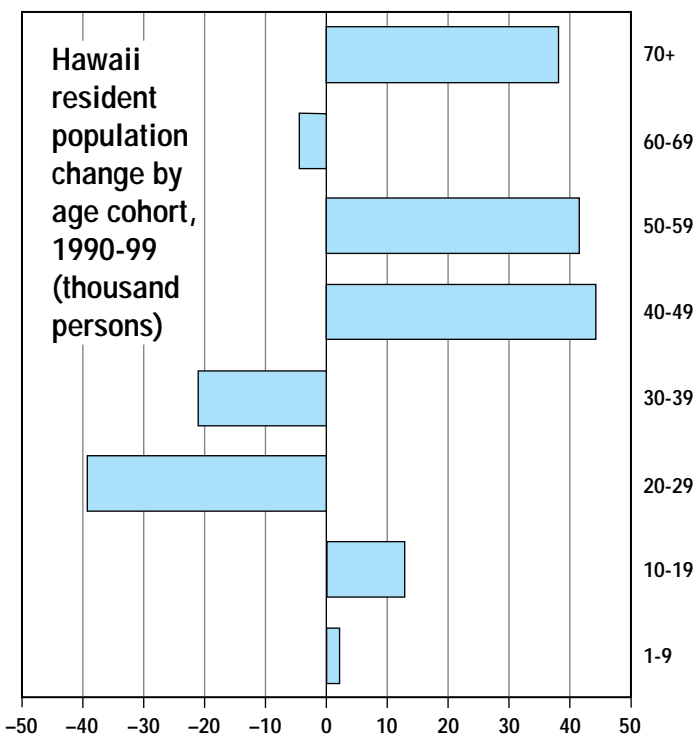
Agricultural job counts were up slightly on the neighbor islands, but jumped 17.9 percent on Oahu where the transition to diversified agriculture was strongest. Most other sectoral job counts were flat to down, with notable exceptions. Nonfinancial services employment registered the most consistent increases across the four counties. Transportation jobs increased 11.1 percent on Maui and 7.8 percent on Kauai in 1999 in response to additional nonstop mainland flights. Though the overall transportation job count on the Big Island was unchanged in 1999, air transportation jobs there were up 18.1 percent.

With job gains starting to occur on the neighbor islands, unemployment continued its downward drift. Unemployment averaged 4.9 percent of the labor force on Oahu during 1999, just under the statewide average of 5.6 percent for the year. Statewide unemployment continued its decline into first quarter 2000 to the 4.7 percent rate noted above, led by the decline in Oahu unemployment to 4.1 percent, matching the national average. Though job growth has been most rapid on the neighbor islands, only Maui has joined Oahu as islands where unemployment is lowest. This is a customary distinction, however, because structural unemployment (for example, mismatches

between workers' skill sets and employer's needs) tends to be a greater challenge for neighbor island economies, which are not as diverse as Oahu's economy.

Notwithstanding their higher unemployment proportions of the labor force, the neighbor islands experienced significant declines in unemployment rates in 1999. Rapid absorption of unemployed labor is anticipated statewide, but especially on the neighbor islands, during 2000. Unemployment rates have been falling about 0.1 percentage point per month on Oahu, but have been falling almost fifty percent faster on the neighbor islands. Unemployment fell to around 4.5 percent of the labor force on Maui in first quarter 2000, down from 6.0 percent in first quarter 1999. From around 8.7 percent in first quarter 1999, unemployment on the Big Island dropped below 6.5 percent of the labor force in first quarter 2000. The unemployment rate on Kauai declined from 9 percent to 7 percent between first quarter 1999 and first quarter 2000. Considering that neighbor island unemployment rates in the mid-1990s were higher than 7 percent on Maui, close to 11 percent on the Big Island, and as high as 15 percent on Kauai, labor force absorption in the last several years has been dramatic.

Why have income and the number of persons



employed grown while payrolls have remained unchanged for so long? Though the pattern statewide is expected to change from 2000 onward, with payrolls catching up, income growth has outstripped payroll growth throughout the 1990s. Both income and employment (persons) have responded, however modestly, to the growth of mainland tourism and a revival of construction and investment activity. Jobs have not. Taken at face value, the apparent contradiction between a rising number of persons employed and a lack of job growth can be resolved if employment growth is among the self-employed. The household survey through which the number of persons employed is estimated would capture rising self-employment, while establishment surveys from which payroll data are obtained would not. Unfortunately, self-employment data are notoriously unreliable, and labor statisticians discontinued reporting these data several years ago as a result. Thus, the hypothesis that self-employment is a growth leader can only be supported by inference, not direct data.

Still, a rise in self-employment, small business formation and the spread of outsourcing would be consistent with the hypothesis that changing workplace technology—personal computers, e-mail and fax machines—make possible more independent workers in nontraditional employment settings. The trend toward outsourcing, in which larger firms increasingly rely on the services of independent, outside suppliers, means that employment could be growing even though payrolls of larger organizations are not. Small firms and new firms tend to be overlooked in the establishment surveys from which payroll data are obtained. Larger firms have entered an era of downsizing in which commercial viability can be sustained even though staffing has decreased. Some combination of these changes in working environments probably explains the fact that payrolls have expanded less rapidly than the number of persons employed in Hawaii.

Tourism

Tourism in Hawaii emerged into a new century poised for renewed growth and disciplined by the shocks of the 1990s. During 1999, nearly 6.85 million visitors arrived in Hawaii by air, and an additional 45,916 visitors arrived by cruise ships. The year's 6.89 million total visitor count was up only 1.7 percent from the 1998 total. In both years, arrivals fell short of all-time highs as a result of lingering effects from the Asian economic crisis on eastbound travel. Asia's crisis of 1997-98 was replaced by an economic rebound during 1999. Quarterly

real GDP growth rates of 10-12 percent marked Korea's turnaround, and GDP growth of 5-7 percent was experienced by Thailand. Because Japan's moribund economy—expected to experience little or no real growth in 2000—is so dominant in Hawaii's totals, the strength of North American travel to Hawaii will continue to be partially offset by comparative weakness in Asian travel demand. Nonetheless, a recovery in international travel is expected to complement travel from the more robust mainland market. Together, this should produce solid growth in visitor arrivals and visitor days for Hawaii during 2000. Bank of Hawaii forecasts 3.5 percent visitor arrivals growth in 2000. Slightly higher growth in visitor days should be recorded, to the extent that growth in mainland arrivals pulls upward visitors' average length of stay in Hawaii.

