

Economic and Revenue Update

Presented to
Economic Symposium

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November 22, 2013
Olympia, Washington



WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL



Summary

- The updated economic forecast is fairly similar to the September forecast, but with slightly slower growth in Washington housing construction
- Uncertainty in the baseline remains very high, mostly due to concerns about China, federal fiscal policy, housing affordability and Europe
- Washington employment has been slowly increasing in most sectors; aerospace and the federal government are exceptions
- The updated revenue forecast increases expected revenue by \$9 million in the 2011-13 biennium and by \$16 million in the 2013-15 biennium



Four major risks to the forecast



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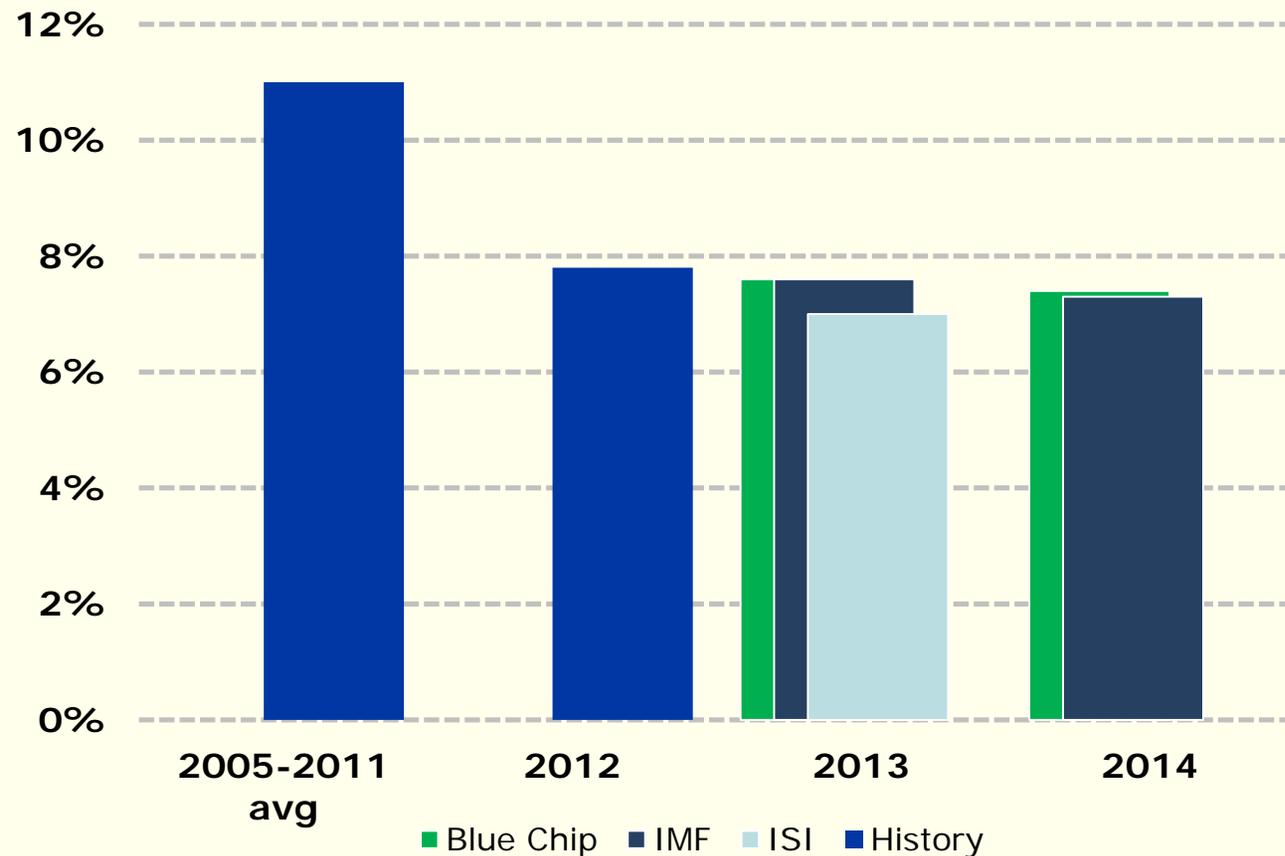
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Source: ERF

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China's 2014 GDP growth expected to be at or below 2013 rates



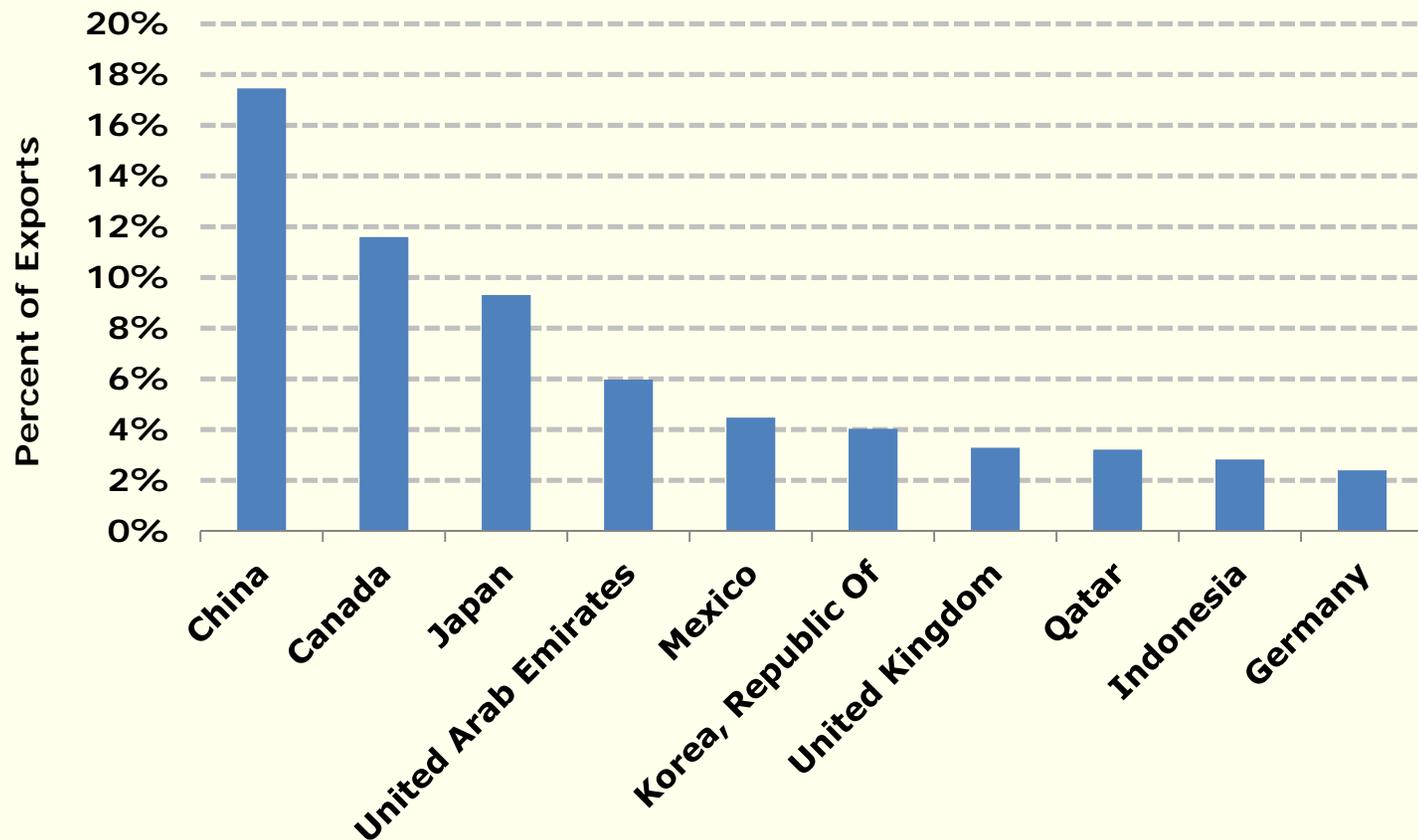
Source: Blue Chip, IMF, ISI; data and forecasts through October 2013

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China is Washington's largest export market

Top 10 export destinations, 2013 YTD



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Source: WISER Trade, data through July 2013

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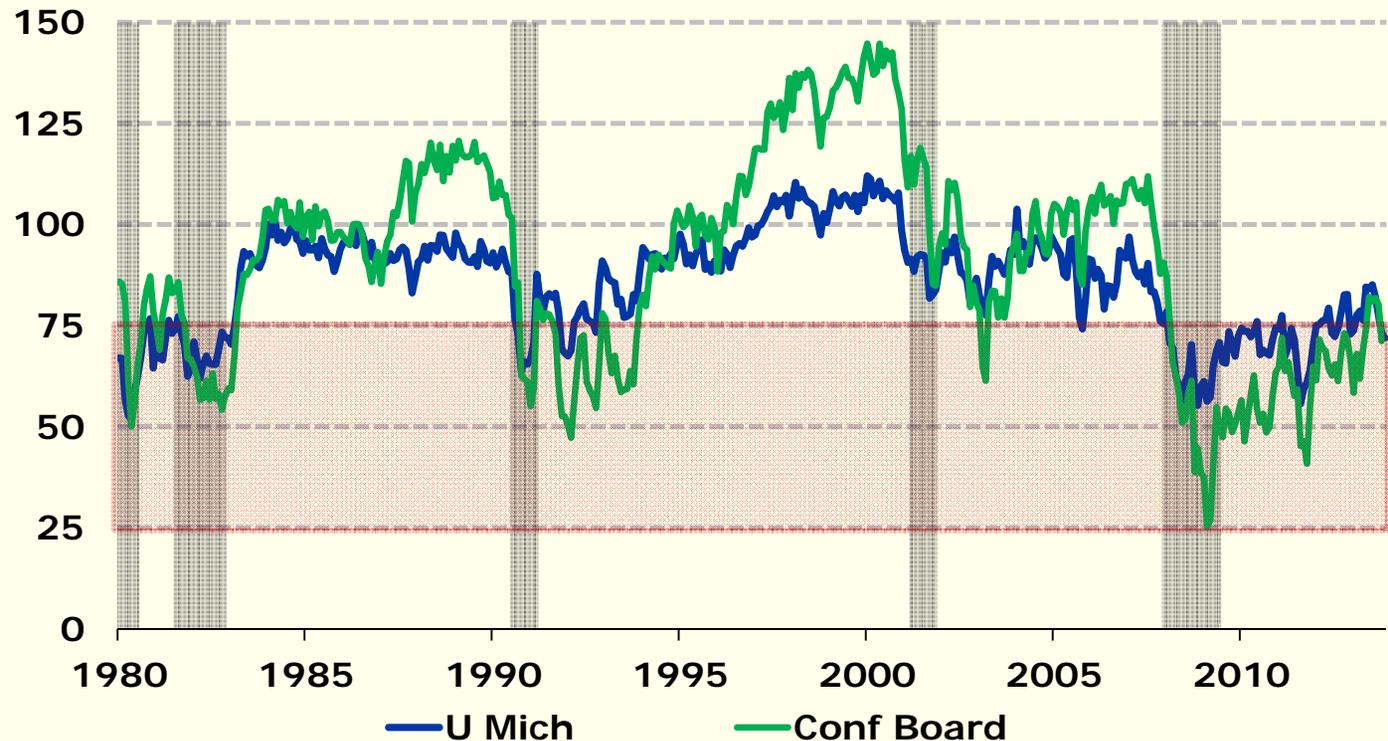


Consumer confidence weakened after the government shutdown

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Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA



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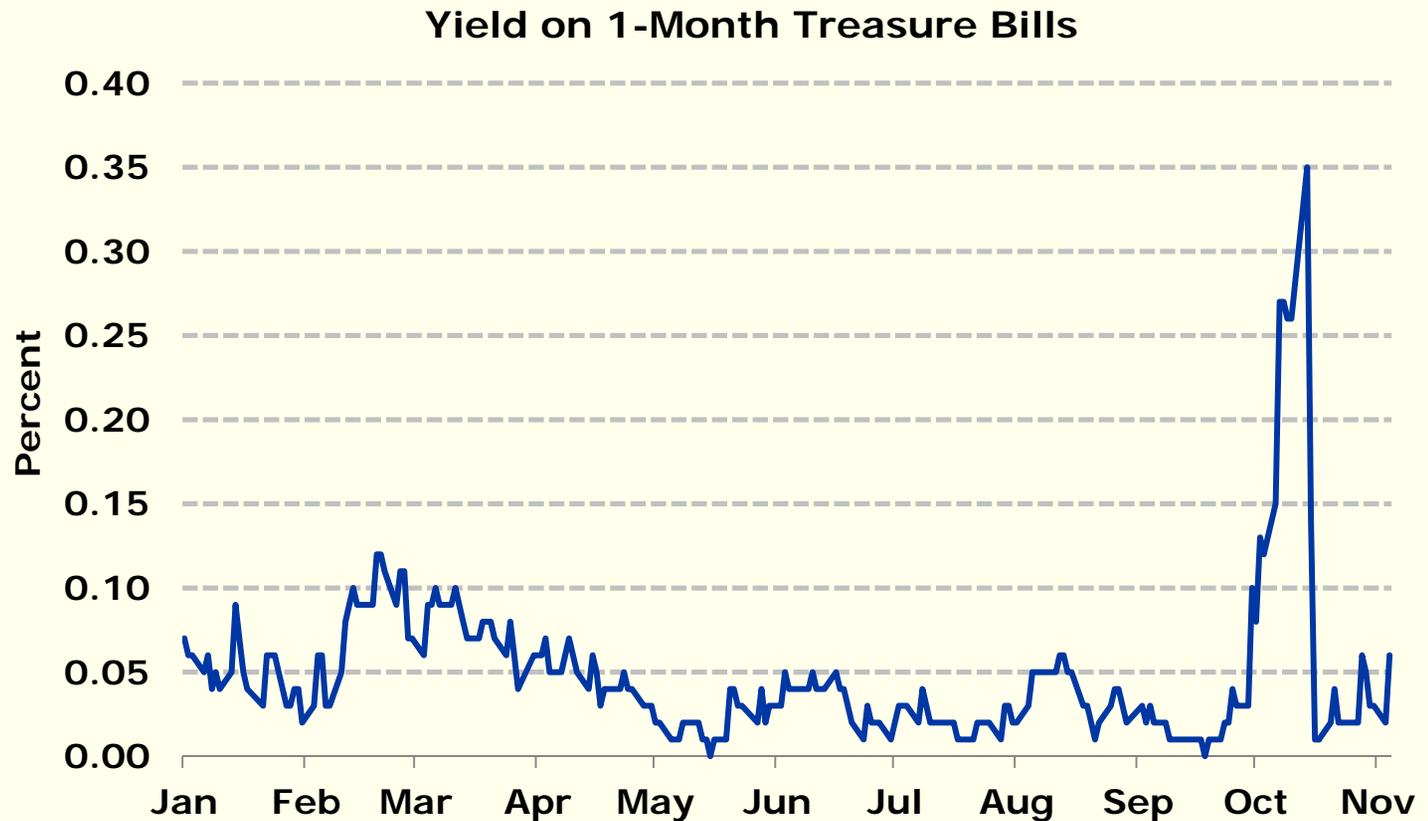
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Source: University of Michigan; Conference Board, data through November 2013

