CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

September 4, 2012

The Honorable City Council
Palo Alto, California

City of Palo Alto Sales Tax Digest Summary First Quarter Sales (January - March 2012)

This is an informational report, and no action is required.

BACKGROUND

Sales and use tax represents about 14 percent, 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 Policy and Services 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 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 first quarter sales (January through March 2012). 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 second quarter sales (April through June 2012) should be available by November 2012. ASD advises that in mid-September, it should receive information from the State on aggregate sales and use tax receipts for second quarter 2012.

[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 first quarter ending March 2012 increased by approximately $453,200, or 9.6 percent, (including pool allocations) compared to the first quarter ending March 2011.[2] For all jurisdictions in Santa Clara County, sales and use tax revenue for the first quarter ending March 2012 increased by $9.6 million, or 13.1 percent, compared to the first quarter ending March 2011.

- Statewide, every region in California experienced an increase in sales and use tax revenue for the year ending March 2012, compared to the prior year ending March 2011. Statewide sales and use tax revenue has shown growth of 9.3 percent during the first quarter ending March 2012 compared to the first quarter ending March 2011.

- In Palo Alto, sales and use tax revenue totaled $21.5 million for the year ending March 2012, an increase of 9.0 percent from $19.7 million in the prior year ending March 2011.[2] 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 Overview (Attachment B), MuniServices discusses economic influences including national economic trends, auto sales, retail sales, housing, and national and state forecast information that may affect the City's sales and use tax revenue.

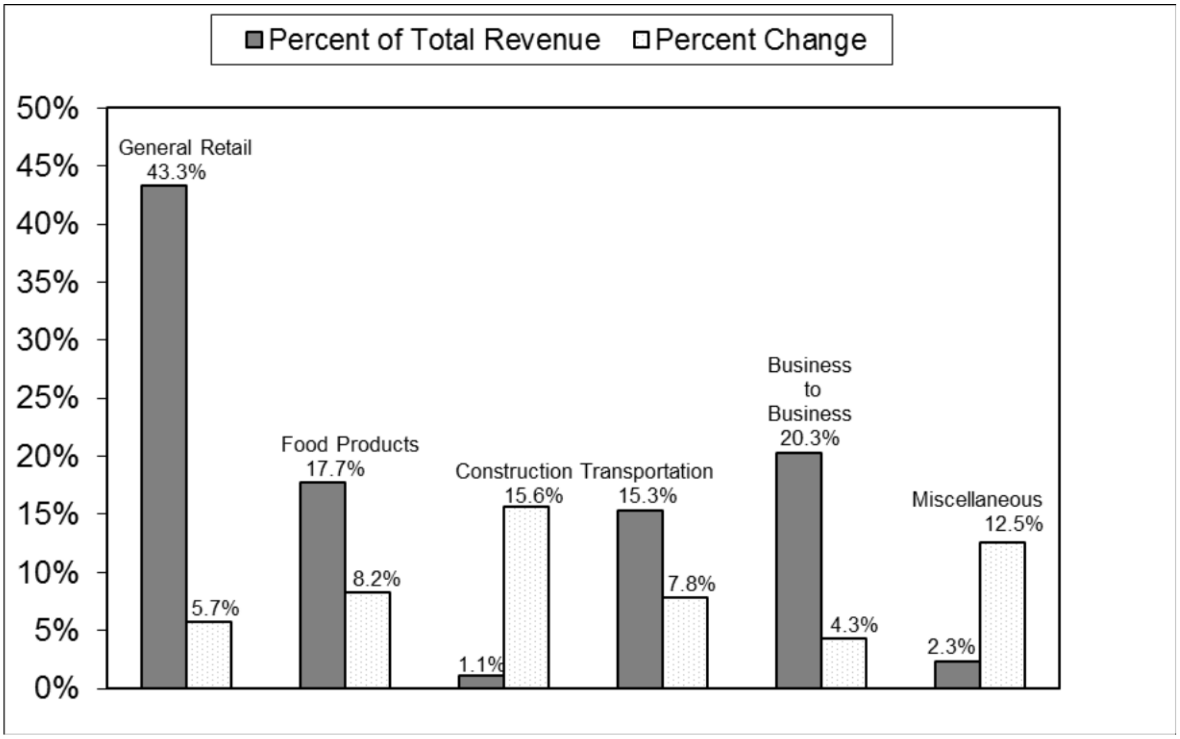
Preliminary estimates from the State of California Employment Development Department show the June 2012 unemployment rate in Santa Clara County at 8.7 percent and Palo Alto at 4.6 percent.

Economic Category Analysis

MuniServices' analysis of six economic categories, for the year ending March 2012, shows that General Retail comprised the largest percentage of Palo Alto's sales and use tax revenue and experienced 5.7 percent growth. Business to business experienced a 4.3 percent increase and comprised 20.3 percent of total revenues. Transportation experienced a 7.8 percent increase and comprised 15.3 percent of total revenues.

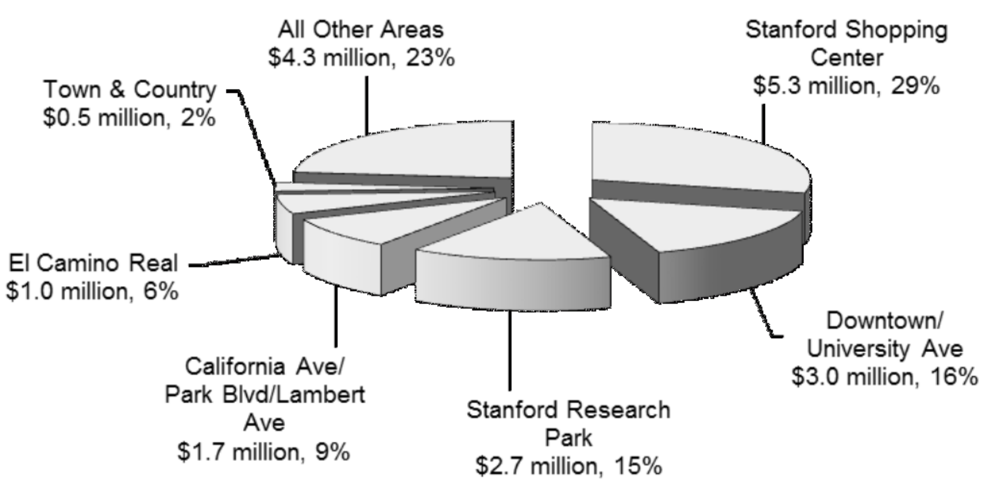
[2] Excluding pool allocations and adjusting for prior period and late payments, Palo Alto's sales and use tax revenue for the first quarter ending March 2012 increased by 9.0 percent compared to the first quarter ending March 2011. On a yearly basis, Palo Alto's sales and use tax revenue for the year ending March 2012, increased by 6.4 percent compared to the prior year ending March 2011.

Exhibit 1 - Comparison of Palo Alto's Sales and Use Tax Revenue and Percent Change by Economic Category for the Year Ending March 2012



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 March 2012 (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 during the first quarter 2012 was 8.25 percent, and the City should receive 1 percent of every taxable transaction. Effective July 1, 2012, the sales and use tax rate in Palo Alto increased to 8.375 percent.

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 Overview (July 2012) (PDF)

Department Head: Jim Pelletier, City Auditor

Attachment A

City of Palo Alto
Sales Tax Digest Summary
Collections through June 2012
Sales through March 2012 (2012Q1)

California Overview

The percent change in cash receipts from the prior year was 9.2% statewide, 9.8% in Northern California and 8.7% 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 1st Quarter 2012 by 7.7% statewide, 7.5% in Northern California and increased by 7.4% in Southern California.

City of Palo Alto

For the year ended 1st Quarter 2012, sales tax cash receipts for the City grew by 9.0% from the prior year. On a quarterly basis, sales tax revenues increased by 9.6% from 1st Quarter 2011 to 1st Quarter 2012. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments.

