

The Kiplinger California Letter

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Dear Client:

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Prices of low-end homes are close to bottom as more foreclosed houses are absorbed by buyers, many of whom are finding the best bargains in years.

Costlier homes...no such luck. Their values will continue to decline through much of the year. Sellers of upscale houses will have to accept less than they had hoped for, exacerbating the price drop for homes in the move-up market and above.

**REAL
ESTATE**

Figure on a 20% drop in median home prices in 2009, much of it coming in the first half. That's on top of the 38% decline recorded for 2008. While the 2008 figures were dramatically distorted by foreclosures, this year's figures may not be. Fewer distressed homes will be sold off by lenders, and sellers will have to cut prices on costly houses.

Sales of homes will keep humming, though... up 25% in 2009...as purchasers seek fire-sale prices.

Low mortgage interest rates provide a spark, even though underwriting standards are tighter now.

Many buyers will be first time homeowners who couldn't afford to get into the market before.

Special deals are helping. They include layoff insurance offered by builders and the Calif. Association of Realtors. First time home buyers who lose their jobs can receive up to \$1500 per month for six months to help with mortgage bills.

But the move-up market will be slow. Homes costing over \$400,000 typically attract the same people who are now trying to rebuild investment portfolios or hang on to their jobs. Though sales of low-end homes may be improving, many move-up buyers will have trouble selling their current homes this year.

Condominiums won't do well, either, especially in Southern California, where many neighborhoods are overbuilt. Expect big discounts in some areas. But some investors are buying them up now, anticipating higher prices later. Sycamore Urban Properties of Irvine has purchased a Rancho Cucamonga project that will be rented out first and then sold, likely in three to five years.

Overall prices will probably stabilize by fall and turn upward in 2010. The government's loan forbearance programs and a better job market will help.

But the climb will be sluggish for a long time. Don't count on returns to double-digit increases or housing prices of the mid-2000s for a long time.

Noncoastal regions will lag the rest of the state in returning to health. Unemployment and a housing glut will hurt Central Valley and Inland Empire areas.

There could be trouble again in 2010. Many home loans made at the height of the boom in 2005 will have lending terms reset in 2010. Even if interest rates are low, people could lose their homes if they're worth less than the loans.

STATE INDUSTRY OUTLOOK



Entertainment

Hollywood will have a solid year as moviegoers seek escapist fare



Agriculture

Water shortages, weak demand for exports will take their toll



Tourism

Foreign travelers won't visit, but Californians will take short trips



High tech

Weak business demand is sure to hurt software and PC industries



International trade

Trucking, warehousing and others depending on the ports will suffer



Construction

Roadwork is likely to pick up, but few homes will be built



Retail

Fewer shoppers as job losses rise

SOUTHERN CALIF.

A solid year lies ahead for Hollywood...escapism sells during recessions. A movie ticket, even with popcorn and a soda, is still a cheap night out. Domestic box office receipts will exceed \$10.5 billion this year, up substantially from the \$9.85 billion in 2008. Among films that will do well: *Wolverine*, *G.I. Joe*, *Public Enemies* and *Up* plus sequels to *Star Trek*, *Harry Potter* and *Terminator*.

But tight credit will hurt studios. Even producers with good track records have a tough time finding financing. With fewer films in production, they'll cut jobs.

A Disney Cruise Line ship will anchor in the Port of Los Angeles starting in 2011. It's moving from Port Canaveral, Fla. About 2600 jobs are expected to be created when the 964-foot-long *Disney Wonder* begins cruises, likely to Mexico. Disney needs room in Fla. for two cruise ships that start service in 2011 and 2012.

Pasadena's new convention center will bring in tourists and employers. The \$150-million center, which opened April 3, already has a number of bookings that will use 55,000 sq. ft. of new exhibit space and a 25,000-sq.-ft. ballroom.

Downtown L.A. will get a \$1-billion office, hotel and retail development at the site of the Wilshire Grand hotel at Figueroa Street and Wilshire Boulevard. South Korea's Hanjin Group plans a 40-story hotel and a 60-story office tower.

