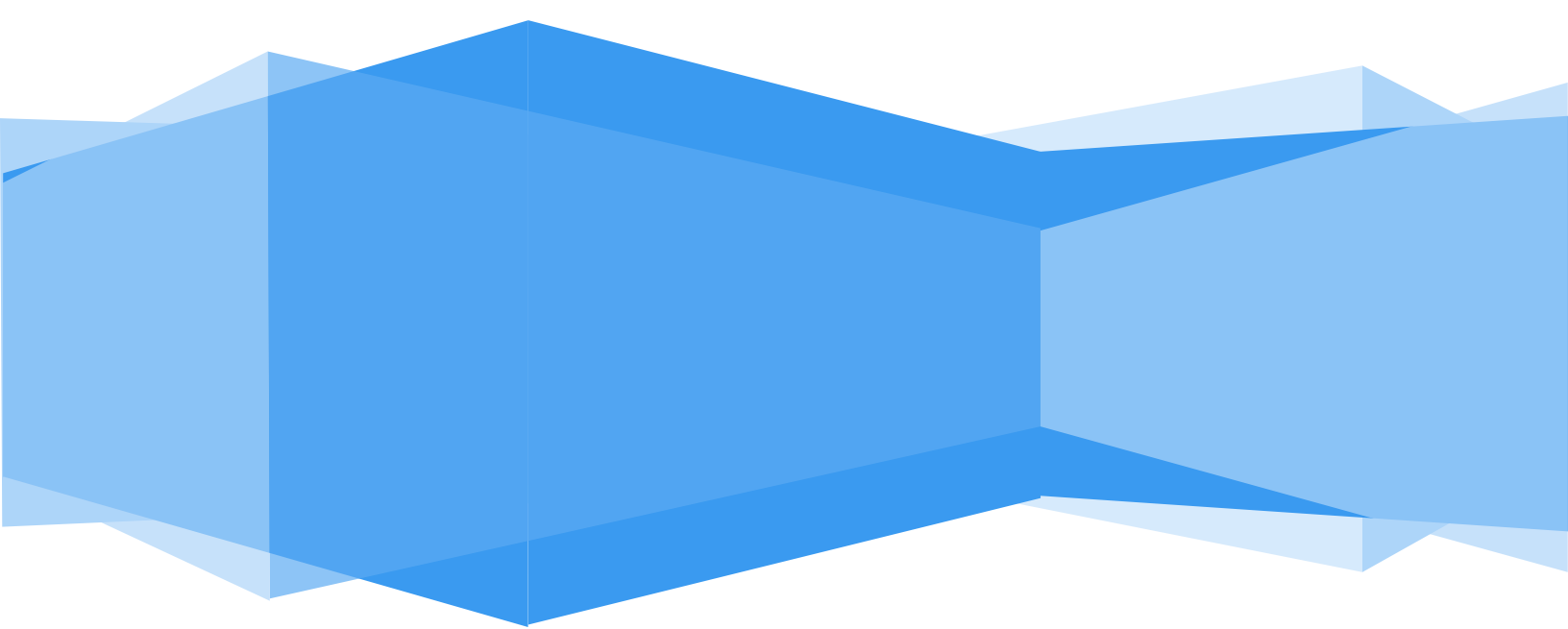




Economic Outlook

4Q2010 News



National Economy

Growth too listless to spur hiring.

Economy shows signs of life, but not enough to change jobs picture.

The American economy is showing a little more pep in its step, the government reported recently, but not enough to help bring down high unemployment or put the country on the road to sustained and widespread prosperity.

The nation's gross domestic product - the total value of all goods and services produced inside U.S. borders - grew at a modest annual rate of 2 percent in the third quarter, up from 1.7 percent in the second quarter, the Commerce Department said.

"The most striking thing about the report on gross domestic product is that it shows that the U.S. economy is still smaller today than it was when the recession began -- even after more than a year after the recession officially ended," said EPI economist Josh Bivens. "This remains an historically slow recovery. Never since (World War II) has it taken so long to recover to pre-recession levels of GDP," he said.

Business investment, too, was solid in the July-to-September period. Companies' spending on equipment and software again rose by double digits, although at a slower pace than in the second quarter, and investment in offices and other commercial buildings posted the first upturn after eight straight quarters of decline.

