



Wells Fargo Community Advisory Meeting

Regional Economic Outlook

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Introduction

- Recession now here
 - Need to consider what happened
 - North Bay economy slowing down
 - Federal Reserve actions attempting to do many things
 - Fiscal policy to come: will it stop the bleeding?
- Changing financial environment
 - Real estate, banking markets to change
 - Continued opportunities in real estate
 - Internal and external demand for Sonoma County real estate
- Election solves few problem, create a couple more

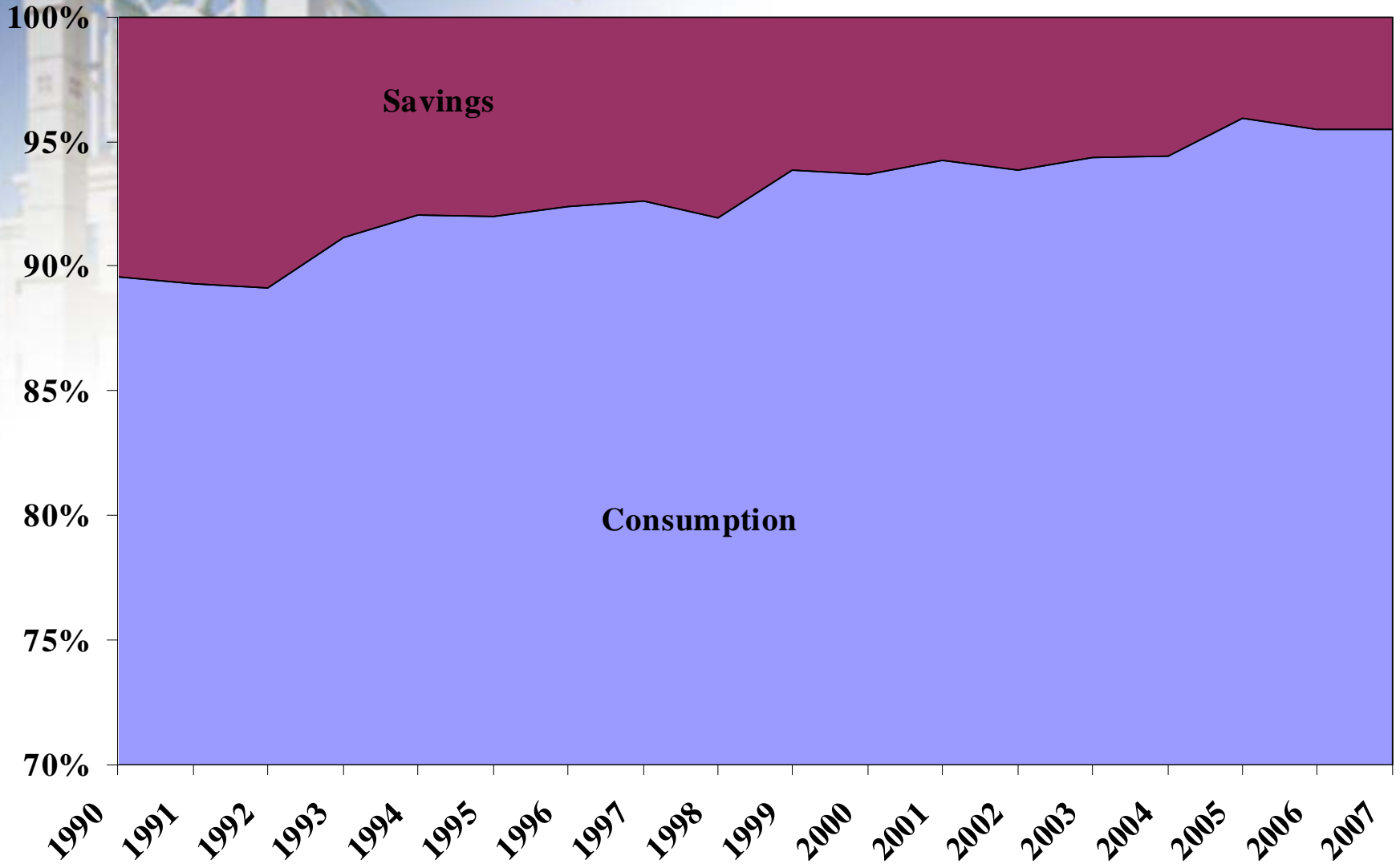
The Current Economic Situation

- Foreseen in direction, not in magnitude
 - Partially greed
 - Partially a lack of financial literacy
 - Partially cultural
 - Partially cyclic
- What is likely coming
 - More market sorting
 - More banking regulation, specific to documentation

