

Economic & Revenue Outlook

Presented for
2011 Yakima Economic Symposium

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July 8, 2011
Yakima, Washington



WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL



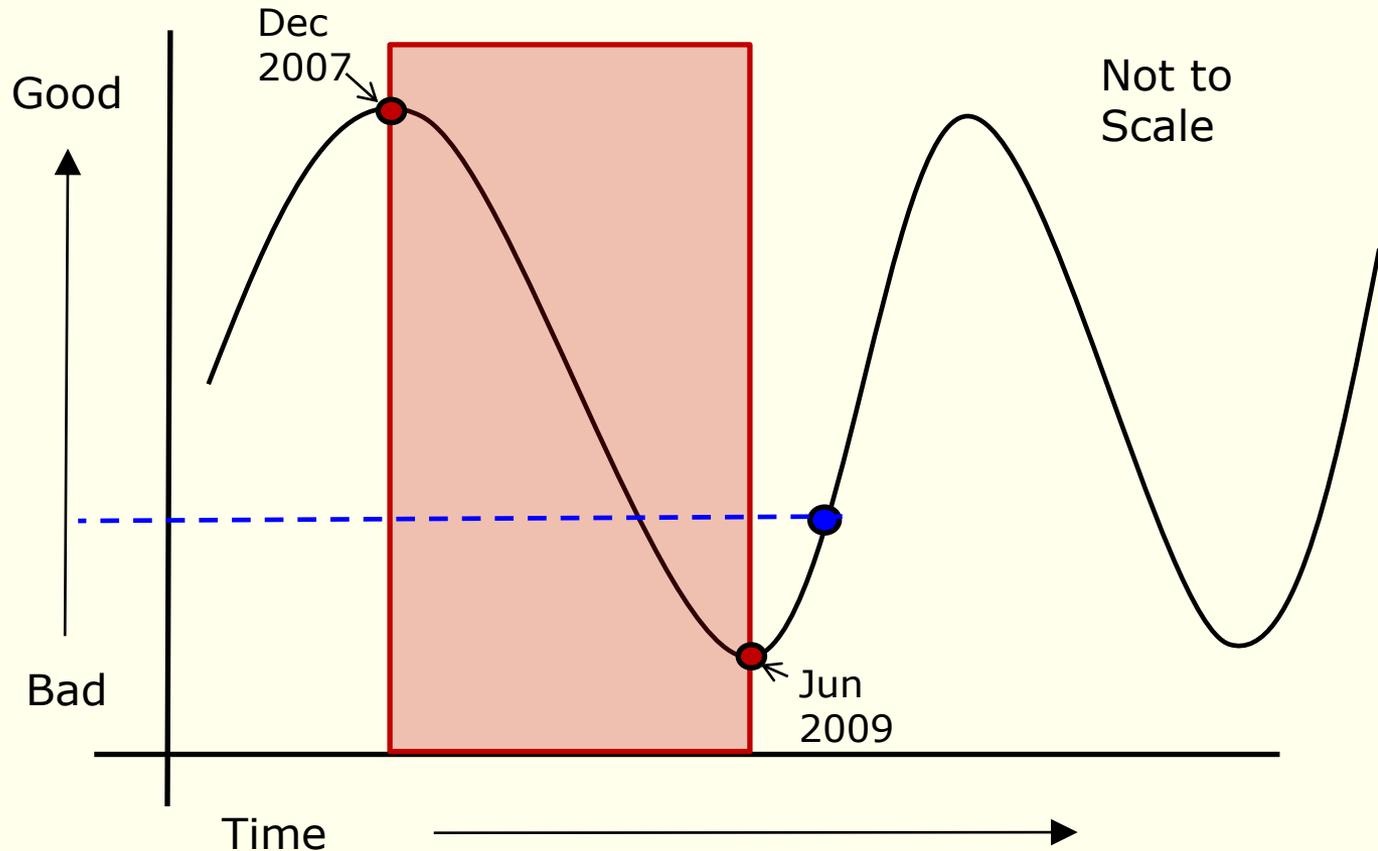
Summary

- The near term economic outlook has weakened since the March forecast.
- The impact from the devastation in Japan was worse than anticipated and the turmoil in the Middle East and North Africa has added to uncertainty in oil markets.
- We expect growth to pick up momentum later this year, as supply chain disruptions from Japan recede, and oil prices stabilize.
- This forecast changes expected GF–S revenues by
 - Up \$171 million this biennium (09-11)
 - Down \$183 million next biennium (11-13)



Definition of a recession

National Bureau of Economic Research (NBER) is the official arbiter of business cycles



Source: ERFC

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This is the worst recession since WW II

| Recession | Peak-to-trough decline | | Recession Duration |
|----------------|------------------------|----------------|--------------------|
| | Real GDP | Employment | |
| | <i>percent</i> | <i>percent</i> | <i>months</i> |
| 1948-49 | 1.6 | 5.0 | 11 |
| 1953-54 | 2.5 | 3.4 | 10 |
| 1957-58 | 3.1 | 4.2 | 8 |
| 1960-61 | 0.5 | 2.3 | 10 |
| 1969-70 | 0.2 | 1.2 | 11 |
| 1973-75 | 3.2 | 1.9 | 16 |
| 1980 | 2.2 | 2.3 | 6 |
| 1981-82 | 2.6 | 3.1 | 16 |
| 1990-91 | 1.4 | 1.4 | 8 |
| 2001 | 0.7 | 1.7 | 8 |
| Average | 1.8 | 2.6 | 10 |
| 2007-09 | 4.1 | 6.3 | 18 |

Source: NBER, ERFC

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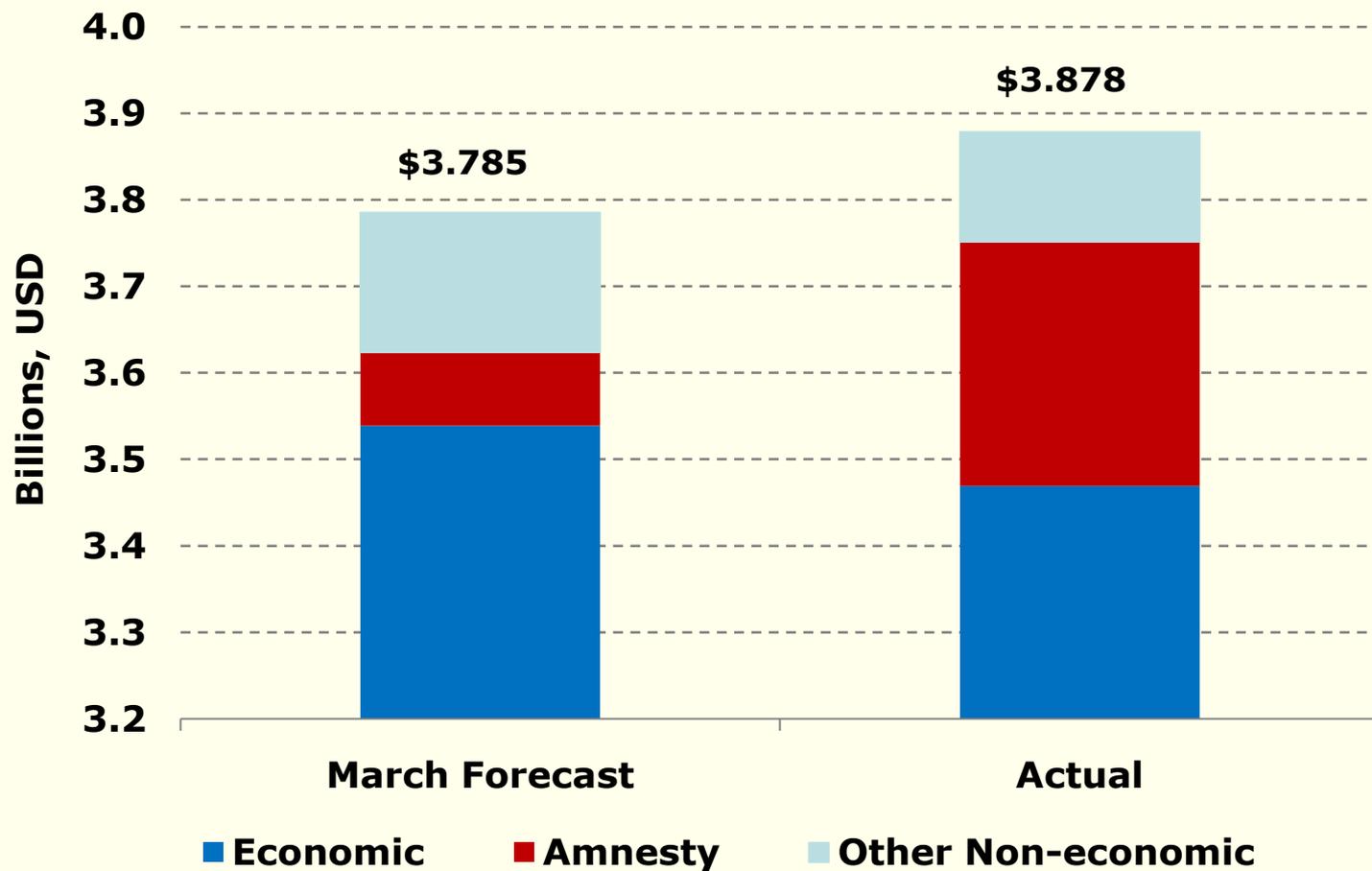


Collections since March were \$93 million above target because of the amnesty program

Amnesty:

March Forecast
\$85 Million

Collections
\$282 Million



Source: ERFC; data through June 10, 2011 Collections

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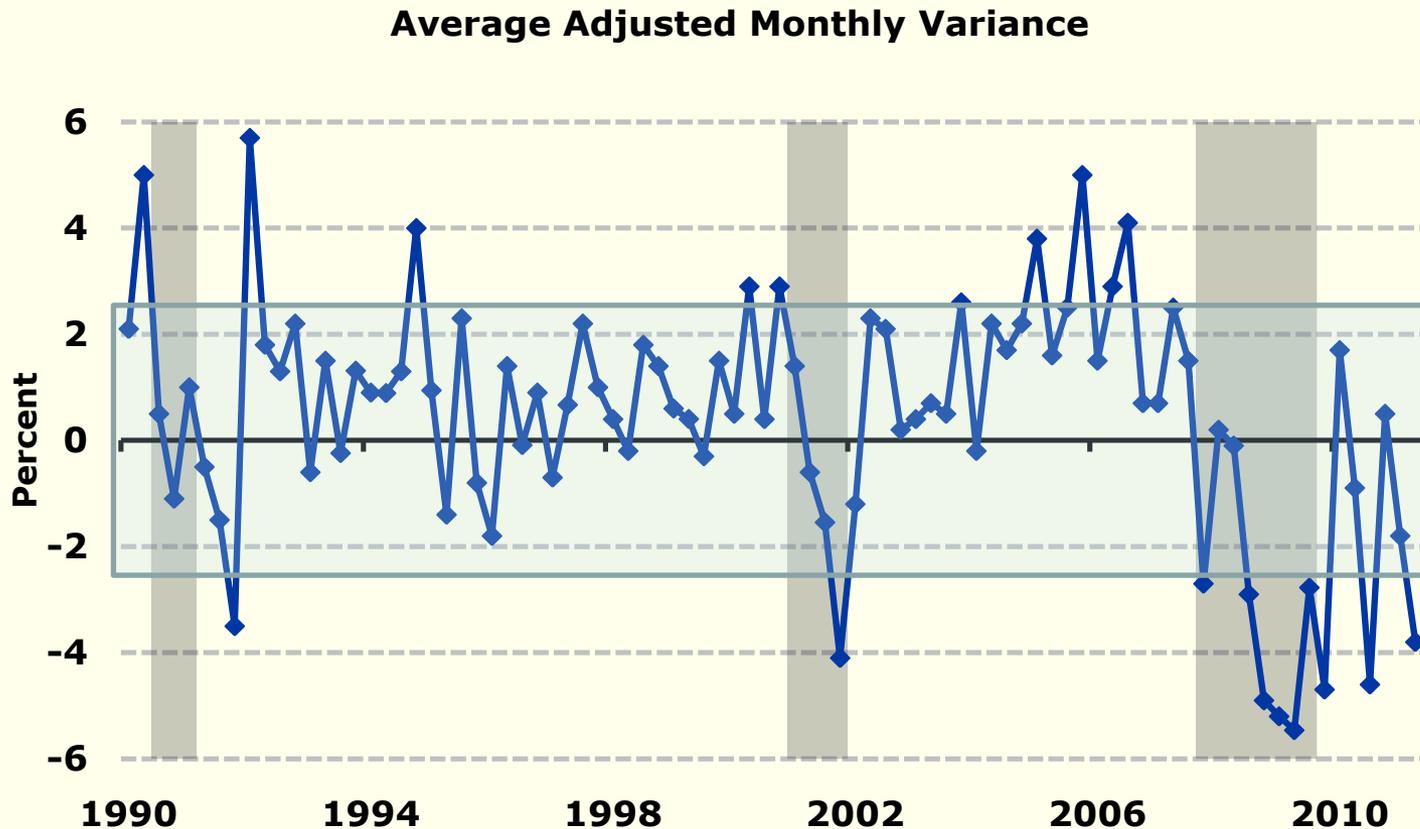
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Excluding one-time factors, revenues were 3.8% below the March forecast

