Economic Development Board
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# Local Economic Report Series

# Summer 2003


Presented By
Sonoma County Economic Development Board
in partnership with
Sonoma County Workforce Investment Board

September 2003

The Sonoma County Economic Development Board, in partnership with the Sonoma County Workforce Investment Board, is pleased to present the Summer 2003 edition of the *Sonoma County Local Economic Report*.

Sonoma County's economy continues to struggle. While Sonoma County's unemployment rate is better than the US, it continues to worsen. Despite declines across most industries, the tourism sector is stable and offers the best potential for near-term economic growth. Some highlights from the report include:

- Moderate job growth is expected by the end of the year, and the long term outlook for the Sonoma County (SON) economy is positive, outpacing the national economy.

- The tourism sector proved strong over the summer months, and showed a 5% increase in employment since the beginning of 2003.

- Low interest rates were able to offset any downward pressure in housing prices. As interest rates rise, prices should flatten.

- The rising unemployment rate has stayed below the US average because of a nonexpanding labor force. The nonexpanding labor force may be a result of net migration flows, which were negative last year for the first time in recent history.

- Business conditions are weak, as business bankrupcies are at a record high for three consecutive quarters.

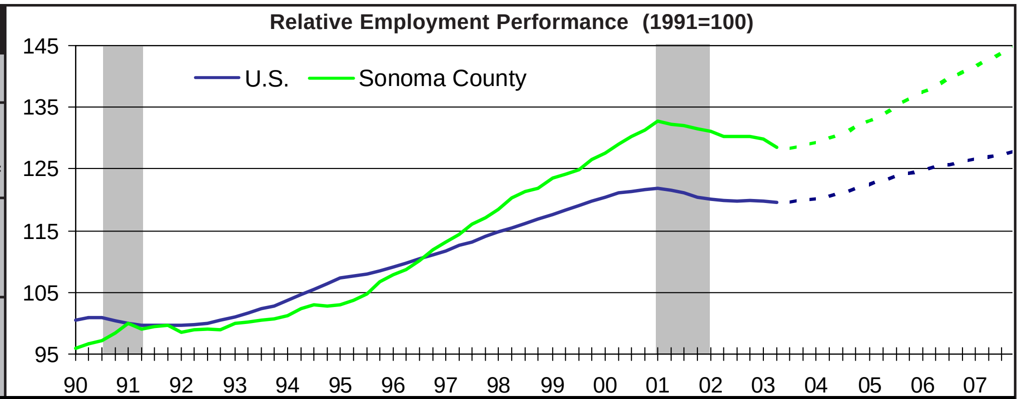
*Economy.com* produces the Local Economic Report Series for the EDB. Thank you for your continuing interest in the local economy.

Yours sincerely,

Ben Stone
EDB Director

# SONOMA COUNTY

| EMPLOYMENT GROWTH | MSA LIFE CYCLE PHASE |
|---|---|
| *2002-04* | Growth/Mature |
| **256** | VITALITY: Best= 1 **80** Worst= 325 |
| *2002-07* | COST OF DOING BUSINESS: U.S. = 100% **99%** |
| **73** | COST OF LIVING: U.S. = 100% **127%** |
| Best=1 Worst=325 MSAs | |