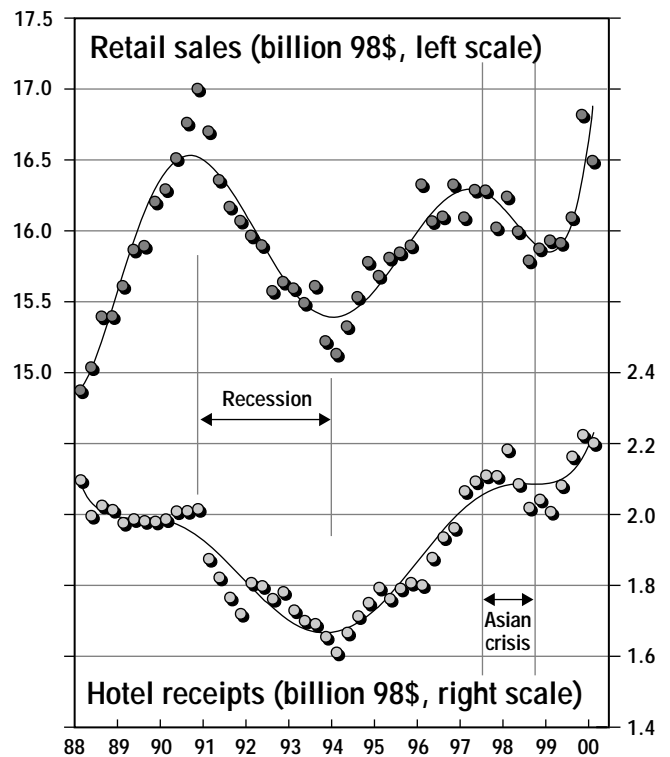
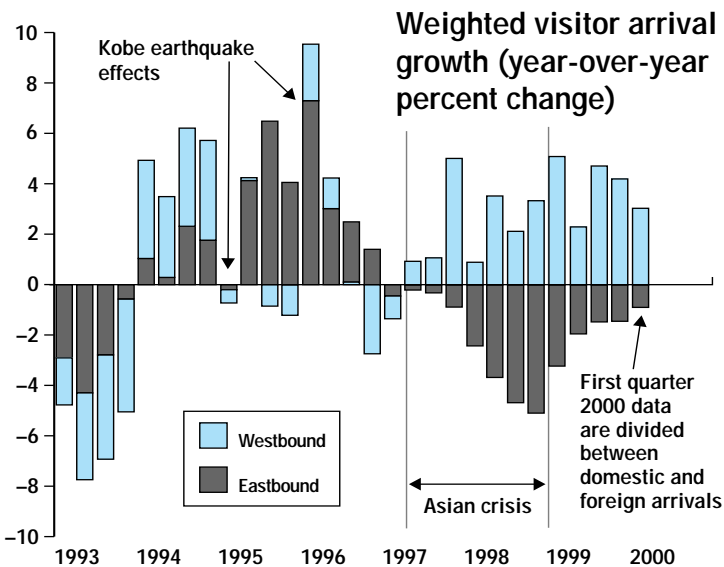
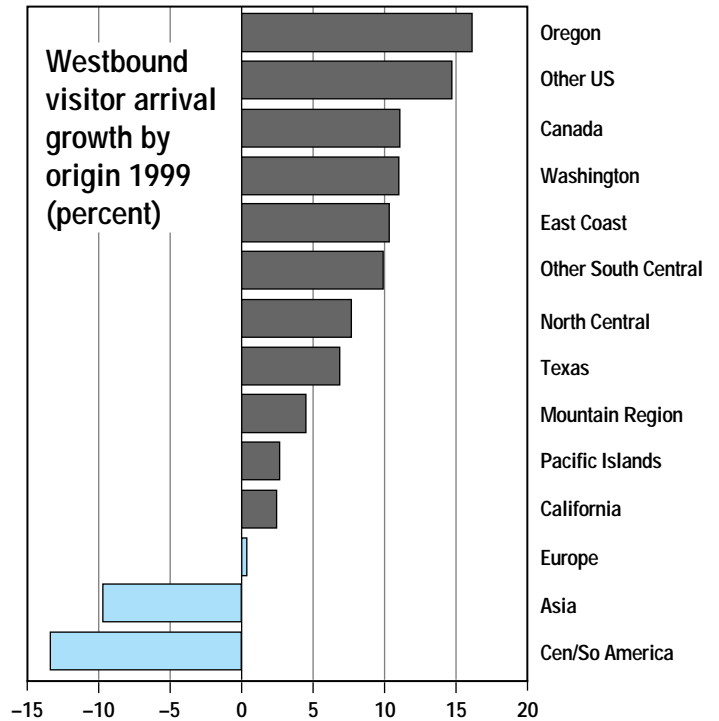
Tourism's performance indicators for 1999 were a snapshot of the turbulence typical of the last decade. As the US economic expansion converged on a steady-state path with around 4 percent real GDP growth, and buoyed by a rising stock market, demand for travel to Hawaii in 1998 and 1999 surged. During 1999, Hawaii's westbound visitor count, comprising tourists from North America and Europe, jumped 6.1 percent. This rise was recorded in spite of a flat December 1999 performance (up only 0.1 percent) when travel was dampened by Y2K concerns. Mainland travel to Hawaii was strong across the entire Hawaiian island chain, including Waikiki on Oahu, generally most popular among Asian tourists. Oahu's westbound visitor count in 1999 rose 8.2 percent; the number of westbound visitors traveling only to Oahu soared 9.6 percent. Island-specific travel was up sharply throughout the state during 1999 because of the increasing number of non-stop flights bound directly for the neighbor islands. The Kauai-only westbound visitor count leapt 12.5 percent in 1999. Gains for Maui-only and Big Island-only westbound visitor counts were more modest, increasing 1.5 percent and 4.1 percent, respectively. Neighbor island westbound visitor counts were up 4.6 percent overall. Though the westbound total reached more than 4.5 million during 1999, multi-island travel assured Oahu of a westbound count in excess of 2.47 million and neighbor island counts exceeding 3.14 million.

