

# CALIFORNIA ECONOMY

## WHY SO SKITTISH?

The biggest fear among today’s media and policymakers is that California’s economy is heading for a double-dip recession. The skepticism about the current economy stems in part from the severity of the Great Recession, which took a huge psychological toll on California’s residents and policymakers alike. In some sense, the state went from a mode of denial about whether the bubble would ever burst (and force a correction to the key imbalances that had built up over several decades), to a mode of hysteria about whether the recovery would ever materialize.

**California's Recessionary Effects**  
**Peak-to-Trough Decline, Selected Indicators**

Category	Decline
Jobs Lost (000s)	-1,366.40
Home Price Decline (%)	-57.1
Taxable Sales Decline (%)	-22.2
Residential Permit Decline (%)	-84.8
Nonresidential Permit Decline (%)	-56.6

Source: Calculations by Beacon Economics

When you take stock of the damage done during this downturn, it is easy to see why Californians are so apprehensive. There is a big hole in our economy: whether you are looking at the nearly 1.4 million jobs lost, the 57% decline in home prices, or the 22% decline in taxable sales, it’s clear that California was hit hard by the recession. Many of the jobs lost were in retail and construction—sectors that are expected to lag the recovery, therefore leading to a lot of uncertainty among that segment of the unemployed. But the recessionary effects were fairly widespread, extending beyond retail and construction, with financial markets and banks also highly affected by the bursting of the bubble. This cocktail of declines in employment, consumer spending, home prices, and asset values over the past few years has left little for Californians to feel hopeful about in the absence of positive news.

On top of these psychological effects, the first half of 2011 saw several key data releases that led many in the media to fear the worst. This pessimism about the recovery first kicked off when the S&P/Case-Shiller home price index showed weakening home prices across the nation. Suddenly, grim headlines were increasingly splashed across the local daily newspapers. Mortgage

News Daily looked at the data and concluded, along with many others, that “Case-Shiller Data Confirms Double-Dip in Home Prices.”<sup>4</sup>

U.S. Real GDP Growth & Contributions to Growth						
Component	Q1-10	Q2-10	Q3-10	Q4-10	Q1-11	Q2-11
Gross Domestic Product	3.90	3.80	2.50	2.30	0.40	1.00
Consumption	1.92	2.05	1.85	2.48	1.47	0.30
Durables	0.70	0.56	0.63	1.20	0.85	-0.40
Nondurables	0.75	0.30	0.47	0.67	0.25	0.07
Services	0.47	1.18	0.75	0.61	0.36	0.64
Gross Domestic Investment	3.25	2.92	1.14	-0.91	0.47	0.78
Structures	-0.76	0.18	0.10	0.26	-0.40	0.38
Equipment/Software	1.32	1.45	0.94	0.56	0.60	0.55
Residential	-0.41	0.50	-0.76	0.06	-0.06	0.08
Change in Inventories	3.10	0.79	0.86	-1.79	0.32	-0.23
Net Exports	-0.97	-1.94	-0.68	1.37	-0.34	0.09
Exports	0.86	1.19	1.21	0.98	1.01	0.41
Imports	-1.83	-3.13	-1.89	0.39	-1.35	-0.33
Government	-0.26	0.77	0.20	-0.58	-1.23	-0.18
Federal	0.23	0.71	0.26	-0.26	-0.82	0.16
State/Local	-0.49	0.05	-0.06	-0.33	-0.41	-0.34

Source: U.S. Bureau of Economic Analysis

Next were the national economic releases, which showed that after fairly robust growth in 2010, real GDP growth slowed to less than 0.4% in the first quarter of 2011 and to 1% in the second quarter. On top of that, a weak national employment report in August showed the unemployment rate holding steady at 9.1% after the country added no jobs from July. Indeed, here in California the unemployment rate remains in double digits, with only modest improvements from its peak.

Finally, the summer was capped off by the debt-ceiling debacle, with politicians playing a game of economic chicken over our willingness to meet our short-term obligations. The standoff created a great deal of uncertainty in the marketplace, and both businesses and consumers sat on the sidelines wondering what would come of the debate. Combined with the natural disaster in Japan, which had a significant impact on auto sales during June and July due to supply chain disruptions, these events caused us to see some rather weak performances in the consumer accounts in the second quarter.

Still, as bad as the news has been recently, a double-dip recession requires the double D’s: drivers and data. In the run-up to the recession, we had an ample supply of both. The drivers of the Great Recession were the fundamental imbalances in the housing, consumer, and finan-

<sup>4</sup>Graham, Matthew, “Case-Shiller Data Confirms Double-Dip in Home Prices,” Mortgage News Daily, May 31, 2011, [http://www.mortgagenewsdaily.com/05312011\\_case\\_shiller.asp](http://www.mortgagenewsdaily.com/05312011_case_shiller.asp).

