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KERN ECONOMIC JOURNAL

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In This Issue…

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KERN ECONOMIC JOURNAL is a quarterly publication of California State University, Bakersfield. Its purpose is to track local trends and analyze regional, national, and global issues that affect the economic well-being of Kern County. The journal provides useful information and data that can help the community make informed economic decisions.

We wish to gratefully acknowledge the Journal sponsors:

KERN ECONOMIC JOURNAL is a quarterly publication (February, May, August, November) of California State University, Bakersfield. Its purpose is to track local trends and analyze regional, national, and global issues that affect the economic well-being of Kern County. The journal provides useful information and data that can help the community make informed economic decisions. Sources of funding for the journal include university contributions and sponsorship and subscription fees.

Editorial and analytical articles on important local, regional, national, and international issues and trends are invited for *consideration* of publication in the journal. Articles (not exceeding 800 words in length) must be submitted to the Managing Editor in hard or electronic copy. Individual authors are responsible for the views and research results.

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INSIDE THIS ISSUE:

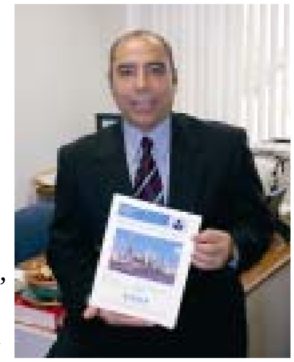
Econ Brief!

Economic Status of Women in California

Women make up nearly one-half of California's labor force of more than 18 million workers. A recent study published by the Public Policy Institute of California reports considerable improvement in the economic status of women. The study finds a greater rate of workforce participation, increased annual earnings, and more active participation in social and cultural events. However, the study indicates that women still earn less than men, single mothers with small children have low work participation rates, and many women still live in poverty and lack health care insurance. The highlights of this study are as follows:

- Women have greater levels of educational attainment than men at the college level.
- Women earn approximately 80 cents for every dollar men make as they spend more hours raising children and work in lower wage occupations than men.
- Nearly 30 percent of married women earn as much or more than their husbands.
- More than 10 percent of all women live in poverty and 28 percent of single mothers earn less than the federal poverty line.
- Full-time care for preschool children consumes a large percentage of women's earnings.
- Foreign-born Hispanic women have the lowest work participation rate largely because they, on average, have more children and a lower level of education.
- The concentration of women in the ten most common female occupations (e.g., teaching, nursing, and office management) has dropped in the past two decades.

LETTER FROM THE PUBLISHER



Last quarter, we sent complimentary copies of the Journal to 1,700 local businesses in order to disseminate the information that you may find helpful in making more informed decisions. This quarter, we continued our promotional campaign by contacting some of the local businesses that expressed interest in supporting the Journal. We are pleased to welcome four new sponsors: Manco Abbott Real Estate Management, Houchin Community Blood Bank, Willits and Newcomb, Inc., and Extended University Division of the CSUB. In addition, we have been asked to edit a companion economic journal for publication by the Tulare Economic Development Corporation. We will continue our marketing efforts to expand the Journal's subscription and sponsorship base.

Our assessment of Kern's economic conditions is summarized as follows:

Kern County's economy has shown signs of improvement in the fourth quarter of 2004. Businesses and households have remained optimistic about local economic conditions. The economy added $90 million of personal income and expanded at an annual rate of 2.4 percent. In the meantime, labor productivity inclined $200 or at an annual rate of 1.7 percent.

The labor market data were mixed. The rate of unemployment climbed 0.7 percent to reach 11.4 percent, whereas nonfarm employment increased at an annual rate of 1.3 percent. Among the nonfarm industries, retail trade, professional and business services, and local public education added jobs. However, construction, manufacturing, and leisure and hospitality reduced employment. Weekly wages paid to local manufacturing workers inclined $7 to reach $606.30.

The median housing price appreciated $6,500 (or 3.5 percent) to reach $186,800. In dollar value, housing prices appreciated more than the county average in Bakersfield, California City, Delano, Ridgecrest, Rosamond, Taft, and Tehachapi. Lower mortgage interest rates helped the construction and real estate boom to continue in the county.

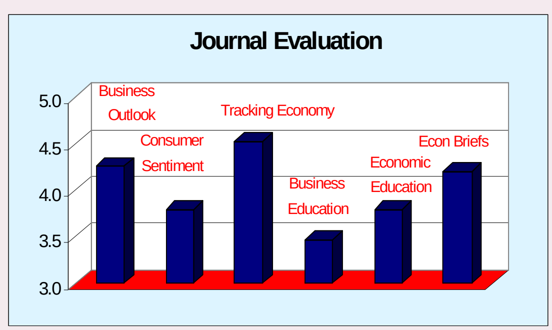
Higher oil and gasoline prices fueled inflation in the market for consumer and producer goods and services. Output prices

For Your Information:

Kern Economic Journal has been published since the first quarter of 1999. The idea was originated in 1995 when Mr. Jeffrey Johnson asked Dr. Mark Evans to track local economic indicators. Subsequently, Mr. Johnson secured a grant from *The Bakersfield Californian* to fund a project of tracking six local economic indicators. This project was evolved into the publication of a quarterly journal.

Kern Economic Journal is funded by community sponsorship and subscription funds and subsidies from CSUB Foundation and Office of the Provost. The main features of the Journal are two telephone surveys assessing the business climate and consumer confidence, tracking local economic indicators, and invited community articles. In addition, the Journal includes three features of business education, economic education, and current economic issues.

Last quarter, we asked the Journal sponsors and subscribers to evaluate the above-mentioned sections of the Journal in terms of their usefulness for business decision making. On a scale of *1: not useful at all* to *5: very useful*, the survey results are summarized in the following graph.



The Kern Business Outlook Survey received an average score of 4.3 and the Bakersfield Consumer Sentiment Survey obtained a rating of 3.8. The Tracking Local Economy section had the highest evaluation score of 4.5 and *Econ Briefs* made a mark of 4.2. Business Education received a score of 3.5 and Economic Education obtained a rating of 3.8.

The survey results confirm the supporting comments we have received about the usefulness of the Journal content. Our goal is to bridge the economic information gap in our community. Your support has made our efforts very rewarding. Thank you!

KERN COUNTY BUSINESS OUTLOOK SURVEY

ABBAS P. GRAMMY
PROFESSOR OF ECONOMICS, CSUB

Business decisions are made with respect to both internal and external factors. Internal factors include data on the financial viability of the firm and external factors depend on the evaluation and expectation of the economic outlook. Optimistic managers plan for expansion of their operations by hiring additional labor, buying more equipment, or adding extra space. Additional dollars spent on business expansion would place more dollars in the hands of consumers, hence creating additional dollars and adding new jobs.

In the fourth quarter of 2004, we measured a high degree of optimism about local economic conditions. We administered telephone surveys to a random sample of private-sector managers and public-sector administrators across the county, asking each two sets of questions. Each set included four questions, one set regarding the assessment of local economic conditions in the current quarter and the other set in the forthcoming quarter.

Employment Outlook - The majority of survey respondents (69 percent) reported that the number of jobs in their companies stayed constant this quarter. Fifty-one percent expected the number of jobs to remain unchanged next quarter.

Financial Outlook – More than one-half of the survey respondents reported improvements in financial conditions (sales or profits) of their companies this quarter and expected such improvements to continue next quarter.

Industry-wide Business Outlook – About 70 percent of survey respondents perceived that employment and general business conditions of their industries stayed constant this quarter. They anticipated that these conditions would remain constant next quarter.

County-wide Business Outlook – Nearly 60 percent of survey respondents perceived no improvement in local business conditions this and next quarter.