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Debt ceiling debate spiked short-term interest rates



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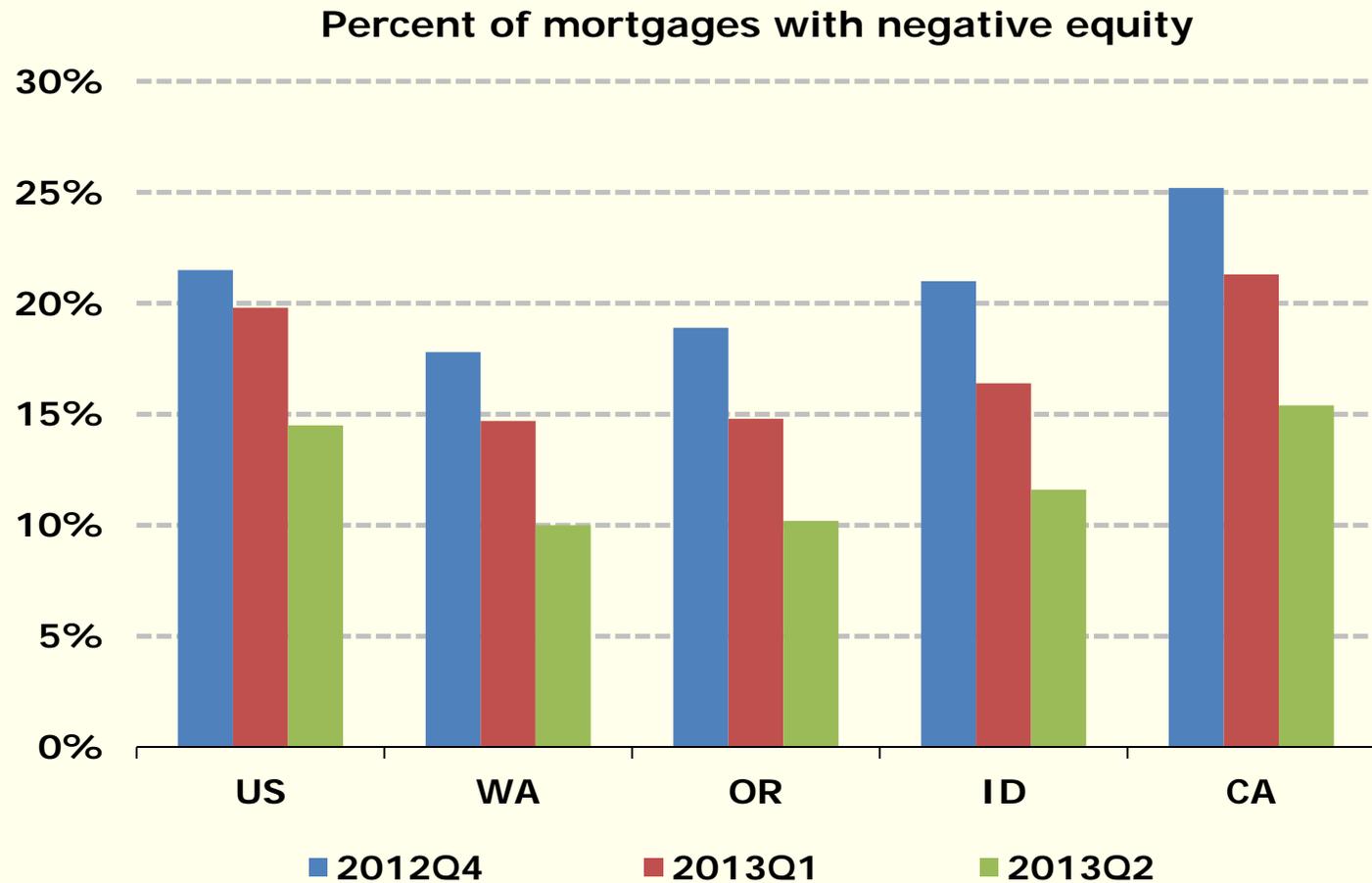
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Source: U.S. Treasury; data through November 5, 2013

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Rising home prices have reduced the number of underwater mortgages



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Source: CoreLogic, ERFC

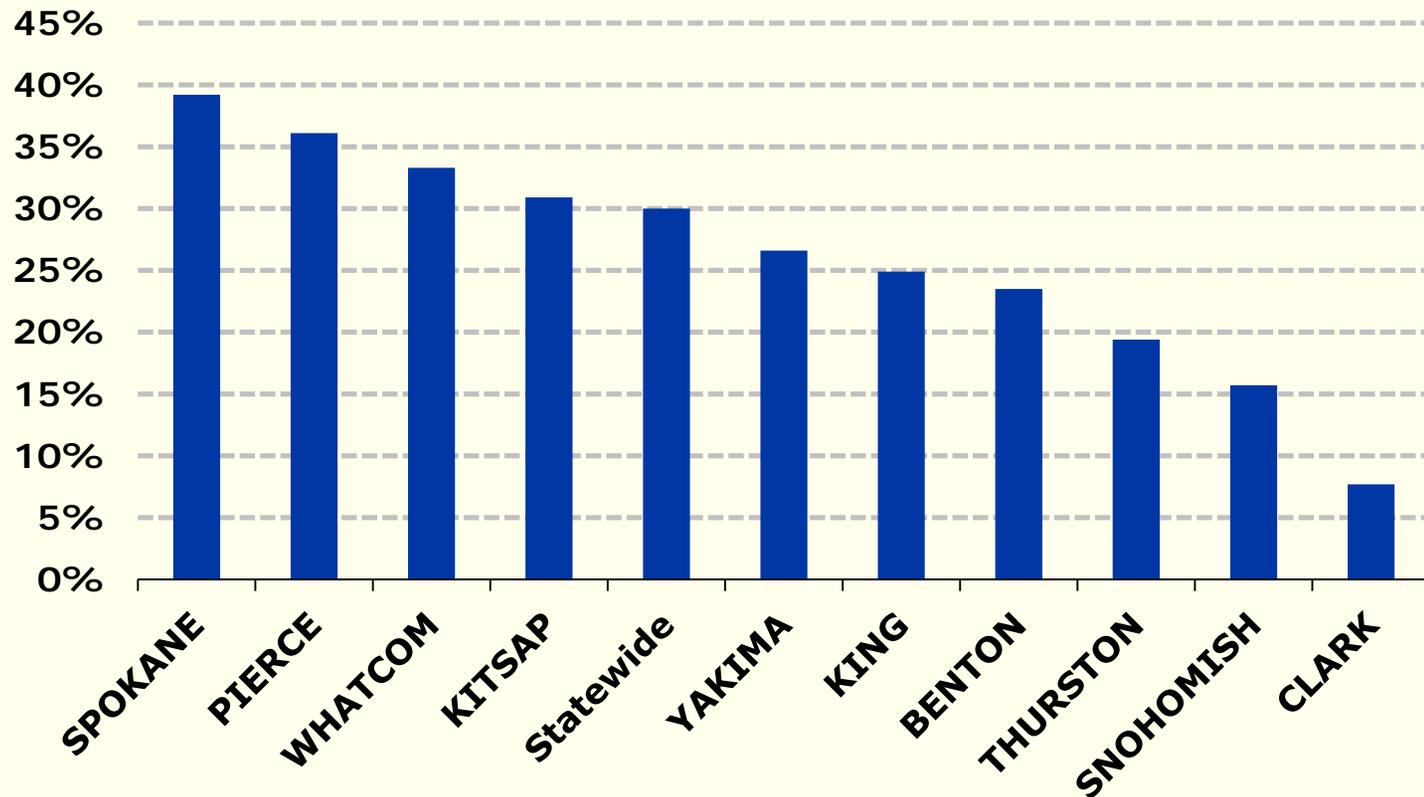
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Strong growth in existing home sales statewide

*Ten counties with highest existing home sales, 2013Q3

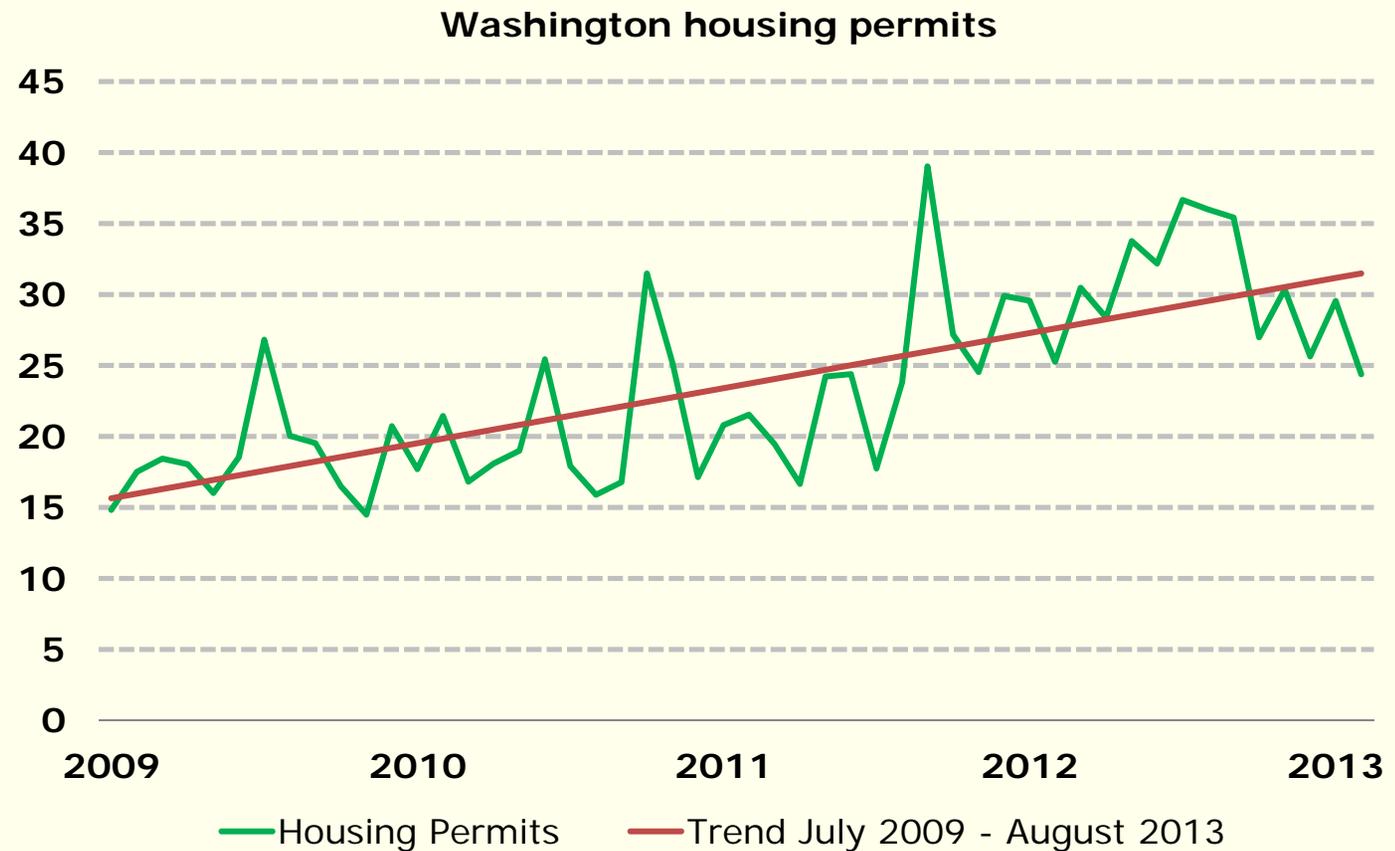
Existing Home Sales
Year over Year % Change*



