PROPERTIES

March 2, 2009

Mr. Andrew Crabtree
Principal Planner
City of San Jose
200 East Santa Clara Street
San Jose, CA 95113

Dear Mr. Crabtree,

Beacon Economics recently prepared its report entitled *"The Future of Housing Demand in San Jose: 2008-2040."* The forecast predicts a rapid aging of our population. If we allow these predictions to come to fruition, the forecast will have dire consequences for the City and our local economy. Our responsibility to ensure that the City's land use promotes economic growth should not be underestimated. Economic growth must become a top priority of our general plan. Attracting and retaining young, highly educated workers to replace the baby boomers is the key.

Without major changes in our approach to land use and public policy aimed at accomplishing this task, San Jose residents, its local government and its driving industries will feel the effects for decades. Maintaining financial stability and a desirable quality of life will become impossible if we are unable to provide our driving industries with enough workers. A higher proportion of older residents will force our driving industries to locate jobs elsewhere in search of global talent and place an enormous financial burden on already stressed City services and budgets.

California and San Jose, in particular, have relied on a steady supply of college graduates for decades in order to propel the economic base and achieve some of the highest living standards in the world. Over the next decade, however, the aging of the baby boomers will result in a massive brain drain and new jobs will require even more skilled workers. According to Joint Venture Silicon Valley Index 2008, last year marked the first year in which baby boomers could retire and collect Social Security. The U.S. Department of Labor's data shows that 25 million workers will retire in the next ten years and an even larger number will leave the workforce in the following decade. In California, three million workers will retire by 2018, and the number of retirees in Silicon Valley will be close to 300,000. The San Francisco-based Public Policy Institute of California predicts that the state needs almost 160,000 more college graduates a year through 2025 to meet future demands for highly skilled labor. The PPIC also forecasts that by 2025 two in five jobs will require a college degree, up from 31-32% now.

Domestic migration trends, an inability to attract college graduates from other states and restrictions on immigration will make replacing these workers extremely difficult. The PPIC's report, *Can California Import Enough College Graduates to Meet Workforce Needs?,* states "it is clear that since the 1970s, there has been a sharp decline in the share of California's college graduates who were born in other states." Domestic outmigration, or those leaving the region to other markets, accelerated after the dotcom crash in 2000 and finally reversed course in 2005. From 2000 through 2004, Economy.com reported that the San Jose MSA lost approximately 74,000 residents. An inability to attract out-of-state college graduates and the effects of domestic outmigration would have been a much larger problem if it weren't for highly educated foreign born immigrants. Russian, Indian and Chinese scientists and engineers have become the new innovative class in Silicon Valley. However, foreign immigration alone the will not replace the void left by the baby boomers either. Changing immigration policy by expanding programs such as the H1-B visa has been extremely difficult and probably won't happen in the current economic climate.

> ***"Companies that do not plan for this aging workforce may find themselves suddenly faced with a loss of labor, experience and expertise that will be difficult to offset, given the relatively small pool of new workers and the competition for new talent likely to result from so many companies facing the same problem." –Inc Magazine***

To meet this challenge, we need to attract and retain college graduates domestically and internationally at unprecedented rates and to reverse domestic outmigration trends. Andy Grove, the former CEO of Intel, wrote a book entitled *"Only the Paranoid Survive: How to Exploit the Crisis Point That Face Every Company."* Mr. Grove's premise can also apply to our task at hand. The demographic trends we face represent a strategic inflection point for the City and for the General Plan Task Force. We can address the coming labor shortage crisis now and gain a competitive advantage in the global economy or we can turn away from the challenge and accept the trends forecast by Beacon Economics and Stephen Levy, director and senior economist of the Center for Continuing Study of the California Economy.

The General Plan Task Force can help attract and retain the pool of new workers required by our companies by adopting an aggressive housing growth scenario. In *Can California Import Enough College Graduates to Meet Workforce Needs?,* the authors note that one of the largest barriers to attracting and retaining the global talent necessary to propel our driving industries and create jobs is the cost of housing. The problem is even more pronounced in San Jose. Although home prices have dropped significantly and affordability rates have improved due to the current economic climate, San Jose's home prices are a major deterrent for our young people especially when compared to other markets. While San Jose has some of the highest incomes, its home prices and the associated cost of living are cause for alarm. The crisis becomes very clear when you analyze the median home price to income multiplier. According to Claritas, the median income in San Jose was approximately $85,000 per year in 2008. In Q3 2008, the median home price in the San Jose MSA was approximately $650,000 according to the National Association of Realtors. Therefore, the home price to income multiplier for San Jose was 7.6 times. The multipliers for Seattle, Austin and Portland are 5.7, 3.4 and 5.0 respectively. At Q3 2008 levels, median incomes in San Jose would need to rise to over $250,000 to compete with Austin, $130,000 to vie with Portland and $114,000 to rival Seattle.