Business Outlook Index – We enumerated the survey responses to construct the Business Outlook Index (BOI). The index value greater than 100 expresses *optimism*, and less than 100 *pessimism*. The BOI fell 10.4 percentage points from 136.8 in the third quarter to 126.4 in the fourth quarter. These numbers indicate that business managers remain *optimistic* about local business conditions, but their degree of *optimism* has slightly declined. However, the BOI was 10 percentage points higher than that of four quarters ago.

Furthermore, we calculated the index for each of the two sets of questions. The Index of Current Business Conditions had a value of 130.8 and the Index of Future Business Conditions measured at 122. These index values confirm the survey results that the survey respondents are *optimistic* about local economic climate. Like the previous quarter, we found that the survey respondents were less optimistic about business conditions in the next quarter.

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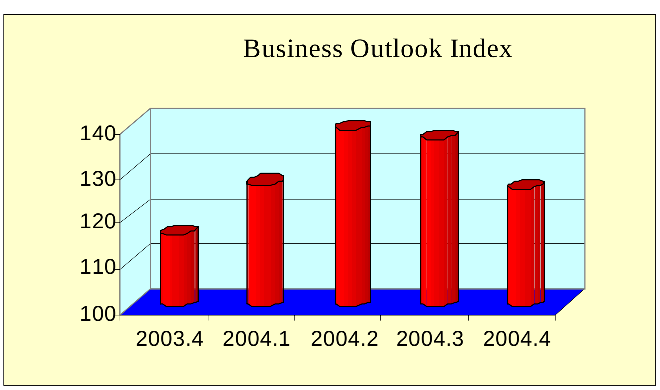

INDEX VALUES			
	Most Recent Quarter	Previous Quarter	One Year Ago
Business Outlook Index	126.4	136.8	115.8
Index of Current Business Conditions	130.8	142.3	103.4
Index of Future Business Conditions	122.0	131.3	129.3

BAKERSFIELD CONSUMER SENTIMENT SURVEY

MARK EVANS
INTERIM DEAN, EXTENDED UNIVERSITY DIVISION AND PROFESSOR OF ECONOMICS, CSUB

As sales levels change, a business leader must ask, "To what extent are my company's trends the result of changes in the overall economy and to what extent do they result from changes in my competitive position?" Unfortunately, companies serving the local market do not have access to sufficient economic data when pondering this question. For example, quarterly data on taxable retail sales typically is not available at the county level for the <u>four</u> previous quarters. Income data is not even published on a quarterly basis at the county level and annual data beyond <u>2002</u> has not yet been released! To help decision makers assess local economic conditions, CSUB began compiling the Bakersfield Consumer Sentiment Survey in 1999 from telephone surveys administered to a random sample of households listed in the phone book. Consumer sentiment indexes have been shown to embody information about current economic conditions as well as future short-term changes in the economy.

The Bakersfield Index of Consumer Sentiment reached a value of 144 in the fourth quarter. This is the highest level since CSUB began compiling the index in 1999, considerably higher than the 115 reading in the third quarter. The previous high was 143 in the fourth quarter of 2003.

The index is disaggregated into sub-indexes relating to recent trends and future expectations. The sub-index measuring recent trends is constructed from responses to questions relating to expenditures on discretionary items, financial status of the household compared to one year ago, and perceived changes in the financial condition of acquaintances in Kern County. This sub-index attained a value of 126 in the fourth quarter. The sub-index registers a value this high only 5 percent of the time. Only nine percent of the households reported that they spent less than usual on discretionary items in the fourth quarter after adjusting for seasonal factors. In the third quarter, 28 percent reported spending less than usual. Only five percent reported that their household was worse off financially compared to one year ago, whereas nearly 20 percent of those surveyed in the third quarter reported being worse off. Only two percent thought that the financial situation of their acquaintances in Kern County deteriorated in the past year.

To assess future expectations, households are asked how they think the financial situation of their families will change over the coming year, how their acquaintances in Kern County view the coming year, and whether this is a

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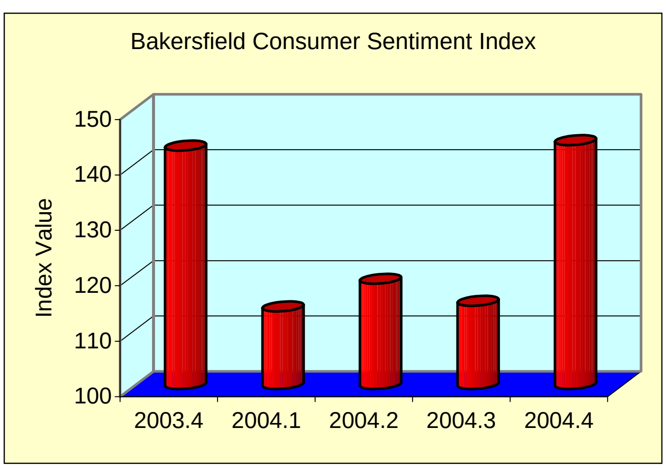

INDEX VALUES			
	Most Recent Quarter	Previous Quarter	One Year Ago
Consumer Sentiment Index	144	115	143
Index of Recent Buying & Financial Trends	126	107	130
Index of Consumer Expectations	161	123	155

Consumer Sentiment *(Continued from page 4)*

safe or risky time to draw down savings or incur debt. The sub-index measuring future expectations attained a value of 161 in fourth quarter, the highest level ever recorded. In third quarter, the future expectations sub-index stood at 123, an average reading. There were very few pessimists. Only one percent expected the financial situation of their family to worsen over the next year. Almost two households expected financial improvement for every one that expected things to stay about the same. Only one percent perceived their acquaintances to be pessimistic about the coming year with the remainder being almost equally divided in expecting improvement and expecting no change. Only three percent thought this was a risky time to use savings or incur debt, compared to 40 percent in the previous quarter. Three-in-four respondents thought it was a safe time to make a major purchase.

Summarizing, the Bakersfield Index of Consumer Sentiment attained the highest level since CSUB began estimating it 24 quarters ago. Pessimism is nearly nonexistent. For every question on the survey, the frequency of pessimistic responses was less than 10 percent.

Survey Results	More than usual	Same as usual	Less than usual
Your recent spending on discretionary items (dining out, weekend outings, entertainment)	46%	45%	9%
	Better off	Same	Worse off
How your family is doing financially compared to one year ago.	30%	65%	5%
How your acquaintances in Kern County are doing financially compared to one year ago.	19%	79%	2%
	Better	Same	Worse
The most likely financial situation of your family one year from now	63%	36%	1%
	Optimistic	Neutral	Fearful
How your acquaintances in Kern County view the coming year.	51%	48%	1%
	Safe	Same	Risky
Is now a safe or risky time for most people to use savings or incur debt to buy expensive goods?	75%	22%	3%

Business Outlook *(Continued from page 3)*

Factors Affecting Business Outlook – We also asked the survey participants to comment on local, regional, national, or international factors that have affected employment and financial conditions of their companies. They felt several factors brightened the local business outlook:

- Greater local spending for the November elections
- The holiday season helping with retail sales
- Growth in local construction and services industries

However, the survey respondents expressed the belief that several factors darkened the local business outlook:

- High fuel costs
- The winter season lowering agricultural activity
- The high cost of war in Iraq

In conclusion, our survey results show that local decision-makers have remained optimistic about the local economic climate. However, the degree of business confidence has declined for the second consecutive quarter.

