Board Elects Chevron VP as 2011 CalChamber Chair

S. Shariq Yosufzai, vice president of Chevron Corporation, has been elected 2011 chair of the California Chamber of Commerce Board of Directors. He succeeds Larree M. Renda, executive vice president, chief strategist and administrative officer for Safeway, Inc., Pleasanton, in the CalChamber’s top volunteer position.

“Creating the right climate for innovation and job creation is central to driving California’s recovery,” said Yosufzai. “As the 2011 CalChamber chair, I look forward to working alongside the new administration to enact sensible reforms that will restore economic growth.

“Governor-Elect Brown brings a reputation for fiscal discipline and has focused on a number of critical priorities for job creators including: streamlining regulation, reforming budget negotiations, cutting spending, improving permitting and reining-in irresponsible policies in the pension system.”

Willie Brown Comments on California Politics

Willie Brown, the longest-serving Assembly speaker and former mayor of San Francisco, offers insights on the state political scene, the November election results and anecdotes from his four decades of involvement in public policy at the dinner gathering of the CalChamber Board of Directors on December 2 in San Francisco. More photos on Page 3.

U.S.-Korea Trade Agreement Closer to Passing

On December 3, the United States and South Korea announced the successful resolution of the outstanding issues with the U.S.-Korea Free Trade Agreement (FTA), setting the stage for consideration of the agreement by Congress in the coming months.

In announcing the agreement, President Barack Obama commented, “American manufacturers of cars and trucks will gain more access to the Korean market and a level playing field to take advantage of that access. We are strengthening our ability to create and defend manufacturing jobs in the United States; increasing exports of agricultural products for American farmers and ranchers; and opening Korea’s services market to American companies. High standards for the protection of workers’ rights and the environment make this a model for future trade agreements, which must be both free and fair.”

The FTA was signed on June 30, 2007, but has yet to be approved by the U.S. Congress. Since that time, South Korea has successfully concluded an FTA with the European Union and is in advanced FTA negotiations with Canada. This increased competition from countries...
12:30 p.m. actually punches out at 12:07 and punches in at 12:25. The rounded time is 30 minutes while the actual time is 18 minutes. This is a violation of Labor Code Section 226.7(a) and penalties are assessed under Section 226.7 (b).

A full 30 minutes must be given; a de minimis argument on a minute or two may be accepted, but the strong recommendation is that the full 30 minutes be taken.

The de minimis policy of the State Labor Commissioner is covered in opinion letter 1995.06.02. This gives some guidance, but the issue is fact-driven and would require further investigation before a final determination is made. A full 30-minute meal period should always be taken.

Rounding of time to the nearest 5 minutes, or to the nearest one-tenth or quarter of an hour has been used in industry prior to calculators and computers. This was primarily for ease of recordkeeping, and allowed by both state and federal authorities with the full understanding that employees be compensated for all the time they actually work.

Generally, this means consistency in all punches, including in and out for meal periods, and that over a period of time, the employee will be paid for all the time worked. For employers who give 30-minute meal periods, supervisors should be aware of the requirement that employees take the full 30 minutes and ensure that employees do so.

Rounding to the nearest quarter of an hour can be used, but the actual punch should be when starting and stopping work. Employees who come in early on their own should not punch in before the starting time. Supervisors should check time cards frequently for accurate time reporting.

The Labor Law Helpline is a service to California Chamber of Commerce preferred and executive members. For expert explanations of labor laws and Cal/OSHA regulations, not legal counsel for specific situations, call (800) 348-2262, or submit your question at www.hrcalifornia.com.

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Business Resources
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International Trade


Labor Law

Next Alert: January 7, 2011
CalChamber Board Meeting

Speakers Cover U.S., State Policy, Politics

Alan Mulally, president and CEO of Ford Motor Company, describes for the CalChamber Board of Directors his experiences since joining Ford in September 2006. Seated are 2010 CalChamber Chair Larree Renda of Safeway, Inc., and Second Vice Chair Timothy S. Dubois of The Edward Thomas Companies.

Longtime campaign consultants Gale Kaufman, Kaufman Campaign Consultants, and Rick Claussen, Goddard Claussen West, present perspectives on what happened in the November elections to the CalChamber Board of Directors.

Ro Khanna (left), deputy assistant secretary at the U.S. Department of Commerce, covers the post-election outlook for U.S. international trade policies at a December 3 international breakfast forum presented by the CalChamber Council for International Trade, chaired by Susan Corrales-Diaz (right).
Board Elects Chevron VP as 2011 CalChamber Chair

From Page 1

“The CalChamber is committed to a positive, constructive relationship with the new administration and we will be at the table ready to work as a dependable partner. Together, I’m confident that we can get California growing again.