Most small businesses can't plan on getting air pollution permits this year because of a court decision. The South Coast Air Quality Management District has issued a moratorium on permits for firms that want generators or any devices that may add to pollution unless they buy emission credits from a company that has reduced pollution. Such credits are hard to find and quite expensive.

The delay will last until at least September...and possibly all year. The superior court in L.A. invalidated free permits given firms and local governments that have low emissions, are relocating or are replacing their equipment. When the agency gave the free permits to power plants, environmentalists sued and won. It will take most of the year to rewrite the rules to exclude power plants.

SAN DIEGO

The San Diego area will land \$758 million in new Defense Dept. spending under the federal stimulus program. Solar and energy efficient projects, which are a high priority for the Navy, will get tens of millions of dollars.

A wireless health institute will be developed by Qualcomm, Scripps Health and the Gary and Mary West Foundation. The \$45-million project will aid technology that sends messages from the human body to the doctor to signal health conditions.

The economy is jeopardizing plans for expanding the convention center. The city could probably land at least five big conventions with more exhibit space, but developers, hoteliers and attorneys worry that the timing for expansion is wrong.

An Indian tribe has acquired naming rights to a university sports stadium. The San Diego State Aztecs basketball team's arena will be renamed Viejas Arena on July 1. The Vieja Band of Kumeyaay Indians locked up a \$6-million, 10-year deal.

Watch out for extra cell phone roaming charges while in San Diego. Occasionally, phones pick up signals from strong towers in Mexico, resulting in up to \$200 in roaming charges. Calling from a plane could also be a problem. Don't make a call unless a U.S. carrier's name shows up on the cell phone screen.

INLAND EMPIRE

The housing slump is bad news for Starbucks. In the real estate boom of the mid-2000s, coffeeshouses accompanied the flurry of tract housing. But when the housing bubble burst, so did the business for lattes and cappuccinos. Of 88 Calif. stores that Starbucks is closing, one-fourth are in this hard-hit region.

The U.S. stimulus will revive Tamco Steel's Rancho Cucamonga operation. The company has called 100 employees back to work for its rebar rolling factory in expectation of demand for its products for highway and bridge construction.



BAY AREA

Cash starved Vallejo will be able to void labor contracts with its employees, according to a court ruling. The city, which filed for Chapter 9 bankruptcy, got permission because federal bankruptcy law trumps state labor regulations, a judge ruled. The case is being closely watched by other cities in financial trouble.

A \$70-million performing arts theater is planned in Livermore as part of a downtown project that will eventually have shops, condos and transit. Backers of the 2000-seat theater hope to land concerts and touring Broadway shows.

Chances are growing that the San Francisco 49ers will move to Santa Clara. The team is close to a deal with city officials to build a stadium near Great America, the theme park, in time for a 2013 opening. City voters would have to OK the plan.

But the Oakland A's probably won't relocate to San Jose, despite city efforts to bring the baseball team south. San Jose is considered part of S.F. Giants territory, and the A's would have trouble raising enough money to pay off the Giants.

Brace for more water cutbacks as reservoirs stay low this summer. The Sierra Nevada snowpack was 81% of normal at the season's official end on March 31, but that's not enough to raise water levels much in an area that has already had two years of dry spells. Many localities will require residents and businesses to cut usage or pay extra for exceeding government imposed quotas.

CENTRAL VALLEY

Electricity rates are going up in the Sacramento Municipal Utility District. The utility will decide in June whether to pursue plans for a 9.5% increase on Sept. 1 and an additional 3.5% hike in January 2011. Rates went up 7% in 2008.

Prison expansions are planned in Kern County. State corrections officials want cell blocks for 900 more inmates each at Kern Valley and North Kern prisons.

Dozens of shopping malls will be left without anchors after liquidation of Gottschalks, the Fresno based department store chain that'll go out of business. Liquidators bought Gottschalks at an auction of the troubled 59-store company.

An onion dehydrating plant will reopen in Firebaugh, Fresno County. Key Foods Ingredients, a division of Olam International of Singapore, foresees better prospects than a family owned business did when it closed the plant in 2006. Key Foods will hire 300 workers for the opening, planned for this summer.

