

Economics Group

Special Commentary

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Colorado Economic Outlook: August 2018

Colorado is Helping Drive the Acceleration in U.S. Economic Growth

The recent acceleration in economic growth is readily apparent in Colorado, where GDP growth has outpaced the nation for the past 7 quarters. The improved economic outlook reflects a reversal of momentum from the state's energy sector and a bit of an increase in construction activity. Fiscal policy has also turned more accommodative, with tax cuts giving households a boost and increased defense budgets helping Colorado's defense sector. International trade remains a question mark, however. Stronger global economic growth has boosted exports but contentious trade negotiations may slow exports in coming quarters, potentially impacting manufacturing and agriculture.

Real GDP grew 3.0 percent at an annual rate in Colorado during the first quarter and has risen 4.5 percent over the past year. The Centennial State has consistently outpaced the nation in recent quarters and we suspect that Colorado's real GDP growth once again topped the nation in the second quarter, when the nation's real GDP grew at a 4.1 percent pace. Nonfarm employment has risen 2.8 percent over the past year, while the unemployment rate has remained at an exceptionally low 2.7 percent. Colorado's tight labor market challenges companies looking to expand. Unfilled jobs exceed available talent in many markets. Moreover, high housing costs may be discouraging net migration, although an apartment building boom should curb the relentless rise in rents.

Colorado's economy has outpaced the nation for the past 7 quarters.

Colorado's highly skilled workforce makes the state a top destination for expanding tech companies. Millennials are still in love with Denver, if they can afford to live there. Denver's high housing costs have encouraged residents to migrate to other parts of the state. With its lower relative housing costs, Colorado Springs is one of the beneficiaries of this shift and recent data show it has become a millennial magnet in its own right. The Greeley MSA, in Northeast Colorado, posted one of the strongest job gains in the country over the past year, reflecting increased energy production.

Figure 1

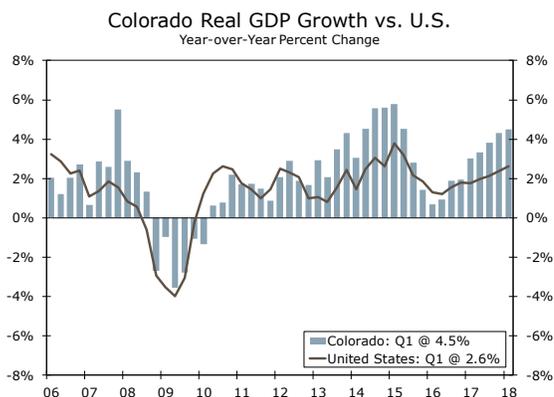
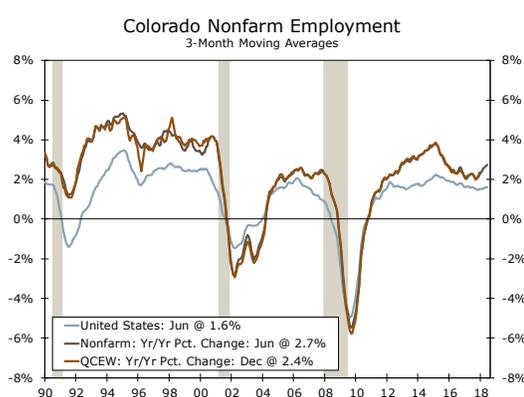


Figure 2



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Securities



Colorado's Job Engine Up and Running

Colorado's job growth moderated throughout much of 2017 but has perked up during the first half of 2018. Total nonfarm payrolls have increased by 74,600 jobs over the past year. That gain represents a 2.8 percent increase, making Colorado the nation's fifth fastest growing job market, behind Utah, Idaho, Nevada and Texas. Colorado's robust nonfarm job growth is even more impressive considering the state has one of the tightest labor markets in the country, with a seasonally-adjusted unemployment rate of just 2.7 percent in June. The Centennial State is tied with Iowa and New Hampshire for the second lowest unemployment rate, behind Hawaii.

