LIFE IN THE VALLEY ECONOMY

SAVING THE MIDDLE CLASS: LESSONS FROM SILICON VALLEY - 2012

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EXECUTIVE SUMMARY

CHAPTER 1: MAKING A LIVING

Silicon Valley is widely hailed as leading the nation in the jobs recovery. But a closer examination of the job situation in Silicon Valley reveals fundamental challenges.

Silicon Valley is indeed roaring back. From July 2011 to July 2012, the region added jobs at one of the fastest rates in the nation. Property values grew substantially in 2011 for the first time in four years. And the top 150 companies in Silicon Valley posted a profit increase of 22%.

Yet unemployment remains at recession-level highs. The modest job growth of the past two years is not on track to make up for the job losses of the previous fifteen. Total unemployment now, even after 24 months of year-over-year gains, has only just come down to the highest level of unemployment experienced by Silicon Valley during the dot-com bust of 2001.

The long-term trend of the employment rate is downward. Even when business profits and GDP grow, jobs do not. In Silicon Valley, economic growth appears to have become decoupled from job growth.

Looking deeper, the disappearance of nearly 100,000 manufacturing jobs has deeply impacted employment opportunities, especially for the half of the population without a college degree. As manufacturing shrinks, it is taking with it the largest source of secure middle-class jobs. In their place, the industry mix in Silicon Valley is shifting towards very high-end jobs in the information sector or low-end jobs in the service sector.

In a demonstration of the basic law of supply and demand, the weak labor market, in which there is not enough employment demand to match the supply of willing workers, has pushed down wages further.

The combination of slack employment, falling wages and rising cost of living has taken a toll on household incomes. At the national level, the median household's inflation-adjusted income has fallen by 6 percent since 2000 – its worst performance since the Great Depression. Economists have declared the 2000s to be a "lost decade" for middle class incomes.

In Silicon Valley, this trend is magnified. From 2000 to 2010, real median household income in the Valley has fallen by 19% - more than three times the national decline.

It's not that the region has stopped producing wealth. Total personal income flowing into Silicon Valley increased, as did per capita earnings for workers. But a disproportionate share of this growth is flowing to a small segment of highly compensated individuals – leaving the majority of working families struggling to get by on reduced incomes. In total, households in the secure middle class ($50,000 to $199,999) dropped from 62% of all households in 2000 to 55% of all households in 2010.

These distributional changes suggest that Silicon

KEY FINDINGS

Stagnant Employment: Silicon Valley has not added any net new jobs in 16 years.

Falling Incomes: Since 2000, the median household in Santa Clara County has seen its real income fall by 19.5%. African American and Latino households lost the most: their real incomes dropped 29%.

Widespread Low Wages: An estimated 31% of jobs in Silicon Valley pay $16/hr or less. Even with two working parents, this wage is not enough to meet the basic standard for family self-sufficiency.

Widening Inequality: From 2000 to 2010, the portion of Silicon Valley households in the secure middle class dropped from 62% to 55%, while the number of households making less than $10,000 more than doubled.

Cost of Living Increases: Between 2000 and 2011, the cost of every major household expense category increased faster than wages. The biggest average increases in Bay Area households' spending went to health care and retirement; for the first time, the average household is spending more on retirement contributions than on food and drink.

Income Insufficiency: As of 2010, one out of every three households (33.5%) in Santa Clara County fell below the self-sufficiency standard, meaning their income is too low to meet a basic standard of living. The number of families struggling to make ends meet has increased considerably since 2000, when one out of every four households (24.1%) was below self-sufficiency.

Valley may be progressing even past the so-called hourglass economy to a “Victorian gown economy”. Whereas in the hourglass economy of the 1990s, the Valley saw a shrinking middle class with some middle class families falling down and others rising up, the real income distribution trend is now shaped less like an hourglass and more like an old-fashioned Victorian gown: small on the top, squeezed ever tighter in the middle, and ballooning out at the bottom.

