Economic Forecast

Introduction - General Economy

The September 2013 UCLA Anderson Forecast indicates that the economy is moving toward a more normal pattern, and, although current economic conditions are better than the past four years, the current pace is not enough to fully offset the Great Recession in terms of income and employment. The forecast reports that real GDP is returning to a 3% growth path; the unemployment rate is moving toward 6.5%, and housing continues to rebound.

A report released by the Federal Reserve Board in October 2013 indicates that the twelve Federal Reserve Districts report "national economic activity continued to expand at a modest to moderate pace during the reporting period of September through early October." Trends in key economic indicators reflect modest to moderate growth, including increased consumer and business spending, employment and payrolls, and minimal growth in the demand for nonfinancial services.

Consumer sentiment declined sharply between September and October 2013, primarily due to uncertainty surrounding the federal government shutdown and debt-ceiling crisis. The Conference Board's *Consumer Confidence Index* fell 9.0 points in October 2013, from 80.2 points to 71.2 points (1985=100). Overall, recovery continues to be modest and economists project subdued growth through 2013 with slightly higher growth expected in 2014.

National Economy 

According to the Congressional Budget Office (CBO) Monthly Budget Review-Summary for Fiscal Year 2013, the federal government experienced a budget deficit of $680 billion in fiscal year 2013, which was a $409 billion decrease from the deficit in fiscal year 2012. When viewed as a percentage of the nation's gross domestic product (GDP), the deficit dropped from 6.8% in 2012 to 4.1% in 2013. In 2007, prior to the Great Recession, the deficit was 1.1% of GDP.

The three major sources of government revenues: individual income taxes, social insurance taxes, and corporate income taxes, increased by 12% or more in 2013. At the same time, total net government outlays declined by 2.4%. And, under current law, although federal debt held by the public is expected to be smaller in relation to the size of the economy in 2018 than it is now, the long-term outlook is not as positive. Several factors including the aging baby-boom population, growth in health care spending, and expansion of federal subsidies for health insurance are all expected to increase the government's spending for Social Security and major health care programs. Assuming no changes to current law, the additional spending may contribute to mounting budget deficits beginning in a few years.

Due to restrained economic growth, business owners, consumers, and investors are cautiously optimistic. CBO forecasts, released in February 2013, of percentage change for key National indices are presented as follows:

Indices		Forecast		Projected Annual Average	
		2013	2014	2015-2018	2019-2023
Real GDP	1	1.4%	3.4%	3.6%	2.2%
CPI	1	1.5%	2.0%	2.2%	2.3%
Unemployment	2	7.9%	7.8%	6.1%	5.4%
3-Mo. T-Bill	3	0.1%	0.2%	2.2%	4.0%
10-Yr. Treasury Note	3	2.1%	2.7%	4.5%	5.2%
Fed. Deficit % to GDP	4	3.7%	2.4%	N/A	N/A

Notes:
1 – Fourth Quarter to Fourth Quarter, percentage change
2 – Fourth-Quarter Level, Percent (Annual averages reported reflect value for last year in the range)
3 – Calendar Year Average, Percent
4 – Year-over-Year Change, as a percentage of Gross Domestic Product

California Economy 

The Governor signed the 2013-14 budget package on June 27, 2013, adopting a budget projected to end with a $1.1 billion reserve. In September 2013, legislation to address a federal order requiring the state to reduce the prison population provided $315 million (General Fund) in funding, which would lessen the projected ending reserve to $756 million.

The 2013-14 Budget Act assumes a decrease in revenue of $1.1 billion offset by fund balance carryover of $872 million and a projected operating surplus of $199 million. In May 2013, the LAO projected higher revenue due to a greater assumed level of capital gains and personal income tax revenues in 2013-14. However, after negotiations with the Governor, the Legislature passed a budget package that relied on the administration's lower revenue estimates.

Local economists, including forecasts by Chapman University and UCLA, predict that the slow pace of recovery will continue through 2015 with better, but not great, economic growth and moderate employment growth. Per Chapman University, the

California and Orange County economies could be facing higher unemployment rates as previously discouraged workers reenter the labor force; and interest income is still expected to remain flat through 2014. Positive signs are the steadily improved construction spending and continuing rebound in home prices.

