ECONOMIC FORECAST | EMERGING TRENDS IN SACRAMENTO'S ECONOMY

UPDATE

MID-YEAR 2019

sacramento BUSINESS REVIEW

Volume 11 Issue 2 » sacbusinessreview.com

The economic boom continues, but a slowdown looms.

Labor Market & Regional Economy
SBR/SAFE Credit Union Consumer Sentiment Survey
Small Business
Real Estate
Capital Markets & Banking Forecast
Human Capital Trends

MID-YEAR 2019

sacramento BUSINESS REVIEW

MISSION

To educate consumers on the economic and financial health of the Sacramento region.

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CONTACT

Sanjay Varshney, PhD, CFA, Chief Economist,
Sacramento Business Review
(916) 799-6527
Sanjay@sacbusinessreview.com

EDITORS
Jason Bell, CFA
Sanjay Varshney, PhD, CFA

GRAPHIC DESIGN
Carrie Dennis Design

PHOTOGRAPHY
Tim Kesselring Photography
iStockphoto

PROOFREADING
Suzanne Stone Freelance Services

PARTNERS
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MESSAGE FROM THE CHIEF ECONOMIST

Dear Friends,

I am pleased to share the 22nd edition of the *Sacramento Business Review* – the most comprehensive, precise, and intellectually sophisticated analysis of the regional economy. For over 11 years, our team has provided thoughtful predictions that have accurately forecasted the economic and business climate. With 17 of Sacramento's very best financial analysts and researchers combining their skills and talent, the *Sacramento Business Review* is the most credible source of independent thinking, insights, and research on our economy in the region.

Recovering from the worst December on record since 1931, the U.S. stock market bounced back in 2019 to produce the best first half in two decades and the best June in over 50 years. Corporate earnings came in better than expected in the first two quarters, and the U.S. economy grew at a faster pace than anticipated — looking a lot stronger than the rest of the developed world. However, a synchronized global slowdown, a downshift in the second-largest economy of the world (China), an escalating trade conflict between the U.S. and China, an inverted yield curve, and BREXIT continue to pose headwinds. While we can clearly celebrate not having to deal with a recession in 2019, concerns remain about 2020. Recently the Federal Reserve ended a 9 time rate increase cycle to reverse it through the first 25 basis point rate cut in 11 years. Over one third of global bonds outstanding in the world are yielding negative interest rates. Central banking rates in many countries are also negative — in other words investors are paying banks to keep their money safe in deposits! And don't forget — 2020 is an election year.

At present, we do not expect a national or global recession in 2019 or even in 2020. However, we remain increasingly cautious on the local Sacramento economy, which has a history of entering recession before a national recession begins. The greater Sacramento region's job growth has slowed, with declines in both consumer and business confidence. While the commercial real estate market remains active, the housing market is exhibiting weakness in spite of low mortgage rates. The yield curve between the 10 year Treasury and 30 day T-Bill has inverted — an early indicator of recessionary pressures to come. Sacramento appears to be experiencing a decline in labor force, and mismatch and disconnect between university graduates' aspirations and what the market really needs. While economic conditions in our region remain largely unchanged from January, I want to remind readers that the region desperately needs to do something about developing or attracting higher paid jobs and diversifying the job mix to prepare ourselves for the next recession.

Our upcoming 12th anniversary milestone demonstrates the success and commitment of our analysts, who do this work entirely as a public service to the region. We plan to continue doing this as long as our team continues to enjoy producing the forecast.

I invite your feedback. Please do not hesitate to let me know how we may improve future issues or if you wish to be a supporting partner. To download your free copy, please visit **sacbusinessreview.com**.

Warm regards,

Sanjay Varshney

Sanjay Varshney, PhD, CFA
Chief Economist, *Sacramento Business Review*
(916) 799-6527 | Sanjay@sacbusinessreview.com | sacbusinessreview.com

FEATURES

ABOUT THE AUTHORS

Chase Armer, CFA

Chase Armer is a co-owner of Planned Solutions, Inc., a Sacramento-based financial planning and investment advisory firm, where he is a financial planner and a member of the Planned Solutions Investment Management Committee. Chase holds several professional designations, including Certified Financial Planner Practitioner, Chartered Financial Analyst, and Enrolled Agent. Chase has a degree in economics from California State University, Sacramento, a master's in taxation from William Howard Taft University, a certificate in personal financial planning from UC Davis Extension, and a doctorate in business administration from William Howard Taft University. He is a past president of the Financial Planning Association of Northern California.

Will Austin

Will Austin is a Senior Analyst at Cushman & Wakefield, where he assists in the disposition, acquisition, and leasing of office, industrial, and retail commercial real estate throughout Northern California and Northern Nevada. He holds bachelor's and master's degrees in sociology from Trinity College and California State University, Fullerton, respectively and an MBA from UC Davis.

Seung Bach, PhD

Seung Bach is Professor of Entrepreneurship and Strategic Management in the College of Business Administration and the faculty director of the Center for Entrepreneurship at California State University, Sacramento. He earned his PhD in business administration at the University of Tennessee, Knoxville, and his MBA at the George Washington University, Washington, D.C. His expertise is in the areas of new venture creation, small business management, entrepreneurial transitions, innovation and corporate entrepreneurship, and global management and strategy.

Jessica Bagger, PhD

Jessica Bagger is a Management Professor at California State University, Sacramento, and Associated Faculty at the University of Gothenburg in Sweden. She received her PhD in management at the University of Arizona. Dr. Bagger's scientific research relates to factors impacting employee well-being and performance, including HR systems, leadership, and organizational culture.

Jason Bell, CFA

Jason Bell is Chief Investment Officer and a Partner at Capital Planning Advisors, LLC, where he is responsible for directing the investment policy of the firm and managing the investment and research team. He earned his bachelor of science degree in business administration from the University of the Pacific and holds a master of business administration degree from the University of California, Davis, where he was inducted to the Beta Gamma Sigma academic honor society. He is a Past President of CFA Society Sacramento and previously spent four years as an advisor to the Board of Governors of CFA Institute.

Jesse Catlin, PhD

Jesse Catlin is a Professor of Marketing at California State University, Sacramento. He holds a PhD in management with an emphasis in marketing from the University of California, Irvine, and holds master's and bachelor's degrees in economics from California State University, Sacramento. His research interests include consumer behavior and decision-making. Prior to his academic career, he worked as a consultant on projects related to market research and economic development.

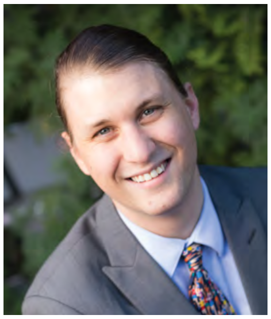
Matt Cologna

Matt Cologna graduated with a degree in business from California State University, Sacramento, and has been active in commercial real estate for the past 21 years in Sacramento. His experience includes owner/user and investment sales, logistics, landlord and tenant representation, land assemblage, build to suits, and developer relations. He has represented clients on a local, regional, and national basis. He is involved with the Cushman & Wakefield Global Supply Chain Solutions Group, offering additional insight into current and future needs of occupiers in the market. Matt has completed over 17 million square feet of deals with a value exceeding $620 million.

John E. Frisch

John Frisch has been active in commercial real estate brokerage for 37 years in the Sacramento region. During his career, he has been involved in over 1,000 lease, sale, and build-to-suit transactions totaling over 10 million square feet. John also is an active volunteer with several non-profit organizations in the region, including the Salvation Army, the Los Rios Community College Foundation, the Sacramento Metro Chamber of Commerce and the Rotary Club of Sacramento.

ABOUT THE AUTHORS



Nick Hladek

Nick Hladek works as a Quantitative Modeler at Golden 1 Credit Union, where he assists in the development and implementation of quantitative models. Prior to his time at Golden 1 Credit Union, Nick worked as a Senior Research Analyst at the Greater Sacramento Economic Council. He holds both a bachelor's degree and master's degree in economics from California State University, Sacramento.

Hao Lin, PhD, CFA

Hao Lin is a Professor of Finance in the College of Business Administration at California State University, Sacramento. He has a PhD in finance and MS in financial mathematics, both from the University of Warwick in England. His expertise is in the areas of financial markets and market microstructure. Dr. Lin holds the Chartered Financial Analyst designation.

Lan Liu, PhD, CFA

Lan Liu is a Professor of Finance in the College of Business Administration at California State University, Sacramento. She received both her PhD in finance and MSc in economics and finance from the University of Warwick in England. Her research focuses on portfolio risk management, forecasting, and performance measurement. Dr. Liu holds the Chartered Financial Analyst designation and serves on the Board of Directors of the CFA Society Sacramento.

