



# CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

June 10, 2013

The Honorable City Council  
Palo Alto, California

## City of Palo Alto Sales Tax Digest Summary Fourth Quarter Sales (October - December 2012)

This is an informational report, and no action is required.

### BACKGROUND

Sales and use tax represents about 15 percent, or \$22.5 million, of projected General Fund revenue in the City's Adopted Operating Budget for fiscal year 2013. According to the Midyear Financial Report, projected sales and use tax revenue has increased and is now estimated at \$23.4 million for fiscal year 2013. This revenue includes sales and use tax for the City of Palo Alto and pool allocations<sup>1</sup> from the State and Santa Clara County.

The City Auditor's Office contracts with MuniServices LLC (hereafter MuniServices), the City's sales and use tax consultant, to provide sales and use tax recovery services and informational reports. The City Auditor's Office uses the recovery services and informational reports to help identify misallocation of tax revenue owed to the City, and to follow up with the State Board of Equalization to ensure the City receives identified revenues. The City Auditor's Office includes information on sales and use tax recoveries in our quarterly reports to the Policy and Services Committee.

The City Auditor's Office also shares the information provided by MuniServices with the Administrative Services Department (ASD) for use in revenue forecasting and budgeting, and Economic Development for business outreach strategies. We coordinated this informational memo with them.

### DISCUSSION

The attached report (Attachment A) was prepared by MuniServices and covers calendar year fourth quarter sales (October through December 2012). These funds are reported as part of the City's fiscal year 2013 revenue. Due to the timing of reporting by businesses and the State, MuniServices' detailed reports on first quarter sales (January through March 2013) should be available by August 2013. ASD advises that in mid-June, it should receive information from the State on aggregate sales and use tax receipts for first quarter 2013.

<sup>1</sup> See definitions on page 4.

Following are some highlights of the sales and use tax information we received:

- In Palo Alto, overall sales and use tax revenue (cash receipts) for the fourth quarter ending December 2012 increased by approximately \$1.9 million, or 32.8 percent, (including pool allocations) compared to the fourth quarter ending December 2011.<sup>2</sup> For all jurisdictions in Santa Clara County, sales and use tax revenue for the fourth quarter ending December 2012 increased by \$8.4 million, or 9.4 percent, compared to the fourth quarter ending December 2011.
- Statewide, every region in California experienced an increase in sales and use tax revenue for the year ending December 2012, compared to the prior year ending December 2011. Statewide sales and use tax revenue has shown growth of 3.5 percent during the fourth quarter ending December 2012 compared to the fourth quarter ending December 2011.
- In Palo Alto, sales and use tax revenue totaled \$23.7 million for the year ending December 2012, an increase of 12.4 percent from \$21.1 million in the prior year ending December 2011.<sup>2</sup> This amount includes sales and use tax for the City of Palo Alto and pool allocations from the State and Santa Clara County.

More detailed information is shown on Attachment A.

### **Economic Influences on Sales and Use Tax**

In its Economic Overview (Attachment B), MuniServices discusses economic influences including national economic trends, holiday and retail sales, auto sales, and state forecast information that may affect the City's sales and use tax revenue.

Preliminary estimates from the State of California Employment Development Department show the March 2013 unemployment rate in Santa Clara County at 7.1 percent and Palo Alto at 3.8 percent.

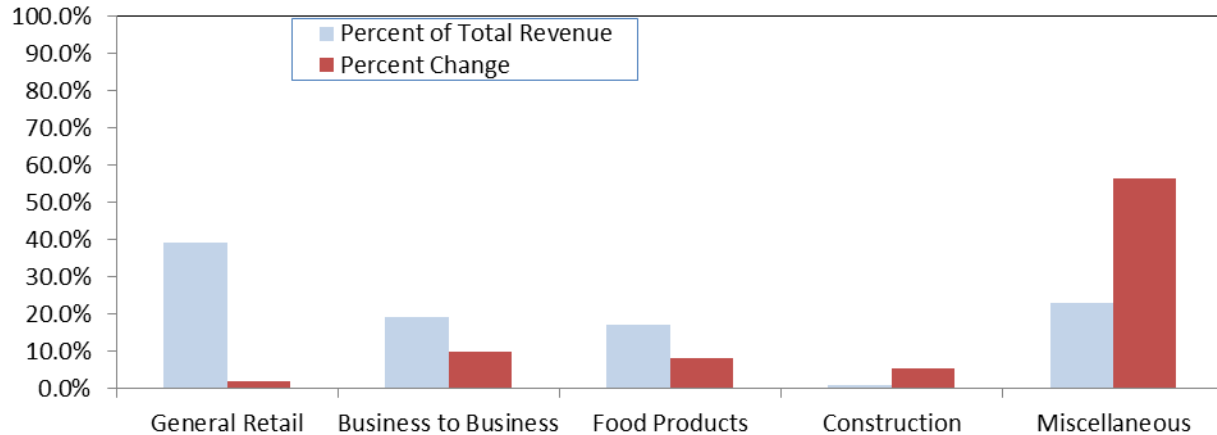
### **Economic Category Analysis**

MuniServices' analysis of economic categories, for the year ending December 2012, shows that General Retail comprised the largest percentage of Palo Alto's sales and use tax revenue and experienced 2.0 percent growth. Business to Business experienced a 9.9 percent increase and comprised 19.4 percent of total revenues. Food Products experienced an 8.2 percent increase and comprised 17.1 percent of total revenues.

<sup>2</sup> Excluding pool allocations and adjusting for prior period and late payments, Palo Alto's sales and use tax revenue for the fourth quarter ending December 2012 increased by 25.5 percent compared to the fourth quarter ending December 2011. On a yearly basis, Palo Alto's sales

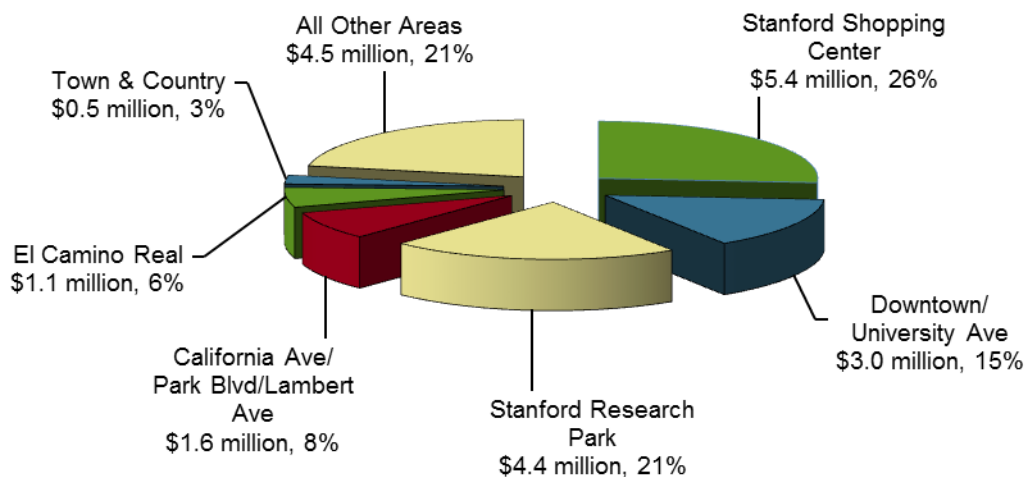
and use tax revenue for the year ending December 2012, increased by 13.9 percent compared to the prior year ending December 2011.

**Exhibit 1 - Comparison of Palo Alto's Sales and Use Tax Revenue and Percent Change by Economic Category for the Year Ending December 2012**



The following chart shows sales and use tax revenue by geographical area based on information provided by MuniServices.

**Exhibit 2 – Palo Alto's Sales and Use Tax Revenue by Geographical Area  
For the Year Ending December 2012  
(Amounts include tax estimates and exclude pool allocations)**



## DEFINITIONS

In California, either sales tax or use tax may apply to a transaction, but not both. The sales and use tax rate in Palo Alto during the fourth quarter 2012 was 8.375 percent, and the City should receive 1 percent of every taxable transaction. Effective April 1, 2013, the sales and use tax rate in Palo Alto increased to 8.75 percent.

**Sales tax** – imposed on all California retailers; applies to all retail sales of merchandise (tangible personal property) in the state.

**Use tax** – generally imposed on: consumers of merchandise (tangible personal property) that is used, consumed, or stored in this state; purchases from out-of-state retailers when the out-of-state retailer is not registered to collect California tax, or for some other reason does not collect California tax; leases of merchandise (tangible personal property).

**Countywide/statewide pools** – mechanisms used to allocate local tax that cannot be identified with a specific place of sale or use in California. Local tax reported to the pool is distributed to the local jurisdiction each calendar quarter using a formula that relates to the direct allocation of local tax to each jurisdiction for a given period.