The impact of expanding direct-air service, both to neighbor island destinations and combining nontraditional city pairs on the mainland, was reflected in westbound visitor counts by origin market. Travel to Hawaii from the East Coast was up 10.3 percent in 1999. The North Central states produced a 7.7 percent increase in westbound arrivals. South Central states generated a 10.0 percent increase, adjusted for the 6.8 percent rise in

westbound traffic from Texas. Regional strength was not the sole determinant of strong arrivals growth during 1999. The data suggest that increasing commercial aviation capacity (lift) has played a significant role in unlocking pent-up demand in strong regional economies. Expanded non-stop and one-stop service to Hawaii from cities like Houston, St. Louis, Atlanta, Newark and Detroit as well as other cities has contributed greatly to the rising westbound visitor count.

In the Far West, regional economic strength and increased lift have buoyed the visitor count. California's strong economy produced nearly 1.36 million westbound visitors in 1999, but that number reflected an increase of only 2.4 percent. Elsewhere in the Pacific region, arrivals growth was in the double-digits. Visitor arrivals from Oregon rose 16.2 percent in 1999. Visitor arrivals from Washington rose 11.0 percent. Canada's westbound visitor count was up 11.1 percent. States in the Mountain region produced a 4.5 percent increase in westbound visitor arrivals. Hawaii tourism has acted as a conduit through which the US mainland economic expansion has been transmitted to the island economy.

Improving economic conditions in Asia will probably augment US mainland tourism growth by turning upward the Asian visitor count for the first time since 1996. In Japan, the balance sheet implosion caused by falling stock and property values in the early 1990s has never been overcome. Pumping nearly 10 percent of GDP annually in to central government deficits to generate a fiscal stimulus, Japan has barely



HAWAII 1999: ANNUAL ECONOMIC REPORT

eked out a single percentage point of real growth. Consumer confidence has languished at a low ebb, weighed down by uncertainties associated with the demise of Japan's implied lifetime employment guarantees. Only a strengthening currency, relative to the US dollar, provided any boost for Hawaii in 1999 by enhancing the purchasing power of the yen for Japanese tourists. Still, the number of eastbound Japanese tourists arriving in Hawaii declined 7.4 percent during 1999, falling to 1.8 million. Oahu's Japanese visitor count dropped 9.1 percent from 1.91 million in 1998 to 1.74 million in 1999. Neighbor island travel by Japanese compressed even more, falling 15.2 percent in 1999. Only a slight increase in length of stay, which remained at a historically brief 5.65 days, dampened the decrease

Hawaii Tourism Statistics

(In thousands, or as noted)	1996	1997	1998	1999	% Change
Total Visitor Arrivals	6,830	6,876	6,738	6,849	1.6
Westbound visitors	4,004	4,078	4,245	4,503	6.1
Eastbound visitors	2,826	2,798	2,493	2,346	-5.9
Total Visitor Days (millions)	59.157	57.716	58.342	59.567	2.1
Average Daily Census*	161.6	157.9	159.9	163.2	2.1
Estimated National Origins*					
United States	3,658	3,632	3,871	NA	—
Foreign	3,172	3,244	2,867	NA	—
Canada	329	303	319	NA	—
Asia	2,417	2,521	2,156	NA	—
Japan	2,090	2,223	2,009	NA	—
Other Asia	327	298	152	NA	—
Oceania	129	131	116	NA	—
Australia	85	83	70	NA	—
New Zealand	33	40	37	NA	—
Other Oceania, Pacific	11	8	9	NA	—
Europe	260	255	242	NA	—
United Kingdom	76	77	80	NA	—
West Germany	86	81	68	NA	—
Other Europe	97	97	94	NA	—
Other Foreign	37	34	34	NA	—
Total Visitors by County					
Oahu	4,982	5,018	4,718	4,732	0.3
Hawaii	1,228	1,206	1,271	1,260	-0.9
Kauai	969	1,008	1,040	1,092	5.0
Maui	2,327	2,352	2,303	2,261	-1.8
Westbound Visitors by County					
Oahu	2,350	2,280	2,283	2,471	8.2
Hawaii	880	915	961	995	3.5
Kauai	825	857	904	975	7.9
Maui	1,825	1,879	1,891	1,943	2.7
Eastbound Visitors by County					
Oahu	2,632	2,738	2,435	2,261	-7.1
Hawaii	348	290	309	265	-14.2
Kauai	144	151	137	117	-14.6
Maui	503	473	412	318	-22.8

Source: Hawaii Visitors & Convention Bureau, Market Research Department; Hawaii Department of Business, Economic Development and Tourism (DBEDT).

Hawaii Hotel Industry Indicators

	1996	1997	1998	1999	% Change
State of Hawaii					
Visitor accommodations	70,288	71,025	71,480	NA	—
Hotel units	49,737	53,735	54,055	NA	—
Condominium units	20,551	17,290	17,425	NA	—
Hotel occupancy (%)	75.5	74.0	72.0	73.1	1.5
Average daily room rate (\$)	127.95	135.94	140.63	142.39	1.3
Hotel rentals (\$000)	2,047.5	2,130.0	2,059.6	2,263.3	9.9
Hotel employment	38,350	38,350	37,750	37,100	-1.7
Annual wage (\$)	24,486	25,423	25,959	NA	—
Oahu					
Visitor accommodations	36,146	35,971	36,206	NA	—
Hotel units	29,732	32,002	32,178	NA	—
Condominium units	6,414	3,969	4,028	NA	—
Hotel occupancy (%)	81.6	78.6	73.8	73.1	-1.0
Average daily room rate (\$)	117.07	123.21	122.83	118.88	-3.2
Hotel employment	18,050	17,550	16,800	16,100	-4.2
Annual wage (\$)	25,570	26,628	26,687	NA	—
Hawaii					
Visitor accommodations	9,558	9,913	9,655	NA	—
Hotel units	7,170	7,922	7,413	NA	—
Condominium units	2,388	1,991	2,242	NA	—
Hotel occupancy (%)	62.2	65.4	68.2	67.4	-1.2
Average daily room rate (\$)	127.89	147.28	157.64	165.92	5.3
Hotel employment	6,000	6,550	6,600	6,450	-2.3
Annual wage (\$)	22,981	23,737	25,073	NA	—
Kauai					
Visitor accommodations	6,760	6,579	6,969	NA	—
Hotel units	3,673	3,364	4,100	NA	—
Condominium units	3,087	2,925	2,869	NA	—
Hotel occupancy (%)	67.5	68.8	67.0	72.4	8.1
Average daily room rate (\$)	137.04	148.26	154.2	159.89	3.7
Hotel employment	3,450	3,400	3,550	3,650	2.8
Annual wage (\$)	21,902	22,824	23,074	NA	—
Maui					
Visitor accommodations	16,973	17,582	17,711	NA	—
Hotel units	8,541	9,487	9,704	NA	—
Condominium units	8,432	8,095	8,007	NA	—
Hotel occupancy (%)	73.2	71.6	72.8	77.3	6.1
Average daily room rate (\$)	151.02	156.37	161.37	167.08	3.5
Hotel employment	10,900	10,850	10,800	10,950	1.4
Annual wage (\$)	24,324	25,310	26,315	NA	—
Molokai					
Visitor accommodations	481	601	570	NA	—
Hotel units	251	291	291	NA	—
Condominium units	230	310	279	NA	—
Hotel occupancy (%)	39.1	40.4	43.1	41.1	-4.8
Average daily room rate (\$)	74.21	74.02	75.46	74.54	-1.2
Hotel employment	150	150	200	200	0.0
Lanai					
Visitor accommodations	370	369	369	NA	—
Hotel units	370	369	369	NA	—
Condominium units	0	0	0	NA	—