WHEN WILL THE HOUSING *BUBBLE* BURST[1]

HENRY LOWENSTEIN
DEAN, SCHOOL OF BUSINESS AND PUBLIC ADMINISTRATION AND PROFESSOR OF MANAGEMENT, CSUB

The news media blares headlines foretelling a burst in a purported price bubble in the local real estate market for residential units. Good headlines, however, do not crises make. I assert there is no bubble. A price bubble is classically a large speculative run up in price where there is no underlying intrinsic value for the asset other than irrational speculation. This phenomenon was witnessed in the so-called "Dot Com" industry in the late 1990s. If indeed we are not witnessing a bubble in the real estate market, then there is nothing to burst. Instead, what we observe is a classic rise in price based upon supply and demand interaction, particularly rising demand.

The demand side factors contributing to Kern County housing price increases include (1) a growing and maturing population; (2) a sustained increase in personal income; (3) a higher rate of return on real estate investment relative to other assets; and (4) spillover effects from other California housing markets, most notably the Los Angeles area. Homeownership is a national tradition and supported public policy. With recent low rates of return in equities, households prefer investment in housing because of real estate's performance. Real estate price fluctuations in a diversified economy tend to be less risky in a downturn than in a specialized economy, hence a better prospect for value stability.

According to the Federal Reserve Board, nearly 20 percent of the household wealth in the United States is in home equity for a total of $7 trillion. In contrast, household investment in the stock market totals $2.6 trillion. On the supply side, there is a local imbalance due to higher construction costs and regulatory constraints that impede the industry from balancing inventory with consumer demand. The imbalance between demand and supply has placed an upward pressure on housing prices and this pressure will continue for the foreseeable future. A secondary demand factor is the trend of Southern and Eastern Kern areas to become "exurb" communities for an already constricted Los Angeles area market. Greater Bakersfield is rapidly becoming a bedroom community for Northern Los Angeles County with median home prices nearly half those found in Los Angeles.

One error by the media is to view the real estate market as a national one. This is not the case. Like politics and the weather, real estate markets are particularly local in character and dynamic in local price variations. Across the country, there is a real estate boom in some regions and poor real estate markets in other regions. While California and Florida have experienced unprecedented price increases, towns losing major industries are in a real estate downturn, for example those in the traditional textile and furniture belt in the South and manufacturing areas in the Northeast and Midwest. Regional sales in November 2004 reveal a boom in the West, a leveling in the Midwest, and a slump in the Northeast:

- West +6.5%
- South +1.8%
- Midwest +0.7%
- Northeast -1.3%

Local real estate markets are affected by some national factors, primarily tax policy; Fed interest rate policy; availability of loanable funds; government regulatory actions; and general economic growth elements.

In California, there are nearly 35 million people. It remains one of the fastest growing states in the U.S. in terms of population and economy. People want to live here. The source of population growth is both internal (i. e., natural increase) and external (i.e., migration). The California State University System, the largest in the world, enrolls nearly 450,000 students and is looking at nearly 400,000 more students over the next 10 years. The system could not create 50 CSUB-size campuses to handle the growing population of college students. Real estate markets are similarly impacted.

California home sales are roughly 600,000 units a month or 7.2 million units a year. This is equivalent to two Los Angeles's populations a year! Nearly 26 percent of the households are first time homebuyers. California has wide variations in housing demand, available land, hous-

(Continued on page 7)

[1]This is the revised version of a speech given at the Bakersfield Association of Realtors Breakfast on Friday, January 21, 2005.

Housing Bubble *(Continued from page 6)*

ing stock supply, and hence, housing prices. This year the National Association of Realtors projects a 3 percent increase over last year's record sales. The California median price for a single family home is $465,540, up 22 percent, continuing three years of double-digit appreciation. The median housing price, as of November 2004, varies across the state:

- Bay Area $642,360
- Southern California $460,000
- Central Valley $293,770

Fresno, with a median housing price of $251,950, has recorded a 42.8 percent price increase, the largest price increase in the nation. Bakersfield's median housing price of more than $260,000 is up 37 percent, the 6th fastest in the county.

Before we cheer the housing "affordability" of the Central Valley, at half the cost of a Bay Area home, we should recognize that the national median home price is approximately $188,200. Hence, California housing is priced 148 percent above the national average and the Central Valley priced 56 percent above the national average. This is a long-term negative factor to employer relocation decisions for California or Kern County vs. other areas of the U.S.

The California real estate market includes both the generations of *boomers* and the *retirees*. A typical market seller is married; is 47 years old; has $135,000 of household income; and has previously sold home. They are:

- 50 percent between 45 and 54 years of age
- 88 percent stay in their original county
- 30 percent selling for investment or tax reasons
- 24 percent move for change in family status

Kern County has also experienced an unprecedented real estate boom. When I arrived here in 2000, the median housing price was $98,000; today it is nearly $300,000. What is going on here? Consider the following reasons for the price hikes:

- Population growth is increasing relative to housing inventory
- 14th largest county in California (Bakersfield is the 11th largest city)
- Rapidly growing (21.7 percent in 1990-2000) and shifting (Coast to Central Valley) populations
- Massive in-migration from other parts of the state and foreign countries
- Diversified employment: Kern County is no longer a boom-bust economy with oil and agriculture. The local workforce has grown at 11 percent a year
- Close proximately to Los Angeles-Long Beach metropolitan area with rapid urban spiral in northern LA county
- *Baby Boom* generation in peak of family and income earning years. The first wave of the *Baby Boomers* is retiring and cashing out of coastal California. The first edge of Generation X (larger than the post WWII Baby Boom) is just entering income and family years.
- Affordable cost of living in Kern County relative to coastal California

Real estate investment will remain strong for the foreseeable future, but we need to be aware of long-term trends that may adversely affect the industry and have an impact on slowing future real estate growth:

Rising mortgage interest rates – Most economists feel the market will retain strong growth until mortgage rates hit 8 percent or higher. Currently, the thirty-year conventional mortgage rate is around 5.5 percent with lower rates for adjustables. While the Federal Reserve System is raising short term rates, mortgage rates are affected by the Treasury bond yield (currently around 4.2%). As long as the bond market is healthy, yields will remain low.

Tax policy – Since real estate investment is the major private store of household wealth, any negative impact on tax codes will impact home ownership. Indeed, deductibility of home mortgage interest and taxes is a government subsidy to encourage homeownership. Removal or limitation of this subsidy would negatively affect demand for both mortgage and construction loans.

Diversified economy – Kern County is no longer solely an oil or farm economy. Our economy is increasingly diversified with large services and manufacturing industries. Hence, a major downturn impact would not increase business risk as much as was the case in the recession of the early 1990s.

Inventory – Currently, homes in the market are sold in an average of 29 days; a near record low. Local contractors point to a limited availability of lots, a longer time of construction due to longer permit time and labor and material shortages. As long as there is no overbuilding, high prices would hold. We can, however, expect to see some leveling of the rate of increase as increased supply comes on the market.

