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2012 Central Coast Economic Forecast

Presented by Beacon Economics

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U.S. Forecast

by Christopher Thornberg

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Key Chapter Findings

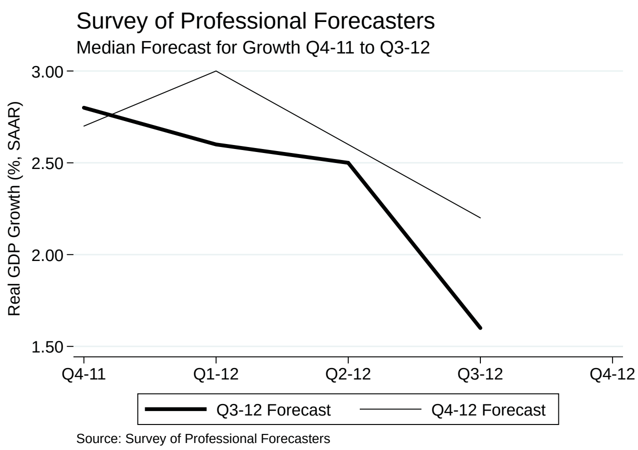
- Expect the U.S. economy to grow somewhere in the 2.5% range in the second half of 2013. Beacon Economics' outlook is more optimistic than many forecasting organizations.
- The current soft patch in the U.S. economy may be less dire than believed. The second quarter was disappointing for economic growth, but turned out better than might have been expected given falling retail sales, declining orders for durable goods, flat industrial production, and weak employment growth. Overall GDP growth came in at 1.7%—and it was 1.88% for the private sector alone.
- Economic weakness in the euro zone is not helping the U.S. economy. Problems in Europe have caused the value of the U.S. dollar to rise, and the weak demand for imports from Europe is having a negative effect on the global economy. But the risks may be overstated. Although European leaders have shied away from taking dramatic steps, they have shown resolve in the face of immediate challenges.
- On January 1st the United States will see a sharp increase in taxes and a large decline in federal spending if the two parties cannot agree on a budget compromise. The overall shock to the system amounts to roughly $550 billion, or $410 in tax increases and $140 in spending cuts over the course of the year. The shock to the country will be substantial, but only if this budget remains in place for a sustained period of time in 2013. In other words, it is more of a fiscal hill, where we start to roll slowly but pick up speed over time.
- Why does the economy feel so fragile? It has much to do with the fact that we didn't get the same bounce in growth we typically get after recessions. After the mid-70's and the early-80's downturn the economy grew close to 6% for two years—erasing economic losses that occurred during those recessions. It didn't happen this time—we simply moved into a standard private sector expansion with no bounce.

Bruised, But Still Optimistic

With the presidential election just weeks away, most of today's news is dominated by campaign rhetoric. The political debates have, not surprisingly, confused issues, twisted statistics, and assigned both blame and credit in all the wrong places. The reality is this: the U.S. economy continues to be in the midst of the slow but steady expansion that began three years ago when the Great Recession came to an end. And current evidence suggests to Beacon Economics--in contrast to what many other forecasts have been saying--that the second half of 2012 will look modestly better than the first half.

It's true that the economy isn't as strong as initially hoped for. Beacon Economics had predicted growth rates in the 3% plus range for the second half of 2012, but like many forecasters, have had to push estimates down. The following chart tracks the median forecast for economic growth from the Philadelphia Federal Reserve's Survey of Professional Forecasters over the last few releases. The estimate for second-half growth has declined from 2.8% to 1.9% over the last half year--a large negative shift in the outlook.

The downgrades have occurred for any number of reasons. Problems in Europe have escalated as European leaders have dithered over needed reforms. Here in the United States, poor consumer spending figures in the second quarter raised angst about the health of this important driver of the U.S. economy. More recent data shows U.S. manufacturing output plateauing. And of course there are worries about the so-called "fiscal cliff" the nation is facing at the start of 2013, when a number of temporary tax cuts end as a result of Congress's inability to reach a compromise on reducing the long-term deficit.



While recent data have been disappointing, Beacon Economics expects better growth in the second half than the consensus forecast of 1.9%. That is, even though some of the data are not as strong as we would like, other numbers offer signs of modest acceleration in the economy. Moreover, Beacon Economics is less worried than others about the fiscal cliff—we believe there is a natural mechanism that will prevent the issue from becoming a true stumbling block for the economy.

Most importantly, both the Federal Reserve and the European Central Bank have recently announced plans for large liquidity injections into their respective economies. This is much needed in Europe, where fiscal austerity in the south requires some short-run countervailing force. The results are already clear—spreads on Spanish, Italian and Portuguese debt over German bonds have come down sharply in recent weeks.

As for the Federal Reserve's actions, Beacon Economics was—to speak candidly—a bit shocked by the announcement to purchase $40 billion in mortgage backed securities monthly for an indefinite period of time. We don't consider recent trends in the U.S. economy sufficiently negative to warrant yet another round of quantitative easing, nor are we convinced that the action will have that much of an impact. And there is already plenty of evidence that the real estate market is moving firmly into recovery mode.

Why do this now? We may never know for sure but here are a few speculative thoughts:

- The Fed's board members may simply see the recent economic figures in a more negative light, or equivalently they don't feel the status quo is good enough. This is worrisome—in Beacon Economics' opinion direct economic interventions should be reserved only for periods of decline.
- The move may have been made to try and offset worries regarding the fiscal cliff. There did appear to be a positive reaction in the equity markets—although this has somewhat faded.
- Alternatively, the move might have been made to help the United States avoid some of the potential negative consequences of the recent actions by the European Central Bank, such as the likelihood of an appreciating dollar vis-à-vis the euro.
- Lastly, there is also a conspiracy theory circulating that the move was made to help support European banks. The bonds the Fed are buying are fairly high quality. Such buyers will need to allocate capital somewhere—and buying assets from capital starved European banks might well be the ultimate resting place for some of this cash.

In any case, the actions of the Federal Reserve can't hurt in the short run, given that it would take two years for it to hit the same quantity of cash pumped into the economy through QE1. We don't see any immediate inflation concern for investors, but it is something to keep in mind for the medium term.

The Private Sector is Doing Fine.

So where is the economy today? Given the rhetoric being thrown about by the campaigns and in the press, one might think the U.S. economy was in the midst of a massive economic crisis. The reality is a bit more placid. The economy is currently in the midst of a three-year expansion characterized by rising economic output, rising wages, improving asset values, and falling unemployment.

It is true that recent GDP growth has been slower than normal, at 2.1% over the last two years compared with 3% for the two decades prior to the recession. But this has nothing to do with the health of the private sector. Quite the opposite, growth has been slower because of declines in spending in the public sector. Typically, growth in direct government spending adds roughly one-third of one percent to growth, while over the last two years it has shaved two-thirds of one percent off overall growth per year. In other words, it is the sole reason why growth is one percentage point lower than normal. When we look at just the private sector, growth is more or less occurring at an average pace.

As for the source of growth, it isn't just consumer spending. Indeed, contributions from spending have been slightly less than average, with the balance made up by greater-than-normal growth in spending on construction and business investments. This latter fact may be a bit of a surprise, since pundits have been repeating the mantra that businesses are afraid to invest because of excessive regulation, fears over healthcare costs, or the impending fiscal cliff. It simply isn't true—at least not in the way that the Bureau of Economic Analysis measures business investment.

Even employment growth in the private sector looks decent. We have seen a 1.8% pace of growth in private sector jobs over the past two years, compared with 1.5% for the two decades prior to the recession. Unemployment is still higher than normal at 8%, but again, the longer-term average is about 6%--this is hardly a dramatic difference. And it is falling—2 percentage points in 2 years. That is a normal pace of decline for an expansion.

Trends in Real GDP Growth
Contributions to % Change in Real GDP

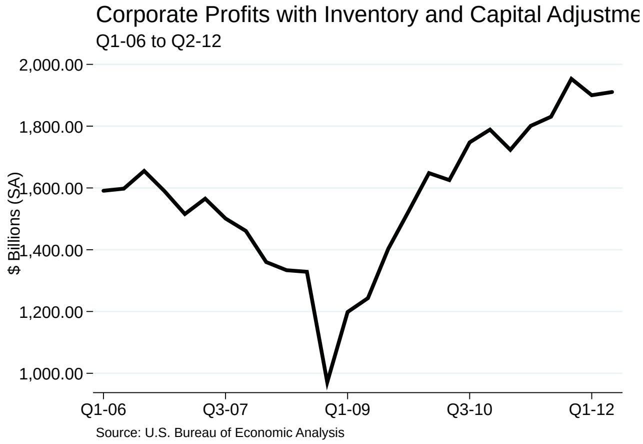
GDP Component	1988 to 2007	Q3-10 to Q2-11	Q3-11 to Q2-12
GDP	2.97	1.90	2.28
Private GDP	2.65	2.56	2.73
Personal Consumption	2.19	1.88	1.39
Non-Res Structures	0.04	0.03	0.31
Equipment and Software	0.54	0.65	0.64
Residential	0.03	-0.18	0.23
Net Exports	-0.14	0.22	-0.06
Government	0.32	-0.66	-0.45
State and Local	0.28	-0.49	-0.19
Unemployment	6%		8%
Participation Rate	66.10%		63.70%
Private Sector Employment	1.5%	1.8%	1.8%
PPP Per Capita Income Rank of Top 30		#1	

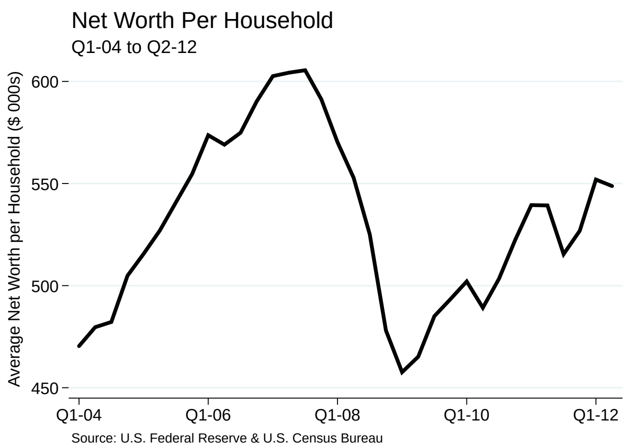
Source: Bureau of Economic Analysis

But what of the U-6 figure you might ask? That includes discouraged workers and is close to 14%. Doesn't that mean the labor market is much worse than the headline number? The U-6 is a tricky number—not that it isn't a relevant figure—but because it is always slightly less than two-times headline unemployment. In good times it is close to 10%. This isn't to diminish the troubles these individuals and households are experiencing—they need help through tough times. But the trends suggest an economy on the mend, not in decline.

And of course the financial statistics are even better. Corporate profits are at record high levels and even household net worth is up 10%. The stock market bounced back from its second quarter swoon. Bank balance sheets are starting to expand, interest rates are amazingly low, and the most recent data from the

Federal Reserve's Survey of Senior Loan Officers show credit standards are loosening for borrowers.





Given all this, why does the economy feel so fragile? It has much to do with the fact that we didn't get the same bounce in growth we typically get after recessions. After the mid-70's and the early-80's downturn the economy grew close to 6% for two years—erasing economic losses that occurred during those recessions. It didn't' happen this time—we simply moved into a standard private sector expansion with no bounce.

Why? There are a number of reasons as we have discussed in past reports. Part of it is due to a variety of misplaced policy priorities, with both parties to blame. It is also the result of the depth and nature of the recession itself. Regardless it implies that the U.S. economy is clearly still well below the long-term trend line it was on prior to the recession. Nonetheless, the U.S. has the highest per capita income of the 30 largest nations in the world (representing 85% of world output), so we shouldn't feel too bad about our lot. From the perspective of the vast majority of the world's population, we still live on the proverbial easy street.

With this in mind, there are three concerns looking ahead: the current soft patch in the economy, the ongoing euro-zone malaise, and the fiscal cliff in the new year. How concerned should we be? We'll look at each of these in turn.

How Soft is the Soft-Patch

The current soft patch in the U.S. economy may be less dire than you've heard. The second quarter was disappointing for economic growth, but turned out better than might have been expected given falling retail sales, declining orders for durable goods, flat industrial production, and weak employment growth. Overall GDP growth came in at 1.7%—and it was 1.88% for the private sector alone.

Stronger growth in consumer spending on services made up for declines elsewhere. While growth in construction spending slowed, business investments maintained a decent pace. In addition, the trade deficit narrowed mainly driven by a decline in imports, which suggests that more consumption was being sourced from domestic producers. In short, the top-level number is well within the range of the typical ebbs and flows of a growing economy.

More important, recent data for the third quarter paints an improving, if mixed, picture. On the consumer front, July's monthly figures from the Bureau of Economic Analysis showed real spending growing again for the first time since April. The August figures are likely to be strong as well. Auto sales hit 14.6 million (SAAR), the highest number yet in 2012 and the highest since the recession began.

Real GDP Growth by Component
Contributions to % Change in Real GDP

GDP Component	Q1-12	Q2-12
Gross domestic product	2	1.7
	2.6	1.88
Personal Consumption	1.72	1.2
Durable Goods	0.85	0.00
Nondurable Goods	0.26	0.09
Services	0.61	1.11
Fixed Investment	1.18	0.63
Structures	0.35	0.08
Equipment and Software	0.39	0.34
Residential	0.43	0.20
Change in Inventories	-0.39	-0.23
Net Exports	0.06	0.32
Exports	0.60	0.82
Imports	-0.54	-0.51
Government	-0.60	-0.18
Federal	-0.34	-0.01
State and local	-0.26	-0.17

Source: Bureau of Economic Analysis

Retail sales numbers are also on the rise and have already erased the declines seen in the second quarter. We have to be cautious, though, since these are nominal values, and the price of gasoline is heading up at the pumps again. But even with gasoline sales removed, the numbers are still clearly trending upward and show a willingness to spend.

More good news comes from the housing sector, where home prices and construction permits have clearly trended into positive territory, while sales of existing homes leaped in August. According to all the major price measures, home values are now 2% to 3% above where they were last year at this time. Housing starts have also continued to rise, hitting 750,000 in August. Given that the large stock of REO units continues to fall, alongside declines in the number of foreclosures, it is likely that the housing recovery will continue.

To be sure, we don't expect the market to accelerate explosively. The lack of home equity is constraining the move-up market, and the number of foreclosures, though falling, is still high, suggesting that most of the new demand will be for rental units. Nevertheless, we expect housing to continue to add to growth for the near future.

Graphs: MBA share of serious delinquent and foreclosures in process shares, home equity as a share of housing values (FOF stats) , households by tenure from the HVR all stuff from my presentation

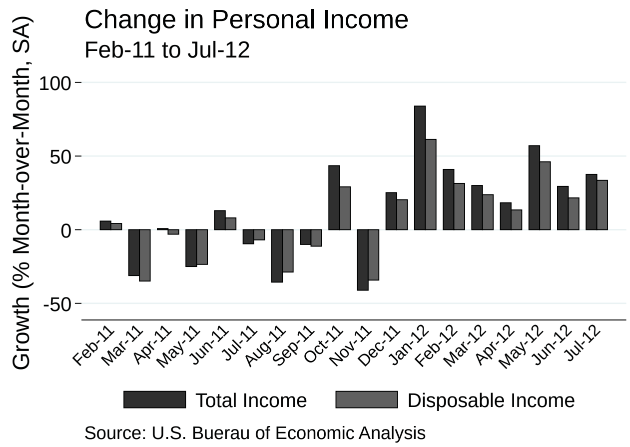
The employment report in August was clearly disappointing. The nation has added only 110,000 jobs monthly for the last three months. But there are still some positive signs in the report. For one, much of the job growth has occurred in the professional services sector, which has relatively well-paying jobs. Unemployment is now at 8.1%, well below last year's rate of 9%.

And while the negative spin on last month's decline was that it was due to people leaving the workforce, this conveniently neglects to mention the fact that the uptick was due to an odd surge in the number of people entering the workforce. The survey used to estimate unemployment is small and is subject to fluctuations, so we should be wary of drawing any sharp conclusions from a few months of data. Most importantly, real personal income continues to grow, after having stalled out in 2011; ultimately, higher incomes will drive the rest of the economy.

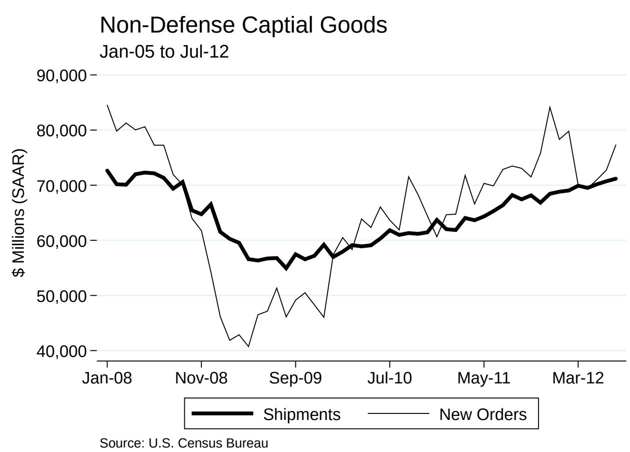
Trends in Employment Growth
Average Monthly Changes (000s)

Industry	1997 to 2007	2011 to 2012
Total Nonfarm	128.6	147.7
Total Private	107.4	165.6
Construction	13.8	1.9
NR/Mining	0.8	5.3
Manufacturing	-26.8	19.8
Wholesale Trade	3.4	8.7
Retail Trade	9.5	11.9
Transport/Warehouse	4.6	7.5
Utilities	-0.5	0.7
Information	0.2	-2.4
Financial Activities	8.9	3.7
Professional/Business	32.2	47.5
Education/Health	35.5	33.8
Leisure and Hospitality	20.1	25.7
Other Services	5.9	1.8
Government	21.3	-17.9
Labor Force	142.5	51.6
Employment	139.5	144.1

Source: Bureau of Labor Statistics



The one bit of bad news comes from the manufacturing front. The ISM surveys have been running below 50 for the last three months, implying contracting activity. Industrial production growth has also slowed in recent months. But even here things seem to be turning a corner. July's durable goods orders popped up, erasing much of the slowdown seen in previous months, and shipments continued to rise.



We expect growth in the third quarter to exceed growth in the second quarter. Look for the economy to grow somewhere in the 2.5% range in the second half of the year. And while there is the potential for a downside risk, there is also the potential for growth to pick up steam, particularly with the new push from the Fed.

The Euro-Zone Malaise

The economic weakness in the euro zone is not helping the U.S. economy. Problems in Europe have caused the value of the U.S. dollar to rise, and the weak demand for imports from Europe is having a negative effect on the global economy. But even here the risks may be overstated. Although the leaders of Europe have shied away from taking dramatic steps to reverse the course of the slowdown, they have shown resolve in the face of immediate challenges.

Most recently, the European Central Bank announced plans to start large purchases of government debt, an act that will surely push rates down for those southern nations at the heart of the crisis. An injection of liquidity can do a lot to offset some of the current strains, both by reducing the interest rate burdens for nations running fiscal deficits and by giving the large European banks some breathing room in order to continue to buttress their balance sheets.

As noted, some U.S. investors (mainly hedge funds) are also starting to help. Seeing a potential deal in their frustrating hunt for yield, they are moving to purchase assets from some of these banks. This will surely hurt the banks' earnings in the long term, but in the short term it raises some much needed capital. And with the Federal Reserve starting to vacuum up $40 billion in high value assets monthly, we may see this trend increase.

As with U.S. monetary policy, this is no long-term panacea. Liquidity is a good salve for the symptoms of underlying problems, but only through the painful political process of deregulation and reduction in government spending will southern European nations be able to stay in the euro zone. Whether they truly have the will to take action remains to be seen.

But in the short term the injection of liquidity will keep the pace of this crisis slow, which is a good thing, since investors have largely been able to get out of the way. The danger of an imminent financial panic seems to be fading, since the risks are understood at this point in time. It remains a "wait and see" situation. In the meantime, while export growth has slowed for the United States, it is nonetheless still increasing.

Stumbling Along the Edge of the Cliff

Turning to our budget problems here at home, we are facing what has been called a "fiscal cliff." Let us say this in no uncertain terms--*there is no such thing.* It is true that on January 1 the United States will see a sharp increase in taxes and a large decline in federal spending if the two parties cannot agree on a budget compromise. The overall shock to the system amounts to roughly $550 billion, or $410 in tax increases and $140 in spending cuts over the course of the year—an enormous shock that could carry a recession-causing impact. But this does not mean that a recession will begin as of January 2. The shock to the country will be substantial, but only if this budget remains in place for a sustained period of time in 2013. In other words, it is more of a fiscal hill, where we start to roll slowly but pick up speed over time.

If the shutdown of the federal government in the 1990s under then-House Speaker Newt Gingrich is anything to go by, the political pressure on politicians to find a compromise will grow exponentially once the checks stop arriving and the tax bills start piling up. And both parties know what it will mean for them politically if they are viewed as the obstruction—a potential clean sweep for the other side in the mid-term elections in 2014. We predict that even if there is no agreement by the deadline, some compromise will be reached in time to avert a major crisis. Could a crisis occur? Politicians have charged like Lemmings off the cliff in the past—but it's unlikely this time. The short-run solutions are too easy.

One point of confusion regarding the potential fiscal cliff in the new year needs to be cleared up, however. The idea that the increase in taxes will cause a recession in the United States would seem to support the Republican Party mantra that the path to faster long run growth is through lowering tax rates permanently. But we must be careful to separate the impact of the level of tax rates and the impact of the change in the level of the tax rate.

It is absolutely the case that a change in the level of the tax rates has a positive or negative impact on the economy if tax rates are lowered or raised, respectively. But this impact, positive or negative, is transitory—once a new level is arrived at and the economy reorganizes itself around this new level, there is a drift back to normal long-run growth.

The upcoming changes in tax policy on January 1 only have the potential to lead to a fiscal cliff because the tax rate changes so much, so rapidly. If the changes were phased in over time, they would have a much smaller negative impact. And ultimately, whether the rate is as it was under Clinton, or what it might be as proposed by the Romney campaign, long-term growth rates are sure to be largely the same—after all the 1990s saw a very healthy economic expansion.

If we consider only the new level of taxes, apart from their sudden onset, it seems that these taxes will have some modest negative long-term implications for economic growth, but these changes are quite small within the level of taxation seen in the United States over the last few decades. Indeed, economists who look for a tax rate effect (for example, looking at differences across states) have a tough time finding it. There are many other factors that seem to carry a larger impact. Hence both Texas and California have been economic success stories in the United States despite having different tax rates. Similarly, the U.S. economy grew considerably faster in the 1990s than it did in the decade after the Bush tax cuts kicked in.

Of course this discussion ignores the long-term issues facing the U.S. government deficit. The Congressional Budget Office recently released some truly startling projections of a blown-out government budget... in the late 2020s. The U.S. government has made promises it clearly cannot afford to keep in the long run and something will have to be done. But, given the political partisanship that has wiped away any ability for compromise, and given the still-fragile state of the U.S. economy, that time is not now. The U.S. economy is showing signs of strengthening and there will be time to address these issues once the healing is complete.

U.S. Historical Table

United States	Q1-2010	Q2-2010	Q3-2010	Q4-2010	Q1-2011	Q2-2011	Q3-2011	Q4-2011	Q1-2012	Q2-2012
National Real GDP ($ Bill.,SAAR)	12,924.00	13,000.80	13,089.50	13,167.50	13,171.60	13,255.80	13,301.60	13,446.10	13,514.80	13,597.20
Growth (%,SAAR)	2.30	2.20	2.60	2.40	0.10	2.50	1.30	4.10	2.00	1.70
Real Personal Consumption ($ Bill.,SAAR)	9,100.80	9,159.40	9,216.00	9,308.50	9,380.90	9,403.20	9,441.90	9,489.30	9,546.80	9,609.80
Real Investment ($ Bill.,SAAR)	1,591.40	1,646.40	1,710.10	1,684.30	1,661.60	1,711.30	1,735.80	1,867.30	1,895.10	1,909.20
Real Government Expend. ($ Bill.,SAAR)	2,604.50	2,623.70	2,622.30	2,593.00	2,545.70	2,540.90	2,521.80	2,507.50	2,488.40	2,482.90
Real Net Exports ($ Bill.,SAAR)	-372.70	-428.70	-458.90	-418.30	-416.60	-399.60	-397.90	-418.00	-415.50	-404.70
Total Nonfarm Empl. (Mill, SA)	129.32	129.96	129.92	130.23	130.68	131.24	131.53	131.99	132.68	133.01
Growth (%,SAAR)	-0.40	2.00	-0.12	0.94	1.42	1.70	0.90	1.39	2.13	1.00
Unemployment Rate (%,SA)	9.77	9.63	9.53	9.57	9.00	9.03	9.07	8.70	8.27	8.17
Personal Income ($ Trill.)	12.09	12.29	12.40	12.51	12.86	12.94	12.98	13.02	13.23	13.36
Growth (%,SAAR)	7.75	6.81	3.51	3.69	11.55	2.59	1.16	1.27	6.60	4.15
Savings Rate (%)	4.18	5.04	4.87	4.31	4.56	4.07	3.48	3.02	3.23	3.54
Tax Rate (%)	9.57	9.54	9.77	9.89	10.68	10.79	10.82	10.90	10.97	11.04

Forecasts by Beacon Economics

U.S. Forecast Table

United States	Q3-2012	Q4-2012	Q1-2013	Q2-2013	Q3-2013	Q4-2013	Q1-2014	Q2-2014	Q3-2014	Q4-2014
National Real GDP ($ Bill.,SAAR)	13,679.12	13,762.70	13,828.01	13,904.71	13,981.78	14,085.28	14,196.90	14,306.59	14,443.40	14,553.81
Growth (%,SAAR)	2.43	2.47	1.91	2.24	2.24	2.99	3.21	3.13	3.88	3.09
Real Personal Consumption ($ Bill.,SAAR)	9,688.22	9,746.22	9,775.58	9,824.47	9,855.02	9,911.58	9,961.39	10,011.00	10,089.83	10,128.36
Real Investment ($ Bill.,SAAR)	1,917.99	1,951.01	1,990.86	2,021.22	2,061.29	2,092.43	2,137.46	2,177.52	2,217.24	2,277.13
Real Government Expend. ($ Bill.,SAAR)	2,480.46	2,478.13	2,476.53	2,476.59	2,476.79	2,478.44	2,480.74	2,483.14	2,486.31	2,489.82
Real Net Exports ($ Bill.,SAAR)	-407.55	-412.66	-414.97	-417.56	-411.32	-397.17	-382.68	-365.07	-349.97	-341.50
Total Nonfarm Empl. (Mill, SA)	133.24	133.69	134.18	134.71	135.28	135.91	136.60	137.31	138.09	138.87
Growth (%,SAAR)	0.71	1.34	1.48	1.58	1.70	1.88	2.03	2.11	2.28	2.29
Unemployment Rate (%,SA)	8.30	8.30	8.22	8.10	7.97	7.83	7.69	7.54	7.41	7.27
Personal Income ($ Trill.)	13.62	13.78	13.95	14.10	14.27	14.44	14.63	14.82	15.02	15.22
Growth (%,SAAR)	7.85	4.80	4.98	4.55	4.81	4.95	5.18	5.45	5.53	5.54
Savings Rate (%)	3.84	3.97	4.09	4.08	3.96	3.83	3.70	3.58	3.47	3.65
Tax Rate (%)	11.02	11.02	11.28	11.48	11.84	12.07	12.37	12.73	12.89	13.09

Forecasts by Beacon Economics

California Forecast

by Jordan G. Levine

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Key Chapter Findings

- In recent quarters, California has largely escaped the doldrums seen in the rest of the nation. The state is poised for continued growth, though the pace of recovery will leave something to be desired.
- Although California's August job numbers were disappointing, they did show steady employment increases across the state's major regions. Beacon Economics is forecasting that employment growth will average roughly 2% during the remainder of 2012 and into 2013, before picking up steam and growing by between 2.5% and 3.0% per year from 2015 through 2017.
- Taxable sales in California posted their 12th consecutive quarterly increase in the second quarter of 2012, and California has consistently outpaced the U.S. economy on this front. Beacon Economics is forecasting that taxable sales will grow by an average of 7% over the next year, reaching their pre-recession peak by the end of 2012. Expect growth to settle out in the 5% to 7% range in nominal terms.
- Real estate has finally begun to add to the state's economy rather than detract from it. Beacon Economics expects home prices to grow at roughly 7% in 2012 and at roughly 5% in 2013, before settling out in the mid-3% range in 2016 and 2017.
- In California, export growth has slowed from the double-digit growth experienced in 2010 and 2011. Exports have continued to increase in 2012, albeit at a more tepid pace. The dollar depreciated slightly against the euro in August, suggesting that investors are slightly less pessimistic about Europe's prospects than they were earlier in the year—helping support demand from abroad.