Elizabeth Lyon, JD, LLM

Elizabeth Lyon is an Assistant Professor of Accountancy at California State University, Sacramento. She holds a JD from the University of California, Hastings College of the Law, an LLM from the University of San Francisco, and an undergraduate degree from the University of California, Davis. Her research interests include issues related to income tax, employment tax, and consumer perceptions of taxation. Prior to joining Sacramento State, she was General Counsel for a global consumer technology corporation.

Joe Niehaus, CFA

Joe Niehaus is the Treasurer for SAFE Credit Union, where he is responsible for managing interest rate and liquidity risks as well as developing and maintaining pricing methodologies across all product lines. Joe has worked as a bank examiner for both the public and private sectors and served five years as an Electronic Intelligence Analyst with the U.S. Navy. Joe earned an MBA from the University of Nebraska, Lincoln, and a BS in business administration from California State University, Sacramento. He holds the Chartered Financial Analyst designation and is President of the CFA Society Sacramento.

Yang Sun, PhD

Yang Sun is Professor of Supply Chain Management and Director of the Master's of Business Administration for Executives program in the College of Business Administration at California State University, Sacramento. In addition to his PhD in industrial engineering from Arizona State University, he has a Six Sigma Black Belt. He also received an engineering degree from Tsinghua University in Beijing, China. Dr. Sun has research and teaching interests in the areas of global supply chain management, operations strategy, Lean and Six Sigma, managerial economics, operations research, and data analytics, and is a recipient of the university's Outstanding Scholarly and Creative Activities Award as well as Outstanding Teaching Award.

Sanjay Varshney, PhD, CFA

Sanjay Varshney is Professor of Finance at California State University, Sacramento, and Senior Vice President/Investment Strategy Specialist for California and Nevada at Wells Fargo Private Bank – Wealth Management Group. He served as the Vice President for Economic and Regional Partnerships and Dean of the College of Business Administration at California State University, Sacramento, for 10 years. He earned an undergraduate degree in accounting and financial management from Bombay University, a master's degree in economics from the University of Cincinnati, and a PhD in finance from Louisiana State University. He also holds the Chartered Financial Analyst designation. Dr. Varshney serves as the Chief Economist for the *Sacramento Business Review*.

Andrés R. Villegas, CFA

Andrés Villegas is Vice President and Investment Strategist for Wells Fargo Private Bank, where he works as a client advisor to develop and execute investment plans. He holds the Chartered Financial Analyst designation and was previously invited by The University of Chicago to attend the Chicago Booth's Business Scholars Program. He holds a bachelor's degree in finance from The University of Texas at Austin.

ABOUT THE AUTHORS

Anna V. Vygodina, PhD

Anna Vygodina is a Professor of Finance in the College of Business Administration at California State University, Sacramento. She holds a PhD in finance from the University of Nebraska, Lincoln, and an MBA with economics minor from the University of Nebraska, Omaha. Dr. Vygodina's research interests are in exchange rates, speculative tensions, and heterogeneous expectations in the capital markets.

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SPECIAL THANKS

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Jeff Bingel
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Sacramento State, College of Business Administration, Office of the Dean Staff

CFA Society Sacramento

KEY POINTS

LABOR MARKETS & REGIONAL ECONOMY

- The Sacramento region recently experienced a decrease of the civilian labor force
- The pace of job growth in recent months has been at its lowest since the last recession
- The region had unequal job growth across different industry sectors, with construction and manufacturing leading the growth recently

SBR/SAFE CREDIT UNION CONSUMER SENTIMENT SURVEY

- Overall, consumer sentiment remains positive and is roughly flat since our January 2019 report at both the regional and national levels.
- Though positive in absolute terms, perceptions of current economic conditions have fallen at the regional level and even more so at the national level.
- Compared to national data, regional consumer sentiment remains less optimistic overall and less positive about current economic conditions.
- Consumer expectations for future economic conditions are up slightly at both the regional and national level.

SMALL BUSINESS ECONOMY

- Total SBA lending decreased, driven by a meaningful drop in Placer and Yolo Counties. A Sacramento County slowdown overshadowed El Dorado's impressive growth.
- SBCI respondents feel more optimistic on all areas, except credit, which remained largely unchanged.
- Business listing activity, which is measured by volume of listings and closed sales, increased from our previous reading, though sales were still largely focused on smaller deals.

REAL ESTATE

- **Office market:** Strong start to 2019 lack of supply is pushing lease rates and property values up.
- **Industrial Market:** Strong lease rate growth was driven by low vacancy and new investors entering the market. New product is coming online, but focuses on large users leaving smaller firms for few options.
- **Retail:** Retail fundamentals continue to be driven by construction, and class A centers are seeing substantial demand due to strong demographics. Tenants continue to look to add experiential elements, resulting in food halls, virtual reality arcades, and the like.
- **Single Family:** Property values are growing, but the pace continues to slow, up 2.8% year-over-year compared to 5.3% growth last year.

CAPITAL MARKETS & BANKING FORECAST

- Fed policy has done an about face from where we thought it would be at the beginning of the year. We initially projected two rate hikes for 2019, and now we are expecting that two rate cuts, with one already occurring in July, may be in store before the end of the year.
- We still think low to mid-single digit returns make sense for equity markets, but that means the market has more to give up before year-end. Volatility observed at the end of July and into August may have already put us on the path to the returns we projected back in January.
- The yield curve was inverted between the 3-month and 10-year for much of the first half of 2019, and the inversion continues to be a factor as of the start of Q3. If history does repeat itself, a recessionary environment may not be too far off.
- Our proprietary SBR Financial Conditions Index shows that the regional economy continues to expand.

HUMAN CAPITAL TRENDS

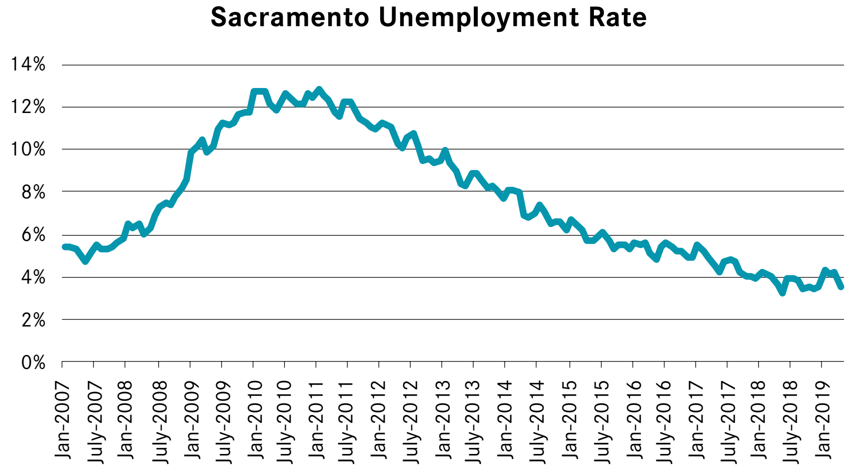
- Increased resignations are reported, accompanied by moderate recruiting efforts, suggesting a possible shrinkage of the local workforce.
- Training and development budgets are increasing, as organizations are conceivably trying to address existing skills gap.
- Overall compensation (salaries/wages and optional benefits/perks) is seeing an uptick in the latter part of 2019.
- Early 2019 reported preparing for Artificial Intelligence as a priority, with the focus shifting from preparation to implementation and training for AI.
- The top two factors expected to exert the most influence on the overall organization are staying consistent – there is an enduring skills gap and talent shortage.

Labor Markets
& Regional Economy

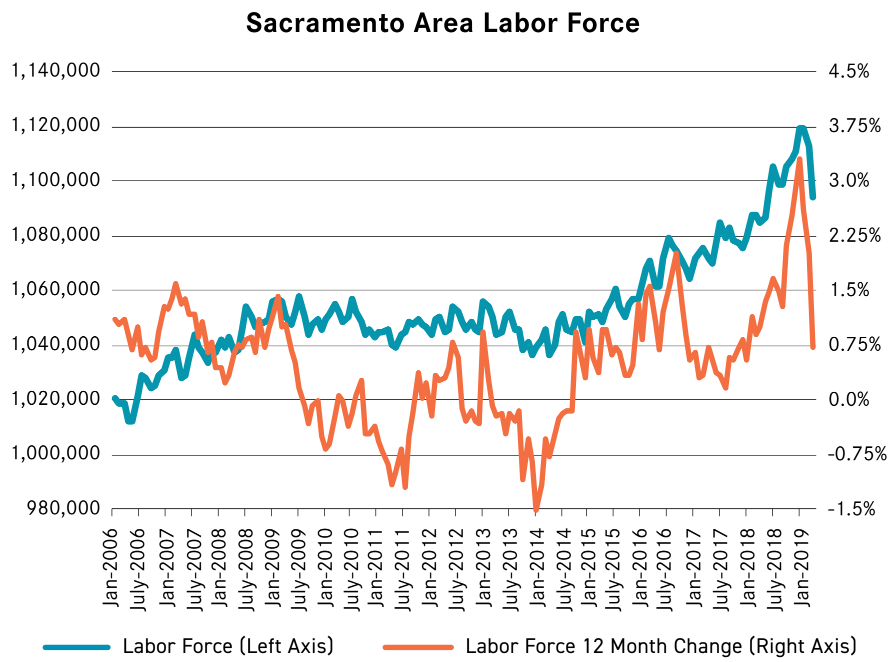
MIXED RESULTS AND UNEVEN GROWTH

While the national unemployment rate was hitting multi-decade lows, the unemployment rate in the Sacramento Region increased slightly in 1Q19. In fact, the unemployment rate increased nearly one percent since our January report and was 0.30% higher than the level of the previous year. However, in 1Q19, the region experienced a significant loss of civilian labor force of about 25,000 people, i.e., about 2.3% of the regional population moved out of the area. It is likely that they moved out of the State, as California experienced the same decline in its labor force. Meanwhile, the Sacramento region lost about 17,500 jobs in 1Q19, or 1.6% of its total employment. As the decrease in the labor market was greater than the loss of jobs, the unemployment rate decreased back down to 3.5% in 2Q19.

