The Answer, my Friend, Is Blowing in the Wind: Uncertainty and the Inland Empire in 2025

by

Manfred Keil and Robert Kleinhenz[1]

The economic report, delivered at the annual State of the Region conference of the Inland Empire Economic Partnership at the Ontario Convention Center on February 18, stressed that it is difficult to make regional economic predictions two years ahead due to the uncertainty surrounding the policies and actions of the Trump administration. The forecast was made in the absence of a budget proposal, and with several legal challenges to the Administration's attempts to make over the Federal government playing out in the courts. Since then, uncertainties persist despite the passed blueprint of a budget by the House, and in face of the threatened new tariffs for Canada, Mexico, and China going into effect in March. The Federal Reserve of Atlanta forecast for national real GDP growth in the first quarter of 2025 is now -1.5 percent: real GDP is *forecasted to decline* by 1.5 percent. Some of the most prominent leading economic indicators, such as the yield curve, housing starts, and consumer sentiment now suggest a national recession for 2026.

While President Trump's policies will have a significant effect on the nation, they will influence the state and regional economy disproportionately even more. Over the past year, most of the job growth in California has occurred in Health Care and Social Assistance, and (Local) Government (read public education), both of which rely heavily on government funding and/or demographics. Together with another low wage sector, Logistics, almost 115 percent of all new jobs in California in 2024 (December 2023 to December 2024) were created by these three sectors. To clarify, the other sectors combined generated an *employment loss* in the previous year, led by a drop of 45,000 workers in Manufacturing, 12,000 in Construction, and 11,000 in Information, which includes the film industry.

This is not a healthy picture, especially given how proposed tariffs will impact the Logistics industry due to reduced trade. The Health industry may be hit by cutbacks in Federal funds for healthcare programs, including the state's Medi-Cal program. The Education sector also expects cuts in Federal support. Research universities face the prospect of reduced funds as well, including a significant reduction in overhead costs on medical research. Finally, deportation of illegal immigrants will result in a reduced availability of workers in agriculture, but more importantly, in residential construction, where their share is particularly high. Regardless of whether these

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[1] Keil: Chief Economist, Inland Empire Economic Partnership, Associate Director, Lowe Institute for Political Economy, Robert Day School of Economics and Finance, Claremont McKenna College. Kleinhenz: CEO, Kleinhenz Economics, California State University, Long Beach.

changes ultimately take place, it is important to acknowledge that the uncertainty arising from these policy changes can have significant short-term as well as long-term effects.

The challenges that the state faces will be magnified in the Inland Empire. Here in the Riverside-San Bernardino-Ontario Metropolitan Statistical Area (MSA), three sectors generate over half of the employment total of people working within the Inland Empire. The three sectors are (in descending order) Health (and Private Education), (Local) Government, and Logistics. Last year these three sectors generated 160 percent of the total employment gains here, meaning that *all* other sectors combined lost employment. Worse, only Retail Trade was the exception with a very small increase in employment. This means that three “low wage” sectors have driven the regional economy, and without the boost from these sectors, the region would have experienced a relatively heavy employment loss.

To clarify, we do not want to appear as unappreciative of the contribution of the three sectors. But it reminds us of a financial portfolio where betting on three successful stocks has gotten you to the current situation. At some point you must realize that putting all of your eggs into one basket is a highly risky strategy when it comes to looking at successful returns in the future. The Inland Empire has been there before and paid a heavy price as a result: military expenditures and aeronautic industries in the ‘90s, and housing and residential construction in the run-up to the Great Recession. The share of the Logistics industry in the Inland Empire has increased from around 5 percent in 2005 in Riverside County to its current level of 13 percent; and from 12 percent in San Bernardino County to 20 percent now.

The dangers emanating from the current economic strategy are particularly relevant when federal policies on tariffs, health, and education threaten the continuation of the currently successful expansions of the industries. There is little doubt that the Logistics industry in the Inland Empire will suffer from reduced imports into the Ports of Los Angeles and Long Beach. Add to that the likely cutbacks in investment because of AB 98 (restrictions on warehouse expansions) starting in 2026, and the biggest employer in San Bernardino County and third biggest in Riverside County, will see declines. Moreover, tariffs of the magnitude currently imposed/planned on Mexico, Canada, and China, will be passed on to consumers and businesses, thereby resulting in higher prices (inflation). These will have negative consequences for Retail Trade and the Leisure and Hospitality industry. Add to this potential supply side disruptions, and the outlook becomes bleak.

There will be similar effects if expenditure cuts to Health Care and Public Education go into effect, which will be compounded if Federal support of Local Government programs are curtailed. The state already considers reduced expenditures on Public Education because of demographics. Putting the various policy effects together, we expect employment in the Inland Empire to shrink in 2026 (forward momentum will result in continued growth in 2025). Given the regional omen of

"First In, Last Out" when it comes to business cycles, this is not a positive signal for the national economy either.

The need to diversify the Inland Empire economy does not just stem from the current economic situation, but more importantly, on the outlook for the region's economy over the next 25 years or so ("Inland Empire 2050"). The following four facts stand out regarding our regional economy: first, it is big - having passed the San Francisco MSA in population size. Second, almost 20% of its labor force commutes daily into the coastal areas (roughly 370,000 people). Third, housing is cheaper in the Inland Empire when compared to the coastal areas; and fourth, educational attainment is relatively low (only 25 percent of the Inland Empire labor force has a bachelor's degree or more, compared to 37 percent in the U.S.). These four facts explain why our major road arteries are as congested as they are, and why per capita GDP (a proxy for average income) is so low, putting us near the bottom of the list of MSAs in the country.

Attracting higher wage industries into our area will be crucial for the future success of the region, since it would allow the vast number of commuters to stay closer to home, and avoid the stress of daily multi-hour commutes. However, high wage firms will not come into our area unless we can show them that we have a labor force that has more human capital (education levels) than the current residents do. Regarding the future, we must also be looking at performance levels of 8th graders for the two counties. Here we see that in 2023-2024 only 40 percent of students in Riverside County met or exceeded the standard for English, and only 24 percent did so in mathematics. For San Bernardino County, the numbers are similar: 39 percent for English and 23 percent for Mathematics. By comparison, they are 45 percent for Orange County, 35 percent for San Diego County, and 50 percent for Santa Clara County for mathematics. Cuts in funding at the K-12 level and in higher education will pose new challenges to the region's education institutions at a time when they are so important.