



UNIVERSITY OF CALIFORNIA SANTA BARBARA
ECONOMIC FORECAST PROJECT



2010 SANTA BARBARA COUNTY **ECONOMIC OUTLOOK**

FIFTY YEARS

of Partnership.



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SINCE 1960

www.sbbt.com

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1960 Cliff Drive
805.965.7125

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3910 State Street
805.898.8879

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805.569.0853

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805.968.6144

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299 North Fairview Avenue
805.683.1404

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5420 Carpinteria Avenue
805.684.4566

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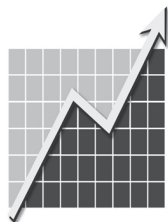
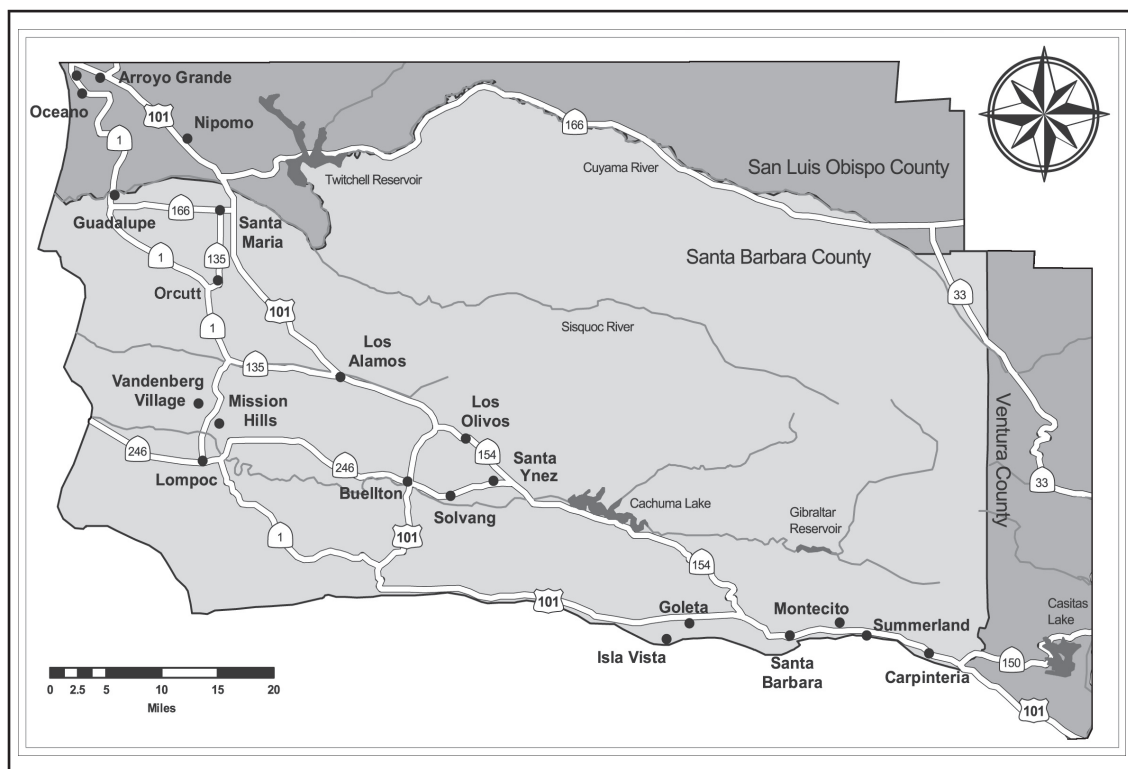
Laura Corsello
Branch Manager

As we celebrate 50 years of service, we extend our gratitude to you, our loyal customers and friends. In the tradition of our founders, we are honored to be your bank and proud to be your community partner.

THE 2010 SANTA BARBARA COUNTY ECONOMIC OUTLOOK

UC SANTA BARBARA ECONOMIC FORECAST PROJECT

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UNIVERSITY OF CALIFORNIA, SANTA BARBARA
SANTA BARBARA, CA 93106-3195
(805) 893-5739

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SANTA BARBARA BANK & TRUST

SINCE 1960



Santa Barbara Bank & Trust (SBB&T), one of California's largest regional banks, is proud to be the founding sponsor of the UCSB Economic Forecast Project in delivering this important economic analysis to the Santa Barbara community. We congratulate everyone involved in the Project for their continued fine work.

For 50 years, SBB&T has provided financial services and products to individuals and businesses in Santa Barbara and Ventura counties. With dedicated professionals in 30 branches, the Bank is committed to continually enhancing the economic vitality and social welfare of the communities served.

With the financial solutions of a large bank and the personal service, responsiveness and familiarity of a local community bank, SBB&T ensures that your banking needs will be met by someone who truly understands your unique objectives and goals.

Our Community. *Your Bank.*SM



www.limottait.com

CIO Solutions enables organization & business success via IT solutions. CIO has been providing complete computer & phone system network management, monitoring, support, and associated products since 1986. CIO's Engineering Team utilizes our state-of-the-art Remote Operations Center ('ROC') to promptly resolve computer network and workstation problems in addition to updating your software and even backing up & recovering your data. Our ROC utilizes advanced remote tools and provides rapid accessibility, allowing our advanced support team to resolve most computer and phone network issues during the FIRST CALL. The result allows your employees to return to being highly productive at the fastest rate possible, greatly minimizing the high costs associated with computer & phone down-time. CIO Solutions also provides you with a highly trained and certified onsite Network Engineer from our team of 10+ for when advanced support or network projects are required. Moreover, we employ actual CIO-level Network Planning and Design Consultants that are trained to focus on the big picture of your business and thus assist you with reaching your organization's vision and goals.

Our specific IT project expertise includes: Switching & Routing Infrastructure; Enterprise Storage; Security; Virtualization; Wireless; Remote Communications; and VoIP Phone Systems. Many years of experience combined with our long established partnerships with the industry's leading vendors uniquely qualify CIO Solutions to proactively manage, support, and design technology environments of all sizes and sophistication.



County of Santa Barbara
Auditor-Controller

www.countyofsb.org/auditor/home.asp

The County of Santa Barbara was established by an act of the State legislature on February 18, 1850. The County provides a wide range of services to its residents including public protection through sheriff, fire, district attorney, probation, child protection and courts, public and mental health services, public assistance programs, construction and maintenance of roads and bridges, environmental services, parks, and a variety of other governmental services. The county has a 4,600-person workforce that strives to provide these services in an effective and efficient manner.

Information provided by the UC Santa Barbara Economic Forecast concerning current and projected economic conditions has proven extremely valuable to the County for strategic planning, and in preparing revenue forecasts and the annual budget. The County believes that participation in the Economic Forecast Project better enables it to serve the needs of its citizens in a progressive and informed manner.



www.DaviesPublicAffairs.com
www.BlazePR.com

Davies and BlazePR, a subsidiary company, rank among the top public affairs and public relations companies in the nation. Both are multi-award winning firms with Davies recently receiving the national award for the best public affairs campaign of 2009, and BlazePR awarded a national Anvil by PRSA.

Winning approval and succeeding today is tied directly to your ability to rapidly reach out, engage others, and do so while everyone watches. Davies creates messages that motivate individuals to stand up, speak out, and take action, influencing the approval process at all levels. Davies develops communication strategies across multiple industries including; creating patient adherence programs for international pharmaceutical companies, redeveloping controversial natural resource extraction and mining projects, permitting energy facilities in sensitive environments, gaining approval for real estate developments facing tough NIMBY opposition, as well as managing the communications crisis of all types. Davies uses authentic grassroots to generate real results. Our unique approach to research, message development and targeted outreach, using all communication channels, has resulted in a 96% success rate for our clients.

Founded in 1983, Davies ranks as the 3rd largest PR firm in California and the 17th largest nationally. We've turned more than 450 controversial public affairs issues.

BlazePR is a pragmatic strategic communications firm that integrates traditional media relations with cutting-edge social media to affect the bottom-line goals of its clients. Founded nearly two decades ago, BlazePR has consistently ranked as one of the leading consumer agencies in North America. With a specialty in hospitality/travel & real estate, BlazePR eschews traditional "publicity," in favor of communications strategies that combine creativity and insight into business-building ROI for its clients.

In an industry where client turnover is the norm, Blaze is proud to claim numerous client relationships that extend beyond a decade.

Davies and BlazePR maintain strong local roots by representing some of the best-known local companies and organizations in the Tri-county. These include, The Bank of Santa Barbara, Museum of Natural History, the Cities of Santa Barbara and Port Hueneme, Business First, the County of Santa Barbara, Santa Barbara City College, Santa Barbara MTD, Westmont College, Sansum-Santa Barbara Medical Foundation Clinic, Ty Warner Sea Center, Santa Barbara Botanical Garden, Four Seasons Biltmore, Bacara Resort & Spa, Miramar, Granite Construction, Venoco, ExxonMobil, PXP, and countless others.

To ensure you have the right messages, strategy and tactics to win, we're standing by at DaviesPublicAffairs.com & BlazePR.com.



www.limottait.com

LIMOTTA Internet Technologies has been a full service Internet Technology Solutions Provider since 1997. The company began with a geographic focus of serving small to mid-size businesses in central coast California (Ventura County, Santa Barbara County and San Luis Obispo County) and have recently expanded to offer services throughout California and 13 other states.

LIMOTTA Internet Technologies can address many questions you may have such as; How do I get internet connectivity when DSL is unavailable? How do I connect to my main office from home or other offices? How do I reduce downtime? How do I reduce the risk of someone hacking into my network? How do I reduce the risk of data loss? How do I increase my connection speed? How do I minimize the labor cost to maintain and support my network? How do I minimize my investment in email/unified messaging? How do I open up new distribution channels for my company's products and services? How do I legally reduce software licensing costs? How do I invest in hardware and software for my business that will guarantee the highest possible return? How do I improve the reliability and lower the costs of my telephone systems?

Our service offerings consist of: Broadband internet connections, network support contracts, website/application developments, hardware, software investments, fiber and wireless retrofits, voip telephony solutions.

Paths to prosperity

www.montecito.com

You know better than anyone that managing your own business takes vision, creativity and lots of hard work. It also takes a special kind of banking relationship to support you as your business grows and evolves.

Although it may seem that most banks offer the same basic services, we think you'll find Montecito Bank & Trust distinctly different. That's because we make it our business to listen carefully and collaborate closely. We'll customize just the right solution for your current needs and future goals, and earn your trust in the process.

Montecito Bank & Trust got its start 35 years ago as a locally owned bank, and remains locally owned today. We are profitable, have the liquidity to be actively lending, and are well-capitalized. For the past ten consecutive years we have received a Premier or Super Premier rating by The Findley Reports, an independent service which rates the financial performance of California banks.

So, whether it's a loan to fuel your growth, a sweep account to maximize the return on your deposits, or the speed and convenience of online and mobile business banking, our relationship managers will help you solve your financial needs. And, our tenured Wealth Management professionals deliver individualized strategies for successful investment management and advisory services, and complete trust and estate services.

There's no better time to make a banking relationship change. We'd like the opportunity to get to know you and learn about your business. Let Montecito Bank & Trust provide you with a uniquely valuable financial experience.

Customized financial solutions just right for the times – some of the many Paths to prosperity® you'll find at Montecito Bank & Trust.

**Rabobank**

www.rabobankamerica.com

Rabobank, N.A. Profile for UCSB Economic Forecast for South Santa Barbara County.

Rabobank, N.A. is a California community bank that provides personalized service and a full array of quality products to individuals, businesses and agricultural clients. With 92 retail branches and 15 commercial banking centers, we serve the needs of communities from Sacramento to the Imperial Valley through local decision making and active community involvement by our employees.

Rabobank serves Santa Barbara County with 17 retail branches and two commercial banking centers. We offer business checking and savings plans, cash management services, business loans and lines of credit, business equipment leasing, agricultural financing, investment management and trust administration services.

Our lending decisions are made locally and the money you deposit at Rabobank is invested back into the community through loans to local businesses like yours. Our unique size allows us to respond quickly to customer needs and tailor our services to each community we serve.

Safe, sound and secure, Rabobank, N.A. is part of the Rabobank Group, one of the safest banks in the world with more than 110 years of trustworthy service. Rabobank, N.A. is well capitalized and can meet the needs of its customers without government assistance.

To learn how Rabobank can help you reach your business goals, stop by or call any of our local offices:

Commercial Banking

33 E. Carrillo Street, Santa Barbara, 879-9318

Retail Banking

33 E. Carrillo Street, Santa Barbara, 963-5871

914 Carpinteria Street, Santa Barbara, 963-8928

2222 Bath Street, Santa Barbara, 682-3999

5340 Hollister Avenue, Santa Barbara, 683-3000

5956 Calle Real, Goleta, 967-0451

5030 Carpinteria Avenue, Carpinteria, 684-7602

Rincon Broadcasting

www.rinconbroadcasting.com



K~LITE 101.7



www.independent.com

The Santa Barbara Independent is Santa Barbara County's most comprehensive weekly guide to local politics, news, lifestyle, entertainment, and the arts. It contains the most complete listing of community events and is must reading for active Santa Barbara County residents.

The Independent is an active sponsor of numerous community events through advertising grants that have supported the Mariachi Festival, Old Spanish Days, UCSB Athletics, and the Economic Forecast Project, among others. More than 125 community non-profits from the Arts Fund to the Endowment for Youth receive free advertising through the Independent's public affairs program.

Readership surveys reveal that the average Independent reader is 40 years old, college-educated and affluent. With a 40,000 circulation, and a pass-along rate of approximately three readers per copy, the total reach of the Santa Barbara Independent is more than 120,000 South Coast readers.

The Independent is available at more than 400 locations from Carpinteria to Lompoc. Like the best things in life, it's still free!



www.newspress.com

As Southern California's oldest daily newspaper, the Santa Barbara News-Press has reported on Santa Barbara County news for more than a century. More than 140,000 readers turn to the News-Press daily for a complete look at the issues that affect the county, state and nation. The newspaper is the leading supplier of news, information and advertising for the Santa Barbara County area. During recent years, the News-Press has been awarded the California Newspaper Publishers Association's prestigious General Excellence Award five times.

In recent years, the News-Press has moved aggressively to serve the changing needs and desires of our audience, and become a multi-media communications company. Broadening our reach beyond the daily paper in providing comprehensive community news and information, we also offer news on the radio, through our partnership with KZSB-AM 1290, and on the web, with live, breaking news and updates throughout the day on newspress.com. The latest addition to newspress.com and one that adds to the News-Press' commitment to being the source for local news on the Central Coast, is News-Press TV streaming local news reports 24 hours a day accessible via computer from anywhere in the world. We also publish several specialty publications, including the weekly Goleta Valley Voice, the monthly Blue Edge Magazine and the bi-weekly Spanish-language El Mexicano de Santa Barbara. And NP Commercial Printing offers pre-press services and high volume offset printing for publishers throughout California.

As part of its ongoing commitment to the community, the News-Press supports more than 100 non-profit organizations each year. Through donated advertising space and cash donations, the News-Press contributes nearly \$250,000 to Santa Barbara area non-profits yearly.



www.towbes.com

The Towbes Group, Inc. is a Santa Barbara based development, construction and asset management company dedicated to providing customer satisfaction. Our company has a history of over fifty years of professional experience in all aspects of residential and commercial real estate development, including construction, development, and property management. We have developed over 5,000 residential units and over 1.4 million square feet of commercial properties. We currently manage 2.0 million square feet of commercial space and 1,800 residential units. Almost all of this development has been in the tri-county area, and a majority has been in Santa Barbara County.

We are pleased to be a sponsor and to support the UC Santa Barbara Economic Forecast.



www.sankofsantabarbara.com

Reversing the national trend of big banks buying local banks in November of 2009, a well recognized group of Santa Barbara business leaders and philanthropists purchased control of the Bank of Santa Barbara from Michigan based Capitol Bancorp.

These local investors shared a vision to create a truly committed Santa Barbara community focused bank. A bank designed not to serve the globe, the state, or even the central coast, but to serve local businesses, professionals, and non-profit organizations from Carpinteria to Goleta.

This change of ownership also came with additional capital to support the needs of our business community. In the first four months under new leadership, the community has acknowledged this change by transferring relationships to grow the Bank by more than 75%.

The Bank of Santa Barbara offers the full array of banking products and services, backed by a commitment to highly personalized service for our neighbors. Every decision is made right here, by experienced local banking professionals who understand your business and our community because they are part of it. These experienced professionals are committed to supporting the people and organizations which make Santa Barbara a special place to live and work.

For us it's a two way street; it's critical the Bank is loyal to our clients in the same way we expect our clients to be loyal supporters of the Bank. Not just in the good times, but especially in the tough times. We are THE BANK of Santa Barbara. We are located at 12 East Figueroa Street and we are open 9:00 a.m. - 5:00 p.m. Monday through Friday or anytime by appointment. Visit us at www.bankofsantabarbara.com or call 805.730.7860.



BARTLETT, PRINGLE
& WOLF, LLP



MISSION WEALTH
MANAGEMENT, LLC

www.bpw.com

Bartlett, Pringle & Wolf, LLP (BPW) and Mission Wealth Management, LLC (MWM) consist of the leading Certified Public Accountants and Wealth Managers on the Central Coast. We provide our clients with the best of both worlds—personalized local service with the knowledge and expertise of a national firm.

To our clients and team members, relationships continue to be a cornerstone to our business for which BPW has served our community since 1948. Offering a full range of financial services, the collective experience of over 75 professionals, including 28 CPAs, are focused on helping clients achieve their goals, strategically plan for the future, meet compliance requirements and be proactive in their quest for opportunity and guidance.

Celebrating the ten-year anniversary of MWM, the integrated services of this nationally recognized firm offers a unique experience for clients. Providing clarity to difficult financial decisions not only saves time but it provides peace of mind. This winning partnership allows clients to evaluate many aspects of their financial landscape in concert with tax, estate, risk and investment choices.

Our professionals have the experience and commitment to provide comprehensive, integrated services across many disciplines. This means that if you need tax or investment services today, a cost segregation study on a building purchased tomorrow and estate planning in the future, our full suite of services are structured to anticipate and keep pace with your ever-changing financial needs.

Together, BPW and MWM offer a complete menu of financial services including:

- Tax Planning and Compliance
- The area's largest Audit and Accounting Department
- Estate Planning
- Financial Planning
- Integrated Wealth Management

- Implementation and support of Microsoft Dynamics business solutions
- Business Consulting
- Bookkeeping Services
- Cost Segregation Studies
- 1031 Exchange Solutions
- Insurance Services
- Forensic Accounting
- Investments
- Risk Management

BPW and MWM successfully help individuals and businesses navigate the myriad of financial issues that face people everyday. Sometimes the solution is simple and other times it is complex. Our clients are comforted that we have seen it before and know how to address the issues to make their lives easier. At the end of the day, it is about people, relationships, communication and experience. When you put all of that together, the client has a winning combination on their side.

To learn more about how BPW and MWM can help you on your path to financial wellness, please call BPW at (805) 963-7811 or MWM at (805) 882-2360.

*Rankings based on average client size for the year ending December 31, 2009 as published in Wealth Manager and Financial Advisor magazines. Securities offered through NATIONAL PLANNING CORPORATION (NPC), Member FINRA, SIPC Advisory services offered through MISSION WEALTH MANAGEMENT, LLC (MWM). California Insurance License #0D35068. BPW and MWM are separate & unrelated companies from NPC.



www.santabarbaraca.gov/Government/Departments/ComDev/

The City has adopted an Economic Development Plan and Implementation Program that contains the following Goal Statement:

To affect and stimulate the Santa Barbara economy through proactive collaboration, teamwork, and establishment of partnerships with the business community, school districts, universities and colleges resulting in replacement of lost jobs, expansion of the diversity of the economic base, and increase of economic activity for sustaining our local economy.

Toward that goal, the City has established a management-level Economic Development Response Team that meets regularly to address specific issues and respond to economic development opportunities. Staff members of the City Administrator's Office and the Community Development Department are charged with implementation of the Plan.

The Redevelopment Agency of the City of Santa Barbara engages in activities in the Central City Redevelopment Project Area that promote economic development and the elimination of blighting influences. Those activities include acquisition and consolidation of property, below-market-rate financing, public-private partnerships, and the provision of affordable housing.



County of Santa Barbara,
County Executive Office

www.countyofsb.org

The County Executive Office (CEO) acts as a key resource to the Board of Supervisors, providing administrative, fiscal, operational, and organizational policy recommendations to the Board, and is responsible for ensuring that the entire organization faithfully implements Board's policies. It is the CEO's role to detect and report horizontal issues, opportunities and trends to the Board in time to take appropriate action, and to keep the Board informed of the socio-economic and political environment of the County through the strategic scan and the strategic planning process.



www.cox.com

Voice, Video and Data services by one incredible company with the highest ratings on customer service, on the most advanced fiber optic network with a company that provided local connections to our community. All this from the people down the street at Cox Santa Barbara.

Cox Business Services offers local businesses access to innovative communication products over an advanced state of the art fiber-based network. Cox Business Services provides for the high bandwidth telecommunications needs of large, medium and small companies in our community. Business phone service is available for small and medium size businesses. Cox Business Video is available with access to the best programming and music available.

Cox Media, the cable network advertising unit, is the most direct method reaching directly into the homes with business messaging over more than 50 cable networks designed for specific product target audiences.

Cox's Digital Cable Service adding to its superior cable television service, more than 180 video and audio channels to Cox's cable television lineup without having to purchase a satellite dish or install an unsightly antenna. Cox HD Service and Cox Digital Video Recording (DVR) devices are also available.

Obtaining faster access to the Internet for your home is why Cox Communications' unique connection is available through the Cox High Speed Internet product.

Cox continues to be a leader in technology as recognized by Cablevision Magazine three times honored as the Operator of the Year. Cox Communications has also been honored twice as the Most Innovative Cable Company Award at NetWorld+Interop by Inter@ctive Week. Cox Communications Santa Barbara consistently receives the National Cable Television Award for Customer Excellence. Cox has recently been awarded JD Powers Awards for small business services, and local phone service.

**www.jordanos.com**

In 1915, when the first Jordano Brother's Market opened in Santa Barbara, a rich tradition of integrity, quality, and service was born. Today, Jordano's has grown to become the 43rd largest independent broadline foodservice distributor in the United States and remains a highly valued member of the local business community.

From its corporate headquarters and warehouse complex in Santa Barbara, Jordano's Foodservice maintains a sales and distribution network that serves more than 35 different market segments in nine key counties throughout Central and Southern California.

Jordano's makes over 10,000 foodservice products available to a diverse customer base that includes restaurants, schools, universities, hospitals, military facilities, casinos, hotels, cruise lines, marine and offshore installations, and federal and state institutions.

Pacific Beverage proudly distributes Anheuser-Busch brands and other fine beers through its four warehouses in the Tri-Counties: Oxnard, Santa Barbara, Santa Maria and Santa Margarita.

Jordano's remains a locally owned company dedicated to providing the best possible products and service to their customers. They are committed to the welfare of their 500 employees and their employees' families in the tri-counties.

**www.noozhawk.com**

Noozhawk delivers the freshest news in Santa Barbara and Goleta, day and night. Since our launch in late 2007, we've established Noozhawk as an accessible, credible and reliable community resource for mainstream local daily news and information — exclusively online at www.noozhawk.com. No other local media source provides more professionally reported content.

We're covering our community in two unique ways: With professional journalists providing original reporting on issues and topics of the day, especially local news and K-12 education, and by inviting community members to share their own stories on the everyday activities with which they're involved. The concept allows Noozhawk to reach more deeply into the community than any other publication.

And if you can't make it to us, we'll come to you — with our free daily e-Bulletin that we deliver to your inbox each day at 4:15 a.m. Your neighbors will never have to see you in your robe again.

We've also got exciting news of our own, with a new look on the way, an iPhone/BlackBerry marketing app powered by Qvew, and a grant from the nonprofit Common Sense California to conduct a civic engagement project for the city of Santa Barbara's budget. You can follow us on Twitter (@Noozhawk) or friend us on Facebook.

We've got affordable, effective advertising and sponsorship opportunities for every budget. Our recently launched Real Estate section is a hit with readers and Realtors and is one of the fastest-growing areas of our site. And we can cross-promote you among our growing family of affiliates: PresidioSports.com, SantaBarbaraSurfer.com, sbparent.com, Pumpflix and KRUZ 97.5-Cumulus Radio.

We're proud to be part of this community and we're privileged to be involved with the UCSB Economic Forecast Project. A healthy economy means a healthy community, and it all starts with business.



paseonuevosshopping.com

Paseo Nuevo Shopping Center, located in the commercial and retail heart of downtown Santa Barbara is the premier shopping destination for locals and tourists. Visitors can stroll the sun-drenched promenade and the winding paseos surrounded by over 70 exclusive local and national shops and restaurants. A unique feature of this outdoor center is the attached Arts Complex which includes the Contemporary Arts Forum and Center Stage Theater.

Anchored by Nordstrom and Macy's, Paseo Nuevo includes such premier destinations as Sephora, bebe, California Pizza Kitchen, Aveda, lululemon athletica, Ben & Jerry's, Abercrombie & Fitch, Pascucci, Aldo Shoes and Cache.



www.pacbiztimes.com

Pacific Coast Business Times is the only weekly business journal serving the Tri-Counties region.

Since its founding in March 2000, the Business Times has built a reputation for accuracy and in-depth reporting and has won numerous national and regional awards including a "Blue Ribbon" small business award from the U.S. Chamber of Commerce in 2007.

The Business Times operates the largest financial news team between the San Fernando Valley and the Silicon Valley. Each edition offers subscribers a variety of news and information, including sections on technology, small business, personal finance and our must-read "Top 25" lists.

Included with each subscription are more than 20 special reports including Dealmakers of the Year, Best Places to Work, a Year-end Tax & Financial Planning Guide and a

number of Who's Who sections that profile the major players in a number of industry segments. Subscriptions also include a copy of our Book of Lists, the region's most comprehensive directory of business-to-business connections.

The Business Times also produces six major business-to-business awards events each year. These events offer special sponsorship and networking opportunities and a chance to get to know the region's top private sector companies.

The Pacific Coast Business Times is delivered primarily through subscription at an annual price of \$49.99 for 52 issues.

A full-time staff in editorial, advertising sales and circulation is eager to help and serve you. For subscription or advertising information, please contact us at 805-560-6950. Or visit us online at www.pacbiztimes.com for news or to sign up for our free email newsletter.



www.radiusgroup.com

Radius Group Commercial Real Estate is the dominant full-service commercial real estate brokerage firm on California's Central Coast. On an annual basis, Radius Group brokers finalize an unmatched volume of commercial sale and lease transactions.

Radius Group provides the strong community engagement and dedication to clients' needs that only a proven team of real estate professionals can support. Radius Group also contributes to the business community with its sustained industry data reporting and market forecasting. With a unique team philosophy as its backbone, Radius Group maintains the distinct ability to not only meet their clients' requirements, but go above and beyond to produce desired results with a high degree of diligence and flexibility.

Should you have any questions please do not hesitate to contact me.

Thank you,

Melinda Bie, Director of Operations
Radius Group Commercial Real Estate, Inc.

205 E. Carrillo, Suite 100 | Santa Barbara, CA | 93101

Tel: 805.965.5500 | Fax: 805.965.5300 | Direct: 805.879.9610

mbie@radiusgroup.com | www.radiusgroup.com



www.sssseeds.com

S&S Seeds inc is a primary wholesale supplier of drought tolerant and native plant seed. We feel our chief distinction is service and fine quality seeds. We have research and development trial fields for evaluation of new and old species. Our production fields and extensive collections of native plant seed allows us to offer more than 900 plant species, including wildflowers, native and reclamation grasses, trees, shrubs and native plants.

We utilize state of the art seed cleaning equipment to process seed and by continually testing for purity, germination and pure live seed counts at certified laboratories, top quality seeds are assured.

Santa Barbara DAILY SOUND

www.thedailysound.com

The Santa Barbara Daily Sound, a free daily publication serving southern Santa Barbara County from Carpinteria to Goleta, focuses on local community news with an unbiased outlook. The Daily Sound is published Monday through Friday and is distributed to over 250 single copy locations throughout the south coast.

In 2006, Editor and Publisher Jeramy Gordon founded the paper as an alternative source for daily news. Since its first publication in March, the paper has quickly grown into a mainstream news source for local information.

As a free circulation newspaper, the Daily Sound relies on advertising to survive. With competitive rates, businesses of all sizes are able to advertise effectively and affordably. The Daily Sound prides itself on community involvement and sponsors many local events at all levels.



www.wib.ventura.org

The Workforce Investment Board is dedicated to serve the workforce needs of businesses, adults, laid-off workers and youth throughout Santa Barbara County. The WIB is a public/private partnership created by the Federal Workforce Investment Act legislation and is staffed by the County of Santa Barbara. We provide free services through the two Workforce Resource Centers (One-Stops). Programs include employment services for job seekers, the latest labor market information, and regional workforce research for businesses as well as training that specialize in helping people gain the skills and confidence necessary to find and obtain a job. We partner with the two local community colleges for training and skills updating in order for job seekers to be prepared for job opportunities. The Workforce Investment Board also provides summer and year-round youth employment programs as well as gathers relevant industry information and data necessary for business success. The Workforce Investment Board is dedicated to ensuring the long term economic success of Santa Barbara County by supporting the needs of employers and pairing that need to find qualified workers with the job seekers' need for career opportunities.



www.uphamhotel.com

The Upham Hotel and Country House, located in the heart of Santa Barbara's historic downtown, is a garden oasis convenient to boutiques, gourmet restaurants, performing arts theatres and museums. The hotel offers 58 unique accommodations including luxurious suites and cottages, some with fireplaces. Well appointed rooms include the special touches that discerning travelers appreciate: spa quality bath products, plush terry cloth robes, down comforters and pillows, and fresh cut flowers. Business travelers appreciate the complimentary wireless internet access and parking. Room rates include a deluxe continental breakfast buffet, afternoon refreshments of fruit, wine and cheese, and Oreo cookies with milk in the evening.

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Best,
Marjorie Robertson
Upham Hotel
805-962-0058



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www.cottagehealthsystem.org

Cottage Health System, formed in 1996 as the parent organization of the following not-for-profit hospitals, is guided by a volunteer board of directors from the greater Santa Barbara community. Its mission lies in providing superior health care through a commitment to our communities and to our core values of excellence, integrity and compassion.

Santa Barbara Cottage Hospital

Today a 408-bed acute care teaching hospital and trauma center, the largest of its kind between Los Angeles and the San Francisco Bay Area, the hospital was founded in 1888 by 50 women determined to provide a healthcare facility for the growing community of Santa Barbara. Now with annual admissions of almost 19,000 patients, 38,500 emergency department visits, and 2,500 births, the hospital is renowned for its comprehensive maternal-child and pediatric services (Cottage Children's Hospital), cardiac, neurosurgical, neuroendovascular and oncology programs, emergency and trauma services, modern operating rooms, sophisticated diagnostic radiology equipment, outpatient imaging center, outpatient surgery, eye

center, rehabilitation services (Cottage Rehabilitation Hospital), and psychiatric and chemical dependency services. Its medical staff of more than 600 includes specialists in all major clinical areas, many of whom are involved in the training and education of new physicians in the hospital's internal medicine, general surgery and radiology residency programs.



www.dyersheehan.com

Dyer Sheehan Group, Inc. (“DSG”) provides a broad range of professional services to the real estate investment and development communities, as well as to governmental agencies and financial institutions. In addition to offering expert brokerage services involving apartment or NNN leased investments, and land for development; DSG conducts detailed market research, feasibility, and other specialized studies, to address specific real estate issues. Dyer Sheehan Group studies over 19,000 Ventura County apartment units, and 5,000 Santa Barbara County apartments on a semi-annual basis. The resulting survey summary data, along with a professional market perspective, is published annually by the UCSB Economic Forecast Project. DSG President, Dawn Dyer, is proud to be a member of the Ventura County Board of Directors of the UCSB-EFP.

Dyer Sheehan Group also specializes in analyzing residential development projects, negotiating complex land use and entitlement permit issues, and building political consensus for the approval of: General Plan Amendments, Zone Changes, Planned Development

Permits, Tract Maps, Annexations, and Local Coastal Plan Amendments. DSG Principals have demonstrated a strong ability to facilitate open and productive dialog, enabling decision makers, community groups, and developers to work together to create development projects which are consistent with the vision and priorities of the specific locale.



FARM CREDIT WEST

www.farmcreditwest.com

Farm Credit West (which is composed of Farm Credit West, FLCA and Farm Credit West, PCA) is a borrower-owned cooperative providing credit to producers of food, fiber, and flowers in Kern, Kings, San Luis Obispo, Santa Barbara, Tulare, and Ventura counties. Farm Credit West is pleased to sponsor this Economic Outlook program in an effort to better document agriculture's important role in California economy.

As a lender specializing in a single industry--agriculture--Farm Credit West is dedicated solely to proving that THE CUSTOMER COMES FIRST by providing superior customer service at competitive rates. For the past six years the Association has returned cash patronage refunds to its borrowers; in each of 2005 and 2006 those refunds averaged 0.50% of the customer's average borrowings.

The Board of Directors for Farm Credit West is composed of agricultural leaders who ensure that the Association provides the highest quality, value-added service by developing an in-depth understanding of California agriculture. Capitalizing on its customer-driven specialization, Farm Credit West is the premier originator of agricultural operating and mortgage loans in its territory. Other services offered include lease origination and fee appraisals.

Visit www.FarmCreditWest.com for more complete information.



First American Title

www.firstamericantitle.com

Evolving from a one-county abstract company in 1889, The First American Corporation is now a diversified, international business information products and services provider and a recognized FORTUNE 500® company. First American brings the strength and expertise of more than 35,000 employees and 2,100 offices and an extensive network of agents throughout the United States and abroad to the nation's businesses and consumers. Using proprietary or public records, First American gathers data and forms it into useful, decision-ready information products and services. By truly focusing on the needs of the consumer, First American has developed services and technology that are increasingly flexible, efficient and cost effective.

With headquarters in Santa Ana, California, First American's role in buying a home includes providing all the related services needed to complete a home purchase including real estate appraisal, title insurance, flood-zone determination, mortgage document preparation, property and casualty insurance and more.

On a local level, First American Title continues to be #1 in overall market share in the resale, refinance and new home markets. Karen Chackel, County Manager, directs five offices in the county - Santa Barbara, Montecito, Santa Maria, Lompoc and Solvang - and is dedicated to providing excellent service with integrity and professionalism.



www.hacsb.org

The Housing Authority of the City of Santa Barbara (HACSB) is a local public agency created for the purpose of providing safe, decent, and high quality affordable rental housing to persons and families with limited incomes. The Housing Authority strives to craft creative solutions to the Community's affordable housing demands in a holistic manner. The Authority's dedicated Commission and Staff ensure that HACSB continues to be a well-managed, compassionate and effective service provider as opposed to a public bureaucracy. The results of this vision are many and include a hard working, high quality and fiscally sound organization with objective goals and measurable achievements. To this end, the Housing Authority currently provides affordable housing to approximately 3,200 low-income households in south Santa Barbara County through a variety of programs. This includes public housing that we own and operate, congregate living facilities for frail seniors, supportive housing for the homeless as well as the Section 8 Housing Choice Voucher program which subsidizes rents for low income households in private rental housing. Through Section 8 alone, the Housing Authority infuses nearly \$25 million per year in federal tax revenue to the South Coast economy.

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U.S. Forecast

by Christopher Thornberg

Beacon Economics

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The Big Picture: Not out of the Woods Just Yet

Any discussion of the 2008–2009 recession will necessarily include a litany of “worst since the Second World War” caveats. The decline in real economic output, the decline in international trade flows, the proportionate and total losses of jobs and real income, the rise in the unemployment rate and the decline in business spending all were at record levels. The best that can be said is that the more bearish predictions of a complete global economic meltdown did not come true. Whether this is due to the massive bailout of Wall Street banks—and bankers—as has been stated countless times by those behind the bailout plans or simply because the risk of such an event was overstated will never be known.

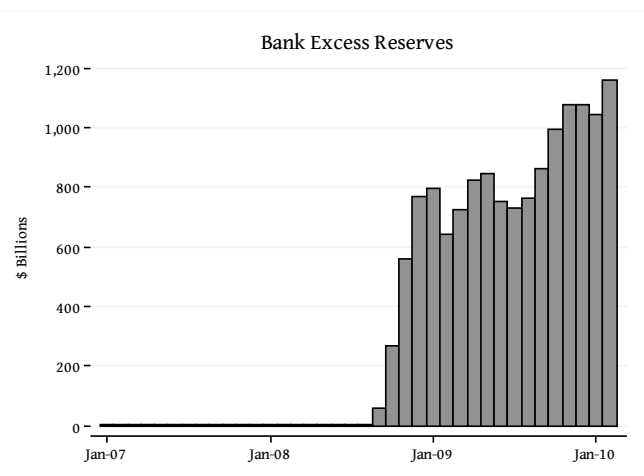
More important, the recession has come to an end. All signs point to it, from housing prices to labor markets, economic output, and, of course, the financial markets, which have been positively giddy over the past 12 months. And banks are starting to loosen their purse strings—recent figures from the Federal Reserve Lender Survey show banks loosening their credit standards and reducing the rate premiums they charge borrowers. The big question now is, how sustainable will the recovery be?

...less than half the stimulus money has been spent—\$151 billion is in process right now, and another \$321 billion will be spent this year. With this kind of boost, 2010 could end up being a very strong year.

Our view on this has been changing in recent months. We are becoming more 'optimistic' in the short run. Recovery is already underway and much of the stimulus has yet to hit the economy. For example, the Federal Reserve has injected unprecedented amounts of liquidity into the economy, but much of this boost

The nation seems to be trading in its private bubble for a public one, swapping one set of unsustainable economic drivers for another.

never made it to Main Street—in fact most has been absorbed by the banking sector in the form of excess reserves. With bank lending starting to flow again some of that \$1.2 trillion could hit the economy this year. Let us not forget to mention all that stimulus spending that is still trying to find a project to fund. According to the website Propublica, less than half the stimulus money has been spent—\$151 billion is in process right now, and another \$321 billion will be spent this year. With this kind of boost, 2010 could end up being a very strong year.



Of course we used the word 'optimistic' in quotes, because a solid 2010 does not necessarily mean a good 2011 or 2012. Indeed, we are also becoming more pessimistic in the medium run. Although having growth return in the short run is clearly a good thing, it has not occurred because the U.S. economy has moved beyond the issues that plagued it at the start of the recession two years ago. Rather it is due primarily to fiscal and monetary policy.

While these actions have done what they were intended to do—namely, stabilize the economy—they come with a cost. First, the interventions are creat-

ing their own set of potential imbalances—an out-of-control Federal deficit and the potential for massive inflation. Second, these programs have slowed the closing of the imbalances in the economy that pushed us into the recession in the first place, and in some cases the problems are actually getting worse.

In short, the nation seems to be trading in its private bubble for a public one, swapping one set of unsustainable economic drivers for another. And as with all bubbles, the pop, when it occurs, will likely prove painful.

What are these ongoing imbalances? They include consumer spending, which is currently at an all-time high percentage of personal income. The recent rise in savings rates is an illusion created by the record tax cuts that were part of the stimulus package. The banks aren't out of the woods yet, either. The collapse in asset values has left banks with many underwater loans. This has been covered up by changes in the accounting rules—but the losses will still need to be accounted for eventually. Rising home prices mask the fact that over 6 million mortgages are currently nonperforming in the United States—a supply that will eventually need to be addressed.

The rally in the equity markets seems to be occurring despite the fact that overall asset prices still seem too high given our long-run potential for growth. And the bounce in the asset markets overlooks the fact that overall the national deleveraging that needs to occur to shed off record levels of debt has yet to really get underway. It's clear that the economy is far from being on stable footing.

But if you are reading this report hoping for some clearer sense of what comes next, we apologize up front for not being able to deliver a clearer picture of the U.S. economy. Forecasting in normal times is a difficult challenge, true to the cliché that it is as much of an art as a science. And right now the economy is a forecaster's nightmare—it is in a place it has never been, with challenges ahead it has never seen before.

Forecasters who think they have a clear vision of how it is all going to play out are either fools or frauds.

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The best-case scenario is that the Federal Reserve and the Obama administration manage to draw down the public bubble slowly, a possibility that private bubbles typically don't share. In this situation, they manage to pull back on the stimulus slowly (The Fed gradually withdraws the excess liquidity, the Federal Government is able to close the budget deficit slowly, the FDIC manages bank failures on a gradual basis, and so on) as the economy heals and meets the ongoing challenges. But this will require a delicate touch, to say the least—one unfortunately not normally associated with congressional politics. In such a scenario, the 2010 boom will be followed by a period of slow growth, perhaps for two years or more.

The worst-case scenario is that the bubble pops rapidly, putting the economy squarely back into another recession—the double dip. The potential sources of such a scenario come from many directions:

- The Federal Reserve might not be able to contain the beast it has unleashed, and the new liquidity-driven financial bubble could continue to grow despite efforts to slow it down, until it painfully pops of its own accord.
- Inflation could change from cold to hot quickly, forcing the Fed's hand. Rates could spike as a result, the dollar could drop in value, and the real cost of borrowing could hit very high levels.
- The global sovereign debt worries could affect the United States, causing the cost of borrowing to rise sharply and forcing the U.S. government to adopt some degree of rapid fiscal austerity.

So enjoy 2010—it should be a good year. But don't overextend.

- The financial markets could get hit by one or two large defaults—perhaps caused by a public debt default in Europe (read Greece) or from some other direction yet to be revealed. Or the stock market could crash and this time the Federal Reserve—largely out of bullets—could do little about the consequences.

So enjoy 2010—it should be a good year. But don't overextend. The one thing you can count on is that economic volatility will be the watchword for the next few years. The U.S. economy is surely in a better place than it was two years ago, but we are not yet in a position to enjoy another extended expansion. And this shouldn't be a surprise. The problems that put us here built up over more than a decade. It is going to take time to work our way out of them.

In the meantime, count your blessings—because even an unstable U.S. economy offers its citizens one of the highest standards of living in the world, something that Americans too often forget in uncertain times.

The 2010 Economic Rebound

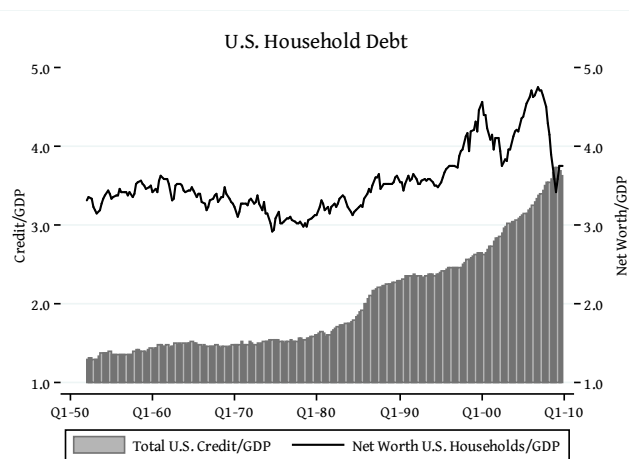
To understand where the economy is today, we have to first understand how we ended up in this particular position in the first place. The roots of the recession began not with the failure of Lehman Brothers, but back in the mid-1990s. It was then that the great

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financial bubble began to form in the U.S. economy. Over the next 13 years, U.S. asset prices, for stocks, bonds, homes, commercial real estate, and so on, rose

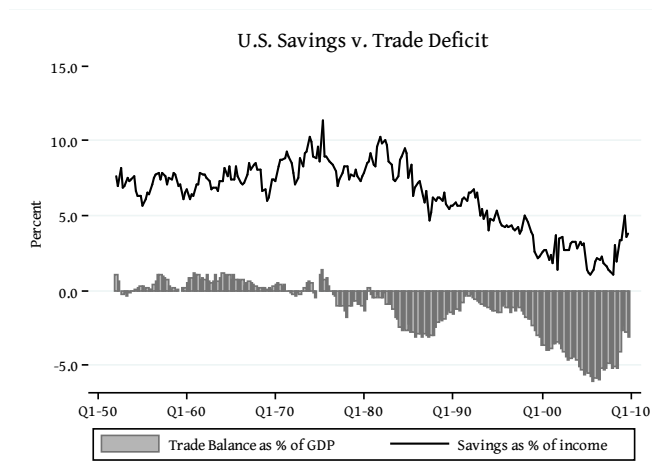
to levels that simply made no sense, given long-run productivity growth in our economy.

One way of seeing this is by considering the basic relationship between the net value of the U.S. economy (U.S. household net wealth) relative to U.S. GDP—our national P/E ratio. Given that the U.S. economy grows at a fairly stable rate (roughly 3% per year in real terms) the value of assets in our economy should be proportional to overall economic output over time.

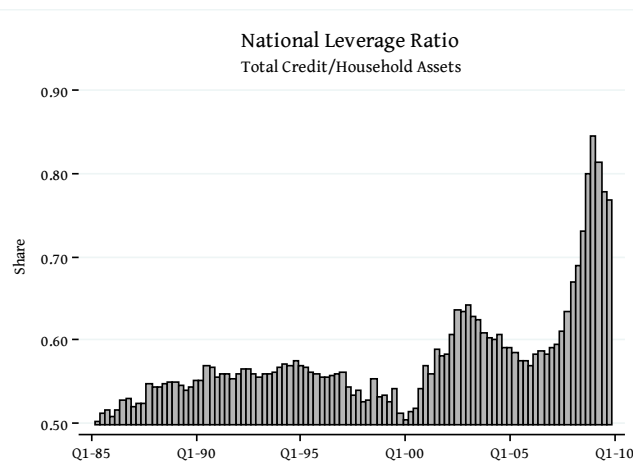


The P/E ratio for the U.S. economy, which had ranged between 3 and 3.5 since the statistic first started being measured after World War II, for whatever reason shot up to 4.7 between the mid-1990s and the start of the last recession. In other words, the market value of the U.S. economy was far too high given our true ability to meet those future claims. Indeed, it could be argued that the U.S. economy was “overvalued” by something on the order of \$15 trillion to \$20 trillion.

Overall, the gross amount of debt in the U.S. economy grew at twice the pace of the overall economy between 1995 and 2008, leaving the nation with record levels of debt. Indeed, this debt is still a large issue for the U.S. economy.



Along with this increase in asset values came an increased use of credit by banks, consumers, businesses, and everyone else. Overall, the gross amount of debt in the U.S. economy grew at twice the pace of the overall economy between 1995 and 2008, leaving the nation with record levels of debt. Indeed, this debt is still a large issue for the U.S. economy. Even though asset price collapses have pushed the P/E ratio down to a figure with a closer resemblance to normalcy (though still high from a long-term perspective), overall debt levels remain quite high relative to GDP even now—consider the following graph that shows the total value of credit in the U.S. economy to the growth value of all assets held by consumers. This leverage ratio has come down some, but still has a ways to go. The process of deleveraging has yet to fully work its way through the system.



The problems haven't only been on the financial side of the ledger. American consumers, convinced that they were rich and getting richer at a record pace, began to save less and less of their income, and as a direct result the U.S. economy began to run a record large trade deficit. In other words, the U.S. economy developed a structural problem to go along with the accounting problems. Too many resources—capital and labor—were being devoted to real industries supporting consumer spending, home building, finance, and imports, which in turn were growing excessively due to the bubble. Too few resources were being devoted to exports and business investment.

What is perhaps most amazing about this past economic downturn isn't that it happened. The downturn was inevitable, and when the bubble popped, the financial havoc was going to be intense. It was inevitable that the U.S. economy—and therefore the world economy—was going to go through a painful period of recalibration as resources were reallocated to sustainable long-run uses. What is truly shocking is

It was inevitable that the U.S. economy—and therefore the world economy—was going to go through a painful period of recalibration as resources were reallocated to sustainable long-run uses.

how many economists argued that the economy was fine even as late as the middle of 2008, even as things had already started to implode.

Now there are clear signs of growth in the economy. GDP growth in the fourth quarter hit nearly 6% in real terms. Admittedly, much of this growth was the end of the inventory runoff, but aggregate demand growth was still well into positive territory (albeit below its long-run average). Consumer spending has been on the rise, as is business spending on equipment. Furthermore, real exports rose faster than imports in the fourth quarter. This is one of the reasons that the industrial part of the economy is also doing well. Industrial production has increased and capacity utilization is rising sharply.

Contributions to Real GDP Growth by Sector (SAAR)

	87 to 07 Avg.	Recess. Avg.	2009-IV
Gross domestic product	3.05	-2.40	5.90
Personal consumption	2.18	-0.86	1.23
Durable goods	0.47	-0.66	0.02
Nondurable goods	0.42	-0.31	0.64
Services	1.29	0.11	0.57
Gross private investment	0.66	-3.32	4.63
Structures	0.04	-0.41	-0.47
Equipment/software	0.51	-1.10	1.09
Residential	0.03	-0.87	0.13
Change in inventories	0.07	-0.94	3.88
Net exports	-0.12	1.23	0.30
Exports	0.67	-1.02	2.32
Imports	-0.80	2.24	-2.02
Government	0.34	0.54	-0.23
National Defense	0.02	0.38	-0.19
Nondefense	0.05	0.13	0.21
State and local	0.27	0.03	-0.25

Source: Bureau of Economic Analysis

Housing construction and the labor markets have not shown much of a rebound as yet, but even here the news is better. The labor markets have at least stabilized, and unemployment rates have fallen slightly. There are a number of signs that recovery in employ-

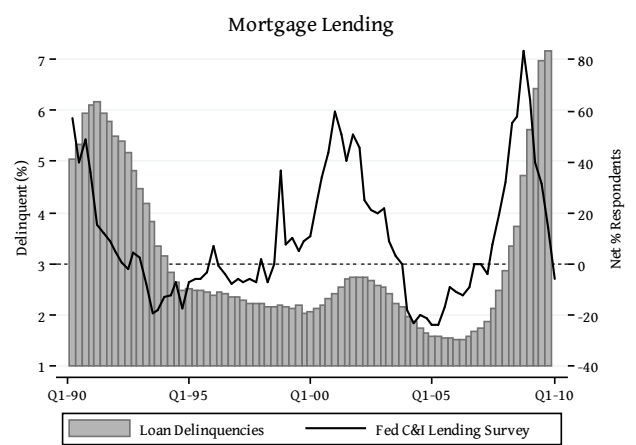
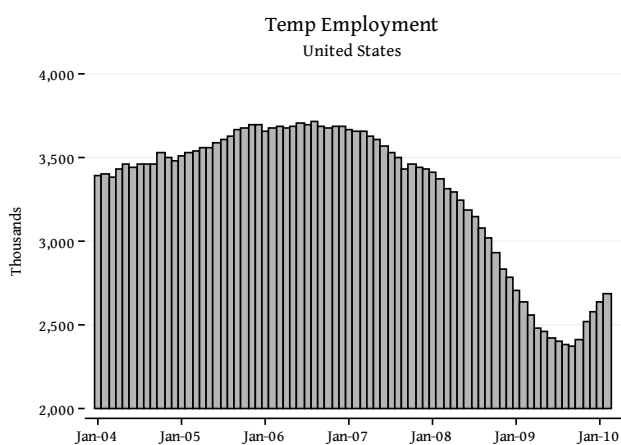
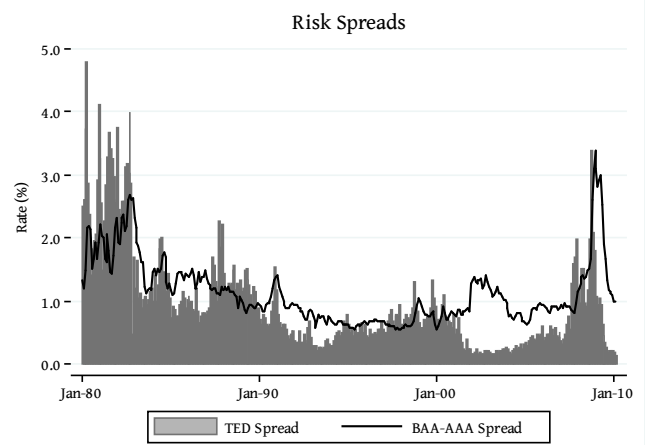
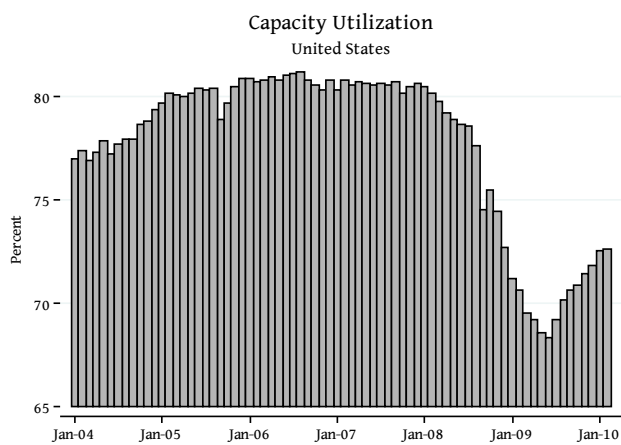
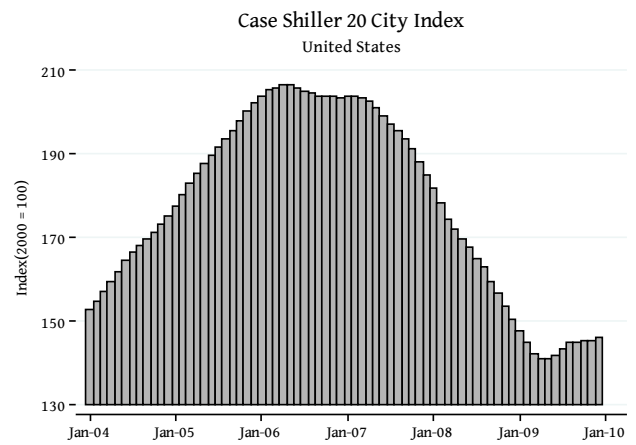
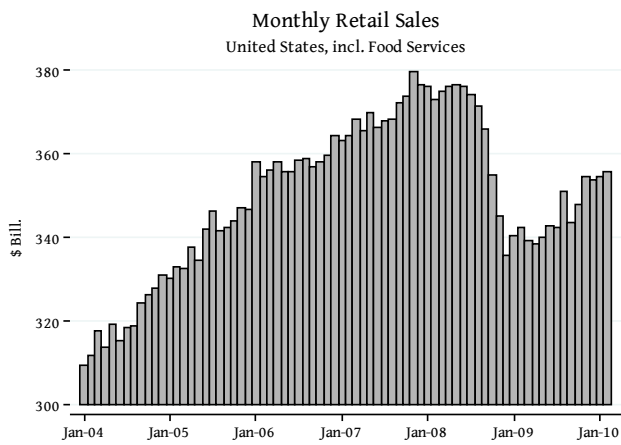
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ment will be starting in the next few months. Weekly hours worked has been rising among employed workers, and temporary employment has seen sharp increases. Similarly, even though housing starts and permits continue to sit on the bottom, home prices have been rising as sales in some markets have been looking solid.

