

REGIONAL INTELLIGENCE REPORT™



BEACON ECONOMICS Prepared by Beacon Economics, LLC



City of Ontario

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The U.S. Economic Outlook: Much Ado About Nothing

Ostensibly, the year has not started well for the U.S. economy. The financial markets spooked in January and equity values dropped sharply even as treasuries rallied to highs not seen since 2012. The markets have recovered, but that hasn't stopped the perpetual worries about China, oil prices, high-yield credit, tech bubbles, deflation, and so on.

However, taking a step back from the noise, the reality is that the U.S. economic expansion continues to move along at a steady, if mediocre, pace. More importantly, there is little reason to believe that the nation will stray from its current path of growth in 2016. Beacon Economics continues to forecast growth in the 2.5% plus range for the year, with perhaps even better numbers next year.

Consumer Spending: Retail sales grew at their weakest pace in years at the end of 2015. But interpreting these data can be tricky since they are based on nominal numbers and inflation is the slowest it has been in decades. Real spending data from the Bureau of Economic Analysis indicates that 2015 was a strong year for consumer spending on goods, particularly in the auto sector where U.S. automakers enjoyed a record year. This shouldn't be surprising given the strong labor market and rising real incomes. The modest slowing seen in the first quarter of this year is being offset by an increase in savings—savings that will surely be spent later in the year.

Construction: The building industry has been one of the slowest recovering sectors in the United States. Single-family housing starts are still under 800,000 (SAAR), one-third less than the long-term, stable number of 1.1 million. But the pace of construction is rising and 2016 is shaping up to be a good year. Fundamentals such as the average equity share of owners and the overall housing vacancy rate have finally returned to historic norms. Credit is slowly easing for borrowers and household formation is picking up. Home prices are still relatively good given low mortgage rates.

Manufacturing: While the ISM Manufacturing Indexes have been running below 50, suggesting contraction, real output data from the U.S. Federal Reserve indicates the opposite—that manufacturing output is up, albeit at a slower than normal pace. January's figure was the highest since the 'Great Recession' began. Some sectors, such as autos, are performing well. Others, particularly primary metals, are being hit by the global commodity glut. All in all, the sector added 50,000 jobs last year—not bad given the circumstances.

Exports: The final worry is the troubled global economy and its impact on U.S. exporters. But despite a slow down in China, oil-producing nations that are in various states of economic distress, and a strong U.S. dollar, exporters managed to increase their overseas sales in 2015 over the previous year by a small amount. The widening trade deficit last year was driven by imports, as U.S. consumers ramped up spending.

There are plenty of reasons why the U.S. economy will not grow as rapidly as everyone would like over the next couple of years, but there is little reason to believe the nation's economy will stop growing. The slow pace of growth may even be an underlying strength as the surest path to a downturn often comes from major imbalances that form in the heady days of a rapid economic expansion. Sometimes it pays to be a tortoise—particularly when that 'tortoise' offers the relatively high quality of life that so many American's enjoy.

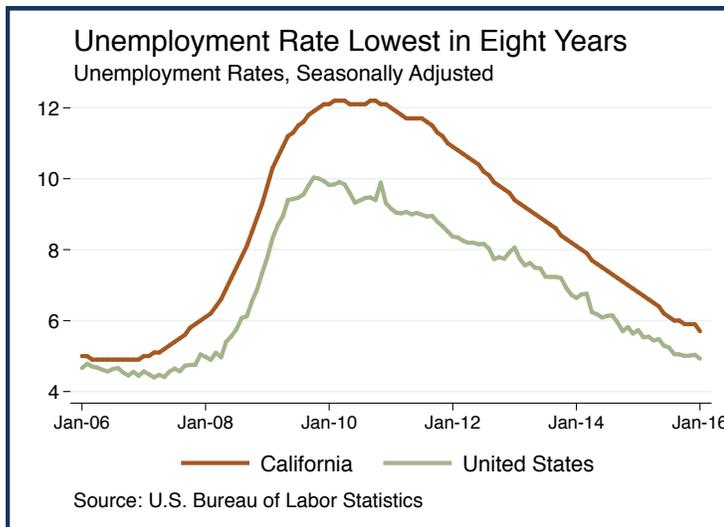
UNITED STATES

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California Economy Outpacing the Nation

California did it again. The high-priced, over-regulated, fruits-and-nuts state that everyone loves to hate turned in another strong performance in 2015. For the fourth year in a row, California outpaced the nation in job growth as well as output. The state experienced broad-based gains across its key industries ranging from agriculture to high tech, and nearly everything in between.

