October 2001

Composite Index

Key Statistics

<table>
<thead>
<tr>
<th>Humboldt County</th>
<th>Seasonally Adjusted</th>
<th>Leading Indicators</th>
<th>% Change From Previous Month</th>
</tr>
</thead>
<tbody>
<tr>
<td>Median Home Price*</td>
<td>$144,950</td>
<td>Help Wanted Advertising</td>
<td>-2.8</td>
</tr>
<tr>
<td>30 Yr. Mortgage Rate (10/3)</td>
<td>6.5%</td>
<td>Building Permits</td>
<td>+111.4</td>
</tr>
<tr>
<td>Prime Rate (10/3)</td>
<td>5.5%</td>
<td>Unemployment Claims</td>
<td>-11.4</td>
</tr>
</tbody>
</table>
The Index of Economic Activity for Humboldt County

| Unemployment Rate** | 4.6% | Manufacturing Orders | -3.5 |

* Home price data are provided by the Humboldt County Board of Realtors. MLS is not responsible for accuracy of information. The information published and disseminated by the Service is communicated verbatim, without change by the Service, as filed with the Service by the Participant. The Service does not verify such information provided and disclaims any responsibility for its accuracy. Each Participant agrees to hold the Service harmless against any liability arising from any inaccuracy or inadequacy of the information.

** Preliminary EDD data. See the EDD Website for updates.

** Sectoral Performance, Index of Economic Activity for Humboldt County**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Sectoral Index Value (1994=100)</th>
<th>Previous Month</th>
<th>Same Month 2000</th>
<th>Same Month 1999</th>
<th>Same Month 1998</th>
<th>Same Month 1997</th>
<th>Same Month 1996</th>
</tr>
</thead>
<tbody>
<tr>
<td>Home Sales</td>
<td>82.91</td>
<td>-40.8</td>
<td>-17.8</td>
<td>-22.1</td>
<td>-22.1</td>
<td>-12.9</td>
<td>-12.0</td>
</tr>
<tr>
<td>Retail Sales</td>
<td>142.3</td>
<td>-8.1</td>
<td>+5.3</td>
<td>-0.9</td>
<td>+1.1</td>
<td>+10.7</td>
<td>+33.7</td>
</tr>
<tr>
<td>Hospitality</td>
<td>107.6</td>
<td>-0.2</td>
<td>-5.2</td>
<td>-4.9</td>
<td>-3.9</td>
<td>+4.7</td>
<td>-2.0</td>
</tr>
<tr>
<td>Electricity Consumption</td>
<td>138.7</td>
<td>+6.6</td>
<td>+5.7</td>
<td>8.2</td>
<td>+34.9</td>
<td>+34.7</td>
<td>+31.8</td>
</tr>
<tr>
<td>Total County Employment</td>
<td>101.6</td>
<td>-0.9</td>
<td>-2.3</td>
<td>-3.3</td>
<td>-2.3</td>
<td>-0.2</td>
<td>0.0</td>
</tr>
<tr>
<td>Lumber Manufacturing</td>
<td>84.7</td>
<td>-11.3</td>
<td>-26.6</td>
<td>-24.6</td>
<td>-30.6</td>
<td>-34.5</td>
<td>-22.5</td>
</tr>
</tbody>
</table>

**Discussion**

**Composite Index and Overall Performance**

The Index of Economic Activity's seasonally adjusted composite value fell a scant 0.1 to 115.7 percent from the August report's upwardly revised 115.8. The current figure is also down slightly in same month comparisons for the past two years, but is up strongly when compared with the same months of 1996-1998.

Despite the large amount of red ink in our sectoral performance chart above, things could be far worse. Humboldt County's economy seems to have not been affected much in the aftermath of September 11th. Retail and hospitality both declined, but not nearly as much as in many parts of the country. Employment, while also slightly lower in most comparisons, reflects a local labor market in relatively good shape. The unemployment rate here is as low as it has ever been in the seven years of the Index's existence. The precipitous drop in home sales is cause for concern, as it has been the most consistently strong sector of the local economy for several months. Lumber manufacturing's continued poor performance, while the rest of the economy remains in fairly good shape, indicates that though this sector is still an important player in local industry, it's not the dominant one it once was. Finally, the electricity consumption data tell us two things. The increased use of energy reflects a higher amount of economic activity, which is a good thing. However, it also reflects that we are conserving less power than we were a couple of months ago. Industry analysts warn that should demand outpace supply, as it did last winter, rolling blackouts again become a likely possibility.

