

ECONOMIC OUTLOOK

Key Economic Indicators

(Annual Percent Change, except for New Housing)

	2002	Forecast	
		2003	2004
U.S. Gross Domestic Product, adjusted for inflation	2.3 %	2.5 %	3.5 %
California Nonfarm Employment	-0.7 %	0.7 %	2.1 %
California Personal Income	0.9 %	3.3 %	5.3 %
California Consumer Price Index	2.5 %	2.8 %	3.2 %
California New Housing Units	159,000	157,000	162,000

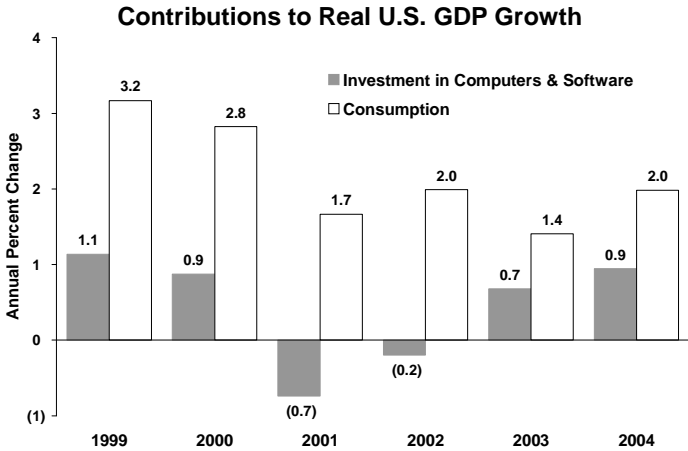
The national and California economies were growing slowly as 2002 came to a close. Labor markets were weak in California and most of the rest of the nation; the state and national economies were experiencing jobless recoveries. Better had been expected from both economies at midyear. Their recovery is now projected to be sluggish through most of 2003, and economic growth in 2004, less robust than had been expected.



The Nation

- ◆ The national economy entered the fourth quarter of 2002 with four consecutive quarters of economic growth behind it. Economic growth slowed considerably in the fourth quarter, and for the year as a whole, the economy grew by about 2.3 percent, adjusting for inflation. That was not enough growth to convince employers to take on new workers, however. In fact, average nonfarm payroll employment fell nearly 1.0 percent from 2001, and unemployment averaged about 5.8 percent, up from 4.8 percent in 2001.
- ◆ Excess capacity will keep capital equipment spending plans modest in many industries. Still, low interest rates, expansive federal fiscal policy, increased spending by businesses on computers and software, and continued, if somewhat more modest, gains in consumer spending will provide enough stimulus to keep the recovery going in 2003. Growth will be modest during the first half of 2003. Firms will squeeze as much output from their current workers as possible, resulting in negligible employment gains. By the end of 2003, however, they will find it necessary to increase hiring in order to meet increased production schedules.
- ◆ The major risk to the outlook is a significant retrenchment by consumers. Consumers have spent aggressively for many years, and their debt loads have increased considerably. Further, their confidence has waned somewhat. The primary development that could boost the economy beyond expectations is a significant new federal fiscal stimulus package made up of well-designed, effective tax breaks and targeted increases in government spending.





California

- ◆ Like the nation, California is experiencing a jobless recovery. The state economy improved in the first half of 2002, with employment and total state personal income posting gains. The improvement faltered at midyear, however. The state lost jobs between June and November, and personal income likely fell in the third quarter. In addition, unemployment failed to improve, as the rate varied between 6.4 percent and 6.5 percent for most of the year.
- ◆ The California economy entered 2003 with little momentum. Labor markets were weak with no signs that significant improvement was imminent. The outlook for the California economy in 2003 depends heavily on the fate of the national economy. Near-historic low interest rates should help the state economy in 2003, as should continued strong spending on



national defense and homeland security. On balance, the outlook for the California economy is for slow growth in 2003 and moderate growth in 2004. Unemployment will likely increase somewhat in 2003 before falling in 2004.

- ◆ The main risk to the outlook for the state economy is the same as that for the national economy—a retrenchment by consumers. In addition, the state is more at risk to a delay in the high-tech recovery. As for the nation, the economy could be stronger than expected if a new federal fiscal stimulus package made up of well-designed, effective tax breaks and targeted increases in government spending is enacted.

Jobless Recovery California