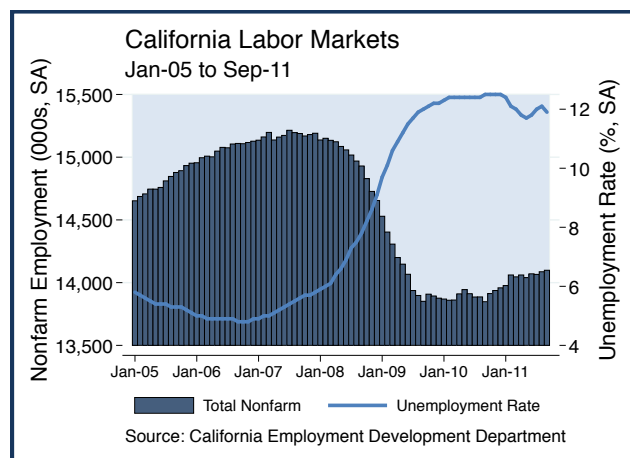
cial markets. Home prices were growing too fast relative to incomes, and consumers' financial institutions were spending too much and taking on excessive amounts of debt. Not only did we have the drivers, but the data supported a recession as well. Defaults and foreclosures started rising dramatically and the securitized real estate loans began suffering losses. The subsequent effects on the financial markets precipitated the housing and financial crisis and led to a major pullback on the part of consumers. This time around, Beacon Economics cannot find either the data or the drivers that would suggest that a double dip is imminent. In the next section, we review the data and discuss why a second recession is not an immediate concern.

## DOUBLE-DIP: FACT OR FICTION?

Despite the double-dip hype in the media, the view at Beacon Economics is that the recovery continues to plug along, though not at the pace that we would like to see. This recovery was always going to be a slow one. California had one of the largest housing and consumer spending bubbles in the nation and has since suffered one of the largest downturns relative to most other states. That said, most of the indicators show that the state continues to recover from the Great Recession.

Take the labor markets as a prime example. We've heard the term "jobless recovery" in the past, and this is certainly a feature of the new economy—in response to weakening demand conditions, employers cut back on their workforce and squeeze as much productivity and efficiency as possible from those who remain. The advent of computers, robotics, and other high-technology products make this more possible for businesses than ever before. Indeed, we can see a marked difference in employment recoveries in the last three recessions compared with earlier recessions.

Nonetheless, California's labor markets are moving forward. In terms of total nonfarm employment, the state has added back more than 225,000 jobs since reaching bottom in 2010. Obviously this is a small number of jobs in relation to the total job losses we suffered, but it is a far cry from a continued decline. The unemployment rate does remain stubbornly high—12% on a seasonally adjusted basis in July. However, even on that front California is making progress, with the rate down



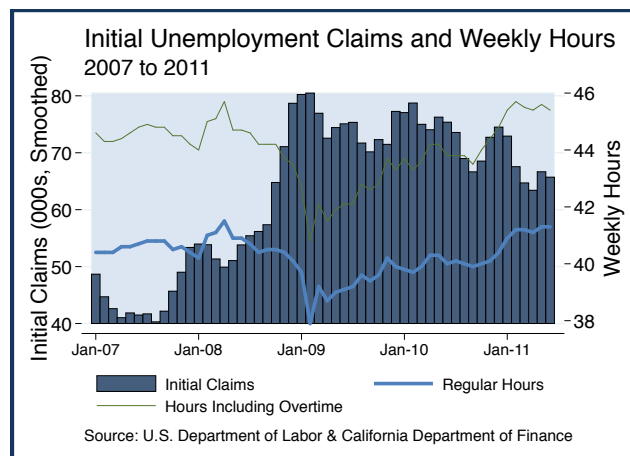
from its peak of 12.5%. And we know that labor markets are traditionally a lagging indicator of economic activity, so it is not surprising that we have yet to see employment take off.

Importantly, the leading indicators continue to show that California's economy is improving. For example, with 56,000 initial claims for unemployment insurance over the last 3-week period in August, California remains well below the 83,000 initial claims for unemployment that were filed during the heights of the recession. In addition, weekly hours of work in the manufacturing sector continue to rise. According to the California Department of Finance, the average work week hit 41.3 hours in the most recent data available, which is the highest level since before the recession began. For existing workers, this has created some overtime opportunities, averaging roughly 4 hours per week. These statistics show that although the news has been rather grim, businesses are continuing to place high demands on their existing workforce. Eventually, these increases in productivity will give way to increased employment as employers reach the limit of what can be extracted from existing workers.

