Washington State Economic & Revenue Outlook

Presented to
Pierce County Fire Chiefs Association

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March 11, 2010
Dupont, Washington

Summary

- We are coming out of the "Great Recession"
  - The economy will gain traction by mid-year
  - The recovery in revenues is underway, but progress will be slow
- The economic recovery faces headwinds
  - Real estate, especially commercial
  - Banking, particularly local and regional banks
- The revenue recovery too faces headwinds
  - Slow job growth
  - Tentative consumer confidence
- Upside
  - Exports
  - Stable aerospace and software publishing

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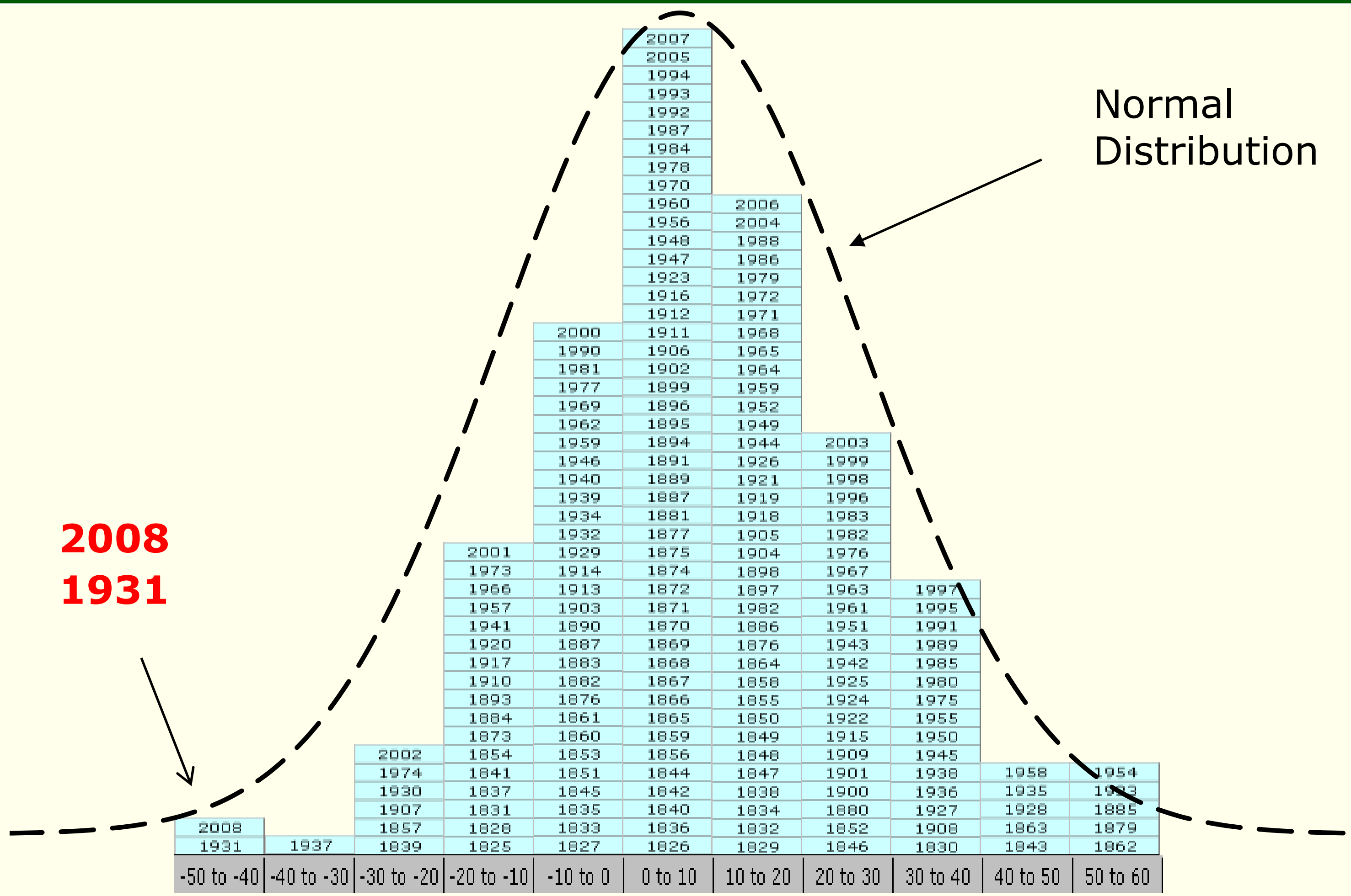
Equity returns in 2008 were a tail event

U.S. Stock Market Total Returns

1825 - 2008



Source: AXA

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At this stage in 1982-83, employment had started to recover

Cumulative job losses at 26 months

1982-83:

1.4% of labor force

This time:

4.7% of labor force

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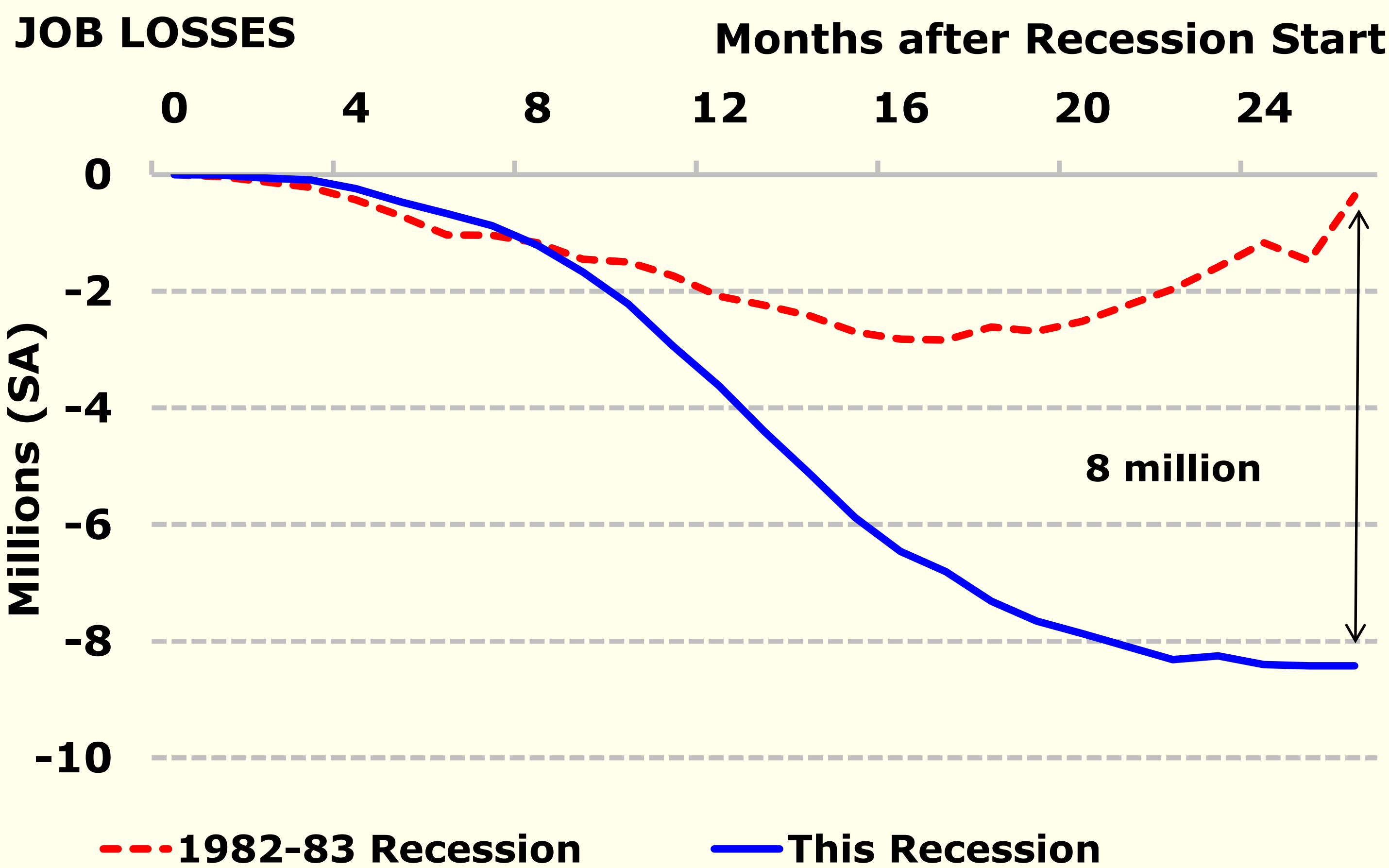
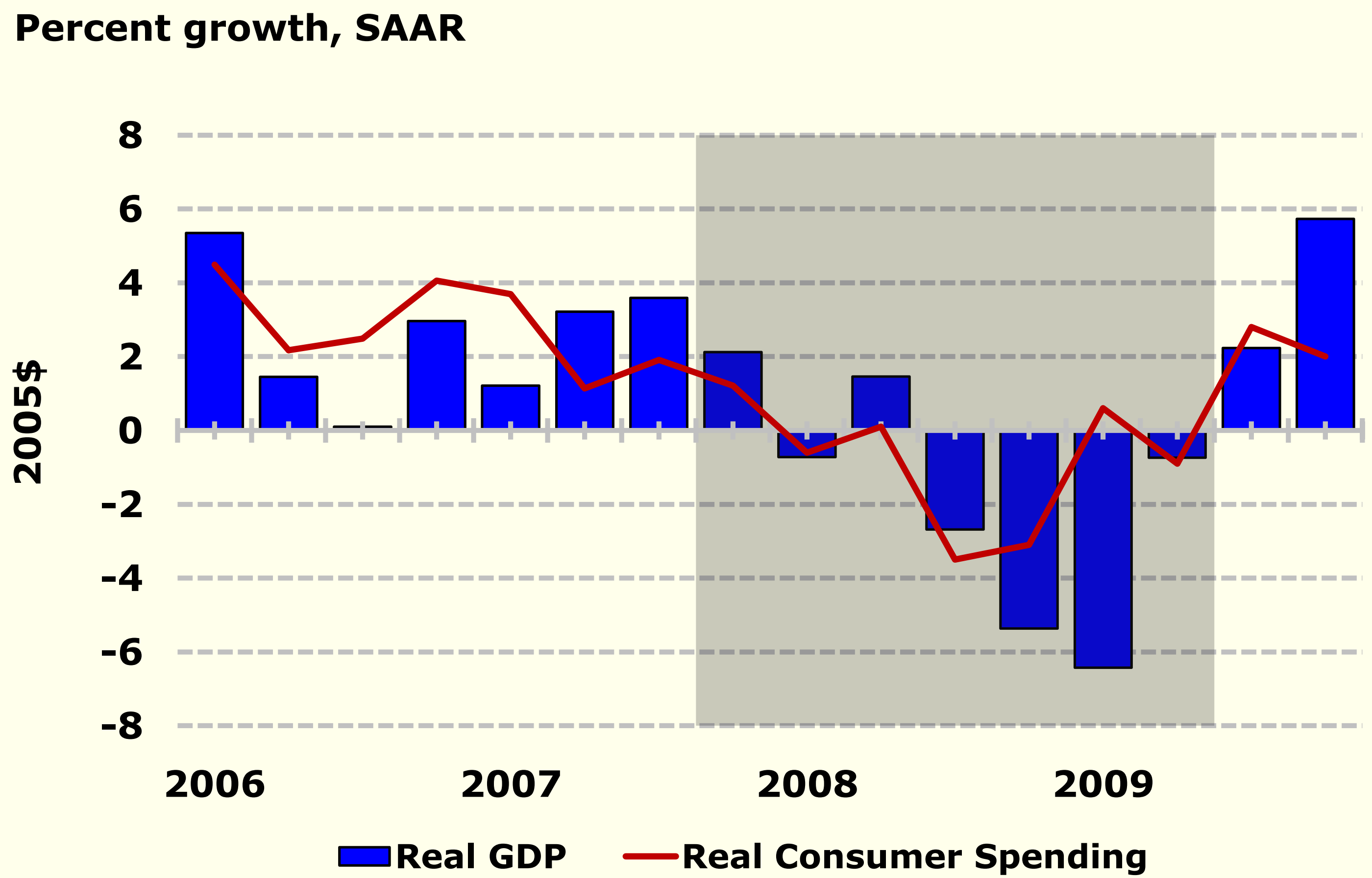


