



San Diego Economic Momentum Slowing in 2013

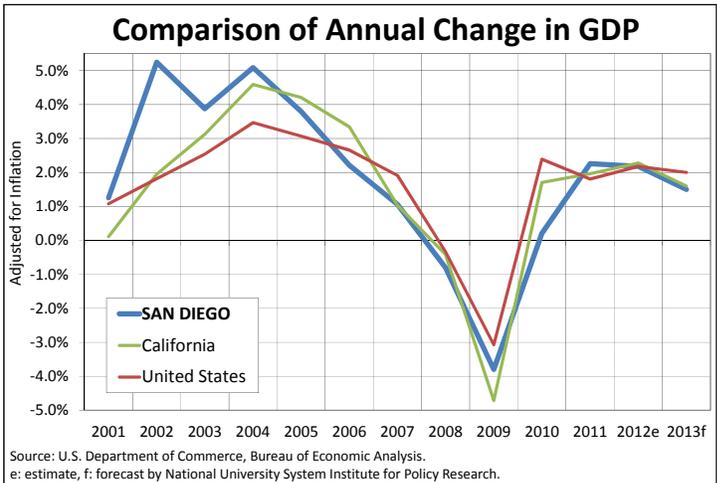
The San Diego economy continues to moderately grow despite multiple challenges along the road. Job creation remains largely subdued as the economy still struggles to mend and expand.

Although we anticipate the recovery will continue, the pace of improvement remains stubbornly sluggish. There is no reason to believe we will see an acceleration of growth in 2013 as drags remain from the national economy. Indeed, as

measured by GDP, we expect San Diego's growth to slow in 2013 as California's economic momentum lags the rest of the nation as well.

In regard to San Diego employment, 17,500 payroll jobs are projected to be added in 2013, less than the 18,900 added during 2012. In the fourth year of recovery, San Diego will only have replaced about one-half of the jobs lost during the "Great Recession".

Most local industries will



continue seeing some job exceptions in defense improvement, with notable based sectors. At least until

SELECTED SAN DIEGO COUNTY ECONOMIC INDICATORS

Indicator	Actual 2008	Actual 2009	Actual 2010	Actual 2011	Estimate 2012	Forecast 2013	Annual Percent Change				
							'09/'08	'10/'09	'11/'10	'12/'11e	'13/'12f
Gross Metropolitan Product (billions)	\$167.7	\$164.9	\$165.9	\$172.6	\$180.1	\$187.6	-1.7%	0.6%	4.0%	4.3%	4.2%
Inflation Adjusted Change+							-3.8%	0.2%	2.3%	2.2%	1.5%
Population*	3,064,436	3,091,579	3,115,810	3,143,429	3,165,429	3,187,729	0.89%	0.78%	0.89%	0.70%	0.70%
Change	31,747	27,143	24,231	27,619	22,000	22,300	-14.5%	-10.7%	14.0%	-20.3%	1.4%
Net Domestic Migration	-10,981	-10,662	-9,728	-4,726	-12,198	-12,000	-2.9%	-8.8%	-51.4%	158%	-1.6%
Net International Migration	15,129	11,861	8,249	7,945	9,998	10,500	-21.6%	-30.5%	-3.7%	26%	5.0%
Natural Increase	27,599	25,945	25,710	24,400	24,200	23,800	-6.0%	-0.9%	-5.1%	-0.8%	-1.7%
Employment											
Labor Force	1,548,300	1,554,200	1,572,600	1,583,800	1,597,300	1,623,000	0.4%	1.2%	0.7%	0.9%	1.6%
Employed	1,455,600	1,405,000	1,407,100	1,426,100	1,455,000	1,485,000	-3.5%	0.1%	1.4%	2.0%	2.1%
Unemployed	92,700	149,200	165,500	157,700	142,300	138,000	61%	10.9%	-4.7%	-9.8%	-3.0%
Unemployment Rate	6.0%	9.6%	10.5%	10.0%	8.9%	8.5%	3.6%	0.9%	-0.6%	-1.0%	-0.4%
Payroll Industry Employment	1,309,300	1,240,900	1,233,300	1,241,200	1,260,100	1,277,600	-5.2%	-0.6%	0.6%	1.5%	1.4%
Change	-10,400	-68,400	-7,600	7,900	18,900	17,500					
Construction											
Residential Units	5,157	2,946	3,494	5,370	5,750	6,500	-45.0%	18.6%	53.7%	7.1%	13.0%
Taxable Sales (billions)	\$45.3	\$39.7	\$41.6	\$44.6	\$48.0	\$50.2	-12.4%	4.8%	7.1%	7.6%	4.7%
Inflation Adjusted Change							-12.3%	3.4%	3.9%	5.9%	2.4%
Per Capita	\$14,792	\$12,851	\$13,359	\$14,176	\$15,148	\$15,749	-13.1%	4.0%	6.1%	6.9%	4.0%
Inflation Adjusted Change							-13.1%	2.6%	3.0%	5.2%	1.7%
Inflation Rate											
San Diego Consumer Price Index (CPI-U: 1982-84=100)	242.3	242.3	245.5	252.9	257.0	262.7	-0.02%	1.3%	3.0%	1.6%	2.2%

