CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

March 5, 2012

The Honorable City Council
Palo Alto, California

City of Palo Alto Sales Tax Digest Summary Third Quarter Sales (July-September 2011)

This is an informational report and no action is required.

BACKGROUND

Sales and use tax represents about 14%, or $20.2 million, of projected General Fund revenue in the City's Adopted Operating Budget for fiscal year 2012. This revenue includes sales and use tax for the City of Palo Alto and pool allocations[1] from the State and Santa Clara County.

The City Auditor's Office contracts with MuniServices LLC (hereafter MuniServices), the City's sales and use tax consultant, to provide sales and use tax recovery services and informational reports. The City Auditor's Office uses the recovery services and informational reports to help identify misallocation of tax revenue owed to the City, and to follow up with the State Board of Equalization to ensure the City receives identified revenues. The City Auditor's Office includes information on sales and use tax recoveries in our quarterly reports to the Finance Committee.

The City Auditor's Office also shares the information provided by MuniServices with the Administrative Services Department (ASD) for use in revenue forecasting and budgeting, and Economic Development/Redevelopment for business outreach strategies. We coordinated this informational memo with them.

DISCUSSION

The attached report (Attachment A) was prepared by MuniServices and covers calendar year third quarter sales (July through September 2011). These funds are reported as part of the City's fiscal year 2012 revenue. Due to the timing of reporting by businesses and the State, MuniServices' detailed reports on fourth quarter sales (October through December 2011) should be available by May 2012. ASD advises that in mid-March, it should receive information from the State on aggregate sales and use tax receipts for fourth quarter 2011.

[1] See definitions on page 4.

Following are some highlights of the sales and use tax information we received:

- In Palo Alto, overall sales and use tax revenue (cash receipts) for the third quarter ending September 2011 increased by approximately $156,000, or 3.0%, (including pool allocations) compared to the third quarter ending September 2010. For all jurisdictions in Santa Clara County, sales and use tax revenue for the third quarter ending September 2011 increased by $5.8 million, or 7.4%, compared to the third quarter ending September 2010.

- Statewide, every region in California experienced an increase in sales and use tax revenue for the year ending September 2011, compared to the prior year ending September 2010. Statewide sales and use tax revenue has shown growth of 9.2% during the third quarter ending September 2011 compared to the third quarter ending September 2010.

- In Palo Alto, sales and use tax revenue totaled $20.5 million for the year ending September 2011, an increase of 7.7% from $19.0 million in the prior year ending September 2010. This amount includes sales and use tax for the City of Palo Alto and pool allocations from the State and Santa Clara County.

More detailed information is shown on Attachment A.

Economic Influences on Sales and Use Tax

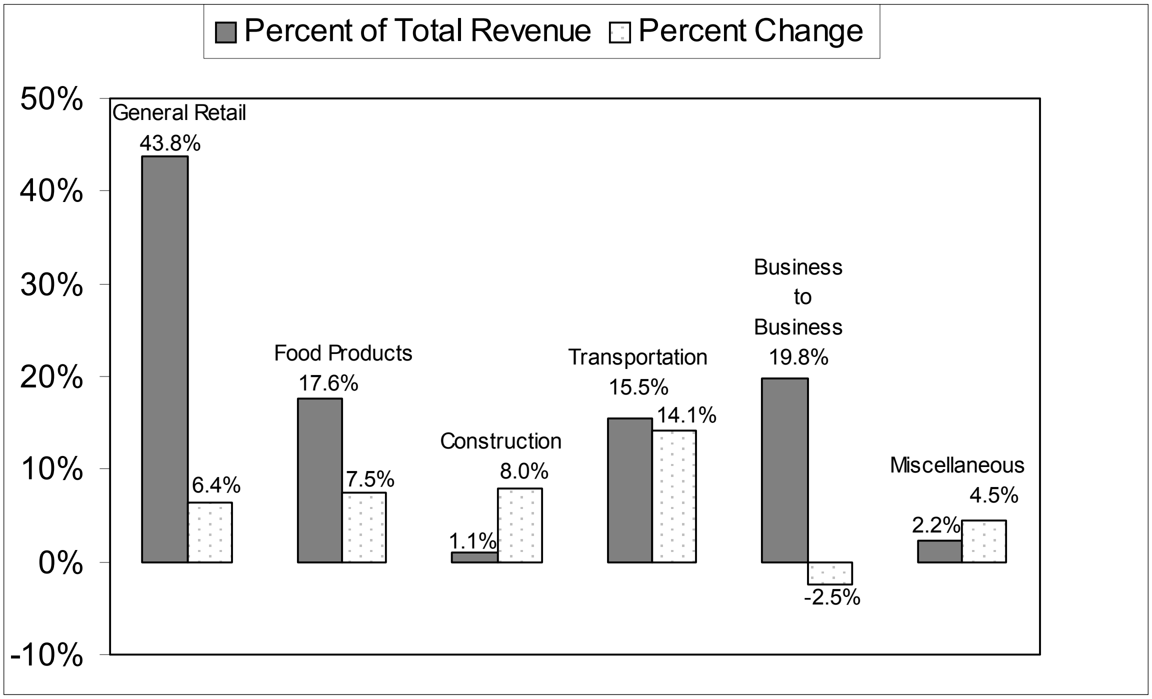
In its Economic Outlook (Attachment B), MuniServices discusses economic influences including world and national economic trends, auto sales, retail sales, and forecast information that may affect the City's sales and use tax revenue.

Preliminary estimates from the State of California Employment Development Department show the December 2011 unemployment rate in Santa Clara County at 8.7% and Palo Alto at 4.6%.

Economic Category Analysis

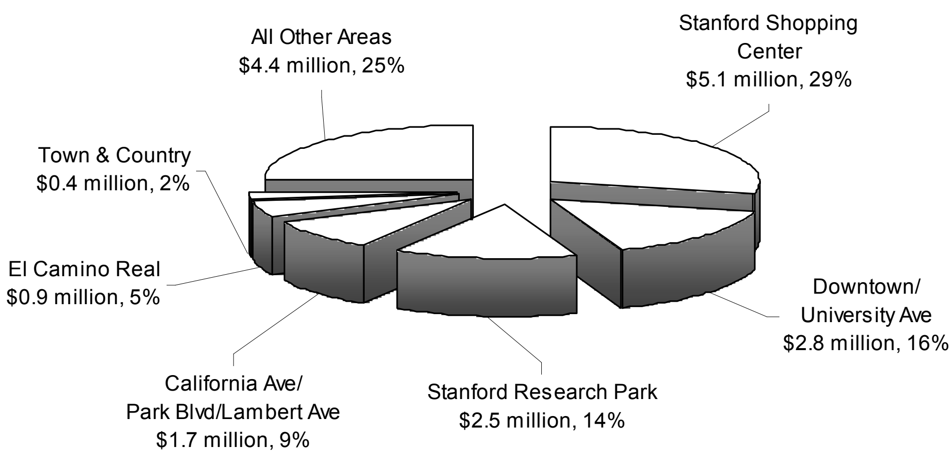
MuniServices' analysis of six economic categories, for the year ending September 2011, shows that General Retail comprised the largest percentage of Palo Alto's sales and use tax revenue and experienced 6.4% growth. Business to business experienced a 2.5% decrease and comprised 19.8% of total revenues. Transportation experienced a 14.1% increase and comprised 15.5% of total revenues.

Exhibit 1 - Comparison of Palo Alto's Sales and Use Tax Revenue and Percent Change by Economic Category for the Year Ending September 2011



The following chart shows sales and use tax revenue by geographical area based on information provided by MuniServices.

Exhibit 2 - Palo Alto's Sales and Use Tax Revenue by Geographical Area
For the Year Ending September 2011
(Amounts include tax estimates and exclude pool allocations)



DEFINITIONS

In California, either sales tax or use tax may apply to a transaction, but not both. The sales and use tax rate in Palo Alto is 8.25%, and the City should receive 1% of every taxable transaction. A temporary tax rate increase to 9.25% expired on July 1, 2011.

Sales tax - imposed on all California retailers; applies to all retail sales of merchandise (tangible personal property) in the state.

Use tax - generally imposed on: consumers of merchandise (tangible personal property) that is used, consumed, or stored in this state; purchases from out-of-state retailers when the out-of-state retailer is not registered to collect California tax, or for some other reason does not collect California tax; leases of merchandise (tangible personal property).

Countywide/statewide pools - mechanisms used to allocate local tax that cannot be identified with a specific place of sale or use in California. Local tax reported to the pool is distributed to the local jurisdiction each calendar quarter using a formula that relates to the direct allocation of local tax to each jurisdiction for a given period.

Examples of taxpayers who report use tax allocated through the countywide pool include construction contractors who are consumers of materials used in the improvement of real property and whose job site is regarded as the place of business, out-of-state sellers who ship goods directly to consumers in the state from inventory located outside the state, and California sellers who ship goods directly to consumers in the state from inventory located outside the state.

Other examples of taxpayers who report use tax through the pools include auctioneers, construction contractors making sales of fixtures, catering trucks, itinerant vendors, vending machine operators and other permit holders who operate in more than one local jurisdiction, but are unable to readily identify the particular jurisdiction where the taxable transaction takes place.