Source: WA Center for Real Estate Research, ERFC; 2013Q3 data



Housing permits below trend since April 2013



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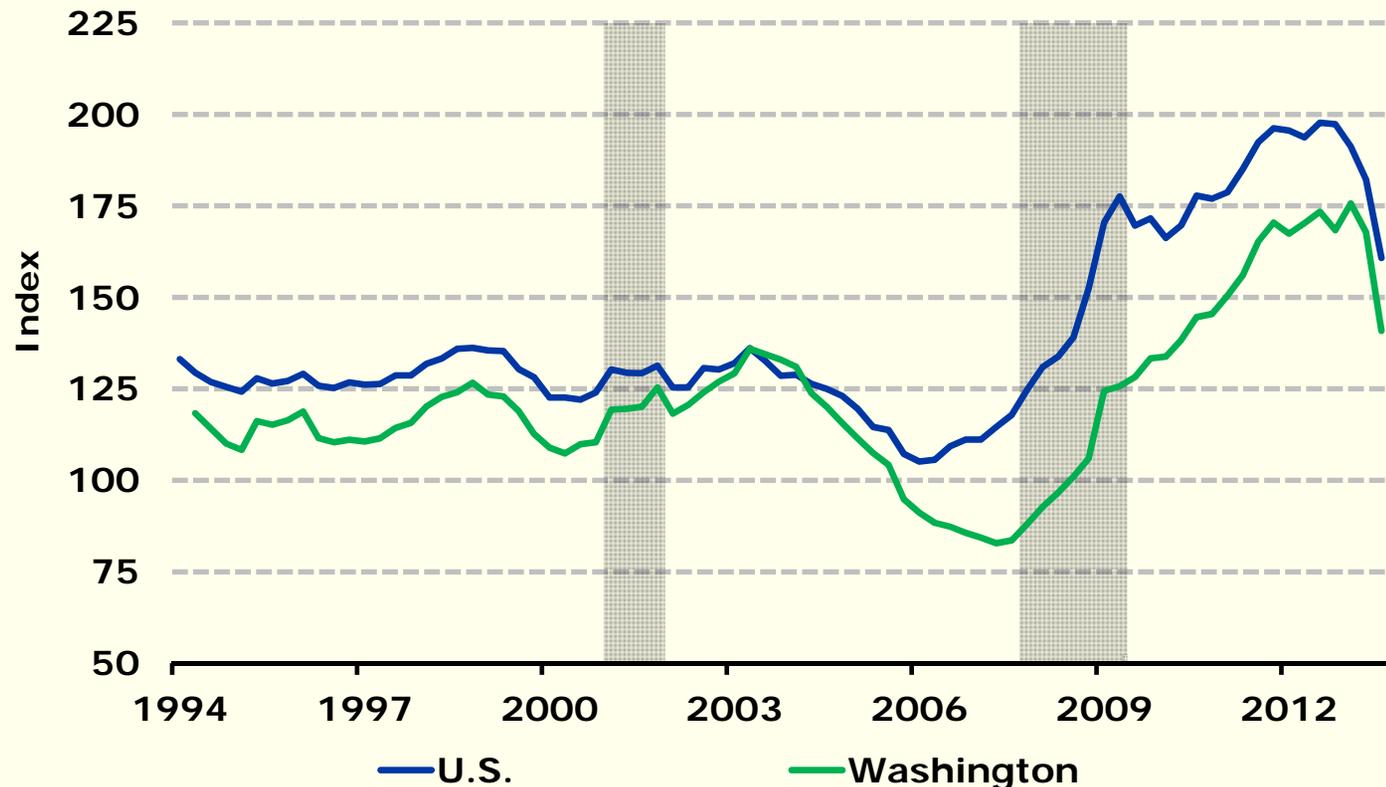
Source: U.S. Census; historical data through August 2013

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Rising mortgage rates and home prices have reduced affordability

Housing Affordability Index, SA



Source: Global Insight, WA Center Real Estate Research, ERFC; data through 2013Q3

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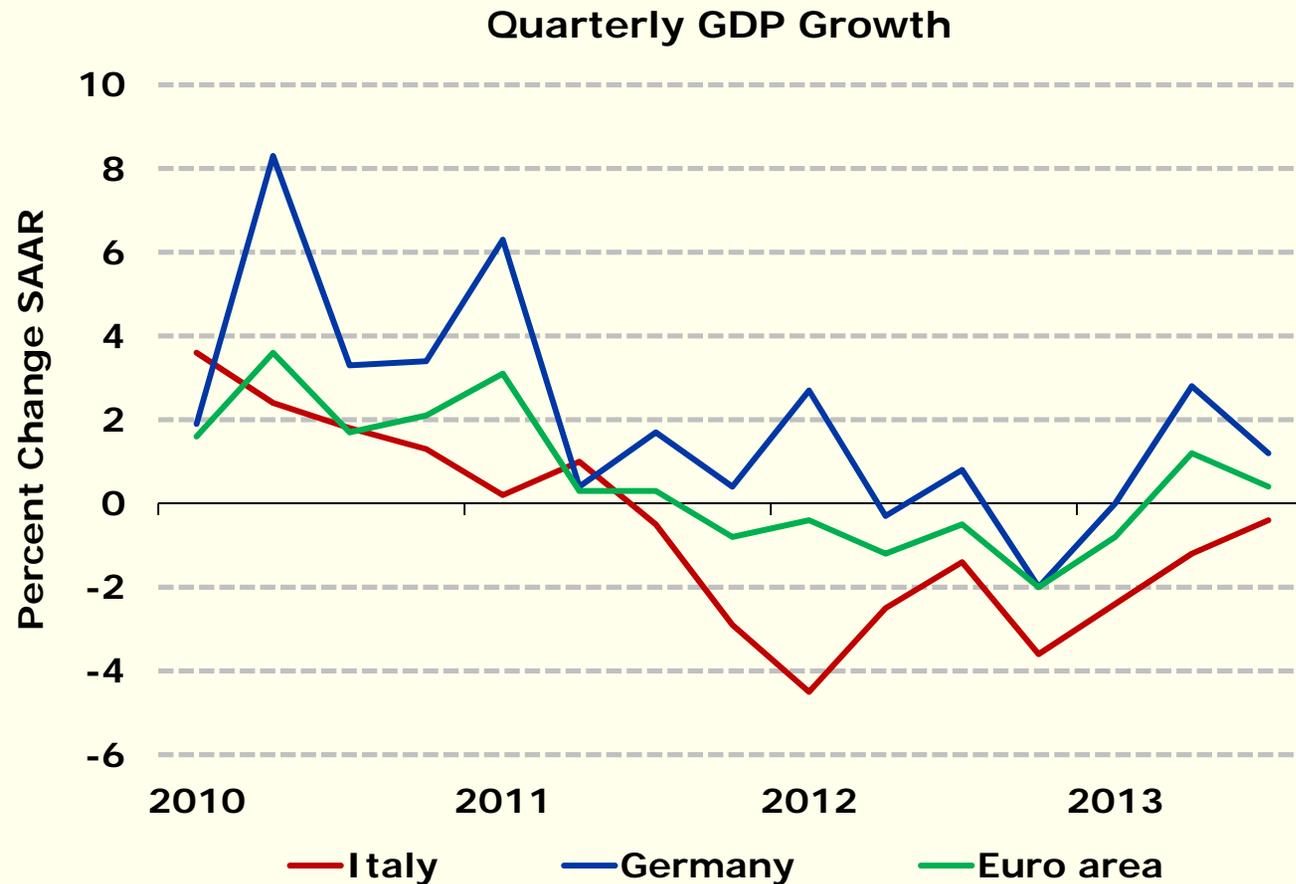


Euro area GDP has returned to positive growth

Eurozone
Forecast:

2013: -0.3%

2014: 1.0%



Source: Eurostat; data through 2013Q3

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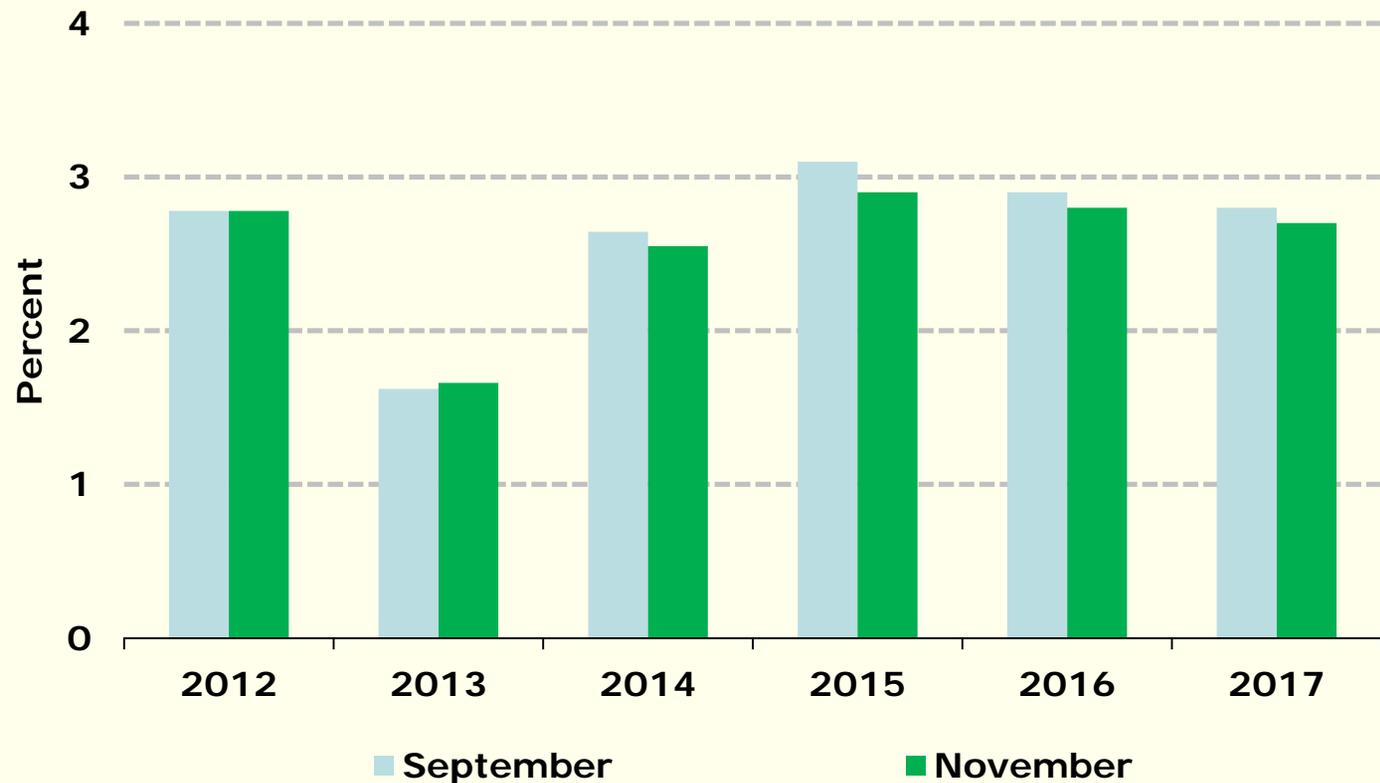
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U.S. GDP forecast slightly lower after 2013

Blue Chip Consensus Real GDP forecast



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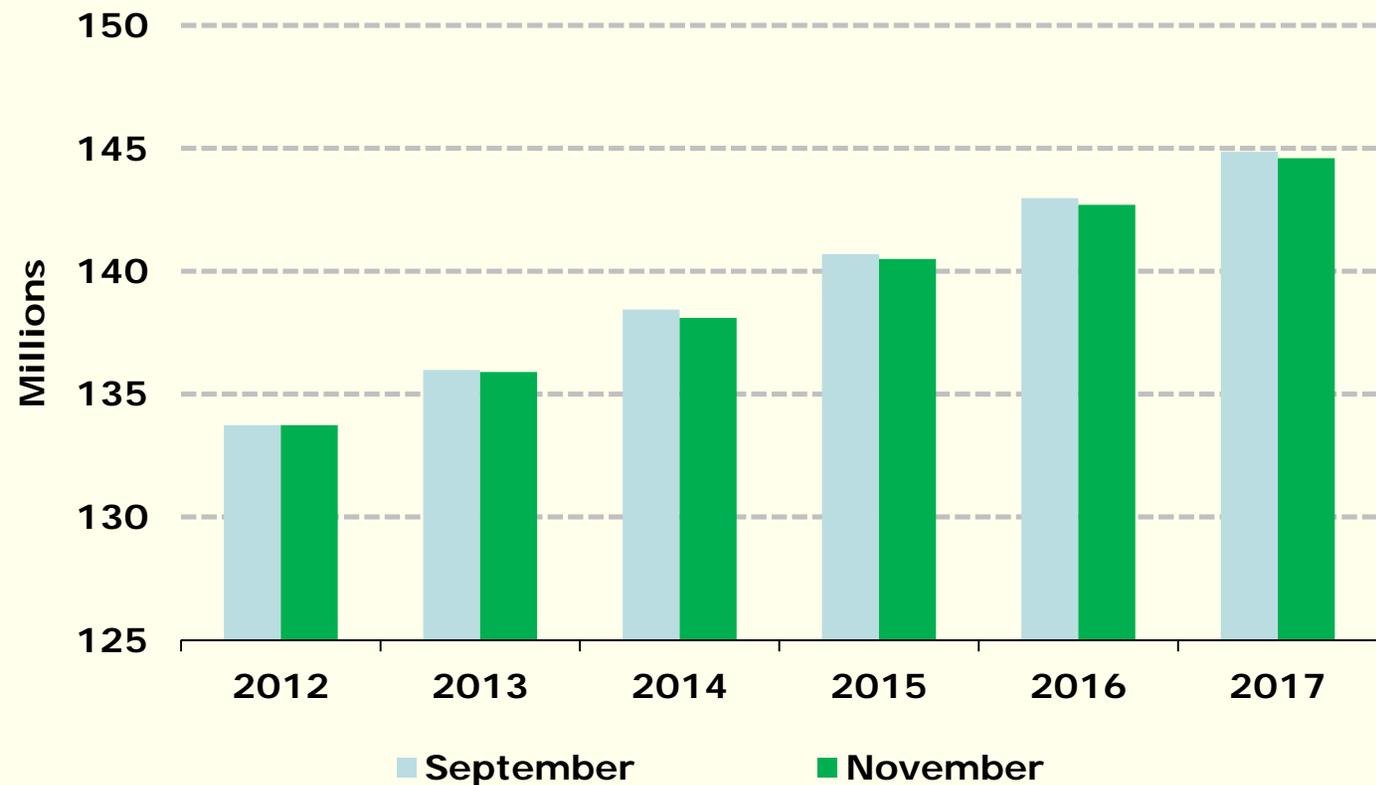
Source: BEA, Blue Chip Economic Indicators November 2013; historical data through 2012

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U.S employment forecast slightly lower