+Adjusted for inflation by Implicit Price Deflator for California. *Population as of January 1 of following year.

Sources: U.S. Department of Commerce, Bureau of Economic Analysis; California Department of Finance; California Employment Development Department; U.S. Bureau of Census; California Board of Equalization; U.S. Department of Labor, Bureau of Labor Statistics.

e: estimate, f: forecast by National University System Institute for Policy Research.

greater certainty emerges in respect to federal spending, it seems imprudent to predict anything better than San Diego's defense economy trading water in 2013.

As far as inflation, we expect it will remain somewhat muted. While inflation was reportedly 1.6 percent in 2012, in 2013 it will rise to 2.2 percent. Frustratingly, San Diego households will feel their budgets further squeezed by rising commodity, food, energy and gas prices.

The litany of factors associated with the "Great Recession"—deleveraging, collapse of residential housing market, weakening of financial institutions, and speeding up of fiscal reconvening facing the modern welfare state — are well-known and oft discussed. While we would agree that the economy is healing, it is at best a maddeningly slow recovery. Certainly not the kind of robust expansion we should be experiencing in the fourth year of recovery.

Slowing GDP outlook

The year 2013 begins with hopes of momentum accelerating and employment prospects rising. The year 2012 also began with such hopes for greater recovery. Job numbers jumped toward the middle of the year, but dwindled as the year progressed. The uncertainties of fiscal, monetary, and regulatory policies during an election year, with Congress locked in gridlock and "fiscal cliff" looming, served to diminish prospects of more vigorous economic expansion.

San Diego's gross domestic product (GDP), the most comprehensive measure of the local economy, reached an estimated \$180.1 billion in 2012. San Diego barely trailed the rest of California's economic growth as northern California was bolstered by thriving international technology companies, such as *Apple*, *Facebook*, and *Google*.

Economic momentum is estimated to have slowed in San Diego from 2.3 percent in 2011 to 2.2 percent during 2012. While San Diego slightly exceeded both California and U.S. gains in 2011, momentum faded somewhat in

SAN DIEGO GROSS DOMESTIC PRODUCT						
Year	GDP	Percent of		Constant Dollars*		
	(Billions)	Calif.	U.S.	S.D.	Cal.	U.S.
2001	\$114.472	8.54%	1.11%	1.3%	0.1%	1.1%
2002	\$123.271	8.89%	1.16%	5.2%	1.9%	1.8%
2003	\$131.025	8.97%	1.18%	3.9%	3.1%	2.5%
2004	\$141.495	9.01%	1.19%	5.1%	4.6%	3.5%
2005	\$151.388	8.96%	1.20%	3.8%	4.2%	3.1%
2006	\$159.582	8.87%	1.19%	2.2%	3.3%	2.7%
2007	\$166.019	8.87%	1.18%	1.1%	1.0%	1.9%
2008	\$167.732	8.83%	1.17%	-0.8%	-0.4%	-0.3%
2009	\$164.948	9.02%	1.18%	-3.8%	-4.7%	-3.1%
2010	\$165.912	8.84%	1.14%	0.2%	1.7%	2.4%
2011	\$172.583	8.81%	1.14%	2.3%	2.0%	1.8%
2012e	\$180.059	8.82%	1.15%	2.2%	2.3%	2.2%
2013f	\$187.644	8.83%	1.14%	1.5%	1.6%	2.0%