More affordable home prices in other markets are a major competitive advantage for employers looking to relocate or expand operations and a welcome benefit for those college graduates looking to stay close after graduation. Job growth in our community has been negatively impacted by the cost of housing for almost a decade. From 2000-2007, job growth rates in San Jose have been some of the lowest in the Western United States. We've never fully recovered from the technology correction in 2001 and we won't unless we change course.

The General Plan Task Force can aggressively promote housing and minimize the impact on City services. In *Toward the Future: Jobs, Land Use and Fiscal Issues in San Jose's Key Employment Areas 2000-2020 ("Toward the Future")*, the authors conclude that, while the preservation of industrial lands is important to the City's long-term economic development, the City must continue to develop new housing in a variety of settings. Certain areas within the City are appropriate for residential use and conversion. *Towards the Future* points out that the financial impact of new development can vary significantly from area to area within the City and how with proper planning and the right mixture of services, the City can reduce the financial impact of new housing. One of the best opportunities to mitigate the increase in services is by locating new housing development in close proximity to employment and transit centers.

Since high density housing is generally more expensive to construct, one way to promote housing in these areas is to create incentive zones. Incentive zones for housing near employment and transit centers will stimulate housing production in designated areas, help the City achieve its goals of reducing greenhouse gas emissions and promote public transit. Achieving operational efficiencies for public transit is dependent on increased ridership. We can markedly improve ridership through densification along transit corridors for BART and LRT. Demonstrating a land use strategy that encourages transit oriented development now is vital in attracting Federal and State funding for construction and expansion of these initiatives. Waiving impact fees, accelerating processing, providing density bonuses and reducing parking requirements are some of the many ways to create incentives and improve affordability.

The general plan update also gives us an opportunity to address the types of housing young workers will demand and that's critical to making sure we can hit our housing goals. A recent USA Today article noted that 57% of urban dwellers younger than 30 say that the City is where they wanted to live. The homebuyer of the future will demand the lock and leave lifestyle often associated with higher density development. Most won't have children and will have pets. They'll seek and develop a sense community from the distinct neighborhoods where they choose to live. Sometimes referred to as "Digerati" in Silicon Valley speak, these are recent grads from Stanford, UC Berkeley, Santa Clara University and San Jose State who leave Silicon Valley to live in San Francisco or other dynamic technology centers after graduation. We can look at areas like the Mission District in San Francisco and the Pearl District in Portland, Oregon for inspiration in our planning efforts and identify areas where we can provide housing to meet this future demand. General Plan Task Force members, city leaders and staff must carefully balance the myriad of neighborhood interests and the City's economic interests. We must make sure the General Plan creates opportunities to develop neighborhoods that provide live, work and entertainment opportunities for our college graduates. The urban renaissance in San Jose is in its infancy and needs leadership to usher in a new future.

The economic impact of new housing construction shouldn't be underestimated either. The current economic crisis started with housing and probably won't recover until housing stabilizes. The drop in housing construction has had major adverse impacts on Federal, State and local budgets. In light of the current crisis, I think it would be fair to challenge the conventional wisdom by stating that housing does pay for itself. The CBIA estimates that California lost $46 billion in economic output and over 287,000 jobs since home production peaked in 2005. New home construction and impact fees are critical to building the amenities we all want to maintain our quality of life. Parks and trails, open space, transportation improvements and schools are dependent on new home construction. By aggressively promoting new home construction in areas like Downtown and Midtown, we could provide the funding necessary to complete projects like the Guadalupe River Park and Trail. Building 10,000 residential units in Downtown and 5,000 in Midtown would result in $268,500,000 (15,000 X $17,900 per multifamily unit) in revenue via in-lieu park fees. The Guadalupe River Park and Trail has the potential to be our Central Park and would be a direct beneficiary of an aggressive housing growth strategy.

While the availability of employment lands in San Jose may be an important consideration for the General Plan Task Force, the opportunity cost must be carefully considered. Net absorption for existing office and industrial properties has remained weak for a decade. The San Jose Business Journal recently reported that office vacancy rates may exceed 27% in the current downturn and rents may drop by as much as 25%. Demand for employment lands in North San Jose, Edenvale, Evergreen and Coyote has also been virtually non-existent. Why have we been so slow in absorbing our available land? Demand profiles for land are changing. First, we live in a knowledge based economy and manufacturing is becoming a smaller percentage of our base. We may continue to manufacture first generation products here, but mass production will continue to be done overseas. Second, companies are becoming more efficient in their space planning. Companies can use a fraction of the space they traditionally used by employing practices such as hoteling. I recently talked with a real estate consultant for a major professional services firm. The firm has been able to reduce its space requirements from 285 square feet to 125 square feet per person, a 56% decrease. Third, knowledge workers can be "warehoused" in much denser buildings. Floor area ratios have been intensifying and the trend will continue. More companies will require 5-6 story R&D buildings like Brocade at North First rather than the 1-2 story building constructed in the 1970s, 80s and 90s. Last, and most importantly, we're not growing.