All to blame

- Banks use a secondary market to move loans off their balance sheets
- Investors and brokerages purchased these assets
 - Gambled that housing prices would continue to rise on average
 - Homes salable in worse case
 - Investment banks became lending institutions
- Consumption unabated throughout this decade
 - 9/11 had little effect on consumption
 - Housing prices, fueled by both good and bad lending, increase consumer wealth
 - Wealth effect: consumers spent more than their income, used home equity lines
- Banks, consumers and investors all wagered on home prices rising with minor downward cycles

US Disposable Income Since 1990



Source: Bureau of Economic Analysis

The Bailout Plan(s)

- Basically printing money to facilitate growth
 - Nothing more than repackaged monetary expansion
 - Initially, just financial institutions
 - Now: automakers, school loans, State of California, etc.
 - Treasury has become a hedge fund of sorts
- Inflation not an issue if circle remains unbroken
 - Assets slowly sold off as markets stabilize and rise
 - May be profits in the end(!!)
 - Gas prices falling an anomaly
 - Likely back in \$2.50 range by summer 2009
 - Deflation short-lived, if it happens

New Stimulus Possibilities

- Obama gave five sectoral targets
 - Energy
 - Education
 - Health Care
 - Social Welfare/Insurance
 - Infrastructure
- Why not defense here?
 - In many ways defense spending must target similar sub-sectors

Possibilities (cont.)

- Need to consider supply-side versus demand-side
 - Would providing tax breaks or subsidies for firms innovating energy products provide supply-side stimulus?
 - What about defense spending if trained personnel go back into labor force versus war veterans?
- High social value projects the key here
 - Energy seems like best in short-term
 - All of these have relatively high social value

Long-Term Effects

- A decade of fiscal stimulus has made national debt soar
- Current “monetary” package is fueled by a combination of debt and money printing
- Permanent cuts have larger short-term effects than temporary
 - Temporary cuts or spending provide better long-term signal of discipline
- Social security suffers during downturns due to reduced tax revenue and larger draw

National Conclusions

- Policy has now done all it can
 - Federal budget continues to grow
 - May be redirected and cut slightly in 2009-10 version
 - Monetary policy aggressive
 - Lowest cost of funds for banks in decades
 - Why are they not lending yet?
 - Consumer confidence continues to fall
 - This is the driver, and is a fickle statistic
- Need a supply-side boost
 - This may come from a “New Deal” style of budget
 - More likely from environmental sciences and tech

California as Microcosm

- 2002 saw use of fiscal surplus from capital gains taxes spent on **permanent** spending
 - We are now paying for that in current deficit of > \$40 billion
 - Federal spending may stimulate state economies
 - Lag structure here between federal and state budgets
 - Sometimes new packages happen in states
 - Infrastructure and education at state level
- Bet on capital gains from stock market and housing speculation (began in 2002)
- **140,000 households provide 50% of income tax revenue for California**

California's Fates

- Assume California will not go bankrupt
 - Raise taxes (sales or cap gains)
 - Prop 13 will not be repealed (though likely not a bad time to do it)
 - Cap gains tax hike reduces capital gains seeking
 - Should not assume inelasticity for this revenue
 - Cut spending
 - 2002 programs increased automatic spending
 - Now budget an effort to keep programs rather than balance
 - Borrow (or be bailed out)
 - Most likely the first step, cannot be the only step
 - Will investors trust this debt?
 - Likely a mix, but reform is needed
 - A consumer-led expansion may provide an ephemeral, illusory boost to state coffers

