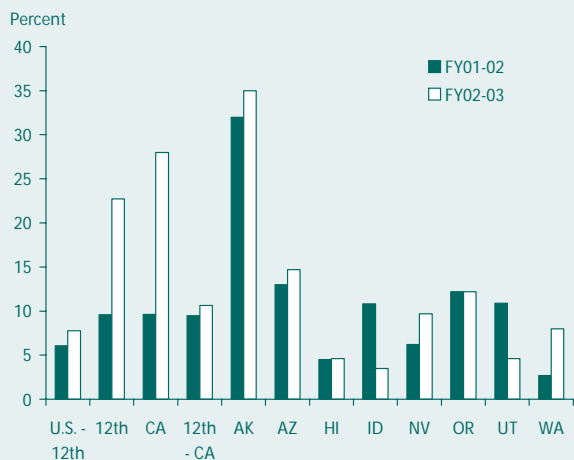


Western Economic Developments



Economic downturn challenges state budgets in Twelfth District

Figure 1: Anticipated state budgetary shortfalls

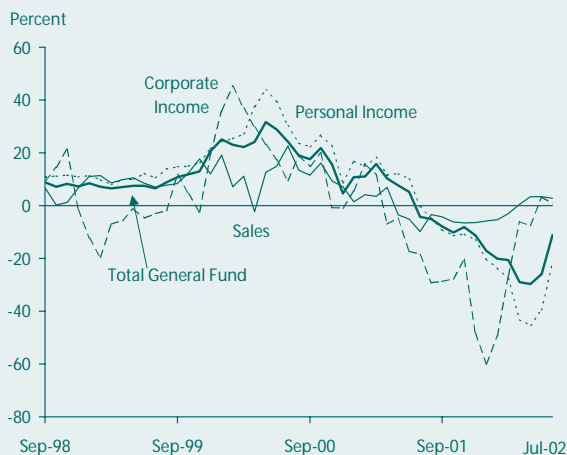


Source: National Conference of State Legislatures.

The deterioration in economic conditions since 2000 has put significant pressure on state budgets across the Twelfth Federal Reserve District. Figure 1 displays the anticipated revenue shortfalls as a percent of budgeted expenditures in fiscal years 2001–2002 and 2002–2003 for the District and the rest of the U.S. As the figure illustrates, fiscal pressures are especially acute for California; California’s 28% anticipated shortfall in 2002–2003 dwarfs that in every state except Alaska. Other District states also face more severe budgetary crunches than the average state outside of the District. The mean anticipated shortfall in fiscal year 2002–2003 for the District excluding California is 10.6%, compared to 7.8% for the U.S. excluding District states.

The primary reason for weak state fiscal conditions has been a greater-than-expected decline in state tax revenues. In California, personal income tax (PIT) revenues were 40–50% below year-earlier values in the spring of this year, accounting for most of the 30% drop in total revenues during the period (see Figure 2). The drop in PIT and total revenues was due largely to the sharp growth and subse-

Figure 2: California state revenues



Source: California Department of Finance.

SEPTEMBER 2002

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quent fall in PIT revenues associated with stock market gains.¹ Although the weak stock market remains a drag on revenue growth relative to previous years, California's revenue crunch may be easing a bit. All categories of income tax revenue have shown smaller year-over-year declines in recent months and sales tax revenues have increased (Figure 2).

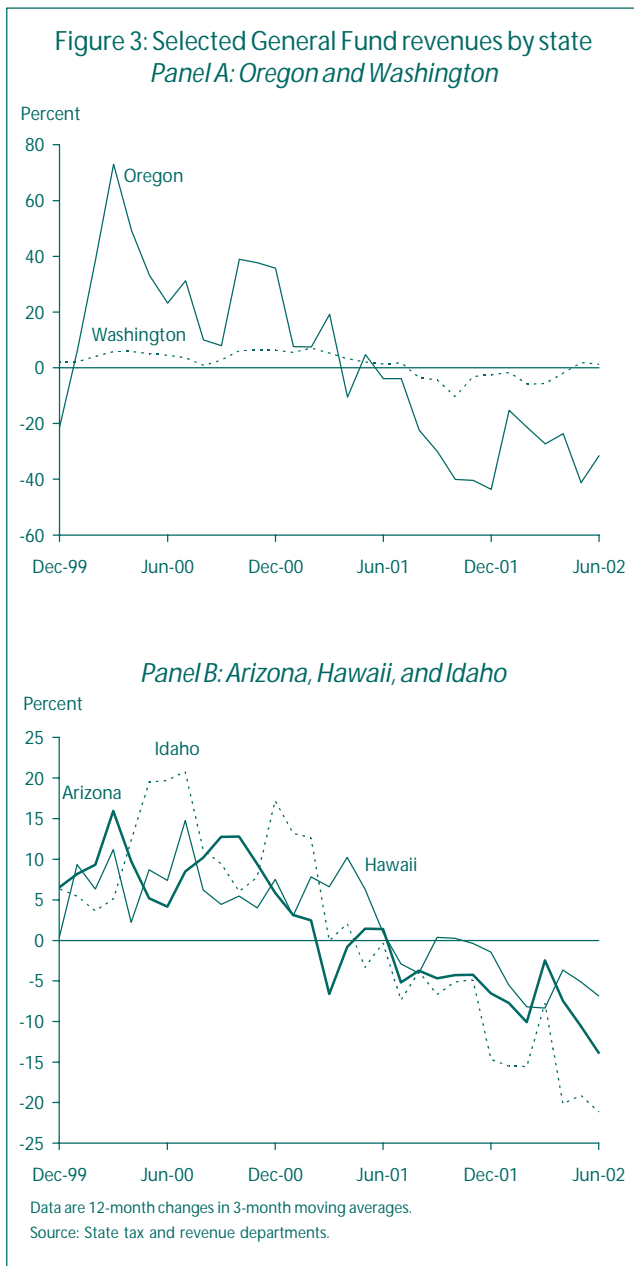
Among other Twelfth District states with total revenues data available, declines have been most severe in Oregon, Idaho, and Arizona (Figure 3). Like California, the first two of these rely heavily on income taxes for state revenues (ranking sixth and seventh nationwide). The revenue decline has been less severe in Washington, which does not collect state income taxes, and in Hawaii.²

All District states have made adjustments to deal with budget gaps, with most relying at least in part on spending cuts and tax increases. To gauge the possible economic impact of such measures, consider the case of California. Plans to close the state's \$23.7 billion budget deficit include spending cuts (program reductions) of \$7.5 billion and tax increases of \$2.9 billion during the current fiscal year. If these measures act as offsets to overall economic activity in the state, their net negative impact (\$10.4 billion) equals 0.8% of the state's \$1.34 trillion nominal gross state product in 2000 (the latest year for which data are available). Although such cuts are unlikely to have large multiplier effects, the need for further cuts later (to eventually make up for much of this year's large remaining shortfall) suggests that California's fiscal problems may hamper the state's economic recovery in future years as well. Other Twelfth District states also will feel the effects of tight fiscal conditions, although they probably will not be as large as those in California.

