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) and updated per their Annual Forecast released October 2007. The Fullerton economic reports serve as a basis for developing the Orange County General Purpose Revenue Forecast.

Orange County Economy

While the Orange County economy is well diversified, it is still impacted by national economic trends. The slowing growth forecasted in the 2006 Strategic Financial Plan was realized in the last two quarters of 2006 and has continued into 2007. The County will experience a continued slowdown in 2007 which is expected to extend into 2008, similar to the national economy. An economic recovery is projected for 2009 and beyond when real gross domestic product is anticipated to grow again at its long term secular trend rate of approximately three percent per year over the forecast period.

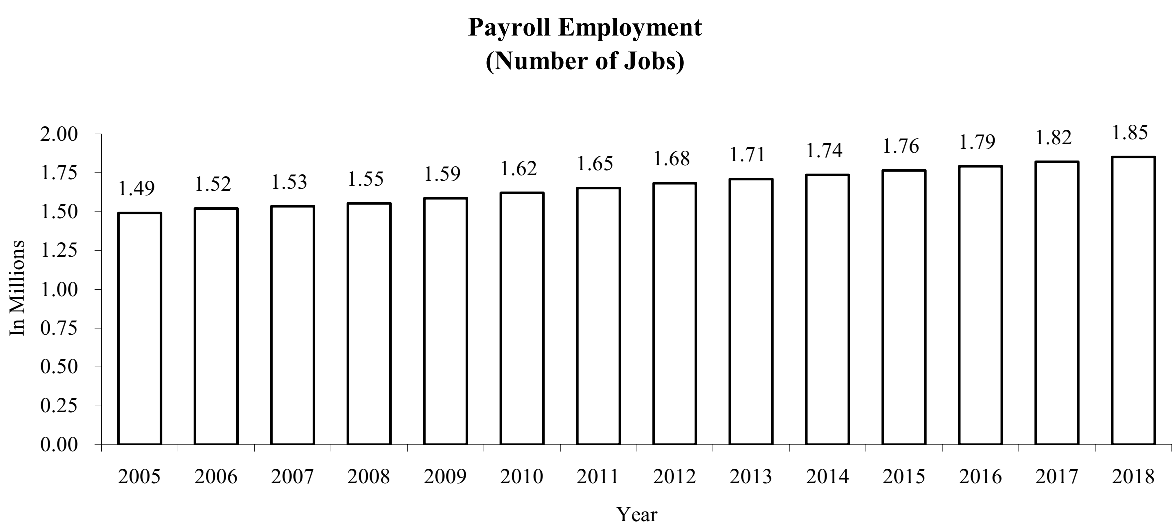
The slowdown continues to be attributed mostly to the housing market, due to sub prime lending issues. Attempts to contain fallout of the sub prime market have not yet worked resulting in credit issues, housing market concerns and some intermittent financial market impacts. Although it is anticipated that there will be continued fallout from the sub prime issue, measures continue to be taken to mitigate those effects. Uniform enforcement rules and standards are being developed to guide lending practices. The Federal Reserve lowered its target rate by 50 basis points in September which should provide liquidity and help to restore consumer and investor confidence. Nationwide, the sub prime issue should remain relatively well contained as it comprises a little over 10 percent of all mortgages outstanding.

Historically, the County has grown at a higher rate than the national economy and has experienced lower unemployment rates. Due to the diversity of its economy, it has also experienced less adverse trends than other local regions during periods of slow growth. However, the mortgage industry and construction industry has a large presence in Orange County and the full impact of declining home values and sales can not yet be quantified. In spite of the slowing economy, the County's strengths (climate, infrastructure and workforce) are still anticipated to continue to provide a solid base for sustainable 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 1.3% to 2.2% per year. Payroll employment (number of jobs) is estimated at 1.53 million in 2007 and increases to 1.85 million by 2018 (Figure 1). Most of the growth will occur in the leisure and hospitality, education and government sectors of the economy. Sub prime market issues have caused sizeable job losses in regional finance-related and construction sector occupations which have a major presence in the County. Housing employment growth rate has reversed from 7.1% in 2006 to a decline of -1.6% in the first half of 2007.