Employment has risen solidly across nearly every major category over the past year. The leisure and hospitality sector posted the largest gain, adding 15,200 new jobs year-to-year, on a three-month average basis. Colorado enjoyed a record tourism season this past year, hosting 84.7 million visitors, up 2.8 percent from the prior year. The gains are evident both at the ski resorts and in Denver, which is the state's top tourist destination. The growth in tourism is helping fuel hotel construction, driving demand for restaurants and fueling a major expansion at the Denver International Airport.

Providers of professional and business services added 17,600 jobs this past year, with the gain roughly evenly distributed between professional and tech positions and administration and support. Professional and tech captures Colorado's thriving tech sector, defense contractors and life sciences, and the most recent increase is the largest this subcategory has seen since 2015.

Hiring has also perked up outside Colorado's services sector. Mining payrolls posted the largest percentage increase, with hiring surging 15 percent over the past year and 3,200 jobs being added. Despite the increase, Colorado's mining and logging sector has recovered less than half of the positions cut since employment peaked back in 2014. The energy sector has become much more efficient and the industry is producing more oil and gas with far fewer workers than it did earlier in the decade. Construction employment has risen 4.9 percent, or by 7,900 jobs, and manufacturing payrolls are up 1.9 percent, or by 2,700 jobs.

All ten of Colorado's large counties, those with 75,000 or more jobs, saw payrolls rise faster than the nation in 2017. Weld County has consistently ranked among the fastest growing counties in the nation over the past year, with 5.2 percent year-to-year growth claiming the number six spot for 2017. Most of the areas ahead of Weld County were also in the energy patch, mostly in Texas. Adams County, northeast of Denver where the airport is located, also made the top ten list of the nation's fastest growing counties in 2017, with its 5.1 percent payroll growth coming in eighth. Douglas County, located between Denver and Colorado Springs, posted the fourth fastest growth in average weekly wages over the year, with the \$108 per week increase being the fifth largest change in the nation, behind only counties in New York City and the San Francisco Bay Area.

Colorado continues to add jobs at a rapid rate, despite maintaining an extremely low unemployment rate.

The energy sector has largely recovered, but is now much more efficient, meaning relatively fewer workers are needed to ramp up production.

Figure 3

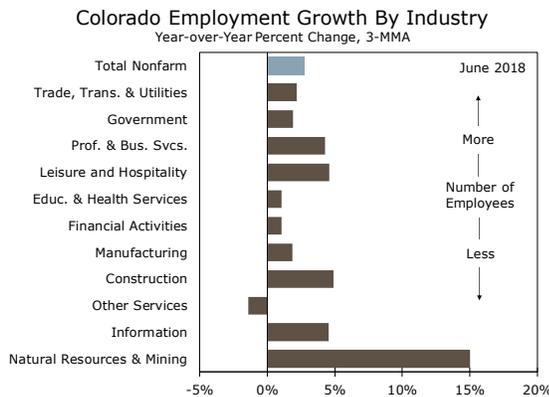
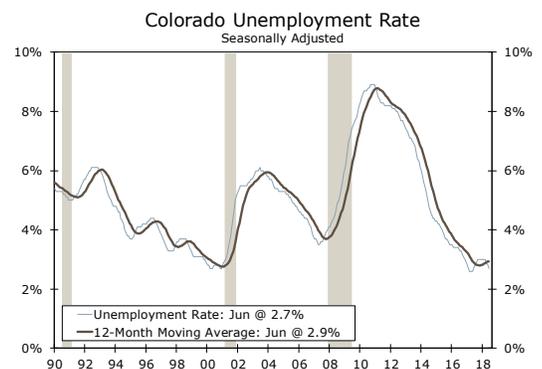


Figure 4



Source: U.S. Department of Labor and Wells Fargo Securities

Home on the Front Range

Colorado’s population growth moderated in 2017. Echoing the trend in 2016, the state received less of a lift from domestic net migration, or the difference between the number of people moving to and the number moving away from Colorado. Fewer Americans have chosen to move as the decade has progressed. The mover rate fell to just 11 percent of the population in 2017, down from 11.2 percent in 2016 and 16.5 percent back in 1997. Colorado’s popularity has slipped among those that chose to move, sliding from the third largest gainer from domestic net migration in 2015 to 11th this past year. The slide likely is due to Denver’s higher housing costs. Domestic migration accelerated in states with more affordable homes for sale, such as Arizona, Idaho and Nevada in the West; as well as North Carolina, Georgia and Tennessee in the South.