*Adjusted by GDP implicit price deflator. e: estimate f: forecast
 Source: Bureau of Economic Analysis, U.S. Department of Commerce; National University System Institute for Policy Research.

2012 as San Diego matched U.S. expansion and slightly trailed California.

The 2013 outlook for San Diego is further slowing to 1.5 percent, slightly lagging California's similarly tepid 1.6 percent growth. The forecast for the nation is somewhat better at 2.0 percent, the second highest expansion of the past six years, only exceeded in 2010 as the country began to emerge from recession.

California fell deeper into recession five years ago than the rest of the nation. The state has subsequently also lagged in recovery. The state's three tax revenue sources — personal income, sales and property, and corporate/franchise taxes — all experienced "massive" declines as Californians lost jobs and the housing bubble burst. State budget shortfalls, unfriendly business regulations, high business and wage earner tax rates, and "out-of-control" healthcare costs continue to stifle more vigorous economic expansion. Wages, housing, and new college graduates seeking employment continue to be constrained despite the economy recovering.

Increasing taxes in an attempt to accommodate budget gaps further drives wealth producers and business owners out of the state. Anticipated implementation of "cap and trade" for carbon dioxide emissions — essentially a massive tax and policy action that will generate even higher utility costs — adds yet another impetus for manufac-

turers, in particular, to head to friendlier states.

A study by the *Manhattan Institute* called "The Great California Exodus: A Closer Look" offers a sobering assessment of the state's fiscal problems. "For decades after World War II, California was a destination for Americans in search of a better life. In many people's minds, it was the state with more jobs, more space, more sunlight, and more opportunity. They voted with their feet, and California grew spectacularly (its population increased by 137 percent between 1960 and 2010). However, this golden age of migration into the state is

over. For the past two decades, California has been sending more people to other American states than it receives from them. Since 1990, the state has lost nearly 3.4 million residents through this migration."

As authors Tom Gray and Robert Scardamalia explain, "The data suggest that many cost drivers — taxes, regulations, the high price of housing and commercial real estate, costly electricity, union power, and high labor costs — are prompting businesses to locate outside California, thus helping to drive the exodus." Californians are fleeing "chronic economic adversity," congestion, and "constant fiscal instability" at state and local governmental levels, which "can be seen as tax hikes waiting to happen."¹

San Diego struggles by these same factors, only partially performing better in recent years because of the massive infusion of military and defense spending in the region. Some technology sectors also managed, for the most part, to perform relatively better. Despite this, migration nevertheless turned negative as well, moving away from San Diego in recent years.

Trends among San Diego industries

San Diego benefits from near perfect climate attracting an educated and talented labor force, with technically advanced research institutions and educational systems, and both active and retired military personnel, and generally thriving retirees. A core

strength is the well-diversified tech driven economy of telecommunications, biotech, computers, and electronics. Mixed in with popular travel destinations, international border, ocean front coastline, among extensive military base operations and affiliated industries, these assets generally provide economic resiliency.

Professional and business services and the health care sector have risen significantly relative to the total economy over the past decade. **Healthcare** continually led job gains growing even throughout the recession. Home to an expanding population of retirees, San Diego requires ever more health care services and health providers expanding facilities and services.