Perhaps most impressive is the rebound in the financial markets. Of course, the equity markets are way up from last year at this time, as has been widely reported in the press. But the bounce is deeper than seen in the major indexes. After hitting record high levels in the midst of the crisis in late 2008, risk premiums have come way down. The so-called TED spread¹ has dropped to almost nothing, as has the record spread between seasoned Baa and Aaa corporate bonds.

Companies in need of refinancing outstanding debt are finding the process easier than they thought. In the middle of 2009, as the economy swooned, many bond experts predicted that 2010 was going to be one of the worst years ever for corporate bond defaults. Instead, given the data on loan problems to date, this year may end up being a below-average year for defaults.

¹The difference between the 3-month T-bill interest rate and the 3-month LIBOR interest rate.



The banking sector has also been a surprise. While Federal Reserve data shows that loan delinquencies continue to rise, the recently released data from the Senior Loan Officer Opinion Survey on Bank Lending Practices shows that lending terms on many sorts of loans have actually begun to ease. This is completely out of sync with past data that shows lending terms only loosening with a substantial decline in the rate of delinquency.

As noted, this rebound in the economy owes more to government policy than strong fundamentals. While we have all heard bits of information about the interventions, it may be worthwhile to put them into one place.

- The Federal Reserve has reduced short-run rates to near zero. The Fed has also embarked upon an aggressive plan to lower long-run rates through quantitative easing—a fancy term for printing money. The Fed has added almost \$1.3 trillion to the monetary base—one of the most aggressive expansions on record.
- The Treasury has been involved in many direct support programs—from bailing out AIG and the GSEs (government-sponsored entities) to managing the spectacularly underperforming PPIP (the Legacy Securities Public-Private Investment Program) and of course TARP. It has also been running the HAMP programs that are designed to encourage the modification of mortgages for delinquent homeowners.
- Congress and the Obama administration have also been involved, with a nearly \$1 trillion stimulus program that does everything from cut taxes to backfill state welfare systems, direct spending on various infrastructure projects, and provide a tax credit for home purchases. A controversial change in the FASB rules has also been passed, addressing how banks and other financial institutions value loans.
- The FHA, which after years of being more or less pushed out of the home lending market, has come

back with a vengeance, insuring home purchase mortgages at a record pace.

The potential consequences of these interventions are clear. Federal debt levels will rise to 70% of GDP within 5 years according to current estimates. It will likely get there more quickly, given that much of the bailout tab has yet to be fully recognized on the public books. In addition, there is the issue of the monetary base expanding by 150%. If the velocity is held constant, this implies that prices in the U.S. economy should also rise by 150% within the next five years—a rate of inflation that makes the 1970s look tame.

The potential consequences of these interventions are clear.

Of course, the challenges raised by these interventions are worth it if these actions get the economy moving again. But there's the rub. Even though the economy is currently expanding, the problems in our economy are still profound. As the stimulus is unwound, it remains to be seen whether the momentum of current growth will allow us to take these problems in stride. If not, the economy will quickly tumble back into a recession.

To illustrate the problems still entrenched in the economy we will first take a deeper look at two sectors: real estate and consumer spending. In each case, the positive signs on the surface mask problems underneath. Next, we will take a closer look at Federal Reserve policy and what it may mean for inflation.

Real Estate

Home prices started to bounce back in 2009 as sales began to heat up. While the national numbers are modest, some markets are positively hot. Cleveland, Memphis, the San Francisco Bay Area, Denver, and St. Louis all saw double-digit increases in median prices in 2009

according to the National Association of Realtors. The number of bank owned “REO” units has also been in decline.

Policy, not fundamentals, is driving the real estate market—a telling analogy for the force behind the U.S. economy overall.

The Case-Shiller Home Price Index offers additional evidence of price growth, with more accurate data broken down by market. The following table lays out the Case-Shiller estimates of price growth from June to December by tier of housing. While a few of the markets still lag, others have shown significant price gains—particularly at the low end of the market.

Case-Shiller Home Price Index

Price Growth by Tier, Jun-09 to Dec-09, (% SA)

	Low	Middle	High
Las Vegas	-2.7	-4.3	-3.0
Tampa	0.0	-1.5	-2.3
New York	0.1	-0.1	-0.8
Seattle	1.1	-0.6	0.1
Miami	1.9	-1.2	3.2
Chicago	7.8	1.3	1.1
Denver	5.7	1.1	0.9
Portland	0.4	2.5	1.7
Atlanta	7.0	3.1	1.4
Boston	4.2	2.2	2.4
Washington, D.C.	7.4	5.5	3.6
Los Angeles	7.5	7.2	4.2
Phoenix	19.6	5.7	2.3
Minneapolis	22.4	6.5	5.1
San Diego	11.7	7.2	3.4
San Francisco	11.5	7.6	4.5

Policy, not fundamentals, is driving the real estate market—a telling analogy for the force behind the U.S. economy overall. In the real estate sector, policy has created a big demand push even as it has restricted supply. Buyers are enjoying record low interest rates

due to the Fed’s policy of “quantitative easing,” where money is printed and used to buy debt being issued by Fannie Mae and Freddie Mac. Similarly, the FHA has vastly expanded its presence in the market over the past two years, guaranteeing a record number of mortgages. And, of course, there is the homebuyer tax credit program (scheduled to end at the end of April). The original deadline for the program, November 30, 2009, drove a number of people into the market, leading to an uptick in sales; it remains to be seen if the new deadline will lift sales in March and April.

All of these programs have a limited lifespan. Fed Chairman Ben Bernanke has to worry about the inflationary pressures created by the expansion of the money supply. The FHA’s portfolio is seeing record increases in delinquencies. In the very near future, the government will be reaching into its wallet to bail out this institution (as well as its banking counterpart, the FDIC) to the tune of hundreds of billions of dollars.

And even though the housing industry strongly pushed for and received an extension of the tax benefit, it is only the last two or three months of such programs that really create the desired result of expanding sales. It is the end of such programs that makes them work in the first place, as it forces people to get into the market before the program ends as opposed to sitting on the sidelines waiting for prices to fall further. Note how sales have been falling for the last three months after the initial deadline. The new deadline is already showing less of an impact. To extend them indefinitely takes away their very purpose.

The largest issue, however, is that of foreclosures. Although much has been made of the various homeowner rescue plans, they have had little to no impact on the pace of foreclosures, or on the eventuality that these problem mortgages will ultimately have to be taken over by the banks. Instead, they have only slowed the process down.

According to the Mortgage Bankers Association, almost 13% of all mortgages (on properties with 1 to

4 residential units) were nonperforming at the end of 2009—this includes those that are seriously delinquent or somewhere in the foreclosure process (but not yet REO). For the MBA this implies that there are 5 million nonperforming loans out there. Of course, they only cover 80% of the market; hence we can estimate that nationally this number hits 6.2 million.

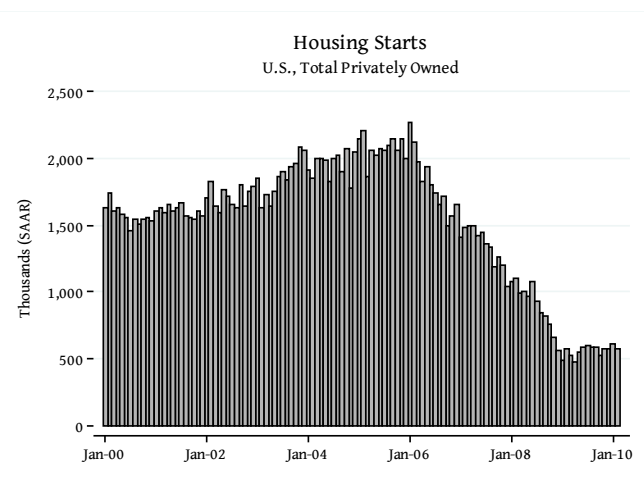
As with many policies, the HAMP loan modification plan is a policy designed to fight the last war, when it was interest rate resets that caused foreclosures. Today, the problem is that an enormous number of homes are underwater—the mortgage value is greater than the value of the home. Modifying loan payments will not solve this problem. To date, the HAMP program has only permanently modified 160,000 loans, with another 90,000 modifications close to being completed. This is a proverbial drop in the bucket relative to the scale of the problem.

Although much has been made of the various homeowner rescue plans, they have had little to no impact on the pace of foreclosures...

It might be hoped that rising prices would help the situation. But bear in mind that overall prices have fallen by 33% in the 20 metropolitan areas tracked by the Case-Shiller Home Price Index. In the areas hardest hit by mortgage problems, home price declines are closer to 45%, and for the big four (Nevada, Florida, California, and Arizona) the number is 55%. Home prices fell because they had reached unsustainably high levels during the course of the bubble. They will not reach these levels again under normal circumstances (read—normal inflation rates) for many, many years. Indeed in many markets prices have not even gotten back to 2000 levels relative to incomes—a time when prices seemed close to their long-run sustainable levels.

Nor can we expect much in the way of a recovery in housing construction. The last few years saw annual

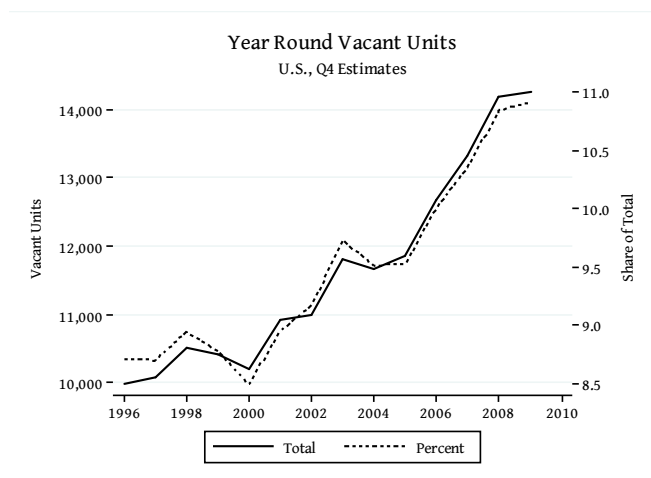
housing completions top 2 million units in a nation that needs perhaps half as many units to meet the demand of population expansion. The cumulative number of housing completions outstripped the number of new households by more than 3 million over the past decade. The second quarter housing vacancy report from the census shows that the share of year-round empty units stands at 10.7%, or 1.7% above the rate it was at in 2002. This implies that there are still 2.5 million too many units in the system. Thus, while some areas will need quicker recoveries, many will not see substantial building for years.



The nonresidential construction market has been the one positive surprise in the system. Construction tanked in the first quarter of 2009 but started to stabilize in the second quarter. While spending on retail, office, and warehouse space, as well as on hotels, has dropped, spending elsewhere—on infrastructure (especially specialized structures such as schools, hospitals, and manufacturing plants)—has largely offset the declines. Further, the great wave of commercial delinquencies has yet to emerge, contrary to predictions and despite rising vacancy rates and falling rents. This is surprising, given that even optimistic experts in the industry recognize that prices have fallen at least 30% in the hardest-hit markets.

Mortgages 60+ Days Delinquent or in Foreclosure

	Q4-06		Q4-08		Q4-09	
	Share	Number	Share	Number	Share	Number
West North Central	3.05	83,550	5.59	158,294	7.35	203,228
West South Central	4.39	176,442	6.21	269,178	8.00	343,164
East South Central	4.49	90,383	7.01	151,487	9.25	197,198
New England	2.47	45,455	6.47	123,868	9.54	179,384
Mid Atlantic	3.11	146,819	6.76	330,800	10.14	490,646
Mountain	2.17	81,290	7.75	307,310	11.74	452,954
East North Central	5.11	306,374	8.88	555,175	12.08	723,905
Pacific	1.59	121,097	8.56	684,908	12.34	969,141
South Atlantic	2.83	272,027	9.74	998,105	14.00	1,401,471
Total		1,323,438		3,579,125		4,961,091



Once again, there is a worrisome backdrop to the story. Lenders have little incentive to be aggressive toward commercial property investors who are unable to meet balloon payments or fall short on loan covenants. Banks are already under substantial duress and the change in the Financial Accounting Standards Board (FASB) rules gives great leeway on how potentially problematic loans are valued. Extend (the terms of the loan) and pretend (the loan is healthy) has become the rule of the day for banks' survival, despite the fact that this formula relies on deceiving investors about the true state of their loan portfolios. Combine this with low short-run rates that take some of the pressure off the borrowers with adjustable-rate loans, and we can see that the wave of commercial delin-

quencies is still in the offing, it has just been temporarily frozen in its path.

Consumer Spending and Public Deficits

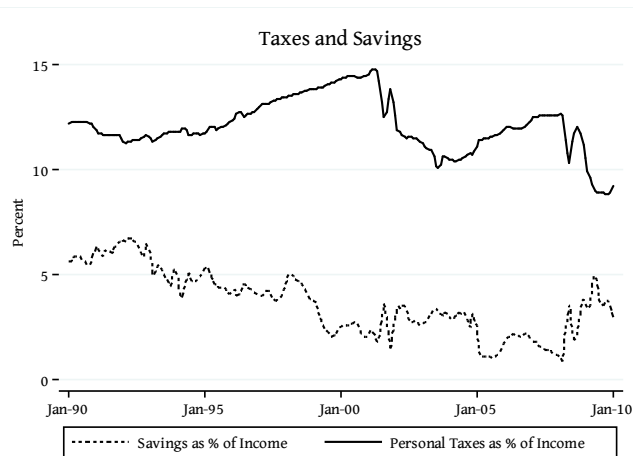
As noted, consumer spending was clearly too high at the onset of the recession. With savings rates at near zero and debt levels at a record high of 120% of annual income (at the start of the decade this figure was roughly 80%) spending had to come down some. And it did, with the expected results for the economy. Now, personal savings rates are running slightly over 3% of income—still too low from a long-run perspective, but moving in the right direction. More important, consumer spending is on the rise as well, which is clearly good news for the economy in the short run.

But, the fact that it is rising should be raising warning flags. After all, real income was battered by the loss of jobs and has yet to recover at all. How can Americans be spending and saving more even as they earn the same amount? That good trick came via the record cut in taxes Americans received in 2009 as part of the stimulus program, as well as from the progressive nature of our tax system. Americans had been paying roughly 12% of their income in taxes at the start of

the downturn. Last year that number was down to a record low 8.8%.

...the wave of commercial delinquencies is still in the offing, it has just been temporarily frozen in its path.

It may be the case that savings is larger than it appears—after all, as we saw in the last section, millions of households are enjoying housing services without bothering to pay the mortgage. Unfortunately, this income transfer does not appear in the BEA income statistics. But it can't be that much. If each of the 6 million nonperforming mortgages in the nation cost on average \$1,500 per month and was not paid for a full year, this still would only add roughly 1% to consumer incomes. It simply isn't large enough to swing the statistics one way or the other. So what this means is that consumer spending as a share of income is currently at a record high—and rising. The consumer part of the problem has not been solved.



Of course, if the government makes the tax cuts permanent, this would solve the problem. Unfortunately, this is not a valid option. The U.S. government had serious debts coming into the recession. The Bush administration chose to fund its Middle East adventures not through tax increases but through borrowing. For a while the public sector needed to borrow an amount

roughly equivalent to 6% of GDP—roughly the level of borrowing through much of the Reagan and George H.W. Bush administrations. But the bailout plans took this to a level not seen since World War II, with the current pace of borrowing reaching 11% of GDP — \$170 million per hour, or \$4 billion per day.

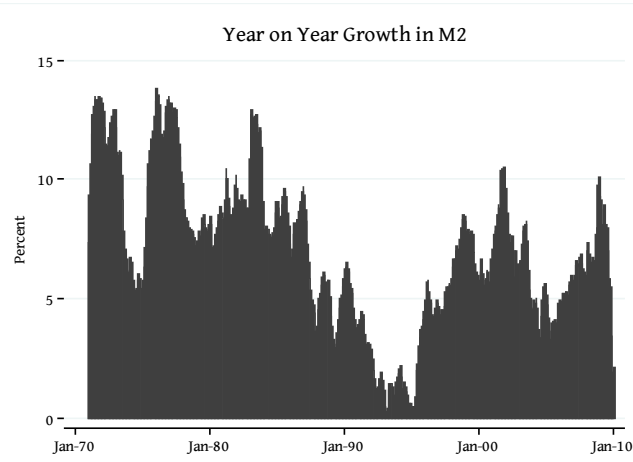
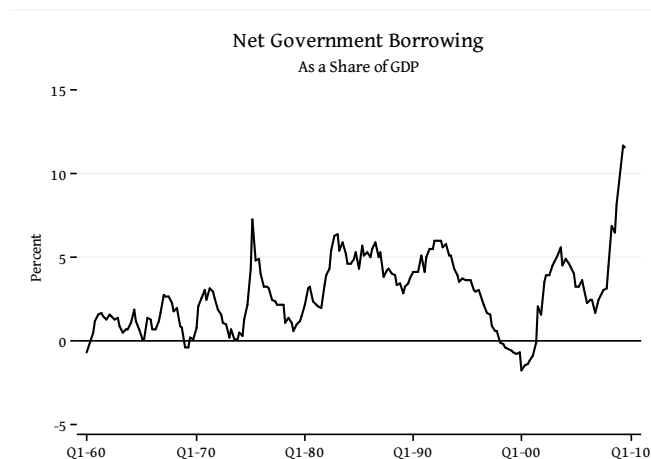
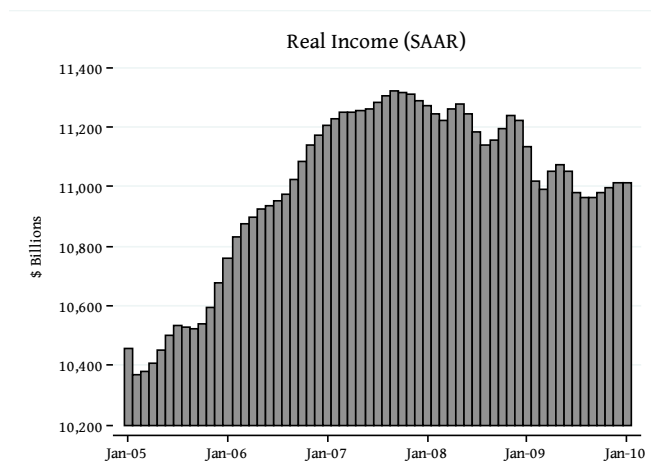
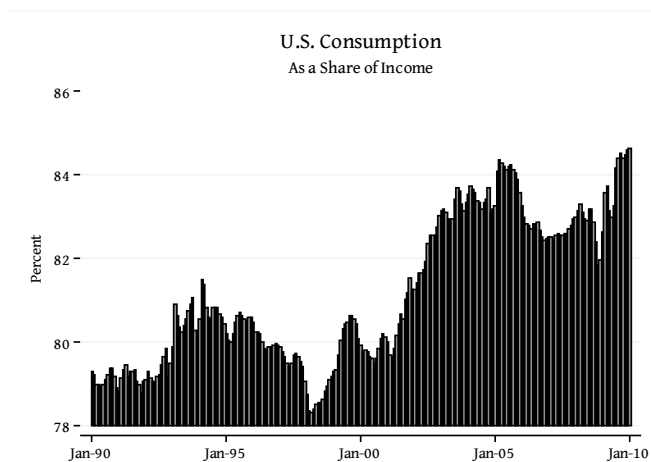
This puts us close to the Greek level of fiscal deficits. Fortunately, the world's lending community doesn't put us in the same category of risk—hence our government still pays relatively low rates on its debt. But how long we can continue on such a path is unclear, particularly if inflation starts to set in at any level. And is such an action ethical? Should the next generation of Americans be held financially responsible for this generation's inability to spend at a reasonable level?

Taxes will necessarily increase in the next two years, although the speed at which they will rise is yet to be determined. The current budget proposal on the part of the Obama administration includes some extensions of middle class tax cuts but allows tax rates to go up on higher-income households. This will clearly put consumers in the difficult position of having to reduce spending or savings. The first is bad for the short-term health of the U.S. economy, the second is bad for long-term health.

The only real hope for the administration is that income growth will return with enough speed to allow Americans to pay higher taxes without cutting back elsewhere. At this point in time, it seems unlikely to occur. The labor markets remain weak, and the last few recessions seem to indicate that the jobless recovery is a standard part of a modern recession. It may be even worse this time around. Because of the shift in economic drivers, away from housing and consumer spending, many laid off workers will need to be retrained in new fields before they become employable. This may be why job creation is such a top policy priority.

Inflation and the Federal Reserve

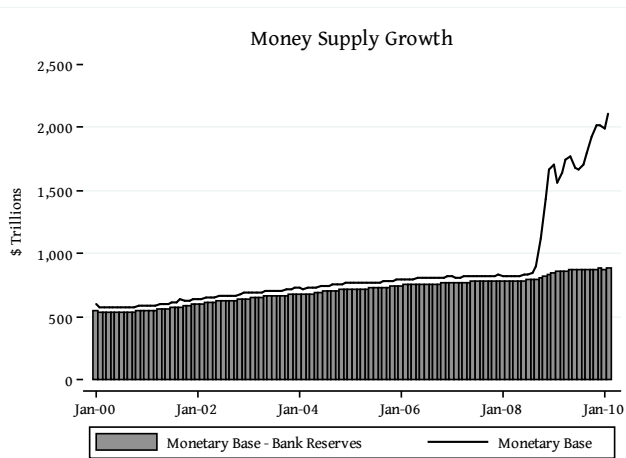
What about inflation? We have already noted that the Federal Reserve has been printing money in order to push down long-term interest rates. To date, they have expanded the monetary base by nearly \$1.3 trillion dollars. Much of this has gone to purchasing Fannie Mae and Freddie Mac debt—but some has also been used to buy longer-term treasuries and some private label asset-backed securities. As noted, this has expanded the base money supply by 150%, which implies that there is the potential for 150% inflation in the next five years. With this level of risk, it seems astonishing that the bond markets have been so willing to continue to lend.



One reason for the continuation in lending is that there is no immediate risk of inflation. Much of the stimulus has landed in the banks in the form of excess reserves. Indeed, taking the growth of excess reserves out of the equation, the monetary base has grown by only 12.5%. And even here we are not seeing inflationary pressures. The increase in savings and lack of confidence has slowed the velocity down substantially. M2—the best measure of broad money that corresponds to serious inflation—has actually decelerated in recent months. When the Fed states that it is willing to hold rates low for the foreseeable future, it has the confidence of knowing that it has 18 months before inflation can become an issue.

Still, the Fed has to begin to slow the expansion eventually—and to date they are planning to by the end of April. One might have expected to already see the impact on the debt markets—but not yet. The problems in Greece and the European Union have likely pushed a flight to security. Plus, with rates on high-risk debt coming down, there isn't much for the liquidity already in the market to do.

The real risk for the Federal Reserve starts not when they stop printing money, but when they need to mop up the liquidity. Much of the liquidity they injected into the economy has been sitting in the banks. Once the banks begin to lend again, excess reserves will start to fall. This hasn't happened yet, but with indications of loosening credit at banks and with firms starting to invest again in capital equipment and inventories, it will only be a matter of time. When excess reserves begin to fall, the Fed will have to start selling off assets to control inflation—or, in an equivalent move, they will have to raise the rate they are paying the banks on those excess reserves. In either case, rates will begin to rise and will pull some of the stimulative effects out of the economy.



Bear in mind that one of the largest failures of the Federal Reserve during the Great Depression was that it allowed the money supply to collapse, adding to the overall painful recession the nation was in as a result of the collapse of that asset bubble. Fed Chairman

With all the risks on the horizon, one might wonder if there are any bright spots. The answer, as always, is yes. In the short-to-medium run the export market may continue to shine.

Bernanke was not going to let that happen. Currently, price levels are nearly flat despite the massive injection of liquidity. We might argue not that the Fed overdid it—but that they did just enough.

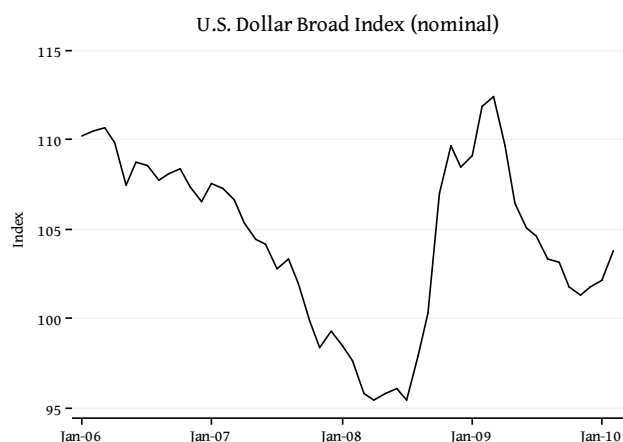
Of course, this assumes that the Fed is actually planning on fighting off inflation. As already discussed, the financial system is not out of the woods yet. The FDIC continues to take over banks at a record pace. But inflation poses a cheaper, simpler solution for the Federal Reserve—inflate the value of the assets above the value of the debt. While this is bad for the debt holders, it can go a long way to reducing the painful deleveraging process the nation is still working its way through. Inflation is now a realistic political option rather than a bad economic decision.

Are There Any Bright Spots?

With all the risks on the horizon, one might wonder if there are any bright spots. The answer, as always, is yes. In the short-to-medium run the export market may continue to shine. With the world economy starting to expand again (particularly the developing world), and with a weaker dollar, firms who sell products to these parts of the world may find themselves doing quite well. Of course troubles in Europe have put some upward pressure on the value of the dollar in the short run, but it still remains at a relatively low level. The one worry is that a deepening sovereign debt crisis could cause a worldwide flight to safety again. This would not be unlike what happened in the second half of 2008 when the export surge that occurred at the

start of the year – and that somewhat offset the decline in domestic demand – was put to a quick end.

Another bright spot in the short term will continue to be business spending. Real net investment dropped to a near all-time low level during the downturn. The catch-up effect should keep growth in the sector decent if not spectacular. Similarly, a state and national policy push for alternative energy should create possibilities there.



In the longer term, the U.S. economy, once it works through its current issues, will be back on a solid growth path. Today's problems do not take away from the fact that the U.S. is still the center of the technological and financial world. While many worry that the U.S. economy is being undermined by trade with Asia (primarily China), in fact there is little direct competition between the two economies. Prior to this downturn industrial production in the U.S. economy was at a record high level. Incomes were rising at a solid pace for Americans—faster than in most of the developed world. These trends will return.

All of this does lead to one longer run worry having to do with the employment markets. An ongoing problem in the United States has been the widening gap between the skilled and the unskilled. This has to do fundamentally with changes that have allowed businesses to use information technology to replace many low skilled positions in the U.S. economy. The boom in housing and retail that was fueled by the massive financial bubble had masked the problem. As the economy returns to normal, these issues will reemerge. And they show how badly the nation needs to embark on a long run program of enhancing the educational opportunities available to the next generation—something at which we are clearly failing.

National Forecast 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)	13,264.47	13,389.67	13,452.28	13,517.19	13,546.28	13,548.72	13,562.15	13,567.99	13,545.80	13,605.01
<i>Growth (%)SAAR</i>	3.52	3.83	1.88	1.94	0.86	0.07	0.40	0.17	-0.65	1.76
Real Personal Consumption (\$ Bill.,SAAR)	9,330.60	9,394.97	9,429.39	9,482.31	9,492.67	9,488.12	9,489.52	9,477.80	9,443.24	9,442.17
Real Investment (\$ Bill.,SAAR)	1,677.84	1,723.65	1,754.64	1,774.07	1,793.53	1,805.46	1,819.80	1,836.67	1,844.55	1,896.79
Real Government Expend. (\$ Bill.,SAAR)	2,602.93	2,620.60	2,624.14	2,619.82	2,611.14	2,595.34	2,582.75	2,571.96	2,563.42	2,560.99
Real Net Exports (\$ Bill.,SAAR)	-346.90	-349.55	-355.88	-359.01	-351.06	-340.20	-329.94	-318.44	-305.41	-294.93
Total Nonfarm Empl. (Mill, SA)	129.64	129.89	130.20	130.60	131.05	131.42	131.75	132.06	132.32	132.62
<i>Growth (%)SAAR</i>	0.05	0.76	0.97	1.24	1.38	1.13	1.00	0.96	0.77	0.90
Unemployment Rate (%SA)	9.80	9.66	9.57	9.47	9.36	9.31	9.28	9.25	9.25	9.21
Personal Income (\$ Trill.)	12.19	12.32	12.42	12.55	12.67	12.80	12.91	13.04	13.16	13.27
<i>Growth (%)SAAR</i>	2.47	4.45	3.23	4.19	3.97	4.21	3.51	3.98	3.70	3.40
Savings Rate (%)	3.25	3.40	3.48	3.28	2.53	2.42	2.63	2.82	3.13	3.15
Tax Rate (%)	9.28	9.31	9.28	9.50	10.54	11.14	11.18	11.50	11.85	12.18

Forecasts by Beacon Economics

National Historical Table

United States	Q3-2007	Q4-2007	Q1-2008	Q2-2008	Q3-2008	Q4-2008	Q1-2009	Q2-2009	Q3-2009	Q4-2009
National Real GDP (\$ Bill.,SAAR)	13,318.90	13,389.50	13,357.10	13,398.00	13,300.70	13,114.50	12,902.60	12,877.90	12,958.40	13,150.40
<i>Growth (%)SAAR</i>	3.60	2.10	-0.70	1.50	-2.70	-5.40	-6.40	-0.70	2.20	5.90
Real Personal Consumption (\$ Bill.,SAAR)	9,335.60	9,363.60	9,349.60	9,351.00	9,267.70	9,195.30	9,209.20	9,189.00	9,252.60	9,291.70
Real Investment (\$ Bill.,SAAR)	2,166.50	2,123.40	2,082.90	2,026.50	1,990.70	1,857.70	1,558.50	1,456.70	1,474.40	1,628.70
Real Government Expend. (\$ Bill.,SAAR)	2,458.90	2,468.70	2,484.70	2,506.90	2,536.60	2,544.00	2,527.20	2,568.60	2,585.50	2,577.90
Real Net Exports (\$ Bill.,SAAR)	-638.40	-564.00	-550.90	-476.00	-479.20	-470.90	-386.50	-330.40	-357.40	-347.10
Total Nonfarm Empl. (Mill, SA)	137.66	137.86	137.90	137.49	136.70	135.02	132.81	131.09	130.08	129.63
<i>Growth (%)SAAR</i>	0.11	0.60	0.10	-1.17	-2.28	-4.83	-6.38	-5.10	-3.05	-1.38
Unemployment Rate (%SA)	4.63	4.80	4.97	5.30	6.03	6.97	8.17	9.27	9.63	10.03
Personal Income (\$ Trill.)	11.95	12.10	12.14	12.29	12.29	12.23	11.95	12.05	12.01	12.11
<i>Growth (%)SAAR</i>	4.20	5.28	1.39	5.06	-0.20	-1.72	-8.87	3.25	-1.44	3.68
Savings Rate (%)	1.42	1.27	1.04	3.05	1.92	3.34	3.37	4.94	3.59	3.76
Tax Rate (%)	12.56	12.58	12.62	10.79	11.70	11.72	9.93	8.99	8.92	8.79

Forecasts by Beacon Economics

California Forecast

by Jordan G. Levine

Beacon Economics

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State Overview

Despite the considerable pain being caused by the current cyclical fluctuation in the economy, California remains poised for long-term success once the imbalances that caused this downturn work their way through the system. In addition to great weather, scenic natural beauty in the form of oceans, mountains, and deserts, and just about all of the man made attractions a human being could possibly want, California is home to some of the finest universities in America, attracting the best students and researchers from across the nation and the world. Nearly 19% of the state's residents have bachelor's degrees compared with 17.5% in the United States overall, and 11% have graduate degrees compared with 10% nationwide. As a result, California remains an attractive place to locate a business—especially among the high-tech industries that now call the state home including information technology, biotech, and renewable energy. Unlike low-skilled manufacturing industries like textiles and apparel, these industries rely more on the quality and skills of their labor force than they do on the cheap price tag and relative abundance of low-skilled workers. If California can maintain this trend going forward, it will be well-positioned to continue attracting industries that will carry us into tomorrow.

This isn't to say that California does not face challenges in maintaining this position. Education, for example, is a critical issue. Because of the sheer magnitude of both K-12 and university education relative to the rest of California's General Fund revenue, it is often a prime target for spending cuts in times of fiscal turmoil. Although we have a greater concentration of highly educated residents compared with the country overall, we also have a larger concentration of residents who lack even a high school diploma. In 2008, it was estimated that nearly 20% of Californians over the age of 25 had less than a 12th grade education. Despite our skilled labor force and ability to attract high-tech businesses, adequately funding education is vital if we

hope to maintain our position as a leader into the future.

California also serves as a hub for goods, services, and people coming into and going out of the United States. In terms of goods trade, roughly 13% of U.S. exports come from California's ports though this number has fallen slightly since the onset of the recession. In other words, California provides a crucial gateway for U.S. businesses to access overseas markets. The majority of what we export is emblematic of our high-tech businesses. In 2009, over 50% of the state's exports were in electrical machinery, industrial equipment and computers, optic, photo, and medical equipment, and aircraft. California is also a large exporter of services to the rest of the world. Predominantly, California provides professional and business services to foreign firms that include management and operational consulting. California also exports our intellectual property such as patents and trademarks, as well as entertainment licensing of movies and music. Tourism is also one of the state's strongest exports. And, as the value of the dollar declines, California is uniquely positioned to exploit the increased competitiveness of U.S. goods and services abroad.

California remains an attractive place to locate a business—especially among the high-tech industries that now call the state home including information technology, biotech, and renewable energy.

Just as critically, California is an important point of entry into the U.S. for foreign immigrants who come to study, work, and live. Nationwide, just over 12% of our residents were born overseas versus nearly 30% in California. This has brought vast diversity of cultures and ideas to the state and has made it a melting pot of peoples from all over the world. Indeed, California has much more racial diversity than the United States overall, with larger shares of black, His-

panic, and Asian residents and smaller shares of non-Hispanic whites.

These characteristics of the state's economy and demography have been a boon to our success, which is borne out in the statistics. At \$61,000, median household income is almost \$10,000 higher in California than it is nationwide where median household income was only \$52,000 in 2008. In addition, nearly 19% of California's households earn at least \$125,000, while only 13% of U.S. households earn as much.

The private equity markets seem to agree that California is still a good place to start and grow a business. Although venture capital investment across the country has taken a severe knock since the economic downturn began, California still receives a disproportionate share of these dollars. It is estimated that over 50% of the venture capital dollars invested nationwide in 2009 came to California.

Since the onset of the recession, California has seen turbulence across virtually all aspects of its economy.

This is not to say that California does not face real and significant challenges. Labor markets remain weak, and we have yet to see a rebound in employment across the state. New business formation, as measured by venture capital money, is down substantially from its 2007 peak, and remains well below the levels seen during the tech boom of the late 1990s. We have real policy challenges ahead as well. California's regulatory structure is unfriendly to businesses, and mandates such as pensions are in real trouble following the CalPERS fiasco. Budget problems abound in Sacramento, and little has been done to change a tax system that leaves the state vulnerable to the boom and bust revenue cycles that have plagued California for years—the state continues to levy relatively high taxes on relatively small tax bases. However, these challenges have yet to slow California down, and can be

fixed if policymakers in Sacramento find the political will to do so.

Since the onset of the recession, California has seen turbulence across virtually all aspects of its economy. The consumer pulled back sharply in 2008 and 2009, and taxable sales in California fell dramatically. This was the result of a huge imbalance in consumer spending behavior, where savings had fallen to near-zero over the past 25 years, and debt levels steadily rose as credit became easier to access. The recession forced consumers to deal with this imbalance, and we have seen savings rates climb back up into the 5% territory. Although it has been painful for businesses and households, consumption levels have now fallen back to a level that is proportionate to incomes, where they are much more sustainable.

The housing market fell victim to some of the same trends, and has since taken a beating as well. Home prices began coming down precipitously in 2007, and there was a subsequent surge in defaults and foreclosures. As option-ARM (adjustable rate mortgages) reset to higher interest rates many people were unable to make their monthly payment and were forced into foreclosure. Others saw their property values decline so much that they entered into a negative equity situation where they owed far more on their mortgage than their home was worth. Many of these underwater homeowners made a decision to walk away from their home rather than make payments on an asset that was worth half of its original purchase price. Now that prices have fallen so dramatically, homes are returning to affordable levels across the state. Ultimately, it is a good thing for California to have home prices that are supported by incomes, and more households and families can consider investing in their first home.

While the residential real estate market appears to be leveling off and returning to fundamentals, the commercial real estate markets continue to be an area of concern. Across California, vacancy rates on commercial property continue to rise. Asking rents have con-

tinued to fall as well, and fewer units are being occupied each quarter than were vacated. California's hotels have also seen sustained reductions in both room occupancy and revenue per available room. Until these trends turn around, the nonresidential construction market will continue to be a drag on California's recovery.

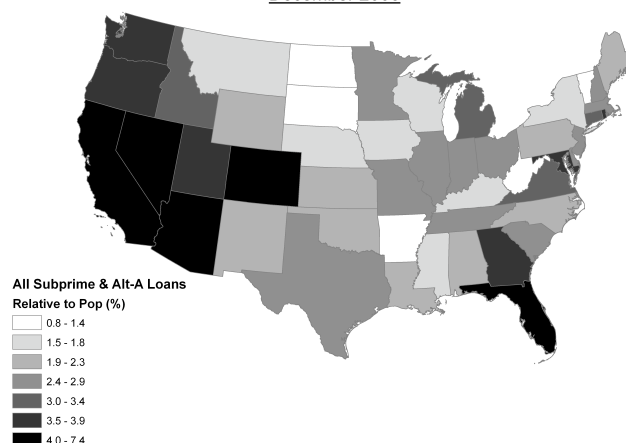
...federal stimulus dollars are beginning to make their way into actual projects, and California should gain from this as well.

Encouragingly, recent evidence suggests that the economy is beginning to slowly turn around. The country saw strong economic growth in the second half of 2009. This was driven by consumer spending, which itself was the beneficiary of massive government intervention through federal incentive programs to buy homes and cars. Although these were temporary programs, which have since expired, they did appear to help the American consumer find some sort of a level footing. The strong growth in real GDP also came from one of the largest inventory burn-offs in recent history. During the recession, many firms shifted into a mode of depleting their shelves rather than making new orders, and industrial production stalled as a result. Now, we have seen inventories bottom-out in recent quarters and both production and new orders have seen a small uptick. This should be a positive indicator for the labor markets, which should benefit as plants across the country begin to switch back on. In addition, federal stimulus dollars are beginning to make their way into actual projects, and California should gain from this as well.

Down, but Not Out

Looking back as we begin a new year, it is hard to deny 2009 was one of the worst years for California's economy in more than two decades. This cyclical fluctuation has hit California hard. Indeed, the state played a major role in the downturn we see nationwide. California was subject to the primary imbalances that drove the country into recession. For example, California took on a disproportionate share of the subprime and Alt-A loans relative to most other states. These loans were often structured as adjustable rate mortgages with an option for a lower payment for an initial period of 5 or 7 years.

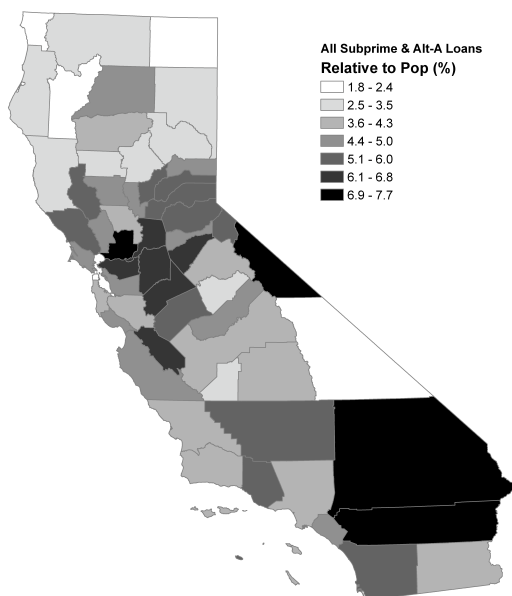
National Subprime & Alt-A Loans Outstanding
December 2005



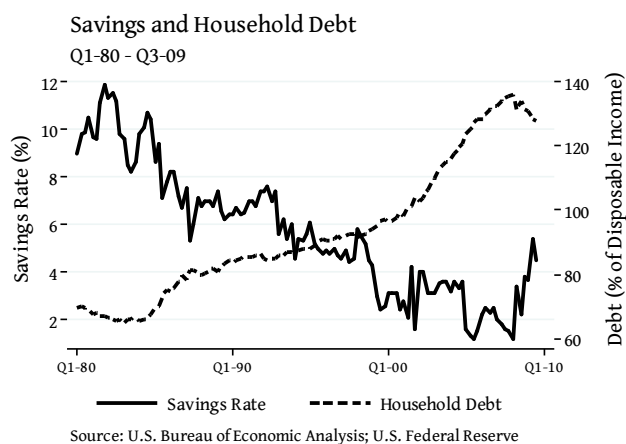
Unfortunately, many buyers did not realize that their loans would reset to higher interest rates (and thus higher payments) long before they reached their 5-year option period. In many cases, buyers lacked the sophistication to fully understand the structure of their mortgages and failed to realize that their introductory payment amount would not cover all of the interest being amortized during those years. Typically, banks have a cap on the amount of negative amortization that can be accumulated before an adjustable rate mortgage recasts, so many people saw their payments rise dramatically well in advance of their introductory period actually ending. Others were speculating on continued price increases, and some were pro-

viding false information in order to secure a loan for a home they couldn't afford.

California Subprime & Alt-A Loans Outstanding
December 2005



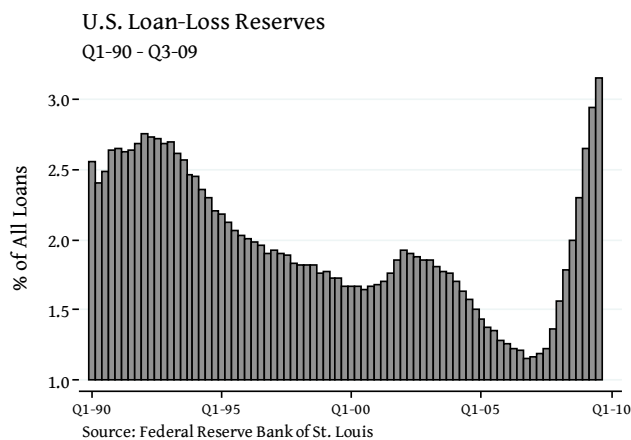
As a result of all of these factors, we were more vulnerable to the inevitable housing collapse that began in late 2006. Specifically, in December 2005, it is estimated California had roughly 19.5% of the outstanding subprime and Alt-A loans in the nation.



This is much higher than the state's share of the U.S. population, which averages roughly 12%. This shows that California had more than its fair share of these risky loans, and is one reason that we are feeling a large degree of the pain.

The unbalanced levels of savings and debt were not only the prime suspect in the widening U.S. trade deficit and national debt, they were clearly unsustainable.

Across California's counties, the subprime and Alt-A loans were highly concentrated in specific areas. Areas exposed to the largest number of risky lending practices relative to their population bases were both the Inland Empire, consisting of Riverside and San Bernardino Counties, and the East Bay region of the San Francisco Bay Area, including Contra Costa and Alameda Counties. Both regions—Inland Empire and East Bay—saw some of the largest run-ups in home prices as the subprime bubble grew. Subsequently, both regions have seen some of the largest declines in prices and the largest increases in defaults and foreclosures.



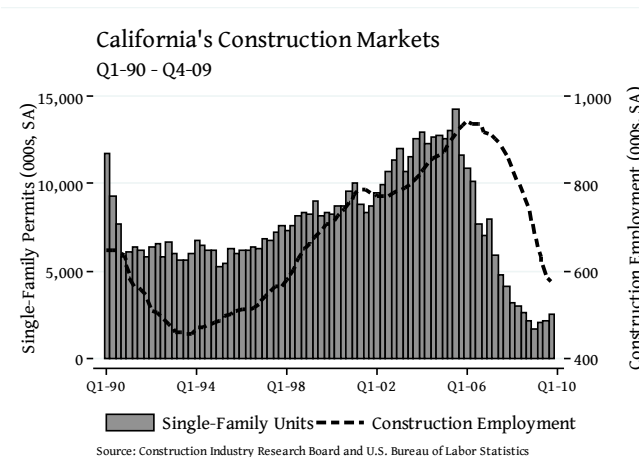
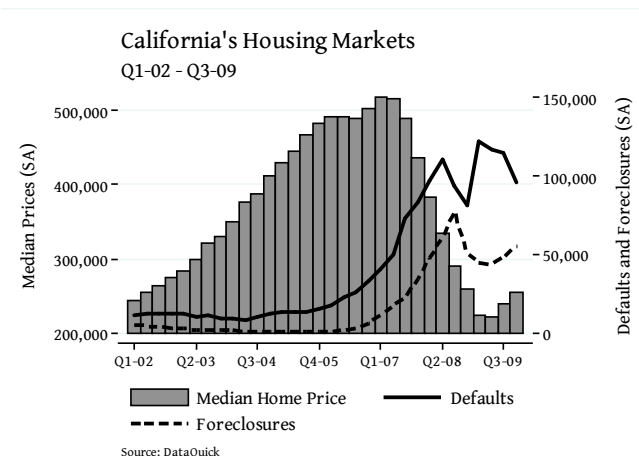
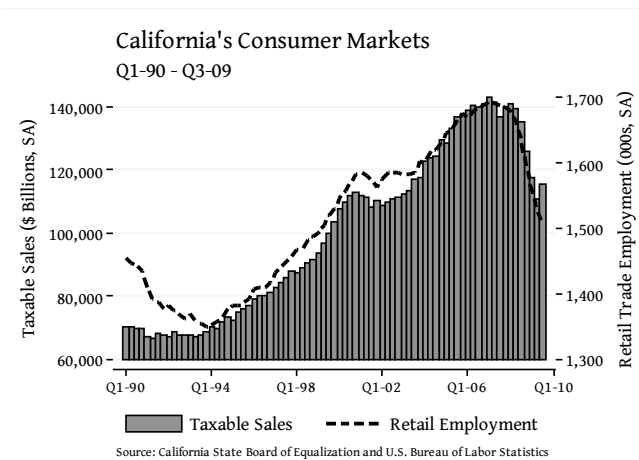
Additionally, the spending imbalances that built up over 20 years made the economy susceptible to a major consumer downturn. Savings rates, which historically have averaged over 7% of disposable income, be-

gan a downward trend in the early 1980s. By the first quarter of 2008, savings fell to just over 1% of income. At the same time, household debt as a percentage of disposable income went through the roof—rising from 69.7% of income in 1980 to 136% by the first quarter of 2008. This trend, coupled with a large share of consumption compared to the overall economy, created the perfect storm for a recession. The unbalanced levels of savings and debt were not only the prime suspect in the widening U.S. trade deficit and national debt, they were clearly unsustainable.

These bad habits eventually caught up with us. As banks started to suffer with under-performing loans and non-performing loans and asset prices appeared to be peaking in 2006, the spigot was essentially shut off. The easy credit driving this bubble evaporated. Indeed, we can see in the national numbers that once the real estate markets sustained losses and labor markets began to shed jobs in late 2007, the banks began reducing credit availability and pumping up their loan loss reserves. These reserves, which tend to go up in times of turmoil, rose from 1.16% of all loans in late 2006 to more than 3.15% of all loans by the third quarter of 2009.

Taking Stock

Since the collapse, California has been feeling pain across all aspects of its economy. The state's labor markets have been especially hard hit. In January 2010, the unemployment rate reached 12.5% on a seasonally adjusted basis and over 1.39 million total non-farm jobs were shed by December 2009 from peak employment in July 2007. When asset prices fell and the labor market started losing jobs, consumers began to dramatically pull back. By the second quarter of 2009, taxable sales were off their peak levels by 22.9% and retail trade continued to trim workers—with over 212 thousand jobs lost from its peak level by December of 2009.

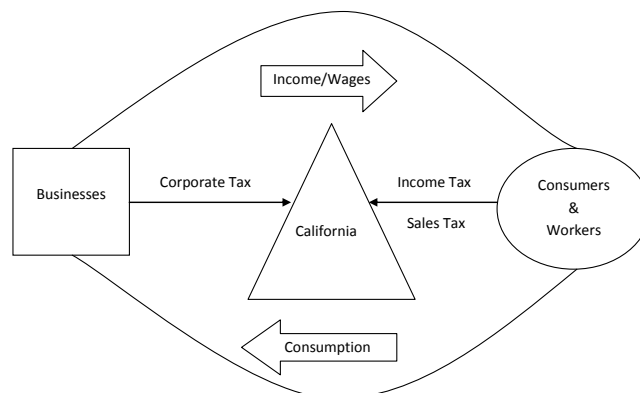


The real estate and housing markets have also taken a beating. After posting record gains between 2003 and 2006 home prices peaked. They began falling sharply in 2007, 2008, and 2009. At the same time defaults and foreclosures surged to decade highs. Residential building permits began to decline in late 2005 and by January 2009, with only 2,500 permits issued, they had fallen by 89% from their peak of more than 20,000 per month. Construction employment followed shortly after permits, and shed more than 379 thousand jobs, or 40% of its workforce by the end of 2009.

Commercial real estate came later to the game. In both the retail and office segments, vacancy rates did not begin to rise by any significant amount until late 2007 and early 2008. The slowdown in commercial real estate lagged the housing market and consumer pull-back and highlights the extent to which businesses follow the consumer. Looking out at the commercial market, there are many ominous signs. In every type of property (office, retail, or industrial), and in every region across the state, the same trends hold true: cap rates are up, rents are down, and net absorption remains negative while vacancy rates keep climbing higher.

The economic turmoil borne by the state has created an enormous amount of stress on our fiscal position as well. Between 90% and 95% of the state's General Fund Revenues are derived from three major sources—the so-called “Big 3”—personal income tax, corporate tax, and sales and use tax. Unfortunately, these revenues are almost entirely determined by California's economic health. For example, higher unemployment leads to lower incomes, which in turn drives lower consumer spending, which then drives corporate profits down. Then, the whole process starts over

again. These linkages create a vicious cycle for California's budget in times of economic downturn.



During the run-up in home prices, the decline in savings, and the increase in consumer spending, California began experiencing large increases in its General Fund Revenue. The state's revenue grew from roughly \$70 billion in the 1999-2000 fiscal year to more than \$95 billion by the 2006-07 fiscal year. This growth—which ranged from 6% to more than 13% per year (with the exception of the 2000-01 fiscal year which was hurt by the 2001 recession)—was very strong and could have been leveraged to get our fiscal house in order or to save for a rainy day. Unfortunately, it was not.

California General Fund Revenues (\$000s)

Source	2006-07	2001-02	1999-00
PIT	52,353,056	33,295,428	39,272,755
CORP	10,767,189	5,088,175	6,575,403
SALES	27,515,361	21,368,831	20,825,007
Big 3	90,635,606	59,752,434	66,673,165
TOTAL	95,665,223	64,341,833	70,771,088

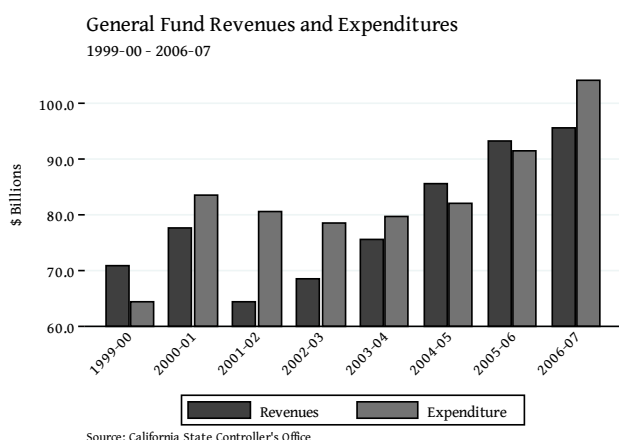
Source: California State Controller's Office

Then, in 2009 it poured with the Big 3 revenues declining dramatically. But rather than putting the increased revenues into a war chest to use to smooth out the state's finances during an economic downturn, expenditures were steadily increased each year. Because of this, the state's went from a \$2.7 billion budget surplus in June of 2006 to a year-to-date deficit of \$12.9 billion as of December 31, 2009.

In January 2010, the unemployment rate reached 12.5% on a seasonally adjusted basis...

The economic turmoil borne by the state has created an enormous amount of stress on our fiscal position as well.

Now California policy makers are forced to make choices about which programs to cut, and which to trim, how to create new, better ways to increase revenues. We have already seen cuts to K-12 education, furloughs of State employees, and increases in sales tax and personal income tax rates as temporary fixes. However, a true recovery in California's fiscal position relies most importantly on a recovery in the State's economy. Additionally, while California does have more than \$20 billion in outstanding debt (both internal and external borrowing), it represents only a small percentage of our gross state product. As consumer spending and employment return to growth, so will the state's three major sources of revenue.



A Bird's-Eye View

Looking at the nation from a bird's eye view, California clearly has been hard hit. With nearly 1.4 million jobs lost since employment peaked in July 2007, California has shed the largest number of jobs of any state. However, in other ways, this recession has affected some states even harder. For example, in terms of employment decline as a percentage of peak em-

ployment, California ranks 6th with a decline of 9.2%. Michigan ranks 1st, having shed 18% of its jobs from its peak, followed by Ohio and the states with subprime and Alt-A woes—Nevada, Florida, and Arizona, with declines of 13.8%, 11.5%, and 11.1%, respectively. Indeed, the number of jobs lost in the combined five states of Michigan, Ohio, Arizona, Nevada, and Florida are roughly twice as large as the number of jobs lost in California.