The Leading Indicators are mixed this month, and thus don't offer much help in making informed guesses about the future. The number of building permits issued is extraordinarily positive, but this level of performance is probably not sustainable. The number of new unemployment insurance claims is down sharply for the second straight month, which is a positive indication of the labor market. However, since the size of the
labor force shrunk over the current period, these data are consistent with the notion that people losing their jobs may be leaving the county rather than filing for unemployment compensation. Help wanted advertising and manufacturing orders are both down after positive showings last month.

Home Sales

The home sales sector fell by a discouraging 40.8 percent in September. It is also down by double-digit percentages in all of the year-over-year comparisons going back to September 1996. This brings the seasonally adjusted Index figure for this sector to its lowest point since February 1998. Since, presumably, most of the 88 units sold in this period entered escrow prior to the events of September 11th, the decline seems to be due to already eroding economic conditions rather than to uncertainties arising from the attacks. Nonetheless, local real estate professionals would probably maintain that the monthly drop off is little more than an anomaly. According to several realtors and loan officers interviewed in a recent Times-Standard article, the Humboldt County market remains fundamentally strong with tight demand and appreciating values. Information from the Humboldt Association of Realtors lends some credence to this view. The average number of days on the market for homes sold in September was the fewest of any month this year and the median home price rose 1.0 percent from $143,500 in August to the current $144,950. The median price is also up 5.8 percent from the September 2000 figure of $137,000. As always, next month's data will help determine the overall significance of this month's dismal showing.

Real estate markets in other parts of northern California experienced similar downturns in sales volume during September. In the Bay Area, 25.6 percent fewer homes were sold this month than in the same month of 2000 (locally, the year-over-year comparison in units sold fell 17.8 percent) and the median sale price of $373,000 is 5.4 percent above the September 2000 figure (www.sfgate.com). The Sacramento area market saw a 12 percent year-over-year decrease in the number of escrows closed. The number of pending sales in the Sacramento region offers some evidence that the September 11th attacks may be affecting sales adversely. This figure fell by about 33 percent from August to September, and by 35 percent from September of last year. In 2000, the August-to-September decline was just 5.5 percent (www.sacbee.com).

Nationally, the number of both new and existing home sold in September fell from the previous month. New home sales dropped by 1.3 percent from August's downwardly revised figure and, by 4.2 percent from September 2000. Existing home sales declined more sharply with September's number coming in 11.7 percent lower than August's upwardly revised figure. A large part of the latter drop is due to the market returning to a more normal level after the record setting number of existing homes sold in August. Since these figures largely represent pre-September 11th activity, they indicate a weakening in what had been the last consistently positive sector of the economy. Analysts at the Dismal Scientist expect sales to remain sluggish until the second or third quarter of next year. The national median sale prices for new and existing homes were $171,100 and $148,100, respectively (www.dismal.com).

Meanwhile, an article in the San Francisco Chronicle reported on the high cost of renting an apartment. San Francisco is the least affordable city in the U.S. for apartment dwellers. A renter there must earn $33.60 per hour (nearly $70,000 per year) in order to afford a two-bedroom apartment. Affordable housing is routinely defined as that costing 30 percent or less of one's gross income. Across the bay, in Oakland, the hourly wage needed for a similar apartment is $23.90. For the U.S. in general, the figure is $13.87 per hour. Assuming that the monthly rent for a typical two-bedroom in central Humboldt County is $550, a local renter must earn $11.46 per hour in order to meet the affordability criteria.