California Overview

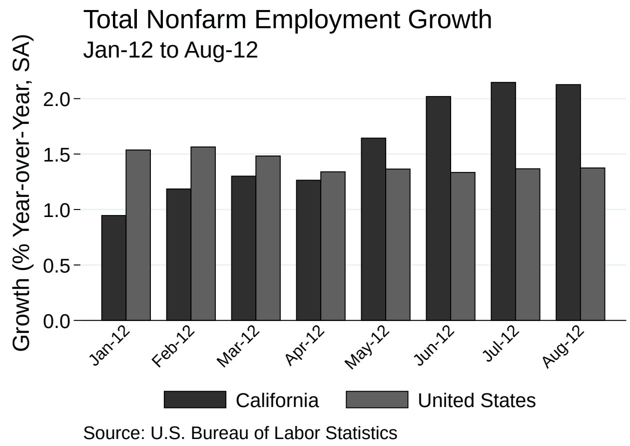
The nationwide midsummer slowdown in economic and employment growth has sparked new fears about the short-run direction of the economy. However, California has largely escaped the doldrums seen across the rest of the nation over the past few quarters, and the state is poised for continued growth, though the pace of that recovery will still leave something to be desired.

Several external risk factors are looming, such as the impending "fiscal hill," the ongoing issues in the euro zone, and of course the upcoming elections, but fears over what these risks mean for California's economy are likely overstated. A major calamity in Europe would certainly affect California's exports to the rest of the world, both through reduced demand from Europe directly and through shifts in the exchange rate, given that the U.S. dollar would likely appreciate in the wake of a European meltdown. However, European Central Bank officials have recently committed to providing additional liquidity to their banks, which should help to stave off a major crisis. And although export growth has slowed, exports from California have still been rising in 2012. Regarding the fiscal hill, if no compromise is reached by January 1, the increase in taxes could impede consumer spending over the short run as households adjust to new tax levels, but some of this effect will be offset by rising incomes and by a healthy labor market—an increasing number of Californians are getting back to work.

Not only are some of the potential risks to the economy likely overblown, but some of the truly bright spots in California's economy remain unreported, vanishing into the ether of the popular press. Consumer spending, housing, commercial real estate, bank lending, exports, personal income, and the labor markets all continue to move forward. Is it time to start popping the champagne corks? No. We still have elevated levels of unemployment, defaults, and foreclosures; a state government budget that is chronically in the red; and local government budgets that are reeling from the effects of the Great Recession. Is the worst clearly behind us and is the Golden State poised for slow but steady growth as the recovery progresses? Absolutely. California continues to move forward and has even begun to lead the nation—several key indicators suggest that California is helping to drive the rest of the U.S. economy through the recovery process.

Labor Markets—Lurch or Leap?

It's true that California's labor markets have not sprung back to life in the wake of the current recession, certainly not in the manner experienced in the post-recessionary periods of the 1980s and prior. However, California is not on the brink of disaster. August was a relatively lackluster month for job growth in the state, with only 12,000 new positions added. Nonetheless, although we lost 7,400 jobs in the public sector, the private sector expanded by nearly 20,000 positions. The largest gains of late have come from Construction and Leisure and Hospitality, which together produced 9,500 jobs in August alone. Through August, California has added more than 173,000 jobs to its nonfarm employment base. In addition, the unemployment rate ticked down to 10.6% in August, though 65,000 Californians dropped out of the labor force. Thus, while the employment report for August was not stellar, it indicates that California's economic recovery continues to make progress.



Even though job growth in the most recent report was not anything to get excited about, the previous three months showed above-average growth. In fact, during the second quarter, California actually leapt ahead of most other states in the nation in terms of creating new jobs. This may be hard to believe, given that we are constantly bombarded with rhetoric claiming that California's business climate is unfriendly and business-killing, but the state accounted for half of all the jobs created nationwide in May and all of the job growth in the United States in June. Even the national media took note of this strength with headlines such as, "California Defies Lower-Tax Texas in Creating More Jobs."[1] Put in a different way, California contributed almost 17%, or 300,000, of the 1.8 million jobs added in the United States between August 2011 and August 2012—more than the state's share of population or national GDP.

The recently released figures did include revisions to the last three years of employment data. These changes show that California's trough employment level back in February 2012 was 7,500 jobs lower than previously reported and the total employment base was reduced by roughly 20,000 over previous esti-

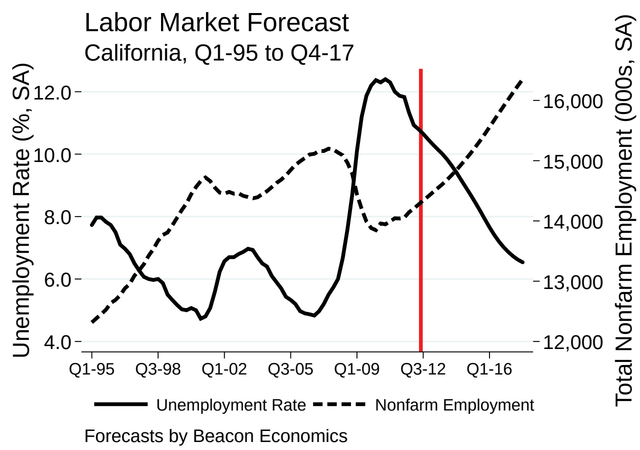
[1]James Nash and Darrell Preston, "California Defies Lower-Tax Texas in Creating More Jobs," Bloomberg News, August 28, 2012, `http://www.bloomberg.com/news/2012-08-29/california-defies-lower-tax-texas-in-creating-more-jobs.html`.

mates in May through July. Still, the trend is heading steadily upward. And just as critically, this improvement remains relatively broad-based. With the exceptions of the Farm, Manufacturing, and Government sectors, every sector in California has posted job growth over the past 12 months.

On a percentage basis, Construction employment has led the charge, adding 6.0% to its payrolls, with 33,000 new construction jobs since last August. Both residential and nonresidential permit activity are increasing across the state. Permit activity is nowhere near the pace of growth we saw before the housing bubble collapsed, but slow and steady growth is helping to generate new opportunities in the Construction sector. The existing home sales and rental sides of the market are helping to create jobs as well, with nearly 10,000 new Real Estate employees in the last 12 months.

Education and Health Care, a sector relatively unaffected by the Great Recession, has also continued to grow, contributing over 57,000 jobs to California's employment recovery over the past year. The Administrative Support and Professional industries, two areas that have led the employment recovery, are also up over last year, accounting for nearly one-third of all new jobs created this year despite a modest slip in August. Nationwide, business investment continues to be the preferred mechanism for meeting increasing demand, as businesses continue to put off expanding their number of permanent employees. The Administrative Support and Professional industries have benefited as a result, and the Professional sector is expected to remain an engine of growth.

Clearly the labor markets in California are on the mend and the worst of the downturn is behind us. Although the employment report for August was disappointing, it did show steady increases in California across many of the major regions in the state. The Bay Area has done well throughout the recovery, and it continued to improve in August. The Inland Empire, which was a bit slower out of the gate, actually added the most jobs of any region in California last month, increasing by 9,000 workers, with broad-based growth across most of its major sectors. With most major industries and regions across the state solidly in growth mode, Beacon Economics is forecasting that California's labor markets will continue to improve in the remainder of 2012 and beyond.



Specifically, Beacon Economics is forecasting that employment growth will average roughly 2% during the remainder of 2012. Growth is expected to remain in the 2% range for 2013, as the economy adjusts to rising tax rates associated with the upcoming fiscal hill before picking up steam and growing by between 2.5% and 3.0% per year in 2015 through 2017. At that rate, Beacon Economics forecasts that California will get back to its pre-recession employment peak of 15.2 million jobs by mid-2015. As employment steadily gains ground, the forecast calls for unemployment to slowly subside in the Golden State—falling to the single-digits by the end of 2013 and dipping below 8% by the end of 2015. California is making real progress, but it will take time for the state to return to "normal."

No Spending Slowdown

During the second quarter of 2012, consumer spending slowed and added only 1.2% to overall GDP growth—down from a 1.7% contribution to growth

California Employment by Industry

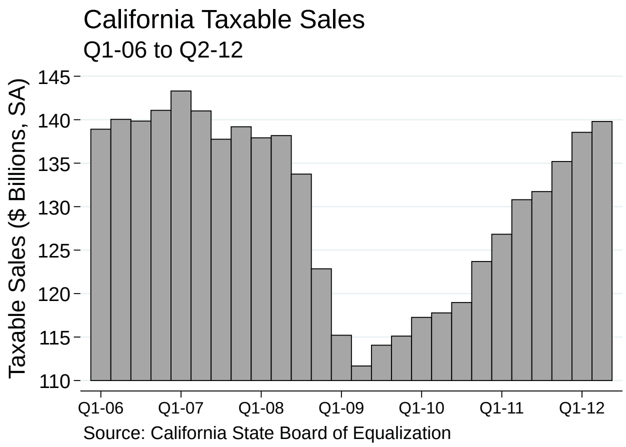
Industry	Aug-11 (000s)	Aug-12 (000s)	Change (000s)	Change (%)
Education/Health	1,839.7	1,897.2	57.5	3.1
Leisure/Hospitality	1,531.5	1,587.9	56.4	3.7
Admin Support	873.4	925.0	51.6	5.9
Professional	1,057.5	1,105.8	48.3	4.6
Construction	547.8	580.8	33.0	6.0
Retail Trade	1,532.2	1,553.6	21.4	1.4
Information	432.7	452.6	19.9	4.6
Wholesale Trade	663.9	676.3	12.4	1.9
Finance/Insurance	515.0	526.9	11.9	2.3
Real Estate	244.7	254.4	9.7	4.0
Management	199.2	202.6	3.4	1.7
Transport/Warehouse	470.8	473.6	2.8	0.6
Other Services	484.7	485.3	0.6	0.1
NR/Mining	28.6	28.9	0.3	1.0
Farm	387.4	382.8	−4.6	−1.2
Manufacturing	1,250.9	1,243.9	−7.0	−0.6
Government	2,374.9	2,351.5	−23.4	−1.0
Total Private	11,672.7	11,994.8	322.1	2.8
Total Nonfarm	14,047.6	14,346.3	298.7	2.1

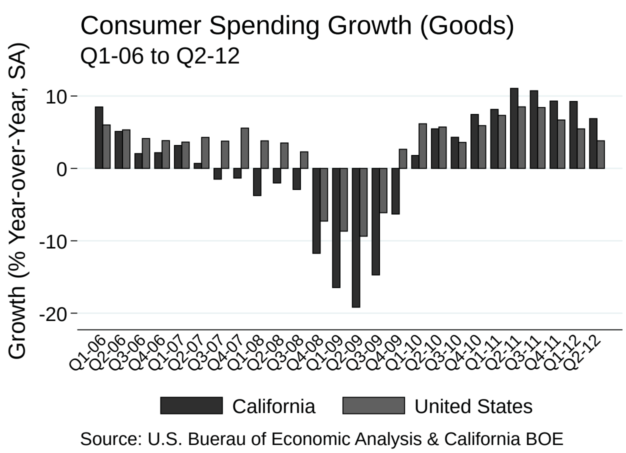
Source: California Employment Development Department

during the first quarter. In addition, retail sales actually declined in April, May, and June of this year—the first significant declines since mid-2010. These declines renewed concerns that the U.S. economy was tipping back into a recession. However, at the U.S. level, retail sales bounced back solidly in July and August, and in real terms, they have posted their third consecutive increase. In addition, auto sales have surged in recent months, posting their best performance in five years, for an annualized pace of more than 14.5 million vehicles.[2] There's no doubt that the road to recovery has made for a bumpy ride, but retail sales reports in July and August, along with auto sales figures in August, show that concerns concerns that a drop in consumer spending will push us into a double-dip recession are overblown at best and flat wrong at worst.

Perhaps more importantly, the spending slowdown that we observed nationwide during the summer was not nearly as acute here in California. According to data just released by the California State Board of Equalization, taxable sales in California posted their 12th consecutive quarterly increase. To date, taxable sales in California have rebounded by more than 25% since hitting bottom in the second quarter of 2009. Through the midpoint of 2012, taxable sales are just 2.4% below their pre-recession peak of $143 billion per quarter. And while retail sales stumbled nationwide between April and June, spending in California continued to rise.

[2] Bernie Woodall and Deepa Seetharaman, "Auto Sales Post Best August in Five Years," Reuters, September 4, 2012, http://www.reuters.com/article/2012/09/04/us-autos-sales-idUSBRE8830JF20120904.





The pace of growth in taxable sales did slow marginally, but certainly did not tip into negative territory. Specifically, taxable sales increased by roughly 1% in the second quarter of 2012 compared with the first quarter. This is slightly less than the 2% and 3% growth in taxable sales over the prior two quarters, respectively, but with a 6.9% increase on a year-over-year basis, it's clear that spending in the state has not ground to a halt. In fact, with respect to spending, California has consistently begun to outpace the U.S. economy overall. The second quarter of 2012 marked the eighth consecutive quarter that California's taxable sales growth has outpaced U.S. consumption of goods—a two-year streak. In other words, while some aspects of the economy, particularly the real estate and labor markets, have yet to fully recover in the Golden State, consumer spending is not an area that has been holding the state back over the past few years: it was one of the stronger aspects of the economy, helping to move us forward at a faster pace than seen in the U.S. overall.

Breaking this spending down by category reveals that California is not experiencing isolated pockets of improvement but rather broad-based growth. According to sales tax auditing firm HdL Companies, sales tax receipts across the state were up in every single spending category. In addition, the growth was evenly split between spending by consumers (up 7.5% on a year-over-year basis) and spending by businesses (up 7.1% year-over-year). On the consumer side, auto sales have contributed significantly to this growth, increasing by more than 17% over the second quarter of 2011.

The boost in auto sales is not surprising, given the surge in auto sales nationwide and the fact that growth in California has been outpacing the rest of the United States. Still, surprising or not, this represents a critical trend insofar as it provides much-needed sales tax revenues to state and local governments. It's also a bellwether, signaling that consumers are feeling optimistic enough about the economy to make these long-term durable goods purchases. Indeed, the California Department of Finance (DOF) reports that through April 2012, there have been almost 500,000 new car registrations filed with the DMV—an increase of more than 70,000 (16.7%) over April of last year. This same data show that for the 2011–12 fiscal year through April, there were roughly 1.1 million new car registrations, or 112,000 more than during the first 10 months of fiscal 2010–11. This provides solid evidence that the California consumer is feeling better about the prospects for the remainder of 2012 and beyond.

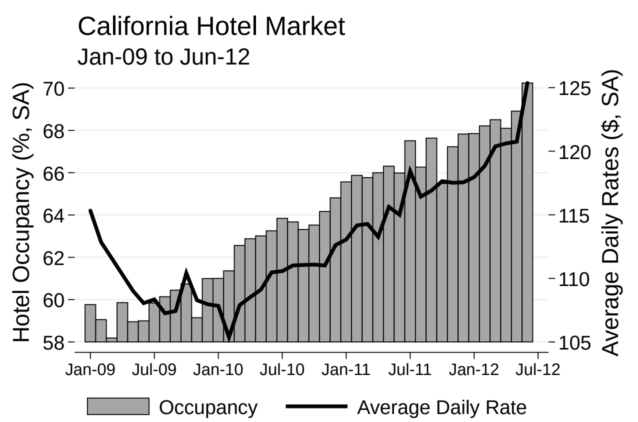
The rebound in spending in the state has not been limited to auto sales. There have also been solid performances in both local and tourist spending across California in 2012. For example, sales tax receipts at California's restaurants and hotels were up more than

California Sales Tax Receipts

Category	Q2-11 ($ Millions)	Q2-12 ($ Millions)	Change (%)
Consumers	1,094.0	1,176.5	7.5
Autos/Transportation	163.4	192.2	17.6
Restaurants/Hotels	151.2	164.2	8.6
Food/Drugs	75.5	79.8	5.7
Building/Construction	91.0	95.4	4.8
General Consumer Goods	296.6	308.4	4.0
Fuel/Service Stations	177.9	181.6	2.1
Business/Industry	192.2	205.8	7.1
Total	1,286.2	1,382.3	7.5

Source: HdL Companies

12% during the second quarter of 2012 over last year. California is known for its diverse geography, idyllic climate, and popular destinations—from Hollywood, to SeaWorld, to the Golden Gate Bridge. These assets, along with a relatively weak dollar (compared with historical norms) and a gradually recovering local economy, are helping to bolster the California tourism sector. The Automobile Club of Southern California projected record-breaking levels of tourism in Southern California on Labor Day for the second year in a row.[3] Though somewhat volatile, both hotel occupancy and hotel room rates are clearly trending upward, as they have been since early 2009. Not only is California benefiting from the industry's rising sales tax receipts, but tourism-oriented businesses are also benefiting as the increases in demand lead to rising revenues.

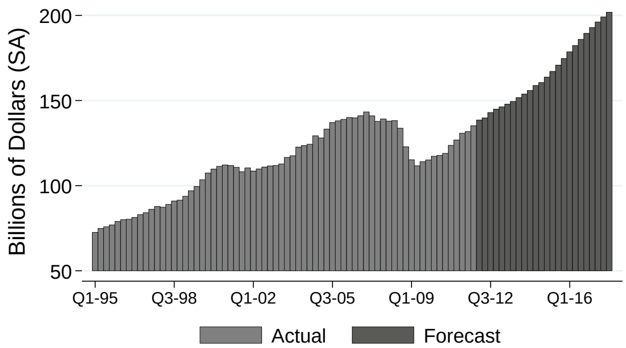


Source: VisitCalifornia

As noted, all other sectors continued to perform well through the halfway mark of 2012. Year-over-year increases ranged from as little as 2.1% at gas stations to 5.7% at grocery and drug stores. Even the construction sector, which has long been a source of pain, has seen spending on building materials increase over the past few quarters. Obviously, some sectors are faring better than others, but none of the state's major categories have seen sales tax receipts decline in 2012.

[3] Gregory J. Wilcox, "Record Labor Day Tourism Expected in Southern California," *Contra Costa Times,* August 29, 2012, `http://www.contracostatimes.com/california/ci_21430665/record-labor-day-tourism-expected-southern-california`.

Taxable Sales Forecast
California, Q1-95 to Q4-17



Forecasts by Beacon Economics

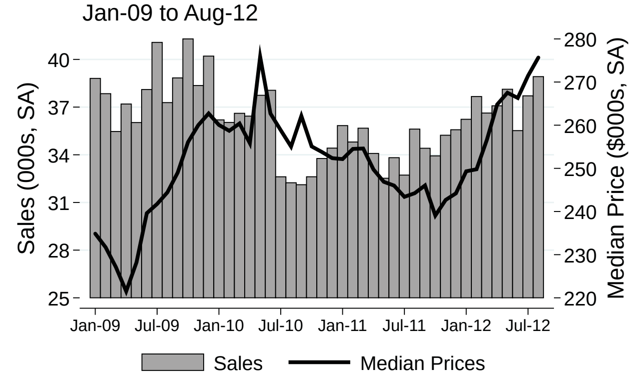
With the labor markets growing (albeit at a relatively tepid pace relative to the post-recession expansions of the 1970s and 1980s), and with the economy healing, taxable sales in California are poised for continued growth. California has already been outpacing the nation in this area for two years, and we expect the state to continue to do well as the unemployment rate falls and incomes rise. Specifically, Beacon Economics is forecasting that taxable sales will grow by an average of 7% over the next year, reaching its pre-recession peak by the end of 2012. As the economy gets back on its feet and taxable sales get back toward their long-run trend lines, we expect growth to settle out in the 5% to 7% range in nominal terms. This is slightly high relative to historical norms, but given that some demand will accumulate in 2013 and 2014 as households absorb the increase in taxes, and given that the state's population is increasing, California is likely to experience solid growth in spending from 2015 to 2017.

Real Estate Pitches In

Over the past few years, the real estate markets have been a drag on statewide economic growth. However, 2012 ushered in a new trend, where real estate has begun to add to the economy at large rather than detract from it.

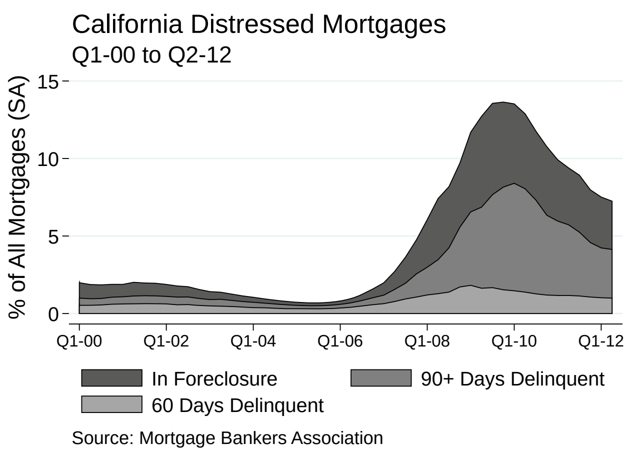
In fact, this trend began even before we entered the new year. According to real estate tracking firm DataQuick, California home sales posted their 14th consecutive year-over-year increase in August 2012, reaching their highest level since December 2009, when the first-time homebuyer tax credits were drawing a significant number of new buyers into the market. Although these tax credits have since expired, Californians are in more of a buying mode currently than they were at that time. As labor market conditions improve and incomes rise, many of our residents are looking to take advantage of record low mortgage rates and more reasonable prices; the cost of housing is now more in keeping with incomes again. In fact, the Federal Reserve is reporting that the average rate for a 30-year fixed-rate mortgage, —at 3.55% in July—was at its lowest level since the Fed began reporting on mortgage rates in 1971.

California Residential Real Estate
Jan-09 to Aug-12



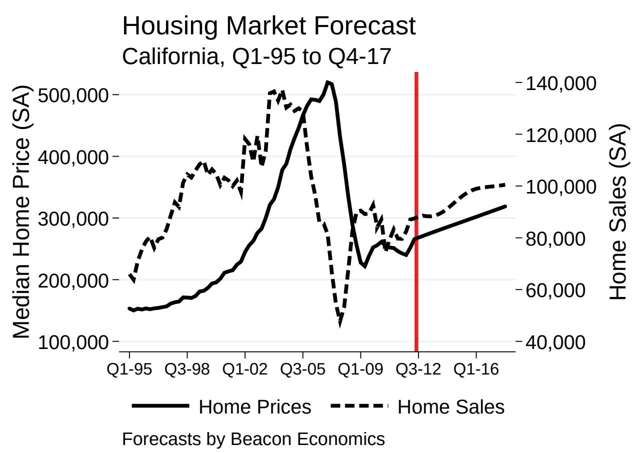
Source: DataQuick

The boost in demand for homes in California has also contributed to price appreciation in the state. Since hitting bottom in April of 2009, the median price of a home in California is up more than 24%, from a low of $221,500 to over $275,000 in August. Helping this trend is the fact that distressed mortgages in the state continue to dwindle and represent a smaller share of the overall sales mix. In fact, Radar Logic reports that over the summer distressed sales fell to their lowest share of home sales in over four years.[4] The Mortgage Bankers Association corroborates these statistics, showing that only 7% of California mortgages were seriously delinquent (60+ days past due) or in foreclosure by the second quarter of 2012. This is down from a peak of almost 14% and represents the lowest share of distressed properties in the state since early 2008.



The growth in home prices has not necessarily been distributed evenly across the state. Between the second quarter of 2011 and the second quarter of 2012, price growth for existing single-family homes ranged from as much as 7.9% in the South Bay to no growth in Modesto. The coastal areas in northern and southern California did well, but that growth also spread to the inland areas, including the East Bay, the Inland Empire, and the Stockton metropolitan statistical area (MSA), which all saw year-over-year increases in median home prices. Importantly, only a few smaller MSAs, including Hanford, Napa, and Yuba City, posted year-over-year declines in home prices.

Given that home prices are rising almost across the board in California and that interest rates remain at near record lows, Beacon Economics is forecasting continued improvement in the local housing market. Home sales, which have bounced back steadily over the last year, are expected to continue to climb—slowly at first, as we have already seen a solid bump, but picking up speed in 2014 and 2015. By 2017, home sales are expected to level off, with 90,000 to 100,000 transactions per quarter. Home prices are expected to continue to rise as well, though this time they will rise in line with incomes. This will mean slower growth than we experienced during the bubble, but the growth will be sustainable this time around. Specifically, Beacon Economics expects home prices to grow at roughly 7% in 2012 and at roughly 5% in 2013, before settling out in the mid-3% range in 2016 and 2017.



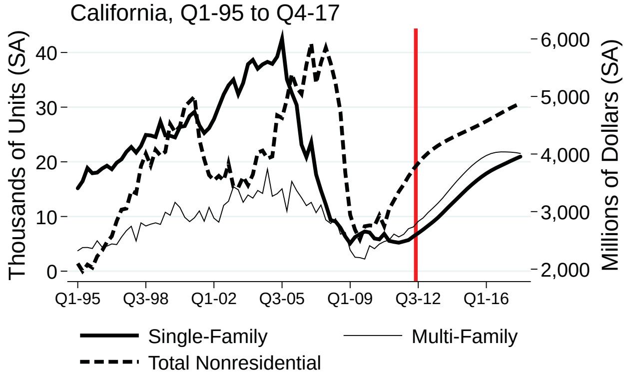
In terms of new construction, we've already begun to see an uptick in both residential and nonresidential permitting. Fortunately, unlike many other states, California still does not have enough housing. This fact is evident in the cost of housing. California has a much higher share of residents spending more than 35% of their incomes on housing relative to the national average. It is also evident when you look at housing vacancies in the state: despite all the construction that took place during the bubble, California still maintains one of the lowest housing vacancy rates in the nation, particularly on the rental housing side of the market. On the commercial side of the market, vacancy rates have begun to come down across the state for retail, office, and industrial properties, while rents have be-

[4] Tory Barringer, "Radar Logic: Share of June Distressed Sales Lowest Since 2008," DSNews.com, August 28, 2012, http://www.dsnews.com/articles/radar-logic-share-of-june-distressed-sales-lowest-since-2008-2012-08-28.

gun to inch upward. In addition, the bump in construction activity has increased construction employment in the state solidly over the past few months.

As a result, Beacon Economics expects both residential and nonresidential construction to continue to increase as the recovery progresses. The residential market is expected to experience a bit of a shift, with multi-family permits accounting for a larger share of overall residential housing moving forward. Nonresidential permitting, which has been concentrated in alterations of late, is expected to improve as well, with a larger portion of those permits moving toward new structures as firms begin to feel better about their opportunities for growth and expansion. Neither residential nor nonresidential permits are expected to get back to the heights reached during the bubble, but the upward trend will continue. We expect roughly 40,000 new residential units this year, with that number increasing to 85,000 units in 2013 before hitting 100,000 units in 2014.

Construction Market Forecast
California, Q1-95 to Q4-17



Forecasts by Beacon Economics

California just weathered one of the worst real estate storms in recent history, but there is a ray of light on the horizon. Home sales and prices have started to rebound, and permit activity is picking up. The commercial markets have begun to improve, and broader economic conditions point to a continued recovery in the state. As such, the forecast calls for more improvement in California's residential and commercial real estate market as we enter 2013 and beyond.

Exports Still Growing

The problems bubbling over in Europe of late have given rise to fears of a major contraction in U.S. exports. In California, export growth has slowed from the double-digit growth that we experienced in 2010 and 2011. However, exports have continued to increase in 2012, albeit at a more tepid pace. Through July, California's exports were roughly 5% higher than they were at the same point in 2011. While this is not a massive increase, it represents growth nonetheless.

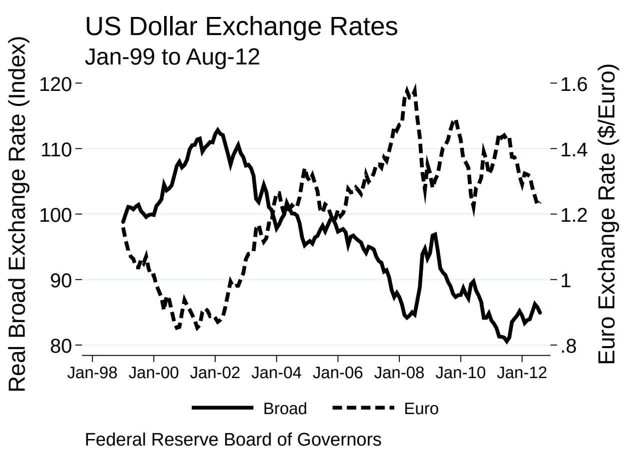
California Exports

Country	July 2012 YTD ($ Millions)	Change (%)
Mexico	16,376	17.57
Canada	9,907	2.14
China	8,182	0.46
Japan	7,728	1.13
Republic of Korea	5,228	4.13
Hong Kong	4,458	5.28
Taiwan	3,676	0.61
Germany	2,905	−7.12
Netherlands	2,620	−2.16
United Kingdom	2,528	6.05
Total	95,052	5.11

Source: Wiser Trade

Even though the headline numbers show slower growth so far this year, several areas continue to do rather well. Take agriculture as a prime example: exports of live animals, fruits and nuts, and dairy products have increased by 17.6%, 16.2%, and 13.1%, respectively. In addition, our manufactured goods have held their ground relatively well with aircraft/spacecraft exports up 11.5% this year while railway equipment has increased by nearly 13% to date in 2012. California vehicle exports are also on the rise, with more than $4.3 billion sent abroad so far this year, for a 9.8% increase over 2011. Thus, even though export growth has slowed, it continues to move forward. It is also important to keep in mind that export growth has slowed in part because we are catching up to our historical trend lines. Because exports took a big hit in 2009, part of the accelerated growth we experienced in 2010 and 2011 was a catch-up effect and was not expected to persist indefinitely.