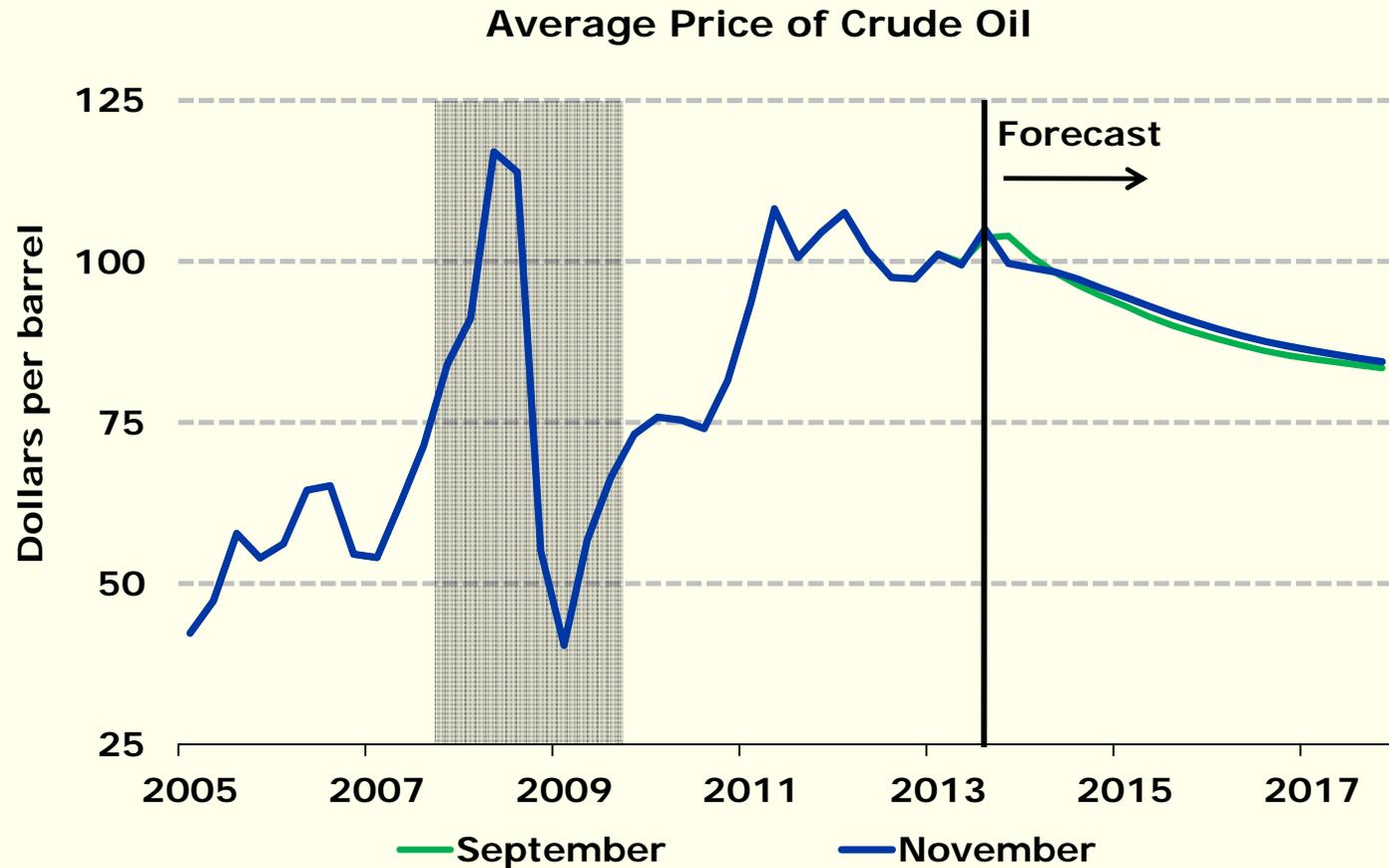
U.S. Total Nonfarm Employment



Source: BLS, ERFC November 2013 forecast; historical data through 2012



Oil prices are expected to be slightly lower in the near term



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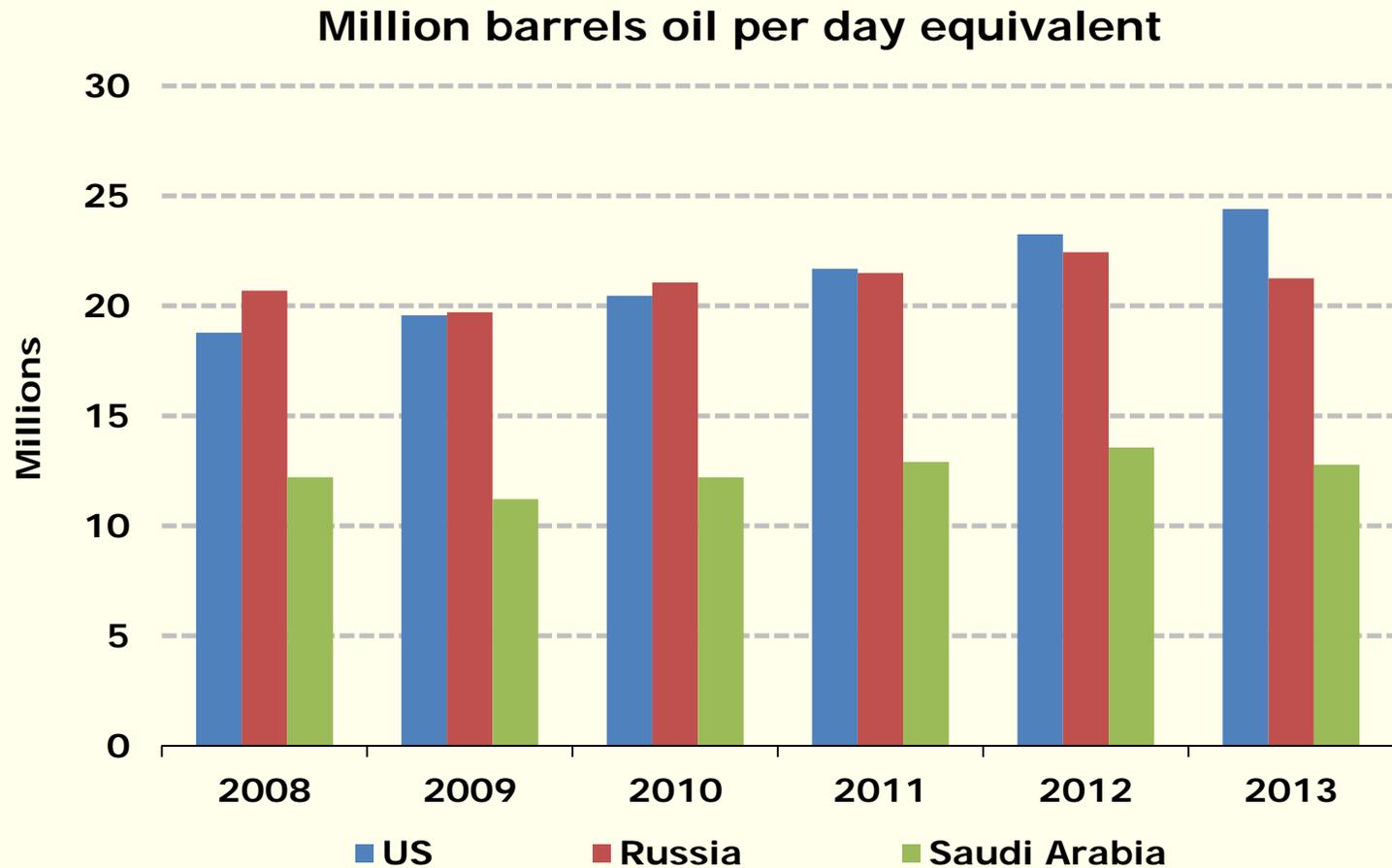
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Source: DOE, ERFC November 2013 forecast; historical data through 2013Q3

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U.S. expected to be top petroleum and natural gas producer in 2013



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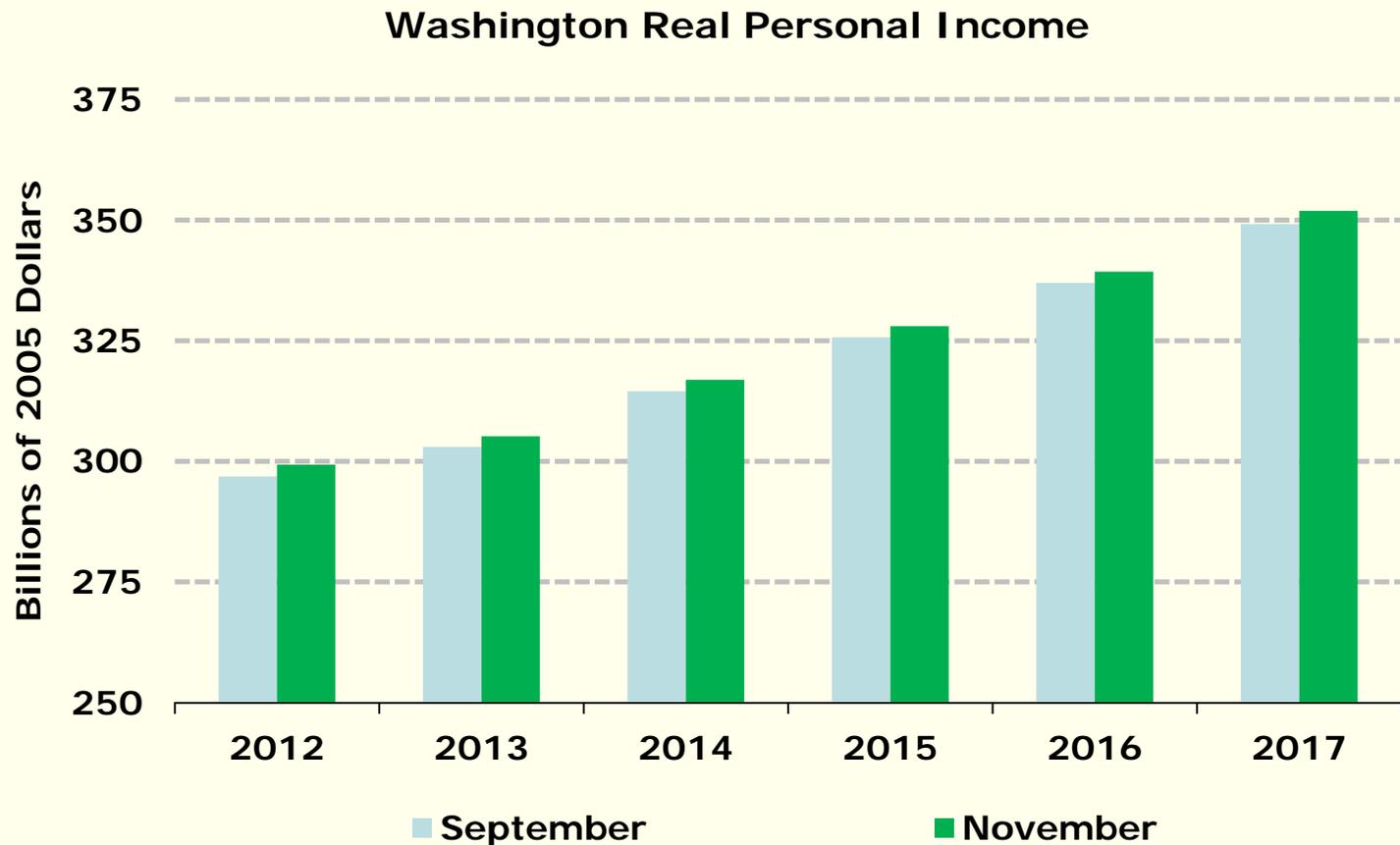
Source: U.S. Dept. of Energy; data through June 2013

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Washington real personal income forecast is slightly higher...

Recent comprehensive data revisions added \$2.9 billion to 2012 state personal income



Source: BEA, ERFC November 2013 Forecast; historical data through 2012

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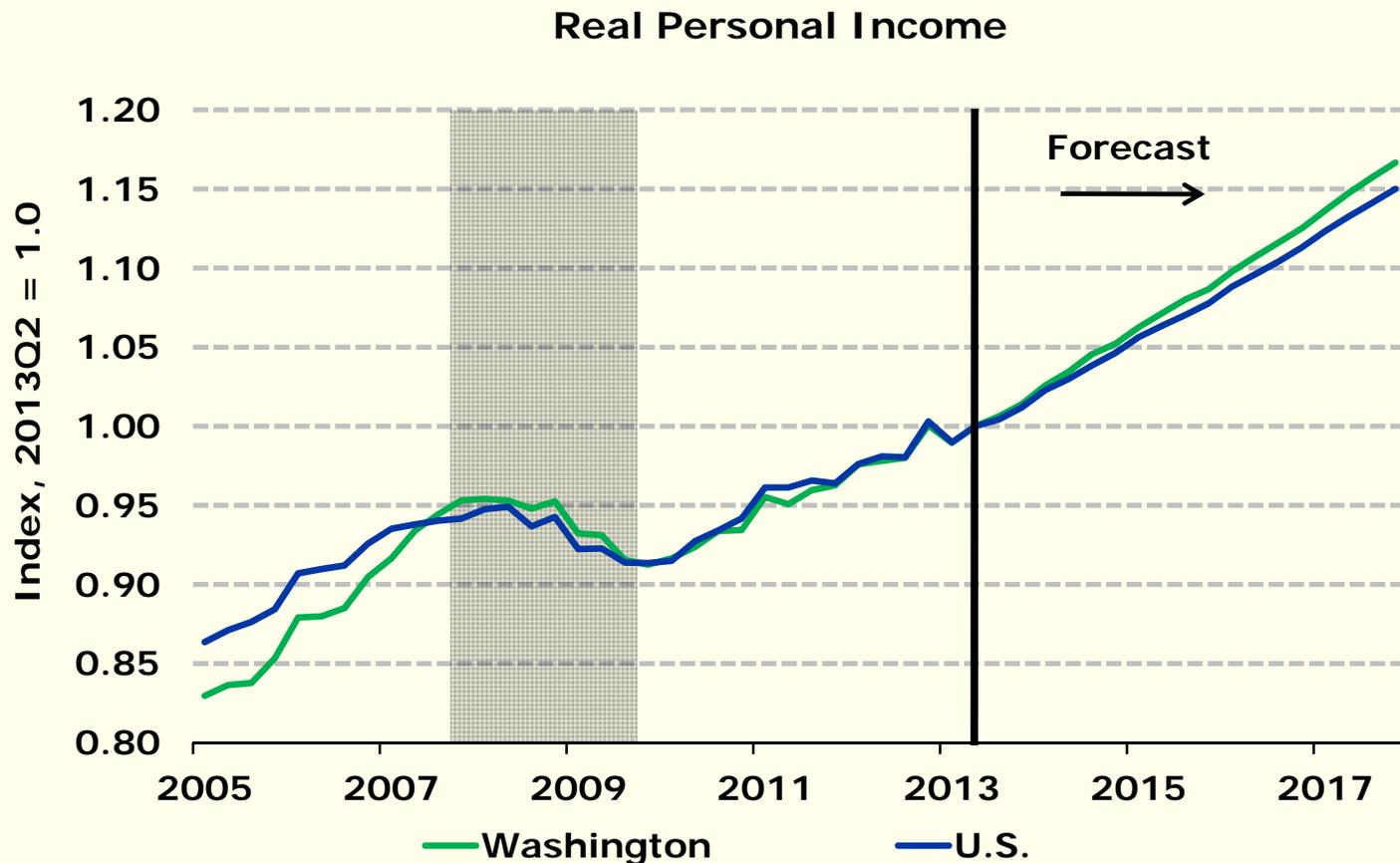
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...and state personal income will recover slightly faster than the U.S.