Retail Sales

Sales among the retailers participating in the Index decreased by a sharp 8.1 percent from the previous month, but the current figure compares favorably with same month performance in most years of the recent past. Next month's number will give a better idea of whether the fall is due mostly to the events of September 11th, or is an indication of a sustained cooling off in consumer spending.
As expected, the September 11th attacks sharply impacted nation-wide retail sales. The optimism that came with August's revised 0.4 percent gain evaporated with September's 2.4 percent decline, the largest monthly fall-off on record. Much of the drop can be attributed to the severe decrease in consumer activity in the week immediately following the disaster and to a dramatically increased level of overall economic uncertainty. The apparel subsector was hit hardest, with sales down 5.9 percent. Automobile sales were also down for the second straight month, falling 4.6 percent. Subsectors that experienced gains in August, but fell this month include electronics and sporting goods. Sales of necessities, such as gasoline and health and personal care items increased as consumers appeared to be stocking up. Food and beverage sales were unchanged from August's performance (www.dismal.com).

An apparent fear of public places may be at least partially responsible for the woes of conventional retailers. E-commerce experienced huge, unexpected gains in the aftermath of September 11th. According to Nielson/NetRatings, retail spending online was up a startling 54 percent from the same month last year as many people seem to be cocooning themselves in their homes (www.sfgate.com).

Despite consumer confidence measures that remain high compared to those during the last recession, confidence in the immediate period is falling. As a result, the many retail analysts are expecting weak holiday sales. Sales growth is predicted to be around 1.5 percent in the fourth quarter. Last year's figure for the same period was 4.5 percent (www.sfgate.com).

Hospitality

We use occupancy rates at participating county hotels and motels as the indicator of this sector's performance. The hospitality sector is down across nearly all comparisons. The good news is that the magnitude of the decline is far smaller than in many other areas.

The hospitality industry was one of those most affected by events of September 11th. Nation-wide, occupancy rates are currently estimated to be around 30 percent. Profitability in this industry generally depends on occupancy rates higher than 55-60 percent. Particularly hard hit are hotels in major metropolitan areas. The most recent data on revenue per available room show that July performance in San Francisco and Boston was down by over 20 percent from the same month in 2000. New York, Chicago and Atlanta were down by at least 15 percent over the same period. The situation has only gotten worse since then. In the weeks following the attacks, there has been a wave of cancellations of conventions, business travel and vacations (www.dismal.com). This is especially bad news for San Francisco, where travel and tourism is a $20 million per day business. September and October two of that city's busiest months. In an attempt to lure the relatively few clients still traveling, hotels are slashing their rates. It's not unusual to see nightly rates at 50 percent of what they were last year (www.sfgate.com).

Meanwhile, news on gasoline prices--which has found a home in this section of our report for lack of a better place--continues to brighten. According to the latest survey by the California State Automobile Association (released 10/16), the price of a gallon of self-serve unleaded regular gas in Eureka fell 12 cents from the previous month to $1.89. The Bay Area price for the same gallon of gasoline fell 7 cents to $1.79, while the state and national prices dropped 13 and 19 cents to $1.60 and $1.35, respectively. As noted in last month's report, lower demand due to fewer total miles traveled both in the air and on the road is primarily responsible for the falling prices.

Electricity Consumption

We use kilowatts of electricity consumed as our indicator of the energy sector of the Humboldt county economy.

The local trend towards electricity conservation seems to have ended. Data on actual usage during the third quarter indicate that Humboldt County residents consumed 7.2 percent less electricity in July than in the same month of 2000. State-wide, this figure was 5.2 percent. In August, local consumers used just 0.5 percent less than...
in August 2000, while California as a whole used an encouraging 8.9 percent less. September's numbers show that we used 6.6 percent more power than in August and 5.7 percent more than in September 2000.

