

# CERF

the bottom line

## *THE CERF REPORT*

2010 : QUARTER 2



Center for Economic Research & Forecasting

<http://www.clucerf.org>

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## The United States

*Bill Watkins, April 26, 2010*

Lately, I've seen a few articles with titles declaring that we are in an economic boom. This is beyond premature; it's silly.

Last year's fourth-quarter GDP number was striking, and the stock market is also showing strength, but we are not yet in a boom. For one thing, the strong gross product growth is unlikely to be sustained. Indeed we expect to see a significantly lower estimate for this year's first quarter when the initial estimate is released on April 30<sup>th</sup>.

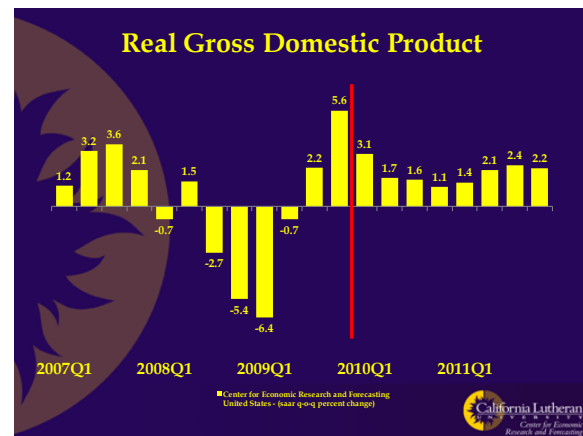
Not only do we expect that 2010 first-quarter growth to be below 2009's final quarter, we expect to see quarterly gross domestic product growth to decline throughout the year, reflecting a very weak recovery, one where unemployment remains at very high levels.

The weakness of the recovery is such that the NBER, the group of economists who assign start and end dates to recessions, recently declined to state that the recession is indeed over.

As much as we try to avoid discussing the stock market, its strength demands some comment. Its recovery has been impressive. At least part of the recovery is a result of overshooting at the bottom of the market; prices were probably too low during the panic that accompanied the financial crisis.

The stock market recovery also reflects increasing profits, and a recovery of some large financial institutions. However, those profits have come not from increasing activity, but by

increasing productivity through layoffs and restructuring.



The stock market's recovery may also reflect something much more subtle. Our analysis indicates that financial crisis and its aftermath have changed the relative competitiveness of small businesses and large businesses.

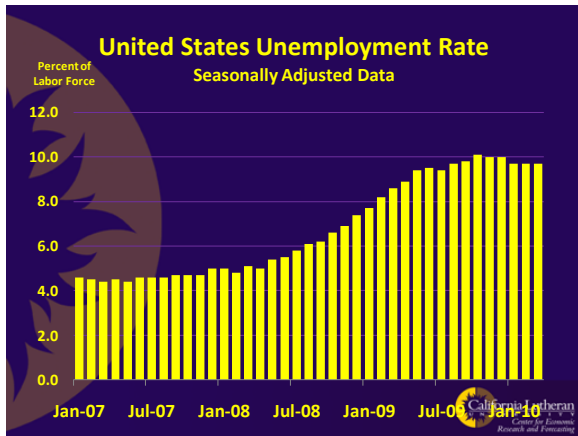
Large businesses appear to have gained a relative advantage that did not exist before the crisis. Part of the advantage reflects their more direct access to financial markets. Small businesses must borrow from a still-sick banking sector.

Big business also gains relative to small business from increased regulation. It is just cheaper for large businesses to comply, on a per-unit-sales basis.