Including one time payments, **overall revenue collections were \$93 million above forecast**

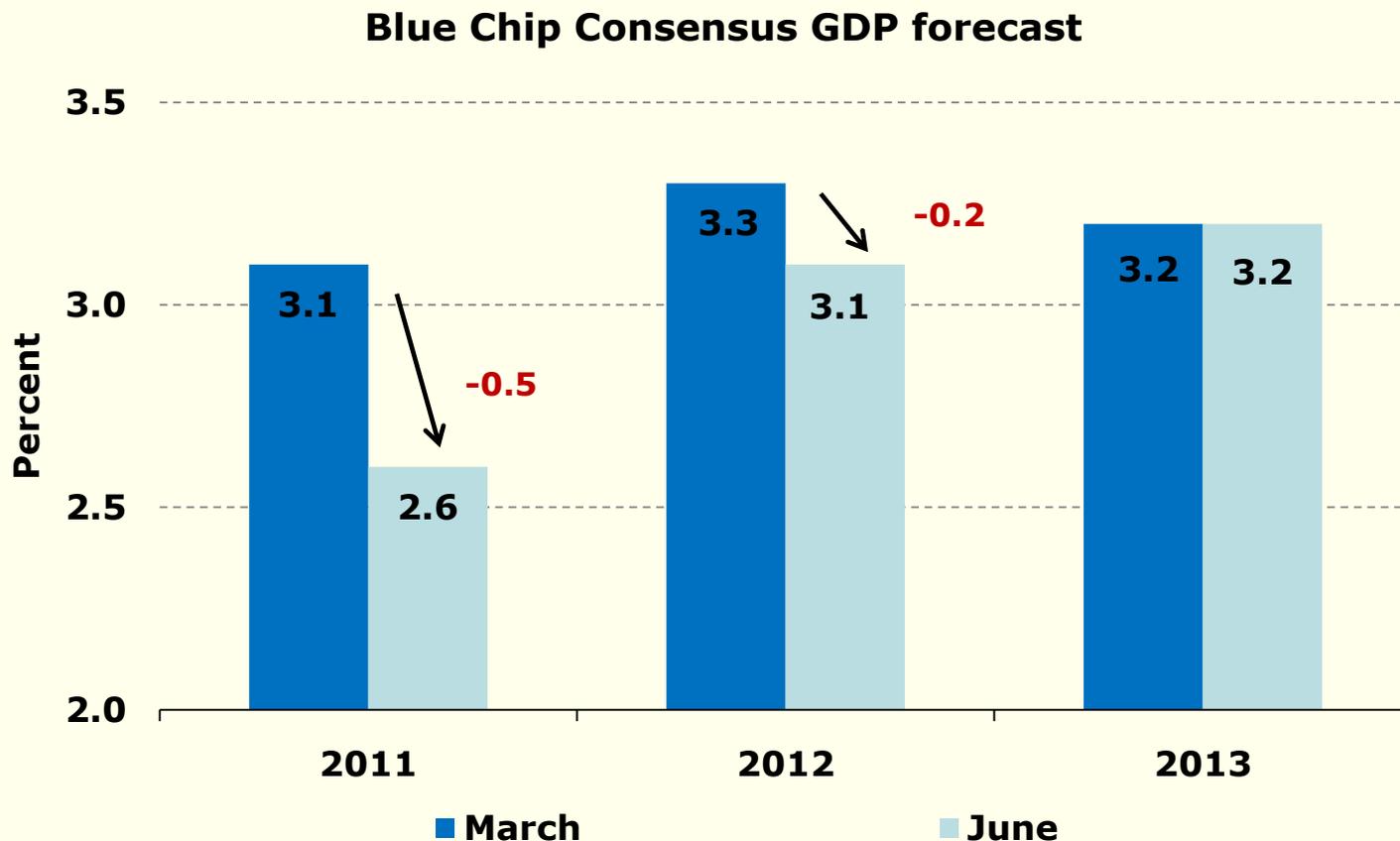


Source: ERFC; Based on collections through June 10, 2011

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The consensus near-term economic outlook has weakened since March

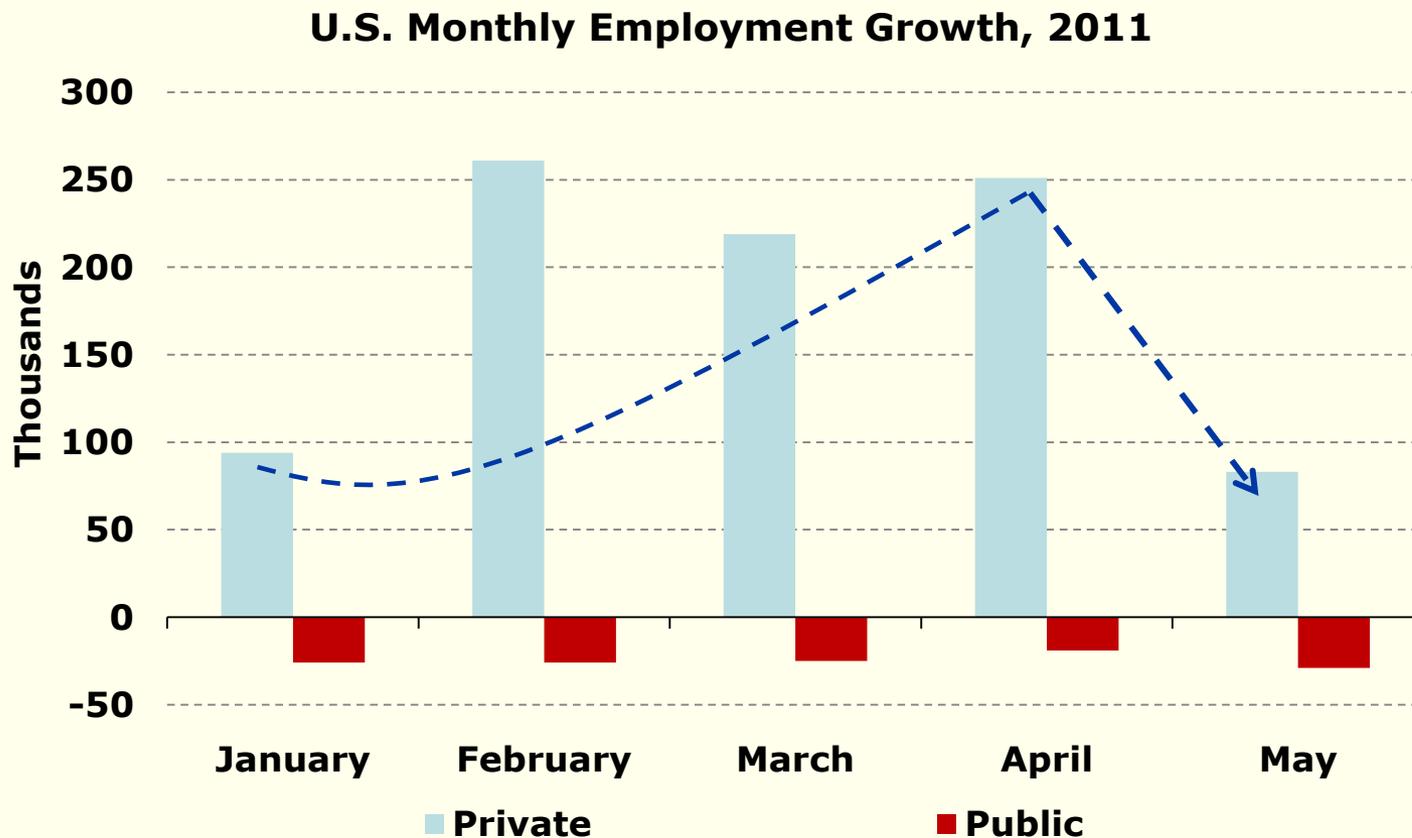


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Source: Blue Chip Economic Indicators, data through June 2011



Private sector job gains slipped in May



Source: BLS; data through May 2011

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This has been the slowest recovery in U.S. employment

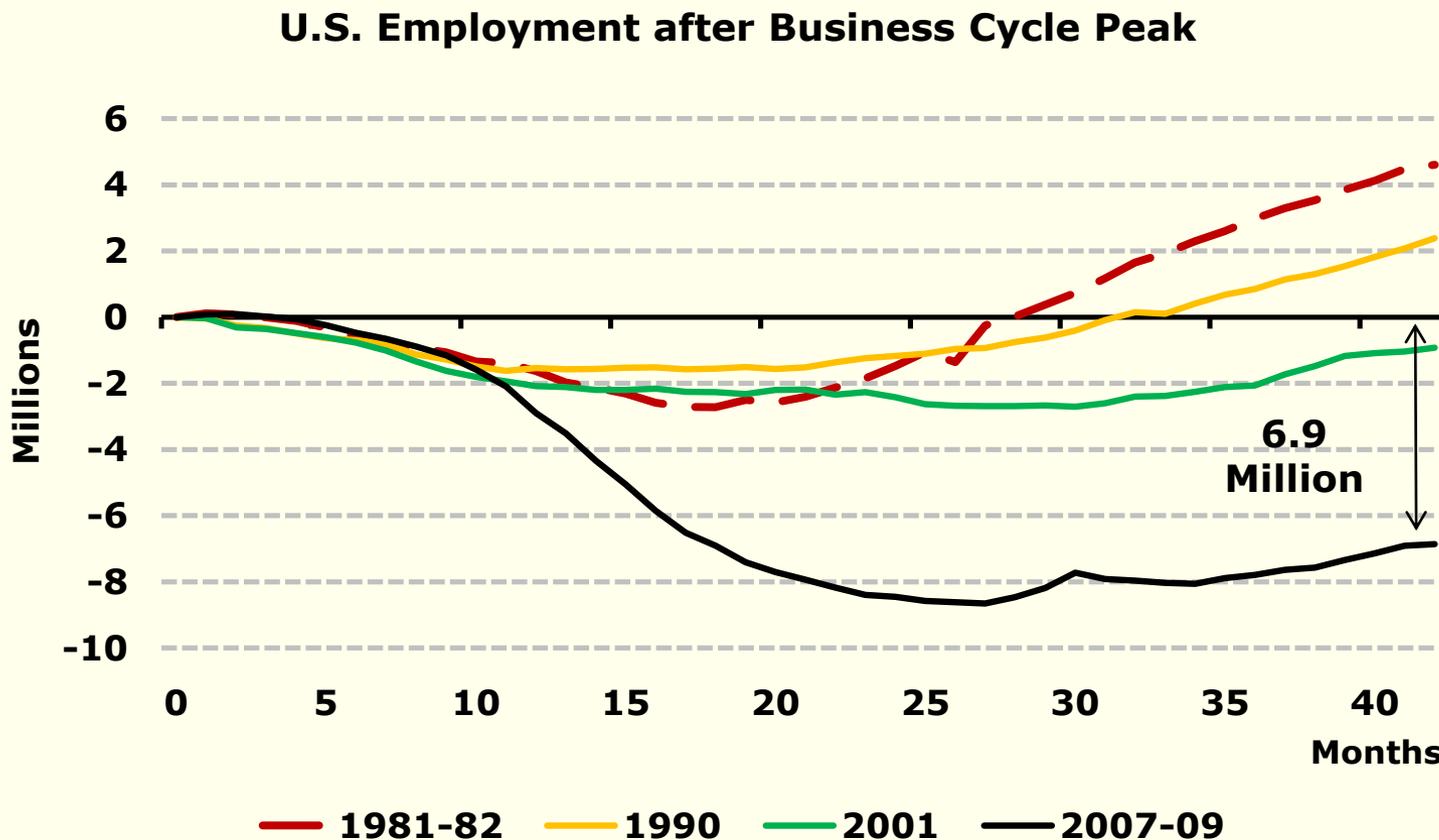
Peak to trough job losses

1981-82:

2.6% of labor force

This time:

5.7% of labor force



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Source: BLS, WA ESD, ERFC; data through May 2011

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Employment should pick up as labor productivity growth declines