District employment slow to recover

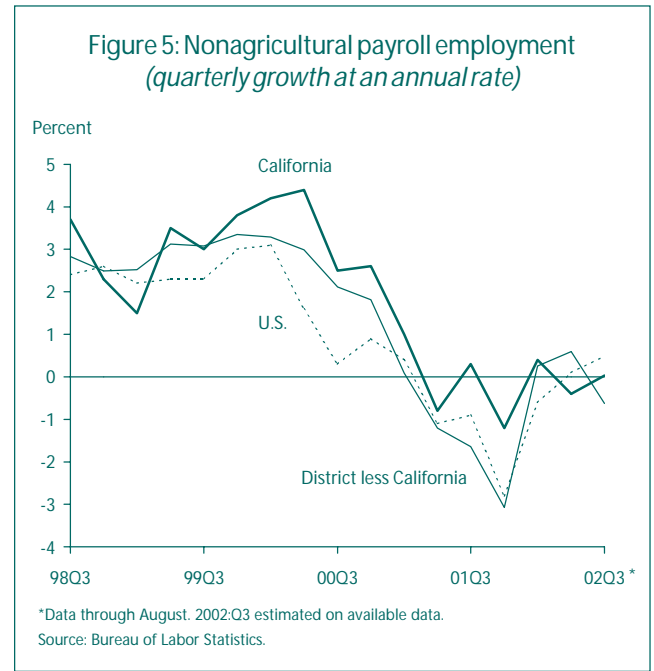
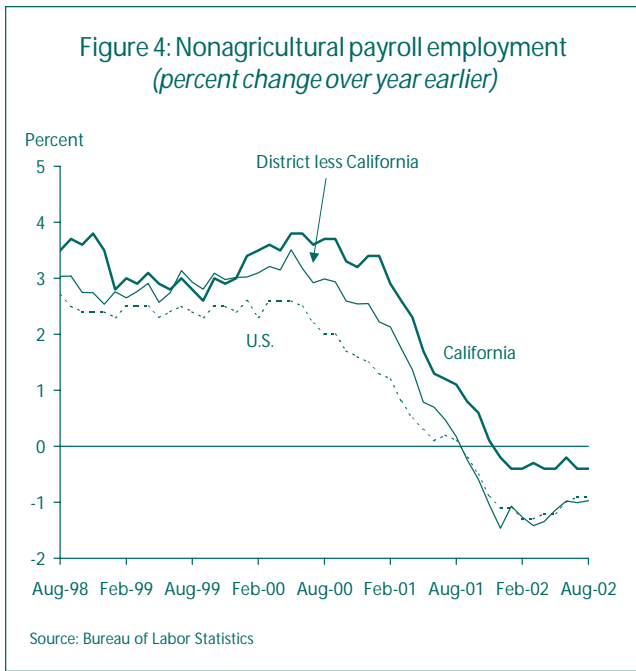
District employment has been essentially flat this year, as businesses remain cautious about expanding capacity. Indeed, in most District states employment remains below levels from a year ago. On a yearly basis, California has fared better than the rest of the District and the nation. Data through August show payroll employment declined -0.4% over the past 12 months, compared to -0.9% in the U.S. (Figure 4). Year-over-year employment changes in the rest of the District have been tracking the U.S. However, in terms of quarterly changes, both California and the rest of the District are off to a slow start in the third quarter of 2002. Partial data show that growth for California and the rest of the District has dropped below that in the nation as a whole (Figure 5).

In California, payroll employment was essentially flat on net in July and August. Despite the lack of payroll job growth,



1 In the year 2000, California was ranked first among all states in its share of capital gains in IRS adjusted gross income and its share of income taxes in state General Fund revenues (source: Nelson A. Rockefeller Institute of Government, tabulations of IRS and Census data).

2 Within the District, Alaska and Nevada also do not have a state income tax. Alaska relies heavily on its Permanent Fund, which is funded by oil revenues and is separate from the General Fund.



California's unemployment rate fell in those months, from 6.5% to 6.2%. California's falling unemployment rate, however, was due largely to a drop in the size of the labor force that exceeded the drop in employment (measured from the household survey). Some of the decline in the labor force may be due to job seekers leaving the labor market in response to rising durations of unemployment in the state. For example, the percentage of unemployed in California who have been job seekers for at least 27 weeks has risen steadily this year, from a cyclical low of 12.7% in December 2001 to 17.3% in August 2002 (measured on a 12-month moving average basis). The corresponding figure for the nation as a whole was 15.8% in August, which suggests that long durations of unemployment and associated low exit rates are a slightly greater problem in California than elsewhere in the nation.

Among California regions, the San Francisco Bay Area continues to exhibit the weakest conditions, with employment falling at a 3% annual rate on average in July and August. The size of the labor force fell by about the same amount, keeping the Bay Area unemployment rate approximately constant (5.7% in August). Southern California fared better in July and August, with slight job gains evident and a drop in the unemployment rate from 5.8% in June to 5.3% in August.

Outside California, most Twelfth District states saw little or no job growth in the past few months, with unemployment remaining at elevated levels. The main exceptions were

Hawaii and Nevada, which have benefited from improved tourism activity this year. Hawaii saw domestic visitor counts that exceeded year-earlier levels during much of August, although these counts dropped back down in early September and have not been high enough to offset weak international visits. Still, the improvement has been sufficient to keep Hawaii growing at a moderate pace this year, and the unemployment rate there has fallen from 5.6% at the end of last year to 4.0% in August. Nevada's performance has been uneven this year, with a surge in the first quarter followed by substantial slowing in subsequent months; its tourism and gaming sector continues to struggle with somewhat depressed visitor counts and revenues. However, like Hawaii, the state's unemployment rate has fallen substantially this year, from 6.9% in December 2001 to 5.1% in August.

Consumer spending, housing hold their own

In a sign of underlying strength throughout the District, consumer spending has continued to grow, although not as rapidly as in the rest of the nation. Data for the broad West region show year-over-year gains in retail sales (excluding food services) of 3–5% in June through August.⁴ Although the West's one-month gain in August (over July) led the nation, its year-over-year growth has been trailing behind

⁴ Data are from Bank of Tokyo-Mitsubishi. The West region includes the Twelfth District plus Colorado, Montana, New Mexico, and Wyoming.

the rest of the nation this year, with recent gains in the range of 4–6% evident for other regions.

Home sales have been rapid in most parts of the Twelfth District and prices have been rising, although signs of slower activity are emerging for the months ahead. Home sales surged in California and the rest of the District in the first quarter of this year, but they came down a bit in the second quarter (Figure 6). Figures for California show that sales fell substantially in June on a month-to-month basis, followed by only a slight increase in July; sales in those months remained above year-earlier levels, although the annual pace of increase has slowed relative to earlier in the year.