Source: BLS, ERFC; data through January 2009

GDP returned to growth in Q3



Source: BEA, data through 2009 Q4

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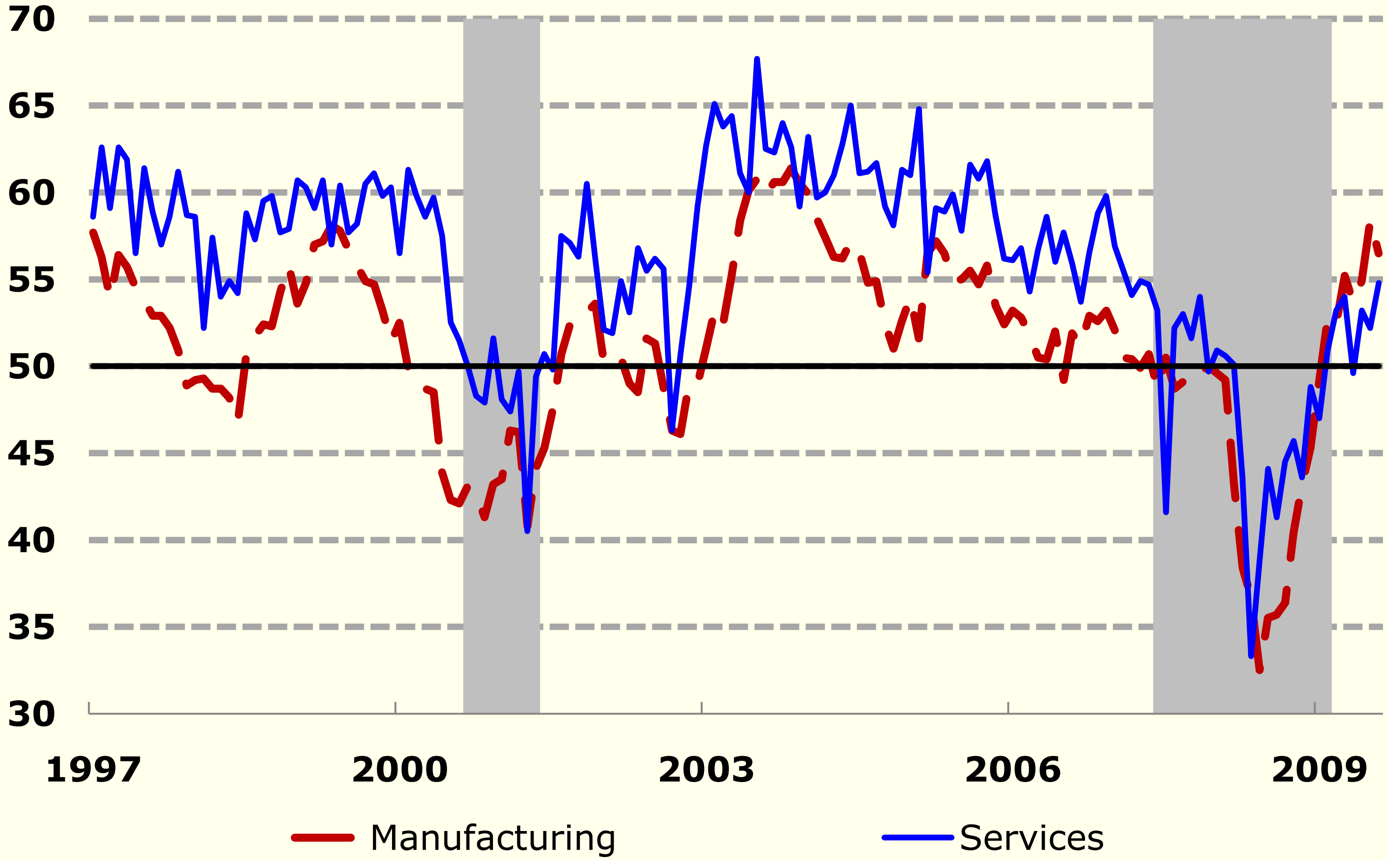
Both services and manufacturing are improving

An index greater than 50, implies growth



Source: Institute of Supply Management; data through February 2010

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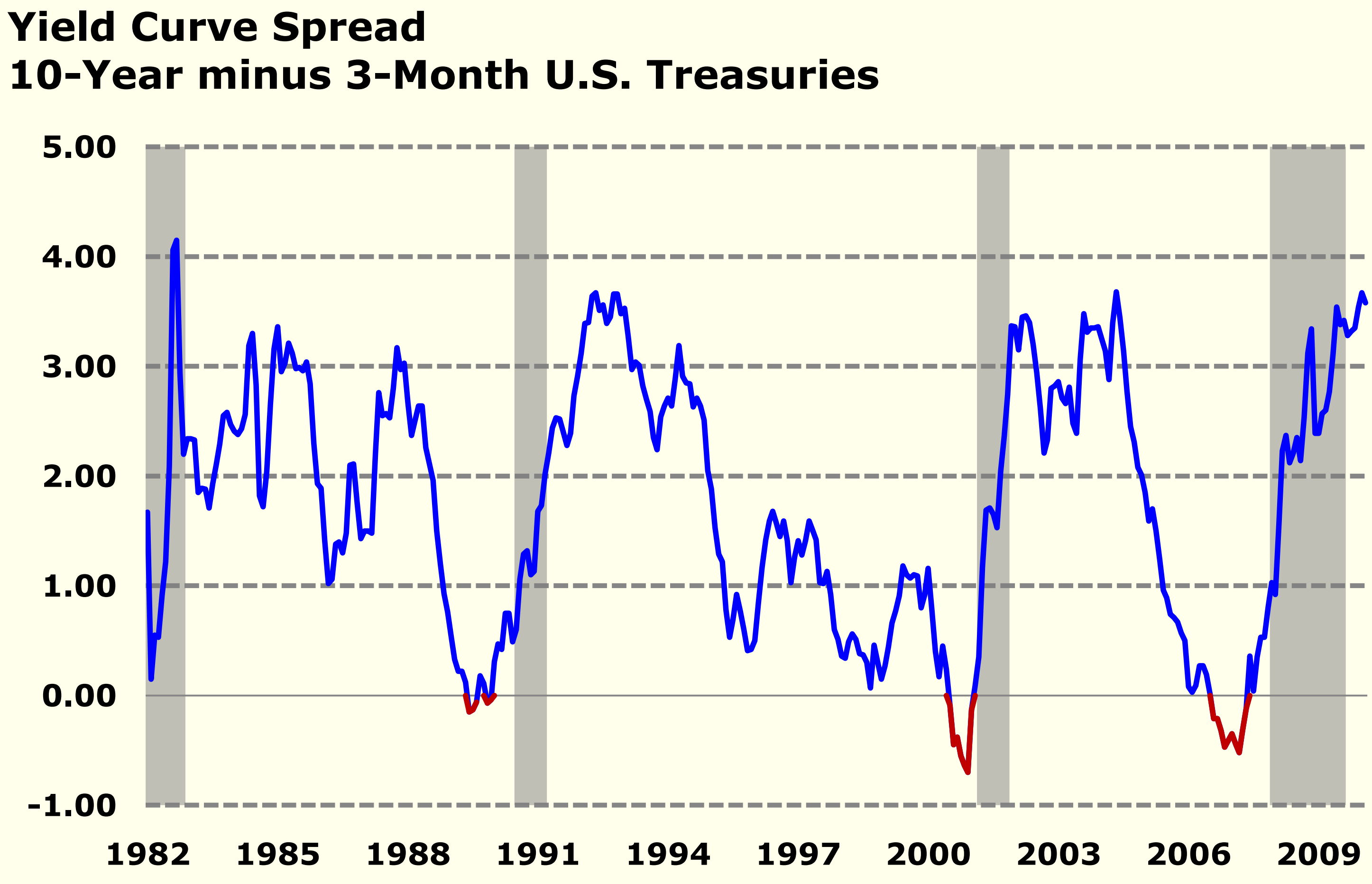
Increasing yield curve spread points to growth

An inverted yield curve typically precedes a recession while a steepening yield curve signifies a recovery



Source: Federal Reserve Board, ERFC; data through February 2010

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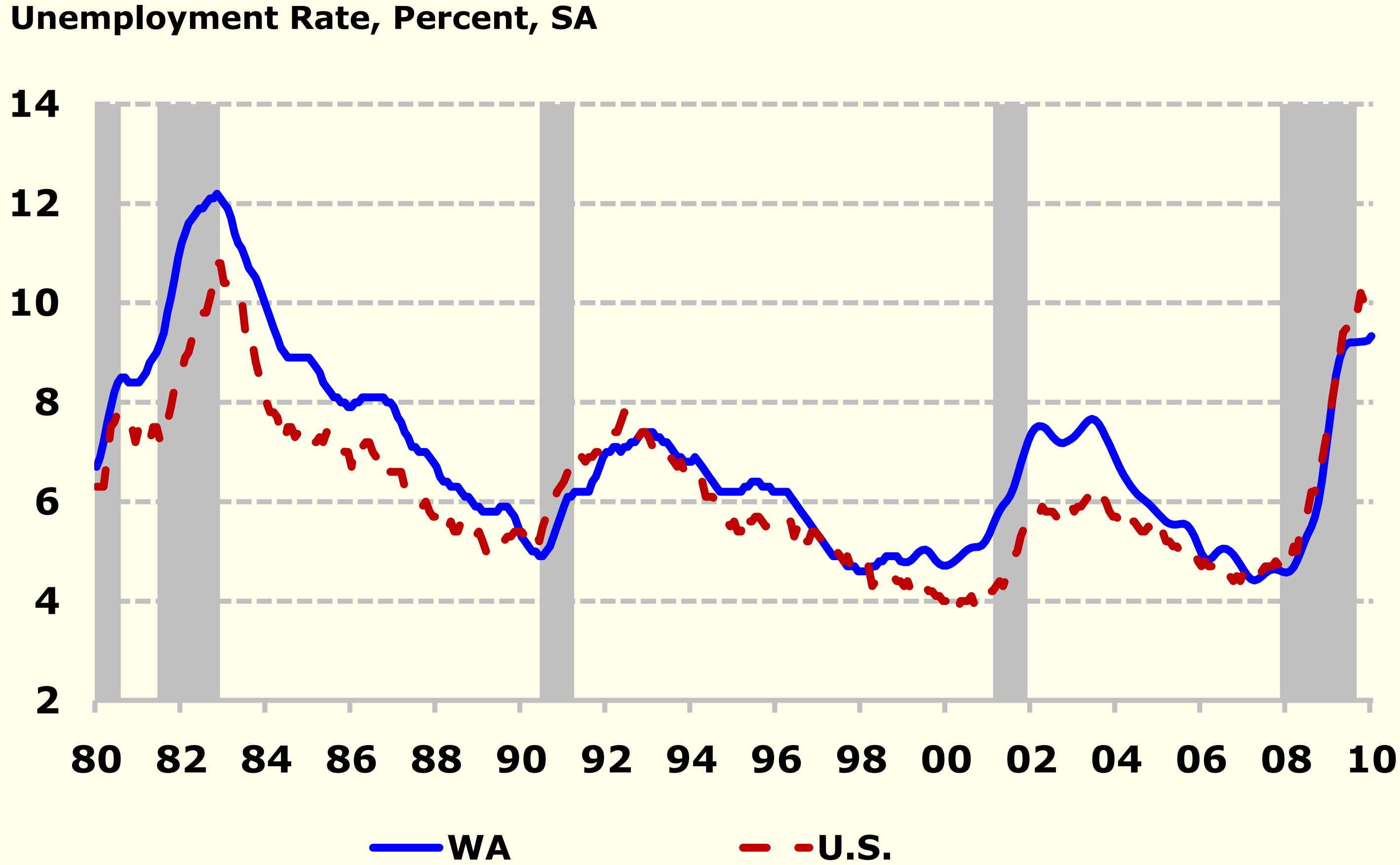
Unemployment is still high

It is normal for this rate to continue to rise even after the economy is in recovery



Source: WA ESD, BLS; data through January 2010

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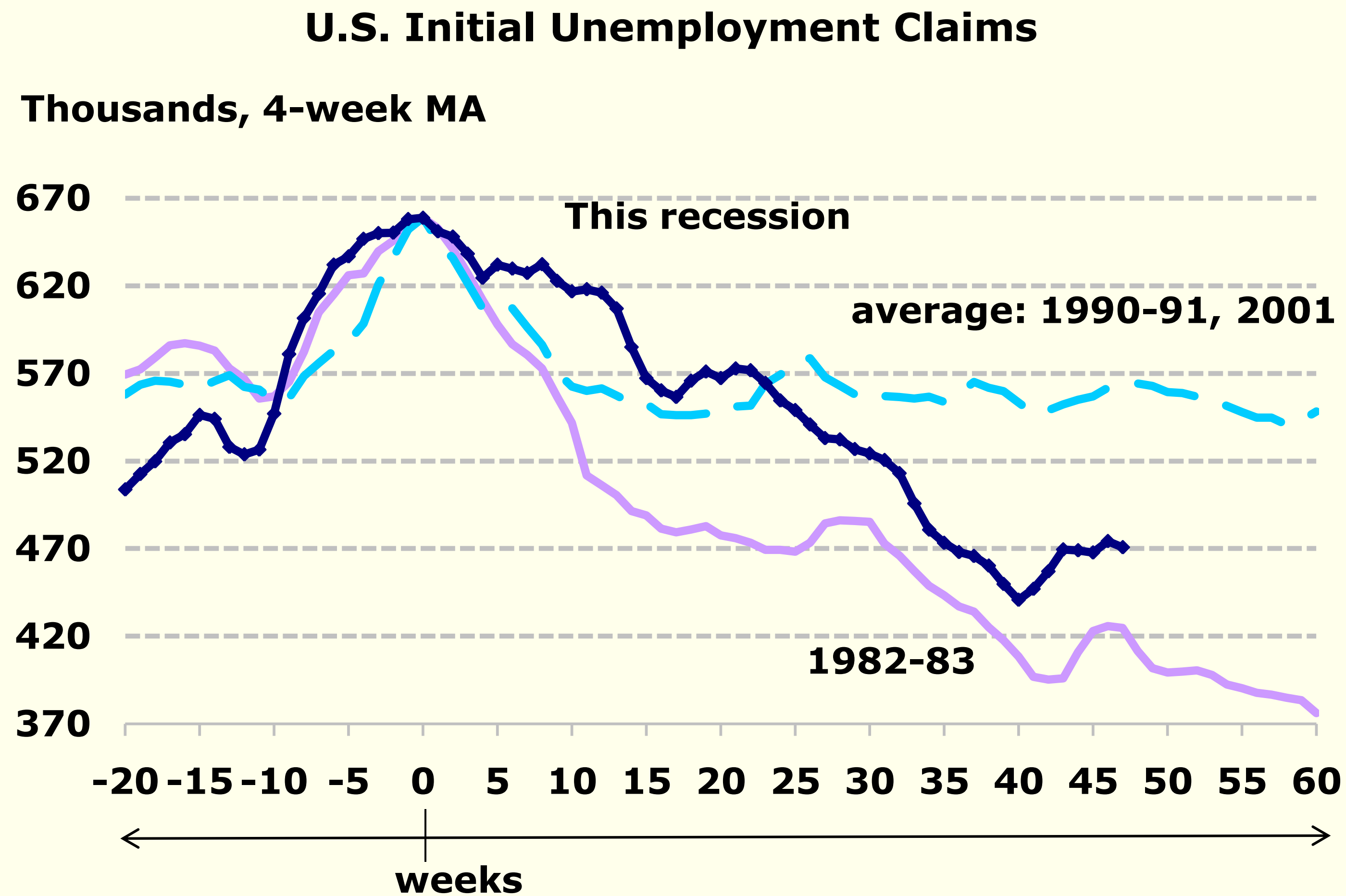
The recovery in employment has been slow, but is poised to improve