Any increase in final demand will translate to job growth

U.S. Employment & Labor Productivity Growth



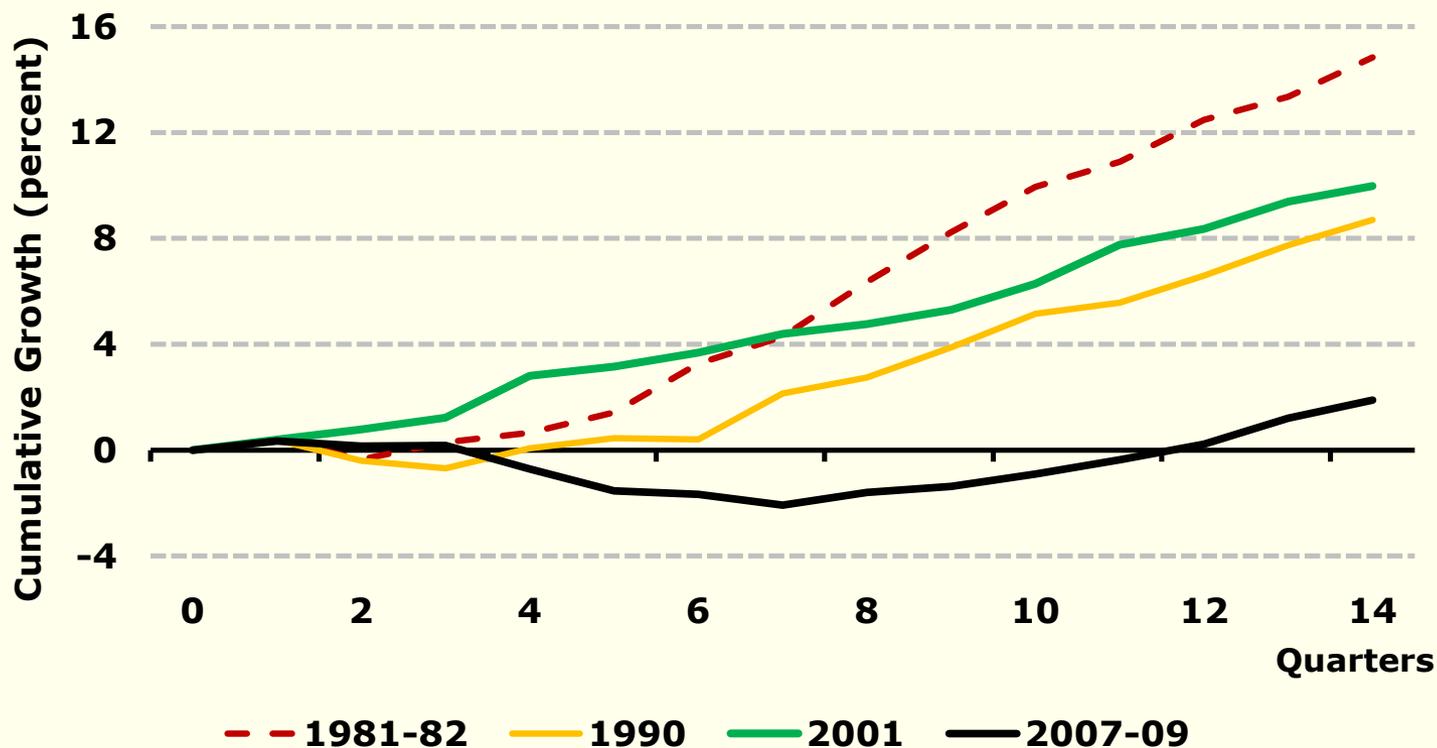
Source: BLS; data through 2011 Q1

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Consumer demand is weak

U.S. Consumption after Business Cycle Peak



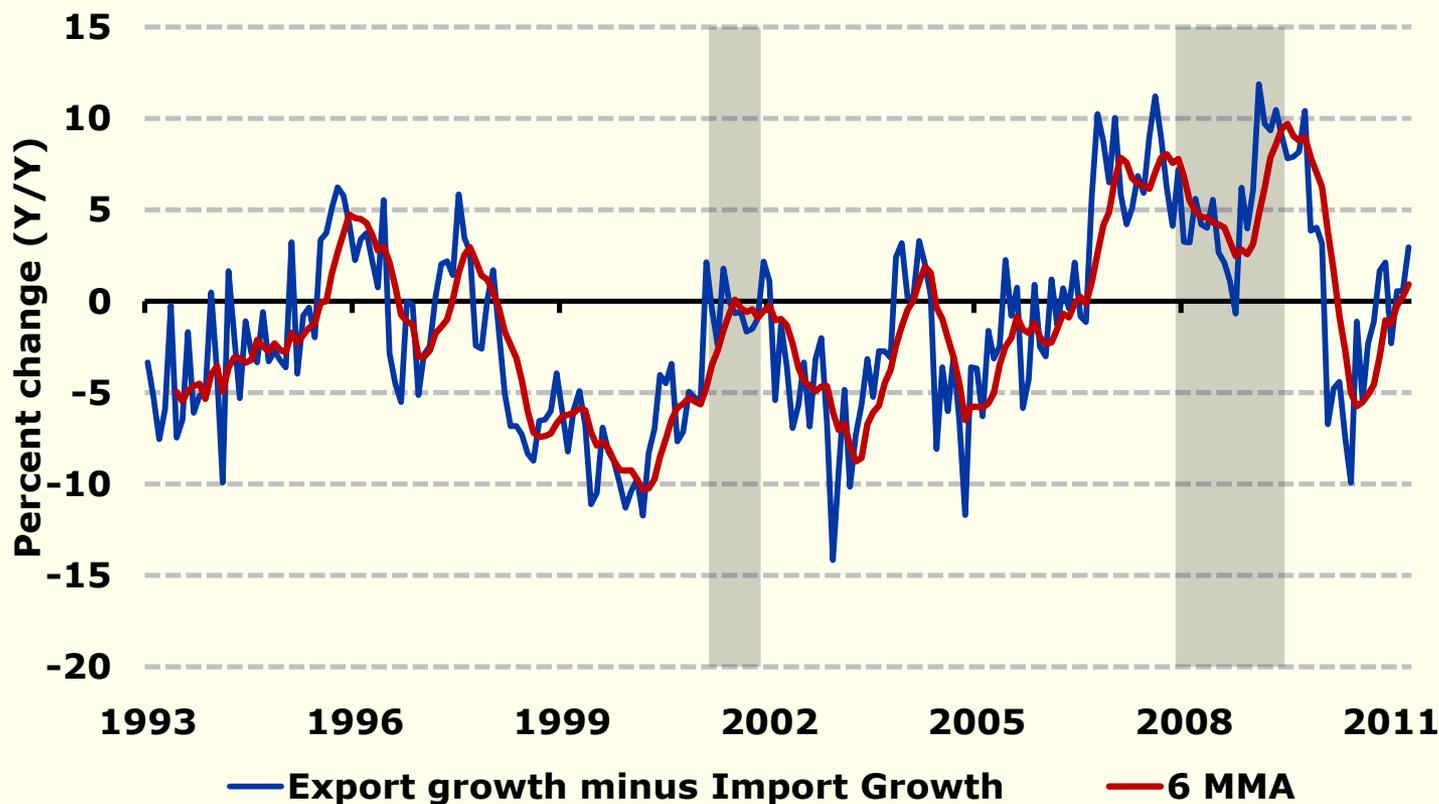
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Source: BEA, ERFC; data through 2011 Q1