Examples of taxpayers who report use tax allocated through the countywide pool include construction contractors who are consumers of materials used in the improvement of real property and whose job site is regarded as the place of business, out-of-state sellers who ship goods directly to consumers in the state from inventory located outside the state, and California sellers who ship goods directly to consumers in the state from inventory located outside the state.

Other examples of taxpayers who report use tax through the pools include auctioneers, construction contractors making sales of fixtures, catering trucks, itinerant vendors, vending machine operators and other permit holders who operate in more than one local jurisdiction, but are unable to readily identify the particular jurisdiction where the taxable transaction takes place.

Respectfully submitted,



Jim Pelletier  
City Auditor

Sources: MuniServices; California State Board of Equalization; State of California Employment Development Department; City of Palo Alto's Adopted Operating Budget Fiscal Year 2013

Audit staff: Lisa Wehara

**ATTACHMENTS:**

- Attachment A: City of Palo Alto Sales Tax Digest Summary (PDF)
- Attachment B: Economic Overview April 2013 (PDF)

Department Head: Jim Pelletier, City Auditor





# City of Palo Alto

## Sales Tax Digest Summary

### Collections through March 2012

### Sales through December 2012 (2012Q4)

Attachment A

#### California Overview

The percent change in cash receipts from the prior year was 6.8% statewide, 6.9% in Northern California and 6.7% in Southern California. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments. When we adjust for non-period related payments, we determine the overall business activity increased for the year ended 4th Quarter 2012 by 6.3% statewide, 6.5% in Northern California and increased by 5.6% in Southern California.

#### City of Palo Alto

For the year ended 4th Quarter 2012, sales tax cash receipts for the City grew by 12.4% from the prior year. On a quarterly basis, sales tax revenues grew by 32.8% from 4th Quarter 2011 to 4th Quarter 2012. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments.

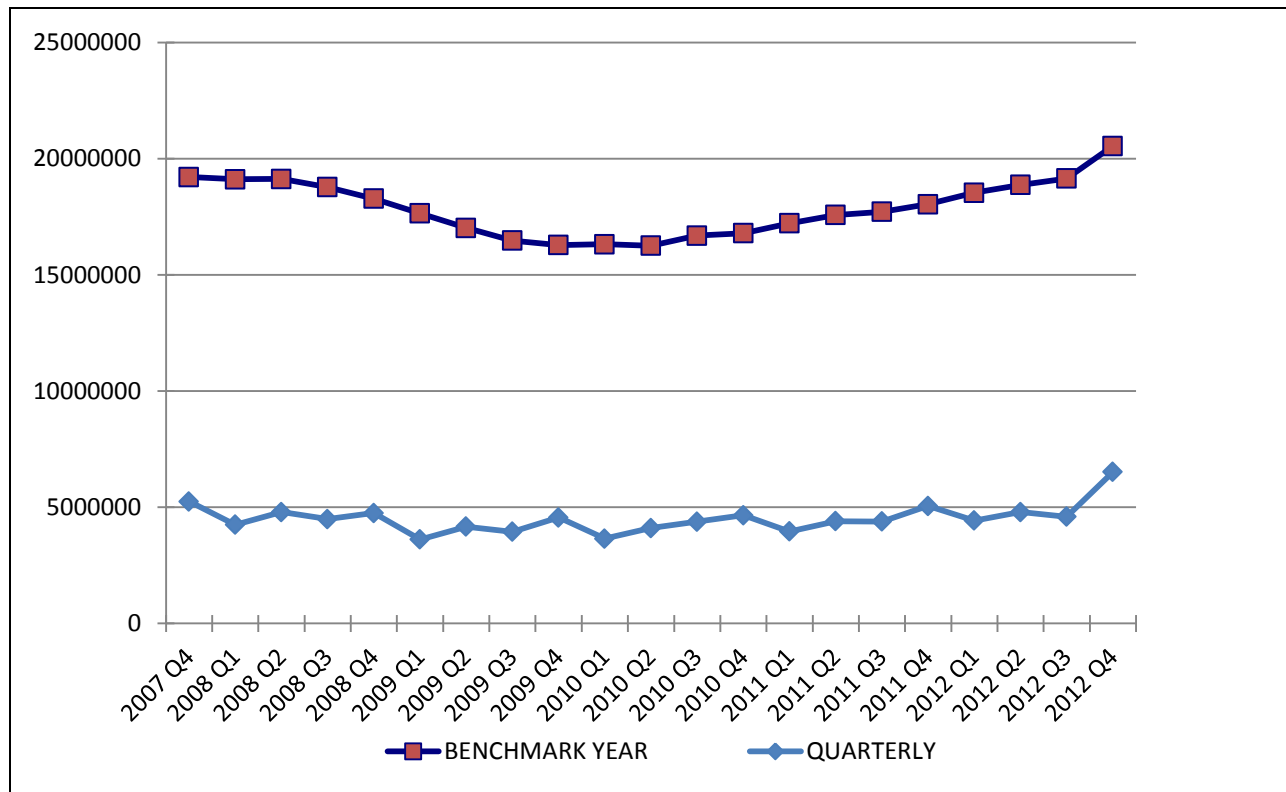
Excluding state and county pools and adjusting for anomalies (payments for prior periods) and late payments, local sales tax increased by 13.9% for the year ended 4th Quarter 2012 from the prior year. On a quarterly basis, sales tax activity grew by 25.5% in 4th Quarter 2012 compared to 4th Quarter 2011.

#### Regional Overview

This seven-region comparison includes estimated payments and excludes net pools and adjustments.

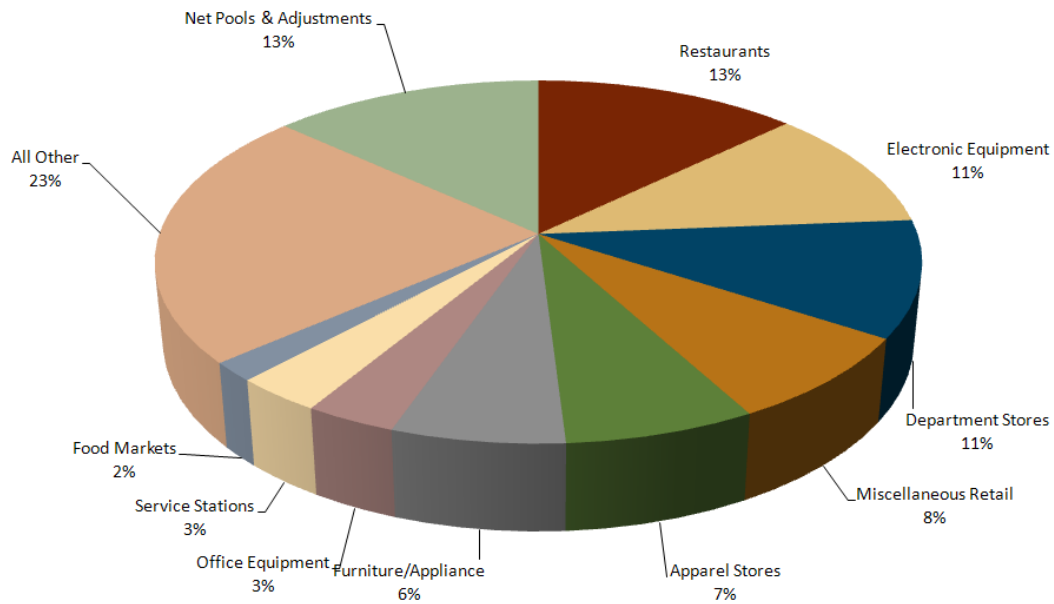
ECONOMIC CATEGORY ANALYSIS FOR YEAR ENDED 4th QUARTER 2012									
% of Total / % Change	City of Palo Alto	California Statewide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	Inland Empire	North Coast	Central Coast
General Retail	39.3 / 2.0	28.8 / 4.0	28 / 4.3	29.3 / 3.0	30.8 / 4.1	29.1 / 3.7	27.2 / 5.6	28.8 / 2.2	32.4 / 3.7
Food Products	17.1 / 8.2	19.2 / 6.6	19.9 / 7.4	16.7 / 3.8	16.1 / 4.1	19.9 / 6.7	16.7 / 8.9	18 / 4.0	31.7 / 7.0
Construction	1.0 / 5.5	8.6 / 6.9	8.4 / 6.7	9.9 / 1.2	10.7 / 7.9	7.8 / 5.3	10.9 / 19.9	11.8 / 4.1	8.4 / 0.4
Business to Business	19.4 / 9.9	17.4 / 5.5	20.7 / 5.7	14.3 / 5.6	14.1 / 9.3	17.2 / 4.4	15.2 / 9.3	8.9 / -0.4	5.5 / 5.2
Miscellaneous/Other	23.2 / 56.5	26 / 9.2	23 / 11.4	29.9 / 11.5	28.3 / 10.6	26 / 7.8	30.1 / 9.2	32.5 / 9.8	22 / 2.0
<b>Total</b>	<b>100.0 / 13.9</b>	<b>100 / 6.3</b>	<b>100 / 7.0</b>	<b>100 / 5.6</b>	<b>100 / 7.0</b>	<b>100 / 5.6</b>	<b>100 / 9.2</b>	<b>100 / 4.9</b>	<b>100 / 4.1</b>
ECONOMIC SEGMENT ANALYSIS FOR YEAR ENDED 4th QUARTER 2012									
	City of Palo Alto	California Statewide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	Inland Empire	North Coast	Central Coast
Largest Segment	***	Restaurants	Restaurants	Department Stores	Department Stores	Restaurants	Service Stations	Service Stations	Restaurants
% of Total / % Change	*** / ***	13.1 / 6.5	13.7 / 7.7	12.2 / 3.0	14.3 / 3.6	14.1 / 6.2	12.2 / 3.7	15.1 / 6.8	20.7 / 8.5
2nd Largest Segment	Restaurants	Service Stations	Auto Sales - New	Auto Sales - New	Service Stations	Service Stations	Auto Sales - New	Department Stores	Service Stations
% of Total / % Change	14.9 / 8.8	10.5 / 3.4	9.1 / 21.3	11.1 / 22.9	12.3 / 4.0	10.5 / 2.2	18.7 / 18.7	11.9 / 0.1	9.8 / 8.9
3rd Largest Segment	Electronic Equipment	Department Stores	Service Stations	Service Stations	Restaurants	Department Stores	Department Stores	Restaurants	Misc. Retail
% of Total / % Change	12.5 / 24.8	10.4 / 3.7	9.1 / 5.4	10.8 / 4.9	9.6 / 5.4	10.2 / 3.6	4.5 / 4.5	9.6 / 4.0	9.7 / 0.1
	*** Not specified to maintain confidentiality of tax information								