Source: U.S. Department of Labor, ERFC; data through Feb 20, 2010

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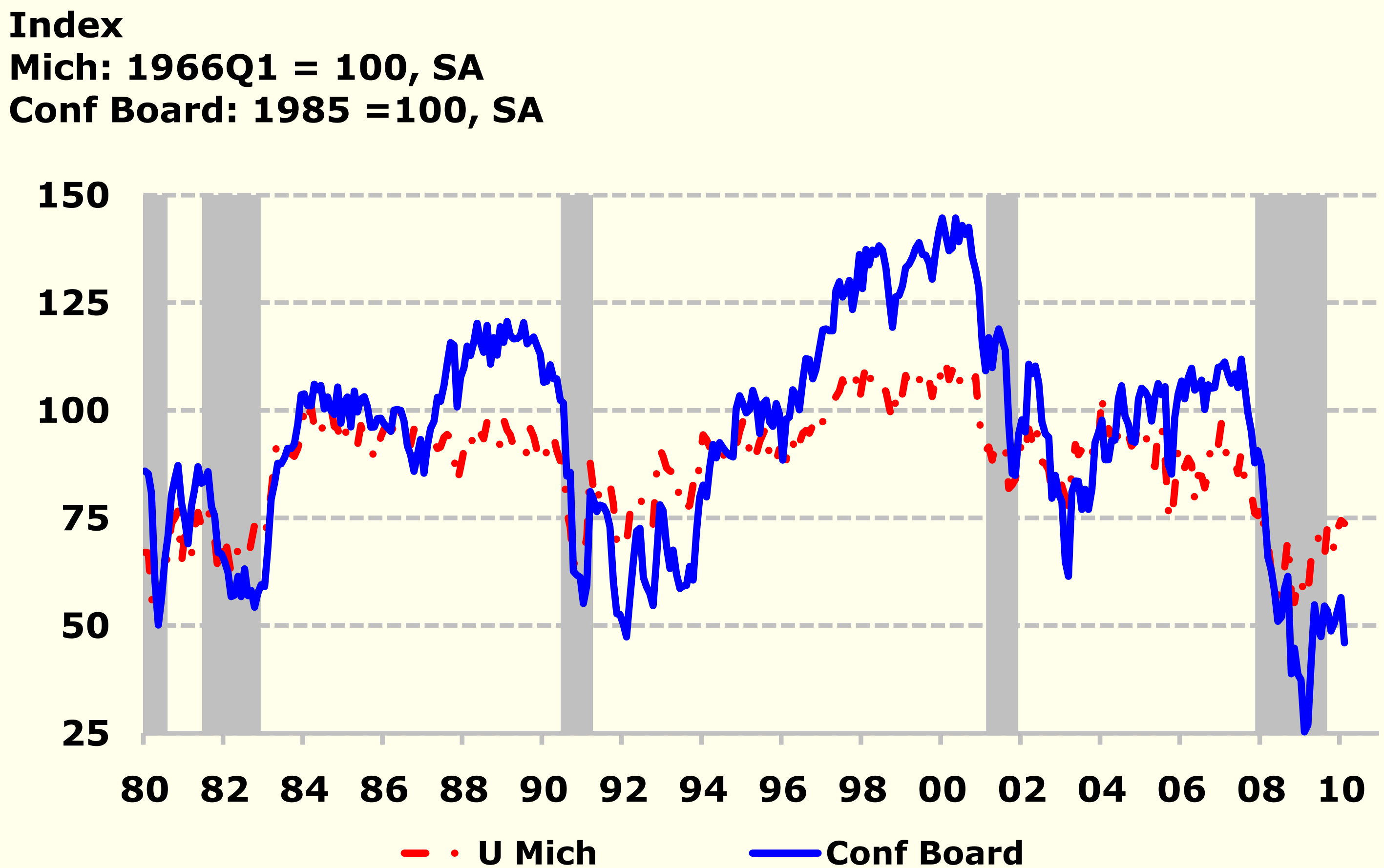
Consumer confidence is giving mixed signals



Source: University of Michigan; Conference Board, data through February 2010, preliminary

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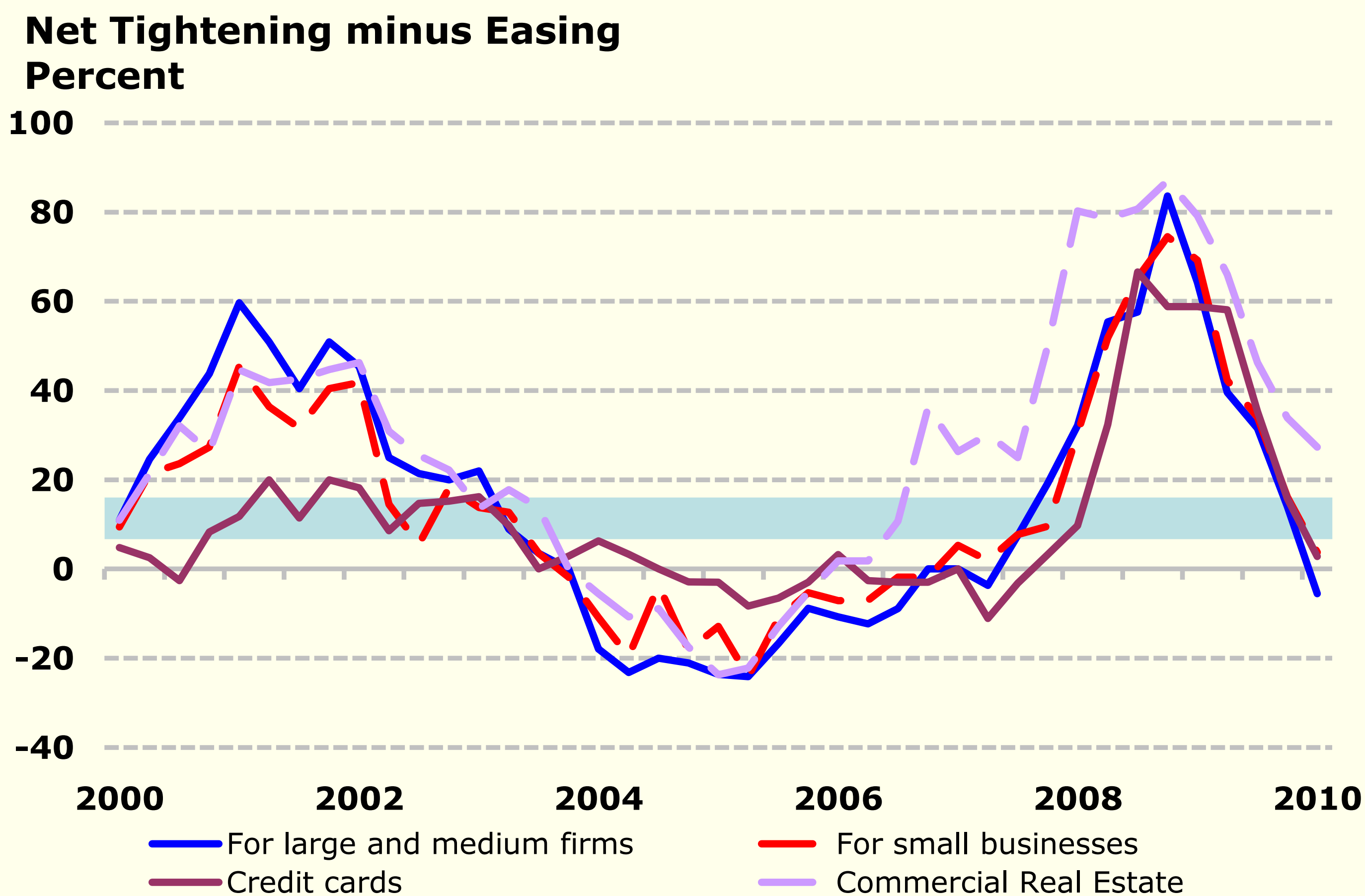
Bank lending appears to be easing, but not for commercial real estate

Survey includes 60 large domestic banks and 24 U.S. branches of foreign banks



Source: Federal Reserve Board, Senior Loan Officers Quarterly Survey; data through January 2010 survey

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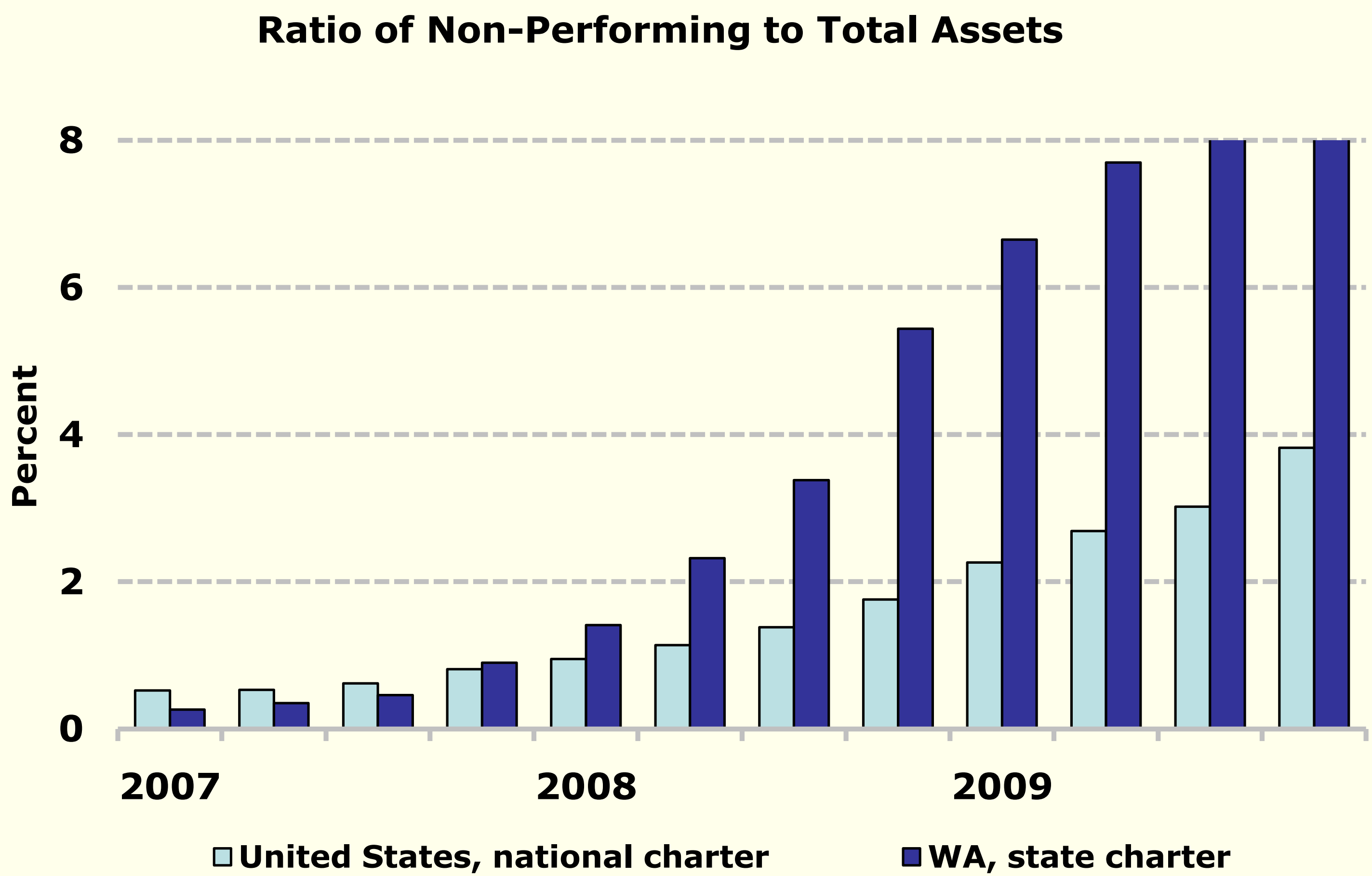
Asset quality of regional banks is poorer, but leveling off

The poorer asset quality of regional banks is due to their disproportion-ately high exposure to commercial real estate