It is also important to point out that although the euro zone continues to be in the midst of a financial ordeal, Europe is neither our only trading partner nor our largest—our largest trading partners are our North American neighbors in Canada and Mexico. Importantly, exports to Mexico in particular have held up well, posting 17.6% growth so far in 2012 compared with the same point in 2011. In addition, of our top 10 trading partners here in California, exports have only dipped negative with respect to two of them: Germany and the Netherlands. Even exports to the United Kingdom have gone up this year.



In addition, the market's initial reactions to the newly announced plan by the European Central Bank to buttress the continent's financial and banking system has been relatively well received. In fact, the dollar depreciated slightly against the euro in August, suggesting that investors are slightly less pessimistic about Europe's prospects than they were earlier in the year. Although the dollar has appreciated against a broad basket of currencies since late 2011, the value of the U.S. dollar is still fairly weak relative to historical standards. This suggests that U.S. goods are still relatively affordable on overseas markets, which should help to support demand from abroad.

Therefore, while Beacon Economics is not expecting export growth in California to take off, exports should continue to move along at a tepid but positive pace.

Summary

Overall, California has had a bumpy ride down the path to economic recovery, but it has made significant progress in that direction. Employment growth has been relatively consistent, with California jumping way ahead of the rest of the nation in May and June. July and August brought with them lackluster employment reports, but nothing to support fears of a double-dip recession in the state. Consumer spending, real estate, and exports all continue to move forward, and California has led the nation in some of these areas. We still have a long way to go before we can declare ourselves fully recovered, and the fiscal hill and upcoming presidential election will affect how the next few years play out, but the fundamentals of California's economy are improving and are expected to continue to do so in 2013 and beyond.

State Historical Table

California	Q1-2010	Q2-2010	Q3-2010	Q4-2010	Q1-2011	Q2-2011	Q3-2011	Q4-2011	Q1-2012	Q2-2012
Total Nonfarm Empl. (Mill, SA)	13.85	13.96	13.94	13.99	14.04	14.04	14.06	14.14	14.21	14.27
Growth (%,SAAR)	-1.02	3.23	-0.38	1.37	1.52	-0.11	0.42	2.55	1.73	1.88
Unemployment Rate (%,SA)	12.37	12.30	12.40	12.30	12.00	11.87	11.83	11.33	10.93	10.80
Personal Income ($ Bill)	1,554.94	1,579.21	1,591.69	1,623.77	1,658.40	1,667.72	1,683.53	1,683.94	1,707.41	1,721.47
Growth (%,SAAR)	8.66	6.39	3.20	8.31	8.81	2.27	3.85	0.10	5.69	3.34
Taxable Sales ($ Bill, SA)	117.26	117.78	118.97	123.69	126.82	130.80	131.73	135.19	138.55	139.79
Growth (%,SAAR)	7.70	1.77	4.10	16.83	10.54	13.14	2.88	10.92	10.32	3.64
Single-Family Home Prices ($ 000s, SA)	255.81	261.30	255.28	252.19	251.28	246.24	242.59	240.11	251.55	265.67
Growth (%,SAAR)	5.50	8.87	-8.91	-4.76	-1.44	-7.78	-5.80	-4.02	20.46	24.43
Single-Family Home Sales (000s, SA)	84.10	87.02	74.46	79.38	83.25	79.70	79.59	82.42	87.06	87.46
Growth (%,SAAR)	-31.94	14.59	-46.39	29.16	20.96	-15.99	-0.55	15.00	24.52	1.83
Single-Family Permits (000s, SA)	7.07	5.98	5.82	6.82	5.55	5.36	5.21	5.45	5.69	6.35
Growth (%,SAAR)	-9.88	-49.03	-10.17	88.95	-56.27	-13.13	-10.63	19.84	19.13	54.68
Multi-Family Permits (000s, SA)	4.65	4.11	4.95	5.42	5.68	6.78	6.27	6.74	7.77	8.10
Growth (%,SAAR)	1,841.87	-39.20	110.72	43.17	20.99	102.99	-26.99	33.39	77.18	18.02
Nonresidential Permits ($ Bill, SA)	2.76	2.75	2.93	2.75	3.04	3.19	3.35	3.47	3.61	3.74
Growth (%,SAAR)	2.29	-1.28	29.25	-23.12	50.28	21.53	20.56	15.68	17.48	14.33
Population (Mill)	37.26	37.32	37.38	37.45	37.51	37.58	37.65	37.72	37.80	37.89
Growth (%,SAAR)	0.66	0.67	0.68	0.69	0.70	0.71	0.75	0.79	0.84	0.89
Net Migration (000s)	-10.65	-9.03	-7.53	-6.16	-4.92	-3.80	-0.78	3.05	7.36	11.87
Natural Increase (000s)	71.59	71.17	70.86	70.64	70.53	70.52	70.67	71.08	71.47	71.92

State Forecast Table

California	Q3-2012	Q4-2012	Q1-2013	Q2-2013	Q3-2013	Q4-2013	Q1-2014	Q2-2014	Q3-2014	Q4-2014
Total Nonfarm Empl. (Mill, SA)	14.34	14.41	14.47	14.54	14.61	14.68	14.76	14.84	14.93	15.03
Growth (%,SAAR)	1.95	1.82	1.88	1.87	1.85	2.03	2.17	2.29	2.45	2.50
Unemployment Rate (%,SA)	10.65	10.48	10.32	10.16	10.01	9.84	9.64	9.42	9.18	8.94
Personal Income ($ Bill)	1,751.45	1,769.33	1,788.53	1,806.39	1,825.89	1,846.54	1,868.72	1,892.68	1,917.58	1,943.10
Growth (%,SAAR)	7.15	4.15	4.41	4.06	4.39	4.60	4.89	5.23	5.37	5.43
Taxable Sales ($ Bill, SA)	142.89	144.94	146.29	147.88	149.44	151.67	153.80	155.91	158.85	160.58
Growth (%,SAAR)	9.17	5.84	3.78	4.42	4.30	6.11	5.72	5.59	7.77	4.43
Single-Family Home Prices ($ 000s, SA)	268.22	270.73	273.22	275.68	278.11	280.52	282.92	285.31	287.69	290.06
Growth (%,SAAR)	3.88	3.80	3.73	3.65	3.58	3.52	3.46	3.42	3.38	3.34
Single-Family Home Sales (000s, SA)	88.14	88.55	88.32	88.29	88.61	89.20	90.09	91.26	92.61	94.01
Growth (%,SAAR)	3.15	1.86	-1.04	-0.12	1.45	2.68	4.08	5.26	6.07	6.21
Single-Family Permits (000s, SA)	6.96	7.61	8.30	9.00	9.76	10.63	11.54	12.41	13.28	14.16
Growth (%,SAAR)	44.44	42.79	41.56	38.37	38.16	40.72	38.92	34.05	30.85	29.19
Multi-Family Permits (000s, SA)	9.11	9.74	10.71	11.53	12.39	13.35	14.44	15.51	16.54	17.50
Growth (%,SAAR)	59.97	30.67	46.05	34.32	33.50	34.81	36.77	33.31	29.40	25.22
Nonresidential Permits ($ Bill, SA)	3.84	3.94	4.02	4.08	4.14	4.19	4.24	4.28	4.33	4.37
Growth (%,SAAR)	11.54	10.48	8.39	6.90	5.91	5.11	4.53	4.12	3.93	3.69
Population (Mill)	37.97	38.07	38.17	38.27	38.38	38.50	38.62	38.74	38.86	38.99
Growth (%,SAAR)	0.95	1.00	1.06	1.11	1.15	1.19	1.23	1.27	1.30	1.34
Net Migration (000s)	16.94	21.86	26.49	30.80	34.71	38.22	41.39	44.31	47.09	49.77
Natural Increase (000s)	72.50	72.97	73.54	74.27	75.04	75.83	76.67	77.54	78.43	79.32

Forecasts by Beacon Economics

San Luis Obispo Forecast

by Jordan G. Levine
Beacon Economics

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Key Chapter Findings

- Although the road to recovery has been a bumpy one locally, San Luis Obispo is seeing solid improvement in its labor markets with a 6.7% expansion in nonfarm payrolls since hitting bottom—faster than the Bay Area overall and Southern California and second only to San Jose—and the county maintained one of the lowest unemployment rates in the state at 7.5% in September 2012.
- Tourism remains a critical driver of growth for the region and San Luis Obispo's hotels are seeing increased occupancy and room rates, and Leisure and Hospitality has accounted for roughly one third of all the jobs created in the county over the past year. Increasingly, the region's tourism, agriculture, and retail sectors are becoming intertwined given the growth in the northern part of the county, and those sectors are also posting solid increases.
- The real estate markets are beginning to turn as well, and sales home prices are rising across the county from north to south, and from the beach to further inland. Defaults and foreclosures continue to dwindle as well, and new residential permitting has started to slowly increase with plans for several large-scale developments in the works.
- Beacon Economics forecasts that the San Luis Obispo County economy will continue to improve, with the region reaching its pre-recession peak of 105,000 by 2015. Leisure and Hospitality is forecasted to continue to be a driving force in the county, though real estate, business and consumer spending, agriculture, and even energy become stronger components in the overall growth mix for San Luis Obispo.

SLO: Not So Slow Anymore

The Central Coast in general and San Luis Obispo County in particular are poised for continued economic growth as we enter the new year. And, while San Luis Obispo County has traditionally lagged the broader economic trends we observe across the state, it has been one of the most solid growing economies in California since hitting bottom. In fact, San Luis Obispo was one of the first metros in the state to hit bottom in terms of nonfarm employment. Only the San Jose metropolitan area hit its employment trough as early as San Luis Obispo in July 2009—much sooner than Santa Barbara (Dec-09), Monterey County (Aug-11), and even the larger markets in San Diego, Orange County (MD), Los Angeles (MD), San Francisco (MD), or California, which all hit their trough during the first quarter of 2010.

Perhaps more importantly, San Luis Obispo is actually one of the fastest growing areas in the state as well. Since hitting its low point at just 94,000 jobs, San Luis Obispo has seen its nonfarm payrolls expand by 6,300 positions. Despite dipping briefly during the second half of 2011, current employment levels represent a 6.7% expansion in jobs over the past three years—second only to the booming San Jose area, and well ahead of the other driving regions in the state including San Francisco (MD), San Diego, Orange County (MD), Los Angeles (MD) and its Central Coast neighbors in Monterey and Santa Barbara. In addition, at 7.5% in September 2012, San Luis Obispo maintains the 4th lowest unemployment rate in the state, just behind San Francisco (MD), Orange County (MD), and Santa Barbara and well below the statewide average, which remains in the double-digits.

So, what's going on in San Luis Obispo that is driving this surge? Overall, California's economic recov-

Regional Labor Market Trends by Region, Peak to Current

Location	Peak Month	Peak (000s)	Trough Month	Trough (000s)	Peak to Trough (%)	Current (000s)	Trough to Current (%)
San Jose	Mar-08	921.1	Jul-09	839.5	−8.9	907.5	8.1
San Luis Obispo	Apr-07	105.1	Jul-09	94.0	−10.6	100.3	6.7
San Francisco (MD)	Apr-08	1,002.6	Feb-10	925.1	−7.7	983.0	6.3
Salinas	Oct-07	129.7	Aug-11	120.0	−7.5	126.1	5.1
Santa Barbara	Dec-07	174.5	Dec-09	160.8	−7.9	168.1	4.5
San Diego	Jul-07	1,314.5	Feb-10	1,211.2	−7.9	1,257.7	3.8
Orange County (MD)	Oct-06	1,526.5	Mar-10	1,342.8	−12.0	1,394.2	3.8
Los Angeles (MD)	Dec-07	4,136.6	Feb-10	3,756.7	−9.2	3,861.4	2.8
California	Jul-07	15,212.2	Feb-10	13,842.3	−9.0	14,347.9	3.7

Source: California Employment Development Department

ery has been fueled by three primary factors over the past three years: business spending, agriculture, and tourism. The latter two are strongly represented in the San Luis Obispo economy, and the Professional and Business Services sector has played a large part in the employment growth we've seen in the region to date. Let's consider each in turn.

Hands down, tourism in the region has been a huge driver of growth throughout the recovery. And, over the past 12 months, San Luis Obispo has seen some of the greatest increases in hotel occupancy rates in the state. In August, hotel occupancy hit 64.7%—a 3.1 percentage point increase over last year, trailing only San Jose and Los Angeles in terms of improvement. Room rates have seen slightly less improvement, though average daily rates are up by more than 3% so far this year: on par with Santa Barbara, and slightly better than in Monterey.

In addition to an idyllic climate and miles of pristine coastline, the region's agricultural sector has increasingly become tied in to the local tourism market as visitors come to San Luis Obispo County to visit the tasting rooms in North County and consequently inject the local economy with additional consumer spending at retail establishments, restaurants, and other entertainment options. In addition, given the weakness of the $US by historical standards, the region is benefitting not only from increased international tourism, but also by U.S. households' looking to substitute an expensive overseas vacation for one along California's Central Coast. The popularity of the region was highlighted in a recent survey by the American Automobile Association (AAA), which revealed that the Central Coast was the third most popular Labor Day destination for Californians this year—many of whom patronized San Luis Obispo County's hotels, bed and breakfasts, and other accommodations.[5]

This boost in local tourism is also creating a surge in consumer spending in the regional economy. This is true both of spending by businesses as well as spending by consumers, though the latter has been a more consistent trend. In fact, spending by consumers in San Luis Obispo is up more than 33% through the midpoint of 2012 compared to its low at the end of 2009, while business spending has increased by more than 140% compared with 2009. Again, the spending numbers show the impact of tourism on the local economy, with tax receipts at the county's restaurants up more than 10% so far this year.

Clearly, these are positive economic trends, which have begun to give way to a rising tide of employment. Through September, San Luis Obispo County

[5] Patti Pibum, "Central Coast Top Labor Day Travel Destination," *KCOY Central Coast News*, August 31, 2012, `http://www.kcoy.com/story/19429734/central-coast-top-labor-day-travel-destination`.

has added roughly 3,300 jobs since last September. Of those new jobs, nearly 1,100 were created in the Leisure and Hospitality sector and were concentrated in restaurants and hotels. That is the largest number of new jobs contributed from any sector in the region, which means that San Luis Obispo is well positioned to harness the growth in a sector that is driving the overall state economy forward.

Hotel Trends by Region

Location	Aug-11 YTD	Aug-12 YTD	Change (%)
	Average Daily Rates		
San Francisco (MD)	151.71	169.87	12.0
San Jose	111.63	122.86	10.1
Orange County	112.02	118.28	5.6
Los Angeles (MD)	122.83	129.14	5.1
San Diego	123.90	129.95	4.9
Napa	152.59	159.72	4.7
Santa Barbara	143.90	148.56	3.2
San Luis Obispo	111.25	114.82	3.2
Monterey	151.50	155.26	2.5
California	115.11	121.62	5.7
Location	Aug-11	Aug-12	Change (%)
	Occupancy Rate (%)		
Los Angeles (MD)	71.8	75.8	4.1
San Jose	69.9	73.2	3.4
San Luis Obispo	61.5	64.7	3.1
San Diego	67.7	70.3	2.6
Orange County	70.2	72.6	2.4
Napa	60.3	61.9	1.6
Monterey	60.9	61.5	0.6
Santa Barbara	65.1	65.7	0.6
San Francisco (MD)	78.0	77.9	−0.1
California	66.2	68.9	2.7

Source: VisitCalifornia

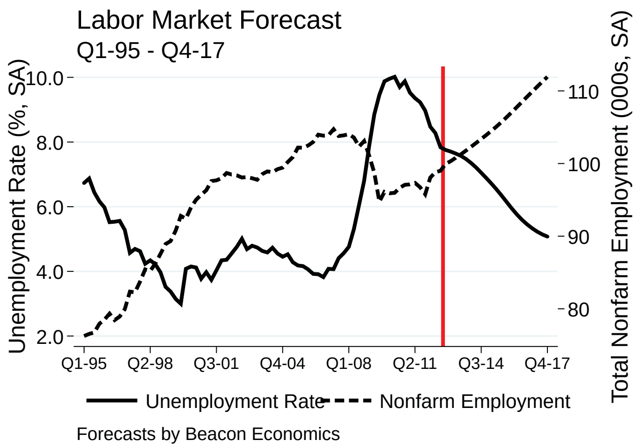
Fortunately, these gains have been broad based across the county, with each of the region's incorporated cities posting solid growth over the past year. Although the results have not been evenly spread, no area is experiencing continued declines. The coastal areas have fared particularly well, with sales tax receipts so far in 2012 up by more than 15% in Morro Bay and nearly 9% in Grover Beach. However, it isn't just the coastal areas that are doing well: Paso Robles has seen a 7.6% bump in sales taxes year-to-date in 2012 as well. The cities of San Luis Obispo and Pismo Beach have also seen an increase in spending of more than 6% this year, while Atascadero and Arroyo Grande have seen more modest growth in the 5% range. Thus, not only is spending by tourists and consumers up across the broader region, this improvement is relatively widespread across the north and south, coastal and inland areas of San Luis Obispo.

Sales Tax Receipts by City
San Luis Obispo County

Location	2011 YTD	2012 YTD	Change (%)
Morro Bay	61,775.2	71,277.5	15.4
Grover Beach	45,521.3	49,563.9	8.9
Paso Robles	332,442.8	357,595.8	7.6
Pismo Beach	102,181.7	109,269.8	6.9
San Luis Obispo	581,981.8	617,721.3	6.1
Atascadero	137,429.3	144,634.8	5.2
Arroyo Grande	132,748.8	139,380.6	5.0

Source: HdL Companies

Given that these indicators continue to point in a positive direction in the county, Beacon Economics is forecasting that San Luis Obispo's labor markets will continue to improve as well. The unemployment rate, which has already fallen to one of the lowest levels in the state, is expected to keep falling at a gradual rate. The unemployment rate is expected to dip below 7% by mid-2014, and reach 6% by 2016. Nonfarm employment will also continue to grow, adding roughly 2,800 jobs by the end of 2013 and reaching its pre-recession peak of 105,000 by 2015. Leisure and Hospitality is forecasted to continue to be a driving force in the county, though the Professional and Business Services sector is also expected to be at the leading edge of the recovery. Construction, which has already seen a 12% increase so far in 2012, will also continue its upswing—especially if several large-scale development projects break ground. A few sectors, including Government and Manufacturing have continued to face difficulty, but those losses are being more than offset by gains in the rest of the economy. It is not time to start celebrating, but the outlook is definitely improving.



Not Just Tourism

As strong as the tourism sector has been for San Luis Obispo, it's important to keep in mind that this is not the only source of strength for the region. Take spending as an example: although the region's restaurants and hotels have seen solid growth in sales tax receipts in the double-digit range this year, several categories of spending have grown by even more during 2012. Specifically, building and construction materials have seen almost 60% increases so far this year. In part, this owes to the two large solar projects in the region, for which construction is already underway. The development of both the Topaz Solar Farm (550 megawatts) and the California Valley Solar Ranch (250 megawatts) are already beginning to generate new construction jobs, which in turn will boost economic output in the region.[6] These projects are not trivial in size: Topaz Solar Farm will cover 5.5 square miles and California Valley Solar Ranch will cover about 2.5 square miles with solar panels.[7] To put this in perspective, the City of San Luis Obispo covers roughly 9 square miles.

Although these solar projects are large, they are not the only energy game in town. In fact, the oil fields located in Price Canyon in Northern San Luis Obispo County have experienced a mini renaissance of late as well. Not only are these projects and a gradually healing economy driving increases in building materials, they are also responsible for the surge in business spending that we've observed in the county over the past year. Business and industry sales tax receipts are up by 15% this year alone.

Sales Tax Receipts by Category
San Luis Obispo County

Location	2011 YTD	2012 YTD	Change (%)
Building/Construction	1,587,642	2,521,617	58.8
Business/Industry	2,823,963	3,246,168	15.0
Autos/Transportation	2,118,147	2,365,483	11.7
Restaurants/Hotels	2,369,933	2,621,377	10.6
Fuel/Service Stations	2,824,258	2,997,961	6.2
General Consumer Goods	4,166,067	4,364,807	4.8
Food/Drugs	1,284,622	1,323,627	3.0
Total	19,042,544	21,610,733	13.5

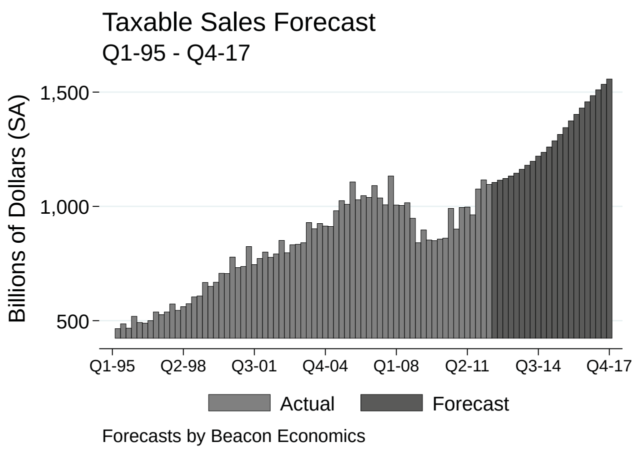
Source: HdL Companies

These projects are just getting going in San Luis Obispo and while the county is enjoying the big bump in activity currently it is likely that some of the one-off expenditures on items like construction will eventually wear off. Thus, it is important to zoom out to the broader picture, which shows many more underlying signs of strength. Auto sales underscore this point–with an 11.7% increase in sales tax receipts from autos this year, things are definitely looking up. This is a positive sign for several reasons. First, it provides some much needed revenues to local government budgets, which have been a source of consternation in the local economy for several years. However, it is also critical from an economics perspec-

[6] Zach Behrens and Leon Koenen, "Groups Sue Solar Company Over San Luis Obispo County Project," *KCET*, September 12, 2012.

[7] David Sneed, "Top 10 Stories of 2011: No. 7 —SLO County turns into a solar system," *San Luis Obispo Tribune*, December 25, 2011, `http://www.sanluisobispo.com/2011/12/25/1884166/top-ten-stories-of-2011-no-7-slo.html`.

tive. During the downturn, many long-term durable goods purchases like cars were deferred as uncertainty and overall economic conditions worsened. As the economy has started to heal, with jobs rising and unemployment falling, consumers in San Luis Obispo County are beginning to feel comfortable opening their wallets again. This increase in auto sales shows that local residents are indeed feeling more confident about the economic outlook and have started to ratchet up spending in turn.



And, like the regional breakdowns, sales tax receipts are up across each category of spending, be it gas, food and groceries, or general merchandise. Consumers certainly are not the problem in San Luis Obispo's Economy. Spending has been on the rise for the better part of three years, and both businesses and consumers are showing signs of increasing optimism.

On that basis, Beacon Economics is forecasting that consumer spending in San Luis Obispo County will continue to rise. This will be driven in part by rising employment and falling unemployment as well as rising incomes. By early 2013, Beacon Economics expects the region to return to its pre-recession peak of $1.1 billion per quarter, and will continue its upward trend at a rate of 5% thereafter.

Still Not Convinced—How About Housing and Construction

Unlike last year's report, Beacon Economics is happy to report that real estate is no longer a drag on the local or state economies in 2012. In fact, residential real estate in particular has started to become a source of growth for the San Luis Obispo economy over the past year. And, unlike during the bubble, this improvement in the housing market is being driven by solid fundamentals, rather than by a huge expansion in leverage and borrowing.

Recently released information on the single-family home market in San Luis Obispo County shows that home sales through the first three quarters of 2012 are up by more than 11% from the same point in 2011. In fact, the third quarter of 2012 marked the 7th consecutive quarter of year-over-year growth in home sales in San Luis Obispo County. Again, these gains have been slightly uneven, but with the exception of Paso Robles (where home sales have been relatively flat this year), existing home sales are up across the county: north, south, coastal, and inland—by as much as 26.7% in the City of San Luis Obispo.

Fortunately, this increase in transactions has already started to give rise to price appreciation in San Luis Obispo County. Given the surge in sales in the City of San Luis Obispo, it is not surprising to see that home prices there are up disproportionately relative to the rest of the county by nearly 20%. That compares to 10% growth in median prices in Paso Robles, 9.7% growth in Grover Beach, and almost 8% in Atascadero. Only Arroyo Grande has seen home prices rise by less than 5% this year. Clearly, the recovering labor markets, rising incomes, and historically low interest rates are enticing buyers back into the market again within the region.

Real Estate Trends by City

City	2011 YTD	2012 YTD	Change (%)
Home Sales			
San Luis Obispo	221	280	26.7
Arroyo Grande	220	253	15.0
Atascadero	236	256	8.7
Grover Beach	82	85	4.6
Paso Robles	462	458	-0.8
San Luis Obispo Co.	2,048	2,284	11.5
Location	Q3-11	Q3-12	Change (%)
Existing SFR Prices ($)			
San Luis Obispo	465,169	562,420	20.9
Paso Robles	284,431	313,239	10.1
Grover Beach	287,641	315,658	9.7
Atascadero	302,160	325,688	7.8
Arroyo Grande	441,667	451,647	2.3
San Luis Obispo Co.	349,746	384,635	10.0

Source: DataQuick

Furthermore, this is another area in which San Luis Obispo has started to jump out in front of the pack. At nearly $385,000, the median price of an existing single-family home is up by 10% ($35,000) over the third quarter of 2011. This is much faster than in Santa Barbara, where home prices this year are up a paltry 2%. San Luis Obispo also led the larger markets to the north and south during the third quarter, including the Inland Empire, San Francisco MD, San Diego, Orange County, and Los Angeles.

Not only are the trends moving in the right direction, but the fundamentals are back to levels that make sense again. During the bubble, the median price of a home grew to an unsustainable level relative to per capita incomes in the region. This was just as true across the state as it was in San Luis Obispo County. As painful as these steep declines in home values have been since that bubble burst, home prices have fallen back down to a level that are in-line with incomes. This fact, combined with a recovering economy and interest rates that have never been lower, should help to propel the housing market in San Luis Obispo County into 2013 and beyond.

Indeed, one glance at the number of distressed properties in San Luis Obispo shows that the worst is certainly behind us. In many ways, this is one of the most positive signs for the future of real estate in the county, as these properties tend to take a significant amount of time before they actually make their way back onto the market. Therefore, the fact that San Luis Obispo County has seen a nearly 29% reduction in new defaults so far in 2012 and more than 46% fewer foreclosures over 2011 is a sign that the region, much like the state as a whole, has clearly turned the corner. As the number of distressed sales dwindles relative to the overall sales mix, there will be less downward pressure on prices in coming years. Defaults and foreclosures do remain elevated relative to historical norms, but the third quarter of 2012 marks nearly three years of falling defaults and foreclosures.

Distressed Mortgages by City

City	2011 YTD	2012 YTD	Change (%)
Defaults			
San Luis Obispo	131	57	-56.9
Arroyo Grande	112	76	-32.6
Paso Robles	245	176	-28.1
Grover Beach	60	49	-17.8
Atascadero	162	144	-11.3
San Luis Obispo Co.	1,183	842	-28.8
Location	Q3-11	Q3-12	Change (%)
Foreclosures			
Atascadero	125	53	-57.6
Grover Beach	49	21	-57.1
Paso Robles	186	92	-50.5
Arroyo Grande	62	44	-29.7
San Luis Obispo	32	25	-21.9
San Luis Obispo Co.	767	414	-46.1

Source: DataQuick

This is not only true for the county as a whole, but is a trend that is being shared across the county's incorporated cities. The City of San Luis Obispo has led the charge, with defaults down nearly 56% this year—owing in part to solid increases in home prices. However, cities in the north and south have all seen fewer homes falling into distress. Defaults are down by more than 28% in both Arroyo Grande and in Paso Robles to the north, and even Atascadero, which has lagged other areas somewhat, has seen a decline in defaults of over 11%. The same is true of foreclosures, in which each incorporated city has seen at least 21% fewer foreclosures this year compared to 2011. Does the area still have a long way to go before it gets back to "normal"—yes. Is there ample evidence that San Luis Obispo weathered the worst of the storm and that better days lie ahead—absolutely.

These signs of life in residential real estate are beginning to give way to new construction in San Luis Obispo. As noted, construction employment was up by more than 12% in September 2012 compared with September 2011. Although single-family permitting is still down through June 2012, multi-family permits are up by double—with almost 20 new multi-family units permitted so far. Although this is relatively small as a share of the overall housing stock, it is a sign that new construction is on the rise.

Most of this new construction has been concentrated in 3 cities: San Luis Obispo, Pismo Beach, and Paso Robles. Other areas including Morro Bay, Arroyo Grande, Atascadero, and Grover Beach had seen relative little permitting activity through the first six months of the year.