By the end of 2015, the unemployment rate stood at 5.9%, the lowest since late 2007. Meanwhile, California outpaced the nation in growth of wage and salary (nonfarm) jobs (3.0% vs. 2.1% for the U.S.), and actually accelerated to its fastest pace of job growth in over fifteen years. The state added over 460,000 jobs, with both coastal and inland regions participating in that growth.



Nearly every industry in California experienced job gains over the past year, generally adding to the gains of recent years. Health Care & Social Assistance, Leisure & Hospitality, and Construction led the state's industries, combining to produce nearly 45% of the state's total job gains last year. Only Mining and Logging lost jobs, as that sector reeled from the plunge in energy prices.

California's housing market continued its upward trajectory last year in terms of prices, sales, and new construction. The statewide median price for a home was \$403,600 in final quarter of 2015, an increase of 5.5% from one year earlier. Sales rose by 10.5%, but were still constrained by

lean inventories. Meanwhile, rental markets across the state were marked by low vacancy rates and rising rents, as the state's homeownership rate (54.3%) showed little sign of improvement. Looking ahead, higher home prices and sales, driven mainly by income growth, low but rising mortgage rates, and demographics, ought to trigger an increase in construction over this year and next.

Job Gains Across California's Industries

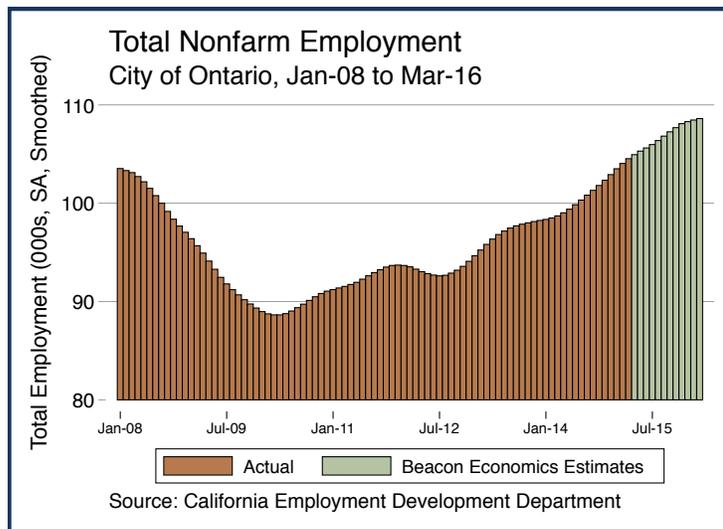
Industry	2015 Jobs (000s)	Change '14-15 (000s)	Change '14-15 (%)
Construction	726.6	52.2	7.7
Transport, Warehouse, Uti	553.5	30.1	5.8
Information	482.5	19.6	4.2
Leisure and Hospitality	1,828.3	69.4	3.9
Education/Health	2,455.8	90.0	3.8
Admin Support	1,058.8	33.8	3.3
Prof Sci and Tech	1,207.4	34.1	2.9
Real Estate	271.9	6.7	2.5
Retail Trade	1,663.4	34.5	2.1
Management	230.1	4.5	2.0
Government	2,460.0	48.3	2.0
Finance and Insurance	526.2	9.6	1.9
Farm	423.3	6.9	1.6
Other Services	545.3	8.7	1.6
Wholesale Trade	720.8	10.8	1.5
Manufacturing	1,292.2	18.0	1.4
NR/Mining	29.0	-2.6	-8.3
Total Private	13,591.7	419.4	3.2
Total Nonfarm	16,051.8	467.7	3.0

Source: California Employment Development Department

This year is shaping up to be one of steady gains in overall economic activity and employment, with the state's key industries continuing to see job growth and the fortunes of California's households improving with rising wages and growth in personal income. Despite concerns over the business climate, the state economy is one of the most dynamic in the country, as evidenced by the large amount of venture capital it has attracted on a consistent basis over the last several years.

Employment

With significant improvements in the overall U.S. and California economies, the City of Ontario has continued to enjoy steady gains in both payrolls and employment over the last year. During that time, total employment in the City increased by 4.2% to 108,975 jobs in March 2016, according to data from the California Employment Development Department and estimates by Beacon Economics, outpacing job growth in Inland Southern California (3.3%) during that time. Along with Inland Southern California, the City has recovered the jobs lost during the recession and has recently surpassed its pre-recession peak levels of employment.