Source: FDIC, data through 2009 Q4

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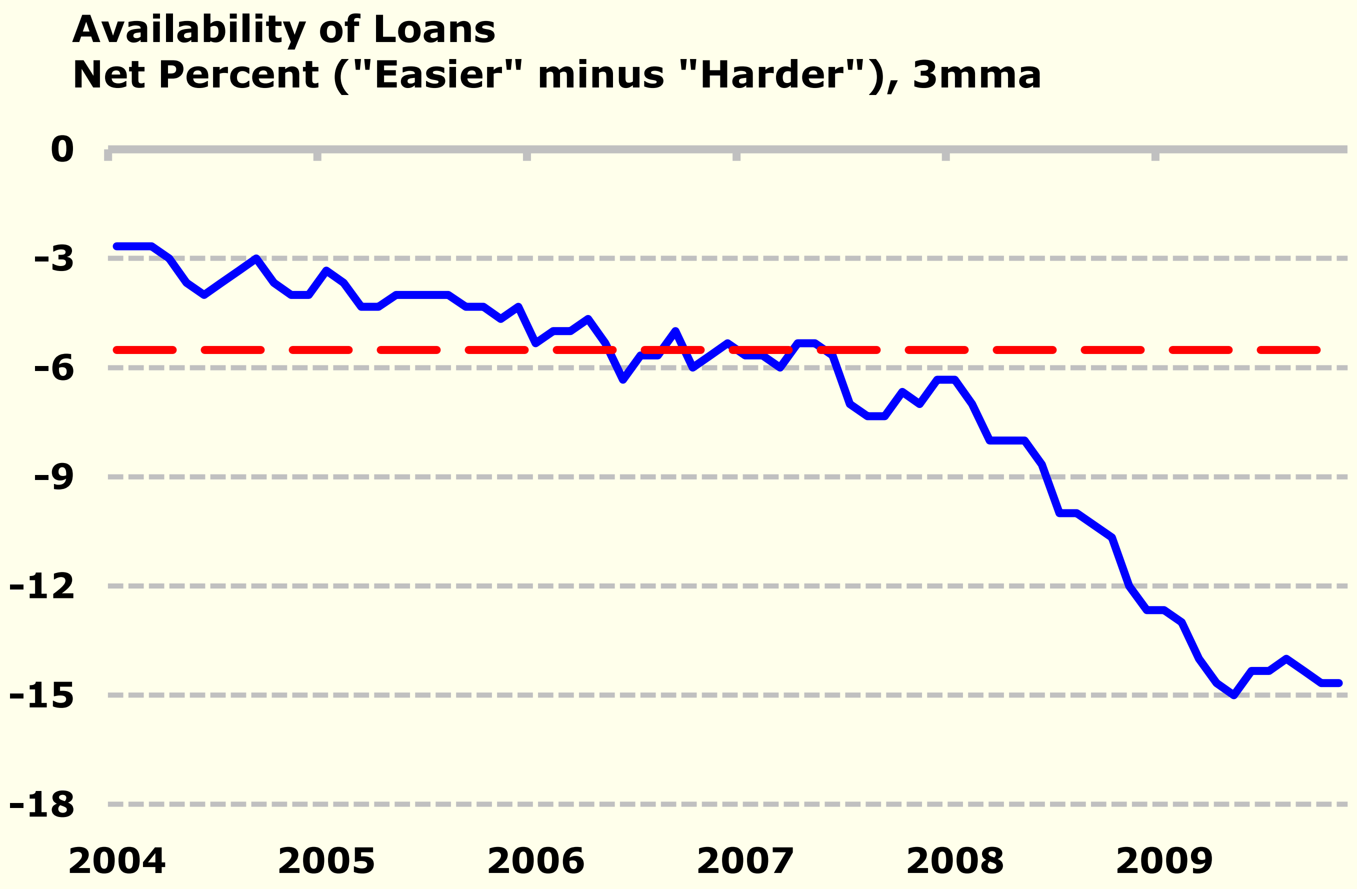
Credit conditions remain tight for small business...



Source: National Federation of Independent Business; data through January 2010

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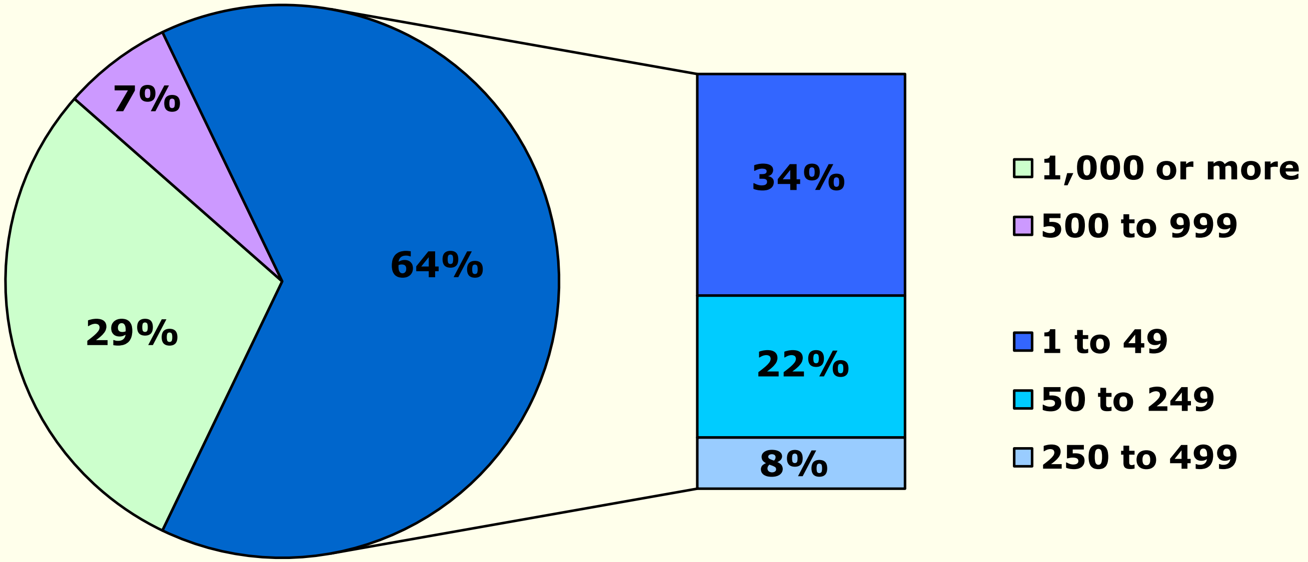
... who create most of the jobs

Since 1992, 64% of the net change in employment has occurred in small businesses



Source: BLS, data from 1992 Q3 to 2009 Q1

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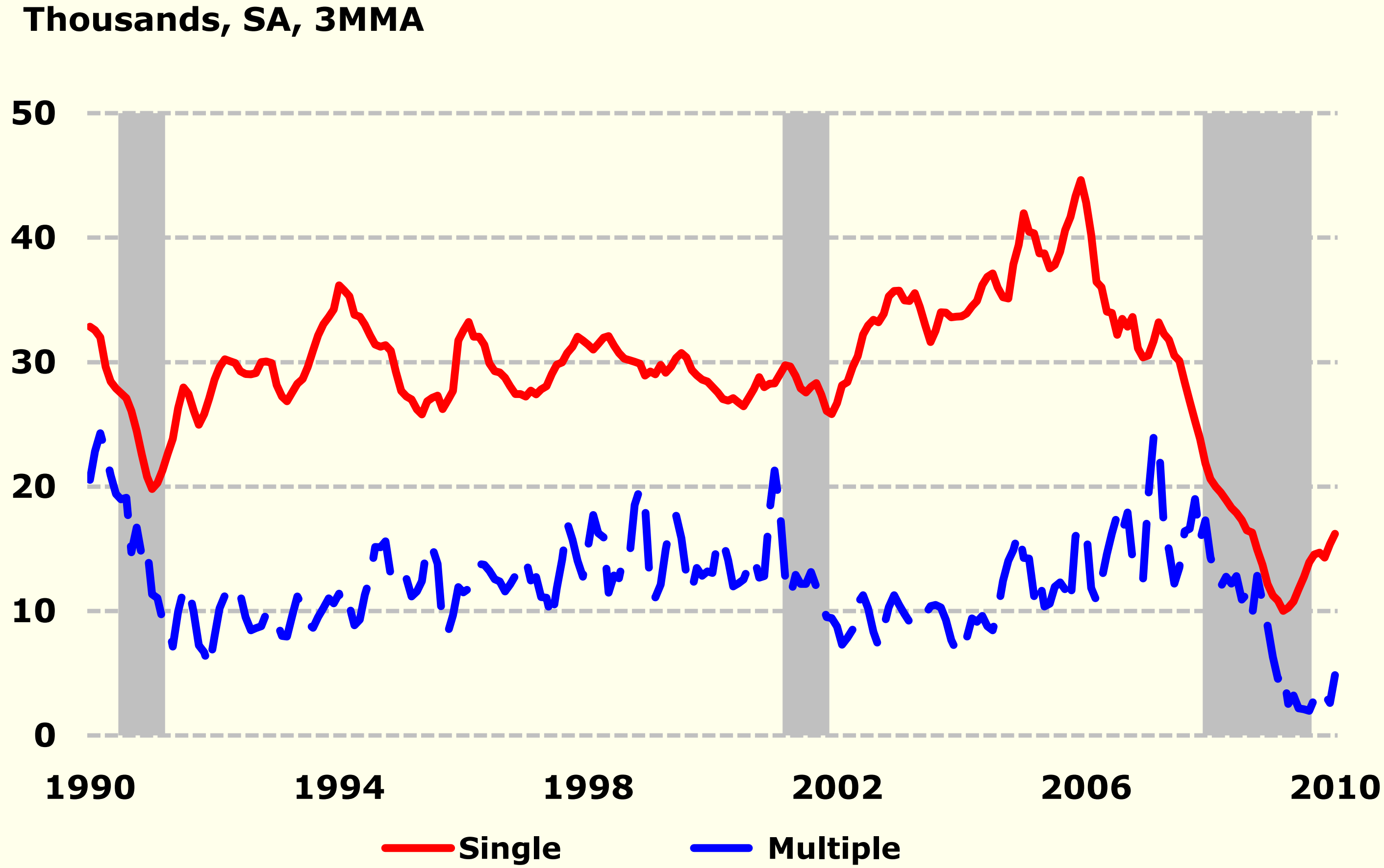
WA single family building permits are doing better than multi-family



Source: U.S. Census Bureau; data through January 2010

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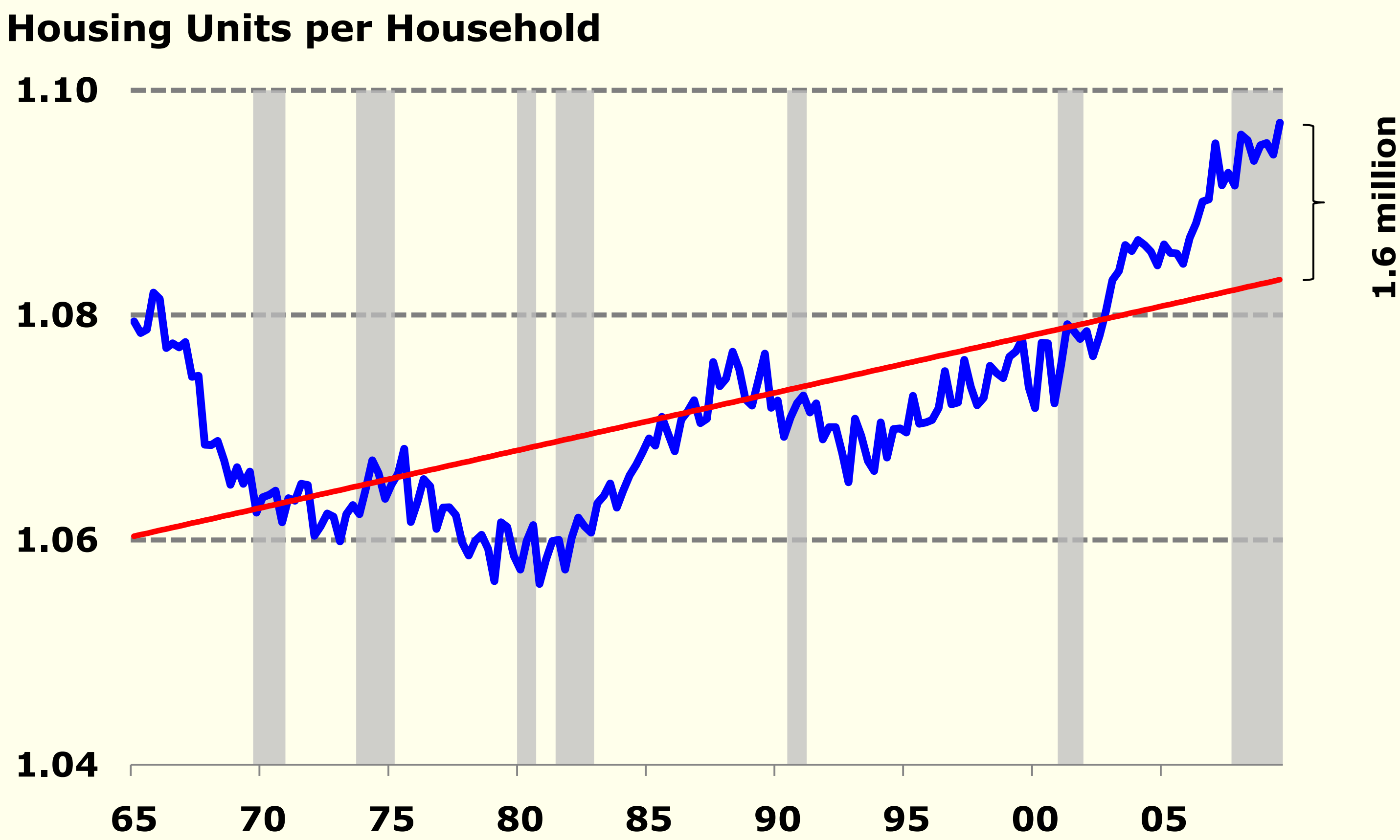
National housing inventory remains well above trend