Respectfully submitted,

Jim Pelletier
City Auditor

Sources: MuniServices; California State Board of Equalization; State of California Employment Development Department; City of Palo Alto's Adopted Operating Budget Fiscal Year 2012

Audit staff: Lisa Wehara

ATTACHMENTS:

- Attachment A: City of Palo Alto Sales Tax Digest Summary (PDF)
- Attachment B: Economic Outlook (PDF)

Department Head: Jim Pelletier, City Auditor

City of Palo Alto
Sales Tax Digest Summary
Collections through December 2011
Sales through September 2011 (2011Q3)

Attachment A

California Overview

The percent change in cash receipts from the prior year was 8.4% statewide, 9.2% in Northern California and 7.8% in Southern California. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments. When we adjust for non-period related payments, we determine the overall business activity increased for the year ended 3rd Quarter 2011 by 7.2% statewide, 6.3% in Northern California and increased by 3.8% in Southern California.

City of Palo Alto

For the year ended 3rd Quarter 2011, sales tax cash receipts for the City grew by 7.7% from the prior year. On a quarterly basis, sales tax revenues increased by 3.0% from 3rd Quarter 2010 to 3rd Quarter 2011. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments.

Excluding state and county pools and adjusting for anomalies (payments for prior periods) and late payments, local sales tax increased by 5.8% for the year ended 3rd Quarter 2011 from the prior year. On a quarterly basis, sales tax activity grew by 0.7% in 3rd Quarter 2011 compared to 3rd Quarter 2010.

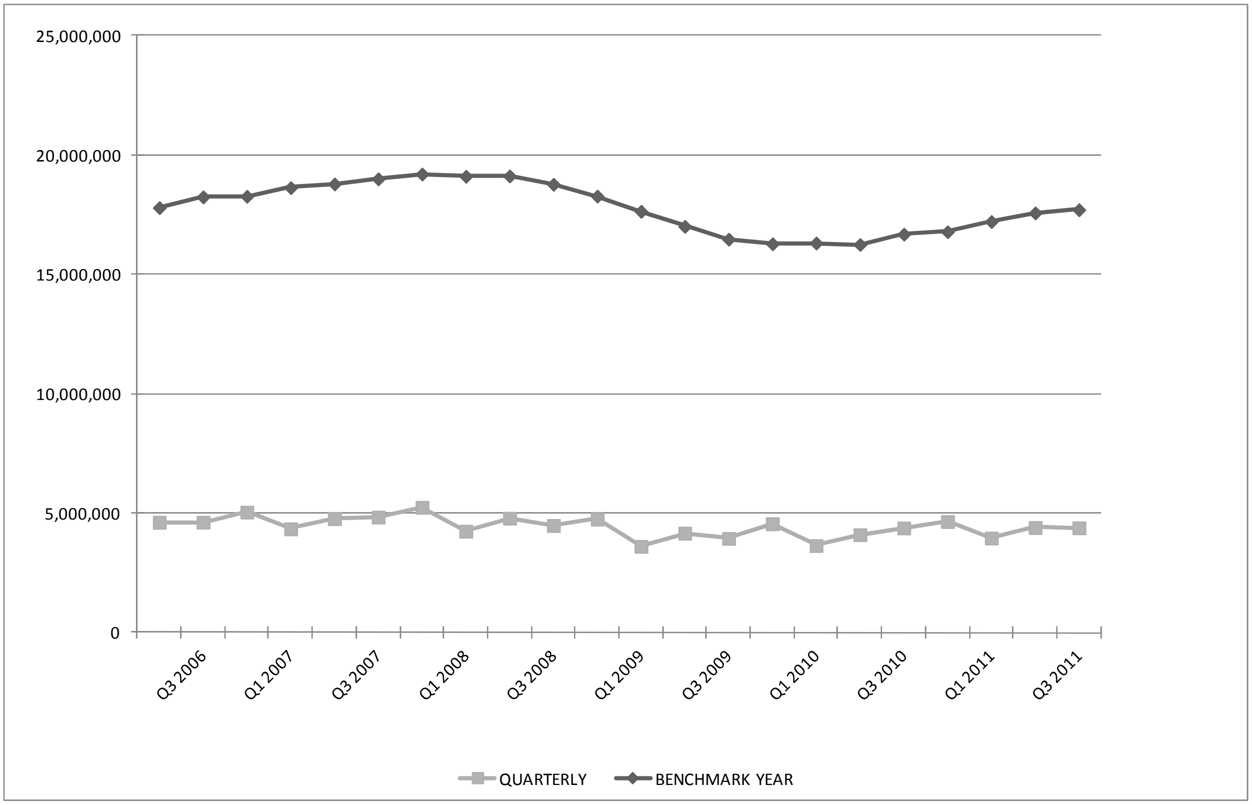
Regional Overview

This seven-region comparison includes estimated payments and excludes net pools and adjustments.

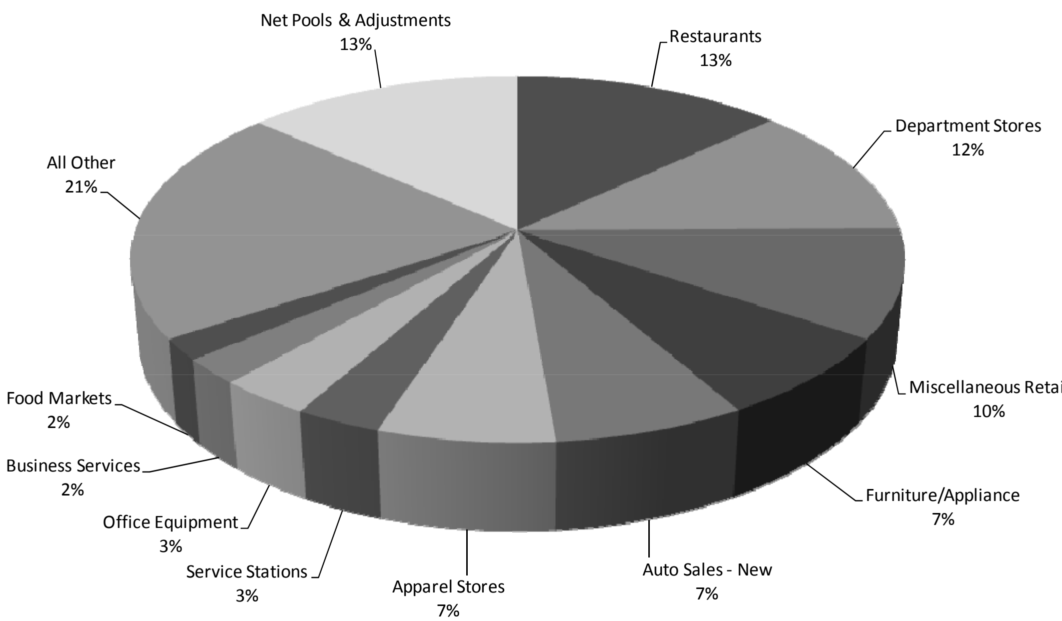
ECONOMIC CATEGORY ANALYSIS FOR YEAR ENDED 3rd QUARTER 2011								
	Palo Alto	California Statewide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	North Coast	Central Coast
General Retail *% of Total / % Change*	43.8 / 6.4	29.9 / 4.1	29.5 / 4.6	30.6 / 0.8	32.0 / 4.2	29.8 / 4.1	31.8 / 1.1	33.2 / 1.0
Food Products *% of Total / % Change*	17.6 / 7.5	19.1 / 4.4	19.8 / 5.9	17.5 / 3.3	16.7 / 3.9	19.4 / 4.0	17.7 / 1.3	29.5 / 2.9
Construction *% of Total / % Change*	1.1 / 8.0	8.3 / 4.2	8.1 / 4.8	10.1 / 3.0	10.5 / 7.0	7.8 / 3.8	12.5 / -0.4	8.7 / -4.3
Transportation *% of Total / % Change*	15.5 / 14.1	23.5 / 15.0	20.6 / 14.4	26.8 / 13.7	25.4 / 18.8	24.1 / 14.7	28.4 / 15.3	21.7 / 16.6
Business to Business *% of Total / % Change*	19.8 / -2.5	17.9 / 8.1	20.8 / 7.9	13.6 / 0.8	14.1 / 15.9	17.6 / 8.3	8.6 / 4.3	5.8 / -7.7
Miscellaneous *% of Total / % Change*	2.2 / 4.5	1.3 / 2.8	1.2 / -0.7	1.3 / 2.7	1.4 / 32.9	1.2 / 1.8	1.0 / -62.5	1.1 / -30.5
Total	**100.0 / 5.8**	**100.0 / 7.2**	**100.0 / 7.4**	**100.0 / 4.7**	**100.0 / 9.8**	**100.0 / 7.2**	**100.0 / 3.2**	**100.0 / 3.0**

THREE LARGEST SEGMENTS FOR YEAR ENDED 3rd QUARTER 2011								
	Palo Alto	California Statewide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	North Coast	Central Coast
Largest Segment	**Restaurants**	**Restaurants**	**Restaurants**	**Department Stores**	**Department Stores**	**Restaurants**	**Department Stores**	**Restaurants**
% of Total / % Change	15.1 / 7.9	13.2 / 5.1	13.7 / 6.7	12.8 / 0.3	15.1 / 2.8	13.9 / 4.9	14.6 / 1.2	19.8 / 2.6
2nd Largest Segment	**Department Stores**	**Department Stores**	**Department Stores**	**Restaurants**	**Service Stations**	**Service Stations**	**Services Stations**	**Misc. Retail**
% of Total / % Change	13.5 / 5.4	10.9 / 3.1	9.7 / 3.5	10.8 / 19.0	12.2 / 25.6	10.7 / 20.7	13.6 / 23.4	10.4 / 0.6
3rd Largest Segment	**Electronic Equipment**	**Service Stations**	**Service Stations**	**Service Stations**	**Restaurants**	**Department Stores**	**Restaurants**	**Service Stations**
% of Total / % Change	Confidential / -9.5	10.5 / 21.3	9.1 / 21.7	10.7 / 2.1	9.8 / 3.6	10.5 / 3.4	9.7 / 1.0	10.1 / 21.0