Finance and Insurance was the City’s fastest-growing sector over the last year. From March 2015 to March 2016, the industry is estimated to have increased payrolls by 13.0%, adding roughly 300 jobs. This growth is driven by increases in business activity and consumer income, a sign that the business climate continues to improve. Not far behind was the Management, Professional, Scientific, Technical and Technical Services industry, which increased 9.6% from March 2015 to March 2016. The Corporate Advocate, a management/consulting firm, moved from Rancho Cucamonga to Ontario¹ in April 2016 and is expected to provide a useful resource for the City’s businesses by helping them work through the red tape that typically acts as a barrier to entry for prospective start-ups.

Employment by Industry in the City of Ontario

Industry	16-Mar	YOY Chg.	YOY (%)
Finance & Insurance	2,675	300	13.0
Prof, Sci, Tech, & Mgmt	6,775	600	9.6
Construction	4,525	375	8.8
Transport/Warehouse	16,500	1,225	8.2
Education/Health	8,650	575	7.1
Other Services	3,350	225	6.8
Wholesale Trade	10,950	500	4.8
Admin Support	12,725	275	2.2
Manufacturing	13,000	250	1.9
Retail Trade	13,275	75	0.5
Information	1,875	0	0.5
Leisure & Hospitality	7,125	25	0.5
Government	5,550	0	0.3
NR/Mining	725	-25	-3.0
Real Estate	1,275	-50	-3.0
Total All Industries	108,975	4,375	4.2

Source: EDD & Beacon Economics

Another industry that stood out in March 2016 was Transportation and Warehouse, which supported 28% of total employment growth across all industries, adding 1,225 jobs from March 2015 to March 2016. Logistics giant UPS announced in March that it plans to add 500 jobs, expanding its operations at Ontario International Airport.² Already, the UPS facility in the City supports 4,500 jobs. With UPS committed to expanding and serving customers in Inland Southern California and beyond, the future for transportation is bright and should continue to grow in 2016.

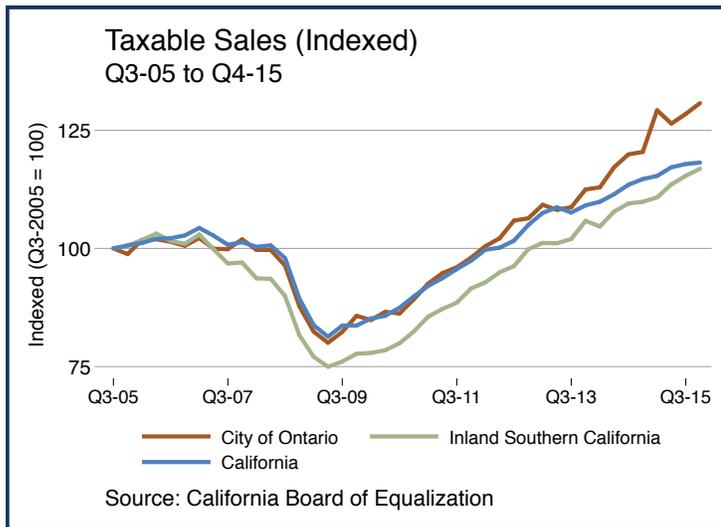
With wages increasing 3.4% across all industries and employment surpassing its pre-recession peak, the City is expected to continue to grow in 2016.

¹“The \$800 Million Corporate Advocate Moves to Ontario – Host Grand Opening.” Inlandempire.us. April 14, 2016.

²Marquez, Liset.“UPS adding jobs, space at Ontario airport.” Inland Valley Daily Bulletin. March 27, 2016

Local Spending

With consumer confidence on the rise and local labor market conditions gaining traction throughout the region and in the state, consumer and business spending in the City continued to rise through 2015. From the fourth quarter of 2014 to the fourth quarter of 2015, taxable sales in Ontario increased by 8.6% to \$1.8 billion. Local spending in the City outpaced growth in both California (3.0%) and Inland Southern California (6.4%). On an annual basis, taxable sales in the City increased 9.4% from 2014 to 2015, outperforming Inland Southern California and California, which grew 5.7% and 4.2%, respectively. After a low in 2009, taxable sales in Ontario have increased 63.4%, with positive year-over-year growth for 24 consecutive quarters. Local spending by consumers and businesses continues to grow at a strong pace.