UCLA, in its June 2013 report, agrees that the economy continues to recover slowly and is still in search of the “Great Recovery” that has typically followed recessionary periods. Their forecast is for a slightly better future than in recent years with 2015 expected to be better than 2014.

Forecasts by local economists of average, nominal percentage changes for key state indices are presented as follows:

Indices	Chapman		UCLA		
	2013	2014	2013	2014	2015
CPI	2.2%	2.6%	1.8%	2.3%	2.5%
Taxable Sales	5.4%	5.6%	2.1%	4.1%	4.5%
Personal Income	4.9%	5.3%	4.1%	5.7%	5.9%
Payroll Employment	2.1%	2.3%	2.6%	2.1%	2.1%
Unemployment Rate (not % change)	N/A	N/A	9.1%	8.1%	7.1%

<u>Orange County Economy</u> 

In Orange County, economic recovery continues to outperform national and state economic growth in many areas. Orange County recovery trends are also positive when compared to peer counties. In 2013, the County’s rate of unemployment continued to drop, and there was slight growth in jobs.

Two of the County’s funding sources are property taxes and sales taxes which track in correlation with changes in the housing sector and taxable sales activity. By 2012, both housing and sales trends showed growth, although the rates of growth have cooled from 2011 trends. Trends in 2012 and 2013 projections have been generally positive.

Overall, Orange County economic recovery is positive and rates of growth anticipated in the 2012 SFP have been equal to, or slightly better than, projected. Growth has been steady and is likely to remain positive. Key growth trends are highlighted in the chart below and additional discussion of key indicators follows.

(Year-to-Year Percentage Changes)

Indices	2009	2010	2011	2012	2013 Projected	2014 Forecast	Trend
Payroll Employment	-7.4	-1.3	1.1	2.3	2.3	2.6	
Total Personal Income	-6.8	1.3	4.8	4.1	5.3	5.9	
Taxable Sales	-14.7	4.3	8.5	6.3	5.9	6.1	
Permits – Dwelling Units	-30.4	40.5	55.5	42.8	30.2	11.1	
Consumer Price Index	-0.8	1.2	2.7	2.0	2.0	2.5	
Homes Index, Resale Single Units (1990 = 100)	-7.7	7.6	-5.7	4.9	15.7	8.8	

Source: Chapman University, *Economic and Business Review*, June 2013

Employment – According to Chapman University and data released by the California Employment Development Department, payroll employment in many metro areas is still below peak levels. The good news is that there was job growth during the first two quarters of 2013. From August 2012 to August 2013, Orange County has experienced job growth in all sectors. The following sectors with the highest year-over-year growth increased by: 9.4% in Construction, 6.5% in Financial Activities, 3.5% in Leisure and Hospitality, and 2.2% in Educational and Health Services. Orange County's rate of unemployment has declined to 6.2% and remains below the national rate of 7.3%.

Key employment indices and analysis for Orange County follow:

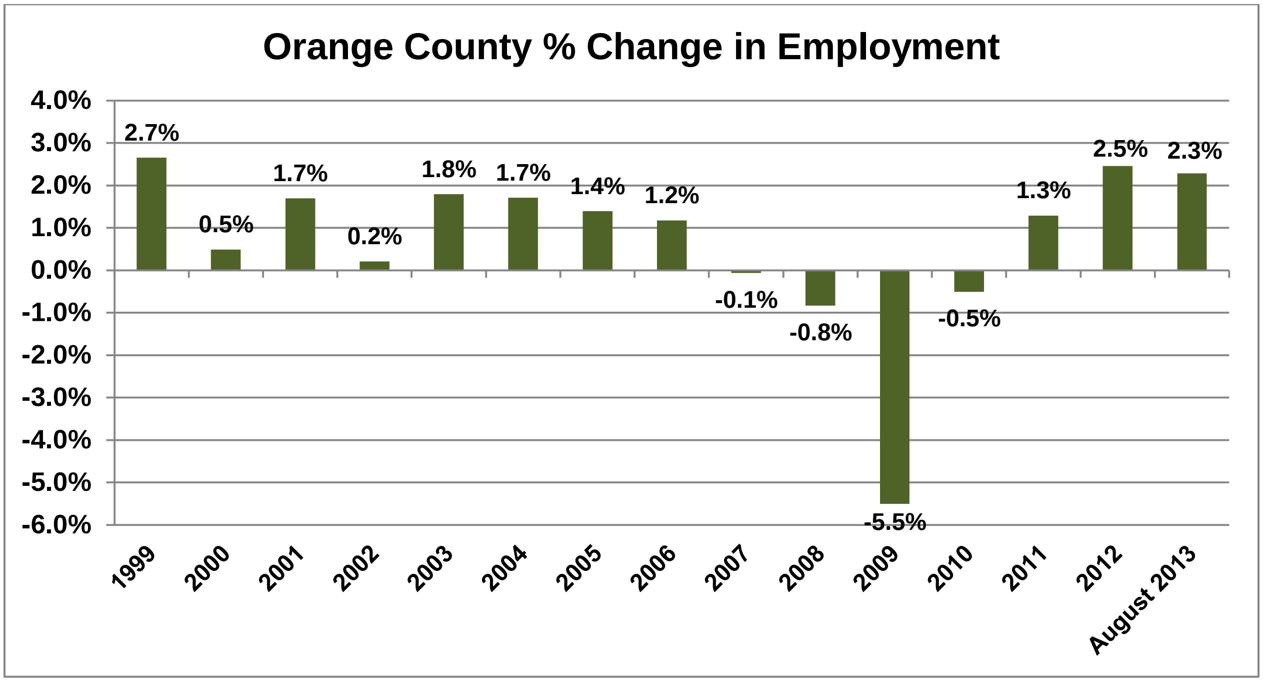
COMPARATIVE EMPLOYMENT STATISTICS (August 2013 preliminary)

	Total Labor Force	No. of Employed	% Unemployment
Los Angeles County	4,996,600	4,486,400	10.2%
Orange County	**1,633,900**	**1,532,900**	**6.2%**
Riverside County	937,100	835,600	10.8%
San Bernardino County	849,100	764,100	10.0%
San Diego County	1,608,300	1,488,700	7.4%

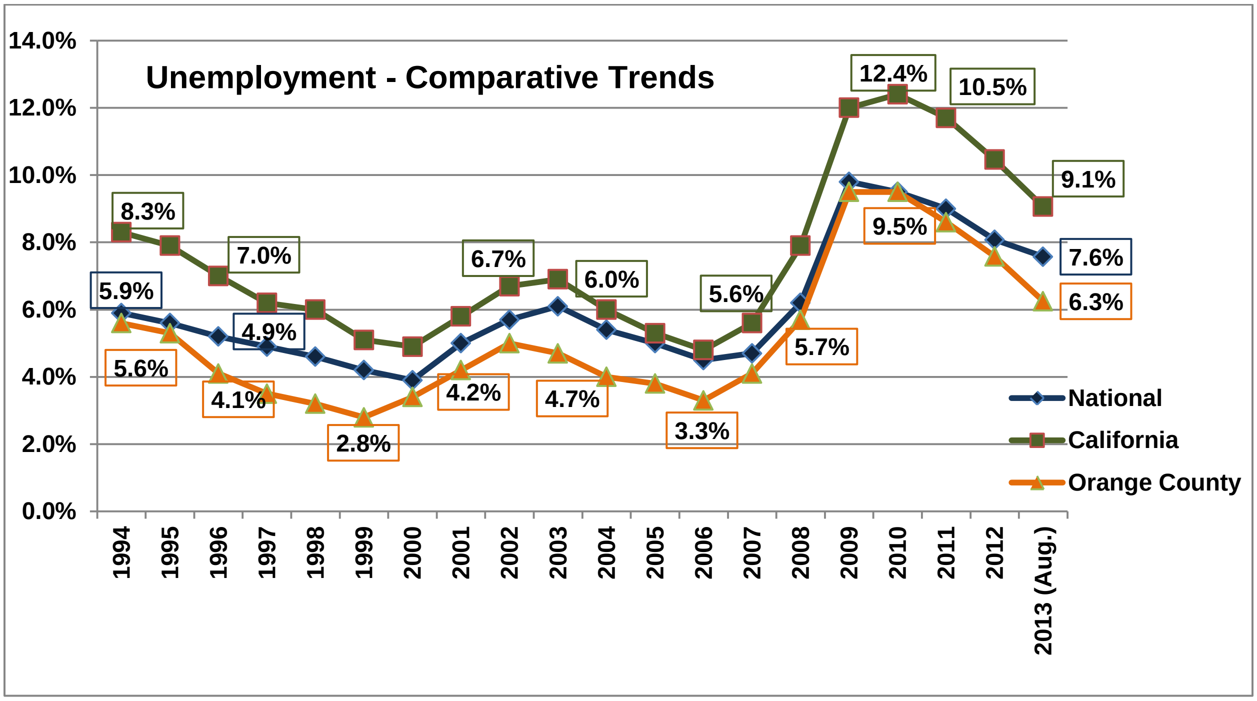
Source: State of California Employment Development Department