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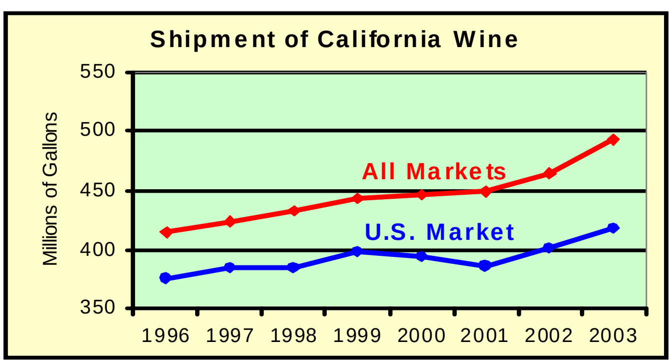
THE CALIFORNIA WINE INDUSTRY

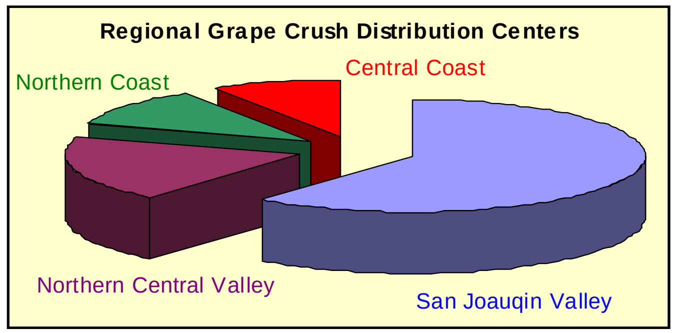
SERENITY RADNEY
CSUB GRADUATE, ECONOMICS

The California wine industry is the focal point of the United States wine industry as it accounts for more than half of the U.S. production and is still rapidly growing. The growth of domestic wine sales has been strong in the past few years with California being the leading state in production and consumption. According to industry experts, this growth is a result of higher demand, a concentration on quality, and better marketing campaigns.

The most recent complete statistics of the wine industry were released in the spring of 2002, stating that the economic importance of wine was $33 billion to the state of California. At the time, California was producing approximately 464 million gallons of wine, which was 90% of all U.S. wine production. Forty-five of California's 58 counties are growing wine grapes, covering more then 565,000 acres. If California were a nation, it would be ranked the 4th leading wine producer, falling close behind Italy, France, and Spain respectively. Accordingly, wine was given the title of California's most valuable finished agricultural product. As illustrated in the following chart, the shipment of California wine to all markets had a rising drift from about 415 million gallons in 1996 to 494 million gallons in 2003. In the meantime, California wine shipment to domestic markets inclined from 376 to 417 million gallons. The difference between these two figures measures California wine exports, which nearly doubled from about 39 to 76 million gallons.



The U.S. has been found to be the best place in the world to grow grapes for two fundamental economic reasons. First, the technology and weather in the domestic premier growing areas rival that of France and Italy because they are so similar. Napa Valley and Sonoma Valley, California's number one and two wine producing regions, are huge tourist attractions which boost the market with a constant source of customers. San Joaquin Valley (61%) is the leading region in the distribution center of grape crush within California. Other grape crush distribution regions include North Central Valley (19%), North Coast (11%), and Central Coast (9%).
Second, American wineries, especially in California's Napa and Sonoma counties, interact in strong competi-



tion which results in continuous changes in the product quality and rising prices. Other wine producing countries do not have such a large market base and rarely compete against each other simultaneously for an expensive, non-durable consumer good. The U.S. also differs from French and Italian producers with wine sales and production that concentrate on bulk sales rather than quality over quantity.

Product Differentiation

Product differentiation drives competition in the growing market of wine sales and production. There are two main ways in which firms of the U.S. wine industry differentiate themselves. In response to competition, first, there is the continuous change made to the product. The chemistry of the wine may rarely change, but rather it's the marketing and the story surrounding the wine that is changed towards consumer preference. Second, wineries offer different "wine segments" (expanded on in the following section) which change the competitive forces of their brand. Smaller wineries have a tendency to cater towards those looking for low-priced wine while still seeking superb quality. Thus, these smaller wineries sacrifice their competitive advantage, or how the firm adds value through specific functions, to the foreground in order to produce a good value with excellent quality wine.

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***Wine** (Continued from page 8)*

Another way in which the firm differentiates its product is by matching food and wine. Firms are continually trying to make wine more attractive as a complement to food, similar to European meals. When the consumer's philosophy about the good is changed, the firm persuades the consumer to purchase based on the purchase of other goods.

The Market Structure

The domestic wine industry has five specific demand segments that are primarily concerned with price. When the consumer believes that price and quality are correlated, then these segments separate wines by perceived quality. The 'economy wines' are dominated by large domestic firms that produce in bulk. These wines are sold in bottles or boxes of more than 1.5 liters (the common wine bottle is 0.75 liters) with no smaller quantities available. Economy wines are most often purchased by consumers who drink wine with most meals and use wine as a compliment to food. 'Sub-premium wines' sell in lower-volume bottles at a low cost and are a varietal-specific alternative for everyday use. 'Premium wines' are inexpensive and varietal-specific as well. Many premium wineries use lower-quality varietal fruits to produce their wine. 'Super-premium' and 'deluxe wines' are where the market takes a major separation.

Large firms are not as dominant and no one firm dominates the industry. There is more precision, more care over the fruit source, and different production and marketing policies in these segments. Smaller quantities are produced and sold at a higher price. Super-premium wines are always varietal-specific and are mainly sold on the premises of the winery itself. These wines are consumed with complementary goods and not on a regular basis. Napa Valley and Sonoma Valley specialize in super-premium and deluxe wines. A big difference between these wines and the lower grade ones is that the marketing campaign builds an image based on the production process and location in which these wines are sold.

The Nature of Competition

California's wine industry is competitive primarily because of three key aspects of the market structure of California's wine industry. These key aspects are differentiation, the firm's ability to determine price, and the global nature of competition. Because of the number of firms in California, any claim of oligopoly is somewhat absurd. There certainly are market leaders but these leaders only control prices in certain market segments, mostly economy and sub-premium. The remaining segments, premium, super-premium, and deluxe, are extremely competitive, and become more competitive with each passing year. The ability to compete is tied to recognizing threats and reacting optimally, but California firms have not realized the threat of new entrants in the international arena, so is the California wine industry still competitive? Some say no; they believe California's wine industry is monopolistically competitive rather than contestable because California wineries react quickly to competition. This ability to differentiate signifies a monopolistically competitive market. Either way, we know that the California wine industry is not oligopolistic in nature but rather competitive with some slight monopolistic behavior in certain segments.

In the U.S., most wine production is controlled by large companies who produce many of their own brands of wine. While the dominant brands do shift, the strong companies stay at the top. Recently in the industry there has been a movement toward consolidation, as the large firms on top buy smaller wineries and add them to their collection of brands. A notable development in the industry's structure is the recent formation of partnerships between U.S. and South American wineries. In recent years, several domestic wineries have made investments in Chile, responding in large part to a grape shortage in the U.S. in 1996 and 1997.

The Foreign Market

The wine industry is very much global and like much of American culture, the wine industry first began overseas and eventually made it's way to the U.S. Traditionally, wine has been rooted in strong varietals coming not only from California but other distinct regions of the world as well. Such regions are the French regions of Burgundy and Beaujolais, Italy and Greece, Spain and Portugal, Australia and New Zealand, or Brazil and Chile.

Internationally, the wine industry relied on exports to increase sales in the past. More recently, however, the wine market has evolved into a global, marketing-oriented industry. Demand that was created by positive health messages, strong economies, and earlier supply shortages in Australia, California, and elsewhere initially pushed winemakers to seek new supply deals in foreign markets. The global wine market is now alive with international joint ventures, global consolidation, and increased branding. Marketing strategies have fueled a shift in market philosophy from old world (regional) wines such as those from Western Europe to new world (branded varietal) wines such as those from the United States, Australia, Chile, Argentina, and South Africa. Although new world wines still have a relatively small global export share, 12.5%, there has been growth since 1990, when these wines accounted

(Continued on page 10)

Housing Bubble *(Continued from page 7)*

Affordability - Californian realtors will have to address the issue of home price affordability. The national affordability index is 54 percent; the state index is only 19 percent and the county's index is 34 percent. Here in Kern County, median family income is $38,600. How can you qualify for a $300,000 home? Increasingly, the gap threatens the ability of families to find affordable housing and impacts locational decisions by businesses creating jobs in this area.