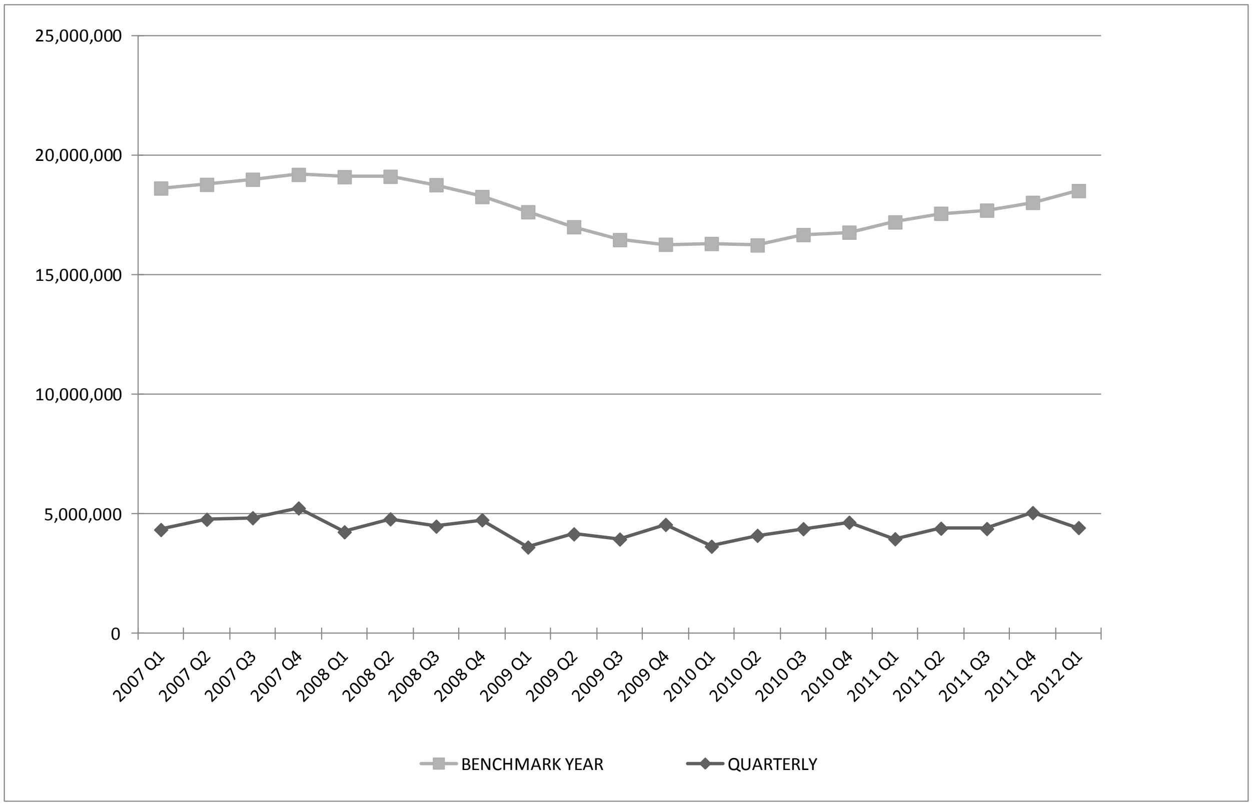
Excluding state and county pools and adjusting for anomalies (payments for prior periods) and late payments, local sales tax increased by 6.4% for the year ended 1st Quarter 2012 from the prior year. On a quarterly basis, sales tax activity grew by 9.0% in 1st Quarter 2012 compared to 1st Quarter 2011.

Regional Overview

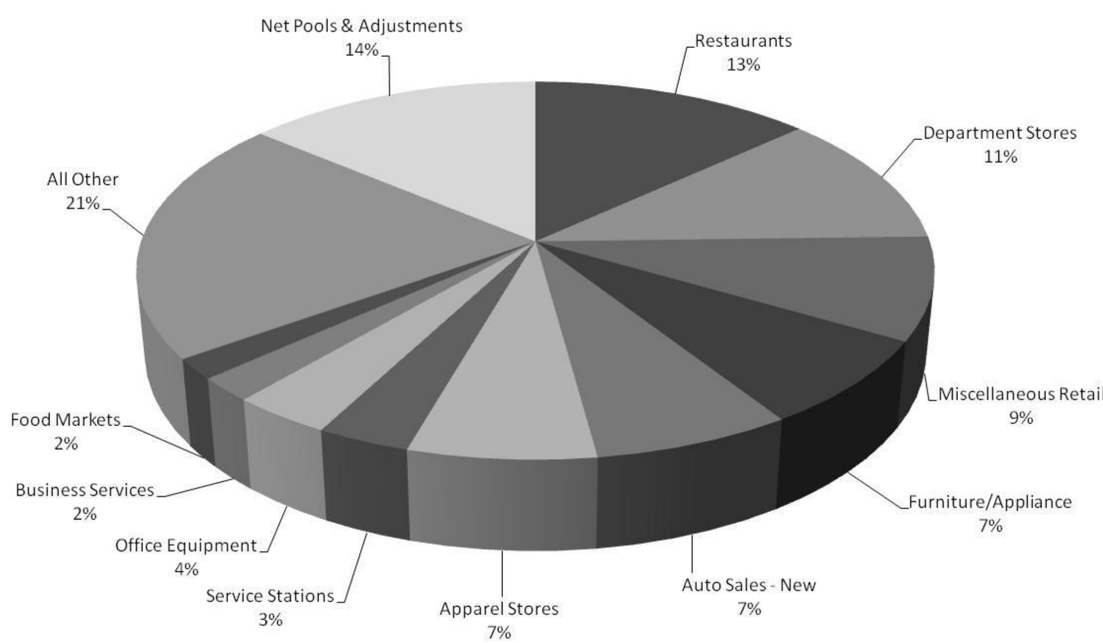
This seven-region comparison includes estimated payments and excludes net pools and adjustments.

ECONOMIC CATEGORY ANALYSIS FOR YEAR ENDED 1st QUARTER 2012									
% of Total / % Change	**City of Palo Alto**	**California Statewide**	**S.F. Bay Area**	**Sacramento Valley**	**Central Valley**	**South Coast**	**Inland Empire**	**North Coast**	**Central Coast**
General Retail	43.3 / 5.7	29.7 / 4.9	29.1 / 5.3	30.2 / 2.5	31.6 / 5.6	29.5 / 4.9	26.0 / 6.1	31.4 / 4.6	32.9 / 2.5
Food Products	17.7 / 8.2	19.1 / 6.5	19.8 / 7.0	17.2 / 4.3	16.4 / 4.8	19.6 / 6.7	13.9 / 8.0	17.2 / 2.0	29.8 / 5.0
Construction	1.1 / 15.6	8.3 / 4.8	8.2 / 7.3	9.7 / 2.8	10.7 / 10.6	7.8 / 2.9	7.7 / 4.5	12.6 / 4.9	8.6 / -3.4
Transportation	15.3 / 7.8	24 / 14.5	21.0 / 14.0	27.8 / 15.3	26.4 / 18.2	24.5 / 13.9	24.6 / 17.2	28.9 / 14.7	21.8 / 11.5
Business to Business	20.3 / 4.3	17.7 / 7.1	20.7 / 6.2	13.7 / 4.4	13.7 / 13.2	17.4 / 7.1	24.0 / 6.8	8.8 / 9.6	5.9 / 3.2
Miscellaneous	2.3 / 12.5	1.2 / -2.8	1.2 / 1.3	1.3 / 10.5	1.2 / -7.8	1.2 / -4.5	3.8 / -6.2	1.1 / 20.2	1.1 / -25.2
Total	**100.0 / 6.4**	**100.0 / 7.7**	**100.0 / 7.7**	**100.0 / 6.5**	**100.0 / 9.9**	**100.0 / 7.4**	**100.0 / 8.4**	**100.0 / 7.5**	**100.0 / 4.1**
ECONOMIC SEGMENT ANALYSIS FOR YEAR ENDED 1st QUARTER 2012									
	City of Palo Alto	**California Statewide**	**S.F. Bay Area**	**Sacramento Valley**	**Central Valley**	**South Coast**	**Inland Empire**	**North Coast**	**Central Coast**
Largest Segment	**Restaurants**	**Restaurants**	**Restaurants**	**Department Stores**	**Department Stores**	**Restaurants**	**Service Stations**	**Department Stores**	**Restaurants**
% of Total / % Change	15.4 / 10.4	13.2 / 6.9	13.8 / 7.9	12.7 / 2.5	14.7 / 3.8	14.0 / 6.9	11.1 / 17.9	14.1 / 2.1	20.0 / 4.6
2nd Largest Segment	**Department Stores**	**Service Stations**	**Department Stores**	**Service Stations**	**Service Stations**	**Service Stations**	**Restaurants**	**Service Stations**	**Service Stations**
% of Total / % Change	13.2 / 4.9	10.7 / 19.6	9.6 / 4.5	11.1 / 18.8	12.8 / 22.5	10.9 / 18.9	10.4 / 6.5	13.6 / 17.4	10.1 / 15.9
3rd Largest Segment	**Electronic Equipment**	**Department Stores**	**Service Stations**	**Restaurants**	**Restaurants**	**Department Stores**	**Office Equipment**	**Restaurants**	**Misc Retail**
% of Total / % Change	11.9 / 4.1	10.7 / 4.4	9.4 / 20.6	10.6 / 3.9	9.7 / 5.7	10.4 / 4.7	9.8 / 10.1	9.4 / 2.1	10.1 / -0.8