“We have great people and talented entrepreneurs. We need to empower them with a positive business climate. When that happens, I’m confident that California will begin retaking its position as an international economic leader.”

Serving with Yosufzai as 2011 officers of the CalChamber Board are:

● First Vice Chair Timothy S. Dubois, president, The Edward Thomas Companies, Beverly Hills;

● Second Vice Chair Frederick E. Hitchcock, chairman and chief executive officer, Hitchcock Automotive Resources, City of Industry; and

● Third Vice Chair Anne Buettner, senior vice president, corporate tax, The Walt Disney Company, Burbank.

S. Shariq Yosufzai

In his role at Chevron, which has its headquarters in San Ramon, Yosufzai supports Chevron’s chief executive officer and chairman on the National Petroleum Council Future Transportation Fuels Study as chair of the Chevron-led Supply & Infrastructure Task Group, and as decision executive on Downstream Portfolio Projects worldwide.

Yosufzai graduated with a bachelor’s degree in chemical engineering from Texas A&M University. He joined Texaco in 1975 as a process engineer at the Port Arthur, Texas, refinery. After serving in a number of positions of increasing responsibility, he was named president of Texaco Lubricants Company in 1994 and later served on the management committee of Star Enterprise.

In 1998, Yosufzai was appointed vice president of Caltex Petroleum Corporation with geographic responsibility for Africa. In 1999, he was named corporate vice president of Caltex Corporation and president of Caltex Lubricants & New Business Development, responsible for the global lubricants business, and for activities encompassing all businesses in China, India, Vietnam, Sri Lanka and Indonesia. He was also chairman of Caltex Lubricants Lanka Ltd. and a board member of Caltex Australia Ltd., both publicly traded companies.

Yosufzai was named president, Global Lubricants, upon the formation of ChevronTexaco in October 2001. In that role, he was responsible for the manufacturing, blending, sales and marketing of base oils, lubricants and coolants to customers worldwide.

In July 2003, Yosufzai assumed the responsibility of co-leading Chevron Products Company, responsible for Chevron’s North America Refining and Marketing Operations. From January 2004 until April 2010, he served as president, Chevron Global Marketing, where he was responsible for leading Chevron’s fuels marketing, commercial and industrial marketing, and convenience retailing operations across 90 countries and three world class brands, including Chevron, Texaco and Caltex.

Yosufzai was elected a Fellow of the American Institute of Chemical Engineers (AIChE) in 2002 and received the inaugural Industry Leadership award in 2010. Yosufzai was named Lubricants World magazine’s “Person of the Year” in 1996. In 1999, he was named both the Outstanding International Alumnus and a Distinguished Alumnus of Texas A&M University.

He is chair of the board of directors of The Association Former Students of Texas A&M University and is an executive committee member of the San Francisco Opera’s Board of Directors. Previously he served as chair of the Societal Impact Operating Council of AIChE, and on the boards of the Houston Grand Opera, Jesse H. Jones School of Business at Texas Southern University, the Chick-Fil-A Peach Bowl in Atlanta, Junior Achievement of Southeast Texas Inc., the Greater Houston Area Recycling Council and the College of Science at Texas A&M University.

Executive Committee

The CalChamber Executive Committee also named its two at-large members. Serving in the one-year rotating position will be:

● Jerry J. Carnahan, executive vice president, field operations, Farmers Insurance, Los Angeles; and

● Joseph M. Otting, president and chief executive officer, OneWest Bank, FSB, Pasadena.

In addition to the at-large members and current officers, the Executive Committee includes the last three Board chairs. The Executive Committee works with the CalChamber’s top management to determine policy, financial and program direction, including, when necessary, providing policy guidance between the Board’s regular quarterly meetings.

Staff Contact: Dave Kilby
Greenhouse Gas Emission Requirement for Refrigerants to Take Effect January 1

Certain facilities with stationary, non-residential refrigeration systems will become subject to new requirements on January 1, 2011. The rules are among “early action measures” approved by the California Air Resources Board (ARB) to implement AB 32, the Global Warming Solutions Act of 2006. AB 32 requires that greenhouse gas (GHG) emissions be reduced to 1990 levels by 2020.

2011 Regulation

The regulations, part of the Refrigerant Management Program (RMP), require that facilities with stationary non-residential refrigeration systems with more than 50 pounds of a high-global warming potential (GWP) refrigerant begin leak detection inspections, repair and recordkeeping.

