

**BOARD MEMBERS**

Betty T. Yee
Acting Member
San Francisco
First District
415-557-3000

Bill Leonard
Sacramento/Ontario
Second District
916-445-2181

Claude Parrish
Long Beach
Third District
562-983-7855

John Chiang
Los Angeles
Fourth District
213-239-8506

Steve Westly
Sacramento
State Controller
916-445-2636



Ramon J. Hirsig
Executive Director

❖ U.S. Economic Developments

Job Creation Following Consensus Forecast in Early 2005

In the first quarter of 2005, U.S. nonagricultural payroll employment increased 1.7 percent compared to the first quarter of 2004. This percentage gain is close to the average from a survey of 36 professional forecasters polled by the Federal Reserve Bank of Philadelphia in February, which called for a 1.6 percent gain for all of 2005. Therefore, it appears that employment growth so far in 2005 is closely following this consensus forecast.

Better Than Average Growth Expected

The consensus forecast by these economists is for real gross domestic product (GDP) to increase 3.6 percent in 2005 and 3.4 percent in 2006. If these forecasts prove accurate, growth this year and next would be above the 10-year annual average of 3.3 percent. Preliminary estimates released by the U.S. Department of Commerce show that real GDP increased 3.1 percent in the first quarter of 2005.

Moderate Overall Inflation in 2004 Despite Soaring Energy Costs

The U.S. consumer price index rose 2.7 percent in 2004, up from 2.3 percent in 2003. Soaring energy costs were largely responsible for the higher inflation rate in 2004. The average price of gasoline increased 18.2 percent for consumers in 2004. However, despite the increase in energy prices, the overall Consumer Price Index increase of 2.7 percent was close to the ten-year average increase of 2.5 percent per year.

Rising Energy Prices May Impact Economic Growth

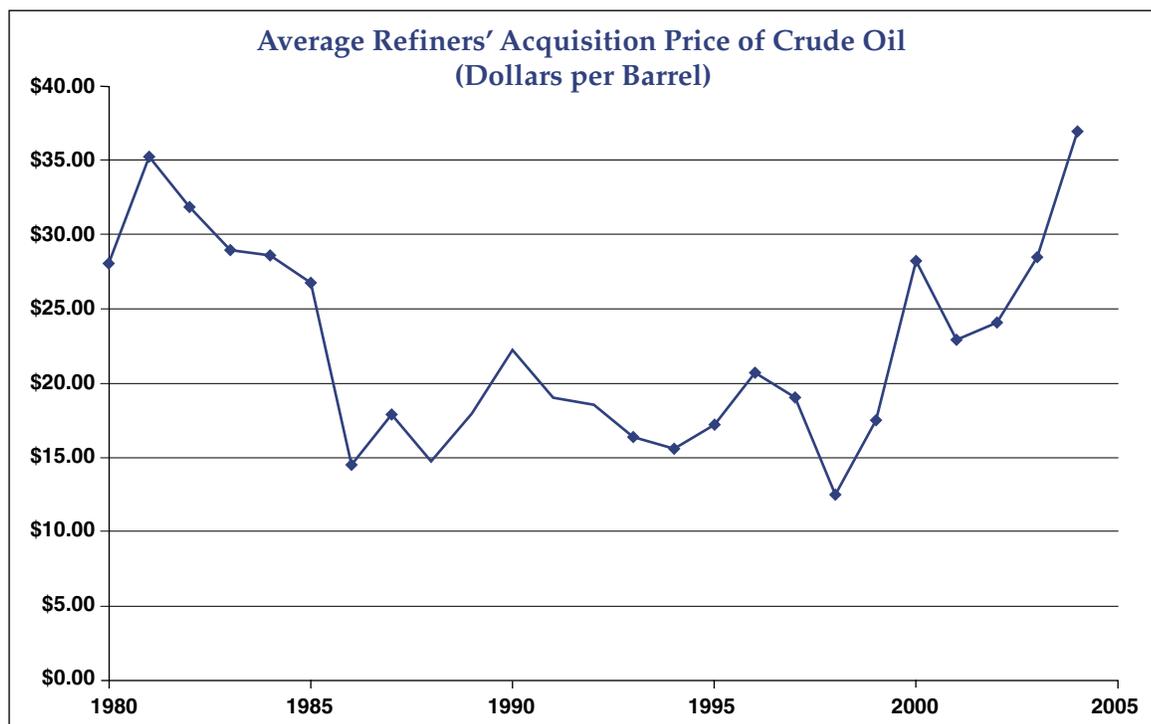
As shown in the chart on the next page, in 2004 the average refiners' acquisition price for crude oil surged 30 percent over that of 2003 and was above the 1981 average price for the first time ever (prices unadjusted for inflation). Despite the sharp increase in oil prices, real GDP increased 4.4 percent in 2004, well above the ten-year average of 3.3 percent per year. It is estimated that higher energy prices reduced U.S. real GDP by 0.75 percent in 2004.