It's not only the labor markets that give us optimism about the recovery going forward. There have also been noticeable improvements in several sources of demand. Chief among these are exports. California has always been an export state, due in part to its ports and its access to the faster-growing economies in East Asia. However, California also produces the high-technology products and services that have continued to do well in the new economy. This includes pharmaceuticals, intellectual property, biotechnology products, industrial machinery, and computers.

In fact, on a year-to-date basis, California's exports continue to do well, rising 12.7% over this time last year. The boost in exports has been led by our technology products (electrical and industrial machinery, and photo/optic/medical equipment), though our agricultural sector has been posting strong gains as well.

Because the dollar has weakened during the downturn, California's exports have grown even more attractive in overseas markets, and this trend is evident in the uptick in California-made exports. Currently, the real U.S. exchange rate measured against a broad basket of currencies is at its lowest level in over three decades. As the price of our currency falls, California's goods



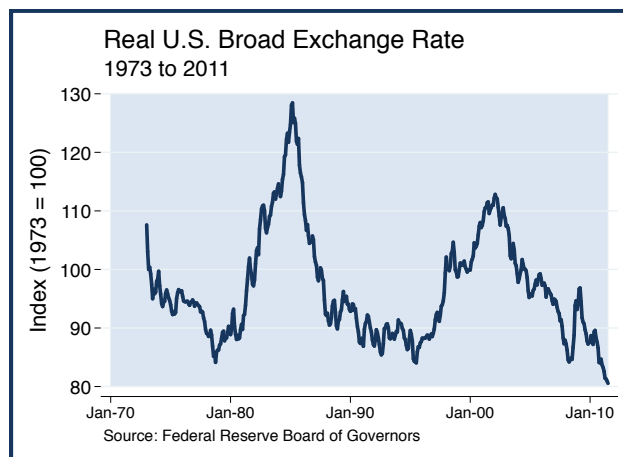
**California-Made Exports by Commodity Type**  
**Values in \$000s**

Commodity	2010 YTD	2011 YTD	Percentage Change	
			2009-10	2010-11
Electric Machinery/Sound Equip/TV Equip	15,409.83	16,338.39	19.74	6.03
Industrial Machinery/Computers	13,748.84	15,373.03	32.26	11.81
Optic/Photo/Medical/Surgical Instrmnts	8,970.25	9,710.30	18.78	8.25
Natural Resources/Precious Metals	3,339.90	4,168.30	63.29	24.80
Edible Fruit & Nuts/Citrus/Melon	3,467.31	4,038.68	21.05	16.48
Vehicles/Parts	3,476.14	3,995.70	13.24	14.95
Aircraft, Spacecraft, & Parts	3,389.63	3,861.90	-10.49	13.93
Mineral Fuel/Oil/Bitumin Subst/Mineral Wax	2,483.13	3,172.57	23.03	27.76
Plastics	2,335.90	2,586.14	16.98	10.71
Pharmaceutical Products	2,248.61	2,363.62	13.59	5.11
<b>Total</b>	<b>80,345.11</b>	<b>90,527.84</b>	<b>19.25</b>	<b>12.67</b>

Source: Calculations by Beacon Economics

become increasingly competitive on global markets. Given that the state produces goods that are in demand overseas, this should continue to bolster the state’s recovery moving forward.

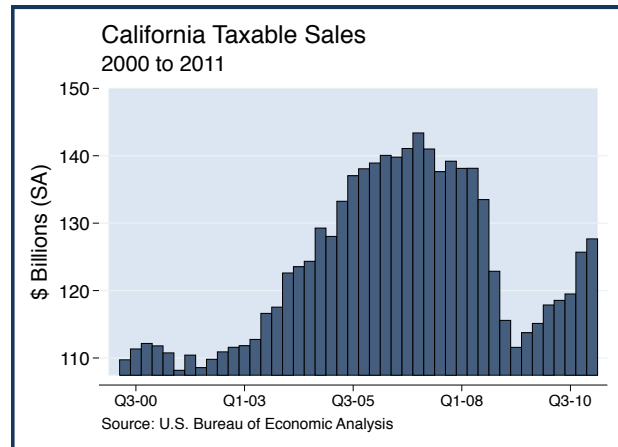
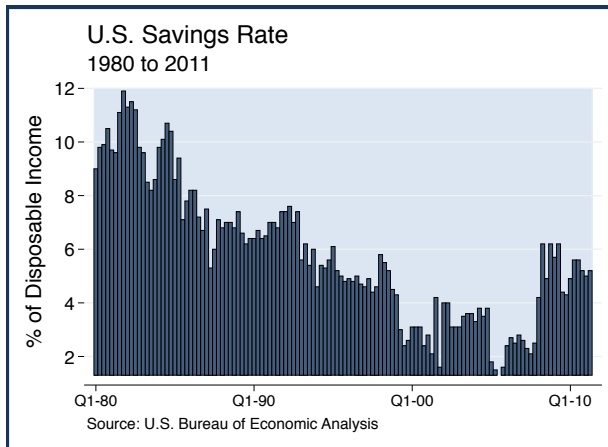
Another positive sign for the state is that consumers are beginning to feel comfortable about opening their wallets again. In the run-up to the bubble, many households felt so asset-rich that they stopped saving for the future. In the minds of many, the surge in home equity and the value of their stocks were sufficient to finance their retirements. As a result, we saw savings rates fall from more than 10% in the 1980s to less than 1% by the peak of the market. As the downturn gained steam, many consumers realized that a zero-savings cushion did not provide the flexibility required to deal with economic fluctuations; they pulled back sharply and began saving again.