Government, including military base operations, directly contribute to 18 percent of San Diego's GDP. Contributions from government expenditures rose significantly over the past decade almost exclusively from the expansion of military spending, while state and local governments otherwise imposed budget austerity.

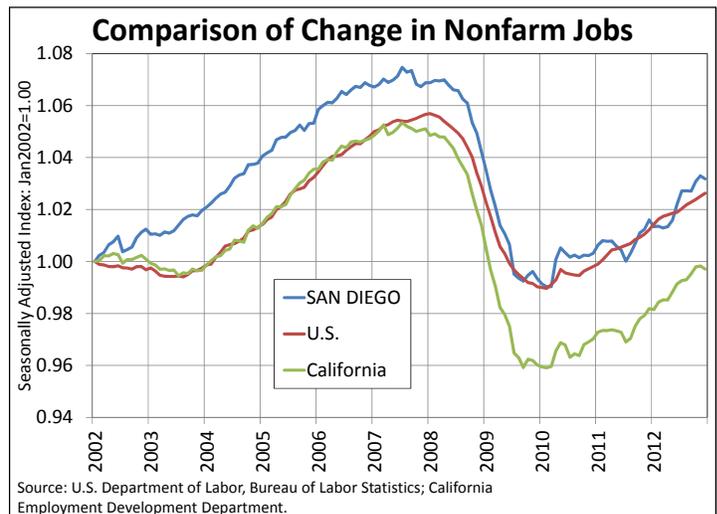
Defense contracting is deeply ingrained throughout San Diego's industrial sector providing for modern military systems. Cutting-edge applications developed by local defense contractors include intelligence gathering, cyber security, and other electronics and computer software systems. These efforts are increasingly used to more efficiently run military operations particularly with budgets being constrained and cost-cutting measures enacted.

Despite San Diego **manufacturing** employment decreasing, production steadily rose

in recent years by expanding high value manufacturing processes. Value-added manufacturing increasingly uses fewer but more highly skilled (and highly compensated) technology labor to produce far greater output. San Diego is a hub for such high-value research and innovation in biotechnology, genomics, communications, software development, cyber-security and clean-tech. San Diego's historic ties to the aerospace sector are also thriving from unmanned aerial vehicle (UAV) systems, so prominently used by the U.S. military, developed and produced here.²

Federal government resolutions to cut back on defense expenditures have major implications for San Diego especially considering we are home to the largest number of military personnel and operations anywhere in the nation. In total economic impact, nearly one-quarter of the regional economy depends upon defense expenditures, including direct, indirect, and induced government and defense related contract spending. San Diego could potentially benefit by cut-backs enacted elsewhere and reassigned or consolidated to local base operations. A strategic refocusing to the Pacific Rim could also bolster San Diego's extensive Naval facilities. But it is difficult to foresee a scenario where defense spending overall is not reduced in upcoming years.

Travel and tourism is staging one of the more dynamic recoveries among San Diego economic sectors. Both hotel occupancies and room rates are rising as visitor numbers rebound and attractions and event attend-



ance increases.

After several years of severely reduced building activity, the **construction** industry is beginning to show some stirrings of greater activity. Both residential and nonresidential construction projects are reappearing around parts of the county.

Slowly improving and evolving employment

Overall employment trends show some improvement in San Diego, particularly as sectors that had previously lost the most jobs started adding again. For the first time since the recession began, construction, retail, and accommodations employment increased in 2012.

Payroll jobs overall are estimated to have increased by 18,900 in 2012. Another 17,500 jobs are forecast to be added in 2013.

Despite economic production improvement, employment in San Diego, as in the rest of the nation, remains far below pre-recession peaks. Between 2007 and 2010 San Diego lost 103,300 jobs, 7.9 percent of the total existing at the peak. Since that time, approximately 51,000 jobs have been added through

2012, nearly half-way to full recovery of job numbers.

San Diego generally exceeded relative gains in jobs over the state and nation prior to the recession. In recovery the County more or less mirrors the nation's job gains, while California has yet to recover to 2002 levels, although state employment grew somewhat faster the past year.