Refrigerant distributors, wholesalers and reclaimers also are required to begin recordkeeping, and are prohibited from selling, purchasing or disposing high-GWP refrigerants.

Servicing technicians will be required to be certified by the U.S. Environmental Protection Agency (EPA) and cylinders will need to be properly evacuated before disposal.

Businesses Affected

The ARB estimates that approximately 64 percent of the facilities potentially affected by the 2011 RMP requirements are small businesses.

Primary Impact

These regulations will primarily affect businesses that have refrigeration systems with more than 50 pounds of high-GWP refrigerant. These businesses typically include:

- Supermarkets and large grocery stores;
- Food and beverage processors;
- Cold-storage warehouses; and
- Facilities using industrial-process cooling.

Generally Not Affected

Business that generally do not have these types of refrigeration systems are:

- Bars and restaurants;
- Gas stations;
- Liquor stores; and
- Office buildings.

Potential Benefits

The ARB predicts the regulations also will lead to cost savings for businesses. According to ARB, the regulations will reduce high-GWP emissions by 8 million metric tonnes of carbon dioxide equivalent, the equivalent of removing 1.4 million cars and light trucks from the road each year.

As a direct result of reduced refrigerant consumption, the ARB estimates a cost savings of $2 per metric tonne of carbon dioxide equivalent in emissions reduced.

Future Deadlines

For the next six years, other businesses will become subject to the refrigerant management program, depending on the largest refrigeration system used at a facility.

Beginning January 1, 2012:

- Facilities with large refrigeration systems of 2,000 pounds or greater of high-GWP refrigerant are required to register with the ARB, submit an annual report and pay annual fees;
- Distributors, wholesalers and reclaimers must report annually.

Beginning January 1, 2014:

- Facilities with medium refrigeration systems with greater than or equal to 200 pounds, but less than 2,000 pounds, of high-GWP refrigerant must register, submit an annual report, and pay annual fees.

Businesses Affected

- Supermarkets and large grocery stores
- Food and beverage processors
- Cold-storage warehouses
- Facilities using industrial-process cooling

Source: California Air Resources Board

Beginning January 1, 2016:

- Facilities with small refrigeration systems with greater than 50 pounds, but less than 200 pounds, of high-GWP refrigerant must register.

Refrigerant Management Program

The RMP establishes regulations for refrigerant leak detection and monitoring, leak repair, system retirement and retrofitting, reporting and recordkeeping, and proper refrigerant cylinder use, sale and disposal.

ARB reports the program is designed to complement U.S. EPA and South Coast Air Quality Management District regulations and better control emissions of ozone-depleting substances and substitute refrigerants.

More Information

High-GWP refrigerants include chlorofluorocarbons (CFC), hydrochlorofluorocarbons (HCFC) and hydrofluorocarbons (HFC) refrigerants. Ammonia and carbon dioxide refrigerants are not high-GWP.

To determine the refrigerant charge of a refrigeration system, businesses should contact the manufacturer of the system or their refrigeration system service provider.

For further information regarding AB 32, visit www.arb.ca.gov.
High Court Leaves in Place Decision Weakening Workers’ Comp Reform

The California Supreme Court has turned down a request to review a crucial workers’ compensation case relating to how physicians determine how impaired an injured worker is. The state high court denied a petition to review Milpitas Unified School District v. Workers’ Compensation Appeals Board (WCAB) and Joyce Guzman.

The effect is to weaken the 2004 workers’ compensation reforms enacted to make the calculation of permanent disability (PD) awards more objective.

Background

In February 2009, the WCAB ruled in the Guzman case that the American Medical Association (AMA) guidelines for determining PD can be rebutted. Essentially, in cases of rebuttal, a physician may assess an injured worker’s whole person impairment (WPI) based on any chapter of the AMA guidelines, rather than solely on the chapter related to the injured body part.

In an attempt to overturn Guzman, the California Chamber of Commerce filed a friend-of-the-court brief in 2009, arguing that the Guzman ruling circumvents the Legislature’s 2004 mandate establishing a consistent and concrete method of calculating PD.

Allowing physicians to pick and choose which chapters of the AMA guidelines to use when rating a WPI, the CalChamber argued, opens the door to subjectivity, inconsistencies and immeasurable factors. Consequently, employees in similar situations may not be treated equally and fairly, as the WPI calculations will differ depending on the physician’s assessment.