Similarly, California's labor markets began heading into decline relatively early in this recession, with employment peaking in July 2007. Of the 50 states and the District of Columbia, 16 did not begin to see employment contract until the second quarter of 2008. Yet, 10 states including Michigan, Florida, Nevada, and Ohio began eliminating nonfarm payroll positions before California, and another five including Arizona, saw employment peak by the end of 2007. The Golden State has the 5th highest unemployment rate in the nation with 12.5%, trailing Michigan (14.3%), Nevada (13.0%), Rhode Island (12.7%), and South Carolina (12.6%). In sum, while California is feeling the sting of this downturn more than most, there are a few places in the country that are struggling even more.

The Golden State has the 5th highest unemployment rate in the nation with 12.5%, trailing Michigan (14.3%), Nevada (13.0%), Rhode Island (12.7%), and South Carolina (12.6%).

The same is true for California's housing markets. A disproportionate share of subprime and Alt-A loans went to California before the market peaked, making it susceptible to a housing downturn. Since the bubble has collapsed, we have seen a wave of foreclosures

Comparative Labor Market Statistics

State	Peak Employment	Decline (000s)	Decline (%)	Unemp. Rate
California	Jul-07	-1,393.0	-9.2	12.5
Florida	Mar-07	-926.1	-11.5	11.9
Michigan	Jun-00	-845.9	-18.0	14.3
Ohio	May-00	-652.5	-11.6	10.8
Illinois	Jan-08	-437.1	-7.3	11.3
Texas	Aug-08	-431.3	-4.1	8.2
New York	Apr-08	-367.4	-4.2	8.8
Georgia	Feb-08	-341.3	-8.2	10.4
North Carolina	Feb-08	-305.0	-7.3	11.1
Arizona	Aug-07	-298.0	-11.1	9.2
Pennsylvania	Apr-08	-269.9	-4.6	8.8
New Jersey	Jan-08	-242.9	-5.9	9.9
Indiana	Jun-07	-235.1	-7.9	9.7
Tennessee	Feb-08	-221.2	-7.9	10.7
Washington	Mar-08	-199.7	-6.7	9.3
Wisconsin	Jun-07	-198.0	-6.8	8.7
Nevada	Feb-07	-179.4	-13.8	13.0
Virginia	Feb-08	-177.2	-4.7	6.9
Massachusetts	Mar-08	-166.7	-5.0	9.5
Alabama	Jan-08	-162.2	-8.1	11.1
Minnesota	Jun-07	-159.6	-5.8	7.3
Colorado	May-08	-156.5	-6.6	7.4
Missouri	Feb-08	-153.7	-5.5	9.5
Oregon	Feb-08	-148.6	-8.5	10.7
South Carolina	Sep-07	-145.7	-7.5	12.6
Maryland	Feb-08	-125.3	-4.8	7.5
Kentucky	Jun-07	-117.2	-6.3	10.7
Connecticut	Mar-08	-103.4	-6.0	9.0
Utah	Dec-07	-85.5	-6.8	6.8
Oklahoma	May-08	-79.0	-4.9	6.7
Mississippi	Feb-08	-76.0	-6.6	10.9
Kansas	Apr-08	-74.6	-5.3	6.4
Iowa	May-08	-71.2	-4.7	6.6
Louisiana	Aug-08	-69.4	-3.6	7.4
Idaho	Nov-07	-55.2	-8.4	9.3
Arkansas	Feb-08	-54.6	-4.5	7.6
New Mexico	Apr-08	-46.2	-5.4	8.5
Rhode Island	Jan-07	-44.6	-9.0	12.7
Hawaii	Dec-07	-43.0	-6.8	6.9
Maine	Jan-08	-33.6	-5.4	8.2
Nebraska	Oct-08	-32.9	-3.4	4.6
West Virginia	Oct-08	-32.8	-4.3	9.3
New Hampshire	Jan-08	-31.1	-4.8	7.0
Delaware	Feb-08	-30.9	-7.0	9.0
Montana	Mar-08	-26.4	-5.9	6.8
Wyoming	Oct-08	-21.2	-7.0	7.6
Vermont	Jun-07	-15.8	-5.1	6.7
South Dakota	Aug-08	-12.5	-3.0	4.8
District of Columbia	Aug-08	-9.4	-1.3	12.0
North Dakota	Nov-08	-5.7	-1.5	4.2
Alaska	Dec-08	-1.9	-0.6	8.5

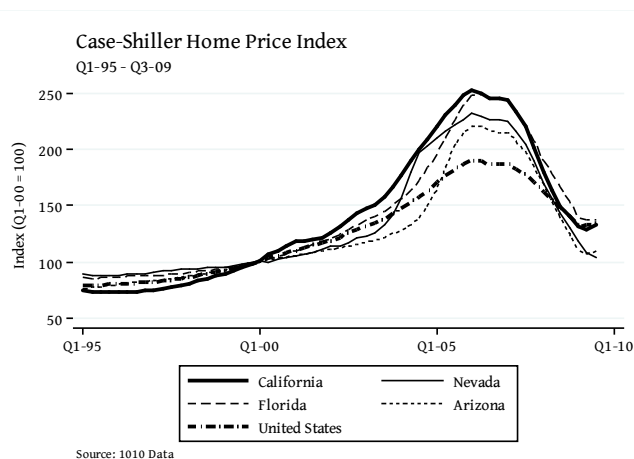
Source: U.S. Bureau of Labor Statistics

Mortgage Delinquencies and Foreclosures (% of All Loans)

State	30 Days Past Due	60 Days Past Due	90 Days Past Due	In Foreclosure
Florida	3.80	2.05	6.31	12.98
Nevada	3.69	2.27	8.16	9.78
Arizona	3.58	2.05	6.19	6.37
California	2.84	1.67	6.12	5.94
New Jersey	3.40	1.58	3.98	5.48
Illinois	3.66	1.76	4.75	5.28
Ohio	4.13	1.79	4.44	4.67
Michigan	4.29	2.10	5.90	4.52
Hawaii	2.33	1.20	3.23	4.31
Maine	3.73	1.64	3.38	4.22
Indiana	4.52	1.85	4.97	4.06
Rhode Island	3.78	1.81	4.47	4.04
New York	3.30	1.45	3.92	3.94
Maryland	3.62	1.73	4.46	3.79
Wisconsin	2.85	1.32	3.15	3.69
Connecticut	3.35	1.56	3.53	3.59
Idaho	3.06	1.46	3.32	3.54
Georgia	5.05	2.30	5.11	3.51
Minnesota	2.60	1.24	3.06	3.47
Massachusetts	3.43	1.47	4.14	3.41
South Carolina	4.19	1.72	3.72	3.31
Delaware	3.75	1.42	3.32	3.19
Utah	3.35	1.55	3.33	3.11
Kentucky	4.17	1.71	3.42	3.11
Louisiana	4.39	1.84	4.12	2.91
Dist. of Columbia	2.91	1.31	3.11	2.91
Mississippi	5.84	2.50	5.47	2.90
New Mexico	3.46	1.39	2.71	2.89
Oregon	2.44	1.16	2.99	2.87
Colorado	2.65	1.20	2.70	2.87
Pennsylvania	3.88	1.63	3.42	2.73
Iowa	2.96	1.20	2.50	2.71
Oklahoma	3.81	1.44	2.80	2.70
New Hampshire	3.54	1.54	3.36	2.38
Vermont	2.58	0.98	1.96	2.37
Washington	2.42	1.19	3.26	2.30
Tennessee	4.63	1.92	4.22	2.30
Virginia	3.07	1.36	3.12	2.27
Kansas	3.27	1.32	2.72	2.24
West Virginia	4.84	1.88	3.33	2.19
North Carolina	4.07	1.70	3.57	2.09
Alabama	4.69	1.88	4.14	2.08
Missouri	3.90	1.68	3.57	2.08
Texas	4.25	1.78	3.44	2.00
Arkansas	4.07	1.49	3.07	1.93
Nebraska	2.85	1.12	2.22	1.91
South Dakota	2.00	0.78	1.55	1.65
Montana	2.35	0.96	1.85	1.60
Wyoming	2.52	1.01	1.77	1.49
Alaska	2.42	0.98	1.54	1.38
North Dakota	1.99	0.69	1.18	1.13

Source: Mortgage Banker's Association

and nonperforming mortgages. By the third quarter of 2009, 5.8% of all mortgages were in foreclosure in California, which is the highest in at least 30 years. Even more troubling are the number of loans that are nonperforming, but have yet to hit the foreclosure process. According to the Mortgage Bankers Association, an additional 10.5% of all mortgages in California are at least 30 days past due. Combine these, and 16.3% of California's mortgages are distressed – and will play a role in moderating the recent growth we have seen in home prices as the economy begins to recover. We also see a large percentage of California's homeowners who remain current on their mortgage, but who face the daunting prospect of being severely underwater. First American Corelogic currently estimates that 35% of all mortgages in California are in negative equity situations, and another 4% are within 5% of being underwater.



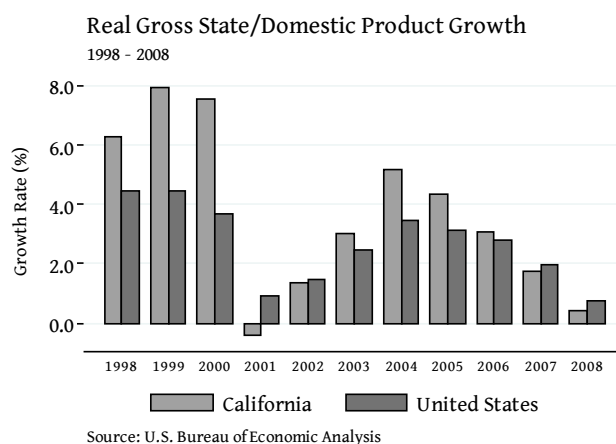
As bad as things are in California, other states were wrapped up in the housing bubble as well. Along with those in California, home prices in Florida, Arizona, and Nevada grew at an unsustainable rate during the first part of the decade. This growth surpassed that of the nation overall, and was completely out of line with income growth—which should be the primary driver of home values. Now, Florida, Nevada, and Arizona all have larger proportions of their existing mortgages in foreclosure relative to California at 13.0%, 9.8%, and 6.4%, respectively.

These states also have large shares of distressed mortgages that have yet to hit the foreclosure process. By the third quarter of last year, Nevada had the largest stock of 30-, 60-, and 90-day delinquencies at 14.1% of all loans. This was followed by Florida with 12.2% of all loans in delinquency. Arizona had slightly less delinquent mortgages with 11.8% of all loans at least 30 days past due. Thus, although California has battled with beleaguered housing markets, it has not been the hardest hit.

California is still a major growth engine in the U.S. economy. For the past 10 years, real economic growth in California has exceeded that in the United States overall.

These Boots Were Made for Walkin'

Despite the problems in California's housing, consumer and labor markets, it is important to keep the state's underlying economy in perspective in any economic outlook. When we zoom out from the cyclical volatility the state is currently facing and focus on long-run trends, it becomes clear that the future is bright for the Golden State.

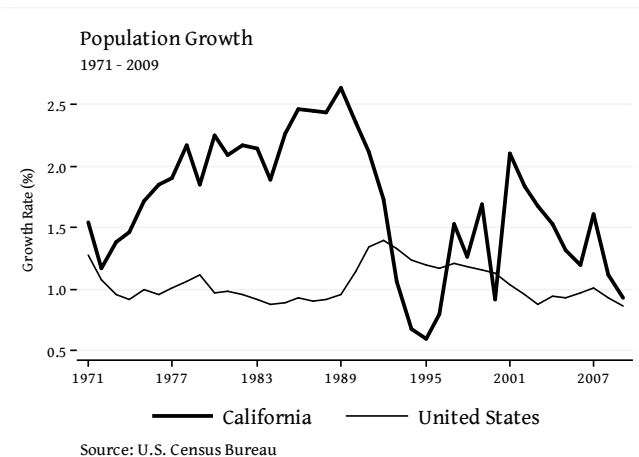
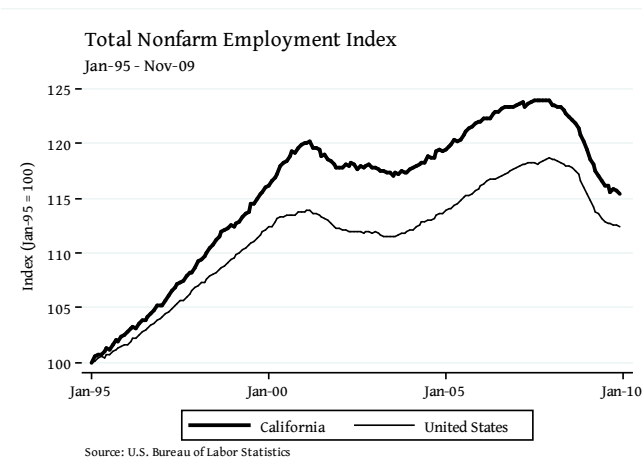
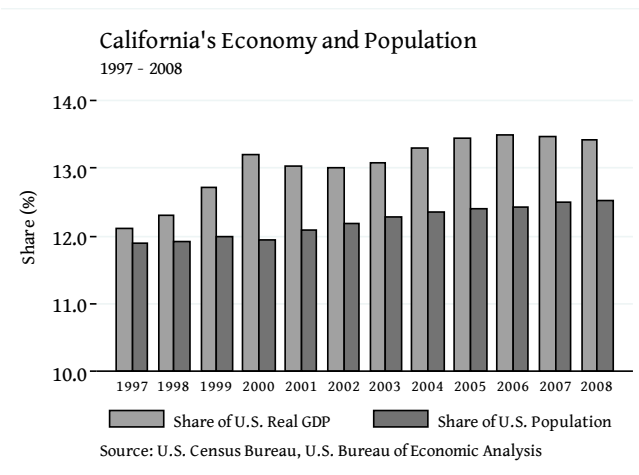


California is still a major growth engine in the U.S. economy. For the past 10 years, real economic growth

in California has exceeded that in the United States overall. During the past 10 years California has averaged an annual growth rate of 3.7% in its real gross state product, while the United States achieved average economic growth of only 2.7%. The exceptions to this trend are the 2001 downturn when growth was slower than that of the nation overall, and the current recession. This is unsurprising given that the pullback in California led the nation in this recession and illustrates the economic impact of California on the country. During growth periods California grows faster than the nation, but pulls back harder in times of recession.

The long-term strength in California's economy is also illustrated by comparing California's share of U.S. economic output relative to its share of the population. Since 1997, California has maintained between 11.9% and 12.5% of the nation's total population. Over the same period, the state had a larger share of the country's economic output, which ranged from 12.1% to 13.5%. This shows that California has had a significant influence on the national economy. Californians are adding more than their fair share to the nation's economy.

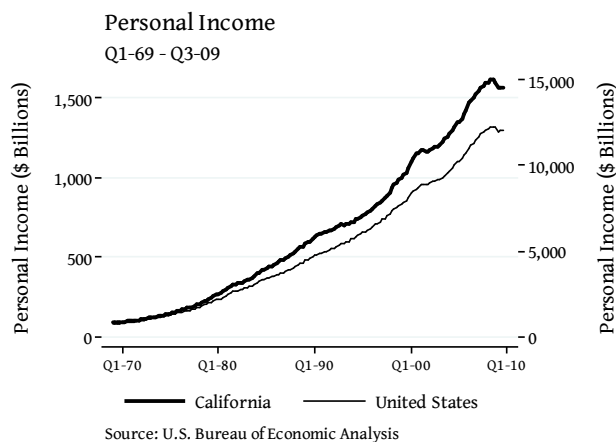
Other economic indicators point to a bright future for the Golden State as the recovery begins. For example, employment growth has outstripped that of the United States in the majority of the last 15 years. To illustrate, between January 1995 and peak employment in 2007, California's total nonfarm payrolls grew by almost 24%. During that same time the United States expanded its employment base by only 18.3%. So again, it is clear the state has been one of the key regions driving employment growth in the nation, in addition to driving its economic growth.



The state's demographic trends are a sunny spot for the future as well. With the exception of the mid-1990s, California's population has been growing faster than the nation overall. Part of this population growth is due to natural increase with more births than deaths occurring each year. However, another part of this population growth is from net migration of new residents from the rest of the U.S. and all over the world.

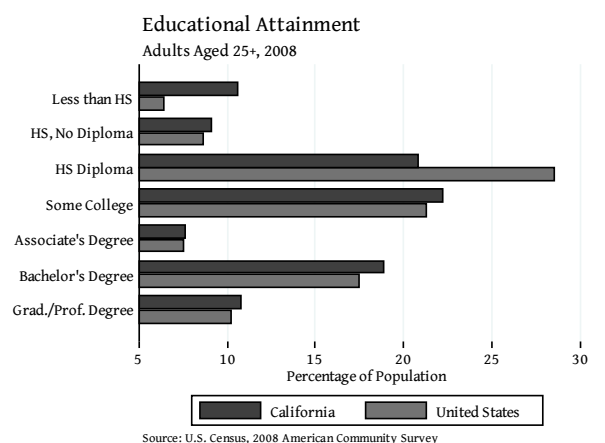
While our outlook for California's income is partly based on an expected increase in population growth, it is also founded on other demographic assets within the State

While population growth also presents challenges for the state, California's income growth, which has consistently outpaced the United States overall, is partly due to this strong population growth over the past 30 years. Although personal income in the state has contracted more sharply than the nation since the onset of this recession, it has also had its labor markets hit harder. As employment begins to increase, we expect a return to healthy income growth in both California and the United States.



While our outlook for California's income is partly based on an expected increase in population growth, it is also founded on other demographic assets within

the state. The primary advantage California has moving forward is its highly educated population. In addition to being home to many top-tier public and private universities—including among others U.C. Berkeley, U.C.L.A., University of Southern California, and Stanford University—California has many highly educated residents.

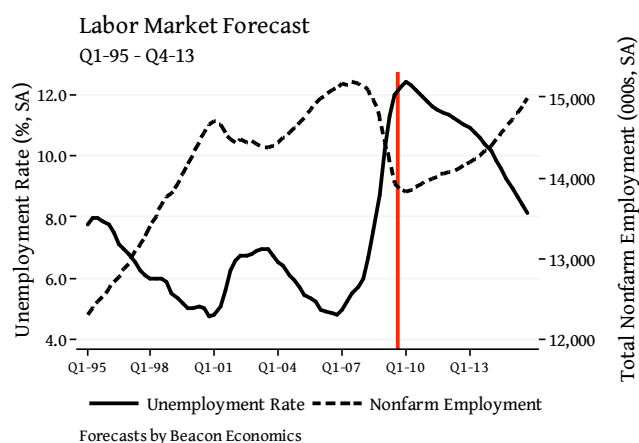


Compared to the United States overall, a larger share of California's residents have associate's degrees, bachelor's degree's, and graduate and professional degrees. This increases the ability for California to attract high-skilled businesses that need skilled workers to fill their jobs. Higher education levels also add to worker productivity, which will ultimately lead to higher wages and incomes for the state's population.

Forecasts

Based upon this analysis of California's economy, we forecast California's labor markets to begin turning around over the next few quarters. The state's unemployment rate was at or near its peak of 12.5% in the first quarter of 2010. Growth in nonfarm payrolls will resume in the first half of 2010, but the growth will be muted as housing and consumer markets struggle to regain a solid footing in 2010 and 2011 due to uncertainty about future growth. There is also uncertainty as to whether several key tax cuts at the state and na-

tional level will be allowed to expire or whether they will be extended or made permanent.

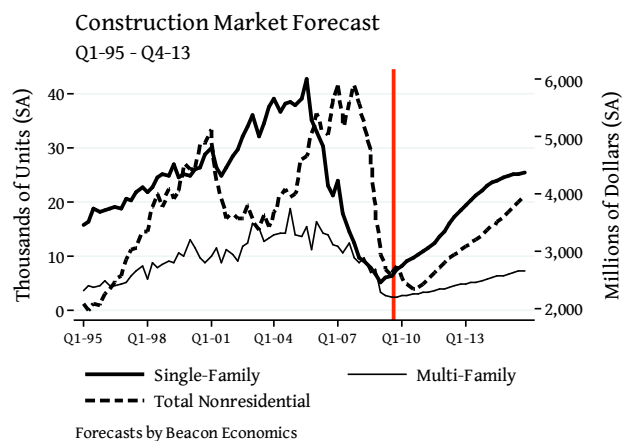


The housing market, which has taken a beating over the past three years, is also feeling for a bottom. While home prices in California have risen in recent quarters, there still exist a large number of nonperforming loans and mortgages in foreclosure that will make the rebound in home prices less steep than many expect. Also, as the tax credits for first-time home buyers expire, home prices rise, and the pool of eligible first-time buyers is absorbed, we expect to see home sales come down slightly in 2010, though they will remain above 80,000 per quarter over the next two years.



However, the pent-up demand for homes and the growing population—along with a real estate market nearing its bottom—should benefit the construction

market. We have seen an uptick in residential building permits issued over the past six months in California, and we expect to see this trend continue over the next few years, though activity will not reach the peak levels seen in 2005 and 2006 for many years to come. Nonresidential construction, which has fallen to levels not seen since the mid-1990s, still has problems to work out. Nonresidential building permits will not return to growth until later in 2010 and will stay well below 2007 levels of permitting through 2015.



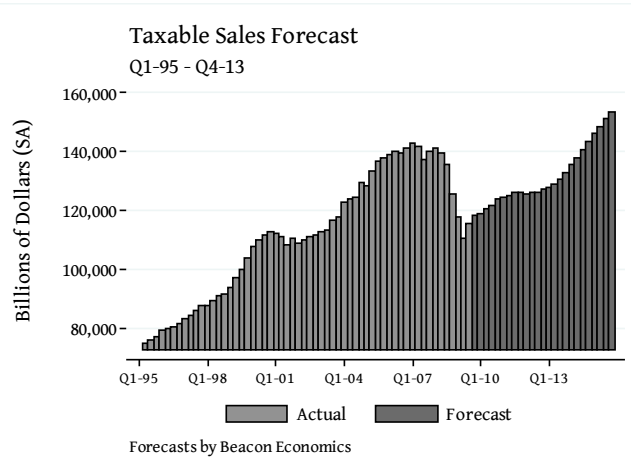
Unfortunately, the picture for commercial real estate is grimmer. In all of California's 8 major regions, cap rates are increasing—traditionally a positive sign. But, when we dig deeper into these numbers a different story emerges: cap rates are rising despite falling prices because rents are falling faster than prices. These trends do not point to a return to growth in nonresidential construction any time soon. In addition, as long as net absorption remains negative and vacancy rates rise, the commercial real estate market will be a drag on California's recovery.

...pent-up demand for homes and the growing population—along with a real estate market nearing its bottom—should benefit the construction market.

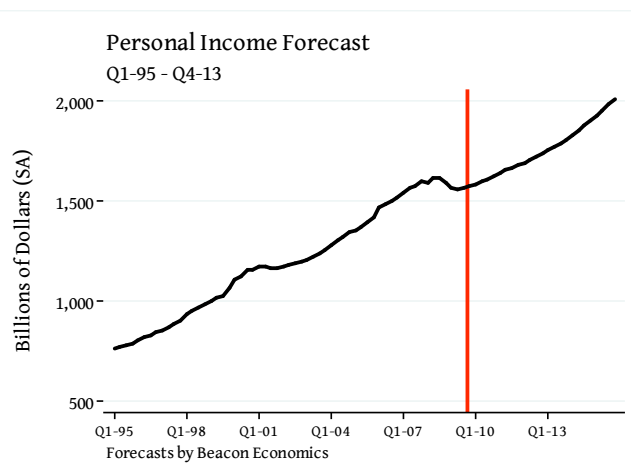
Taxable sales, which saw a strong bump in the third quarter of 2009 due to the Cash for Clunkers program and the first-time homebuyer tax credit, are expected to remain weak through 2010. They will likely rise above 2009 levels by roughly 1.3%. Part of this is due to slow projected growth in employment and part is due to the uncertainty over the expiration of the tax cuts and incentives discussed earlier. Consumer spending will also be affected by the increase in savings rates, as people shift toward replenishing their savings or become first time savers.

As the labor markets have been slowing their decline, we have seen personal income level off as well. We currently predict that 2010 will see a return to growth in personal income in the Golden State. As the labor markets continue to heal, we expect to see income trend upwards at a slower, but more healthy and sustainable pace of growth than we have seen over this past decade we expect to see income trend back upward at a slower, but more healthy and sustainable pace of growth than we have seen over this past decade.

Despite today's turmoil and the hard times we face in the immediate future, California's long term outlook is bright. While we need to address political challenges in order to overcome our troubled regulatory structure and fiscal situation, the state's fundamentals are sound. Among other things, we have a highly skilled labor force, continue to attract high-tech businesses and new investment, and our ports and airports remain a vital gateway for goods, services, and people into and out of the United States. We may be down, but the Golden State is surely not out.



we expect to see income trend back upward at a slower, but more healthy and sustainable pace of growth than we have seen over this past decade



State Historical Table

California	Q3-2007	Q4-2007	Q1-2008	Q2-2008	Q3-2008	Q4-2008	Q1-2009	Q2-2009	Q3-2009	Q4-2009
Total Nonfarm Empl. (Mill. SA)	15.19	15.18	15.14	15.09	14.96	14.75	14.45	14.18	13.93	13.85
Growth (%SAAR)	0.81	-0.31	-0.91	-1.45	-3.32	-5.45	-8.07	-7.26	-6.71	-2.40
Unemployment Rate (%SA)	5.47	5.70	6.00	6.67	7.53	8.70	10.17	11.30	11.97	12.27
Personal Income (\$ Bill)	1,577.54	1,600.47	1,591.69	1,613.95	1,615.23	1,595.58	1,566.08	1,562.65	1,566.09	1,576.42
Growth (%SAAR)	3.36	5.94	-2.18	5.71	0.32	-4.78	-7.19	-0.87	0.88	2.66
Taxable Sales (\$ Bill, SA)	136.99	139.96	140.85	139.28	135.33	125.70	117.63	110.61	115.45	118.17
Growth (%SAAR)	-11.91	8.96	2.55	-4.38	-10.86	-25.57	-23.33	-21.82	18.70	9.78
Single-Family Home Prices (\$ 000s, SA)	488.49	435.74	383.58	334.00	289.44	259.00	224.81	221.81	238.50	255.99
Growth (%SAAR)	-19.81	-36.69	-39.95	-42.51	-43.60	-35.89	-43.24	-5.22	33.67	32.72
Single-Family Home Sales (000s, SA)	54.03	48.18	54.13	66.98	81.86	90.86	92.25	87.90	88.31	93.45
Growth (%SAAR)	-55.89	-36.77	59.29	134.45	123.15	51.79	6.25	-17.57	1.89	25.39
Single-Family Permits (000s, SA)	14.44	12.43	9.54	9.00	7.72	6.56	5.12	6.14	6.46	7.59
Growth (%SAAR)	-56.35	-45.18	-65.33	-20.67	-46.01	-47.72	-62.93	107.45	22.35	90.67
Multi-Family Permits (000s, SA)	12.51	9.68	8.62	9.73	7.09	7.59	3.36	2.61	2.53	2.43
Growth (%SAAR)	88.75	-64.19	-37.05	61.84	-71.83	31.39	-96.16	-63.26	-12.81	-14.90
Nonresidential Permits (\$ Bill, SA)	5.59	5.91	5.56	5.17	4.78	3.67	2.93	2.67	2.57	2.73
Growth (%SAAR)	35.77	24.52	-21.29	-25.16	-27.40	-64.97	-59.65	-31.43	-13.30	26.69
Population (Mill)	37.79	37.91	38.02	38.13	38.24	38.33	38.42	38.49	38.55	38.60
Growth (%SAAR)	1.24	1.24	1.23	1.18	1.10	1.00	0.88	0.72	0.62	0.53
Net Migration (000s)	32.22	33.51	32.51	29.20	23.58	15.67	5.45	-7.07	-15.23	-22.65
Natural Increase (000s)	83.67	83.54	83.09	82.35	81.29	79.93	78.26	76.29	74.87	73.76

Forecasts by Beacon Economics

State Forecast 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)	13.84	13.85	13.89	13.92	13.96	14.00	14.03	14.05	14.07	14.09
Growth (%SAAR)	-0.28	0.48	0.89	1.10	1.17	0.95	0.81	0.72	0.55	0.62
Unemployment Rate (%SA)	12.40	12.28	12.12	11.93	11.74	11.60	11.48	11.39	11.33	11.25
Personal Income (\$ Bill)	1,583.41	1,598.66	1,610.04	1,625.21	1,639.93	1,655.20	1,667.82	1,682.32	1,695.69	1,708.13
Growth (%SAAR)	1.79	3.91	2.88	3.82	3.67	3.78	3.08	3.52	3.22	2.97
Taxable Sales (\$ Bill, SA)	118.82	120.36	121.68	123.59	124.60	125.10	125.78	125.94	125.50	125.87
Growth (%SAAR)	2.21	5.28	4.45	6.44	3.31	1.61	2.21	0.50	-1.41	1.20
Single-Family Home Prices (\$ 000s, SA)	261.53	261.94	260.50	259.08	258.05	257.47	257.55	258.36	259.79	261.73
Growth (%SAAR)	8.93	0.63	-2.17	-2.16	-1.58	-0.90	0.13	1.25	2.24	3.02
Single-Family Home Sales (000s, SA)	97.58	97.34	95.33	92.52	89.67	87.69	87.01	87.66	89.48	92.12
Growth (%SAAR)	18.86	-0.97	-8.02	-11.26	-11.77	-8.53	-3.10	3.03	8.57	12.32
Single-Family Permits (000s, SA)	8.20	8.94	9.66	10.24	10.83	11.59	12.50	13.48	14.57	15.88
Growth (%SAAR)	35.87	41.57	35.94	26.24	25.31	31.33	35.17	35.43	36.14	41.35
Multi-Family Permits (000s, SA)	2.58	2.65	2.86	3.02	3.19	3.39	3.61	3.81	4.01	4.24
Growth (%SAAR)	26.97	12.30	36.36	23.82	24.46	27.04	28.67	24.33	22.05	25.33
Nonresidential Permits (\$ Bill, SA)	2.54	2.41	2.33	2.35	2.43	2.52	2.61	2.70	2.79	2.87
Growth (%SAAR)	-24.76	-19.29	-12.35	3.95	13.65	15.42	15.77	14.64	13.47	11.49
Population (Mill)	38.64	38.68	38.72	38.75	38.78	38.81	38.84	38.87	38.90	38.93
Growth (%SAAR)	0.46	0.41	0.36	0.33	0.31	0.30	0.30	0.31	0.32	0.34
Net Migration (000s)	-28.36	-33.32	-37.26	-40.27	-42.30	-43.43	-43.77	-43.41	-42.53	-41.19
Natural Increase (000s)	72.97	72.45	72.16	72.08	72.17	72.42	72.79	73.27	73.84	74.48

Forecasts by Beacon Economics

Santa Barbara Forecast

by Brad Kemp

Beacon Economics

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Key Chapter Findings

- Santa Barbara is the largest economic engine in California's Central Coast, producing nearly \$16.5 Billion in economic activity in 2008. It was the second fastest growing in terms of economic output between 2002 and 2008, expanding by 20.4%. Only San Luis Obispo grew faster on the Central Coast, increasing by 29.6%. Ventura County was both larger in terms of output value (\$29.3 billion) and growth (21.1%).
- Santa Barbara felt the effects of the recent recession much later than its neighbors and the State overall. The rise in home prices, a bubble which ultimately burst and lead to the onset of the recession, and recession created job losses happened later here than in most areas of California.
- The largest job losses in Santa Barbara County were found in the usual suspects, not surprising given the housing and consumer imbalances were the primary recessionary drivers. Construction, financial activities, and retail trade posted the greatest employment declines in the County.
- Despite going into the recession later than most, the County will rise out of the downturn at the same time as its surrounding counties. This means that the residents of Santa Barbara will perceive the duration of the recession as shorter than many others throughout the state.
- The different regions of the County, North County and the Central Coast, will surely continue on their individual paths following the recession. The North will continue its policy of growth, while the South Coast continues to attempt to resist growth. Both areas will face unique challenges, but both will ultimately share the County's bright future.

Economic Reality

Santa Barbara is known for providing an escape from the realities of the world outside its borders. A luxury get-a-way destination, it benefits from beautiful weather, breathtaking scenery, a growing wine industry and proximity to one of the most populous places in the world—Los Angeles. Santa Barbara also benefits from an international reputation—drawing travelers from around the world to enjoy its many offerings.

But Santa Barbara is more than just a tourist destination. The county also enjoys a strong employment base, with more than 160,000 employees. Many residents—23%—work in government, with the majority of these employed by the county's multiple cities, public schools and military bases. The high percentage of government employment has even grown lately because the union heavy government work centers have

been resistant to job losses during the recent recession, during the same time when other industries have rapidly shed jobs.

Santa Barbara is known for providing an escape from the realities of the world outside its borders...But Santa Barbara is more than just a tourist destination. The county also enjoys a strong employment base, with more than 160,000 employees.

Not surprisingly, tourism related employment ranks second in the county. Leisure and hospitality—comprised of hotels, eating and drinking establishments, and entertainment—employ 13.5% of all workers. Like government employment, leisure and hospitality has seen an increase in positions as a percentage of total employment, after having

Santa Barbara is clearly partitioned by the Santa Ynez mountains, dividing the county into two areas—North County and the South Coast. But the division is more than a pile of sedimentary rocks. It also marks a division of ideals, politics and policy.

represented only 11.1% of total employment in 1990. Unfortunately, this is the industry with the lowest wages of any in the region, with an average wage of only \$19,760 per year, a low figure compared to the average wage of \$63,750 in information, the highest paid super sector in the county.

Santa Barbara County boasts the largest total economic output of California's central coast counties, producing nearly \$16.5 billion in 2008. Monterey County was a close second, with \$15.2 billion, while San Luis Obispo and Santa Cruz counties reported \$8.5 billion and \$8.3 billion, respectively. That said, San Luis Obispo has been the fastest growing county in terms of output, expanding by 29.6% since 2002, while Santa Barbara grew by 20.4% and Monterey grew by only 17.1%. Santa Cruz actually contracted by 1.3% during that period. On the other hand, Ventura County, part of the Tri-County region, is larger in terms of economic output than Santa Barbara, producing nearly \$29.3 billion in 2008, and Ventura grew faster between 2002 and 2008, increasing by 21.1%.

A County Divided

Santa Barbara is clearly partitioned by the Santa Ynez mountains, dividing the county into two areas—North County (including the Santa Ynez Valley) and the South Coast. But the division is more than a pile of sedimentary rocks. It also marks a division of ideals, politics and policy.

The economy in the North County (including the areas around Santa Maria, Lompoc, Guadalupe, the Cuyama Valley, and the Santa Ynez Valley) has been driven by agriculture, oil extraction, and military bases, although there is also a tourism component in the region. It is a blue collar region made up of a diverse, hard working population.

The northern region focuses on encouraging economic vitality by taking advantage of its population growth and expanding its employment base. The region's political stance is conservative. Political leaders in the region seek to maximize the area's considerable potential.

The northern region focuses on encouraging economic vitality by taking advantage of its population growth and expanding its employment base...South County residents favor slow growth...clearly focused on environmental issues.

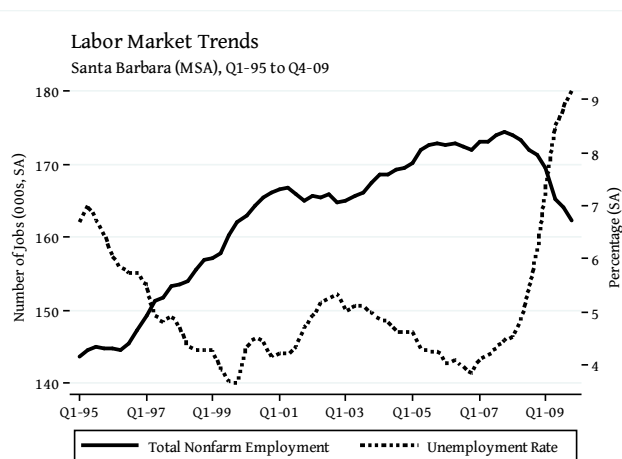
The South Coast focuses on tourism and high-tech industries. Its industries and population are supported by the University of California, Santa Barbara. The university's presence explains the area's high educational levels and its above average representation of professional and business services employment. South County is home to a large number of retirees and wealthy individuals.

South County residents favor slow growth. The quality of life in the area is very high and many residents believe this quality will be compromised if the region grows considerably. Thus the area limits the number of new building permits to be approved. The region's residents are politically liberal and clearly focused on environmental issues.

Santa Barbara County was resistant to the recent recessionary forces while other areas were feeling the full effects of the downturn. Employment losses in the county started much later than in neighboring communities.

Employment Overview

Santa Barbara County was resistant to the recent recessionary forces while other areas were feeling the full effects of the downturn. Employment losses in the county started much later than in neighboring communities. Whereas Santa Barbara County started to shed jobs in the beginning of 2008, a full year after the onset of the recession, San Luis Obispo County had been losing jobs since the third quarter of 2007, and Ventura County's employment contraction began even earlier, in late 2006.



From the employment peak of nearly 174,400 positions in the fourth quarter of 2007, the county's employment base has shrunk by over 12,000 jobs, or 7% to date. Compare that to Ventura County, which has lost 8.6% (25,500 jobs), and California, which lost 8.9% (over 1,350,000 jobs).

Santa Barbara County has historically posted lower than average unemployment rates. Between mid-1996 and mid-2008, the unemployment rate ran from a minimum of 3.6% to a high of 5.8%, averaging 4.6%. During the same period, California's average unem-

ployment rate (5.9%) was higher than Santa Barbara's peak of 5.8%. The rate in California ranged from a 4.7% to 7.6%.

Unlike industry employment losses, which started relatively late compared to the onset of the recession, the rise in the unemployment rate in Santa Barbara happened at the same time as it did for its Tri-County partners and in the state overall. Starting in late 2006, the rate began to creep up. Given that job losses didn't start in the county until much later, the rate rise can be attributed to residents working in surrounding counties and losing their positions there, thus driving up the rate in Santa Barbara.²

Ultimately, the rate expanded to peak at over 9% in late 2009, a rise of over 5.4 percentage points from its base, and much higher than its peak of 7.9% in the 1990s. While this sounds bad, Ventura County's rate increased by nearly 7 percentage points, trough to peak, while the rate in California rose by 7.6 percentage points. The number of unemployed Santa Barbara County residents grew by over 12,200.

The forces that shaped the recent downturn at the national and state level are the same forces that brought change to Santa Barbara County. The two primary cul-

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²Labor force statistics are a measurement of the employment status of residents by area, whereas employment by industry statistics are a measure of the number of workers by area.

prits are the bursting of the housing bubble and the consumer contraction that followed.

What Did Housing Have to Do with It?

In the first half of the 2000s, home prices throughout the nation were rising exponentially—especially here in California—driven by the seemingly insatiable appetite for homes. Consumers were heavily debt loaded and looking for a quick fix to their cash problems. Many people had the feeling that, after successfully recovering from the dotcom bust, they were on their way to early retirement once they sold their home at the peak of the market. Many new buyers jumped in hoping to cash in on the unprecedented equity gains homeowners were experiencing, even if they had to financially stretch themselves a bit. And why not, given the incredibly lax qualification standards most financiers were displaying?

Problems arose because most people assumed that prices were going to continue to climb for a long time to come. Many new buyers were counting on equity gains to help them to be able to actually afford the home they bought. Both new buyers and existing homeowners were in for a big surprise.

In 2000, median prices in Santa Barbara County were lower than they were in Ventura or San Luis Obispo counties. The area had been more expensive in the mid-1990s, but prices fell in the latter half of the decade, while the other two regions saw price gains. This is likely representative of the shift to more residential growth in the north of the county, where prices were considerably lower than in the south.

Then, starting in 2001, prices in Santa Barbara began to grow at a faster rate than in the other two counties. The fact that Santa Barbara had permitted significantly fewer single-family homes in the 1990s resulted in significantly fewer available homes on the market. Because of this, when the housing hysteria started

there was serious competition for a limited number of available prospects. In the northern region of the county, there were considerably more new homes being built than in the south, but the population growth there outpaced the increase in home formation. Taken together, the two causes led to the accelerated price gains.

By 2007, the median price in Santa Barbara County had surpassed that of its neighbors, peaking at nearly \$650,000 in the second quarter, a rise of 231% from the trough.

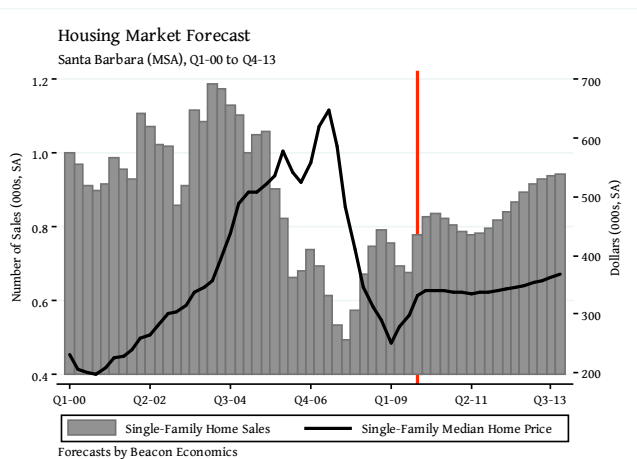
within two years median prices in Santa Barbara County had fallen by nearly \$400,000, again making the homes in the county more affordable than in its Tri-County partners, especially in the northern region of the county.

Both Ventura and San Luis Obispo counties had peaked a year earlier and were already on the decline.

Then the bottom fell out of the housing market in Santa Barbara County. Prices fell off a cliff, and within two years median prices in Santa Barbara County had fallen by nearly \$400,000, again making the homes in the county more affordable than in its Tri-County partners, especially in the northern region of the county. In the first quarter of 2009, Santa Barbara's median price was nearly \$250,500, while San Luis Obispo and Ventura's were \$370,900 and \$362,500.

Therefore it's unsurprising that of the Tri-Counties, Santa Barbara has the largest share of current mortgages underwater, meaning that more properties in the county are worth less than what is owed on them. Nearly 28% of the county's mortgages are underwater, compared to 25.8% in Ventura County and only 16.6% in San Luis Obispo County.

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Starting in 2008, sales started to pick up in the region, but they have only returned to mid-1990s levels. Prices, too, have been on the rise, having gained 32.8% of their value from the trough. Despite these recent price gains, Beacon Economics forecasts that there will be negative price pressure in 2010 due to an increasing number of foreclosures that are sure to happen. This shouldn't be a surprise, given the high number of distressed (underwater) homes in the market. Banks have been working to help those homeowners they can, but the number who are being successfully assisted is just a drop in the bucket. The county's prices will remain flat through the middle of 2011, and then return to modest growth at best.

How the difference plays out in the North County and South County markets remains to be seen. The South County will continue to be a slow growth area, severely limiting the number of permits it allows. That would imply that there would be positive price pressure there, given that buyers are competing for a limited number of homes. But, we must consider the demand for homes as well. Prices in the southern region are considerably higher than in the northern part of

the county, making the homes in the north more attractive to money conscious buyers. Add to this the limited availability of financing on jumbo loans, and the demand for South County homes may be limited.

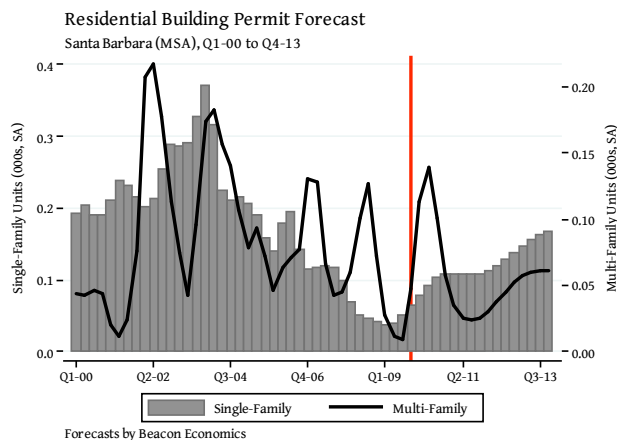
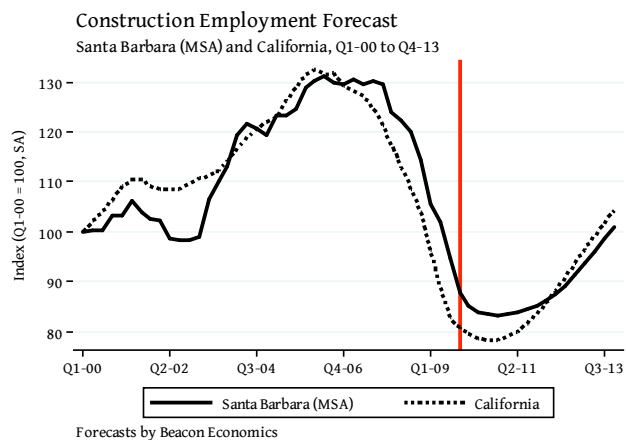
Prices in the southern region are considerably higher than in the northern part of the county, making the homes in the north more attractive to money conscious buyers.

Conversely, North County has seen more robust population growth than the southern region. This means demand for homes has been very high. Unlike the South County, the North County has been trying to keep up with the demand by permitting liberally. During the rise of the housing bubble, they were unable to keep up with the rising demand causing prices to dramatically rise. No doubt, the north will continue to be the faster growth region. Prices there will be dependent on how many new homes are built to meet that demand.

Housing Related Employment

Most of the county's employment losses were in the construction sector, which shrank by more 3,500 jobs. This is not surprising given the buildup of construction jobs during the inflation of the housing bubble seen throughout California. Starting in mid-2006, this industry lost jobs at an accelerating pace. In the first year of losses, 2006-2007, the industry dropped an average of 23 jobs per month. This bumped up to 43 per month the next year, 2007-2008. The worst period for

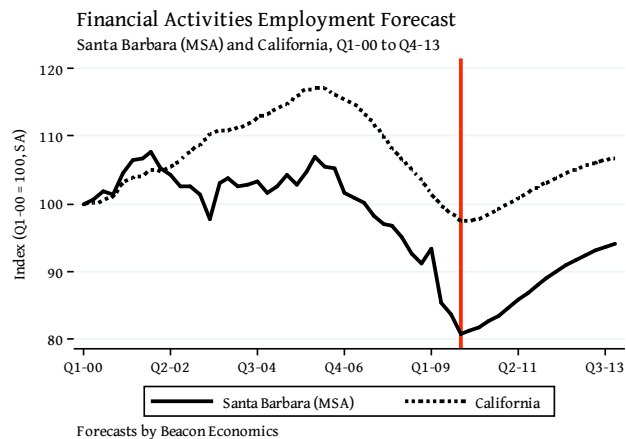
this industry was between 2008 and 2009, when construction jobs were being shed at a rate of 156 jobs per month. The pace has slowed since the middle of 2009 and in the most recent months the losses have been in the teens.



Building permit activity has been on the rise recently—mostly in North County—in both the residential and nonresidential markets. However, the activity remains very low compared to normal pre-recession levels and well below the number being generated during the rise of the housing bubble. Most of the new building growth will be in the North County, while there will be alterations permitting across the county.

Building permit activity has been on the rise recently...However, the activity remains very low compared to normal pre-recession levels...The return to growth for the building industry will be very slow—too slow for the likes of laid off construction workers.

The return to growth for the building industry will be very slow—too slow for the likes of laid off construction workers. For the construction industry, 2010 will be a relatively flat year, with the sector losing only a few hundred more positions by late fall. Then, in 2011, modest growth will return to this industry. It won't be until 2012 that we see this industry add jobs at a more historically normal pace. Even with that, the number of construction jobs won't come close to the sector's 2006 employment peak within the life of our forecast, indicating a very competitive job market for those workers.



Consistent with the huge impact of the bursting of the housing bubble, financial activities posted the second largest job contraction in the county, losing 2,200 positions. Slow job losses started in early 2002, but picked up pace in 2006. To date, this industry has contracted by over 25% from peak.

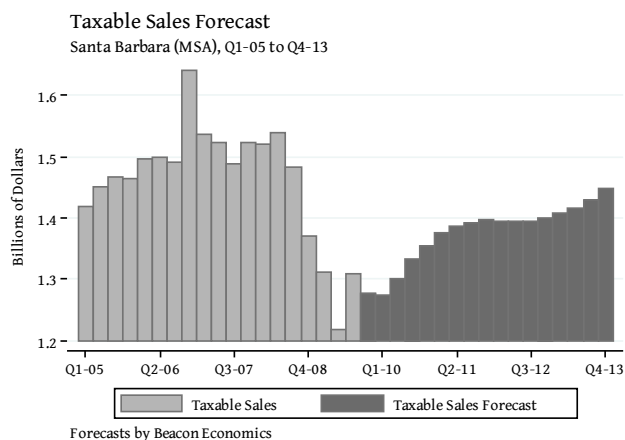
Jobs losses from the financial services sector have slowed recently and will return to growth soon. Most

Despite the recent taxable sales gains, 2010 will remain very flat for Santa Barbara County...Beacon Economics is still concerned that when these tax cuts end there will be another consumer slowdown.

of the growth over the next year will be in the banking and insurance sector, but later in the year the real estate, rental, and leasing sector will gain some momentum.

The Consumer Contraction

When the housing bubble burst and the reality of the loss of the perceived equity gains set in—alongside the bracing news of rising unemployment rates—the consumer was shocked into a state of paralysis. Taxable sales in Santa Barbara County fell off a cliff in the fall of 2006—consistent with the residential employment drop. Total taxable sales fell by 25.8% from the fall of 2006 to the second quarter of 2009 when they hit bottom. Taxable sales figures have returned to growth since then, regaining 5% from the recent low mark.



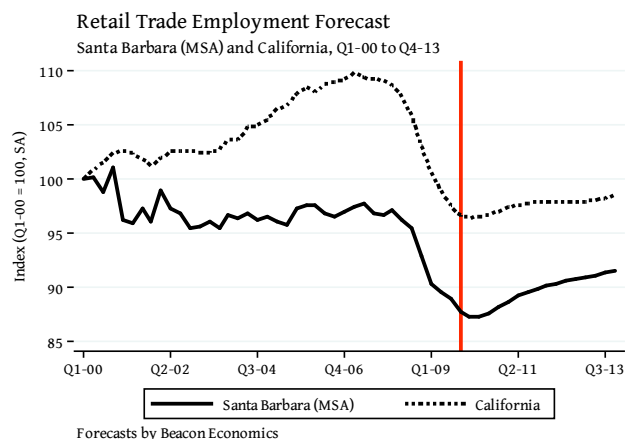
Despite the recent taxable sales gains, 2010 will remain very flat for Santa Barbara County. Consumers have curbed their debt driven spending habits of the

Retail trade employment experienced the third largest employment decline in the county...

last 20 years, and savings rates have moved in the right direction. But the gains in savings are not due to fundamental changes in consumer patterns, but rather due to the record low taxation consumers have been enjoying. Beacon Economics is still concerned that when these tax cuts end there will be another consumer slowdown. This means after we see a slight return to growth in 2010, the economy will slow again in 2011. The area will return to more historically normal growth in 2012.

Consumer Related Job Losses

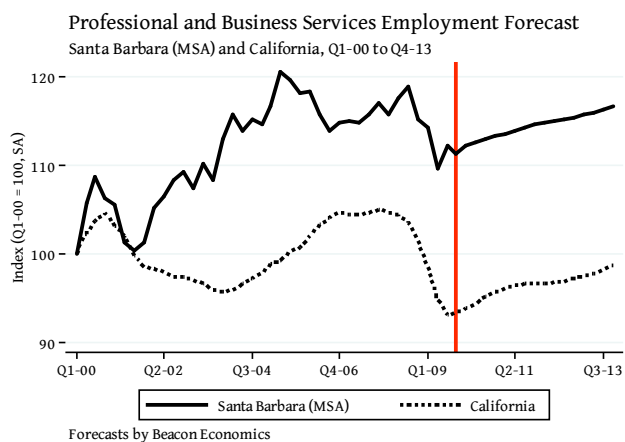
Although the housing imbalances had a large impact on the Santa Barbara economy, the effects were primarily limited to a narrow band of industries. Once the psychological effects of the housing meltdown had hit the consumer, the resulting job losses were spread across a broader spectrum of employers.



Retail trade employment experienced the third largest employment decline in the county, losing over 2,000 jobs—10.2%—from peak. This is despite

the fact that unlike its neighboring counties Santa Barbara had no significant buildup of new retail jobs prior to the recession. In fact, the county maintained around 20,000 retail trade employees between the beginning of 1999 and the end of 2008. During the same period, Ventura County increased its employment in retail sales by over 16.8%.

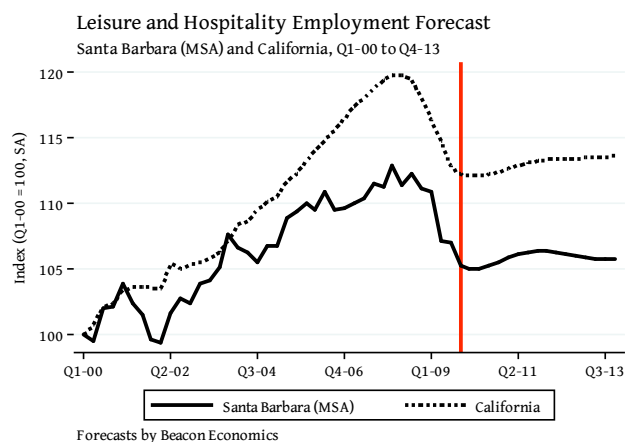
Consistent with the taxable sales forecast above, and with past growth in this industry, retail employment growth will be very slow. In fact, employment fails to return to the 20,000 employee level until well after the end of 2013.



Professional and business services began its slide earlier than most, beginning its employment drop in the fall of 2005. It continued to fall until the middle of 2006 when it rallied a bit into 2007. Then it went south again, ultimately losing nearly 1,500 jobs along the way. This industry, heavily dependent on business profits—and thus consumer spending—will take some time to recover. That said, this industry has already posted some job gains. According to our forecast, professional and business services will grow at a low pace for the foreseeable future.

...professional and business services will grow at a low pace for the foreseeable future.

