California Forecast Highlights

2019 Q4

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California's economic growth data was revised with a BEA data release on November 7th, 2019. This release included the results of the BEA's annual state GDP update. The 2014 to 2018 annual estimates were revised and the quarterly data was revised through 2019 quarter 1. The update incorporates more complete source data, updates to seasonal factors, and the changes to the US national income accounts (including GDP) that occurred in July.

California Economic Growth

	Previous	Revised
2010	1.6	1.6
2011	1.6	1.6
2012	2.5	2.5
2013	3.6	3.6
2014	4.0	4.1
2015	5.0	5.0
2016	3.0	3.0
2017	3.6	4.4
2018	3.5	4.3

Source: U.S. Bureau of Economic Analysis

The revisions imply that in 2017 and in 2018, California's growth was substantially higher than previously understood. The revisions indicate California's economy grew at 4.4 percent in 2017 and 4.3 percent in 2018, compared with 3.6 and 3.5 percent, respectively. Relatively slow job growth during these 2 years, compared to the prior 5 years, implies a strong productivity growth rate.

The list of countervailing positive and negative factors for California is longer and more complicated than for the United States. Our *US Forecast*, and *US Forecast Highlights* essays provide a thorough review of the various offsetting factors for the nation.

California has positives that the U.S. does not have including sublime weather, gorgeous beaches, mountains, and deserts, abundant natural resources, an educated workforce, a globally-leading technology sector, access to Mexico, and ports that provide a gateway to Asian markets.

Consideration of California's economic forecast requires asking if the trade war's negative impacts harm the state as much as they harm the nation. It does appear to be apparent in California's GDP data. The table below shows year-on-year GDP growth in the technology sector, alongside overall GDP growth.

California Real GDP Growth

	Overall - All Sectors	Technology Sector
2016 Q1	**3.4**	**16.4**
2016 Q2	**1.9**	**10.1**
2016 Q3	**2.9**	**12.7**
2016 Q4	**3.7**	**5.8**
2017 Q1	**3.2**	**6.9**
2017 Q2	**4.4**	**12.3**
2017 Q3	**4.5**	**10.7**
2017 Q4	**5.4**	**15.0**
2018 Q1	**4.8**	**13.7**
2018 Q2	**4.9**	**16.3**
2018 Q3	**4.1**	**10.6**
2018 Q4	**3.2**	**7.4**
2019 Q1	**3.4**	**5.6**
2019 Q2	**2.4**	**0.8**

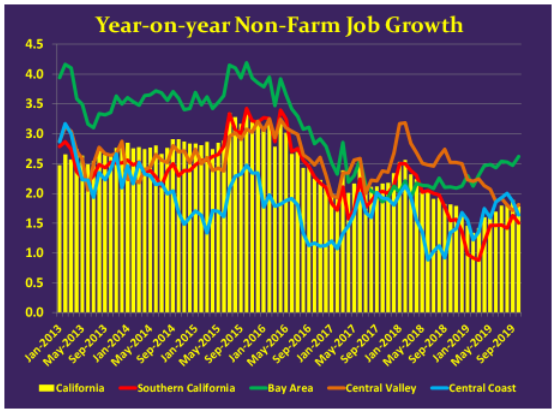
Source: U.S. Bureau of Economic Analysis

GDP growth in the state's technology sector has slowed by an amazing amount in the last five quarters for which we have data. From a rate of 16 percent in the second quarter of 2018, the latest estimated growth measure is less than a percent!

The timing of this slowdown coincides with the start of the trade war. As detailed in the nearby U.S. Forecast essay, the first wave of tariffs hit on July 6, 2018. U.S. Business investment dropped sharply as a result. We believe that the decline in California technology sector output is also (to a large extent) a result.

This just might be the canary in the coal mine for a more broad-based slowdown in California's overall economy. We have to allow for the possibility that the trade-war has played a key role in the slowdown that is apparently underway.

Considering the regional decomposition of activity using Non-Farm jobs as an indicator, most of the major regions grew with considerable strength from 2013 through 2016. However, during 2016, that rapid growth began a slowdown. By sometime in 2017, each of the state's major regions had experience a job slowdown of a full percentage point or more. Non-Farm job growth resurged a bit in the Central Valley and the Bay Area in early-to-mid 2018, and this resurrected the broader state's job growth rate a bit.



For the past seven months the only major region with strong job growth was the Bay Area. This is the geographic link with California's technology sector. How might this square with the dramatic slowdown in the technology sector GDP growth shown above? In many instances, jobs tends to lag GDP growth. To contextualize this a bit, it can take the HR department three months to come up with a new employee, even when management has provided an unconditional green light. Our guess is that the state's job growth will slow as well, in upcoming quarters.

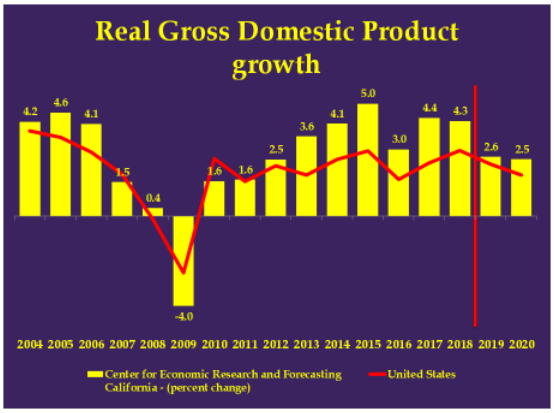
The Forecast

The state's economic forecast consists of a path of GDP growth that attempts to march through the many positives and negatives facing the economy.

Although data revisions show that the state was much stronger in 2017 and 2018 than

previously understood, GDP growth data thus far in 2019 appears to show that the state's economy is slowing down from the 2018 growth rate.

We forecast that the state's growth will exceed that of the United States but not by a large margin.



We believe that the net risks to this forecast are on the downside. This is based in two parts. First, theory and logic specify an eventual slowdown for the state relative to the nation due to the state's less economically forgiving policies. Second, the above discussed and dramatic slowdown in technology sector GDP is potentially a leading indicator for an overall economic growth slowdown.

One question is how well California's overall economy can perform despite the policy headwinds. Another question is if the state is more or less immune to the trade war. At the moment, it appears safe to say that the state's economy is at least as sensitive to the trade war, if not more.