What's more, federal government expenditures continued to add juice to GDP growth. So why wasn't U.S. economic output stronger than 2 percent? In a word, imports. Although American exports were up in the quarter, imports rose at an even faster clip. And the resulting trade deficit, in effect, amounted to a halving of the GDP growth rate in the third quarter. "It does say that we continue to basically consume more than we produce," said economist Lynn Reaser of the National Association for Business Economics. To be sure, exports are helping boost overall GDP, she said, and import growth is not a bad thing, as it reflects stronger American demand. But, she added, "We've got to do something about the trade deficits."

Friday's economic report isn't likely to change companies' outlook for the economy or give them more reason to beef up hiring. The GDP data was in line with expectations, painting a picture of an economy that faces a reduced threat of falling back into recession but that is nonetheless plodding along at an unsatisfactory speed. "The pace of growth is still too weak to get a real recovery in the labor market... and that's the key ingredient to a sustained recovery that'll lead to more consumer spending and more support for the housing market," said David Regan, a senior investment specialist at JP Morgan Private Wealth Management in Los Angeles.

Weak economic growth expected through 2011

Survey sees little improvement in jobs, housing and the deficit.

Top forecasters say the economy will grow this year and next at a slower pace than previously thought, weakened by governments and consumers spending less so they can pay down debt.

That's the findings of a new survey released recently by the National Association of Business Economics. The 46 economists polled tempered their expectations after seeing weak expectation after seeing weak economic data in recent months. The panel reduced its forecast for annual economic growth to 2.6 percent in 2010 and 2011. That's down from its forecast of 3.2 percent in May. The economists expect the economy will add jobs through the end of 2011, but not enough to bring down the unemployment rate below 9.2 percent. They don't see home prices rising much or the nation's soaring deficit falling much.

The mainly downbeat report comes as persistently high unemployment, weak consumer spending and stagnant wages drag on the U.S. economy. The nation emerged last summer from the deepest recession since the 1930s.

But the economic recovery has not yet led to widespread job gains or growth. "This summer's slowdown has exposed the economy's sensitivity to wealth losses, the unwinding of debt, and the reductions in economic stimulus," NABE President elect Richard Wobbekind said in a statement. The NABE's Outlook survey is conducted four times per year. It compiles economists' big picture expectations for factors such as growth, hiring, home prices and spending. The economists work for industry groups, government agencies, banks and economic analysis firms.

The economy grew at a 1.7 percent annual rate in the second quarter, according to the government's latest estimate. That's a sharp slowdown from a 3.7 percent growth rate logged in the January-March quarter. Most economists expect growth to be similarly weak in the July - September quarter, with estimates ranging between 1.5 percent and 2 percent.

Consumer spending accounts for about 70 percent of economic activity. Economists told the NABE that consumer spending is likely to remain low over the next year. The housing market also will struggle, the economists said. Home prices will not rise enough in 2011 to keep up with inflation, and housing starts will remain near record lows, they said. Still, they expressed few concerns about inflation, deflation or so-called stagflation - a dangerous mix of rising prices and slow economic growth.

The economists expected hiring to increase at a painfully slow rate. They predicted the economy will add 150,000 or fewer jobs each month until the middle of 2011, after which the numbers will improve to about 175,000. Only then will the jobless rate begin dropping, from 9.6 percent to 9.2 percent, the economists said. The economy needs to add 125,000 net new jobs each month just to keep up with population growth. The biggest concern among the economists was the federal deficit. They predicted it will shrink by only about \$100 billion to \$1.2 trillion - a level the NABE called "extreme."

There were a few bright spots. Economists expected businesses to increase spending on equipment and software as their profits keep rising. Spending by businesses has helped keep up demand for goods from American factories, a vital sector for the economic recovery.

Growth will strengthen over the next three years, but not enough to bring unemployment back down to more normal levels of around 5.5 percent to 6 percent, according to the Fed's forecasts. At best, the Fed projects 3.6 percent growth in 2011, and 4.5 percent growth in 2012 and 2013.

The latest Fed projections also suggest no better than 8.9 percent unemployment next year, roughly 8 percent in the 2012 presidential election year and, at best, just under 7 percent for 2013. Under one rule of thumb, the economy would need to grow by 5 percent for a full year to push down the unemployment rate by a full percentage point. The Fed acknowledged that progress in reducing unemployment has been "disappointingly slow."