Some of the factors that have contributed to low affordability are:

- **Construction technology/productivity -** We are still building homes as it was done 100 years ago. If the auto industry operated this way the average car would cost $150,000, not $25,000. We need to look at new ways, new materials, and innovative techniques in construction to reduce costs without sacrificing quality or safety standards.

- **Regulatory actions -** We need to balance environmental factors with the need for housing. We must plan infrastructural requirements in advance of suburban growth. The trend of ever increasing impact fees must be examined. These fees are merely passed on by builders directly into the base price of homes.

- **Building codes -** We need to streamline and maintain safety and building integrity at reduced costs as well as keep them up to date with modern innovations and technology.

- **Transaction costs -** If buying an automobile were like buying a house, the auto industry would be bankrupt. Think of the paperwork, time and cost. A 30-day escrow is considered fast. One day some innovative title or real estate company will become the *Southwest Airlines* of real estate, find a way to close a home at a fraction of the paperwork and cost of today and revolutionize the industry. If change is inevitable, the industry is well placed to plan its transformation to minimize rapid shocks to the system.

- **Internet –** Over 56 percent of home buyers and sellers use the Internet in some way in their home buying process. Most counties now have all key data on electronic data bases. Do we still need to do title searches? Are all the documents necessary to be signed or can we refine the legal disclosure processes? Can the process be streamlined and consolidated? Are there states with better models? That is the challenge for the future of real estate businesses and the industry. History tells us that those who do not prepare will be left out. In theory these improvements could reduce the cost basis of a new home by almost 25 to 33 percent.

Home ownership is the American dream. That really distinguishes us from the rest of the world. We need to make sure in our zeal to create governmental regulations (e.g., taxes, environment and social issues) that we do not ruin this dream for future generations. California cannot afford to have home ownership become affordable only by the wealthy or those who just happened to get in the market before the boom.

Wine *(Continued from page 9)*

for only 5% of world exports. In the U.S., exports have been increasing. Between 1992 and 1996, wine exports increased more than 130%, reaching 8% of total world production, up 4% from 1992.

Conclusion

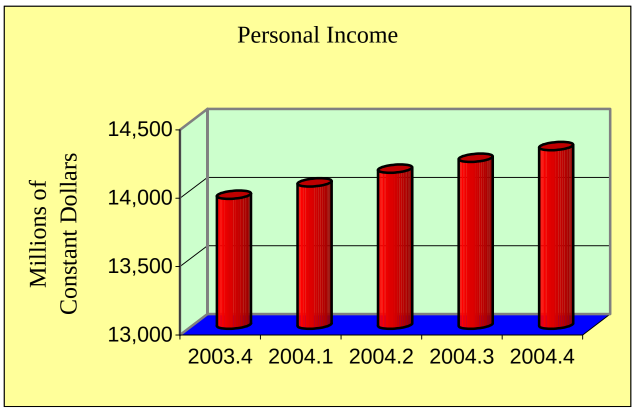
Ernest Hemingway once wrote that "Wine… offers a greater range for enjoyment and appreciation than possibly any other purely sensory thing which may be purchased." For this reason, people are willing to pay a high price for premium wines. Many entrepreneurs have recognized this market and entered hoping for their 'piece of the pie.' The California wine industry will continue to grow well into the future with new winemakers, new varietals, and new technology to make the process even more efficient than it already is. The industry is differentiated, so some growers and wineries may do quite well while others struggle to compete. California's firms must recognize the threat of the international market and adjust their marketing, public relations, pricing, and varietal choices to protect their competitive advantage. The key to controlling one's market share is through competitive advantage. In the wine industry, product differentiation and maintaining low costs lead to this advantage. In the long run, there is no question that there is a large amount of land, capital, and human capital in the United States that is well suited to the production of both high-quality, high-priced wine in some places (such as the coastal districts of central and northern California) and lower-priced, everyday wine in other places (such as the Central Valley of California). The industry is well positioned to compete in the long-term, both in the domestic market and in a growing export market.

TRACKING KERN'S ECONOMY

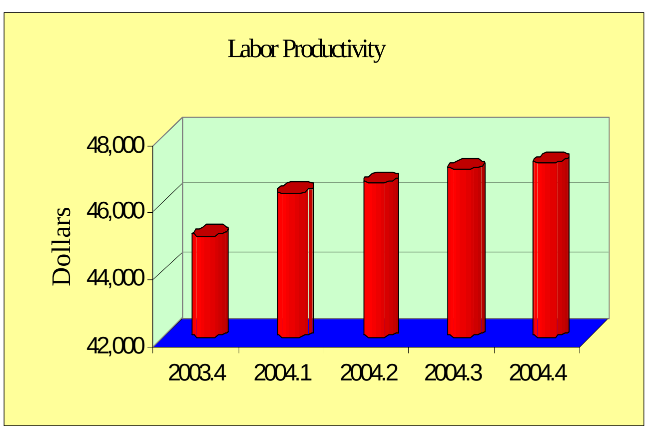
ABBAS P. GRAMMY
PROFESSOR OF ECONOMICS, CSUB

Economy

Personal Income - Kern County's personal income (in constant 1996 dollars) increased from $14.22 billion in the third quarter to $14.31 billion in the fourth quarter. The county's economy expanded $90 million or at an annual rate of 2.4 percent. Over the last four quarters, Kern's economy has created $350 million of income.

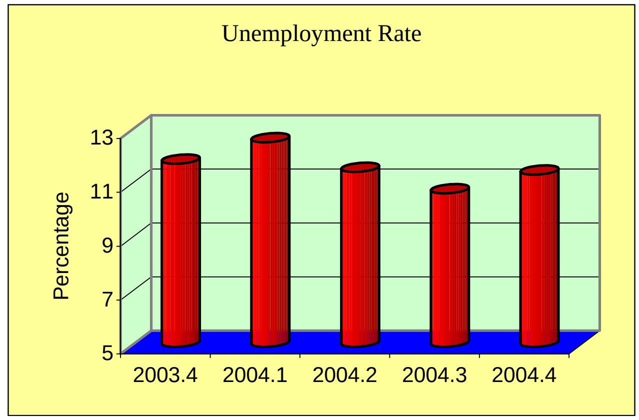


Productivity - Labor productivity is measured as Personal Income divided by Labor Force. In constant dollars, labor productivity inclined $200 from $47,000 in the third quarter to $47,200 in the fourth quarter. This increase translated into an annual productivity growth rate of 1.7 percent. Compared with four quarters ago, labor productivity in Kern County has increased $2,185.

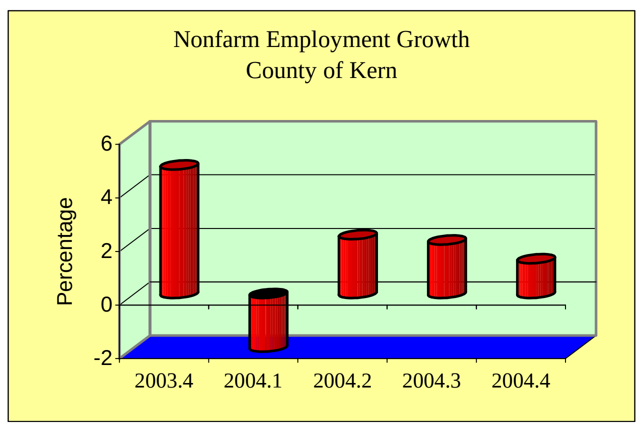


Labor Market

Unemployment Rate - A large decline in farm employment offset a moderate gain in nonfarm employment, resulting in a higher rate of unemployment. When adjusted for seasonality, the rate of unemployment in Kern County climbed 0.7 percent from 10.7 percent to 11.4 percent. In spite of this rise, the county's unemployment rate was 0.4 percent higher than that of four quarters ago. Kern's unemployment rate was 5.6 percent higher than the state average and 6 percent greater than the national average.