Source: U.S. Census Bureau, ERFC; data through 2009 Q3

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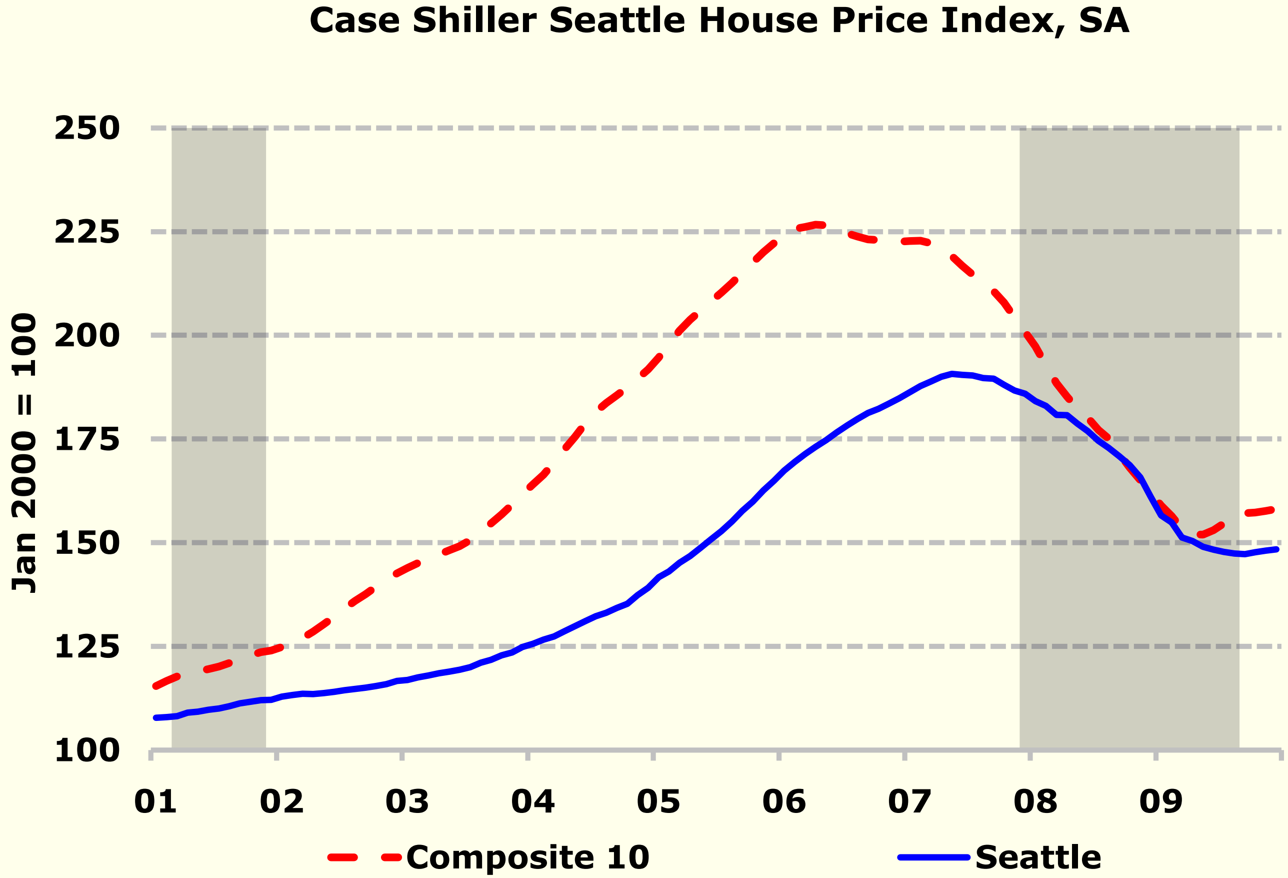
Home prices in Seattle appear to be leveling off, but lag the nation in the turnaround

Seattle Home Prices



Source: S&P/Case-Shiller; data through December 2009

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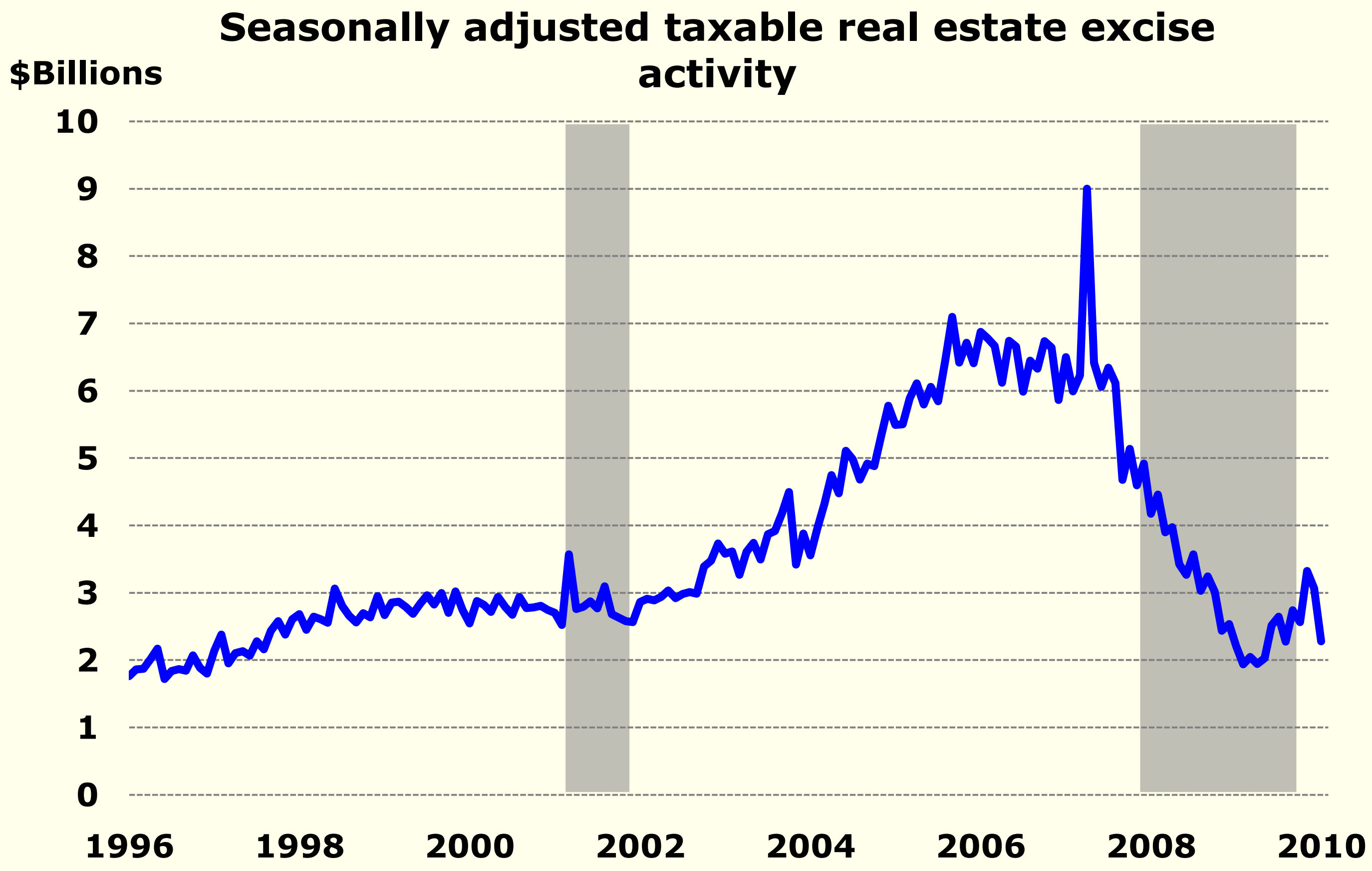
REET collections fell after first round tax credits expired



Source: ERFC; Monthly data through January 2010

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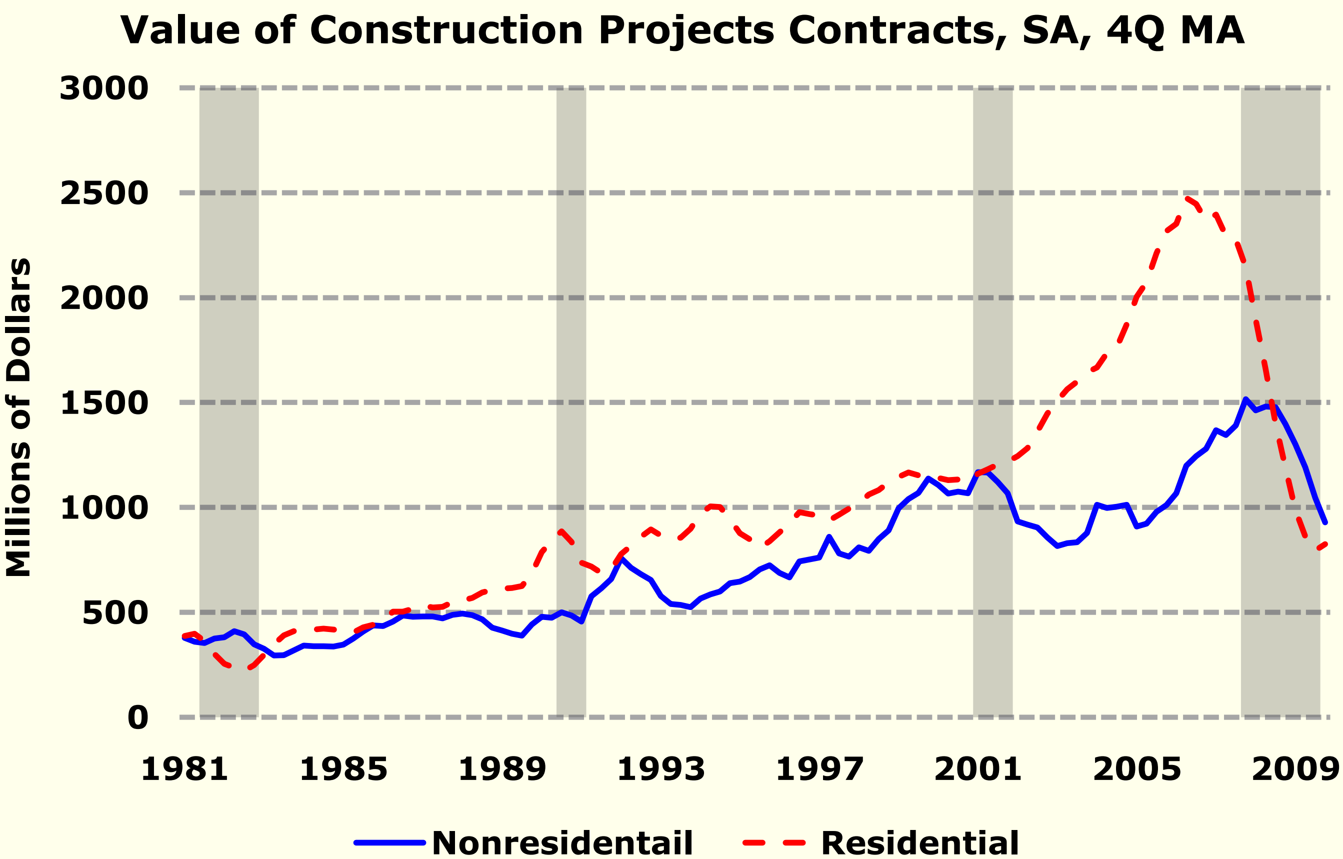
Non-residential construction lagged residential on the way down, and has yet to find bottom



Source: McGraw-Hill Construction, ERFC; data through 2009 Q4

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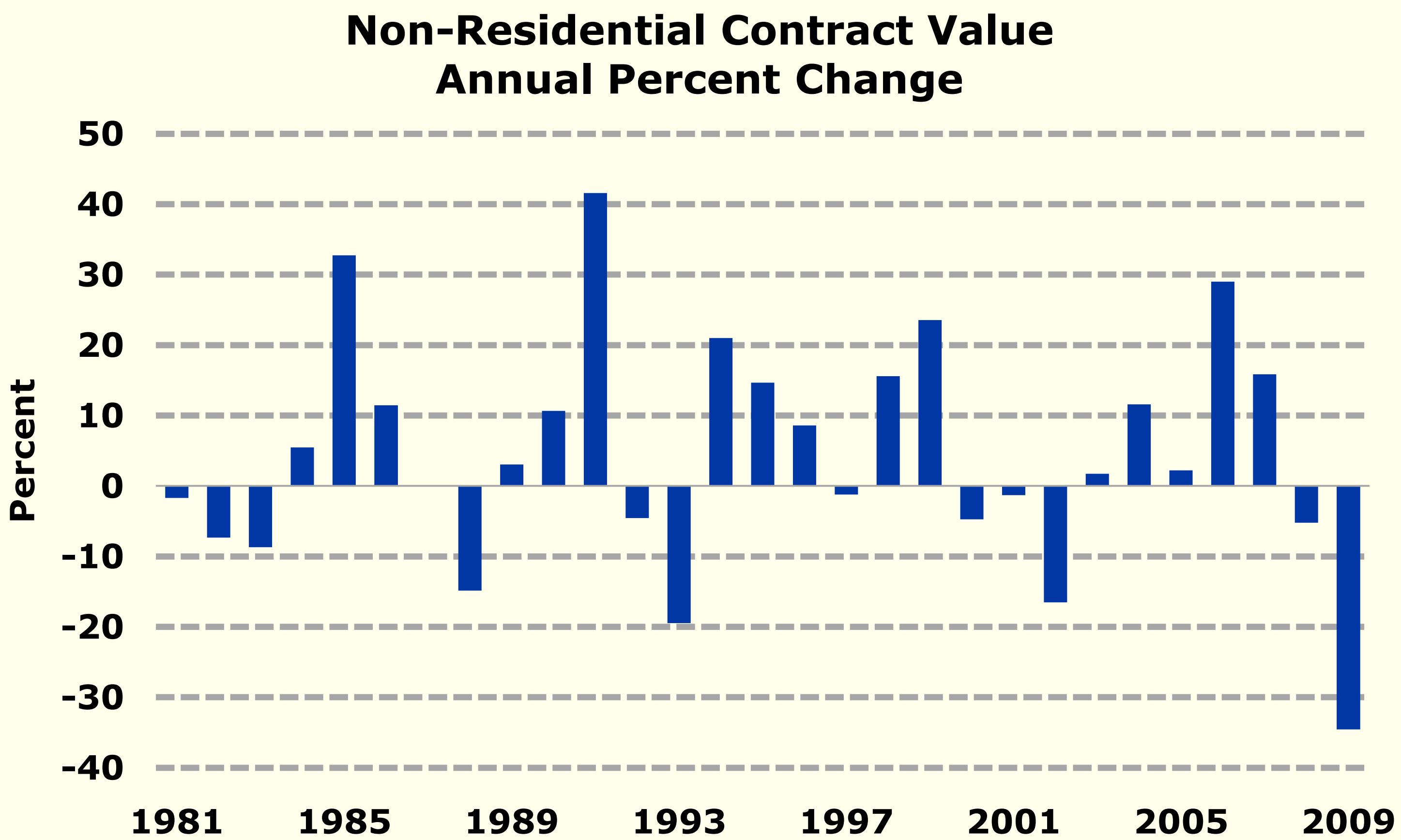
This is the worst downturn in non-residential construction in 30 years