The recent influx of people entering the labor force was offset by the people leaving; therefore, the year-over-year labor force growth is less than 1%. On the bright side, employment growth remains positive and the region's total nonfarm jobs have increased 1.35% year-over-year. However, the pace of job growth in the region in recent months has been at its lowest level since the last recession.



Source: Economagic.com



Source: Economagic.com

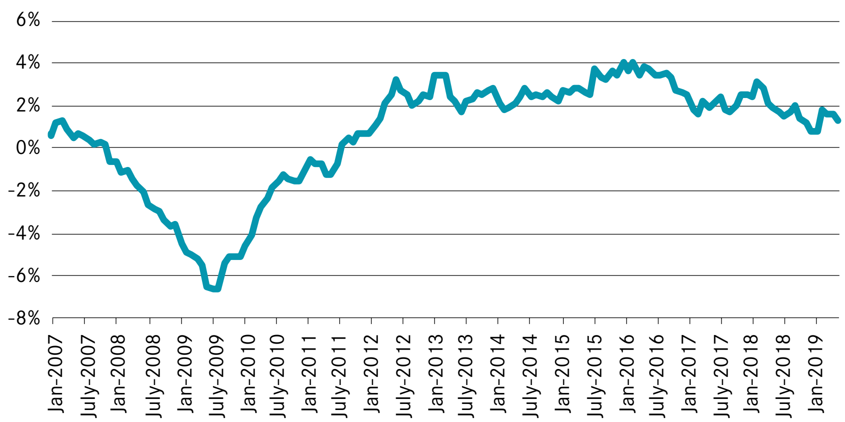
Health care and Leisure & Hospitality sectors REPORTED STRONG EMPLOYMENT GROWTH

We believe the fast growing years are behind us and economic growth in the region will be slower in the next 12 months.

Not all sectors of the job market are contributing equally to the increase in employment growth. Construction and manufacturing jobs are coming back to the region. The health care and leisure & hospitality sectors, which represent two of the region's largest employment sectors behind government, also reported strong employment growth. Meanwhile, government jobs, which represent one out of every four jobs in the Sacramento Region, increased just 0.2% year-over-year.

Overall, the economic expansion continues. However, we are beginning to see higher volatility in employment data and need to be aware of a number of short-term and long-term economic risks, e.g., the Fed being accommodative for shorter term, increasing debt and deficit, overvalued equities, election year hesitation, geopolitical issues and trade wars, and a global slowdown with an aging demography. We believe the fast growing years are behind us and economic growth in the region will be slower in the next 12 months.

Sacramento Employment Growth Rate



Source: Economagic.com

Sector	Year-over-year Growth
Construction	+5.4%
Manufacturing	+5.3%
Health Care	+5.1%
Leisure & Hospitality	+5.0%
Trade, Transportation, & Utilities (including retail)	+2.5%
Education	+2.3%
Finance Activities	+1.3%
Professional & Business Services	+0.4%
Government	+0.2%

Source: California EDD

Consumer Sentiment *Survey*

For the mid-year update, the Sacramento Business Review (SBR), in partnership with SAFE Credit Union, conducted another round of our regional consumer sentiment survey. The survey included measures of personal and regional economic conditions along with purchasing and credit utilization.

Regional vs. National Sentiment

The SBR team once again compared regional sentiment with national sentiment measures with the results shown in Table 1. To measure sentiment, we utilized questions from the University of Michigan Consumer Sentiment© survey that were adapted to specifically address the Sacramento region. Per methods used by the University of Michigan survey, we calculated the following three indices for the region and compared them to the national data.

(1) **Index of Consumer Sentiment:** An overall measure of how consumers assess their own personal economic prospects and broader regional or national economic conditions.

(2) **Index of Current Economic Conditions:** A measure of how consumers assess their own personal economic prospects compared to a year ago, along with perceptions about the current market for making major household purchases.

(3) **Index of Consumer Expectations:** A measure of what consumers expect to happen in the future for their own finances and the regional or national economy.

Consumer sentiment at the regional level was the same or higher in two of the three categories since our January 2019 report. Nationally, consumer sentiment was the same or lower in two of the three categories over the same period. The biggest drop off both regionally and nationally was for consumer perceptions of current economic conditions. However, we see optimism for the future as both regional and national data showed increases in the index capturing consumer expectations for future economic conditions. (See Table 1.)

Table 1
Regional vs. National

	Regional Index Score		National Index Score	
	Mid Year Update	Change Since January 2019	Mid Year Update	Change Since January 2019
Index of Consumer Sentiment	90.8	**+0.1**	98.2	**-0.1**
Index of Current Economic Conditions	95.7	**-1.6**	111.9	**-4.2**
Index of Consumer Expectations	87.7	**+1.2**	89.3	**+2.3**

Notes: National data obtained from the University of Michigan Consumer Sentiment Survey June 2019 Data, available at: https://data.sca.isr.umich.edu/. Indices calculated using the methods specified at: https://data.sca.isr.umich.edu/fetchdoc.php?docid=24770.

INDEX OF CONSUMER EXPECTATIONS in the region and nationally HAVE INCREASED

CONSUMER SENTIMENT

Purchasing and Credit

We again asked regional respondents about the types of credit they currently hold and their plans to acquire credit over the next year. The patterns of credit usage and plans for acquisition are generally consistent with those in our last report. (See Figure 1.)

Summary

While consumer sentiment remains positive in absolute terms, local consumer sentiment continues to lag behind national levels and we have seen some tapering. While the data suggest dips in perceptions of current economic conditions regionally and nationally, consumers also seem to have increasing optimism about future economic conditions. Going forward to our next release, it will be important to keep an eye on how consumers are impacted by issues such as interest rates and changes in trade policy (e.g., tariffs).

Figure 1
Types of Credit Held

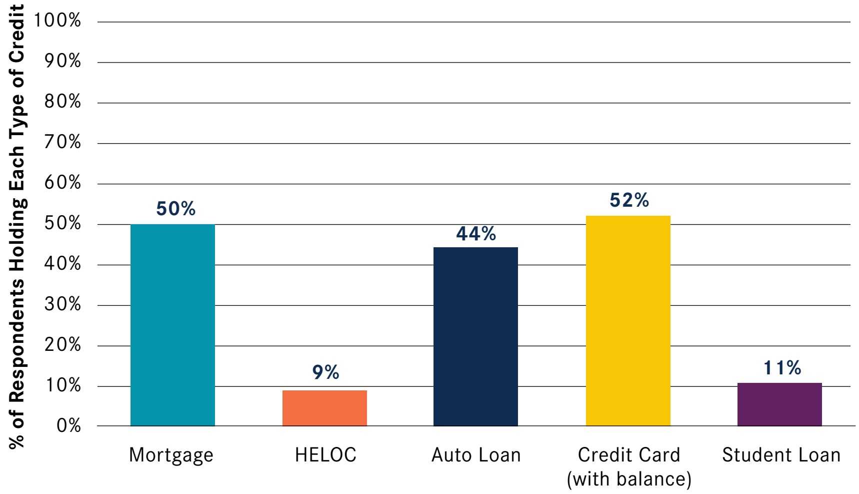
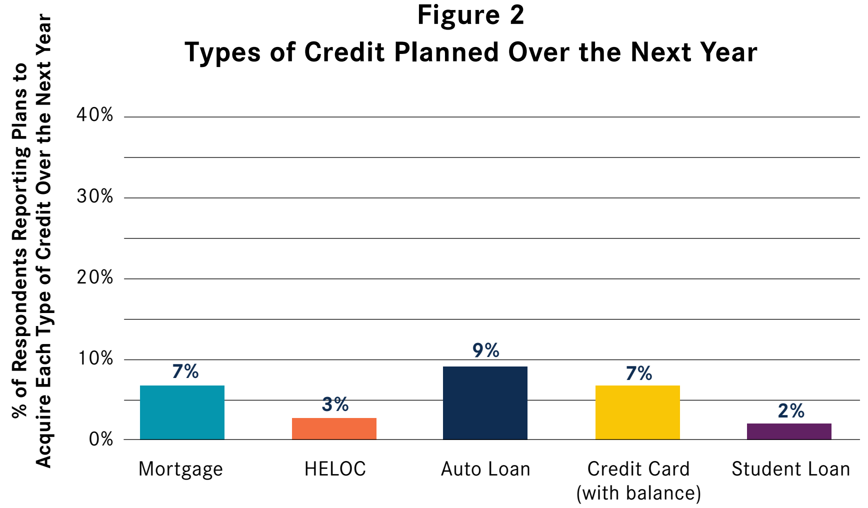