The Orange County Workforce Investment Board reported in October 2013 that Orange County industry employment was showing increases in the majority of industries, "with the greatest improvements coming from Education and Health Services, Construction, and Financial Activities." They also reported that the "Professional, Scientific, and Technical Services employment is expected to grow by 23.8% from 2010 to 2020." The

Chapman University California Employment Indicator Index reflected growth with a change from 112.7 in the second quarter of 2013 to 115.6 in the third quarter (an Index greater than 100 suggests job creation and growth).



Source: State of California Employment Development Department; August 2013 change is an average of 8 months ended August 31, 2013 compared to the prior year 2012 annual employment



Sources: US Bureau of Labor Statistics (National); State of California Employment Development Department (State and County); August 2013 data is the 8-month year-to-date average unemployment rate

Housing – The Southern California and Orange County housing market has experienced sharp increases in median home prices between 2012 and 2013, and foreclosures continue to drop. But unit sales growth has begun to cool as the inventory of homes for sale is limited.

In Orange County, 2013 housing trends, overall, have been on the rise, with a 25.8% increase in median sales price reported by DataQuick in August 2013. Total Orange County sales of residences in August 2013 were up 4.2% from a year prior with only Riverside County exhibiting a higher sales rate increase among peer counties. Foreclosures are down to 7.1% of the Southland resale market, and are at the lowest rate seen since the 5.5% experienced in June 2007.

Key housing indices and analysis for Orange County are as follows:

Peer Counties - Comparative Housing Analysis							
County	**Median Home Price**			**Unit Sales**			**Median Family Income**
(as of August 31)	**2012**	**2013**	**% Change**	**2012**	**2013**	**% Change**	**2013**
Los Angeles	$335,000	$429,000	28.10%	7,917	8,038	1.50%	$56,266
Orange County	**$445,000**	**$560,000**	**25.80%**	**3,337**	**3,477**	**4.20%**	**$75,762**
Riverside	$210,000	$265,000	26.20%	3,520	3,740	6.30%	$58,365
San Bernardino	$168,000	$210,250	25.10%	2,705	2,773	2.50%	$55,853
San Diego	$345,250	$415,000	20.20%	3,981	4,099	3.00%	$63,857
Ventura	$365,000	$450,000	23.30%	978	930	-4.90%	$63,857
So. California	$309,000	$385,000	24.60%	22,438	23,057	2.80%	$61,632

Data Sources: DataQuick (Housing)-Median Home Price as of August 31, 2013; and U.S. Census Bureau (Income); Median Family Income is as of June 2013

The following chart, based upon data published by DataQuick, summarizes trends in year-over-year growth as of October 31 (except where noted) for Orange County Median Home Prices and Unit Sales.

Foreclosure rates are calculated by dividing total County housing units per the U.S. Census Bureau by the total number of properties that received notices of default (new filings, foreclosure in process, not yet recorded) within the month. The lower the second number is in the ratio, the higher the foreclosure rate (e.g. 1 in 100 is higher than 1 in 1,000). RealtyTrac, Inc. forecasts that 1 in 1,323 Orange County homes received a foreclosure filing in September 2013. Among peer counties, Orange County had the lowest foreclosure rate in September (see table below). For the first nine months of 2013, there were 4,357 notices of default issued and trustee's deeds filed (completed and recorded) of 1,432. In calendar year 2012, there were a total of 13,209 notices of default and 4,847 trustee deeds issued. RealtyTrac reports that, to date, the average foreclosure sales price in Orange County was $426,000, approximately 23% lower than non-distressed home prices.