Based on the February 23, 2009 task force meeting, it appears that all stakeholders in this process want job growth. Pat Dando from the Silicon Valley Chamber requested that the task force look at factors affecting job growth. This is extremely important, but I think you'll find that the answer is fairly complicated and involves a myriad of variables including educational attainment, immigration, venture capital funding, new technological breakthroughs, healthy capital markets, opportunities for personal networks and a culture of risk taking among others. Local professors like Annalee Saxenian, author of *"The New Argonauts: Regional Advantage in a Global Economy"* and *"Regional Advantage: Culture and*

Competition in Silicon Valley and Route 128," have studied this issue extensively. The good news is that the task force is only charged with the responsibility of understanding how land use affects job growth. Even if you can't accept my argument that housing is critical to job growth, I think the correlation becomes clear by looking directly to our local CEOs. Our CEOs make decisions to employ or not employ people every day by choosing to locate a quality assurance facility in Bucharest, to close a manufacturing facility in Sunnyvale or open a chip plant in Vietnam. CEOs in this Valley consistently cite three reasons for not expanding job opportunities right here in Silicon Valley that relate to land use: the availability of talent, transportation and the cost of housing.

Our competitive advantage is our people. Future job growth will be directly correlated with our ability to lower the cost of housing and to provide housing in areas of the City where young, college educated workers want to live. Employment centers and transit corridors offer compelling areas for growth within the City. Promoting housing in these areas will mitigate the impact on City services, reduce our carbon footprint and improve public transit's operational efficiencies. We must realize that we cannot grow our economic base and maintain our quality of life without increasing the supply of housing for our young people. It's time to set a new course for our local economy in San Jose. Failure to alter our way of doing business now will have dire consequences for future generations. Our economic competitiveness, financial stability and quality of life are at stake.

Sincerely,

Shawn A. Milligan
Vice President

Attachment

In addition to land use, public policy will be critical in attracting and retaining young workers in the region. Public policy must make sure that college students that graduate here must have the opportunity to stay here. We must also increase the pool of college educated workers and skilled labor through education and immigration reform.

- Many college graduates here in Silicon Valley receive high starting salaries, but lack the down payment necessary to buy a home. As a result, many recent grads leave to other lower cost regions. The City should look at expanding its Housing Trust Fund by identifying a permanent funding source. All college graduates that work for local employers should be eligible for assistance. An expanded Housing Trust Fund could also be used to provide rental vouchers and rental credit enhancements for those hurt by the current financial crisis. One approach for permanent funding might be a parcel tax. Many politicians have been reluctant to rely on these taxes because of the required supermajority. However, State Senator Joe Simitian is currently proposing legislation to make parcel tax passage easier. Senate Constitutional Amendment 6 would reduce the margin necessary for passage from 66.67% to 55%.

- We need to improve our elementary and secondary education system and ensure that our workers have the skills to compete in the digital economy. The City should view education as its primary tool in pursuing economic development. High school graduation rates are abysmal and need to improve dramatically. Joint Venture Silicon Valley Index 2008 reported that every district reported drops in graduation rates and the number of UC/CSU qualified students also fell slightly. Joint Venture Silicon Valley's Index for 2008 sums it up best... "The future success of the region's young people in a knowledge-based economy will be determined largely by how well elementary and secondary education in Silicon Valley prepares its students for higher levels of education."

- We need to develop a world-class network of technical and trade schools. I recently obtained a bid for solar panels on my house from a major regional installer. The sales rep told me that they had a backlog of 1,000 installations and couldn't find enough qualified workers to perform the work. The Company was actually going to local city colleges to recruit employees and train them. Increased residential development will also require a qualified pool of electricians, plumbers and carpenters.

- The City needs to take a leadership role in lifting restrictions on immigration for those skilled in science, technology, engineering and math. Many will use the current economic climate to question the necessity of expanding the H1-B visa, but the H1-B visa is critical to our long-term economic competitiveness. In 2007, Bill Gates, the founder and former Chairman of Microsoft, stated in Congressional testimony that "we need to attract and retain the brightest, most talented people from around the world. This will not happen until we reform our immigration policies for highly skilled workers. America should be doing all it can to attract the world's best and brightest. Instead, we are shutting them out and discouraging those already here from staying and contributing to our economic prosperity."