In August 2009, the 6th District Court of Appeal sustained the WCAB approach, emphasizing that in special and complex circumstances, physicians need to be able to have some flexibility in describing impairment.

The court also required that a rebuttal of the AMA guidelines would necessitate substantial evidence, not solely a physician’s opinion. The court added that medical opinions should not be applied routinely.

The CalChamber pointed out that the 2004 reforms already addressed all the court’s concerns. The reforms, the CalChamber argued, defined each element used in a PD calculation with objective and measurable factors. Altering the reforms allows inconsistency and biased findings.

“Maintaining the board’s decision will result in burdensome litigation, inconsistent ratings…and ‘doctor shopping,’” the CalChamber said in its friend-of-the-court brief. “[The AMA guides will become] irrelevant whenever an evaluating physician and/or the Workers’ Compensation Judge disagrees with the result.”

Related Case

Although the Supreme Court declined to review Guzman, the 5th District Court of Appeal may consider similar issues in a related case, Almaraz. If the 5th District Court disagrees with the 6th District Court, the conflict will need to be resolved by the Supreme Court.

Staff Contact: Erika Frank

U.S.-Korea Trade Agreement Closer to Passing; Action Needed

From Page 1 around the world threatens the economic benefit the United States and California stand to gain from exports to the Asian country.

In fact, it is estimated by the Trade Partnership Worldwide, LLC, that the failure to approve the U.S.-Korea FTA will result in a U.S. goods export loss of $35 billion, gross domestic product (GDP) loss of $40 billion and an employment loss of 345,000. The economic damage would be similar in California, with a goods export loss of $2.5 billion, GDP loss of $5.2 billion and an employment loss of nearly 40,000.

According to the U.S. International Trade Commission, implementing the FTA will boost the U.S. GDP by nearly $12 billion and generate nearly $11 billion in U.S. merchandise exports. It would generate an additional boost to U.S. exports to other countries of more than $5 billion.

A recent U.S. Chamber of Commerce study found that 345,000 American workers stand to lose their jobs if the agreement is not implemented while other countries’ FTAs with Korea enter into force.

Benefits

Korea is a significant market for U.S. small and medium-sized companies, which make up a majority of U.S. businesses exporting to Korea. Passage of the U.S.-Korea FTA will eliminate tariffs and other barriers to trade in goods and services, promote economic growth, enhance trade between the United States and Korea, and help expand market access in Korea for U.S. farmers, manufacturers, service providers and financial services firms.

In 2009, California exported $5.9 billion to Korea, making it the state’s fifth largest export market. Korea is a $1 trillion economy and is the United States’ eighth largest goods trading partner. Korea’s commercial relationship with the United States is largely complementary. In 2009, two-way trade between the two countries topped $69 billion. In 2009, U.S. goods exports to Korea were $28.6 billion, a slight decrease from the previous year.

Under the FTA, more than half of current U.S. agricultural exports to Korea will become duty-free immediately, including high-value agricultural products such as almonds, pistachios, wine and cherries. For many other key agricultural goods, such as pork and citrus products, the FTA will provide unparalleled access to the South Korean market and its prosperous consumer base.

Action Needed

The CalChamber is urging members of the business community to contact California congressional representatives and urge support for the U.S.-Korea FTA.

For further information, visit www.calchamber.com/korea.

Staff Contact: Susanne Stirling
California Economy Begins Modest Upturn; Activity Level Still Low, Uncertainty High

U.S. Economic Upturn Continues

Many economic statistics for the nation improved during the past three months, though not all. Reflecting the underlying trends, the government’s preliminary estimate of gross domestic product (GDP) in the second quarter came in at a +2 percent annual rate, after a +1.7 percent uptick in the second quarter.

Progress was fairly widespread in the third quarter, though growth overall was moderate. Consumer spending, business investment in plant, equipment and software, federal government spending, and exports all increased. Collectively they contributed +5.4 percentage points to third-quarter GDP growth.

Private-sector inventories jumped by $115 billion last quarter, which had the effect of adding +1.4 percentage points to the economy’s growth rate. However, on the downside, imports soared, slicing -2.6 percentage points from GDP growth in the third quarter and residential investment slid, pulling GDP growth down by -0.8 percentage points.

Growth

Final domestic demand (which includes spending by U.S. consumers, business firms and all levels of government, but excludes changes in inventories and net exports) was up by +2.1 percent last quarter compared with third quarter 2009. This increase was the largest since late 2006 and marked the economy’s fifth quarter of growth after six quarters of downturn.