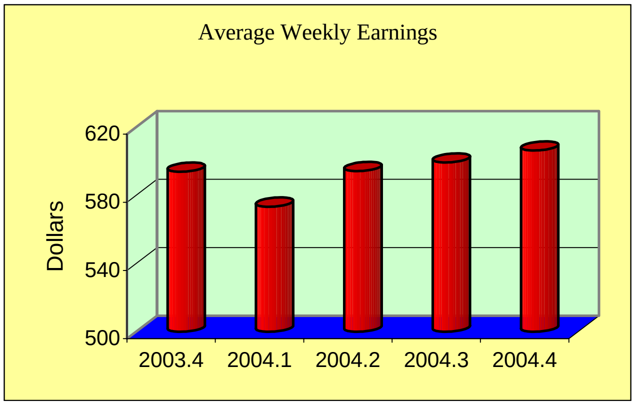
Employment Growth – Nonfarm employment grew at a slower rate than the previous quarter. When adjusted for seasonality, nonfarm employment increased at an annual rate of 1.3 percent. Among the nonfarm industries, retail trade, professional and business services, and local public education added jobs. However, construction, manufacturing, and leisure and hospitality reduced employment.



Wages – Weekly wages paid to local manufacturing workers inclined $7.01 from $599.30 in the third quarter to $606.31 in the fourth quarter. This wage increase was attributed to both the rise in the hours of work and average hourly earnings. Compared with four quarters ago, local manufacturing workers earned $12.41 more per week.

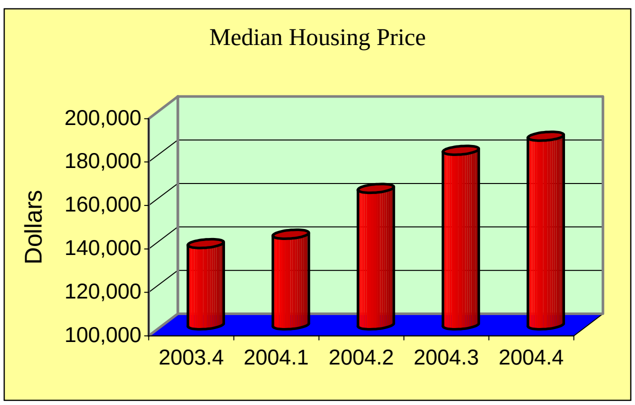
(Continued on page 12)

Tracking *(Continued from page 11)*



Housing Market

Housing Prices - The median sales price of all homes (i. e., new and existing condominiums and single-family detached homes in current dollars) soared $6,470 or 3.5 percent from $180,330 in the third quarter to $186,800 in the fourth quarter. Since the fourth quarter of last year, the county's median price has appreciated $49,380 or 36 percent.

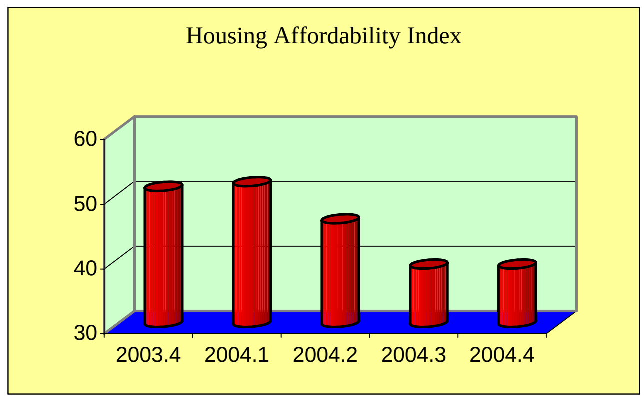


In the fourth quarter of 2004, housing prices appreciated in all of the major cities of Kern County. In dollar value, housing prices appreciated more than the county average in Bakersfield, California City, Delano, Ridgecrest, Rosamond, Taft, and Tehachapi. Percentage wise, housing prices appreciated the most in Taft, Delano, and Rosamond.

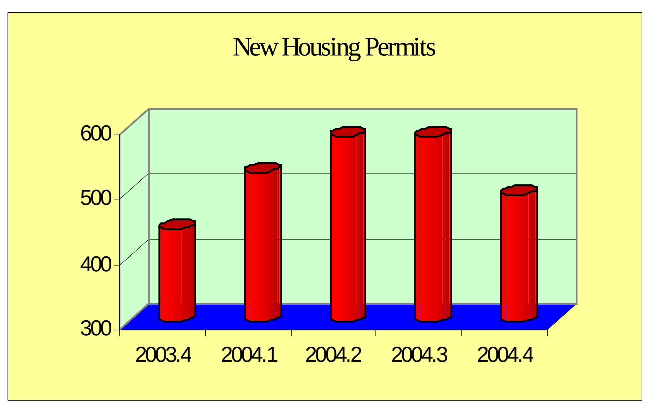
Housing Affordability - The index of housing affordability remained unchanged at 39 percent in the fourth quarter. Over the past four quarters, the county's index has fallen 12 percentage points. The current index value indicates that a family earning the median household income has 39 percent of the income necessary to qualify for a conventional loan covering 80 percent of a median-priced existing single-family home.

Area	Fourth Quarter ($)	Third Quarter ($)	Quarterly Change ($)	Quarterly Change (%)
Kern County	186,800	180,300	6,500	3.5
Bakersfield	200,200	193,200	7,000	3.5
California City	137,400	129,500	7,900	5.7
Delano	127,300	115,500	11,800	9.3
Ridgecrest	130,300	123,300	7,000	5.4
Rosamond	218,300	200,900	17,400	8.0
Taft	90,800	80,700	10,100	11.1
Tehachapi	222,500	214,400	8,100	3.6
Wasco	117,500	114,500	3,000	2.6

Source: California Association of Realtors



Building Permits – The construction and real estate boom continued in the county as the monthly number of new building permits for single-family homes remained at a high level of 496 in the fourth quarter. However, the number of building permits fell 89 units from the previous quarter. Relative to the fourth quarter of the previous year, 54 more building permits were issued.

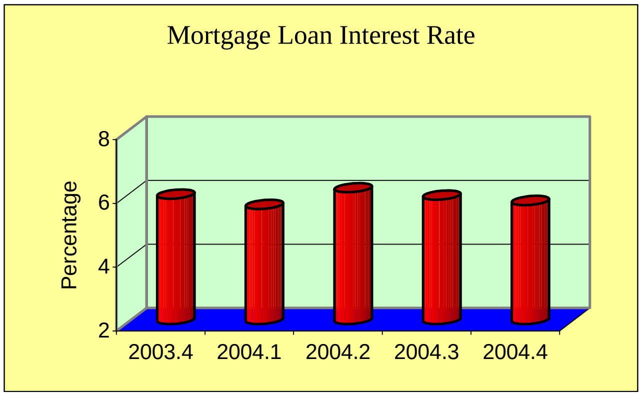


Interest Rate - The interest rate of thirty-year conventional mortgage loans dropped from 5.90 percent in the third quarter to 5.73 percent in the fourth quarter. Rela-

(Continued on page 13)

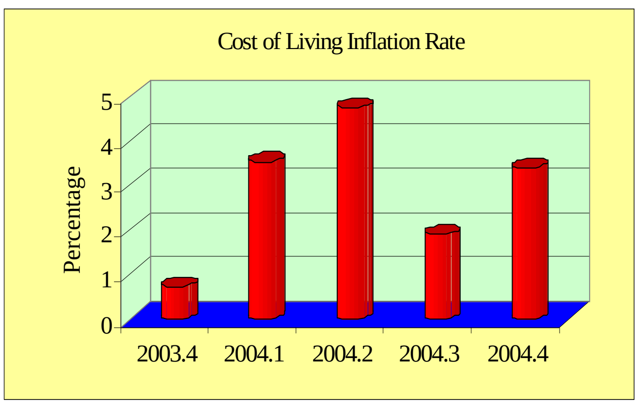
***Tracking** (Continued from page 12)*

tive to the fourth quarter of last year, the mortgage loan interest rate has fallen 0.20 percent.



