



California Forecast: Sales Tax Trends and Economic Drivers

September 2011

HdL provides relevant information and analyses on the economic forces affecting California's local government agencies. In addition, HdL's allocation audits and software help clients to maximize revenues.

HdL serves over 335 cities, counties and special districts in California and across the nation.





	2011/12	2012/13
Autos/Transportation	9.2%	6.0%
Vehicle shortages, a lack of manufacturer incentives, economic uncertainty and renewed consumer caution are slowing the pace of sales. However, pent-up demand remains and financing is becoming easier. Analysts expect buyers to return to dealer showrooms in the second half of the year.		
Building/Construction	2.9%	2.5%
Private sector construction activity continues to be depressed. The loss of redevelopment financing and local and state budget cuts will further hamper spending. Stimulus-funded construction activity helped prop up first half results. Housing activity has stabilized but at historically low levels. High unemployment, strict mortgage underwriting and property foreclosures will keep single family homebuilding sluggish through 2013/14. Maintenance of existing homes and repair of foreclosures keeping home improvement chains stable.		
Business/Industry	4.6%	3.5%
Manufacturing has been one of the strongest sectors of the economy in the two years since the recession officially ended. Economic activity in the manufacturing sector expanded in August for the 25th consecutive month with business purchases of technology and computer software being particularly bright spots. However, political paralysis here and economic uncertainties in Europe have recently slowed the rate of growth and new investment.		
Food/Drugs	2.3%	2.0%
Traditional supermarket chains are facing fierce competition from independent operators while at the same time being squeezed by specialty markets on the high end and discounters on the low end. Chains are fighting back with more prepared meals and broader selections of other merchandise.		
Fuel/Service Stations	19.6%	3.0%
Long-term forecasts from oil industry analysts expect that investor activity, world events, increased export of U.S. refinery output to other countries, and growing fuel demand in Asia and South America will keep prices high for U.S. consumers even if domestic gasoline demand declines.		
General Consumer Goods	4.2%	3.5%
Retailers serving the luxury market have fared well since the end of the recession although stock market setbacks may slow this trend. Saturation, new competition and new uncertainties for middle and lower income families have resulted in only modest growth for many discounters. Consumer shifts to online spending are also impacting electronic stores and related brick-and-mortar retailers who are reducing inventories and floor space to better deal with heated price competition from online rivals.		
Restaurants/Hotels	4.2%	4.0%
Hotel occupancy is creeping back following a two-year drought of leisure and business travelers. Despite high fuel prices consumers are expected to boost spending on travel and leisure. Restaurants operators are reporting modest gains with same-store sales and increased customer traffic. New outlets are contributing to gains in the quick and full service restaurant segments.		
State and County Pools	6.9%	6.0%
Private vehicle transactions are up as have been equipment leases and out of state purchases of business equipment and supplies. Tax from out of state purchases under \$500,000 is allocated via use tax allocation pools rather than to place of use.		
TOTAL	6.8%	3.9%

The **Proposition 172** growth factor is **6.5%** for Fiscal Year 2011/12. This factor varies from HdL's Bradley Burns growth rates due to differing collection periods and comparisons to prior year data that include onetime payment aberrations.



	2011/12	2012/13
U.S. Real GDP Growth	2.7%	3.4%

U.S. real gross domestic product has slowed during the first half of 2011, though we remain optimistic about the second half of 2011 and 2012. Much of the recent slowdown in the economy was driven by transitory events like the tsunamis in Japan and the tornados in the Midwest that disrupted the automobile supply chain and a spike in oil prices. These effects are already reversing trend with a surge in autos and declining prices at the pump, which should help to bolster real consumer spending.

U.S. CPI Inflation	2.0%	2.6%
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Although inflation has been kept relatively in bay, a lot of fiscal and monetary stimulus was injected into the U.S. economy during and after the Great Recession. The Federal Reserve has kept interest rates low in an effort to help stimulate spending, but eventually this extra liquidity will give rise to upward pressure on prices. We expect inflation to remain relatively stable over the short run, but by 2013 prices are expected to begin growing at a 3% rate.

California Population	38,086,835	38,561,128
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Recently released data from the 2010 Census shows that California grew at a slower pace between 2000 and 2010 than previously reported. The California Department of Finance revised its original growth rate of 13.9% down to 9.9%—a reduction of over 1.3 million residents. But, we forecast that California's population will continue to grow. California's housing market is more affordable than it has been for several years and the high unemployment in neighboring states should alleviate the incentive to migrate out of state.

California Nonfarm Employment	14,188,420	14,508,923
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California's labor markets stumbled slightly in August, but Beacon Economics remains confident that the labor market recovery is underway. Weekly hours in manufacturing remained above 41 per week in the most recent data and workers averaged more than 4 hours of overtime per week. Combined with falling initial claims for unemployment, the leading indicators show that there is still underlying demand for workers in the state. We forecast employment to grow by 1.6% in 2011-12 and by 2.3% next fiscal year.

California Unemployment Rate	11.3%	10.3%
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California's unemployment rate remains stubbornly high at 12.1%. Most of this has been driven by declining labor force statistics, which show that Californians are still relatively pessimistic about their chances of getting work. However, several sectors like professional/business services and education/healthcare have consistently added jobs. The bigger problem from California's labor markets is the skills mismatch. Many of the construction and retail workers who lost their jobs during the downturn are not equipped to take advantage of the growing high-skilled, high-technology jobs in the state. The labor markets will continue to recover, but the skills mismatch will make that process slower than it would otherwise be.

California Median Home Price	\$254,048	\$258,873
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Despite the hype in the news, Beacon Economics is not calling for a double-dip in home prices. In fact, the state's housing market is healthier than it has been in many years. Home prices have fallen to levels that make sense with incomes in the state and interest rates remain very low. This makes affordability conditions some of the best they have been over the past decade. In addition, defaults and foreclosures have been trending downward across the state, which will alleviate some of the downward pressure on home prices moving forward. As a result, we forecast that home prices will begin growing slowly—averaging less than 1% this year and by less than 2% next fiscal year.

California Nonresidential Permit Values (\$ Millions)	\$ 13,397	\$ 14,951
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Despite lackluster gains in the labor market, California has seen some increased demand for new nonresidential structures. Total nonresidential permit values have risen for two straight quarters, and modest growth is forecasted for the next two years as the economy gains steam.

California Single-Family Building Permits	30,016	39,905
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Residential construction remains tepid at best. Although home prices have stabilized and defaults and foreclosures have come down from peaks, there remains an inventory of distressed properties that must be reabsorbed into the system before new construction can begin again in earnest.



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California's allocation data trails actual sales activity by three to six months. HdL compensates for the lack of current information by reviewing the latest reports, statistics and perspectives from fifty or more economists, analysts and trade associations to reach a consensus on probable trends for coming quarters. The forecast is used to help project revenues based on statewide formulas and for reference in tailoring sales tax estimates appropriate to each client's specific demographics, tax base and regional trends.



"Good information leads to good decisions."



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Beacon Economics, LLC has proven to be one of the most thorough and accurate, economic research/analytical forecasters in the country. Their evaluation of the key drivers impacting local economies and tax revenues provides additional perspective to HdL's quarterly consensus updates. The collaboration and sharing of information between Beacon Economics and HdL helps both companies enhance the accuracy of the work that they perform for their respective clients.