Labor market conditions showed little improvement during the third quarter. Non-farm payroll employment across the nation turned up early in 2010, rising by a million jobs between December 2009 and May 2010. However, employment declined by -393,000 jobs during the next four months, bringing the net gain in employment through September down to +613,000 jobs.

Much of this volatility was created by the federal government’s hiring—and then firing—of temporary workers for the 2010 Census. Meanwhile, the nation’s unemployment rate, which peaked at 10.1 percent in October 2009, edged down to 9.6 percent by September 2010.

Consumer Confidence Weak

Not surprisingly, consumer sentiment continues at very low levels. Weak consumer confidence reflects persistent anxiety about the personal impact of the recession against a backdrop of poor labor market conditions.

Other economic indicators recorded gains in the third quarter but at a slower rate of growth. Industrial production grew by +1.2 percent in the third quarter, somewhat slower than the second quarter pace of +1.7 percent. Similarly, the value of shipments by U.S. manufacturers flattened out after April, following three solid quarterly increases. Growth in retail and food service sales also ebbed during the third quarter.

Recent trends on the inflation front have continued generally favorable except for energy. Excluding food and energy, consumer inflation rates are running around 1 percent. Crude oil prices, while volatile, have fluctuated in the $75-$85 a barrel range, drifting higher in early November. In California, regular gasoline is hovering around $3.10 a gallon, up a bit from the first six months of the year.

Concerns grew about the pace of the recovery during the summer quarter. The California Chamber of Commerce Economic Advisory Council applauds the continued improvement in economic activity, but remains wary about the underlying, fundamental strength of the economy once the impacts of expansionary monetary policy and federal stimulus programs begin to wind down. In addition, other recoveries in the past were slowed by financial industry restructuring. Some caution still seems appropriate.

Interest Rates and Financial Markets

The Federal Reserve’s main concern continues to be low levels of resource utilization (i.e., high unemployment rates and low capacity utilization). With the economy growing more slowly than the Fed previously expected and inflation at minimal levels, the Federal Open Market Committee (FOMC) feels no need to raise short-term rates from current rock-bottom levels.

At its August meeting, the FOMC decided to tackle long-term interest rates by recycling principal repayments from its huge mortgage-backed securities portfolio into long-term U.S. Treasury securities. The committee took more steps at its November meeting, announcing plans to purchase up to $600 billion in additional Treasury securities through June 2011.

Long-term interest rates, already low, sank even further in response to the news. Meanwhile, with corporate bond spreads quite narrow, firms possessing both high and low credit ratings have rushed to issue large volumes of new debt. Also, more and more homeowners—at least those with good credit and equity in their homes—are refinancing mortgages.

Outside of the capital markets, however, credit conditions for less-than-prime-quality households and small to midsize business firms still remain tight.
California Economy Begins Modest Upturn; Uncertainty High

From Previous Page

Many of these firms face strict credit quality constraints when they apply for new or renewal business loans from commercial banks.

A large number of locally oriented and community banks are wrestling with delinquency problems, and consequently are reluctant to take on additional risks. It’s no surprise that commercial banks’ loan balances continue to decrease. The Advisory Council’s prognosis: the capital markets have improved significantly, but it remains unclear when the central bank will be able to return to traditional policymaking.

California Economic Signs Mixed

California’s economy saw few positive signs during the past quarter. The state lost an estimated -1.4 million farm and non-farm jobs during 2008 and 2009, a most distressing figure. The upturn to date in 2010 has been modest at best. Some 90,300 new jobs appeared between December 2009 and May 2010, but 97,200 jobs disappeared between May and September, leaving a net loss of -6,900 jobs over the first nine months of the year.

Most of the losses were government jobs, as the federal government slashed its Census 2010 workforce and school districts and cities reduced headcount. Meanwhile, California’s unemployment rate continued at 12.4 percent during third quarter 2010, compared with 12 percent a year earlier. Joblessness has been at or above 12 percent since August 2009; these rates were the highest since before World War II.

Other Indicators

Other broad-based indicators paint a somewhat less gloomy picture. Personal income earned in California increased by 2.3 percent during second quarter 2010 compared to second quarter 2009 (latest data available). A moderate increase, this marked only the second uptick in personal income since third quarter 2008.

Problems in the state’s construction, state/local government and finance/real estate sectors accounted for much of the drag on the state’s earnings growth. On the plus side, personal income increased in farming, mining, health care and private education [Note that the personal income figures are subject to revision].