Gross Historical Sales Tax Performance by Benchmark Year and Quarter (Before Adjustments)



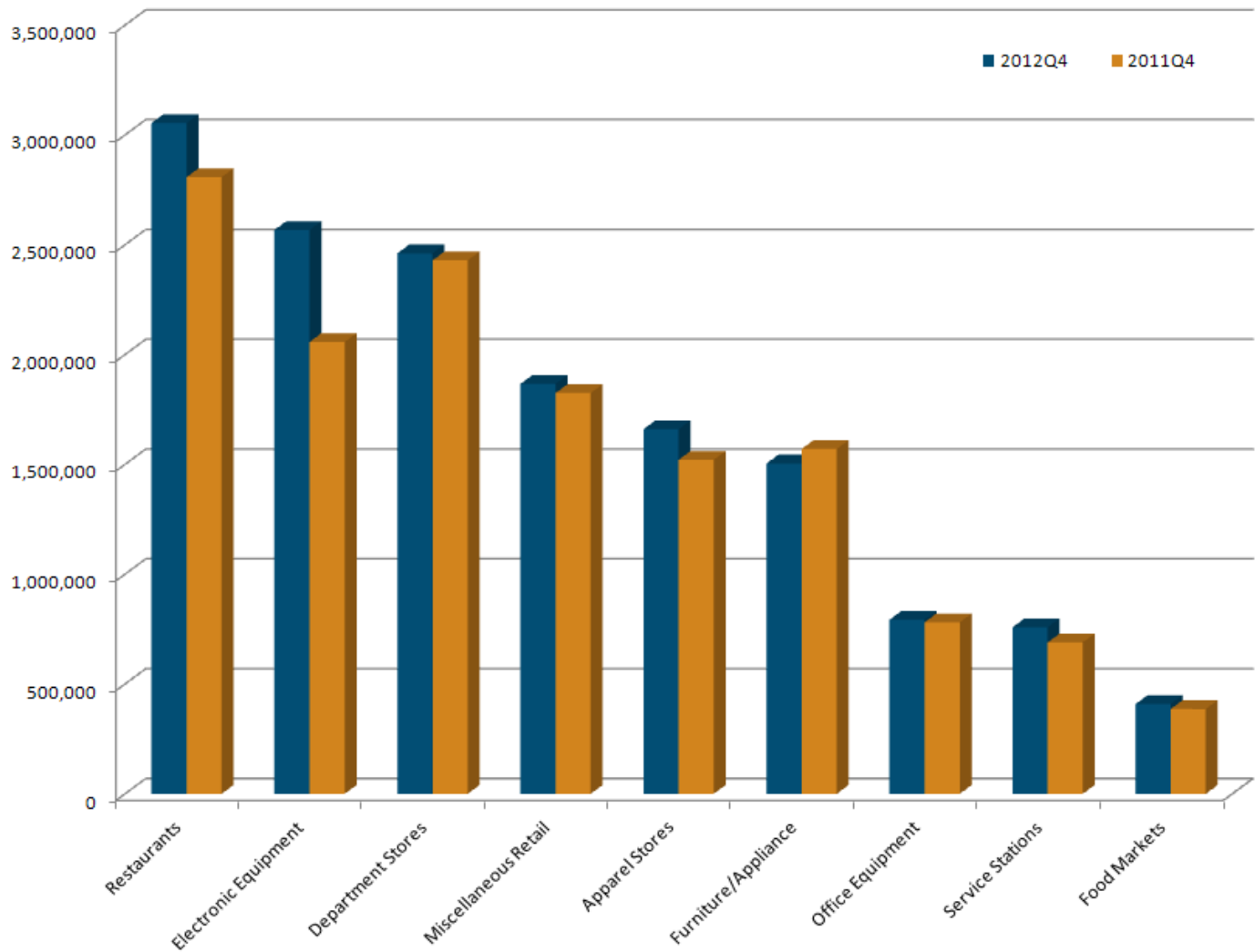
Net Cash Receipts for Benchmark Year 4th Quarter 2012: \$23,682,418

\*Benchmark year (BMV) is the sum of the current and 3 previous quarters (2012Q4 BMV is sum of 2012 Q4, Q3, Q2, & Q1)





## Sales Tax from Largest Non-confidential Economic Segments



Historical Analysis by Calendar Quarter

Economic Category	%	2012Q4	2012Q3	2012Q2	2012Q1	2011Q4	2011Q3	2011Q2	2011Q1	2010Q4
General Retail	31.9%	2,444,528	1,913,125	2,009,452	1,701,757	2,440,953	1,886,520	1,984,860	1,573,474	2,275,627
Business To Business	14.3%	1,101,068	843,770	993,147	1,064,996	932,723	842,771	842,709	925,263	887,037
Food Products	11.8%	905,156	877,520	886,852	816,336	838,138	799,167	806,987	740,594	769,253
Miscellaneous/Other	26.1%	2,004,507	905,479	848,911	797,436	781,336	812,130	720,550	680,987	665,286
Construction	0.8%	62,618	53,420	50,544	47,432	62,282	46,843	44,589	38,765	54,645
Net Pools & Adjustme	15.1%	1,155,841	603,635	840,789	754,099	725,000	933,424	845,214	769,789	508,973
Total	100.0%	7,673,718	5,196,949	5,629,695	5,182,056	5,780,432	5,320,855	5,244,909	4,728,872	5,160,821
Economic Segments	%	2012Q4	2012Q3	2012Q2	2012Q1	2011Q4	2011Q3	2011Q2	2011Q1	2010Q4
Restaurants	10.2%	782,184	760,929	780,314	714,487	783,595	689,568	705,459	639,353	651,614
Electronic Equipment	9.1%	695,663	516,554	651,686	488,132	724,274	563,373	608,784	474,566	748,885
Department Stores	10.2%	779,973	584,178	608,894	382,336	573,750	455,335	482,723	399,243	584,895
Miscellaneous Retail	7.6%	584,169	429,989	456,771	347,112	488,492	385,236	392,126	301,427	421,877
Apparel Stores	6.5%	496,073	383,337	402,471	178,409	171,472	160,037	181,065	158,421	147,520
Furniture/Appliance	5.8%	444,725	345,043	365,585	99,210	104,348	104,234	105,507	100,241	146,732
Service Stations	2.4%	182,060	198,973	198,604	90,636	101,023	98,054	89,530	91,274	105,573
Office Equipment	2.9%	223,538	162,015	188,369	46,718	48,340	49,977	51,743	47,157	43,537
Food Markets	1.4%	110,625	106,652	95,807	37,116	38,854	42,654	35,131	34,857	36,962
Health & Government	1.2%	88,669	94,969	92,612	31,168	44,402	41,338	38,236	34,016	48,591
Recreation Products	0.8%	57,916	92,186	82,846	11,199	12,838	11,321	11,319	9,967	12,060
Business Services	1.0%	73,619	69,722	71,828	6,634	9,046	9,857	8,724	6,458	8,714
Drug Stores	0.9%	65,440	62,624	65,943	7,110	22,227	8,349	8,029	3,833	3,580
Misc. Vehicle Sales	0.6%	45,656	45,325	57,680	16,264	17,880	5,505	6,353	4,749	6,054
All Other	24.6%	1,887,567	740,818	669,496	1,971,426	1,914,891	1,762,593	1,674,966	1,653,521	1,685,254
Net Pools & Adjustme	15.1%	1,155,841	603,635	840,789	754,099	725,000	933,424	845,214	769,789	508,973
Total	100.0%	7,673,718	5,196,949	5,629,695	5,182,056	5,780,432	5,320,855	5,244,909	4,728,872	5,160,821