CENTRAL COAST

Forget about an 80-room hotel and restaurant in the Lompoc Valley at La Purisima Golf Course. The Santa Barbara Co. Board of Supervisors has rejected the plan, saying that rezoning the farmland would set a bad precedent.

OLDER WORKERS

If your workforce seems to be getting a lot grayer, you're not alone. The employment rate for Californians aged 65 to 69 rose from 25.2% in 2007 to 29.7% in 2008, says the California Budget Project research group.

Employees are putting off retirement as the economy remains uncertain, their savings shrink, their home values slide and health care costs increase. Other reasons: Improved health, longer life expectancy and less demanding jobs. The big one-year increase just accelerates a trend that began in 1995, when the employment rate for the 65 to 69 age group was only 20.3%.

The employment rate for older women is rising faster than for older men. More men work in the hard-hit construction and finance industries.

The trend is bad news for younger people, who are bearing the brunt of most of the job cutbacks. They may find it harder to work their way up to jobs held by their elders, as firms opt to retain more experienced employees.



AG

Wine grape growers are changing to new varieties to meet shifting tastes. Consumers want lighter wines: Reds...Zinfandel, some Syrahs, rosé. And whites...Pinot Grigio/Gris, White Zinfandel and Riesling. Pinot Noir is a hit, too. Younger customers prefer light-bodied fruity choices to the older, heavier reds. Merlot, an exception, is rebounding. Its volume plunged 25% in California last year, but acreage is again inadequate just as shoppers return to cheaper wines.

Many growers are planting tomatoes because of strong export demand. The state's tomatoes have become more competitive since European farmers stopped receiving government subsidies. Calif. farmers are being paid 17% more than last year by canneries, which expect to buy 11% more tomatoes this year. Much of the planting is outside traditional locations, where water is in short supply.

The U.S. trade victory on pistachio nuts may be moot. Israel raised tariffs on all non-U.S. pistachios, targeting mainly Iranian pistachios that are shipped from Turkey to Israel, which eats more pistachios per person than any other country. But a salmonella outbreak at one California pistachio plant may scare off consumers.

BUSINESS
LAW

Employees can't waive class action lawsuits in an arbitration agreement, according to a California Court of Appeal decision. Judges agreed that a truck driver could file a class action suit against his former employer alleging denial of meal and rest periods, overtime and other labor code violations. The waiver in the arbitration agreement could not be enforced, the court said.

The U.S. Supreme Court is likely to rule on the S.F. health care law, which is bitterly opposed by business groups. The 9th U.S. Circuit Court of Appeals has refused to review the law, which requires many firms to pay for employees' care or donate to a city fund. Opponents say only the feds can control employee benefits.

STATE
FINANCE

Road and transit projects are resuming, funded by \$6.5 billion in borrowing from the largest long-term general obligation bond sale in U.S. history. The state's financial troubles delayed work on hundreds of transportation projects, even though managers of 270 projects were instructed to continue without funding. Funds were also raised for water storage projects and work at schools and colleges.

The money is in addition to \$2.8 billion in federal stimulus funds recently OK'd for Calif. Some of the awards were needed to get matching funds. Bidding on about \$349 million for new projects is scheduled to be completed in June, but it will probably take 2½ months more before construction actually starts.

Among locations of new and continuing projects financed by the bond sales: Alameda County. HOV lanes on two portions of Interstate 580. Placer County. Lincoln Bypass. San Diego County. Interstate 905. Santa Clara County. Central Expressway and Southwest Expressway. Kern County. Westside Parkway, Phase 1. L.A. County. Imperial Highway. Orange County. Seismic refit for Santiago Canyon Road bridge. Southern Calif. Metrolink's Sealed Corridor passenger rail project.

SALES TAX

Rates in several communities are creeping up past 10¢ on the dollar. The 1¢ increase in the state sales tax that took effect April 1 is on top of others passed by localities short of funds. Among cities with the highest sales tax: Pico Rivera, 10¼¢; South Gate, 10¼¢; Oakland, 9¾¢; and Berkeley, 9¾¢. In Oakland, an effort is being made to raise the tax to 10¼¢ to reduce a \$120-million deficit.

Yours very truly,



THE KIPLINGER EDITORS

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