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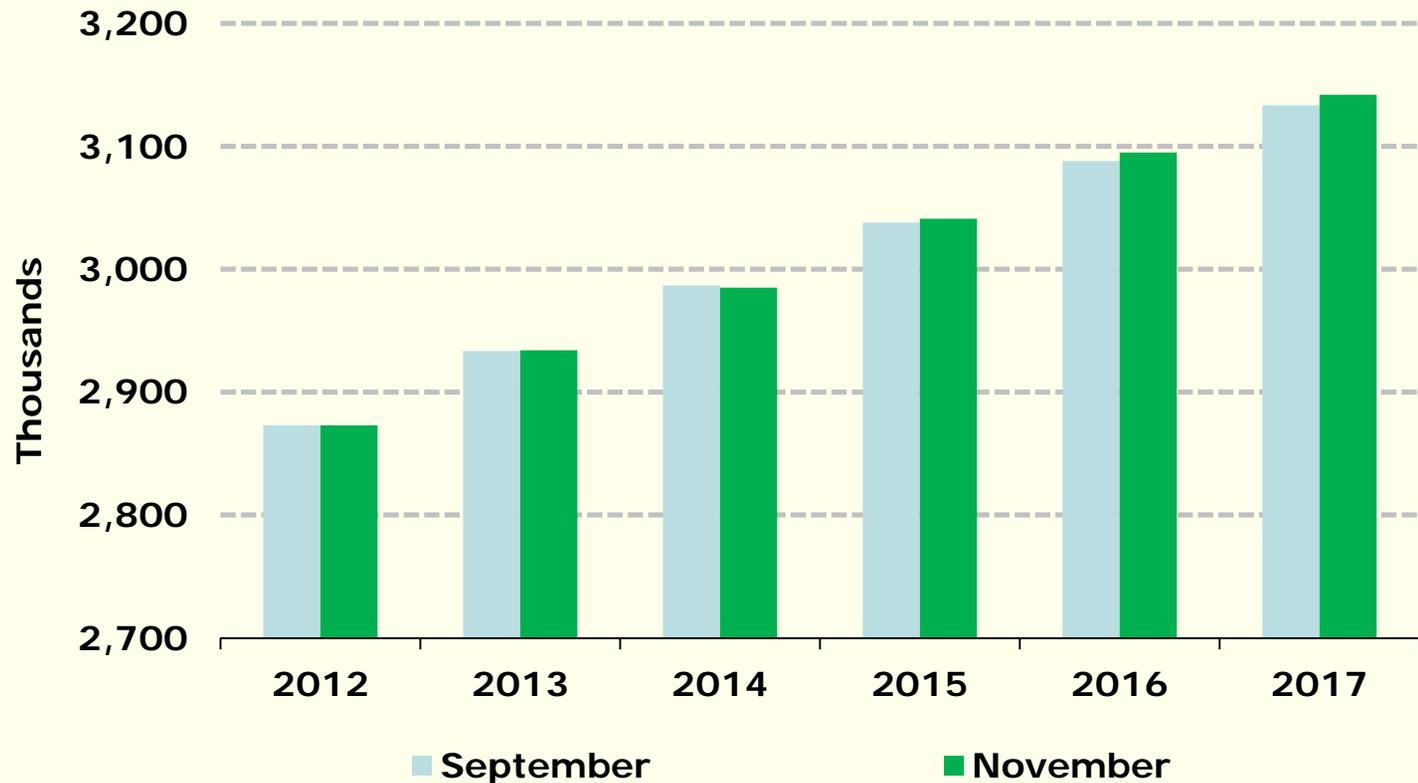
Source: ERFC November 2013 forecast; historical data through 2013Q2

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Washington payroll employment forecast is slightly higher after 2014

Washington Nonfarm Payroll Employment



Source: WA ESD, ERFC November 2013 forecast; historical data through 2012

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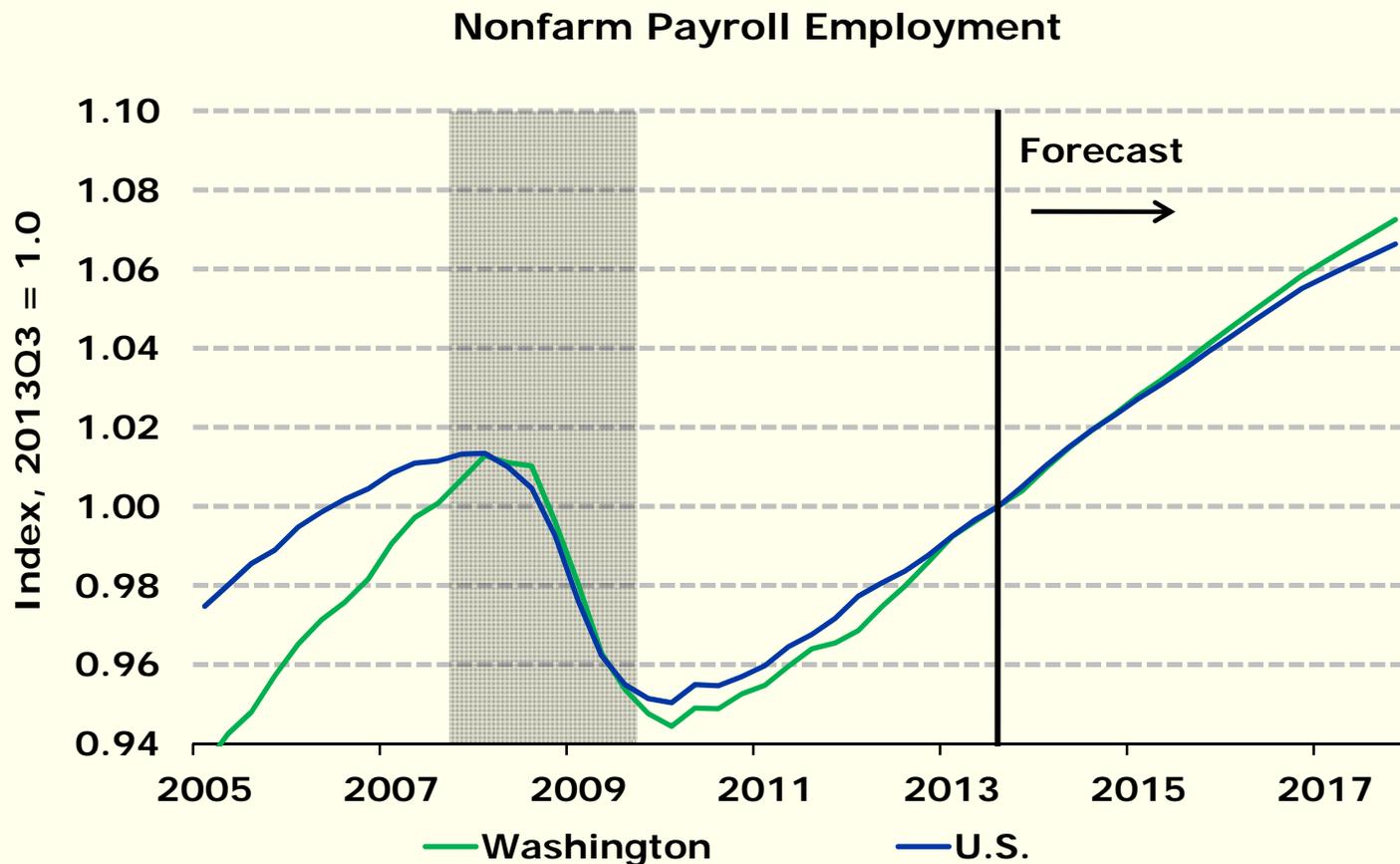


Washington employment will recover slightly faster than the U.S.

Date of regaining peak:

WA:
2014Q3

U.S.:
2014Q3



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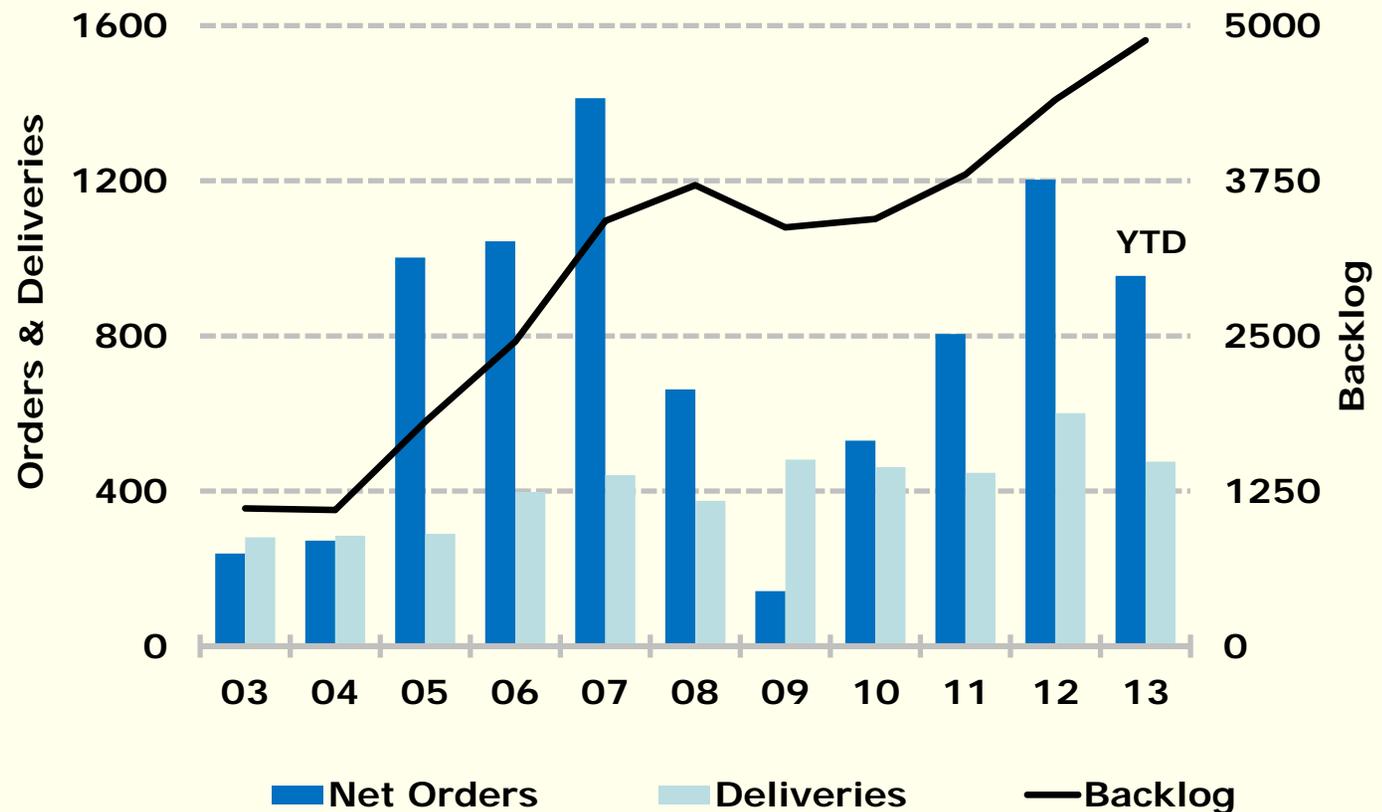
Source: ERFC November 2013 forecast; historical data through 2013Q3

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Boeing has over 7 years of commercial orders on its books