Fewer people are moving to Colorado, as soaring housing costs are making other areas look more attractive.

Much of the moderation in Colorado’s population growth is due to fewer people relocating to the Denver area. Denver was among the top ten largest metro areas in terms of domestic migration during the first half of the decade, but fell to 18th in 2017. The Mile High City served as a beacon for millennials in particular, as the metro area’s 20 to 34 year old population grew by 83,162 from 2010 to 2016, which was the tenth largest gain in the nation. That growth fueled an apartment building boom, with luxury or life-style units accounting for most of the increase. Denver’s attraction to millennials may be hampered in coming years by skyrocketing housing costs. While job and income growth have also been strong, many younger persons are still struggling to save for a down payment, particularly with home prices rising so rapidly. Colorado Springs is emerging as a nearby alternative. The Colorado Springs metropolitan area, which has a total population of roughly 712,000, has seen its population aged 20 to 34 increase 19.3 percent since 2010—which marks the largest percentage gain of any metro area, and equal to about 27,000 millennials, using data from the American Community Survey.

The space between Denver and Colorado Springs, located along I-25, is booming, particularly Castle Rock. Once a ranch community marking the half-way point between Denver and Colorado Springs with fewer than 8,000 residents in 1990, Castle Rock is now a bustling town of over 62,000 residents. Since just 2003, the population has essentially doubled. Castle Rock was the nation’s seventh fastest growing city in 2017, adding 3,000 residents and growing 5.1 percent. Castle Rock’s 3,000-person gain was the fourth largest of any city or town in Colorado. Only Denver, Colorado Springs and Aurora had larger population gains. Castle Rock’s rapid growth can partially be attributed to its proximity to jobs in Denver and the surrounding areas in Douglas County, of which Castle Rock is the county seat. Douglas has been one of the fastest growing counties in terms of job growth and posted the fourth fastest pace of average weekly wage growth in the nation in Q4 2017. Homes in Douglas County are less affordable than in Denver, as Douglas County is one of the wealthiest counties in the nation.

The city of Castle Rock has seen its population surge in recent years.

Figure 5

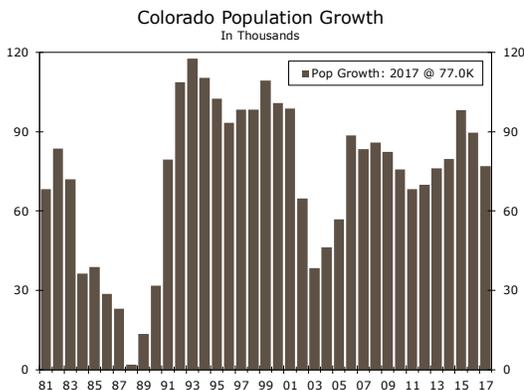
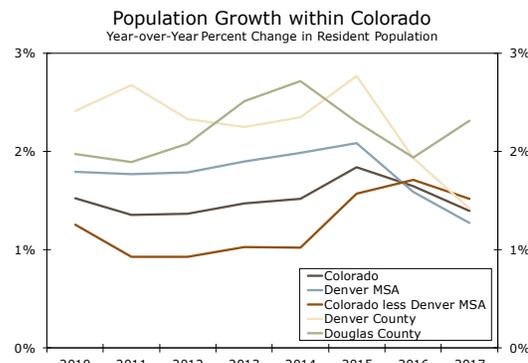


Figure 6



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Securities

Energy production and employment have picked up along the Front Range.