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



Net Cash Receipts for Benchmark Year 1st Quarter 2012: $21,528,252

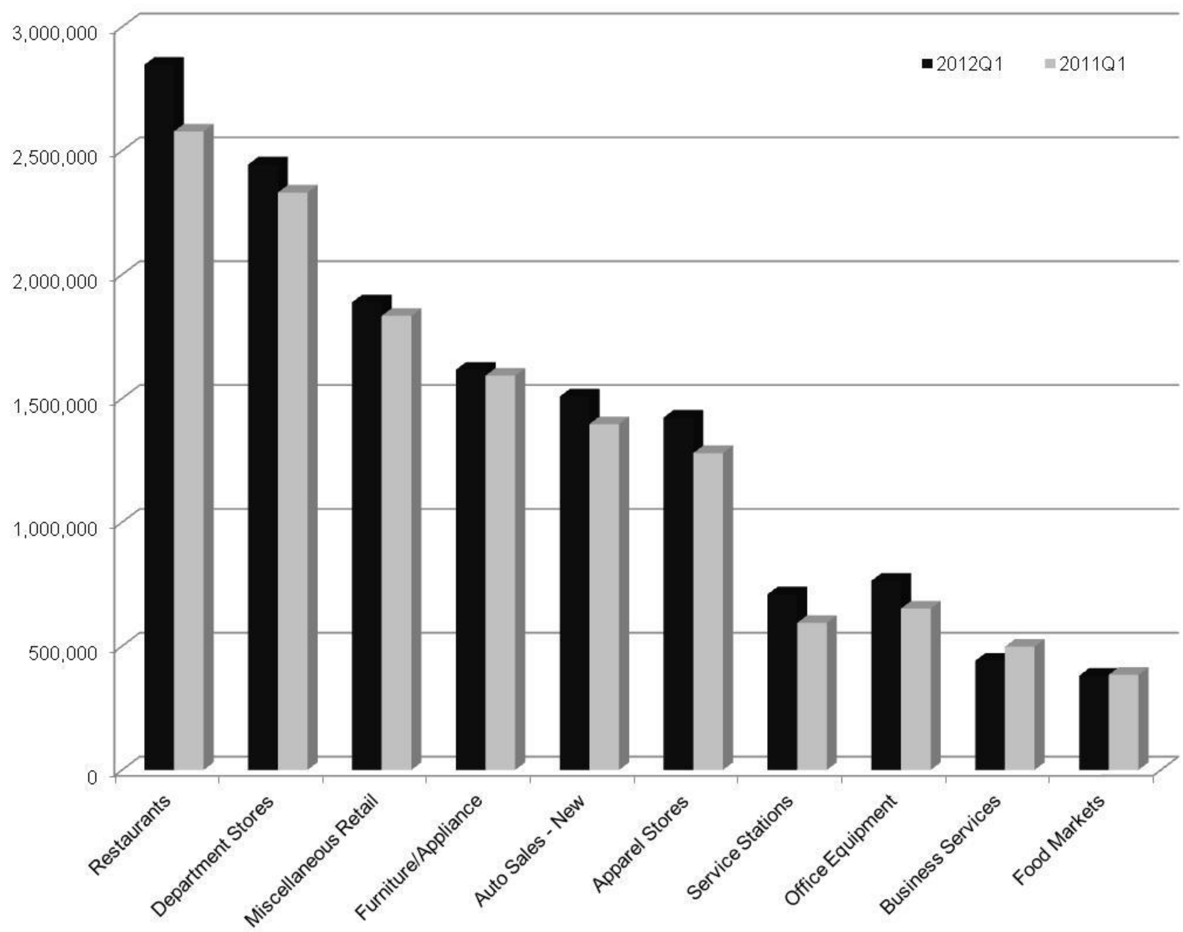


TOP 25 SALES/USE TAX CONTRIBUTORS

The following list identifies Palo Alto's Top 25 Sales/Use Tax contributors. The list is in alphabetical order and represents the year ended 1st Quarter 2012. The Top 25 Sales/Use Tax contributors generate 51.6% of Palo Alto's total sales and use tax revenue.

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

Sales Tax from Largest 10 Non-confidential Economic Segments



Historical Analysis by Calendar Quarter

Economic Category	%	2012Q1	2011Q4	2011Q3	2011Q2	2011Q1	2010Q4	2010Q3	2010Q2	2010Q1
General Retail	32.8%	1,701,757	2,440,953	1,886,520	1,984,860	1,573,474	2,275,627	1,810,271	1,864,922	1,473,821
Business To Business	20.6%	1,064,996	932,723	842,771	842,709	925,263	887,037	1,006,576	788,373	849,181
Food Products	15.8%	816,336	838,138	799,167	806,987	740,594	769,253	726,360	739,629	666,388
Transportation	13.6%	703,039	682,786	694,998	619,897	593,452	590,209	576,597	551,313	534,793
Miscellaneous	1.8%	94,397	98,550	117,132	100,653	87,535	75,077	217,465	78,340	67,673
Construction	0.9%	47,432	62,282	46,843	44,589	38,765	54,645	44,171	40,415	37,914
Net Pools & Adjustments	14.6%	754,099	725,000	933,424	845,214	769,789	508,973	782,981	626,593	487,801
Total	100.0%	5,182,056	5,780,432	5,320,855	5,244,909	4,728,872	5,160,821	5,164,421	4,689,585	4,117,571

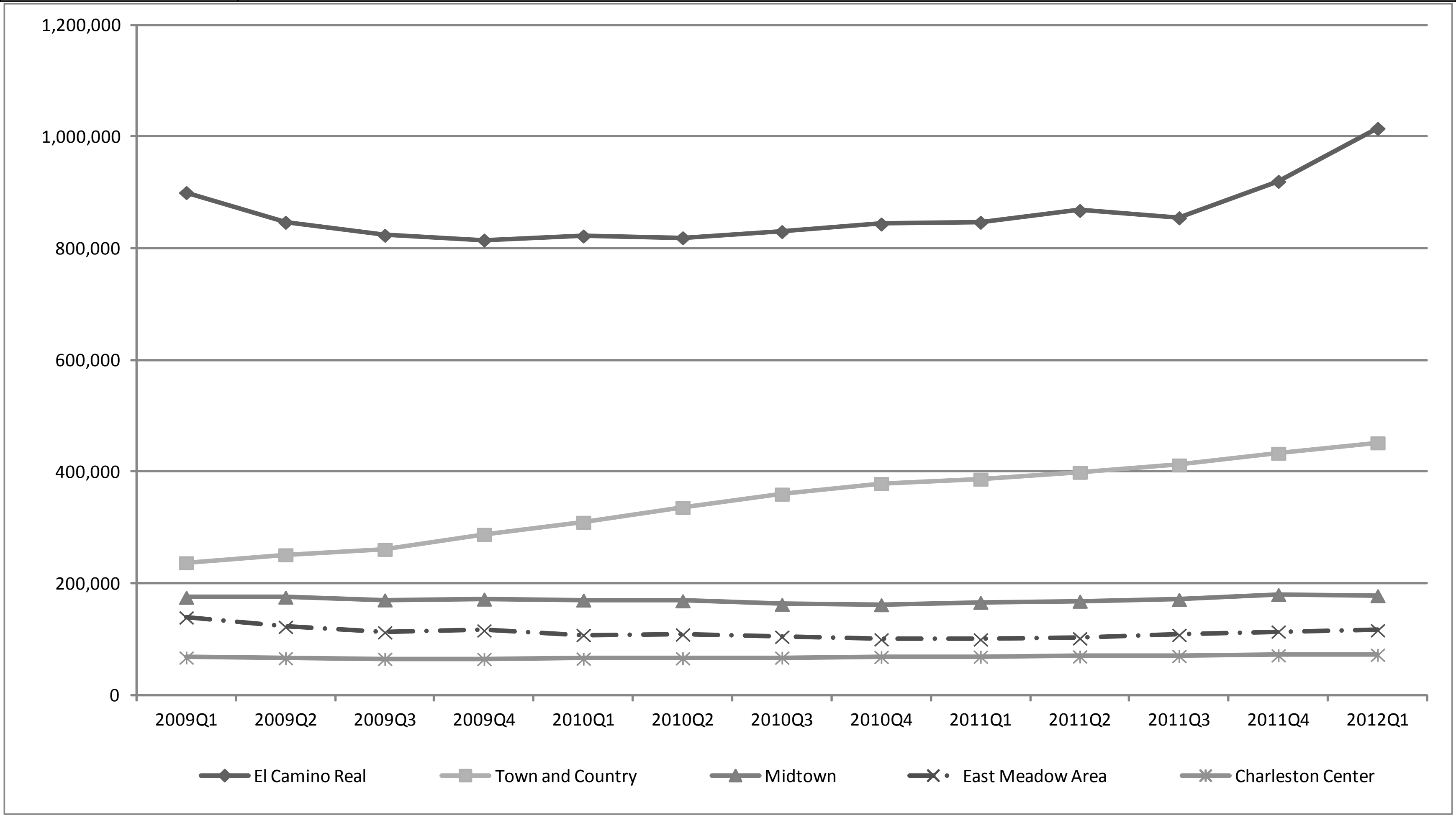
Economic Segments	%	2012Q1	2011Q4	2011Q3	2011Q2	2011Q1	2010Q4	2010Q3	2010Q2	2010Q1
Restaurants	13.8%	714,487	783,595	689,568	705,459	639,353	651,614	622,517	636,566	568,305
Department Stores	9.4%	488,132	724,274	563,373	608,784	474,566	748,885	541,942	565,706	455,378
Miscellaneous Retail	7.4%	382,336	573,750	455,335	482,723	399,243	584,895	396,580	381,222	325,512
Furniture/Appliance	6.7%	347,112	488,492	385,236	392,126	301,427	421,877	447,946	416,128	282,989
Apparel Stores	6.5%	335,069	429,491	321,296	333,697	266,990	387,682	299,340	321,787	267,315
Service Stations	3.4%	178,409	171,472	160,037	181,065	158,421	147,520	143,233	140,859	139,906
Business Services	1.9%	99,210	104,348	104,234	105,507	100,241	146,732	112,153	143,241	110,989
Food Markets	1.7%	90,636	101,023	98,054	89,530	91,274	105,573	93,651	92,036	86,892
Auto Parts/Repair	0.9%	46,718	48,340	49,977	51,743	47,157	43,537	45,689	40,037	39,150
Leasing	0.7%	37,116	38,854	42,654	35,131	34,857	36,962	40,480	36,129	34,760
Bldg.Matls-Retail	0.6%	31,168	44,402	41,338	38,236	34,016	48,591	39,747	35,783	33,297
Liquor Stores	0.2%	11,199	12,838	11,321	11,319	9,967	12,060	10,192	11,027	11,162
Miscellaneous Other	0.1%	6,634	9,046	9,857	8,724	6,458	8,714	5,751	7,689	6,550
Heavy Industry	0.1%	7,110	22,227	8,349	8,029	3,833	3,580	3,288	4,887	4,782
Bldg.Matls-Whsle	0.3%	16,264	17,880	5,505	6,353	4,749	6,054	4,424	4,632	4,617
All Other	31.6%	1,636,357	1,485,400	1,441,297	1,341,269	1,386,531	1,297,572	1,574,507	1,225,263	1,258,166
Net Pools & Adjustments	14.6%	754,099	725,000	933,424	845,214	769,789	508,973	782,981	626,593	487,801
Total	100.0%	5,182,056	5,780,432	5,320,855	5,244,909	4,728,872	5,160,821	5,164,421	4,689,585	4,117,571