Fortunately, there are several large developments in the works that could help to bolster the construction outlook even further. The Spanish Springs project calls for the construction of as many as 390 single-family homes, 83 apartments or condos, and 320 senior residential units in Price Canyon north of the Pismo Beach city limits.[8] The project would require the City of Pismo Beach to annex 1,264 acres of land, which would increase the square mileage of the city by approximately 50%.[9] The Pismo Beach City Planning Commission approved the project by a three-to-two vote in early October, and the city council is expected to consider the project in late November or early December.[10] If approved, Spanish Springs could bring an estimated 1,500 new residents to the city, as well as some much-needed construction jobs to the region.[11]

Construction is expected to begin by mid-2013 on 32 new residential units on Monterey Street downtown, as part of a much larger Chinatown redevelopment already underway in San Luis Obispo. The project was originally approved by the city in 2009, but stalled upon the onset of the economic recession.[12] Meanwhile, in Los Osos, construction of the long-delayed sewer project will proceed after much political debate, with an expected completion date of 2014[13] and a total budget of $173.4 million.[14]

These trends suggest that builders are beginning to seek new opportunities again. And with the residential market overall trending in a positive direction, Beacon Economics is forecasting that new residential construction will continue to improve in the coming

[8]Cynthia Lambert, "Price Canyon Plan Forwarded to Pismo Beach City Council," *San Luis Obispo Tribune,* October 9, 2012, http://www.sanluisobispo.com/2012/10/09/2257356/price-canyon-pismo-development.html.

[9]Tayler Duprel, "Price Canyon Gets a Green Light from Pismo Commission," *San Luis Obispo New Times,* October 10, 2012, http://www.newtimesslo.com/news/8448/price-canyon-gets-a-green-light-from-pismo-commission/.

[10]Cynthia Lambert, "Price Canyon Plan Forwarded to Pismo Beach City Council."

[11]Matt Fountain, "A Beach of a Race," *San Luis Obispo New Times,* October 18, 2012, http://www.newtimesslo.com/news/8502/a-beach-of-a-race/.

[12]AnnMarie Cornejo, "Chinatown Project Begins in Downtown San Luis Obispo," *San Luis Obispo Tribune,* September 24, 2012, http://www.sanluisobispo.com/2012/09/24/2240569/chinatown-project-begins-in-downtown.html.

[13]Michelle Hauser, "Project Overview," *Dig Los Osos: Los Osos Wastewater Collection System,* The County of San Luis Obispo, October 24, 2012.

[14]David Sneed, "Attempt to Halt Construction of Los Osos Sewer Fails," *San Luis Obispo Tribune,* July 15, 2012, http://www.sanluisobispo.com/2012/06/15/2107854/attempt-to-halt-construction-of.html.

Nonresidential Construction Trends, San Luis Obispo Co.

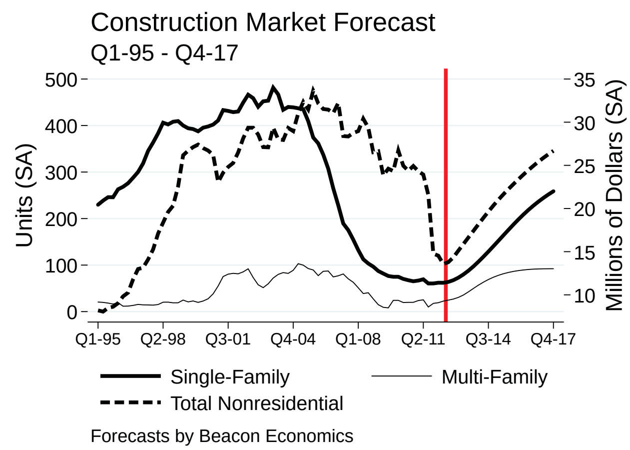
Permit Type	2010	2011	2011 YTD	2012	Change (%)
New Commercial	29,419	6,818	700	3,673	424.8
Office	0	0	0	2,723	N/A
Retail	17,305	6,818	700	950	35.7
Hotel	7,001	0	0	0	N/A
Industrial	15,893	822	822	5,758	600.5
Other Nonres.	25,892	18,028	8,303	7,306	−12.0
Nonres. Alts./Adds.	48,126	41,615	24,205	15,920	−34.2
Total Nonres.	119,330	67,283	34,030	32,657	−4.0

Source: California Homebuilding Foundation

years. Roughly 500 new residential permits are forecasted for 2013 and activity should continue to increase—reaching 1,300 units per year by 2017.

In addition, the nonresidential side of the construction market is beginning to show signs of life as well. Although total nonresidential permitting in San Luis Obispo County is down roughly 4% so far in 2012, there are some positive signs below the surface. Firstly, the entire decline in nonresidential permit values this year is attributable to fewer nonresidential alterations permits. During the downturn and initial stages of the recovery, businesses were deciding to stay put and renovate or improve their existing facilities rather than breaking ground on new space and alterations/additions grew to a large share of total nonresidential construction. As the economy is improving, we are seeing nonresidential construction shifting towards new structures, which is ultimately a positive sign despite the relatively lackluster headline number.

In fact, through June 2012 new commercial permit values in San Luis Obispo County are up by more than 400%—to nearly $3.4 million so far this year. This has been driven by a surge in new office space, which saw no new permitting through the first six months of 2011. However, new industrial permits are up solidly as well. Even retail space, which is being driving by rising spending by businesses and consumers in San Luis Obispo, are up by nearly 36% so far in 2012.



Thus, while the overall value of nonresidential permits is down slightly relative to last year, there is a shift underway against alterations and additions to existing space towards the construction of new nonresidential structures. Therefore, don't be fooled by the headlines—scratch the surface and factors are improving locally.

Time to Pop Champagne?

Given all this good news, does that mean that it is time to pop the champagne corks and kick off the celebration? Not quite. There's no doubt that the economy in San Luis Obispo is moving in the right direction. Tourism, agriculture, and professional services are all driving the local economy forward and we have seen that translated into rising consumer and business spending, an improving local real estate market, and the initial stages of a residential and commercial permit uptick. However, employment remains below its pre-recession peak and unemployment, though lower than most other parts of the state, are still above historical norms. And, while the residential markets are improving, defaults and foreclosures remain high—though they are trending downward.

There are also external risks to be concerned about—though these are better characterized as causes for concern rather than panic. Europe's economic woes continue to drag on the U.S. and California economies. Given that many of San Luis Obispo's agricultural products are exported to world markets, this has the potential to slow growth in local businesses. However, the European Central bank has agreed to backstop the troubled banks, Moody's recently announced that they would not downgrade Spanish bonds, and the $US has since depreciated against the Euro.

There is also the fiscal cliff—or rather the fiscal hill—to be concerned with as well. Rising tax rates, particularly on the middle-class, could stifle the growth in consumer spending that the Central Coast has enjoyed over the past three years. However, given how politically unpalatable allowing the government to go over the edge, Beacon Economics believes that a compromise will ultimately be reached, saving San Luis Obispo from any major negative effects.

Thus, while it is not time to celebrate, it is a time to look forward to the future of San Luis Obispo's economy.

Employment

by Eric Meux

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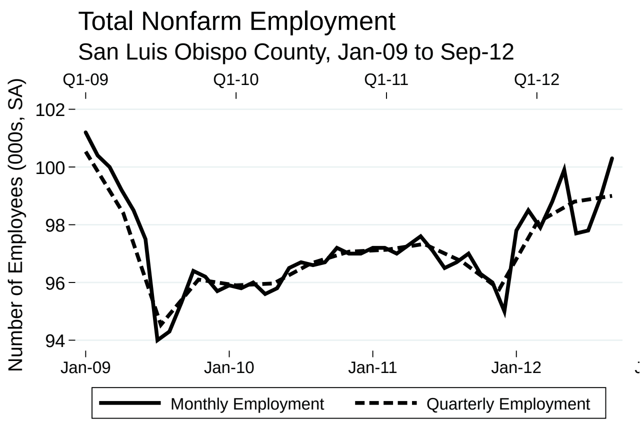
Key Chapter Findings

- San Luis Obispo County's employment recovery continues moving forward in 2012, outpacing nonfarm growth in the state overall and in most other metropolitan areas in California.
- Despite wide month-to-month volatility, the uptrend in employment gains over the last three quarters is clear: the local labor market is growing again at a healthier pace.
- The unemployment rate in the county has dropped to 7.5% over the last year, the third-lowest in the state. Many local residents who were unemployed are now employed, and the labor force is expanding, confirming the upward trends we are seeing in industry employment.
- The Leisure and Hospitality sector, one of the bellwether industries for the county, has been the clear driver of employment gains over the last year, making up one-third of all nonfarm industry job growth.
- The U.S. Department of Energy estimates the Central Coast region is home to 15.5 billion barrels of oil locked in shale deposits. This presents a very promising growth opportunity for the region in the years to come and should boost Natural Resource and Mining employment.
- Average annual wages across all industries increased by 2.0% from 2010 to 2011, but lagged behind average wage growth for the state overall. Leisure and Hospitality wage growth in particular outpaced overall wage growth in the county, with a 3.1% year-over-year increase.

Industry Employment

The latest jobs report from the California Employment Development Department (EDD) held some pretty good news for the County of San Luis Obispo, to say the least. September total nonfarm employment stood 3,300 payroll positions higher than a year before, a 3.4% increase on a seasonally adjusted basis and the second fastest year-over-year increase in the state, behind Santa Rosa MSA (3.9%). Total private employment showed even stronger year-over-year gains, at 3,700 positions, or 4.8%. What was even more impressive in the latest jobs report was that almost half of the year-over-year employment gains came in this September. Indeed, according to the EDD, San Luis Obispo saw 1,400 nonfarm jobs added to local payrolls from August to September, a 1.4% increase and the second highest month-over-month growth among California metropolitan areas. Of course, sudden increases in such a short time frame should always be taken with a grain of salt, as they are usually revised in the following months. The latest month's gains were driven mostly by an increase in government employment, which has seen a large degree of volatility historically. So while the 1,400 increase from August to September may not be the best estimate of month-over-month job gains for San Luis Obispo County, the 3,300 year-over-year gain gives a better idea of the employment facts on the ground and indicates where the county's employment data are heading.

We can take out much of the month-to-month volatility by looking at total nonfarm employment on a quarterly basis, which shows us that the employment recovery in San Luis Obispo County is moving forward at a healthy pace, given today's challenging economic environment. From the third quarter of 2011 to the third quarter of 2012, our quarterly average of the monthly employment figures shows a 2,300 job gain. While this certainly is not as bright a picture as the monthly figures suggest, the year-over-year growth of 2.3% outpaces national job growth (1.4%) as well as state annual growth (1.9%). San Luis Obispo County may have had a slower start to the employment recovery after the recession, but the last three quarters of employment data have clearly shown that the county labor market is growing again.



Source: California Employment Devlopment Department

The employment gains over the last year have been fairly broad-based, aside from weakness in the Manufacturing and Government sectors, with key industries reporting the largest year-over-year gains. The top four industries by employment level all posted strong annual gains.

San Luis Obispo County Employment (000s and % Change, SA)

Industry	Sep-12 (000s)	Aug-12 to Sep-12	Sep-11 to Sep-12
Total Nonfarm	100.3	1.4%	3.4%
Total Private	79.5	0.4%	4.8%
NR/Construction	5.8	-0.9%	12.1%
Manufacturing	5.4	-1.5%	-6.2%
Trade,Transport,Util.	20.3	0.8%	4.6%
Information	1.2	0.2%	0.4%
Financial Activities	4.2	2.0%	8.2%
Professional/Business	11.1	0.1%	7.4%
Education/Health	12.1	0.5%	7.6%
Leisure and Hospitality	15.6	1.4%	7.3%
Other Services	3.9	-2.5%	-11.6%
Government	20.8	5.5%	-1.7%

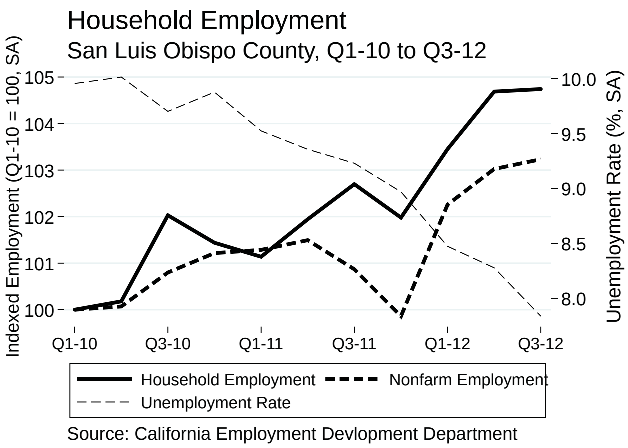
Source: CA Employment Development Department

Leisure and Hospitality employment, a key sector for local growth, led with an increase of 1,100 jobs. Trade, Transport, and Utilities; the Professional and Business sector; and Education and Health services saw employment levels rise by roughly 800 positions each. The fastest-growing sector on an annual basis was Natural Resources, Mining, and Construction. Due to confidentiality requirements for employment sectors with a small number of employees, we cannot say for sure how much of the past year's employment increases have been from mining activities, but some of the growth in this combined sector could be tied to the development of local energy resources in the Monterey Shale formation.

Household Employment

Over the past year, San Luis Obispo County has enjoyed one of the lowest unemployment rates in the state. At 7.5% as of September 2012, only Orange County (7.1%) and Santa Barbara County (7.4%) had lower unemployment rates, and Napa County tied San Luis Obispo County for third place. As the unemployment rate in San Luis Obispo has come down, we have also seen increases in household employment and in the labor force. (Household employment is employment tracked by residency. The payroll survey measures employment by industry.) From September 2011 to September 2012, household employment increased by 3,700 positions, and the labor force grew by 1,500 employees. This year-over-year household employment growth shows that not only are more people entering the labor force and finding gainful employment, but many who were out of work but still searching were successful in finding jobs.

Since the downturn, we have seen household employment grow faster than nonfarm employment, a strong sign of a labor market in recovery. Because the household survey estimates how many of the county's residents are employed, as opposed to what industry in the county they are employed in, it also picks up *informal* employment. Those who are self-employed and those paid with cash are not counted in the payroll survey, making nonfarm employment an incomplete measure of what is happening in the local labor market.

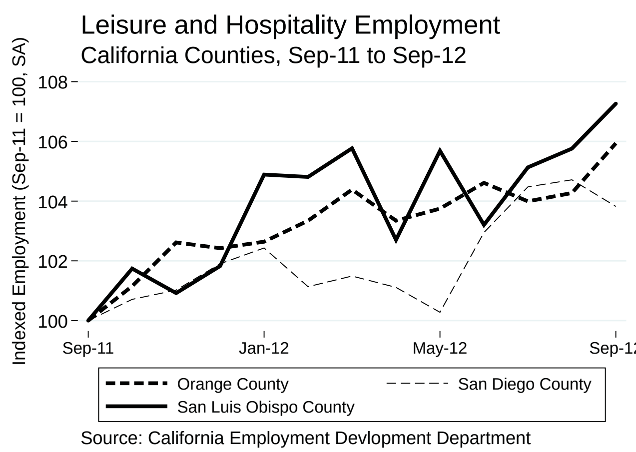


Since the beginning of 2010, the first year of positive job growth after the downturn, to September 2012, household employment has added back 5,900 jobs, for a 4.7% increase. During the same time period, nonfarm employment increased by 3,000 jobs, a 3.2% increase. This faster job growth in the household survey is indicative of the fact that the informal economy, as well as local industries in San Luis Obispo County, is moving forward at a good pace, in spite of the reports we keep hearing in the national media regarding the supposedly "jobless recovery."

Leisure and Hospitality Leads the Local Employment Recovery

It's no secret that tourism is big in San Luis Obispo County; indeed, it is one of the bedrocks of the county's overall economy. When the housing bubble collapsed and California households reined in spending, regional economies dependent on tourism dollars saw a period of stagnation at the outset of the Great Recession. Now that the consumer spending recovery in the Golden State has picked up steam, areas like San Luis Obispo have been benefiting from healthier household balance sheets— people are getting out more and enjoying everything California has to offer.

The gains in employment in Leisure and Hospitality that we have seen in San Luis Obispo County over the last year highlight how the recovery in consumer spending has greatly benefited the local labor market recovery. From September 2011 to September 2012, the Leisure and Hospitality sector added 1,100 jobs on a seasonally adjusted basis, a 7.3% increase and one-third of nonfarm job growth during the same year-over-year time period.



The bulk of these gains came from the Accommodations and Food industry, which makes up roughly 91% of Leisure and Hospitality employment in the county. The job growth in the Leisure and Hospitality sector in San Luis Obispo County has outpaced gains in other large metropolitan areas with heavy tourism industries. Orange County saw a 5.9% increase from September 2011 to September 2012, and Leisure and Hospitality employment in San Diego County grew 3.8% over the same period. As the overall economic recovery continues and consumer spending returns to pre-recession levels, San Luis Obispo County is well positioned to benefit from those gains.

Central Coast Employment (000s, SA)

Location/Industry	Sep-12 (000s)	Aug-12 to Sep-12	Sep-11 to Sep-12
San Luis Obispo NR/Construction	5.8	-0.9%	12.1%
Santa Barbara NR/Mining	1.2	-0.6%	8.8%
Santa Barbara Construction	6.9	-0.1%	2.5%
Monterey NR/Mining	0.2	0.0%	0.0%
Monterey Construction	3.9	0.7%	-0.03%

Source: CA Employment Development Department

There's Oil in Those Hills!

While many geologists and local residents have known for some time about the oil in shale deposits along the Central Coast, the rest of the country got a wake-up call in July as to just how much oil was there for extraction. Estimates released in July by the U.S. Department of Energy claimed that the Monterey Shale formation, a mineral formation which runs along most of central and coastal California, holds 15.5 billion barrels of oil and accounts for 64% of total shale oil reserves in the United States. Needless to say, the future economies of Central Coast communities will greatly benefit from increased extraction in the area. Some states that barely noticed the Great Recession, North Dakota for example, can attribute their current low unemployment rates to the booming shale oil production in the area.

Shale oil extraction, however, does not come without its costs—in this case, environmental costs. Energy companies use a technique called hydraulic fracturing that employs a chemical cocktail to release the oil from the shale deposits. Environmentalists around the country have voiced concerns regarding the fracturing technique, citing the possible contamination of underground water tables. Both the federal government and the California state government have yet to establish comprehensive regulations with regard to the hydraulic fracturing process, and in the years to come this subject is sure to become a hot-button issue in local and state politics given the enormity of the shale oil resources in the Central Coast region.

San Luis Obispo County currently has a very small Natural Resources and Mining labor force, so small that it is aggregated with Construction-sector employment by the EDD to preserve the confidentiality of specific employers in the county. So while we are not able to discern how Natural Resources and Mining employment in the county is trending, we do know that the combined NR/Construction sector has been posting the highest year-over-year growth of all industries in the county. Neighboring Santa Barbara County does have NR/Mining employment data available for the public, which also shows strong year-over-year job gains. NR/Mining in Monterey County, on the other hand, has been flat for years, at 200 employees; however, this lack of movement is most likely a result of data suppression by the EDD for confidentiality reasons rather than a reflection of a stagnant local industry.

Wages

According to the U.S. Bureau of Labor Statistics, the average annual wage in San Luis Obispo County across all industries grew by 2.0% from 2010 to 2011. The rate of average annual wage growth outpaced that of neighboring Monterey County, but fell behind wage growth in Santa Barbara County, as well as behind wage growth in the state overall and major metropoli-

Regional Wages by Industry, 2010 to 2011

Location	Total All Industries		Leisure/Hospitality		Professional/Business	
	Wage	Change (%)	Wage	Change (%)	Wage	Change (%)
San Luis Obispo	36,849	2.0%	17,470	3.1%	40,134	−2.4%
Santa Barbara	43,424	2.3%	20,403	3.0%	59,571	−5.7%
Monterey	36,559	1.2%	24,165	1.0%	52,234	−0.2%
Los Angeles	53,364	2.6%	33,964	3.7%	66,131	2.9%
San Francisco	80,984	6.1%	32,431	4.5%	112,434	8.6%
California	54,345	3.4%	24,616	2.7%	71,199	4.5%

Source: CA Employment Development Department

tan areas in Northern and Southern California. The average annual wage across all industries stood at $34,849 in 2011, slightly higher than the average wage in Monterey County but substantially lower than the state average of $54,345.

The tourism industry has played a large role in driving employment growth in the region, but, unfortunately, the strength of the tourism industry is also the reason for lower overall wages for local residents. Leisure and Hospitality employment in San Luis Obispo County accounts for over 15% of nonfarm jobs, but it is also one of the lower-paying industries, with an average annual wage of $17,470. This high proportion of low-paying jobs is one of the main reasons the average annual wage across all industries is lower in San Luis Obispo County than in the state and in other major metropolitan areas in Northern and Southern California. Wages for Leisure and Hospitality employment are lower than the levels in other Central Coast regions and the state overall.

Professional and Business Services, another large driver of labor market growth over the past year, saw average annual wages in San Luis Obispo County decline from 2010 to 2011, which also contributed to slower wage growth across all industries. San Luis Obispo was not alone in this trend, however. Santa Barbara and Monterey Counties both saw year-over-year declines in Professional and Business Services wages.

BEACON ECONOMICS

Business Activity

by Dustin Schrader

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Key Chapter Findings

- Consumer spending continues to grow, with seasonally adjusted taxable sales up 9.9% year over year.
- Rising hotel occupancy and revenues show that the tourism sector is rebounding.
- 2012 proves a great year for San Luis Obispo County wine, as near-perfect weather yields a great wine grape crop.

Consumer Spending Is Growing Quickly, but B2B Spending Makes the Biggest Gains

The outlook for consumer spending in San Luis Obispo County is very promising. Year-over-year taxable sales growth in the county has soundly bested that of neighboring regions and the state overall. At $1.1 billion in the second quarter of 2012, seasonally adjusted taxable sales in San Luis Obispo County have risen by 9.9% year over year, compared to 5.3% in Monterey County, 6.1% in Santa Barbara County, 4.6% in Ventura County, and 6.9% across the state.

Taxable Sales by City
San Luis Obispo County, Q2-10 to Q2-12

City	Q2-10 ($000s)	Q2-11 ($000s)	Q2-12 ($000s)	2-Yr Chg (%)	1-Yr Chg (%)
San Luis Obispo	266,616	294,577	303,622	13.9	3.1
Paso Robles	148,935	169,336	181,693	22.0	7.3
Atascadero	62,636	70,961	71,273	13.8	0.4
Arroyo Grande	63,680	66,183	67,213	5.5	1.6
Pismo Beach	46,027	53,452	55,395	20.4	3.6
Morro Bay	29,532	30,829	36,313	23.0	17.8
Grover Beach	21,230	23,283	25,066	18.1	7.7

Source: CA Board of Equalization

Bearing in mind that statistics are more volatile at the local level, we can see that consumer spending among incorporated cities in San Luis Obispo County is growing across the board. Seasonally adjusted taxable sales in the City of San Luis Obispo increased by 3.1% year over year, and by 7.3% year over year in Paso Robles. Year-over-year growth was slowest in Atascadero, but nonetheless positive, at 0.4%. Taxable sales growth from the second quarter of 2011 to the second quarter of 2012 shows a substantial recovery: up 22.0% in Paso Robles, 13.9% in San Luis Obispo, and 13.8% in Atascadero.

Business taxable receipts are up a phenomenal 53% from the second quarter of 2011 to the second quarter of 2012.

Fast-rising aggregate consumer spending is a great sign for economic growth in the region. Moreover, at the sector level, business-to-business spending has been very strong as well. Business taxable receipts are up a phenomenal 53% from the second quarter of 2011 to the second quarter of 2012, compared to 7.1% in the state overall. Growth has also been strong in Restaurants and Hotels, with taxable receipts up 9.1% over the same time period compared with 8.6% in the state. This is especially good news for a tourism-heavy region like San Luis Obispo. Mimicking a statewide trend, Autos and Transportation spending in the San Luis Obispo MSA is up substantially: 11.4% year over year, though growth has been slower than in the state overall (17.6%).

Ultimately, with spending up in every sector—especially in key sectors such as Business and Restaurants and Hotels—the San Luis Obispo economy appears headed for a strong year to come. With these levels of growth in spending, we should see businesses begin to increase investment in jobs and construction. Indeed, the recent uptick in San

Luis Obispo County total nonfarm employment shows that this process is already underway.

Bank Deposits Are Increasing, but Banks Show Difficulty Building Assets

Capital is up among commercial banks in San Luis Obispo County. Total bank deposits for the 2012 fiscal year increased in most of the top banks in the county, and by substantial margins in some: total deposits at Wells Fargo grew by 15.4% from the 2011 fiscal year and by 9.5% at JPMorgan Chase. Total deposits were down steeply (14.4%) in the third-largest bank by deposit volume in San Luis Obispo County, Bank of America Corp., but they were up by 4.7% in the largest bank by deposit volume in the county, Rabobank Nederland, and up by 5.2% at locally-based Heritage Oaks Bank.

Total Bank Deposits
San Luis Obispo County Commercial Banks

Bank	County Mkt Share (%)	2011 Total Deposits ($ Millions)	2012 Total Deposits ($ Millions)	1-Year Change (%)
Rabobank Nederland	25.7	1,271.5	1,331.4	4.7
Wells Fargo & Co.	13.5	607.0	700.4	15.4
Bank of America Corp.	11.8	712.5	610.3	-14.4
JPMorgan Chase & Co.	11.0	519.9	569.2	9.5
Heritage Oaks Bancorp	10.0	493.7	519.5	5.2
Carpenter Bank Partners Inc.	6.9	381.1	358.9	-5.8
PacWest Bancorp	5.3	269.4	276.0	2.4
Pacific Capital Bancorp	2.9	140.0	150.2	7.3
U.S. Bancorp	2.6	125.7	134.2	6.7
Coast Bancorp	2.5	124.1	126.8	2.2
All SLO Cnty Comm. Banks	100.0	5,053.2	5,180.7	2.5

Source: SNL Financial

Among all commercial banks in the county, total deposits increased from approximately $5.05 billion to approximately $5.18 billion, or 2.5%. With all of this new capital, banks in the county are searching for—but having difficulty finding—assets to invest in.

Total commercial lending in the county remains at its lowest level since the first quarter of 2008. Loans and leases for commercial and industrial institutions continue to fall, having decreased by approximately 19.1% from the first quarter of 2011 to the first quarter of 2012 alone, or approximately $47.9 million in nominal terms. Indeed, commercial and industrial lending has not rebounded since turning south at the onset of the economic recession. By comparison, total commercial lending in the state overall is at its highest level since early 2009, while lending to commercial and industrial institutions is up 22.1% since reaching bottom in the second quarter of 2010.

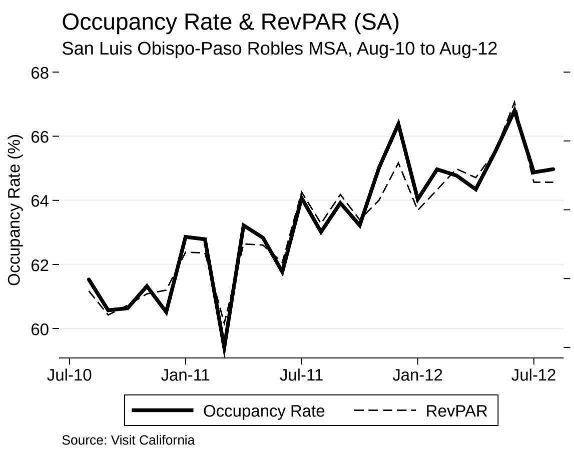
Loans and leases for commercial and industrial institutions continue to fall.

On the other hand, following the general path of the state overall, real estate lending remains well above recessionary lows in San Luis Obispo County. Both residential and commercial real estate loans and leases grew substantially in the run-up to the housing bubble, but simply leveled off with the onset of the recession. Residential real estate loan and lease values decreased by only 3.3% from the first quarter of 2011 to the first quarter of 2012, while commercial real estate loan and lease values decreased by only 1.9% over the same period. These figures are comparable to those in the state, where residential real estate loan and lease values increased by 4.6% from the first quarter of 2011 to the first quarter of 2012, while commercial real estate loan and lease values increased by 1.9% over the same period.

In all, though banks in the county have more capital to invest in assets, interest rates remain at their lowest levels in decades, and consumer spending and business spending continue to increase, it appears that these banks will continue to have difficulty turning that new capital into new loans.

With Consumer Spending Rising, the SLO Tourism Sector Reaps Big Benefits

As shown in the analysis of San Luis Obispo County consumer spending above, the Restaurants and Hotels sector has seen a substantial increase in overall spending in the past year. In addition to the growth in consumer spending, occupancy rates and revenues for hotels in the region indicate that tourism is rebounding strongly. On a seasonally adjusted basis, the occupancy rate for hotels in the San Luis Obispo metro area increased from June-August 2011 by 2.5 percentage points to approximately 65.5% from June-August 2012. At the same time, the revenue per available hotel room (RevPAR) increased by approximately 6.1%, to $88.94.