Figure 2
Types of Credit Planned Over the Next Year



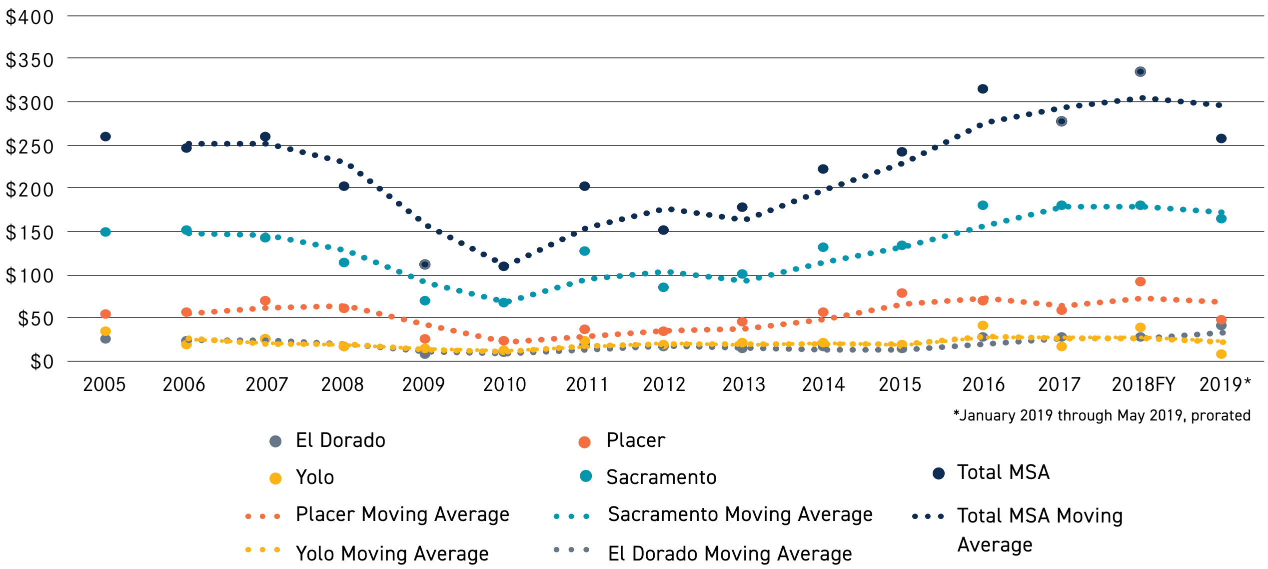
The Small Business *Economy*

MID-YEAR UPDATE

After breaking through all-time high levels, SBA total lending activity declined, driven by a noticeable drop in both Yolo and Placer Counties. Additionally, Sacramento County experienced a slowdown year to date, overshadowing the continued growth in El Dorado County, which is on pace to increase over 50% from 2018 levels. The total dollar volume of SBA loans in the Sacramento MSA is on track to decrease slightly below its two-year moving average.

Total SBA Loan Approvals by County

(in millions, 2-Year Moving Average)



Moving Average is average of two previous data points.

SBA Lending Activity shows SIGNS OF WEAKNESS... EXCEPT IN EL DORADO COUNTY

3-Year SBA Loan Growth Rate By County

County	Share of 2019 Loan Volume	2017-2019* Compound Annual Growth Rate
El Dorado	15%	13.8%
Placer	18%	-6.6%
Sacramento	64%	-2.8%
Yolo	3%	-23.1%
Total MSA	**100%**	**-2.5%**

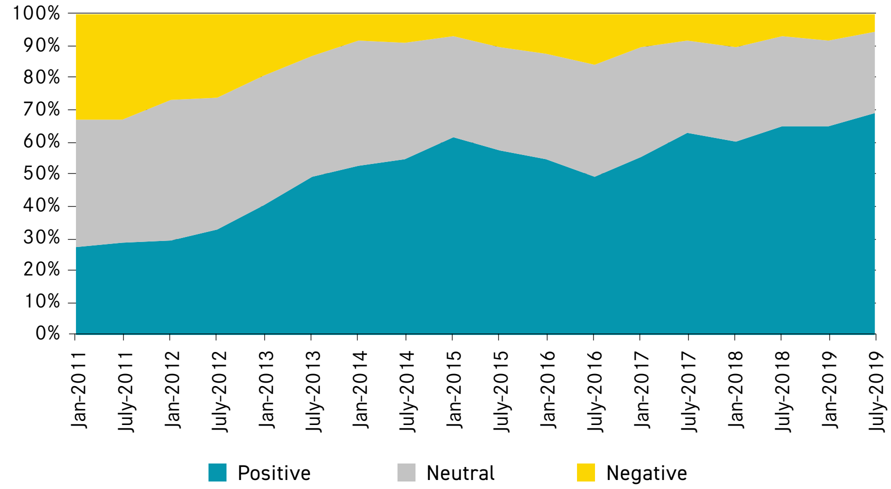
*January 2019 through May 2019, prorated

SMALL BUSINESS SENTIMENT IS UP

The latest reading of our Small Business Confidence Index (SBCI) showed a positive outlook across all areas except credit access, which stabilized and remained virtually unchanged from the previous reading. Though stabilizing, this slight dip in sentiment for credit access adds color to the slowdown in SBA total lending activity. When looked at more closely, the overall sentiment varies across the three sectors we measure – manufacturing, services, and other. The manufacturing sector showed the strongest reading on future revenue and the likelihood of new hires, though the weakest reading in credit access. Respondents from the services sector were the most confident regarding the future economic outlook and local business conditions ahead. The other sector respondents displayed the best reading in access to credit. Notwithstanding differences in sector responses, overall sentiment in our SBCI survey was largely optimistic.

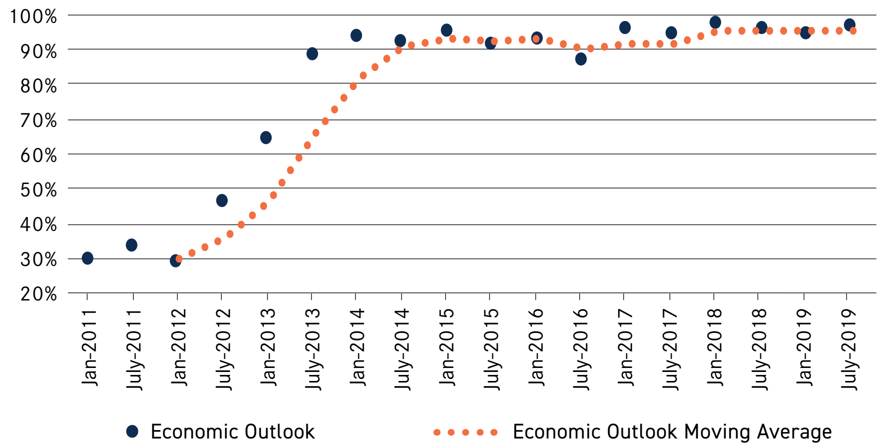
SBCI Overall Sentiment Responses

January 2011 – July 2019



SBCI Total Economic Outlook

(18-month moving average)



Moving Average is average of three previous data points.

Notwithstanding differences in sector responses, overall sentiment in our SBCI survey was largely optimistic.