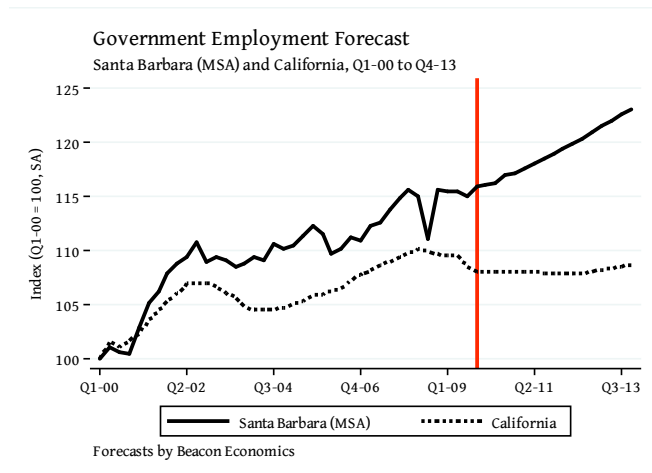
The second largest employer in the county, leisure and hospitality...is still on the decline.



Santa Barbara County has long been known as a tourist destination. Although it is less dependent on this sector than San Luis Obispo, tourism makes up a large piece of the county's economic spectrum. The second largest employer in the county, leisure and hospitality started to shed positions in early 2008, ultimately losing nearly 1,600 jobs. Thus far, this industry is still on the decline.

The decline, in part, stems from the considerable shift happening in leisure and hospitality. Large employers, such as banks, who in the past took advantage of the luxury accommodations the county has to offer, are now suffering from an embarrassment of riches and may not wish to be seen making purchases that could appear lavish. Thus, many employers when planning events such as conferences and retreats are looking for more affordable, cost-effective destinations.

At least in the short term, the South Coast will need to refocus its marketing efforts to bring in more of these cost conscious clients. The North County, on the other hand, has been marketing toward these clients for some time. With its growing wine industry, it's well poised to take advantage of the new market.

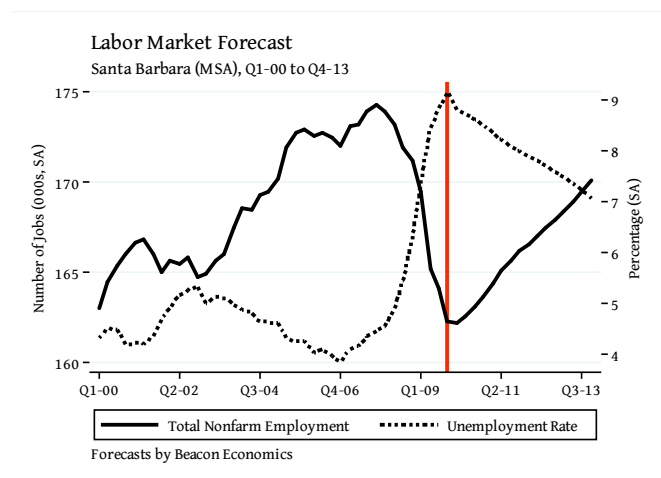


Despite the drop in home prices and taxable sales, which have surely led to decreases in tax revenues, government has been resistant to any job losses. Neither federal, state, nor local employment have lost one job in Santa Barbara County since the onset of the recession. Traditionally, government tries to fill in where business spending drops off, but at what cost? Local deficits are rising, and most municipalities will need to come up with a plan to recover from serious shortfalls. Beacon will be watching to see what plans and policies these municipalities initiate.

Neither federal, state, nor local employment have lost one job in Santa Barbara County since the onset of the recession.

Conclusion

Overall, Santa Barbara County was heavily affected by the recession. Although not as caught up in the housing boom as the counties surrounding it, the area nonetheless still lost a considerable number of housing related jobs. By not having the buildup of retail jobs during the rise of the bubble, there was relatively less fat to cut from that industry.



Despite feeling the full effects of the recession later than most in the state, Santa Barbara will pull out of the downturn along with the rest, meaning that most Santa Barbara residents will feel that the recession has been shorter than the duration experienced by others outside the region. The unemployment rate has already begun to fall, and jobs are on the rise. While the different regions of the county will continue to grow at different paces, they both share the same positive future.

Employment and Income

by Alexander Lin Beale

Beacon Economics

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Key Chapter Findings

- Santa Barbara County is the second-largest employment center in the Central Coast, employing 161,200 workers in nonfarm industries. Employment in the region has suffered in the current recession, declining 7.6% since November of 2007, corresponding to a loss of around 13,200 payroll positions. The county has seen a smaller relative decline than the state, where nonfarm employment has fallen 8.9%.
- Unemployment reached the highest level observable in the available data in October of 2009, when it reached 9.3%, but has fallen slightly since. The unemployment rate is higher in every other MSA in the state. As of January, there were 19,840 unemployed persons in Santa Barbara County.
- The Santa Barbara Metropolitan Statistical Area has had moderate growth in personal income over a long period of time. Annual personal income growth averaged 5.2%, from 1988 to 2008, but slowed dramatically between 2007 and 2008, increasing by just 3.8%.

South County

- Average annual wages in South County are significantly higher than in North County, owing to the greater prevalence of jobs in higher-paying sectors, including professional services, manufacturing, financial activities, and information. Note that average wages in the County overall are fairly low—\$5,000 below the state average—as Santa Barbara County's economy is heavily concentrated in low-wage sectors, notably agriculture, and leisure and hospitality.

North County

- North County's heavy engagement in agriculture—26% of employment in the north is at farms—depresses average wages in the area. However, it also mitigated the impact of the recession, as agricultural employment grew through the past two years. Average wages have been growing faster in the north, although there may be some risks to future growth as oil fields continue to shrink, and agriculture may be squeezed by rising production costs.

The Santa Barbara Metropolitan Statistical Area (MSA) is renowned for its pristine beaches, historic charm, and rolling countrysides, making the County a popular tourist destination, particularly for domestic travelers.³ The MSA is also widely known for having some of the priciest real estate in the nation. However, this is primarily characteristic of the southern portion of the County, where services, such as retail trade, leisure and hospitality, and professional and business services, are the major industries, and wages

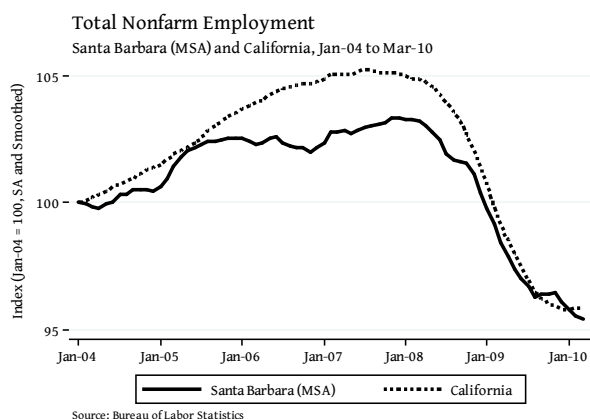
are significantly higher. Much of the popular image of Santa Barbara is associated with the southern side of the County. Agriculture predominates in the northern part of Santa Barbara County, although the area is also home to a number of tourist attractions, including several Spanish missions, the town of Solvang, and the local wine country. Historically, North County was heavily engaged in oil extraction, which provided fairly high-paying jobs and fueled much of the development in the area, but as the oil fields have dwindled, these activities have been scaled back, although there are still a number of off-shore oil rigs along the

³The Santa Barbara MSA comprises all of Santa Barbara County.

Overall, Santa Barbara County went into full-blown recession only slightly earlier than the nation, but employment growth came to a halt almost two years earlier.

coast of Santa Barbara County. In addition to agriculture, Vandenberg Air Force Base is a substantial driver of economic activity in the north.

Employment in the region is concentrated in five major sectors, accounting for over 60% of local employment—local government, leisure and hospitality, retail trade, agriculture, and health care. The remaining sectors in the MSA each provide under 12,000 payroll jobs. Santa Barbara's mix of industry has contributed to moderate but consistent growth in personal income over a long period of time—per capita income is above the state average. Nonetheless, personal income in the county has grown less than in the state or in its neighboring counties of Ventura and San Luis Obispo, notably since the recession in the early 1990s when the California defense industry saw significant declines. Even though Santa Barbara's housing-market bubble was substantial, it was not reflected in employment and income to the extent it was in areas such as the Inland Empire and the Southern Central Valley which were extremely exposed to the housing bubble and the use of subprime mortgages.



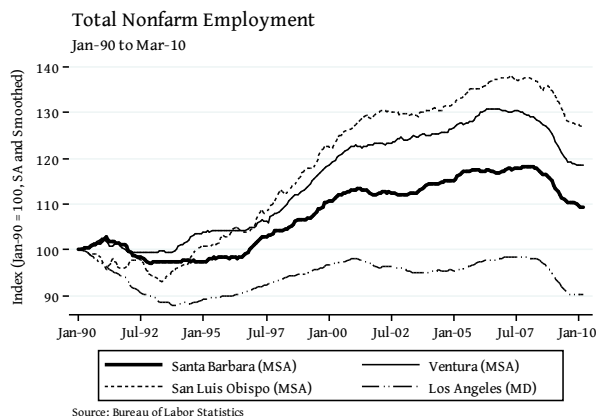
Employment in the Santa Barbara MSA was only mildly affected by the 2001 recession, which is some-

what surprising as the region was quite vested in sectors that brought about the downturn, such as information and hi-tech consumer electronics manufacturing. Some sectors that are also dependent on wider economic performance—including retail trade and leisure and hospitality—did see more substantial ups and downs at that time. Overall, employ-

Santa Barbara's mix of industry has contributed to moderate but consistent growth in personal income over a long period of time—per capita income is above the state average.

ment fell by 1.4% between April of 2001 and November of 2001, and stagnated through mid-2003. Thereafter, employment growth was slow, as the County added just 9,900 jobs (6%) between March of 2003 and November of 2007, the most recent peak in employment. In fact, Santa Barbara hit a plateau in employment in late 2005, after which employment fluctuated around 173,000. Since November of 2007, nonfarm employment in the Santa Barbara MSA has declined by 7.6%, shedding around 13,200 jobs and bringing employment numbers well below levels observed during the 2001 recession. This is a significantly lower rate of decline than observed in the state overall, where nonfarm employment has fallen by 8.9% since peaking in July of 2007. Overall, Santa Barbara County went into full-blown recession only slightly earlier than the nation⁴, but employment growth came to a halt almost two years earlier.

⁴The nation officially fell into recession in December of 2007 according to the National Bureau of Economic Research.



Although employment losses are showing signs of slowing, they are still occurring as a result of the three phases of this downturn: (1) the housing collapse, (2) the following financial crisis, and ultimately (3) the contraction in consumer spending. Each of these forces brought on significant job losses in specific industries, such as construction, finance and insurance, and retail trade. The relatively late onset of the re-

Since it began increasing in late 2006, the unemployment rate has risen by 5.6 percentage points to a peak of 9.3% in October of 2009. These are the highest levels observed since the data began...

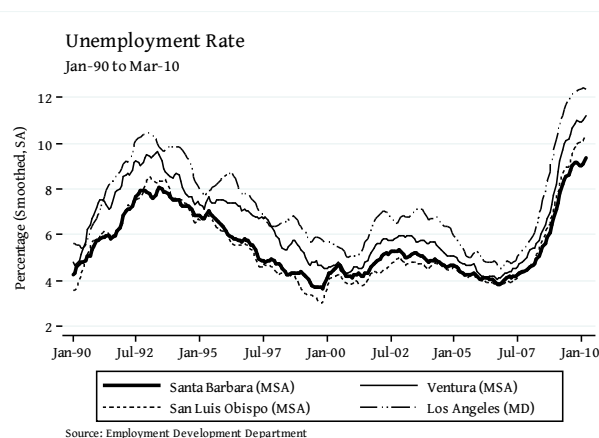
cent recession in Santa Barbara compared to most of California⁵ may be partially explained by the County's very moderate employment growth after the 2001 recession. Given that the region fell into recession somewhat late, and given that nonfarm employment continues to decline, Santa Barbara may not begin to see employment recovery for a few more months.

Unemployment

The unemployment rate in the Santa Barbara MSA began picking up after October of 2006, when it hit a low

⁵The State overall fell into recession in July of 2007

of 3.7%. Prior to that it had been gradually decreasing from a high of 5.4% following the dot-com bust. Unlike many areas of the state and the country, Santa Barbara County saw much higher unemployment rates in the 1992 recession than in the 2001 recession. Consequently, the county maintained unemployment levels below 6% from February of 1996 to November of 2008. Since it began increasing in late 2006, the unemployment rate has risen by 5.6 percentage points to a peak of 9.3% in October of 2009. These are the highest levels observed since the data began—1.3 percentage points higher than the previous peak levels recorded in mid-1993. Since October the unemployment rate has dropped slightly, to 8.9%.



Although higher than at any point in the available data, the unemployment rate in the Santa Barbara MSA is still the lowest in California, highlighting the dire condition of the state's economy and pointing to California as an epicenter of this recession. Only three metropolitan areas and divisions in the state have unemployment rates below the national average.

Although higher than at any point in the available data, the unemployment rate in the Santa Barbara MSA is still the lowest in California, highlighting the dire condition of the state's economy and pointing to California as an epicenter of this recession.

The largest employment losses in Santa Barbara have occurred in construction, and finance and insurance. These losses are directly tied to the causes of the current recession—the collapse of the housing market devastated construction employment, while the financial crisis necessitated cutbacks in finance and insurance.

Although there are a couple counties with lower unemployment rates, Santa Barbara currently ranks first out of 28 MSAs and MDs in California by unemployment rate. At 12.5% as of January, the statewide unemployment rate is 3.6 percentage points higher, but this still appears moderate, relative to areas in the Central Valley, such as Stockton, Modesto, and Merced, where the unemployment rate is at 16% and higher. While Ventura and San Luis Obispo counties are faring slightly worse—with unemployment rates of 10.8% and 10.0%, respectively—all three have fairly low unemployment rates compared to most of California.

Unemployment Rates (%), Jan. 2008-2010

Area	Jan-08	Jan-09	Jan-10
California	6.1	9.7	12.5
<i>Central Coast</i>			
San Luis Obispo	4.6	7.4	10.0
Santa Barbara	4.5	7.0	8.9
Ventura	5.1	8.1	10.8
<i>Southern California</i>			
Inland Empire	6.2	11.3	14.7
Los Angeles	5.9	10.1	12.5
Orange County	4.2	7.4	9.9
San Diego	4.8	8.2	10.7
<i>Bay Area</i>			
East Bay	4.8	8.6	11.5
San Francisco	4.0	7.1	9.5
San Jose	4.9	8.9	12.0

Source: California EDD

Currently, the California Employment Development Department estimates there are 19,838 unemployed persons in Santa Barbara County, 4,370 more than in January of 2009—a year-over-year increase of 28.3%. However, it is likely that this figure does not capture the full extent of out-of-work persons in the county, as the labor force has been fluctuating since March

of 2009, suggesting the presence of discouraged workers who have left the labor force. Persons who, after failing to find work for an extended period of time, give up their search for employment are no longer counted in employment and unemployment statistics. The number of unemployed persons has risen by 153.9% since October of 2006—an increase of over 12,000 people.

Employment by Industry

The largest employment losses in Santa Barbara have occurred in construction, and finance and insurance. These losses are directly tied to the causes of the current recession—the collapse of the housing market devastated construction employment, while the financial crisis necessitated cutbacks in finance and insurance. Although initial employment losses were greatest in construction and financial services, dwindling consumer spending and mounting unemployment spread these troubles across all sectors.

Currently, the California Employment Development Department estimates there are 19,838 unemployed persons in Santa Barbara County, 4,370 more than in January of 2009—a year-over-year increase of 28.3%....The number of unemployed persons has risen by 153.9% since October of 2006—an increase of over 12,000 people.

⁶The real estate sector in the Santa Barbara MSA has been in long-term decline, since the 2001 recession. Thus, the employment losses observed here are not directly attributable to the re-

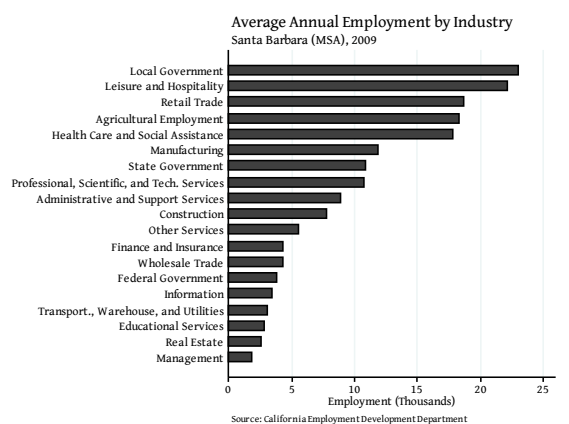
Santa Barbara (MSA) Industries Directly Affected by the Housing and Consumer Spending Downturns

Industry	Peak	Jobs Lost Since Peak	Percentage
Construction	Jun-06	-3,706	-34.7
Finance and Insurance	Jan-06	-1,524	-26.4
Real Estate ²	Dec-01	-1,271	-33.9
Retail Trade	Jul-08	-1,837	-9.1

Source: California Employment Development Department

The largest sector in the Santa Barbara MSA is local government, followed by leisure and hospitality, and retail trade.

The largest sector in the Santa Barbara MSA is local government, followed by leisure and hospitality, and retail trade. The local government sector provides over 23,000 full-time jobs, while leisure and hospitality and retail trade employ close to 22,100 and 18,700 persons, respectively. The majority of sectors have suffered employment declines at this point. Only three sectors, government, education and health services, and agriculture, sustained growth through 2008 and 2009.



As the largest sector in the metropolitan area, local government provides around 14% of nonfarm, full-time equivalent positions. This sector encompasses

cent housing and consumer spending downturns, but they are included here as this sector was directly and heavily affected in most areas.

all local public sector employees, including workers at government agencies, law enforcement and emergency personnel, and public school teachers. Local government employment reflects economic bubbles quite well, though there is typically a lag of one year between changes in economic cycles and changes in government employment. Nonetheless, due to the increased revenues generated by higher incomes and property values during bubble years, services and therefore employment are typically scaled up. When a bubble bursts, it takes a budget cycle to truly account for changes in projected revenues. Overall though, local government employment has grown at a fairly linear rate, as the level of government services provided is primarily dependent on population size and characteristics. Although there have been some job losses, no widespread layoffs are expected for public sector employees in Santa Barbara County. Note that the precipitous drop and recovery observable in mid-2008 is an anomaly in data collection and is not the result of an underlying shift in the sector.



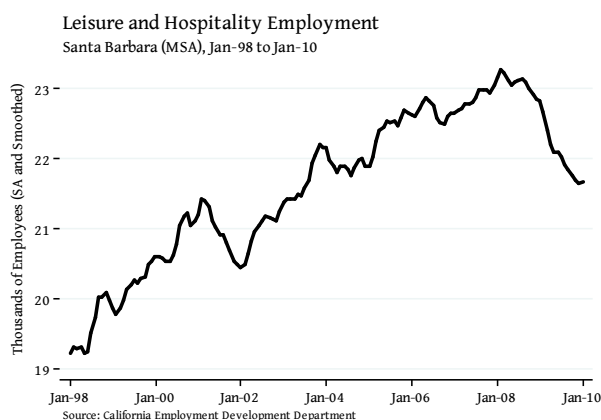
Leisure and hospitality is the mainstay of the Santa Barbara MSA's economy. It accounts for 13.5% of non-farm employment and almost 19% of private sector

Although there have been some job losses, no widespread layoffs are expected for public sector employees in Santa Barbara County.

employment, while contributing close to 5% to annual output. The sector has seen strong and fairly consistent employment growth over many years. Although employment did contract in the aftermath of the dot-com bust, the sector saw a healthy return to growth thereafter. Prior to the recent recession, employment was growing in line with trends observed leading into the 2001 recession. Employment at leisure and hospi-

Interestingly, taxable sales in the County grew unabated throughout this period, suggesting that the retail trade establishment as a whole reached a sustainable, balanced level of employment...

tality establishments peaked quite late, in February of 2008, shortly after the official onset of the recession nationwide. The sector was able to resist serious employment declines until October of 2008. From peak, the sector has shed almost 1,700 jobs, around 7.2% of payroll. Recovery in this sector will depend heavily on consumer behavior, which in turn hinges on returning job growth and an increase in the availability of credit.



Employment in the retail sector has been essentially stagnant since the 2001 recession. While the sector saw tremendous growth in the years leading up to the dot-com bust, once the bubble burst the sector contracted and did not return to growth. From April of 2002 to July of 2008 employment remained between

20,000 and 20,500 positions, fluctuating slightly from month to month. suited for the demand this sector experiences. Since July of 2008, the sector has lost approximately 1,840 payroll jobs, a 9.0% decline in retail trade positions. This sector is fairly intertwined with tourism in the region, and much like leisure and hospitality, will be dependent on the whim of consumers going forward—recovery will hinge on confidence and a return to lending, which banks continue to resist.

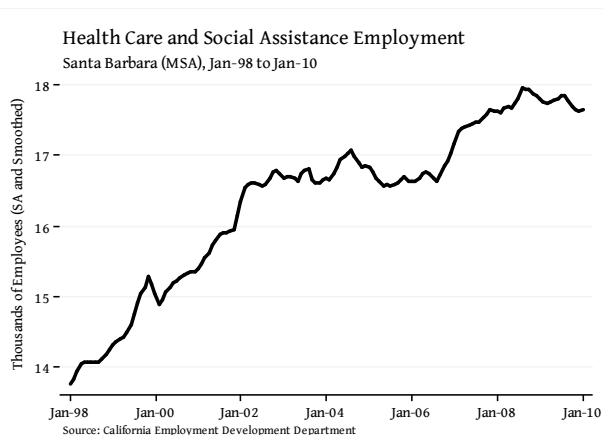


Health care is, without a doubt, the most stable sector in the region, having grown consistently through the last three recessions. This is the case in most regions of California. As with local government employment, the main driver of growth in this sector is the population. The demand for health care is not really subject to eco-

Health care is, without a doubt, the most stable sector in the region, having grown consistently through the last three recessions.

nomic whims. While people will certainly cut back on elective and cosmetic procedures, very few will opt to forego essential treatment. As the populace continues to age, and as diseases such as diabetes and cancer become ever more prevalent, the demand for health care services will only increase, ensuring that this sector will continue to enjoy strong growth. However, with the current debate on health care and the potential

introduction of a national health care plan, there may be some significant changes in this sector in the near future. Additionally, a significant challenge for health care providers arising at this time is the increasing number of people who are losing their health insurance coverage due to job loss.



Santa Barbara (MSA)

Employment by Industry, 2009 Annual Average

Industry	
Local Government	23,034
Leisure and Hospitality	22,099
Retail Trade	18,671
Agricultural Employment	18,329
Health Care and Social Assistance	17,759
Manufacturing	11,851
State Government	10,914
Professional, Scientific, and Tech. Services	10,692
Administrative and Support Services	8,903
Construction	7,709
Other Services	5,517
Finance and Insurance	4,258
Wholesale Trade	4,244
Federal Government	3,734
Information	3,475
Transport., Warehouse, and Utilities	3,051
Educational Services	2,816
Real Estate	2,600
Management	1,775

Source: California Employment Development Department

Employment by Firm Size

Given that larger employers generally have higher operating costs and more redundancy, it seems intuitive that the majority of employment contraction will have been in the larger firm size classes. Larger firms can cut costs fairly rapidly by reducing payroll, without a major impact on operations and productivity. That said, data from the Bureau of Labor Statistics shows that many of the recent terminations nationally have been in the smaller employment size classes, which have smaller cash cushions and are more susceptible to short-term volatility.

Smaller firms do not have as many options for reducing costs and are therefore more likely to fail. At this time, in particular, small businesses are facing a severe credit crunch. The traditional sources of financing for small firms—credit cards, home equity, and small, local banks—have either been curtailed or are facing significant problems of their own. According to a recent article in the *Economist*, firms with fewer than 50 employees have suffered around 45% of job losses to date, while employing roughly one-third of U.S. workers.⁷

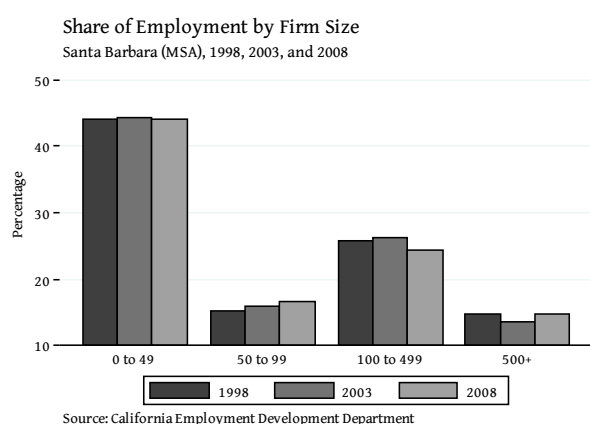
Additionally, a significant challenge for health care providers arising at this time is the increasing number of people who are losing their health insurance coverage due to job loss.

⁷The *Economist*, "For want of a loan," December 12-18, 2009, p.33.

Pre-Recession vs. Recession Employment Trends, Santa Barbara (MSA)

Sector	Avg. Annual Employment Chg.		
	2002-2007	2007-2009	Off Trend
Construction	491	-1,373	-1,864
Retail Trade	1	-836	-837
Leisure and Hospitality	381	-376	-756
Manufacturing	-27	-699	-672
Financial Activities	-78	-680	-602
Professional, Scientific, and Technical Services	321	-187	-509
Wholesale Trade	1	-262	-263
Other Services	9	-254	-262
Administrative and Support Services	-42	-290	-248
Natural Resources and Mining	68	-162	-230
Information	-45	-208	-162
Education and Health Services	212	133	-79
Transportation, Warehousing, and Utilities	44	9	-36
Management of Companies and Enterprises	40	54	14
Government	256	329	72
Agriculture	356	1,147	791

Source: California Employment Development Department

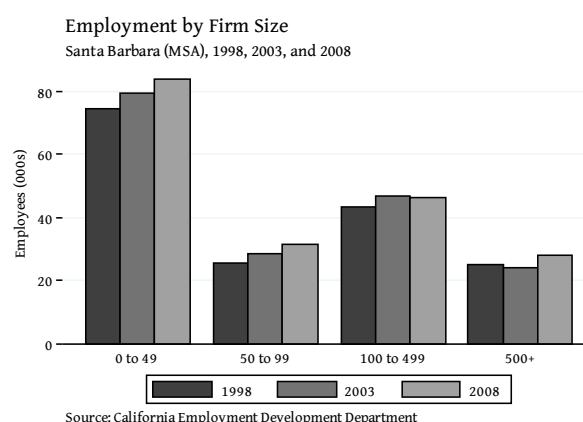


Santa Barbara County's employment structure by firm size has been very stable over the past decade, though there has been a minor shift from firms with 100 to 499 employees to the next-smallest firm size class. By far the largest share of employment in 2008 was at firms with less than 50 employees, at 44.2%, the exact same share of workers that worked at these firms

The traditional sources of financing for small firms—credit cards, home equity, and small, local banks—have either been curtailed or are facing significant problems of their own.

By far the largest share of employment in 2008 was at firms with less than 50 employees, at 44.2%, the exact same share of workers that worked at these firms in 1998.

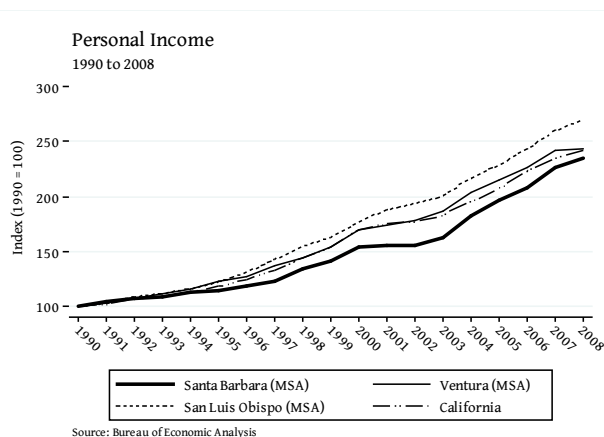
in 1998. The share of employees working at firms with 50 to 99 employees has increased by 1.4%, which corresponds exactly to the loss in employment share at firms with 100 to 499 employees. Like the smallest firms, establishments with over 500 employees have had no change in their share of employment.



The underlying data show that the shift in share is indeed due to declining employment at firms with 100 to 499 employees, particularly in the past four years, and not a result of any exceptional employment growth at firms with 50 to 99 workers. Employment at large firms declined through 2006, but saw significant growth in 2007 and 2008. The largest firm size class was also the only category that saw an overall increase in employment from 2007 to 2008. Most of the largest employers in the County are government agencies, schools, hospitals, or farms, all of which fall into sectors that have proven fairly resilient to economic cycles.

Income and Wages

Santa Barbara County's mix of industry has fostered consistent but fairly moderate growth in personal income over a long period of time. The dot-com bubble had a significantly smaller impact on personal income than on employment in the area. Rather than a substantial spike, there is only a slight acceleration in growth leading up to 2000, followed by two years of essentially zero growth. Nonetheless, this plateau shows that the area was more heavily vested in the high-tech sector than surrounding counties and the state overall. The effects of the current recession still appear to be fairly moderate, as growth only slowed between 2007 and 2008.



From 1990 to 2007, annual growth in personal income averaged 4.9%. In the years since the most recent recession, personal income has grown an average of 7.8% per year, but from 2007 to 2008 personal income grew by just 3.8%, less than half the average growth in the prior five years. Personal income in Santa Barbara County has grown at a slower pace than in San Luis Obispo and Ventura counties, and the state overall, particularly since the recession of the early 1990s, although there has been some convergence in recent years. Note that growth in personal income is also dependent on population growth, which is fairly weak in Santa Barbara County. On a per capita basis, Santa Barbara is outperforming all of these areas.

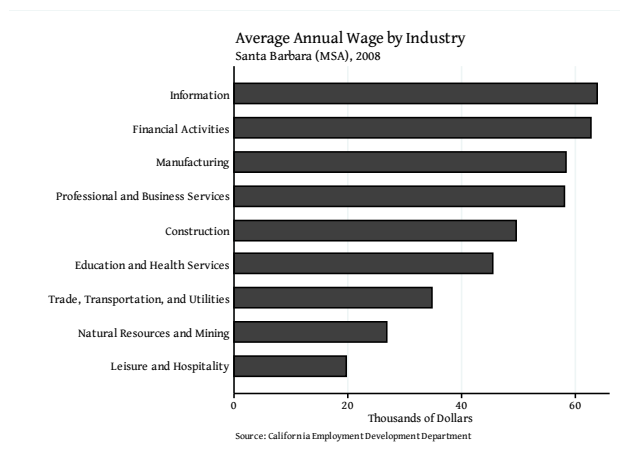
Average Annual Wages and Growth, 2008

Area	2008 (\$)	2001-2008 Absolute Chg.	2001-2008 (%) Change
San Francisco County	75,062	16,367	27.9
Los Angeles County	56,615	11,804	26.3
Ventura County	56,615	13,754	32.1
San Diego County	54,171	11,765	27.7
Santa Barbara County	51,818	12,012	30.2
San Luis Obispo County	47,255	10,621	29.0
California	56,927	11,999	26.7

Source: California Employment Development Department

Although per capita personal income is fairly high, other measures of income, including median family and household income, fall below those of the state. Much of personal income in the County (over 30%) is derived from non-wage sources, as such, average annual wages in the County are quite low, over \$5,000 less than the statewide average. At \$51,818, average wages are still higher than in San Luis Obispo County, but lower than in Ventura County and the major metropolitan areas of California. However, average wages have been growing fairly quickly, outpacing growth in Los Angeles, San Francisco, and the state. The rest of the Tri-County area has seen similar relative increases in average compensation. The highest-earning sector in Santa Barbara County is information, paying an average of over \$60,000, while workers in the lowest-paying jobs, in leisure and hospitality, make an average of around \$20,000.

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The following sections break out employment and wages by industry for northern and southern Santa Barbara County. These data are aggregated from zip-code level data, obtained from the Quarterly Census of Employment and Wages (QCEW). Unfortunately, QCEW data lags by nine months, so a model was used to generate a rough estimate of current employment in these areas, using data at the county level as a guide. Each employment table presents data from December of 2007 (the official onset of recession nationwide), June of 2009 (the most recent month of actual data), and an estimate for January of 2010.

The highest-earning sector in Santa Barbara County is information, paying an average of over \$60,000, while workers in the lowest-paying jobs, in leisure and hospitality, make an average of around \$20,000.

South County

Roughly half of the industries in southern Santa Barbara County are expected to still be suffering employment declines at this point. However, eight industry clusters along the "South Coast," including government, education and health care, professional and business services, and agriculture are expected to already have entered into recovery and to have improved their from position six months ago.

Three sectors, education and health care, administrative and support services, and management of companies and enterprises, are expected to have seen overall gains in employment during the course of the recession.

The following table breaks out employment by geographic place. Note that this includes unincorporated portions of the county, which are associated with nearby incorporated communities to simplify analysis and distinguish between unincorporated areas of northern and southern Santa Barbara County. The single largest employment center is the City of Santa Barbara, providing more than 40% of jobs in the county. This is not particularly surprising, given that the South Coast employs more than 60% of workers in the County. All three areas in southern Santa Barbara are beginning to see some tentative employment recovery.

Total Employment by Place, South Santa Barbara County

City/Area	Dec-07	(%) Change Dec-07 to Jun-09	Jun-09	(%) Change Jun-09 to Jan-10	Jan-10 (Est.)
Carpinteria	8,686	-5.0	8,249	2.5	8,457
Goleta	36,009	-6.0	33,836	0.6	34,033
Santa Barbara	82,766	-5.6	78,161	0.9	78,880

Source: California Employment Development Department

Employment by Industry and Percentage Change, South Santa Barbara County

Sector	Dec-07	(%) Change Dec-07 to Jun-09	Jun-09	(%) Change Jun-09 to Jan-10	Jan-10 (Est.)
State & Local Government	21,110	-5.6	19,938	1.7	20,280
Leisure & Hospitality	15,273	-2.3	14,917	-2.1	14,605
Education & Health Care	13,330	-0.2	13,298	0.6	13,384
Retail Trade	11,452	-7.8	10,564	-1.7	10,383
Prof., Sci., & Tech. Svcs.	7,587	-6.7	7,078	1.5	7,186
Manufacturing	7,803	-9.0	7,103	-2.8	6,903
Admin. & Support Svcs.	6,133	-1.9	6,017	5.9	6,373
Financial Activities	5,613	-14.5	4,799	-4.4	4,587
Other Services	4,577	-0.7	4,544	-3.7	4,374
Construction	6,006	-21.4	4,721	-12.0	4,153
Agriculture	3,150	-14.5	2,693	10.9	2,986
Information	3,095	-5.7	2,919	-3.9	2,805
Wholesale Trade	2,777	-12.6	2,426	0.4	2,436
Management	1,239	0.2	1,242	4.4	1,297
Transport., Warehouse, & Util.	974	-5.0	925	-0.5	920
Federal Government	461	-6.7	430	5.6	454
Nat. Resources & Mining	231	1.7	235	-7.7	217

Source: California Employment Development Department

The highest-paying sectors in the southern portion of the County are mining and management of companies and enterprises, each of which pays in excess of \$110,000 per year. Thereafter there is a significant drop in average earnings. The next-highest earning sector—utilities—pays its workers an average of just \$78,680. The highest-paying industries have also seen the greatest growth in average annual wages over the course of the available data, although utilities and administrative and support services (one of the lower-paying sectors) have seen substantial growth as well. The weakest growth has been in retail trade and leisure and hospitality (the lowest-paid sector), which holds down average wages for the region, as these are two of the largest sectors by employment.

Average Annual Wages and Growth by Sector, 2009

Sector	2009 (\$)	2003 to 2009 (\$ Change)	2003 to 2009 (%) Change
Agriculture	27,363	2,268	9.0
Mining	117,333	40,677	53.1
Construction	48,127	7,503	18.5
Manufacturing	69,606	9,486	15.8
Wholesale Trade	54,399	6,316	13.1
Retail Trade	30,666	2,454	8.7
Transport. & Warehouse	38,203	8,401	28.2
Utilities	78,680	23,377	42.3
Information	66,498	9,703	17.1
Financial Activities	68,219	7,386	12.1
Prof., Sci., & Tech. Svcs.	75,255	12,932	20.8
Admin. & Support Svcs.	41,720	13,324	46.9
Management of Co. & Ent.	113,923	60,976	115.2
Education & Health Care	48,735	10,095	26.1
Leisure & Hospitality	20,071	649	3.3
Other	26,981	2,790	11.5
Government	53,544	9,361	21.2
All Industry Average	47,552	6,580	16.1

Source: California Employment Development Department

North County

The breakout of industry employment for North County highlights the predominance of agriculture in

Employment by Industry and Percentage Change, North Santa Barbara County

Sector	Dec-07	(%) Change Dec-07 to Jun-09	Jun-09	(%) Change Jun-09 to Jan-10	Jan-10 (Est.)
Agriculture	13,956	9.9	15,333	17.9	18,084
State & Local Government	10,147	-0.4	10,109	0.0	10,104
Retail Trade	8,716	-7.1	8,095	-2.0	7,934
Leisure & Hospitality	7,472	-6.0	7,023	-0.2	7,010
Education & Health Care	6,750	3.3	6,970	0.0	6,970
Manufacturing	4,766	-14.7	4,067	0.1	4,070
Construction	3,851	-24.8	2,896	-8.7	2,644
Admin. & Support Svcs.	3,218	-21.4	2,529	2.8	2,599
Other Services	1,660	59.2	2,642	-2.1	2,587
Financial Activities	2,535	-25.5	1,888	-0.2	1,885
Prof., Sci., & Tech. Svcs.	2,026	-9.8	1,828	2.4	1,872
Wholesale Trade	2,077	-17.4	1,715	3.3	1,771
Transport., Warehouse, & Util.	1,492	1.4	1,513	-5.4	1,431
Information	804	-22.8	621	-3.1	602
Federal Government	282	-2.5	275	0.0	275

Source: California Employment Development Department

the region: 26% of employment in northern Santa Barbara is in the agricultural sector and 86% of agricultural employment in the County is in the north. However, the data also demonstrate the relative importance of tourism and retail trade to the area, with North County contributing significantly to these activities. Retail trade employment in the northern part of Santa Barbara County accounts for 45% of retail employment countywide and roughly one-third of workers in leisure and hospitality are employed in the north. It is expected that more sectors in North County are still in decline. Only five sectors are estimated to have had employment gains since June of 2009, and only agricultural employment and health care are expected to have grown through the recession. Other services employment likely declined from June of 2009 to January of 2010, but the sector has still grown tremendously since December of 2007, which represents a major outlier.

Employment by place in northern Santa Barbara County is of interest, as Santa Maria is in all likelihood still experiencing job losses. This appears to be the only area with ongoing employment declines, which is plausible, given that total employment in the County has been relatively stable since June of 2009,

although nonfarm employment continues to decline. Also of note is that although the population is roughly evenly split between north and south, employment is heavily concentrated in the South Coast.

Total Employment by Place, North Santa Barbara County

City/Area	Dec-07	(%) Change Dec-07 to Jun-09	Jun-09	(%) Change Jun-09 to Jan-10	Jan-10 (Est.)
Lompoc	9,911	-2.6	9,651	2.4	9,879
Santa Maria	50,410	-1.8	49,515	-1.0	49,043
Santa Ynez	10,887	-5.7	10,271	0.2	10,289

Source: California Employment Development Department

Average annual wages are lower across the board in northern Santa Barbara County. Every single industry pays less on average than its counterpart in the South Coast. The average annual wage across all industries is a whopping \$15,034 higher in the southern portion of the County. Workers in the north earn just \$0.68 for every \$1 earned by a worker in the south. The highest-paying sector in the north is management of companies and enterprises, at \$84,355, followed by mining, at just \$65,587. Thereafter, average wages drop to around \$45,000, which is the average annual compensation for six different industries. Wages grew fastest in the management sector, increasing by 67.8% over six years. Other sectors with relatively fast growth

include information, government, and education and health care, but their wages grew at less than half the rate that management wages did. Interestingly, some sectors had much more dramatic wage growth in the South Coast than any sector in North County, but overall average wages are growing faster in the northern part of Santa Barbara County.

Average Annual Wages and Growth by Sector, 2009

Sector	2009 (\$)	2003 - 2009 (\$ Change)	2003 - 2009 (%) Change
Agriculture	21,791	2,494	12.9
Mining	65,587	14,459	28.3
Construction	45,618	7,325	19.1
Manufacturing	40,519	6,109	17.8
Wholesale Trade	45,001	5,452	13.8
Retail Trade	25,801	1,400	5.7
Transport. & Warehouse	38,062	7,347	23.9
Utilities	45,548	9,471	26.3
Information	46,856	11,224	31.5
Financial Activities	40,042	1,764	4.6
Prof., Sci., & Tech. Svcs.	44,470	7,323	19.7
Admin. & Support Svcs.	24,819	2,988	13.7
Management of Co. & Ent.	84,355	34,096	67.8
Education & Health Care	37,705	8,056	27.2
Leisure & Hospitality	16,486	2,317	16.3
Other	21,377	865	4.2
Government	46,027	9,980	27.7
All Industry Average	32,518	4,809	17.4

Source: California Employment Development Department

Business Activity

by Riley Newman

Beacon Economics

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Key Chapter Findings

- In 2008, as in past years, Santa Barbara MSA's economy ranked 11th among California's 26 metropolitan statistical areas.
- Gross domestic product grew steadily through 2005, before the recession set in. Thanks to the commodity price boom, mining and agriculture buoyed the economy in 2007, but growth contracted in 2008 as commodity prices came back to earth.
- The professional, scientific, and technical services sector exhibited strong growth prior to the recession, becoming the third-largest contributor to local GDP.
- A survey of business sentiment reveals growing optimism among the county's business owners, especially regarding their perception of the six months ahead.

North County

- Harder hit than the south, northern Santa Barbara county suffered from greater retail sales contraction as a result of the recession. Cheaper rooms have, however, managed to attract more tourism, abating recessionary forces.

South County

- The wealthier southern portion of Santa Barbara County has also felt the recession's pinch, although retail sales have fared slightly better, particularly the apparel industry. Traditionally expensive accommodation rates have been forcibly reduced as travelers have sought out better deals. Some believe this to be a paradigmatic shift that will outlive the recession.

Business activity in the Santa Barbara metropolitan statistical area is like a microcosm of California overall. Its mediterranean climate is as valuable for the tourists it attracts as the wine grapes it breeds. But it is far from dependent on tourism, with footholds in both agriculture and cutting-edge science. A large housing bubble prior to the recession has undoubtedly taken its toll on local commerce, especially consumer

Santa Barbara...is far from dependent on tourism, with footholds in both agriculture and cutting-edge science.

spending, but a growing optimism ensures future success. In this section, our analysis of business activity in the county draws upon a variety of data, includ-

ing gross domestic product by industry, commercial building permits, taxable sales, a survey conducted by the UCSB Economic Forecast Project, hotel industry estimates, and indicators of the wine industry's performance.

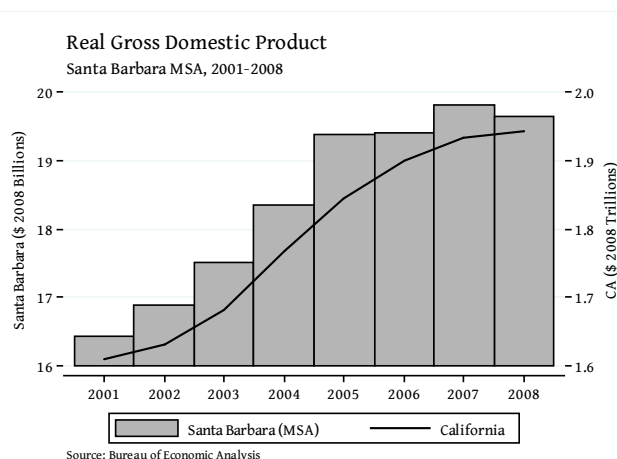
Local Gross Domestic Product

Gross domestic product, calculated as the sum of production value-added across industries, is one of the broadest performance indicators available to economists. By this measure, we are able to determine, for example, that California comprises the largest share of the U.S. economy,⁸ and would consti-

⁸13.4% in 2008.

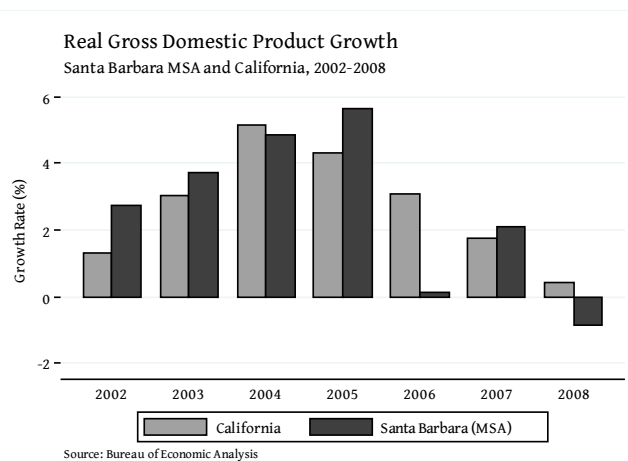
tute the world's tenth largest economy if it were its own country.⁹

On a more local level, the Bureau of Economic Analysis reports annual output data for the Santa Barbara metropolitan statistical area dating back to 2001. As of 2008, the most recent year for which data are available, Santa Barbara's GDP ranked 11th among California's 26 metropolitan statistical areas. That year the county added approximately \$20 billion in value to goods and services produced locally – almost double that of nearby San Luis Obispo MSA, and half that of Ventura MSA.



As many local business leaders will attest, Santa Barbara has not been spared the wrath of the recession. In 2008, the metropolitan area's total output had dropped 0.9% from its 2007 peak, but remained a solid 19.6% above 2001.¹⁰ Year-over-year growth was positive through 2005, after which the recession began to take hold. In 2006, declines in the information, administrative and waste, and finance and insurance industries restricted growth to a meager 0.1%. And this contraction would likely have continued in 2007 but for the global rise in commodity prices. Output in the farming and mining sectors – two key arenas for Santa Barbara's economy – outweighed losses else-

where, contributing to a 2.1% rise in GDP over 2006. As commodity prices came back to earth, Santa Barbara's contracting industries outweighed agriculture and mining, resulting in the negative growth between 2007 and 2008.



The information sector has felt the most pain through the recession,¹¹ shedding almost 20% of output between 2005 and 2008. However, most of this was due to a significant decline between 2005 and 2006, after which time the industry managed to stabilize. Con-

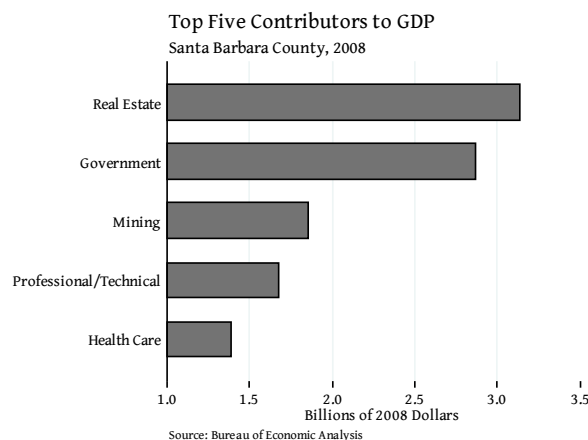
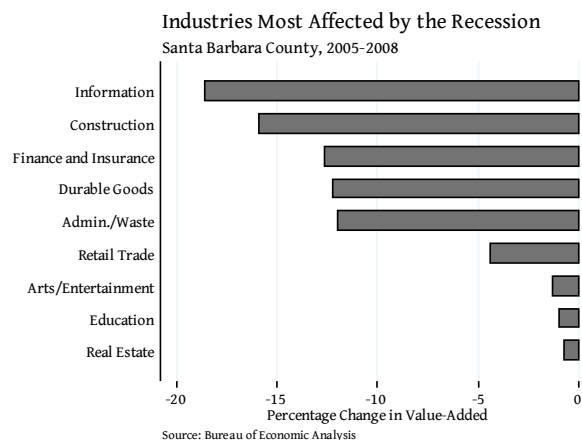
*As many local business leaders will attest,
Santa Barbara has not been spared the
wrath of the recession.*

struction was the next hardest hit, as the real estate bubble burst throughout California. Financial services followed in construction's footsteps, as declining property values resulted in mortgage defaults and foreclosures; and the recession spread shortly thereafter throughout the rest of Santa Barbara's business community.

⁹Calculated using 2008 dollars in purchasing power parity terms by the International Monetary Fund. California falls just behind Brazil and ahead of Italy.

¹⁰All calculations here are in real 2008 dollars.

¹¹Defined here as the period following 2005.



Pre-Recession Contributors to Real GDP in Santa Barbara MSA

Rank	Industry	2001 (\$ 2008 mill.)	2005 (\$ 2008 mill.)	Growth (%)
<i>Fastest-Growing</i>				
1	Construction	682	980	44
2	Farming	801	1,110	39
3	Professional/Technical	1,124	1,505	34
4	Mining	1,127	1,492	32
5	Finance and Insurance	783	997	27
<i>Largest</i>				
1	Real Estate	2,772	3,159	14
2	Government	2,364	2,700	14
3	Professional/Technical	1,124	1,505	34
4	Mining	1,127	1,492	32
5	Retail Trade	1,301	1,446	11

Source: Bureau of Economic Analysis

As was the case for most metropolitan areas of California, construction was the fastest-growing industry before the recession. Between 2001 and 2005, it grew 44% in Santa Barbara (in real 2008 dollars), ending 2005 just short of a billion dollars in annual value-added production. Farming exhibited the next largest

Despite the impact of the recession, most of Santa Barbara's top contributors to GDP remained the same in 2008.

growth during this time, thanks mostly to strong output in 2002 and 2003. And Santa Barbara's burgeoning professional, scientific, and technical services sector was also expanding rapidly, adding to its already large size.

Despite the impact of the recession, most of Santa Barbara's top contributors to GDP remained the same in 2008. As in 2005, real estate topped Santa Barbara's industry rankings in 2008. However, this is more of a reflection of the low cost of maintaining real estate (commercial as well as residential) relative to strong returns for rents and sales than simply the strength of sales overall. Professional, scientific, and technical services fell in relation to mining, given the commodity price boom in 2007 and 2008; and retail sales were knocked out by the recession, leaving health care, a classic economic stalwart, in fifth place.

Commercial Building Permits, 2007-2009

Santa Barbara County (\$ thousands)

Category	Q4-2007	Q4-2008	Q4-2009
Hotels	16,564	29	0
Industrial	4,798	1,639	2,317
Office	5,315	0	2,671
Stores	1,818	1,777	3,947
Commercial	19,202	2,214	10,864
Non-Res. Alts	23,972	22,321	16,193
Non-Res. Total	55,320	34,021	37,394
Total Permits	113,838	78,313	85,461

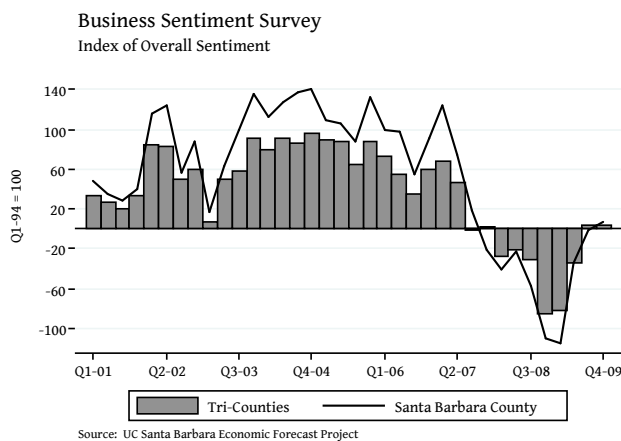
Source: Construction Industry Research Board

While construction has been hit hard by the recession, the fourth quarter of 2009 witnessed a rebound in some arenas of commercial development activity. Building permits for industrial structures grew 41.4%

over the fourth quarter of 2008, after a 65.8% fall over the fourth quarter of 2007. Similar gains were made in permits for office and commercial structures, and permits for stores exceeded the Q4-2007 values by 117.1%. A decline in permits for alterations to existing structures – typically the most lucrative permit for the county – restricted permits for nonresidential structures overall to 9.9% growth. Nevertheless, this is a much more positive picture than was the case last year.

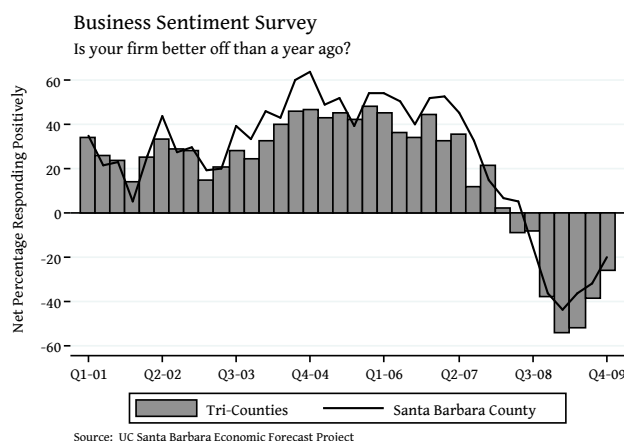
Business Sentiment

Santa Barbara's economic topography is, of course, a moving target. And a critical component to growth is the impressions held by current members of the business community about the future. In order to identify such trends, the UCSB Economic Forecast Project conducts a survey each quarter of local business owners about their perceptions of the economy. The results of the survey paint an optimistic picture of what's ahead for Santa Barbara.



According to the overall index of business sentiment, the fourth quarter of last year represented the first instance of a net positive outlook in almost two years. While the marginally weaker trajectory between the third and fourth quarters relative to the first and second, and second and third, reflects the less-than-

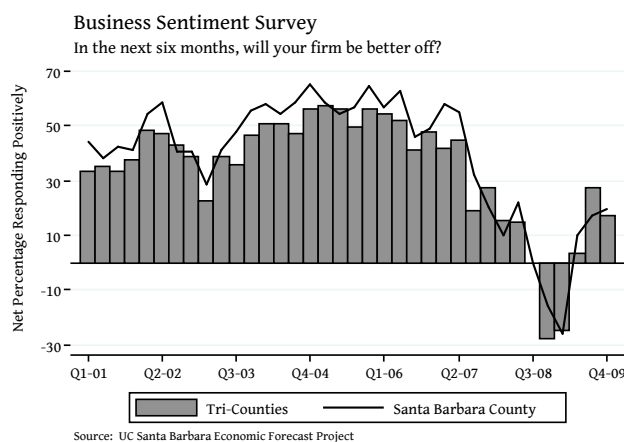
anticipated sales surrounding the holiday season, the degree of optimism relative to late 2008 is profound.