Cyber Monday sales top \$1 billion for first time

Free shipping and sales made it busiest online shopping day ever.

Americans jumped on deals and promotions offered online on Cyber Monday, spending \$1 billion and making it the busiest online shopping day ever, according to new data. Research firm comScore Inc. says revenue rose 16 percent from a year ago to \$1.03 billion on the Monday after Thanksgiving, the first one-day spending total above \$1 billion ever. Since the beginning of November, online sales are up 13 percent to \$13.55 billion.

Meanwhile, another company that tracks online spending, IBM's Coremetrics, found Cyber Monday sales rose 19.4 percent over last year. Cyber Monday was also PayPal's biggest day ever. Online payments rose 19 percent from last year. Though it is growing quickly, online spending makes up only 8 to 10 percent of total holiday spending.

The Cyber Monday figures come a day after a report showed American's confidence in the economy rose to a five-month high in November and is welcome news for retailers hoping that Americans start spending more freely. But shoppers are still holding out for bargains and spending cautiously as unemployment remains high. According to ShopperTrak figures, revenue at stores in shopping malls was flat over the weekend following Thanksgiving, but traffic rose 2.8 percent. ComScore said the number of buyers online increased at a slower rate than total spending, up 4 percent to 9 million. The average shopper spent 12 percent more, at \$114.24 each, according to the data.

Cyber Monday got its name from the National Retail Federation trade group in 2005 to describe the unofficial kickoff to the online shopping season. The idea was that people returning to work after the long weekend would shop at their desks. It never really was the busiest online shopping day of the year, but it has gained significance as sellers have trained shoppers to expect deals that day. Nearly 90 percent of U.S. retailers offered some kind of Cyber Monday promotion this year, compared to 72 percent in 2007.

While people used to shop at work to take advantage of broadband connections, the data shows even though broadband has become common at home, about 49 percent of the dollars spent at U.S. Web sites originated from work computers, down 4 percent from last year, comScore says. Buying at home rose just 4 percent to make up about 45 percent of dollars spent. International shoppers on U.S. sites made up the rest.

The fact that buying at work remains so prevalent suggests they are doing it "to shop for holiday gifts while minimizing the risk that their children, spouses and significant others might see" them shop, Fulgoni said.

Holiday Retail Sales

Shopping surge spurs higher holiday outlook.

A bigger-than-expected surge in holiday spending in November led a prominent research firm to raise its forecast for the season for the second time in a matter of weeks. The upgraded forecast by ShopperTrak follows an upgraded outlook from the National Retail Federation. The early buying surge is likely to offset a disappointing start to December.

ShopperTrak, based in Chicago, said it expects holiday sales to rise 4 percent over last year, up from a projection of 3.2 percent made in mid-November. The original estimate was for a 2.9 percent increase. ShopperTrak said November's revenue rose 5.8 percent compared with a year ago, as stores successfully pulled in shoppers with discounts. ShopperTrak had expected 3.7 percent.

The National Retail Federation now expects total holiday sales to rise 3.3 percent, 1 percentage point higher than the original 2.3 percent growth forecast. The increasing optimism comes as government figures released recently showed that retail sales for November jumped 0.8 percent over October, marking the fifth straight monthly gain. The increase was led by department stores, which posted a 2.8 percent gain.

Retail Sales November

Retailers see best November in four years.

Generous discounts lured American's to stores and online for holiday gifts in November, providing cheer and delivering the best gains for retailers in four years. That raises hopes, already buoyed by reports of crowded malls and early numbers, for a strong holiday shopping season and is an encouraging sign for the economic recovery.

The International Council of Shopping Centers' index reported a 5.8 percent gain, much better than the 3 to 4 percent increase expected. It marked the biggest increase since March when a quirk of the Easter calendar

resulted in a 9 percent gain. Aside from that month, the last time retailers reported such a big increase was in September 2006, when it registered 6.2 percent increase.

"All forces came together to yield a performance better than what we've seen in the last four years," said Mike Niemira, chief economist at International Council of Shopping Centers. November's sales results are being compared with weak spending over the last two years, but Niemira said that plenty of discounting along with what appears to be a sustained recovery is helping to boost spending.

