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# Economy & Efficiency Commission
# Presentation

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*Editorial Note: Although every effort has been made to insure the accuracy of the material in this presentation, the scope of the material covered and the discussions undertaken lends itself to the possibility of minor transcription misinterpretations.*

**PRESENTATION BY**
**Dr. Ryan Ratcliff, PhD**

**Topic: The Past and Future Economic Performance of Los Angeles County**
**February 2, 2006**

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Chair Hill introduced Dr. Ryan Ratcliff and welcomed him to the Commission.

Dr. Ratcliff began by responding to an inquiry regarding whether the Anderson Forecast had looked into the economic consequences of the occurrence of a major disaster in Los Angeles County. Dr. Ratcliff stated that such a review had not been undertaken, but is being discussed as a theme for a future Anderson Forecast conference.

**The Los Angeles County Economy in 2005: Half Empty or Half Full?**

Dr. Ratcliff declared that in the first half of 2005, Los Angeles County had the fastest job growth since the recession of 2001-2003, although it only grew at a modest rate of 1.7%, with unemployment hitting a 15 year low of 4.5%. Through the second half of 2005, job growth stalled at 0.5% and unemployment rose to 5.5%. He also noted that the County has yet to recover all jobs lost from the previous recession.

Dr. Ratcliff explained that the largest area of job growth in the first half of 2005 occurred in information employment (19,500 jobs, a 20% growth rate and 13% of California's increase in non-farm payrolls during this period). Construction, leisure and hospitality, and retail also showed moderate growth. While Southern California has the largest concentration of manufacturing in the United States, durable and non-durable goods continued a slow contraction that has been the pattern for many years, losing about 5,000 jobs over the course of 2005.

In the second half of 2005 information employment lost about 15,500 of the jobs that had been gained. Dr. Ratcliff pointed out that about 63% of information employment is in motion picture and sound recording, with growth occurring in television show production. Approximately 100 of 134 prime time television shows are now produced in Los Angeles County. The cyclical growth and contraction in this sector follows the pilot production schedule.

The only sectors that did not slow down in the second half of 2005 were Administrative Services and Government. Growth in Administrative Services primarily came from temp agencies, which provide workers in clerical, transportation, and manufacturing jobs.

Commissioner Petak asked about the use of a “multiplier effect” analysis. Dr. Ratcliff preferred to use a “comparative advantage” analysis which looks at areas of specialization in a local area, noting that the idea that loss of jobs under a multiplier effect analysis assumes that an unemployed person will not find other work. Dr. Ratcliff did agree that high-end, high paying jobs do create a greater multiplier effect in dollars generated throughout the economy than low-end temporary or seasonal jobs.

Commissioner Parks asked about a possible “snail darter effect” caused by loss of large suppliers and industries. Dr. Ratcliff cited the recent departure of Nissan, and noted anecdotal evidence that many employees did not follow the company to its new location, but instead chose to find other employment and stay in the County. He emphasized that the high skill and educational levels of many of these employees aided them in the search for similar paying jobs.

**The Future of the Manufacturing Sector**

Dr. Ratcliff acknowledged that the manufacturing sector has traditionally seen cyclical employment patterns with recovery following recessions. Since the 2001 recession, however, the United States manufacturing sector has not recovered, and Los Angeles County has fared even worse. Dr. Ratcliff noted that this is an alarming picture because of dwindling opportunities for workers with only a high school education, and that service sector jobs with similar educational requirements offer substantially lower pay than manufacturing jobs.

**The Latino Impact**

Dr. Ratcliff discussed the heavy concentration of Latinos in three employment sectors in the County. Latinos hold 77% of all production jobs, 83% of building cleaning and maintenance jobs, and 71% of construction jobs. The continuing contraction in manufacturing, and the potential slow down in the real estate market will have a significant impact on the Latino population in the County.

