

# The Kiplinger Letter

FORECASTS FOR EXECUTIVES AND INVESTORS

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Dear Client:

Washington, Sept. 26, 2014

With Calif.'s drought threatening to persist... likely through next year, and possibly even longer...

The effects will be widespread: Rising prices for certain foods. New costs and opportunities for firms in the Golden State and beyond. And big investment in new infrastructure, to withstand the next dry spell.

**DROUGHT** Reservoirs and aquifers are sorely depleted and continue to shrink after three dry years. Though a wet winter would certainly help the cause, it still wouldn't be nearly enough to boost water tables. It would take several seasons of rain to refill supplies, and by the looks of things, that's not in the cards. So...

Billions will be spent to save and store water across Calif. A \$7.5-billion bond likely to get OK'd by voters this Nov. will serve as the down payment.

Among coming efforts: Artificial wetlands, to absorb rainfall and funnel the water underground. New pipelines to channel storm runoff into reservoirs. Filtration and treatment plants, to recycle wastewater and pull pollutants from contaminated groundwater. Possibly desalination. And more low-flow plumbing.

Most of the strategies for coping with drought will take years to pay off.

Water customers and taxpayers can expect to foot the bill, of course.

There will be higher rates and surcharges to pay for needed infrastructure, but subsidies, too...for firms and homeowners installing water conservation gear. Sacramento will use some of the money raised by the bond issue for the subsidies.

Legal limits on pumping groundwater are coming, too. Local water districts are under state orders to conserve groundwater or the state will do it for them.

Meanwhile, scores of businesses will feel the pinch from drought.

Hardest hit: Agriculture. Calif. will remain as the U.S.'s top farm state. But, farmers will cut back on some lower-value crops that use a lot of water...rice, alfalfa, tomatoes, spinach, broccoli, etc...so consumers of such items can expect to pay more. But less impact on higher-value, long-term investments in orchards and vineyards.

Calif.'s loss could be a gain for rival farm states not suffering from drought.

Other industries sure to experience a toll: Energy. Hydroelectric power generated in Calif. won't return to its normal capacity until reservoirs fill up again.

Tourism. Ski resorts will find it harder to tap water to create man-made snow to make up for a lack of real snow. Summer tourists face more threats from wildfires.

Grounds maintenance. Expansive grass lawns will disappear in many places as golf course owners and others turn to hardier native plants wherever possible.

All told, a continuing headwind for the vast Calif. economy. The challenges of making do with less water will tax the state for the rest of the decade and beyond.

## CREDIT AVAILABILITY

Through December 2014

➤	<b>Commercial &amp; industrial</b> Terms still easing; lender risk tolerance rising
➤	<b>Commercial real estate</b> Rates remain favorable; some terms easing
➤	<b>Small business</b> Gradual improvement as lending supply grows
↔	<b>Home mortgages</b> Rates still favorable; harsh terms for nonprime
➤	<b>Credit cards</b> Terms easing as lenders pursue new business
➤	<b>Auto loans</b> Rates, terms easy in buoyant market