Excludes the military's new refueling tanker

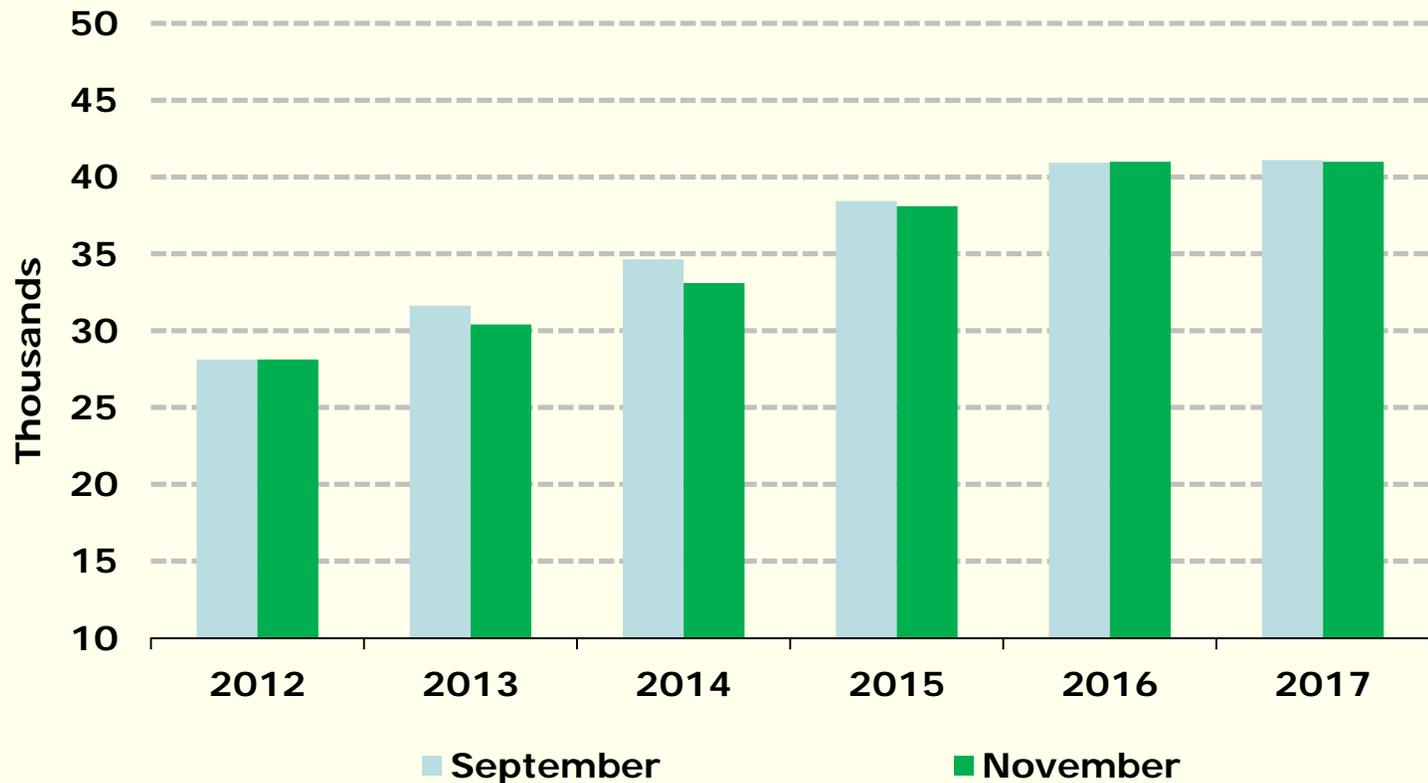


Source: Boeing, data through October 2013



Washington housing permits forecast is lower in the near term

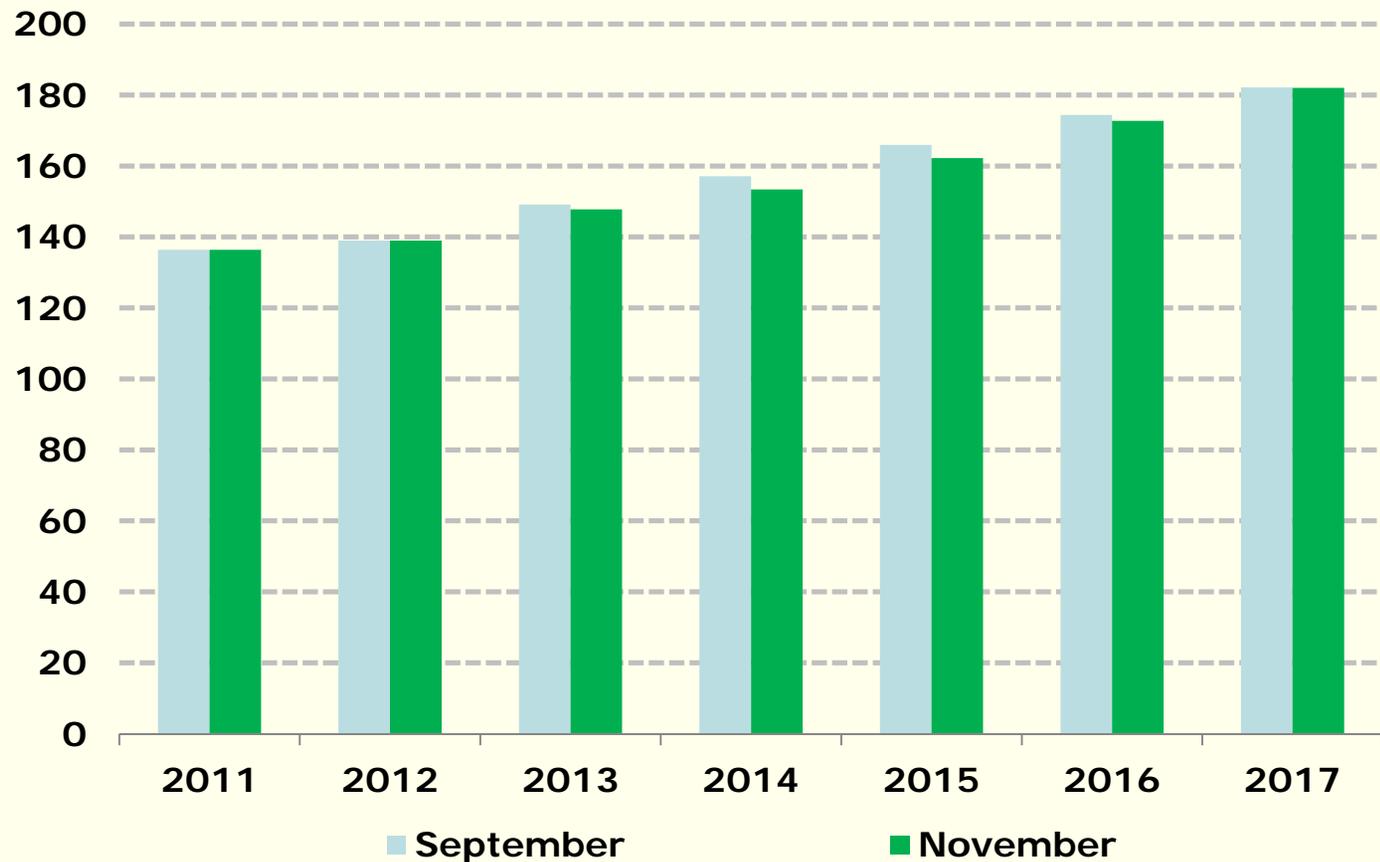
Washington Housing Permits



Source: U.S. Census, ERFC November 2013 forecast; historical data through 2012



Construction employment forecast is also slightly lower in the near term



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Source: WA ESD, ERFC November 2013 forecast; historical data through 2012

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Forecasted Revenue Act growth relative to income is above the long-term average...

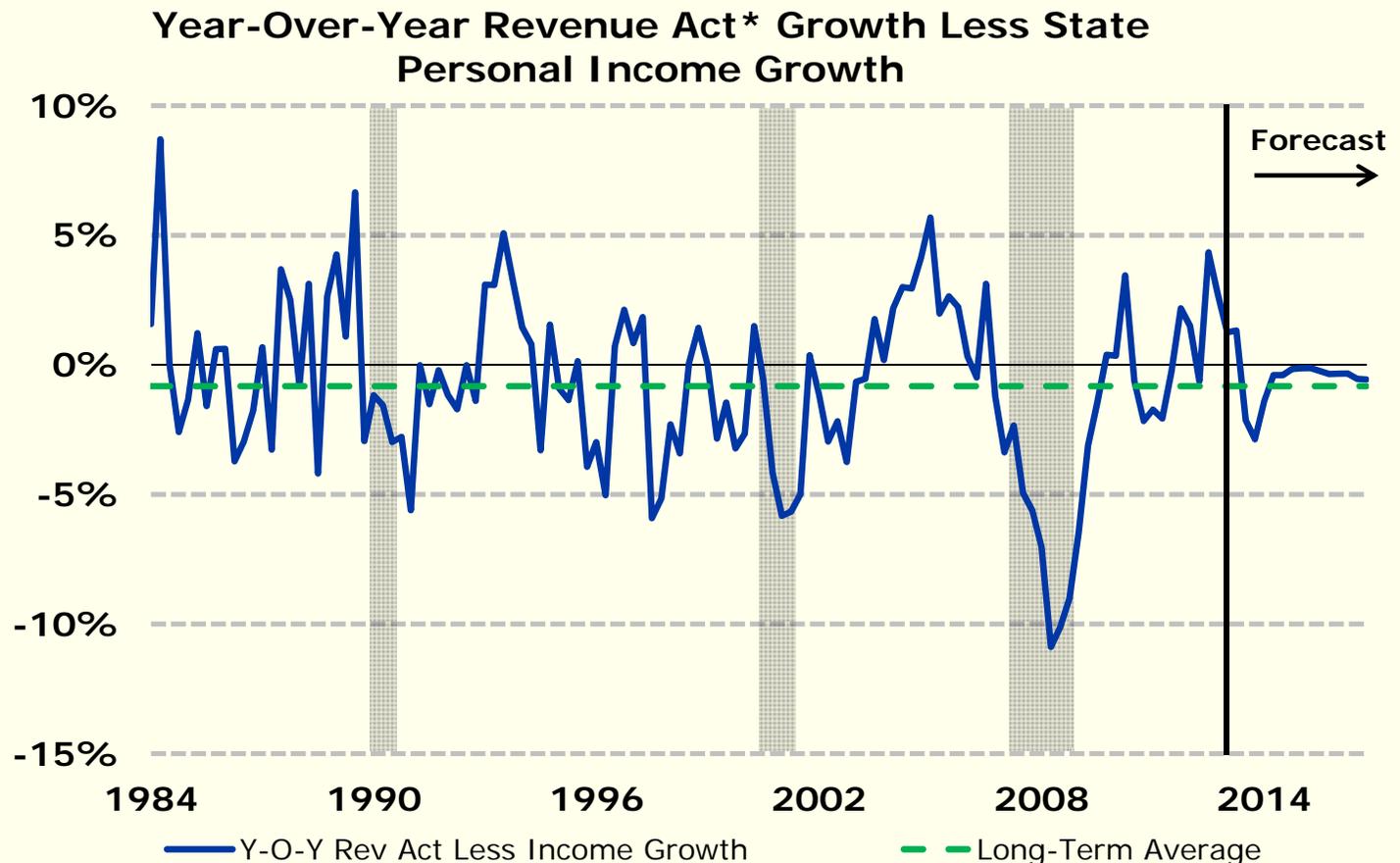
Revenue Act growth compared to income growth is forecasted to be slightly above the long-term average due to construction activity

The dip in the chart in mid-2013 through mid-2014 reflects the expiration of the B&O service tax surcharge

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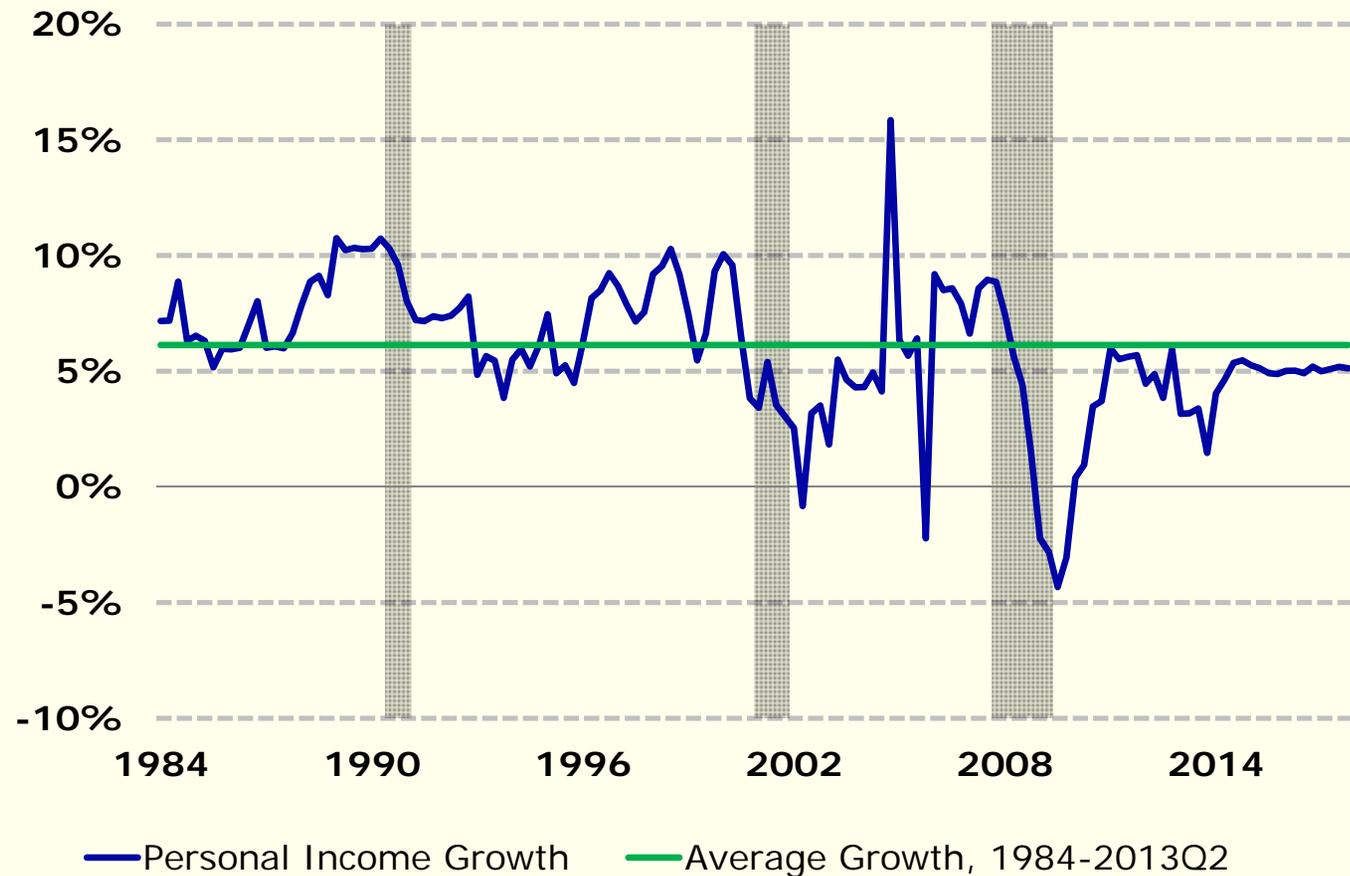
*Adjusted for large one-time payments and refunds and payments under the amnesty program

Source: ERFC; Quarterly revenue data through Q3 2013, November 2013 income estimates

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...but personal income is growing slowly



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Source: BEA, ERFC; historical data through 2013Q2

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Rev Act collections still above pre-recession peak despite surtax sunset

Seasonally adjusted collections increased slightly in the October 11th - November 10th collection period (September taxable activity)