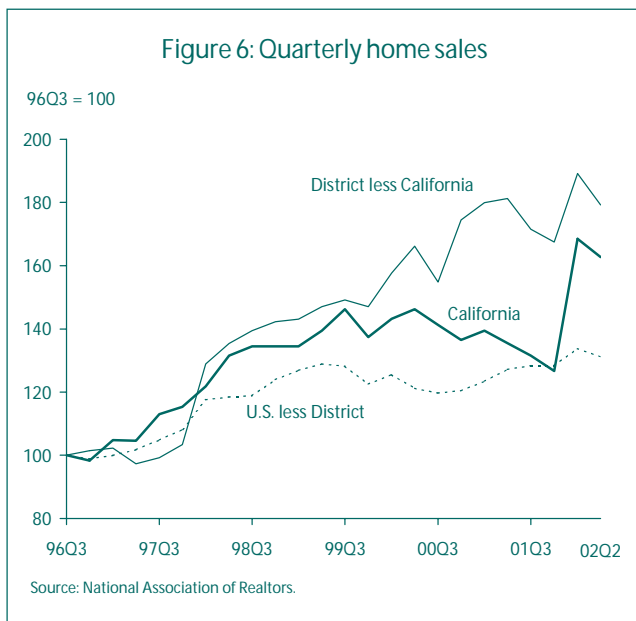
Residential builders throughout the District responded to the surge in buying activity earlier this year by increasing planned building activity in recent months. However, residential building activity has not been at especially high levels in the District over the past 12 months.

Finally, District commercial real estate markets have remained largely stable in recent months. Based on data through 2002:Q2, vacancy rates on commercial and industrial space have stabilized at high levels in most urban areas, and the decline in rental rates generally has slowed or stopped. However, demand for commercial real estate remains weak, especially in tech-dependent areas.

High-tech sector slows, cuts employment

After improving in the spring, conditions in the District's high-tech sector held steady or declined a bit recently. On a 3-month basis, the growth in sales and shipments of semi-conductors, computers, and communications equipment picked up substantially earlier this year, but it slowed again in recent months (see charts on p. 5). The pace of job losses in California's computer, communications, and electronics manufacturing industries slowed in the second quarter of this year but accelerated again in July and August. Similarly, average hours worked per week in these sectors in California have fallen by 1 to 4 hours since reaching peaks of 40 to 44 hours earlier this year.

Recent news from the District's technology sector has focused on job cuts and reductions rather than expansions. Sun Microsystems already has reduced its workforce by 9,000 jobs companywide and plans to reduce employment by another 1,000 workers by the end of the year. In the wake of its merger with Compaq, Hewlett Packard has cut 4,740 jobs companywide so far, with another 10,000 cuts expected by October 31. Numerous smaller tech firms also are cutting jobs throughout the District. Microsoft's recently announced plan to increase employment by 5,000 companywide is one of the few pieces of positive news from the tech sector.

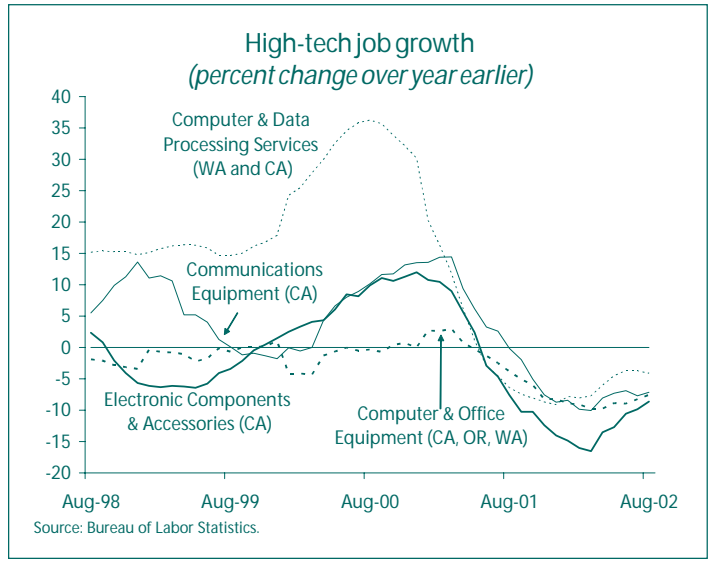
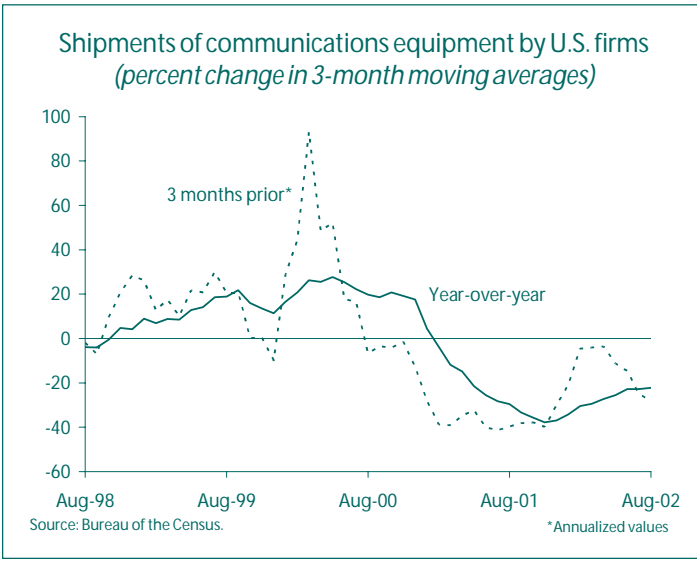
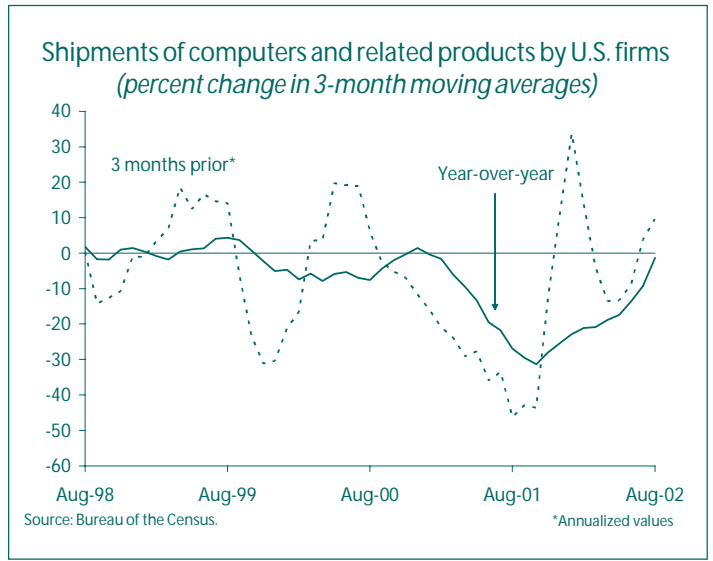
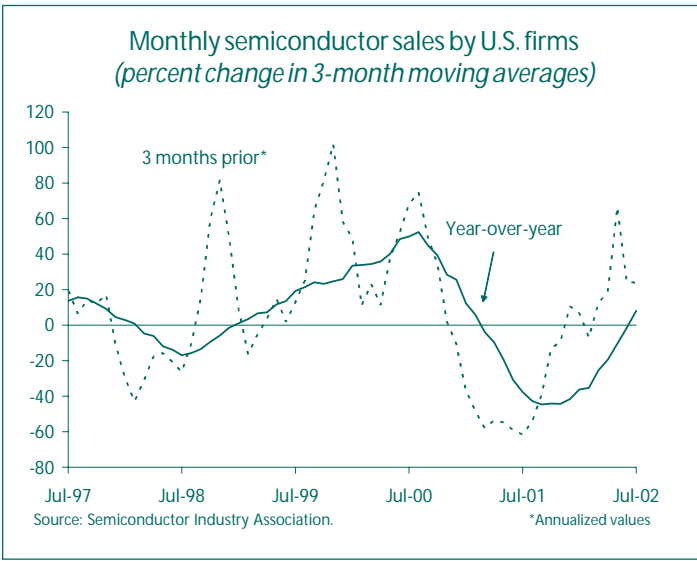
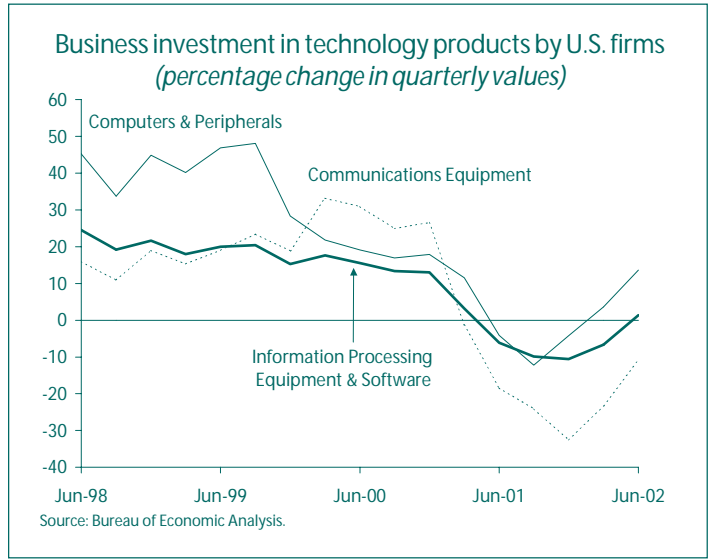
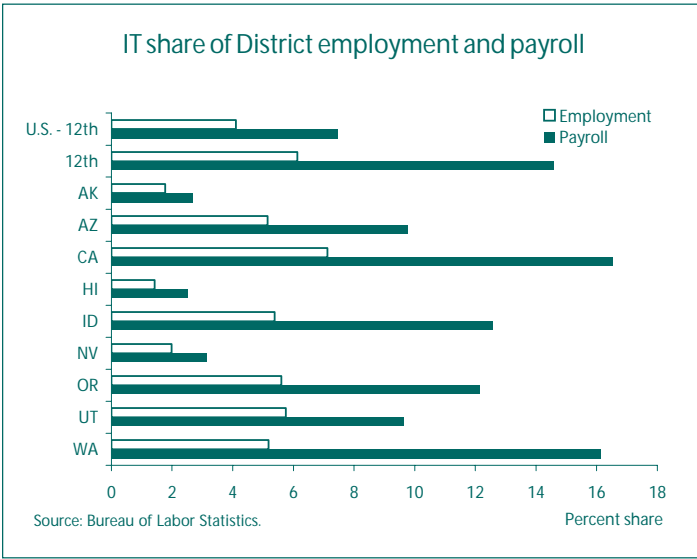