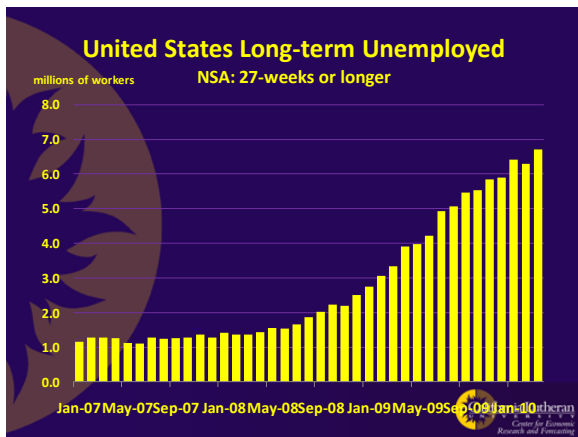
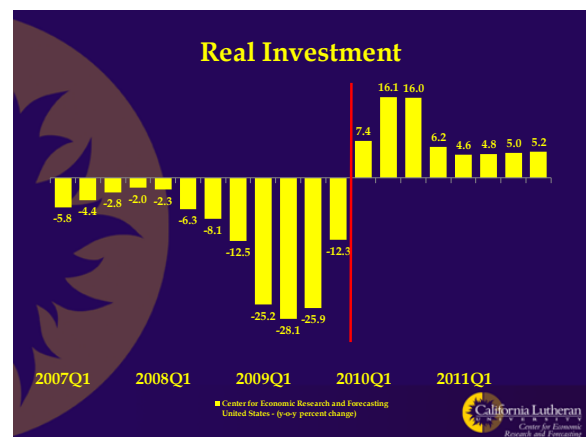
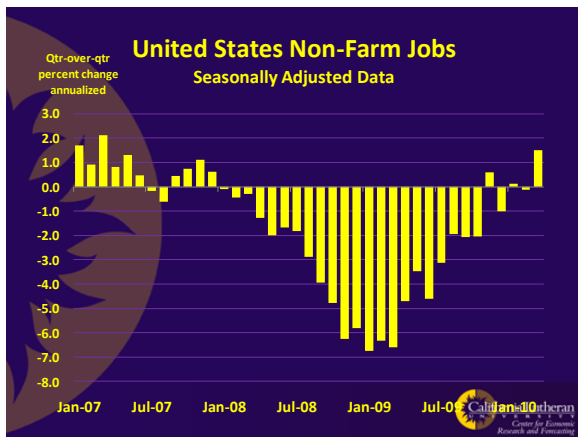
Finally, large companies appear to have gained explicit too-big-to fail status. This is in the process of being codified, through regulatory reform, into law for financial institutions. There is a reason that Goldman Sachs supports the proposed regulations.

The United States – continued

History



Forecast



**California**

*Bill Watkins, April 26, 2010*

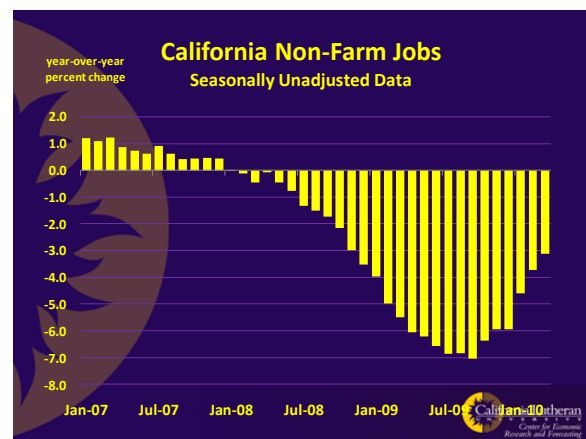
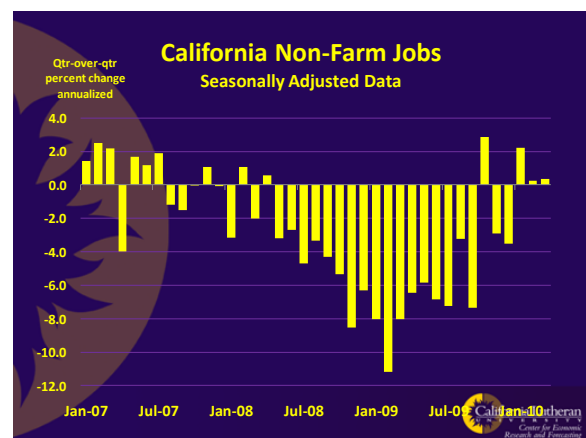
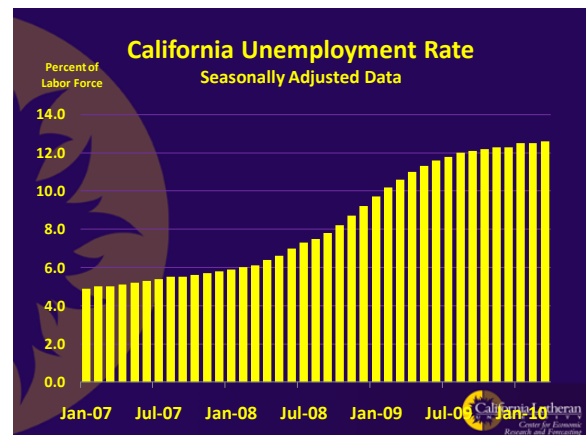
California continues to suffer its most devastating recession in decades. The most recent unemployment data showed California’s unemployment climbing to yet another record, even as a few jobs were created.

Which brings up an interesting point, job growth will not reduce unemployment unless it is strong enough to absorb new entries into the labor force. New entries come from maturing young people and immigrants. For California, only international immigration creates net new immigrants. Domestic migration is now consistently negative, as workers and their families leave California for more prosperous states, like Texas and Oklahoma.

California’s job growth is likely to be insufficient to reduce the State’s unemployment rate, even with the negative domestic migration. The reasons are numerous and include high taxes, long lead times for development, a declining and increasingly inadequate infrastructure, and onerous regulation.