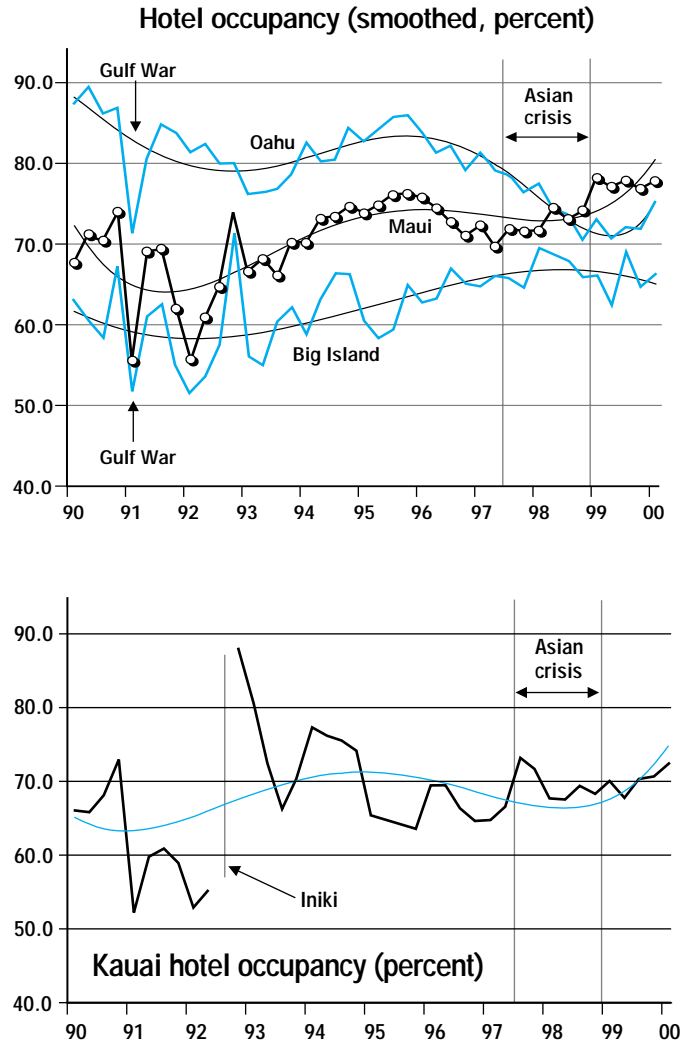
Sources: Hawaii Visitors & Convention Bureau, Pannel Kerr Forster, Hawaii Department of Taxation (adjusted), Hawaii Department of Labor and Industrial Relations

in Japanese visitor days to 6.9 percent. The 7 percent decrease in 1999 Japanese visitor counts is expected to be replaced by a small turnaround during 2000.

The overall eastbound count to Hawaii was down 5.9 percent in 1999, to 2.35 million from 2.49 million in 1998. Asian air lift dropped sharply, 9.3 percent, as Asian air carriers adjusted to the aftermath of the regional economic crisis. Despite a decrease in eastbound travel across the entire state, a performance footnote managed to squeak through during 1999. Eastbound visitors traveling only to neighbor island destination increased by nearly 47 percent during 1999. This group still numbers less than 4 percent of the eastbound market (i.e. 96 percent of eastbound visitors still visit Oahu, and 74 percent visit only Oahu).

The Asian crisis tended to have a generally adverse impact on neighbor island eastbound travel between 1998 and 1999. The proportion of eastbound visitors spending some time on the neighbor islands fell from 28.4 percent to 26.3 percent between 1998 and 1999. Maui lost about 3 percentage points (from 16.5 percent to 13.9 percent), while Big Island and Kauai shares were more stable (from 12.4 percent to 11.3, and from 5.5 percent to 5.0 percent, respectively). Interestingly, the aftermath of Asia's economic crisis—at least from 1999 performance indicators—seems to have been more of a retrenchment in Asian travel patterns back to a traditional destination: Oahu. Oahu's visitor count decreased 7.2 percent under the weight of Asia's 1997-98 recession and nascent recovery in 1999. However, the compression for neighbor islands from Asia's economic turbulence was more severe: a 12.8 percent decrease for neighbor island destinations as a whole in 1999, and a 18.5 percent drop in multiple-island travel in the eastbound market segment. Compounding this decline was a 2.5 percent decrease in eastbound average length of stay. Total eastbound visitor days, as a result, fell 8.3 percent in 1999.