North Bay Economic Situation

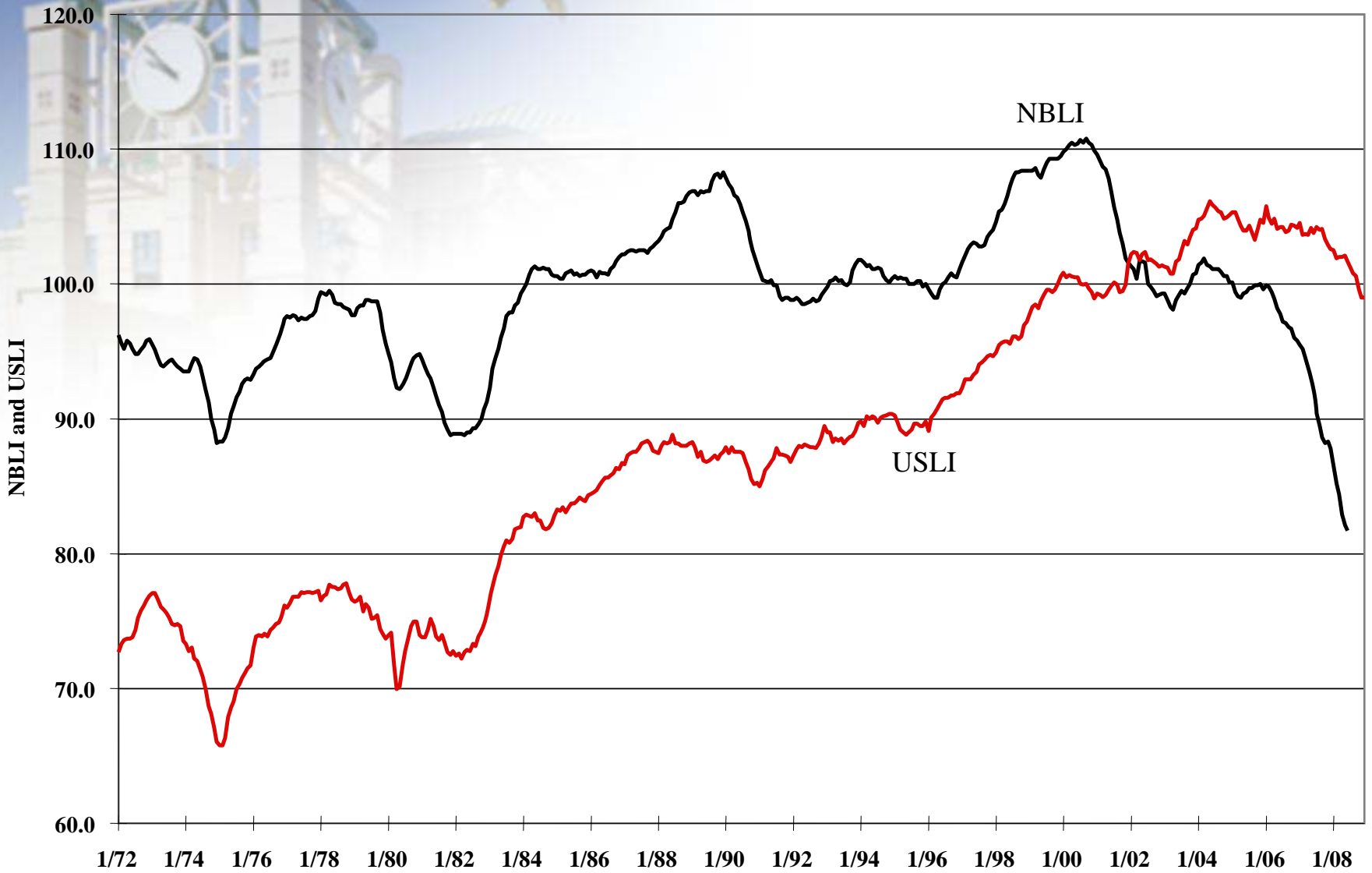
- Short-term
 - Continued stagnation
 - Consumer-led boom from budget and monetary stimulus short-lived, if it takes place
 - Efforts need to focus on two issues
 - Putting funding in hands of innovative businesses
 - Regional, not local or county, economic development
- Opportunities good for long-term growth
 - Environmental Tech
 - Tourism and associated industries
 - Biotech/Health care
 - Wine and agriculture
 - Non-profits