All these forces combined are producing a region where, despite a rising GDP, more and more families must struggle daily just to put food on the table and pay the rent. In Santa Clara County, one-third of all households are now living below the self-sufficiency standard, a basic indicator of economic well-being which measures a family’s ability to provide for its own basic needs without deprivation and without relying on public assistance or charity. This unconscionably high number signals that financial insecurity has now become mainstream.

As the ranks of struggling families swell with formerly middle-class households, the inability of so many to make ends meet overburdens the safety net and strains the social fabric.

CHAPTER 2: SEEKING SECURITY

If income inequality is a widening gap, wealth inequality is a chasm. The top 1% own 35% of all wealth in the United States, while the bottom 25% don’t own – they owe. 2010 marked the highest negative net wealth on record for the bottom quartile of U.S. households, who owed an average of $12,800 more than they were worth.

This long-term and large-scale transfer of wealth is one component of a larger trend of increasing insecurity for the American middle class – what economist Jacob Hacker calls “the great risk shift.”

Over the past three decades, a transformation of the nature of work in the United States, coupled with changes in public policy, has resulted in a dramatic transfer of risk: away from corporations and other large-scale institutions, and onto individual families. Today, the middle class walks a tightrope of insecure jobs, unreliable incomes, inaccessible health insurance, and increasing debt, with worrisome prospects for the immediate future, let alone for retirement.

Silicon Valley is at the epicenter of this trend. Even before the Great Recession, the Silicon Valley economy had ceased to provide financial security for the typical working family. From 2006 to 2008, foreclosure activity in Santa Clara County jumped 513% and bankruptcy filings nearly quadrupled. Yet these clear signs of a crisis failed to provoke a sufficiently strong public policy response. Now we are seeing the results. The steady rise of homeownership, long viewed as a symbol of rising middle-class prosperity, is being reversed. Over the last decade, the share of Americans who own their homes declined. And Silicon Valley is at the forefront: homeownership fell twice as fast here as it did nationwide.

Adding to the hardships created by an insecure job market and high unemployment is the fact that the nature of unemployment has dramatically changed as well. Where being unemployed for more than 6 months was once so rare that state unemployment insurance does not allow for it, long-term unemployment is fast becoming the norm. The portion of unemployed Californians who have been out of work for more than 6 months is growing explosively and by the end of 2011 was up to 46% - fast approaching half of all jobless workers.

Long-term unemployment at these levels represents a new paradigm – one in which laid-off workers do not face a job search of a few weeks or months, but must be prepared to endure a prolonged jobless spell of half a year to several years. The United States’ workforce system was built upon the assumption that laid-off workers who put effort into their job search could quickly find work. Neither traditional unemployment insurance, nor job search services designed to assist unemployed workers, nor retraining programs are designed to deal with so many workers facing such stubborn and prolonged unemployment.

The federal extension of unemployment insurance has enabled millions of jobless workers to access extended unemployment benefits. However, the current federal program providing extended benefits to the long-term unemployed is set to expire on January 2, 2013. If federal unemployment disappears, half of all California workers currently receiving unemployment may find themselves with no source of income.

Even these extremely high rates of long-term unemployment do not show the whole picture.

Hundreds of thousands of Silicon Valley workers are underemployed – a category which includes those who have been forced to take part-time work because there are no full-time jobs available, as well as "discouraged workers" who, finding no jobs available at all, have given up actively searching. Underemployment in Silicon Valley has grown three times as fast as unemployment and is now 60 percent higher than the national underemployment rate.

While essential, work alone does not guarantee security. The ranks of the working poor – those who have a job so low-paying that their household income remains below 200% of the federal poverty line – are growing in Silicon Valley and nationally. In 2010, 151,932 Santa Clara County workers were classified as working poor, representing 16.2% of the workforce.