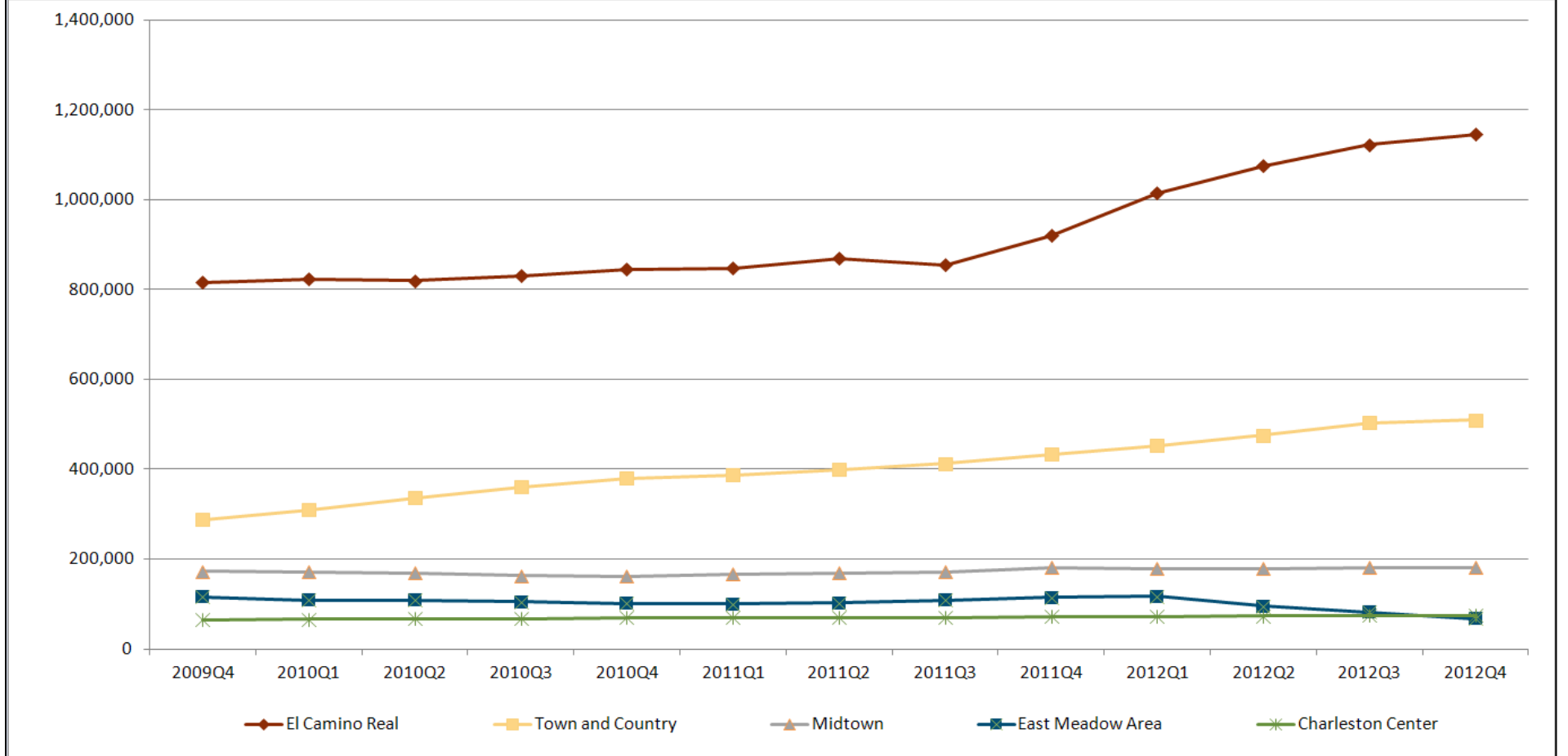
\*Net Pools & Adjustments reconcile economic performance to periods' net cash receipts. The historical amounts by calendar quarter: (1) include any prior period adjustments and payments in the appropriate category/segment and (2) exclude businesses no longer active in the current period.

## Quarterly Analysis by Economic Category, Total and Segments: Change from 2011Q4 to 2012Q4

	General Retail	Food Products	Construction	Business to Business	Misc/Other	2012/4 Total	2011/4 Total	% Chg	Largest Gain	Second Largest Gain	Largest Decline	Second Largest Decline
Campbell	-2.3%	5.1%	1.9%	16.9%	5.2%	2,205,865	2,123,834	3.9%	Business Services	Restaurants	Furniture/Appliance	Leasing
Cupertino	-3.2%	9.5%	12.0%	19.4%	2.6%	6,782,039	5,873,395	15.5%	Business Services	Electronic Equipment	Department Stores	Miscellaneous Retail
Gilroy	-2.1%	-1.1%	4.7%	10.6%	1.8%	3,224,932	3,222,702	0.1%	Auto Sales - New	Department Stores	Apparel Stores	Service Stations
Los Altos	-16.5%	5.5%	-9.1%	-6.9%	-1.8%	529,925	552,843	-4.1%	Restaurants	Food Markets	Florist/Nursery	Furniture/Appliance
Los Gatos	-33.7%	5.4%	15.6%	-0.9%	-13.0%	1,818,853	2,284,306	-20.4%	Restaurants	Electronic Equipment	Miscellaneous Retail	Auto Sales - New
Milpitas	4.3%	3.1%	17.6%	5.3%	4.1%	4,442,420	4,225,020	5.1%	Electronic Equipment	Bldg.Matls-Whsle	Light Industry	Department Stores
Morgan Hill	11.1%	9.0%	-2.2%	51.1%	30.3%	1,776,921	1,449,447	22.6%	Electronic Equipment	Auto Sales - New	Light Industry	Auto Sales - Used
Mountain View	2.0%	3.6%	-7.7%	4.5%	8.1%	3,619,785	3,486,650	3.8%	Office Equipment	Service Stations	Business Services	Electronic Equipment
Palo Alto	-0.3%	5.1%	-4.1%	11.2%	142.6%	6,517,877	5,194,296	25.5%	***	Electronic Equipment	Business Services	Furniture/Appliance
San Jose	4.4%	3.1%	8.9%	0.8%	5.5%	34,810,776	33,447,806	4.1%	Auto Sales - New	Miscellaneous Retail	Electronic Equipment	Chemical Products
Santa Clara	6.4%	3.6%	27.8%	20.8%	4.8%	9,857,943	8,738,106	12.8%	Leasing	Bldg.Matls-Whsle	Health & Government	Bldg.Matls-Retail
Santa Clara Co.	-50.7%	-2.2%	5.2%	-30.9%	-15.6%	946,416	1,248,080	-24.2%	Light Industry	Apparel Stores	Miscellaneous Retail	Heavy Industry
Saratoga	31.5%	-1.9%	-86.8%	-22.5%	-3.0%	237,045	237,642	-0.3%	Furniture/Appliance	Miscellaneous Retail	Bldg.Matls-Retail	Restaurants
Sunnyvale	1.2%	2.5%	3.2%	1.8%	3.0%	6,833,061	6,692,686	2.1%	Office Equipment	Department Stores	Light Industry	Furniture/Appliance

\*\*\* Not specified to maintain confidentiality of tax information

City of Palo Alto - Selected Geographic Areas of the City													
Benchmark Year 4th Quarter 2012													
	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4
El Camino Real	814,940	822,245	818,947	830,152	843,626	846,897	867,868	854,828	920,020	1,014,867	1,074,079	1,122,001	1,143,951
Town and Country	288,103	309,848	336,444	360,254	379,066	386,944	399,378	412,361	433,313	451,982	475,054	502,127	509,180
Midtown	172,297	170,517	169,297	162,869	162,122	166,440	168,537	171,719	180,415	178,344	179,250	181,352	181,654
East Meadow Area	116,128	107,931	108,922	104,777	100,155	100,032	102,028	108,176	114,083	116,558	94,868	81,598	67,124
Charleston Center	64,981	65,642	66,446	67,447	68,693	69,150	69,606	70,301	71,555	72,602	73,408	74,213	74,683