Exports are growing faster than imports

Export growth *minus* Import growth

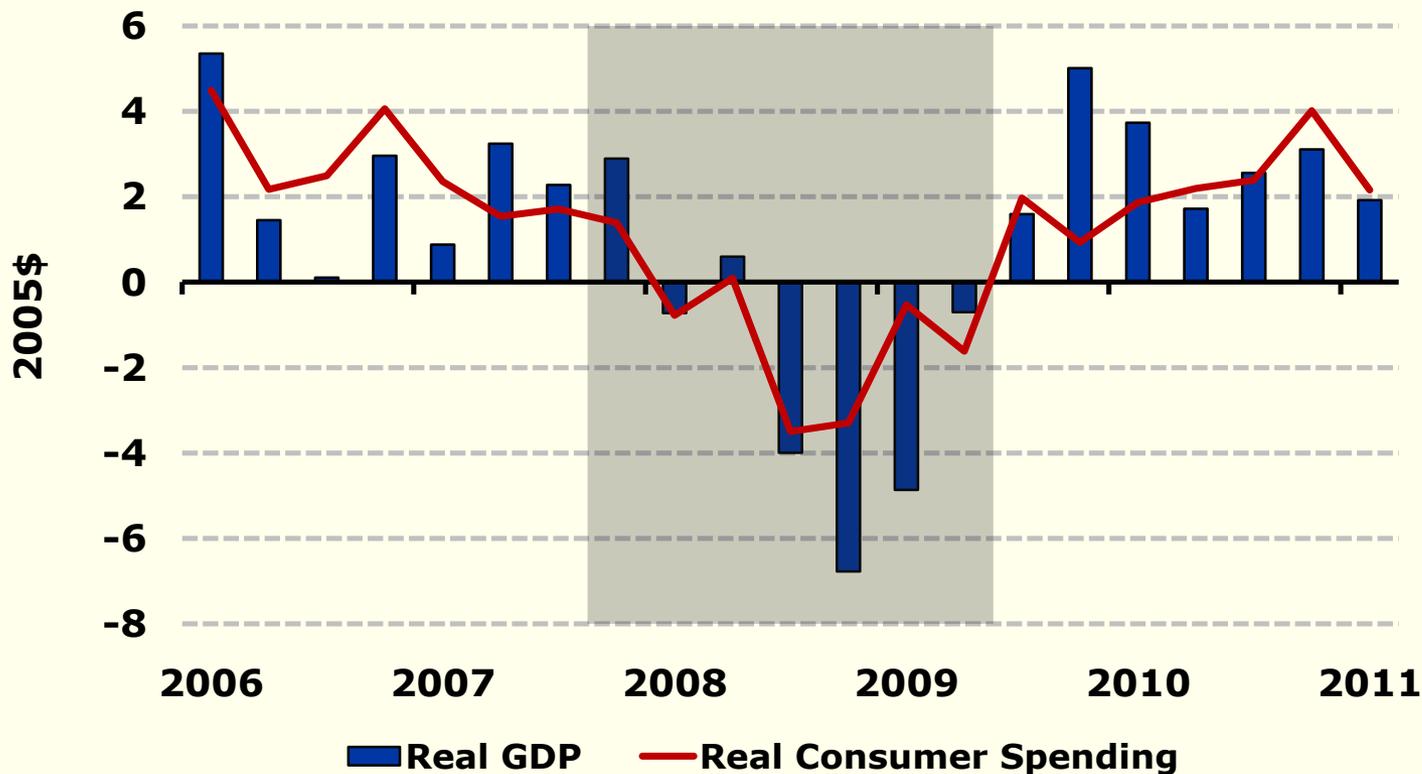


Source: Census Bureau, U.S. Balance of Payments Account; data through April 2011



GDP and consumer spending growth slowed in Q1

Percent growth, SAAR

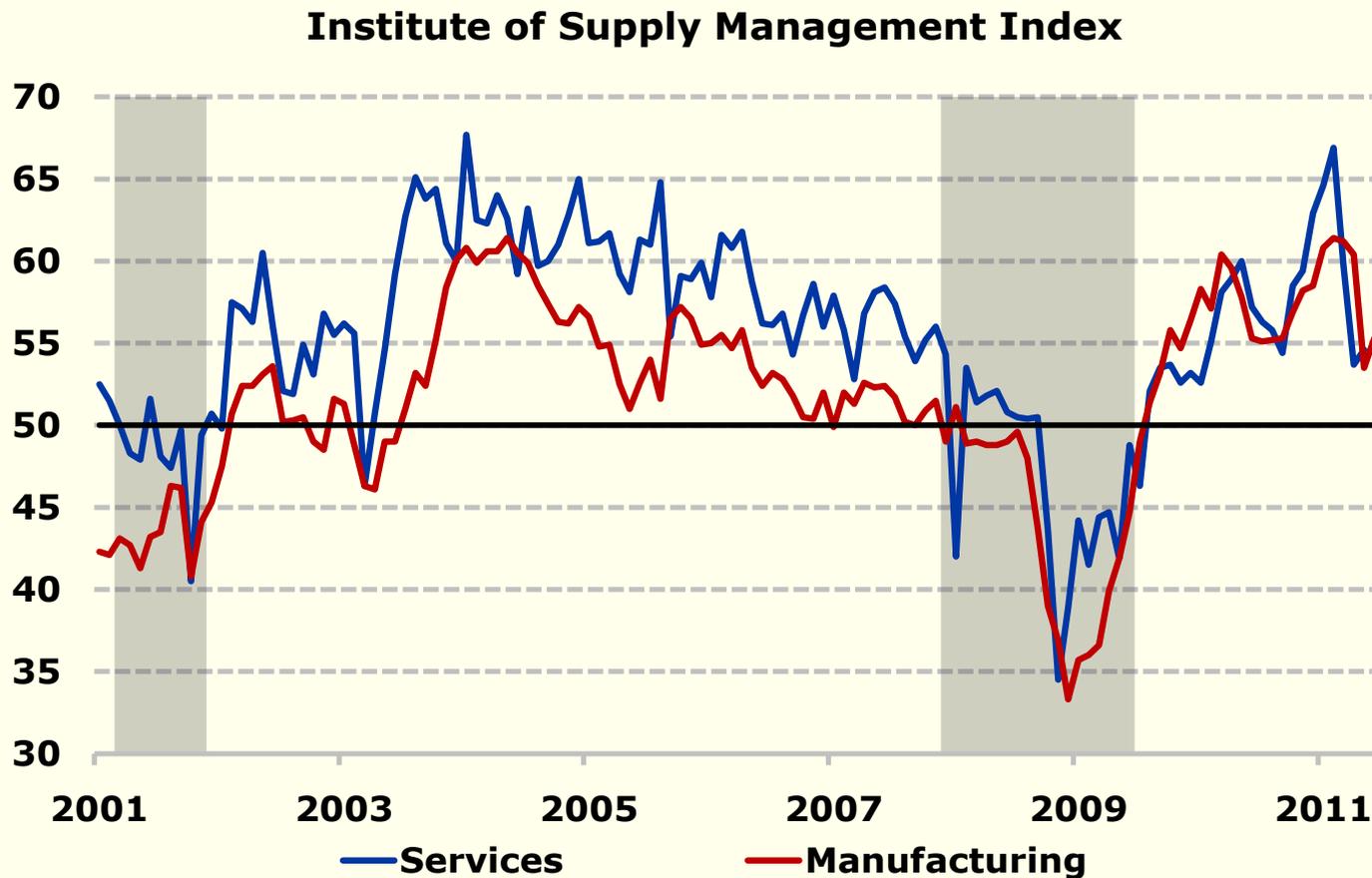


Source: BEA, data through 2011 Q1, third estimate



Manufacturing and service sector growth is slowing

An index greater than 50, implies growth



Source: Institute of Supply Management; data through June 2011

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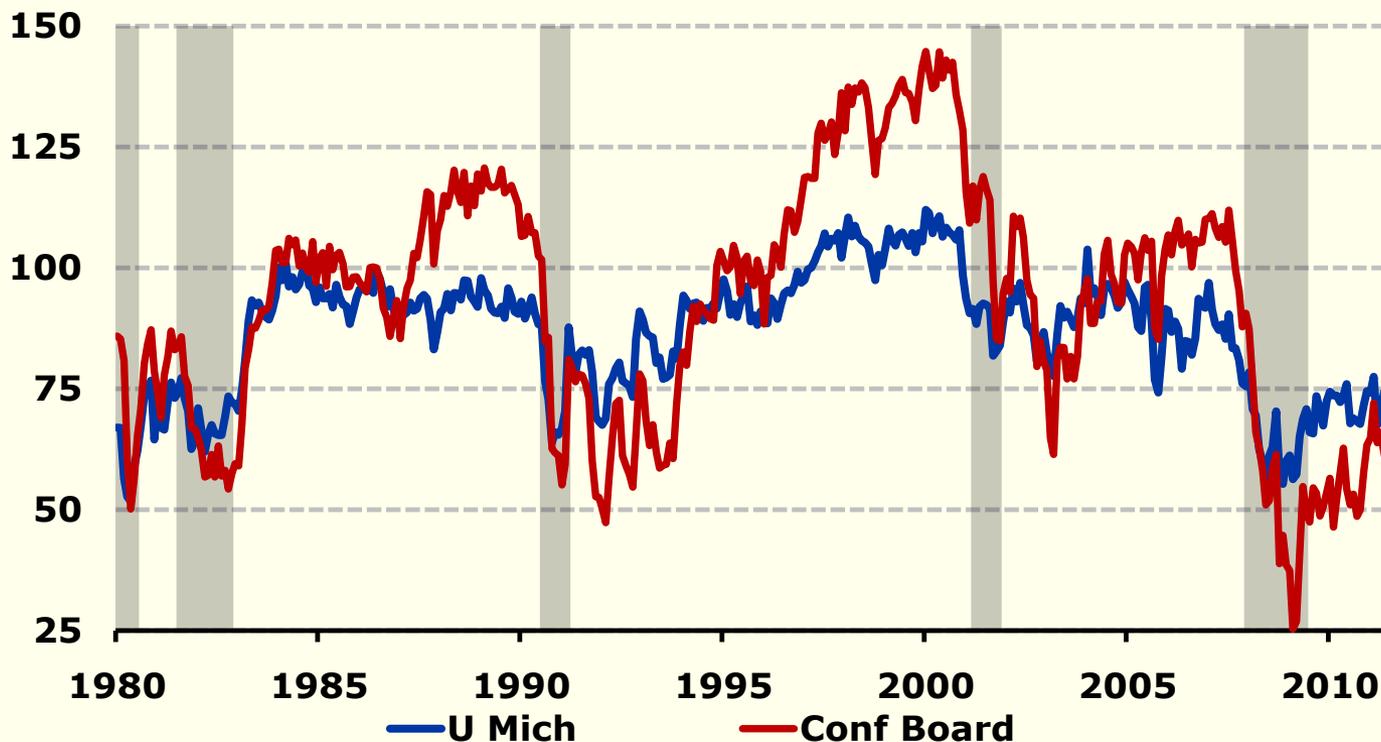


Consumer confidence is showing signs of softening

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA



Source: University of Michigan; Conference Board, data through June 2011

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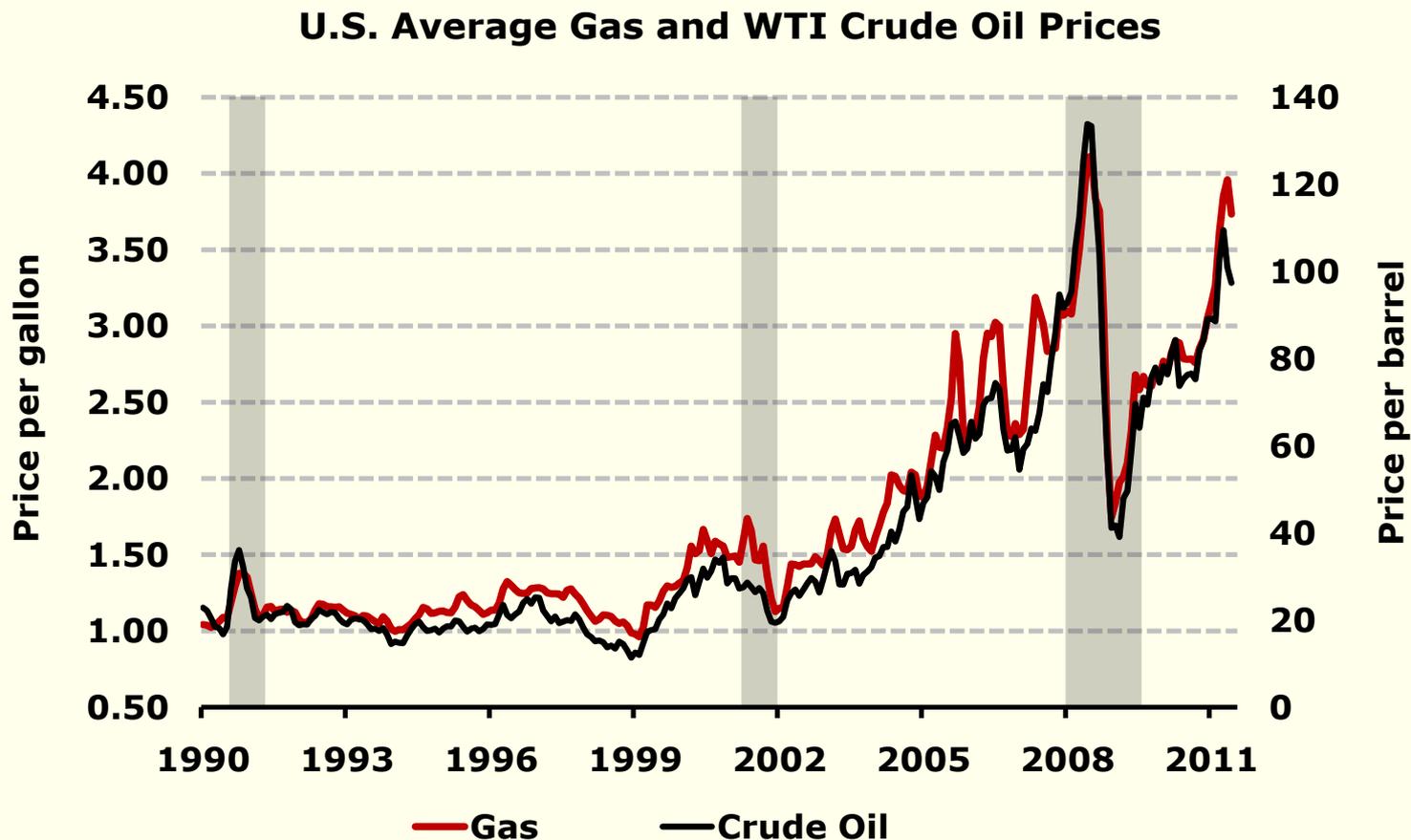
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Gas prices are retreating, but remain high

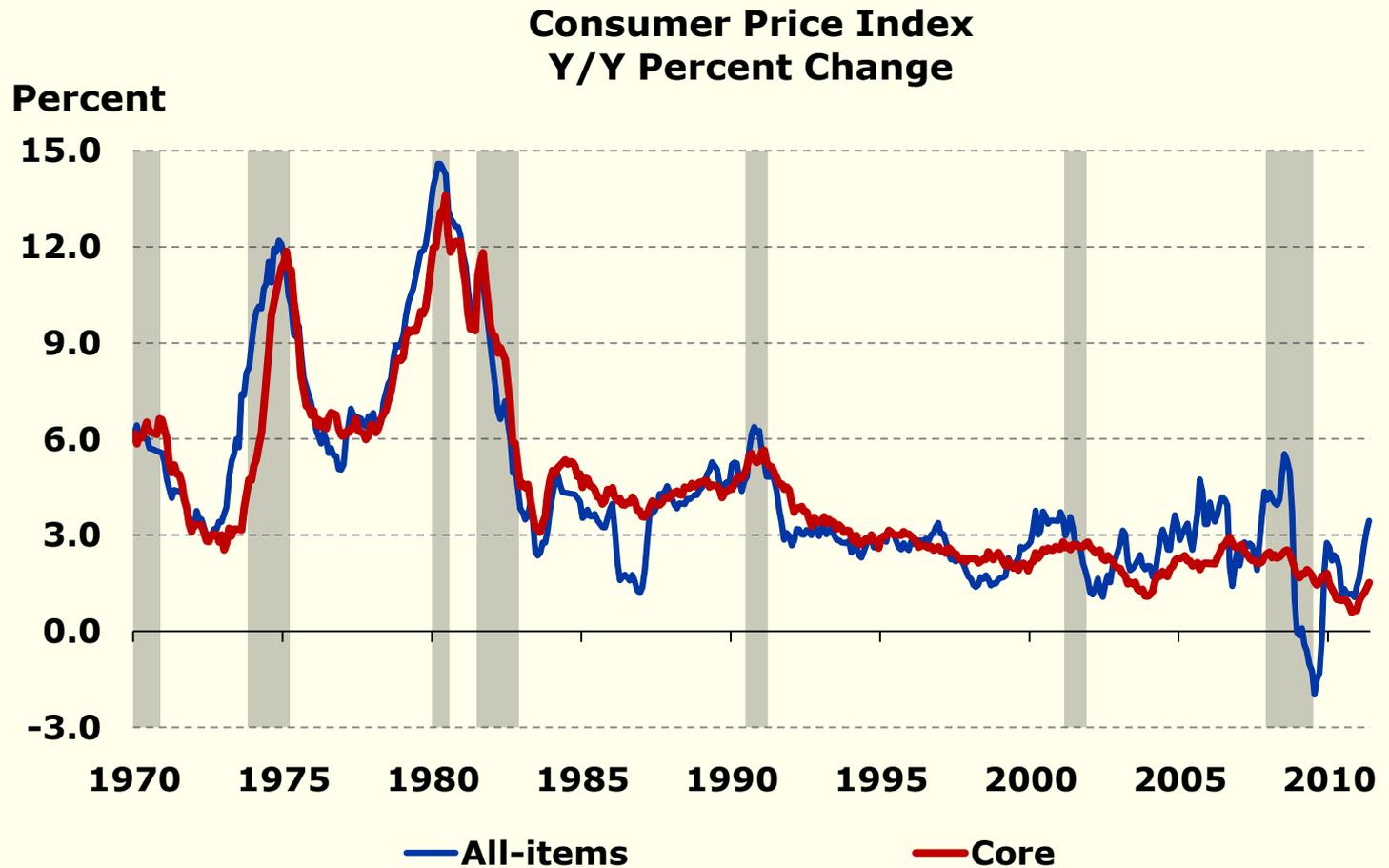


Source: U.S. Energy Information Administration; data through June, 2011

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All-items inflation is ticking up, but the "core" remains stable