Among all industries in Silicon Valley, manufacturing workers are least likely to be among the working poor. This makes manufacturing particularly important for sustaining a strong middle class, as it offers living-wage jobs accessible to the half of Silicon Valley's population that does not have a college degree.

But Silicon Valley has lost nearly a hundred thousand manufacturing jobs since 2000. Reducing the ranks of the working poor will require a two-pronged approach: lifting up wages in low-wage sectors such as hospitality and reinvigorating the growth of middle-class jobs in manufacturing.

SEEKING SECURITY: KEY FINDINGS

Homeowners Absorb Major Losses: Home values in Silicon Valley have fallen by 25% since 2007. Homeowners in the lowest-priced tier of housing have lost the most value on their homes, while owners of million-dollar homes emerged largely unscathed.

Foreclosure Rate Declining: The pace of foreclosures has slowed considerably over the past two years, but foreclosure activity in Silicon Valley remains three times higher than the pre-crash baseline.

Homeownership Drops: The homeownership rate in Silicon Valley not only declined in the last decade, but fell twice as fast as the national rate. Silicon Valley now has a lower homeownership rate than the U.S.: 57.6% vs. 65.1%.

Household Wealth Lost: Real net worth of the median U.S. household plunged 39% in 2010, erasing all gains since 1989.

Underemployment Reaches Historic High: Since 2007, underemployment in the San Jose region has grown nearly three times as fast as unemployment. By 2011, one out of every four workers (25.6%) was unemployed or underemployed, well above the national figure of 15.9%.

Food Stamps Provide a Safety Net: Due to state cuts and federal restrictions, CalWORKs has failed to serve as a safety net in the recession; 81 thousand Santa Clara County residents are depending on food stamps only, as food stamps use has grown 114% from 2008 to 2012.

CHAPTER 3: STAYING HEALTHY

The County of Santa Clara has consistently emphasized residents' health as one of its top priorities, developing innovative models of improving health insurance coverage, health care access, healthy living environments, and health outcomes. These efforts have borne fruit. In study after study, Santa Clara County consistently ranks near the top in residents' health and well-being. Over the last decade, San Jose residents enjoyed the highest life expectancy of any major U.S. city.

The pioneering Santa Clara County Children's Health Initiative (CHI), launched in 2001, has contributed considerably to this success. CHI has helped parents apply for health coverage for more than 210,625 children throughout its ten years of operation, achieving the highest rate of children's health coverage among California's 58 counties. The model created by CHI has been replicated in 30 counties and provided an important push for state and national health care reform.

Yet Silicon Valley has not been immune to the growing challenges of the U.S. health system, chief among them its outsized costs. Rising premiums, co-pays, and other medical expenses are all impacting working families' budgets as well as business' bottom lines.

When the Great Recession hit in 2008, many employers responded by laying off workers, or – for those workers who kept their jobs – discontinuing the provision of employment-based health coverage. This additional drop came on the heels of a decade-plus trend of declining employer-based health coverage.

Across the United States and California, millions of workers and their families were thrown off of health insurance. In addition to health effects, the loss of insurance had major financial impacts. Medical debt – one of the leading causes of bankruptcy – soared among Californians. From 2007 to 2009, the number of Californians with medical debt grew by 400,000, up to 2.6 million.

In Silicon Valley, the Children's Health Initiative provided a safety net for kids whose parents lost health coverage; for adults, however, far fewer options were available. By 2010, 17.0% of Santa Clara County adults had no health insurance, up from 14.6% in 2008.

Implementation of the Affordable Care Act, the federal health care reform passed into law in 2009, is expected to considerably improve access to treatment and health outcomes. The ACA includes a number of significant insurance market reforms that will help reduce health care costs for individuals and employers, thereby increasing economic competitiveness of U.S. workers and businesses.

Beginning in 2014, additional provisions of the ACA will greatly expand health insurance coverage. Nine out of ten non-elderly Californians are expected to have health insurance once the ACA coverage expansion takes place. In Santa Clara County, a projected 110,000 uninsured residents will gain coverage.