One negative news development since the Philadelphia Federal Reserve survey (referred to earlier) release is that energy costs have once again jumped. In the first two months of 2005, the average refiners' acquisition price for crude oil increased about 30 percent above its average for the first two months of 2004. The U.S. Energy Information Agency's April 2005 forecast calls for an increase of 32 percent for crude oil prices (West Texas Intermediate Crude Oil, another oil price benchmark) in 2005. If this forecast is accurate, higher energy prices could reduce economic growth in 2005. Higher energy prices would also raise the overall inflation rate, likely in proportion to their impacts in 2004.

❖ California Economic Developments

California Employment Growth Tracking Consensus Forecast in Early 2005

In the first quarter of 2005, nonagricultural employment increased 1.7 percent compared to the first quarter of 2004. As with the U.S., California growth in employment



is tracking a commonly cited consensus growth forecast in early 2005. The April 2005 Western Blue Chip Economic Forecast, a consensus California forecast, calls for California nonagricultural employment to rise 1.8 percent in 2005.

Construction Strong in 2004

A total of 212,000 residential building permits were issued in 2004, well above the ten-year average of 143,000 units. More residential building permits were obtained in 2004 than in any other year since 1989. However with rising interest rates, many economists are forecasting a decline in home permits in 2005. The California Construction Industry Research Board predicts that 202,000 residential home permits will be issued this year, down 4.6 percent from 2004.

Nonresidential construction activity also rose last year. After three years of declines, the inflation-adjusted total value of private nonresidential construction rose 5.8 percent in 2004. Unlike home construc-

tion, the California Construction Industry Research Board forecasts expanding activity, a 7.1 percent predicted increase in the 2005 value of nonresidential permits after adjusting for inflation. A strong economy (and its associated increasing demand for office space and other building activities) and high corporate profits are likely major factors behind the predicted increase.

Continued Taxable Sales Growth in Fourth Quarter

Based on preliminary data, the Board of Equalization estimates an increase of 7.0 percent in California taxable sales for the fourth quarter of 2004 compared to taxable sales in the fourth quarter of 2003. For all of 2004, taxable sales have increased 7.3 percent based on preliminary data for the final two quarters of the year. This is much stronger than the 4.3 percent increase for all of 2003. The 2005-06 Governor's Budget forecasts taxable sales to increase 5.7 percent in 2005, implying a slowdown from the fourth quarter.

❖ In-Depth Perspective: The Changing Wireless Telecommunications Industry

The Board administers the state-assessed property program and sets market values for public utilities and railroads as defined by the State Constitution. These values are allocated to local jurisdictions for levy and collection of local property taxes.

The wireless telecommunications industry is one of the public utilities valued by the Board. With rapid adoption of technology by consumers, wireless communications has quickly become a very important industry. Industry trends have had major impacts not only for the wireless industry itself, but also for the wired telecommunications industry, which provides close substitute services. The wireless telecommunications industry accounted for about 9 percent of the value of state-assessed utilities and railroad properties in fiscal year 2004-05, while the wired telecommunications industry accounted for about 27 percent.