Contributions by Rob Valletta, Geoffrey MacDonald, and Lily Hsueh,
Financial and Regional Studies, Economic Research Department, FRBSF

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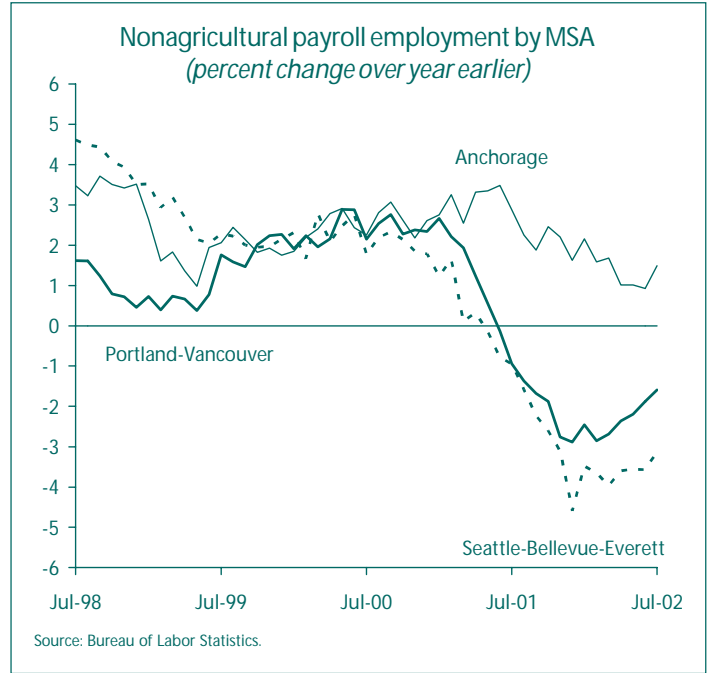
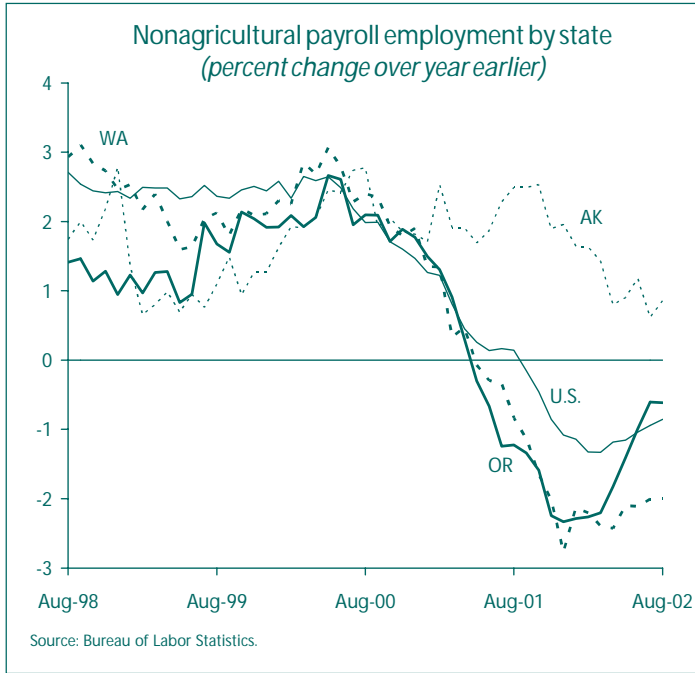
High-tech Watch