Source: BLS; data through May 2011

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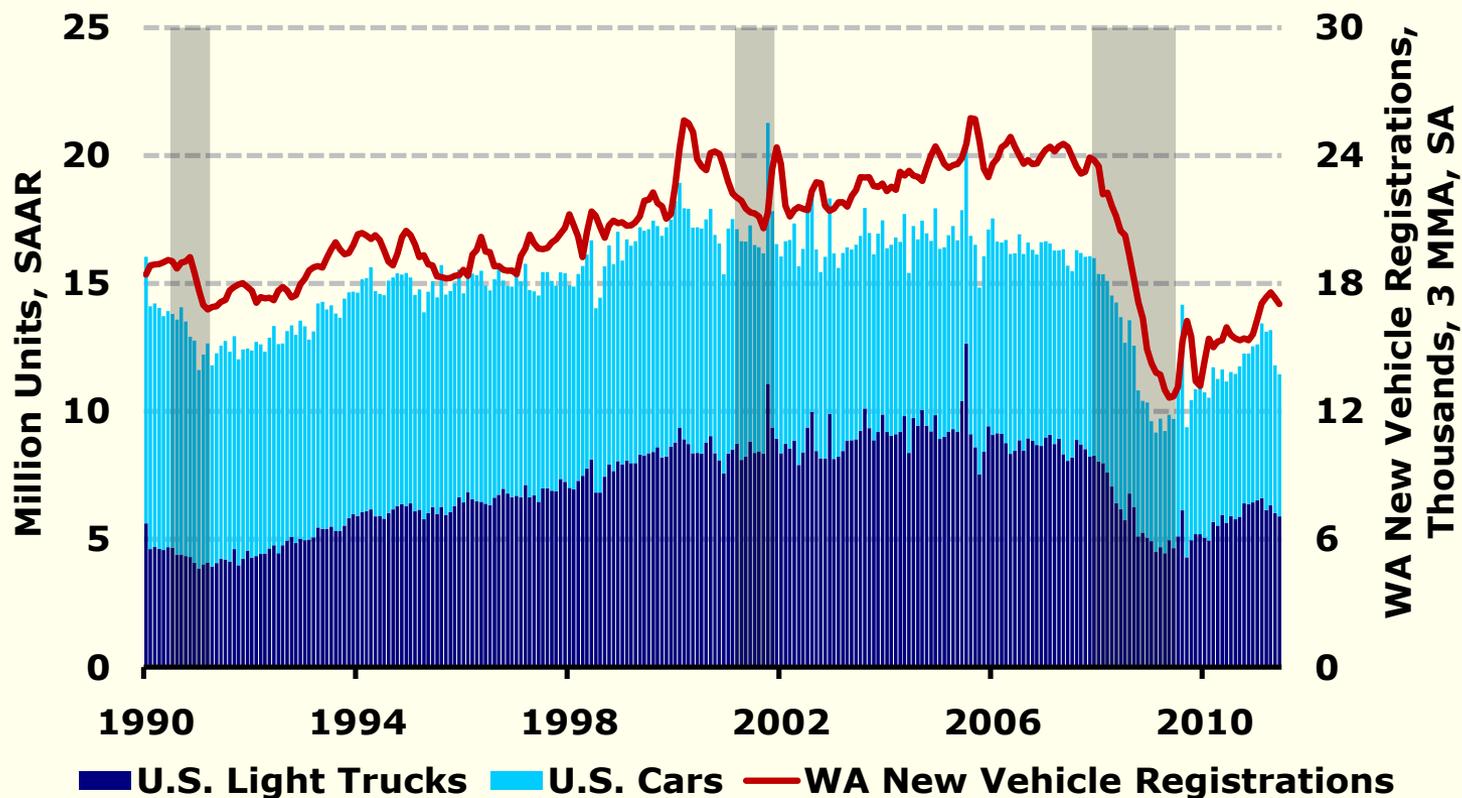
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U.S. LMV sales slowed in May and June...

U.S. LMV sales fell 10.4% in May

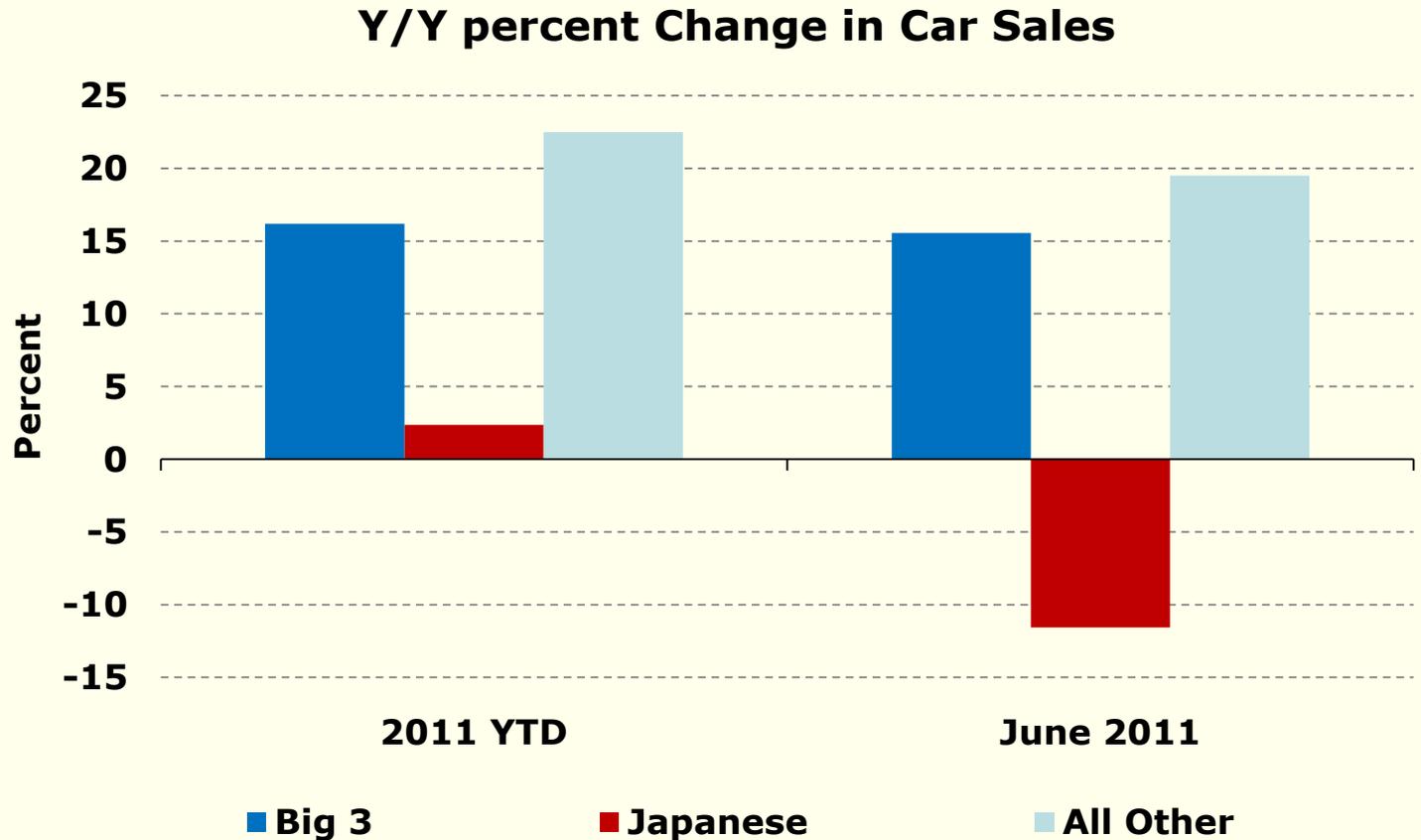


Source: Autodata Corporation, WA DOL; data through June 2011

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... as Japanese brands were hit by supply chain disruptions