Source: McGraw-Hill Construction, data through December, 2009

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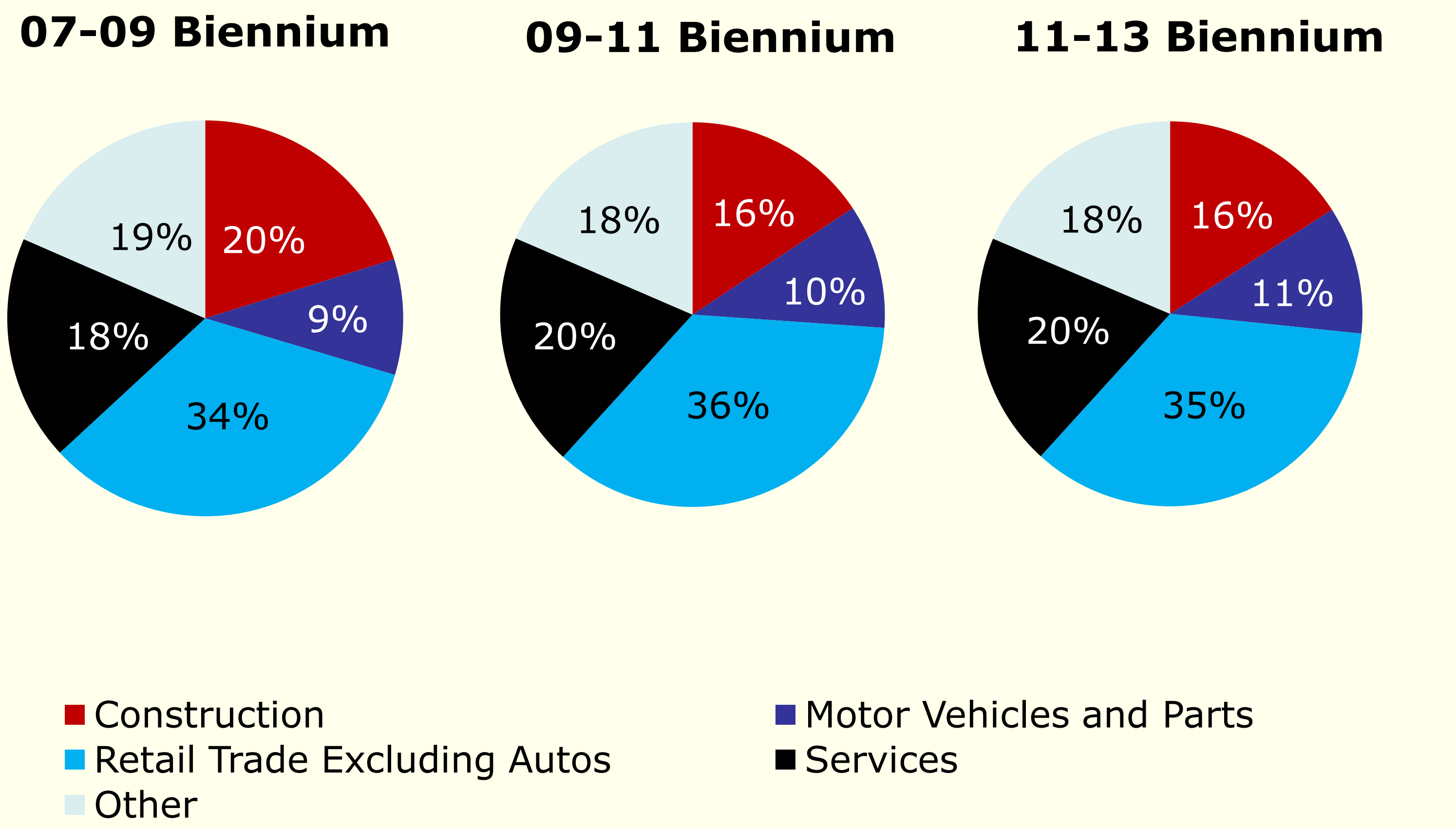
The share of construction in the Retail Sales tax base has shrunk



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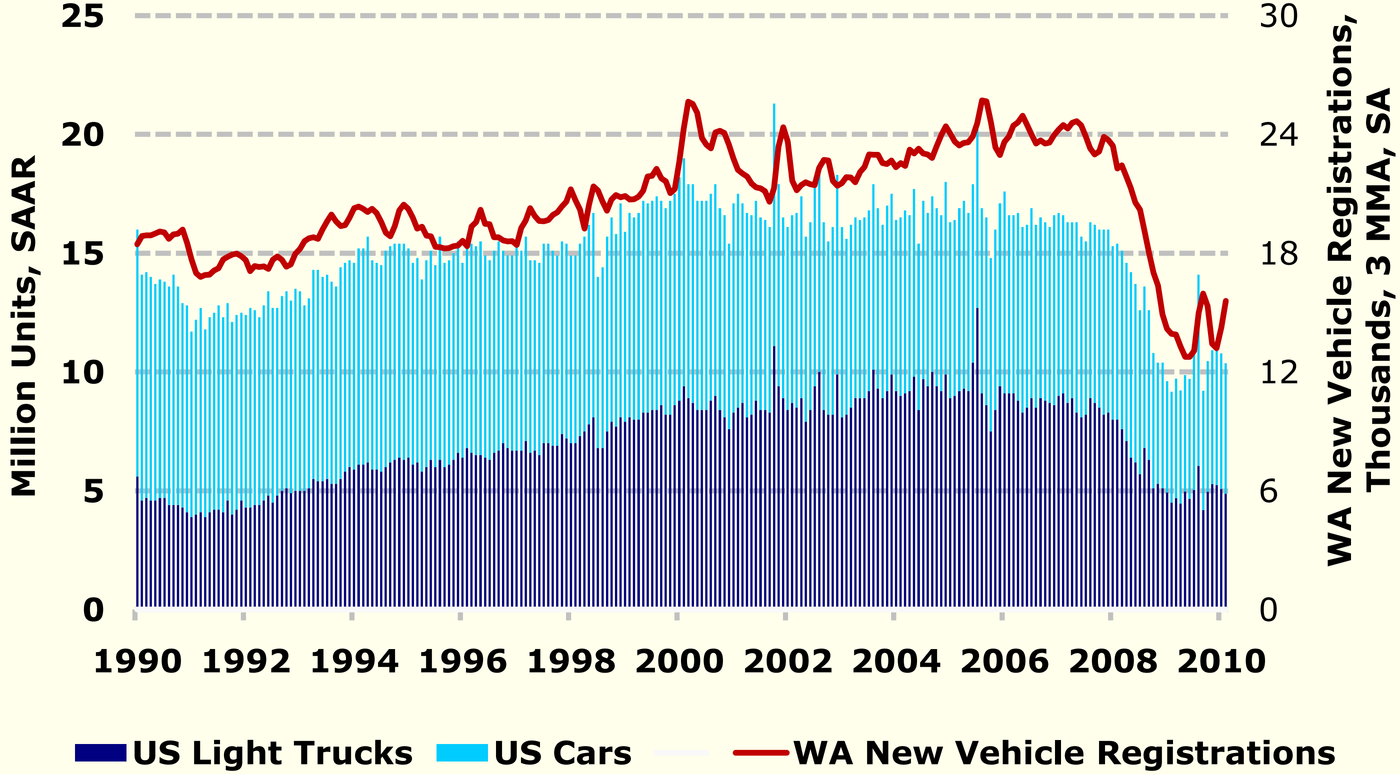
Automotive sales have stayed stable despite inclement weather

National car sales were 1.2 million units (ann.) higher in February 2010 than in February 2009



Source: Autodata Corporation, WA DOL; data through Feb 2010

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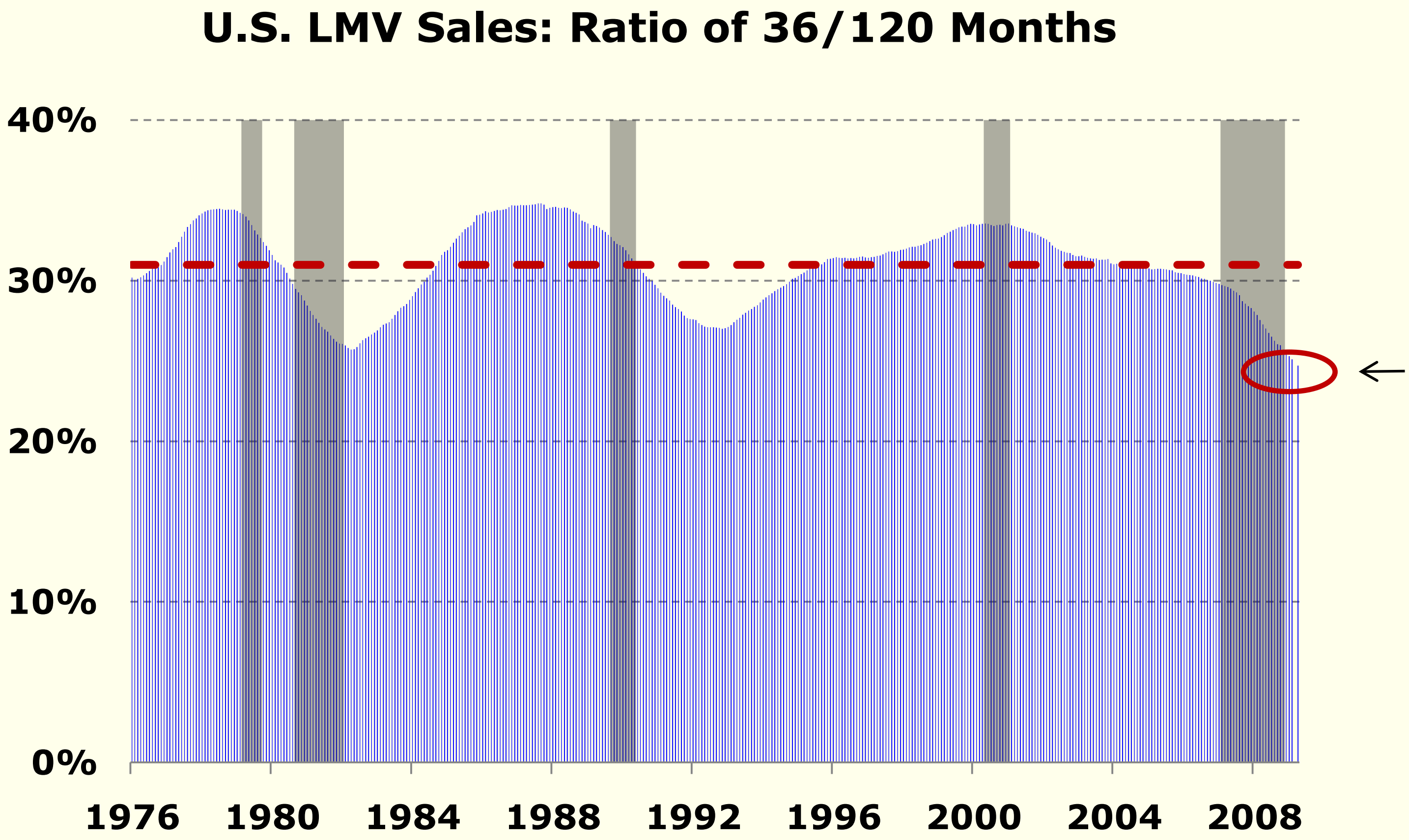
Relative age of the car fleet indicates imminent turnaround in car sales