Recovery will, however, take time. When asked how their firm stood relative to the year prior, the net response remained negative as of the fourth quarter of 2009. This was true throughout the Tri-County area as

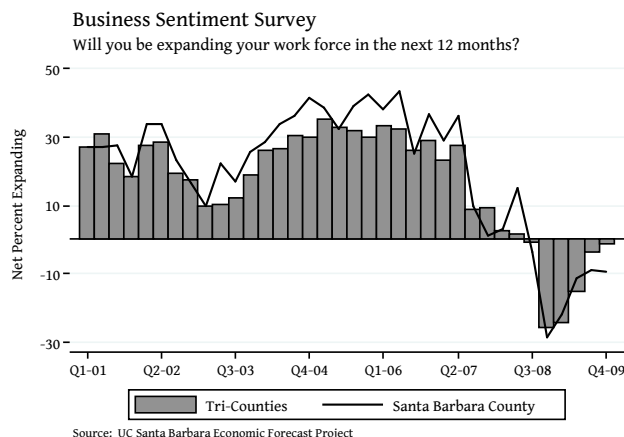
The results of the survey paint an optimistic picture of what's ahead for Santa Barbara.

well as in Santa Barbara. But here again we see an upward trajectory from the depths of pessimism in late 2008.



Perhaps the most important question is how local businessmen perceive the near future relative to

where they currently stand. Optimism regarding the future invokes consumption and investment in the present, and America's legendary optimism is clearly reviving in Santa Barbara. There were only two quarters in which the net response was negative, but the rebound since has been strong. Despite a reduction in the positive outlook in the fourth quarter, responders overall still view the future favorably.



Economic recovery will not be complete, however, until the unemployment rate eases. In hopes of determining the likelihood of such an event, the survey included a question about hiring decisions in the next year. In this light, there remains some restraint among Santa Barbara's business leaders relative to the broader Tri-County area. The fourth quarter, again,

The "cash for clunkers" program was especially useful in Santa Barbara, given the beating the auto sales industry endured between 2007 and 2008.

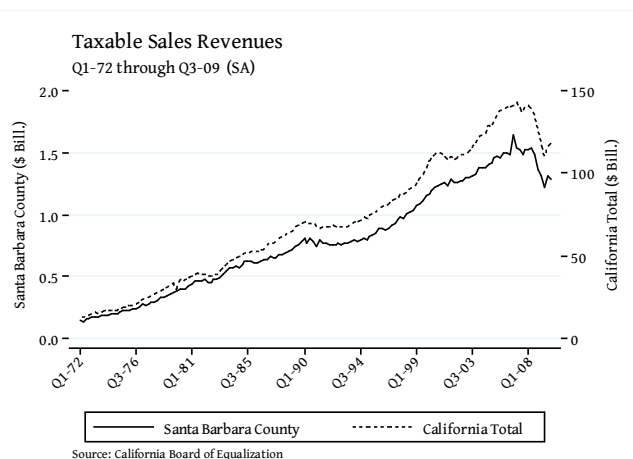
dampened the rebounding optimism since late 2008, but a return to expansion nevertheless appears close at hand.

Taken together, it is easy to see the light at the end of the tunnel. While firms are not yet comfortable with where they currently stand relative to a year ago, the trajectory of business sentiment is clearly upward.

Most respondents believed their firm will be better off in the next six months, which speaks well to future hiring decisions.

The Consumer

Consumer spending is the most significant component of the U.S. economy and is similarly important for Santa Barbara. In 2008, the county witnessed \$5.9 billion in sales, almost double that of San Luis Obispo County and about half that of Ventura County.



But consumer spending has been hit hard by the recession, and Santa Barbara has fared no better than the state overall. Indeed, spending contracted over 23% across California between the peak in the first quarter of 2007 and the \$110 billion trough in the second quarter of 2009, before rising 4.5% in the third quarter. In Santa Barbara County, the peak occurred one quarter earlier, but the rebound in the third quarter of 2009 is the same. Most of this return to growth can be attributed to government intervention, especially the "cash for clunkers" program and the first-time home-buyer's tax credit.

The "cash for clunkers" program was especially useful in Santa Barbara, given the beating the auto sales industry endured between 2007 and 2008. As is true across California, vehicle sales declined substantially

Taxable Sales by Category
 Santa Barbara County

Category	2008 (\$ millions)	2007 (\$ millions)	Change (%)
Totals All Outlets	5,884	6,067	-3.0
Retail Stores Totals	4,097	4,429	-7.5
Apparel stores	235	221	6.4
General merchandise	614	674	-9.0
Food stores	302	295	2.3
Eating and drinking	677	676	0.1
Home furnishings/appliances	175	189	-7.4
Building materials	385	489	-21.3
Automotive	536	671	-20.0
Service stations	545	485	12.2
Other retail stores	629	729	-13.6

Source: California Board of Equalization

— in Santa Barbara's case by 20%. The only retail category more affected was building materials, as demand for new construction halted. The most positive growth of any component of retail sales came from service stations, as the high price of oil commanded strong revenues and consumers opted for fixing their cars over buying new ones. This wasn't enough, however, to prevent the 3% contraction in taxable sales overall.

North County and South County

Geography plays an important role in economic patterns within Santa Barbara County, and taxable sales provide one of few opportunities among business indicators to examine these differences. Using the Board of Equalization's city-level data we can differentiate some of the trends in consumption between the northern and southern regions of Santa Barbara County.

Total taxable sales in Santa Barbara's North County — defined as the sum of sales in Buellton, Guadalupe, Lompoc, Santa Maria, and Solvang cities — constituted 35.6% of sales across the county in 2008. For comparison, the same figure for the wealthier south — defined here as the sum of sales in Carpinteria, Goleta, and Santa Barbara cities — was 43.7% that year. Consumers in both North County and South County reduced their

spending between 2007 and 2008, although the contraction was greater in the north.

Taxable Sales
 North County and South County, \$ millions

Category	North County			South County		
	2008	2007	Chg (%)	2008	2007	Chg (%)
Retail Stores	1,647	1,841	-10.5	2,018	2,134	-5.4
Apparel	47	50	-7.1	170	152	11.4
General merchandise	353	363	-2.6	277	326	-15.0
Food	107	99	8.3	146	145	0.3
Eating & drinking places	182	181	0.9	389	385	1.0
Home furnishings/appliances	51	44	15.2	106	119	-11.3
Building materials	160	235	-31.6	204	230	-11.1
Motor vehicles/parts	328	426	-22.9	215	254	-15.3
Service stations	202	169	20.0	222	193	15.1
Other retail stores	215	275	-21.8	289	329	-12.1
Totals All Outlets	2,094	2,212	-5.4	2,570	2,650	-3.0

Source: California Board of Equalization

In general, the trends were similar between north and south: spending on merchandise, building materials, and vehicles decreased; eating and drinking establishments saw mild growth, and service stations performed quite well. However, consumers in the south

Consumers in both North County and South County reduced their spending between 2007 and 2008, although the contraction was greater in the north.

increased their spending on apparel, while those in the north cut back. Meanwhile, spending on home furnishings grew dramatically in the north but declined in the south.

Tourism

Santa Barbara County is one of the most attractive tourist destinations in California. An iconic California coastal region, the "American Riviera" draws visitors each year from around the world. A recent study by Dean Runyan Associates estimates the value of tourism to be in the billions for the local economy, the majority of which falls to restaurants and bars, accommodation centers, and retail. As of 2007, approximately 16,000 jobs — almost 10% of total nonfarm

employment – relied on travelers, and government revenues were estimated at approximately \$79 million, with a 60/40 split between state and local governments.

Benefits of Tourism to Santa Barbara County, 2002-2007

	2002	2004	2006	2007
Total Travel Spending (\$ millions)	1,170	1,272	1,429	1,409
Accommodation	260	281	335	343
Food/Beverage	313	344	380	370
Food Stores	37	40	42	41
Ground Tran./Motor Fuel	84	119	158	169
Arts/Entert't/Rec.	184	196	206	195
Retail	287	290	303	285
Employment Generated ¹ (Thsd. Jobs)	15	16	17	16
Accommodation/Food Svc	10	10	11	10
Arts/Entert't/Rec.	4	4	4	4
Retail ²	2	2	2	2
Tax Receipts Generated (\$ millions)	79	87	98	97
Local Tax Receipts	32	36	41	42
State Tax Receipts	47	51	57	56

¹ May not add due to rounding.

² Retail employment includes gas stations.

Source: Dean Runyan Associates, 2009

Last year's weak dollar did not create enough of an incentive for foreign travel to compensate for tourism declines associated with the recession. In the county overall, the hotel occupancy rate declined 6.1%, from the 72.3% average in 2008 to 67.9% in 2009. As a result of declining demand, hotels were forced to reduce their rates by 7.7%, from an average \$162 per room per night, to \$150.

Some members of the local tourist industry believe a paradigmatic shift to be underway, as visitors both for business and pleasure now avoid luxury rooms with expensive nightly rates. Accordingly, the greatest decline in room rates occurred in the Montecito area, where a room that cost \$273 per night in 2008 was cut back 12.7% to \$238 in 2009. The prime location of the "Town" area (the downtown Santa Barbara city submarket) likely saved hotels from a similar cutback, as occupancy rates (and, to a lesser degree, room rates) declined substantially in the less-popular Carpinteria and Lompoc/Santa Maria areas.

Nevertheless, a rebound is in sight. Despite a rough year for the local travel industry, December's figures

Tourism Indicators, Annual Average 2008 & 2009

Location	Average Daily Rate (\$)			Occupancy Rate (%)		
	2009	2008	Chg (%)	2009	2008	Chg
South County						
Santa Barbara/Montecito	238	273	-12.7	70.1	74.5	-5.9
Town	151	157	-4.0	67.9	73.3	-7.3
Carpinteria	76	77	-2.2	66.2	72.5	-8.7
Goleta	128	137	-6.9	73.1	75.1	-2.8
North County						
Solvang/Santa Ynez	112	116	-4.0	73.1	74.5	-1.9
Lompoc/Santa Maria	93	94	-0.4	58.6	64.8	-9.7
Overall Average	150	162	-7.7	67.9	72.3	-6.1

Note: Calculations for percent change reflect pre-rounded numbers.

Source: PKF Consulting, 2009

were much more positive relative to the same month the year prior. While both occupancy rates and room prices were significantly lower across the board relative to the yearly average, the rate of decline appeared to be slowing. The Montecito area continued to be

Some members of the local tourist industry believe a paradigmatic shift to be underway, as visitors both for business and pleasure now avoid luxury rooms with expensive nightly rates.

the most expensive submarket, but the average cost of a room was \$200 – only 1.4% below the rate for December 2008. Some areas attempted a raise in daily room rates, including Santa Barbara's downtown area, Solvang/Santa Ynez, and Lompoc/Santa Maria. These may have been overly ambitious attempts to capture holiday revenues, as occupancy rates had not yet revived, except for Solvang/Santa Ynez, which saw mild growth.

Tourism Indicators, Dec. 2008 & Dec. 2009

Location	Average Daily Rate (\$)			Occupancy Rate (%)		
	2009	2008	Chg (%)	2009	2008	Chg
South County						
Santa Barbara/Montecito	200	202	-1.4	50.8	53.3	-4.6
Town	134	132	1.4	51.4	54.7	-6.1
Carpinteria	60	60	-0.8	52.9	54.5	-3.0
Goleta	107	108	-1.5	56.0	55.4	1.0
North County						
Solvang/Santa Ynez	98	97	1.4	62.7	62.2	0.7
Lompoc/Santa Maria	89	86	3.1	45.2	47.0	-3.8
Overall Average	127	128	-0.5	51.9	53.5	-3.0

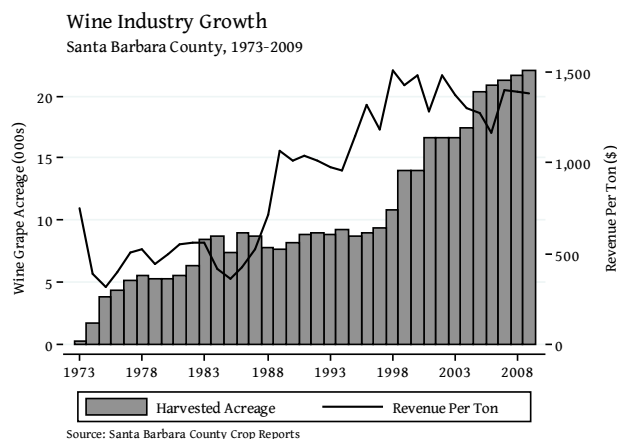
Note: Calculations for percent change reflect pre-rounded numbers.

Source: PKF Consulting, 2009

North County Vineyards

A prominent feature of Santa Barbara's attractiveness to tourists is its growing acclaim as a wine region. While its success became popularized by the 2004 film *Sideways*, the viticultural side of the county's economy dates back to the Mission era. Since its resurgence in the 1960s, the industry has grown to comprise over 100 wineries. Drawing upon the combination of ocean air, warm climate, and complex soil, several wineries have managed to establish themselves on the world stage, and a regionalization has emerged within the northern area of the county.

The Santa Maria Valley American Viticultural Area (AVA) has become known for chardonnays and pinot noirs, while the Santa Ynez AVA specializes in cabernet, merlot, and several Rhone varietals. Meanwhile, the younger Happy Canyon AVA is becoming known for its Bordeaux, and the Santa Rita Hills AVA has won awards for its chardonnays and pinot noirs.¹²



Taken together, these regions have grown impressively over the last 35 years. As the quality of the county's grapes have gained a reputation, their value has climbed at a year-over-year average rate of 3.4%, reaching \$1,385 per ton in 2009, although the highest prices per ton were seen during the years leading up to

the dot-com bust, peaking at \$1,510 per ton in 1998.¹³ As demand increased for the grapes, farmers began converting more cropland to viticulture, and harvest yields increased. Since 1973, farmers have converted an average 607 acres per year to vineyards, reaching 22,050 acres in 2009.

Accordingly, the number of tons of grapes harvested per acre fell noticeably, from 6 tons to 3 tons.

While the number of acres devoted to wine grapes has increased relatively steadily, yields have not necessarily been as consistent. The strong growth rate from 1995 to 2005 slowed thereafter, contracting 20.9% between 2005 and 2008. Accordingly, the number of tons of grapes harvested per acre fell noticeably, from 6 tons to 3 tons. Some of this dramatic decline in value resulted from the series of wildfires that ravaged Santa Barbara County around this time. 2009, on the other hand, was a stellar year for wine grape production in terms of overall value: the amount of grapes harvested increased by more than 50% and total value grew by almost 60% over 2008, while output per acre increased to 4.5 tons, but the value per ton actually fell slightly for the second year in a row.

Wine Performance Indicators Santa Barbara County

	1995	2000	2005	2009
Tons Harvested	17,462	60,769	125,503	99,225
Harvested Acreage	8,731	14,002	20,308	22,050
Tons per Acre	2	4	6	4
Total Revenue (\$ Mill)	20	90	160	137
Revenue per Ton (\$)	1,153	1,482	1,278	1,385

Source: Santa Barbara County Crop Reports

This drop in yields cut the industry's revenue from \$160 million in 2005 to \$137 million in 2009, although it was even lower in intervening years. So long as the growth in planted area and harvested output continues to outpace the gentle declines in value per

¹²Source: Santa Barbara County Vintners' Association.

¹³Santa Barbara County Crop Reports.

ton, Santa Barbara County's grape growers will generate increasingly large revenues. As this trend continues, Santa Barbara's wineries will benefit greatly from higher-yield seasons, their success providing an ever-greater draw for tourism in the county.

Conclusion

A challenging feature of economic forecasting is the time lag among indicators upon which we rely for estimating current and future trends. Given what is available, it is easy to see the impact of the recession on business activity within the county. GDP contracted almost 1% between 2007 and 2008, owners of businesses began to view the future with growing pessimism, consumer spending declined around the county, and hotels (among other establishments) suffered from a drop in tourism.

But it is telling that the more current indicators point to a resurgence in commerce. Federal attempts to stabilize the economy, through the "cash for clunkers" program and the first-time homebuyers tax credit, clearly revived consumer activity in the third quarter of last year. Accordingly, optimism at long last gained the upper hand among local business leaders, and tourism slowed its decline. Looking forward, Santa Barbara has much to offer as a business center. Its climate alone will attract the talented and independent, while its varied industrial base provides a fertile ground for future growth.

North County

According to the two indicators which can be used to differentiate business dynamics in northern and southern Santa Barbara, namely consumption and tourism, the north appears to have been harder hit. Between 2007 and 2008, retail sales declined almost twice as dramatically, as consumers responded to recessionary forces. In particular, a \$3 million drop in

apparel purchases, combined with \$47 million and \$98 million reductions in general merchandise and motor vehicles, respectively, have impacted the local economy. Some of this can be attributed to the contraction in tourism.

Nevertheless, when the data becomes available, we're likely to see a rebound in consumption midway through 2009, as the federal stimulus packages came into effect. Simultaneously, a growing appetite among travelers for cheaper hotel rooms (among visitors traveling for both business and pleasure) will be met by accommodation options in the North County. Occupancy rates in the Solvang/Santa Ynez area have been as high or higher than elsewhere in the county, and showed positive growth in December 2009 over December 2008. Perhaps it's the wine.

South County

The wealthier south has also been affected by the recession, albeit to a lesser degree. Consumption retracted 5.4% in the form of retail sales, resulting primarily from declining sales in general merchandise, home furnishings, building materials, and motor vehicles. Relative to the north, sales of apparel performed much better, and many of the areas of loss were not as extreme.

These issues are also likely to have been assuaged by the federal stimulus. Sales of vehicles in particular have been helped by stimulus programs. Tourism is also returning to the South County; its traditionally more expensive room rates have been forcibly reduced by a decline in local travel, as demand for rooms dropped between 2008 and 2009.

Agriculture

by Alexander Lin Beale

Beacon Economics

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Key Chapter Findings

- Farms in Santa Barbara County have been getting smaller and more productive, generating an estimated \$1.24 billion in total output in 2009. As one of the few billion dollar industries in the County, agriculture plays a central role in the local economy.
- The top crop items are strawberries, broccoli, and wine grapes, which together contributed more than 50% of total agricultural value in 2009.
- Agriculture was one of the best-performing sectors over the course of the recession; employment dipped briefly in early 2009, but has been growing very rapidly over the past nine months.

Agriculture is a major contributor to economic output in Santa Barbara County, being among the few billion-dollar industries in the County. Farm production generates around 5% of the County's gross annual output, and the County's farms provide almost 10% of jobs in the County. Although its agricultural output is impressive, Santa Barbara County ranks only 14th in California by value of total agricultural production (24th nationwide), but it is the eighth-largest producer of crops in the state (9th nationwide), highlighting the County's importance primarily as a producer of crops.

Notably, Santa Barbara County is among the nation's top producers of broccoli and cauliflower by production area. The County is also home to a booming wine industry, noted for producing some of the most valuable wine grapes in California; however, due to the wine industry's overlap with tourism, it is treated in more detail in the business activity chapter of this book. The most important crop for Santa Barbara's agricultural sector is strawberries; with more than \$340 million in gross output in 2009, strawberry farms contributed close to 28% of total agricultural value in the County.

Agriculture is heavily concentrated in the northern portion of the County; approximately 85% of agricultural employment is in areas north of the Santa Ynez Mountains, although there are significant farming operations in the area surrounding Carpinteria, in the southeast corner of the County. The wineries

and vineyards that constitute Santa Barbara's well-known wine industry are all located in the northern area of the County, as are most of the high-value crops, including strawberries, broccoli, cauliflower, and lettuce.

The region's farms generated an estimated \$1.24 billion in agricultural value in 2009; however, the sector consumes relatively little land, compared to other counties whose farm output exceeds \$1 billion annually, owing to the marginal importance of livestock farming. On the other hand, as a share of the County's total land, farming consumes a tremendous amount of space. As of 2007, 41.5% of the County's land was dedicated to agricultural use, down from slightly over 43% five years earlier.

Farms

Farms in Santa Barbara County tend to be somewhat larger, but on average they are less productive than farms statewide. The average farm in the area is roughly 45% larger than the average California farm, but generates only 42.5% more output. Although average per farm production is almost \$178,000 more per year, output per acre is slightly lower in Santa Barbara County, at \$1,309 compared to \$1,336 across California.

Santa Barbara County Farms, 1992 to 2007

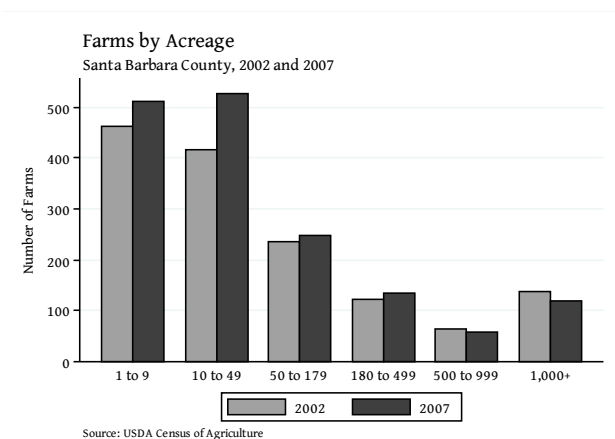
	1992	1997	2002	2007
Number of Farms	1,613	1,771	1,444	1,597
Land in Farms (Acres)	836,989	835,271	756,937	727,050
Average Size of Farm (Acres)	519	472	524	455
Market Value of Products Sold (\$000s)	391,022	668,530	717,257	951,326
Average Per Farm Reporting Sales (\$)	242,419	377,487	496,715	595,696
Real Average Per Farm Reporting Sales (2007 \$)	358,258	487,657	572,484	595,696
Government Payments (\$000s)	N/A	334	538	132
Average Per Farm Receiving Payments (\$)	N/A	5,760	11,209	8,226
Real Average Per Farm Receiving Payments (2007 \$)	N/A	7,441	12,919	8,226

Note: Data on government subsidies are not available prior to 1997.

Source: USDA Census of Agriculture

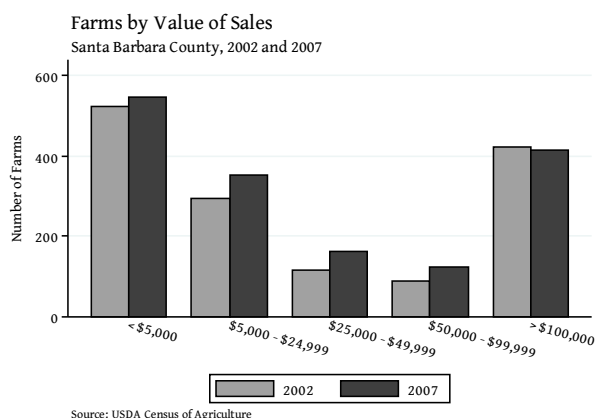
Between 2002 and 2007, farms in the county became significantly smaller, yet more productive, a trend that is reflected across the state. However, the average farm size has fluctuated over the past four agricultural censuses, whereas it has been declining consistently in most parts of the state. The 2007 census saw a 3.9% decline in the overall area dedicated to farming. Simultaneously, the number of farms grew by 10.6%, to 1,597, reducing the average farm's acreage by 13.2%, to 455 acres. Nonetheless, the vast majority of farms continue to be between 1 acre and 49 acres in size, and the median is just 20 acres. The county has seen a shift from larger farms, with more than 500 acres, to small farms, coupled with an increase in the number of smallest farms. This decline in farm size can be attributed to several factors, including ongoing water conservation measures, a shrinking livestock farming sector, the sale of agricultural lands closest to cities for development, and an increased focus on small-scale and sustainable farming. Additionally, many of the smaller farms that have sprung up recently are very small, high-end vineyards.

The County has seen a shift from larger farms, with more than 500 acres, to small farms, coupled with an increase in the number of smallest farms.



Meanwhile, the market value of products sold increased 32.6% from 2002 to 2007, or 19.9% on an average per farm basis. In real terms, average per farm sales only increased by 4.1%, which, nonetheless, indicates an increase in productivity. In particular, as the total amount of land committed to agricultural ventures has declined, this growth points to more efficient and profitable land use. As of 2007, the average revenue per farm stood at \$595,696, while the average expense of maintaining a farm was \$495,024. Note that almost 75% of farms in the County produced less than \$100,000 in output, so the average is severely skewed by the few multi-million dollar farms. Average government receipts declined 26.6% from \$11,209 to \$8,226 per farm receiving payments, although in real terms they actually declined by 36.3%. Additionally, the number of farms receiving financial assistance fell

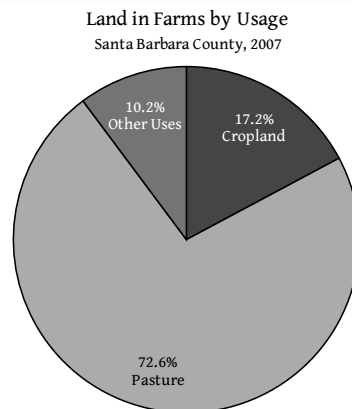
dramatically, from 48 in 2002 to 16 in 2007, bringing total government payments in the county down 75.5%, from \$538,000 to \$132,000.



Production and Output

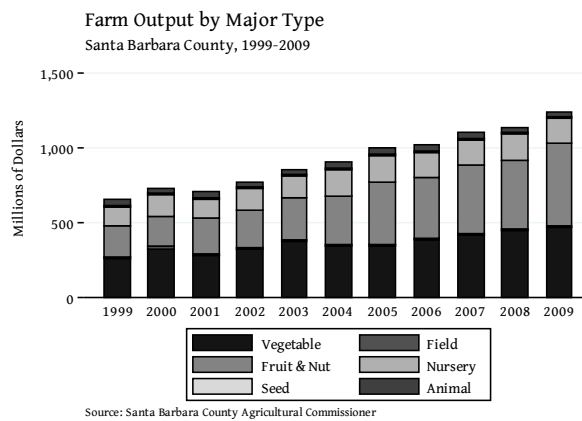
The distribution of land by usage bears little relation to the distribution of sales by commodity, as output per acre differs widely between products. Pastures consume an inordinate amount of land, 72.6% of overall agricultural area, relative to the additional value generated by grazing livestock, which is around 3% of total agricultural output. Among crops, which consume the second-largest share of land, at 17.2%, there are still significant differences in output per area. In 2008, an acre planted with strawberries generated roughly \$43,000 in output, while an acre of broccoli produced just \$5,700, and a 1-acre vineyard returned only \$4,000. The remaining 10.2% of agricultural lands are dedicated to other uses, including housing and storage facilities.

Lemons, the historically most important crop, have become less predominant.



Source: USDA Census of Agriculture

Santa Barbara's top ten crops have remained fairly constant for many years, although 2009 did see some significant changes. Notably, cattle and calves did not fall within the top ten products for the first time, while two varieties of cut flowers, lilies and gerbera daisies, are now among the top ten crops. Strawberries, broccoli, and wine grapes continue to be very important. Lemons, the historically most important crop, have become less predominant. 2009 was a mixed year for agriculture. Vegetable crops fared poorly, with declines in value and harvested acreage in all of the County's major vegetable crops. The County's major fruit crops on the other hand, had a stellar year; strawberries, wine grapes, and avocados all saw huge increases in total value. Santa Barbara County is not the top producer of any of its major crops, although it is the nation's second-largest grower of broccoli and cauliflower by production area.



Santa Barbara County's Top Ten Crops, 2006 - 2009

Crop	Value of Production (\$000s)				Harvested Acreage			
	2006	2007	2008	2009	2006	2007	2008	2009
Strawberries	231,392	312,755	309,278	344,614	6,210	6,414	7,193	7,550
Broccoli	128,873	131,070	159,818	149,895	28,250	28,376	27,954	26,293
Wine Grapes	107,378	99,919	86,148	137,427	20,829	21,263	21,643	22,050
Cauliflower	37,415	46,107	47,377	63,217	8,621	8,659	8,452	7,819
Head Lettuce	66,950	87,846	83,006	62,050	13,021	12,835	12,462	10,215
Avocados	40,288	20,812	37,714	47,129	8,607	8,328	8,148	7,520
Celery	41,691	39,686	41,189	40,861	3,654	3,726	3,646	3,588
Leaf Lettuce	26,852	25,705	29,465	28,688	4,103	4,252	4,235	4,074
Gerbera (Cut)	18,168	23,565	22,195	25,912	N/A	N/A	N/A	N/A
Lily (Cut)	18,911	15,260	19,878	22,493	N/A	N/A	19	24
Total	1,016,735	1,103,322	1,137,350	1,241,401	722,601	721,105	716,121	710,820

Note: Total harvested acreage includes land used for pasture.

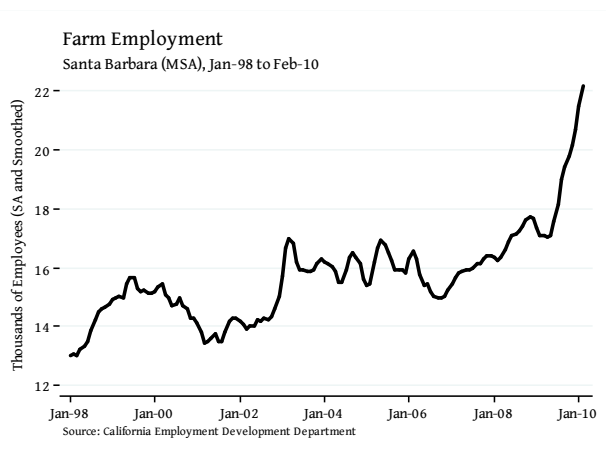
Source: Santa Barbara County Agricultural Commissioner

Local farm production breaks out into six major categories: animal products (which include livestock, poultry, and apiary products), fruit and nut crops, vegetable crops, nursery products, seed products, and field products (which encompass grains and lands used for pasture). The bulk of agricultural value comes from vegetable production, and fruit and nut production, each accounting for roughly 40% of Santa Barbara County's annual agricultural output. The vegetable crop's share of output has remained fairly constant in the past 10 years, while fruit and nut production has gained in importance, growing from around 30% of annual output in 1999. The next-largest contributor to farm production is nursery crops, primarily cut flowers, which constitutes close to 16% of the sector's output. Nursery products play a much more substantial role in Santa Barbara than they do in other agricultural counties, but they appear to be declining in importance, as their share of output has fallen from just under 20% to 15.5% in the past decade. Likewise, animal products are becoming a smaller component of the County's agricultural mix, having fallen from over 6% of county agricultural production to around 3% in recent years. Field and seed products each contribute roughly 1% of annual farm output.

Employment

Overall, agricultural employment in Santa Barbara County has been growing steadily over the past 20 years, although there is considerable short-term fluctuation, which is typically the result of variations in growing conditions from year to year. While it appears as though there is a significant bubble in farm employment during the IT bubble, the peak of this bubble actually corresponds to employment levels and growth observed throughout the 1990s and reflects a return to normal trends from a dip in employment that occurred in early 1998. In the last decade, the agricultural sector has added over 2,500 jobs, representing a greater than 17% increase in farm employment. In real terms, the County's agricultural output has increased significantly more than employment, indicating that efficiency and output per worker have been improving in the farming sector.

Agricultural employment is only moderately influenced by economic cycles; other factors, such as weather and transportation costs, have a much more direct and noticeable effect.



The current recession does not appear to have had a significant impact on agricultural employment in the

region. Although employment at farms fell slightly through the last quarter of 2008 and the first quarter of 2009, the number of jobs lost did not exceed historical fluctuations. Employment in the agricultural sector has been growing at an astonishing rate since May of 2009, and is currently at a record high level, having added over 5,000 jobs in the past nine months. Given these trends, it seems highly unlikely that the sector will sustain major declines as the economy heads into recovery. Ultimately, agricultural employment is only moderately influenced by economic cycles; other factors, such as weather and transportation costs, have a much more direct and noticeable effect.

Santa Barbara County Wine Industry

by Matt Turrentine, Broker
Turrentine Brokerage

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Key Chapter Findings

- The wine business in Santa Barbara County has grown in prestige and in volume over the past 25 years. The 17,000 acres under vine has tripled from just over 5,000 acres in 1985 and now accounts for 7% of the coastal acreage in the State.
- Santa Barbara County grapes have commanded some of the highest prices in the State, especially for Pinot Noir and Chardonnay.
- While the total volume of wine sold in the United States has grown slowly during the recession, there has been strong downward pressure on prices as consumers move to less expensive wine.
- Chardonnay, the variety with the largest acreage in Santa Barbara County, is also the variety with the largest current excess, putting pressure on grape and bulk wine pricing.
- There are a couple of challenging years ahead as the economy recovers, but the future looks bright. Wine sales continue to grow and no increase in production is expected, except for Pinot Noir.

Wine in Santa Barbara County

The wine industry has grown rapidly in prestige and in volume in Santa Barbara County over the past 25 years, with vineyard acreage tripling to over 17,000 acres today from just over 5,000 acres in 1985. The number of local wineries has grown from just a handful to over 100. The first commercial vineyards were planted in Santa Barbara County in early 1970s, and the County has seen acreage growth ever since, although faster at certain times than at others.

Wine Demand and the Supply Cycle

The California wine industry has experienced dramatic supply cycles during the past 40 years. Wine sales have steadily grown over that period. When supply is tight, spot market prices quickly rise and the

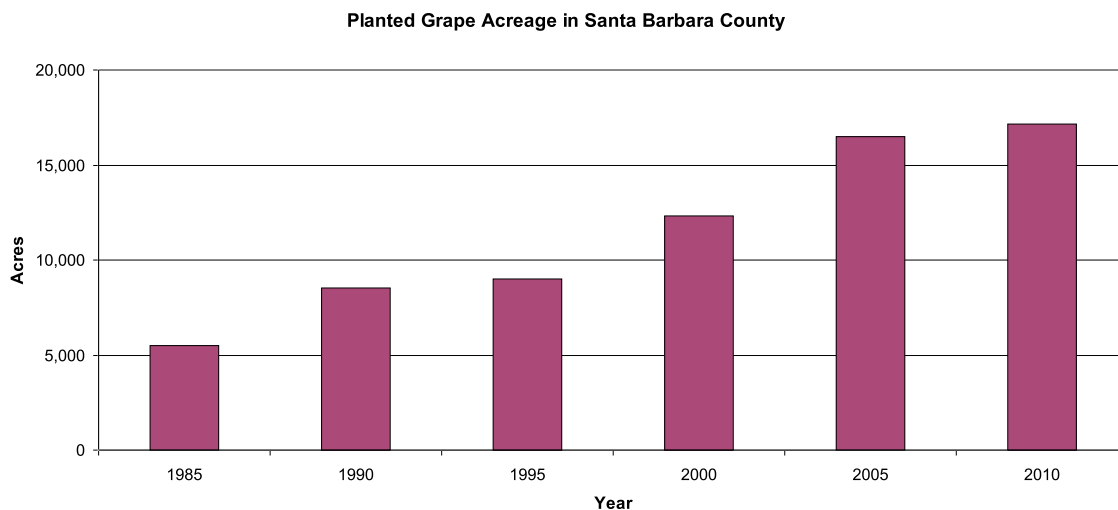
high margins attract significant new capital to the industry.

That capital goes into new vineyard plantings to provide the needed supply. But it takes a new vineyard roughly four years to reach commercial production. So even after enough new acres may have been planted to satisfy demand, the production has not yet been realized. Prices can remain high and this continues to stimulate planting over and above the true long-term demand.

...capital goes into new vineyard plantings to provide the needed supply. But it takes a new vineyard roughly four years to reach commercial production.

Eventually all those new acres come into production and the industry is flooded with far more supply than is needed. With the flood of supply, prices collapse and margins disappear. Wineries' marketing teams launch new brands and find creative ways to move wine. After a few years, sales reach a level sufficient to utilize all

The number of local wineries has grown from just a handful to over 100.



Source: CA Grape Acreage Report

the existing acres, supply becomes tight and the cycle begins again.

The full supply cycle lasts from 8 to 14 years.

Supply Cycle and the Recession

The most recent period of extreme shortage was in the late 1990's. This was a booming period of growth for all of California, including Santa Barbara County. Prices were high and many new acres were planted.

In 2000, as many of those new acres came into production, the industry moved into a protracted period of extreme excess supply. There were five very chal-

In 2000, as many of those new acres came into production, the industry moved into a protracted period of extreme excess supply.

lenging years, characterized by huge excess supplies of grapes and bulk wine. Prices were very low and many grapes were left un-harvested in the vineyards. Wineries were forced to discount their wines severely to move inventory.

Early in 2005, the large excesses of the previous few years were returning to manageable levels. Continuing growth in wine consumption had whittled the excess away. The Santa Barbara-based movie, *Sideways*, had been nominated for an Academy Award. Demand for Pinot Noir was strong. Prices were on the rise for most varieties and some wineries began offering multi-year contracts for grapes. However, this strength in the marketplace was short-lived. The 2005 crop was by far the biggest in history, both statewide and in Santa Barbara County. Wineries were overwhelmed and the industry plunged back into an excess position.

...the first quarter of 2008... just as harvest was getting underway, the financial markets collapsed and a global recession began.

While two smaller harvests followed the monster 2005 harvest, the grape and bulk wine markets remained depressed in Santa Barbara County. Pinot Noir was the exception. With sustained sales growth of over 20% on an ever growing base, Pinot Noir prices were astronomically high for both grapes and wine. As prices increased, many wineries, desperate for supply, offered planting and grafting contracts in Santa Bar-

bara County. Some growers planted Pinot Noir speculatively without a contract.

By the first quarter of 2008, the market had largely returned to balance, again poised to enter a period of shortage. Prices were moving upwards. Then, just as harvest was getting underway, the financial markets collapsed and a global recession began to set in. The effects of the recession were buffered for the wine business by a light harvest in 2008. By February of 2009, however, restaurant sales had contracted, wholesalers were whittling down their inventories and consumers were trading down for many of their wine purchases.

Current Status

Impact of the Recession

Compared with many other industries, the Wine business has been quite resilient in the face of the recession. Overall wine sales have grown although consumers have traded down to less expensive bottles. This has created a profound dichotomy in the indus-

Compared with many other industries, the Wine business has been quite resilient in the face of the recession.

try. Wineries and regions primarily like Santa Barbara County which sells wine over \$20 a bottle have seen sales drop off, while wineries and regions that primarily sell wine for less than \$10 a bottle have been thriving.

Key Variety #1: Chardonnay

Chardonnay is by far the most widely planted variety in Santa Barbara County. With approximately 7,000 acres in the ground, Chardonnay accounts for 40% of

the vineyard acres in the County. Currently, the market for Chardonnay grapes and bulk wine is challenging, with more supply available than demand. Like

Chardonnay accounts for 40% of the vineyard acres in the County. Currently, the market for Chardonnay grapes and bulk wine is challenging, with more supply available than demand.

most varieties, there is more demand for less expensive grapes and wine destined for bottles priced below \$10, where recession-weary consumers are buying. However, Santa Barbara County is an expensive place to grow grapes, and yields per acre are smaller on average than Monterey County or the Interior Valleys of California. To be profitable for both growers and wineries, Santa Barbara Chardonnay grapes typically need to be going into \$12-\$25 bottles of wine.

Key Variety #2: Pinot Noir

. Santa Barbara County was a beneficiary of the explosion in demand for Pinot Noir over the past six years. In many ways, the Pinot Noir boom began in Santa Barbara County with the film *Sideways* in 2005. This surprise hit extolled the virtues of wines made from the Santa Barbara County Pinot Noir grapes, and sales have been growing rapidly ever since—although the recession has dampened demand at higher price points.

With 4,200 acres planted, Pinot Noir is the second largest variety grown in Santa Barbara County, representing almost 25% of the county's vineyard acreage.

Pinot Noir is the second largest variety grown in Santa Barbara County, representing almost 25% of the county's vineyard acreage.

Even when the recession ends, it may take some time for recovery at these high price points, and we may have more expensive Santa Barbara County Pinot Noir grapes and wine than we need for an extended period.

Currently there is still strong demand for Pinot Noir, however, much of that demand is at unsustainably low price points. Pinot Noir is a challenging variety to grow and is notoriously fickle and low yielding.

Over the next few years, as the recession ends and consumers trade up again to more expensive wines, prices should return to sustainable levels for Pinot Noir in Santa Barbara County. However, many of the recently planted acres of Pinot Noir were destined for new brands, in most cases priced above \$30 a bottle. Many of these new brands were planning to sell a high percentage of their wine at restaurants, and they were consequently hit harder by the recession. Even when the recession ends, it may take some time for recovery at these high price points, and we may have more expensive Santa Barbara County Pinot Noir grapes and wine than we need for an extended period.

Other Varieties

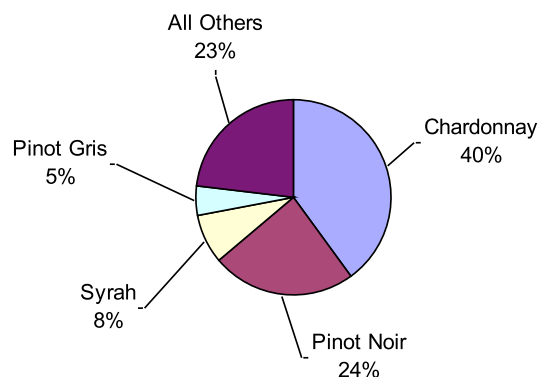
Chardonnay and Pinot Noir dominate the acreage in Santa Barbara County, however many other varieties are also grown.

Syrah is the third largest variety, accounting for 8% of the County's acres. While many of the best Syrahs in the state come from Santa Barbara and receive high scores from famous critics, Syrah has not become a major variety in California. There is only limited de-

Syrah has not become a major variety in California. There is only limited demand for high quality Syrah grapes and wine...

mand for high quality Syrah grapes and wine at this time.

Planted Acres by Variety in Santa Barbara County



Source: CA Grape Acreage Report

No other variety amounts to more than 5% of the total vineyard acres, with Pinot Gris at 5%, Cabernet Sauvignon and Merlot both at about 4% and Sauvignon Blanc at 3%.

The Future

There are a couple of challenging years ahead as we ride out this recession and wait for the anticipated resurgence in demand for more expensive wine. An additional challenge is that a significant volume of grapes from Santa Barbara County go into wines carrying a broader appellation, such as Central Coast or California.

There are not enough brands that use the Santa Barbara County appellation to utilize all the grapes grown in the County. Those wines with broader appellations generally sell at a lower price point. Santa Barbara County needs more brands to use the Santa Barbara

County appellation, to both promote the area and support a price structure that can sustain the cost of growing grapes in Santa Barbara County.

Santa Barbara County needs more brands to use the Santa Barbara County appellation, to both promote the area and support a price structure that can sustain the cost of growing grapes in Santa Barbara County.

Despite the challenges, the long-term future looks bright in Santa Barbara County. Wine sales continue to grow and no increase in production is expected, except for Pinot Noir.

Americans' increasing interest in the quality and wholesomeness of their food seems to be a strong trend that bodes well for wine consumption. Some studies indicate high-end wine consumers have continued to occasionally purchase high-end wines during the recession, even while trading down for most of their wine purchases. This supports the expectation that in the future consumers will return to higher-priced wines. Even cautious consumers may consider super-premium wines to be an affordable luxury that serves as a reward on special occasions.

These strong consumer trends bode well for the future of the Santa Barbara County wine industry. In addition, research continues to demonstrate the health benefits of moderate wine consumption. And perhaps most encouraging, the Millennial Generation, aged 21-32, is adopting wine as their beverage of choice and have entered the market at higher price points than any other generation.

Residential Real Estate

by Patrick S. Duffy

MetroIntelligence Real Estate Advisors

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Key Chapter Findings

- After nearly quadrupling between 1998 and 2006, the sharp decline in Santa Barbara County home prices has sent affordability levels soaring from just 4% five years ago to 47% by the fourth quarter of 2009.
- As a relatively minor market for home builders, new home sales in the county typically range from 200 to 250 units per year. Due to these limited sales, the median price can vary greatly, and currently stands at \$366,639, or at levels last seen in the first quarter of 2004.
- Due to price declines of 31% over the past two years to nearly \$330,000, sales of existing homes—of which about one-third are foreclosures—rose by 58% to nearly 780 homes, although a worsening economy meant that sales fell by 1.6% over the last quarter.
- Due to price declines of 16% over the past two years to just over \$385,000, sales of existing condominiums rose by 64% during the same time period. Over the past year, however, both condominium prices and sales have rebounded by about 20%.
- Landlords of larger apartment properties have reacted swiftly to a changing market, offering various incentives to keep countywide occupancy levels over 94%. Even with these incentives, however, asking rents have fallen by 3.2% to \$1,223 per month and are down even further for studios, one-bedroom flats and smaller two-bedroom flats.
- Even with political pressure and various moratoria attempting to keep the lid on distressed sales, nearly one-third of home sales during January of 2010 were for foreclosed homes, with the total pace up by 36% between the third and fourth quarters of 2009.
- Owing to the housing downturn, building permit activity is a fraction of what it was in previous years, totaling just 262 units in 2009. Yet as the market eventually heals itself, residential permits are forecast to gradually build back up to 800 homes by the end of 2015.

Santa Barbara County Overview

As one of the country's most desirable places to live, Santa Barbara County is also home to some of the priciest real estate. But since this is really a story of two separate regions in terms—of not just geography but also of the demographics, politics and economics of the coastal region to the south and the inland area to the north—any analysis on the residential real estate market must also discuss, whenever possible, North County and South County as separate entities. Following this overview of the entire county, following sections will separately review ongoing res-

idential real estate trends for the North and South County.

Because California—and therefore Santa Barbara County—was front and center during the housing boom, both the state and the region were also hit disproportionately hard by the correction which followed. The good news is that the correction in home prices has occurred faster and more steeply than witnessed in previous downturns, which should help bring prices back into balance with household incomes and potential rental rates sooner rather than later, thereby setting the stage for future growth.

Fortunately, Santa Barbara County's affordability index, as measured by the NAHB/Wells Fargo Opportunity Index, reached 47% by the fourth quarter of 2009. While that rate is lower than the recent peak of 62% during the first quarter of 2009, it's still exponentially higher than the 3% to 4% rate noted for most of 2005 and the first quarter of 2006. This means that at current household incomes, 47% of the county's households can afford a median-priced home at prevailing interest rates.

From an historical perspective, the earlier increase in home values throughout the region, state, and nation reduced home affordability to levels never seen before. After remaining flat throughout much of the 1990s in both the state and Santa Barbara County, the S&P/Case-Shiller Home Price Index—which compares the sales prices of the same homes over time—began to rise in Santa Barbara County, first gradually and then exponentially. Between the first quarter of 1998 and the first quarter of 2003 the index doubled. By the third quarter of 2004 it had more than tripled. And by the first quarter of 2006 it had nearly quadrupled.

When the housing bubble finally did pop in Santa Barbara County in the middle of 2006, at first the decline in the index was small, falling by just 4% over the next year. By the end of 2007, however, the pricing decline began to gain momentum, with the index falling by 29% between the second quarters of 2007 and 2008. During that same time period, median prices for the state and for the 20 markets surveyed throughout the nation by the index fell by 30% and 15%, respectively.

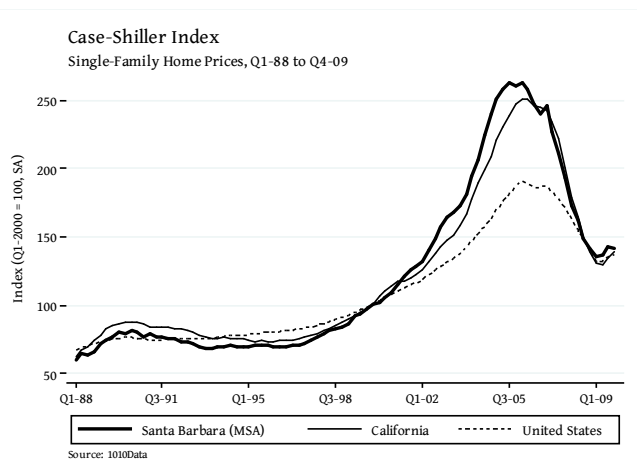
More recently, it seems as if median prices for Santa Barbara County hit bottom in the first quarter of 2009 and closely approximated levels last seen in the middle of 2002, although we could see a second decline as interest rates rise and as the federal government removes its support for the housing sector. In fact, although prices in the county did rise again between the second and third quarters of 2009, the size of the increase—an anemic 4%—demonstrates that the hous-

ing rebound is quite fragile. As proof of this, during the same time period the index rose by 3.4% throughout California and by a lackluster 1.8% for the entire United States.

Moreover, prices for mid- and high-priced homes could continue to face pricing declines because, according to the index, these prices did not decline as much as those of homes in the entry-level sector. Although pricing by various tiers is not available for Santa Barbara County, reviewing tiered prices from the S&P/Case-Shiller Index for the entire Los Angeles metro area can still be instructive. Between December of 2007 and 2009, prices for entry-level homes priced under \$300,990 in the overall Los Angeles metro area fell by 42%, compared to a decline of just 24% for mid-level homes (those priced from \$300,990 to \$509,366) and 19% for the higher-priced homes (those priced over \$509,366). Since the pricing peak in 2006, prices for entry-level homes fell by 53%, compared to 37% for mid-level homes and just 25% for higher-priced homes.

Eventually, homes in the mid- and high-priced tiers—especially those originally reliant on jumbo or option adjustable-rate mortgages—could see the same types of price declines already noted for the entry-level tier. Because the housing market typically provides a financial “ladder” for most homebuyers—that is starter condo to townhome to small single-family home to larger single-family home to luxury condo—without sufficient equity to purchase mid-level homes, entry-level buyers who can afford their mortgages often have little choice but to remain in place. Consequently, in order to sell their homes, owners of mid-level units may eventually have to capitulate on price. Similar trends could also affect the highest pricing tier, although that segment also captures buyers with greater resources who bring in equity based not just on previous home sales but also on prior gains from stocks, bonds, and other investments.

For now, however, the specter of further price declines has been avoided, as the S&P/Case-Shiller Index for the Los Angeles metro area actually rose by 4.6% overall (and from 1.3% to 8.2% for each pricing tier) between July and December of 2009, as bargain hunters have taken advantage of sharply lower prices, thus providing a floor—which could be temporary—to housing prices.

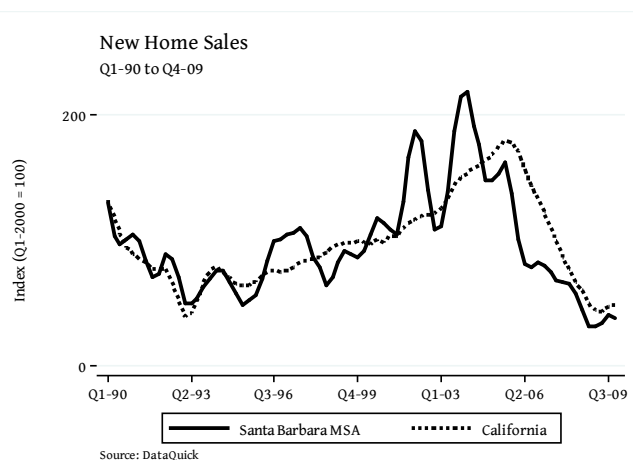


New Home Sales

Because of various growth initiatives long in effect throughout southern Santa Barbara County, the level of new home sales in the area tends to ebb and flow based on the availability of permits rather than on market demand. Notably, the entire Central Coast of California is also generally too small of a market to interest larger, nationally known developers, so it tends to be dominated by custom builders who create the occasional production home project, as well as by smaller regional players who have long focused on the region.

After last peaking at over 300 seasonally adjusted units in the fourth quarter of 2003, new home sales struggled to stay above 200 units per quarter through the end of 2005. Since then, quarterly sales have largely been on a descending path, falling below 100 sales per quarter by the middle of 2006 even as the

national boom in new housing was reaching its apex. Although it does appear that new home sales in this county bottomed out at just 22 homes in the first quarter of 2009, it's still too early to label the doubling of that level over the next year as an ongoing trend. In fact, quarterly sales in the fourth quarter of 2009 were still down by 44% from the same period of 2008. For now, it appears that the county can absorb just 50 to 60 new homes per quarter, or up to about 250 units per year.



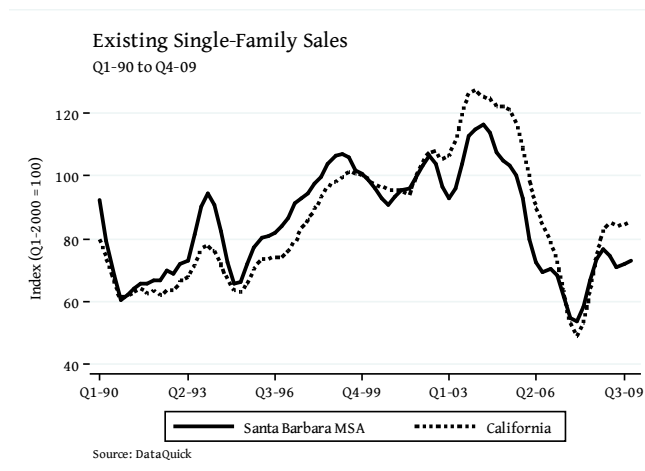
Owing to the combination of the national housing boom and the county growth restrictions, seasonally adjusted new home prices did gradually rise to eclipse \$600,000 by the first quarter of 2006, but subsequently ranged mostly from \$470,000 to \$570,000 through the end of 2007. It wasn't until the beginning of 2008 that new home prices remained below the \$500,000 level, predominantly continuing to fall over the next two years. By the fourth quarter of 2009, the median price for a new home in Santa Barbara County had fallen to \$366,639, down by 30% over the previous two years but still up by nearly 5% over the past year. More recently, however, new home prices fell by 17% between the third and fourth quarters of 2009, approaching levels last seen in the first quarter of 2004.