Gross Historical Sales Tax Performance by Benchmark Year and Quarter (Before Adjustments)



Net Cash Receipts for Benchmark Year 3rd Quarter 2011: $20,455,458

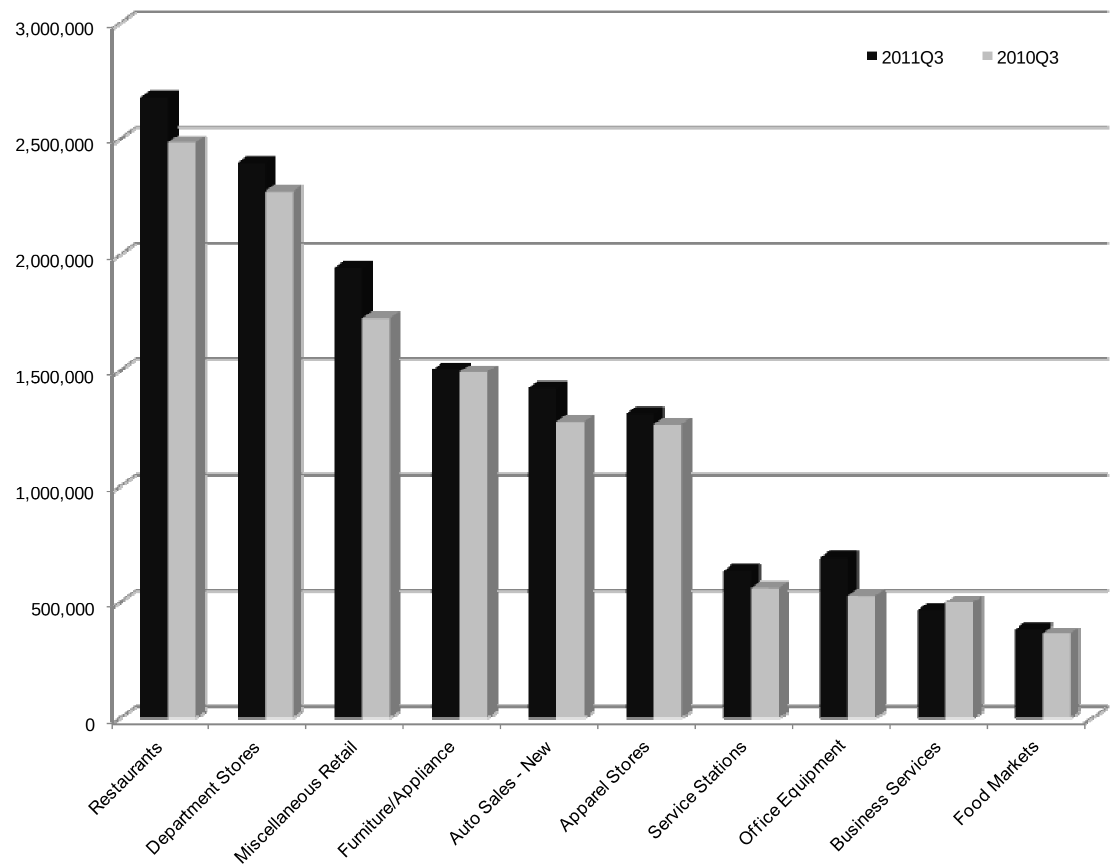


TOP 25 SALES/USE TAX CONTRIBUTORS

The following list identifies Palo Alto's Top 25 Sales/Use Tax contributors. The list is in alphabetical order and represents the year ended 3rd Quarter 2011. The Top 25 Sales/Use Tax contributors generate 52.0% of Palo Alto's total sales and use tax revenue.

- Anderson Honda
- Apple Stores
- Bloomingdale's
- Carlsen Motor Cars
- Carlsen Subaru
- Crate & Barrel
- CVS/Pharmacy
- Dow Jones & Company
- Fry's Electronics
- Hewlett-Packard
- Integrated Archive Systems
- Keeble & Shucat Photography
- Loral Space Systems
- Macy's Department Store
- Magnussen's Toyota
- Neiman Marcus Department Store
- Nordstrom Department Store
- Pottery Barn
- Shell Service Stations
- Stanford University Hospital
- The Gap
- Tiffany & Company
- Valero Service Stations
- Varian Medical Systems
- Walgreen's Drug Stores

Sales Tax from Largest 10 Non-confidential Economic Segments



Historical Analysis by Calendar Quarter

Economic Category	%	2011Q3	2011Q2	2011Q1	2010Q4	2010Q3	2010Q2	2010Q1	2009Q4	2009Q3
General Retail	35.5%	1,886,520	1,984,860	1,573,474	2,275,627	1,810,271	1,864,922	1,473,821	2,064,636	1,615,455
Business To Business	15.8%	842,771	842,709	925,263	887,037	1,006,576	788,373	849,181	993,411	894,386
Food Products	15.0%	799,167	806,987	740,594	769,253	726,360	739,629	666,388	699,788	665,680
Transportation	13.1%	694,998	619,897	593,452	590,209	576,597	551,313	534,793	516,345	594,725
Miscellaneous	2.2%	117,132	100,653	87,535	75,077	217,465	78,340	67,673	70,822	79,799
Construction	0.9%	46,843	44,589	38,765	54,645	44,171	40,415	37,914	48,862	44,182
Net Pools & Adjustments	17.5%	933,424	845,214	769,789	508,973	782,981	626,593	487,801	634,071	684,537
Total	100.0%	5,320,855	5,244,909	4,728,872	5,160,821	5,164,421	4,689,585	4,117,571	5,027,935	4,578,764

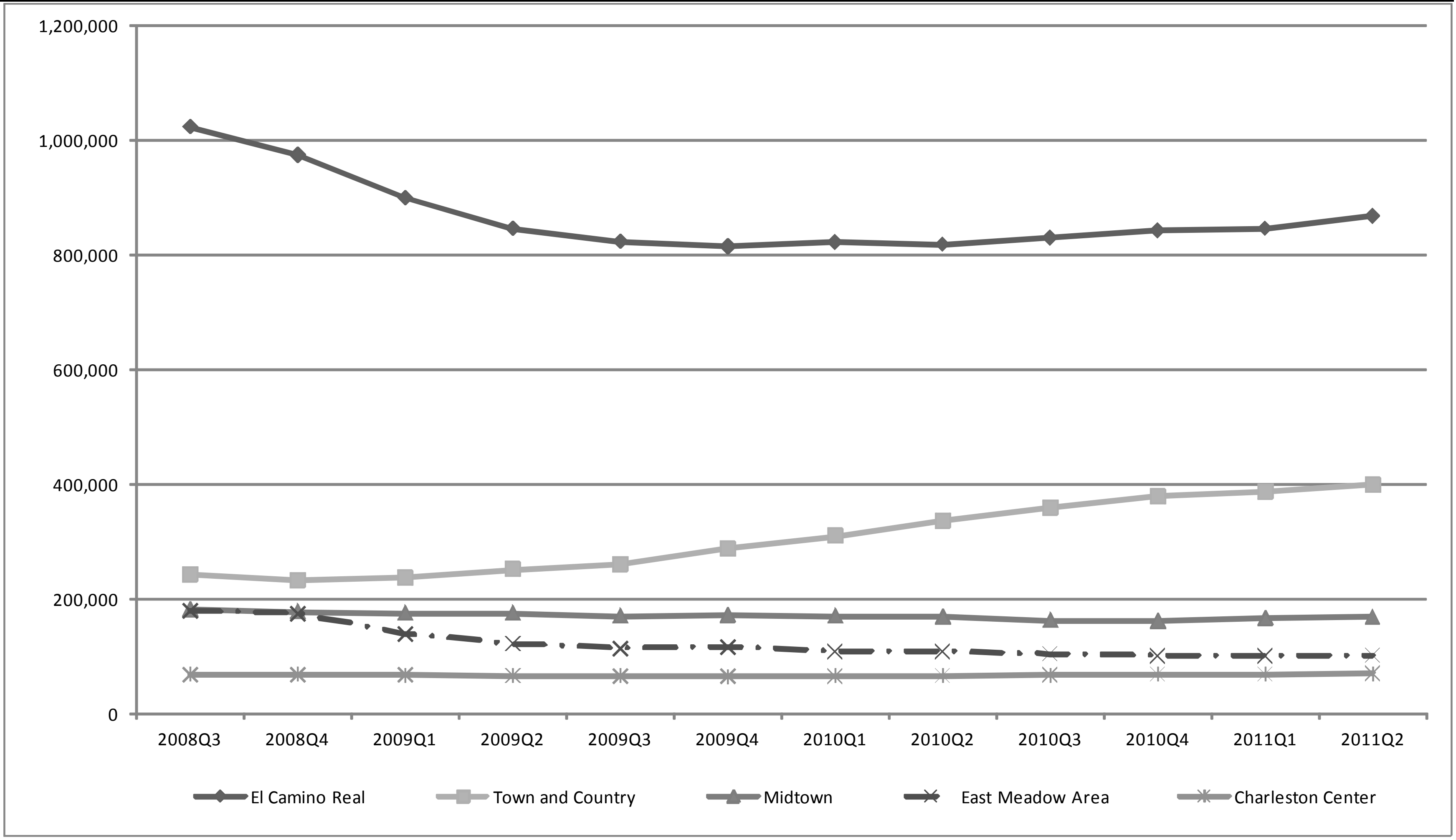
Economic Segments	%	2011Q3	2011Q2	2011Q1	2010Q4	2010Q3	2010Q2	2010Q1	2009Q4	2009Q3
Restaurants	13.0%	689,568	705,459	639,353	651,614	622,517	636,566	568,305	597,762	580,829
Department Stores	10.6%	563,373	608,784	474,566	748,885	541,942	565,706	455,378	714,431	480,038
Miscellaneous Retail	8.6%	455,335	482,723	399,243	584,895	396,580	381,222	325,512	459,998	341,947
Furniture/Appliance	7.2%	385,236	392,126	301,427	421,877	447,946	416,128	282,989	345,141	352,050
Apparel Stores	6.0%	321,296	333,697	266,990	387,682	299,340	321,787	267,315	375,133	286,511
Service Stations	3.0%	160,037	181,065	158,421	147,520	143,233	140,859	139,906	128,317	134,369
Business Services	2.0%	104,234	105,507	100,241	146,732	112,153	143,241	110,989	113,481	124,575
Food Markets	1.8%	98,054	89,530	91,274	105,573	93,651	92,036	86,892	88,469	74,317
Auto Parts/Repair	0.9%	49,977	51,743	47,157	43,537	45,689	40,037	39,150	39,592	40,669
Leasing	0.8%	42,654	35,131	34,857	36,962	40,480	36,129	34,760	37,222	41,697
Bldg.Matls-Retail	0.8%	41,338	38,236	34,016	48,591	39,747	35,783	33,297	38,766	39,314
Liquor Stores	0.2%	11,321	11,319	9,967	12,060	10,192	11,027	11,162	13,297	10,534
Miscellaneous Other	0.2%	9,857	8,724	6,458	8,714	5,751	7,689	6,550	9,061	7,637
Heavy Industry	0.2%	8,349	8,029	3,833	3,580	3,288	4,887	4,782	5,944	5,090
Bldg.Matls-Whsle	0.1%	5,505	6,353	4,749	6,054	4,424	4,632	4,617	10,096	4,868
All Other	27.1%	1,441,297	1,341,269	1,386,531	1,297,572	1,574,507	1,225,263	1,258,166	1,417,154	1,369,782
Net Pools & Adjustments	17.5%	933,424	845,214	769,789	508,973	782,981	626,593	487,801	634,071	684,537
Total	100.0%	5,320,855	5,244,909	4,728,872	5,160,821	5,164,421	4,689,585	4,117,571	5,027,935	4,578,764