Nearly every major industry category in San Diego added jobs in 2012. The notable exceptions are manufacturing and wholesale trade continuing to shed positions. Shipbuilding and aerospace added some jobs, but significant losses among computer and electronics employers dragged total manufacturing employment downward. Jobs among wholesale trade also decreased despite retail sectors adding jobs.

The strongest job gains continue to be in health care, administrative and support services, professional and technical services, as well as retail, restaurants, and hotels.

After five consecutive years of job losses, with 40 percent of construction jobs existing in 2006 lost, the industry has started adding

jobs again in 2012. Further gains are anticipated in 2013 with stirrings in both residential and commercial construction beginning to revive.

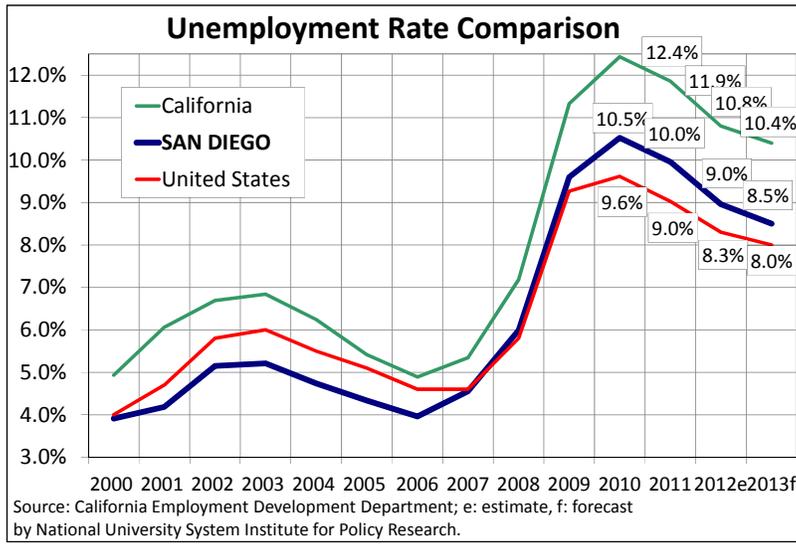
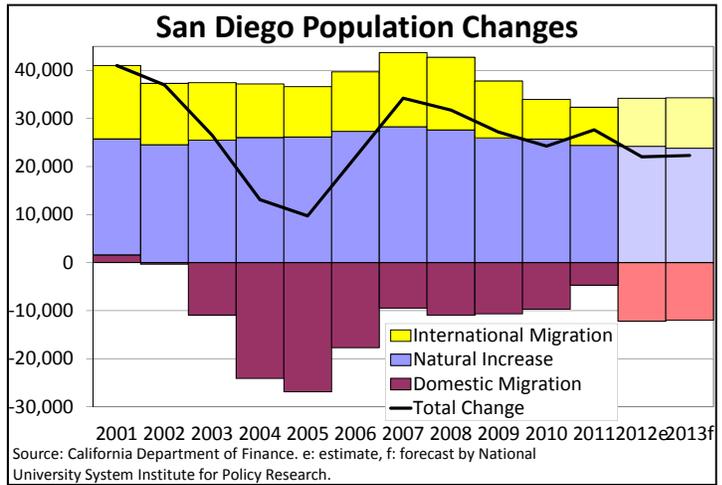
Data on San Diego occupations and average compensation shows higher wage occupations (defined as 25 percent above the county-wide average) increased between 2007 and 2011. In addition, compensation for those positions requiring specific training and technical skills increased by a stronger pace than other occupations.

At the same time, middle income jobs (+/-25 percent average wage) were most

Unemployment rate comparisons

Prior to the recession, San Diego's unemployment rate was usually lower than the rest of California or the U.S. Unemployment started rising in San Diego and California well before the nation. San Diego's rate continued above the national rate, although not as high as California's double-digit levels. With unemployment coming back down, San Diego maintains more or less the same marginal position between the U.S. and California.