According to taxable receipts data from HdL Companies, most categories of spending increased in San Bernardino County during 2015. Taxable receipts in the Business and Industry category increased faster than in any other, gaining 18.6% year over year and reflecting strong business-to-business spending on services. Businesses in San Bernardino County continued to spend on structural improvements and expansions as well, as marked by the 11.5% increase in taxable receipts from Building and Construction over the same period.

The Restaurants and Hotels sector in San Bernardino County saw modest increases in taxable sales receipts, increasing 6.2 percent from the fourth quarter of 2014 to the fourth quarter of 2015. With the local labor market continuing to expand, consumers are willing to spend more on leisure and hospitality. Tourism in the City of Ontario is supported from both its hotel presence and the local airport, Ontario International. Hotel data suggest that both tourism and business travel are growing

Sales Tax Receipts by Category in San Bernardino County

Category	Q4-2015 (\$000s, SA)	YoY Chg. (%)	2 Yr Chg. (%)
Business and Industry	20,198	18.6	34.8
Building and Construction	7,073	11.5	16.2
Autos and Transportation	14,733	7.4	15.6
General Consumer Goods	18,343	6.4	7.8
Restaurants and Hotels	8,100	6.2	15.6
Food and Drugs	3,730	4	7.9
Fuel and Service Stations	9,180	-12.7	-15.1
Total	90,767	7.2	13.8

Source: HdL Companies

steadily in the City. According to data from PKF Consulting, the annual average daily rate for a hotel in Ontario increased 7.7% in 2015 over 2014, and the annual hotel occupancy rate increased 2.8% over the same period. Leisure and hospitality spending continues to grow in the City of Ontario, with taxable receipts up 7.2% from the fourth quarter of 2014 to the fourth quarter of 2015, and this growth can be expected to continue. This is the kind of growth we should expect for the City as the economy continues to grow.

In a move that will also expand Ontario's leisure and hospitality sector, Congress is taking a key step in transferring ownership of Ontario International Airport.³ Recently, the U.S. House of Representatives approved a bill that would expedite the transfer of ownership to local control. With ownership falling into local hands and the Inland Empire's economy rapidly expanding, the Ontario International Airport will be a significant driver of economic growth in the City and region. Airports play a major role in generating economic activities by encouraging commerce and tourism, both of which create jobs and grow the local economy. The City of Ontario stands to benefit from the control, as travelers spend their earnings on hotels, restaurants, flights, and other discretionary spending locally in the City.

In San Bernardino County, as in the rest of the state, relatively low gasoline prices have led to a significant drop in Fuel and Service Stations spending. From the fourth quarter of 2014 to the fourth quarter of 2015, taxable receipts in that category fell 12.7%. Although low gasoline prices can hurt the Fuel and Service Stations sector, the savings to businesses and consumers will help drive spending in other categories, offsetting the decline in taxable receipts associated with gasoline.

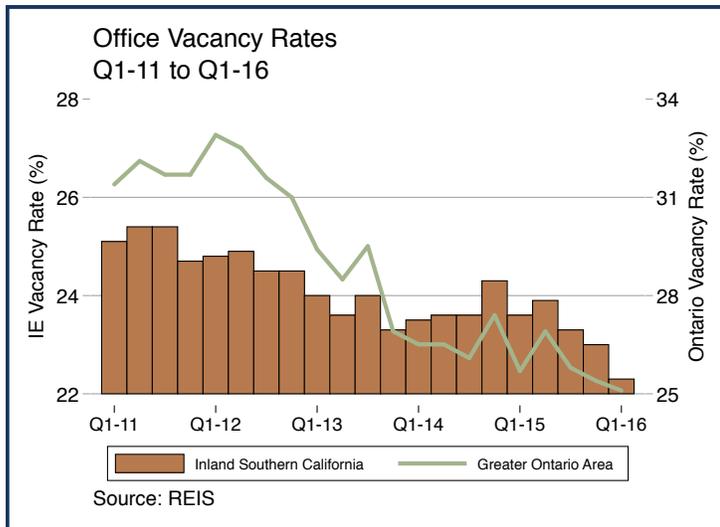
³Congress approves key step in Ontario airport transfer process." *The Daily Bulletin*. June 21, 2016.