*Net Pools & Adjustments reconcile economic performance to periods' net cash receipts. The historical amounts by calendar quarter: (1) include any prior period adjustments and payments in the appropriate category/segment and (2) exclude businesses no longer active in the current period.

Quarterly Analysis by Economic Category, Total and Segments: Change from 2010Q3 to 2011Q3

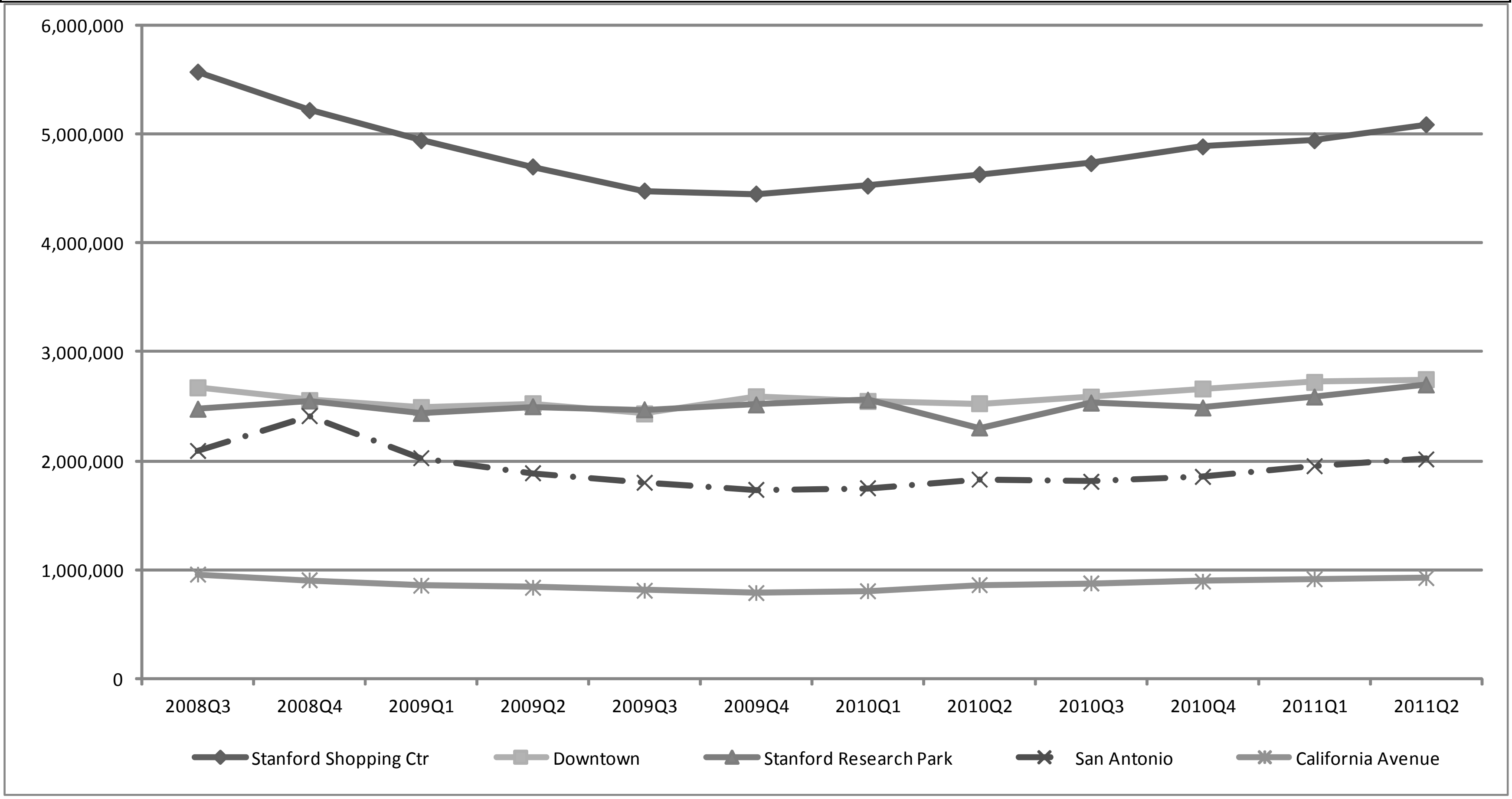
	General Retail	Food Products	Transportation	Construction	Business to Business	Miscellaneous	2011/3 Total	2010/3 Total	% Chg	Largest Gain	Second Largest Gain	Largest Decline	Second Largest Decline
Campbell	0.4%	9.7%	40.8%	10.0%	24.7%	-14.1%	2,009,144	1,766,305	**13.7%**	Service Stations	Business Services	Furniture/Appliance	Auto Sales - Used
Cupertino	5.8%	8.9%	14.2%	37.2%	-6.6%	-15.0%	4,351,180	4,476,410	**-2.8%**	Office Equipment	Service Stations	Business Services	Electronic Equipment
Gilroy	5.8%	5.5%	20.1%	5.3%	7.2%	21.4%	2,993,882	2,742,565	**9.2%**	Apparel Stores	Misc. Vehicle Sales	Department Stores	Electronic Equipment
Los Altos	-3.7%	7.5%	14.3%	7.8%	-23.9%	-7.1%	502,760	483,138	**4.1%**	Service Stations	Food Markets	Miscellaneous Retail	Furniture/Appliance
Los Gatos	5.8%	7.7%	-0.7%	-11.8%	9.1%	-17.4%	2,149,046	2,047,533	**5.0%**	Miscellaneous Retail	Restaurants	Furniture/Appliance	Auto Sales - New
Milpitas	4.8%	5.5%	2.9%	10.0%	-5.2%	-0.4%	3,771,964	3,703,980	**1.8%**	Office Equipment	Apparel Stores	Electronic Equipment	Auto Sales - New
Monte Sereno	-38%	-100.0%	-100%	-100%	100%	38.5%	694	2,419	**-71.3%**	Furniture/Appliance	Business Services	Auto Parts/Repair	Department Stores
Morgan Hill	3.1%	4.6%	19.2%	-1.3%	13.5%	8.3%	1,355,078	1,228,943	**10.3%**	Electronic Equipment	Service Stations	Chemical Products	Light Industry
Mountain View	-0.9%	6.0%	3.0%	0.3%	-38.0%	-17.2%	3,123,399	3,475,280	**-10.1%**	Service Stations	Restaurants	Electronic Equipment	Business Services
Palo Alto	3.1%	8.6%	6.9%	4.1%	-15.5%	19.3%	4,387,431	4,357,123	**0.7%**	Office Equipment	Restaurants	Electronic Equipment	Furniture/Appliance
San Jose	1.1%	5.4%	16.0%	6.9%	1.2%	0.7%	30,964,268	29,289,077	**5.7%**	Service Stations	Auto Sales - New	Office Equipment	Furniture/Appliance
Santa Clara	-0.6%	7.5%	10.9%	7.2%	31.5%	-3.9%	8,539,693	7,432,520	**14.9%**	Electronic Equipment	Office Equipment	Auto Parts/Repair	Auto Sales - Used
Santa Clara Co.	-3.7%	10.7%	6.5%	24.2%	-24.9%	45.7%	1,061,571	974,062	**9.0%**	Electronic Equipment	Office Equipment	Health & Government	Food Processing Eqp
Saratoga	11.4%	1.2%	22.3%	-40.2%	0.3%	36.0%	251,334	236,304	**6.4%**	Furniture/Appliance	Service Stations	Miscellaneous Retail	Office Equipment
Sunnyvale	-1.5%	8.1%	14.3%	-11.2%	13.6%	-30.2%	6,432,741	5,977,429	**7.6%**	Electronic Equipment	Office Equipment	Light Industry	Bldg.Matls-Whsle