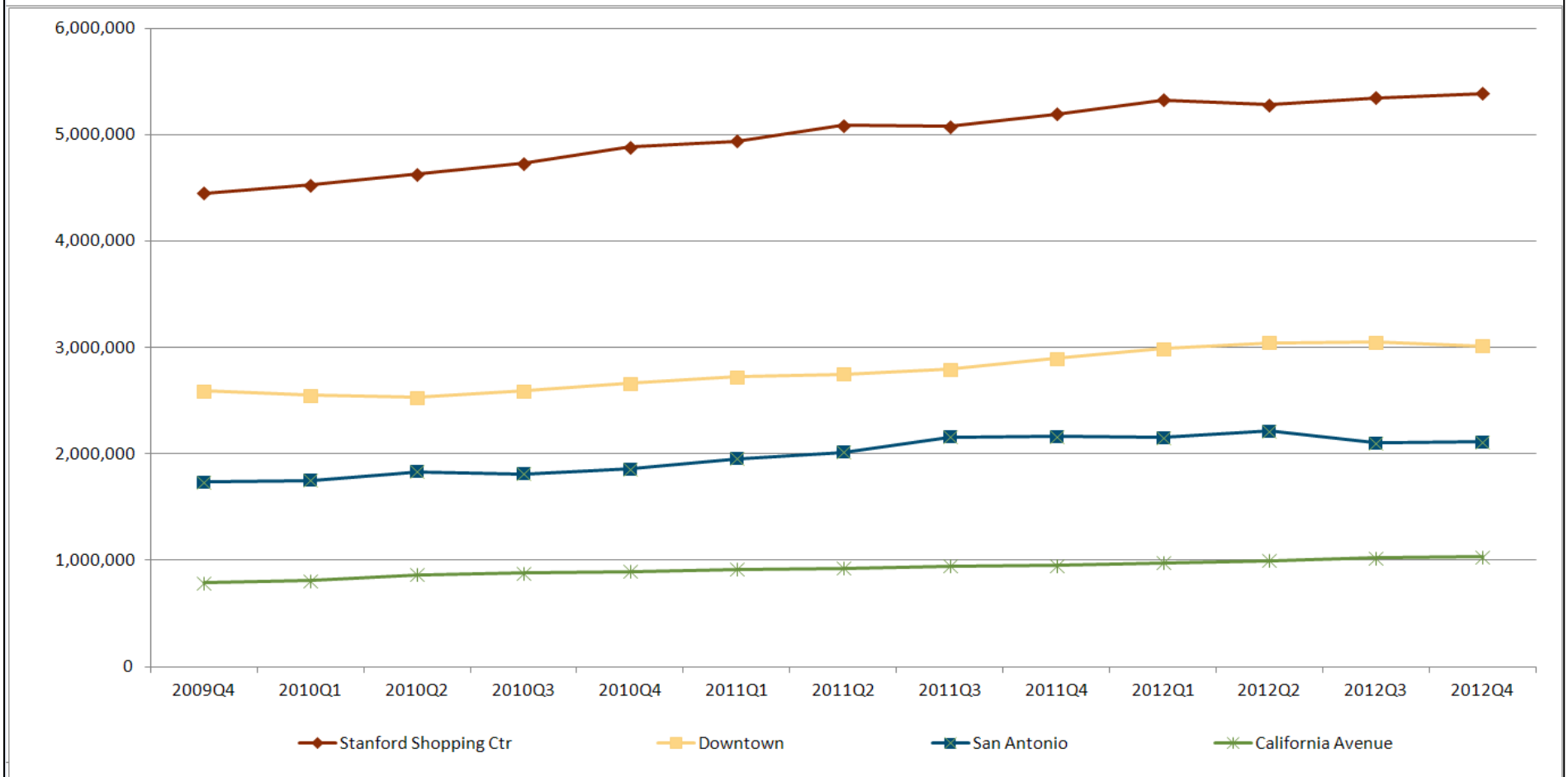


\*Benchmark year (BM) is the sum of the current and 3 previous quarters (2012Q4 BM is sum of 2012 Q4, Q3, Q2, & Q1)

## City of Palo Alto - Selected Geographic Areas of the City

Benchmark Year 4th Quarter 2012

	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4
Stanford Shopping Ctr	4,451,986	4,524,318	4,631,095	4,731,800	4,884,843	4,941,127	5,087,834	5,079,526	5,194,491	5,325,435	5,281,772	5,345,618	5,388,747
Downtown	2,591,213	2,549,106	2,528,095	2,589,660	2,663,500	2,723,552	2,748,925	2,793,987	2,897,003	2,986,093	3,044,755	3,047,356	3,013,183
San Antonio	1,737,780	1,752,653	1,831,894	1,811,722	1,856,817	1,954,526	2,017,259	2,156,535	2,164,335	2,155,721	2,212,977	2,103,881	2,114,306
California Avenue	790,954	807,490	863,730	879,364	895,989	917,851	928,031	945,340	952,300	976,897	999,421	1,020,704	1,034,151

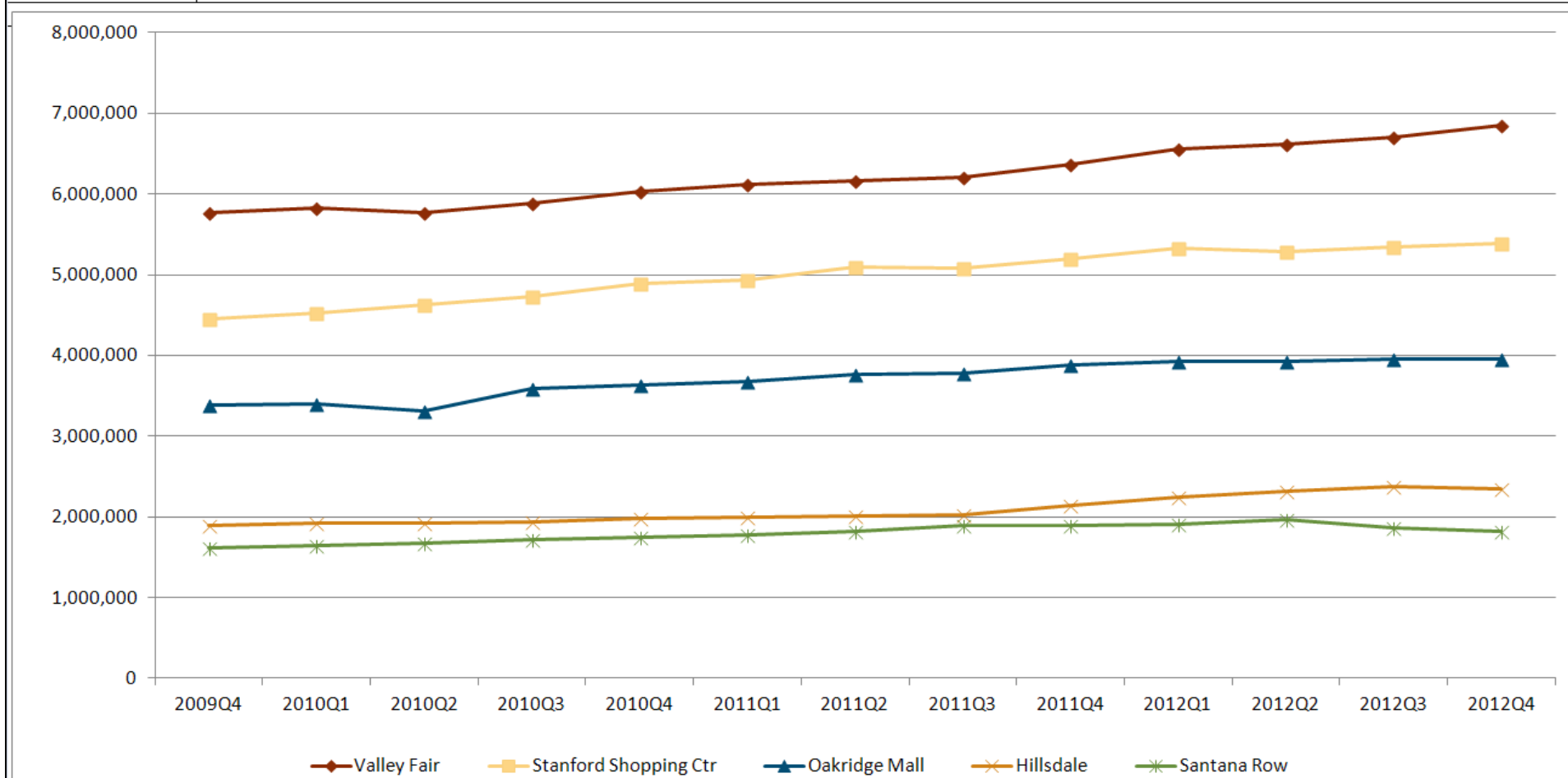


\*Benchmark year (BMY) is the sum of the current and 3 previous quarters (2012Q4 BMY is sum of 2012 Q4, Q3, Q2, & Q1)