North Bay Indicators

- Leading and Coincident Indicator for Marin, Napa and Sonoma counties
 - The leading tells us where we are
 - The coincident tells us where we are going
 - The combination suggests a cyclic shape
- The indicators show recession has been here for some time

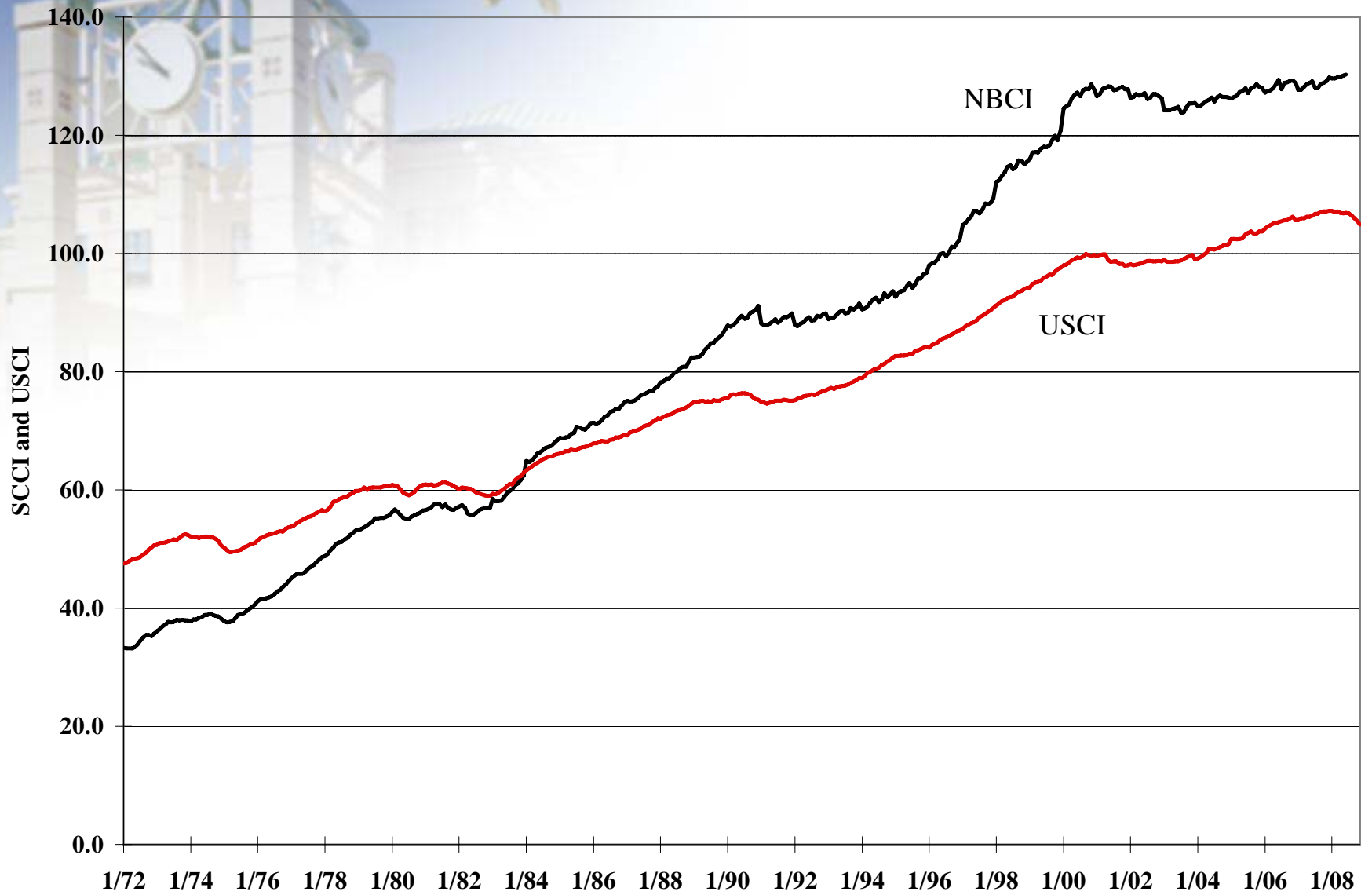
Leading Indicators

- Tyler Leading Indicators tell us where we are headed:
 - Default Notices (**Inverse**)
 - Building Permits (**Positive**)
 - New UI Claims (**Inverse**)
 - US Leading Index (**Positive**)
 - Help-Wanted Ads (**Positive**)
 - Ag Price Index (**Positive**)****
- As indicator increases, economy forecasted to move in **bolded** direction.



Coincident Indicators

- Coincident Indicators tell us where we are:
 - Non-agricultural employment
 - Retail Sales
 - Personal Income
- Once business and consumers receive positive signals, they hire and spend more as a reaction.
- The leading indicator drives the coincident.
 - Leading a mix of business activities, hiring and firing
 - Coincident a mix of worker and resident activities



Local Housing

- The local housing market difficult to gauge concerning transition
 - Was the old pricing correct?
 - Is the current pricing correct?
 - As of Sept. 2008, Napa County down approx. 29.5% from last Sept. in median home price (down to \$349K median).
- Some regional perspective
 - Sonoma County (Sept. 2005, \$580K)
 - Stockton (Sept. 2005, \$385K, now \$155K)
 - SF (Sept. 2006, \$759K, now \$670K)

Economic Development

- Tourism
 - Casino growth still happening?
 - City of Napa expansion has slowed
- Biotech already here and growing again
- Environmental (Green) Tech likely a growth area in the future
 - Can companies like ZAP take advantage of this?
- Non-profits in recession
 - Can be decent or very bad

Tourism and Wine

- Lower \$ value helps stimulate tourism
 - Can long-term market be seized?
- Natural choice of California tourism also
 - Can we rely on just this element?