Several forces come together to paint a rosier picture for tourism in 1999. Capacity utilization in the hotel sector has been rising because of growth in the longer length-of-stay westbound market, especially for the neighbor islands. This means higher revenues, profitability and upward pressure on room rates for 2000. Virtually no new hotel inventory has been created in half a decade, although timeshare (interval ownership) development seems to have caught the wave from rising mainland household wealth. Bookings at the Hawaii Convention Center are starting to build, and recent conventions have been a successful validation of the concept that both

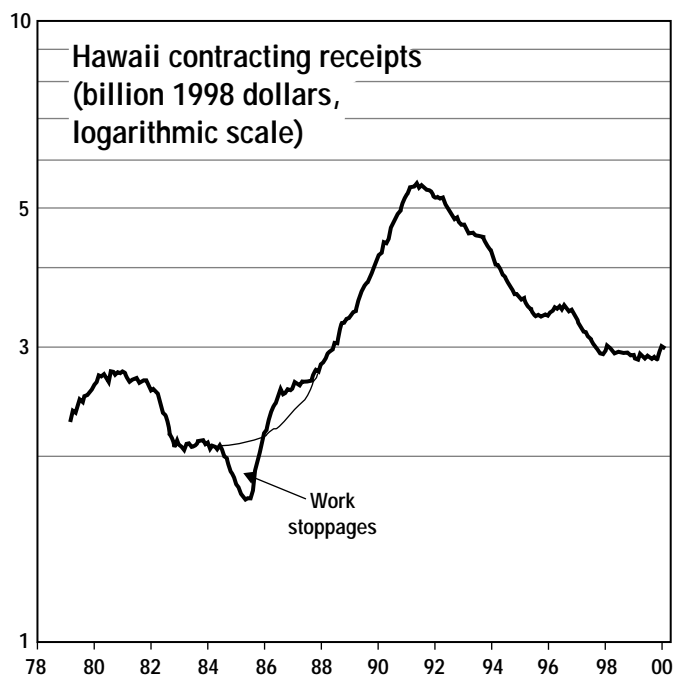


Waikiki and neighbor island destinations have the potential of win-win outcomes with the state government's investment in the convention facility. Economic strength in North America, and the emerging recovery in Asian markets, point to an improving foundation for travel demand. Travel supply is being expanded by airlines serving the North American markets, at least. Finally, the dedication of significant promotional and marketing resources toward generic destination awareness building and advertising, combined with the culmination of a decade-long investment "boomlet" in retail development, add two more ingredients to the positive outlook. Tourism in Hawaii will rise to record levels in 2000, setting a course through previously uncharted territory for a future with greater opportunity than ever before.

HAWAII 1999: ANNUAL ECONOMIC REPORT

Investment

The difference between the modest growth Hawaii has experienced the last two years, and the more robust growth that seems imminent, will be determined by the pace of construction and investment activity. Tourism has proven to be the customary engine of recovery, but it is the investment cycle that has distinguished Hawaii's business cycles in the past. The deep cyclical decline in Hawaii construction during the 1990s means that new hotel inventories, housing and some



classes of commercial space are in shorter supply. In 1999 construction indicators gave clear signs of turning the corner, with a sharp 27.5 percent increase in the dollar volume of building permits issued for new construction leading a 4.6 percent rebound in contracting

Construction in Hawaii

(In million dollars, or as noted)	1996	1997	1998	1999	% Change
Total Construction Completed	3,239.9	2,893.6	2,956.4	3,091.7	4.6
Private Building Permits	1,157.8	1,196.6	1,087.0	1,386.2	27.5
Residential	660.3	694.2	621.4	769.6	23.8
New single-family dwellings	396.5	370.0	427.4	536.4	25.5
New multifamily dwellings	108.1	187.4	57.0	93.0	63.2
Additions & alterations	155.7	136.9	137.1	140.2	2.3
Nonresidential	497.4	502.4	465.6	616.7	32.5
New hotels	0.5	19.3	5.9	50.9	765.1
New manufacturing buildings	19.7	26.2	22.6	23.2	2.4
New office buildings	35.6	38.6	5.0	17.0	237.6
New utility buildings	0.6	2.7	2.3	0.0	-98.9
New mercantile buildings	28.1	37.4	27.9	42.6	52.8
New miscellaneous buildings	152.8	138.6	141.0	169.9	20.5
Additions & alterations	260.1	239.6	260.9	313.1	20.0
Government Construction Contracts					
Bid openings and contract awards	961.8	834.9	NA	NA	—
State government agencies	526.0	357.5	NA	NA	—
City & County of Honolulu	85.8	153.3	NA	NA	—
Neighbor Island counties	61.9	NA	NA	NA	—
Federal agencies	288.2	322.6	NA	NA	—
Construction Job Count (number)	23,450	22,300	21,650	21,550	-0.5
Cement Consumption (thousand tons)	348.9	279.9	NA	NA	—
Housing Units Authorized (number)	4,096	4,257	3,360	4,358	29.7
Private single-family units	2,954	2,659	2,830	3,335	17.8
Private multifamily units	1,142	1,598	530	1,023	93.0

Source: Economics Department, Bank of Hawaii

COMPARATIVE HAWAII FORECASTS FOR 1999-2000

1999-2000 Hawaii Forecasts (annual percent changes; blanks are not)	Personal Income						Visitor Arrivals		CPI		Gross State Product				Construction	
	Jobs		(Nominal)		(real)				Honolulu	Honolulu	(nominal)		(real)		(real)	
	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001	2000	2001
Paul Brewbaker, Bank of Hawaii ¹	1.2	1.5	4.5	6.0	3.0	3.5	3.5	3.0	1.5	2.5	4.5	6.0	3.0	3.5	10.0	15.0
Byron Gangnes & Carl Bonham, University of Hawaii Economic Research Organization (UHERO) ²	1.5		4.4		2.6		4.0		1.8		4.4		2.6		5.0	
Pearl Imada-Iboshi, Hawaii Department of Business, Economic Development and Tourism ³	2.0	1.7	5.5	5.0	3.5	3.0	3.8	3.5	2.0	2.0	5.4	4.9	3.5	3.0		
Leroy Laney, Hawaii Pacific University ⁴	0.5		3.5		2.3		3.5		1.2		3.7		2.5			
Council on Revenues consensus ⁵	NA	NA	4.3	4.7	2.4	2.6	3.2	3.1	1.9	2.1	4.1	4.4	2.2	2.3	4.7	6.2

Source: As noted below, updated from the April 2000 Hawaii Economic Association Conference on Current Economic Issues

Notes:

¹Revised March 31, 2000 in preparation for publication of "Hawaii 1999: Annual Economic Report" www.boh.com/econ/