Seasonally-Adjusted Energy Index for Humboldt County (Jan.'00-Sept.'01)

Total County Employment

In their preliminary report for September, the Employment Development Department (EDD) reported that 56,500 people were employed in Humboldt county, down 100 jobs, or 0.2 percent from August’s revised figure. The seasonally adjusted October Index figure for this sector is down 0.9 percent from the corresponding revised number in September's report. It is also down when compared to the same month's performance in the most recent years. Preliminary EDD data indicate the following changes in Humboldt county employment:

- Total county employment in the various service industries increased 1.0 percent from a revised 41,500 during the month of August to a preliminary 41,900 for the month of September. This sector is also up 1.5 percent over last year's figure. The increase was led by job creation in the various government subsectors and in Business Services. The preliminary figure for the retail subsector in September shows 11,000 jobs, which is unchanged from the revised August figure. Not unexpectedly, the Hotel and Other Lodging and the Transportation subsectors both seem to have been adversely affected by the events of September 11th. They fell by 10.0 percent and 9.1 percent, respectively from August's revised figures. The decreases each represent about 100 jobs lost.
- Total county manufacturing employment regained the roughly 100 job lost last month. The number of people currently employed in this sector stands at approximately 6000. The Lumber and Wood Products subsectors experienced no change, while Food and Kindred Products rose by a strong 14.3 percent. Total manufacturing employment is down 3.2 percent from September 2000.

Despite the slight fall in the total number of jobs, the County's unemployment rate, now at a preliminary 4.6 percent, dropped for the third consecutive month. This is due to a 0.7 percent decrease in the labor force. There were some 400 fewer people working or actively seeking work in September than in August. The national jobless rate remained unchanged at 4.9 percent and California’s rate fell to 5.2 percent.

Nationally, 199,000 net jobs were lost in September. Yet again, reports indicate manufacturing led layoffs with 93,000 jobs shed. This is the fourteenth consecutive monthly decrease for this sector. Service industries employment was flat. It is critical to note that these data were gathered just prior to the events of September 11th. As such they reflect a labor market continuing to deteriorate even before the shock of that date. This month's decline was the largest since February 1991. When the jobs lost as a result of the attacks are accounted
for, the employment situation will darken considerably. Analysts at the Dismal Scientist present a best case scenario in which the labor market continues to contract through the second quarter of 2002, with the unemployment rate rising to 6 percent.

While we have become accustomed to jobless levels well below this in recent years, most economists probably are not too concerned about the above projection. A commonly held theory states that zero unemployment is impossible since there will always be people in between jobs trying to improve their economic situations (this is called frictional unemployment) as well as people losing jobs due to things like overseas competition or their skills becoming obsolete (this is known as structural unemployment). Because of these factors, the theory holds that there is a "natural" rate of unemployment that is not only inevitable, but necessary in order to inhibit inflation and sustain growth. Conventional wisdom currently puts this rate at around 5.2 percent. There are at least a few economists, however, who disagree. Jared Bernstein and Dean Baker argue that proponents of the consensus figure are "engaged, perhaps unknowingly, in a subtle breed of class warfare." Due primarily to a tight labor market, middle- and low-income workers made welcome gains in the late 1990s after experiencing nearly a quarter century of declining real wages and growing wealth inequality. These gains will soon be erased if policy makers accept the conventional wisdom on the natural rate of unemployment. Bernstein and Baker claim this is economically unnecessary since the experience of the past few years demonstrates that when virtually everyone who wants a job has one, acceptable levels of inflation and growth can be maintained at a jobless rate no higher than 4.0 percent. Maintaining the lower level, according to the two economists, is merely a matter of political will (www.prospect.org).

Lumber Manufacturing

We use a combination of payroll employment and board feet of lumber production at major county lumber companies as our indicator of the manufacturing sector for the Humboldt county economy. Lumber-based manufacturing generates about two-thirds of total county manufacturing employment.

This sector fell sharply in September. The Index figure is 11.3 percent lower than it was in August. It is also down by double-digit percentages in all of the year-over-year comparisons.