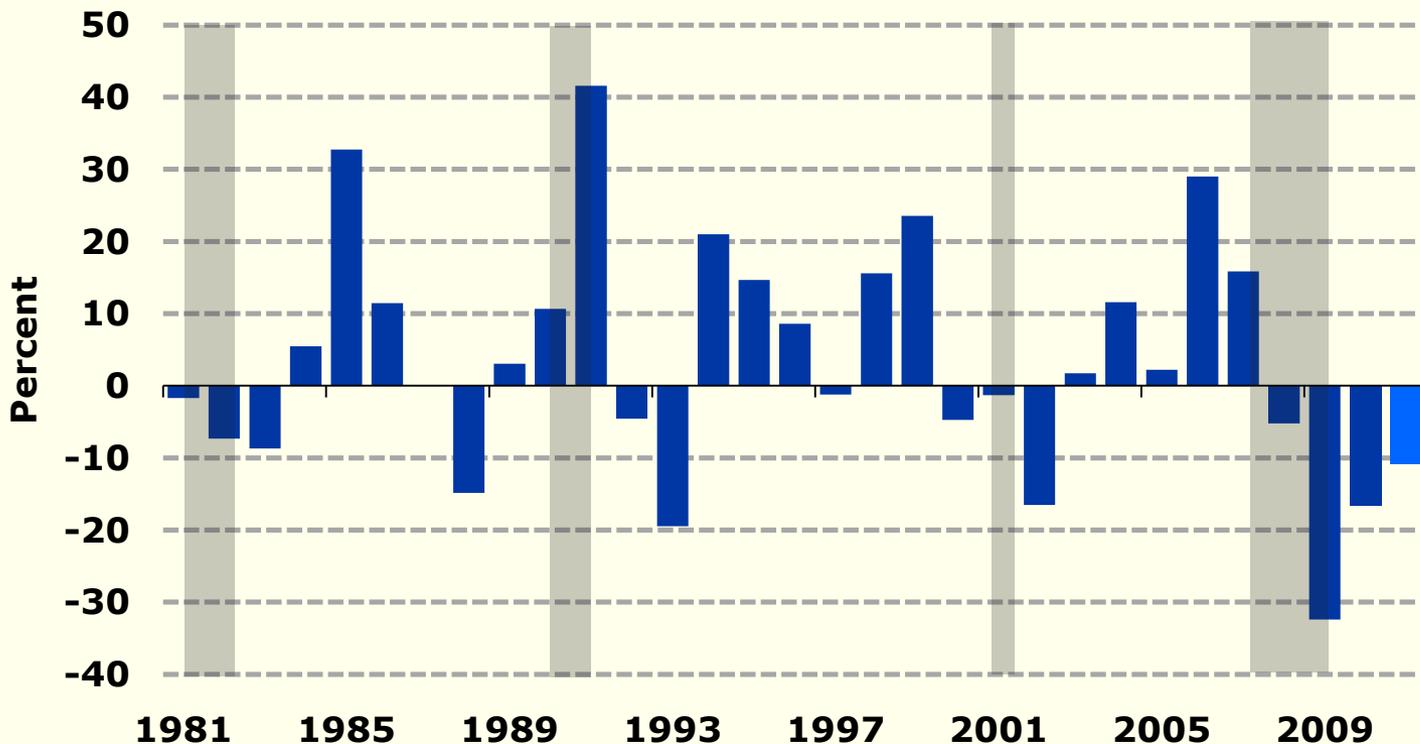


Source: Autodata Corporation, data through June 2011



This is WA's worst downturn in non-residential construction in 30 years

Non-Residential Contract Value Annual Percent Change



Source: McGraw-Hill Construction, data through May 2011

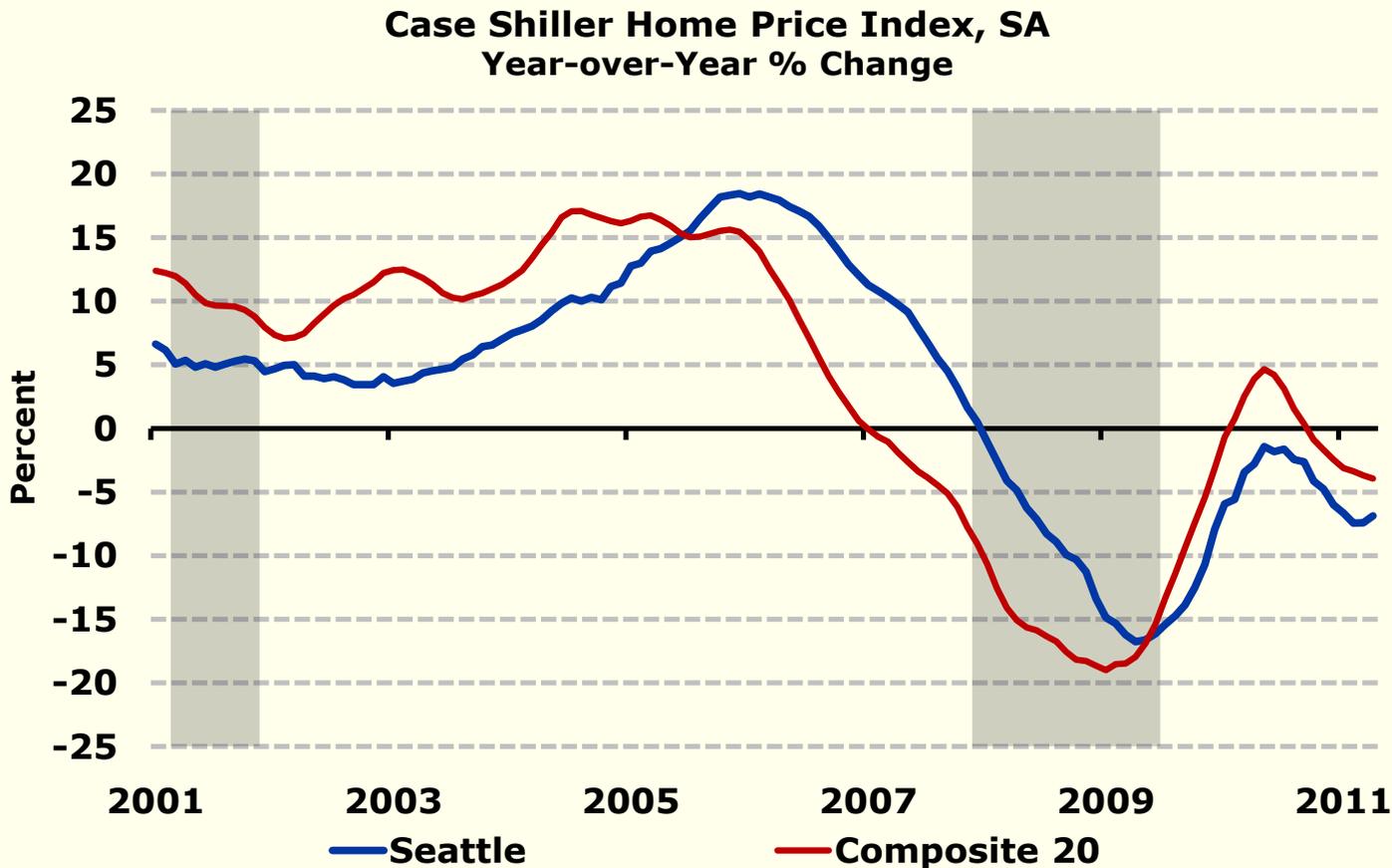


Home prices continue to decline

Apr 2011

**U.S is
down
3.9%**

**SEA is
down
6.9%**



Source: S&P/Case-Shiller; data through April 2011

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More foreclosures can be expected...

WA Rank:

2010Q4 : 25

2011Q1 : 23

Seriously
Delinquent =
90+ Days Past
Due or in
foreclosure

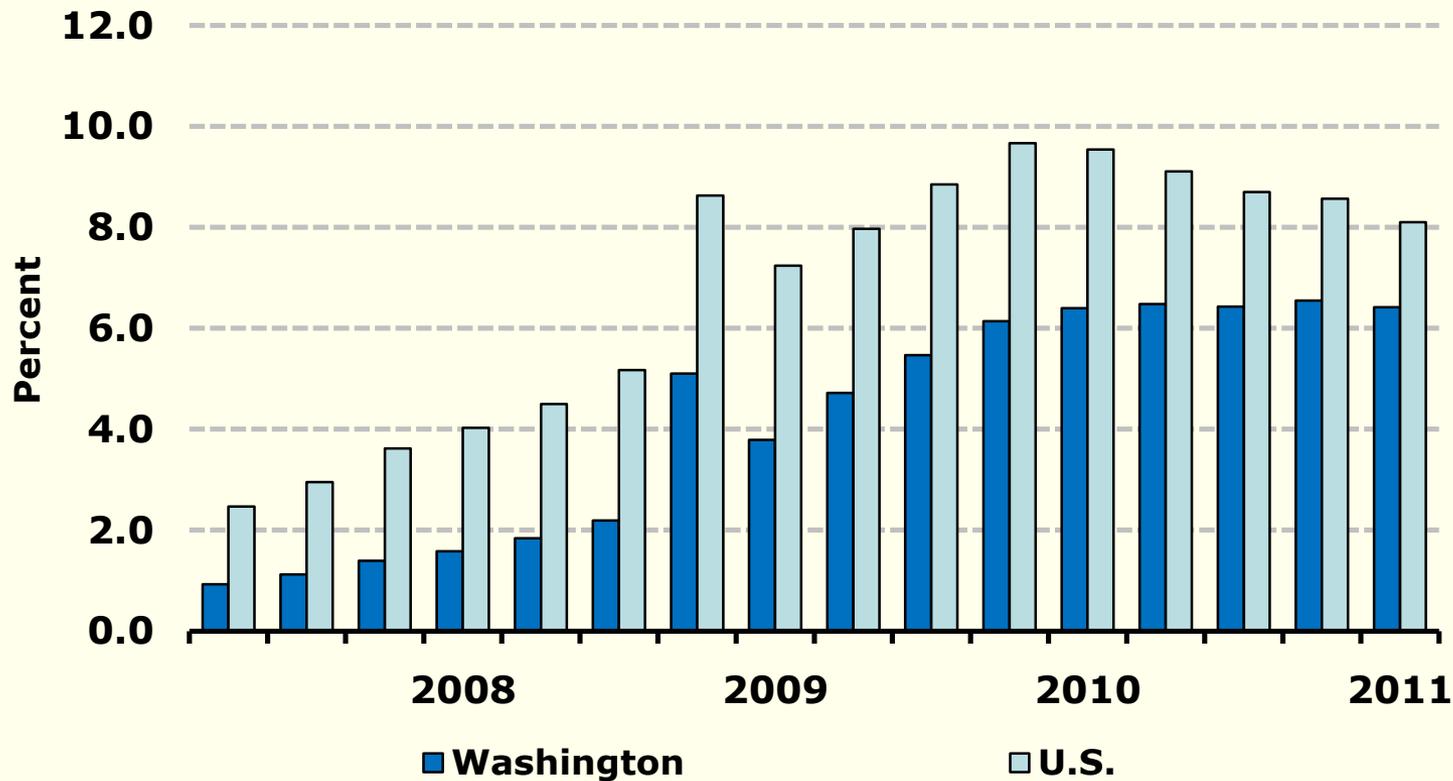
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Seriously Delinquent



Source: Mortgage Bankers Association® National Delinquency Survey, data through 2011 Q1



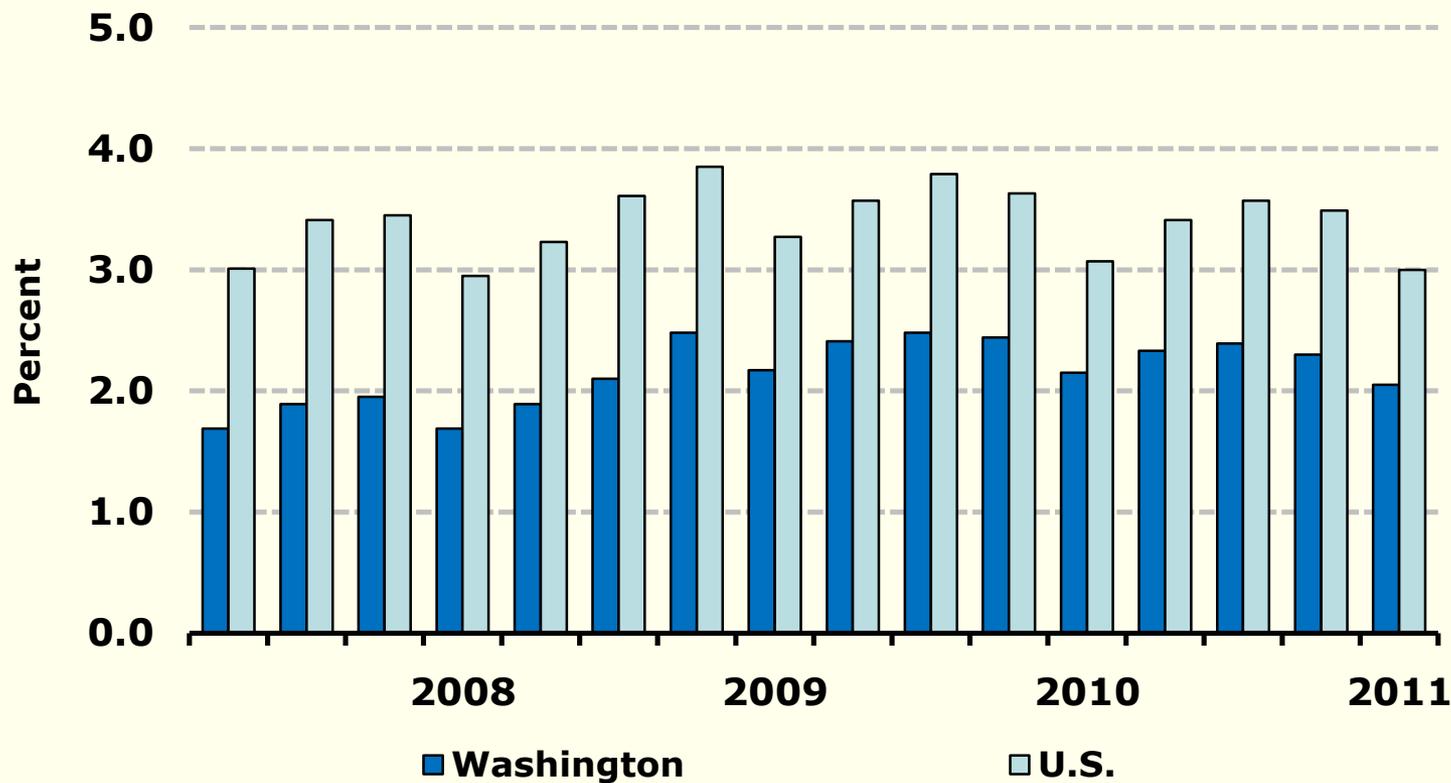
...but will eventually slow down

WA Rank:

2010Q4: 46

2011Q1: 47

30 Days Past Due



Source: Mortgage Bankers Association® National Delinquency Survey, data through 2011 Q1

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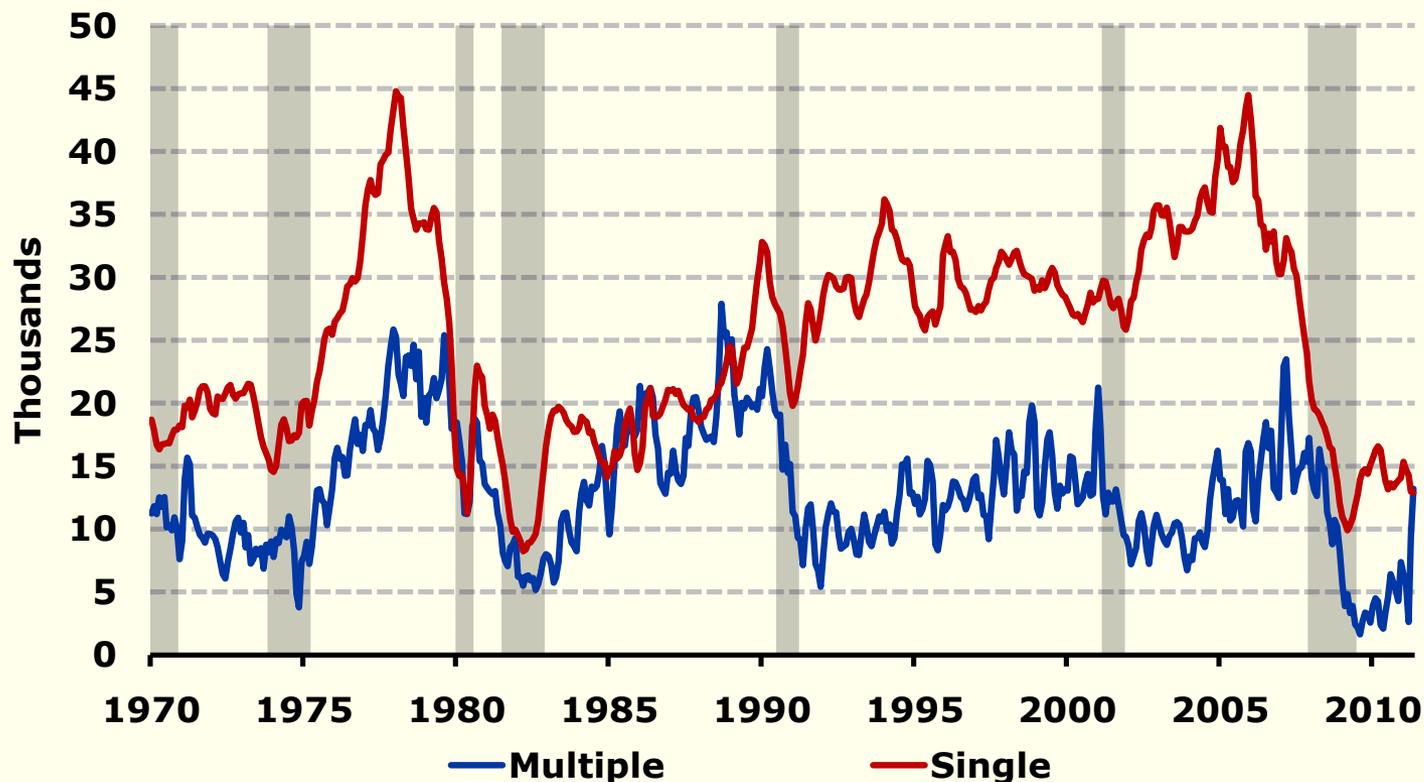
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WA multi-family building permits are gradually improving