STATE HIGHLIGHTS

Alaska • Oregon • Washington



Employment by Industry

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
Alaska					
Total	294.6	5.5	4.8	1.7	0.9
Mining	10.1	0.0	-14.4	-4.3	-7.3
Construction	15.4	17.0	14.1	6.1	4.1
Manufacturing	13.6	0.0	54.4	4.6	-6.2
T.C.P.U.	27.7	0.0	-2.8	-2.1	-1.1
Trade	59.0	4.2	2.8	0.5	1.2
F.I.R.E.	12.8	9.9	-3.1	-1.2	0.8
Services	75.0	4.9	2.7	2.7	2.0
Government	81.0	7.7	6.7	2.8	2.0
Oregon					
Total	1,582.2	-0.4	0.2	0.2	-0.6
Mining	1.7	0.0	65.0	0.0	-5.6
Construction	72.9	0.0	-0.5	-3.4	-6.8
Manufacturing	226.6	-6.1	1.4	-1.2	-2.7
T.C.P.U.	76.8	-11.7	-4.6	-2.3	-3.0
Trade	387.7	-6.3	-3.0	-0.1	-0.5
F.I.R.E.	95.3	-6.1	-2.5	0.2	0.1
Services	447.9	2.7	2.7	1.0	0.9
Government	273.3	14.7	1.8	2.1	0.8

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
Washington					
Total	2,644.8	-1.4	-1.4	-0.6	-2.0
Mining	3.1	0.0	0.0	-4.7	-11.4
Construction	145.8	7.7	3.4	-0.6	-5.8
Manufacturing	306.8	-11.0	-9.2	-6.5	-9.2
T.C.P.U.	136.5	-2.6	-5.4	-4.7	-8.1
Trade	624.1	-2.3	-0.8	-0.1	-1.6
F.I.R.E.	143.2	-1.7	-0.8	-0.7	0.8
Services	767.3	-1.7	0.0	0.5	-0.4
Government	518.0	4.0	0.1	2.0	2.1

Unemployment Rates (%)

	Aug-02	Jul-02	Jun-02	May-02	Aug-01
Alaska	7.3	6.7	6.7	6.0	6.3
Oregon	7.0	7.3	7.2	7.2	6.7
Washington	7.2	7.1	6.8	7.1	6.5
U.S.	5.7	5.9	5.9	5.8	4.9

Unemployment rates are from the household employment survey; all other data are for nonagricultural payroll employment. All data are seasonally adjusted.
^a Annualized.

Source: Bureau of Labor Statistics.

Residential permits—August 2002

	3-mo. average number	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Alaska	221.0	-18.6	10.2
Oregon	1,784.8	-7.7	5.2
Washington	3,482.5	0.6	-9.6

Source: Bureau of the Census.

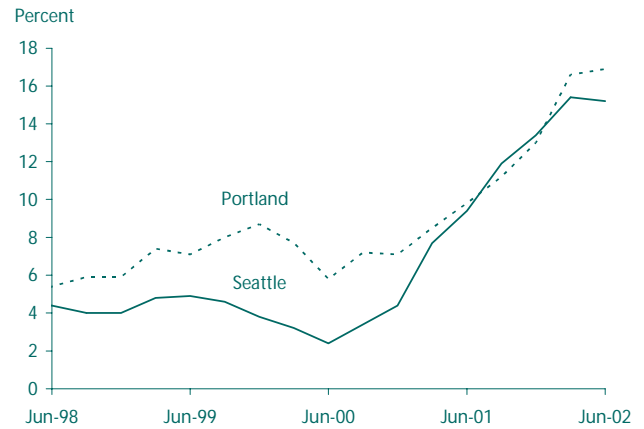
Non-residential construction awards—August 2002

	3-mo. average \$ millions	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Alaska	28.3	-74.6	7.7
Oregon	203.1	8.4	-16.4
Washington	320.9	17.5	-19.2

^a Underlying data are seasonally adjusted moving averages.

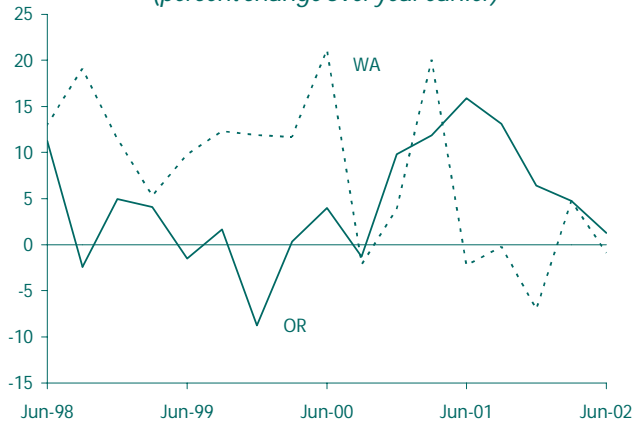
Source: F.W. Dodge.

Metro area office vacancy rates



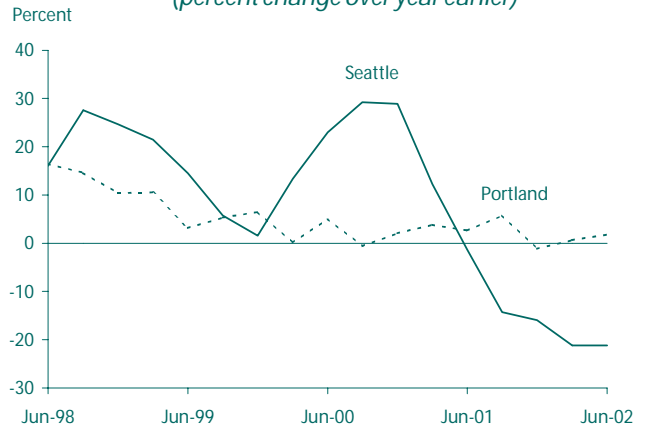
Source: Torto Wheaton Research.

Sales of existing homes (percent change over year earlier)



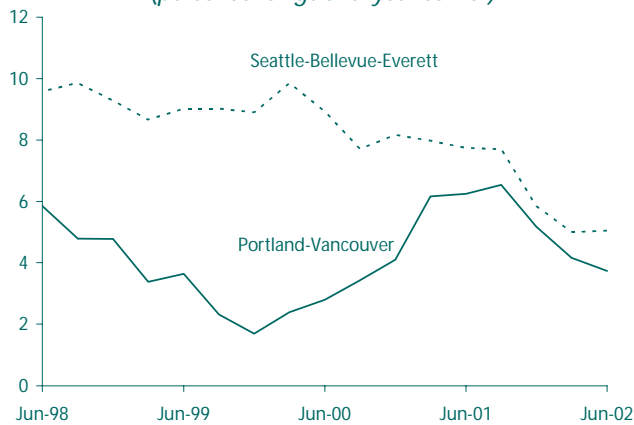
Source: National Association of Realtors.

Metro area office gross rents (percent change over year earlier)



Source: Torto Wheaton Research.

Home price index (percent change over year earlier)



Source: Office of Federal Housing Enterprise Oversight.