## City of Palo Alto - Regional Shopping Mall Comparison

Benchmark Year 4th Quarter 2012

	2009Q4	2010Q1	2010Q2	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4
Valley Fair	5,761,442	5,829,695	5,769,507	5,887,510	6,031,602	6,119,960	6,166,420	6,204,976	6,370,656	6,559,394	6,621,598	6,708,343	6,855,987
Stanford Shopping Ctr	4,451,986	4,524,318	4,631,095	4,731,800	4,884,843	4,941,127	5,087,834	5,079,526	5,194,491	5,325,435	5,281,772	5,345,618	5,388,747
Oakridge Mall	3,380,772	3,395,994	3,308,231	3,589,119	3,630,341	3,679,073	3,768,899	3,782,531	3,888,402	3,928,855	3,925,454	3,947,751	3,957,195
Hillsdale	1,895,456	1,915,711	1,917,510	1,943,391	1,982,532	1,989,259	2,015,790	2,019,678	2,145,957	2,241,553	2,315,120	2,381,548	2,348,668
Santana Row	1,615,462	1,637,476	1,667,967	1,711,667	1,749,506	1,770,255	1,821,843	1,897,528	1,892,070	1,900,328	1,961,561	1,867,513	1,819,616

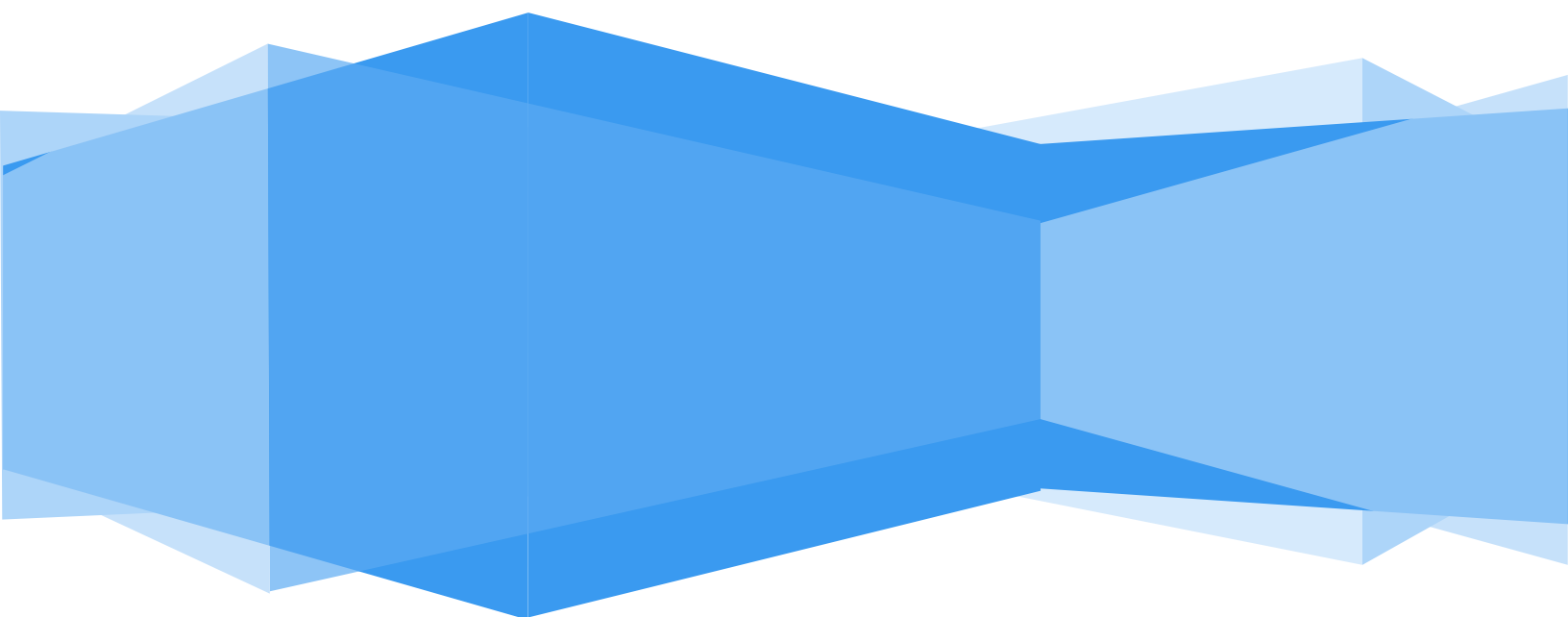


\*Benchmark year (BMV) is the sum of the current and 3 previous quarters (2012Q4 BMV is sum of 2012 Q4, Q3, Q2, & Q1)



# Economic Overview

## 1Q2013 News



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## **HOLIDAY SHOPPING SEASON**

### **Ending on a high note**

National retail sales, traffic up 2.5 percent after last-minute buys

Extended shopping hours and big sales helped retailers overcome a sluggish start to the holiday season and post strong sales during the final shopping days of the year. National retail sales and shopper traffic increased 2.5 percent from the holiday shopping season last year, ShopperTrak announced recently. The boost came largely from last-minute shoppers who waited until the final weekend before Christmas to hit the stores, according to ShopperTrak, which follows retail foot traffic.

The uptick in sales offers some much-needed positive news for retailers, who scrambled through the holiday season with a flurry of extreme discounts and promotions, "but it's a little bit unremarkable," said Bill Martin, ShopperTrak founder. "I don't think the retailers could have done anything differently," he said, citing consumer uncertainty about the fiscal cliff and preoccupation with the election. In October, the research firm had projected a 3.3 percent increase in sales from last year, but in mid-December scaled it back to 2.5 percent to account for the sluggish activity.

The 2012 holiday season had an unusually long stretch -- 32 days -- between Black Friday and Christmas, and many customers procrastinated. After a shopping lull that worried retailers, the Saturday before Christmas -- known as Super Saturday in the retail world -- turned out to be the second busiest day of the year, after Black Friday. Sales on Sunday were also among the strongest for the year. ShopperTrak estimates that shoppers spent \$249 billion in November and December, when some retailers get up to 40 percent of their annual sales.

Bay Area stores also benefited from bad weather. The rainstorms that blanketed the region during the weekend before Christmas weren't wild enough to down power lines but were dreary enough to drive shoppers to dry and warm malls, where many lingered and extended their shopping to escape the cold and rain, mall managers said. Shoppers who made impulse purchases helped boost sales in the final stretch. The promotions retailers pushed this year wooed shoppers to visit more stores than last year and buy items that weren't on their list, Martin said. Lower gas prices also encouraged shoppers to make more trips to the mall or visit more stores, Martin said. Bay Area gas prices were on average about 10 cents a gallon cheaper in December 2012 than the previous year.

Bay Area stores said they were able to beat back economic worries spurred by the fiscal cliff, and the strong Silicon Valley economy kept local merchants busy when stores elsewhere in the country struggled against the noise of deadlocked budget negotiations in Washington. The Bay Area's booming job growth, which outpaces the national average, and high salaries in the tech industry kept shoppers confident to open their wallets a bit wider than consumers in other parts of the country. According to a consumer survey by Citi done



in November 2012, about three-quarters of San Francisco area residents believe their financial situations are the same or better than a year ago, and that they would earn more money in 2013.

The 2012 holiday season marked the third consecutive year of increased retail sales, and the second of the past three years that saw increased foot traffic. But Marshal Cohen, a consumer behavior and retail expert with The NPD Group, cautions that ShopperTrak's traffic figures don't tell the whole story about consumers' plunging Christmas spirit and their fizzling desire to shop -- which may carry over to 2013. "While traffic is a preliminary indicator about holiday sales, it's not a tell-all story," Cohen said. "Consumer sentiment changed dramatically from the beginning of the holiday period." There was a lot of bad news and distractions to dampen even die-hard shoppers' excitement to hit the malls during the bustling season. The presidential election, Superstorm Sandy and the Connecticut school shooting may have pushed holiday shopping to the back burner for some. "There was a tremendous amount of distractions, each and every week, starting the week before the election," Cohen said. "The consumer psyche was so different this year."