Oil & Gas Drilling Are Providing a Boost

Colorado’s economy is blessed with an abundance of natural resources, and technological advances have allowed more of these resources to be brought to market in recent years. The active rig count is hovering in the low 30s, twice the number at the trough in 2016 but well below the 70 rig range averaged in 2014. Employment has perked up, with hiring in the mining and logging sector surging 15 percent over the past year. Employment in the sector, however, remains well below its all-time peak hit earlier this decade. Drilling applications have surged this year. The increase reflects higher oil prices, improved drilling technologies and possibly some concern that this year’s national and statewide elections might usher in a more restrictive environment for oil and gas production.

Much of Colorado’s oil and gas production occurs along the Front Range, which is where the majority of the state’s population resides. Weld County, located in the Northeast corner of the state, is the most energy-intensive county in the state and has seen employment surge this past year. Colorado has also made huge inroads into alternative energy. Several wind power projects were put into place earlier in the decade and Colorado ranks ninth nationally in terms of generating wind energy. There has also been a great deal of growth in solar energy, although tariffs on imported solar panels are believed to have slowed growth this past year.

A good part of Colorado’s strong economic performance can be tied to the growth of its high tech sector. Colorado’s well-educated workforce is a big draw to tech companies looking to expand. The state has seen an influx of companies from California in recent years, including Google, Marketo, Slack, Xactly, Guild Education and OpenTable. The influx of established firms enhances an already vibrant tech ecosystem that has produced a number of notable rapidly growing businesses, including Ibotta, Convercent and SendGrid. The growing base of technology companies in Denver, and all along the Front Range, has made the region a top destination for tech workers. The real estate firm CBRE ranks Denver as the nation’s tenth largest tech market, with just under 100,000 workers employed in the tech sector or about 6.2 percent of the workforce.

The high tech, defense and aerospace sectors continue to attract new investment and skilled labor.

Colorado’s defense and aerospace industry is another source of high-quality job growth. Colorado has the second largest number of workers employed in the aerospace industry, behind California. Much of the industry is in the Colorado Springs area, which is home to five military installations, including The Air Force Academy, NORAD and Peterson Air Force Base, home of the Space Command. The concentration of defense and aerospace facilities has attracted hundreds of contractors, including Boeing, Lockheed Martin, Raytheon and Northrop Grumman. With defense budgets growing, the aerospace industry will continue to expand. Recent expansions include Polaris Alpha, which recently announced plans to add 450 jobs over the next eight years to its operations in Denver and Colorado Springs; and Ball Aerospace, which is adding 145,000 square feet of space to its manufacturing center in Westminster.

Figure 7

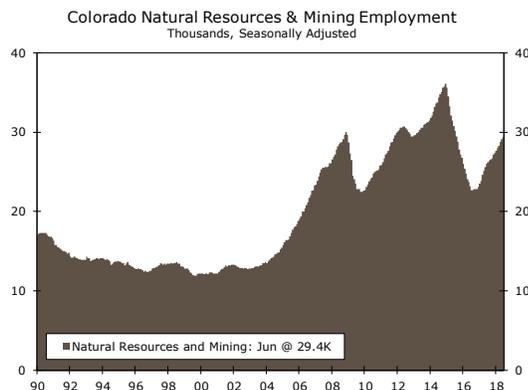
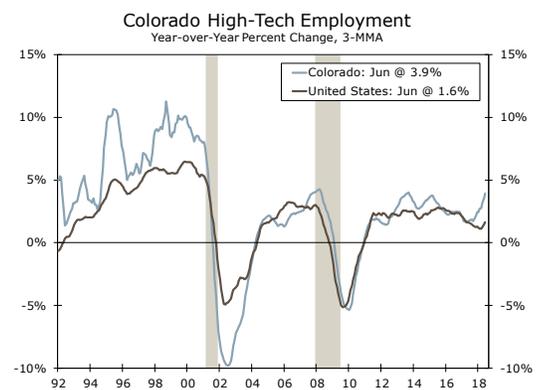