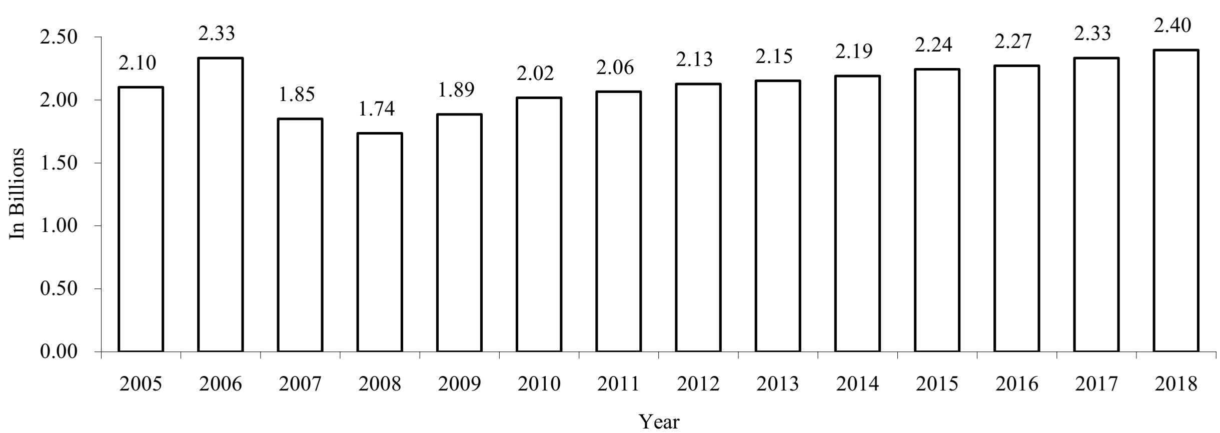
Figure 1



Residential Valuations - Residential valuations are expected to continue to decline before showing positive gain by 2009. Residential valuation, which measures the overall value of housing construction and improvements, increased by 11% in 2006 but is expected to decline by 20% during the current year. 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.

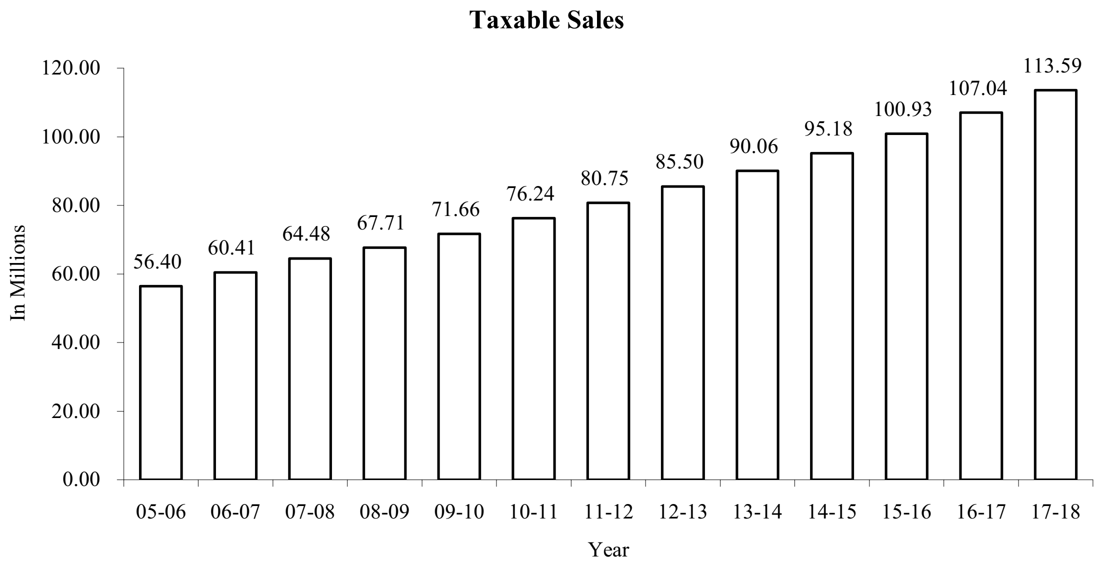
Figure 2

Residential Valuations (Permit Values-Housing Construction and Improvements)



Taxable Sales - Even with the slowdown in the economy, taxable sales are anticipated to grow annually over the forecast period as incomes rise and the population grows. County-wide taxable sales will increase from $64.5 million in 07-08 to $85.5 million in 12-13, representing an annual average sales growth rate of 5.8% (Figure 3).

Figure 3


Taxable Sales
In Millions
Year
120.00
100.00
80.00
60.00
40.00
20.00
0.00
56.40
60.41
64.48
67.71
71.66
76.24
80.75
85.50
90.06
95.18
100.93
107.04
113.59
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