City of Palo Alto - Selected Geographic Areas of the City Benchmark Year 3rd Quarter 2011													
	2008Q3	2008Q4	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3
El Camino Real	1,023,703	974,931	900,018	846,897	823,627	814,940	822,245	818,947	830,152	843,626	846,897	867,868	854,828
Town and Country	243,683	233,208	237,307	251,608	261,294	288,103	309,848	336,444	360,254	379,066	386,944	399,378	412,361
Midtown	181,687	178,212	175,471	175,723	170,741	172,297	170,517	169,297	162,869	162,122	166,440	168,537	171,719
East Meadow Area	179,006	173,424	139,391	122,493	112,819	116,128	107,931	108,922	104,777	100,155	100,032	102,028	108,176
Charleston Center	68,363	68,585	67,632	66,529	65,328	64,981	65,642	66,446	67,447	68,693	69,150	69,606	70,301

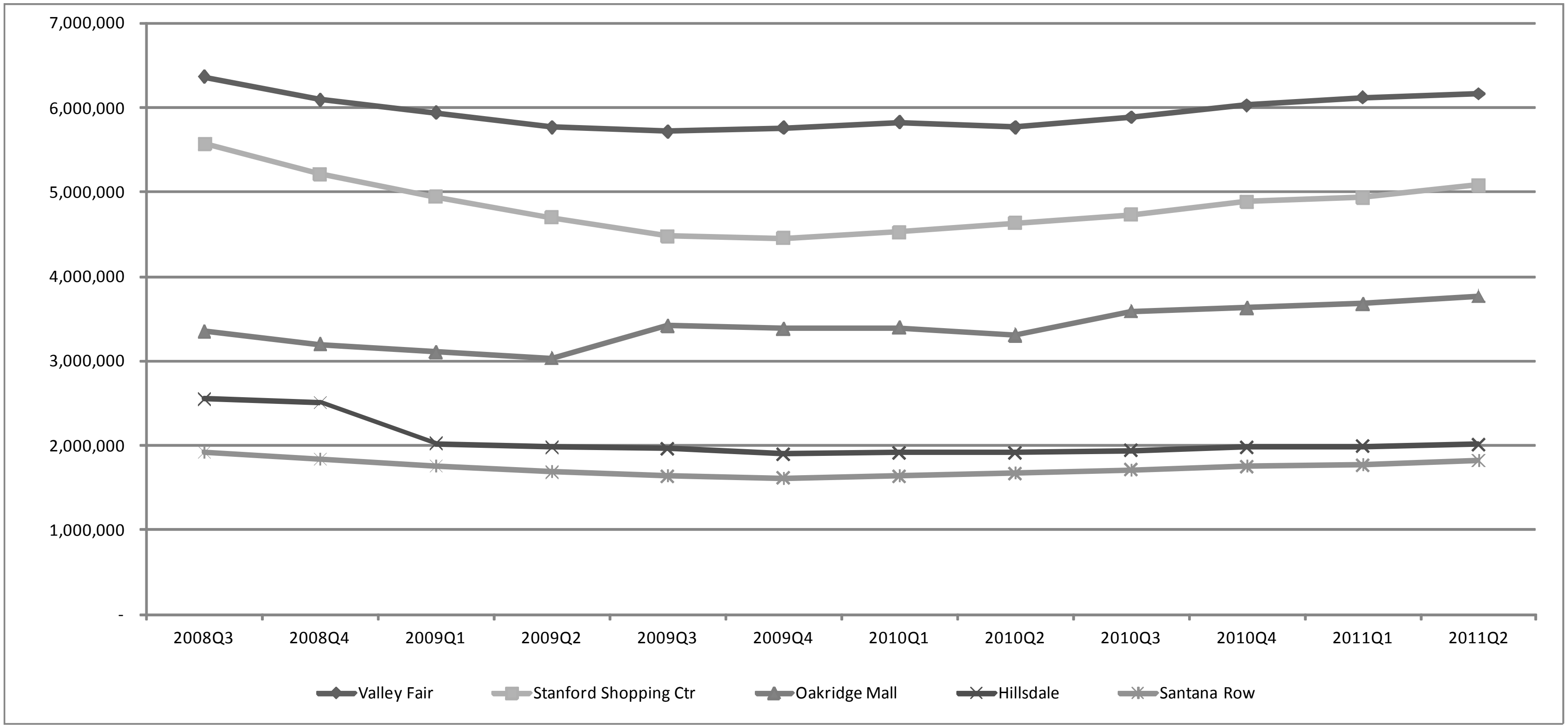


City of Palo Alto - Selected Geographic Areas of the City
Benchmark Year 3rd Quarter 2011

	2008Q3	2008Q4	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3
Stanford Shopping Ctr	5,570,554	5,218,085	4,941,824	4,701,109	4,479,311	4,451,986	4,524,318	4,631,095	4,731,800	4,884,843	4,941,127	5,087,834	5,079,526
Downtown	2,674,057	2,557,974	2,493,666	2,528,443	2,434,567	2,591,213	2,549,106	2,528,095	2,589,660	2,663,500	2,723,552	2,748,925	2,793,987
Stanford Research Park	2,478,283	2,552,881	2,439,025	2,500,473	2,472,512	2,517,622	2,560,998	2,305,707	2,534,669	2,489,301	2,589,986	2,700,836	2,487,708
San Antonio	2,094,820	2,414,351	2,028,139	1,890,196	1,802,851	1,737,780	1,752,653	1,831,894	1,811,722	1,856,817	1,954,526	2,017,259	2,156,535
California Avenue	960,772	908,095	858,391	839,591	812,294	790,954	807,490	863,730	879,364	895,989	917,851	928,031	945,340



City of Palo Alto - Regional Shopping Mall Comparison Benchmark Year 3rd Quarter 2011													
	2008Q3	2008Q4	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3
Valley Fair	6,367,597	6,093,294	5,941,991	5,769,466	5,717,263	5,761,442	5,829,695	5,769,507	5,887,510	6,031,602	6,119,960	6,166,420	6,204,976
Stanford Shopping Ctr	5,570,554	5,218,085	4,941,824	4,701,109	4,479,311	4,451,986	4,524,318	4,631,095	4,731,800	4,884,843	4,941,127	5,087,834	5,079,526
Oakridge Mall	3,355,538	3,199,518	3,105,561	3,035,077	3,419,383	3,380,772	3,395,994	3,308,231	3,589,119	3,630,341	3,679,073	3,768,899	3,782,531
Hillsdale	2,551,004	2,509,227	2,020,719	1,981,010	1,961,708	1,895,456	1,915,711	1,917,510	1,943,391	1,982,532	1,989,259	2,015,790	2,019,678
Santana Row	1,919,027	1,840,846	1,755,862	1,685,331	1,635,305	1,615,462	1,637,476	1,667,967	1,711,667	1,749,506	1,770,255	1,821,843	1,897,528



Attachment B

Economic Outlook

4Q2011 News

GLOBAL INSTABILITY

European crisis could stall U.S. recovery

American economy has safeguards in place, but 'financial contagion' a fear

For the second time in two years, European debt troubles threaten to slow the momentum of the fragile recovery in the United States. Although U.S. financial institutions have taken steps to protect themselves from Europe's long-simmering problems, the likely slowdown in Europe could damage consumer and business confidence in America and strengthen the dollar, making U.S. exports less competitive.

"Financial contagion can lead to the very rapid global spread of recession," said Chris Varvares, senior managing director for Macroeconomic Advisers, a forecasting company. "If trouble intensifies and spills over to equities and other U.S. risk assets, we could see a soft patch."

Economists say Europe's troubles would need to worsen significantly before putting the U.S. economy, which has been strengthening lately, at risk of a new recession. The European Union and United States economies are the two biggest in the world and their financial institutions are deeply intertwined. They have the single largest bilateral trade relationship, together accounting for nearly a third of global trade flows.

Recently, the European Commission announced that it foresaw little or no growth in the European Union in the fourth quarter of the year, and a slight 0.1 percent contraction for the eurozone, the 17 countries using the euro currency. It forecast a scant 0.5 percent annual growth in 2012 for the union and warned that the Continent may be slipping into a "deep and prolonged" recession. As recently as spring, the commission forecast that Europe would grow 1.75 percent for 2012.

Fed lowers target on growth, hiring through next year

Bernanke says low consumer confidence is 'very discouraging'

As the Federal Reserve downgraded its economic projections, Chairman Ben Bernanke admitted that the central bank's board was in the same distressing position as the average American family - frustrated by the slow recovery, limited in its options and largely reduced to hoping for the best. "I certainly understand that many people are dissatisfied with the state of the economy." "I'm dissatisfied with the state of the economy."

The Fed noted in its official statement after its two day meeting that economic conditions strengthened somewhat from July through September and that inflation appeared to have slowed. But the European debt crisis weighed heavily on the U.S. economy. The Central bank warned of "significant downside risks to the economic outlook, including strains in global financial markets."