- Wineries help for long-term flows
 - Have built a tourism arm that works
 - Natural link to restaurants here
 - With global recession, wineries likely to see slower growth
- Links to grow stronger

Biotech and Health Care

- Commercial vacancy rates high
 - Slowly filling back up
- Biotech
 - Growing locally, like small version of late 1990s
- Health Care
 - Demography provides a long-term market

Environmental Tech

- Sonoma County has a large community of high-tech engineers
 - Need partnerships: private and public
 - Waste management tech
 - Solar panels
 - Hydrogen cars
- Can these firms begin and stay here?

Non-Profit Sector

- Recession generally a difficult time for non-profits
 - Some reports have 1,100+ non-profits in Sonoma County alone
 - Competitive environment for donations
 - Recessions demand more services
- As wealth liquidated, tax issue may drive donations
 - End of 2008 may have seen some unexpected activity
 - General contributions slowing way down
- With state budget woes, who will survive?

A background image of a clock tower with a large clock face, set against a clear blue sky. The tower is made of light-colored stone or concrete. The clock face is white with black hands and numbers. The tower is partially obscured by the text and other elements of the slide.

Opportunities

- Continued Export Expansion
- In-source jobs
- Stock markets are currently a historic bargain
- Need to consider “correct” growth
 - Living wage referenda coming: G,B&U
 - Where will workers live?
 - Transportation issues
 - Need to consider social equity issues

Conclusions

- Recession to continue through mid-2009
 - Need supply-side movement or longer problems
- Consumption and savings must walk together over time
 - Not equally, but you must save
- North Bay will come out of this ok
 - We need a supply-side, not demand-side jolt
 - May be a little while
- Economic Development
 - Think regionally



www.sonoma.edu/org/crea/wells091.ppt