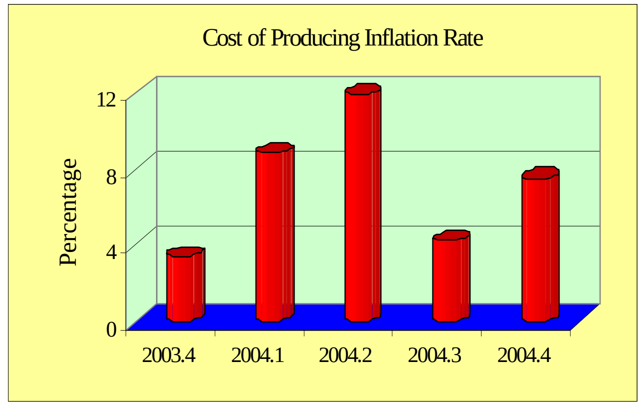
Commodity Prices

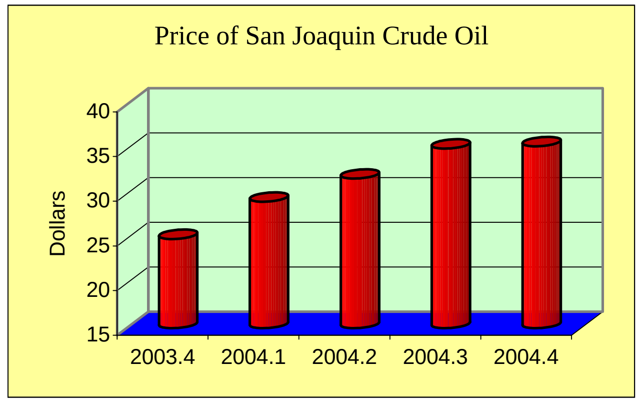
Cost of Living - The Consumer Price Index for all urban areas (1982-84 =100) rose from 189.5 in the third quarter to 191.1 in the fourth quarter. The annual cost of living inflation accelerated from 1.9 percent in the third quarter to 3.4 percent in the fourth quarter. Relative to the fourth quarter of the previous year, the cost of living inflation climbed 2.7 percent.



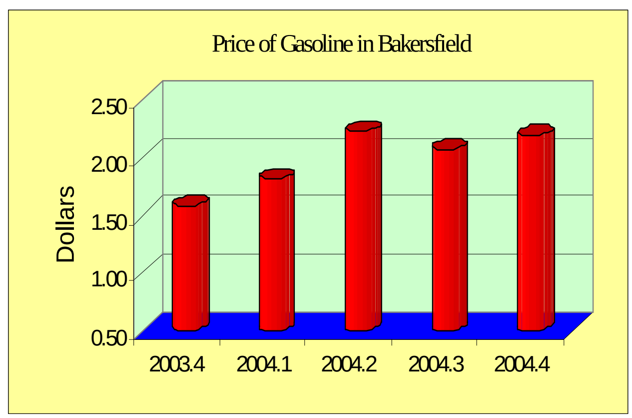
Cost of Producing - The Producer Price Index for all commodities (1996 =100) jumped from 147.7 in the third quarter to 150.4 in the fourth quarter. The annual cost of producing inflation rate accelerated from 4.2 percent in the third quarter to 7.5 percent in the fourth quarter. Relative to the fourth quarter of the previous year, the cost of producing inflation climbed 4.1 percent.

Price of Oil - The average price of San Joaquin Valley heavy crude climbed 26 cents per barrel from $35.09 in the third quarter to $35.35 in the fourth quarter. Compared with four quarters ago, the average price of crude oil ascended $10.37 per barrel.





Price of Gasoline - In the Bakersfield metropolitan area, the average retail price of regular gasoline per gallon inclined 12 cents from $2.07 in the third quarter to $2.19 in the fourth quarter. Compared with four quarters ago, the price of gasoline was 61 cents higher.



Farm Prices - The national Index of Prices Received by Farmers for all farm products (1990-92 = 100) plunged 6 points from 120 in the third quarter to 113 in the fourth quarter. The Index was one point lower relative to the fourth quarter of last year.

In the meantime, the national Index of Prices Paid by Farmers for commodities, services, interest, taxes, wages, and rents remained unchanged at 134. Relative to the fourth quarter of last quarter, this Index has gained 4 points.

(Continued on page 16)

Tomatoes on Steroids Creating New Jobs

The Kern Economic Development Corporation's (Kern EDC) *Tomatoes on Steroids* project is an innovative, economic gardening strategy aimed at growing small companies in Kern County. It targets small and medium-sized companies with 50 or fewer employees located in small communities with high unemployment. The program is funded through an $80,000 grant from the U.S. Department of Agriculture Rural Development Office.

Kern EDC has selected nine small businesses to participate in the project. Companies were selected among 22 total applicants based on how well they met a stringent set of criteria which included (1) the benefits they provide to their respective communities that go beyond the jobs they create; (2) whether they have the potential to add jobs that pay more than the minimum wage plus benefits; (3) demonstrated creativity and business ingenuity; (4) willingness to participate in the process; (5) offer products and jobs that are sustainable; and (6) apply unique or advanced technology.

The following companies participating in this yearlong program have plans to add 58 new jobs:

The Apple Shed, Inc., Tehachapi – Restaurant with catering and gift shop. The project plans to add 5 new jobs by improving its e-commerce sales, offering pre-packed frozen food dinners; and to expanding its dining room and kitchen.

Advanced Micro Research, Inc., Delano - Plan to offer two computer training programs for students and adults. Classes will be offered at Delano High School and the North Kern Vocational Training Center. Expansion will include public and private sector small businesses and will add 5 paid positions.

Bennett Optical Research, Inc., Ridgecrest - Expand facilities for production of lightweight active and adaptive mirrors. Continue to bid on NASA and Department of Defense contracts and researching potential market for lightweight mirrors for astronomy field. The company expects to create 5 new positions.

Carney's Business Technology Center, Bakersfield - Expand new service to small businesses with network Management Services by hiring 4 account executives and account specialists.

Central California Power, located in the unincorporated area of the county - Increase number of California dealers selling Daewoo engines and offer complete anaerobic digester system to the dairy industry. This project plans to add 10 new jobs.

Oasis Air Conditioning, Bakersfield - Expand residential construction and service departments and add computerized duct design and duct sealing services. Assist with needs for building expansion and staff training programs. Five new paid positions will be added to the company's workforce.

Terrio Therapy-Fitness, Inc., Bakersfield - Expand physical therapy services to Delano, Taft, Tehachapi, and other areas of Kern County. Need to hire 15 physical therapists, aids, and receptionists.

Tomato Man, Ridgecrest – Expand greenhouses by approximately 16,000 square feet and will seek real estate loans. Expansion will allow more efficient production and cost containment and will require 3 new employers.

XCOR Aerospace, Inc., Mojave - Need technical grant writers for NASA and Department of Defense contracts. Seeking investors for capital design and construct rocket vehicle. The company plans to hire 6 new staff members.