SMALL BUSINESS

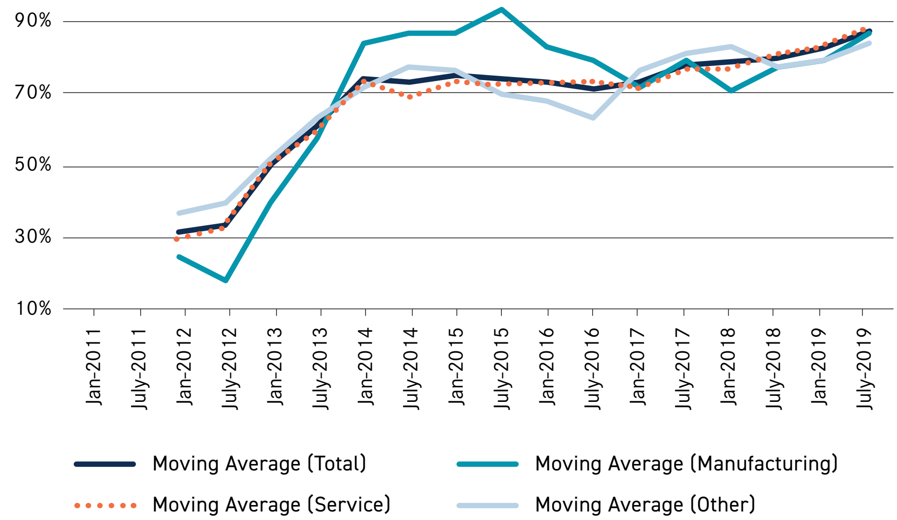
The Small Business *Economy*

Business transaction activity picked up from last quarter, as shown by a 7% increase in listings, paired with a 27% bounce in actual transactions; however, business sales are still down 21% from a year ago. Subject companies improved slightly in both median revenue and cash flow metrics; however, transactions were still largely focused on smaller deals, signaling a blinking yellow light in business transaction activity.

CREDIT ACCESSIBILITY CONTINUES ITS UPWARD TREND

SBCI Credit Accessibility by Sector

(18-month moving average)



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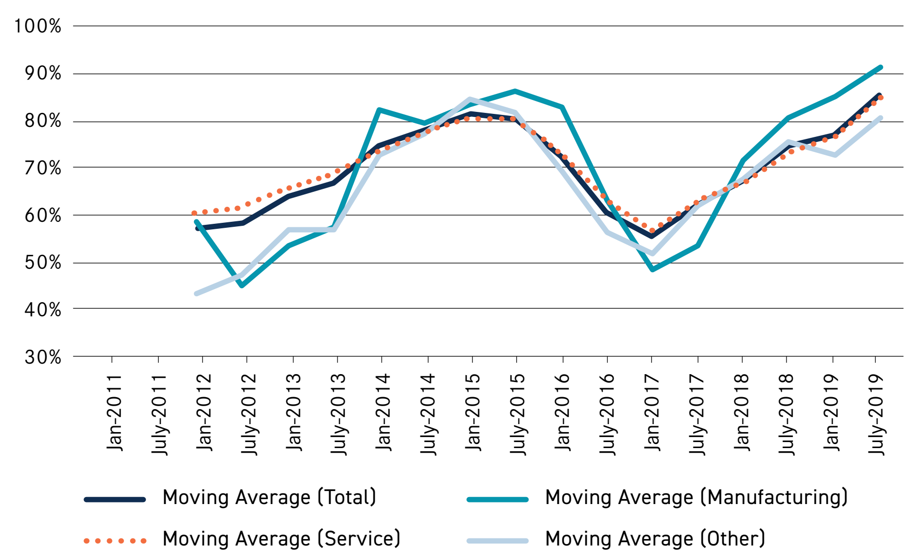
SMALL BUSINESS CONTINUING TO HIRE

SBCI Likelihood to Hire by Sector

(18-month moving average)



Moving Average is average of three previous data points.

Business transaction activity picked up from last quarter, as shown by a 7% increase in listings.

BUSINESS TRANSACTION ACTIVITY SAW A NOTABLE INCREASE...

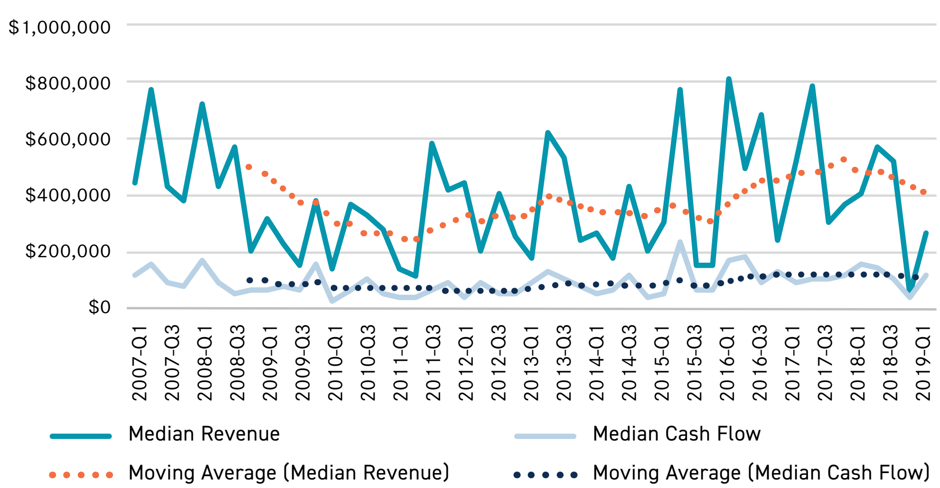
Listings vs. Closed Sales

Data Source: BizBuySell

...but SIZE AND VALUATIONS REMAIN LOW

Median Revenue & Cash Flow of Transactions

(2-year moving average)



Moving Average is average of eight previous data points.

Data Source: BizBuySell

SMALL BUSINESS

Real Estate

Office

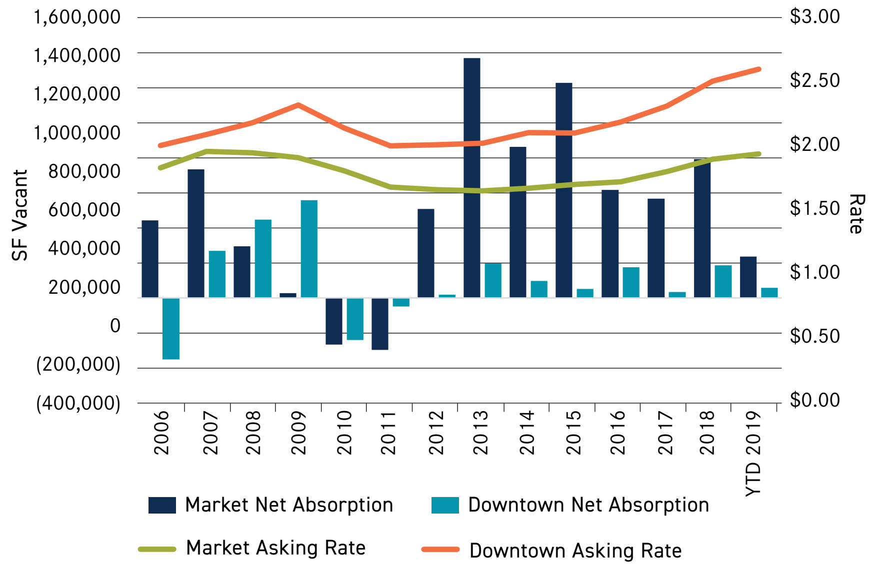
The office market has started 2019 strong, recording more than 237,000 square feet of net absorption resulting in a decline in vacancy of 110 basis points year-over-year to 8.6. Demand remains strong as more than 2.2 million sf of tenants are actively seeking office space in the Sacramento region. Construction remains a significant market trend but will bring little new available product to the market as only 90,000 sf of the 2.1 million sf is available.

High levels of demand have also led to an increase in lease rates and property values. Downtown remains a prime destination for tenants as asking lease rates for Class A properties eclipsed the $3.10 mark for the first time. More of the same is expected for the balance of the year as the market will continue to tighten, pushing lease rates further up.

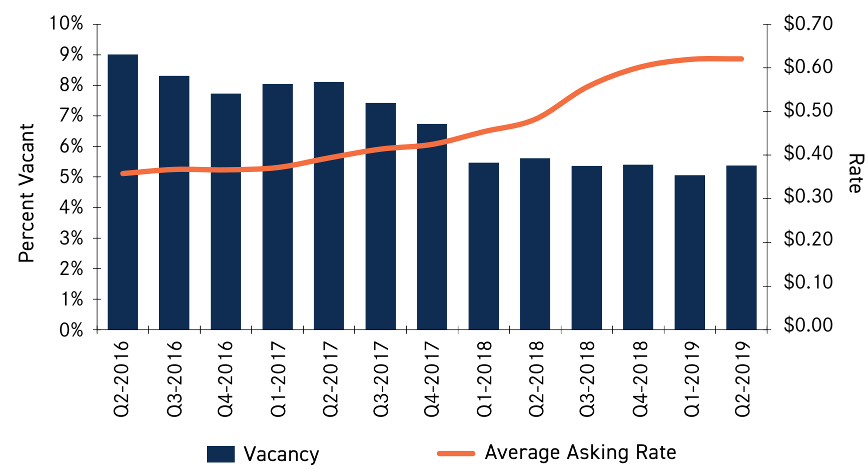
Industrial

The industrial market continues its record growth. Net absorption reached 238,000 square feet for the year, with vacancy reaching a record low of 4.4%. Sustained levels of low vacancy are responsible for lease rate growth which is up 8.7% per CoStar, the fastest growing industrial rents in the nation.