Figure 8



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Securities

High Home Prices Follow Californians Back to Colorado

The cost of housing has become a major issue in Colorado. Years of rapid population growth, much of it in the form of relocation from California and other high-priced parts in the West, have pulled home prices up at a much faster rate than the nation as a whole. Many of these new residents have come flush with dollars from the sale of higher-priced homes in California or Seattle or simply have a different perspective on what is expensive. Construction has also lagged behind population growth. Home prices are rising nearly three times faster than income in the Centennial State, which has caused affordability to plummet. The situation will worsen as the Fed raises interest rates. Moreover, saving for a down payment is proving difficult for many younger households that moved to Denver earlier this decade because so much of their income is needed to cover rent and repay college loans.

Colorado's home price appreciation accelerated in the first half of 2018. The latest data show home prices rising 8.5 percent over the past year. Rents have also outpaced incomes. Denver has seen a great deal of apartment construction but most of the development has been at the high end of the market, where rents have eased somewhat. Harvard University's Joint Center for Housing Studies notes that about one quarter of Denver area residents spend more than 30 percent of their income on rent, leaving relatively little to spend elsewhere or save. The proportion spent on rent is even higher for lower income households.

While price appreciation has cooled from its earlier double-digit pace, finding a starter home in Denver remains difficult. Years of strong job growth and limited construction have left potential buyers with few viable choices. The median price of a home sold in Denver in May was \$411,270, an increase of 8.6 percent over the past year, according to CoreLogic. Price growth in Boulder has also moderated, with the median existing home sold rising 6.7 percent to \$499,125 in 2017.

While Colorado Springs' median home price rose faster than Denver's, climbing 9.3 percent over the past year, it rose from a lower base. The median price of a home sold in Colorado Springs during May was \$300,203, according to CoreLogic. The region also saw an increase in supply of homes for sale over the past year, contrasting with Denver, where current inventory is the lowest on record. With more homes available for sale and at lower prices, Colorado Springs has seen population growth accelerate even as population growth has moderated statewide. Millennials are increasingly moving to Colorado Spring as they are priced out of Denver and Boulder.

Higher home prices and rents are spurring new construction. Single-family homebuilding has also picked up steam, with single-family permits running 26.6 percent ahead of last year, on a year-to-date basis in June. Building is up through June in Denver, Colorado Springs, Pueblo, Greeley and Grand Junction but down in Boulder and Breckenridge.

Many new Colorado residents have come flush with dollars from the sale of higher-priced homes in California or Seattle.

New construction has picked up, but still lags population growth, pressuring affordability.

Figure 9

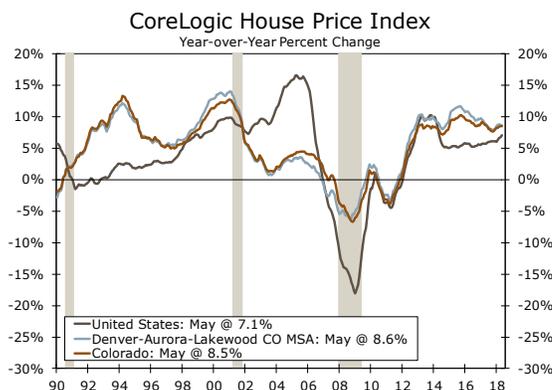
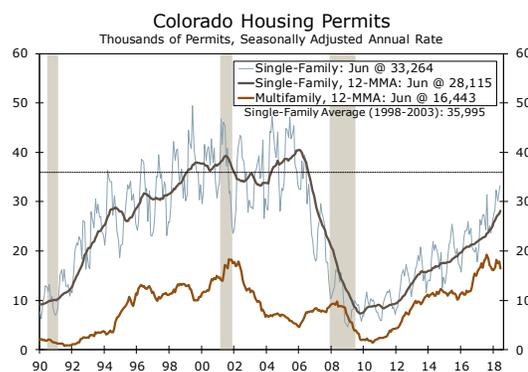


Figure 10



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Securities

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