These numbers stack up very favorably against the figures posted in neighboring Santa Barbara and Monterey counties. The occupancy rate for hotels in the Monterey MSA increased by approximately 2.3 percentage points, to 62.6%, during that same time period, while RevPAR increased by approximately 1.7%, to $97.98. Meanwhile, in the Santa Barbara MSA, the occupancy rate for hotels increased by approximately 1.2 percentage points, to 66.7%, while RevPAR increased by approximately 6.9%, to $103.36.

The average daily rate among hotels in the San Luis Obispo metro area has yet to increase much over last year. From June–August 2011 to June–August 2012, the average daily rate increased by only 1.8%, to $133.06 on a seasonally adjusted basis. But the region is not very far behind the average daily rate for hotels in the Santa Barbara MSA, which grew by 5.0%, to $152.43, in the same time period. The rate increase for hotels in the San Luis Obispo MSA is also higher than the increase experienced by hotels in the Monterey MSA, where the average daily rate fell by 2.2%, to an average of $150.74.

The Restaurants and Hotels sector has seen a substantial increase in overall spending in the past year.

At the city level, we are seeing steady growth in these three measures across the board. For example, from June-August 2011 to June-August 2012, the occupancy rate at Pismo Beach hotels increased by 3.7 percentage points (or 4.4%), to 87.8%, while RevPAR increased by 4.8%, to $151.06. In San Luis Obispo, the hotel occupancy rate increased by 2.1 percentage points (or 2.4%), to 86.2%, while RevPAR increased by 5.9%, to $116.92. We can compare these figures to those seen in Santa Barbara/Montecito and Monterey/Carmel over the same time period. Though RevPAR increased by 14.2%, to $249.55, in Monterey/Carmel, hotel occupancy actually decreased by 2.3 percentage points. In Santa Barbara/Montecito, RevPAR increased by 3.9%, to $264.02, while hotel occupancy increased by 1.6 percentage points to 90.2%.

Although hotels throughout San Luis Obispo County are thriving, passenger traffic out of San Luis Obispo County Regional Airport has yet to rebound after experiencing a steep drop during the economic recession. From January 2012 to September 2012, the airport hosted 197,084 passengers, compared to a peak of 272,134 passengers in 2007.

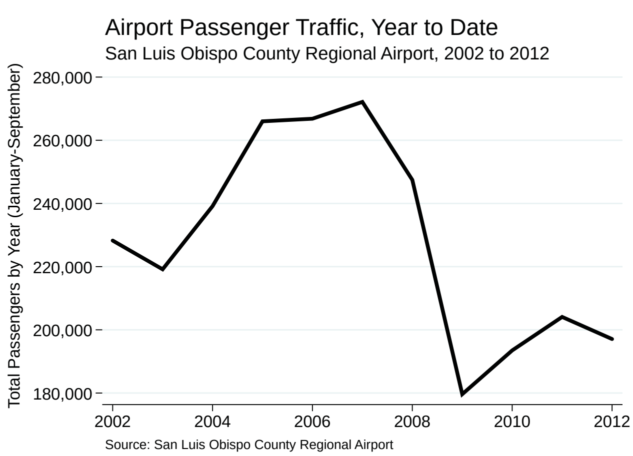
While the decline in traffic was dramatic, it does not negate the positive trends observed for hotels,

Hotel Statistics by City
San Luis Obispo MSA & Other Coastal Cities, Jun-Aug 2011 to Jun-Aug 2012

Location	2011 Average Daily Rate ($)	2012 Average Daily Rate ($)	1-Year Change (%)	2011 Occ Rate (%)	2012 Occ Rate (%)	1-Year Change (%)	2011 RevPAR ($)	2012 RevPAR ($)	1-Year Change (%)
Pismo Beach	170.96	172.04	0.6	84.1	87.8	4.4	144.21	151.06	4.8
San Luis Obispo	131.33	135.79	3.4	84.1	86.2	2.4	110.44	116.92	5.9
Paso Robles	111.92	116.57	4.2	71.3	75.3	5.6	79.85	87.80	10.0
North Coast	144.65	153.65	6.2	73.0	78.0	6.8	106.21	120.11	13.1
Overall	147.22	151.05	2.6	80.1	83.6	4.4	118.16	126.42	7.0
Santa Barbara	285.63	291.79	2.2	88.6	90.2	1.8	254.05	264.02	3.9
Monterey	282.33	302.93	7.3	84.5	82.2	-2.6	218.57	249.55	14.2

Source: PKF Consulting

nor does it imply that tourists are avoiding San Luis Obispo. Rather, airport traffic remains a small component of overall traffic to the region, with only a few hundred thousand total passengers in a given year. San Luis Obispo continues to draw heavy auto traffic from Northern and Southern California. Thus, even though there is room for growth in passenger traffic out of San Luis Obispo County Regional Airport, we don't expect tourism in the region to lag in the coming year.



The California Mid-State Fair in Paso Robles illustrates the region's popularity. In 2012, even as general attendance decreased by about 4.7% from the record high of 2011, revenues for carnival attractions were equal to 2011 values, and revenues from livestock sales increased by over $347,000 (or approximately 24.6%) .[15] It was an impressive showing for the fair following a record-breaking 2011.

Cities in San Luis Obispo County are seeing robust benefits from the resurgence in tourism spending, even more than nearby tourist havens Monterey and Santa Barbara. As an area renowned for its beautiful coastlines, pristine weather, and growing wine industry, tourism plays a central role in the San Luis Obispo County economy, and the steady increase in tourism will bolster the region's economic growth in the coming year.

2012 Proves One of the Best Years for SLO Wine

The strength of the growing wine industry is worth emphasizing—2012 has proved one of the best years on record for wine grapes in the region. Warm days and cool nights in the summer have made for an exceptionally great harvest, yielding an abundant crop of very high quality.[16] A recent heat wave, though a concern, is not expected to significantly disrupt the

[15] "Another Great Year in 2012!," *California Mid-State Fair: The Great American Road Trip,* October 24, 2012.
[16] Julie Lynem, "SLO County Grapes Are Looking Great," *San Luis Obispo Tribune,* September 23, 2012.

harvest. North San Luis Obispo vineyards faced the hottest temperatures, but heat in the harvest season has both positive and negative effects. While grape vines without adequate shade or moisture can shrivel, the heat also helps grapes to mature faster by raising their sugar content. A quicker maturation process is a benefit to vintners hoping to harvest sooner rather than later.[17]

Wine export values suggest that demand is on the rise once again in 2012. From January to August, wine export values totaled $776.4 million, compared to $737.2 million in the first eight months of 2011, and $598.1 million in the first eight months of 2010. There will likely be enough demand to meet the growing supply this year, and the quality of wine grapes this year in San Luis Obispo County should increase demand even further.

A harvest of this type will come as a benefit not only to the region's agricultural sector but also to its tourism sector. Wine and tourism are closely knit in San Luis Obispo County. Wine-tasting tours continue to be a big draw in the region, and as the industry expands, they will only become more popular. With an exceptional crop this year, San Luis Obispo will continue to build its reputation as one of the best wine regions in the country, with the likes of Napa Valley and Sonoma.

Conclusion

With both consumer spending and business spending continuing to increase in San Luis Obispo County, tourism in the region will continue to reap big benefits. Hotel occupancy is on the rise, and hotel rates are increasing as well. In fact, several cities in San Luis Obispo County have seen stronger increases in occupancy rates than observed in tourism-heavy areas such as Santa Barbara/Montecito and Monterey/Carmel. Moreover, as the economy continues to grow in the region and throughout California, tourism in the coming year should be even stronger. Wine tourism should see exceptional growth in the near future, as a great harvest will further San Luis Obispo's reputation as one of the country's top wine regions. Ultimately, the outlook for businesses in San Luis Obispo County remains very positive for the year ahead.

[17] Hope Hanselman, "Hot Temperatures Affect Wine Grape Harvest," KSBY News, October 1, 2012.

Agriculture

by Eric Meux

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Key Chapter Findings

- Total crop value in 2011 sets record high, while strawberries overtake wine grapes as top crop.
- Farm employment in 2011 is also at an all-time high, however experienced farm labor is becoming harder to find.
- State agriculture exports posting positive year-to-date growth, however wine export growth has slowed from last year.

Introduction

San Luis Obispo County is one of the key players in California's agriculture industry for wine grapes and strawberries. According to the California Department of Agriculture, in 2010 the county accounted for 8.3% of California's total wine grape crop by dollar value, and 6.9% of California's total strawberry crop by dollar value. By comparison, the county ranked just 13th among California counties for total crop values—close to 2% of total crop values statewide. Thus, while San Luis Obispo County may not be a major contributor to total agricultural output in the state, its specialized crop production plays a crucial role in the state's harvest of cash crops.

Compared to the state overall, San Luis Obispo County has similar proportions of small and large farms respectively. The majority of California farms are small farms, which range from 10 to 49 acres in size. These small farms constitute 34.7% of all farms in California, while large farms of 1,000 acres or more make up only 5.5% of farms in the state. In San Luis Obispo County, as in the state overall, the majority of farms range from 10 to 49 acres, however San Luis Obispo County has a slightly higher proportion of farms of 50 or more acres than does the state. Meanwhile, the county's high concentration of smaller farms helps to ensure that the county does not put all of its eggs in one basket, so to speak, and fundamentally depend on continually solid growth at only a few farms.

Farms by Size
California and Selected Counties, 2007

Size	California		Fresno		San Luis Obispo	
	# Farms	% of Total	# Farms	% of Total	# Farms	% of Total
1 to 9 acres	25,278	31.2%	964	15.9%	509	18.3%
10 to 49 acres	28,080	34.7%	2,766	45.5%	1,069	38.4%
50 to 179 acres	12,939	16.0%	1,148	18.9%	567	20.4%
180 to 499 acres	7,014	8.7%	547	9.0%	292	10.5%
500 to 999 acres	3,267	4.0%	311	5.1%	133	4.8%
1,000 acres or more	4,455	5.5%	345	5.7%	214	7.7%
Total	81,033		6,081		2,784	

Source: U.S. Dept. of Agriculture, 2007 Census of Agriculture

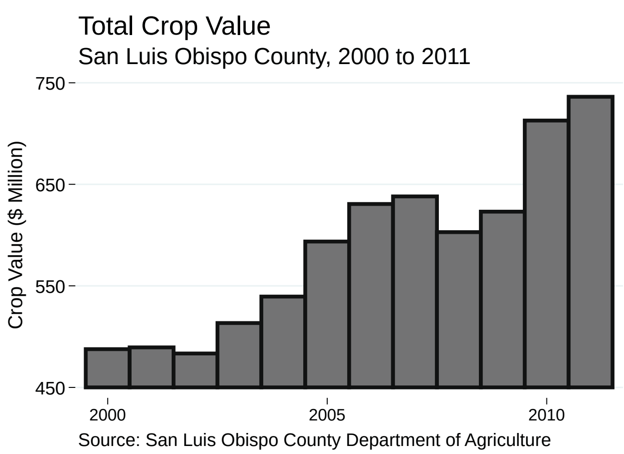
Total Crop Value

The total dollar value of crops in San Luis Obispo County did not disappoint in 2011, increasing by $23.4 million (3.3%) from 2010 to 2011. While this increase may not seem impressive, it is important to remember that unfavorable growing conditions constrained the output of some of the county's major cash crops, such as wine grapes. However, ups and downs in the county's agriculture industry are normal, and weather plays a continual role. The inherent risk of rough weather in damaging crop yields is amplified by the relative unpredictability of crop prices from year to year. Consequently, 3.3% growth in crop values for San Luis Obispo County is actually quite impressive, given the adverse circumstances county farmers faced in 2011.

The largest year-over-year increases in crop values on both a percentage and absolute basis came in the Animal category, with an overall increase of $14.3 million (25.1%) from 2010 to 2011. These gains can be attributed to favorable grazing conditions, which helped increase cattle herd sizes by 4.5%, as well as a 13.4% increase in market prices over the previous year. The Animal category is actually the second smallest category by product value, but because of the exceptionally large increases in Animal yields, the county reached total crop values higher than in any other year.

... 3.3% growth in crop values for San Luis Obispo County is actually quite impressive, given the adverse circumstances county farmers faced in 2011.

The second largest year-over-year increase in absolute crop values came in the Fruit and Nut category, which grew by$4.6 million(1.3%) from 2010 to 2011. This increase is mostly the result of a substantial increase in fresh strawberry production. The impact of higher yields was diminished by lower prices, however. While production per acre increased from 26.1 tons in 2010 to 28.8 tons in 2011, prices decreased $10 (0.1%) per ton.



The Field Product category, the smallest in the county in terms of absolute crop value, also grew substantially year over year. Field Product crop values increased from $18.6 million in 2010 to $23 million in 2011, or 23.6%. A surge in alfalfa hay prices from $140 per ton in 2010 to $260 per ton in 2011 was the biggest contributor to this increase. At the same time, the growth in Field Product crop values was amplified by sharp increases in the prices of barley and grain hay. Total crop values for nursery products grew by a modest 1.8% from 2010 to 2011, driven primarily by slightly higher production and market prices.

The Vegetable category was the only category that faced a decline in total crop values from 2010 to 2010, but even then, only by 1.0%. Part of this decline is attributable to the conversion of traditional vegetable acreage to strawberry acreage, however the decline was exacerbated by lower yields in a few key products. Production per acre for broccoli, the largest vegetable crop by dollar value, decreased by 6.6%. At the same time, as light 0.5% increase in broccoli prices helped to offset some of the year-over-year losses due to lower yields.

San Luis Obispo Crop Values ($ 000s)

Category	2010	2011	2010 to 2011
Fruit & Nut	365,750	370,365	1.3%
Vegetable	176,666	174,981	-1.0%
Nursery	94,708	96,454	1.8%
Animal	57,139	71,479	25.1%
Field	18,545	22,929	23.6%
Total	712,808	736,208	3.3%

Source: San Luis Obispo Dept. of Agriculture

Specialty Crops

San Luis Obispo County harvests a diverse range of agricultural products, but two stand out as major contributors: wine grapes and strawberries. Unfortunately, both products did not share the same fortunes in the 2011 harvest. Strawberry yields were higher, and strawberry production increased, but growing conditions were less favorable for wine grapes, and wine grape output decreased as a result. San Luis Obispo was not the only region of California with a lower wine grape crop this year. Both the Napa and

Sonoma regions reported lower production for 2011 due to unfavorable growing conditions.

As in previous years, fresh strawberries constituted the bulk of strawberry production. In 2011, fresh strawberries made up 76% of total strawberry output, up from 74% in 2010. In turn, fresh strawberries passed up wine grapes to take the top spot for highest total crop value. Consider this a temporary phenomenon, though. Wine Grapes had held the top spot for the preceding 20 years, and will most likely reclaim it in the 2012 crop report due to exceptionally favorable growing conditions for wine grapes these past several months.

Wine production across all varieties declined precipitously in 2011, with Sauvignon Blanc logging the highest percentage decrease from 2010, at 39.4%. The smallest proportional decline in production was for Pinot Noir grapes, at 20.2%. Yet, prices also increased across the board, helping to mitigate overall decreases in crop values. If it hadn't been for these price increases, San Luis Obispo County may have seen total crop values decline from 2010 levels.

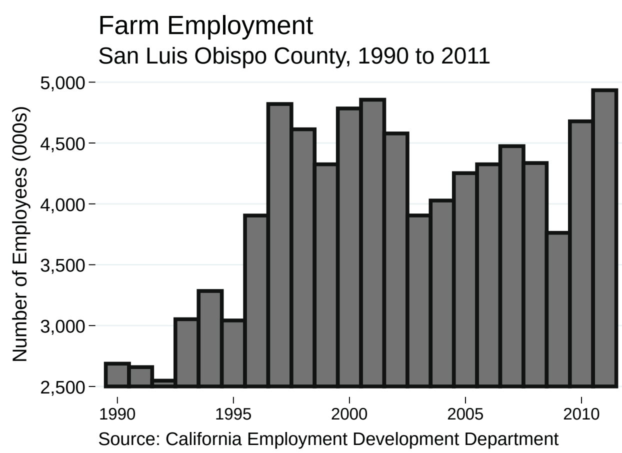
San Luis Obispo Wine Grapes, 2010 to 2011

	Change in Production	Change in Prices
Chardonnay	-39.2%	1.5%
Sauvignon Blanc	-39.4%	18.5%
White Wine (Other)	-38.8%	5.8%
Cabernet Sauvignon	-39.1%	16.0%
Merlot	-24.9%	17.6%
Pinot Noir	-20.2%	8.4%
Syrah	-38.7%	21.7%
Zinfandel	-23.0%	9.4%
Red Wine (Other)	-31.5%	15.8%

Source: San Luis Obispo Dept. of Agriculture

Employment

Because the agricultural industry includes many informal workers, it is difficult to assess total farm employment in the county. The state's Employment Development Department (EDD) collects information for employees on company payrolls, which provides a fairly good indication of employment trends in the local industry. While the data is released monthly, the farm employment series is more volatile than most, and discerning meaningful trends from the just the last few months can be very difficult. Examining annual farm employment over the last twenty years provides a better sense of where trends are heading. Farm employment in 2011 stood at roughly 5,000 employees in the county, an all-time high. Coincidentally, crop values were at a record high in 2011, and production levels for several commodities were higher than in previous years. As demand for farm labor has risen over the years, the supply of farm labor has generally risen to meet it.



Unfortunately, at present, there is a shortage of farm labor in California.[18] While this may seem odd, given the traditionally high levels of unemployment in many of California's agricultural counties, it highlights the need for experienced harvesters. According to one San Luis Obispo County farmer, "We started noticing labor getting tighter a couple years ago. Then last year it got even worse, and this year it seems like it is getting to be much more challenging. Our harvest

[18] Justin Ellison, "California Farmers Report Labor Shortages" Farm Plus Financial, June 27, 2012. http://www.farmloans.com/blog/tag/illegal-immigration/

has come into full swing in the last month, and that is when we really started noticing that we are having a tough time filling out harvest crews."

Recent Trends

2011 was not the best year for some products, wine grapes in particular, but trends in 2012 suggest that things should be brighter in the 2012 report. Wine regions across California are reporting a beautiful harvest, both in quantity and quality. This year's favorable growing conditions should help boost wine grapes to the number one spot for total crop values in San Luis Obispo County once again. This increase in wine grape production might be tempered, however, by a slowdown in national exports, a trend which so far California agriculture products been able to avoid.

California Agriculture Exports, 2010 to 2012 YTD

Export Commodity	2010 to 2011	2011 YTD to 2012 YTD
Total Agriculture Products	13.4%	14.0%
Wine	20.1%	5.4%
Strawberries, Fresh	-0.5%	6.9%

Source: WISER

For the first eight months of 2012, the export values of all California agriculture products were up 14.0% over the same year-to-date period. San Luis Obispo's two primary crops are still seeing positive export growth at the state level. Fresh Strawberry exports are up 6.9% year-to-date, after marginally negative growth in 2011. Wine exports for the year to date are up 5.4% from where they were during the first eight months of 2011, but growing at a slower pace than they were from 2010 to 2011. The slowdown in Wine exports is likely connected to the lower-than-average wine grape production in 2011, making fewer bottles of California wine available in that vintage.

An important recent development for Central Coast farmers in the coming year is an order from the California State Water Resources Control Board (WRCB) to comply with new, stricter regulations on the discharging of wastewater in irrigated land. The order requires farmers to install and maintain backflow protection for discharging waste water and to conduct monitoring of riparian areas and wetland habitats. Agriculture groups throughout the state have petitioned the Board, claiming that its order fails to take into account the negative economic impact of the regulations on the agriculture industry. The ball is now back in the WRCB's court, and the Board has until roughly the middle of next year to act on those petitions, hold a hearing, or obtain a 60-day extension. Whatever the eventual outcome of the Board's order, one thing is certain: mandating that farmers become environmental monitors is sure to add to farmers' costs of doing business, unless the farmers are subsidized or otherwise compensated for monitoring costs.

Residential Real Estate

by Dustin Schrader

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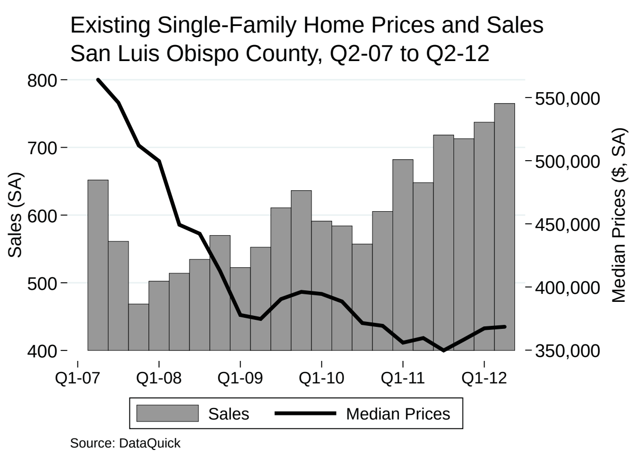
Key Chapter Findings

- Home prices in San Luis Obispo County remain low, but the trend is moving upward.
- Foreclosures are down substantially in the region, due in part to an increase in short sales.
- Residential construction growth remains slow, but upcoming projects could change the outlook.

A Slow Trend Upward for the Housing Market

As the economic recovery continues in San Luis Obispo County, the outlook in the homebuyer's market is no longer one of doom and gloom. Although home prices remain low for the county, the trend is moving upward. Moreover, home sales continue to increase as defaults and foreclosures steadily fall, suggesting that the worst is indeed in the past for San Luis Obispo County's residential real estate market.

Among existing single-family homes, median home prices reached $369,000 on a seasonally adjusted basis in the second quarter of 2012. Since reaching bottom in the third quarter of 2011, existing single-family home prices have risen approximately 5.5%. In the state overall, existing single-family home prices have risen over 9% over the same time period. Year over year, home prices have grown by approximately 2.5% in San Luis Obispo County, lagging the increase in the state overall (7.9%).



Existing single-family home prices are growing more rapidly in neighboring Santa Barbara and Monterey Counties. Year over year, prices are up approximately 6.8% in Santa Barbara County and up approximately 7.7% in Monterey County. On the other hand, even though home price appreciation in San Luis Obispo County has lagged behind the increases observed in the county's Central Coast neighbors and the state, it has nonetheless been much faster than increases in many other areas of the state. Prices for existing single-family homes are approximately flat at -0.3% year over year in Los Angeles and down 2.7% in San Francisco, and up slightly in Orange County and San Diego, at 1.0% and 0.7% growth, respectively. Thus, while home prices in San Luis Obispo County are not as strong as we would like to see, they have nonetheless turned the corner.

768 home sales were completed in the second quarter of 2012, for an increase of 17.8% year over year.

Existing single-family home sales in San Luis Obispo County are increasing much more quickly. On a seasonally adjusted basis, 768 home sales were completed in the second quarter of 2012, for an increase of 17.8% year over year. This is ahead of the pace of sales in the state overall, where, on a seasonally adjusted basis, 87,460 home sales were completed in the second quarter of 2012, for an increase of 9.7% year over year. Granted, because of the comparatively small size of the San Luis Obispo County housing market, home sales statistics are likely to be more volatile each quar-

Existing Single-Family Home Prices (SA)
By Region, Q2-12

Location	Median Price Q2-12 ($)	1-Year Chg (%)	1-Qtr Chg (%)
Central California			
San Luis Obispo	369,000	2.5	0.0
Santa Barbara	308,000	6.7	4.7
Monterey	267,000	7.8	-3.2
Southern California			
Los Angeles*	328,000	-0.3	1.7
Orange County*	492,000	1.0	5.0
San Diego*	359,000	0.7	1.3
Inland Empire*	180,000	4.6	3.5
Other Southern California*	399,000	-1.3	1.5
Northern California			
San Francisco*	668,000	-2.7	0.9
Oakland*	350,000	10.0	10.7
San Jose*	571,000	6.7	8.5
Sacramento*	161,000	0.6	-1.7
Other Northern California*	252,000	4.8	3.1
State of California	266,000	7.9	5.6

Source: DataQuick
*Average Regional Price

San Luis Obispo County Residential Real Estate, by City (SA)

Existing Single-Family Home Median Prices*			
Location	Q2-11 ($)	Q2-12 ($)	Change (%)
Arroyo Grande	458,000	394,000	-13.9
Atascadero	295,000	336,000	14.0
Grover Beach	305,000	312,000	2.4
Paso Robles	292,000	292,000	0.0
San Luis Obispo	554,000	502,000	-9.4
San Luis Obispo County	360,000	369,000	2.5
Residential Sales			
Location	2011 YTD	2012 YTD	Change (%)
Arroyo Grande	170	195	14.7
Atascadero	187	208	11.2
Grover Beach	74	76	2.7
Paso Robles	323	319	-1.2
San Luis Obispo	211	227	7.6
San Luis Obispo County	1,596	1,788	12.0

Source: DataQuick
*Prices have been rounded to the nearest thousand

ter on average. But the trend in the county is clearly positive.

Since the dip in home sales in mid-2010, following the expiration of the tax credits for first-time homebuyers, home sales have matched or surpassed sales in the preceding quarter in all but the second quarter of 2011. Seasonally adjusted quarterly home sales are up 38.5% from the third quarter of 2010. In fact, the second quarter of 2012 marked the sixth consecutive quarter of year-over-year increases in home sales; so, while home prices have been slower out of the starting gate, the underlying sales trends suggest that the region is indeed moving forward at a solid clip.

The real estate data are also volatile at the city level, especially for seasonal numbers, but we see some positive trends in the housing markets of individual cities, though some cities are clearly faring better than others. Fortunately, activity is increasing in both North and South San Luis Obispo County. Arroyo Grande, in South San Luis Obispo County, has seen a solid increase in residential transactions in 2012—rising 15.4% above the same point in 2011. Residential sales in Atascadero are also 9.2% higher through the second quarter of 2012, and existing single-family home prices are up roughly 15% year over year. Still, other parts of North and South San Luis Obispo have lagged the county overall, such as Paso Robles in the North, where home sales were actually lower through the first six months of 2012 than they were a year ago. In addition, home prices in Arroyo Grande and in the City of San Luis Obispo are down relative to last year, which shows that while the recovery continues in the county overall, the progress has not been evenly distributed.

In total, the data suggest that the homebuyer's market in San Luis Obispo County has turned the corner but has yet to take off. Why might this be so? According to the California Association of Realtors (CAR), the problem lies in a severe lack of supply. Even as home affordability remains as high as ever, interest rates remain as low as ever, and demand for homes is high as well, there simply aren't enough homes for sale. According to CAR, there is a 4.5-month inventory of homes in the county, compared to a 10- to 15-month inventory in the early 1990s. Demand for rental units is very high, and investors are buying up the available inventory and opting to rent homes out rather than sell them.[19]

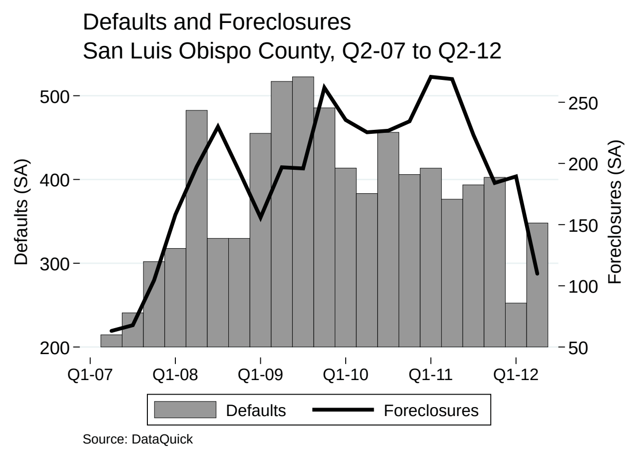
According to Reis, Inc., asking rents for apartments in San Luis Obispo County grew by 0.8% in the first half of 2012. The vacancy rate for apartments decreased from approximately 2.7% in 2011 to 2.3% in the first half of 2012. Even as demand remains high for single-family homes, even higher demand for apartments encourages a widespread buy-up of homes for rentals, keeping the available supply of homes for sale very low. Until this trend slows, it may be difficult for the homebuyer's market in San Luis Obispo County to continue to grow.

Distressed Mortgages Are Falling, with Far Fewer Moving into Foreclosure

Despite a steep uptick in the second quarter of 2012, mortgage defaults in San Luis Obispo County are generally decreasing over time from their peak in mid-2009. In the second quarter of this year, approximately 348 notices of default were issued in San Luis Obispo County, compared to 376 in the second quarter of 2011 and 383 in the second quarter of 2010. The number of defaults in the second quarter of this year was still roughly 62% higher than the figure from 2007, back before the housing market imploded, but defaults are nonetheless well on their way toward getting back to more "normal" levels.

Defaults are nonetheless on their way toward getting back to more "normal" levels.

As quarterly defaults move steadily downward, foreclosures in the county are falling fast. Foreclosures peaked in the first quarter of 2011 at 271 (on a seasonally adjusted basis), but fell to 110 in the second quarter of 2012, with much of this decline coming in the most recent quarters. Furthermore, outside of a momentary plateau from the fourth quarter of 2011 to the first quarter of 2012, seasonally adjusted foreclosures have declined sharply and consistently since early 2011. The data simply do not support the belief that a second wave of foreclosures will commence in the near future, which means that the worst is in fact behind us.



