ECONOMIC FORECAST

This section provides a summary of the projected outlook of the Orange County economy. The summary is based on the U.S. Macroeconomic and Orange County Overview Forecast and Report prepared by the Institute of Environmental & Economic Studies at California State University, Fullerton (Fullerton). The Fullerton economic report serves as a basis for developing the Orange County General Purpose Revenue Forecast.

Orange County Economy

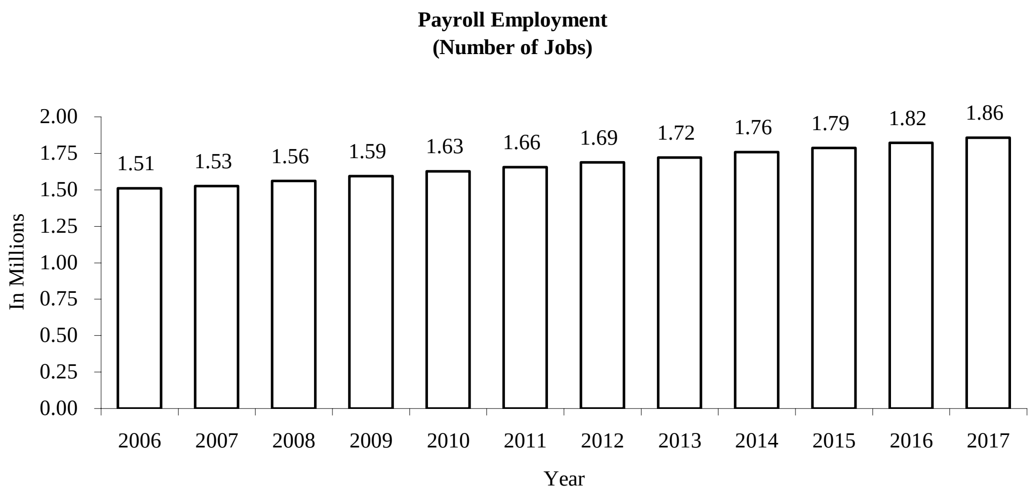
Orange County enjoys a strong economic foundation with its diverse economy, as well as other unique characteristics, making it strong, dynamic and resilient from severe fluctuations. The County, however, is not exempt from trends impacting the national economy and Southern California region. The County will experience a slowdown in 2006 and 2007, similar to the national economy, but will rebound in 2008 with long-term sustainable growth.

The slowdown can be attributed mostly to the housing market, with a combination of slower housing sales and rising mortgage rates. The Federal Reserve Bank's 17 consecutive increases to the federal funds rate beginning in June 2004 resulted in the loss of jobs in the construction, financial services and high-tech sectors. However, the County's climate, infrastructure and workforce will allow it to rebound from this slowdown and serve as the base for long-term growth.

The following section provides an overview of the projected trends in the local economy as reflected by three local economic indicators (payroll employment, residential valuation, and taxable sales). These local economic indicators show the local economy will continue to grow at a modest level over the long-term.

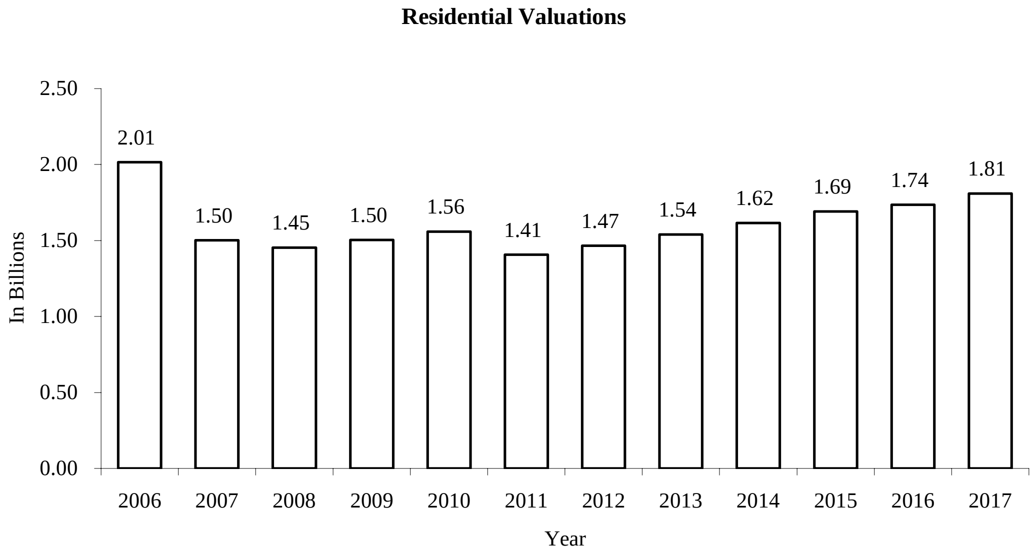
Payroll Employment. The Fullerton forecast calls for a slowdown in the job growth rate over the forecasted period as the County population growth decreases and as a slowdown in the housing market occurs. Job growth will continue to increase at levels between 1.1% to 2.2% per year. Payroll employment (number of jobs) is estimated at 1.53 million in 2007 and increases to 1.86 million by 2017 (Figure 1). Most of the growth will occur in the high-tech, tourism, education, and leisure industries sectors of the economy.

Figure 1



Residential Valuations. Residential valuations are expected to decline the next few years before showing positive gains. The maximum annual decline in valuation is expected to be 25% in 2007 as a mortgage rates increase and economic growth slows (Figure 2). Residential valuation will fluctuate until 2011, when it is expected to steadily increase annually through the end of the forecast period. It should be noted that future construction of single family homes will be limited as the amount of available land diminishes and the County transitions toward high density, high-rise buildings. Five cities in the County have current or future projects underway to build high-rise dwellings.

Figure 2



Taxable Sales. Even with the slowdown in the economy, taxable sales are anticipated to grow an average of 6.8% annually over the forecast period as incomes rise and the population grows. Taxable sales will increase from $63.6 billion in 2007 to $87.7 billion in 2012, representing an annual average sales growth rate of 6.6% (Figure 3).

Figure 3