As retailers report their monthly results, they showed that many types of shoppers were in the mood to buy - if the product and price were right. Stores reporting gains that topped Wall Street expectations included Costco Wholesale Corp., Target Corp., Victoria's Secret and pricey teen retailer Abercrombie & Fitch.

Others who topped expectations:

- Target Corp., with a 5.5 percent increase, above the 3.7 percent estimate.
- Limited Brands, which owns Victoria's Secret and Bath & Body Works, 10 percent increase, 4 percent expected.
- Macy's Inc. reported a 6.1 percent gain; analysts had expected 5 percent. The department store chain raised its outlook for fourth-quarter earnings and revenue at stores open at least a year.
- Teen retailer Abercrombie & Fitch, which had been hurt by young people flocking to less expensive brands during the depths of the recession, reported a robust 22 percent gain, far above the 6.8 percent estimate. That compares with a 17 percent drop in 2009 compared with the previous year. That's a strong signal that teen shoppers are ready to splurge, Perkins said.

Consumer confidence hits 5-month high

Americans' confidence in the economy rose to a five-month high in November amid more hopeful signs. The Conference Board, a private research group based in New York, said recently that its Consumer Confidence Index rose to 54.1 in November, up from a revised 49.9 in October. The November reading is the highest since June, when the index stood at 54.3. Economists surveyed by Thomson Reuters expected 52.0. September's index had been the lowest since February and was down sharply from 53.2 in August. It takes a level of 90 to indicate a healthy economy, which hasn't been approached since the recession began in December 2007.

One component of the index, how Americans feel now about the economy, rose to 24.0, up from 23.5. The other gauge, which measures how American feel about the economy over the next six months, rose to 74.2, up from 67.5 last month.

"Consumer confidence is now at its highest level in five months, a welcome sign as we enter the holiday season," Lynn Franco, director of The Conference Board Consumer Research Center, said in a statement. "Consumers' assessment of the current state of the economy and job market, while only slightly better than last month, suggests the economy is still expanding, albeit slowly. Hopefully, the improvement in consumers' mood will continue in the months ahead."

The index, which measures how respondents feel about business conditions, the job market and the next six months, has recovered fitfully since hitting an all-time low of 25.3 in February 2009. In October 2009, the index stood at 48.7. Since then, it has hovered in a tight range between the mid-40s and the high 50s. May 2010 was the only month when the index topped 60.

Economists watch confidence closely because consumer spending accounts for about 70 percent of U.S. economic activity and is critical to a strong rebound. But a rebounding job market is necessary for shoppers to feel like spending again.

There have been some encouraging signs. Americans' income rose 0.5 percent in October, boosted by a 0.6 percent rise in wages and salaries, according to a government report released last month. That was after incomes didn't rise at all in September.

November Auto Sales

Major automakers, except Toyota, show strong November sales gains.

All major automakers except Toyota reported strong U.S. sales increases in November as the auto industry's slow-motion recovery continued to gain traction. Ford, General Motors, Chrysler, Nissan, Hyundai and Honda all reported double-digit increases, and only Toyota, which has been hurt by a string of safety recalls, had a sales drop. Overall, according to Autodata Corp., U.S. sales last month rose 17 percent from November 2009, a month marked by consumer paralysis due to high unemployment.

The November performance helped an industry that is trying to recover from last year's historic lows as credit froze up and two major automakers slid through bankruptcy court. Sales started the year with promise, peaked in May as consumer confidence rose, fell off during the summer and now have started to rebound.

Industry analysts say the solid November sales numbers, combined with a strong October, show that consumers who have kept their jobs through the economic downturn are now feeling confident enough to spend money and replace older vehicles. Bob Carter, Toyota's top U.S. sales executive, said Toyota could tell things were shifting because buyers are opting for more highly equipped sport utility vehicles, which indicates they aren't buying just because they need family transportation. "At the beginning of the year, the vast majority of buyers were those who needed a car, versus wanted a car," he said.

Those who spent money last month also bought crossovers like the Chevrolet Equinox and the Hyundai Santa Fe. Midsize cars like the Ford Fusion and Hyundai Sonata also sold well. The increased sales are probably due to a combination of rising confidence and delayed buying as people replace vehicles they have kept for longer than normal during a severe auto industry downturn, said Bruce Clark, senior vice president of Moody's Investors Service. "There is a degree of pent-up demand that's being met gradually by people who have kept jobs and can go out and afford to do such things," Mr. Clark said. The sales are not as robust as historic highs from the early 2000s, but they are still a good sign for the industry, Mr. Clark said.