San Diego's unemployment rate in 2012 averaged 8.9 percent. The rate should gradually continue improving



squeezed the past four years in terms of number of jobs and total compensation. Low income jobs (25 percent below average) slightly increased in proportion, and slightly decreased in total compensation.

The proportion of workers employed among higher wage occupations increased from 2007 to 2011, as well as total wages. In contrast, the number working in middle wage occupations declined, while low wage jobs slightly increased in proportion.³

in 2013 to 8.5 percent, approaching but not quite reaching U.S. levels, and remaining significantly lower than the rest of California.

Diverging population patterns

San Diego's population reveals significantly diverging patterns of change. Growth over the past decade significantly slowed from previous eras

that at times were two to three times higher despite the much larger population base now.

Recalibrated to the 2010 Census, San Diego's population will approach nearly 3.2 million in 2013. San Diego ranks as the nation's fifth largest county and 17th as a metropolitan area.

Migration the past several years shows as many residents moving away as international migrants moving to San Diego. Population growth in recent years only increased by natural increase with some 26,000-27,000 annually added.

The result is an increasingly ethnically and culturally di-

verse mix particularly among younger age groups. The average age of white and black populations, on the other hand, has grown older.

San Diego, as in the rest of the nation, is much more racially and ethnically diverse. The 2010 Census showed San Diego's white population now accounts for less than one-half of residents. Hispanics make up fully one-third, and one in ten are of Asian descent.

Both white and black populations are decreasing by moving away from the County, as well as being somewhat older and not having as many babies or children. Hispanic population has grown the most from both migration and natural increase. Much smaller in number, Hawaii/Pacific Is-

SAN DIEGO POPULATION BY ETHNICITY/RACE							
Ethnicity/Race	2010	2011	2012	Change		Percent	
				11/10	12/11	11/10	12/11
Hispanic	991,348	1,010,784	1,035,226	19,436	24,442	2.0%	2.4%
White	1,500,047	1,495,582	1,492,320	-4,465	-3,262	-0.3%	-0.2%
Black	146,600	142,905	139,383	-3,695	-3,522	-2.5%	-2.5%
American Indian	14,098	14,229	14,314	131	85	0.9%	0.6%
Asian	328,058	334,836	341,711	6,778	6,875	2.1%	2.1%
Hawaii/Pacific Islander	13,504	13,888	14,224	384	336	2.8%	2.4%
Other	6,715	6,911	7,070	196	159	2.9%	2.3%
Two Plus*	94,943	96,675	99,181	1,732	2,506	1.8%	2.6%
TOTAL	3,095,313	3,115,810	3,143,429	20,497	27,619	0.7%	0.9%

*Refers to two or more combinations of race categories.
Source: San Diego Association of Governments, based upon 2010 Census, U.S. Bureau of Census.

landers, “Other” and mixed races show slightly higher rates of growth.

Children of Hispanic heritage already outnumber white children, and are nearly equal among young adult age ranges. White population decidedly skews older.

With lowered levels of population growth resulting almost entirely from babies, demands on housing are somewhat muted, at least for now. Consumer sales, business demands, and tax revenue increases are also somewhat moderated by this type of population growth.