The Affordable Care Act offers both an opportunity and a challenge for Santa Clara County. The public health care system and associated safety net providers will play a critical role in helping uninsured, low-income, and underserved populations to benefit from the advantages offered by the Affordable Care Act.

Just because health reform expands the eligibility for programs does not mean people will actually enroll in those programs. Enrollment requires strategies to actively inform people of benefits and a system to get through what are often complex administrative procedures. Reaching these underserved populations to enroll in newly available health coverage and take advantage of preventative health services will be a key strategic goal for the health care safety net system in the next several years.

STAYING HEALTHY: KEY FINDINGS

Children's Health Initiative is Succeeding: As of 2010, 94.4 percent of Santa Clara County children are insured – the highest rate among California's 58 counties. Public health insurance covered 153,000 children in 2011, up from 67,000 in 2000.

Adult Health Coverage Declines: The portion of Santa Clara County adults without any health coverage grew from 14.6% in 2008 to 17% in 2010. Low-income and non-white adults are the least likely to have health insurance.

Health Care Reform Will Improve Coverage: Up to 110,000 uninsured residents of Santa Clara County are expected to gain coverage in 2014 as new provisions of the Affordable Care Act come into effect.

Health Care Costs Continue to Rise: Over the last decade, the cost to workers in California for job-based health insurance premiums has grown by 147%.

Progress Made Against Childhood Obesity: Overweight/obesity among pre-teens in Santa Clara County declined from 32% in 2000-01 to 26% in 2010-11. However, Latino children are the most impacted by obesity and have seen the least progress; 39% of Latino pre-teens were overweight or obese in 2010-11, virtually unchanged from 40% in 2000-01.

Public Health Care System Provides a Safety Net: Santa Clara Valley Medical Center, the anchor institution of Silicon Valley's public health care system, saw the number of uninsured or self-pay patients it served jump by 55% in the Great Recession. At the same time, the number of insured patients declined by 40%.

CHAPTER 4: BUILDING A COMMUNITY

The collapse of the housing bubble in 2007-08 wreaked havoc on the national and local economy – and on the lives of millions of families. In Santa Clara and adjoining Bay Area counties, between 2007 and 2011, homeowners collectively lost $387 billion in home equity, a loss equivalent to the entire market value of Google, eBay and Cisco combined.

This loss of assets led to a massive drop-off in consumer spending as families have had to grapple with tens or hundreds of thousands of dollars in vanished wealth, or worse, with the loss of their home and decimation of their credit. Homeownership among Silicon Valley households is now lower than at the start of the century.

Families who do not own their homes are faced with an increasingly tight rental market. The average monthly rent in Santa Clara County now stands at $1,961, rivaling the all-time high of $1,935 set at the end of 2000. Forbes magazine recently ranked San Jose as one of the worst places in the country to be a renter, behind only New York City, Minneapolis and San Francisco.

Among both renters and owners, nearly half of all Santa Clara County households are living in housing considered unaffordable for their income. This excessive housing cost burden impacts the local economy in two ways.

In the short term, families putting most of the income towards rent or a mortgage have less income remaining to spend on other goods and services – spending which is more likely to go to local businesses and circulate in the local economy.

In the longer term, the lack of reasonably priced housing may drive away the workforce that is needed to sustain and grow Silicon Valley businesses. Affordable workforce housing has long been a top concern of the high-tech industry in Silicon Valley, which sees housing as a critical element in attracting and keeping the talent they need. The return of growth in the tech sector has brought with it the reemergence of the affordable housing challenge.

Adding to this challenge is the loss of tools that communities had used to increase the stock of affordable housing. As of 2012, the state of California has eliminated all local redevelopment agencies, which had been a primary source of local funding for affordable housing. Inclusionary housing ordinances, designed to include a portion of affordable units in market-rate housing development, were another promising local tool; however, two court decisions have struck down inclusionary ordinances for both rental housing and owner-occupied housing respectively. Silicon Valley urgently needs to find or build new tools to encourage production of adequate and affordable housing.