Taxable sales sagged during the recession, plunging by -15 percent during 2009. However, here too the year-to-year comparisons turned positive during the first and second quarters of 2010, another sign of progress. Although data are still incomplete, sales declines during the recession were most severe for California’s motor vehicle dealers, furniture stores and building materials dealers. However, automotive sales have led the 2010 upturn to date, with unit sales through July up nearly 20 percent over the first seven months of 2009.

Budget Caution

Reflecting the changing economic momentum, tax receipts came into the General Fund a little better than expected during the early part of fiscal year 2011 (which ends June 2011). However, the estimated budget gap for the fiscal year was estimated at $18 billion-$19 billion. Some caution about the budget situation seems to be warranted despite changes in personnel at the top levels of government.

While employment may be near bottom in California, the state still lost a total of ~62,100 non-farm jobs over the 12 months to September, with key industries still reporting negative results.

Still, seven sectors recorded year-over gains, including administrative services; professional, scientific and technical services; private education; finance and insurance; health care; and leisure and hospitality.

Nine sectors reported employment declines. Job counts fell the most in California’s construction, government, wholesale trade, manufacturing and retail trade sectors.

Exports Up

International trade has picked up very strongly in 2010. Exports of goods made in California jumped by +19.7 percent in the third quarter of 2010 compared with the third quarter of 2009.

The largest category of exports—computers and electronic products (semiconductors, computer equipment and navigational instruments)—rose by +25.6 percent. Exports of California’s second largest export products—industrial machinery—leapt by +47.3 percent, the biggest gain of the top five export product groups.

Meanwhile, exports of transportation equipment climbed by +10.2 percent versus the same quarter last year and exports of miscellaneous manufactured commodities (including medical equipment and supplies) rose by +22.5 percent. Exports of chemicals (including pharmaceuticals) advanced by +5.6 percent.

Employment

Two of the state’s major metro areas reported year-to-year gains in non-farm employment in the year to September, while the others recorded smaller rates of declines than in previous quarters.

Job gains were positive for Orange County (+1 percent over the year) and
California Economy Begins Modest Upturn; Uncertainty High

From Previous Page

the San Jose metro area (+0.8 percent). Among the other areas, employment declined the least in San Diego (-0.4 percent). Job losses were moderate in two areas of Southern California—Los Angeles (-1 percent) and Ventura County (-1.1 percent), followed by Bakersfield, San Francisco and Modesto (at -1.4 percent, -1.4 percent and -1.5 percent respectively). Riverside-San Bernardino and Fresno (both -1.6 percent) were close behind. The Stockton, Oakland and Sacramento metro areas recorded the deepest declines (of -2.1 percent, -2.2 percent and -2.7 percent respectively).

Bay Area employment declined overall during the third quarter compared with the previous quarter. Job losses were bigger in the San Francisco and Oakland areas than in the San Jose metro area (using seasonally adjusted figures for all areas).

Compared with last year, construction activity has fallen around the Bay, with job counts down by -10 percent (in the East Bay area) to -7 percent (San Francisco and San Jose areas).

Manufacturing job losses were still a problem in the Oakland area. However, the high tech sector provided a bright spot, especially in San Jose. Travel and tourism indicators looked better this year, with higher international and domestic passenger traffic through San Francisco International Airport.

Also, hotel occupancies were up around the Bay and room rates moved up slightly. However, local schools and city governments reduced employee counts, a drag on the regional economy.

Non-farm employment decreased across Southern California during the third quarter (on a seasonally adjusted basis). Compared with 2009, the downturns were most pronounced in construction and government (local schools and city governments again) combined with some manufacturing, and retail industry distress.

Trade Flows

International trade flows through the area’s ports have turned up strongly, with both exports and imports on the rise. The change has had an impact, not just on the ports themselves, but also the transportation network, wholesale trade, and the distribution centers of Los Angeles, Orange County and the Inland Empire.

The region’s entertainment sector looks markedly better this year, with local filming activity on the rise. The Southern California tourism sector also is making progress, with hotel occupancies up (though room rates are still mostly down). Aerospace firms are stable for the moment.

However, new Department of Defense proposals for the 2011 fiscal year and forward include procurement declines in several programs of regional interest, which could have a negative impact on the region’s key aerospace industry.

Agriculture and Resources

California’s agriculture sector is improving in 2010 after a difficult 2009. Prices of several products have risen, including oranges, nuts and tree fruits (except peaches). Demand for premium California grapes continues to be soft, but prices for bulk wines and raisins increased.