Construction outlook

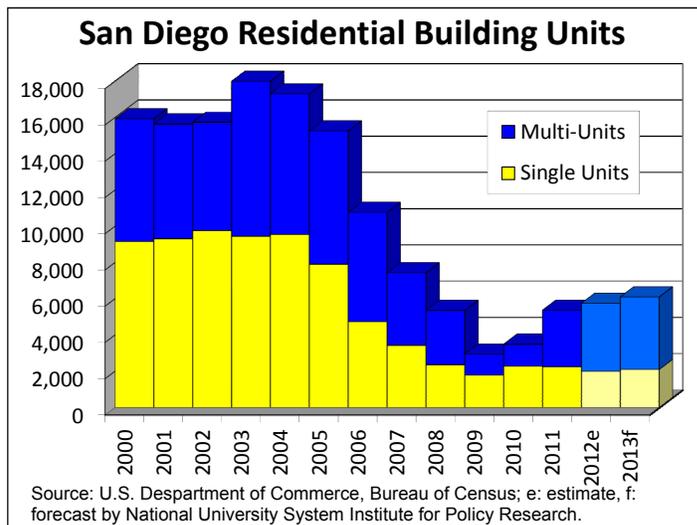
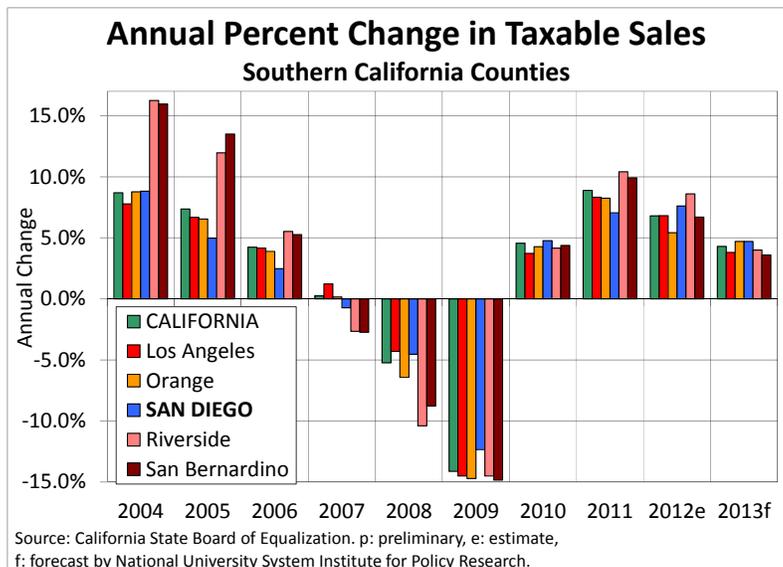
Real estate transactions account for nearly one in five dollars generated within the local economy. Residential construction is rising, although from greatly diminished levels of the past several years. Demand for apartments and other rental housing significantly increased with the housing market collapse and many would-be buyers losing their homes to foreclosure. Two-thirds of new residential unit building permits are for somewhat less expen-

sive multiple-housing.

Home prices appear to have bottomed in 2012 and slightly rose throughout the year. Further price gains are likely to be mixed, however, as the weak economy persists, employment opportunities are constrained, and foreclosures continue to work through the system. This trend will continue in 2013 with relatively small numbers of new units added to the housing supply.

The lack of land available for construction is a contributing factor to the low gains. Ramping up construction, as usually occurred during previous eras coming out of recessions, are not as easily accommodated by infill and limited space available. Construction activity and associated jobs will therefore remain limited.

Nonresidential real estate is similarly mending but long way from full or healthy recovery. Office and industrial vacancies remain relatively high, although appear to be stabilizing among some key submarkets. Rents are relatively flat in most markets, while others still declining. Premium properties in key areas continue to attract the best demand having dis-



counted rental rates. With slow but steady job increases coming, demand will start to rise for office, industrial, and other commercial properties.

Improving consumer sales reflect some improvement of personal finances

Consumer spending in San Diego as measured by taxable sales is rising but still not regaining pre-recession levels. Rebounding from 2008-09 lows, annual sales nevertheless are lower when adjusted for inflation than recorded every year since 1999.

One in seven San Diego business outlets closed during the course of the recession. Since 2010, 4,500 outlets have reopened or been added, but still remain 8.0 percent lower than the number existing in 2006.

San Diego led the rebound of taxable sales in 2010 among southern California counties. Riverside, San Bernardino, and Orange County plunged deeper in 2009, but rebounded percentage wise higher in 2011. Sales are estimated to have

increased at a faster pace in San Diego during 2012, and are projected to tie Orange County in 2013 in slightly exceeding the rest of California.