Closely linked to the lack of housing are transportation challenges. Workers in Silicon Valley who cannot afford nearby housing are forced to commute long distances, generally by car.

Silicon Valley faces considerable transportation challenges which cost residents time and money and may become a drag on job growth. Freeways remain congested and are likely to grow worse as the region's population grows. The public transit

BUILDING A COMMUNITY: KEY FINDINGS

Housing Market Shows Signs of Life: After nearly 5 years of a depressed housing market, 2012 brought tentative signs that the housing market appears to have hit bottom. In the first 6 months of the year, home sales grew by 12.4% and the median sales price was up 7% over the prior year.

Rental Housing Costs Soar: Rent increases in the San Jose region were the highest in the nation, at 11.7% for 2011. In 2012 rents are on pace to grow even faster; from January through June, the average rent has already grown by 10%, to an all-time high of $1,961.

Highways Remain Congested: Nearly a quarter (23%) of freeway miles in Santa Clara County were severely congested in 2011, with little change from prior years.

Transit Revenues Recovering: VTA operating revenue has bounced back from the recession and is projected to grow 7.4% in 2011-12.

Bus Service Not Yet Restored: VTA added service hours for both bus and light rail in 2011-12; however, following years of severe cuts, bus service remains at its lowest level in a quarter-century.

Crime Rates Up: Both burglaries and homicides have spiked in 2012 and are on track to reverse a four-year trend of lower crime.

system is underdeveloped compared to other major metro areas and has undergone severe cuts to basic bus service. Forthcoming expansions of the transit system, including the implementation of Bus Rapid Transit and extending the BART regional rail system into San Jose, may help move us towards solving the Valley's transportation dilemma, but only if reliable funding is found to maintain both local and regional levels of transit service.

The availability of transit and other alternative transportation options also carries environmental implications, as automobile travel continues to play a major role in greenhouse gas emissions contributing to climate change.

A third frequently cited indicator of a community's quality of life is the crime rate. Until recently, public safety in Santa Clara County appeared to be on a positive trend. Violent and property crime rates, as well as domestic violence-related calls for assistance and substantiated cases of child abuse, all fell dramatically between 2006 and 2009. But in 2011-12, although final data is not yet available, all of these indicators appear to have reversed direction and be headed back upwards.

One driver of this reversal of fortune may be broad cuts in public and community services. The City of San Jose has considerably reduced its police force, and other cities have undergone similar, though less dramatic cuts. Community programs that strengthen families and neighborhoods have also suffered cutbacks. Notably, San Jose's nationally lauded Strong Neighborhoods Initiative was shuttered in June 2012 when the state of California dissolved all local redevelopment agencies .

While crime rates remain low relative to other major metropolitan areas, the upsurge is impacting quality of life in Silicon Valley. In 2010 and 2011, San Jose was ranked the 4th safest city of its size, a letdown from earlier years when the city touted its #1 status as the "safest big city in America."

CHAPTER 5: PURSUING THE DREAM

Education is one of the most important predictors of economic success for workers and their families. As the state's economy grows and changes, demand has grown for not just a highly educated workforce, but a workforce with very specific and rapidly changing skills. However, the state and local educational systems lack adequate resources to make higher education accessible, and those resources that do exist are often not targeted to support the students who most need them.

New, more accurate student tracking has revealed that 20% of Silicon Valley high school students drop out before graduating. Although this is better than the state average, the fact that one of every five students in the county does not graduate is a community-wide challenge.

Multiple years of state budget cuts have left the already under-resourced school system with wholly inadequate funding to meet the challenges of preparing the current generation of children to work and live in today's economy. Between 2007-08 and 2010-11, core state funding for K-12 schools was cut by $3.6 billion, or $530 per student for every student throughout the state. Statewide, the total number of teachers in classrooms fell by 11 percent, a loss of 32,000 teachers. California now ranks dead last among all states in student-to-teacher ratios.