California-grown agricultural exports increased by +17 percent in the first nine months of 2010 compared with 2009. Feed costs are rising again, driven by higher wheat and corn prices. Water availability for California farms is better this year after severe shortages last year.

Although the situation eased this year, water continues to be a concern in California. Precipitation was decent in 2010 and runoff was nearly normal after a string of dry years. Storage levels have recovered at many in-state reservoirs, but reservoirs along the Colorado River are still at very low levels.

The State Water Project and the Central Valley Project both increased water deliveries in 2010. However, the supply of water that must transit the Delta is still at risk due to actual and threatened pumping cutbacks to protect native species of fish. These problems won’t be solved soon.

The supply of electricity in California should be more than adequate in the near term, as capacity has grown in the last two years and industrial demand will take some time to recover from the recession. Electricity prices might be moving down in the next year, as natural gas prices have fallen and many of the power contracts signed by the state during the energy crisis are unwinding.

On the other hand, the state’s utilities face increased costs associated with mandated investments to reduce their environmental footprints and to improve their distribution networks. This suggests prices will be stable at best and could even rise.

Real Estate and Construction

Existing home sales in California were quite healthy between late 2008 and the first half of 2010, but sales dropped below the 500,000 transactions pace (annual rate) in the third quarter. Here are some recent statistics for the state’s resale home market:

- Existing single-family homes sales in California decreased by -12.2 percent over the year to September 2010, and condo sales were down by -14.8 percent.
- Prices have risen from early 2009 levels in most areas of the state. Statewide, the median price of single-family homes sold in September 2010 (at $309,900) was up by +4.5 percent compared with September 2009.
- The number of homes available

See California: Next Page
California Economy Begins Modest Upturn; Uncertainty High

From Previous Page

for sale represented 6.2 months supply (at September’s sales rate) compared with 4.2 months a year earlier.

The housing market’s performance in the third quarter reflected a number of countervailing forces. On the one hand, mortgage rates continued to be low, despite the March cessation of the Federal Reserve’s purchase program in the secondary mortgage market.

Also, at current transaction prices, many home sales in California fall inside the government housing agencies’ conforming loan limits (up to $729,750 in 2010), which increases the availability of mortgage loans to well-qualified buyers.

However, the federal government’s temporary tax credit program ended as of May. Worse yet, the tax incentives apparently pulled a number of purchases forward in time, as home sales declined markedly in June and July, after the incentives expired.

Existing Home Sales

While sales volumes stabilized in August and September, the outlook for existing home sales is uncertain. Demand for homes appears to have bottomed for the near term at least.

On the supply side, however, mortgage foreclosures continued relatively high during the third quarter, though the figures were below 2009 levels. Temporary foreclosure delays complicate the picture even more.

The big question is: when will lenders bring their distressed homes onto the market and in what volumes? Aside from foreclosures, significant further improvement in the pace of sales seem unlikely until the economy—and buyers’ confidence—begin to revive more strongly.

Residential construction continued at very low levels across the state during third quarter 2010. Total housing permits were issued at a preliminary annual rate of 40,500 units during third quarter 2010, about the same as in the second quarter but 14 percent greater than the third quarter 2009 pace of 35,600 (annual rate) units.

However, summer 2010 marked the third quarter of decline in single family detached permits from the recent fourth quarter peak (which had been elevated by builders’ efforts to attract buyers using the first round of federal tax credits). Single-family permits at 21,600 units (annual rate) were at the lowest levels since early 2009, the cycle low point.

Meanwhile, multi-family permits nearly doubled to 18,900 (annual rate), fully 98 percent above the third quarter 2009 pace. The overall improvement seen thus far in 2010 is certainly welcome, but the current construction pace still represents a drastic decline of -83 percent from the peak permit level of 2004 (213,000 homes).

The near-term outlook for new home construction is just as uncertain as that for existing homes. Tax credits have expired and builders must work through any excess inventory built up earlier in the year that remains unsold. The more optimistic industry observers don’t expect a significant upturn in new home construction before next year, while the pessimists worry that substantial improvement might take several years.

Commercial Real Estate

California’s commercial real estate markets declined drastically during the recession. Vacancy rates increased, asking rents dropped and external development funding virtually disappeared. The situation was most problematic for retail, office and industrial space. With most lenders unwilling to commit new funds for commercial real estate development, construction of new commercial space plunged. In 2010, the volume of transactions has turned up, though the level of activity remains muted compared to the pre-recession period.