Office Market Activity 2006-YTD 2019



Industrial Asking Rate & Vacancy Rate Q2-2016 to Q2-2019



New speculative construction has begun to come online, with two speculative projects completed so far this year. More are expected, and while none have leased to date, they have seen strong activity and are not expected to remain available for long. Current construction is limited to large, high-cube buildings, while small businesses looking for smaller spaces in multi-tenant buildings have few options and rapidly increasing lease rates. The market is nearing replacement cost for these buildings, and there may be relief in sight for these small tenants.

Retail

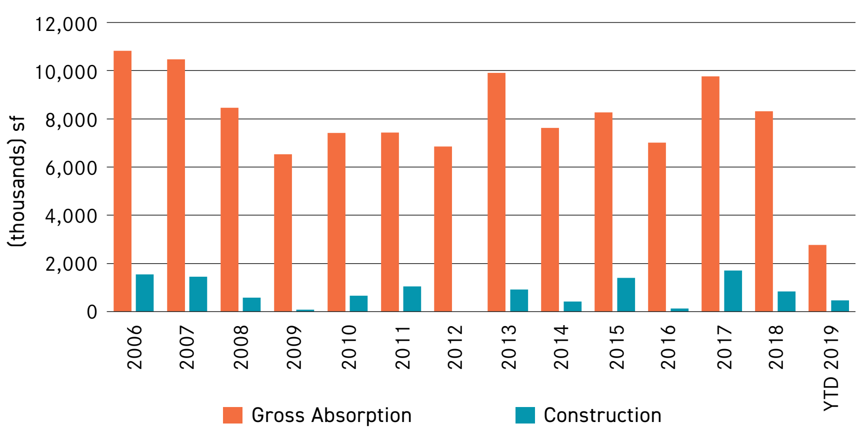
The Sacramento Retail market has largely plateaued. Net absorption has reached approximately 83,000 sf for the year, while leasing activity has been strong, surpassing 1.2 million sf. The strong market fundamentals are driven, in part, by a shift in landlord preference regarding tenant type. Experiential tenants like escape rooms, ax-throwing bars and indoor trampoline parks remain popular with customers and landlords alike.

While there is still retail construction, developers are selective with the projects they undertake. A large amount of new retail will be mixed use in the urban core, associated with either new office or multi-family projects. New shopping centers are largely relegated to the suburbs, with a strong anchor tenant needed in order for construction to begin.

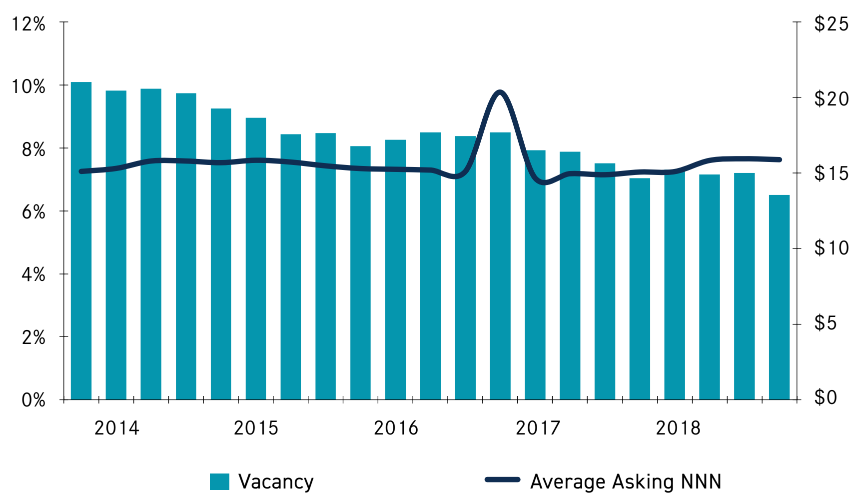
THE INDUSTRIAL MARKET CONTINUES ITS RECORD GROWTH

THE SACRAMENTO RETAIL MARKET HAS LARGELY PLATEAUED

Gross Absorption & Construction 2006-Q1 2019



Vacancy & Average Asking Rates 2013-2018



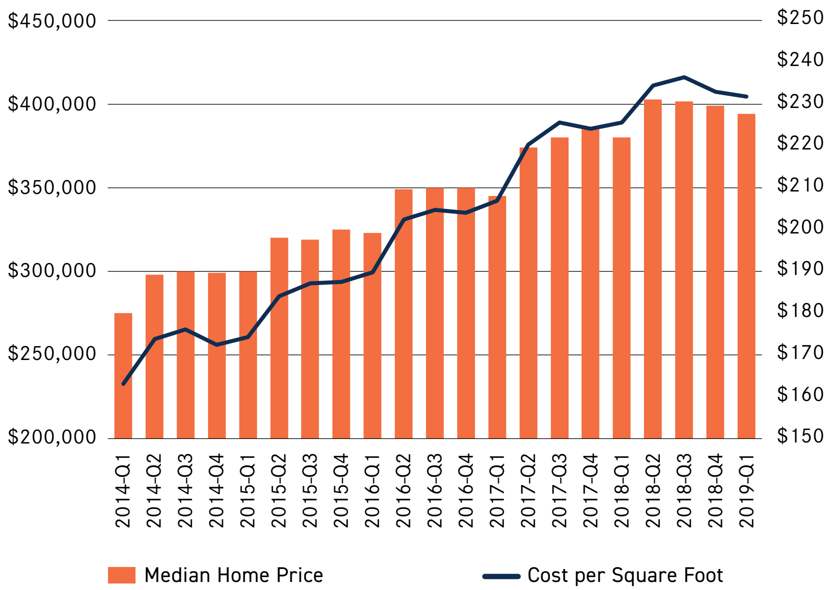
Real Estate

THE SINGLE-FAMILY HOUSING MARKET CONTINUES TO SEE GROWTH

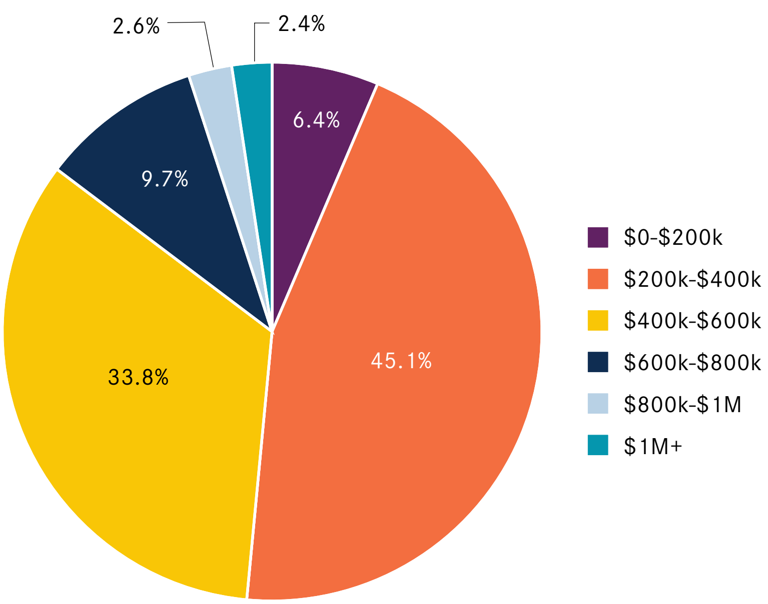
Single Family

The single-family housing market continues to see growth, but there are signs of deceleration. Sale prices on a per square foot basis across the Sacramento region increased by 3% year-over-year, compared to 6% in 2018 and 9% growth or more the prior 3 years. This is in part due to increased construction of single-family homes effectively capping home values at or very near their replacement cost. While more construction is taking place, we are still well below the peak of 22,000 in 2004. However, the cost basis for starter homes remains too high to justify new construction, leaving much of the construction market focused on second- or third-time buyers. With that said, home prices are far from outrageous, with sales below the $600,000 threshold, accounting for 85% of all home sales in the region.

Median Home Prices & Cost Per Square Foot 2014 - 2019



Home Sales by Price: YTD 2018



*2018 data includes January 1 through October 31

MID-YEAR UPDATE

Capital Markets & Banking *Forecast*

What a difference half a year makes! The SBR team along with just about everyone else interested in the capital markets expected to be on a path of increasing interest rates in 2019, and now we suddenly find ourselves asking "how low can we go?"

We initially predicted two quarter point hikes to the target range for Fed funds, but now, we could end up with two quarter point cuts before the end of the year, with one already taking place at the end of July. Concerns cited for the cut in July included worries about falling price levels as well as a hit to the domestic economy from a global trade environment that is experiencing ever increasing levels of friction.