²Vector-autoregressive model (VAR) (April 27, 2000); www2.hawaii.edu/~uhero/

³DBEDT Quarterly Forecast (June 30, 2000) www.hawaii.gov/dbedt/forecast.html

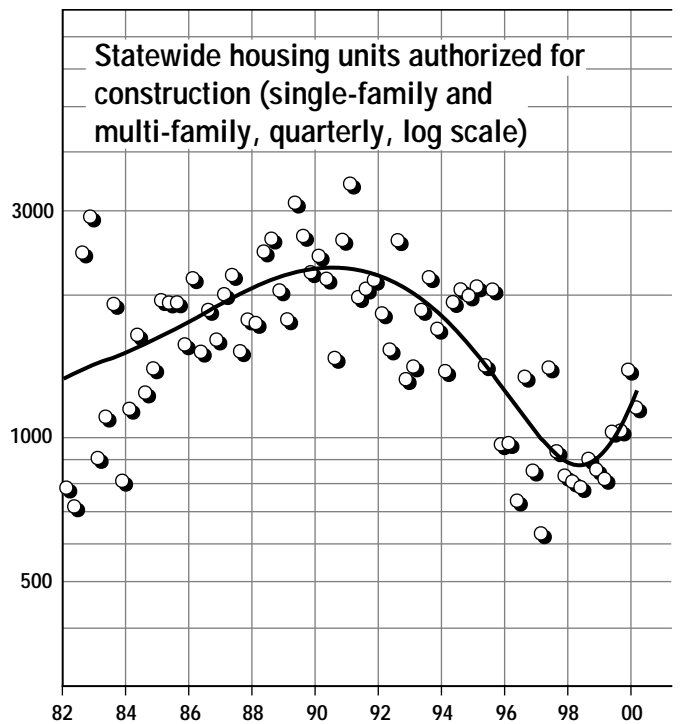
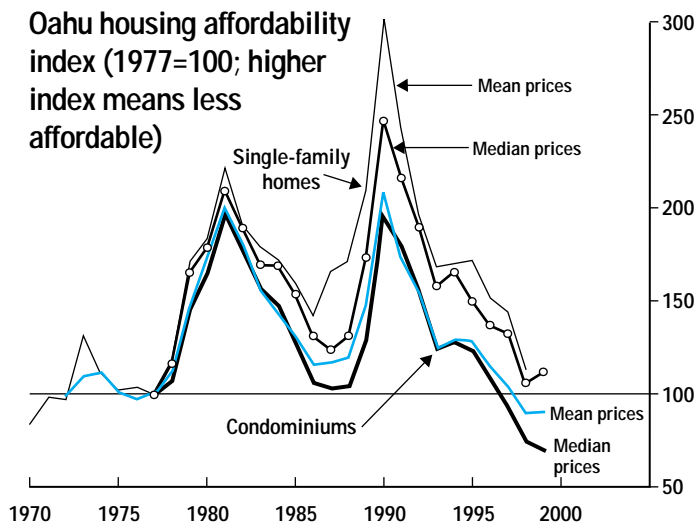
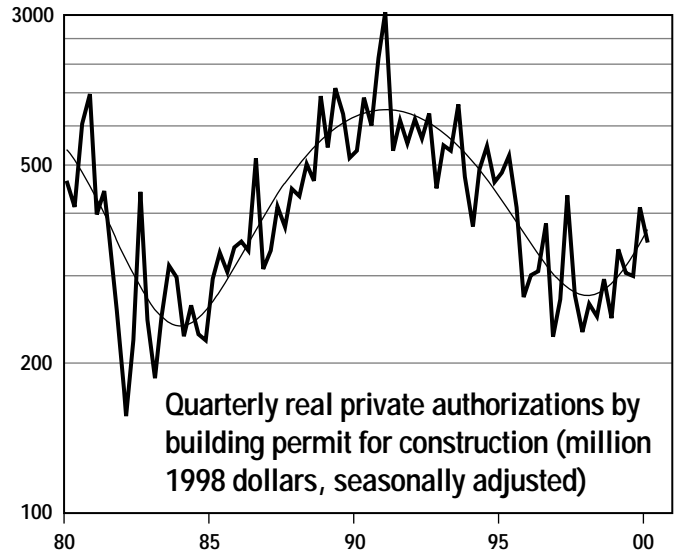
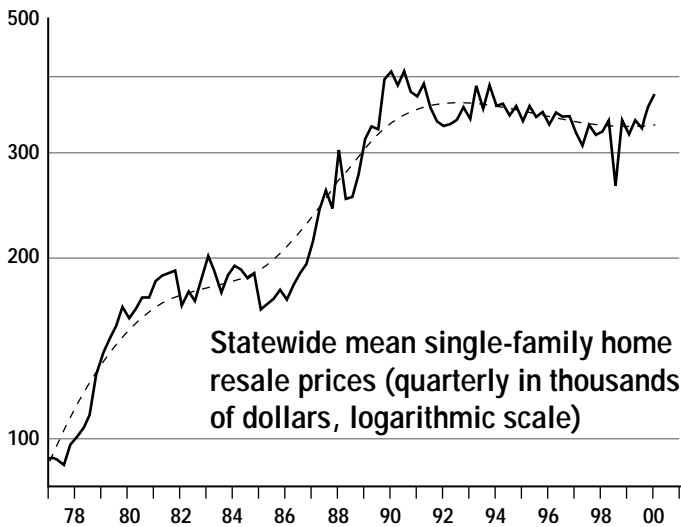
⁴Updated at the HEA conference

⁵Council on Revenues May 18, 2000 revenue forecast assumptions

receipts. Construction employment followed suit, rising 12 percent in May 2000 from one year earlier. Developers and institutional investors are moving ahead with plans for the next generation of resort properties and housing projects.

Part of the reason why construction has rebounded is the recent influence of US West Coast investors in Hawaii real estate, who perceive that the differential between Hawaii and California properties will be closed by appreciation of Hawaii values. As with housing cycles of the past, the affordability window created by stable housing costs in recent years seems

likely to begin closing in 2000, because historically developers have been unable to raise housing production fast enough to turn back the cyclical rise in home prices. It seems likely these cyclical dynamics will unfold in the customary pattern during the next several years, as construction and investment feed Hawaii's economic acceleration.



Bank of Hawaii

Visit Bank of Hawaii's Internet website at <http://www.boh.com/econ> for more information on the economy of Hawaii as well as analyses of business trends in the state and the Pacific region.