Export update

	\$ billions		12 - month Percent Change		
	2001	July*	2000	2001	July*
Alaska	2.4	1.4	-5.6	-2.0	5.2
Oregon	8.0	5.1	6.6	-24.0	8.1
Washington	33.9	20.2	-13.1	8.5	-1.7

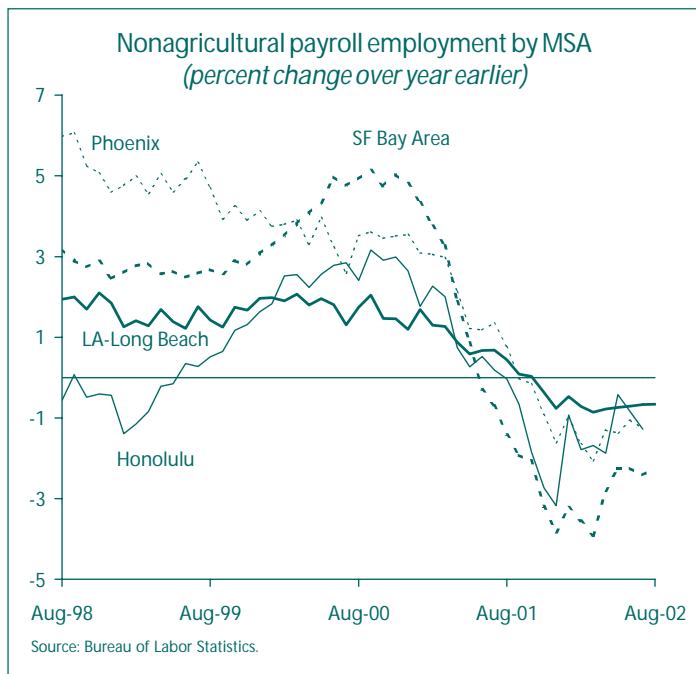
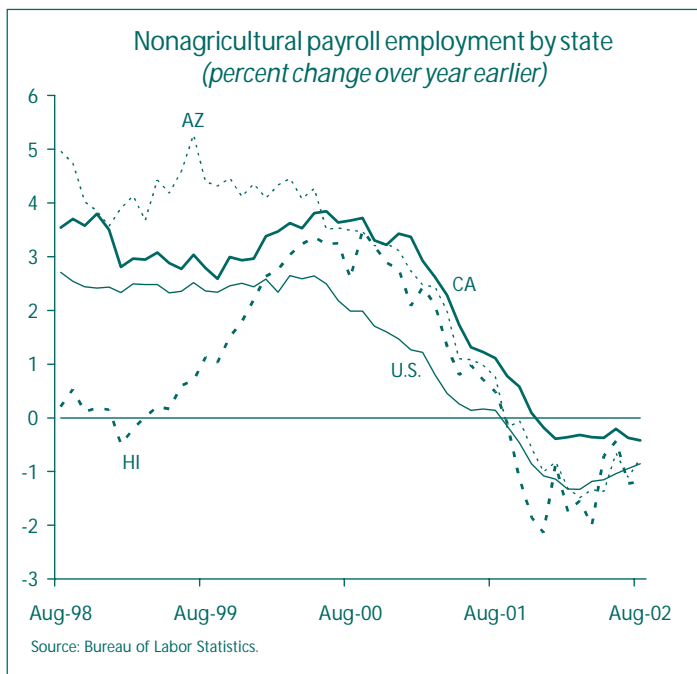
* Indicate year-to-date values.

Source: Census FT900 Supplement, Origin of Movement Series.



STATE HIGHLIGHTS

Arizona • California • Hawaii



Employment by Industry

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
Arizona					
Total	2,253.6	4.8	2.9	0.4	-0.8
Mining	8.4	-13.2	-20.6	-11.3	-10.6
Construction	158.7	12.1	4.7	-1.4	-3.9
Manufacturing	193.4	-7.2	-3.2	-6.5	-7.1
T.C.P.U.	105.0	-2.3	-3.7	-4.5	-5.7
Trade	537.1	-3.3	-0.4	0.5	0.8
F.I.R.E.	148.9	0.0	-0.5	-2.4	-1.4
Services	710.1	10.2	1.0	2.3	-0.2
Government	392.0	15.2	18.4	4.2	2.5
Hawaii					
Total	549.1	-1.7	-1.2	1.0	-1.2
Mining
Construction	24.4	-9.3	-9.3	2.5	5.2
Manufacturing	17.5	-12.7	-4.4	-1.7	-2.8
T.C.P.U.	39.1	0.0	2.1	3.1	-8.6
Trade	132.3	0.0	-1.8	-0.1	-3.2
F.I.R.E.	33.0	-3.6	0.0	0.9	0.6
Services	186.3	8.1	4.9	2.3	-0.6
Government	116.5	-14.2	-8.8	-0.4	1.6

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
California					
Total	14,659.6	1.0	0.1	0.0	-0.4
Mining	23.3	0.0	-1.7	-4.9	-4.1
Construction	756.2	-0.8	-0.1	-1.0	-2.4
Manufacturing	1,807.7	-4.1	-3.4	-2.9	-4.0
T.C.P.U.	718.9	-2.1	-2.8	-3.2	-4.3
Trade	3,371.2	1.3	1.5	1.6	1.0
F.I.R.E.	845.1	0.6	-0.7	-1.0	-0.1
Services	4,668.2	-0.2	-1.1	-0.6	-0.4
Government	2,469.0	8.3	4.4	3.1	2.1

Unemployment Rates (%)

	Aug-02	Jul-02	Jun-02	May-02	Aug-01
Arizona	5.7	6.0	6.0	5.7	4.7
California	6.2	6.4	6.5	6.4	5.5
Hawaii	4.0	4.3	4.0	4.2	4.3
U.S.	5.7	5.9	5.9	5.8	4.9

Unemployment rates are from the household employment survey; all other data are for nonagricultural payroll employment. All data are seasonally adjusted.
^a Annualized.

Source: Bureau of Labor Statistics.

Residential permits—August 2002

	3-mo. average number	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Arizona	5,759.1	19.1	0.2
California	11,974.5	-3.2	-1.5
Hawaii	402.5	-16.2	3.3

Source: Bureau of the Census.

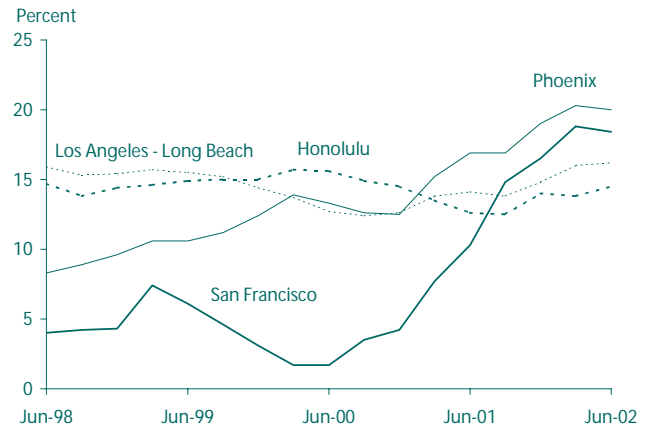
Non-residential construction awards—August 2002

	3-mo. average \$ millions	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Arizona	313.1	34.5	-15.8
California	1,317.9	12.8	-21.1
Hawaii	22.6	-27.6	9.1

^a Underlying data are seasonally adjusted moving averages.