### **GPD revised to 0.1% growth in fourth quarter**

The U.S. economy barely grew late last year, thanks largely to a plunge in federal defense spending that in part was likely preparation for the budget cuts under the so-called sequestration. The nation's gross domestic product, or the total value of all goods and services produced, rose by a measly 0.1 percent annual rate in the fourth quarter, according to the Commerce Department's latest calculations released recently. The government's first estimate said inflation-adjusted GDP shrank 0.1 percent in the final three months of last year. Analysts on average were expecting the quarterly GDP growth rate to be brought up to about 0.5 percent on average. GDP grew by 3.1 percent annualized in the third quarter of last year. Still, economists did not seem troubled by the modest revision, noting the unusually steep 22 percent annualized fall in defense spending in the fourth quarter. The stagnant GDP rate also reflected a big slowdown in business inventories, suggesting that companies may produce more in coming months to stock up on goods that have been run down.

### **GLOOMY FIELD POLL**

#### **Californians sour on jobs, future**

Experts say outlook hurts the state as it struggles toward full recovery

California voters have a sour outlook about the state's economy and their own employment prospects, according to a downbeat poll released recently that mirrors the sluggish and uneven rebound in the Golden State's job market. An estimated 72 percent of California voters say the economy is mired in "bad times," according to a new Field Poll survey of 834 registered voters in February. For the sixth consecutive year, a dreary stretch that began with the onset of the recession in 2008, more voters reported their present financial

situation is worse than it was the year before compared with those who reported that their financial situation has improved. "The unemployment situation is weighing down the economy," Mark DiCamillo, director of San Francisco-based Field Research, said in an interview. "There are not a lot of silver linings in this report. People are very pessimistic."

The poll also determined that 61 percent of California voters see the unemployment situation as "very serious," and only one-third say they expect their job prospects to improve during 2013. About the only bright spot in the poll, Field Research said in a prepared release, is "a slight improvement in the extremely bleak assessments of the state's economy that voters have offered over the past five years." Jordan Levine, director of economic research with Beacon Economics, said that while the state's economy is growing, the poll reflects "a sense that we haven't caught up with the prior expansions. People believe we are still in hard times."

Compared with the state as a whole, there is less cause for gloom in the Bay Area, which created 91,400 jobs last year -- 40 percent of the 225,900 jobs created in all of California. "The Bay Area is in much better shape than California," said Scott Anderson, chief economist with Bank of the West. "Job growth in the Bay Area is twice as fast as California and the nation." The California jobless rate remained stuck at 9.8 percent in December, and job totals fell by 17,500. Both results point to a statewide economy that is still facing challenges. "The poll results are surprising and they are disappointing," said Jon Haveman, chief economist with the Bay Area Council's Economic Institute. "That pessimism will hurt the economy."

According to the poll, 44 percent of California voters believe they are worse off financially now than they were a year ago, while 30 percent believe they are better off financially. "The more pessimistic people are, they will be less likely to spend money," Haveman said. "That will reduce aggregate demand and curtail the recovery." Mike Henneberry, a spokesman for United Food and Commercial Workers Local 5, said the pessimistic poll results reflect the mood of the rank-and-file supermarket workers he represents. "Hours are down in retail grocery," he said.

The brutal recession and sluggish recovery left many workers with an attitude of resignation that their financial and employment circumstances simply won't improve in any meaningful way. "It's almost like a new normal in California," DiCamillo said. "We are nowhere near full employment. And people are being asked to deal with high levels of unemployment as a structural situation."

## **February auto sales up as consumers show "nerves of steel"**

Auto sales rose nearly 4 percent in February, delivering a better-than-expected performance as strength in the housing market tempered worries over the wave of federal spending cuts which began on March 1. The annual auto sales pace for February was 15.38 million vehicles, according to Autodata, better than the 15.1 million rate expected by economists polled by Thomson Reuters. This marked the fourth month in a row that the

sales pace held above the 15 million-vehicle mark, a sign that rising home values are helping American consumers feel more confident about buying a new vehicle. "The escalator is heading up and not down," said Kurt McNeil, head of U.S. sales operations for General Motors, which posted a better-than-expected sales gain.

This boost in housing comes at a time when the average vehicle on the road is at an all-time high of more than 11 years old and pushing past the point of repair. Increased housing construction helped boost sales of pickup trucks during the month. GM's truck sales to small business owners were up 40 percent, giving a "strong vote of confidence in the underlying economy," McNeil said. GM, the largest U.S. automaker, posted a nearly 30 percent jump in sales of its Chevrolet Silverado trucks, while Ford Motor's F-Series gained 15.3 percent.

### **HONDA, NISSAN FALL**

Auto sales each month are an early indicator of economic health. The auto industry is in the midst of its fourth year of recovery from an economic downturn that pushed GM and its smaller U.S. rival, Chrysler Group LLC, into bankruptcy in 2009. GM's U.S. sales rose 7 percent in February to 224,314 cars and trucks, while Ford, the No. 2 U.S. automaker, saw sales rise 9 percent to a weaker-than-expected 195,822 vehicles. U.S. auto sales in 2012 rose more than 13 percent to 14.5 million cars and trucks. Sales rose 14 percent in January to an annual sales rate of 15.3 million. Like January, February is typically a slow sales month for the industry, so a small change in sales can have a large impact on the annual rate for the month.

Sales at Chrysler, majority-owned by Italy's Fiat, rose 4 percent to 139,015 vehicles, slightly less than some analysts expected. Japanese automakers Toyota Motor Corp, Honda Motor Co and Nissan Motor Co each posted weaker-than-expected sales last month. Toyota's sales rose 4.3 percent, while Honda fell 2 percent and Nissan dropped 6.6 percent.

### **MARCH AUTO SALES**

#### **Strong demand for trucks driving U.S. auto sales**

America is getting back to work, and it needs pickup trucks.

Strong truck demand in March drove U.S. auto sales to their highest monthly total since August 2007, as everyone from oil and gas producers to home builders raced to replace the aging trucks they held onto during the recession. Overall auto sales rose 3.4 percent to 1.45 million, according to Autodata Corp.

March is typically a good month for the auto industry. Many car buyers put tax refund checks toward a down payment. And Japanese automakers, whose fiscal year ends in March, often juice sales with deals to end the year on a high note.

But this year had additional incentives for buyers. Fuel prices ended the month lower than a year ago. The number of Americans seeking unemployment benefits fell to a five-year low during March. Interest rates are low, and home values are rising. And the stock market – which is a strong predictor of auto sales – closed the first quarter with the S&P 500 at an all-time high.

GM, Ford and Chrysler sold 154,722 full-size pickups, up 14 percent from a year ago. It's the third straight month that pickup sales have outpaced overall industry sales. Cars with the latest designs are enticing buyers. The redesigned Nissan Altima sedan outsold the Toyota Camry, the perennial midsize king, in March by 100 vehicles. The redesigned Honda Accord, which went on sale at the end of last year, also came close to outselling the Camry, which was last redesigned in 2011. Small car sales have slowed, in part because gas prices are relatively low.

## **'Showrooming' a threat to many retailers**

### **Study: Shoppers check prices, then buy on Amazon**

The rapid rise in the use of smartphones has brought a new curse on brick-and-mortar retailers: showrooming. That's when shoppers visit a store to try out products and then buy them cheaper online from Amazon.com or another website — often making their purchases on a smartphone in plain view of the store's staff.

To combat showrooming, Best Buy and Target recently promised to match the prices of online competitors, but they're not the only chains that should be worried about losing sales to Amazon. A new study by Seattle startup Placed identifies home-goods chain Bed Bath & Beyond as most at risk of becoming a showroom for Amazon, followed closely by PetSmart and Toys R Us. The survey — based on responses from nearly 15,000 U.S. consumers, as well as an analysis of their movements through the physical world — also puts Costco Wholesale on notice that its customers have no qualms about showrooming. While it's unclear how many Costco customers use the chain to test-drive products before buying them from Amazon, Placed believes there's enough overlap to raise the warning flag. Amazon Prime members, who pay \$79 a year for free two-day shipping of their online orders, are 45 percent more likely than the average consumer to shop at Costco, the study found. (By comparison, Costco members pay an annual fee of \$55, or \$110 if they want a 2 percent reward on most purchases.) Also, Prime members who tend to showroom are 38 percent more likely than the average showroomer to visit Costco, meaning the chain's customers regularly shop on Amazon and are adept at using technology to find deals.

Amazon promotes a free mobile app to encourage customers to check prices on its website while browsing in stores. What's more, it's known to play hardball: In 2011, it offered a special discount to holiday shoppers who made a purchase on Amazon after using its price-check application. "I think Costco should be scared," said David Shim, founder and CEO of Placed, a location-analytics firm backed by Madrona Venture Group. "For Amazon to carry

bulk items is not a stretch. It could quickly adjust its merchandise mix and highlight the fact that it has similar products as Costco and can get them to your house in two days."