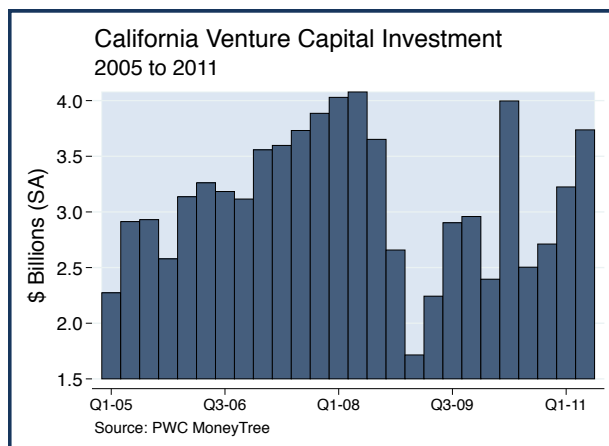
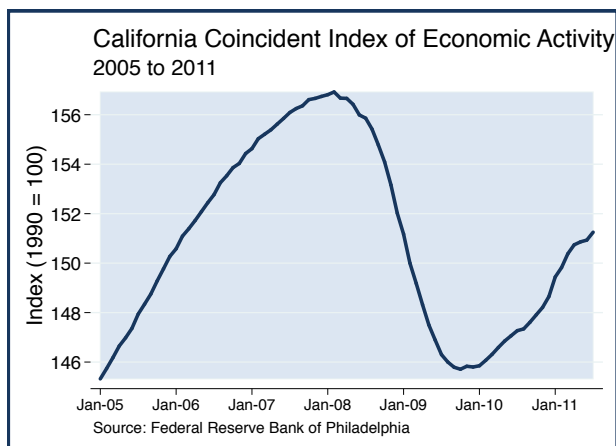
### California Sales Tax Revenue Allocations by Type Adjusted for Economic Factors

Category	2010 Q1	2011 Q1	% Change
Autos/Transportation	142,127,742.99	160,995,259.81	13.28
Building/Construction	73,706,220.14	77,746,769.87	5.48
Business/Industry	157,200,542.93	166,949,888.87	6.20
Food/Drugs	68,035,978.14	70,137,400.70	3.09
Fuel/Service Stations	120,414,739.67	147,124,997.79	22.18
General Consumer Goods	264,529,997.88	277,841,051.13	5.03
Restaurants/Hotels	132,645,507.83	140,970,581.08	6.28
<b>Total</b>	<b>1,075,443,136.83</b>	<b>1,174,103,828.18</b>	<b>9.17</b>

Source: HdL Companies



Currently, savings rates have popped back into the 5% range, which is still probably not enough, but household balance sheets are in much better shape than when the recession began. This is showing up in the state's numbers on consumer spending, which have risen consistently for several quarters consecutively. Although the data for the second quarter of 2011 are not available yet, taxable sales rose by more than 14% from the trough in the second quarter of 2009. Most of these gains have come from spending on automobiles and on general entertainment, with restaurants posting solid gains in the first quarter of this year. However, the state is also benefiting from increased business investment. Specifically, the business and industry category posted a 6.1% year-over-year gain in the first three months of 2011. Given that consumers are such a large part of the economy, this increase in spending should help to bring about increased economic growth as California moves forward.



In fact, we’ve already seen these trends contribute to overall economic growth in the state. According to the Federal Reserve Bank of Philadelphia’s coincident index of economic activity, California’s economy is indeed on the mend. In total, it is estimated that the state has added back roughly 3.8% of its economic output since reaching bottom in October 2009. The index does show California well below its 2008 peak, but the state has seen 19 straight months of uninterrupted growth. Although the labor markets in particular are leaving much to be desired, this is not an indication of a double dip in the economy but rather an indication of rising efficiency and rising productivity—as well as a rising skills mismatch that we will discuss below.