California’s budget issues persist. Recent reports of higher-than-forecast tax are true, but the amounts are insufficient to fundamentally alter the underlying problem.

It really doesn’t matter if California’s day of fiscal reckoning comes in July, September, or December. The State has a date with a crisis, and a broken public sector appears completely unable to effectively deal with challenges it will soon face. Certainly, there is no sign that California’s response will be something that encourages renewed economic vigor.



**Oregon**

*Bill Watkins, April 26, 2010*

Oregon’s unemployment rate has moderated since it peaked, but this is not because of job creation. Instead, workers have left the workforce, and some may be leaving the state.

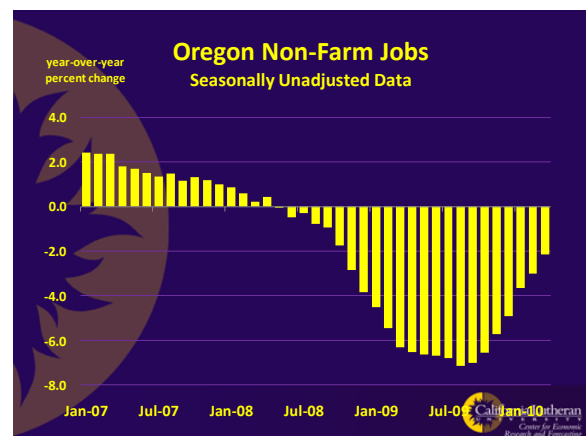
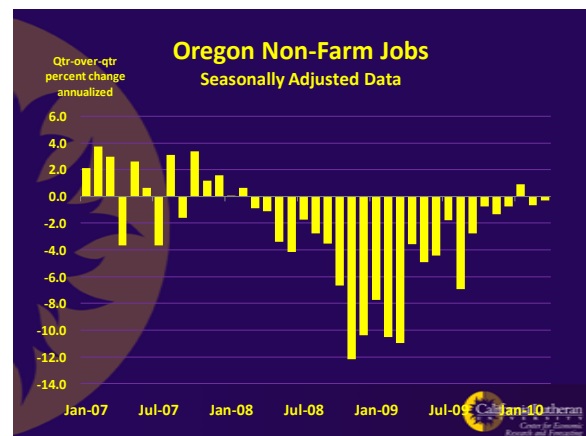
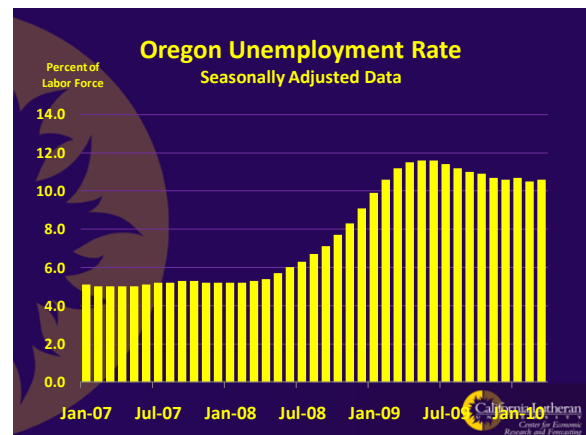
Job losses, though, have clearly peaked, with only small monthly losses, and the occasional positive month.

This economic malaise is likely to persist for some time. Oregon’s building materials sector will likely be weak for years. We see little demand for new residential building, and commercial real estate is currently in the midst of its own crisis.

California has most recently been a source of Oregon’s economic growth, ultimately with disastrous results. For good or for ill, California is unlikely to be a source of economic growth for at least a few years.

Oregon is hoping that technology and alternative energy will be its economic salvation. This is unlikely to achieve the most optimistic expectations.

Oregon is endowed with significant solar, wind, and geothermal resources, and much like hydro, may use these sources to generate exports to other states, particularly California. However, manufacturing is not likely to grow significantly. Oregon, despite its abundant natural and cultural amenities, will find that it is uncompetitive with foreign countries and even other states.





The Center for Economic Research and Forecasting (CERF) at California Lutheran University provides regularly updated forecasts of the United States, California, Oregon, Central Oregon, and Ventura County economies. The State forecasts include regional breakdowns of key measures. The center also performs custom applied economic research and forecasts for clients on a contract basis.

Bill Watkins, Ph.D. is the CERF's Executive Director. Dan Hamilton, Ph.D. and Kirk Lesh, M.A. are the other founding economists. Bill Watkins and Dan Hamilton have been doing Economic Research, Economic Forecasting, and Economic Consulting together since 2000. They ran the UCSB Economic Forecast Project from 2000 to 2009. Kirk Lesh joined Bill and Dan in 2007 and provides critical research and consulting functions.

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