Commercial Real Estate

The commercial real estate market in the City of Ontario showed mixed results. Consistent with employment growth across the Professional Services sector, office vacancies continued to decline, falling 0.6 percentage points from the first quarter of 2015 to the first quarter of 2016.

Recently, there has been both bad and good news about the market for warehouse space in the City.

The Bad: After operating for nearly six decades, the California-based Sport Chalet announced it would be closing its doors in April 2016. Sport Chalet has a number of locations in the Inland area, including Chino, Jurupa Valley, Rancho Cucamonga and Riverside. The closure will free retail space in those locations and will also increase the supply of warehouse space because the City of Ontario is home to Sport Chalet's distribution center. A&G Realty Partners, a commercial real estate investment group, is managing the sale of the retail stores, office space, and the distribution center. The company is accepting bids for the distribution center, and an auction is tentatively set for June.⁴



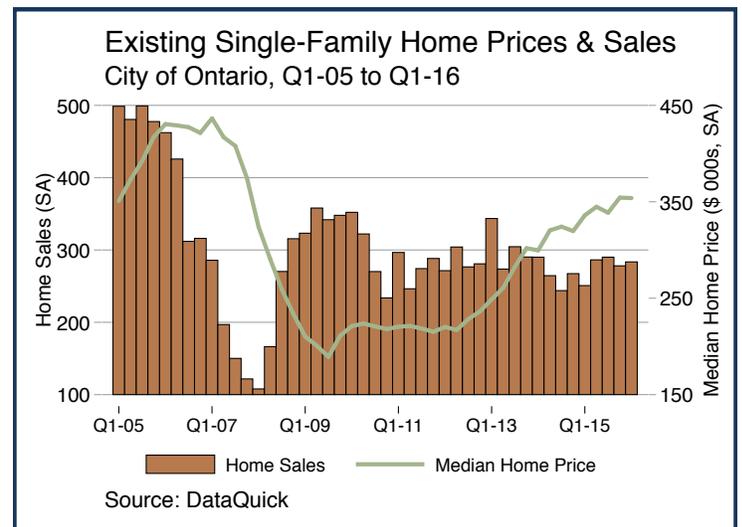
The Good: Ontario is slated to be the future sight of QVC's first West Coast distribution center. Construction of the 1.2-million-square-foot warehouse is underway, and the center is expected to open this summer.⁵

Construction activity in the City is expanding beyond the warehouse and distribution sector. Ontario Mills recently constructed 80,000 square feet of retail space in an area formally occupied by a J.C. Penney outlet store to make space for smaller retail stores.⁶ Ontario's commercial real estate sector should continue to grow this year.

Residential Real Estate

As the coastal cities of California become more expensive, more people are moving inland to take advantage of relatively affordable home prices. From the first quarter of 2015 to the first quarter of this year, the median price for existing single-family homes increased 5.3% to more than \$353,000. With a 13.1% increase in single-family home sales, the City of Ontario is off to a good start for 2016. With the labor market improving in the state overall and with no short-term hurdles to overcome, the demand for single-family housing in the City should remain strong through the year.

Home price appreciation and increased sales are setting the stage for a healthy housing market in the City of Ontario. The number of defaults and foreclosures in the first quarter of 2016 supports this belief, and as defaults and foreclosures continuing to decline, the housing market in the City is gaining strength.



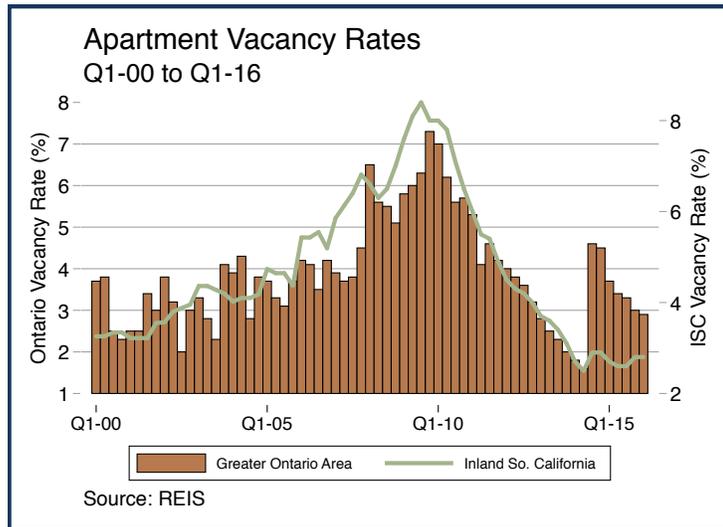
⁴A&G Realty Partners Retained by Sport Chalet, LLC to Manage the Sale of 50 Leases." www.businesswire.com, May 2, 2016.