Other Bank of Hawaii economic publications include Pacific islands reports on the economies of: Samoa and American Samoa, Commonwealth of the Northern Mariana Islands, Federated States of Micronesia, Fiji, French Polynesia, Guam, New Caledonia, Republic of the Marshall Islands, Palau,

Solomon Islands, and Vanuatu.

This report was researched and written by Paul H. Brewbaker, Chief Economist; Sterling Nakano, Senior Analyst; Tanner Fahl, summer intern, Investments Division, Treasury Group. Additional hard copies of *Hawaii 1999 Annual Economic Report* (ISSN 1043-6685) can be ordered by contacting Bank of Hawaii, Corporate Communications Department, PO Box 2900, Honolulu, Hawaii 96846. Phone: 808-537-8246, Fax: 808-537-8440.

Bank of Hawaii Managing Committee

Lawrence M. Johnson, Chairman of the Board and Chief Executive Officer
Richard J. Dahl, President and Chief Operating Officer
Alton T. Kuioka, Vice Chair and Chief Lending Officer
Mary P. Carryer, Vice Chair
David A. Houle, Executive Vice President, Treasurer and Chief Financial Officer
Karl K.Y. Pan, Executive Vice President

Bank of Hawaii Website

www.boh.com

Bankoh By Phone

Ph: 1-888-643-3888

24 hours a day, 7 days a week

Toll-free from anywhere in Hawaii (including Oahu),
the U.S. Mainland, Guam, Saipan or Canada

Private Client Services Division

808-537-8914

Trust Division

808-538-4444

Asset Management & Institutional Services

808-538-4431

Hawaii Commercial Banking Division

808-537-8775

Visitor Industry

808-537-8775

Commercial Real Estate Loan Division

808-537-8261

Mortgage Banking Division

808-693-1389

Consumer Products Division

808-537-8711

Business Products Division

808-537-8678

E-Commerce Development Group

808-538-4828

Electronic Banking Division

808-537-8190

Bankoh Insurance Agency, Inc.

a subsidiary of Bank of Hawaii

808-845-2271

Pacific Century Leasing, Inc.

a subsidiary of Bank of Hawaii

808-537-8198

Pacific Century Investment Services, Inc.

a subsidiary of Bank of Hawaii

808-537-8500

Corporate Communications

808-537-8246

South Pacific Banking Division

808-537-8223

West Pacific Banking Division

671-479-3625

East Asia Division

808-537-8486

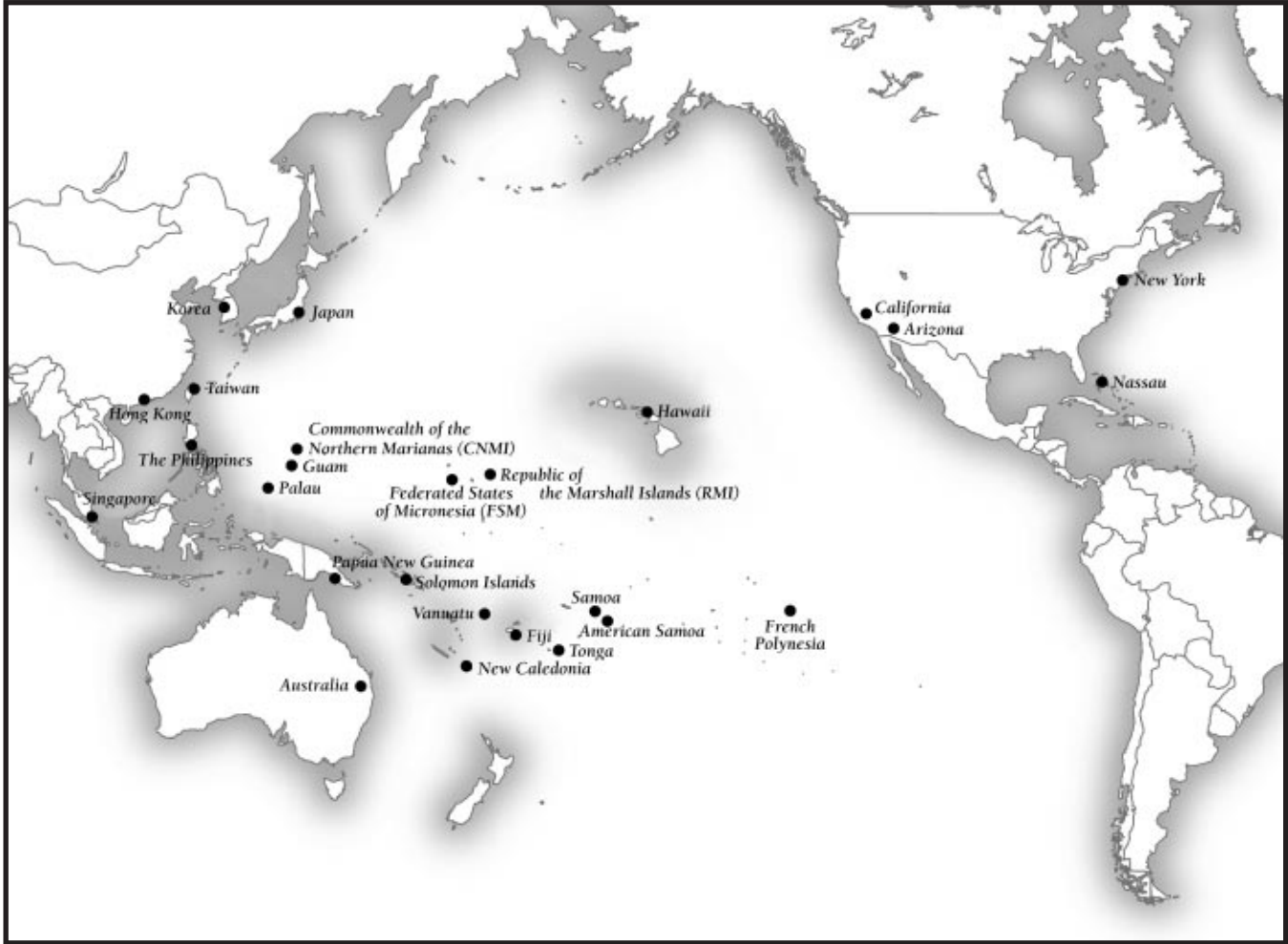
Corporate Banking Division

808-537-8017

Pacific Century Bank, N.A.