There have been some concerns about broader macroeconomic conditions recently, with real GDP growth slowing in the first half of 2011. Our view is that this below-average growth was temporary—mostly associated with (1) supply chain disruptions related to

### California Venture Capital Investment % of Total, Q2 2011

Sector	% Share
Software	24.1
Medical Devices and Equipment	15.0
IT Services	11.9
Biotechnology	9.7
Media and Entertainment	9.6
Industrial Energy	8.3
Semiconductors	7.6
Consumer Products and Services	2.7
Networking and Equipment	2.1
Business Products and Services	1.8
Electronics Instrumentation	1.6
Telecommunications	1.5
Computers and Peripherals	1.3
Financial Services	1.3
Healthcare Services	0.9
Retailing and Distribution	0.5
Other	0.2
<b>Total</b>	<b>100.0</b>

Source: PWC MoneyTree

natural disasters in Japan and the Midwest, which caused auto sales to take a tumble, (2) the political game of chicken that defined the debt-ceiling debate, which created a sense of uncertainty among both businesses and consumers, and (3) the erosion of purchasing power fueled by the spike in oil prices, which have already begun to come down. Despite the transitory nature of these phenomena, policymakers and the media have all pointed to these events as a sure sign that a double-dip recession is imminent. The view at Beacon Economics is actually quite the contrary. Despite this turbulence, the underlying indicators of demand have yet to drop off despite what you read in the newspapers.

When one looks to the private equity markets, many in the industry are still “betting” on California. According to a joint project between PWC and MoneyTree, venture capital investment is on the rise. Since hitting a low of \$1.7 billion in the first quarter of 2009, new venture capital investment has risen sharply—nearly 118%. We have another cause for optimism about California’s future when we see where these funds are being directed. Specifically, four sectors took home more than 60% of all the venture capital funding in the state last quarter: the software, medical devices and equipment, IT services, and biotechnology industries. These are sectors that play to California’s strengths in that they require a highly skilled workforce and access to overseas markets for future growth. As the economy heals, having a concentration in these sectors will help California resume the strong growth trajectory that it exhibited before the downturn.

## THE REAL CULPRIT—SKILLS MISMATCH

Although we believe that fears of a double dip have been largely overblown in the media and that there are reasons to be cautiously optimistic about a sustained recovery, there are nonetheless several factors preventing California from experiencing faster growth. The most serious problem is the skills mismatch in the labor market. To be more specific, there is a real dichotomy between the skill sets of the workers in those sectors that were pummeled by the downturn and the skill sets required by the sectors that are leading California out of the recovery. On a proportional basis, construction, real estate, and retail trade were among the hardest-hit sectors in the region in terms of job losses. These sectors traditionally have low education requirements and pay relatively low wages, which are two of the predominant characteristics of our unemployed population.

The Annual Social and Economic Supplement to the Current Population Survey (CPS) allows us to examine the characteristics of the employed and unemployed populations in California. Given that the consumer-oriented and housing-oriented sectors suffered the most during the

**California Unemployment by Industry  
2010 Current Population Survey**

Industry	Employed	Unemployed	Unemployment Rate (%)
Agriculture, forestry	395,361	209,439	34.6
Construction	1,137,637	244,155	17.7
Transportation and utilities	689,358	130,142	15.9
Other services	1,025,837	190,259	15.6
Wholesale and retail trade	2,395,685	392,817	14.1
Leisure and hospitality	1,437,273	234,077	14.0
Manufacturing	1,446,132	204,776	12.4
Information	482,804	60,392	11.1
Financial activities	1,078,028	115,255	9.7
Educational and health services	3,300,270	264,470	7.4
Professional and business	2,003,732	116,383	5.5
Public administration	636,122	31,106	4.7
<b>Total</b>	<b>16,028,239</b>	<b>2,193,271</b>	<b>12.0</b>

Source: National Bureau of Economic Research

recession, it is no surprise to see that these sectors are exhibiting the highest unemployment rates in the state, while the sectors that have been performing relatively well have maintained much lower levels of unemployment. According to the 2010 statistics, the unemployment rates for construction, wholesale and retail trade, and the household sector (other services) are showing unemployment rates ranging from 14% to nearly 18%, which are much higher figures than the statewide average for all sectors. On the other hand, education, and professional and business services are far below the state average, with unemployment rates in the single digits. If we want to plan for future growth, it is important to realize that the sectors with high rates of unemployment account for more than one-third of all the unemployed workers in California. Getting these folks back to work is a big part of bringing down California's unemployment rate—though this is much easier said than done.