These cuts were not distributed evenly. The complex formulas characterizing the current K-12 finance system resulted in widely varying losses by district. Within Santa Clara County, East Side Union High School District suffered the greatest per-student drop in general purpose funding, a loss of $614 per student – totaling a $15.3 million cut for the district.

And the cuts continue. In 2010-11, the state reduced K-12 funding by an additional $7 billion. Moreover, the 2012-13 budget includes 'trigger cuts' that will take effect January 2, 2013 if voters do not approve a November 2012 ballot measure intended to raise revenue for state services. Eighty percent of the impact would fall on K-12 schools. If these cuts take effect, schools will lose another $4.8 billion and will be authorized to shorten the school year by 15 days.

The public higher educational system has been similarly battered by cuts. Multiple years of cumulative funding reductions have resulted in higher tuitions and fewer available spots at California's public institutions of higher education.

In the past ten years, the cost of a year at a California State University has more than tripled, increasing by 218%, while the cost for the University of California has nearly quadrupled (up 296%) and is now among the highest in the nation for a public university system.

In addition to tuition increases, state budget cuts for higher education have led a number of campuses to place caps on enrollment. In Silicon Valley, San Jose State University was forced this spring to end its promise of local guaranteed admission. For the first time, Santa Clara County high school graduates who meet all of the qualifications to attend San Jose State will no longer be guaranteed a spot.

The ongoing financial assault on California's public higher education system – once considered the best in the world – is threatening to eliminate access to higher education for large portions of today's students.

If this trend is not quickly reversed, its economic impacts will be felt for decades to come. Not only will today's students shut out of college be more likely to struggle financially throughout their lives, but lower levels of education among the next generation would present a significant barrier to the Valley's future as a world capital of innovation.

An under-resourced educational system short-changes our children and youth, and will ultimately result in a shortage of highly skilled workers. In a high-tech region whose driving industries are dependent on an educated workforce, Silicon Valley is producing a generation of students whose academic achievements are inadequate to sustain healthy economic growth.

At the same time, a drive to improve educational access should be accompanied by and focused through the lens of quality job creation. Education is critical to economic success, but education alone is not enough; in order to lead to middle class careers and restore economic prosperity, it must be combined with a strategy to create good jobs.

PURSUING THE DREAM: KEY FINDINGS

Wide Ethnic Disparities Persist in College Preparedness: Among Santa Clara County's high school seniors, 46% are prepared for a four-year college, exceeding the state average. However, the college preparedness rate is only 17% for Latinos, 23% for African-Americans, and 25% for Pacific Islanders.

College-Going Rate Rebounds, But Is Still at Historic Low: The college- going rate for high school graduates in Santa Clara County rebounded from its historic low of 36% in 2008, up to 48% in 2010. Even with this upswing, fewer Santa Clara County high school graduates are going on to college than at any time from 1991 to 2007.

Budget Cuts Impact K-12 Schools: Per-student spending in Silicon Valley's schools has fallen for two consecutive years and is now 20% below the state average. The region's wealthiest school district spends $5,745 more per student than the poorest district.

Cost of College Soars: Since the start of the Great Recession, the cost of attending a CSU college has almost doubled; the cost of attending a UC has jumped 71%; and the cost of community college has grown 130%.

Silicon Valley Residents are Highly Educated: The average educational level in Santa Clara increased substantially over the decade; Silicon Valley residents are twice as likely as the state or national average to hold an advanced degree. Yet wide disparities remain; 61% of Latino adults and 43% of Vietnamese adults have never attended college.

Value of a College Degree: Santa Clara County workers with a bachelor's degree earn two-and-a-half times as much as workers with only a high school diploma. This wage gap is the largest in the nation.