(Los Angeles, CA) 818-907-9122

(Phoenix, AZ) 602-257-4440



Hawaii

- Bank of Hawaii (76 branches)

Arizona

- Pacific Century Bank, N.A. (9 branches)

California

- Pacific Century Bank, N.A. (19 branches)

West Pacific

Commonwealth of the Northern Marianas Islands (CNMI)

- Bank of Hawaii (2 branches)

Federated States of Micronesia (FSM)

- Bank of Hawaii (3 branches)

Guam

- Bank of Hawaii (3 branches)
- First Savings and Loan Association of America (3 offices, 4 in-store branches)

Republic of the Marshall Islands (RMI)

- Bank of Hawaii (1 branch)

Republic of Palau

- Bank of Hawaii (1 branch)

South Pacific

American Samoa

- Bank of Hawaii (2 branches)

Fiji

- Bank of Hawaii (3 branches)

Subsidiary Banks

French Polynesia

- Banque de Tahiti (17 branches)

New Caledonia

- Bank of Hawaii - Nouvelle Calédonie (8 branches)

Vanuatu

- Banque d'Hawaii (Vanuatu), Ltd. (2 branches)

Papua New Guinea

- Bank of Hawaii (PNG), Ltd. (2 branches)

Affiliate Banks

Samoa

- Pacific Commercial Bank, Ltd. (4 branches)

Tonga

- Bank of Tonga (5 branches)

Solomon Islands

- National Bank of Solomon Islands (11 branches)

Alliances

Australia

- Bank of Queensland Limited (94 branches)

International Offices/Branches

Hong Kong

- Bank of Hawaii (1 branch)

The Philippines

- Bank of Hawaii
1 representative office,
2 extension offices

Nassau

- Bank of Hawaii (1 branch)

New York

- Bank of Hawaii International Corporation, New York

Korea

- Bank of Hawaii (1 branch)

Singapore

- Bank of Hawaii (1 branch)

Taiwan

- Bank of Hawaii (1 branch)

Japan

- Bank of Hawaii (1 branch)

Opening a world of opportunity

Founded in 1897, Bank of Hawaii is the largest commercial bank in Hawaii and the principal subsidiary of Pacific Century Financial Corporation, a \$14.3 billion regional financial services holding company. With over 180 locations in our trans-Pacific network, Bank of Hawaii provides a full range of financial services to consumers, businesses and governments in four principal markets: Hawaii, the West and South Pacific, Asia and selected markets on the U.S. Mainland.

Whether you're interested in consumer or business banking services, private client services, investments, trusts, estate planning, insurance, leasing, and more, we're here to help you. Our goal is to provide you with easy, convenient, "24x7" access to financial services through our branches, the Internet, Bankoh BankMachines (ATMs), and Bankoh by Phone. For more information, please visit our website at www.boh.com.

We Built This City.

Okay, maybe not all of it. But more than 5,000 architectural projects in Hawaii and around the world were designed by Architects Hawaii. Including the Hawaii State Capitol, some of the tallest high rises, and the most complex multi-use projects.

Today, Hawaii's leading architectural design firm engages in projects that span the Pacific, from Japan, Hong Kong, and Singapore to the Golden State of California.

For 54 years, we've built a reputation for creative projects that capture a sense of place, culture, and purpose. After all, isn't that what creating a great city is all about?

What architecture can we create for you?

Pacific Tower, Suite 300 • 1001 Bishop St • Honolulu, Hawaii 96813
Ph. 808.523.9636 • www.architects-hawaii.com

ARCHITECTS
H A W A I I
L I M I T E D



*Castle & Cooke Homes Hawaii and Bank of Hawaii.
Helping to build your dreams.*

For years, Castle & Cooke Homes Hawaii has been the islands' premier land developer. Together with Bank of Hawaii, we've helped more people move into new homes than anyone else.



Castle & Cooke Homes Hawaii



95-1091 Ainamakua Drive, Mililani, Hawaii 96789 808-626-1133 www.castle-cooke.com



Keeping Hawaii on the move for 25 years.

Cutter Ala Moana Volkswagen Mazda
800 Ala Moana Blvd., Honolulu ~ 585-7777

Cutter Ford Isuzu
98-015 Kam Hwy., Aiea ~ 487-3811
94-081 Farrington Hwy., Waipahu ~ 678-9870

Cutter Chevrolet
1391 Kapiolani Blvd., Honolulu ~ 946-8311
3060 Kapiolani Blvd., Honolulu ~ 737-0500



Family Auto Centers

Cutter Dodge Chrysler Plymouth Jeep
735 Dillingham Blvd., Honolulu ~ 842-6300
905 Kam Hwy, Pearl City ~ 453-1111
94-149 Farrington Hwy., Waipahu ~ 671-4991

Cutter Maui Nissan Hyundai Mitsubishi
25 S. Kahului Beach Rd., Kahului, Maui ~ 877-9009

Cutter Maui Family Auto Center
260 Hana Hwy., Kahului, Maui ~ 877-2066

HAWAII. YOUR HOME. OUR BUSINESS.

Global Reach. With over 4,900 professionals in 52 Countries on 6 Continents, Colliers' international exposure and expertise enables us to work closely with foreign investors around the globe.

Leasing & Sales. Colliers Monroe Friedlander was founded over 27 year ago. Since then we have acquired a reputation for excellence in servicing a broad range of commercial and industrial real estate clients. We can find the right space for you.

Investments. Colliers Monroe Friedlander provides full commercial investment services to investors in the acquisition, management and disposition of commercial and industrial properties.

Management. Our commercial and industrial real estate management company recognizes that every owner and each property has specific needs and requirements. Our expertise, knowledge & technology can maximize the value of your real estate investment.

Additional Services.

Retail Services ~ Leasing & Sales
Office Services ~ Leasing & Sales
Industrial Services ~ Leasing & Sales
Consulting & Research
Hotel Sales
Golf Course Sales



220 South King Street, Suite 1800
Honolulu, Hawaii 96813
Phone 808.524.2666 Fax 808.521.0977
www.colliers.com/honolulu



Individual Memberships

Commercial, Industrial & Investment Real Estate Services Since 1973