⁵QVC readies Ontario distribution center for grand opening." *Inland Valley Daily Bulletin*. January 29, 2016.

⁶Get the details on Ontario Mills' new Fashion Alley." *Inland Valley Daily Bulletin*. April 25, 2016.

Ontario’s apartment market remains robust. After a spike in vacancy rates in the third quarter of 2014 because new units were added, apartment vacancy rates have declined, reaching 2.9% in the first quarter of 2016. The increase in demand for apartment rentals over the last year was met by a 2.2% increase in apartment rental rates in the City, which now average \$1,253 a month compared to \$1,226 a year ago.

Moving forward, the outlook for the City’s residential real estate market remains strong. According to recent data from CIRB, the City has permitted nearly 1,000 single-family and multi-family units over the last 24 calendar months. The economies of the City and of Inland Southern California as a whole have improved substantially since the recession. Residential real estate can be expected to reach levels that were observed before the recession, but this time with better underlying fundamentals.



Commuting Patterns and Trends

Located on the southwest edge of San Bernardino County, the City of Ontario is served by several major freeways. Where do the City’s residents travel for work? Not surprisingly, 58% of residents stayed in San Bernardino County—the largest county in the country—in 2014. Roughly one fourth commuted to Los Angeles County. Despite sharing a sizeable border with Riverside County, a slightly larger (but nearly comparable) share of the City’s residents commuted to Orange County than to Riverside County in 2014.

A closer look reveals that the majority of those commuting to Orange County work in Professional Services (26.9%), Manufacturing (15.5%), and Construction (14.2%). Alternatively, residents commuting to Riverside County were

employed primarily in Wholesale Trade (16.4%), Education and Health Services (15.9%), and Construction (12.6%). Residents who commute to Los Angeles County also are heavily employed in Education and Health Services (15.9%) and Manufacturing (14.0%).

Of those who work in San Bernardino County, the largest industry to employ Ontario residents is Education and Health Services (18.6%), which employed 22.0% of San Bernardino’s residents in 2014. The second largest industry employing City residents is Retail Trade (15.9%), which employed 13.0% of San Bernardino’s residents. Why Retail Trade? In 2014, the median earnings for Retail Trade workers were \$22,400 in Orange County and \$20,600 in San Bernardino. Typically, the higher the earnings, the higher chances that residents will be willing to commute.

The largest share of workers who make the long commute to Orange County are employed in Professional Services. Because of the higher cost of living, employers in less affordable areas tend to pay higher wages; this offsets the costs of commuting for residents who cannot afford to live in expensive areas. The median wage in Orange County for Professional services was nearly \$45,000 in 2014. The median wage for the same industry in San Bernardino County was around \$27,300.

Over time, more Ontario residents are finding employment outside of San Bernardino County. In 2005 62.2% of employed City residents worked in San Bernardino County. By 2014, that share fell 4.2 percentage points to 58.0%. Ontario residents are willing to accept longer commutes for both employment prospects and higher wage opportunities. The trade-offs are commute times. From 2010 to 2014, City residents’ mean travel time to work increased 17.7% to 41.3 minutes. Over the same period, the share of residents who worked outside of San Bernardino increased 6.2 percentage points.

By exporting workers, the City of Ontario has benefited immensely. Although the mean travel time to work increased 17.7%, the unemployment rate for City residents declined 8 percentage points from 2010 to 2014 because of both business cycle improvements and a larger share of residents increasing their commutes. Keeping local residents employed, even if outside of the county, has helped them retain and develop important vocational skills during a period when local businesses were scaling back production. As the economic expansion continues, these workers will continue to entice more businesses development in the City of Ontario.



About Beacon Economics

Beacon Economics, LLC is a leading provider of economic research, forecasting, industry analysis, and data services. By delivering independent, rigorous analysis we give our clients the knowledge they need to make the right strategic decisions about investment, growth, revenue, and policy.

Services

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- Industry and market analysis
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