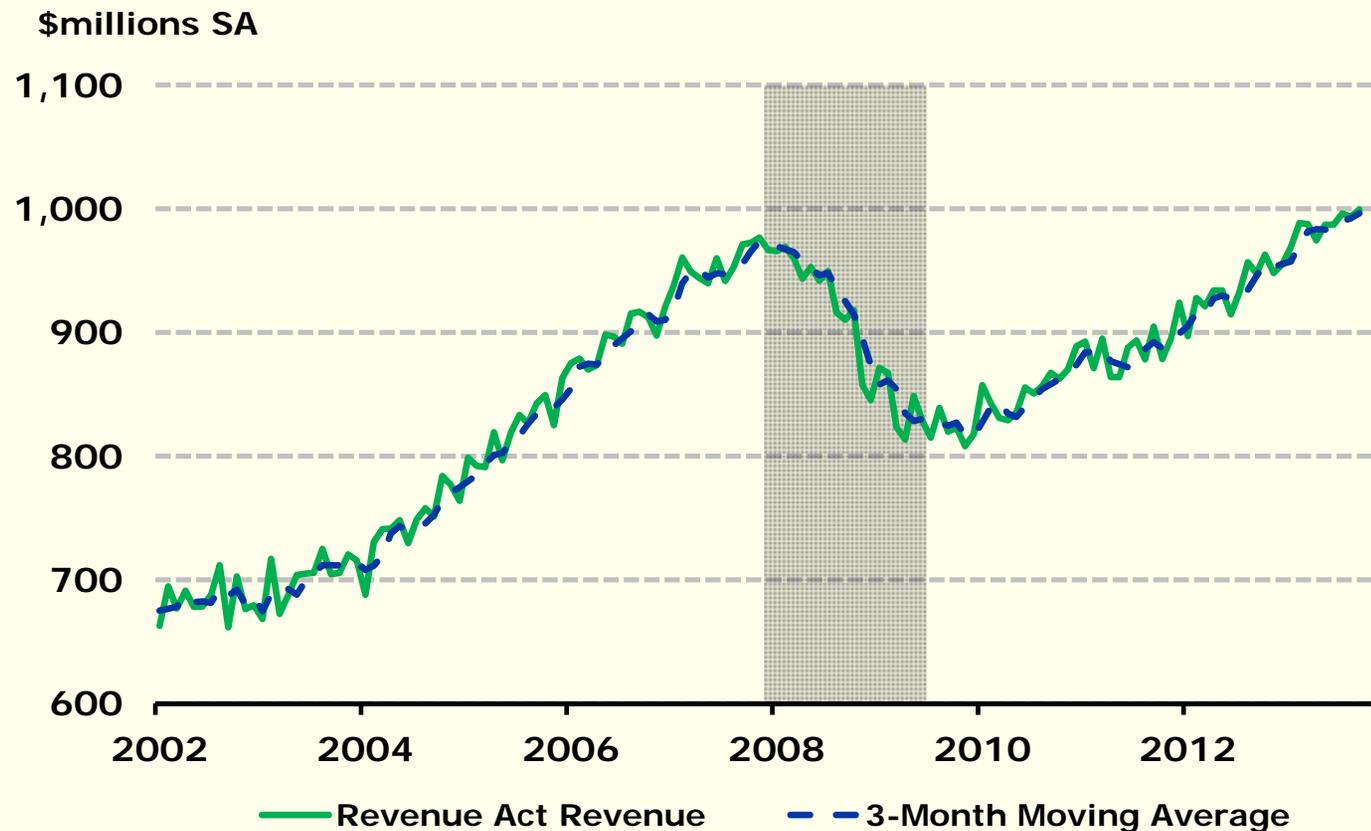
Collections in the previous period decreased due to the surtax sunset

The surtax brought in \$20-\$26 million per month

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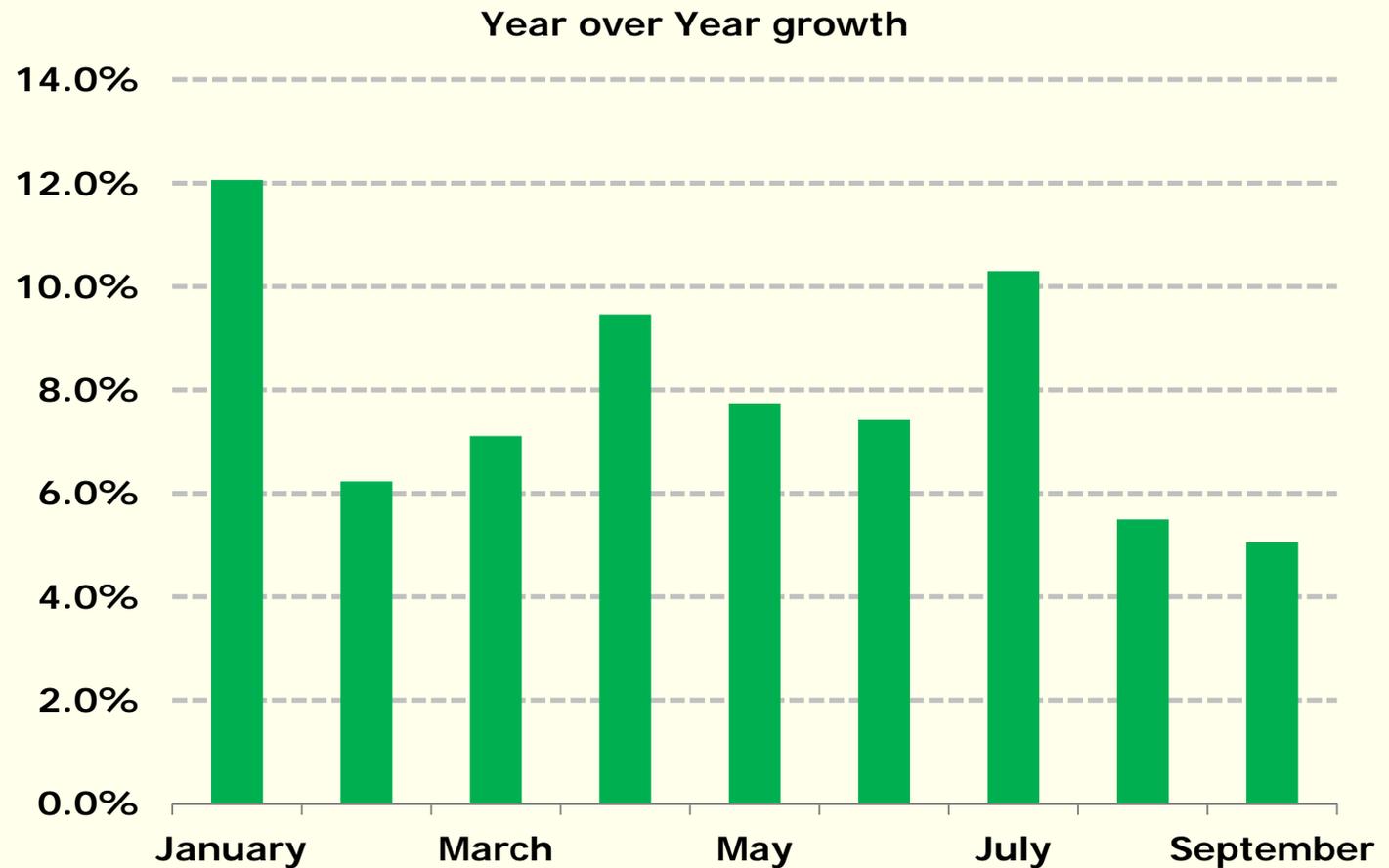
* Adjusted for large one-time transactions, amnesty payments and reporting frequency change, current definition of Revenue Act

Source: DOR and ERFC; monthly data through estimated September 2013 activity

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Sales tax growth has slowed in last two months



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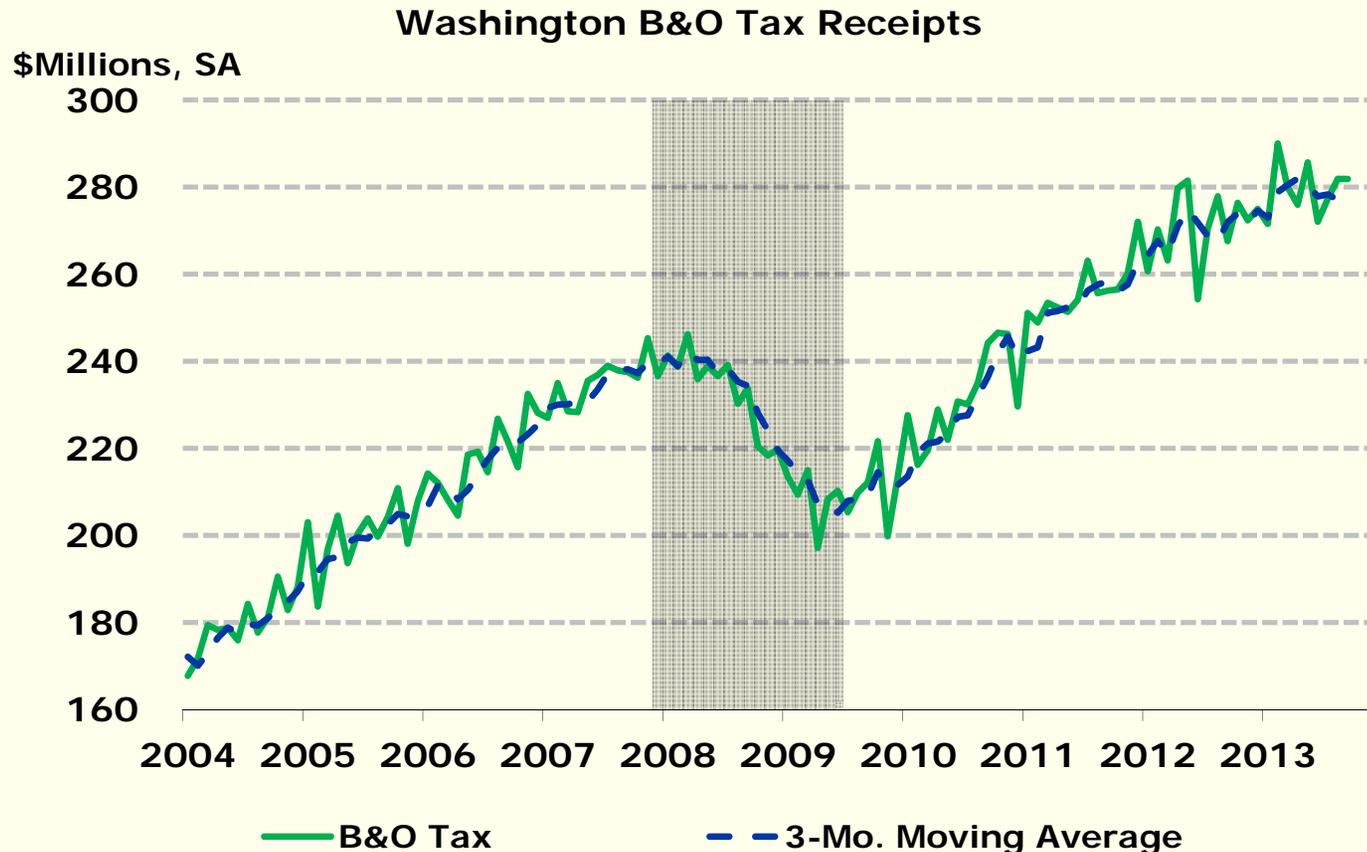
Source: ERFC; data for economic activity through September 2013

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September B&O collections show effects of service surcharge removal

The 0.3% B&O service tax surcharge, effective May 1, 2010 – June 30, 2013, generated \$20-\$25 million in taxes per month over the last fiscal year



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Source: ERFC; Monthly data through September 2013 preliminary activity
Adjusted for taxpayer frequency shift, amnesty payments, and recent large refunds

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Underlying REET trend positive with occasional spikes in commercial sales

While the residential market has strengthened, investor interest in commercial property has brought several months of elevated large commercial sales

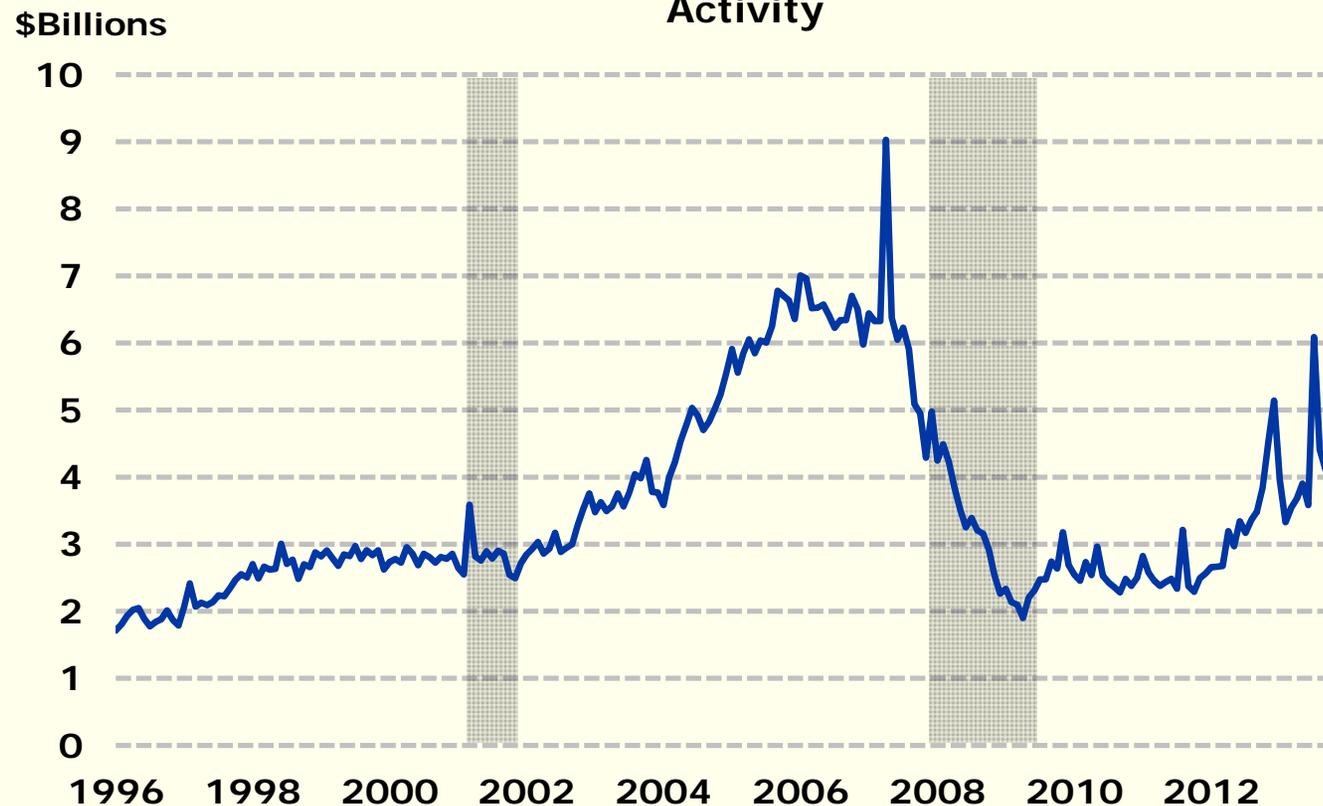
September sales of property worth \$10 million or more totaled \$222 million while October's sales totaled \$1 billion