Given those troubles, the Fed lowered its projections for economic growth and for an improved unemployment rate for the third time in 2011. The new figures show the recovery slogging along at least through next year. "In short, while we still expect that economic activity and labor market conditions will improve gradually over time, the pace of progress is likely to be frustratingly slow," Bernanke said, acknowledging that the Fed had overestimated the strength of the recovery. Annual growth will be between 1.6 percent and 1.7 percent to 2.9 percent. And growth will remain below 3 percent next year, well below the June forecast of 3.3 percent to 3.7 percent.

The unemployment rate now at 9.1 percent - also won't show much improvement. It could remain above 8 percent through 2013, the Fed said. And Bernanke noted: "You can see that right now, consumer confidence is about where it was in the depths of the recession. That's very discouraging."

Still, the Fed's policymaking Open Market Committee took no new steps to boost the recovery. The central bank appears to be holding its few remaining options in case the European situation worsens or some other new shock hits the economy. "We've already taken quite a bit of action, but we're prepared to do more, and we have the tools to do more if that's appropriate, " Bernanke said.

With short-term interest rates likely to remain near zero through mid-2013, however, there's not a lot left for the Fed to do. After two major rounds of bond buying to try to stimulate the economy, the Fed has taken smaller steps recent months. In September, for example, the Fed started shifting more of its portfolio to longer term Treasury bonds in a move to bring down long-term interest rates. The goal was to lower mortgage rates to help improve the housing market. Some Fed officials have suggested the central bank could buy a large amount of mortgage-backed bonds to lower mortgage rates even more. Bernanke said that would be a "viable option" should economic conditions warrant it.

ECONOMIC RECOVERY

Signs of life, but where are jobs?

Applications for jobless benefits remain high despite growth in manufacturing and construction

The economy is picking up. If only job growth would follow. A spate of data recently showed U.S. factories grew last month at the fastest pace since June, construction spending increased for a third straight month, and both retail sales and auto sales rose in November.

But the number of people applying for unemployment benefits is still too high to signal strong hiring. The reports offered a mixed picture for the economy. Economists project that employers added a net 125,000 jobs. That's not enough to lower the unemployment rate, which is projected to stay at 9 percent for the second consecutive month. And manufacturers could face stains overseas in key export markets, especially if Europe's debt crisis worsens and leads that continent into another recession.

For now, factories are growing. The Institute for Supply Management, a trade group of purchasing managers, said recently that its manufacturing index rose to 52.7 in November, up from 50.8 in October. Any reading above 50 indicates expansion. Factories have grown for 28 straight months.

Cautious optimism

Bradley Holcomb, chair of the ISM's survey committee, said manufactures "are cautiously more optimistic about the next few months based on lower raw material pricing and favorable levels of new orders." Still, companies have tempered their outlook with concerns about future economic growth, government regulation and the debt crisis in Europe, he added.

New orders rose to a seven-month high and production increased, according to separate indexes in the report. Ian Shepherdson, an economist at High Frequency Economics, said the gains suggest factory output will expand at an even faster pace next month. "The economy seems finally to be developing real momentum; growth is accelerating," he said in a note to clients.

But a measure of factory employment fell. The drop indicates manufacturers are still hiring, but at a slower pace than the previous month. Worker productivity rose in the July-September quarter by the most in 18 months, while labor costs fell, the government said recently. A more productive and lesscostly workforce can boost corporate profits. But unless companies see more demand, they're unlikely to step up hiring.

China, the world's second-largest economy, is also slowing. Manufacturing in China contracted in November for the first time in nearly three years, according to recent business surveys.

Revised report scales back economic growth in Q3

The U.S. economy grew more slowly over the summer than the government had earlier estimated because businesses cut back more sharply on restocking of shelves.

The Commerce Department said that the economy expanded at an annual rate of 2 percent in the July-September quarter, lower than an initial 2.5 percent estimate made the previous month. The government also said after-tax incomes fell by the largest amount in two years, reflecting high unemployment and lower pay raises.

The downward revision was largely because weaker data on inventory building came in after the government's first estimate. Many businesses reduced their stockpiles over the summer, probably because they didn't anticipate the strength of consumer and business spending. A decline in inventories is not always a bad sign. Economists believe this could lead to stronger growth in the current quarter, if businesses foresee more demand and restock shelves.

Economists predict growth will strengthen to around 3 percent in the October-December quarter. Many raised their estimates after seeing encouraging October reports on retail sales and factory output. "While this report is disappointing, it is a look back in time," said Jennifer Lee, senior economist at BMO Capital Markets. "It is encouraging, to say the least, to see the October data coming in stronger, which is good news for the fourth quarter."

Still, growth could be slowed if consumers continue to earn less. After-tax, inflation-adjusted incomes fell at a 2.1 percent rate. That's steeper than the 1.7 percent decline initially estimated and the biggest drop since the third quarter of 2009, just as the recession was ending. It also marked the second straight quarterly decline.

Incomes are primarily wages and salaries, but they also include dividend and interest payments and government benefits. While the decline doesn't directly affect economic growth, income fuels consumer spending and that makes up 70 percent of economic activity. "For now the U.S. economy looks to be moving in the right direction," said Paul Ashworth, chief U.S. economist at Capital Economics, who predicts growth of more than 3 percent in the fourth quarter.

Car Sales / November

Zooming November car sales surprise dealers

Car dealers are getting a surprise end-of-year bonus: More Americans are replacing old cars and trucks, enlivening a normally sleepy time for auto sales and putting November on track to be the industry's strongest month of the year.

Dealers and analysts say people are finally getting rid of cars and trucks they've held onto for more than a decade. That demand, plus attractive lease deals, an ample supply of Japanese models and promotions on remaining 2011 models have drawn buyers to showrooms in large numbers. "We're seeing the most showroom traffic that we've seen all year," said Ed Williamson, part-owner of two Miami-area GM Buick-Cadillac-GMC dealerships.

The spike in activity comes after months of sputtering sales. Consumers have been reluctant to take on major debt such as car payments because of the uncertain job market. Unemployment has been around 9 percent for more than two years with no sign of significant improvement.

Sales also suffered when Honda Motor and Toyota Motor ran short of models during the summer and early fall because of factory disruptions caused by the earthquake in Japan and flooding in Thailand. Now supplies are starting to return to normal and customers have a better selection. So far this year, sales have been better than 2010, an annual rate of 12.6 million compared with 11.5 million, but that's still far short of the 2005 peak of 17 million.

Recent sales have been so strong that General Motors' top sales executive predicts that November figures will hit an annual rate of about 13.8 million light vehicles in the U.S. That's a big step up from last November, when the auto industry was just starting to recover from the economic meltdown. Back then, the sales rate was only 12.3 million.

After years of holding off on purchases, people are tiring of their old cars and trucks. So despite a volatile stock market, high unemployment and worries that the European debt crisis could destabilize the global financial system, people are buying, said Jesse Toprak, vice president of industry trends for the TrueCar.com auto pricing website.

The average age of a car on U.S. roads is now a record 10.6 years, according to the Polk auto industry research firm. Vehicles are so old that people's lives changed, and they need different models, or their cars are just worn out, he said.

Buyers shun midsized cars in favor of smaller.

You can't drive far in the U.S. without seeing a Toyota Camry, Honda Accord or Ford Fusion. Midsize sedans have been America's favorite cars for decades. That's changing. More people are choosing small cars like the Chevrolet Cruze and even smaller ones like the Honda Fit because they're worried about gas prices and car payments. Compact cars will out-sell midsize ones as early as this year, forecasts J.D. Power and Associates.

Car Sales / December

Carmakers end year on a roll

For Detroit's Big 3, December, full-year sales set torrid pace

Automakers finished 2011 on the upswing, with strong December sales in the United States and expectations for further growth this year. For Chrysler, December was the best month in nearly three years, as passenger-car deliveries more than doubled and total sales rose 37 percent. Chrysler's sales for all of 2011 were up 26 percent.

General Motors reported a 5 percent increase in December and a 13 percent gain for the year. At the Ford Motor Co., sales were up 10 percent in December and 11 percent for the year. Sales by Ford's namesake brand totaled 2.06 million, the most by any automotive brand since 2007.

Each of the three Detroit carmakers gained market share, something they had not all done in the same year for decades. Sales increased for all but one brand based in Detroit, the exception being Lincoln, which Ford is focused on revitalizing this year.

Only two major carmakers, Toyota and Honda, posted sales declines in 2011. Honda posted a 19 percent drop in December, while Toyota's sales were essentially flat. Full-year sales for both companies were 7 percent lower. Each is still working to replenish its dealer inventories, which were decimated by plant shutdowns and parts shortages in the wake of the Japanese earthquake and tsunami. Toyota executives said they expected inventories to be back to normal by the end of the first quarter.

Nissan, which was affected less severely by the disaster, posted a 15 percent increase for the full year, and its primary brand set a record. The company also reported a record high for December with a 7 percent increase.

Hyundai and Kia each set new records for annual sales, with gains of 20 percent and 36 percent, respectively. Together, the companies, which are affiliates of one another in South Korea but operate independently in the United States, accounted for more than 1 million sales for the first time, surpassing Nissan and nearly topping Honda. For December, sales rose 13 percent at Hyundai and 43 percent at Kia.

Volkswagen reported gains of 36 percent for December and 26 percent for the year, its best since 2002.