Yingzi Su, GM's senior economist, said the stable and increasing auto sales mean that consumers with jobs are starting to spend again, the start of an upward trend for automakers and a good sign for the broader economic recovery going into next year. Incentives such as sweet lease deals and rebates also helped push up sales last month. Automakers raised incentive spending about 6 percent over October to an average of \$2,712 per vehicle, said the auto website TrueCar.com.

Of the major automakers, Hyundai Motor Co. had the biggest increase, up 45 percent from the same month last year. Nissan Motor Co. sales were up 27 percent, followed by Honda Motor Co. at 21 percent and Ford Motor Co. with 20 percent. Chrysler had a 17 percent increase, while General Motors reported sales up 11 percent from November of last year.

Toyota sales dipped 3 percent, with the company blaming the drop on a 60 percent cut in sales to fleet buyers such as rental car companies. Mr. Carter said Toyota didn't want to match competitors' low prices on fleet vehicles.

Toyota said sales to individual customers were up slightly, but that they didn't increase as much as the industry average.

December Auto Sales

U.S. auto sales rose 11 percent in 2010

Toyota only major automaker to sell fewer cars last year than in 2009

Auto sales rose in the United States last year for the first time since the recession. They're still far from what they were just a few years ago — but that's just fine with the downsized auto industry, which can post profits even if it sells millions fewer cars and trucks.

For the year, new car and truck sales came in at 11.6 million, up 11 percent from last year, automakers reported Tuesday. For December alone, sales were 1.14 million, also up 11 percent from a year earlier.

While the figures have some in the industry talking about a return to the glory days, it's a fragile idea. Rising gas prices or more economic trouble could still shake the confidence of American car buyers.

But for now, executives are optimistic about this year. General Motors, Ford and Toyota all predict sales will come in at 12.5 million to 13 million for 2011. It will take years, analysts expect, to get back to the peak sales of last decade - more like 17 million.

"The economic downturn has lasted quite a while," says Jessica Caldwell, director of pricing and analysis for consumer website Edmunds.com. "It's going to be slow and gradual rather than a fast bounceback."

Toyota was the only company that sold fewer cars and trucks than in 2009. The company was stung by sudden-acceleration recalls in early 2010 and never fully recovered despite luring buyers with generous incentives. Production problems at its San Antonio plant cut its supply of Tundra and Tacoma pickup trucks, and troubles importing the Prius hybrid also hurt sales.

Over the past two years, many Americans, even those who had enough money to buy a car during the recession, had been wary to commit to monthly car payments, so they put off making such a large purchase. Many opted to repair or make do with what they had.

Those buyers are easing back into the market, replacing aging vehicles. The average vehicle on U.S. roads is now 10.2 years old — the oldest since 1997 and a full year older than in 2007, before the recession, according to the National Automobile Dealers Association.

"With 240 million vehicles out there on the road, a lot of them are going to be ripe for replacement," says Ellen Hughes-Cromwick, Ford's chief economist.

Auto sales peaked in 2005 at 17.4 million and bottomed out at 10.6 million in 2009. The peak was fueled, in part, by big incentives — like the employee-discounts-for-everyone schemes that were popular in the summer of 2005. But those deals may be a thing of the past.

Chipmakers bullish on next year

Survey shows that most expect increased revenue in 2011.

Despite the still sluggish economy, senior chip-industry executives generally are upbeat about 2011 and many are even planning to do some hiring, according to a survey released recently. Of 118 executives queried in September and October by the corporate advisory firm KPMG, in conjunction with the Semiconductor Industry Association, 78 percent said they expect their revenue to grow by more than 5 percent next year and 29 percent predicted their workers' ranks would increase by about the same rate.

That is noteworthy given what usually happens when chip sales surge in any given year, as was the case in 2010 when chip sales jumped 33 percent, said Ron Steger, a KPMG partner who specializes in the chip business. "If you look at the history of the semiconductor industry, whenever you have a year of growth of 20 percent or more, it is almost always followed by a year of double-digit decline," he said. Consequently, after seeing the survey results, he added, "I was surprised."

