

ECONOMIC OUTLOOK

The nation and California entered 2009 at the peak of what would become the worst recession since the Great Depression. Monthly job losses were high and increasing, unemployment was increasing at an alarming rate, and national economic output was plummeting. Credit was scarce and few financial markets were operating normally. Equity markets had stabilized after plunging in October 2008, but would soon slump again. While there are no official quarterly output series for state economies, the variables for which there are California versions were clearly showing that California was not spared in any of this.

Rightly alarmed, policy makers took quick and comprehensive action to address the rapidly declining national economy. Results came quickly. Job losses began to slow in the nation and California in the first quarter of 2009. After plunging in the fourth quarter of 2008 and the first quarter of 2009, national economic output fell only slightly in the second quarter and then increased moderately in the third quarter.

A more serious crisis was averted at great cost, but much more remains to be done. Some economists believe that the recession ended in June 2009. If so, the ranks of the unemployed increased from about 7.5 million to 14.7 million in the nation and from 1.1 million to more than 2.2 million in California during the recession. This must be remedied for prosperity to be restored. It could be a long recovery for the nation and California.

The outlook for the national economy is for modest growth in 2010, moderate growth in 2011 and 2012:

- Real Gross Domestic Product (GDP) is projected to grow by 2.2 percent in 2010 and 2.9 percent in 2011 and 2012, as compared to falling by 2.5 percent in 2009 and the 2.9-percent average growth rate from 1988 to 2008.
- Nonfarm payroll employment is forecast to fall by 0.9 percent in 2010, and grow by 1.7 percent in 2011 and 2.2 percent in 2012, as compared to a decline of 3.8 percent in 2009 and the 1.4-percent average growth rate from 1988 to 2008.

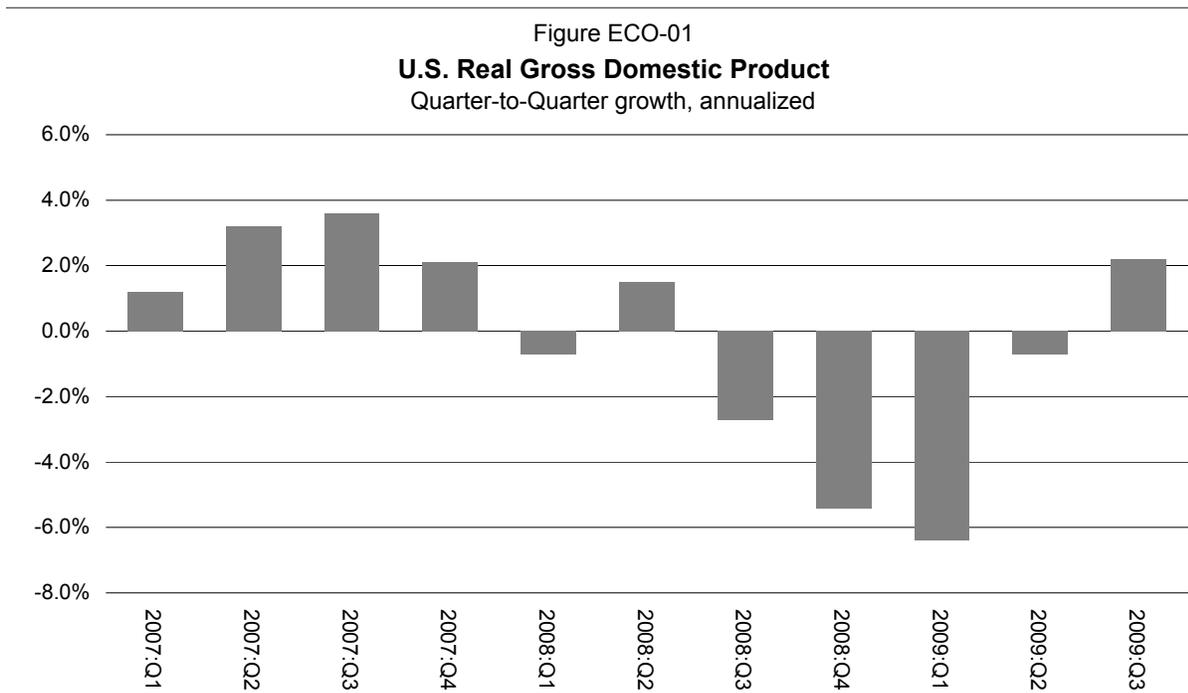
The outlook for the California economy is modest growth in 2010 followed by moderate growth in 2011 and good growth in 2012:

- Personal income is projected to grow 2.4 percent in 2010, 3.6 percent in 2011, and 4.8 percent in 2012, as compared to falling by 2.8 percent in 2009 and the 5.6-percent average growth rate from 1988 to 2008.
- Nonfarm payroll employment is forecast to fall by 0.7 percent in 2010 and grow by 1.3 percent in 2011 and 1.9 percent in 2012, as compared to falling by 5.6 in 2009 and the 1.3-percent average growth rate from 1988 to 2008.