*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.

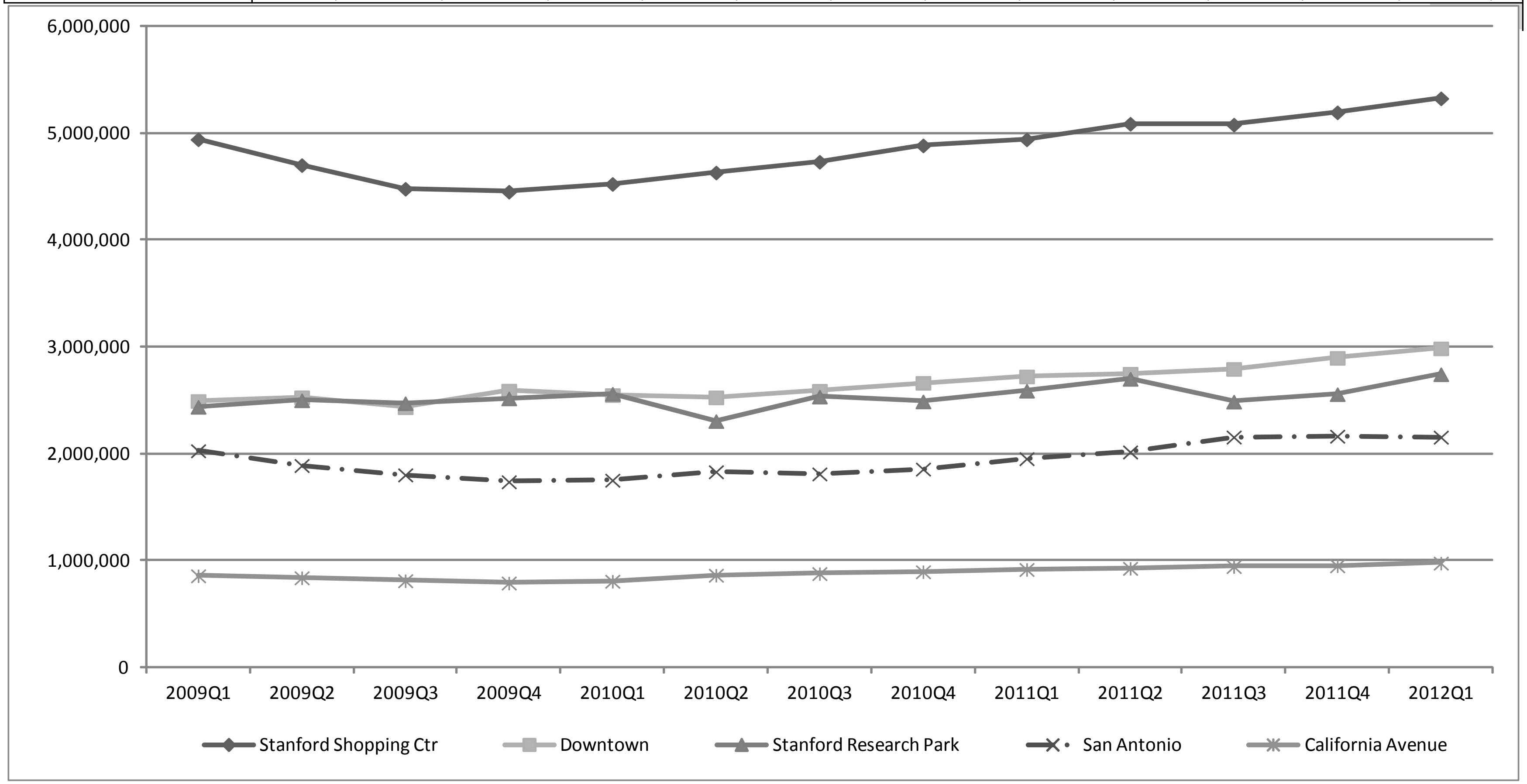
Quarterly Analysis by Economic Category, Total and Segments: Change from 2011Q1 to 2012Q1

	General Retail	Food Products	Transportation	Construction	Business to Business	Miscellaneous	2011/4 Total	2010/4 Total	% Chg	Largest Gain	Second Largest Gain	Largest Decline	Second Largest Decline
Campbell	-0.5%	11.1%	31.4%	14.1%	-2.7%	-6.0%	1,908,849	1,737,133	**9.9%**	Service Stations	Bldg.Matls-Whsle	Business Services	Furniture/Appliance
Cupertino	1.7%	10.7%	0.5%	27.8%	9.4%	-13.4%	4,768,803	4,400,559	**8.4%**	Business Services	Office Equipment	Heavy Industry	Health & Government
Gilroy	7.5%	4.3%	-2.8%	-0.7%	9.6%	-67.1%	2,645,837	2,571,912	**2.9%**	Apparel Stores	Misc. Vehicle Sales	Service Stations	Auto Sales - New
Los Altos	0.8%	8.6%	5.5%	31.5%	-25.7%	-24.4%	481,791	461,761	**4.3%**	Restaurants	Service Stations	Miscellaneous Retail	Auto Parts/Repair
Los Gatos	-28.5%	13.0%	-5.6%	-15.7%	5.5%	-5.1%	1,752,747	2,096,946	**-16.4%**	Restaurants	Furniture/Appliance	Miscellaneous Retail	Auto Sales - New
Milpitas	4.9%	6.1%	19.0%	93.9%	70.9%	18.5%	4,342,813	3,350,520	**29.6%**	Electronic Equipment	Bldg.Matls-Whsle	Chemical Products	Business Services
Morgan Hill	2.8%	9.9%	33.8%	7.8%	20.4%	-0.9%	1,461,625	1,233,635	**18.5%**	Auto Sales - New	Electronic Equipment	Business Services	Misc. Vehicle Sales
Mountain View	-2.1%	7.8%	7.6%	32.3%	-2.6%	-5.9%	3,124,612	3,048,614	**2.5%**	Service Stations	Restaurants	Electronic Equipment	Department Stores
Palo Alto	7.4%	9.8%	3.5%	19.8%	14.7%	6.4%	4,427,952	4,063,567	**9.0%**	Electronic Equipment	Restaurants	Misc. Vehicle Sales	Miscellaneous Retail
San Jose	3.6%	5.4%	14.5%	9.1%	10.6%	11.7%	29,967,086	27,571,307	**8.7%**	Office Equipment	Auto Sales - New	Light Industry	Food Markets
Santa Clara	8.9%	4.5%	10.3%	19.3%	-4.5%	5.6%	8,082,655	7,762,867	**4.1%**	Office Equipment	Auto Sales - New	Electronic Equipment	Heavy Industry
Santa Clara Co.	-2.0%	9.3%	-25.5%	51.4%	-33.8%	22.8%	803,303	795,426	**1.0%**	Bldg.Matls-Whsle	Health & Government	Misc. Vehicle Sales	Electronic Equipment
Saratoga	-18.6%	7.7%	-3.1%	93.9%	3.8%	5.5%	206,048	203,626	**1.2%**	Restaurants	Bldg.Matls-Retail	Furniture/Appliance	Service Stations
Sunnyvale	63.1%	8.5%	5.2%	5.8%	18.4%	-9.5%	7,195,011	6,016,855	**19.6%**	Miscellaneous Retail	Electronic Equipment	Leasing	Health & Government