Foreclosure Statistics	
	Foreclosures
Los Angeles County	1 in 1,017
Orange County	**1 in 1,323**
Riverside County	1 in 519
San Bernardino County	1 in 542
San Diego County	1 in 1,058

Source: RealtyTrac, Inc.

Taxable Sales – Taxable sales represent consumer spending transactions that are subject to sales and use taxes. The California Board of Equalization (BOE) reports sales on a quarterly basis, generally two quarters in arrears (the Department of Finance provides monthly projections two months in arrears). Taxable sales provide an indication of economic activity and drive County funding sources such as General Purpose Revenue sales taxes and General Fund department sources such as Public Safety Sales Tax and a portion of Realignment Revenue.

After steep drops in years 2007 through 2009, there has been growth in taxable sales in years 2011 and 2012 and modest rates of growth are projected for 2013 and 2014. At September 30, 2013, General Purpose Revenue sales tax receipts were approximately 5.0% higher than the same period in the prior year. General Fund sales tax receipts typically trend with taxable sales. Orange County historical taxable sales are summarized in the following table:

Orange County Trends – Taxable Sales in the 3rd Quarter		
For the 3rd Quarter / Calendar Year	**Taxable Sales (Billions)**	**Percent Change**
2014 (f)	$15.65	6.1%
2013 (f)	$14.75	6.1%
2012	$13.90	6.3%
2011	$13.08	8.1%
2010	$12.10	4.6%

Table continued on following page

Table continued from previous page

Orange County Trends – Taxable Sales in the 3rd Quarter		
For the 3rd Quarter / Calendar Year	**Taxable Sales (Billions)**	**Percent Change**
2009	$11.57	-15.2%
2008	$13.64	-4.3%
2007	$14.26	-2.1%
2006	$14.57	2.8%
2005	$14.17	9.2%

Source - State Board of Equalization through 2011; Chapman University (June 2013) for 2012, and Forecast (f) years 2013 and 2014

Taxable sales tend to increase when personal income increases. Based on Chapman University's June 2012 Economic & Business Review report, total personal income is projected to increase by 4.9% to 5.3% in the next two years which is slightly less than the forecasts for future taxable sales increases.

Other Economic Data – There are other positive indications that Orange County recovery is gaining speed.

- In September of 2013, the Orange County Automobile Dealers Association reported that registrations of new cars and light trucks increased by 11.9% during the first three quarters of 2013 when compared to a year earlier, and forecasted growth in 2014 is expected to increase by 7%.
- Bankruptcies in the County decreased 26.5% in September from a year earlier. This provides another sign that the local economy is recovering, although the number of monthly filings is still far more than what is was before the start of the recession.

Summary

The economy is attempting to return to normal, but it is anticipated that the momentum will be modest over the next year. After the crash of 1929, it took nearly 25 years for the housing market to recover and for economic balance to be restored. During that time, the economy reinvented itself with new labor policies, changes in manufacturing technologies, and unionization.

As the County works through its recovery from the Great Recession, it must keep in mind that returning to normalcy will likely be a long and protracted process. Recovery levels that impact County funding sources suggest that continued focus on rebenchmarking and/or re-tooling already established programs and services is necessary. Key questions that continue to need answers include:

- How can costs be stabilized or reduced without sacrificing quality?
- What impact will long-term investing in technology and human capital contribute to productivity?
- What are the best ways to identify critical needs and measure performance success?

Beginning in 2007, Orange County made adjustments to smooth out the impacts of the Great Recession. Through the diligent efforts of Departments and thoughtful and timely action by the Board of Supervisors, the County has been able to maintain key services with fewer resources. The County has also taken slow and deliberate action to ensure that actions taken now do not create long-term, unintended consequences. Orange County continues to carefully plan for today and the future to ensure that the County remains “a safe, healthy, and fulfilling place to work, and play, today and for generations to come.”

“Setting a goal is not the main thing. It is deciding how you will go about achieving it and staying with that plan.” ~ Tom Landry