We have already started to see the extent to which uncertainty around trade policy can adversely impact equity markets that are already trading at or above peaks in terms of cyclically adjusted price-to-earnings-ratio, and the "risk-off" trade has already led to the yield on the 10 year UST dipping well below 2.0%. Figure 1 shows what the trajectory of the S&P 500 would have to look like between now and the end of the year to achieve a 2019 return of 5%, in line with our initial forecast of equity returns in the low to mid-single digits for 2019.

Figure 1

2019 Mid to Low Single Digit Equity Return Scenario

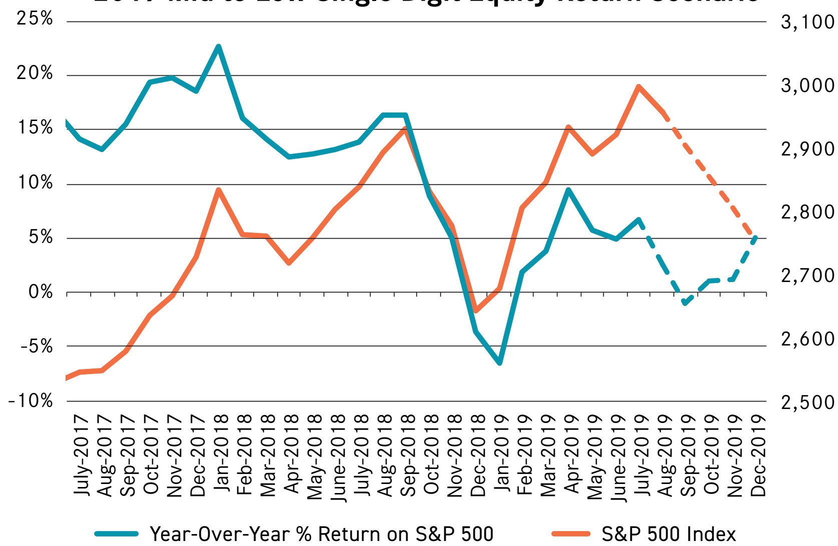
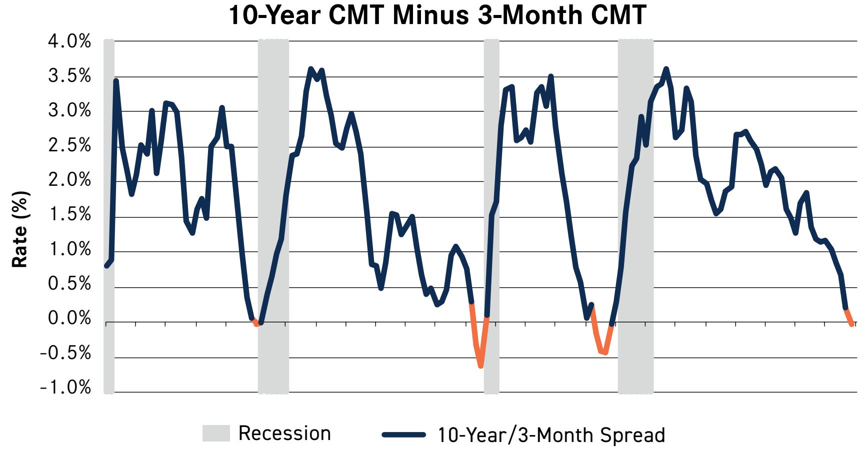


Figure 2

10-Year CMT Minus 3-Month CMT



> *...the volatility experienced toward the end of July suggests that markets are well aware of what the Treasury curve may be signaling.*

Figure 2 shows what the yield curve may be trying to tell us with the 10 year Treasury rate declining to less than the 3 month Treasury rate in the first half of 2019. As shown in the chart, this inversion typically predates a recession, and the volatility experienced toward the end of July suggests that markets are well aware of what the Treasury curve may be signaling.

On a more positive note, the region's financial institutions have performed very well in light of the flat/inverted yield curve; although, asset growth is expected to continue along a slowing trend. Net interest margins have continued to expand and efficiency ratios have continued to contract. But, the loan-to-deposit ratios shown in Table 1 coupled with the recent decline in the yield curve overall suggest margin expansion is likely to cease going into the latter half of 2019. Credit losses have remained near cyclical lows, and are not expected to become an issue this year, but they may tick back up if the economy slows too much in 2020 due to a broader weakness for the domestic economy.

Table 1
Bank and Credit Union Performance Trends

	12/31/14	12/31/15	12/31/16	12/31/17	12/31/2018[1]	3/31/2019[2]
Total Assets ($ in 000s)						
Banks Growth %	$12,964,736	$14,256,660 10.0%	$15,614,770 9.5%	$16,608,673 6.4%	$19,202,556 15.6%	$19,590,370 16.4%
Credit Unions Growth %	$14,341,117	$15,615,129 8.9%	$17,091,518 9.5%	$18,415,635 7.7%	$19,669,888 6.8%	$20,404,382 7.5%
Total Loans ($ in 000s)						
Banks Growth %	$7,312,850	$8,342,836 14.1%	$9,395,492 12.6%	$10,199,760 8.6%	$12,069,540 18.3%	$12,246,151 18.4%
Credit Unions Growth %	$7,821,320	$9,350,834 19.6%	$11,647,344 24.6%	$13,156,329 13.0%	$14,473,409 10.0%	$14,467,989 8.5%
Loans-to-Deposit Ratio						
Banks	65.5%	68.2%	70.0%	71.6%	73.0%	73.4%
Credit Unions	62.3%	68.2%	77.6%	81.6%	84.3%	81.4%
Net Charge-Offs / Avg. Loans						
Banks	0.11%	-0.10%	-0.04%	0.04%	0.03%	-0.01%
Credit Unions	0.43%	0.33%	0.34%	0.43%	0.46%	0.41%
Net-Interest Income / Avg. Assets (aka, Net Interest Margin)						
Banks	3.21%	3.30%	3.29%	3.33%	3.52%	3.60%
Credit Unions	2.40%	2.51%	2.57%	2.68%	2.85%	2.94%
Efficiency Ratio						
Banks	71.8%	68.2%	69.2%	63.9%	60.8%	61.6%
Credit Unions	74.7%	76.5%	72.2%	68.8%	66.5%	64.5%
Return on Assets						
Banks	0.90%	1.00%	0.98%	0.93%	1.29%	1.34%
Credit Unions	0.82%	0.72%	0.82%	0.84%	0.93%	1.03%

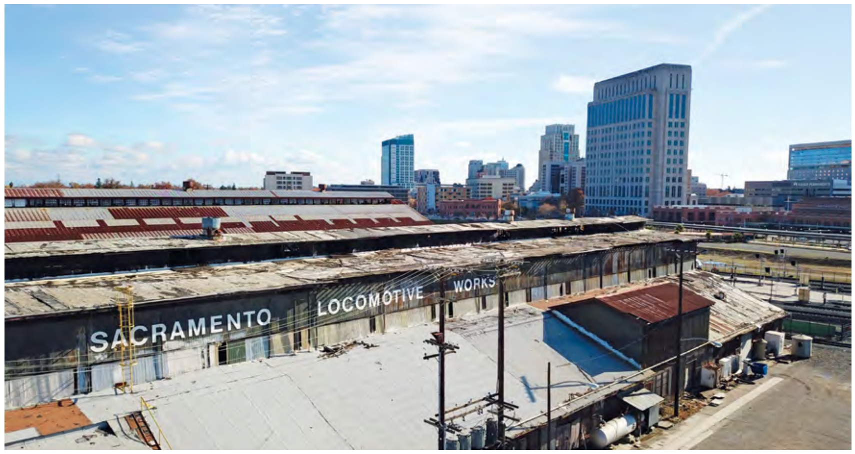
Source: Callahan

[1] Regional bank figures impacted by the acquisition of First Northern Bank of Northern California by Tri Counties Bank in 2018.

[2] Data as of March is year-over year.