According to a wood products analyst in Eugene, Oregon, the industry's ongoing poor performance is a case of there being too many boards chasing too few buyers. As such, the preliminary 19.3 percent tariff imposed on Canadian softwood lumber in August will improve the bottom lines of U.S. producers for a time because the action allows them to charge more for their product. But, the trade restriction may ultimately hurt domestic lumber firms since the higher prices will likely lower an already reduced level of demand. American lumber companies are also seeking to have a 39 percent penalty assessed on Canadian firms that sell their lumber in the U.S. at below-market prices. The U.S. Commerce Department is scheduled to issue a final ruling on both the tariff and the penalty on October 30. It is widely thought that the size of any restrictive actions imposed will be substantially less than the figures cited above (www.seattlep-i.com).

This news may be too little too late for at least one local lumber company. As reported last month, Eel River Sawmills announced the closures of Mill A in Fortuna and the power plant in Fairhaven citing weak market conditions for lumber and wholesale electricity, respectively. The resulting 122 layoffs will take place at the end of November and will last at least three months. According to a company spokesperson, if conditions don't improve early next year, the action could be permanent. Over 200 employees at the Alton mill, and mills B and D in Redcrest were laid off earlier this year (www.times-standard.com).

A look at the graph below shows that the seasonally adjusted Index figure for this sector is at its lowest point ever.
Nationally, manufacturing activity fell for the twelfth consecutive month. According to the Federal Reserve, industrial output dropped by a full percentage point in September. This follows August's 0.7 percent decline. The last time this measure experienced such sustained negative growth was from November 1944 to October 1945, when the country was transitioning out of a full scale wartime economy. The dramatic decrease in production is due primarily to consumer demand that went from bad to worse after September 11th. Factories were also severely hampered by the disrupted flow of supplies due to heightened security resulting from, and a transportation system stressed by the attacks. Data indicate that industry is operating at just 75.5 percent of capacity, the lowest level since June 1983 (www.nytimes.com). An unsurprising effect of this performance is a fourteenth consecutive month of net job loss in this sector. As noted above, 93,000 fewer people were employed in manufacturing prior September 11th. Many more have lost their jobs in the immediate aftermath. Since the beginning of the year, the manufacturing sector has shed approximately 900,000 jobs (www.dismal.com).

Leading Indicators

We track four leading indicators to get a sense of the direction of change in the county economy in the near future. The four leading indicators are (i) number of help-wanted advertisements in the Times Standard, (ii) number of claims for unemployment insurance, (iii) volume of manufacturing orders, and (iv) number of building permits issued.

Employment-Based Economic Indicators:

A count of help-wanted ads indicates the number of new job openings. September's Index figure is down 2.8 percent from the previous month. Its performance is mixed in the year-over-year comparisons. The measure fell 15.5 percent and 4.6 percent from the same month in 2000 and 1999, respectively. It has risen strongly, when compared to September activity in 1998, 1997 and 1996: by 27.6 percent, 31.6 percent and 15.2 percent, respectively.

Claims for unemployment insurance indicate the number of newly unemployed people in Humboldt County. Thus the number of new unemployment claims is a negative indicator of economic activity. This sector experienced a double-digit drop for the second month in a row. The number of claims made in September was 11.4 percent lower than it was in August. This follows a 12.5 percent decline between August and July. The change in the number of new claims filed between June and July was positive 12.6 percent, not negative as was reported last month. The sector is up 0.7 percent from September 2000. The current figure is lower when
compared to same month activity in the years 1999-1996 by 9.3 percent, 11.4 percent, 41.7 percent, and 31.4 percent, respectively.

Manufacturing Economic Indicator:

Manufacturing orders, a leading indicator of activity and employment in the County, are down across all comparisons once again. September's number decreased 3.5 percent from August's. In the year-over-year comparisons, the current figure fell 25.1 percent from September 2000, 23.3 percent from September 1999, 34.5 percent from September 1998, 41.5 percent from September 1997, and 40.9 percent from September 1996. Nationally, orders for durable goods decreased 8.5 percent in September (www.dismal.com).