In addition to letting us pull out unemployment statistics by industry, the CPS also allows us to look at unemployment by education level, which highlights some important challenges that our state will face going forward. The most recent data for 2010 shows that Californians with the lowest levels of educational attainment are being disproportionately affected by the downturn, while the most highly educated residents are maintaining “normal” levels of unemployment. More than 17% of all adults over the age of 25 who have less than a high school diploma were unemployed last year, compared with roughly 5% of all Californians with a graduate or

**California Unemployment by Education  
2010 Current Population Survey**

Education	Employed	Unemployed	Unemployment Rate (%)
Less than HS	1,923,102	409,726	17.6
High School	3,087,210	346,450	10.1
Some College	3,523,567	510,446	12.7
Bachelors Degree	3,774,069	317,492	7.8
Grad./Prof. Degree	1,838,829	100,481	5.2
<b>Total</b>	<b>14,146,776</b>	<b>1,684,595</b>	<b>10.6</b>

Source: National Bureau of Economic Research

professional degree. Not only do the less educated suffer from higher rates of unemployment, but they are a much larger group than Californians with graduate degrees. Residents without a college degree constitute more than 75% of the unemployed.

This represents a serious issue for both the short-term prospects and the long-run growth of California's economy. Earlier, we discussed some of the bright spots in the state's recovery, from trade in high-tech goods and intellectual property to new developments in biotechnology and software. California is indeed adding jobs: more than 225,000 since late 2010; but almost half of these jobs have been in the professional and business services or education and health industries. It is very difficult to take advantage of growth in these sectors without a college degree. It's true that some of the jobs in administrative support and in education and health care do provide some jobs for those on the lower end of the educational-attainment scale, but these industries are dominated by jobs that require some postsecondary training.

Of course, policymakers cannot wave a magic wand and grant every Californian a college degree. But that does not mean that we should ignore the skills mismatch that is currently bogging down the state's recovery and jeopardizing the long-run growth in sectors that, up to now, have been the centerpiece of California's "new economy." The current budget woes certainly do not make things any easier, but these simple statistics would suggest that we need more focus on education, not less.

This means requiring better quality results from our K-12 system, which will require investments at a time when K-12 spending is on the chopping block. This also means that we will need to fill our universities with more Californians, even though the state can collect more money from out-of-state students. California needs to expand enrollments and provide more assistance to lower-income students. And not everyone wants or needs a four-year degree,

**California Unemployment by Age  
2010 Current Population Survey**

Age	Employed	Unemployed	Unemployment Rate (%)
25 or Less	2,221,619	522,260	19.0
26 to 35	4,112,447	371,910	8.3
36 to 45	3,454,542	545,583	13.6
46 to 55	3,503,335	492,566	12.3
56 to 65	2,095,266	209,710	9.1
66+	655,150	51,240	7.3
<b>Total</b>	<b>16,042,358</b>	<b>2,193,271</b>	<b>12.0</b>

Source: National Bureau of Economic Research

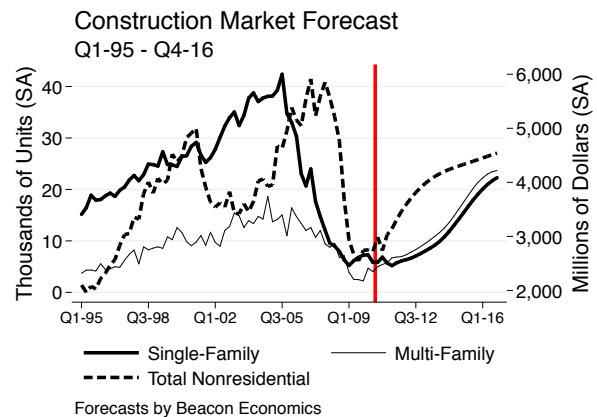
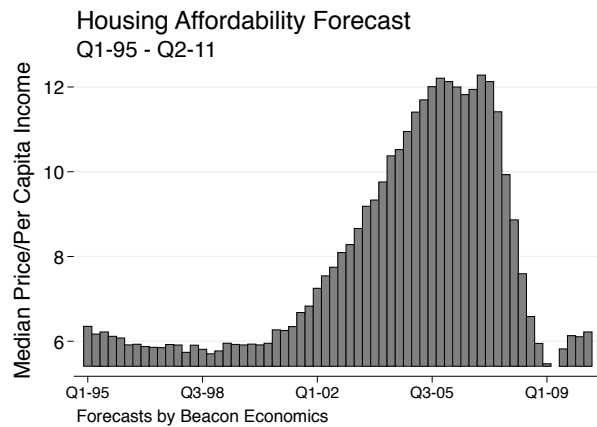
which is why our community college system can play a critical role—especially over the short-run—in providing professional development opportunities in certificate or other training and retooling programs that would allow students to take advantage of the jobs that are in demand. Of course, accepting in-state fees and providing more financial assistance will strain the paper-thin budgets of the university system, and new and expanded community college programs will require new resources to be effective, but the costs of failing to make higher education available for California residents will be even more expensive in the long run if the state doesn't take steps to address these challenges today.

