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UCLA Anderson Forecast: National Economy Growing; Unemployment Rate Dropping; Defense Spending on the Rise

California recovery continues at a “painfully plodding” pace

LOS ANGELES (Sept. 11, 2014) — UCLA Anderson Forecast's third quarterly report of 2014 indicates that the real Gross Domestic Product for the United States will grow at about 3 percent over the next two years, following a decline of 2.1 percent in the first quarter of this year and a rebound of 4.2 percent growth in the second. On an annual basis, GDP growth will rebound a full percentage point in 2015 to 3.1 percent and to 3.4 percent in 2016. Payroll job growth should average 230,000 per month; by the end of 2016 the unemployment rate will drop to 5.3 percent. In California, employment growth is forecast to be 2.4 percent in 2015 and 2.2 percent in 2016, which will drive down the unemployment rate to 5.7 percent by 2016, just 0.3 percent higher than the U.S. rate.

This UCLA Anderson Forecast includes additional research that examines the relationship between employment and wages in Los Angeles. The report concludes that, although Los Angeles has undergone a rigorous economic recovery over the past two years, long-term employment growth is still falling behind that of other major metropolitan areas.

The National Forecast

Highlights of the September forecast include an expected rise in inflation, as measured by the headline and core consumer price indices. UCLA Anderson Senior Economist David Shulman forecasts inflation at 2 percent or higher over the next two years, driven primarily by rising residential rents and increasing health care costs. The Federal Reserve Board could raise rates by March 2015, in response to declining unemployment and rising inflation. The sectors expected to fuel the nation's economic growth include housing, nonresidential construction and investment in equipment and software.

"Despite the housing recovery being slower than we anticipated, we forecast that housing starts will rise from this year's estimated 1.025 million units to 1.32 million and 1.47 million units in 2015 and 2016, respectively," Shulman writes. "Because of continuing investment in energy production and a revival in commercial construction, nonresidential construction will start to increase rapidly in mid-2015. In 2016, investment in nonresidential construction is forecast to expand at a robust 8.2 percent. Continued strength in equipment and software spending will continue to buoy the economy."

There is a major change from prior forecasts stemming from anticipation that defense spending will increase, rather than decline. Citing the rise of Islamic State of Iraq and the Levant (ISIL) in the Middle East, and the presence of Russian troops in Ukraine, Shulman writes that there will be a "rethinking" of the U.S.'s defense posture. The forecast models in an additional \$24 billion per year in defense spending by 2016.

"For those with a long memory, we would note that the Reagan defense build-up started under President Carter in 1979 after the Iranian Revolution and the Soviet invasion of Afghanistan," Shulman writes.

The California Forecast

In the California forecast for September 2014, UCLA Anderson Senior Economist Jerry Nickelsburg writes, "The California economy is moving forward in an expansion from the depths of the Great Recession. But, even though the number of jobs is now higher than any time in the past, the state remains below its potential in output and employment. That we are entering the sixth year of expansion illustrates just how painfully plodding this recovery process has been."

The current forecast accounts for two countervailing forces that will be affecting the California economy: the U.S. economy is growing stronger, while the world economy is expected to be weaker. The result is a forecast that is only slightly stronger than that released in June.

In the housing sector, Nickelsburg notes that prices continue to rise in response to new household formation. "Construction permits have been increasing and our expectation is that this will continue through the forecast horizon," writes Nickelsburg. New home starts are expected to increase by 5 percent in California and nationwide. Job growth for 2016 is forecasted at 3 percent in California, rising more quickly than growth in the nation.

Employment and Wages in Los Angeles

UCLA Anderson Economist William Yu authored a companion piece that looks at employment and wages in Los Angeles. Yu notes that, although Los Angeles has undergone a rigorous economic recovery during the past two years, long-term employment growth is still falling behind that of other major metropolitan areas. Also, since Los Angeles has a bigger share of low-wage earners than San Francisco, the effect of raising the minimum wage on employment could be different for these two cities.

About UCLA Anderson Forecast

UCLA Anderson Forecast is one of the most widely watched and often-cited economic outlooks for California and the nation and was unique in predicting both the seriousness of the early-1990s downturn in California and the strength of the state's rebound since 1993. More recently, the Forecast was credited as the first major U.S. economic forecasting group to declare the recession of 2001. Visit UCLA Anderson Forecast at <http://uclaforecast.com>.

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