| 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | Indicators | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 9.9 | 10.9 | 11.8 | 12.7 | 14.3 | 14.3 | 14.5 | **Gross Metro Product, C$B** | 14.8 | 15.3 | 15.9 | 16.6 | 17.3 |
| *4.6* | *9.8* | *8.1* | *7.5* | *12.6* | *0.3* | *1.6* | *% Change* | *2.0* | *3.1* | *3.9* | *4.5* | *4.1* |
| 157.5 | 165.4 | 173.0 | 179.3 | 186.1 | 189.8 | 187.4 | **Total Employment (000)** | 185.1 | 187.2 | 193.1 | 199.6 | 205.5 |
| *4.8* | *5.0* | *4.6* | *3.6* | *3.8* | *2.0* | *-1.3* | *% Change* | *-1.2* | *1.2* | *3.2* | *3.4* | *3.0* |
| 4.4 | 3.8 | 3.3 | 2.7 | 2.6 | 2.9 | 4.5 | **Unemployment Rate** | 4.9 | 5.0 | 4.4 | 4.1 | 3.9 |
| 6.4 | 8.4 | 8.1 | 6.2 | 13.4 | -0.2 | -0.7 | **Personal Income Growth** | 2.4 | 5.8 | 6.5 | 6.4 | 6.1 |
| 428.4 | 437.1 | 445.9 | 453.4 | 460.4 | 466.5 | 468.4 | **Population (000)** | 471.1 | 477.0 | 487.2 | 498.3 | 508.4 |
| 1,412 | 1,785 | 2,098 | 2,348 | 2,013 | 1,717 | 1,350 | **Single-Family Permits** | 1,719 | 1,876 | 1,855 | 1,888 | 1,849 |
| 75 | 176 | 964 | 688 | 492 | 866 | 578 | **Multifamily Permits** | 648 | 607 | 619 | 694 | 739 |
| 215.6 | 225.8 | 246.7 | 276.4 | 325.7 | 364.9 | 402.9 | **Existing Home Price ($Ths)** | 435.2 | 449.3 | 458.9 | 480.6 | 501.5 |
| 2,458 | 2,839 | 5,163 | 4,499 | 3,990 | 8,651 | 10,875 | **Mortgage Originations ($Mil)** | 14,752 | 4,151 | 3,577 | 3,905 | 4,269 |
| 4.3 | 7.0 | 7.1 | 6.0 | 5.3 | 4.1 | -0.3 | **Net Migration (000)** | 0.2 | 3.5 | 7.5 | 8.4 | 7.1 |
| 2,011 | 2,090 | 2,173 | 1,627 | 1,158 | 1,183 | 1,223 | **Personal Bankruptcies** | 1,239 | 1,061 | 905 | 974 | 1,035 |

## STRENGTHS & WEAKNESSES

### STRENGTHS

- High per capita income.
- Links to stable consumer economy through winemaking and tourism.
- Attractive environment.

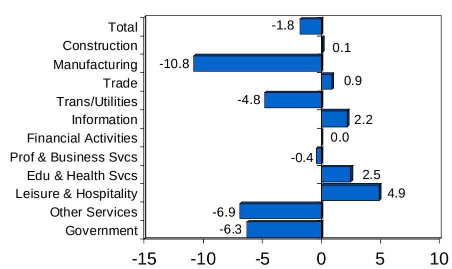
### WEAKNESSES

- Demand remains weak for telecom equipment.
- Burgeoning global supply of wine dims profit outlook for this critical industry.
- High cost of living.
- Complex regulatory environment.

## CURRENT EMPLOYMENT TRENDS

**July 2003 Employment Growth**

*% Change Year Ago*




## FORECAST RISKS

| SHORT TERM ↓ | LONG TERM ↑ | RISK-ADJUSTED RETURN, '02-07 | 0.73% |
|---|---|---|---|

### UPSIDE

- Business investment quickly extends to high-tech telecom and optical equipment.
- Turnaround in tourism boosts hospitality and wine industries.

### DOWNSIDE

- Housing market suffers price correction, diminishing homeowners' equity.
- Dollar regains its luster, reducing competitiveness of local exports.

## ANALYSIS

**Recent Performance.** Sonoma County's (SON) economy continues to struggle. Employment is in its third year of decline, and industrial production is flat and well below its peak of early 2001. The labor force has stopped expanding, which is the only reason why the jobless rate is able to stay below the U.S. average. The pace of job cutbacks in manufacturing has barely slowed over the past year as its two primary components, wine making and electronics/optical equipment, still face weak demand and little pricing power. The strongest component of the economy at the moment is tourism.

With business bankruptcies at a record high for three consecutive quarters, business conditions remain weak, with considerable risk of further layoffs. This puts at risk household financial conditions, which so far have escaped serious damage. Stable and high house prices have given some cushion to households through the availability of substantial home equity.

**Signs of stability.** A little relief for vineyards comes from some renewed stability in prices, following several years of decline and oversupply. Local and statewide grape production this year is expected to fall, the result of some acreage being removed from production and a wet spring that will contribute to lower yields from vineyards. Prices could rise moderately for grape growers, although this could put a minor squeeze on winemakers who still face stiff competition from imports.

Some stability is also seen in the travel and tourism industry. The summer months saw some improvement in travel as short-distance travel from nearby major metro areas picked up. Employment in arts, entertainment, recreation and hotels bounced back in the summer and is now up by over 5% for the year. The travel industry offers the best potential for near-term economic growth as demand for leisure travel and services is improving. Business travel, however, has barely improved over the past year.