THE NATION – DIGGING OUT OF THE HOLE

Output of the national economy grew by a 2.2-percent annual rate in the third quarter of 2009 (Figure ECO-01). It was the first gain since the second quarter of 2008. In between were consecutive quarters with a cumulative decline of almost 12 percent, the fourth quarter of 2008 and the first quarter of 2009. In the entire series of quarterly real GDP, which begins in the first quarter of 1947, there is only one instance of consecutive quarters with a cumulative decline in real GDP that was greater: the fourth quarter of 1957 and the first quarter of 1958.

What started as a housing sector slump in 2005 and turned into a generalized economic slump in 2008 has become a consumption slump. Consumer expenditures fell sharply in the third and fourth quarters of 2008. Since then, consumer spending has been flat. There will not be much growth in the national economy if the consumer stays on the sideline. Currently consumers have plenty of reasons to be cautious—fear of job loss, high debt burdens, eroded home equity, and tight credit. What would best boost consumer spending now is better employment growth. Some modest progress has been made on that front as monthly job losses have been trending downward since February



Source: U.S. Commerce Department, Bureau of Economic Analysis

of 2009. November brought a relatively very small loss of 11,000. It should not be long before employment starts to increase.

With consumer spending continuing to be weak, spending on new equipment and software will likely be lackluster. The outlook for spending on new structures is even worse. Retail and office space have been over-built, resulting in high vacancy rates.

Single-family housing is showing some signs of life. Residential construction has trended up in recent months but from very low levels. New home sales have trended up during most of 2009, with perhaps some help from the federal tax credit for first-time homebuyers. The inventory of new homes available for sale is at its lowest level since March 1971. Sales of existing homes are soaring, but a significant number of them are distressed properties.

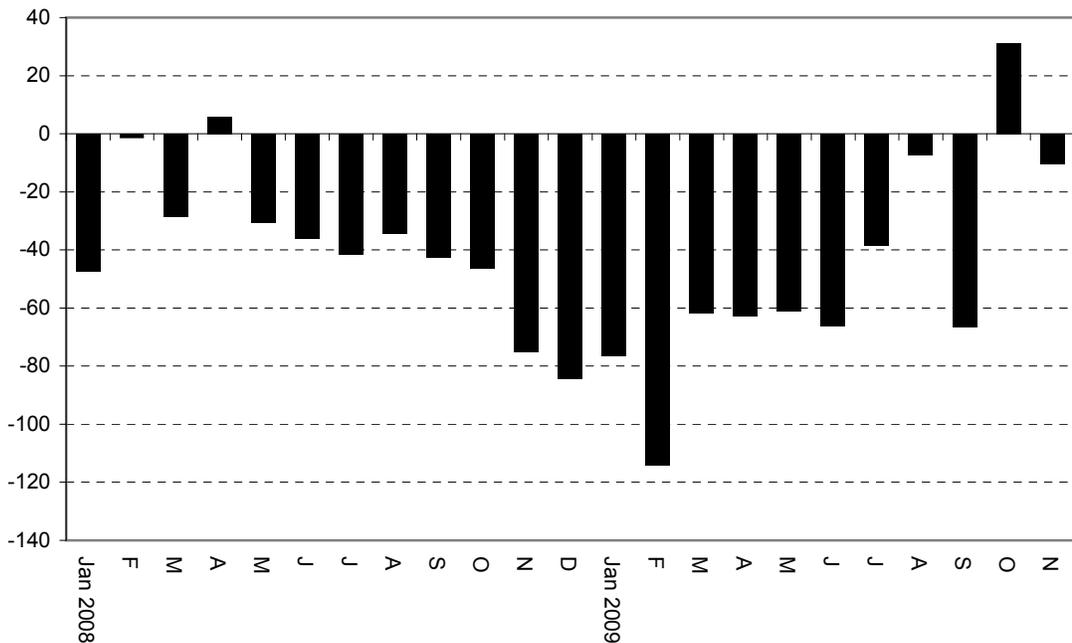
Manufacturing is growing, but from a low level.