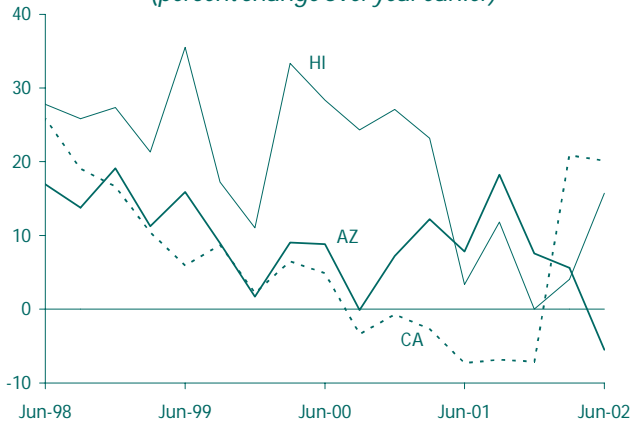
Source: F.W. Dodge.

Metro area office vacancy rates



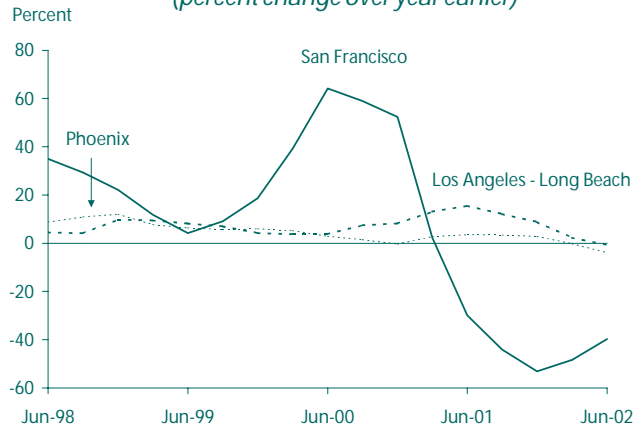
Source: Torto Wheaton Research.

Sales of existing homes (percent change over year earlier)



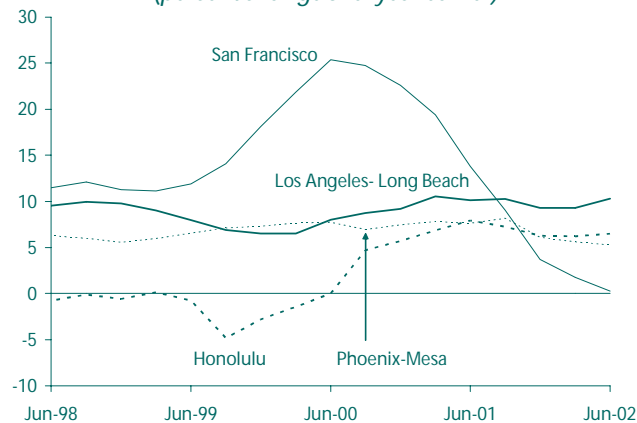
Source: National Association of Realtors.

Metro area office gross rents (percent change over year earlier)



Source: Torto Wheaton Research.

Home price index (percent change over year earlier)



Source: Office of Federal Housing Enterprise Oversight.

Export update

	\$ billions		12 - month Percent Change		
	2001	July*	2000	2001	July*
Arizona	11.1	6.0	19.0	-15.6	-13.4
California	90.7	45.2	19.5	-10.2	-19.2
Hawaii	0.3	0.2	33.4	8.8	-2.2

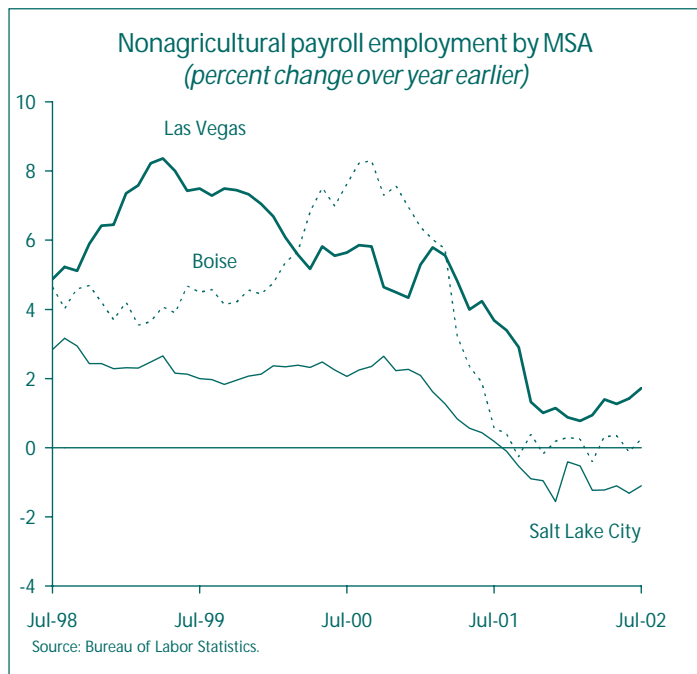
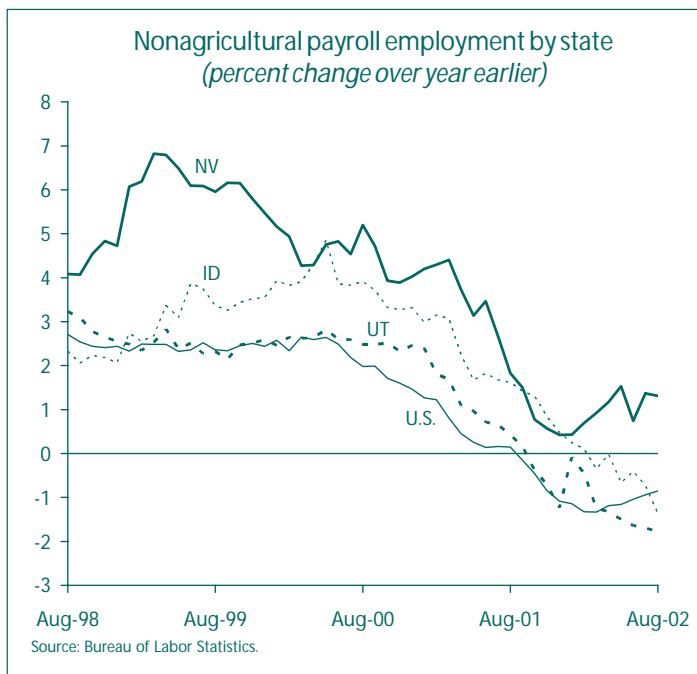
* Indicate year-to-date values.

Source: Census FT900 Supplement, Origin of Movement Series.