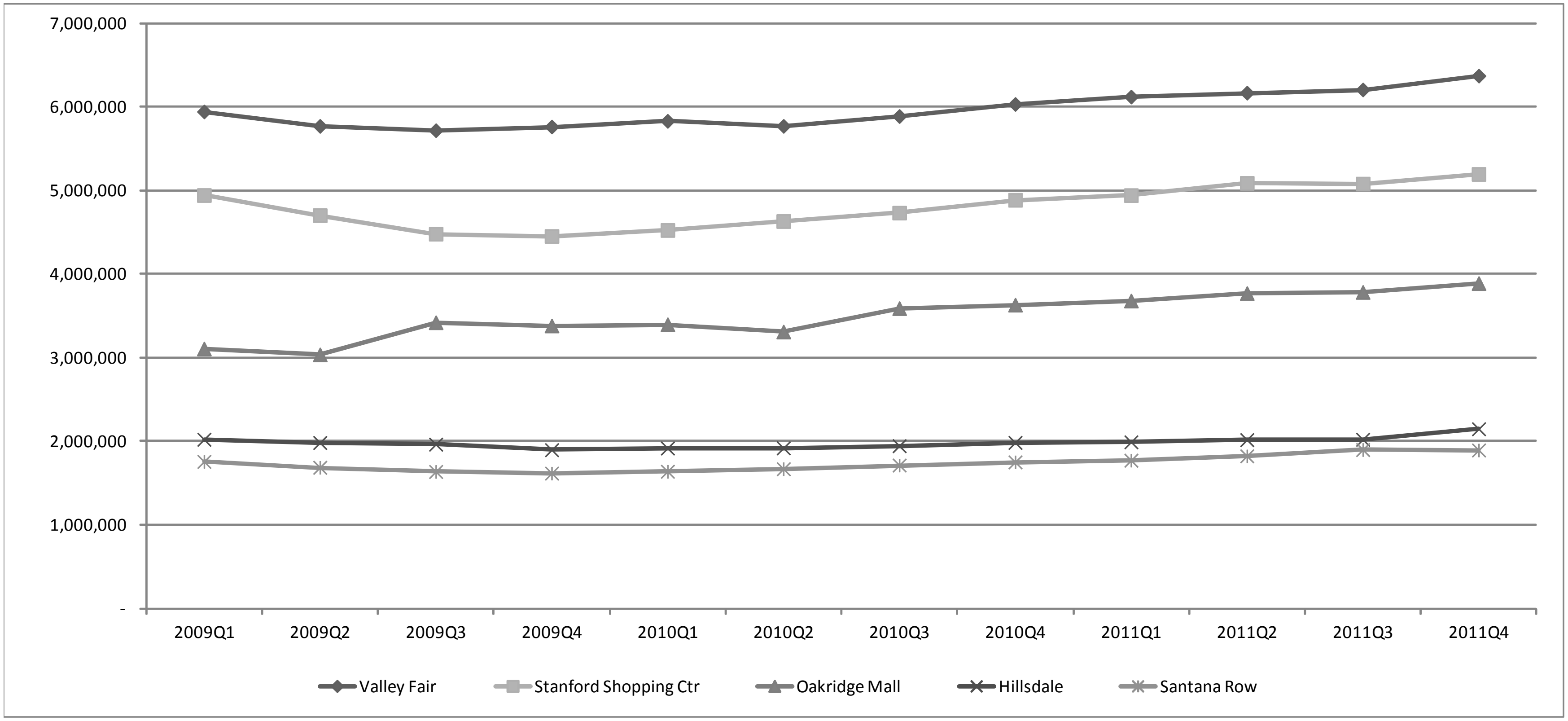
City of Palo Alto - Selected Geographic Areas of the City Benchmark Year 1st Quarter 2012													
	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1
El Camino Real	900,018	846,897	823,627	814,940	822,245	818,947	830,152	843,626	846,897	867,868	854,828	920,020	1,014,867
Town and Country	237,307	251,608	261,294	288,103	309,848	336,444	360,254	379,066	386,944	399,378	412,361	433,313	451,982
Midtown	175,471	175,723	170,741	172,297	170,517	169,297	162,869	162,122	166,440	168,537	171,719	180,415	178,344
East Meadow Area	139,391	122,493	112,819	116,128	107,931	108,922	104,777	100,155	100,032	102,028	108,176	114,083	116,558
Charleston Center	67,632	66,529	65,328	64,981	65,642	66,446	67,447	68,693	69,150	69,606	70,301	71,555	72,602



City of Palo Alto - Selected Geographic Areas of the City Benchmark Year 1st Quarter 2012	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1
Stanford Shopping Ctr	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	5,194,491	5,325,435
Downtown	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	2,897,003	2,986,093
Stanford Research Park	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	2,557,399	2,744,058
San Antonio	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	2,164,335	2,155,721
California Avenue	858,391	839,591	812,294	790,954	807,490	863,730	879,364	895,989	917,851	928,031	945,340	952,300	976,897



City of Palo Alto - Regional Shopping Mall Comparison Benchmark Year 1st Quarter 2012	2009Q1	2009Q2	2009Q3	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1
Valley Fair	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	6,370,656	6,559,394
Stanford Shopping Ctr	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	5,194,491	5,325,435
Oakridge Mall	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	3,888,402	3,928,855
Hillsdale	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	2,145,957	2,241,553
Santana Row	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	1,892,070	1,900,328



MUNISERVICES

Economic Overview

2Q2012 News

Economy growing - just slowly

First-quarter stalls 'will be temporary,' analyst predicts

Don't panic yet. The government reported recently that the economy got off to a tepid start this year, but that doesn't foreshadow a repeat of the near-standstill that happened in 2011. "The economy is firmly on a growth trajectory," said Sung Won Sohn, an economics professor at California State University's Smith School of Business. "The first-quarter slowdown will be temporary." Still, the January-March report was discouraging. Economists had expected gross domestic product – the broadest gauge of economic output – to expand at a 2.5 percent annual rate for the first three months of the year. Instead, the Commerce Department said it was 2.2 percent, mainly because of government budget-cutting and a slowdown in business investment.

And some of the January-March growth, meager as it was, probably came at the expense of the current quarter. An unseasonably warm winter pulled car buyers into showrooms earlier than usual. The same was true for housing construction. That's one reason it jumped at a 19 percent pace from January through March.

Economists doubt consumers can keep spending as freely as they did in the first three months of this year: an annual pace that was 2.9 percent faster than in the previous quarter and the fastest in more than a year. They probably can't afford to. Americans' after-tax income rose just 0.6 percent in the first three months compared with a year earlier. That was the puniest pay increase in two years. People spent more in part because they socked away less. The savings rate fell to 3.9 percent of after-tax income. That was down from 4.5 percent. Economists worry that people won't keep spending more unless their income grows.

Fed Chairman Ben Bernanke "has created the impression that if the economy stumbles, he'll be there to hold your hand," Rosenberg said. The lackluster first-quarter growth follows government reports that hiring slowed sharply in March and the number of people seeking unemployment benefits reached a three-month high. With 12.7 million people unemployed, today's economy needs much faster growth to boost hiring. Growth would have to be roughly 4 percent for a full year to lower the unemployment rate, now 8.2 percent, by 1 percentage point.

In 2011, a series of setbacks struck the economy. Gas prices rose sharply. An earthquake in Japan shuttered factories there and cut off supplies to U.S. manufacturers. A standoff in Washington brought the federal government to the brink of default, rattling investors and consumer confidence. And Europe's debt crisis threatened to diminish U.S. exports and further spook investors.

Auto Sales Trends

Baby boomers' retirement savings may have taken a hit during the financial crisis. Their inheritances may have shrunk as their parents may be living longer and in need of expensive care. But they're buying new cars like never before. Those age 50 and older are buying more than three of every five new vehicles sold, or about 62 percent, according to a new study from J.D. Power and AARP. That's up from 39 percent in 2001 when Power began tracking the data. For the Detroit Three, boomers now account for 67 percent of all sales. "The amazing thing is the retirees. They're coming in waves," said Dan Frost, owner of Cadillac of Novi and Chrysler-Jeep-Dodge-Ram dealerships in Southfield and Taylor, Mich. "They used to be cash buyers. Now we're getting them into leases so they come back in a few years."

The flip side is those between 18 and 34 make up just 13 percent of the market, down from 24 percent in 2001."Boomers can afford to buy new vehicles. Millennials cannot. The numbers don't lie," said Mark Bradbury, director of integrated marketing at AARP Media. Demographers define baby boomers as those born between 1946 and 1964, and generally as the crush of children born post-World War II. Millennials are the generation born anytime after the late 1970s.

The research raises the question of whether automakers' vigorous efforts to reach younger buyers through social media or targeted reality shows, such as Ford's "Escape Routes," are generating much return. There are older consumers spending significant time on social media and watching shows aimed at their children. But until the incomes of more millennials stabilize and grow, the question will persist. "You can't build any loyalty among people who are not paying attention," said AARP's Bradbury. To be sure, Americans older than 50 already make up a larger percentage of the population, about 42 percent, up from 37 percent in 2000, census data show. But from 2000-10, the over-50 crowd's new vehicle purchasing increased at a much faster clip than the percentage population increase in that age group, making their purchasing power disproportionately stronger.