Foreclosures have been limited in part by an increase in short sales of distressed properties throughout the state. For example, 27% of all existing home sales in California this past September were short sales, up from 23.8% in September of last year.[20] According to realty data from Scenic Coast MLS,[21] roughly 13.1% (274 in all) of sales of single-family residences (stick built, not prefabricated) in San Luis Obispo County were short sales through the first nine months of 2012, compared to roughly 12.9% (324 in all) in 2011 and 10.6% (222 in all) in 2010.[22]

A simple exchange of foreclosures for short sales is not a sign of a healthy housing market, as short sales

[19] Julia Hickey, "Local Housing Market's Growth Limited by Supply of Homes, Expert Says," *San Luis Obispo Tribune,* October 9, 2012.

[20] Lawler Economic & Housing Consulting, LLC., "NAR: Existing Home Sales Down Slightly on Seasonally Adjusted Basis; Inventories Dip," October 19, 2012.

[21] MLS data is deemed reliable but not guaranteed accurate by the MLS.

[22] The Keith Byrd Team, "San Luis Obispo County SFRSB Sales," San Luis Obispo, October 23, 2012, `http://www.slocountyhomes.com/stats_all.html`.

San Luis Obispo County Defaults & Foreclosures, by City (SA)

Location	2011 YTD	2012 YTD	Change (%)
Defaults			
Arroyo Grande	67	52	-22.9
Atascadero	116	96	-17.3
Grover Beach	35	35	0.0
Paso Robles	156	135	-13.7
San Luis Obispo	90	43	-52.5
San Luis Obispo County	786	597	-24.1
Foreclosures			
Arroyo Grande	47	33	-30.0
Atascadero	92	39	-57.7
Grover Beach	29	13	-55.2
Paso Robles	133	64	-52.3
San Luis Obispo	22	20	-9.1
San Luis Obispo County	545	303	-44.3

Source: DataQuick

are still detrimental to mortgage servicers and damage the credit of home sellers, but short sales are only part of the foreclosure story. Fewer homes are going into foreclosure in San Luis Obispo County as fewer homeowners are defaulting on their mortgages. The economy of the county is improving, and more residents are returning to work. Loan modifications are helping some homeowners to keep up with their mortgage payments. The steep uptick in foreclosures in 2009 came amid a period of economic contraction. Alternatively, the current pace of slow, steady economic growth in San Luis Obispo County greatly reduces the likelihood of another large wave of foreclosures to come.

Residential Construction Dips Slightly in 2012, but Local Projects May Improve the Outlook

Even as existing single-family homes are in short supply in the county, building permits for single-family homes are down for the year-to-date relative to 2011. Eighty-three single-family building permits were issued in the first half of 2012, totaling $28.6 million, compared to 105 single-family building permits in the first half of 2011, totaling $36.5 million. On the other hand, multifamily construction is up slightly for the year-to-date. In the first half of 2012, 19 multifamily building permits were issued, totaling $2.0 million, compared to nine building permits, totaling $1.4 million, in the first half of 2011.

Though total residential construction remains sluggish in 2012, projects currently in development or just underway could change the outlook in the near future. The Spanish Springs project calls for the construction of as many as 390 single-family homes, 83 apartments or condos, and 320 senior residential units in Price Canyon north of the Pismo Beach city limits.[23] The project would require the City of Pismo Beach to annex 1,264 acres of land, which would increase the square mileage of the city by approximately 50%.[24] The Pismo Beach City Planning Commission approved the project by a three-to-two vote in early October, and the city council is expected to consider the project in late November or early December.[25] If approved, Spanish Springs could bring an estimated 1,500 new residents to the city, as well as some much-needed construction jobs to the region.[26]

Construction is expected to begin by mid-2013 on 32 new residential units on Monterey Street downtown, as part of a much larger Chinatown redevelopment already underway in San Luis Obispo. The project was originally approved by the city in 2009, but stalled

[23]Cynthia Lambert, "Price Canyon Plan Forwarded to Pismo Beach City Council," *San Luis Obispo Tribune,* October 9, 2012, http://www.sanluisobispo.com/2012/10/09/2257356/price-canyon-pismo-development.html.

[24]Tayler Duprel, "Price Canyon Gets a Green Light from Pismo Commission," *San Luis Obispo New Times,* October 10, 2012, http://www.newtimesslo.com/news/8448/price-canyon-gets-a-green-light-from-pismo-commission/.

[25]Cynthia Lambert, "Price Canyon Plan Forwarded to Pismo Beach City Council."

[26]Matt Fountain, "A Beach of a Race," *San Luis Obispo New Times,* October 18, 2012, http://www.newtimesslo.com/news/8502/a-beach-of-a-race/.

upon the onset of the economic recession.[27] Meanwhile, in Los Osos, construction of the long-delayed sewer project will proceed after much political debate, with an expected completion date of 2014[28] and a total budget of $173.4 million.[29]

The completion of the sewer project could have a positive effect on the economy of Los Osos and San Luis Obispo County. Homebuying generally is not limited to the purchase of a home itself. It entails appliance and furniture purchases, as well as home alterations and additions for existing properties. In the first half of 2012, permit values for residential alterations and additions in the county are well below permit values for the first half of 2011: $8.5 million versus $12.6 million, respectively. But a project such as the construction of a sewer system in Los Osos may encourage homeowners in the city to invest in new plumbing for their homes, as a means of adapting to the new system, to the benefit of businesses and construction workers in the city and in the county. Similarly, new construction in other parts of the county will spur new spending on residential goods and services. The impact will not be immediate, but it will nonetheless provide a boost to the county's economic productivity down the road.

Conclusion

Although the housing market has yet to take off in San Luis Obispo County, there are reasons to be optimistic as the market has experienced modest improvement over the past year. Defaults and foreclosures are decreasing while home sales are increasing, and even though residential construction in 2012 trails last year's totals for the year to date, several projects may help to jump-start construction in the county very soon. Home prices have been slow to increase, but the gains in San Luis Obispo County compare favorably to the gains in other regions, such as Los Angeles and Orange County. Neither North nor South San Luis Obispo County show any signs of tipping back into a real estate double dip. As the economy continues to grow in the coming year, we expect home prices and home sales to rise in turn, but it will take a marked increase in the supply of homes to maximize growth in the housing market in the near future.

[27] AnnMarie Cornejo, "Chinatown Project Begins in Downtown San Luis Obispo," *San Luis Obispo Tribune,* September 24, 2012, `http://www.sanluisobispo.com/2012/09/24/2240569/chinatown-project-begins-in-downtown.html`.

[28] Michelle Hauser, "Project Overview," *Dig Los Osos: Los Osos Wastewater Collection System,* The County of San Luis Obispo, October 24, 2012.

[29] David Sneed, "Attempt to Halt Construction of Los Osos Sewer Fails," *San Luis Obispo Tribune,* July 15, 2012, `http://www.sanluisobispo.com/2012/06/15/2107854/attempt-to-halt-construction-of.html`.

2012 Commercial Real Estate

by Steve McCarty and Steve Davis

Stafford McCarty Commercial Real Estate

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Key Chapter Findings

- The market is moving in a positive direction, although at a slow pace.
- Interest rates continue to remain near record lows, but qualifying remains an issue.
- The volume of on market and off market commercial transactions is increasing.

A Brief Note on Residential Market—Over-Coming Inertia

San Luis Obispo

Prices have stabilized in San Luis Obispo; homes are selling faster than in the prior year and the volume of transactions has increased. Agent interviews point to shrinking inventory and faster transactions. Volume is up and agents are reporting a lack of lower end inventory—homes priced under $400,000. Properties in this lower price range are receiving multiple offers. Even with the median price staying flat at $535,000 for this last year, the lack of lower end inventory is creating economic opportunity to build and the market is seeing the start of new construction. Median values in San Luis Obispo remain approximately $100,000 less than they were in 2008 and houses are selling at approximately $305 per square foot.

North County

The North County home market is also seeing an increase in the volume of sales and a decrease in average time on the market. Contrasted to San Luis Obispo, there has been upward movement in median valuation in the North County. Median values in North County have risen $35,000 over 2011 numbers and houses are selling for approximately $180 per square foot.

Also in North County, sales volume is up and agents there are reporting a lack of lower end inventory–under $300,000. With the lower price in North County, buyers are taking advantage of buying property for less than the price of production. However, the lower median price does not provide the economic confidence to build new tract housing product at this time.

In both market areas there is movement in multi-family land development and renewed interest in identifying projects.

Housing Related Projects

- ROEM Development completed its tax credit project at the Village at Broad.
- The balance of the housing component at the Village at Broad is under construction for studio product.
- The Housing Authority has nearly completed the first phase of work on their low income project at the old railroad "Y" site off of Broad Street.
- A land sale at Orcutt and Broad Street, approved for approximately 80 entitled units, sold for $28,750 per unit.
- Prado Road was previously purchased and construction has commenced on the residential portion of the project.
- The Marsh Street Commons, a 32,000 sq. ft. mixed use project on the corner of Marsh and Nipomo, is under construction with presales occurring.

Residential Unit Sales, 3rd Quarter Annual Data

Variable	2008	2009	2010	2011	2012
San Luis Obispo					
# Units Sold	159	163	191	215	273
Median Price ($)	635,000	569,000	550,000	535,000	535,000
North County					
# Units Sold	638	702	698	892	991
Median Price ($)	390,000	340,000	296,000	270,000	305,000

Source: San Luis Obispo Multiple Listing Service;
Compilation by Stafford McCarty Commercial Real Estate
Note: Comparative data is for the first three quarters of each year

Residential Foreclosure Activity

The number of reported defaults is less than in previous years. However, this can be misleading as short sales are making up a larger part of the market transactions. All in all, most feel the worst is behind us.

Commercial Markets

Lending

Evidence of new commercial loans is emerging as lenders are placing their signs on construction sites. Loans are being refinanced and there seems to be a relaxing exhale as compared to the tightness of the market in previous years.

The lender pipeline of commercial product coming on the market is thinning. Lenders appear to have increased their willingness to deal with borrowers, extending credit and working out short sales on troubled commercial assets, which decreases the number of properties going to foreclosure.

Leasing Activity

Leasing activity is being driven by two factors. First are companies that have made it through the downturn, have resized, and are matching their leasehold space to their new requirements. Second are companies moving into the market and companies that are expanding (particularly in the tech and medical sectors). A few examples: American Tires is opening new locations in San Luis Obispo and Paso Robles. Tek Tegrity, Rosetta and Mind Body are expanding operations. Franchises such as Plutos, Rocket Fizz, Mr. Pickles, etc. are all moving into the San Luis Obispo trade area.

Buyer Sources of Capital

User buyers are turning to banks mostly for Small Business Administration (SBA) loans in which cash for down payments can be minimized. Investors are coming in with cash, taking advantage of opportunities, repositioning assets, and meeting tenant need within the market. The exchange market is reemerging and brokers are seeing exchange monies seeking replacement properties.

Commercial Vacancy Rates (%), San Luis Obispo Metropolitan Area

Property	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Industrial/Warehouse	2.8	3.8	6.4	4.0	4.3	2.3	5.4	6.1	9.1	8.7	4.5
Retail Functioning	1.9	2.4	2.2	1.7	1.8	1.4	3.0	5.6	5.1	3.4	3.7
Office Functioning	9.9	8.4	5.4	3.2	4.7	3.5	6.1	9.7	12.6	11.6	8.6

Source: Stafford McCarty Commercial Real Estate

Commercial Markets in San Luis Obispo

Retail

The retail market segment was the only segment adding inventory last year (approximately 51,000 sq. ft.) and now stands with a base retail inventory of 4,156,000 sq. ft.. Despite the recovering economy, the retail segment remains flat with just a slight increase in vacancy: up to 3.7% compared to 3.4% from last year. There is approximately 154,000 sq. ft. on the market.

These retail additions were primarily at the Target Center on Los Osos Valley Road which is now home to Olive Garden and Dick's Sporting Goods. Additionally, Fresh and Easy opened its 9,000 sq. ft. operation on Broad Street at the beginning of the year.

There has been a shuffling of grocery store inventory. A group of Scolari's Markets closed its doors and was purchased by NKT Commercial in markets from Santa Barbara to Paso Robles. Locations will be backfilled by such tenants as Albertsons, Smart and Final, and Fresh Market. NKT recently has taken over University Square in San Luis Obispo, an approximately 89,000 sq. ft. former food/pharmacy center undergoing a makeover.

Office

Given the lingering effects of the economic downturn, there have been no new office additions to the market this year. The office inventory base is approximately 2,700,000 sq. ft.

Throughout the Central Coast, the office sector remains the market segment with the largest vacancy, although office vacancy dropped, 25% compared to last year, to 8.6%. There is an interesting disparity in the San Luis Obispo market where the available office inventory is not matching user needs. The user requirements are currently for larger office product, 20,000 sq. ft. to 60,000 sq. ft (some even larger). The existing vacant inventory is undersized, averaging 2,500 sq. ft. As a result, there are a number of users waiting to have build-to-suits completed, and there are other projects currently in the negotiation stage.

At present, available office inventory in San Luis Obispo is approximately 234,000 sq. ft. Depending on location and landlord tenant improvement contributions, downtown offices have leased for as little as $1.00 per sq ft. per month gross. Second generation unit rents continue to be $0.20 to $0.40 per sq. ft. off of their pre-recession average. Free rent and larger owner contributions to tenant improvements are part of lease negotiations.

Buildings with character, especially former residences converted to offices, continue to be desirable. A few sales noted:

- 1305 Marsh Street: 2,564 sq.ft. Approximately $279 square feet
- 1118 Palm Street: 2,144 sq.ft. Approximately $210 square feet

SESLOC Federal Credit Union had approximately 9.5 acres of land it owned for sale but has subsequently withdrawn it from the market electing to build a new

35,000 sq. ft. headquarters, plus a 5,000 sq. ft. retail branch. The project is presently in planning.

Manufacturing

The vacancy rates for manufacturing product has dropped to 4.5% (8.7% in 2011) with San Luis Obispo's available manufacturing inventory standing at approximately 171,000 sq. ft. The total base of industrial inventory is approximately 3,804,000 sq. ft.

Similar to the office market, user demand for manufacturing product is there, but users are having difficulty finding suitable property. Demand is, across the board, for small manufacturing spaces up to warehouse spaces of 15,000 (plus) sq. ft. This is the second year in a row that no new buildings have been added to the manufacturing inventory.

Sales

Industrial land sales have been brisk in an area known as East Airport. However, there is a key backstory. These finished lots sat on the market for several years, tied up in litigation. The parcels, located in the County of San Luis Obispo adjacent to the City, have a competitive advantage with lower impact fees. By way of example, the fees for a 50,000 sq, ft. building in the County could be as much as $750,000 less than in the City. Like water seeking low spaces, emerging activity and new construction are happening on these parcels. Last year, a local buyer purchased 10 lots from the lender and this year purchased the balance for under $5.00 per sq. ft. Some of these lots were subsequently re-traded. This, coupled with tenant demand for large buildings (noted earlier), has led to new construction. New construction rents are approximately $2.00 per sq. ft., triple net (NNN).

The comparable sales have established a new market value ($6 to $8 per sq. ft), and other parcels, from two acres to ten acres, which have subsequently sold, are aligning themselves with these East Airport parcel transaction valuations, adjusting downward to offset for impact fees, level of lot finish, and available services. A ten acre parcel with similar zoning sold for $1.71 per sq. ft., as it had none of the off site improvements, no services installed, and was tagged with impact fees of approximately $17 per sq. ft.

Along with this, existing buildings for sale have been absorbed, and as noted above, larger product is not available. In the first two sales noted below, the buildings had been on the market for over three years.

- 21 Zaca Lane with approximately 21,800 sq. ft. at 980,000 or $87 per sq. ft.
- Farm House, approximately 20,000 sq. ft. of shell construction, $2,700,000, sold to a high end manufacturer/retailer - office/manufacturing product on five acres at approximately $135 per sq. ft.
- 4500 Santa Fe, approximately 21,000 sq. ft of metal industrial buildings with excess land; the asset was purchased by San Luis Garbage for $3,700,000 or approximately $173 per sq. ft.

Underscoring these sales is the fact that assets are continuing to sell for less than current reproduction values. This is soon to change as the inventory disappears.

As noted in previous years' reporting, the East Airport Development has numerous finished lots suitable for constructing larger warehouse and office buildings. To date only one of the twenty-plus lots has seen completed construction and the price paid for the land was approximately $17 per square foot. This year ten parcels of acre-plus lots have sold from just under $5 per square foot to $6 per square foot.

Downtown San Luis Obispo: A Changing Face—Restaurants

With modest exceptions, available downtown inventory has all but disappeared with only a few lingering vacancies on the fringe. The changing face of downtown noted in previous articles has taken place—soft goods retailers are being replaced by restaurants.

Key projects are moving forward:

- Garden Terraces is proposing 35,000 sq. ft. of commercial space.
- Chinatown Project with 50,000 sq. ft. of commercial space has broken ground on the Palm Street side of the project.
- Marsh Street Commons has broken ground on 8,500 sq. ft. of commercial space, 4 lofts and 8 single-family homes.

These are in the downtown core and have multiple stories; retail on the ground floor, residences on the upper floors. Additionally, Garden Terraces and the Chinatown Project both include hotels.

Rents downtown can vary widely. Second and third generation rates are typically under $1.75 to $2.00 per sq. ft. while retrofitted buildings have asking rents between $2.00 and $3.50 per sq. ft. The units in the core blocks of downtown, have achieved high watermark rents as high as $4.50 per sq. ft.

Commercial Markets in Paso Robles and North County

Vacancy rates in Paso Robles and the North County are higher than in San Luis Obispo across all market segments. Compared to previous years, there appears to be more product available for purchase, as opposed to being available just for lease. A few properties which have been on the on the market for a long time are finally selling. Valuation patterns follow a familiar story where sale prices are below reproduction costs. However, even with all of these factors, the influx of new businesses and the expansion of existing businesses are providing a sense of vitality to the area.

Retail

Modest inventory has been added to the retail market—most noticeable is the 25,000 sq. ft. building for TJ Maxx in the Regency anchored center along Highway 46. The Retail base inventory for the market currently stands at approximately 4,634,000 sq. ft. (similar to San Luis Obispo) Retail vacancies have increased slightly from 3.5% last year to 4.75% this year. A significant amount of that vacancy is in the Scolaris building (+/- 40,000 sq. ft.) and former Powerhouse buildings (+/- 60,000 sq. ft.). There is approximately 220,000 sq. ft. of retail space on the market at this time and, like last year, smaller, speculative spaces have been slow to absorb. A few noted sales:

- Downtown, 12th and Pine, A & R Furniture and adjacent buildings, 27,853 sq. ft. sold for approximately $3,400,000 or $122 per sq. ft.
- 205 Oak Hill, $3,317,500, 12,384 sq ft., approximately $267 per sq. ft.

A flurry of smaller buildings, 1,000 to 3,000 sq. ft., have sold throughout the market at varying price points from approximately $100 to $295 per sq. ft.

Office

Office product in the North County is still the weak spot and absorption has only marginally decreased from 18.41% in 2011 to 18.27%. Office vacancy is scattered and is predominately in smaller unit sizes—under 2,500 sq. ft. There is approximately 71,000 sq. ft. vacant.

As noted in previous years, this market is still in recovery from the financial market fall out that occurred at the beginning of the recession. Asking rents have shifted to gross versus NNN rents and are still in the middle range for the overall Central Coast market at approximately $1.50 per sq. ft for quality office space.

Commercial Vacancy Rates (%), Paso Robles Metropolitan Area, 2012

Property	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Industrial/Warehouse	9.4	10.7	3.5	5.0	2.8	7.5	13.2	8.0	7.7	6.5
Retail Functioning	1.9	< 1.0	< 1.0	< 1.0	< 1.0	2.2	4.1	4.5	3.5	4.8
Office Functioning	1.2	1.8	1.2	5.2	5.6	7.7	24.1	17.5	18.4	18.3

Source: Stafford McCarty Commercial Real Estate

We project more sales next year as there is available inventory on the market for purchase. Rents are still down which in turn keeps a lid on upward values for buildings.

Notably, this last year there was a LEED office building short sale at 2727 Buena Vista Dr, 19,499 sq. ft., $2,800,000 or approximately $144 per sq. ft.

Manufacturing

Overall absorption has been lackluster but the owner/user expansion has been active. A few include Silicone Fabricators, Santa Cruz Biotech, and a number of wineries. The industrial sector added approximately 170,000 sq. ft., with vacancy now standing at 6.47%, (down slightly from 7.73% last year). Paso Robles has an industrial base of approximately 3,100,000 sq. ft. A 5,000 sq. ft. building at 2754 Concrete Ct., sold at $110 per sq. ft. Otherwise, there have been sales in the market of smaller units in the similar price point range.

North of Highway 46, lenders have taken back finished industrial parcels and placed them on the market. Finished parcels vary widely in price and can range from $1.50 per sq. ft. to $6.00 per sq. ft.

Agricultural Impact: The Wine Industry and Commercial Inventory

This industry sector continues to broaden its base as it matures in the market. Buildings supporting viticulture are continuing to be built. This last year over 150,000 sq. ft of facilities have been issued final permits in the County. Over an 11-year period, this growth of additional winery related inventory in the County translates to approximately 50% of the entire Paso Robles industrial base.

The region is attracting greater attention as major corporations establish themselves and continue expanding and having existing operations change hands. Weyrich's vacant Villa Toscana sold, as did the former Arceiro/EOS approximately 112,000 sq. ft production facility (both to off shore money). Most noticeable is the sale of the 300,000 sq. ft. (plus) San Miguel custom crush operation, to Gallo, another major player expanding their roots in the County.

Commercial Investments

Investment sales are continuing throughout the Central Coast. Some are true investment sales, having a stabilized tenant base and easily calculated cap rates. Other investment sales are buildings which can be repositioned by filling vacancies or changing tenants and have an anticipated cap rate. These investments are selling for below reproduction costs and are being turned around in a short time with higher rents, The trend has been more on the latter investment sale type. Discussions with lenders and appraisers indicate cap rates at this point to be in the mid 7s.

Investors are expecting well-anchored centers to be priced below 6 caps. Locally, buyers are still looking for 8 caps, but these are rare to find.

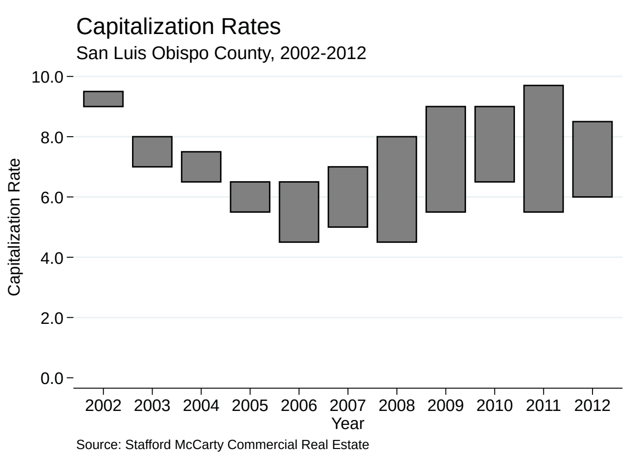
Local capitalization rates are firming up and the examples are noted to evince:

- 205 Oak Hill in Paso Robles (mentioned above), 7.3 cap on existing rents, 12,384 sq ft., $3,317,500, approximately $267 per sq. ft (with 30% vacancy).
- 105 South Main Street, Templeton, $2,483,750, 13,144 sq. ft., approximately $190 per sq. ft., 6.7 cap.
- 1327 Archer Street in San Luis Obispo, $1,800,000, 8,076 sq. ft., approximately $223 per sq. ft., 6.7 cap.
- 1001 Marsh Street, San Luis Obispo, $2,300,000, 5,126 sq.ft., approximately $450 per sq. ft, 5.9 cap.

Lenders are looking to loan on "bankable deals"–meaning transactions involving cash flow and good credit. Available financing for institutional investments can be at sub 5% interest rates while conventional financing is sub at 7%.

As noted earlier, tax deferred exchanges, once an active part of the market, have begun to surface again. But each transaction appears to be occurring on a case-by-case basis, with buyers having their own basis for determining value.

Following are capitalization rate ranges evinced over the last ten years for our market area:

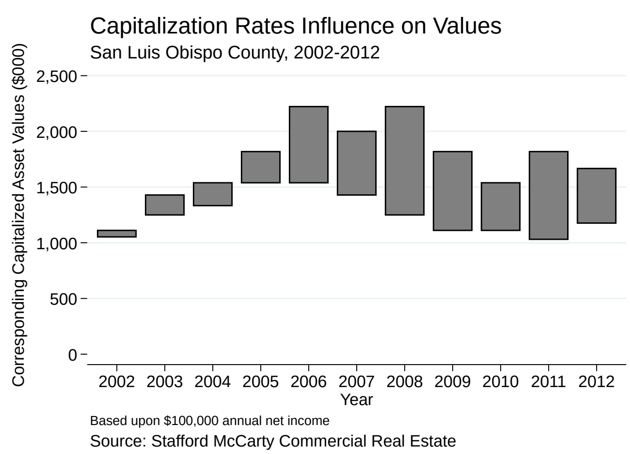


Cap Rates and Implied Value

Year	Cap Rate Range Low	Cap Rate Range High	Implied Asset Value ($)
2002	9.0	9.5	1,100,000
2003	7.0	8.0	1,428,000
2004	6.5	7.5	1,538,000
2005	5.5	6.5	1,818,000
2006	4.5	6.5	2,222,000
2007	5.0	7.0	2,000,000
2008	4.5	8.0	2,000,000
2009	5.5	9.0	1,818,000
2010	6.5	9.0	1,538,000
2011	5.5	9.7	1,818,000
2012	6.0	8.5	1,176,471

Source: Stafford McCarty Commercial Real Estate
Note: Value based upon $100,000 in annual net income

To illustrate the capitalization influence on valuation, let us assume a commercial building produces a net income to the investor of $100,000 per year. The declining market cap rates would correlate to the approximate purchase prices according to the following years:



Final Words—Turning a Corner

In summation, the signs of recovery are reaching our area and the commercial real estate market is improving, although slowly. The data from our region demonstrates that properties are starting to sell but are still below reproduction values, and nowhere close to previous high water marks. Data from other parts of the state, the San Francisco Bay Area, and the coastal side of Southern California, indicate a market recovering more quickly. Historically the Central Coast region has lagged them.

There is demand for new construction in certain markets and sectors, but rents for these newly constructed properties are higher than rents for existing buildings, as rents are down in today's market. The exchange market is bringing out buyers for commercial properties. Banks are cautiously lending, but those buyers with cash are still able to command the best deals in the market. All in all there is reason for optimism.

Demographics and Quality of Life

by Vedran Kaluderovic

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Key Chapter Findings

- San Luis Obispo County reached 270,000 residents with increasing diversity.
- Population remains one of the oldest, compared to nearby regions.
- The county still is one of the most attractive places to live.
- Uncertainty over public education exists, but passage of Props. 30 or 38 could help.

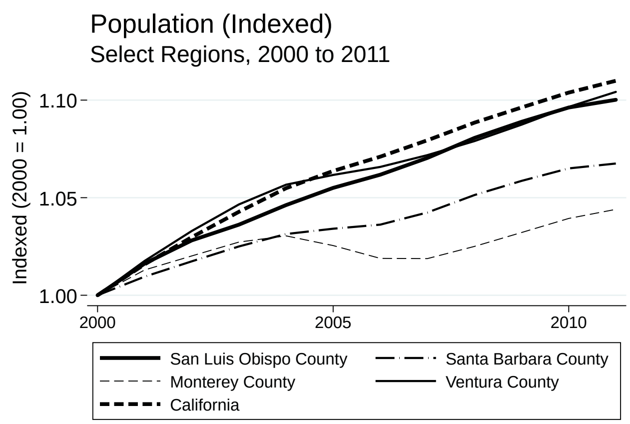
Overview

Despite the slowing in net migration, San Luis Obispo County still remains a very attractive place to live. The incomes are rising as the population is furthering their education. Crime rates remain low while dependence on social services is decreasing. The primary and secondary public education system is doing quite well.

There is some uncertainty over the future of the public education system. The outcome of Proposition 30 and 38 could have a significant impact on K-12 and tertiary education. The performance of K-12 schools could potentially reverse course with additional budget issues. Cuesta College is contemplating program cuts while Cal Poly students could face additional tuition hikes.

Population and Housing Statistics

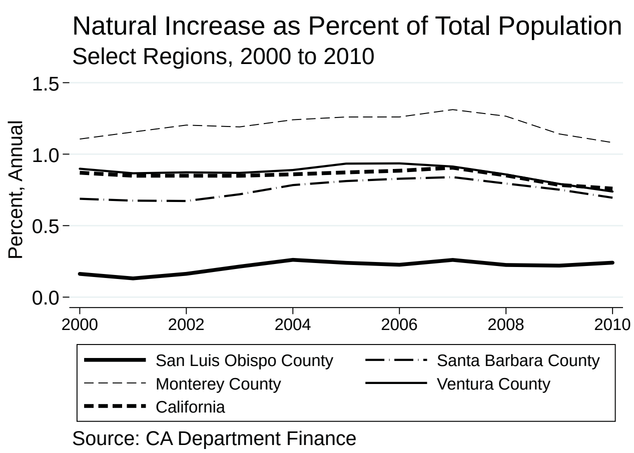
According to the California Department of Finance, the population of San Luis Obispo County recently surpassed 270,000 residents. The increase in population in the county since 2000 has been on par with increases in California and Ventura County, at approximately 10%, while the county experienced faster growth than two neighboring coastal counties, Monterey and Santa Barbara.