One sign of a broader turnaround in the local economy would be an increase in the hiring of temporary staff. While such employment did rise a bit this summer, the number of temp workers still remains below a year ago, so this evidence of a turnaround remains less than compelling.

**Technology.** Such stability is not yet evident in the electronics, telecom equipment and optical equipment industries. Indeed, the downturn in employment in the manufacture of computer and electronic equipment has accelerated since the beginning of this year, and is now down by nearly half from its peak of 9,000 in 2001. Business investment is improving nationwide, but little of this is directed yet toward telecom and optical equipment. There is simply still too much excess capacity in the industry. Thus, the turnaround in SON's tech-based economy will lag other tech centers that focus more on consumer products and computing components.

**Real estate.** The economic downturn has had a moderate impact on residential real estate. Low interest rates have generated sufficient demand to offset any downward pressure in sales prices due to weak income growth. However, prices are expected to flatten for at least the next 18 months given that interest rates are up from historic lows and supply outstrips fundamental demand, as indicated by household formations. Nonresidential construction has slowed and will maintain its moderate pace for at least one more year, until net absorption turns positive for industrial and office properties.

**Sonoma County's outlook is weak, yet does call for moderate net job growth by the end of this year. Risks remain solidly on the downside, however, for two of its three main drivers, winemaking and tech-based manufacturing. However by 2005, SON will once again outpace the U.S. average as national and international markets improve.**

*Steven G. Cochrane*
*August 2003*

## EMPLOYMENT & INDUSTRY

### TOP EMPLOYERS

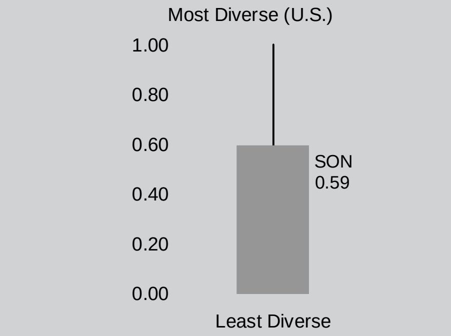
| | |
|---|---|
| Agilent Technologies, Inc. | 2,600 |
| Sonoma State University | 1,799 |
| Medtronic, AVE | 1,400 |
| St. Joseph Health System | 1,225 |
| JDS Uniphase Corporation | 1,200 |
| State Farm Insurance Company | 822 |
| Kendall-Jackson Wine Estates | 820 |
| Sutter Medical Center | 752 |
| Longs Drug Stores, Inc. | 700 |
| Kaiser Permanente | 675 |
| Sonoma Misson Inn & Spa | 675 |
| Washington Mutual | 650 |
| Hansel Dealer Group | 606 |
| Advanced Fibre Communications | 600 |
| Cisco Systems, Inc. | 600 |
| SBC Communications, Inc. | 600 |
| Pacific Gas and Electric Company | 535 |
| Wal-Mart Stores, Inc. | 420 |
| Exchange Bank | 417 |
| F. Korbel & Bros. | 403 |

*Sources: North Bay Business Journal, February 2003 & The Santa Rosa Press Democrat, June 2003*

**Public**

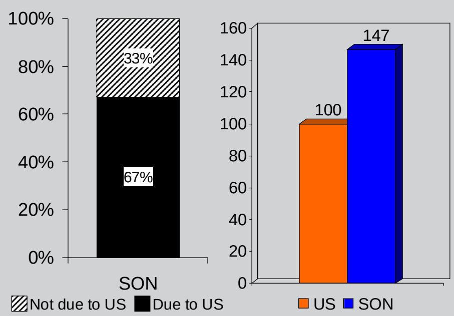
Federal ........................................................ 1,808
State ............................................................ 5,708
Local ........................................................ 20,843
*2002*