Many factors influence spending — level of consumer confidence, availability of credit, inflation, and most importantly, employment. With labor markets gradually improving, spending is also rising. Continuing levels of high consumer debt and consumer uncertainties, however, still restrain greater spending.

Inflation prospects

San Diego’s cost of living accelerated from only 1.3 percent in 2010 to 3.0 percent in 2011, and 1.6 percent in 2012. The local inflation rate is forecast to rise to 2.2 percent in 2013.

Guarded outlook in 2013

Falling back into recession for at least part of the year is a possibility, particularly depending upon federal government actions regarding spending cuts and tax increases. The sluggish recovery could lapse with any number of shocks from state and federal policy actions being implemented to tax and regulatory decisions and “sequestration”.

The slow growing economy reflects the persisting lack of consumer confidence and uncertainties for both businesses and consumers to take on more risk. With these continuing cautions, the outlook for San Diego is only moderate growth through 2013.

¹Tom Gray & Robert Scardamalia, The Great California Exodus, Manhattan Institute, September 2012, http://www.manhattan-institute.org/html/cr_71.htm.

²See “An Assessment of Unmanned Aerial Vehicles Impact on San Diego’s Defense Economy”, www.nusinstitute.org/assets/resources/pageResources/UAV_San_Diego_report.pdf.

³See our report on San Diego occupations and wages in the December 2012 edition of the San Diego Economic Ledger at <http://www.nusinstitute.org/Economic-Ledger/Issues.html>.

Dashboard Observations- December 2012

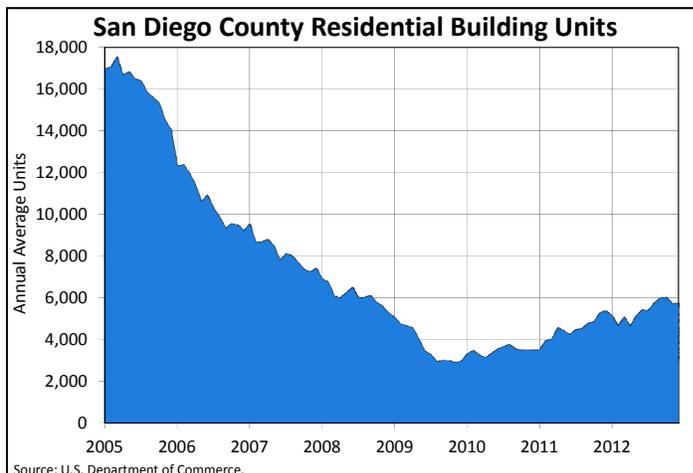
By Kelly Cunningham, Economist and Senior Fellow

Residential building in San Diego continued the slow recovery from historic lows. The annual average number of housing authorized in 2012 approached 6,000 units, the most since 2008.

Nearly all other December 2012 Dashboard indicators show improvement over the year as well. The **stock index** of San Diego based publicly-traded companies was slightly up in December, and over the past year.

The local **unemployment rate** continues to improve, although barely up in December adjusted for seasonal changes. Over the past year the rate improved considerably from 9.0 percent in December 2011 to 8.0 percent in December 2012. This was the lowest it has been since December 2008.

The number of **business licenses** issued by the City of San Diego slightly improved with another 1,054 issued in December. This was 26 percent higher than a year ago, but for the entire year, the 2012 annual number was down 2.0 percent from 2011.



Indicator	Dec 2012	Month Change (Sea. Adj.)	Annual Change
Unemployment Rate¹ San Diego County	8.0%	0.1% ▼	-1.0% ▲
Residential Building² Units authorized for construction San Diego County	392	23% ▲	8% ▲
New Business Licenses³ Issued by City of San Diego	1,054	0.3% ▲	26% ▲
San Diego Stock Index⁴ San Diego based companies	122	3.7% ▲	9.7% ▲

¹California Employment Development Department.

²U.S. Bureau of the Census.

³Business Tax Program, City of San Diego.

⁴Second Thursday of month, Bloomberg News, San Diego Daily Transcript.



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