Existing Single-Family Home Sales

After peaking at 1,190 units in the first quarter of 2004, seasonally adjusted sales of single-family homes in Santa Barbara County continued to slowly decline to about 1,000 units through the third quarter of 2005. Quarterly sales then steadily fell, bottoming out at 494 units by the fourth quarter of 2007. Since the end of 2007, however, sales of existing single-family homes have predominantly ranged from 700 to 800 units per quarter, finishing up the fourth quarter of 2007 with 779 sales, albeit in a market that is still very much in flux. For example, although sales rose by 58% between the fourth quarters of 2007 and 2009, since the fourth quarter of 2008 they fell by 1.6% before rising by nearly 15% between the third and fourth quarters of 2009.

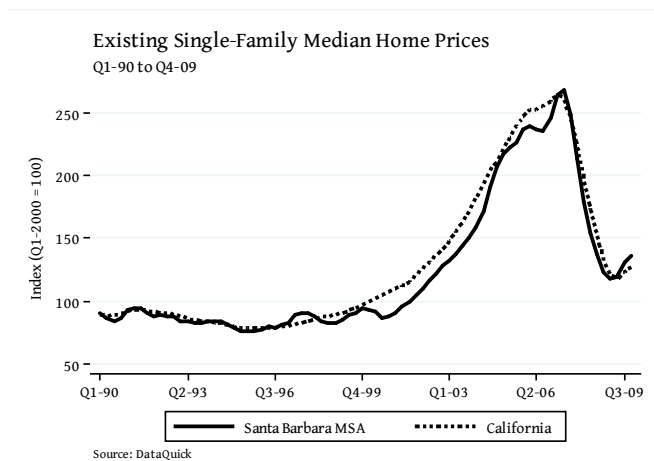
Moreover, steeply discounted foreclosure sales create another wrinkle in the market: Because a significant share of recent sales stems from homes which have been in foreclosure, it makes it very difficult for home-builders and sellers of market-rate existing homes not at risk of foreclosure to compete.

Looking ahead through 2015, Beacon Economics is forecasting existing single-family home sales to range for the most part from 700 to 800 quarterly sales through the end of 2011 before slowly rising to 900 sales per quarter by the end of 2012. From 2013 through 2015, quarterly sales should range mostly from 900 to 950 units.



Not surprisingly, there remains a strong correlation between the rebound in sales and the continuing decline in median prices. Since peaking close to a seasonally adjusted \$650,000 in the second quarter of 2007, the median price for an existing single-family home in Santa Barbara County fell to just \$250,474 by the first quarter of 2009, or a change of 61%. By the fourth quarter of 2009, however, that median price had staged a minor rebound to \$332,789. Although the median price fell by 31% between the fourth quarters of 2007 and 2009, since the fourth quarter of 2008 it rose by nearly 15%. Moreover, between the third and fourth quarters of 2009, it rose by nearly 12%.

According to forecasts by Beacon Economics, the median price for a single-family home countywide is expected to exceed \$340,000 in the first half of 2010 before falling back to the mid-\$330,000s as interest rates rise and as the government support of the housing market is gradually removed. By early 2012, prices are expected to start rising, exceeding \$400,000 by early 2015.



According to Zillow.com, there were just under 2,700 homes for sale countywide in January of 2010, of these, 2,435 were single-family dwellings and nearly one-third were previously foreclosed homes. This level of inventory was up by about 1.5% from the previous month but down by 3% from the previous quarter and down by 13% from January of 2009.

Existing Condominium Sales

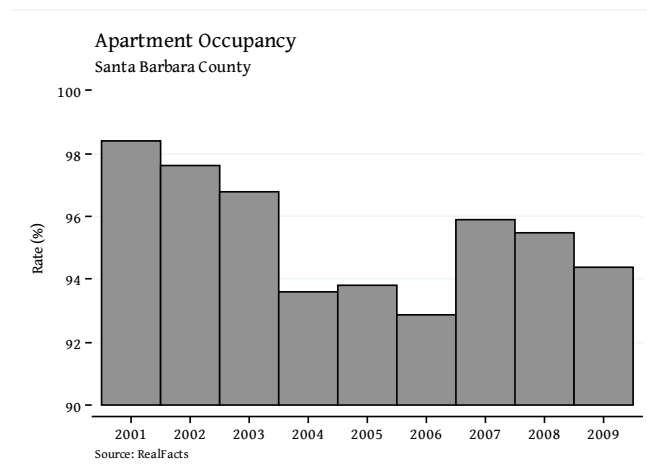
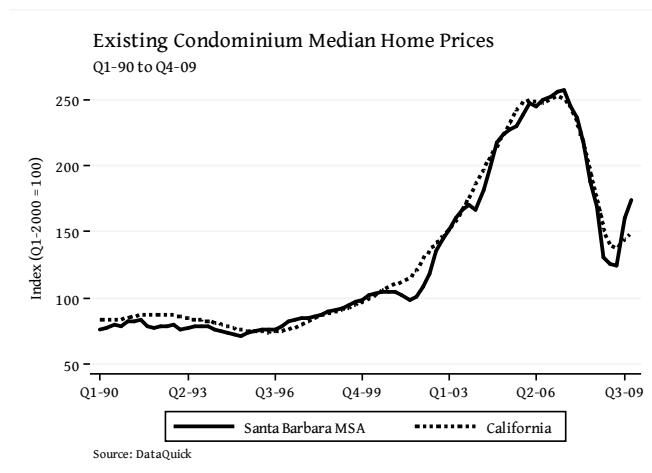
Although the demand for condominiums in Santa Barbara County represents a small fraction of the overall market, during boom-and-bust cycles the pricing momentum for condominiums can change even faster than for single-family homes. And in a county such as Santa Barbara, buying a condominium can provide either a leg up for first-time buyers or a more affordable vacation home.

In contrast to sales in many other counties in California, condominium sales in Santa Barbara County were fairly consistent from the beginning of 2000 through the end of 2005, typically ranging from 200 to 300 units per quarter. But as prices approached and exceeded \$500,000, sales began to slowly descend, falling under 100 units per quarter by the fourth quarter of 2007. Only when prices began to fall below \$400,000—and even below \$300,000—did condominium sales begin to revive. In fact, between the fourth quarters of 2007

and 2009, seasonally adjusted sales of existing condominiums rose by 64%, to nearly 160 homes. Smaller increases were also noted when compared with the fourth quarter of 2008 (up by nearly 19%) and the third quarter of 2009 (up by nearly 14%) even as prices have again approached the \$400,000 level.



Of course, as with sales of single-family homes, condominium sales have risen since hitting bottom at the beginning of 2008 because prices have fallen, from well over \$400,000 to under \$175,000 by the first quarter of 2009; since then, prices have steadily rebounded to over \$300,000 by the third quarter of 2009 and to \$385,000 one quarter later. However, despite the increases of 23% to 25% between the third and fourth quarters of 2009, as well as since the fourth quarter of 2008, it's still too soon to say whether this recent pricing increase is sustainable. In fact, that newfound strength in pricing may also weaken as the FHA tightens requirements for both approved condominium projects and for its borrowers.



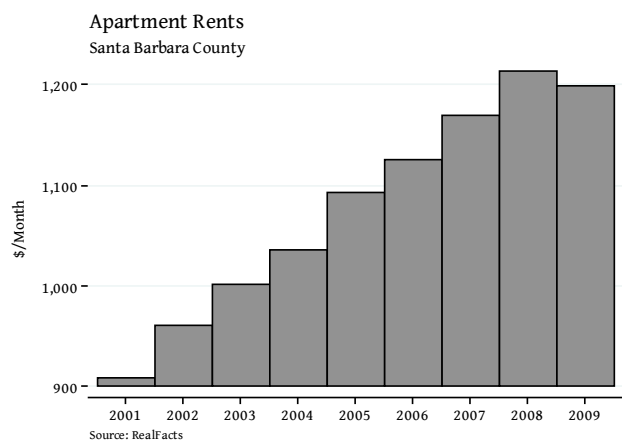
The Apartment Rental Market

After suffering from the effects of two years of massive job cuts and competition from the “shadow inventory” of condominiums and single-family homes put up for rent, the national apartment market finally seems to be stabilizing, with net absorption turning into positive territory and the vacancy rate holding steady at just under 8%. Looking forward, the future remains bright for this housing sector, as the population surge among persons ages 20 to 34 and low levels of construction will eventually conspire to force vacancy rates lower and allow landlords to raise rents.

In Santa Barbara County, the rental market for the type of larger, investment-grade properties tracked by RealFacts has remained relatively solid, with occupancy rates consistently ranging from about 93% to 97% during the past two years. Of course, one reason landlords have been able to maintain occupancy levels has been by offering various incentives and adjusting rents accordingly, thus pushing overall occupancy levels up from just 93.3% in the third quarter of 2009 to 95.5% one quarter later. Still, occupancy levels in Santa Barbara County in 2009 (which averaged 94.4%), although up from the sub-94% levels noted in 2005 and 2006, are down sharply from 2001 and 2002, when they averaged closer to 98%.

Asking rents in the county last peaked at \$1,223 in the fourth quarter of 2008, even as occupancy levels continued to improve slightly. Between the fourth quarters of 2008 and 2009, however, average asking rents fell by 3.2% to \$1,184. Declines were even more pronounced for two-bedroom townhomes (4.1%), studios (4.3%), one-bedroom/one-bath units (3.8%), and two-bedroom/one-bath units (3.8%). At the same time, rent declines were much lower for two-bedroom/two-bath flats (2.8%) and actually rose by 0.2% for three-bedroom townhomes. Still, over the past four years, average asking apartment rents countywide have risen by nearly 10% while vacancy rates have risen by 0.7%.

Of course, landlords are routinely offering incentives (sometimes as much as two free months of rent in exchange for a long-term lease), so effective rents could be 10% to 15% lower than reported asking rents.



Santa Barbara County Apartment Market Overview, Q4-2009

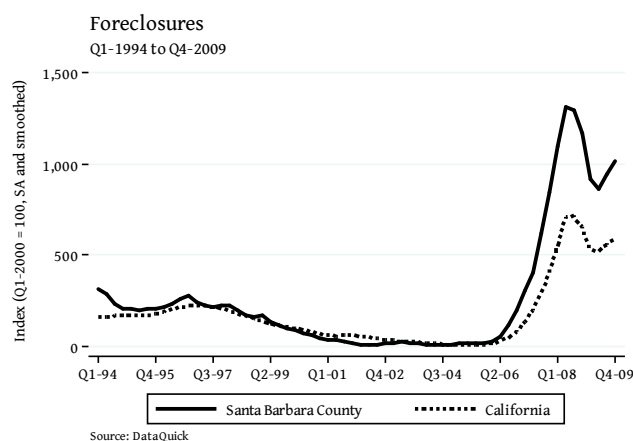
Unit Type	Units	% of Mix	Sq. Ft.	Average	
				Rent (\$)	Rent/SF (\$)
Studio	100	2.4	405	707	1.75
1B/1b	1,781	42.8	646	1,032	1.60
2B/1b	1,188	28.6	825	1,161	1.41
2B/2b	577	13.9	997	1,414	1.42
2B TH	98	2.4	1140	1,933	1.70
3B/2b	146	3.5	1254	1,581	1.26
3B TH	90	2.2	1464	2,277	1.56
All Types	4,159	100.0	792	1,184	1.49

Source: RealFacts.

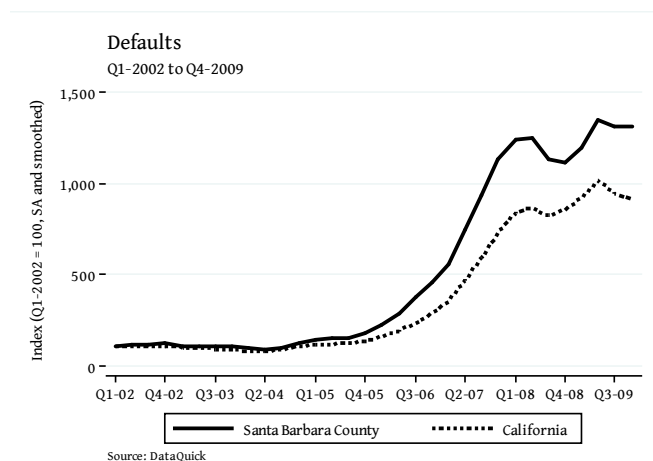
Foreclosures and Defaults

Certainly the most important story still impacting the Santa Barbara County real estate market is that of foreclosures, which during January of 2010 accounted for nearly one-third of all existing home sales (and even higher in the cities of Lompoc and Santa Maria). The \$75 billion plan promoted by the Obama Administration has not been able to assist many homeowners at risk of default because many are simply too far underwater—although lenders such as Bank of America are finally starting to address this problem by allowing for principal reductions under certain circumstances. Moreover, many experts are forecasting a potential new wave of foreclosures to be released onto the marketplace in 2010 and beyond as option ARMs reset to higher interest rates.

Whereas foreclosures in the county were virtually unheard of as recently as 2005—with fewer than 10 seasonally adjusted foreclosures each quarter—by the third quarter of 2008 the number of foreclosures per quarter had skyrocketed past 500. Foreclosures have since fallen from that peak, but over the past year foreclosures have still ranged from 270 to 390 homes per quarter. Moreover, after falling to 270 foreclosures in the second quarter of 2009, they've since risen to 390 homes—an increase of 31%—and are expected to continue rising.



As further proof of this, loan defaults, which had consistently totaled less than 100 homes per quarter through the end of 2005, have exploded in recent years, ranging from 726 to 787 homes per quarter throughout 2009, a more than seven-fold increase, and by nearly 40% between the fourth quarters of 2008 and 2009. Although loan defaults did fall by nearly 8% between the third and fourth quarters of 2009, they are expected to rise again during 2010.



Looking ahead, Beacon Economics forecasts that single-family permits, which totaled about 35 units in the fourth quarter of 2009, will continue to rise slowly but steadily through 2015. By the fourth quarter of 2015, single-family permits could hit 100 units per quarter. Following a few spikes in permits in the middle of 2010 to the triple digits, quarterly permit issuances for multifamily units are projected to fall to under 40 units per quarter by the middle of 2011 but should, like the single-family sector, slowly begin to rebound and approach 100 permits per quarter by the end of 2015.

Residential Building Permits

Since the issuance of building permits tends to follow the fortunes of the construction industry, it should be of little surprise that the total number of permits in 2009 countywide—262—is a fraction of the totals in previous years.

Building Permits (SA), 2007-2009 Santa Barbara County

Type	2007	2008	2009
Single-Family	454	205	191
Multi-Family	282	359	96
Total	683	521	262

Source: RealFacts.

Of this total, 191 were for single-family homes, and 96 were for various multifamily projects (both apartments and condominiums). Since 2007, total permit issuances have fallen by 161%, with the fall in multifamily permits (194%) far greater than that of declines in the single-family sector (137%). Even since 2008, total permit issuances have declined by nearly 100%, although the split between declines in the multifamily sector (275%) and those in the single-family sector (7.0%) is exponentially greater. Not surprisingly, this is largely due to a lack of financing for multifamily development, as well as market fundamentals that are not conducive to supporting construction anyway.

South Santa Barbara County

Home to UC Santa Barbara and well-known for its resorts and exclusive housing, South County's reliance on tourist dollars often means lower-paying service jobs, thus prompting these employees to live in northern Ventura County as well as North Santa Barbara County. While a large percentage of white collar workers in the South County are focused on software and other high-tech pursuits, due to the region's historical preference for slow growth, the existing housing stock remains relatively pricey even after adjustments related to the housing bust.

S&P/Case-Shiller Index South Santa Barbara County, Q3-07 to Q3-09

Area	Index Q3-9	Percent Change		
		Q2-9 to Q3-9	Q3-8 to Q3-9	Q3-7 to Q3-9
Carpinteria	159.3	1.9	-7.9	-30.7
Goleta	150.8	1.7	8.5	-31.0
Santa Barbara	157.3	2.7	-5.8	-30.0
Countywide	142.5	4.1	-4.2	-32.5

Source: S&P/Case-Shiller Index, Jan-00 = 100

Home Price and Sales Overview

In the southern portion of Santa Barbara County—which for the S&P/Case-Shiller Index includes the communities of Carpinteria, Goleta and

the City of Santa Barbara—the index rose from 1.7% to 2.7% between the second and third quarters of 2009, or generally higher than the increase seen in the North County. Between the third quarters of 2008 and 2009, the index fell by 5.8% to 8.5% in these communities versus 4.2% countywide, and between the third quarters of 2007 and 2009 it fell by 30% to 31% versus 32.5% countywide.

In addition, the following table summarizes all home sales by community for South Santa Barbara County during the first quarter of 2009. Please note that these sales and pricing statistics have not been seasonally adjusted and therefore do not necessarily match those cited in the following discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year.

All Home Sales

South Santa Barbara County, Q4-2009

Area	Sales	% of County	Median Price 12/09	% of County
Carpinteria	31	3.3	615,714	139.8
Goleta	60	6.5	608,400	138.1
Santa Barbara	281	30.2	797,083	180.9
Countywide	930	100.0	440,544	100.0

Source: DataQuick

Finally, the table on the next page summarizes various statistics on the existing real estate market as of January 2010 for specific cities in the South County compared with the entire county.

New Homes

The following table summarizes new home sales by community for South Santa Barbara County. As noted above, these sales and pricing statistics have not been seasonally adjusted and therefore do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the third quarter of that year.

South Santa Barbara County New Homes, Q4-2009

Area	Sales	% of County	Median Price 12/09	% of County
Carpinteria	1	3.4	880,000	114.3
Goleta	1	3.4	770,000	100.0
Santa Barbara	6	20.7	1,175,000	152.6
Countywide	29	100.0	769,955	100.0

Source: DataQuick

Existing Single-Family Homes

The following table summarizes existing single-family home sales by community for South Santa Barbara County. As noted above, these sales and pricing statistics have not been seasonally adjusted and therefore do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the third quarter of that year.

Existing Single-Family Homes

South Santa Barbara County, Q4-2009

Area	Sales	% of County	Median Price 12/09	% of County
Carpinteria	18	2.4	667,500	149.9
Goleta	38	5.07	645,000	144.9
Santa Barbara	215	28.4	845,000	189.9
Countywide	756	100.0	445,224	100.0

Source: DataQuick

Existing Condominiums

The following table summarizes existing condominium home sales by community for South Santa Barbara County. As noted above, these sales and pricing statistics have not been seasonally adjusted and therefore do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year.

Resale Home Statistics for North Santa Barbara County, Jan-10

Area	Median List Price		Homes For Sale		Total Homes Sold		Foreclosure Re-Sales		Median List Price/SF	
	Current (\$)	Year Over Year (%)	Current	Year Over Year (%)	Current	Year Over Year (%)	Current (%)	Year Over Year (%)	Current (\$)	Year Over Year (%)
Buellton	429,000	-14.0	N/A	N/A	N/A	N/A	N/A	N/A	253	-13.49
Guadalupe	214,000	29.8	21	-57.1	N/A	N/A	N/A	N/A	131	-6.30
Lompoc	184,900	-8.0	N/A	N/A	49	6.5	55.1	-11.0	147	-6.98
Los Alamos	499,000	-9.3	18	-41.9	N/A	N/A	N/A	N/A	N/A	N/A
Mission Hills	420,000	-10.4	21	-25.0	N/A	N/A	N/A	N/A	175	-3.21
Orcutt	325,000	-7.1	278	-16.5	31	-16.2	32.4	-12.6	194	-4.05
Santa Maria	230,800	2.1	471	-42.9	91	-38.9	44.7	-33.6	149	2.23
Santa Ynez	949,000	-31.0	82	2.5	N/A	N/A	N/A	N/A	381	-8.34
Solvang	675,000	4.0	76	-26.9	N/A	N/A	N/A	N/A	322	0.48
Summerland	1,750,000	6.2	28	21.7	N/A	N/A	N/A	N/A	N/A	N/A
Toro Canyon	2,300,000	-17.9	24	-7.7	N/A	N/A	N/A	N/A	N/A	N/A
Vandenberg Village	399,000	-10.7	65	-5.8	N/A	N/A	N/A	N/A	184	-8.81
Countywide	564,900	18.1	2,673	306	-10.3	32.4	-23.7	261	8.8	

Source: Zillow.com

Existing Condominiums**South Santa Barbara County, Q4-2009**

Area	Sales	% of County	Median Price 12/09	% of County
Carpinteria	12	8.3	480,000	146.4
Goleta	21	14.5	416,250	126.9
Santa Barbara	60	41.4	475,000	144.8
Countywide	145	100.0	327,977	100.0

Source: DataQuick

Foreclosures**S. Santa Barbara County, Q4-2009**

Area	Units	% of County
Carpinteria	11	3.4
Goleta	7	2.2
Santa Barbara	40	12.5
Countywide	319	100.0

DataQuick

Apartment Market

In the case of South Santa Barbara County, the Dyer Sheehan Group has written a special section for this conference book specifically oriented towards the multi-family market in this region.

Foreclosures & Defaults

The following table summarizes foreclosure activity by community for South Santa Barbara County. As noted above, figures have not been seasonally adjusted and therefore do not match those cited in the previous discussion.

Residential Building Permits

The following table summarizes building permits by community for South Santa Barbara County. As noted above, figures have not been seasonally adjusted and therefore do not match those cited in the previous discussion.

Building Permits, (SA) South Santa Barbara County

Area	Single-Family	% of County	Multi-Family	% of County
Carpinteria	7	3.7	0	0.0
Goleta	1	0.5	0	0.0
Santa Barbara	44	23.2	13	13.8
Countywide	191	100.0	96	100.0

Source: CIRB

North Santa Barbara County

Once relied upon as a considerable source of oil, as these fields have proven less profitable and either shut down or turned over to smaller operators, North County has gradually transformed into a housing mecca for white-collar workers who work for companies locally in the South County and neighboring San Luis Obispo County as well as for those employed in and around Vandenberg Air Force Base. As the area has grown, its own largest city—Santa Maria—has also emerged as the county's largest, providing more moderate-priced housing compared to the coast.

Home Price & Sales Overview

In North Santa Barbara County, home prices rose by 1.2% to 2.3% from a sampling in the communities of Lompoc, Santa Maria and the Santa Ynez Valley versus a larger increase of 4.1% countywide. Between the third quarter of 2008 and 2009, the index fell by 4.2% countywide and by 8.0% to 9.2% in these specific communities of the North County, as summarized in the table at the top of the next page.

S&P/Case-Shiller Index

North Santa Barbara County, Q3-07 to Q3-09

Area	Index	Percent Change		
	Q3-9	Q2-9–Q3-9	Q3-8–Q3-9	Q3-7–Q3-9
Lompoc	152.3	1.2	-9.2	-33.0
Santa Maria	158.1	1.6	-8.0	-31.7
Santa Ynez	159.8	2.3	-9.0	-27.5
Countywide	142.5	4.1	-4.2	-32.5

Source: S&P/Case-Shiller Index, Jan-00 = 100

In addition, the following table summarizes all home sales by community for North Santa Barbara County during the first quarter of 2009. Please note that these sales and pricing statistics have not been seasonally adjusted and therefore do not necessarily match those cited in the following discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year.

All Home Sales

North Santa Barbara County, Q4-2009

Area	Sales	% of County	Median Price 12/09	% of County
Buellton	22	2.4	338,375	76.8
Guadalupe	18	1.9	135,000	30.6
Lompoc	136	15.0	215,189	48.8
Santa Maria	367	39.5	238,056	54.0
Santa Ynez	15	1.6	680,000	154.4
Countywide	930	100.0	440,544	100.0

Source: DataQuick

In addition, the table below summarizes various statistics on the existing home market for specific cities in North County versus the overall county.

New Homes

The following table summarizes new home sales by community for North Santa Barbara County. Please note that these sales and pricing statistics have not been seasonally adjusted and therefore do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year. This table is provided for the purpose of comparing new home sales and prices in the various communities only.

North Santa Barbara County New Homes, Q4-2009

Area	Sales	% of County	Median Price 12/09	% of County
Buellton	4	13.8	358,000	46.6
Guadalupe	0	0.0	N/A	N/A
Lompoc	2	6.9	168,000	21.8
Santa Maria	12	41.4	492,500	64.0
Santa Ynez	3	10.3	695,000	90.3
Countywide	29	100.0	769,955	100.0

Source: DataQuick

Resale Home Statistics for North Santa Barbara County, Jan-10

Area	Median List Price		Homes For Sale		Total Homes Sold		Foreclosure Re-Sales		Median List Price/SF	
	Curr (\$)	Yr Over Yr (%)	Curr	Yr Over Yr (%)	Curr	Yr Over Yr (%)	Curr (%)	Yr Over Yr (%)	Curr (\$)	Yr Over Yr (%)
Buellton	429,000	-14.0	N/A	N/A	N/A	N/A	N/A	N/A	253	-13.49
Guadalupe	214,000	29.8	21	-57.1	N/A	N/A	N/A	N/A	131	-6.30
Lompoc	184,900	-8.0	N/A	N/A	49	6.5	55.1	-11.0	147	-6.98
Los Alamos	499,000	-9.3	18	-41.9	N/A	N/A	N/A	N/A	N/A	N/A
Mission Hills	420,000	-10.4	21	-25.0	N/A	N/A	N/A	N/A	175	-3.21
Orcutt	325,000	-7.1	278	-16.5	31	-16.2	32.4	-12.6	194	-4.05
Santa Maria	230,800	2.1	471	-42.9	91	-38.9	44.7	-33.6	149	2.23
Santa Ynez	949,000	-31.0	82	2.5	N/A	N/A	N/A	N/A	381	-8.34
Solvang	675,000	4.0	76	-26.9	N/A	N/A	N/A	N/A	322	0.48
Summerland	1,750,000	6.2	28	21.7	N/A	N/A	N/A	N/A	N/A	N/A
Toro Canyon	2,300,000	-17.9	24	-7.7	N/A	N/A	N/A	N/A	N/A	N/A
Vandenberg Village	399,000	-10.7	65	-5.8	N/A	N/A	N/A	N/A	184	-8.81
Countywide	564,900	18.1	2,673	306	-10.3	32.4	-23.7	261	8.8	

Source: Zillow.com

Existing Single-Family Homes

The following table summarizes existing single-family home sales and prices by community for North Santa Barbara County. Please note that these sales and pricing statistics have not been seasonally adjusted and therefore countywide totals do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year. This table is provided for the purpose of comparing new home sales and prices in the various communities only.

Existing Single-Family Homes**North Santa Barbara County, Q4-2009**

Area	Sales	% of County	Median Price 12/09	% of County
Buellton	17	2.2	360,000	80.9
Guadalupe	18	2.4	135,000	30.3
Lompoc	123	16.3	215,000	48.3
Santa Maria	316	41.8	246,250	55.3
Santa Ynez	11	1.5	675,000	151.6
Countywide	756	100.0	445,224	100.0

Source: DataQuick

Existing Condominiums

The following table summarizes existing condominium sales and prices by community for North Santa Barbara County. Please note that these sales and pricing statistics have not been seasonally adjusted and therefore countywide totals do not match those cited in the previous discussion. In addition, the median price presented is for the month of December 2009 only and not the entire third quarter of that year.

Existing Condominiums**North Santa Barbara County, Q4-2009**

Area	Sales	% of County	Median Price 12/09	% of County
Buellton	1	0.7	190,000	57.9
Guadalupe	0	0.0	N/A	N/A
Lompoc	11	7.6	220,000	67.1
Santa Maria	39	26.9	133,500	40.7
Santa Ynez	1	0.7	270,000	82.3
Countywide	145	100.0	327,977	100.0

Source: DataQuick

Apartment Market

As opposed to the overall county, the apartment market for North Santa Barbara County has been un-

der greater pressure over the past several years. Occupancy rates for the type of larger, investment-grade properties tracked by RealFacts, which averaged 94.8% during the fourth quarter of 2009, was a dramatic improvement from the previous quarter's average of 91.3%, although they're still up by nearly 2% from the same quarter of 2008. For all of 2009, the multi-family properties tracked by RealFacts averaged an occupancy rate of 93.7%, which is down from the 95% levels noted in 2008 and 2007 but up substantially from the 90.3% rate seen in 2006. And of course occupancy levels in North Santa Barbara County are still down sharply from the 98% averages noted in 2001 and 2002.

Asking rents in the North County region last peaked at \$1,013 in the third quarter of 2008 even as occupancy levels fell from 97.2% to 94.8% from the previous quarter. While asking rents here have fallen by 3.5% over the past year, they've actually consistently ranged from \$970 to \$977 over the past three quarters. Moreover, as noted with the overall county, these declines were even more pronounced for certain unit types such as two-bedroom townhomes (-9.8%), studios (-4.9%) and one-bedroom flats (-4.9%). At the same time, rent declines were unchanged for three-bedroom townhomes and much lower for three-bedroom/two-bath flats (-2.5%). Over the past four years, however, average asking apartment rents countywide have risen by 4.0% while vacancy rates have risen by 1.8%.

As noted above, because landlords are routinely offering incentives (sometimes as much as two free months in exchange for a long-term lease), actual effective rents could be 10% to 15% lower than reported asking rents.

Foreclosures & Defaults

The following table summarizes foreclosure activity by community for North Santa Barbara County. Please

Santa Barbara County Apartment Market Overview, Q4-2009

Unit Type	Units	% of Mix	Sq. Ft.	Average	
				Rent (\$)	Rent/SF (\$)
Studio	90	3.3	400	675	1.69
1B/1b	1,101	40.9	642	845	1.32
2B/1b	838	31.1	826	982	1.19
2B/2b	383	14.2	973	1,235	1.27
2B TH	10	0.4	908	925	1.02
3B/2b	129	4.8	1,247	1,584	1.27
3B TH	8	0.3	1,232	1,095	0.89
All Types	2,693	100.0	768	976	1.27

Source: RealFacts.

note that these statistics have not been seasonally adjusted and therefore countywide totals do not match those cited in the previous discussion.

Foreclosures

S. Santa Barbara County, Q4-2009

Area	Units	% of County
Buellton	5	1.6
Guadalupe	5	1.6
Lompoc	76	23.8
Santa Maria	171	53.6
Santa Ynez	4	1.3
Countywide	319	100.0

DataQuick

Residential Building Permits

The following table summarizes building permits by community for North Santa Barbara County. Please note that these statistics have not been seasonally adjusted and therefore countywide totals do not match those cited in the previous discussion.

Building Permits, (SA) North Santa Barbara County

Area	Single-Family	% of County	Multi-Family	% of County
Guadalupe	0	0.0	0	0.0
Lompoc	3	1.6	0	0.0
Santa Maria	8	4.0	3	3.1
Countywide	191	100.0	96	100.0

Source: CIRB

South Coast Apartment Market

by Dawn Dyer
Dyer Sheehan Group Inc.

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Some Specials, but ‘Doing Fine’

In asking about current market conditions, we received a wide range of responses from property owners and managers during our April 2010 Santa Barbara County South Coast Apartment Market Survey.

While many described the market as slow, with a few even offering move-in specials or rent reductions, several others reported they are doing fine. In addition, many properties have no vacancies and little turnover.

Demand Props Up Investments

Despite the conservative market sentiment expressed by many survey participants, the overall average monthly rent for the combined South Coast market areas fell a mere 1.2% from April to October 2009, and has remained flat during the past 6 months. At the same time, the rental market has remained very tight, with an April 2010 overall vacancy rate of only 3% for the South Coast combined market areas, down a full percentage point from the prior year. Multi-family property owners may not see much rent appreciation over the next year as the economy struggles to recover, but the supply/demand imbalance in the Santa Barbara South Coast apartment market should continue to insulate investors from any significant market risk in the foreseeable future.

Smaller Unit Go Wanting

Size does seem to matter, with significantly higher vacancy rates reported in smaller (450-550 sq. ft.) one bedroom units, as people strive to reduce housing costs by doubling up with roommates in larger units. This trend is particularly evident in the City of Santa Barbara, where a significant majority (64%) of the 2,204 units in our survey are one-bedrooms.

The City of Santa Barbara also has the oldest multi-family housing stock in the South Coast, with an average property age of 47 years, which could account for the large number of smaller units. While overall rents in the City fell 1% over the past year, rents for the limited number of three-bedroom apartments went up 1.5%. Santa Barbara City was the only sub-market in our study where the vacancy rate increased over the past year, with a slight uptick to 3.9%, up from 3% last April.

Rents Drop in Goleta

After escalating a full 10% from the previous year, overall average monthly rent in Goleta peaked in April 2009 at \$1,604., and then fell less than 1% to \$1,590 in April 2010. While average studio unit rents have gone up 1% since last April, rents for all other unit types in Goleta have fallen, with the average rent for a three-bedroom unit down over 2%. Despite softening in rents, Goleta occupancy levels tightened significantly over the past year to 96.75%, up from just 95% in April 2009.

UCSB Benefits Isla Vista

Isla Vista continues to enjoy the benefits of being in its own little bubble, nestled up against UCSB. Most properties surveyed have full occupancy, as reflected in the I.V. market area vacancy rate of just 1.5%. While overall average rent is down just over 2%, many properties have held rents flat for the past two years. The Isla Vista market is one of the only areas where we found properties that actually raised rates last year, and some buildings are already pre-leasing units for next fall.

Quick Turnovers in Carpinteria

Several Carpinteria property owners expressed concerns about the market, with higher turnover rates, with more competition for tenants as people lose jobs, move in with family or leave the area. The last year has certainly been more challenging in this southern-most tip of the South Coast, where the vacancy rate rose steadily during 2008 and 2009 before peaking at 7% in October of 2009; but it has since retreated to just under 3% by April 2010. Carpinteria overall average rent has remained flat during the past year at \$1,413, but Studio rents are up 2%.

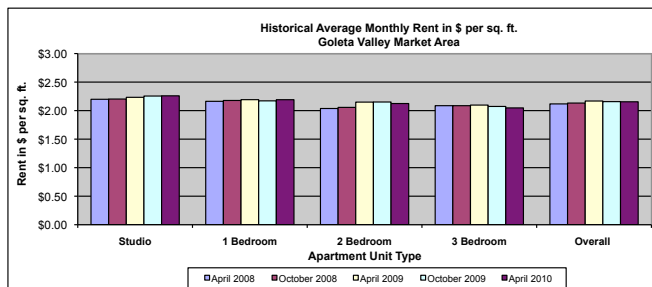
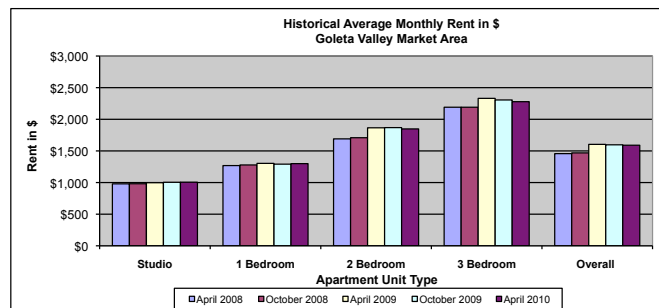
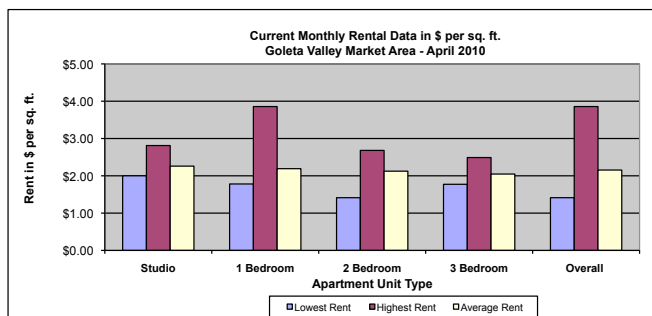
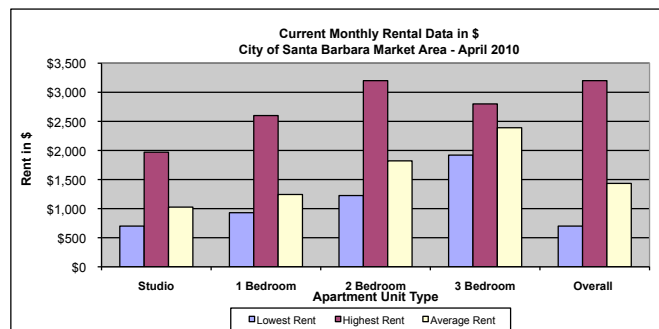
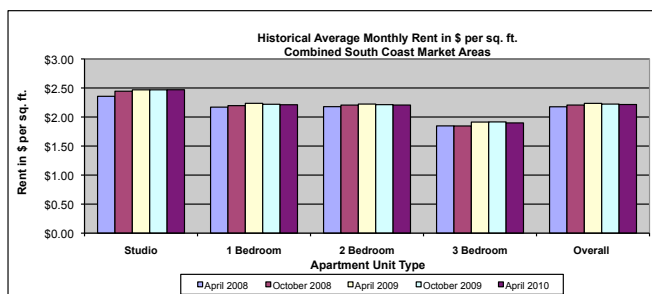
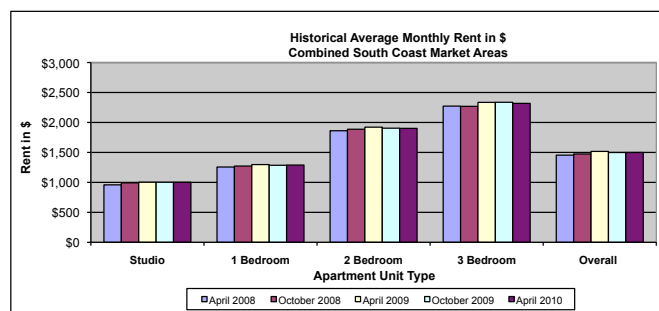
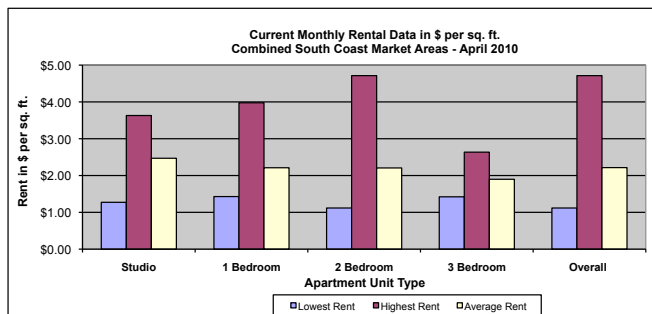
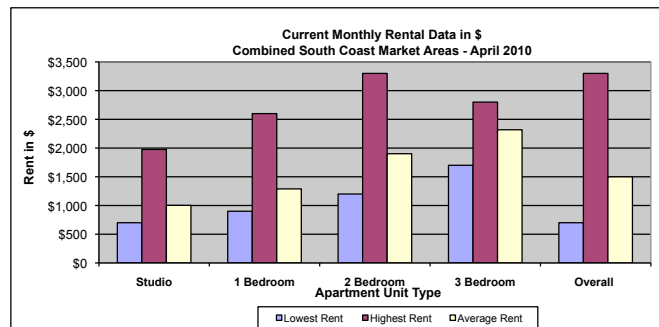
Downturn Prompts Improvements

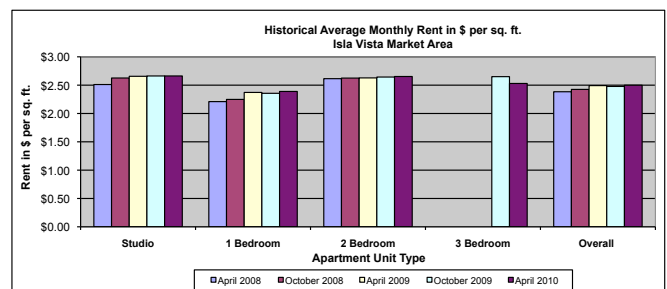
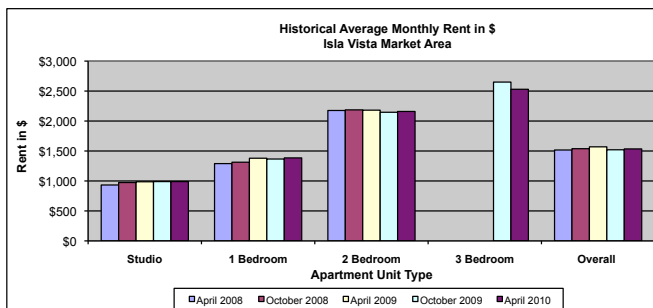
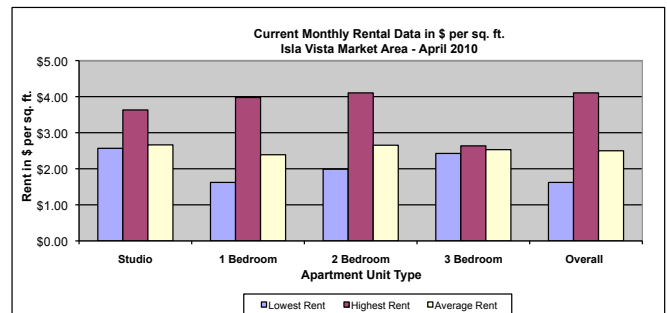
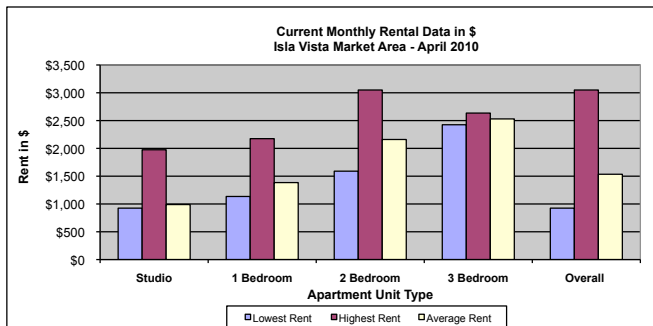
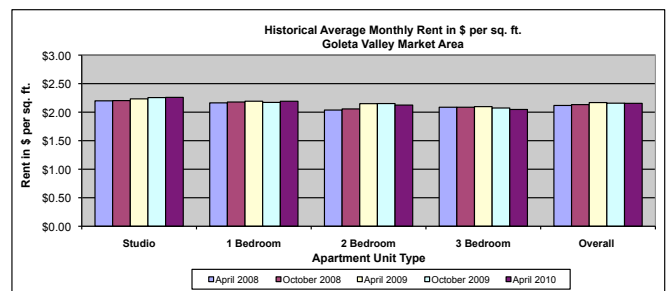
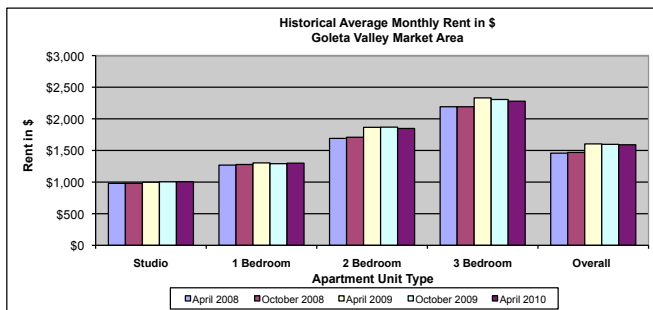
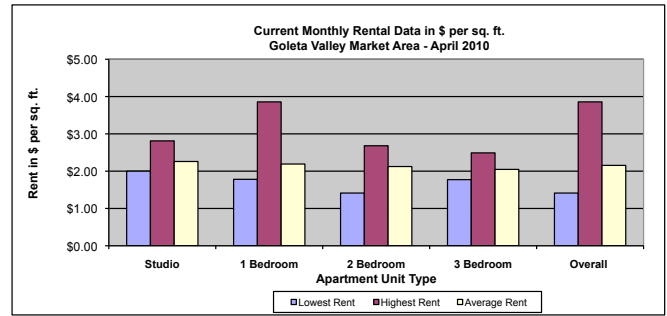
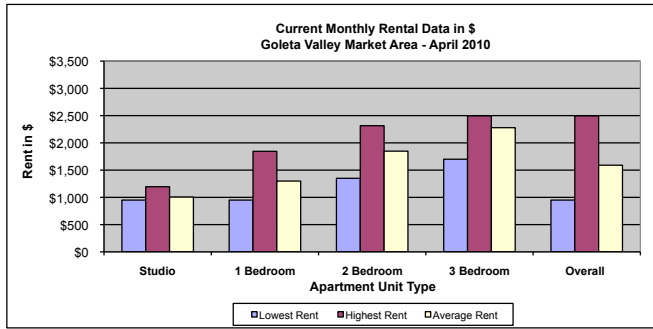
One benefit to the broader community from this slight downturn in the local rental market is that the increased competition for tenants has motivated a number of property owners to rehab their buildings. For many years, owners could rent vacant units quickly without taking time to complete renovations or upgrades on turnover. Numerous survey participants told us that they are currently completing significant property repairs and improvements, which will enhance the quality of life for renters, as well as stimulating the local economy.

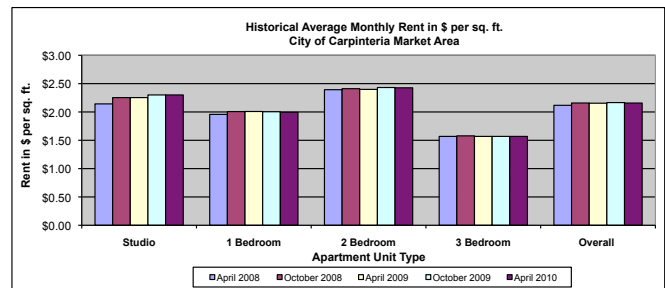
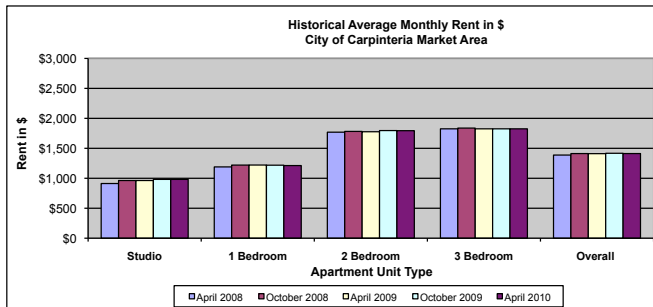
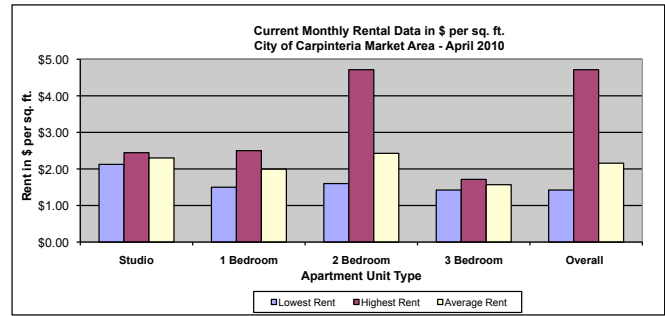
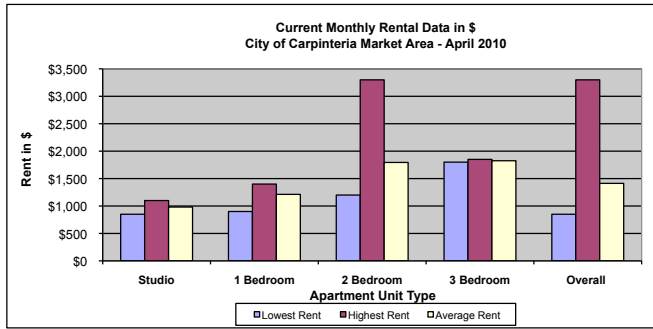
Decade Ahead Looks Up

Demographic and economic trends will lead to an increase in demand for apartments over the next decade. As baby boomers enter retirement, many will sell their homes and opt for the flexibility and financial freedom of renting, while they travel or spend time with grandchildren. Young adults are starting families later in life, while they pursue degrees, careers, and hobbies. The cost of homeownership in Santa Barbara has outpaced the incomes of many local workers. Even with renters leaving the area for jobs or buying homes, people doubling up in housing, and employers contracting, closing or relocating... the Santa Barbara South Coast apartment market will remain relatively recession-proof due to the limited supply of rental housing and the significant barriers to building new apartments.

South Coast Rent Survey







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Multifamily Market Review and Forecast

by Steve Golis and Daniel McGregor
Radius Group Commercial Real Estate

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South County — 2009 Review and 2010 Forecast

The rapid collapse of the financial and credit markets beginning in September of 2008 negatively impacted both apartment and commercial investments. Investors dug in their heels with a wait and see attitude. Recently the national company Marcus and Millichap reported 60% of their 2009 multifamily transactions occurred during Q4, supplying signs of improvement. On a local level, most transactions along the Central Coast were dispersed evenly throughout the year.

Apartment financing is more readily available than commercial property loans. Many banks are ready and willing to make loans with great terms on multifamily properties.

The first quarter of 2010 has already had some large transactions unmatched in 2009:

- 32 units in Carpinteria selling to an out-of-area investor for \$7.2M with a 5.4% cap rate.
- Lavendar Court, a bank-owned condo and retail project in Carpinteria, closed to a local buyer for \$12.55M.
- Two large properties in Isla Vista, The Breakpointe and Coronado, are currently in escrow with a Southern California corporation.

Although buyers are readily available, the inventory for available properties in South County remains relatively small with few on the open market priced within comparable ranges. There seems to be an appetite in our area for larger properties. The appeal of the South County remains strong as a blue chip investment. Prices seem to be stabilized again though we forecast little to no appreciation this year.

- 2009 Gross Rent Multipliers (GRM) in the South County averaged 13.70.
- 2009 Cap Rates in the South County averaged 5.2%.

- 2009 Price Per Unit Averages were at \$202,000.

With little, if any, new rental units coming on the market, we are in an environment where too many people are chasing after too few available properties—keeping our rents stable, which makes the central coast an attractive investment area.

Vacancy rates of between 2 to 4% were the norm throughout most of the South County in 2009. Our forecast for 2010 is for rental rate appreciation to continue to ease on the South Coast though still to remain positive.

Rents above the average have made landlords rethink their positions. We have seen some of those rents softened and expect this to continue.

In our year to date data for 2010 we have seen an increase in sales and escrow from the previous year. The South County still appears to be the blue chip investment for our current economic environment. We had 14 sales of apartment buildings in 2009, exceeding the total for 2008. There have been four sales of apartment properties with more than five units as of early April 2010.

South County Forecast for 2010

- Prices per unit for 10+ units will average between \$180,000 to \$220,000 per unit. Smaller buildings (5-9 units) will sell between \$195,000 and \$230,000 per unit.
- We forecast that cap rates have moved down for the South County. Sales will happen between 5.25% to 6.00% on average.
- Gross rent multipliers will stay at or near 10.5X – 12.75X for 10+ units, while 5-9 unit buildings will sell between 11-14X gross.
- Rents in Santa Barbara will increase modestly by between 1-3%.

- Vacancy rates will remain stable and should still be under 5%. We predict this may go down even further as would-be home buyers cannot qualify for home loans without proper credit and income. Our little-to-no growth rental climate should keep the rental market strong with mostly stable rents.
- Isla Vista continues as a bright spot for the South County. Sales activity and interest in property purchases remain very strong. In 2010 there have been two sales with two large properties in escrow as mentioned above.
- In 2009, the South county had a total of 14 sales of over 5 plus units as opposed to only 9 in 2008, a substantial increase though not at the levels of previous years. Our forecast for 2010 is to surpass those numbers.

Santa Barbara North County — 2009 Review and 2010 Forecast

Santa Maria and Lompoc had very slow sales in 2008 and 2009. We are not aware of any recorded sales of over five plus units during 2009 in either Lompoc or Santa Maria.

However, there are currently three properties in escrow in Santa Maria. While small in numbers this is a quantum jump from the previous 20 months. We are seeing signs of the market rebounding with interest from investors in sales in the North County.

Rents in North County remained stable. Some rents improved in the latter part of 2009, with some complexes implementing rent increases. We feel rents will continue to rise for the same reasons as in Santa Barbara—little to no construction, more home foreclosures (making more homeowners into renters and these foreclosed home selling at brisk paces), and fewer would-be homeowners because they cannot qualify for home loans.

Though the market in general has slowed, the investment fundamentals for apartments have improved during the last year. Multifamily loans are very competitive with rates in the high 5% to low 6% range. Vacancy rates are compressing. Rents are increasing. There is little, if any, new construction to compete with existing properties. We expect investors to see the benefits of investing in North County apartment buildings. All of the properties we are involved with whether with the brokerage hat or the ownership side are experiencing very high levels of occupancy with no rent concessions.

North County Forecast for 2010

- Price per unit averages for 10+ units will stay at or near \$90,000 per unit the remainder of this year in Santa Maria while Lompoc should see averages over \$80,000 per unit as we forecast a slight increase over last year.
- CAP Rates will average between 6.0-7.0% depending on location, condition, quantity of units and rental income.
- Gross rent multipliers will stay at or near 8.5-11 x gross rents.
- Rents in Santa Maria and Lompoc will increase by another 1-3%, modest gains we forecast still remain positive. The foreclosure of homes and short sales in these two areas seem to be sifting through the market.
- Vacancy rates will compress in both Santa Maria and Lompoc with Santa Maria averaging 3-4% and Lompoc averaging 4-6%.

North Santa Barbara County Commercial Real Estate

By Steve McCarty and Steve Davis
Stafford-McCarty Commercial Real Estate

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Key Chapter Findings

- Santa Barbara county is working toward a ‘New Normal’ in commercial real estate.
- Vacancy rates remain high and continue to inch upward in the Office, Retail and Industrial market segments.
- Downward pressure on commercial real estate values is showing up.
- Minimal commercial transactions in 2009.

Toward the New Normal

As commercial real estate brokers we are continually asked, “Where are we going? Is the recovery happening?” Since we do not have a crystal ball to predict the future, we pose the following question in response: “How do you feel about things now versus where you were last year?” The general outcome of this dialog is that nearly all people decide that consumer confidence is stabilizing and we are now dealing with what will be a ‘new normal’. So what will that look like for the north Santa Barbara County commercial markets?¹⁴

Commercial Financing the Cornerstone

The new normal is being shaped both by lender practices and demand for commercial properties. The nascent level of commercial activity over the previous year is comprised of foreclosure activities, downsizing businesses, a few businesses looking to expand, and some investors taking advantage of the overall declining commercial values. The common thread running through all types of activity is that everyone is looking for a deal.