### INDUSTRIAL DIVERSITY




### EMPLOYMENT VOLATILITY

**DUE TO U.S. FLUCTUATIONS** | **RELATIVE TO U.S.**

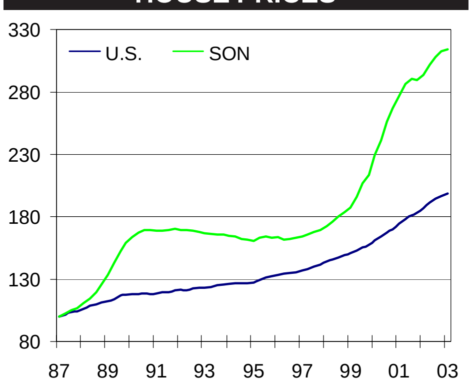



## COMPARATIVE EMPLOYMENT AND INCOME

| Sector | % of Total Employment SON | CA | US | Average Annual Earnings SON | CA | US |
|---|---|---|---|---|---|---|
| Construction | 7.2% | 5.3% | 5.2% | $50,463 | $47,877 | $39,845 |
| Manufacturing | 14.2% | 11.3% | 12.0% | $52,640 | $55,970 | $48,756 |
| *Durable* | *62.0%* | *64.3%* | *62.0%* | *nd* | *$63,121* | *$50,404* |
| *Nondurable* | *38.0%* | *35.7%* | *38.0%* | *nd* | *$42,646* | *$45,969* |
| Transport/Utilities | 2.2% | 3.4% | 3.6% | $39,995 | $47,311 | $44,972 |
| Wholesale Trade | 3.2% | 4.5% | 4.4% | $44,017 | $52,350 | $51,842 |
| Retail Trade | 12.9% | 10.9% | 11.7% | $25,949 | $27,420 | $22,635 |
| Information | 2.3% | 3.4% | 2.6% | $57,463 | $83,422 | $69,569 |
| Financial Activities | 5.6% | 5.9% | 6.0% | $27,675 | $40,394 | $41,740 |
| Prof. & Business Services | 10.3% | 14.7% | 12.4% | $39,583 | $48,046 | $43,053 |
| Education & Health Services | 12.7% | 10.4% | 12.5% | $33,147 | $36,158 | $34,032 |
| Leisure & Hospitality Services | 10.6% | 9.5% | 9.0% | $17,930 | $23,238 | $19,135 |
| Other Services | 3.6% | 3.5% | 3.9% | $22,955 | $21,695 | $19,842 |
| Government | 15.1% | 16.9% | 16.2% | $43,588 | $48,959 | $42,939 |

*Source: Percent of total employment - BLS, 2002; Average annual earnings - BEA, 2001*

## HOUSE PRICES




*Source: OFHEO, 1987Q1 = 100, NSA*

## CREDIT QUALITY

| MOODY'S RATING | COUNTY **Aa3** |
|---|---|

## LEADING INDUSTRIES

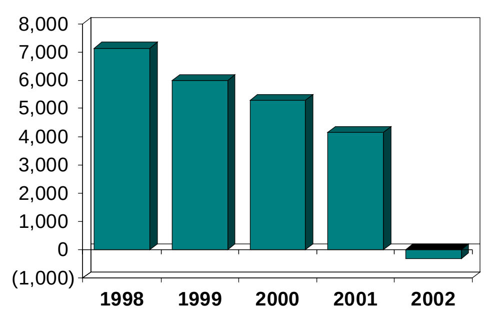
| NAICS | Industry | Employees (000) |
|---|---|---|
| 7222 | Limited-Service Eating Places | 5.7 |
| FR | Farms | 5.3 |
| 4451 | Grocery Stores | 4.8 |
| 3345 | Nav., Meas., Electro., & Con. Instru. Manuf. | 4.8 |
| 2360 | Construction of Buildings | 3.9 |
| PH | Private Household Workers | 3.9 |
| 7211 | Traveler Accommodations | 3.3 |
| 5511 | Management of Companies and Enterprises | 2.9 |
| 2383 | Building Finishing Contractors | 2.5 |
| 3391 | Medical Equipment and Supplies Manufacturing | 2.5 |
| 2381 | Foundation, Struc., & Bldg. Ext. Contractors | 2.1 |
| 3119 | Other Food Manufacturing | 2.0 |
| 4441 | Building Material and Supplies Dealers | 2.0 |
| 8111 | Automotive Repair and Maintenance | 2.0 |
| 7139 | Other Amusement and Recreation Industries | 1.8 |
| | High-tech employment | 13.6 |
| | As % of total employment | 6.9 |