The percent of "old" cars on the road is at a historic high



Source: Autodata Corporation, ERFC; data through February 2010

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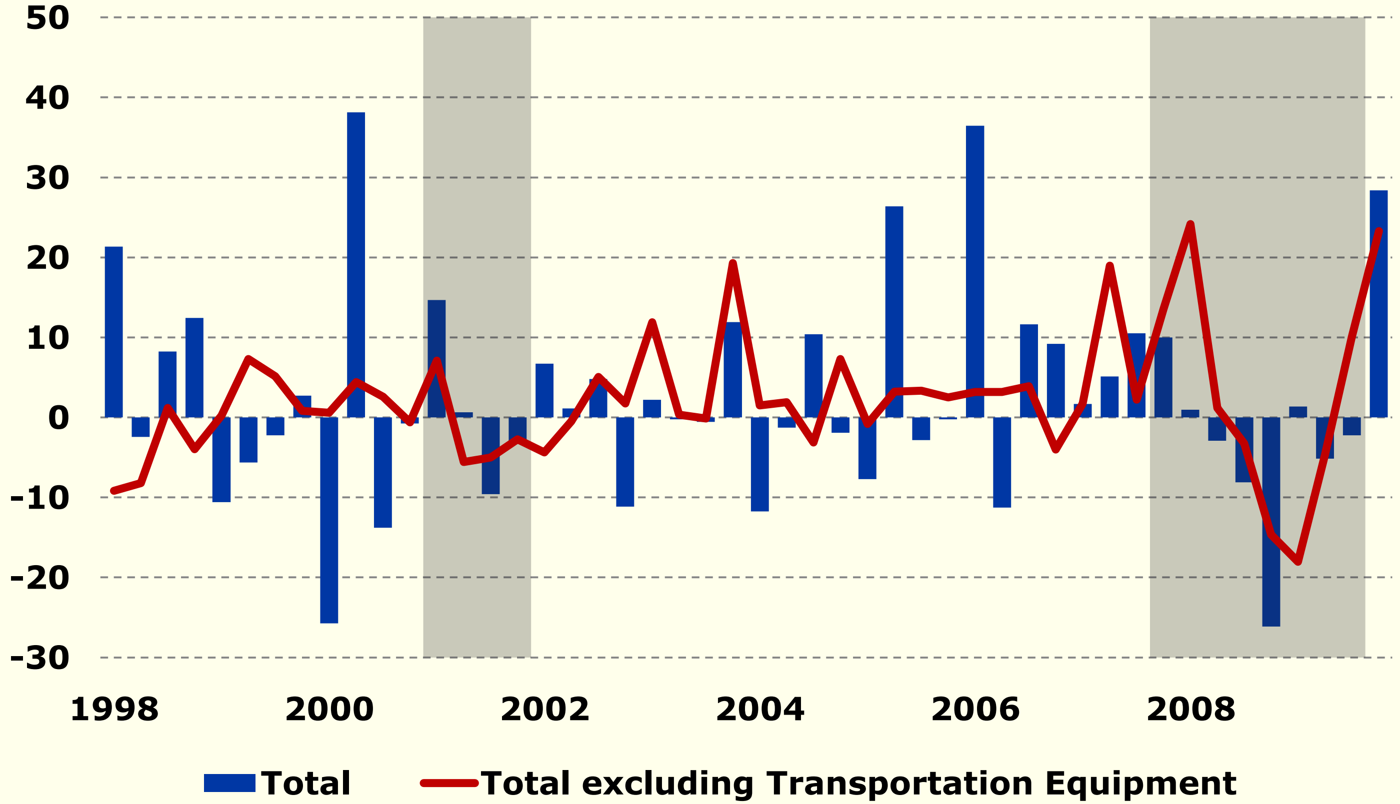
Exports will help the state recover faster than the nation

Exports excluding transport equipment were up 23% in Q4

Exports, SA
Percent Change, quarter ago



Source: Wiser Trade Data; through 2009 Q4

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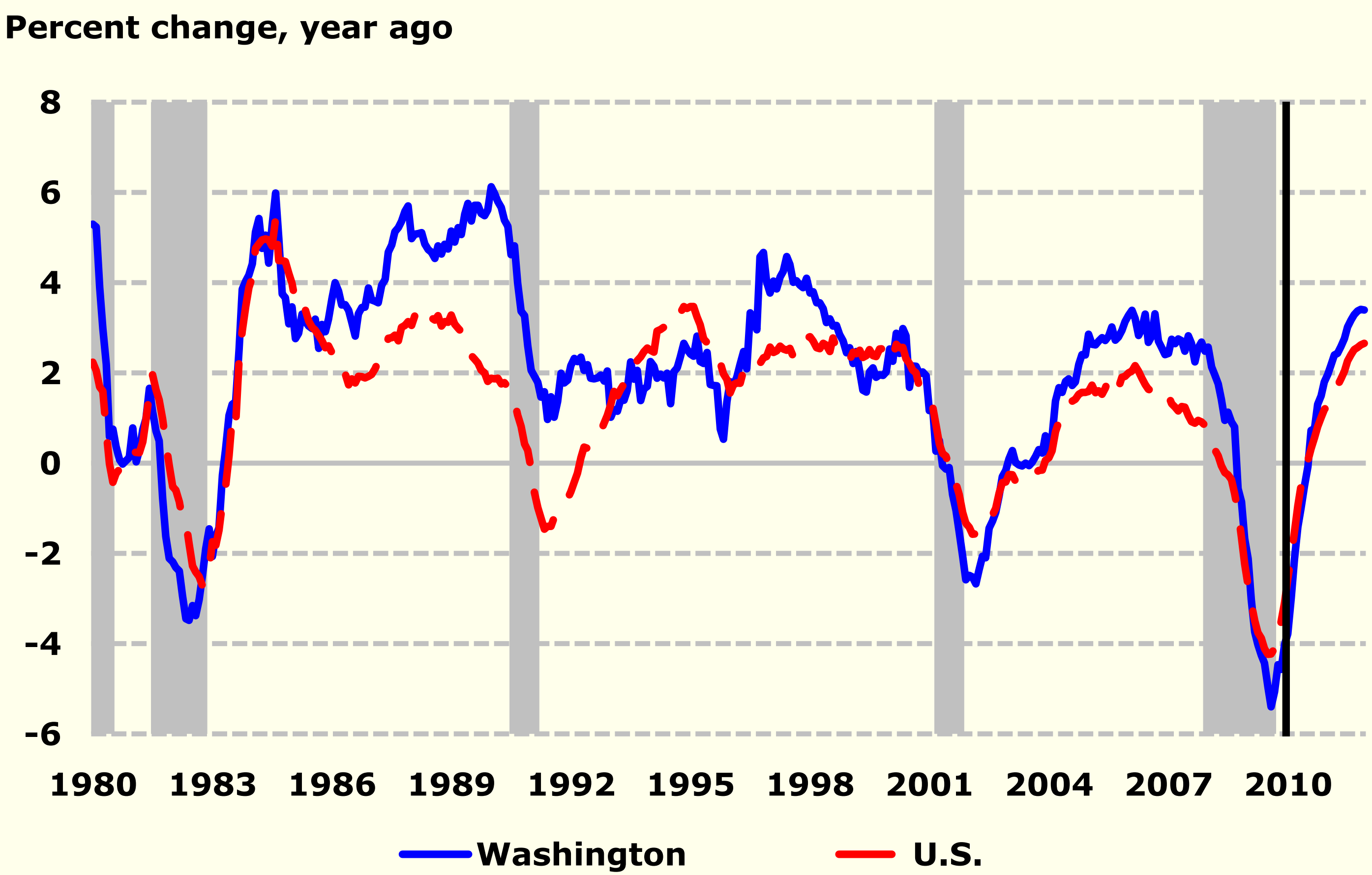
WA <u>employment</u> lagged the nation in the downturn and will recover a little stronger than the nation



Source: ERFC November 2009 forecast; actual through December 2009

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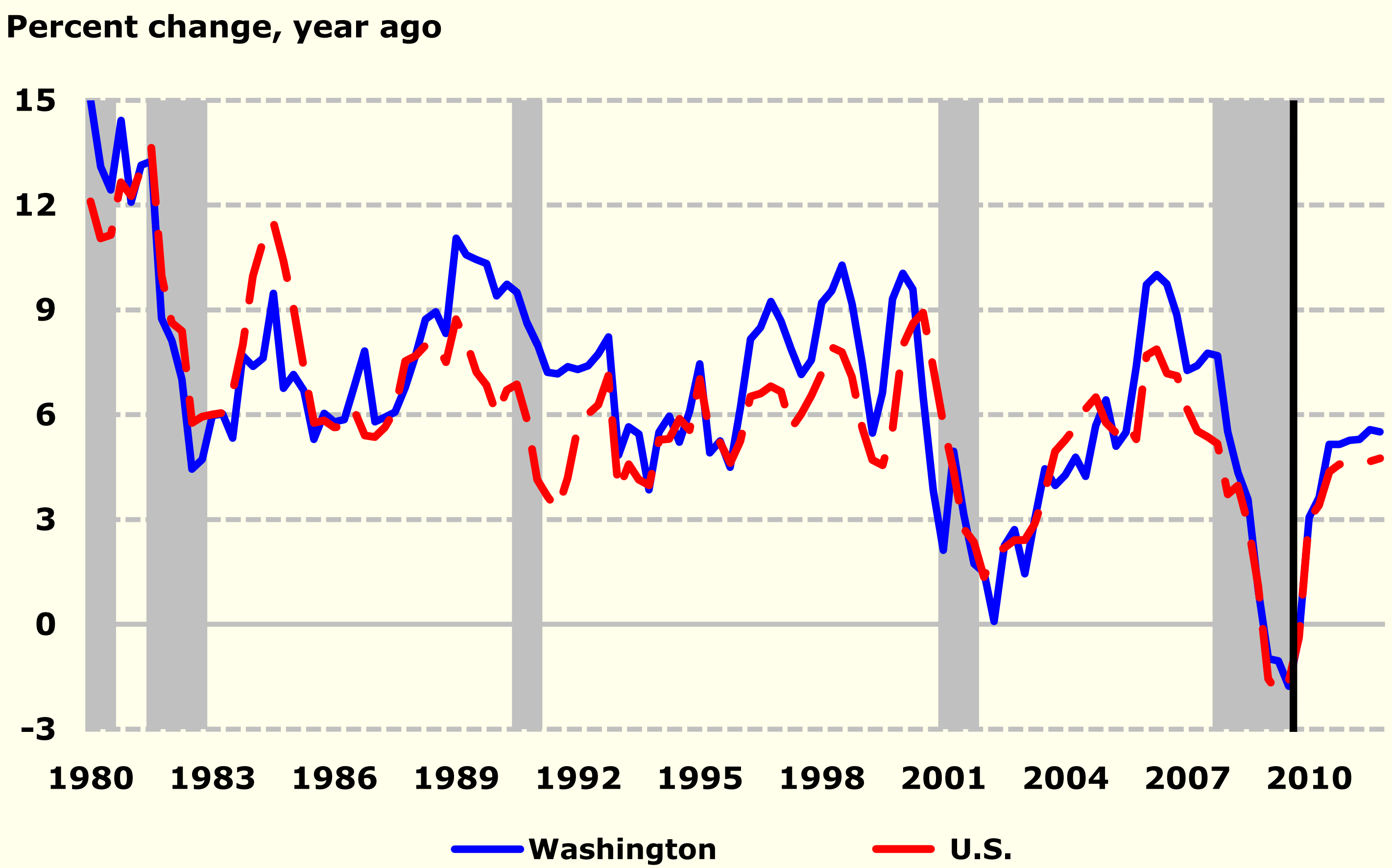
The recovery in WA personal income growth is expected to be better than the nation's



Source: ERFC February 2010 forecast; actual data through 2009Q3

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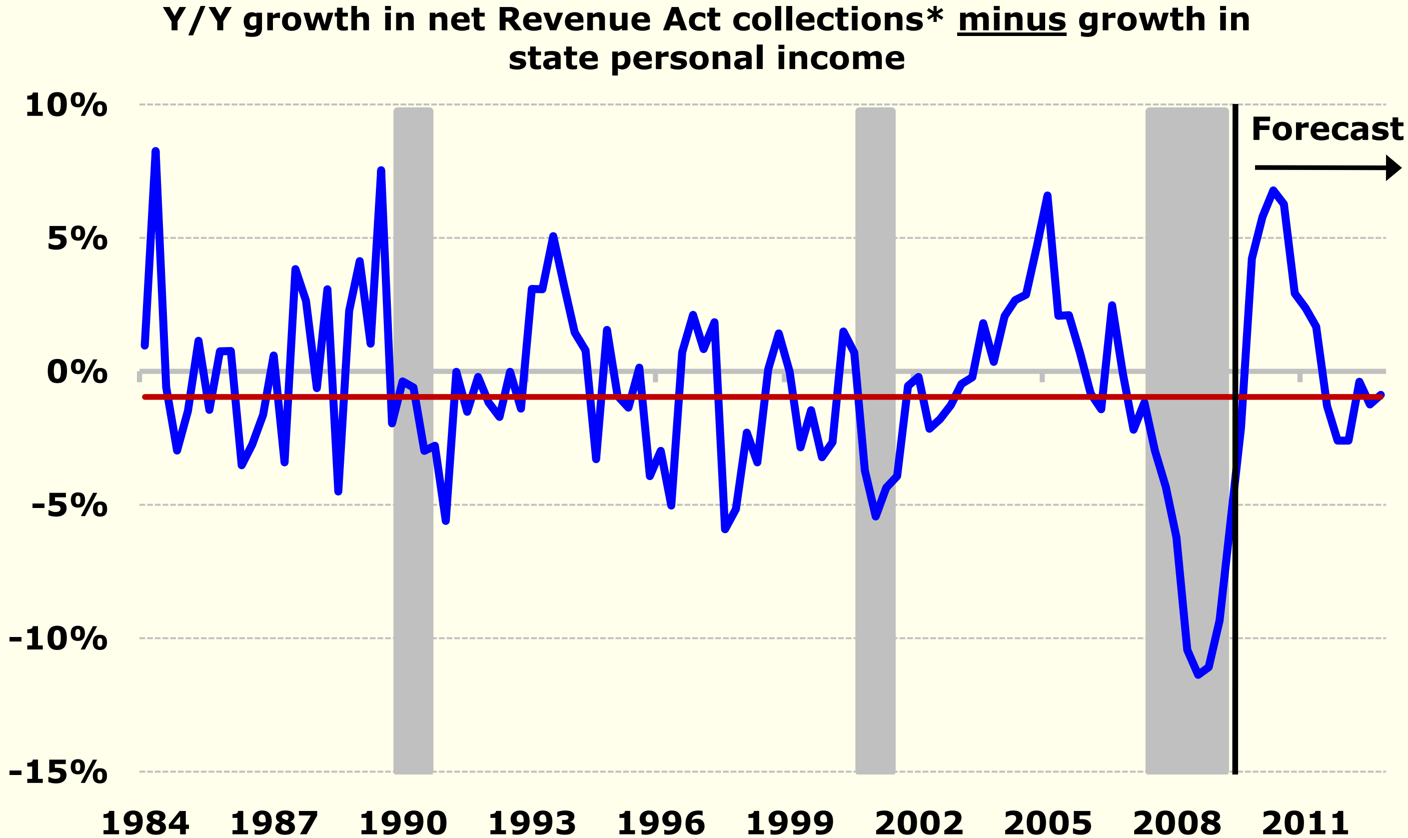
Revenue growth relative to income is starting to turn around

The difference between the growth rate of Revenue Act collections and state personal income began to shrink in the second quarter of 2009.