As commercial lenders work through foreclosures, key issues will be declining rental rates, a smattering of vapid transactions showing no clear direction

of valuation, and once lenders have taken the properties back, how to price them.

So where are all the commercial foreclosures?

They just haven’t hit the market yet. The emerging lender practice of “Pretend and Extend” became evident last year. Lenders dealt with potentially problematic loans by negotiating work-out deals with borrowers, pushing problems out to the future so that banks did not have to take properties back and could avoid loan losses on their books. But this practice cannot go on indefinitely, as borrowers who held on to their assets last year may have finally hit the wall. There is no wiggle room left.

Part of the new normal is lenders working quietly with select investors to purchase problem loans at discounts. This is in contrast to the more traditional processes of foreclosing and then working with the brokerage community to expose and dispose of the property. This new approach helps keep the banks public profile low in working through troubled assets.

On the demand side of the equation, there is good news for buyers. If they can qualify, loans are at historically low interest rates. Commercial funds are in the low to mid 6% range. Small Business Administration (SBA) loans are active due to their minimum down payment requirements—near 10%. Banks are willing to take the reduced risk given the underwriting criteria. However, the loan process can be challenging. Borrowers are dealing with an appraisal process akin to alchemy. Lenders are favoring income val-

¹⁴Reported as of the first quarter of 2010.

Single Family Detached Unit Sales
Santa Maria and Orcutt

Category	2006	2007	2008	2009
Single Family Sales in Units	1,335	627	1,242	1309
Single Family Sales OREO in Units	3	116	772	668
Total Sales OREO by Percentage	0.22	18.50	62.16	51
Median Price in Dollars	455,000	395,000	270,000	240,000
Square Foot Cost in Dollars	278	246	179	157

Data Source: Central Coast Regional MLS

Data may vary from last year's reported statistics due to variable change accommodating multi year comparisons and regional reporting.

uation over reproduction methods, and with the lack of transactions, appraisers have had to become more narrative than empirical.

Following is a brief description of the various market segments.

Residential

Santa Maria continues to be the focus for bank owned property in the Central Coast markets. Given that the bulk of new housing was produced in Santa Maria it reasonably follows that the largest foreclosure market is also in Santa Maria. You can buy existing homes cheaper than you can build them. The cost of resale homes declined further this year, more than \$20 per sq. ft. from last year. This sets back the start of the new home building market until existing home prices recover to the tipping point, triggering new building. Foreclosed units will need to normalize to pre-2008 numbers before we see a strong new home market emerge.

Retail/Commercial

After years of adding additional inventory, the retail/commercial market ground to a halt this year. Just 4,688 sq.ft. of retail space was added in all of Santa Maria – the size of a retail bank branch or a couple of small restaurants.

Available commercial/retail space within the City of Santa Maria (as of first quarter 2010) is about 521,312 sq. ft., representing approximately +/-12.43% vacancy (total retail inventory base in the City of Santa Maria is approximately 4,189,503 sq. ft.).

Four major retail projects are still on the books for development. Square footages are approximations:

Project	Sq. Ft.
Lakeview Promenade	70,000
The Westgate Marketplace	120,000
Orcutt Plaza	225,000
Orcutt Marketplace	295,000

Together, these total 710,000 sq. ft. or approximately 17% of the existing base.

That said, construction on the Damon Porter complex on North Broadway has started, with approximately 47,633 sq. ft. in two buildings. Vallarta Market will occupy approximately 36,461 sq. ft. market with the balance being constructed as speculative retail. Fresh and Easy is slated for North Broadway on a land lease.

Retail Vacancy Rates by Percentage (%)
City of Santa Maria Metropolitan Area

2004	2005	2006	2007	2008	2009
2.3	+/- 1	2.0	2.7	9.8	12.5
Without Gottshalks or Mervyns				5.4	8.2

Source: Stafford-McCarty Commercial Real Estate

A former C-2 zoned United Rentals yard at 2691 Santa Maria Way with an approximately 4,200 sq.ft. building on 1.26 acres, sold for \$1,100,000 in September of last year and since has gone back on the market for \$1,495,000. It will be telling to see how this works in today's market.

The former 4,160 sq. ft. Bakers Square restaurant at 1841 South Broadway sits on a site that is a little less than an acre and sold to an owner-buyer for \$900,000. This translates to approximately \$216 per sq. ft.

Previous land price ranges were from \$25 to \$50 per sq. ft. depending upon size and location of the property. Without any definitive land sales, these ranges still may apply (although, if sales price were calculated on land alone without attributing any value to the functioning building, the well-located Bakers Square sale would come out to \$22.38 per sq. ft.)

Office

The office market saw no additions to its base this past reporting period and the market is still very soft. The office vacancy rate, as of this writing, is now at approximately 10.6%, versus 12.4% the year before. After staggering increases, the vacancy has stabilized and even declined a bit. Keep in mind that vacancy in 2008 was 12.4% – almost double what it was in 2007 (6.2%), and triple what it was in 2006 (2.1%).

The office component of this market has a base inventory for 2010 of approximately 1,156,283 sq. ft.

Similar to last year, typical deals are being cut for well located space from \$1.15 and up NNN. The typical second generation asking rates are anywhere from \$.50 to \$1.25/sq. ft./mo./NNN. Newer space has asking rates as high as of \$1.85/sq. ft./mo. Modified Gross. Owners are approaching tenants and rewriting leases for less rent to get them to stay.

A prospective bellwether transaction is the expansion of San Luis Obispo-based American Principle Bank into

Santa Maria with a 3,500 sq. ft. branch office. This is significant in that banks as an industry are consolidating. And the rent was approx \$1.79 per sq. ft with minimal concessions, which was favorable for the ownership given the state of the market.

Some medical spaces have been on the market for over a year. The 220 South Palisades property of 3,213 sq. ft has gone into escrow. With just a few properties selling each year, comparable sales for medical units over the last several years demonstrate values of approximately \$300 per sq. ft.

Office Vacancy Rates by Percentage (%)

City of Santa Maria Metropolitan Area

2004	2005	2006	2007	2008	2009
2.7	2.5	2.1	6.2	12.4	12.2

Source: Stafford-McCarty Commercial Real Estate

The price of land zoned for construction of office space is similar to land prices in the retail segment, as Santa Maria's C-2 zoning allows office uses as well as retail uses. Land price asking rates have dropped—some larger parcels are at \$10.00 per square foot and there are still no takers. Hard-to-find smaller parcels, which typically command a higher price, have come down in asking rates as well.

Industrial

Industrial vacancy again increased from 8.8% in 2008 to 9.57% as of this writing. There is approximately 741,744 sq. ft. of industrial space available for lease (the industrial base is approximately 7,672,586 sq. ft.).

It was a slow year with a notable lack of transactions. A 12,000 sq. ft. concrete tilt up facility on A Street sold for under \$100 per sq. ft. after long exposure on the market – this is a number to watch. This square foot price has fallen close to \$50 per square foot from past neighboring sales.

McCoy Land has two side-by-side offerings from the same owner with listing prices which have just dropped to \$98 per sq. ft. for each of two approximately 21,000 sq. ft. buildings.

Industrial Vacancy Rates by Percentage (%)
City of Santa Maria Metropolitan Area

2004	2005	2006	2007	2008	2009
7.5	5.6	3.6	5.7	8.8	9.6

Source: Stafford-McCarty Commercial Real Estate

There are several noted industrial lease transactions on Industrial Parkway:

- 10,000 sq. ft. – warehouse requirement leased to SAC at \$0.50/sq. ft./mo. gross
- 9,800. sq. ft. – plus yard space leased to Berrypack for \$0.50/sq. ft /mo. Modified Gross plus yard rent
- 14,950 sq. ft. – a 3 year lease renewal at lower rates to PODS for \$0.55 Modified Gross

Sublease availability is increasing in the market and will most likely drive rents downward as sub-lessors will want to stop the bleeding of paying for under utilized space, taking a small loss in rent versus no income on the excess space. Rents and deals are offered below current market rates.

Asking rental rates have shifted downward by moving more toward gross rent from triple net rent. Rents for smaller industrial spaces were approximately \$0.75 to \$0.85 per sq. ft. NNN. Demand has tapered off and is demonstrated by vacancy increases in the “bread and butter” user segment of the Santa Maria market place. These are typical multi-tenant industrial units, in the range of 1,000 to 4,000 sq. ft. where actual rents have decreased to make them effectively gross leases.

Industrial Land

Land sales hibernated this last year. Asking price reductions from appraised values at \$11.00 per square

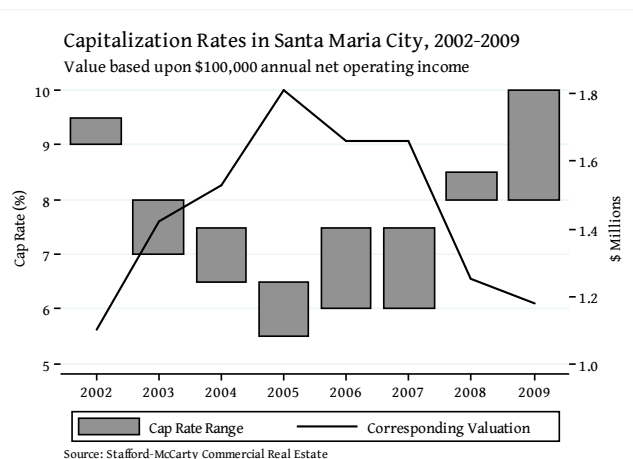
foot for finished industrial parcels three years ago are now on the market for \$9.50 asking values.

Finished or near finished lot product is minimal. Valuations between the M1, CM, and M2 zones are becoming more singular. Acre sale prices can range from \$7 to \$8 per square foot. Comparable sales are now eighteen month plus in age. Oddly enough, these sales are still being used for comparable data in appraisal re-finance and re-evaluations by lenders.

Agricultural

This market segment has had several noteworthy transactions.

The following sale runs counter to the market of downward valuations: Approximately 110 acres of Santa Maria’s best row crop land sold and raised the watermark to approximately \$58.5k per acre, topping a neighboring ranch, which previously set the high watermark at approximately \$56,000 per acre. As always, quality parcels rarely become openly available on the market. These values are approaching values in the iconic Salinas Valley.



It has been rumored that Fosters has the White Hills vineyard south of Orcutt Hill along Highway 1 in escrow in excess of \$25,000,000. This was primarily val-

ued at \$10,000 per planted acre. In comparison, vineyards can cost up to \$30,000 per acre to establish.

Commercial Investment

The 5,450 sq. ft. Carrow's Restaurant at 1635 S. Broadway on approximately 34,258 sq. ft. was recently sold for \$1,580,000 and was valued at a 9.7 capitalization rate.

Although there are very few sales, the following are key for different reasons. One of the highest priced properties to sell in 2009 was the resale of the Hollywood Video at 1846 N. Broadway selling for \$1,888,544. It sold for \$2,350,000 approx a year before.

The estimated cap rate range is the low nine's and indicates both a downward valuation and demand for higher caps. Again with limited transactions, sellers are concerned about "leaving money on the table" and are pricing their asset offerings at 8.0 to 9.5 caps; yet no takers.

CalPortland is offering a sale-leaseback of their 27 plus acre site and operation on Donovan Road for an 8 cap on a long term lease.

The table above shows the capitalization rate ranges evinced over the last eight years. To illustrate the capitalization influence on valuation, assume a commercial building produces a net annual income to the investor of \$100,000. The market cap rates would correlate to the approximate purchase prices for the same piece of property and income according to the following years as noted in the table.

Summary

The new normal is seeking stability. It will be that platform from which we will work in the coming years. The market segments of commercial real estate in Santa Maria are experiencing increased vacancy

rates—some at all time highs. Lenders taking property back in 2009, flat out, just did not happen. It is anticipated that this year deals will begin to emerge to bring investors back into the market, as well as user-buyers. As those deals materialize we will see the new normal stabilize.

Note: For the purpose of this report, databank numbers include functional, non-competitive inventory (older buildings and warehouses) and exclude non-market square footage such as mini-storage, airport hangers, etc.

A Cap Rate (Capitalization Rate) is calculated by dividing the annual net operating income (NOI—which does not include debt service) by the purchase price (e.g. \$100,000 NOI/ \$1,500,000 purchase price equals .0667 or a 6.67 cap rate).

South Coast Commercial Real Estate—2009 Year End Review

by Francois DeJohn (Commercial)

Kris Roth (Commercial)

Brian Bailey (Multifamily)

Hayes Commercial Group

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Key Chapter Findings

- Santa Barbara's retail vacancy has been greater than 2% for four consecutive quarters, and there are currently 127,000 square feet available in the downtown retail corridor of the 300 to 1200 blocks of State Street.
- The 24 sales completed in the second half of the year accounted for 75% of the total sales in 2009, and total sales volume was down 56% compared to 2008.
- Office vacancy increased a full percentage point in the first quarter of 2009, but has remained flat since then despite an 84% increase in square footage leased.

Overview and Summary

Market Indicators

	2009	Change
Sales Transactions	32	-45%
Vacancy	5.0%	+24%
Asking Rates	\$2.09	-10%
Achieved Rates	\$1.92	-17%
Net Absorption	-341K	

Change percentages and net absorption are since 1/1/2009

Figures above include all commercial property types

As we look back on 2009, a year most of us in commercial real estate would not be eager to re-live, we find some unexpected countertrends and even signs of growth among the grim statistics. Judging by continuing high unemployment, record foreclosure rates, and depressed consumer confidence, the national

economy was still under the weather in 2009, and it remains unclear whether it has truly begun to recover. At the same time, the stock markets rebounded robustly through the second half of the year, and major banks began returning TARP funds ahead of schedule. Despite this apparent stabilization in the financial and equity markets, real estate investment remained lackluster due to limited financing, perceived risk, and the disconnect between buyers and sellers over the appropriate discount for said risk.

The South Coast commercial real estate market managed to avoid the high vacancies and precipitous drops in values seen in larger metropolitan areas. That said, vacancy on the South Coast climbed across all leas-

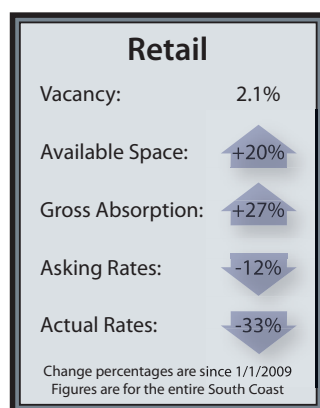
ing sectors and reached a combined rate of 5.0% by the end of 2009, a full percent higher than a year earlier. Not surprisingly, achieved lease rates were down about 15% across the board. Countering both these trends though, leasing activity in both number of leases and transaction value was up for the year. The total square footage leased was 1.3M with a total value of \$134M, a 23% increase over 2008. The number of signed leases was up 38%, including a respectable number of large spaces leased in the office sector. Commercial sales volume was down for the second consecutive year and 56% below 2008's modest pace. However, transaction activity did pick up significantly in the second half of 2009, which could signal a turning point in the sales market.

Office vacancy, after jumping a full percentage point in the first quarter, remained high and remarkably flat through the rest of 2009 and ended the year at 8.4%. Behind this apparent stability there was a surprising amount of activity. 2009 produced 19 leases in excess of 10,000 square feet, led by the renewal of 86,000 square feet at 70 Castilian in Goleta by FLIR and the new lease of 48,000 square feet at 4050 Calle Real

Office	
Vacancy:	8.4%
Available Space:	+14%
Gross Absorption:	+84%
Asking Rates:	-7%
Actual Rates:	-10%

Change percentages are since 1/1/2009
Figures are for the entire South Coast

by CenCal Health. Of these large transactions, seven were high tech tenants, four were medical, and four were government contractors. In the smaller office market, we saw a trend toward opportunistic activity whereby tenants moved into superior locations at favorable terms. Higher quality spaces were even able to command multiple offers, which was not the case a year ago. While this reflects an increase in demand, it mainly circulated around the better spaces, while spaces with limited parking, inefficient layouts, or poor locations had difficulty attracting offers even at reduced rates. Nevertheless, office square footage leased was up 84% from 2008.



South Coast retail vacancy decreased slightly in the fourth quarter but was still up 20.3% since the beginning of 2009. By now, South Coast residents have grown accustomed to seeing available retail spaces in the area's commercial centers, including nine spaces currently

available in the 700 to 900 blocks of State Street in Santa Barbara. The overall vacancy rate of 2.1%—still reasonable compared to national levels—proves that the local market is not completely sheltered from the larger storm. As we have previously reported, there were very few leases by national retailers in the first nine months of the year. Still, buoyed by increased demand in the 4th quarter, the South Coast saw big chains such as Ross and ANGL taking spaces during 2009. In the absence of major national tenant activity smaller chains and local “mom and pop” stores such as So Good Jewelry, Step N’ Out, and The Closet took advantage of the low-demand environment to improve their locations at historically low rental rates. Santa Barbara has seen a sharp reduction in achieved rates as they fell 32.3% in 2009 (rents along the 300 to 1200 block of State Street fell 19.8% in 2009 to \$3.45

GR per square foot). With holiday sales better than expected and consumer confidence figures up for the past two months, retailers have renewed cause for hope heading into 2010.

The market for industrial space by now has swung clearly in the favor of tenants, with more space available than we have seen since at least 2001. Unfortunately, in this economy there seem to be few large tenants willing or able to capitalize on the opportunities. The current industrial vacancy rate of 5.9% even surpasses the high levels of 2002-2003 when the departure of DuPont, Applied Magnetics and Joslyn put a total of 316,000 square feet on the market. The current increase in available space includes 63,921 square feet at 1026-1030 Cindy Lane in Carpinteria. Mirroring the trend seen in the other leasing sectors, vacancy was up despite the fact that 24% more leases were signed in 2009 than the prior year. At the same time gross asking rates slipped down another 11% to \$1.21 per square foot.

Commercial Sales continued to pick up from the stagnant first half of 2009 with 24 sales occurring in the last two quarters, bringing the total to 32 for the year. Even with this increased activity in the second half, the number of sales was still down 45% from 2008, which was a

very slow year, and 58% below the average of 76 sales annually from 2004-2007. The following four sales accounted for about half of the total volume in 2009: the office building at 1111 Chapala St (\$11.3M); the land at 5333 Hollister Ave (\$10.0M); the office building at 1101 Anacapa St (\$8.8M); and the retail building at 1200 State St (\$6.7M). There continues to be a shortage of financing available to investors, and most of the sales last year went to cash buyers or owner-users. With tight credit the new norm, investors have be-



come more risk averse, and we have seen a shift in expected capitalization rates from 4-5% a few years ago to 6-7%. Meanwhile, as the recession enters its third year, some owners who have been holding out for a recovery in buyer demand will soon find their loans coming due. As a result, we expect to see more sellers bringing property to market in 2010.

See the multifamily sales market section later in this chapter for a thorough analysis.

Looking Ahead

Is the worst of the “great recession” behind us? According to most experts it’s still too soon to say for sure. The primary engine of the national economy, the American consumer, is still running in low gear. The financial system is clearly in better shape than a year ago but is still retooling. While 2009 saw a sur-

prising number of leases signed, many of them were relatively short term, “band-aid” leases that will expire in 2010 or 2011. Which means many tenants and landlords will have more tough decisions to make in the coming year.

Taking all of the current trends into consideration, we are not expecting dramatic growth in the local commercial markets this year. For leasing, 2010 will look similar to 2009, with market friction driving steady leasing activity while vacancy remains relatively high and rental rates remain relatively low. We do expect a modest increase in properties for sale in 2010, which should translate to more completed transactions, though not dramatically so. While the coming year may not bring a major recovery to our local markets, it bears repeating that compared to other locations, the South Coast is still in good shape. And there are plenty of enticing opportunities out there for those willing and able to make a move.

Commercial Markets

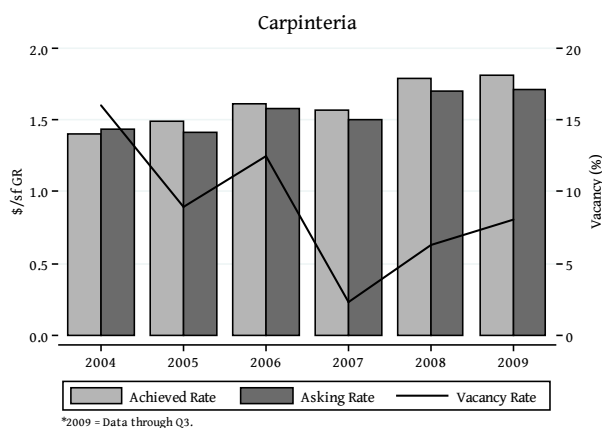
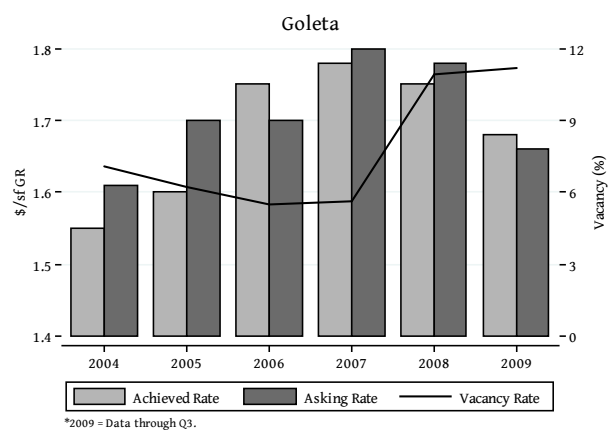
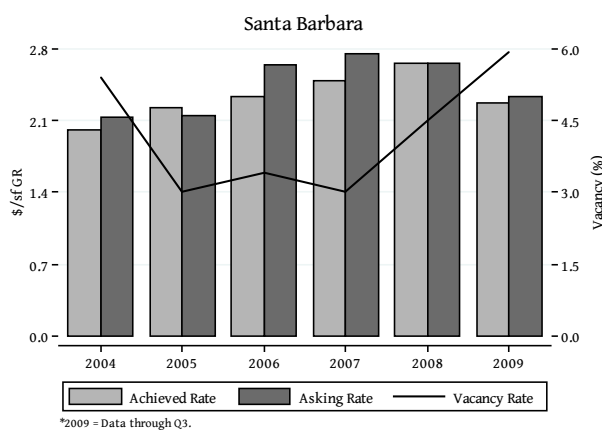
Office Market

The office market produced some interesting results over the past four quarters. Gross absorption has increased 84% since 2008 while vacancy has increased 13.5% over the same period. There were 24 leases completed greater than 10,000 square feet, led by FLIR Technology's renewal of 86,000 square feet at 70

Castilian in Goleta and CenCal Health's leasing of a total of 48,483 square feet at 4050 Calle Real in Santa Barbara. CenCal's lease resulted in a net reduction of 5,000 square feet in overall vacancy as its move has placed 43,000 square feet on the market in Goleta.

Market	Available	Change (%)	Gross Absorption	Change (%)	Asking Rate (\$)	Change (%)	Actual Rate (\$)	Change (%)
Santa Barbara	298,017	32.9	305,920	65.3	2.33	-12.0	2.27	-14.4
Goleta	490,869	3.0	453,738	113.2	1.66	-6.9	1.68	-4.2
Carpinteria	55,355	28.8	67,298	30.8	1.71	0.8	1.81	0.9
Totals	844,241	13.5	826,956	84.0	1.90	-6.8	1.91	-10.3

Change calculated since 1/1/2009.



Retail Market

South Coast retail vacancy decreased slightly in the fourth quarter but is still up 20.3% since the beginning of 2009. While our market is healthy compared to national levels, the number of available properties along historically sought after blocks in the heart of

Santa Barbara's retail corridor is a sign that the local market is not sheltered from the broader recession. Santa Barbara achieved rates fell 32.3% in 2009, and rents along the 300 to 1200 block of State Street fell 19.8% to \$3.45 GR per square foot.

Market	Available	Change (%)	Gross Absorption	Change (%)	Asking Rate (\$)	Change (%)	Actual Rate (\$)	Change (%)
Santa Barbara	248,459	35.4	146,590	13.8	3.44	-18.2	2.86	-32.3
Goleta	50,424	-17.0	57,301	77.4	2.55	5.1	2.31	-28.9
Carpinteria	22,361	-1.7	na	na	2.31	-8.2	na	na
Totals	321,244	20.3	203,891	26.5	3.22	-11.9	2.70	-32.8

Change calculated since 1/1/2009.

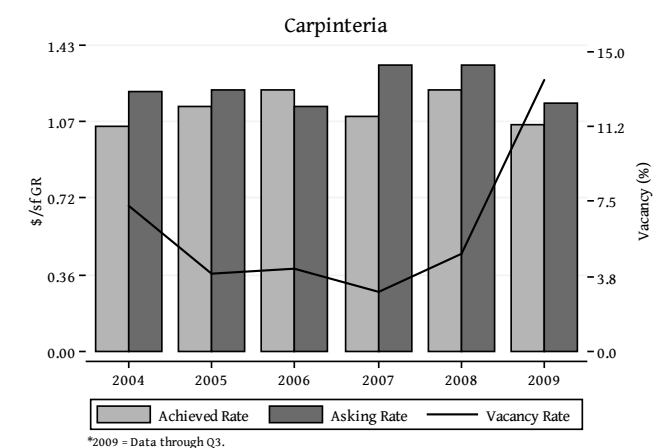
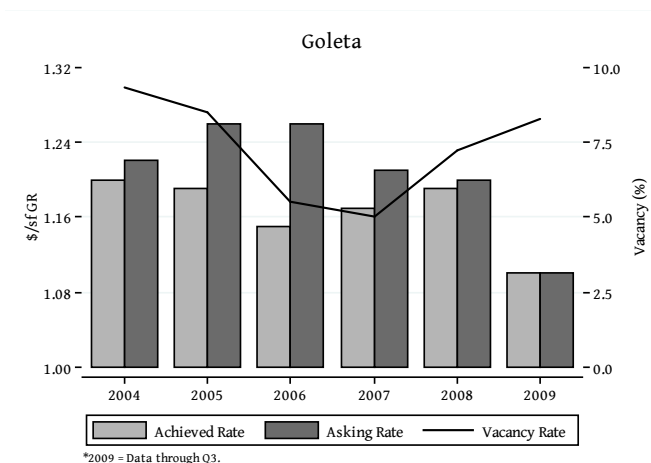
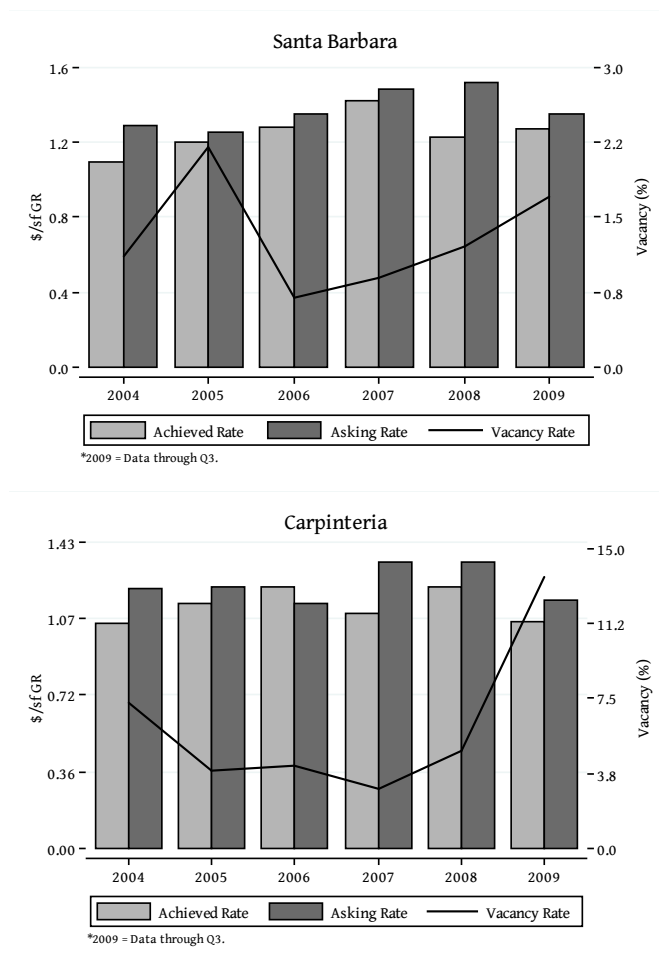
Industrial Market

The South Coast industrial market has seen an increase in vacancy in each market over 2009. Through the end of December there were 46 industrial leases completed, which represents a 24% increase over 2008. However, there has also been a 44% increase in overall square footage available resulting in an over-

all vacancy of 5.9%, the highest year-end rate since at least 2001. Carpinteria saw the largest spike in vacancy from 4.9% to 13.6% due primarily to 63,921 square feet at 1026-1030 Cindy Lane coming on the market.

Market	Available	Change (%)	Gross Absorption	Change (%)	Asking Rate (\$)	Change (%)	Actual Rate (\$)	Change (%)
Santa Barbara	82,228	49.4	68,717	-8.6	1.35	-10.9	1.27	3.6
Goleta	347,986	14.5	92,306	1.5	1.10	-10.2	1.10	-8.5
Carpinteria	180,296	175.8	79,058	16.0	1.16	-13.2	1.06	-13.3
Totals	610,510	43.9	240,081	2.5	1.16	-10.0	1.14	-6.6

Change calculated since 1/1/2009.



Sales in the Market

Sales picked up in the second half of 2009, with 24 of the 32 sales this year completed in the last two quarters. Even with this significant increase, the number of sales was still down 45% from 2008, which was also a sub par year. The following four sales in 2009 ac-

counted for about half of the total sales volume: the office building at 1111 Chapala St (\$11.3M); the land at 5333 Hollister Ave (\$10.0M); the office building at 1101 Anacapa St (\$8.8M); and the retail building at 1200 State St (\$6.7M).

Multifamily Market

The market volume for 5+ units on the South Coast featured a nice increase from six sales for 2008 to 13 sales for 2009. This volume featured eight sales of 5-9 units and five sales of 10-24 units. There were no sales of 25+ unit buildings. The median number of sales from 2003-2009 is 16 and from 1993-2009 is 18 so we are fairly close to our typical volume. We are looking great in comparison the overall U.S. multifamily market which featured a 70% decline in volume through the third quarter of 2009.

As stated in earlier reports, we have a shallow market with low volume. That is why large national multifamily brokerages are almost non-existent locally. Santa Barbara tends to be a money destination, and hold periods tend to be quite long.

The local multifamily market has typically featured resilience and stability as compared to markets in larger metropolitan areas of California. Being a money destination has its advantages. We do not feature GRMs¹⁵ as low and capitalization rates¹⁶ as high as the larger areas, but we do have less volatility. We are considered to be a lower risk area than many larger markets.

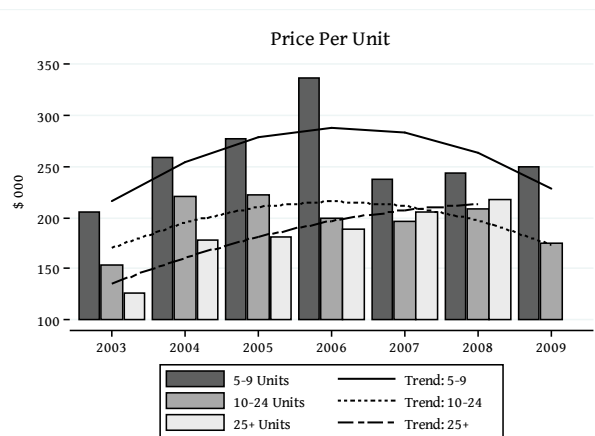
The current market continues to resemble a more “balanced” market. Price Per Unit, GRM and Cap. Rate factors all continue to demonstrate a market moving away from the overheated period of 2004-2006, as shown in the graphs at right.

There have been no fee simple sales of 25+ unit buildings on the South Coast during 2009. There were three 25+ unit sales in 2008 out of six total sales and six 25+ unit sales in 2007 out of 21 total sales. If interest rates remain low, this segment of the market will pick up as investors adjust to a more balanced market.

Sales involving properties in need of substantial renovation have been largely absent in 2009. Such purchases involve a buyer purchasing an underperforming property, making substantial renovations and enjoying the resultant rent increases. This classic real estate investment play has been more prevalent in the past few years. According to Dyer Sheehan Group, Inc. the average age of an apartment building on the South Coast is 42 years, and much of that property is in need of renovation due to age.¹⁷ The exception to this trend was the March 2009 sale of a 12-unit apartment building occupied by a fraternity in Isla Vista. Post renovation numbers produced better than a 7% cap. rate making for the highest cap. rate of the year.

Median Proforma factors:

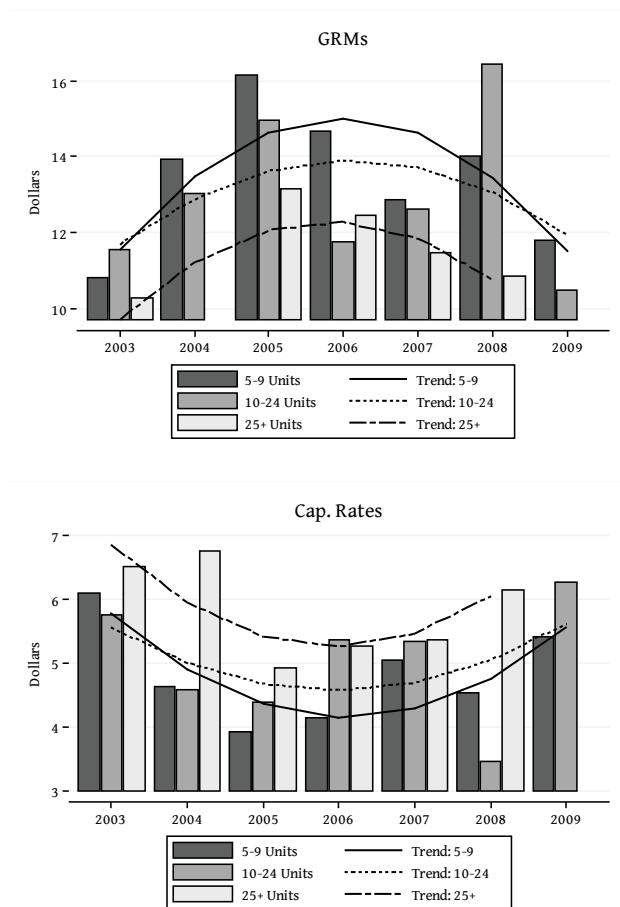
Category	Price/Unit (\$)	GRM	Cap. Rate (%)
All Sales	200,000	11.76	5.96
5-9 Units	250,000	11.79	5.42
10-24 Units	175,000	10.50	6.27
25+ Units	n/a (no sales)		



¹⁵GRM: value or price / annual gross operating income

¹⁶Capitalization (Cap.) Rate: Net Operating Income / value or price – the “yield” of the property without reference to debt

¹⁷Dyer Sheehan Group, Inc., October 2009 Santa Barbara County – South Coast Apartment Market Survey.



Rental Market

The local rental market has continued to weaken, although compared to the national market it is still strong. According to the most recent Dyer Sheehan Group, Inc. report, the overall South Coast vacancy factor was 2.87% in October 2009.¹⁸ This is up from 1.56% in 2008 and 1.38% in 2007. Area numbers show the importance of knowing your sub-market:

City	Vacancy (%)
Santa Barbara	3.11
Goleta	3.27
Isla Vista	0.85
Carpinteria	7.05

¹⁸Dyer Sheehan Group, Inc., October 2009 Santa Barbara County – South Coast Apartment Market Survey.

National Trends

Here is a summary of the opinions expressed by experts at the Apartment Conference—2009:

- Most large apartment investors are net buyers.
- The market has shown signs of recent stabilization.
- The favorable arbitrage between cap. rates and long term financing continues, but may be short term.
- Interest rates will trend upward in 2010.
- The national rental market is weak and will plateau in 2010, begin to rise moderately in 2011 and more decidedly in 2012.
- The Southern California rent concession percentage is now around 8% in many areas.

Local Trends

The volume for 2009 was a large improvement over 2008 and in line with historic volume. Long-term financing for properties remains available at historically low interest rates. The likely increase in interest rates will have a negative effect on this market.

Local buyers should remain alert for any building in good location featuring anything near or exceeding a 6% cap. rate on proforma rents. Sellers waiting for the market to reset to 2005/2006 values will be disappointed. Current values are much more in line with long term value trends in the area. Motivated sellers will find a good market for well-located properties in good condition with market rents and a good set of books. Sellers and properties with opposing features will encounter challenges.

Buyers waiting for the “bottom” or opportunistic purchases will be disappointed in their non-action. Large down payments, quick decision making, appropriate brokerage representation and a track record in this asset class will result in successful acquisitions.

For your multifamily needs contact a specialist:

Brian Bailey

brian@brianbailey.com

James Celmayster

james@hayescommercial.com

South Coast Commercial Real Estate Vacancy and Sales Update

**by Brian Johnson, Bob Tuler,
and Gene Deering**

Radius Group Commercial Real Estate

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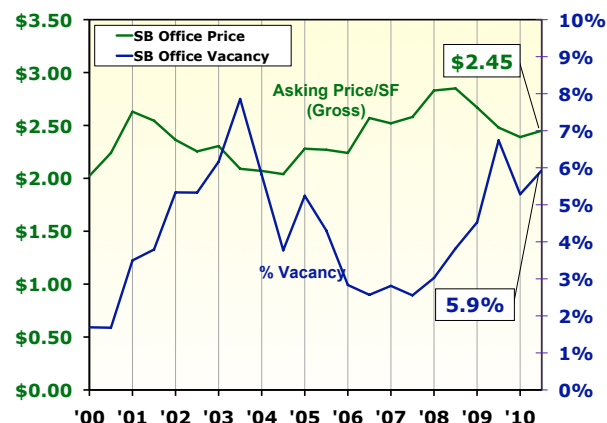
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First Quarter South Coast Market

Overview

While the markets are heating up compared to 2009, commercial real estate in South Santa Barbara County needs several strong consecutive quarters for vacancy rates to improve. At the end of Q1 2010, the vacancy rate for the South Coast office market was 9.3%, the highest we have seen since 1992, the year we started tracking vacancies. In perspective, a vacancy rate of 9.3% is low compared to the 20% vacancies in most of Southern California.



First Quarter Leasing Overview

The first quarter of 2010 saw an increase in commercial activity across nearly all submarkets. This resulted mainly from changing mentality among local businesses. Throughout 2009, local companies were mostly planning for the short-term because of the uncertainty of the future of their businesses. In early 2010 this mindset returned to a more long-range view as companies could more clearly predict future business activity. Real estate decisions are normally part of long-term planning.

Santa Barbara Retail

Santa Barbara's retail market saw the second straight quarter of vacancy declines. While it is not yet time to declare the retail woes over, there are some positive indicators. State Street is seeing an increase in activity as potential tenants view space and make offers. Several smaller retail spaces in Downtown State Street are receiving multiple offers. We expect the retail market to continue to see strong activity throughout Q2. A bright spot is the leasing of 820 State, formerly Anchor Blue, by Guess Jeans for a new concept called "G by Guess".

Santa Barbara Office

Santa Barbara office space leasing experienced a robust first quarter. Leasing activity during Q1 2010 was 30% higher than in the same quarter of 2009. However, the majority of larger leases completed were renewals, which do not improve the vacancy rate. Vacancy actually rose 0.6%, due to the addition of Santa Barbara Bank & Trust's existing administrative offices to the market. Expect Q2 to carry that momentum forward. However, there remains a long list of properties available, suggesting it will take some time for the office market to stabilize.

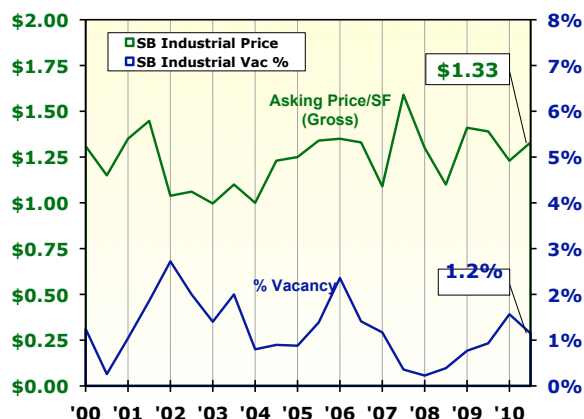


Santa Barbara Industrial

The industrial vacancy rate in Santa Barbara decreased slightly as activity was relatively shallow. This submarket continues to have the lowest vacancy rate in the South Coast because the economy has kept many small businesses from expanding out of their current locations. The few larger spaces available are difficult to fill because smaller tenants are staying where they are until the economy improves. Similarly, smaller vacancies are without leases because tenants are sitting tight, not wanting to make decisions until they see business activity improve.

Additionally, the few smaller vacancies are hard to fill because tenants are sitting tight right now and don't want to make decisions until they see their own business activity improve.

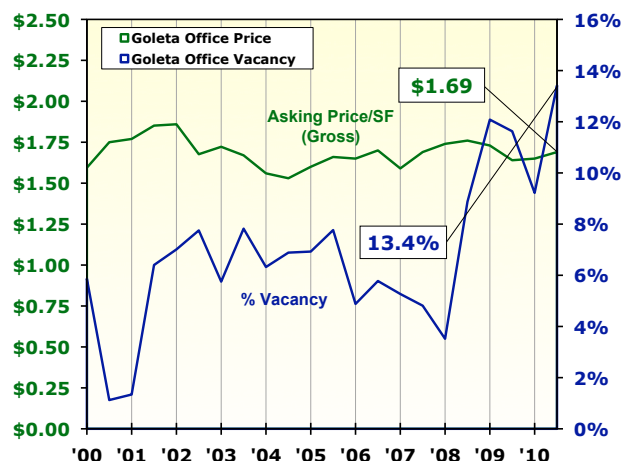
Look for this sector to remain tight during Q2.



Goleta Office

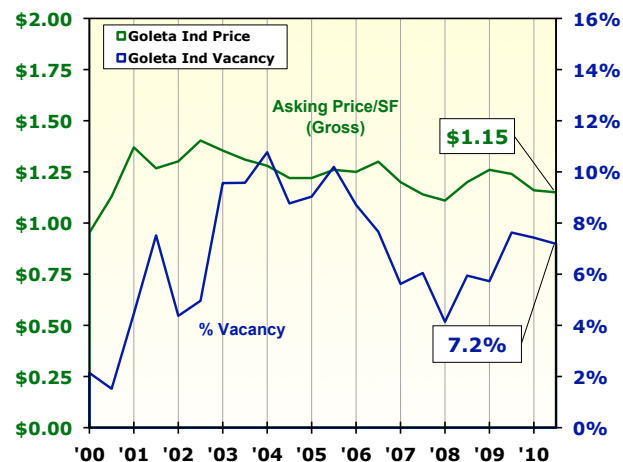
Goleta Office vacancy experienced a spike from 9.2% to 13.4% during Q1. This happened because several large vacancies occurred in the market without the signing of large leases to offset the losses. The two previous quarters had shown steady vacancy rate reductions. The only bright spot was the renewal of Inogen on Bollay Drive. For office markets in the County, Goleta

will take the longest to recover. Companies looking to expand into larger spaces are becoming scarce, while the creation of new local companies has dramatically slowed. This market will take several years to fully recover.



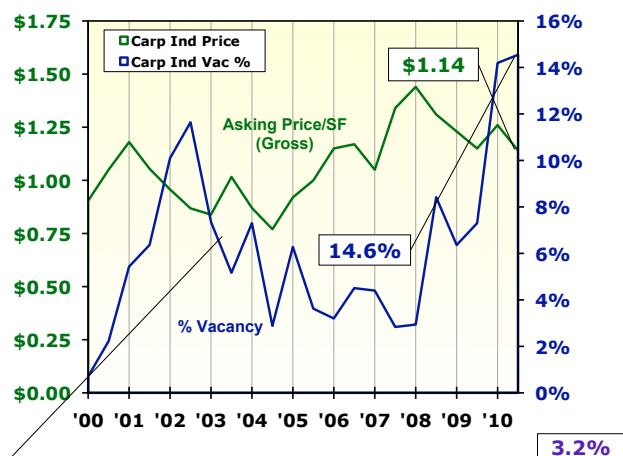
Goleta Industrial

Activity in the Goleta industrial sector was quiet during Q1. Vacancy decreased slightly from 7.4% to 7.2%. The lack of industrial activity is similar to that of Santa Barbara and Carpinteria. The industrial markets are currently showing the least amount of activity. We are seeing more renewals than new transactions across all three industrial markets.



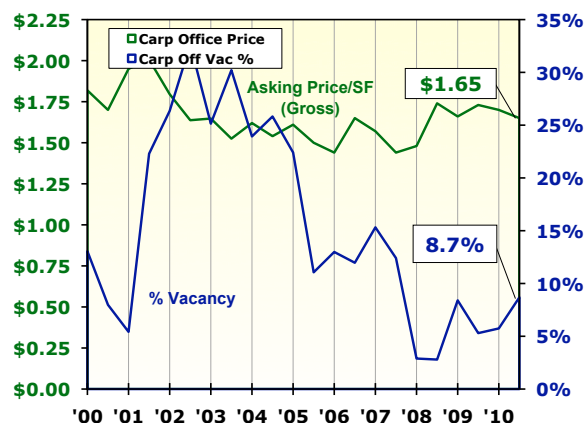
Carpinteria Industrial

Carpinteria industrial saw vacancy levels increase slightly during Q1. The majority of leasing activity continues to be renewals, thus giving little relief to the surplus vacancies. We are seeing asking rates continue to fall as landlords work to attract tenants to the area. The lease rates will need to fall further to compete with the nearby Ventura industrial markets.



Carpinteria Office

Carpinteria's office market saw another increase in the vacancy level in Q1. Several midsize office properties came onto the market and leasing activity was slow. The vacancy rate rose higher than expected to 8.7%. Look for Q2 to remain flat as slow activity continues in this sector. In addition, rates will continue to adjust downward.



First Quarter Sales Overview

The first quarter of 2010 saw an increase in the number of commercial sales from six to nine. While the number is still low compared to historical averages, this represents a great improvement in the overall market. There were several high profile sales during the first quarter including several retail buildings on State Street, plus a large set of office and industrial buildings in Goleta. These activities indicate there is more money coming into the market.

Banks and other lending institutions continue to have a small presence in these activities. However, there have been marked upticks in Small Business Administration loans, seller carry back financing and all cash transactions.

While Santa Barbara should be largely immune to the rise in commercial defaults, the ability to borrow money will continue to be a problem. We will see ongoing difficulty in putting transactions together and this will keep the market from recovering for some time. On the positive side, there are funds that recognize Santa Barbara as a good place to invest and there is a limited inventory of properties for sale.

Demographics

by Eric Weitz

Beacon Economics

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Key Chapter Findings

- Santa Barbara County's population growth rate has basically mimicked that of the state, but with a consistently smaller rate throughout the last 20 years.
- As of July 2009, Santa Barbara County was home to 432,981 residents. An estimated 86,585 of the 139,212 households in the county are families; 34.2% of total households are home to children under the age of 18, and 25.1% are home to seniors over the age of 65.
- Natural increase and foreign immigration have been the most consistent sources of population growth in Santa Barbara County, adding annual averages of 7,442 and 3,868 people per year, respectively, since 1991. Net total migration has been increasing in recent years since a low in 2005.
- Although the median household income in Santa Barbara County is relatively middling in comparison with surrounding counties at \$61,543, median income grew by almost 5.4% from 2007 to 2008 and income inequality decreased in that period as well.

North County

- Santa Maria had the highest annual growth rate of cities within the county in the last year, and Santa Maria, Buellton, and Guadalupe had the highest average annual growth rates from 2000 to 2009.
- Age and ethnic distributions are very different between the southern region of the county and the northern region. The population in the northern region has a Hispanic majority and is much younger on average.
- The median household income is not as high as in south Santa Barbara County, yet has still increased by 4.7% from 2007 to 2008. The North County's relatively low poverty rate and low level of income inequality remained virtually unchanged in that same time period.

South County

- Population growth in Santa Barbara, Goleta, and Carpinteria has been very low since 2000, with an annual average growth rate of 0.25% or lower over the past nine years.
- Median household income is much higher than the county average along the South Coast, but accompanied by a high poverty rate and high income inequality.
- In the southern region the population is aging and primarily white, but still holds a high proportion of people ages 20 to 34, no doubt due to the presence of UCSB.

Santa Barbara County is located along the beautiful central coast of California in between San Luis Obispo and Ventura counties. The county seat is the city of Santa Barbara, which is just surpassed by Santa Maria

as the most populated city in the county. While the characteristics of the overall county population—such as income, poverty rate, and age and ethnic distribution—are mostly similar to those in California, there

While the characteristics of the overall county population—such as income, poverty rate, and age and ethnic distribution—are mostly similar to those in California, there are many important differences within Santa Barbara County.

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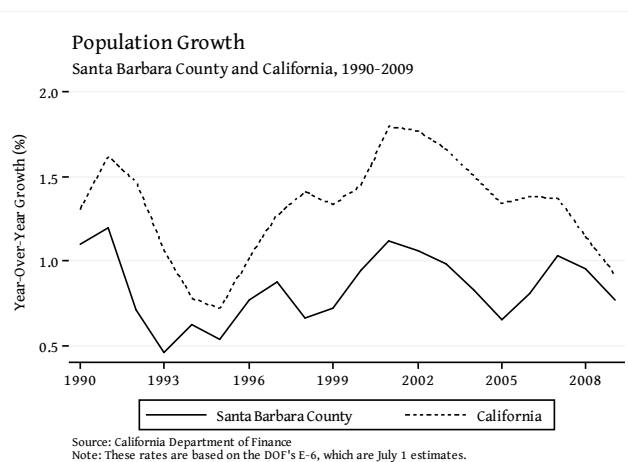
The northern region of Santa Barbara County—which in this chapter comprises everything north of the Santa Ynez Mountains—makes up at least 85% of the county's land mass and half of its population. The biggest cities in the northern county are Santa Maria, Guadalupe, and Lompoc. The central valley, a separate and slightly smaller northern community, is primarily composed of Santa Ynez, Solvang, and Buellton. Overall, the northern county has lower income levels, greater ethnic diversity and a younger population than its southern counterpart.

The southern region of Santa Barbara County—also referred to as the South Coast—has fewer cities in a much smaller geographical area. This region has a higher population density and its residents hold a higher median income—but also a higher poverty rate and greater income inequality. The southern county population has a higher median age than the northern, but still retains a high proportion of people ages 20 to 34, along with a higher percentage of people who have attained a bachelor's degree or higher—both statistics that are no doubt boosted by the presence of the University of California, Santa Barbara (UCSB).

Population

The estimated population of Santa Barbara County reached 432,981 as of July 1, 2009. Annual population growth was 0.77% between July 2008 and July 2009, corresponding to 3,311 new residents. This is slightly lower than the average 0.92% growth rate observed since 2000. Although California's population

has been growing faster than that of Santa Barbara County over the past nine years—at an average annual rate of 1.4%—that gap has narrowed considerably in the past three years and the estimated difference is now only 0.16%, according to the California Department of Finance.



If the past is any indicator, population growth in Santa Barbara County will correspond with that of the state. The California Department of Finance predicts both to slowly decline in the future.

Santa Barbara County has a population density of 150 persons per square mile. While this is greater than that of neighboring San Luis Obispo County at 80, it is considerably less than the southern counties of Ven-

Although California's population has been growing faster than that of Santa Barbara County over the past nine years—at an average annual rate of 1.4%—that gap has narrowed considerably in the past three years...

While net domestic migration in Santa Barbara County has been negative since 2001—with an average yearly outflow of just over 1,400—foreign immigration has contributed an average of almost 1,900 persons per year since 2000, keeping total net migration positive overall.

Fastest-Growing Cities in Santa Barbara County

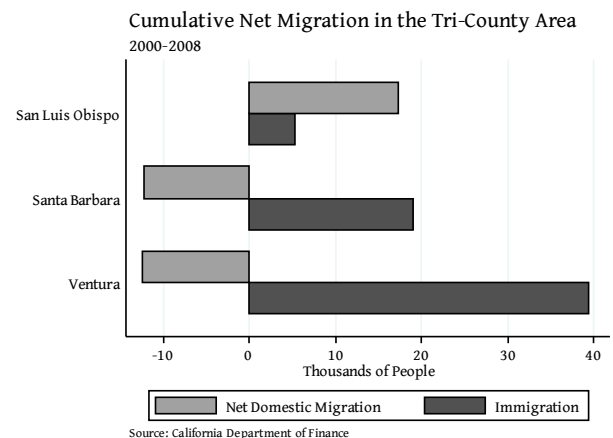
City	Population January 2009	Absolute Change 2008–2009	Annual Growth Rate (%) 2008–2009	Average Annual Growth Rate (%) 2000–2009
Santa Maria	92,542	1,669	1.84	2.07
Carpinteria	14,409	174	1.22	0.25
Buellton	4,740	53	1.13	2.36
Solvang	5,446	48	0.89	0.46
Goleta	30,476	157	0.52	–0.18
Santa Barbara	90,308	234	0.26	0.20
Guadalupe	6,534	10	0.15	1.32
Lompoc	42,892	35	0.08	0.52

Source: California Department of Finance

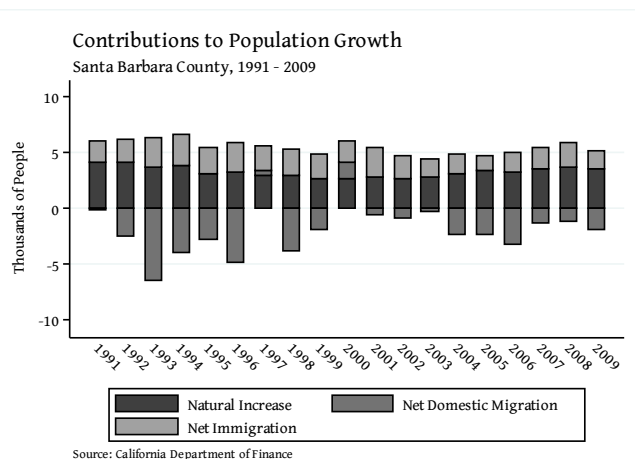
tura and Los Angeles, at 449 and 2,500 persons per square mile, respectively. The disparity in these densities makes sense when looking at a topographical map—the mountainous regions of San Luis Obispo and Santa Obispo give way to more open flat land as you make your way south to the metropolis of Los Angeles.