*Source: BLS, Economy.com, 2002*

## MIGRATION FLOWS

| Into Sonoma County | Number of Migrants | Median Income |
|---|---|---|
| San Francisco | 3,599 | 38,234 |
| Oakland | 1,178 | 33,343 |
| Vallejo | 777 | 27,593 |
| San Jose | 729 | 42,030 |
| Los Angeles | 607 | 26,211 |
| Sacramento | 499 | 25,688 |
| San Diego | 349 | 20,681 |
| Riverside | 219 | 21,407 |
| Orange County | 206 | 21,590 |
| Seattle | 192 | 24,109 |
| Total Immigration | 14,772 | 27,943 |
| **From Sonoma County** | | |
| San Francisco | 1,815 | 32,083 |
| Sacramento | 1,438 | 32,738 |
| Vallejo | 1,009 | 34,661 |
| Oakland | 918 | 28,425 |
| Los Angeles | 461 | 19,860 |
| San Diego | 407 | 17,642 |
| San Jose | 396 | 31,183 |
| Redding | 348 | 32,777 |
| Riverside | 329 | 23,096 |
| Phoenix | 325 | 27,249 |
| Total Outmigration | 17,735 | 26,583 |
| **Net Migration** | **-2,963** | **1,360** |

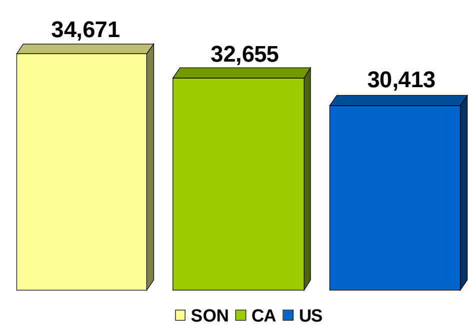
**Net Migration, SON**




| | Domestic | Foreign | Total |
|---|---|---|---|
| 1998 | 3,862 | 3,269 | 7,131 |
| 1999 | 2,929 | 3,055 | 5,984 |
| 2000 | 2,260 | 3,020 | 5,280 |
| 2001 | 1,096 | 3,054 | 4,150 |
| 2002 | -3,360 | 3,049 | -311 |

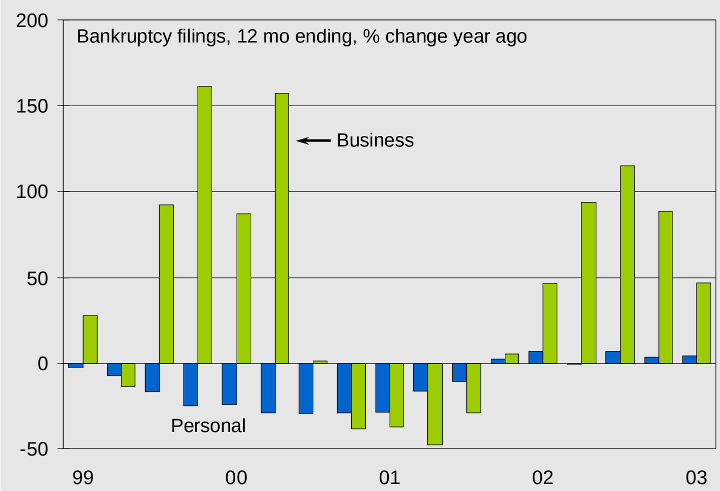
*Source: IRS (top), 2002; Census Bureau, 2002*