For all of 2011, analysts said, the industry sold about 12.8 million cars and trucks, a 10 percent increase from the 11.6 million sold in 2010. Sales are expected to climb this year, as well. The automotive research website Edmunds.com forecast 2012 sales of 13.6 million, while another site, TrueCar.com, expects 13.8 million. Either figure would represent the industry's best year since 2007, when sales totaled 16.1 million.

Online sales tax gets support

Bipartisan group is backing Senate bill allowing states to collect from Internet retailers

Lawmakers, looking to help cash-strapped local governments, are coalescing around legislation aimed at letting states require most online retailers and catalog-only companies to collect sales taxes from customers. The momentum is building nearly two decades after the U.S. Supreme Court barred states from requiring out-of-state companies to collect in-state taxes on sales. But the court left the door open for Congress to allow such collection through legislation.

The new effort is being boosted by a major crack in the nearly solid wall of opposition by Internet retailers. Amazon.com, the world's largest online retailer, wants standardized federal rules in the face of new online sales tax collection laws in California and a growing number of other states. "If I were president of an online retailer … I would look at this week in Washington, D.C., and I'd make my plans to start collecting sales taxes wherever I sold things in the United States," said Sen. Lamar Alexander, R-Tenn. Alexander was part of a bipartisan group of senators – five Democrats and five Republicans – who introduced legislation aimed at leveling the playing field among online, catalog and bricks-and-mortar retailers.

The bill, called the Marketplace Fairness Act, also would enable state and local governments to collect an estimated $23 billion in tax revenue each year for online, catalog and other so-called remote sales. "It's about closing a tax loophole," Alexander said.

Alexander, a former Tennessee governor, predicted that the bill would pass Congress because it is a bipartisan endeavor and is more flexible than previous efforts. The bill is similar to recent legislation introduced in the House. A 1992 Supreme Court ruling prohibits states from collecting sales taxes from retailers unless they have a physical presence in the state. The ruling has exempted most online sales, and the majority in Congress for years has allowed the no-tax rule to remain. But as online retailing has grown over the last decade, states have been trying to solve the problem on their own by expanding the definition of physical presence to include third-party affiliates, typically in-state websites that earn commissions by providing links to Amazon and other out-of-state retailers.

Nearly six months ago, California enacted a law requiring most online retailers with affiliates in the state to collect sales tax from purchases made by state residents. Amazon, which has fought such efforts in other states, eventually agreed to begin collecting the taxes starting in September 2012. Amazon said it “strongly supported” the Senate bill. But some high-tech groups and large online retailers, including San Jose- based eBay and Overstock.com, said they opposed the legislation. “It will leave a lot of very small retailers with a new burden to make it harder for them to compete,” said Brian Bieron, eBay’s senior director of federal government relations and global public policy.

The legislation would give states the authority to enact laws requiring retailers to collect sales tax for remote purchases as long as they adopted measures to make it easier for businesses to pay the taxes. Retailers have argued for years that it would be too complicated to collect state and local sales taxes because of differing definitions and the difficulty of submitting payments to thousands of jurisdictions.

The Senate bill would require states that want to require the collection of those sales taxes to join an existing 24-state group called the Streamlined Sales and Use Tax Agreement that has standardized definitions and provided a single location in each state to send all payments. States such as California, whose tax systems might be too complicated to join the group, still could be allowed to require retailers to collect taxes if they adopted similar tax simplification measures. Retailers that take in less than $500,000 in total remote sales each year would be exempt.

Amazon finds a new revenue source as Internet tax collector

Amazon.com for years has fought state efforts to force it to collect sales taxes from its customers. Now, instead of battling the tax man, the company is looking to profit -- by hiring itself out as an Internet tax collector. In an abrupt about-face, the company is now offering to handle sales-tax chores for merchants who sell products through its site for a fee equivalent to 2.9 percent of the taxes collected. The optional service, which is set to roll out Feb. 1, will be offered to Amazon's third-party vendors in all 50 states. It's a strategy that could reap millions of dollars in new revenue for Amazon, which has been among the most vocal opponents of government attempts to tax e-commerce.

Analysts said Amazon's shift is an acknowledgment that Internet retailers ultimately will have to play by the same rules as brick-and-mortar stores. It's also a recognition that there's money to be made in the process, said George Runner, a member of the California State Board of Equalization, the agency that administers sales tax. "This is what smart business people do," Runner said. "They are going to use whatever model they can to expand their business opportunities. They're very slick at it."

Seattle-based Amazon currently collects sales taxes from its own customers in Washington, New York, Kentucky, Kansas and North Dakota, as well as in some foreign countries where it does business. In the

U.S., Amazon and other online merchants have long contended that they're legally obligated to collect sales taxes only in states where they have a physical presence. However, the rise of Internet commerce has made it a target for wider taxation. U.S. Internet retail sales topped $176 billion last year and are expected to reach $279 billion by 2015, according to Forrester Research. Online sales currently account for about 9 percent of total retail sales, a share that's projected to triple over the next few decades. State and local governments are determined to force Amazon and others to pay up. "The reality is ... that they are going to be collecting sales tax," said Benjamin Schachter a senior analyst for Internet and interactive entertainment stocks for Macquarie Capital (USA), a New York investment bank.

In California, Amazon recently abandoned a much-criticized effort to repeal a new Internet sales tax law passed by the Legislature this year. Instead, the company cut a deal with the administration of Gov. Jerry Brown to start collecting and remitting California's 7.25 percent sales tax, plus local sales taxes, beginning Sept. 15, 2012. That agreement was a victory for traditional retailers, who say they've lost billions in sales to Internet merchants that sell identical merchandise free of sales taxes. But news that Amazon now is angling to make a buck from those levies has some fuming anew. Wal-Mart Stores, Target and major chains continue to push legislators to close legal loopholes that allow Amazon to dodge sales tax collection in most U.S. states. "It's hypocrisy of the highest order," said Jason Brewer, a spokesman for the Retail Industry Leaders Association in Arlington, Va. "Now, they're trying to profit from collecting sales tax everywhere else, while still digging in their heels from collecting for their own company." Amazon's new offer is aimed at businesses ranging from booksellers to major manufacturers.

Retail Sales / October

Retail sales rise fifth month in a row

Consumers are giving a modest lift to the economy. They spent more on trucks, electronics and building supplies in October to boost retail sales for the fifth straight month. The gains provide an encouraging start for the October-December quarter. They come just as separate reports show that wholesale prices are flattening and U.S. shoppers are spending more at Wal-Mart, the world's largest retailer.

Still, consumers might not be able to sustain their spending growth if unemployment remains high and pay raises scant. And Europe may be on the brink of a recession that could further slow U.S. growth next year. "The consumer has to come through this holiday season if we are going to get back to more decent growth rates, and the early readings are those households have hit the stores quite strongly," said Joel Naroff, chief economist at Naroff Economic Advisors.

Retail sales rose 0.5 percent from September to October, the Commerce Department said Healthy auto sales helped. Even without autos, sales rose by the most since March. And excluding autos and sales at gasoline stations, sales rose 0.7 percent, also the biggest increase since March. A rebound in consumer spending was the key reason why the economy grew at an annual rate of 2.5 percent in the July-September quarter. It was the best quarterly performance in a year. Economists said the October retail sales data suggest that the economy is growing at roughly the same pace in the final three months of the year.

Consumer spending fuels about 70 percent of economic activity. Stronger growth has helped calm fears that the U.S. economy might be at risk of another recession. Still, economists worry that the spending can't continue at the same pace. Over the summer, consumers spend more while earning less. Many had to dip into their savings to make up the difference. "Overall, the economy appears to be growing at a decent clip," said Paul Dales, a senior U.S. economist at Capital Economics. Still Dales added, "Consumption cannot grow at a faster rate than incomes indefinitely." One positive sign for the U.S. economy: Inflation pressures are starting to ease, largely because energy costs have declined.

U.S. companies paid less for wholesale goods for the first time since June. And excluding volatile food and energy costs, so-called "core" wholesale prices were unchanged.

Big day in online shopping

Sales rose 22% to $1.25 billion on Cyber Monday

Online shoppers spent record amounts on the Monday after the Thanksgiving holiday weekend, making it the biggest online shopping day in history.

Online sales rose 22 percent to $1.25 billion on Cyber Monday, when retailers ramp up online promotions, according to research firm comScore Inc. That makes it the biggest online shopping day ever, the research firm said. A year ago, Cyber Monday sales topped $1 billion for the first time.

IBM Benchmark, another company that tracks online sales, reported a 33 percent rise. The average order rose 2.6 percent to $193.24 this year, according to IBM Benchmark. It didn't give total dollar sales numbers for comparison. The company said about 80 percent of retailers offered online deals. The Cyber Monday numbers point to Americans' growing comfort with using their personal computers, tablets and smartphones to shop.

Over the past few years, big chains like Wal-Mart Stores Inc., the world's largest retailer, have offered more and better incentives, like hourly deals and free shipping, to capitalize on that trend. It's important for retailers to make good showing during the holiday shopping season, a time when they can make up to 40 percent of their annual revenue.

"Retailers that adopted a smarter approach to commerce, one that allowed them to swiftly adjust to the shifting shopping habits of their customers, whether in-store, online or via their mobile device, were able to fully benefit from this day and the entire holiday weekend, said John Squire, chief strategy officer, IBM Smarter Commerce. About 6.6 percent of online shoppers used a mobile device to shop, up from 2.3 percent last year. Apple Inc.'s iPhone and iPad were the top mobile devices for retail traffic, with Android devices coming in third.

Web traffic rose 28 percent on Monday, according to another firm, online content-delivery firm Akamai. The peak was at 9 p.m. Eastern Standard Time when shoppers across the country were online.