Wireless Subscriptions Increase as Real Prices Decrease

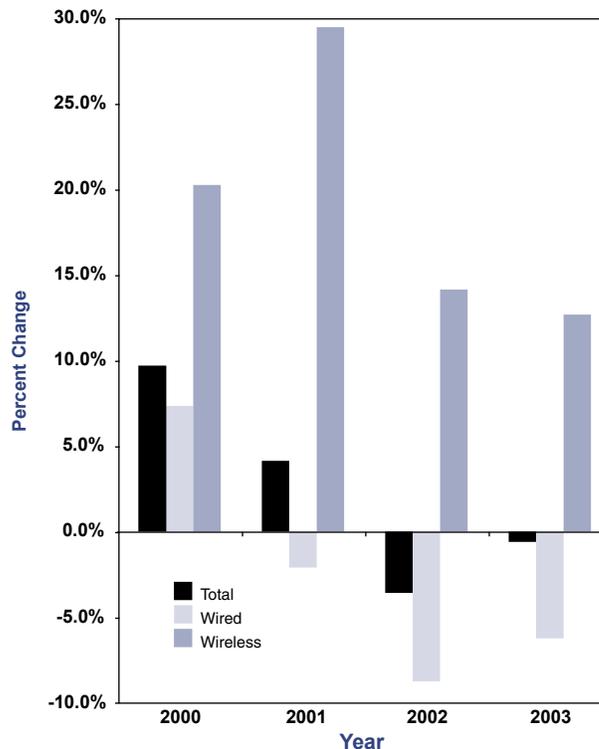
An industry trade association recently reported that more than 60 percent of U.S. households were wireless telephone subscribers in December 2004, more than twice as many households as in 1999. Falling prices have been largely responsible for the increasing popularity of wireless phones. According to the Federal Communications Commission, the real price of a wireless minute has fallen by 81 percent for the ten-year period ending in 2004.

Wireless Revenues Growing While Wired Revenues Declining

U.S. Census Bureau data show that revenues for cellular service providers nearly tripled from 1998 to 2003. A large part of wireless revenue growth has come at the expense of wired phone services. In 1998, wired services accounted for 80 percent of total U.S. telecommunications revenues and wireless services accounted for 15 percent. By 2003, the wired market share had dropped to 64 percent and the wireless share had risen to 31 percent. From 1998 to 2003, revenues for U.S. cellular telecommunications providers increased from \$35.2 billion to \$104.2 billion. Over the same time period, revenues for U.S. wired telecommunications providers declined from \$227.9 billion to \$222.6 billion.

While revenues for wireless telecommunications companies have increased,

Revenues, 1999 to 2003 Annual Percent Changes in Total, Wireless, and Wired Telecommunications Industry Revenues 1999 to 2003



revenues for wired telecommunications companies have declined over the past several years (see chart page 3). In 2003, the most recent year for which these data are available, total U.S. telecommunications revenues were essentially flat, declining by 0.6 percent. However, wired and wireless revenue trends moved in opposite directions in 2003. Revenues from wired services declined 6.2 percent, and revenues from wireless services increased 12.7 percent.

Other industry association data indicate that these trends continued in 2004 with few signs of changing significantly. The implication of these trends is that valuations of the wireless services companies have become a much larger share of total state-assessed valuations than they were just a few years ago while the wired services companies' share has declined.

Contact Us

Please contact us if you would like to be added to our mailing list, need additional copies, or have any questions or comments.

Joe Fitz, Chief Economist
State Board of Equalization, MIC:67
P. O. Box 942879
Sacramento, CA 94279-0067
916-323-3802
jfitz@boe.ca.gov

Current and past issues of this publication are on the Board's website:
www.boe.ca.gov/news/epcont.htm.

Taxpayers' Rights Advocate:
888-324-2798

Online Resources

For more information about topics covered in this issue, please visit any of the websites listed below. Some sites charge a fee to use their services.

California Board of Equalization News Release,
2004 Taxable Sales – Fourth Quarter
(forthcoming)
www.boe.ca.gov

California Department of Finance
www.dof.ca.gov

California Employment Development Department (EDD),
Labor Market Conditions in California,
April 15, 2005 Construction Industry Research Board
www.cirbdata.com

CITA – The Wireless Association
www.ctia.org/

Federal Reserve Bank of Philadelphia,
Survey of Professional Forecasters,
February 14, 2005
www.phil.frb.org/econ/spf/index.html

National Association for Business Economists
www.nabe.com

U.S. Bureau of Economic Analysis,
Survey of Current Business
www.bea.doc.gov/bea/pubs.htm

U.S. Bureau of Labor Statistics
www.bls.gov

U.S. Census Bureau,
Service Annual Survey
www.census.gov

U.S. Department of Commerce,
STAT-USA U.S. Energy Information Administration
www.eia.doe.gov

Western Blue Chip Economic Forecast,
Bank One Economic Outlook Center, Arizona State University