## **Barnes & Noble will close a third of stores**

### **Chain to shut about 20 locations per year over the next decade**

Barnes & Noble will shut up to a third of its brick-and-mortar bookstores over the next decade as reading habits change and digital publications evolve, according to a new report. The chain will end up with 450 to 500 stores in 10 years, down from the 689 physical stores it has now, according to Mitchell Klipper, chief executive of Barnes & Noble's retail group.

That evens out to about 20 stores shuttered yearly over the period, Klipper said in an interview with the Wall Street Journal. Over the last decade, Barnes & Noble has balanced an average annual closing rate of 15 stores with 30 openings each year through 2009. "Of that number, some of the stores are unprofitable while others are relocations to better properties," spokeswoman Mary Ellen Keating said of the closures.

Since then, however, the growth rate has shriveled, with the company opening just two stores this fiscal year. Klipper told the Journal that the smaller physical footprint is "a good business model." "You have to adjust your overhead, and get smart with smart systems," he said. "Is it what it used to be when you were opening 80 stores a year and dropping stores everywhere? Probably not. It's different. But every business evolves."

In a statement, Keating said Klipper's projections "are consistent with analysts' expectations" and are historically consistent. "Barnes & Noble has not adjusted its store closing plan whatsoever," she said. She also noted that the chain has opened two prototype stores and plans to test others this year. The New York company began selling its Nook e-readers in 2009 and also has a separate division with 674 college locations. Rival bookseller Borders Group Inc. began liquidating all its stores nationwide in 2011, crushed by massive debt and changes in the industry. Said Keating: "Barnes & Noble has great real estate in prime locations and the company's management is fully committed to the retail concept for the long term."

## **Americans' household wealth reaches new high**

Surging stock prices and steady home-price increases have finally allowed Americans to regain the \$16 trillion in wealth they lost to the Great Recession. The gains are helping support the economy and could lead to further spending and growth.

Household wealth amounted to \$66.1 trillion at the end of 2012, the Federal Reserve said Thursday. That was \$1.2 trillion more than three months earlier and 98 percent of the pre-recession peak. Further increases in stock and home prices this year mean that Americans'

net worth has since topped the pre-recession peak of \$67.4 trillion, private economists say. Wealth had bottomed at \$51.2 trillion in early 2009. "It's all but certain that we surpassed that peak in the first quarter," said Aaron Smith, senior economist at Moody's Analytics.

Household wealth, or net worth, reflects the value of assets like homes, stocks and bank accounts minus debts like mortgages and credit cards. National home prices have extended their gains this year. And the Standard & Poor's 500 index, a broad gauge of the stock market, has surged 8 percent so far this year. Some economists caution that the regained wealth might spur less consumer spending than it did before the recession. Americans are cashing out less home equity, for example, than they did five years ago, notes Dana Saporta, an economist at Credit Suisse, notes that Americans are now less likely to use the equity in their homes to fuel spending. The value of home equity has fallen 90 percent in six years, she said. And since the housing bust, when home values fell broadly for the first time in decades, many homeowners are skeptical that higher prices will last, Saporta said. They won't necessarily spend more as a result.

## January a good month for retailers

### Discounts after the holidays lure more shoppers

Retailers got a much-needed boost in January after a lackluster holiday shopping season, using post-holiday clearance deals to lure cagey consumers worried about higher payroll taxes. For a cross section of major retailers, that translated into a 5.8% sales upswing last month from January 2012. Analysts had expected a 3.5% boost. The data from Thomson Reuters feature a roundup of 18 retailers' same-store sales, which account for revenue at retail locations operating for at least a year to strip out the fluctuations of recent openings and closings.

Some experts say the figures represent at most a snapshot of retail health because the report doesn't include behemoths such as Wal-Mart Stores Inc. and Best Buy Co. And more chains, including Macy's Inc. and Target Corp., are planning to ditch their monthly sales reports to focus on quarterly earnings. The numbers that retailers did disclose surprised analysts with their strength, given the economic strain weighing down shoppers. A higher payroll tax went into effect last month. Consumer confidence slid to its lowest level since November 2011, according to the Conference Board recently. "Our guests continue to shop with discipline in the face of a slow economic recovery and new pressures," Target Chief Executive Gregg Steinhafel said.

## Job growth spurs jump in February retail sales

Thanks to solid job creation, Americans spent more at retailers in February despite smaller paychecks. The surprisingly strong increase helped allay fears that higher Social Security taxes and gasoline prices might chill spending early this year. Much of the increase in February retail sales compared with January reflected the higher gas prices. But even excluding the volatile categories of gas, autos and building-supply stores, so-called core



retail sales rose strongly. Economists were encouraged by healthier-than-expected numbers from the Commerce Department. Afterward, some revised their estimates of U.S. economic growth for the January-March quarter.

Americans increased their overall retail spending 1.1 percent last month over January, the department said. It was the sharpest month-to-month increase in five months. Core sales rose 0.4 percent. And the government revised up its January figures to show that core sales rose 0.3 percent from December, better than its initial estimate of a 0.1 percent gain. Over the past 12 months, retail sales have risen 4.6 percent — far more than consumer inflation.

## **Economy showing two faces in latest data**

Despite a measure of caution on the part of consumers, new data recently suggested that the economy had underlying strength. Factories reported a healthy gain in output in February, and inflation remained under control, even though gasoline prices have been rising sharply. Led by the automobile sector, industrial production jumped 0.7 percent in February, the biggest gain in three months, the Federal Reserve said. Economists had been expecting a 0.4 percent rise.

By contrast, the Thomson Reuters/University of Michigan's preliminary reading for consumer sentiment in March showed a marked drop; the index fell to 71.8, from 77.6 in February. That was its lowest level since December 2011. The split in the data underscores the wider crosscurrents buffeting the economy. On one hand, the stock market is near record levels, big companies are reporting strong profits and the labor market seems to be finally gaining some steam, with better data last week and this week on unemployment. In particular, the addition of 236,000 new jobs in February spurred hopes that the economy was finally producing enough jobs to lower the unemployment rate, which has been stuck at just lower than 8 percent since September. Still, consumers are being hit by the restoration of full Social Security taxes, which went into effect in January, in addition to feeling the effects of federal spending cuts that began March 1.

## **UCLA ANDERSON SCHOOL FORECAST**

### **State's growth mired in a rut**

#### **Anderson Forecast: As Bay Area Continues to thrive, California recovery to remain slow in 2013**

While the Bay Area economy remains robust, California has gotten stuck in a slowdown, according to the latest report from the closely watched UCLA Anderson Forecast. But it's not time to push the panic button. The sluggish pace of the Golden State's recovery, caused in part by Washington's budget struggles and weak economies overseas, is temporary and doesn't signal a contraction or drastic slump, the report says. "We began slowing down near the end of 2012, and that slowdown will last a while during 2013," said Jerry

Nickelsburg, a senior economist with the Anderson Forecast. "You will be getting an upswing in jobs by the end of 2014 and into 2015."

The state's jobless rate, which was unchanged in December at 9.8 percent, is expected to average 9.6 percent in 2013, 8.4 percent in 2014 and 7.2 percent in 2015, Anderson projected. Nickelsburg and other economists said the tech-oriented South Bay and the San Francisco-San Mateo-Marin regions will continue to enjoy robust job gains in the coming year or two. Recent gains have been strong enough to make Silicon Valley and San Francisco the two best employment markets in the entire country. "That whole slow-recovery, sluggish-growth scenario doesn't apply in the Bay Area," said Jeffrey Michael, director of the Stockton-based Business Forecast Center at University of the Pacific.

"There is a long way to go in this tech boom and job boom in Silicon Valley," added Mark Vitner, a senior economist and managing director with San Francisco-based Wells Fargo Bank. "We are still in the early stages of this tech expansion, when you look at the demand for tablets, smartphones, social media, social gaming." The South Bay added payroll jobs at an annual rate of 3.5 percent during 2012. That growth rate could jump to a 4 percent yearly pace during 2013, Vitner predicted. "Job gains are occurring across a broad set of industries in the Bay Area now," Vitner said. "It's not just tech. Construction, leisure and hospitality are now stronger. Housing is getting stronger."

The Anderson Forecast predicted that nonfarm payroll growth in California will reach an annual rate of 1.4 percent in 2013, 2.1 percent in 2014 and 2.3 percent in 2015. California's economy has reached an "inflection point," according to the UCLA researchers. "We're moving toward a more solid recovery that will drive down the unemployment rate," Nickelsburg said. "The California economy is growing unevenly. But it continues to grow."

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