**The Future of the Economy in 2006 and the Real Estate “Bubble”**

Dr. Ratcliff explained that taxable sales showed impressive growth in the fourth quarter of 2004, increasing 11.6%, with estimates showing similar growth continuing through 2005. Wages and salaries also showed increases but lagged behind taxable sales.

Dr. Ratcliff argued that low interest rates resulting from the 2001 recession spurred investment in housing, resulting in the current housing boom. The Anderson Forecast believes there is a housing bubble: the price of housing has lost its connection to fundamentals like income and rents, and that expectations of double-digit appreciation create a self-fulfilling prophecy. While Los Angeles County and the rest of California have not shown any signs of a housing slowdown, Dr. Ratcliff pointed out that San Diego County has seen falling sales and flat home prices since the middle of 2004. Dr. Ratcliff also pointed to the recent stock price declines in three leading home building corporations as a sign that investors believe the new home market has peaked.

He noted that housing bubbles usually deflate rather than burst: instead of collapsing like the price of a stock, home price either stay flat (like the recent trend in San Diego County) or gradually decline over a period of years. Previous price declines in California have always been accompanied by job losses; absent this kind of economic distress, sellers are content to wait longer and longer to receive what they think is a fair price. Dr. Ratcliff argued that the critical factor in whether a real estate slowdown would generate a recession is whether the national and local economies were vulnerable to substantial job loss in the next year.

Dr. Ratcliff then confirmed that the Anderson Forecast considers that a real estate slowdown is likely, and that while the California job base is vulnerable, particularly in construction, the slowdown will probably not generate enough job loss to cause a full recession. A drop in housing starts of 15% to 20% will probably mean a 1% to 2% drop in construction employment. However, Dr. Ratcliff points out that historically it takes job loss in two sectors to cause a recession – usually Construction and Manufacturing. Manufacturing has already been hard hit and may avoid further substantial impact, and growth in most other sectors is consistent with long-run trends. With major job losses in only one sector, the result will be a sluggish economy, with little payroll growth (1% or less) and a flattening of real estate prices.

Chair Hill opened the floor to questions.

**Questions and Comments**

Commissioner Petak considers that the lack of savings and high debt ratios of many homeowners would lead to foreclosure in the event of unemployment. Dr. Ratcliff elaborated on newer financing methods some buyers employ such as negative amortization and adjustable rate mortgages with short-term “teaser” rates. He also recognized that the reliance on being able to refinance and cash out equity has resulted in unwise spending and investment practices. While a cause for concern, Dr. Ratcliff stopped short of predicting a major wave of foreclosures.

Commissioner Padilla commented that the national debt had risen to approximately $200,000 for every US citizen and asked what effect this would have on the future of the economy. Dr. Ratcliff felt that while excessive government borrowing normally drives up interest rates by increasing demand for scarce sources of borrowing, the current willingness of Asian central banks to buy up government debt has kept the supply fluid, interest rates relatively low, and prevented the lack of savings in the United States from having a major impact.

Commissioner Petak reiterated his concern about the vulnerability of the County economy to a major disaster. Dr. Ratcliff recognized this and said that the Anderson Forecast, while not predicting robust economic growth, has a relatively positive outlook. Factors such as significantly higher interest rates, a national recession, or the occurrence of some other major event could significantly darken the picture for Los Angeles County, causing across the board job loss and declines in home prices.

Commissioner Petak asked what the County could do to improve its economic future. Dr. Ratcliff stressed that jobs providing middle class incomes today have higher educational requirements, and that over 20% of the County’s population has less than a high school education. The County needs to find ways to narrow this disparity.

Commissioner Parks asked Dr. Ratcliff for his views regarding the distribution of wealth and the pressures on the middle class. Dr. Ratcliff replied that historically most investment money has come from the wealthiest members of society. Although this growth has not been spread out equally among all segments, it is unlikely that a major redistribution of wealth will take place.

Chair Hill thanked Dr. Ratcliff for his thoughtful and enlightening presentation.

Return to Top of Presentation

Return to Agenda

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