Washington Housing Units Authorized by Building Permits, 3MMA, SAAR



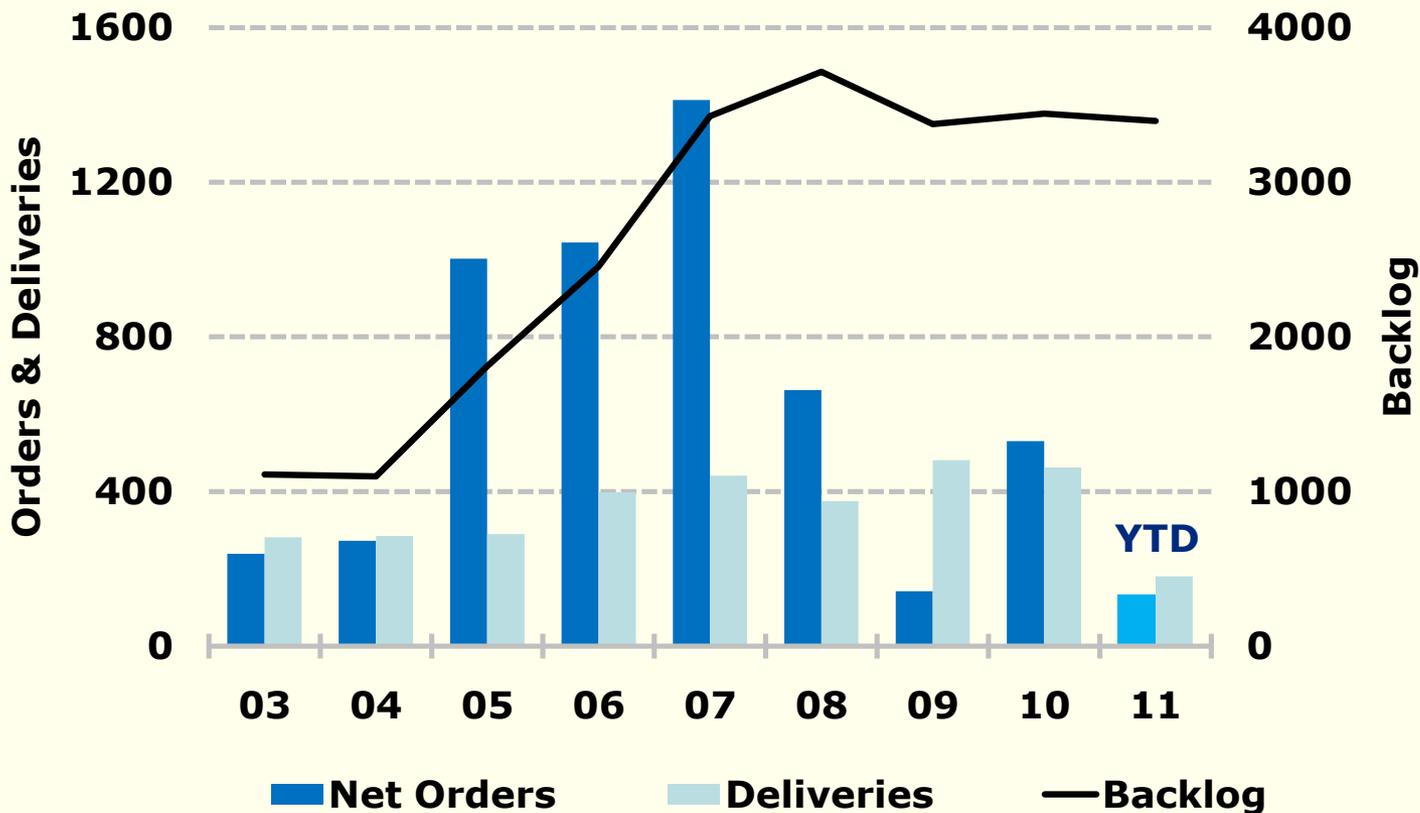
Source: U.S. Census Bureau; data through May 2011

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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 May 2011

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Software publishing employment is growing

Percent change, year ago



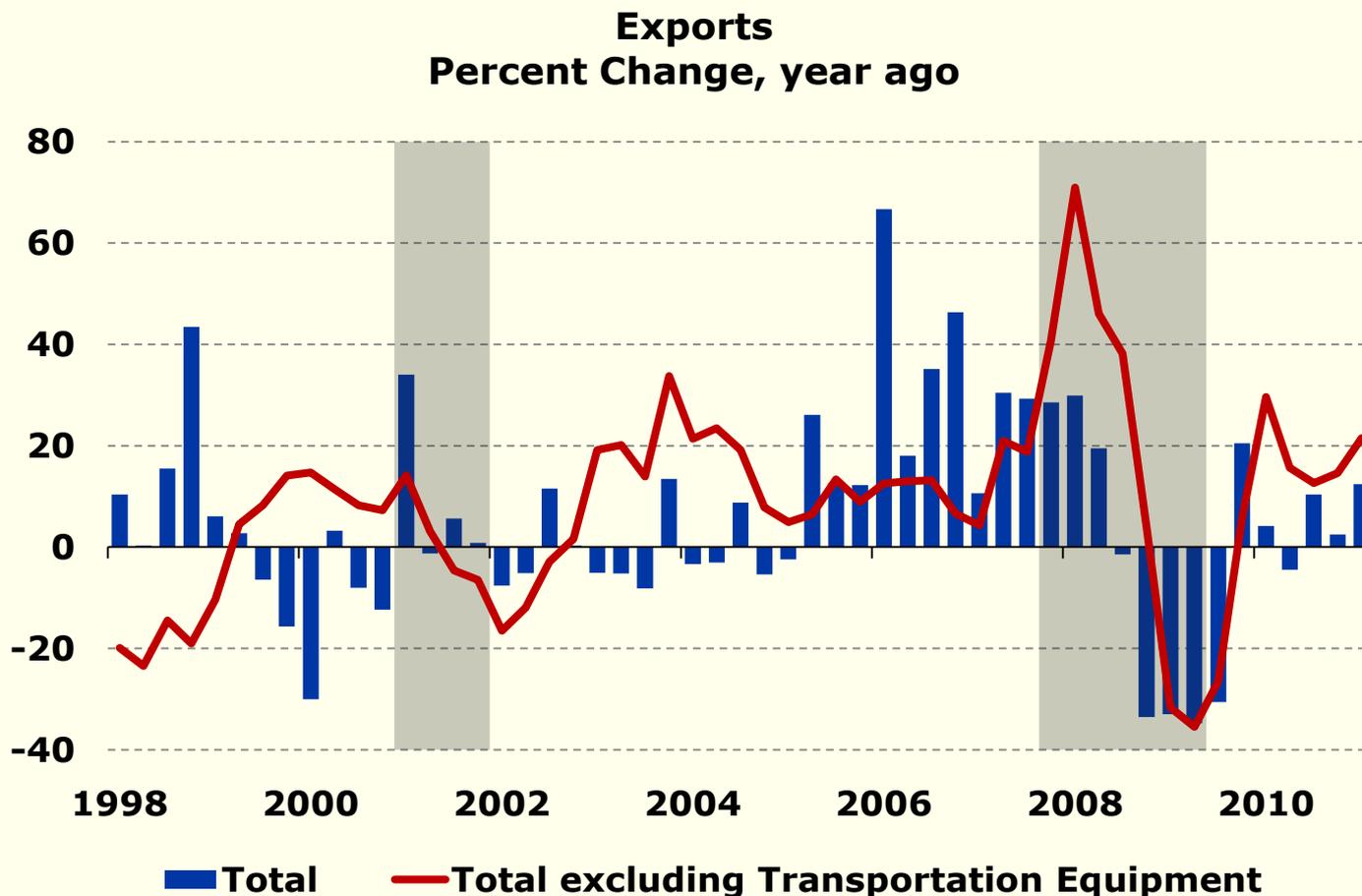
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Source: ERFC Preliminary June 2011 forecast; actual through May 2011



WA export growth is strong, and will help state outperform in the recovery

Total exports were up 12.4% y/y in Q1



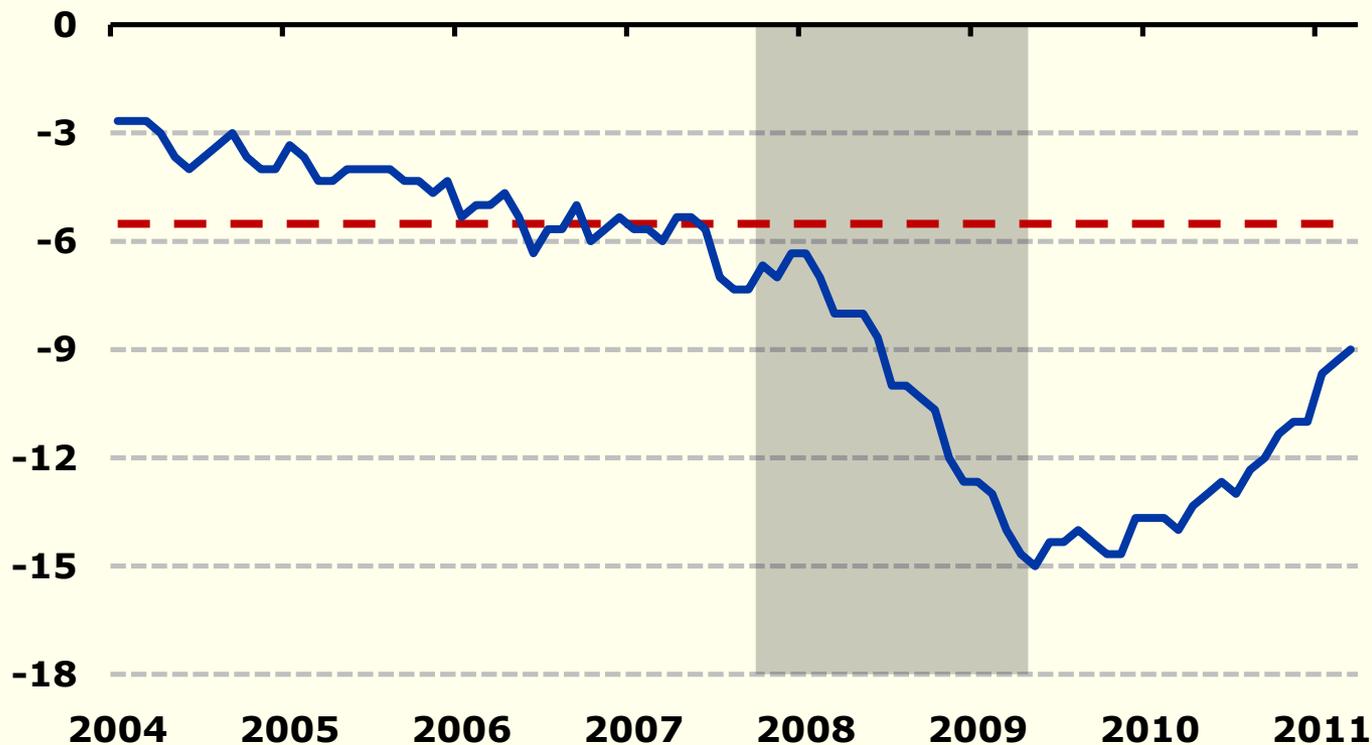
Source: Wisier Trade Data; through 2011 Q1

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Credit conditions for small business are improving, but remain tight