Overall, about 90 percent of the executives surveyed said they expected some revenue increase and 39 percent foresee their sales rising by 10 percent or more in 2011, said Gary Matuszak, another KPMG executive involved with the study. In addition, 37 percent expect their profit to increase by more than 5 percent next year.

"That was pretty optimistic," Matuszak said, noting that many of the executives planned to expand their operations in the United States, which suggests a significant number of their new employees will be added in this country. Asked which market sectors they expected to boost sales of chips next year, 68 percent of the executives cited wireless communication devices, 62 percent energy-efficient gadgets and 38 percent automotive products. In addition, 70 percent considered China the most important driver of chip sales in the next three years. But an increasing number of executives see Europe and the U.S. as important sources of revenue, too.

Still, experts generally agree the remarkable growth in chip sales experienced last year is tailing off. While worldwide sales for 2010 are expected to total \$300.5 billion, an increase of 33 percent over 2009, the increase should only be 6 percent in 2011 and 3.4 percent in 2012, the Semiconductor Industry Association predicted last month.

UCLA Anderson Forecast

No quick fix to state's jobless.

California will remain stuck at a historically high unemployment rate for at least two more years and any recovery will likely be spurred by the high-tech and health care industries, a report released recently says. By the time the final three months of 2012 roll around, California should manage a jobless rate of 9.9 percent, the UCLA Anderson Forecast said in a closely watched report. California's unemployment rate at present is about 12.4 percent. "It is difficult to be very optimistic about the near term," said Jerry Nickelsburg, a senior economist with the forecast. "On the job front, California has yet to make meaningful progress."

California must scale an economic Mount Everest. Since the recession began, the statewide employment loss has been about 1.3 million jobs. Yet through the first 10 months of 2010, California has added 48,000 payroll jobs, or an average of 4,800 jobs a month. Put another way, at that pace of per-month job creation, it would take 270 months, or more than 22 years, for California to get back to where it was in 2008 before the slump began. "These are scary numbers," said Christopher Thornberg, a partner with Beacon Economics, which tracks regional economies. "Things are in a bit of a mess." If job creation picked up to a robust 48,000 jobs a month, it would take more than two years for California to reach its pre-recession heights.

Other economists think California must traverse an even more forbidding financial landscape. Jeffrey Michael, director of the Stockton-based Business Forecasting Center at the University of the Pacific, said the state will not achieve a jobless rate below 10 percent even by the end of 2012. "We see things as being even weaker," Michael said. "The double-digit jobless rate in California will continue until the second half of 2013."

Among the key predictions for the UCLA Anderson Forecast:

- The unemployment rate, now at 12.4 percent, will drop to an average 11.4 percent in 2011 and an average 10.3 percent in 2012, before dropping to 9.9 percent by the end of 2012.

- Personal income, adjusted for inflation, will rise 1.4 percent in 2010, by 1.6 percent in 2011 and 3.6 percent in 2012.
- Taxable sales, on an inflation-adjusted basis, will increase 1.1 percent in 2010, 1.4 percent in 2011 and by 2 percent in 2012. "As compared to our forecast of last June, the current forecast is slightly weaker in the near term and slightly stronger in the long term," said Nickelsburg, the Anderson economist.

The collapse of the housing market was one of the prime culprits that unleashed the national and statewide recession. In California, those woes persist amid an economic recovery that a number of pundits trumpet. "The problem is one part of our economy, the housing and construction markets, have been hit so hard by the downturn," Thornberg said. "The other problem is California has such a high proportion of low-skilled workers."

He suggested numerous jobs that have materialized in the feeble upswing are beyond the skill sets of many unemployed workers. "Those low-skilled workers will find it hard to secure employment on the back end of this downturn," Thornberg said. "The recovery is too weak to carry these low-skilled workers."

Until housing improves measurably, California could remain mired in economic woes. "Housing and construction have gone nowhere," Michael said. "Nearly half of the jobless problems California has had are related to real estate and construction. Those industries are still lying flat on the floor."

Yet as brutal as things seem now, the future remains promising for California, the Anderson forecasters said. "We are seeing a restructuring of the economy in California that is laying the foundation for longer-term economic growth," Nickelsburg said. "The primary drivers of the long-term rebound in California will be high-tech and other sectors, he said. "There is growth in high-tech manufacturing, exports, logistics, and professional business services," he said. "They might not be hiring right now. But they are laying the groundwork to absorb a larger work force in the future."

Sources:

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