Home Sales Economic Indicator:

The building permits indicator is up spectacularly across all comparisons this month. The number of permits issued in September rose a stunning 111.4 percent from August. The figure is also up 67.8 percent from September 2000, 52.8 percent from September 1999, 44.7 percent from September 1998, 48.7 percent from September 1997, and 89.6 percent from September 1996. The most likely explanations for this month's performance are low interest rates and good weather. According to an article in the Times-Standard, another factor may include more people taking advantage of federal assistance like the Guaranteed Rural Housing program that allows for 100 percent financing on new residential construction and no mortgage insurance. Nevertheless, industry analysts forecast a 1 percent decline in the number of new homes built nationally for the rest of this year because of declining conditions made worse by the attacks last month.

The Bigger Picture

There's not a lot to be optimistic about with the overall economy this month. The Conference Board's Consumer Confidence Index fell by 11.5 points. This follows last month's 17+ point decline. The index, which now stands at 85.5, is at its lowest point since February 1994. A year ago it was at 140.7 (www.sfgate.com and www.dismal.com).

The preliminary report on Gross Domestic Product growth for the third quarter shows that the economy contracted for the first time in nearly a decade. GDP dropped by an annualized 0.4 percent from July through September. While this is considerably better than the 1.0 percent decrease economists expected, it is still sobering news since it indicates an end to the longest economic expansion in U.S. history. Furthermore, since most of September's data has been estimated, the figure will almost certainly be revised downwards (www.dismal.com).

The latest figures on new claims for unemployment insurance are also less than encouraging. The four-week moving average of initial claims topped 500,000 for the first time since 1991. The number of continuing claims, 3,654,000, is very near the peak level reached during the last recession, and it's rising at a faster rate than it did then.

The latest release of the Federal Reserve's Beige Book, covering economic activity for late September and October, reflects this information despite being released a couple of weeks ago. It reports on deteriorating conditions across almost all sectors and all regions. Weak manufacturing and consumer spending activity continue to exacerbate a soft labor market. Although over 200,000 layoffs have been announced in the aftermath of September 11th, wages have remained stable. Prices are either steady or declining slightly depending on region. Of particular concern to the central bank is the relatively poor performance of the real estate and construction sectors. Up to now, these two areas have been consistently strong even as the rest of the economy faltered. Despite exceptionally low interest rates, both residential and commercial activity was off in almost every district (www.federalreserve.gov).

The Fed cut interest rates for the ninth time (10/2) this year, and for a second time in a month, in an attempt to ameliorate the negative effects of these conditions. The Federal Funds Rate, now at 2.5 percent, is at its lowest
level in 39 years. While the move is having a positive impact in the market for refinanced home mortgages, it has yet to gain traction in other sectors of the economy.

Congress has also taken action to cushion the fall. The House of Representatives narrowly passed an economic stimulus bill. According to an article in the New York Times, the legislation would cut corporate taxes by more than $70 billion this year. The package also includes $28 billion in tax breaks to individuals, and $12 billion in aid to states to extend aid for the unemployed. Proponents of the bill claim lower taxes to big business will stimulate capital investment, which will ease the severity of the recession and pave the way for the eventual recovery. The bill's critics say the package is little more than a payoff to wealthy campaign contributors. They argue that corporations have little incentive to invest in more production capability when they aren't utilizing the capacity they currently have. Furthermore, the bulk of money saved on individual taxes would go to those who need it least during hard times. The legislation is expected to be modified as it works its way through the Senate.

Explanatory Note: For those of you who are new or less familiar with the Index, we have been tracking economic activity since January 1994. The composite indices plotted as blue and green lines in the diagram at the top of this page are weighted averages of each of the six sectors described in the table above. Each sectoral index, and the composite index, started at a value of 100 in 1994. Thus if the retail sectoral index value is currently 150, that means that (inflation-adjusted) retail sales among the firms that report data to us are 50 percent higher than in January 1994. We also seasonally adjust each sector, and the composite index, to correct for "normal" seasonal variation in the data, such as wet season vs. dry season, and so trends in the seasonally-adjusted composite index (the blue line in the diagram above) provide a better indication of underlying growth and fundamental change in the economy. This month's report reflects data gathered from the previous month, and so the "October 2001" report reflects data from September 2001. As is common, our initial report is preliminary, and as we receive final data we revise our reports accordingly.
The Index of Economic Activity for Humboldt County