Roughly two out of five unemployed Californians are 35 years old or younger. For these folks, retooling and learning a new trade is well worth the investment relative to a lifetime of higher earnings. For the 56-and-over crowd, retooling can be a more challenging prospect. However, there will always be demand for lower-skilled workers in California. Although retail, construction, and real estate are not expected to lead the economic recovery, they will begin to add jobs eventually. California specifically has a long-term need for additional housing units given that we have one of the lowest housing vacancy rates in the nation. And California's idyllic climate and treasure trove of destination spots will ensure that it continues to draw tourists from around the world, which will create increased demand for the retail, and leisure and hospitality sectors. However, if we do not address the skills mismatch, then the healing process will take that much longer and the ability of California to thrive in a knowledge-based economy will be hampered.

## FORECAST HIGHLIGHTS

The outlook for California remains positive. The media hype suggesting the onset of a second, more severe downturn is largely overblown—the state is lacking both the drivers of a new collapse and the data to show that one is coming down the pike.

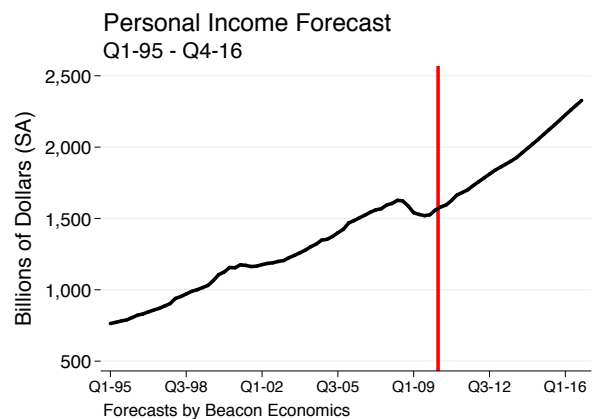
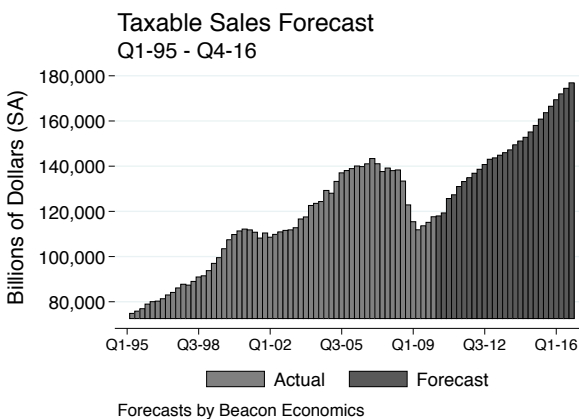
The housing market is a prime example. Despite the precipitous decline in home values when the housing bubble burst, California’s housing market is healthier today than it has been in many years. Home prices have been driven primarily by incomes in the state, averaging between six and seven times per capita income over the last several decades. It’s important to note that this ratio is skewed somewhat by the inclusion of non-homeowners, who traditionally drive the per capita income figures downward. Still, this was a relatively stable range from the mid-1970s through the turn of the century. During the housing bubble, home prices shot up to more than 12 times per capita income—a level that was clearly unsustainable. As painful as the downturn in prices has been for many Californians’ individual balance sheets, home prices have returned to a level that makes sense.



As a result, Beacon Economics is forecasting that home prices will begin to grow slowly as the year draws to a close, but that growth will be tepid at best. In 2012, we will see home price appreciation accelerate gradually, rising by between 1% and 2% on a year-over-year basis. The

affordability of homes and a slowly healing labor market will drive sales higher next year, averaging roughly 80,000 sales per quarter before climbing into the 90,000 range by late 2013.

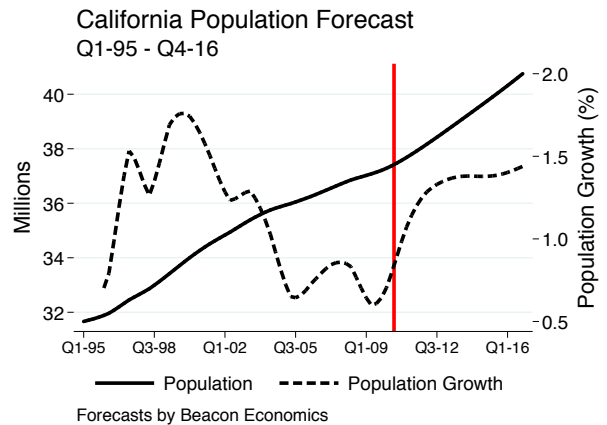
New home construction will need to wait awhile before growth begins in earnest. Yet here, too, we see reasons for optimism. Both defaults and foreclosures have been trending downward for several quarters. They remain elevated, but the market is being allowed to reabsorb these units as both rental housing and ownership housing. As this inventory is processed through the system, there will be a demand for housing in the state. According to the U.S. Census Bureau, California has one of the lowest housing vacancy rates in the nation at 5.9% for renters and 2.3% for homeowners. Thus, unlike other states, such as Florida, Nevada, and Arizona, which overbuilt during the bubble, California does not have enough housing. As these distressed properties are cycled through the system and as the economy continues to heal, new households will begin forming at a faster pace. This will lead to additional residential construction in the coming years. Beacon Economics is forecasting that the next 18 months will be slow, with the state seeing between 12,000 and 18,000 new units permitted per quarter. By 2013, California should see permitting increase, ranging from 80,000 to 90,000 per year. This will create some much-needed construction jobs in the state, but patience will be critical as the remaining problems left over by the downturn work their way through the market.