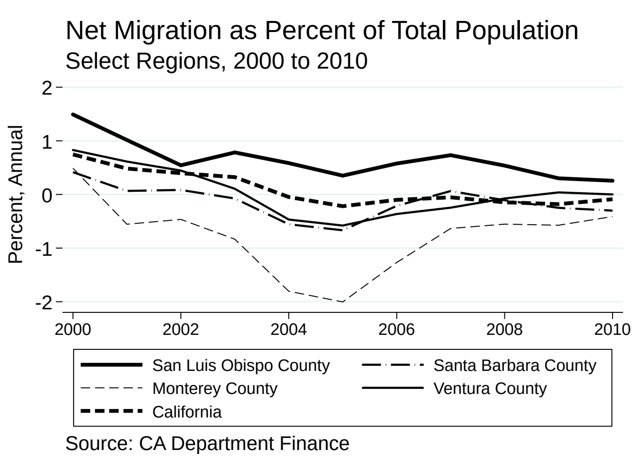


Source: CA Department Finance

Population can increase in two ways: through natural increase or net positive migration. Natural increase is the difference between the number of deaths and the number of births, assuming the latter exceeds the former. Since 2000, the rate of natural increase has remained relatively flat in the county, at about a quarter of a percent. This means that natural increase is, on average, responsible for a quarter of a percentage point increase in population every year. Compared with nearby coastal counties and the state, San Luis Obispo has a relatively low rate of natural increase. California, Ventura County, and Santa Barbara County, all post rates of about 0.75%, while Monterey County has been experiencing a rate of over 1%. The reason San Luis Obispo County has a lower natural increase rate is because the birth rate is lower compared with the other regions, while the death rate is higher.

The birth rate of a county can be affected by the age structure of the population, the race and ethnicity of its residents, household economic characteristics, and levels of educational attainment. The death rate can be affected by the age structure of the population and the health of the population. The most notable difference between San Luis Obispo County and the comparison regions is the age structure of the population. Because the age structure affects both the birth rate and the death rate, it has a significant impact on the rate of natural increase. According to the 2011 American Community Survey, as compiled by the U.S. Census Bureau, the median age of the population in San Luis Obispo County is 40.3 years, compared with 36.5 years in Ventura County, 35.4 years in California, 33 years in Santa Barbara County, and 32.8 years in Monterey County.





Furthermore, the U.S. Census Bureau decennial survey shows that the number of households with children has decreased from 28.2% in 2000 to 24.5% in 2010, although the number of households grew at the same pace as the population. The proportion of households with children is lower in San Luis Obispo than in our comparison regions. On average, 33% of households in the state have children under the age of 18. In Monterey County, approximately 36.5% of households have children under 18 years of age, in keeping with the county's relatively high birth rate.

San Luis Obispo County statistics suggest that some of the county's older population has moved beyond childbearing years, while the share of others in the older age group might be decreasing. If we dig deeper into the age breakdown of the county, we can potentially determine whether the latter scenario is also present in the county. We are assuming that women of childbearing years tend to be between the ages of 20 and 44. All residents in this age group held a 36% share of the population in 2000, but the proportion declined to 33% in 2010. This implies that the decline in households with children could be attributed to the decline in residents ages 20 to 44. The decline in the share of the population between the ages of 20 and 44 could potentially reduce the birth rate in the future .

Net migration has been a bright spot for San Luis Obispo County. The area has remained attractive for both domestic and international migrants. San Luis Obispo County—unlike Santa Barbara, Monterey, Ventura, and the state overall—has yet to experience negative net domestic migration. That is, more people within the United States choose to move to the county than to move out of the county. However, this could change in the near future, as net domestic migration is approaching zero.

Although the trend in international migration has slowed, net international migration is still a contributor to San Luis Obispo County's population growth. In contrast, neighboring regions are depending solely

Households and Population By Age

	Households with Own Children Under 18			Population Under 18			Population Over 18			Population Over 62		
	2000	2010	Change	2000	2010	Change	2000	2010	Change	2000	2010	Change
Monterey County	39.1	36.5	-2.6	28.4	26.7	-1.7	71.6	73.3	1.7	11.8	13.4	1.6
San Luis Obispo County	28.2	24.5	-3.7	21.7	18.9	-2.8	78.3	81.1	2.8	16.7	18.8	2.1
Santa Barbara County	32.4	29.8	-2.6	24.9	23.1	-1.8	75.1	76.9	1.8	14.8	15.6	0.8
Ventura County	39.7	35.2	-4.5	28.4	25.7	-2.7	71.6	74.3	2.7	12.2	14.6	2.4
California	35.8	33	-2.8	27.3	25	-2.3	72.7	75	2.3	12.6	14.2	1.6

Source: U.S. Census Bureau

on birth rates to exceed death rates for the population to grow. For example, while the population in California is, in fact, growing, more residents are leaving the state than coming into the state.

The influences on net migration are varied, including the performance of the local economy, levels of affordability, and the quality of life.

San Luis Obispo County Becomes More Diverse

The ethnic and racial composition of California has changed over time. The most notable change has been an increase in the Hispanic population. San Luis Obispo County has experienced a similar change, but at a slower pace. As of 2010, the Hispanic population in the state was approximately 37.6% of the total population, or a 5 percentage point increase from 2000. Of our comparison regions, Santa Barbara County experienced the largest increase in its share of Hispanic residents, with an increase of nearly 9 percentage points. The share of the Hispanic population in San Luis Obispo County increased by 4.5 percentage points, for a share of approximately 21% of the total population.

The county's non-Hispanic white population has decreased by 5 percentage points, to 71.1%. This was the smallest percentage point decline among the neighboring counties, and the county still has the largest proportion of non-Hispanic white residents. Monterey County has the lowest proportion of non-Hispanic white residents, at 32.9%, while the state average is around 40%. The Asian and black populations in San Luis Obispo County have increased by half a percentage point or less.

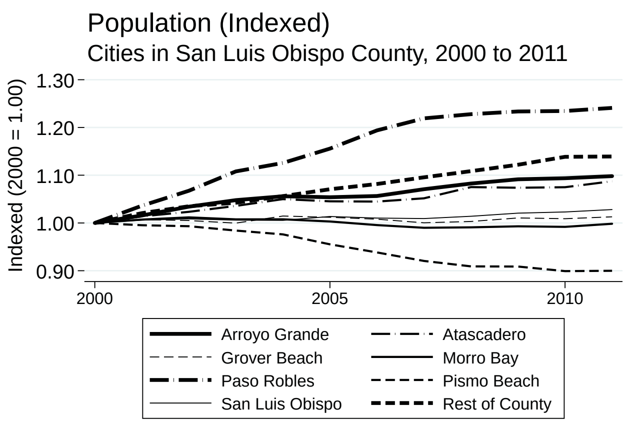
Paso Robles Becomes the Second-Largest City in the County

San Luis Obispo County as a whole has seen an approximately 10% increase in its population since 2000, but the growth in the county has not been evenly distributed among cities. Pismo Beach is the only city in the county that experienced a population decline. Since 2000, the number of residents in the city shrank by nearly 10%. The populations of Grover Beach, Morro Bay, and the City of San Luis Obispo have remained more or less flat. Atascadero, Arroyo Grande, and the unincorporated area of the county grew by around 10% since 2000. Finally, the population growth story of the county is Paso Robles. The city increased its population by nearly 25% and overtook Atascadero as the second- largest city in the county. Interestingly, the population growth in Paso Robles and the unincorporated area accounted for nearly 90% of the total population growth in San Luis Obispo County.

Ethnic Composition by Select County and California, 2000–2010

	White			Hispanic			Asian			African American		
	2000	2010	Change	2000	2010	Change	2000	2010	Change	2000	2010	Change
Monterey County	40.3	32.9	-7.4	46.8	55.4	8.6	6	6.1	0.1	3.7	3.1	-0.6
San Luis Obispo County	76.1	71.1	-5	16.3	20.8	4.5	2.7	3.2	0.5	2	2.1	0.1
Santa Barbara County	56.9	47.9	-9	34.2	42.9	8.7	4.1	4.9	0.8	2.3	2	-0.3
Ventura County	56.8	48.7	-8.1	33.4	40.3	6.9	5.3	6.7	1.4	1.9	1.8	-0.1
California	46.7	40.1	-6.6	32.4	37.6	5.2	10.9	13	2.1	6.7	6.2	-0.5

Source: U.S. Census Bureau



Source: CA Department Finance

The affordability of a county can boost inflows to the region. Although migration data on the city level is not available, perhaps some residents of Pismo Beach chose to relocate to Arroyo Grande due to lower home prices. The most recent statistics compiled by Zillow show that homes in Arroyo Grande are selling at nearly a 20% discount compared to Pismo Beach.

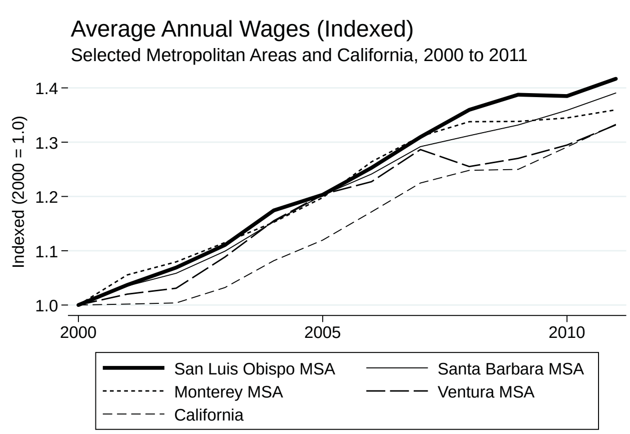
Population growth in Paso Robles could also be attributed to relatively more affordable housing and the performance of the local economy. Ever since Paso Robles Wine Country was designated an American Viticultural Area in 1983, tourism and wine production has seen impressive growth, which may have attracted new residents.

Cities in San Luis Obispo County have seen a similar pattern when it comes to increased diversity. The Hispanic population in Paso Robles had the largest increase in share, at nearly 7 percentage points, between 2000 and 2010. Shares of the Hispanic populations in Grover Beach and Atascadero grew in excess of 5 percentage points. The smallest growth was seen in Pismo Beach and San Luis Obispo.

On a similar note, the share of white residents has decreased in all cities in the county; the largest drop was in Grover Beach, where the white population decreased by nearly 7 percentage points. Shares of Asian and black residents have seen a small increase in some cities and in the county overall.

Income/Affordability in San Luis Obispo

As mentioned earlier, the rate of net migration is influenced by the performance of the local economy, the county's level of affordability, and the quality of life. San Luis Obispo has done quite well in these areas, providing incentives for residents to move to the county and stay.



Source: U.S. Bureau of Labor Statistics

Personal income from wages has increased faster in San Luis Obispo County than in neighboring regions.

Ethnic Composition by City, 2000–2010

	White			Hispanic			Asian			African American		
	2000	2010	Change	2000	2010	Change	2000	2010	Change	2000	2010	Change
Arroyo Grande	82.7	76.9	-5.8	11.2	15.7	4.5	3.1	3.4	0.3	0.6	0.9	0.3
Atascadero	82.7	76.8	-5.9	10.5	15.6	5.1	1.3	2.4	1.1	2.4	2.1	-0.3
Grover Beach	69.1	62.3	-6.8	22.5	29.2	6.7	3.7	4.1	0.4	1	1.1	0.1
Morro Bay	83.4	79.4	-4	11.4	14.9	3.5	1.8	2.5	0.7	0.7	0.4	-0.3
Paso Robles	64.2	59.1	-5.1	27.7	34.5	6.8	1.9	2	0.1	3.3	2.1	-1.2
Pismo Beach	87.1	85	-2.1	6.9	9.3	2.4	2.9	2.7	-0.2	.6	.7	0.1
San Luis Obispo	78.7	75.8	-2.9	11.7	14.7	3	5.3	5.2	-0.1	1.5	1.2	-0.3
San Luis Obispo County	76.1	71.1	-5	16.3	20.8	4.5	2.7	3.2	0.5	2	2.1	0.1

Source: U.S. Census Bureau

Although the level of wages in the county is the lowest of the regions, growth in wages since 2000 has been slightly over 40% (not adjusted for inflation). Educational attainment is strongly correlated with income, and in this regard, San Luis Obispo has also led its neighboring counties in improvement. The share of residents with a graduate or professional degree increased by more than 3.5 percentage points between 2000 and 2011.

According to the 2000 census, 26.7% of San Luis Obispo County residents had earned a bachelor's degree or higher. At the time, this was smaller than the shares observed in Santa Barbara County and the state. Since then, the county has gained ground. As of 2011, almost 31% of residents had a bachelor's degree or higher, a proportion equivalent to that of Ventura County and larger than the shares observed in Santa Barbara County, Monterey County, and the state overall. The improvements in educational attainment are a great sign for the county and should continue to pull incomes higher in the future. Median income in the county for a person with a graduate or professional degree is a little over $61,000, which is 44% higher than the income for people with a bachelor's degree only and 90% higher than income for people with some college completed.

One way to look at affordability is to compare home prices between various areas. Some have argued that residents from the Bay Area and from Southern California have been drawn to the Central Coast over the years because of the region's affordability. San Luis Obispo home prices appear relatively attractive compared to prices in the more populated counties in the north and south. Of the select counties, Los Angeles County is the only region where median home prices have been at a discount compared to San Luis Obispo County. However, residents of Los Angeles County most likely have different reasons for relocation, such as the desire to escape congestion and to live near high-quality public schools.

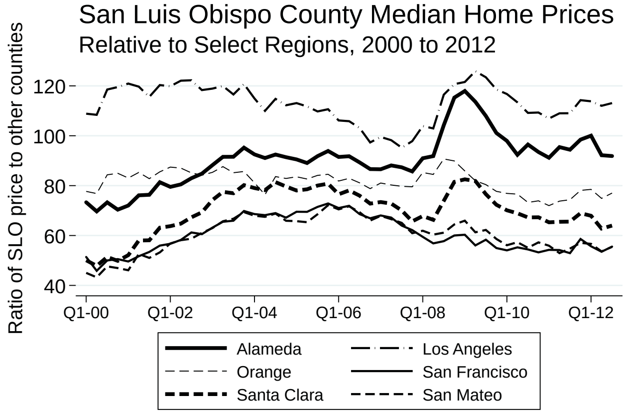
Residents of Bay Area counties on average pay a relatively large premium for homes relative to prices in San Luis Obispo County, which may have prompted some residents to migrate south. Furthermore, the premium for living in the Bay Area or in Orange County has been increasing since the end of the Great Recession. The premium is most likely increasing because median home prices are increasing faster in those areas. If the trend continues, San Luis Obispo County could see an increase in net domestic migration in the future.

Educational Attainment by Selected County, 2000–2011

	San Luis Obispo			Santa Barbara			Ventura			Monterey		
	2000	2011	Change	2000	2011	Change	2000	2011	Change	2000	2011	Change
No High School Grad.	14.4	12	-2.5	17.9	20.4	2.5	18.7	18	-0.8	27.2	28.5	1.4
High School Grad.	21.8	21.8	0	19.4	18.6	-0.8	19.6	18.8	-0.8	19	21	2
Some College	37.1	35.4	-1.6	32.3	31.2	-1	35.7	32.5	-3.2	28.8	27.8	-1
Bachelor's Degree	17.4	17.9	0.5	18.5	17.5	-1	17.1	19.4	2.3	17.7	13.9	-3.8
Grad. or Prof. Degree	9.3	13	3.6	12	12.3	0.3	8.9	11.4	2.5	7.4	8.9	1.5

Source: U.S. Census Bureau; American Community Survey

San Luis Obispo County Median Home Prices
Relative to Select Regions, 2000 to 2012



Source: DataQuick

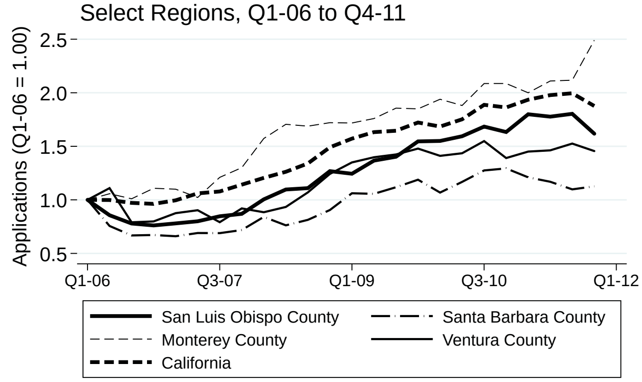
A Brighter Future for the Less Fortunate

Changes in the county's poverty rates and in the usage of social services reflect shifts in the standard of living in the region. As in most areas, the poverty rate in San Luis Obispo County has been increasing since the start of the Great Recession. According to the 2011 American Community Survey, the poverty rate for all residents in San Luis Obispo County ticked up nearly a percentage point, to 15.3%. This is below both the state average (16.6%) and the rate in Monterey County (17.4%). The poverty rate in Santa Barbara fell to the level observed in San Luis Obispo County. To fall below the poverty line an individual under 65 must earn less than $11,344 annually; an individual over 65 must earn less than $10,458.

The uptick in the poverty rate could stem from the dearth in the number of jobs being added in the low-paying sectors. It's possible that the improving employment situation is benefiting skilled workers. In addition, there could be a lag between survey methodology and reality. For example, perhaps the survey answers were based on 2010 incomes which saw more drastic jobs cuts and a worse economic picture, hence the higher unemployment rate in 2010. We expect the poverty rate to decrease in the near future due to the improving employment situation. As of September of 2012, the unemployment rate for the county stood at 7.4%.

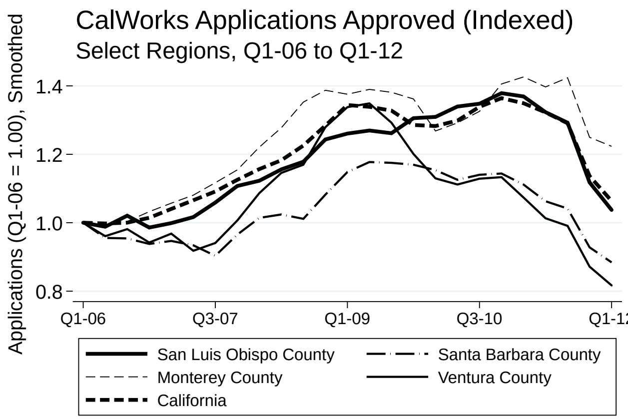
Examining the usage of social service benefits gives us another indication of whether the poverty rate should decrease in the near future. The number of approved applicants for CalFresh, California's arm of the U.S. Supplemental Nutrition Assistance Program, has slightly decreased since the peak in mid-2011. Currently, the level of approved applicants remains nearly 50% higher than it was prior to the recession.

CalFresh Applications Approved (Indexed)
Select Regions, Q1-06 to Q4-11



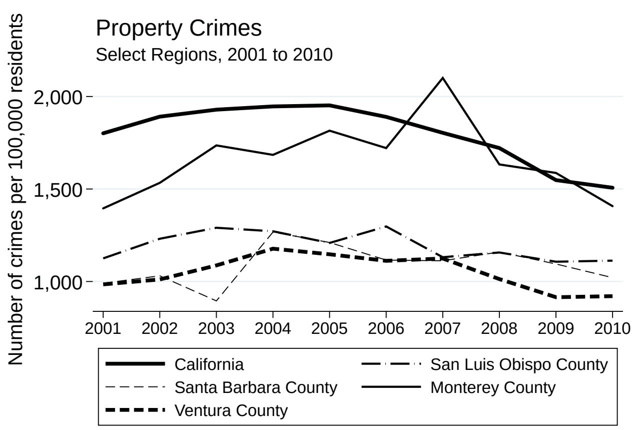
Source: CA Department of Social Services

The number of approved applicants for CalWorks (California's cash assistance program for needy families) has sharply decreased since 2011. The number of approvals is approaching the pre-recession level.

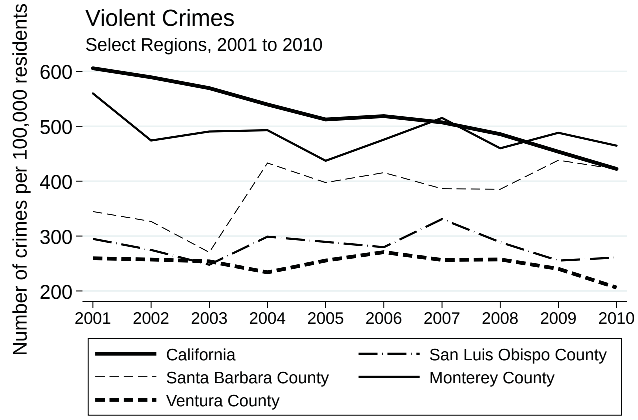


Source: CA Department of Social Services

Relatively low crime rates in San Luis Obispo County attract many residents to the area. Property and violent crime rates have remained relatively flat. Crime rates in the county are on par with those in Ventura County, which is considered one of the safest counties in the state. The level of violent crime has increased in Santa Barbara County, in line with levels in Monterey County and the state overall.



Source: CA Department of Justice



Source: CA Department of Justice

An Uncertain Future for Education

The quality of education in San Luis Obispo County is another pull for residents thinking of moving to the region. High school graduation rates in the county remain well above the state average by nearly 9 percentage points. As of 2010, nearly 90% of all high school students graduated, significantly higher than the state's average of 80.5%.

Recently, the Department of Education in California released the 2012 Academic Performance Index levels (API). Although not a perfect measure of student achievement, API scores serve as useful guidelines. API scores range from 200 to 1,000 and are calculated using the STAR (Standardized Testing and Reporting) test results and California High School Exit Exam (CAHSEE) scores. The API goal for the state is for schools to be at the 800 level. Currently, the state average API score is 788. Furthermore, the state sets API growth targets for each student group and schools attempt to reach them every year.

In 2012, approximately 80% of San Luis Obispo County schools hit their API growth target. The largest improvement in API scores was seen in Shandon Joint Unified, where the score increased by 6.2%. According to the API reports, this is the district with lowest scores so a 6.2% increase is encouraging. Lucia Mar

Unified was the only school district that had a decrease in scores. The decrease was very small (1%) and its API score of 813 is still above the state average.

Templeton Unified was the best-performing school district, with an API score of 859. Since 2011, Templeton's score has increased by 0.6%, with improved scores observed across all student groups in all but one school. The school with the highest API score is Teach Elementary in San Luis Obispo. Although this is a very small school with only 115 students and four teachers, its score of 975 puts the school in the top 10% of all California schools. The best-performing high school is Templeton High, with an API score of 851. This score puts Templeton High in the top 20% of all California schools.

These are clearly good signs for the primary and secondary education system in the county. However, the future is uncertain. The outcome of the November election could have a profound impact on the education system. The ballot in California includes Proposition 30 and Proposition 38, both of which argue for higher taxes to support the education system in California. Failure to pass one of the propositions (they are mutually exclusive) would put a dent in education all over the state, not just in San Luis Obispo County.

Primary and secondary schools are not alone in feeling uncertainty about the future. Cuesta College is contemplating cutting up to 29 programs (out of 70) due to budget constraints[30], while Cal Poly might face another tuition hike[31]. Again, the decisions of both schools will be made after the November election, pending the results of the vote on Proposition 30 and Proposition 38.

[30]Connie Tran, "Cuesta College Faces Program Cuts," KCBY.com, Oct 19, 2012, http://www.ksby.com/news/cuesta-college-faces-program-cuts/.

[31]Cynthia Lambert and AnnMarie Cornejo, "Battle Lines are Drawn on Proposition 30," The Tribune, Oct 20, 2012, http://www.sanluisobispo.com/2012/10/20/2269341/battle-lines-proposition-30-obispo.html.

High School Graduation Rates by School District, 2006 - 2010

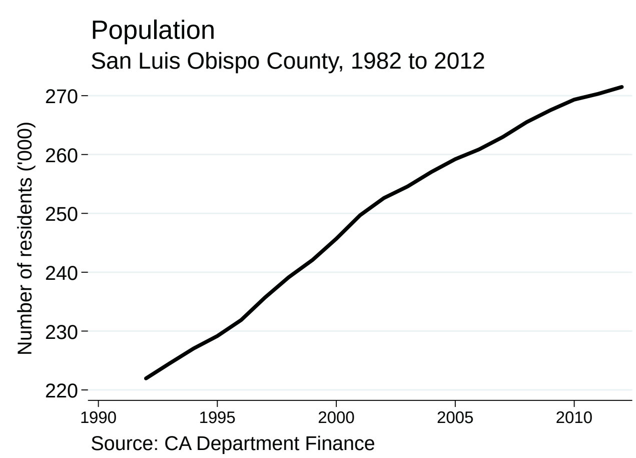
	2006	2007	2008	2009	2010
Atascadero Unified	88	91.2	92.7	91.7	93.9
Coast Unified	96.4	91.9	87.4	93.5	92.2
Lucia Mar Unified	89.4	92.8	90.7	90.2	91.1
Paso Robles Joint Unified	87.2	84.8	84.6	78.2	87.2
San Luis Coastal Unified	93.7	96.9	96.4	95.2	96.4
Shandon Joint Unified	92.9	100	82.4	100	96.2
Templeton Unified	94.5	90.8	92.6	97.6	97.4
San Luis Obispo County	87.4	88.5	87.7	86.2	89.3
California	83.4	80.6	80.2	78.5	80.5

Source: CA Department of Education

Summary

The population of the county has recently reached 270,000, with growth coming from a natural increase and migration. As net migration approaches zero, the county will depend on birth rates to be higher than death rates for population growth.

Despite the change in net migration trends, the county still remains one of the most attractive places to live. The wages in the county are increasing as the population improves their education level and the economy gains traction. In addition, home prices remain affordable compared to the more populated areas in the Bay Area and Southern California. It appears that the situation is improving for the less fortunate residents, as seen by the change in trend in social services applications. As a result, we should expect the poverty rate to decrease in the near future.

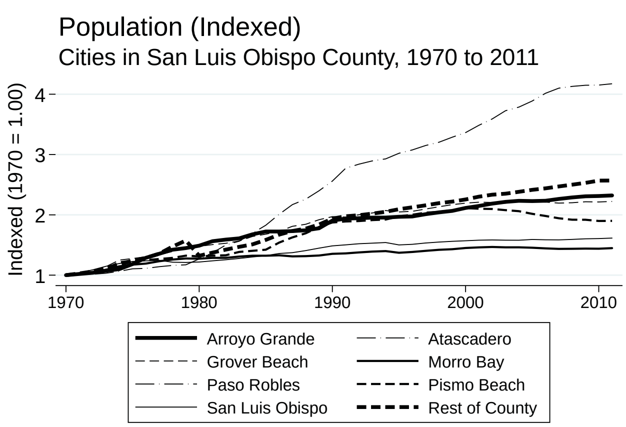


Population Growth in Select California Counties, 2010 and 2011

County	Census 2010	Census 2011	Census Growth Rate (%)	Dept. of Finance 2010	Dept. of Finance 2011	Dept. of Finance Growth Rate (%)
Riverside	2,202,978	2,239,620	1.66	2,191,800	2,226,552	1.59
Monterey	416,366	421,898	1.33	415,825	419,710	0.93
Santa Clara	1,786,267	1,809,378	1.29	1,787,553	1,805,861	1.02
Contra Costa	1,052,605	1,066,096	1.28	1,052,192	1,061,132	0.85
Orange	3,017,598	3,055,745	1.26	3,017,089	3,043,964	0.89
San Bernardino	2,042,027	2,065,377	1.14	2,038,771	2,059,630	1.02
San Diego	3,105,115	3,140,069	1.13	3,104,581	3,131,254	0.86
Alameda	1,513,043	1,529,875	1.11	1,513,493	1,525,655	0.80
San Mateo	719,604	727,209	1.06	719,582	725,245	0.79
Fresno	933,168	942,904	1.04	933,075	941,965	0.95
San Benito	55,520	56,072	0.99	55,350	55,684	0.60
Sacramento	1,422,094	1,436,105	0.99	1,420,447	1,430,537	0.71
Madera	151,468	152,925	0.96	151,160	152,281	0.74
San Francisco	805,340	812,826	0.93	807,177	814,088	0.86
Marin	252,789	255,031	0.89	252,767	254,114	0.53
Ventura	825,445	831,771	0.77	825,378	830,215	0.59
San Luis Obispo	270,112	271,969	0.69	269,333	270,305	0.36
Los Angeles	9,826,773	9,889,056	0.63	9,827,070	9,857,567	0.31
Santa Cruz	262,880	264,298	0.54	263,174	264,824	0.63
Santa Barbara	424,630	426,878	0.53	424,291	425,840	0.37

Source: U.S. Census Bureau, CA Department of Finance

The public education system is doing quite well. The most recent API scores indicate that 80% of all schools have reached the goal set by the state. Another encouraging point is that many schools saw an improved API scores for all student groups.