Sources of Population Growth

Population growth stems from two sources—natural increase and net migration. Natural increase is driven by the characteristics of the local population, such as changes in the age structure and birth rates. Conversely, net migration is driven by the characteristics of the region, including economic performance, affordability, the sociopolitical environment and quality of life.



While net domestic migration in Santa Barbara County has been negative since 2001—with an average yearly outflow of just over 1,400—foreign immigration has contributed an average of almost 1,900 persons per year since 2000, keeping total net migration positive overall.



Like foreign immigration, natural increase has remained positive and steady in Santa Barbara County, with a net gain of 2,600 to 3,600 residents annually since 1995.

North County

The fastest-growing city from 2008 to 2009 was the city of Santa Maria. The three cities with the highest average yearly growth rate over the last ten years are Santa Maria, Buellton, and Guadalupe—all North County cities. These statistics suggest a pattern of expansion in the north region that is not as prevalent in the southern cities. With greater growth will come a greater need for new and expanding businesses.

South County

The only city in the southern region of Santa Barbara County that increased its population by more than 1% last year was Carpinteria. Not only did the larger

The three cities with the highest average yearly growth rate over the last ten years are Santa Maria, Buellton, and Guadalupe—all North County cities.

...all three of the most populated South Coast cities had their lowest average annual growth rate since 2000, with Goleta actually showing a net outflux...

cities of Santa Barbara and Goleta show little population growth in the past year, but all three of the most populated South Coast cities had their lowest average annual growth rate since 2000, with Goleta actually showing a net outflux of people during this time.

Structure of Population

Households

In 2008, the county contained 139,212 households, 62.2% of which were families. The remaining households were non-family households—non-family means unrelated people living together or one person living alone. Of these, 73.6% were a householder alone. Over 34% of total households were home to children under the age of 18, which is lower than the statewide percentage. At the other end of the spectrum, 24.9% of households were home to someone age 65 or greater, slightly higher than in California.

Household Characteristics Santa Barbara County, 2008

2008	Santa Barbara County	North County	South County
Occ. Households	139,212	66,593	72,619
Owner-occupied (%)	53.97	60.59	47.89
Change 2006-08 (%)	0.68	2.97	-1.18
Renter-occupied (%)	46.03	39.41	52.11
Family Households (%)	62.20	72.93	52.36
Change 2006-08 (%)	-1.54	0.8	-3.2
Avg. Family Size	3.37	3.64	3.03
Change 2006-08 (%)	4.01	5.51	1.68

Source: U.S. Census Bureau

The South Coast, however, shows an almost even renter/owner split, with renters just outnumbering owners, along with a noticeably smaller proportion of family households and a smaller average family size... A decrease in family households by 3.2% since 2006 would suggest that families have been moving elsewhere to live—possibly into northern Santa Barbara County.

North County

In the northern regions of the county, the share of the population owing the home in which live in is over 60%. Both the number of family households and the average family size are larger than those of both any bordering counties and the State. Family size and the share of owner-occupied homes have been increasing considerably since 2006, which is usually a sign of a more affordable general cost of living.

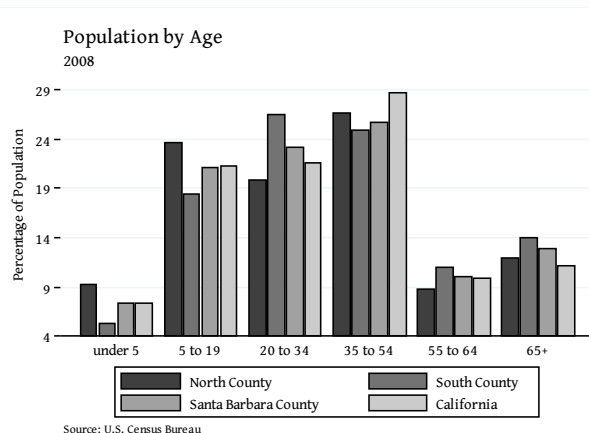
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South County

The South Coast, however, shows an almost even renter/owner split, with renters just outnumbering owners, along with a noticeably smaller proportion of family households and a smaller average family size. Both of the latter figures are not only lower than in the County, but also much lower than in the State as well. A decrease in family households by 3.2% since 2006 would suggest that families have been moving elsewhere to live—possibly into northern Santa Barbara County.

Age

In 2008, Santa Barbara County's overall age structure was mostly representative of California as a whole, with a slightly larger share of younger people and senior citizens and fewer middle aged persons. The largest share of the population falls into the 35-to-54 category, followed by those ages 5 to 20. Again, the differences within the county are larger than those between county and state.



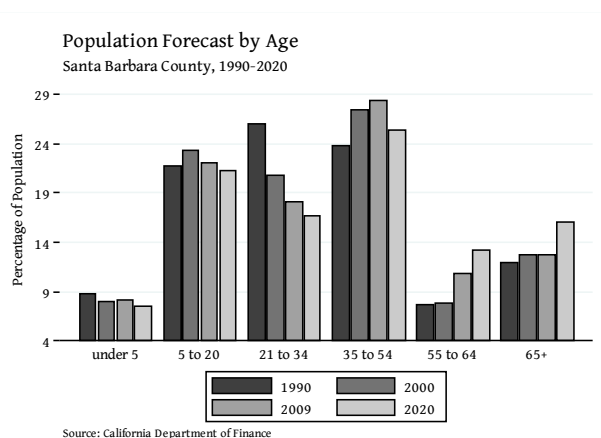
North County

The most notable characteristic of the northern region's age distribution is the comparatively large population under the age of 20, which contributes to an overall younger population. As mentioned above, this is a product of a greater proportion of families and bigger family size, with more children.

South County

The average resident in the south region is generally older than the county and state average age, but the South County is not without its own young population, as the 20-to-34 age group is proportionately greater there. With UCSB bringing in a large population of people mostly in this age range, that number is unlikely to change very much in the future. The higher share of people over 55 years, however, does suggest a growing population of senior citizens, especially along the southern coast, over the next several years.

The average resident in the south region is generally older than the county and state average age...



The California Department of Finance forecasts the population of the entire county to get older in the next decade. All age groups under 55 years are predicted to decrease in percentage from current levels, while the 55-to-64 and 65-and-over age groups will both be increasing. An older population will create a higher demand for health care and social services at the very least, as older people are the most common consumers in that industry.

Race and Ethnicity

Throughout Santa Barbara County there is a lower proportion of people of both African American and Asian ethnicity than in the state, counterbalanced by higher percentages of both Hispanics and non-Hispanic whites.

Population by Ethnicity in Santa Barbara County, 2008

(% of Population)	Santa Maria City	Santa Barbara City	North County	South County	Santa Barbara County	Statewide
African American	0.3	4.3	1.7	2.3	2.0	5.9
Asian	4.5	4.0	3.0	5.6	4.3	12.2
Hispanic	68.8	30.6	48.4	30.0	39.5	36.6
Non-Hispanic White	25.5	59.5	44.8	59.2	51.7	42.0
Other	0.8	1.6	2.1	3.0	2.5	3.2

Source: U.S. Census Bureau

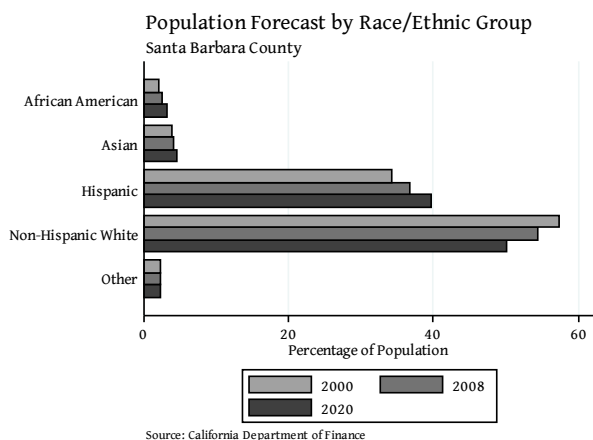
North County

Santa Maria, the most populated city in Santa Barbara County, has a mostly Hispanic population at just under 70%. Likewise, in the North County overall, Hispanics represent a large portion of the population, at just under 50%.

South County

As shown in the chart, Santa Maria's ethnic distribution is in stark contrast to the major city of the South County, Santa Barbara, which is mostly representative of the southern region overall. The majority of residents are white. The Hispanic, Asian, and black populations all fall below the statewide percentage.

...when income started to increase again in 2002, the county levels rose considerably faster than those of the state over the following five years, leaving a margin of about \$6,000 between the two.

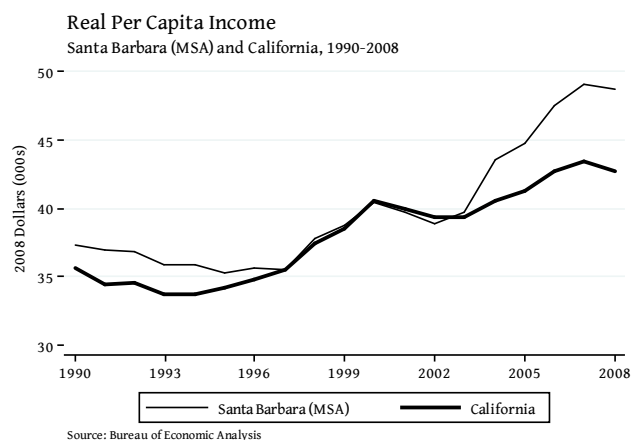


Over the next ten years, the county's population is expected to follow a pattern similar to many of California's counties and the state overall. The Hispanic population will increase more rapidly than other ethnic groups, while non-Hispanic whites will decrease by a similar proportion. All other ethnic groups will either increase just slightly or simply maintain their current share of the population.

The Hispanic population will increase more rapidly than other ethnic groups, while non-Hispanic whites will decrease by a similar proportion.

Income and Poverty

Much of Santa Barbara County's income and poverty statistics follow the levels and patterns seen in California. According to the Bureau of Economic Analysis, real per capita income was almost identical for the county and the state from 1997 to 2003.



However, when income started to increase again in 2002, the county levels rose considerably faster than those of the state over the following five years, leaving a margin of about \$6,000 between the two. As of 2008, the state still appears to have been hit harder by the recession, as Santa Barbara's decline in income was not quite as steep as the decline in the state from 2007 to 2008.

Median Household Income Comparisons, 2008

County	Number of Households	Median Household Income (\$)	Share < \$35,000 (%)	Share > \$100,000 (%)
Ventura	256,944	76,860	21.2	37.4
Orange	971,559	75,078	21.3	36.4
Santa Cruz	93,759	67,466	27.2	32.8
San Diego	1,037,958	63,026	26.8	29.1
Santa Barbara	139,212	61,543	26.8	27.6
San Luis Obispo	100,901	60,534	29.9	24.3
Monterey	126,066	59,375	27.8	24.0
Los Angeles	3,168,362	55,499	32.6	25.4
California	12,176,760	61,021	28.9	28.2

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

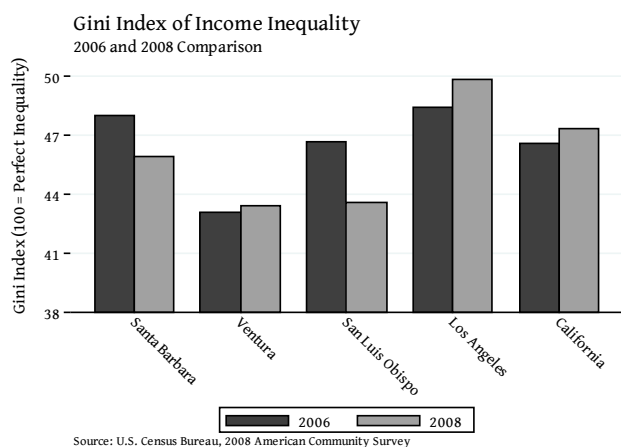
With regard to median household income, Santa Barbara County ranks somewhere in the middle when compared with both central coast and southern California counties. While the county has a higher median household income than that of Los Angeles, San Luis

...while the South Coast receives a higher median income, the northern portion of the county enjoys a lower poverty rate and less income inequality. There are fewer very rich people, yet fewer poor people as well.

Obispo, and California, it lags behind the high-income counties of Ventura, Orange, and Santa Cruz.

The Gini index measures income inequality, with a value of 0 representing perfect income equality and 100 representing perfect income inequality. Santa Barbara County overall has higher income inequality than its surrounding counties of Ventura and San Luis Obispo, although not as high as Los Angeles or even the state. The income and income inequality levels combined suggest there are greater income inequalities in Santa Barbara than in its neighboring counties. In practice terms this means there are a few households with large incomes and many with much low incomes.

While the county has a higher median household income than that of Los Angeles, San Luis Obispo, and California, it lags behind the high-income counties of Ventura, Orange, and Santa Cruz.



Similarly, the 12.4% poverty rate in Santa Barbara County is just higher than that in San Luis Obispo, but still about 1% lower than the statewide rate. Ventura has an impressively low countywide poverty rate, while Los Angeles rises above the state level to over 15%.

Income and Poverty in Santa Barbara County

	Santa Barbara County	North County	South County
2008			
Med. Household Inc.	61,543	54,496	69,309
Change 2007-08 (%)	5.38	4.70	11.57
Poverty Rate (%)	12.40	10.10	14.90
Change 2007-08 (%)	0.5	0.1	0.9
Gini Index	45.90	42.50	47.70
Change 2007-08 (%)	-2.13	0.95	-4.22

Source: U.S. Census Bureau

South County

Southern Santa Barbara County has a higher median household income than the northern region by just under \$15,000. This may go hand in hand with the much higher real estate values and denser, more urban cities along the South Coast. Another notable difference is the much greater increase in median income in the southern county from 2007 to 2008, which would be considered a big jump in one year almost anywhere.

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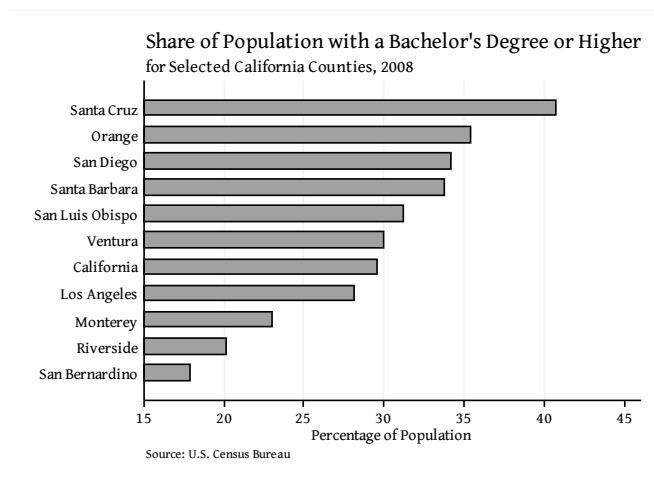
The proportion of people in the northern region with less than a high school level of education is almost as high as the proportion with a bachelor's degree in the south.

North County

However, while the South Coast receives a higher median income, the northern portion of the county enjoys a lower poverty rate and less income inequality. There are fewer very rich people, yet fewer poor people as well. As the cost of living is less and real estate rates are lower in the northern regions, incomes much lower than those in the south would not affect quality of life as much as it may appear to at first glance.

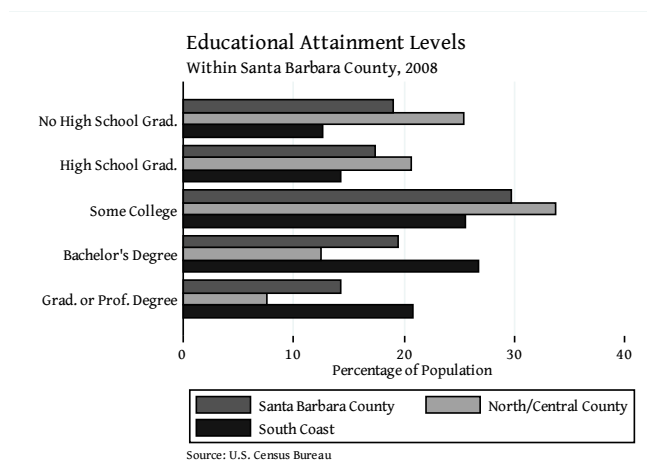
Educational Attainment

Santa Barbara County has a higher proportion of people who have earned a bachelor's degree or higher than every Central Coast county except for Santa Cruz. The only counties with a higher overall percentage in Southern California are San Diego and Orange. Again, the presence of a university—and a UC school in particular—appears to keep educational attainment averages high in such counties.



North County

The proportion of people in the northern region with less than a high school level of education is almost as high as the proportion with a bachelor's degree in the south. Although the highest share in the north is actually in the "some college" category (which includes people who have earned an associate's degree), there are large shares in the lower educational attainment levels.



South County

In the the southern region, it is no surprise that the proportion of the population with a bachelor's degree or higher comprises almost 50% of that area's population, accompanied by a much lower proportion that have never attended any college. In addition to housing a university, the county's increasing median household income and the type of employment available may attract higher-educated residents.

...the county's increasing median household income and the type of employment available may attract higher-educated residents

The most obvious places for additional residents would be the locations that have been expanding the most throughout the past several years, such as Santa Maria, Buellton, Guadalupe, and Lompoc.

Projections and Implications

While population growth in Santa Barbara County has been slowing over the past 10 years or so, growth remains positive and the population is still increasing.

North County

The most obvious places for additional residents would be the locations that have been expanding the most throughout the past several years, such as Santa Maria, Buellton, Guadalupe, and Lompoc. In addition

While population growth in Santa Barbara County has been slowing over the past 10 years or so, growth remains positive and the population is still increasing.

to their capacity for expansion, these places are all in the north region, which are considered more affordable to live in than the southern cities. A growing population in the north region would mean a greater workforce and more opportunities to expand on existing industries, as well as create new ones, in the area.

Furthermore, the population in northern Santa Barbara County is younger and less educated than the county overall, which may create a greater need for educational services in the future.

South County

Over the past 10 years, population growth in the county's southern cities has been very low, either because there is no room to expand or no desire or both. If the poverty rate continues to stay as high as it is, and increase like it did from 2007 to 2008, more people may leave the area to try a new life somewhere with a lower cost of living.

If the poverty rate continues to stay as high as it is, and increase like it did from 2007 to 2008, more people may leave the area to try a new life somewhere with a lower cost of living.

As the mean age of the population along the South County region grows higher, as it is predicted to, demand for health care and social services will increase. Although this is already a big industry in the southern region, health care and social services may require further expansion.

Population Characteristics

2008	Santa Barbara County	San Luis Obispo County	Ventura County	Los Angeles County	California
Foreign born (%)	22.7	11.6	22.3	35.2	26.8
<i>Naturalized of the foreign born (%)</i>	30.8	42.6	41.2	44.6	44.6
Poverty status (%)	12.3	12.1	8.3	15.1	13.2
Homeownership rate (%)	54.0	63.1	66.3	48.2	57.0
Vacancy rate (%)	8.3	13.6	6.1	6.4	9.1
Household size (persons per household):					
<i>Total</i>	2.8	2.5	3.1	3.0	3.0
<i>Owner-occupied</i>	2.7	2.5	3.0	3.2	3.0
<i>Renter-occupied</i>	2.9	2.5	3.1	2.9	2.8
Transportation to work (%):					
<i>Drive alone</i>	64.6	74.3	78.8	71.5	72.7
<i>Carpool</i>	16.7	10.4	11.6	11.6	11.9
<i>Public transit</i>	3.5	1.2	1.1	7.3	5.3
<i>Motorcycle, bicycle, taxis</i>	4.8	3.7	1.7	2.3	2.5
<i>Walk</i>	4.1	4.3	1.7	2.9	2.8
<i>Work at home</i>	6.3	6.1	5.1	4.4	4.8

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

Population Growth for Selected California Counties

County	Population July 2009	Absolute Change 2008–2009	Annual Growth Rate (%) 2008–2009	Average Annual Growth Rate (%) 1999–2009
Riverside	2,127,612	30,175	1.44	3.45
Fresno	948,928	12,822	1.37	1.80
Santa Clara	1,872,049	24,888	1.35	1.15
San Diego	3,208,466	38,976	1.23	1.49
Contra Costa	1,068,759	12,513	1.18	1.38
Alameda	1,568,903	18,351	1.18	1.04
San Mateo	750,436	8,282	1.12	0.69
Santa Cruz	270,882	2,931	1.09	0.74
Monterey	433,887	4,689	1.09	1.06
Ventura	841,001	8,708	1.05	1.31
Orange	3,155,393	31,187	1.00	1.26
San Francisco	851,485	8,083	0.96	1.06
Sacramento	1,439,985	12,891	0.90	1.94
Santa Barbara	432,981	3,311	0.77	0.91
Marin	259,772	1,804	0.70	0.63
Los Angeles	10,409,035	67,625	0.65	1.06
San Luis Obispo	271,821	1,532	0.57	1.12
San Bernardino	2,064,375	9,952	0.48	2.06
California	38,487,889	353,393	0.93	1.45

Source: California Department of Finance

Quality of Life

by Alexander Lin Beale

Beacon Economics

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Key Chapter Findings

- Santa Barbara's successes in improving educational outcomes and lowering crime rates can be classified as moderate. Some educational measures are improving, while others are declining, and crime rates, though low, were lower quite recently.
- Efforts to improve the quality of life in the county, particularly raising educational outcomes and reducing crime, will likely suffer under the current economic downturn. The severe fiscal problems facing the state will further complicate progress in these areas.

South County

- South County has slightly lower rates of crime overall, although a more significant divide in crime is between the larger and smaller cities in the County. The City of Santa Barbara itself has the second-highest crime rate in the county. Academic performance, particularly as measured by proficiency rates, is also slightly higher.

North County

- North County has somewhat higher crime rates, with Santa Maria posting the highest rates of violent and property crimes. The lower educational attainment levels and average incomes in the north likely contribute to this difference. The northern part of the County also demonstrates lower educational outcomes, although Santa Ynez Valley Union High has exceptionally high proficiency rates, by far the highest in the County.

Santa Barbara County is renowned for its high quality of life, with its fairly small cities and towns dotting the Pacific coastline and the valleys inland of the Santa Ynez Mountains. Truly, proximity to nature is one of the County's great appeals. However, the County is significantly divided between the northern and southern portions, essentially split by the Santa Ynez Mountains, with major differences in economic activity and demographics. This divide is so substantial that there have been two fairly recent attempts at creating a separate northern county, in 1978 and 2006. These efforts were unsuccessful—not entirely surprisingly—given that the most recent county to be created in California was Imperial County in 1907.

The southern portion of the County includes some of the wealthiest areas in the United States, among them the unincorporated community of Montecito,

noted for its expensive real estate and celebrity residents. This part of the County has a quaint feel to it, particularly in downtown Santa Barbara, owing to the predominance of Mission-style architecture, although areas further west are more urbanized. As a result of its aesthetic appeal, recreational opportuni-

This divide is so substantial that there have been two fairly recent attempts at creating a separate northern county, in 1978 and 2006.

ties, and year-round mild climate, southern Santa Barbara County is heavily engaged in the tourism sector, drawing thousands of visitors annually. The area is also home to one of the top public universities in the country, UC Santa Barbara.

However, due to the very high property values in this area, many of the people employed in southern Santa Barbara County, particularly in its hospitality and retail sectors, although increasingly professionals as well, cannot afford to live in the area and are instead looking to North County for its greater affordability. The northern portion of the County was long heavily engaged in oil extraction, but as the oil fields have been depleted, the other major economic drivers of the area — agriculture and Vandenberg Air Force Base — now predominate. The area's wineries and vineyards are a source of renown and local pride, although agriculture in the County is quite diversified. Like the southern part of the County, this area has its

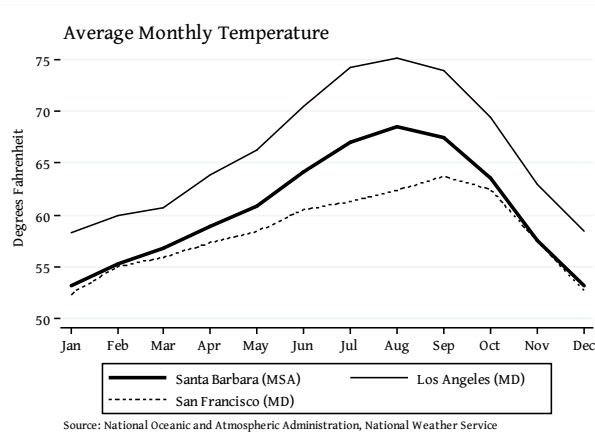
Pollution is of relatively little concern in the region. The county is not plagued by the air pollution common to Southern California...

tourist attractions, most notably the town of Solvang, which offers visitors a unique chance to experience some traditional Danish architecture and culture, but also the wine country itself and the historic Spanish missions.

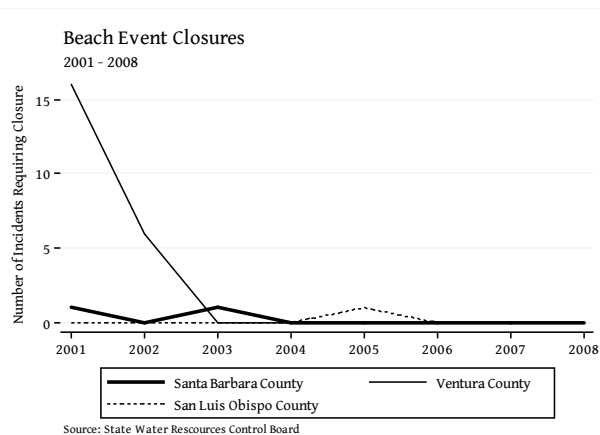
Environment

The local climate is typical of coastal areas of California, though summers tend to be milder than in counties further south and east. Average temperatures range from a low of roughly 53 °F in December and January, to a high of 68.5 °F in August. Of course, this is an average for the county, and the northern portion of the county tends to have much greater extremes than the southern cities.¹⁹

¹⁹MSA stands for Metropolitan Statistical Area; these areas are regional aggregations, commonly used by government agencies for statistical analyses. The Santa Barbara MSA encompasses all of Santa Barbara County.



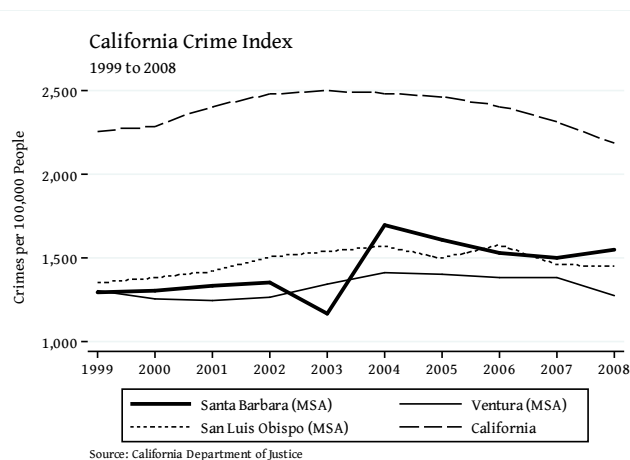
Pollution is of relatively little concern in the region. The county is not plagued by the air pollution common to Southern California counties, owing to generally favorable wind conditions. Although there were a couple of incidents earlier in the decade, beach closures, which are primarily precipitated by sanitary sewer overflows, have not occurred in Santa Barbara County since 2004. This is similar to the other counties in the Tri-County area, which have also mostly avoided beach closures in recent years, but again in sharp contrast to Southern California counties, as well as the Bay Area, where closures are commonplace.



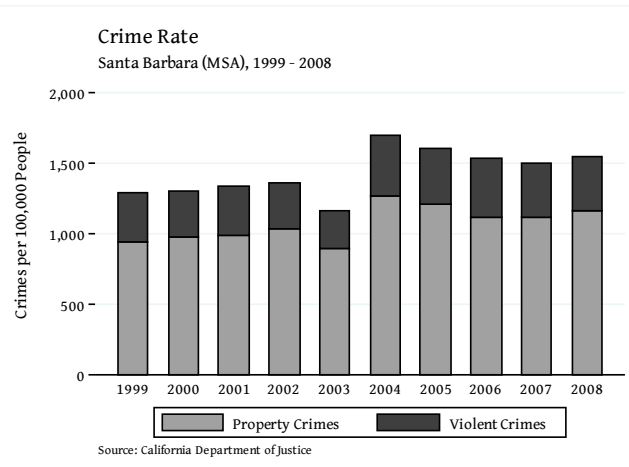
Crime

Although the Santa Barbara MSA enjoys much lower rates of crime than the California average, crime rates

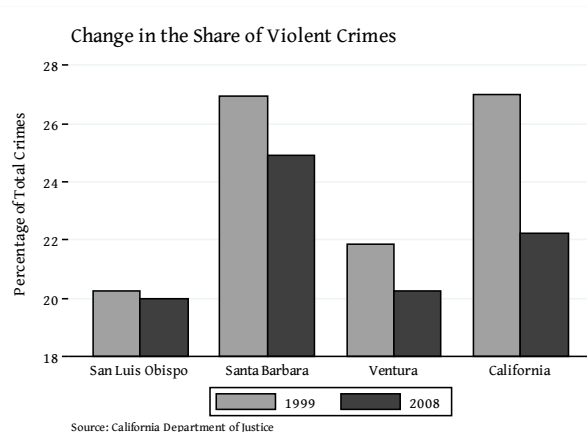
unfortunately shot up from their most recent low in 2004. While crime rates have been declining gradually since then, the county still saw roughly 335 more crimes per 100,000 residents in 2007 compared to 2003. In 2003, when crime rates were at their lowest, 1,165 crimes were committed per 100,000 persons; currently the figure is closer to 1,500.



While all crime has a negative impact on society, violent crimes take a particularly harsh toll on communities. A disconcerting attribute of crime trends in Santa Barbara County is that the share of violent crimes has been increasing. Since 2003, when property crimes has been increasing. Since 2003, when property crimes per 1,000 residents were at their lowest, the relative number of property crimes committed has increased by 24.4%. The fewest violent crimes were perpetrated that same year – the most recent trough year for overall crime – but fully 43.3% more (117 per 1,000 residents) were committed in 2007. Both rates have been declining, and the share of violent crime did fall slightly from 2006 to 2007, but it remains above historical levels. Nonetheless, Santa Barbara MSA experiences much less crime than California overall, with more than 800 fewer crimes committed per 100,000 residents and over 120 fewer violent crimes.



Violent crimes have been occurring at elevated levels since 2004, almost at the same rates as seen in the late 1990s, but they made up a larger proportion of the overall crime rate in 2007 than they did ten years prior. Violent crimes contributed almost 4 percentage points more to the overall number of crimes committed in 2007 when compared to 1997.



This is in sharp contrast to neighboring Ventura and San Luis Obispo counties, where the share of violent crime has declined substantially. In particular, San Luis Obispo went from having a higher share of violent crimes than Santa Barbara towards the end of the 1990s, to a lower share in recent years. Ventura County has always had lower crime rates, owing to the fact that its population is mostly located in suburban areas. California and most of its counties have seen greater declines, or at least smaller increases, in vio-

lent crimes than in property crimes, which is encouraging, as a reduction in violent crime tends to have a greater effect on quality of life.

The distribution of crimes across Santa Barbara County, and the underlying reasons therefore, are somewhat difficult to assess, given the fairly small number of incorporated places in the County and the very different attributes of the unincorporated communities. The very small populations of some cities can also skew crime rates.

Crime in Santa Barbara County by Area Rankings, 2007

City/Place	Crime Rates	
	Violent Crimes per 100,000 People	Property Crimes per 100,000 People
<i>South County</i>		
Santa Barbara	516.2	1,388.6
Carpinteria	204.4	788.3
Goleta	179.9	811.0
<i>North County</i>		
Santa Maria	704.9	1,727.3
Lompoc	672.6	964.3
Buellton	255.6	1,347.6
Solvang	232.7	950.3
Guadalupe	136.1	680.5
<i>Unincorporated</i>	145.5	709.5

Source: California Office of the Attorney General

According to broadly observable crime trends, the incidence of violent crimes tends to be higher in more urbanized, densely populated areas with lower average incomes and educational attainment levels, although occasionally this also occurs in rural areas. This trend appears to hold true for most of Santa Barbara County; the most populated areas see the greatest number of violent crimes, but Goleta, one of the larger cities in the County, clearly does not fall into this pattern. Note that there is a sharp drop in the rate of violent crimes between the three largest cities and the rest of the County.

Typically, the incidence of property crimes is highest in affluent, urban areas, but southern Santa Barbara, where most of the wealth is concentrated, has very low rates of property crimes, with the exception of the City of Santa Barbara. Arguably, the majority of Santa Barbara County is simply not sufficiently urbanized to

see a high occurrence of property crimes, which is by no means a negative attribute. The two largest cities, Santa Maria and Santa Barbara, have the highest rate of property crimes, but Buellton represents a significant outlier, likely driven by its small population.

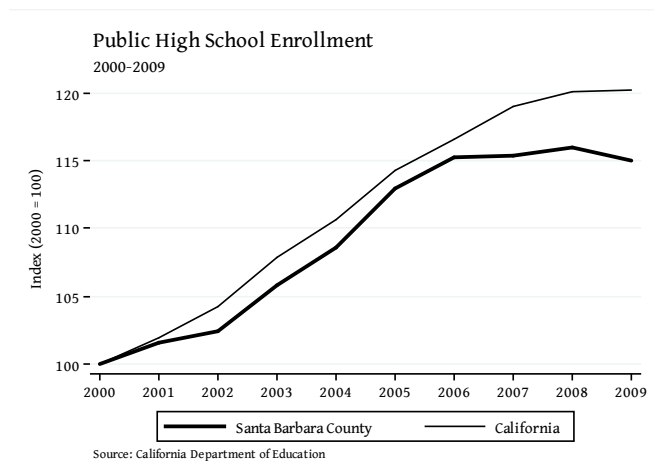
The distribution of crime does highlight some social differences between northern and southern Santa Barbara County: The safest areas, excluding the City of Santa Barbara itself, are in the south, while the incidence of crime is higher in the areas with lower incomes and lower educational attainment levels in the north. Interestingly, Santa Barbara and nearby San Luis Obispo counties both have essentially identical crime rates, but communities in San Luis Obispo

Santa Barbara and nearby San Luis Obispo counties both have essentially identical crime rates...

County all have fairly similar crime rates, while there is a significant disparity in the distribution of crime in Santa Barbara County. These two areas are roughly equally "safe" on average, but in San Luis Obispo, cities conform to this average, while Santa Barbara has communities at both extremes.

Education

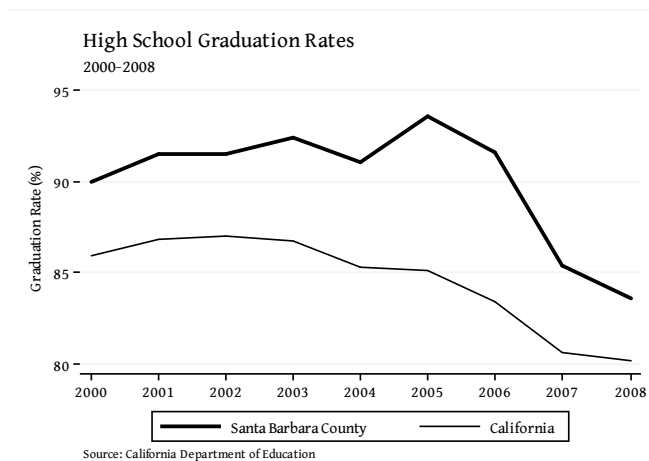
Santa Barbara County is home to a somewhat mixed public education system. Schools in the County are significantly outperforming the state by some measures, but underperforming on others. Public school enrollment in Santa Barbara County has been declining since 2005. Over the past four years, public school enrollment has fallen by 2.4%, which translates to roughly 410 fewer students enrolled per term. These declines were driven by a drop in elementary and middle school enrollment, at least up until 2008.



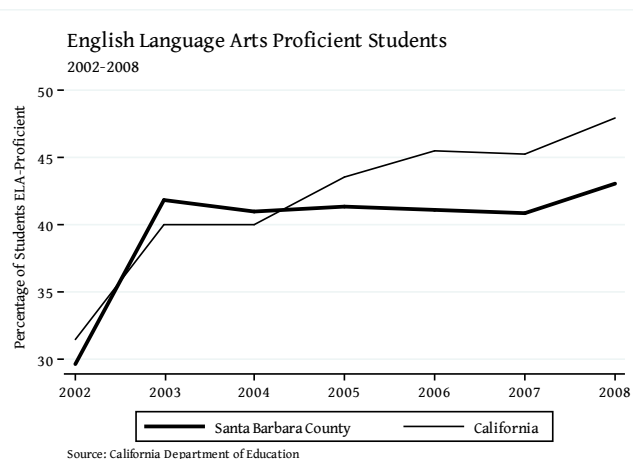
High school enrollment actually increased through 2008; the last school year is the first time high school enrollment has fallen this decade. Now, both overall enrollment and high school enrollment are declining, which may indicate declining numbers of school-aged children or an increase in the use of private schools. California has seen similar trends in total enrollment, but high school enrollment continues to grow. A

California has seen similar trends in total enrollment, but high school enrollment continues to grow.

closer look at enrollment by grade over time reveals that falling enrollment is indeed the result of fewer students enrolling, not an increase in the dropout rate.



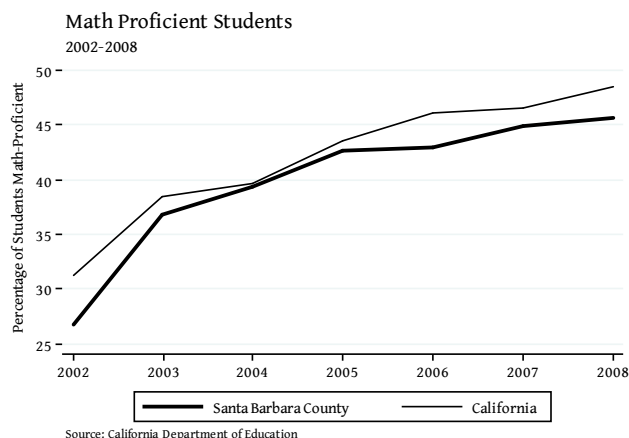
Graduation rates in Santa Barbara County, though still quite high, have been declining recently. Whereas in 2005 around 94% of seniors graduated, in 2008 only 84% of the graduating class received their diplomas.²⁰ Graduation rates are almost four percentage points higher in the County than at the state level, but they were close to nine percentage points higher in 2005, and they continue to converge.



Proficiency in English Language Arts and math have increased by about 14 and 21 percentage points, respectively, since 2002. However, virtually all the gains in English proficiency occurred from 2002 to 2003; proficiency levels have remained practically flat since

²⁰The methodology used by the Department of Education accounts for dropouts across all four years, and should accurately capture the share of a freshman class that graduated on time.

then, whereas math proficiency has been growing more consistently. Consequently, English proficiency has fallen below statewide rates and math proficiency continues to lag behind as well.



Standardized test scores are one measure by which the County is performing unequivocally well. Scores on both the verbal and the math section of the SAT are well above the state average and have consistently increased in recent years. Verbal scores in Santa Barbara County remain lower than those in San Luis Obispo County, but on average students now perform better than students in Ventura County.

Average SAT Verbal Scores, 2005-2008

County	2005	2006	2007	2008
Los Angeles	478	475	472	472
San Francisco	472	473	476	483
San Luis Obispo	538	534	535	538
Santa Barbara	523	520	517	529
Ventura	533	526	523	526
California	499	495	493	494

Source: California Department of Education

Santa Barbara County students are now on par with other Tri-County students on the math section of the SAT, as scores in the other two counties have declined slightly, while improving in Santa Barbara. As a result, Santa Barbara's average scores on the math and ver-

bal sections are 29 and 35 points higher, respectively, than California's, where average scores have fallen.

Average SAT Math Scores, 2005-2008

County	2005	2006	2007	2008
Los Angeles	503	495	492	490
San Francisco	530	531	528	536
San Luis Obispo	545	542	539	543
Santa Barbara	538	537	532	542
Ventura	550	542	540	543
California	521	516	513	513

Source: California Department of Education

The ranking of best- and worst-performing high school districts highlights some strengths of the public education system in the County, but also points to some serious concerns. None of the districts has a graduation rate below 85%, not an insignificant achievement in California. However, once proficiency rates are taken into account, significant disparities become apparent. Only one district, Santa Ynez Valley Union High, has strong proficiency rates. Santa Barbara High has a promising number of English proficient students, but the remaining districts all significantly underperform the state average. Math proficiency paints a more promising picture, as only two districts fall below the state average.

It is these two districts, Cuyama Joint Unified and Lompoc Unified, that are particularly disconcerting. Both districts have significantly above-average graduation rates, at 100% and 89.3%, respectively, but have dismal proficiency rates (34% to 43.9%). Given these statistics, well over half of graduates at these schools are not proficient in one subject, or both.

Santa Barbara County High School Districts, 2008

School District	Graduation Rate (%)	ELA Proficient (%)	Math Proficient (%)
Cuyama Joint Unified	100.0	34.0	38.9
Santa Ynez Valley Union High	96.9	78.8	75.8
Carpinteria Unified	94.3	46.8	53.5
Lompoc Unified	89.3	43.9	41.2
Santa Barbara High	88.1	61.5	52.8
Santa Maria Joint Union High	86.7	45.3	53.5

Source: California Department of Education

Annual Per Pupil Spending for School Districts in Santa Barbara (MSA), FY 2007-08

School District	Enrollment	ADA	Revenue per Student (\$)	Expend. per Student (\$)	Avg. Teacher Salary (\$)	Pupil-Teacher Ratio
<i>South Santa Barbara County</i>						
Carpinteria Unified	2,553	2,527	8,738	8,693	N/A	19.9
Santa Barbara High	7,038	N/A	N/A	N/A	N/A	26.0
<i>North Santa Barbara County</i>						
Cuyama Joint Unified	298	295	10,929	10,671	52,227	15.9
Lompoc Unified	10,551	10,088	8,323	8,543	64,912	21.3
Santa Maria Joint Union High	7,746	7,514	8,587	7,970	70,761	24.8
Santa Ynez Valley Union High	1,130	1,068	11,450	10,990	69,469	23.1
California Average District	5,977	N/A	9,115	8,830	65,808	20.9

Note: ADA stands for average daily attendance.

Source: Ed-Data

In analyzing per pupil expenditures, teacher compensation, and pupil-teacher ratios in Santa Barbara County, one observes significant disparities between districts, but a fairly weak correlation between these measures and academic performance. The conventional wisdom that higher expenditures, higher compensation, and lower pupil-teacher ratios produce better academic outcomes does not appear to hold true across the county. Looking at Santa Ynez Valley Union High, one might readily argue that increased revenues and expenditures per student have a strong positive impact on performance, but Cuyama Joint Unified undermines this reasoning, with its very low proficiency rates. Some school districts with below-average funding still outperform state averages. Overall, it appears that teacher compensation has the greatest correlation to academic performance, particularly proficiency rates, but Santa Maria Joint Union High does not conform to this trend, and given that two districts did not have this information, it is difficult to make a full evaluation. In combination, these measures appear to have a mild influence on graduation rates, but little bearing on other academic outcomes.

Of course, one cannot discuss education in the County without mentioning the University of California at Santa Barbara, one of the top public research universities in the nation. UC Santa Barbara ranks 42nd among national universities on *US News and World Re-*

...one cannot discuss education in the County without mentioning the University of California at Santa Barbara...

port's 2010 Best Colleges rankings. The university offers well over 100 undergraduate degree programs and more than 55 graduate degree programs, and boasts five Nobel Laureates among its faculty. With almost 22,000 students, the school contributes heavily to life in the County, bringing intellectual vitality and curiosity to the area, particularly in the community of Isla Vista, where most students reside.

Summary

Santa Barbara County offers its residents a high quality of life; however, it does entail a fairly high cost of living, and workers in the most desirable areas frequently commute significant distances. The cost of living is particularly high in the southern portion of the County; among the many contributors to the high cost of living are the area's exceptionally high property values. Consequently, the population has been shifting towards the northern part of the County, which has the appeal of being more affordable, but also has greater social challenges. Crime rates in the

County are well below the California average and the region is home to a moderately strong public education system. However, significant disparities exist within the County, as there are considerable differences in crime rates and educational performance throughout the region. Unfortunately, even

though Santa Barbara County still performs quite well by most measures, there have been only minor improvements recently in the area's quality of life. Given the current state of public finances, it seems unlikely that much will be done to better these measures in the near future, as funding for education and safety programs is cut.

Santa Barbara (MSA) Crime by Area, 2007 (Crimes per 100,000 Population)

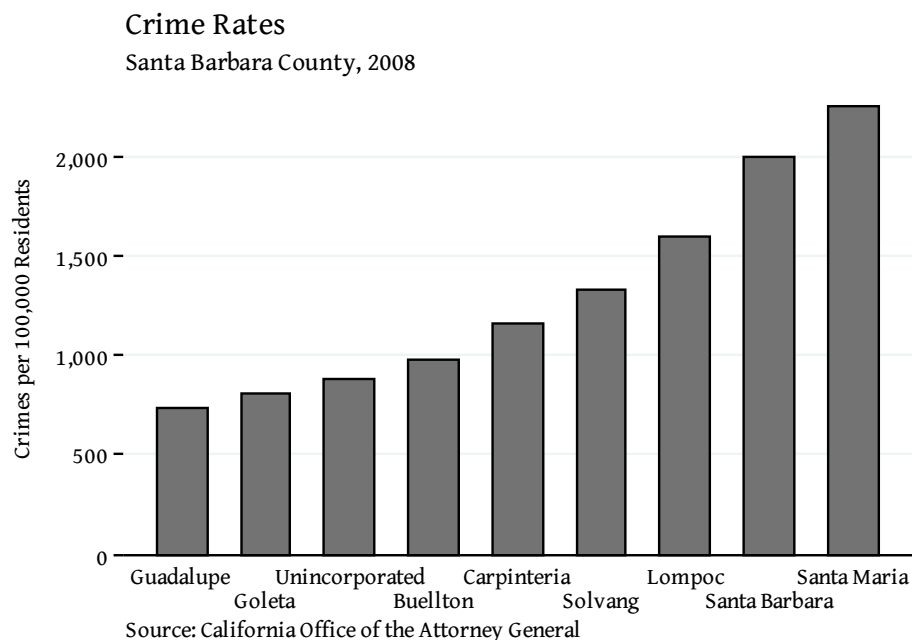
City/Place	Violent Crimes				Property Crimes			Arson
	Homicide	Rape	Robbery	Assault	Burglary	Car Theft	Larceny	
Buellton	0.0	64.0	0.0	42.7	426.7	42.7	405.4	21.3
Carpinteria	0.0	35.1	35.1	98.3	435.5	77.3	477.7	7.0
Goleta	0.0	6.6	19.8	52.8	339.7	66.0	323.2	3.3
Guadalupe	15.3	30.7	0.0	199.3	260.6	107.3	122.6	15.3
Lompoc	0.0	42.0	63.0	541.3	422.3	114.3	410.7	21.0
Santa Barbara	2.2	28.9	129.9	385.2	541.8	125.5	792.7	35.5
Santa Maria	9.9	62.7	110.0	501.8	581.0	539.2	452.3	20.9
Solvang	0.0	18.5	18.5	166.7	592.8	55.6	481.7	0.0
Unincorporated	1.4	13.4	23.2	82.4	400.9	5.6	360.0	13.4

Source: California Office of the Attorney General

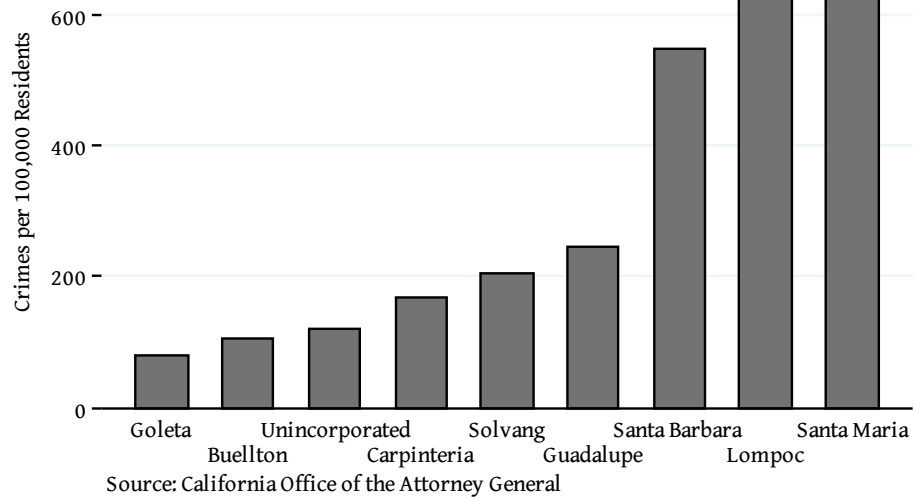
Santa Barbara (MSA) High School Districts, 2008

School District	High School Enrollment (# Students)	Graduation Rate (%)	ELA Proficiency (%)	Math Proficiency (%)
Carpinteria Unified	891	94.3	46.8	53.5
Cuyama Joint Unified	89	100.0	34.0	38.9
Lompoc Unified	3,289	89.3	43.9	41.2
Santa Barbara High	7,038	88.1	61.5	52.8
Santa Maria Joint Union High	7,746	86.7	45.3	53.5
Santa Ynez Valley Union High	1,130	96.9	78.8	75.8

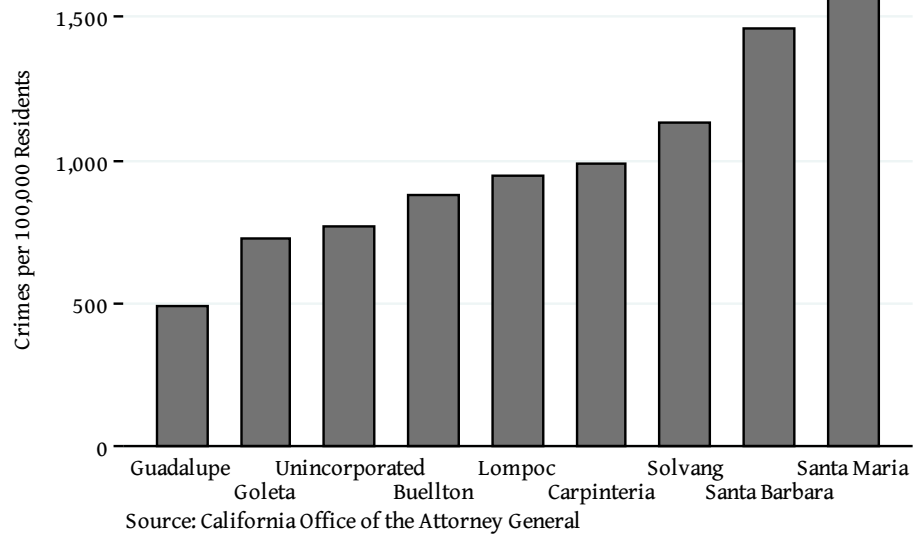
Source: California Department of Education



Violent Crime Rates Santa Barbara County, 2008



Property Crime Rates Santa Barbara County, 2008



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	Grubb & Ellis
California Air Resources Board	Hanley Wood Market Intelligence
California Association of Realtors	HousingTracker.net
California Board of Equalization	Marcus & Millichap
California Dept. of Education	Mortgage Bankers Association
California Dept. of Finance	National Science Foundation
California Dept. of Justice	NOAA National Weather Service
California Employment Development Dept.	Property & Portfolio Research
California New Car Dealers Association	RealFacts
California State Controller	Research and Development (RAND)
California State Franchise Tax Board	S&P Case Shiller
California State Legislative Analyst's Office	Texas Transportation Institute
CB Richard Ellis	U.S. Census Bureau, American Community Survey
Central Coast Major Listing Service	U.S. Census Bureau, Longitudinal Employment - Housing Dynamics
Construction Industry Research Board	U.S. Dept. of Commerce, Bureau of Economic Analysis
CoStarr/The London Group	U.S. Dept. of Labor, Bureau of Labor Statistics
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Federal Reserve Economic Data (FRED)	
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Acknowledgments

Beacon Economics Chapter Authors/Research Staff

Dr. Jon Haveman, Principal

Brad Kemp, Director of Regional Research

Jordan Levine, Senior Research Associate

Alexander Lin Beale, Research Associate

Riley Newman, Senior Research Associate

Dr. Christopher Thornberg, Principal

Eric Weitz, Information Specialist

Guest Authors

Matt Turrentine, Turrentine Brokerage

Patrick S. Duffy, MetroIntelligence Real Estate Advisors

Brian Johnson, Radius Group Commercial Real Estate

Bob Tuler, Radius Group Commercial Real Estate

Gene Deering, Radius Group Commercial Real Estate

Dawn Dyer, Dyer Sheehan Group Inc.

Steve McCarty, Stafford-McCarty Commercial Real Estate

Steve Davis, Stafford-McCarty Commercial Real Estate

Francois DeJohn, Hayes Commercial Group

Kris Roth, Hayes Commercial Group

Brian Bailey, Hayes Commercial Group

Steve Golis, Radius Group Commercial Real Estate

Daniel McGregor, Radius Group Commercial Real Estate

Document Format and Editing

Bettina Nicely Johnson, Copy Editor

Bob Kerstetter, LaTeX Consultant, Village Hiker Company

Cover Design

DAVIES

Print Production

Andre Rosenberg, Copyland Printers

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Contact

- | | |
|--|---|
| <ul style="list-style-type: none"> ■ Jon Haveman
Founding Principal
(415) 457-6006
Jon@BeaconEcon.com ■ Christopher Thornberg
Founding Principal
(310) 739-3286
Chris@BeaconEcon.com | <ul style="list-style-type: none"> ■ Victoria Pike Bond
Director of Communications
(415) 457-6030
Victoria@BeaconEcon.com |
|--|---|

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UC Santa Barbara Economic Forecast Project Staff

Llad Phillips

Acting Executive Director

Eric Sonquist

Director

Jane Donnellan

Director of Business Development & Marketing

Deb Owens

Business Officer

Susan Yamashiro

Event Coordinator

Research and Development Assistants

Eliza Chon

Jessica Cope

Vince Garcia



UC Santa Barbara Economic Forecast Project

Mail Code 3195 University of California

Santa Barbara, CA 93106-3195

(805) 893-5739

www.ucsb-efp.com



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