* Adjusted for new legislation, current definition of Revenue Act

Source: DOR and ERFC; data through 2009Q4 estimated

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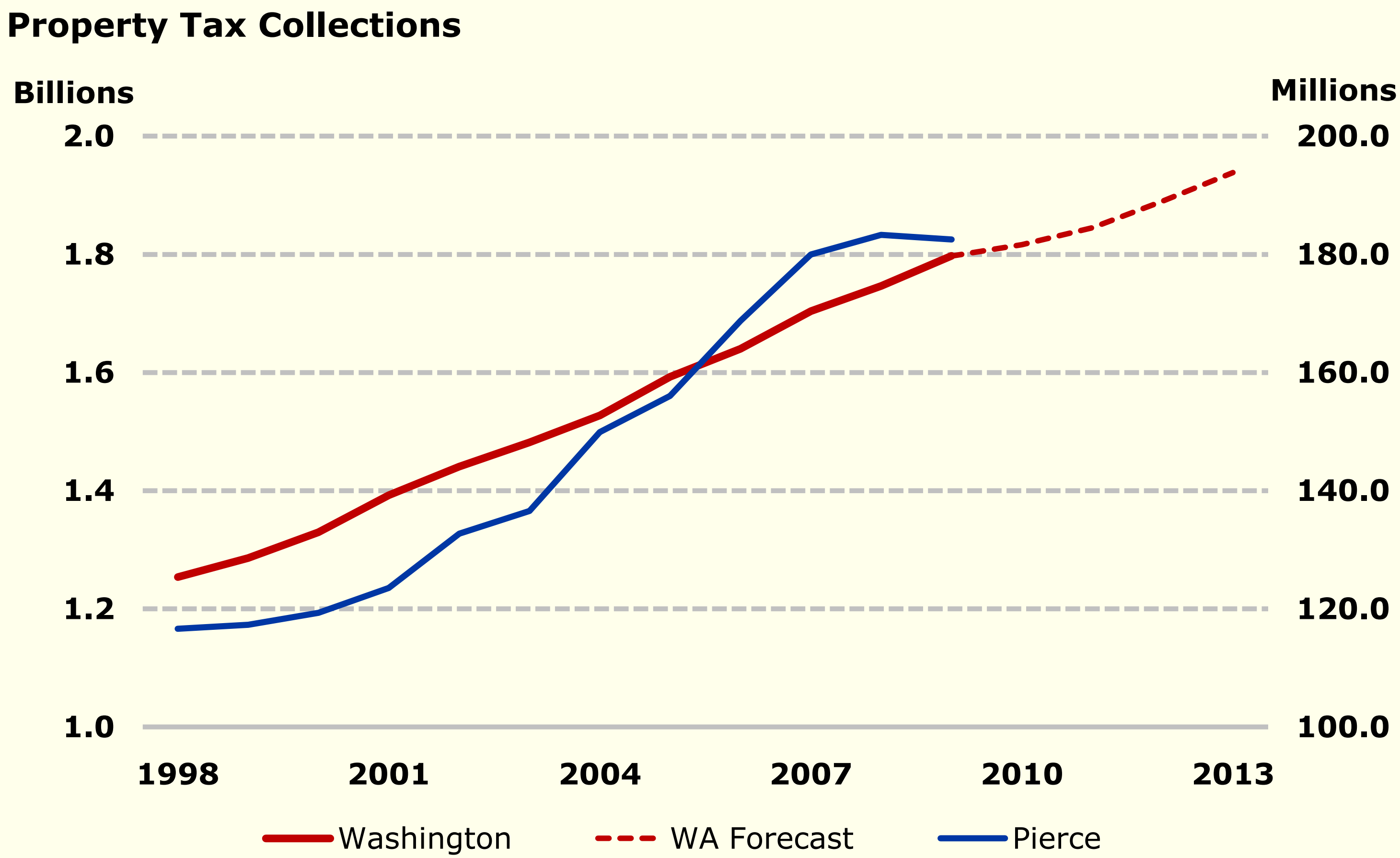
Property Tax collections in Pierce County have slowed, but should pick up along with the State

New Construction in Pierce County was down 42% in 2009 compared to down 35% for the state



Source: DOR; Data through February 2010

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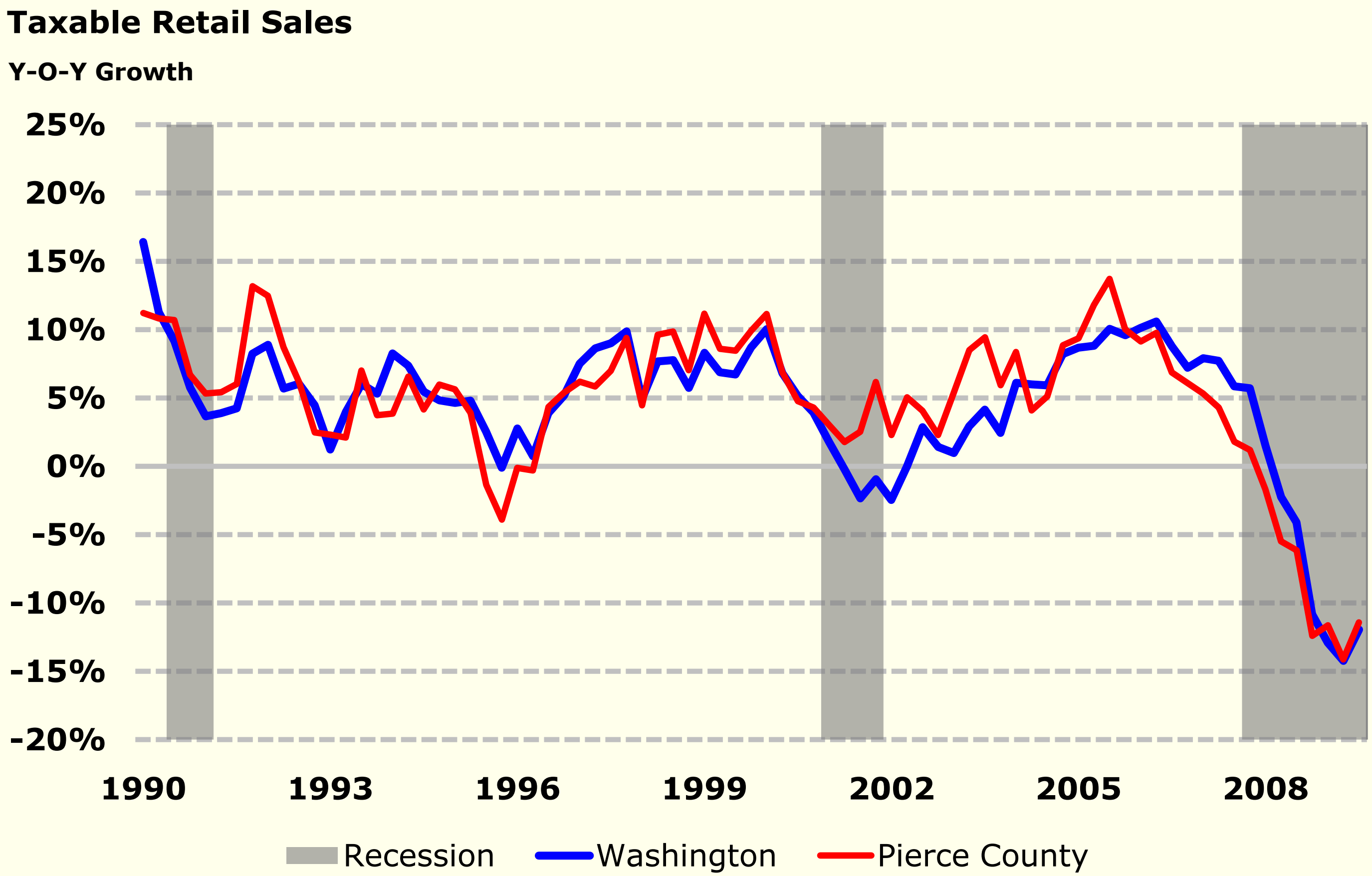
Downturn in Pierce County retail sales began slightly before state's but recovery has been similar

Pierce County taxable sales were negative year-over-year in first quarter of 2008; Washington sales turned negative in second quarter



Source: DOR; Data through 2009Q3

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Forecast changes: General Fund State, 2009-2011 Biennium

November Forecast:

$28,843 million

USD millions		**February '10 Forecast**			
	Collection Experience	Non-economic Change	Forecast Change	Forecast	Total Change*
Dept. of Revenue	$61	($150)	($52)	$27,245	($141)
All other agencies	$1	$0	$22	$1,479	$23
Total GF-S	**$61**	**($150)**	**($30)**	**$28,725**	**($118)**

* Detail may not add to total due to rounding

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Initial Forecast: General Fund State, 2011-2013 Biennium

USD millions

USD Millions

	Forecast
Dept. of Revenue	$30,658
All other agencies	$1,566
Total GF-S	**$32,224**

* Detail may not add to total due to rounding

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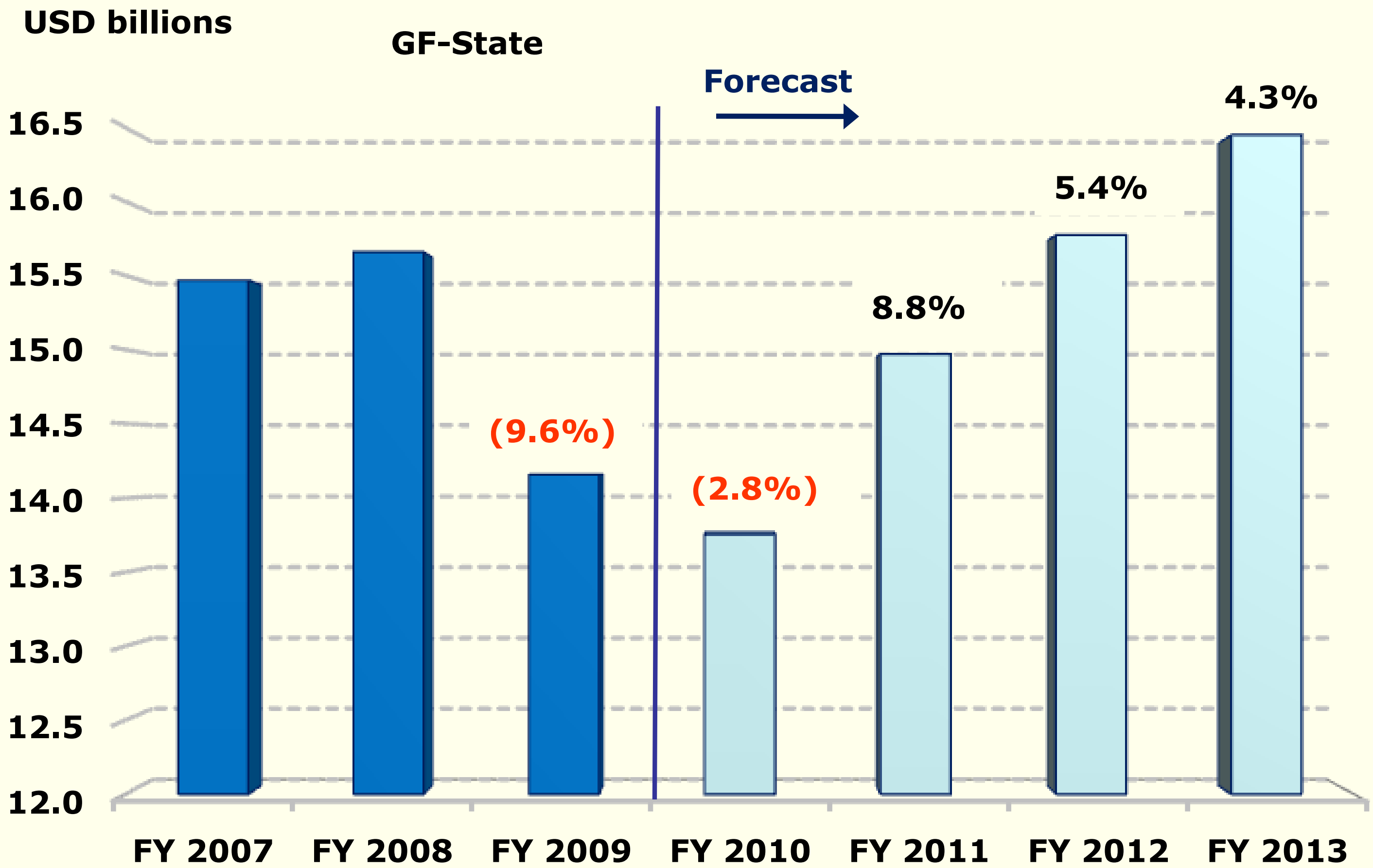
General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07, 08, and 09

General Fund – new definition, for FY 10-13



Source: ERFC forecast, February 2010

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Conclusion

<u>Pluses</u>

- Recovery in progress
- Employment likely to improve soon
- Car sales have stabilized
- Large banks able to extend credit

<u>Minuses</u>

- Problems at community banks
- Weak consumer confidence
- Slow recovery in construction

- Revenues have come in close to our November forecast, and are bumping along the bottom
- We expect 12.2% revenue growth in the 11-13 biennium compared to the current one

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Questions

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