Foreign trade is picking up as a turnaround in Asian economies, spurred by China, and an improving Europe are helping exports, while an improving U.S. economy is pulling in more imports.

CALIFORNIA – PICKING UP THE PIECES

The best news on the California economy is that the state gained 31,100 jobs in October—it was the first gain since April 2008. Monthly job losses have been trending downward since March 2009, so more monthly job gains should be in store. While this is a milestone of sorts, the state has lost nearly 1 million jobs since the recession began (Figure ECO-02).

Figure ECO-02
Month-to-Month Change in California Payroll Employment
 1,000s of Nonfarm Jobs, Seasonally Adjusted



Source: California Employment Development Department

California personal income fell sharply in the fourth quarter of 2008 and the first quarter of 2009 before falling moderately in the second quarter of 2009 and growing modestly in the third quarter of 2009—the same pattern as the national real GDP. The decline in the first quarter of 2009, 1.5 percent (not annualized), was the second biggest loss in the series, which goes back to the first quarter of 1969.

Taxable sales have been very weak in the last two years. In the third quarter of 2009, they were 16.8 percent lower than a year earlier but 0.5 percent higher than in the second quarter of 2009.

Construction was weak in the first ten months of 2009. Residential building permits were issued at a very low level. The value of private nonresidential permits fell 46 percent. Public works construction fell 28 percent.

Existing home sales have stabilized around the half-million-unit rate (seasonally-adjusted and annualized) and the median sales price has risen for eight consecutive months, pushing the median price of these homes close to \$300,000.

THE FORECAST

The California and national economies will enter 2010 having weathered the worst recession since the Great Depression. The destruction was great but, unlike last year, the clouds will be clearing (Figure ECO-03).

Figure ECO-03

Selected Economic Data for 2009, 2010, and 2011

United States	2009 (Est.)	2010 (Projected)	2011 (Projected)
Real gross domestic product (2005 CW* \$, percent change)	(2.5)	2.2	2.9
Personal consumption expenditures	(0.6)	1.5	2.3
Gross private domestic investment	(23.3)	11.9	14.3
Government purchases of goods and services	1.9	1.4	(1.5)
GDP deflator (2005=100, percent change)	1.3	1.2	1.5
GDP (current dollar, percent change)	(1.2)	3.4	4.5
Federal funds rate (percent)	0.2	0.2	1.7
Personal income (percent change)	(2.2)	2.7	4.1
Corporate profits before taxes (percent change)	(2.2)	14.0	11.0
Nonfarm wage and salary employment (millions)	131.9	130.6	132.9
(percent change)	(3.8)	(0.9)	1.7
Unemployment rate (percent)	9.2	10.0	9.4
Housing starts (millions)	0.57	0.85	1.26
(percent change)	(36.2)	48.2	48.2
New car sales (millions)	5.4	6.0	7.5
(percent change)	(20.2)	9.9	25.1
Consumer price index (1982-84=100)	214.5	219.1	223.9
(percent change)	(0.4)	2.1	2.2
California			
Civilian labor force (thousands)	18,531.2	18,638.0	18,886.0
(percent change)	0.8	0.6	1.3
Civilian employment (thousands)	16,382.2	16,396.8	16,764.7
(percent change)	(4.0)	0.1	2.2
Unemployment (thousands)	2,149.1	2,241.2	2,121.3
(percent change)	61.3	4.3	(5.3)
Unemployment rate (percent)	11.6	12.0	11.2
Nonfarm wage and salary employment (thousands)	14,158.2	14,063.1	14,239.5
(percent change)	(5.6)	(0.7)	1.3
Personal income (billions)	1,559.0	1,597.2	1,654.8
(percent change)	(2.8)	2.4	3.6
Housing units authorized (thousands)	36.3	60.8	101.0
(percent change)	(43.8)	67.3	66.1
Corporate profits before taxes (billions)	145.2	163.8	177.2
(percent change)	(12.8)	12.8	8.2
New auto registrations (thousands)	1,116.9	1,292.8	1,357.0
(percent change)	5.3	15.7	5.0
Total taxable sales (billions)	447.4	456.0	496.2
(percent change)	(15.6)	1.9	8.8
Consumer price index (1982-84=100)	224.4	229.9	235.7
(percent change)	(0.2)	2.5	2.6

* CW: Chain Weighted

Note: Percentage changes calculated from unrounded data