## PER CAPITA INCOME



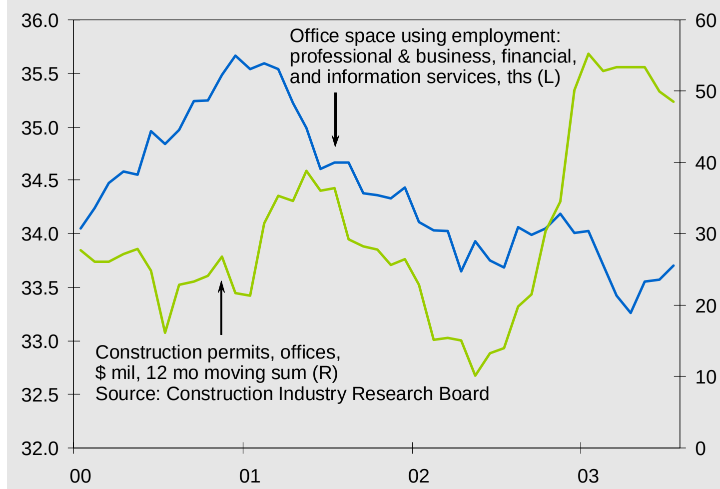

*Source: Bureau of Economic Analysis, 2001*

**Business Bankruptcies Indicative of Current Weakness**



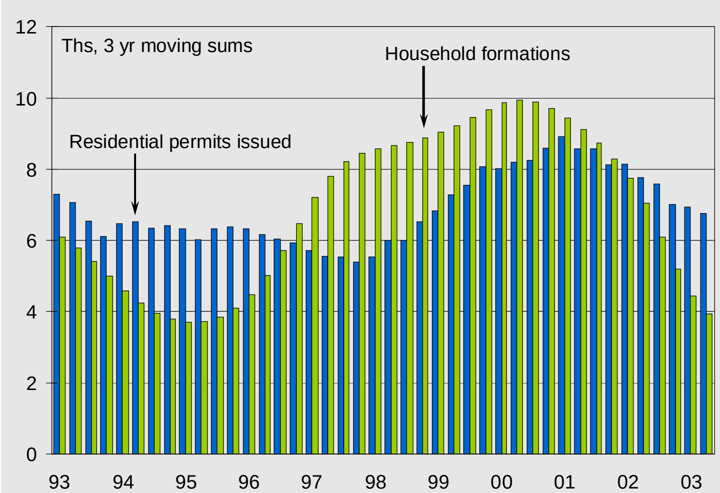

The continued weakness of SON's economy is illustrated by rising bankruptcy filings among both businesses and households. The more than doubling of business filings in recent quarters is indicative of the broad range of industries hit by the recession and the weak economic recovery, including telecom equipment, wineries and the travel industry. Personal filings also continue to rise, and likely will not improve until business conditions improve and hiring recommences. Thus, demand for retail and personal services will remain stable, at best, in the near term.

**Office Space: Weak Demand, Increasing Supply**



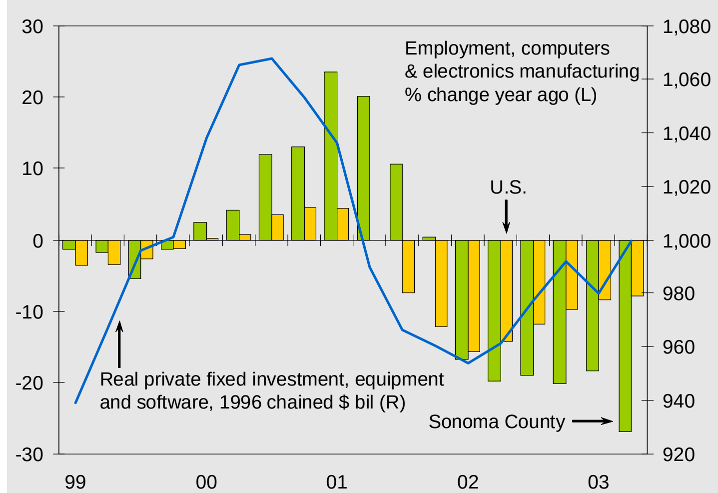

Office space demand has not turned up yet. Indeed, the total office vacancy rate in SON soared in the first quarter to over 18%, according to Keegan & Coppin Co., Inc. This includes a considerable quantity of available sublease space as well as new supply. Indeed, the value of construction permits issued for office space over the past 12 months was its highest in over 10 years, according to the Construction Industry Research Board. Thus, there is some risk that lease rates, which so far have held fairly stable, will fall in the coming quarters.

**Pressure on Housing Market Is Easing**




The excess demand in residential real estate is fading. Demographic trends now indicate that new supply is outstripping demand. However, house prices do not reflect this shift as yet, with price appreciation holding steady in the low teens, according to the California Association of Realtors' median sales price for their North Bay region. Considerable pent-up demand, a result of a lack of affordability in recent years, and the low interest rate environment, are combining to support demand and prices. However, there is considerable risk to the market, as interest rates rise amid a weak local economy.

**Sonoma County's Tech Sector Is Slow to Recover**




SON's economic recovery will lag the national pace, due in part to a slow turnaround among local tech industries. While nationwide, the worst has clearly past among manufacturers of electronic and other tech-related products; the downturn just seems to get worse among local producers. Business investment is improving broadly for industrial equipment, but it is not yet filtering through to the telecom equipment industry, which still suffers from lack of demand and excess capacity. Technical innovations among the local industry will ultimately support it, but demand will be slow to turn around.

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