The assistance that Kern EDC provides for these companies will include arranging and attending meetings with the clients, attending meetings on their behalf, and tapping into expertise of the Kern EDC team, investors and board members. As part of this strategy, the companies will participate in an intensive economic development effort and get individualized business consulting that will help them identify opportunities and link them to business resources that will ultimately lead to job growth in Kern County.

For more information on the *Tomatoes on Steroids* project, call (661)862-5150 or visit the Kern EDC website at www.kedc.com.

BUSINESS EDUCATION:

A New Year: Two HR Resolutions

Michael Bedell
Assciate Professor of Management/M.B.A
Program Director, CSUB

The New Year is viewed as a time of renewal among most people and organizations. So what should your New Years Resolution be from an HR standpoint? Two ideas come to mind. The first of these – regulatory data – probably creates the need that we make the following resolution: "I promise to collect my HR regulatory data throughout the year and not wait until the last minute." The second set of HR data that we need to think about collecting and examining this year are HR metrics. HR metrics helps us to determine: (a) cost of our HR processes; (b) effectiveness of our HR processes; (c) improvement of HR processes. The second resolution should be: "I promise to collect some data about my HR processes to find out what they cost."

Some regulatory data, such as the Equal Employment Opportunity survey (EEO-1) is due on September 30. Remember if you have 15 or more employees are covered by the federal Civil Rights Act and the Americans with Disabilities Act. Twenty or more employees means that the Age Discrimination in Employment Act pertains to your organization. Finally, most organizations with ONE or more employees are covered by the Equal Pay act. Check with a labor attorney or www.dol.gov for more specific information.

Safety training and accident data also need to be tracked throughout the year for most employers with 10 or more employees. OSHA requires three forms be maintained year round (OSHA 300 Log of Work-Related Injuries and Illnesses, the annual OSHA 300A Summary of Work-Related Injuries and Illnesses, and the OSHA 301 Injury and Illness Incident Report). Check with your labor attorney to be certain as there are many exemptions and quirks to this legislation.
HR metrics sound like they are complex, they really are not. Most metrics consist of a series of simple measurements to assess the time each HR process requires and which is then multiplied by the hourly labor base rate. There is not a "right" way to measure instead the process should be examined to determine the best place in the process to measure. Once the data is collected it should be examined for decision making and improvement opportunities.

The recruiting component will be used to illustrate an HR metric. Most organizations prefer to have a full employee complement and few or no open positions. Open positions mean that work is not being completed or the existing employees are doing extra work – with or without overtime – both have a long-term cost. Some recruiting metrics we might examine:

- time factors – time to interview; time to offer; time to fill a position
- labor cost per hire – (time to hire) * (hourly rate for those involved in hiring)

The time factors can be easily adapted to show costs. We might find that we are able to interview many candidates but unable to hire. More importantly, we develop a realistic picture of the cost of recruiting (which can be compared to the cost of a small pay raise that might keep an employee from turning over). One word of warning: It is simple to use one or two HR metrics, however, the real power is found when the metrics interact in the same way as the various HR processes. Measurement in one area may not provide the entire picture.

ECONOMIC EDUCATION:

THE ECONOMIC ROLE OF SMALL BUSINESS

Small businesses are companies that are independently owned and operated. They are not dominant in their field of business. Small businesses are major providers of jobs and products, accounting for 98 percent of all companies and 40 percent of the nation's Gross Domestic Product.

Small businesses play four major roles in the economy:

Creating Jobs – Virtually all the new jobs created in the United States economy over the past decade were in businesses with fewer than 100 employees. Interestingly, companies with fewer than 20 employees were responsible for nearly two-thirds of these new jobs. However, jobs created by small businesses differ from those added by large companies in several key aspects. Small businesses generally pay less both in terms of wages and benefits. They hire many workers on a temporary or part-time basis. On average, workers employed by small businesses are either younger or older than those hired by big businesses, and have fewer years of formal education and work experience.

Producing New Products – Small businesses foster product innovation. A recent study of innovation in 121 industries found that small firms and individual inventors produced 40 percent of all new products. This is a remarkable contribution since small businesses account for only 5 percent of the nation's research and development funds. Many small business inventions such as the helicopter and stainless steel have turned into big business ventures.

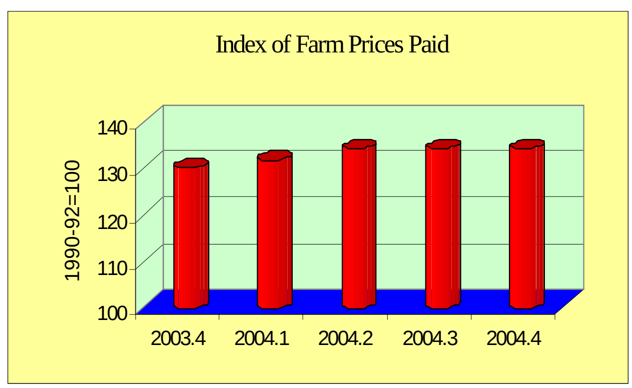
Serving Large Corporations – Small businesses assist the operation of large corporations. They act as distributors of products, suppliers of materials, and contractors of services. In fact, some of the industry leaders outsource many of their products to smaller companies. For example, Liz Claiborne, a leading firm in the fashion industry, has no factories of its own. All of its garments are made on contract by outside suppliers.

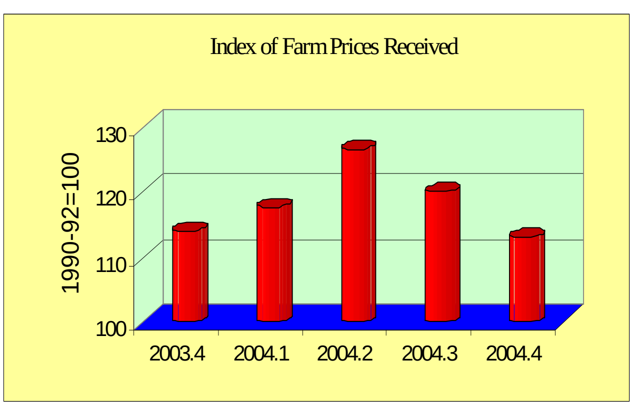
Providing Specialized Products – Many small businesses specialize in production of goods and services that meet consumers' special needs. Unlike large companies that specialize in mass production, small businesses supply the kinds of products that are custom-made for a smaller cliental. Many successful small businesses find a "niche" in providing goods and services that satisfy special needs and wants.

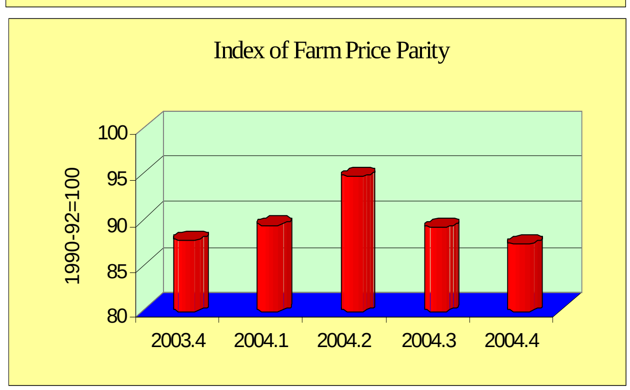
Summary: Abbas Grammy. Source: D. Rachman, M. Mescon, C. Bovee, and J. Thill, *Business Today*, New York: McGraw-Hill, 1990.

Tracking *(Continued from page 13)*

Here, we measure the Index of Price Parity as the ratio of the Index of Prices Received to the Index of Prices Paid. In the fourth quarter of 2004, the Index of Price Parity fell 2 points from 89 to 87. This disparity points out the growing imbalance between prices farmers pay for their inputs and prices farmers receive for their outputs.







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