Capital Markets & Banking *Forecast*

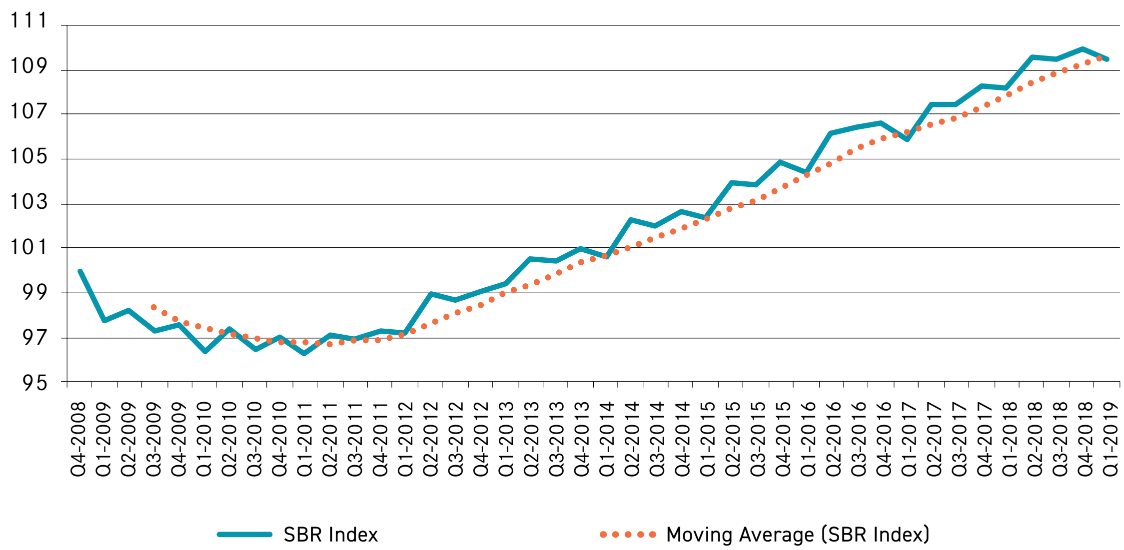
THE REGIONAL ECONOMY CONTINUES TO EXPAND



Our proprietary SBR Financial Conditions Index aligns with the success of our regional financial institutions and shows that the regional economy continues to expand (Figure 3).

Our proprietary SBR Financial Conditions Index aligns with the success of our regional financial institutions and shows that the regional economy continues to expand

Figure 3
SBR Index (with 2-year moving average)



Moving Average is average of four previous data points.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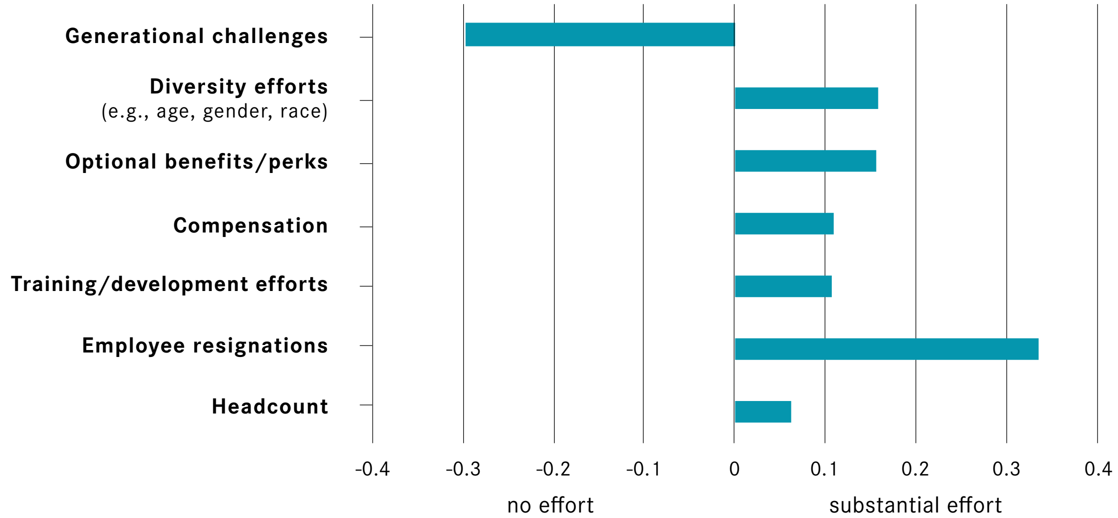
MID-YEAR UPDATE

Human Capital *Trends*

Figure 1 shows the first half of 2019 changes, where positive numbers indicate growth and negative numbers indicate reductions or shrinkage. We see a change in anticipated voluntary turnover, with increased resignations indicated. Meanwhile, headcount is staying static from the first part of the year such that organizations report moderate recruiting efforts. Together these two indices may indicate an overall shrinkage of the local workforce. At the same time, reports indicate increased efforts regarding training and development internally. In essence, the focus appears to be to increase competencies in existing workforce instead of hiring new talent in the open labor market. Regarding overall compensation, we see increases both for basic compensation (salaries and wages) as well as optional benefits and perquisites. Finally, diversity and inclusion efforts are seeing an uptick.

Greater efforts on talent management initiatives across the board are reported, with a vast majority of companies (93%) reporting new or considerably revised talent management initiatives; the top three being learning and development, broader non-financial employee recognition, and individual performance-related bonuses (Figure 2). HR's fundamental training and development efforts captured the number one spot in the first part of the year, while recognition and bonuses declined, indicating a shift in focus for these two initiatives. Artificial Intelligence remains a priority, although the focus has shifted from preparation to implementation and training. Diversity and inclusion remains a priority, while renewed efforts for employee autonomy and creativity (bottom up innovation ideas) are reported. Initiatives not on the upcoming agenda include team- and organizational- level performance bonuses, encouragement of employee entrepreneurship

Figure 1
Human Capital Trends, Summer 2019



Our local organizations are in need of job candidates to fill positions, as well as applicants with the right set of knowledge, skills, and abilities.

GREATER EFFORT ON TALENT MANAGEMENT INITIATIVES across the board AS COMPARED TO EARLY 2019

without penalizing possible related failures, complementary health care assistance, complementary pension arrangements, and efforts towards reducing wage disparity between top management and highly skilled talent.

Table 1 lists factors expected to exert the most influence on the overall organization as we close 2019, with the top two from 2018 remaining in place: skills gap and talent shortage. Our local organizations are in need of job candidates to fill positions, as well as applicants with the right set of knowledge, skills, and abilities. Lingering concerns are challenging productivity and profit targets as well as cost reductions. Artificial Intelligence is increasing in importance, moving from a shared eighth place in early 2019 to rank number five. Restructuring and downsizing are not indicated to be the avenues by which cost reductions will need to occur.

Figure 2
Q3 and Q4 Talent Management Initiatives

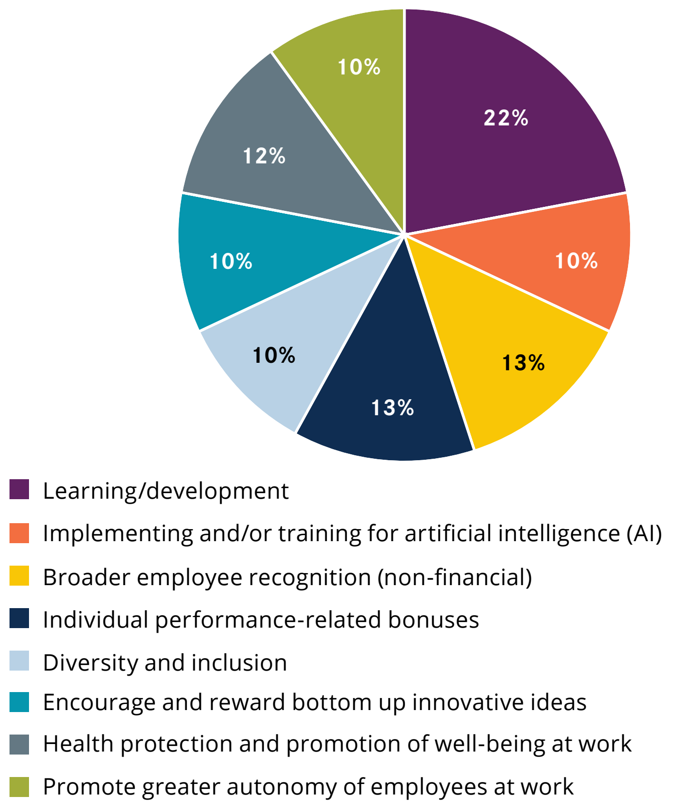


Table 1
Factors Expected to Exert the Most Influence in Q3 and Q4 2019

Rank	Factors
1	Skills gap (job candidates available but don't have desired skills)
2	Talent shortage (job candidates not available)
3	Challenging productivity and profit targets
4	Pressure on cost reduction
5	AI (machine learning, new technologies)
6	Change in company culture
7	Development and management of new competencies
8	Expansion of operations in new markets
8	Increased market competition
8	Market volatility and fear of recession
9	Organizational restructuring
10	Downsizing

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LENNY MENDONCA
Director, California Governor's Office of Business and Economic Development

JANUARY 2020

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University Union Ballroom

Keynote Speaker: Lenny Mendonca

Lenny Mendonca is the Chief Economic and Business Advisor to Governor Gavin Newsom of California and Director of the Governor's Office of Business and Economic Development (GO-Biz). He is a Senior Partner Emeritus of McKinsey & Company and a Lecturer on Inequality at the Stanford Business School.

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