Conversely, 18- to 34-year-olds are much less likely to buy a new car, though their portion of the population has remained steady -- 23.2 percent in 2010 vs. 23.8 percent in 2000. Charles Ballard, Michigan State University economist, said "a substantial portion of it has to be a result of income shifts. ... The Great Recession has visited a lot of pain upon those who are early in their careers." AARP's Bradbury said the median income of those 50 and older is $67,537 compared with $55,856 for the 18-to-34 demographic. Boomers on average have investments that are worth $107,833, roughly four times the $23,490 value of a millennial's portfolio. "The average price of a new vehicle is slightly over $30,000. We tend to forget that," said Tom Libby, senior automotive analyst with R.L. Polk in Southfield. "For a 22-year-old, that's a lot of money."

Jump in gasoline prices spurs sales of electric, hybrid vehicles

'Green' cars reach highest share of U.S. market ever

Americans are buying record numbers of hybrid and electric cars as gas prices climb and new models arrive in showrooms, giving the vehicles their greatest share yet of the U.S. auto market. Consumers bought a record 52,000 gas-electric hybrids and all-electric cars in March, up from 34,000 during the same month last year. The two categories combined made up 3.64 percent of total U.S. sales, their highest monthly market share ever, according to Ward's AutoInfoBank. The previous high was 3.56 percent in July 2009, when the Cash for Clunkers program encouraged people to trade in old gas guzzlers for more fuel-efficient cars. And while their share of the market remains small, it's a big leap from the start of the year, when hybrids and electrics made up 2.38 percent of new car sales. Buyers were drawn by new models like the Toyota Prius C subcompact, the Prius V wagon and Camry hybrid. Gas prices near or above $4 per gallon added to the cars' attraction.

Stronger sales of the Volt and the Nissan Leaf were a positive sign for electric car makers. The two vehicles have struggled to gain acceptance from buyers worried about how far they can drive on a battery charge. Another concern: Volt maker General Motors Co. had to change the car's charging system because its batteries caught fire after government crash tests. GM sold just 7,671 Volts last year, below its goal of 10,000. But in March, it set a new monthly record of 2,289 for the Volt, an electric car with a small backup gas engine. Sales of the all-electric Leaf nearly doubled to 579.

Toyota sales in U.S. come roaring back from 2011

Gap with Chevrolet, Ford narrower than year ago after quake

Toyota is back. It's putting a year of earthquake-related shortages behind it and grabbing sales from stumbling General Motors and Ford. Toyota's sales rose 12 percent in April, and its share of the market returned to levels it hasn't seen since before the March 2011 earthquake in Japan. Its sales outpaced the industry as a whole, which saw growth of 2.3 percent to 1.18 million cars and trucks according to Autodata. Toyota's resurgence could mean better deals as its rivals fight for customers by offering discounts and promotions. Already, Toyota had zero-percent financing and other deals in May. It also means better selection for buyers. Toyota's factories are cranking out popular models that were missing from showrooms last year when the earthquake disrupted production. Toyota snatched buyers from General Motors, Ford, Honda and Nissan, according to trade-in data from auto research site Edmunds.com. All of those companies saw sales fall in April. Among those who saw sales gains was Chrysler, which posted a 20 percent jump.

April started slowly, but sales picked up toward the end of the month. Sales ran at an annual rate of 14.4 million, making it the fourth consecutive month in which the annualized pace has been 14 million or more. Jeff Schuster, senior vice president of forecasting for the LMC Automotive consulting firm, said pent-up demand for new cars is driving sales, as the average age of vehicles on U.S. roads approaches a record 11 years. That demand continues even after a strong February and March. "We're in a more pronounced recovery here," he said. GM now expects U.S. industry-wide sales of 14 million to 14.5 million this year. That's still lower than the peak of 17 million in 2005, but better than the 2009 downturn, when 10.6 million new vehicles were sold.

High gas prices continued to fuel small car sales. But pump prices appear to have peaked and have fallen 12 cents a gallon in the past month to $3.81 nationwide. The average price in California is $4.16 – 15 cents lower than a month ago. That helped boost truck sales last month, which will mean higher profits for companies. Full-size pickups rose to 10 percent of the market from 8 percent last year, Ford U.S. sales analyst Erich Merkle said. While Ford and GM benefited from Toyota's struggles last year, they're seeing that advantage fade. Ford outsold Toyota by 2,314 vehicles in April. Only one month earlier, it was outselling Toyota by nearly 20,000 vehicles. GM's lead over Toyota also has tightened.

Most of Toyota's growth is coming from buyers who are new to the brand, said Bob Carter, group vice president of the Toyota division in the U.S. Toyota has now fully recovered from its earthquake-related slowdowns. It's entering May with 18,000 more cars and trucks to sell than it had a year ago, Carter said. Its incentive deals also show it has plenty in stock. "There's no doubt the Japanese are back in the market," said Don Johnson, GM's U.S. sales chief. Toyota's share of new car sales hit 15 percent, its highest level since December 2010. While that's below the 17 percent share it commanded in 2009, it's far higher than the 10.5 percent share it had last June.

May Auto Sales

Auto Sales in steady climb back

First five months of year show 10 percent over year ago results

The auto industry's recovery maintained a steady pace in May as Chrysler reported a 30 percent gain in new-vehicle sales, Ford said its sales climbed 13 percent and General Motors reported an 11 percent increase. Total sales during May for all manufacturers were forecast at about 1.4 million vehicles, compared to 1.18 million in April. The closely watched, seasonally adjusted annual sales rate was estimated in the mid-14-million range. Sales in the first five months of this year had risen 10 percent from the same period in 2011. Despite a sluggish economic recovery, consumers are increasingly replacing their older vehicles with new models and seeking out fuel-efficient small cars to cope with volatile gasoline prices.

"Pent-up demand continues to fuel auto sales at a steady and sustainable level in May," said Jesse Toprak, chief market analyst for the auto research website, TrueCar.com. "All major manufacturers will see double digit growth this month." The gains at Chrysler marked the 12th consecutive month of year-over-year increases of 20 percent or more. The company reported strong results for its SUVs and pickup trucks, as well as its revamped line of passenger cars. "In spite of a tremendous amount of global economic uncertainty, the U.S. new vehicle sales industry continues to power ahead," said Reid Bigland, head of domestic sales for Chrysler.

Ford said its gains were fueled in part by a 29 percent rise in sales of F-Series pickup trucks. The strength of the pickup market often correlates to better economic conditions in the construction industry and related businesses. GM said its monthly results were its best in nearly three years. Among the foreign automakers that have reported May results, Volkswagen said its sales increased 28 percent over last year. Industry analysts forecast sales in May to be the highest for the month since 2007. Sales were expected to climb as much as 30 percent over May 2011.

June Auto Sales

June Vehicles Move

Carmakers report swelling auto sales

Industry on track to have best year since 2007.

From mini cars to monster pickups, sales of new cars and trucks surged in June and eased concerns that Americans would be turned off by slower hiring and other scary headlines. Automakers sold nearly 1.3 million cars and trucks in June, up 22 percent from the same month last year. Chrysler posted its best June in five years. Sales soared at Volkswagen, which is on track for its best year in the U.S. since 1973.

The results allayed fears that growth would stall after a strong start to 2012. Earlier this spring, sales were on track to reach 14.5 million this year, boosted by mild weather and the post-earthquake return of Japanese cars to dealers. But the pace dropped to 13.8 million in May, as the stock market plunged and hiring slowed. In June, there was more bad news about jobs growth, and consumer confidence fell for the fourth straight month. But buyers didn't go away. June's sales pace rose to 14.1 million, according to Autodata Corp. And if sales stay at that rate for all of 2012, it will be the industry's best year since 2007.

Falling gas prices, cheaper loans and new models like the Ford Escape and Dodge Dart drew buyers. A revived housing market lifted sales of pickups. And there was still plenty of demand from people who bought cars in the middle of the last decade and needed to replace them. Annual sales hit a high of 17 million in 2005, and those cars and trucks are now seven years old. "If a family in Iowa's only mode of transportation is on the fritz, they are going to buy a replacement vehicle, even if Spain's economy is on the brink of collapse," says Alec Gutierrez, a senior market analyst at Kelley Blue Book.

Automakers also started their Independence Day promotions a little early and that juiced sales at the end of the month. "In the last two weeks we really went all-out," says Bill Underriner, who sells Volvo, Buick, Honda and Hyundai cars in Billings, Mont. The Buick Verano small car -- one of Underriner's big sellers last month -- is now $239 per month for a two-year lease. That's $50 less than usual. Low interest rates are making deals like the Verano's more attractive. The average interest rate on a 60-month new-car loan is 4.5 percent, down from 6.98 percent two years ago, according to Bankrate.com. Credit availability is also improving. "The affordability of cars is probably at an all-time high," Chrysler Group sales chief Reid Bigland said last week.

Falling gas prices meant buyers were more likely to consider bigger cars and SUVs in June, not just the small cars that sold well at the beginning of the year. Jeep Liberty SUV sales rose 50 percent and the Ford Explorer jumped 35 percent. Gas averaged $3.43 per gallon at the end of June, down 41 cents from the end of March. Pickup truck sales also improved as home building perked up. Chrysler's Ram pickup sales rose 12 percent and sales of the Ford F-Series -- which has long been the country's best-selling vehicle -- rose 11 percent. At Chrysler, sales of the tiny Fiat 500 and Chrysler 300 large sedan more than doubled from a year earlier, helping the company to a 20-percent gain for the month.