STATE HIGHLIGHTS

Idaho • Nevada • Utah



Employment by Industry

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
Idaho					
Total	563.7	-4.8	-2.5	-1.4	-1.4
Mining	1.8	98.6	0.0	9.0	-10.0
Construction	34.3	-15.9	-11.9	-11.8	-9.3
Manufacturing	70.8	7.0	-1.7	-3.7	-5.6
T.C.P.U.	27.1	-12.4	-5.7	-3.8	-2.9
Trade	140.4	-1.7	2.3	1.1	-0.6
F.I.R.E.	24.8	-4.7	1.6	0.6	0.4
Services	151.4	-10.5	-4.9	-1.8	-0.7
Government	113.1	-3.1	-2.8	1.2	2.4
Nevada					
Total	1,071.5	0.8	-0.7	3.1	1.3
Mining	9.0	0.0	-4.3	-9.2	-9.1
Construction	93.4	1.3	1.7	5.5	2.4
Manufacturing	46.2	2.6	2.6	1.6	-0.4
T.C.P.U.	57.5	2.1	1.4	2.7	-0.3
Trade	227.5	0.5	-0.4	3.8	2.4
F.I.R.E.	51.8	2.3	5.6	5.1	3.4
Services	454.6	-2.9	-3.7	2.4	0.6
Government	131.5	12.7	3.1	4.0	2.6

	Total Employed (thousands)	Percent Change			
		Aug-02	1-mo. ^a	3-mo. ^a	YTD ^a
Utah					
Total	1,063.2	-2.1	-2.2	-1.5	-1.8
Mining	7.2	0.0	-15.1	-9.6	-7.7
Construction	65.1	-8.8	9.8	-11.8	-8.2
Manufacturing	119.6	-3.0	-1.0	-4.1	-5.2
T.C.P.U.	57.7	4.3	-5.4	-1.8	-4.8
Trade	246.0	2.5	-4.1	-0.8	-1.6
F.I.R.E.	59.4	2.0	-1.3	-1.7	-1.7
Services	313.7	-9.8	-6.8	-0.2	-0.5
Government	194.5	5.1	5.3	1.9	1.7
Unemployment Rates (%)					
	Aug-02	Jul-02	Jun-02	May-02	Aug-01
Idaho	5.3	5.4	5.2	5.0	4.9
Nevada	5.1	5.4	5.5	5.5	5.3
Utah	5.0	5.2	4.7	5.1	4.4
U.S.	5.7	5.9	5.9	5.8	4.9

Unemployment rates are from the household employment survey; all other data are for nonagricultural payroll employment. All data are seasonally adjusted.
^a Annualized.

Source: Bureau of Labor Statistics.

Residential permits—August 2002

	3-mo. average number	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Idaho	890.4	-5.5	-4.8
Nevada	2,900.3	6.8	-8.8
Utah	1,601.3	1.5	6.5

Source: Bureau of the Census.

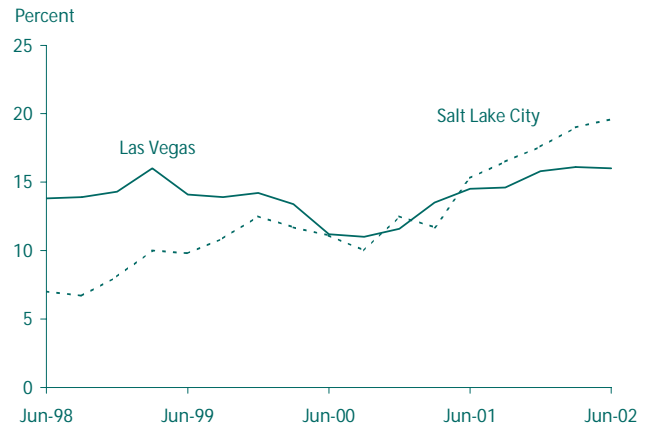
Non-residential construction awards—August 2002

	3-mo. average \$ millions	Moving average percent change	
		3-mo. ^a	12-mo. ^a
Idaho	55.5	43.9	-21.7
Nevada	156.3	22.1	1.8
Utah	131.4	0.2	2.7

^a Underlying data are seasonally adjusted moving averages.

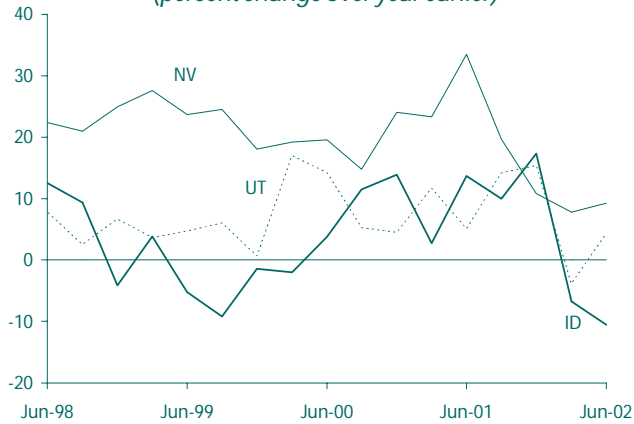
Source: F.W. Dodge.

Metro area office vacancy rates



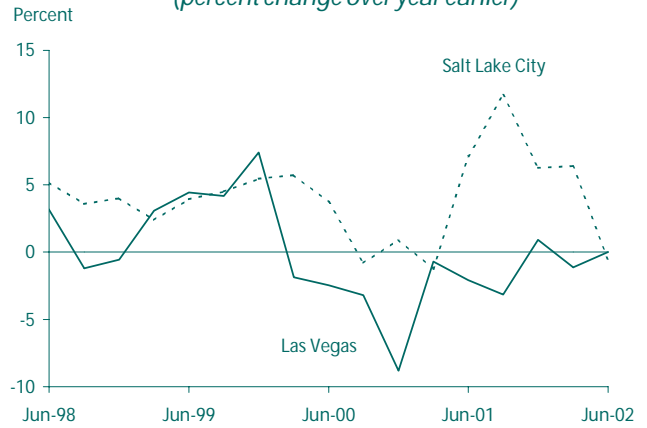
Source: Torto Wheaton Research.

Sales of existing homes (percent change over year earlier)



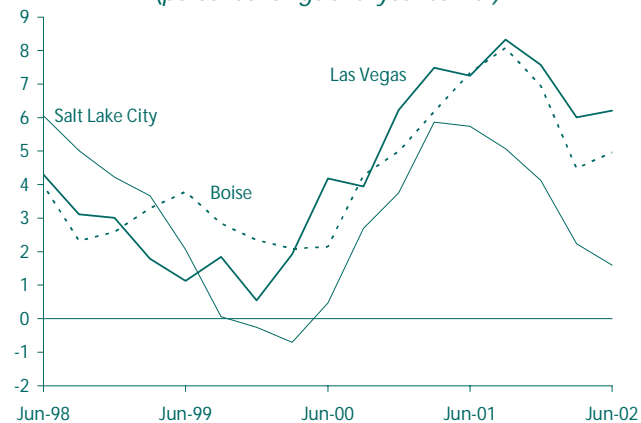
Source: National Association of Realtors.

Metro area office gross rents (percent change over year earlier)



Source: Torto Wheaton Research.

Home price index (percent change over year earlier)



Source: Office of Federal Housing Enterprise Oversight.

Export update

	\$ billions		12 - month Percent Change		
	2001	July*	2000	2001	July*
Idaho	1.9	0.9	53.6	-41.7	-25.4
Nevada	1.1	0.5	21.8	13.9	-15.2
Utah	3.4	2.4	1.7	9.3	22.8

* Indicate year-to-date values.

Source: Census FT900 Supplement, Origin of Movement Series.

2002 Issues

Mailing Dates

March	March 26
June	July 2
September	October 4
December	December 17

Four additional updates to statistical charts are available online during interim periods at <http://www.frbsf.org/publications/economics/wed/index.html>

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Federal Reserve Bank of San Francisco
101 Market Street
San Francisco, California 94105

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