Demand for office space continued to be slow in the third quarter, reflecting continued weak employment trends in office-based industries. Many firms are still reluctant to hire new workers, and are vacating or subleasing excess space.

Office vacancy rates continued high in most California metro areas during the third quarter.

- In the Inland Empire, office vacancy rates edged up to 23.9 percent from 23.7 percent the previous quarter.
- Orange County’s vacancy rate eased to 20.7 percent in third quarter 2010 from 21 percent.
- In Sacramento, the average office vacancy rate ticked up to 20.5 percent in third quarter 2010, just above San Diego County’s 19.5 percent rate.
- Silicon Valley saw its vacancy rate dip to 18.3 percent.
- In Oakland, the average vacancy rate moved up to 17.9 percent in third quarter 2010 from 16.5 percent the previous quarter, while the San Francisco rate fell to 17.7 percent from 18.3 percent.
- Los Angeles recorded a 17 percent rate for the quarter after holding steady at 16.6 percent during the previous two quarters.
- Meanwhile, in Ventura County, the rate ticked up to 16.1 percent (second quarter 2010, latest data available).

Unsurprisingly, office rents continued to weaken in most locations. In Los Angeles, however, average asking rents remained unchanged, while rents in San Jose rose by about +2 percent and in San Francisco by +5 percent. Though the

See California: Next Page
California Economy Begins Modest Upturn; Uncertainty High

From Previous Page

Office construction pipeline has nearly run dry, vacancies in most areas will likely continue high until employment turns up more strongly.

Industrial vacancy rates also continued high during the third quarter. The lowest vacancy rates were in Los Angeles County, at 3.3 percent, followed by the East Bay, at 5.6 percent, and Orange County, at 6.6 percent. Vacancy rates were highest in San Jose (15.6 percent), San Diego (12.2 percent) and the Inland Empire (10.8 percent). The Sacramento area registered an 11.8 percent vacancy rate in the second quarter (latest available). As in office, industrial space rental rates were on the decline in most areas.

Non-Residential Building Permits

The total value of non-residential building permits in California increased by +2.1 percent during the first three quarters of 2010 compared with the same period in 2009. Permits for office buildings increased by +40 percent and the value of industrial permits was up by +10 percent.

In both cases, the level of activity was still very low, with industrial permit value -73 percent beneath the same period in 2008 and the value of office permits was up by +10 percent.

Several major metropolitan areas have posted significant gains in total non-residential permit activity in 2010 compared with the first nine months of 2009: San Francisco (+26.2 percent), Orange County (+16.2 percent), the Inland Empire (+14 percent), Los Angeles (+5.1 percent) and Oakland (+4.8 percent). Lagging behind were Sacramento (-18.7 percent), San Jose (-5.4 percent) and San Diego (-1.3 percent).

Lender financing for most types of commercial real estate projects continues difficult to obtain. However, traditional investors are showing somewhat more interest, especially in high-quality projects. Nonetheless, non-residential permit values are expected to continue at relatively low levels until the economic recovery gathers more strength.

Risks

Risks appear to be about even, though the downside issues certainly receive more attention. The economy has passed the bottom of a serious, lengthy recession, but the level of activity is still low. Some observers are still unconvinced about the recovery’s staying power. Among others, uncertainty is high because we do not yet know what the rest of the recovery will look like.

One key event risk would be renewed volatility in global capital markets. Central banks and governments around the world have poured trillions of dollars into their financial sectors, and some, like the Federal Reserve, continue to do so. While the results of their efforts are clear, markets are still fragile and easily upset. Further instability in capital markets could spill over into the real economy if money-center banks cut back even more on lending to businesses and consumers.

Another identifiable risk concerns the state’s still-troubled housing industry. Home sales have slowed markedly now that most federal government support has been withdrawn. How long will the slowdown last? Is the industry—already weakened after several bad years—strong enough to weather another downturn?

There is also, however, an upside risk best described as “Optimism Returns.” Consumers and businesses have been worrying about the economy and their own financial situations for more than two years now. Yet the economy seems to be on the mend. Retail sales have improved and so have international trade flows. Industrial production rates are rising, especially in the state’s high technology sector.

Attitudes have not improved as much as revenues, but they might yet catch up. Economic recoveries often begin slowly and then run faster than economists project. The Council would be delighted if this recovery follows such a path!

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The California Chamber of Commerce Economic Advisory Council, made up of leading economists from the private and public sectors, presents a report each quarter to the CalChamber Board of Directors. The council is chaired by Nancy Sidhu, vice president and chief economist, Los Angeles County Economic Development Corporation.

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