General Motors' sales rose 16 percent, with strong demand for the Chevy Malibu midsize sedan and Volt electric car. Ford's overall sales rose 7 percent. The Escape small SUV posted its best month ever after a new version of the popular vehicle went on sale. Toyota's sales rose 60 percent for the month while Honda's climbed 49 percent, but that wasn't surprising. Last year, both companies had little inventory at U.S. dealerships because of the earthquake in Japan. Now, they're taking back sales that their rivals gained last year. The Chevrolet Cruze, for example, was the top-selling car in the country June 2011, but its sales dropped 24 percent last month. Sales of its Japanese rivals, the Honda Civic and Toyota Corolla, jumped more than 40 percent each.

Sales would have been slower if carmakers hadn't sold so many vehicles to government, commercial and daily rental fleets, says Jesse Toprak, vice president of market intelligence for the car buying site TrueCar.com. A little more than a third of all the cars GM sold went to fleets, up substantially from last year. Ford also sold a third of its vehicles to fleets, but that was about the same percentage as last year. GM said that was just the way some sales were timed, and its fleet sales should fall this month. Toprak thinks that even if sales soften a little, they're still on track to reach 14.4 million by the end of the year. That's better than last year's 12.8 million, and it's far better than the 30-year low of 10.4 million during the recession in 2009. "This is a healthy and sustainable rate of recovery," he said.

Retail

Retail sales up 3.9 percent in month of May

Job gains, falling fuel prices prompt consumers to spend

Despite slower job gains and signs of flagging consumer confidence, consumers hit the malls in May to refresh their wardrobes as the summer shopping season begins. Major chain stores posted a 3.9 percent sales increase in May compared with the same month a year earlier, beating analysts' expectations of a 3.6% rise, according to Thomson Reuters' tally of 18 retailers. Top performers were a mixture of high- and low-end stores. Action-sports chain Zumiez Inc. led the way with a 13.7 percent bump. Luxury retailer Nordstrom Inc. saw sales rise

5.3 percent. Benefiting from a continuing thrifty mindset, off-price retailers Ross Stores Inc. and TJX Cos. saw an 8 percent rise. Limited Brands, parent company of Victoria's Secret and Bath & Body Works, said sales rose 6 percent.

The healthy May jump in sales comes on the heels of a poor April when more than half of retailers posted lower-than-expected results. Some retailers did not fare as well. Struggling teen clothier Wet Seal said sales fell 8.8%, while department store chain Kohl's Corp. reported a 4.2% drop. All told, about 69% of retailers beat expectations, Thomson Reuters said. Analysts said recent signs of smaller job gains were balanced out with Mother's Day promotions and falling gas prices, which prompted some people to reopen their wallets for summer apparel. Results are based on sales at stores open at least a year, known as same-store sales and considered an important measure of a retailer's health because it excludes the effect of stores' openings and closings.

Consumer confidence hits 4-year high

A better hiring outlook and lower gas prices pushed a measure of U.S. consumer confidence to its highest level in four and a half years. The Thomson Reuters-University of Michigan index of consumer sentiment jumped to 79.3 in May, up from 76.4 in the previous month. That's the best reading since October 2007 — two months before the recession began.

A high proportion of consumers say they are hearing about job gains rather than losses. The number of those who say they heard of job losses dropped to its lowest point since mid-2007. Gas prices have also fallen steadily in recent weeks, freeing up more money for other purchases.

Housing

Jump in April home prices raises economists' outlook

National home prices marked their second year-over-year increase in April, according to a widely watched index, signaling that housing strengthened during the critical spring shopping season. The home price index by research firm CoreLogic increased 1.1% over April 2011, notching the second consecutive year-over-year increase since June 2010. The index includes sales of foreclosed and other so-called distressed properties. Excluding sales of those distressed homes, prices were up 1.9% from the same period a year earlier, a rate of improvement not seen since late 2006, and better than the brief period of housing strength in 2010 that was driven by popular buyer tax credits. CoreLogic forecast that prices will continue to rise in coming months due to a lack of homes available for sale. "Home prices are responding to a restricted supply that will likely exist for some time to come — an optimistic sign for the future of our industry," said Anand Nallathambi, president and chief executive of CoreLogic.

The most widely watched measure of home prices, the Case-Shiller index, has painted a different portrait of the national housing picture. Released recently, the index showed prices in the U.S. ended the first quarter at their lowest point since the housing crisis, with values in 20 major cities dropping 2.6% in March, compared with the same period a year earlier. But many analysts have turned optimistic on housing despite those disappointing numbers, noting that given the lag in the Case-Shiller data, a turnaround in housing values will probably not be captured until well after its occurrence. While the Case-Shiller numbers are the industry standard, the CoreLogic numbers are followed by the Federal Reserve as well as many analysts.

Any significant housing rebound is unlikely to get underway until the shaky jobs market shows sustained improvement. A report recently showing that the nation's unemployment rate in May rose for the first time in nearly a year, to 8.2%, and created on net just 69,000 jobs last month, convinced several economists that the U.S. is entering another summer slump. But given the improvement in the CoreLogic data, as well as a steady increase in sales, the housing market looks poised to avoid the results of last year's silent spring, in which the traditionally busy season posted a largely lackluster performance.

S. California's median home prices climb

The Southland's move-up market showed some signs of life as the region's median home price improved for the second consecutive month in May, new data show. The median home price rose 5.4 percent in May from the same month last year to hit $295,000, real estate research firm DataQuick reported recently. That was a 1.7 percent improvement over the prior month. Sales throughout the Southland also improved, up 20.6 percent from May 2011 and 15.1 percent from April to hit 22,192. Helping boost the median was a narrower share of foreclosures selling as part of the market for previously owned homes. Foreclosed homes typically sell at a discount. Sales volume also improved for homes priced above $300,000, helping boost prices.

Jobless rates rise in 18 states in May

Unemployment rates rose in 18 U.S. states in May, the most in nine months. Increasing unemployment in more than a third of U.S. states is the latest evidence of a weaker job market.

The Labor Department said that unemployment rates fell in only 14 states. That's fewer than the previous month, when rates fell in 37 states. Rates were unchanged in 18 states. Nationally, the rate rose to 8.2 percent in May from 8.1 percent in April, the first increase in almost a year. Employers added only 69,000 jobs, the fewest in 12 months. Still, 27 states added jobs in May. California gained the most, adding 33,900. Ohio was next with 19,600.

North Carolina reported the biggest loss, shedding 16,500 jobs. It was followed by Pennsylvania, which lost nearly 10,000. Nevada had the nation's highest unemployment rate, at 11.6 percent, followed by Rhode Island's 11 percent and California's 10.8 percent.

North Dakota, meanwhile, reported the nation's lowest rate of 3 percent. Nebraska had the next lowest, at 3.9 percent. Despite the slowdown in hiring in recent months, some of the hardest-hit states have seen substantial improvement in the past year. Michigan and Nevada have both seen their unemployment rates fall 2.1 percentage points in the past 12 months. Both states still have higher unemployment rates than the national average. But Michigan's rate was 8.5 percent last month, down from 10.6 percent in May 2011. Florida and Mississippi have seen their rates fall 2 percentage points in the past 12 months. Florida's rate was 8.6 percent, down from 10.6 percent in the same month last year. Mississippi's is 8.7 percent, down from 10.7 percent in May 2011.

Survey: CEOs expect strong job growth in Silicon Valley

Nearly half of area's top executives intend to make more hires in 2012

Silicon Valley employers expect to maintain a robust pace of hiring this year, although problems will continue to challenge the region's rebounding economy, according to a recent report.

SILICON VALLEY CEO SURVEY

The Silicon Valley Leadership Groups survey of 188 CEOs found:

- 46 percent expect improved job growth for their company this year, while 13 percent expect a decline.
- 56 percent see improved job growth for their industry sector this year, while 14 percent expect a decline.
- The CEO's indentified housing costs, high taxes, health care and traffic congestion as big challenges for their employees.

An estimated 46 percent of chief executives say their companies intend to hire during 2012, while only 13 percent plan to reduce staffing levels. An additional 36 percent plan no staffing changes, the study by the Silicon Valley Leadership Group stated. A total of 188 CEOs participated in the survey. Optimism about hiring plans appears to have waned a bit. Last year's survey found that 55 percent were expecting job growth for their company during 2011, while 5 percent anticipated cutbacks.

Nevertheless, those who are unemployed may be able to take heart from the strong prospects overall for job growth in the area. "Our survey portends very well not only for Silicon Valley's economic strength, but also for job growth for those who are eager to work but have been unable to find work in the region," said Carl Guardino, president of the Silicon Valley Leadership Group. The leadership group found that 63 percent of the companies that participated added employees in 2011, while 13 percent reduced employment. That's similar to the hiring results for 2010, when 66 percent of the companies surveyed added jobs, while 11 percent cut jobs. An additional 21 percent undertook no staffing changes, the study found. "This looks like a solid and sustainable expansion," said Jon Haveman, chief economist with the Bay Area Council's Economic Institute.