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Seasonally Adjusted Taxable Real Estate Excise Activity



Source: ERFC; Monthly data through October 2013 preliminary

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Total changes: General Fund State, Education Legacy Trust Account, and WA Opportunity Pathways Account

**2011-13
Biennium**

Final Totals

\$Millions	<u>Non-econ Change</u>	<u>Nov. Forecast Change</u>	<u>Nov. Forecast</u>	<u>Total Change</u> *	<u>Total Resource Change</u> *
General Fund-State	(\$22)	\$9	\$30,657	(\$13)	\$9
Education Legacy Trust	(\$0)	\$0	\$215	(\$0)	(\$0)
WA Opportunity Pathways Account	\$0	(\$0)	\$244	(\$0)	(\$0)
Total	(\$22)	\$9	\$31,116	(\$13)	\$9

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* Detail may not add to total due to rounding

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Total changes: General Fund State, Education Legacy Trust Account, and WA Opportunity Pathways Account

**2013-15
Biennium**

\$Millions	<u>Non-econ Change</u>	<u>Nov. Forecast Change</u>	<u>Nov. Forecast</u>	<u>Total Change</u> *	<u>Total Resource Change</u> *
General Fund-State	(\$30)	\$6	\$32,973	(\$25)	\$16
Education Legacy Trust	\$0	\$13	\$377	\$13	\$13
WA Opportunity Pathways Account	\$0	(\$8)	\$229	(\$8)	(\$8)
Total	(\$30)	\$11	\$33,589	(\$19)	\$21

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* Detail may not add to total due to rounding

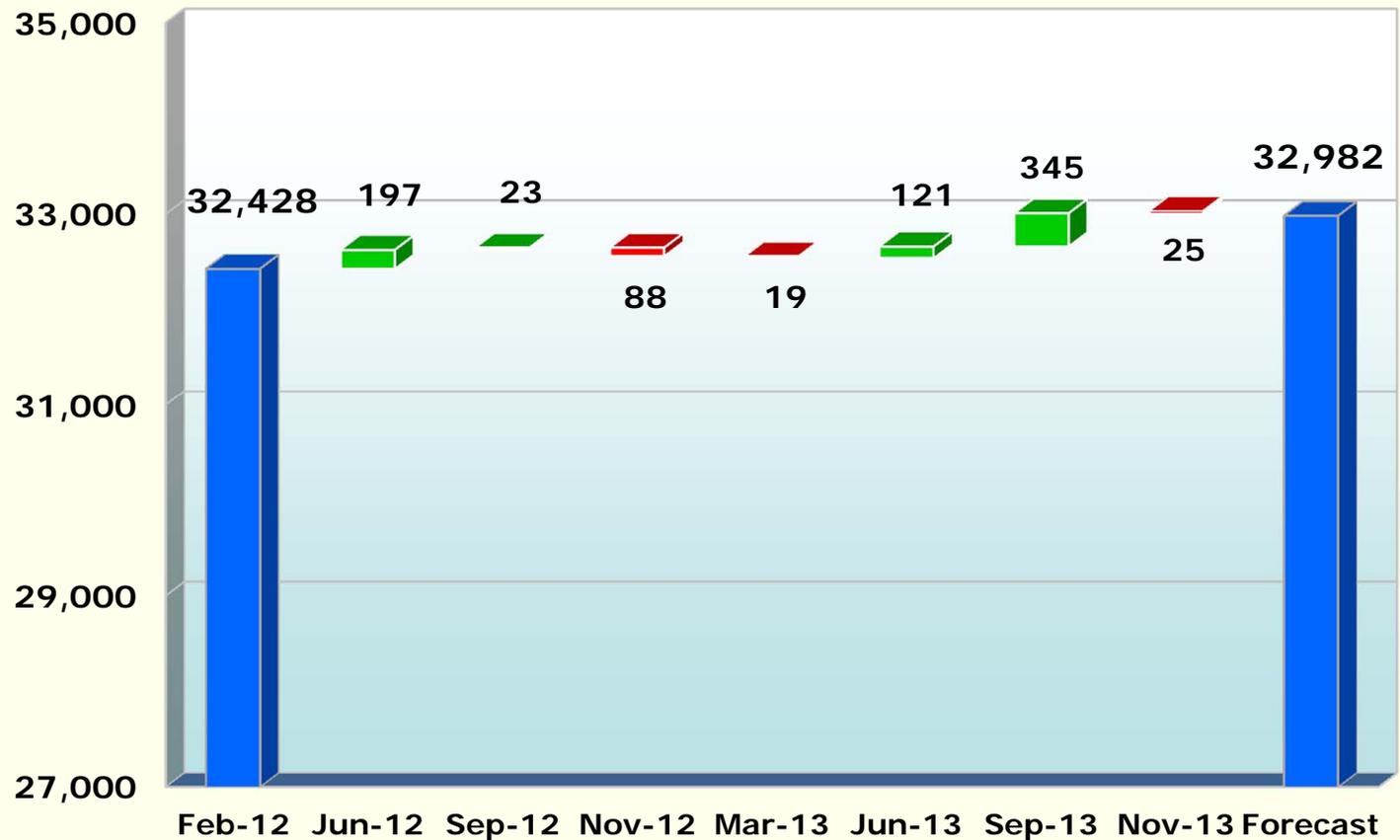
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GF-S forecast revisions to the 2013-15 biennium

**GF-S
New
Definition**

\$Millions



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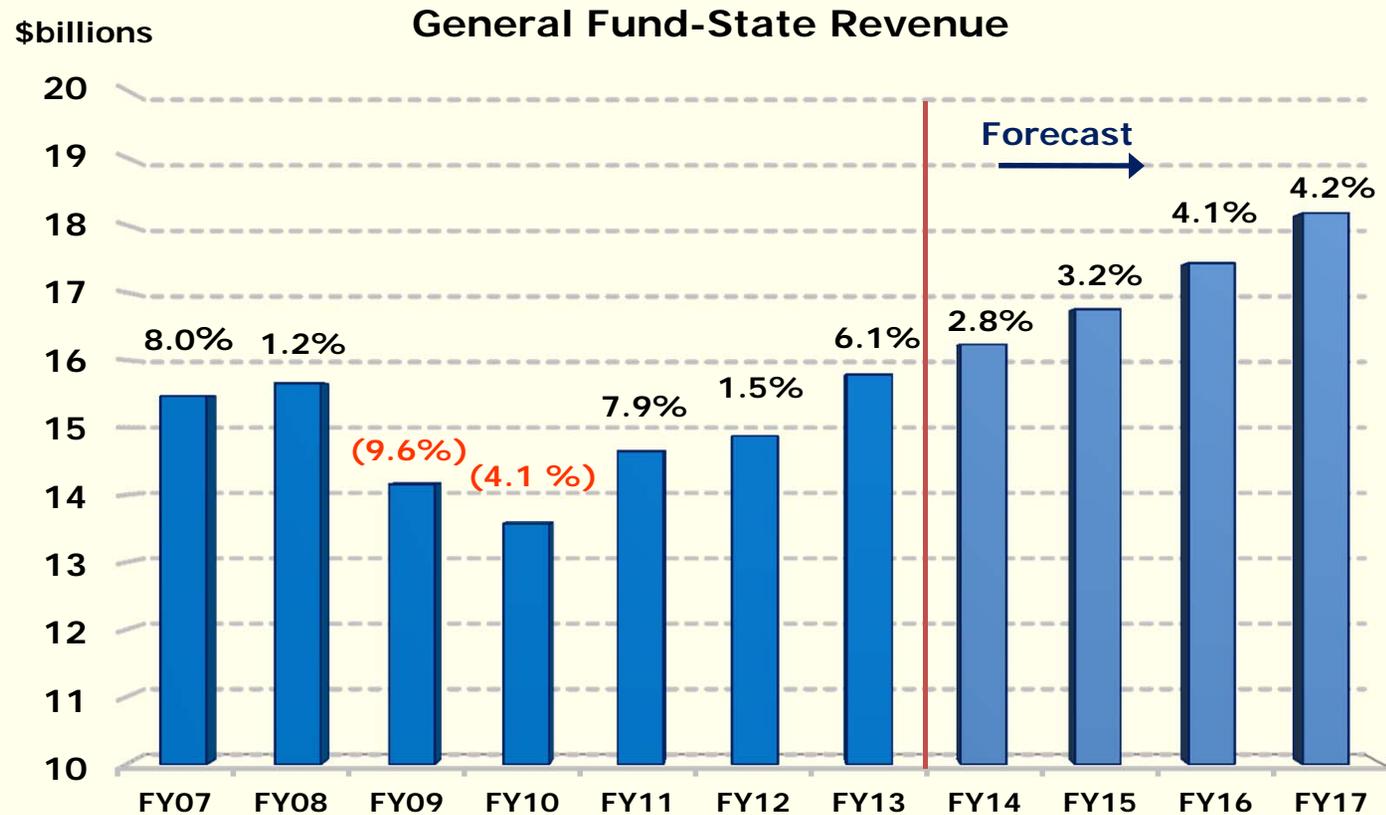
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Source: ERFC February 2012 - November 2013 forecasts

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General Fund-State* forecast by fiscal year



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*General Fund-State & Related Funds for FY 07-09, General Fund-State new definition for FY 10-17
Source: ERFC forecast, November 2013

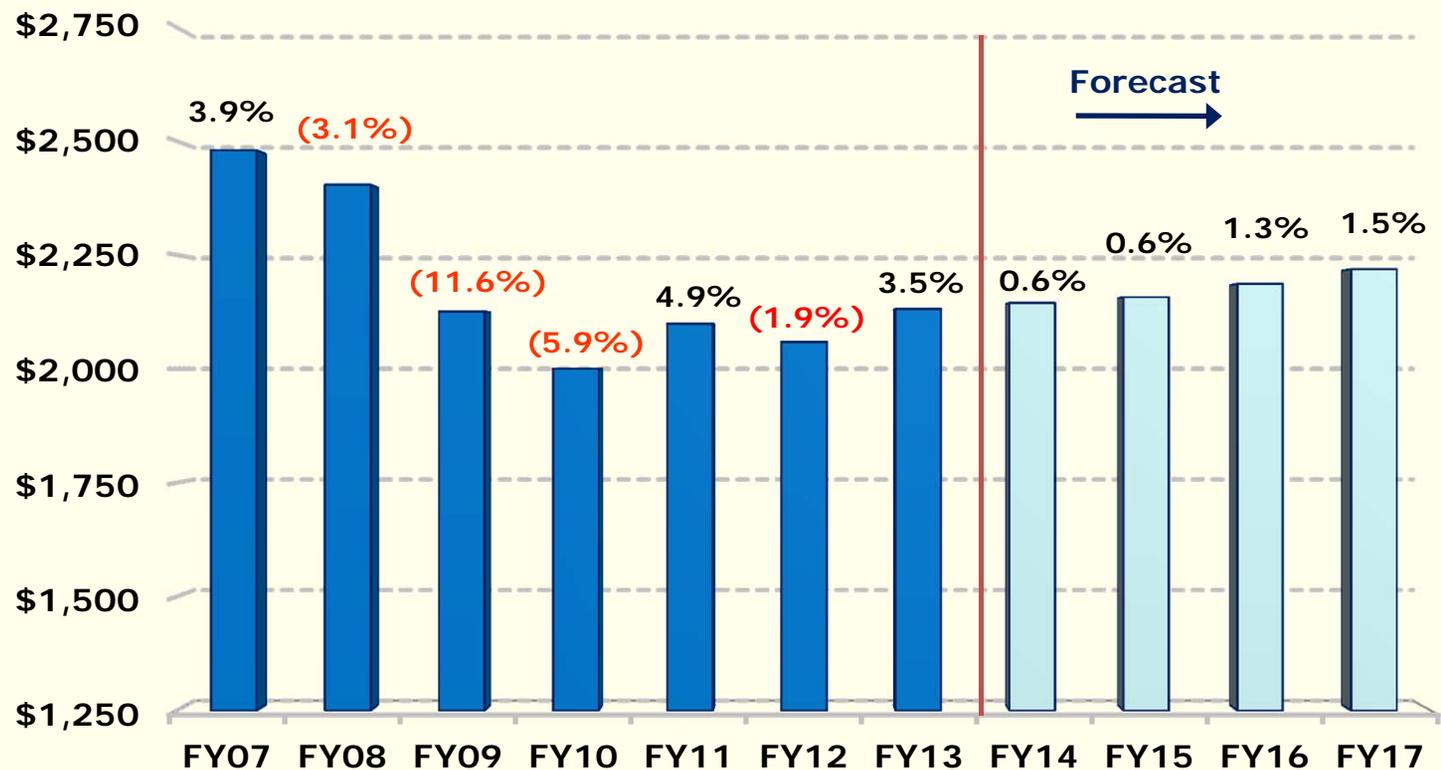
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Real Per Capita General Fund* -State Revenue

* General Fund & Related Funds for FY 2007-2009, General Fund – new definition, for FY 2010-2017

Per Capita GF-S* , \$2009



Source: ERFC forecast, November 2013



2013-15 Biennium alternative forecasts – cash basis

\$Millions	2013-15 Biennium	Difference From the baseline
November 2013 Baseline (55%)	\$32,982	
<u>November 2013 Alternative Forecasts</u>		
Optimistic (15%)	\$35,058	\$2,075
Pessimistic (30%)	\$30,961	(\$2,021)
Probability Weighted Average	\$32,687	(\$295)
GCEA*	\$33,171	\$189

*Based on the Governor's Council of Economic Advisors' assumptions

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Conclusion

- Our November forecast update shows relatively small changes in our economic and revenue forecasts
- We continue to forecast slow economic and job growth for both the national and state economies
- The level of uncertainty in the baseline remains extremely high, and downside risks outweigh upside risks
- GF-S revenues grew 8.6% between the 2009-11 and 2011-13 biennium and are expected to grow 7.6% between the 2011-13 and 2013-15 biennium



Questions



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