Source: CA Department of Finance

Population Change by City, 2010 - 2011

City	2010	2011	Change (%)
Arroyo Grande	17237	17306	0.40
Atascadero	28274	28601	1.16
Grover Beach	13147	13199	0.40
Morro Bay	10227	10294	0.66
Paso Robles	29761	29918	0.53
Pismo Beach	7676	7682	0.08
San Luis Obispo	45046	45269	0.50
Unincorporated	117965	118036	0.06
County Total	269333	270305	0.36

Source: CA Department of Finance

There is some cause for concern in the county. The outcomes of the election, more specifically Proposition 30 and 38, could have a significant effect on public education. Budget issues could put a dent in local school performance. Cuesta College is contemplating significantly reducing the number of programs offered while student at Cal Poly might be faced with another tuition hike.

Data Appendix

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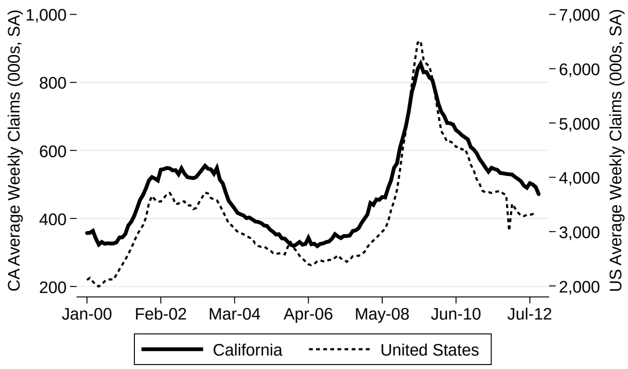
Employment

Continued Claims for Unemployment Insurance

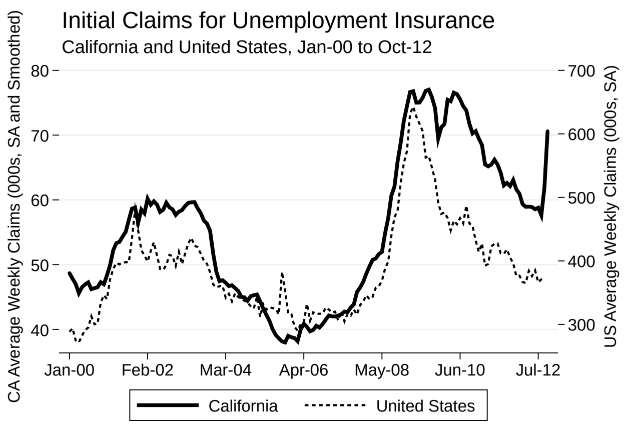
California and United States, Jan-00 to Oct-12



Source: U.S. Department of Labor

Initial Claims for Unemployment Insurance

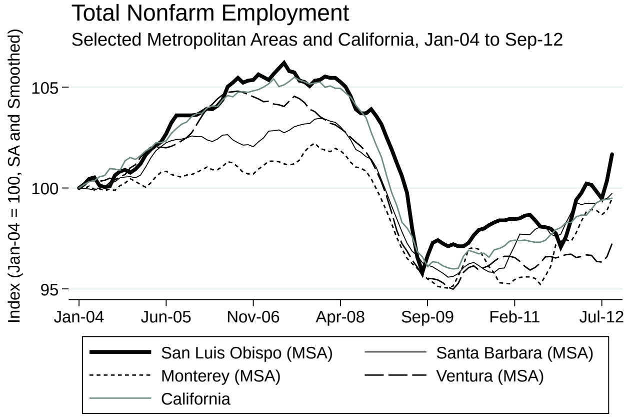
California and United States, Jan-00 to Oct-12



Source: U.S. Department of Labor

Total Nonfarm Employment

Selected Metropolitan Areas and California, Jan-04 to Sep-12



Source: California Employment Development Department

Unemployment Rates

Select Regions, Sep-10 to Sep-12 (%)

Area	Sep-10	Sep-11	Sep-12
Inland Empire	14.2	13.3	11.5
Los Angeles	12.8	12.4	10.6
Orange County	9.3	8.6	7.1
San Diego	10.5	10.0	8.4
East Bay	11.1	10.3	8.6
San Francisco	8.9	8.1	6.6
San Jose	11.0	9.7	8.1
Bakersfield	15.9	14.9	13.2
Fresno	17.2	17.0	14.8
Sacramento	12.5	11.8	9.9
Stockton	17.5	16.9	14.4
Monterey	12.8	12.5	10.9
San Luis Obispo	9.8	9.2	7.5
Santa Barbara	9.4	8.8	7.4
Ventura	10.7	10.0	8.7
California	12.4	11.7	10.2

Source: California EDD

Average Annual Wages by Industry

State of California, Select Years ($)

Industry	2006	2010	2011
Agriculture	22,278	24,642	25,425
Natural Resources & Mining	98,143	129,716	128,533
Construction	48,338	54,855	56,145
Manufacturing	63,041	72,563	74,878
Wholesale Trade	59,433	64,325	66,811
Retail Trade	29,922	30,870	31,549
Information	87,472	99,934	106,018
Finance & Insurance	87,168	92,275	95,657
Real Estate, Rental, & Leasing	48,180	48,611	51,303
Professional & Technical Svcs.	77,604	89,571	93,357
Management of Co. & Ent.	83,944	94,255	100,562
Administrative & Waste Svcs.	31,917	36,499	37,743
Educational Svcs.	37,771	44,437	45,482
Health Care	46,056	52,365	53,470
Arts, Entertainment, & Rec.	46,083	49,455	51,553
Accommodations & Food Svcs.	17,437	19,002	19,434
Other Services	24,384	25,918	26,208
Government	61,072	66,865	69,580
Total All Industries	48,344	53,268	55,001

Source: U.S. Bureau of Labor Statistics

Total Nonfarm Employment and Annualized Change
Selected Areas and California, Sep-07 to Sep-12

Area	Sep-07 (000s)	5-Year Ann. % Chg.	Year-Over-Year Chg.	3-Month Ann. % Chg.	Sep-12 (000s)
Monterey (MSA)	128.9	−0.4	2.9	2.6	126.1
San Luis Obispo (MSA)	103.5	−0.6	3.4	11.1	100.3
Santa Barbara (MSA)	173.4	−0.6	2.1	0.7	168.1
California	15,179.7	−1.1	1.9	0.9	14,347.9
Ventura (MSA)	296.2	−1.3	0.5	3.2	277.1

Source: California Employment Development Department

San Luis Obispo MSA Employment by Industry and Annualized Change
San Luis Obispo MSA, Sep-07 to Sep-12

Industry	Sep-07 (000s)	5-Year Ann. % Chg.	Year-Over-Year Chg.	3-Month Ann. % Chg.	Sep-12 (000s)
Agriculture	4.4	1.4	−6.1	−11.8	4.7
Manufacturing	6.1	−2.6	−6.2	−8.8	5.4
Wholesale Trade	2.7	0.1	4.4	9.7	2.7
Retail Trade	14.1	−0.4	4.3	13.5	13.9
Trans., Warehouse, & Util.	4.1	−2.2	6.1	14.4	3.7
Information	1.4	−3.3	0.4	5.5	1.2
Financial Activities	4.4	−1.1	8.2	14.8	4.2
Arts & Entertainment	1.5	−0.1	7.9	−1.4	1.5
Accommodations & Food	14.2	−0.1	7.2	18.8	14.2
Other Services	4.1	−1.2	−11.6	−7.4	3.9
Federal Government	0.7	−2.3	0.8	30.8	0.6
State Government	9.6	−0.9	−10.0	−12.6	9.2
Local Government	11.9	−1.6	6.4	27.8	11.0
Total Nonfarm	103.5	−0.6	3.4	11.1	100.3

Source: California Employment Development Department

California Employment by Industry and Annualized Change
State of California, Sep-07 to Sep-12

Industry	Sep-07 (000s)	5-Year Ann. % Chg.	Year-Over-Year Chg.	3-Month Ann. % Chg.	Sep-12 (000s)
Agriculture	382.6	0.1	−0.7	9.1	385.0
Construction	881.9	−8.2	4.7	−2.3	574.1
Nat. Res. & Mining	27.1	0.9	−0.4	−9.3	28.4
Durable Goods Mfg.	923.2	−3.5	−1.0	−2.6	771.0
Non-Durable Goods Mfg.	534.2	−2.7	−0.8	−2.9	466.8
Wholesale Trade	717.9	−1.2	2.1	0.1	676.7
Retail Trade	1,680.3	−1.5	1.3	−0.4	1,555.4
Transport. & Warehouse	451.9	−1.5	1.4	−1.7	418.7
Utilities	58.1	0.3	0.7	−0.2	59.1
Information	474.4	−0.8	6.0	3.9	456.4
Finance & Insurance	603.5	−2.6	2.2	3.5	527.8
Real Estate	283.3	−2.0	4.5	5.5	255.5
Prof. & Business Svcs.	2,264.0	−0.3	4.1	1.6	2,231.0
Education & Health Svcs.	1,693.7	2.3	3.1	4.6	1,901.5
Arts & Entertainment	252.7	−0.7	0.0	0.0	244.5
Accommodations & Food	1,314.3	0.6	4.9	7.2	1,355.2
Other Services	515.8	−1.4	−1.1	−2.2	481.0
Federal Government	246.7	0.4	−2.0	0.3	251.2
State Government	492.6	−0.4	1.1	0.0	481.8
Local Government	1,765.0	−1.8	−2.5	−3.9	1,612.0
Total Nonfarm	15,179.7	−1.1	1.9	0.9	14,347.9

Source: California Employment Development Department

Distribution of Employment by Industry
San Luis Obispo MSA and California, Sep-07 and Sep-12 (%)

Industry	Sep-07 San Luis Obispo MSA	Sep-07 California	Sep-12 San Luis Obispo MSA	Sep-12 California
Agriculture	4.1	2.5	4.5	2.6
Construction		5.7		3.9
Nat. Res. & Mining		0.2		0.2
Manufacturing	5.7	9.4	5.1	8.4
Wholesale Trade	2.5	4.6	2.6	4.6
Retail Trade	13.1	10.8	13.2	10.6
Trans., Warehouse, & Util.	3.8	3.3	3.5	3.2
Information	1.3	3.0	1.1	3.1
Financial Activities	4.1	5.7	4.0	5.3
Prof., Sci. & Tech Svcs.		6.9		7.5
Management of Co. & Ent.		1.3		1.4
Admin. & Support Svcs.		6.3		6.3
Educational Svcs.		1.9		2.4
Health Care		9.0		10.5
Arts & Entertainment	1.4	1.6	1.4	1.7
Accommodations & Food	13.2	8.4	13.5	9.2
Other Services	3.8	3.3	3.7	3.3
Federal Government	0.6	1.6	0.6	1.7
State Government	8.9	3.2	8.7	3.3
Local Government	11.0	11.3	10.5	10.9
Total Nonfarm	95.9	97.5	95.5	97.4

Source: California Employment Development Department

Business

Imports by Commodity
California Ports, 2012 YTD Through August ($ billions)

Commodity	Value
Electric Machinery	59.81
Industrial Machinery/Computers	56.37
Vehicles/Transport Equipment	31.13
Coal/Oil	24.60
Knit/Crochet Apparel	11.67
Furniture	10.24
Apparel (Not Knit)	10.02
Optic/Photo/Medical Equipment	9.56
Footwear	9.44
Toys/Games/Sport Equipment	7.52
Other Products	81.51

Source: WISER Trade

Exports by Commodity
California Ports, 2012 YTD through August ($ billions)

Commodity	Value
Electric Machinery	18.58
Industrial Machinery/Computers	18.57
Optic/Photo/Medical Equipment	10.98
Plastics	6.35
Vehicles/Transport Equipment	5.51
Aircraft/Spacecraft	4.77
Coal/Oil	4.55
Edible Fruits/Nuts	4.23
Precious Stones/Metals/Pearls	4.10
Meat	3.49
Other Products	47.01

Source: WISER Trade

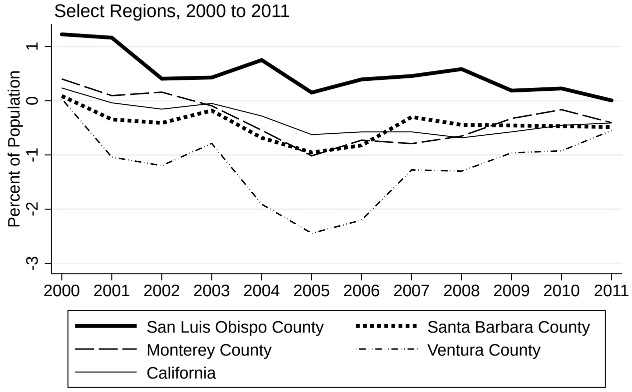
Real Taxable Sales Growth
San Luis Obispo MSA Cities,
Selected Counties and California, Q2-11 to Q2-12

	Taxable Sales			Taxable Sales Per Capita		
	Q2-11	Q2-12	Change (%)	Q2-11	Q2-12	Change (%)
Region	$ billions			$ per person		
San Luis Obispo	0.29	0.30	3.1	6,507	6,701	3.0
Paso Robles	0.17	0.18	7.3	5,660	6,011	6.2
Atascadero	0.07	0.07	0.4	2,481	2,503	0.9
Arroyo Grande	0.07	0.07	1.6	3,824	3,887	1.6
Pismo Beach	0.05	0.06	3.6	6,958	7,218	3.7
Morro Bay	0.03	0.04	17.8	2,995	3,534	18.0
Grover Beach	0.02	0.03	7.7	1,764	1,904	8.0
County	$ billions			$ per person		
San Luis Obispo	1.0	1.1	9.9	3,690	4,037	9.4
Monterey	1.3	1.4	5.3	3,152	3,291	4.4
Santa Barbara	1.4	1.5	6.1	3,370	3,553	5.5
Ventura	2.7	2.9	4.6	3,302	3,434	4.0
California	130.8	139.8	6.9	3,495	3,710	6.2

Sources: California Board of Equalization, Department of Finance

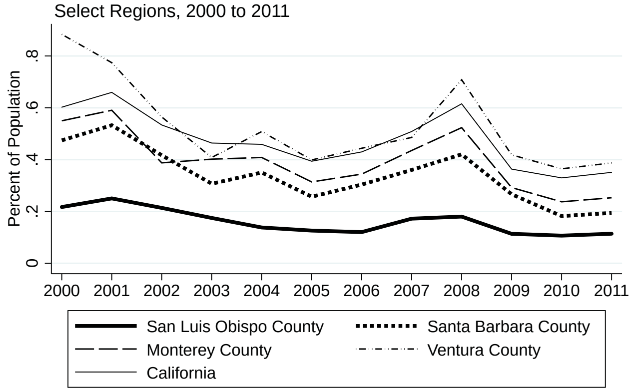
Demographics

Domestic Migration as a Share of Population
Select Regions, 2000 to 2011



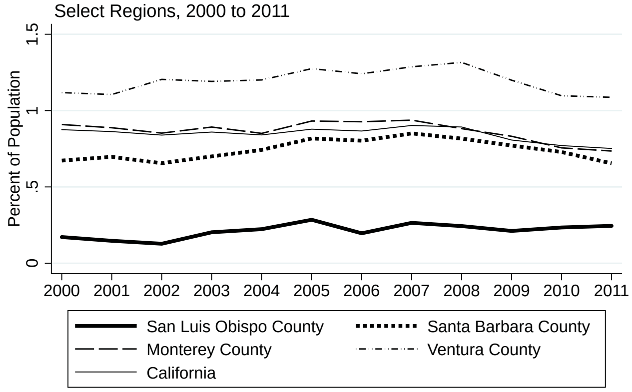
Source: California Department of Finance

International Migration as a Share of Population
Select Regions, 2000 to 2011



Source: California Department of Finance

Natural Increase as a Share of Population
Select Regions, 2000 to 2011



Source: California Department of Finance

Population by Age, 2011 (%)

Age Group	San Luis Obispo County	Santa Barbara County	Ventura County	Monterey County	California Overall
Under 5	4.9	6.4	6.6	7.9	6.7
Age 5 to 19	18.5	21.4	21.6	22.0	20.8
Age 20 to 34	22.1	24.0	19.9	23.0	21.9
Age 35 to 54	24.5	24.3	28.0	25.6	27.7
Age 55 to 64	14.4	10.8	11.8	10.7	11.2
Age 65 and Over	15.8	13.1	12.0	10.8	11.7

Source: U.S. Census Bureau, American Community Survey

Educational Attainment by Selected County, 2000–2011

	San Luis Obispo			Santa Barbara			Ventura			Monterey		
	2000	2011	Change	2000	2011	Change	2000	2011	Change	2000	2011	Change
No High School Grad.	14.4	12	-2.5	17.9	20.4	2.5	18.7	18	-0.8	27.2	28.5	1.4
High School Grad.	21.8	21.8	0	19.4	18.6	-0.8	19.6	18.8	-0.8	19	21	2
Some College	37.1	35.4	-1.6	32.3	31.2	-1	35.7	32.5	-3.2	28.8	27.8	-1
Bachelor's Degree	17.4	17.9	0.5	18.5	17.5	-1	17.1	19.4	2.3	17.7	13.9	-3.8
Grad. or Prof. Degree	9.3	13	3.6	12	12.3	0.3	8.9	11.4	2.5	7.4	8.9	1.5

Source: U.S. Census Bureau; American Community Survey

Population by Ethnicity, 2011 (%)

Ethnic Group	San Luis Obispo County	Santa Barbara County	Ventura County	Monterey County	California Overall
White	69.9	47.1	47.9	32.4	39.6
Hispanic/Latino	21.3	43.4	40.9	56.1	38.1
Asian	3.7	4.8	6.8	6.0	13.0
Black/Afr. American	2.2	1.6	1.7	2.8	5.7
Two or More Races	2.2	2.2	2.2	1.9	2.6
Amer. Indian/Alaska Native	0.4	0.6	0.2	0.3	0.4
Some Other Race	0.4	0.1	0.0	0.1	0.2
Native American/Pac. Islander	0.0	0.2	0.2	0.5	0.4

Source: U.S. Census Bureau, Census 2011

Population Characteristics, 2012

	San Luis Obispo County	Santa Barbara County	Ventura County	Monterey County	California Overall
Foreign Born (%)	10.5	22.8	23.0	30.8	27.2
Naturalized of the Foreign Born (%)	44.6	34.4	45.0	27.3	46.8
Homeownership Rate (%)	56.1	50.7	65.4	47.4	54.9
Occupied Units (%)	86.1	92.2	94.0	89.2	90.9
Renter-Occupied (%)	43.9	49.3	34.6	52.6	45.1
Vacancy Rate (%)	13.9	7.8	6.0	10.8	9.1
Household Size (Persons Per Household):					
Total	2.5	2.9	3.1	3.2	3.0
Owner-Occupied	2.5	2.8	3.1	3.0	3.0
Renter-Occupied	2.6	3.1	3.1	3.4	2.9
Transportation to Work (%):					
Drive Alone	72.4	66.8	75.4	69.6	73.3
Carpool	9.2	14.9	13.3	12.6	11.1
Public Transit	1.4	3.3	1.4	2.0	5.2
Motorcycle, Bicycle, Taxi	4.1	5.1	2.0	7.5	2.4
Walk	4.7	4.0	1.9	3.7	2.8
Work at Home	8.2	5.9	6.0	4.6	5.3

Source: U.S. Census Bureau, American Community Survey

Median Earnings by Educational Attainment, 2011 ($)

County	Less than High Sch.	High Sch. Grad.	Some College	Bach. Degree	Grad./Prof. Degree
No HS Diploma or Equivalency	22, 320	18, 968	17, 501	15, 800	18, 261
High School Graduate	24, 919	27, 605	27, 186	23, 589	26, 941
Some College	32, 262	33, 726	38, 257	35, 454	35, 303
Bachelor's Degree	46, 531	54, 406	60, 639	51, 095	52, 824
Graduate or Professional Degree	61, 248	69, 360	81, 130	66, 561	76, 253

Source: U.S. Census Bureau, American Community Survey

Income Levels and Poverty, 2011

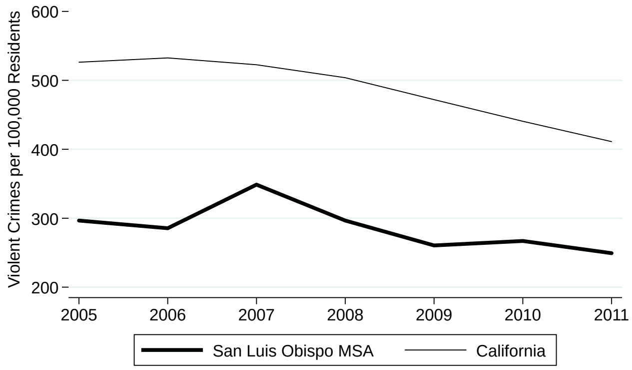
	San Luis Obispo County	Santa Barbara County	Ventura County	Monterey County	California
Median Household Income ($)	54,195	60,505	74,623	53,179	57,287
Number of Households	101,179	140,889	265,492	123,757	12,468,743
Under $25,000	24.6	20.0	15.9	20.7	22.1
$25,000 to $49,999	22.2	22.7	18.8	26.0	22.1
$50,000 to $74,999	16.8	17.2	15.5	18.7	16.9
$75,000 to $99,999	12.7	11.5	13.4	12.0	11.9
$100,000 to $149,999	15.3	14.9	19.5	13.0	14.2
$150,000 to $199,999	4.4	6.8	8.6	5.3	6.2
Over $200,000	3.9	6.9	8.3	4.3	6.5
Gini Index (0-1)	0.46	0.47	0.44	0.46	0.48
Poverty Rate (%)	15.3	15.1	11.3	17.4	16.6

Source: U.S. Census Bureau, American Community Survey

Quality of Life

Violent Crimes Per Year

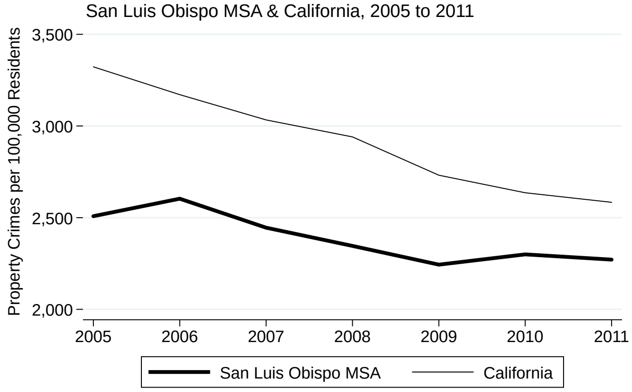
San Luis Obispo MSA & California, 2005 to 2011



Source: Federal Bureau of Investigation

Property Crimes Per Year

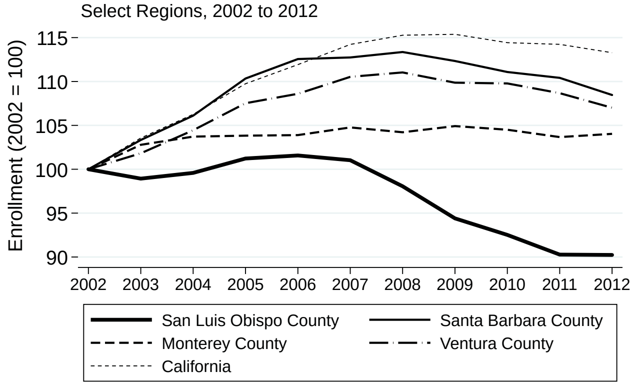
San Luis Obispo MSA & California, 2005 to 2011



Source: Federal Bureau of Investigation

Public High School Enrollment (Indexed)

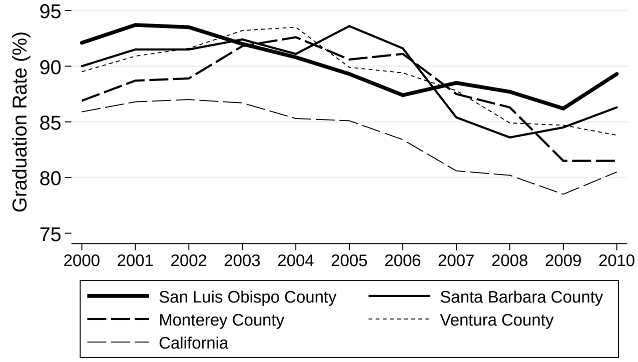
Select Regions, 2002 to 2012



Source: CA Department of Education

High School Graduation Rates

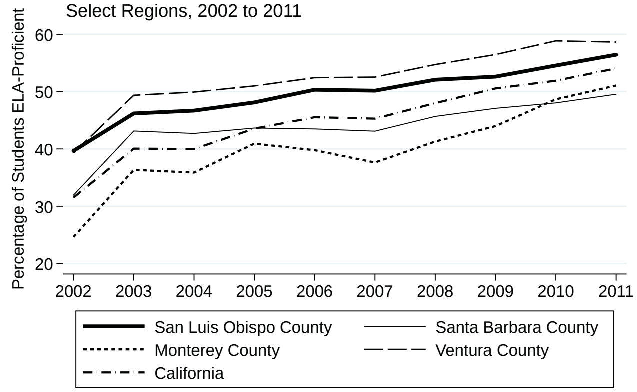
Select Regions, 2000 to 2010



Source: CA Department of Education

English-Language Arts Proficient Students

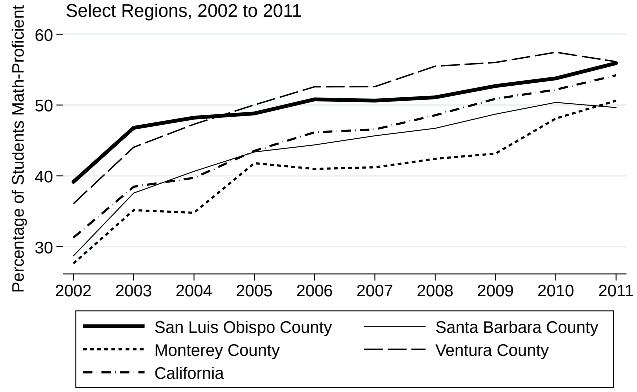
Select Regions, 2002 to 2011



Source: California Department of Education

Math Proficient Students

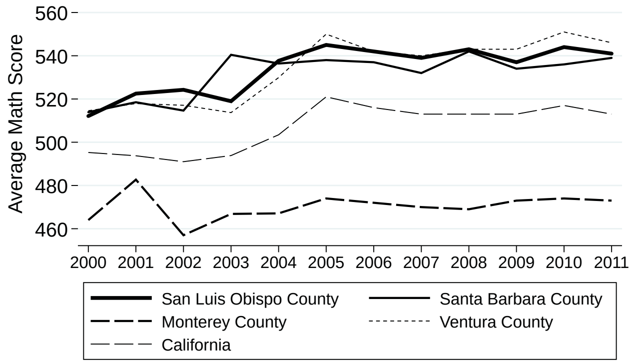
Select Regions, 2002 to 2011



Source: California Department of Education

SAT Math Scores

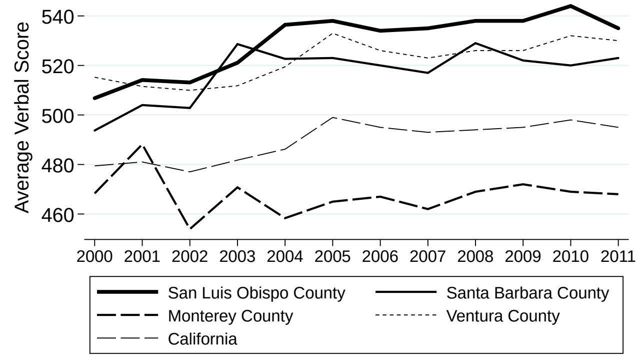
Select Regions, 2000 to 2011



Source: CA Department of Education

SAT Verbal Scores

Select Regions, 2000 to 2011



Source: CA Department of Education

Data Sources

The creation of this report would not have been possible without numerous public and private sources of data. We would like to acknowledge those sources here.

Bureau of Transportation Statistics

California Air Resources Board

California Association of Realtors

California Board of Equalization

California Dept. of Education

California Dept. of Finance

California Dept. of Justice

California Employment Development Dept.

California New Car Dealers Association

California State Controller

California State Franchise Tax Board

California State Legislative Analyst's Office

CB Richard Ellis

Central Coast Major Listing Service

Construction Industry Research Board

CoStarr/The London Group

DataQuick Information Systems

Federal Reserve Economic Data (FRED)

Fiserv Lending Solutions

Grubb & Ellis

Hanley Wood Market Intelligence

HousingTracker.net

Marcus & Millichap

Mortgage Bankers Association

National Science Foundation

NOAA National Weather Service

Property & Portfolio Research

RealFacts

Research and Development (RAND)

S&P Case Shiller

Texas Transportation Institute

U.S. Census Bureau, American Community Survey

U.S. Census Bureau, Longitudinal Employment - Housing Dynamics

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