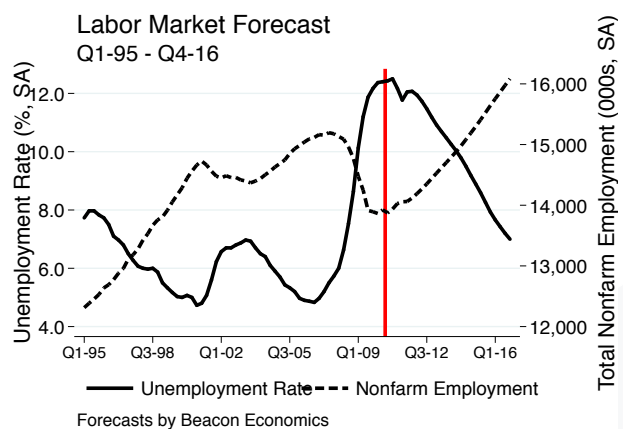
On the consumer side, the numbers will continue to improve. Income has already begun to rise and has surpassed its previous peaks after turning the corner in late 2009. On a per capita basis, incomes are improving as well. Based upon updated population figures from the 2010 census, Beacon Economics estimates that per capita income is above \$44,000. Rising incomes, combined with healthier balance sheets on the part of households, have already driven solid increases in taxable sales over the past 18 months. Through the first quarter of 2011, taxable sales had added back more than 14% of their 2009 trough, and we expect to see continued

growth through the rest of 2011. By 2013, taxable sales will exceed the previous peak and will see growth accelerate through the end of our forecast in 2016.

California's population is expected to see continued growth. Traditionally, California experiences significant downward pressure on population during times of economic turmoil as potential new residents forego a move to the state due to high levels of unemployment. Our own residents can also be attracted to neighboring states in hopes of finding better opportunities. This time around, the recession was broad based, both across sectors and across geographies. As such, the incentive to move has been moderated by the fact that labor markets in many other states are lagging—especially those of our closest neighbors in Nevada and Arizona. And, with home affordability at very high levels, due to both low home prices and relatively low interest rates on home mortgages, the timing has never been better for California to attract new residents from the rest of the U.S. and around the world. Therefore, Beacon Economics is forecasting that California will see its population continue to rise as the economy heals. We expect the state's population to increase by between 1% and 1.3% per year moving forward. This will be driven in part by new migration into the state as well as by natural increase from our existing population. By 2016, Beacon Economics forecasts that the total population in California will breach the 40 million mark for the first time.



Unfortunately, the speed of the labor market recovery will continue to disappoint. There's no doubt that the recovery is underway: we see it in the leading indicators of employment, from unemployment insurance claims to weekly hours to employment itself, which is up by more than 225,000 since hitting bottom. However, the pace of the jobs recovery will be slow. Part of this is due to gains in productivity and efficiency; employers are currently in a mode of maximizing returns on their existing workforce. Yet, an even bigger



issue is the skills mismatch that is stifling job growth in the state. Eventually productivity growth will slow, which will give rise to new positions, but the more difficult task will be placing relatively less-educated workers into jobs in growing industries because they simply don't have the requisite skill set. Indeed, employers are hiring, as evidenced by the job growth we have seen over the past 10 months, but the jobs have been concentrated in the highly skilled industries.

Therefore, Beacon Economics is forecasting that the labor market will continue to improve, but the pace of the recovery will be slow. The rest of 2011 will leave something to be desired, with employment growth averaging 1.5%. There will be a slight acceleration in job growth to nearly 2%. The labor market will continue to gain steam in 2013, and we expect it to surpass its previous peak of more than 15 million jobs by 2014. The unemployment rate will begin to come down gradually as well. Although it is expected to remain in the double digits through the end of 2012, the unemployment rate should drop into the 9% range by 2013. Still, it will be several years before the state gets back to "normal" levels of unemployment, and that could be a relatively higher baseline of 7% if we cannot find a way to address some of the structural problems with our workforce.