Despite the positive tenor of the report, the surge in Silicon Valley hiring has yet to extend to every nook of the region's economy. "These are good results if you are in the innovation sector or technology industry, but the trickle-down hasn't fully happened yet," said Steve Wright, a spokesman for the Silicon Valley Leadership Group. "It's a robust number, but it's not a panacea."

The leadership group's study identified four challenges confronting employees and their families in Silicon Valley: housing costs, high taxes, health care and traffic congestion. Silicon Valley also must cope with a widening host of rivals who hunger to capture the jobs being created in this area. "Economies are fickle under the best of conditions," according to the study. "More than ever, challenges to Silicon Valley's resurgent prowess persist from other regions in the nation and from countless sources abroad." Survey respondents said they hope local, state and federal officials will soon take steps to improve the business and regulatory climate, according to the study. "We need to recognize that we can't nibble away at these challenges," Guardino said. "It's time to take big bites to deal with these problems."

Economy stuck in neutral

Consumer spending up but growth slows ahead of jobs report

The U.S. economy is looking slightly weaker after a critical report on May job growth. Economic growth was a little slower in the first three months of the year than first estimated, largely because governments and consumers spent less and businesses restocked their supplies more slowly. The number of people who applied for unemployment benefits rose to a five-week high recently. And a survey of private companies showed only modest hiring gains last month. Still, a softer job market hasn't caused Americans to scale back spending. Consumers spent more at retail stores in May than the same month last year, buying more clothes and Mother's Day gifts.

Recent data showed that:

- Weekly applications for unemployment aid rose 10,000 to a seasonally adjusted 383,000, the Labor Department said.
- Private businesses added 133,000 jobs last month, according to a survey by payroll provider ADP. That figure disappointed most economists, who had hoped to see job growth accelerate after ADP's survey found that just 113,000 jobs were added in April.

Peter Newland, an economist at Barclays Research, said he was discouraged by the slowdown in first-quarter growth. "This report does little to change the perception of an economy ticking along at a moderate pace but failing to break out into a full-on recovery with consistently above-potential growth," Newland said.

The government makes three estimates of quarterly economic growth, or gross domestic product. GDP measures the output of all goods and services in the United States, from haircuts and coffee to airplanes and appliances. A big reason growth slowed in the January-March quarter was that government spending at all levels fell at a 3.9 percent annual rate. That's the biggest decline in a year and nearly a full percentage point more than estimated last month. Government spending has declined for six straight quarters. And national defense spending has tumbled in the past two quarters. It fell at an 8.3 percent annual rate in the first quarter of 2012 and at a 12.1 percent annual rate in the final three months of 2011. The declines largely reflect the winding down of the Iraq war.

Federal government spending fell at a 5.9 percent annual rate in the first quarter. Spending by state and local governments fell at a 2.5 percent annual rate in the first quarter, double the initial estimate. Many economists had thought the worst was over at the state and local level. "This throws some cold water on the view that state and local governments have already bitten the bullet and are now likely to add to, rather than subtract from, growth in 2012," said Diane Swonk, chief economist at Mesirow Financial.

Government spending at all levels fell last year. That subtracted nearly a half of a percentage point from 2011 growth, which was 1.7 percent. Joel Naroff, chief economist at Naroff Economic Advisors, said the economy would be growing at least a full percentage point faster if governments were spending at the rate they normally do three years into a recovery. "Fiscal austerity comes at a price whether you are talking about the United States or Europe," Naroff said. "In the United States, we are taking moderate growth and turning it into sluggish growth."

Analysts think the economy is growing at a slightly faster rate this spring. Hiring has been steady and gas prices are lower, allowing consumers to spend more freely. Consumer spending drives 70 percent of economic activity. Economists foresee growth at an annual rate of between 2 percent and 2.5 percent in the April-June quarter. Many expect the economy will maintain that pace for all of 2012. Still, growth of 2.5 percent typically generates only enough jobs to keep pace with population changes. Most economists say it takes almost twice as much growth to boost hiring enough to lower the unemployment rate by 1 percentage point over a year. The unemployment rate has fallen a full percentage point since August — from 9.1 percent to 8.1 percent last month.

UCLA Anderson School Forecast

Sluggish Economy Continues Despite Improvements in the Housing Market

Pool workforce development seen as major contributor to slow growth

In its second quarterly report of 2012, the UCLA Anderson Forecast’s outlook for the U.S. says that Gross Domestic Product (GDP) and job formation will remain weak in the near-term, mirroring conditions that have prevailed for the last two years. GDP growth is forecasted to be 2.4% by the end of 2013, increasing to 3.4% in 2014. The unemployment rate by the end of

2013 should be 7.7%. The forecast assumes the Federal Reserve Bank cannot risk a rate increase, particularly if the nation experiences the forecasted inflation rate of 1.6%.

In California, slow and steady gains are anticipated throughout 2012. More accelerated growth in 2013 and 2014 could see California's unemployment rate decrease to 7.7% by the end of 2014, which is within 0.6% of the U.S. rate.

The National Forecast

In his June Forecast report, UCLA Anderson Forecast Director Ed Leamer speculates on the economic factors that will become the engine(s) of growth for the U.S. economy. In an essay titled, "Wall Street, K-Street or Main Street? Who Can Save US?," Leamer suggests that the "distraction" caused by focusing on the financial sector (Wall Street) and the federal government (K-Street) is causing most to miss the "real Main Street problem," that is, inadequate workforce development for 21st century labor markets. Re-emphasizing themes he's discussed in previous forecasts, Leamer writes, "The solution is workforce development. We need to take a deep breath and accept the fact that two bubbles have disguised the inferior quality of our educational system. Good jobs in the United States in the 21st century will require humans to do things that are not suited to the capabilities of far-away foreigners, robots or microprocessors. We need a workforce that can think creatively and solve the new problems, not merely recall the solutions to old problems."

Leamer's essay notes that there has been no real recovery from the "Great Recession" of 2008/9. In each of the previous ten recessions, GDP returned to its previous peak within two years. This time it has taken almost four years. A recovery with exceptional GDP growth requires greater than normal employment growth. Payrolls have typically recovered to their previous peaks within two to two and a half years. Given current lags, Leamer says this recession could take seven or eight.

In a companion piece, UCLA Anderson Senior Economist David Shulman casts an eye on the nation's housing market. In his essay titled, "Rebuilding the Housing Economy," Shulman writes that average home prices have declined by one-third, a searing experience for most homeowners who never believed housing prices would ever fall. Amid continuing foreclosure activity "and potential homeowners either unable to meet more stringent purchase requirements or fearful of continued price declines, the homeownership rate declined from a peak of 69% in 2004 to 66% in 2011 and is forecast to drop to 65% by the end of this year." However, Shulman's analysis suggests that the housing market may have bottomed out and that a recovery is underway. Foreclosures appear to have peaked. Existing home sales are on the rise. Shulman says that this recovery is bolstered by a gradually improving labor market, a rebound in household formations and record low mortgage rates. But he warns that the recovery will be "gradual and uneven." The improving job market is far from healthy. While higher down payment and credit score requirements are nullifying some of the stimulative effects of the low interest rates, the specter of exploding student loan debt will keep potential buyers out of the housing market for years to come.

Housing starts are expected to increase from a very depressed 610,000 units in 2011 to 755,000 units this year and 1.01 million units and 1.37 million units in 2013 and 2014, respectively. Although the increase is substantial, the recovery represents a return to a more normal level of activity. Shulman notes that the "real drama" is coming in multi-family housing, citing the current boom in multi-family construction, which is underpinned by a low vacancy rate (5%), rising rents and a flood of institutional money coming into the sector.

The California Forecast

In the California report, Senior Economist Jerry Nickelsburg looks closely at California's housing market, specifically residential construction, which "first led the decline in employment and economic activity going into the recession and has been at the rear dragging down potential growth during the recovery." In an essay titled, "California Housing Markets: Data, Mirages, and Recovery," Nickelsburg writes that California's unemployment rate rose faster than the nation's due to 350,000 lost construction jobs.

Is California's housing market ready to turn? Nickelsburg's analysis suggests that California real estate markets are "either still in the trough or still declining toward it. While there is some data giving rise to optimism, there is no real indication that the housing market is on the cusp of a recovery." However, there is data that leads Nickelsburg to expect the California housing market to grow more rapidly than the nation's in 2013 and 2014. "We expect a modest growth in housing starts for the balance of the year at approximately one quarter of the U.S. rate," writes Nickelsburg. "This will be predominantly multi-family housing. In 2013, we forecast a 40% jump in permits, slightly above the U.S. rate and a dramatic rise to 130,000 permits in 2014, double the U.S. rate."

The current forecast is for continued slow steady gains in employment through 2012, with growth expected to rise 1.9%, 1.8% and 2.5% in 2012, 2013 and 2014, respectively. Payrolls will grow more slowly at 1.6%, 1.8% and 2.4% for the three forecast years. The unemployment rate will linger around 10.6% through 2012 and average 9.7% in 2013, about the same as was forecasted in the March report. The unemployment rate is expected to drop to 8.3% in 2014.

Sources:

Valley Times
San Jose Mercury News
San Francisco Chronicle

Wall Street Journal
Economy.com