Retail Sales / December

Merchants post a holly jolly week of retail

Final period of year showed 5.3% gains in same-store sales

A flurry of post-Christmas bargain shopping helped drive sales higher in the last week of December, according to a report from a shopping mall trade group. Increased gift card use, mild weather and a federal holiday on Monday all contributed.

Sales at stores open at least one year rose 5.3 percent during the week ended Saturday compared with the same period a year ago. That report comes from the International Council of Shopping Centers and Goldman Sachs Weekly Chain Store Sales Index, which estimates sales for 24 major stores like Target Corp. and Costco Wholesale Corp.

Revenue at stores open at least a year rose 1.2 percent for the week ended Saturday compared with the previous week, according to the index. The metric is considered a key gauge of a retailer's health because it excludes results from stores recently opened or closed.

As a result of the latest surge, the group increased its December sales growth estimate to a range of 4 percent to 4.5 percent. Previously the council expected December sales to rise by 3.5 percent to 4 percent.

Housing poised for turnaround

Homebuilders find niche in building apartment units

The depressed housing market has held the economy back for four years. No longer. Home construction has finally begun a gradual comeback and should add to the nation's economic growth in 2012, a turning point in the recovery from the Great Recession.

The main reason appears to be a positive consequence of the weak economy: Apartments are being built almost twice as fast as two years ago. Renting is the only option for many people who have lost their jobs, their homes or both. Builders in November broke ground on homes - houses and apartments alike - at an annual rate of 685,000, the government said recently. That was a 9.3 percent jump from October and the fastest pace since April 2010.

The numbers show how far the housing industry has come and still has to go:

- Builders should start at least 600,000 homes this year. That's up from 587,000 last year and 554,000 in 2009 - the worst year on record. In a healthy market, economists say, about 1.2 million homes are started each year.

- The pace of apartment construction has soared. About 175,000 will be started this year, also roughly half the number in a healthy economy. But it's far more than the 97,000 apartments begun in 2009.

- Single-family home construction, which accounts for about 70 percent of the housing industry, has essentially stalled for three years. This year will probably turn out to be the worst in the half-century records have been kept.

Construction of single-family homes this year could reach 440,000. That would be below last year's 471,000. In a good economy, builders would break ground on about 840,000 homes. New homes are 20 percent of the housing market but have an outsize economic impact. Each home built creates an average of three jobs for a year and generates about $90,000 in taxes, according to the National Association of Home Builders.

Since the recession began in December 2007, housing has subtracted between 0.5 and 1.1 percentage points from U.S. economic growth each year. Cuts in spending by homeowners have further reduced growth. But economists say apartments are going up so fast that housing should add to economic growth this year, even if fewer families are buying houses. The U.S. economy grew at a 2 percent clip last quarter. "Finally, it appears that the process of healing is under way," says Joel Naroff, president and chief economist at Naroff Economics.

Patrick Newport and Michelle Valverde, U.S. economists at IHS Global Insight, said in a note to clients that the figures demonstrate that the housing industry is "finally getting off the mat." The industry seems to think so, too. A survey of industry sentiment recently found builders were more optimistic than at any time since May 2010.

But the numbers remain weak, even though mortgage rates are near record lows and home prices have fallen by a third since 2006. Tighter lending standards are preventing many families from buying houses, and diminished prices on single-family homes have given the industry little reason to build more.

Builders are also competing with foreclosures, which hold prices down. Yet they have found a way to make money - by serving the rising demand for rental apartments. The average rent has risen 2.4 percent this year to $1,004 a month, according to the real estate data firm Reis Inc. It rose 1 percent last year and fell 2.7 percent in 2009.

JOBS

Unemployment fell in 43 states in November

Unemployment rates fell in 43 states in November, the most number of states to report such declines in eight years. The falling state rates reflect the brightening jobs picture nationally. The U.S. unemployment rate fell sharply in November to 8.6 percent, the lowest since March 2009. The economy has generated 100,000 or more jobs five months in a row — the first time that's happened since 2006, before the Great Recession.

Only three states reported higher unemployment rates in November, the Labor Department said. Four states showed no change. Nevada for the 18th straight month had the highest state unemployment rate: 13 percent. It was followed by California at 11.3 percent. North Dakota again enjoyed the lowest unemployment rate: 3.4 percent. It was followed by Nebraska at 4.1 percent and South Dakota at 4.3 percent.

Microchip companies foresee slower growth

Only 41 percent of executives anticipate revenue growth of more than 5 percent

Microchip company executives expect the economy's continuing sluggishness to put a drag on their finances as well as their spending on new hires, capital improvements and research and development efforts next year, according to an industry survey. Of 155 executives with Silicon Valley and other chip companies who were surveyed in October and November by the audit, tax and advisory firm KPMG, just 41 percent said they expect their revenue to grow by more than 5 percent in 2012. That compares with 78 percent who had predicted to see that rate of growth in 2010 and 87 percent in 2009, according to KPMG, which has done the survey for seven years.

Optimism about chip-company bottom lines has waned, too. While 30 percent of the surveyed executives anticipate profits will increase by more than 5 percent next year, that's down from 37 percent last year. As a result, the executives said they plan to carefully control expenses. Only 27 percent, compared with 46 percent a year ago, anticipate capital spending to increase by more than five percent. Just 33 percent of them expect more than a five percent rise in R&D outlays, compared with 47 percent a year ago. And 19 percent think their workforces will expand by more than 5 percent, compared with 29 percent who had predicted that rate of growth in 2010.

"It is not unexpected to see the industry take a breath after two strong years following the economic and industry downturn," concluded Gary Matuszak, who chairs KPMG technology, media and telecommunication's practice. While many chip companies still expect their businesses to grow next year, many of them "remain very apprehensive about the direction of the economy." At Santa Clara-based Intel, the world's biggest chipmaker, "our early plans are for an incremental increase in hiring of a few percentage points," said spokesman Jon Carvill, noting that the company this year bolstered its workforce by about 17,000 in part through corporate acquisitions. Beyond 2012, he added, Intel plans "significant" increases in its manufacturing-related workforce.

Connecticut technology research firm Gartner also foresees only modest growth for the chip industry in 2012. In a report earlier this month it predicted worldwide chip sales would be about $309 billion next year, up 2.2 percent from 2011. Gartner previously had expected 2012 sales to increase 4.6 percent. Gartner's revised estimate was partly prompted by the recent floods in Thailand, which limited hard drive production and caused a slowdown in personal computer sales.

Another factor weighing on the industry is counterfeiting, according to KPMG. It found that nearly two thirds of the chip executives it surveyed feared the proliferation of bogus chips will cut their sales by at least three percent next year. In addition, 30 percent of the respondents expect their costs to rise by more than five percent due to infringements of their intellectual property.

UCLA Anderson School Forecast

South Bay leads the nation in job growth

The South Bay led the nation in job growth over the past year, according to a new government report - and economists predict the region's surge will power a Bay Area expansion. During the 12 months that ended in October, the South Bay job market grew by 3.2 percent, the U.S. Bureau of Labor Statistics reported recently. The pace of job growth in the South Bay was nearly triple the nationwide rate and almost double the growth rate for California. And improvement in the Bay Area job market is likely to continue, according to the UCLA Anderson Forecast.

"The Bay Area will be the fastest-growing economy in California in the coming few years, based on employment and income growth," said Jerry Nickelsburg, a senior economist with the Anderson Forecast. This time around, the growth has a better foundation than during the dot-com bubble, whose spectacular flameouts included Pets.com, Boo.com and Startups.com. Companies such as Apple, Google, Facebook, LinkedIn and Zynga have real sales and real product plans, notes Stephen Levy, director of the Palo Alto-based Center for Continuing Study of the California Economy.

Brisk pace could slow

"This rebound is for real in the Bay Area," Levy said. "The wave of tech hiring is continuing. There are job openings all over the place in the South Bay." That should produce a ripple effect for the nine-county region, said Jeffrey Michael, director of the Stockton-based Business Forecasting Center at University of the Pacific. "The South Bay has been at the front of the recovery and over time we expect the rest of the Bay Area to join Silicon Valley," Michael said.

Although the South Bay was the national leader among major metro centers over the past year, it was closely followed by energy nexus Houston, which powered to a 3.1 percent jobs gain; and by tech and trade hub Seattle, up 2.3 percent. The weakest large urban center was Atlanta, with a job base that eroded by 1 percent.

Employment growth across California, which gained 39,200 payroll jobs in September and 25,700 in October, has encouraged economists, who see those two months as springboards to propel further expansion. "Although other indicators did not predict stronger growth in payroll employment, there it was" in September, Nickelsburg said. "October job growth has followed course, yielding the first signs of a nascent new recovery."

Yet analysts warn the brisk pace could slow. They foresee a pathway to full recovery that's dotted with potholes.

"The current forecast is for the surge in employment to abate and slow growth to persist on average through 2012," Nickelsburg said. Double-digit unemployment will haunt California in 2012 and will still average 10.5 percent during 2013, according to the Anderson Forecast. Some economists think 10 percent unemployment will continue beyond 2013. "California will have double-digit unemployment well into 2014, possibly all the way through 2014," Michael said.

Is tech surge enough?

While the tech surge is a welcome counterpoint to dreary sectors of the Bay Area economy, tech's weak cousins will have to become stronger for the overall economy to significantly improve. And many economists don't see that happening soon. "The Bay Area is growing, but the job market is not on fire," said Jon Haveman, chief economist with the Bay Area Council's Economic Institute. "It will grow more quickly than the rest of the nation, but the pace will be much slower than what we would like."

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