Availability of Loans
Net Percent ("Easier" minus "Harder"), 3mma



Source: National Federation of Independent Business; data through May 2011



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

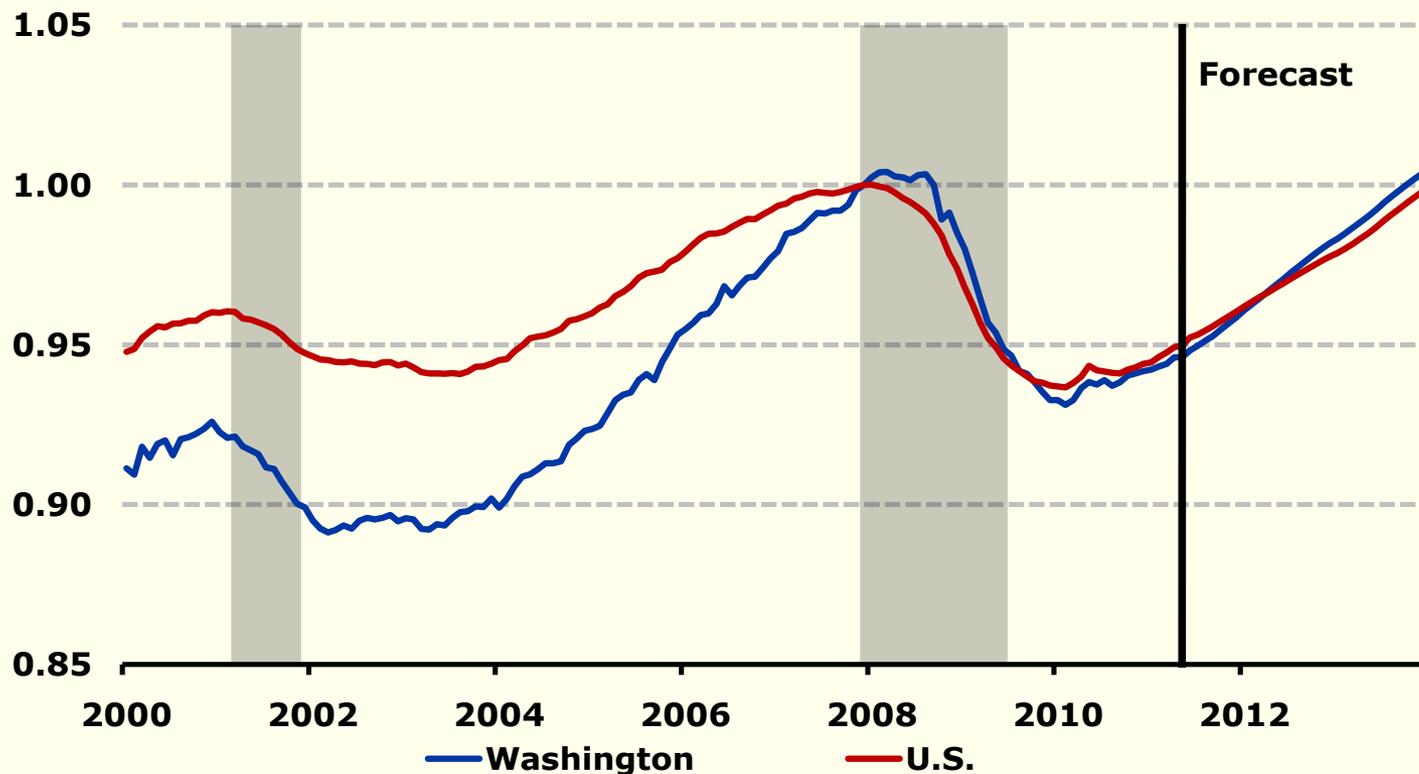
WA employment peaked 1 month after U.S. (Feb. 2008 vs. Jan. 2008)

Both WA and the U.S. reached a trough in Feb. 2010

WA is forecasted to reach its pre-recession peak in December 2013, the U.S. after 2013

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December 2007=1.0



Source: ERFC June 2011 forecast; actual through May 2011



WA personal income will recover faster than that of the U.S.

Date of regaining peak:

WA:

Nominal 10Q2

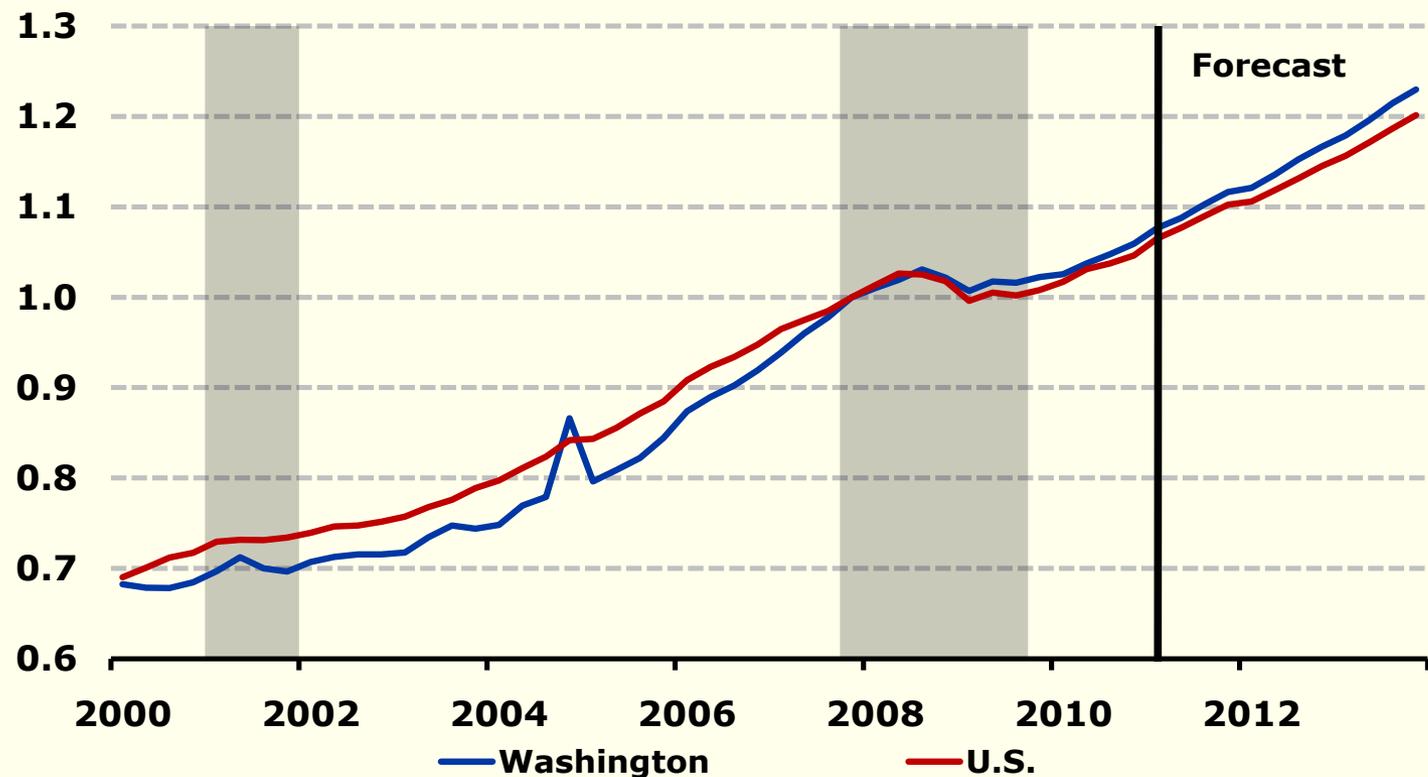
Real 10Q3

U.S.:

Nominal 10Q2

Real 11Q1

2007Q4 = 1.0



Source: ERFC June 2011 forecast; actual data through 2011Q1

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Forecast changes: General Fund State, 2009-2011 Biennium

March Forecast:

\$28,047 million

| USD millions | June 2011 Forecast | | | | |
|--------------------|------------------------------|----------------------------|------------------------|-----------------|----------------------|
| | <u>Collection Experience</u> | <u>Non-economic Change</u> | <u>Forecast Change</u> | <u>Forecast</u> | <u>Total Change*</u> |
| Dept. of Revenue | \$94 | \$147 | (\$74) | \$26,769 | \$168 |
| All other agencies | (\$1) | \$0 | \$5 | \$1,449 | \$3 |
| Total GF-S | \$93 | \$147 | (\$69) | \$28,218 | \$171 |

* Detail may not add to total due to rounding

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Forecast changes: General Fund State, 2011-2013 Biennium

| USD millions | June 2011 Forecast | | | | |
|--------------------|------------------------------------|-------------------------------------|----------------------------|-----------------|--------------------------|
| | <u>March 2011 Forecast</u> | <u>Non- economic Change</u> | <u>Forecast Change</u> | <u>Forecast</u> | <u>Total Change*</u> |
| Dept. of Revenue | \$30,340 | \$33 | (\$217) | \$31,156 | (\$184) |
| All other agencies | \$1,567 | \$7 | (\$6) | \$1,568 | \$1 |
| Total GF-S | \$31,907 | \$40 | (\$223) | \$31,724 | (\$183) |

* Detail may not add to total due to rounding



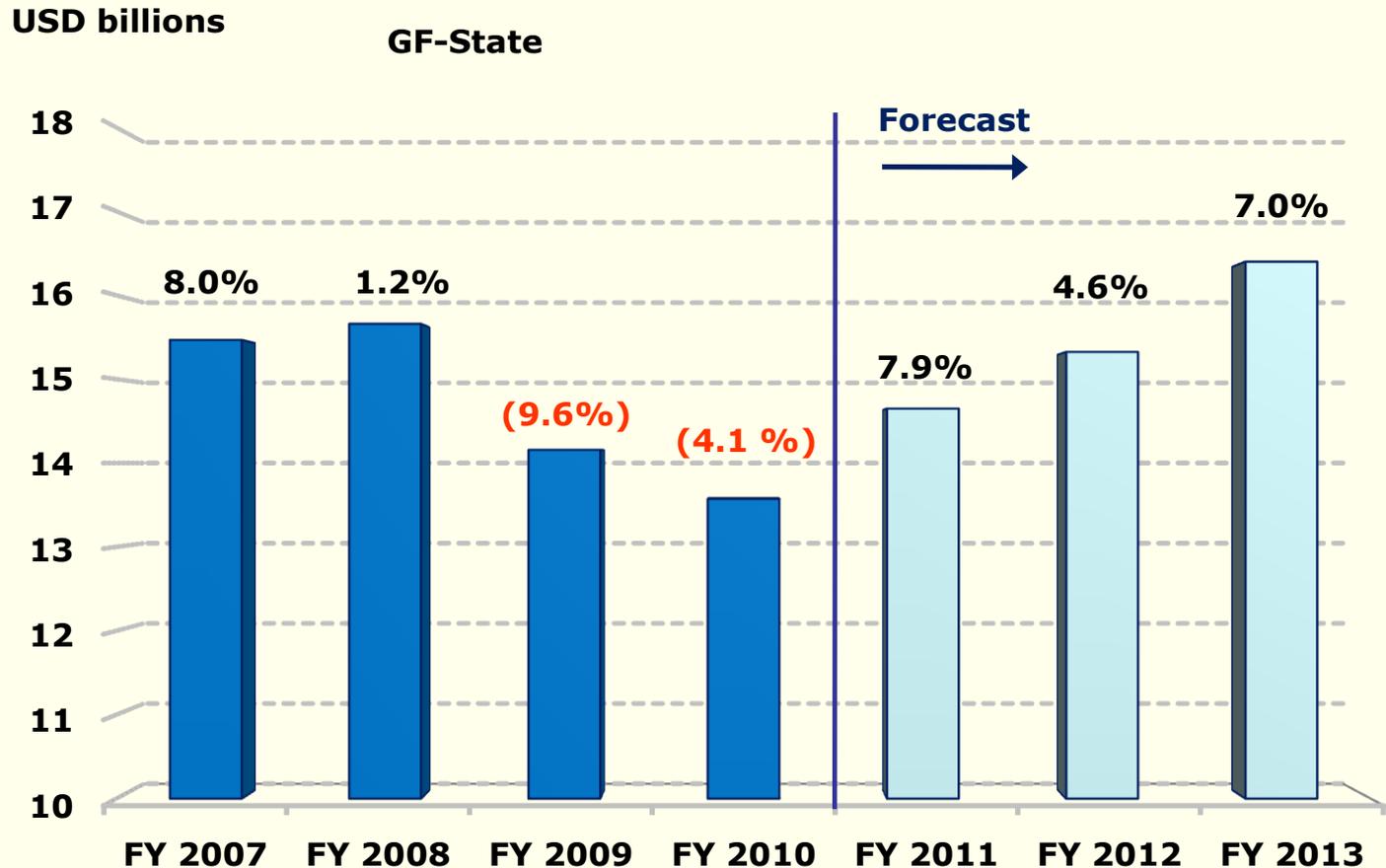
General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07-09

General Fund – new definition, for FY 10-13

YTD: 8.1%

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Source: ERFC forecast, June 2011



Conclusion

- The U.S. economy has entered another soft patch in the recovery.
- The impact of the Japanese disaster was worse than anticipated and uncertainty in oil markets has increased.
- GDP growth will have to rely on private demand going forward.
- The recovery should pick up momentum in the third and fourth quarter of the year.
- Downside risks are four times as high as upside risks.



Questions



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